Acumen
Credit Insurance Brokers
an Aon company

30th September 2018

RISK ROUND-UP

INTRODUCTION

Most of the credit insurers who offer export and global trade credit insurance have their own teams of Economists carrying out research and publishing articles, helping Brokers and Clients understand the risk outlook of the economies around the world. As Brokers for the whole trade credit insurance market, Acumen are in a unique position to have access to all this information and so this Risk Round-Up is designed to bring together the key ideas and information in one document. If you are interested in the greater depth of the original articles from which this information is taken, please contact your Acumen Broker (or call 0845 073 8630) and they will be able to provide this.

CONSTRUCTION, UK : ARE THE BIG BOYS STILL PLASTERING OVER THE CRACKS?

2018 has seen some of the traditional 'Big boys' of the construction industry start to show cracks after years of aggressive acquisition and turnover, diversification from core business and increasingly tight margins. The collapse of Carillion at the start of the year sent shock waves through the industry marking a stark wake up call as damaging revelations appeared in the media. These revelations have brought the industry and those at the top in to the spot light.

Profit warnings have doubled to the half year with legacy internal operating processes and external elements continuing to influence the previously Teflon coated companies. Political and economic uncertainty around Brexit, ever increasingly complex projects and losses from Energy-from-Waste contracts add further weight to these giants. Cash balances are significantly depleted following years of acquisition resulting in more heavily geared main contractors. The top 10's borrowing sitting at £3.92 billion, up by £77 million.

Gearing in this industry sector is nothing revolutionary; the difference is there are now new factors pressing which could have significant impact not only on the top tier but the industry as a whole. Interest rate rises are something which can not be ignored and the compulsory adoption of the changes in the accounting regulations under IFRS 15. Indications so far, from the early adopters, are these regulations could have significant impact.

The Office for National Statistics Q2 figures brings some better news. The extreme weather experienced at the beginning of the year, which lead to an output slump of 0.8 % quarter on quarter, Q2 the output increased 0.9%. The repair and maintenance sector notably grew output by 2.7%, infrastructure, industrial work and new public housing all experienced increases during this period. The industrial market is specifically benefitting from 'mega sheds' which are seen as relatively risk-free contracts.

The need for 'Super Joint Ventures' is increasing with the size and complexity of projects and contracts within the infrastructure area. Collaborative working in this way could be construed as spreading the risk in light of the Carillion experience. The potential for a domino insolvency effect should not be ignored due to the large number of joint and severally liable agreements.

Between 2010 and 2017 construction insolvencies reached a peak of 3979 in 2011 followed by a steady year on year decline until it bottomed out in 2015. Since then the numbers have been increasing with full year figures for 2017 showing 2640 companies went in to insolvency. Q2 2018 and the numbers are already up 126 on the corresponding period in 2017, totalling 1476 failing companies.

The expected large scale fall out from the Carillion situation has not as yet appeared in the numbers forecast. There are however some who have cited Carillion as being the reason their businesses have failed but the eventual release of the creditors listing may see more businesses point the finger.

Trading conditions continue along a challenging path for this industry sector with a number of factors contributing to on-going result concerns. There is a section of the construction industry which has been quietly adapting and becoming more agile over the last 10 years. The environment has lead them to aggressively manage their costs, resist diversification, adhering to their core expertise and a refusal to tender on zero margin contracts, all actions now resulting in them winning more work whilst having much more secure foundations.

Supply Chain Finance (SCF) is a major source of funding and is the result of sustained low interest rates and competition on the banking sector. Whether this is a positive or not is how it is applied. It can enhance liquidity and working capital but there is on-site pressure for sub-contractors to sign up to such facilities when tendering for new business. Concern is these facilities are often used to extend payment terms to 90 days or beyond.

The uncertainty of Brexit means any beneficial fall out, following the demise of one of the top players, to the rest of the market could be delayed.

Source: Tokio Marine HCC Industry Insight – Construction Update 2018

GREECE - WHERE IS IT NOW?

This year is the 10th anniversary of the global financial crisis which almost led to economic ruin for Greece and departure from the Euro. Now 10 years on is Greece really out of the woods as some are hinting at or do they still have a long way to go?

2017 was the first year since the crisis that Greece started showing positive growth with a +1.4% increase. Predictions for 2018, even with weakening growth in the Eurozone, is for Greek GDP to come in at +2%.

The period 2008 to 2015 saw GDP fall 25% and investment by 60% with unemployment reaching 28%. The business turnover dived steeply by a third. Three key factors were cited as being fundamental to the situation, a sovereign debt crisis, a banking crisis and a “sudden stop”. Inwardly focused on domestic trade, transport, accommodation and catering construction were hard hit with low value-added goods, such as furniture suffering the most with a 70% drop. Automotive and shipbuilding didn’t fair much better with significant losses of -55%. The National Bank of Greece state between 2008 and 2016 about 250,000 small and medium sized enterprises went bankrupt. Though Greek banks have undergone recapitalisation in 2015 they continue to record high rates of non-performing loans. The International Monetary Fund (IMF) and Euro Commission predict it will take 10 years before the economy returns to pre-crisis levels as Greek companies continue to face liquidity shortages. March 2018 saw the gross value of non-performing loans totalling EUR 98 billion.

Despite regulatory changes and increased transparency, the judicial liquidation process has lead to there being a high number of zombie companies. The Organisation for Economic Co-operation and Development (OECD) average timeframe to recover claims after bankruptcy, is 1.9 years whereas Greece stands out with an average of 3.5 years.

Having partially addressed fiscal and current account imbalances, fiscal credibility has been reinforced enabling the country to re-enter the international market and to disburse with part of the capital controls as it is about to pull out of its third bailout package. The enduring crisis has meant Greek companies have become more competitive in the export market with the contraction of wages (a fall of 22% between 2008 ad 2017) contributing to lower production costs and an up turn in profitability. This re-focusing away from domestic to export (increasing 27% from 2008 to 2017) now means the main concern for Greek companies is the external environment such as the slowing of growth in the rest of the euro area and a variety of political risks.

Throughout the crisis Greece’s tourism has continued to be resilient, benefiting from political events such as the Arab Spring. In the last 10 years foreign tourist arrivals have increased by 82% worth an estimated EUR 3 billion.

Source: Coface Economic Publications - Businesses in Greece: finally a fresh start? - August 2018

Acumen
Credit Insurance Brokers
an Aon company

Acumen Credit Insurance Brokers Ltd
T: 0845 073 8630
E: acumen@credit-insure.co.uk

Acumen Credit Insurance Brokers Ltd are authorised and regulated by the Financial Conduct Authority, No.310986. Registered Address: Trueman House, Capitol Park, Leeds LS27 0TS. Registered in England, Number 2215326.