The Causes of Failure in the Retail Trade

The business man, even more than the professional man, needs not only to be trained, but to have aptitude for the business as well

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Present high prices have been unjustly laid upon the retailer, who in the vast majority of instances, is the victim and not the cause of the present situation. Especially in the West a rise of two or three cents per unit of commodity cannot be easily shifted to the consumer, owing to the fact that the nimble penny is not in general use. Everywhere throughout the country those lines that retail at two or three packages for a quarter have advanced in price, and it is exceedingly difficult to make the consumer understand that they must now sell at ten or fifteen cents straight. Added to the war difficulties, and rising manufacturing costs in the East, the railroads have just announced that general freight charges on western shipments will be advanced twenty per cent. Under these circumstances it is a real achievement that retailers throughout the country have been able to keep the prices of goods as low as they have. In view of the fact that business in the retail trade has become doubly difficult since the outbreak of war, and notwithstanding the apparently high profits that are being made by the larger retail concerns, it is more than ever important that retailers should make a careful calculation, not only of original costs, but of selling expenses as well, to the end that they may know precisely where they stand. Many a large retailer has increased the volume of his sales and his apparent profits only to discover later that he has been selling at a loss. The old conception that volume of sales is the important factor in business success, contains a large element of truth; but at the same time it is also fraught with much danger to the business man who considers sales alone. Everyone knows the story of the chartered accountant who, after investigating the books of a large corporation and discovering that the profits were mere paper profits, being eaten away by selling costs, asked the head of the business how it is was possible to continue the undertaking under those conditions. The reply was, that he could sell for less than his competitors owing to the volume of his sales. It is just here that the ordinary retailer, as well as the big dealer, usually falls down on his calculations. It goes without saying, therefore, that a careful scrutiny should be made, from time to time, and at definite intervals, of every aspect of the business in order that it may be known definitely whether the profit and loss account discloses a real or fictitious gain.

IN THE RETAIL TRADE.

As this article is to deal with business failures, however, and especially with failures in the retail trade, it will be necessary first of all to define precisely what is meant by failure or insolvency. It is the general conception that insolvency occurs where the debits of a business exceed the assets; but nevertheless it is apparent that such a condition need not necessarily lead to failure. Of course, a condition of this nature in any business could not be permanently maintained without leading to disaster; and yet every retailer can recall cases where a concern owed more than it owned and nevertheless pulled itself out of its difficulties. Insolvency occurs—legal insolvency—not when the debits exceed assets but when the firm is unable to meet its liabilities as they fall due.

The total assets of a company often over-balance its total liabilities, and yet it may be forced into liquidation if it cannot promptly meet its current liabilities. In that case it makes no immediate difference as to how large a concern's real assets may be. It is just here that many retailers get into difficulties—their resources are large enough to take care of all obligations; but too large a part has been tied up in a form that makes it unavailable to meet obligations as they accrue. Legal insolvency of this nature inevitably leads to a suspension of business, or to some form of compromise with creditors.

"TRUE" INSOLVENCY.

Keeping in mind that we have drawn a distinction between what might be termed "true" insolvency and "legal" insolvency, we may inquire how a concern gets into a position where true insolvency arises — that is, where the liabilities exceed the firm's assets. This may have been a condition that has existed from the foundation of the business; the proprietor too often over-estimates the value of his assets, especially when he has bought assets at second hand, or where he has acquired real estate during a boom period. These conditions have obtained very largely in the prairie provinces where a considerable number of retailers bought land and built stores during the height of the boom, only to find at its collapse that their business was weighed down by a permanent overhead charge that absorbed nearly all profits. Then again, the business man, in many cases, has foolishly expended borrowed funds in expensive showcases, silent salesmen, store fixtures, and so forth—appliances that have their value, it is true, but that too often merely typify "conspicuous expenditure." Of course, many a good business man has found his permanent assets greatly reduced in value through no fault of his own, as when a prolonged business depression occurs, reducing the value of all property; including stocks and fixtures; or when through some act of nature—such as a cyclone or a flood—his property is destroyed. This latter was the case in Regina a few years ago; and merchants who held no insurance were ruined. Aside from fire and flood, however, which may be adequately provided for by insurance, Canada, fortunately, has not been compelled to meet many such disasters.

BAD MANAGEMENT.

The majority of retail businesses that fail are forced out of line, undoubtedly, by bad management in buying and selling goods. It is particularly important at this juncture that merchants should be careful in stocking their shelves with high-priced commodities; for without doubt there will be a decline in many staple lines at the concluding of peace, although consumers must not expect to find any great and immediate decline in the cost of food. Owing to the complexity of modern business, as has been already remarked, it has become imperatively necessary for business men to make a searching analysis of all costs of production in their business, including selling and administrative expenses. And especially is this true under the abnormal conditions that prevail to-day.

The two great commercial agencies, Bradstreet's and Dun's, annually present their customers and the public with an analyzed statement of the causes of business failures. This statement varies from year to year, but the following may be accepted as typical:

CAUSES OF BUSINESS FAILURES.
100 PER CENT.

Incompetence	22.6
Inexperience	4.9
Lack of capital...	37.
Unwise credits	2.3
Failure of others	1.4
Extravagance	0.9
Neglect	2.5
Competition...	1.2
Specific conditions in business	16.3
Speculation	0.7
Fraud	10.1

It is interesting to note, in examining this table, that the usual explanation of business failures — namely, speculation, extravagance and neglect of business—is, comparatively speaking, quite inadequate to meet the case. The truth is that lack of capital, incompetence, and specific conditions that affect business in particular localities, are the main factors making for business failures. The table makes abundantly clear that the business man, even more than the professional man, needs not only to be trained, but to have aptitude for the business as well. The old idea that almost any type of man will make a success in the retail trade is ready to be thrown upon the scrap-heap of forgotten things. The truth is that incompetence, inability to manage the business, accounts for more than one-fifth of failures in this country and in the United States. The biggest single source of failure, however, is to be found in what Bradstreet's survey calls "lack of capital." In this case "capital" must be interpreted, manifestly, as lack of "working" capital; for as already explained very few businesses are forced into liquidation through impairment of assets alone. It is inability, rather, to meet obligations on demand, that causes by far the greatest number of business failures.

Since this is true, it is evident that, as a general proposition, the merchant should never permit his accounts payable to exceed more than from seventy to eighty per cent of his accounts receivable. Moreover, he should take care that his bank loans are balanced by a correspondingly large deposit; and that his stocks on hand are not offset by current or long-time liabilities. It really requires no emphasis, at least in the case of the careful merchant, to demonstrate that working capital is essential to the taking advantage of cash discounts and other economies that may make all the difference between success and failure. The merchant who permits his working capital to be unduly decreased must depend too much on current sales and accounts receivable to meet his own demand obligations. If sales suddenly fall off—as they did at the outbreak of war in August, 1914—or if debtors do not pay him promptly, the retailer must face difficulties immediately. A concern that neglects these two precautions will fail, although its assets may be otherwise thoroughly sound and may far exceed total obligations, and although its business may be large and growing, and its profits apparently great.

A retail partnership, also, often gets into difficulties by increasing its "quick" obligations—current accounts—in order to pay dividends. The profits may have been really earned in this case, but put back into the business by the partners in a permanent investment form—in store fixtures and appliances of one sort or another. This necessarily involves the borrowing of money at the bank or elsewhere, to meet current needs; and sometimes a part of such borrowed funds is used to declare dividends or profits. This is a dangerous practice. It is hardly necessary to say that the distribution of profits should be prepared for well in advance, and cash accumulated for that specific purpose, so that working capital will not be decreased to the danger limit.

A few observations may be made, in conclusion, concerning the methods of handling insolvency and bankruptcy in Canada and the United States. Both in this country and in the United States it lies within the power of the Federal Government to pass legislation dealing with bankruptcy. This the United States has done; but there is as yet no bankruptcy act in Canada applying to individuals, partnerships and corporations.

The reader should remember that insolvency and bankruptcy—where provision is made for the latter—may be either voluntary or involuntary in nature. That is, it may be asked for by an insolvent person or company in order to secure a legal discharge from debt; or, on the other hand, it may be demanded by creditors whose claims are unsatisfied, in order that they may obtain an equitable division of the property. It may be observed, also, that there is a third method, of dividing assets among creditors, a method which is usually followed by corporations; namely, the appointment of a receiver by the court. This is done in order to provide for an equitable division of the property among the various claimants; and, what is perhaps of as great importance, to continue the operation of the business. Under the Dominion Winding-up Act a receiver may be appointed to take charge of a corporation's assets, on a petition being presented to the court by the corporation itself, by interested stockholders, or by secured or unsecured creditors. The Dominion Winding-up Act, however, is insufficient to meet the country's needs, since it applies only to corporations, and even then not to all of them. It is true that the several provinces have Winding-up Acts which apply to individuals and partnerships; and under these acts an individual, or partnership, business may go into voluntary liquidation. There is, nevertheless, imperative need in this country for the passing of a Dominion Bankruptcy Act which will, on the one hand, protect creditors, and on the other, free the debtor from all future claims, once he has handed over all his assets to those who have claims against him. This is possible under the National Bankruptcy Act of the United States as amended in 1910, and from its provisions much may be learned that will prove useful for meeting Canadian needs.

FEATHERED SENTRIES.

A sailor recently stated that seagulls are very useful for betraying the whereabouts of a submarine. When the birds discern a periscope they rise in a flock from the water's surface, and circle round it uttering shrill cries. This performance attracts the attention of the crews of approaching vessels, and ofttimes results in the submarine being discovered.

Whilst seagulls are unconsciously aiding sailors, parrots are carrying out equally useful work for soldiers. It has been discovered that parrots have an extraordinary faculty for anticipating the approach of aircraft. Before an aeroplane has come within range of the human eye, the feathered alarum becomes violently agitated and shrieks incessantly. In France wild birds often provide artillery observers with clues as to the whereabouts of hidden batteries. Birds rise in flocks from trees in the vicinity of which guns are being fired, and when there is a lull in the activities of the concealed artillery many of them return to their former perches. A trained observer can quickly tell, from the erratic movements of flocks of birds, the approximate locality of gun batteries hidden from his view.—Tit-Bits.