Insolvencies in Europe

2003/04

A survey by the
Creditreform
Economic Research Unit

Creditreform

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■ 1 Introduction Corporate stability versus economic upturn?

The economic indicators in Western Europe are at green. Since summer 2003, the first signs of an upturn have been evident in Germany and the neighbouring countries. In the wake of the US recovery – but also in the shadow of the strong euro – industrial output in most Western European countries looks to be taking a positive course. But neither in Germany nor in Europe as a whole is the picture on the insolvency front anything like as bright. Even though the rise in the number of business bankruptcies is not as marked as it has been in recent years, the negative trend still continues. The collapse of the Parmalat group in Italy revealed once again that the mechanisms for supervising and assessing business companies are still far from able to prevent wheeling and dealing. Anyone with the requisite criminal energy and in the appropriate position in the corporate hierarchy can still send a company into bankruptcy, causing immense damage to creditors and shareholders alike. And in such cases, harm is caused not just by the direct losses in the form of bad debts but also by the impact on the confidence of investors and lenders. Nor is it just the big, spectacular collapses which have this effect – the large numbers of small and medium-sized enterprises going broke also help to create an adverse climate by suggesting that investment or granting credit is generally a risky business.

So improving stability and increasing the transparency of business companies with regard to their financial situation has to come high on the agenda that governs greater European coalescence.

Adding weight to this demand is the upcoming admission of several Central and Eastern European countries to the EU, in May 2004. Although these new members can claim to have functioning market economies, their institutional frameworks reveal quite a few weaknesses. Market entry and exit in these countries may well be governed by law, but there are “difficulties where practical implementation" is concerned, as a report by the German Finance Ministry puts it. Whereas in Hungary and Poland, the situation regarding commercial registers and the formal handling of new entries and closures is in balance, the Czech Republic and Slovenia reveal a need for action. In this survey, in line with a frequently expressed wish, the Creditreform Economic Research Unit has for the first time examined the insolvency picture in the future member states. This examination makes it clear that for reasons of social or economic policy, the relevant legislation is not applied rigorously in some of these countries. Firms which are over-indebted or actually insolvent by the relevant legal standards continue to operate and thus represent a danger for investors.

Nevertheless there are grounds for optimism – both regarding consolidation on the corporate front in the new EU member countries and also in respect of the future economic development of Western Europe.

■ 2 Insolvencies in Western Europe – Figures for 2003

In 2003, the number of business insolvencies in Europe continued to climb: the total was 157,138, which was 6,000 firms or 3.9 percent more than the year before (2002: 151,255).

In Germany, the percentage increase – at 5.5 – was above the average for the EU as a whole. 39,700 firms filed for bankruptcy, as against 37,620 in 2002.

Renewed increase

It should be noted that because of legal and cultural differences, insolvency figures in the various countries are comparable only to a limited extent. Spain provides an example: its insolvency volume is far below that in the other big European nations. This is due to the fact that in Spain a limited company can be set up without any major investment, and so if it becomes insolvent, it is not worthwhile to organise its liquidation – it remains in the commercial register as a "ruin". In this respectt, there is a similar situation in some of the future EU entrants.

Despite the fact that the economy has been picking up steam in many European countries, there are still no signs of a turnaround on the insolvency front. However, the rate of growth has slowed down: in 2002, the year-on-year increase in business collapses was 10.7 percent; last year's rise, at 3.9 percent, was 6.8 percentage points lower.

Tab. 1: Business insolvencies in Europe 2003 in comparison with 2002

■	2003	2002	Change in percent
Austria	5,564	5,281	+ 5.4
Belgium	7,463	7,222	+ 3.3
Denmark	2,465	2,469	- 0.2
Finland	2,810	2,885	- 2.6
France	40,472	37,987	+ 6.5
Germany	39,700	37,620	+ 5.5
Greece	480	489	- 1.8
Ireland	316	379	- 16.6
Italy	16,000	15,500	+ 3.2
Luxembourg	641	695	- 7.8
Netherlands	6,355	6,489	- 2.1
Norway	3,080	2,603	+ 18.3
Portugal	2,980	2,092	+ 42.4
Spain	545	629	- 13.4
Sweden	8,061	7,819	+ 3.1
Switzerland	4,539	4,002	+ 13.4
UK	15,667	17,094	- 8.3
Total	**157,138**	**151,255**	**+ 3.9**

Portugal with highest rate of insolvency growth…

The highest percentage rise in insolvent companies was posted by Portugal, where the figure was 2,980, an increase of 42.4 percent. Domestic demand in Portugal is weak, and has been declining since 2001, and this is forcing more and more companies – German companies among them – to withdraw from this market. The textile and garment industry has been particularly hard hit.

Second place in the list of the countries with the biggest growth rate is Norway, with a rise of 18.3 percent to 3,080 cases of insolvency. The economy of

Europe‘s biggest oil exporter has been going through a lengthy recession, from which it only started recovering in the third quarter of the year, Support came from private consumption, which has strengthened despite a high unemployment rate, and public-sector orders. Overall, though, this was unable to offset the negative effects of weak investment (with the exception of oil-related investment) and weak exports coupled with high imports.

Switzerland was another country with a double-digit rise in business bankruptcies. These were up by 13.4 percent (537 cases) to 4,539. In the middle of last year, Switzerland emerged from its previous recession, and in Q3 exports grew faster than at any time for about a year – and exports account for almost half of Swiss GDP. But there is always a delay between economic recovery and any fall in insolvency figures, which explains why business bankruptcies continued to climb at a rate that is out-of-the-ordinary in this Alpine country.

... while the Emerald Isle is booming

At the other end of the scale came Ireland: the Emerald Isle was able to cut its business insolvencies by 16.6 percent to 316. This was lower than in just one big German city: Düsseldorf, for instance, recorded 480 business failures in 2003. Thanks to low rates of taxation, the “Celtic Tiger” has evolved in the past 30 years from the EU’s poorest country to one of the most favoured locations for foreign companies. From the German angle, and against the background of the sinsolvency situation in this country, Ireland’s economic framework appears exemplary. There are just two rates of private income tax: 22 and 41 percent, capital gains tax has been halved to 20 percent, while corporate income tax – the important factor for investors – is just 12.5 percent. But revenues from this tax have increased eightfold since 1990.

Two of the European “big five” countries, Spain and the United Kingdom, also posted significantly lower business insolvency figures. In the United Kingdom, there was a fall of 8.3 percent to 15,667 (2002: 17,094). Spain registered just 84 fewer cases, but in view of the low absolute total of insolvencies, this was a decline of 13.4 percent.

Tab. 2: Insolvencies in Europe 1998 - 2003

■	Absolute						Changes in percent				
	2003	**2002**	**2001**	**2000**	**1999**	**1998**	**02/03**	**01/02**	**00/01**	**99/00**	**98/99**
Austria	9,944	9,047	8,777	9,006	8,934	7,319	9.9	3.1	- 2.5	0.8	22.1
Belgium	7,463	7,222	7,062	6,791	7,150	6,925	3.3	2.3	4.0	- 5.0	3.2
Denmark	2,465	2,469	2,189	1,732	1,586	1,800	- 0.2	12.8	26.4	9.2	- 11.9
Finland	2,810	2,885	2,793	2,908	3,080	3,136	- 2.6	3.3	- 4.0	- 5.6	- 1.8
France	40,472	37,987	34,876	37,449	41,186	55,000	6.5	8.9	- 6.9	- 9.1	- 25.1
Germany	99,800	84,330	49,510	41,780	33,870	33,977	18.3	70.3	18.5	23.4	- 0.3
Greece	480	489	591	636	694	871	- 1.8	- 17.3	- 7.1	- 8.4	- 20.3
Ireland	316	379	427	344	815	686	- 16.6	- 11.2	24.1	- 57.8	18.8
Italy	16,000	15,500	15,200	15,000	14,760	15,000	3.2	2.0	1.3	1.6	- 1.6
Luxembourg	641	695	750	597	545	423	- 7.8	- 7.3	25.6	9.5	28.8
Netherlands	8,537	8,297	5,832	3,726	3,920	5,031	2.9	42.3	56.5	- 4.9	- 22.1
Norway	5,324	4,473	3,541	3,576	3,342	3,347	19.0	26.3	- 1.0	7.0	- 0.1
Portugal	2,980	2,092	1,594	1,308	999	783	42.4	31.2	21.9	30.9	27.6
Spain	545	629	335	602	620	896	- 13.4	87.8	- 44.4	- 2.9	- 30.8
Sweden	8,666	8,387	8,012	7,301	7,261	9,200	3.3	4.7	9.7	0.6	- 21.1
Switzerland	9,679	8,802	8,145	8,300	8,490	8,850	10.0	8.1	- 1.9	- 2.2	- 4.1
UK	53,640	50,895	48,397	47,404	46,900	37,500	5.4	5.2	2.1	1.1	25.1
Total	**269,762**	**244,578**	**198,031**	**188,460**	**184,152**	**190,744**	**10.3**	**23.5**	**5.1**	**2.3**	**- 3.5**

Private bankruptcies exceed business insolvencies

Not all countries have a procedure allowing private individuals to file for bankruptcy. In Germany, the law on consumer insolvencies, introduced in 1999 and amended at the end of 2001, has led to a huge, growing volume of such cases. The table above shows all insolvencies, i.e. including “non-business” bankruptcies in those countries where there the relevant legislateon exists: Germany, the United Kingdom, Switzerland, Austria, Sweden, Norway and the Netherlands. Although in France, too, private individuals can seek debt forgiveness, the procedure is completely different from that applied in corporate bankruptcies and there are no statistics on the relevant figures.

The total number of insolvencies in Western Europe in 2003 increased by 10.3 percent to a new high of 269,762. The figure the year before was 244,578. The increase was fuelled particularly by Germany and the

United Kingdom. In Germany, the total rose to 99,800, 18.3 percent more than in 2002. The United Kingdom registered 53,640 insolvencies, an increase of 5.4 percent. In both these countries, and in Austria, Norway, Sweden and the Netherlands, the rise in private bankruptcies was greater than that in business insolvencyes.

Switzerland bucks the trend

In Switzerland, the opposite was true. There, business collapses were up by 13.4 percent to 4,539, while private bankruptcies rose by 7.1 percent to 5,140.

If the number of business insolvencies is set against the number of firms in that country, Spain comes out best, with just two cases for every 10,000 companies. In second place in 2003 was Greece, with 6, followed by Ireland, with 33.

At the other end of the list are Austria, with 247 insolvencies for every 10,000 firms, Sweden with 299, and Luxembourg with 321.

The Western European average is 79 insolvencies for every 10,000 firms.

Germany was in the middle of the list for West Europe, with a ratio of 136 firms for every 10,000.

Tab. 3: Insolvency ratios in the individual Western European countries

■	Insolvencies per 10,000 companies
Spain	2
Greece	6
Ireland	33
Italy	39
Portugal	44
UK	45
Netherlands	115
Germany	136
Belgium	137
Denmark	137
Switzerland	142
Finland	144
France	163
Norway	176
Austria	247
Sweden	299
Luxembourg	321
Total	**79**

■ 3 Insolvencies in Germany

Economic growth in Germany was significantly below the EU average and was in fact negative for the first time since 1993. With a fall of 0.1 percent, it dropped even below "the bottom horizon of expectation", as Johann Hahlen, president of the German Federal Office of Statistics, put it. He saw this as being due in part to the general decline in the global economy and uncertainty among consumers and business companies. But there is light at the end of the tunnel, he believes, and forecasts positive growth of 1.5 to 2.0 percent in 2004. These hopes are based mainly on exports, which is dangerous, though, since the stronger euro is making German goods more expensive in important overseas markets.

Tab. 4: Insolvencies in Germany

■	2003	2002	Change in %
Total	99,800	84,330	+ 18.3
Companies	39,700	37,620	+ 5.5

Germany posts new insolvency record

The number of insolvencies in Germany reached a new record in 2003: altogether, 99,800 companies and private individuals filed for bankruptcy. Compared with the year before (2002: 84,330) that represents an increase of 18.3 percent. 39,700 business companies went broke, a year-on-year increase of 5.5 percent (2002: 37,620). For the second time running, the number of private bankruptcies was higher than the business insolvency total: 60,100 consumers and self-employed persons turned to the insolvency courts in an effort to rid themselves of their debts. That is 28.7 percent more than in 2002.

Fall in business failures in Eastern Europe

Business insolvencies grew at a slower rate than in the two previous years. But it is too early to speak of any reversal of the trend. In the past ten years, insolvencies have more than doubled. Last year, the rise was fuelled by Western Germany, where 29,700 companies had to make their way to the insolvency courts, 11.9 percent more than in 2002. In Eastern Germany, insolvency figures are actually falling: 10,000 firms applied for bankruptcy, a drop of 9.7 percent.

Where private bankruptcies are concerned, the growth was higher in Eastern Germany, with an increase of 34.7 percent to 13,900, as against a 27.0 rise in Western Germany to 46,200.

Last year, the total damage which insolvencies caused to business companies, private individuals and the public sector amounted to 40.5 billion euros. The relevant figure in 2002 was 38.4 billion euros. More than two-thirds of this damage affected the private sector: lenders, suppliers and the employees of bankrupt firms suffered damage totalling 27.9 billion euros. The impact on the public sector was 12.6 billion euros.

The number of insolvency-related job losses last year was 613,000, an increase of 3.9 percent on 2002.

In 2002, the insolvency scene was distinguished by the collapse of numerous large companies and corporate groups, and 2003 also saw several tradition-rich companies affected, such as Grundig, Wienerwald, Kettner and, not least, Aero Lloyd. However, there were no business insolvencies on the scale of those the year before. This present year got off to a bad start, though, when coachwork-builder Kögel, another well-known German company, had to file for insolvency.

■ 4 At the core of the problem: Financing

There are some 20 million firms in Western Europe. Of these just 65,000 employ more than 250 people. So the corporate landscape is dominated by small and medium-sized enterprises (SMEs). Many of these regard access to financing as a problematic area. Banks are changing their financing strategies, and not just because of Basel II – they are shaking out their credit files and reducing risks in order to improve their earnings situation.

But other factors also influence the ability of SMEs to obtain funding for their operations. The overall framework plays a decisive role in generating business stability – or triggering insolvency. One quarter of all bankruptcies by European companies are caused by late payments. In August 2000, the EU directive on delayed payment came into force as a step towards counteracting this factor. The directive is aimed at protecting business companies, especially SMEs, from the substantial administrative and financial burdens caused by excessively long payment periods and belated payments.

Tab. 5: Payment conduct in Europe in days

■	Payment terms	Payment delay	Total
Italy	64 (66)	21 (21)	85 (87)
France	45 (46)	11 (10)	56 (56)
Belgium	40 (39)	23 (22)	63 (61)
UK	30 (31)	25 (23)	55 (54)
Austria	27 (27)	12 (10)	39 (37)
Sweden	26 (26)	10 (8)	36 (34)
Netherlands	25 (26)	20 (20)	45 (46)
Germany	24 (23)	16 (17)	40 (40)
Switzerland	23 (22)	15 (14)	38 (36)

( ) = 2002

No relief from new laws

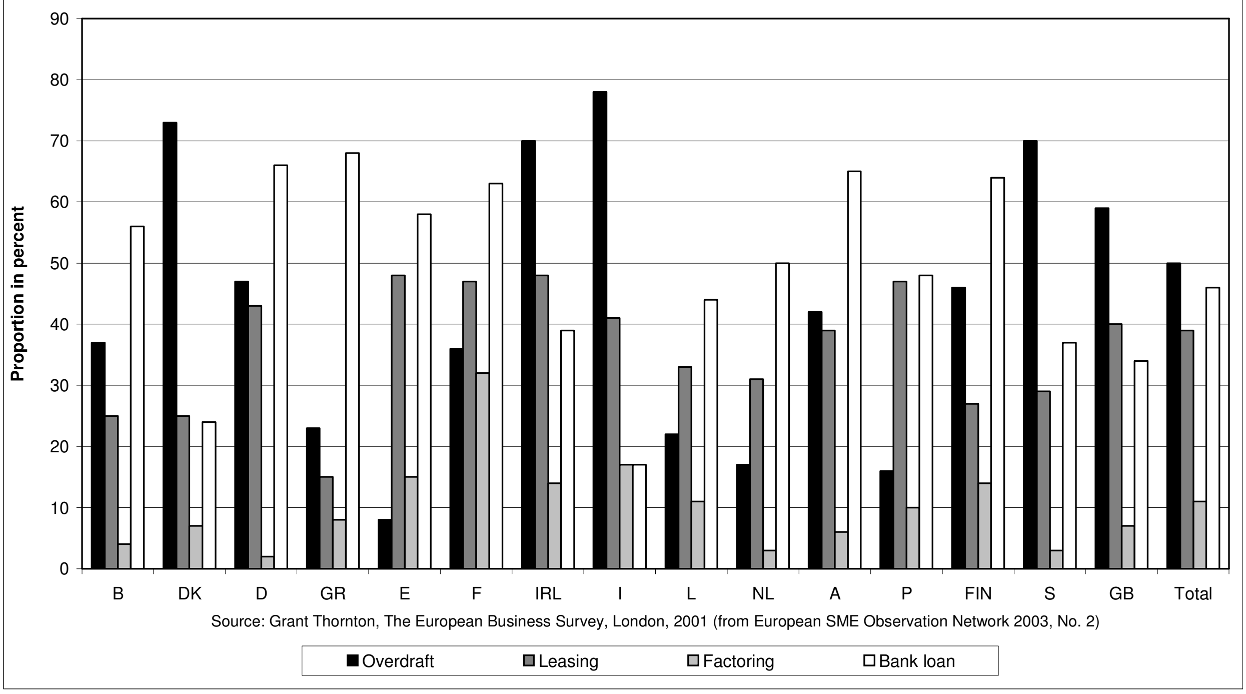
On September 30, 2002, the European Commission filed a complaint against seven member states for not implementing the directive. Thereupon, Austria and Italy converted it into national law, but this has still not been done in Spain, Greece, Portugal, the Netherlands or Luxembourg.

However, even in those countries where the directive has been given legal force, not much has happened yet. Companies still have to wait too long for their money. Particularly in Italy, France and Belgium, invoices take a long time to settle: in Italy almost three months (85 days), in Belgium more than two months (63 days) and in France on average 56 days.

SMEs generally finance their activities via banks, by means of loans and overdraft facilities. A survey by Grant Thornton showed that 41 percent of European SMEs have lines of credit at just one bank, almost a third at two or three banks and five percent at more than three.

In view of the changes in the financial sector, banks will in future require SMEs to provide greater transparency about their financial situation. Within the next few years, one minimum requirement will be for firms to submit their balance sheets to any bank where they obtain loans or the like. A study by the ENSR Enterprise Survey shows that up to now only around 60 percent of all SMEs in Europe regularly let their bank have their profit-and-loss statements or balance sheets. The readiness to provide information varies with the size of the company concerned. One third of all firms with up to nine employees do not provide their bank with any information at all. According to the ENSR, readiness to submit information to banks has increased in the past few years, particularly in Spain and Luxembourg.

Proportion of SMEs in Europea with outside financing (15 countries)



Source: Grant Thornton, The European Business Survey, London, 2001 (from European SME Observation Network 2003, No. 2)

Among European SMEs, the use of supplier credits is wide-spread. In Denmark, Ireland, Italy, Sweden and the United Kingdom in particular, they play a more important role than bank loans. However, for the credit-receiver they represent an expensive form of financing, because the supplier adds on his financing costs and a risk surcharge. Often the supplier offers a rebate for prompt payment but if this is not used, it represents an additional cost factor. Because of liquidity bottlenecks, many SMEs in Europe are not in a position to pay their suppliers before they have been paid by their custumers – often a vicious circle.

Alternative forms of financing for SMEs: leasing and factoring

For SMEs, one alternative form of financing is leasing and this used particularly by companies in Spain, France, Luxembourg, the Netherlands and Portugal.

Unlike an investment financed by a loan, leasing does not bind any capital and therefore improves liquidity and extends the financial scope of the company concerned. Another positive factor is that it generally does not necessitate any additional form of security, since the leasing company remains the owner ofwhatever has been leased.

Factoring is becoming increasingly important in Europe. Between 2000 and 2001, turnover in this field increased by 15 percent to 474 billion euros. The highest increase was posted in Spain (plus 300 percent) and Greece (plus 547 percent). On average, 11 percent of European SMEs make use of factoring but the actual proportion differs considerably from one country to another. In France, for example, 32 percent of all SMEs take advantage of factoring, whereas in Germany and Sweden the figures are just 2 percent and 3 percent respectively.

■ 5 Insolvencies and the economy

All hopes rest on 2004 – hopes that Europe’s economy will pick up steam, that unemployment will fall and that private individuals will consume more. But there is a problem: the strength of the euro.

One prerequisite for a healthy boom on the domestic front and for a revival of private demand is cutting unemployment and creating new jobs. But Julian Callow of Investment Bank Credit Suisse First Boston (CSFB) warns against over-optimism about reducing unemployment: “The situation won’t get any better, it will just no longer worsen so severely”. An analysis of job ads in the most important national newspapers in Germany, France and the United Kingdom carried out by French bank Société Générale shows that the demand for personnel is close to its lowest point in 10 years. Bijal Shah of SG thinks that this is due not just to weak economic activity but also, and chiefly, to globalisation. “The main reason for the low level of demand for employees in the Western industrialised countries is that the Western demand for goods is increasingly being met by Asian nations.” In other words, he says, industrial jobs are being moved to Asia on a massive scale. A survey of 7,000 industrial companies by the DIHK, the umbrella organization of the German chambers of industry and commerce, confirms this. It shows that one company in every four intends to move at least parts of its production abroad in the next few years in order to avoid the disadvantages of manufacture in Germany. If this trend intensifies, the hoped-for upturn could take place without invigorating the labour market – there would just be what the Americans call a jobless recovery.

Insolvency makes 1.7 million people jobless

In 2003, the unemployment rate in the EU was 8.4 percent. 1.7 million jobs were lost as a result of businesses going bankrupt, a rise of 100,000 on the year before. But at least that is a lower rate of growth than in 2002, when the year-on-year increase in insolvency-related job losses was 200,000.

Tab. 6: Insolvency-related unemployment in Europe

■	**Number of jobs lost (in millions)**
1997	1.8
1998	1.6
1999	1.4
2000	1.1
2001	1.4
2002	1.6
2003	1.7

In some of the big countries of the eurozone – Germany, France and Italy – industry started gathering momentum again in the fourth quarter of 2003, with a rise in output and new orders. In parallel, the contribution made by manufacturing companies to the insolvency total fell by 1.2 percentage points to 11.2 percent.

Tab. 7: Insolvencies in the main branches of the economy in Europe in 2003 (average)

■	Share of total volume
Manufacturing	11.2 (12.4)
Construction	20.6 (21.4)
Commerce	25.3 (25.6)
Services	42.9 (40.6)

Figures in percent, ( ) = 2002

Service firms generate biggest rise in insolvencies

Whereas commerce and the construction sector were able to cut their contribution to the insolvency total slightly, by 0.3 and 0.8 percentage points respectively, the share accounted for by service-providers in Europe increased by all of 2.3 percentage points, with the figure up from 40.6 to 42.9 percent.

In November 2003, personnel downzsizing in the services sector in the eurozone came to a halt. Previously, since summer 2002, this sector had dismissed more employees than it recruited new ones, as is shown by the Reuters purchasing manager index for the service sector. This sector depends strongly on domestic demand and particularly in Germany this is sluggish.

Tab. 8: Insolvencies in the main branches of the economy 2003

■	Manufacturing	Construction	Commerce *	Services
Belgium	8.3 (9.9)	13.9 (18.5)	32.3 (41.4)	45.4 (30.2)
Denmark	10.7 (9.2)	12.6 (10.8)	42.5 (19.4)	34.2 (60.5)
France	11.3 (12.7)	23.3 (21.7)	26.4 (26.3)	39.0 (39.3)
Germany	9.1 (10.5)	20.7 (23.1)	23.7 (23.2)	46.4 (43.2)
Netherlands	13.9 (13.6)	15.5 (14.3)	22.4 (26.9)	48.2 (45.3)
Norway	10.9 (11.2)	10.9 (10.4)	32.1 (35.5)	46.0 (43.0)
UK	18.7 (30.0)	21.9 (23.6)	19.1 (19.6)	40.3 (26.8)

*) including catering, figures in percent, ( ) = 2002

Not all countries provide detailed information on the development of insolvencies in the main sectors of the economy but generally speaking there are considerable differences between the different countries. In

Norway, the contribution made by the construction sector is just 10.9 percent – in France, Germany and the United Kingdom it is over 20 percent. In Denmark, 42.5 percent of all insolvencies originate in the field of commerce; in the United Kingdom the figure is just 19.1 percent. On the other hand, Denmark has the lowest insolvency volume in the services sector, with just 34.2 percent of the overall total, while in the Netherlands this sector contributes almost half of all business bankruptcies (48.2 percent).

■ 6 National reports

6.1 The United Kingdom

The United Kingdom (England, Wales and Scotland) appears to be mirroring the way insolvencies in the United States have developed: business insolvencies are lower while consumer bankruptcies are on the increase. Where the overall total is concerned, the United Kingdom posted a rise for the fifth time in succession by 5.4 percent to 53,640. The figure for business insolvencies took the other direction, with a fall of 8.3 percent to 15,667.

Tab. 9: Insolvencies in the United Kingdom

■	2003	2002	Change in %
Total	53,640	50,895	+ 5.4
Companies	15,667	17,094	- 8.3

British economy stabilizing

In the final quarter of last year, the British economy picked up considerably. In the first half, the UK's export performance had been the lowest among the G7 nations, then in November the Bank of England cut the key interest rates (by 0.25 base points) for the first time in almost four years. The United Kingdom has the most consumption-oriented population. The unemployment rate fell in the second quarter to 5.0 percent. Although industry reduced its job total of four million by 200,000. the services sector and the public sector took on new staff. According to a study by the Mori opinion research institute, Britain is nonetheless becoming less attractive as a location: 60 percent of top managers expect to see the situation in British industry deteriorate in the next five years. The main reason cited is the high level of taxation, which is almost on a par with that in Germany. In addition, wage and salary costs are leading to jobs being exported – not just in the low pay sector but increasingly also in the field of more highly qualified work. So where the ongoing stability of British business companies is concerned, there are justified doubts.

6.2 Italy

Business insolvencies in Italy are still on an upward course. Last year they rose by 3.2 percent to 16,000 – a higher rate of growth than in the two previous years (1.3 and 2.0 percent respectively).

Tab. 10: Business insolvencies in Italy

■	2003	2002	Change in %
	16,000	15,500	+ 3.2

Italy provided last year's biggest business scandal. In December, it was revealed that dairy group Parmalat had been fudging its books. An account in the Cayman Islands allegedly holding 3.95 billion euros proved non-existent. Parmalat founder Calisto Tanzi was arrested on charges of defrauding the company of around 10 billion euros and falsifying balance sheets ever since 1988. Public prosecutors are currently investigating whether international banks, rating agencies or auditors were involved in this massive fraud. An Italian bankruptcy court declared Parmalat insolvent. This gives the company a breathing space, by allowing it to concentrate of settling current invoices rather than paying off past debts.

In the meantime, the Italian government has promised help for thousands of farmers. They are to be granted favourably priced loans to offset the losses caused by unpaid bills.

Italy and Parmalat

The Italian economy is weak anyway and prices have been rocketing. In the first half of 2003, the average Italian family had to pay 274 euros more on food than the year before. The Milan economic research institute puts the average rate of inflation in 2003 at 2.7 percent. But then there is also the “perceived” increase in prices, a phenomenon similar to that in Germany. According to the ISAE research institute, Italians are afraid that the situation will get even worse. And this result dates from September, i.e. before the Parmalat scandal.

6.3 Spain

In Spain, insolvencies are traditionally at a low level. However, this has less to do with the country’s economic performance than with the legal prerequisites for liquidating a company. Following a record low in the field of business insolvencies in 2001, with 335 cases, the figure started growing again. But 2003 brought a renewed fall, of 13.4 percent to 545 companies, in line with Spain’s flourishing economy.

Tab. 11: Business insolvencies in Spain

■	2003	2002	Change in %
	545	629	- 13.4

Spain is booming

And in Spain, the economy really is booming. This year the Spanish government expects to see 3.0 percent growth and the creation of around 300,000 jobs. The upturn in Spanish GDP is due on the one hand to strong domestic demand and on the other to the buoyant construction sector. The government in Madrid is investing a lot of money in the country’s infrastructure. In the period 2000-2007, it has earmarked some 114 billion euros for improving the rail network, roads and airports. This program is also receiving funding from Brussels. In addition, Spanish building contractors are benefiting from the still high demand for housing. Although housing prices have risen in the last twelve months by 17 percent, low interest rates are encourageing many Spaniards to buy their own homes. To offset the impact of the higher prices of property, Spanish banks offer mortgages of up to 30 years, thus keeping monthly payments low. The Spanish Central Bank has called for more caution in granting loans, but the banks are delighted to see their mortgage volume registering increases of up to 20 percent.

One weak point in the Spanish economy is research and development. Here Spain is one of the tail-enders in the EU. And the unemployment rate is significantly higher than the average for the eurozone (11.3 percent as against 8.4 percent) – this is despite the fact that substantial reform efforts have helped to create new jobs.

6.4 France

France posted 40,472 business bankruptcies in 2003, a rise of 6.5 percent. This puts France above Germany both where the rate of growth is concerned and also in respect of the absolute total.

But the economic indicators for this coming year point upwards. Since Q3 2003, the French business community has been exhibiting optimism. According to figures published by the Insee statistics office, the business mood index for the manufacturing sector rose from 95 points in October to 100 points in November. It estimates that GDP could increase in 2004 by up to two percent, with the upturn in the global economy fuelling higher exports and more investment and also invigorating the labour market.

Tab. 12: Business insolvencies in France

■	2003	2002	Changes in %
	40,472	37,987	+ 6.5

In 2003, France almost suffered the biggest businesss collapse in Europe. In July, the Alstom group, which manufactures turbines and high-speed trains and employs 85,000 people, sounded the alarm bells. It had accumulated debts of 5 billion euros against equity of under one billion euros. In September, the group was saved by means of a spectacular rescue plan: together with the French government, banks and other business companies presented a concept to inject a volume of 8.2 billion euros into Alstom in the form of cash and guarantees. Since some 1.9 billion euros of this is being borne by the state, the European Commission is still examining whether or not this represents a forbidden subsidy.

In the meantime, Alstom's order book situation has improved, but analysts warn that that the company's financial problems have not been solved yet. In France, Alstom has a status comparable to that of Siemens in Germany. It was involved in the construction of the TGV and the luxury liner Queen Mary 2.

■ 7 The Eastern enlargement of the EU: Future members

On May 1, 2004, ten further countries will be admitted to the EU. They are Poland, Hungary, the Czech Republic, Slovakia, Slovenia, Estonia, Latvia, Lithuania, Malta and Cyprus. Bulgaria and Romania are set to follow in 2007. Just when Turkey joins the EU has not been decided yet.

The financial package agreed on for the ten new members has a volume of 40.85 billion euros, of which Poland will get about half. Following their admission all ten new member states will be net recipients.

The economic situation in the new member states of Central and East Europe is relatively good. Their average economic growth in 2002 was higher than that of the 15 present EU members. For 2003, the forecast was for GDP growth of 3.4 percent, fuelled particularly by strong domestic demand created by public investment and higher wages.

The drawback is that the expansive fiscal policies have had a negative impact on the budgetary situation in many of the future member states; reducing the deficits will probably have a curbing effect on further demand. In addition, these countries have to cope with high unemployment rates, worsening current account balances and stagnating direct investment.

Although the future EU members from Central and Eastern Europe are all considered functioning market economies, they will have to step up their reform efforts even further. In several of these countries, the institutional framework leaves something to be desired. Company start-ups and market departures are regulated by law but in some countries, such as the Czech Republic and Slovenia, practicial implementation of the regulations is still uncertain, especially where company closures are concerned.

In most cases, there is still no functioning insolvency legislation backed by appropriate authorities. For this reason, violations of insolvency law are seldom penalized. As a result, there are many companies still active in the market which are in fact insolvent and thus in a position to trigger bad debt losses.

Tab. 13: Business insolvencies in Eastern Europe 2003 in comparison with the previous year *)

■	**2003**	**2002**	**Change in percent**
Czech Republic	4.000	4.002	- 0,05
Hungary	7.718	6.240	+ 23,7
Latvia	986	902	+ 9,3
Lithuania	589	798	- 26,2
Poland	1.076	1.238	- 13,1
Slovakia	5.554	6.263	- 11,3
Slovenia	1.555	1.408	+ 10,4
Total	**21.478**	**20.851**	**+ 3,0**

*) unfortunately, no figures are available for Estonia

Now a look at the business insolvency situation in the future Eastern European member states: last year the number of business insolvencies increased by 3.0 percent to 21,478, after 20,851 the year before. But in fact, for the reasons stated above, these figures probably represent only the tip of the iceberg: many companies which by Western standards are already bankrupt simply go on operating.

The extent of the problem varies. According to the German Finance Ministry, company closures are inadequately regulated particularly in the Czech Republic and Slovenia. But there are also still shortcomings in connection with firms entering or leaving the market in Slovakia, Latvia and Lithuania, despite some progress in this respect. In this sphere, Hungary, Estonia and Poland are considered more advanced.

The relative incidence of insolvencies also varies strongly: In Slovenia, for instance, 243 out of every 10,000 firms went bankrupt in 2003 as compared with just three in Poland.

Tab. 14: Insolvency rates in the individual Eastern European countries *)

■	Insolvencies per 10,000 companies
Poland	3
Czech Republic	17
Lithuania	46
Hungary	90
Slovakia	104
Latvia	232
Slovenia	243
Total	**29**

*) unfortunately, no figures are available for Estonia

7.1 Poland

In Poland, the economy is picking up again after two years of stagnation. In 2002, GDP grew in real terms by 1.4 percent. The greatest dynamos of growth were domestic consumption and net exports. In the second quarter of 2003, GDP posted a substantial rise, of 3.8 percent. The estimates for 2003 as a whole are of three percent growth, mainly fuelled by exports because of the weakness of the zloty. In 2002, inflation declined and since the beginning of 2003 has remained at a low level at around 0.7 percent.

Despite the good data, more and more foreign investors are withdrawing from the country and the inflow of foreign direct investment has fallen since 2001. The country still suffers from high unemployment and a growing burden of debt. The reform efforts have also slowed down: privatizations have declined and structural reforms are being addressed only hesitantly. Moreover, there is a crisis in the banking sector, which has suffered as a result of the stagnant economy and an increase in non-performing loans. This in turn has let to more restrictive lending policies.

Insolvencies increasing

The number of insolvencies fell by 13.1 percent last year to 1,076. Compared with some of the other new members, the absolute total of insolvencies in Poland is relatively low. To an extent, though, this is due to the difficulties in conducting insolvency cases. The present insolvency and liquidation regulations generate high costs, and because of their scanty resources, the courts implement them only inadequately.

Tab. 15: Business insolvencies in Poland

■	2003	2002	Change in %
	1,076	1,238	- 13.1

7.2 Slovakia

Flat-rate tax system

Slovakia comes in for considerable praise by economic experts for its structural reforms. In addition to reforming the social security system, the government has decided on a far-ranging fiscal reform and introduced a flat-rate tax system: income tax, corporate taxation and value-added tax are all 19 percent. The country is also hoping for positive impulses from amending its labour and social legislation.

Slovakia’s economy is developing steadily. In the first half of 2003, GDP growth in real terms was 3.9 percent (2002: 4.4 percent). In the past few years, growth has been based above all on increasing domestic demand and the inflow of foreign direct investment (2002: 17 percent of GDP). However, in 2003, the investment boom weakened somewhat. Unemployment is still at a relatively high level; in the first six months of 2003 it fell slightly, from 18.6 to 17.7 percent.

The number of business insolvencies in Slovakia declined last year by 11.3 percent from 6,263 to 5,554. The new insolvency stipulation that the debtor is obliged to apply for bankruptcy or seek a settlement if his over-indebtiness lasts for more than 60 days has not yet had any impact. This is despite the fact that non-compliance can trigger sanctions under criminal law.

Tab. 16: Business insolvencies in Slovakia

■	2003	2002	Change in %
	5,554	6,263	- 11.3

7.3 Slovenia

Stable growth

Economically and politically, Slovenia is the most stable of the new member states. At close on 14,000 USD, its per capita income is far higher than that in the other new entrants. Slovenia's most important economic partners are Germany, France and Italy – but their current economic weakness made real-term growth in Slovenia fall last year to an estimated 2.4 percent, after 3.2 percent in 2002. This year, though, researchers expect to see it rising again, to 3.5 percent.

Compared with Slovakia, Slovenia's reform efforts are less radical and leave room for substantial improvement. The EU Commission's Monitoring Report highlights the particular need for action in the field of privatization and in overcoming old, monopolistic structures.

Business insolvencies in Slovenia rose from 1,408 in 2002 to 1,555, an increase of 10.4 percent. Slovenian insolvency law is based on that in Germany and Austria. In actual practice, however, enforcing the collection of outstanding accounts is severely hampered by the extremely long time the procedure takes – a situation under which business companies still suffer.

Tab. 17: Business insolvencies in Slovenia

■	2003	2002	Changes in %
	1,555	1,408	+ 10.4

7.4 Czech Republic

In the Czech Republic, economic growth is relatively stable. In the second quarter of 2003, it reached 2.1 percent and for the year as a whole, a figure of 2.5 percent was expected. In 2002, growth had been fuelled mainly by public and private-sector consumption, when wage increases lifted demand by private households by 4 percent. In view of the strength of the Czech koruna, exports made only a minor contribution to growth.

Growth fuelled by vigorous demand

The situation regarding public finances is not so good. In 2002, the budget deficit was 3.9 percent of GDP, in 2003, it is likely to have risen to 6.7 percent.

In Czech Republic, the process of privatization is progressing only hesitantly. But the government has amended the commercial code and is drawing up new bankruptcy legislation. Special training courses are being held for judges and bankruptcy administrators with the aim of ensuring that distressed companies are restructured or liquidated faster than in the past.

Tab. 18: Business insolvencies in the Czech Republic

■	2003	2002	Change in %
	4,000	4,002	- 0.05

Business insolvencies in the Czech Republic fell by 0.05 percent to 4,000. In fact, though, since the relevant current legislation does not function so well in practice, the true number of insolvencies could be higher.

7.5 Hungary

The economic situation in Hungary worsened somewhat in 2003. Following GDP growth of 3.3 percent in

2002, the rate in the first half of last year was 2.6 percent. In this export-oriented country, growth is generated by greater private demand subsidized by public funds. In 2002, for instance, private consumption rose by 9 percent. The price to to be paid for this was an expansion of the budget deficit to 9.1 percent. In 2002, foreign direct investment fell to 13.8 percent of GDP, and in the first half of 2003, this negative trend actually intensified.

Less direct investment

The overall economic framework, though, has been improved by a cut in interest rates, a reduction of the public-sector deficit and reticence on the wages front.

In line with the weaker economic development, the number of insolvencies in Hungary rose from 6,240 in 2002 to 7,718 last year, an increase of 23.7 percent.

Tab. 19: Business insolvencies in Hungary

■	2003	2002	Change in %
	7,718	6,240	+ 23.7

7.6 The Baltic states: Estonia, Latvia and Lithuania

The Baltic states of Estonia, Latvia and Lithuania have been enjoying strong economic growth and largely balanced state budgets but have also had high current account deficits. Despite uneasy political conditions, all three countries have passed important structural reforms in the past few years.

In **Estonia**, economic growth in 2003 is estimated to have been 4.5 percent, the lowest rate of growth in the Baltic states. Nonetheless, according to Deutsche Bank, Estonia has good chances of joining the European Currency Union at a relatively early stage. The country’s current account deficit, at 14 percent of GDP, was very high, due to extensive imports of machinery and equipment which will ultimately be reflected in the form of improved productivity.

The highest rates of economic growth of all the new member states are reported by **Latvia** (6 percent) and **Lithuania** (8 percent). Their current account deficits are lower, but so too is the proportion of funds they spend on the imports of machinery. In both countries, internal domestic political tension is impacting negatively on the readiness of outside business companies to invest. In Lithuania in particular, the political scene is dominated by corruption scandals and political rivalries which tend to scare off investors.

Baltic states: Highest growth rates

One positive feature is that the Lithuanian government is still pursuing its reform course. Good progress is being made, for instance, in the privatization of previously state-owned companies. And the legal framework for dealing with insolvencies and corporate restructuring has been improved, with stipulations intended to make market entry and exit easier. In 2003, business insolvencies in **Lithuania** sank by 26.2 percent to 589; in **Latvia** they rose by 9.3 percent to 986 (2002: 902).

Tab. 20: Business insolvencies in the Baltic States *)

■	2003	2002	Change in %
Latvia	986	902	+ 9.3
Lithuania	589	798	- 26.2

*) unfortunately, no figures are available for Estonia

■ 8 Insolvencies in Japan and the USA

8.1 Japan

The world’s second biggest economy is gradually recovering after decades of stagnation. Thanks to more investment by business companies and higher exports, the Japanese economy grew by a surprising extent between April and June. During that period, business firms invested 4.7 percent more than in the prior quarter. This suggests that the long period of cost-saving and restructuring is paying off. Instead of losses, the big companies are now earning more than they have been for a long time and are reinvesting part of their profits. Demand from abroad – in particular from other parts of Asia – also encourages investment.

And even consumers, who were long reticent to spend money, are now stepping up their expenditure again slightly. For an economy which has gone through three recessions and deep-reaching structural crises, with growth averaging barely more than one percent, the present results are notable.

Japan: Fall in number of bankruptcies

Tab. 21: Business insolvencies in Japan

■	2003	2002	Change in %
	16,855	19,458	- 13.4

In 2003, insolvency figures in Japan declined by 13.4 percent, following a 4.7 percent increase the year before: in 2002, 19,458 firms filed for bankruptcy, last year's figure was 16,855.

However, in the coming months it remains to be seen whether these positive figures point to any real recovery in Japan's economy. At present, the high volume of non-performing loans is holding banks back from granting credit, while the ongoing fall in prices increases the real-term debt burden of business companies and restricts the scope for monetary policy.

8.2 USA

The number of business insolvencies in the USA has been in decline since 2001 and is now below the total in Germany: in 2003, 35,454 companies filed for bankruptcy, a fall of 8.0 percent.

Tab. 22: Insolvencies in the USA

■	2003	2002	Change. in %
Total	1,688,285	1,577,651	+ 7.0
Companies	35,454	38,540	- 8.0

Fewer business bankruptcies in the USA than in Germany

9,805 firms underwent restructuring under the provisions of Chapter 11, a stipulation aimed at granting distressed companies a breathing space in which to make themselves fit for business survivaö – the principle of saving a "going concern" wherever possible. If the reorganization then proves successful, the company can repay its debts from its future earnings. If not, it can re-apply for Chapter 11 protection or be liquidated. At any rate, last year the American economy suffered no business collapses on the scale of those in previous years.

Tab. 23: The 10 biggest insolvencies in the USA since 1980

■	**Business sector**	**Date of insolvency**
Worldcom, Inc.	Telecommunications / IT	21.07.02
Enron Corp.	Energy facilities / transport	02.12.01
Conseco, Inc.	Insurance	18.12.02
Texaco, Inc.	Refineries / petrochemicals	12.04.87
Financial Corp. of America	Financial services	09.09.88
Global Crossing Ltd.	Telecommunications	28.01.02
United Airlines Corp.	Civil aviation	09.12.02
Adelphia Communications	Telecommunications	25.06.02
Pacific Gas and Electric Co.	Utility	06.04.01
Mcorp	Bank / financial services	31.03.89

The US economy is in optimistic mood and in the third quarter of 2003 grew at a faster rate than at almost any time in the past 20 years. This growth was driven mainly by consumers, who spent more money than expected. A contribution to this was made by tax reductions and low interest rates. Private expenditure rose by 6.9 percent. The other side of the coin: 2003 also brought an increase in the number of over-indebted consumers taking advantage of the opportunities offered by American insolvency law: more than 1.6 million private individuals applied for the chance of making a fresh start without debts. This represents a rise of 7.4 percent.

■ 9 Summary

The economic signals in Europe point to green, and since last summer things have been moving generally upwards. So all hopes are staked on 2004. On the insolvency front, on the other hand, the negative development is continuing – perhaps not so marketly as in recent years but all the same we are far removed from any trend reversal in the field of insolvencies.

In 2003 157,138 companies in Western Europe filed for bankruptcy. This was almost 6,000 firms more than the year before, a rise of 3.9 percent. However, this means that the growth rate on the insolvency front has slowed down: in 2002, the year-on-year figure was up by 10.7 percent; last year's increase was 6.8 percentage points lower. The rise in Germany – with 39,700 companies having to make their way to the bankruptcy courts – was 5.5 percent, higher than the EU average.

The unemployment rate in the EU last year was 8.4 percent. Insolvency-linked job losses totalled 1.7 million, an increase of 100,000 on the year before, representing a rise of 6.3 percent.

The largest percentage rise in business insolvencies was posted by Portugal, where the total number of firms going bankrupt was 2,980, an increase of 42.4 percent. Second place in this "negative chart" was taken by Norway, where the figure rose by 18.3 percent to 3,080; Norway's economy has been going through a long recession from which it only started recovering in the third quarter of the year. A double-digit rise in business insolvencies was also reported by Switzerland. The increase there was 13.4 percent, to take the total to 4,539.

At the other end of the scale came Ireland: the Emerald Isle was able to cut its business insolvencies by 16.6 percent to 316. Spain and the United Kingdom could also point to a substantial fall. In the U.K. the number declined by 8.3 percent to 15,667 (prior year: 17,094). In Spain, 84 fewer companies than the year before had to make their way to the insolvency courts; in view of the low absolute number of insolvencies (2003: 545), this represented a drop of 13.4 percent.

The total number of insolvencies in Western Europe, i.e. including both business insolvencies and private bankruptcies (as far as these are statistically recorded), rose by 10.3 percent to 269,762. This rise was due particularly to higher figures in Germany and the United Kingdom. In Germany the overall insolvency total increased by 18.3 percent to 99,800; in the U.K. by 5.4 percent to 53,640.

When the relative incidence of insolvency is concerned (i.e. the number of cases per 10,000 companies), the best performance was by Spain, where only two firms in every 10,000 went broke in 2003. In Greece, the relevant figure was six and in Ireland 33. The biggest number of insolvencies per 10,000 business companies was registered by Luxembourg, with 321; it was followed by Sweden with 299. Germany was in the mid-field of this list, with 136.

Despite the efforts made by the European Union, which in August 2000 had issued a directive on payment delays, actual payment conduct in Western Europe has not changed much. The directive has still not been turned into national law in all the member states, and even in those countries which have implemented it, business firms still have to cope with tardy payment. It is in Italy where firms have to wait longest for their money: there, it takes an average of 85 days before the invoiced amount is credited to the recipient's account. The fastest country is Switzerland, where firms pay their bills on average after 38 days.

SMEs in Western Europe finance their operations mainly by means of bank loans and supplier credits. Particularly in Denmark, Ireland, Italy, Sweden and the United Kingdom, supplier credits, even though these are very expensive, play a more important role than bank loans. Leasing is used especially by companies in Spain, France, Portugal, Luxembourg and the Netherlands. Factoring as an alternative form of financing is becoming increasingly important in the entire EU zone, with firms in Spain and Greece in particular making growing use of it.

The biggest contribution to the insolvency volume in Western Europe in 2003 was made by the service sector, which accounted for 42.9 percent of the total (prior year: 40.6 percent). Manufacturing made up only

11.2 percent of all business bankruptcy cases (prior year: 12.4 percent). But the distribution varies considerably from country to country. In Norway, for instance, the construction business accounts for just 10.9 percent of all insolvencies, whereas in Germany, France and the United Kingdom, the figure is over 20 percent. In Denmark, 42.5 percent of all business insolvencies are in the field of commerce; in the U.K., the relevant proportion is just 19.1 percent.

In Germany, the rate of growth on the business insolvency front has eased: the 5.5 percent rise in 2003 was preceded in 2002 by a year-on-year increase of 16.1 percent. The rise was fuelled by firms in Western Germany, where 29,700 companies filed for bankruptcy last year (11.9 percent more than in 2002). In Eastern Germany, the development was in the opposite direction: just 10,000 companies went bankrupt, 9.7 percent fewer than the year before. The number of jobs lost or under threat through insolvency in Germany as a whole totalled 613,000 in 2003, 23,000 up on 2002.

For the first time, Creditreform also surveyed the insolvency situation in the countries which will be joining the European Union. Most Eastern European countries do not yet have fully functioning insolvency codes with relevant law-courts and appropriate experience, but they do have an upward trend in the number of firms going bankrupt. Last year, the total number of business insolvencies in the seven countries surveyed – Poland, Czech Republic, Lithuania, Hungary, Slovakia, Latvia and Slovenia – increased by 3.0 percent, from 20,851 cases in 2002 to 21,478. Although the figures in some countries were down – in Lithuania by 26.2 percent and Poland by 13.1 percent – there were also marked rises, such as in Hungary (up 23.7 percent) and Slovenia (up 10.4 percent). Just as in Western Europe, the relative incidence of insolvencies (insolvencies per 10,000 companies) varied strongly: the figure for Slovenia, for instance, was 243 as opposed to just three in Poland.

In Japan, the number of insolvencies declined by 13.4 percent last year, with bankruptcy affecting 16,855 firms, compared with 19,458 the year before. In 2002, the figure was still on an upward course, with a rise of 4.7 percent. Last year's figure shows that economic recovery in Japan is already having an impact on the insolvency front.

In the USA, the situation split two ways: business insolvencies were down, the number of private bankruptcies increased. In 2003, just 35,454 business firms (fewer than the German total of 39,700) filed for bankruptcy, a year-on-year decline of 8.0 percent. On the other hand, at over 1.6 million, the number of cases of private bankruptcy in the United States was extremely high.

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