CREDIT RISK MANAGEMENT: STRATEGIC APPROACHES TO ACCOUNTS RECEIVABLE IN PUBLIC COMPANIES

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Abstract: The article examines strategic approaches to credit risk management related to accounts receivable in public companies. It analyses the theoretical foundations of credit risk, its role in working capital management, and the main methods for assessing clients' creditworthiness. Key tools such as credit policy, factoring, receivables insurance, and the implementation of ERP systems are presented. Particular attention is given to international and European standards for credit risk management, as well as to practical challenges within the Bulgarian context. Based on the analysis, it is concluded that credit risk management should be perceived as a strategic function requiring a comprehensive and integrated approach that combines technology, expertise, and organizational commitment.

Key words: credit risk, accounts receivable, public companies.
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Introduction

In the modern economic and financial environment – characterized by a high degree of instability, increasing competition, and limited access to liquid resources – credit risk management acquires crucial importance for the sustainable operation of public companies. Practice shows that poorly managed accounts receivable can become not only an operational issue but also a factor that undermines overall financial stability and the investment attractiveness of

companies. This determines **the relevance** of the topic and the need to explore strategic approaches to mitigating risks associated with accounts receivable.

The object of this study is *the processes of credit risk management in public companies*, with a focus on their financial policies and organizational practices. **The subject** of the research includes *the strategies, tools and systems through which accounts receivable are managed within the context of the Bulgarian capital market*.

Based on this, the following **research thesis** is formulated: *the effective management of credit risk related to accounts receivable is a strategic factor for the financial sustainability of public companies, which requires the integration of analytical approaches, technological support, and organizational commitment within the systemic and market constraints of the Bulgarian economy.*

The aim of the study is to analyse and systematize effective approaches to managing credit risk arising from accounts receivable, as well as to identify the key problems and challenges in the Bulgarian context.

To achieve this aim the following **objectives** are set: (1) To clarify the theoretical foundations of credit risk and its relationship with working capital management; (2) To examine the main problems, barriers, and managerial deficiencies in the context of Bulgarian public companies; (3) To analyse strategic tools for managing accounts receivable, including credit control systems, factoring, insurance, and ERP solutions.

1. Credit risk and accounts receivable – a review of literature and practice

Credit risk represents the possibility that a counterparty will fail to meet its contractual payment obligations to the enterprise, thereby compromising the normal cash flow and financial stability of the organization. This type of risk is part of the broader category of financial risks and relates directly to the management of accounts receivable – a key component of working capital (Fabozzi, 2010).

Accounts receivable represents the amounts arising from goods or services provided on credit and are typically reported as current assets on the balance sheet (Brigham & Ehrhardt, 2016). From a financial analysis perspective, a high level of accounts receivable may indicate weak collection mechanisms, an ineffective credit policy, or excessive tolerance toward higher-risk clients (Ross, Westerfield, & Jordan, 2019).

The relationship between accounts receivable and credit risk is direct and bidirectional. On one hand, poor receivables management leads to increased

credit risk, while on the other, inadequate risk assessment when extending trade credit results in growing volumes of non-performing receivables (Gitman & Zutter, 2015). Therefore, receivables management should not be viewed merely as an administrative function but rather as **an integral part of the company's risk management and financial strategy**.

At the conceptual level, the academic literature presents various approaches to the classification and measurement of credit risk. According to the Basel Committee on Banking Supervision (2000), credit risk is a key component in assessing capital adequacy and refers to "the loss that would occur if a counterparty failed to fully meet its obligations." Although this definition was initially developed primarily for the banking sector, similar principles can be applied in corporate governance – especially in the case of public companies the operations of which are subject to strict regulatory and market oversight.

Modern methods for assessing credit risk include scoring models, financial analysis of clients, historical payment data, as well as information from credit registries and agencies (Altman & Saunders, 1998). All these approaches aim to minimize the probability of bad debts and to optimize the structure of the receivables of the company.

Within the context of the Bulgarian capital market Todorov (2022), tested eleven models for predicting bankruptcy risk, focusing on thirty-eight public companies included in the broad stock index BGBX40. The author concluded that the applied formula-based methods produced contradictory results, mainly due to the developmental characteristics of the Bulgarian capital market, the specific regulatory framework, and accounting policies that record balance sheet positions in a distinctive manner.

Working capital represents the difference between a company's current assets and current liabilities and plays a critical role in maintaining day-to-day operations. One of the most significant components of working capital is accounts receivable, which directly affect the liquidity, profitability, and financial sustainability of an enterprise (Brigham & Daves, 2021).

When a company provides goods or services on deferred payment terms, it essentially acts as a creditor to its clients. This naturally involves assuming credit risk, which – if not properly identified, assessed, and controlled – can lead to **poor collection performance**, increased impairment expenses on receivables, and even cash flow shortages. Therefore, the effective management of accounts receivable is an essential element of **overall working capital management** and requires a balanced approach between increasing sales and maintaining adequate risk control. (Hill, Kelly, & Highfield, 2010).

The classical models of working capital management – such as the **operating cycle** and the **cash conversion cycle** – emphasize the time dimension of receivables. Longer payment periods may stimulate sales growth, but they

also increase the likelihood of delays and bad debts, particularly among customers with low creditworthiness (Moyer, McGuigan, & Kretlow, 2011).

In this context, **credit risk** becomes a key factor in decision-making related to the extension of trade credit. Implementing a credit policy based on an analysis of counterparties' solvency allows companies to limit potential losses without foregoing attractive market opportunities. For instance, public companies, especially those listed on the stock exchange, are required to maintain a high level of transparency and risk control, since any significant deterioration in asset quality may influence their valuation by investors and regulators (Ross et al., 2019).

Moreover, contemporary corporate practice demonstrates a growing **integration between financial management and risk management**, whereby receivables policy is aligned with the company's overall strategic objectives. This integration includes the use of scoring models, internal credit ratings, customer credit limits, and real-time monitoring of overdue receivables (Gitman & Zutter, 2015).

Thus, credit risk management within the scope of working capital is not merely a defensive mechanism but rather a **strategic tool** for achieving financial efficiency, optimizing cash flows, and ensuring sustainable market presence.

Credit risk management is also subject to a comprehensive regulatory framework at both international and European levels – particularly after the 2008 financial crisis and subsequent economic disruptions. The systemic nature of credit risk has necessitated the introduction of standardized rules for its identification, measurement, and control, applicable not only to financial institutions but also to non-financial corporations, including public companies.

A cornerstone in the global management of credit risk is the Basel framework developed by the Basel Committee on Banking Supervision, which, through its successive accords – Basel I, II, and III - establishes principles for assessing capital adequacy and managing risk (BIS, 2011). Although these standards are primarily intended for the banking sector, they also exert significant influence on the corporate environment by defining the information and credit analysis requirements that banks impose on corporate clients; affecting the terms and conditions of corporate lending; creating internal risk assessment standards increasingly adopted by large public companies.

According to *Basel III*, companies are expected to apply integrated risk management frameworks that include quantitative measurement of *Expected Losses* (EL) through the following parameters: *Probability of Default (PD), Exposure at Default (EAD), and Loss Given Default (LGD).* (BIS, 2011).

Within the European Union, credit risk management is regulated by a series of legislative acts, including Regulation (EU) No. 575/2013 on capital requirements (CRR); Directive 2013/36/EU (CRD IV) on access to the activity

of credit institutions; and the Guidelines of the European Banking Authority (EBA) on risk management, internal control, and governance. Although these norms are formally applicable to banks, they exert an indirect effect on non-financial companies. For instance, credit institutions increasingly require their corporate clients to maintain detailed financial reporting and structured receivables management policies – especially in the context of lending or credit rating assessments.

Public companies, particularly those engaged in cross-border operations or listed on regulated markets, are increasingly adopting internal credit risk management policies inspired by best practices from the banking sector. These include setting internal credit limits and client risk rankings; regular review of trade credit terms; the use of receivables insurance through credit insurers such as Euler Hermes, Coface, and Atradius; and outsourcing debt collection through factoring arrangements or specialized agencies (Altman et al., 2008).

In addition, the adoption of International Financial Reporting Standards like **IFRS 9** requires companies to perform an **expected credit loss assessment of receivables -** even within the non-financial sector. This requirement positions credit risk management at the core of accounting and managerial practice in public companies (IFRS Foundation, 2014).

In a related study, Todorov (2018), examining market risk assessment in the FOREX market, applies several models - VaR, CVaR, MVaR, Historical Simulation VaR, and Delta-Normal VaR - and concludes that these models should be tested in combination to achieve a more comprehensive and reliable evaluation of market risk.

2. Challenges in managing accounts receivable in the Bulgarian context

The management of accounts receivable in Bulgarian public companies faces a number of structural and systemic constraints that hinder the effective implementation of best practices commonly applied in more developed markets. These barriers can be grouped into three main categories: legislative, market, and organizational.

Legislative barriers relate to the fact that some existing regulatory and institutional conditions in Bulgaria create an uncertain legal environment for managing receivables. Key problems include:

- Slow and inefficient judicial procedures for debt collection, both in civil and commercial proceedings, especially when collateral is lacking (Kolev, 2018);

- Inconsistent law enforcement, which makes outcomes of judicial or enforced collection unpredictable;
- Limited access to credit information – although a Central Credit Register exists, it primarily covers the banking sector, and access to intersectoral and corporate client data is limited;
- Lack of incentives for voluntary settlement – legislation does not provide sufficiently effective mechanisms for alternative dispute resolution or voluntary repayment.

Additionally, in Bulgaria, receivables insurance and factoring are underdeveloped, remaining weakly regulated and rarely used in the corporate sector.

Market barriers stem from certain characteristics of the Bulgarian market that challenge sustainable receivables management:

- Weak payment discipline – late payments are often considered "normal" in some sectors, particularly construction, trade, and services (BICA, 2023);
- Competitive pressure and price wars – companies frequently compromise on credit terms to retain clients;
- Low risk management culture – few companies have internal systems for credit scoring and limit-setting;
- Limited liquidity of SMEs – many firms, including suppliers to public companies, rely on delayed payments to finance operations, increasing risk for the receiving company.

Organizational barriers also exist, as many public companies in Bulgaria face operational and structural difficulties internally:

- Lack of specialized credit control departments – the function is often divided between accounting and sales, without a clear responsible unit;
- Insufficient staff training on accounts receivable, credit risk, and creditworthiness assessment;
- Outdated IT systems – many companies still rely on manual data entry, Excel sheets, or accounting software without receivables functionalities;
- Weak interdepartmental integration – poor communication between sales, finance, logistics, and legal departments leads to incomplete or outdated client information.

The combination of these barriers results in increased credit risk, lower collection rates, and higher working capital financing costs. Overcoming these limitations requires both internal restructuring and improvements in the business environment and judicial infrastructure. Enhancing these aspects is crucial for the sustainable development of Bulgarian public companies.

Beyond the objective legislative, market, and organizational barriers, Bulgarian public companies also face several *behavioral and managerial challenges* that affect the efficiency of accounts receivable management. These factors often stem from organizational culture, leadership style, internal control levels, and attitudes toward risk. These include:

- **Tolerance of overdue payments and a "culture of leniency"** – many Bulgarian companies still compromise with clients who pay late, particularly long-term or "strategically important" partners. This reluctance to take stricter action leads to accumulation of structural overdue receivables; distorted revenue recognition and misreported risk; weakened internal financial discipline (Mian, S. L., & Smith, C. W., 1992).
- **Insufficient engagement of top management** – one common problem is the lack of strategic attention to receivables management. Leaders often perceive it as an operational or accounting function, rather than linking it to liquidity, risk, and returns. Consequently, resources for credit control systems are insufficient; comprehensive trade credit policies are absent; regular analysis of collection rates and client risk profiles is not conducted.
- **Conflict between commercial and financial interests** – sales teams are frequently incentivized to increase sales without considering client creditworthiness, leading to high-risk deals aimed solely at meeting sales targets. This creates tension between commercial and finance departments and a lack of coordination regarding acceptable risk levels, credit limits, and payment terms. Such conflicts can be mitigated through interdepartmental policies, including joint approval of new clients or automatic blocks when limits are exceeded.
- **Limited expertise and lack of training** – many companies lack trained credit risk specialists, and finance teams do not have the necessary analytical tools. This results in subjective, intuition-based client assessments rather than data-driven approaches, poor identification of early warning signals, and delayed response to deteriorating collections.
- **Absence of standardized internal processes** – unregulated or informal procedures lead to inconsistencies in policy implementation, such as varying approaches to clients depending on the employee, inconsistent payment terms, and lack of a centralized database for credit history, payments, and receivables.

Behavioural and managerial factors are key to understanding weaknesses in receivables management. Addressing them requires not only technological and legal changes but also cultural transformation, leadership, and

training. Only with clearly defined responsibilities, interdepartmental coor-ination, and top management commitment can real reductions in credit risk be achieved.

3. Strategic approaches to accounts receivable management

Successful management of accounts receivable requires the implement-tation of well-defined and strategically oriented credit policies. These policies provide the framework within which an organization establishes rules, proce-dures, and criteria for extending trade credit to its customers. At the same time, they serve as a tool for controlling credit risk and maintaining the company's financial sustainability (Gitman, L. & Zutter, C., 2015). As noted by (Radukanov, 2017), „economic entities operate in a complex and dynamic environment ", which necessitates the application of adaptive strategies in managing financial risk.

The primary goal of a credit policy is to **balance the increase of sales with the control of default risk**. An overly liberal credit policy may boost revenue but also worsen collection performance, whereas an excessively restrictive approach may limit market share and result in customer loss (Brigham, E. & Ehrhardt, M., 2016). Therefore, the key lies in adapting the policy based on the type of customers (e.g., corporate, institutional, retail); industry sector; economic conditions; and the company's internal liquidity position.

A well-designed credit policy typically includes the following elements:

1. Creditworthiness assessment criteria – This involves analyzing the customer's financial statements, credit history, market reputation, credit rating, and past transaction behavior (Hill, N., Kelly, G., & Highfield, M., 2010). Assessing solvency is a critical element of accounts receivable management and forms the basis for informed decisions on extending trade credit. The goal is to evaluate *the likelihood that a client will meet their obligations on time*, thereby minimizing the risk of bad debts and losses. Public companies often manage large and diverse client portfolios, which requires a systematic approach to risk analysis. Proper solvency assessment enables optimal determination of payment terms (deadlines, advances, limits); early identification of high-risk clients; improved collection performance; and protection of cash flows and profitability (Gitman, L. & Zutter, C., 2015).

There are two main approaches to analysis: quantitative (financial) and qualitative (behavioural) (Михайлов, Ем., Вътев, Ж., Асенова, М.,Божинов, Б., Кръстев, Б., Георгиев, Г., 2003). The **quantitative approach** includes analysis of financial indicators extracted from the client's accounting records –

for example: current ratio (*current assets/current liabilities*), debt-to-equity ratio, days sales outstanding (DSO), and interest coverage ratio. These financial data are compared against sector benchmarks to produce an objective evaluation (Hill et al., 2010). The **qualitative analysis** examines non-financial factors, such as payment history (timeliness of previous transactions); reputation and corporate structure (management stability, involvement in public scandals, bankruptcies); legal risks (pending lawsuits, insolvency of related entities); and external factors (market conditions, regulatory changes, political risk).

Public companies increasingly use external information sources, including credit bureaus and agencies (e.g. Experian, Dun & Bradstreet); rating agencies (Fitch, Moody's, Standard & Poor's); public registries (Commercial Register, insolvency databases).

In the context of digitalization and the need for rapid assessment, many companies use scoring models and automated platforms for risk classification. Commonly used criteria combine financial indicators, past credit behavior, and machine learning algorithms that detect risk patterns in real time (Altman et al., 2008). Based on the analysis, individual credit profiles are developed, and parameters such as the following are determined: credit limits; payment terms; requirements for collateral or advance payments; need for receivables insurance.

Companies that systematically analyze solvency can minimize their exposure to insolvent clients and improve their liquidity position and capital turnover.

2. Determination of credit limits – This involves establishing the maximum allowable volume of receivables from a particular client or group of related clients. Credit limits are set according to the assessed level of risk, the client's financial position, and the volume of transactions. The credit-limiting policy forms the foundation of active risk management. In addition to internal limits, companies often employ complementary mechanisms, such as *credit insurance* (transferring credit risk to specialized insurers – e.g. Coface, Euler Hermes); *factoring and forfaiting* (assigning receivables to third parties); *pledges and collateral instruments* (securing trade credit through contractual guarantees, avals, mortgages, etc.). Companies that maintain a proactive approach to credit and limit-setting policies are able not only to reduce losses from overdue receivables but also to enhance the quality of their client portfolio, liquidity, and return on assets *(ROA)* (Hill, N., Kelly, G., & Highfield, M., 2010).

3. Payment terms – These include the repayment periods, opportunities for discounts in cases of early payment, and penalty interest rates applied in the event of delays.

4. Approval procedures – the approval hierarchy for different credit limits, the division of responsibilities between the sales and finance departments. In publicly listed companies, credit and limit-setting policies are usually formalized in separate *internal regulations and procedures*, subject to internal audit oversight and, when necessary, reporting to the board of directors.

5. Control and revision mechanisms – regular monitoring of overdue accounts, revision of limits when risk conditions change, and automatic alerts when limits are exceeded (Moyer, R., McGuigan, J., & Kretlow, W., 2011). The dynamic environment in which modern public companies operate requires flexible credit policies that can be adapted according to the overall economic environment (e.g., inflation, recession); the level of uncollectible receivables in the sector; regulatory changes (e.g., provisioning obligations under IFRS 9).

In an era of increasing business process complexity and high financial flow dynamics, public companies increasingly rely on **integrated software solutions** for managing accounts receivable. The implementation of Enterprise Resource Planning (ERP) systems and specialized receivables management modules has become a strategic tool for ensuring control, traceability, and prevention of credit risk.

The automation of receivables management processes leads to substantial improvements in several key areas:

- Comprehensive control over receivables – real-time tracking of obligations, deadlines, and inflows;
- Timely risk identification – automatic alerts for overdue payments, limit breaches, or negative trends;
- Shortening of the collection cycle – automated notifications to clients, issuance of reminders, invoices, and collection letters;
- Enhanced reporting accuracy – detailed analytics by clients, regions, sectors, and time periods;
- Greater operational efficiency – elimination of manual processing, reduction of errors, and optimization of resource utilization.

Systematic automation enables companies to **transition from a reactive to a proactive model of risk management**, providing timely information for decision-making and preventing the accumulation of non-performing receivables (Вътев, 2010*).*

ERP platforms integrate all core business functions within a unified environment — finance, sales, procurement, accounting, and customer management. In the context of accounts receivable management, the most commonly used modules include *Accounts Receivable (AR)* (management of invoicing, payments, and account balances); *Credit Management* (setting of credit limits, payment terms, and scoring profiles); *Collections Management*

(automated receivables collection processes); *Customer Relationship Management (CRM)* (monitoring of client interactions and transaction history).

Leading ERP systems such as *SAP, Oracle NetSuite, Microsoft Dynamics 365,* and *Infor* provide comprehensive functionality for receivables management, tailored to the needs of large public corporations. Some of these systems also allow integration with external credit bureaus, factoring platforms, accounting systems, and banking services, thereby expanding analytical and control capabilities

Contemporary ERP systems increasingly incorporate **artificial intelligence (AI)** and **machine learning (ML)** technologies to predict client behavior and identify emerging risks. These technologies enable: forecasting of delinquency probabilities; risk-based client classification; personalization of credit terms based on client profiles; optimization of collection efficiency through automated action planning.

According to a PwC (2022) study, more than 60% of large European companies already employ **AI-based solutions** for receivables management, resulting in a 20–30% average reduction in non-performing receivables.

The adoption of ERP solutions is not without challenges. Key difficulties include high initial costs related to software, hardware, and employee training; the need to restructure internal processes; employee resistance and the necessity for cultural change; ongoing maintenance, adaptation to local regulations, and tax compliance. Nevertheless, the long-term advantages far outweigh the initial investments, particularly when ERP systems are aligned with the corporate strategy for working capital and credit risk management.

In addition to internal policies and systems, public companies increasingly rely on **external financial instruments and partnerships** to optimize risk exposure, liquidity, and operational efficiency. Among the most widely used mechanisms are factoring, trade credit insurance, and outsourcing of collection processes.

Factoring is a financial mechanism whereby a company transfers its receivables to a specialized financial institution (a factor), which advances part of the invoice value and assumes responsibility for collecting client payments. Factoring arrangements may be with recourse (regressive): where the seller retains the credit risk; and without recourse (non-recourse): where the factor assumes full risk of non-payment. The primary benefits of factoring in the context of receivables management include immediate release of working capital; improved liquidity and cash flow; reduced administrative burden associated with collections; potential anonymity from the client (depending on the factoring type). Factoring is especially prevalent in industries characterized by high sales volumes with deferred payment terms, such as manufacturing, distribution, and logistics (Soufani, 2002).

Trade credit insurance offers protection against the risk of non-payment due to insolvency, bankruptcy, or political events. The insurance company covers a set percentage of the losses (typically 80-90%) when the risk conditions are met. The benefits for public companies include mitigating credit risk, enhancing trust from investors and shareholders, improving financing conditions, especially when dealing with banks, and enabling bolder expansion into new markets and customer bases. Leading companies in Bulgaria's market for this type of insurance include Coface, Atradius, and Euler Hermes, which collaborate with international clients and provide risk assessments by country, sector, and company (Atradius, 2023).

Outsourcing refers to delegating the receivables collection process to an external company (a collection agency). This practice is mainly used in cases of chronic late payments, numerous small debts, or situations where direct communication with the client is either undesirable or ineffective. The advantages of outsourcing include freeing up internal resources, improving collection rates through professional methods, reducing tension in customer relationships, and applying additional pressure through legal or judicial measures (if necessary). However, it is crucial to select reputable agencies and ensure they adhere to ethical and legal standards.

Other external tools for managing credit risk in trade receivables include **receivables securisation** (turning receivables into tradable securities, which are then sold to investors); **fintech platforms** (leveraging digital channels for credit scoring, online factoring, and receivables collection); **legal protection and legal counsel** (for contracts, penalties, and legal proceedings against difficult debtors).

Conclusion

Managing credit risk related to accounts receivable is an integral part of financial stability and strategic management for publicly listed companies. In today's dynamic economic environment - marked by increased uncertainty, inflationary pressure, and shifting regulatory conditions - the ability of companies to identify, assess, and limit their exposure to high-risk clients is becoming increasingly critical.

However, an analysis of the Bulgarian context reveals several legislative, market, and managerial barriers that hinder the implementation of best practices. Notable among these are inefficient judicial procedures, weak payment discipline, and organizational inertia. Overcoming these challenges requires not only a transformation of the regulatory and institutional framework but also a shift in the internal organizational culture of companies.

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