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# 6 crucial steps for managing through periods of high inflation

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Unless you're a child prodigy, you probably weren't a manager the last time inflation was this high—in 1982.

On one hand, such a long stretch of moderation is a blessing for consumers and corporations. On the other, most of today's managers haven't had to build the skills needed to guide their companies through high inflation, which comes with sharp price increases and demand for higher wages. That's a problem.

The good news is that while there's no playbook for managing through the first global pandemic in 104 years, the first war between nations on the European continent in 77 years, or the lowest labor force participation in 45 years, inflation is nothing new. Leaders who skillfully manage through today's economic volatility will almost certainly report fatter profit margins and far outpace competitors for years to come. Here are crucial steps leaders should take now:

**Accept that inflation may last longer than you think**

"We continue to expect inflation to decline over the course of the year," Fed Chairman Jerome Powell told Congress in early March. But just one week later, the Bureau of Labor Statistics reported inflation had jumped from 7.5% to 7.9%, an already-high figure that doesn't reflect higher oil prices fueled by the Russia-Ukraine war. Analysts predict that inflation will remain elevated for months to come and will likely worsen, while some business leaders, prepping for a more discouraging scenario, expect inflation to linger for up to four years. Corporate America's predictions are significant because inflation responds to expectations; if consumers and businesses act on expectations of continued inflation, their expectations tend to be right.

Inflation has already become self-reinforcing, with companies across industries raising prices, often preemptively, and workers demanding higher pay. Chanel, LVMH's Louis Vuitton, and other luxury goods brands, which typically wield strong pricing power, have recently raised prices 20% or more, far ahead of inflation so far. Software makers, which can also raise prices easily, will likely follow suit.

Though the Fed is considering more aggressive interest rate increases to tame inflation, some economic sectors will remain tight, pushing prices up regardless of the Fed's short-term response. New semiconductor plants will take years to build; the labor shortage is outlasting predictions; and the shipping industry is short tens of thousands of truck drivers, a crucial link in supply chains for the whole economy.

While Powell has toughened his tone on fighting inflation, today's global environment is uncharted territory. The Fed was far behind the curve in anticipating inflation, which Powell conceded on Monday, and has been slow to address price rises. Planning for stubborn inflation, at least through 2022, is only prudent.

### Focus on cash above all

Cash is king, now more than in any other economic environment. During periods of high inflation companies need more cash to cover expenses. It isn't just because their costs are rising. Companies want to pay slower, and cash-strapped consumers fall behind on installment payments. It seems the entire business pipeline is trying to stall payments—by as much as 200 days in some cases—leaving vendors grievously short of cash. At the same time, everyone is trying to collect payments faster.

Not everyone can win, meaning companies may still face a cash crunch despite their best efforts. Fortunately, leaders can act now to avoid trouble later by identifying three main cash traps:

• *Slow-paying customers*. Confront this issue at the first sign. Some B2B companies have fixed-price long-term contracts and can't afford to absorb late payments. These companies must speak with customers and work out new payment terms. If a customer asks for accommodations beyond what's in the contract, leaders should request something in return such as an extension of the contract, an expansion of its scope, an early renewal, or prices that reflect a margin above costs. Leaders should keep in mind that some slow-paying customers become nonpaying customers. The smartest move may be to stop selling to a customer before that happens.

• *Hoarding*. As inflation rises, managers may want to order more inventory than needed. It seems sensible at first glance but can actually lead to a cash bleed. Hoarding is a bad idea if you believe your revenue will rise at least as fast as the cost of the supplies in question.

• *Capital expenditures*. Every proposed capital expenditure has an internal constituency arguing for it, but leaders must examine whether each project has to start promptly. The answer depends on how long you think today's high inflation will last and whether the Fed's inflation fighting policies will trigger a recession. Conserving cash by lowering the company's breakeven point—in part by postponing some capital expenditures—may have to be top priority.

Across the organization, cash management must rise higher on everyone's to-do list, without exemptions. Some CEOs are making salespeople accountable for collecting payments and providing financial rewards for doing so, while others are reporting cash inflows and outflows to the CFO daily. The board of directors should join discussions about the company's cash position and planned capital allocation through 2024.

## Get a grip on your data

Your competitor may seem to be gaining market share, but that could be an illusion in times of inflation. Competitors could be buying share, leaving prices unchanged while paying higher prices for inputs. Or perhaps they're raising prices, but only in line with inflation in the industry and locations where it operates. To fully understand what's happening, leaders must know the price trends specific to their part of the industry and the areas where they do business.

Government statistics are nearly useless because they're outdated and far too broad. A single national indicator like the consumer price index tells little about conditions in an industry subsector. The only way to get meaningful data is by gathering intelligence on price changes in one's sector of the industry. For example, some companies scrape websites for price increases in real time to identify patterns and trends. Managers and the board should receive financial data not just in nominal terms but also adjusted for industry-specific inflation.

### Preemptively raise prices and compensation

In periods of high inflation, businesses need a full-time task force on pricing. This team should gather external data such as competitors' prices, input prices, and consumer psychology.

The war for talent also intensifies in economically volatile times, so leaders must play offense. Star employees can easily go elsewhere and, as a result, companies will need to offer more than an inflation-adjusted raise. Keep in mind that as stocks wobble, employers are revising pay packages to focus more on fixed compensation than on equity.

### Prepare for a recession, even though it might not happen

To tame inflation, the Fed may have to clamp down hard on the economy by raising interest rates and constricting the money supply. Former Treasury Secretary Larry Summers, who saw inflation coming a year ago, wrote recently that "the Fed's current policy trajectory is likely to lead to stagflation, with average unemployment and inflation both averaging over 5% over the next few years—and ultimately to a major recession."

Most Wall Street forecasters are pegging the chance of a recession at about 30%. We won't speculate on the odds, but it's clear that companies should start writing their recession playbook now, just in case.

### Use your inner strength

In today's light-speed economy, and amid rising inflation, a subsiding pandemic, and geopolitical tension, leaders will never have all the information they want for decision-making. Leaders will have to rely on judgment and intuition. Beyond that, they'll need fortitude and courage to handle some of the hardest problems they've ever faced. These traits and abilities are sometimes called soft skills, but they're really the hard skills. Embrace them. In times like these, they're your best friends.

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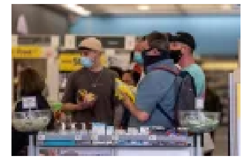

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