

Should You Prioritize Growth or Profitability in a Recession? The Answer May Surprise You.



Opinions expressed by *Entrepreneur* contributors are their own.

This year has seen economic slowdown, inflation and war combine into a cocktail that's now fueling fears of a recession across business sectors, driving uncertainty in everyone from business leaders to investors to employees. Such uncertainty is forcing business leaders to reprioritize and scale back their once-ambitious growth plans. And now, as interest rates go up and valuations go down, more and more businesses are returning to prioritize what was once the only way to ensure a business's success – positive free cash flow.

All of this is a very strong reminder for all businesses, but particularly startups and small businesses, that it's vital to build a company to make money – in both good times and bad. Prioritizing free cash flow is the only way to manage against forces outside of your direct control.

Related: [Never Worry About Cash Flow Again by Using These 5 Strategies](#)

Positive free cash flow isn't a luxury

Many entrepreneurs, especially as they start their businesses, begin at a deficit. While this is expected ("You've got to spend money to make money," as the saying goes), too many businesses, especially in the last decade or so, have spent too long in the unprofitable growth stage. Many notable companies in tech are now faced with hard decisions with real consequential and disruptive effects, including dramatically curtailing investments and layoffs.

This recent and too-common strategy of sacrificing profitability for growth's sake can and has worked for some companies. Private and public capital markets faced with a low-interest rate environment have been heavily anchored on the high growth segments of the economy to deploy their capital. This capital glut has distorted long-term value drivers of business, i.e., the relationship between revenue growth rate and free cash flow margins. Given the valuation rewards, too many have solely built their businesses for high growth at all costs.

For most companies, prioritizing profitability and free cash flow should be seen as the norm. Many business leaders might be surprised that doing so doesn't materially impact revenue growth.

Speaking frankly, if you're running a \$100+ million organization that is just burning cash, it is a hobby. That doesn't mean leaders shouldn't invest in the business, it's simply a question of prioritizing investment with the goal of also generating positive free cash flow.

Businesses are meant to turn a profit. While Wall Street has recently been exceptionally forgiving to growing but unprofitable companies, this historically has not been the case. With extremely low interest rates since the financial crisis of 2007-08, there have been little to no penalties for taking risks on fast-growing but heavily cash-burning companies. The phrase TINA – there is no alternative – came about as a result of the extremely low interest rates providing a significant incentive for investors to chase growth without considering risk, as they had few opportunities to realize returns with lower risk. With interest rates normalizing, however, there are very real investment alternatives to high growth, and valuations for growth are down substantially as a result.

Now that we're trending towards a "normal" economy as interest rates return to something approaching long-term historical levels, it's time for business leaders to return to managing their business operations for these "normal" times. Capital access is going to be tougher now, and investors will demand more balance between growth and free cash flow after the initial phases of product-market fit are established.

Related: [How to Maintain Profitability in a Changing Market](#)

Prioritizing what's important

For small business owners and startup founders who have been less concerned with generating free cash flow and are looking to bolster their balance sheet, there are a few things you can and should do immediately.

First, you must determine the math that will allow you to control your burn. You and your team need to find a realistic revenue trajectory and break-even point. Without realistic expectations for your near and long-term revenue and fixed expenses, you and your team can never plan for responsible, realistic and profitable growth.

Once you have your revenue and break-even point, you should be able to figure out what you can plan to spend. Armed with that spend number, it's time for leadership at all levels to take a look at how their activities connect to revenue. This is where you need complete buy-in from your team and likely a significant change in mindset.

People get sloppy in good times, which we've all been fortunate to enjoy for the last decade. There's more room for experimentation when horizons are far out, but now as horizons shorten, pies shrink and forecasting becomes less sunny, business leaders must get ruthless about prioritizing projects that are driving revenue – everything else must be seen as a luxury. Projects outside revenue drivers will likely need to either operate off a slimmed-down budget and with more creativity or put on the shelf until sunnier days come.

Being honest is going to be important here. Be honest with yourself as the business leader about your growth and spending trajectories, with your team about what can and will be prioritized and with investors about what you're doing to generate cash flow. Setting these expectations will be key to keeping your employees motivated and engaged during what can be a stressful time.

Related: Positive Cash Flow and Smart Financing Solutions

Focus on productivity

As I've seen various economic cycles come and go, there are always two terms that seem to come back with a vengeance at

every downturn – efficiency and productivity. While there is nothing wrong with having an efficient operation, it seems to me that many companies and leaders only prioritize efficiency when times get tough.

Instead, I wish leaders focused more on productivity. For many, it will be a return to early startup days when teams were lean and scrappy. It's incredible what teams can do when focused on making the highest impact on the highest priority work. Get your teams focused and aligned on the right things, and cut out the low-priority items. You'll be amazed at what can be accomplished.

There is nothing wrong with making operations more efficient, but this can't and shouldn't be a short-term fix that goes out the window the second things look brighter, and neither should a focus on productivity. If and when we climb out of inflationary and recessionary periods, and your team goes right back to prioritizing growth over cash flow, you will likely find yourself in a similar situation the next time the markets begin to dip.

Related: Why Founders Should Focus on Productivity Instead of Efficiency

It is easier to burn cash than to generate positive free cash flow. That is to say, it's easier to defer hard decisions instead of making them now. If the last few years have taught us anything, it's that the future is unpredictable, and businesses – especially SMBs and startups – would be wise to shore up a safety net built on a foundation of profitability. Be realistic with your revenue and spending expectations, and prioritize projects that represent the best opportunities to drive growth and efficiency. This will enable long-term sustainability in good and bad times.

<https://www.entrepreneur.com/article/437540>