Summary for non-specialists
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Economic Impact of Late Payments

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The importance of trade credits, i.e. sellers accepting payment after the delivery of goods and services, has increased during the economic and financial crisis. Because of the need to restore balance sheets as a result of the financial crisis, the problem of late payments has become more urgent.

Late payments can give rise to tighter financial conditions and lead to increased administrative and financial costs, as external financing may be necessary in order to manage cash flows. Late payments by governments can be particularly damaging for businesses: firms, often credit-constrained SMEs, are involuntarily lending to the authorities. This can give rise to insolvency and ultimately bankruptcy, which means that firms cease to exist or in other words, exit the market each year.

Member States are aware of the harmful consequences that late payments can have on business dynamics and measures have been undertaken recently both at Community level (a new Directive on Late Payments) and country-level. The problem is particularly severe in Greece, Italy, Spain and Portugal, as these countries show the highest delay: 109 in Greece, 90 days in Italy, 75 in Spain and 73 in Portugal, all in 2013 for Government to Business (G2B) transactions.

This paper analyses late payments, both by public and private entities, by computing a proxy for the implicit financial cost it implies to firms and by estimating the effect that late payments have on the exit rate of firms.

The estimated implicit financial costs associated with payment delays by public administrations observed in 2012 ranges from 0.005% of GDP in Finland to 0.19% of GDP in Greece.

The econometric analysis carried out uses annual data for 2005-2010 for 17 EU Member States. Data on late payments, measured as delay over contractual terms, comes from *Intrum Justitia*. The analysis takes into account the economic cycle as well as other possible determinants of exit decisions such as sunk costs associated with investment in a company's workforce. The results confirm the negative effects that late payments have on exit rates, both in the case of payments by public administrations and by the private sector.

The results suggest that the modest improvement observed in late payments delays in Italy and Portugal between 2010 and 2013 have lead to a slight decrease in exit rates. Over the same period, late payments in Spain continued to deteriorate, thus having an adverse effect on firms. What is more encouraging, is the significant potential gains in terms of a reduction of exit rates if countries were to reduce payment delays to zero days.