Insolvencies in Europe

2007/08

A survey by the
Creditreform Economic
Research Unit

Creditreform

CONTENTS **PAGE**

■ 1 Introduction

Any discussion of insolvencies these days quickly focuses on to the subprime crisis and its repercussions for the world economy. When the brick bubble burst, it impacted directly on the development of insolvencies in the USA, as will be outlined later in this survey. But what about Europe? Here, the crisis did not start to make itself felt until early autumn, when it encountered an economy which up to then had been surprisingly robust.

Has the peak already been passed?

In 2007, the European economy, both in the eurozone and throughout the EU, got off to a good start, with quarter-on-quarter growth of 0.7 percent in gross domestic product (GDP). This was due above all to the lively level of investment activity. Then, in the second quarter, GDP growth in real terms declined to 0.3 percent in the eurozone and to 0.5 in the EU as a whole One reason for this quarter-on-quarter fall was that whereas the Q1 result reflected unusually mild winter weather which naturally influenced investment in the construction sector, the less favourable weather conditions in the second quarter slowed the economy down quite considerably. It is also conceivable, though, that the growth cycle had already peaked out in the course of last year and the turbulence in the financial markets simply made things worse.

Nevertheless, the improved situation in the labour market boosted expenditure by private households. Domestic demand in both the eurozone and the wider EU remains the most important growth driver, with private consumption playing an increasingly important role (Eurostat). This reflects the higher numbers of people in gainful employment, not least in Germany. During the summer, the unemployment rate in the EU and in the eurozone fell to under seven percent. With the unemployment rate at levels not seen since the early 1980s, the volume of corporate insolvencies in Europe also continues to shrink.

■ 2 Insolvencies in Western Europe in 2007

2.1 Corporate insolvencies

Although the trend towards lower corporate insolvency figures in the EU-15 states plus Norway and Switzerland which began in 2004 is still in place, the rate of decline is slowing down. Last year, a total of 129,822 companies had to file for insolvency – 6,929 fewer than in 2006. That represents a fall of 5.0 percent, as compared with a reduction of 12.3 percent the year before.

Tab. 1: Corporate insolvencies in Western Europe

■	2007	2006	2005	2004	2003	Change 2006/07 in percent
Austria	6,362	6,854	7,136	6,328	5,643	- 7.2
Belgium	7,690	7,617	7,878	7,836	7,593	+ 1.0
Denmark	2,400	1,987	2,497	2,620	2,506	+ 20.8
Finland	2,300	2,285	2,278	2,385	2,769	+ 0.7
France	42,670	40,360	41,930	40,776	38,296	+ 5.7
Germany	27,490	30,680	36,850	39,270	39,470	- 10.4
Great Britain	12,950	13,686	13,462	12,813	14,815	- 5.4
Greece	510	520	580	577	480	- 1.9
Ireland	310	304	327	321	346	+ 2.0
Italy	5,410	8,827 *)	17,150	17,500	16,000	- 38.7
Luxembourg	680	634	682	665	655	+ 7.3
Netherlands	4,710	5,941	6,780	6,648	6,386	- 20.7
Norway	2,870	3,032	3,540	4,297	5,223	- 5.3
Portugal	3,350	3,400	3,300	3,123	2,980	- 1.5
Spain	830	853	869	561	646	- 2.7
Sweden	4,890	5,243	5,865	6,588	7,099	- 6.7
Switzerland	4,400	4,528	4,751	4,955	4,539	- 2.8
Total	**129,822**	**136,751**	**155,875**	**157,263**	**155,446**	**- 5.0**

*) Since 2006, the insolvency statistics compiled by the register of companies in Italy includes only company headquarters and no longer individual branches.

The biggest fall in business bankruptcies last year was posted by Italy, but this was due to the specifics of the country's statistics. In 2006, the chamber of commerce changed the basis for its figures, no longer registering every branch of a company as a separate insolvency, but only the headquarters. This led to a significant drop in the volume (in 2006 by 48.5 percent and in 2007 by 38.7 percent to 5,410 cases).

Out in front: The Netherlands and Germany

Another country to report a considerably lower level of business failures was the Netherlands, where the number fell by 20.7 percent to 4,710 cases – the lowest level for six years. The decline corresponds to the development of the Dutch economy: following relatively restrained economic growth in the years 2001-2005, GDP has been expanding significantly since 2006. There are three reasons for this. For a start, the Dutch are now consuming more. Estimates talk of up to 2.5 percent more in 2007, with a similar figure expected this year. Secondly, gross investment in plants and machinery has risen substantially, by 7 percent. Thirdly, the economy is being boosted by the volume of exports, whose contribution to GDP is firmly up at a relatively high level.

In third place among the countries with the biggest reductions in corporate insolvencies came Germany, where the figure fell in the course of the year by 10.4 percent to 27,490 cases. The times when the insolvency volume was close to the 40,000 mark (2003), seem to be over. All the same, the rate of downturn has slowed considerably: the decline last year was seven percentage points lower than the almost 17 percent of the year before. The provisional figures for this present year also point to a stagnating level of business bankruptcies. And if the effects of the subprime crisis should make themselves felt more widely – which numerous experts fear – there is a danger that the trend could even be reversed (more on the insolvency situation in Germany in Chapter 5.1).

Although overall the number of business collapses has dropped, the number of countries where the volume has been rising actually doubled last year to six: Denmark, Luxembourg, France, Ireland, Belgium and Finland.

The highest increase was in Denmark, where the figure climbed by over 400 cases – i.e. more than 20 percent – to 2,400. This development is somewhat

Danish ups and downs

surprising because Denmark is one of the European leaders in terms of the key economic indicators. However, its previously buoyant economy is gradually flattening out, with the growth forecast cut from 3.3 to 2 percent. The unemployment rate has fallen to 3.1 percent (or 3.5 percent according to EU calculations), corresponding to de facto full employment and resulting in a lack of labour in some business sectors, particularly the construction industry. This has been offset, though, by an influx of foreign workers, especially from Germany and Poland. Despite fears to the contrary, inflation has not materialized – the anticipated rise in prices in 2007 was 1.7 percent. The economic boom has been fuelled mainly by revenues from oil exports, while private consumption, financed chiefly by housing mortgages, has been declining in line with the fall in property prices. However, the significance of the high growth of corporate bankruptcies should not be overestimated: Denmark's insolvency statistics are among the most volatile in Europe – just the year before the country had posted the biggest decline (of 20.4 percent to just under 2,000 bankrupt companies).

The country with the second-largest increase in insolvencies was Luxembourg. However, the number increased only by a moderate 7.3 percent to 680 affected companies, after 634 cases in 2006. Last year, Luxembourg's economy expanded by 5.5 percent, while as of October 2007, the inflation rate was 2.9 percent and the unemployment rate was 4.3 percent. Luxembourg remains one of the countries with the highest per capita income in the world, and for neighbouring regions it is an important employer, with around 134,000 people commuting there to work every day.

Another country where corporate insolvency figures climbed was France. It is traditionally the country with the highest number of insolvencies in Europe (only in 2003 was it ousted from that position by Germany). Last year, business collapses in France totalled 42,670, representing an increase of 5.7 percent. Globalization has subjected French industry to an intensified process of structural transformation. To maintain and even perhaps improve its international competitiveness, France needs a broader business sector base and must significantly strengthen its small and medium-sized enterprises (SMEs) as the backbone of the economy. The country's big companies, listed in the CAC 40 index, have been diversifying very successfully on a global scale and increasingly moving their operations to countries with higher growth rates. SMEs are not generating sufficient numbers of the new people that France needs and they are also being forced to outsource work abroad because of labour costs and the pressure to remain competitive. At present, the tertiary sector is unable to fully offset the job losses which these factors create (for more information on France, see also Chapter 5.3).

35-hour week slows growth

Tab. 2: Insolvency ratios in the individual Western European countries

■	**Insolvencies per 10,000 companies**
Spain	3
Greece	7
Italy	13
Portugal	27
Ireland	31
Great Britain	82
Netherlands	87
Germany	90
Norway	90
Sweden	92
Switzerland	93
Finland	95
Belgium	110
Denmark	131
France	166
Austria	240
Luxembourg	256
Average	**67**

Mediterranean countries keep average down

The highest relative incidence of insolvency (number of insolvencies per country in relation to the total number of businesses in that country) was once again posted by Luxembourg (256), followed by Austria (240) and France (166). However, the general picture is distorted by the fact that the insolvency statistics in Spain, Greece and now also Italy are not strictly comparable to those of other countries. Another factor is that the hosts of micro-firms there push the average ratio down. Over all of the countries surveyed, the average is 67 insolvencies for every 10,000 companies. With a ratio of 90, Germany lies above the average but that puts it in good company with the most flourishing European economies: Norway, the Netherlands and Sweden.

2.2 Private insolvencies in Europe

While corporate insolvencies continue to decline, the volume of private insolvencies moved in the opposite direction. Since 2004, when we first started covering this field, the number of debt clearance proceedings has been on the increase. However, the rate of growth has been slowing down, which in a way is a parallel to the development of business bankruptcies. Whereas in 2006, the increase was 31.9 percent, it fell in 2007 to 8.3 percent. This is due to a large extent to two countries, Germany and Great Britain. In 2006, consumer insolvencies in Germany grew by almost 25 percent, while last year the figure was 12.3 percent. In Great Britain, the development is even more striking: last year, the volume of private insolvencies increased by just 2.3 percent, as against a rise of more than 50 percent the year before.

New debt clearance procedure in Sweden

In Sweden, on the other hand, there was a truly explosive rise in private bankruptcy applications – these rose by 85.9 percent last year to 7,120. One reason for this was that on January 1, 2007, Sweden introduced a new debt clearance procedure. This was intended to do something about the high proportion of applications which up to then had been rejected (18,000 rejections out of 29,000 applications between 1994 and 2001) and also to streamline the legal proceedings. The figures indicate that that has been successful: whereas in 2006, just 3,830 applications for residual debt relief were made, the figure last year was 7,120. A further increase can be expected.

Tab. 3: Private insolvencies in Europe

■	2007	2006	2005	Change 2006/07 in percent
Austria	8,616	7,583	6,462	+ 13.6
Germany	139,510	124,180	99,720	+ 12.3
Great Britain	123,700	120,926	79,426	+ 2.3
Netherlands	15,060	14,928	14,666	+ 0.9
Sweden	7,120	3,830	4,178	+ 85.9
Switzerland	6,300	5,840	5,714	+ 7.9
Total	**300,306**	**277,287**	**210,166**	**+ 8.3**

Advisory services for debtors are financed in different ways in different countries. In the UK, for instance, the credit sector itself has, for some years, been contributing to the funding of an independent advisory service. Moreover, the British government has set up a Financial Inclusion Fund to finance advisory services above all in those regions where broad sections of the population are affected by over-indebtedness and subsequent exclusion from the credit market. Since such regions also exist in Germany – Creditreform encountered this phenomenon during the preparation of its Debtors Atlas – the British initiative is also of interest here. In 2006 and 2007, the Financial Inclusion Fund was furnished with a total of 45 million pounds. Britain, which for over 15 years has been committed to improving financial education, is now undertaking further efforts. The “Task Force: Tackling over-indebtedness” established by the government has commissioned a new national programme from the Financial Services Authority. This will include an evaluation of previous measures in this field and new surveys aimed at providing a more reliable picture of basic financial knowledge among the general public. On the basis of this, new educational concepts are to be developed and made an obligatory part of schooling.

Varied moves to increase financial awareness

The relative incidence of private insolvencies is obtained by comparing the number of consumer bankruptcies in each country with the size of the population. The highest incidence is still in Great Britain, with 21 cases for every 10,000 individuals. In Sweden – despite last year's massive relative increase – the figure is only eight insolvencies for every 10,000 inhabitants.

Tab. 4: Private insolvency ratios in the individual Western European countries

■	Insolvencies per 10,000 private individuals
Sweden	8
Switzerland	8
Netherlands	9
Austria	11
Germany	17
Great Britain	21
Total	**16**

Fresh start vs. earned fresh start

In the USA, even after the reform of 2005, insolvency legislation is still relatively lax. However, this is the case in all countries governed by Common Law, whereas in continental Europe, the relevant laws tend to be derived from the principles of social justice and a welfare state. This results in two different philosophies: whereas the Anglo-American countries adhere to the idea of a fresh start, the governing notion in continental Europe is of an "earned fresh start". In the USA, the focus is on quickly re-integrating over-indebted individuals into the market; in continental Europe, consumers are not released so easily from their obligations to pay off their debts – they first have to earn this privilege. Unlike in Europe, over-indebtedness in the USA is regarded not as a moral failure but as a natural feature of a market economy. As a consequence, American banks, as the "cheapest cost avoider", are expected to price in the costs of defaults when they grant credit; in other words, those who service their loans are paying for those who slip into insolvency. However, even after debt clearance, American consumers cannot simply return to the primary credit market. One result of this is the establishment of a so-called secondary credit market, which is largely unregulated and provides loans to debt-cleared consumers on far less favourable terms.

2.3 The subprime crisis and insolvencies in the USA

It is impossible to examine the development of insolvencies in the USA without studying the mortgage crisis and its repercussions.

Brick bubble: Causes and effects

For two years or so, experts such as the American economist Robert Shiller have been warning about the possibility of the speculation bubble in the American property market bursting. The background is that since the mid-90s, housing prices in the USA have been increasing rapidly. At the same time, banks were making generous offers of mortgages, which tempted tens of thousands of Americans who could not really afford to finance their own homes – the “subprime borrowers”. Unlike for example in Germany, mortgage rates in the USA are generally variable – and in spring 2007, the rates went up. As a result, many Americans were no longer able to pay off their mortgage debts and had to sell their homes. This sent house prices tumbling. The brick bubble had finally burst. Consumer insolvencies soared.

Tab. 5: Insolvencies in the USA

■	2007	2006	Change in %
Total	820,340	617,660	+ 32.8
Companies	18,500	19,695	- 6.1
Private individuals	801,840	597,965	+ 34.1

Within just twelve months, the number of private bankruptcies in the USA increased by all of 34.1 percent to over 800,000. Samuel J. Gerdano, chief of the American Bankruptcy Institutes, expects to see this trend intensify in 2008. Up to now, the insolvency peak in the USA was in 2005, when over 2 million private individual and almost 40,000 firms went broke. In October of that year, insolvency legislation was tightened up by the passing of the Bankruptcy Abuse Prevention & Consumer Protection Act. The announcement of the upcoming change initiated a real flood of last-minute applications for bankruptcy; the following year saw the figure decline significantly.

The renewed growth of consumer insolvencies in the USA has not been the only consequence of the subprime crisis. Mortgage banks had securitized their claims and sold the packages to international banks, hedge funds and other investors. Since then, though, these securities have fallen dramatically in value, rating agencies have down-classed them and they have become impossible to sell. This inflicted severe wounds in particular on Citigroup, Merrill Lynch and Morgan Stanley. Then, in September, the subprime crisis started to impact on Europe. The worst affected was the British mortgage bank Northern Rock; long queues of customers desperate to retrieve their deposits formed in front of its branch offices. In Germany, the crisis "revealed the weakness of the public-sector banks", as Catherine Hoffman put it in the newspaper FAZ am Sonntag. The background to this: Since 2005, the state authorities no longer bear liability for the debts of the regional public banks, the Landesbanken. This reduced their scope for granting credit and so they speculated with derivatives on an off-balance-sheet basis; up to the crisis they had earned well from this.

Egg Bank and Citigroup

Citigroup recently hit the headlines again when its Internet banking subsidiary Egg Bank announced a decision to withdraw 160,000 credit cards from customers. A spokesman said that this was not due to the credit crisis but followed a re-assessment of the credit risks involved: the cards had been withdrawn from customers who on closer examination represented an "unacceptable risk profile" – a startling seven percent of Egg's 2 million customers. However, the accusation was voiced that Egg was simply withdrawing credit cards from customers who didn't earn it any money. Citibank's most recent quarterly report posted a loss of almost 10 billion dollars.

The turbulence in the financial markets and the resultant acute liquidity problems of banks in Germany and elsewhere has led to a loss of confidence in the banking system and to increased caution in the field of risk management. The most recent surveys among banks on both sides of the Atlantic show that firms with a lower credit rating are now finding it more difficult and also more expensive to borrow money. Creditreform has established that as a result of the financial crisis and the greater risks, banks are more reticent to grant credit to business customers or consumers. This is not a panic reaction, but is connected above all to the stricter equity stipulations of Basel II. A business company's credit rating is determined to a decisive extent by its equity ratio. In Germany, despite the economic upturn, equity ratio figures have improved only slightly and even today, close to a third of all SMEs are undercapitalized (meaning less than 10 percent equity as a ratio of the balance sheet total). Since recent experience shows a lower incidence of insolvency in periods when liquidity was easier to obtain, there are now fears that the trend towards declining insolvency totals could be reversed both in Germany and the rest of Europe as well as in the USA and that 2008 could bring more bankruptcies than before.

Upturn fails to produce significant equity ratio improvement

And this might not be the only negative effect. Banks are already registering massive defaults in the field of consumer loans, says Deutsche Bank chief Josef Ackermann. He believes that this will impact on the private customer business of financial institutions. That in turn could dampen consumer demand and thus slow down the economy overall.

Excursus: European efforts to upgrade the image of insolvency

Regarding insolvency as an opportunity

In America, financial failure is not regarded as some personal stigma. The insolvency legislation there makes it easier for bankrupts to get off to a fresh start again afterwards. This is one reason for the high number of start-ups in the USA. Now there are also efforts in the European Union to free insolvency of its exclusively negative connotations. According to the European Commission, one in every three of the member states is planning legislative amendments on the basis of the reform programs initiated in connection with the Lisbon strategy for more growth and employment. All the amendments are aimed at simplifying bankruptcy laws, offering a greater range of solutions in cases of

Support for restarters

actual or imminent insolvency, making it easier for companies to restructure, and supporting business people when they start out again. France, for instance, is already operating a system whereby companies on the verge of insolvency can obtain advice from three bankruptcy legislation experts and via a specialized website. In the Netherlands, there is an organisation of retired business people ready to provide free support to SMEs which are in difficulties. In the UK, a reform of the insolvency laws helps companies which have slipped into insolvency through no fault of their own; it reduces the number of reasons which prohibit an individual from managing a business company and it also shortens the repayment periods for outstanding debts. Germany has drawn up a directive for potential restarters and in Northrhine-Westphalia, a network has been created for those affected and a restart bonus has been introduced.

3 SMEs and financing

In the European Union, small firms with fewer than 10 employees predominate – they account for 92 percent of all business companies in the EU, according to a recent European Commission survey. The average European company employs seven people, but there are differences between the member countries, due to various structural, institutional and historical conditions. In Greece, for instance, SMEs employ an average of just two people, in Italy the figure is four, in Spain six, in the Netherlands twelve and in Germany ten. In Europe as a whole, people employed in SMEs account for 66 percent of the total workforce; in the USA the figure is 33 percent. One reason for this marked difference is that many micro-enterprises in the USA are sole traders; another is that the lively fluctuation of business start-ups and closures in the USA means that there are always many firms in the start-up phase, with a correspondingly smaller size.

Small companies finance their operations differently from large companies. After all, particularly in the early years, they have no access to the financial market. KPMG recently surveyed how firms throughout Europe regard the importance of various forms of financing for their future growth. Over two-thirds of the companies questioned considered equity financing and cashflow as their most significant forms of financing. In some countries, the proportion of firms taking this view is even higher: Greece (95 percent), Sweden (88 percent), Hungary (83 percent) and Denmark (78 percent). One firm in every two considers financing growth via the bank important (in Germany the figure is 52 percent). This study, like others before it, comes to the conclusion that a vital factor in ensuring greater SME stability is increasing the equity capital. A higher equity ratio means fewer financing problems and earns a firm a better rating. This in turn makes it easier to obtain third-party capital.

Equity ratios develop in different ways

Tab. 6: Equity ratios of SMEs in Germany

■	up to 10%	32.9 (29.3)
	up to 20%	24.8 (30.3)
	up to 30%	18.7 (18.4)
	over 30%	23.5 (22.1)

In percent of respondents, rest unspecified, ( ) = prior-year figures

The table above shows equity ratios in Germany in autumn 2007 in comparison with the prior year. Some companies had taken advantage of the economic upturn to retain their profits and build up their own capital resources (23.5 percent; prior year: 22.1 percent). On the other hand, the number of undercapitalized firms had increased by 3.6 percentage points to 32.9 percent.

One million SMEs have difficulties in obtaining finance

It is above all small companies which anyway have only limited equity capital of their own which are affected by the credit squeeze. Our own surveys show that at present around one million companies in Germany with an equity ratio of under 10 percent find it difficult to service their loans or sometimes even to obtain credit in the first place. So in respect of their scope for financing, one firm in every three in Germany is feeling the effects of the credit crisis.

The wide-spread belief that small companies are earning good profits thanks the brighter economic climate is not correct. In many cases, the financial crisis is intensifying an anyway tight earnings situation. Despite full order books, such firms are often not in a position to form reserves and build up their own capital. The best advice for firms of this kind is to extend their financing spectrum. Instead of tapping only such traditional forms of financing as bank loans, cashflow, leasing and supplier credits, they should be taking a closer look at raising mezzanine capital, i.e. a mixed form of financing between equity and third-party capital.

Tab. 7: Payment conduct in Europe in days

■	Payment terms	Payment delay	Total
Italy	66 (67)	23 (23)	89 (90)
France	43 (43)	14 (12)	57 (55)
Great Britain	35 (34)	19 (18)	54 (52)
Belgium	33 (34)	13 (13)	46 (47)
Austria	30 (29)	11 (10)	41 (39)
Switzerland	23 (24)	16 (16)	39 (40)
Netherlands	24 (25)	15 (14)	39 (39)
Germany	25 (25)	12(14)	37 (39)
Sweden	28 (28)	8 (9)	36 (37)

( ) = 2006

A company's strength depends not just on its equity ratio but also on the extent of its receivables. The longer a firm has to wait for its invoices to be paid, the greater the risk of illiquidity. The longest wait is in Italy, where it takes an average of just under three months for bills to be paid. As always, the payment conduct in the Scandinavian countries is very good, with Sweden in particular setting a fine example for others. Swedish firms pay for services or products after 36 days on average (prior year: 37 days) – that is the best figure in Europe. But in Germany, too – despite all statements to the contrary – bills are paid relatively punctually, within 37 days (prior year: 39 days).

Excursus: Micro-loans

Every year, around 2 million companies are set up. Over 90 percent of these are micro-firms with fewer than 5 employees. In the EU, some 30 percent of all start-ups survive no more than 3 years, around 50 percent no more than 5 years. According to a study by the European Commission, insolvency rates are lower in those member states where young business people can obtain high-quality support in the period prior to and just after the start-up. This includes making it easier for them to gain access to funding. In some cases, already existing small companies receive the same kind of support.

50 percent of company founders require less than € 25,000 start-up capital

Just under half of all start-ups have a financing requirement of less than 25,000 euros, but only around half of these can cover this from their own resources (for example "love money" from their families or by taking up personal loans). For the others, one new form of financing takes the form of so-called micro-loans (micro-credits). Micro-loans are distinguished not just by their small scale and short repayment periods but also by what is called "stepping", that is the granting of credit gradually in line with the progress being made. The EU Commission says that in all the old EU member states and most of the new ones, public-sector funding in different forms is available for this to offset the reticence of banks to grant loans to small firms.

In the United Kingdom, for example, there is the "The Prince's Scottish Youth Business Trust", which provides support for underprivileged or unemployed 18 to 25-year olds by granting micro-loans of up to ₤ 5,000 and providing mentors to advise young people during their first two years in business. Training in bookkeeping is available; company founders have access to a free bookkeeping system, they receive support for PR measures and are networked with other young entrepreneurs.

Best practice

In Finland, the state business development bank Finnvera grants direct loans "to promote and develop en trepreneurship in Finland, exports and internationalization". Business development measures include giving help to start-ups or expansion projects to acquire plant and machinery.

France has its "Association pour le droit à l'initiative Economique" (ADIE), which comprises 22 regional branches and 300 standby services, in operation particularly in areas with a substantial number of underprivileged individuals. ADIE staff offer local inhabitants interested in setting up a business a range of financing instruments and intensive advisory and support services, for instance in applying for and obtaining loans. ADIE is mandated to borrow money from banks and provide funds for small businesses. According to its own figures, in the last nine years ADIE has created 19,000 jobs. After two years, the survival rate of firms supported in this was 64 percent, on a par with the French average for start-ups.

■ 4 The sectoral distribution of insolvencies

According to initial estimates by Eurostat, GDP growth in the eurozone in the third quarter of 2007 was 0.7 percent in real terms. This means that economic growth has slowed down somewhat not just in industry, but also in the services sector. On the whole, though, economic fundamentals in the eurozone last year were solid, with robust growth in the number of new jobs and an unemployment rate lower than at any time in the last 25 years. Insolvency-related jobs losses in Europe also declined significantly, from 1.4 to 1.2 million; however, that does not match the best result achieved in recent times, in 2000, when "only" 1.1 million employees lost their jobs as a result of their firm going broke.

Bankruptcies cause 1.2 million job losses

Tab. 8: Insolvency-related job losses in Europe

■	Job losses (in millions)
1999	1.4
2000	1.1
2001	1.4
2002	1.6
2003	1.7
2004	1.6
2005	1.5
2006	1.4
2007	1.2

The biggest contribution to the insolvency volume came from the services sector, the largest of the four main branches of the economy. It was responsible for more than one third of all insolvencies (37.0 percent; prior year: 35.3 percent). The most significant relative fall was posted by the construction industry (20.9 percent; prior year: 22.2). The smallest contribution was made by manufacturing. Its share, of just 8.6 percent, also represents a decline compared with 2006 (9.1 percent) and 2005 (10.5 percent).

Tab. 9: Contribution to the insolvency volume by the key economic sectors in Europe in 2007 (average)

■	Contribution to insolvency
Manufacturing	8.6 (9.1)
Construction	20.9 (22.2)
Commerce	33.5 (33.4)
Services	37.0 (35.3)

Figures in percent, ( ) = 2006

Commerce and services with higher shares of insolvency total

Unlike Germany, most European countries include hotels, restaurants and cafés – “horeca” – in the insolvency figures for commerce (wholesale/retail) rather than for services, so we have done the same in order to provide easier comparability. One notable development was that in the Netherlands: the year before, over half of all business bankruptcies were in the services sector, while last year the figure declined to just one in every three (36.6 percent; prior year: 55.3 per cent). The other three main economic sectors posted significant increases.

Tab. 10: Insolvencies in the key economic sectors in 2007

■	Manu-facturing	Construc-tion	Com-merce *)	Services
Belgium	4.2 (6.7)	14.9 (13.4)	51.8 (53.1)	29.1 (26.7)
Denmark	6.7 (5.8)	13.0 (12.9)	38.2 (45.6)	42.0 (35.7)
France	7.7 (9.1)	28.7 (24.0)	28.4 (33.4)	35.2 (33.5)
Germany	10.5 (11.0)	18.1 (19.3)	31.9 (30.1)	39.4 (39.6)
Great Britain	8.9 (7.6)	14.4 (27.6)	22.2 (29.6)	54.5 (35.2)
Netherlands	11.6 (6.9)	15.4 (10.8)	36.4 (27.0)	36.6 (55.3)
Norway	5.9 (6.1)	22.7 (21.7)	28.3 (39.5)	43.1 (32.7)

*) including hotels, restaurants and cafés, figures in percent, ( ) = 2006

In all the countries surveyed, the lowest contribution to the insolvency volume is made by manufacturing. But the figures vary, from 10.5 percent in exports world champions Germany (prior year: 11.0 percent) and just 4.2 percent in Belgium (prior year: 6.7 percent).

Denmark's construction industry booming

In France, 28.7 percent of all business bankruptcies are in the field of construction (prior year: 24.0 percent), whereas the relevant figure for Denmark is just 13.0 percent (prior year: 12.9 percent). One reason for this is that in the period 2003 to 2007, Denmark's construction industry registered growth of around 22 percent. New planning legislation there, which permits the building of larger retail properties in cities (an increase of 500 sqm to 3,500 sqm for retailers serving daily needs and to 2,000 sqm for power stores), has helped to boost construction activity. According to an estimate by the Construction Federation, industrial construction in 2008 is likely to remain at the prior-year level of 0.70 million sqm, but, just as in 2007, considerable investment can be anticipated in the field of large, fully-automated logistics centres. Public-sector investment in office premises, cultural and leisure facilities and hospitals last year rose by over 30 percent. This followed the administrative reform of January 1, 2007, regarding the erection/modernization of office buildings for new regions and municipalities.

Commerce (retail/wholesale) accounts for a large proportion of insolvencies above all in Belgium, where the figure is 51.8 percent. This was, though 1.3 percentage points down on the prior year. In the UK, on the other hand, insolvencies in this sector play a relatively subordinate role, accounting for just 22.2 percent of the total volume, which was 7.4 percentage points less than the year before. The largest proportion of corporate bankruptcies in the UK came in the services sector, where the figure was 54.5 percent (up from 35.2 percent the previous year). In Belgium, services account for fewer than one in three business bankruptcies (29.1 percent).

■ 5 National reports
5.1 Germany

The number of corporate insolvencies in Germany fell in 2007 by 10.4 percent to 27,490 cases. This means that the downward trend is slowing: the prior year, the volume had fallen by 16.7 percent. Consumer insolvencies, on the other hand, passed the 100,000 threshold for the first time to total 109,330 cases, a year-on-year increase of 18.3 percent. The year before, though, the increase, at 34.2 percent, had been even greater. Other bankruptcies in 2007 – insolvent estates and personally liable partners – totalled 30,180 cases, representing a slight decline of 4.9 percent. This means that for 2007 as a whole, the number of insolvencies was 167,009 – 12,140 more than in 2006, a rise of 7.8 percent.

Corporate insolvencies 2008: Decline slowing down

Tab. 11: Insolvencies in Germany

■	2007	2006	Change. in %
Total	167,000	154,860	+ 7.8
Companies	27,490	30,680	- 10.4
Private individuals	139,510	124,180	+ 12.3

In the Western part of Germany, the decline in business bankruptcies slowed down to just 8.1 percent, to give a total of 21,530. In Eastern Germany, on the other hand, the decline was almost twice as high, at 17.7 percent. In that part of the country, a total of

5,960 businesses had to make their way to the insolvency courts.

In Western Germany, consumer insolvencies increased by 17.0 percent to 81,540 affected individuals; in Eastern Germany there was a rise of 22.3 percent to 27,790. Overall, 124,490 applications for bankruptcy were filed in West Germany, corresponding to a year-on-year increase of 7.5 percent. In Eastern Germany the figure rose by 8.9 percent to a total of 42,510.

Contstruction still a cause for concern

The biggest decline in the field of insolvencies was achieved by the construction industry, where the figure fell by 15.9 percent to a total of around 5,000 affected companies. But since there were significant falls in the insolvency volume in all the other main branches of the economy, construction still has the biggest relative incidence: of 10,000 companies, an average of 154 went broke in 2007. The figure for manufacturing, at 77, was just half of that.

The damage caused to the economy by insolvent companies in 2007 totalled 29.2 billion euros, down on the 31.1 billion euros of the year before. There was a decline in the number of insolvency-related job losses: whereas in 2006 the figure was 473,000, last year it was 440,000.

5.2 Great Britain

In 2008, British industry expects to see a marked reduction in economic growth in 2008. The 2007 growth estimate has been lowered to 2.0 percent, after an initially anticipated 3.0 percent, said the CBI, the Confederation of British Industry, which cited the impact of the global credit market crisis in combination with higher prices for raw materials as the reason for this. But the increases in the base interest rate, the weakening property market, higher energy prices and a pound which was for a long time stable in terms of the euro have also had an effect. So the decline in the growth of private consumption and investment was hardly surprising. Financial and B2B services have been developing at a less dynamic rate than before, and this cannot be offset by the UK's strong construction trade or the small and relatively stagnant industrial manufacturing sector. 2008 is likely to be a somewhat more difficult year for the UK where imports are concerned, while exports will be boosted somewhat by the now weaker level of the pound sterling.

Tab. 12: Insolvencies in Great Britain

■	2007	2006	Change in %
Total	136,650	134,612	+ 1.5
Companies	12,950	13,686	- 5.4
Private individuals	123,700	120,926	+ 2.3

Crisis leaves UK unscathed so far

In the course of 2007, the volume of business insolvencies fell by 5.4 percent to just under 13,000 affected companies. That is the lowest figure in the past five years. This indicates that the subprime crisis did not have any direct impact on the number of corporate bankruptcies in the UK – whether this will also be the case in 2008 remains to be seen.

In all, insolvencies in Great Britain totalled 136,650, which is almost 30,000 fewer cases than in Germany.

5.3 France

The French government has dampened the expectations for economic growth. In mid-January 2008, economics minister Christine Lagarde said that growth this year is likely to be at the lower end of the previously named range of 2.0 to 2.5 percent. This was due, she went on, to the deteriorating international environment. "The endogenous factors in France are solid", she emphasized. Her remarks are the clearest signs so far that the French government does not expect any significant invigoration of the economy in the foreseeable future. President Nicolas Sarkozy has said that everything is in place to reduce the budget deficit, but he has yet to say when this objective could be achieved. The anticipated deficit for 2007 was 2.4 percent and the figure this year is due to fall to 2.3 percent.

French industry is losing its competitiveness. This does not apply to the small elite of generally well managed large companies listed in the CAC-40 index, but to the general mass of other firms. SMEs are not exporting enough and are also seeing their market shares at home declining. The constantly growing foreign trade deficit, which can no longer be explained just by high oil prices or the strong euro is evidence of the need for action. Business companies need relief in respect of social security contributions, taxation and red tape. But the pre-election announcement that the level of corporate taxation would be lowered has not been followed up. The scale of trade tax also remains a millstone. Expenditure by the welfare authorities is not covered by revenues, while Sarkozy's tax incentives for private households have placed a severe burden on the anyway deficit-ridden national budget.

Tab. 13: Corporate insolvencies in France

■	2007	2006	Change in %
	42,670	40,360	+ 5.7

Another factor is that despite international competitors such as China and India, which do not limit working hours or have minimum wages, France allows itself the luxury of prescribing long periods off work for its working population. The tight legislative restrictions on weekly hours represent one of the biggest fundamental problems facing the economy. From the 36th hour onwards, business firms must pay overtime of 25 percent. President Sarkozy has in fact now increased the overtime rate for companies with up to 20 employees, from 10 to 25 percent. The simultaneous reduction in the level of social security contributions was not sufficient to offset this.

France bucks trend

Consequently, France was last year one of the few countries in Europe to generate a higher number of corporate insolvencies, with a rise of 5.7 percent to 42,670 affected companies. France has always had a large bedrock of business bankruptcies, but the 2008 volume represented a reversal of the prior-year decline.

■ 6 EU Eastward expansion: New member states

The new members of the EU in Central and Eastern Europe are benefiting strongly from their admission to the community in May 2004. “Economically, they are today in a far better position than they were prior to joining the EU”, says Sandor Richter of the Vienna Institute for International Economic Studies (WIIW). He points out that since 2004, the economies of these countries have grown by an annual rate of 5.3 percent since 2004, compared with just 3.1 percent in the years before admission.

In these new member states, just as in “old Europe”, the volume of corporate insolvencies is on the decline. In 2006, the total was over 20,000 cases; last year this fell slightly – by 1.2 percent – to 19,857. However, such figures remain difficult to compare with those in Western Europe. This is evidenced most clearly by the insolvency statistics for Poland. These are unbelievably low and continue to fall every year. In 2007, just 447 Polish firms filed for bankruptcy. That was 22.4 percent down on the 576 on the year before – and the total is only half that in far smaller Lithuania.

3.5 million firms but only 447 insolvencies

Tab. 14: Corporate insolvencies in Eastern Europe

■	2007	2006	2005	Change 2006/07 in percent
Czech Republic	4,250	4,227	3,882	+ 0.5
Estonia	234	228	265	+ 2.6
Hungary	9,500	9,447	7,983	+ 0.6
Latvia	1,272	1,174	830	+ 8.3
Lithuania	814	808	773	+ 0.7
Poland	447	576	793	- 22.4
Slovakia	2,100	2,150	2,200	- 2.3
Slovenia	1,240	1,246	1,383	- 0.5
Total	**19,857**	**20,089**	**18,294**	**- 1.2**

With effect from January 1, 2008, the Czech Republic has introduced a new insolvency law. Among other things, it obliges law courts to publicize any applications for the opening of insolvency proceedings. In addition, the country has established a public register of insolvencies. This should make it easier to verify the country's insolvency statistics. Another new move was the introduction of restructuring proceedings for business companies. However, this applies only to companies with more than 100 employees or turnover of over 100 million Czech crowns (3.9 million euros). To enable a smaller firm to seek restructuring, at least half of all the creditors have to agree.

The Czech Republic has also introduced a debt clearance procedure for consumers, which is similar to that in Germany. The good conduct period, however, was set at five years.

The Czech economy is booming. For 2007, the National Bank expected GDP growth of 5.5 percent. The key driver for this is domestic demand. Higher wages and salaries have evidently inspired many Czech citizens to go on a spending spree. And the banks are helping by being increasingly ready to grant private loans.

Tab. 15: Insolvency ratios in individual Eastern European countries

■	Insolvencies per 10,000 companies
Poland	1
Czech Republic	47
Estonia	69
Slovakia	75
Lithuania	128
Slovenia	135
Hungary	165
Latvia	252
Total	**36**

The figure for Poland of just one insolvency for every 10,000 active companies naturally lacks credibility and is even lower than the figure reported by Spain. The average incidence of insolvency in the new member states was 36 for every 10,000 companies. The result in Latvia, which together with the two other Baltic states generally counts as a showpiece economy, was well above this average, at 252. The problem is that Latvia in particular, but also Estonia and Lithuania, face the threat of overheating. The rating agency Standard & Poor's sees Latvia as being in danger of making a "hard landing" and has set the country's rating outlook at "negative". Latvia has the highest level of economic growth in the EU, but this is fuelled quite substantially by mortgage loans. The square metre prices for residential properties in Riga are now higher than in Vienna or Frankfurt.

Overheating in the Baltic states?

7 Japan

In Japan, corporate insolvencies fell between 2005 and 2006, but last year they rose again quite significantly, by 38.9 percent to just under 11,000.

Tab. 16: Corporate insolvencies in Japan

■	2007	2006	Change in %
	10,980	7,905	+ 38.9

One major burden for the future of Japan and a direct consequence of state economic growth programmes in the 90s is the extremely high level of public indebtedness. At the end of June 2007, state indebtedness totalled 836.52 billion JPY – which is more than 1.5 times Japan's annual GDP.

For a long time, Japan went through a period of deflation or, at best, price stability, but now things look like going in the opposite direction. Recently there have been perceptible increases in prices for food and fuel and this is likely to lead to moderately higher prices in other fields as well. A role in this is played by the relatively weak level of the yen.

The country's monetary policy is still distinguished by an exceptionally low interest rate. On February 21, 2007, the base rate was lifted to 0.5 percent and has remained at this level since then. Although the Bank of Japan favours a return to normality in the field of monetary policy, uncertainties about the development of the US economy and worries that domestic dynamism could wane are currently making the bank steer clear of any rise in interest rates.

The rapid ascent of China, but also of other threshold countries in the region, is taken more seriously in Japan than elsewhere, for understandable geographical reasons. China plays an important role for Japan in particular as a production platform for Japanese firms. But at the same time, China's inadequate efforts to protect intellectual property and the country's worsening cost structures have helped to shape the Japanese view that the first major Chinese boom is already over.

■ 8 Summary

In 2007, the number of corporate insolvencies in the EU-15 states plus Norway and Switzerland, which has been falling for the past three years, dropped to 129,800 cases; the year before, the figure was 6,930 higher. This corresponds to a decline of 5.0 percentage points. On the other hand, though, the number of countries now again posting higher insolvency levels doubled last year to six. The biggest rise, of 20.8 percent to 2,400 cases, was registered in Denmark. Then came Luxembourg with an increase of 7.3 percent to 680 (prior year: 634) and France with growth of 5.7 percent to 42,700 bankruptcies (prior year: 40,400).

The biggest drop in insolvency totals was posted by Italy. However, this was due not so much to any significant improvement in the economic situation, but rather to the fact that the commercial register has changed the basis for its statistics. So Italy's handsome reduction of 38.7 percent (to 5,410 affected firms) should not be overrated. Another country with a significant fall in the number of insolvencies was the Netherlands, where the figure fell by 20.7 percent to 4,710 – the lowest level for six years. In third place in this respect was Germany, where corporate insolvencies declined by 10.4 percent to 27,500, as against 30,700 in 2006.

The highest relative incidence of insolvency (number of insolvencies compared with a country's total number of companies) was once again to be found in Luxembourg, with a ratio of 256 insolvencies for every 10,000 active business companies. It was followed by Austria (240) and France (166). The three Mediterranean countries of Spain (3 insolvencies for every 10,000 companies), Greece (7) and Italy (13) lead the table, but this is due more to specific statistical factors than anything else. Over all the countries surveyed, the average insolvency ratio is 67 per 10,000 companies. With a figure of 90, Germany finishes well above this average level, but is nonetheless in good company: Europe's top economic performers exhibit similar levels: Norway (90), Sweden (92) and Switzerland (93).

Contrary to the development in the field of business insolvencies, private bankruptcies continued to climb in the countries surveyed – Germany, Great Britain, the Netherlands, Austria, Sweden and Switzerland. In 2007, a total of 300,300 private individuals applied for bankruptcy (prior year: 277,300). That represents a rise of 8.3 percent. The biggest increase was in Sweden, where the total grew by a massive 85.9 percent to 7,120 cases. The main reason for this was the new insolvency law introduced at the beginning of 2007. Under the previous law, too many applications for bankruptcy had been turned down. In Germany, private insolvencies rose by 12.3 percent to 139,500.

A comparison of the number of consumer insolvencies with the number of inhabitants of any specific country shows the relative incidence of private bankruptcies. In the UK, the figure last year was 21 for every 10,000 inhabitants, whereas in Sweden, despite the huge relative increase in the total, it was just 8.

In the USA, the subprime crisis impacted directly on the volume of insolvencies among private individuals, which rose by 34.1 percent to 801,800. Experts expect this trend to continue in 2008. On the other hand, corporate insolvencies in the USA fell in 2007, by 6.1 percent to 18,500.

In line with the decline in corporate insolvencies in Europe, the number of insolvency-related job losses also fell. The figure for the year as a whole was 1.2 million, as against 1.4 million in 2006.

In Europe, it is the services sector which accounts for the largest proportion of the insolvency total: on average 37.0 percent of all insolvencies were in this branch of the economy (prior year: 35.3 percent). The most marked reduction in this respect was the proportion contributed by the construction sector, whose share fell from 22.2 percent in 2006 to 20.9 percent in 2007. The lowest contribution to the total volume comes from manufacturing. with just 8.6 percent of the total (prior year: 9.1 percent). The fourth main economic sector, commerce (wholesale/retail), last year accounted for 33.5 percent of the total volume (prior year: 33.4 percent).

However, a closer look at the distribution of insolvencies between the various sectors of the economy in individual countries reveals considerable differences. Manufacturing, for instance, is the smallest contributor in all the countries surveyed, but its share varies between 11.6 percent in the Netherlands and just 4.2 percent in Belgium. In France, 28.7 percent of all insolvencies are in the construction industry, which in Denmark accounts for just 13.0 percent of the total.

Last year, the volume of insolvencies also fell in the new member countries of the European Union – Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia and Slovenia. In the course of 2007, the total declined to 19,900, representing a year-on-year reduction of 1.2 percent. However, overall results from Central and Eastern Europe must be viewed with caution; the economic and judicial prerequisites there are not yet on the same level as in most of the Western European countries and this makes figures difficult to compare. This is particularly apparent in Poland, where according to official statistics there were only 447 corporate bankruptcies last year (prior year: 576). However, since there are more than 3.5 million business enterprises in Poland, this is a highly improbable figure.

Finally, the number of corporate bankruptcies in Japan rose again in 2007, by a substantial 38.9 percent to just under 11,000. The year before, the figure was just 7,910.

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Responsible for the content:
Creditreform Economic Research Unit
Head: Michael Bretz, telephone: (02131) 109-171
Editor: Anne Salm. telephone: (02131) 109-229
Hellersbergstr. 12, D - 41460 Neuss

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