COVID-19 IMPACT ON CRITICAL ACCOUNTING OPERATIONS PART 3

The Advantage of Scalability

The coronavirus has impacted businesses across sectors in dramatically different ways. In commercial real estate, demand has evaporated overnight, while tech SaaS companies have kicked into overdrive to help companies transition to remote work. These examples are extremes on opposite ends of a spectrum. But whether your own company's situation has been one of boom, bust, or somewhere in between, in a global pandemic, scalability is a universal asset.

SCALING FOR SUCCESS

The ability to rapidly grow or reduce company operations has been vital during the pandemic and is likely to remain essential for quite some time. With the trajectory of the virus across the country and the world uncertain, so too is the path to economic recovery. It remains to be seen whether we have hit the bottom yet—or if the worst is yet to come.

In fact, even as some cities are returning to in person work and school, other pockets of the country are facing a surge in cases delaying reopening plans. Meanwhile, Dr. Fauci advises that most Americans should expect that they may not have access to a vaccine until the second half of 2021.

And while the stock market continues to charge forward, unemployment claims signal that the labor market has not fully recovered as companies continue to lay off workers. Despite this, the future of federal stimulus remains uncertain with Congress unable to cut a deal on a sequel to the CARES Act as of time of writing.

With so many unknowns, we can assume that COVID-19 will continue to disrupt businesses across sectors for some time. Some will need to increase headcount, production or distribution to meet unprecedented demand. Others will look for ways to contain costs in order to weather the months ahead. In times like these, one thing is certain: flexibility in scale is key to business survival.

In this third and final piece in **our COVID-19 series**, we'll look at examples of businesses at opposite ends of the spectrum, scaling up, or down, to ride out ongoing challenges brought on by the pandemic.

SHRINKING TO SURVIVE: SPOTLIGHT ON NONPROFITS

The nonprofit industry has seen an array of COVID-19 impacts. Based on various sources of funding, some nonprofits have more liquidity and resources to contend with an indefinite downturn than others. With endowments hampered by market volatility and many organizations deemed nonessential, some nonprofits have been forced to shutter their doors permanently, displacing workers and the communities that depend on the work of the organization.

Consider as an example a nonprofit community-based child development center. In March, they were forced to close their campus by local government order—leaving them to figure out how to scale back operations and sustain the center so they might return to full capacity and capability once they were able to reopen.

To scale back costs and ensure long-term survival, the child development center needed:

- **Liquidity:** As with many nonprofits, the child development center—which typically operates using a combination of Federal Head Start funding, state and local funding, and private-pay tuition—had far less than six months of operating reserves to pull from at the start of the pandemic. In order to stay afloat, they needed to identify and secure additional funding:
  - Maintaining Government Funding: To maintain their partial government funding, they were required to provide some services while campus was closed. They could not pause all operations through the shutdown or they would risk losing their government funding—and likely never reopen again.
  - Government Stimulus: The nonprofit evaluated their options, which at the time included: Paycheck Protection Program loans with the potential for forgiveness offered through the **CARES Act**; Economic Injury Disaster Loans through the Small Business Administration; and, later, the **Main Street Lending Program** which was recently expanded to include nonprofits. All debt had to be taken on carefully with an understanding of the net cash flow that would need to be generated to pay the loans back, if needed. While the future of additional government stimulus programs is uncertain, these resources may once again present an opportunity for an additional liquidity infusion.
- **Cost containment:** While spending on in-person programming was put on hold, chronic underfunding of nonprofit infrastructure presented an issue: reskilling workers to offer online services and managing finances to ensure the nonprofit could reopen post-crisis required operational investment.
  - While the child development center was able to maintain its government funding, other sources of revenue fell through. Parents who were caring for their children in their own home did not feel they should continue to pay full—or in some cases even partial—tuition for online resources provided.
  - This left the organization to trim and manage costs wherever possible so that they could continue to carry the staff and keep families engaged. By shuttering campus, they were able to curtail expenses including utilities and supplies as well as janitorial and food services.
  - This issue is not uncommon; with limited unrestricted assets to cover overhead costs, nonprofits often need to consider cost containment measures such as furloughs and reducing variable costs when navigating lengthy COVID-19 closures.

For this nonprofit—and many others like it—scaling back while managing important functions such as government grant management and compliance allowed them to weather the storm up until this point. Now, with flu season around the corner and people retreating indoors, a second wave of the virus becomes a concrete possibility even in markets that have already reopened. Many organizations may need to navigate extended or second-time-around closures, once again stretching liquidity and containing costs to sustain them through the next phase of the pandemic.

UNBRIDLED GROWTH: SPOTLIGHT ON BIOTECH

In the early days of the pandemic, biotech innovators struggled as clinical trials well-underway were derailed as the entire healthcare landscape pivoted to focus on the novel coronavirus. Many small biotech companies without the liquidity to pivot were forced to undergo layoffs, cut compensation and scale back spending on clinical trial programs. But there are also major success stories emerging in the industry.

On this end of the spectrum, consider an example of a private biotech player agile enough to quickly redirect resources toward developing a vaccine for the coronavirus—capitalizing on available government grants.

With Biomedical Advanced Research and Development Authority (BARDA) funding in hand, the current climate presents an opportunity to catapult the biotech start-up into the next phase of growth. To support this growth, the biotech company must develop a plan to address:

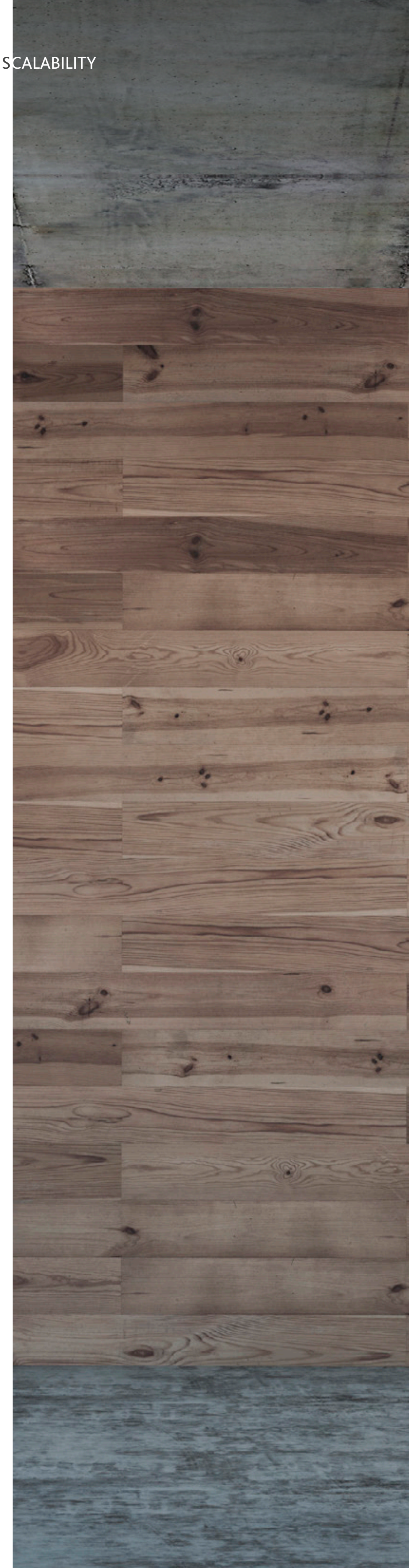
Compliance: With government grants, the company requires a financial controller to help with rigorous reporting. Government grants lead to additional layers of scrutiny—so the company needs to have all the systems and controls in place on day one.

Funding management: With an influx of new funds, the company must appropriately track funding sources and terms for its capital. The biotech also needs to maintain their chart of accounts and track clinical trial contracts spend management. As the vaccine moves through the Research & Development cycle into the manufacturing stage, they will need inventory management as well.

People: As the company scales, it will need to align organizational design to the future state of the business, ensuring the right people are in the right roles to support rapid growth, as well as hire to build out research teams and/or reskill current staff.

Exit strategy or commercialization planning: Next, the biotech company will need adequate planning to navigate the final stage of their R&D cycle. They will want to think through potential scenarios and run models to explore these options. If the vaccine works, what is their plan? Will they scale their manufacturing infrastructure? Will they choose to license the vaccine or will they sell to cash out?

The ability to scale up quickly offers the biotech company the flexibility and speed they need in order to capitalize on a rare moonshot opportunity. With the virus likely continuing to disrupt business as usual for some time, there will continue to be pockets of opportunity across industries for businesses that can scale effectively enough to meet a need during the crisis.




Social
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4 LEVERS FOR FLEXIBILITY OF SCALE

To expand or contract a business on a dime requires flexibility, agility and foresight. For companies navigating COVID-19, taking concrete steps now can ease the pain of scaling a business down the road.

How can companies ensure the flexibility of scale to navigate economic recovery?

1. **Contain costs.** When met with financial constraints—or the need to rapidly invest in growth areas—it will be critical to contain unnecessary expenses. Consider what costs can be pared back: Can you pause certain projects and initiatives and reallocate funds where there is the greatest opportunity for growth? Do you need to maintain your physical workplace, or can you lose the overhead? Do you need to pay for utilities while your workplace is closed? Can you temporarily furlough workers or negotiate pay reductions or freezes until the situation improves?
2. **Build a safety net of liquidity.** COVID-19 could continue to disrupt the business environment for another 12 months or longer. Whether your business needs a capital reserve to invest in areas of growth, or to pay the bills while waiting out the storm, conserving liquidity will help fortify the financial health of your company. Investigate all potential funding sources available, as well as the terms attached to potential loans and grants.
3. **Cultivate a nimble workforce.** COVID-19 has required workers to work harder and differently than ever before. An adaptable workforce is key to scaling your business up or down. Be prepared to: reskill and upskill your existing workers to fill new roles; staff for agility so workers can serve as pinch hitters to serve areas with spikes in demand; and, when possible, hire contractors and freelancers instead of full time employees to keep costs variable.
4. **Outsource infrastructural needs.** One way to minimize fixed costs and ensure best-in-class operational agility is by hiring external experts for non-core business functions, such as technology, finance & accounting and human capital resources. Business operations are critical to maximizing workforce productivity and financially navigating a challenging climate. External experts working with companies across industries to scale during COVID-19 can offer tried and true best practices to chart what would otherwise be uncharted territory.

While it's impossible to know precisely what lies ahead as the business world navigates the global pandemic, companies that take these four steps to ensure flexibility of scale will be best poised to contend with whatever comes their way—from a second-wave shutdown to an unprecedented growth opportunity.

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