McGrathNicol releases Dick Smith report

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Dick Smith in Northland closes for the last time. Picture: Jake Nowakowski

DICK Smith had too much crap that it couldn't sell.

Administrator McGrathNicol has released its report into the collapse of the electronics retailer, pinning the blame largely on a series of massive inventory purchasing failures combined with an ill-thought out and costly expansion.

Prior to its successful listing on the stock exchange in late 2013, Dick Smith had enjoyed strong sales growth, underpinned by an expansion plan and new lines of business.

"In that environment, management were very focused on increasing revenue and generating profitability," administrator Joe Hayes said in a statement on Wednesday.

"This ultimately came at the expense of sustainable growth and the business struggled to maintain performance."

Dick Smith's expansion plans ate up all its surplus earnings and required significant borrowing at the same time as customer preferences began to change and the retailer began to lose market share.

The expansion plans "went unchecked" and major inventory purchasing decisions in early to mid-2015 "meant Dick Smith was carrying too much stock that was not saleable and was overvalued".

“By December 2015, a rapid clearance sale was needed at a time the business should have been achieving strong margins,” he said.

“However, cash receipts were simply insufficient to meet commitments. Dick Smith failed because the company did not have enough cash resources available to meet its current and future commitments.

“The appointment of the Administrators on 4 January 2016 was the only step available to the board and management.”

McGrathNicol said Dick Smith’s accounts to December 2015 indicate considerable losses in the six months to December 31 of $116.7 million.

“Those losses are attributable to poorer than expected sales and margins, inventory write downs, lease provisions and other asset impairments,” the report said.

Mr Hayes said the failure of Dick Smith represented an unfortunate end for one of Australia’s iconic retailers.

“The collapse was made all the more significant given its speed and scale, just a couple of years after the successful public ASX listing of Dick Smith, as well as the time of year, just following the Christmas period,” he said.

However, Mr Hayes said time would be needed to determine the real causes of such a rapid demise, and that the significant turnaround in the retailer’s financial position required a period of reflection and review.

It comes after receivers Ferrier Hodgson revealed 10 former Dick Smith managers and directors would be called to court to answer questions about the collapse of the company.

The Australian Financial Review reported that Anchorage Capital Partners’ Phillip Cave and Bill Wavish, who represented the private equity firm on the Dick Smith board until early last year, would be grilled on their roles.

Mr Cave, who had previously strenuously denied allegations that Anchorage had pulled off a so-called “private equity heist”, said he would co-operate fully with the receivers.

Anchorage bought Dick Smith from Woolworths for $20 million and made $500 million after floating it on the stock exchange nine months later. Dick Smith collapsed in January with debts of around $390 million.

McGrathNicol said total losses to creditors will be in excess of $260 million. The “substantial difference” between this shortfall and the $170 million book value of Dick Smith’s assets as at June 30 2015 would require “fuller investigation and reconciliation”.

“However, it is largely attributable to significant trading losses in 1HFY16, losses on the wind down of inventory during the receivership, and the very significant supplier and bank commitments,” the report said.

Around $2.1 million in historical staff underpayments remains outstanding but will be paid this calendar year. Dick Smith's lenders will receive some of what they are owed but are likely to suffer a "significant shortfall".

McGrathNicol said there was "no expectation" that unsecured creditors including gift card holders would receive any return "unless very significant recoveries are made in the liquidation process".

Responding to criticisms from the retailer's namesake entrepreneur describing the equity flippers as "greedy", "dishonest" and "immoral", Mr Cave said the firm had made "a significant investment in staff, stores, marketing and the operating systems" before the float.

Other former Dick Smith staff summonsed to face court hearings starting September 5 include former chief executive Nick Abboud and chairman Rob Murray, who is also chairman of retail wholesaler Metcash.

Ferrier Hodgson will question the group using powers under sections 586A and 597B of the Corporations Act. The securities regulator is also conducting its own investigation into the collapse.

The last stores closed at the end of April, with all of the more than 3300 staff paid their employee entitlements in full.

Online retailer Kogan purchased Dick Smith's online business from the receivers earlier this year, with the website relaunching in May.

WHY DID DICK SMITH FAIL?

• The consumer electronics market is highly competitive with rapid changes in consumer demand patterns.

• DSG had a store network much larger than its competitors, and so a higher cost base, with considerable exposure to and reliance on the fast moving office/computer products market.

• DSG was losing market share by experiencing declining comparable sales. Revenue growth was based on store growth and commercial sales at low margins.

• DSG's expansion plan required considerable financial commitment, utilised all cash resources, required considerable supplier commitment and required bank borrowings.

• Inventory decisions made in this environment were not consistent with consumer demand, and DSG was ultimately left with a considerable level of obsolete and inactive stock, requiring a major writedown.

• Clearance sales did not generate sufficient sales or margin to alleviate the cash pressure.

• Inability to obtain favourable credit terms impacted on stock levels, product mix and store presentation.

• Cashflow pressures led to banking covenants being breached that could not be remedied.

Source: McGrathNicol

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