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**Spending Cuts - An Inconvenient Truth?**

# Recovery Matters



Welcome to the Spring edition of Recovery Matters. In this issue I look at: insolvency statistics over the last year or two, the likely pressures business owners will encounter and finally the H M Revenue & Customs factor following cuts in the public sector.

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## Spending Cuts - An Inconvenient Truth?

In the early part of this year we have seen a marked reduction in corporate insolvencies on the same period last year. In fact, the statistics show that there was an 11% drop in liquidation appointments compared to the same period last year. Of the other corporate insolvencies that comprise receiverships, administrations and company voluntary arrangements there was a 24% reduction. The all time high of 25,432 corporate insolvencies in 2009 saw a considerable rise on the average recorded from the previous 5 years of 16,321 per annum. This has somewhat distorted the figures as the 2010 levels are in fact 29% higher than they were pre-credit crunch. I expect around another 24,000 businesses will fail throughout 2011, much on the same level as 2010. A fall as large as 1,500 insolvencies in a year may indicate that businesses

are over the worst of the recession. I urge business owners that this may not be the case and that to take their finger off the pulse could be fatal. There has been an increase in the use of company voluntary arrangements (CVA) and administration appointments across the board, especially where businesses have sought to agree making stores compromises with their landlords on loss. There have been several ground breaking cases that have made legal waves by using a CVA to drop unprofitable stores and then use the same procedure to cull further dead weight from their portfolio.

Property administrations from the real estate sector are at a higher volume than I would have expected and this may add further weight to the economic view that there is a second wave of distress post "Credit Crunch Recovery".

## Other Inconvenient Truths?

Whilst I can look at the cold statistics with regard to corporate insolvency numbers, there are a number of other factors that will impact on businesses. The Government have announced and started to implicate vast public sector cuts that will have a long lasting effect on the businesses that not only contract with them but the knock on

effects will be seen in their customers as time elapses. A more immediate cash flow shock will be the introduction of the higher rate of VAT. This is already biting at the heels of cash strapped businesses, especially those who have little market share and compete in an already tight margin market, who will be unable to pass on the rise to the customer. Inflation is also at a higher than Government targeted rate and this will further squeeze the coffers. An expected and some say imminent interest rate rise or rises over the next 12 months will mean that should the gearing of a business not be at appropriate levels to sustain itself there may be trouble for many entities over many industry sectors. In the past this may have been mitigated by further borrowing but as many businesses are already struggling to attain lending and indeed lenders are reluctant to fund business this option may not be available. I am not that sure that interest rates will rise too sharply this year, as the Government cannot afford it.

Other funding options should be considered and larger and more niche factoring and invoice discounting companies are now offering competitive rates. A study by R3, found that approximately 10% of

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businesses describe themselves as reliant on public sector contracts. The cuts the Government have proposed will start to bite this year. This will inevitably have a much greater than usual knock on effect on the construction industry that may be worst affected by the public sector cuts due to reduction in capital spending, with many education and social housing projects being shelved. Many businesses may be experiencing a buoyant time coming out of the worst recession in living memory although it is highly likely that tougher margins, reduced access to capital and inflationary pressures will bring management a headache in the not too distant future. I urge all businesses owners to take the appropriate advice where necessary and act quickly to avoid future cash flow pressure.

If I look at the UK economies country by country there is a distinct picture showing a 2 tear economy in the UK. England and Wales are bouncing back and Scotland and Northern Ireland seem to be sinking in deeper. It is sound advice to make the appropriate checks on new and existing customers to ensure your business does not get burnt by others' failures if at all avoidable.

### The Inconvenient History?

As mentioned in the previous Recovery Matters, whilst this has

undoubtedly been the worst recession since the 1930s there are troubled times ahead. Current low insolvency numbers can be attributed, in part, to the leniency of H M Revenue & Customs in allowing Time to Pay arrangements to many businesses. Time for this generosity appears to have since passed and the need, and public desire, to see better collection rates from H M Revenue & Customs means that they are becoming much stricter with their collection policy. I reiterate that I expect them to start enforcing their right to petition for companies to be wound up once they themselves have seen some form of reorganisation, which no doubt will also be a shock to them.

Another factor may be the banks proactive attitude to managing their portfolios rather than taking any drastic action. As the economy and asset values improve, banks may be more inclined to cut their losses in certain sectors and make a number of insolvency appointments once their public relations are back on track. This is speculative but it is my belief that there are thousands if not ten times this amount of businesses that the Banks could not, in the current financial climate, take remedial action against as they would be increasingly hounded by the press and Government alike.

One thing is clear. In an attempt to avoid insolvent liquidation or other insolvency procedures, effective, timely and appropriate advice from an Insolvency Practitioner should be sought at the first instance if any alarm bells start ringing.

If clients need help, I am able to provide speedy and frank advice regarding any restructuring, financing or other options available for troubled business owners. This action has never been more crucial



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