



Creditreform Latvia SIA
credit management survey

**TRADE CREDIT AND PAYMENT
DELAYS IN COMMERCIAL
TRANSACTIONS AMONG
BUSINESS ENTITIES IN LATVIA
IN 2011.**

RESULTS OF SURVEY

May 2012

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INTRODUCTION

SIA Creditreform already fourteen years has provided a survey in Latvia of condition of the sale and late payment trends in commercial transactions among legal entities in the domestic market. The aim is to research the situation in Latvia of late payment in various business sectors, to clarify the changes in the customer bill payment discipline, what problems are caused by late payment and how problems are solved.

The survey in a random check was carried out in business sectors in which selling goods and services on post-paid payment are essential. Thank you to everyone who participated in the making of this research.

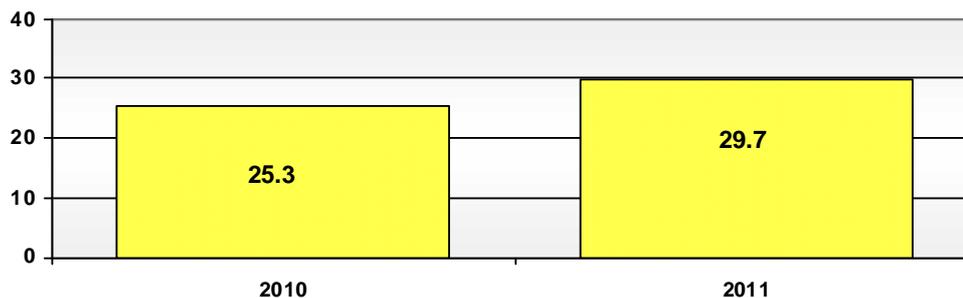
In 2011 Latvian economy continued to successfully recover from the crisis. Credit management research on the 2011 sales terms and late payment trends gives a positive expectation even though the actual situation and mood in the country is not so positive. Last year in Latvia rapidly reduced the proposed number of insolvency, but it is still not small, and doesn't give rise to a relaxation. It should be noted that the year 2010 was the highest point of the global crisis, when the initiated number of insolvencies was also the largest - 2813, in 2011 it had fallen to 1651, which is 41.3% less, however, the number remains considerable. Gross Domestic Product in Q3 by 6.6% exceeded over the previous year's quarter. As compared to the lowest point of crisis in the Q3 of 2009, it increased by 9.6%. The increasing risks in foreign markets, especially in the Euro zone, haven't significantly impacted Latvian economy; therefore remaining external demand, exports of Latvian goods and services continues to grow.

CONVENTIONAL TERMS OF PAYMENT

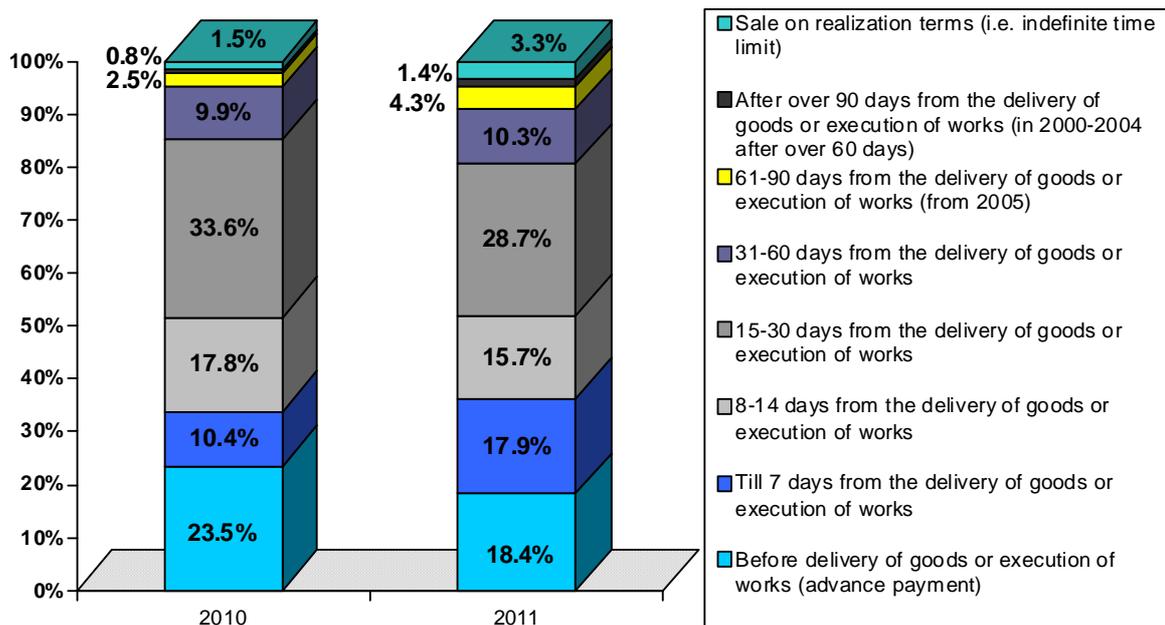
Last year, many entrepreneur with more confidence operated with the post-paid payment. This is due to the both small improvement in the economic situation in the country, and also during the crisis weeded out insolvent and financially questionable enterprises. Those customers who have successfully survived the crisis and kept the confidence of business partners can expect to pay non-contentious payment conditions. However, a significant part of entrepreneur don't make their activities to the additional risk and most of the deals are closed only with pre-payment (in advance).

In 2011 the average contractual term of payment transactions was 29.7 days after delivery of the goods or execution of works and it is 4.4 days or 17.4% longer than in 2010.

Picture 1. The average contractual term of payment transactions in 2010-2011



Picture 2. Contractual payment terms in Latvia in 2010-2011



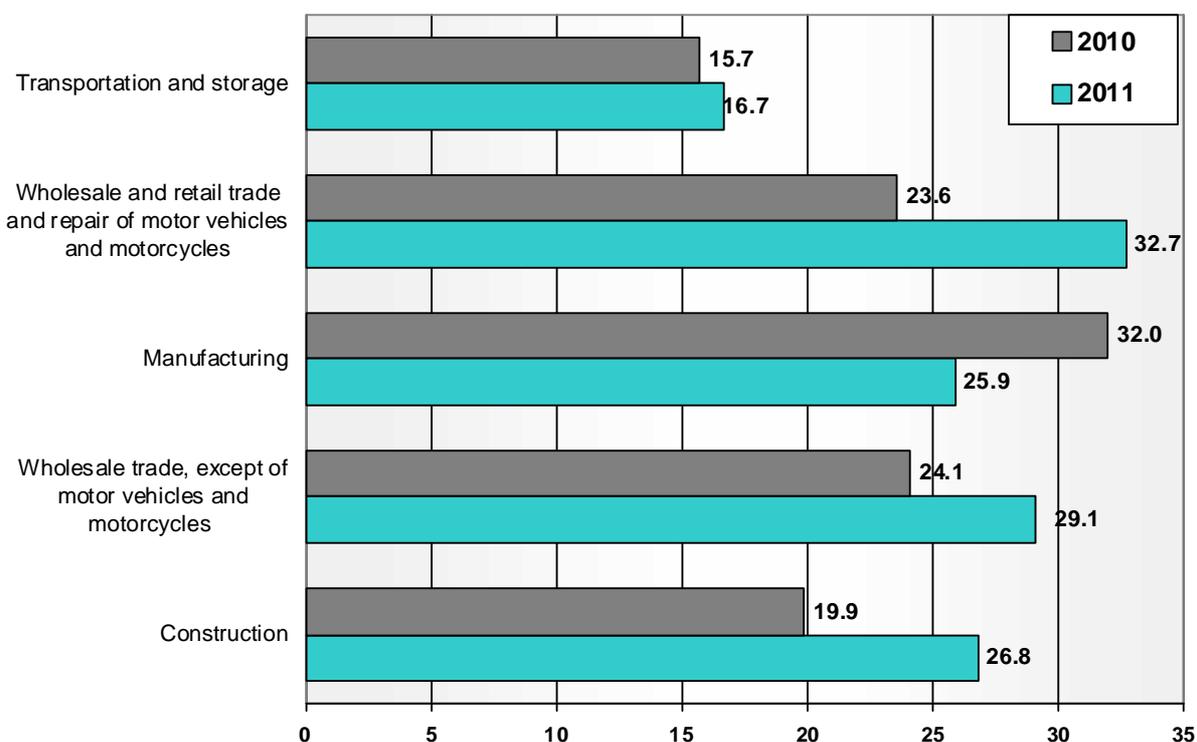
The research shows that during 2011 by 5.1 percentages point decreased the number of transactions with 100% prepayment. At the same time, the largest increase (+7.5%) observed in transaction with small post-paid transactions for up to 7 days representing 17.9% of all transactions. In total the conditions of payment before delivery of goods and transactions with a maturity of up to 14 days after delivery; in 2011 they account for 52%, which is only about 0.3% more than in 2010, which shows that, overall entrepreneur's precaution remains. In 2011 is also seen another trend - half the number of transactions has increased, where a conventional payment term after the delivery of the goods is more than 61 days. In 2011 such transactions account for 9%, while in 2010 they were 4.8%. Traditionally, the majority of customers the deadline for payment of the transaction is set within 15-30 days after delivery of the goods or execution of works. In 2011, the following terms in contracts provided 28.7% of respondents that compared with 2010 are of 4.9% less.

In terms of industries an interesting trend reflects construction industry companies - the average down payment in 2011 in the *construction industry* is 26.8 days, which is a rapid extension, compared with 19.9 days in 2010. Due to the increase of investments in the country, after a considerable decline in 2010, quite rapidly revived construction market, especially in Riga and Jurmala. Increased investment activity last year was also observed in power industry, wood processing and transportation and warehousing industries. The reason for the positive results in the construction industry is more active European Structural Funds acquirement and allotted funds. Currently the construction industry has a tendency that domestic demand is growing slightly faster than the supply of construction companies. It is based on qualitative and competitive labour shortages in certain specialties. Sized down payment deadlines is also influenced by the fact that the construction industry order objects and the transaction amounts become larger, and transitional periods for which payments are made, are defined longer. While the construction companies who acquire European structural funds, will benefit only after a complete execution of work or stage. However, obviously more rapid rise in investment limits slow recovery of private sector crediting and insufficient funds available to entrepreneur for investment funding.

Payment terms in agreements for goods or services drowned out for the wholesale and retail trade and repair of motor vehicles and motorcyckes industries from 23.6 days in 2010 to 32.7 days in 2011. Contractual terms increased also in wholesale trade, except of motor vehicles and motorcycles industry companies (from 24.1 day in 2010 to 29.12 days in 2011) and in transportation and storage industry companies, where the changes are very small - from 15.7 days in 2010 to 16.7 days - in 2011.

Average down payment terms decreased only in the manufacturing industry. In 2010 in the manufacturing industry companies the down payment terms was 32.0 days, while in 2011 it decreased by 6.1 days and makes on average 25.9 days. Strict payment terms also significantly impacted the effectiveness of cooperation; as a result manufacturing industry companies in 2011 experienced a sales increase, particularly in export. This is one of the most important Latvian national economy recovery process guides. Level of capacity use in manufacturing at the end of 2011 amounted to 69.4%, suggesting that the current level of production is close to possible future. It can be noted that the export market is growing faster than the internal market.

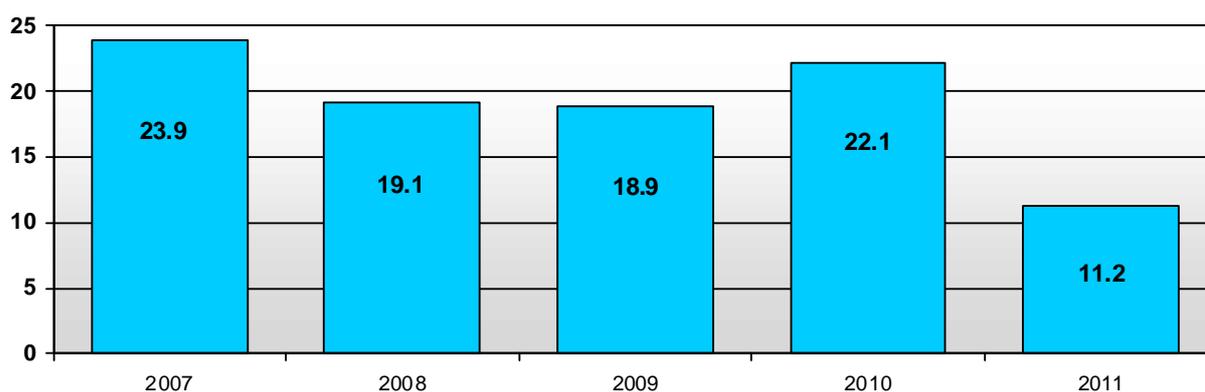
Picture 3. Average contractual payment terms in individual business sectors in 2010 (in days from delivery of goods or execution of works)



AVERAGE PAYMENT DELAYS

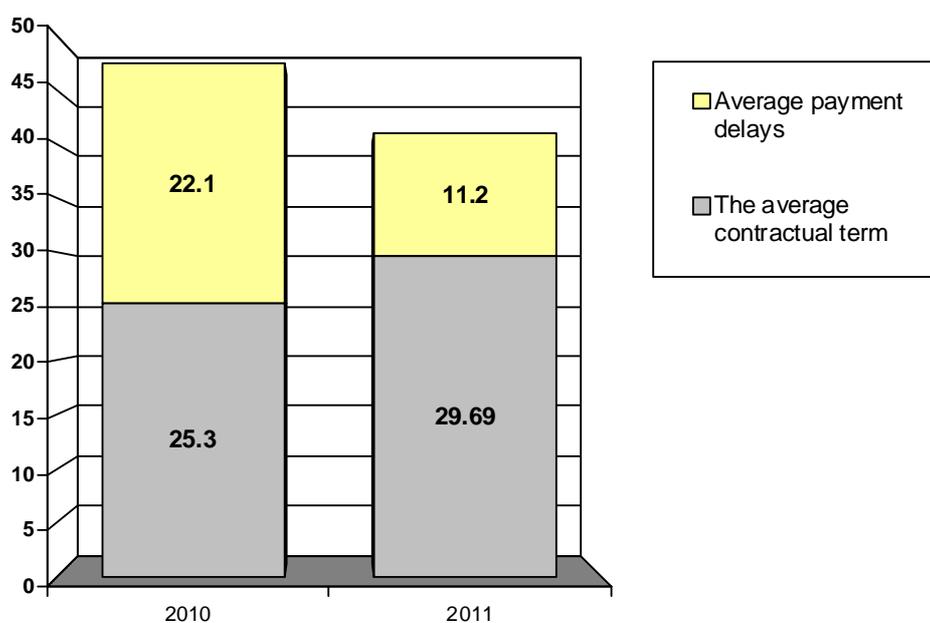
Businesses with post-paid conditions in 2011 have increased, but mostly they are closed with a reliable and proven cooperation partners. This is shown by the late payment rates, which declined sharply in 2011. In 2011 the average payment delay is 11.2 days, which is by 10.9 days shorter than in 2010. Compared to previous years, in 2011 is achieved the lowest rate of late payments. Partly this is due to the crystallisation of the market - in previous years weaker companies due to the competition or poor management went into insolvency or bankruptcy. The other part, which went through a serious crisis, accumulated experience and now expands activity on various financial and business risk reductions.

Picture 4. Average payment delays in Latvia in 2007-2011



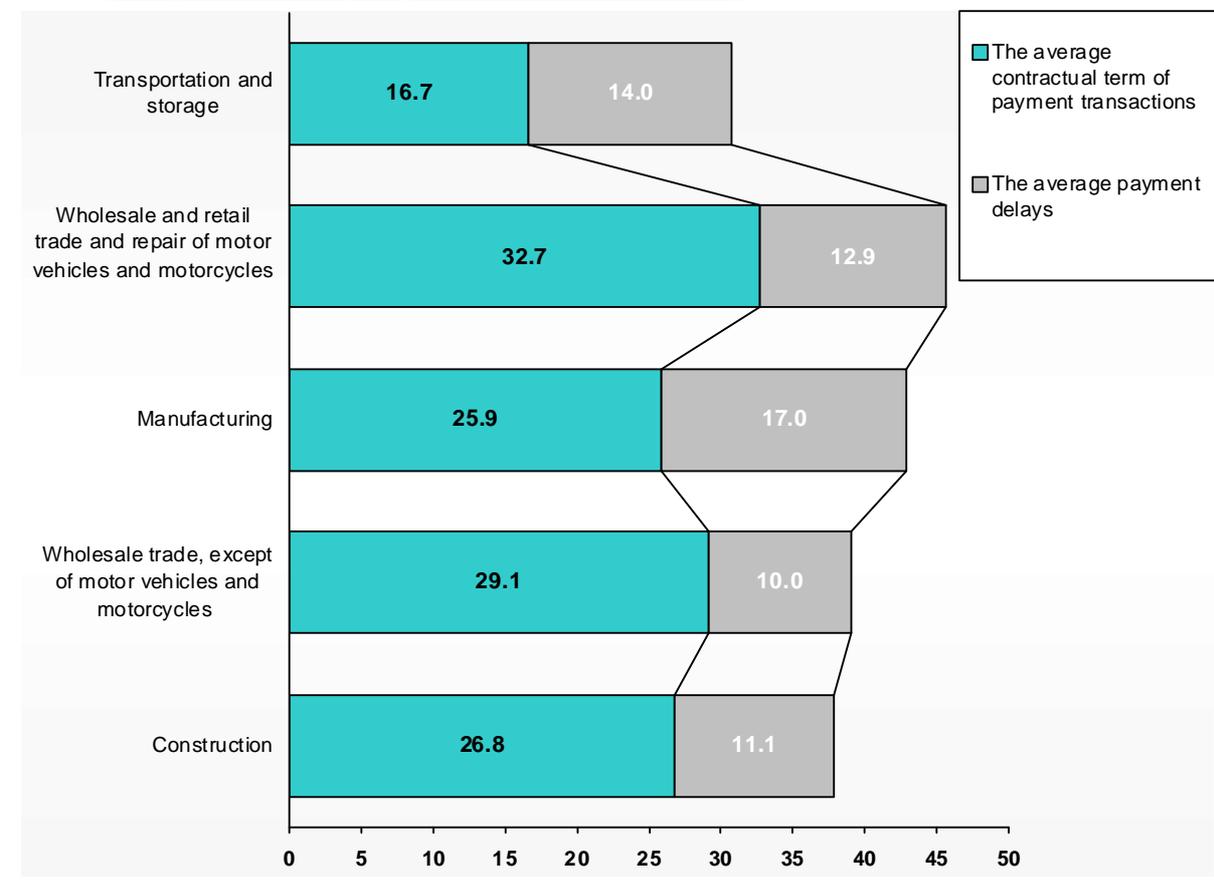
The survey data shows that in 2011 generally accelerated turnover of debts of debtors (counting the average contractual term with the average late payment days) making an average of 40.1 days after delivery of goods or execution of work, when in 2010 it was 47.4 days.

Picture 5. Accelerated turnover of debts of debtors, 2011



When looking at the turnover of debts of debtors by sector it shows that in 2011 it was faster in the transportation and storage industry companies, as well as in wholesale trade companies, except of motor vehicles and motorcycles industry companies accordingly 30.7 days, respectively, and 39.1 days. While the payment for the sale of goods or services the longest were forced to wait the wolesale and retail trade and repair of motor vehicles and motorcycles industry companies - 45.6 days.

Picture 6. Average amounts receivable movement in the individual business sectors in 2011.g. (in days from delivery of goods or execution of works)



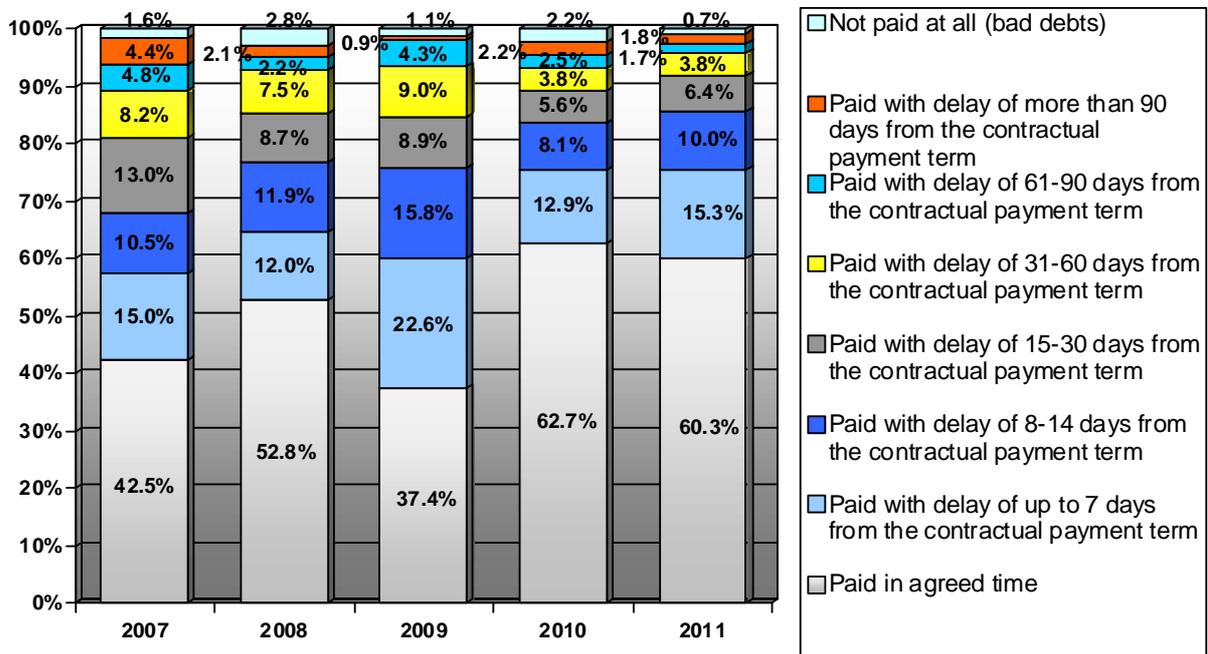
Remaining the positive trends in export is expected that also in 2012 will continue to raise manufacturing production volumes. In January of 2011 manufacturing industry production volumes were 11.9% higher than previously. There remains a tendency to increase production volumes of all manufacturing sectors, especially in the production of woodworking, metalworking, electronics, machinery and equipment. Overall, the manufacturing industry provides an average of 1/3 of total economic growth.

LATE PAYMENT STRUCTURE

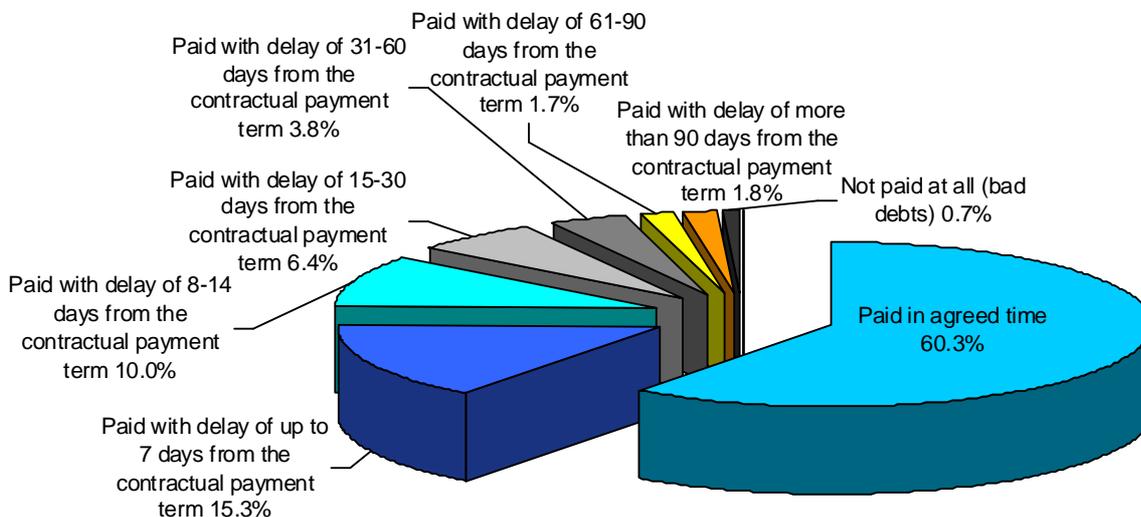
As the research shows, during 2011 slightly decreased the number of invoices paid timely. However, taking into account that part of the late payments are developing as a result of various external conditions and often it is not wilful default, that part of customers whose payments are paid on time or with a delay of 30 days in 2011 was up 92% of all transactions.

Delay over thirty days is considered a significant delay and shows the customer's/cooperation partner's solvency problems or complaints regarding the goods or services received. In 2011 continues to decrease the number of such transactions with payments delays over 31 days after delivery of the goods or execution of works. Long-term debtors (payment delay over 31 days) amount of unpaid bills in 2011 accounts for 8%, which is of 2.7% less than last year. While in percentage a little has increases the number of transactions with the bill payment delays from 8 to 14 days and from 15 to 30 days.

Picture 7. Payment delays in Latvia in 2007-2011



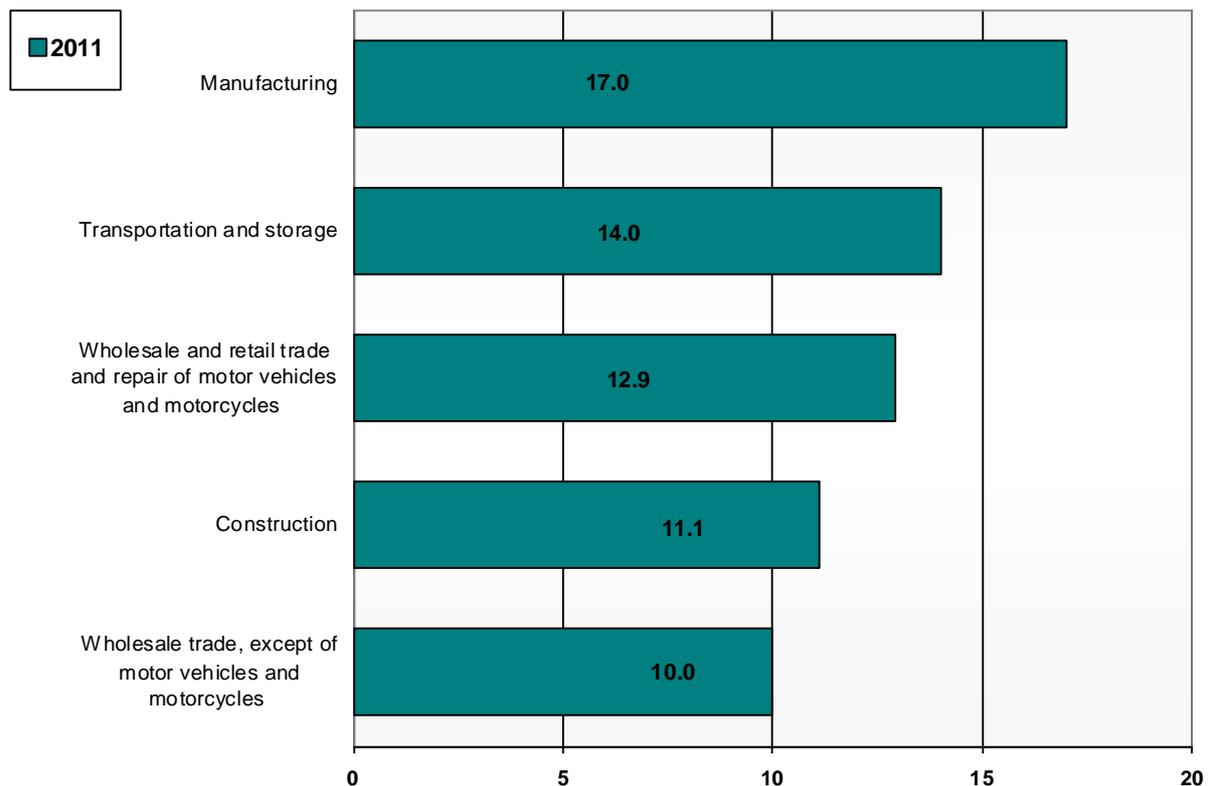
Picture 8. Payment delays in Latvia in 2011



The survey data show that the in 2011 the last were paid the bills of manufacturing industry companies (the average delay of 17.0 days). The most long-term debtors in 2011 are characteristic for the manufacturing industry companies - 10.4% of customers paid the bills with a delay over 31 days. Almost as much long-term defaulters are also to wholesale and retail trade and repair of motor vehicles and motorcycles companies - 10.3%.

While the fastest payment for goods or services in 2011 received wholesale, except of motor vehicles, industry companies - 10 days. Slightly higher figure in 2011 was for the construction industry companies - 11.1 days. This is largely due to the increase of industry services inquiry and essential European Union structural funds absorption.

Picture 9. Average payment delays in certain business sectors in 2011 (in days from contractual payment term)

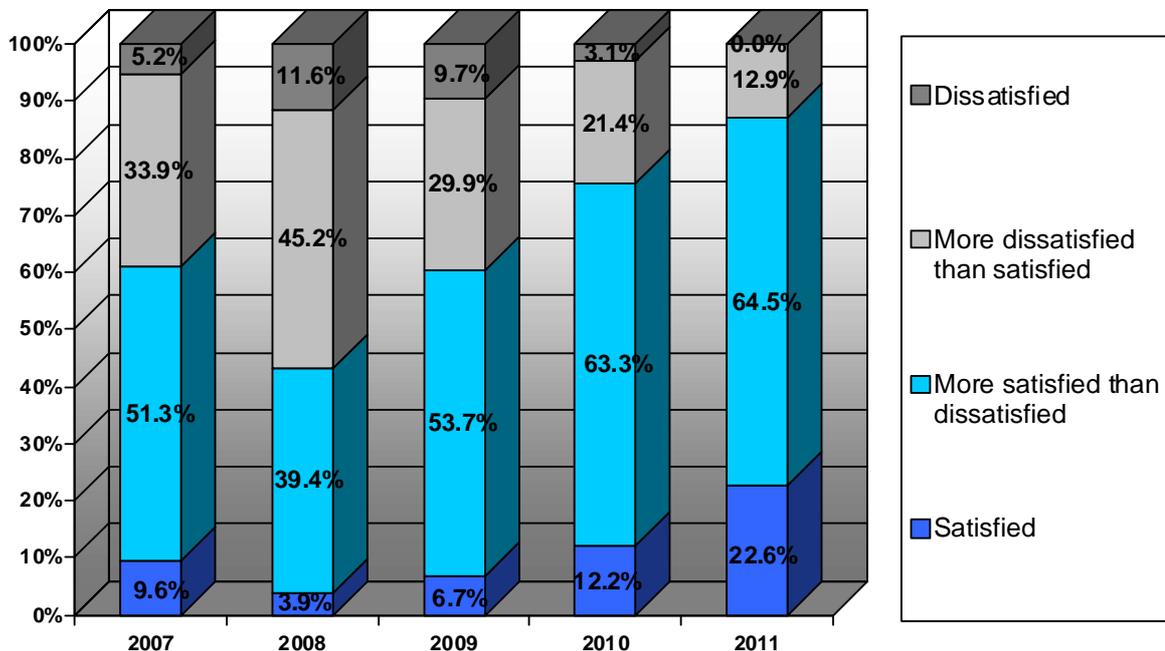


CUSTOMER PAYMENT DISCIPLINE

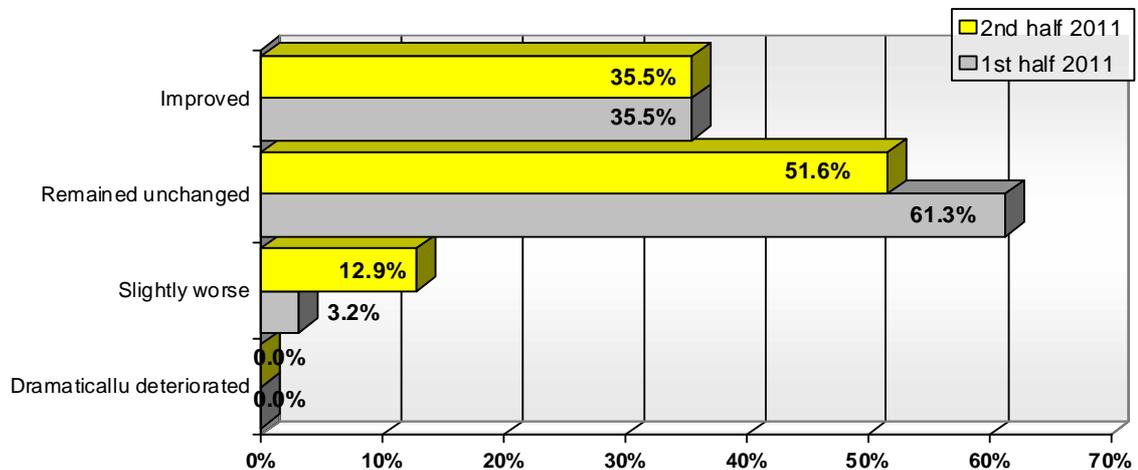
By improving customer payment customs, by reducing the amount of delayed payment and terms, entrepreneur satisfaction with the customer's payment discipline has grown also in 2011. By half (from 12.2% to 22.6%) increased the number of satisfied entrepreneur and reduced to a minimum the number of dissatisfied entrepreneur with the customer paying habits in 2011. This suggests that for the allocation of deferred payment, entrepreneur more carefully evaluate the customer's credit history to help predict the behaviour of cooperation partner's in payment transactions. In their turn to potential, new customers more carefully are evaluated prior history of payment transactions. Entrepreneurs in 2011 tried to minimize the risks of unpaid bills.

A large majority of respondents indicated that during 2011 customer payment discipline has improved, however, much of the customer payment habits kept the level of 2010. It can be noted, however, that an important part of entrepreneur (12.9%) in the 2nd half 2011 experienced a slight worsening of the situation in relation to the customer payment habits.

Picture 10. Satisfaction with the customer's payment discipline in 2007-2011



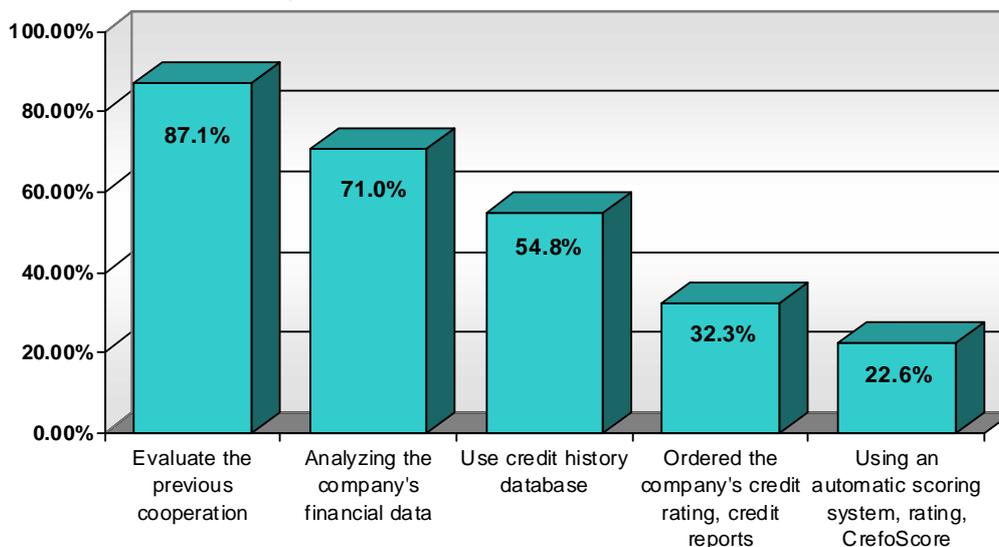
Picture 11. Customers' payment discipline changes 2011th year



CUSTOMER ASSESSMENT AND LATE PAYMENT CHALLENGES

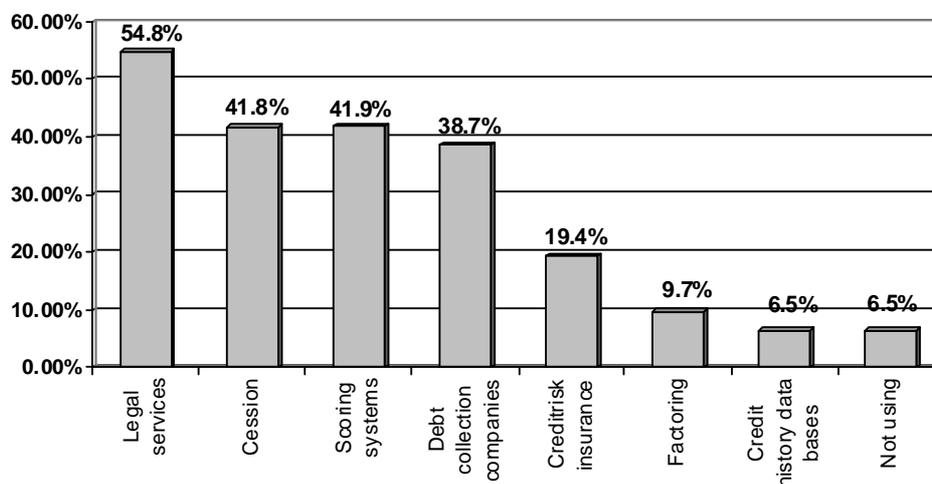
For the transactions concluded to be as effective and safe as possible, all respondents in 2011 much more active than previously before the co-operation with new or existing partners tested their ability to pay and previous credit history. Most companies base their cooperation on the previous cooperation efficiency and effectiveness. However, the large part in addition to the previous cooperation assessment focuses on the partner financial position, cash management, credit history and solvency assessment, and its changes. Approach to the assessment of co-operation partner solvency and risk of co-operation, each operator has its own – part provides penalties for the defaulters, part of them duly collecting feedback from other industry players, but a part - provide with additional guarantees.

Picture 12. How do companies ensure that customers will fulfill the commitments, 2011



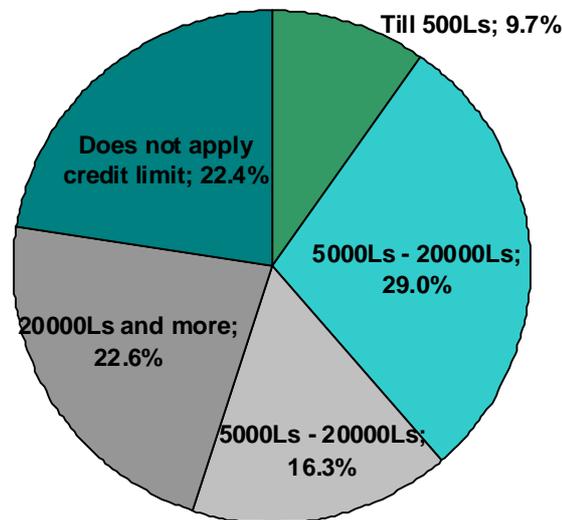
More and more of the companies deal with the problem of late payments by attracting professional outsourcing service providers. More than a half of entrepreneur in 2011 used the legal services for late payment problems - 54.8%. Almost equal proportion of companies using the services of an assignment and scoring systems, respectively, 41.8% and 41.9%. As a significant part (38.7%) of entrepreneur are using debt recovery services for companies to deal with the debt problems.

Picture 13. The use of professional services in order to solve delayed payment problems in enterprises in 2011



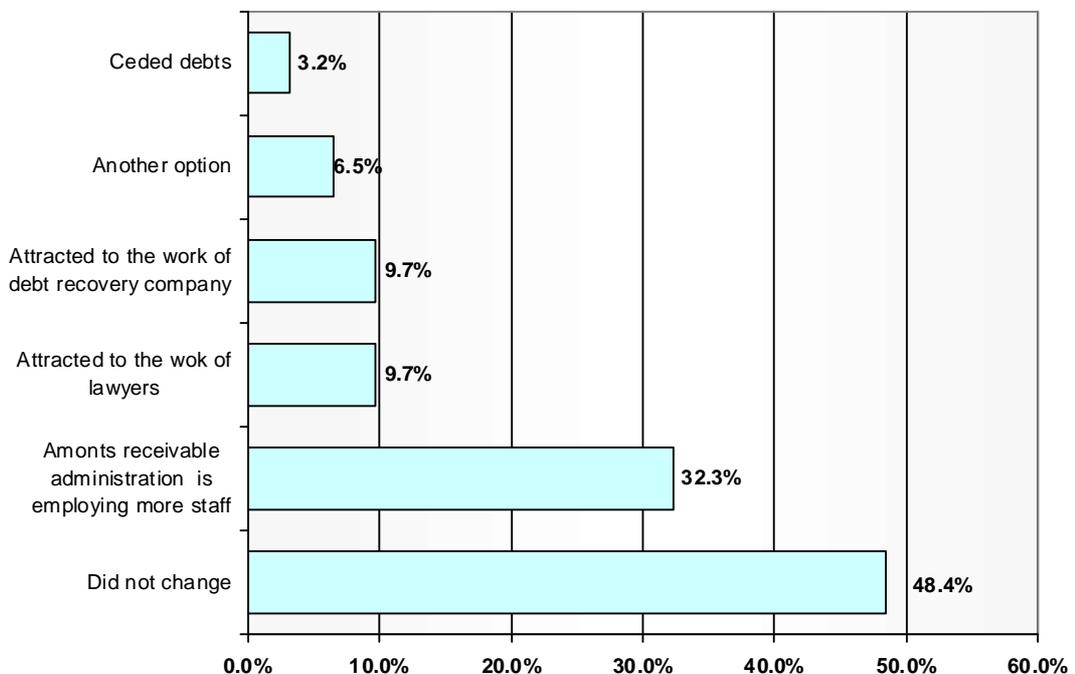
Last year increased the number of entrepreneur which provides its customers credit limits, thus avoiding transactions in which the potential co-operation partner would reach his financial capacity. If in 2010 credit limits were 68.4% of the companies, then in 2011 it was 77.6%. The majority - 29.0% of customers set a credit limit ranges from 500Ls to 5000Ls. Proportionately similar part (22.6%) fixes the credit limit 20000Ls and more, while 22.4% co-operation partners fix the credit limits for the co-operation partners.

Picture 14. Set credit amounts for 2011



The research shows that in 2011 the majority of entrepreneur (48.4%) worked in accordance with a prescribed debt management procedures, which ensured the most effective business results in dealing with non-payers. However, a significant proportion (32.3%) of entrepreneur for more effective debt business administration in 2011 has involved more employees.

Picture 15. How do the companies changed their debt management procedures during 2011

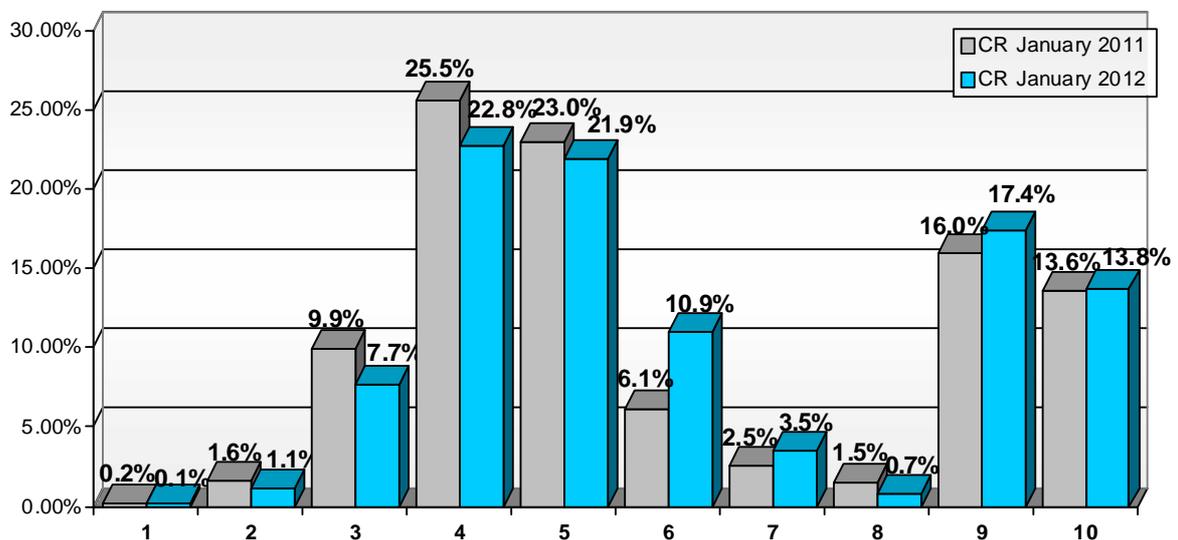


Method for a rapid assessment of credit risks

Entrepreneurs increasingly are looking for operative and effective methods for a new or existing partner's assessment which would allow substantial savings in the company's time and resources. One of those is the Scoring system, which allows companies the credit decisions for small transactions to take quickly without co-operation partner's financial data research, analysis, and additional funding attraction.

Creditreform specialists, in cooperation with the German company Creditreform Risk Management, have developed a mathematical model CrefoScore, which is automatic on-line credit risk assessment system on www.crediweb.lv. Its main component is Score - a specially calculated index, which indicates the probability of the company over the next 12 months to live up to their financial obligations. For the easier and quicker perception - created 10 CrefoScore risk classes from one to ten, where the first and eighth-grade shows the company solvency. But in the ninth class of risk the company comes in, if in the past year has registered a significant amount of late payment, but in the tenth - if the company is insolvent, or takes place in the reorganization or liquidation proceedings.

Picture 16. Percentage breakdown of Latvian Commercial Register enterprises in CrefoScore risk classes in January 2011 and in January 2012



During 2011, among the Commercial register companies in general negative changes occurred - reduced the number of companies in the first CrefoScore risk classes with excellent, very good, and good solvency. A large part of these companies have fallen for the sixth and seventh risk class, where the ability to pay is below average or a little tense.

Compared to the previous years, also at the beginning of 2012 most of the Commercial register companies were in the fourth and fifth CrefoScore risk class (ability to pay above-average and average). During 2011 the number of companies risk classes from first to fifth has fallen by 6.6%. Changes in 2011 occurred in the ninth CrefoScore risk class (collaboration with these companies is not recommended because of the credit risk) - at the beginning of 2012, a 1.4% increase in the number of companies with a poor ability to pay, by the reason of outstanding liabilities to the co-operation partners and the registered cases of negative credit history.

Through publications, reference to Creditreform Latvijā SIA compulsory.