Bankruptcies, Insolvencies Surging with Economic Uncertainty Ahead

J.C. Penney. Pier 1 Imports. 24 Hour Fitness. Brooks Brothers. Ruby Tuesday. The list goes on and on, but what do these companies have in common—a high-end men's retailer, national gym and department store?

Collins Dictionary announced its Word of the Year on Nov. 10 as "lockdown," giving consideration to many others, including "coronavirus," "social distancing" and "BLM" (Black Lives Matter). Those words, among many others, have impacted peoples' lives dramatically since March, and the coronavirus has no doubt burdened businesses and their workers as well. However, "bankruptcy" might very well be the word of the year for businesses this year, next year and going forward.

Some businesses have survived, hanging on by a threat, while others have seen their share of new opportunities. J.C. Penney received new life with a deal to avoid liquidation and save roughly 60,000 jobs, notes CNBC. Others, such as businesses that rely on the in-person aspect—restaurants, movie theaters, etc.—continue to struggle with bankruptcy, a foregone conclusion or on the horizon.

According to the latest data from the American Bankruptcy Institute, total bankruptcy filings declined 41% in October from last year. However, commercial Chapter 11 filings increased by 4% year over year. "Families and businesses are faced with increasing financial challenges due to the COVID-19 pandemic and growing debt loads," said ABI Executive Director Amy Quackenboss in a release. "The expiration of government relief programs, high unemployment and a difficult financial outlook for many sectors will likely lead to filings increasing in early 2021."

The uncertainty caused by the pandemic over the last eight months has impacted credit departments and how they protect themselves and their companies. With the continued rise of COVID-19 cases in the U.S., the future is also clouded in regard to the way credit professionals are able to do their jobs. Despite some changes in the journey, the destination is the same: protecting the company and its assets.

Evaluating risk has always been important and at the forefront of credit department processes, but now, mitigating risk and gathering information to do so is even more vital with the pandemic. Cheryl Vail, senior credit analyst with fitness equipment brand SportsArt, said she is "checking credit bureaus more frequently and watching customer terms; staying closer in contact with those accounts and monitoring much more closely than normal."

The business insolvency outlook through the first half of 2021 has deteriorated, according to the e-book, "A Surge in Bankruptcies and Insolvencies: How to Keep Your Business Afloat," from Euler Hermes. The trade credit insurer predicts insolvencies will rise 57% in the U.S. by 2021 and by 35% globally compared to 2019 levels.

Doing business with a company going through bankruptcy can be tricky. Among the options to consider when accepting new business from one that has filed a Chapter 11 bankruptcy are shortening credit terms, requiring cash on delivery and requiring a deposit or a letter of credit before delivery, states Euler Hermes. "If you are doing business with a company in Chapter 11 bankruptcy, you should carefully review your client's monthly operating reports to understand its creditworthiness," according to the e-book. "Understanding the creditworthiness of any customer is important in guarding your own business' cash flow."

There are also steps that must be taken prior to a customer filing for bankruptcy, when nonpayment first surfaces. The process starts by having an invoice cadence with actionable steps once receivables become past due. Euler Hermes states that this practice can provide a "valuable paper trail" should action need to be taken. Once nonpayment occurs, contact the customer and find out the reason for nonpayment. This is also a time to explain the consequences of nonpayment. Euler Hermes suggests having a standardized business practice with timetables and payment schedules written into a contract. New policies, such as cash in advance or different forms of payment, can mitigate issues.

As stated before, credit departments are here to protect their company, and monitoring a customer's creditworthiness is one of the functions assigned to credit professionals. While the current economic plight has impacted many, credit departments have continued powering through credit decisions for new and current customers.

Despite not having a bankruptcy in over four years, Vail said, "This year could be a game changer." But she believes "the future of credit will remain the same for the time being."

During the month of November, FCIB is offering three country-specific webinars, free to members, on insolvency laws in Brazil, France and Germany. These webinars are part of a series available online to members in the Academy of Global Credit, located in the FCIB Knowledge Center. Insolvency laws in the United Arab Emirates will be covered in January.

—Michael Miller, managing editor