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How SMEs can learn from one economic downturn to prepare for the next

Do you know that sinking feeling you get when your business starts to slow down, or worse yet, stop? You’ve invested time and money into this venture, so the last thing you want to happen is for it all to come crumbling down.

If you’ve already been there, as so many of us have, you know it’s not a good place to be, so it’s only natural that you would do whatever it takes to stop it from happening again. But what can you do to be better prepared for the next economic crisis? As the economy continues to recover, there’s one thing in the back of many business owners’ heads: cutting costs. This article will help small business owners identify their current expenses and offer tips and actionable advice to reduce costs in preparation for the next downturn.

Let’s get started!

Tip #1. Start by analysing your business’s current expenses

The first thing you need to do to start managing your expenses is to know exactly what your business’s expenses are. In other words, you need to measure your burn rate and classify all of your expenses. This alone may give you some surprising insights into how your particular business can start cutting costs.

It’s also important to understand how your current expenses are impacting your bottom line. It may be the right time to look at factors such as:

- How much money is lost due to *unproductive time*?
- How much money was wasted on unmet goals?
- How much money can you save by reducing or eliminating overheads?
- What is the return on investment for supplier relationships, and how can you improve them?

You should also look at these expenses in terms of how they relate to revenue, margin, and other related metrics for measuring success. This will help you make more informed decisions about scaling back or eliminating certain expenses should it be required.

It may be difficult to make these determinations overnight, but it will be worth it in the end, and it’s certainly better to start doing it in preparation rather than waiting for the next crisis to show its ugly teeth.

But, what do you do now that you’ve identified where your business is losing money? You need to decide what stays and what goes.

Tip #2 Apply the 80/20 rule to keep your major expenses in check

The 80/20 rule or “Pareto Principle” is a management principle that states that 80% of the effects come from 20% of the causes. Simply put, this means that the greatest impacts on your business usually come from about 20% of your expenses. This is great news because it means that you can cut down on major expenses without sacrificing too much revenue. So, you should focus on identifying and reducing the other 80%.

One of the most effective ways to cut down on that 80% is to save on office space costs. Some ways to accomplish this are:

- Switching to *co-working spaces*.
- Downsizing to a more affordable space or moving to a *home office*.
- Going fully remote and hiring a *virtual mailbox* to handle any physical mail.

Getting a virtual telephone service, etc.

While cutting these costs will potentially hurt your productivity and team cohesion, they’ll only hurt a part of the 20% that it affects, so the money you save will have a much bigger impact than the revenue you stand to lose.

Tip #3 Switch to online banking platforms

The days of standing in line at the bank are long gone. Now, you can manage your business’s finances on your own time, from virtually anywhere, by using an *online bank*. The best part is that you’ll be saving time and money at the same time.

Online banks also offer the benefit of charging lower fees, and they offer better interest rates on savings accounts than traditional brick and mortar banks. This is particularly relevant for small businesses since they generally need to keep a good emergency fund in case of a rainy day.

Tip #4 Negotiate better deals on insurance

Insurance is a major expense for business owners, so the next time you shop around or renew your policy, be sure to haggle for a better price or terms. Insurance companies are known to offer discounts or waive fees to keep customers happy, so be sure that you explore these concessions.

This is especially important in the face of an economic downturn, as insurance premiums tend to spike during such periods because of higher claims. The opposite happens during sunny days when the economy is booming, so that’s the point in time when you want to start negotiations.

Tip #5 Beef up your emergency fund

As mentioned, emergency funds are important for small businesses. They act as a safety net in case of an economic downturn and let you meet necessary operational expenses, keeping your business afloat without incurring debt or taking out loans. Beefing up your emergency fund can be as simple as throwing a couple more pounds into it every week or finding other creative ways to invest funds from your company’s revenue stream.

Tip #6 Make your business more resilient by diversifying your products

One great way to make your business more resilient is by offering other products or services. It's a way of saying, "don't put all your eggs in one basket." For example, if you're a marketing consultant who focuses solely on SEO, adding additional services like social media marketing, PPC, and email marketing will spread your risk while increasing your revenue potential.

To understand this better, think about the different effects of the pandemic on a travel consultant specialising only in cruises and hotels, compared to one that also covered RV rentals, holiday rentals, and outdoor activities. Yes, both would have still felt the pinch of a decrease in business, but the latter would have definitely recovered faster because of the spike in staycations and family road trips that made social distancing easier while travelling.

Tip #7 Be conservative when hiring to avoid having to cut down on staff

It's normal to want to hire a big team as your business grows, but there are several reasons why this may not be a good idea, especially if you're preparing for a dry business season. On the one hand, when things get slow, there may not be enough work to go around, so some jobs may simply become unnecessary. On the other, if business becomes slow for an extended period or even dries up entirely, then you won't be able to pay your staff. This will inevitably result in the need to let part of your staff go, a position that no one wants to be in.

So, my advice is to grow your team conservatively. Only hire new talent when you actually need it and do your best to get the most out of the talent you already have.

The bottom line

One of the most important things to think about when managing expenses better for the next downturn is understanding exactly what those expenses are. The 80/20 Rule is a great way to manage major projects. Cut down on big expenses that don't produce results and give attention to the tasks with the highest return on investment. Switching from traditional banking platforms to online banking will save both time and money in various ways, and using them to build a good emergency fund for your company will also translate into a better passive income stream. Finally, hiring conservatively, negotiating insurance prices and diversifying your products and services portfolio will be all you need to prepare your business for another potential reset of the global economy.

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