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# Surviving AND Thriving IN A DOWNTURN

**W**hat is the one thing that a good economy and a bad economy have in common? They don't last!

Signs may be emerging that the worst economic downturn since the Great Depression could be waning, with July's unemployment rate making its first drop in over a year and the rate of U.S. job losses slowly starting to ebb. Even with these stabilizing indicators, staffing firms are not out of hot water yet.

The staffing industry has been hit hard by the recession with recent statistics showing a 25%-35% drop in unadjusted temp jobs depending on the sector and an estimated industry-wide revenue loss of between \$25-\$35 billion in 2009 – not to mention the nearly 50% drop in direct hires. While the implementation of hiring freezes by nervous business owners may be an easy target to explain these dismal staffing numbers, the cause runs much deeper.

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Staffing firms react to these clients by lowering markups and downsizing their own staff.



The ailing economy was exacerbated and underscored by a multitude of factors, the likes of which this country has never seen: the bankruptcy of Lehman Brothers, the largest bankruptcy filing in U.S. history; the failure of Washington Mutual, the largest bank failure in U.S. history; the conviction of Bernie Madoff, mastermind of the largest Ponzi scheme in U.S. history; and the list goes on and on.

As unique and insidious as this economic downturn has been, it still followed a mostly familiar pattern as it relates to the staffing industry:

### **The Cycle and Segment Trends**

Initially the blue collar sectors see declines followed by professional positions and then direct hires. The difference this time is that the decline was twice that of the previous worst downturn.

### **Direct Hire**

Direct hire revenue drops faster than contract revenue by a ratio of 2:1.

### **Healthcare**

This segment usually flatlines. However, this time staffing in the nursing/allied sector saw its largest segment decline ever, dropping by more than 20%, and still falling. This has never happened before.

### **Gross Margins and Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) Erode**

This occurs due to the change and decline in the revenue mix (temp and direct hire), increases in workers compensation and unemployment insurance, and marketplace pricing pressure.

### **Price Compression**

Price compression always occurs in a recession, and this time was no different. What was different was that the drop came much quicker and, in some sectors, it appears to be more severe. Some public firms have reported 20% or greater reductions in gross margin percentages this year.

### **Downward Spiral**

Once the perfect economic storm begins its downward spiral, clients react to the market by laying off temporary workers and asking for pricing concessions in their remaining contracts. Staffing firms react to these clients by lowering markups and downsizing their own staff.

For the most part, this recession has remained true to this standard cycle. The one difference is that this time it occurred with such great velocity and depth. Being aware of the cycle allows staffing executives the ability to plan for these changes and even strategically take advantage of them,

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Scour the books, crunch the numbers and give your accounting department a good hard look.



thus weathering the ups and downs more efficiently.

There are five key questions every staffing business owner, CEO, CFO and division manager need to ask themselves when determining a game plan for recession survival and, as importantly, the upturn that may be just around the corner.

### **How Long Will It Last?**

Historically speaking, those in the staffing industry often find that their measure of prosperity is cyclical, with revenue booms lasting six or seven years, punctuated by two or three years of lowered returns. Global recessions obviously will skew these numbers. Though no one has a crystal ball, keeping oneself informed on emerging labor trends and economic indicators is vital. The GPalmer forecast is projecting an upward turn in year-over-year industry revenue in the second quarter of 2010. Keep in mind that forecasts are merely educated speculation, so a good dose of caution is warranted. However, if in the fourth quarter the industry sees single-digit or low double-digit year-over-year revenue decline comparisons, it is likely the upturn is very near. The first sign will be a positive year-over-year GDP reported by the federal government.

### **Do I Cut My Rates or Not?**

The knee-jerk reaction for many companies trying to thrive in a competitive market is to lower their pricing to attract more customers and set themselves apart from the competition based on price.

While cutting rates may indeed be a good option to increase sales, it is important to consider the long-term repercussions in relation to the perceived quality of goods and services. It is rarely the recipe for future profits. My personal recommendation is to concentrate on the wage side of the bill rate equation when possible, build some success fees into goal achievement with your clients, consider lowering temp benefits and, when all else fails, make those gut-wrenching decisions in order to keep existing business or take on new lower margin new business. That being said, lowering rates should not be your first choice.

### **Do I Have Enough Capital?**

The old adage is that when you run out of cash you run out of options. Scour the books, crunch the numbers and give your accounting department a good hard look. Determining the longevity of your current capital is key to establishing your plan of action. I know of both small and large companies that are currently struggling with cash flow issues. I would suggest that they pay particular attention to Days Sales Outstanding (DSOs). Cut deals with clients to encourage quick payments, but if a client is pushing 60-plus days, get tough quick. Industrial staffing firms have the additional issue of collateral for workers comp claims, and lenders are being tougher on letters of credit, which further compounds the cash issue. There are resources available through the American Staffing Association or

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In this market you cannot be over-networked or over-informed.

your insurance broker that may help you determine creative insurance programs to help loosen your capital.

### **Have I Lowered My Costs Enough?**

With a decreased influx of margin dollars, it is important to be discerning and creative in cost-cutting strategies. Your vendors are just as eager as you are to maintain and build their client base, so if you find your payables are simply too high to weather the lost revenue, renegotiate the terms of service and related costs. Many firms have renegotiated leases, job board fees, benefits (internal and external) and many other high dollar items. It is surprising what is negotiable in today's markets. There are even vendors available that will work on a contingency basis, charging a percentage of the money they are saving your company.

### **Do I Have the Right Strategy for Today and Tomorrow?**

While surviving the economic downturn is obviously at the top of every executive's to-do list, simultaneously having a cohesive plan for future success is equally as important. Segueing from "survival mode" to "endurance mode" takes some serious planning, and having a comprehensive, long-term strategy in place now will help determine tomorrow's success. Surround yourself with a strong advisory board, consider joining business groups like Vistage and YPO (there are many others) and attend industry

functions such as the ASA Conventions and Staffing Industry Analysts' Executive Forums. In this market you cannot be over-networked or over-informed.

After asking and then carefully answering these questions you will be better equipped to lay the initial foundation for progress. Below are three strategies to help your business survive today and thrive tomorrow. These concepts were developed by three of my clients after meticulously debating the above questions. It is important to note that these strategies are designed to focus on the most immediate ways to achieve the highest EBITDA and position one's company for the eventual uptick. Raising your EBITDA will better allow your business to generate and preserve cash, while laying a foundation from which to build upon.

### **Lower/Flexible Costs = High EBITDA**

Lower your fixed costs and/or make them more elastic. Begin by renegotiating all vendor contracts, review temp benefits (many firms are adjusting to today's favorable recruiting environment) and offer your sales team a significantly higher percentage of gross margin on their book of business in exchange for lower base salaries. I have seen several examples of successfully negotiating and implanting entire new models that allow for many fixed costs to become variable. Also, strongly consider the excellent options available today to outsource departments such as risk management, back office and

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recruiting and sales lead generations. Finally, after you think you have lowered all your costs as far as you can, take one more aggressive pass at it.

### **Incremental Revenues = Higher EBITDA**

Taking on additional business at decreased margins and considering acquisitions is not for the faint of heart, but the idea is straightforward. If you leverage your fixed overhead with incremental lower-margin revenue you can often add enough margin to cover your costs and then some. The trick is to take on clean business, with good credit and a low-risk profile that will not incrementally add to your costs. I am not advocating frantically lowering margins across the board, but by engineering incremental business without taking on additional costs (i.e., more staff), your company may have the opportunity to add important incremental dollars to the bottom line.

### **High Margin/High Risk = High EBITDA**

By now, some of you are likely saying: "I'm tired of all the cost cutting and low margins. Tell me something new." Bold staffing firms are emerging alongside their traditional counterparts and creating solutions that incur more risk but if executed well, reap a large return. Light industrial staffing, traditionally considered one of the lowest gross margins areas, is enacting "per piece pricing." This sector's gross margins have historically ranged from high single-digits to the mid-teens, but there is a movement to change the existing model. Instead of charging clients by a bill rate or markup, some clever firms are charging by the piece. For example, when a staffing firm takes over an area from a client (such as a section of a warehouse or manufacturing facility) and enacts the "per piece pricing" model, it might ditch the markups, hire an engineer to help create the onsite process flow and charge a fixed sum for the work. The goal is to provide the client a turnkey solution.

The benefits are many: the work gets done with fewer workers, client costs are often reduced by 20% and expenditures are fixed. The assigned workers earn 20%-40% more, due to strong performance incentives, and the staffing firm significantly increases its gross margin, often by 15% to 20%. Most "per piece" contracts will range from a 30% to 40% gross margin. Keep in mind that it is mandatory to work the numbers hard going into a "per piece pricing" contract, as a miscalculation of your estimate can ultimately cause your firm to lose a considerable amount of money. If you don't have the in-house ability in this area you can easily search out several reputable firms (NGroup and others) that can coach you through the process.

If you are still a member of the "I-think-I-will-just-ride-this-one-out-and-not-turn-my-company-upside-down" camp, here are a few final straightforward thoughts that can help:

### **Credit and Collection**

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# Surviving AND Thriving IN A DOWNTURN

Survival goes to the swiftest, and to thrive tomorrow you must survive today.



## **The “Three Taps and You’re Out” Sales Approach**

If you are not making headway with a prospect, knock on the next door. Time is of the essence, and you need to go where the opportunities are. You can circle back around to the hard-to-crack accounts when times improve. Some might disagree, but I have seen too many firsthand examples of firms wasting valuable time in this market by continuing to call on businesses that simply are not going to sign on any time soon.

## **Bring Value and Bring It Immediately**

In today’s market, custom solutions can take too long to implement and sell. You need to go directly to a potential client, armed with a proven solution of which you have a track record of delivering.

## **Draw Down Your Credit Line for Rainy Day**

Interest rates are at an all-time low. This is the time to borrow, and these times won’t last forever.

## **Bring On New Talent**

Even if you can’t afford it I would encourage you to be creative with a 100% variable comp plan for sales talent. I have one client who recently brought on a new sales rep that he could not afford. She paid 100% commission, and in 60 days the new rep brought in \$8,000 of margin in a single month. With a 50% payout, \$4,000 in margin

magically appeared, with no hard dollars investment by the staffing firm. For those with a stronger balance sheet, you will never find a better time to add to talent than today. People’s incentive has been cut; there is obvious frustration in the market. To me, this is a recipe for opportunity.

The bottom line is simple. Survival goes to the swiftest, and to thrive tomorrow you must survive today. Staffing companies need to actively seek new business by swiftly adjusting their sales approach, business models, marketing plans and services offered. In an arena filled with recession-induced industry innovation, businesses simply cannot afford to wait it out while relying on yesterday’s strategies. Those who innovate, motivate and accelerate will be the winners once this economy starts to see an uptick. The promise of better days ahead doesn’t necessarily make it any easier when you find your staffing firm in an immediate make-or-break situation. And while these different times require different approaches to see your company through to the other side, knowing that neither the good nor bad times ever last underscores both the timeliness and timelessness of taking action today. ■

**Greg Palmer** is the former CEO of Remedy Temp Inc and founder of GPalmer and Associates, a management consulting firm focused on the staffing industry. You can find the recently published GPalmer temp labor forecasts and related material on the GPalmer Website, [www.GPalmerandassociates.com](http://www.GPalmerandassociates.com).