Credit Insurance for the Retail Sector: Managing Risks in an Ever-Changing Market

The number of companies going bust in 2023 is at its highest since the 2009 financial crisis. Recent government figures show insolvencies rising 10% year-on-year in the three months to the end of September. Insolvencies in the retail sector are second only to the construction industry. In fact, in the 12 months to Q3 2023, insolvencies in retail jumped 52%.

We have to understand this in the context of a constantly evolving market, and the still ongoing effects of Brexit. In this article I explain these factors in more detail and how they can be mitigated.

The role of Trade Credit Insurance in retail

For retail, trade credit insurance (TCI) is a particularly crucial tool for businesses to manage their credit risks. This is because businesses in the sector often operate on thin margins and so are unable to afford significant payment defaults.

And this year has seen some significant failures. The market has been exacerbated by the cost of living crisis squeezing consumer spending. Among the 900+ retail business failures have been well-known brands including Cath Kidson, Wilko, M&Co, Paperchase and Hunter Boots. Some of these were high street staples and it demonstrates how delicate the current trading climate is.

But for suppliers to the retail sector, trade credit insurance can manage this risk. It enables them to trade with confidence, knowing they are protected against sudden non-payment.

A trade credit insurance policy is also an important tool when it comes to loss payee assignments.

When a bank or a financial institution funds a business through non-recourse factoring (which excludes insurance) or invoice discounting, they nearly always require the credit insurance policy to be assigned to them. This is either via a banker's endorsement (the bank has the same controls over the policy as the policy holder, and claims are paid to them directly) or a loss payee assignment, which is a simple clause telling the insurer to pay claims payments directly to the bank or finance company. If the loss is not directly funded then a waiver is issued.

Through a loss payee assignment, a trade credit insurance policy can be assigned to trade finance and banks. Also with insured invoices, suppliers can potentially access better financing terms from lenders.

Unprecedented changes in the retail sector

The UK retail sector faces unique challenges compared to other industries: Fluctuating consumer demand; the rise of e-commerce; and changing shopping habits following the COVID pandemic. These factors have led to unpredictability in revenue streams.

A trade credit insurance policy allows suppliers looking to work with new buyers or enter new markets - including export markets - to do so in the knowledge that they're covered if things go wrong.

Because of these trends, retail is a sector that is undergoing significant transformation. Changes in consumer behaviour have led a shift from bricks-and-mortar to online shopping. This has in turn led to the emergence of omnichannel retailing - a strategy in which retailers and brands engage customers through multiple integrated digital and physical touchpoints, such as physical stores, websites, social media and apps.

This transition can be helped by trade credit insurers, not just through protecting against potential debt but also because they bring expert market knowledge, providing insights into the creditworthiness of potential buyers. This aids in making informed decisions.

The effect of Brexit on the retail industry

Brexit has caused uncertainty in trade relationships, currency fluctuations and disruptions in supply chains. This has had a significant impact on the UK retail industry, and brought with it fresh challenges.

With the UK no longer part of the EU single market, trading with EU-based buyers now comes with more potential risks. After talking with owners of businesses of all sizes, I've observed that trading with EU buyers post Brexit brings many issues that previously didn't exist. More than a few say it's the worst thing to happen to the UK since the Second World War. These include:

1. Customs declarations: Goods needing to go through customs with full documentation can be complex and time consuming, causing delays.
2. Border delays: This can be seen on a daily basis with increased border checks affecting the supply chain and just in time deliveries.
3. Tariffs/taxes: Often now imposed between the UK and EU; tariffs on many types of goods were previously tax free.
4. Goods now not meeting EU standards: Some goods no longer automatically meet EU standards and this can change at very short notice.
5. Regulatory and legal restrictions, including data protection: This can potentially lead to non compliance with EU laws and can change at very short notice.
6. Legal enforcement: The collection of overdue debts now often requires specialist intervention.
7. Passporting: A massive oversight by the UK government. One of the biggest issues, especially in the early days of Brexit, is financial services passporting. This meant, from day one, that UK businesses with subsidiaries or offices in Europe have often had to completely change the way they insure those businesses. This resulted in using either EU insurance companies, or brokers, or both, often with considerable cost implications.

Retailers could also suffer if suppliers face financial difficulties due to Brexit-related disruptions. Again this is where trade credit insurance comes in, helping secure the supply chain by ensuring suppliers are protected against non-payments.

Another consequence of Brexit is it has led to significant GBP volatility. While trade credit insurance doesn't directly protect against currency risks, it indirectly offers stability from suppliers to retailers by safeguarding against payment defaults.

Trade credit insurance as a tool for growth

In an ever-changing market, especially post-Brexit, trade credit insurance is an invaluable tool to thrive and grow in the UK retail sector. It offers financial protection, enables informed decision-making, and provides the confidence to navigate uncertainties.

As the market continues to evolve, the suppliers to retailers who have a policy in place will be better poised to face challenges and seize opportunities.

Contact us

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