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Survival of the fittest

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A briefing from our Dispute management team

David Murray, a lawyer and insolvency specialist discusses the impact of the continuing harsh economic conditions on high street retailers.

With Christmas and the January sales accounting for an estimated 23% of annual retail sales, the last few weeks have been a critical time for High Street retailers as they look to combat the effects of high unemployment, weak consumer confidence and the crisis in the Eurozone. What's more, the unseasonably warm weather means that many of us haven't been buying traditional winter items and the increasing popularity of online shopping leaves many questioning whether the days of high street shopping might be numbered.

Blacks Leisure, Barratts and La Senza are just a few of the high street names that have kicked off the New Year by going into Administration. Increasing pressure on margins and spiralling costs created a perfect storm from which they were unable to seek shelter without entering into insolvency.

With quarterly rents due again in March, many other retailers face the prospect of a bleak future as Banks may wait for cash to come in from the Christmas and Sales periods and then seek to reduce their borrowing exposure before the next quarter's rent is due on 25 March 2012. It is then that we could well see other big high street names facing further substantial issues of financial viability and possible insolvency.

It is easy to understand the temptation in the current climate for the retail sector to reduce margins and start drastically cutting prices to shift stock and increase cash flow. Indeed one had only to walk down any high street in the country before Christmas to see "Sale" signs not normally observed until after the Queen's speech. Such discounting may increase cash flow and indeed will have enabled a few high street performers to gain some invaluable breathing space. However at Morgan Cole, we caution against panic and the short-term temptation to drastically reduce prices to sell stock. There have been winners and losers on the high street this year and they are not necessarily those who engaged in the most draconian price cutting exercises. Rather those who have survived and may prosper in the future are those who took a more holistic approach to their business. The right business structure is absolutely paramount during these difficult times. This starts with taking expeditious, proactive and protective steps to limit exposure to the vagaries of the economic cycle.

Companies with healthy cash flow, low debt levels and sustained customer demand will survive; conversely retailers facing a cash squeeze, large debt burdens, faltering sales and - particularly those with expensive and large store portfolios - will face a tough time.

With the cushioning effects of suppressed interest rates having worn off, persistently worsening consumer spend is starting to crystalise in business failure. Unfortunately the fundamental economic indicators suggest that retail insolvency figures are likely to continue to worsen this year.

This may be the worst trading environment for years but help is available and that is why our approach at Morgan Cole is always to work closely with our clients, their funders, advisors and landlords to safeguard the long-term future of a business. Of the utmost importance is to have created a coherent but flexible strategy. To rely merely on historic practices and "feel" for what will work in these uncertain times is to increase the chances of insolvency. As Winston Churchill said, "He who fails to plan is planning to fail". Any strategy should be kept under constant review and have the buy in of all stakeholders in the business. Strategies which appear to have insulated many retail businesses from the worst effects of the downturn include adopting a multi-channel approach to selling. Prime examples of this approach include Next who saw poor high street income but soaring income sales from Next Directory (up some 16.9%) and John Lewis who bolstered good high street income (up 6.2% - frankly excellent in the current climate) with sales derived from johnlewis.com up a staggering 27.9%. Businesses which survive will also have a renewed focus on self-help. This might include product development and additional marketing, where appropriate, as well as tough negotiation with suppliers and landlords to improve payment terms.

It is imperative that retail businesses (and indeed all businesses) are proactive in their approach to the downturn and act swiftly. In particular it is not necessary to deal with the current harsh economic situation in isolation. Seek out professional advice, critically examine your core business, premises and employees. Those who are simply reactive to and follow the market are those most likely not to be around next Christmas. 2012 really will be a year when we see the survival of the fittest.

More information

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