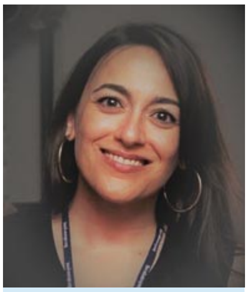
A closer look at:
Current business failure rates at artificially low levels



EMMANUELLE INACIO
INSOL Europe
Chief Technical Officer

Emmanuelle Inacio takes a closer look at the Dun & Bradstreet 2021 Global Bankruptcy Report

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The analysts at Dun & Bradstreet Worldwide Network (WWN) have prepared a 2021 Global Bankruptcy Report that's covers bankruptcy data from 43 economies[1].

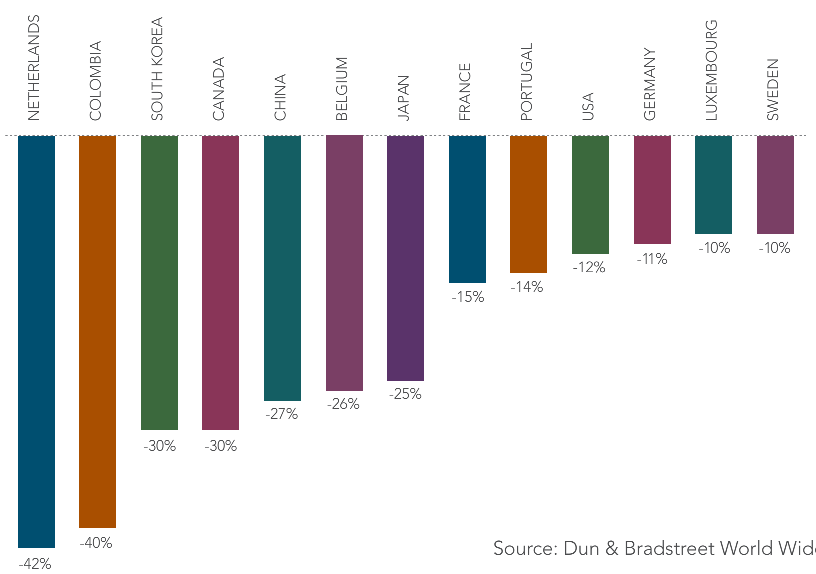
According to the Dun & Bradstreet 2021 Global Bankruptcy Report, nearly half of the 43 economies covered saw a decrease in business failures during 2021. In some countries, business failures reached their lowest level in a decade. Much like 2020, when business disruption rose to unprecedented levels, Covid-19 dominated the narrative in 2021. Sporadic increases in cases across many countries prompted mandatory shutdowns and continued to wreak havoc on businesses.

Data from the Dun & Bradstreet Commerce Disruption Tracker shows that the percentage of businesses disrupted globally increased by 4 percentage points in the first half of 2021 compared to the second half of 2020. As a result, the precipitous fall in business failures may appear counterintuitive. But there are several factors that have helped thousands of businesses keep their heads above water.

Undoubtedly, one of the biggest factors that helped many firms stay afloat was the massive support packages provided by governments across the world. While many of the measures were announced in 2020, they were also extended beyond this period. Cumulative fiscal measures in response to the Covid-19 pandemic account for 18% of the global Gross Domestic Product (GDP), according to data from the IMF.

Much of this stems from advanced economies, which on average have provided fiscal support to the tune of 28.4% of their GDP. By comparison, stimulus packages provided by these economies in response to the Global Financial Crisis of 2008 were worth just 2.6% of their GDP.

Access to low-cost liquidity has been a defining characteristic of the capital markets during the pandemic. The outstanding amount of total debt securities - which includes the amount borrowed in the domestic and international market, raised by non-financial corporations - stood



at USD19.05 trillion as of June 2021, according to data from the Bank for International Settlements (BIS). This represents a 15.8% increase from March 2020, compared to a 6.2% average annual increase over the preceding five years. This has served as a lifeline for many firms that were on the brink of bankruptcy.

Central banks across the world have been equally swift in easing monetary conditions to help businesses survive the pandemic. 32 of the 35 countries for which data is available have reduced their policy interest rates in response to the pandemic. These economies have, on average, reduced their policy rate by 123 basis points, according to data from the BIS. A basis point is equal to one one-hundredth of a percentage point. This is a significant decrease given that the average policy rate of these 32 economies stood at 2.01% during March 2020. The remaining three countries – Switzerland, Japan and Sweden – already had either negative or zero interest rates.

Another equally important factor that has resulted in a lower level of bankruptcies is the forbearance of creditors. In some economies, changes were made to the bankruptcy laws to provide businesses more breathing space and to avoid hostile takeovers by predatory firms. Such changes included an increase in the threshold amount above which a creditor could take action against a late-paying debtor, and the period within which the debt had to be repaid. Economies that suspended the mandatory obligation to declare bankruptcy include: India until March 2021; Germany until April 2021; and Spain until June 2022. These factors have played a role in suppressing business failure rates.

It appears that as fiscal and monetary policy supports are withdrawn and lenders become strict we would see a spike in businesses failures during 2022. While bankruptcies may not rise sharply across many economies, there will be more pockets of

distress surfacing, particularly during the second half of 2022. Fiscal packages are unlikely to be extended beyond 2021, given public debt has reached proportions comparable to those seen in the aftermath of the Second World War.

Driven by several factors of varying importance, inflation is turning out to be persistent and broad based than previously anticipated transient and narrow based (select commodities). As central banks scramble to ward off inflationary pressures by raising interest rates, the cost of servicing debt will increase for firms. Subsequently, the capital markets may also be less forgiving this time around. Data from the BIS shows that 16 out of 36 economies have already seen an increase in their policy rates during the second half of 2021.

The emergence of new variants of the virus, such as omicron, would further stress the already-fragile global supply chain, adding to inflationary pressures, and disrupt businesses by prolonging their recovery. In addition, comprehensive financial and trade sanctions imposed on Russia following its invasion of Ukraine threaten to exacerbate business bankruptcies in many countries, particularly in Europe, due to their high reliance on Russia for energy. A prolonged escalation of the crisis will also hurt businesses that are vulnerable to commodity shocks and increase bankruptcy risks. This warrants a more active approach to credit risk management. In the absence of additional support measures, this could be the spark that starts a chain reaction of bankruptcies and undermines creditors' confidence. ■

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Footnotes:

1 Download the complete Global Bankruptcy Report here: https://www.dnb.com/content/dam/english/economic-and-industry-insight/Updated_FINAL_TSK-10488_Global_Bankruptcy_Report%202021_20220509.pdf