Supporting firms during the COVID-19 crisis

Options and trade-off for policy makers in developing countries

Development Policy and COVID-19 e-Seminar Series
Outline

- Why should we care?
- A simple conceptual framework
- Design and implementation considerations
  - A single metrics to evaluate interventions
  - Policy sequencing: different policies for different stages
  - Targeting dilemma
  - Avoidable mistakes
  - Reaching informal firms
- What to do now or how do I get started?
  - Know thyself
Why should we care and act quickly

- This is a unique crisis for various reasons
- Profitable firms and productive jobs could disappear
  - Destruction of productive jobs and production capabilities (organization)
  - Recovery slow and costly if this happens: V-shaped vs U-...or L-shaped
  - “Market” selection channels muted by size of shock
    - E.g. young productive firms disproportionately affected because of low liquidity
- Size of shock
  - E.g. in Mexico about 50% of employment (based on economic census)
- Potentially short-lived (at least part of it) therefore with “affordable” solutions (at least some)
  - But with long-term consequences if not addressed
## COVID-19 shock pathways

1. **Shutdown shock**: result of health measures to reduce contagion
   - Simultaneous supply and demand shock
   - Limited in time
   - Only affects certain sectors (and certain locations)
   - Mitigated by relying on online

2. **Demand shock** beyond the shutdown
   - Businesses manufacturing durables and their suppliers
   - Indirect demand shock due to the shutdown (suppliers to businesses in shutdown)
   - Exporters

3. **Supply shock**: Disruption in production capacities due to
   - Decline in labor (health, childcare, precautionary measures)
   - Lack of intermediate goods (disrupted value chains)
   - Lower productivity

4. **Financial shock**
   - Deterioration in access to finance and credit conditions because of bankruptcies and defaults
   - USD-denominated debt + devaluation

5. **Uncertainty shock**
A taste of the heterogeneity of impacts

Within sectors

Viral variance
Global stockmarket performance by sector*, %
January 1st-April 3rd 2020, $ terms

-60 -40 -20 0 20 40

Health care
Technology
Consumer staples
Communications
Materials
Industrials
Utilities
Consumer discretionary
Financials
Energy

Source: Bloomberg

*Companies with current market capitalisation over $5bn

Within countries

Share of state-level employment in potentially affected businesses
How to spend the limited resources available?

- Q.: Countries are implementing many policies…what should we do? What should we advise?
- Policy makers very active…many policies and different packages
- Resources are scarce…especially in developing countries
  - Be explicit about trade-offs between policies
- Focus on maximizing a single metrics to evaluate interventions
  - Key policy objective: protect productive jobs (and production capabilities)
- **In short term maximize $ per job protected**
  - Weighting using “wages” as a measure of productivity
  - Account for distributional consideration
  - Make support conditional to keeping workers
- Note: keeping firms profitable is key but beware…
  - Trade offs between targeting profitability and keeping jobs
Policies for today…and policies for tomorrow

- Distinguish two phases
  - Phase 1: Crisis and immediate response
  - Phase 2: Recovery

- What priorities in each phase? Distinguish two phases
  - Phase 1: Keeping jobs and productive capabilities
  - Phase 2: Focus on productivity and economic transformation

- Appropriate interventions phase 1 ≠ Appropriate interventions phase 2
  - Measures in phase 1 should be time-bound (explicit deadline!)

- Key to note that the shocks are likely to be different in each phase
  - Phase 1: Demand shock due to lockdown
  - Phase 2: Demand shock due to slow recovery of tourism and durables consumption
To target or not to target?

- **Why target?**
  - Available resources are scarce
  - Make sure support is commensurate with needs
  - Avoid that support given is insufficient for those that need it…and superfluous or distortive for those that don’t need it

- **Why not to target? (or what to avoid)**
  - Adds complexity…slow down intervention
  - Adds discretion…potential rent seeking and misallocation
  - Especially problematic where institutional capacities are weaker

- **Possible targeting in phase 1**
  - Locations
  - Sector
  - Self-targeting (support conditional to keep jobs!)

- **Possible targeting in phase 2**
  - Address channels that are likely to be more important (e.g. uncertainty)
  - Focus on firms that could maximize productivity growth and economic transformation
Avoidable mistakes

- Resist the instinct to take interventions from different contexts (e.g. richer countries) and apply them
  - Less fiscal space
  - Some policies may reach only very few companies (e.g. tax breaks and formal companies)

- Tackle trade-off explicitly
  - There are many trade-off that the situation involve
  - Be explicit and identify some agreed measures to assess them (i.e. short term $ per job saved)

- Try avoiding the common economist’s mistake
  - Address conflict between what is easier vs what is needed
  - E.g.: channel more resources through existing cash transfer for elderly
Special consideration for certain groups of firms

- **Informal firms**
  - Much harder to reach…but not impossible
    - Reach them through their suppliers
    - One time income grant towards future formalization (only minimal proof of existence – bills paid or invoices from suppliers)
    - Extend factoring for informal firms

- **Indirectly affected firms**
  - Especially from shutdown and demand shock
  - Very large impact

- **Young firms/Startups**

- “Integrated” firms

- Systemic companies
What do we do now? How to get started?

- **First know thyself!**
  - Assess magnitude and distribution of impact
  - Is intervention the “right” magnitude?
  - Will policies reach firms and jobs most affected?

- **Monitor ongoing impact to refine (or review) intervention**
  - Rapid survey
  - Measure impact of different channels – different policies and different responses needed
  - Understand firms responses and adjustment (process, product and market innovation)
  - Understand uncertainty – distribution, magnitude across firms/sectors/locations
  - Understand barriers to access Government programs…key for “plumbing”
Thank you for your attention!