EU CORPORATES AND COVID-19: THE SHORT AD LONG TERM CHALLENGES

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Covid-19 economic crisis – EU corporates

- A massive economic shock:
  - Lockdown as a massive shock across geographies and sectors
  - Demand and supply shock, trade collapse and questioning on GVC model

- Rebooting in the face of sectoral, country, regional and firms heterogeneity

- Huge uncertainty remains:
  - Medical (immunization, timing for a vaccine, second round of contagion, etc.)
  - Shape of the recovery (effectiveness of policy answers and consequent likelihood/severity of second round effects of the crisis)
  - Long term structural changes (change in individual preferences, labor market, value chains security, role of the state)

Corporates – a sizable impact on EU corporate sector

- After 3M of lockdown, 51-58% firms might face liquidity shortfalls, despite discounting for policy intervention

Table 1: Liquidity shortfall of non-financial corporations under various scenarios and across time *(EU)*

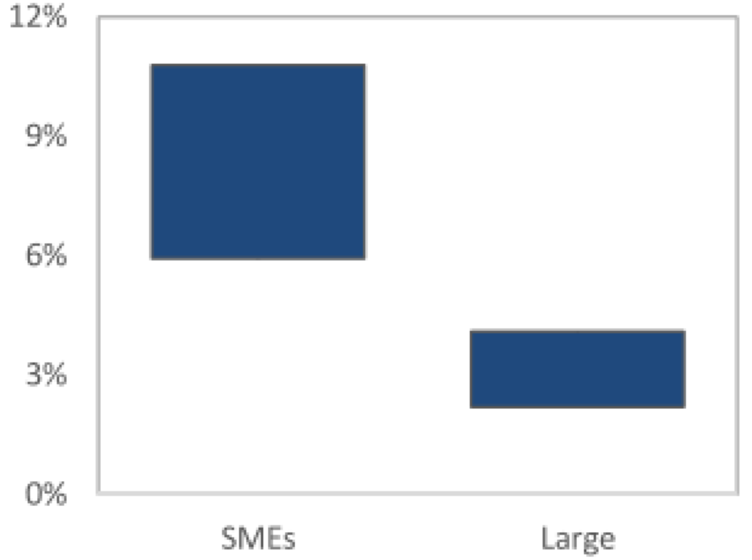
	1 month				***2 months***				***3 months***			
	Share (%)		*Shortfall*		*Share (%)*		*Shortfall*		*Share (%)*		*Shortfall*	
	Firms	Value added	EUR bn	% GDP*	Firms	Value added	EUR bn	% GDP*	Firms	Value added	EUR bn	% GDP*
Policy support	26%	29%	**46**	0.3	46%	50%	**149**	1.1	58%	70%	**287**	2.1
Heightened policy support	19%	21%	**14**	0.1	38%	43%	**47**	0.3	51%	60%	**95**	0.7

Source: ORBIS[ii] and EIB calculations. Note: Based on EU27. The columns "Share" indicates the proportion of corporates that do not have enough cash to withstand their payment obligations over the period, as % of the population (1st column) and of value added (2nd column).

- Normalisation will take time. The cumulative loss in net revenues for the corporate sector might amount to 13% - 24% of GDP

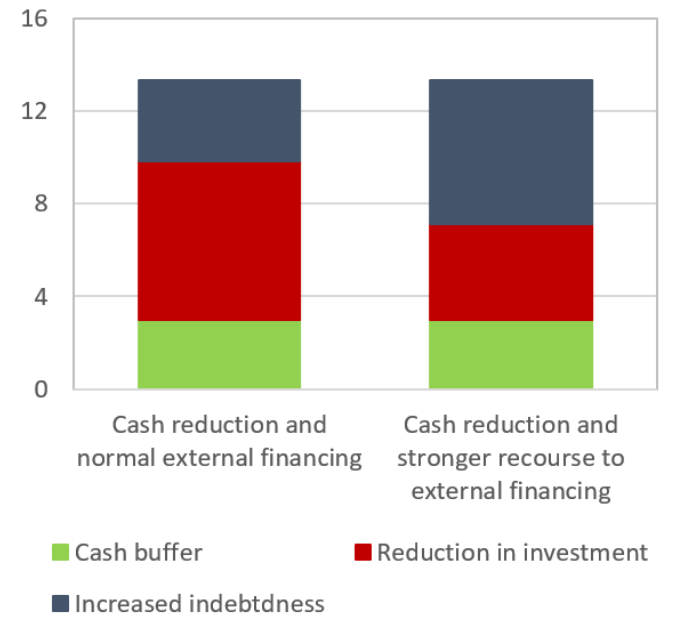
Corporates – resilience dependent on size. For all firms, in the medium term, a trade off between investment and leverage emerges

Figure 12: Interval of net revenues reduction by size of corporation (median, % of total assets)



Source: ORBIS and ECON calculations.

Fig 9 – Filling the gap: impact on investment and indebtedness *(%, EU economy)*



Source: ECON computations based on EUROSTAT and ORBIS. Results under the begnine scenario.

- Investment decline: 31 to 52%
- Higher leverage 6% vs 4% of GDP, depending on strategic choices

Optimal policy sequencing

Economic Crisis

- Drop in revenues and fix costs
  - Cash buffers depleting fast, particularly for SMEs

- In the recovery phase, at the firm level strategic choices:
  - Reduce investment
  - Increase debt
- Need to keep focus on innovation and diffusion of innovation, as well as climate
- At the economic level: preserve, but adapt and transform fast

Policy Response

Rebates and grace periods

Liquidity and credit (and guarantees)

Equity and equity type instruments

Lock down | Unlocking and recovery | Long term

Conclusions

- The Covid19 crisis strongly affect firms
- Liquidity shortfall and long term-strategic trade-off emerging: leverage vs investment
- Optimal sequencing of policy intervention
  - Grace periods
  - Access to credit and guarantees
  - Complemented by equity type of instruments
  - Long term focus: climate and innovation

Digital adoption:
EU 58% vs US 69%

Investment in EE:
EU 40% vs US: 47%

EU firms: 13% of the group of new top innovators (vs US 34%)

80% firms in the lowest productivity group stuck for at least 3Years

VC/GDP: EU 0.05% vs US 0.33%

ANNEX - Corporates – a sizable impact on EU corporate sector

- An accounting exercise with balance sheet and profit and loss figures for 1.4 mn firms in Europe (Eur 8 tn)
  - Simulate the drop in revenues and stickiness of costs (distinguishing by different costs)
  - Simulate the policy intervention (grace periods and rebates)
  - Assume different "business normalization" scenarios

Table A2 – Calibrations used

	Sales	Cost of employees	Administrative costs	Financial expenses	Material cost
Policy support during lockdown	70% drop	40% reduction	40% reduction	60% reduction	50% reduction
Heightened policy support during lockdown	70% drop	60% reduction	60% reduction	70% reduction	50% reduction
Recovery period fast, 3 months	gradually increasing in 3 months from 40% to 5% below "normal"	gradually increasing in 3 months from 35% to 5% below "normal"			
Recovery period slow, 6 months	gradually increasing in 6 months from 40% to 5% below "normal"	gradually increasing in 6 months from 35% to 3% below "normal"			