

Economic Downturn to Have Mixed Impact on Businesses

Economists, businesspeople and other observers who appeared unfazed by the gathering clouds of recession now admit that the economic storm is upon us. Nothing sinks markets like pessimism, but a little clarity - not to mention honesty - goes a long way in determining how Wall Street's pain will affect Main Street.

Keeping in mind that "recession" is a technical term, sources at least agree on the presence of an economic downturn. Some industries will feel more pain than others, while small businesses often have a smaller margin of error.

Opinions differ on the severity of the downturn and how long it may take before a recovery takes hold, but concern among businesspeople is palpable.

"I think the economy is in serious trouble. The manufacturing numbers were seriously low and [businesses are] laying people off," says Harrison Barnes, CEO of Pasadena-based Juriscape, an umbrella company with 30 different holdings.

The numbers speak volumes.

The Dow Jones Industrial Average (DJIA) shed 4% of its value last week, prompting global markets to plunge 4% to 7% yesterday (U.S. exchanges were closed for the holiday); California's unemployment rate for November was 5.6%, eighth highest in the nation (according to the most recent figures from the Bureau of Labor Statistics); oil continues to flirt with the \$100-per-barrel mark; while the deepening weakness among creditors continues to exacerbate the economy as a whole.

Adding insult to injury, California faces a \$14 billion budget deficit.

One bright spot in the U.S. economy, the result of a weak currency, is the export business. But 2008 will be a year of tightening the belt for most businesses.

Determining the Nature of the Beast

The U.S. economy picked itself back up after the dot-com slowdown largely as a result of sustained consumer spending connected with the real estate boom. But now that the housing collapse is in full bloom, and with it the end of the mortgage-as-piggybank phenomenon, consumers have less to spend, says Howard Fletcher, principal of Bayshore Management Partners, based in Long Beach.

The consumer is simply "tapped-out," says Fletcher, who believes high gasoline and food prices will continue to cut into non-essential consumer goods purchases. The resulting correction will perhaps be a long-term period of pain, he suggests, necessary to fix years of deficit spending and Americans' failure to sock away money.

"I think the correction probably will put us in an extended period of slow growth, perhaps a decade," Fletcher says. "We've gone through essentially two decades of spending, with very little being put away in savings."

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Not everyone shares Fletcher's sobering outlook, even though all sources agree that the near-term future is less than rosy. It feels more like the recession of the early 1990s, and not nearly as bad as the post-9/11

downturn, says the optimistic Chuck Pappalardo, CEO of Burlingame-based Trilogy Search Non+Profit, an executive search firm.

"Overall, it seems to me, that the fundamentals around all of the businesses we deal with are pretty darn healthy," says Pappalardo, adding that the Federal Reserve Bank is on the right track. "My sense is that in California, we are well poised to make it through."

Economy's Pain = Some Businesses' Gain
Not all industries will suffer in the face of recession.

Several of Juriscape's holdings were in the private student loan business - an industry hammered in the wake of the credit crisis - before Barnes changed strategies. After witnessing a slowdown in the student loan business, Barnes decided to bet on paid niche job search Web sites instead.

Juriscape's "EmploymentScape" division operates [specific job search sites](#) for 31 different industries and positions, such as advertising, law and transportation. Barnes says the sites have become very popular in the past few weeks, without giving specific numbers, since jobseekers are more willing to pay for job listings when opportunities are slim.

"In a normal market, paying for a job board seems like a ridiculous thing," Barnes says. "It was a huge risk for us. Even as recently as three months ago, I had people leaving my company because they thought it was a bad idea."

Any business helping individuals or other businesses deal with tax headaches also will prosper in the downturn, say Los Angeles-based tax consultant Eva Rosenberg and Rich Boggs, the founder of Brentwood-based Nationwide Tax Relief.

"As more homes are lost to foreclosure, many won't qualify for the new acquisition mortgage exception to the cancellation of debt rules - since so many people refinanced a couple of years ago and drew cash out," Rosenberg says. As a result, she adds, even people who have lost their homes may owe a lot more in taxes than they expected.

Small business owners tend not to budget well for quarterly tax payments and consequently suffer when times are tough, Boggs says. And since small businesses usually live on slim margins and do not always have the resources to keep their tax burdens under control, reversals in fortune often precipitate problems with the Internal Revenue Service.

For Boggs and Rosenberg, increased tax pressure on small businesses caused by a downturn in the broader economy translates into upside for their respective businesses.

Any business plan built around saving money, relieving debt or increasing productivity tends to do well when times are tough, sources say. Freedom Financial Network, based in San Mateo, negotiates with creditors to relieve consumer credit card debt, taking a percentage of savings as payment.

"Unfortunately for the American consumer, business will be booming for us. We can't answer the phones fast enough," says Brad Stroh, co-CEO of Freedom Financial. "The demand we're seeing certainly is a warning sign."

Other types of businesses cited by sources as well-poised for the downturn include credit counselors, telephone answering services, law firms and related legal services, real estate investors buying foreclosed properties, therapists, insurance agencies, Web-conferencing providers, alternative energy startups,

businesses courting European tourists, law enforcement, healthcare and anything targeting the aging population.

Hard Times for the Small Business Owner

Small businesses in general shoulder a disproportionate burden during economic downturns, sources say. Since small businesses usually do not have the resources and deep pockets to make significant changes in strategy, the downturn hits them particularly hard, Stroh says.

"Even though there were signs of a slowdown, we waited way too long collectively to pull back on the reigns," Stroh says, stressing that the real hurt will come once demand slows. "As a small business owner, you don't have that kind of flexibility."

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Although demand for basics such as food, clothing and health care should remain stable, most small businesses - particularly retailers on Main Street - will get pinched in the consumer-driven recession, Fletcher says.

Boggs points to the plight of the truck driver, explaining how owner-operators are, in essence, small business owners. Sky-high fuel prices have, in Boggs's words, "slaughtered" these owner-operators, whose workflow is directly related to consumer demand. Twenty percent to 30% of all owner-operator truck drivers owe the IRS at least \$30,000, he says, relating this scenario to similarly situated professionals who deal with a high volume but end up with relatively little.

"At the end of the year, the net isn't that great. Anyone with that kind of business - contractors, physicians, dentists, etc. - because of the money flowing through the bank, they'll begin to see debt mounting," Boggs says.

On the bright side, small businesses that buckle down and **survive the downturn** may emerge with fewer competitors, greater efficiency and better understanding of business fundamentals. Executives often say that leaders are made during particularly challenging times.

"Business owners - when they get depressed - that's when the ship goes sideways, and they blame everything on the IRS or the housing market," Boggs says. "We say, wake up, here's where you can improve your situation."

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