

Beware of trading into insolvency

The present pandemic has created just the right conditions for certain businesses to trade their way into insolvency.

As we start the gradual withdrawal from lockdown, consumers will be on the lookout to spend after months of enforced “house arrest”. This will likely fuel an increase in economic activity on an unprecedented scale as we bounce-back towards pre-pandemic levels.

But isn't this good news?

Under normal circumstances, yes, this is great news, but unfortunately, many businesses have needed to spend reserves and borrow in order to survive the last fifteen months of COVID-19 disruption. It is like they are standing on the starting line for a marathon, wearing slippers; unprepared financially for what is about to unwind.

Does your business fit into this category?

- Cash reserves are limited.
- Losses have stripped away accumulated profits.
- You are obliged to offer better terms of trade to your customers than you receive from your suppliers, for example you sell goods on 60-days credit terms but pay your suppliers for raw materials as cash on delivery.

But why does this matter if sales are profitable?

When you sell goods on credit – 60-days in our example – for those 60 days you will have to pay suppliers and other overheads, wages, rent and other costs, before cash arrives in your bank account for sales made almost two months ago.

Ironically, the more successful you are in creating new sales, the more damaging this funding crisis potentially becomes. In accounting speak, you will be over-trading.



Planning is critical

If your business fits the description that we have outlined is imperative that you plan your business growth. It may still be possible to manage higher sales, as long as you organise cash-flow support to fund costs until higher sales - and therefore retained profits - provide you with the resources to self-sustain future growth.

No business owner should have to suffer the financial tragedy of over-trading through lack of planning. Contact your accountant who will be able to advise you through this strategy.

Published in the Wigan Observer 18th May 2021.