Export Factoring in Greece: Current Developments and Future Prospects

Factoring is a set of financial services which meet the needs of businesses that sell their products or services on short-term open account terms to those of their customers that exhibit a recurring buying behaviour. It is a tripartite interaction between a seller, his buyers and a specialized financial intermediary (the “factor”) who undertakes the book-keeping, the administration and collection of the invoices issued by the seller. Furthermore, the factor may make advance payments on these invoices and may conditionally cover the seller’s credit risk.

Factoring is beneficial not only to new, small or rapidly growing companies which have increased working capital needs, but also to larger mature businesses that want more rational management of customer accounts, to limit the risks of possible insolvency or to improve the image of their balance sheet.

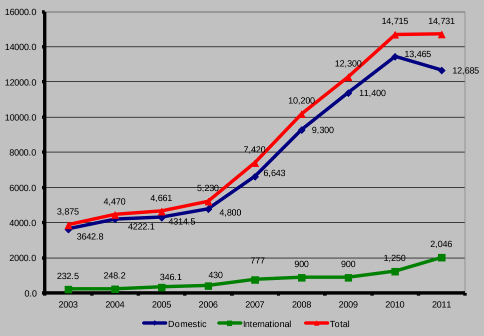
One specific type of factoring, ***export factoring***, enjoys outstanding growth at an international level (mean annual growth 30.5% in the last decade) due to the increase in international trade and escalating credit risk. Europe is the largest market since it accounts for 70% of international factoring (export-import). However, in recent years, there has been an impressive growth in international factoring in Asia (mainly China).

Export factoring services are offered by all ***Greek factors***, but about 80% of the export factoring turnover in Greece is concentrated in only three factors. Likewise there is a similar geographic concentration where 82.7% of total export factoring turnover is generated in just four countries (51.6% in Germany alone).

Both the short and long-term prospects of the sector are positive. Reinforcing factors that indicate growth of the factoring industry include a substantial growth in international trade, the need of Greek SMEs for continuous growth of export activities and the positive demand in international markets for Greek products.

July 2012

Factoring Turnover Growth in the Greek Market (mn €)



Source: FCI

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EXPORT FACTORING

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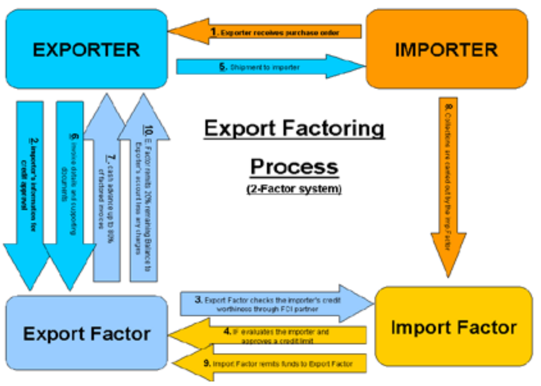
It is a tripartite interaction between a seller, his buyers and a specialized financial intermediary (the “factor”) who undertakes the book-keeping, the administration and collection of the invoices issued by the seller. Furthermore, the factor may make advance payments on these invoices and may conditionally cover the seller’s credit risk.
Factoring is beneficial not only to new, small or rapidly growing companies which have increased working capital needs, but also to larger mature businesses that want more rational management of customer accounts, to limit the risks of possible insolvency or to improve the image of their balance sheet (“window dressing”).
The primary piece of legislation regulating the establishment, supervision and operation of factoring companies in Greece is Law 1905/1990 “for the factoring contract and other provisions” as modified by subsequent additional national legislation and acts of the Governor of the Bank of Greece.
According to the current legislation, the business of factoring may be performed only by banks (having a specialized division in the field of factoring) or by bank subsidiaries (having as an exclusive purpose the selling of factoring).
From a statistical perspective, factoring is within the field of financial intermediation and according to the classification of NACE Rev.2 in the sub:

64.99 Other financial service activities, except insurance and pension funds (or 65.23 by NACE Rev. 1.1, and 64.99 in ISIC Rev.4).
The predominant forms of export factoring are ***Direct Export Factoring*** where the factor deals directly with the importers and the ***Two-Factor System***, where there is cooperation between two factors – the export and import factor (in the destination country of the seller’s products).
Depending on whether the credit risk is assumed by the factor, export factoring is divided into (a) ***Non (or Without) Recourse Factoring***, where the factor takes the credit risk against the buyer’s inability to repay its obligations and (b) ***With Recourse Factoring,*** where credit risk remains with the Supplier.

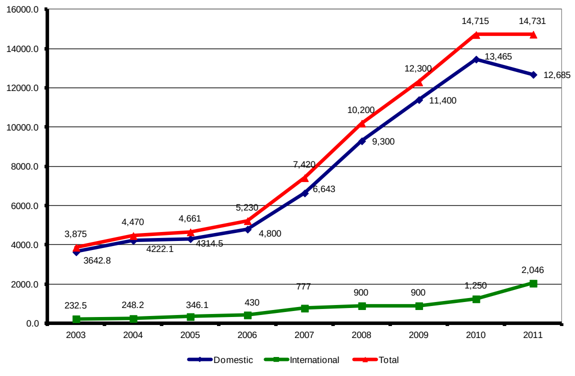
In 2011 78.6% of the Greek export factoring was launched through the two-factor system and as non-recourse export factoring.

Export Factoring Process



Source: Factors Chain International

Factoring Turnover Growth in the Greek Market (mn €)



Source: FCI

Industry environment

After 1990, following the establishment of the relative institutional framework, some banks began to offer products which were based on the logic of factoring, although they could not be considered factoring in the modern sense.

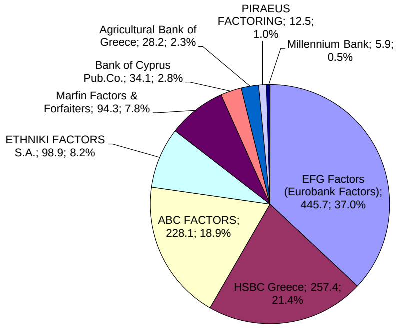
Factoring in our country began to develop significantly around 1994 with the creation of the first factoring company which offered full factoring services. During the period 1996-1999, the average annual growth rate of the factoring business was impressive, exceeding 45%. Then during 1999-2005 the growth rate became 31%, while for the latest period (2006-2011) the growth rate was 21.8%, a rate that can be regarded as very satisfactory given the deterioration of the Greek financial market. A key feature of this last period is the accelerating growth rate of export factoring, which was 37.2% as compared to 20.8% of domestic factoring.

Market performance and supply

The Greek factoring market is comprised of five independent companies which are bank subsidiaries and five bank factoring divisions. In addition to the above, export factoring services to major Greek export companies are provided through foreign banks, some of which may also have a physical presence in Greek territory.

Since the introduction of factoring in 1991, there have been significant changes in the market share, reallocations and increased concentration of production. Some commercial banks attempted to grow their business through their branch network; this did not prove to be successful due either to internal competition with traditional banking products or to organizational difficulties. In recent years, the above situation has changed and synergies have been created which are a result of both the special circumstances prevailing in the Greek market and the accounting and tax treatment of factoring. In export factoring, the concentration of production is very high since the top three companies control 77% of the market (EFG Factors 37%, HSBC 21.4%, ABC Factors 18.9%; others 23%). Another feature of the Greek export factoring market is the very high geographical concentration of business as the top four countries cover 82.7% of the total (Germany 51.6%, Italy 13.3%, France 9.2%, Great Britain 8.6%); a disproportionately high percentage, considering the total share of Greek exports to these countries (24.2% in 2011). This is mainly due to the orientation of the three major players in these markets (EFG Factors, 88.5%, HSBC 98% ABC Factors 92.4%), while smaller companies have comparatively lower geographical concentration (Ethniki Factors 65.4%, Piraeus Factoring 48.8%, Marfin Factors & Forfaiters 26.6%, Bank of Cyprus 49.9%).

Export Factoring Market Shares (2011, mn € and %)



Source: FCI

Export factoring development & Total Factoring(in ml €.)

	2008	2009	2010	2011
EXPORT FACTORING				
2-Factor Non Recourse Factoring	364	414	1.107	1.447
2-Factor With recourse	301	34	292	93
Direct Export Fact.	183	29	0	0
Export Factoring (total)	**849**	**777**	**1.399**	**1.840**
Import Factoring (Total)	175	157	214	207
International Factoring (Total)	**1.023**	**934**	**1.613**	**2.047**
Domestic Factoring (Total)	9.596	11.515	13.103	12.685
Factoring (Total)	**10.619**	**12.449**	**14.716**	**14.732**

Source: Hellenic Factoring Association

The factors that affect firms' decisions to consider export factoring is (a) the need to reduce credit risk, (b) liquidity reasons, (c) reduction of accounts receivables management costs (especially for international clients), (d) prompt payment of suppliers so the seller can doubly benefit by taking advantage of prompt payment discounts and improving his credit standing with suppliers, (e) lower administration costs for the Seller as his buyers' portfolio is managed by the factor (outsourcing philosophy), (f) lower collection costs etc.

Quantifying the importance of each factor is difficult and pointless because each client company has its own distinct characteristics (financial structure, strategy, market conditions etc) and needs vary depending on economic conditions. Empirical studies carried out abroad show that the factoring client's main aim is to minimize credit risk and, to a lesser extent, to improve liquidity or management of their accounts receivables needs.

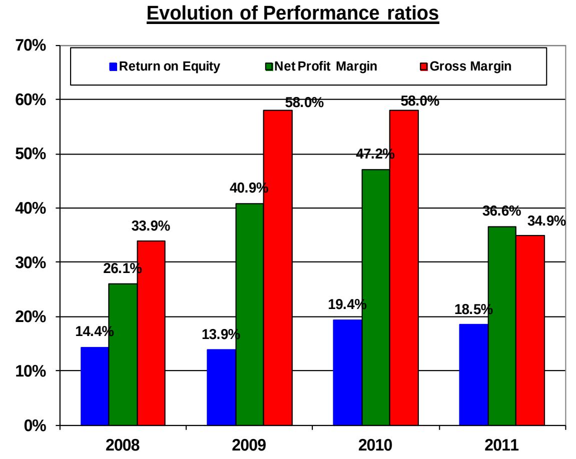
Financial analysis – Greek market

Consolidated industry figures relate only to the five independent factoring companies and do not include bank divisions as the latter do not publish detailed data on their factoring operations. Total revenue in 2009 had decreased by 31.8% and then showed an impressive increase of 34.8% in 2010 and 41.8% in 2011.

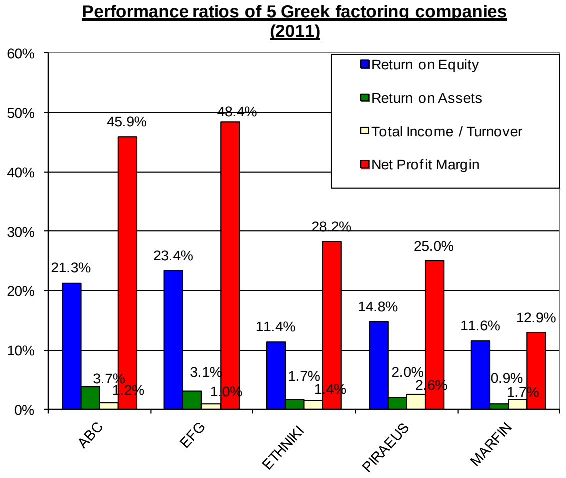
Performance indices are at very satisfactory levels, especially when taking into consideration the severity of the economic crisis affecting Greece. Return on Equity in 2011 is 18.5% (14.4% in 2008), Gross Margin declined in 2011 (to 36.6% from 58% in 2010) while the Net Profit Margin (Net Profit Before Tax / Total Revenues) despite a significant reduction (to 36.6% from 47.2% in 2010) is still remarkable considering the severity of the current crisis.

Structural indices are continuously improving and in 2011 all companies are at satisfactory levels. The Equity/Total Liabilities ratio is constantly improving and reached 13.9% in 2011 from 9.5% in 2008. The Capital Adequacy ratio is high; in 2011 it was 18.5% with three companies above the 20% mark (EFG 26.2%, ABC 21.9%, Piraeus 20.4%). According to the consolidated balance sheet, 0.19% of turnover and 1.08% of total accounts receivable is in arrears while NPL/Projections is 1.23.

The average International Factoring accounts receivables share was 11.9%, albeit with large differences from company to company (Marfin 35.2%, EFG 14.5%, ABC 7.7%, Piraeus 6.4% and Ethniki 2.4%).



Source: Piraeus Research



Source: Piraeus Research

International Environment

Factoring is one of the fastest growing industries, with a total turnover exceeding two trillion euros in 2011 (€2,015.4 billion). When compared to 2001 (€685.7 billion) it can easily be seen that factoring has more than tripled in absolute value. Similarly, one can observe an unprecedented growth in export factoring turnover. More specifically, during the last decade, total turnover has grown by a factor of more than 12, while the share of export factoring compared to total factoring activities has grown from 4.3% in 2001 to 14.2% in 2011. Moreover, the annual mean growth of export factoring during the period 2001-2011 was 30.5%, while the rate for import factoring was 15.9% and for domestic factoring 12.4%.

In 2011 total global turnover increased by 22%, while the growth of global international factoring turnover was even higher (37%).

Countries with the most spectacular growth in factoring turnover include China (77%), Russia (74%), South Africa (41%), Holland (31%) and Australia (28%). Those impressive rates are due to increasing familiarization of exporters and importers with the advantages of factoring, which can mitigate risks in today's highly volatile global economic environment.

Europe is the biggest factoring market, accounting for 59% of total global factoring turnover, while it is responsible for 70% of total international factoring turnover and 59% of total domestic factoring turnover. Asia accounts for 23.4% of the total international factoring turnover, while America accounts for 6.3%, Africa for 0.2% and Oceania for 0.1%

Problems - Future trends

Export factoring is one of the few financial activities in Greece that exhibits positive trends in today's severe and ongoing economic crisis. Factoring can mitigate problems of international trade, especially those faced by small and medium-sized enterprises. Such problems include decline in domestic demand, lack of liquidity, increase in high-risk debts and lack of access to credit lines. All these problems can be tackled efficiently through factoring (domestic or export), the utilization of which offers numerous advantages.

Some of the most important benefits of export factoring include: a) immediate financing b) diminishing collateral needs c) financing of sales ensuring uninterrupted liquidity d) increased bargaining leverage with creditors and clients e) on-going monitoring of existing clientele and evaluation of prospective customers, improving both the collection of accounts receivable and liquidity f) improved management of the ledger account which decreases operational costs g) protection against customers' defaults and credit risk.

In addition to the above, factoring (non-recourse) improves the client company's credit rating and financial ratios since it is not treated as a liability. Export factoring allows for the provision of an extended credit period to clients, while it provides absolute protection against their customers' default. Moreover the exporter is able to finance invoices, decrease the financial cost by avoiding the use of Letters of Credit, and get paid within the 90-day limit. Through the use of the twin factor system, the corresponding factor is able to communicate in many languages, offering a competitive advantage for exporters who require excellent communication with their clients. Likewise, the corresponding factor offers specialized services with regard to the legislative framework of different countries.

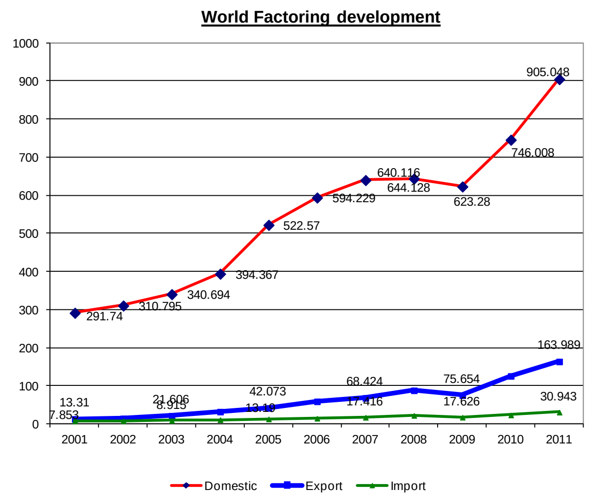
Extroversion is probably the only answer to declining sales in the domestic market. Factoring is a financial tool that can provide a great boost to any company's outward orientation, providing access to foreign markets and improved business terms with customers and suppliers.

The Greek economy presents a rather disappointing extroversion profile, which in many cases is similar to those of underdeveloped and Third World economies. Thus there is a lot of room for improvement in this area, given that domestic production means will respond to an increased demand. Economic extroversion has improved substantially (mainly due to increased exports rather than a reduction in GDP), from 9% in 2009 to 13% in 2011 and a prospective 15% for 2013.

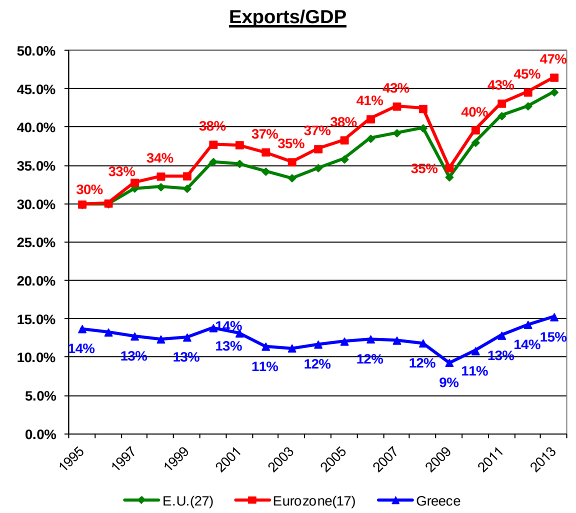
By dispersing risk to countries with stable economies, accounts receivable turnover ratio and inventory turnover ratio can be improved, and debt delinquencies can be decreased. According to recent research on Greek businesses (Atradius, 2012), only 10.9% of international sales receivables' is over a 60-day credit limit (compared to 28.3% for domestic sales), delinquencies from foreign clients is down to 17.6% (compared to 41.1% for domestic sales), while the percentage of non-collectable receivables after 6 months is merely 2% of sales (compared to 7.4% for domestic sales).

Due to the different credit approach, whereby factors are interested in the creditworthiness of clients (accounts receivable), rather than that of suppliers, companies with "unhealthy" balance sheets can still be financed, whereas banking institutions would have rejected their applications.

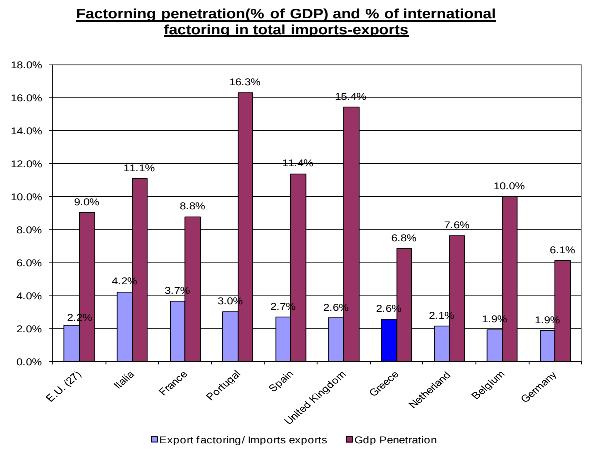
While the aforementioned advantages are expected to boost the use of factoring by small and medium-sized businesses, the growth of international trade will provide an additional positive impact on the sector, especially due to increased demand by developing countries.



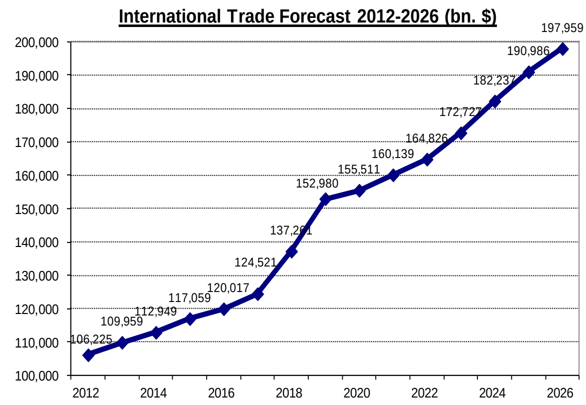
Source: FCI



Source: EUROSTAT



Source: FCI and EUROSTAT



Source: HSBC: Trade Forecast, June 2012.

According to an HSBC-Delta Economics report, the short-term prospects for international trade are positive while the long-term ones are excellent. The annual growth rate of international trade is projected to be 3.7% until 2017, while for the five-year period after 2017 an acceleration with a mean annual growth of 5.9% is projected.

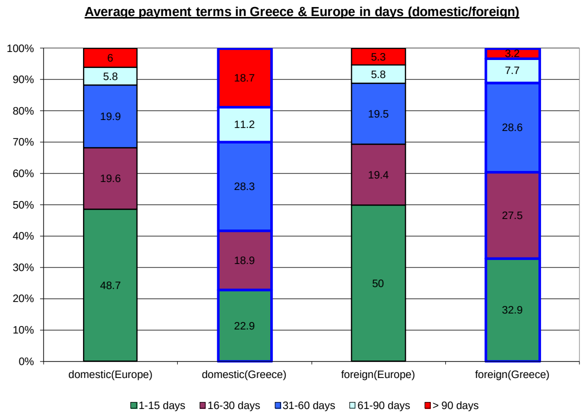
One positive aspect for Greece is that international demand will be higher for products which are already produced in our country, and which enjoy a certain competitive advantage. Some industries like chemicals, car manufacturing, oil trade, and electronics will face an economic downturn where others will be favoured. Industries which are more likely to experience an uptrend include electricity production, packaging materials, logistics, metal products, food production, telecommunications and pharmaceutical products.

The only possible problem that may impede the growth of export factoring could be the lack of liquidity of the Greek banking system and the resulting drought in financing. Credit risk was at a record level high in 2008, but it is now back to normal levels, which do not affect profitability prospects for factoring companies.

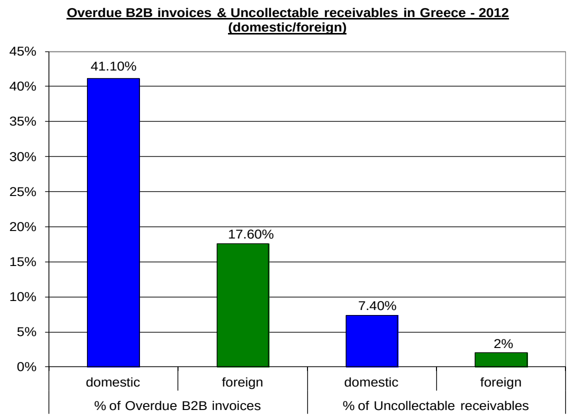
In today's volatile conditions, projections for the export factoring industry can only be made with a high degree of uncertainty. However, if we assume that the current crisis has run its course and there will not be any further deterioration in the financial situation, then there are several reasons to believe that factoring will enjoy positive growth rates. Such reasons include the projected growth of international trade, the call for business extroversion (due to low domestic demand) and the need to overcome liquidity problems and credit risk issues, which will certainly be apparent for the next couple of years.

The parameters used for the three projected scenarios are: businesses' liquidity, level of penetration in the economy, export projections for the four mature export markets (where we had a mean penetration of 28% for 2011) and for the rest of the markets where growth is more promising (where we had a mean penetration of only 1.87%).

In order to quantify business liquidity we have used the ratio Accounts Receivables/Total Assets (AR/TA) since, according to recent research, this is the defining factor in the decision to use factoring. We have used data for the last five years and we found that for any 10% change (increase/decrease) in the ratio AR/TA, there is a similar change in sales of 3.9%.



Source: Atradius Payment Practices Barometer, 2012



Source: Atradius Payment Practices Barometer, 2012

Conclusions

Export factoring is one of the fastest growing industries, and it can have very significant positive effects on business extroversion, enhanced liquidity and decreased delinquencies. Apart from the obvious advantages that can be offered to a wide array of companies, factoring is also a useful financial tool that can facilitate national economic growth and improve national competitiveness.

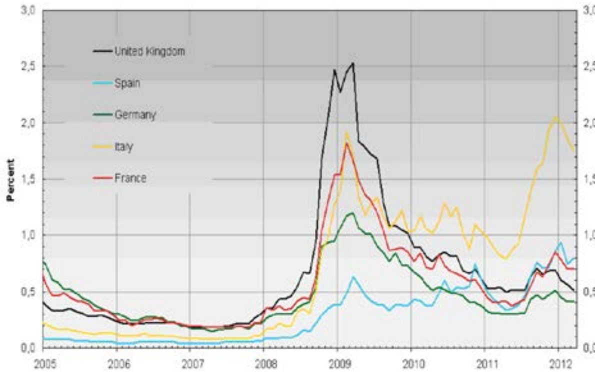
Export factoring services are offered by all Greek factors, but about 80% of the export factoring turnover in Greece is concentrated in only three factors. Likewise there is a similar geographic concentration where 82.7% of total export factoring turnover is generated in just four countries (51.6% in Germany alone).

Similarly, there is outstanding growth of export factoring at an international level (mean annual growth 30.5% in the last decade) due to the increase in international trade and escalating credit risk. Europe is the largest market since it accounts for 70% of international factoring (export-import). However, in recent years, there has been an impressive growth in international factoring in Asia (mainly China).

Both the short and long-term prospects of the sector are positive. Reinforcing factors that indicate growth of the factoring industry include a substantial growth in international trade, the need of Greek SMEs for continuous growth of export activities and the positive demand in international markets for Greek products.

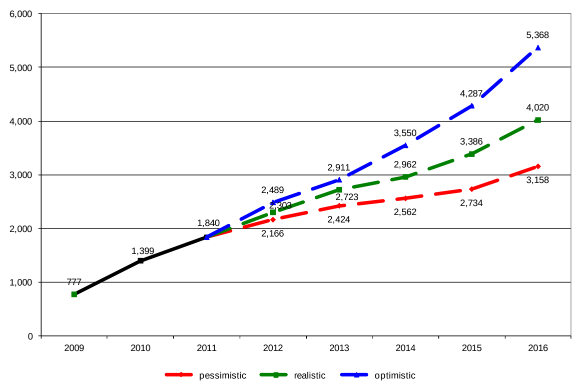
On a macro level, there are serious problems and threats due to the tragic failure of Greece's old economic model. However, the current crisis might have a profound influence on the birth of a new more dynamic, modern and innovative economy. The magnitude and complexity of the current crises (economic, political, social) demand a transformation to a more productive and extrovert economy. In this light, there will be several opportunities for growth of export activities, hence for an equivalent growth in the export factoring market.

Median EDF evolution in the most important markets of Greek export factoring



Source: KMV Credit Monitor and Atradius Economic Research June 2012

Growth forecasts for Export Factoring in Greece



Source: Piraeus Research

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