How Firms in Eastern and Central Europe Are Performing in the Post-Financial Crisis World

Paulo Correa, Mariana Iootty, Rita Ramalho, Jorge Rodríguez-Meza, Judy Yang

The Financial Crisis Survey monitors the effects of the financial crisis on private enterprises. The second wave of data was collected in February and March 2010 covering 1,892 enterprises in Bulgaria, Hungary, Kazakhstan, Latvia, Lithuania, Romania, and Turkey. The data show that annual sales declines have uniformly decreased and for a few countries, permanent employment levels and capacity utilization have stabilized or slightly increased. However, firms in most countries have decreased their employment levels and capacity utilization. The finances of enterprises have yet to improve: the concentration of short-term debt and the proportion of firms accumulating arrears increased in most of the surveyed countries. On the positive side, credit remained relatively accessible for most of those who applied for it. Surprisingly, the majority of enterprises reported keeping or expanding their R&D investments during the previous six months.

The Financial Crisis Survey (FCS) was developed to measure the effects of the financial crisis on private firms in selected countries. From the information collected during telephone interviews, indicators were computed to measure the effects of the crisis on key elements of the private economy: sales, employment, finances, and expectations of the future. Indicators were generated for a subsample of firms drawn from those previously interviewed in the Enterprise Surveys (ES) of 2008. Efforts were made to contact all respondents of the baseline survey to determine which of the firms were still operating and which were not. Participation in the Financial Crisis Survey was voluntary, and covered all sectors in the original sample. In all countries, the original sample of the ES was representative of the nonagricultural private formal economy. The original ES data also served as a baseline for comparisons because they referred mostly to fiscal year 2007, thus measuring the pre-crisis scenario. The results analyzed here were estimated through the use of sampling weights of the ES 2008 adjusted by non-response in each wave of the financial crisis survey. Therefore the results are still representative of the nonagricultural private economy within each country.

Table 1 Round two sample description

		Sample composition by size (%)			Sample composition by industry (%)		
	Total	Small (<20)	Medium (20-99)	Large (≥100)	Manufacturing	Retail	Other services
Bulgaria	152	47	33	20	35	32	34
Hungary	152	34	26	39	39	22	39
Kazakhstan	233	27	40	33	35	31	34
Latvia	221	36	33	32	36	33	31
Lithuania	224	41	32	28	38	27	35
Romania	304	30	37	34	40	23	37
Turkey	606	32	38	29	80	10	11

Note: Percentages may not add up to 100 due to rounding error.

The first round of the FCS was conducted in June and July 2009 in six countries: Bulgaria, Hungary, Latvia, Lithuania, Romania, and Turkey. The second round was implemented in February and March 2010 in the same six countries and in Kazakhstan, where a comparable questionnaire and methodology were used. The 2010 survey covered 1,892 firms both from manufacturing and service sectors (table 1).

Sales, Employment, and Production

Firms in all surveyed countries continued to experience a decrease in sales in the twelve months between February/ March 2010 and February/March 2009 (figure 1). The average percentage change in sales per country over a year's period (computed as the percent change reported by firms, weighted by the sales they recorded in the baseline survey of 2007) shows that the deepest reductions occurred in Latvia, Lithuania and Bulgaria. Yet, with the exception of Bulgaria, the sales reduction over a year period in 2010 was not as extensive as noted over the same length period in 2009.

The picture regarding permanent employment showed mixed results. Comparing the average permanent employment in February 2010 to June 2009 showed that in two countries, Turkey and Romania, average permanent employment increased (figure 2). Bulgaria experienced the largest decline, around 5 percent, while Lithuania and Hungary experienced a decline in permanent employment of 3.3 and 3.2 percent, respectively.

The concentration of short-term debt (with maturity of less than one year) rose in four of the surveyed countries.

The survey also measured the difference in capacity utilization in each wave of the financial crisis survey. In Bulgaria, Latvia, Lithuania and Romania the capacity utilization of manufacturing firms decreased between June 2009 and February 2010. Romania showed the deepest reduction: 15 percentage points. On the other hand, in Hungary the use of capacity utilization in manufacturing increased by almost 8 percent while in Turkey the use of capacity utilization remained almost constant (figure 3).

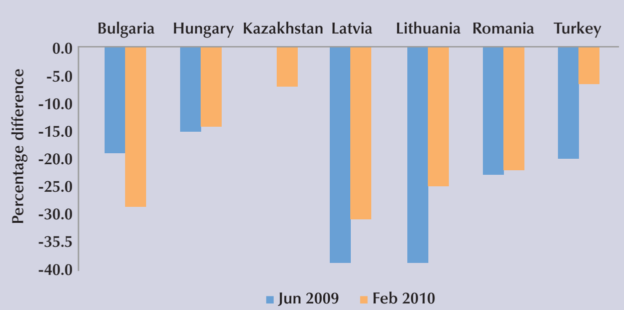
Financing and Access to Credit

Firms' finances have not yet improved. In four of the six countries surveyed initially, the percentage of firms overdue on their financial obligations increased from 2009 to 2010. Only Latvia and Hungary witnessed a decrease in this percentage (figure 4). Also, the concentration of short-term debt (with maturity of less than one year) rose in four of the surveyed countries: Turkey (from 67 percent to 77 percent)[1]; Romania (from 57 percent to 75 percent); Latvia (from 49 percent to 66 percent); and Bulgaria (from 49 percent to 58 percent). Firms in all countries reduced their foreign-denominated debt exposure. In Hungary, for instance, the average share of corporate sector debt in foreign currency fell from 35 percent to 17 percent.

Debt restructuring activities in early 2010 varied by country. In Hungary, extension of grace period was the most used instrument by firms seeking to restructure their liabilities; maturity extension was the most used instrument in Bulgaria, Kazakhstan, Latvia, Lithuania

Figure 1 Firms in nearly all countries lost sales in 2010, though less than in 2009

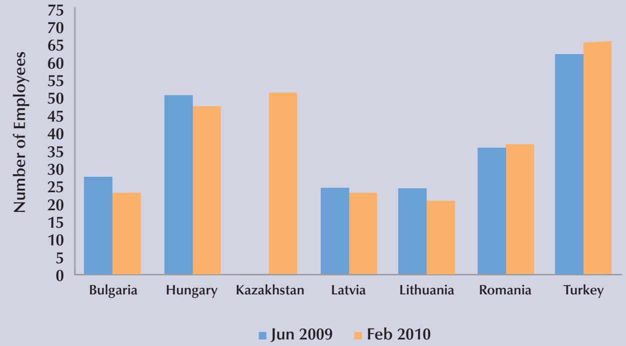
How sales in the last completed month compared to the same month a year ago



Source: Financial Crisis Survey, Enterprise Surveys.
Data for Turkey refer only to the manufacturing sector.

Figure 2 Permanent employment showed mixed results

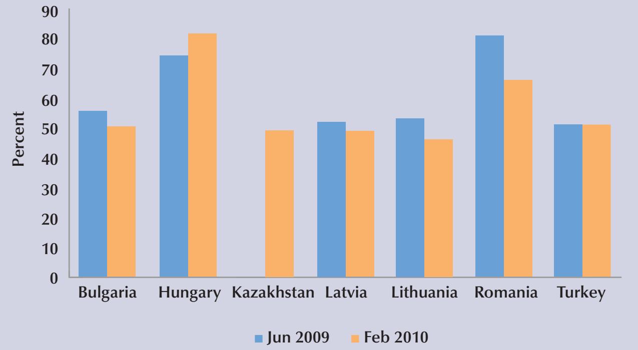
Average permanent employment



Source: Financial Crisis Survey, Enterprise Surveys.
Data for Turkey refer only to the manufacturing sector.

Figure 3 **Capacity utilization in manufacturing firms also showed mixed results**

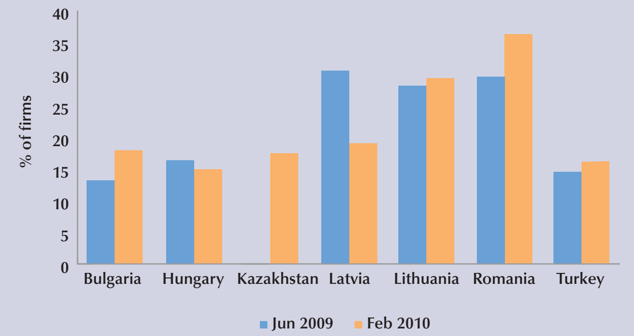
Average capacity utilization



Source: Financial Crisis Survey, Enterprise Surveys.

Figure 4 **Firms in Latvia and Hungary were less likely to be overdue in 2010**

Percentage of firms overdue on obligations in the previous year



Source: Financial Crisis Survey, Enterprise Surveys.
Data for Turkey refer only to the manufacturing sector.

and Turkey. In Romania, debt reduction was the main instrument used for debt restructuring.

Access to credit was another topic of the 2010 survey, measuring both the percentage of firms applying for loans or lines of credit as well as the ratio of loan size approved to that requested in the preceding 12 months. Data showed that Turkey had the largest proportion (56 percent) of manufacturing and service firms applying for loans or lines of credit. In Bulgaria and Romania, 25 percent and 29 percent of firms applied for credit. Kazakhstan, Latvia and Lithuania showed smaller proportions: 18 percent, 13 percent and 17 percent, respectively. Hungary showed the smallest proportion of credit applicants, just 3 percent.

In four of the six countries surveyed initially, the percentage of firms overdue on their financial obligations increased from 2009 to 2010.

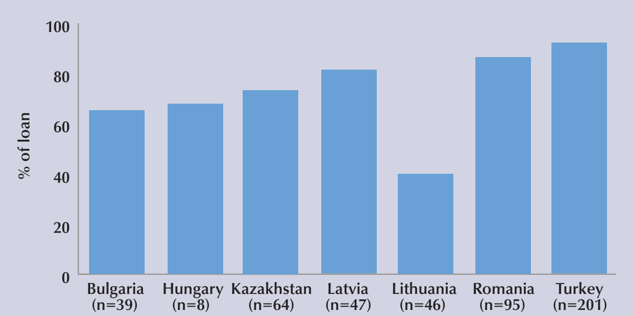
Firms that applied for credit did not seem to face severe credit rationing except in Lithuania, where loan size averaged just 40 percent of that requested. In Romania and Latvia, for instance, the average loan sizes approved were 86 percent and 81 percent of those requested (figure 5). There is, however, some heterogeneity across firm sizes. Small firms seemed to be credit squeezed when compared to large firms. In Bulgaria and Hungary, for instance, small companies received on average 62 percent and 57 percent, respectively, of their loan requests, while large firms received 92 percent and 80 percent, respectively.

In all countries but Romania, large firms were more likely to request loans than small or medium firms (figure 6). The trend was apparent in all six of the seven countries, but the scales varied strongly. In Hungary, very small percentages of firms in each size category requested loans in the preceding year. In Turkey, on the other hand, firms were much more likely to request loans—on average 52 percent of small, 62 percent of medium, and 62 percent of large firms did so.

Overall, enterprise finances in all countries have yet to improve. In four of the six countries surveyed both in 2009 and 2010 the proportion of firms accumulating arrears increased, with Hungary and Latvia being the exception. Moreover, the concentration

Figure 5 **Credit was relatively accessible In all countries, except Lithuania**

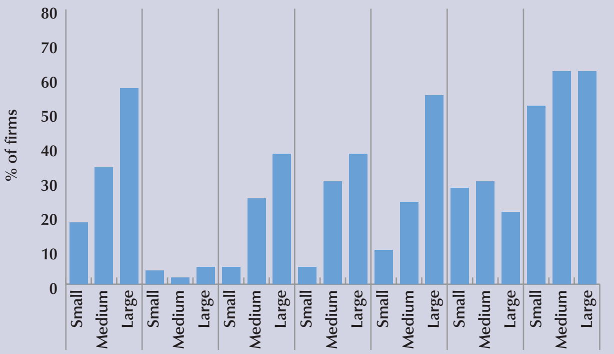
Percentage of loan obtained vs. amount requested in 2009



Source: Financial Crisis Survey, Enterprise Surveys.
Sample size in parenthesis.

Figure 6 Large firms predominated in applying for loans

Percentage of firms applying for loans in 2009



Source: Financial Crisis Survey, Enterprise Surveys.

of short term debt rose in most countries. Despite the substantial deleveraging of global financial markets, credit remained relatively accessible to those who applied for it, less so in Lithuania.

Research and Development

The 2010 survey asked firms whether R&D spending had increased, decreased or remained constant during the crisis in 2009. Despite the uncertainty in the credit markets, the majority of firms managed to maintain or expand their R&D spending in 2009. For example, 93 percent of the firms in Hungary and 82 percent of firms in Bulgaria sustained or improved on their 2008 levels of R&D (figure 7).

Despite the uncertainty in the credit markets, the majority of firms managed to maintain or expand their R&D spending in 2009.

Firms were also asked if they expected their R&D spending to increase, decrease or remain the same in the next six months. Results were somewhat less positive. In six of seven countries, firms reported to be more likely to decrease or maintain R&D spending in the future. For instance, in Hungary and Latvia 98 percent of firms expected either to decrease or keep constant their R&D spending. In Lithuania, this proportion was 87 percent. Only in Turkey was there a significant number—50 percent—of firms optimistic about future R&D spending.

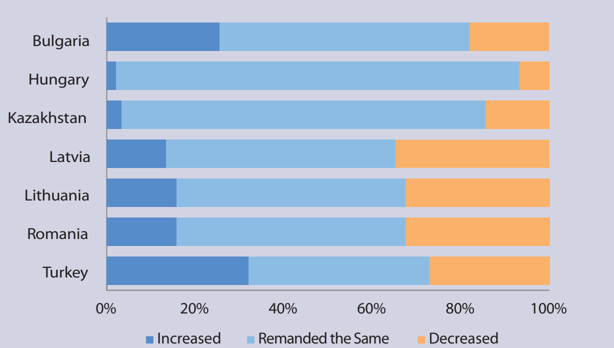
The fact that most firms managed to keep or expand their R&D activities is somewhat surprising, given the global downturn, but is consistent with the findings of other surveys.[2] If the expectations on R&D spending are confirmed, this could restrain future business innovation, thereby hindering firms from exploiting future growth opportunities.

Perceptions of Firms

The 2010 survey also asked firms how their overall situation compared to six months earlier. Most firms responded their overall situation did not improve or worsen; small and medium sized enterprises reported a more pessimistic view as compared to large firms particularly in Bulgaria and Latvia (figure 8). Data for Turkey indicate a more positive outlook from the business sector: almost 20 percent of small and more than 50 percent of large firms reported the situation to have improved in the previous six months.

Figure 7 Most firms managed to sustain or expand their R&D investments

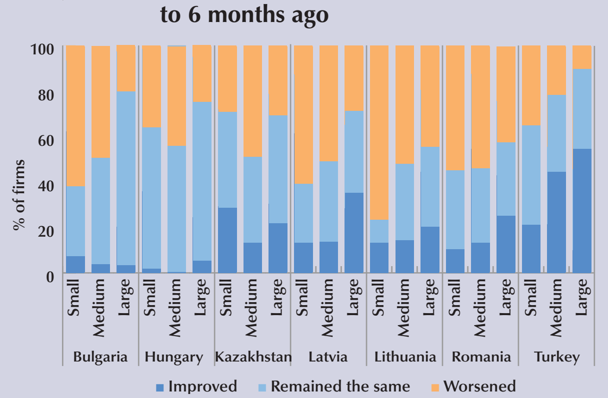
R&D spending in 2009



Source: Financial Crisis Survey, Enterprise Surveys.

Figure 8 Firms were still feeling the effects of the crisis

Firms overall situation compared to 6 months ago



Source: Financial Crisis Survey, Enterprise Surveys.

Conclusion

Sales declines have decelerated but losses in permanent employment showed mixed results between June 2009 and February 2010. Enterprise finances have yet to improve: the proportion of firms accumulating arrears increased in all countries except Hungary and Latvia; the concentration of short-term debt also rose, except in Hungary and Lithuania.

On the positive side, credit remained relatively accessible for those who applied for it (less so in Lithuania) despite the substantial deleveraging of global financial markets. Also, the majority of firms managed to keep or expand their R&D activities in 2009—even though most do not expect to increase it further in the near future.

Overall, firms' indebtedness might force them to allocate internal surpluses to service the debt. This, in turn, would affect their capacity to invest in R&D projects or, more broadly, explore new growth opportunities. In this sense, the sustainability of the recovery in the surveyed countries remains uncertain.

Notes

1. In Turkey, the proportions refer to manufacturing firms.
2. According to a Booz-Allen survey of the 1,000 public corporations worldwide that spent the most on researching and developing products and services, approximately 2/3 kept or increased their R&D spending. R&D spending for the top 20 companies was up 3.2 percent for 2008, less than half the 10.7 percent increase of the previous year.

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