

## Company Insolvencies



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This panorama shows, through our barometer, new trends about insolvencies in France, considering the first four months of 2014.

A lull is observed from January to April 2014, the number of insolvencies falling by 2.3%. Over the same period, the financial cost (outstanding amounts) decreased by 16.4% and jobs threatened by the insolvencies of 13.9%. However, the number of insolvencies over a year remain still high (64 127). We find the most number of insolvencies in business sectors such as services for companies and local authorities, food industry, paper - wood and automotive and transport, particularly auto-retailers.

You will also find in this panorama a comparison between the situation of SMEs in France and Spain. Essential in both countries, SMEs are dependent on challenging economic environment, with an upsurge in the number of insolvencies since 2009. However, since the crisis, despite a number of similarities, the situation of SMEs differs between the two countries. The Spanish economy improves in 2014, driven by the renewed dynamism of exports, and in parallel the situation of SMEs is recovering. Thus we expect in 2014 a decrease of the number of insolvencies of SMEs in Spain. The crisis was less pronounced in France, but the financial situation of its SMEs gradually degraded and continues to deteriorate recently. Therefore, the acceleration of growth in France will stabilize (but at a high level) the number of insolvencies in 2014.

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# Insolvency Barometer

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Thus far, 2014 has been characterised by a record number of insolvencies year-on-year (64,127, up 3.5%), well ahead of the peak seen in 2009. However, over the first four months of 2014, there has been a slowdown, with the number and cost of the insolvencies falling 2.3% and 16.4% respectively compared to the first four months of 2013. In addition, this financial cost (outstanding amounts) is at a level close to that of 2009 (4.64 billion euros), and has been on a downwards trend since December 2013. Most of the companies currently experiencing difficulties are small companies.

	January - April 2014	May 2013 - April 2014			
	Number	Number	Cost (€ bn)	Cost/GDP	Jobs at risk
Insolvencies	22,601	64,127	4.64	0.22%	192,771
Change*	-2.3%	+3.5%	+2.3%	-0.4%	-6.4%

\* Versus the same period 12 months earlier

Sources: Scores & Décisions, Coface

At the end of April 2014, the number of insolvencies reached a record level: 64,127 over one year (*Graph 1*), an increase of 3.5% year-on-year. There were more insolvencies than in 2009, during the worst period of the crisis.

The financial cost, i.e. total outstanding amounts of the insolvent companies, reached 4.64 billion euros, a level close to that at the peak of the crisis. The percentage against GDP (0.22%) decrease of 0.4 percentage point. The social cost was also high, with 192,771 jobs threatened by these insolvencies in one year, but is 6.4% lower than in the preceding twelve months.

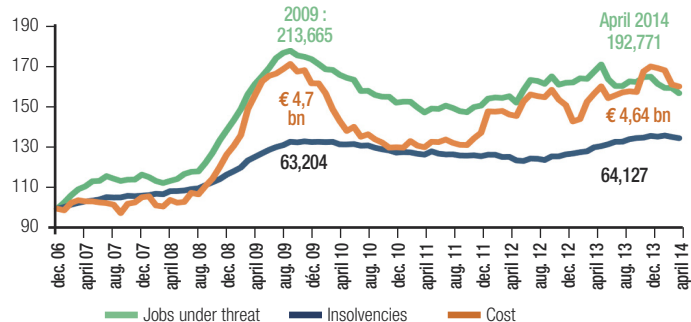
The trend seen over the first four months of 2014 was more favourable. There were 22,601 insolvencies in the period, still high and a long way off the pre-crisis levels (between January and April 2008 there were 18,427 insolvencies). Compared with 2013, this number was nevertheless 2.3% lower. The number of jobs involved and the outstanding amounts also fell, by respectively 13.9% and 16.4%.

Over a sliding twelve months, the rise in the number of insolvencies was mainly in terms of micro-enterprises (+3.9%), which accounted for 92.7% of this, together with VSEs (+0.7% for companies with between 10 and 19 employees). SMEs (between 20 and 249 employees) have a slight slowdown in terms of insolvencies (-2.8%). Among them, there was the Court ordered liquidation of «Etablissements Laporte» (clothing manufacturer) in March the receivership of «Derichebourg Atis Maintenance Services» (service activities incidental to air transportation) in April 2014, two companies with, respectively, turnovers of 23.7 and 20.6 million euros.

MSBs seem to have fared better since the beginning of 2014, with a fall of 10.5% in the number of insolvencies year-on-year. There were 34 MSB insolvencies in a year including the receiverships, in March, of «Ascometal» (2,240 employees) and, in April, of «Francaise de roues» (380 employees) and «Altia la souteraine» (324 employees), all three in the metal industry. We can mention also the receivership of «Airwell» (378 employees, specialized in manufacture and wholesale of non-domestic cooling and ventilation equipment).

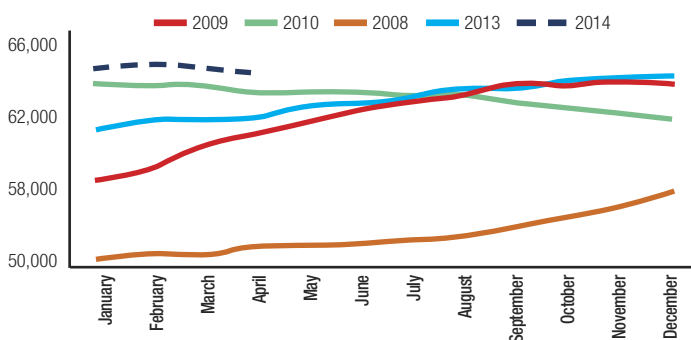
In the first four months of 2014, there was a dip in the number of company insolvencies for all kind of companies (MSB: -9%, SME: -17%, VSE: -5% and, micro-enterprises: -2%).

GRAPH 1:  
Changes in number and cost of insolvencies (base 100: December 2006)



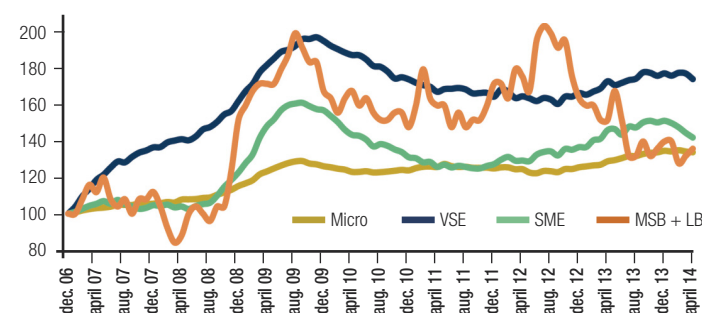
Sources: Scores & Décisions, Coface

GRAPH 2:  
Change in dynamic of insolvencies in France



Sources: Scores & Décisions, Coface

GRAPH 3:  
Change in number of insolvencies by company type (base 100: December 2006)



Sources: Scores & Décisions, Coface

# Sector Analysis

In April 2014, the number of insolvencies hit the company and public administration services, food industry, paper - wood and the automotive and transport sectors particularly hard. The only sectors with a slight slowing in insolvencies were the chemicals and metals sectors.

Sectors	Number**	Change**	Share***	Change in cost**	Cost share
Construction	20,537	0.3%	32%	-1.3%	25.3%
Services to individuals	11,151	4.5%	17%	14.3%	4.5%
<b>Other services*</b>	<b>9,704</b>	<b>6.3%</b>	<b>15%</b>	<b>13.8%</b>	<b>10%</b>
Retail	6,085	6.2%	9%	5%	10.1%
Automotive and transport	4,242	2.6%	7%	9.1%	9.9%
<b>Food industry</b>	<b>4,645</b>	<b>9%</b>	<b>7%</b>	<b>-32%</b>	<b>7.8%</b>
Textiles and clothing	2,361	3.2%	4%	-18.7%	3.6%
Electronics and IT - telecom	1,936	6.7%	3%	82.5%	11.1%
<b>Paper - wood</b>	<b>1,780</b>	<b>5.3%</b>	<b>3%</b>	<b>5%</b>	<b>5.6%</b>
Metals	1,074	-4.1%	2%	45.3%	9.5%
Chemicals	612	-2.7%	1%	-62.4%	2.6%
<b>Total</b>	<b>64,127</b>	<b>+3.5%</b>	<b>100%</b>	<b>+2.3%</b>	<b>100%</b>

\* Services for companies and public administration

\*\* 12 months from May 2013 to April 2014

\*\*\* Share: number of insolvencies in the sector/total number of insolvencies

Sources: Scores & Décisions, Coface

## ● Services for companies and public administration

This sector was particularly hard hit. It accounted for 15% of all insolvencies, with the numbers up 6.3% at the end of April on an annual sliding basis.

This related mainly to advertising agencies (+9.8%), office cleaning companies (+12.7%). Landscaping and security companies concentrate a high number of insolvencies although it decreases (respectively of 0.2% and 12.6%). Indeed, there were advertising agencies experiencing difficulties at the beginning of 2014: «Circular France» entered in receivership in January and «Selling Attitude» was in liquidation in April 2014.

There was also a 13.8% increase in the level of outstanding amounts year-on-year mainly due to the insolvency of MSBs such as «Hôpital européen de Paris» GVM Care & Research. Moreover, a large number of SMEs were also involved, including the liquidation in February of «Agce prévention sécurité privée».

## ● Food industry

This sector is somewhat underrepresented in the insolvencies (7%), but risk in the food industry is deteriorating with a 9% increase in insolvencies year-on-year. Bakers, specifically (accounted for 23.4% of insolvencies in the sector) have a 12.1% increase in number. Farming-related companies also suffered a large number of insolvencies (+27.1% year-on-year, constituting 10.1% of the sector).

These inauspicious developments were less marked in terms of outstanding amounts (-32%) as the receivership of the Doux group, at a very high cost, recedes. Moreover, there has not been any insolvency of larger-size companies in this sector since then. Recent insolvencies include SMEs with fewer than 250 employees, such as the receivership of «Villeneuve Pet Food» in March 2014, and the liquidation of «Les volailles du Penalan» in April 2014.

## ● Paper - wood

There was an 5.3% increase in the number of insolvencies in the sector as a whole, year-on-year, at the same time as the associated costs rose also quickly, by 5%. These evolutions were worse than the average across all sectors and reveal a worsening within the segment. One-third of insolvencies in the sector are printing companies, for which there was a 8.4% increase in insolvencies. The other third of insolvencies are from wood-

furniture companies, but with only a slight increase during the year (+1%). There are a number of possible reasons for this: the economic slowdown that has led to cutbacks in household expenditure, and including furniture buying. In addition, printers and publishers are feeling the impact of advancing dematerialisation and the digital revolution, smaller print runs in the printed press, and finally the shift among advertisers towards online and on mobile advertising. The continuing increase in the price of paper, which cannot be passed on in full to the end customers, is also playing a part. The receivership of the publisher «Club International du Livre France», is one example, the SME had an annual turnover of 40 million euros. We can mention also the receivership in April of «Imprimerie Gresset» (138 employees)

## ● Automotive and transport

This sector continues to suffer, as revealed by the 2.6% increase in the number of insolvencies year-on-year.

In terms of transport services, there was a 3.2% rise in insolvencies year-on-year, largely due to the worsening in the local road freight haulage sector (+6%).

Car sales have risen in the first three months of 2014 year-on-year, especially in the case of light vehicles driven by the good performance of the French car makers. There is still however at the beginning of 2014 a certain degree of fragility in the downstream segment of car-retailers (+6.1%). The receivership in March 2014, of the MSB specialized in automotive part retailer «Recam-Sonofadex» (558 employees), is an example of this.

## GLOSSARY

- **Insolvency:** legal insolvency i.e. court-ordered receivership or liquidation
- **Micro-enterprises:** companies with fewer than 10 employees
- **VSE:** very small entities with 10-19 employees
- **MSB:** medium-sized businesses with between 250 and 4,999 employees
- **Cost of insolvency:** total outstanding amounts of the insolvent companies

# Changes regarding SMEs in France and Spain: convergence, then divergence

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SMEs in France and Spain are, in many ways, similar: they represent only a small proportion of companies, but they have a critical economic weight. They are the first to suffer when the economy deteriorates: more insolvencies, reduced turnovers and cash flow shortages. They are all engaged in a fight for survival.

Although they share these characteristics, there was not evolved in the same way in 2013. There were differences in terms of their wage costs, debt and profitability. This divergent dynamic means that the forecasts are different. Despite the weakness of the recovery, Spanish SMEs, now more robust in financial terms, should see a falling off in the number of insolvencies. In France, however, the slight upturn does not give much hope for an ebbing in the number of SME insolvencies.

## CONVERGENCE: IMPORTANCE OF SMES AND OF THEIR WEIGHT IN INSOLVENCIES

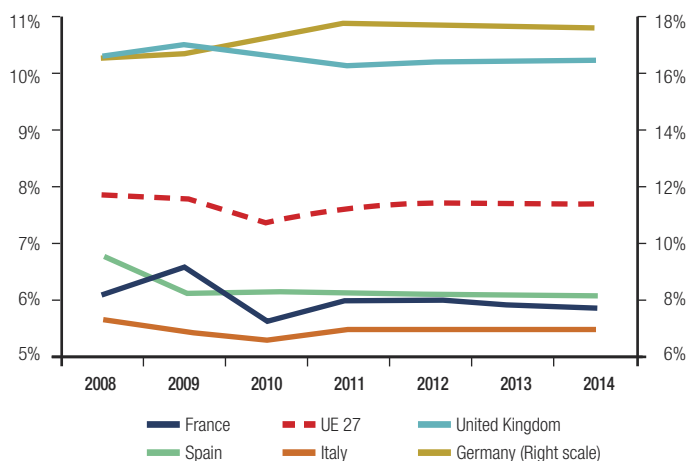
France and Spain have similar entrepreneurial structures, with SMEs forming a sort of backbone within their economies. Although small in number, they are indispensable.

### Only 6 to 7% of companies in France and Spain are SMEs...

One of the points in common in both countries is the makeup of their company infrastructure. These countries have a significant pool of micro-enterprises (94% of companies in the two cases compared with 81% in Germany).

The proportion of SMEs is therefore limited (5.9% in France and 6.1% in Spain in 2014). In addition, this proportion is also small when compared with the European average (7.7%), the United Kingdom (10.2%) and above all Germany (17.6%). There has even been a decrease in this number since 2008, by 4.2% in France and 10.1% in Spain.

GRAPH 1 :  
Change in proportion of SMEs in major European countries



Sources: Eurostat, Coface

## Definition of an SME

A Small and Medium-sized Enterprise describes a company with fewer than 250 employees, an annual turnover of less than 50 million euros or a total balance sheet not exceeding 43 million euros.

This category of companies is defined, in France, by Decree 2008-1354, compliant with European Commission Recommendation 2003/361 adopted on 6 May 2003.

In Spain, an SME was deemed, for a long period, to be any company with fewer than 50 employees. In October 2013, i.e. 10 years after most other European countries, an instruction was published in the Official Journal redefining an SME as being a company with fewer than 250 employees.

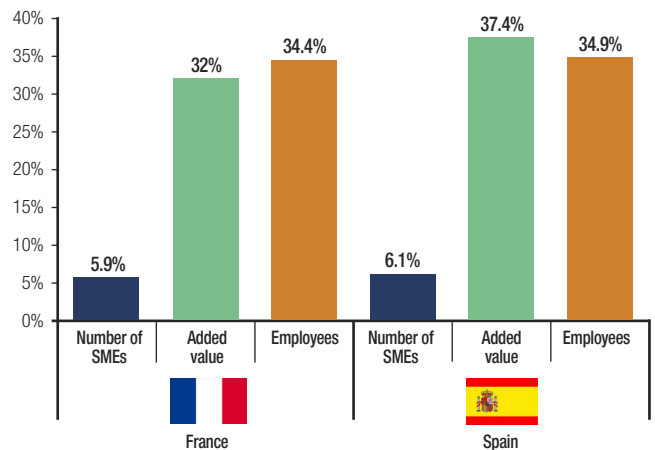
In this analysis, we will examine SMEs excluding micro-enterprises (e.g. those with between 10 and 249 employees).

## ... but they play an important social and financial role

Despite the small size of the proportion, their role within the economy is a significant one. More than one-third of all French and Spanish workers are employed by SMEs.

They also represent a significant proportion of added value <sup>(1)</sup>: 32% (284 billion euros) in France and 37.4% (167 billion euros) in Spain in January 2014.

GRAPH 2:  
Proportion by number, added-value and employees of SMEs in France and Spain



Sources: Eurostat, Coface

SMEs therefore have a major role for any growth in the two economies and are spread over a wide range of sectors.

## Similar sectorial structures

In France, as in Spain, SMEs are strongly represented in the wholesale and retail sectors (respectively 27% and 21% of all SMEs), as well as within industry and construction. The proportion in Spain (14%)

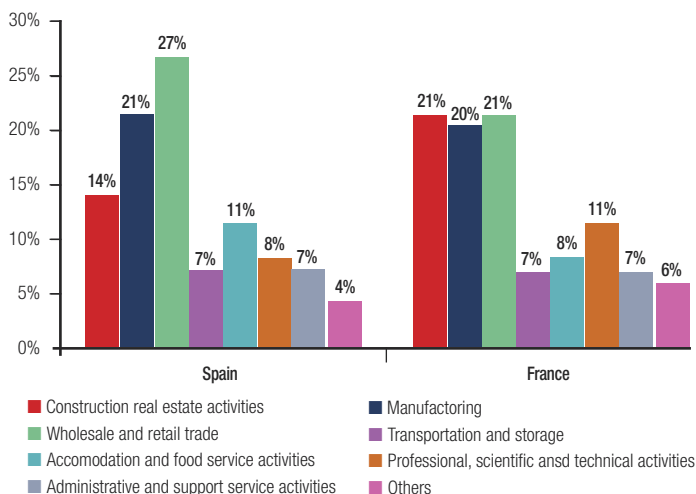
(1) Source: Eurostat, added-value for all business sectors other than agriculture, financial services and public administration



is however lower than it is France (21%), even though the share of added-value of these companies is greater there (40% compared to 36.8% in France).

In addition, there is a high percentage (26% for both countries) of SMEs in the services sector (services for individual, companies and public administration, according to Eurostat).

**GRAPH 3:**  
Distribution of SMEs by business sector at 1<sup>st</sup> January 2014



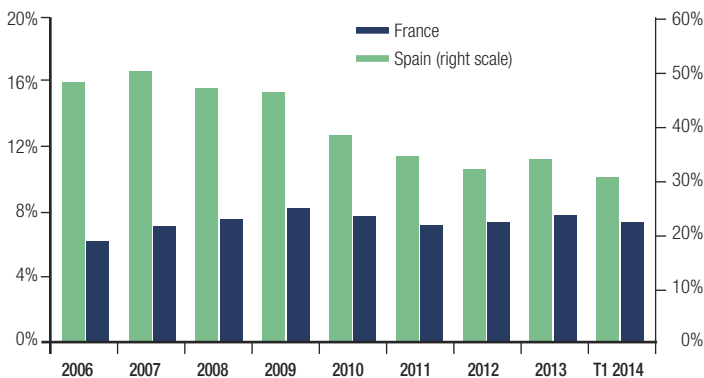
Sources: Eurostat, Coface

## A worrying dynamic of insolvencies in both countries

Despite the fact that SMEs only form a relatively limited percentage of all companies, they have a much greater representation in terms of insolvencies and particularly so in Spain. In France they account for 7.3% of insolvencies (+20% compared with 2006). In Spain, this percentage is much higher with SMEs accounting for 30.9% of insolvencies.

This kind of companies is thus seriously overrepresented in terms of insolvencies, especially in Spain.

**GRAPH 4:**  
Percentage of SMEs in total insolvencies



Sources: INE, Scores & Décisions, Coface

Until the 2008 crisis, SMEs in Spain accounted for almost half of all insolvencies (against 48.7% of insolvencies in 2006). The recent changes to insolvency legislation (see box) since 2009 have enabled more smaller companies to access insolvency proceedings, which resulted in an even greater increase in the total number of insolvencies in Spain.

Thus, since 2009, both the total number insolvencies and those of SMEs have soared: +72.6% in total and +28.5% for SMEs. This situation is a result both of legal changes and the economic crisis.

## Insolvency law in Spain

### With contributions from Christophe Barbé

Whilst the insolvency of a company in France corresponds, from a legal point of view, with receivership or Court ordered liquidation, the situation in Spain is somewhat different. Insolvency corresponds with a «concurso», i.e. a bankruptcy. There are two types here: either «voluntary» (the company starts the proceedings itself), or «necessary» (a creditor makes the application). A «necessary» insolvency is the most frequent occurrence (97%).

The law on bankruptcy 22/2003 came into force as of 1 September 2004, it was amended in March 2009, and again (38/2011) in October 2011. These amendments extended it for all types of businesses, whether incorporated entities or natural persons, and provided improved protection for the companies involved.

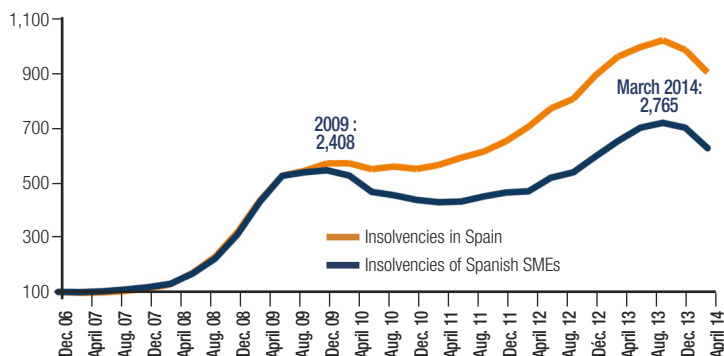
Thus, since 2009, more small companies have been able to access bankruptcy proceedings.

The Spanish law on company insolvencies grants greater protection to credit institutions, creditors of the company in difficulty, with the aim notably of protecting the banking system. In France the law is more specifically targeted at protecting employees and, in Germany, at the continued survival of the company.

The procedure in Spain is however long and costly, and therefore not especially easily accessible for small companies, even when shortened.

In the first quarter of 2014, there were 2,765 SME insolvencies in Spain over one year, a decrease of 4% compared to the year before, after a 30% increase in 2013. This insolvencies level exceeded the one recorded in 2009.

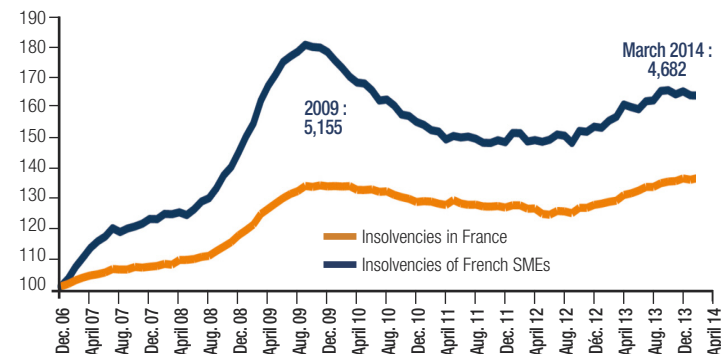
**GRAPH 5:**  
Changes in number of SME insolvencies in Spain  
(Base 100 = 2006; moving average)



Sources: INE, Coface

In France, at the end of March 2014, there were more SME insolvencies than in Spain, at 4,682 (+4% compared with 2013). This was the type of company for which insolvencies increased most in 2013.

**GRAPH 6:**  
Changes in number of SME insolvencies in France  
(Base 100 = 2006; moving average)

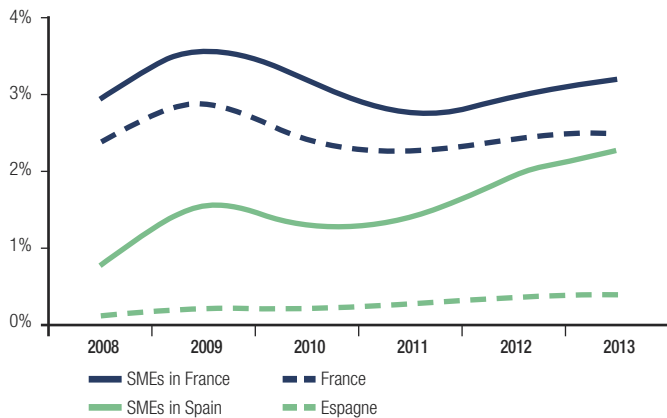


Sources: Scores & Décisions, Coface

In addition, if we compare this number with the total population of SMEs, we see that the rate of insolvency is higher in France (3.2% in 2013) than in Spain (2.3%), although the divergence between the two countries is shrinking.

This rate for SMEs in France is also higher than for all other companies. It is worth noting that in Spain the rate for all companies is especially low because of the limited number of insolvencies in the country until now.

**GRAPH 7:**  
Insolvency rate <sup>(2)</sup> for SMEs and all companies <sup>(3)</sup>



Sources: Eurostat, INE, Scores & Décisions, Coface

### SME insolvencies are occurring in the same sectors in both Spain and France

In both France and Spain, most insolvencies occur in the construction sector: one-third in France and almost 40% in Spain. The next sector for insolvencies in both countries is the services sector. This sector has more weight in France (30.7% of all insolvencies in 2013) than in Spain (19.9%). In 2013, the tertiary sector was especially hard hit, with a 25.6% increase in the number of insolvencies in France and 60.9% in Spain.

**Table 1:**  
Sectors with highest rates of SME insolvencies in 2013

Business sectors	France		Spain	
	Weight in 2013	Change**	Weight in 2013	Change**
Construction (including housing)	32.7%	-2.8%	39.6%	+10.9%
Services*	30.7%	+25.6%	19.9%	+60.9%

\* For individuals, companies and local administrations

\*\* Moving average, 2013 against 2012

Sources: Scores & Décisions, Coface, BOE, Unidad Concursal PwC

In Spain, residential investment, running at an exceptionally high level prior to the property crisis, led to seriously high household debt and an increase in the relative weight of the construction sector within the economy. This has been in freefall since the bursting of the property bubble, despite the continuing weakening of property prices (-35% since 2008). The consequence of this is that the construction sector seems to be stuck in a vicious circle. The stock of unsold homes remains large and investment in the residential sector is still shrinking, despite lower property prices, and confidence remains at rock bottom. This depression has resulted in a sharp reduction in the rate of investment, which was significantly in excess of available savings until the bursting of the property bubble. In addition, the rate of delinquent loans in this sector continues to rise and is in excess of 30%, evidence of the degree of vulnerability of the sector.

In France, there was a decline in the number of new housing starts in 2013 (-4.2%), struggling because of the high cost of land which is discouraging many property developers who are uncertain about their ability to then sell it on. As economic growth is weak and unemployment remains high, housing prices seemed to have reached an unaffordable level in the boom years of the 2000s, without however reaching comparable levels to the Spanish bubble. The French property market has been in a gradual adjustment phase for the last two years.

The tertiary sector accounts for almost a third of all insolvencies in France, but it is nevertheless not overrepresented, in so far as its share is essentially the same in terms of the number of companies (31%). In addition, companies in the sector are structurally more fragile, because they have less capital (the median equity for insolvent SMEs in the services sector in 2013 was €10,000 compared with €38,000 for all SME insolvencies). In addition, services, whether for companies or individuals, are the first cost item eliminated when budgets are cut.

## INTERVIEWS

**Ramón Baucells,**  
Chief Executive Officer, Grup Baucells  
Alimentacio S.L.\*

«The situation in Spain is going to improve, but slowly»

### What are the main problems you are facing, as an SME, in Spain?

We are in fact on the boundary between an SME and a MSB in that we employ 257 people and have a turnover of 67 million euros. The key difficulties relate to business financing. Banks are reluctant to grant new credit and are trying to cut back on their positions. On top of this, the government has raised taxes, and in particular VAT, to increase its revenues, which is particularly handicapping for exporting companies.

### As a general rule, what types of companies have been worst affected by the crisis since 2009?

Companies associated with the construction sector have been very hard hit since 2009. The other leading victims of the crisis include those companies that depend on public expenditure, which has been significantly reduced.

### Do you think the situation is going to improve for your company, and more generally, in Spain in 2014?

My feeling is that the situation in Spain is actually going to improve, but only very slowly. This should also apply to my company, although the food processing sector did hold up pretty well through the crisis.

\* Family-owned group specialised in processing and preservation of meat products

(2) Number of SME insolvencies relative to total number of SMEs

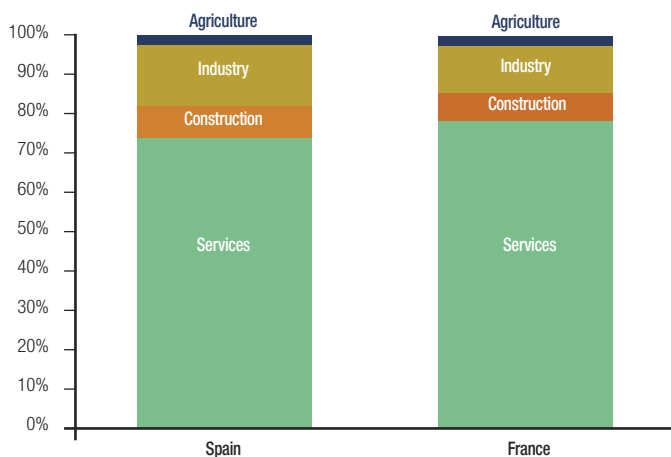
(3) Eurostat perimeter which includes companies and individual entrepreneurs (not including «auto-entrepreneurs», civil partnerships, general partners, self-employed professionals, or agricultural businesses).

## CHANGE IN SPAIN, STAGNATION IN FRANCE

### Two economies with lots of points in common

France and Spain are both so-called «advanced» economies, with structures sharing many common points. The tertiary sector accounts for between 70% and 80% of GDP. The Spanish economy however is slightly less dependent on services, and more on industry (15.9% of GDP in 2012) and the construction sector, despite the share of GDP by this sector declining from 12% to 7.9% between 2009 and 2012.

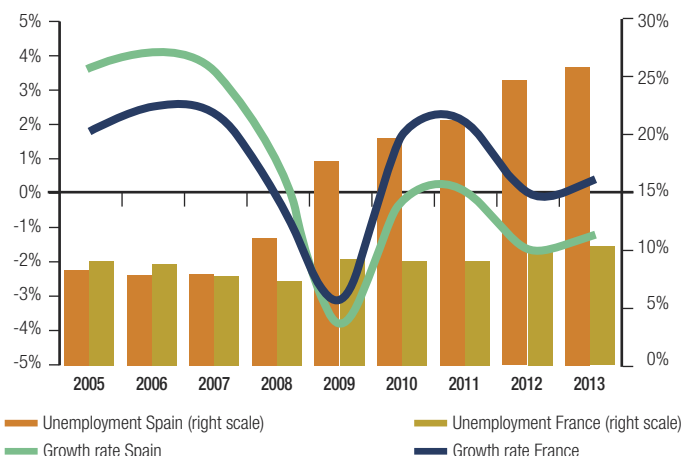
**GRAPH 8:**  
GDP distribution by sector



Sources: INE, INSEE, Coface

Spain was experiencing growth well ahead of that of France prior to the onset of the crisis in 2008 and a slightly lower rate of unemployment (8.2% against 8.9% in France in 2006). It has however suffered more in the crisis, and has reported annual growth around 2 percentage points lower. The reasons for the persistence of the crisis in Spain are mainly a result of the accumulated imbalances prior to 2008, such as the property bubble, the over-indebtedness of the private sector and the weakness of the banking sector. Imbalances have currently being resolved, but have delayed any return to growth. The ferocity of the crisis resulted in major changes for Spanish companies. As the effects of the crisis were less marked in France and with activity indicators remaining stable, companies were not forced to restructure their businesses or their operations.

**GRAPH 9:**  
Growth rate and unemployment

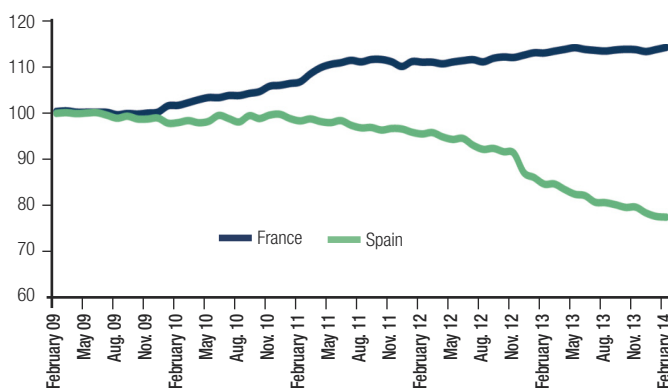


Sources: INE, INSEE, Coface

### Consumption: resilience in France, collapse in Spain

The Spanish economy is currently suffering a drought of credit. Following the bursting of the Spanish property bubble, which led, among others, to the disappearance of over 80% of regional saving institutions, highly exposed to the real estate sector, the conditions for obtaining credit have remained very tight.

**GRAPH 10:**  
Change in credit in the private sector (base 100 = February 2009)

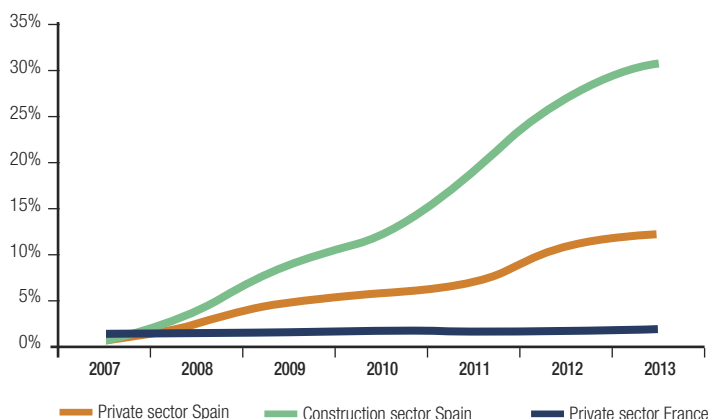


Sources: Banco de España, Banque de France, Coface

There was also a rapid growth in the rate of delinquent loans, reaching 13.4% in February 2014 (less than 2% in France), which forced the banks to become much more cautious and set aside larger provisions (*graph 11*). These banks have had to restructure and, for the time being, reduce the amount of credit.

The contraction of credit in Spain (-10.6% between August 2012 and November 2013) cannot however be explained solely in terms of the supply.

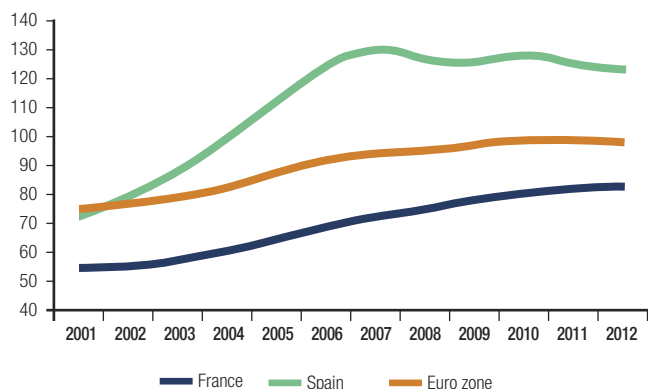
**GRAPH 11:**  
Delinquent loan rate



Sources: Banco de España, Banque de France, Coface

The heart of the problem in the Spanish was the excessive debt of the private sector: households (with gross debt running at 130% of disposable income prior to 2007) and companies, were forced to take steps to reduce their debts. This meant that applications for credit from individuals declined. The domestic market in Spain is thus particularly depressed, with very weak consumption.

**GRAPH 12:**  
Change in gross household debt;  
% of available income

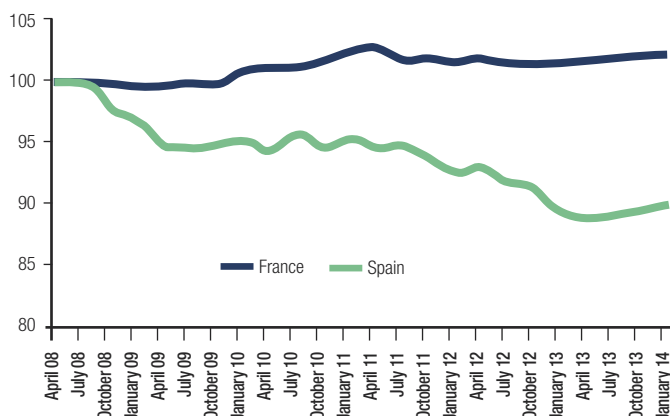


Sources: Eurostat, Coface

At the same time, in France, private sector credit slightly increase (*graph 10*). French banking institutions suffered much less in the crisis than their Spanish counterparts. In addition, household debt, whilst higher, held at a relatively low level in France, at around 80% of disposable income, compared with 100% as an average in the Eurozone and 120% in Spain (*graph 12*). This stability in credit and the relative margin of manoeuvre for French households helped sustain consumption which, whilst not dynamic, was at least stable (*graph 13*).

Whilst household consumption, since 2008, has contracted by an average of 1.7% a year in Spain, it grew at an annual average rate of 0.4% in France.

**GRAPH 13 :**  
Household consumption (base 100 = April 2008)



Sources: INSEE, INE, Coface

Another significant factor in France, the unemployment rate although high (10.2% in the 4th quarter 2013) remains stable and, above all, very low compared to that in Spain (25.9%), with the result that the purchasing power of many households was drastically reduced. Thus, whilst Spanish SMEs point to the lack of demand as the main factor holding up their growth, their French counterparts tend to point to the cost of production and of regulations<sup>(4)</sup>.

Despite these divergent consumption dynamics, the sectorial structure of insolvencies remains similar.

### 3 questions for

**Roseline Giraud,**  
Head of Risk, Coface Iberica

#### «Spanish SMEs have had to adapt to survive»

#### What is the situation of Spanish companies (excluding the big groups), after five years' of crisis?

Spain is currently going through a severe economic crisis with extremely serious social consequences. Between 2008 and 2012, almost 1.9 million companies closed, 99.5% of these employed fewer than 20 employees, resulting in mass unemployment in Spain. At the same time, 1.7 million new companies were created, resulting in a change in the profiles of Spanish SMEs, and in particular of the sectors in which they operate.

Those companies that survived this lengthy period of crisis have to deal with a significantly worsened economic environment (collapse in domestic demand, problems obtaining finance).

To endure this particularly difficult economic context, companies have had to adjust their sizes, by cutting workforces, and labour costs. These latter have declined markedly over the last three years, resulting in an increase in productivity in Spain. Companies have also improved their internal processes and their current assets.

In this depressed domestic climate, exports have provided an important alternative. Those companies that were already exporting before the crisis then refocused their efforts on developing sales in foreign markets (in Europe, as well as in Africa, South America and even Asia). After this time we have seen that the companies able to adapt were those with a «professional» management that was able to deal with the drying up of bank credit. Following years of open-handed granting of credit, Spanish banks carried out a major internal restructuring, which has an impact on the real economy. They were forced to make drastic reductions to the lines of credit and working capital loans, thereby undermining the Spanish entrepreneurial fabric and especially SMEs.

Now, after five years of crisis, the remaining companies are better organized, with rationalised costs and flexible structures.

#### Do you think that the situation of French (SME) companies is comparable with Spanish companies?

I think that the «timing» for the two countries is not the same. French SMEs are currently facing challenges that Spanish SMEs had to face several years ago.

The crisis is much more severe in Spain, and has lasted much longer than in France.

In Spain, the crisis was triggered by the collapse of the construction sector (and associated sectors), which, after a slow period, had achieved a significant weight within the Spanish economy. This collapse led to the insolvency of many companies in the sector as well as in dependent sectors.

Another major difference is that the Spanish labour market has become much more flexible, as a result of the Labour Reform implemented, two years ago, by the government. This increased flexibility was also enabled by the unions (poorly represented in SMEs) which were looking for solutions, together with the companies, to help protect jobs.

(4) "Survey on the access to finance of small and medium-sized enterprises in the euro area", European Central Bank, April 2014..



... 3 questions for

**What is, for you, the outlook for Spanish companies in 2014, and 2015?**

In global terms, 2014 is still going to be very difficult for them, because of the limited GDP growth expected and the extremely high rate of unemployment.

A number of measures recently adopted by the Spanish government and Central Bank do however give us grounds for optimism about the future for SMEs.

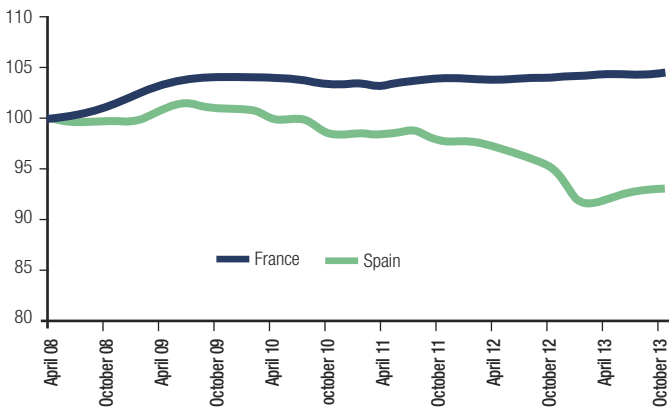
In terms of banking, once they have completed their restructuring, the major Spanish banks are about to launch specific programmes aimed at providing financial support for SMEs, and these should help make more credit available over the coming months.

Finally, over recent months there has been an upturn in foreign capital investments in Spain, thanks to improved productivity and lower wage costs in the country, together with quality service. In terms of underwriting<sup>(5)</sup>, despite the lack of any noteworthy improvement in turnover and profitability, we have noticed, since the final quarter of 2013, a slight reduction in risks.

**Globalisation of Spanish companies and status quo in France**

In coping with an especially unfavourable context, Spanish companies have had to reduce their labour costs. The reductions in workforces led to a significant increase in unemployment, a drop in wages and in the cost of labour in 2012-2013, helping Spanish companies improve their competitiveness in the export market. In addition the Spanish government has implemented certain measures, notably through ICEX (Institute for Foreign Trade) with the aim increasing the global reach of companies.

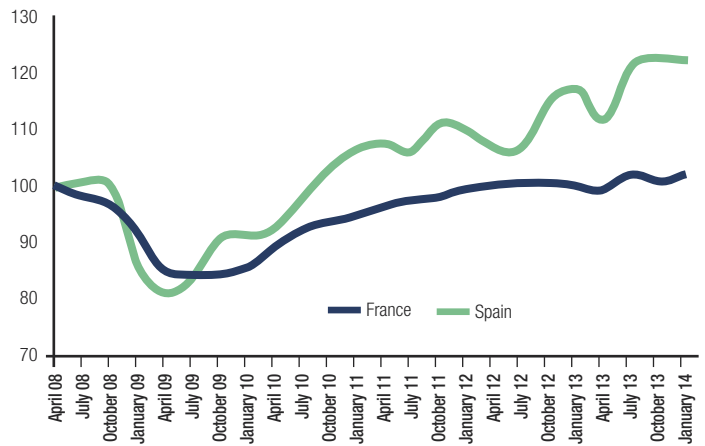
**GRAPH 14:**  
Changes in real unit labour costs (base 100 = April 2008)



Sources: Eurostat, Coface

At the same time, labour costs have continued to rise in other European countries. As a result, Spanish exports of goods grew by over 7% in 2013, whilst they stood still in Italy and Germany (graph 15). This growth in exports helped counterbalance the recession in Spain in 2013. Spanish SMEs have benefited from this trend in that 25% of them are exporters (compared with only 19% in France).

**GRAPH 15:**  
Exports of goods (base 100 = April 2008)



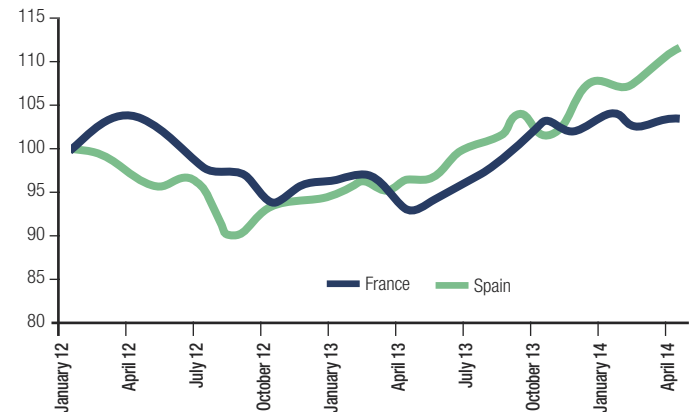
Sources: Eurostat, Coface

The picture in France is quite different, exports of goods dipped by 0.1% in 2013. French companies, unlike their Spanish counterparts, have not had to deal with the competitiveness shock, and are thus not in a position to win back market share in export markets. They are thus essentially reliant on the resilience of domestic demand, supported by a constant increase in earnings. Despite the depressed state of foreign trade, the fact of exporting is nevertheless an advantage for SMEs. There was thus a decline (-1.8% in 2013) in the number of insolvencies among exporting SMEs (17.5% of the total).

**Investor confidence: ray of hope in Spain, persistent gloom in France**

In addition, the Spanish business confidence indices<sup>(6)</sup>, whilst still relatively pessimistic, are improving. The proportion on «pessimistic» businesses with regard to the next quarter was 15% higher than those saying they were «optimistic» in April 2014, against 39% the previous year. The sour note is that businesses in the construction sector remain mostly «pessimistic», with the percentage of these latter being 48% greater than those who are «optimistic». SMEs, relatively more «pessimistic» than other types of companies until July 2013, are now more «optimistic», the above mentioned ratio was at just 13% for Spanish SMEs.

**GRAPH 16:**  
Change in business confidence indicators; (base 100 = January 2012)



Sources: INSEE, INE, Coface

(5) Underwriting: Department specialising in managing the risks involved in the credit-insurance business.  
(6) Source: INE, Indicadores de Confianza Empresarial (ICE)

Whilst SMEs see the future in a relatively optimistic way in Spain, in France, the trend for the business confidence index is one of stagnation (*graph 16*). Whilst the Spanish business confidence index has constantly improved since August 2012, it has persistently fluctuated in France. The business confidence index is currently at the level of October 2013 in France and in Spain it has risen by almost 10%. In terms of French SMEs, the latest surveys carried out since the beginning of 2014 <sup>(7)</sup> reveal a renewed optimism and investment intentions. They are therefore positive but do not in any way guarantee a sustainable improvement, business confidence remains fragile.

The particularly difficult macroeconomic context in Spain seems to explain the high level of SME insolvencies in the country. Growth in France was more resilient but even so it has been historically weak since 2009. French SMEs are however increasingly vulnerable to the economic situation because of a worsening of their financial situations.

### 3 questions to

**Farida Taleb,**  
Senior Underwriter,  
Coface France

«End of the tunnel, at last, perhaps»

#### What is the situation of the French SMEs in 2014?

As creators of jobs, SMEs have a significant position in the French economic fabric.

In 2013, there was a sharp increase in the number of insolvencies for this type of company. The sectors that suffered most were those of construction and services, where a high level of concentration of SMEs can now be seen.

In day-to-day terms, there has been a worsening in the financial situations of companies resulting from fewer orders and a gradual erosion of their margins.

With negative EBITDA and self-financing capacities, companies can no longer finance their investments or growth. This situation can be seen in all business sectors.

#### What are the difficulties facing SMEs today?

In our business, we have noted two major problem areas:

The first is the lengthening of the average payment period. The cash flows of SMEs are dependent on the conditions of payment of the major buyers.

The worsening margins for the companies means that they cannot expand their capacities. The shortage of liquidity is a brake on investment for SMEs, the key driving force for growth through research and development (moving upmarket) and opening to exports outside Europe.

#### Is the situation for SMEs going to improve between now and end of the year?

It is difficult to predict but there has been, since the beginning of the year, some revival in activity for SMEs. If this trend continues, the number of insolvencies should begin to decline.

And whilst there might be shorter payment times for SMEs, that is not the case for micro-enterprises.

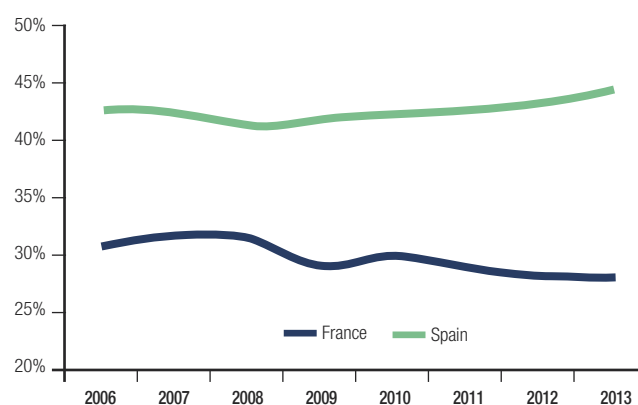
In general the construction sector is expected to have a difficult year, in so far as we have not seen any increase in the number of building starts or new contracts.

## Divergence in how the financial situations of SMEs are changing

Starting from a similar entrepreneurial structure, Spain and France are now showing marked divergences from a micro-economic point of view.

Firstly, the profitability of Spanish SMEs has been improving since 2008 (margins increased by 2.5% in 2013). The level in 2013 was higher than that recorded prior to the crisis (*graph 17*). This was driven up by the significant reduction in wage costs as well as the disappearance of weaker and by unprofitable companies. This ongoing improvement in their financial health reflects the recovery among Spanish companies and is in contrast with the dynamic within French companies. The margins for non-financial companies reached almost 45% in 2013, against less than 30% in France, where the trend is towards further contraction.

**GRAPH 17 :**  
Gross margins for all companies \*



(\*) Gross margin = EBITDA/AV  
Sources: INE, INSEE, Coface

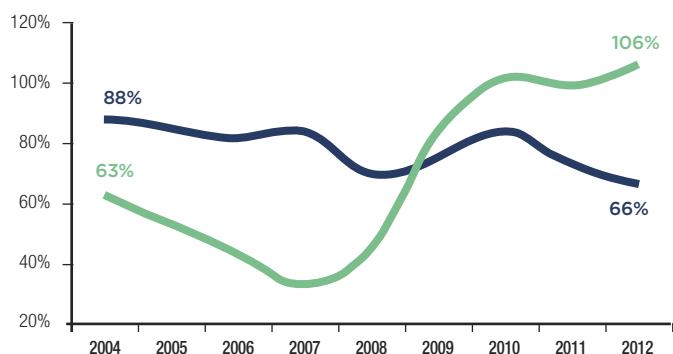
In France, margins remain at low levels because even when business slows, employment and fiscal charges continue to rise, preventing companies from remaining profitable. This applies to all companies, regardless of size. French SMEs are in fact the hardest hit with margins of 20.8% <sup>(8)</sup> in 2012, down 1.1 percentage point on 2011. This is the lowest margin since the 1990s. It is also the lowest in Europe: In 2012, this was 40% in Germany, 39% in Italy and 37% in Belgium and 28% for the European Union. In addition to this decline, French SMEs have a structurally poor profitability which holds them back once business activity starts to pick up. They are locked in a struggle to survive.

The rate of self-finance is another divergence between French and Spanish companies. Until 2008, this was less than 60% in Spain and below the French rate. In 2012, this was 106%. The financial crisis in Spain resulted in a sharp reduction in credit and required companies to find finance sourced from their own resources.

French companies have for their part been experiencing a slow erosion of their ability to self-finance, reaching a very low level in 2012 (66%). They are becoming increasingly dependent on bank credit.

(7) The 36<sup>ème</sup> Observatoire Banque Palatine des PME-ETI (17 April 2014) and Baromètre CapEx 2014 by GE Capital (7 April 2014).  
(8) Source: Banque de France

**GRAPH 18:**  
Self-financing rate for all companies  
(gross savings / GFCF)



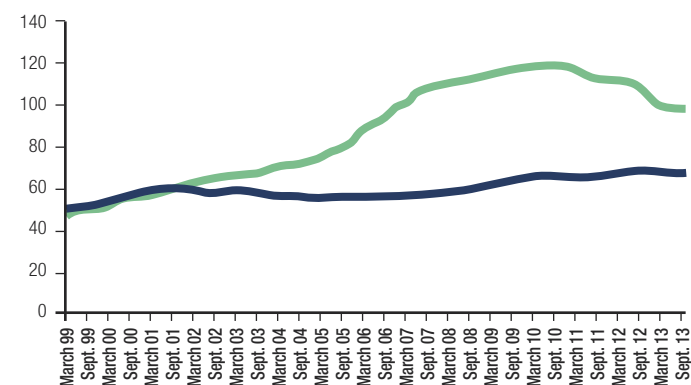
Sources: Eurostat, Coface

The second major factor is company debt.

Whilst Spanish SMEs may seem more profitable, they are still heavily penalized by their debt levels.

Although the situation of companies in terms of debt (relative to GDP) were similar on both sides of the Pyrenees in 2002, their trajectories have diverged since then.

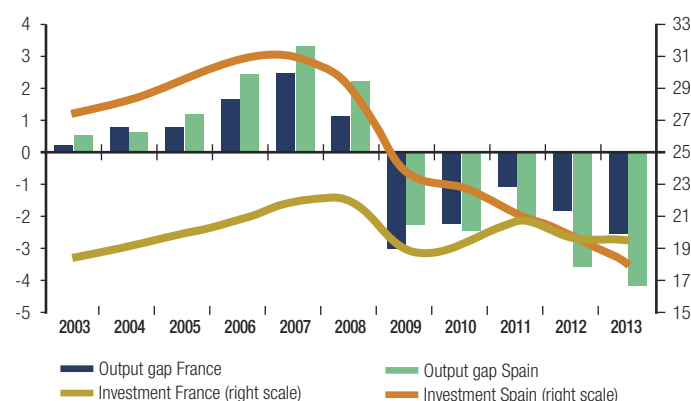
**GRAPH 19:**  
Debt for all companies, as % of GDP



Sources: Banque de France, Coface

Thus, in 2013, Spanish companies were heavily indebted (97.9% of GDP in the 3<sup>rd</sup> quarter), despite the ongoing debt reduction operation referred to earlier. This high level of debt acts to paralyse companies as they use their accumulated cash to service the debts. The scale of the debt then requires further action to restructure their liabilities, to the detriment to investment, notably in R&D (graph 20).

**GRAPH 20:**  
Output gap<sup>(9)</sup> and investment rate; % of GDP



Sources: OCDE, Coface

The result of this decline in investment has been a growing «output gap»<sup>(9)</sup>, of 4% of potential GDP, compared with 2.5% in France, where investment, although not outstanding, has at least been resilient, similarly to credit and consumption. The feebleness of domestic demand, together with the operations to reduce company debt levels, are holding back the recovery of the economy in Spain, which is operating well below its potential.

The level of debt is lower in France (67.3% of GDP in 4<sup>th</sup> quarter 2013), and relatively stable since 2000. SMEs have only a limited level of bank debt (63.5% in 2012<sup>(10)</sup>) and a financial debt level<sup>(11)</sup> of 86%.

### Governmental measures in support of SMEs in France and Spain

In France, President François Hollande announced, during his Christmas Message on 31 December 2013, the establishment of the Responsibility and Solidarity Pact (*Pacte de responsabilité et de solidarité*), aimed as a priority at SMEs and VSEs. This is based around three elements: A reduction in social contributions, a reduction in taxation, and the simplification of administrative procedures, also known as the «choc de simplification» («simplification drive»). In 2015, exemptions from employer contributions paid to Urssaf will help reduce the cost of labour for employees on the SMIC (Minimum wage). As of 2016, family benefit contributions will be reduced by 1.8 points, for wages between 1.6 and 3.5 times SMIC. In total, according to the government, the additional wage cost reductions will amount to 9\* billion euros. Family benefit contributions will also be reduced for free-lance workers, in an amount of 1 billion euros. These reductions in contributions will also be accompanied with a modernisation and a reduction in corporation tax to help encourage investment. The 'social solidarity' contribution on companies, paid by around 300,000 companies, will be ended by 2017, with a first cut of 1 billion euros in 2015. The 'exceptional corporation tax contribution' (*contribution exceptionnelle sur l'impôt sur les sociétés*) - will also be withdrawn, in 2016, and the standard rate will be reduced from 33.3% to 28% in 2020, with a first cut in 2017. In terms of the choc de simplification, an initial measure that allows companies with fewer than 50 employees (previously 20) to use simplified accounting has already been implemented. Further simplification measures will be applied over the coming months, in application of the recommendations of the Simplification Council (*Conseil de la Simplification*), which submitted, on 14 April, 50 proposed measures. The reduction in the amount of legislation on micro-enterprises, the possibility of setting up a company with just one document registered with a single agency and the extension of the «*chèque emploi*» (for personal/domestic service employees), simplification of the hiring procedures for VSEs, for companies with fewer than 20 employees (10 currently), are mentioned specifically. In return, companies must commit to investing more in France and ultimately to creating jobs. The MEDEF and three of the five trade union organisation signed an agreement on 5 March 2014, giving each business sector union responsibility for negotiations covering potential detailed objectives. The Responsibility and Solidarity Pact is in addition to the employment competitiveness tax credit (credit *impôt compétitivité emploi*) (CICE), in force since January 2013, including a reduction in corporation tax, estimated to be worth 20\* billion euros by 2017, aimed at helping finance R&D work. Thus, with the aim of increasing their competitiveness, French companies will benefit from an overall annual reduction in the cost of labour of 30 billion euros and a related simplification in taxation and administrative procedures. All of these reductions will be financed through budget savings worth 50\* billion euros included in the stability Programme approved by the French National Assembly on 29 April.

\* Source: [www.gouvernement.fr](http://www.gouvernement.fr)

(9) Output gap: Gap between potential output and actual output

(10) Source: Banque de France

(11) For Insee, the financial debt rate includes principally loans (notably securities and bank) as well as current bank credit.

The Spanish government introduced, on 7 March, by Ministerial Decree, measures aimed at helping with the refinancing and restructuring the debt of companies in difficulty. The debt/GDP ratio of Spanish companies is 30 points higher than it is in Germany and France. Under this, creditor banks can more easily convert the debts of companies that are in danger, but operationally viable, into equity, and thus become shareholders. In addition, this Decree also withdrew the obligation to make an offer for all the equity of the company when a holding reached in excess of 30% of the equity. If there was opposition from the majority shareholder, a report by an independent expert, assessing the viability of the company, could require that shareholder to agree to the refinancing operation. In addition, as of the beginning of the year, Spanish SMEs have been able to delay the payment of VAT until the recovery of the corresponding invoice. This measure is intended to reduce the vulnerability of these companies, often exposed to long payment terms leading to cash flow problems when paying VAT. On top of this, companies with turnovers of less than 10 million euros can now deduct 10% from their profits subject to the condition that they reinvest it, when paying taxes. These measures supplement the law on supporting businesses and their globalisation, approved in September 2013. This is intended to support the development of business projects, to simplify administrative formalities, encourage globalisation, the mechanisms for extrajudicial negotiations, the tax and Social Security measures to help provide the financing. Finally, a draft law aimed at promoting company financing was submitted in March and is awaiting approval. This would in particular introduce a system of advance notice to SMEs from the banking institutions prior to any withdrawal or reduction in their lines of credit.

### Another key point for SMEs: Their ability to manage their cash flows

In France, customer and supplier payment terms<sup>(12)</sup> in 2012 were 43.7 and 51.7 days of turnover for all companies. These decreased 17% between 2006 and 2012. In Spain, the average observed payment term that was 95 days<sup>(13)</sup> in 4th quarter 2013, has been a decrease of 7.3% since 2011 but, after Italy, it is still the longest in Europe.

Since the adoption of European Directive 2011/7/EU in February 2011, transposed in Spain (by Royal Decree) and in France (as part of the economic modernisation law - LME) in 2013, all public bodies are required to apply a maximum payment term of 30 days for companies, with companies subject to a 60 days maximum.

Whilst the terms of payment are identical on paper, the reality is quite different. These terms are not always applied in fact and SMEs are frequently burdened with overly long waits for payment. Thus, in France, the customer and supplier period specific to SMEs were respectively 43.5 and 51.5 days of turnover in 2012 (in continuous descent since 2006), smaller companies find it in reality extremely difficult to deal with bad payers. The overly long payment periods result in liquidity shortages, often a precursor of an insolvency. The smaller the company, the greater its vulnerability in terms of cash flow.

Spanish SMEs are precarious because of their high levels of debt and significant pressure on their cash flows, but have seen an improvement in their profitability since 2012. French SMEs have seen a worsening in their financial situations and a loss of competitiveness, and this despite a lower level of debt than their Iberian counterparts.

What is going to happen in 2014?

## OUTLOOK FOR SME COMPANY INSOLVENCIES IN 2014

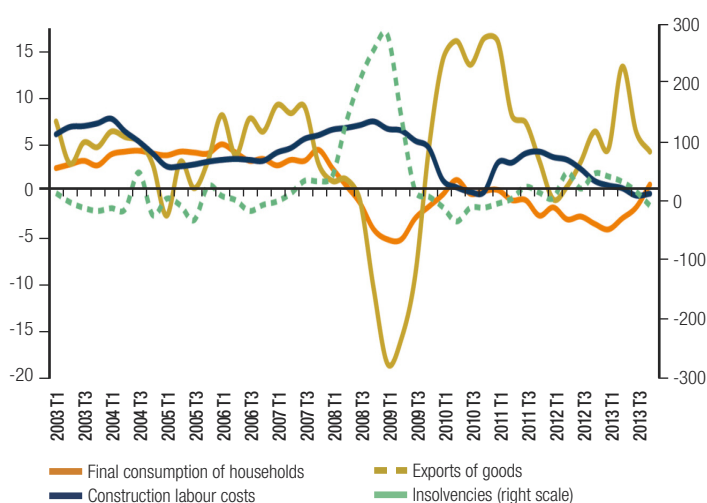
As we have seen, SMEs are sensitive both to the macroeconomic environment in their home countries as well as to the state of health of their business sectors. A set of indicators has been used to identify the critical factors in SME insolvencies, both in Spain and in France.

### SME insolvencies in Spain are influenced by exports of goods and by household consumption

We have included three variables in our forecast insolvencies model for Spain, covering quarterly data from 2003 to 2013. The first quarter 2014 was not integrated because GDP components, were not, at this stage, available.

These reflect the influence of the construction sector, preponderant among SME insolvencies, but also the dependence of SMEs on demand, whether domestic, represented by household consumption, or external, in the form of exports of goods.

GRAPH 21: Key factors in insolvencies in Spain, Change N/N-1



Sources: INE, Eurostat, Coface

Final consumption (cons) of households, as explained above, is the driving force of the Spanish economy, and is thus a key component for company insolvencies. An extended downturn in consumption would have the knock-on of keeping the rate of insolvencies at a high level. Construction, the sector with the most SME insolvencies, is shown in our model by the cost of labour in the sector (Lab cost). This rose by around 5% during the period 2003 to 2009 in the wake of rising wages (4.8% a year on average, compared with 4% in industry and services) and well ahead of annual inflation (2.7%). Whilst, until the property bubble burst, the vitality of the sector made it possible to absorb these costs, this is no longer the case, lack of outlets, and labour costs are thus a major handicap for the profitability of the sector.

The upturn in labour costs (+3%) within the sector between mid-2011 and mid-2012 therefore resulted in a significant increase in SME insolvencies during that period. Conversely, the reduction in costs during the last two quarters of 2013 (-0.5%) helped bring down the number of insolvencies in the 4<sup>th</sup> quarter (-9.5%). A sharp rise in labour costs in the construction sector in 2014 would therefore drive up the number of insolvencies.

As we noted previously, Spanish companies are becoming increasingly global. The weakness of domestic demand has forced them to look to other markets. This means their export performances are critical. Following the restructuring of their businesses and the fall in their labour costs, they have now

(12) Annual report of the French payments period Observatory (l'Observatoire des délais de paiements) in 2013

(13) Source: Informa



achieved a certain level of competitiveness. As a result, the export of goods (expgoods) now sustains Spanish SMEs and will contribute to reducing the rise in the number of insolvencies during the year.

The model for Spanish SME insolvencies is thus:

$$\Delta \text{Def} = \text{Const} + \alpha \Delta \text{LabCost} + \beta \Delta \text{Expgoods} + \gamma \Delta \text{Cons} + \epsilon$$

**Table 2:**  
Statistical model of Spanish SME insolvencies

Variable	Coefficient	P Value*
Constant	14.5	0.44
Construction labour costs	9.05	0.0102
Final household consumption	-10.23	0.0003
Exports of goods	-3.39	0.0167

(\*) Makes it possible to check the significance of the variables the p-value is the smallest of the values for  $\alpha$  for which the decision will be to reject H0.  $\alpha$  is the probability of incorrectly rejecting the H0 hypothesis;  $\alpha$  is also known as type I risk (size of test). In addition, R<sup>2</sup> adjusted is 0.60.

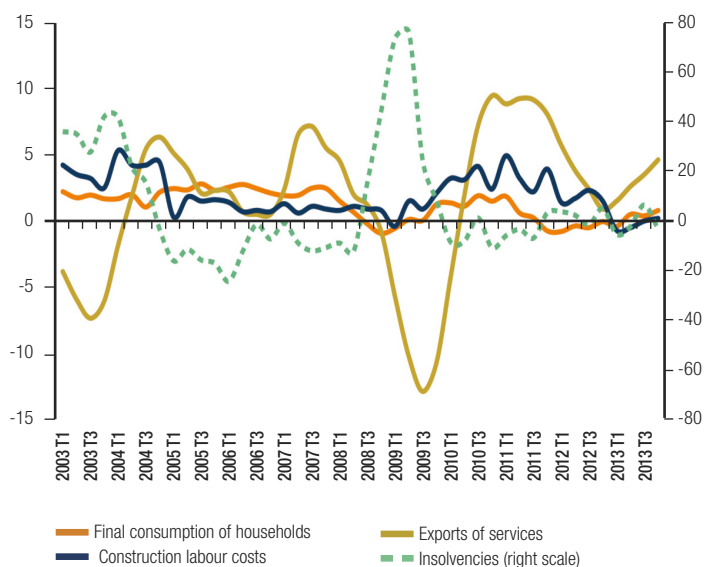
Thus, in our hypotheses for 2014, with a slight upturn in consumption (+1.1%), significant growth in exports (+5.5%) and a standstill in labour costs in construction (+0.3%), SME insolvencies in Spain should decrease between 13 and 15% (according to growth between 0.7 and 1.2%).

### French SME insolvencies sensitive to household consumption and exports of services

When we apply this model to the French economy, the outcomes are also significant but with slight differences. Household consumption (cons) and labour costs in the construction sector (Lab cost) are also, in France, a significant influence on SME company insolvencies, with one divergence however: the coefficient for the «construction labour costs» factor is 3 times higher in Spain than in France.

French SMEs are dependent on the good health of domestic demand. As construction is the most frequent sector among SME insolvencies, changes in labour costs in that sector have repercussions on the number of insolvencies. In addition, because of the cutting of wages in the sector in Spain, French SMEs in the construction sector are facing increased competition, illustrated by the loss of a number of contracts won by their Spanish counterparts, making them even more sensitive for variations in costs.

**GRAPH 22:**  
Key factors in insolvencies in France, change N/N-1



Sources: Insee, Eurostat, Scores & Décisions, Coface

In France it is the export of services (expserv) and not goods that has the largest significant influence on the number of SME insolvencies. This element might appear as something of a surprise in that exports of services are often ignored. They do however account for more than a quarter of all French exports, and France is the world's 5th largest exporter of services. Extending from tourism to transport, and including communication, computing, insurance and construction services, exports of services have proven more dynamic than exports of goods over the last few years (+5% on average since 2011 against +2.4%). These have also helped ensure a constantly growing balance of trade surplus (33.2 billion euros in 2013). This solid performance by in terms of services exports since 2011 has helped bring about a stabilisation in the number of insolvencies during the period (-0.6% on average), despite resilient, but relatively flat, consumption (+0.1%).

This means that the number of SME insolvencies in France, where the economy is more service oriented than in Spain, is sensitive to changes in service exports. The higher percentage of tertiary sector companies among French SME insolvencies, higher than in Spain, explains this sensitivity. Any increase in exports of services thus leads to a reduction in the number of insolvencies.

The model for French SME insolvencies is thus:

$$\Delta \text{Def} = \text{Const} + \alpha \Delta \text{LabCost} + \beta \Delta \text{Exp serv} + \gamma \Delta \text{Cons} + \epsilon$$

**Table 3:**  
Statistical model of French SME insolvencies

Variable	Coefficient	P Value*
Constant	11.38	0.0099
Construction labour costs	3.96	0.0012
Final household consumption	-7.46	<0001
Exports of services	-2.64	0.0150

Based on the Coface forecasts for 2014, household consumption should increase at a moderate rate (+0.8%), exports of services will remain strong (+3%) and labour costs in the construction sector will increase slightly (+0.5%). This means that, in France, the level of SME insolvencies is expected to remain stable (-0.5%) through the year.

## CONCLUSION

The situation of SMEs in the two countries has been diverging since 2012. Spanish SMEs remain vulnerable because of their high debt levels, although their profitability has improved with the significant reduction in labour costs. French SMEs have lower debt levels but their margins have been in decline since 2008, despite a temporary lull in 2010-2011. The problems being faced by Spanish SMEs can be explained by the difficult macro-economic environment (drying up of credit, weak consumption and investment, very high unemployment). But this labour costs decrease, as painful as it was, now seems to be starting to bear fruit, in particular in microeconomic terms. The financial situation of SMEs in France has gradually worsened since the start of the crisis. Growth has proven to be more resilient but not strong enough to save those SMEs that have been weakened by their increasing financial vulnerability in a context of depressed activity.

Thus, thanks to the vitality of Spanish exports and the relative stagnation of consumption and labour costs in both countries, we are forecasting a decrease in the number of SME insolvencies in Spain of around 13%, whereas the number in France should remain stagnant during 2014.