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Begbies Traynor

Decrease in industrial distress in stark contrast to surge in problems for consumer industries

Published on the back of gloomy GDP data, the most recent Begbies Traynor Red Flag Alert research shows that the situation in Yorkshire reflects that in much of the UK, with substantial decreases in company distress levels in key sectors such as manufacturing and construction leading an overall improvement. Meanwhile, the rapid decline in the financial health of consumer facing industries, including retail, suggests the development of a twin-track economy.

The survey, which monitors a series of indicators of company distress, was published today (1 February) by business rescue and recovery specialist Begbies Traynor, and reveals that the number of companies in the region with 'critical' problems (such as the issuing of major CCJs and winding up petitions) fell by 36% from 334 cases in the third quarter of 2012 to 214 in the final quarter of the year.

Overall, the UK experienced a 12% decrease in the level of 'combined' distress (categorised as companies experiencing 'significant' or 'critical' financial distress) from 223,125 in Q3 2012 to 196,636 in Q4 2012, indicating the first tentative signs of recovery for parts of the economy . Factors driving this improvement include continued low interest rates, a reduction in actions taken by creditors and their increased forbearance.

In Yorkshire, a number of industries have shown substantial improvement during Q4 of 2013. Construction, the largest sector by number of businesses, saw a decrease of 39% in 'significant' financial distress (including less serious problems such as minor CCJs) from 1,688 cases to 1,023. Real estate too saw a major improvement in fortunes, with distress levels dropping a dramatic 64% to 838 cases from 2,332 in Q3. Manufacturing - including food and beverage, and other manufacturing - also dropped by 21% in Q4 2012 from 779 cases to 613.

While much smaller in terms of volume of business, the most significant improvements among other sectors were seen in industrial transportation and logistics, with a 47% decrease in distress from 429 in Q3 2012 to 227 in Q4 2012, and printing and packaging, with a 45% decrease from 102 in Q3 2012 to 56 in Q4 2012.

In stark contrast, Yorkshire, mirroring the UK as a whole, saw a clear deterioration in the financial health of most consumer facing sectors. Leading the increases in 'significant' financial distress in the fourth quarter of 2012 compared to the third quarter, was the general retailing sector with a 36% increase (from 599 to 814), followed by bars and restaurants with a 38% increase (from 566 to 780), and food retailing, which increased by 68% from 141 to 237. Distress in the sport and recreation sector was up 15% (from 229 to 264) and in leisure and culture by 10% (from 262 to 288).

Julian Pitts, regional managing partner for Begbies Traynor in Yorkshire, commented: "Our Red Flag figures demonstrate an improvement in the financial health of the construction sector, which we believe reflects the fact that those construction firms that have survived the crisis are now benefiting from improving margins on a lower cost base. It is also evident that some construction firms have purchased land banks at substantially discounted prices following the financial crisis which, combined with a material improvement in the sector's output towards the end of 2012*, are encouraging signs. The sector is also benefiting from decreased competition since the onset of the crisis, and continued creditor forbearance, with our analysis showing increased liabilities across the sector."

He added: "In the real estate industry, a substantial surge in buy to let activity during 2012 (with buy to let mortgages reported to be up approximately 20% on 2011**) has driven a clear revival in the financial health of property management businesses, which account for a high proportion of this sector."

David Wilson, regional senior partner for Begbies Traynor in Yorkshire, said: "The overall improvement in the construction and real estate sectors may also reflect an easing in the mortgage market, which has been much lauded as the main beneficiary of the Funding for Lending scheme, launched in August 2012. Although these sectors are typically the first to be hit in a recessionary environment, they are also usually the first to come out the other side, so this positive development could be a predictor of a slowly improving UK economy overall."

Commenting on the good news across other sectors, he said: "It is encouraging to see significant improvements in the industrial transportation and logistics industry as well as the printing and packaging sectors, where a shake out of the weakest companies has benefited the most efficient businesses that remain. Our analysis shows that a greater proportion of businesses in these sectors are reporting improving profitability as a result, with increased utilisation of their relatively high fixed cost bases being driven by the pre-Christmas growth in internet retail sales and flowing quickly through to their bottom line."

Julian Pitts concluded: "The substantial increases in financial distress in these key consumer-facing sectors demonstrate the sheer scale of the challenges facing the consumer economy, particularly as these rises come at a time when spending in the run up to Christmas should have provided a welcome boost to many of these businesses. It is clear that these businesses are feeling the effects of the constraints on discretionary consumer spending brought about by years of wage rises not keeping pace with the rate of inflation and households reducing debt, where possible. Unfortunately, this year will offer no respite for family budgets as changes to the child benefit allowance, rising utility bills, travel fares and other costs, and continued weak growth in real pay rates can only be expected to drain more cash away from these sectors."

** Source: According to ONS statistics, construction output in Great Britain (at constant 2005 prices, non seasonally adjusted) grew by 1.8% to £25.2bn for the three months to November 2012 from £24.8bn in the three months to August 2012*
*** Source: Council of Mortgage Lenders reported, in November 2012, that "the value of buy-to-let lending in the first nine months of 2012 amounted to £11.8 billion, 19% higher than the £9.9 billion advanced over the same period in 2011"*

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Photography: L to R Julian Pitts & David Wilson of Begbies Traynor

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About Begbies Traynor Group

Begbies Traynor Group plc is a specialist professional services consultancy providing independent professional advice and solutions to businesses, financial institutions, the accountancy and legal professions and individuals in the areas of recovery, corporate finance, investigations and risk management. It is listed on AIM (Ticker: BEG). Further information can be found at: www.begbies-traynorgroup.com.

About Red Flag Alert

Red Flag Alert measures corporate distress signals through a comprehensive and complex methodology, drawing on factual legal and financial data from a wide range of relevant sources for companies that have been trading for over a year.

The release refers to the numbers of companies experiencing 'Combined' difficulties, which provides an overall picture of business distress and represent an aggregation of the 'Significant' and 'Critical' problem categories recorded by Red Flag. Companies with 'Significant' problems are those with minor CCJs (of less than £5k) filed against them or which have been identified by Red Flag's proprietary credit risk scoring system which screens companies for a sustained or marked deterioration in key financial ratios and indicators including those measuring working capital, contingent liabilities, retained profits and net worth. Companies with 'Critical' problems are those with CCJs totalling over £5,000 within a three month period or winding-up petitions against them or which have entered Corporate Voluntary Arrangements.

Following in-depth research and substantial development of Red Flag Alert the latest statistics now produced by the system cover a broader range of stress indicators and provide a much stronger indication of the propensity to fail, amongst the UK's corporate community. Our research has shown that a wider range of aspects of a company's trading history can be utilised in determining their likely decline and need to be included in the measurement of 'Significant' corporate stress across all regions and industry sectors. This change to the screening for 'Significant' problems means that we are unable to provide prior year comparatives at this time (and until we have collated a year's data under the new system).

Red Flag Alert is commercially available to all businesses, on an annual subscription basis, to help them better understand risk and exposure and help prepare them for the future. Further information about Red Flag Alert can be found at: www.redflagalert.com