

the Credit Crunch



Whilst I do not want to add to the woes of our pitiful economic affairs, at least dear reader you cannot blame me for not being topical.

Having tried desperately to avoid becoming morose and disenchanted with life, unfortunately at every turn the modern media is berating us at an ever-increasing pace into financial depression. Mr Brown's multibillion lending to the banks and his retrospective encouragement of them to pass the benefit back to ourselves from our own hard-earned tax money has yet to really sink in. The clearing banks, which whilst very happy to accept the handouts, seem stuck on trying to make as much money as they can from businesses, squirreling away the benefits they should be passing on.

For those that have been shut off from all forms of media, below is a brief overview of why we are where we are.

Due to the fallout from the subprime US market, credit markets have started to worry. The subprime mortgages were packaged up and sold on to anybody who would have them basically and then unfortunately, due to a rise in mortgage arrears, those packaged products started producing increasing losses. The economic climate then fanned the flames with increased interest rates, falling house prices and the inability to refinance as quickly as one could have done previously. A major lack of trust started flowing through the financial world with a lot of institutions believing that if the subprime loans were doing badly then perhaps other structured products of any type would also fail.

To the likes of you and me in business it simply means that the banks are putting the squeeze on lending, trying to maximise their charging structures, freezing overdrafts or at worst calling in their facilities. Deals are slowing down and the purchasing power through loans and mortgaging is drying up. The ability to generate cash flow has never been more critical when external sources of finance have become a non-option.

Personally I have never had much trust with any of the banks in the first place and therefore I can sympathise with their lack of seasonal feelings towards their fellow institutions. One thing is for sure; we will be in this predicament for some time to come.

All that being said where does it leave your average business?

A lot of businesses will slow down payments to suppliers, and the cleverer ones will chase up payments owed to them.

The extension of lines of credit effectively means that if you are not one of those in control of your aged debt – then you will be paying for another company's overdraft in simple terms. The banks with their ever increasing appetite to make more money (or as they would have it pass on the pain of more expensive borrowing) will put up your rates. Obviously if you are not borrowing as much, then you will be paying less back to them.

What is in every business' power is to actually sit down and analyse the aged debt – knowing "who owes you" is not as important as knowing "when it was owed". Considering your own aged debt profile and trying to minimise your debtor days (0 – 30, 31 – 60 or 61 – 90) is absolutely critical at present. Try to reduce the percentages in the different categories of time. Of course a lot of financial institutions are offering facilities and capitalising on the fact that you cannot bank on traditional finance and they will have a good pitch at you accepting debt and speaking to their expert. Personally I am not convinced and inevitably such credit card financing does not actually resolve problems that are obvious, and more importantly, in your control.

As a simple guide your aged debt profile should be looked at very carefully and telephone calling used to chase the money – literally. This is more cost effective and quicker than writing a letter and cuts down on administration etc. As such if your category 31-60 days is increasing in size – your credit controller could be deployed to take action against that group of debtors. If an increase of cash flow is necessary immediately, then your 0-30 days should be targeted. What is obvious though is if you aren't looking at it – nobody else will be!

One thing that is for certain is that if a debtor is appearing in each time category and you are carrying on supplying services/goods to that company, then something has gone fundamentally wrong as you are working for nothing and the odds are that ultimately you might not get paid for whatever you are doing. You are therefore wasting your time, and if a debt is of a large amount and outstanding for any real length of time, then decent solicitors should be deployed after your own efforts have failed to recover the debt as soon as possible.

As one client has put it – the phone should never be put down. He wasn't referring to 0898 numbers either!

May we at Milners wish you a prosperous New Year and hopefully 2009 will see the banks and our government make life a little easier for us all.