COFACE PUBLICATIONS

APRIL 2023

CEE Insolvencies 2022

CONTENT

coface FOR TRADE

1 More challenges, more company insolvencies

Regional insolvency trends

Insolvency trends in the Central and Eastern European (CEE) region have been subject to various economic conditions, support measures and legal changes in last three years. Indeed, challenges started with the Covid-19 pandemic that triggered the economic downturn and officially implemented lockdowns, through a relatively prompt recovery with soaring demand and supply disruptions and then the economic impact of war in Ukraine. All of those developments brought concerns not only for macroeconomic activity and commodities markets but also the companies' payment liquidity. The economic volatility and fluctuations were confirmed by bumpy GDP growth rates. Indeed, while all CEE countries recorded negative growth rates in 2020 (with the exception of Lithuania where it was flat), 2021 brought mostly higher growth rates than a contraction pace recorded a year before. That helped to gain back the pre-pandemic nominal GDP level of CEE economies and the solid economy activity was continued also in the first half of 2022 despite materializing consequences of war in Ukraine. As a result, Croatia's and Slovenia's GDP growth exceeded 5% in 2022 while growth rates in Poland, Romania and Hungary were close to it. On the other hand, Estonia fell into recession with growth of -1.3%.

Macroeconomic volatilities were referred on the business side. As a reminder, the Covid-19 pandemic forced governments to introduce unprecedented measures to support households and companies. In terms of the latter it included moratoria on insolvency applications as well as various measures reducing consequences of pandemic impact on the liquidity situation of companies in order to save them from bankruptcies. Among other measures, those included exemptions and deferrals of taxation and social security contributions, furlough schemes, loans, subsidies and other financial assistance, guarantees, employees' salary supplementary payments and facilitating and simplifying various administrative procedures. As a result, support measures contributed to the drop of business insolvencies in 2020 as shown on chart 2. The process of their termination was gradual and companies still benefited from them amid low interest rates in 2021. Then, the year 2022 brought mostly an increase of insolvencies as companies suffered from challenges, including high prices of energy, inputs, series of prompt interest rate hikes, the highest inflation in decades, the uncertainty related to the war in Ukraine with a close geographical proximity to the CEE region.

The total number of business insolvency proceedings in CEE countries covered by our analysis rose from 25,917 in 2021 to 36,090 in 2022, i.e. by 39.3%. Statistics in a number of countries confirm the regional trend – after a drop of business insolvencies in 2020, those proceedings started to increase in 2021 and then accelerating in 2022. As shown in chart 1, last year eight countries experienced a higher number of insolvencies than a year before (Bulgaria, Croatia, Hungary, Latvia, Lithuania, Poland, Romania and Serbia), and four countries recorded a decrease (Czech Rep., Estonia, Slovakia and Slovenia). The highest surge of insolvencies was recorded by Serbia and Hungary (+106% and +86%, respectively), while the drop of proceedings was the largest in Estonia (by -17%). At the same time, the increase of insolvencies in CEE last year made that several countries already exceeded the pre-pandemic level of proceedings recorded in 2019 (chart 3). That included mostly Poland, where a number of proceedings was strongly contributed by a surge of dedicated procedures implemented to support companies suffering from liquidity difficulties due to the pandemic. Although intended to be temporary, the measures were implemented into Polish law permanently (see details on Poland's insolvencies on page 18). Even despite such a surge, the insolvency rate in Poland i.e. the share of total number of proceedings in the total number of active companies reached 0.08%, meaning that only 8 in 10,000 companies in Poland went through available official procedures. Much higher insolvency rates were recorded in countries were the usage of insolvency procedures is more popular – those rates reached 1.5% in Hungary, 2.1% in Croatia and 6.7% in Serbia. Especially, nominal insolvency figures were diverse across the CEE region, as they were not only affected by their economic situations but also by the definitions of insolvency in specific countries (with amendments to insolvency laws, or more widespread use of insolvency procedures).

Insolvencies increased not only in energy-intensive sectors

The increase of insolvency proceedings in the CEE region was expected due to unwinding the massive scale of support measures and raising challenges. Nevertheless, the payment situation has not bounced back immediately. As mentioned above there are still few CEE countries where business insolvencies are lower than in the pre-pandemic year of 2019. The similar phenomenon was also observed in the number of Western European countries. Moreover, business liquidity trends have hidden the increasing risk. For example, the latest Coface Payment Survey[1] confirmed that average payment delays for Polish companies decreased to 51.8 days in 2022 from 56.7 days in 2021. While it could be surprising that payment delays shortened facing various challenges, it was a result of companies' willingness to build up stocks of products and components to avoid suffering from ongoing price increases, therefore making payments even faster than requested. Also, macroeconomic data confirmed that inventories growth contributed on average to more than half of Polish GDP growth the last year.

Nevertheless, both payment liquidity and business solvency already deteriorated for energy-intensive sectors. Indeed, those ones suffered from soaring prices of commodities and therefore significantly higher operating costs. As a result, their weaker liquidity is confirmed in microeconomics data – in the Coface Payment Survey on Poland chemicals, metals, paper-wood and agri-food reported longer payment delays than the average while a bulk of them experienced lengthening of delays compared to a prior year. Furthermore, those sectors were also widely represented in regional insolvency statistics, mostly metals, paper, wood as well as agri-food reported high insolvency growth or accelerating insolvency rates. The agri-food sector is one of the evident examples that its agricultural part benefited from soaring commodity prices and resilient demand; however, on the other hand, it has suffered from high energy costs and fertilizers prices. The latter accelerated not only due to increased prices of natural gas which constitute the bulk of production costs of nitrogen fertilizers but also sanctions on Russia and Belarus that decreased supplies from such global producers and exporters. In Lithuania insolvencies of agricultural companies jumped by 70% in 2022 while lower but still double digit dynamics were also recorded in Bulgaria.

Construction is another sector that was often reported in cross-regional insolvency statistics of 2022. Insolvency rates (the share of insolvent companies in the total number of active companies in a given sector) were especially high in Croatia, Estonia, Hungary, Latvia, Lithuania and Poland. The construction sector has usually reported long payment delays; however, 2022 brought other challenges with it. Prices of building materials and inputs accelerated further and even those weakened in the late last year, they still remained higher than in past years. The previous contributor of sector's activity, i.e. the housing market slowed down due to the series

Chart 1:
Insolvencies in Central Europe

* Share of insolvencies in the total number of active companies

Total Insolvencies					Dynamics	Insolvency rate*
	2019	2020	2021	2022	2021/2022	2022
Bulgaria	405	488	516	532	3.1%	0.13%
Croatia	5,132	5,445	5,101	5,498	10.5%	2.08%
Czech Republic	1,081	978	1,035	1,024	-1.1%	0.25%
Estonia	264	330	268	222	-17.2%	0.08%
Hungary	5,187	4,053	4,359	8,111	86.1%	1.54%
Latvia	590	388	268	308	14.9%	0.21%
Lithuania	1,641	815	817	1,041	27.4%	0.85%
Poland	1,019	1,040	2,054	2,752	34.0%	0.08%
Romania	6,384	5,564	6,113	6,531	6.8%	1.12%
Serbia	6,446	6,096	4,445	9,149	105.8%	6.69%
Slovakia	445	330	388	347	-10.6%	0.17%
Slovenia	1,294	1,125	679	575	-15.3%	0.27%
CEE Total	**29,888**	**25,013**	**25,917**	**36,090**	**39.3%**	**0.54%**

Source: Coface

[1] *Coface Poland Payment Survey: Stock building makes payment delays shorter but only temporarily, December 2022 (https://www.coface.com/News-Publications/Publications/Poland-Payment-Survey-2023-Stock-building-makes-payment-delays-shorter-but-only-temporarily)*

of interest rate hikes executed by region's central banks and soaring inflation which eroded the disposable income of households. Furthermore, the increased uncertainty and proceeding economic slowdown made companies reluctant to conduct investments in fixed assets. At the same time, labour shortages remained an obstacle and even grow further partly as a result of Ukrainian men workforce returning to their home country to serve in the army. Some CEE countries, namely Hungary and Poland haven't taken a huge benefit of so-called EU recovery funds so far due to their clashes with the EU what limited the possible acceleration of infrastructural investments, among others.

Focusing on other sectors, retail constitutes a sizeable share of insolvencies in most of countries. Nevertheless, its insolvency rates and growth of proceedings were relatively limited in 2022. The exceptions are Baltics where insolvencies of trade companies went up by above 20% in Latvia and Lithuania as well as Poland. The large share of insolvent retail companies in total insolvencies could be attributed to the high number of sector's entities, especially small ones, in CEE countries in general. However it is anticipated that accelerating insolvency rates will follow as well. As it has already started in Baltics, stubbornly high inflation takes an increasing toll on consumer spending. Despite wage growth is still vivid in nominal terms in CEE countries, it turned to be negative in real terms making household consumption subdued. While the resilience of consumer spending lasted longer than expected and supported economies throughout 2022, it has lost the momentum and its contraction will not only make the regional GDP growth rate lower but also trigger further insolvencies in the sector. Inflation rates likely reached a peak in the first quarter of 2023; however, the disinflation process will not be so prompt to expect reaching inflation targets set by central banks already this year.

Chart 2:
Total business Insolvencies in CEE region

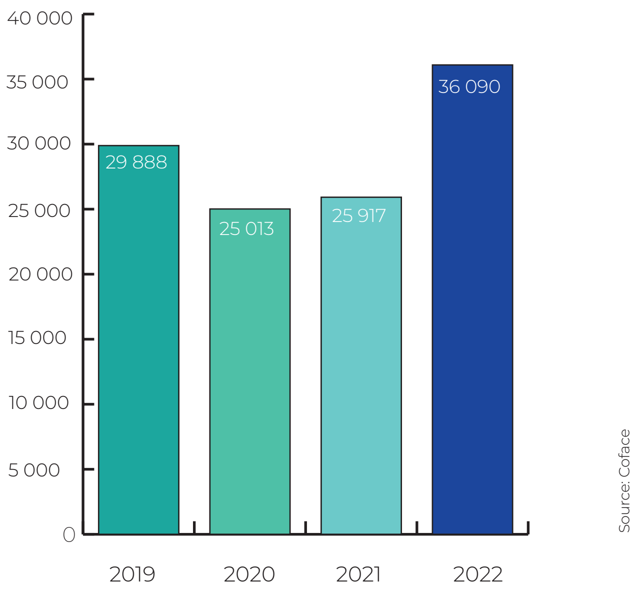
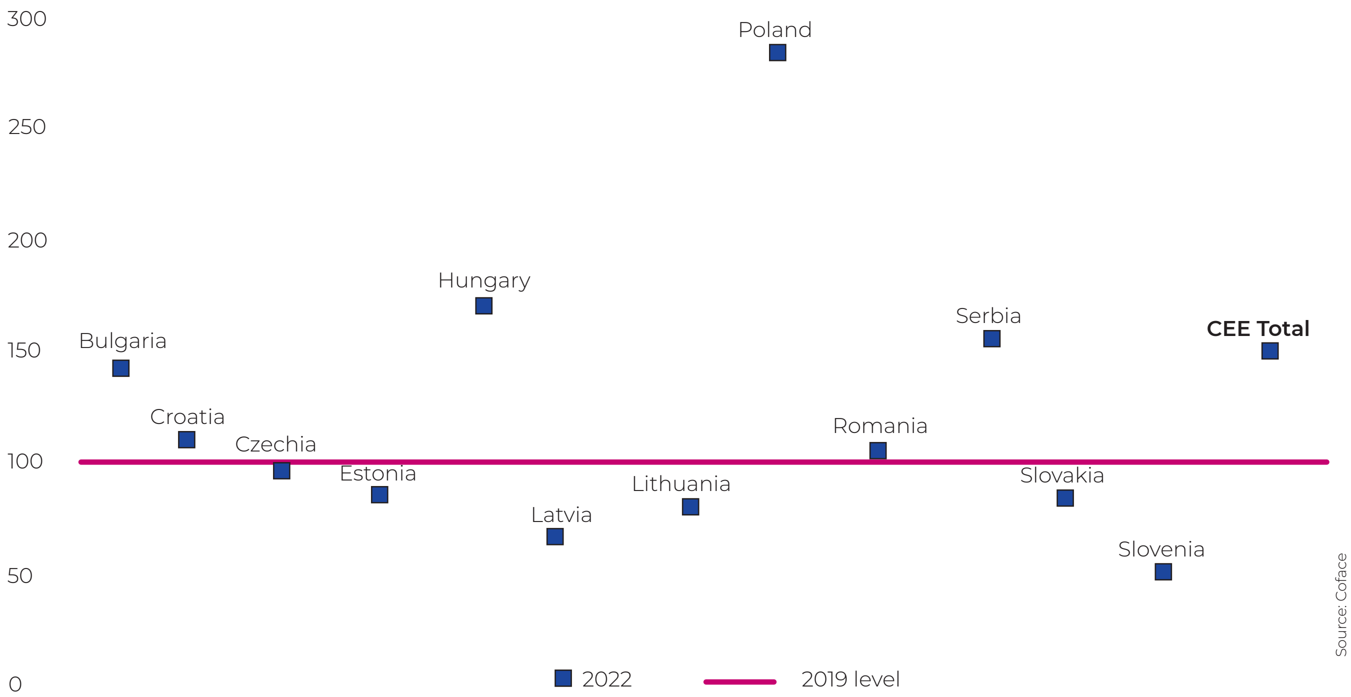


Chart 3:
Business insolvencies in CEE countries in 2022 compared to pre-pandemic 2019 (2019=100)



No time for recovery

2022 was a difficult year for CEE economies. No sooner had the COVID-19 pandemic passed, than Russia's invasion of Ukraine hit the world economy, and the economies of the region. From an economic point of view, international trade has experienced disruptions. Some of the disturbances directly concerned Ukraine. In 2021, the country produced nearly half of the world's exports of sunflower oil, 10% to 20% of other agricultural commodities (corn, wheat, rapeseed and barley), almost exclusively transported by sea (99% for cereals). After the start of the conflict and the naval blockade of Russia, Ukraine's trade was redirected to other countries, especially countries in the CEE region. In 2022, exports from Ukraine to Romania increased by 150%, while the increase was 51% to Slovakia, 40% to Hungary and 27% to Poland. With regard to trade with Russia, the European Union sanctions against it have led to a drop in exports from Russia to the EU (-36% from January to October 2022), but also in imports (- 41%), the Union to which most of CEE countries belong. EU sanctions against Russia have led to an increase in energy prices. Indeed, before the war with Ukraine, in 2021, 14% of world crude oil production was produced by Russia, of which more than 20% was exported to Europe. The European Union also imported 40% of natural gas from Russia. Apart from energy, the CEE region is dependent on some commodities from Russia and Belarus, for example fertilizers. The redirection of trade in commodities and energy has led to an increase in the prices of these two components. Inflation, mostly explained by the rise in energy and food prices, hit the countries of the CEE region harder than the countries of Western Europe, reaching two-digits figures. In 2022, the highest year-over-year inflation was recorded in Lithuania (19%), followed by Hungary and the Czech Republic (15%). In this context of high inflation, the growth of nominal wages was found to be lower than the growth of prices. Negative real wages have eroded household purchasing power and contributed negatively to demand (mainly driven by household consumption). Central banks in the CEE region reacted to this inflation by tightening monetary policy several times. From the beginning of 2022, the largest central bank interest rate increases were led by Hungary (from 2.40% to 13.00%), Romania (1.75% to 6.75%) and Serbia (1.00% to 5.75%), followed by Poland (1.75% to 6.75%), the Czech Republic (3.75% to 7.00%) and Bulgaria (0.00% to 2.47%). The rise in prices has also disrupted industrial production in the countries of the CEE region. While some countries have managed to maintain dynamic industrial production (Poland and Bulgaria, with annual growth of 11.1% and 12.9%), other countries have experienced negative or weak development (Romania, Slovenia and the Czech Republic with respectively -1.9%, 1.8% and 2.8%). Given the specializations of certain countries, this lower industrialization has had a direct impact on the Gross Domestic Product (in the Czech Republic, for example, industrial production contributes 30% of the added value of GDP). Despite difficulties on the world markets and the disruption of macroeconomic variables, the Gross Domestic Product of the countries of the CEE region has proved to be more resilient than expected. In 2022, large disparities were observed, between struggling economies (such as Estonia, with negative GDP growth of -1.3%), economies with low growth (Lithuania and Czech Republic, with 1.9% and 2.5%, respectively), or dynamic economies (Poland, Romania and the Hungary, with 4.9%, 4.8% and 4.6%, respectively). Despite the expected slowdown in the rise in world prices, a bulk of economies of the CEE region are expected to experience weaker growth in 2023. In particular, this includes inflation, which will remain well above central bank targets and continue to affect the solvency of companies. The number of companies in a situation of insolvency should therefore continue to increase during the year 2023.

Chart 4:
Gross Domestic Product (year-over-year change in %)

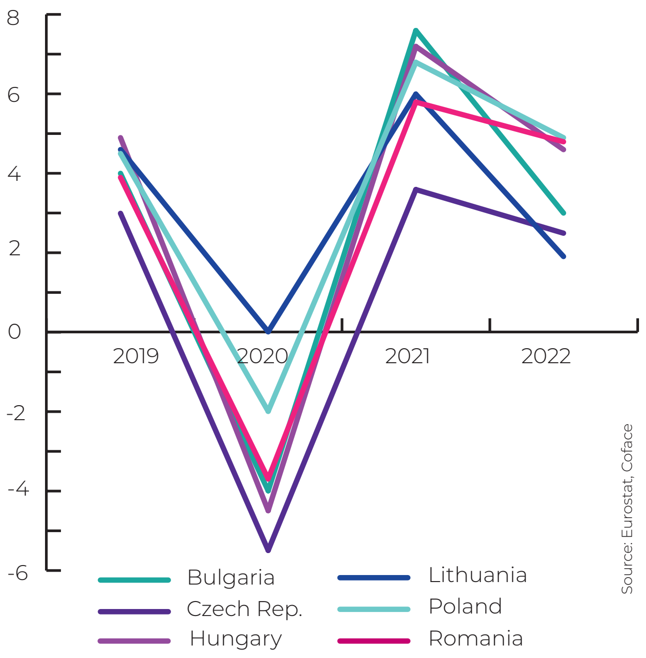
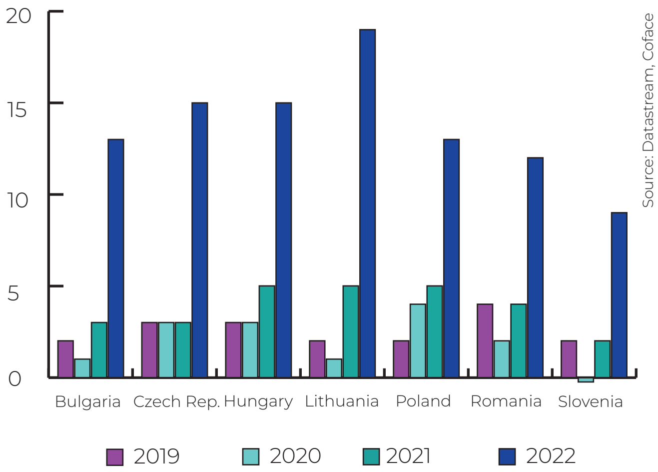


Chart 5:
Average annual inflation (Year-on-year evolution, in %)



2 Commentaries from country experts

Baltics

2021/2022 Insolvency dynamics
-17.2% Estonia
+14.9% Latvia
+27.4% Lithuania

Out of the three Baltic States, the number of insolvencies has increased the most in Lithuania followed by Latvia; however, in Estonia number of insolvencies actually decreased, As a matter of fact, Estonia is the only one of the three where the number of insolvencies has been decreasing ever since previous financial crisis of 2008 (with the exception of 2020 when the number of insolvent companies increased due to sharp negative effects on the hospitality and catering industry, which accounted for significant part of country's GDP). Traditionally the accommodation and food service industry has been the leading sector in terms of insolvency statistics in Estonia and 2022 was no exception. While in Lithuania and Latvia the most insolvencies in 2022 occurred in wholesale/retail businesses and construction followed by accommodation and food services, manufacturing and transportation. Nevertheless, despite the increase of insolvencies in Lithuania and Latvia, the number is still significantly below pre-Covid levels as business are still demonstrating resilience and adaptability to the changing economic environment.

Mindaugas Valskys

HEAD OF RISK UNDERWRITING
Coface Baltics

Croatia

+10.5 % Insolvency dynamics

After the anomalies in the trend of the number of opened bankruptcies in the two years of the pandemic (2020 and 2021) where we experienced the spread of the COVID-19 disease, 2022 is showing significant recovery and a return to pre-pandemic trends.

From the total number of insolvencies in 2022 there were 96.8% bankruptcies opened and immediately closed due to lack of assets (93% in 2021).

Data on the number of opened bankruptcies by activities and groups of activities tells us that the most bankruptcies were opened in the Coface sectors of Construction (27.43%), Business and Personal services (13.71%) as well as Non-specialised trade (13.14%). Sectors with the lowest number of opened bankruptcies were Financial services (1.14%) and Metals (1.14%).

The largest bankruptcy procedure in 2022 according to company turnover was opened for CELOX d.o.o. za trgovinu i usluge u stečaju, registered in the Non-specialized trade sector of activity. **(Sergej Simoniti)**

Slovenia

-13.3 % Insolvency dynamics

At the beginning of 2022, the COVID-19 pandemic was still having an effect on global economic activity. That being said though, the rest of the year was not without challenges as we all felt the impacts of the geopolitical situation. As a result, the Ukrainian crisis and instability in the energy markets also had an impact in Slovenia.
There were fewer insolvency procedures in 2022 than in previous years: the number of opened bankruptcy procedures was 15.3% lower compared to 2021 and almost 50% lower compared to 2020. In the last quarter of 2022, there were more insolvency procedures in almost all industries except trade, maintenance and repair of motor vehicles, then education, health, social care, culture and other service industries. When we consider the total number of bankruptcies opened during 2022, companies from the construction sector (25.39%) and service industries (21.39%) take the lion's share with financial services being the industry that seemed to get off lightly in comparison (0.87%).

Sergej Simoniti

COUNTRY MANAGER
Coface Adriatic Hub, including Croatia, Serbia and Slovenia

Serbia

+105.8 % Insolvency dynamics

Bankruptcy procedures still take too long, micro companies have the most problems

The global recession in 2020 caused by the Covid-19 pandemic has continued in 2022 as a result of the war in Ukraine. The economy is faced with an accelerated prices increase in the energy and food industry. Moreover, supply chains are being disrupted and company debts are rising to record levels as a result of previously taken loans. Bankruptcy procedures continue to take a long time, the number of active companies with 0 employees is going down very slowly (approx. 20 percent of the total number of active companies), and their current losses in the economy is always at a high level.
Also, the operations of more than 80,000 micro-enterprises (up to 9 employees) are burdened with numerous problems. For years, their business segment has continually experienced insolvency, low profitability, high levels of indebtedness and net losses. The main reasons for this lie in the slow implementation of structural reforms, the need for more favorable sources of financing and implementation of infrastructure for microfinancing, including lack of connection with foreign markets.

Too many companies in liquidation compared to previous years.

Year 2022 saw a large increase of companies forced into liquidation. This has been caused by decision from the Serbian Business Registers Agency (SBRA) in June 2022 when it implemented a forced shortened liquidation procedure. Conditions are: non-submission of financial statements; when a prohibition to perform activities would be imposed in the event that the company does not register its deletion, i.e. change of that activity; where there is a revocation of license in place and the company does not start regular liquidation procedure within 30 days from the day when the decision becomes final, and finally, when the company does not have any legal representative. For the first reason, it means if the company did not submit financial statements until the end of previous business year for two consecutive business years preceding the year in which the financial statements were submitted. **(Sergej Simoniti)**

Czech & Slovakia

2021/2022 Insolvency dynamics

-1.1% Czech

-10.6% Slovakia

Martin Procházka

HEAD OF RISK UNDERWRITING CZ&SK
Coface Czech

The year 2022 was very challenging. Companies faced many consequences of conflicts in neighboring countries, especially in broken supply chains, price volatility and the unavailability of materials or extreme growth of energy prices.

Despite that, the number of insolvencies in both countries declined, in CZ this was to about 1% to 1024 cases, in SK about 10% to 347 cases.

Number of bankruptcies and restructurings in CZ declined by about 3% to 724 cases, in SK this increased by about 4.5% to 302 cases. The rate of bankruptcies and restructurings on the total number of insolvencies has continued to grow.

The biggest insolvencies in the Czech Republic were experienced by Sberbank (financial institution with a direct relation to the Russian state lost the trust of Czech clients), NWT (wide range of activities including construction or agriculture, nevertheless the reason for their insolvency was the division of energy supplies).

The investment group Arca Capital and e-commerce retailer with clothes Dedoles were the victims of the biggest insolvencies in Slovakia.

From a statistical view, most of the insolvencies came from Wholesale & retail. Nevertheless this has been driven by wide range of activities under this classification. When looking at the sectors, the construction sector has the most visible significant presence in both countries, which corresponds with our experience with payment incidents.

2020 was very extraordinary year in both countries due to Covid. We can read the growth of insolvencies in 2021 as a return to normality. Our expectation for 2022 was much more negative, nevertheless the government reaction to the energy crisis contributed to a lower impact on households, so they were spared in the same way as companies thanks to government aid. Getting rid of the renewable sources fee, the price ceiling for small and middle companies and special compensation for energy intensive large companies – all of these measures limited the impact on costs and what is maybe more important, created a business environment that was much more predictable.

Improvements in the business culture, for example when companies come up with solutions to difficulties in good time and are able to obtain additional capital for the transition period, also contributed to a reduced number of insolvencies. This year we observed several such cases both in CZ and in SK.

In 2023 the companies have had to deal with growing interest rates, pressure on salary growth and keeping competitiveness on global market. Companies are exhausted and even if we are now observing a fall in energy prices and more and more positive sentiment in the business world, some business models will be not sustainable in a challenging environment. An increase of insolvencies is very likely but we do not expect anything dramatic here.

BULGARIA

2022 Insolvencies

3 Insolvencies in Bulgaria

Insolvencies in Bulgaria have continued to steadily rise by 3% on a YOY basis during 2022 and although this is not as much as in the rest of EU, it still follows the global pattern. Furthermore, the number of insolvencies during past year compared to last pre-pandemic year of 2019 is 7.5% higher, clearly indicating rising risks in the domestic economic environment. More warning signals are coming from the number of newly registered companies as well as companies in liquidation. The peak of new registrations was felt at the beginning of the year, but then concerns about the general economic environment and declining optimism led to a gradual cool down by the end of the year. Therefore, as a whole, the number of newly registered companies remained lower than the pre-pandemic year of 2019. These factors also contributed to a significantly higher number of companies in liquidation. In 2022 their number was equal to 4056, increasing by nearly 8% compared to the YOY basis.

As the process of insolvency in Bulgaria is rather conservative and long, it is worth noting that the number of companies in the process of bankruptcy is also increasing by 2.2% on annual basis to 536.

The market environment during the observed period was more than dynamic. It was not only business or economic factors which were affecting companies' financials, but the uncertainty of geopolitical tensions was also thrown into the mix. This was something we neglected entirely in the past, but now it's turning out to be one of the major factors of the current year. Alongside that we are also experiencing soaring costs, weakening consumer demand under the burden of high inflation and, after years of government support, companies were once again placed under pressures entirely unprecedented for our generation. Logic determines that it is precisely these factors leading to the increment of insolvency numbers.

Rumen Shikov

HEAD OF ENHANCED INFORMATION CENTER
Coface Bulgaria

Flop 5 sectors (the highest insolvency rates in 2022)	Insolvency rate 2022	Insolvency rate 2021
Paper products	0.62%	0.00%
Meat	0.32%	0.32%
Glass and ceramics	0.24%	0.00%
Wood	0.22%	0.28%
Petroleum & other hydrocarbons	0.22%	0.42%

Source: Coface

The above sectors are among the most affected by changes in global environment. Paper, wood and petroleum suffered from supply shocks: a direct result from disruption and changes in the global supply chain due to sanctions on Russia and their contra-sanctions. Shortages and a lack of quick substitute opportunity resulted in the decrement of activity and additional bankruptcies.

On other hand, glass and meat production suffered indirectly due to higher energy prices. This has proven very true for the glass segment, where activity is strongly linked to regular energy deliveries and has limited capabilities in reacting in the event of unexpected changes. The meat segment was also exposed to the rising cost of animal feed (due to the large share that Russia and Ukraine have in producing global cereal), but also due to quickly growing transportation costs.

Top 5 sectors (the lowest insolvency rates in 2022)	Insolvency rate 2022	Insolvency rate 2021
Leisure articles and miscellaneous	0.01%	0.11%
Textiles	0.03%	0.10%
Furniture	0.04%	0.24%
Financial services	0.04%	0.06%
Motors vehicles and motorcycles	0.06%	0.06%

Source: Coface

On the other hand, these 5 factors show resilient to the above-mentioned challenges. The common factor for them is that they were in focus over past few years due to oversupply (textile), Covid restrictions and disruptions of global networks (textile, leisure and automotive) and, generally speaking, the companies that reacted more flexibly remained. Financial services is a relatively new sector which is gathering speed with increment of economy and local fintech sector.

Leisure activities already suffered significantly during the COVID period. The return of outdoors activities as well as increases in international tourism has brought fresh air to this sector.

Furniture production is still following growing construction output in the residential segment and finishing works is related to that. Usually there is gap period between decrement of construction output and slowdown in sectors, so that in the short to middle term, changes could be expected here.

The largest company in Bulgaria to experience insolvency is Udineks. Udineks was engaged in trade of gas and registered to the newly constructed "Balkan" gas hub. Owned by Georgian citizens, the company was one of the biggest players in the sector until it entered bankruptcy during 2022. The main reason was cited as being too high customer concentration and the bankruptcy of their main customer, Secenergy Hungary.

HUNGARY

2022 Insolvencies

4 Insolvencies in Hungary

Liquidation proceedings initiated in Hungary in 2022

In 2022, a total of 8,111 liquidation proceedings were opened, which was almost double the 4,359 proceedings started in 2021. Looking at the sectors with the highest number of liquidations, the top six remained unchanged compared to last year: construction continued at the top of the list with 2,526 proceedings (1,280 in 2021), followed by services to enterprises with 985 proceedings (584 in 2021). The motor vehicles and motorcycles sector came in third once again with 795 cases. The sector has been battered by the economy in many ways over the past year, through shortages of electronic components and other raw materials, a sharp rise in purchase prices, exchange rate volatility, for example, and the list of negative events goes on. However, the full picture shows that the car manufacturers are not among the losers, despite the fall in production volumes due to the shortage of parts. The real losses have been suffered by Tier-1 suppliers (but by having a group background they are more protected), and by Tier-2 suppliers in particular, as they have had to face the negative effects of a backlog of orders without the support of being in a group. It is also worth noting that the 324 procedures launched in 2021 is significantly lower than in 2020 (414), but the 2022 figure is still well above the 2020 peak.

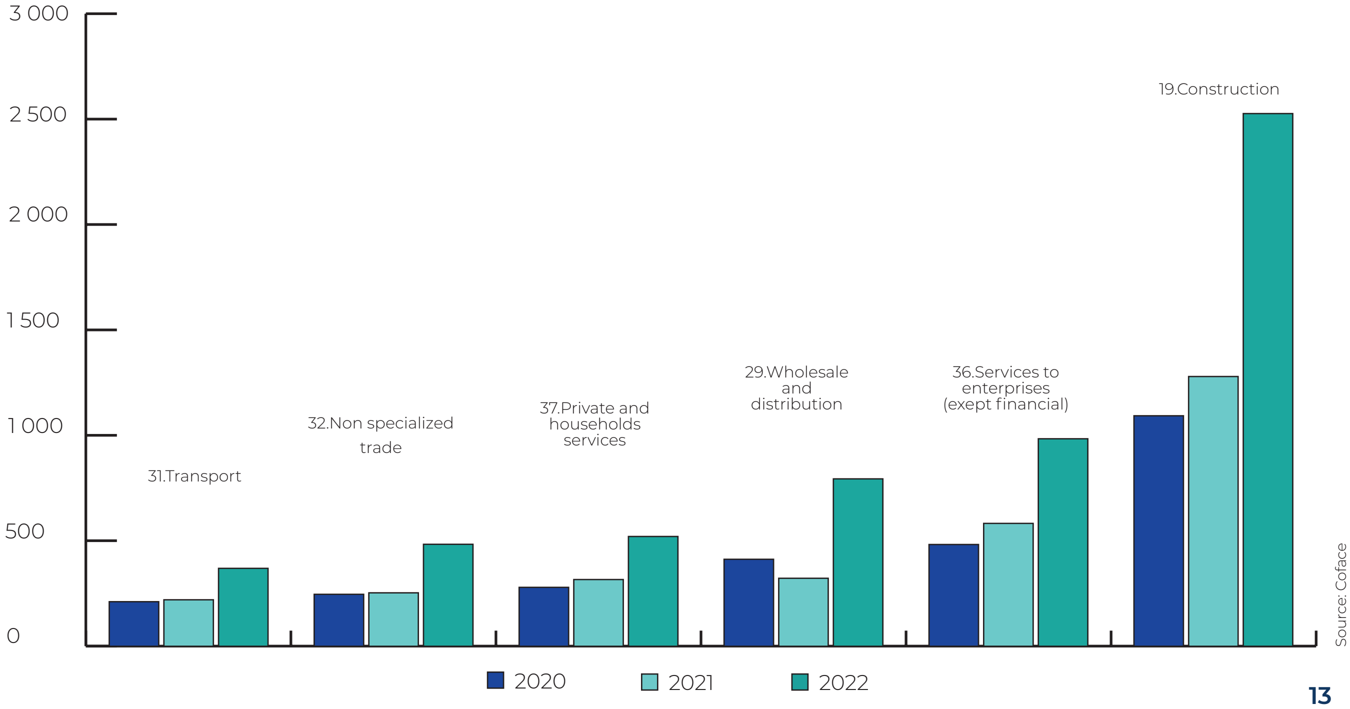
Services to households came in at fourth place again, with 522 liquidation proceedings, compared to 318 in 2021. Slightly behind was non-specialized trade with 485 (2021:255) and transport with 371 (2021:222) proceedings, which came fifth and sixth on the list respectively.

In terms of the sectors that appear to be the least

Henrietta Kiss

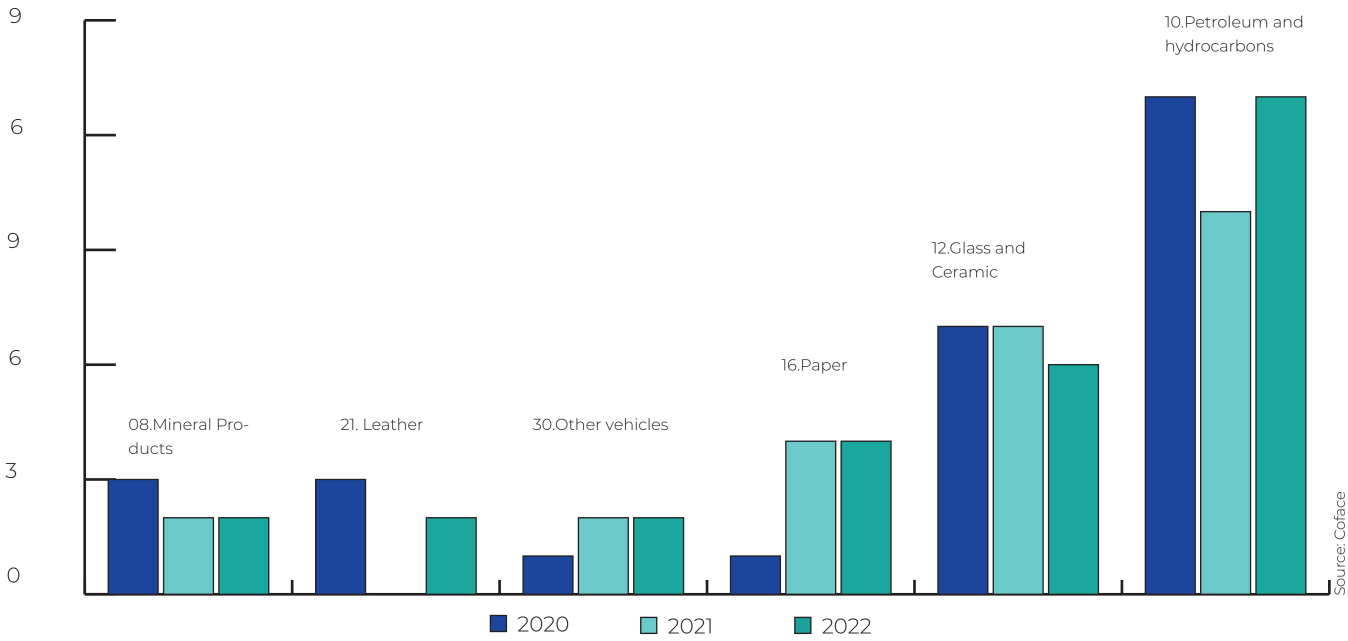
ENHANCED INFORMATION SENIOR ANALYST
Coface Hungary

Chart 5:
Hungary: Sectors most affected with insolvencies



vulnerable, there has been no substantial change. As in previous years, one or two liquidations already had a significant impact on the sector's position on the podium. For example, in 2022, two liquidations were launched in the leather sector (none in 2021), while mineral products and other vehicles also finished with 22 liquidations. However, it is also worth pointing out that there is a significant increase in the number of metal-related cases among the least affected sectors, even if the number of cases (29) is insignificant in itself.

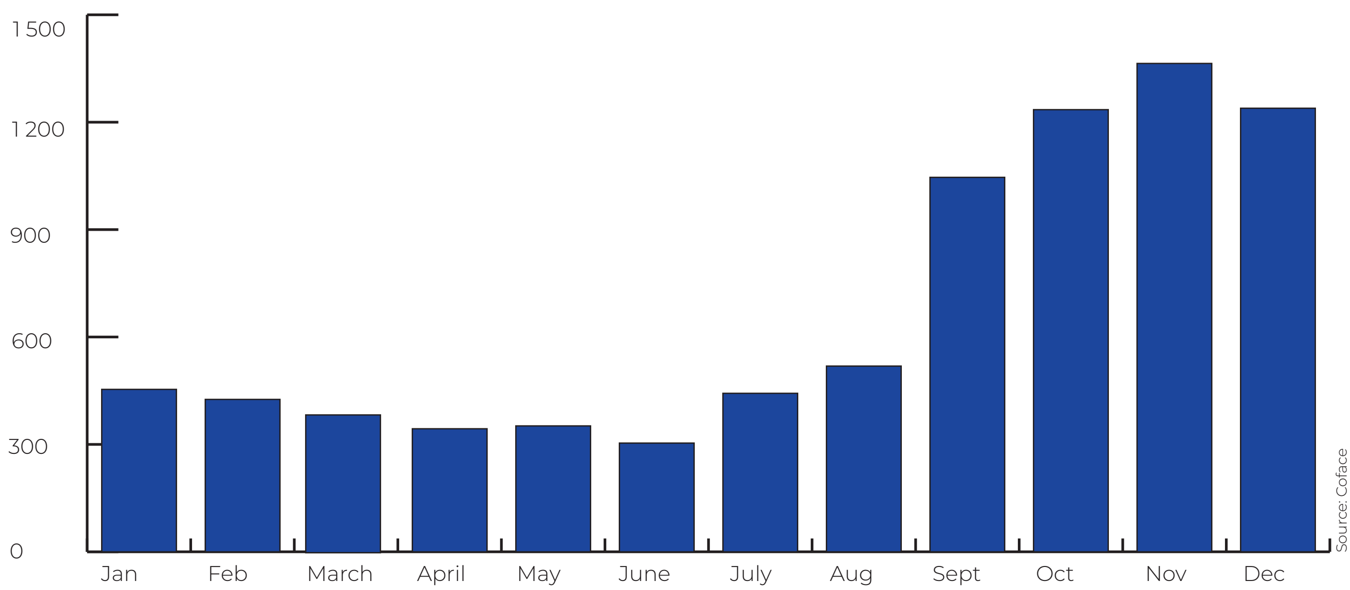
Chart 6:
Hungary: Sectors less affected with insolvencies



The temporal distribution of the initiated liquidation proceedings

However, when we look behind the numbers, an interesting fact emerges: nearly 60% of all proceedings opened in 2022 were launched in the last third of the year. In the first 8 months, an average of 403 proceedings were initiated – as shown in the Chart 7 – without minor fluctuations, with almost the same number of proceedings opened each month. The big question for 2023 is how long this trend will continue, when it will peak and when it will return to the 400-450 average number of proceedings seen in previous years. On the other hand, it is obviously not yet clear how much the establishment of new businesses will be able to offset and balance the number of liquidations.

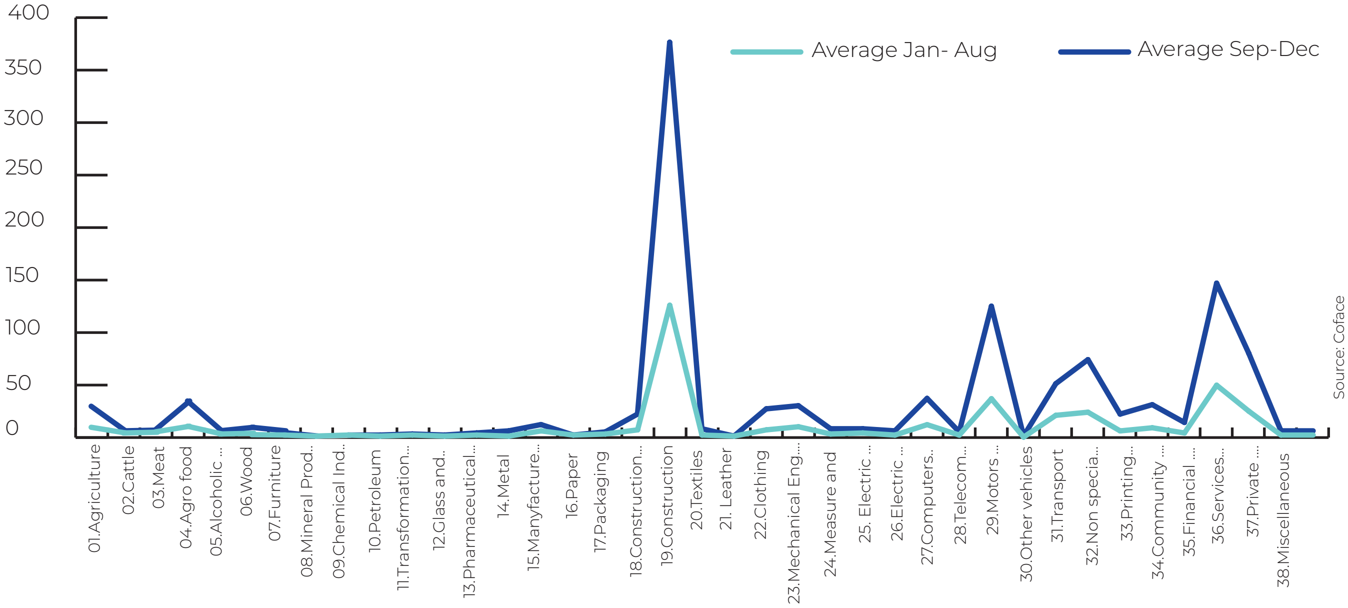
Chart 7:
Hungary: Liquidation proceedings in 2022



Industry breakdown of the initiated liquidation proceedings

If we examine these figures by sector, we can see that there has indeed been an increase in the average number of proceedings in almost all sectors, but there are some in which a clear rise in the proportion of firms in liquidation can be observed. These are construction, motor vehicles and motorcycles (which are of major importance for the Hungarian GDP), non-specialised trade and services to enterprises, which show significant variations and are therefore sensitive and risky. As the sector essentially covers key activities, services to enterprises are especially worth mentioning here.

Chart 8:
Monthly average of the liquidation proceedings (2022)



Cause and effect?

To understand clearly the significance of the above figures, it is important to see how many firms are operating in Hungary within a given industry.
According to the data of the Hungarian Central Statistical Office, the construction sector counts the highest number of liquidation proceedings, not only in terms of number but also in terms of proportion. Trade and motor vehicle repair is also significantly affected (both of these sectors were the top 6 sectors with the highest number of liquidation proceedings in 2022, but in terms of proportion, they don't even come close to the construction sector). Agriculture is clearly one of the least affected sectors, especially if the number of primary producers and individual entrepreneurs is included.
However, it is also worth noting that the overall number of registered enterprises has fallen sharply over the last quarter.
Exchange rate and inflationary effects are commonly cited as explanations for the rise in liquidations – we will not repeat these in this study, but rather focus on other factors. One important element is the changes in the industry output and input prices. For the sake of comparability, we will look at the two extremes: construction and agriculture. Agricultural output prices increased by 49% in the first three quarters of last year; one interesting fact is that the price increase for crop products (54%) outpaced that of animal and animal products (39%). Also in the input price area, the significant increase (46%) was mainly due to a 51% increase in the price of intermediate consumption components, while the price of related investment increased by 15%. The reasons for the increase include supply disruptions, rising energy prices and adverse weather conditions. By contrast, input prices in the construction sector did not approach the 50% level, according to the data from the Hungarian Central Statistical Office.
It is also worth including that while agricultural output was 15% higher in 2022 than a year earlier (total output was 19% higher, including 28% for crop production, 6.1% lower for livestock production and 1.0% higher for services), construction output overall increased by 3.0%, including 6.3% for buildings and 1.4% for other construction. In 2022, the volume of new contracts was 3.1% lower, within which the volume of contracts for the construction of buildings was 10.3% higher and that for other construction 17.3% lower.
However, it is also important to note that the major players in the construction sector are fundamentally stable, despite many years of shortcomings such as chronic shortages of skilled workers, efficiency improvements and related price levels, digitalisation, to name just a few.
Not so much the subcontracting sector, where the impact of the significantly reduced order numbers is finally being felt. The insolvency risk of small subcontracting firms – existing day-to-day, without reserves – could increase significantly in 2023. Projects postponed by the state until 2024-25 will play a major role in this. Whether the investments in the corporate sector can save the construction industry this year depends on many things. Even if they do manage to save the industry, projects will require planning, authorisation and other preparations, which means that even if there is investment, delays are already coded in terms of this year's performance.

POLAND

2022 Insolvencies

5 Insolvencies in Poland

The challenging year of 2022 ended with a 10% increase in corporate insolvencies ordered by the courts, and, also taking into account out-of-court proceedings, the total number increased by as much as 30%. Last year, companies were no longer supported by measures that had been put in place shortly after the start of the pandemic to limit the negative economic consequences while increasing challenges and the slowing economic activity created a more difficult business environment. High inflation began an obstacle not only to households, but also businesses, and its rise was further exacerbated by the impact of the war in Ukraine. Companies experienced cost increases, both through higher prices for components used in production as well as energy. Some were unable to operate in such an economic environment. This is confirmed by the insolvency statistics – in energy-intensive industries such as rubber, plastics and furniture production, for example, the rate of increase in insolvencies exceeded the overall average.
Still, many companies in liquidity difficulties opted for out-of-court proceedings, which were initially introduced temporarily as a countermeasure during the first phase of the pandemic, but due to their high popularity, it was decided to introduce them permanently into the legal system. In 2022, their share of the total number of proceedings reached as high as 63%. Unfortunately, not all of these attempts to regain liquidity have the desired effect – although a large increase in proceedings for the approval of an arrangement as the next, already judicial, stage of restructuring is noticeable, there is still not as many as out-of-court proceedings.
In macroeconomic terms, 2022 has not yet seen a significant deterioration in economic activity. GDP growth reached 4.9%, which was admittedly a weaker pace than in 2021 (6.8%), but the outlook for 2023 is much worse. Coface's forecast assumes that GDP growth will reach just 1% this year. Recent months have already confirmed the intensifying economic slowdown. This was quite quickly reflected on the business side with the aforementioned increase in corporate insolvencies. Admittedly, household consumption continued to support economic growth, however, the highest inflation in 26 years, the lowest level of consumer optimism, high interest rates and persistent uncertainty were already being felt by the retail industry, where insolvencies rose by as much as 57% in 2022. The worsening economy is also confirmed by the more than doubling of insolvencies in the transport industry, which is usually the first to experience an upturn as well as a downturn in demand and economic conditions.

Grzegorz Sielewicz

COFACE CHIEF ECONOMIST in Central and Eastern Europe

Inflation will remain the number one topic in 2023 as well. Although its peak is likely to be recorded in the first quarter of the year, elevated price levels will also remain in Poland during and beyond 2023. The energy crisis that Europe is experiencing was responsible for a significant increase in inflation. Energy commodity prices had already started to rise before the war in Ukraine, and its outbreak has further accelerated this process. Although Europe prepared for the current winter in terms of necessary gas stocks, many companies will continue to use this raw material in their production process even after the winter, when both stocks and prices remain a huge uncertainty. Furthermore, the next winter of 2023/2024 may be more challenging in this respect as infrastructure changes take time, even despite the many efforts of European countries in this regard.
The effects of rising energy and agricultural commodity prices in 2022 were experienced and their immediate impact has been partially mitigated by the measures introduced at government level. However inflation has 'spilled over' to other parts of the economy, as evidenced by the double-digit level of core inflation, i.e. the index after excluding energy and food prices. Unfortunately, despite a series of interest rate rises, this process has so far failed to stop and the consumer price index is well above the upper range of the inflation target set at 3.5%. Moreover, forecasts indicate that high inflation is staying in Poland

for longer. In all likelihood, double-digit levels of inflation will continue to accompany the Polish economy for the first half of the year, and a decline to around 7% in the last quarter of 2023 will be a poor relief. The inflation target is unlikely to be reached before 2025. Thus, it is difficult to expect that monetary easing will be initiated in 2023, i.e. the reduction of interest rates, which currently remain at their highest level since 2002.

Concluding the macroeconomic environment outlined above, the number of corporate insolvencies will increase, and their structure will unfortunately be fed more by bankruptcies, i.e. liquidation of companies, than restructurings, which could lead to the return to effective business activity.

Chart 9:
Poland: Insolvencies and restructuration proceedings

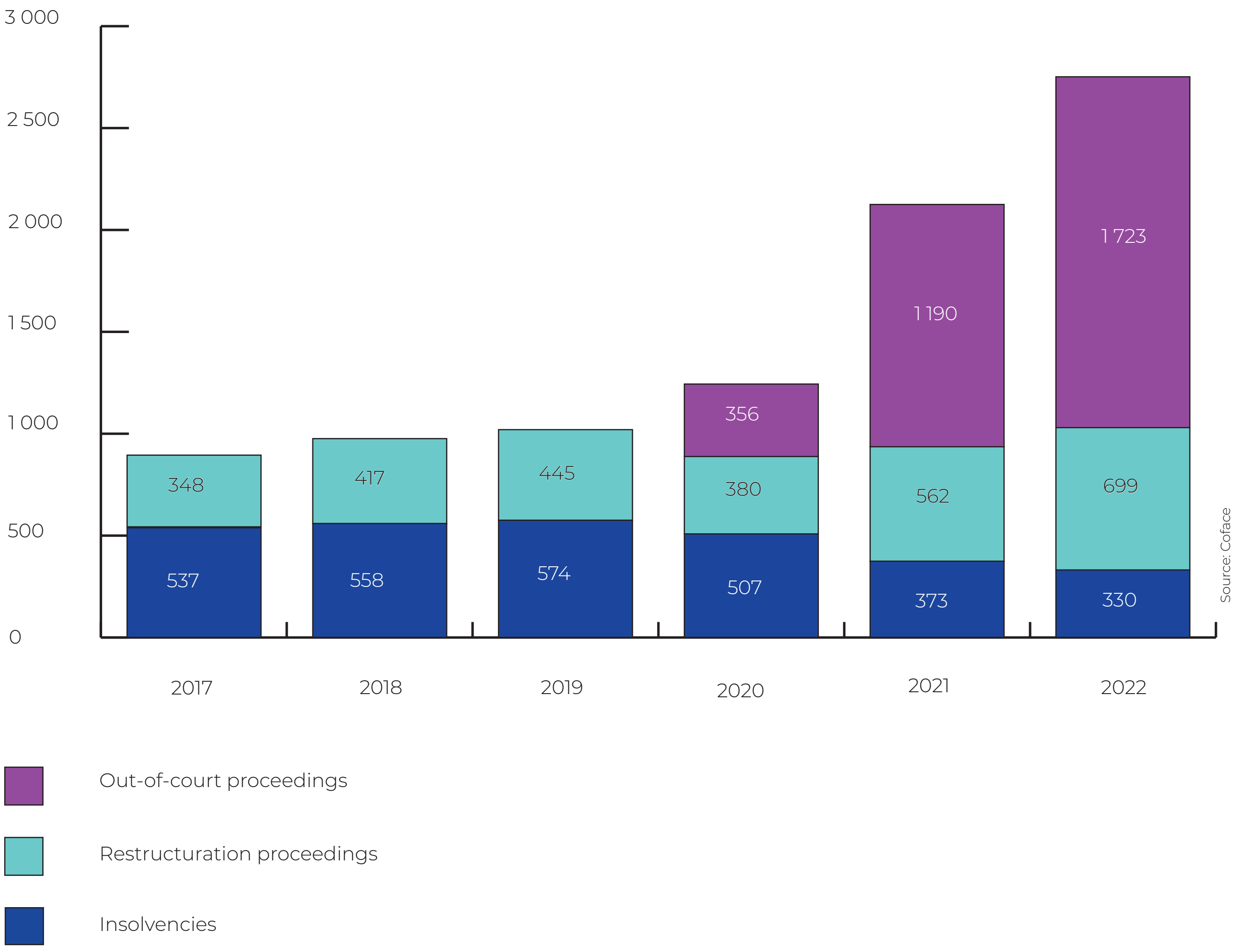


Chart 10:
Poland: Insolvencies and restructuration proceedings in sectors

Sector	Number of proceedings 2021	Number of proceedings 2022	Growth 2022/2021
PRODUCTION	**385**	**429**	**11%**
Manufacturing:	350	396	13%
Manufacture of basic metals and fabricated metal products	79	87	10%
Manufacture of food products and beverages	51	63	24%
Manufacture of furniture	22	37	68%
Manufacture of machinery and equipment	26	29	12%
Manufacture of wood products, except furniture	33	24	-27%
Manufacture of rubber and plastic products	16	24	50%
Manufacture of clothing and textiles	23	22	-4%
Printing and reproduction	13	18	38%
Manufacture of other non-metallic mineral products (including building materials)	15	17	13%
Manufacture of paper and paper products	11	12	9%
Other manufacturing	61	63	3%
TRADE	**399**	**567**	**42%**
Retail trade	170	267	57%
Wholesale trade	184	215	17%
CONSTRUCTION	**205**	**280**	**37%**
TRANSPORTS	**133**	**273**	**105%**
AGRICULTURE	**414**	**376**	**-9%**
SERVICES	**589**	**827**	**40%**
Professional, scientific and technical activities	145	195	34%
Human health and social work activities	74	120	62%
Accommodation and food service activities	92	105	14%
Leasing, administrative and support services	84	97	15%
Information and communication, including software services	36	77	114%
Real estate activities	69	68	-1%
Financial and insurance activities	40	62	55%
Education	17	33	94%
Arts, sports, entertainment and recreation	10	18	80%
Other services	22	52	136%
TOTAL	**2,125**	**2,752**	**30%**

ROMANIA

2022 Insolvencies

6 Insolvencies in Romania

Although a recession has been avoided, the economic context remains a complicated one, due to imbalances that generate risks and vulnerabilities for the population and the business community. Firstly, high and persistent inflation calls for tougher monetary and fiscal measures to raise the interest rates, tighten the control over liquidities and reduce the budget deficit. All these erode the traction of most important engine that has supported the Romanian economy in the recent decades: consumption. Thus, the turnover in the retail trade registered a continuous deceleration throughout 2022, the annual advance falling from about 10% in January, to about 2%-3% at the end of the year. Implicitly, the pace of economic growth slowed down from about 6% in 2021, to approx. 4% in 2022, therefore most economic forecasts for 2023 indicate a growth rate closer to 2%. The execution of the public budget for 2022 confirms the same structural problem from the past decades: the very small percentage of current public revenues as compared to the GDP. More precisely, in 2022 the current public revenues accounted for 28.6% in Romania, while the European average was about 40%. The inefficient collection of taxes and fees, coupled with the rigidity of budget costs (86% of tax revenues are directed to public sector salaries, pensions and other social transfers), generates increasing risks regarding new taxes for companies (the solidarity tax) or increases the existing risks (dividends and capital taxes, in general). Thus, companies face several growing difficulties: erosion of the purchasing power of the population due to persistent inflation over the dynamics of salaries, increasing costs of salaries, raw materials and energy, the fiscal risk due to the increase in taxes on capital, as well as the monetary risk related to the high level of interest rates, which discourage consumption and investment. In this context, the number of companies that became insolvent during 2022 increased by 7% as compared to the previous year, to 6,531 insolvent companies.
Over the past 3 years, the number of new insolvencies among the companies with revenues over EUR 0.5 million has increased, to 357 companies in 2022, as compared to 322 during the previous year. In this context, the losses caused by the insolvent companies to creditors remain at a high level, namely 4.6 billion lei. The sectors with the highest number of insolvent companies are as follows: Constructions, Retail Trade and Wholesale & Distribution, which account for almost half of the total number of the insolvencies registered in 2022. Out of them, the largest increase was reported in the Constructions sector (+20% vs 2021), which has the largest share of the total number of insolvencies (21%).
The general economic context and the increase in risks also generated the deterioration of the payment behavior.
Thus, during 2022, 28,814 payment instruments were refused for payment, a level similar to the one registered in the previous year. However, the total amount refused for payment in 2022 increased by 26%, up to 1.56 billion RON. At the same time, a total of 131,328 companies went out of business during 2022, up 12% from the previous year. Out of them, the largest share was generated by strike-offs (54%) and dissolutions (29%).

Iancu Guda

SERVICES DIRECTOR
Coface Romania

CHANGES IN THE NUMBER OF INSOLVENCIES

According to the data published by the Bulletin of Insolvency Procedures (BPI) and based on Coface methodology, insolvency proceedings were initiated for 6,531 companies in 2022. This is an increase of 7% as compared to 2021 or 2% as compared to 2019, when the insolvency procedure was initiated for 6,384 companies. It is also worth mentioning that, during the second semester of 2022, insolvency proceedings were initiated for 3,021 companies, down by approximately 14% as compared to the first semester of the same year, the dynamics being influenced by the reduced activity of the courts during the summer period.
In the past 3 years, an increase in the number of new insolvencies among the companies with revenues over EUR 0.5 million was noticed. Thus, as the following graphs illustrate, insolvency proceedings were initiated in 2022 for 357 companies with revenues over EUR 0.5 million, an

increase compared to 2021 when 322 new insolvencies were registered, but below the level of 2019 when 444 insolvencies were registered on the same segment. Despite the 7% increase in the total number of insolvencies registered in 2022 as compared to 2021, as well as the increase in the number of large companies (revenues over EUR 0.5 million) that became insolvent in the past two years, the financial losses generated to the creditors of the companies that became insolvent in 2022 amounted to 4.67 billion RON, down by 12% as compared to 2021.

Based on the financial statements submitted in the year before the year of insolvency and taking into account the main business object indicated by the NACE code, Coface distributed the companies that became insolvent in 2022 by the most important 23 sectors, the figures being indicated in the chart below.

Chart 11.
Distribution of insolvencies by sectors for past 2 years[1]

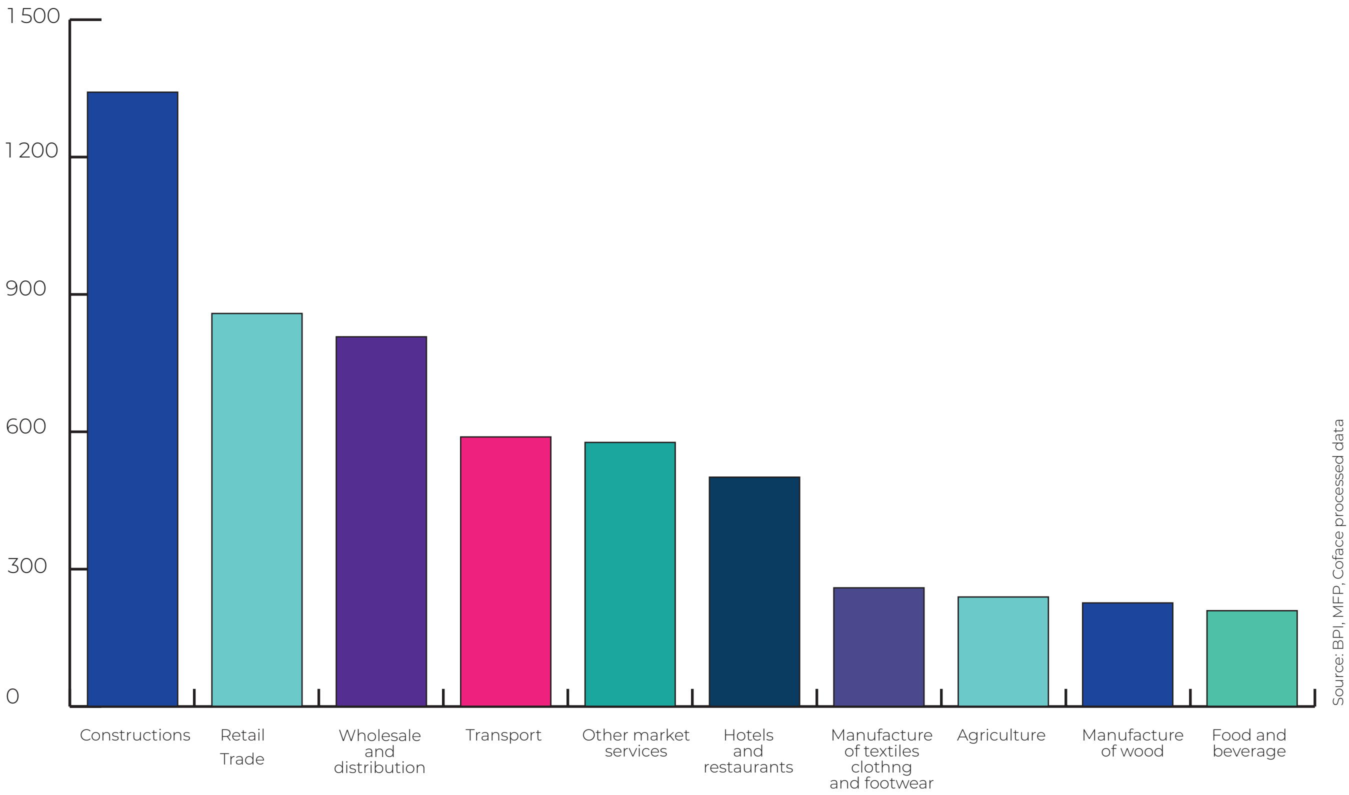
Sector	Insolvencies 2022	Insolvencies % Total	Insolvencies 2021	Insolvencies per 1.000 companies*
Manufacture of textiles, clothing and footwear	**258**	**4%**	**248**	**49**
Constructions	**1,342**	**21%**	**1,115**	**41**
Food & drinks industry	**208**	**3%**	**167**	**34**
Cleaning and waste removal; sanitation and similar activities	**67**	**1%**	**54**	**31**
Hotels and restaurants	**513**	**8%**	**564**	**27**
Extractive industry	**20**	**0%**	**22**	**26**
Metallurgical industry	**160**	**2%**	**160**	**26**
Manufacture of wood and wood products	**225**	**3%**	**158**	**23**
Transportation	**588**	**9%**	**565**	**20**
Post and telecommunications	**45**	**1%**	**36**	**18**
Agriculture	238	4%	258	17
Recreational, cultural and sports activities	86	1%	99	17
Wholesale and distribution	807	12%	833	16
Machinery and equipment industry	80	1%	61	15
Manufacture of chemical substances and products	41	1%	29	15
Other personal services	152	2%	136	14
Other services provided mainly to enterprises	576	9%	470	13
Retail trade	858	13%	847	13
Production and supply of electricity, heat, water and gas	11	0%	18	12
Financial intermediation	56	1%	45	10
Real estate transactions	74	1%	77	8
IT	78	1%	81	7
Health and social care	48	1%	34	5
TOTAL	**6,531**	**100%**	**6,113**	**19**

[1]By linear extrapolation of the companies that submitted their financial statements to the MFP in the year before the year of becoming insolvent. The first ten sectors with the highest number of insolvencies per 1,000 active companies were bolded (only companies with a turnover over EUR 1,000 per year during 2021 were considered active companies).

Even if we do not have the information on the main business for all the companies that became insolvent during the period[2] under analysis, there are two considerations on the basis of which we assess that the sectoral distribution within the entire portfolio is similar to the analyzed sample, as follows:
The weight of the sample is statistically significant for both years;
The sector distribution weights within the sample have values similar to the distribution weights within the entire portfolio, registered in the annual studies conducted by Coface.

Just like in the past few years, the top 3 sectors by number of insolvent companies (Constructions, Retail Trade and Wholesale & Distribution) concentrated about 46% of the total number of insolvencies in 2022. Out of them, the highest increase in the number of companies that became insolvent was registered in the Constructions sector (+20% vs 2021), which has the largest share of the total number of insolvencies (21%). This trend was noticed in the previous Coface studies mainly due to the high level of indebtedness of such companies, combined with the decrease in lending to the residential segment due to the significant increase in interest rates. We believe that the large number of companies that will become insolvent in the Constructions sector will continue in 2023 considering that, according to the National Institute of Statistics, 43,600 building permits have been issued in 2023 for residential buildings, down by about 15% as compared to 2021. In addition, if we take intoaccount the number of building permits for residential buildings issued in December 2022 (2,691 permits), we see a decrease of about 33% as compared to the same month of 2021.

Chart 12:
Top 10 sectors in terms of number of insolvencies in 2022



[2]*Such data can be calculated for approximately half of the insolvent companies.*

7 Manage your risks

One of most common reasons a company or business becomes insolvent is failure of its clients to pay owed money. The analysis of credit worthiness and payment behaviors of customers or business partners is critical element of non-payment risk prevention.
Coface international risk underwriting and economic research teams assess and monitor business risks on a daily basis. In addition to our information on more than **200 million** companies across the world, including **40 million** in Central and Eastern Europe, we have access to the best available global data sources to monitor world events.

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Dorota Angotti

REGIONAL BUSINESS INFORMATION DIRECTOR

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Quantification of the relative strength of a country's fundamentals and its vulnerability to shocks, as measured by companies non-payments. Expressed on a scale from A1 to E.

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