The Legacy of COVID-19 Financial Supports:
(1) Judging the Effects of the Pandemic-Era Measures

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Introduction

As the first of two articles for the *Journal of International Banking Law and Regulation*, this article considers the immediate effects of financial support measures implemented during the COVID-19 pandemic. These measures ranged from direct subsidies to guaranteed loan facilities. The article describes the initial purposes of the assistance, explains the distinct phases of financial supports, and questions how the 'success', or efficacy, of the measures can be quantified. The second article will address how public supports may be adapted to life beyond the pandemic, specifically by analysing how measures could be shaped towards key policy objectives, such as promoting viable and solvent businesses' investment in sustainable practices and in expediting digitalisation of their activities.

Although both articles focus on developments within the European Union, the emergency circumstances of the COVID-19 pandemic prompted an unprecedented re-appraisal of how governments internationally should intervene to financially support businesses. To state the plainly obvious, the repercussions of the pandemic altered many facets of society. The various financial measures introduced during the height of the pandemic have left a legacy of opportunity and uncertainty as to whether these public supports should be retained.

Since the pandemic, certain viewpoints may maintain that state intervention was irrefutably necessary to respond to an exigency of ensuring that all businesses stay afloat. From this vantage, the financial supports were decisive to future stability as economies emerged from the throes of lockdowns, restrictions, and a general suspension, or slowing, of business activity. Moreover, financial support measures could be argued as being completely intrinsic to corporate investment in sustainable and innovative practices. On the other hand, some perspectives may assert that the pandemic-era responses exhibited a panicked complacency

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by enabling funds to be distributed in a free-for-all to businesses. In this more critical outlook, the financial measures not only signified a dubious expenditure of public money, but, also, saddled otherwise healthy companies with hefty debt burdens to last well beyond the grimmest days of the pandemic.

As we cautiously analyse pandemic-era measures in retrospect – as features of approaches taken during an astonishing period of recent history – which of these divergent attitudes is the most credible? The most reasonable answer may be 'neither'. There are merits to both disparate viewpoints. Nonetheless, the time may have arrived to accept that there are ongoing functions and advantages associated with the kinds of measures used to alleviate the worst of the pandemic's economic fallout.

The first section of this article will depict the original aims of support measures which were established across the EU at the earliest stages of the pandemic. An overview of the types of supports will be provided. The second section of the article will distinguish between phases of financial assistance, especially the shift from an approach which was based primarily around safeguarding the liquidity of struggling businesses. By reference to relevant studies and commentary, the third section of the article explores how the outcomes of public supports can be feasibly gauged. Depending on how the 'success' of a measure is envisaged, the effects of the pandemic-era programmes and schemes should prove instructive to the creation of similar measures to complement EU policies for a twin transition towards sustainable, technology-oriented innovation.

Purposes and variations of public supports

From the outset of the COVID-19 pandemic, the rationale for public intervention to help struggling businesses was predicated on mitigating liquidity problems, as predominantly evinced by cash flow difficulties. The liquidity shortages of businesses were treated as being relatively short-term in nature. [1] Once commercial activities began to be affected by lockdowns and associated restrictions, there was a pressing demand for further liquidity. [2] Whether the responses smacked of panic or not, the chief motive for the introduction of a

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[1] EBA, *Closure Report of COVID-19 Measures* (EBA/REP/2022/32) (December 2022), para. 2

[2] See V. Acharya and S. Steffen, 'The Risk of Being a Fallen Angel and the Corporate Dash for Cash in the Midst of COVID' (2020) 9(3) *Review of Corporate Finance Studies* 430.

plethora of financial measures in jurisdictions worldwide was to support businesses in withstanding the brunt of the pandemic and the consequent decline in customer footfall, trade and profitability. Aside from a crisis reaction, sights were set on preserving future prospects of economic growth, as "governments sought to prevent widespread bankruptcies of firms that could not operate profitably because of the Great Lockdown but could rebound quickly after." [3]

As intimated by the reference to a 'Great Lockdown', the degree to which the COVID-19 pandemic signalled an unprecedented shock cannot be underestimated. The "unexpected, severe, and complex" [4] scale of the pandemic's impact prompted a similarly drastic level of response. After the Global Financial Crisis, analogous financial support measures were implemented by governments to erode the challenges confronting businesses. [5] However, the expense arising from the COVID-19 measures far outstripped the magnitude of public interventions in the prior decade. For instance, it is estimated that announced measures globally reached $6 trillion, whereas, in the aftermath of the financial crisis, the 37 largest economies established about $1.6 trillion worth of direct loan and equity supports and approximately $1.9 trillion in guarantees. [6] In a European context, fiscal supports among European Systemic Risk Board (ESRB) member states amounted to almost 21% of the Gross Domestic Product (GDP) for 2019. [7]

The figures are staggering, but the span of the public intervention should be understood in terms of what exactly is meant by support measures and in terms of the actual uptake for these measures. As identified by a European System of Central Banks (ESCB) report in 2024, financial measures can be distinguished by either being budget-relevant or being fiscal. Budgetary measures can include direct grants, cash transfers, tax deferrals and tax relief for businesses. Fiscal measures connote the protection of liquidity and solvency. As the measures

[3] B. Battersby, R. Espinoza, J. Harris, G. Hee Hong, S. Lizarazo, P. Mauro, and A. Sayegh, 'The State as Financier of Last Resort' (International Monetary Fund Staff Discussion Note 2022/003) (October 2022), p. 5.
[4] P-O. Gourinchas, S. Kalemli-Özcan, V. Penciakova, and N. Sander, 'COVID-19 and SMEs: A 2021 "Time Bomb"? (National Bureau of Economic Research Working Paper 28418) (January 2021).
[5] For example, this author previously examined the likely efficacy of a tailored loan guarantee scheme in Ireland in: J. McCarthy, 'A Review of the Credit Guarantee Scheme' (2013) 20(8) *Commercial Law Practitioner* 170; and J. McCarthy, 'The Credit Guarantee Scheme: An Analysis of Recent Reforms and of its Performance to Date' (2017) 24(9) *Commercial Law Practitioner* 183.
[6] Battersby et al, 'The State as Financier of Last Resort' (IMF SDN 2022), p. 3.
[7] ESRB, *Fiscal Support and Macroprudential Policy – Lessons from the COVID-19 Pandemic* (2022): available at: https://www.esrb.europa.eu/pub/pdf/reports/esrb.2022.11.21.note.on.fiscal.support.and.macroprudential.policy~e5abc993e9.en.pdf (date accessed: 9 June 2024).

apposite to this analysis, fiscal supports encompass loan moratoria, public guarantees on loans, public or subsidised loans, government support for credit insurance, and the provision of government equity. [8] A broader interpretation of support measures is given by the European Investment Bank (EIB) in categorising four distinct types: [9] new subsidised or guaranteed credit (subject to lower rates) that will require repayment; payment deferrals which represent future liabilities for businesses; subsidies or supports which will not require repayment (such as through job retention schemes); and any other miscellaneous forms of support.

As an overall observation on the patterns of uptake, there were variations across jurisdictions – and across EU Member States – in the use of supports. [10] Although it was reported that some 56% of firms in Europe were availing of at least one type of support, [11] it has also been recorded that a rather low fraction of the total announced funding was ultimately sought and accessed by eligible businesses. [12] To summarise simply, governments committed to substantial quantities of support, and, even though most businesses availed of public funding, the uptake was for a very modest share of the total amounts which were provided for.

Pandemic-era measures, such as guaranteed loan facilities, placed governments in a considerably more risk-intensive position than at any time since the Global Financial Crisis. The effects of public 'participation' in the financing of firms, by re-configured regulatory and monetary policies, were borne out by increases in the available funding channels for European businesses, particularly during 2021. [13] As surmised by Alexander Lehmann, governments were now expected to carry the risk of borrower default in a manner akin to

[8] ESCB Expert Group on Productivity, Innovation and Technological Change, 'The Impact of the COVID-19 Pandemic and Policy Support on Productivity' (European Central Bank Occasional Paper No. 341) (2024), p. 41.
[9] For findings based on these categorisations and the results from the EIB's Investment Survey 2021, see P. Harasztosi, L. Maurin, R. Pál, D. Revoltella, and W. van der Wielen, 'Firm-Level Policy Support During the Crisis: So Far, So Good?' (2022) 171 *International Economics* 30.
[10] Battersby et al, 'The State as Financier of Last Resort' (IMF SDN 2022), Figure 6, p. 6.
[11] Harasztosi et al, 'Firm-Level Policy Support During the Crisis: So Far, So Good?' (2022) 171 *International Economics* 30, 34.
[12] About 10% of the fiscal supports permitted by ESRB member states amount in fiscal supports was used: ESRB, *Fiscal Support and Macroprudential Policy – Lessons from the COVID-19 Pandemic* (2022), p. 2.
[13] See AFME, *Capital Markets Union. Key Performance Indicators – Sixth Edition* (Association of Financial Markets in Europe, November 2023), p. 5.

equity investors. [14] Loan guarantee mechanisms are the most prominent examples of such a transfer of risk towards states. [15]

By guaranteeing state exposure for some, or all, of specific loans advanced by private banking institutions, the intention is that banks are incentivised to surpass any risk aversion in extending credit to commercial borrowers such as small- and medium-sized enterprises (SMEs). [16] Yet, provision for public 'skin in the game' may also give rise to situations of adverse selection. Funds could be diverted in an overly lenient fashion towards businesses who cannot demonstrate suitable creditworthiness in ordinary circumstances and who would not therefore usually seek loans from private financial institutions. Furthermore, there are moral hazard concerns surrounding a deliberate choice to use taxpayers' money in favouring certain inherently risky borrowers over others for investment. [17] Loan guarantees were more readily availed of in some EU states, compared to others. According to European Banking Authority (EBA) data, loans subject to public guarantees were at a peak value of €378 billion in the third quarter of 2021, before declining from 2022 onwards. [18] As evinced by the EBA findings, 95% of the total loans within public guarantee schemes were utilised in the three countries of France, Italy and Spain. [19]

If the availability of guarantees and other supports tended to vary across the EU, the funding was consistently aimed towards businesses that were most directly affected by lockdowns, restrictions, and closures. Businesses providing in-person services were abruptly curtailed, while the most conspicuous reductions in revenues were witnessed by businesses in the

[14] A. Lehmann, 'Confronting the Risks: Corporate Debt in the Wake of the Pandemic' (Bruegel, 28 April 2021); available at: https://www.bruegel.org/blog-post/confronting-risks-corporate-debt-wake-pandemic (date accessed: 9 June 2024)

[15] O. Blanchard, T. Philippon and J. Pisani-Ferry, 'A New Policy Toolkit is Needed as Countries Exit COVID-19 Lockdowns' (Bruegel Policy Contribution 12/2020) (June 2020), p. 7; available at: https://www.bruegel.org/sites/default/files/wp-content/uploads/2020/06/PC-12-2020-230620.pdf (date accessed: 9 June 2024).

[16] As construed in accordance with the European Commission Recommendation 2003/61/EC, of 6 May 2003, on the definition of micro, small and medium-sized enterprises, OJ L 124/36, whereby an SME employs fewer than 250 persons and has an annual turnover not exceeding €50 million and/or an annual balance sheet total value not exceeding €43 million.

[17] For an assessment of these factors in relation to COVID-19 financial measures (specifically, a Spanish loan guarantee scheme implemented in March 2020), see G. Jiménez, L. Laeven, D. Martinez-Miera, and J.-L. Peydró, 'Public Guarantees, Private Banks' Incentives, and Corporate Outcomes: Evidence from the COVID-19 Crisis' (European Central Bank Working Paper No. 2913) (2024).

[18] EBA, *Closure Report of COVID-19 Measures* (2022), para. 60.

[19] EBA, *Closure Report of COVID-19 Measures* (2022), para. 64.

accommodation and food sectors. [20] Social distancing requirements imposed stringent losses on small firms engaged in services. Amid pervasive uncertainty as to the duration and consequences of the pandemic, jobseekers can be increasingly inclined to look to careers with established firms rather than early-stage start-up businesses. [21]

The initial outcomes of the financial measures show that comparably more productive firms had a higher probability of acquiring guaranteed loans or other supports. [22] By the same token, it is discerned that loan guarantees gave 'riskier' firms a chance to attain financing, when these businesses would not have been able to prove their capacity for repayment to lenders in ordinary market conditions. [23] These findings are not as contradictory as they may seem at first glance. In essence, financial support measures contributed to harnessing the potential productivity of businesses that possess innate risks – risks which exist regularly because of those business' investment in innovative, but untested and unfamiliar, activities or novel technologies.

Even if the measures outlined in this section stemmed from exceptional circumstances, the persisting question is whether there is a continuing need for specialised funding facilities. As recognised by Federico Fabbrini, path dependency can influence the development of economic processes or governance arrangements. [24] In effect, the longer a measure is in place, the more difficult it becomes to dislodge. The contrary view would be that a support measure becomes obsolete and unused as soon as an emergency or crisis wanes. For commentators like Fabbrini, both possible eventualities have a bearing on discussions concerning legal reforms (such as EU constitutional amendments) to enable the establishment of exceptional initiatives. By allowing for a flexible application of State Aid rules under Article 107 of the Treaty on the Functioning of the European Union (TFEU), the adoption of the EU's Temporary Framework for State Aid in March 2020 can be seen as a provisional and

[20] ESCB Expert Group on Productivity, Innovation and Technological Change, 'The Impact of the COVID-19 Pandemic and Policy Support on Productivity' (2024), p. 47.

[21] M. Pagano and J. Zechner, 'COVID-19 and Corporate Finance' (2022) 11 *Review of Corporate Finance Studies* 849, 861.

[22] ESCB Expert Group on Productivity, Innovation and Technological Change, 'The Impact of the COVID-19 Pandemic and Policy Support on Productivity' (2024).

[23] G. Jiménez, L. Laeven, D. Martinez-Miera, and J.-L. Peydró, 'Public Guarantees, Private Banks' Incentives, and Corporate Outcomes: Evidence from the COVID-19 Crisis' (ECB Working Paper No. 2913) (2024).

[24] F. Fabbrini, 'The Legal Architecture of the Economic Responses to COVID-19: EMU Beyond the Pandemic' (2021) 60 (1) *Journal of Common Market Studies* 186, 195.

less formal, but necessary, step in enacting legal procedures for extraordinary intervention in the interests of the EU's economy. [25]

If there are renewed calls for further reforms to introduce designated support measures and policies for times of emergency or crisis, additional thought should be put towards the purposes of these measures. The experience gained from the pandemic should be the guiding standard. Most crucially, measures which are oriented towards short-term objectives of maintaining business liquidity cannot be conflated with measures that are gravitated towards shielding the longer-term solvency and viability of businesses.

From liquidity to solvency: Distinct phases of public supports

The above summary could give a false impression that meeting liquidity demands was the constant determinant of public intervention since the advent of the pandemic. It is possible to delineate distinct phases of financial support measures. However, it should also be acknowledged that the availability and uptake of measures dwindled as the perceived threats to public health abated. As stated by the ESRB, support measures decreased most notably between the final quarter of 2021 and the second quarter of 2022. Loan moratoria were almost entirely phased out by the end of 2021, while applications for guaranteed loan facilities were planned to be ended by most ESRB member states from late 2022. [26] Although supports have gradually been cast aside by jurisdictions within the EU and beyond, the types of measures and initiatives which were created – and the differing phases through which these supports evolved – represent salutary examples for any future mechanisms to promote business growth, innovation and sustainability.

As expressed by the ESRB, "[l]iquidity measures have consistently been the dominant form of the COVID-related support, but solvency support has increased over time." [27] If a timeline can be drawn for when the aims of financial support measures began to reformulate, the ESRB indicated that the first quarter of 2021 revealed an increase in solvency-centred

[25] Communication from the European Commission, 'Temporary Framework for State Aid Measures to Support the Economy in the Current COVID-19 Outbreak' (20 March 2020); OJEU C 91 I/01.
[26] ESRB, *Fiscal Support and Macroprudential Policy – Lessons from the COVID-19 Pandemic* (2022), pp. 3–4.
[27] ESRB, *Fiscal Support and Macroprudential Policy – Lessons from the COVID-19 Pandemic* (2022), p. 5.

supports, relative to liquidity-focused measures. [28] The quantity of direct grants to support viable businesses increased generally, even though liquidity measures (such as guarantees) retained their status as the most common category of supports, both in governmental announcements and in uptake. [29]

A change from liquidity to solvency involves more than a simple decision to deploy direct grants to individual businesses. A range of factors must be taken into account for support measures to suitably protect the solvency of a business. The most salient considerations are a business' viability as a profitable going concern, the strength of an underlying business model, and the capacity for repayment by demonstration of creditworthiness.

As emphasised by the ESRB, a 'tweaking' of measures – from a liquidity focus, towards a solvency lens – can accomplish a reduction in longer-run financial stability implications. [30] In this reasoning, solvency is deemed to be the equivalent of viability, whereby targeted measures need to differentiate between firms which can raise funds privately on their own initiative, firms which have viable prospects and are struggling to generate capital, and firms which do not have a definitive ability to survive. For instance, by looking to the probability of loan default (PD) as a yardstick of viability, businesses in the manufacturing and transport sectors could be identified as being fundamentally more vulnerable in the longer-term, in contrast to other businesses which are confronted with more immediate liquidity difficulties resulting from a pandemic-like crisis scenario (such as in the hotel, restaurants and hospitality sectors). [31]

Modifications, or amendments, of support measures can only occur when the original severity of a crisis eases. As reported by ESRB member states, there was little requirement for restructuring arrangements pertaining to guaranteed loans or moratoria in the earliest stages of the pandemic. [32] However, as time progressed, "more targeted support" was being supplied

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[28] ESRB, *Monitoring the Financial Stability Implications of COVID-19 Support Measures* (2020), p. 3; available at: https://www.esrb.europa.eu/pub/pdf/reports/esrb.20210908.monitoring_the_financial_stability_implications_of_COVID-19_support_measures~3b86797376.en.pdf (date accessed: 9 June 2024).
[29] ESRB, *Monitoring the Financial Stability Implications of COVID-19 Support Measures* (2020), p. 4.
[30] ESRB, *Monitoring the Financial Stability Implications of COVID-19 Support Measures* (2020), p. 7.
[31] See ESRB, *Fiscal Support and Macroprudential Policy – Lessons from the COVID-19 Pandemic* (2022), p. 12.
[32] ESRB, *Fiscal Support and Macroprudential Policy – Lessons from the COVID-19 Pandemic* (2022), p. 9.

to "affected sectors or firms with attested viability." [33] There is an inevitable riposte to this advocacy for more solvency-focused measures. When a crisis of the nature of a global pandemic strikes, it can be anticipated that governments will first want to concentrate on relieving the liquidity needs of businesses. Crisis decision-making does not afford scope for pragmatic calls as to which firms are most deserving of supplementary funding. The same dilemmas exist for private financial institutions.

Under the EU's Capital Requirements Regulation (CRR), [34] a PD denotes the default probability of a counterparty over a one-year period. [35] In a crisis context, a prospective judgment of default, looking a year ahead, can be tough to achieve. Banks and other institutions may agree to forbearance by not enforcing against a borrower "that is experiencing or is likely to experience difficulties in meeting its financial commitments." [36] Private and informal forbearance and restructuring arrangements between banks and borrowers were a hallmark of the pandemic years, [37] in addition to the breadth of public financial supports. Although there can be weaknesses connected to bank discretion – as noted with moral hazard concerns in the use of guaranteed facilities – the participation of financial institutions is pivotal to concerted public-private efforts to assist struggling businesses. As elaborated on in the forthcoming second article, the role of banks will be inextricably tied to the feasibility of future measures to promote specified public policy objectives.

The task of 'diagnosing' the solvency of a business can be exacerbated by how ripple waves of a crisis or shock may affect particular businesses and sectors more disproportionately than others. Businesses which were in a healthy condition prior to the pandemic rapidly found themselves in a mire of cash flow issues. At the same time, the rising tide of liquidity demands camouflaged the pre-existing vulnerabilities of businesses which were already falling behind on repayments to creditors during the period preceding the pandemic. This 'asymmetric' trait of the cross-sectoral shock is underscored by the 2021 commentary of

[33] ESRB, *Fiscal Support and Macroprudential Policy – Lessons from the COVID-19 Pandemic* (2022), p. 23.
[34] Regulation (EU) No. 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No. 648/2012; OJ L 176/1 [hereinafter 'CRR'].
[35] CRR, Article 4(1)(54)
[36] As provided for through Article 47(b)(1) of the CRR. See also EBA, *Closure Report of COVID-19 Measures* (2022), para. 37.
[37] See Irish data on the use of forbearance during the pandemic in S. Sweeney and A. Kearns, 'Forbearance During the COVID-19 Crisis in 2021: Who Has Needed Lenders' Support?' (Central Bank of Ireland, December 2021); available at: https://edit.centralbank.ie/statistics/statistical-publications/behind-the-data/forbearance-during-the-covid-19-crisis-in-2021 (date accessed: 9 June 2021).

Ryan Banerjee, Joseph Noss and Jose Maria Vidal Pastor for the Bank for International Settlements (BIS). [38] Some exposure was felt across all sectors, but consumer-facing firms were instantly hit. Over time, other sectors may incrementally encounter the most enduring indebtedness, closures, and insolvencies. As charted in the findings of Banerjee, Noss and Vidal Pastor, businesses such as those in the hotel, restaurant and leisure sector carried the brunt of the original liquidity risks. However, the most substantive and long-term balance sheet risks materialise for other sectors – for example, in construction – as lockdowns, restrictions and social distancing guidelines are removed. [39]

As explicated in the next section, the losses resulting from liquidity risks were attended to by an array of financial measures launched since the start of the pandemic, irrespective of whether this response can be categorically regarded as 'successful'. As an indication of how radically unparalleled a shock the pandemic was, the attention devoted to liquidity "stands in sharp contrast to tight credit conditions" after the Global Financial Crisis. [40] In the summation of the ESRB, [41] the initial preoccupation with tackling liquidity problems could be viewed as an essential 'react' phase in responding to financing concerns. The next – and arguably more contentious phase – is to 're-assess', by keeping supports targeted towards the solvency of viable businesses. A final phase is to 'rebuild', or 'repair', which should address the 'scarring' implications of the pandemic for economies. As argued in the forthcoming second article, an integral element of future economic rebuilding should be the use of financial support measures for identified public policy objectives, based on the allocation of funds towards businesses with demonstrably robust solvency.

When placing all of this emphasis on the meaning of 'solvency', it is necessary to be cognisant of the corollary: the insolvency of businesses. Corporate insolvency, rescue and debt restructuring processes serve a function of separating viable companies from companies which do not have realistic possibilities of survival as going concerns. If solvency-oriented financial supports are to be widely used in future for public policy interests, these measures

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[38] R. Banerjee, J. Noss, and J. M. Vidal Pastor, 'Liquidity to Solvency: Transition Cancelled or Postponed?' (BIS Bulletin No. 40) (March 2021).
[39] Banerjee et al, 'Liquidity to Solvency: Transition Cancelled or Postponed?' (BIS Bulletin No. 40) (2021), Table 1, p. 3.
[40] Banerjee et al, 'Liquidity to Solvency: Transition Cancelled or Postponed?' (BIS Bulletin No. 40) (2021), p. 4.
[41] ESRB, *Prevention and Management of a Large Number of Corporate Insolvencies* (April 2021), Figure 2, p. 15; available at: https://www.esrb.europa.eu/pub/pdf/reports/esrb.report210428_PreventionAndManagementOfALargeNumberOfCorporateInsolvencies~cf33e0285f.en.pdf (date accessed: 9 June 2024).

must be assuredly accompanied by accessible and efficient insolvency and rescue processes. Financial support measures cannot be misallocated towards propping up businesses that do not have the ability to survive as going concerns. As an analysis which will be expanded on in the second article, the potential for indelible economic damage (through long-term legacy indebtedness or debt overhang, and corporate 'zombification') can be diluted by a "well-prepared insolvency and restructuring regime to prevent permanent losses of tangible capital stock." [42]

It could appear all too easy to make sweeping arguments for a grand fabric of complementary legal frameworks. The complexities arise in choosing which businesses should warrant support on the basis of solvency and then, in adjudging when support measures are, in fact, successful or, at the very least, satisfying the objectives for which they were established.

How to quantify success?

In view of the emergency context in which financial support measures were introduced, it may be inappropriate to attempt to brand measures as being successful or unsuccessful. The 'firefighting' semblance of most of the measures would imply that merely saving businesses from the possibility of rapidly spiraling liquidity and cash flow problems should be expected to be the most practicable outcome. Nonetheless, as the dust settles, the efficacy of support measures from the pandemic years is being realised. In developing its findings from a survey of approximately 12,000 European firms, the European Investment Bank (EIB) report for 2023/2024 affirms that "[p]ublic intervention at the national and EU level has played an essential role in cushioning the effects of shocks, allowing investment to recover strongly, driven first by households and more recently by companies." [43] Although the same report predicted a decline in firms' rate of investment for the next year, the key findings are commensurate with previous studies of the data yielded from support measures.

[42] J-M. Natal, E. Pugacheva, and S. Albrizio, 'Corporate Indebtedness During COVID-19: The Hangover of the Vulnerable' (VoxEU, 7 June 2022); available at: https://cepr.org/voxeu/columns/corporate-indebtedness-during-covid-19-hangover-vulnerable (date accessed: 9 June 2024).
[43] EIB, *Investment Report 2023/2024: Transforming for Competitiveness* (EIB, 2024), p. 3.

The research of Peter Harasztosi and others (as already cited in this article) was grounded in the EIB's 2021 survey results. [44] One of the foremost findings from the study is that there was no evidence to suggest that financial support was tilted towards firms that were weak, significantly distressed, or highly indebted in the period before the pandemic. For the authors, there were no factual foundations for arguments relating to moral hazard – that is, the wasteful use of public funds in intentionally selecting unviable businesses for support.

This appraisal corresponds to evidence on the correlation between the size of financial support measures and the frequency of corporate failures. International Monetary Fund (IMF) statistics disclose that decreases in the bankruptcies of companies were more pronounced in accordance with how large a particular financial support programme was. [45] The reduction can also be attributed to other policies, such as the forbearance being exhibited by banks, but the findings reveal the direct link between financial support measures and fewer business failures. Even though the IMF data applies just to 2020, the same tapering off in the numbers of corporate insolvencies was visible across EU Member States from 2020 onwards. This plateau effect on insolvencies – and the consequent apprehension about future surges in insolvencies – is considered in further depth in the second article when assessing economic scarring in the years following the pandemic.

Financial support measures may have helped to preclude business failures, but at the cost of having companies become substantially more leveraged. As set out in ESRB findings on companies within ESRB member states, corporate borrowings increased throughout 2020 and partly in 2021. [46] The cumulative effect was an increase in companies' average gross bank debt ratio (the proportion of a company's bank debt to the value of its total assets) to almost 40% in the space of a single year. As articulated by Marco Pagano and Josef Zechner, the liquidity supports for businesses may well have produced enhanced resilience to the shocks generated by the pandemic, but there are 'downsides' which should be highlighted.

For Pagano and Zechner, "…the abundance of credit has made small firms considerably more levered, and the very strength of the policy response has eroded both fiscal space and scope

[44] Harasztosi et al, 'Firm-Level Policy Support During the Crisis: So Far, So Good?' (2022) 171 *International Economics* 30.
[45] Battersby et al, 'The State as Financier of Last Resort' (IMF SDN 2022), Figure 8, p. 8.
[46] ESRB, *Fiscal Support and Macroprudential Policy – Lessons from the COVID-19 Pandemic* (2022), p. 12.

for monetary easing in response to future shocks." [47] As reiterated in the second article, the pressure on state finances is a catalyst for imminent reforms to EU fiscal rules. For businesses, the combination of supports during the pandemic may constitute a short- to medium-term windfall but could prove tantamount to a long-term debt burden. As conceded by Pagano and Zechner, "[t]he effects that such a panoply of policy interventions had on companies are obviously very hard to assess, not least because of their mutual interaction." [48]

Aside from corporate borrowers, financial institutions also needed to face the consequences of credit decisions sanctioned during the pandemic. As noted by the EBA, the asset quality of loans which were subject to moratoria deteriorated promptly relative to average loans. [49] Commercial real estate loans with expired moratoria were quickly re-classified by banks. [50] Loans which were subject to public guarantee facilities have also deteriorated in asset quality, which has equally instigated re-classification moves by banks. [51] Although the state exposure applies to guarantee loans for longer durations (for over five years in some instances), the maturity periods for guarantee facilities constitute a persisting drain in banks' asset quality. [52] However, any worries for the condition of financial institutions' assets could be undue. As of the final quarter of 2023, the capitalisation of EU and European Economic Area banks stands at record levels. [53] The more latent risks are for corporate borrowers in the form of a possible increase in non-performing loans.

When insisting on the essential role of public intervention to tackle liquidity problems, the EIB's 2024 report proceeded to convey how European firms were able to keep investing during the pandemic, "notably through greater investment in digitalisation, energy efficiency and diversifying their supply chains", thereby "embarking on needed transformation." [54] Similar insights are alluded to in the work of Lilas Demmou and Guido Franco, in accounting for how the pandemic opened new business opportunities and how certain industries

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[47] M. Pagano and J. Zechner, 'COVID-19 and Corporate Finance' (2022) 11 *Review of Corporate Finance Studies* 849, 851.
[48] M. Pagano and J. Zechner, 'COVID-19 and Corporate Finance' (2022) 11 *Review of Corporate Finance Studies* 849, 871.
[49] EBA, *Closure Report of COVID-19 Measures* (2022), para. 56.
[50] EBA, *Closure Report of COVID-19 Measures* (2022), para. 57.
[51] EBA, *Closure Report of COVID-19 Measures* (2022), para. 61.
[52] EBA, *Closure Report of COVID-19 Measures* (2022), para. 60.
[53] EBA Risk Dashboard, Q4 2023; available at: https://www.eba.europa.eu/publications-and-media/press-releases/eu-banks-are-robust-signs-credit-quality-deterioration-are-becoming-apparent-ebas-risk-dashboard (date accessed: 9 June 2024)
[54] EIB, *Investment Report 2023/2024: Transforming for Competitiveness* (EIB, 2024), p. 5.

(especially revolving around information technology) “faced an even higher path of business formation than during the previous years…” [55]

On the other hand, this Phoenix-rising-from-the-ashes conception can be overestimated. As Harasztosi and others demonstrate, there is only “some evidence” that the policy support during the pandemic enabled the financial expansion of firms’ investments and that support “could have” hastened business digitalisation. [56] Although the authors’ research contains findings of improved optimism among firms about investment outlook, it would be misplaced to regard financial support measures during the pandemic as being fundamentally geared towards accelerating a prevalent transformation of business practices towards innovation, sustainability, and digitalisation. As reiterated in the preceding section, the various measures were primarily directed towards immediate and short-term liquidity concerns in a crisis setting.

If there are expectations about financial measures’ ability to boost commercial transformation, rigorous data collection will be vital to determining the results of the allocation of public funds. It is only by reference to empirical outcomes that a judgment can be made as to whether an initiative is satisfying the purposes for which it was implemented to achieve. As manifest from this section, there are currently no obvious methods of tracking the success of a financial support measure. As endorsed by the IMF’s research, “new analytical capabilities” should be cultivated with governmental departments and ministries, in addition to information channels for administrative agencies. [57] Support programmes should be underpinned by transparency, involving regular updates on cost-benefit factors. Moreover, the consistent provision of information can facilitate decisions on when supports should be withdrawn, since a premature ending of a measure could have tangential, but profound, effects for businesses across multiple economic sectors. This is a warning which resonates with the ESRB view that “[a]ssessing whether the expiration of measures remains aligned with the economic recovery is important.” [58]

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[55] L. Demmou and G. Franco, ‘From Hibernation to Reallocation: Loan Guarantees and Their Implications for Post-COVID-19 Productivity’ (OECD Economics Working Paper No. 1687) (2021), pp. 31 – 32.
[56] Harasztosi et al, ‘Firm-Level Policy Support During the Crisis: So Far, So Good?’ (2022) 171 *International Economics* 30.
[57] Battersby et al, ‘The State as Financier of Last Resort’ (IMF SDN 2022), p. 20.
[58] ESRB, *Monitoring the Financial Stability Implications of COVID-19 Support Measures* (2020), p. 15.

In building towards the second of these two articles, it can be argued that the pandemic has forced a re-visiting of the objectives of financial support measures. The broad-based approach towards liquidity demands should be examined within its context of an unprecedented crisis situation. This line of reasoning again resonates with an ESRB conclusion that "… should fiscal support be made available, the response to the COVID-19 pandemic shows the importance of defining clear objectives, targeting support and carefully monitoring and evaluating the effects of such measures." [59] There are other aspects of the pandemic response which could be core to future measures, particularly the participation of financial institutions in creditworthiness assessments in the approval of guaranteed loan facilities and the prioritisation of solvency over liquidity in deciding when supports should be extended to eligible businesses.

By questioning how the success of financial measures can be gauged, this section may have taken a circumspect view of the benefits of the measures. However, when vindicating the use of public support mechanisms for policy goals in future, it is worth returning to a finding in the EIB's report in respect of the ongoing value of these measures. As expressed in the report, "[g]overnments across the European Union paid a heavy price for reducing public investment in the aftermath of the euro debt crisis" and this experience was instructive in the maintenance of investment during the pandemic. In turn, it strengthened an understanding "that public investment is not just an expenditure item in the current budget, but rather benefits society for many years." [60]

Conclusion

This first article focused on how the effects of the pandemic-era financial support measures can be judged. In so doing, the article implicitly recognises that developments will continue apace in how corporate indebtedness may transpire and in how support initiatives could be adjusted for differing public policy goals. The purposes and variations of measures were considered, before outlining the progression from a fixation on addressing liquidity concerns exclusively, and, finally, contemplating how the success of financial support measures could plausibly be quantified.

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[59] ESRB, *Fiscal Support and Macroprudential Policy – Lessons from the COVID-19 Pandemic* (2022), p. 24.
[60] EIB, *Investment Report 2023/2024: Transforming for Competitiveness* (EIB, 2024), p. 89.

The article weighed the advantages and drawbacks of the efforts made to assist businesses since the outbreak of the pandemic. Although much remains to be ascertained about the longer-term effects, the approaches taken may proffer informative examples of how to design effective measures for future years. The forthcoming second article will proceed from a rather more pleasant starting point of a life beyond the pandemic. The next article's argument flows from the proposition that public supports still have a role to play in striving promoting objectives of EU policy, law and regulation. However, this role must be informed by the experience of the pandemic era and by how adept financial support measures will be in resolving any potential scarring of the EU economy.