ASSET BASED FINANCE ASSOCIATION

LATE PAYMENT

An analysis by sector

Late Payment: An analysis by sector

Introduction

For any business, the length of time taken for invoices to be paid is critical. It determines cash flow, the business's ability to invest and grow, and ultimately its financial stability. Delays in payment have become more commonplace since the financial crisis and have a knock-on effect down the supply chain - and a small business at the end of that chain will be hit particularly hard.

The Federation of Small Businesses recently reported that one in five small businesses in UK is 'bullied' by its big business customers.

The payment practices of some of the UK's biggest businesses have hit the headlines in recent times, with the supplier contracts used by supermarkets coming under particular scrutiny.

The aims of this White Paper are to analyse, using data from Companies House, the scale of late payments across the economy to assess whether certain industry sectors are more adversely affected than others and to identify in which areas the situation is improving.

Taking a five-year view, we also compare what effect, if any, the economic recovery is having on the average time taken between invoicing and payment. The issue of payment delays remains pertinent even as firms start to see the business outlook improve.

In an economy where late or extended payment of invoices is still a live issue across a huge range of sectors, businesses are inevitably seeking out sources of finance that will enable them to invest and grow. Asset based finance is a key form of funding for businesses, with £19.4 billion being advanced to UK and Irish businesses at the end of December 2014. Invoice finance is the most popular type of asset based finance, with funding provided against invoices – against the debts owed to client businesses by their customers.

The ABFA is continuing to campaign for all businesses to be able to use asset based finance. The Government published a consultation in December on outlawing so-called 'bans on assignment' – clauses written into contracts by big businesses that can prevent their SME suppliers from using their unpaid invoices as a source of funding.

We urge the incoming Government to keep this issue on the agenda and implement regulations ensuring that all businesses can use asset based finance to access the funds that will fuel their growth.

About the ABFA

The Asset Based Finance Association (ABFA) is a trade association representing the asset based finance industry, an industry supplying much needed liquidity to UK and Irish businesses. The main types of finance provided by the industry are invoice finance (factoring and invoice discounting) and asset based lending. ABFA Members include the UK and Irish high street banks, specialist and challenger banks, the specialist businesses of some international banks and corporates, and a number of independent non-bank finance providers.

As well as providing information about the products and services provided by the industry, in 2013 the ABFA established an independent Standards Framework for its members and their clients. The Framework incorporates: a new ABFA Code and supporting Guidance, setting out the standards which clients and potential clients can expect from ABFA Members; an independent Complaints Process delivered by Ombudsman Services; and an independent Professional Standards Council. This Framework has been designed to allow more businesses to use asset based finance with confidence. Further information about the Framework can be found at: www.abfa.org.uk/standards.

About Asset Based Finance

There are two basic types of asset based finance.

Invoice Finance: The two main types of invoice finance are factoring and invoice discounting. Both allow businesses to release the working capital tied up in their unpaid invoices. In both the finance provider will normally purchase the client's outstanding invoices, providing an immediate initial payment of the majority of the invoice, with the remainder (less the financier's fees) paid to the client on payment by the debtor. Factoring incorporates an added service element, with the financier normally managing the credit control and collections process. This makes it particularly suitable for smaller businesses. In an invoice discounting facility the client would normally manage its own credit control. The majority of the funding currently provided by the industry in the UK and Ireland is through invoice finance facilities.

Asset Based Lending: An asset based lending facility will provide a broader mix of funding including revolving and amortising structures against the entire range of business assets. Traditionally advances are available against debts, inventory, real property, plant and machinery, but can be arranged against intangible assets such as brands and forward income streams.

Executive summary

Key findings of our research include:

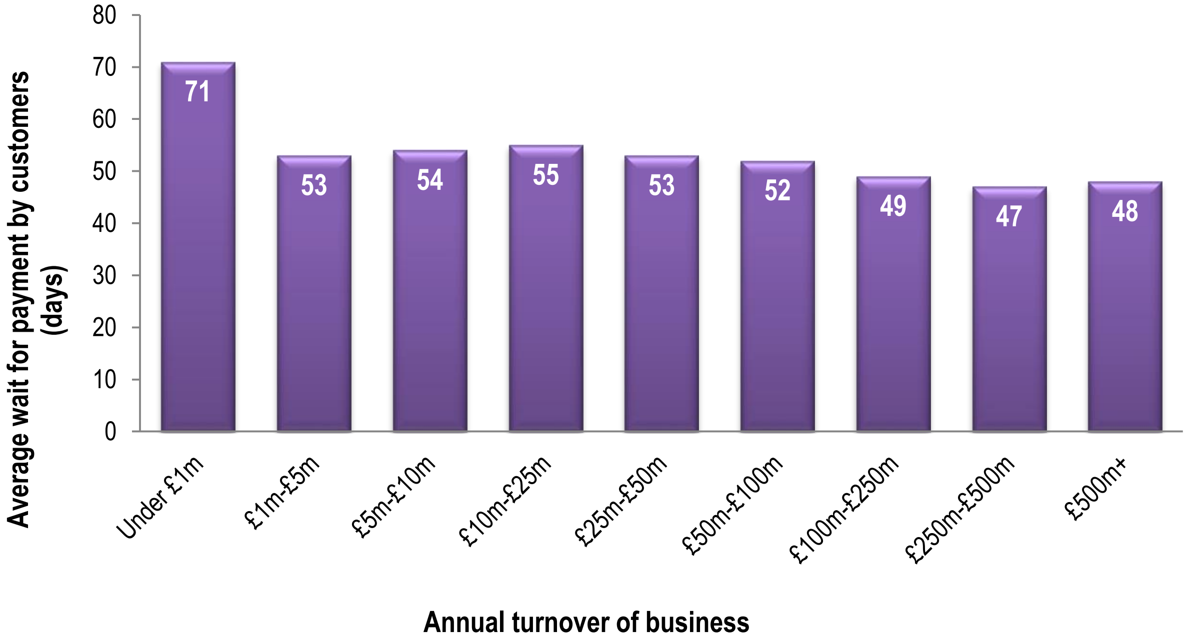
- Despite the economic recovery, which should allow for more prompt payment of suppliers, the average time taken for invoices to be paid has risen since 2008.
- There is a stark difference between the payment delays experienced by small businesses and their larger rivals. Small businesses – those with an annual turnover of under £1 million – have to wait an average of 71 days for invoices to be paid, compared to 48 days for the largest businesses (annual turnover of £500 million or more).
- The construction and real estate sector are particularly adversely affected by long waits for payment. Waits for payment have increased by 22 per cent in the last five years to 107 days, from 88 days in 2008.
- Extended payment periods are also common in the professions, with lawyers and accountants seeing payment periods increase from 72 days in 2008 to 78 days today.
- UK food and drink producers have seen a sudden jump in the amount of time they wait for payment from their customers, with average waits increasing from 44 days to 47 days in the last year alone. Concerns have recently been raised over supermarkets forcing their suppliers to accept lengthened payment terms, as these retailers respond to the growth of discount supermarkets.
- Businesses in the hospitality sector – hotels, restaurants and bars – have some of the shortest waits for payment, at an average of just 20 days, down by a fifth on 2008, as they reap the benefits of their ability to enforce up-front payment.
- Many of the sectors that have enjoyed the biggest improvements in payment delays provide services to publicly funded bodies. The education sector and museums and libraries have both seen their average debtor days fall by around 50 per cent since 2008, thanks to central Government pressure on public sector bodies to pay invoices promptly.

Despite the recovery, the average wait for payment is longer now than in 2008

Despite the improvement in the economy since 2009, the waits for payment that worsened during the credit crunch have not shortened. In fact, the average UK business now waits 63 days for an invoice to be paid, compared to 62 days in 2008.

As with so many of the strains faced by British businesses in the last five years, SMEs have borne the brunt of the late payment problem.

SMEs waiting three weeks longer for payment than biggest businesses



Businesses in the construction and real estate sector are suffering the longest waits for their invoices to be paid, with delays now averaging more than 15 weeks. Waits for payment in this sector have increased by 22 per cent in the last five years to 107 days, from 88 days in 2008.

In the construction and real estate sectors, there has been a long history of delays in payment, and despite numerous attempts by several Governments to improve the situation, these figures show that the problem is actually worsening.

This is putting continuing pressure on a sector which has not yet fully recovered from the collapse in the property market of 2008/9. For a lot of construction businesses, the effects of the recession were exacerbated by the difficulties they had in getting paid on time for the contracts they did win.

Long supply chains in industries like construction mean that the ripple effect of delays is likely to affect many other businesses further down, with SMEs hit the hardest. In an industry with high overheads in terms of materials and labour costs, this can be a particular problem.

Architects have also been hit by the construction industry slow-down, seeing their invoices remain unpaid a full ten days longer than they did in 2008, up from 61 to 71 days on average.

One driver of this may be the unwillingness of firms in the professions to proactively pursue debts in an effort to retain clients in the long term. This may be borne out by the fact that lawyers and accountants saw their invoices paid six days later on average this year than in 2008, with waits increasing from 72 to 78 days.

Finally, there are several sub-sectors of the manufacturing industry that are among both the ten sectors with the longest overall waiting times, and the ten sectors in which waits for payment have grown the most since 2008.

Asset based finance has been able to make a particularly positive impact in mitigating the effects of late payments in manufacturing, supporting continued investment and growth. Manufacturers made up 30 per cent of all users of asset based finance in the UK at the end of the third quarter of 2014.

Ten sectors facing the biggest increases in payment delays since 2008

Industry	Increase	Average wait for payment 2008 (days)	Average wait for payment 2014 (days)
Construction and real estate	22%	88.1	107.3
Architects	17%	60.7	71.2
Advertising	13%	67.8	76.5
Oil & gas extraction	12%	51.5	57.5
Legal and accountancy	9%	71.7	78.2
Construction	8%	84.1	90.4
Manufacture of machinery	7%	64.2	68.6
Manufacture of motor vehicles	6%	46.6	49.2
Computer programming	5%	59.0	61.7
Manufacture of food products	5%	44.4	46.6

Ten sectors with the longest delays in awaiting payment for invoices in 2013

Industry	Average wait for payment 2014
Construction and real estate	107.3
Legal and accountancy	78.2
Advertising	76.5
Architects	71.2
Scientific research and development	69.6
Manufacture of pharmaceuticals	69.4
Manufacture of machinery	68.6
Manufacture of electrical equipment	67.0
Publishing	66.4
Waste management	65.4

Restaurants, bars and hotels receive payment from their invoices most promptly (in days)

The hospitality industry tops the list of those sectors seeing the most prompt payment, with restaurants, bars and hotels being paid in an average of just 20 days.

Payment delays for both sectors are down by around a fifth, from 25 days and 26 days respectively five years ago.

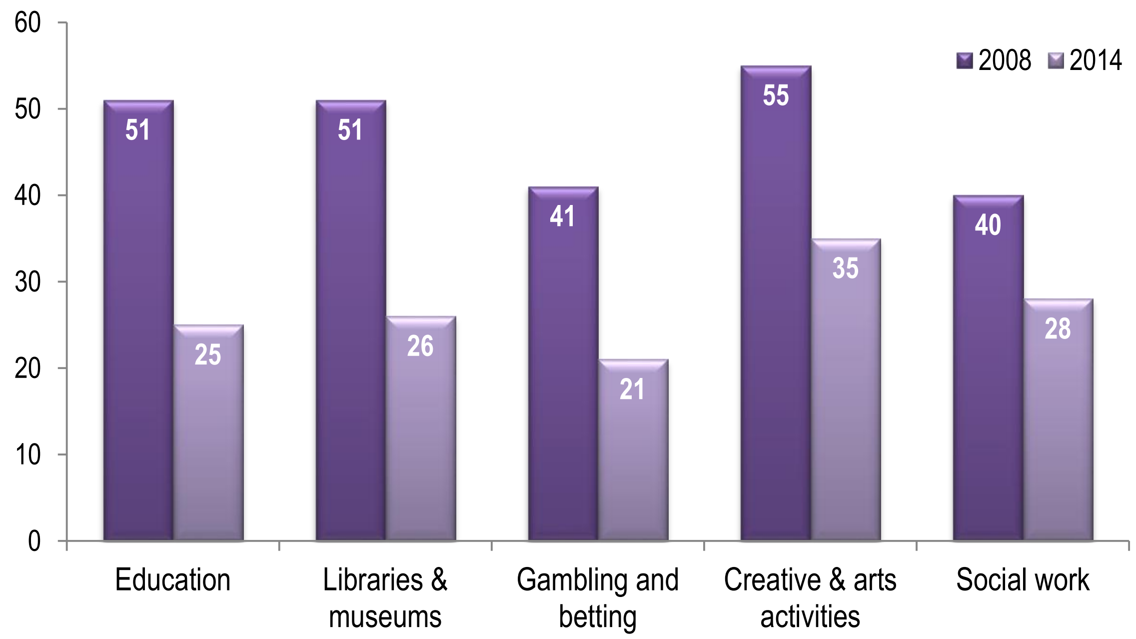
The standard in many consumer-facing businesses is for upfront payment, or even payment in full or a charge on a credit card in advance, an option not open to many of the businesses at the other end of the payment waits table*.

Increasing demand for corporate events and hospitality as the economy recovers may be one reason why payment times have fallen, giving these businesses greater confidence to impose payment terms slightly more robustly with less worry about damaging relationships with repeat customers.

Five sectors with the shortest average waits for payment

Industry	Average wait for payment 2014
Restaurants and bars	19.9
Hotels	20.1
Gambling and betting	21.4
Residential care	22.9
Vets	23.5

Five biggest decreases in average delays receiving payment



Some sectors have seen payment delays fall significantly over the last five years

Many of the sectors that have enjoyed the biggest reductions in payment delays provide services to publicly funded bodies. The education sector and museums and libraries have both seen their average debtor days fall by around 50 per cent since 2008 to 25 and 26 days respectively, thanks to central government pressure on public sector bodies to pay invoices promptly.

The health and social work sectors have also enjoyed reduced waits for payment. They now see debtors pay invoices in 28 and 36 days respectively, down from 40 and 49 days in 2008.

Since 2010, Central Government departments have been ordered to pay 80 per cent of invoices within five days, although the actual proportion of invoices paid within five days has routinely topped 97 per cent in the past year. Local government targets are less stringent, aiming for all invoices to be paid within 30 days of receipt.

Central Government pressure on other public sector bodies to pay promptly is now clearly paying off, with organisations higher up the public sector supply chain feeling the benefits.

The ten sectors which have seen the largest decrease in waits for payment since 2008

Industry	Decrease	Average wait for payment 2008 (days)	Average wait for payment 2014 (days)
Education	-50%	50.9	25.3
Libraries & museums	-49%	50.9	26.1
Gambling and betting	-48%	40.9	21.4
Creative & arts activities	-36%	54.6	35.2
Social work	-31%	40.3	27.7
Membership organisations	-28%	59.0	42.8
Healthcare	-27%	49.4	36.2
Residential care	-26%	30.8	22.9
Hotels	-23%	26.0	20.1
Restaurants and bars	-21%	25.1	19.9

Conclusion

Our sector by sector analysis reveals some stark differences in payment practices between different industries. While some businesses– primarily those related to the public sector – are seeing improvements in payment times, many others across the private sector are experiencing long and increasing delays.

Alleged mistreatment of suppliers has become headline news in recent months, shining a light on the payment practices of some of the UK's biggest businesses, and what can be devastating effects on SME suppliers.

Long supply chains in industries like construction mean that the ripple effect of delays is likely to hit smaller businesses the hardest. For smaller businesses that are already struggling with a lack of available lending from traditional sources, late payment of invoices is a substantial barrier to investment and growth.

Initiatives such as the Prompt Payment Code, which encourages larger businesses in particular to reduce the length of time it takes them to pay their suppliers, and the 2013 Late Payment of Commercial Debts Act, giving SMEs the power to levy interest on late payments, are well-intentioned, but have yet to have a noticeable impact on debtor days.

Asset based finance can enable businesses to access the value of their invoices up front, bridging the gap between doing the work and getting paid. It gives businesses the freedom to invest in the capacity, personnel, research and assets that they need to grow as soon as they need to, not just when their client's cheque finally hits the doormat.

** ABFA Members only fund B2B transactions and do not fund debts owed by consumers*

For further information about asset based finance and how it can help businesses unlock their cash-flow please visit the ABFA's website at www.abfa.org.uk.

Research undertaken by Mattison Public Relations. For further information please call 020 7645 3636 or email info@mattison.co.uk.

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