What should I be considering for my company with a recession likely approaching?

By Susan Koss

Although a hotly debated area for economists, many are predicting a recession in the next 6 to 12 months given negative indicators such as the inverted yield curve[1] and a slow-down in manufacturing. With a potential recession looming, many business owners may be wondering what they should be doing to prepare for it. How can they get ahead of the curve and avoid being forced to react hastily in a crisis? Unfortunately, a sound recession business strategy isn't something one can "pull out of a hat" as soon as the economy turns. It is a comprehensive plan that includes a proactive and strategic response to the economic downturn.

According to *Harvard Business Review,* a study was conducted on U.S. public companies with greater than $50 million in annual sales during the last four economic downturns.[2] The study determined that the companies that weathered the downturns successfully tended to respond differently than unsuccessful companies in a few key areas. First, the most successful companies acted early on with the threat of an economic downturn before actual evidence of one happening. (Companies should already be in the process of preparing their recession strategy given the ongoing recession threat[3] we have been experiencing for at least the past year.) The successful companies focused on building more flexibility into their investment-planning and operations in addition to pursuing continued earnings expansion. By the time the recession was in full swing, the successful companies had reduced debt as compared to the unsuccessful companies that added more debt during this time.

The second key area is that most successful companies did not only focus on short-term issues to weather the impending economic rollercoaster, they maintained a long-term strategic perspective. Although many companies pursued operational efficiencies and improving profit margins, the most successful companies also focused on revenue growth. Prior to and during a recession, it is critical to understand that loyal customers are the primary, stable source of cash flow and organic growth. Although it is prudent to contain costs, failing to support brands or examine core customers' changing needs can threaten performance over the long-term. Companies that put customer needs under the microscope and tactically adjust strategies and product offerings are more likely than others to flourish both during and after a recession.

Another area of importance, that is often overlooked, is to review and amend the practices for ongoing management of order fulfillment, new product launches, and product discontinuation. A well designed and properly implemented product management policy will maximize margins on new products. In addition, through the use of technology, implementation of new strategies to tightly integrate the company with its customers on one end and its suppliers and/or operations on the other end can provide tremendous efficiencies. Improvements in technology, if designed and implemented properly, can also reduce risk cycle time from order to delivery, inventory levels, and costs associated with administration. Learning to understand the implications of changes in technology and how to adapt and utilize new technology can be key to attaining a competitive edge.

Management should also review the supplier base including, but not limited to, the number of suppliers, locations, terms/pricing, minimum order quantities, lead times, and level of defects. It is important to re-examine the methods and key performance indicators that are used to manage key external suppliers to mitigate supply chain risk. This type of analysis can result in more reliable, timely, and cost-effective raw material and finished product sourcing.

A critical indicator for a business' strength is its ability to perform during recessionary times. Downturns can shine a spotlight on the long-term health of a business, revealing vulnerabilities that might not have been as visible in good times. Successful companies have proven the importance of a proactive and strategic business plan to prevent vulnerabilities which can be the key to thriving rather than just surviving the next economic downturn. Many companies do not take the time to make this objective self-assessment leading to an outside stimulus to provide change when options are fewer.

***Susan Koss** CPA/ABV/CFF, CVA, Partner and Managing Director, leads the firm's Litigation Support Practice Group. She specializes in litigation support, business valuation, quality of earnings and forensic accounting.*

---

1 The inverted yield curve is measured when longer-term government bond interest rates fall below short-term interest rates.

2 Kevin Laczkowski and Mihir Mysore, "What Companies Should Do To Prepare For A Recession," *Harvard Business Review,* May 9, 2019.

3 The yield curve has been inverted since March 2019.

Michigan Dairy Angst

By Stephen Weber

We're number one! In case you didn't know, our cows are the most productive in the U.S. Based on the latest report from the USDA National Agricultural Statistics Service ("NASS"), the average daily production rate for Michigan cows was 71.1 pounds per cow. The national average is 63.8. Based on our high production rate, Michigan dairy farmers should be happy, right? Unfortunately, that is not the case.

Causes of Dairy Angst

Michigan dairy farmers have faced depressing operating results for some time now. It is becoming so critical that the Michigan Agri-Business Association (MABA) had a session at their 2020 Winter Conference on recognizing the dangerous signs of depression in farmers, including dairy farmers.

The largest source of angst for Michigan dairy farmers is low prices for their milk. As you can see from the graph, over the last 4 years, Michigan dairy farmers have been receiving lower-than-average prices for their milk.

Recently, prices have experienced an uptick to slightly above the long-term real (inflation-adjusted average) milk prices. This is good news for farmers.

There are many causes for the low prices. First, consumers are switching from drinking cow's milk to alternatives such as soy and almond milk. They perceive health benefits from this change. Pain from this choice is being felt by dairy farmers across the U.S. as well as noted in the recent bankruptcy filings of Dean Foods and Borden.

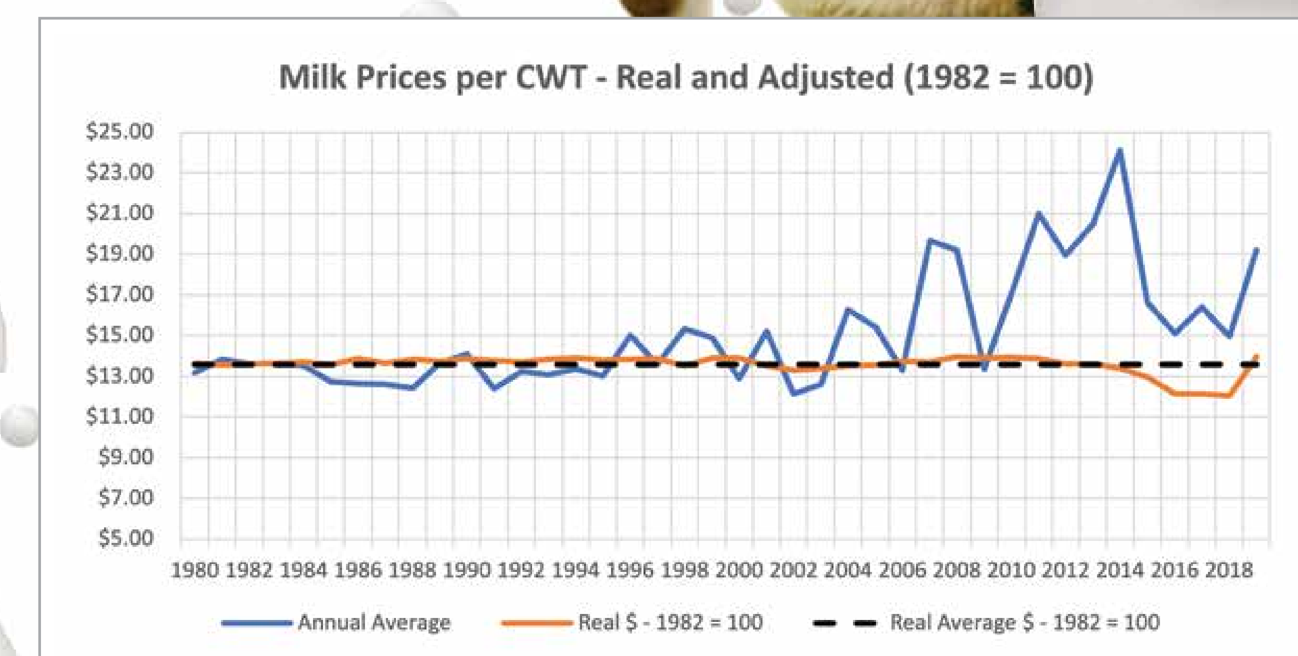
Secondly, the U.S. has been involved with trade disruption with its most significant foreign export customers: Mexico, Canada, and China. In prior years, the U.S. exported 15% of its total dairy production to foreign countries. Prior to the disruption, the U.S. supplied 75% of Mexico's cheese. Following the end of NAFTA and the implementation of other tariffs, Mexico began to import cheese from the EU. Additionally, without NAFTA in place, Canada was able to export skim-milk powder to Mexico at very favorable prices which undercut U.S. prices. Now that the USMCA is in place, we can hope that trade practices revert back to the "old normal" and Mexico returns to purchasing more economical U.S. cheese and dry skim milk.

Third, Michigan has suffered from a lack of milk processing capacity for some time. Due to our high production, a significant portion of our milk was being "exported" to other states for processing. The cost of shipping this milk out-of-state drove down the per hundredweight (CWT) price of milk from Michigan to the lowest level in the Midwest. In 2020, two new processing facilities will go online: a cheese factory in St. Johns and a milk processing facility in Greenville. This added processing capacity will significantly reduce the shipping costs and mean added revenue to Michigan dairy farmers.

Fourth, in 2019, we had horrible farming weather in Michigan. While grain prices have not increased significantly, for many farmers who plant grain, alfalfa hay, and corn silage to feed their herds, the late/small harvest has meant a significant increase in input costs. While there are supplements available for purchase to offset these nutritional losses, for farmers who lost money planting grain or hay which was not harvested, they now must shoulder the additional burden of supplement purchases to augment their herd's diet or face declining milk yields in a low-priced environment.

For 2020, we can hope that raw milk prices maintain or exceed historical real averages and return local dairy farms to positive cash flow and secure operations. However, until that happens, expect to see continued exists from the dairy market by smaller and marginal producers. The revised chapter 12 and small business bankruptcy regulations mentioned in another article in this issue may come into play for those operators.

***Stephen Weber** CPA/CFF, CTA, Director, works with clients in the fields of turnaround management and business refinancing, litigation support, forensic and fraud evaluations, as well as performance improvement.*



Source: USDA NASS data