Business support must now facilitate the recovery from COVID-19

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These are extraordinary times. Governments have shown through their unprecedented policy actions that they will do whatever it takes to support companies and workers through the COVID-19-induced lockdowns. The OECD COVID-19 Policy Tracker (OECD, 2020a) reports that massive credit supply, cash grants and tax deferrals provided unprecedented liquidity support for businesses. These policies have helped firms weather the sharp drop in demand resulting from the pandemic, and short-time work schemes allowed firms to maintain existing employment relationships to enable them to return fast to full production (OECD, 2020b). Without the extensive policy responses governments have swiftly put in place, nearly one in three companies would have faced liquidity shortfalls during lockdowns, and many otherwise viable firms would now be bankrupt (OECD, 2020c). But these measures came at the price of higher public and corporate indebtedness, may have kept unviable firms artificially alive, and may have increased the scope for lobbying and capture by sectoral interests.

As many countries are entering a new phase of re-opening, economic revival and rebuilding, under continued caution over health risks, governments will need to adjust life support to businesses. Loans and guarantees should be scaled back in favour of policies that help kick-start the economy and at the same time tackle long-term challenges such as climate change and digitalization. As some sectors will see persistently low

demand, it is crucial that policies facilitate structural change. Several countries have already started to lay the ground for the recovery.

Policy support kept companies alive during the initial COVID-19 crisis

The COVID-19 shock has led governments and central banks to implement unprecedented measures to keep existing companies alive. They deployed extraordinary lending support in the form of loans and loan guarantees for struggling businesses in response to strict containment measures put in place to contain the impact of the pandemic (OECD, 2020d). For example, Germany has announced EUR 756 billion (22% of GDP) in public sector loans and guarantees in addition to unlimited credit supply by the national development bank KfW, followed by Italy (17% of GDP) and the United Kingdom (15%). The headline figures are upper limits, while the effective uptake of funds is often much lower (Figure 1). Nevertheless, targeted lending support came at massive fiscal costs and brings with it the risk of lobbying by big firms and capture by political powerful sectors. This bias remains even in countries coupling state support with a ban on dividend payments and share-buybacks, and excluding firms domiciled in tax havens.

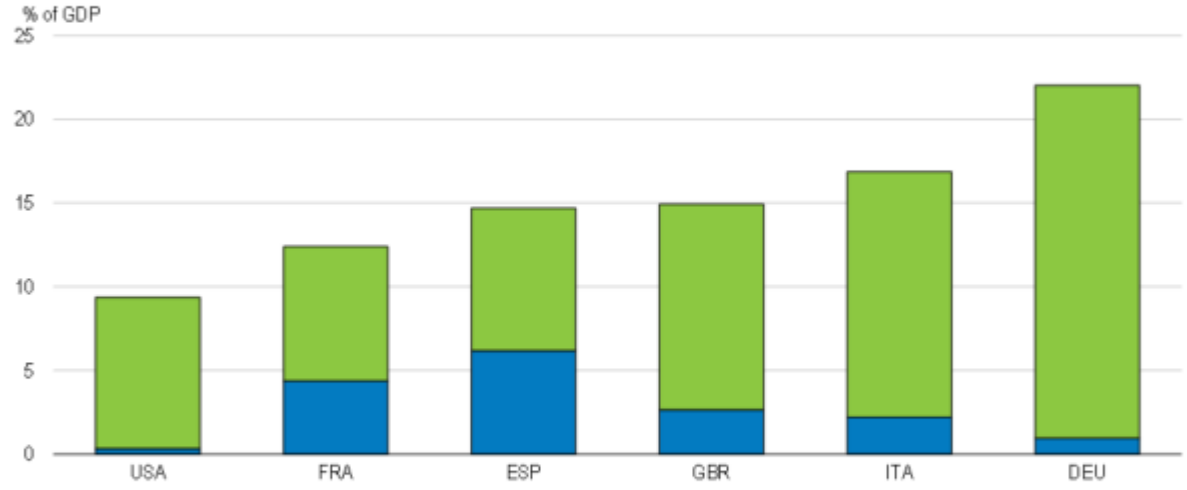
- Central banks provided massive liquidity injections to maintain credit supply to solvent firms, averting short-term liquidity issues from toppling otherwise healthy firms, and reducing the tail-risk of cascading failures from the insolvency of interconnected firms (Banque de France, 2020; Barnes et al., forthcoming). Five central banks have extended temporary liquidity facilities and started to directly purchase new classes of corporate bonds, including the Bank of England, the Bank of Japan, and the US Federal Reserve (OECD, 2020d).
- SMEs are suffering most from the crisis because they have less cash reserves to weather the drop in demand.

Several countries have programmes targeting SMEs, including equity funding and convertible loans for tech start-ups in France, Germany and the United Kingdom. Governments also improved access of capital-weak SMEs to existing loan schemes by temporarily easing co-financing requirements, as in Israel, the Netherlands and the United Kingdom.

- Governments' actions were also a response to falling global demand. At least 11 countries extended export credit guarantees to help stabilise demand in the wake of the disruption. For instance, the Swedish Export Credit Agency's loan limit was extended to SEK 200 billion (about 3.8% of GDP) with a higher ceiling for guarantees for export credits.

Figure 1. Headline envelopes versus actual uptake of public loans to businesses

Envelopes for public loans and guarantees (in green) and credit commitments (in blue) (% of GDP)



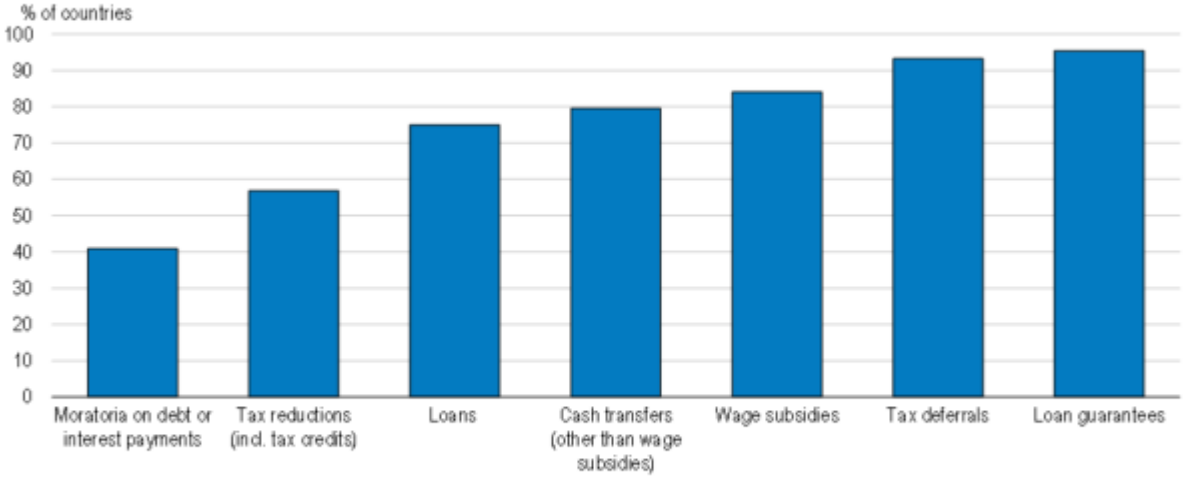
Note: Amounts show announced envelopes for public loans and guarantees and actual credit commitments to businesses (% of GDP) in selected advanced economies as of week of 22 June.
Source: OECD COVID-19 Policy Tracker (2020) https://www.oecd.org/coronavirus/country-policy-tracker/; Brookings (2020) https://www.brookings.edu/research/fed-response-to-covid19; and Bruegel (2020) https://www.bruegel.org/2020/07/government-guaranteed-bank-lending-beyond-the-headline-numbers.

Tax deferrals and cash support to foot companies' wage bills and avoid permanent lay-offs provided additional liquidity at a time when many businesses saw a sharp drop in revenues due to the pandemic (Figure 2). They prevented the break-up of existing relationships between firms and their employees, ultimately laying the ground for a quicker recovery. However,

their design often risks opportunistic behaviour by firms and unnecessarily restricts activity in sectors that remained open.

- Tax deferrals were a common measure to alleviate pressures on cash-strapped businesses, with 41 of 43 countries having deferred tax payments at least until the end of June, often until the end of 2020.
- Short-time work programmes, furloughing schemes and administrative measures to limit dismissals helped businesses stem their wage bill and preserve existing jobs. These schemes helped to dampen the hit to firms' short-term liquidity (OECD, 2020c), but they may also hinder the transition of workers from unviable jobs to firms with better medium-term growth prospects (OECD, 2020d). In some countries, firms cannot flexibly reduce their workers' hours as needed and keep some workers employed on a part-time basis, and generous replacement rates risk opportunistic behaviour by firms in sectors where confinement restrictions are lifted or where workers work remotely.
- 35 out of 43 countries have used cash grants in addition to wage subsidies covering the hardest hit sectors, notably hospitality and tourism. In the Netherlands, for instance, firms that needed to close due to the coronavirus can receive a one-off lump sum allowance of EUR 4 000.
- Another 18 of 43 countries introduced loan repayment moratoria and loan-maturity extensions to roll over their existing debt. In Hungary, for example, a 3 600 HUF billion (7.7% of GDP) moratorium on loan payments and interest offers debt relief until the end of 2020.

Figure 2. Frequency of business support measures during the initial phase of the COVID-19 crisis



Note: Non-OECD countries include Brazil, China, India, Indonesia and South Africa.
Source: OECD COVID-19 Policy Tracker (2020) https://www.oecd.org/coronavirus/country-policy-tracker/, and national sources.

Policy now needs to focus on supporting demand for a sustained recovery

Moving forward, a new set of policies needs to replace life support to businesses. Policy should continue to support demand until the recovery has taken hold. Loans and guarantees should be scaled back in favour of fiscal policies that help kick-start the economy and structural policies that tackle long-term challenges such as climate change and digitalization. As some sectors will see persistently low demand, it is crucial that policies facilitate structural change.

A number of countries have already announced fiscal packages that give priority to private investment and public spending with presumably high multipliers. These packages could inform those currently in preparation in other countries.

- Governments should prepare public investment plans that can be implemented swiftly in the recovery phase. Public investment in widely accessible digital infrastructure is important to ensure that businesses can reap the full benefits of digitalisation, and improved e-government

can reduce the administrative burden for businesses. Among those countries emerging from the immediate health crisis, nine countries have announced public investment in digitalisation. An important component is the frontloading of the rollout of 5G infrastructure, as announced in China, Germany, Japan, Korea, and the United Kingdom. Parts of the German and Korean recovery packages aim to improve e-government services.

- Streamlining planning regulations could help boost public investment during the recovery. In the United Kingdom, for example, the government announced a reform of the planning system to accelerate construction of public housing, hospitals and infrastructure.
- Eleven governments provide additional tax relief measures for businesses to help spur private investment. For instance, Austria and Germany are extending the loss carry-back and extend depreciation allowances for the years 2020 and 2021.
- Countries have also announced investment in the green transition to help put the recovery on a more sustainable footing by reducing CO2 emissions. The Korean government announced KRW 73.4 trillion (3.8% of 2020 GDP until 2025) of investment into renewable energy technologies and smart grids to raise energy efficiency.
- Governments should take advantage of the ongoing digitalisation wave in response to the pandemic (OECD, 2020e) and support private investment of lagging firms to boost overall productivity. Korea, for instance, is bringing forward parts of its KRW 58.2 trillion (3% of 2019 GDP until 2025) investment plans for digitalisation (in so-called “New Deal” projects), while Japan supports the digitalisation of SMEs with JPY 0.9 trillion (0.2% of GDP).
- Some countries have put in place measures to facilitate a fast resolution of insolvent firms, either through streamlined debt resolution or debt forgiveness (OECD, 2020d). The Netherlands, for instance, improved a

dispute resolution mechanism as an alternative to bankruptcy.

- Temporary VAT cuts as in Austria, Germany, or the United Kingdom could bring forward consumption spending, but they are often difficult to revert once the situation normalises. Furthermore, there are more transparent and effective instruments to support struggling sectors.

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