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New Report On Bay Area Companies Shows How They Are Surviving the Recession and How They Will Drive The Recovery

Bay Area Companies Cut Deeper, Faster and Many are Placing Bets on Green Tech and Innovation

SAN FRANCISCO, April 24, 2009 — Bay Area businesses have responded quickly to the economic downturn by aggressively managing costs and making key investments to position themselves for the economic upswing, according to “Managing Recession: Strategic Responses to the Economic Downturn,” a report released today by the Bay Area Council Economic Institute, conducted in partnership with global management consulting firm Booz & Company.

The report is the result of in-depth interviews with 56 senior executives from large and small Bay Area companies in a range of industries and compared their responses to a global survey. Interviewees were asked about both defensive strategies to survive the recession and long-term strategies to participate in a recovery.

The region’s economy merits special study due to its central global role. The Bay Area’s economy has undergone massive growth in the past decade and now has a regional gross domestic product of \$437 billion a year. If the region were a country, its economy would be the tenth largest in the world, between Canada and Brazil.

The report finds that perhaps due to the recent experience of the 2001 recession – which originated in the Bay Area and had a much more severe impact on the local economy – Bay Area businesses appear to be better prepared to get through the current downturn. Bay Area businesses generally planned for the recession early, and acted quickly to reduce costs and conserve cash. At this stage in the recession, Bay Area businesses are optimistic and focusing on opportunities offered by the disruption – in essence, placing strategic bets that will create advantaged positions once recovery emerges. The key engine of future growth in the Bay Area – innovation – does not appear to be materially threatened by the recession, and the recession may in fact accelerate the shift in focus to new areas such as clean technology

Like the rest of the United States, the recession that began in late 2007 has heavily impacted the Bay Area. Though lightly affected at first, the Bay Area has followed the rest of the state and the nation into a steep economic downturn, with local governments, ports, transit agencies, foundations and employers and employees all swept into unprecedented economic territory. Few have been unaffected.

“The reports findings are predictably sobering, considering the declining revenue, loss of jobs, and diminished financial base common to most businesses we interviewed,” said Economic Institute President & CEO Sean Randolph. “But behind this reality and the headlines of deepening crisis, we found that many regional businesses are both adapting in the short-term, and continuing to think

long-term. Entrepreneurs remain active, and most technology companies are continuing to invest in research and development, which gives us grounds for optimism. The Bay Area is all about innovation, and our companies appear well-positioned to benefit from a recovery.”

While struggling – Bay Area companies have lost more than 40 percent of their market cap since the start of the recession – they appear better prepared to navigate this recession than the 2000 downturn, and have acted more aggressively than companies in other regions of the world. For example: 75 percent of Bay Area companies interviewed have a clear recession plan versus 66 percent globally; 80 percent have cut discretionary spending versus 71 percent globally; and 62 percent have laid off staff versus 58 percent globally.

Companies generally say their survival strategy is to focus on cost reductions, cash conservation, and credit risk reduction. Companies explain that Bay Area labor costs account for more than 60-70 percent of total costs, making layoffs nearly inevitable. All companies spoken to appear to be laying off 5-15 percent of their work force. Generally layoffs are occurring across all levels of the corporate hierarchy and many “first round” layoffs have already been implemented. As additional labor cost management, most companies are implementing net hiring freezes, and, faced with uncertainty, many companies are giving themselves flexibility through increased use of temps and contractors.

Even companies that didn’t have to – or where the effect is minimal – have reduced discretionary spending, including: limiting travel; using phone- and videoconferencing more; reducing conference and trade show presence; and eliminating employee perks. Interestingly, wage concessions are viewed as a place of last resort, and often limited to salary freezes at higher levels.

By now, most executives have moved beyond cost cutting to thinking about how to strategically capture opportunities offered by the recession.

“Most companies we interviewed are using the downturn to increase their efficiency and refocus on priorities,” said Booz & Company Vice President Narayan Nallicheri. “Some see opportunities for acquisitions, or to attract newly-available talent. And many companies see themselves emerging from the recession in a more competitive position than when it began. On the whole, Bay Area companies express more optimism about their future than counterparts in other regions globally.”

Bay Area companies are more aggressively pursuing external opportunities such as talent acquisition (54 percent versus 37 percent globally) and mergers and acquisitions (58 percent versus 38 percent globally).

Some companies are taking advantage of the recession to implement operational changes that are hard to make during good times with the rationale that during a recession, stakeholders are much more accepting of substantial change. Frequently cited examples included: consolidation of business units; full integration of past acquisitions; creation of shared services; centralization of decision making; renegotiation of union contracts; revamping compensation structures; cross-training and elimination of support functions; and, retirement of legacy IT systems.

Investments in research and development have largely escaped the cost reductions – even at financially struggling companies – and executives appear to be focused on fostering innovation despite the depth and length of the recession. Although venture capital financing has been dramatically reduced, underlying entrepreneurial activity in the region remains high. The Bay Area received a disproportionate 43 percent of all of U.S. venture capital in 2008. Most venture capital

firms and entrepreneurs do not believe future innovation and growth will be jeopardized by the recession, though much of the current innovation in companies is targeted at reducing cost.

The interviews covered a range of industries, but one stood out. Green technology is being heralded as the next big growth engine for the Bay Area. Global venture capital investments in cleantech have risen from approximately \$500 million in 2001 to \$8.5 billion in 2008. Last year, the majority of investments were made in the solar industry. Large energy companies, utilities and venture firms continue to invest in renewable energy and conservation technologies as fossil fuel prices are expected to rise post-recession and renewable mandates remain. Additionally, businesses generally continue efforts to raise their green energy profile, which is predominantly seen as a cost-saving activity. Due to the credit crisis, executives say the next generation solar power technologies will be more cost competitive. However, near term the solar industry suffers from an inventory glut and limited access to financing. Besides solar, executives say investments in “smart-grid” technology by utilities are growing strongly and will likely continue. They say the Bay Area is clearly advantaged in some aspects of cleantech, particularly those that leverage semiconductor technology (e.g. solar) and software (e.g. smart grid).

Executives also identified a number of public policy challenges that could either help or hurt their prospects for recovery and competitiveness: inadequate investment in education; overburdened infrastructure that causes traffic; a high cost of doing business; protectionist pressures that could hurt trade and immigration by educated professionals; and, weak policy coordination at the regional level.

Bay Area Council President and CEO Jim Wunderman called on the region’s leadership to meet the challenge of recession by redoubling its efforts to address these issues: “This survey finds that despite the pain our companies and workers are going through, we have the ability in the Bay Area to lead an economic recovery. To be successful in the long-term we need to meet these issues head-on.”

About the Authors:

The Bay Area Council Economic Institute is a public-private partnership of business, labor, government and higher education leaders that produces agenda-setting research and analysis, and works to support a competitive economy in California and the Bay Area. The Bay Area Council provides a united voice for hundreds of the region’s largest companies and its members employ more than 4.43 million workers and have revenues of \$1.94 trillion, worldwide. Booz & Company is a global management consulting firm that serves clients on over 30 countries. The report can be viewed on-line at www.bayareaeconomy.org.

About Booz & Company:

Booz & Company is a leading global management consulting firm, helping the world’s top businesses, governments, and organizations. Our founder, Edwin Booz, defined the profession when he established the first management consulting firm in 1914. Today, with more than 3,300 people in 59 offices around the world, we bring foresight and knowledge, deep functional expertise, and a practical approach to building capabilities and delivering real impact. We work closely with our clients to create and deliver essential advantage. Visit www.booz.com to learn more about Booz & Company.