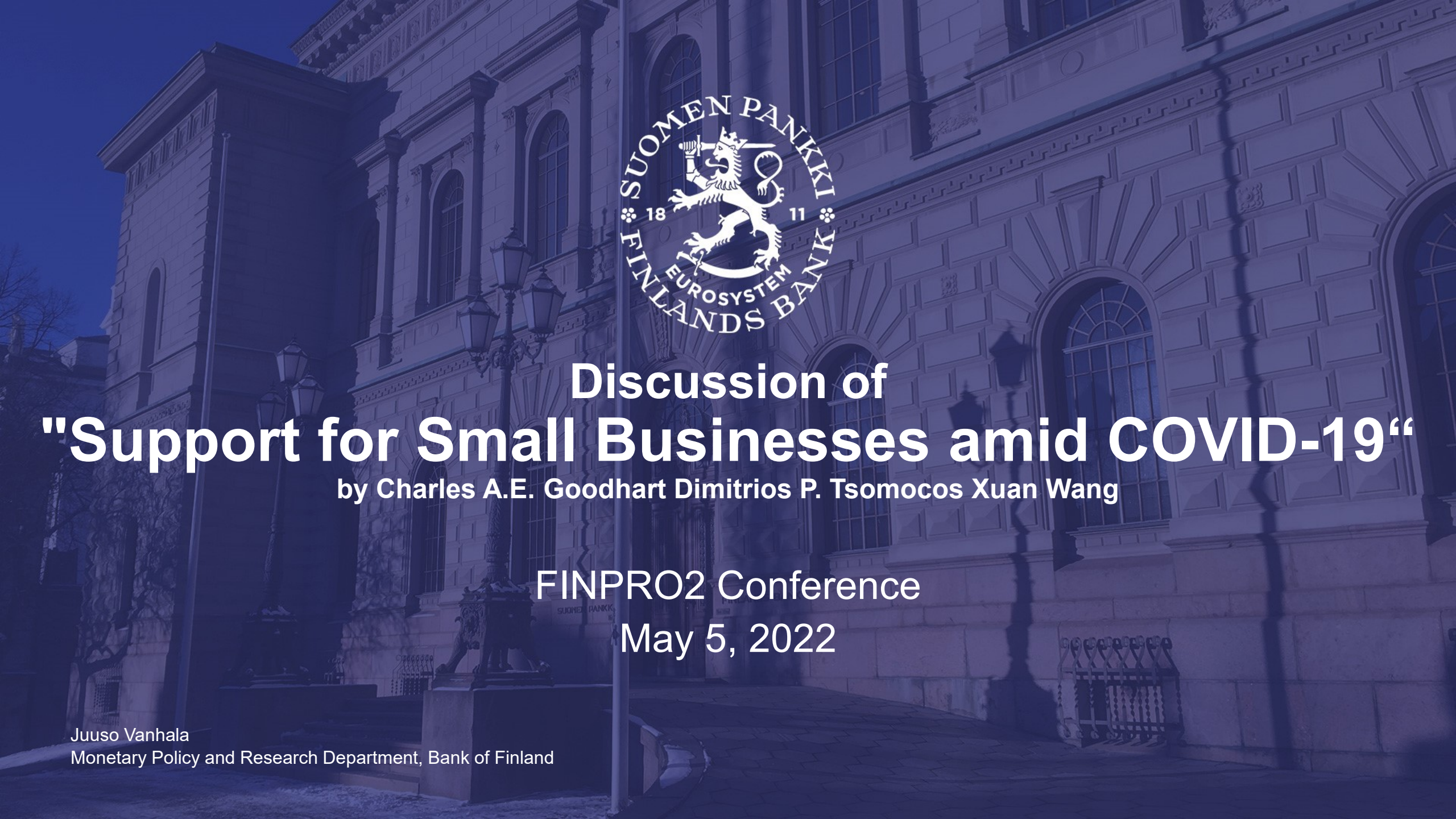

Discussion of "Support for Small Businesses amid COVID-19“

by Charles A.E. Goodhart Dimitrios P. Tsomocos Xuan Wang

FINPRO2 Conference

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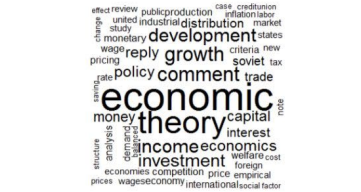
Support for Small Businesses amid COVID-19

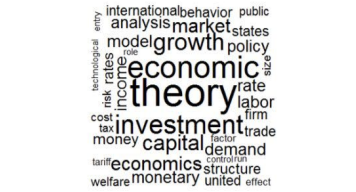
- Concern of misallocation of support and zombification
- Growing literature on pandemic support measures
- Very welcome contribution – theory!
- Important for policy makers to analyse thoroughly – future crises

Theory…!

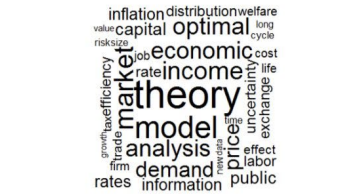
Figure 1: Most Utilized Words in the Titles of the 500 Most-Cited Articles in the AER, JPE, and QJE by Decade



Panel A: 1950s (1950-1959)



Panel B: 1960s (1960-1969)



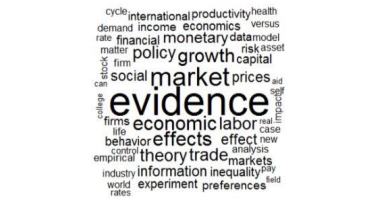
Panel C: 1970s (1970-1979)

Panel D: 1980s (1980-1989)

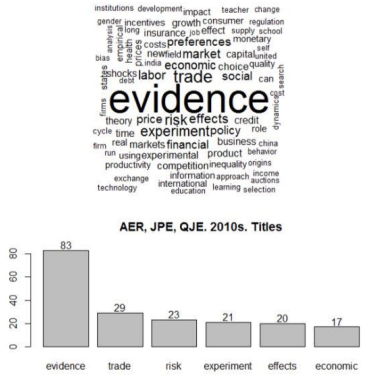
Based on the titles of the 500 most cited articles in the AER, JPE and QJE.
Source: Thomson Reuters Web of Science.

Figure 2: Most Utilized Words in the Titles of the 500 Most-Cited Articles in the AER, JPE, and QJE by Decade

Panel A: 1990s (1990-1999)



Panel B: 2000s (2000-2009)



Panel C: 2010s (2010-2015)

Panel D: All Decades (1950-2015)

Based on the titles of the 500 most cited articles in the AER, JPE and QJE.
Source: Thomson Reuters Web of Science.

The paper

- How should the government support SMEs amid a pandemic crisis?
- Policy tool: credit guarantees
- Policy trade-off of short-run employment stabilization and long-run allocation
- Socially optimal screening and the current state of the world?
  - Competitiveness of the affected industry
  - Effective Lower Bound
- Model to evaluate structure of credit guarantees in future crises

The paper: Two-sector equilibrium model of SMEs

- Two-sector equilibrium model (interaction - complementarity)
  - Pandemic shuts down one sector, firms apply for government loans
  - Other sector remains operative

- Loan applicants
  - Private information on expected future profitability
  - Low profitability firms more likely to default loans

- Government: default sanction (screening contract) to reduce adverse selection

- Condition and parameters that determine policy - “Stabilisation Proclivity"

The paper: Features

- Government tradeoff:
  - Pro-stabilisation: lenient default sanction, lower unemployment, lowers LR productivity
  - Pro-allocation: harsh default sanction, improves LR productivity, cost of persistent unemployment

- Default sanction: monetary deduction on defaulter's residual income – no bankruptcies

- Lenient policy (e.g. 100% credit guarantee) attracts and keeps afloat low profitability firms?

The paper: results

- “Stabilisation proclivity”: characterizes conditions and parameters that determine policy choice:
  - Monitoring efficiency (-)
  - Market power of SMEs (+)
  - Project return of left tail (-)
  - Discount rate (-)

- Simulations: intermediate policy is optimal

Comments

1. Preliminaries: theory and evidence
2. Entry and exit – firm demographics
3. Competition and congestion
4. Model assumptions

Comment 1: Theory and evidence

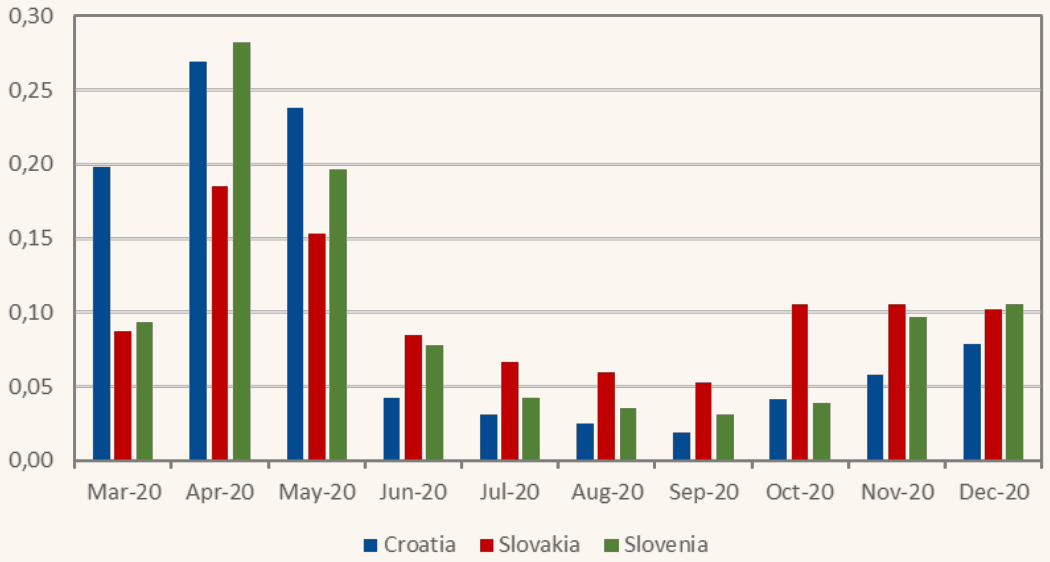
- Theory: Why are companies supported?
- The market mechanism is not working
  - Externalities, incomplete information, increasing returns to scale
- Key issues
  - Effectiveness (as intended)
  - Distortive effects on competition
  - Unconditional vs conditional - selection and selecting
  - Potential conflict between the short-term and long-term effects of subsidies
  - In times of crisis: urgency, short-term goals, avoiding economic collapse,…
- What measures successful business support?

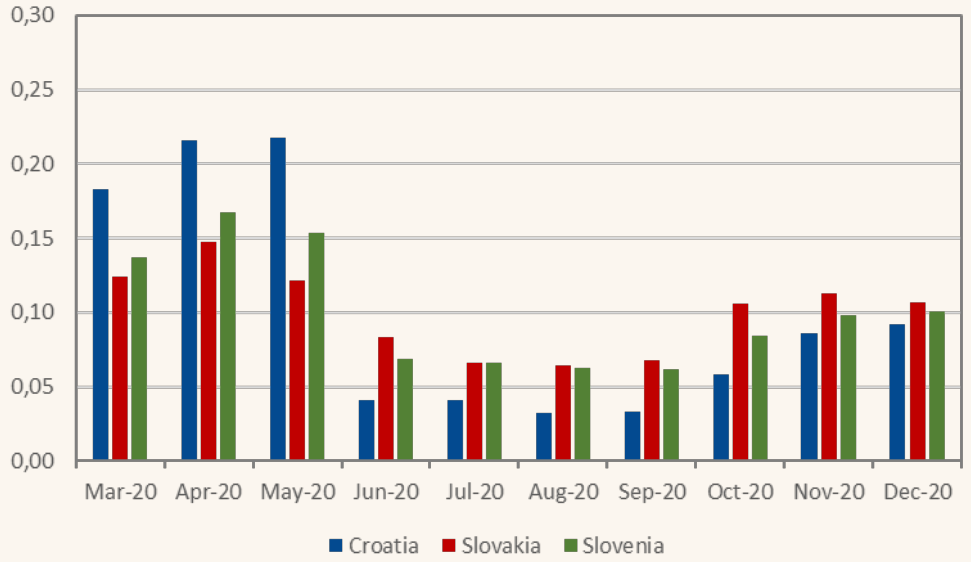
Comment 1: Scale, speed, scope, channels and success of government support

- Support was distributed relatively fast by governments (Bighelli et al. 2021, Coeuré et al. 2022)
- Tightening eligibility criteria produced delays in payments (Coeuré et al. 2022)
- Pre-existing subsidy infrastructure
- Subsidies played a key role (along with credit guarantees)

Comment 1: 45-70% of subsidies during first wave

- Share of allocated employment subsidies (% of year total)
- Share of supported firms (% of year total)





Source: CompNet Data Providers.

Comment 1: subsidies reached a large share of firms

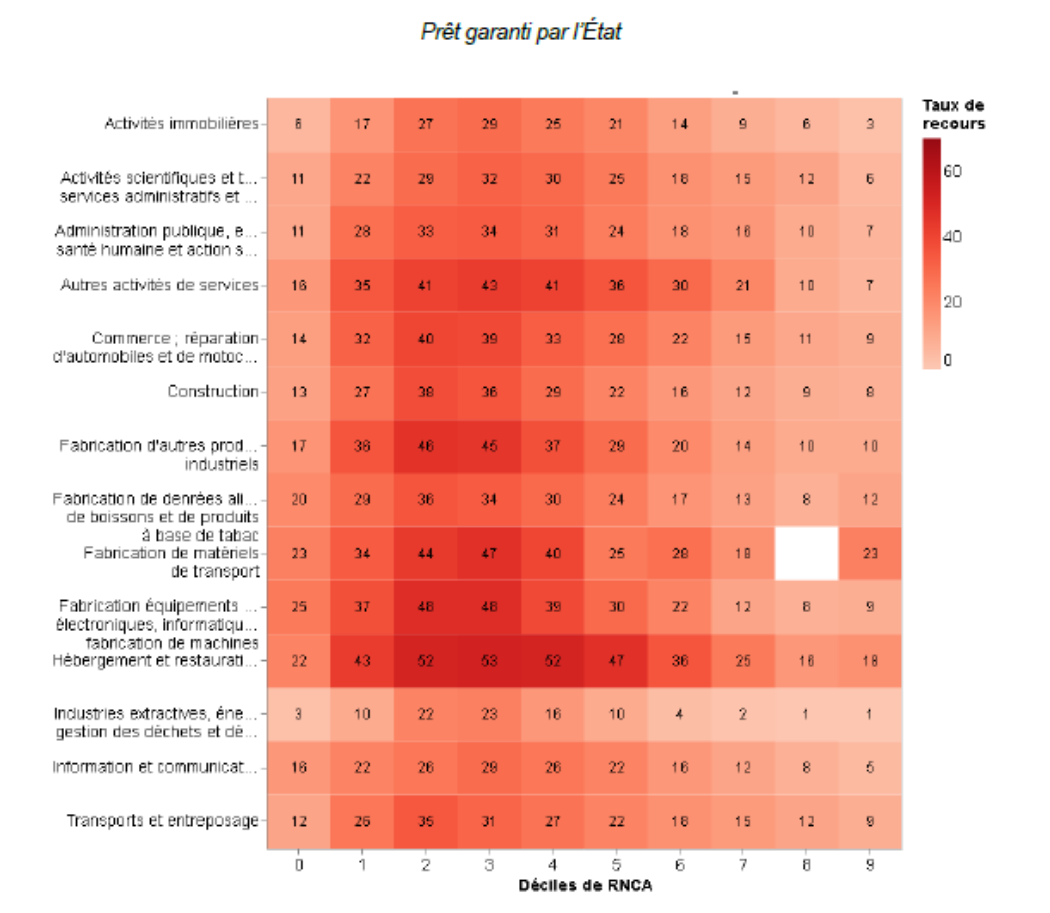
Variables	Croatia	Finland	Netherlands	Slovakia	Slovenia
Revenue (Thousand EUR)	1400	2542	8469	2765	2863
Employees	10.7	13.1	33.8	11.2	14.0
Supported firms (Share of total)	0.59	0.29	0.50	0.29	0.46
Size of support (Share on revenue)	0.05	0.07	0.11	0.02	0.03
Observations	85424	113454	120211	93520	36339

Note: Relative support for supported firms only. Based on employment support (Croatia, Slovakia and Slovenia) and overall direct support (Finland and Netherlands). Employment support in the Netherlands reached 0% of firms (i.e. coefficient is 0.4) and its size was 0.5.

Source: Bighelli et al. 2022

Comment 1: Role and allocation of credit guarantees

- Public support has been a “tentative success” and mostly allocated to “deserving firms” (e.g. Coeuré et al. 2021, Bighelli et al. 2022)
- Zombies have not been disproportionately subsidized
- Role of credit guarantees varies across countries
  - France: 69 billion in subsidies
    161 billion in loans
  - Finland: negligible role of guaranteed loans



Source: Coeuré et al. 2021

Comment 2: Exit and entry – firm demographics

- No bankruptcy – but exit flow from entrepreneur to worker (consistent with data)
- New entries – inflow of workers who may become entrepreneurs - assumption that industry gap is closed by new entries
- Flirting with entry-exit – free entry? (exit is formalized, though)

Comment 3: Exit and entry – implications

- Market competition (de Loecker et al 2020, Philippon…)
  - Shock would affect the number of firms in sector I
  - Would affect market power of remaining firms
  - BUT: SMEs and market power?

- Zombie congestion (Caballero & Hoshi 2008, OECD…)
  - Supporting distressed firms
  - Connecting to the zombie congestion literature
  - Is a liquidity crisis different?
    - Purely exogenous to firm
    - Short run effect?

Comment 4: model assumptions

- Private information is a standard feature
  - Did the firms know more than banks or the government in 2020q2?
- Do prices in the model reflect market conditions (shocks)?
- Maximum or equilibrium production capacity of firms Q/2N?
- The return distribution
- Productivity: abstracting from physical capital?
  - How innocent is this assumption when studying long run and productivity?
  - Evidence (e.g. EIB 2021) shows that firms “digitalized” during the pandemic

Comment X: What is productivity?

- Lenient default sanction
  => keep workers with low productivity

- Harsh default sanction
  => unemployed workers have zero productivity

- In the latter case the average productivity of employed workers is higher, but average productivity of all workers is lower

Miscellaneous

- Market power of SMEs?
- Bankruptcies rarely pursued
  - Lenders garnish residual income
  - Japan 1990s or Finland 1980s bank-firm ties
  - Provide more evidence of government-bank-firm relationships
- Model to evaluate structure of credit guarantees in future crises?
  - Pandemic shock was sudden – liquidity crisis
  - Russia's invasion war in Ukraine – trade, uncertainty and inflation shock
- Very intriguing paper!

Thank you!

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