collective szabo wisdom®
SZABO ASSOCIATES, INC. VOLUME 27, ISSUE 1, MARCH 31, 2012

Dear Friends:

At times it seems we're in economic limbo, a transitional state where the worst is past but a good deal of post-recession uncertainty remains. Media reacted to the worst downturn of the past half-century with its usual "can-do" spirit, pursuing every avenue to get business and get paid. With the worst of the present crisis over, however, indecision and inattention have begun to take the place of some organizations' usual diligence, seriously compromising collections. This issue's feature discusses the perils of "post-panic collection syndrome" and how to keep your organization from falling victim.

Our spring calendar begins with the Media Financial Management Association/Broadcast Cable Credit Association (MFM/BCCA) annual conference on May 20-23 at Caesars Palace in Las Vegas, Nevada. Szabo is pleased to sponsor the association's May 21st opening night party, featuring the Spazmatics, live onstage at the Hard Rock Cafe. We'll also attend the Georgia Association of Broadcasters Awards Program on June 2nd here in Atlanta.

Best wishes for a wonderful spring,

Robin

Robin Szabo, President
Szabo Associates, Inc.

Post-Panic Collection Syndrome . . .
Don't Let It Get Your Profits Down!

The recession of 2007 hit the media industry hard. Of the 10 recessions experienced by the U.S. economy since the end of World War II, this one was the longest. It was also the deepest, as determined in part by its 18-month duration, but more importantly, by the magnitude of the decline in economic activity. In June of 2009, the National Bureau of Economic Research issued a "trough announcement," officially proclaiming the recession's end and the beginning of the rising phase in economic activity.

So severe was the recession that, understandably, a kind of panic rippled through the media industry. As the economic forecasts continued to be bleak, concern about ensuring adequate revenues in order to emerge successfully from the downturn became a major focus of media properties. Faced with shrinking advertising budgets and an increasing number of delinquent customers, many turned to third-party collection professionals fairly early in the collection cycle to maximize their chances of getting paid and to improve cash flow.

After 2009, media began to feel some relief from their initial fears as economic indicators improved. Focus turned away from payment delinquencies and toward lagging sales and cost restructuring. In an effort to save money, properties began doing more collections in-house, while many business departments continued to ask themselves, "Is this really a good idea?" and "How can we best deploy our limited resources?" Before tackling these questions, we should take a fresh look at the current economic and advertising environment.

Good News and Not-So-Good News about 2012.
This year will be an auspicious year for advertising revenue. MagnaGlobal, the strategic global media unit of Interpublic Group's Mediabrands, predicts a 4% uptick in U.S. year-over-year advertising, due largely to the presidential, congressional and gubernatorial elections, as well as the Summer Olympics. It also cited the Supreme Court's loosening of campaign finance rules as another possible boon for the advertising industry. Accordingly, a new STRATA quarterly survey of leading advertising agencies found that 81% expect their clients' approach to advertising and marketing to either increase or stay the same in 2012.

On the other hand, while certainly helpful, the quadrennial booster shot of a presidential election year does not change the realities of our ongoing economic problems. On February 1st, Congressional Budget Office Director Doug

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Elmendorf, in a hearing before the House Budget Committee, projected that economic growth will be only 2% this year and 1.1% in 2013, with an unemployment rate at 8.9% at the end of this year. Because of increasing labor productivity and natural population increases, a growth rate of 2.5% to 3% is necessary to keep unemployment steady. A primary contributor to the weakness of the recovery has been home prices, whose decline has severely curtailed consumer spending for goods and services, which accounts for 71% of GDP. Other factors, such as the European financial crisis and an economic slowdown in Asia, have contributed to investor unease. While projections do not necessarily come true, many analysts conclude that it might take only one unfortunate event to push the weakly recovering economy into negative territory again.

The Perils of Post-Panic Malaise.

Other than people and cash, an organization's accounts receivable are its most important asset. As part of an organization's working capital, they are expected to be turned into cash within the annual operating cycle of the business. Even so, many organizations seem willing to gamble on receivables, when the odds for winning are clearly against them. The older they get, in good economic times as well as bad, receivables have a diminishing chance of recovery. According to collection industry surveys, the probability of collecting an account after 90 days is 69.9%; after 180 days, the probability is 52.1%; after one year, the probability plummets to 22.8%; and after two years, the probability is a mere 9.3%. With collections of intangibles such as media, the probability is even less.

In the past couple of years, Szabo has observed changes in the way many media organizations are handling collections of overdue accounts. At the beginning of the recession, accounts were generally worked in-house at intervals of 30, 60, 90, and 120 days, with turnover to third-party collectors at under 180 days. Now, it has become common for some accounts to be ignored until they have aged 90 days, automatically reducing their collectibility by 30% without any attempt at resolution, and to delay placement for third-party collection until they have aged well beyond 180 days. Many of these accounts might have been easily collected in-house in full with a single contact; instead, media not only lost money but set an unfortunate precedent for future delinquencies. Why would media organizations gamble, with odds stacked against them, on the prospect of recovery after such hard-fought sales?

When receivables are allowed to become older and older, the options for recourse become less clear. It has been our observation in recent months that an increasing number of media companies are giving serious first consideration to collection options that we believe should be “last-ditch” efforts; in other words, when all other efforts at collection have been earnestly tried and have failed. For example, filing lawsuits against delinquent customers whose accounts have not been previously “worked” has become a more common consideration, perhaps because of the perception that there is a slim chance of collecting otherwise on a very old account. Additionally, more organizations are choosing to handle the complex matter of client bankruptcies in-house. And perhaps the most counter-productive of all has been a “do-nothing” approach as accounts continue to age beyond the window of likely collectibility. Indecision about the best course of action has become more pervasive as organizations have become increasingly sales-driven and cost restraints have been instituted as a result of the economic environment.

Striking a Balance That Pays Off.

Every organization has to work within the parameters of its resources and according to the goals and strategies of its management. In difficult times, the pendulum often swings toward aggressive sales in an increasingly competitive environment. The credit and collections department is required not only to work harder to approve credit for marginal customers but also to maximize collections with limited personnel resources. Striking the correct balance to meet both objectives is one of the credit manager's most difficult challenges in tough economic times. A few good strategies can help your staff use their efforts to best advantage.

Prioritize your collection efforts. Know that you can't do everything, so choose the most important first. Your first priority should be new customers. Even if the amount owed is relatively small, you never want to set a precedent for late payment. The high-stakes accounts, with which you have the most to lose, should be your second priority. Slow pays, which often just need a quick, simple reminder, should be your number three priority. If you have any remaining time, contact anyone else who is overdue, concentrating on those with more substantial amounts and the best chance of collection.

Use measures to gauge overall results. While measures have their shortcomings, they remain a useful tool to evaluate the effectiveness of your credit and collections department. Days

Sales Outstanding (DSO) is typically calculated monthly and represents the average number of days that invoices are outstanding. A significant shortcoming of this traditional measure is that the numbers may fluctuate due to factors beyond your control. In economically troubled times, you may find yourself with higher-than-normal DSO, not only because of more slow-to-pay customers but also because of management's decision to extend sales terms and/or liberalize your credit policy. For example, an increase in credit sales that also increases the total receivables balance will give you an increased DSO.

Measures that compensate for some of the deficiencies of DSO to evaluate personnel effectiveness are Average Days Delinquent (ADD), which gives you the average number of days invoices are past due; Percent Current, which adds the dimension of relativity between departments and personnel; and Collection Effectiveness Index, which measures the effectiveness of collection efforts over time as opposed to a single point in time.

If the outcomes of these measurements are disappointing, determine the reasons why they are subpar. For example, if your credit policy has become more lenient, have you made changes in your collection processes to minimize DSO? How does the overall quality of your accounts receivable compare to pre-recession receivables? (For a more detailed description of objective measures as well as subjective considerations, see *Collective Wisdom, December 2009.)*

Turn over accounts for third-party collection by 120 days. Keeping aged receivables in-house will not help your DSO. By 120 days, when collectibility has already been reduced about 35%, additional efforts on your department's part are an inefficient expenditure of valuable resources. If the account has been worked at the proper intervals from the day it became delinquent, any discrepancies or disputes should have been cleared up by the 90-day mark. If it becomes clear prior to 90 days that the debtor has no intention of paying, turn it over at that time. Chances are, broken promises and unfounded disputes will not be resolved unless taken to the next level.

Acting early in the aging cycle pays off. Throughout the recession, the fifth since Szabo has been in business, the company was able to resolve 75% of its clients' collections issues within 90 days. From a different financial standpoint, collection services are a recognized and legitimate business expense. And finally, the cost of personnel and material resources is better spent on pursuits other than collecting seriously delinquent accounts. (Historically, creditors receive payment on approximately 25% of accounts to which past-due notices are sent.) A more profitable use of your time is to assist sales by finding ways to say "yes" to marginal customers, and to stay on top of new and existing customers to keep them current.

Consider "last-ditch" efforts only when all else fails. Lawsuits are end-of-the-game undertakings that need to be handled by professionals who are knowledgeable and experienced in media law. Lawsuits can be complicated and demanding courses of action, with no guarantee of a successful outcome. Additionally, a lawsuit marks the end of a business relationship, when perhaps a different approach might result in retaining the customer who is simply going through a bad patch. For these reasons, credit managers need to carefully evaluate the potential cost, time, and chance of the lawsuit's success before "pulling the trigger" with an attorney. A third-party agency with experience in collections and media litigation, and perhaps with your particular debtor, can help you make this decision. The objective is to collect your money at minimum expense in the shortest possible time. If proceeding with a lawsuit is deemed to be the best way

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"Boss, you know how Sales took one day a week last month to help collect past-due accounts? The good news is, he finally got that old skinflint Mr. Harper to pay up. The bad news is, sales revenue for the month took a nosedive."

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to meet this objective, an agency with litigation services can also shepherd you through the process to make it as smooth and effective as possible.

Bankruptcy is another possible unpleasant outcome of customer indebtedness. This looming possibility is also another reason to place accounts early for third-party collection. The "red flags" for bankruptcy can go unnoticed with aged accounts, and quick and proper recovery of debt is imperative under these circumstances. Payments within 90 days of bankruptcy generally fall under the "voidable preferences" ruling and must be returned to the bankruptcy court. Bankruptcy law is complex, particularly in areas such as executory contracts, where there are material duties remaining to be performed on both sides. Unfortunately, recovery of debt from a bankrupt customer is generally slow and small; therefore, efforts to manage the process in-house are not an efficient use of your resources. An agency experienced in bankruptcy procedures and an attorney who specializes in bankruptcy law can maximize your chances of collecting on your claim.

Boost your value. U.S. businesses could well be in for another difficult stretch before we enjoy an enduring upswing in economic activity. As valuable as credit and collections is to your organization during times of strong economic growth, its value is arguably even more important when the goal of bringing in sufficient business holds sway over your preferred methods of running your department. By clarifying priorities, outsourcing unprofitable tasks, and deploying your reclaimed resources to better assist credit sales, your organization will be positioned to take best advantage of the difficult times now and the good times ahead. ♦

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