

The background of the cover is a photograph of a man in a dark suit standing in a field of tall, golden-brown grasses. The man is on the right side of the frame, looking towards the left. The sky is a clear, bright blue. The overall mood is one of resilience and growth.

Growing Businesses

Issue 15

From the editor

Welcome to Issue 15 of *Growing Businesses*.

From a position of unparalleled economic growth and prosperity, storm clouds have gradually descended upon the world's major economies over the past year. In this edition we take a look at the current economic climate and shed some light on how to best position your organisation to weather the storm.

Bernard Curran, Editor

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It's not all gloom!

There is no doubt that 2009 and beyond will be a challenging business environment for most organisations. Although the duration of the economic downturn is unknown, there is still strong evidence of the optimism typical of our Australian culture.

It may seem counter intuitive to speak of business opportunities at a time of rising joblessness and inventories, slumping profits and falling exports and business investment. However, the change in asset values – property, shares, businesses and cash – has encouraged some new investment from many who stayed on the sidelines during the recent boom.

These investors, many of them longstanding family businesses, have low debt levels and strong balance sheets. These businesses have benefited greatly from the nation's recent boom, and are looking to seize opportunities arising from the current economic climate. Recent acquisitions by private investors in commercial property markets are indicative of the return these private investors are making, and more such investment is likely in the months ahead.

While 2008 was a year of managing growth and building capacity, 2009 is set to be a year of managing to the current level of business activity rather than over-expansion. It is time to get back to the fundamentals of business success: hiring the right people, understanding the market, developing the right strategy and executing well.

In the current environment, only businesses with the right strategy and execution can successfully build market share and position themselves for the future.

With the fiscal stimulus packages launched by Australia and our major trading partners, together with large cuts in official interest rates around the world and the injection of liquidity by central banks, it will not be long before the global economy picks up speed.

While the exact timing of the recovery is uncertain, what is certain is that those who maintain their commitment to customers and staff in the current downturn will emerge even stronger in the upturn.

Bernard Curran, Editor

Staying afloat in uncertain times

Tom Lesnikowski, Associate Director, BDO Kendalls, Melbourne

It is critical to continuously monitor the financial health of your business in both good and uncertain times. As we enter a time of great uncertainty, now is the best time to be on top of the performance of your business, giving yourself the opportunity to fix any operational and financial aspects before they become an issue.

Businesses may fail for a variety of reasons. Some of those reasons are as follows:

- poor planning;
- lack of appropriate funding;
- inadequate management of working capital;
- poor relationships with key customers & suppliers; and
- inadequate financial records management.

While the above is not an exhaustive list of causes of failure, all are influenced by management. Studies indicate that more than 80% of businesses fail due to poor management.

What is poor management?

Poor management has been described as the inability to recognise that the above factors are affecting performance and to implement strategies and controls to overcome those factors.

Below are some areas you may need to consider and focus upon:

Poor planning

Have a business plan that identifies your businesses' current status, including the objectives, strategies, operational and financial plans for the future. Regularly review and modify your structure and strategies to reflect prevailing economic conditions.

Lack of appropriate funding

You will need to consider what level of external funding is required and what repayment terms best suit the business. This area directly impacts every size and type of business

and should be reviewed on a regular basis, particularly as financial markets themselves go through a period of change.

Inadequate management of working capital

It is critical to manage the key elements of working capital: stock, debtors and creditors. These components of working capital have a significant influence of your cash flow. Sustainable ongoing cash flow is a critical element of the success of your business.

Poor relationships with key customers and suppliers

Customers are your cash flow and livelihood. Reliance on too few customers can be disastrous. It is also important that your customers continue to pay within agreed terms. Ensure you have a strategy in place for dealing with late payers and possibly rewarding those that pay early or on time.

Maintaining positive relationships with suppliers lets you maximise your products and services and can ensure referrals and other business opportunities. How well are you looking after your key customers and clients? Do you have a loyalty program in place? These are some things to consider that can help keep your relationships on track and make sure that your client base continues to stay with you and not jump ship to a competitor.

Inadequate financial records management

Informed and accurate decisions cannot be made in the absence of reliable financial data that is prepared and presented in a timely manner. Regular analysis of your financial status will assist in ensuring that all revenue opportunities are maximised and costs managed for the maximum benefit of your business.

Should you wish to find out more about business recovery and turnaround services for your organisation, please contact your local BDO Kendalls adviser.



Greed is not good, Mr. Gecko

Kieran Netting, Director, BDO Kendalls, Melbourne

The current financial markets situation is the result of incentive mechanisms that rewarded excessive risk, driven by greed and self-interest by both investors and the financial engineers housed in Wall Street investment banks.

In Oliver Stone's 1987 movie, 'Wall Street', the leading character, Gordon Gecko delivered the movie's memorable speech to the Teldar Paper shareholders. It went like this:

"The point is, ladies and gentleman, that greed – for lack of a better word – is good. Greed is right. Greed works. Greed clarifies, cuts through, and captures the essence of the evolutionary spirit.

Greed, in all of its forms – greed for life, for money, for love, knowledge – has marked the upward surge of mankind. And greed – you mark my words – will not only save Teldar Paper, but that other malfunctioning corporation called the USA."

If you recall the movie, greed got the better of everyone as they embarked on a series of transactions, otherwise known as insider trading. Of course, the movie ends with Gordon Gecko being exposed as an inside trader, and who no doubt, spent many years in prison as a result.

So, Mr Gecko, greed is not good is it?

The point is that incentive systems tend to drive individual behaviour. Where we are heavily incentivised to assume excessive levels of risk in the hope of extra-ordinary rewards, we tend to ignore the downside risk and focus on the potential gains, leading to poor choices and poor investment decisions.

The road to where we are today – How did we get to where we are now?

To ease housing affordability in the US, easy credit was provided to those people who could ill-afford it (otherwise known as 'sub-prime' loans). The US Banking system, being highly fragmented and competitive, aggressively promoted the new low-doc lending opportunity in the pursuit of corporate profitability.

Sub-prime loans were characterised by minimal financial disclosure and a low 'honeymoon' rate of interest. The volume of loans was so large that the risk profile of the bank's balance sheets had taken a turn for the worst, putting the Bank's credit rating at risk.

Investment bankers saw the opportunity to securitise these mortgages into products called Collateralised Debt Obligation (CDO). CDO's diversified the risk to achieve a credit rating that allowed for these products to be sold to other financial institutions and investors. It also achieved the dual purpose of taking the loans 'off the balance sheet' of various banks.

Rapid rate rises in the US (1% to 5.25%), combined with the re-setting of the 'honeymoon' rates, led many home-owners to default on their repayments. Banks started to foreclose and sell people out of their houses.

Major financial institutions in the US were now collapsing. In this environment, counterparties scrambled to understand their exposure to those that had fallen. Banking stocks were marked down by investors. Banks didn't trust one another and inter-bank lending came to a complete standstill. Financial markets could not operate. Markets hate uncertainty and so, the broader equities market was marked down heavily.

On 29 September 2008, the DJIA lost 777 points, the biggest one day fall in history! The outlook for the US economy rapidly deteriorated in the space of days – the United States Treasury and the United States Federal Government stepped in to propose a Financial Rescue Bill.

Where we are heavily incentivised to assume excessive levels of risk... we tend to ignore the downside, leading to poor choices

Financial Rescue Bill

The original intention of the Bill was to allow a Treasury-controlled company the ability to purchase non-performing assets from financial institutions; reducing the risk of a financial market collapse.

The original Bill was not passed by the US House of Representatives (thus the 777 point fall in the DJIA) and was subsequently revised, and on 3 October, was passed in the House providing the US Treasury Department with a US\$700 billion bailout package. Unfortunately this did not stabilise the equity or credit markets. Equity markets continue to be sold-off. Credit markets remain frozen, as evidenced by an even higher cost of funding (LIBOR). It was anticipated that the reverse would occur. Going forward, investors should monitor LIBOR, because until it lowers, financial markets generally will maintain their negative bias.

Global Economic Slowdown

In terms of the broader global economy, we've seen:

- capital investment and infrastructure programs put on hold (after all, who will fund them?);
- demand for commodities reduced substantially (as reflected in share prices of BHP and RIO recently); and
- oil price free-falling.

A synchronised global recession is upon us. In Australia, whilst we are in a relatively strong economic position, many consider that if we're not already in recession, a recession is nonetheless inevitable. Of course, this sort of economic picture is negative for global equities. Not until such point that valuations fall to attractive levels (to justify the equity risk premium) coupled with increased liquidity levels in credit markets will global equities maintain a sustainable rally. In the meantime, we think that cash, government bonds and high yielding corporate fixed interest will be well supported.

But remember, and this is important, equity markets tend to precede economic activity – they will rally when they look through the current economic situation to see a revived economy. The investor who tries to time this eventuality is foolhardy.

Unfortunately if the client is overweight in any particular asset class, the effects have already been felt. This is particularly distressing for retirees and those who may be approaching retirement as the balance of their superannuation funds have fallen.

The Learning: Greed Is Not Good, Intelligent Asset Allocation Is!

Strategic and Intelligent Asset Allocation is proven to dramatically minimise the risk of an individual's investable portfolio without an adverse impact on returns,

We would advise clients to take decisive action in this environment and manage your financial situation. In times like these, your adviser is your most valuable ally. Work with your adviser to re-balance your investment portfolio in line with your particular financial objective. And remember, this needs to be a dynamic process going forward.

We strongly recommend that you consider the following:

- re-test your assumptions around your tolerance for risk. Having now lived through and experienced some massive volatility, ask yourself the question: "How do I really feel about this?";
- if you don't have a financial and investment strategy, you should get one;
- if you do, re-weigh your asset allocation according to your answer to 1 above. This is a personal decision, as most will struggle to want to realise losses in risky asset classes; and
- stick to your strategy. Regardless of the trigger, economic slow-downs and negative investment markets are a part of the natural business cycle. We've had them before, and we'll have them again. Just as we will have economic booms where holders of risky assets will be rewarded. As any backward looking analyst will demonstrate, in the long-term, markets reward an appropriate degree of risk. Ensure your portfolio is invested in line with your capacity and your willingness to assume financial risk.

If you're in need of financial or investment advice, please contact your local BDO Kendalls financial adviser.

Rise of fraud in the current economic climate

Andrew Howard, Manager, BDO Kendalls, Brisbane

The current economic environment and the difficulties presently facing many Australians and businesses alike has been well documented of late. However, will a slowing economic environment result in an increase of fraud?

When considering whether there is a direct link between a slowing economic environment and an increase of fraud, one must consider the underlying motivations of why people commit fraud.

The BDO not-for-profit fraud survey released in 2008 indicated that the two most common motivations of fraud were financial problems and/or pressure (representing 28% of reported cases), followed by the desire to maintain a lifestyle (representing 16% of reported cases).

Please refer to Table 1 to view the full results of the comparative motivation behind fraud committed survey.

TABLE 1 – COMPARATIVE: MOTIVATION BEHIND FRAUD COMMITTED		
Motivations	2008	2006
Financial problems/pressure	28%	26%
To maintain a lifestyle	16%	19%
Gambling problem	11%	10%
Family pressure	5%	4%
Revenge against the organisation	3%	17%
Lack of appropriate compensation/rewards	2%	0%
Drugs	2%	3%
Other	25%	21%
No response	8%	0%

The results of the Association of Certified Fraud Examiners 2008 *Report to the Nation*¹ indicated that the two major motivations and behavioural patterns underlying fraud was

¹2008 *Report to the Nation*. Copyright 2008 by the Association of Certified Fraud Examiners, Inc.

individuals living beyond their means which represented 38.6% of cases reported, and individuals facing financial difficulties representing 34.1% of cases reported.

TABLE 2 – BEHAVIOURAL RED FLAGS PRESENT DURING FRAUD SCHEME (SORTED BY FREQUENCY)			
Behavioural Red Flag	# of Cases	% of Cases	Median Loss
Living beyond means	370	38.6%	\$250,000
Financial difficulties	327	34.1%	\$111,000
Wheeler-dealer attitude	195	20.3%	\$405,000
Control issues	179	18.7%	\$250,000
Divorce/family problems	164	17.1%	\$118,000
Unusually close association with vendor/customer	146	15.2%	\$410,000
Irritability, suspiciousness or defensiveness	130	13.6%	\$180,000
Addiction problems	128	13.3%	\$225,000
Past legal problems	83	8.7%	\$184,000
Past employment-related problems	76	7.9%	\$163,000
Complaining about inadequate pay	70	7.3%	\$132,000
Refusal to take vacations	65	6.8%	\$250,000
Excessive pressure from within organisation	62	6.5%	\$388,000
Instability in life circumstances	47	4.9%	\$58,000
Excessive family pressure for success	40	4.2%	\$90,000
Complaining about lack of authority	35	3.6%	\$120,000

Do organisations need to be more vigilant against fraud in the current economic climate?

With the two major motivations for fraud being financial pressures and individuals living beyond their means, it is reasonable to suggest that organisations should be more vigilant in a slowing economy, particularly when individuals are experiencing increased financial pressure.

In short, we would always recommend that organisations be aware of the potential for fraud and do everything in their control to implement both fraud detection and prevention measures.

Detection controls will help detect a fraud after it has occurred, while prevention controls will help prevent fraud from occurring. Regardless of the size of an organisation, being proactive against fraud is imperative.

Further tips to enable an organisation to develop a proactive approach against fraud are as follows:

- the development of a Fraud Control Policy and Whistleblower Policy;
- undertaking a Fraud Risk Assessment at least every two years; and
- review controls regularly.

In particular, the review of controls (and the processes surrounding them) is important for any organisation.

During an economic downturn, it is not uncommon for organisations both large and small to consolidate job positions and/or not replace staff that may have ceased employment or moved to other areas of the organisation.

Furthermore, organisations may be forced to decrease the number of staff employed, and therefore should be aware that there will potentially be a decrease in the segregation of duties, especially in key areas such as financial operations.

As segregation of duties diminishes, especially when responsible for financial operations, there is an increased risk of fraud occurring. Segregation of financial duties will prevent an individual having complete control and therefore the potential for fraud diminishes.

Take for example an organisation that has one employee, who authorises all expenditure, prepares and makes all payments and finally completes the bank reconciliations. This organisation is susceptible to an increased risk of fraud occurring (due to a lack of segregated duties), as opposed to an organisation that segregates these duties between a mixture of employees.

The effect of fraud on an organisation can be devastating. When considering the cost of a fraud on an organisation, most of us would generally only consider the initial cash that has been stolen.

However, organisations should also be aware of the additional costs of fraud. There are a number of additional costs to a fraud, including the often overlooked constraints a fraud can have on debt covenants.

At present, many organisations are faced with increased pressure to meet their debt covenants. Potentially, as a result of a fraud, an organisation may be faced with the situation that they are no longer able to meet their required debt covenants.

Moving forward

With the two major motivations for fraud being financial pressures and individuals living beyond their means, and businesses tightening their belts through consolidating employee roles, organisations need to be vigilant during the current economic climate.

However, we suggest, regardless of the economic environment, organisations should be aware of the potential for fraud and do everything in their control to implement both fraud detection and prevention measures.

To find out more about how you can implement fraud detection and prevention measures in your organisation please contact your local BDO Kendalls adviser.

Designing your organisation for sustainability & increased productivity

Karina Collins, Partner, BDO Kendalls, Brisbane

Increasingly we are learning from the market that untapped productivity is a symptom of poor or little organisation alignment which is not only hampering our efforts to execute on strategic goals; it is also decreasing the sustainability of our organisations.

In the current economic conditions, organisations have to be operating at their best. Untapped productivity is neither affordable nor acceptable.

Overwhelmingly the lead indicator of untapped productivity is how the organisation is designed. So how do we tackle this issue? How do we design our organisations to:

- break down operational silos;
- get rid of inefficiencies in how we do things;
- empower our people to encourage high performance; and
- continuously increase shareholder value.

How do we design our organisations for increased productivity and sustainability? The following is a five step approach to assist your organisation.

Step 1 = Strategy

For any organisation to develop or make changes to work performance, business owners and managers must first understand the strategic goals of the business, and how to operationalise longer term goals into short term work packages or projects. Implementation of strategy starts with:

- communication of the plan;
- understanding the capacity and capability of the organisation to implement the changes the plan calls for; and
- aligning teams and individuals to the associated change process.

Step 2 = Structure follows strategy

The business structure will be dependent on owner aspirations, complexity or requirements of the operating entities and the countries or regions in which the business operates (and in what capacity) or trades.

The organisational structure is the way in which roles and responsibilities are organised into: team, work groups, or individual levels to carry out the work of the business. The most common being:

- hierarchical with centralised support services;
- self-contained units with decentralised support services;
- functional matrix; and
- process-based.

Leading organisations understand the link between managed innovation and increased productivity. Current research shows that these organisations:

- have a decentralised management structure;
- separate core and support services;
- establish strategic partnerships to acquire or leverage intellectual property;
- have structured teams and networks for idea creation and collaboration; and
- provide access to resources to commercialise innovations.

Step 3 = Roles

Every role within an organisation should be aligned to the strategic goals of the business by:

- establishing strategic responsibility at a role level (qualitative);
- identifying role related critical success factors (qualitative); and
- assigning key performance indicators or outcomes that can be used to measure performance against agreed goals or critical success factors (quantitative).

Leading organisations embed performance measures in every role to encourage organisational behaviours that drive sustainability.

“In the current economic conditions...untapped productivity is neither affordable nor acceptable.”

Step 4 = Process

Organisational capital often resides in the unique processes and techniques adopted to run the business on a daily basis. Efficient processes are critical to ensure value is identified, protected and leveraged. Leading organisations will:

- understand and leverage unique and value adding process or techniques;
- embed work practices for continuous process improvement;
- identify risks and formulate internal control system; and
- understand the relationship between process and organisational sustainability.

Step 5 = Technology

It's simple – invest in technology that will meet the needs of the business (once you understand what those are). Don't do the reverse and invest in technology before you understand what the business needs – that will only result in the business forever being dictated to by the technology that underpins it.

Technology, as an enabler of business strategy, can help a business realise sustainability and productivity through its application to work practices and opportunities for continuous innovation.

To conclude

Organisational design must be strategy-led. A primary outcome of organisational design is through its alignment of Structure (business and organisation), Roles, Process, and Systems.

A key driver in the overall design (and one that will mature in time) is linked performance management to establish, recognise and appropriately manage or reward organisational, team and individual outcomes.

For more information on ways to increase productivity and implement strategy led sustainability in your organisation please contact a BDO Kendalls Performance Improvement Consultant.

Risk management – the big picture

Marita Corbett, Partner, BDO Kendalls, Brisbane

In today's business environment risk management is a 'must have' for all organisations. Since the introduction of Australian Standard AS/NZS 4360 Risk Management, and the COSO Enterprise Risk Management framework, risk management is clearly something that cannot be ignored.

Organisations are achieving reasonable success in establishing governance structures, frameworks and processes and implementing these in areas of financial and core business risk. However, limited advancement in integrating processes at all levels of the organisation is being realised; integration across operations and functions should include non-core, non-financial, operational and less traditional categories of risk.

To be successful in implementing an Enterprise Risk Management framework, organisations must tackle this project on two fronts:

- vertical integration – Developing strategic drivers and alignment; and
- horizontal integration – Taking a 360 degree organisation perspective.

Boards and CEOs want three things from their risk management programs:

1. a proactive approach that focuses on more than just the hazards;
2. a truly holistic discussion of the various risks in terms of how the organisation should operate and what they as the Board and senior management should be concerned about (rather than a compendium of risk reports from all business units); and
3. more robust ideas about how to better run their businesses.

The goal of an enterprise and organisational wide effort is to gain a competitive advantage. By looking at how risks might impede the achievement of strategic objectives and then working to establish a system to keep that from happening.

For that system to work, risk management must be intrinsically linked to the organisation's business strategy, therefore encompassing the organisation's:

- established vision, mission and objectives;
- process for defining operational imperatives; and
- philosophies, policies, plans and initiatives for growth and development.

Organisations achieving enterprise and organisational wide perspectives are reporting significant added value to:

- governance and accountability;
- planning structures;
- frameworks for better informed and more insightful decision making;
- tangible and intangible asset protection;
- identification and exploitation of opportunity; and
- regulatory compliance monitoring and assurance.

When all is said and done - effective risk management is about people performing better. A formal framework applied across the entire organisation promotes daily discipline and focus by putting staff members through a discrete exercise that forces them to think outside the box. Because this process is built into the way the organisation conducts its business, it isn't something that people only do once and never again.

Should you wish to find out more about developing a risk management framework for your organisation, please contact your local BDO Kendalls adviser.

Sectors in the spotlight

Challenging conditions for the Resource Industries

Sherif Andrawes, Partner, BDO Kendalls, Perth

The favourable market conditions of the past, easily accessible capital markets, strong commodity prices and growing international demand for Australian commodities, meant that the number of resource exploration companies increased dramatically during the course of the commodity boom. However, the current market conditions are proving a challenge for speculative resource companies.

Why some resource companies are hurting

Almost overnight, demand for natural resources fell in line with global economic growth, and projects that were attractive prospects 12 or 18 months ago are no longer feasible as the bottom fell out of commodity prices. As a result, the days of cheap capital raisings and easily accessible debt are over and with market participant's appetite for risk having evaporated, speculative companies with limited income streams are finding it difficult to raise the cash required to continue their operations.

If junior explorers do in fact have a feasible project, regardless of the perceived quality of these assets, the fact that they are non-producing means that they are a risky proposition to investors. With a low appetite for risk in equity markets and market sentiment the lowest it has been in decades, the issues affecting global capital markets are exacerbated for exploration and speculative resource companies trying to raise cash. Companies find themselves weighing up the cost of raising cash in the current market to fund exploration and project development, or alternatively, sit on their assets and cut all discretionary expenditure (including exploration) in an attempt to ride out the storm.

Riding the storm

The issue with riding out the storm is that from the viewpoint of a speculative investor, there is nothing speculative about investing in a company that doesn't generate revenue and that isn't actively exploring. Similarly, deferring equity raising is at the risk that capital markets deteriorate further. The average junior explorer might need around \$6 million to continue exploration work for the next two years; made up of \$1 million for administrative expenses, at least \$2 million per year for exploration and up to \$1 million for unforeseen expenses. Few junior explorers have sufficient cash to support this.

Speculative resource companies are trying to raise cash in a market where there is a very limited demand for the investment that they are offering. To make matters worse,

when debt funders review existing debt facilities, the terms of facilities are being altered or even withdrawn, inducing huge additional costs for companies that already have limited cash and no income stream. Similarly, given that share prices are at a 5 year low, consideration must be given to companies' capital structure which generally speaking, has changed dramatically over the past year.

A number of recent capital raisings in equity markets by perceivably safe companies is illustrative of the fact that equity issues by speculative companies would attract little interest from investors or, at the very least, would require a considerable discount and result in significant dilution for current equity holders.

Carefully consider the options

A common solution to conserve cash has been to defer payments to bondholders and cash raisings have generally been in secondary markets. Both of these options are expensive propositions that will undoubtedly have an impact on future earnings. The difficulty in finding cash has led to a number of companies resorting to issuing convertible notes. For the holder of these notes this represents a relatively attractive proposition.

Should the current market conditions improve and the company's share price appreciate, note holders are exposed to the upside of the note's equity component. An alternative option is to approach bigger companies and negotiate alternative arrangements such as farm-ins or a joint venture to develop projects or approach acquisitive companies with cash holdings about the prospect of being taken over.

In light of these issues, in the current market management face a dilemma. Management is confronted with a trade-off between dilution, financial viability and future earnings. A choice must be made between issuing securities at a significant discount resulting in a dilution of assets, being acquired cheaply by another company at the expense of shareholders or paying a large risk premium to access debt facilities at the expense of future returns. Essentially, it is only the size of this trade-off that will vary between companies as determined by the company's marketability and asset quality.

For further information on how our Corporate Finance team can assist with solutions for your organisation, please contact your local BDO Kendalls adviser or visit our website.

Dealership focus on profitability

Brett Fowler, Partner, BDO Kendalls, Melbourne

With just over one million sales, 2008 proved to be the second highest market in automotive history! That however is in the past. Most predictions for 2009 are for 'tough times' ahead.

The automotive industry has come under significant scrutiny in the media with predictions that the economic downturn will have a greater affect than in other industries. This view has been widely reported, as issues regarding the viability of vehicle manufacture in Australia, the lack of available wholesale finance, fuel prices and environmental issues have all been reported as affecting all elements of the industry equally, and not offering any clarity with regards to the long term consequences of these issues.

Fuel Prices

The cost of fuel had a twofold affect on vehicle buying behaviour. It had the effect of modifying consumer buying habits away from large 6 cylinder vehicles to smaller, more fuel economic 4 cylinder vehicles. This had a significant effect on vehicle manufacturing in Australia, as Holden & Ford produce only 6 cylinder vehicles in Australia and Toyota also produces 6 cylinders (but not exclusively). This change in preference by customers was already well established, but the rapid rise in fuel costs has significantly accelerated the change. This change in consumer preference has already seen both Holden and Ford announce plans to build 4 cylinder cars for the Australian market.

Environmental Issues

The high cost of fuel also generated debate about reducing the environmental impact of vehicles. Support for alternative fuels has become more widespread and there has been increasing criticism of manufacturers for not building more environmentally friendly vehicles.

In light of this, all manufacturers have announced that development in alternative energy vehicles has been brought forward. Confusion still surrounds the actual demand for these vehicles due to the higher cost, while the cost of petrol has fallen considerably. It appears that manufacturers are committed to the production of these cars, as long as government support is aligned with alternative energy options.

Finance

With the withdrawal of automotive financiers GE and GMAC (and the partial withdrawal of Ford Credit) from the finance market, much media speculation focussed on the imminent bankruptcy of a significant number for dealers. Much of the media coverage failed to highlight that wholesale finance of vehicles by dealers is the usual way of business. GE & GMAC's withdrawal reduced available credit in the market for dealers to operate by over 30%!

Following significant lobbying from the automotive industry, the Federal Government has set up a trust to the value of \$2 billion (funds contributed by the Big 4 Banks) to cover the shortfall in market liquidity. These funds are expected to be used by the existing automotive financiers to cover the wholesale finance requirements of ex-GE & GMAC dealers over the next 12 months. At which time the fund will be wound down and existing automotive financiers will fund the wholesale market.

Sales volume

A fundamental principle of the car business is sales volume; the lifeblood of the business is turnover. The industry has been on a path of increased volumes for many years - that is until the second half of last year.

Firstly, the concern over fuel prices prompted the consumer market to review the type of vehicles they drive because of fuel consumption. This was then coupled with environmental concerns and alternative energy propulsion. The media proclaimed that car dealers were not selling what people wanted and used the significant fall in large car sales as proof.

The fact is that in 2008 the second highest number of new vehicles was sold and although 2009 is predicted to be a significant drop (some journalists have commented as much as 12%) in volume, 880k – 900k units in 2009 would still be equal to 2003's sales figures of just over 900,000 units.

Market growth has largely been driven by a 'supply push' from manufacturers and distributors. Increasing incentives and increasing targets coupled with easy availability of retail credit, have seen the automotive market increase significantly over the last five years. During this period, average dealer profitability has been under increasing pressure. In fact, the anticipated decline in volume will likely force a reappraisal of the fundamental structure of dealership profit centres.

Strong volumes over the last five years have disguised the need to address expense control, profitability and performance issues. The old adage of 'volume hides many sins' has truly been the case with the automotive industry. Focus has been on increasing throughput and not improving profitability.

The considerable experience of the BDO Kendalls dealership team has taught us that Dealerships review and modify their business in line with the predicted fall in volume and focus on continually looking for ways to improve their return on investment.

Should you wish to know more about dealership profitability, please contact your local BDO Kendalls adviser.

Six steps to stay on track

To obtain your copy of 'Six steps to stay on track', visit our website to download the PDF at: <http://www.bdo.com.au/sixsteps>



Dealing with economic turbulence

- ▶ 1 **Monitor cash**
- ▶ 2 **Be proactive: Take fast and decisive action and develop a comprehensive approach**
- ▶ 3 **Prepare targeted and timely reporting**
- ▶ 4 **Know your lender, creditors and stakeholders**
- ▶ 5 **Understand your fiduciary duties to creditors**
- ▶ 6 **Get outside help**

Victorian bushfire appeal

Bushfire relief – Operation Angel

The BDO Kendalls Melbourne office went into immediate action to support the bushfire survivors, and through director Brett Fowler, became part of a larger initiative called Operation Angel.



Operation Angel was led by Jacqueline Pascarl, who has had significant experience providing aid relief in war torn countries. As a result of her experience and untiring efforts, Operation Angel was a huge success, largely based

on being able to get immediate and direct aid to those in need, making a real impact for hundreds of families.

Some of her account is detailed below:

“This pyro destruction is much, much worse than the war zones in which I have worked, mother nature has consumed everything that was combustible and the emerging evidence of arson makes the tragic outcome of 7000 homeless and hundreds dead a terrible fact to confront.

Have you ever seen a movie where a long fuse is lit and we watch as the flame whooshes along the wick until the explosion? Well, multiply

the width of that wick by one million, and that will give you an idea of the breadth and speed of the destructive fire's path as it cut a swathe up and down the rolling valleys on the edge of town. Blackened trees, denuded of foliage stood to attention on the greyed and ash covered slopes that filled the views from our vehicle windows as we made our way to the distribution point. Destroyed homes, desolate and collapsed, still smoked exhaustedly at the road's edge.

Our trucks, stuffed to the gunnels with meticulously folded and sorted (pre-loved) clothing – from a massive collection of donations from the Rialto building co-ordinated by the staff of BDO Kendalls, well stocked and individual hygiene and toiletry packs, \$150,000 worth of new GazMan clothing, a semi-trailer load of toys, fold out kids couches, new clothing for families valued at \$200,000 all from Funtastic, and over four thousand new items of underwear and sleep wear from Mitch Dowd, ensured that all twenty of our fabulous volunteers, felt like Santa Claus on steroids.”

This tragedy will require long term support from the community. Remember you can continue to assist by donating time, money or blood to The Red Cross, a most worthy organisation to be entrusted with the management of the funds and community relief efforts – www.redcross.org.au

McGrath Foundation

BDO Kendalls supports the McGrath Foundation

Over the last few years, BDO Kendalls staff have spent October/November donating their money and time to a range of activities aimed at raising funds for breast cancer research, education, awareness and support.

Each year a number of events are held in our offices nationally. Through these events, we aim to help raise awareness of breast cancer, as well as raise funds.

The recipient of funds raised by our 2008 activities was the McGrath Foundation, supporting the valuable work they do in funding McGrath Breast Care Nurses in communities right across the country. The impact that these nurses can have on a patient's physical and mental wellbeing during and after treatment is immense; allowing them to voice their frustration and emotions to someone outside of their immediate family, and provide someone who can give informed and knowledgeable answers to their questions or concerns.

Through activities such as Bandana Day, the Miss BDO pageant, morning teas and cocktail function and auction, we were thrilled to raise over \$21,000 - an overwhelming majority of which came directly from the pockets of BDO Kendalls staff.



As a warm up for 2009's activities, staff from our Sydney office also took time out from their summer holidays to volunteer for the McGrath Foundation during the New Year's Test Match at the SCG. The volunteers sold wristbands and collected donations over the course of the test match, where Day 3 - traditionally 'Ladies Day' - was renamed in honour of Jane McGrath.

Our thanks to all staff - and also those clients - who generously contributed to our record total. We look forward to bettering it in 2009!

For more information about the McGrath Foundation's activities, please visit their website: www.mcgrathfoundation.com.au



From left to right: Matt Fulton (Coca-Cola Amatil), Glenn McGrath, Matt Leivesley (BDO Kendalls Sydney).

Introducing our newest Partners & Directors:

The partners and directors of BDO Kendalls are pleased to announce the following partner and director appointments.



Rocco Angerosa
Private & Entrepreneurial Clients
Melbourne



Raj Deepan
Private & Entrepreneurial Clients
Sydney



Iain Kemp
Audit & Assurance
Sydney



Dennis Lin
Corporate & International Tax
Brisbane



Nick Michael
Audit & Assurance
Melbourne

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