REPRINT | FINANCIER WORLDWIDE MAGAZINE

FINANCIER WORLDWIDE corporatefinanceintelligence

REPRINTED FROM:
DECEMBER ISSUE 2011

Plus ça change

BY DAVID BRYAN

As we approach the end of 2011 we have been living with banking problems, recession and Eurozone problems for over three years. There are few days when there isn't another dramatic headline regarding a financial or economic problem. But is this constant flood of bad news making us all a bit punch drunk? Are business leaders thinking *"plus ça change, plus c'est la même chose"?*

One of the counterintuitive features of the last few years has been the remarkably low number of business failures. There was an increase in late 2008 and early 2009 as the very weakest went to the wall quickly but since then the figures have fallen back to levels broadly comparable to pre 2008 numbers. Even these have been concentrated in certain sectors, particularly retail and construction. The usual working of the capitalist system whereby the weak are culled in a recession does not seem to be happening.

There are many reasons for this. Without a doubt, businesses were quicker than in past recessions to cut costs and adjust to the economic downturn but many external factors have helped. Record low interest rates have played a significant part and for a while, HMRC's 'Time to Pay' policy also helped. Add to that a banking sector that has been very reluctant to do anything that might make a loan non-performing and conditions have been unusually benign. So much so that business may be getting a little too used to it.

Predicting the future in these uncertain times is almost impossible with any accuracy. At the time of writing there looks a very real prospect of a double dip recession. Further down the road, some things are certain, even if we don't know the timing. At some point interest rates will have to rise and at some point we will return to more normal levels of economic growth.

A further drop in demand will be very difficult for many businesses. Costs have already been cut and the room for manoeuvre is getting smaller. Similarly, the start of an upward cycle in interest rates will hit hard. With current rates so low, a relatively small series of upward movements will represent a large percentage increase in actual interest charges.

Eventual recovery in demand will increase working capital requirements and is often a painful period of change for all in the supply chain. It should be remembered that in past recessions many more companies went bust in the recovery phase than in the recession itself. The recession of the early 1990s lasted for five quarters. The peak in business failures was not until two quarters after the end of the recession and it was several years before the level of business failures returned to pre-recession levels. The road ahead looks rocky indeed. How should businesses be positioning themselves for the journey ahead?

The time for planning and change is now. Not when the crisis starts. It is surprising how many businesses of all sizes do not forecast outside the status quo to see what would happen if there are significant changes to certain key assumptions. Just how bad would the effect of a large fall in demand be? What would be the impact of losing a major customer? How would a series of interest rate rises affect the business? How much additional working capital would a significant recovery in demand require? Should we merge or should we sell? Should we retrench further or should we refocus? If the business is approaching a refinancing, what is the likely reaction of current lenders? What would be the effect of some of these happening together?

Far too many businesses are bumping along the bottom, just about making ends meet. They are in survival mode, rushing around dealing with the day to day problems and rarely giving much thought to the future beyond the very short term. Such businesses are unlikely to survive when the bigger changes come.

For most management teams it is hard to contemplate such future events and many will choose not to until they have to. By then it will often be too late. Those that do have little experience of distress and are unable to understand what will happen and what their options are because it is unknown territory. Management are often blamed for getting a company into difficulties. Whilst bad decisions can easily be identified it is often their inability to correct those decisions and change course that is the real cause of their predicament.

Time and again, turnaround and restructuring professionals see situations which have been allowed to drag on far too long. And yet, with the help of robust analysis, no sacred cows, a willingness to think the unthinkable and the steel to negotiate the seemingly impossible the business is rescued and recovers. There is no substitute for independence of mind and experience; outside help before a crisis erupts need not involve huge expense and disruption. It is often the catalyst a management team needs to help find the solutions to its own problems and prepare the business for what lies ahead.

In addition a well communicated course of action will give lenders a great deal more confidence. These days, banks are more enlightened

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and see insolvency as value destructive and a last course of action. A good business, with proactive management and a robust plan will get the support of lenders.

In 1513, almost 500 years ago, Machiavelli wrote in the The Prince, chapter 6 of the difficulty of change. His words still ring true today: "And it ought to be remembered that there is nothing more difficult to take in hand, more perilous to conduct, or more uncertain in its success, than to take the lead in the introduction of a new order of things. Because the innovator has for enemies all those who have done well under the old conditions, and lukewarm defenders in those who may do well under the new."

Nobody would pretend it is easy being a business leader. Nothing is more difficult than fundamental change. But change is necessary and change is good and the eventual recovery from the current economic and financial turmoil will be characterised by those who managed it and those who didn't. ■

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