Thriving on adversity

Some companies are finding opportunities in the recession.

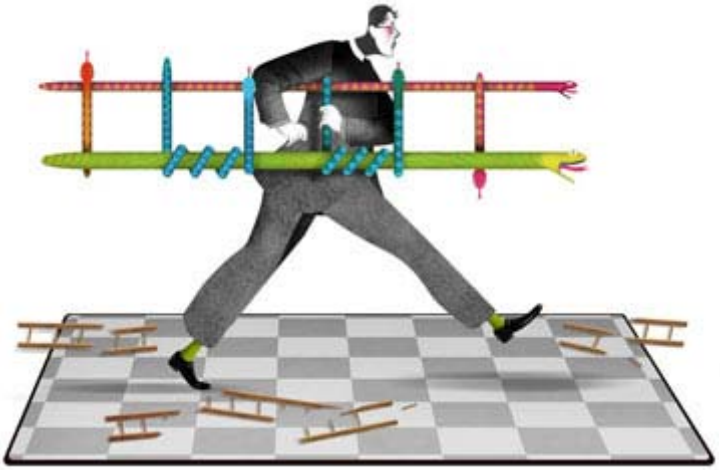

Illustration by Brett Ryder

Just after Barack Obama was elected president, his incoming chief of staff, Rahm Emanuel, told a conference of American captains of industry, “You never want a serious crisis to go to waste.” Here’s hoping his audience was paying attention, because recessions—particularly gut-wrenching slumps like this one—provide as many opportunities for business people as they do for politicians. Although they are often called “slowdowns”, recessions shake things up rather than slowing them down. They reward strengths and expose weaknesses, create new opportunities and kill old habits, release pent-up energy and destroy old business models. Distressed assets can be bought for a song, talented people hired cheaply and new ideas given an airing.

The most striking example of this was the Depression. Most people think of the 1930s as an economic desert littered with foreclosure signs and unemployment queues. But for the canny few it was a huge opportunity. DuPont invested heavily in research and development (R&D) and hired unemployed scientists. By the late 1930s 40% of its sales were from products that were less than a decade old—including world-changing inventions such as nylon and synthetic rubber. Procter & Gamble (P&G) invested so heavily in radio advertising that it created a new artistic form, the soap opera. The list of companies which took off during the Depression includes Revlon, Hewlett-Packard (now HP), Polaroid and Pepperidge Farms, the last of which was founded by a society lady whose husband was a victim of the Wall Street crash.

More recent recessions have produced a similar pattern of creative destruction. Two studies by management consultants show that they dramatically rearranged the pecking order of companies in many fields. Bain & Company discovered that twice as many firms made the leap from “laggards” to “leaders” (ie, from the bottom quartile of companies in their industry to the top quartile) during the recession of 1991-92 than during non-recessionary times. McKinsey discovered that one-third of banks and two-fifths of big American industrial companies dropped out of the first quartile of their industries in the recession of 2001-02. These shake-ups can have long-lasting consequences: more than 70% of the companies that made big strides during the previous recession in the Bain study preserved their gains during the subsequent boom, whereas fewer than 30% of the companies that lost ground were able to make it up.

What about the current recession? A great deal is still up in the air, of course. But it is possible to get some idea of the sorts of companies that are doing well and the kinds of strategies they are pursuing. The most obvious winners are established giants: market leaders that entered the recession with cash in their pockets and sound management systems under their belts. These companies are reaping rewards from investors who are skittish about shakier rivals. They are also using their corporate muscle to squeeze their costs (for example, by negotiating cheap rates for advertising) and so win market share from their competitors. BCG, another consultancy, notes that 58% of companies that were among the top three in their industry had rising profits in 2008 and only 30% saw their profits decline. In contrast, only 21% of companies outside the top three had rising profits, and 61% had falling profits.

McDonald's is simultaneously sharpening its appeal to its core customers, even introducing computer systems that allow its outlets to adjust their prices to local economic circumstances, and moving upmarket with lattes and salads. Asda, a British supermarket chain, is building 14 new stores and hiring 7,000 new workers. PepsiCo has taken direct control of two of its biggest bottling companies, at a cost of $6 billion. Many big companies are also taking advantage of bargain-basement prices to make acquisitions. That is wise: a BCG study of mergers and acquisitions in America in 1985-2001 found that deals done during a recession generated about 15% more return to shareholders than those that took place during a boom.

Spend it to make it

A second group of winners is made up of companies with a record of innovation. Despite seeing its revenues fall by 23% in the last quarter of 2008 compared with the last quarter of 2007, Intel is continuing to invest heavily in innovation. Craig Barrett, the company's former boss, insists, "You can't save your way out of a recession; you have to invest your way out." P&G is launching its biggest expansion in its 170 years, opening 19 new factories around the world and investing heavily in new ideas, despite disappointing recent results. IBM is holding a series of "innovation jams" designed to squeeze ideas out of its employees.

A third group consists of companies which are using the recession to reposition themselves. Cisco is speeding up its transformation from a backroom network plumber into a much more versatile internet giant, using its cash reserves to snap up start-ups in new fields and expand its business portfolio. Repositioning is a strategy that has paid off dramatically in the past. When the Soviet Union collapsed, plunging Finland into economic turmoil, Nokia's response was to abandon 90% of its businesses to concentrate on telecoms, particularly mobile phones.

There is also every reason to believe that the current recession will produce lots of upstarts. The Kauffman Foundation, which studies entrepreneurship, points out that about half of Fortune 500 and Inc. 500 companies (lists of the biggest and fastest-growing firms in America, respectively), including such household names as FedEx, CNN and Microsoft, were founded during recessions or bear markets. A disproportionate number of these upstarts produced industry-changing ideas that established companies failed to appreciate until it was too late. Indeed, business is more likely to take advantage of this "serious crisis" than the world's politicians.

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