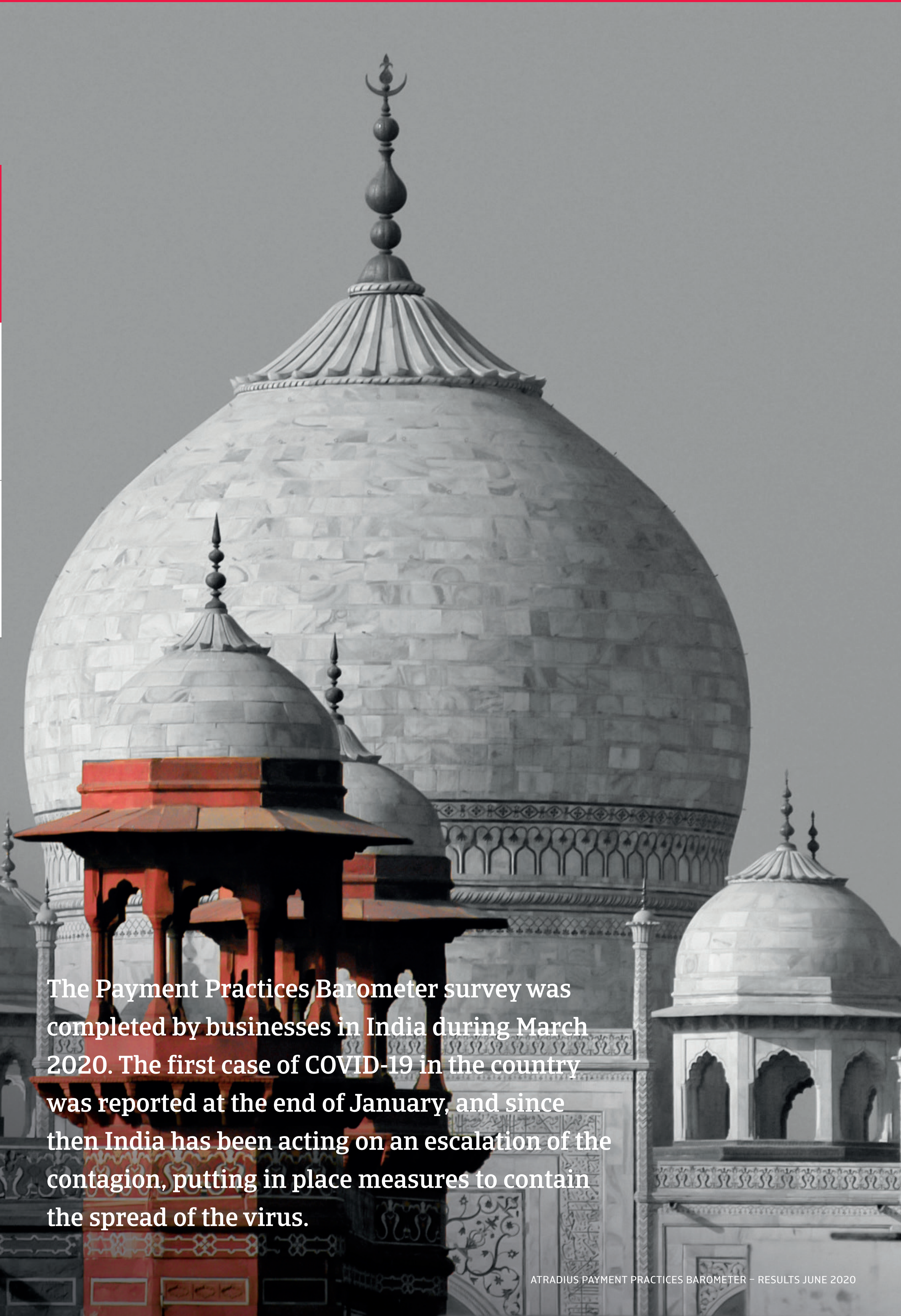
June 2020

India: bleak outlook for customer credit risk in B2B trade

Atradius Payment Practices Barometer



The Payment Practices Barometer survey was completed by businesses in India during March 2020. The first case of COVID-19 in the country was reported at the end of January, and since then India has been acting on an escalation of the contagion, putting in place measures to contain the spread of the virus.

**Arun Soundarajan,
Country Manager for India commented
on the report:**

"The outbreak of the coronavirus pandemic and the consequent supply disruptions from China have significantly hurt Indian industries that are heavily dependent on imports. The virus-containment measures that severely affected domestic demand are expected to cause a contraction of household consumption growth over the coming months. This adds to an expected decline of both investment and industrial construction, amid forecasts of a significant decrease in exports.

Overall, business performance and credit risk has deteriorated in all main industries in India, thus worsening the insolvency outlook this year.

Reflecting on all the challenges posed to the country's economic performance, businesses polled in India expressed concern over their short-term financing flexibility and working capital cycle over the coming months.

Introduction

Like many other economies that depend on Asian supply chains, the outbreak of the pandemic in India has triggered severe economic shocks. In the case of India, however, these latter added to an economic slowdown that had already started last year largely caused by faltering domestic demand.

Key takeaways from the report

The vast majority of businesses in India anticipate a significant deterioration in B2B payment behaviour. Key indicators of financial stress echo this, including the year-on-year threefold increase in write-offs of uncollectable debt and doubling in average value of long-overdue invoices. In all, the majority of respondents to the survey pointed to significantly lower success rates in debt collection than last year.

Perhaps as an indicator of a reduced appetite for risk amid an expected rise in insolvencies, total value of B2B sales transacted on credit has declined compared to last year's survey results. This is not surprising when you consider that the vast majority of businesses polled used self-insurance as a risk mitigation tool. While any risk-mitigation technique is better than none, self-insurance does little to transfer risk and can prove to be costly during a period of increased insolvencies.

Businesses in India predict an increase in reliance on bank finance in the coming months. In addition they could benefit from a strategic approach to credit management combining several approaches including pre-credit assessment checks of all customers, discount incentives for early settlement of invoices and payment guarantees. These may be letters of credit, credit insurance and payment bonds.

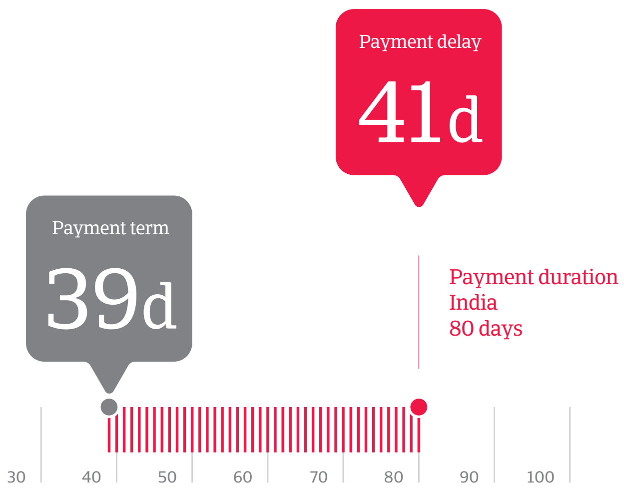
Survey findings for India

Decrease in B2B sales on credit reflects increase in credit risk environment

The Atradius Payment Practices Barometer survey in India reveals that respondents polled in the country transacted half of the total value of their B2B sales on credit. This is lower than the average recorded last year (55%). The decreased use of B2B trade credit in India is most probably a reflection of a heightened perception of customer credit risk, triggered by the severe impact of the coronavirus outbreak on the country's economy, leading to a subdued outlook and an expected rise in insolvencies.

In terms of market split for B2B trade, survey findings highlight that 56% of survey respondents' sales on credit were transacted on the domestic market (regional average for Asia: 61%), and 44% on foreign markets (regional average: 40%). This is most often the case for both SMEs and enterprises in the wholesale trade sector, who appeared to be the most likely to trade on credit terms with their B2B customers, particularly abroad.

Payment duration in India



d = average days
Sample: companies interviewed (active in domestic and foreign markets)
Source: Atradius Payment Practices Barometer – June 2020

Significantly longer payment terms accommodate need for short-term trade finance

Along with a decreased use of trade credit in B2B sales, survey findings highlight that B2B customers enjoy significantly longer payment terms than last year. This is particularly the case for SMEs and for the wholesale sector. Payment terms are on average ten days longer, at 41 days from the invoice date. This suggests that in times of severe cash flow issues, B2B buyers lean on suppliers to fill a gap in short-term trade financing. When asked about the underlying criteria for setting payment terms, 57% of respondents reported that they set payment terms in accordance with their company standards and internal business practices, while 44% do so in accordance with industry standards. As much as 30% of respondents set individual payment terms, customised according to the credit capacity of the customer.

Most common credit risk mitigation technique in India: self-insurance

Consistent with the more liberal payment terms offered to their B2B customers, respondents to the India survey appear to use an almost equally balanced mix of techniques aimed at mitigating customer credit risk in these challenging times. These most often include self-insurance (92% of respondents), and the request of guarantees of payment in B2B trade (84%). This is particularly the case for respondents from SMEs and in the retail / distribution sector. Additional customer credit risk management techniques commonly cited include: adjustment of payment terms, offers of discounts for early payment of invoices, requests for letters of credit, and trade credit insurance (each reported by as many as 80% of respondents).

Atradius · Key Findings

70 %

of Indian respondents anticipate a significant deterioration of their B2B customers' payment practices over the coming months

Atradius Payment Practices Barometer – June 2020

Write-offs of uncollectable B2B receivables three times higher than last year

According to survey findings, respondents in India reported having written off nearly 9% of overdue receivables as uncollectable (three times higher than the average of last year and the current average for the region). The survey also highlighted a significant increase in late payments from B2B customers. An average of 66% of the total value of B2B invoices were overdue (far above the 39% recorded last year). This compares to the 52% average for the region. Long-term overdue invoices (still outstanding after 90 days past due, with a high likelihood of turning into bad debts) amount to 29% of the total value of B2B invoices issued by respondents (regional average: 15%).

Overdue invoices are cashed in within 39 days of the invoice due date, significantly longer than the 24-day average of one year ago, and above the 27-day average for the region. In all, the survey respondents indicated significantly lower success in debt collection than last year, consistent with the substantial worsening of the insolvency environment, particularly at country level. Survey responses showed that collecting outstanding debts was most difficult in the ICT/electronics, chemicals and pharmaceuticals industries.

When asked about the reasons for payment delays from their B2B customers, 70% of respondents in India stated that B2B customers delay payments as they use outstanding invoices

> *"As a key driver of working capital, businesses should focus their attention on account receivables, and specifically the efficiency of their turnover through a strategic approach to credit management. These strategies should aim at protecting their balance sheet from losses, and remain financially sound particularly, but not only, in times of economic uncertainty."*
>
> **Arun Soundarajan, Country Manager for India**

as a form of financing. In order to manage the risk of liquidity constraints caused by delayed B2B payments, most of the respondents (55%) postponed payment of invoices to their own suppliers, 40% needed to strengthen their internal credit control procedures increasing time, resources and costs to chase overdue payments, and almost the same percentage (39%) needed to pursue additional financing from external sources.

Poor outlook for B2B customers' payment practices

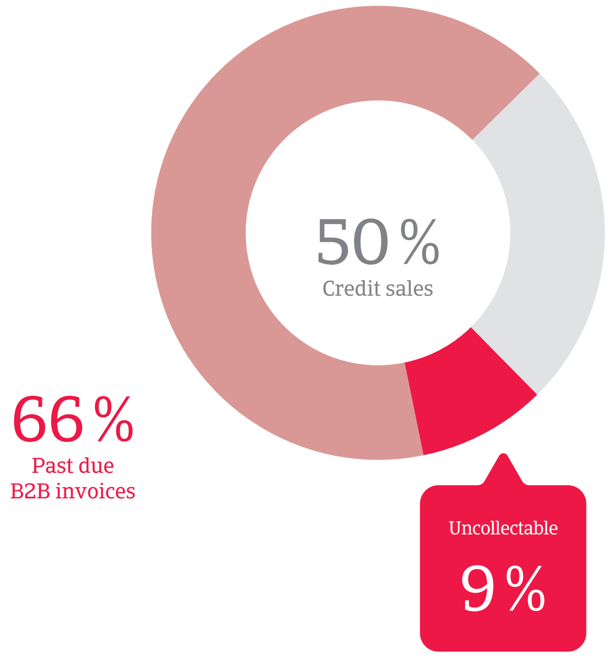
Respondents in India are deeply pessimistic about the payment practices outlook for their B2B customers over the coming months, with a vast majority (70%) of respondents anticipating a significant deterioration. In particular, the default risk is expected to increase in the agriculture, construction and machines industries, as well as in the hospitality sector, with negative repercussions on the cash flow and investment capacity of the businesses. In response, many businesses are planning on further strengthening their credit management procedures, with 62% of respondents planning on resorting to self-insurance. In addition, many respondents anticipate requesting guarantees of payment more often, or seeking to avoid the concentration of trade credit risk on single buyers in their customer portfolios.

Dependence on bank finance expected to increase due to cash flow constraints

Consistent with the challenges posed to the country's economic performance by the pandemic-induced domestic containment policies and the global economic downturn, survey respondents in India expressed concern over their working capital cycle and short-term financing flexibility. For 9 in 10 respondents, this will increase dependence on bank finance. However, 83% of respondents believe that the liquidity injected into the economy by the banking system will largely contribute to offset the impact of the economic crisis on the business community. Displaying an optimistic mindset, 95% of the India survey respondents expect their business performance to improve significantly over the coming months. In particular, respondents expect a recovery of investments (67%) and household consumer demand (57%) to have a positive impact on their business. 37% of respondents, chiefly from large enterprises and in the wholesale trade sector, expressed concern about the negative impact of an increasing exchange rate volatility on their export flows over the next 12 months.

Uncollectable B2B receivables in India

(% of total value of B2B receivables)



Sample: companies interviewed (active in domestic and foreign markets)
Source: Atradius Payment Practices Barometer – June 2020

Overview of payment practices in India

By industry

Chemicals

Nearly 30% of the total value of B2B invoices is over 90 days overdue

28% of the total value of invoices in the Indian chemicals sector remains unpaid more than 90 days past the due date. This percentage is consistent with the average for the country. 8% of the total value of B2B invoices is written off as uncollectable (country average: 9%). As highlighted by the survey findings, an average of 67% of the total value of B2B invoices in the chemicals industry extends past the due date. This is in line with the country average. Respondents reported outstanding receivables in their own industry were most difficult to collect. According to most of the survey's respondents, payment delays are caused by B2B customers in the Indian chemicals industry using outstanding invoices as a form of financing, or because of disputed invoices (67% of respondents in each case).

In terms of average timings of invoice-to-cash-turnaround, 65% of respondents reported a DSO (Days Sales Outstanding) up to 30 days, 23% up to 90 days and 12% of 90 days or more. This results in a 33-day industry average (country average: 60 days). If considered in light of the strong focus on debt collection displayed by Indian respondents in the chemicals industry, particularly through internal sources as well as law offices and attorneys (88% in each case), this average DSO figure confirms a relatively high success rate in collecting receivables, particularly invoices of high value.

9 out of 10 chemicals businesses choose to self-insure

9 out of 10 Indian respondents in the chemicals industry reported they retain and manage customer credit risk internally (self-insurance), or ask for guarantees of payment. 87% request letters of credit from their B2B customers to whom they sell goods and services with deferred payment.

In order to remain financially sound and avoid liquidity constraints caused by customer payment defaults, many respondents from the industry (54%) said they needed to delay payment of invoices to their own suppliers. In addition, 45% reported they had to increase time, resources and costs to chase overdue invoices.

Despite expected deterioration in credit risk, business confidence remains strong

Significantly more Indian respondents from the chemicals industry (71%) expect customer credit risk to deteriorate than to improve (11%) over the coming 12 months. In response to this, most of the survey's respondents (80%) plan on selling on cash terms, on offering discounts for early payment of invoices and on putting in place measure to avoid credit risk concentration in their customer portfolio substantially more often over the coming months.

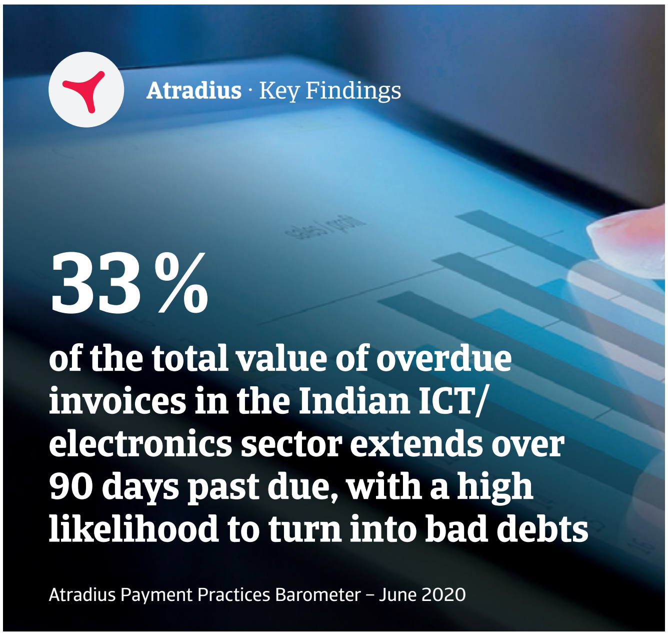
For 91% of respondents, dependence on bank finance will increase over the coming months due to the increased indebtedness of the industry. When asked their opinion on the outlook for the availability of bank financing over the coming months, 82% of the respondents in the chemicals industry are confident that banks will continue provide loans to businesses to alleviate cash flow constraints. With the same positive mindset, the majority of Indian respondents in the chemicals industry believe that the business performance of their industry in terms of sales and profits will improve over the coming months.

Textiles / clothing

Majority experience late payment as customers use overdue invoices as a form of financing

For 7 in 10 of the survey respondents in the Indian textiles/clothing industry, B2B customers delay payments because they use outstanding invoices as a form of financing, or due to disputes over the goods and services provided. Based on survey findings, late payments in the industry amount to an average of 66% of the total value of invoices issued in B2B trade (in line with the country average). Long overdue receivables (more than 90 days overdue) average 28% of the total value of overdue payments (in line with the country average). The proportion of receivables written off as uncollectable averages 8%, (country average: 9%). Respondents reported that they had the most difficulty in collecting debts from the consumer durables sector.

In terms of average timings of overdue invoices collection, 47% of respondents reported a DSO (Days Sales Outstanding) up to 30 days, 28% up to 90 days and 25% of 90 days or more. This results in an 89-day industry average (significantly above the 59-day country average). Despite the strong focus on debt collection displayed by Indian respondents in the textile/clothing industry (91% reported to use internal resources for debt collection), the average DSO figure points to a very low success rate in collecting receivables, particularly invoices of high value.



Late payments cause a ripple effect throughout the industry's supply chain

Over half of the respondents in the Indian textile/clothing industry (54%) reported that due to late payments from their customers they needed to delay payments to their own suppliers to avoid liquidity shortages. 45% needed to pursue additional financing from external sources.

In order to strengthen their credit management procedures, almost all businesses surveyed (94%) said they have resorted to self-insurance, (retaining and managing customer credit risk in-house). Selling on a cash basis and putting in place measures to avoid a concentration of credit risk are also credit management techniques frequently used in the industry.

Upswing in long overdue invoices expected with negative impact on cash flow

Significantly more respondents in the Indian textiles/clothing industry (69%) anticipate a deterioration of the risk of customer payment default than an improvement (10%) over the coming months. 21% do not expect any change. In particular, the anticipated deterioration in customer credit risk is expected to cause an upswing in long-term (over 90 days old) outstanding invoices, further straining businesses' cash flow. To safeguard their liquidity position from the negative impact of customers' payment default, nearly half of the respondents in the industry (47%) plan to offer discounts for early payment of invoices, and 40% to request guarantees of payment more often over the coming months.

Looking ahead, respondents expressed concern about an increasing dependence of their industry on bank finance, due to higher levels of indebtedness. On a positive note, however, 4 in 5 respondents are confident that banks will further increase financial support for the industry going forward. When asked about the outlook for business performance of the industry, 92% of respondents said that business performance (sales and profits) will improve over the coming months.

ICT / electronics

Majority uses overdue invoices as a form of short-term finance

In terms of the average time it takes to cash in overdue invoices, 71% of respondents reported a DSO (Days Sales Outstanding) up to 30 days, 12% up to 90 days and 17% of 90 days or more. This results in a 54-day industry average (below the 59-day country average). When asked about the reasons for customers' payment default, 76% of respondents reported that B2B customers most often delay payment as a form of financing. Late payments also are quite often due to disputed invoices and inefficiencies of the banking system (69% of respondents).

Overall, survey findings show that late payment in the Indian ICT/electronics industry average 64% of the total value of the B2B invoices issued in the industry (country average: 66%). Long-overdue receivables (more than 90 days overdue, with a high likelihood of turning into bad debts) average 33% of the total value of overdue invoices (country average: 29%). The proportion of receivables written off as uncollectable averages 11% (country average: 9%). 3 in 5 respondents said they had the most difficulty collecting invoices from B2B customers in their industry.

Strengthening of internal credit control procedures needed to avoid cash flow issues

Over half of the respondents in the Indian ICT/electronics industry (57%) reported that due to late payments they needed to strengthen their internal credit control procedures. In order to do so, almost all respondents in the industry reported they resorted to the retention and management of customer credit risk internally (self-insurance).

For 55% of respondents, customers' late payments caused them to delay payments of invoices to their own suppliers, or to ask for an extension of their bank overdraft. To minimise the impact of poor cash flow on their business operations, all respondents reported to have increased costs, time and resources to strengthen bad debt collection operations through internal resources, or by employing law offices or attorneys (83% of respondents).

Dependence of industry on bank finance expected to grow in the near term

As observed earlier, respondents in the Indian ICT/electronics industry are strongly focused on the collection of bad debts. Over the coming months, over half of the respondents (52%) plan on increasing their dunning activities (outstanding invoices reminders), or on outsourcing debt collection to an external agency in addition to strengthening their dedicated internal resources. This is likely to be linked to concerns expressed by the majority of respondents in the industry (70%) about a further deterioration of B2B customers' payment practices in their industry over the coming months, resulting in a lengthening of DSO, with negative impacts on the investment capacity of the business.

Against this backdrop 86% of the respondents, particularly from the services sector of the ICT/electronics industry, foresee an increase in businesses dependence on bank finance due to cash flow constraints. However, respondents are confident that banks will play a major role in safeguarding the country's economy from the fallout of the pandemic. With the same positive mindset, 97% of respondents in the industry believe that business performance (sales and profits) will improve over the coming months.

SURVEY RESULTS

SURVEY DESIGN

STATISTICAL APPENDIX

Survey design for Asia

Survey objectives

Atradius conducts annual reviews of international corporate payment practices through a survey called the 'Atradius Payment Practices Barometer'. In this report focusing on Asia, which is part of the 2020 edition of the Atradius Payment Practices Barometer, companies from seven economies (China, Hong Kong, India, Indonesia, Singapore, Taiwan and United Arab Emirates) have been surveyed. Due to a change in research methodology for this survey, some year-on-year comparisons are not feasible for some of the results.

Using a questionnaire, CSA Research conducted 1,413 interviews in total. All interviews were conducted exclusively for Atradius.

Survey scope

- **Basic population:** companies from seven economies (China, Hong Kong, India, Indonesia, Singapore, Taiwan and UAE) were surveyed. The appropriate contacts for accounts receivable management were interviewed.
- **Sample design:** the Strategic Sampling Plan enables to perform an analysis of country data crossed by sector and company size. It also allows to compare data referring to a specific sector crossed by each of the economies surveyed.
- **Selection process:** companies were selected and contacted by use of an international internet panel. A screening for the appropriate contact and for quota control was conducted at the beginning of the interview.
- **Sample:** N=1,413 people were interviewed in total (approximately n=200 people per country). In each country a quota was maintained according to three classes of company size.
- **Interview:** Computer Assisted Web Interviews (CAWI) of approximately 15 minutes duration. Interview period: March 2020.

Sample overview – Total interviews = 1,413

Economy	n	%
China	209	14.8
Hong Kong	200	14.2
India	204	14.4
Indonesia	200	14.2
Singapore	200	14.2
Taiwan	200	14.2
UAE	212	12.3
Sector (total Asia)	**n**	**%**
Manufacturing	593	42.0
Wholesale trade/ Retail trade / Distribution	598	42.3
Services	222	15.7
Business size (total Asia)	**n**	**%**
Small enterprises	140	9.9
Medium-sized enterprises	949	67.2
Large enterprises	324	22.9

It may occur that the results are a percent more or less than 100%. This is the consequence of rounding off the results. Rather than adjusting the outcome so that it totalled 100%, we have chosen to leave the individual results as they were to allow for the most accurate representation possible.

Statistical appendix

Find detailed charts and figures in the Statistical Appendix for Asia. This is part of the June 2020 Payment Practices Barometer of Atradius, available at www.atradius.com.au/publications

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