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July 2016

PANORAMA

INSOLVENCIES IN CENTRAL AND EASTERN EUROPE

THE COFACE ECONOMIC PUBLICATIONS

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Companies in the Central and Eastern Europe region reported solid economic growth rates as well as more structured growth last year. Thanks to the healthy situation of the labour markets, unemployment rates have been decreasing, to reach historically-low levels in many cases. This, combined with rising wages and low inflation, have made private consumption a key driver for growth. Investments, another important component of domestic demand, grew – thanks to businesses' improved expectations and, in particular, the accelerated use of EU funds (during the final year of previous EU budget availability) to co-finance projects. Last but not least, CEE companies have seen improving demand from their main export destination, the Eurozone. Although recovery in the Eurozone is weak, higher exports to the region are compensating for the Russian slowdown and the official ban on exports of selected merchandise to Russia.

Positive macroeconomic conditions have, unsurprisingly, led to an improved situation for CEE businesses. The number of insolvencies decreased over the course of last year in 9 out of 13 countries and the GDP-weighted regional insolvency average was -14%. Obviously, company insolvencies varied at different rates among CEE economies. Double-digit deterioration was recorded in Ukraine and Lithuania, whereas Romania and Hungary enjoyed significant improvements. Some of these huge fluctuations hide country specifics that affected their performances last year and these are explained in this report. The number of insolvencies has not yet returned to the pre-crisis levels of 2008 for most countries. In the Czech Republic, insolvencies were almost 4 times higher than in 2008, in Poland 1.8 times higher and in Slovenia 2.2 times higher. At the same time, company insolvencies in Slovakia and Romania are still below pre-crisis levels. Overall, however, 2015 insolvency statistics paint a more positive picture of CEE companies. This trend should persist, as corporates continue to benefit from the favourable economic environment, especially when compared to the turmoil being experienced by many other emerging economies.

The regional improvement is confirmed by Coface's country risk assessments, which included several upgrades this year. In January, Hungary's assessment was raised to A4, while in June there were upgrades of Latvia to A4, Lithuania to A3, Romania to A4 and Slovenia to A3. Most CEE countries have thus moved to acceptable risk levels.

Businesses will continue to take advantage of supportive conditions this year, although insolvencies will decline at a slower pace than last year. Coface forecasts that company insolvencies will drop by 5.3% for the full year 2016.

The CEE Insolvencies Panorama examines the regional economic situation that companies faced during the course of last year. It then highlights particular economies within the CEE, with a more detailed focus on insolvencies, including the best and worst performing sectors, as well as the largest insolvencies. The final section analyses the business environment that CEE companies faced in 2015, as well as the outlook for activity in 2016.

DOSSIER

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"The CEE region enjoyed solid growth last year but corporates benefited even more, with average regional insolvencies declining by 14%. Although this year will be favourable, these exceptional results on both the macro and micro sides are unlikely to be repeated."

1 INSOLVENCIES IN CENTRAL AND EASTERN EUROPE IN 2015

Countries in the CEE region[1] enjoyed good economic conditions last year. The average regional GDP growth rate accelerated from 2.6% in 2014, to 3.3% in 2015. Moreover, last year's GDP result was the highest since the post-crisis level of 2009. This robust economic activity was supported by higher absorption of EU funding - due to being the final year of access to the previous EU budget. As most CEE countries are EU members, they are able to benefit from Cohesion Funds, which are often used to enhance activities in the construction sector and various related industries. Although 2015 saw an exceptional boost in EU co-financed investment activities, this was not the only factor in the region's solid economic activity. For the majority of CEE countries, strengthened domestic demand, especially private consumption, was the main growth driver. Declining unemployment rates, rising wages, low inflation (or even deflation in some economies), depressed commodity prices and rock-bottom interest rates all made positive contributions and led to household consumption being the most important driver for growth. The propensity of households to spend has increased - as confirmed by rising consumer confidence indicators. Nonetheless, consumers remained relatively cautious in their spending habits as, in many cases, they had been affected by the challenging times in the labour market during 2012 and 2013. Despite this, households did become more inclined to purchase durable goods in 2015, rather than being focused on daily necessities.

CEE economies are highly exposed to exports. An example is the automotive sector, which sends the bulk of its production to foreign markets. External demand is also important for other sectors, especially in the smaller CEE economies, where they need to take advantage of their export potential, as their own domestic markets are often too small. The region's premier foreign trade destination is the Eurozone, particularly Germany, where CEE countries send not just final products but components for manufactured goods which are subsequently sold locally or exported. The external environment supported CEE exporters last year. Eurozone growth increased from 0.9% in 2014, to 1.6% in 2015. Although Germany recorded slightly slower growth than in 2014, at 1.5% for 2015, this was still a good result when compared to current 'standards' for advanced economies. Even though the Eurozone's improvement is weak, it can still be defined as a recovery. Nevertheless, the recent "Brexit", combined with other political uncertainties, could affect business confidence.

An educated workforce, attractive labour costs and the region's geographical proximity to the deep markets of the Eurozone and CIS countries, have all been crucial factors enabling the CEE to produce goods demanded by external markets and to be included in global supply chains. However, some CIS markets, previously seen as opportunities, have now entered into an economic slowdown. Russia, the most crucial market, imposed an embargo on meat, fish, fruit, vegetables and milk products from the EU, US, Australia, Canada and Norway in August 2014. This is still weighing negatively on a number of companies in the CEE region. Although exporters have been effective in their attempts to redirect exports to alternative markets, a faster rebound in Russia's economy, accompanied by the lifting of its embargo, would bring a boost to foreign trade. So far, however, this appears unlikely, as the EU is more likely to prolong sanctions.

[1] The following countries are included as the CEE region: Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Serbia, Slovakia, Slovenia, Ukraine.

Table 1: Insolvencies in Central Europe 2014/2015

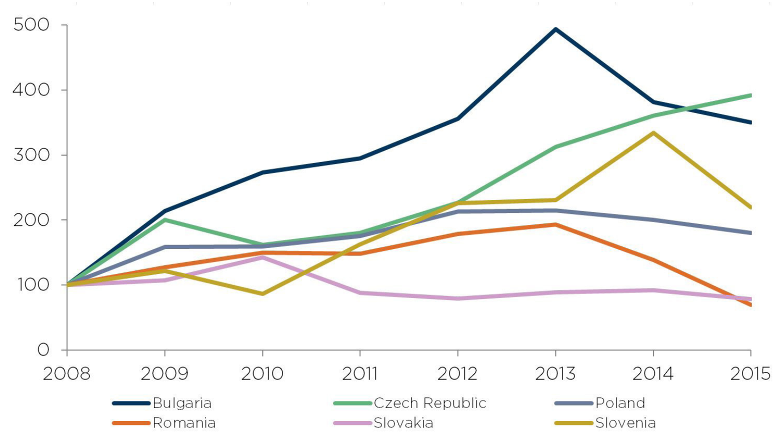
	Total insolvencies		Dynamics	Bancruptcies		Total number of active companies*	Insolvency rate**
	2015	2014	2015/2014	2015	2014	2015	2015
BULGARIA	592	644	-8.1%	n.a.	n.a.	400,000	0.15%
CROATIA	1,977	2,764	-28.5%	388	719	263,897	0.75%
CZECH REPUBLIC	13,877	12,772	8.7%	11,314	9,050	1,439,747	0.96%
ESTONIA	131	145	-9.7%	n.a.	n.a.	192,000	0.07%
HUNGARY	9,748	17,461	-44.2%	9,686	17,377	560,853	1.74%
LATVIA	830	963	-13.8%	830	963	220,000	0.37%
LITHUANIA	1,960	1,686	16.3%	n.a.	n.a.	99,200	1.98%
POLAND	741	823	-10.0%	650	701	1,842,589	0.04%
ROMANIA	10,170	20,120	-49.5%	n.a.	n.a.	450,286	2.26%
SERBIA	5,109	4,773	7.0%	2,062	1,831	126,262	4.05%
SLOVAKIA	446	522	-14.6%	354	407	539,089	0.08%
SLOVENIA	950	1,446	-34.3%	816	1,302	203,542	0.47%
UKRAINE	1,306	1,081	20.8%	1,290	1,063	1,117,000	0.12%
GDP WEIGHTED AVERAGE			-14.0%				0.81%

* National statistics or estimations from expert organisations, average
** Share of insolvencies in a total number of active companies

Bankruptcy proceedings: This term refers to insolvency proceedings that are directed to achieve the orderly wind-up of an insolvent enterprise with the objective of liquidating or reorganising the business.

Thanks to the environment of rising domestic demand and improving prospects on core foreign destinations, businesses have felt comfortable with expanding and addressing opportunities. The GDP-weighted average of insolvencies in the CEE region dropped by 14% in 2015, resulting in less than 1% of bankruptcies in active firms. Only 4 countries among the 13 analysed experienced an increase in insolvencies. These were the Czech Republic, Lithuania, Serbia and Ukraine. It should, however, be noted that within this group of weak performers Lithuania particularly suffered from the embargo implemented by Russia, its most important trading partner. The biggest impact came from the process of "weeding" the market from companies that still officially existed, despite being insolvent for some time. This process, carried out by the State Tax Inspectorate and Social Fund, resulted in a significant rise in the number of Lithuanian bankruptcies last year, making it impossible to compare like for like dynamics with previous years.

Chart 1: Change in insolvencies in the CEE region since 2008 (2008=100)



Source: Coface

The dynamics of company insolvencies varied between countries. The strongest rise, of nearly 21%, was recorded by Ukraine. The country's economy is still deteriorating. Its industries are faced with contracting private consumption, due to high inflation and weak confidence indicators, within an environment of war-related destruction. In addition to the number of insolvencies last year, many Ukrainian companies went out of business without filing for insolvency. In contrast, the biggest improvement was recorded by Romania, where company insolvencies dropped by almost 50%. The country's high GDP growth rate was supported by fiscal measures which boosted retail sales and positively affected business operations. Nevertheless, the overall decline in insolvencies was aided by a high number of bankruptcies among non-active companies.

Most CEE economies benefited from improvements in the labour market, which led to higher consumer spending, Trade companies, however, were still widely represented in the 2015 insolvency statistics. Many of these companies, challenged by strong competition and low margins, sought ways of keeping costs under control and finding new growth opportunities for expansion. With countries benefiting from the last opportunities to use the former budget of EU funds to support numerous construction projects, insolvencies in the construction sector declined in many countries. However, the construction sector still displayed weak payment behaviour. In many cases, losses suffered during previous challenging years have not yet been compensated for. Moreover, the slow start in funding from the new EU budget has already had a negative effect on construction output during the first months of this year. Better prospects for the sector are likely to be seen as from 2017.

Insolvency figures varied between countries, as they were not only affected by their economic situations but also by insolvency definitions in specific countries, with amendments to insolvency laws, or more widespread use of insolvency procedures.

Favourable business conditions are continuing in 2016. Further improvements in the labour market, along with growing confidence, will reinforce household consumption as the main growth driver for CEE economies. The contribution of investments will not be as high as last year, due to a slow start in new EU co-financed projects. This is weakening the expansion of the construction sector and various other industries associated with it. On the external side, CEE countries will remain active exporters, although the slowdown of global trade could hamper their ambitions. Global turbulence, including the steeper Chinese slowdown, is particularly affecting Germany, the CEE's main partner, which could diminish export dynamics. Confidence indicators could be hampered by rising political risks and uncertainties related to Britain's referendum decision to exit the EU. Nevertheless, overall business conditions will remain supportive, even if less so than last year. Coface consequently forecasts that insolvencies will decline (although at a slower rate than in 2015), with the average number of bankruptcies down by 5.3% for the full year 2016. The biggest slump in insolvencies will be seen in Serbia and Lithuania - the latter of which is likely to include a compensation effect following the strong surge experienced last year. Estonia's high dependence on foreign demand, affected by the weak growth of its main trading destinations, will cause a slight increase in company insolvencies. Ukraine's prolonged recession will lead to a further rise in the number of bankruptcies. The following table provides forecasted dynamics of insolvencies in specific CEE countries:

Country	Company insolvencies dynamics	
	2015	2016 Coface forecast
BULGARIA	-8.1%	-2.3%
CROATIA	-28.5%	-2.7%
CZECH REP.	+8.7%	-5.5%
ESTONIA	-9.7%	+3.4%
HUNGARY	-44.2%	-4.9%
LATVIA	-13.8%	-2.8%
LITHUANIA	+16.3%	-9.6%
POLAND	-10.0%	-8.9%
ROMANIA	-49.5%	-4.1%
SERBIA	+7.0%	-10.5%
SLOVAKIA	-14.6%	-4.3%
SLOVENIA	-34,3%	-2.6%
UKRAINE	+20.8%	+7.1%
GDP weighted average	**-14.0%**	**-5.3%**

2 FOCUS ON COUNTRIES

Bulgaria - Private sector focuses on deleveraging

Last year the Bulgarian economy expanded by 3.0%. The pace of growth exceeded expectations, as well as results recorded in previous years (as the highest growth seen between 2009 and 2014 was 1.6%). Economic activity in 2015 was supported by rising exports and, especially in the second half of the year, domestic demand, with growing private consumption and fixed investments. EU funds, with their higher than anticipated absorption, benefited public investments and enhanced GDP growth. The dynamics of household consumption are supported by the falling unemployment rate, which dropped below 10% for the first time since 2009. Although employment will be on an improving track, it should be noted that the aging population and emigration are contributing to these lower unemployment rates.

Within this environment, domestic demand will be the main growth driver this year. Coface's forecast for GDP growth is 2.1%. The highest contribution will come from private consumption. Investments will slow down, as EU funds will be less supportive than last year and the private sector is still focusing on deleveraging. As Bulgarian companies are highly indebted compared to their CEE peers, less room for further leverage has led to weak credit growth dynamics. Corporate debt is forecast to reach 120% of GDP - i.e. above the level of 90% of GDP considered "an alert threshold" in debt literature[2]. On the other hand, corporate debt in Bulgaria has not seen a rapid rise since 2008, as was the case for the majority of large emerging countries. On the exports side, corporates will be able to benefit from the European Central Bank's moves to make the euro (to which the Bulgarian lev is pegged) weaker. This enhances Bulgaria's competitiveness, as the list of its main export destinations also includes non-euro countries.

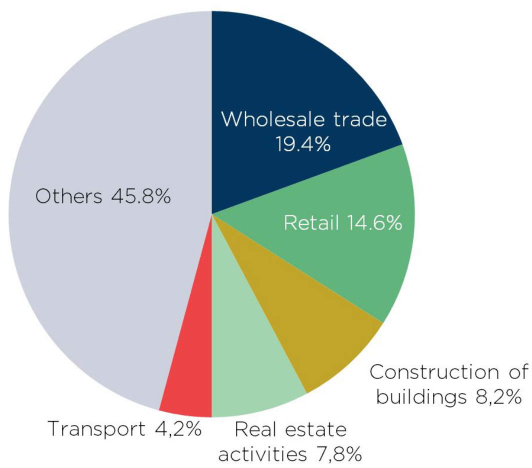
Chart 2:
Dynamics of loans to private sector (y/y changes)

Source: Bulgarian National Bank

However, there are doubts on whether the ECB's actions will bring the anticipated results. In terms of both export potential and attracting FDIs, Bulgaria has the lowest levels of labour costs but an unsupportive business environment. Limited foreign capital inflows will drag on investment growth and further economic expansion.

Although the closure of the Corporate Commercial Bank took place in 2014, it was only declared insolvent by the courts in 2015. This bankruptcy impacted public finances, as the guarantee fund was unable to meet EU obligations of refunding deposits of up to EUR 100,000 and commitments were undertaken by the public sector. In addition, further fiscal loosening will result from widening expenditure, with the revision of the budget and increasing borrowing needs. Nevertheless, public debt will stay at a manageable level, increasing from 27.0% in 2015, to 28.0% in 2016, according to Coface's forecast.

Chart 3:
Company insolvencies, by sectors, in 2015



Source: Coface

Corporate Commercial Bank's insolvency was the biggest bankruptcy last year. It related to liabilities worth almost EUR 1 billion and concerned over 600 employees. However the overall impact of this insolvency for households, businesses and the entire economy was even bigger, as Corporate Commercial Bank was one of the largest banks in Bulgaria. Other major bankruptcies included sizeable businesses, such as the construction company Integrirani Patni Systemi and Burgas Shipyards. As a result, Bulgaria's insolvency statistics last year were stronger for bankruptcies of large companies whose payment problems affected a great number of their counterparts. However, with improving macroeconomic conditions, Bulgarian corporates took advantage of rising demand and the general insolvency statistics

[2] Cecchetti, S.G., M.S. Mohanty and F. Zampolli (2011) : «The Real Effects of Debt,» Bank for International Settlements, Working paper n°352

delivered a positive picture. In the course of 2015, insolvencies dropped by 8% - translating to less than 2 bankruptcies per 1,000 active companies. Despite stronger demand, trade companies were among those the most affected by bankruptcies, accounting for over a quarter of all insolvencies. The construction sector was also widely represented in the statistics, as was the case already in 2014. Bankruptcies of both construction and real estate companies took a 15% share.

Top 5 sectors
Information service activities
Pharmaceuticlas
Manufacture of machinery and equipment
Social work activities
Water collection, treatment and supply

Flop 5 sectors
Wholesale trade
Retail trade
Construction of buildings
Real estate activities
Land transport and transport via pipelines

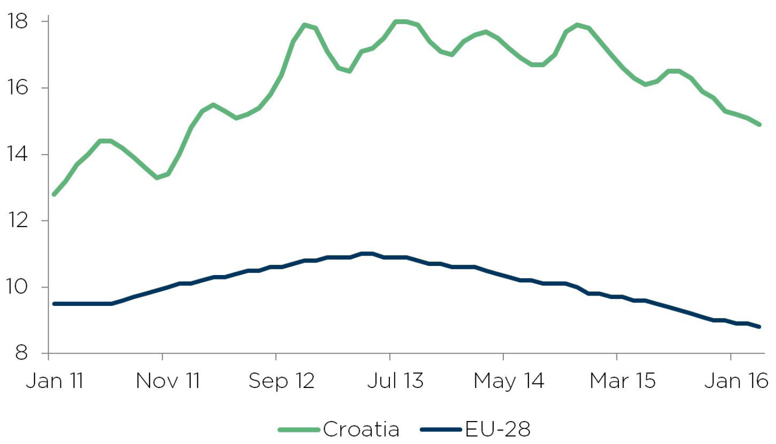
The 5 biggest insolvencies in 2015

	Company Name	Sector	Number of employees	Town
1.	CORPORATE COMMERCIAL BANK	Bank	629	Sofia
2.	INTEGRIRANI PATNI SISTEMI AD	Construction of roads and motorways	96	Skriniano village
3.	BURGAS SHIPYARDS JSC	Ship building	10	Sofia
4.	TC IME VEST	Financial service activities	n.a.	Sofia
5.	INTERTRUST HOLDING	Business and other management activities	6	Sofia

Croatia - rebounding from a long recession

Economic activity in Croatia has finally returned to positive growth. After six consecutive years of recession, Croatia recorded growth of 1.6% in 2015. This was supported by both external and internal demand. In terms of the latter, household consumption finally increased and delivered a positive contribution to GDP growth - which had not been the case during the previous three years. The labour market improved, with falling unemployment levels and rising wages. Reductions in personal income tax further encouraged consumer spending. Nevertheless, despite contracting, the unemployment rate remains high. It stood at 16.3% in 2015 and, according to the latest available data (chart 4), as of March 2016, at 14.9%. This level is still the highest in the CEE region, as well as being one of the highest in the entire European Union - just after Greece and Spain. Gross fixed capital formation was supported by higher absorption of EU funds, with investments growing mainly in the public sector. However, improvements in this regard have also started to appear in the private sector.

Chart 4:
Unemployment rate (%)

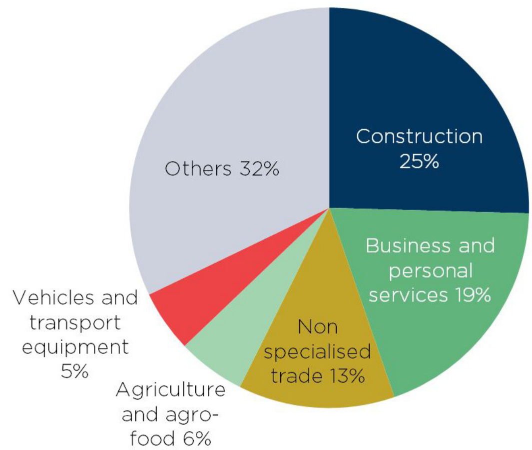


Source: Eurostat

After years of excessive government deficit exceeding 5% of GDP, it declined to 3.2% of GDP in 2015. The government is focusing on further reducing the budget deficit, as well as stabilising public indebtedness. The latter it is expected to show a slight increase - but significantly less so than in recent years.

Increasing business competitiveness is one of the government's priorities. To stimulate the growth of small and medium enterprises, it is dedicating a programme of EUR 500 million. To address the companies sector, the authorities intend to tackle the obstacles that entrepreneurs and investors face in the country. The government has announced that it will lower parafiscal levies, introduce changes to the judiciary system (in order to harmonise court practices and shorten court proceedings) and speed up the construction permit process[3]. Coface forecasts that GDP growth will reach 1.9% this year, with further improvements in the labour market positively contributing to economic activity. Nevertheless, the continued deleveraging process is hampering a decisive recovery in household spending. Contrary to last year, investment will be mainly fueled by the public sector, with only minor growth from the corporate side. The persistently high debt burden is a constraint to both the public and private sectors. Although structural improvements are on the agenda, the progress of governmental reforms is uncertain.

Chart 5:
Company insolvencies in Croatia, by sectors, in 2015



Source: Coface

It is not only the macro side that improved last year. In 2015, the number of company insolvencies decreased by 28% y/y. However, the amount of 696 judicial compositions announced last year (out of 1,977 total insolvencies), hides a high number of submitted proposals for the opening of bankruptcy proceedings. Bankruptcy proceedings spiked with the entry into force of the new Bankruptcy Act in September 2015. Under the new legislation, the National Financial Agency is required to file bankruptcy for any company whose accounts have been blocked for more than 120 days, with a 8-day deadline for opening the procedure. This led to a hike in the number of bankruptcies in Croatia last ear. Among other

[3] http://www.total-croatia-news.com/business/2947-good-news-for-entrepreneurs-croatian-government-to-reduce-parafiscal-levies

factors that contributed to insolvencies were short bankruptcy procedures which were opened and closed due to a lack of assets, no employees or the non-release of financial statements to the official bodies for three consecutive years. Another rule has determined that having bank accounts blocked for more than 60 days in a row is a reason for suggesting judicial composition proceedings, which can lead to agreements with debtors and a continuation of business - or the opening of insolvency procedures.

The construction sector is still widely represented in insolvency statistics. Although the number of construction company bankruptcies decreased last year, the sector still accounted for a quarter of all insolvencies – as was the case in 2014. The list of flop sectors, which ranks business activities with the highest insolvency rates, also includes the textiles and clothing sector, as well as utilities and public services. The latter suffered from a 53% increase in insolvencies in 2015.

Top 5 sectors
Financial services
Mineral products, chemicals, petroleum, plastics, pharmaceuticals and glass
Motor vehicles, motorcycles, other vehicles and transport
Business and personal services
Metals

Flop 5 sectors
Utilities and public services
Construction
Textiles, leather and clothing
Electrical equipment, electronics and IT Technology
Wood and furniture

The 5 biggest insolvencies in 2015				
	Company Name	Number of employees	Total liabilities in Euro	Town
1.	ANTE JURKOVIĆ	1	44,755,535	Zagreb
2.	TLM Aluminium	487	41,615,840	Šibenik
3.	TRGOVAČKI CENTAR SOLIDUM	9	32,039,530	Zagreb
4.	ADRIA ČELIK	237	31,047,344	Kaštel Sućurac
5.	MERKUR-HRVATSKA	132	28,770,179	Zagreb

Czech Republic - GDP growth leader in 2015

Last year the Czech economy recorded an impressive growth rate of 4.2%, beating all other CEE countries in this regard. This positive result can be attributed to an exceptional boost from public investment. 2015 was the final year for using the previous EU budget and the Czech Republic was successful in tapping funds and engaging them into EU co-financed investment activities. Inventories also expanded, with the purchase of military aircraft further enhancing GDP growth. It will not be possible for the Czech economy to maintain such robust growth this year. Coface forecasts a lower, but still fair, growth of 2.4% for 2016. Similar to last year, economic activity will be driven by private consumption. The Czech Republic is benefiting from a low unemployment rate which, at 5.1% in 2015, is one of the lowest in the entire European Union. Rising wages and low inflation are further supporting private consumption.

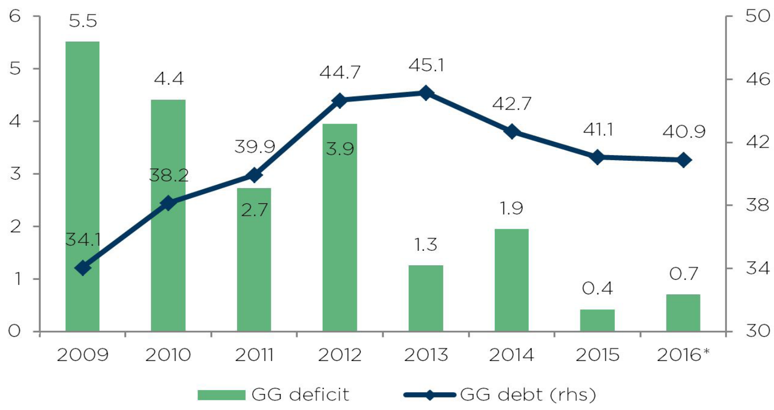
In contrast to this growing private consumption, gross fixed capital formation is expected to decrease slightly, following the strong rally it experienced last year. On the other hand, private sector investments are likely to record an increase, thanks to promising demand prospects which will increase companies' capacities. As a manufacturing hub for European brands, especially German ones, the Czech Republic has benefited from becoming a significant element in supply chains. Although it still relies, to some extent, on the assembly of foreign imported components and services, the Czech economy has undoubtedly benefited from a strong foreign presence. This also brings risks, as these foreign firms could consider other country locations, with more attractive costs, for their new investments. Growth in employee compensation in the Czech Republic has been higher than the increase in productivity and several other countries in the CEE region could provide lower labour costs.

After years of fiscal consolidation, in 2014 the situation became more relaxed and last year government investments and consumption spending sped up to support economic activity. The Czech Republic will continue to enjoy favourable public finance indicators, with a moderate deficit and a manageable level of public debt.

From the public finance perspective, the accelerated use of resources from EU funds was a significant contributor to reaching a low level of deficit. The record-breaking low yields of government bonds were also supportive. In August 2015, medium-term state bonds were sold on the primary market, for the first time in history, with negative yields. Since then, a further ten auctions of medium-term state bonds have been held on the primary market with negative yields. Government treasury bills have continually achieved negative interest yields on the primary market and the same phenomenon has also been seen on the secondary market[4].

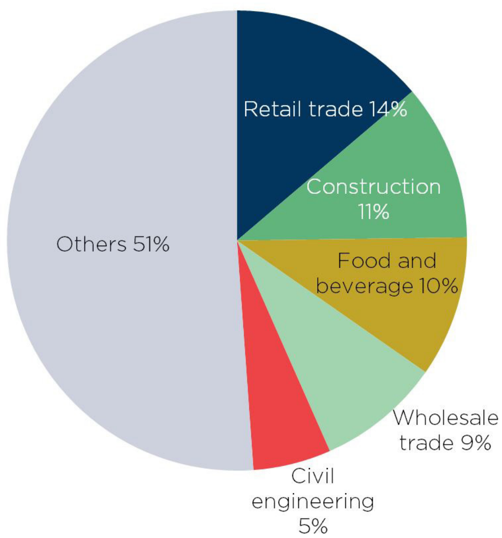
Despite the impressive economic expansion that the Czech Republic recorded last year, the number of company insolvencies increased by 8.7% y/y, reaching almost 13,900 entities during the period. It should be noted that most insolvencies concerned inactive self-employed persons, as was the case in previous years. While good macroeconomic conditions, with a significant rise in private consumption, were favourable for companies, the high competition experienced by many sectors forced businesses to operate at low margins. Although the positive situation of the labour market is supporting households and their spending habits, companies have found it more difficult to hire employees, particularly specialised ones. Moreover, growth in wages has resulted in rising operational costs for corporates.

Chart 6:
General government deficit and debt (%)



*Coface forecast
Source: Convergence Programme (May 2016 update), Coface

Chart 7:
Company insolvencies in the Czech Republic, by sectors, in 2015



Source: Coface

[4] Convergence Programme of the Czech Republic, May 2016, http://www.mfcr.cz/assets/en/media/Convergence-Programme-CR-May-2016_v01.pdf.

As in the previous year, insolvencies in the Czech Republic in 2015 were dominated by retail trade companies, in line with their quantity in the whole economy. Nevertheless, their share dropped from 15.8% in 2014, to 13.8% in 2015. In contrast, the construction sector's share increased during the period, indicating that liquidity problems and overdue payments are still hampering the sector's business activities. Despite this, insolvency rates in the retail and construction sectors have not risen sufficiently to push them into the list of flop sectors. The challenging situation on the commodities markets, with low prices, contributed to a strong presence of mining and quarrying companies in insolvency statistics. The manufacturing of coke and refined petroleum products became one of the flop sectors.

Top 5 sectors
Manufacture of pharmaceutical products
Insurance
Mining support services activities
Air transport
Manufacture of tobacco products

Flop 5 sectors
Remediation activities and other waste management services
Civil engineering
Manufacture of coke and refined petroleum products
Office administrative and other business support activities
Financial service activities (except insurance)

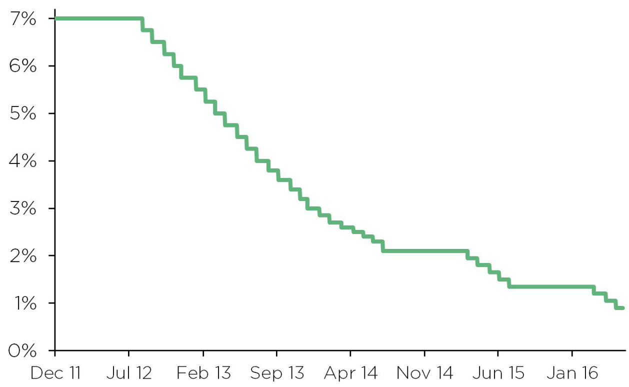
The 5 biggest insolvencies in 2015				
	Company Name	Sector	Number of employees	Town
1.	KF Oil s.r.o.	Wholesale of fuels and related products	19	Praha
2.	RD CZ Energy s.r.o.	Trade of electricity	2	Praha
3.	VOKD, a.s.	Civil engineering	480	Ostrava
4.	LIJA a.s.	Wholesale of metals and metal ores	24	Frýdek-Místek
5.	EFEKTIM a.s.	Wholesale of household goods	10	Praha

Hungary - SME support measures in force

The Hungarian economy has been recording solid growth rates since its recession in 2012. EU funding has been an important contributor to growth, but by no means the only factor. The country's high pace of growth has been supported by government policies including monetary easing, more unconventional measures aimed at boosting SME lending and increasing public sector employment. The perspectives for the Hungarian economy and most of the country's main trading partners have been improving. Households have seen a growth in demand for labour from both the public and private sectors. They have also benefited from the conversion of their foreign currency mortgage loans into domestic currency. Although the growth of 2.0% forecast for this year by Coface will be slower than the 2.9% achieved in 2015, this will mainly be due to the decrease in absorption of EU funds - which should speed up as from next year. Nevertheless, ongoing improvements in the labour market and fiscal measures (such as cuts in personal taxes and VAT rates), are supporting private consumption as the main driving force behind the economy. Unemployment reached an all-time low of 6.8% in 2015 and it further decreased to 5.6% in March this year. Employment is likely to grow further, thanks to the hiring of employees by the private sector and governmental programmes for public works.

In recent years, businesses have been suffering from various taxes and quasi-taxes. These have included additional financial burdens for the country's banks, energy and telecommunications companies, as well as its biggest retailers. Despite improvements to the budget situation and stronger growth, further taxes have been implemented - such as a health tax, a tax on tobacco companies, food inspection fees, taxes on financial transactions, taxes on chemical products and an internet tax (the latter of which was revoked due to social unrest). The possibility of further changes to the country's regulatory and legislative frameworks has caused uncertainty, making companies reluctant to invest and expand their businesses. The Hungarian central bank has implemented stimulus measures, including the substantial lowering of interest rates and the Funding for Growth Scheme, which provides low interest rate loans to SMEs. Nevertheless, the entire corporate sector has continued deleveraging. Additional measures, to support further borrowing by SMEs, may contribute to the country's economic activity. Among larger entities, the sentiment is that there could be improvements if no further tax burdens are implemented. Banks will feel some relief, as the banking tax was lowered at the beginning of this year and the government has announced that it will refrain from policy measures with negative impacts on banking sector profitability. In addition to unconventional measures aimed at boosting investments (such as the new Market Based Lending Programme), the central bank is continuing to use traditional measures. So far this year, there have been three rate cuts, bringing the base rate to 0.90%. There have been a large number of rate decreases over recent years. The easing cycles started in August 2012, when the base rate was at 7%. Interest rate cuts also led to the Hungarian National Bank being the first emerging market central bank to enter a negative interest rate environment. The overnight deposit rate has been -0.05% since March this year.

Chart 8:
The Central Bank base rate



Source: The Central Bank of Hungary

All of these measures will still not be sufficient to sustain economic growth at the levels recorded last year, particularly with the slow start to using EU funds from the new EU budget. Companies are becoming more confident about the economic outlook and the Central Bank is continuing to develop measures to discourage corporates from deleveraging and to help boost the economy. While the contribution of investments will be weaker this year, positive growth dynamics should be recorded as from 2017. The most important segment in Hungary's economic activity remains the automotive sector, which created nearly 4.5% of the country's added value and over 10% of total output. The industry's relatively positive outlook is benefiting from Hungary's preferential business climate for the sector, demand from Western Europe (the destination for most of its production) and its continued cost competitiveness compared to other Eurozone plants, which often suffer from overcapacities.

Satisfactory economic growth, more favourable prospects for Hungarian companies and improved payment experience all contributed to the upgrade of the country's assessment to A4 in January this year. Improvements on the microeconomic side are also confirmed by insolvency statistics. However the impressive 44% drop in bankruptcies last year was mainly due to administrative terminations of inactive companies.

Hungarian law determines that companies closing their business year on December 31 must publish their annual financial reports on or before the following May 31. If a company delays performing this obligation, the tax authorities will impose a default penalty and request that it publishes its annual financial report within 30 days. If the company fails to comply with this request, the tax authorities will impose a second default penalty and request it to publish the annual financial report within 60 days. If the company fails to comply with this second request, the tax authorities will immediately withdraw the company's tax number and inform the appropriate registration court. The registration court will declare the company terminated 20 days after receipt of notice from the tax authorities and then initiate the forced deletion procedure. These regulations, designed with the aim of deleting companies which no longer perform business activities, particularly boosted the insolvency statistics for 2014. These dormant companies were thus less present in last year's bankruptcies, which led to a significant decrease in insolvency numbers in 2015. Nevertheless, even if 2015 insolvencies are compared with 2013 levels (which seems more reasonable given the 'administrative terminations' of 2014), the improvement is still marked. Strengthened demand, from both domestic and external markets, has already reaped positive results in terms of insolvencies. The high share of construction companies in total insolvencies decreased last year compared to 2014, although the sector again took a humble top position in terms of bankruptcies (followed by wholesale and retail businesses).

Top 5 sectors
Healthcare
Education
Electronics and Computer activity
Printing
Banking and financial activities

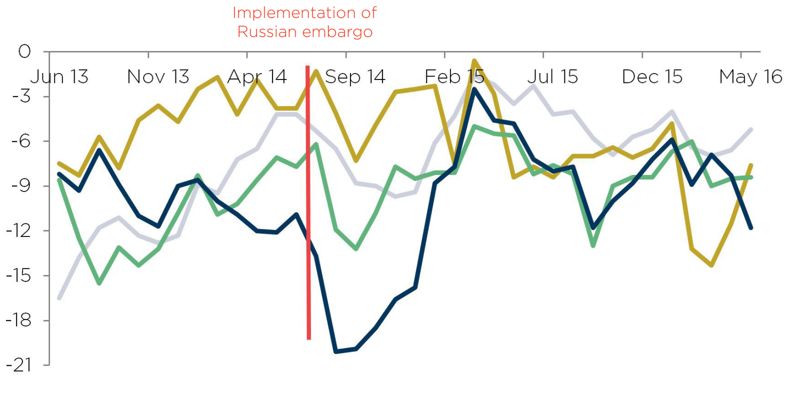
Flop 5 sectors
Paper and packaging
Energy
Food
Wood
Public utilities

Baltic States - Russia´s economic deterioration less harmful than expected

Among CEE economies, the Baltics States are the most exposed to trading with Russia. The ban on food imports, introduced in 2014, and the deterioration of Russia's economy have thus posed significant risks for Baltic economies and local businesses. Nevertheless, they are the part of the European Union and joining the euro was a demonstration of their political integrity with Western Europe. Faced with contracting Russian demand, the Baltics have shifted their export focus to other markets, while significant compensation is coming from improvements in domestic markets. Unemployment rates are continuing to fall, while wages are growing. Businesses are now experiencing greater pressure to increase salaries, due to the rising shortage of employees.

Household confidence in Lithuania is positive, further benefiting from two increases in the minimum wage this year (January and July). There are positive dynamics, with new lending for the private sector and in terms of real estate loans. The Lithuanian Central Bank has introduced changes to reduce the risk of high household indebtedness, with shorter maturities and more restrictive calculations on financial burdens. 2015 was a challenging year for the construction sector. The sector's added value gradually decreased during the course of last year, to reach low, but positive, dynamics in the first quarter of 2016. A rising number of building permits and higher demand for construction work indicate that this year should bring some improvements for the sector. The construction sector's weak performance is confirmed by insolvency statistics which show that construction companies reported the highest insolvency rates, taking first place in the list of Lithuania's flop sectors.

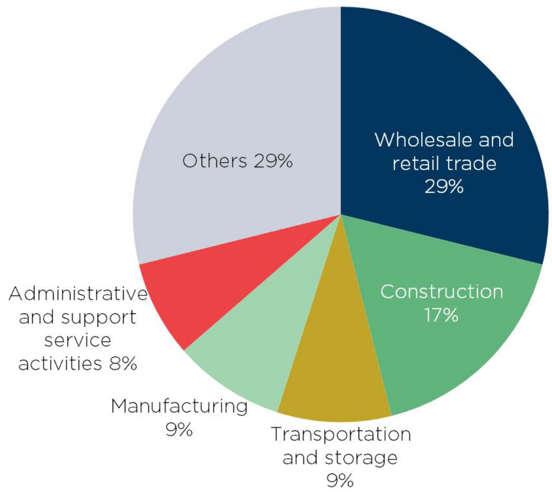
Chart 9:
Consumer confidence indicator



Source: Eurostat

Coface forecasts that Lithuanian growth will reach 2.8% this year, almost the double of the 1.6% last year, following the slump in exports to Russia which affected the country's overall economic activity. Private consumption, supported by strong wages growth, will remain the main driving force. Although the trade sector was a significant contributor to economic activity last year, it has been unable to avoid payment problems. Trade companies took a 29% share of insolvencies, while they accounted for 26% of all bankruptcies in the previous year. They included the bankruptcy of the Fresh Market UAB group, which initially ceased its e-commerce operations, before announcing the insolvency of its entire business. Overall, Lithuania's economy saw insolvencies increase by 16.3% last year. Intense competition and low margins negatively affected the performance of some sectors, while the Russian embargo led to a relatively widespread contraction of business activities. Nevertheless, it would seem that the strongest impact came from the process of "weeding" the market from companies that still officially existed despite having been insolvent for some time. This operation, performed by the State Tax Inspectorate and the Social Fund, significantly boosted the number of bankruptcies in Lithuania last year, making it impossible to compare with the dynamics of previous years.

Chart 10:
Company insolvencies in Lithuania, by sectors, in 2015



Source: Coface

Latvia is expected to record a slower pace of growth. Nevertheless, the forecast rate of 2.3% for 2016 will be a relatively good result, considering the deterioration of economic conditions in Russia and other CIS countries with which Latvia has intense trading relations. Exports to Russia fell by around a quarter in 2015 and a rebound is not expected this year. As is the case for Lithuania, Latvia's economy is also expected to benefit from growing domestic demand. The improvement in the labour market is being supported by rising wages, bolstered by increases in the minimum wage in both 2015 and 2016. The unemployment rate finally returned to single digits last year, for the first time since 2008. This falling trend has continued in recent months. Although there is still room for a more gradual reduction of unemployment and government policies are focusing on resolving structural shortages, further contraction of unemployment is still being hindered by structural constraints. Business conditions vary according to sectors of activity. Latvia's largest steel producer, Liepajas metalurgs, resumed production in 2015 after it was declared insolvent in 2013. Even so, the steel industry is still suffering from low prices, due to Chinese oversupply, which is affecting the global market. The European Commission's anti-dumping regulations are bringing some relief, but the sector's situation remains challenging worldwide. The construction sector is continuing to face difficulties, while the deterioration in Russian demand and protectionist measures introduced by some European countries are negatively affecting the transport sector. Both of these sectors are clearly present in the country's insolvency statistics, with a high share of bankruptcies last year. Rising consumer demand was not sufficient to bring sustainable improvements for trade companies – a sector which saw one of the highest frequencies of insolvencies declared last year. Despite these negative elements, general insolvencies dropped last year, to 830 bankruptcies (13.8% lower than in 2014).

Similarly, Estonian businesses showed an improved insolvency picture for 2015. Bankruptcies decreased by 9.7% compared to 2014. The sector breakdown mirrored that of Latvia. The list of worst performers, in terms of bankruptcies, included wholesale and retail trade, construction, manufacturing and transportation. Insolvencies in the transportation sector were mainly related to companies involved in the transportation of goods by road in the CEE region, although the biggest bankruptcy was that of Estonian Air, a company which employed more than 250 employees and had liabilities of over 90 million euros.

On the macro side, Estonia generated the slowest growth rate among the Baltics. The country recorded growth of 1.1% in 2015, although it is expected that economic activity will gradually increase, to reach 1.8% this year and close to 3% in 2017. It should be noted that Estonia benefits from a more diversified export structure than its Baltic peers but its higher trading exposure to the Nordic countries (than is the case for other CEE economies) meant that it was affected by their slower pace of growth. Although Finland recovered from its recession, growth was still weak, at 0.5% last year. Norway and Denmark recorded slower economic activity last year, compared to 2014. Despite Estonia's diversification in terms of trading markets, Russia remains a significant destination for its exports. Moreover, Estonia suffered from low oil prices, which made its shale oil production inefficient. While exports to EU markets did deliver positive dynamics, household consumption was the strongest growth driver. Consumer spending has been supported by positive developments in the labour market, with falling unemployment rates and growth in both minimum and real wages. Nevertheless, the unemployment situation will probably not improve as much as it has done recently. Already in March this year, unemployment, at 6.8%, was higher than in the same period last year – in contrast to most countries in the region which saw further falls in unemployment during the period. The performance of the labour market will be affected by the decline in the working-age population and the Working Ability Reform, which will entice pensioners to return to the labour market. It is likely that the unemployment rate will increase over the next few years, although it is expected to stay safely below the two-digit level.

Lithuania: Top 5 sectors
Public administration and defence
Education
Human health and social work activities
Other service activities
Mining and quarrying

Lithuania: Flop 5 sectors
Construction
Administrative and support service activities
Accommodation and food service activities
Transportation and storage
Water supply, waste management and remediation activities

The 5 biggest insolvencies in 2015 in Lithuania				
	Company Name	Sector	Number of employees	Town
1.	FRESH MARKET UAB	Retail sale in non-specialised stores	693	Vilnius
2.	SKIRNUVA UAB	Construction of buildings	435	Alytus
3.	INTERNETINE PREKYBA FRESH MARKET UAB	Retail sale via Internet	412	Vilnius
4.	LA - NIKA BALTICS UAB	Manufacture of underwear	407	Vilnius
5.	LIETUVOS JURU LAIVININ-KYSTE UAB	Sea and coastal freight water transport	378	Klaipeda

Latvia: Top 5 sectors
Public administration and defence
Mining and quarrying
Financial and insurance activities
Electricity, gas, steam and air conditioning supply
Human health and social work activities

Latvia: Flop 5 sectors
Wholesale and retail trade
Construction
Manufacturing
Transportation and storage
Professional, scientific and technical activities

The 5 biggest insolvencies in 2015 in Latvia				
	Company Name	Sector	Number of employees	Town
1.	PĀRTIKAS KOMPĀNIJA SIA	Wholesale and retail trade	23	Riga
2.	TMMetal Baltic SIA	Manufacturing	56	Ogre
3.	METRADE SIA	Wholesale and retail trade	105	Riga
4.	Cēsu miesnieks SIA	Manufacturing	62	Cesis
5.	Baltijas Taksometre SIA	Transportation	422	Riga

Estonia Top 5 sectors 👍
Water supply, waste management and remediation activities
Information and communication
Education
Other service activities
Agriculture, forestry and fishing

Estonia Flop 5 sectors 👎
Wholesale and retail trade
Construction
Manufacturing
Transportation and storage
Real estate activities

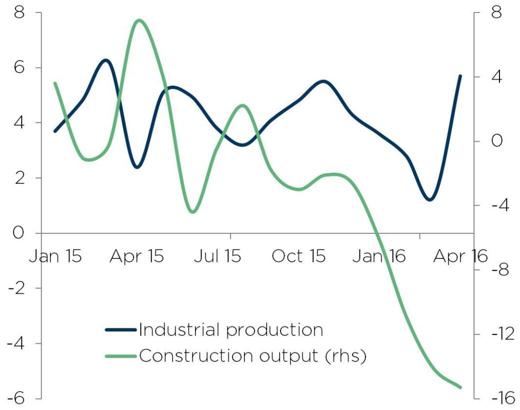
The 5 biggest insolvencies in 2015 in Estonia

	Company Name	Sector	Number of employees	Town
1.	ESTONIAN AIR AS	Transportation	256	Tallin
2.	LÕUNA PARK OÜ	Real estate	n.a.	Tallin
3.	PIDULA MÕIS OÜ	Real estate	n.a.	Kihelkonna
4.	REY SEAKASVATUS OÜ	Agriculture	30	Rapla
5.	B.W.T. KING AS	Wholesale and retail trade	320	Tallin

Poland - Houshold consumption is strenghtening further

The Polish economy has been delivering solid growth rates, of over 3%, since 2014. This path will be continued and Coface forecasts that GDP growth will reach 3.4% in 2016 (slightly below the 3.6% recorded last year). Polish growth continued to be powered by domestic demand, with both strong private consumption and increasing investments in fixed assets. The two previous years delivered impressive growth in terms of fixed asset investments, even recording two-digit dynamics in some quarters. Poland has been highly effective in its allocation and use of EU funds, which also contributed to the growth levels recorded last year. The support of EU funds also made positive impacts on the construction sector, thanks to infrastructural projects. Nevertheless, the challenging times that the sector suffered from previously, are still constraining improvements in its payment behaviour. On the housing side, companies have been benefiting from rising demand, supported by the lowest levels of interest rates in the country's history. These modest rates not only made mortgage loans more attractive but also led to increased interest in property investments as an alternative to the low interest rates on bank deposits. 2015 saw a decrease in construction company insolvencies, although they still constituted over one-fifth of all insolvencies. The effect of the fading out of previous EU funds and the slow start to current EU financial perspective has already resulted in negative growth dynamics for Poland's construction output.

Chart 11:
Dynamics of industrial production and construction output (%, y/y changes)

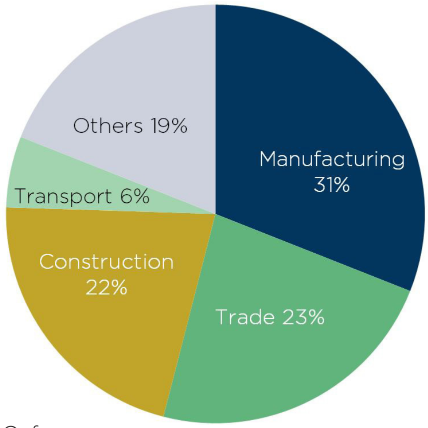


Source: Central Statistical Office

Households have been benefiting from the positive situation on the labour market. The unemployment rate dropped from 10.3% in 2013, down to 7.5% in 2015 and then further again to reach 6.3% in April 2016. In the main Polish cities and locations with a high concentration of industries, companies are struggling to fill job vacancies, even if they offer higher compensation. Nominal wage growth, at 3.5% last year, was enhanced in real terms by deflation. Deflation, present in Poland since mid-2014, has mainly been caused by low commodity prices. Positive inflation readings are forecast to be seen in the final months of this year. Favourable labour market conditions are expected to continue. Household consumption will be boosted by the introduction of a new child allowance, which should encourage retail sales, especially in the third and fourth quarters of this year.

Although Polish exports' share of GDP in 2015 was 49.4%, this is relatively low compared to the country's CEE peers. The economy is also subject to the situation on global markets. This is particularly seen with Poland's supply of components used for final production by German industries. Concerns over the slowdown in the biggest emerging markets, such as China, are important considerations for Poland due to its trade links. In addition to this and other external factors, Poland has been suffering from a deterioration in sentiment, as witnessed by currency depreciation and higher spreads on government bonds. Investors became more cautious when there was a change on the Polish political scene, following the elections. Some of the measures implemented by the new government will come at high costs for public finances (such as the child benefit programme mentioned above), while plans to increase tax collection will not bring the revenues anticipated. Already, in January this year, Poland experienced a downgrade of its rating for the first time, when the Standard & Poor's rating agency revised it down from A- to BBB+. The rating agency put the highest stress on the country's political risks, explaining that "Poland's new government has initiated various legislative measures that are considered to weaken the independence and effectiveness of key institutions". In order to fulfill its election promises, the government introduced burdens on the financial sector's largest firms (including banks). This has, however, not hampered the supply of loans so far. Another charge, which aims to increase the competiveness of small and medium enterprises, is the introduction of a new tax on the retail sector. The final details of this tax are now being discussed and it is likely to be introduced shortly.

Chart 12:
Company insolvencies in Poland, by sectors, in 2015



Source: Coface

So far, sectorial taxes have not hampered Poland's business activities, although a more cautious approach to fixed asset investments and some levels of uncertainty over further burdens are being expressed by a number of corporates. Higher domestic demand and growing exposure to export markets (supported by comfortable levels of exchange rates) contributed to improvements in the corporate sector. Last year company insolvencies dropped by 10% y/y. Sectors directly dependent on consumer demand benefited from the improved prospects of Polish households, while profitable activity on export markets (such as furniture and machinery) confirmed the insolvency statistics. Despite improving domestic and external economic conditions, as well as low oil prices, bankruptcies in the transport sector increased. Due to their strong exposure to foreign markets, road cargo transport companies are suffering from a slump in demand from the Russian market and the embargo. In addition, some Western European destinations (Germany, France) are subject to minimum local wage requirements, which are lowering the competitiveness of Polish companies. Last but not least, domestic competition in the sector remained strong, which imposed the acceptance of lower margins amid stable fixed costs.

Top 5 sectors
Pharmaceutical industry
Telecommunications
Paper
Furniture
Chemical industry

Flop 5 sectors
Metals
Construction
Wholesale
Retail
Transports

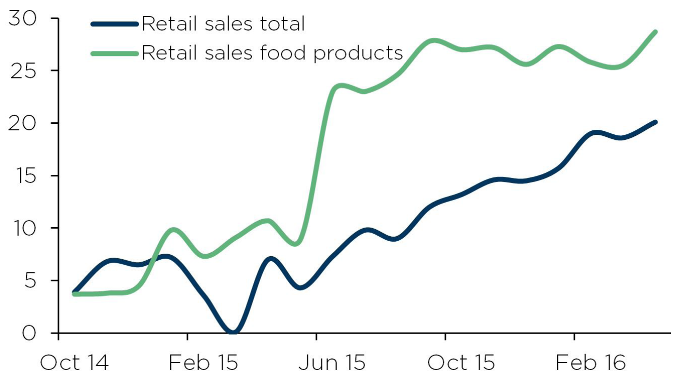
The 5 biggest insolvencies in 2015

	Company Name	Sector	Number of employees	Town
1.	Spółdzielcza Kasa Oszczędnościowo-Kredytowa	Financial	300	Warszawa
2.	HYDROBUDOWA Gdańsk	Construction	350	Gdańsk
3.	Q9	Wholesale	n.a.	Warszawa
4.	Hurtownia Opon KRAKUS Brożek	Wholesale	20	Kraków
5.	NFC POLSKA	Production and distribution	20	Szczecin

Romania - boost from the fiscal side

Economic growth in Romania reached 3.8% last year. The highest contribution came from private consumption, thanks to a fiscal stimulus. As from 1 June 2015, the value added tax rate for food products decreased from 24% to 9%. The government accelerated the introduction of this measure, aimed at boosting household consumption, and disposable income subsequently increased following the VAT cut. Private consumption represents 63% of Romania's GDP. A further cut, introduced this year, was the lowering of VAT rates on non-food products (from 24% to 20%). Further changes are planned as part of a new fiscal code. These include scrapping the tax on dividends and increasing the competiveness of enterprises via lower wage costs and taxes on active micro-enterprises, as well as cuts in excise duties on fuel and alcohol. Moreover, the minimum wage was increased by 19% in May 2016. All of these changes will support growth this year, which is expected to reach 4.2% according to Coface's forecast.

Chart 13:
Retail sales in Romania (%, annual changes)



Source: Eurostat

The structure of growth last year showed an increase of nearly 9% in investments. Similar to other countries, Romania took the opportunity to use EU funding in the final moments of access to the previous budget. Net exports made a negative contribution to growth, due to strong imports resulting from an increase in domestic demand. The government has been able to implement fiscal support measures, thanks to the comfortable situation of public finances. The general government deficit, already at a low level of 0.9% of GDP in 2014, declined to 0.7% of GDP in 2015. Romania has one of the most disciplined fiscal policies in the EU and this resulted in a modest public debt level of 38.4% of GDP at the end of 2015. However, strong tax cuts and expenditure increases are expected to widen the budget deficit to 2.9% this year and even more in 2017. There will be also a slight increase in public debt, to 40.9% this year, despite having the strongest growth in the CEE region. Nevertheless, public debt will remain at a manageable level – lower than in a number of other economies. The reduction of VAT rates has resulted in a fall in inflation, which reached a historical low of -3.5% y/y in May 2016. This should increase to positive territory in the second half of this year, supported by growing private consumption, faster wages growth and the increase in the minimum wage. Although these factors will put upward pressure on inflation, VAT cuts mean that high readings will not be delivered.

The corporate sector has benefited from a booming economy. The construction sector, which had the highest insolvency rates in 2014, benefited from improvements in the housing sector, with anacceleration in new buildings and construction permits. Large infrastructural projects, on the other hand, were often delayed. Despite increased absorption of EU funds, institutional inefficiency hampered greater usage in this regard. The construction sector constituted 16% of all insolvencies last year. It accounted for one of Romania's biggest insolvencies and was one of the worst performing sectors in terms of insolvency rates (almost 6 bankruptcies per 100 active construction companies).

Last year, insolvencies in Romania dropped by an impressive 49.5%, y/y. However, a more detailed analysis indicates that the highest decrease was among non-active companies - a phenomenon which resulted in a strong fall in total insolvencies. The share of companies which had zero turnover, or did not submit financial statements last year, amounted to 59%. The breakdown also shows that a further 23% share was taken by very small companies (with turnovers of up to EUR 100,000). Nevertheless, despite a contraction in the number of bankruptcies, Romania's insolvency rate remains the one of the highest among CEE economies. There were more than 2 bankruptcies per 100 active companies in 2015.

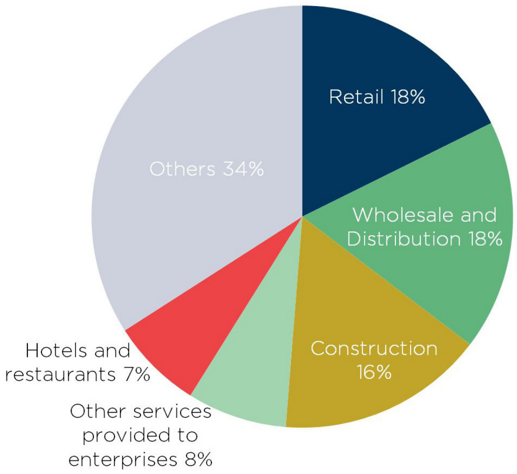
Liquidity management was one of the causes of bankruptcies. The liquidity of companies has decreased, due to lengthy periods for collection of receivables - despite one third of insolvent companies reporting increased turnover and higher profits. Moreover, the days-sales-outstanding ratio increased, after having doubled already in 2014 (181 days) compared to 2008 (95 days). The weak financial performance that companies experienced in 2014 led to payment difficulties and finally caused insolvencies in 2015. Overall sales dropped by 5% during 2014 and the net result was 7.9% lower. Last but not least, the indebtedness rate has increased significantly over recent years, rising from 76% in 2008, to reach 123% in 2014.

Chart 14:
Structure of insolvency proceedings

Turnover	2015	2014	Dynamics 2015/2014	Share in total
Without financials	4,514	10,132	-55%	46%
Zero - no activity	1,303	3,766	-65%	13%
EUR 0-100K	2,287	4,082	-44%	23%
EUR 100K-500K	937	1,231	-24%	9%
EUR 500K-1,000K	268	327	-18%	3%
EUR 1-5 mio	455	476	-4%	5%
EUR 5-10 mio	66	79	-16%	1%
EUR 10-50 mio	51	66	-23%	1%
EUR 50-100 mio	3	8	-63%	0.03%
> EUR 100 mio	2	3	-33%	0.02%

Source: BPI, MF, Coface

Chart 15:
Company insolvencies in Romania, by sectors, in 2015



Source: Coface

With growing household consumption and a sizeable decrease in the VAT rate on food products, the retail sector benefited from booming sales. This translated to a large drop, of 59%, in retail insolvencies last year. Nevertheless, the high number of active retail and wholesale companies led to the sector being the largest group represented in the total insolvency breakdown.

Top 5 sectors
Health and social care
IT
Financial intermediation
Real estate transactions
Other services rendered to enterprises

Flop 5 sectors
Manufacture of textiles, clothing and footwear
Sewage and garbage removal; sanitation and similar activities
Construction
Hotels and restaurants
Food and beverage industry

The 5 biggest insolvencies in 2015

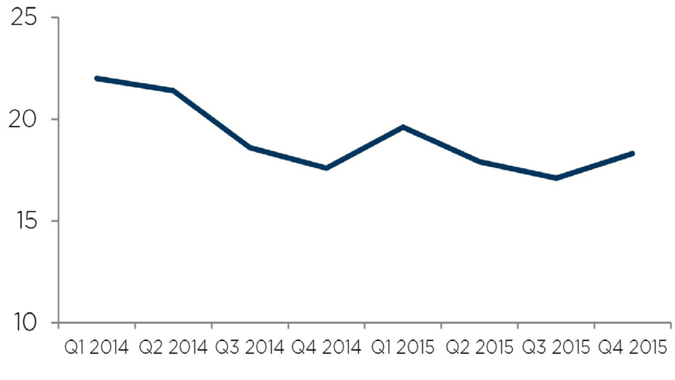
	Company Name	Sector	Number of employees	Town
1.	FAMILY HOME CONCEPT SRL (FOSTA DOMO RETAIL SA)	Retail	1,052	Bucharest
2.	AMBIENT SRL	Wholesale and distribution	1,276	Sibiu
3.	SUCCES NIC COM SRL	Retail	899	Ilfov
4.	STRACO GRUP SRL	Construction	513	Bucharest
5.	OCEAM SRL	Retail	1,431	Iasi

Serbia - economy awaits stronger contribution from private consumption

Serbia's economy recorded a weak growth rate of 0.7% last year. This was, however, an improvement following the recession experienced in 2014, where the growth rate was -1.8%. Unlike most other CEE economies, Serbia did not have the benefit of private consumption being the main growth driver. Household consumption decreased for a fourth year in a row, caused by the weak labour market. The decline in real wages reached 2.5% y/y last year and the restructuring of state-owned enterprises will result in further redundancies. The unemployment rate remains high, at 17%, even though it has declined in recent years. Retail trade and wage data for the first few months of 2016 signals that some revival in household consumption is likely to take place.

2015 growth was fueled by growing investments and the positive contribution of net exports. Investments benefited from significant monetary easing and the improving business environment. The recovery of trading partners supported the growth of exports, which are mostly destined for Italy, Germany, Bosnia and Herzegovina, Russia and Romania. As a non-EU country, it was expected that Serbia would benefit from its free trade agreement with Russia and not being covered by the Russian embargo – but this did not lead to a significant increase. The Russian recession resulted in a contraction of Russian imports, but even in 2014, when Russian growth was positive, Serbia only sent 7% of its total exports to the country. Nevertheless, total exports should support Serbia's economic activity again this year, with the benefits of demand coming from EU markets. However, as a small economy, Serbia is not able to offer a wide supply of exportable goods. Its accession to the European Union remains a priority for the government.

Chart 16:
Unemployment rate (%, working age population 15-64 years old)



Source: Statistical Office of the Republic of Serbia

Fiscal consolidation and structural reforms are on their way, but they have included unpopular measures such as a 10% nominal cut in compensations and pensions, which have negatively affected private consumption. Progress in implementing restructuring is crucial and will bring further risks if it fails or delays. Coface forecasts that GDP growth will speed up to 2.0% this year and 2.5% in 2017. Nevertheless, the situation of public finances will remain challenging, with the general government deficit slightly below 3% of GDP in the best case scenario, while gradually increasing public debt will creep closer to 80% of GDP.

Facing improved, but still challenging economic conditions, company insolvencies rose by 7.0% y/y in 2015, to reach 4.05%. As seen in many other economies, the worst performing industries included the steel and construction sector. Indeed, the two biggest insolvencies in Serbia last year were companies from the steel sector. With a gradual rise in household consumption, increasing confidence, the effects of past monetary easing, growing foreign direct investments and public investments, along with increasing foreign demand, the corporate sector should experience an improved environment and conditions for doing business.

Top 5 sectors 👍
IT
Telecomunications
Oil industry
Pharmacy
Agriculture

Flop 5 sectors 👎
Steel
Construction
Food
Retail
Wholesale

The 5 biggest insolvencies in 2015

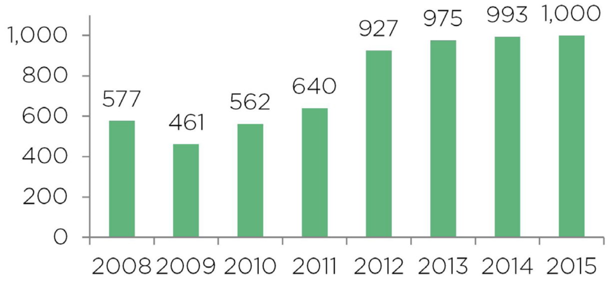
	Company Name	Sector	Number of employees	Town
1.	SIRIUM STEEL DOO	Steel	270	Sremska Mitrovica
2.	FABRIKA ŽELEZNIČKIH VOZILA ŽELVOZ	Steel	392	Smederevo
3.	KONCERN FARMAKOM M.B. ŠABAC	Food	457	Šabac
4.	BIP AD	Food	530	Belgrade
5.	INDUSTRIJA MAŠINA I TRAKTORA AD	Machinery	809	Belgrade

Slovakia - attracting further automotive investments

In 2015, the Slovak economy expanded by 3.6% - the strongest result for four years. The main contribution came from gross fixed capital formation, thanks to a higher usage of EU funds at the end of the drawing period of the previous EU budget. As a result, investments delivered 2.9 percentage points of total output growth - the highest contribution since 2005. Another component of domestic demand, private consumption, also made a solid input to economic activity, as it benefited from the improving labour market, wages growth and negative inflation. Slovakia's unemployment rate has been on an improvement track and declined to 11.5% last year - whereas not so long ago, in 2013, it stood at 14.2%. In April 2016, unemployment decreased further, to 10.2%. An annual single-digit average is likely to be reached in 2017. Although the current level is an improvement, Slovakia's unemployment rate is higher than the EU average, as well as that of its main regional peers. The country has experienced higher levels of long-term and youth unemployment than its neighbouring economies. The governmental's social package aims to reduce the regional disparities which are also a characteristic of the Slovak labour market. On the positive side, real wages increased by 3% in 2015, the minimum wage rose to EUR 405 and salaries of civil servants progressed by 4%. Further growth in wages will support household purchasing power.

The automotive sector remains an important part of the economy. Slovakia is the largest car producer per inhabitant in the world, manufacturing 184 cars per 1,000 inhabitants. Good perspectives for the sector contributed to the pronounced results in industrial production last year. The Volkswagen scandal does not seem to have had a devastating effect on the brand's sales. This had brought some threats, as Volkswagen accounts for a 40% share of Slovakia's total car production.

Chart 17:
Car production in Slovakia (thousands)

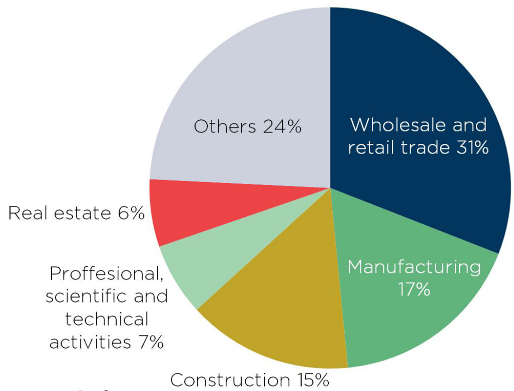


Source: OICA

The industry achieved growth of 6% in 2015, with the total number of manufactured cars exceeding 1 million units for the first time in the country's history. In addition to Volkswagen, major car manufacturers in Slovakia include KIA Motors and PSA Peugeot-Citroën. Jaguar Land Rover has announced investments worth more than EUR 1 billion, with the construction of a new factory beginning this year and production scheduled to take off in late 2018. This major investment will contribute to enhancing the GDP growth rate over following years.

Growth in 2016 will be driven by household consumption, which is benefiting from the healthy situation of the labour market, with rising employment opportunities and wages. Although private investments will not contribute to growth as much as they did last year, investments in addition to the Jaguar Land Rover project investment will be seen. The ECB's accommodative monetary policy will support businesses in making fixed investments. Production from the automotive sector is mainly for export and relatively good demand prospects will support the industry's growth. The slowdown of the Chinese economy and the Russian recession could still drag on sizeable export increases but exports to the country's main partners (including Germany, the Czech Republic and other EU economies) seem to be secured. This does not only apply to the automotive sector but to exports overall.

Chart 18:
Company insolvencies, by sectors, in 2015



Source: Coface

Against the backdrop of good economic conditions and solid growth, Slovak companies have been operating in comfortable business conditions. Last year, company insolvencies dropped by 14.6%, y/y. Besides overdue payments as causes of bankruptcies, businesses have also expressed they are still feeling the negative effects of the Russian embargo on their exports, a factor which is deepened by Russia's recession. Thanks to the speeding up of EU structural funds, the construction sector began to recover, following its decline over the six previous years. Insolvency data showed a 20% decrease, y/y, in the number of construction company insolvencies. Nevertheless, the share of the construction sector in total bankruptcies is relatively high, accounting for 15% last year. Due to the challenging situation in the steel sector, Slovakia's biggest bankruptcy in 2015 was Slovakia Steel Mills. The company's total debt, of EUR 244 million, by far exceeded its turnover of EUR 80 million in 2014.

Top 5 sectors 👍
Mining and quarrying
Education
Health and social work
Financial and insurance activities
Professional, scientific and technical activities

Flop 5 sectors 👎
Water supply, waste management and remediation activities
Electricity, gas, steam and airconditioning supply
Real estate activities
Wholesale and retail trade
Manufacturing

The 5 biggest insolvencies in 2015

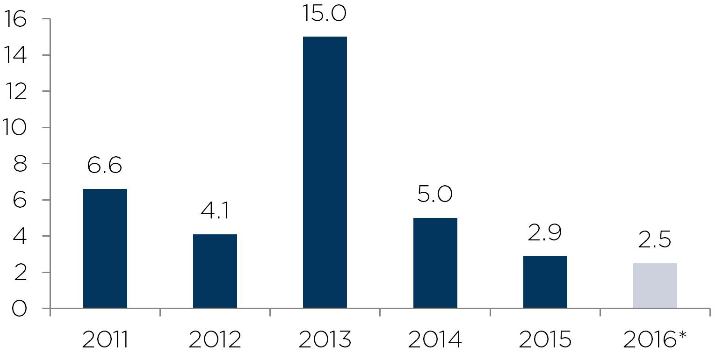
	Company Name	Sector	Number of employees	Town
1.	SLOVAKIA STEEL MILLS, a.s.	Manufacture iron and steel	250-499	Strážske
2.	BIO OIL s.r.o. & co., k.s.	Collection of waste	3-4	Špačince
3.	KOVOD, a.s.	Collection of wholesale of waste and scrap	50-100	Banská Bystrica
4.	FARMSYSTEMS s.r.o.	Wholesale of agricultural machinery, equipment and supplies	10-19	Pribeta
5.	Berto sk, s.r.o.	Production of meat products	150-199	Vysoká pri Morave

Slovenia - improvements for the economy and corporates

Subsequent to two years of recession in 2012 and 2013, Slovenia returned a solid growth of 3.0% in 2014. This pace saw just a slight decrease last year, to 2.9%. Strong exports and recovering domestic demand fueled the country's economic expansion in 2015. As with other CEE economies, there was a positive stimulus from EU funds at the end of drawdown period. Although public investments rose slightly, a strong rebound in private investments was constrained by continued deleveraging. Construction activities decreased last year and were unable to prolong the recovery which started to be experienced in 2014. Industrial production, on the other hand, recorded the highest growth rate for the last five years, mainly supported by increased manufacturing volumes of cars and other transport equipment.

Private consumption strengthened its contribution to GDP growth, thanks to the improving labour market. Nevertheless, wages growth was moderate and the average unemployment rate of 9.0% in 2015 was only slightly better than levels recorded in 2013 and 2014 (and still higher than rates recorded in the years up until 2012). In 2015 the rise in employment was low, mainly due to an increase in self-employment. The private sector, especially manufacturing, is likely to increase the number of employment opportunities this year and a further contraction in unemployment can already be seen in hard data. The unemployment rate dropped to 7.8% in April 2016.

Chart 19:
General government deficit (%)



* Coface forecast
Source: Coface

Household consumption will be the main growth driver for 2016 and 2017, while the contribution of exports will remain significant, but lower. The latter will mainly be caused by higher imports. Risks relating to slowing foreign demand are out of the baseline scenario but remain possible. Slovenia's main export countries are Germany, Italy and Austria but regional peers (Croatia, Hungary, Serbia), along with Russia, are also among the leading destinations for shipments.

On the public finance side, general government deficit was much lower than the peak value of 15% of GDP recorded in 2013 and it fell further from 5% of GDP in 2014, to 2.9% of GDP in 2015. This improvement was a result of increased tax revenues, including value added and corporate income taxes. Activities of the Bank Asset Management Company (BAMC), to which non-performing assets of the banking sector have been transferred, have contributed to widening the deficit. However, budgets for 2016 and 2017 forecast reductions in deficits, down to 2.1% and 1.7% of GDP, respectively. In June 2016, the European Council closed the excessive deficit procedure for Slovenia. This was thanks to the reduction of deficit to below 3% of GDP and based on the European Commission's forecasts for deficits of 2.4% of GDP in 2016 and 2.1% in 2017.

Chart 20:
Company insolvencies, by sectors, in 2015

Source: Coface

Improvements were experienced not only on the macro side, but also by corporates. In 2015, company insolvencies decreased by 34.3%, y/y. Rising demand supported trade companies, whose share in total insolvencies dropped to 17% last year, down from 21.4% in 2014. Favourable economic conditions, along with construction projects financed with EU funds, contributed to this noticeable decrease, even though the sector is still present in the flop list of Slovenian industries. Its delayed recovery prevented it from showing a rebound in insolvency statistics.

Top 5 sectors	Flop 5 sectors
Human health activities	Gambling and betting activities
Creative, arts and entertainment activities	Financial service activities, except insurance
Repair of computers and personal and houshold goods	Construction of buildings
Information service activities	Mining and quarrying
Manufacture of furniture	Manufacture of other transport equipment

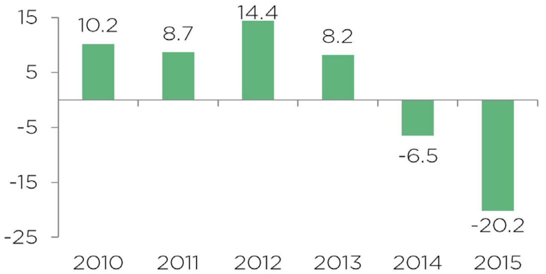
The 5 biggest insolvencies in 2015				
	Company Name	Sector	Number of employees	Town
1.	CIMOS d.d. AVTOMOBILSKA INDUSTRIJA	Automotive parts	1,020	Koper
2.	T - 2	Telecommunications	302	Ljubljana
3.	POMURSKE MLEKARNE d.d.	Manufacture of dairy products	157	Murska Sobota
4.	Seaway Yachts	Building of pleasure and sporting boats	112	Puconci
5.	JAVOR PIVKA	Manufacture of veneer sheets and wood-based panels	334	Pivka

Ukraine - Still weak performance on the cards

The weak performance of the Ukrainian economy reached its lowest level last year, with GDP growth contracting by 9.9%. A slow improvement is anticipated but the recession will still be present this year (forecast GDP growth of -3.0%), leading to a positive growth rate of 1.5% in 2017. Although the figure for 2017 will not be impressive, if it does materialise, it will be the highest growth rate since 2012.

The Ukrainian economy has been suffering from war-related destruction, which has resulted in the loss of the production and export capacities in the two separatist provinces in the east (Donetsk and Luhansk). It is here that a large percentage of the country's steel production facilities and coal mines are concentrated. The deep recession figure for 2015 does not include occupied territories and a part of the anti-terrorist operation zone. Even so, industrial production dropped by 13% last year, with huge decreases recorded in the Donetsk and Luhansk regions, of 35% and 66%, respectively. Nevertheless, the country's poor economic activity was mainly caused by the negative contribution from household consumption. High inflation (at almost 50%) and the heavy depreciation of the hryvnia resulted in reduced household purchasing power. Public sector wages and pensions, which were frozen last year, are to be indexed by a total of 12.5%. However, this will be insufficient to boost private consumption, especially as Coface forecast's an inflation rate of 20% this year.

Chart 21:
Real average wages (%, yearly dynamics)



Source: State Statistics Service of Ukraine

Exports declined last year and the dynamics remained negative during the first months of 2016. Although its currency has depreciated, Ukraine is unable to benefit much from its increased competitiveness, as the prices of its main export products (steel, coal and agricultural raw materials) are fixed on global or regional levels. Moreover, slow growth in production remains another constraint. Weaker export volumes were also recorded for shipments to EU markets. Although the Deep and Comprehensive Free Trade Agreement (DCFTA) with the EU became valid at the beginning of this year, it has not resulted in an upswing of exports. Ukrainian exports have already benefited from free access to EU markets, for most goods, since 2014 and the DCFTA seems to be supportive for EU exporters. However, the weakness of the Ukrainian hryvnia hampers the domestic demand and the expansion of EU exporters in Ukraine is also constrained as a consequence. Despite the tensions between the two countries and the recession of the Russian economy, Russia is still Ukraine's biggest export destination. In addition to a contraction in demand from Russia, Ukrainian exports are also suffering from an imposed Russian embargo on food, with import duties on other products and restricted transit of Ukrainian goods to third countries.

The country's economic deterioration and weak confidence indicators also had a negative effect on the corporate side. Companies are suffering from challenging business conditions and a slump in demand. Against this backdrop, insolvencies in 2015 increased by 20.8%, y/y. Even though this is already the highest surge by comparison with the rest of the region, many Ukrainian companies went out of business without even filing for insolvency in the course of last year. As the economy is rebounding very slowly and business conditions remain challenging, Coface anticipates that the number of company insolvencies in Ukraine will increase again in 2016.

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