THE NETWORK OF LEADERS

CRITICALEYE

CEO Breakfast - September 2009

Date
September 2009

Chair
Matthew Blagg, CEO, Criticaleye

This article is based on the proceedings of a meeting of Members of the Criticaleye Community. To encourage open debate, the meeting was held in a confidential environment. This article presents the distilled insights and conclusions from the session.

Take-aways

- There were mixed feelings in the group. Most weren't confident about a quick recovery but are increasing headcount.
- Participants were wary of what form the recession is taking with U-, W- or L-shapes being discussed.
- Getting financing is still difficult with many banks 'running scared' from investments and setting what participants felt are incredibly high fees
- 'Dead men walking' companies are being kept alive by banks and HM Revenue and Customs. These firms provide interesting opportunities for strong companies to make acquisitions

Introduction

This CEO Breakfast once again saw the discussion gravitate towards macroeconomic issues. Participants were concerned with the shape the recession is taking, banking, funding and their confidence in the market.

In a month in which signals have suggested an economic recovery may be underway, the discussion turned to green shoots; participants were not actually confident that a real recovery was underway.

Although confidence around the table was low, there were mixed reactions to the current climate. Almost all believed that their businesses are now 'right-sized' and a good portion is increasing headcount. This was thought to be a good sign. However, some delegates disagreed and one participant believed that the next five years would be extremely gloomy.

The Member, who works with SMEs, thought we currently exist in a “capital starved world”. He said:

“It is hard to see how investment capacity will come back into the market. I can’t see where the capital will come from. It will take a couple of years to get the capital back, even with several years of good profits and low dividends and private equity flowing toward the larger end of businesses.”

However, another delegate challenged that by saying capital would come from alternative sources, such as, high net-worth individuals,

Capital and financing are still hard to come by with brokers’ fees increasing to what one delegate felt were “unbelievable” levels, and banks still ‘running scared’ from most investments.

Funding update

Increased fees and harsh covenants are making refinancing impossible for some.

A participant looking to refinance found that prices have increased ten-fold, “that is, if you can get a deal at all.” This has forced investigation into different markets.

The renewal of one Member’s facilities was impeded by a new entity entitled, *the capital allocation committee*. This meant he had to go through both the credit and this committee to get approval, and it almost didn’t go through as a result.

Fundamental changes in the banks are also causing problems with funding. Internally this means staff members aren’t sure who to report to, while senior managers have much wider remits. These shifts are slowing down the decision-making process.

Members felt the banks are now significantly fearful of lending money to the wrong organisations. Some CEOs around the table believed banks will finance but squeeze as much as they can get out of the deals.

‘Dead men walking’ companies

Many believed that ‘dead men walking’ companies, ie, organisations being kept alive either by the banks or HM Revenue and Customs, are going to run into trouble in the coming year and will end up dying out.

Banks are dealing with this by trying to manage their exits gracefully, picking in which quarter to write the companies off.

HM Revenue and Customs is also keeping many companies afloat. According to Members at the Breakfast, it has been instructed by the government to do so, and the degree of accommodation being given is massive.

Opportunities emerging

For the cash-rich, the current environment is bringing about many opportunities to buy up companies with reduced values.

“Where there is change there is an opportunity to take market share from somebody,” said a participant.

“If you’re in the market for acquisitions, being listed is the ideal place to be,” thought a Member, adding, “You can raise money in the market for acquisitions.”

One Member’s company was recently purchased by an American company at a 70 per cent premium. Although the company’s ownership wasn’t looking to sell, the purchase went uncontested. The current environment meant that the leadership didn’t have the confidence to say no to such a lucrative offer.

The chair then asked the group whether they thought the recession would take a V, W, U or L shape.

One Member believed that we are in a U-shaped recession, with the UK currently in the bottom of the U where it will remain for some time.

Many were concerned with the news that more Britons had repaid debt in August than in previous months, meaning there will be less spending, causing the recession to prolong.

Are we in a ‘new normal’? Yes, thought the group. Corporate decision-making and governance is changing. There is also a growing importance on building strong and lasting relationships with customers.

It was also mentioned that the private and public sectors are not in the same place along the U; it would appear that, from a macroeconomic perspective, the private sector is better situated.

Members felt we are likely to see a change in government in the coming months. This has influenced spending and budgets in the public sector, which are standing still.

The second wave of the recession will see public spending decreased. There are also ‘loud whispers’ about tax hikes, but this will result in decreased consumer spending thus knocking the private sector back to where it was in the recession.

Some CEOs felt that the downturn has taken an L shape and that the bottom stretch will last for five or six years. “Growth will come back, but not significant growth,” said a Member.

"Productivity will come back. This is a great time to be a CEO," said the chair. "A good CEO can make a considerable contribution in this type of environment."

CEOs today

One Member, who recently stepped down from a CEO position, found it difficult to identify where job opportunities lie. "Someone in my position cannot afford to be choosy about industry when looking for a company with a strong balance sheet, market share and a good board. I am taking time off and examining the market to see what comes up," he said.

There is a confidence issue in the 'new normal' with the way that businesses are run. The chair summed up the morning by reiterating that decisions are indeed hard to make in such uncertain times. "It is an odd era for leadership," he said. "But a rewarding one; getting decisions right is extremely important."

It is important not to forget the positive signs, asserted the chair. Many around the table were increasing headcount and feel that their businesses are right-sized, which is more positive than everybody thinks.
