European Payment Index 2008 white paper Industries and credit management best practices

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INTRUM JUSTITIA
European Payment Index 2008
WHITE PAPER

Cost Of Late Payment For European Businesses Soars To €250 Billion
Specific European industries have to adopt credit management best practices immediately

September 2008

INTRODUCTION

European Economic Growth Threatened By Soaring Increases In Late Payment – Urgent Need For 'Best Practice' Credit Management

European firms and public authorities are facing ever-increasing pressure to implement speedier and to the point collection strategies as poor payment behaviour escalates across the entire business and consumer spectrum in the face of the economic volatility sweeping Europe.

Retail credit loss projections based on research and analysis of European financial performance during the first six months of 2008 by Intrum Justitia together with financial consultancy agency Oliver Wyman indicate losses in Europe will rapidly increase. This highlights the need for enterprises to speedily adopt and implement 'best practice' credit management processes.

The cost of late payment to European Businesses during 2007 reached an awesome new record of €250 Billion during 2007 with invoices on average being paid after 55.5 days – almost four weeks late.

The percentage of non-paid debt (written off %) has also climbed to new heights, 2% compared to 1.9% a year earlier. And European public bodies sustained their position in 2007 as the worst payers, taking an average of 65 days to pay an invoice, compared to 55 days for the business community and 40 days for consumers.

The sober insight into the economic realities being faced by European firms of all sizes emerged from the annual European Payment Index (EPI 2008) compiled by Intrum Justitia, Europe's largest credit management agency. The EPI is the result of a survey conducted simultaneously among over 6,000 chief executives and corporate financial officers and experts in 25 European countries in the first quarter of 2008.

Additional research and analysis of the European retail credit situation during the first half of 2008 indicates significant increases in losses can be expected over the next 18 months. The grim conclusion was supported by a complimentary survey, done in cooperation with renowned consultancy agency Oliver Wijman of over 40 European financial institutions covering all key aspects of the credit value chain.

The late payment behaviour trend is almost certain to worsen further during 2008 and 2009, especially in the deteriorating economies of the UK, Spain, Ireland and Denmark. However, the credit crunch and rising oil and food prices will certainly exacerbate the problems created by poor payment behaviour by consumers, businesses and governmental bodies throughout much of Europe.

With the squeeze expected to persist for many months its impact on European business activity has probably yet to peak. The implied threat posed by a worrying economic environment can only be countered by creation of good and sustained credit management processes using proven tools and techniques that deliver real, tangible value.

This white paper will examine the challenges posed by escalating late payment behaviour and introduce the many advantages of full range credit management services, from prospecting to collecting.

EPI 2008 Industry analysis

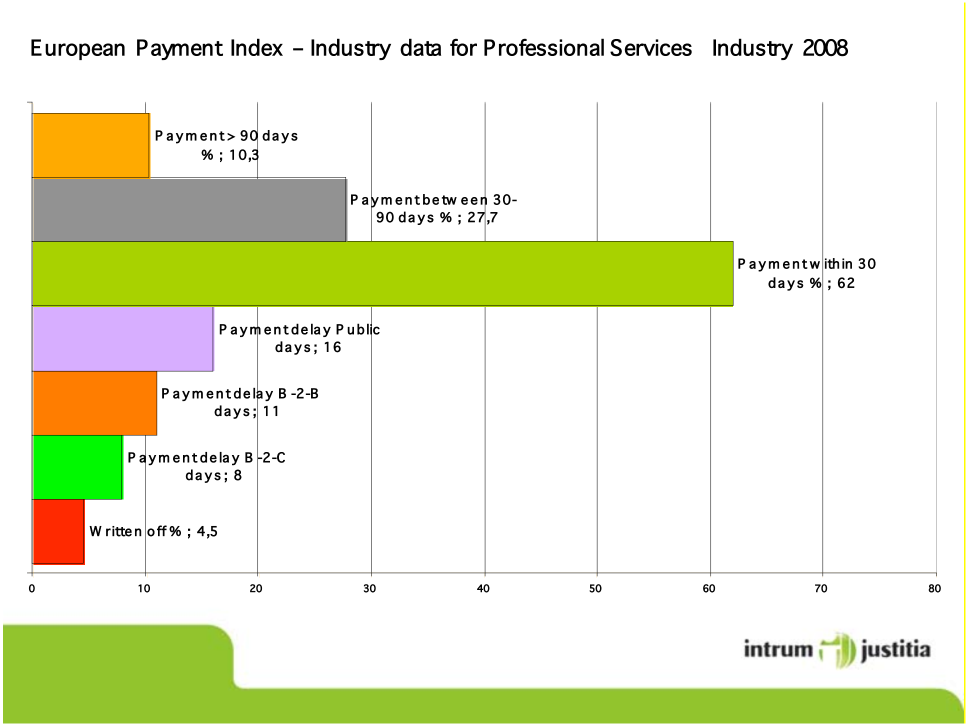
There is a clear north-south divide when it comes to payment behaviour comparing countries. Portugal, Greece and Cyprus are the countries where it takes longest to be paid, while the fastest is Finland followed by the other Nordic countries. However, the Intrum Justitia survey highlighted the fact that in the face of the current economic uncertainty payment risks have already increased in Switzerland, Spain, Italy, Ireland and France.

Getting paid on time or not, varies considerably from business category to category. For example, consumers across Europe are generally selective, opting to first settle invoices relating to high dependence functions such as utility bills and rent or mortgage payments. However, a recent article in the Financial Times noted how many homeowners in the US now no longer prioritise paying their mortgages as they see their property values are going down. This is a significant development considering how paying either the rent or mortgage appears to be the top priority among consumers. Whether this will also happen in Europe remains to be seen.

Lowest on the consumer payment priority list are payments to health sector companies and media companies for subscriptions, among others.

If we look at the various industries we see the following

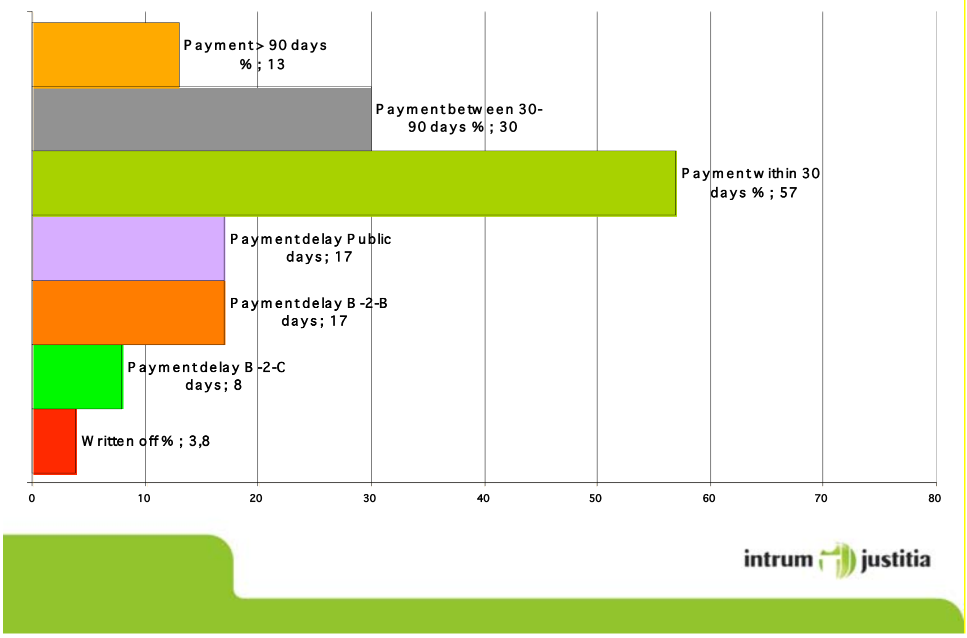
Professional services industry



The professional services industry (accountants, solicitors, recruitment agencies, architects, translators etc) in Europe suffer from the highest write-off percentage compared to other industries; a sizeable 4.5% is expected to be written off in 2008. The EU average over all industries and countries is 2%. Payment delay is highest from the public sector with a 16 day delay. 38% of the invoices are paid after 30 days. The nature of how professional services are often delivered helps to inflate this figure, with some areas of service provision being for one-off deals. Additionally, fees in this area can be large for services which some clients may find largely intangible.

Construction & building industry

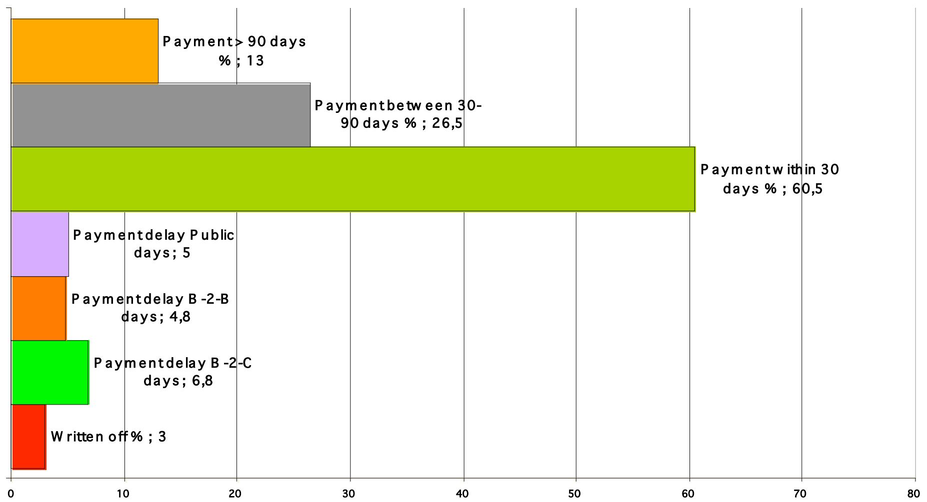
European Payment Index – Industry data for Construction Industry 2008



The building and construction industry in Europe face a write-off percentage of 3,8%. The EU average across all industries and countries is 2%. Payment delay is around 17 days from businesses and the public sector. 43% of the invoices are paid after 30 days. Late or non-payment in this industry is being revaluated in a number of countries. In Scotland, new legislation for the construction industry will help contractors get paid on time, for instance.

Education industry

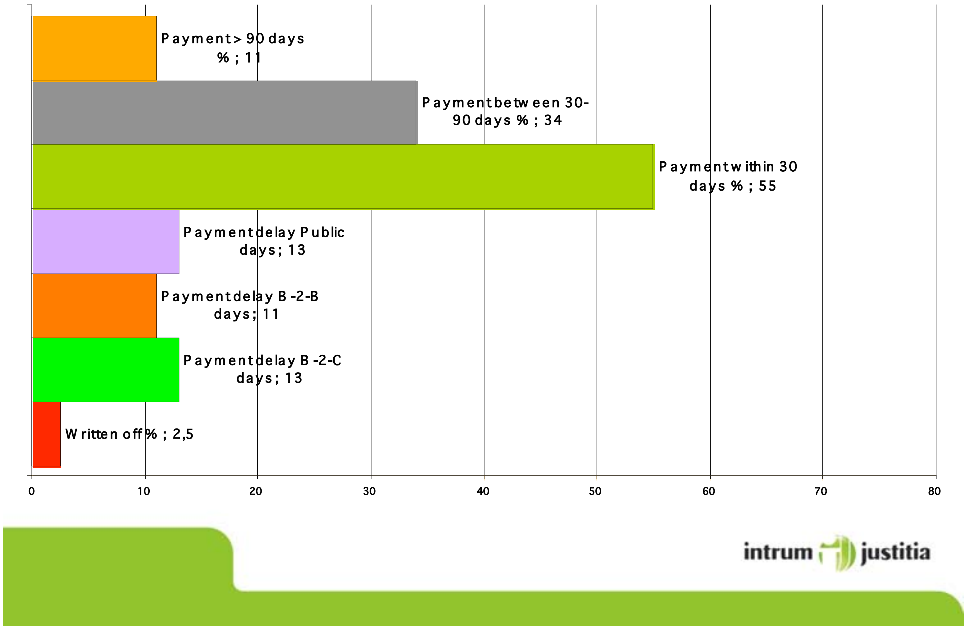
European Payment Index – Industry data for education industry 2008



In the education industry (schools, university, adult education, educational materials etc.), the payment delay is the highest among consumers, with a delay of almost 7 days. The write-off percentage is 3.0%, which is quite high compared with the Europe's average of 2%. Almost 40% of the invoices are being paid late, with 13% later then 90 days.

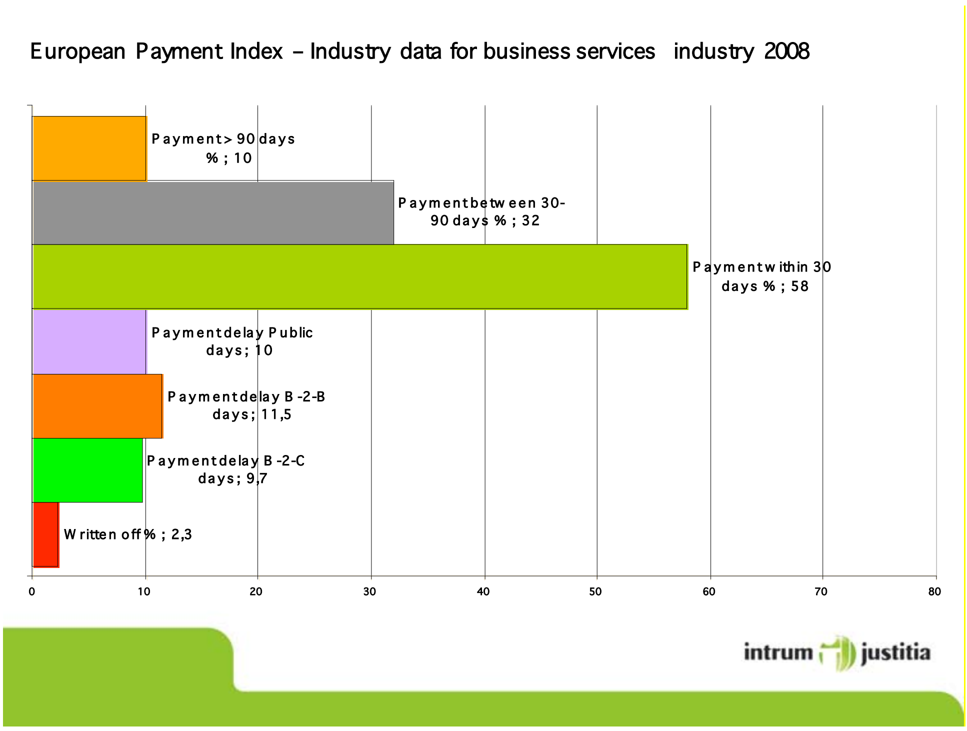
Media industry

European Payment Index – Industry data for Media Industry 2008



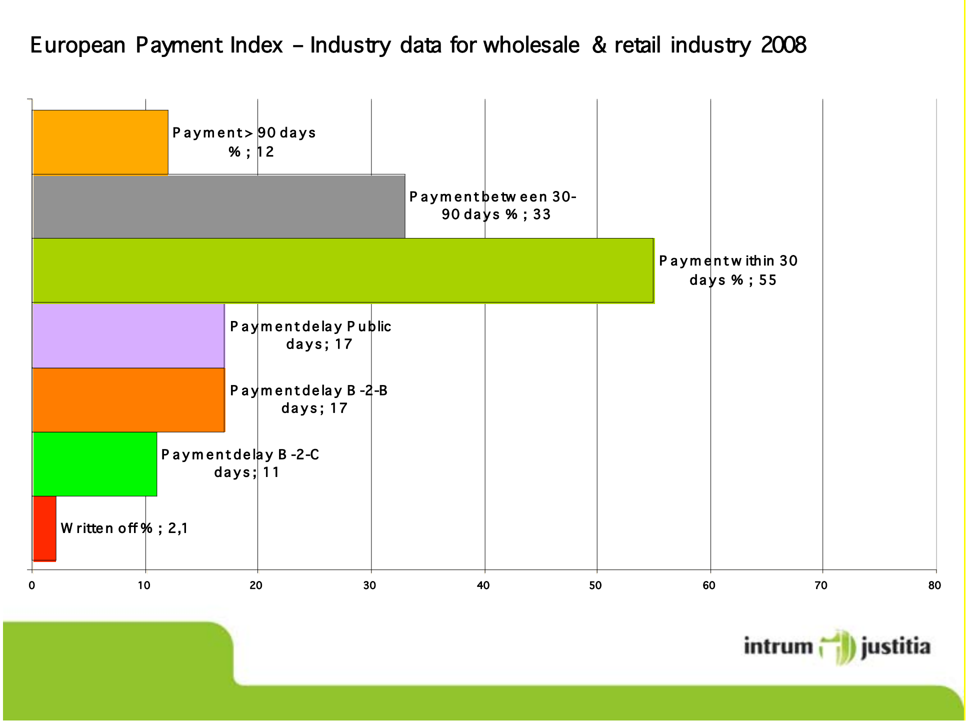
The media industry (publishers, magazine/newspaper subscriptions, media producers etc.) has an average write-off percentage of 2.5% and an average payment delay of around 13 days. 45% of the invoices are paid after the 30-day contractual term. It is a certain trend among consumers to pay very late or not at all for subscriptions, also internet related subscriptions.

Business Services



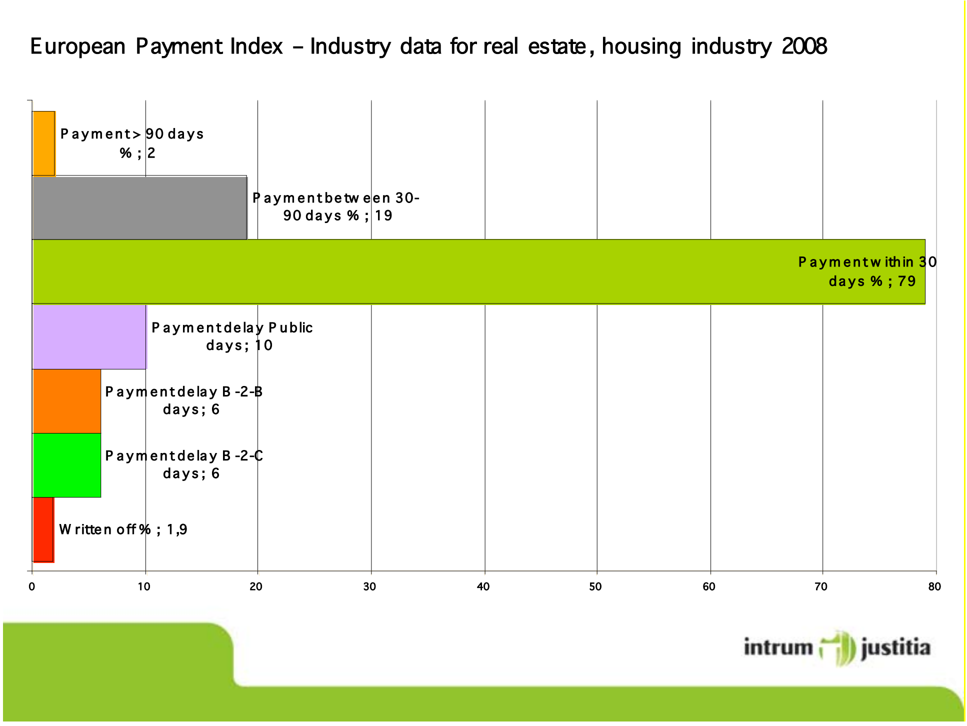
Business Services such as research agencies, intermediaries, consultancy firms, marketing/PR/advertising agencies, text agencies experience an average write-off of 2.3%, better then the professional services industry with a staggering 4.5%. This has to do with the ongoing relationship the business services industry most likely have with their customers. As the professional services industry often have a one-time relation with their customer - a company needs a lawyer for a problem, but once the problem is solved, the relationship ends until a new problem arises. In general, various studies have shown that the stronger, the more frequent and the tighter the relationship is with a customer, payments are made faster.

Wholesale and retail industry



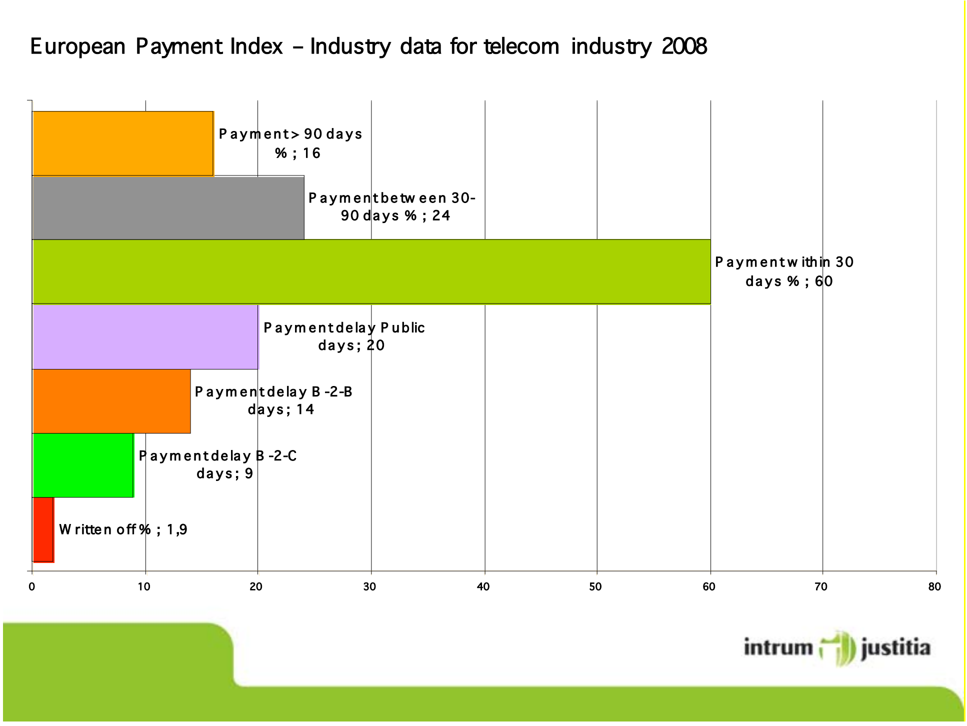
Wholesale and Retail have an average write-off percentage of 2.1%. Payments for this industry are rather slow with 17 days delay from businesses and public sector and 45% of the invoices being paid later then the 30 days contractual term.

Real Estate and housing industry



This industry has an excellent payments track record with some 79% of monies due being paid within the 30 days. The write-off percentage is 1.9%, which is below the EU average of 2%. Businesses and consumers delayed 6 days, obviously due the fact that payments for a house and/or office are high on the priority list.

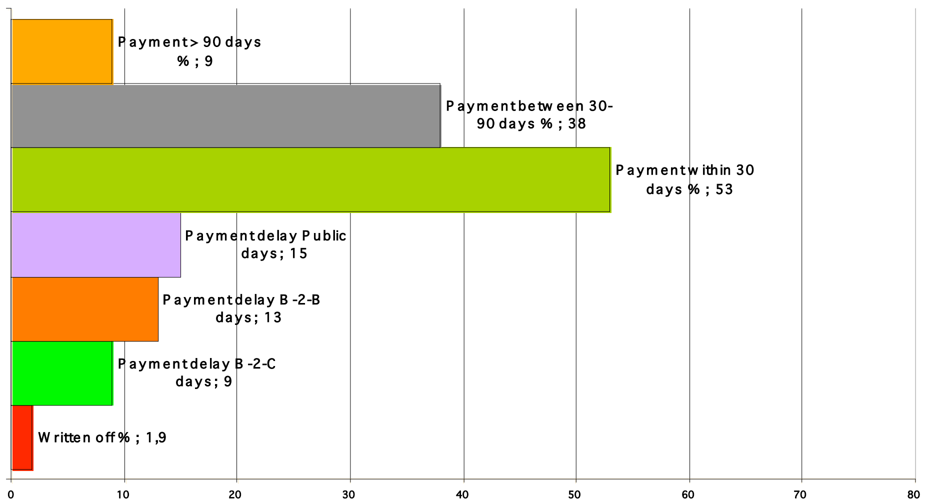
Telecom Industry



The Telecommunication industry write-off percentage is 1.9%. 60% is paid within 30 days and 40% later than 30 days. Payment delay with consumers is rather low at 9 days, while the public sector pays with a delay of 20 days.

Transport & Logistics

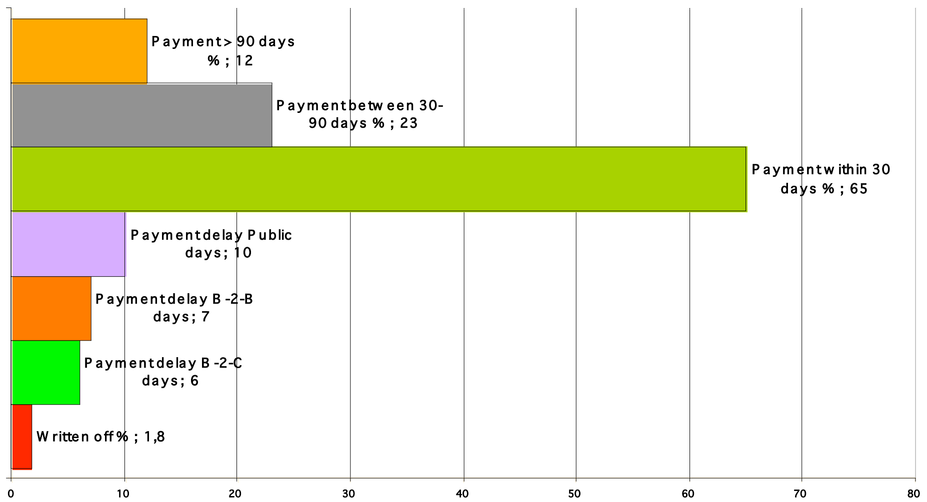
European Payment Index – Industry data for transport & logistics industry 2008



This is an industry that directly suffers from higher oil prices. Fast payments and low write-off percentages are important in this industry. In France, legislation is already in place to help this industry with low margins to get paid without the long delays.

Financial Services Industry

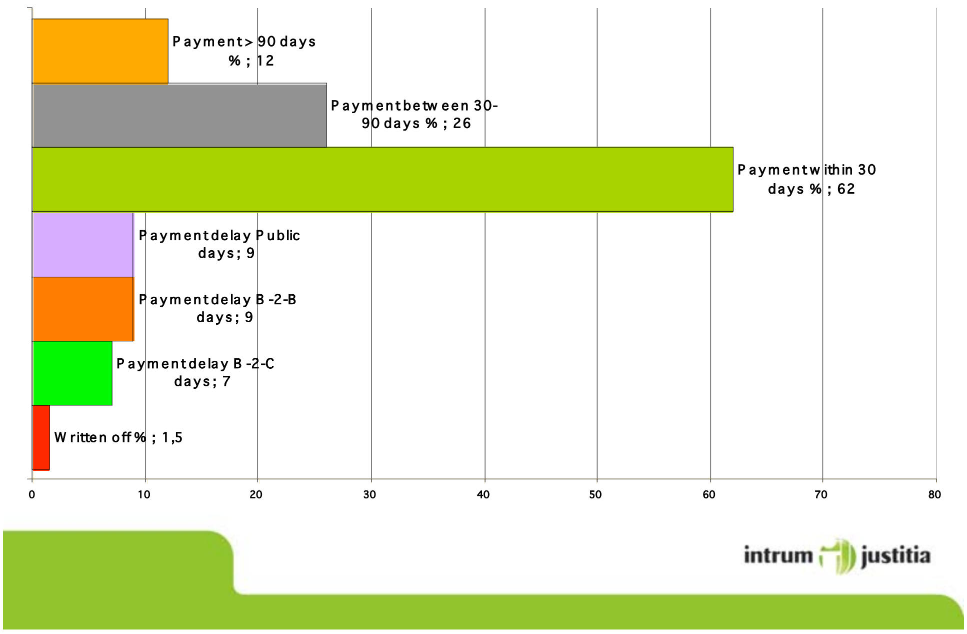
European Payment Index – Industry data for financial services industry 2008



Credit card companies, banks etc. have an average write-off percentage of 1.8%. Delays in payment vary from 6 days for consumers to 10 days for the public sector. In general, 65% is paid within 30 days. In general payments to financial institutions are high on the priority list. More in depth information for this industry can be found in the report "European Retail Credit".

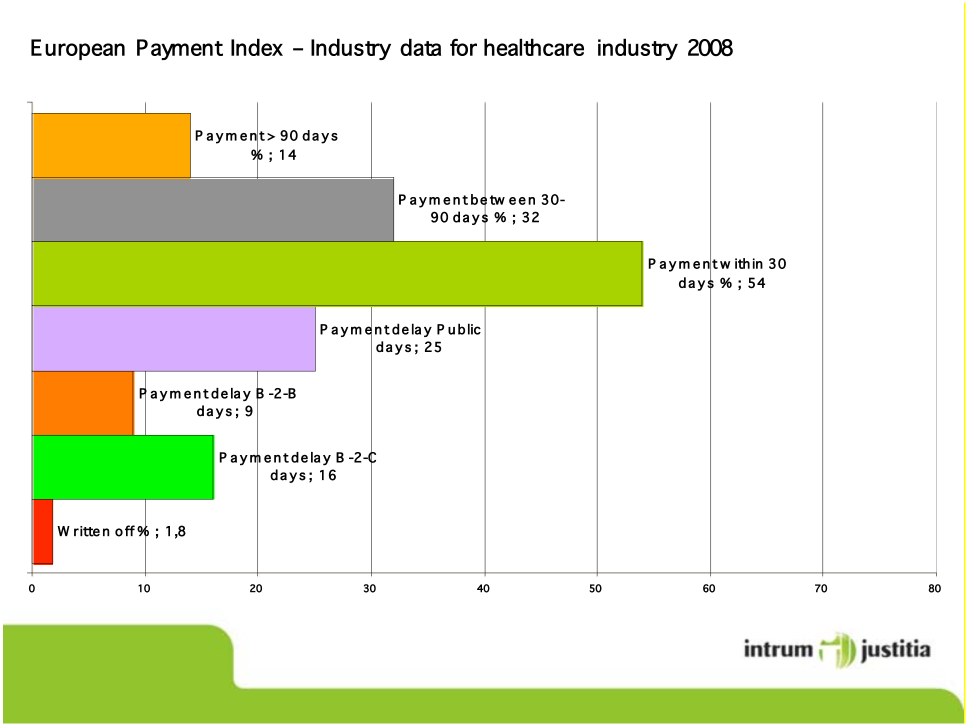
Utilities (gas, water, energy) industry

European Payment Index – Industry data for utilities industry 2008



The utility industry has a rather low write-off percentage of 1,5%, which is normal bearing in mind no one can do without water and energy. Payment delay is between 7 and 9 days and 62% of the invoices are paid on time.

Healthcare industry



The healthcare industry in general struggles with long payment delays, around 16 days from consumers and 25 days from the public sector. The write-off is 1.8% and 46% of the invoices are not paid on time. The healthcare sector is a rather soft sector and not very strong in efficient collection practices.

European Payment Trends

In 2007, the European business community lost a record €250 billion as a direct consequence of invoices not being paid on time. The amount in question practically equals the total domestic product of Belgium, a wealthy European Union country of 10.5 million people.

The latest European Payment Index survey by Intrum Justitia, carried out in the first quarter of 2008 among thousands of companies in 25 European countries, also showed southern Europe heads the league of payment defaulters. The Scandinavian countries ranked the best overall payers of invoices, while countries such as The Netherlands came somewhere in the middle.

The reality of modern business life is that companies, public authorities and private individuals are taking longer than ever before to settle their outstanding invoices. The worst offenders are the people who should be setting the best example when it comes to paying on time – public authorities.

European public sector bodies such as municipalities took an average of 65 days to pay an invoice compared to 55 days for the business community and 40 days for consumers. Portuguese public authorities set the worst example in Europe, taking almost 138 days in 2007 to pay their bills.

There is a clear north-south divide when it comes to payment behaviour. Portugal, Greece and Cyprus are the countries where it takes longest to be paid, while the fastest is Finland followed by the other Nordic countries. However, the Intrum Justitia survey highlighted the fact that in the face of the current economic uncertainty payment risks have already increased in Switzerland, Spain, Italy, Ireland and France.

Getting paid on time or not, varies considerably from business category to category. For example, consumers across Europe are generally selective, opting to first settle invoices relating to high dependence functions such as utility bills and rent or mortgage payments. Lowest on the consumer payment priority list are payments to health sector companies.

With the payment delay increasing from 16 days in 2007 to 17 days currently, there is growing pessimism among businesses. Some 30 percent of the more than 6,000 respondents to the Intrum Justitia survey believed it would get harder to receive payment during 2008. Businesses in Hungary, Ireland, Portugal and Spain are the most pessimistic.

Non public domain research sponsored in part by Intrum Justitia into the level of credit losses being experienced by the retail trade across Europe during the first half of 2008 has indicated there are solid grounds for such pessimism. Scenarios based on the research and analysis show total European retail credit losses could soar in 2008 to €34.7bn, rising to €42.5bn in 2009, a 35% increase on 2007 levels, while losses in 2009 may be even higher, and possibly exceeding €50bn.

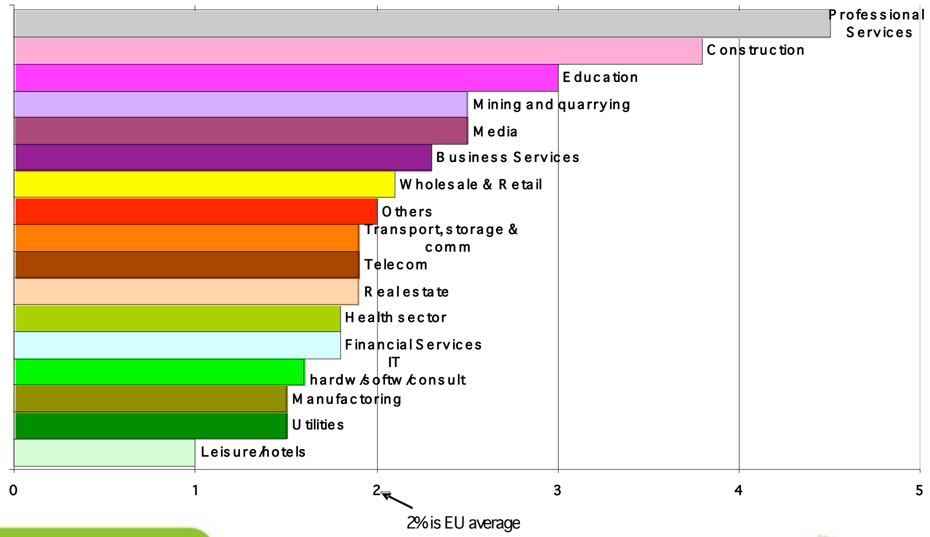
Complicating the European picture is the significant differences that occur in the credit market outlook across countries, with the UK and Spain expected to see the majority of incremental losses due largely to mortgage lending. In countries with less highly developed and aggressive lending practices, such as the Nordics, the Netherlands, Czech republic and Poland, credit loss rates remain lower.

Additional complications in Europe concern the differing average contractual terms from industry to industry and country to country. For example, the average contractual term in Europe for consumers is between 20 – 30 days, whereas in industry it is often 30 days although in the real estate and utilities industries it is just 18 days. When it comes to government related orders, the contractual terms are often stretched by an addition 10 – 15 days.

The underlying message behind the latest research is that the need for stepping up credit management activities to combat the effects of the credit crunch and volatile oil and food prices is urgent. And it is especially pressing for the professional and business services industries. Also there is urgent need for greater harmonisation of regulations relating to contractual arrangements as well as payment and credit management processes. So far EU regulations (in particular the Late Payment directive) have had a very limited impact on contractual arrangement etc.

Industries where the written off percentage is highest:
1. Professional Services
2. Construction & building industry
3. Education industry
4. Media industry
5. Business Services
6. Wholesale and Retail

European Payment Index – written off percentage 2008 / per industry EU



Smaller companies must concentrate on getting paid on time, thus chasing outstanding invoices

Size-class breakdown for average payment term and delay in days 2008 for (B-2-B)

2008	Average contractual payment term in days	Average payment duration in days	Average payment delay in days	Average written off percentage %
Up to 19 employees	35	56	21	3,1%
20-49 employees	33	55	22	3,0%
50-249 employees	35	54	19	2,0%
250-499 employees	35	56	21	1,5%

Again from the European Payment Index 2008 it derives that smaller companies are being hit by late payments, they have to deal with prolonged payment duration and a higher written off percentage than larger companies. Obvious sales and marketing are very important for smaller firms to hit their targets, as well as having and keeping good relations with customers. A couple of customers often account for a large part of the turnover. And last but not least, smaller companies have less employees, thus certain tasks might be delayed or not given enough time. From various researches it is known that chasing after unpaid invoices is one of the tasks that might be treated last. At the other hand waiting too long will seriously decrease the success rate. Outsourcing the complete credit management process will increase the cash flow situation, so that the company can put all the emphasis on growing the business, while getting paid.

The Cost of Late Payment

Around one billion invoices that are defaulted on in Europe every year turn into debt collection cases. Therefore it demands little imagination to understand that the consequences of late payment for Europe are dire.

Late payments remain one of the most significant barriers to trade across Europe, creating additional costs for companies in the region of €25 billion every year. Respondents to the Intrum Justitia survey said uncertain and late payments led to managers becoming seriously hesitant about pursuing cross-border business.

The survival of many small and medium sized businesses (SMEs) is directly threatened by late payment. Delayed invoice payments place companies in a critical credit squeeze while long payment periods strain cash flow and fuel uncertainty, impeding the development, competitiveness and profitability of SME's.

Late payment forces companies to spend excessive amounts of time chasing debtors and hinders other investment in research and development, technology and human resources.

As far back as 1997, the European Commission stated that 'late payments represent an increasingly serious obstacle for the success of the single market'. Yet in the majority of European countries, the fundamental changes required to combat late payment are still missing.

Improving credit management practices

Tried, tested and proven tactics to avoid or manage late payment risks already exist.

One tool that extends beyond national insolvency statistics that severely lag behind time is the Intrum Justitia European Payment Index that provides up to date information based on current trends. In addition, the index combines a number of different risk indicators such as payment duration, payment delay, days sales are outstanding, payment loss, forecasts and consequences.

The Intrum Justitia Risk Index survey shows that the lowest payment risks are found in the Nordic countries. The reason is that countries like Denmark, Finland, Norway and Sweden have readily available addresses and data, regulated structures, fast legal processes for small claims and compensation fees for late payments that are simply not present in most other European Union countries.

Another good example is the legislation in the French transport industry, where legislative changes have improved the amount of outstanding receivable considerably, which has ensured better business for all involved in the industry.

But tools such as the European Payment Index are just one component in the toolbox required to improve credit management practices. There is no doubt that government's across Europe need to act to introduce improved legislation and regulations as well as implement programs to change cultural attitudes that pro-actively help small and medium sized enterprises avoid the ultimate risk of bankruptcy due to late payment.

Better credit management practices deliver enhanced growth potential, not only for SME's but also for national economies. By harmonizing credit management rules and standards, European governments will stimulate a freer flow of capital that will not only stimulate their local business environment and benefit the national economy but also enhance the future competitiveness of Europe as a whole.

The measures to help combat late payment
Powerful advice for 2008 and 2009

- Use scoring analysis before acquisition to increase the profitability of your sales and marketing actions
- Analyse risk portfolios
- Monitor your prospect/customer credit-worthiness on a regular basis
- Review your customer base frequently
- Open personal, preferably face-to-face, contact prior to invoice due date, discuss delivery, the invoice and payment
- Follow-up directly after due date if the invoice is unpaid
- Use a professional intermediary to follow up claims

When seeking to combat or reduce late payment risks, be sure to examine the following critical requirements:

Credit policy: Create and consistently implement a clear credit policy tailored to the individual risk orientation and financial strength of the company. The core of the credit policy should include: requirements for delivery against invoice, solvency checks before decisions are made on whether deliveries can be made against invoice, payment targets, measures and consequences in the event of delayed payment, credit limits, and internal competence regulations. Customers and all staff in contact with customers must be made fully aware of the credit policy.

Credit limits: The development of the receivables of individual regular customers should be monitored with the help of credit limits. In practice, the provision of two limits of credit for each (key account) customer has proven to be particularly effective. The crossing of the lower limit serves as an early warning and permits gathering additional information and implementing suitable measures, while reaching the upper limit results in automatic delivery stoppage on the account.

Address checks: Ongoing checks on the billing address. Experience has shown that preventing the use of invalid or out of date billing address is an important factor in optimising the credit management process. Addresses should be updated as an ongoing process and should be subject to routine checks.

Economic information: Ongoing solvency checks should be implemented before decisions are made on deliveries against invoice. If there is a lack of solvency, deliveries should be made against an alternative form of payment.

Routine solvency checks on key customers: Experience shows that the majority of payment losses arise from deliveries to key customers. The insolvency of a key customer has particularly has far-reaching consequences. Therefore, repeated solvency checks, integrated into operational procedures as a matter of routine, are an important element in the overall credit management process.

Flexible contractual payment terms: Offer flexible payment terms on the basis of the bonus-malus-principle. New customers are granted a shorter time period to settle than regular customers who pay by the agreed due date. At the same time, new customers are offered the benefit of a longer payment term to settle when they place repeat orders, provided the payment is made on or before the due date. However, even regular customers may lose their privilege of a longer payment term should they fail to pay on time.

Differentiate; reward good payers with lower prices or extended (payment) terms or free extra services, so that they feel even more rewarded and connected to your company. Definitely you like to sell more to those reliable customers.

Swift reminders: Reminders should be issued rapidly and firmly.
The most successful formula in practice is the so-called ‘2-2-2-Formula’:

- Issue the first reminder letter two weeks after passing of the due date
- Issue only two further reminders before taking legal measure or retaining Intrum Justitia for the collection of the debt
- Maintain a consistent cycle of two weeks maximum between reminder letters

Default interest and billing of operating costs: Invoice late payers for default interest and the operating costs caused by the payment delay (operating costs for bank transactions, administration costs, cost of third parties etc.)

Professional cooperation: Ongoing and consistent cooperation with Intrum Justitia, fully integrated into the company’s customer management process, will ensure efficient credit management tailored to generating rapid receipt of payments.

Extending client structure: Reduce dependency on one or just a limited number of large customers.

Outsourcing; in times of economic volatility and low unemployment, the best way of doing business is focussing on your core business. Credit management in most cases is not a company’s core business. Credit Management in all its aspects is Intrum Justitia’s core business and we are good at it, lowering companies’ days sales outstanding, increasing the cash flow, keeping track of changes in payment behaviour to feedback to sales and CRM. With outsourcing our customers performance is enhanced effectively against lower costs.

How Intrum Justitia helps improve credit management services

Intrum Justitia is Europe's leading credit management services company, serving over 90,000 customers in 24 European markets with efficient, high quality services designed to improve cash flow and long-term profitability. Listed on the Stockholm Stock Exchange (Stockholmsbörsen) since June 2002, the Group employs 2,900 people. Intrum Justitia's head office is in Stockholm, Sweden.

Intrum Justitia's services cover the entire credit management chain, from credit information via invoicing, reminders and collection, to debt surveillance and recovery of written-off receivables. Intrum Justitia also offers sales ledger services, purchased debt services and a number of specialised services related to credit management.

Intrum Justitia values

We understand people Behind every transaction, every company, every invoice, every debt and ever ambition is a person. By understanding people, Intrum Justitia can contribute to profitable business relationships, unhindered trade and sound, long-term business practices for everyone involved.

We are committed to challenge Intrum Justitia deals with situations that can impact the future of a business or an individual. Likewise, our work can influence the economy as a whole by contributing to fair trade and sound business practices.

We seek insights to feed ingenuity By understanding people, being a market leader, and having the necessary expertise, Intrum Justitia is creating new solutions that benefit clients, their customers and other stakeholders. The key to this work is the use of the unique information, knowledge and experience the Group has gained from various aspects of sales, credit and payment processes.

We make a difference Many companies and individuals need help managing their finances. Intrum Justitia's role is to develop solutions that contribute to a sound, stable economy and ultimately benefit our clients and their customers alike. In our work, we show respect for individuals and businesses that, for whatever reason, face payment difficulties. Negotiation, realistic solutions and settlements increase the chances of obtaining payment.

For more information, please contact: m.bosch@nl.intrum.com or your local Intrum Justitia office via www.intrum.com