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Management Accountants

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# The impact of economic recession on business strategy planning in UK companies

Research executive summary series

Volume 6 | Issue 9

## Key findings:

The key findings from this research were:

- There is very little optimism about the prospects for the UK economy in the short to medium-term.
- There is quite a degree of optimism from companies about their own commercial future based on a combination of factors such as: accessing overseas markets, improving the way they do things, better customer relations, product innovation etc.
- Businesses recognise the importance of having a robust business strategy to guide them through a recessionary period. However, what was done in response to the recession largely conforms to the emergent theory of strategy formulation discussed within.
- Although there have clearly been in-depth discussions and analysis about how existing business strategies might change, the changes made were largely amendments to existing strategies, with changes of emphasis, focus, timing etc.
- Most companies seem to be applying many aspects of a retrenchment approach to business strategy (e.g. reduced fixed costs, narrower product offerings, reduced staffing) but there are also some aspects of an investment approach which can be observed. However, the potential for these investment approaches is conditioned by concerns about getting access to capital finance.
- Both in terms of liquidity support and access to capital finance, there are concerns about the attitude of UK banks in relation to small to medium businesses.
- Companies have identified several managerial areas where they felt the robustness and quality of the approaches being applied had been allowed to decline in recent years. As a consequence of the challenges of a recession, urgent improvements have had to be or need to be made.

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## Overview

The UK economy recently emerged from a long period of economic recession. National statistics and surveys provide generalised findings of the current state of business during and after recession but fail to offer insights into how UK based businesses made (or failed to make) strategic responses, during the period of recession and subsequently. Against such a backdrop, this project is concerned with the strategic responses made by a small but varied sample of businesses in response to stringent economic conditions resulting from economic recession.

The specific aims of the project were to:

- obtain a perspective of how businesses of various types saw the recession in terms of length and depth
- understand the impact of recession on the businesses and the actions they took in the short/medium term to deal with the challenges of recession
- obtain a view as to how businesses might plan to change their business strategies to deal with the impacts of the recession
- consider any management and financial management implications which ensued.

The researchers would like to thank CIMA for funding this project.

A fuller version of the project report including relevant references and sources can be obtained from Professor Malcolm Prowle at [Malcolm.prowle@ntu.ac.uk](mailto:Malcolm.prowle@ntu.ac.uk)

## Contextual factors

This section briefly discusses some key factors, drawn from published literature relevant to any consideration of business strategy in the current economic climate. For more detail on these issues the reader is referred to the full version of the report mentioned above.

### The nature of economic recession

Having formally come out of recession the future prospects for the UK economy seem still somewhat gloomy with a considerable degree of pessimism about the longer term. However this latest recession is often regarded as being different from previous recessions because of the impact of three factors:

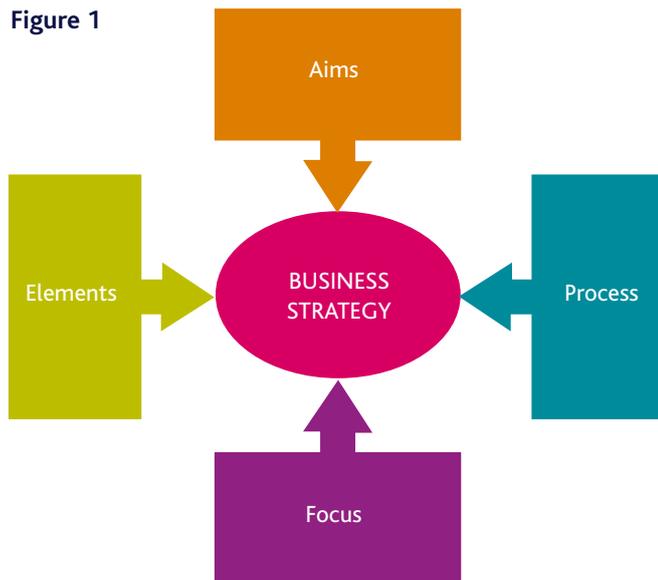
- Credit Crunch - banks have had serious liquidity problems and became very risk averse about lending to business and individuals as well as to other banks.
- Globalisation of the world economies - the globalisation of business and finance has caused huge inter-dependencies between economies. Thus a recession in one country will potentially have large scale impacts on other countries to an extent not seen in previous recession.
- Impact of UK public finances – the problems of the UK's public finance deficit creates major concerns for businesses:
  - Increasing levels of corporate taxation would have negative impacts for businesses.
  - Increasing levels of individual taxation could reduce consumer demand for goods and services.
  - Public sector procurement will decline with implications for businesses who have significant public sector customers.
  - High levels of public sector redundancy could inhibit consumer confidence.

Moreover, although there are short and medium term impacts of recession on businesses there may also be longer-term impacts which are difficult to discern. Some examples might include: greater risk aversion, a shift from consumption to savings and a greater focus on value for money from spending. Again the reader is referred to the full report.

## Business strategy

Most business organisations of any size will probably have some form of business strategy (even if it is not articulated in such terms). However the term 'business strategy' is sometimes a nebulous term and there are many different definitions and aspects of business strategy. Some of these are shown in figure 1 and subsequently discussed briefly. All of these themes were considered during the course of the research.

Figure 1



### Aims of business strategy

In broad terms a business strategy should aim to define:

- The external, environmental factors affecting the businesses' ability to compete.
- The position the business is trying to get to in the long-term.
- The markets a business should compete in and the activities are involved in such markets.
- The values and expectations of those who have power in and around the business.
- The resources required in order to be able to compete.
- The means by which the business can perform better than the competition in those markets.

### The process of strategy development

There is strong debate about exactly how business strategies are or should be developed and these are shown in figure 2 overleaf.

Proponents of **deliberate strategy** take the view that strategy formation is a process based on acting intentionally. It is important to plan and think before acting. The strategy must be clear, explicit and must be executed by the company. Proponents of **emergent strategy** hold that strategy originates from the interaction of the organisation with its environment and that it is an ongoing process of constant learning, experimentation and risk taking. The probability is that these two views represent two ends of a continuum. Real-world strategies probably lie somewhere along this continuum, contingent on a range of factors such as: environment, culture, location etc.

Also a business strategy must be thought of as being more than just the preparation of a strategic plan but a process which comprises three elements:

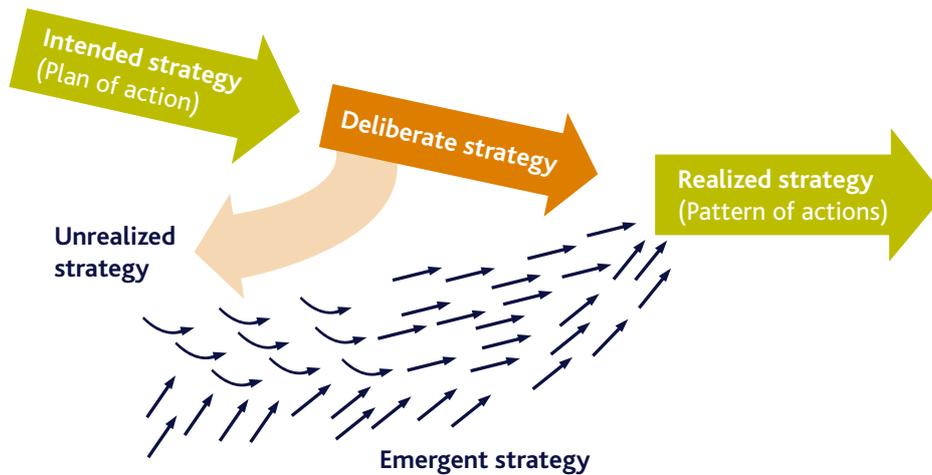
- **Plan** - the conduct of an appropriate exercise culminating in the production of a strategic plan which is feasible, sustainable and acceptable. However, the means of preparing the plan is as important as the actual plan itself and should involve consultation with stakeholders in order to facilitate acceptability of its content.
- **Implementation** - the successful implementation of that plan which may require a substantial focus on change management because of the high degree of organisational change which may be involved.
- **Evaluation** - an evaluation of the extent to which the strategy has been successful in achieving its objectives.

### Focus of business strategy

There are two mainstream schools of strategy which have different foci:

- **The positioning school** views the firm as concerned with achieving 'strategic fit' with its environment; that is with evaluating the competitive forces operating within the environment to assess where and how best to compete. Hence this approach to business strategy implies a primary focus on looking outside the business at the external political, social, economic and technological environment and identifying changes and trends in that environment. The task is then to shape and fit the organisation to respond to market opportunities arising from the changing environment.

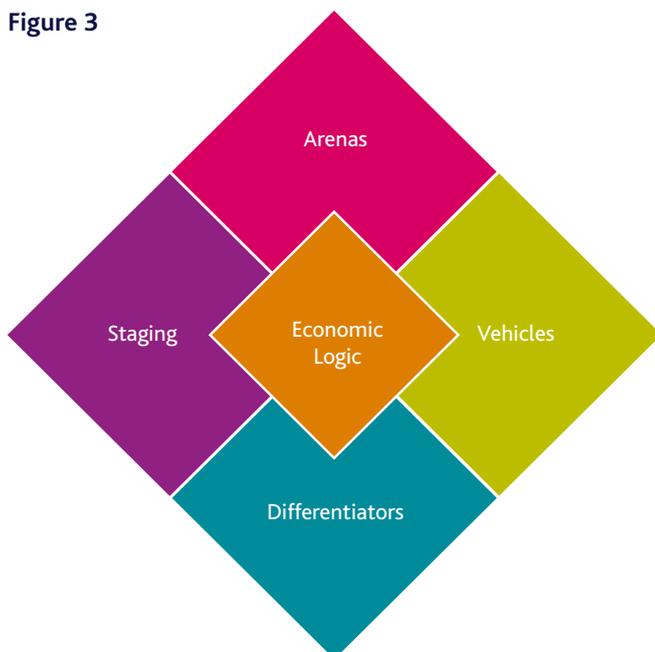
Figure 2



- **The Resource Based View (RBV)** believes that a firm's competitive advantage lies mainly in the bundle of resources at its disposal and how it can stretch these to achieve competitive advantage. This approach derives from the work of C.K. Prahalad who believed firms should seek not simply to position themselves well within their existing markets but to capitalise on their advantages to redefine markets in their favour.

Again, it seems that real world business strategies probably involve a combination of both approaches with different degrees of mix between different companies. Both perspectives are important in explaining business behaviour, including adaptation under recessionary conditions.

Figure 3



### Elements of business strategy

There are various elements which make up the strategy of the business and these are illustrated in figure 3.

- **Arenas** - where will we be active? (e.g. product categories, market segments, geographic areas, core technologies)
- **Vehicles** - how will we get there? (e.g. internal development, joint ventures, franchising)
- **Differentiators** - how do we differentiate ourselves? (e.g. reliability, price, customisation etc)
- **Staging** - what will be our speed and sequence of moves? (e.g. speed of expansion, sequence of initiatives, need for quick wins)
- **Economic logic** – how will we obtain our returns (profits, cash, ROI etc)

All these elements are relevant in considering business strategy in recessionary times.

### Business strategy and economic recession

In general terms it is possible to identify three broad ways in which businesses might adapt during difficult economic conditions such as recession:

- **Retrenchment strategies** – this appears to be the most common approach adopted by businesses to deal with recessionary conditions and might involve cutting operating costs and divestment of non-core assets, especially in the short-term. Examples include: divestment of businesses, closure of plants, reductions in employment; cuts on a wide range of expenditure including R&D, marketing and training.

- **Investment strategies** - this might involve expenditure on innovation and market diversification. Recession is regarded as an opportunity to implement strategic change that would otherwise not have occurred. Such strategies are risky and many firms are likely to be too preoccupied with short-term survival to think about innovation and growth, or lack the resources to implement such strategies effectively.
- **Ambidextrous' strategies** – these combine retrenchment and investment. It is likely that most firms adapt under recession conditions through judicious cost/asset-cutting behaviour and through investment in product innovation and market development.

However, business performance is highly variable under recessionary conditions, and no particular strategy can guarantee survival and success. Much depends on contingent factors such as, for example, business resources, relations with other stakeholder groups etc. Furthermore, business performance under recessionary conditions does not map closely on to organisational characteristics such as business size or sector.

**Figure 4**

	Large size company	Medium size company	Small size company	Trade Association	Total
Manufacturing	1	1	1	1	4
Services	-	3	2	-	5
Construction	-	1	-	-	1
Total	1	5	3	1	10

### Perceptions of economic recession

This section concerned the perceptions of the respondent companies about the economic recession in the UK and worldwide and also their perception of future economic trends. It should be noted that these questions were asked during the period November 2009 to February 2010 and subsequent to that date the UK formally came out of recession with small GDP growth in the last quarter of 2009.

This theme is essentially about the **perceptions** of companies about future economic prospects but the reality is that companies will base their business strategies around these perceptions whether they are correct or incorrect. Different companies had different bases for these perceptions. Some were quite sophisticated and relied on

### Findings of this study

In this section of the report we analyse the findings of the primary research carried out as part of this project. A total of nine companies were interviewed plus a representative of one trade association from the textiles industry. In addition to the interviews, the interviewees were also asked to complete a short post-interview questionnaire which reflected the content of the interviews.

The pattern of interviews was varied in nature as illustrated in figure 4.

The findings of this study are analysed under five main headings:

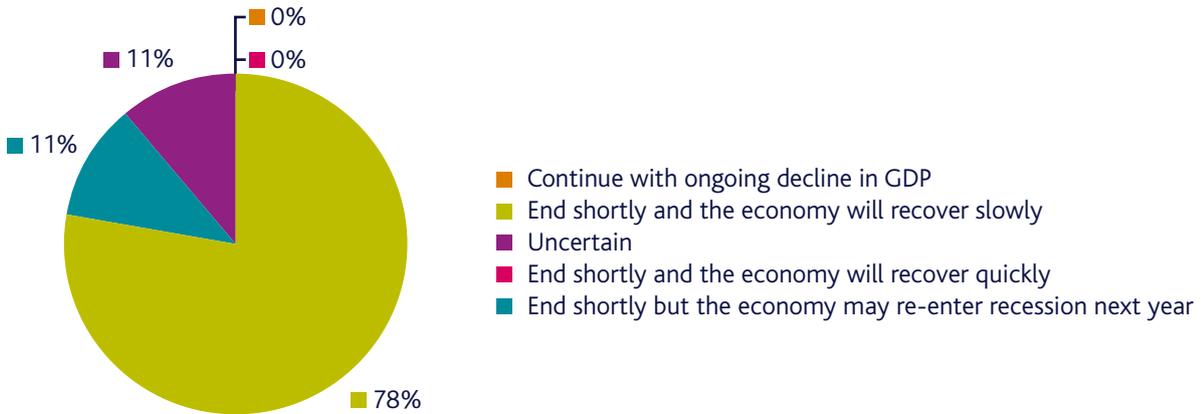
1. Perceptions of economic recession.
2. Initial impact of recession and short/medium term actions taken in response.
3. Changes to business strategy as a consequence of recession.
4. Barriers to future business growth and development.
5. Managerial implications.

specialist economic intelligence and information gained from industry bodies while for others it was little more than hunches.

The questionnaire asked respondents what was their perception of how the UK economic recession might evolve? The results are shown in figure 5.

Overall the bulk of respondents are not at all optimistic about the prospects of the UK economy with none of them anticipating a brisk recovery. Where companies are already operating in overseas markets they are anticipating expanding into those markets (particularly Asia and Eastern Europe). Where they are not already operating in overseas markets it is an option some might consider for the future.

**Figure 5: Perceptions of how the recession might evolve**



There was a general belief among most companies that they were going to have a very tough two to three years and a slow recovery afterwards. Several respondents suggested that it is the construction industry which drives a lot of economic growth in the country and that the housing industry and the associated construction industry are very, very sluggish at the moment. Another company had a view that while their international markets seemed to be recovering strongly and provided opportunities, they believed the UK economy will recover very slowly and so UK markets will be sluggish. Several companies also believed that the state of UK public finances suggests that their public sector markets will be constrained.

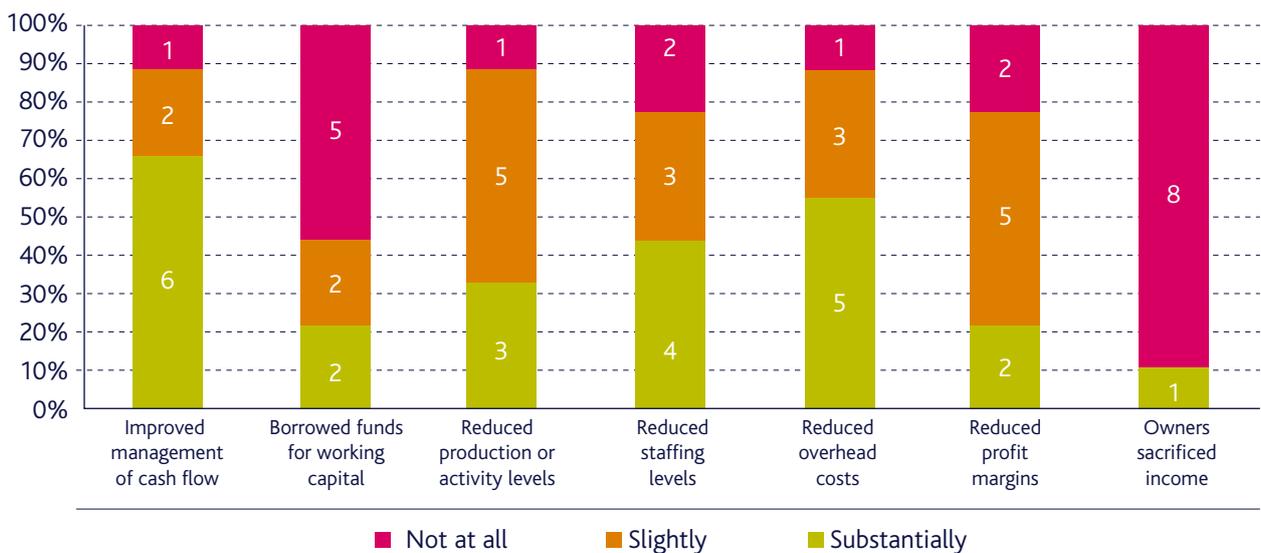
This did not mean that there would not be opportunities for businesses who seek to try and differentiate themselves

and drive forward but it's going to be tough. One company commented that the biggest impact was going to be a change of attitudes. They stated *'In previous recessions, people forgot the messages quite quickly but this time they have had such a scare in the last 18 months that there's a lot of caution out there. This time they may not forget it as quickly.'*

**Initial impact of recession and the short and medium-term actions taken in response**

Companies were asked to describe the initial impacts of recession and what, largely, short and medium-term actions they had been forced to take (or felt it important to take) following the economic downturn leading to recession. Their responses are summarised in figure 6.

**Figure 6: Initial actions taken in response to recession**



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The timing and magnitude of the recessionary effect impacted on companies in different ways. Some believed that they started to feel the impact of the forthcoming economic storm around the end of 2007 which is over a year before recession was formally declared in May 2009. Others reported feeling the impacts much later.

For most companies, the recession had a significant impact. One company reported losing substantial sums of money (approximately 10% of turnover) after having had seven years of strong profitability – something they never anticipated. Several companies reported large and sudden reductions in customer orders which have never really recovered. Another company described the effect as *'we saw a situation where there was a hole in the ground that we were shovelling money into and we didn't know how deep the hole was. We said to ourselves all we can do now is act on what we know today, we don't know how long this is going to go on for'*.

Some companies seemed to regard what happened as something unusual. Although they had seen the warning signs prior to formal recession this was not seen as an ordinary recession. One company described it as *'an economic meltdown which was like a tap that just turned off business and shook business confidence overnight'*.

It must be noted, however, that not all companies were affected in the same way to the same extent. Some companies in the services sector felt that they were always in a situation where they had to manage large variations in business demand and that the challenges of the recession were not really much different from 'normal' times. Their existing business and managerial arrangements coped well such that the effects of the economic downturn were not that significant to them.

As a consequence of the economic downturn, credit control and cash flow became major problems and nearly all companies took, at least, some actions to improve the management of their cash flow and working capital. Some felt that this was an area of management where they had let things slip a bit during the economic good times but now it had become a priority. Linked to this, as is usual in recessionary times, companies reduced stocks substantially to improve cash holdings. Most of the companies surveyed did not need to borrow funds to deal with cash flow problems and so did not report this as an issue. This seems to be because most of them already had reasonably good cash reserves which they supplemented with improved cash flow management.

The two other areas where most companies surveyed had taken at least some action concerned cost reduction. Costs

were reduced either through reduced staffing levels and/or reduced overhead costs. This is very much in line with the retrenchment strategies described earlier.

Regarding staffing levels, the actions taken were often quick and substantial. One manufacturing company reduced staffing levels from 160 to 70, almost overnight, but made a point of retaining specialist and irreplaceable skills. A services company made across-the-board reductions of 20% almost overnight since they feared for their survival. A third small manufacturing company made reductions of similar magnitude and coupled these with the introduction of greater flexibility of working arrangements for the remaining staff. Although this greater flexibility was implemented as a consequence of recessionary pressures, with the benefit of hindsight, it does seem as if it was something that should have been done earlier. Where companies operated partly outside the UK, the staffing reductions seemed to be focused on the UK end of the operation.

Most companies have taken action to reduce overhead costs substantially. Some examples of this included:

- temporary mothballing of some productive capacity
- reduced use of consultants and outsourced services
- reduced training budgets
- reduced travel expenses and greater use of tele-conferencing.

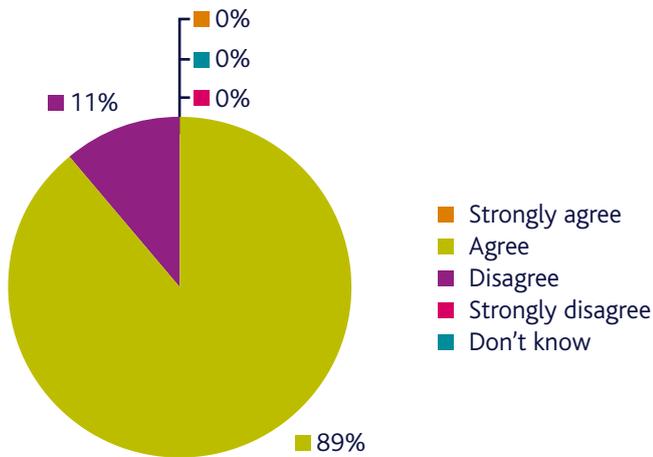
Perhaps one concern is that cutting back on some of these items too much may inhibit the company's developments in a post-recessionary climate. For example, much of the costs of travel are incurred on marketing and selling products. However reducing emphasis on these functions too much may inhibit business recovery from recession.

### Changes to business strategy as a consequence of recession

This is perhaps the key section of this report. Its aim was to elucidate from the companies involved what they saw as the major changes (if any) to their existing business strategies that they saw as necessary in the context of the changed social and economic environment following the economic recession.

Initially respondents were asked whether, prior to economic downturn and recession they felt they had developed and implemented a business strategy which was robust in terms of the expected economic circumstances. Their responses are shown in figure 7.

**Figure 7: Robust business strategy prior to recession**



Thus virtually all of the companies surveyed felt they had a robust and effective strategy prior to recession and that they were thriving businesses.

They were then questioned on what changes they had implemented (or were considering) in their business strategy as a consequence of recession. Their responses are shown in figure 8.

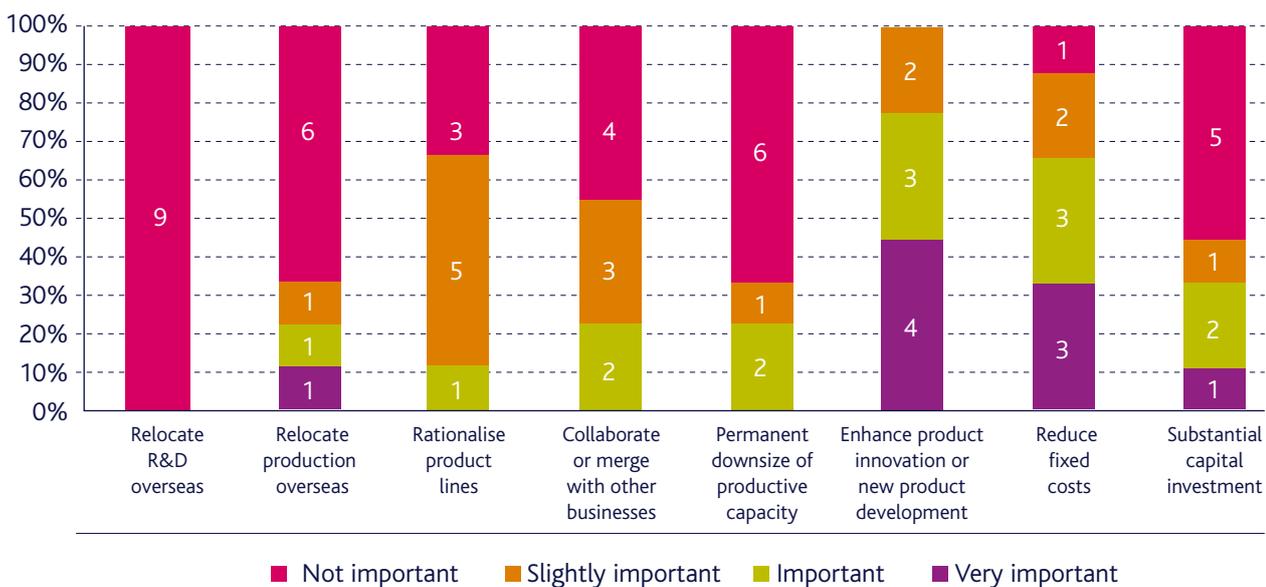
This is perhaps the key issue in this report. Our observations of practices in the nine companies surveyed suggest to us that:

- What was done largely conforms to the 'emergent theory' of strategy formulation. Although there had clearly been in-depth discussions and analysis about how existing business strategies might change, the eventual amendments were generally less substantial changes of focus and emphasis.
- The changes to strategy appear largely to be adaptive although there are some aspects of capital investment involved. Some of the companies appear to be combining investment with adaptation thus implying an ambidextrous approach.
- In many ways, the changes to the business strategies of the companies have involved changes of pace and timing to existing strategies rather than major changes of direction. Thus, for example, a company which was already in the process of expanding into overseas markets might have decided to accelerate that process in response to the pressures of recession.

A number of key strategic themes emerged:

- Many companies see it as important that they continue to try and drive down their fixed cost base as a means of sustaining competitive advantage. Part of this could involve bringing in new approaches to product development which could spawn multiple (rather than single) products thus taking out a lot of that fixed cost within engineering, the supply base and manufacturing.
- No companies envisage, at this point in time, transferring their research and development activities to an overseas country. This is because they have confidence in their existing UK based workforce to fulfil these critical roles.

**Figure 8: Changes to business strategy as a consequence of recession**



- Where companies already have overseas production operations their revised business strategy usually involves expanding the overseas production activity levels. Interestingly, one company which plans to expand production at its base in China sees this production plant as sourcing product to Eastern Europe (as well as Asia) rather than from the UK which is geographically closer. At the same time it will be noted that three companies envisage some degree of permanent reduction of UK based production capacity.
- The strongest theme of all concerns product innovation and new product development, where all the companies surveyed believe this is important to a smaller or greater degree. Companies may develop their innovative capabilities using existing staff or they may resort to buying in talent from other companies and other countries.
- Some service based companies see a key part of their revised business strategy as improving operational efficiency. This could involve doing things better, faster and looking for means of better integrating the various processes involved.
- Some companies seem to be adapting some degree of an investment approach to business strategy. However, that seems to be conditioned by, on the one hand, being able to have access to the required capital funds but, on the other hand, companies are going to be more cautious about speculative investments. They will require more robust business cases to justify such investments which indicate a high probability of success.

### Barriers to future business growth and development

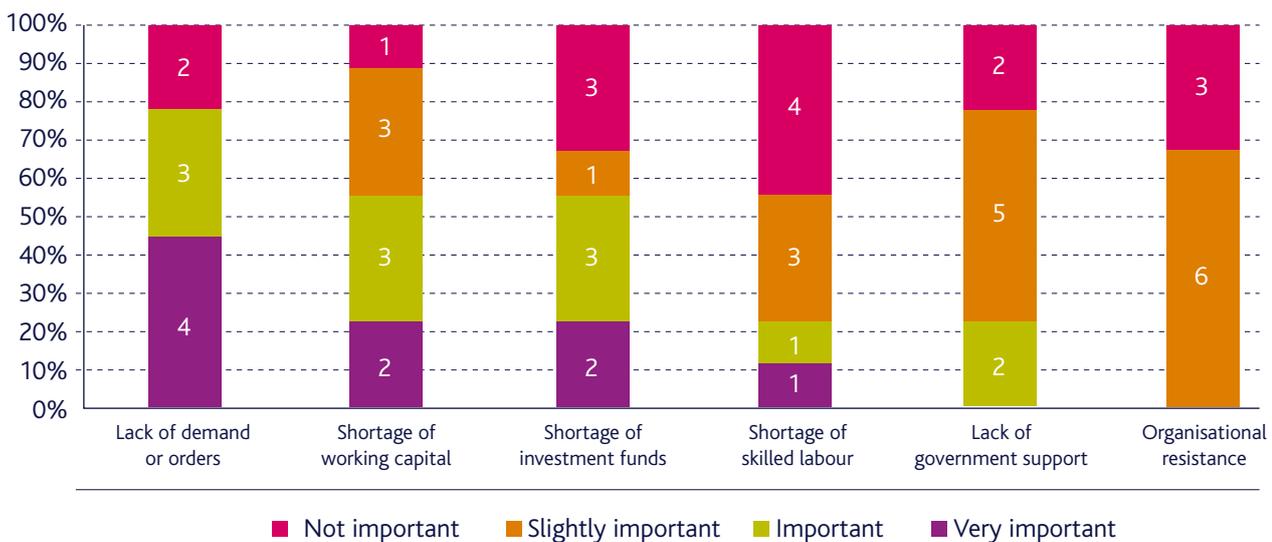
This section looked very much to the future and asked business what they saw as the main barriers to future business growth and development with regard to their company. Their responses were as shown in figure 9.

The key factor inhibiting future growth and development of companies is felt to be the lack of demand for product. During recession, some companies have lost clients, others have kept clients but have had reduced volume of orders while others have suffered both. However, given that most companies believe that the UK economic recovery will be sluggish, they do not think this bodes well for increasing product demand even though there will inevitably be some increase due to the need for customers to rebuild stocks which have been run down during the recession. Hence, much of their strategy will probably involve trying to seize market share from competitors.

There are particular problems for those companies who do a large part of their business with the public sector. The fiscal problems described earlier and the inevitable cuts in UK public expenditure pose huge threats to their business base. The uncertainty about what precise policies on public spending will be adopted just adds to this uncertainty.

Those companies which already operate in overseas markets see better prospects in those markets (e.g. Asia, Eastern Europe) and will inevitably concentrate their efforts on those markets, with the possibility of establishing or increasing production operations in those areas of the world. Of the remaining companies, most see no prospects for them in overseas markets because of the intrinsic nature of their product.

**Figure 9:** Barriers to future business growth and development



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While the majority of companies surveyed had not had, up until now, major liquidity problems, they see this as a possible problem for the future which would inhibit growth and development. Some saw potential liquidity problems arising as a consequence of over-trading as the economic environment improves which might be exacerbated by an inability to get financial support from the banks. It was noted earlier that post-recession some business might adopt pure investment strategies or ambidextrous strategies involving some investment. Some of the companies (particularly the smaller ones) who wish to do this had concerns about the willingness of banks to provide the necessary finance. Some reported instances where banks were asking what they saw as unreasonable terms for investment finance.

The role of banks in economic recovery was mentioned several times and it was often suggested that there was a role for government in this area. The question was often asked '*if the government can bail out banks why can't they support businesses*'. However, it was clear that what was being talked about was a limited role for government in assisting businesses with liquidity problems and in providing some access to capital finance where other approaches had proved fruitless. This was not a case of government bailing out failing businesses or having strong involvement in the operational aspects of businesses.

The other factors identified were not seen as major inhibitors to growth and development but it was interesting to note that there was felt to be little or no internal resistance within companies to the strategic changes needed to cope with the recession.

### Managerial implications

The view of the majority of respondents was that, by and large, their managerial systems and processes were adequate and would not need major adaptation to deal with a post-recessionary environment. There were, however, three particular areas which were highlighted as weaknesses and which were in need of improvement.

#### Cash and working capital management

During the recessionary period, some businesses experienced difficulties in managing their cash flow and working capital and this was sometimes exacerbated because of the difficulties in obtaining support from banks to deal with cash shortfalls. As a consequence, many businesses have made efforts to improve their arrangements for the management of cash and working capital which had somewhat deteriorated over a period of years. Moreover the continuing problems being experienced with the banks coupled with the potential future liquidity problems means that effective cash and working capital management is still seen as a managerial priority.

#### Business case development

Several respondents were of the view that the managerial processes for developing and analysing the business case for new developments were not sufficiently robust. They felt that during the economic good times, money had sometimes been thrown at projects with insufficient analysis of what was being proposed. Sometimes such projects were successful and sometimes they were failures but the prevailing economic climate meant that the failures were just seen as 'one of those things' and no lessons were learned. There was a belief that such luxuries will not be permissible in the future and that business case processes needed sharpening-up with a much stronger focus on business risk analysis.

#### Negotiation

The recession led to a situation, where competition between businesses was much fiercer, and much of that competitive pressure still exists. Some companies felt that their staff had, to some degree, lost the edge in terms of negotiating with suppliers, customers etc and this was something that needed enhancing as a matter of urgency.

#### Conclusions

This project provides detailed insights into how UK companies have responded strategically to the impact of economic recession. While the companies are not optimistic about the future of the UK economy, they are largely optimistic about their own future and their ability to deal with problems that might occur in the years ahead.

Many of the companies have had to make large scale organisational changes to deal with the impact of recession and have had to make changes (sometimes substantial) to their existing business strategies. They recognise that in the 'good times' prior to recession there was some degree of loss of focus on certain aspects of management and financial management but remedial action has been taken to alleviate these problems.

For the future of the UK economy, it is to be hoped that most other UK companies will have the same attitude and ability to affect change that has been demonstrated by the companies researched during this project.

A fuller version of the project report including relevant references and sources can be obtained from Professor Malcolm Prowle at [Malcolm.prowle@ntu.ac.uk](mailto:Malcolm.prowle@ntu.ac.uk)

ISSN 1744-7038 (online)

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