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CONTROL THE CONTROLLABLE - FOCUSING ON FINANCIAL MANAGEMENT

Michael Neary, a corporate finance partner with Grant Thornton, highlights the importance of practising and maintaining the key principles of sound financial management to help ensure long-term sustainability of your business.

Cost control

Firstly, the control of costs is an essential aspect of a business in the Motor Industry. In this economic environment, effective cost management is a priority to ensure profitability is maintained. With higher competition in the marketplace, there is growing pressure on management's margins. To counteract this, businesses need to focus on minimising their costs as much as possible. Reviewing fixed and variable costs will enable members to cut costs in the short term while at the same time building a more efficient operating model over the long term.

While the current focus is on cutting overheads, management should not be taking decisions that hinder their long-term prospects. Cost cuts should be reviewed very carefully in terms of their value to the business. While many organisations have cut costs recently due to year-on-year declines in the number of car registrations, it may be worthwhile to consider a review of overheads including insurance and utility providers as there may be further opportunities for value.

KPIs

Businesses in the motor industry need to consider performance through a series of key performance indicators (KPIs). These indicators will tell you how your business is performing against prior years and against budget. Fundamental KPIs could include revenue, gross profit, EBITDA margin and interest costs.

A revenue KPI is useful to show if sales have surpassed budgeted figures but also where your company stands within the industry. Gross profit is key for assessing the profitability and financial performance of the company and is useful in assessing the efficiency of your management team in terms of using labour and supplies. The EBITDA margin may show that certain operating costs are increasing disproportionately in comparison to the overall business. Interest costs also have a strong impact on the profitability of a business.

A review of your debt obligations may highlight that you do not have the appropriate debt mix (i.e. too much short-term debt, permanently in overdraft). Overall, businesses should focus on strengthening their profit position to ensure they have a level of headroom, so growth and profitability can be achieved in future operating periods.

Cash flow control

Cash is the lifeblood of any business. During any period of difficult trading, the ability to manage cash flow on a daily basis can be crucial to the survival of a business. It is important to assess cash flow requirements before they arise, and to plan to meet these in the most cost-effective manner possible. For example, collecting accounts receivable promptly should always be a priority, but it is especially important during a slow economy, when everyone is holding on to their money a little longer. Your customers are getting paid more slowly, so they pay you slower. As a result, cash will trickle into your business, potentially resulting in you being unable to pay short-term costs.

In order to make sure the company maintains sufficient cash flow to meet short-term operating costs and short-term debt obligations, each business must have a good working capital management policy. If businesses are maintaining margins and managing their working capital efficiently, this will translate through to cash flow, thereby allowing you to reinvest and expand your business.

According to information on the AA website, 'for every new car bought in Ireland almost 2.5 second-hand ones are bought'. This is having a profound effect on the Irish Motor Industry, and is a trend that many in the industry will need to take note of, Vehicle Recovery Operators and Vehicle Testing Network businesses in particular. These businesses will need to stay vigilant and proactive in terms of cash flow control, given the potential for a fluctuation in demand.

Maintain a good relationship with your bank

The importance of nurturing open, upfront relationships with financiers is well accepted by SMEs. This relationship will be enhanced by the quality of information provided to the finance provider, and the ability of the company to establish credibility by matching plans and promises with performance. Where unexpected difficulties arise, banks should be informed immediately to allow both the customer and the bank to work together to address any issues.

Brexit

The short-term impact of Brexit on the Irish car market has been mainly felt through the currency change, which has put pressure on the used car market however, the long-term effects may be significantly different. The long-term effects of Brexit still remain mostly unknown as they are dependent on an agreement between Britain and the EU over market access and trading rights. This could result in a strengthening of second-hand car prices in Ireland as trade costs counteract the benefit of a weak sterling. In other words, potential trade barriers between Ireland and the UK could make it more difficult and expensive to import cars into Ireland. While there is no certainty in what Brexit will bring, the uncertainty itself presents perhaps the greatest challenge to the Irish Car Market.

Overall, it is important for the Industry to stay wary of the drop in new car registrations, which is set to continue for the rest of the year, and to adhere to a good financial management policy by:

- maintaining sufficient working capital;
- implementing effective cash management; and,
- staying proactive.

In a situation where only the strongest will survive, businesses should seek to adjust to the current marketplace, while having a full understanding of their cash flows and costs.