

Opinion: Why businesses fail and how to fight it

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Eighty percent of small businesses survive the first year. That may be surprising, considering the commonly held idea that most businesses fail within 12 months. However, the longer the business is in operation, the more the viability decreases. The five-year mark is when half of small businesses fail, according to Forbes. From there, the likelihood that the business survives to see year 10 drops to 1 in 3.

Several issues can contribute to the failure of a business, but uncontrolled growth and a lack of succession planning are both causes that can be prevented.

Uncontrolled growth

Uncontrolled growth is a major reason companies fail, and that can happen at any point in the lifecycle of a business. It is common for business owners to inaccurately assess opportunity, whether it's a new line of business or a new helpful resource through a vendor.

In 2018, the most commonly cited reason for small-business failure was the lack of need in the market. Therefore, to be a successful business owner, it is important to constantly keep a finger on the pulse of the market you serve.

Benchmarking can help. Develop relationships with peers and use accountants and bankers who can assess whether a business is able to sustain growth. For example, a subscription to the Risk Management Association can offer industry standards and a group of industry peers that business owners can bounce around ideas, solicit advice or get different perspectives.

Owners should analyze vendor partnerships before jumping into a new phase of growth. A vendor might tell a client they are able to support its growth, but in actuality aren't be able. Before sticking with the same vendor as they age into growth, the management of the small business might want to ask for financials from key suppliers to analyze whether they are able to meet the increased demand.

Cash flow and timing should be examined as well. Cash flow is the largest determining factor of a small business' success or failure. When business experts talk about cash flow, they are not only referring to how much money the business has overall, but also the timing of the cash inflow in relation to the cash outflow. Before a company opens its doors for business, there should be a plan in place for managing cash flow and creating safety nets for times when business is slow.

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Lack of planned succession

Poor and nonexistent succession plans are another reason businesses fail. Business owners need to have a plan in place for the transfer of ownership to the next CEO, whether that person will be a family member or an employee. If there is no succession plan, a business owner has no say over the direction of the company when they decide to retire or a worse-case scenario happens, like death, disability or illness. In the latter case, the business will be directionless and at higher risk of failure. Family members could be forced to sell the company and be shortchanged on the value of the business.

The first step in building a succession plan involves finding a trustworthy financial adviser. The job of a financial adviser is to bring all business players together to make decisions, including current business owners, supposed heirs, attorneys and tax advisers. Because succession planning can be a highly emotional process and requires cooperation from the next generation of company leaders and current major stakeholders, business owners should choose an adviser that mirrors their values and understands their business makeup.

An adviser is especially key in family-owned businesses or businesses where there is a family member set to assume ownership of a company. In these cases, it can be difficult for the owner to determine where the distinction between inherited wealth and business transfer lies. However, the major trademark of a successful succession plan, and what an adviser knows well, is the plan's ability to be executed. This requires planning before the drafting of the plan even begins. It is key to identify the people, resources and timelines that are central to the business. Craft the plan with those three factors in mind. Having an exit strategy attached to the succession plan is also crucial in making sure the execution process is as simple as possible.

Small businesses take a lifetime of hard work to build. Establish the right key players, both inside of and outside of your small-business team.

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