Atradius
Managing risk, enabling trade

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Canada: trade credit KPIs hold steady despite Covid recession

Atradius Payment Practices Barometer

Chris Short
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commented on the report

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>
> *Businesses are right to be wary of these threats and should take steps now to protect themselves from future turbulence.*

On paper, things are looking good for businesses in Canada. A strong post-recession rebound is predicted for the economy. Close to three-quarters of the population over the age of 12 has received at least one dose of the vaccine. A raft of support measures forming Canada's Covid-19 support plan are in place and, for now at least for most, are ongoing. Yet despite this largely positive picture, businesses on the ground are more wary and less likely to express optimism.

This can clearly be seen in the results of the Payment Practices Barometer survey where despite recording the lowest levels of deterioration in payment timings in the USMCA region during recent months, businesses in Canada overwhelming told us that they do not feel optimistic about the future for their business.

Could this be explained by a more cautious national temperament? Possibly. However, it is more likely that businesses are looking ahead to the end of the government's Covid-19 Response Plan and, quite rightly, anticipating a rise in the number of insolvencies once external support is removed. This will be a dangerous time for businesses.

We are likely to see some evidence of domino-effects, where one major insolvency can cause a ripple of stress and possibly further insolvencies along a supply chain. More commonly, we will see bankruptcies among businesses that would have gone bust regardless of the pandemic, but that have been propped up over recent months by the Government support. Businesses are right to be wary of these threats and should take steps now to protect themselves from future turbulence.

Many of these steps will simply be good business sense. Get to know your customer. Are they struggling with cash flow? Perhaps extending payment terms will be enough to get them over this bumpy patch, or perhaps there are deeper structural problems in their business. Find ways to minimize the risk to your accounts receivable, take note of credit risk concentrations and work out how well you are placed to survive the worst-case scenario. If your business would struggle to cope with a large bad debt, or the bankruptcy of a key customer, now is the time to act with credit risk management tools such as factoring, letters of credit or trade credit insurance.

Key takeaways

Canadian business confidence lags behind peers

Canadian businesses were largely downbeat when asked about their outlook for the coming 12 months, lagging far behind their peers. Only 36% anticipate growth, far fewer than both the US (60%) and Mexico (81%). In many ways this is at odds with the survey data that showed Canada has the lowest levels of deterioration in customer payment practices and DSO (days sales outstanding) in the region. However, this largely pessimistic view could reflect the fact that 72% of businesses are braced to take the hit of bad debts internally. This is the highest percentage of businesses opting for self-insurance in North America. In addition, the majority of businesses told us they use trade credit to maintain existing relationships with customers, rather than using it as a tool to win new business. These are both areas that could be supported through the use of trade credit insurance.

B2B credit valued as a short-term finance tool

Businesses in Canada stressed the importance of trade credit as a way to support ongoing customer relations, including as way of providing short-term finance. Such a mutually supportive approach to trade credit can be incredibly valuable and a great way to 'oil the wheels of commerce'. This approach works best when there is a high degree of transparency and understanding between customer and supplier. However, although knowing your customer is key for all trading relationships, it does not protect businesses from the risk of unforeseen catastrophes. Businesses should take steps to protect themselves from going under if their customer collapses. Credit insurance provides peace of mind, however other steps such as avoiding concentrations of risk, ongoing monitoring of customer activity and bad debt funds can also help.

Businesses worry about cost of credit management

The majority of the businesses we spoke to in Canada told us that they did not increase the amount they traded on credit after the outbreak of the pandemic. Yet despite this, almost half told us that they had spent more on managing their account receivables over the past year, with additional costs spent on collecting overdue payments.

A significant proportion cited containment of credit management costs as a major concern for the coming months. For businesses that choose to self-insure their account receivables such costs can increase during periods of heightened credit risk, particularly where customers slow down payments to support their own liquidity. Outsourcing to a provider, such as a credit insurer, can prove to be cost effective in such instances, through enhanced operational and collection efficiencies and stability of liquidity.

More than a third plan to adopt credit insurance moving forward

Interestingly, 36% of the businesses we surveyed said they plan to adopt credit insurance during the coming months. This is by far the largest percentage of the region. The use of credit insurance will go some way to supporting businesses that expressed concerns about the costs of internal credit management and will provide liquidity security to support ongoing operations and possibly investment. The businesses that take on credit insurance will also gain insight into the enhanced market intelligence of underwriters, which will be a valuable tool for expanding their customer base or exploring a new market.

Survey results for Canada

B2B credit sales remain stable following the outbreak of the pandemic

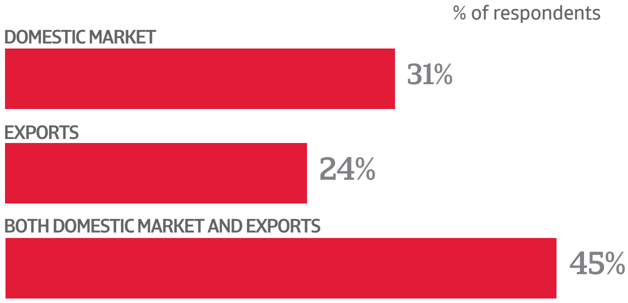
The Payment Practices Barometer survey findings reveal that the majority of businesses polled in Canada (63%) did not significantly increase credit sales in the months following the outbreak of the pandemic.

This contrasts with the US and Mexico where 51% and 62% respectively told us they traded on credit more often than they did one year ago. Overall, businesses surveyed in Canada made an average of 54% of the total value of B2B sales on credit over the past year. 58% occurred on the domestic market and the remainder on export markets.

Among the industries surveyed in Canada (chemicals/pharma, steel/metals and services), the most conservative trade credit policy was seen in the chemicals/pharma industry, whereas businesses in steel/metals displayed a more liberal approach. However, the greatest appetite for credit sales is seen in the Canadian services sector, which favoured trading on credit domestically. The chemicals/pharma industry was the most active in trading on credit with B2B customers abroad.

Canada: how do you expect your business performance to change over the coming months?

Which key developments will drive your business improvement?



Sample: all interviewed companies
Source: Atradius Payment Practices Barometer - July 2021

36%

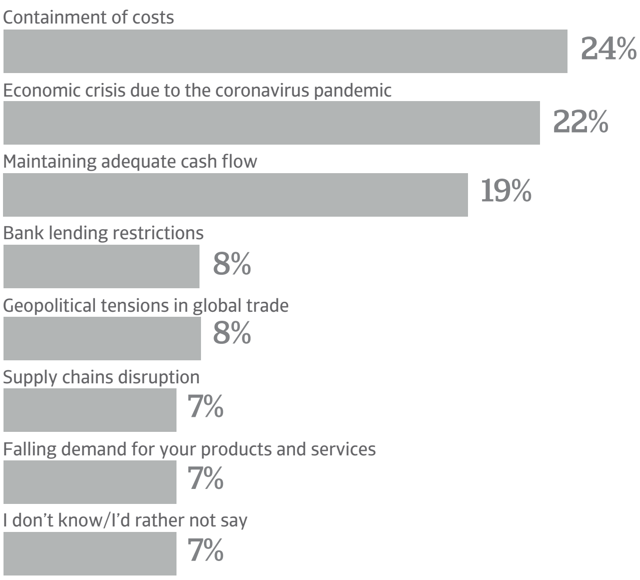
of the businesses surveyed in Canada plan to employ credit insurance over the coming months, (more than the 26% reporting the same in the US and 31% in Mexico).

Businesses offer credit to consolidate established trade relations

55% of the businesses polled in Canada told us they accepted trade credit requests to encourage repeat business with established B2B customers (compared to 38% in the US and 53% in Mexico). 23% accepted trade credit requests to win new customers (compared to 40% in the US and 26% in Mexico). Additional reasons for offering trade credit cited by respondents in Canada include: staying competitive in their markets, and allowing customers time to pay (for example, if they are awaiting payment from their buyers, need to sell goods on, or to obtain bank finance). Interestingly, the latter appears more common in Canada than it is in the US and Mexico. This suggests that trade credit is more often used as a short-term trade finance tool by Canadian suppliers than their peers in the region.

Canada: top 5 greatest challenges to business profitability in 2021

% of respondents



Sample: all interviewed companies
Source: Atradius Payment Practices Barometer - July 2021

Credit management costs increased during the pandemic

48% of respondents in Canada reported increased administrative costs associated with the management of accounts receivable during the year following the outbreak of the pandemic (compared to 55% in the US and 37% in Mexico). This is a fairly sizeable increase in costs considering that most businesses in Canada did not increase their credit trade. Most of the cost increases were reported by businesses that relied on their own internal credit management resources, self-insurance, (as opposed to using trade credit insurance, factoring or professional debt collection services, for example). Correspondingly, self-insurance was the most-commonly used credit management technique in Canada (as reported by 72%, compared to 69% in the US and 66% in Mexico). Businesses told us that credit management costs also applied to acquiring and monitoring credit information. This was sourced most often through the customer's financial statements, credit information from specialist agencies monitoring customer credit risk and through the evaluation of internal information provided by the customer.

40% of respondents in Canada (same as in Mexico and compared to 37% in the US) reported increased capital costs in the months following the outbreak of the pandemic (i.e. financing or interest costs paid during the time-lag between the credit sale and the settlement of the invoices). 35% of businesses reported increased costs for the collection of unpaid invoices. This is a lower percentage than last year, but is similar to the survey results seen in the US (38%) and Mexico (36%).

Two-thirds of businesses employed trade credit insurance last year

Survey data shows that second to self-insurance a significant number of businesses employed trade credit insurance after the outbreak of the pandemic. This appears to be used by 65% of respondents in Canada, compared to 53% in the US and 68% in Mexico. Against this backdrop, it is not surprising that respondents in Canada (and in Mexico) appeared to be more successful in keeping costs for collection of long-term overdue trade debts (over 90 days overdue) under control. Increases in these costs were reported by 23% in Canada, compared to 30% in the US and 20% in Mexico. Consistent with this, year-on-year increases in DSO were reported by just 27% of respondents in Canada, compared to 36% in the US and 38% in Mexico.

Businesses in Canada reported by far the lowest levels of deterioration in customer payment practices in the USMCA region over the past year. 32% reported deterioration in Canada, 47% in the US and 44% in Mexico. This relatively favorable picture contrasts with the more negative result of the 35% of businesses that reported increases in collection costs.

However, this may be explained by the tight grip exerted by Canadian businesses on curbing the impact of customer credit risk and unlocking working capital tied up in overdue receivables.

Average payment terms hold steady over the past year

To mitigate credit risk, 65% of the businesses polled in Canada told us they did not vary payment terms in the year that followed the outbreak of the pandemic (higher than the US and Mexico with 49% and 54% respectively). Over the past year 24% offered customers longer time to settle invoices (41% in the US and 40% in Mexico). The Canadian chemicals/pharma industry displayed the most conservative approach, with only 12% of respondents offering more relaxed payment terms over the past year, averaging 41 days from invoicing. In contrast, 30% of the steel/metals industry offered more relaxed payment terms over the past year, averaging 47 days from invoicing. Consistent with the regional pattern, most Canadian businesses set payment terms that reflect company standards. This was reported by 45% of survey respondents, compared to 48% in the US and 61% in Mexico. Although applied less often, both the credit capacity of the customer and the payment terms received by their own suppliers also dictate payment terms set by Canadian businesses.

Canada: on average, within what time frame do your B2B customers pay their invoices?

% of respondents

Sample: all interviewed companies
Source: Atradius Payment Practices Barometer - July 2021

Businesses turn to external financing to fund credit risk management costs

Businesses reporting an increase in late payments told us they allocated more time and resources to chase unpaid B2B accounts and set in place more frequent customer credit risk monitoring activities. This tallies with the increases in administrative costs seen earlier. Possibly as a result of these costs impacting the business and operational working capital, businesses polled in Canada accessed external financing more frequently than their peers in the US and Mexico. Further detail can be found below in the overview by industry section.

An average of 48% of the total value of B2B invoices issued by businesses polled in Canada are overdue (compared to 50% in the US and 45% in Mexico). 5% of long-term overdue invoices (more than 90 days overdue) were written off. This is the same percentage as reported in Mexico and lower than the 8% for the US. As seen earlier, 32% of businesses polled in Canada reported deterioration of B2B customers’ payment practices over the past year (much lower than the 47% in the US and 44% in Mexico). This suggests a more benign trade credit risk environment for Canadian businesses than for their peers in the region.

Containing credit management costs considered main threat to business profitability

24% of businesses polled in Canada are concerned about the containment of credit management costs over the coming months. This is the highest parentage in the USMCA region and compares to 19% in the US and 12% in Mexico. 22% are worried about the uncertain outlook for the pandemic worldwide (18% of respondents in the US and 28% in Mexico).

Maintaining adequate cash flow is also mentioned as a factor that could adversely impact business profitability, although cited less often by the businesses we polled in Canada (19%) (and reported by 19% in US and 31% in Mexico). Interestingly, a potential resurgence in geopolitical tensions affecting international trade was also only cited by a small proportion of the businesses we surveyed, although this was listed more often by businesses in the Canada (8%) compared to the region (5% in the US and 2% in Mexico).

This may point to Canadian businesses being more skeptical than their peers across the region over greater geopolitical stability going forward.

Canadian business confidence is lowest in USMCA region

Improvement in business performance over the next 12 months is anticipated by only 38% of respondents in Canada (compared to 60% in the US and 81% in Mexico). 45% anticipates that potential improvement will come from a combination of a rebound in the domestic economy and healthier export flows (an opinion shared by 39% in the US and 48% in Mexico). 31% believes the improvement in performance will be mainly due to a rebound of the domestic economy (41% in the US and 27% in Mexico). 24% anticipates improvement in their business performance will stem exclusively from increased export flows (compared to 18% in the US and 24% Mexico).

Looking ahead, 51% of businesses in Canada told us they expected credit would be used more often as a short-term trade finance tool over the next 12 months (significantly more than in the US 32% and Mexico 36%).

Credit insurance planned by more businesses in Canada than across the region

Looking ahead, 36% of businesses plan to employ credit insurance over the coming months, (more than the 26% reporting the same in the US and 31% in Mexico). The majority, however, favour self-insurance with 41% planning to increase their internal credit management resources to mitigate the impact of trade credit risk on the business (compared to 51% in the US and 31% in Mexico). For businesses in Canada these will include: offering discounts for early payment of invoices, adjusting credit terms to reflect the credit risk profile of the customer and reducing reliance on single large buyers to avoid trade credit risk concentrations in their sales ledgers. 38% plan on requesting cash payments more often over the coming months (largely in line with the 36% of respondents reporting the same in the US and Mexico alike).

Despite these differing approaches to credit management, Canadian businesses share a common target with their peers of keeping Days Sales Outstanding (DSO) under control over the coming months. 34% of businesses polled in Canada expressed concern over the potential for an upward trend of DSO over the coming months (compared to 43% in the US and 38% than in Mexico).

Canadian businesses appear to be more skeptical than their peers across the region over greater geopolitical stability going forward.

Overview of payment practices in Canada By industry

CHEMICALS/PHARMA

Overview

The chemicals/pharma industry in Canada ranks among the world's largest suppliers of chemicals and plastics products. About 80% of Canada's chemical production is exported, mainly to the US. In the year following the outbreak of the pandemic, businesses polled in the local industry reported increased use of trade in B2B transactions, largely due to consolidated trade relationships with established customers. However, the industry's more liberal trade credit policy aimed at encouraging repeat business, led to increased costs for the management of B2B trade debts.

This was in particular due to less effective collection of long term overdue invoices, which adversely impacted DSO in the industry. In 2021, growth expectations are positive, mainly due to the global high demand generated by the pandemic. Pharmaceuticals also benefits from rising health costs, with value added expected to increase further in 2021 after already experiencing a 5% increase last year.

Increased B2B trade debts management over the past year

54% of the total value of B2B credit sales in the chemicals/pharma industry in Canada is overdue. This compares to 41% in the steel/metals industry and 48% in services). On average, overdue invoices are settled by 25-days past the due date. 6% of the total value of unpaid B2B accounts was written off. 55% of chemicals/pharma businesses told us they had to employ more resources and time to chase overdue payments and many told us that in order to avoid liquidity shortages they also sought external sources of funds, with consequent increases in their capital costs associated with trading on credit.

Perhaps due to the reported increased credit management activities, a significant number of respondents (68%) were able to keep DSO under control over the past year. The remaining respondents reported increased DSO over the same time frame, chiefly due to a more liberal trade credit policy combined with less effective collection of B2B trade debts. Taken together, these survey findings point to DSO now amounting to a 50-day average for the local industry.

More than half of US agri-food businesses use trade credit insurance

A significant majority of the Canadian chemicals/pharma industry are proactive in their approach to credit management. 80% relies on internal resources (self-insurance), 74% uses factoring and 72% employs trade credit insurance. The majority of businesses in the sector told us that they adjust payment terms offered to B2B customers to reflect their credit risk profile and manage of trade debts collection in-house.

Looking ahead, business in the industry seem to be primarily concerned about maintaining adequate cash flow levels over the coming months, and express concerns over the potential for any continuation of the pandemic economic slowdown to impact their profitability.

This is an indication that much of the chemicals/pharma industry in Canada anticipates financial distress for businesses going forward. This may explain why a significant percentage of respondents (66%) told us that trading on credit with B2B customers will become more widespread in the short-term to allow businesses more time to pay for their purchases on credit. When asked about the outlook for their business performance over the coming months, most of the businesses polled in the industry (nearly 40%) anticipated improvement in sales and profits over the coming months mainly coming from the combination of healthier domestic economic conditions and stronger exports.

STEEL/METALS

Overview

Last year, both manufacturers and traders alike in the steel/metals industry in Canada were severely impacted by deterioration of turnover and profit margins. However, due to ongoing government support programs, which remain a key contributor to the Canadian economy, businesses appear to have successfully cushioned the impact of customer credit risk on their operations. This year the industry has started to benefit from a rebound in some key buyer industries, such as construction. This may explain why, looking ahead, business confidence appears to be positive.

Credit insurance underpins stability of DSO

An average of 44% of the total value of B2B credit sales in the Canadian steel-metals industry were overdue last year, with most of the industry's customers taking around one month to settle overdue invoices. 3% of the total value of unpaid B2B accounts was written off as uncollectable. Despite this, 66% of steel-metals businesses appear to have successfully cushioned the impact of customer credit risk on their operations and reported no significant change to DSO, which held steady at a 63-day average. This is likely to be due to a widespread strategic approach to credit management, most often involving the use of credit insurance.

Where businesses reported an increase in DSO, the majority told us they opted for relying on their internal credit management resources (i.e. self-insurance) to minimize the impact of customer credit risk on their business operations. This primarily involved dedicating more resources and time to chasing unpaid invoices and strengthening in-house credit risk monitoring processes. In addition to leading to increased trade debt management costs (as reported by 47% of the respondents in the local industry), this approach proved to be less effective at safeguarding businesses from the negative impacts of deteriorating DSO on the liquidity position of the business. It also resulted in many businesses pursuing additional financing from external sources to avoid cash shortages, which in turn had an adverse impact on the business capital costs.

Containment of credit management costs is top of future concerns

Looking ahead into 2021, steel/metals businesses told us their primary future concern is to be able to keep trade debt management costs under control over the coming months. They also cited the uncertain outlook for the pandemic worldwide, alongside concern about protection of liquidity levels. The latter reflects local industry concern over potential difficulties in accessing bank lending leading to impaired liquidity positions over the coming months. Despite this, most of steel/metals businesses in Canada (55%) appear to be confident that their business performance (sales and profits) will not change significantly over the coming months. Industry peers who anticipate improvement going forward believe that predicted growth is likely to stem from both a rebound of the domestic economy and increased exports (52% of respondents). Fewer respondents (27%) anticipated improvement to come from stronger demand from foreign markets, and 21% expected that this would come mainly from improved conditions of the domestic economy. Against this backdrop, over half (53%) of the steel/metals businesses in Canada expressed the opinion that trading on credit will become more widespread over the coming months, primarily as a short-term trade finance tool for B2B customers experiencing financial distress. Moreover, most of the respondents in the local industry (58%) do not anticipate any significant change in DSO over the coming months. 26% anticipate increases, mainly due to less effective long-term unpaid B2B accounts collection and the remaining percentage of respondents foresees a decrease in DSO.

SERVICES

Overview

During the pandemic the services sector has been heavily affected by decreased turnover and profits due to lockdown measures taken to contain the spread of the virus. Late payments and bad debt have increased across some subsectors of the hospitality services industry.

In contrast, logistics and supply chain service segments (e.g. customs brokers, freight forwarders, supply chain management and warehousing) continue to see demand. The outlook for customer credit risk remains uncertain, therefore services businesses polled in Canada told us they plan to put in place all measures needed to safeguard their liquidity levels, including requesting guarantees of payment more often, or payment in cash.

Liquidity levels protection paramount for the services sector

Nearly 40% of the respondents in the sector in Canada told us that their customers' payment practices worsened in the year following the outbreak of the pandemic. This resulted in 48% of all B2B credit sales recorded as outstanding past the due date, on average up to 33 days late. 6% of the total value of B2B receivables was written off. Corrective measures to safeguard businesses from the impact of customer credit risk was most commonly done through reliance on credit management through internal resources (i.e. self-insurance, reported by 61% of respondents). Delaying payments to suppliers was the most common measure applied by respondents in the services sector. In addition, businesses tightened credit control processes, employed additional resources to chase unpaid B2B accounts and accessed external financing sources to avoid potential liquidity shortages.

Interestingly, besides skewing administrative costs upwards, the self-insurance approach led to increased capital cost for a significant number of respondents (42%). This may explain why a sizeable percentage of services businesses in Canada told us they set payment terms according to the availability and cost of capital needed to finance credit sales. The strong focus on liquidity protection measures can be seen in the strict controls on DSO (reported by 60% of respondents) over the past year. DSO now averages 84 days.

Trade debt cost containment top future concern over the coming months

Consistent with the upward trend in administrative costs for managing unpaid B2B accounts, many businesses reported their top future concern is to be able to contain credit management costs over the coming months. Uncertainties over the outlook for the pandemic worldwide, and concern over liquidity levels, also worry businesses in the services sector. When asked for their opinion on the outlook for their business performance (sales and profits) over the coming months, the services sector did not have a clear cut opinion, with half anticipating no change and half predicting improvement.

Most of the latter (42%) believe that predicted growth is likely to stem from both a rebound of the domestic economy and increased exports. 39% anticipated improvement to come from a rebound of the domestic economy only. The remaining respondents expect improvement in business performance to come from stronger demand from B2B customers abroad. Against this backdrop, 36% of services sector businesses expressed the opinion that trading on credit will become more widespread over the coming months, primarily as a short-term trade finance tool for B2B customers experiencing financial distress. This may reflect the widespread belief that the Canadian services sector will experience a deterioration of DSO over the coming months, as expressed by 40% of respondents.

Survey design for the USMCA

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 the USMCA, which is part of the 2021 edition of the Atradius Payment Practices Barometer, companies from Canada, Mexico and the US 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 600 interviews in total. All interviews were conducted exclusively for Atradius.

Survey scope

- **Basic population:** companies from Canada, Mexico and the US 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=600 people were interviewed in total (n=200 people per country). In each country a quota was maintained according to four classes of company size.
- **Interview:** Computer Assisted Web Interviews (CAWI) of approximately 15 minutes duration. Interview period: Q2 2021.

Sample overview – Total interviews = 600

Economy	Interviews	%
USA	200	33,3
Canada	200	33,3
Mexico	200	33,3
TOTAL USMCA	600	100,0

Business sector	Interviews	%
Manufacturing	275	45,8
Wholesale trade/Distribution/Retail	196	32,7
Services	129	21,5
TOTAL USMCA	600	100,0

Business size		
Micro enterprises	51	8,5
SME (Small enterprises)	253	42,2
SME (Medium enterprises)	244	40,7
Large enterprises	52	8,7
TOTAL USMCA	600	100,0

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 the USMCA.
This is part of the July 2021 Payment Practices Barometer of Atradius, available at
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