

SECTOR COMMENT

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Contacts

Antonio Tena, Ph.D. 34-91-768-8235
Vice President
 antonio.tena@moody.com

Greg Davies 44-20-7772-5311
AVP-Research Analyst
 gregory.davies@moody.com

Christopher Chambers 44-2077-72-8746
Associate Analyst
 christopher.chambers@moody.com

ABS SME - EMEA

Differences in Net Growth of Enterprises Indicate Divergence of SME Performance Across Europe

Summary

A valuable indicator to forecast the performance of asset-backed securities (ABS) backed by loans granted to small and medium-sized enterprises (SMEs) in Europe is an analysis of net growth in the number of enterprises per country, and the rate of failure. These growth and failure rates correlate closely with the credit performance of SMEs, alongside domestic and European macroeconomic trends. Trends in the number of newly created enterprises minus dissolved enterprises is a strong forward-looking indicator for SME performance in a specific country, providing insight into the business climate for SMEs in Europe.

This report forecasts performance and compares trends in six SME ABS markets in Europe: Belgium (Aa3 stable), France (Aa2 stable), Italy (Baa2 stable), Portugal (Ba1 stable), Spain (Baa2 stable) and the UK (Aa1 stable). Overall, we anticipate that SMEs in Western European countries will outperform their weaker Southern European counterparts in light of the stronger net growth of enterprises.

Growth rate of enterprises predicts stronger SME credit performance in Western Europe

Different business climates among countries are driving the divergence in performance for SMEs in Europe. As a result, we anticipate much stronger SME performance in Western Europe (the UK and Belgium) than in Southern Europe (Italy, Spain and Portugal). The UK shows the most dynamic growth in the number of SMEs, which correlates with the best performance for SMEs across the countries in this study. On the contrary, deterioration of enterprise performance correlates with the highest non-performing loans (NPLs) for non-financial corporates (NFCs) in Italy. The correlation in France and Portugal between performance and business growth is shown to be weak.

There are more than 22 million SMEs in the European Union, which represent a significant part of national economies, as Exhibit 1 shows. SMEs total more than 99% of total enterprises in the main markets, approximately 58% of the total value added in the EU (i.e. gross income from operating activities after adjusting for operating subsidies and indirect taxes).

SME markets in the UK and Belgium will continue to show the strongest credit performance in Europe. The steady growth of enterprises in the UK and Belgium shows that SMEs in these

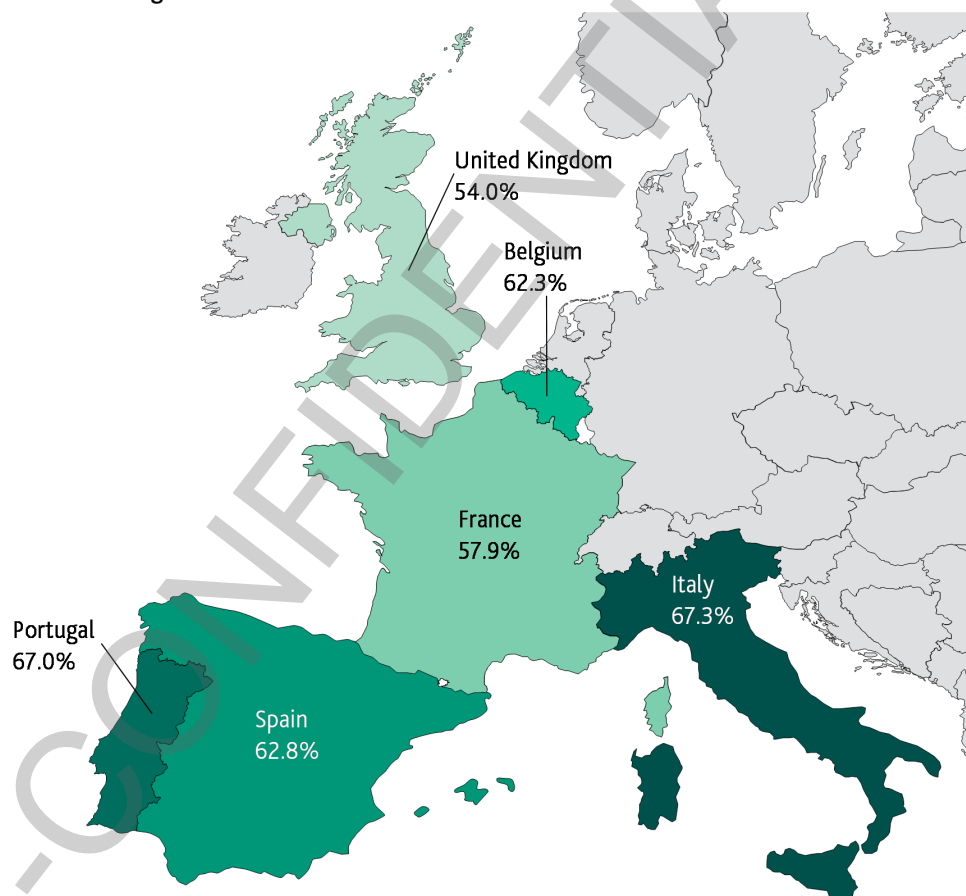
countries have performed steadily through years of economic turbulence and will be less vulnerable to headwinds.

Spain shows high NPLs for SMEs, following the net failure of enterprises over the 2008-13 period, although the trend reversed course in 2013, the same year that net growth of enterprises also turned positive.

Exhibit 1

ABS SME Markets in Europe Show a Significant SME Weight as % of Total Added Value in National Economies

Italy	67.3%
Portugal	67.0%
Spain	62.8%
Belgium	62.3%
France	57.9%
UK	54.0%



Source: Eurostat

Exhibit 2 shows the correlation between business demography and SME performance, and compares two data series per country:

- » NPLs for NFCs per country, year by year, as reported by the national banks. There are no historical data for NPLs on NFCs in the UK. Exhibit 2 shows the global levels of write-offs in the UK banking system as reported by the Bank of England.
- » Net growth of enterprises (NGE), the difference between the number of created and failed enterprises, as a percentage of existing enterprises in the country. This ratio can be positive (if there are more created than dissolved companies), or negative. Positive levels show a good business climate for the country in a specific year.

Exhibit 2 shows how the growth of enterprises remained unaffected in the UK and Belgium despite the turbulence in recent years. Net growth of enterprises has remained positive in Belgium each year, and the situation is similar in the UK, with only 2009-10 showing a

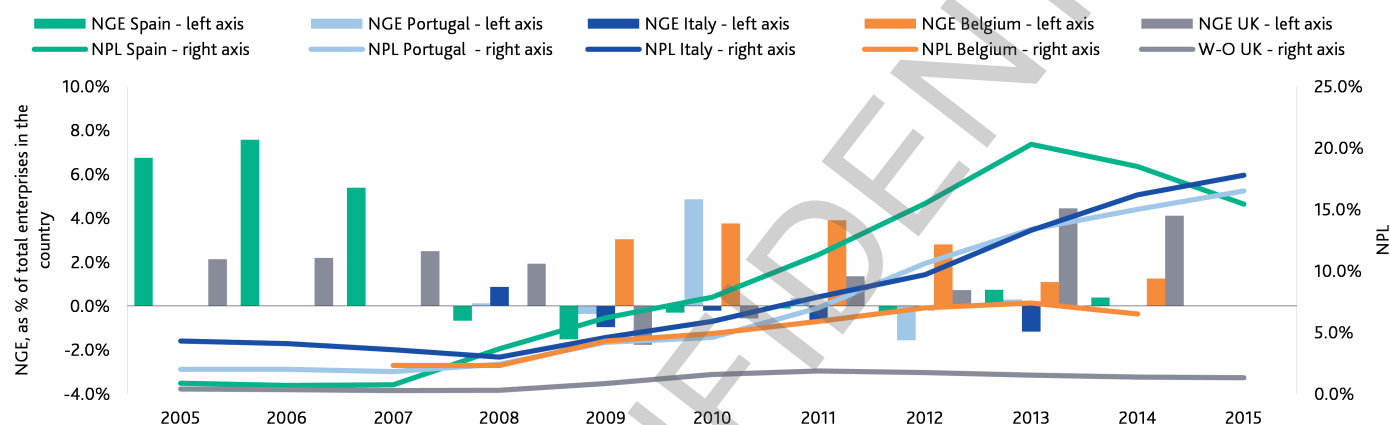
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net failure of enterprises. This strength correlates with stable performance of loans granted to enterprises, as indicated by the lines for these two countries representing NPLs.

In contrast, the Italian data shows that the failure of companies has accelerated, as represented by the bars below zero, which correlate with the steadily growing NPL line that represents the performance of loans to enterprises in the country. This correlation shows the deepening of the deterioration in SMEs' credit performance. The exhibit also shows that in Spain, net growth of enterprises turned positive in 2013; since then, NPLs for Spanish NFCs have been in decline.

Exhibit 2

Variations in Net Growth of Enterprises Forecasts Divergence of SME Performance Across Europe



Comparable data unavailable for France

Sources: National Banks, Spanish National Institute of Statistics (INE), Portuguese National Institute of Statistics (INE), Italian National Institute of Statistics (ISTAT), UK Office of National Statistics (ONS), Direction générale Statistique - Statistics Belgium

Country Specific Analysis

UNITED KINGDOM

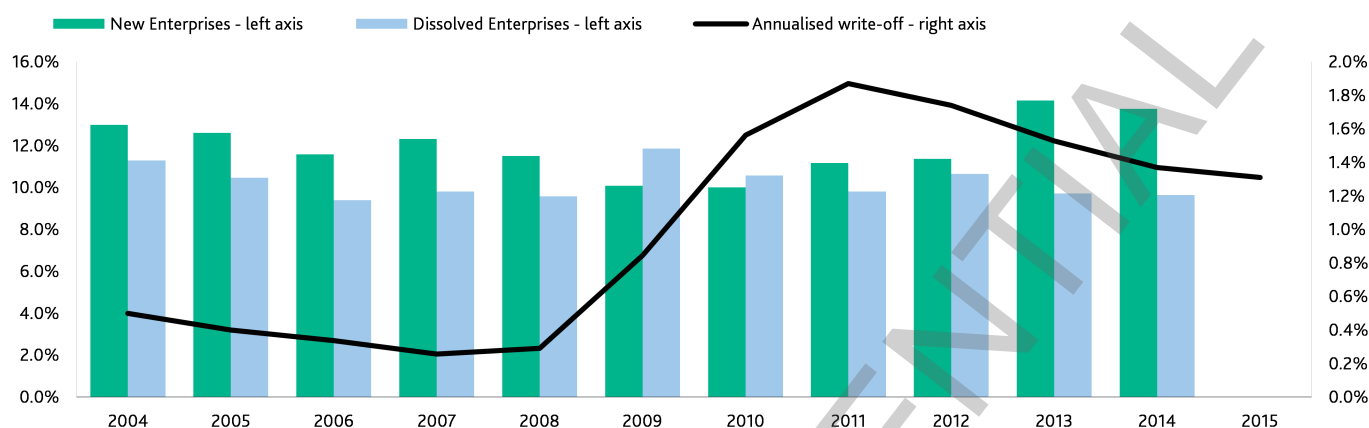
Expansion of SMEs will continue to boost the performance of SME loans into 2016

The UK will continue to show the most dynamic environment for growth in SMEs, based on the solid performance through the turbulence over the last 10 years. During this period, there has been steady net growth in the number of SMEs in the UK¹. The strong performance of SMEs in the UK is partially a result of UK SMEs benefiting from positive sentiment in political will to increase funding availability, competition², and political measures (i.e. the government-owned British Business Bank). As a result, UK SMEs' value-added grew by 11.6% in 2014, compared with the European average of 3.3%³.

This strong growth has coincided with unemployment in the UK improving to 5.1% as of 2015, from a peak of 8.1% in 2011, with SMEs playing a key role in the recovery⁴. Small employing enterprises contributed the highest amount (482,000 in headcount), a 14% increase between 2011-15, according to the Department for Business, Innovation & Skills (BIS). The global financial crisis has not affected the general increasing trend in UK SMEs, unlike the other European markets in this report.

Despite the deterioration in write-off levels for NFCs from 2009 until 2011, UK enterprise expansion has accelerated in the last two years. A record net creation of 108,860 enterprises in 2013 was followed by strong new enterprise creation of 104,750 in 2014, bringing the total to 2.6 million as of the end of 2014. Data sourced from the Office of National Statistics (ONS) excludes non-registered businesses and businesses with no employees. This growth, combined with the recent increase in net registrations of new SMEs, is generally positive for UK SMEs.

Exhibit 3

Increasing Number of UK SMEs Suggests Strong Credit Performance

New and dissolved enterprise percentages are calculated compared to total stock of enterprises for each year.

Source: ONS

UK SMEs show the best performance across European countries

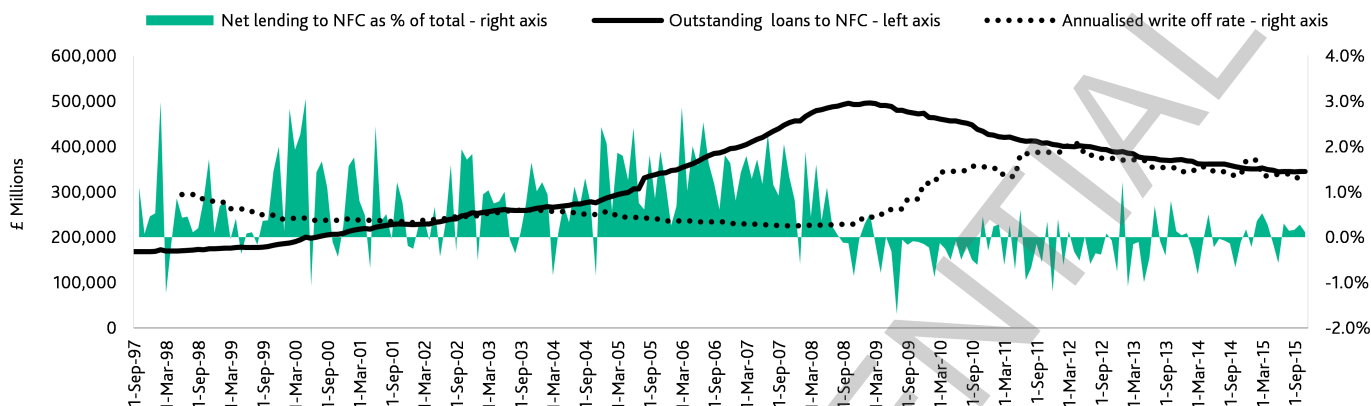
The Bank of England (BoE) shows the level of write-off loans for UK NFCs, but it does not report the historical series of NPLs. The annualised write-off rate of loans to private NFCs stood at 1.3% as of 2015, still higher than before the global financial turmoil in 2009 (0.3%), but write-offs have recently been trending downward. Furthermore, NPL ratios for NFCs in the UK as reported by the European Banking Authority (EBA) since 2014 are significantly better than in other EU countries, at 4.3% as of June 2015, down from 5.4% as of December 2014⁵. This level compares with Italy at 25.2% and Portugal at 29.2%. However, the lower NPL ratio coincides with high levels of forbearance on SME loans, with 6% of SME borrowers reported to be in some form of forbearance. This forbearance is concentrated in SMEs that had large amounts of debt, which signifies that the forbearance is not a systemic issue within the market itself⁶. Nonetheless, this forbearance could be reducing the actual improvement in UK SME credit performance.

The number of SMEs is growing with hurdles to access finance easing

Alongside the net number of UK SMEs growing, SMEs' access to finance has shown recent indications of improving. Application acceptance levels have increased, with 73% of applications for finance being approved in Q4 2015 for the previous 18 months compared to only 59% in Q4 2012⁷. This has not yet followed through to increased levels of borrowing, as while there are no figures for the specific SME segment, the overall financing of NFCs has been decreasing since 2008, as Exhibit 4 shows.

Volumes are significantly weaker than they were before the financial crisis, but they appear to be largely driven by decreasing borrowing by large corporates rather than the retrenchment of SMEs. Corporate borrowing should show signs of vigour as recent activity in the merger and acquisition market is creating demand from larger corporates⁸. On the positive side, net lending to private NFCs improved in December 2014 and was net positive for nine months in the rolling 12 months, indicating a change toward more access to finance for SMEs. The number of SMEs using bank-based lending in Q4 2015 was the greatest since Q4 2013, demonstrating a recent uptick in demand⁹.

Exhibit 4

Stock of Loans to UK NFCs Going Down Since 2008

Source: ONS, BoE, Moody's calculations

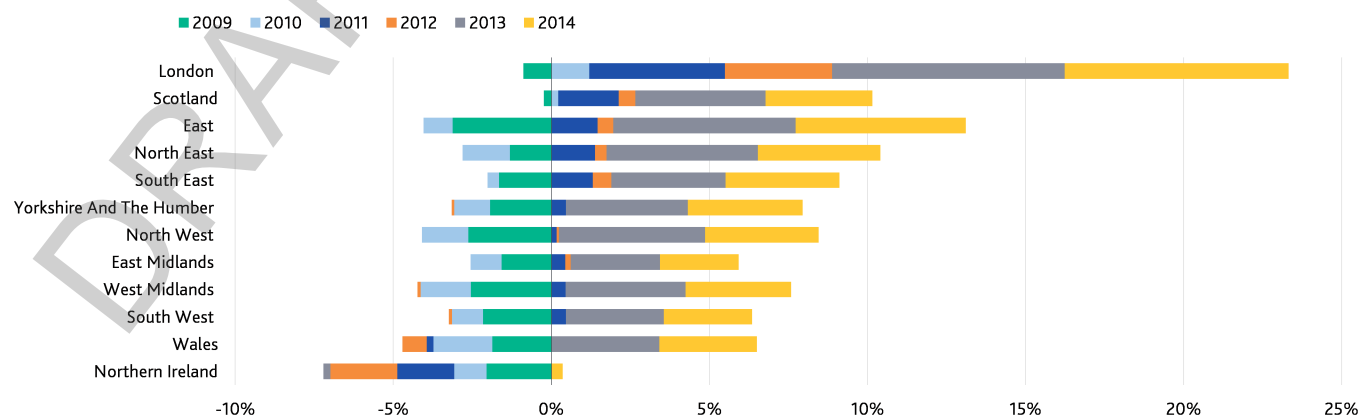
Diversification of funding sources for UK SMEs is credit positive

Funding for SMEs (via loans) by the Bank of England and HM Treasury's 'Funding for Lending' scheme incentivised banks to lend to SMEs by providing access to £5 of low rate funding in return for every £1 of net lending to SMEs, available to drawdown until the end of 2018¹⁰. Furthermore, the entry of several new challenger banks into the UK banking sector is providing alternative sources of funding; this is also positive as they offer more sources and decrease SME reliance on any single funding source. Overall, this additional support is credit positive for the UK SME market. A recent survey indicated the positive sentiment in SME markets, with only 6% of SMEs rating access to finance as a barrier to their business performance, with another positive indicator that 47% of SMEs are planning to grow in the next 12 months¹¹.

Difference in business climate for SMEs across UK regions

While the net increasing registrations of new SMEs is a positive trend, the growth of companies is heavily skewed towards London and the surrounding regions, with Northern Ireland only registering a small increase in 2014 for the first time since 2009, as Exhibit 5 shows. Despite the concentrations in growth, the typical five-year survival rate of SMEs does not differ largely between regions, with London achieving the lowest rate of survival at 38.6% compared to South West at 45.0% (UK total was 41.7%). Regional company growth was more widespread in 2013-14, this is a positive credit trend and is further evidenced through all regions demonstrating economic growth on the year¹². Northern Ireland is yet to have sustained registration growth, but economic activity increased by 1.1% year over year as of the third quarter of 2015, driven by private sector growth, which is a positive credit indicator for the SME sector¹³.

Exhibit 5

Net Regional Business Creation Is London Centric

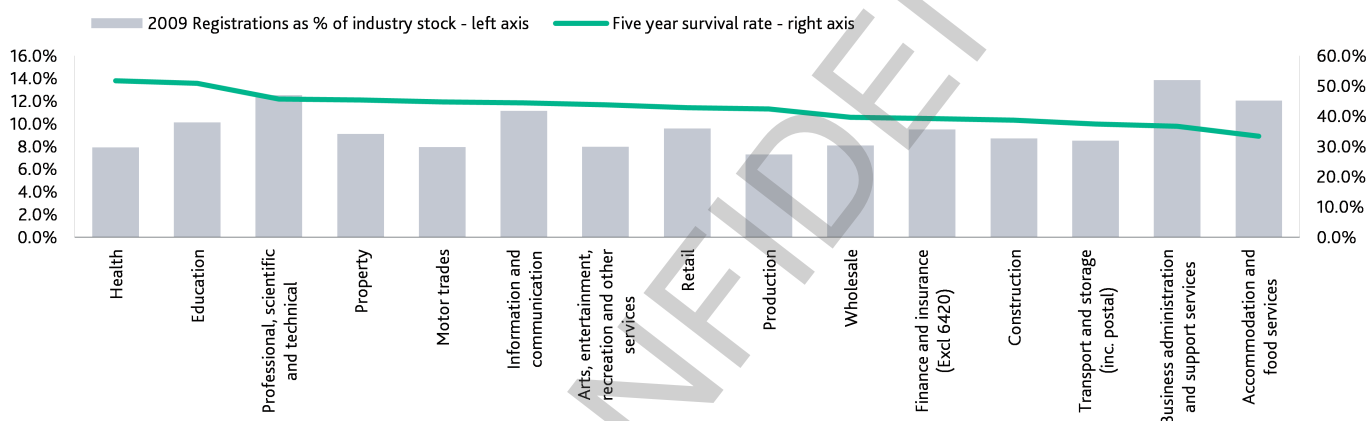
Source: Office for National Statistics

Different trends in SMEs per industry

Education and Health-focused SMEs are likely to record the strongest performance among SME sectors because they are the two industries with the highest five-year survival rates. However, as of 2009, they made up only 5% of the total registrations for new SMEs. Among other reasons, the Education and Health sectors may have the highest survival rate because they are industries that are largely protected from the UK government's austerity programme. The worst performers were accommodation and food services, followed by business administration and support services, although both were in the top three industries for new company registrations (alongside professional and scientific). Alongside having the lowest survivability, accommodation and food services has not shown signs of improving, as it also had the greatest dissolution rate of industries in 2014, of 13.1%. The construction industry shows weak performance, in line with other countries, although with higher survivability than the former three industries.

Exhibit 6

Health and Education SMEs Displayed Highest Levels of Survivability



Source: ONS

More exports will benefit UK SMEs

SMEs in the UK underperform at exporting compared to other European countries. One in four EU SMEs have exports,¹⁴ compared with one in ten for the UK¹⁵. Lower exports for UK SMEs compared to other countries in the EU is partially explained by its geography. The UK government is promoting SMEs to start exporting and is aiming to double exporting to GBP1 trillion a year by 2020 and increase the number of companies exporting by 100,000¹⁶. Exporting has been more expensive for UK-based SMEs as a result of the strong GBP/EURO exchange rate. However, the sterling has depreciated in recent months. The sterling depreciation will help firms remain competitive with European trading parties, with 78% of UK SMEs exporting to Europe, compared with only 21% exporting to China¹⁷. The expansion of UK SMEs out of the national market and with less emphasis on Europe and more globally will benefit SMEs' performance going forward.

Positive trend for UK SME ABS transactions given better perspective on construction and building

We currently rate nine UK SME transactions, consisting of Business Mortgage Finance (5), Ascot Black (1) and Sandown Gold (3). Both Sandown Gold and Ascot Black transactions have the largest industrial concentration in construction and building (30-35%). The construction and building sector has shown a contraction of 0.4% in Q4 2015¹⁸ because of poorer performance in private industrial and commercial work types. Despite the decline, survey results indicate growth, with 61% of respondents expecting workloads to increase during 2016, with a forecast increase of 3.4%¹⁹.

BELGIUM

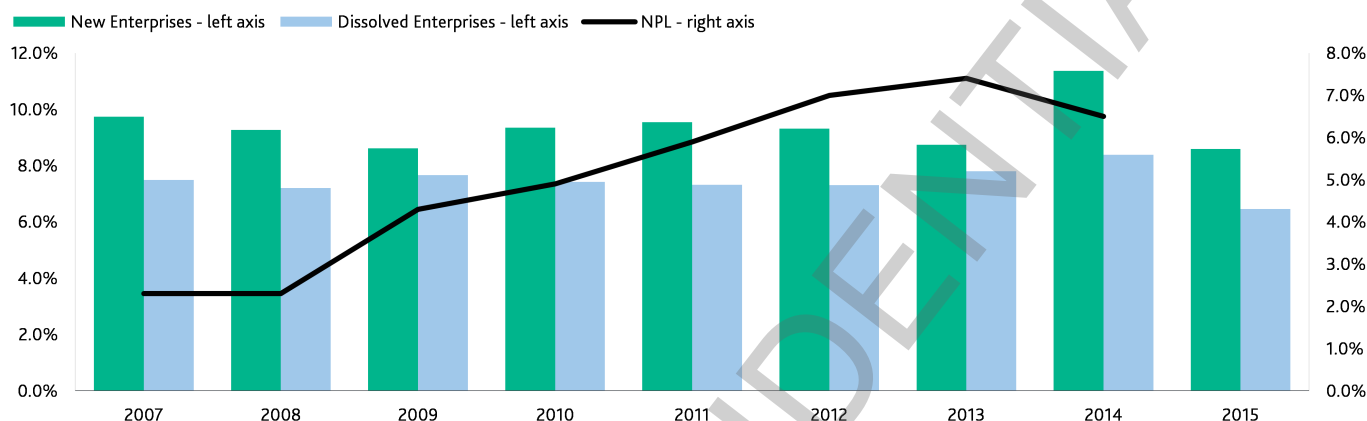
Strong performance will continue, despite the misleading NPL trend

The performance of Belgium SMEs will remain strong, as it was through the global financial crisis. It is a very robust market, with no instance of any year showing negative net growth in SME registrations between 2007-15 (according to the historical series). Although Exhibit 7 shows an increase between 2008-13 in NPLs levels to 7% from 2%, this increase is not a reflection of current Belgium SME performance. Instead, the increase is a result of the reporting including loans granted to enterprises outside of Belgium, given the

global scale of the Belgian banking system²⁰. The first data point reported specifically for Belgium SMEs shows a NPL level of 5.6% as of 2014²¹. Although not directly comparable, this proves the steadiness of Belgium SMEs compared to other countries, with specific information on SME performance as of 2014 (i.e. 18.4% in Portugal or 28.1% in Spain).

Exhibit 7

Constant Pace in SMEs Increase in Belgium in Recent Years



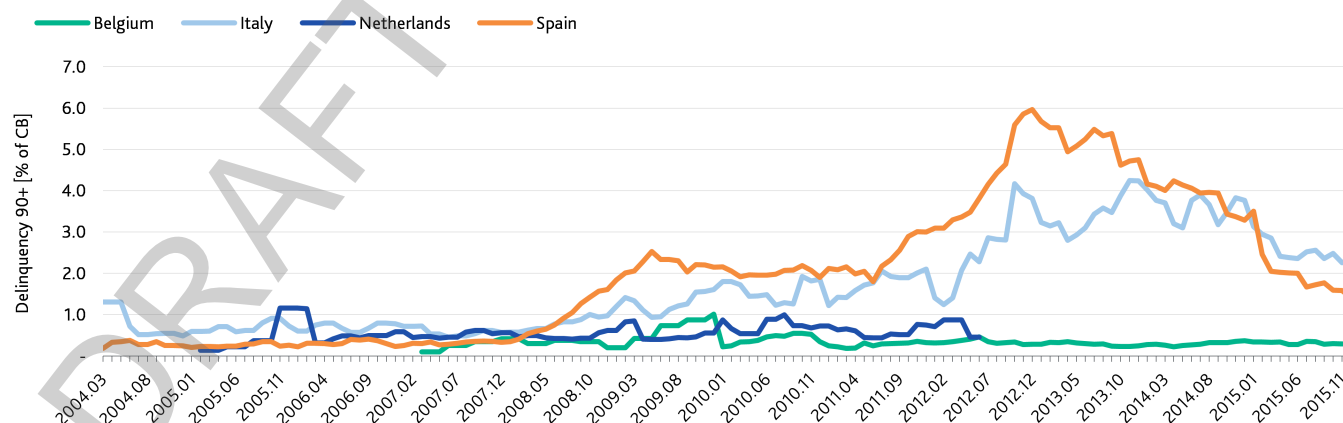
Sources: NBB, Statistics Belgium

The global financial crisis did not hit Belgium SME ABS deals

The SME growth rate in Belgium indicates no change in the strong performance of the deals that we rate. The performance of Belgium SME ABS deals has been very stable through the crisis, with 90+ delinquencies contained below 0.4% as shown in Exhibit 8. The first stage of the crisis affected performance momentarily in 2009, with a short and limited increase that never exceeded 1%. From that moment onward, 90+ delinquencies were back to the low levels at around 0.3%, unlike the deterioration in other ABS SME markets as in Italy or Spain. We have rated six Belgium SME ABS deals since 2007, with three of them still outstanding (Esmee Master Issuer, Mercurius Funding and Belgian Lion SME II), originated by three banks among the top five in Belgium. The volume of these three transactions is in line with the volume of ABS SMEs that we currently rate in Italy and Spain (approximately EUR19 billion in the three countries as of January 2016).

Exhibit 8

Good Performance in Belgium SME ABS Deals Were not Affected by the Crisis



Source: Moody's Investors Service, Moody's Performance Data Service, periodic investor/servicer reports

Belgian SMEs outperform other markets

Belgium is the only market in this study in which the number of SMEs has been growing through the crisis at a constant pace since 2007 without exception, as Exhibit 7 shows, indicating the steadiness of Belgium's business climate. In cumulative terms, 2015 ended with a number of enterprises (almost 420,000) 20% higher than as of 2008, unlike the rest of countries suffering a significant reduction of SMEs by the same period. This is driven by an annual birth rate of around 10% in each year, showing a much more dynamic market for SMEs than the rest of countries in this report. On the other side, dissolution rates have been maintained below 8%, with the lowest level observed as of 2015 (6.5%), even lower than pre-crisis, indicating that the good performance of Belgium SMEs will continue²².

SPAIN

Stronger performance for Spanish SMEs expected in 2016

Improvements in Spanish SME performance that began in 2013 will continue during 2016, although this recovery will stay at a low pace, far from the boosting pre-crisis economy, when two new companies were created as each company dissolved. In general, Spanish SMEs are already benefiting from better financing conditions, which will support better performance.²³

Dissimilar trends by region and industry will determine whether loan performance affects ABS SMEs

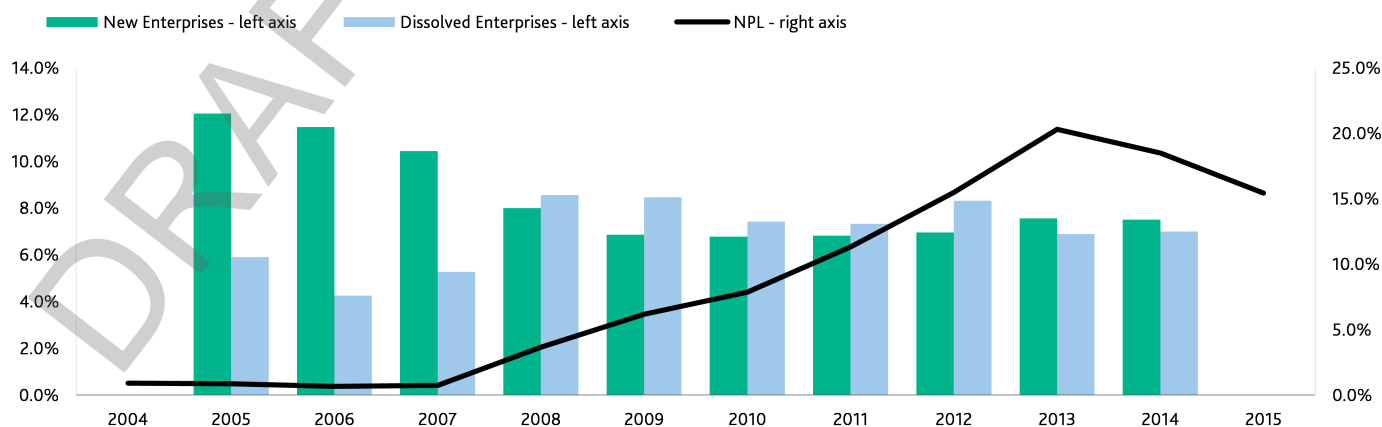
The business climate differs from industry to industry and from region to region. Certain industries are showing a stronger recovery, such as food and beverage, information technology (IT), research and development (R&D) and healthcare. Other industries such as building & construction and textiles are experiencing a weaker recovery. Among the main geographic regions, the number of SMEs increased in Madrid while it continues to decline in Catalonia and Andalusia. As a result, ABS SME transaction performance will depend on the specific characteristics of loans backing each deal.

Positive signs for Spanish SMEs in light of net growth of enterprises

In 2014, the number of new businesses created in Spain exceeded the number of dissolved businesses for a second consecutive year, after five years of negative growth, as Exhibit 9 shows. This trend is credit positive for Spanish SMEs in general and SME ABS securitisations in particular, because it signals an improved business climate that will strengthen the credit quality of the underlying borrowers in the deals. Despite the tighter lending environment in Spain, banks have begun targeting SMEs in an effort to boost profitability, as the recession eases and banks become gradually less risk averse. The weight of Spanish SMEs over the total added value (i.e. gross income from operating activities after adjusting for operating subsidies and indirect taxes) is at 62.8%, above the European Union average. Some factors, such as an exports boom²⁴ and tourism²⁵ were the first elements to pave the way to recovery for SMEs, before household consumption experienced significant growth of 2.4% in 2014²⁶. We have changed our outlook for Spanish ABS SME from stable to positive²⁷.

Exhibit 9

2013 Turning Point for SME Growth in Spain Has Boosted SME Performance



The stock of NPL is affected by real estate loans transferred by banks to the Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria (SAREB), the Spanish bad bank.

Source: Bank of Spain, Spanish National Institute of Statistics (INE)

Turning point to net growth of enterprises in Spain

The net number of Spanish businesses increased by 0.4% in 2014, compared with 0.7% in 2013²⁸, the vast majority of which are SMEs²⁹. The last time there were two consecutive years of net gains in new businesses was in 2006-07, just before the crisis hit the country in 2008. Year-to-date data in 2015 confirms the continued recovery trend. The 94,598 companies created in 2015³⁰ is on par with the 94,158 businesses created in 2014 and the 93,420 businesses created in 2013. The number of dissolved companies has improved year over year, from 24,616 companies in 2013 to 21,874 in 2014 and 20,703 in 2015. However, SME formation still only represents approximately two thirds of the level before the crisis, when about 140,000 new SMEs were created annually³¹.

ITALY

NPLs for SME keep growing, but at a slower pace

Italian SMEs represent 67.3% of the total added value over the national economy, the highest ratio among all countries in this report. Italian SME performance remains relatively weak, with 3.6% of new defaults for micro-enterprises in 2015 (see Exhibit 11), and NPL keeps growing albeit at a slower pace. The 3.6% of new *sofferenze* for micro-enterprises in 2015 (Exhibit 11) compares to 3.9% in 2014, the first decrease in annual growth since 2011. Looking at the NPL stock for NFCs reported by Bank of Italy, the annual increase in 2015 (as of October) of +2.1% compared with +3.5% from October 2013 to October 2014, confirming the slower pace.

New initiative by the government of Italy will assist to reduce the NPL stock

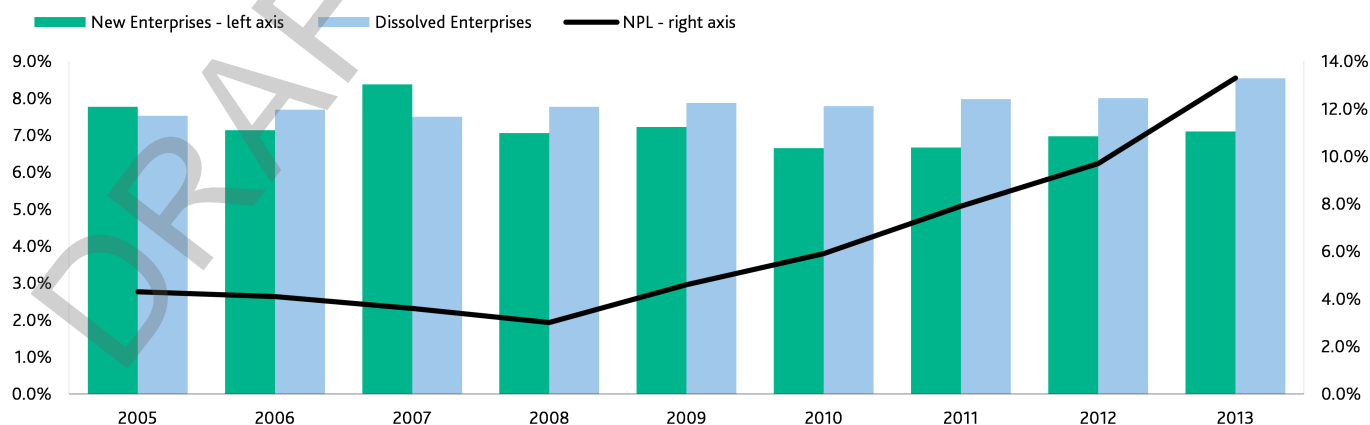
The government of Italy (Baa2 stable) has put forward a plan that aims to resolve the issue of the large amount of bad loans in the banking system³². According to the new plan, Italian banks would be able to securitise their bad loans, subject to certain conditions, and investors in the senior notes would benefit from a government guarantee. The plan will have limited impact in the short term on the reconstitution of banks' balance sheets. However, it gives banks the option to gradually reduce bad loans at somewhat improved values, compared to sales in the market. Bad loans have accumulated since the beginning of the crisis in 2008. This measure will not reduce bad loans significantly this year, but will assist in a gradual reduction.

Business demography does not forecast a significant change in performance for Italian SMEs

There is no net growth in the number of companies in Italy since the 2008 crisis, with the dissolution of companies exceeding the creation of companies by more than one percentage point, as of the latest observation in 2013 (8.5% compared to 7.1%). This is the highest SME failure rate observed across all the countries studied in this report. This is reflected in the fast deterioration of performance for SMEs on a national level, with the NPL stock for NFCs at 13.3% as of 2013, 4x higher than before the crisis. It must be noted that the longer time to write-off bad loans in Italy (*sofferenza*) makes this series not perfectly comparable to other NPL definitions in the rest of countries³³. The negative trend reflects the burden of the crisis on the credit risk for SME loans, in line with the failure rate of SMEs in Italy.

Exhibit 10

No Improvement in Performance for Italian NFCs Until 2013



Source: ISTAT, Banca d'Italia

Performance shows a deterioration in ABS SME transactions, although limited

According to our market index, Italian ABS SME transactions show 90+ arrears of 2.8% as of year-end 2015, compared to 2.3% as of year-end 2014. ³⁴Cumulative defaults increased by 3% in these transactions, in line with the deterioration in performance observed for the national NPL index (from 15.7% in October 2014 to 17.8% in October 2015), and anticipating performance will remain relatively weak for these transactions. However, there are signs that the deterioration in performance has reached its peak and it will be followed by a period of stabilisation. The slower growth in the NPL stock, the lower inflow of new defaults as per Exhibit 11 and overall the stronger GDP growth expected in 2016-17 will support this stabilisation.

No specific divergence in performance per region in Italy

Notably, there is not a significant deviation on this pattern of business demography per region. Although Southern regions present the highest levels of SME failure rates, they are also more active in creating new enterprises; therefore, as a result the path of reduction in enterprises is similar across the country, even slightly better in the South (-0.8% in the South compared to -1.1% in the North and Center as of 2012)³⁵.

SME performance is deteriorating faster than for corporates

The current performance gap between SMEs and corporates is widening if we compare the inflow of new defaults (*sofferenze*) per year before the crisis and currently, from +1.1% in 2007 to +2.0% in 2014-15 (see Exhibit 11).

Exhibit 11

Inflow of New Defaults (Sofferenze) per Year and Enterprise Size

Enterprise Size	2007	2014	2015
Microenterprises	1.70%	3.90%	3.60%
Corporates	0.60%	1.90%	1.60%
Gap	1.10%	2.00%	2.00%

Source: ABI-Cerved

Better performance for ABS SME transactions compared with the national SME loans market

The SME loan and lease ABS segments perform better than the national market of loans granted to SMEs. This is mainly because of the stronger credit quality of ABS portfolios, owing to originators' positive loan selection at closing, repurchases of loans³⁶, as well as the eligibility criteria for these portfolios. Cumulative defaults in Italian ABS SME transactions stand at 8% of original portfolio balance on average as of October 2015, compared to the national NPL stock at 17.8% for the same period.

PORTUGAL

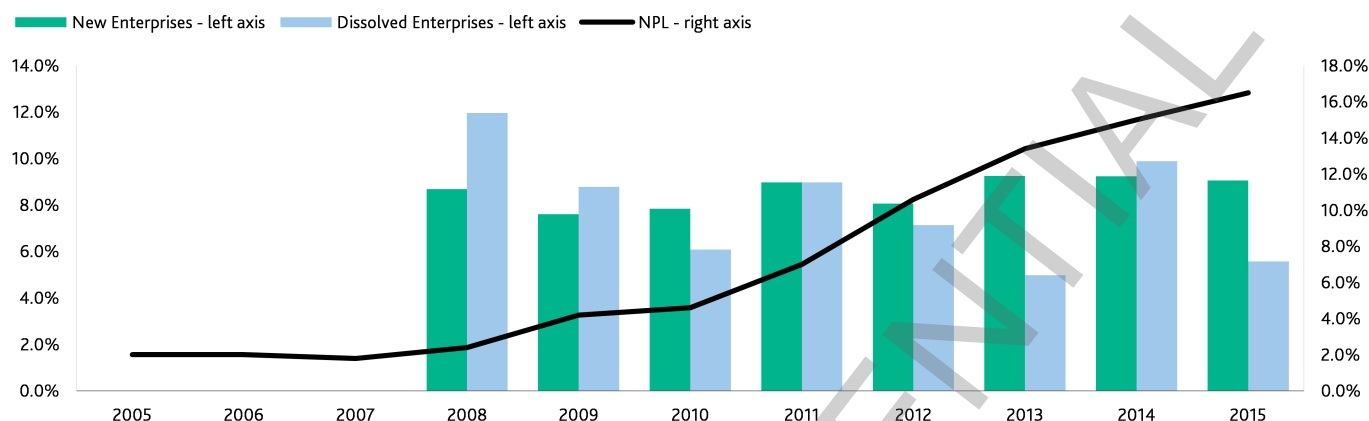
No sign of recovery for Portuguese SMEs in 2016

Portuguese SMEs will continue to show the worst performance across the markets studied in this report. The lowest enterprise survival rate in the EU confirms this: only 25% of micro-enterprises registered in 2008 survived by 2012, less than half the rate in Belgium³⁷. This is especially negative in a country like Portugal, with SMEs representing 67% of total added-value in national economy, compared with 58% in the EU.

Weak correlation between growth in number of enterprises and performance

Portugal shows the weakest correlation between net growth in number of enterprises and SME performance among the markets studied in this report. Exhibit 12 shows how the number of companies³⁸ in Portugal has increased several years since the crisis hit the country for the first time, with no positive effect in NPL levels.

Exhibit 12

Irregular Trend for the Number of Enterprises in Portugal with a Severe Deterioration in Performance

Source: INE Portugal, Banco de Portugal

More enterprise registration in Portugal has not translated into better performance

There is a steady deterioration in the performance of NFCs in Portugal, with no sign of recovery yet. The performance for the NFCs in Portugal has suffered enormously from the effects of the crisis, multiplying by 8 the level of pre-crisis NPLs, to more than 16% in 2015 from 2% in 2007. Focusing on SME performance, the performance is even weaker, showing 18.4% of NPL as of June 2015³⁹. There are different factors that might explain this deterioration, despite the increase in the number of enterprises. First, both the employment and revenues of these enterprises dropped by almost 10% from 2010 to 2013. Second, the statistical series of number of NFCs in Portugal could distort reality, given the changes implemented in both fiscal and reporting rules⁴⁰.

High exposure to building & construction will continue to negatively affect ABS SME performance

Portuguese ABS transactions have high exposures to this specific industry (30%-35%), which will prolong the weak performance of the deals that we rate throughout 2016. Moreover, the recovery in the building & construction sector in the euro area – with an annual increase of 2.1% in production in construction in the euro area in November 2015⁴¹ – compares to the recession for the industry in Portugal, the country with the largest decrease in production in construction (-4.5%).

Chaves SME CLO No. 1, closed in 2006, shows a level of cumulative defaults on original balance close to 8%. We forecast weak performance for Atlantes SME No. 5, given the high percentage of building & construction exposure in the portfolio. Our assumption of cumulative default rate for this transaction, 31.7% of original portfolio balance, reflects the expectation of weak performance.

SMEs perform significantly worse than corporates in Portugal

The crisis has hit the performance of SMEs more severely than for corporates. While NPL levels for corporates and SMEs were not far from 2% before the global financial crisis, now the performance of SMEs is much weaker than for corporates, and the gap is widening. For example, NPL levels for micro-enterprises stood at 24.9% as of June 2015, 5x worse than for corporates (5.0%)⁴². The rest of SMEs (excluding micro-enterprises) also show a high level of NPL (13.9%) compared to corporates.

Portuguese exports are concentrated in corporates and European countries

The top ten exporting companies dominate 20% of national exports⁴³ compared with 16% in Spain. The number of export companies, according to the official definition, remains flat at 5% since 2006. Exports to Spain represent approximately one quarter of total Portuguese exports. Only Spain, France and Germany represent almost 50% of Portuguese exports.

FRANCE**Net growth of number of enterprises is not a strong indicator of SME performance in France**

Net growth of enterprises in France does not provide a strong forward-looking indicator of performance as per other markets. Figures are only available on bankruptcies rather than company deregistration as per other countries in this report, so not directly comparable i.e. there is no record of voluntary dissolutions, the key part of business closures. Since the introduction of the auto-entrepreneur

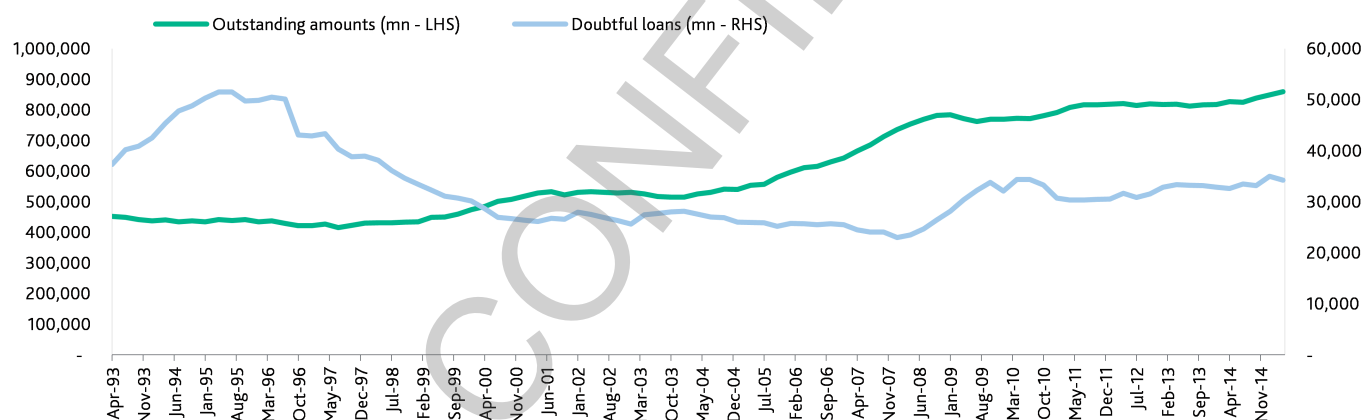
status, the bankruptcy rate is displaying a lower trend and a lower level of volatility. However, the recent trend in French enterprises shows an increase in the number of new business registrations, but still below the levels seen before the change in company status. This might be reflecting businesses failing before reaching the required size to register as an enterprise, which is positive for the SME loan sector owing to reduced bankruptcies.

Stock of loans is growing with stabilising levels of doubtful loans despite dispirited economic environment

The growth rate of loans in France has remained steady despite the slower GDP growth (0.2% in 2014 compared to 2.1% in 2011). France witnessed a quick recovery in supply of loans to NFCs after the 2009 financial crisis, which has contributed to a relatively small dip in the stock of loans, as per Exhibit 13. During this period, bank loans to the SME market kept growing year to year despite the crisis, though some sectors of SMEs, such as agriculture, did suffer a decline⁴⁴. An official NPL ratio is not available for SMEs, but it is possible to use a proxy of the stock of total loans compared to stock of doubtful loans (Créances douteuses) to NFCs. This comparison demonstrates that despite the stock of loans increasing, the levels of doubtful loans to NFCs have remained low and well below the historic peak of €51.5 billion reached in 1995. The value of doubtful loans has stabilised since 2009 in the range of €30 billion - €34 billion. The stock of overall loans has continued to increase which is positive, especially for French growth, as SMEs employ 70% of individuals and provide 57.9% of value added⁴⁵. This increase in stock of loans is positive for French SME ABS deals, as 96% of SMEs who seek finance through an intermediary achieve this through bank loans⁴⁶.

Exhibit 13

The Stock of Doubtful Loans Granted to NFCs has Stabilized since 2012



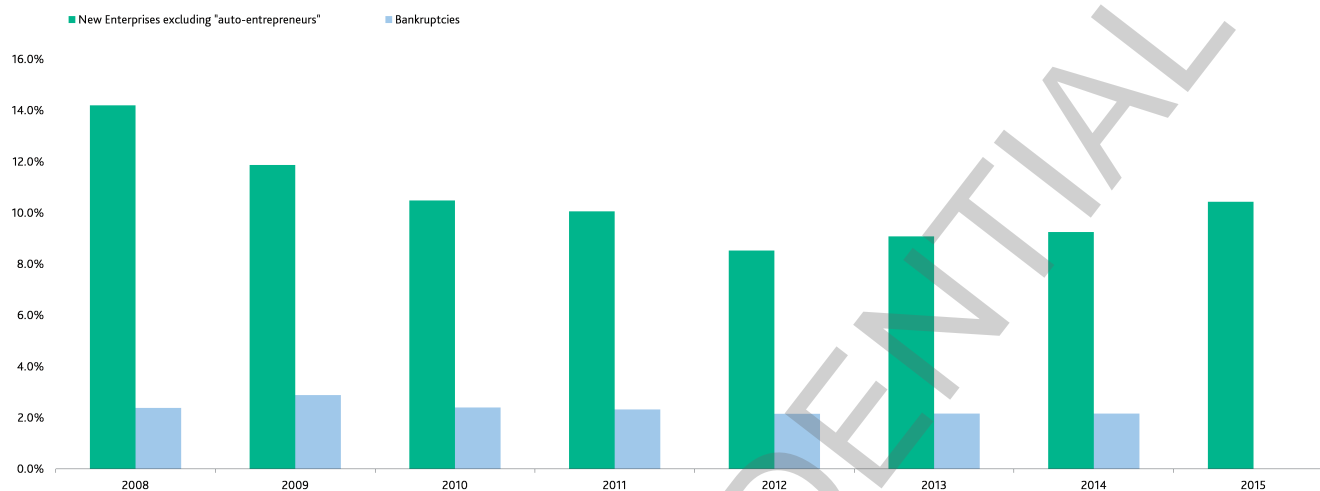
Source: Banque de France

There are three rated French SME transactions, FCT GIAC Obligations Long Terme, FCT GIAC Obligations Long Terme II and FCC GIAC 6. GIAC loans are primarily for agricultural industries, food and consumer goods.

Levels of business registrations are recovering

French SME's represent 99.9% of total French businesses, in line with other countries analysed in this report. France introduced the ability for small businesses led by individuals to register as an auto-entrepreneur instead of as an enterprise in 2009. This new status was low cost, easy to start up and had reduced tax implications for the new firm. The low percentage of deregistrations year-on-year is driven by the data for dissolution not capturing voluntary closures, only bankruptcies

Exhibit 14

Increasing Numbers of New Enterprise Registration

Source: The French National Institute of Statistics and Economic Studies

Moody's Related Research

Sector Comments:

- » [Belgium: Belgian SME Loan Securitisations Are Among the Strongest in Europe](#), February 2016 (1014012)
- » [Europe: Growing Number of SMEs Reflects Spain's Improved Business Environment](#), December 2015 (1010228)
- » [Bad-Loan Plan Using Securitisation Lets Banks Clean-Up Balance Sheets, Albeit With Possible Losses](#), February 2013 (1015768)
- » [High Levels of Repurchased Loans in Italian Lease and SME ABS Transactions Suggest Actual Default Levels Are Higher than Reported, a Credit negative](#), July 2014 (SF374326)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

Endnotes

- 1 There were 1.3 million employer companies as of the end of 2014, 13% higher than the 1.2 million in 2004. This figure excludes small businesses that consist of only the self-employed owner-manager or employee director. Source: Department for Business Innovation and skills.
- 2 The former coalition government committed to achieve 25% of procurement spend to benefit SMEs. See [Central Government Direct and Indirect Spend with SMEs 2013-14](#).
- 3 Source: Eurostat.
- 4 Employer SMEs increased their employment headcount over 2011–15 by 9.5% (a 969,000 increase) compared to 6.5% for corporates (a 626,000 increase).
- 5 Source: EBA.
- 6 Source: Bank of England Quarterly Bulletin Q4 2013.
- 7 BDRC Continental (BDRC) SME Finance Monitor Q4 2015
- 8 Source: Bank of England Credit Conditions Survey Q4 2015.
- 9 BDRC SME Finance Monitor Q4 2015
- 10 The borrowing allowance available for larger institutions is frozen as at end 2015 with availability to drawdown until 2018. New banks will continue to generate new allowances to drawdown over the extension
- 11 Source: BDRC SME Finance Monitor Q4 2015.
- 12 Source: RBS/NatWest Regional Growth Tracker Q2 2015.
- 13 Source: Northern Ireland Composite Economic Index Statistical Bulletin Q3 2015.
- 14 Source: The Confederation of British Industry
- 15 Source: ONS - Annual Business Survey, Exporters and Importers in Great Britain, 2014.
- 16 Source: BIS Performance Indicators - January 2015.
- 17 Source: Western Union International Trade Monitor, April 2015.
- 18 Source: Office of National Statistics.
- 19 Source: Royal Institution of Chartered Surveyors (RICS) UK Construction Market Survey.
- 20 Lending to foreign NFCs accounted for €98 billion in Belgium, representing 45% of the Belgium banking system's total exposure to NFCs, according to the Bank of Belgium (NBB, Annual Report 2015). Only in 2014 did the Bank of Belgium start to report the performance information split by foreign versus national NFCs, and SMEs versus non-SMEs. Loans granted to foreign SMEs show a NPL level of 11.2% as of end of 2014, compared to 5.6% for national SMEs. The NPL series in Exhibit 7, with no split between foreign and national NFCs overestimates the former exposure.
- 21 Source: NBB (National Bank of Belgium).
- 22 See [Belgian SME ABS loan performance will be among Europe's strongest](#), 22 February 2016.
- 23 For more details about the Spanish section, see [Growing Number of SMEs Reflects Spain's Improved Business Environment](#), December 2015.
- 24 See [Moody's Credit Insight Newsletter Highlights Mildly Credit Positive Impact of Spanish Export Boom for SMEs](#), October 2014
- 25 See [Weak Euro and Low Oil Price Will Fuel Continued Tourism Growth, Boosting Spanish SME Transaction Performance](#), February 2015.
- 26 See [Growth In Spanish Household Spending is Credit Positive for ABS SME Performance](#), March 2015.
- 27 See, [2016 Outlook – Credit Quality of European RMBS and ABS Will Improve](#), December 2015.
- 28 Source: Spanish Instituto Nacional de Estadística (INE) - DIRCE, under the definition of sociedad limitada (limited liability company) and sociedad anónima (public limited company).
- 29 According to DIRCE, 99.88% of Spanish companies were SMEs as of 1 January 2014. Hence, we can approximate the trend in the total number of companies to the SME trend.
- 30 Source: INE, Sociedades Mercantiles, Monthly Bulletin.
- 31 Source: INE Spain.
- 32 See [Bad-Loan Plan Using Securitisation Lets Banks Clean-Up Balance Sheets, Albeit With Possible Losses](#), February 2016.
- 33 This is explained by some specificities in Italy, considering both banking and legal systems, i.e. longer time to foreclosure, lengthy insolvency procedures or how Italian banks provision bad debts.
- 34 For transactions closed from 2008 until mid 2014.
- 35 Source: ISTAT.
- 36 See [High Levels of Repurchased Loans in Italian Lease and SME ABS Transactions Suggest Actual Default Levels Are Higher than Reported, a Credit negative](#), July 2014
- 37 Source: Eurostat, Structural Business Statistics.
- 38 99.9% of Portuguese enterprises are SMEs.

³⁹There is no historical series based on official statistics specifically for NPLs on SMEs in Portugal. However, the 18.4% ratio as of June 2015 can be calculated weighting the NPL levels for micro-enterprises and small & medium-sized enterprises as reported in the "Análise setorial das sociedades não financeiras em Portugal 2010-2015" by Bank of Portugal.

⁴⁰In this sense, the revision of business statistics for the 2010-13 period comes from the implementation of ESA 2010 in the Portuguese National Accounts, one result being the changes in the classification of the institutional sector of the entities, thus affecting the delimitation of the business sector. There are also fiscal changes that are affecting the historical series, as the increase in individual enterprises observed in 2013, mostly driven by the obligation of registration of all farmers with business activity. Individual enterprises has been excluded in our analysis.

⁴¹Source: Eurostat.

⁴²Source: "Análise setorial das sociedades não financeiras em Portugal 2010-2015".

⁴³Source: INE Portugal, Instituto de Comercio Exterior (ICEX, Spain).

⁴⁴Banque de France

⁴⁵Eurostat

⁴⁶Banque de France

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