

Why Do Small Businesses Fail?

Eighty percent of all new small businesses fail in their first five years.

Here are the major reasons ranked according to frequency:

1. **Inadequate front-end planning.** No Business Plan prepared; no Feasibility Study done and no Cash Flow Projections done. Continuous planning is essential during the growth of a business. The most common trap for an entrepreneur to fall into is to become so involved in the day-to-day operations of the business that long-range planning, which might point out the need for a change in the business structure, is neglected.
2. **Insufficient capital for startup and backup.** Even the most dedicated workaholic cannot overcome ongoing capital deficiencies due to startup losses.
3. **Inexperienced management.** Insufficient experience in the management and the day-to-day operations of the business or of any business.
4. **The wrong location.** Low traffic, no expansion area, changing characteristics of the neighborhood. The customers are out there, but the business is not convenient because of driving and parking distance, transportation costs, employee unwillingness to live in the community.
5. **Inventory mismanagement.** Too much of the wrong inventory.
6. **Too much capital in fixed assets.** The failure to properly anticipate the cost of equipment and real estate needed to start and expand.
7. **Poor credit practices.** Failure to properly extend and control credit policy and practices.
8. **Unplanned expansion.** If one location is doing well, a second doesn't mean the business will do twice as well unless management is available.
9. **Having the wrong attitude.** Not ready to work longer and harder than ever before; too much money in trappings and appearance.
10. Inadequate records and financial knowledge.
11. **Unwillingness to employ and work with a banker, accountant, and a lawyer.** These are three essential partners to have and use.
12. **Lack of managerial foresight.** Failing to build staff to compensate for the weaknesses of the founder or owner: Failing to adequately compensate second-line management.

Michael Gerber, founder and CEO of Gerber Business Development Corporation, author of *The E-Myth: Why Most Small Businesses Don't Work and What To Do About It* (Harper Business), has compiled, based on his 17 years of small business research, his own list of reasons why small businesses fail.

1. **Lack of management systems.** Most entrepreneurs have no systematic way of generating information or determining what is and what is not working. Also, there is little or no effort to convert data into usable information.
2. **Lack of vision and purpose by the principals.** Entrepreneurs need to view their business as a means to an end. Bill Gates, for example, has become successful because his purpose was to put a computer in every home and his business was a way to achieve that goal - not vice versa.
3. **Lack of financial planning and review.** Most self-employed people concentrate primarily on generating income when they should be most concerned with building equity.
4. **Poor market segmentation or strategy.** Most entrepreneurs don't know who their customers are. Factors such as customer age, geographic location, and family size can have an impact on what and how they buy.

5. **Competition, or lack of market knowledge.** The self-employed are often so engrossed in the daily task of running a business that the last thing they think about is what their competition is doing and how they can do it better.
6. **Inadequate capitalization/under-funded.** Although this factor commonly rates as the primary reason for business failure, it is actually a symptom of underlying problems.

Source: "Why a Large Number of Small Businesses Fail", Home Office Computing, May, 1994, page 16.