Chart a back-up course or risk going under

By Tony Wanless

LESSONS

Have plans in place to deal with possible scenarios. The plans may never be used but become invaluable if the need arises.

Build a reserve. When pulling together strategies, everybody likes to say they're being conservative and managing risk. But they still often operate close to the edge.

Expect to be blindsided. Protective social systems can bring a false sense of security to the business arena. But business is dynamic, so expect to be jolted at some time by some unexpected force.

Chart a Backup Course

PROBLEM: Operating a business too close to the edge without a safety net

SOLUTION: Plan early, consider every potential scenario, and come up with a Plan B, C and D.

When launching any new venture, the first thing to do is to form a business or strategic plan. There's a well-established process for this, aimed at painting a detailed picture of how the business will be operated, marketed and funded well into the future.

A new tool is increasing being added to this planning process: scenario planning, which originated with the military but has spread to the corporate world as a proven risk-management method. A company scans the business landscape in which it hopes to operate and writes up "stories" involving various business scenarios. It maps out possible future problems and devises solutions in case they're needed. It creates a Plan B, and often a Plan C, D and E.

PROBLEM

Sounds like a good idea, doesn't it? And it is. Except, of course, that very few companies bother. Entrepreneurs are optimists and don't like the negativism associated with scenario planning; risk management is something few want to think about.

But they should. Failure to do so can often mean disaster down the road when the proverbial "shit happens" that they preferred not to think about.

A good example is the HarbourLynx high-speed passenger ferry service between Nanaimo and Vancouver that went belly-up in March after the engine on its only vessel conked out. Awash in $4 million in debt and drifting without a revenue source, HarbourLynx had no choice but to go under.

That was a far different outcome than what the company had projected in October 2003 when investors, most of whom were successful small-business people in the Nanaimo area, saw increasing numbers of people moving ot the Island but still working in Vancouver. They put that together with the spotty and expensive BC Ferries service between the two cities and came up with an enthusiastic plan: offer a foot-passenger ferry service for all those commuters and others who want to travel between mid-Island and downtown Vancouver.

But a transportation business isn't easy to set up and it's even harder to operate -- ask anyone who has tried to run a private airline or bus company. They require lots of money to start up, operate and keep going through the ups and downs of the marketplace. There are employees to feed (35 in HarbourLynx's case), masses of regulations to satisfy and, of course, competition – usually from some entrenched competitor no eager to release its grip. In this case, that was BC Ferries, a Crown corporation that can easily continue to fund operations when times get tough – and enjoys government subsidies such as reimbursement for providing free service to seniors.

(NON) SOLUTION

HarbourLynx investors weren't completely starry-eyed. They did recognize they were up against a large competitor, but their analysis convinced them there was a niche for a quick ferry service between just two points. They had a plan: build a focused operation positioned to take advantage of the growing traffic between Vancouver Island and the big city. It was a Plan A. But apparently there was no Plan B.

Of course, the inevitable problems soon appeared Directors of (and investors in) the company, almost all of whom were part of the core business community of Nanaimo, presumed that their familiarity with local bankers would make securing a loan to buy a ferry a snap. No so. Bankers might be buddies on the golf course but when it comes to lending, they get very conservative.

Most took one look at the business plan and passed. So the new company had to go to the private lending market for start-up funds, which involved a higher interest rate. That added to operating costs. Then there was the competition. HarbourLynx presumed it would receive subsidies for seniors the way BC Ferries does, but the government refused – it was, after all, a private company competing with one of its own.

The new company also needed a boat, and the owners thought big. Presumably with an eye on expansion, they bought a 300-passenger ferry – far bigger than what was required. The big boat burned up to 1,000 litres of fuel per trip – at three trips daily, it was running through nearly 3,000 litres of fuel each day. This was doable at 40 cents a litre, but when fuel costs doubled, expenses soared.

There was also the government to contend with – in this case the provincial tax collector, which decided that the Nanaimo Harbour Links Ferry Corp. owed a half million in taxes on the boat, rescinded its claim, then changed its mind and re-issued the tax bill.

Lastly, there was the little matter of revenue: In 2005, the ferry service shuttled covered start-up and operating costs. But unforeseen expenses such as the tax bill, rising fuel costs and a potential doubling of docking fees impacted the bottom line considerably.

A breakdown of that revenue showed a clear growth problem. The ferry serviced about 100 regular commuters who generated around $1.3 million a year in with the rest drawn from tourists and Islanders who took occasional trips to the city for special events. The problem? One hundred was th eceiing for commuter traffic, so the company had to depend on the ficle tourist and day-tripper market if it was to grow.

The HarbourLynx venture faced a host of problems:

- It was underfunded
- It faced deep-pocketed competition
- It operated a gas-guzzler in a rising fuel-cost environment
- It hit a growth ceiling
- It lacked operational flexibility
- It was governed by a board of directors whose full-time businesses absorbed most of their focus

Was the board worried about these obvious problems at the outset? Apparently not, because it did little to correct them. Director John Cavers, a veteran of many business start-ups who was the last man standing when the company capsized, did convince many increasingly skittish investors the company needed a smaller more efficient ship. That would leave the original ferry to act as a reserve if there was a problem.

Ironically, HarbourLynx directors were in Tacoma, Washington, to look at a boat and activate this makeshift Plan B when word came that the HarbourLynx ferry's engine had failed, and all revenue had dried up. Investors jumped ship and it didn't take long for creditors to sink the company into bankruptcy.

HarbourLynx went down after only a couple of years. Early scenario planning might have save the ferry service, but nobody, it seems, saw the need for a lifeboat.