THE INSOLVENCY REVIEW

ISSUE 01 - DECEMBER 2020

State of Play:
Corporate Insolvencies
September Qtr 2020

Personal Insolvency Snapshot:
Key Trends
September Qtr 2020

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WELCOME

Welcome to the first edition of The Insolvency Review.

Drawing on data from Government and expert industry market research, the purpose of this publication is to provide an overview and reference as to the state of the insolvency industry at each quarter throughout the year.

Our aim is to provide a snapshot of the industry as it relates to both corporate and personal insolvency matters, providing both context to the data, key insights and commentary from our own experts.

2020 has been a tumultuous and challenging year, with the industry facing the most expansive corporate insolvency reforms in more than 25 years. As we move forward into 2021, more changes are likely to come into effect and we will address these over coming editions of The Insolvency Review.

We hope this publication acts as a resource for both those in the insolvency industry and the broader business community and encourage feedback and commentary.

Enjoy this first issue.

Terry van der Velde
Managing Director
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EXTERNAL ADMINISTRATIONS

"COVID-19 has dramatically altered the Corporate Insolvency landscape"

Coronavirus has had a significant impact on many aspects of our lives. Businesses around the country have been heavily hit which has resulted in Australia's economy entering its first recession in nearly thirty years.

The measures introduced by State and Federal Governments to assist businesses and individuals during this challenging period have included stimulus packages, loans and other programs to provide relief. External Administrations have hit an all time low, with numbers down across every state (see Fig. 1).

With the exception of the ACT, year on year for the September Quarter has seen a more than 50% drop in the number of external administrations across all states and territories.

The restrictions imposed to protect the broader population from Coronavirus has nevertheless, had a massive impact on business as a whole, particularly those enterprises deemed 'non-essential'.

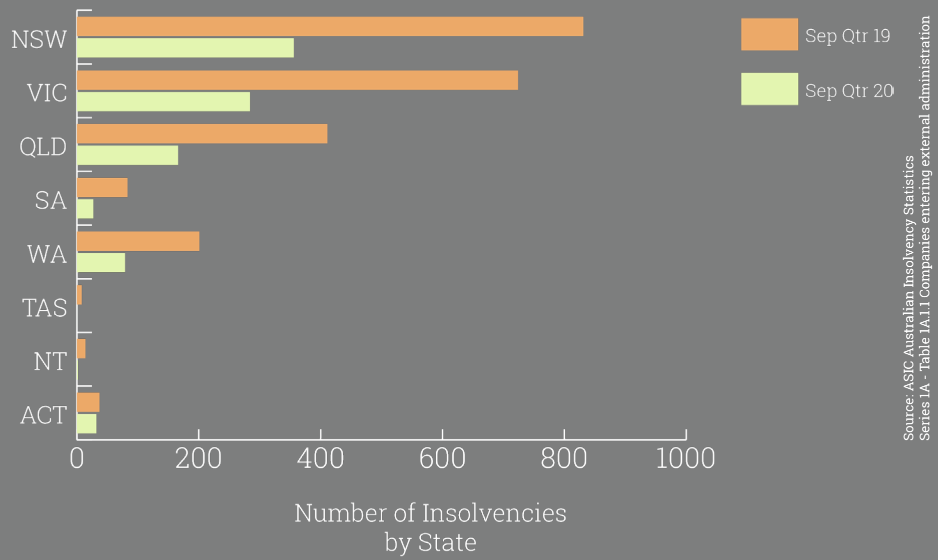
Statistics from ASIC for the September 2020 Quarter show the top three industries with the highest number of businesses entering external administration to be:

- Other (business & personal) services with **305**
- Construction with **181**
- Accommodation and Food Services with **127**[1]

As a result of the implemented closures, many establishments in the business and personal services sector were heavily impacted. Despite trending upwards pre-COVID, businesses providing hair and beauty services suffered a large reduction in revenue due to restrictions. The industry has thus far posted a 14.4% decline in revenue with a 7.3% decline in employment over the same period.

Being a highly competitive market, strong competition has driven down prices over the last 5 years forcing many inefficient operators to close. The industry is however, expected to recover and grow over the next 5 years as businesses emerge from the COVID-19 crisis. [2]

Fig. 1



Businesses providing Motor Maintenance and Repair services are anticipated to have revenue significantly effected due to consumers using their vehicles less over the COVID-19 lockdown period.

The industry has posted a 2.7% decline in revenue for 2020 with a 4.5% drop in employment, however, the number of motor vehicles in Australia is projected to increase over the next five years which in turn should drive revenue upwards thanks to an increase in sales.

Ongoing investment in research and development has driven innovation in the sector. Advanced technology in modern vehicles has forced manufacturers to invest in specialised equipment and training for staff, providing opportunities for employment in, highly skilled, specialised roles in the future. [3]

"Businesses that would otherwise have failed are being kept alive by a combination of the Government's measures, designed to give temporary support to going concern businesses"

Joshua Robb
Associate Director

1 ASIC Australian Insolvency Statistics Series 1A
2 IBISWorld Report S9520 Hairdressing and Beauty Services
3 IBISWorld Report S9419 Motor Vehicle Engine and Parts Repair and Maintenance

IN FOCUS

External Administrations
Key Industry Trends

Growth in the construction industry over the past five years has been largely due to the demand in apartment construction and non-residential building markets. Due to the COVID-19 pandemic, revenue is expected to have declined an anticipated 7.9% by year end.

Demand from non-residential construction is likely to decrease as investor confidence in the market remains low. The drastic changes to working conditions, led largely by restrictions imposed by the Government, has meant that with more Australians working from home and shopping online, new investment in construction projects for offices and retail stores is likely to face further downward pressure.

Government commitments to investing in infrastructure projects to assist in the recovery of the economy is expected to have a positive effect on employment levels, which have declined by 3.8% over 2020.

2020 Key Figures:

- 6.8% decline in profit
- 2.2% decline in total number of businesses
- 5.8% decline in revenue[1]

Restrictions on travel and closure of dining and entertainment establishments throughout the COVID crisis have had a severe effect on the Accommodation and Food Services industry.

The closure of borders crippled tourism, with hotels and resorts suffering with a projected decrease of 23.8% in revenue in the current year. Having faced increasing competition from serviced apartments and private properties through online platforms over the past five years, restrictions compounded the pressure many operators were feeling with statistics indicating a 16.5% decline in employment over the current year.

Recovery is expected over the next five years for the industry but will be largely driven by domestic tourism as the Government navigates a framework for rebuilding international tourism.

Restaurants have faced similar issues with limited capacities on venues throughout the pandemic limiting industry turnover. Further, discretionary income is expected to fall dramatically in 2020/21 due to reduced support measures and high unemployment, limiting recovery to some extent.

Pubs, bars and nightclubs have also experienced limited earning capacity, particularly in Victoria where an extended lockdown has severely effected the industry.

As restrictions are wound back further toward the end of year holiday period and with international tourism still in limbo, domestic tourism is expected to increase relative to Australia's economic recovery, which will provide a boost for the industry as whole.

2020 Key Figures:

- 15% decline in revenue for restaurants with 12.2% decline in employment
- 18.1% decline in revenue for pubs, bars and nightclubs with 17.2% decline in employment
- Overall revenue for pubs, bars and nightclubs expected to fall to $12.6 billion - restaurants dropping to $18.5 billion over five years to 2020/21[2]

Figure 2 below shows the top 5 industries with the highest number of insolvencies.

"Businesses will need to face the reality that they are going to have to continue to deal with the residual debts from COVID-19"

Stuart Otway
Director

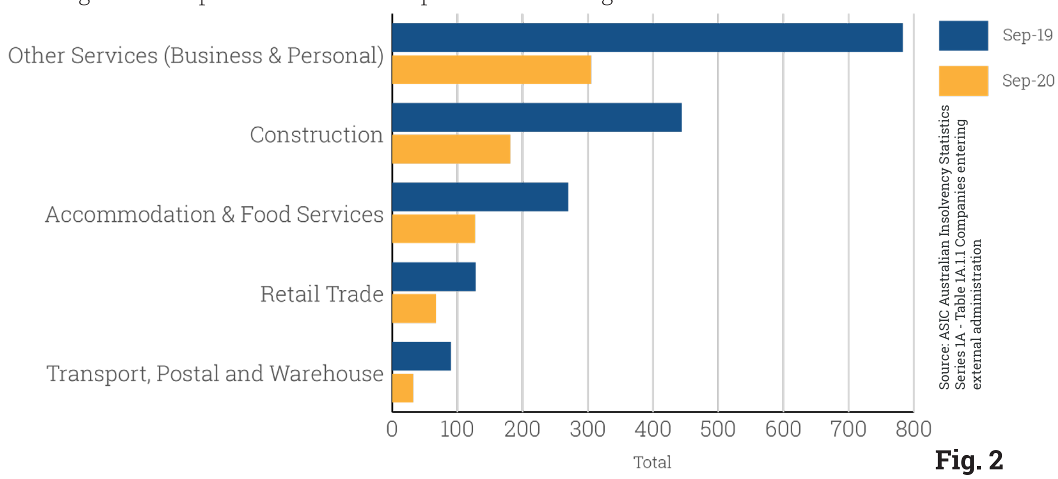


Fig. 2

1 IBISWorld Report E Construction In Australia
2 IBISWorld Report H4520 Pubs, Bars and Nightclubs

PERSONAL INSOLVENCY

Personal Insolvency statistics saw a significant decline over the September Quarter with figures from AFSA indicating a 50.9% decrease compared to the same period in 2019. Bankruptcies for the September 2020 Quarter were at their lowest since AFSA records began in 1986. Of these, 26.3% entered a business related personal insolvency.

Key Stats (see Fig. 4) :

- Bankruptcies (Part IV & XI) - 1,676 matters down from 3,692 in September Quarter 2019
- Debt Agreements (Part IX) - 1,247 down from 2.266 in September Quarter 2019
- Personal Insolvency Agreements (Part X) - 23 down from 48 in September Quarter 2019[1]

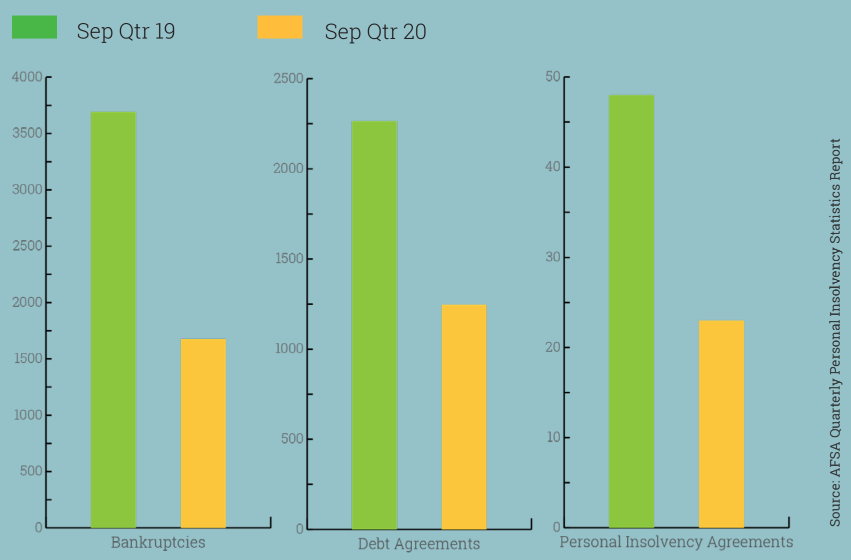
The Federal Government's JobKeeper subsidy, coupled with record low interest rates and a variety of support programs including additional childcare subsidies, bank loan deferrals and superannuation withdrawals, have assisted households in coping with financial setbacks, playing a significant role in the decline in personal insolvencies.

CommSec notes that personal credit also contracted by 10.5% over the year to June, the largest annual decline on record, further supporting the trend of Australians being reluctant to take on more debt since the Global Financial Crisis[2].

Part X appointments have been in decline since reforms in 2004, primarily due to the introduction of Part IX Debt Agreements in 1996 and general creditor skepticism surround Part X agreements.

The continued decline may also be attributed to a lack of interest by debtors, where one of the primary benefits of the previous system was that it limited the examination of their affairs.

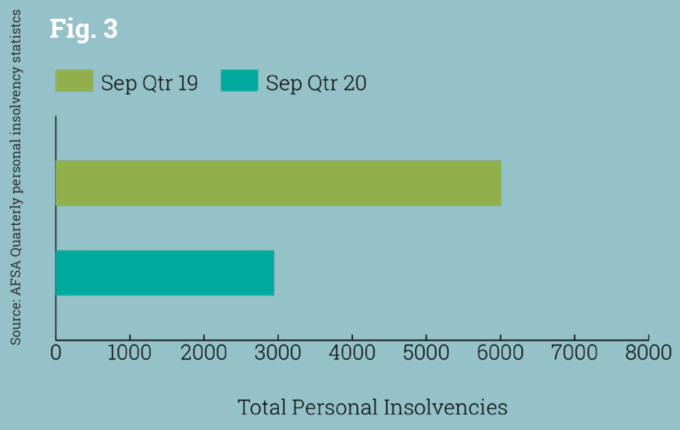
Fig. 4



"When considering a Personal Insolvency Agreement, a debtor should step back and impartially inspect their affairs. They should attempt to form a view on how a controlling trustee may interpret their affairs."

Brett Harron
Supervisor

Fig. 3



What does insolvency mean?

Insolvency means an individual or entity (such as a company) can no longer pay its debts when they fall due. Insolvency can be personal (relating to an individual) or corporate (relating to a company). For each type of insolvency, there are different laws, rules and regulations that are applied.

1 AFSA Quarterly Personal Insolvency Statistics Report
2 CommSec Economic Insights - August 7, 2020

September Qtr 2020 saw a significant drop in personal insolvency activity **with a total decrease of 50.9%**

2946

T he number of personal insolvencies YoY for the September Quarter saw a significant decline with a total change of -50.9% down to 2,946 from 6,006 the previous year (see Fig. 3).

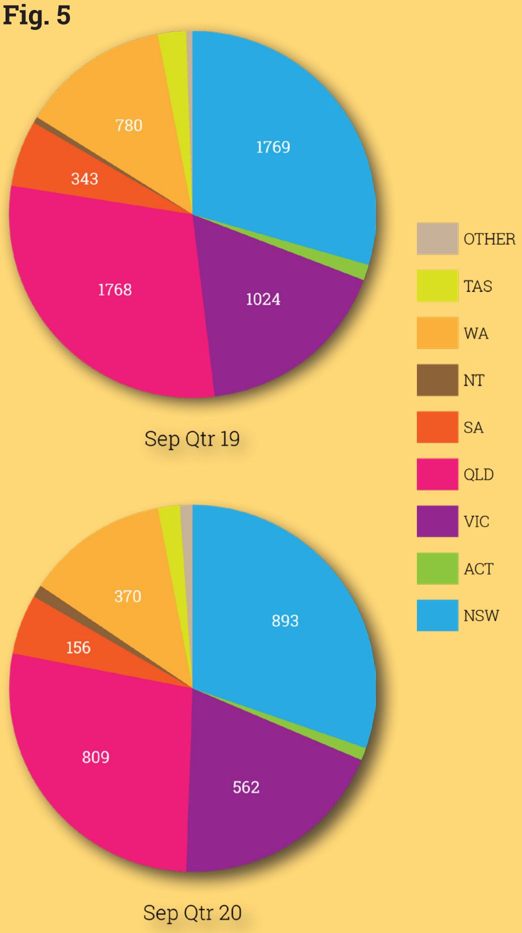
Bankruptcies (Part IV and XI) were down by more than half the number on the previous year with a reduction of 54.6%.Each state, other than ACT, recorded a drop of activity more than 50% (see Fig. 5).

Debt Agreements (Part IX) declined by 45% nationally with each state reporting a reduction of more than 30%. In particular, New South Wales saw 369 new Debt Agreements in the September Quarter 2020, down from 695 the previous year. Queensland record similar figures with 342, down from 690 in 2019.

Key stats:

- 2,946 total new administrations, down from 6,006 in September Quarter 2019
- New South Wales with 893 new administrations down from 1,769 in 2019
- Queensland with 809 new administrations down from 1,768 in 2019

Fig. 5



Source: AFSA Quarterly personal insolvency statistics

1 AFSA Quarterly Personal Insolvency Statistics Report

The Outlook

WHAT'S TO COME?

The new year is fast approaching and, as businesses re-open around the country and take stock of their given situation, many will have to make difficult decisions. From an insolvency perspective, whilst there may not be the anticipated influx of new administrations, with expected changes to insolvency laws coming into effect from January 2021, many businesses will more readily understand their position and have to face the reality of their circumstances and the options available to them.

Here's what to you need to know:

The Debtor-In-Possession Restructuring Process as part of the forthcoming insolvency legislation will have specific eligibility criteria a business must meet including:

- liabilities of less than $1 million (excludes contingent debts, includes secured debts)
- no prior debtor-in-possession restructuring process involvement in the last 7 years (subject to some minor exceptions)
- company must have substantially complied with all employee entitlements and tax returns, statements and BAS lodgements

Additionally, a Small Business Restructuring Practitioner must be appointed to oversee the process.

Simple Liquidations, which form the other side of the proposed changes, are intended to reduce time and cost in comparison to the current liquidation process in relation to investigation, creditor meeting and reporting requirements. Eligibility criteria for businesses include:

- liabilities of less than $1 million
- no prior simple liquidation involvement in the last 7 years (subject to some minor exceptions)
- must have lodged all prescribed taxation documents with the ATO

Once support measures begin to expire, it is expected that the number of insolvencies will increase. It is important that businesses understand the new options available to them and get in contact with a professional insolvency practitioner as soon as possible.

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Publication

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