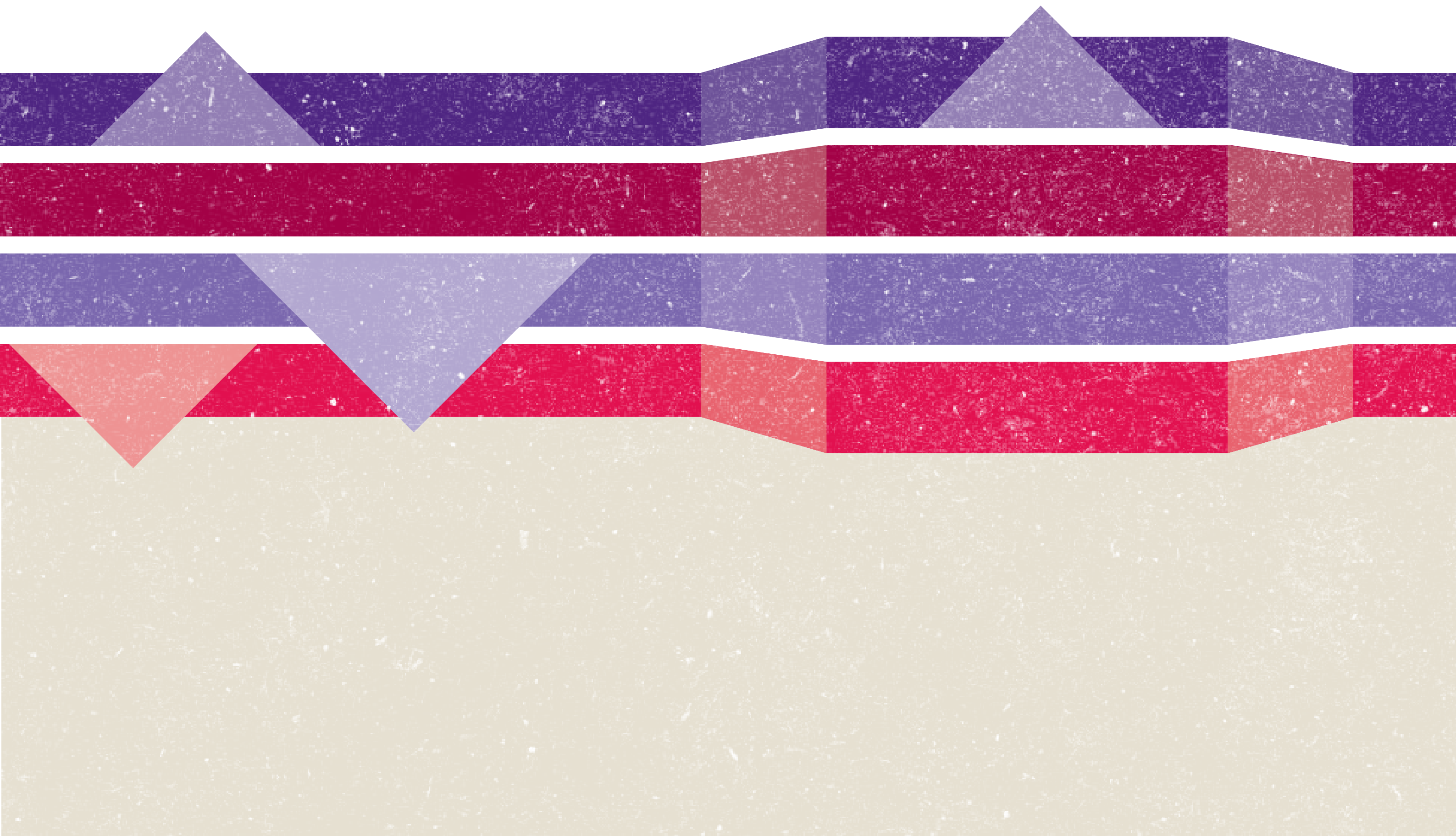
NOVEMBER 2013

Lenderview

A challenging year ahead



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Summary of survey findings

In October 2013, Grant Thornton surveyed senior lenders who attended its Banking Conference series held in Adelaide, Brisbane, Melbourne, Perth and Sydney. 156 lenders from across the lending, credit and asset recovery areas of 22 financial institutions completed the survey.

Here are the results:

1 Businesses will have to prepare themselves for further tough economic conditions in the next 12 months

Most sectors of the economy are feeling the squeeze of Australia's slow growth rates, high Australian dollar and rising costs. The sectors that are being impacted most are automotive, manufacturing, printing and retail.

2 Funding is available if the business has a solid business case

Difficulties accessing equity finance is rated as an issue by 58% of respondents, with almost 50% of respondents listing access to debt as an issue. Access to debt and equity is likely to continue to be an issue for Australian businesses, with the majority (63%) of respondents indicating that availability of debt will not change in the next 12 months.

3 A strong management team is the key to success in these difficult market conditions

The respondents overwhelmingly state that the major cause of business distress is poor management. Many underperforming businesses can be turned around through improved management and financial and operational restructuring.

4 There are opportunities for innovative businesses

The respondents report that most businesses remain cautious and are using traditional measures such as cost-cutting to manage through the tough business conditions. Few businesses are looking for opportunities to re-align strategies to grow sales or alternatively create shareholder value. Given the growth prospects in our region and changing customer trends, this may mean missed opportunities for many businesses.

5 The level of corporate distress is most likely understated

Banks are commonly working with customers to resolve performance issues through measures such as financial and operating restructures, forbearance and debt rollovers with revised terms. Enforcement action remains the 'tool of last resort'.

"Banks are more inclined to support problem debts than in the past. This may be a reflection of the difficult market conditions, as banks are keen to protect the value of assets they hold as security and retain and grow their customer base."

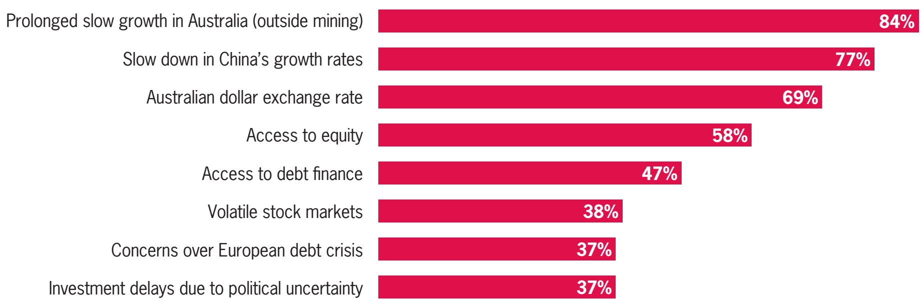
Slow economic conditions are the primary risk to Australian Businesses...

Not surprisingly, 84% of respondents rated the current slow economic conditions as having a significant impact on Australian businesses. The other significant issues were the slow down in China's growth rate and the current relatively high level of the Australian dollar.

Difficulties accessing equity finance was rated as an issue by 58% of respondents, with almost 50% of respondents listing access to debt as an issue for their customers.

Interestingly, most respondents did not consider political uncertainty, the volatile share market or the European debt crisis as having a significant impact on Australian businesses.

% of respondents rating impact as 4 to 6 out of a range of 1 to 6 (6 highest and 0 lowest impact)



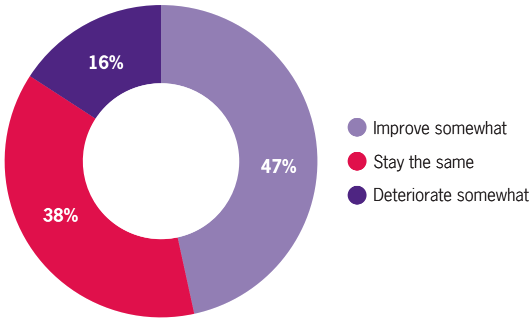
"Despite the recent change in government, the expectations are for the economy to remain fairly flat."

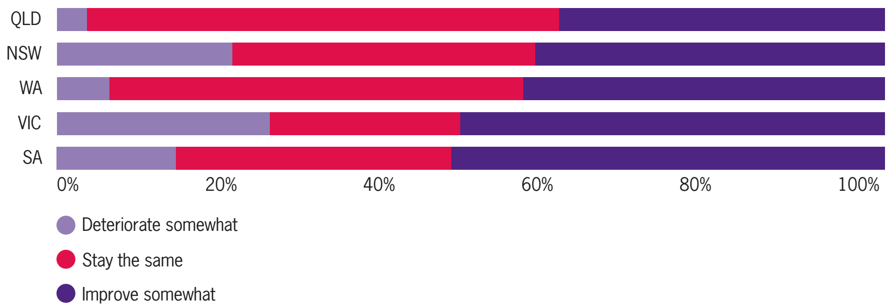
...and no participants expect any significant change in economic conditions in the next 12 months

Most respondents expect economic conditions to remain relatively stagnant or slightly improve over the next 12 months, with no respondents expecting either significant improvement or deterioration.

However, there was some positive news, as more respondents expect economic conditions to improve (47%) than expect to deteriorate (16%).

Looking at the next 12 months, do you expect Australian economic conditions to: Improve somewhat, Stay the same or Deteriorate somewhat?





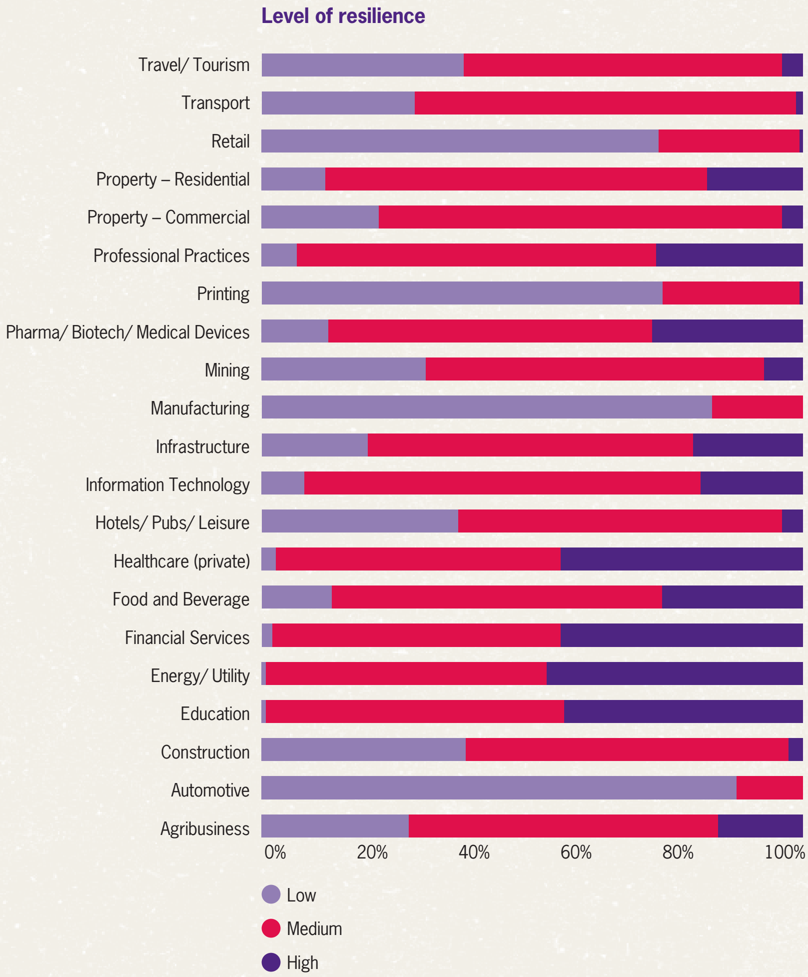
"All the States have similar views on the economic outlook, although respondents were more pessimistic about prospects in NSW and Victoria."

There are no sectors that are generally considered to be highly resilient

The least resilient sector is considered to be automotive, with 88% of respondents considering it to have low resilience. Other sectors that were rated as having low resilience included manufacturing (83%), printing (74%) and retail (73%).

There were no sectors where more than 50% of respondents rated them as having higher resilience. However, the sectors considered to have the most resilience were financial services, energy/utility and private healthcare.

"Most sectors are being affected by the high Australian dollar, low consumer confidence, changing consumer preferences and high labour and energy costs. The sectors most adversely impacted are automotive, manufacturing, printing and retail."

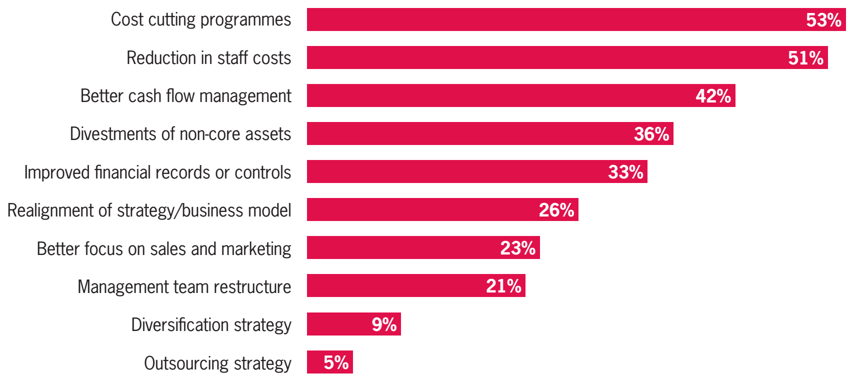


Cost cutting has been the preferred strategy to deal with difficult market conditions

Respondents indicate that businesses have been responding to the difficult market conditions by reducing staff costs and implementing other cost cutting programs. There has also been a focus on cash flow management and divestment of non-core businesses.

Only a small proportion of businesses have been making more wholesale changes, such as realignment of strategy (26%), focusing on sales and marketing (23%) or implementing diversification (9%) or outsourcing strategies (5%).

% of respondent's borrowers implementing the majority or all strategies



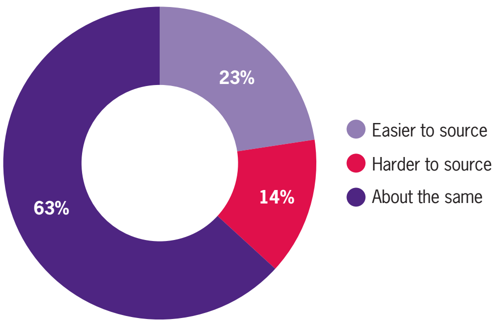
"A lot of businesses have been making some hard decisions, such as making staff redundant or implementing hiring and wage freezes. Fewer businesses have focused on sales and marketing or innovative growth strategies to enhance value."

Lending conditions remain tight

"Lending conditions remain tight and banks are closely scrutinising all deals. Businesses will need a strong business case to raise debt finance to fund proposed mergers and acquisition initiatives, strategic growth opportunities or large capital expenditure programs. The ability to access or continue to access funds will depend on a number of factors including the industry outlook, the borrower's risk profile, the quality of the management team, competitive positioning, financial track record, reliability of financial information and the level and quality of available security".

Access to debt and equity could continue to be an issue for Australian businesses, with the majority (63%) of respondents indicating that availability of debt will not change in the next 12 months. On a positive note, there were more respondents who expected lending conditions to improve (23%) than those who expected lending conditions to deteriorate (14%).

For businesses needing to source new debt or refinance existing debt, compared to the most recent 12 months, do you expect debt finance to be:



"Despite this, one of the biggest issues lenders face is convincing well run, quality businesses to take on additional debt to fund their growth strategies."

Poor management is considered to be the leading contributor to distress

Whilst pressure on revenues was rated by 83% of respondents as a key driver of business underperformance, the highest contributors to business distress were considered to be poor management decisions (91%) and poor financial controls (86%). Poor working capital management was also rated as significant contributor (85%).

An inappropriate business model was also rated as a common cause of distress, indicating that some businesses have been failing to adequately understand and respond to the needs of their customer base.

% of respondents rating impact as 4 to 6 out of a range of 1 to 6 (6 being highest and 0 lowest impact)

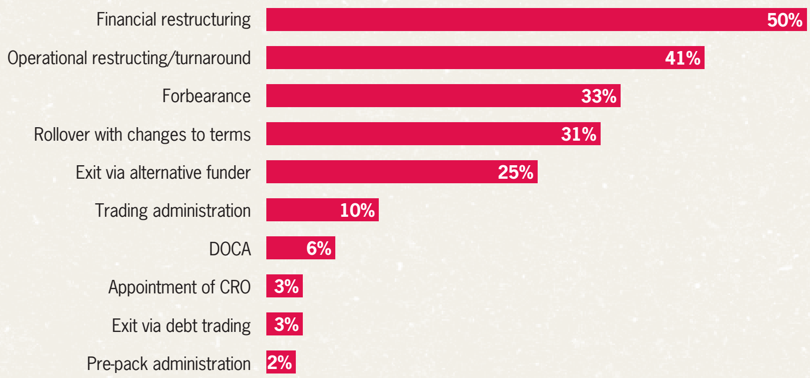
"The survey results support our long held view that poor management is the leading cause of business failure. This highlights the importance of having a strong management team, supported by sound financial systems and processes that enable business decisions to be made based on reliable financial information and analysis. The role of quality external advisers will be critical in assisting businesses through these lean times."

Financial and operational restructures have been used to deal with underperforming loans

There is clearly a preference by the banks to work with clients, as financial and operational restructurings, forbearance and rollovers have been applied more regularly than enforcement action. 50% of respondents indicated that financial restructures had been used in the majority or all of underperforming loans that they had dealt with. 41% of respondents also indicated that operational restructuring had been used in the majority or all cases. Forbearance (33%) and rollovers with revised terms (31%) were also common.

Trading administrations, 'pre-pack' style administrations and Deeds of Company Arrangements (DOCA) were only used in a minority of cases.

% of respondent's borrowers implementing the majority or all strategies



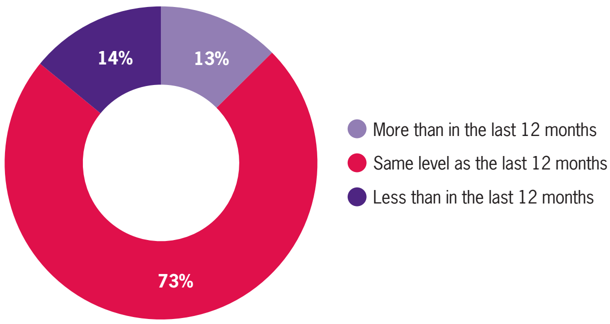
"Australia's relatively inflexible formal restructuring regime makes it difficult to protect business value through a restructure. Banks are more open to considering proposals for informal restructures."

Forbearance is expected to continue to be a strategy utilised by banks over the next 12 months

There is a fair degree of pragmatism at work as banks see little alternative to continuing to support customers.

Forbearance strategies by banks are expected to be used at similar levels to the last 12 months. This is consistent with expectations of stable economic conditions.

In the next 12 months, do you expect bank forbearance strategies to be used?

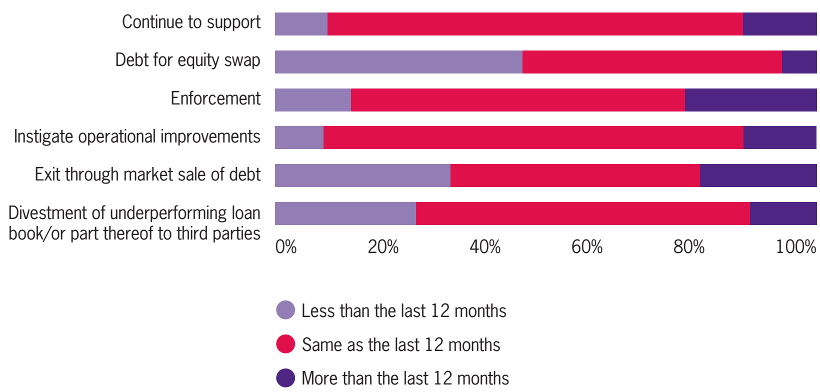


"The banks are indicating an ongoing willingness to support businesses in resolving their operational and funding issues. This is good news, as the mass sale of assets on market, could place pressure on asset values and further exacerbate the difficult market conditions."

The banks do not plan to materially change strategies

Respondents indicate that debt and equity swaps, and exits through sale of debt, are likely to be used less. There is also expected to be a lower level of divestment of underperforming loan books.

If you look after underperforming loans, which strategies will you employ in the next 12 months?

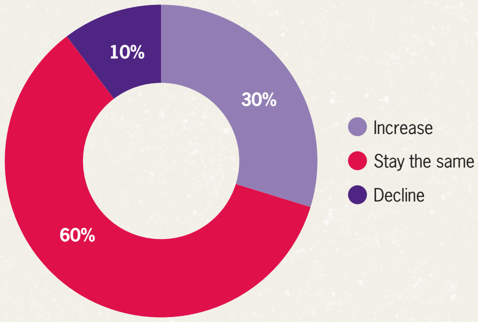


"Banks are likely to continue to support most underperforming businesses. Enforcement action remains a strategy of last resort."

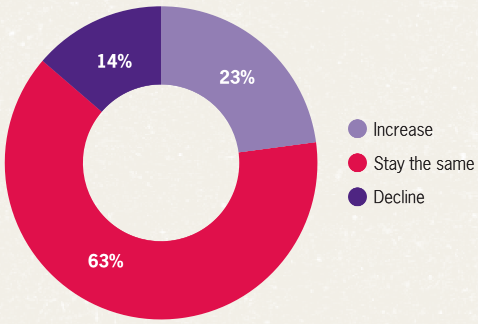
30% of respondents expect default levels to increase... and 23% expect an increase in corporate failures

Whilst economic conditions are expected to remain relatively flat, there is a concern by many that loan default levels and corporate failures could increase.

Looking at the next 12 months, how do you expect debt default levels to develop?



Looking at the next 12 months, do you expect the number of corporate failures to:



> "Banks are less inclined to initiate formal insolvency – opting instead to work with company initiated appointments rather than exposing themselves to the financial and reputational risk of receivership."

Basel III is likely to increase the cost of capital

Basel III will increase the regulatory capital that banks are required to hold. Its objective is to improve bank liquidity and decrease bank leverage, in order to promote a more resilient global banking system in the wake of the Global Financial Crisis.

The majority (77%) of respondents believe that Basel III will increase the cost of capital, as banks are likely to pass on their additional funding and compliance costs to customers in the form of higher interest rates.

40% of respondents indicate that Basel III is likely to squeeze out weaker financiers and 38% believe that it will reduce the risk of a banking crisis.

What impact do you think Basel III will have on banks in Australia?

"Higher risk borrowers are likely to find it harder to access debt funds, with any funds that are able to be raised being more expensive."

Will your business be able to access the funding that it needs?

Funding conditions are likely to remain tight over the next 12 months, at least. Is your business at risk of not being able to access (or retain access to) the funds that it needs to pursue its strategies?

Take our traffic light assessment

		Red light YES	Orange light UNSURE	Green light NO
01	Has the performance of your business been declining?	○	○	○
02	Do you have difficulty producing accurate and timely financial information on which to make decisions?	○	○	○
03	Could your working capital management be improved?	○	○	○
04	Are you concerned about being able to access the funds you need to achieve your strategic objectives?	○	○	○
05	Are you uncomfortable with your level of gearing and/or the assets that you have provided as security?	○	○	○
06	Are the pricing and covenant terms on your loans unreasonable having regard to the credit risks of your business?	○	○	○
07	Is your debt due to be rolled over in the next 12 months?	○	○	○
08	Are you likely to need additional debt?	○	○	○
09	Are there issues in your business that the bank is not aware of?	○	○	○
10	Are you at risk of breaching or have you breached a bank covenant?	○	○	○

If you answered yes or unsure to any of the above, please call one of our Grant Thornton Partners to discuss.

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We are a member of Grant Thornton International which comprises firms operating in more than 100 countries worldwide. Through this membership, we access global resources and methodologies that enable us to deliver consistently high quality outcomes for owners and key executives in our clients.

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