

The Credit Crunch

How should organisations respond?

An article by 7 Days Limited.

From the square mile in the City of London to the far reaches of Britain's most rural villages, few could claim impunity from the "credit crunch" and its threats of impending doom!

Originating within the global financial markets, the term "credit crunch" can be defined as "a sudden reduction in the availability of loans (or "credit") or a sudden increase in the cost of obtaining a loan from the banks."¹ Indeed the IMF considers that financial institutions have suffered \$500bn in declared losses, with the potential for these losses to rise to \$1trillion.² This has directly increased both the cost and effort of borrowing, making the old adage "Cash is King" more apt than ever.

Outside of the money markets, Bloomberg reported (August 2008) a +91% rise in the price of Oil³ which goes some way to account for an adverse impact on food costs (23% rise in the last 12 months⁴), increased cost of domestic utilities (up by up to 34%⁵), and increased transport costs (27% average rise in the last 12 months⁶). Meanwhile UK house prices have fallen by 12.7% in the year to August (declining at the fastest rate since 1983⁷), and unemployment is rising with an increase of 15,000 heads over the year (to June 2008). So it's good news all round then!

This leads us to ask many questions. How did lending get so out of hand? How did "bad debt" enter the markets? How has turmoil in the financial markets been allowed to affect the price of a loaf? Where are the government's reserves for a rainy day? When will the credit-crunch end? And from a corporate perspective, how should organizations respond?

Organisations have the right to respond in many different ways to such economic challenges, but most opportunities are related to increasing profit or decreasing costs. Assuming that most are not at liberty to immediately (and substantially) increase profits beyond their annual targets, reducing costs deserves further consideration.

Cost reduction in an organisational context can be treated tactically and yes the benefits can be reaped quickly. Removing what you don't think you need equals less cost. But as with any organisational intervention that is implemented without consideration of the wider context, the benefits are likely to be short-lived, if not mitigated altogether by the subsequent ramifications. Ill-considered cost-cutting (at least in terms of heads) is often at the expense of organisational effectiveness generally and employee "engagement" specifically. Consider hypothetically an Investment Bank that cuts so many jobs at once (in response to declining market conditions), that those who remain employed are rendered ineffective either through job insecurity⁸, or as a result of the ensuing organisational chaos that makes *business as usual* impossible.

Further challenges exist at the other end of the economic cycle. When recovery is on the horizon and champagne corks are popping to a booming economy, what will be the cost of re-energising existing employees, and attracting or re-employing top talent? It is fascinating to observe that the cultural, emotional and reputational costs for businesses in such a predicament may far exceed the financial ones.⁹Tactical cost-

¹ Wikipedia definition - http://en.wikipedia.org/wiki/Credit_crunch

² BBC News - <http://news.bbc.co.uk/1/hi/business/7302341.stm>

³ BBC News <http://news.bbc.co.uk/1/hi/business/7302341.stm>

⁴ The Telegraphs 'Real Cost of Living Index' (RCLI)

⁵ The Guardian online, <http://www.guardian.co.uk/business/2008/aug/30/utilities.energy>

⁶ The Telegraphs 'Real Cost of Living Index' (RCLI)

⁷ The Times Online, <http://business.timesonline.co.uk/tol/business/economics/article4672431.ece?&EMC-Bln=IJ9519>

⁸ Maslow's Hierarchy of needs; Wikipedia: http://en.wikipedia.org/wiki/Maslow%27s_hierarchy_of_needs

reductions then, as described above, are in the long run likely to cost more than the “value” they claim to create. So how should sustainable cost-reduction be approached?

Cost reduction is unquestionably a powerful means of making any given organisation more streamlined, agile and responsive. Unlocking these benefits without compromising engagement is to approach cost reduction holistically. This should include a review of the organisations *raison d'être*, validation of the linkage between strategic intent and the operating model, and ensuring optimal (and strategically representative) organisational structures are in place. Other initiatives may include a review of processes, supplier contracts, geographic entities, technology infrastructure, attrition planning, and administrative efficiencies.

To avoid compromising engagement, guiding principles for all cost-reduction activities includes careful planning, regular and open communications, transparency, doing what you say, and moving at speed. In addition organisations must ensure that the rules of the game are clear and consistent. Examples may include, how are individuals “rewarded”? How are individuals “punished”? How is success measured? How transparent are accountabilities? How direct is the link between corporate and individual success? Does a balance scorecard exist to reinforce strategic direction and organisational values? Does the brand do what it says on the tin both for the customer and the employee?

If cost reduction is managed astutely, engagement need not take a significant hit. In some cases engagement may even increase with the prospect of newly created opportunities and a turn of organisational pace (in itself generating new energy and greater anticipation). Taking the organisational pulse at regular intervals is a helpful barometer.

This leaves the question of talent which becomes less of a question and more of an answer in itself when cost reduction is treated as part of the strategic agenda, and engagement is given the highest priority. Doing the basics well tends to remove any mystery around how to attract, develop and retain the best talent. As such it could be argued that talent management becomes less operationally onerous and more strategic in nature, or more of a pleasure and less of a chore.

To paraphrase Her Majesty the Queen in her 1999 annual speech, ‘the only certainty in change is change itself’. The question is whether your organisation is a change agent or a change victim. Safe to say those out in front are usually not victims.

For more information on our views, offerings and capabilities please get in touch at www.7days.co.uk or on 01494 671577.

⁹ The anti-dote to *Productivity through the People*, “In Search of Excellence”, Tom Peters and Robert Waterman, Harper Collins 1995.