



Downturn Forcing Private Companies into Cost Cutting, Layoffs

By MATTHEW SCOTT, AOL SMALL BUSINESS
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Small, privately held companies have done an admirable job keeping their businesses afloat during the worst economic conditions since the Great Depression, but now data suggests they are feeling pressure that could lead to more layoffs and more small business failures.

New analysis of privately held companies released by consulting firm Sageworks, shows small privately held companies have tightened cash reserves, are taking longer to collect payment from customers and have inventory lingering on their shelves longer than in previous years. Such trends don't suggest much of a recovery is taking place among these companies, and if current conditions persist, the firms would be forced to implement another round of cost-cutting that could lead to additional job losses.

"We've seen a pretty dramatic downturn in revenue in 2009 for privately held companies overall," said Sageworks' CFO Andrew White in an interview with DailyFinance. "The companies that have stayed in business have taken the right corrective actions to maintain their cash and net income, but they've done that by cutting expenses and overhead which means people, advertising and other overhead expenses."

The loss in revenue this year has forced companies to make difficult decisions, including cutting staff, overhead and expenses, as well as reducing inventory and spreading out their payable days. According to Sageworks, sales for private companies have plummeted since 2006: sales that year increased 7.3 percent and dropped to a 2.4 percent increase in 2008 before declining by 3.75 percent through October 2009. Companies are taking an average of four days longer to collect accounts receivables and it takes an average of six days longer for inventory to leave the store.

The loss in revenue has also resulted in a decline in "payroll as a percentage of sales" among private companies, which White said means companies are devoting less money to employee raises and jobs. That's bad news for workers. The small business administration estimates that half of the nation's private sector jobs are contained in businesses with 500 or fewer employees. Most private firms fall into that category so layoffs may loom.

White said that due to their cost cutting, net profit at private companies has increased 6.4 percent and cash as a percentage of assets has stayed in the 12.5 percent range, allowing them to remain relatively healthy. But he cautioned that private businesses are not buying inventory and not investing in their businesses -- and like the American consumer, they can't get credit -- all warning signs that small business is in "defense mode."

"If you are losing money and you can't borrow, you're not going to stay in business," White said.

Borrowing money is particularly important for retailers and wholesalers that sell tangible products that they have to pay for upfront. White said it is possible some private businesses could soon see demand for their inventory pick up, but not be able to borrow the funds to restock for the holiday season. The recent bankruptcy of CIT Group could have a major negative affect on lending to private corporations, especially those CIT customers that need their operating lines of credit to finance their business.

The one bright spot to glean from the Sageworks data is that White believes that "businesses have taken the appropriate actions to maintain their profitability and their cash, so when they see an uptick in sales, they will be leaner and probably more efficient. When the economy does recover, they will be able to grow with it and expand."

But in this economy, sales increases may take a very long time to materialize.