Payment behavior: wide disparities

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Ludovic Subran, Chief Economist
Arnaud Roger, Director of Claims
Maxime Lemerle, Manager, Macroeconomic and Insolvency Forecasts
Yann Lacroix, Manager, Sector Trend Research
Virginie Reboul, Economist

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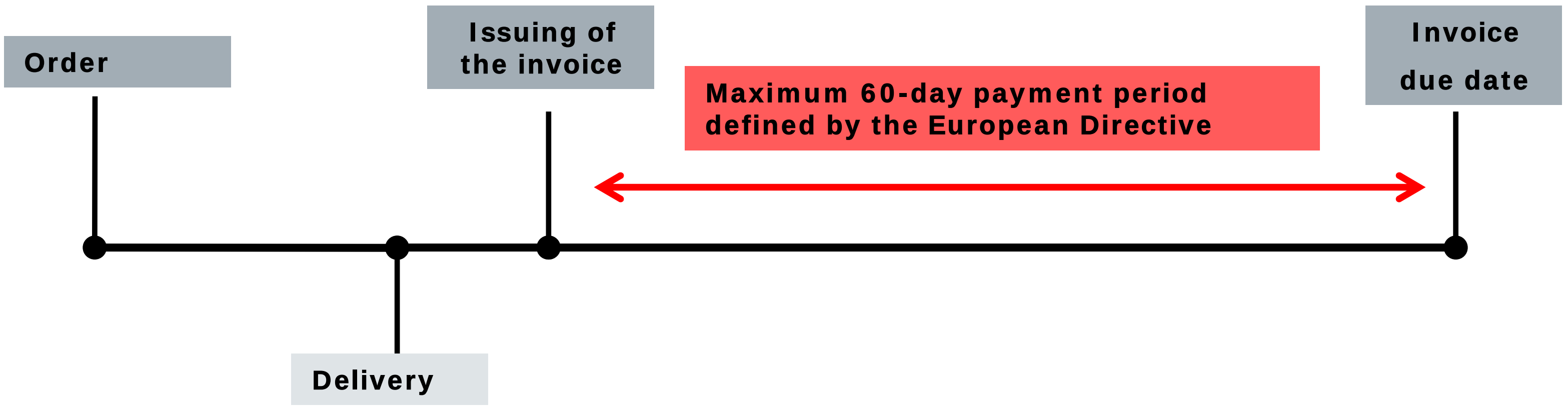
The importance of payment periods

A micro-economic issue...



... and a business climate indicator

An aggregate calculated for a country or sector: $\frac{\text{trade receivables}}{\text{sales excl. tax}} \times 360$

- gauge of fluid exchanges between a country's businesses
- measure of cash flow management vitality
- impact on business climate attractiveness

Reducing payment periods: the legal framework and the goal

Countries are cooperating to resolve payment delay problem

European Union: European Directive of 16 February 2012. The Member States must implement the directive no later than 16 March 2013: maximum period of **60 days**; late payment penalties.

France
LME - Loi de Modernisation de L'Economie (Modernisation of the Economy Act) 2009: maximum payment period = **60 days**.

35 exceptions for cyclical sectors:
- construction
- toys
- jewellery

New government proposal: reduce periods to **30 days for VSEs and SMEs**

Spain
Law of July 2010 - gradual application: maximum **60-day** period by 1 January 2013

Methodology

Objective: reconcile the main research and surveys; provide a detailed prospective analysis per sector/country

Analysis 1 – multi-country approach

Analysis of European countries using an institutional database and forecasts in days sales outstanding (DSO) trends, based on Euler Hermes data

7 countries: Belgium, France, Germany, Italy, Poland, Portugal, Spain

Period: 2000-2010

Forecasts: 2012-2013

Analysis 2 – by sector

Detailed sector-based analysis of DSO and days payable outstanding (DPO), based on Euler Hermes data

9 countries: Belgium, Denmark, France, Germany, Italy, Norway, Spain, Sweden, United-Kingdom

8 sectors: aerospace, air transport, automotive, chemicals, construction, forging, IT services, pharmaceuticals

Period: 2006-2010

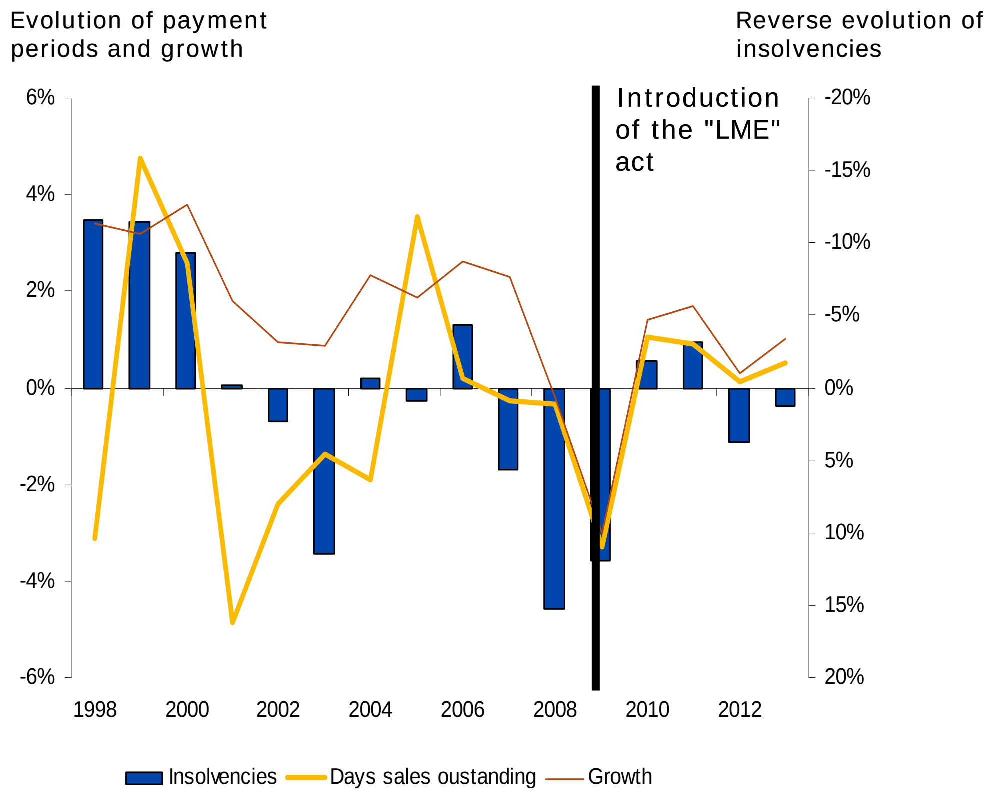
Three top line facts

• **Economic recovery** does not necessarily infer a drop in payment periods:
+0.1% growth for a variation between -1.3% and +0.5% in payment periods

• Longer payment periods compound company **insolvencies** more than proportionately

• A favorable **legal framework** renews business climate attractiveness

France's legal framework: the "LME" effect



Source: Euler Hermes

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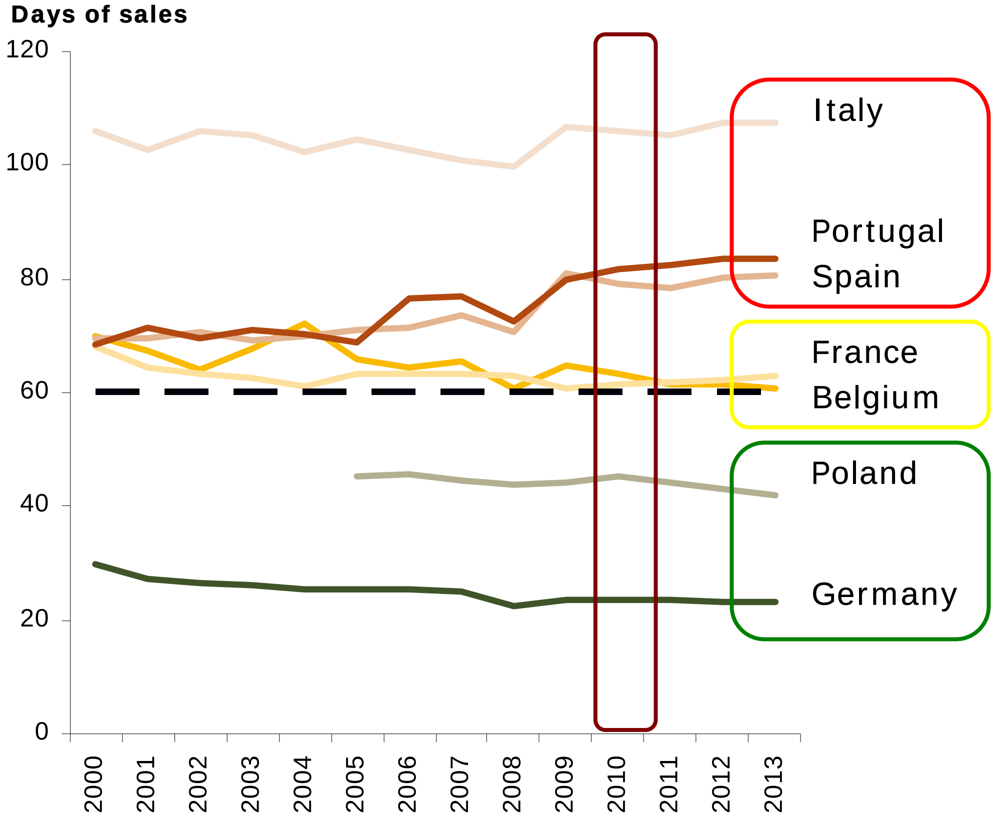
Three European areas emerge

The "easing up" observed from 2009 onwards confirms the existence of three payment period dynamics



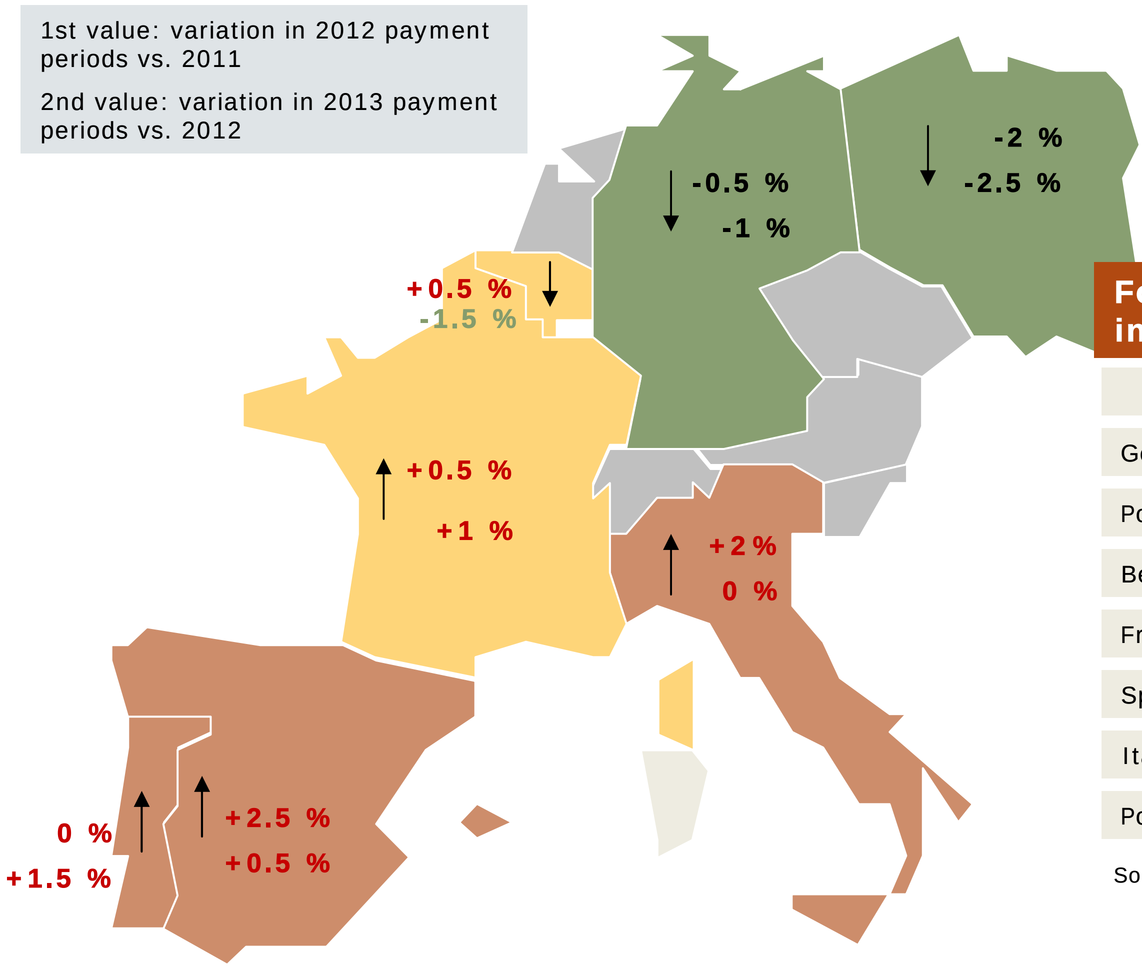
Sources: Base Bach, Euler Hermes

1- Germany and Poland: already on target for EU directive. In Germany, customer payment periods dropped 21% between 2000 and 2010, reaching an average 24 days' revenue in 2010

2- France and Belgium: halfway there. A 10% reduction in French customer payment periods has been observed since 2000, reaching 61 days' revenue in 2010

3- Spain, Italy and Portugal: lagging behind. Payment periods in Spain increased 14% between 2000 2010, reaching the record high of 79 days' revenue in 2010

Payment periods are forecast to lengthen…



Source: Euler Hermes

… due to downgraded economic environment

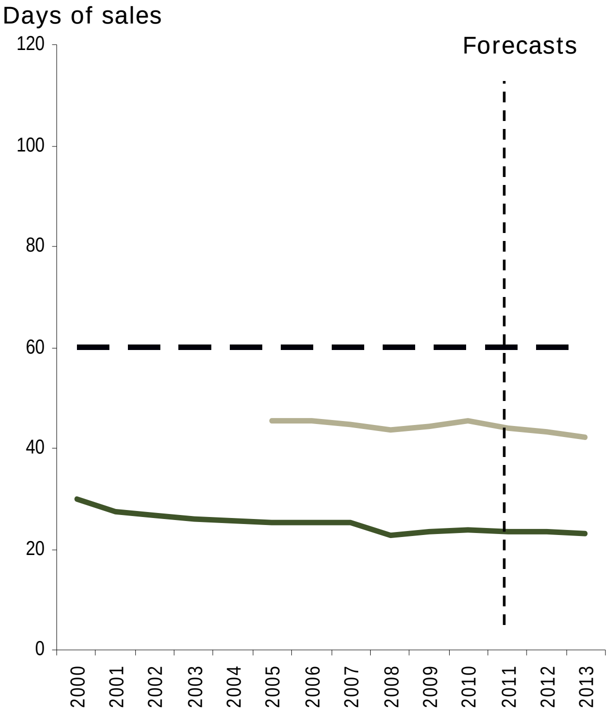
Forecast trend in growth and insolvencies for 2012

Country	Growth	Insolvency
Germany	+1%	-1%
Poland	+3%	+11%
Belgium	+0.2%	+10%
France	+0.3%	+4%
Spain	-1.8%	+20%
Italy	-1.8%	+24%
Portugal	-3%	+29%

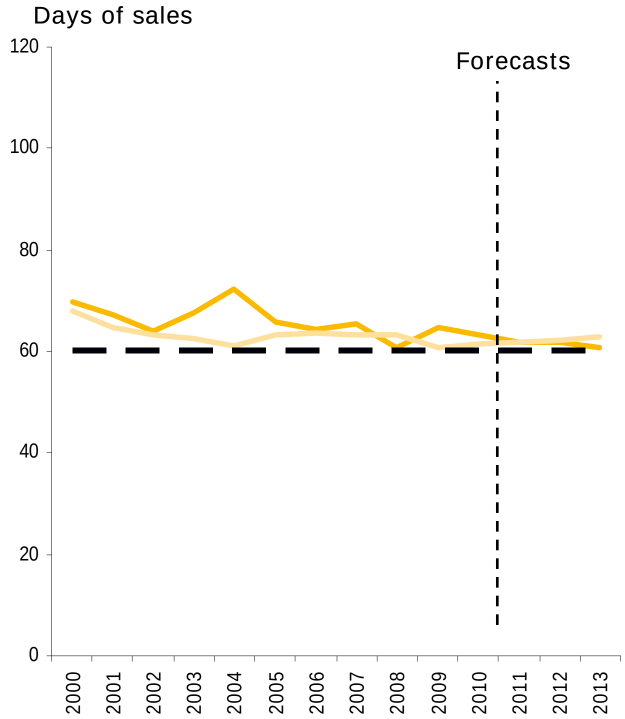
Source: Euler Hermes

A major effort is required – too fast, inopportune timing?

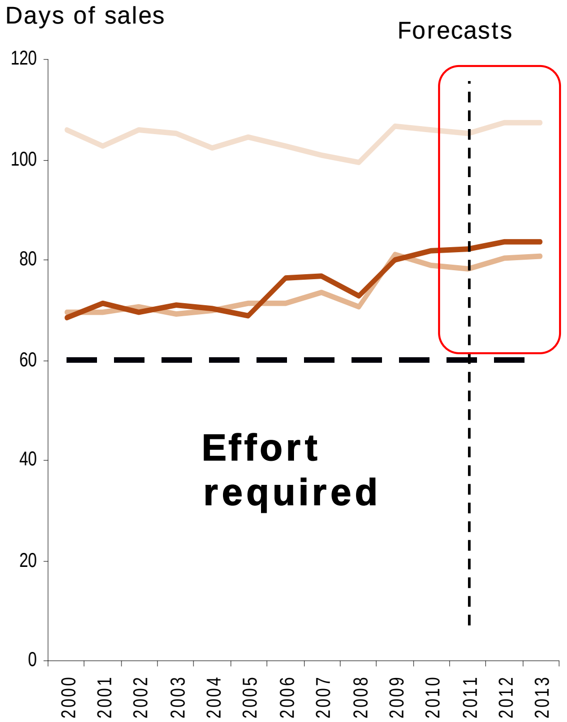
Trend in customer payment periods



Sources: Base Bach, Euler Hermes



Sources: Base Bach, Euler Hermes



Sources: Base Bach, Euler Hermes

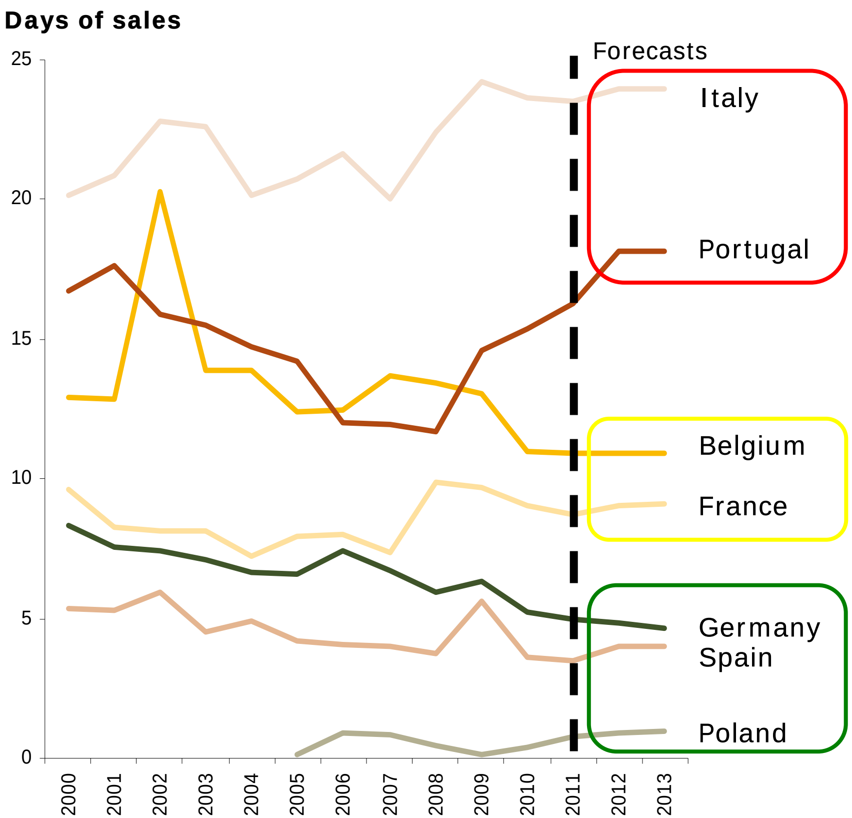
Poland, Germany: Limited variation in drop expected, contribution from the economic environment almost non-existent

Positive inertia in France (LME effect). Belgium – economic stops and starts have greater impact

Hard hit by the crisis, Southern European countries will find it difficult to reach EU targets

Cash flows face renewed pressure

The stress indicator* reveals finance requirements



*Stress indicator = DSO - DPO

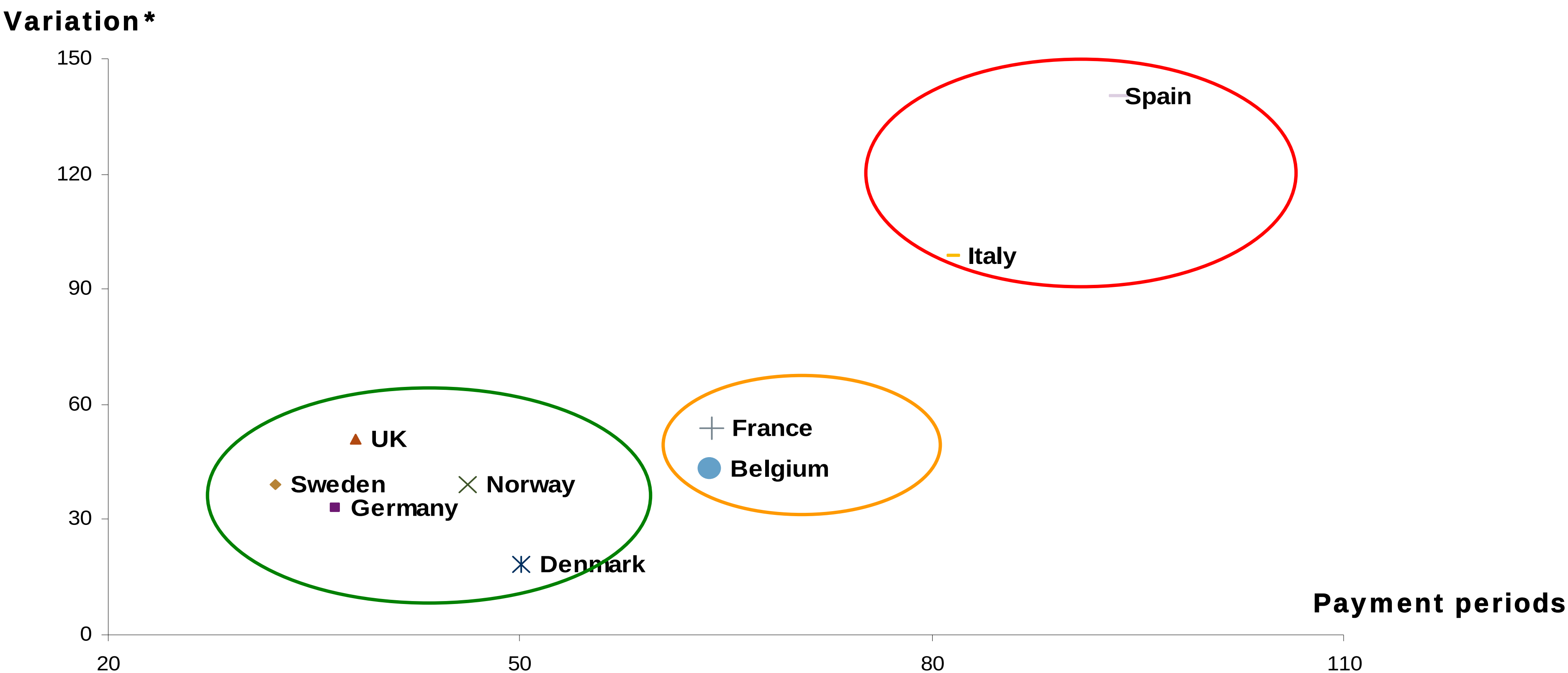
Sources: Base Bach, Euler Hermes

Spain: the exception

1. Germany (5 days of sales) and Poland (1 day of sales) share a low pressure indicator. Convergence by Germany
2. No scissor effect for Spain despite long payment periods
3. Acceptable cash flow requirements for France and Belgium
4. Italy and Portugal suffer from the effects of customer payment periods: high pressure indicators

The average payment period conceals major differences among the sectors

Sector variations are 4 to 5 times higher in the South than the North



* Difference between the sector with the longest payment periods and the sector with the shortest payment periods.
Sectors studied: aerospace, air transport, automotive, chemicals, construction, forging, IT services, pharmaceuticals
Source: Euler Hermes

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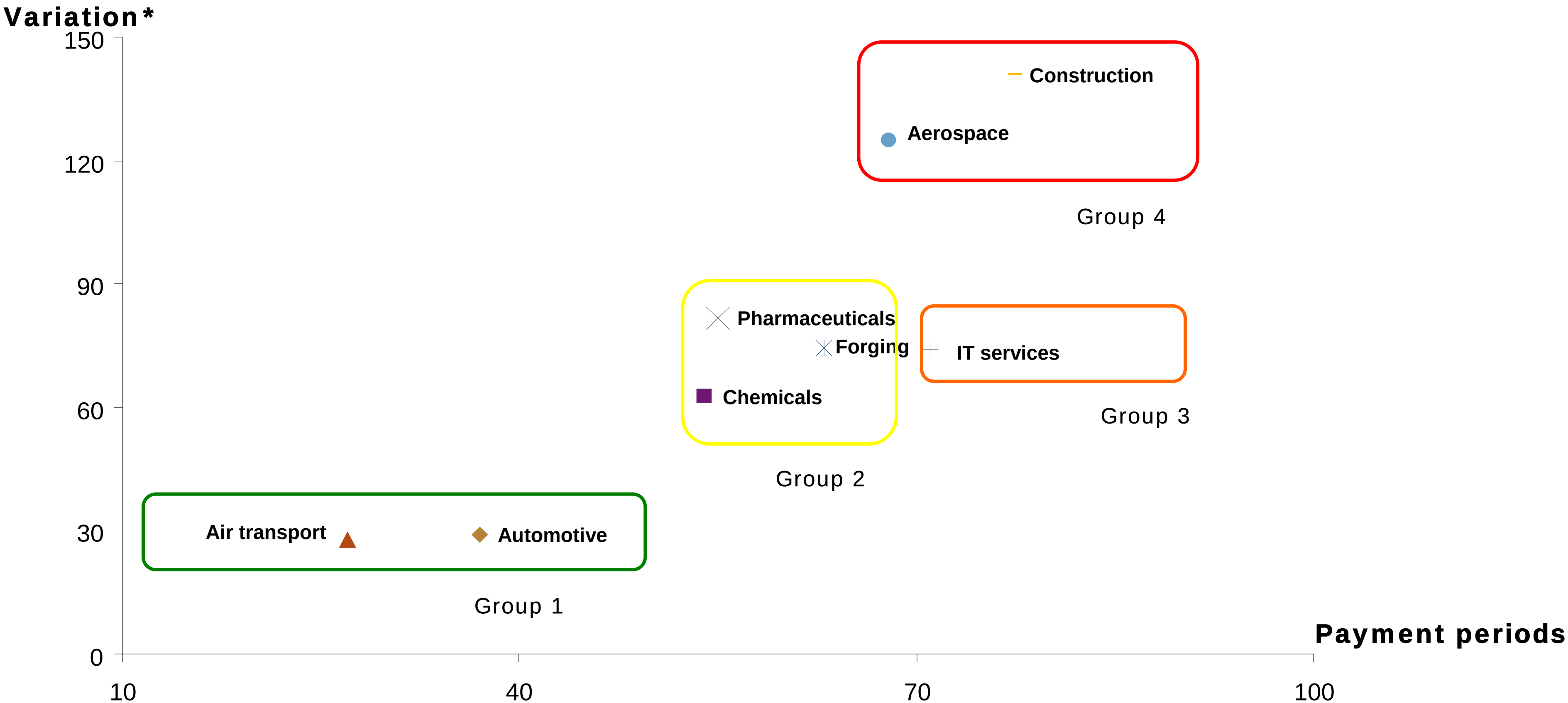
European business sectors: four groups

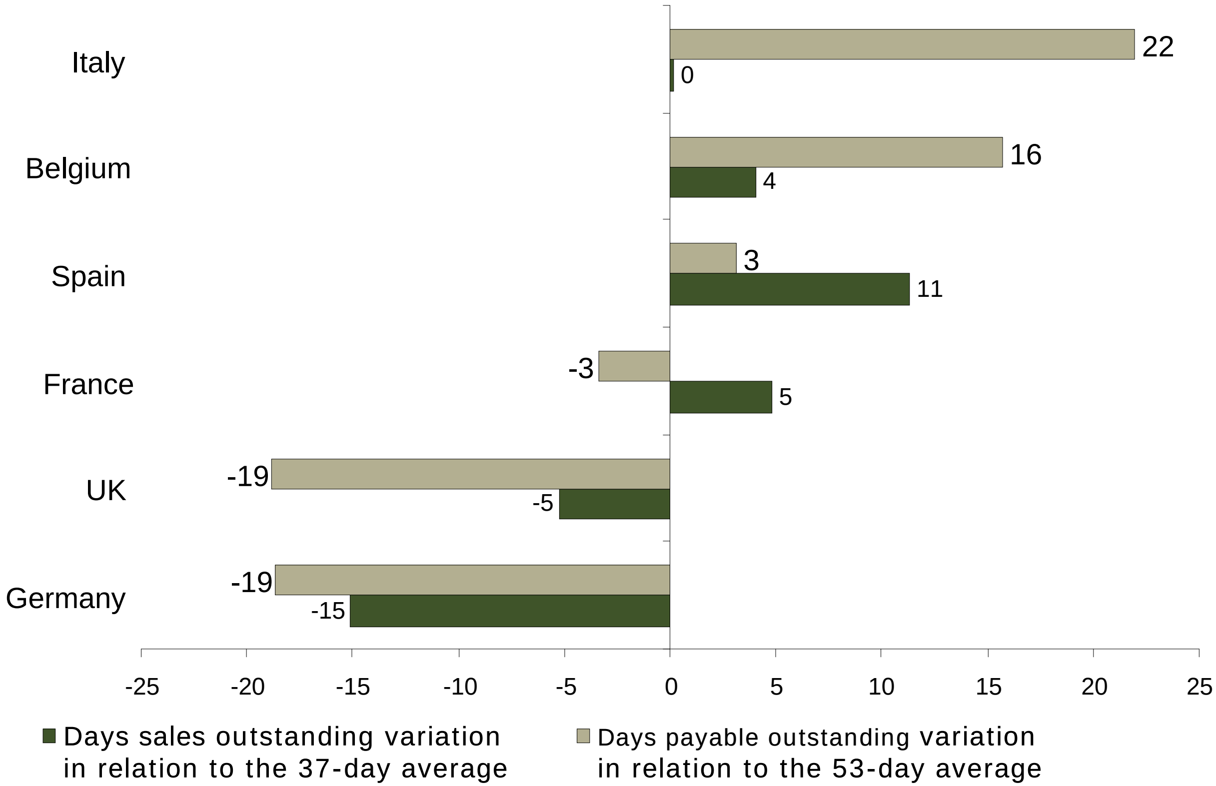
Noticable effects of the internationalization of some sectors



* Difference between the country with the sector's longest payment periods and the country with the sector's shortest payment periods.
Countries studied: Belgium, Denmark, France, Germany, Italy, Norway, Sweden, United Kingdom
Source: Euler Hermes

Group 1 - Automotive: tolerable spreads

Southern European countries, Belgium: dependent on supplier credit to maintain positive cash position

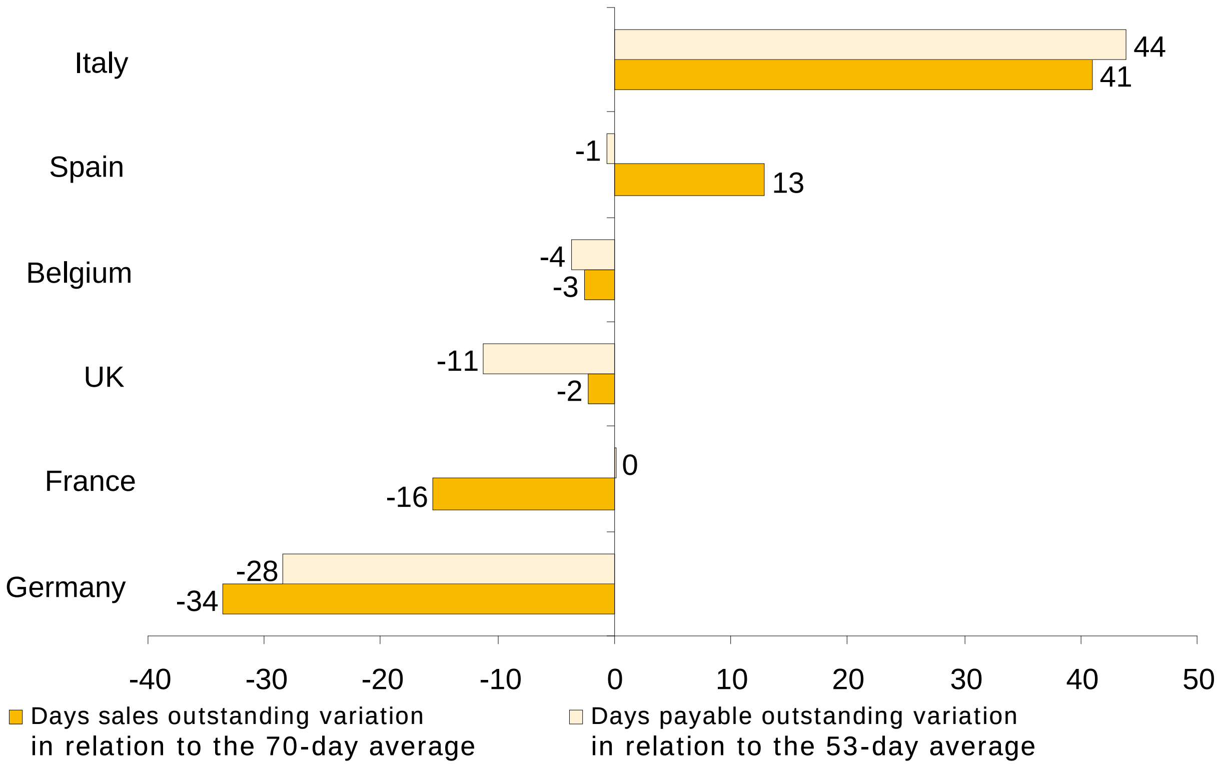


- **Italy:** supplier payment periods reach 75 days, 2.2 times higher than Germany (34 days)
- **Spain:** customer payment periods of 48 days, 2.2 times longer than Germany. The goal is to sustain the distribution network

Source: Euler Hermes database of balance sheets

Group 2a – Forging: SMEs vs. major companies

Considerable differences in payment behavior: periods 4 times longer in Italy than in Germany



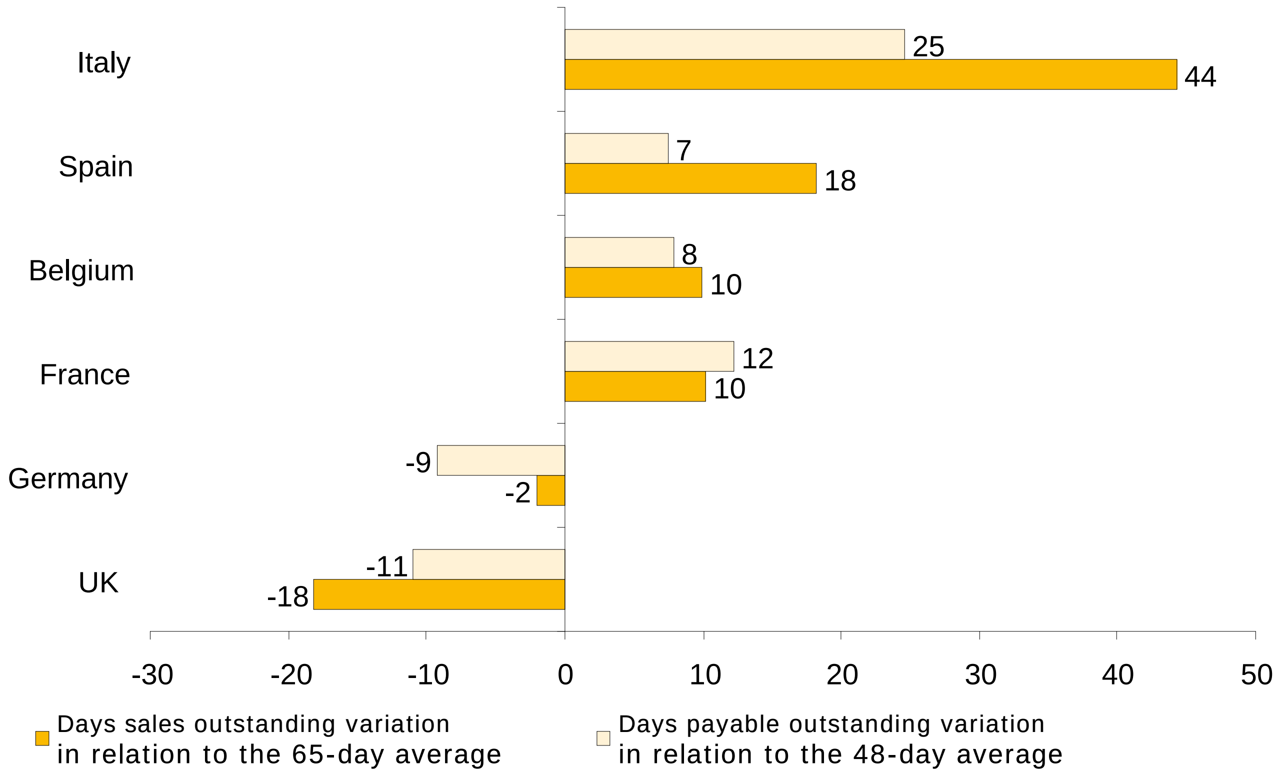
- The weight of trade receivables leads to **structural cash flow requirements**

- The organisation of **France's automotive industry** via round tables has allowed French subcontractors to even out customer and supplier payment periods

Source: Euler Hermes database of balance sheets

Group 2b – Chemicals: the fabric of the industry sustained by customer credit

Suppliers mainly of the world's leading oil and gas groups, hence the relatively low variations in supplier payment periods



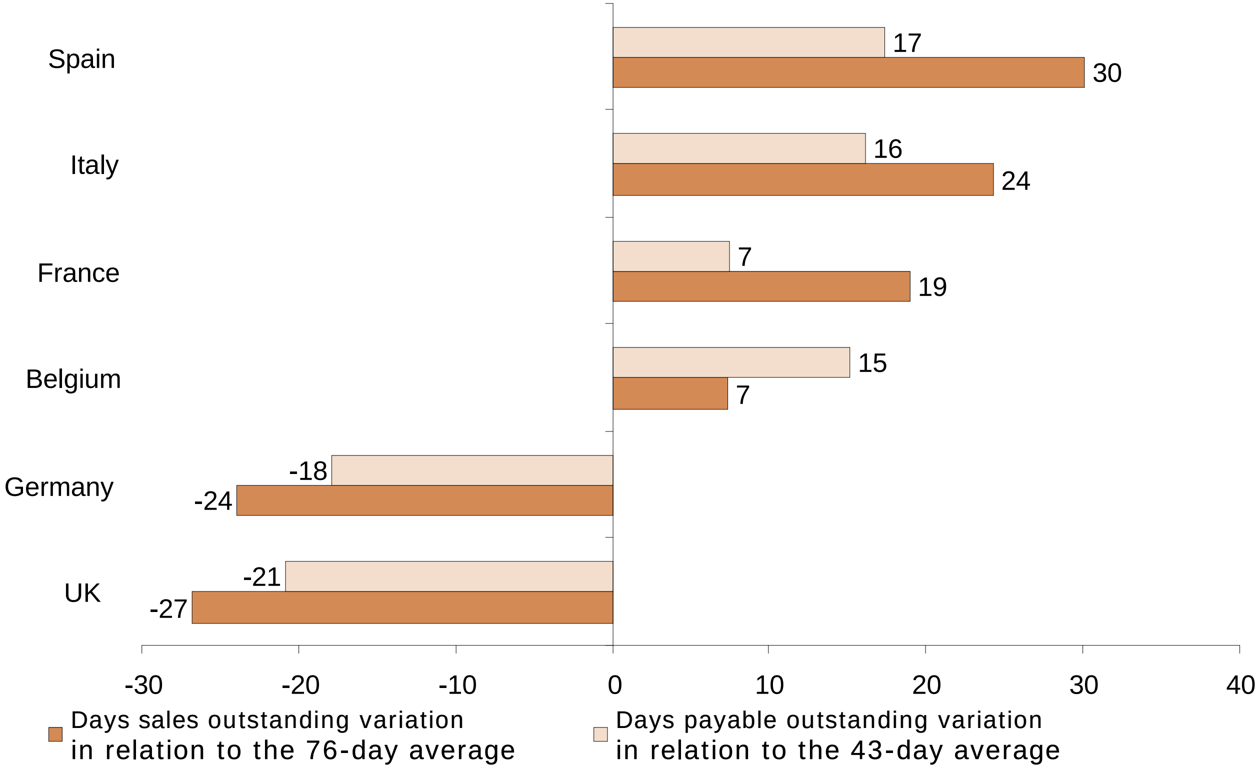
- The extent of customer payment period variations in **Italy** illustrates the fragility of its industry

- Customer payment periods are 3 times longer in Italy than in the UK

Source: Euler Hermes database of balance sheets

Group 3 - IT services: customer pressure

Bargaining power in IT services favors major customers, creates substantial cash flow requirements that weaken the sector's players



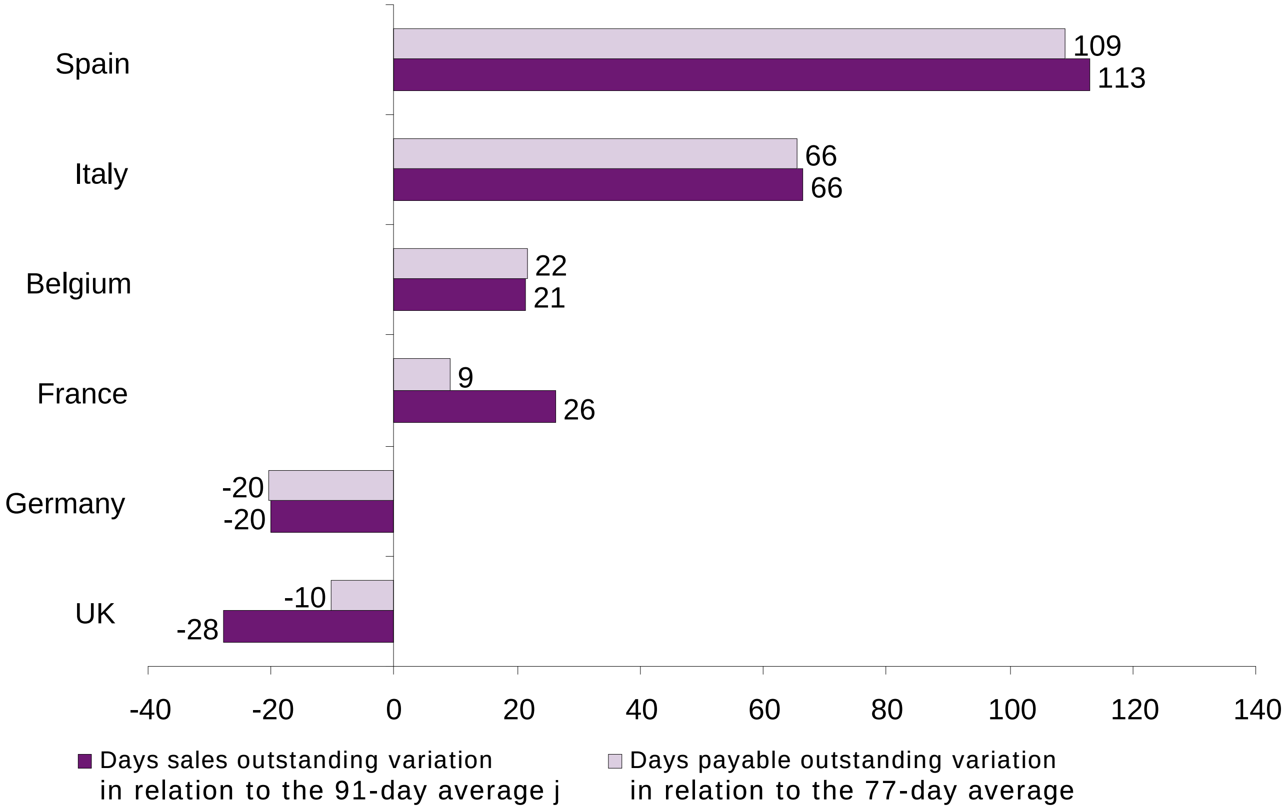
- **Spain, Italy, France:** cash flow requirements exceed 40 days

- **Spain:** customer payment periods are 2.2 times longer than in the UK; supplier payment periods 2.7 times longer

Source: Euler Hermes database of balance sheets

Group 4 – Construction: the sector with the greatest differences

Payment periods largely reflect national economic situations

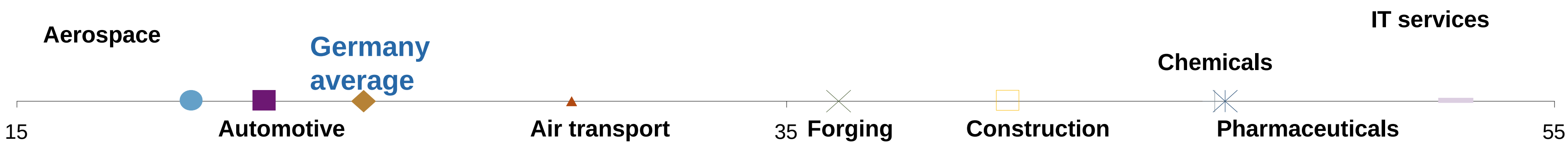


- The construction sector is essentially local, like its customers and suppliers, hence the **abnormally long payment periods**

- In **Spain**, the supplier payment period (157 days) is 5.6 times longer than that of Germany (28 days), the customer payment period is 5.2 times longer than that of the UK

Source: Euler Hermes database of balance sheets

Germany: tops and flops



Source: Euler Hermes

Customer payment periods in days' revenue

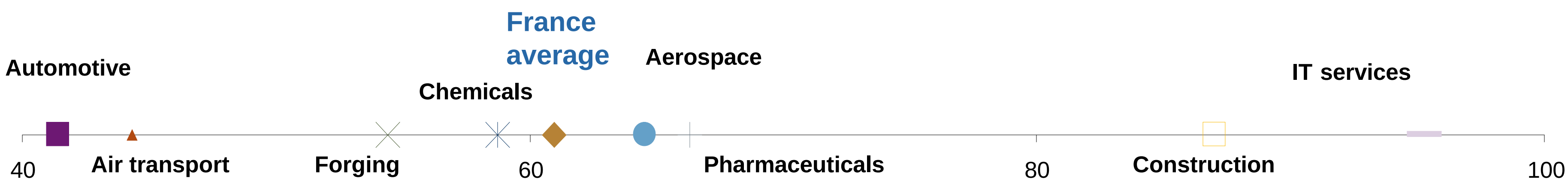
Days sales outstanding and days payables outstanding (2010)

Germany	DSO	DPO
Aerospace	20	51
Automotive	21	34
Air transport	29	31
Forging	36	24
Construction	41	28
Pharmaceuticals	46	16
Chemicals	46	29
IT services	52	25

Source: Euler Hermes

- Payment periods rigourously respected (<60 days)

France: tops and flops



Customer payment periods in days' revenue

Source: Euler Hermes

Days sales outstanding and days payables outstanding (2010)

France	DSO	DPO
Automotive	41	50
Air transport	44	44
Forging	54	53
Chemicals	59	51
Aerospace	65	49
Pharmaceuticals	66	52
Construction	87	57
IT services	95	51

Source: Euler Hermes

- The 2009 LME law has improve industry cash flow
- Two sectors still in trouble: construction (benefits from a dispensation agreement) and IT services

Conclusion

- Variations between Northern and Southern European countries are likely to increase in the very short term, despite the European Directive
  - Abrupt stop to decreasing payment periods in France in 2012
  - Another European Directive will be difficult to implement between now and 2013, especially for Southern Europe

- Sector variations will remain, fuelled by difficult economic situations and continued unequal bargaining power
  - Cash flow requirements remain high and will continue to undermine part of the industrial fabric
  - Inter-sectoral round tables have nevertheless helped to improve payment behavior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