Common Reasons Why Small Businesses Fail

Introduction

It takes a great deal of hard work to set up and run a successful small business. You will not only need to sell your product or service, but also manage the administrative aspects of the business.

In the UK, three out of four business start-ups will not get off the ground at all, and around half of those businesses that do start up will cease trading within 12 months.

By understanding the issues that can cause a business to fail, you are more likely to avoid the pitfalls, and this will increase the chances of your business surviving beyond its first year.

This factsheet looks at some of the common factors that could cause your business to fail and provides some suggestions on how these factors could be addressed.

Lack of skills and qualifications

Anyone planning to start a new business will benefit from training in general business and enterprise skills, but many business owners ignore training because they cannot spare the time or the money.

In some sectors or professions, you must have formal qualifications or certification in order to operate, but often the business owner and staff are not required to undergo any specific training or have any qualifications.

This does not mean that training should be overlooked. Factors that can cause your business to fail include:

- Not having the right skills, qualifications or experience to run a business.
- Not going on any training courses to help you understand marketing, finance, recruitment, etc.
- Getting out of your depth and not learning any new business skills.

Little or no market research

Many business owners make the mistake of making or selling a product or service for which there is little or no demand. You will not have all the information you need about potential demand for your product or service if you don’t do sufficient market research before you start your business.

Failure to undertake sufficient, detailed market research can result in poor sales and can cause your business to fail.

It is vital that you research the following, well before you make the decision to start trading:
• Where your customers shop or buy, how often they buy, and how much they spend.
• Your competitors - who they are, who buys from them, and how they are different from you.
• The trends and issues in your business sector or industry - is the market growing or in decline; are there any external threats to your industry?

You need to be sure that there is a market for your product or service and that there will be sufficient demand for it. This means finding out who else provides the same or a similar product or service and how you can meet customers' needs better than your competitors. Is there sufficient demand in the market for another provider? Are your prices higher than the market can bear?


No clear marketing plan or strategy

New businesses frequently fail due to the lack of a clear marketing plan or strategy, especially if insufficient customers are aware of, or prepared to buy, the product or service on offer.

All businesses need sufficient customers and sales to enable them to cover their costs and make a profit, but customers won't come to you unless they know about you, your product or service and what benefits it will give them.

If you do not have a clear marketing plan, you are at risk of making the following mistakes, which will ultimately result in the failure of your business:

• Not having enough customers and not knowing how to find any.
• Selling your product or service based on its features rather than on its benefits to your customers.
• Failing to describe your product or service accurately or legally.
• Pricing your product too high/too low.


Insufficient finance and cash flow

Too many businesses fail due to lack of start up and working capital, or because of cash flow problems that emerge a few months into trading.

Your business will fail if:

• You don’t have enough cash or other working capital at the start up phase.
• You don’t understand basic finance principles such as breakeven, profit and loss, and cash flow.
• You keep losing invoices, sales receipts, purchase orders, etc.
• You don’t chase late-paying customers fast enough.
It is important to calculate exactly how much finance you will need to meet all of your start up costs (stock, equipment and so on) and to cover the costs of running your business until it becomes established. If you can't raise enough finance to cover the costs you have identified, the business will not be viable from the outset.

Business owners who have no business finance skills will not know whether they are making any money or not. It is vital to learn the basics so that you can prepare a simple profit and loss account and cash flow forecast. You should be aware of how much money you have in the bank, what you owe and what is owed to you, more or less on a daily basis.

A good credit control system is vital even for a small business. You need to have a system for ensuring that you send out invoices on a regular basis, and you need to know who hasn't paid on time so you can chase them up.


**Ignoring legal issues**

Starting a business can involve navigating a legal minefield of rules, regulations and red tape. Even experienced business owners can struggle with all the legal requirements of running a business, which can often prove difficult to understand and manage.

Common issues that can result in legal action being taken against you and/or your business include:

- Illegally using someone else's intellectual property rights, business name or trademark.
- Starting up without the statutory local trading licences.
- Starting up without informing the right people or authorities.
- Failing to comply with health and safety regulations.

In order to ensure you are trading legally from the start, you should familiarise yourself with business legislation relevant to your business, covering the following key areas:

- Health and safety.
- Planning permission.
- Business rates.
- Fire safety.
- Intellectual property.
- Data protection.
- Trading standards.

There are also a number of organisations you must contact and register with before you start trading. If you fail to do so, you risk breaking the law and incurring a penalty or closure for trading illegally.

Problems with people

Becoming an employer is a big step for any business owner, and you need to make sure you get it right.

As soon as you take on your first employee, you are committed to complying with employment legislation and you must dedicate sufficient time and resources to make sure that you are able to manage employees effectively.

Staff can be a great asset to your business, but if you do not manage them properly, they can be a huge drain on your time and energy.

Common mistakes you must avoid include:

- Not coaching, training or explaining to your staff exactly what is required of them.
- Not paying your staff on time, or not paying the right amount.
- Not providing new staff with their written terms and particulars of employment. This is required by law.
- Failing to build a team around you to complement your own skills.

Not insuring against risks

You need all the relevant insurance to be in place as soon as your business is up and running. Some insurance policies are essential, while others are optional. It is important to understand the risks to your business and make sure you insure against them, for example:

- Staff, customers or members of the public getting injured.
- Business interruption following a fire, flood or theft.
- Business interruption due to you being too ill to work.
- Claims of professional negligence or misconduct.
- Accidental damage to premises, equipment and stock.
- Commercial disputes with customers, suppliers and other third parties.

See BIF 6, Insurance Cover for Business for further information.

Poor planning

Whether you are a new or established business, you should have a constantly evolving business plan to help you define your current objectives and your strategies for achieving them.

If you do not stay focused on the objectives in your plan, you will quickly find that you are starting to lose control of your business.

Common mistakes include:

- Not preparing a business plan.
- Spending too long preparing your business plan.
• Being incapable of communicating your ideas, plans or business proposals to partners or funders.

• Always getting distracted and never managing to address your business' priorities.


**Ignoring advice and support**

Businesses that seek advice and support, particularly during their start up phase and their first few months of trading, are far more likely to survive and prosper.

The advice and guidance of an experienced business adviser, coach or mentor can prove crucial. Good business advisers can offer advice, a wealth of business knowledge and experience, as well as access to the latest business information, management thinking and government initiatives.

They can also act as a sounding board for your ideas, and help you spot the potential problems and pitfalls before you hit them.

Common failings of business owners include:

• Starting up without professional support or advice when they obviously needed it.

• Failing to go to a local enterprise agency or other business support agency.

• Failing to go to the trade or professional association in their industry to see how they could help.

• Failing to network or seek advice from other business owners.

**Your own limitations**

Your own personal reasons for starting your business will influence the way you set up and run it, your preparations and your ongoing aims and targets.

Your business needs an investment of your time and energy to make it a success and it is up to you to make sure it does not fail.

There are personal issues that can cause a business to fail, and it is important to understand your own strengths, weaknesses and motivation for starting a business. There are also some basic reasons why you may be ineffective, which in turn can lead to your business failing. These are:

• Failing to apologise for, and learn lessons from, your business mistakes.

• Putting off or avoiding completing tasks you do not enjoy doing.

• Refusing to change your mind, or changing your mind too often.

• Going into business believing that you will get rich quickly.

**Hints and tips**

• Visit your local enterprise agency as you may qualify for free or low-cost support from an accredited business start-up adviser. They can help with preparing a business plan, sourcing micro-finance and finding low-cost business premises.
• Find a business start up training course - again, a good starting point is your local enterprise agency. Your local Chamber of Commerce (www.britishchambers.org.uk) will run regular courses covering most small business subjects.

• Visit your local business reference library for help with market and competitor research, finding suppliers, and checking and registering patents and trademarks. Some libraries employ accredited business advisers.

• Network with other small business owners, either locally through organisations such as BNI (www.bni.com) or your local Chamber of Commerce, or via an online professional network such as LinkedIn (www.linkedin.com).

• Get in touch with the trade or professional association for your sector or industry. They usually run training courses, offer specialist insurance packages, can help with marketing and offer a host of other benefits for start ups.

• Talk to an accountant or bookkeeper as early as possible to help you understand the basic finance principles involved in running a business.

• Talk to the Trading Standards department of your local authority about local licences and restrictions that may apply to your business.

• Visit your bank as early as possible, or shop around with a few different banks to see what package of support they can offer a business in your situation.

Further information

For practical start up and small business tips, ideas and news, go to:
Website: www.enterprisequest.com

To access hundreds of practical factsheets, market reports and small business guides, go to:
Website: www.scavenger.net

BIF 4 A Guide to Writing a Business Plan
BIF 6 Insurance Cover for Business
BIF 40 A Summary of Sources of Finance for Starting a Business
BIF 44 A Guide to Developing a Marketing Plan
BIF 47 A Guide to Sources of Market Information and Statistics
BIF 58 How to Forecast Cash Flow
BIF 67 A Guide to Establishing a Trade Credit Policy
BIF 132 An Introduction to Researching Your Competitors
BIF 185 A Checklist for Start Up Market Research
BIF 236 How to Forecast Sales
BIF 329 A Guide to the Organisations You Must Contact When Starting Up
BIF 341 An Introduction to Business Regulations When Starting Up
BIF 387 A Guide to Avoiding Cash Flow Problems
BIF 392 A Guide to Creating a Marketing Strategy

Useful contacts

The British Chambers of Commerce (BCC) provides a range of support services to businesses in areas such as exporting, training and information. There is a directory of local Chambers on the website.
The National Enterprise Network represents Local Enterprise Agencies (LEAs) in England.
Tel: (01234) 831623
Website: www.nationalenterprisenetwork.org

The Welsh Government provides business support, advice and information to new and existing businesses in Wales.
Tel: 0300 060 3000
Website: http://business.wales.gov.uk

Business Gateway provides business support, advice and information to new and existing businesses in Scotland.
Tel: 0845 609 6611
Website: www.business.scotland.gov.uk

Highlands and Islands Enterprise delivers local business support services for businesses in the Scottish Highlands and Islands.
Tel: (01463) 234171
Website: www.hie.co.uk

Invest Northern Ireland provides business support, advice and information to new and existing businesses in Northern Ireland.
Tel: 0800 181 4422
Website: www.investni.com

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