IMPROVEMENTS IN INSOLVENCIES MAY MASK PROBLEMS IN SOME SECTORS

FTI CONSULTING

Insolvencies across the economy declined in September and October, adding to the better numbers over the past 12 months. But businesses need to be vigilant.

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FTI Consulting's analysis of the latest ASIC insolvency statistics for the months of September and October 2017 show a decline from the levels seen mid this year and in the same period of 2016.

"While the figures reflect a continued downward trend in the number of companies entering external administration, which is positive, in reality there is still a fair bit of stress among businesses, and many remain at risk," said Ross Blakeley, Senior Managing Director, Corporate Finance & Restructuring, at FTI Consulting.

In September, 627 companies entered external administration, down from the 741 recorded in August 2017. This fall represents a 12.4 per cent decline, year-on-year, with 716 insolvency administration appointments recorded in the same month of 2016. The October figure, at 606, follows a downward trend and a 10.5 per cent decline, year-on-year, with 677 appointments recorded in October 2016.

In total, 7,748 entities entered administration for the 12 months to October 2017, a 12.6 per cent improvement on the corresponding period in 2016 when 8,864 insolvencies were recorded.

A breakdown of the industry groups suggests the shake-out of the mining industry appears to be slowing, with just five insolvencies in September and 14 in October. This compares with 28 in September 2016, and 19 in October of that year. It is also a long way from the peak of 106 recorded in April 2016.

The statistics also suggest that conditions for manufacturers have improved, with 13 appointments in September and 18 in October, compared with 24 and 30 in the same months last year respectively. It also improved from the previous corresponding quarter, with 57 appointments compared with 86 in 2016.

"While some industries may have seen the worst of their challenges, such as mining and mining services, there are still a number of sectors, such as retail and construction, and pockets such as hospitality and abattoirs, that are showing signs of stress," Blakeley added. "Anecdotally we are hearing that the revenue and margins just aren't there, with considerable competition and rising costs."

Record low wages growth, high household debt and poor consumer sentiment may be continuing to affect retailers, with 50 appointments in September and 38 in October. Construction companies also still represent a high proportion of formal insolvencies, with 109 appointments made in September and 112 in October.

"The sustained decline in external administrations also reflects a continuation of the increased workout culture and the way major stakeholders are dealing with businesses in financial distress," he said. "But despite this positive and accommodating approach, some businesses that just paper over the cracks without truly fixing the underlying problems will likely eventually fail."

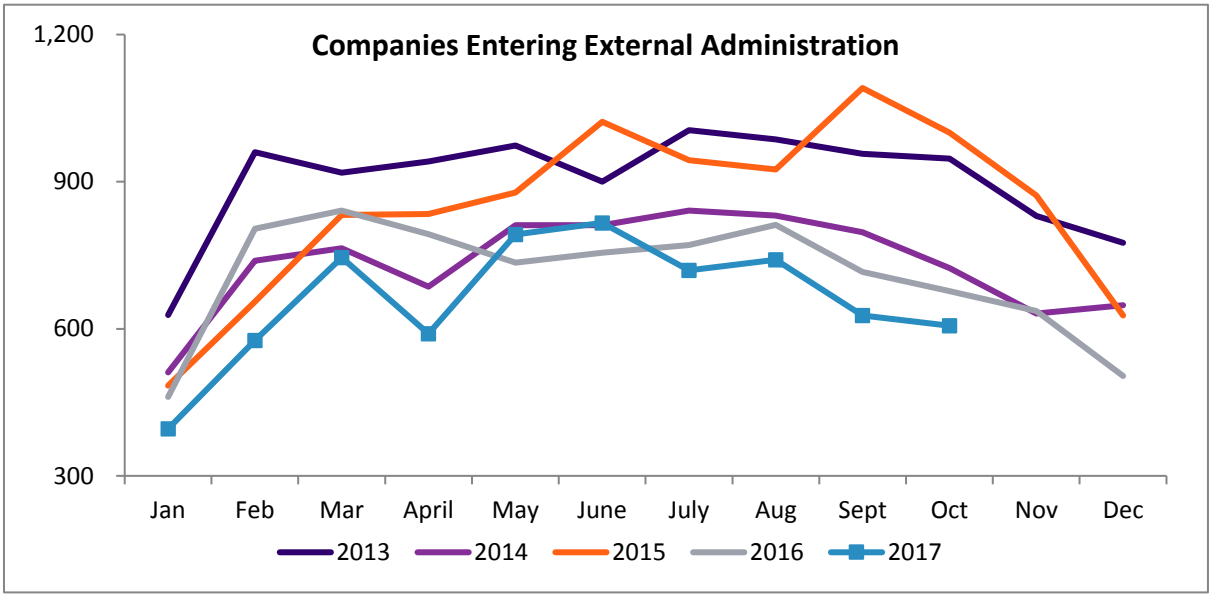
Blakeley added that the relatively new safe harbour legislation was yet to be substantially tested in the real world. So its potential impact on the number of future insolvencies is therefore unknown.

"The legislation offers some protection to directors from liability for 'trading whilst insolvent' whilst exploring alternative workout strategies in pursuit of a better outcome rather than a company immediately entering administration or liquidation.

If problems aren't genuinely addressed or indeed capable of being worked through, it may just defer an inevitable insolvency appointment. Alternatively voluntary administrations may emerge as a prevalent means of implementing a staged workout plan."

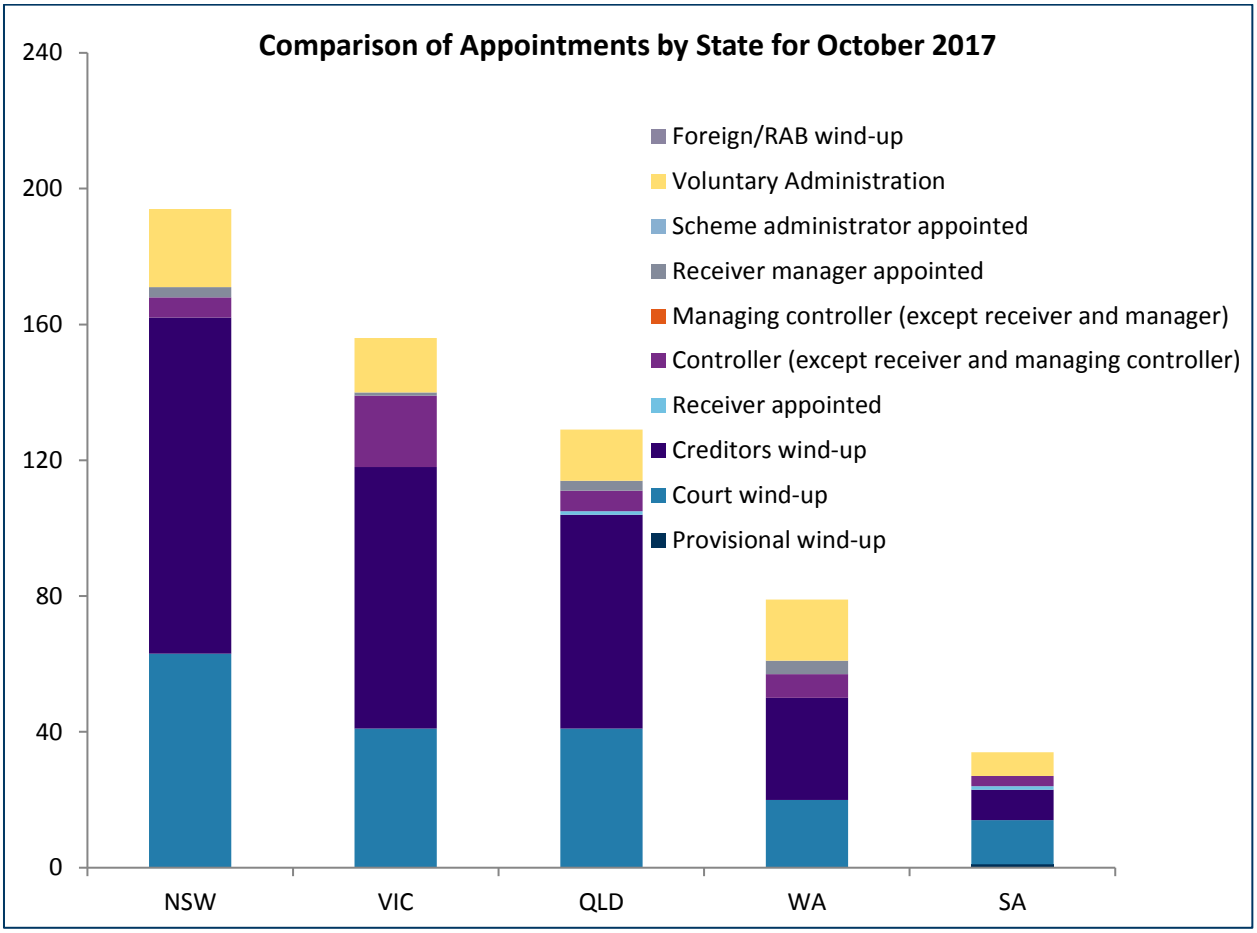
But directors must still tread carefully. One thing that is clear from the safe harbour legislation is the importance of directors being able to justify and support their decisions and chosen path, necessitating having a clear turnaround plan, that takes in to account often numerous complex and varied issues.

"That plan cannot be fanciful and must be readily implementable. Critical to that is obtaining objective input from suitably qualified advisers" emphasised Blakeley.



On a state-by-state basis, only two states recorded marginal increases in the number of companies entering external administration in September. Most had decreases. Figures for South Australia and Tasmania rose by eight and one respectively. New South Wales had the greatest number of insolvencies, at 226, but this was down from 266 in August 2017. The figures were: New South Wales 226 from 266, Victoria 160 from 205, Queensland unchanged at 138, South Australia 28 from 20, Western Australia 54 from 89, Tasmania 4 from 3, the Northern Territory 5 from 6, and the ACT 12 from 14.

The same was largely true for October, with most states and territories recording declines except South Australia (up 6), Western Australia (up 25) and Tasmania (up 2). The figures were: New South Wales 194 from 226, Victoria 156 from 160, Queensland 129 from 138, South Australia 34 from 28, Western Australia 79 from 54, Tasmania 6 from 4, the Northern Territory 2 from 5, and the ACT 6 from 12.



On appointment types, creditor wind-ups saw the most activity, with 363 recorded in September and 281 in October, largely consistent with the previous year's totals of 365 and 304 respectively. Meanwhile, voluntary administrations decreased substantially to 70 in September, from 105 in August, but rose to 83 in October. Court wind-ups saw a decrease to 158 in September, from 225 in August, and a rise in October to 184.

These analyses and comments are based on a review of the ASIC Insolvency Statistics published in December 2017. The full statistics are available here.

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