Is it time to recession-proof your business?

Recently, the Bank of England raised interest rates to 1.75%, the biggest interest rate rise in almost thirty years and its sixth consecutive increase. It's clear that we are in the midst of the most uncertain macroeconomic environment for some time.

Temps de lecture : minute

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After a period where hiring was exceptionally difficult, we've already seen some heavy staffing cuts at startup media darlings like *Gorillas* and *Klarna*.

But here's the thing. Despite all the chatter, we're likely not in a recession yet. While higher interest rates in the US and UK, combined with higher inflation (especially for energy), are understandably concerning, job markets remain pretty firm and consumer savings are in decent shape post-Covid.

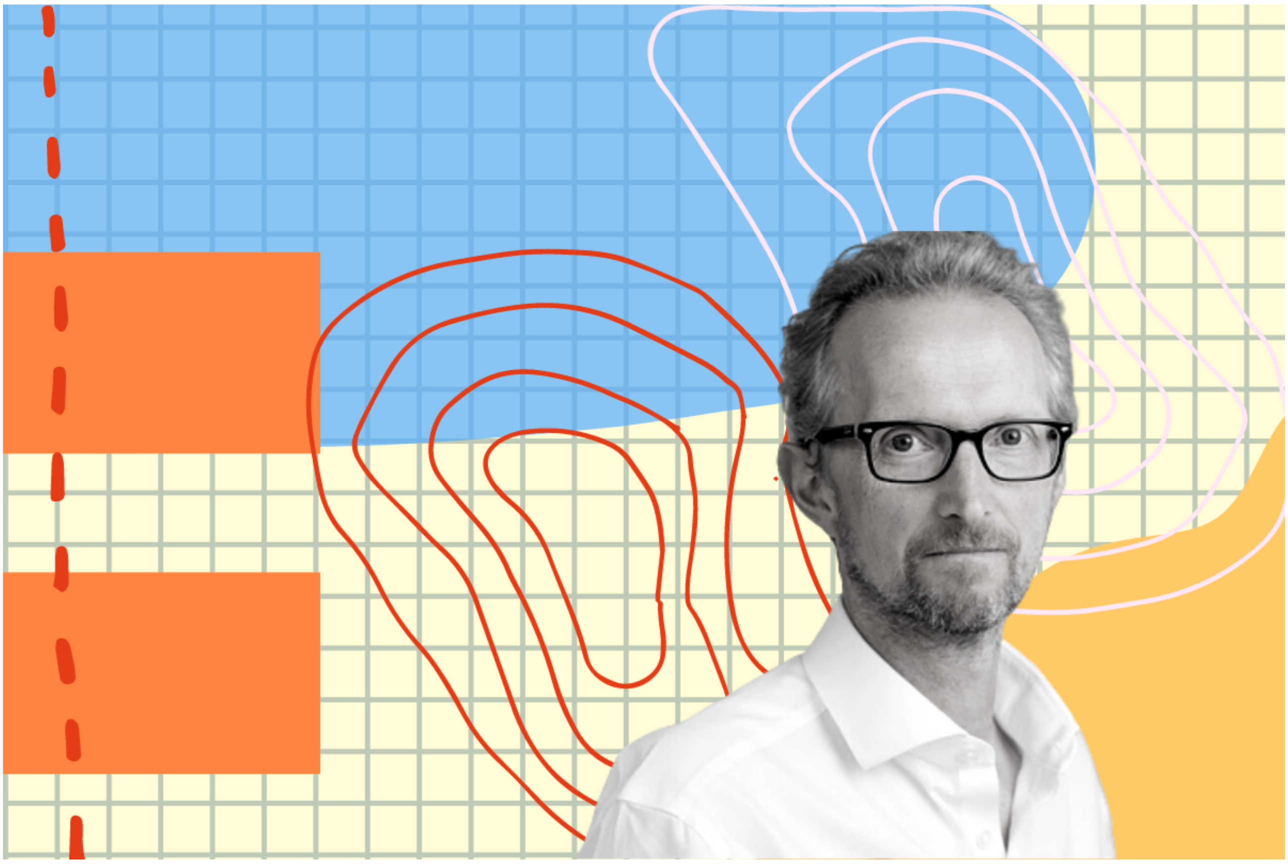
That's not to say things are at all rosy, but the economic situation isn't quite as bad as past crises yet - and we're certainly not heading into another 2008. Companies still have time to plan and prepare for whatever comes next.

What businesses need to know: the context today

Compared with the previous financial crisis, most economists don't expect the damage to run as deep and the wider economic impact shouldn't be as severe.

Despite this, one thing has certainly worsened for venture-backed start-ups. When cash was cheap, we witnessed bumper valuations for both listed and unquoted tech companies. Today, with listed tech stocks down heavily, valuations for unquoted growth companies are coming under more scrutiny. The funding environment is becoming more strained and, while there is still plenty of venture capital cash on the sidelines, founders may want to think about extending the runway sooner rather than later, just in case we do see further economic pressure ahead.

Inflation and the associated energy crisis are squeezing consumers' disposable income which will put pressure on businesses across all industries. We are already seeing how these pressures have affected the value of tech giants like Netflix and Shopify and we will start to see how this impacts early-stage startups soon. However, it’s not time to panic just yet.



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Decide what kind of business you are

Businesses that survive, or even thrive, in a recessionary environment are likely to be what we call painkiller businesses. Painkiller businesses offer a service that is seen as essential by their customers. On the other hand, a lot of businesses can be described as vitamin business, which offers a service that’s ‘nice-to-have’, but not critical to the market.

When it comes to cutting costs, vitamin businesses are often first on the chopping board. While you can’t become a painkiller business overnight, you can make changes to make your company feel more essential to a customer. Ensuring your customer knows the value of the service you provide, improving customer service and considering making customer loyalty rewards more attractive can go a long way. Remaining adaptable is critical for small businesses. Downturns and economic crises can destroy businesses, but for some founders that have embedded a culture of agility across the business, this can be a highly valuable survival mechanism.

For example, companies that adapted quickly to the pandemic were able to thrive, such as Spotify. Pre-pandemic, Spotify disproportionately relied on advertisers to fund its free version of the service. As advertisers cut their budgets, Spotify had to pivot to stay in the game. Instead, they offered original podcast content and signed exclusive deals with celebrities - and saw artists and users upload more than 150,000 podcasts in just one month.

Making the tough decisions

The harsh reality for many founders is that the next few months will involve tough decisions. Look at your cost structure and prepare a plan B for cost-cutting, so that it's ready to go if you need to take action. This could include reviewing staff on payroll, hard negotiations with suppliers, and price markups on products or services.

Of course, cost-cutting is all about balance. You don't want to end up in a situation where you're cutting off your nose to spite your face - you must still show investors that the company is growing.

The key for most businesses here is to focus on retaining the costs that drive revenue: is a cost delivering you revenue growth? If not, you've got to question it. If we move into a recession, then the company's ability to generate revenue will be key to survival and future fundraising.

The Government played a crucial role in supporting businesses during the Covid pandemic, however, this support is unlikely to be made available again. As a founder, you need to decide whether or not you've got a cash runway for the next four to five months. If not, you should consider leaning on investors to raise more now.

When life gives you lemons…

Although the market forecasts are far from overwhelmingly positive today, it remains true that great businesses turn crises into opportunities. Sit down with your inner circle and draw up plans for potential scenarios, so that the business can move quickly when it needs to.

By winning market share from other struggling firms, or refocusing and pivoting into a new market, there are golden nuggets out there waiting to be seized.

We don’t know what the next few months will hold, but there will be winners on the other side of it – the key is to put yourself in the best position possible now so that you can be one of them.

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