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Germinating the seeds of success from other people's failure

A well-known business recently went into administration and last week I had the unusual privilege of attending a closing down sale in one of its' stores. Hardly surprising in the current economic climate you say, except this one was in a segment of the market that is often seen as recession proof – baby clothes and equipment.

I arrived quite late (15 minutes before closing) and was stunned at the scene that greeted me. Imagine this: You have been told that you can take whatever you want from a supermarket as this is the last time you will ever shop for food for the rest of your life. After the masses had passed through, the only things left would be tins of mung beans, used Christmas crackers and packets of lentil burgers in the frozen food section. Otherwise: desolation. Nothing. Just a few broken sugar packets on the floor and row after row of empty shelves.

This was similar to the sight that greeted us that night. Just a few packets of sheets, some toys of dubious quality… and a queue at the registers that was about 25 people long. Why?

The administrators had a 60% off sale on certain items to generate some cash and (presumably) to enable the store to close with minimal additional costs (such as what to do with remaining stock etc.).

> *After the masses had passed through, the only thing left are the tins of mung beans…*

The attraction of a bargain bought out a primal "SALE" urge in the baby shopping fraternity – something that if you are a parent I am sure you would understand.

The infrastructure requirements of a new born child are immense. A cot, a pram, clothes, toys, bath, more toys, stuff for mum (OK you can tell I'm a bloke) as well as gifts for friends kids... Then if you travel, you need a car-seat (perhaps 3 or 4 over the life of a child), a travel cot, stuff to keep them amused in the car that will not get you arrested...

Some studies quote the cost of raising a child to the age of 18 is around $1 million (the government thinks it will cost $385,000). Either way, Children typically are going to be more expensive than the house in which you raise them. It's a wonder the birth rate doesn't flat-line when you consider the cost of not only bringing a child into the world.

So how is it possible that a speciality retailer in a seemingly recession proof could fail?

The story is intriguing but not overly complex. The owners had a deal in place which had a number of conditions attached to it. The acquirer pumped in cash to keep the company running while the conditions were met. Shareholders approved the transaction. However, for some reason the deal fell through (possibly it was the inability to resolve debt funding issues – we'll find out as the administration continues).

So what was going wrong with a "recession proof business"? A quick scan of the financials reveals some telling insights which we all need to remember as we run our businesses day to day:

1. Just because your sell price for an item is higher than your buy price does not mean you make money. It costs a lot to keep a business running. Consider administration, taxation, marketing, depreciation of assets, interest on loans… they all add up.

2. While the balance sheet might show the company is solvent (i.e. assets are greater than liabilities), it typically includes stock (at full value), as well as the current depreciated value of fittings and fixtures. These numbers can be misleading, especially when deep down you know full well if you had to sell this stuff it would be at a deep discount to the value shown on your balance sheet.

3. Debt can kill a business. When the value of your inventory nearly matches your current liabilities (i.e. trade and other payables, plus finance costs), regardless of whether you sell stock at full price, you will be unable to make enough money to pay your debts, staff, rent etc

4. Try to your administrative costs lean. In this case, administration costs seemed high, even after head office wages were stripped out.

5. Be careful not to use your business as an endless source of cash for things that don't generate revenue. At times it might be tempting to over-engineer solutions or buy a system in excess of your needs (both currently and into the 3-5 year future). If things are going well, you want to reward yourself. A great example is up grading a perfectly good mobile phone or to replace office equipment. Make sure you are doing it for the right reason, not just to make yourself feel good. While "treats" are OK – just remember that you need to keep a reserve of cash as things may not always go as well as you hope… and you need to be ready for that.

Remember, discouragement and failures are two of the greatest stepping stones to success

6. Don't instil practices you are not comfortable with in your business. This shop had a price match guarantee – apparently without limits. Fine. But can a bricks and mortar really compete against an internet only business? Ensuring you have a clear policy on what you do and don't do will help you avoid being cornered into selling a product below your minimum price. If you can't sell because you'll lose money – be honest with the customer and tell them. Customers may not be factoring freight and convenience in their calculations. If a customer is in your store they usually have a desire to purchase. Use your skills to show them why it makes sense to buy off you today, rather than save a few dollars only to wait for delivery and have no after sales service.

It is often said that the best lessons come from failure. So the next time you see or hear of a business which has failed, think about what you can learn from it. Remember, discouragement and failure are two of the greatest stepping stones to success. *(Dale Carnegie 1888-1955 – the author of how to win friends and influence people).*

Accretive
PO Box 756 | St Ives NSW 2075 | AUSTRALIA
www.accretive.com.au