
ECONOMIC ALERT

1

gap.



open
eyes
economy
summit

Professor SGH, Agnieszka Chłoń-Domińczak, PhD hab.

Professor Jan Czekaj, PhD hab.

Sławomir Dudek, PhD

Dariusz Filar, PhD hab.

Mirosław Gronicki, PhD

Professor Jerzy Hausner, PhD hab.

Janusz Jankowiak, PhD

Robert Kowalski

Professor SGH, Krzysztof Marczewski, PhD hab.

Professor UG, Leszek Pawłowicz, PhD hab.

Professor SGH, Andrzej Rzońca, PhD hab.

Professor Andrzej Sławiński, PhD hab.

Małgorzata Starczewska-Krzysztosek, PhD

Financial liquidity of enterprises

Problem definition

The implementation of the economic policy priorities stipulated in Economic Alert 1 (EA 1 published on March 27, www.oees.pl/dobrzewiedziec) requires, in particular, ensuring the financial liquidity of enterprises. It is a task of utmost urgency. Without this, a significant number of enterprises will not be able to continue their business operations. It will cause dramatic problems related to the accumulating effects of the epidemic along with catastrophic social and economic aftermath that will reinforce the health consequences.

Enterprises have to remain at the core of the economic policy. Their financial liquidity is a key issue. The market will not work without it, or it will operate in an uncivilised form. Today, defending the market means ensuring the financial liquidity for enterprises!

Efficient targeting of the support does not require the conditioning to be complicated. In the acute phase of the epidemic the government has to rely on the self-assessment of entrepreneurs as regards the extent they need its support and verify it ex post.

Indispensable actions

The fundamental issue of ensuring liquidity to enterprises has several essential aspects:

- 1. releasing the entrepreneurs from financial burdens that they cannot cope with;**
- 2. restraining the spiral of payment gridlocks; and**
- 3. ensuring enterprises with additional liquidity by means of the banking system.**

1. Releasing the entrepreneurs from financial burdens

It is the primary task, the undertaking of which is to mean immediate and automatic release for a period of three months from the public-legal payments for small and medium enterprises and the suspension of their collection in the case of large enterprises (on the voluntary basis), with the possibility of their subsequent partial or even, in special cases, full abolition. Such activities, if necessary, could be selectively or entirely extended for subsequent periods. We have described this activity in more detail in Economic Alert 1 (Priority 2).

Without immediate implementation of the above task, enterprises will fall into the spiral of payment gridlocks. They will not be able to pay to their contractors. Certain enterprises will drag others down.

And this, in turn, will mean that they will quickly lose the ability to take advantage of the liquidity bank support as proposed by the government.

A problem arises with enterprises that not only have no credit capacity, but also no credit history in 2019, which is required to process the application in compliance with the banking law and regulations contained in the governmental “Protective Shield”.

2. Restraining the spiral of payment gridlocks

In this regard, the following actions are recommended:

- suspension of *split payment* and creation of an opportunity to use the resources accumulated within the VAT account without the requirement to apply to do it;
- administrative acceleration of VAT refund (up to 14 days);
- introduction of support mechanisms (even in the form of preferences) for the debt and financial instruments markets with respect to working capital (e.g. factoring).

3. Ensuring enterprises with additional liquidity by means of the banking system

In this respect, two solutions are most important:

- state guarantees for corporate loans; and
- securities for banks supporting the enterprises.

A pillar supporting the liquidity should be the bank support assisted by the BGK guarantee and security system. The guarantees could pertain to 80% of the loan volume. It is recommended to launch a special Liquidity Guarantee Fund. The general task of such a Fund is to support liquidity maintenance by entrepreneurs affected by the effects of the epidemic. The resources within this Fund would be managed by the BGK's Management Board, and the revenues of the Fund would be resources obtained by the Bank from the issuance of bonds called "COVID-19 bonds".

BGK, by means of Guarantee Funds in which it has shares (21 regional and local funds), should offer quick factoring services on simplified terms to the interested entrepreneurs.

Each small and medium enterprise should have an opportunity to receive a guaranteed loan if it paid income tax in 2019. It means that only profitable companies can benefit from this kind of support, which reduces the risk of abuse.

BGK could also guarantee an overdraft within the current account raised by commercial banks. It is also worth considering taking over some loans by BGK and their securitisation.

Corporate loans that are not covered by state guarantees should be exempt from bank tax.

We point out that the postponement of loan repayment currently offered by several banks without extending the repayment period may have counterproductive effects and will then inhibit the economic recovery, absorbing the financial resources of enterprises for the implementation of cumulated payments, and not for restarting and developing business operations.

We postulate a temporary liberalisation of supervisory requirements with respect to the banks.

Macroeconomic framework and system conditions for the state financial security

Anything that can be and should be done for health and economic security has to take place within a specific, defined framework of state financial security. The framework cannot overpower or it cannot restrain the necessary extraordinary activities, but it has to be clearly determined and firmly maintained. We cannot allow such a weakening of public finances that will lead to the collapse of the financial system.

A significant increase in public debt is becoming inevitable – in nominal terms and with respect to GDP. We estimate that the state financial needs this year may reach PLN 130-150 billion. Without this, the anti-crisis measures will not be feasible.

We are awaiting a major amendment to the Budget Act. It needs to be done after a thorough review of all the budget expenditure in order to reduce the level of expenditure that is not necessary this year. In particular, for a period of at least 3 years (2020-2022) it is necessary to resign from the rule of spending 2% of GDP for the military purposes. It will also be necessary to suspend a part of the fixed social expenditure for this period (in particular, this applies to the 13th retirement pension and limiting the 500+ benefit payment to the level before its extension).

If the event of the introduction of *the state of natural disaster* (or any other state of emergency as defined in the Constitution), budget expenses exceeding the limits of the Stabilising Expenditure Rule can be planned. Writing down additional exceptions to the Stabilising Expenditure Rule Act to the Public Finance Act will lead to its actual dysregulation. After exceeding the public debt over 55 percent of GDP, it will be necessary to apply remedial measures provided for in Art. 86 of the Public Finance Act (e.g. no actual valorisation of retirement pensions, freezing of the state budget salaries, etc.)

A significant part of the constitutionally permissible debt level potential should be preserved for the period following the end of the epidemic, among others, in order to be able to carry out the necessary financial restructuring of banks and large enterprises.

Respecting the above legal and financial restrictions is fundamental to assessing the credibility of the state within the international financial markets. Undermining this credibility will lead to a weakening of the Polish zloty and an increase in the yield of Polish Treasury securities. And then, the public debt will grow without any control.

In this context, the issue of openness, transparency and clarity of public finances is of great importance. Accounting manipulations will be recognised quickly and will undermine the trustworthiness.

The more so because the urgent problem is to secure international liquidity - both for banks and enterprises so that they can - if necessary - reach for FX swaps. To help banks, the NBP concluded an FX swap agreement with the Swiss National Bank (SNB) during the previous crisis. Currently, it would be good to have such agreements with the European Central Bank (ECB) and the Federal Reserve (FED).

Furthermore, we also postulate for an urgent review of the regulations regarding the bankruptcy of enterprises and suspension of some of them for the period of epidemic. Otherwise, the assets of many of businesses can be bought for next to nothing. During the protecting activities, the state's share in the economy will increase significantly. That is why it is necessary to determine a time frame and exit path for governmental institutions from the sanctioned private companies.

The Economic Alert is an initiative of the Open Eyes Economy Summit and the College of Economy and Public Administration of the Krakow University of Economics.