Identifying the Tell-Tale Signs of Trouble in Your Busness

By Carter Pennington

In times of uncertainty it can be hard to grow your business. The current economic downturn has meant that more and more businesses are struggling to be successful and make enough of a profit to develop in any way. The current economic climate has led to a significant increase in the amount of business owners turning turnaround consultants to help save their companies and improve finances.

Nowadays, it is not unusual for savvy business owners to enlist the help of a turnaround professional to identify strategies that will aid recovery and help get the business back on the straight and narrow. Not all businesses will necessarily need the help of a turnaround consultant, but it is important to be aware of the distinct symptoms that will become clear when your business is in trouble just in case. These may not be obvious immediately, however once a turnaround advisor gets to work they will be able to show exactly where things went wrong.

Here are some of the tell-tale signs that your business is in trouble:

Cash and liquidity

The most important sign of trouble is paper-thin cash flow and liquidity. If your business is generating just barely the minimum level of cash, on a week-to-week basis, the company is like in serious trouble and potentially heading for disaster. The same is true with liquidity; liquidity is the combination of available cash and available debt, usually a revolving credit line. When cash flow or liquidity problems emerge, it is time for immediate corrective action.

Unfavorable trend in working capital ratios

A downward spiral of one or more working capital ratios usually means trouble. The good news is, by regularly monitoring the company's working capital ratios you will have ample time to make to address the underlying problems that may be causing this trend. Unfortunately, most CEOs tend to either ignore the key working capital ratios, not understand them or do not place enough importance on them. A few examples include: DSO, DPO, DIOH, Working Capital to Assets, EBITDA to Working Capital and the Basic Defense Interval. While the absolute value of these and other ratios are important, far more important is monitoring how they change on a weekly and monthly basis.

Managerial denial

You might say this is the opposite of the previous sign; ratios are analytical and absolute, denial is behavior and judgmental. When companies get into trouble, management usually is in denial of the realities of the business. The company could be disintegrating around them but they simply refuse to accept it. 'Hope springs eternal,' most CEOs believe the company will recover with the next big customer, the new product line, an improved economy and just the steadfast believe that somehow, sales will miraculously increase. I believe managerial denial is one of the best and most reliable tell-tail signs of trouble; unfortunately, by definition, it is extremely difficult for a CEO to identify this sign.

This is a powerful took for a professional turnaround advisor. Not only does a turnaround professional have specialized skills and experience in this area but they are 'outsiders;' they quickly see what is often invisible to the CEO – managerial denial.

The downward spiral

In many cases, the first sign that things are going wrong is a continual decline in business profits. Some business owners may pass this loss off as a reaction to market conditions or as the natural highs and lows of business, but it might be more than this. You may be able to sustain this loss in the short term but if the decline turns into a pattern then the business will really start to suffer. If strategic and speedy corrective action is not taken then the business could fail in the long term.

Short-sighted planning

If as a business owner, you have no strategy or long term plan then you are potentially setting yourself up for failure. If it is the norm to only deal with immediate concerns and not the bigger picture then it will quickly become clear that this approach is not sustainable. A business that lacks direction is potentially risking the success all aspects of the company, from customer service to employee morale which can result in a financial loss.

A one-off event

As a business owner, you can't always control what happens to your business and it may be that an event out of your control can cause problems for you. A good example of a none-off event is the financial disaster of 2008 – 2009; you can't control it but you can and must react to it in order for your company to survive. Such an event may require the business to re-focus or come up with a new plan of action in order to stay afloat. A one-off event could also be something like a large customer going out of business or the cancellation of a lucrative contract. These events could have a knock-on effect on the health of the business and could require the help of a turnaround expert.

Conclusion

Over 30 years of experience with distressed and underperforming companies have shown me that there are significant similarities in managing these types of companies and the Kubler-Ross Model of how people manage personal grief. Based on this Model, people go thru 5 sequential stages of grief: *denial, anger, bargaining, depression* and finally *acceptance*.

We already briefly discussed denial as being one of the best tell-tail signs of trouble. Notice how denial is the first sign; by identifying managerial denial, the CEO is likely well-ahead of the underlying problems with the company. Some of the more analytical signs of trouble can be compared to the *anger* or *bargaining* stages.

Unfortunately, most turnaround professionals are brought in at the *acceptance* stage; this is often very late in the process, leaving the turnaround profession with only a limited options remaining to save the company.

When trouble is on the horizon, time is your enemy – don't wait for the *depression* or *acceptance* stages to arrive before seeking professional help. Look for the early signs of trouble, fess-up to reality and seek professional turnaround advice at the very first signs of trouble and success will follow.

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