



Credit risk management without the risk

Failure Rate Soars

It's an Ill Wind

It's not necessarily time to head for the hills, but it is rather worrying to read news reports that restructuring consultants at PwC have for some time been hiring in expectation of higher levels of bankruptcies.

The banks, too, are apparently taking similar action, while corporate recovery specialists Begbies Traynor are quoted as forecasting a bumper year (for them, that is!).

Of particular concern amongst these institutions are takeover targets – especially buy-outs – where debt levels may be unsustainable if economic conditions go against them.



First the good news. The growth in failures amongst UK companies slowed to 19.2 per cent in the third quarter of 2006 compared to the same period last year. That represented nearly 19,700 companies going bust or ceasing trading between July and September.

And that's as good as it gets. For the year to date, the latest D&B figures show that the rate of increase in corporate collapse is no less than 27.5 per cent, with a total of 59,315 companies going under in 2006 so far.

D&B's statistics show a bleak picture across the country: failures in the traditionally prosperous South East jumped by 26.3 per cent, while the comparable figure for the hitherto healthy South West was 25.3 per cent.

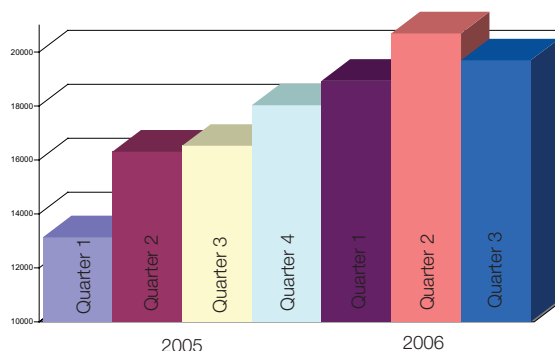
It's more pointed still in the West Midlands, long considered a powerhouse for the British economy. The cascade effect of high profile industrial majors ceasing production has contributed to a 34.5 per cent hike in the failure rate, while the North West – 38.3 per cent higher – is even worse.

Wales, where Cardiff and Swansea are frequently cited as models of regeneration, nonetheless has a failure record 44.6 per cent up on last year.

Commenting on the D&B figures Bob Lilley, managing director of CIFS said: "These figures mask a lot of pain for the principals, employees and, yes, the suppliers of the companies that have folded this year. And yet, a recent research report tells us that 60 per cent of companies transact business without conducting any credit checks at all.

"If ever there was a wake-up call for them, this is it."

UK business failures 2005-06



Export Risk

A new report from the Open University Business School's Enterprise Research Team shows that more than a third of the UK's small businesses are exporters, generating on average some 25 per cent of total sales from abroad.

Some 40 per cent of those exporting are selling to European countries and 12 per cent to North America, the next most popular market.

Highly commendable, but it's debatable whether all members of this new breed of exporters fully appreciate the additional credit risks they run when doing business overseas.

For example, payment performance of Italian companies is much slower than UK norms. And the incidence of business failures in France is significantly higher than at home, while obtaining accurate credit information, too, can be problematic.

For companies reaching the OU average of 25 per cent export sales there's a compelling case for insuring their invoice value.



It makes you think...

Elsewhere on this page we report on the latest D&B statistics covering business failures in the UK and the areas hardest hit. Another information group, Experian, has examined those sectors suffering most in the current climate and concludes that businesses in the plastics and rubber industries are having the toughest time, closely followed by food retailers. Failures are also up amongst building and construction companies. Overall, say Experian, on average some 80 companies fold every working day.





Light at the End of the Tunnel?

Better news for Britain's beleaguered retail sector has come with reports from Carpetright, the country's biggest carpet retailer, that rents may have peaked after a sustained period of steep rises.

"Rent increases are on a downward curve, based on the evidence we have seen this year," says the company. Property owners were lowering their expectations after enjoying a bonanza at the expense of retailers.

Earlier the British Retail Consortium had warned landlords that above-inflation rent hikes could seriously impact the financial health of many retailers. Now, property industry opinion suggests that the market has turned and shop rents could fall.

All of which may engender a feeling of "too little, too late" for creditors of failed furniture retailer Courts. Owed more than £300 million they can perhaps be excused a hollow laugh at learning that advisers have been paid more than £20 million since the company went into administration some 18 months ago.



Matalan Takes the Biscuit



The 2006 prize for sheer bald-faced effrontery is surely already won.

For if there's a more clear-cut case of using corporate muscle to squeeze suppliers unfairly than Matalan, we've yet to see it.

Citing "difficult trading conditions" the company has unilaterally extended payment terms and amazingly levied a retrospective "mandatory 2% contribution" from all suppliers – to be taken off outstanding invoices.

The fact that Matalan's suppliers may themselves be suffering from those same tough conditions seems to have escaped the company. For many, the situation is made worse by the fact that Matalan is no longer dealing with them, yet the arbitrary 2% deduction in invoice value is still being applied to debts incurred before the policy was introduced.

It's encouraging that small firms minister Margaret Hodge is now involved in an attempt to resolve the dispute. Otherwise the options for suppliers faced with this kind of corporate bullying will be to swallow the loss or seek a potentially costly legal remedy – either way a wholly unsatisfactory outcome.

Bob Lilley



Pensions Warning



A stark public warning from the Pensions Regulator's chief executive, Tony Hobman, has identified worrying examples of what could be an emerging trend amongst companies with significant pensions deficits.

The regulator is concerned at attempts to transfer a pension scheme to a new, nominal, employer which doesn't have the financial strength to properly support the scheme it is taking on – clearly if the scheme ran into trouble the new employer would be in no position to bail it out.

"We are starting to see schemes where the primary intent behind the transaction has been to abandon the scheme.", says Mr Hobman. His office has warned that companies may be breaking the law in such circumstances and told pension trustees they must apply an "extremely high level of scrutiny".

More reasons why the pensions liabilities of suppliers are increasingly important in assessing their creditworthiness.





Liquid Assets



The impact of climate change and water shortages has yet to be fully analysed, but it's clear that companies with processes that use significant water resources are likely to face increased operating costs.

So it's good to be able to commend the government's attempts to help businesses in sectors like the chemical and petrochemical industries to reduce water usage.

Envirowise is a government-funded body that provides confidential advice on specific issues – and also supplies companies with outside resource efficiency reviews from specialist advisers.

Envirowise's general advice to companies includes:

- 1 **Always measure and monitor the amount of water you use. Compare annual water use against production output.**
- 1 **Take meter readings regularly and carefully – this will help identify changes in water use.**
- 1 **Consider recirculating cooling water through a closed loop system.**
- 1 **Turn taps off fully and replace leaking hoses and worn tap washers. In staff washrooms, push-button taps use up to half the water used through conventional taps.**
- 1 **Consider using lower quality water such as recycled process water for purposes where quality is not critical.**
- 1 **Reduce the amount of clean water used in every toilet flush by fitting a water displacement device into cisterns.**
- 1 **Make sure staff are fully aware of the importance of water minimisation. Run a staff competition to identify water-saving ideas or organise a brainstorm. Appoint 'water wardens' to take responsibility for water minimisation measures in each area of your site.**
- 1 **Ensure staff are encouraged to report leaks and that leaks are repaired quickly.**
- 1 **When purchasing new equipment take its water efficiency into account. It may be more expensive to buy water efficient equipment, but it may have a short pay back period due to the water savings achieved.**

Start-ups set to Climb

The EU is pressing ahead with plans to enable companies to be established within a week anywhere in Europe.

Currently start-up times vary widely – less than two weeks in France, but 60 days in Slovenia. Costs are set to fall, too. Many countries require entrepreneurs to make substantial cash deposits before setting up in business.

In many ways this encouragement of the entrepreneurial spirit is a welcome step. But existing businesses must take into account the fact that most companies that fail do so within the first 3 years of operation.

If the EU's actions produce a flood of new companies, businesses will need to be even more watchful in analysing the creditworthiness of their trading partners.

People Pay Bills

"Companies owe money, but people pay bills."

A critical message, delivered by Jim Doherty of STA Graydon to CIFS policyholders from across the North of England at our latest seminar for credit professionals at Manchester's prestigious Urbis Centre.

Jim gave delegates a series of insights designed to achieve faster payment of outstanding debt, including how to create a personal obligation and obtain specific promises, always getting alternative contact details and, if possible, mobile 'phone number and, importantly, what to do in the event of a dispute. His key learning of this session was "Persistent Consistency Really Pays."

The seminar which also featured a presentation from our credit information partner, N2 Check, additionally dealt with forms of companies and insolvency as well as giving practical advice to combat the rising tide of commercial fraud. It proved extremely useful to policyholders and CIFS plans to hold further such events in 2007. If your company would like to attend, call Sue Morley on 020 7903 7300.





"Monster"

Bill Could Increase Pressure on Directors

The Company Law Reform Bill – set to become law in 2007 – has been described as a "Monster of a Bill" as it seeks to simplify a whole gamut of legislative requirements affecting companies and the duties of directors.

Much of the "meat" of the bill is uncontroversial – an attempt to codify accepted procedures that have grown through custom, practice and precedent, into a single, comprehensive statutory framework.

But there are some provisions of the Bill, which if they make it through into next year's Act, are rather less clear cut and it may take future legal actions to determine their precise impact.

One such is the change introduced by the Bill to make it a *duty* of directors to promote the success of the company for the benefit of its

members as a whole, rather than as at present simply encouraging them to act in stakeholders' interests.

Clearly directors, in theory at least, will have an increased duty to ensure companies deal properly with their creditors.

What are the consequences? Will creditors be able to sue directors personally for actions which neglect their interests? Will D&O insurers bring pressure to bear on directors to ensure they treat creditors fairly? Will we need to assess the assets of directors before doing business with the companies they run?

At this stage these are all hypothetical questions. The Bill has not been finalised and some provisions will need to be tested in the Courts. Still as it stands at present it seems a step in the right direction for credit managers.



Matthew Fosh, chief executive of Novae Group, CIFS' parent company, was recently invited to address an audience of leading City figures on the consequences of the Company Law Reform Bill.

For Matthew Fosh there is a danger that the law of unintended consequences will come into play. As it stands, he believes, the bill introduces a regime which will inevitably lead to more detailed recording and justification of decision-making and cross-referencing to stakeholder interests. It has the capability to add another layer of bureaucracy to corporate life.

Fosh also expressed concern that the uncertainty surrounding the extent of their responsibilities will inhibit entrepreneurial behaviour if directors feel they must act defensively or cautiously in an attempt to reduce potential personal exposures.



Matthew Fosh
Novae Group plc



Pictured with (left) Sue Morley of CIFS is Diana Rhodes, company administrator of Elliot Scientific and the lucky winner of a new i-pod 60, the prize in our last issue's competition.

Harpenden-based Elliot manufactures and distributes high-technology equipment for the scientific research industries. They've been a CIFS client since 2002 when the company re-appraised its credit management procedures in the light of increased sector risk as new start-up technology groups proliferated.

Diane's win was particularly good news for another member of the Rhodes household. She professes herself to be "not much good with technology" and her prize has been grabbed by her 17 year-old daughter.



Softly, Softly

New research from business restructuring specialists Begbies Traynor suggests that the vast majority of SMEs are wary of using their right to charge interest on outstanding invoices.

Comments partner Mark Fry: "It's clear that the Late Payment of Commercial Debts Act, however well meaning, is much too blunt a mechanism."

The act, introduced in 2002, allows companies to add interest of base rate plus 8 per cent to invoices not settled within agreed terms.

But according to BT only 4 per cent of companies polled were doing so, for fear of losing client goodwill and future business.

It's to help policyholders circumvent this dilemma that we've teamed with debt recovery specialists STA Graydon. Their collections services are geared to improving payment terms without jeopardising customer relations. Contact Sue Morley on 020 7903 7300 for details.

