

## DOING A SME TURNAROUND RIGHT

In a turnaround situation, too many small business owners rush to apply short-term fixes rather than diagnosing the real problem.

These short-term solutions are generally only 'band-aid' actions which, whilst succeeding in buying the business time, don't solve the underlying problem and can often lead to a worse financial outcome for the owners later.

The true and only long-term solution is to identify, harness and magnify a business's competitive advantage and overlay this with employee engagement.

### Trying times highlight a company's weaknesses

Hundreds of SME companies find themselves in financial distress even under the most buoyant economic conditions. This number is magnified tenfold during periods of economic contraction or stagnation. Underlying problems in core business models are intensified during these periods.

### The Balance Sheet is the indicator not the cause

Many SME's facing financial difficulty, which is only reflected (and not caused) by issues in their Balance Sheets, seek to borrow or refinance their way out of trouble. This finance-first approach is short-sighted at best and fatal at worst. Whilst a refinance is helpful for placating hungry creditors now, it does little to guarantee long-term cash flows and operational stability.

This could also include the restructuring of their business through a 'quick-fix' phoenix transaction in order to 'repair' the Balance Sheet, which is often marketed to SME's by some pre-insolvency advisors.

There is a reason why few (if any) large or medium sized corporates are involved in phoenix activity.

The phoenix may falsely repair the Balance Sheet of the sick company by inserting the business in a fresh skin, but the inherent and unaddressed weaknesses in the previous operating model are also transplanted.

It is not uncommon to see a phoenixed business fail in the following two years as it repeats the failings of the past.

### Future prosperity is hidden in the Profit & Loss

Most SME's that we encounter have fundamental flaws in their core business. It is the identification of this flaw and development of a turnaround plan to address this that is critical to long-term prosperity.

Whilst larger companies may have their problems rooted in a diversification into unprofitable side ventures, SME's rarely have the capital necessary for these intensive ventures.

While cost-cutting can help to achieve a cash-neutral or cash-positive position in the short-term, it won't solve deeper structural problems facing the core business.

The launching of a new product or entry into a new market is also not the way to return to profitability. Unprofitable growth in a flawed business only magnifies its already existing issues.

### Can a turnaround of an SME occur?

Whilst the short answer is yes, many don't have the time, money or mental energy to enable a plan to work. An operational turnaround cannot be bought with optimism and good intentions. Nor can you make a silk purse out of a sow's ear.

If there is no clear competitive advantage upon which to build a realistic recovery plan, then a turnaround is going to be difficult.

An effective turnaround involves a combination of short-term and long-term decision-making, which must be executed quickly and communicated clearly.

All of these decisions must be focussed on the end-game. Owner engagement with their staff through open and regular interaction during this phase leads to maximum performance outcomes.

## What will a turnaround look like?

The first step taken in a turnaround is to identify the company's competitive advantage. This could range from having a superior reputation for customer service, support or expertise to retention of exclusive contracts, products or licencing deals.

### We can assist in this process.

Working with the staff and addressing any resistant behaviour (incl. potential new work ethic and environment) is the next task on the list. Whilst the focus initially will be upon securing short-term wins to address cash flows, this will quickly change to activating profitability drivers.

Implementation of the agreed plan through continual communication with stakeholders (primarily the employees) is an essential element to the delivery of sustainable profits and culture shift.

## One Shot?

Owners of SME's often only get one real chance of affecting a turnaround. This is because many find it necessary to use the equity in their homes or rely upon advances from others to provide the funding necessary to meet both the ongoing losses being incurred and turnaround/restructure costs.

If a false turnaround is attempted via a phoenix, as discussed above, when the newly birthed phoenix company fails the owners then lose their business, their homes and their reputation.

Sometimes the best plan can be to let the business die so that the owners themselves can start again.

Turning around any company is often difficult, disruptive and sometimes unpleasant. However, through our involvement, proper strategic planning and consistent decision-making, even the sickest of companies can hope for a recovery and a long, prosperous life.

## Early advice

Any turnaround requires time. For SME's who are in need of a restructure, early consultation with an expert, such as Brooke Bird, is vital.

Many SME's come to seek assistance only when the bank account is empty, creditor goodwill has evaporated and staff relations are at an all-time low. A turnaround against such a backdrop is potentially only achievable through a formal insolvency process (via a Voluntary Administration) but even then the Administrator will require something to work with.

If you are in receipt of a restructure offer from an 'ambulance chaser' advisor, then it's already too late and chances are you are going to be sold a phoenix.

Early engagement with us allows for maximum opportunity for an effective turnaround plan to be developed and implemented.

This plan may be an informal workout or through a formal insolvency process, such as a Voluntary Administration with a Deed of Company Arrangement proposal (potentially funded by the owners).



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