



Credit risk management without the risk

Beware the Brand



We live in an age where establishing brand domination is an acknowledged – if sometimes imperfectly understood – business imperative. But the strength of a brand must not blind you to commercial realities.

Indeed, some of the best known brands in UK marketing have hit the dirt in recent months. One of the most iconic – Golden Wonder – whose legacy includes Cheese & Onion flavour crisps and Pot Noodles – finally succumbed in its battle with Gary Lineker-fronted Walkers.

At one time Golden Wonder was a clear market leader with kids' favourites Ringos and Wheat Crunchies in its portfolio. But the company, operating in a low-margin sector, posted a loss of £10.8 million in its accounts for 2004 and this position was set to continue last year. With a number of different owners over the years, no buyer could be found and the future for employees – and suppliers – is uncertain.

Despite a stylish reputation – both for its merchandise and its stores – fashion chain Kookai has also been placed into administration. Its operator in the UK – AIM-listed Forminster – was simply unable to come to terms with its French franchise owner.

Again, problems were well signalled in advance, showing suppliers must concentrate on business fundamentals in deciding on a trading partner. The strength of the brand is not always reflected in the strength of its owner.



Pensions TIMEBOMB may impact today



CIFS recently received a presentation on the UK's new pensions regime from leading accountants KPMG. It's an extremely dry subject – not for nothing is pensions known as the actuaries' playground – and certainly beyond the scope of a CIFS newsletter. But KPMG did an excellent job in demonstrating the scale of the problem facing UK employers – they estimate the combined pension deficit of the companies in the FTSE 350 to be in excess of £81 billion.

And importantly, while it's likely that pension fund deficits will have narrowed after recent strong market performances, KPMG made the point that most such calculations under the new FRS 17 accounting standard are based on current levels of mortality. If these continue to improve pension liabilities may increase by 6-8%.

One concern when considering the impact of this pensions timebomb is that steps to mitigate the problem may bring the laws of unintended consequences into play.

A key element of the Turner Report, for example, was to mandate employers to pay an additional 3% of payroll costs into employee pension funds. For many companies we believe this will result in reduced employment and in some cases mean the difference

between profit and loss and seriously affect their creditworthiness.

Nearer term we have already seen that the requirement to plug a pension hole at Armstrong played a part in the decision by its parent Caparo to close the company.

It's clear that the need to fund pension liabilities – and for larger companies Pension Protection Fund levies – are going to represent a significant cash call on many companies. And this reduction in cashflow could even result in companies breaching their loan covenants.

It's now become important, if you're considering a long-term relationship with a trading partner, to assess the strength of its pension provision. And companies seeking growth by acquisition must ensure the full potential extent of pension liabilities of possible targets are examined as part of the evaluation process.



Dew gives up the struggle

A vivid – and for many, a painful – illustration of the hidden danger of pension fund deficits has just come with the news that more than 400 jobs are at risk after a £28 million shortfall forced construction group Dew Pitchmastic to put two of its principal subsidiaries into receivership.

Building industry "Bible" Construction News reports that the £140 million turnover firm has appointed Ernst & Young as receivers for Dew Construction and Dew Remediation to the surprise of creditors, after struggling to meet its pension liabilities.

The company, employing 470 staff in eight offices, has faced increasing pressure on cashflow from its pensions crisis and had put in an extra £4.6 million in recent years.

But the group put itself up for sale when it could not meet the liability. After talks collapsed with bidders for part of the business the company decided the pension fund would be better off from insolvency.

Says Receiver Hunter Kelly: *"It is extremely regrettable that a successful and well-established business of some 25 years standing has been forced to seek insolvency protection."*





An Amber light?

HMV is one of the latest high-profile companies to attract the attention of private equity specialists – in this case Permira.

Whatever the merits of this deal we believe businesses should always be wary when they learn that a sizeable customer has been targeted by an outside investor – more especially, perhaps, when the transaction is part of a management buy-out.

Often the rationale of such investments is wrapped up in projections of improved cashflow and

“sweating” the business’ assets within a new corporate environment. Since its largest asset is likely to be its creditors you could argue that this is management speak for getting the business’ suppliers to fund its operation and expansion.

If a customer becomes beholden to private equity finance we recommend you take steps to investigate the new investor’s track record and maintain close monitoring of your customer’s terms and conditions compliance and payment performance.



Bring down the curtain

The final irony for Rover creditors is not – as has been suggested – the £1 million paid by the DTI in professional fees following the company’s collapse.



Rather it was surely the news that a group of ex-managers of the company was negotiating to buy the SV supercar and revive the Austin Healey badge.

There ought to be a law against it.



Competition - Win an ipod

Peace of mind, competitive rates and a comprehensive cashflow management offering. Now CIFS brings you the opportunity to bring some musical harmony into your life.

Simply log in to the CIFS website - www.creditindemnity.com - to find details of our free-to-enter competition and you could win this state-of-the-art iPod. It’s quite simply the most advanced model available. Win it and like CIFS you’ll be ahead of the game.



The other side of the coin



Credit managers have often been characterised as running a unit entitled the “Sales Exclusion Department”.

No longer. Today’s there’s a growing realisation that credit executives are the custodians of much of the information that matches the twin goals of modern businesses: profitable expansion at minimised risk.

The data referenced by the finance department from corporate systems as well as companies like N2 Check can play a major role in helping the marketing team focus its efforts, not just on soundly-based companies but on those likely to achieve the most profitable outcomes.

Payment data, geographic locations and sector classifications for targeted campaigns as well as corporate linkages showing common ownership amongst customers and prospects are all areas where finance professionals can not just identify the risk but also help demonstrate trading potential.

Perhaps it’s time to put information assets to work.

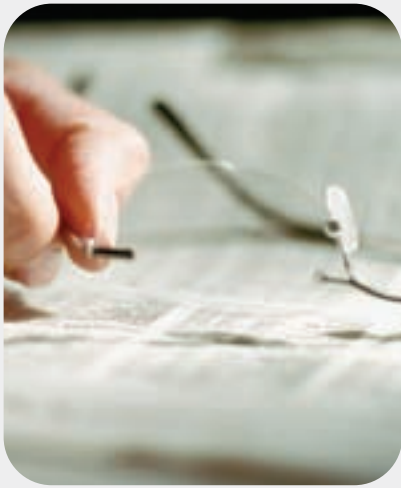
Check Ahead

CIFSCheck reports supplied by N2 Check – an integral plank of the CIFS cashflow management capability – have proved of immediate appeal to policyholders, with take-up rates far exceeding our expectations.

N2 have used Internet technology to deliver high-quality corporate data for use by credit and marketing professionals with significant savings on prevailing market rates. CIFSCheck prices for one-off reports compare favourable with market rates and with major reductions for volume-based subscriptions are available.

The N2 data is augmented by its “Keep it Live” monitoring service for UK and Irish limited and unincorporated businesses, which helps policyholders maintain policy compliance and use discretionary limits with confidence.





Figures sometimes worth a second look

The storm that followed the collapse of High Street off-licence chain Unwins with debts of more than £30 million centred on the alleged lack of reliability of information supplied by its shareholders and auditors Grant Thornton to the private equity purchasers of the company.

Of course this is a very particular case but it raises a general problem: how far can we rely on the information we use to assess a prospective customer's financial health?

For most of us the principal problem with published data from Companies House is timeliness – or rather the lack of it. Frequently accounts are filed up to 22 months late, making them of virtually no value in assessing the company's present state.

That's why analysis of P&L and Balance Sheet strength and trends should be augmented with further sources of information. Payment performance, which can be sourced internally and from external data suppliers (like N2 Check) is an important indicator. When companies' invoice payment drifts away from its long-term norm this can be a powerful predictor of trouble ahead.

Management changes and late filing of accounts are other warning signals that could warrant further investigation before a problem is allowed to escalate.

Court rise

A recent online survey at www.payontime.co.uk (the website of the Better Payment Practice Group) found that of 292 respondents, 31% had been to court last year to collect outstanding debts from business customers.

Even allowing for sample bias this is an astonishingly high figure. Though going to court can be effective – and certainly affords the SME a measure of satisfaction – the BPPG makes the valid point that it is invariably expensive, time-consuming and extremely stressful.

Court action, says the Group, should be seen very much as a last resort and recommends a range of preventative measures to be considered before taking this step.

One such is to employ a debt recovery specialist and CIFS policyholders benefit from preferential rates arranged through our partnership with STA Graydon, the leading company in this field, to make this a still more attractive option than m'learned friends.



Vultures are circling - overseas view

Companies looking to increase trade in the US should take note that so-called "vulture investors" are expecting higher rates of default among high-yield companies in 2006 and beyond.

Vulture investors – among them hedge funds – specialise in troubled companies to achieve high returns. A recent survey found that two-thirds of them believed that big bankruptcies (\$1 billion+) were set to rise this year. They are now looking to make loans secured on specific assets rather than unsecured bonds.

The survey also posited a rise in defaults from 2 to 4% this year and beyond 4% next year. Sectors of particular interest to the vultures were automotive and parts suppliers as well as packaging, healthcare and pharmaceuticals.

Of course vulture investors are focused on the weakest companies, but their views should make exporters especially prudent when granting credit in these areas.





... use a long spoon

Love them or loathe them – and there are plenty who do both – there's no denying the increasingly dominant position of Tesco Stores - both in our physical and corporate landscape .

But who's paying for this seemingly inexorable growth wave?

Writing in the Financial Times recently leading commentator John Plender, in analysing Tesco Stores' annual report, makes the point:

"The accounts reveal that trade creditors continue to make a rapidly increasing contribution to the group's expansion.....

"Broadly trade creditors as a per centage of stocks hovered around the 200% mark from the 2000 year end until 2003. In 2004 the figure jumped to 219% while in 2005 it topped 250%. In contrast trade creditors as a percentage of stocks in the rest of the (Tesco) group excluding Tesco

Stores fell from a peak this decade of nearly 200% in 2002 to 170% last year. "So the financial virtuous circle has been maintained in the UK business to the great benefit of shareholders, while the creditors stump up more."

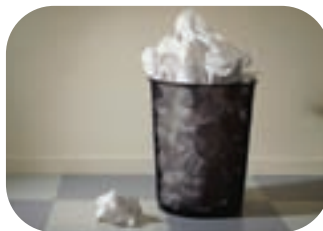
There's no doubt doing business with the supermarkets can be extremely rewarding, but it's an area where attention to payment terms is important.

Interestingly, Plender's article goes on to take a further look askance at the stores group and its advisors:

"Tesco's fabled efficiency does not, incidentally, apply to its filing of accounts, which plopped into Companies House weeks after the filing date. Curious, too, that auditors PriceWaterhouseCoopers sign their report on Tesco Stores 10 months later than they sign off the group's published accounts."



Start-ups, failures, both deteriorate



Business failures in the UK rose by 4% in 2005 – to the highest level since 2002, according to a report from Barclays.

More worryingly – certainly for companies who benefit from new business expenditure – was a significant decline in the number of start-ups. These fell by 13% to 388,300 in 2005, the sharpest rate of decline in a decade.

Barclays points out, however, that new business formation had in fact returned to more typical levels after two boom years and underlying strength was shown by a recovery in the second half of the year.

Nevertheless there is a danger that slower economic growth will continue to deter would-be entrepreneurs.

Unsurprisingly, London accounted for the highest rate of start-ups in the country – with 18 new firms per 1,000 residents. Business/financial services, motor trades, construction and wholesale/retail sectors represented more than half of the country's new firms.

Debt for breakfast



Clients from all over England and from diverse industries including packaging, recruitment and advertising, travelled to the Lloyd's building earlier this spring for the inaugural CIFS training seminar.

They heard Jim Doherty, managing director of STA Graydon deliver insightful advice on how to introduce effective debt management techniques, while Sue Morley, Director of Client Services at CIFS, detailed essential steps to ensure policy compliance.

Audience reaction to the seminar was extremely enthusiastic. One Milton Keynes-based delegate, Jill Stewart, Accounts Department Supervisor at the £13 million turnover Clifford Packaging said: "It was a fantastic day – fun as well as informative – and full of tips which encapsulated applied common sense. There was a lot of interaction with the speakers and it was interesting to hear how other companies of different sizes and in different industries are dealing with the problems we encounter. It enabled me to recognise what we are doing right as well as pick up valuable pointers for the future. I couldn't wait to get back to work to try them out."

Commenting afterwards Sue Morley said: "We were delighted with the response from policyholders to the seminar and will definitely be organising further such events around the country. These will deal with similar topics but will also include contributions from our other partners in credit management and cover status information and trade finance as well as debt collection."

This first breakfast seminar was followed by an extremely informative tour of the Lloyd's building – voted a success by delegates, though some were left a little dazed after travelling in one of the building's high-speed lifts!

Contact Sue Morley on 0207 903 7300 if you'd be interested in attending a future CIFS training seminar.

