Insolvencies

Extensive reading

Gloomy before dawn Q1, China

- Insolvencies in 2017 and 2018
- Improving situations

Allianz

EULER HERMES

EXECUTIVE SUMMARY

- The number of insolvency cases in China increased greatly in 2017(+74%) and 2018 (+50%) mainly due to the acceleration of clean-up zombie companies, slow-down on GDP growth and tightened financing conditions especially for the private owned enterprises.
- In 2019, the insolvencies are expected to grow at lower speed considering improving financing conditions, establishing a science and technology innovation board at the Shanghai Stock Exchange and recovery of real economy.

AUTHOR

EULER HERMES CHINA

INSOLVENCIES IN 2017 AND 2018

The number of insolvency cases in China increased greatly in 2017(+74%) and 2018 (+50%) mainly due to the acceleration of cleaning up zombie companies, slowdown on GDP growth and tightened financing conditions especially for small private owned enterprises.

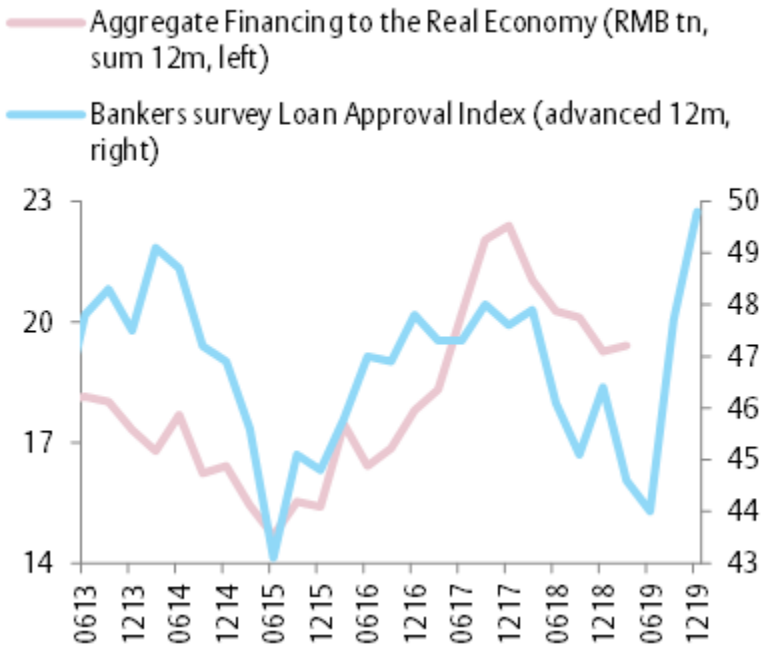
We summarized the reasons for insolvencies in recent years as below:

1. Zombie companies without active operation
2. Aggressive capital expenditure and M&A
3. Failure in new business
4. Main business in downturn
5. Long-term use of short loans
6. Poor cash flow of main business due to poor quality of accounts receivables
7. Unclear ownership structure
8. Poor internal control
9. Shareholders or actual controllers misappropriating funds
10. Sizable external guarantee
11. Excessive amount of related party transactions
12. Financial fraud etc.

IMPROVING SITUATIONS

In 2019, the insolvencies expected to grow at lower speed (+20%) considering improving financing conditions, establishing a science and technology innovation board at the Shanghai Stock Exchange and recovery of real economy benefiting from one-belt on road and tax cut.

Figure 1: Financing conditions



Sources: IHS, Allianz Research

A. Improving financing conditions especially for the private owned companies

In 2019, the supervisory authorities frequently adopted policies to support private enterprises. The State Council set up a bond financing support tool for private enterprises. The central bank increased the amount of refinance for small and micro enterprises. The lenient credit policy is applied to enterprise financing. Moreover, banker's survey suggests a pickup of credit in the coming months

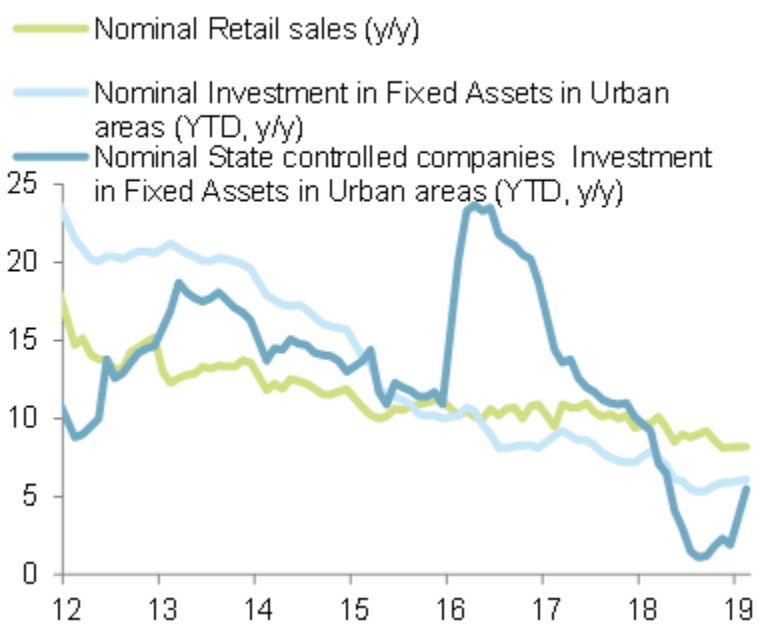
B. Eased capital financing condition

The capital financing condition is expected to ease after establish of Science and Technology Innovation Board at the Shanghai Stock Exchange in 2019. The new board is designed to help growth-oriented technology innovation enterprises with their finances. The capital market of China is expected to be open. Moreover, economic growth in China is expected to remain relatively resilient (GDP +6.4% for 2019), thanks to a proactive stimulus package (CNY 4.15 trillion, 5% of GDP) .The, overall credit condition of private enterprises is expected to improve in the second half of 2019.

C. Recovering demand stimulated by investment and tax cuts.

Domestic demand is likely recover in 2019 considering investment picks up speed as SOEs investment recovers and credit conditions improve.

Figure 2: Demand Indicators



Sources: IHS, Allianz Research

Moreover, consumer demand growth stabilizes on the back of tax cuts. The reduction of VAT tax was implemented on April 1, 2019. The Specific measures include reducing the level of VAT tax rate, expanding the scope of input tax deduction, implementing the system of retained tax rebate at the end of the trial period and adding and deducting the input tax of service industry. Tax reduction in VAT reform would be 10 billion yuan. Moreover, the newly revised regulations on the implementation of the Personal Income Tax Law came into effect on January 1, 2019, mainly through raising the starting point of individual tax and introducing six special additional tax deductions to reduce individual income tax. Tax cuts for individual tax reform are about 400 billion yuan.

Contact Us

Marketing.china@eulerhermes.com

www.eulerhermes.com

Euler Hermes Asia Pacific

WeChat: EulerHermes_China

Scan QR code to follow us in WeChat

Cautionary Note Regarding Forward-Looking Statements:

The statements contained herein may include statements of future expectations and other forward-looking statements that are based on management's current views and assumptions and involve known and unknown risks and uncertainties that could cause actual results, performance or events to differ materially from those expressed or implied in such statements. In addition to statements which are forward-looking by reason of context, the words "may", "will", "should", "expects", "plans", "intends", "anticipates", "believes", "estimates", "predicts", "potential", or "continue" and similar expressions identify forward-looking statements. Actual results, performance or events may differ materially from those in such statements due to, without limitation, (i) general economic conditions, including in particular economic conditions in the Euler Hermes Group's core business and core markets, (ii) performance of financial markets, including emerging markets, and including market volatility, liquidity and credit events (iii) the frequency and severity of insured loss events, including from natural catastrophes and including the development of loss expenses,(iv) persistency levels, (v) the extent of credit defaults, (vi) interest rate levels, (vii) currency exchange rates including the Euro/U.S. Dollar exchange rate, (viii) changing levels of competition, (ix) changes in laws and regulations, including monetary convergence and the European Monetary Union, (x) changes in the policies of central banks and/or foreign governments, (xi) the impact of acquisitions, including related integration issues, (xii) reorganization measures, and (xiii) general competitive factors, in each case on a local, regional, national and/or global basis. Many of these factors may be more likely to occur, or more pronounced, as a result of terrorist activities and their consequences.

No duty to update

The company assumes no obligation to update any information contained herein.