Financial Director

In Your Business Series: The Declining Business

n the fifth of a series of articles looking at companies from every phase from start-up to exit/sale Gary Jesson looks at the declining business

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AN ANTIQUATED BUSINESS MODEL, economic challenges and lack of cash can in a very short space of time, send a successful business into instant decline. While we have witnessed the high profile demise of major institutions and well-known brands such as Woolworths, HMV, Jessops, Blockbusters, Republic and the nationalisation of struggling banks, the SME sector has also witnessed this 'downhill' pattern.

Businesses however rarely experience difficulties overnight, hence if warning signs are spotted early, management is likely to have more options available to them to stop the decline or exit the business with some value intact, and hopefully jobs preserved. Some of these signs may include regular trading losses, declining cash balance, loss of a major trading contract, escalating costs, customers taking longer to pay, new and more agile competitors. If these warning signs are recurring, take advice from an insolvency or legal professional to determine whether there is any personal risk from continuing to trade, and whether any of the options below may be viable:

1. Consider turning around the business and make attempts to revive it. The magic formula to increase cashflow is revenue generation + cost reduction + working capital reduction. See steps 1-5 of the turnaround process below.

2. Choose to exit/sell part or all of the business but remember that the potential purchase price will be based on its current dire state not on any previous glorious value. For a potential buyer, stability, order book, customer base, and growth potential are values they will place a premium on and in the absence of this, you will have to be quite realistic about your expectations. In today's climate, the valuation of businesses for sale have shifted from a strong seller's market to a very strong buyer's market.

3. Call in an insolvency professional. If your aim is to save the business and start trading profitably once more, then this may be a good option for you. For insolvent SMEs, going into administration will give the company more time to settle their debts as they get a legal suspension of creditor payments while the administrator tries to raise capital or salvage the business. A range of cashflow improvement strategies can also be implemented.

As the administrator's aim is to maximise the returns for creditors, if turnaround isn't feasible after such activities as downsizing, selling off some assets and letting go of unprofitable lines, they may then decide to go for bankruptcy and get the best deal for creditors. While a company might be on the verge of going under, it still has intrinsic value which could be appealing to a competitor or to other strategic buyers.

One important point to consider is life after an insolvency process is not often any easier. Getting credit is difficult, opening bank accounts challenging, HMRC will track you more closely and customers cannot always be retained. Only use this as a last resort.

The Turnaround Process

Step 1- Analysis: Do the background work. What is the cause of the decline? What areas of the business are affected? What control do you have? What financial data do you have to make decisions? Why are sales falling? Are there any stars in the portfolio? What are competitors doing to impact you? Can you accelerate new products and services? Are certain geographies better than others - can you switch emphasis? After the analysis, implement the more successful ideas.

Step 2- Business Model Review: Answer this major question every day of the week- Is your business model antiquated? In the case of video rental company Blockbuster, evolving customer behaviour and trendy choices such as itunes downloads, Lovefilm and weekend television made its business model redundant and it was unable to deal with this evolution. Can you deal with the evolution in your industry? What are your options? What are your customers choices? If you can spot the risks early enough and start devising new or complimentary lines, you are one step ahead of the market.

Step 3- Cash Forecasting: Your cash flow forecast will reveal the depth of your cash hole and provide an indication of how much headroom/ breathing space you have before the business grinds to a halt. A forecast will also help to identify cashflow improvement opportunities. Get external help in preparing the forecast if you have limited skills within your company. Buy time using ‘HMRC's Time To Pay' arrangement, or trade supplier

payment plans. Focus on credit control, seek to collect cash more quickly and refinance assets.

Step 4- Cost reduction: Get rid of costs as fast as you sensibly can. Do not hold on just in case next month may be better. You may not be around next month. What product or service lines can be cut off? Under-resourcing can also be quite dangerous so be careful if reducing staff strength and watch out for key employees. Can you switch fixed staffing costs into flexible outsourcing or part time flexible solutions? Are you paying too much for your overheads eg Do you have too many phone lines? Are you over-insured? Do you order too much stationery? Can you email rather than post correspondence? Have you considered cloud computing which is scalable and secure? Choose services that can be scaled up or down as your business changes

Step 5: Improve sales/Bring in income: Invoice for everything when work is done not when you get round to it. Sell non-core assets, consider new routes to market such as selling old stock on eBay and recover old assets such as deposits.

In all of the above scenarios, it is unlikely that any management team will have the entire range of skills to help the company survive. Hence do not be afraid to buy in specialist skills as they will often more than pay for themselves. The survival price you pay will be small in comparison to the horror of losing your once thriving business.

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