FISCAL AFFAIRS

Rethinking Support to Firms: Lessons from COVID-19

MAY 31, 2023

PIIE, “Rethinking Fiscal Policy – Global Perspectives”

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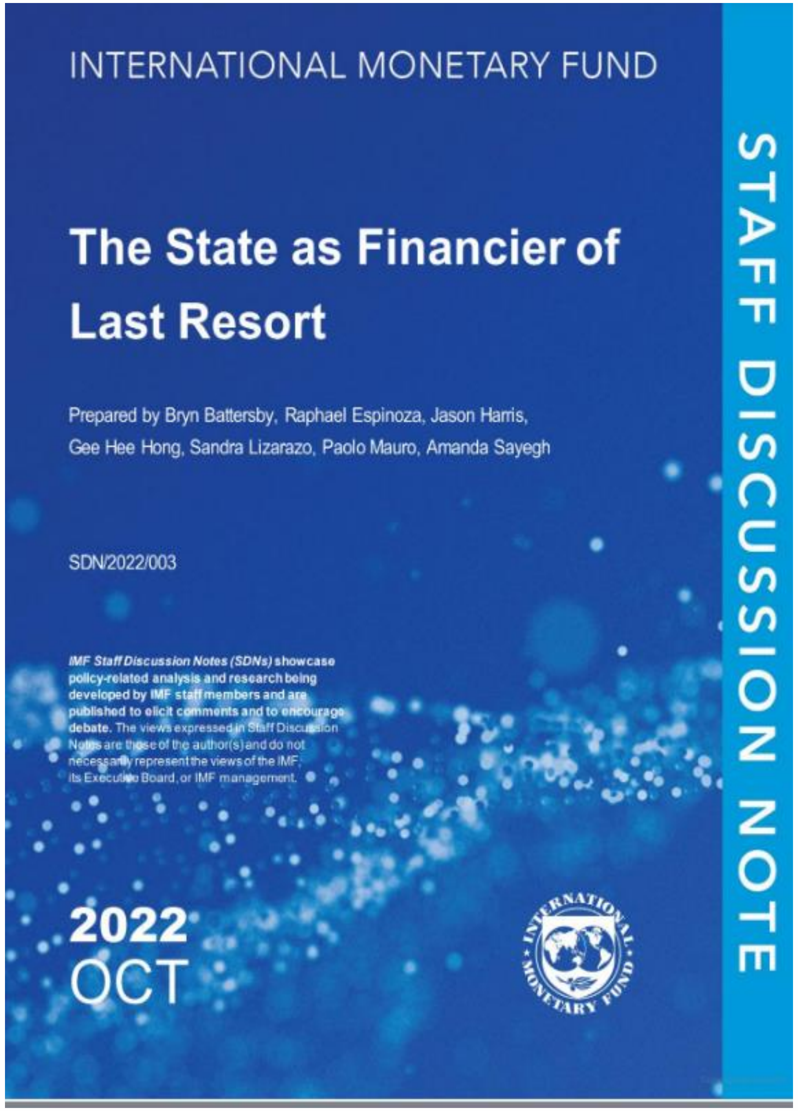
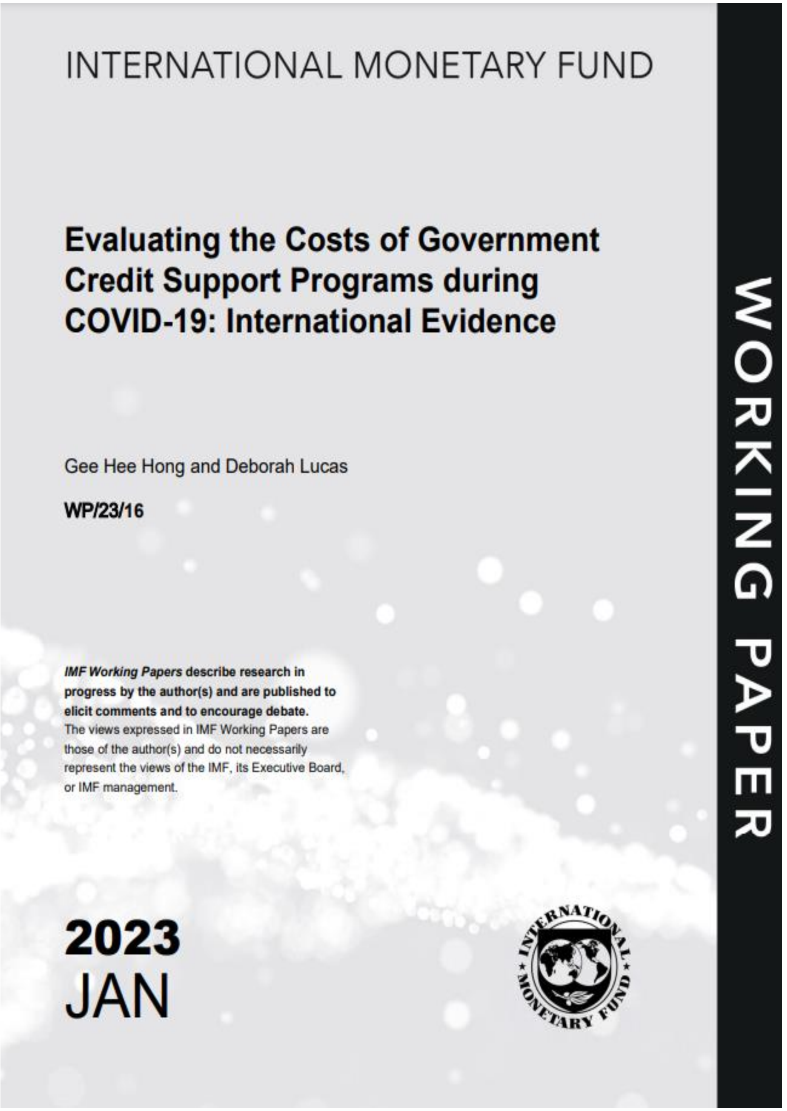
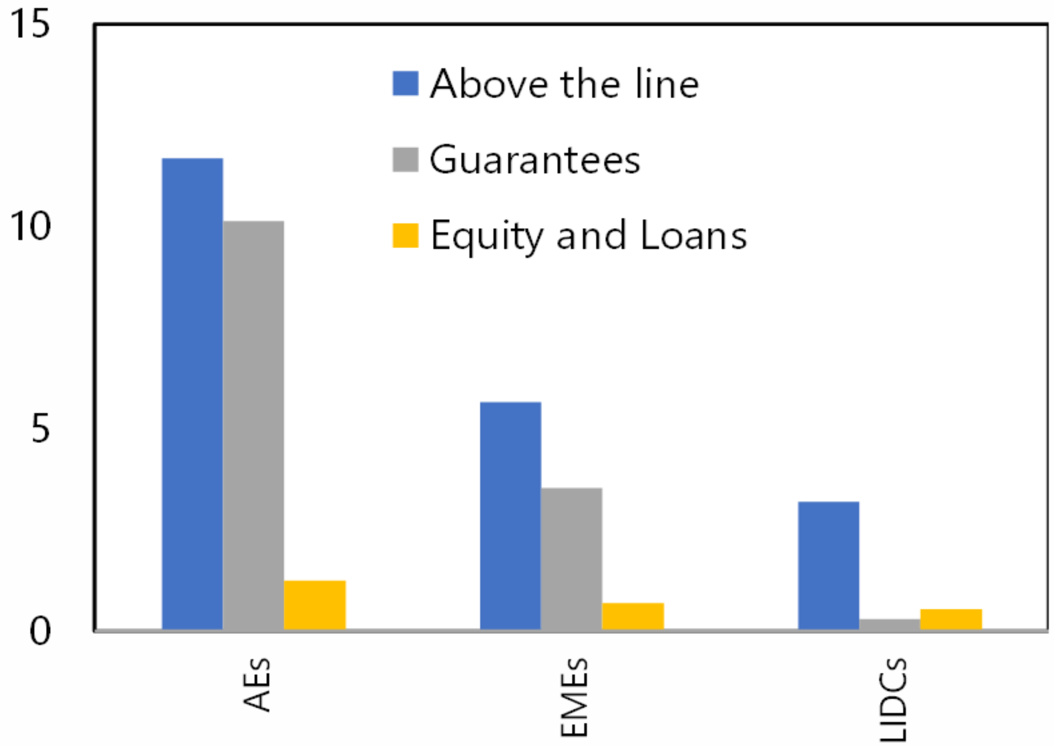
Related IMF Works





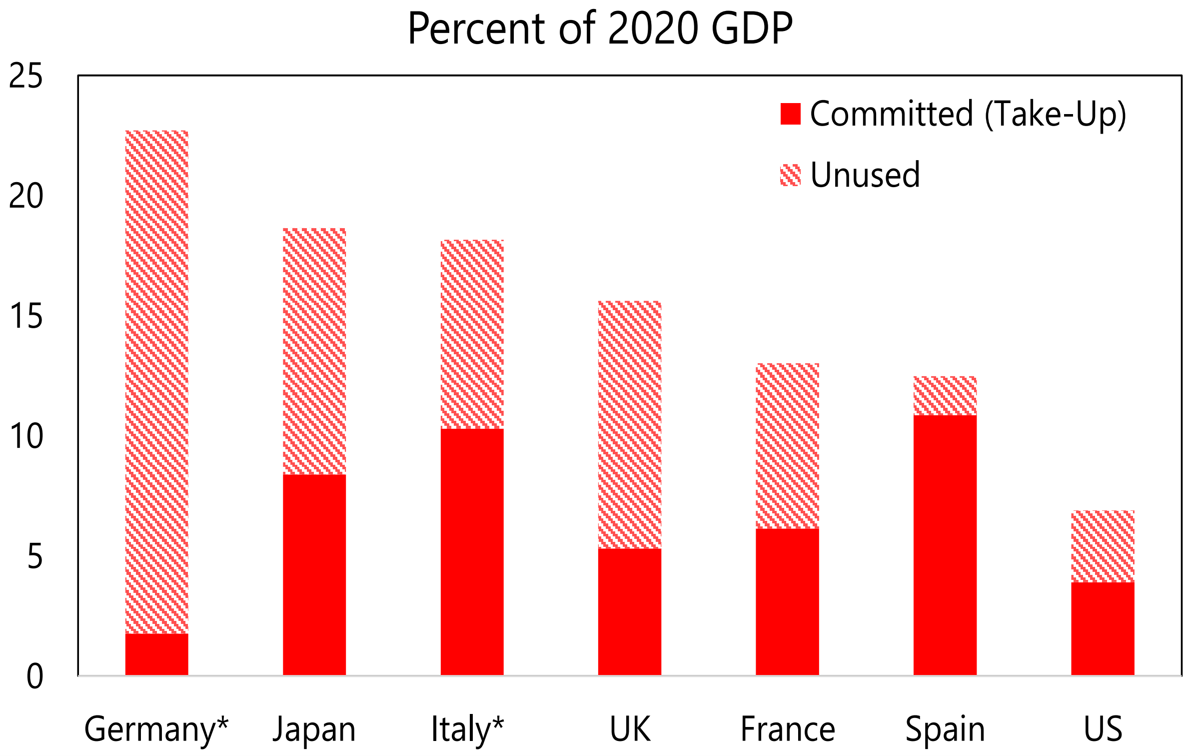
During COVID, governments relied heavily on credit policies to support firms

Announced Measures in response to COVID-19, average by country group
(Percent of GDP)



Source: IMF Fiscal Monitor Database of Country Fiscal Measures in Response to the COVID-19 Pandemic; Battersby et al. (2022).

Credit Programs during COVID-19: Committed vs. Unused Envelope



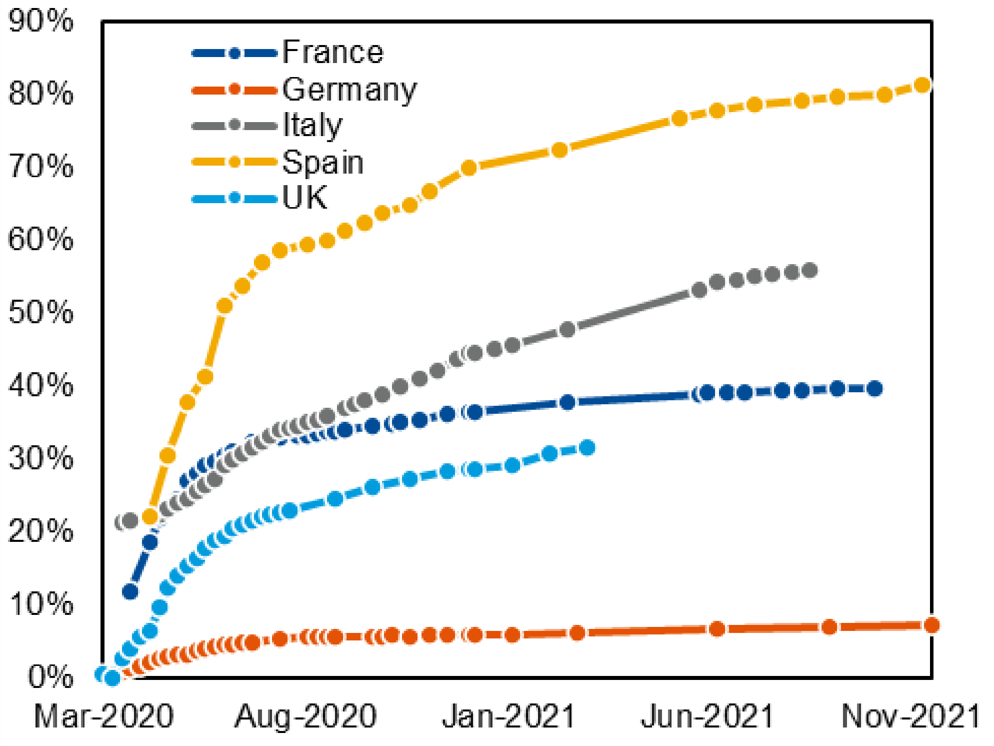
Source: Hong and Lucas (2023)
Note: Some guarantee programs announced by Germany and Italy have uncapped legal limits to provide funds. The bars shown in the Figure show the cap on total guarantees provided by the government, rather than the actual injections to the guarantee funds.

How to think about credit policies vis-à-vis traditional fiscal policies

	Traditional Fiscal Policies (Transfers, tax cuts, etc)	Credit Policies (Guarantees, forbearance, etc)
Advantages	• Greater **transparency** • Better at targeting • Discipline of budgetary process	• **Low-cost** stabilization tool when credit markets are disrupted, and uncertainty is high • "Some skin in the game" helps screen out those not needing help • Quick relief with little bureaucracy (i.e., forbearance policies)
Disadvantages	Relatively high cost	• **Lack of transparency** • Long-horizon fiscal risks • Default costs to borrowers and government

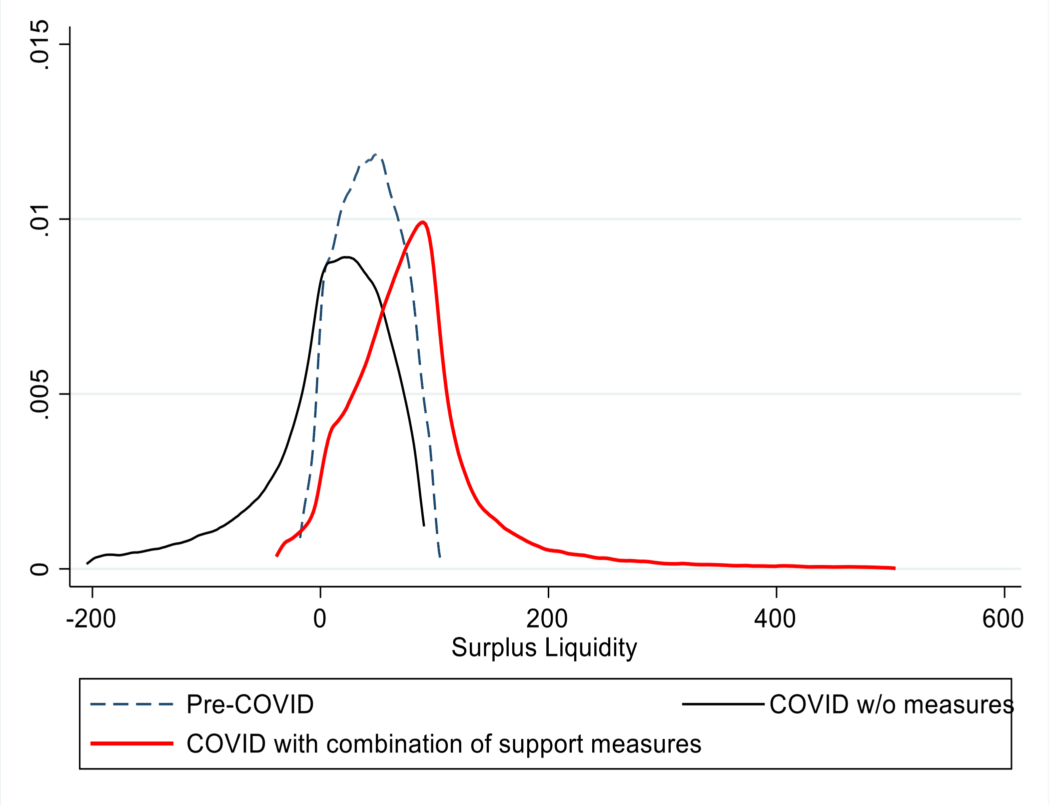
Credit policies averted bankruptcies and shielded firms against "liquidity shocks"

Cumulative take-up of credit support schemes
(Percent of announced envelope)



Source: Battersby et al. (2022)

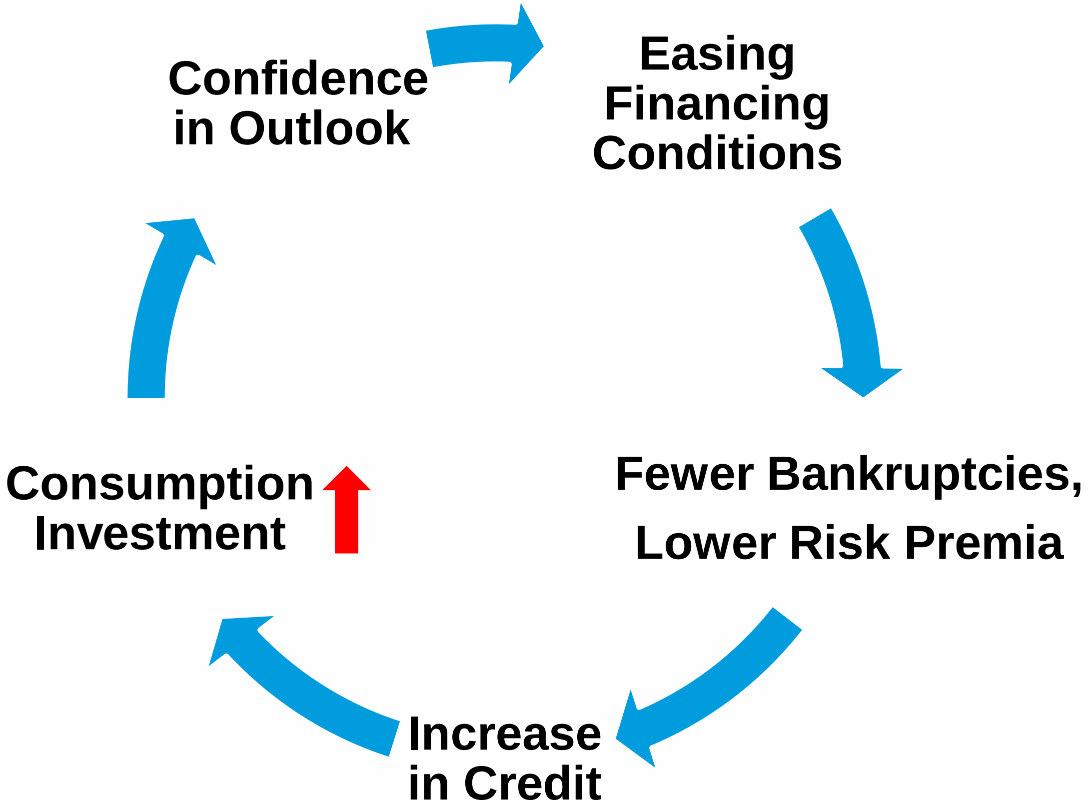
Effect of pandemic and credit policies on firm "liquidity" (example of Portugal)



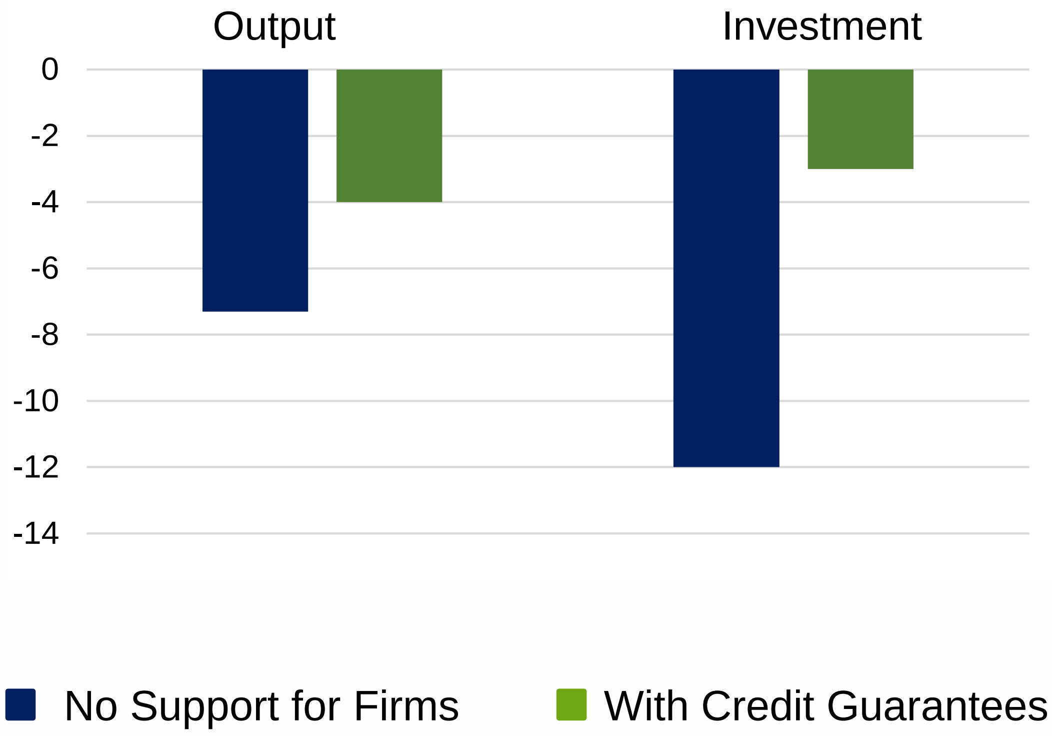
Source: ORBIS Data, IMF staff calculations; Battersby et al. (2022)

Credit policies can be a low-cost stabilization tool, especially during severe economic downturns

Feedback loop of bankruptcies, financial conditions, and sentiment



Macroeconomic effects of credit programs
(deviation from pre-crisis, percentage points)



Source: Battersby et al. (2022).

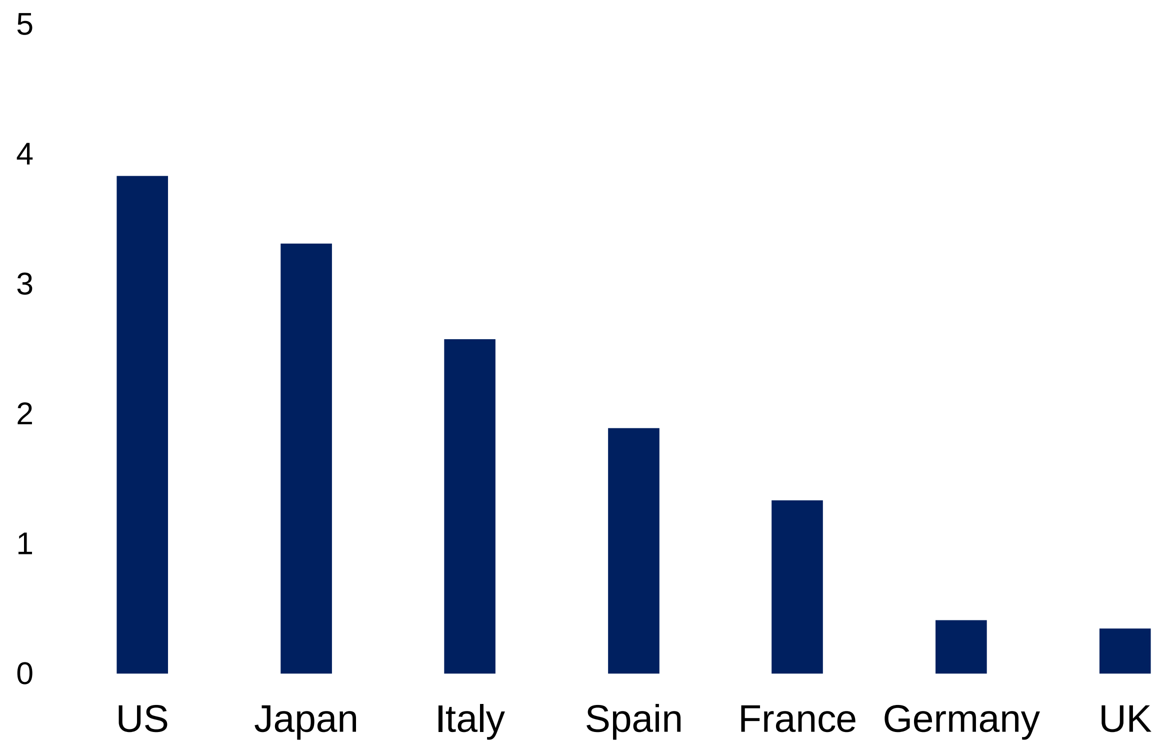
Measures were poorly targeted and may have saved firms that should have exited

- Several programs required no "skin-in-the-game" for banks (100 percent guarantees)
- Simplified monitoring/assessment steps (automatic approval subject to minimal self-reported criteria)

➔ Adverse selection, fraud concerns

➔ "zombifications"

Subsidy Element of COVID Guarantee Programs in Selected Advanced Economies (Percent of GDP)



Source: Hong and Lucas (2023)

Conclusions

During the pandemic, governments deployed credit policies on a historically unprecedented scale

The bar for intervention should be set high.

- Credit policies tend to be less transparent
- Their macroeconomic benefits are not extensively studied yet
- These interventions can also distort private sector decision

An upfront recognition of fiscal costs is critical to avoid future fiscal risks.

Governments should build their institutional capacity and be ready if they need to roll out credit policies quickly in future crises.

Thank you