The 6 Untold Reasons Why Businesses Fail

Written by Dave Lavinsky on Thursday, March 6, 2008
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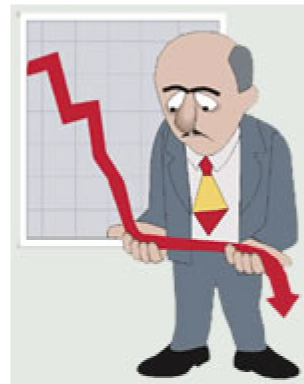

There have been many articles written on the subject of why businesses fail, and most of them point to the same reasons, such as:

-Inadequate funding
-Bad location
-Lack of a well thought-out business plan
-Poor execution
-Bad management
-Expanding too quickly
-Insufficient marketing or promotion
-Inability to adapt to a changing marketplace
-Failure to keep overhead costs low
-Underestimating competitors

These reasons are widespread and no doubt cause many businesses to fail. However, the reason for a company's failure is not always something so obvious. Here are 6 lesser-known reasons why a business might fail.

Why do these reasons remain untold? Simple. Most of the time, the business owner doesn't realize that these reasons are what caused their failure, and consultants generally don't ask the kinds of questions that would identify them.

1) Focusing on Short-Term Profits Rather than Building Long-Term Value

It's important to be profitable, but NOT when short-term profits come at the expense of the long-term value of the business and the lifetime value of the customer.

Here's a real-life example: In the late 1990s, there was a franchise of a national smoothie shop located in West Los Angeles, CA. At this store, smoothies sold for about $4. They cost only around $1 to make, resulting in a solid profit. However, certain ingredients, like mangoes and berries, cost more than the other ingredients, such as juice and frozen yogurt. Since juice and frozen yogurt were cheap, the franchisee put more of these ingredients in their smoothies and less of the expensive ingredients. By doing this, their profit margin per smoothie grew by approximately 20 cents, which seemed great… on paper. Unfortunately for the store, customers weren't satisfied with the taste of the lower cost smoothies, people stopped going there, and the store eventually went out of business.

As you can see here, it's important to consider the lifetime value of a customer. Repeat business is way more valuable than short-term profits. Saving 20 cents on a smoothie today will cost you big in the long run.

(Another great example of this concept is Google giving preference to relevant ads in order to improve the user experience, even though there are less relevant advertisers willing to pay **a higher price** per click.)

2) Ego Business vs. Business Opportunity

The foundation of a good business is a good business opportunity. As an entrepreneur, you want to fill a need in the marketplace. Unfortunately, many businesses are started solely to fulfill an entrepreneur's ego (or, to put it less harshly, to satisfy one of the entrepreneur's interests).

This can often be seen in the restaurant & bar industry, where too many entrepreneurs open shop because it's a "cool" thing to do. Such businesses rarely succeed.

3) Life distractions

The best ideas don't always come between 9 and 5. A person might have a great idea while driving, or in the shower, or while working out. It's moments like these when an entrepreneur leaves behind the day-to-day tasks of running a business and gains a better perspective of the big picture.

Sadly, there are a lot of things that can disrupt a person's home life. Illness, death of a family member, divorce, relationship trouble, and problems with a child are just a few of the many issues that can affect a person's mindset. When things like this occur, moments of clarity are replaced by stress and anxiety.

Many entrepreneurial ventures depend heavily on new ideas and creative thinking, and when an entrepreneur's head isn't clear, business can suffer.

4) Bad feedback & white lies

People like spending time with friends and family.

Unfortunately, when it comes to business, friends and family members don't always give the best advice. This is especially true at the birth of a business. Nobody wants to be a buzz-kill. No one wants to tell an entrepreneur their idea is bad, or their location stinks, or anything else negative. Most people are conditioned to be supportive of their friends and family regardless of the situation.

Plus, nobody wants to be wrong. Imagine your friend has an idea that you think is terrible. You share your objections, but the friend goes ahead with the idea anyways, and it succeeds. Now you'll always be the naysayer that never believed in them. Nobody wants to be that person.

That’s why you’ll rarely get honest, object business advice from friends or family members. And yet, oftentimes friends and family are the first people entrepreneurs turn to for advice.

5) Maybe the owner is just a jerk

There are a lot of great people in the business world, but there are also some jerks. And these jerks sometimes start their own companies.

A jerk, in this case, is someone who a lot of people can’t get along with. Maybe it’s because they’re a super-perfectionist, or they yell a lot, or they demand that everything be done in a certain way, or they constantly complain. Or maybe they’re annoying in some other way.

The key is that nobody -- not employees, customers, partners, suppliers, clients, etc. -- wants to give 100% for a jerk. Clients and customers will be turned off, and employees will start cutting corners. Most people believe that life is too short, and don’t want to spend their time working with someone they can’t get along with.

6) The entrepreneur never took the full leap

In most new business attempts, the entrepreneur never leaves their day job, or they create a back-up plan, or they have a job lined up in case the new business fails. In these cases, failure IS an option, as the entrepreneur has a safety net to fall back on. In cases where failure is NOT an option, and the entrepreneur depends on the new business to provide food, shelter and clothing, the business has a greater chance of succeeding.

There’s a great example of this concept in **this recent NY Times article**. Xiang Yu was a third century (B.C.) General in the Chinese army. He led his troops into enemy territory by crossing the Yangtze River. Then, in order to inspire his troops, Xiang Yu took some unorthodox measures. He burned all of his troop’s ships and destroyed all of their cooking materials. This left the troops with only two options: Move forward and conquer the enemy, or perish. The maneuver did not make Xiang Yu very popular with his soldiers; nevertheless, the troops advanced and ultimately emerged victorious.

Xiang Yu’s methods might be a little drastic in this day and age, but the moral of the story is what’s important. Author Anita Roddick has said that entrepreneurship is a matter of survival, and the truth is, if you’re not totally committed to your business, your chances for success will be greatly diminished.