Business Distress Index October 2011

Association of Business Recovery Professionals
R3
Rescue Recovery Renewal

Increased distress since last quarter

A rise in profits for one in five businesses, but nearly half see profits decline

Cash flow pressures up on last year

Domestic orders are up for just 14% of businesses and only 6% of manufacturers have seen rises in their export orders

Sharp rise in use of maximum overdraft - 22% of businesses frequently turn to this last-resort facility

Welcome to the fifth wave of R3's quarterly Business Distress Index. As the Government looks to the private sector to stimulate the stagnant economy this wave also focuses on signs of growth. The results indicate that conditions are still tough for businesses. While 22% have seen profit rises, 43% are experiencing decreased profits. Distress levels are up on last quarter and cash flow is more stretched than it was this time a year ago.

EXECUTIVE SUMMARY

Quarter on quarter - increasing distress

- There have been increases in distress in eleven of the thirteen key signs since last quarter. The sharpest increases are in the frequent use of maximum overdraft facility (up 9 points to 22%); decreased profits (up 8 points to 43%); and reduction in sales volume (up 7 points to 34%). The number of businesses taking on new borrowing to pay down existing debt has doubled since last quarter, now at 8%.

Year on year - mixed picture

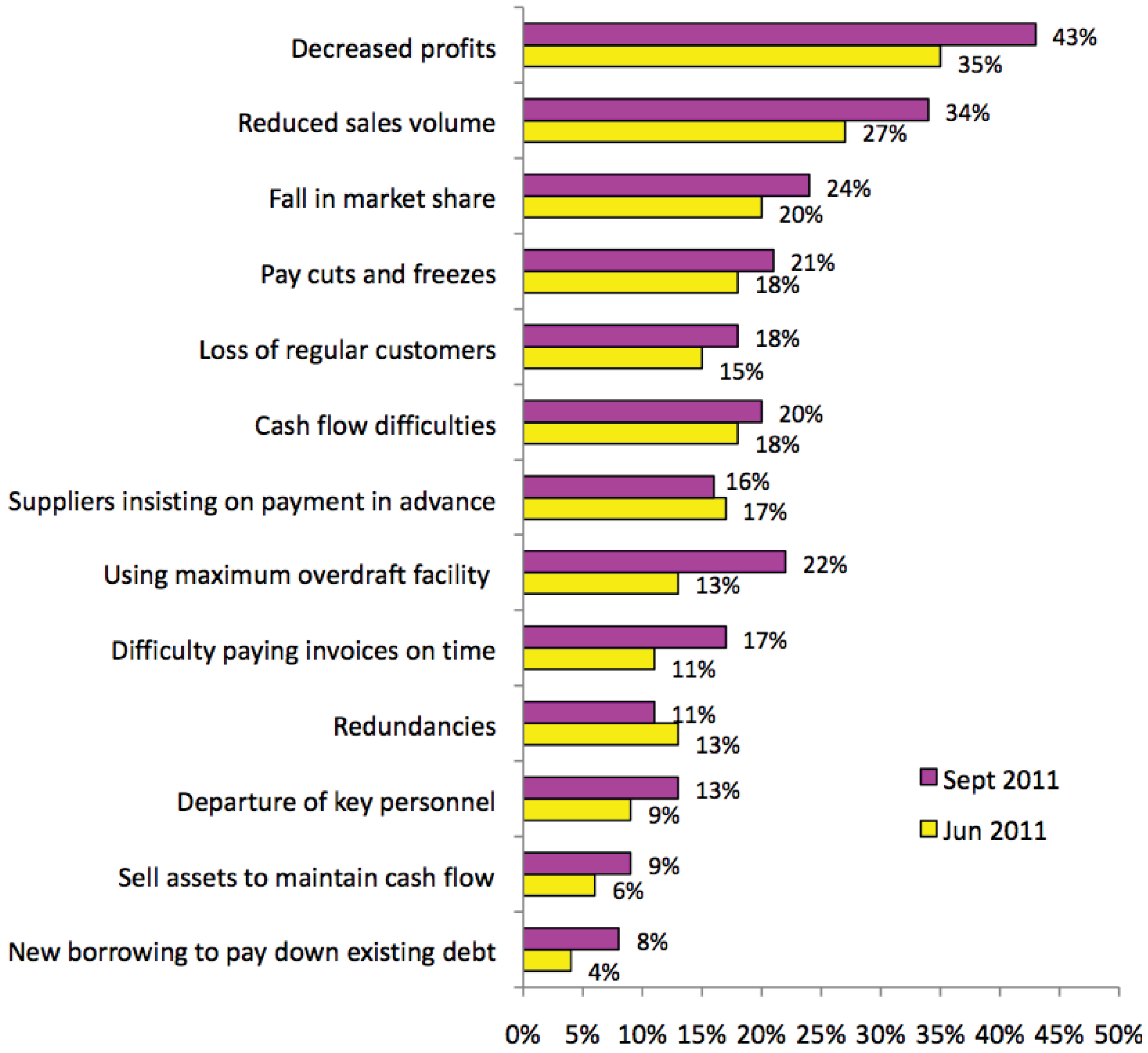
- Distress signs associated with cash flow are generally higher than they were this time last year - there have been increases since September 2010 in the proportion of businesses experiencing cash flow difficulties (up 1 point), difficulty paying invoices on time (up 3 points), using their maximum overdraft (up 5 points), taking on new borrowing to pay down existing debts (up 2 points) and selling assets to maintain cash flow (up 1 point).
- However, a lower proportion of businesses are seeing decreased profits (down 6 points), reduced sales volume (down 10 points), a fall in market share (8 points), a loss of regular customers (down 8 points) and suppliers insisting on payment in advance (down 2 points).

Growth index

- A quarter of businesses have experienced a recent increase in turnover (24%) and just over one in five have seen a jump in profits (22%). A similar proportion are investing in new equipment (23%) and 21% say their business is expanding. Only 14% have seen an increase in domestic orders and just 6% have received an increase in export orders. 11% have recently increased their workforce.
- Businesses in the services sector are more likely to be experiencing most of the indicators of growth than those in the manufacturing sector.

Distress Index: Quarter on Quarter

There have been increases in distress in eleven of the thirteen key signs since last quarter. The sharpest increases are in frequent use of maximum overdraft facility (up 9 points to 22%); decreased profits (up 8 points to 43%); and reduction in sales volume (up 7 points to 34%). The number of businesses taking on new borrowing to pay down existing debt has doubled since last quarter, now at 8%.

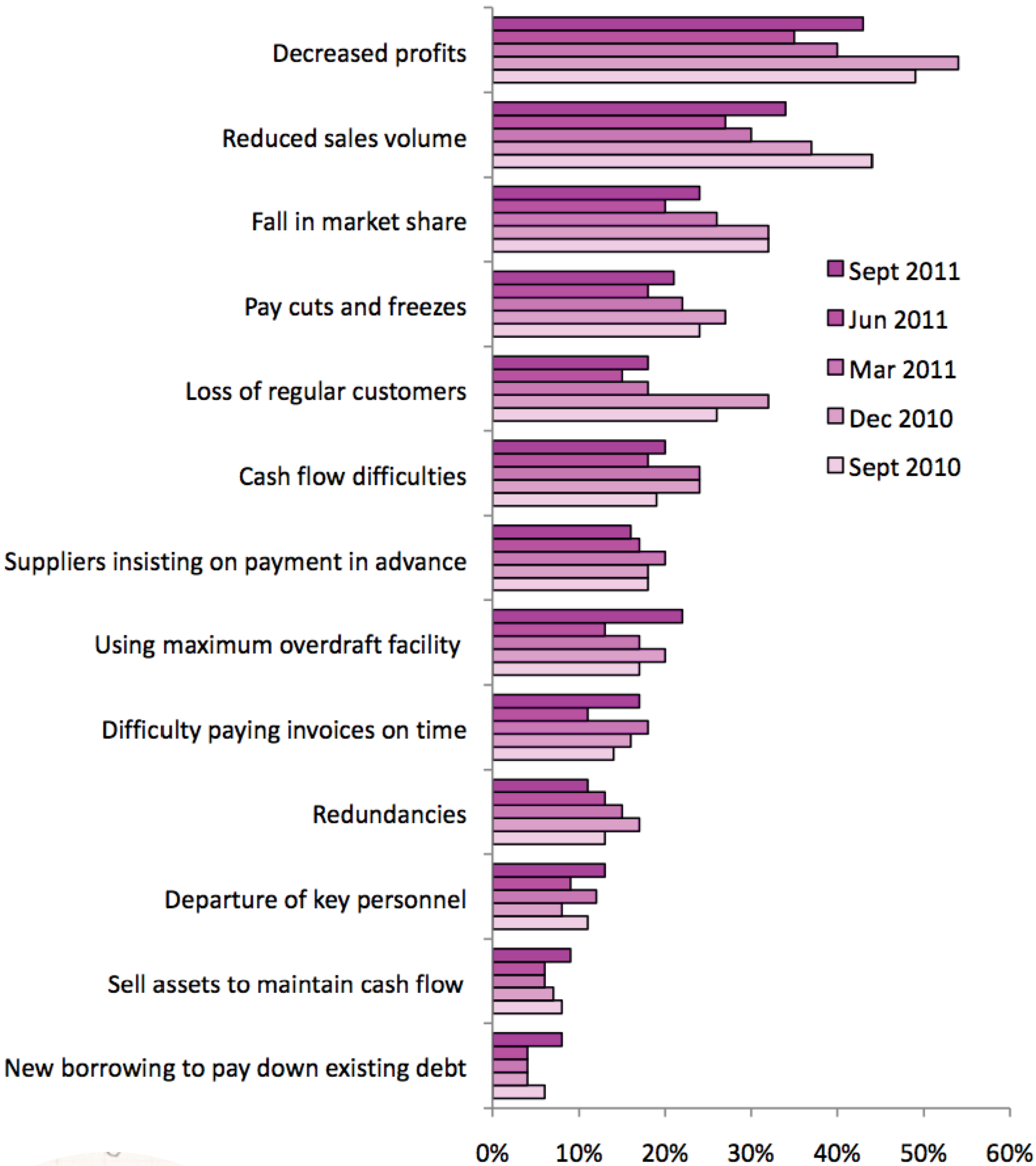


R3 President Frances Coulson explains:

"Times are still tough for businesses, with distress increasing across most key indicators. This worrying trend largely mirrors the slowdown in GDP growth over the last quarter. While current stresses may not be enough to push businesses over the edge, a prolonged period of distress will trigger an increase in formal insolvencies. The first few years after a recession are traditionally difficult as is it some time before businesses can sufficiently rebuild their reserves to support expansion."

Trends a year on: distress during 2010 and 2011

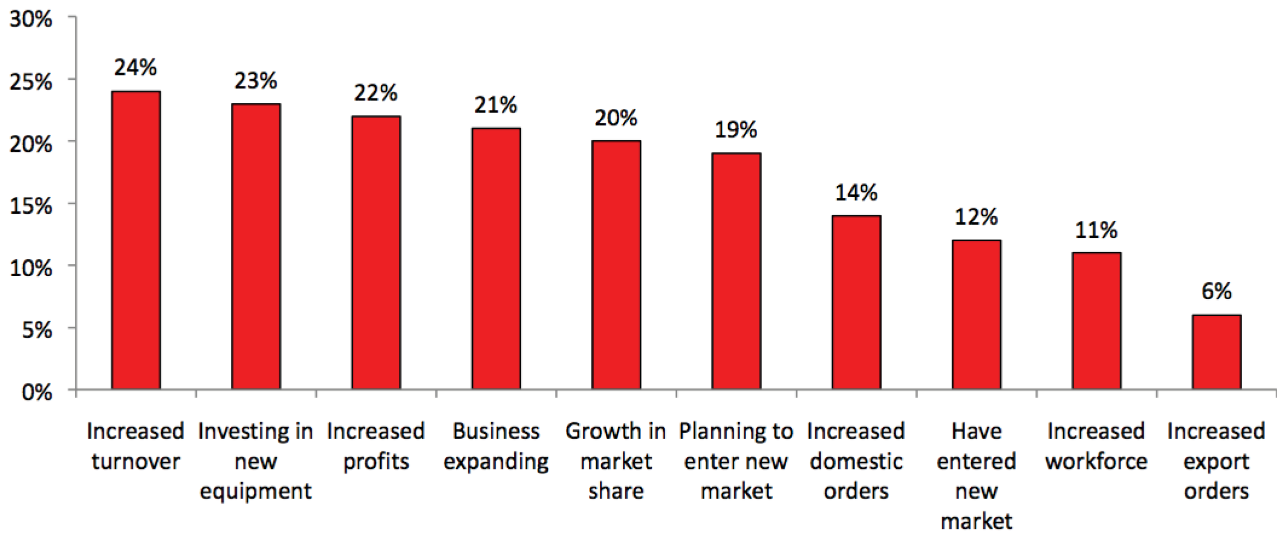
In comparison to September 2010, levels of distress are now higher in six of the warning signs, but lower in seven. A higher proportion of businesses are experiencing cash flow difficulties (up 1 point), difficulty paying invoices (up 3 points), using their maximum overdraft (up 5 points), taking on new borrowing to pay down existing debts (up 2 points), selling assets to maintain cash flow (up 1 point) and losing key personnel (up 2 points) than in September last year.



However, a lower proportion of businesses are seeing decreased profits (down 6 points), reduced sales volume (down 10 points), a fall in market share (down 8 points), a loss of regular customers (down 8 points) and suppliers insisting on payment in advance (down 2 points). A lower proportion of businesses have also introduced pay cuts (down 3 points) and made redundancies (down 2 points) this year than did so in September 2010.

Growth Index

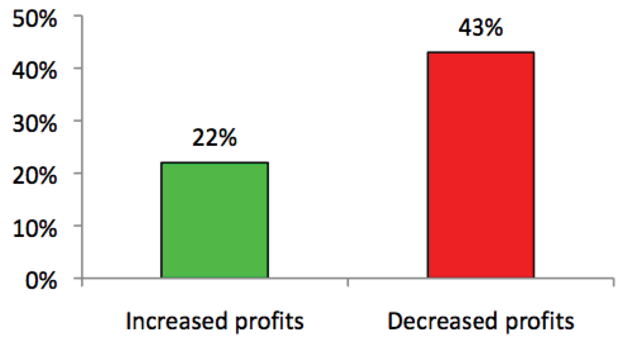
For the first time, businesses were asked whether or not they are experiencing a number of growth indicators. A quarter of businesses are seeing increased turnover (24%) and more than one in five are experiencing increased profits (22%). A similar proportion are investing in new equipment (23%) and 21% say their business is expanding.

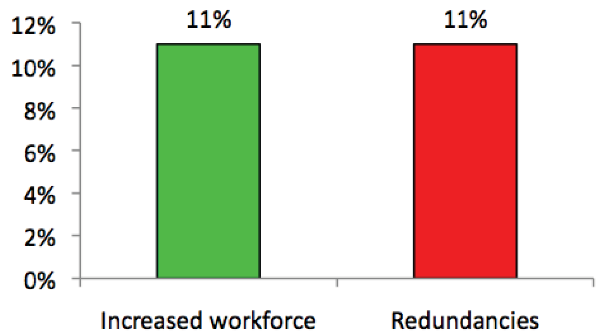


One in five have experienced a growth in their market share (20%) and a similar proportion are planning to enter a new market (19%), with just over one in ten recently having done so (12%). Only 14% have seen an increase in domestic orders; just 6% have received an increase in export orders; and 11% have recently increased their workforce.

The Overall Picture

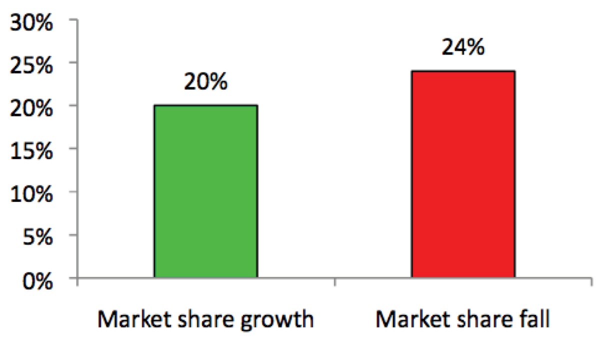
Certain indicators of growth are mirror images of signs of distress. When compared, the results indicate that more businesses are experiencing decreased profits (43%) than increased profits (22%); and a greater proportion have seen a fall in their market share (24%) than an increase (20%). The percentage of businesses taking on staff and the percentage making redundancies are the same, at 11%.





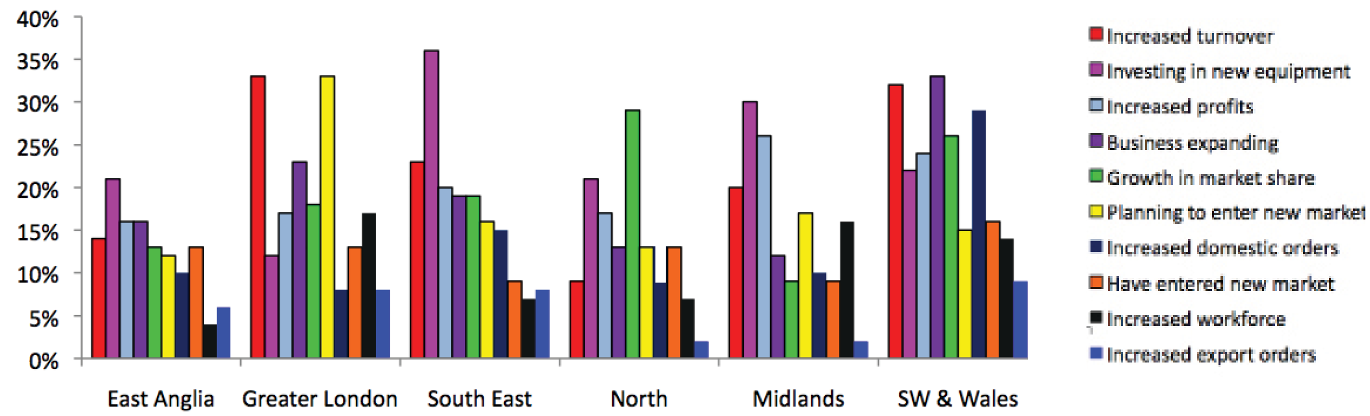
R3 President Frances Coulson explains:

"The private sector has a considerable way to go before it can deliver the kind of expansion the Government yearns for to drive the economy forwards. While it is encouraging that a fifth of businesses are growing, important measures such as increasing exports and increasing employment register poorly."

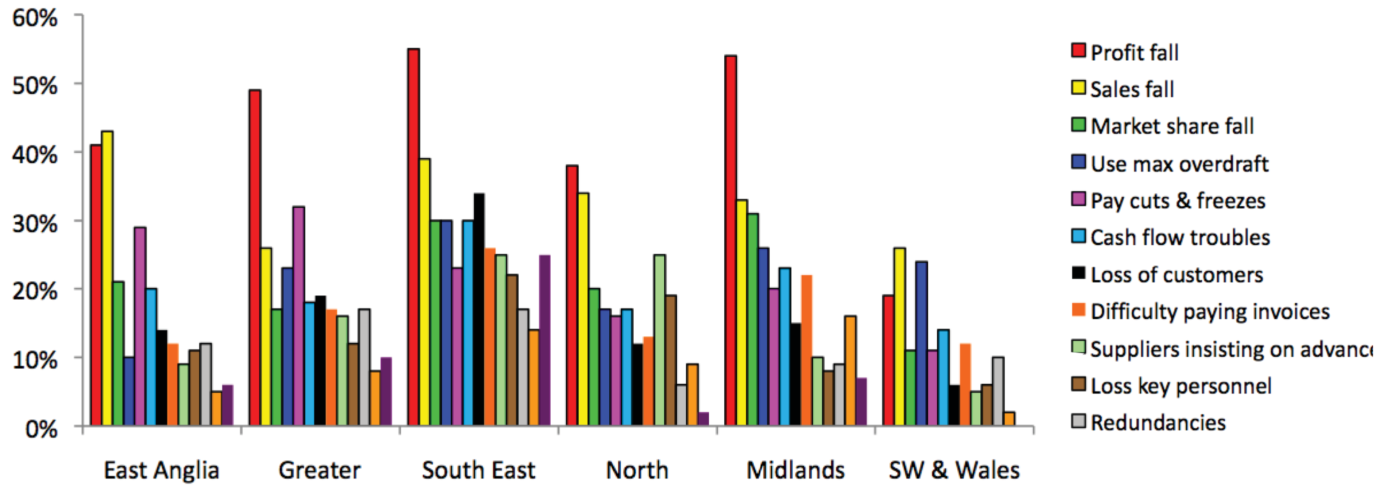


Business growth and distress: regional analysis

Businesses in London are more likely than their counterparts elsewhere to be seeing increased turnover (33%) and to be planning to enter a new market. Businesses in and around the capital are also most likely to have taken on more staff recently (17%), closely followed by those in the Midlands (16%). Meanwhile, businesses in East Anglia are least likely to have increased their headcount (4%); similar to 7% of businesses in the North and South East.



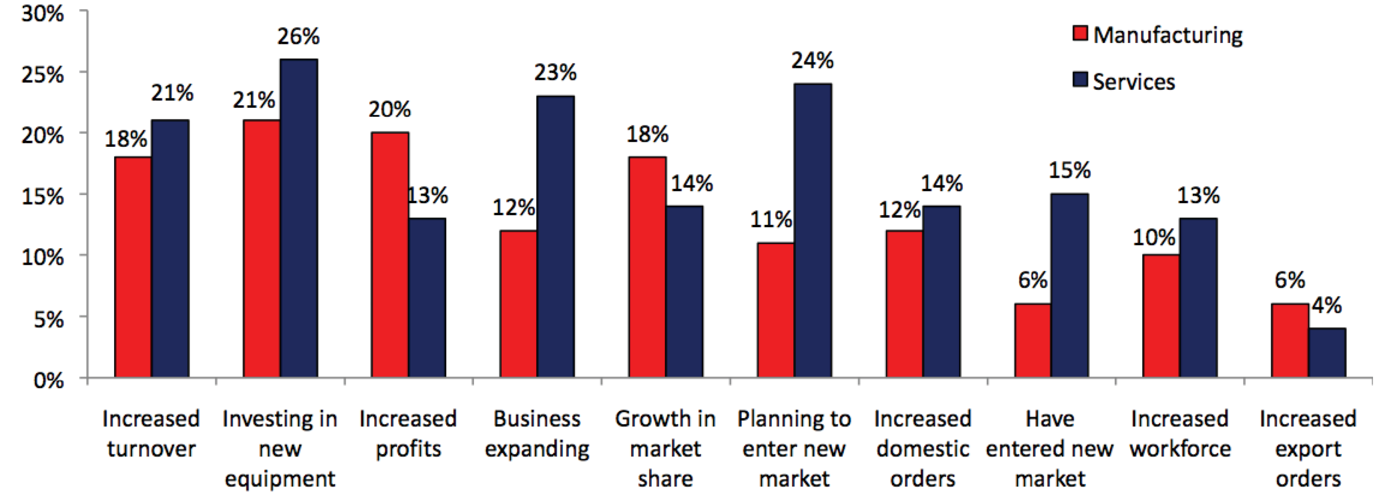
Businesses in the South West and Wales score relatively highly on many signs of growth - 33% say their business is expanding, 29% have seen increases in domestic orders and 32% have experienced a recent increase in turnover. Mirroring these results, South West and Wales businesses show lower levels of distress than their counterparts elsewhere.



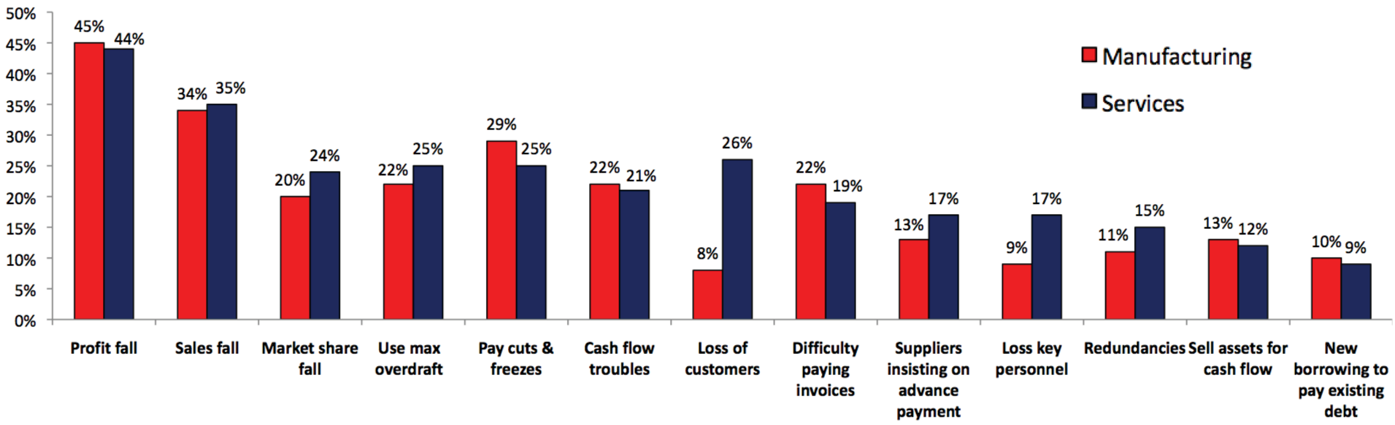
Profit falls are particularly marked in the South East (55%), Midlands (54%) and London (49%). While 17% of businesses in London say they have recently taken on staff, an equivalent 17% say they have made redundancies during the last quarter. Taking on new borrowing to pay down existing debt is especially high in the South East, at a quarter of businesses in the region.

Business growth: sector

Businesses in the services sector are more likely to be experiencing most of the indicators of growth than those in the manufacturing sector. There are three exceptions: increased profits, growth in market share and increased export orders; all of which are experienced by a higher proportion of manufacturing than services businesses.



Signs of distress exhibit greater similarity between the two broad sectors. The sharpest areas of disparity are a loss of customers and loss of key personnel, both more keenly felt among the services sector (26% and 17% respectively).



R3 President Frances Coulson explains:

"The service industries and the south of the country continue to drive growth, albeit at modest levels. More confidence is needed in the economy generally if the manufacturing sector is to expand as the Government desires."

Methodology note: BDRC Continental conducted 502 telephone interviews with small, medium and large business owners and Financial Directors between 5th and 16th September 2011. Quotas are set by size, region and sector and the data weighted to the profile of UK businesses. The respondent in each case is a senior financial decision maker.

About R3

R3, the trade body for insolvency professionals, represents over 97% of Insolvency Practitioners. R3 members are trained and regulated accountants and lawyers who have extensive experience of helping businesses and individuals in financial distress.