performance through partnership

03

HOW TO AVOID BUSINESS FAILURE

cooneycarey.

There are three main reasons why businesses fail, according to accountants and business advisors, Cooney Carey. Most failures are a result of Financial, Trading or Management issues, or a combination of all three. If these problems are recognised and treated early, then failure is not inevitable, says ***Tony Carey,*** *Managing Partner.*

Cooney Carey has significant experience in corporate recovery and business structuring. In the third and final of three linked articles examining these issues, Tony draws on this experience. He also includes some sound advice from senior financial and banking experts, as well as the comments of Irish business people who have not only survived the current recession but have emerged with stronger businesses by following this advice.

The third article examines the most common management causes of business failure.

THE MOST COMMON MANAGEMENT CAUSES OF BUSINESS FAILURE

1. Lack of Management Skills and inappropriate structures
2. Inability to Adapt
3. Internal Culture
4. Inability to Communicate with key stakeholders
5. Lack of Objectivity
6. Excessive Personal Drawings

01. LACK OF MANAGEMENT SKILLS AND INAPPROPRIATE STRUCTURES

Management is a talent and a skill set, and constant updating and training is required.

Care must be taken to recognise that management might not know everything. For specific issues, where the knowledge is not available in-house, experienced advisors are essential. Management should be capable in managing the day-to-day activities, have a capability to design and implement strategy, but also to know its limitations and seek advice where needed.

During periods of growth people may have been promoted beyond their competence. Businesses have been created by people not capable of managing them. A typical example might be a carpenter who established a business during the property boom; as the business grew, the carpenter became the managing director – thereby removing the best carpenter from the business and installing a poor manager.

The management function should not be compromised by filling vacancies with people lacking the necessary skills for those jobs. Internal promotion may be the safe option, but if the skill set is missing the business needs the courage to source externally.

Structural defects include the presence of a dominant and autocratic CEO, a joint CEO, a combined Chairman/CEO role resulting in insufficient challenge to the CEO, an ineffective or unbalanced board of directors and a lack of management depth within the company.

Distressed companies are often characterised by organisational inertia and confusion. They are not able to make or implement decisions as a result of poor leadership or a poorly motivated workforce, poorly defined accountabilities and responsibilities and inappropriate organisational structures and management processes.

Any signs of a lack of consensus among the management team or neglect of the core business also evidence significant management weaknesses.

Key point here for me is Planning. The importance of planning on a weekly, monthly and annual basis is absolutely critical to future success.
Denis Bergin Head of Business Development- Bank of Ireland Business Banking

Pride can be a common pitfall – owners or managers not recognising that they don't know everything about the business
Seamus Carney Ulster Bank Senior Manager

02. INABILITY TO ADAPT

Sentiment and nostalgia can influence decision making - very often unprofitable customers, products and markets are pursued when they should have been dropped a long time ago.

If part of the business is going down the tubes, know the right time to exit and concentrate on new parts of the business.

The temptation to hang in too long will result in larger losses.

Some businesses are unwilling or unable to adapt to modern practices whether in marketing, production or technology, and this can very often lead to them falling behind their competitors.

In start up situations many new owners do not recognise the level of input and commitment that may be required to ensure the success of the business. They can't believe that irrespective of the fact that they are running their own business they will not change lifestyle habits e.g. working regular hours.
Seamus Carney Ulster Bank Senior Manager

03. INTERNAL CULTURE

Especially when times are tough there is a need for the culture and internal atmosphere in the organization to be right. Staff need to be motivated to be positive and to succeed. Without this motivation it is difficult to see how the business can positively interact with its customers and suppliers.

Lack of confidence in delegation can result in the principal trying to do everything including getting involved in relatively unimportant aspects of the business which can result in him neglecting the business essentials.
Seamus Carney Ulster Bank Senior Manager

To be successful in the 21st Century it is more important than ever for companies to have employees, colleagues and co-workers who are engaged, connected and committed to the organisation. Self-awareness and personal insight help individuals and companies build cohesion and organisational strength, allowing the business to focus on its primary objectives of success and growth. Next to sales and profitability, the need to retain and develop talent and mould it into a formidable, effective team is an imperative for every company. In a globalised, market-economy it is committed, aware people, realising their potential, that will make the difference.
James P McIvor, Managing Partner, The Thinking Lab

04. INABILITY TO COMMUNICATE WITH KEY STAKEHOLDERS

Trusted relationships and good communications with banks, trade insurers and creditors are an essential prerequisite in order to elicit their positive reaction toward the business if help is needed.

Bank and creditors are quoting instances where businesses behaved in an unhelpful and provocative manner in the good times and now that they need a sympathetic ear that is not forthcoming – the credits were not built up.

If a Bank feels that the business is untruthful (or not telling it what it feels it should know), the bank will likely lose faith and may look to disengage. The key issues are 1) transparency and 2) co-operation

Centre on good communication with banks and creditors to bring them with you and to enable them to react in good time if necessary
Kieran Moloney Bank of Ireland Head of Business Banking - Challenged

We have a case where a client is involved in the building of a retail network in the country but has lost the faith of a key stakeholder. The client is banked by 3 separate banks and has also brought in mezzanine debt to fund expansion. Client wanted the 3 banks competing against each other. We had belatedly suggested getting a formal syndicate going but client declined. We lost faith in client's bona fides and wanted out. Client also slow providing financial information and not providing us the full story. We are now managing a work down of our debt through asset sales largely, as a refinance is out of the question. Client's provocative approach has backfired big time.
Padraic Kiernan ACC Bank General Manager - Credit Special Asset Management

05. LACK OF OBJECTIVITY

It is always helpful to "bounce" ideas off advisors and confidants. The appointment of non-executive directors can be most beneficial.

This objectivity would help to address issues such as over gearing, over optimism, lack of confidence and risk.

Management's initial success leads to a belief that it only makes good decisions. Begins to take an aggressive approach to expansion (usually funded through additional debt) and then finds that things are not going as well as expected. There are probably loads of examples but we have one where a guy with a good established retail trade business locally, expanded into the UK by buying an existing comparable business through debt (on the strength of strong domestic cash flow) and now is struggling. Client thought that he could apply the same model in the UK as here but the market appears to be different and it hasn't delivered. He may have to sell at a significant loss to save Irish business. He would maybe have been better off expanding organically in local market.
Padraic Kiernan ACC Bank General Manager - Credit Special Asset Management

In a difficult trading environment we can be drawn into a very subjective perspective of our business. At these times the objectivity and wider experience of professional advisors can offer invaluable assistance in enabling us to review not only our financials, but also our trading and our general management of our business.
Brendan Flynn, Managing Director, Church Bar & Restaurant, Dublin

06. EXCESSIVE PERSONAL DRAWINGS

A proprietor and his/her family living beyond their means is a threat to a business. Personal drawings should not exceed profits. The prudent businessperson should ensure sufficient profits are retained in the business for future developments.

Company directors must avoid breaching Section 31 Companies Acts 1990 by drawing down company loans in excess of 10% of the company's net relevant assets.

If the bank discovers fraud or the client is untruthful (or not telling you what you should know) the bank immediately loses faith in the client and will look to disengage. There are many examples of this (largely in property development) where clients confirmed contracted sales only to instruct the solicitor to release them (unbeknownst to the bank) after monies had been advanced. The behaviour of the solicitor is also in question here. Bank will look to disengage or pursue enforcement of security.
Padraic Kiernan ACC Bank General Manager - Credit Special Asset Management

CONCLUSION

With proper insight, planning and implementation the risk of failure can be reduced, but not eliminated. There is no guarantee of success in business; however failing to plan is effectively planning to fail.

It takes imagination, resilience, energy and effort to build a business from scratch. The ability to take and manage risk, to imagine the future, to never take no for an answer – these are the necessary qualities for entrepreneurship.

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