

## Managing the credit crunch

***As the financial situation globally continues to worsen, the importance of sound credit management has risen exponentially and has become a crucial cog in the wheel of business.***

***Gerald Fenech interviews Josef Busuttil, director general of the Malta Association of Credit Management and gets his take on the credit crunch and what remedial measures a business can take to minimise the impact through sound and proactive credit management.***

### **What is your opinion of the current credit crunch and what brought this about?**

*'Credit Management is all about being proactive'*. This is a cliché that I use quite frequently and it also applies to the current credit crunch situation. Should the US banks been proactive in their credit management, today's world economy would have been much different!

However, pointing our fingers at the culprits that have started this world financial crisis is now worthless. This should be the job of the historians to write history and the job of the shareholders to investigate their respective directors who have been paid billions of dollars for their salaries.

We all know what has happened in the United States and what were the consequences on the world economy, as we have read loads of articles and news about the matter. In my humble opinion, the only reason that we should now look back is simply to analyse and learn from what has happened in order not to repeat the same mistakes in the future.

Credit carries an element of risk and costs money. It does not come for free. Lenders or creditors have to finance their credit and they have to make sure that their customers are both trust worthy as well as credit worthy before they grant them credit. Granting credit can be defined as investing money in trusted customers. Lenders and suppliers should not be greedy and they should never grant credit for the sole purpose of increasing their turnover because that would lead to irresponsible lending.

Customers should be analysed for their credit worthiness and their ability to pay on time. Creditors should also know the real worth of their customers prior to granting them credit. A customer can have impressive amount of assets but his/her real worth is zero because all the assets are freezed! It would be to no benefit, both to the creditor and the customer alike, to grant more credit to highly geared customers, as the latter would not be able to honour their financial commitments anyway.

This is some good credit management practice and if the people involved in lending the huge amount of money in the US were competent credit managers, we would have never been in such a financial crisis. This is one of the lessons that banks should learn from this credit crunch: they should employ or train their people to be able to manage credit in a profitable manner and these credit professionals must be involved in the whole credit management process. The business community should likewise learn from these banks' mistakes. Trade creditors should also have an effective and efficient credit policy in place and employ qualified people to manage credit in line

with their credit policy. Creditors should always keep in mind that **Liquidity** is the lifeblood of business and commerce.

It is no news to say that the current credit crunch has negatively effected the demand in the world economy. Liquidity is at its lowest, unemployment figures are increasing, bankruptcies around the globe are the order of the day. Governments and central banks are trying to help in this financial crisis by taking fiscal and monetary measures in order to improve liquidity and increase demand. Governments are using people's money to help large private corporations to recoup their liquidity problems.

- *But to what extent can these measures be employed and sustained?*
- *What will be the economic and financial effect of these measures in the long-term?*
- *What are the long-term consequences of nationalizing large organisations?*
- *Do these fiscal measures apply equally to all countries?*
- *What will be the effect of these fiscal measures on a government's budget?*
- *If the well-being of an economy depends on the government spending, to what extent can the government decrease its revenue?*

These are the kind of questions that the authorities should be asking before taking corrective actions. It is true that measures are needed to combat the current crisis but the long-term effect of these measures should be given its due consideration.

### **How do you believe Malta will fare in the current economic scenario?**

We do have a strong and healthy banking environment in Malta, which is well regulated and the local banks are managed competently. The Maltese banks' credit policies are far different from those of the US and European banks. However, we are not living in a vacuum. We depend on export, and this includes tourism. What happens in a country on the opposite side of the globe, may have an effect on us. We are not only an EU state but also part of the globalised world!

If demand shrinks in another country, it may have a negative effect on our exports. If the unemployment figures increase, less people may be willing to travel, which would have a negative effect on our tourism. If the European Central Bank lowers again the interest rate, it may have an effect on the domestic inflation. If the EU suggests lower VAT rate, it may effect our government's revenue and thus the government's spending power in our economy or it will have an impact on the government's debts. Therefore, I believe that Malta will also experience the pinch to some extent. In fact, some exporting companies in Malta have already taken action following decrease in their orders.

### **What is the MACM doing to protect its members from the credit crunch?**

Being the national organisation providing the necessary promotion and protection of all credit interests pertaining to the local business, during the past months MACM has invested heavily in research and development in order to improve further its services provided to its members.

MACM is in the process of developing valuable tools and providing pertinent information relating to the managing of credit. New databases and effective tools to measure credit management performance will soon be available to all MACM Members through its website:

[www.macm.org.mt](http://www.macm.org.mt)

In view of the financial crisis, MACM has invited all its members to give their feedback in order to understand better their needs and expectations. All databases and tools, which will be available exclusively to the MACM members are in fact being developed on the Members' suggestions and recommendations. Other services, which will be innovative for the Maltese creditors are also being developed following thorough research and long discussions with our foreign counterparts and professional bodies in the field of credit management. The revamped website will be launched early January 2009.

Another responsibility of MACM is to inform and educate its members and the Maltese creditors at large. With the permission of the Institute of Credit Management of the UK, every week, MACM is presently sending informative booklets to the local creditors, which are serving them as guidelines to grant and manage credit proactively and profitably given the current financial and economic turmoil. These guidelines address a number of topical credit management issues, including *Know your Customer; Invoicing; Payment Terms; When Cash Runs Short, Chasing Payments; When Customer Goes Bust; Factoring and Financing; and Credit Insurance*. These guidelines can be obtained upon request by e-mail on [info@macm.org.mt](mailto:info@macm.org.mt) or by telephone on 21423638 / 9.

As has been done during this year, MACM has its annual programme of events for the year 2009, consisting of conferences, seminars and workshops, most of them focusing on the current credit crunch in order to discuss what can be done to protect cash flow and to employ good credit management practices. Foreign speakers, specializing in this field will also be invited.

These activities can only be possible because MACM is a not-for-profit organisation, managed by its own members, which does not have any commercial objectives. Its main objective is solely to satisfy the needs and expectations of its members, especially during these tough times, in order to protect their cash flow and profitability to the benefit of the Maltese companies, the local employment and our economy.

### **Do you believe that Malta is insulated from the credit crisis?**

Definitely not the case. We would be committing a big mistake if we think that we can continue doing business without being effected by the international credit crisis.

If credit is rationed in the US and Europe, for example, the local financial institutions and the Maltese trade suppliers will find it difficult to obtain credit from their foreign principals. Consequentially, both the local financial institutions and the local businesses will make it difficult and will be more stringent in extending loans and credit to the local customers. It is a dominoes effect. The end result could mean that credit would be difficult to obtain and would cost more to the business community.

Additionally, economic and financial factors effecting other countries, especially EU countries, would also effect our economy and commerce. Some local exporting companies have taken employment measures due to a decline in their orders. The Smart City project may also be effected by the international economic slowdown if the International IT companies suffer decrease in demand for their services. As already explained, the tourism industry may be negatively effected if less people are willing to travel during the coming year. And other local industries, such as the construction and fmcg, could also suffer due to low demand in the domestic market.

These factors would all effect to some extent our economy and local businesses may opt to lower their prices and give discounts to encourage demand from customers. Here again, local companies may well suffer from lower margins.

May I take this opportunity to encourage our politicians from both political sides to give this current credit crunch situation its due priority and share their resources in order to protect our economy and to introduce proper measures that will do no harm to our economy in the longer term, whilst give incentives that will drive the short-term demand.

### **How does the MACM work with foreign affiliates in the field?**

MACM is an active member of FECMA - Federation of European Credit Management Associations. Together with its European counterparts, MACM works on a number of fronts in the field of European credit management. One of the most critical matters is surely education. MACM is the accredited Training Centre of the Institute of Credit Management of the UK. Courses leading to Diploma in Credit Management – Level 5 run every year at MACM Training Centre in Mosta. Maltese students read these education programmes and are obtaining remarkable results. The MACM Training Centre has been awarded Certificate of Excellence from the ICM (UK) twice since 2005 and three local students were awarded Prizes for their outstanding results.

FECMA publishes its newsletter, which is aimed for the European creditors. Proficient European credit professionals contribute with articles pertaining to credit management and is distributed to all FECMA Associations' Members, including MACM Members. MACM contributes regularly with intuitive articles.

Currently, FECMA is in the process of organising a Pan-European Conference. It will be held in Maastricht in May 2009. MACM is actively involved in the organisation of this event.

Besides, MACM has just signed an agreement with Graydon International, a London based Credit Rating Agency owned by three of the world's leading credit insurance organisations: Atradius, Coface, and Euler Hermes.

MACM is the official Maltese distributor of Graydon International Credit Reports. Graydon's network spans the globe, with deep roots in Europe where they are a major player. Graydon International's database provides millions of online credit reports in over 130 countries. However, fresh credit investigations are available for any country in the world. Maltese businesses can now obtain credit reports on international companies in an effective and efficient manner. This should obviously help local exporting companies and banks in analysing the trust and credit worthiness of their customers in a proactive manner.

### **What do you believe are the main challenges for the credit industry?**

The main challenges for the credit industry are fourfold:

**a. Understanding the needs of the customers** – Creditors should spend more time listening to the needs of their customers in order to meet their expectations. Thus, building long-term business relationship and customer loyalty, which are critical to maintain competitive advantage in the market. This would make more sense during tough economic times.

**b. Credit Application Form** – Creditors should never assume that the customer knows what the credit terms are. A credit application form should be completed and signed by both parties before credit is extended. The credit application form should include all pertinent information about the customer, as well as the terms and conditions agreed between the parties relating to the sale and payment. If a customer refuses to sign the agreed terms, the creditor should evaluate further the credit risk of the prospective debtor.

**c. Prompt and accurate invoicing** – Issuing inaccurate and unclear invoices is the recipe for late payment. No customer will pay a disputed invoice or if the goods and services are not clearly specified. Additionally, suppliers should invoice the customer promptly. No customer will pay if the invoice is not received.

**d. A sale is only a gift until it is paid for in full** – suppliers should not be afraid to ask for payment. One may have the perception that collecting cash may be offensive and may damage the business relationship with the customer. But how can it be offensive, if one is asking for what is rightfully and legally his? How can it damage the business relationship, if the customer knows that the account is overdue? If anything, the awkwardness of late payment, is with the debtor and surely not with the seller!

### **How can companies improve their profitability?**

The private sector is critical in such a credit crunch situation. As the central banks are reducing their interest rates to encourage more spending and the governments are encouraged to take fiscal measures to improve liquidity in the market, so can the private companies use their marketing tools to increase sales in a profitable manner.

Credit is one of the most effective marketing tools. Credit oils the wheel to keep it turning. It can be used to differentiate the product or the service in the market. However, credit does not come for free. It costs money and carries an element of risk. Therefore, to exploit credit in a profitable manner, companies have to strike a balance between the use of credit as a marketing tool and the credit cost and risks. This balance can only be struck by means of creative strategic planning.

For profitability purposes, credit should be considered as a long-term investment in the customer. If it is wisely used, it can build strong customer relationship and sustain loyalty which is much needed in today's competitive commerce, where demand is shrinking.

More cooperation and synergy between the sales and the credit departments is inevitable, especially in today's economic turmoil where credit is becoming rationed and it is costing more money. The sales team is one of the best sources of information to the credit team as the sales people are out in the market and know the customers well.

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**The Malta Association of Credit Management (MACM)** is a not-for-profit organisation, providing a central national organisation for the promotion and protection of all credit interest pertaining to Maltese businesses.

MACM represents the credit profession across all economic sectors. It is a centre of expertise for all matters relating to credit management in Malta. MACM offers a range of services to the local creditors, including, credit management information systems, credit management education, training, conferences, seminars, and lobbying activities. It is the ICM (UK) accredited Training Centre for Malta. MACM is a member of the Federation of European Credit Management Associations – FECMA.

**MACM is the distributor of Graydon International Credit Reports in Malta.**

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