

UNIVERSITY AMERICAN COLLEGE - SKOPJE

**CORPORATE STRATEGIES IN A DOWNTURN**

M. Bojdziew, PhD

M. Barisin, MBA (PhD applicant)

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## **ABSTRACT**

Undoubtedly the most spoken off topic is the current economic downturn. There is no country that hasn't felt the heat and the fire is not even close to being put out, if anything - it is intensifying.

Browsing through the articles and the different views on what is happening and what is about to happen...is it a depression yet or are we still calling it a recession? Is it the biggest hit since the late 1920's or is the number of jobs lost larger compared to 1940's...

This study will not deal with terminology, it is not focusing on the cause and effect of the situation but the accent is on finding ways to deal with the present in the most painless way and maybe even gain something from it.

This is a two part study, the first part being the result of the secondary research or literature review and the second is a quantitative research using a questionnaire.

The first part is a collection of different studies, views and articles by different authors, professors, experts as well as the CEO's of some of the most prominent corporations in the world at the moment.

It starts off with a quick look of the economy in 2009. Then it goes into the predictions of how different industry sectors will be hit by it. Next are some hands on strategies organizations can use to stay stable in this turbulent time as well as how to manage investor's relations. The literature review concludes with the opinions of a number of successful CEO's.

The research was done on a sample of 100 Macedonian executives currently holding top management positions within domestic and international corporations. The aim of the study is to make a correlation of the business models the Macedonian executives believe to be the right ones for this period and the strategies that are most buzzed about in the international business community.

The analysis of the results was done in SPSS taking into consideration standard margin of error and using the standard deviation curve.

This is not only aimed at contributing to the body of knowledge in the field of business strategy, but hopefully it will make an interesting read as well.

*Key words: strategy, business model, downturn, recession, depression, investors, marketing, management, retail, finance, capital, industry sectors.*

## **PART I: LITERATURE REVIEW**

## ECONOMIC VIEW OF 2009

Trade encourages specialization, which brings prosperity; global capital markets, for all their problems, allocate money more efficiently than local ones; economic co-operation encourages confidence and enhances security. Yet despite its obvious benefits, the globalised economy is under threat.<sup>1</sup>

*“We’ve got so far to climb out of this [financial] hole that if we start today, then on any reasonable time path we might still be climbing out a year from now,”* says Robert V. DiClemente, chief U.S. economist of Citigroup (C) in New York. Predicts the AFL-CIO’s chief economist, Ron Blackwell: *“Things will get worse, perhaps much worse, before they get better.”*<sup>2</sup> That said, this job bust won’t last forever. There are forces at play that will eventually pull the economy out of its free fall. The key is smart government policy that sets politics aside. It must provide a combination of short-term consumer stimulus and long-term investments without stepping over the line into wasteful and innovation-stifling industrial policy.

At the same time, a note from Standard & Poor’s Global Investment Policy Committee on Dec. 3 says: *“Despite ongoing weak global news flow, given that equity performance tends to lead an upturn in the fundamentals by roughly six months, global stock markets have rebounded on hopes the worldwide economic and profit outlook will begin to stabilize by the [second half] of 2009. Time will tell.”*

One way or the other, the fact of the matter is that we have a problem that came on too strong and caught even the best of us unprepared it is time to sit down and strategize!

## THE EFFECT PER SECTOR

How will your sector perform in 2009?

We will briefly look at some of the most profitable sectors in today’s economy to see how the current situation has affected each.

### Advertising

The advertising and marketing sector has largely held up well, despite staff cutbacks in larger groups such as Euro RSCG. And while advertising spend is down across the board – with

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<sup>1</sup> Feb 5th 2009, *The Economist* print edition

<sup>2</sup> Taken from *Investors and the 2009 Economic Outlook* by Ben Steverman, Business Week, December 11, 2008

Nielson reporting dips in internet ad sales – many executives suggest SMEs will want to use the downturn to help get an edge on the competition.

Jane Emery from Grey Group says there are “huge opportunities” for clients willing to take advantage of the tough environment.

“We have clients who see a real opportunity to lift market share. And we have clients in the food area that are having no problems whatsoever because people are not eating at restaurants, they’re eating at home, so they’re doing fine,” she says. “We talk gloom and doom, but the opportunity for anyone is to seize these moments.”

### Agribusiness

While agribusiness has been hit hard by the drought, there are still some positive signs for the next 12 months. The financial crisis has seen commodities fall in price, while global food shortages should help exports. The dollar’s slide should also help in that regard, with the industry’s export value predicted to rise 56.3% on 2007-08.

### Construction and engineering

With credit tight, the industry may not see a huge recovery until next year. Jim Barrett from the Construction Industry Group says the health of the construction and engineering industry depends on new projects booked over the next six months.

“In the public sector, we’re buoyed by the fact state budgets have a significant infrastructure spend. The downside to that are the significant cuts in revenue,” he says. “But unless there’s a significant stimulus in terms of the development of new projects in by the middle of the year, construction will, in 2009-10, start to suffer quite significantly.”<sup>3</sup>

### Food and beverages

For the food and beverage industry, exports are going to be the key in 2009. With the falling dollar, the meat, grains, dairy and wine industries should enjoy a significant boost for export earnings. But with the two biggest customers – the US and Japan outside of Europe – already in recession, the next 12 months will be nervous ones for the industry. And the falling dollar could see the price of raw food materials go even higher. Nevertheless, there is some good news for local food and beverage retailers, which may see a surge in sales as many people opt to spend more time cooking at home.

### Financial services and insurance

The financial services industry will be seeking a recovery in 2009. The collapse of some of the most prominent financial institutions points to a dire season ahead. With disappointed investors

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<sup>3</sup> Jim Barrett, Opinions, The Economist, January 2009

and few signs of a comeback any time soon, perhaps the only opportunities will be for companies dealing in restructuring and insolvency. But Jim Downey, principal of insolvency firm JP Downey & Co, says while much of the financial services sector will be hit, for some it's business as usual. "There's work for the insolvency sector. If you're looking at the accounting world, you wouldn't expect audit activity would be significantly impacted except to the extent that some of their clients might fail. "But the mergers and acquisitions sector may struggle. The tax area would also typically slow down in an environment where profits are diminishing." <sup>4</sup>

### Health and pharmaceuticals

On a global level, the health and pharmaceuticals industry should be safely buffered against the downturn, and kept particularly busy with the ageing population. Robert Bryant, general manager of research firm IBISWorld, says: "Strong growth in the 70-plus demographic will continue to propel growth in nursing homes, with strong government funding helping to stabilise the sector and mitigate risk." But with economic conditions deteriorating, non-essential services such as beauty spas and gyms will likely experience setbacks as discretionary spending falls. Bryant says one possible way wellness businesses can combat this is to promote their products and services as relatively inexpensive "treats" that struggling consumers can enjoy.

### Information technology

The information technology industry will be a mixed bag over the next 12 months. Many companies will be hit by government contracts drying up, while IT budgets are often the first to go during cost-cutting initiatives. But as several IT companies have already dealt with hard times during the dot-com crash earlier in the decade, adjusting for another downturn shouldn't be too much of a problem.

### Internet

After almost a decade of growth, big internet companies will be tested in 2009 as growth rates drop sharply. Google and Yahoo have already cut spending by slashing jobs and dumping projects, and both companies are searching desperately for ways to boost their advertising revenue. Also we are all aware of the managerial changes within Yahoo and the firm is expected to undergo a considerate change process. However, there are bright spots, particularly for those online retailers who are seen to offer "value" – Amazon reported its busiest Christmas period on record.<sup>5</sup> "Despite the general gloom we expect that profit for the period will show a similar level of increase on last year and early holiday period January bookings have continued strongly," Webjet's managing director David Clarke says.<sup>6</sup>

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<sup>4</sup> [www.union-network.org/unifinance](http://www.union-network.org/unifinance)

<sup>5</sup> Amazon Investors Relations, [www.phx.corporate-ir.net](http://www.phx.corporate-ir.net)

<sup>6</sup> 2009 Webjet Annual Report

## Leisure and gaming

The gaming industry should remain relatively stable, despite declining discretionary spending. The real victim is tourism, which will almost certainly be in need of a miracle during 2009. However, the corporate travel industry is down between 15% and 20%. There is a decline in activity and a movement to people buying cheaper fares than they used to.<sup>7</sup>

## Manufacturing

The outlook for the manufacturing sector remains grim. While falls in interest rates, oil prices (oil is a key ingredient in many chemicals and plastics) and input prices (such as steel) have provided welcome relief, deteriorating demand is weighing heavily on the sector's prospects. Activity in the sector fell for the seventh straight month in December on a global level<sup>8</sup>. Another complication for the manufacturing sector is the renegotiation of around 1000 international enterprise bargaining agreements in the first half of the year. It will be crucial for employers to keep wage increases to a minimum if they are to protect margins over the next 12 to 18 months.

## Media

It's getting ugly for the media sector, as consumers stop spending and companies stop advertising. Late last year, Goldman Sachs JBWere's team of media analysts downgraded their outlook for the sector for the third time in just four months because of the worsening economic outlook. "There is little doubt that global growth expectations continue to deteriorate at alarming speed," the analysts wrote. "We now assume a deep ad market recession in 2008-09, minimal growth in 2009-10 and a cyclical recovery in 2010-11."<sup>9</sup>

## Property

Property developers and lobby groups tried their very best to start the year on a positive note, claiming that falling interest rates and subdued house prices could tempt buyers back into the market. However, the falling prices is a trend that has not yet spilled over to Macedonia. And there has been a release of building approvals data on international level showing slump in total building approvals in the developed countries. Hence, any sense of optimism was almost instantly destroyed. However, economist predictions for dwelling investment in 2009 show small growth, and pressure is likely to be put on governments around the world to provide more support for the sector.

## Resources and energy

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<sup>7</sup> [www.Bnet.com](http://www.Bnet.com)

<sup>8</sup> [www.wto.com](http://www.wto.com)

<sup>9</sup> [www.gsjbw.com](http://www.gsjbw.com)

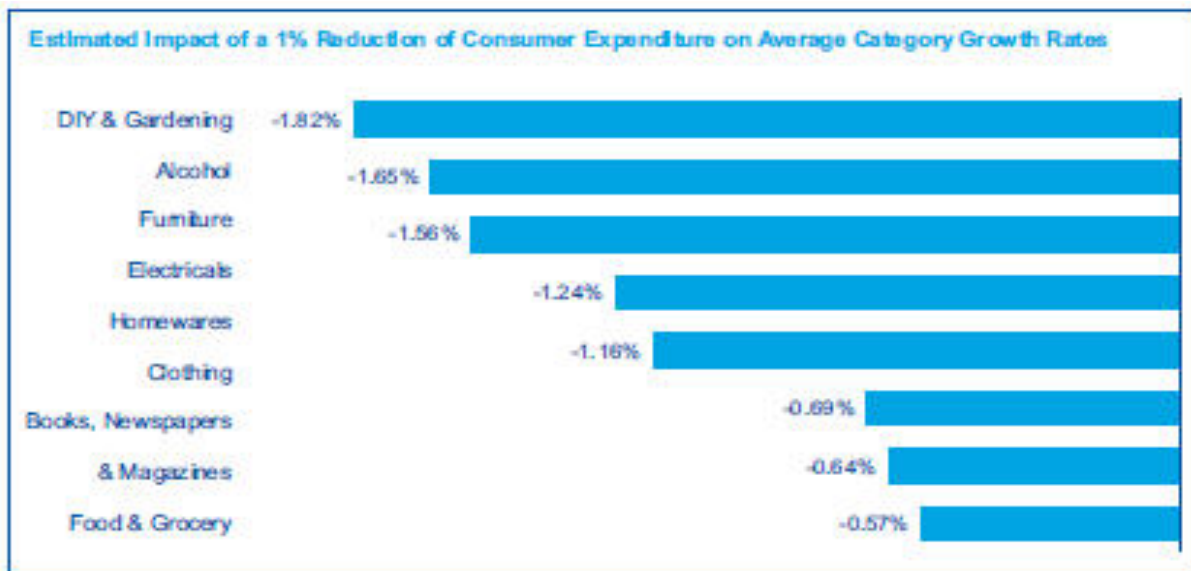


Sharp falls in commodity prices have sent shockwaves through the mining sector, from junior explorers (which find themselves struggling to access funds and looking for merger partners) to global giants. The sector looks like it's in for a rocky year. As global growth slows further, commodity prices will continue to dip, resulting in falling sales and shrinking profit margins. Consolidation in the sector looks almost certain, although tight credit conditions could limit the amount of corporate activity. There is a possibility that China's second half 2009 demand for raw materials is likely to improve, providing a positive catalyst for resources sector investment.

## Retail

Retailers are facing the toughest environment for nearly a decade. How tough depends on who you are. OC&C's research, looking at the performance of retailers over 20 years, shows who are likely to be the clear winners and losers in a downturn:

- Large ticket discretionary categories suffer most: DIY and Furniture typically suffer disproportionately (1.5 – 2.0 times the drop in consumer expenditure) and Food and Grocery the least (spend typically reduces by less than 0.6 times any drop in consumer expenditure).
- Strong players can ride out the storm: A downturn shakes out the retail market with strong players emerging even stronger as weak players lose disproportionate share and, at the margin, collapse.
- Offering value for money rather than becoming a value player is critical to success: The value sector has losers.<sup>10</sup>



## Telecommunications

The fact that most of the products and services sold by the telecommunications sector are now regarded as commodities is both an advantage and disadvantage for those companies operating in the sector. On the plus side, demand should remain reasonably steady, although sales to the SME

<sup>10</sup> Retail in a Downturn: Just How Bad Is It? OC&C Strategy Consultants

sector are likely to be under pressure as businesses cut back on spending. On the negative side, telecommunications companies can only really differentiate on price, which means competition will be cut throat and margins will be under severe pressure. There is a view that the telecommunications reseller will be one of the most at-risk industries in 2009, and predicts a number of smaller players will be forced to consolidate as conditions get tougher.

### Transport and logistics

The transport sector, like the retail sector, is another with fortunes tied very closely to the wider economy – which means companies in this industry are bracing for a tough year. While the sharp fall in oil prices has helped take the pressure off margins, competition in the sector will only intensify as competitors scramble for a diminishing amount of work. Freight rates, which have fallen sharply in recent months, are likely to fall further in 2009. All this looks certain to lead to another round of consolidation, particularly among the smaller players. The airline sector will also be under particular pressure, as consumer spending continues to slump.

## STRATEGIES IN A DOWNTURN

Your best strategy in a downturn depends on where you stand on these three dimensions. For example, if your company has a strong financial position, then your strategic and industry position give you a variety of options. You could out-invest competitors in marketing to increase customer loyalty. You could attack or even acquire weaker competitors; you could price products to gain share. You may be well-positioned to lead consolidation within your industry, or to dominate critical market niches by concentrating your financial and marketing strength.<sup>11</sup>

If your company has a weaker financial position, by contrast, you face a different set of possibilities. Depending on your strategic position and your industry's volatility, your best options may be to divest non-core assets and restructure the balance sheet, or accelerate decisions around reducing cost and debt. You may need to seek alliances or merger partners and dispose of anything that is not essential to survive. Or you may choose to reposition your business by selling weak operations and focusing on a sustainable core business.

So, rather than just lower your prices, what can you do?

1) **Watch for shifts in price structure:** It can be easy to watch the sales organization create unique deals to make sales happen, which have an impact on changing the way pricing is done. Sometimes this is acceptable. But it should be done in the context of understanding the long-term impact, not just on a per-deal basis. For example, it's possible that a change in price structure for

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<sup>11</sup> Kathleen Carr, Winning in Turbulence: Diagnose Your Downturn Strategy, [www.memoceo.harvardbusiness.org](http://www.memoceo.harvardbusiness.org), January 19, 2009

one deal will open up opportunities in other accounts as well, if approached from a corporate-wide perspective.

2) **Monitor customer-level profitability:** As prices decline, you may find that some customers become unprofitable. Others become less profitable and should be approached differently than those with higher profitability.

3) Adjust to changing customer needs: Through market research and direct contact, you can determine how economics are changing for customers. The question to ask is – how can we restructure our pricing to address the changes our customers are facing?

4) **Update price sensitivity research** – often: Your customers are facing cost-management challenges. Your competitors are making pricing changes. The research you completed a short while ago may already be out of date.

5) **Focus on delivering tangible results for your clients**, either getting their customers to spend more, or help save them money. The more you do this, the more they need you. The less likely they will dispense with you.

6) **Build on the existing positives** – do you have any products or service offerings which actually do well in a downturn? (Even in the Great Depression of the 1930's there were industries that actually boomed.) What distinct strengths do you have to keep you ahead of the competition for the foreseeable future? What can you do to build upon these?

7) **Cut back on any non-important/non-urgent expenditure** to build up your cash reserves. It also demonstrates to your people that we are living in different, and more difficult times, where things need to be done differently. Make sure you put into context your reasons for cutting back, but equally, how you are still going forward as a business.

8) **Use spare capacity to revisit and refocus your brand** and rectify inefficient internal processes – make your ship is more robust in more stormy waters ahead.

9) **Maximize every aspect of your resources.** Make every one of your team is part of the firm's marketing department. You need to give them real support to achieve this.

10) **Scenario planning.** David Knowles, head of business evolution practice at accounting firm Pitcher Partners, says it's a good idea to start with scenario planning. Test what will happen to your business if the downturn is mild, bad or severe. Ask yourself what will happen if interest rates jump another 2% or even 5%.<sup>12</sup>

The managing director of 333 Performance Management, Martyn Strickland, says that if a company is sliding into trouble you need to ask yourself one big question – what is the root cause of your problems? He argues that it's unlikely to be an external factor, like higher interest rates.

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<sup>12</sup> James Thomson, *Strategy in a Downturn – 10 lessons from the last recession*, [www.smartcompany.com](http://www.smartcompany.com), May 2008

Instead, look for internal problems, such as poor internal systems, key staff that are not up to scratch, or a poor business plan. He suggests four areas to look at specifically. Revenue, cost structure, the quality of the business plan and the capital structure. If you spot potential problems – such as work drying up in a particular division or business area – then plan how you would respond to that. Will you freeze wages? Force staff to take holidays? Cut wages? Make some staff redundant? “Forewarned is forearmed,” Knowles says. “At least if you are alert to the issues you are going to be able to adapt.”

11) **Flexible balance sheet.** Greg Will says balance sheet flexibility – which basically means making sure you have plenty of cash. “In this cycle, generally businesses will extend their payment terms, so cash is going to get tight,” Will says. “A lot of businesses that held more of their assets in cash survive better in a downturn, because they can weather that storm.”

As well as making sure you are paying careful attention to cashflow – and that means chasing down those debtors – think about ways to turn your assets in cash. Will suggests businesses could look at selling plant or equipment and then leasing it back. If you own your building, think about sub-letting it to bring in cash, or think about moving to another office and leasing out the entire building. Reducing debt will also give you more balance sheet flexibility. We are seeing a number of companies raising money at the start of the downturn to pay down debt increase the amount of cash at their disposal.

12) **Flexible operations.** Most businesses will have more than one source of revenue – that might mean the business has a number of different business divisions or perhaps offices in different locations. Be prepared to switch your focus and effort from one division into another, depending on where the best opportunities are.

13) **Market share.** It’s tempting to cut marketing spending in a downturn. Don’t. If anything, you should be increasing your spending. “When we look at the last recession, the better business actually held that expenditure to win market share,” Will says. “When things turned around they were much better placed.”

If your competitors are struggling during the downturn, you can quickly take advantage of the fact and grab customers from them – but it will only happen if your brand is in good shape.

14) **Staffing.** Hiring costs is one area you can save money in a downturn by concentrating on retaining your staff. “We’re finding that in terms of a downturn, it’s making it increasingly difficult to motivate employees,” Will says. He recommends improving communication with staff where possible and really selling them the benefits of working at your company. Keeping staff is always cheaper than finding new ones.

On the other hand, you must make sure your staff are downturn-ready. It’s also worth remembering that it might be possible to pinch disgruntled staff from struggling competitors. Financial services companies and investment banks are currently going through a big period of poaching as the fallout from the credit crunch wreaks havoc on the sector.

15) **Cost cutting.** Cost cutting is always a good idea in a downturn, but companies must be careful to only cut costs at the periphery of the business. Good cost cutting targets include any investments you may have made when times were good or even projects you have experimented with in recent years - “luxury” type items, such as corporate entertainment, travel and conferences.

16) **Product range.** Now is the time to put that BCG Matrix into use. Review your entire range and think about which products actually, work, with particular attention to the margins products attract and the marketing spend each product needs. Focus particularly on successful products or services and discard less successful ones you may have preserved with during better times. Invite customers into your business to help with the product range review. You’ll be able to better tailor your products to their needs and they’ll feel like they are appreciated and listened to.

17) **Customer/supplier analysis.** It is also worth thinking about how the slowdown will effect key customers and suppliers.

18) **Mergers and acquisitions.** Some of the competitors will not survive the downturn. If you feel your own business is in good shape, it might be the perfect time to acquire a struggling rival, grab their customers and build your market share on the cheap.

19) **Steering committee.** Form a steering committee within your business to plan for future growth when the economy turns again. “Start now to plan for an upturn so you can hit the ground running.

20) **Change management.** Finally implement these changes with a savvy change management techniques to decrease resistance and eliminate possible sabotage.

## **PART II: RESEARCH**

The questionnaire contains 25 questions out of which the last 5 are demographic questions. It was distributed to 100 executives within the Macedonian business community who are considered the key decision makers in their organizations.

The analysis was done by using the SPSS software and the data is statistically reliable.

The questionnaire is included in Appendix 1.

The margin of error of the research is 8%, meaning that if the same questionnaire is administered another 1000 times, the results would be the same within 8% variation.

The results did not find the researchers surprised. It is obvious from the answers that the executives are primarily concerned with their bottom line. Very few of them find opportunities in the harsh times we are faced with.

Howe ever, most of the respondents feel that the economy will recover by the turn of 2010, which is also the case of the Macedonian Stock Exchange, slowly going up (mind you it is the time when most firms revealed their dividend policy for the year so it is not a true representation of the economy).

The bank loans are not affordable nor are expected to be any time soon. Expectation of drop in earnings is already the case and it is predicted to go on. Almost all organizations anticipate liquidity and solvency problems. Vast majority of respondents will diversify their portfolio of investments to make it more secure and a lot would turn to bonds as the most stable and payment guaranteed product.

There are no products in the making at this time and no plans for it either. Competition is stronger and prices are falling squeezing the margins more and more. Demand is going down but some have reported that it has stabilized this month.

Open internal communication is believed to be the way to go to keep the organizational culture and the cohesiveness of the employees. Although hard to do at times, open communication with stakeholders is essential at this time, especially with the shareholders and suppliers who are trying to diversify and escape being locked to one buyer.

All of the respondents require government subsidies in order to lessen the pressure of the falling economy. The ever changing laws in a country of transition where laws change on regular bases makes the business continuously change the way of doing business and not always to the better. None has reported a need to switch suppliers. Going international is an option only for few of the respondents and even those have their doubts. Even if going international it would mean staying

in the Balkans so maybe Kosovo, Albania and such. It is very difficult to get into the EU market at this time due to the high protectionism.

Expensive CRM programs are out of the question but efforts to sustain customer loyalty is crucial as well as possibly attracting new ones. Most respondents are trying to sustain what they already have and not go for more market share.

The confidence to deal with recession effectively and efficiently is subjected to doubts and most have been neutral on this question.

Most of the respondents belong to the profit sector in Service or Manufacturing inductions. All of them hold executive positions and have been at that post for 3 years or longer.

### Appendix 1

1. The economy will recover by the end of 2009.

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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2. We will undertake direct investment in 2009.

Yes	No	I don't know
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3. The bank loans are affordable at this time.

Yes	No	I don't know
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4. We expect solvency problems.

Yes	No	I don't know
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5. We expect reduced level of earnings.

Yes	No	I don't know
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6. We expect liquidity problems.

Yes	No	I don't know
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7. We will diversify our investment portfolio.

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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8. We plan to launch new product or a service.

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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9. We use benchmarking.

Yes	No	I don't know
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10. We expect strong competitive pressures.

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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11. We expect a falling demand in 2009.

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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12. We believe in open internal communication.

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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13. We need transparent communication with the other stakeholders (investors, shareholders, suppliers, customers, public, creditors, community)

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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14. We need a government intervention in the form of a financial bailout (subsidies).

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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15. We believe that the legal environment makes out business run more smoothly.

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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16. We don't plan to change our current suppliers in 2009.



Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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17. We plan to go international or sustain our international presence in 2009.

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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Country \_\_\_\_\_

18. Establishing long-term customer relationships (CRM) is the only way to go in a downturn.

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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19. We plan to increase our market share in 2009.

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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20. We are confident that we are ready to be efficient and effective in an economic downturn.

Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
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21. Type of an organization

Profit

Non-profit

22. Industry sector

Service

Manufacturing

Consulting

Sales and Marketing

Education

Public Administration

23. Current position \_\_\_\_\_

24. Number of years the respective position has been held \_\_\_\_\_

25. Former position \_\_\_\_\_, industry sector \_\_\_\_\_

