

Understanding the Shift in Trade Credit in the COVID-19 Pandemic

Part Two: A Case Study on Small and Medium-sized Enterprises in Europe

Authors

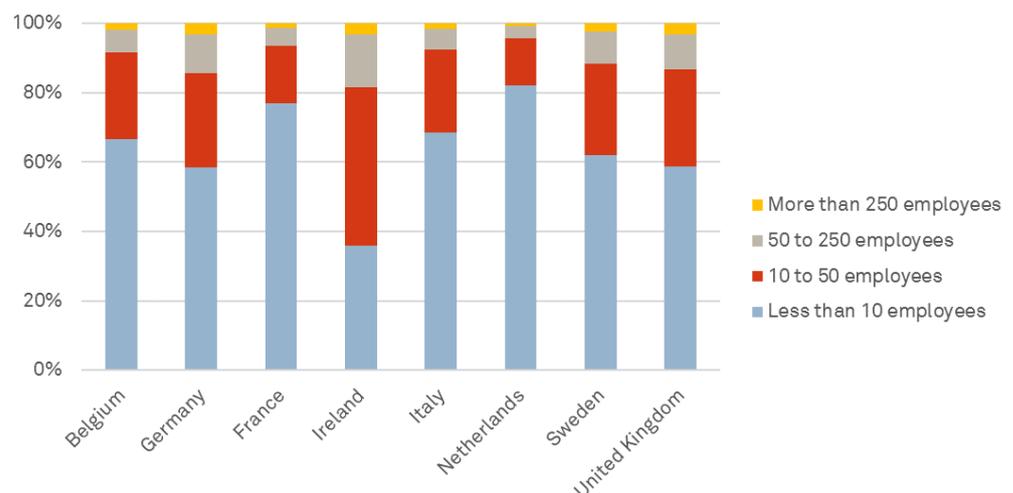
Arsene Lui, CFA, FRM
Senior Quantitative Analyst
Analytic Development Group

In part of one of 'Understanding the Shift in Trade Credit in the COVID-19 Pandemic'¹, we presented the evolution of trade credit activity and payment behavior of American small and medium-sized enterprises (SMEs) since the outbreak of COVID-19. In Europe, many governments have also imposed nationwide lockdown measures restricting business operations, gatherings and social contact, disrupting the lives of hundreds of millions of people and the operations of thousands of businesses. While some European countries are still struggling with the pandemic, some other European countries have already relaxed or announced plans to relax some of the restrictions. In this blog, we would like to compare the most recent trade credit activity and payment behavior of SMEs in eight European countries, aiming to assess the similarities and differences of the impact of COVID-19 among European SMEs.

Research Data

We extracted 1.4 million companies from our Trade Payment Database for eight European countries: Belgium, Germany, France, Ireland, Italy, the Netherlands, Sweden, and the United Kingdom. Outstanding trade credit balances at month end are reported by creditors (i.e., suppliers) and are aggregated for each debtor (i.e. customers). As displayed in Figure 1, the majority of the companies are SMEs with less than 250 employees.

Figure 1: Distribution of companies by the number of employees



Source: S&P Global Market Intelligence, June 5, 2020. For illustrative purposes only.

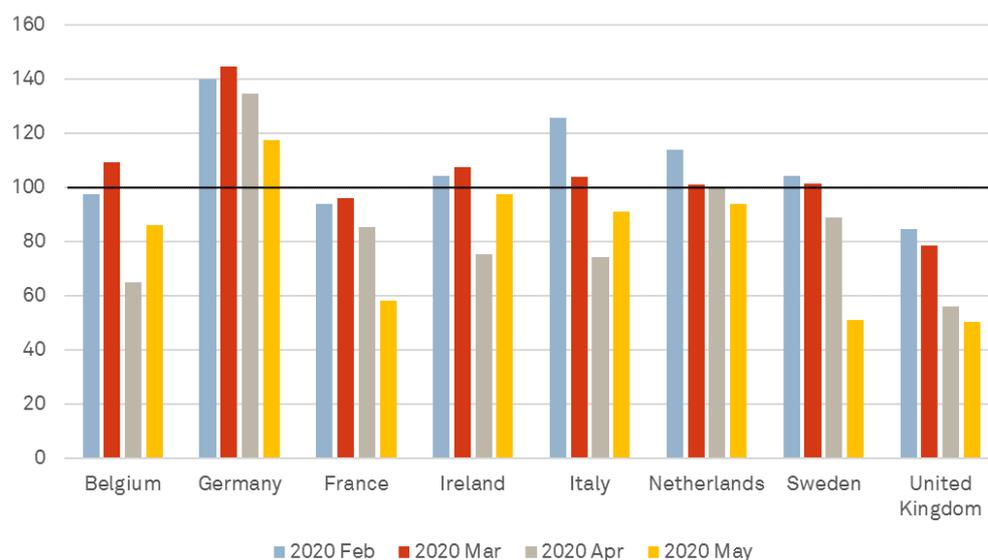
¹ <https://www.spglobal.com/marketintelligence/en/news-insights/blog/understanding-the-shift-in-trade-credit-in-the-covid-19-pandemic>

Are companies able to obtain sufficient trade credits?

The use of trade credit is driven by both the supply and demand side. On the demand side, the trade credits are positively correlated to the customers' business activities and the demand for production goods. On the supply side, the trade credits are negatively correlated to suppliers' risk aversion. By looking at the amount of trade credits obtained by companies, we can estimate the impact of COVID-19 on the economy.

In Figure 2, we show the monthly aggregated outstanding trade credit balances per country. January's values are used as the pre-COVID-19 benchmark. This is because COVID-19 was first flagged to the World Health Organization by China on New Year's Eve², and several Chinese cities went into lockdown in late January, causing severe disruption to the global supply chain. In February, when the number of COVID-19 cases was still lower in Europe and the majority of businesses still operated as usual, the impact of the virus had already reached the United Kingdom. The largest contribution to this drop is in the Metals and Mining sector. It is not surprising as the United Kingdom's major export to China is precious metal. When the virus started spreading uncontrollably throughout Europe in March, Italy was the hardest hit as indicated by the largest drop in trade credit balance from February, which was impacted mainly by the slowdown of business in the Wholesale and Retail sector. Entering into April, all European countries were under different degrees of lockdown/social distancing measures. Trade credit balances decreased for all these countries. When the pandemic started to be brought under control in May, we observed two opposite patterns for trade credit balances: a rebound for Belgium, Ireland and Italy; and a further drop for the remaining countries, which is especially noticeable for France and Sweden.

Figure 2: Monthly outstanding trade credit balances (2020 January level = 100)



Source: S&P Global Market Intelligence, June 5, 2020. For illustrative purposes only.

² Timeline of WHO's response to COVID-19, World Health Organization, <https://www.who.int/news-room/detail/29-06-2020-covidtimeline>

Are companies paying their trade credits on time?

We analyze the time series of trade credit balances and deduce the payment behavior in each month. In Figure 3, we illustrate the percentage of trade credit balances being paid on time in each country. When individual countries decided to lock down their cities in March, companies in Belgium, France and Ireland were seriously hit. The percentage of on-time payments was 32%, 23% and 16%; lower than February's values. However, we see a significant rebound for these three countries in April. The payment behavior in Germany, Italy, the Netherlands, Sweden and the United Kingdom remained stable during the pandemic. We observe a small drop for the Netherlands in February, the United Kingdom in March and Sweden in April, but they were followed by an immediate rebound in the following month. The observed rebound pattern of the on-time payment across different European countries may indicate the success in providing emergency liquidity to the impacted businesses by the corresponding government.

Figure 3: Monthly average percentage of trade credit balances being paid on time



Source: S&P Global Market Intelligence, June 5, 2020. For illustrative purposes only.

We also use our proprietary statistical model, trained on historical payment data, to produce a likely scenario on the payment behavior in June (i.e. green diagonal-shaded bars in Figure 3). The model predicts a slight deterioration for Italy, a moderate deterioration for Germany, France, Ireland, Sweden and the United Kingdom, and a significant deterioration for Belgium and the Netherlands, using the payment behavior from the most recent months and the historical month-over-month correlation of payment behavior.

Summary

There is no doubt the pandemic has slowed down business activity in the eight European countries we analyzed. From trade credit data, we see the impact of COVID-19 reached these European countries at different points in time and at different levels of severity. In June, we even observe a recovery in trade credit for Belgium and Italy. The latest increase in trade credit balance in Italy could be linked to the end of the stricter lockdown measures in the country, since the middle of May. Further data for the

following month may confirm the recovery trend, keeping in mind that trade credit balances are highly seasonal and will likely remain quite volatile during these uncertain periods.

With regards to the payment behavior of companies, the percentage balance of trade credit being paid on time in May is similar to the pre-COVID-19 level. Although some of these countries experienced a drop in on-time payments in March or April, it was followed by a rebound in the next month. Our proprietary model predicts different levels of deterioration in payment behavior across these countries. Governments in Europe have launched significant measures, ranging from tax deferrals to access to finance and grants, to help business struggling through the pandemic. It is likely that the governments will continue to ramp up their support measures. The governments support and the further relaxation of lockdown rules may create a difference between our model predictions and the actual payment behavior of businesses in the future.

About S&P Global Market Intelligence

At S&P Global Market Intelligence, we know that not all information is important some of it is vital. Accurate, deep and insightful. We integrate financial and industry data, research, and news into tools that help track performance, generate alpha, identify investment ideas, understand competitive and industry dynamics, perform valuation, and assess credit risk. Investment professionals, government agencies, corporations, and universities globally can gain the intelligence essential to making business and financial decisions with conviction.

S&P Global Market Intelligence is a division of S&P Global (NYSE: SPGI), which provides essential intelligence for individuals, companies and governments to make decisions with confidence. For more information, visit www.spglobal.com/marketintelligence

Contact Us

Americas
+1 212 438 8701

Europe, Middle East
and Africa
+44 (0)20 7176 1234

Asia Pacific
+852 2533 3565

support.ciq@spglobal.
com

marketintelligence.spglobal.com

Copyright © 2020 by S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

These materials have been prepared solely for information purposes based upon information generally available to the public and from sources believed to be reliable. No content (including index data, ratings, credit-related analyses and data, research, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of S&P Global Market Intelligence or its affiliates (collectively, S&P Global). The Content shall not be used for any unlawful or unauthorized purposes. S&P Global and any third-party providers, (collectively S&P Global Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Global Parties are not responsible for any errors or omissions, regardless of the cause, for the results obtained from the use of the Content. THE CONTENT IS PROVIDED ON “AS IS” BASIS. S&P GLOBAL PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT’S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Global Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

S&P Global Market Intelligence’s opinions, quotes and credit-related and other analyses are statements of opinion as of the date they are expressed and not statements of fact or recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P Global Market Intelligence assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P Global keeps certain activities of its divisions separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain divisions of S&P Global may have information that is not available to other S&P Global divisions. S&P Global has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P Global Ratings does not contribute to or participate in the creation of credit scores generated by S&P Global Market Intelligence. Lowercase nomenclature is used to differentiate S&P Global Market Intelligence PD credit model scores from the credit ratings issued by S&P Global Ratings.

S&P Global may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P Global reserves the right to disseminate its opinions and analyses. S&P Global's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge) and www.ratingsdirect.com (subscription), and may be distributed through other means, including via S&P Global publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.