

SPECIAL 2008 EDITION


# Surviving the Credit Crunch

Barely a day goes by without a news story about the struggling economy, and you may be concerned about how your business will cope in the so-called 'Credit Crunch'.

Good business and financial planning is always important, but especially so in an economic downturn. This guide provides an overview of the current economic difficulties, but more importantly gives you some tips and advice on ensuring that your business is protected during these troubled times.



**What is a Credit Crunch?**



'Credit Crunch' is a term used to describe a sudden reduction in the general availability of loans (or 'credit',) or a sudden increase in the cost of obtaining loans from the banks. The current problems are rooted in the US sub-prime mortgage crisis.

*For an overview of the Credit Crunch, see page three...*

## How we can help...

As your accountants, there are many ways in which we can help to protect your business' profitability. Contact us for more advice about:

- minimising your business taxes
- making the most of capital allowances
- reducing company car costs
- improving your financial position by accelerating expenditure into the current year, or deferring income into the next.

Your income and personal wealth can be significantly reduced by regular income-related taxes and more 'periodic' taxes, such as capital gains and inheritance tax.

We can help you to:

- make the most of personal allowances
- extract profit from your business
- save money tax-efficiently
- review your pension arrangements
- reduce the inheritance tax on your estate.

We hope you find this guide useful – please contact us for more information and advice.

## Inside this Newsletter...

- Protecting your Business
- History and Timeline of the Credit Crunch
- Protecting your Wealth



# Protecting your Business

**Don't get crunched! Here are some tips for protecting your business in an economic downturn...**

## Keep on top of credit control...

When times get tough, it becomes more difficult to get payments from your debtors, and late payment can be a real issue.

According to a recent study, 59% of small and medium-sized enterprises are encountering more difficulties with outstanding debts since the beginning of the Credit Crunch – with 33% claiming that clients' failure to pay on time risks the survival of their business.

Smaller firms are particularly vulnerable to the effects that late payment can have on cash flow, profitability, and ultimately the viability of a business. If you want to avoid falling victim to the 'late payment culture', consider the following strategies:

- **Credit check customers** – Minimise the risk of late payment by conducting credit checks on new and potential customers. It may be possible to obtain a credit report from a reference agency. Information may also be accessed through Companies House.
- **Invoice promptly and efficiently** – Distribute invoices in a timely manner to ensure the payment process remains as efficient as possible, and prevent unnecessary delays by addressing the invoice to the correct contact and department.
- **Debt management** – Make sure you have a clear policy for collecting debts and that customers are aware of it. Above all, ensure you enforce it. Pursue outstanding debts with letters and telephone calls, and threaten legal action if you have to.

If your terms of business allow for adding interest on overdue accounts (they should, and at a good rate), add it. If your terms set credit limits, stick to them and stop supplying as credit limits are reached or bills go unpaid.

- **Remain vigilant** – By keeping an eye on your customers' payment trends, you may spot potential problems before they develop into something more damaging. If customers are becoming increasingly hard to contact, or cheques are suspiciously delayed, it may be beneficial to investigate further.



## Monitor your cash flow

Late payment, coupled with increasing supplier costs, can cause cash flow to stagnate. Being able to identify potential cash flow difficulties is therefore an important part of managing your organisation. It is better to take preventative measures rather than deal with the consequences further down the line.

A cash flow forecast is a simple tool that enables you to make educated financial projections and identify the likely peaks and troughs in net cash over the coming months. You can start with anything from a sheet of paper to proprietary software, but you will need a clear idea of how cash will move in and out of your business over the months ahead.

We can help you draw up a realistic cash flow forecast – contact us for more information.

## Keep on marketing

As budgets get tighter, many firms have been forced to cut back on unnecessary expense where possible. The marketing budget is often the first casualty, but smart businesses continue to market through a downturn and position themselves to take full advantage of the upturn as soon as it starts.

In tough times the marketplace becomes more competitive – you may need to market more vigorously, not less. If you do not have a strategic marketing plan, now is the time to draw one up.

## Maintain customer loyalty

In difficult times it becomes harder to attract new customers. Therefore, it is more important than ever to maintain loyalty

amongst your existing ones. Consider ways of developing and rewarding customer loyalty, such as selected discounts (especially for early payment), regular mailings or loyalty cards.

## Beware of cutting prices

If receipts begin to taper off, it can be tempting to cut prices. But this can be a mistake. In a recession your costs will inflate and as a result you may be forced to raise prices to cover this expenditure. Cutting prices can also have the negative long-term effect of devaluing your image in the marketplace. Remember that suppliers might raise their prices as well, so try to negotiate a long-term discount with them.

## Look after your employees

While job cuts may be necessary in some circumstances, you should always try to retain your key employees: their strengths will help you through an economic downturn, and you will need them when business picks up. You should use any dips in the market as an opportunity for key staff to develop new skills and coach newer members. Remember, employee motivation can rapidly deteriorate in times of economic uncertainty, so maintain good communication with your staff to prevent a decline in morale.

## Planning ahead

Planning is vital for the success of your business. You need to plan the changes that can strengthen your enterprise against tough times, and how those changes will be put into action. However, planning is not just about 'worse case scenarios' – we can work with you to plan for your business future, offering advice on business management and tax planning and personal financial planning.

# History of the Credit Crunch

After so many years of economic growth, why do we find ourselves facing slowdown and even possible recession? Here is a brief overview of the Credit Crunch...

## The sub-prime mortgage crisis

The American 'sub-prime' mortgage crisis is generally identified as the start of the Credit Crunch. At a time when money was plentiful, US lenders had few qualms about offering mortgages to high-risk customers who, should interest rates rise, might not be able to meet the required repayments.

Although this relaxed lending ethos gave many a helping hand onto the housing ladder, the market found itself in disarray when increasing numbers of borrowers fell into arrears and bad debt accumulated to an alarming level. With America such a dominant force in the global economy, it wasn't long before the effects began to be felt across financial markets the world over.

## Going down...

On 12 September 2007, Northern Rock, one of the top five mortgage lenders in the UK, was forced to seek emergency funding from the Bank of England. The bank had a liquidity crisis because institutional lenders had become nervous about lending to mortgage banks following the US sub-prime problems.

As global stock markets and high street sales tumbled, banks and building societies – in the UK and abroad – grew increasingly reluctant to lend to customers, small businesses and each other.

Meanwhile, individuals and firms that were able to secure funding faced far more rigorous lending criteria and unyielding high repayment rates. Consequently, new mortgage approvals have reached an all-time low in 2008 – down by 71% on the previous year. House prices have also seen their most significant fall since 1990.

Conversely the cost of living has increased, with sharp rises in fuel, food and energy prices adding further pressure to the already stretched finances of many UK home owners.

## From Wall Street to Westminster: a timeline of key events

9 August 2007 – 'The day the world changed' according to official figures – in the wake of the US sub-prime crisis, major banks refuse to do business with each other.

13 September – Run on Northern Rock – Bank seeks emergency funding from the Bank of England to offset the impact of the Credit Crunch. Customers withdraw £1bn when the news breaks.

21 January 2008 – Global stock markets, including London's FTSE 100 index, suffer their biggest falls since 11 September 2001.

10 April – The Bank of England cuts interest rates by a quarter of one percent to 5%.

2 May – More than 850 companies have gone into administration between January and March – a rise of 54% on the previous year. Retail and construction firms are hardest hit.

31 July – UK house prices show their biggest annual fall since the Nationwide began its housing survey in 1991, a decline of 8.1%. The average home now costs £169,316. That is nearly £15,000 cheaper than in the same month last year.

31 August – Chancellor Alistair Darling urges Britain to brace itself for stormy economic times ahead, claiming the UK is facing the worst economic conditions for 60 years.



# The Credit Crunch

# Protecting your Wealth

The credit crunch is undoubtedly hitting UK pockets hard. However, preparation and forethought can help to alleviate the effects of the credit crisis.

## Saving...

Although the tough economic conditions may be straining the nation's personal finances, now is a very good time to save if you can afford to. With banks competing for customer savings, there has been an increase in the number of accounts offering interest rates above the base rate.

Gains and most income in Individual Savings Accounts (ISAs) are tax-free, and they are ideal for saving small, regular amounts. You have until 5 April 2009 to make your 2008/09 ISA investment. ISAs are available from banks, building societies and a variety of other providers. The maximum annual deposit is £7,200 overall, of which no more than £3,600 can be in cash.

## Spending

We probably all spend more than we need to. Have you considered:

- switching credit card providers to take advantage of interest-free periods?
- shopping around for utility providers?
- cutting energy costs by making your home energy efficient?

## Mortgages and property

If you have family members looking to get a foot on the housing ladder, you'll know that many first time buyers are struggling to secure a mortgage without a substantial deposit. Figures from the Bank of England show the number of new mortgages approved fell to just 33,000 in July – down by 71% since 2007.

However, you might be able to take advantage of the 'stamp duty holiday'. Until 3 September 2009 stamp duty tax will not be levied on houses costing less than £175,000. The temporary reform could save home buyers up to £1,750.

## On a Lighter Note...

Consider these money-saving tips to help you survive the worst of the Credit Crunch:

Avoid leaving appliances on standby – up to 10% of the total electricity used in your home is due to appliances left on standby.

Did you know... Turning the thermostat down by one degree C can cut more than 10% from the average central heating bill?

Driving in the highest gear possible without labouring the engine is a fuel-efficient way of driving. Travelling at 37mph in third gear uses 25% more fuel than at the same speed in fifth gear.

Have a clear out and make money by selling all your unwanted gifts, clothes and accessories on eBay.

## What Does the Future Hold?

Will Britain enter a recession? And when will the financial storm finally pass? It is impossible to assign accurate dates to these questions. The Chancellor himself recently delivered a stark warning on the issue, claiming that the current economic times 'are arguably the worst they've been in 60 years' and are likely to be 'more profound and long-lasting than people thought.' Whilst the immediate future remains uncertain, both businesses and individuals should be prepared to weather the financial storm.

As your accountants, there are many ways in which we can help improve your personal finances, and also assist your business to remain profitable and successful. For further advice on how to survive the Credit Crunch, please contact us.