Coface economic publications

panorama

Study on the status of insolvencies in Romania for 2013

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1. SUMMARY

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According to the preliminary data published by BIP (Bulletin of Insolvency Proceedings) and based on Coface methodology, in 2013 26,372 new insolvency proceedings were initiated, with approximately 2% more than during the previous year (25,842 insolvency proceedings). **The data from this study is preliminary, and the final data will be confirmed by the end of the first quarter of the current year.** Based on its own computations, Coface estimates that the actual number of newly-initiated insolvency proceedings during 2013 is approximately 27,145, with an actual increase around 5%, compared to the previous year. The initiating pace of these proceedings accelerated during Q4, the increase being triggered by the negative effect conveyed by the insolvency of a record number of medium and large companies, and probably also by the intention of certain companies to "rush" the insolvency initiation in the context of imminent changes within the insolvency procedural code. Thus, the preliminary data shows a 12% increase of insolvencies initiated during Q4 of 2013, compared to the same quarter of the previous year, and Coface's estimations concerning the final data place the increase to be more than 20%.

…but what lurks behind the figures? The negative effects are significant and will impact the private economy!

In the current context, the numerical evolution of the new insolvency proceedings becomes relevant solely from a statistical point of view, even though in Romania the phenomenon is a wide one, under the circumstances of a decrease by 20% or even 30%. The numerical evolution can be expressed both in absolute and relative values, by reporting to the practice of other European countries.

Even though the quarterly frequency data related to the first nine months of 2013 showed a relative stagnation of insolvencies, the preliminary annual figures forecast a slight increase of newly-initiated insolvencies during 2013. Most alarming is that, in 2013, there was a record number of insolvencies among medium and large companies. The number of companies with a turnover higher than 1 MEUR, which became insolvent during 2013, is 718, compared to a level of 485 insolvencies within the same category registered during 2012. Chapter three details all the issues related to this risk.

Which are the reasons that determine such evolution?

After the analysis of the financial data related to insolvent companies, in correlation with the macroeconomic context and the noticed business practices between companies, we identified the following structural reasons, which generated the boost of this systemic risk in Romania:

- The increased importance of the commercial risk, based on a higher weight of receivables in circulating assets, according to the companies' balance sheet.
- The extended payment terms, based on a more aggressive increase of receivables, compared to the turnover dynamics. This shows a relaxation of the crediting terms between the private companies and their business relations with partners that show a higher risk. Thus, the companies that became insolvent during 2013 registered an 11% decrease of their turnover during 2012, compared to 2011, while the value of their receivables increased by 2%.
- The above mentioned trend is mainly noticed in the area of large companies, which had the capacity to take over the net creditor role in this loop of commercial transactions, where a record number of SMEs was affected by the insolvency during 2012.
- The higher level of arrears and their negative impact on the companies that work with the State.

- The more precarious status of the companies, from self-financing perspectives and a financial point of view, in the context of their eroded resources and also taking into consideration the financing restrictions of the last 3 - 4 years.

Switching from the macroeconomic to the microeconomic level and in order to gain a thorough image on the risk amplified by insolvency within medium and large companies, the financial statements related to the last four years prior to insolvency were analyzed for all the companies that initiated insolvency proceedings during 2013. Chapter four details all the issues related to the profit and loss statement (P&L) and the analyzed balance sheets.

An essential element consists of the fact that it was NOT the financial underperformance that caused these companies to cease their business (of course this mattered, but did not play a crucial role in determining the insolvency), but most likely the defective credit risk management decisions, the management of net treasury and the pertinent financing of the operating cycle, the lack of capitalization and the continuous process of disinvestment within the relevant companies.
As we will see at the analysis of chapter four, approximately one quarter of the insolvent companies in 2013 were profitable and registered a theoretically positive liquidity (positive working capital). But this is not sufficient, because both the working capital and the positive profit represent the weighting of future liquidities which, unless materialized [the inventory is not sold according to the expectations, the receivables are not collected on the maturity dates, the non-monetary part of the P&L (sales on credit, adjustments for amortization and depreciation etc.)], the company faces problems in fulfilling its due payment obligations (within due date).

Which is the impact of these insolvencies?

This is and will continue to be a major one, considering the record number of medium and large companies that became insolvent. The final part of chapter four analyzes this issue in detail and monitors two distribution channels of the negative shock:

- Financial plan - based on its own calculations and taking into consideration the insolvencies registered during 2013, Coface considers that debts of approximately 16 BRON (financial and commercial) remained uncovered. Approximately 40% of these had an impact on the banking system, and represent the main reason of increased ratio of bad loans granted to non-financial companies by 4 percentage points during the last year. The remainder of 60% will have an impact on the private partners, which, at their turn, may become unable to pay their debts to their suppliers, the domino effect being twice as fast (based on uncovered debts) as the one registered during the previous year.

- Social plan - the initiated insolvency of the 26,372 companies during 2013 determined the loss of approximately 100,000 jobs, of which more than 60% were concentrated in the following five sectors: The manufacture of textile products, clothing and footwear items; Constructions; Manufacture of chemical substances and products; Other personal services; Metallurgical industry. The social impact of the insolvent companies during 2013 is similar to the one registered by the companies that became insolvent in 2012, but with 41% higher compared to 2011.

How generalized is the risk? What shows the data based on nationwide extended samples?

In order to answer this question, two sources were analyzed, both able to confirm that the risk is a generalized one, and that the payment discipline degraded at the entire economy level. Thus, the two sources are:

A. The data centralized by NBR concerning the unsettled payment instruments reported to PIR (Payment Incidents Register) supports these signals, whereas the number of payment instruments registers a decrease, while the value of payment refusals as well as their average reach new maximum amounts, as we can see in the table below.

Total January - November	Total amounts of payment refusals	Number of incidents	Average value per incident	Amounts PIR %	Number PIR %	Average PIR%
Year 2013	8,654,763	145,657	59.42	8%	-14%	26%
Year 2012	8,000,695	169,590	47.18	38%	-6%	47%
Year 2011	5,779,567	180,283	32.06	19%	-44%	115%
Year 2010	4,843,915	324,815	14.91	-43%	-28%	-21%
Year 2009	8,526,167	451,008	18.90	129%	84%	24%
Year 2008	3,724,866	244,632.0	15.23			

Furthermore, we can notice that the value of payment incidents registered during the first 11 months of 2013 are with 2% higher compared to the similar period of time of 2009, where the average value of payment refusals is by 2.1 times higher. Irrespective of the underlying reasons (more balanced scenarios may exist, and show that the payment instruments were more rarely used in practice), the evolution is extremely worrying, because 2009 marked the most severe contraction of the local economy of the last ten years and the first year when the effects of the world crisis were locally felt.

B. The sample of companies analyzed by Coface through its business information division, namely 36,000 unique companies, with an aggregate turnover of approximately 180 BEUR, represents more than 70% of the turnover of all active companies at national level. The conclusions are:

- Approximately two thirds of the companies show an insolvency risk extremely high or significantly above the average
- More than half of the companies make payments at an extremely slow pace
- 4 out of 10 companies analyzed by Coface do not benefit from the credit limit, and for 3 out of 10 analyzed companies, the credit limit represents maximum 20% of the monthly turnover (while the average payment term is 60 days, the exposure in real time does not exceed 10% of the monthly turnover)
- Coface decreased the value of credit limits (namely the recommendations of suppliers' exposures to their customers) by 20%

The private environment - where to?

The last chapter analyzes this issue based on the ratio of forces between the companies that ceased their business and the newly-incorporated ones. The conclusions are again pessimistic:

- Even though the number of newly-incorporated companies remain constant during the first 11 months of 2013, these do not even cover half of the number of companies that ceased their business during the analyzed period of time.

- The companies that ceased their business in 2013:
  - have an average term of business of 11 years
  - represent 23% of all active companies at the end of 2012
  - cancel the entire added value brought to the economy by the companies incorporated during 2011 and 2012, as shown in the table below:

Companies that...	ceased their business in 2013	were incorporated during 2011 & 2012
Number	142,541	90,209
2012 turnover	50.4 BRON	42.4 BRON
Average number of employees registered in 2012	255,380	225,170
Aggregate value of debts	129 BRON	32 BRON
Value of immobilized assets	47 BRON	20.7 BRON

Source: Data processed by Coface

Thus, we consider that the relative stabilization of insolvencies newly initiated during 2013 becomes relevant only from a statistical point of view, whereas the main reason of concern consists of the insolvency faced by a record number of medium and large companies, the latter being able to generate a faster negative impact on the economy and harder to replace.

2. SECTORAL AND TEMPORAL DISTRIBUTION OF INSOLVENT COMPANIES

Coface Romania has conducted a new study on the evolution of the number of insolvencies in Romania, this time taking into consideration the new cases registered within the Bulletin of Insolvency Proceedings (BIP) during 2013[1].

According to the final data published by BIP and based on Coface methodology, during 2013, 26,372 new insolvencies were initiated, with approximately 2% more than during the previous year (28,842 new insolvency proceedings).

[1] See Methodology Remarks at page 31

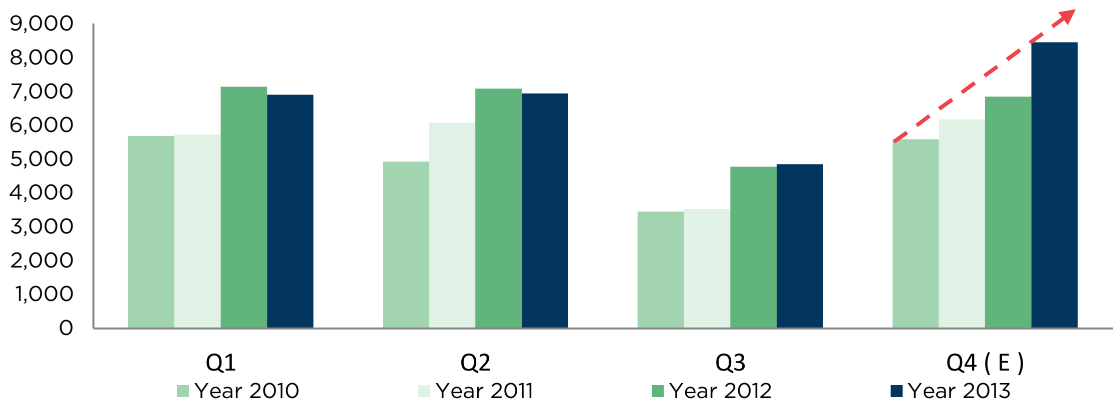
Table 1. Monthly evolution of insolvencies newly initiated during the last 3 years

Month	Year 2010	Year 2011	Year 2012	Year 2013
January	1,897	1,709	2,159	2,102
February	1,903	1,849	2,420	2,439
March	1,887	2,160	2,560	2,364
April	1,506	1,847	2,340	2,680
May	1,544	2,097	2,396	1,942
June	1,880	2,127	2,343	2,316
July	852	811	1,322	1,510
August	575	658	1,007	1,045
September	2,021	2,061	2,444	2,293
October	1,932	2,202	2,724	3,938
November	2,222	2,379	2,504	2,666
December	1,431	1,599	1,623	1,077
TOTAL (preliminary data)	**19,650**	**21,499**	**25,842**	**26,372**
Deviation (preliminary data)		9.4%	20.2%	2.1%
TOTAL Final (Coface Estimates)	**19,650**	**21,499**	**25,842**	**27,145**
Total Deviation (preliminary data)		9.4%	20.2%	5.0%

Source: BIP, Data processed by Coface

The data from this study is preliminary, and the final data will be confirmed by the end of the first quarter of the current year. The publication with BIP of the newly initiated insolvency proceedings may be subject to delays between one and four weeks. However, there are also retroactive amendments to the terms of insolvency proceedings, which can operate for 3 months prior to the initiating date. Based on the noticed historical deviations with monthly frequency, related to the last year, and based on its own computations, Coface estimates that the actual number of newly-initiated insolvency proceedings during 2013 is approximately 27,145, with an actual increase around 5% compared to the previous year. Even though the quarterly frequency data related to the first nine months of 2013 showed a relative stagnation of insolvencies, the preliminary annual figures forecast a slight increase of newly-initiated insolvencies during 2013.

Monthly evolution of insolvencies newly initiated between 2010 - 2013



This increase is mainly based on the more accelerated pace of newly initiated insolvencies during Q4 of 2013 and is assigned to the following factors:

- The chain conveyance of negative effects caused by the initiated insolvencies of a record number of medium and large companies, which determined the rapid generation of a financial and social shock, amplified within the private economy.
- The imminent announcement on the operation of the new insolvency procedural code, which also includes additional charging criteria for the debtor party. Thus, there might have been company directors that accelerated the steps related to the submission of the insolvency application in order to be governed by the former procedural code.
- Hereinafter, we will correlate the data provided by BIP with the financial statements submitted by the companies which became insolvent within MPF[2] in order to understand the structural elements which caused the cease of these companies' activity.

By comparing the data provided by BIP with the ones published by MPF, we can notice a gradual increase on the transparency degree registered by the companies which became insolvent. Thus, if less than 40% of the companies which became insolvent in 2010 and 2011, submitted their financial statements within MPF, this indicator increased to approximately 47% for the insolvent companies in 2012 and to 50% for 2013. Thus, we can appreciate that, in average, one of two companies that became insolvent submits the financial statements during the year prior to the insolvency initiation.

Table 2. Insolvent companies - financial statements within MPF

Total insolvencies 2013	26,372
of which submitted statements within MPF	13,063
Percentage	49.53%
Total insolvencies 2012	25,842
of which submitted statements within MPF	12,021
Percentage	46.52%
Total insolvencies 2011	21,499
of which submitted statements within MPF	8,153
Percentage	37.92%
Total insolvencies 2010	19,650
of which submitted statements within MPF	7,902
Percentage	40.21%

Source: MPF, BIP

Based on the financial statements submitted during the year prior to the insolvency initiation and depending on the main scope of business set out by NACE code, Coface distributed the companies that became insolvent to the 23 most important business sectors, the figures being shown in the following table.

[2] Ministry of Public Finance

Table 3. Sectoral distribution of insolvencies for the last 2 years

Business sector	Insolvencies 2013*	Insolvencies 2013 % Total	Insolvencies 2012*	Deviation 2013/2012	Insolvencies for every 1,000 companies
Retail	5789	22%	5,904	-2%	89
Wholesale and distribution	4508	17%	4,176	8%	95
Constructions	3771	14%	3,696	2%	133
Other services, provided mainly to enterprises	2130	8%	1,991	7%	60
Hotels and restaurants	1823	7%	1,844	-1%	114
Transportation	1720	7%	1,685	2%	76
Manufacture of wood and wooden products	900	3%	966	-7%	94
Agriculture	789	3%	654	21%	69
Manufacture of textile products, clothing and footwear	733	3%	783	-6%	147
Food and beverage industry	604	2%	647	-7%	102
Metallurgical industry	583	2%	560	4%	97
Other personal services	456	2%	421	8%	64
Real estate transactions	456	2%	538	-15%	63
Financial intermediations	339	1%	307	10%	81
IT	329	1%	329	0%	39
Recreational, cultural and sports activities	311	1%	285	9%	86
Manufacture of machinery and equipment	260	1%	281	-7%	58
Manufacturing chemicals	238	1%	224	6%	86
Sewage and waste disposal, sanitation and similar activities	180	1%	180	0%	85
Post and telecommunications	168	1%	101	66%	83
Health care and social security	113	0%	112	1%	20
Extractive industry	101	0%	114	-11%	121
Generation and provision of electrical and thermal energy, water and gas	71	0%	44	61%	132
Total	**26,372**	**1**	**25,842**	**2%**	**87**

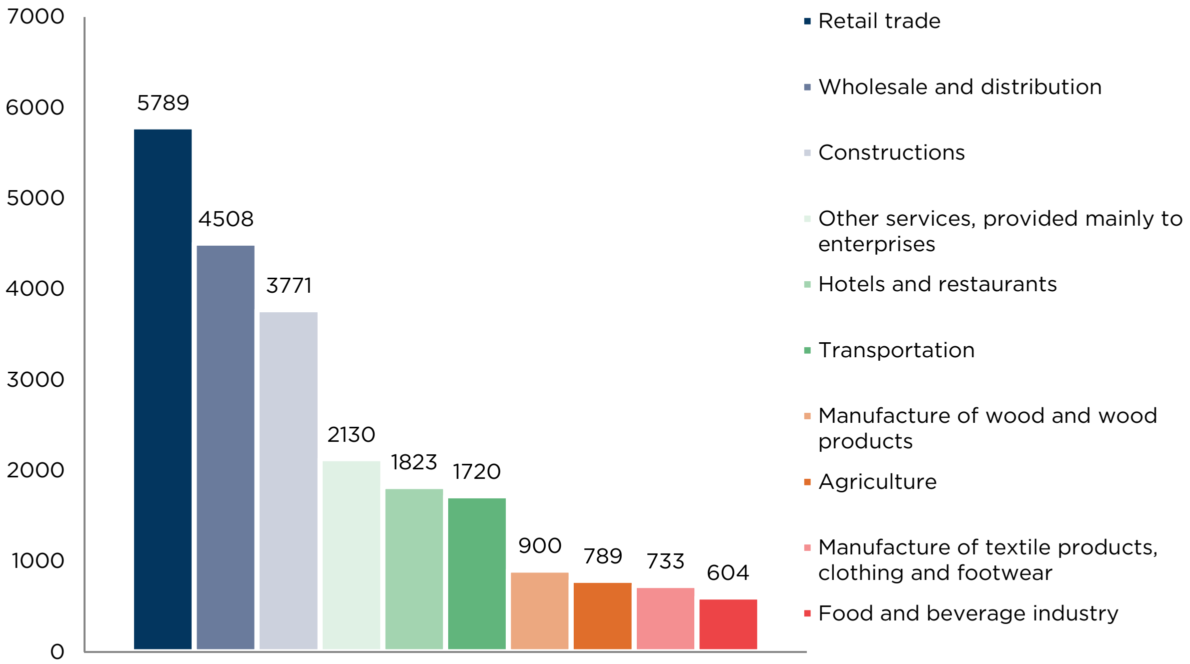
* Through linear extrapolation of the companies that submitted the financial statements within MPF during the year prior to the insolvency initiation. Were highlighted with red the first ten sectors that record the highest number of insolvencies per 1,000 active companies (only the companies that registered a turnover of more than EUR 1,000/month during 2012 were considered active companies).
Source: BIP, MPF

Even if we do not possess the information regarding the main activity for all companies which became insolvent during the analyzed period[3], there are two reasons based on which we estimate that the sectoral distribution at the level of the entire portfolio is similar to the one analyzed for the sample above, namely:

- The weight of the sample is significant from a statistical point of view for both years
- The weights of the sector distribution within the sample show values similar to the weights of the distribution at the level of the entire portfolio registered in the studies conducted by Coface for the last 3 years

[3] Such data can be computed for approximately half of the insolvent companies.

Top 10 sectors based on the number of insolvencies during 2013



Source: BIP, MPF, Data processed by Coface

In most studies conducted by Coface on the evolution of insolvencies, the first ten sectors which report the highest number of insolvent companies are unchanged, as the only modifications relate to the order in the standings, but with variations of one, maximum two positions.

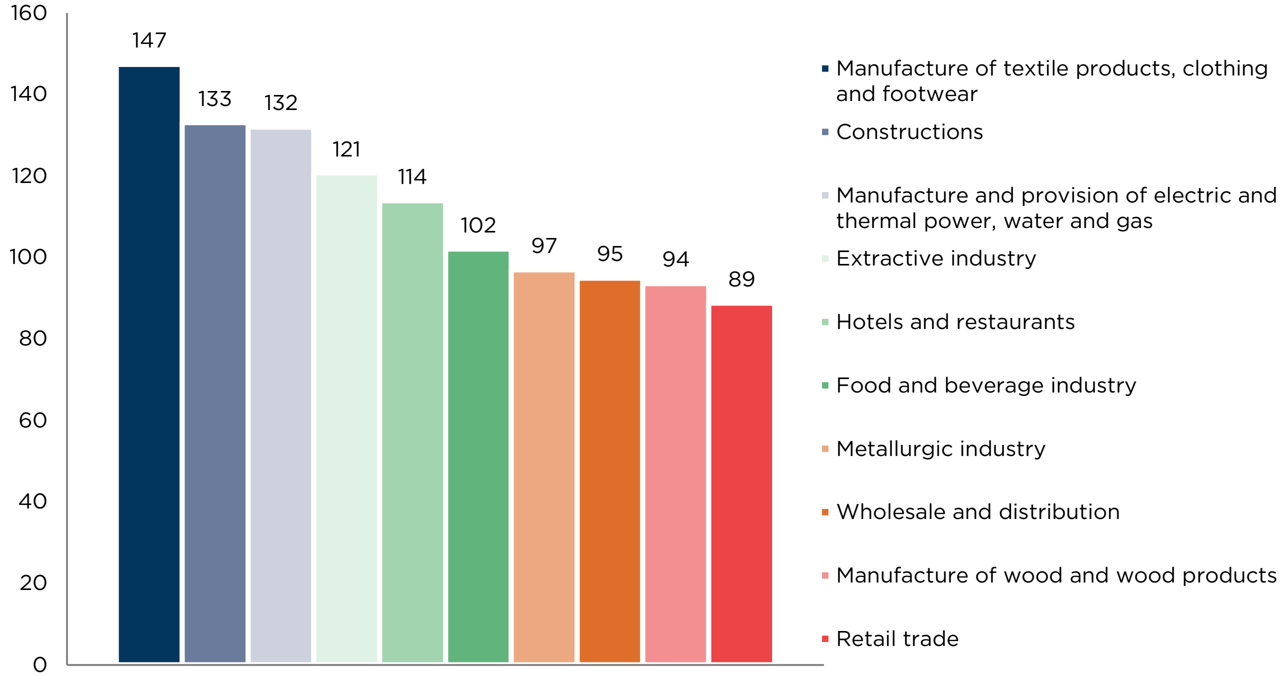
By analyzing the evolution of the pending insolvency cases over the last 5 years, we notice a tendency of consolidating the degree of concentration of volumes in the first 3 and 5 sectors. Thus, the weight of the first 3 sectors which reported the highest number of pending insolvency files in absolute numbers varied during the last 5 years between 50% and 54%, and the first 5 sectors between 65% and 70%.

These weights are not random and are determined by structural factors, such as the sectoral distribution of all active companies at national level. Thus, the first 5 sectors that register the highest number of insolvencies cover a similar weight regarding the total active companies. Taking into consideration this structural factor, it is important to analyze the number of insolvencies based on the number of total active companies[4] in the relevant sector.

Thus, the first ten sectors that register the highest values related to this indicator are mentioned in the following chart. We can notice that 5 sectors of the classification register values that exceed 100, which means that practically 10% of the active companies within the relevant sectors became insolvent.

[4] The "Active companies" category only included the companies with a registered turnover > EUR 1,000 / month during 2012.

Top 10 sectors based on the number of insolvencies during 2013, reported to 1,000 active companies



Source: BIP, MPF, Data processed by Coface

3. FINANCIAL AND SOCIAL DIMENSION OF INSOLVENT COMPANIES

In this section we analyzed the companies for which the insolvency procedure was opened during the last 4 years, based on the financial statements submitted within MPF one year before the initiation of insolvencies[5]. The classification of enterprises by size was performed in compliance with the provisions of Law no. 346/2004 on the encouragement of the development of small and medium enterprises, as subsequently amended and supplemented, which sets the criteria of including the companies in these categories. Thus:

- **Micro-enterprises** - have up to 9 employees and make a net annual turnover or own total assets of up to 2 MEUR, RON equivalent
- **Small enterprises** - have between 10 and 49 employees and make a net annual turnover or own total assets of up to 10 MEUR, RON equivalent
- **Medium enterprises** - have between 50 and 249 employees and make a net annual turnover of up to 50 MEUR, RON equivalent or own total assets which do not exceed the RON equivalent of 43 MEUR
- **Large enterprises** - have between 250 and 999 employees
- **Very large enterprises** - have over 1,000 employees

For the companies which have maximum 249 employees, exceeding one of the inclusion criteria triggers the registration of the company in the next category of size.

Thus, the most important financial indicators for companies that became insolvent during the analyzed periods of time are computed in the table below.

[5] For instance, the companies for which the procedure was opened during 2013 were analyzed based on the financial statements submitted within MPF for the activity carried out in 2012.

Table 4. Financial indicators for insolvent companies during the last 4 years

Indicator	Insolvencies 2013	Insolvencies 2012	Insolvencies 2011	Insolvencies 2010
Average turnover (RON)	1.9 MRON	1.4 MRON	1.3 MRON	1.5 MRON
Average Number of Employees	8.68	8.80	8.76	10.35
Average activity term (no. of years)	10	10	11	12
Net Loss % (of the turnover)	-9.49%	-15.03%	-16.90%	-17.17%
Indebtedness degree	104.24%	121.86%	131.89%	108.00%
Debts / Turnover	125.81%	169.61%	181.42%	137.93%
DSO (number of days)	152	187	199	178

Source: Data processed by Coface

Based on the financial information submitted within MPF for the activity carried out during the year prior to the insolvency initiation, we can notice:

- The average value of the turnover obtained by the companies which became insolvent during 2013 (further to the activity carried out in the year prior to the one in which the company became insolvent) is by 40% higher than the one of the companies which became insolvent during the same period of time of the previous year.
- The social dimension of the companies which became insolvent during 2013 is significantly higher than that of the insolvent companies of the previous year, these registering an average of 8 - 9 employees.
- At the same time, the average debts registered by insolvent companies during 2013 only accumulated 2.55 MRON/company, an ascending trend compared to the level registered by companies which became insolvent during the similar period of time of the previous years (2 MRON/company in 2012 and 2.3 MRON/company in 2011).
- Even if from a numerical point of view the weight of medium, large and very large enterprises accounted for only 3% - 4% of the total number of companies which became insolvent during the last 3 years, the weight of the turnover registered by them in the total turnover rose significantly, from 38% in 2011 and 55% in 2012 to 62% in 2013.
- The same trend can be noticed also for the weight of debts depending on the size category of insolvent companies. Thus, the weight of debts registered by medium, large and very large enterprises rose constantly in the last 3 years, from 30% in 2011 to 60% in 2013.

As we can see in the table above, most financial indicators related to the companies which became insolvent during 2013 are better than those computed for the companies which became insolvent during the same period of time of the last three years. This can be caused by the increasing weight of large and very large insolvent companies, because these already reached maturity in the context of an extended term of business (the average term of operation of these companies exceeds 10 years). Thus, we can notice a significant increase of the financial scale of the companies which became insolvent during 2013 compared to the previous year, which generated the increase of the turnover and debts of insolvent companies, but at the same time the decrease of loss ratio, indebtedness degree and DSO.

Taking into consideration the significant impact of large and very large companies on the consolidated financial indicators for the analyzed sample, it is important to determine these indicators solely for SMEs (including micro-enterprises). The related figures are computed again in the table below, and confirm the above mentioned structural issue, namely that more and more, the large companies become insolvent. This applies to all size categories and can signal an increasing systemic risk.

Table 5. Financial indicators for insolvent SMEs* during Q1 - Q3 of the last 4 years

Indicator	Insolvencies 2013	Insolvencies 2012	Insolvencies 2011	Insolvencies 2010
Average turnover (RON)	1,415,249	984,552	1,278,748	1,472,108
Average Number of Employees	7.06	7.73	7.90	8.80
Net Loss % (of the turnover)	-13.17%	-18.91%	-17.60%	-19.63%
Indebtedness degree	102.82%	109.15%	111.88%	106.89%
Debts / Turnover	137.84%	195.18%	188.76%	152.99%
DSO (number of days)	186	233	207	201

*Including Microenterprises

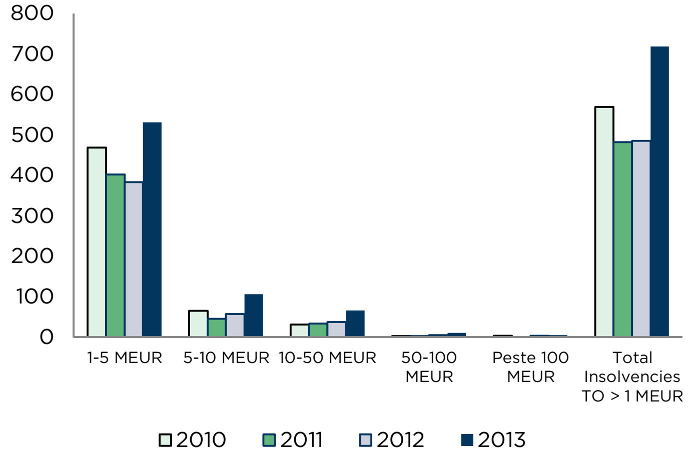
Source: Data processed by Coface

Following the analysis of the financial data related to insolvent companies, in correlation with the macroeconomic context and the noticed business practices between companies, we identified the following structural reasons, which generated the boost of this systemic risk:

- The increased importance of the commercial risk, based on a higher weight of receivables in circulating assets, in the companies' balance sheet.
- The extended collection terms, based on a more aggressive increase of receivables, compared to the turnover dynamics. This shows a relaxation of the crediting terms between the private companies, by means of business relations with partners that imply a higher risk. Thus, the companies that became insolvent during the previous year registered an 11% decrease of their turnover during 2012, compared to 2011, while the value of their receivables increased by 2%.
- The above mentioned trend is mainly noticed in the area of large companies, which had the capacity to take over the net creditor role in this loop of commercial transactions, and which were affected by the insolvency of a record number of SMEs during 2012.
- The higher level of arrears and their negative impact on the companies that still work with the State.
- The more precarious status of the companies, from self-financing perspectives and a financial point of view, in the context of their eroded resources and also taking into consideration the financing restrictions of the last 3 - 4 years.

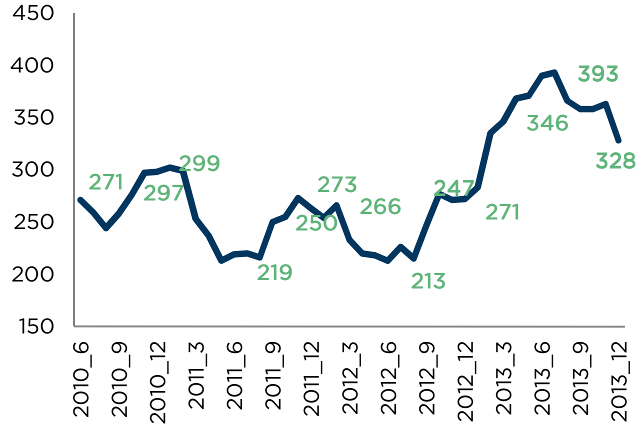
This phenomenon was flagged and analyzed by Coface in all its recent studies regarding the evoltuion of insolvencies. The trend is inflamed by a damaged payment discipline at the level of the entire economy, where the large and very large companies already have a higher sensitivity degree to their exposure to external or internal shocks, in the context of higher pressure on liquidities. This can be noticed in the graphic displays below, where we can notice that the number of companies with a turnover higher than 1 MEUR, which became insolvent during 2013, is 718, compared to 485 insolvencies within the same category registered during 2012.

Distribution of insolvent companies during 2010 - 2013 with a turnover above 1 MEUR



Source: BIP, Data processed by Coface

Number of insolvent companies with a turnover > 1 MEUR (mobile value 6 months)



Source: BIP, Data processed by Coface

The conclusions obtained from the analysis of the sample of companies which became insolvent during 2013 are confirmed by the tendencies noticed nationwide. The increased number of medium, large and very large companies which became insolvent determined the increase of the average value of payment incidents reported to PIR, based on an increased value of incidents and a decreased number of payment refusals (the large and very large companies may register a lower number of transactions, but with a much higher average value than the rest of the companies).

Also, according to the data published by PIR[6], the amounts refused for payment with debit instruments during the first 11 months of 2013 had a total worth of 8.6 BRON, rising by 8% compared to the same period of the previous year. While the number of payment incidents during the same analyzed term decreased by 14%, the average value of payment incidents increased by 26%. Thus, the average payment incidents registered between January and November, 2013 amounted to 59 KRON, compared to the level registered during the same term of the previous year, namely 47 KRON.

Furthermore, we can notice that the value of payment incidents registered during the first 11 months of 2013 is with 2% higher compared to the similar period of time of 2009, where the average value of payment refusals is by 2.1 times higher. Irrespective of the underlying reasons (more balanced scenarios may exist, and show that the payment instruments were more rarely used in practice), the evolution is extremely worrying, because 2009 marked the more severe contraction of the local economy of the last 10 years and the first year when the effects of the world crisis were locally felt.

[6] Payments Incidents Register, NBR

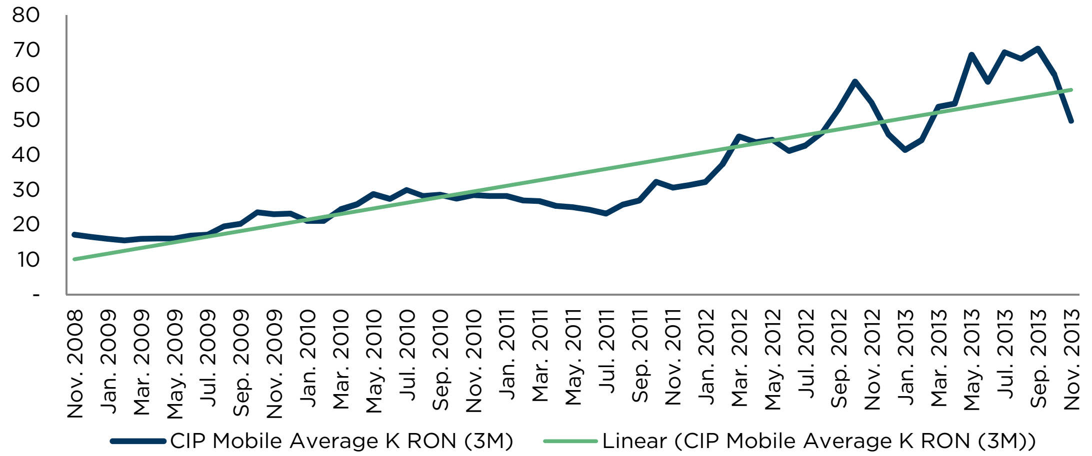
Table 6. Evolution of payment incidents reported by NBR

Total January - November	Total amounts refused for payment	Number of incidents	Average value per incident	Amounts CIP %	Number CIP %	Average CIP %
Year 2013	8,654,763	145,657	59.42	8%	-14%	26%
Year 2012	8,000,695	169,590	47.18	38%	-6%	47%
Year 2011	5,779,567	180,283	32.06	19%	-44%	115%
Year 2010	4,843,915	324,815	14.91	-43%	-28%	-21%
Year 2009	8,526,167	451,008	18.90	129%	84%	24%
Year 2008	3,724,866	244,632.0	15.23			

Source: NBR (PIR), Data processed by Coface, The figures are expressed in K RON

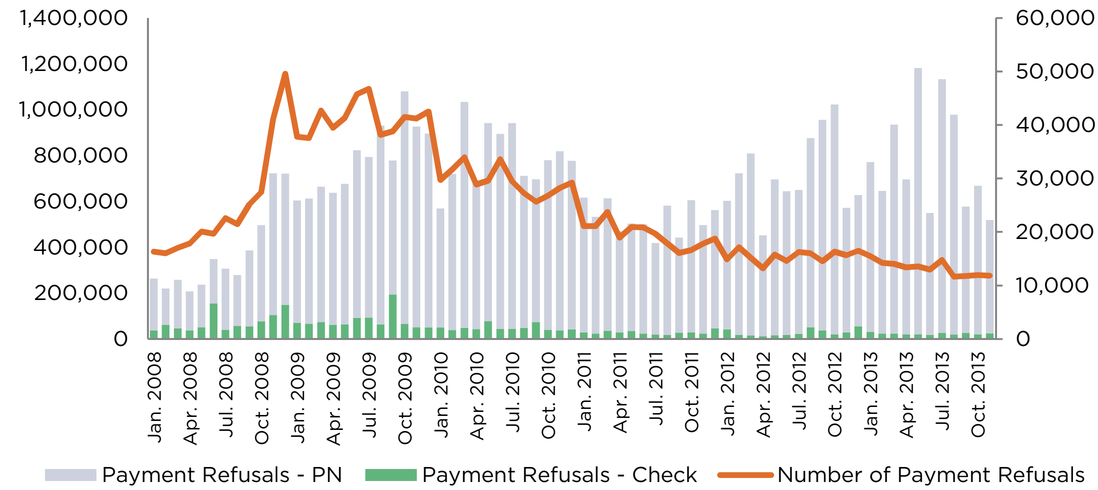
In line with the extension of the receivables collection term from economy, the tendency may indicate a deterioration of the payment behavior regarding the observance of debit instruments, which might cause the companies to require the partial or full payment in advance, in order to protect themselves against the commercial credit risk.

CIP average value (K RON)



Source: BIP, Data processed by Coface

Number of payment incidents and payment refusals (K RON)



Source: NBR, data processed by Coface
PN = Promissory Notes

4. EVOLUTION IN TIME OF INSOLVENT COMPANIES AND THE IMPACT ON THE ECONOMY

In this section we analyzed the consolidated financial statements for the last four full financial years related to the companies which became insolvent during 2013.

Thus, of all companies which became insolvent during 2013, 7,993 companies submitted their financial statements in the last 4 years[7], these accounting for 59% as numerical weight, but 70% as value weight (turnover), the sample being extremely relevant. The results are summarized in the table below.

Table 7. Financial indicators for companies insolvent during 2013 regarding the business carried out during the last 4 years

Indicator for insolvent companies during Jan - Sept 2013	Financials year 2012	Financials year 2011	Financials year 2010	Financials year 2009
Average turnover (RON)	2.4 MRON	2.7 MRON	2.5 MRON	2.3 MRON
Average Number of Employees	9.4	10.6	10.9	11.0
Net Loss % (of the turnover)	-9%	-6%	-7%	-6%
Indebtedness degree	104%	91%	87%	82%
Debts / Turnover	1.33	1.09	1.09	1.03
DSO (number of days)	142	122	121	101

Analyzing the evolution of the financial indicators of the last four years, we notice some structural causes which led to pressures on liquidities and payment default for the analyzed companies.

Thus:

- **The profit and loss account part** (P&L[8]) - except for some distortion of the results concerning the business of 2012, P&L shows no significant reasons of concern. The average value of the turnover remained relatively constant during the last 4 years, with an average value around 2.3 - 2.7 MRON. The 11% decrease registered in 2012 should not generate existential problems for such companies. The financial and operational leverage also remained unchanged during the analyzed period. Instead, the persistence of continuous losses during the last 4 years (and even the boost of these companies during 2012), in the context of a gradual increased indebtedness without a sufficiently strong capitalization, accelerated the end of these companies.

- **Balance sheet part** - here we can identify few structural problems which, in the context of performance challenged identified by P&L, amplified the problems of these companies:

[7] With respect to the activity carried out in 2009, 2010, 2011, 2012
[8] P&L = Profit and loss

- **Inappropriate turnover of current assets**. While the turnover decreased by 11% in 2012, compared to the previous year, the inventories decreased by only 6%, and the receivables increased by 2%. Such dynamics, corroborated with the decrease of deferred revenues (which would have represented additional liquidities), show a degradation of the quality of revenues, based on the faster increase of the non-monetary basis. Thus, the average collection term of receivables registered a constant increase during the analyzed period of time, from 101 days in 2009 to 142 days in 2012. The companies that registered the most abrupt degradation due to this reason were the companies with a turnover below 1 MEUR, which registered a 262 days DSO!

- **The increase of indebtedness degree up to non-sustainable levels.** Thus, the indebtedness degree[9] increased for the entire analyzed sample from 82% in 2009 to 104% in 2012. Obviously, such dynamics were registered based on the corresponding decrease of the capitalization degree, which shows that the shareholders failed to cover the losses accrued during the last 3-4 years by means of appropriate capital increases.

- **Divestiture** - it seems that the additional capital provided by creditors was not directed towards investments, whereas the long-term capital investment degree[10] registered a decrease from 62% (level registered in 2008) to approximately 49% (level registered in 2012). Thus, the long-term assets represented only half of the total debts accrued by these companies.

Dynamic indicators for the companies insolvent during 2013 - the dynamics of certain financial positions for 2011 - 2012, determined for the companies that became insolvent during 2013 **will confirm the acute problems related to the balance sheet, compared to the P&L one**.

Thus[11]:

- 3 out of 10 insolvent companies registered an increase of their turnover, while 5 out of 10 insolvent companies registered a decrease of their turnover by less than 25%. Out of the 8 companies of these categories, approximately two thirds registered a more accelerated increase of their receivables.
- 7 out of 10 insolvent companies registered a decrease of the book value of immobilized assets reported in 2012, compared to 2011. 5 of them register a constant contraction trend for the last four financial years.
- However, 6 out of 10 insolvent companies registered an increase indebtedness degree during the analyzed period of time, in the context of a decreased interest of the shareholders, by means of a decreased capitalization degree.
- 6 out of 10 insolvent companies registered an increase of the DSO during 2012, compared to 2011, while for approximately half of them the DSO increase was of more than 30 days.
- 6 out of 10 companies registered an elasticity of receivables to the turnover change, able to have a negative impact on liquidities. Thus:

[9] Overall debts (short-term + long-term) compared to overall assets
[10] Approximated based on the weight of immobilized assets in the overall assets
[11] The numeric weight (X of Y companies) was rounded to a round figure (rounded down; for instance 10.5 becomes 10).

- o 2.5 companies registered a slower decrease of receivables, in the context of decreased turnover, showing an average elasticity[12] of 0.4 (translated through the following correlation: on the 10% decrease of the turnover, the receivables decreased by 4%).
- o 2.5 companies registered an increase of receivables, in the context of decreased turnover, showing an average elasticity of -1.77 (translated through the following correlation: on the 10% decrease of the turnover, the receivables increased by 17.7%).
- o 1 company registered a more accelerated increase of receivables, compared to the turnover increase, showing an average elasticity of 2.94 (translated through the following correlation: on the 10% increase of the turnover, the receivables increased by 29.4%).

Whereas the dynamics of the average operating cycle[13] is similar to the one registered by the receivables evolution, the increased need of working capital financing became obvious. One of the common problems faced by insolvent companies was the lack of a long-term liquidity buffer (technically called working capital[14]), mainly caused by:

- The orientation of short-term financing resources, so that 8 out of 10 insolvent companies registered an increase of the short-term debts, in the detriment of the long-term debts during 2012, where 5 of them registered a constant such trend during the last 4 years. Furthermore, 75% of the insolvent companies have a weight of short-term debts in total debts higher than 80%.
- The gradual decrease of capitalization, where only 3 out of 10 insolvent companies registered an increase in absolute value of equity in 2012, compared to 2011. However, the increases were bashful, where only 1 out of the 3 companies registered equity increase of more than 10%.

As mentioned during the series of historical studies on the analysis of insolvency phenomenon, the status of theoretical bankruptcy of a company does not imply under any circumstances the market value of the assets (not even of the most marketable ones) in correlation with the total debts, but most likely shows the insufficiency of the current flow of liquidities, compared to the due obligations. Thus, notwithstanding the fraud or bad faith circumstances, the insolvency risk is amplified when the subject company shows the signs of an extremely scarce liquidity, as well as an uncertain horizon (or less predictable) on the continuation of its business[15] (which, most times, is highlighted by a main orientation of short-term debts, an extremely low capitalization degree, as well as by an extremely low weight of tangible immobilized assets in total assets, or at least way below the sector specific average; all these signs defining a circumstance where the exit strategy is significantly simplified).

In conclusion, it is obvious that the liquidity and systemic risk problems (in the context of initiated insolvency for a record number of medium and large companies, phenomenon that generated a negative effect with a rapid conveyance in the private environment) are those that boosted the insolvency risk, and that is why it is crucial to find a pertinent answer to the following question: **how can we quickly and correctly quantify („forward-looking") these signals concerning a scarce liquidity?** To this end, the financial analysis norms recommend two main directions:

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[12] The average elasticity was computed based on the formula ∆%Receivables/ ∆% Turnover, and by weighting the result for each company by the appropriate value of the turnover

[13] The average term of receivables collection + the average term of blocked inventory

[14] Working Capital = Permanent Capital – Long-term Assets, where Permanent Capital = Equity + Long-term debts

[15] "Going concern" - the principle according to which the company shall continue its business for an undetermined period of time

- **Analysis of the balance sheet** - where the most used indicator is the Current liquidity[16], which shows the extent to which a company can cover its short-term debts with its circulating assets. Positive figures show a positive working capital (or circulating capital), which is a requirement. However, figures highly exceeding the sector average show that too much capital is blocked in receivables and inventory, namely an increasing financing demand. However, a positive working capital (equivalent to a positive current rate) is not equivalent to an immediate, actual and guaranteed liquidity. Instead, this represents a weighting (in most cases, most likely) of future collection, to the extent the collections are collected and the inventory is sold.

  Thus, there are a series of reasons, including the factors set out below, that can decrease the probability of this weighting, such as:
  - Transformation of certain liquid receivables into doubtful receivables, to the extent they become old, in particular when the financial standing of the customers deteriorates and the reimbursement risk increases.
  - The inventories' aging or their perishable nature, which determines the decrease of the achievable value.

- **Analysis of the liquidity statement** - where one can see the net cash flows (collections minus payments) for all operational, financial or investment activities. The operational liquidities are of major interest because these represent the source of financial (reimbursement of the borrowed capital) and investment (immobilized assets) activities. Unfortunately, just few companies draft and submit these statements with the competent institutions, mainly due to legal mandatory requirements. Based on Coface estimates, only a number of 3,000 companies meet the requirements related to the mandatory submission of the cash flow statement[17]. From all indicators derived from the cash flow, the ratio between the operational liquidity and the short-term debts is the most eloquent in order to determine the extent to which the relevant company is able to generate sufficient liquidities from its main business in order to cover the debts due within less than one year. The financial analysis norms recommend that this indicator should be positive and with figures higher than 0.5.

Thus, the certitude degree of liquidity indicators determined based on the balance sheet is lower than that of the indicators determined based on the analysis of the liquidity statement, because these confirm the actual liquidity of a company during the financial year. Even though the latter is only available in an extremely low number of cases, the indirect method may be used in order to estimate the operational liquidity.

[16] Current liquidity = Circulating Assets/ Short=term debts.

[17] The entities that, on the balance sheet date, exceed the limits of two out of the 3 size-related criteria set out at art. 3 par. (1) of the Minister of Public Finance's Order no. 3.055/2009 on the approval of accounting regulations in line with European Directives, as further amended and supplemented, namely:

- **total assets: EUR 3.65 MIL;**
- **net turnover: EUR 7.3 MIL;**
- **average number of employees: 50,**

draft annual financial statements that include:

1. balance sheet (code 10);
2. profit and loss account (code 20);
3. statement on equity changes;
4. cash flow statement; - mandatory requirement for very large companies
5. explanatory notes to the annual financial statements.

Based on Coface's own computations, the indirect method was selected in order to determine the operational liquidity. Thus, out of the total number of 13,063 companies that became insolvent during 2013 and filed financial statements within MPF regarding the business carried out in 2012, a number of 6,729 companies show all financial information required in order to apply the indirect method in order to estimate the actual liquidity. Thus, as we can see in table 8, a total number of 2,013 companies (cells highlighted with red) registered a positive current rate (according to the balance sheet, we might appreciate that these companies had sufficient liquidities in order to cover the due debts), but out of these, 1,675 companies (approximately 83%) record negative values or values below the 0.5 level for the Actual Liquidity/Short-term debts indicator[18].

The figures confirm once again that actual liquidity problems may also exist in case of companies that apparently record a positive working capital, but the insolvency risk requires a more thorough analysis of the company's actual liquidities and that can be generated by the company during consecutive financial years.

Table 8. Correlation between Liquidity[19] vs. STD and the Current rate

CF: STD vs. Current ratio	BELOW 0.5	0.5 - 1	1 - 1.5	1.5 - 2	2 - 4	Over 4	NO STD	Total
NEGATIVE	1,418	854	484	161	209	170		3,296
BELOW 0.5	1,088	842	419	107	98	27		2,581
0.5-1	199	114	65	40	39	13		470
1-2	65	22	25	20	29	16		177
Over 2	24	15	9	2	28	52		130
NO STD							75	75
Total	2,794	1,847	1,002	330	403	278	75	6,729

Also, if a company is profitable, that does not mean that it shows a low insolvency risk. The net positive result (following the tax incidence) only represents a weighting of future liquidities, in the context where both the revenues and the expenses in the P&L consist of monetary and non-monetary elements. Thus, the insolvency risk is significantly determined by the extent to which the due debts are covered by available liquidities (certain, namely not potential or future), and the latter should preferably consist of liquidities form own sources (not borrowed). As we can see in the following table, 3 of 10 insolvent companies registered positive profits, but 80% of them registered a negative or insufficient cash flow, compared to the STD value. These companies are highlighted with red in table 9 and represent companies that prioritized the commercial result (quantity), in prejudice of the prudential one (quality).

[18] The short-term debts shall be abbreviated STD
[19] Liquidity shall be abbreviated CF (cash-flow)

Table 9. Correlation between Liquidity vs. STD and the Profitability of insolvent companies

Net result rate - CF: STD	NEGATIVE	BELOW 0.5	Between 0.5 - 1	Between 1 - 2	Over 2	NO STD	Total
BELOW -50%	1,187	579	92	23	16	21	1,918
-25% ~ -50%	437	288	46	16	4	10	801
0 ~ -25%	912	911	114	30	22	25	2,014
0 ~ 25%	591	686	160	71	48	13	1,569
25% ~ 50%	78	71	36	24	19	2	230
Over 50%	91	46	22	13	21	4	197
Grand Total	3,296	2,581	470	177	130	75	6,729

In conclusion, in order to summarize the answer to the previously raised question ["**how can we quickly and correctly quantify („forward-looking") these signals concerning a scarce liquidity?**"], we have the following comments:

- The liquidity of a company is a complex issue, which cannot be quantified by means of an immediate analysis of the current rate or profits. As noticed, approximately one quarter of the companies insolvent in 2013 were profitable and registered a theoretically positive liquidity (positive working capital). This weight is not sufficient, because both the working capital and the positive profit represent the weighting of future liquidities which, unless materialized [the inventory is not sold according to the expectations, the receivables are not collected on the maturity dates, the existence of non-monetary part of the P&L (sale on credit, adjustments for amortization and depreciation etc.)], the company faces problems in fulfilling its due payment obligations (on maturity).

- The quantitative part related to the development of a company (evolution of the turnover, profits) should not take precedence in the quantification of the insolvency risk, because the qualitative one plays a rather decisive role, through:
  - The analysis of the cash flow structure and its sources.
  - The quality of revenues, namely their persistence and sustainability - in other words, the answer to the question: how monetary and non-volatile are these revenues?

The impact of insolvent companies during 2013 is analyzed based on the two direct consequences: financial and social. Thus:

- **Financial impact**, approximated below by means of a simple cascade-type algebra computation:
  - In a scenario related to the next 3 years (following the foreclosure and capitalization process), the value of these companies' assets might be capitalized to approximately 50% of their book value (optimistic scenario).
  - In the same scenario, the accrued debts, of approximately 16 BRON [20] (financial and commercial) remain uncovered. The value is extremely high, where the balance of loans granted by the entire banking system to non-financial companies amounted to 116 BRON at the end of September, 2013.

[20] The amount is obtained like this: 25 BRON total debts of insolvent companies - 50% * 24 BRON total assets (out of which approximately 50% long-term, 48% circulating and 2% advance expenses).

- In average, 40% of these debts are to financial institutions, which means that approximately 6.4 BRON may represent losses of the banking system which, if 100% provisioned, would determine an increase of the bad loans weight (and, consequently, of the provision-related costs) by approximately 5 percentage points.
- The final result is in line with the evolution of bad loans weight registered by the banking system for the corporate portfolio, which increased from 17.3% (September, 2012) to 20.3% (June, 2013), namely by 4 percentage points[21].
- The other losses of 60% of the total debts (9.6 BRON) were borne by the private environment, and on the supplier-customer channel this determined the propagation of the negative effect to other companies as well, by means of the domino effect.

▪ **Social impact** - the initiated insolvency of the 26,372 companies during 2013 determined the loss of approximately 100,000 jobs, of which more than 60% were concentrated in the following five sectors: The manufacture of textile products, clothing and footwear items; Constructions; Manufacture of chemical substances and products; Other personal services; Metallurgic industry.
The social impact of the insolvent companies during 2013 is similar to the one registered by the companies that became insolvent in 2012, but by 41% higher compared to 2011.

5. MEDIUM AND LARGE COMPANIES UNDER COFACE'S MAGNIFYING GLASS

In its capacity as provider of integrated services related to the credit risk management, Coface Romania constantly supports the important role played by the proactive knowledge of financial statements of the business partners in the management of risks related to commercial transactions. This statement applies now more than ever, in the context of turbulent businesses felt as of the launch of financial crisis effects at local level, marked by a feeling of incertitude and multiple, complex and with a higher correlation degree risks. More than 70,000 companies became insolvent during the last 3 years, and the solvency of many companies was severely affected: industries that reported significant increases prior to 2008 further reported severe negative adjustments. If, prior to the crisis, the main target of many corporations was a quantitative one, marked by the increase of the market share and gain on competition, the current context is defined by an extremely different reality. In this new context, the knowledge of the financial standing of the main business partners is no longer an option, but a requirement.

Brief description of the methodology

The computation of the probability of the analyzed subject company to become unable to pay its debts during the next 12 months implies the use of 218 soft variables (related to the payment behavior and company description) and of 299 financial variables. The results obtained through the two categories of variables are further consolidated in order to generate a single risk indicator. Examples of used variables:

▪ **Qualitative** (Soft): the company's date of registration, legal form, location, development, carried out business (affiliation to a sector in order to determine the systemic risk), information concerning the shareholders and relations with other companies, information concerning the payment behavior, existence of collection cases (access and interconnection to/with the database of the collection department within the company, which provides information on the payment behavior of the investigated companies) etc.

[21] According to NBR

- **Financial**: are determined based on the available financial data (both the dynamics of balance sheet indicators in absolute figures and the computed indexes), for instance: dynamics of the turnover, of the fixed assets, equity and its components, liquidity, solvency, profitability or business indicators.

The final score (@rating score of the company) is obtained as a linear combination of the two scores, where the financial one has a weight of 0.7, and the qualitative one of 0.3. The **Coface @rating score benefits from the information acquired by the Insurance Department of Coface, which provides our analysts with additional information (most of the times confidential, which cannot be disclosed in the report) on the investigated companies**.

Classification of the @rating score into risk classes:

Insolvency/ Preliminary/ Debt regulation proceedings	Very High Risk			Medium High Risk		Low Risk				
0	1	2	3	4	5	6	7	8	9	10

@rating score: 1 - 3 (NIGA - Non Investment Grade Aggravated)

For the companies that belong to this risk class (NIGA) the investment, commercial insurance or provision of a commercial loan is not recommended. Due to this reason, the maximum value of the exposure recommended for such companies is always zero.

Generally, the companies that belong to this risk class (NIGA) show a descending evolution (abrupt) for several years in a row, a risky payment behavior (recent payment incidents, subject to banking interdiction, outstanding debts in our database), negative or extremely low equity (< 5% total assets), extremely low liquidity, are extremely small or negative information exist concerning the commercial insurance (confidential information that cannot be provided in the credit reports).

@rating score 4 - 5 (NIG - Non Investment Grade)

For certain companies that belong to this risk class, the investment is not recommended, but may be subject to a commercial insurance or commercial loan (cautious).

The companies with a scoring @rating 4 and 5 show both negative and positive aspects: descending trend, but good financial structure; debts to the budget, old incidents, recent collection cases, positively closed (the company paid the debts), negative capitals, but good evolution concerning the Profit and Loss Account.

@rating score 6 - 10 (IG - Investment Grade)

For the companies that belong to this class, the risk is considered as low. There will always exist a recommended commercial exposure for the scoring of this risk class.

During 2013, Coface Romania CMS individually analyzed, upon the request of the business partners or in order to monitor the direct exposures within the Insurance division, a number of 36,000 unique companies, with a total turnover of 180 BEUR, representing approximately 70% of the turnover of all active companies at national level. By analyzing the distribution of companies per risk areas, we can notice:

- 17% of the analyzed companies belong to the NIGA risk zone, namely a category regarding which Coface does not recommend a credit limit due to the extremely high insolvency risk.
- 46% of the analyzed companies belong to the NIG risk zone, the insolvency risk of these companies being above the average.
- Only 22% of the companies belong to the IG risk zone, category regarding which the insolvency risk is considered low.
- The remainder of 15% consists of companies that, on the moment when the analyze was performed, had either a filed insolvency claim filed and pending with the courts of law (in which case Coface provisionally suspends the @rating and the limit recommendation until the issuance of the final decision) or an already opened insolvency proceeding (in which case the rating is 0, because the risk is already materialized).

In the punctual credit report Coface also includes an indicator on the payment behavior of the subject company. The regime of payments is an indicator that directly influences the maximum exposure[22] recommended by Coface and indirectly influences the risk category to which the subject company belongs.

The most frequent observations mentioned at Regime of Payments section refer to PIR interrogation and debts to the State Budget:

Several elements are considered with respect to this comment:

- Payment incidents (PIR interrogation)
- Debts to the State Budget
- Financial indicators (indebtedness degree, immediate and current liquidity, solvency, payment days, working capital)
- The collection cases
- The insolvency applications

[22] The upper credit limit acceptable for a supplier or service provider with payment within an average term is of 60 days (It is considered that the subject company has an average number of 5 suppliers/providers that deliver goods or provide services at the same time).

Table 10. Meaning of Coface payments regime code

Code	Meaning
0	No relevant payment information available.
1	No available information concerning payment incidents.
12	Based on the current status of the company, at this moment Coface Central Europe cannot provide a final estimation regarding the company's payment behavior.
14	Based on the available information, at this moment Coface Central Europe cannot provide a final estimation regarding the company's payment behavior.
15	Due to the insolvency/ registered debt collection information, the payment regime cannot be assessed at this moment.
100	The payments are made with extreme precision.
200	The payments are made regularly.
300	The payments are made in compliance with the agreed conditions.
400	**The payments are not made regularly.**
450	**The payments are made slowly.**
500	**The payments are made extremely slow.**
550	The payments are made extremely hard, legal proceedings are required on a regular basis.
600	**The payments ceased.**

Source: Internal Coface data

By analyzing the distribution of companies verified by Coface during 2013 based on the market behavior, we can notice:

- No rating can be issued for 20% (due to the reasons mentioned in table 10, codes 0-15);
- 55% of the companies fail to make payments on a regular basis.
- 25% of the companies make payments regularly and in compliance with the agreed conditions.

Also, in the credit report Coface determines the credit limit recommended for the subject company, namely the upper credit limit acceptable for a supplier or service provider with an average 60-day payment term and 5 suppliers at the same time. For the companies classified in the major risk category (NIGA), Coface always recommends the 0 credit limit. Also, there are frequent circumstances (with a weight of approximately 50%) where the companies that belong to NIG risk zone (insolvency risk above the average) do not benefit from the credit limit recommended by Coface (max credit = EUR 0).

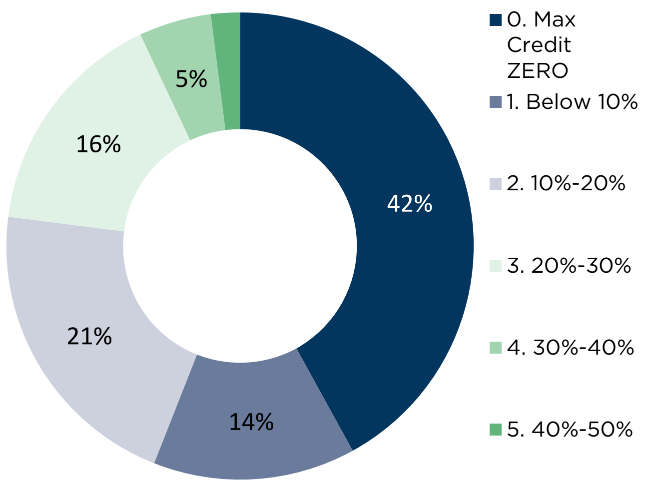
The computation of the maximum credit considers several factors:

- @rating score (4 - 10; for 1 - 3, MC is always 0)
- The sector where the company operates (services, retail trade, wholesale trade/ production)
- Payments regime
- The collection cases registered with Coface
- Debts to the State Budget

The credit limit is determined as a percent of the monthly turnover of the subject company, with the following distributions:

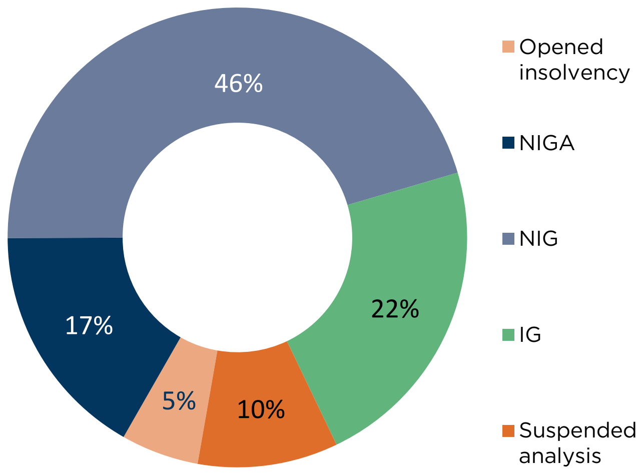
- 42% of the companies analyzed by Coface during 2013 DO NOT benefit from the credit limit. Among these, one third belongs to NIGA risk zone (namely are exempted from the credit limit from the start), while two thirds belong to NIG risk zone (but do not benefit from the credit limit recommended by Coface due to the significant insolvency risk, above the average, and to the deteriorating payment behavior).
- For 35% of the analyzed companies, the credit limit recommended by Coface has a weight of less than 20% in the monthly turnover, for a maximum exposure of 60 days between the invoice issuing date and the maturity date.
- For the remainder of 23% of analyzed companies, the credit limit recommended by Coface ranges between 20% - 40% of the monthly turnover.

Distribution of Maxcredit/ Monthly TO @Coface



Source: Internal Coface data

Distribution of Maxcredit/ Monthly TO @Coface



Source: Internal Coface data

Whereas most information in this survey shows a depreciation signal concerning the companies' payment behavior in general, and of the medium, large and very large companies in particular, we will further focus on the internal data held by Coface and which refer to this segment of companies.

Thus, table 11 shows the companies analyzed by Coface during 2013, as well as during year 2012, the distribution of the average @rating score and recommended credit limits, this being based on various size categories.

By analyzing such data we notice that:

- The higher the turnover amount of the analyzed companies, the lower marginal insolvency risk. Despite this, the average @rating score for all size categories classify the analyzed companies in the category of significantly above the average insolvency risk (NIG, rating 4 or 5).
- All risk categories register an increase of the average insolvency risk, where the largest decrease of the average @rating score is registered for the companies with a turnover that exceeds 1 MEUR.
- At the end of 2012 the companies with a turnover higher than 50 MEUR were classified at the lower edge of the IG risk zone, while at the end of Q3 of 2013 these were classified at the upper edge of the NIG risk zone.
- All risk categories register a decrease of the average value of the credit limit recommended by Coface, with significant decreases registered mainly for companies with a turnover that exceeds 1 MEUR.

Table 11. Distribution of companies analyzed by Coface based on size category

TO Category EUR	Average TO (EUR)	Average @rating score 2013	Average @rating score 2012	Average MaxCredit 2013 (EUR)	Average MaxCredit 2012 (EUR)	Deviation MaxCredit 13/ 12
1. BELOW 0.5 M	146,854	3.71	3.99	2,764	3,447	-20%
2. 0.5 - 1 M	698,417	4.79	4.94	13,724	17,028	-19%
3. 1 - 5 M	2,478,125	4.98	5.35	45,017	52,192	-14%
4. 5 - 10 M	1,458,749	5.17	5.6	140,687	180,460	-22%
5. 10 - 50 M	21,458,712	5.22	5.69	404,206	475,913	-15%
6. 50 - 100 M	68,541,298	5.56	6.15	1,094,023	1,312,116	-17%
7. OVER 100 M	269,417,233	5.51	6.25	1,298,931	1,668,257	-22%
Grand Total	5,107,040	4.42	4.84	59,128	74,245	-20%

Source: Internal Coface data

Below are mentioned the most important conclusions obtained following the analysis of the sample of companies analyzed by Coface during 2013:

- Approximately two thirds of the companies show an insolvency risk extremely high or significantly above the average.
- More than half of the companies make payments at an extremely slow pace.
- 4 out of 10 companies analyzed by Coface do not benefit from the credit limit, and for 3 out of 10 analyzed companies, the credit limit is of maximum 20% of the monthly turnover (while the average term of payment is considered of 60 days, the exposure in real time does not exceed 10% of the monthly turnover).
- Coface decreased the value of credit limits (namely the recommendations of suppliers' exposures to their customers) by 20%.

These conclusions are important, whereas the analyzed sample generates 60% of the turnover of all active companies in Romania.

6. TERRITORIAL DISTRIBUTION OF INSOLVENT COMPANIES

The territorial distribution of insolvency cases registered during 2013 did not register significant changes compared to the circumstances of the same period of the previous year. Thus, the most affected three regions based on the number of insolvencies registered during 2013 were S-E, S and N-W, respectively, which concentrate almost half of the overall insolvencies registered during the analyzed term.

The only regions where the number of insolvencies registered during 2013 significantly increased, compared to the previous year, are the Center and the S-W, while the N-E region shows certain stabilization. We will further see (in the next chapter) that the private environment of these regions records a contraction trend, where the ratio of newly-incorporated companies during the first 11 months, compared to the number of companies that ceased their business during the same period of time is of 1:3 for this region.

The other regions registered a relative stagnation or even decrease of the number of insolvencies reported during 2013, the largest decrease being registered in the S region, namely 11%, and in the W, namely 8%.

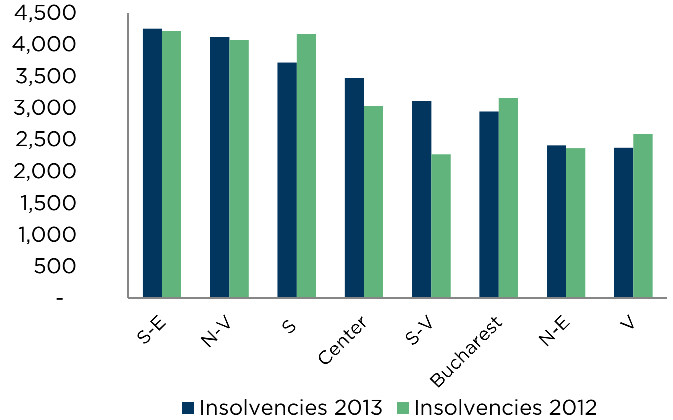
It is worth mentioning that the W region registers two times less insolvency proceedings than the S-E region, while the number of active companies in both regions is similar.

Table 12. Regional distribution of insolvent companies

Region	Insolvencies 2013	Insolvencies 2012	Deviation Insolvencies 2013 - 2012
S-E	4,246	4,207	1%
N-V	4,114	4,067	1%
S	3,712	4,164	-11%
Center	3,471	3,030	15%
S-V	3,109	2,264	37%
Bucharest	2,942	3,156	-7%
N-E	2,406	2,364	2%
V	2,372	2,590	-8%
Grand Total	**26,372**	**25,842**	**2%**

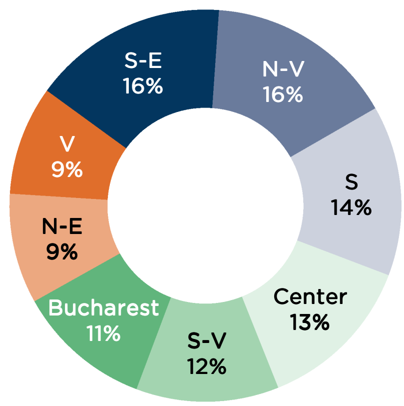
Source: BIP, Data processed by Coface

Geographical distribution of insolvencies cases registered during 2013 - 2012



Source: BIP, Data processed by Coface

Regional distribution of insolvencies cases initiated during 2013



Source: BIP, Data processed by Coface

7. THE PRIVATE ENVIRONMENT - WHERE TO?

There is a series of theories[23] that promote the positive side of elimination, by means of competitive market forces, of the less competitive companies. Thus, the technological progress, fueled by the innovation process will determine the removal of the less competitive companies, which will be replaced by more competitive new companies. Thus, the private economic system is, theoretically, subject to a continuous regeneration dynamics called "creative destruction".

A summary analysis of this theory for Romania shall imply the following steps:

- The numerical analysis of the companies that cease their business during a certain period of time (not solely for those regarding which the insolvency proceedings were initiated), compared to the newly-incorporated ones.
- The comparison between the size of companies that leave the system and the newly-incorporated ones, namely the ratio concerning the financial and social size of these companies.

It is also required and relevant to extend the analysis between the two forces in order to cover all forms of companies' business interruption: insolvency, suspension, deregistration, dissolution. In this analysis, we shall remove the Self-Employed Persons (SEP) or IE[24] organization forms because their analysis is strongly influenced by other non-financial factors.

A. Evolution of new companies registration

Thus, we may appreciate that the number of newly incorporated companies during 2013 is similar to the one registered during the previous year. A negative aspect can be seen in the Center, N-E and S-W regions, which show the largest decrease, while the sole significant increase is registered in Bucharest.

Table 13. Evolution of registrations at regional level

Region	Total number of registrations between 01.01.2013 - 30.11.2013	Total number of registrations between 01.01.2012 - 30.11.2012	Dynamics 2013 - 2012
V	5,808	5,857	-1%
Bucharest	13,231	12,954	2%
Center	5,252	5,642	-7%
N-E	5,561	6,020	-8%
N-V	8,248	8,294	-1%
S	8,931	9,070	-2%
S-E	6,.619	6,630	0%
S-V	4,062	4,360	-7%
Total	57,712	58,827	-2%

Source: NORC

[23] The most well-known is the one promoted by Joseph Schumpeter, in his book *Capitalism, Socialism and Democracy*, 1942.

[24] IE = Individual enterprise

The county level evolutions are extremely different, and the two tables below show the top five counties with the highest increases and decreases.

Table 14. Evolution of registrations at county level

County	Region	Total number of registrations between 01.01.2013 - 30.11.2013	Total number of registrations between 01.01.2012 - 30.11.2012	Dynamic
Vrancea	S-E	628	570	10%
Cluj	N-V	3,448	3,144	10%
Ilfov	S	2,808	2,606	8%
Braila	S-E	717	679	6%
Galati	S-E	1,465	1,394	5%
Suceava	N-E	905	1,074	-16%
Salaj	N-V	441	538	-18%
Mehedinti	S-V	372	455	-18%
Covasna	Center	245	310	-21%
Harghita	Center	385	550	-30%

Source: Internal Coface data

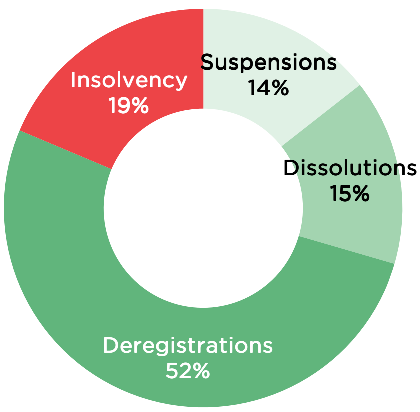
In conclusion, the trend of newly incorporated companies shows stagnation in 2013, compared to 2012.

B. Evolution of companies that suspended their business

According to the data published by NORC[25], a number of 1,007,087 traders were registered as active at the end of 2012. Following the removal of SEPs and IEs, there are 695,492 companies, out of which 615,880 filed the financial statements within MPF for the business performed during 2012.

According to the official status registered with NORC - 615,880 companies on 31.12.2013, we can notice that a number of 142,541 companies no longer operated at that date. These represent 23% of the total companies that filed the financial statements during 2012 and are by 2,47 times more, compared to the number of companies (except for SEPs and IEs) registered during 2013. The distribution of the number of companies, based on the business suspension reason, is shown in the chart below.

Suspended business 2013



Source: NORC[26]

[25] http://www.onrc.ro/documente/presa/comunicat_30_01_2013/6-active-1.pdf

[26] http://www.onrc.ro/romana/statistici.php

Table 15. Evolution of companies that suspended their business

Region	Total number of registrations between 01.01.2013 - 30.11.2013	Number of companies that suspended their business during 2013	Business suspension/ Registrations during 2013
V	5,808	14,507	2.50
Bucharest	13,231	22,069	1.67
Center	5,252	18,946	3.61
N-E	5,561	16,393	2.95
N-V	8,248	22,003	2.67
S	8,931	17,676	1.98
S-E	6,619	19,754	2.98
S-V	4,062	11,193	2.76
Total	57,712	142,541	2.47

*except SFPs and IEs

Source: Internal Coface data

Thus, even though the number of newly-incorporated companies remains constant during the first 11 months of 2013, these do not even cover half of the number of companies that suspended their business during the analyzed period of time.

Obviously, we cannot compare the size of newly-incorporated companies with the one of the companies that suspended their business, because the first are facing an embryonic stage of their life cycle, while the latter are much more mature.

Few figures concerning the profile of companies that suspended their business during the first 11 months of the current year confirm this:

- Average term of operation of 11 years
- Average turnover of approximately 433 KRON and average debts of 1.1 MRON
- Average number of employees - 2.19

Thus, the fact that during 2013 a 2.47 ratio was registered with respect to the number of companies that suspended their business and the number of newly-incorporated companies is not a matter of concern, at least not until we will find the time evolution of the newly-incorporated companies, where the first 3 years play a critical role in this respect.

However, another element represents an important hint of the fact that the private environment follows a contraction trend, namely that the companies that suspended their business during 2013 cancel the entire added value brought to the economy by the companies incorporated during 2011 and 2012, as shown in the table below.

Table 16. Size of companies In - Out

Companies that...	ceased their business in 2013	were incorporated during 2011 & 2012
Number	142,541	90,209
2012 turnover	50.4 MRON	42.4 MRON
Average number of employees registered in 2012	255,380	225,170
Aggregate value of debts	129 MRON	32 MRON
Value of immobilized assets	47 MRON	20.7 MRON

*except SEPs (self-employed person) and IEs (individual enterprises)

Source: Internal Coface data

Thus, we consider that the relative stabilization of insolvencies newly initiated during 2013 becomes relevant only from a statistical point of view, whereas the main reason of concern consists of the insolvency faced by a record number of medium and large companies, the latter being able to generate a faster negative impact on the economy and harder to replace.

8. METHODOLOGY REMARKS

In this study we took into account the insolvencies newly initiated during the last 4 years, based on the data published by BIP. For instance, all companies with insolvency procedures initiated between January - December, 2013 (according to BIP) and which are not registered as operating on January 03, 2014 (according to NORC) were considered as insolvencies newly initiated during 2013. Considering that, this study was drafted at the beginning of January, 2014 and the data concerning insolvencies initiated during 2013 are preliminary. A one month difference (January, 2013) was allowed for final data centralization, which enables the processing of most data registered within NORC statistics with a certain delay from their publication within BIP. The final data on the total number of insolvencies initiated during 2013 shall be published by Coface by the end of Q1 of the current year.

The analysis of financial indicators for the companies taken into account was exclusively based upon the financial statements submitted to MPF in the analyzed period and the data processed by Coface.

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