ProfitGuard | September 2017

Credit Outlook: Metals Sector

Key Risks

- **DSO in the metals segment has lengthened** as conditions and pricing recover in 2017; more competitive terms are being offered.
- **Major U.S. insolvencies have increased overall** YTD 2017- Credit risk remains present but absent on many minds
- **Tension in working capital requirements is emerging** on the heels of higher commodity prices and rising interest rates, meaning higher accounts receivable balances and longer credit terms. This is straining firms' liquidity (cash or borrowing availability) and is a unique area where credit risk is heightened.
- **Consumption and investment is up, but so is debt** – elevated debt in the industry is mainly the result of increased private equity activity. Long term it's not sustainable in this industry; as soon as the market dips again, it could spell trouble.

Current Environment

In our view, the metal segment is experiencing strong market conditions for the most part. However, credit risk remains at a moderate level in our view due to a few drivers. We are seeing a trend toward more competitive credit terms, the return of insolvencies, working capital tension, and persistently elevated debt leverage on many balance sheets.

With the drastic recovery in metal pricing from the recent doldrums, many suppliers are offering more competitive credit terms to win business. Waiting longer to get paid does come at a price though. Open credit exposures will grow and thus so will credit risk in most cases.

Secondly, we are seeing an emerging trend in working capital management. Companies are being hit from two fronts, one a rising price environment and two, a rising interest rate environment. Credit is becoming somewhat more expensive as interest rates begin their climb to more normal levels. To adjust to this, many companies are trying wring out excess cash tied up in inventory or receivables. The tension on this front is in trying to collect faster, pay slower, and balance liquidity needs.

In this current pricing environment, some firms are getting caught in a cash crunch as their liquidity is being consumed by higher levels of activity and higher prices for metal. On the credit front, this is an area we are seeing an increase in risk. Several firms have had to refinance or look for new capital to accommodate the increased working capital requirements. While working through these tensions, customers are being paid even slower or in some cases, not at all.

Current Credit Risk

As interest rates begin to increase the credit and financial impact of poor working capital management can be magnified through higher borrowing needs and cost of capital. This is a key area we see credit risk intensifying on top of persistently high levels of debt still on many balance sheets.

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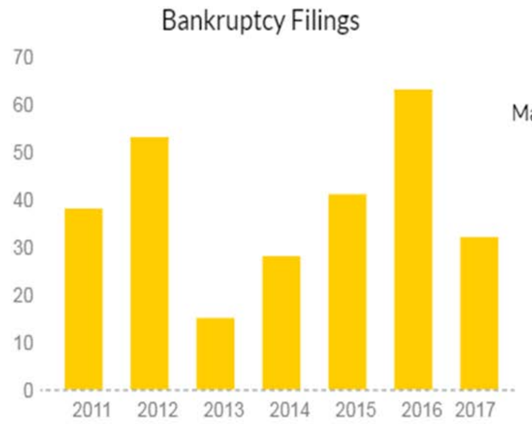
Know The Risk *Before* You Ship

Bankruptcy Trends

PG has tracked 270 bankruptcies in the metals segment over the last seven years. Since our last outlook in March we have seen a 5-6% increase in both chapter 11 and chapter 7 bankruptcies and an overall increase of 13,239 in total business bankruptcy filings.

According to the Atradius Q3 insolvency forecast report; since last year, “the number of overall business insolvencies has been steadily increasing, could continue, and worsen largely due to uncertainty; which may reduce business investment.”



The American Bankruptcy Institute recorded 22,656 U.S. commercial filings in 2017 year to date, a 0.5% (or 106 filings) an increase from last year’s 22,550 during the same period. Along with the energy, paper, retail, and textile markets, the metals segment still remains in the top segments for business defaults this quarter.

What this means for Corporate Credit

In times of moderate corporate credit risk, it’s important to remain aware of credit risk and not become complacent or lax in your credit approval or risk monitoring strategy. Credit risk remains present but absent on many minds which is common in favorable economic times.

PG recommends taking a fresh look at your key accounts and begin reevaluating your customer credit risk now before an unexpected risk event occurs. PG can assist you with reviewing buyer risk, recommending appropriate credit limits, and monitoring your key accounts. Also, PG can assist with insuring your credit risk through its sister company Global Commercial Credit.

ProfitGuard is the leading provider of business credit information to the metals industry of North America. PG assists its clients in managing trade credit risk with valuable credit analysis, credit risk ratings, recommended credit limits, and risk monitoring of their customer portfolios. With PG’s information service, businesses are able to make more informed credit decisions, minimize bad debt losses, and more effectively manage credit risk to remain competitive in today’s rapidly changing marketplace.

To find out how ProfitGuard can help your business, please contact us at **(866) 990-1099** or visit **eprofitguard.com**.