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CORPORATE BAILOUTS

Business-as-usual or opportunity for fostering socio-ecological transition?

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1 INTRODUCTION

The economic impact of the pandemic has revived the discussion on bail-outs of distressed firms whose solvency is at risk. To date, the majority of interventions by public authorities have focused on ensuring the liquidity of enterprises through guarantees, loans, moratorium/deferral of their obligations and delay of insolvency proceedings. Both European countries and the U.S, however, have already completed bailouts, which comprise equity capital injection, mainly in the aviation and transport sector[2].

These individual cases are considered to be early signs of an expected increase of companies that will need capital support during next months[3]. Many analysts foresee the necessity to inject significant financial resources in order to prevent the risks of a major solvency crisis leading to mass bankruptcies[4]. The European Commission has estimated these needs for the European economy at 720 billion euros for 2020 according to its baseline scenario and up to 1.2 trillion in the unfavorable one[5]. Recent estimates for the UK indicates that 100 billion pounds could turn unsustainable debt by the end of March 2021 including 35 billion of debt provided to businesses by

[1] Yannis Eustathopoulos, **ENA Institute for Alternative Policies** https://www.enainstitute.org/

[2] Bailout tracker

[3] 'State equity support runs risk of moral hazard', Financial Times, 30.7.2020.

[4] Megginson, W., Fotak, V. (2020) 'Government Equity Investments in Coronavirus Bailouts: Why, How, When?', 14 April 2020. Wilkes, G. (2020) 'Bailout for business after coronavirus', Institute for Government', IfG Analysis, April 2020. Anderson, J., Tagliapietra, S., Wolff, G. (2020) 'Rebooting Europe: A framework for a post covid-19 economic recovery', Bruegel, Policy brief 2020/1, May 2020.

[5] European Commission, "Solvency Support Instrument", Question & Answers, 29.5.2020.

government loan schemes[6]. Consequently, equity injection has been discussed during recent months as a more appropriate tool for supporting the economy in the upcoming stages of the crisis compared to debt funding. Three reasons can be distinguished. First, as the prospects for a strong V-shaped recovery of the economy decline, companies are expected to be reluctant in further increasing their lending even under favourable terms and conditions. Secondly, the provision of loans and guarantees as the main policy answer for sustaining the activity of businesses is expected to reach its limits given that excessive corporate debt growth increases fiscal risks and economic uncertainty. Finally, the rise of corporate debt is expected to harm the intensity of the economic recovery due to the deleveraging strategies that companies will implement following the pandemic episode.

In this context, Germany has provided an amount of 100 billion euros for the recapitalisation of companies and other related measures under the Economic Stability Fund (of a total amount of 600 billion euros)[7]. Similar provisions have been included in the US fiscal stimulus legislation of an amount of 32 billion dollars[8]. The Spanish government has assigned SEPI (State Society of Industrial Participations) to manage the fund to support the solvency of strategic companies which is endowed with 10 billion euros[9]. In May, the European Commission presented a proposal for the creation of a 32 billion euros 'Solvency Support Instrument' aiming at mobilising 300 billion euros in order to recapitalise businesses[10]. This proposal however has not been included in the European Council's conclusions of 21 July 2020[11]. No clarification on the rationale of this choice has been provided until now.

It should be noted that rescuing large sections of the economy seems like moving in uncharted waters for policy makers. Although governments have been recently

[6] 'Supporting UK Economic Recovery Recapitalising Businesses Post Covid-19', TheCityUK, July 2020.
[7] Wirtschaftsstablisierungsfonds – "WSF" https://www.wfw.com/articles/economic-stability-fund-for-the-german-economy-executive-summary/
[8] '9 things to know about the historic US coronavirus bail-out package', World Economic Forum, 28.3.2020.
[9] 'Three companies have already requested more than 700 million from the Government rescue fund', Offthebus.net, 11.9.2020.
[10] Questions and Answers: Solvency Support Instrument
[11] 'Council brokers historic stimulus pact as budget cuts, rule of law retreat plague deal', Euractiv, 21.7.2020.

involved in the bailout of financial institutions during the 2008-2009 crisis, experience concerning the rescue of non-financial businesses is more limited and remote in time (i.e. restructuring cases in the industrial sector in the 1970s and 1980s). For this reason, the discussion and literature on the approaches, criteria and tools of non-financial bailout policies are more limited, resulting in a significant number of "open issues".

2 DILEMMAS & TRADE-OFFS

The public debate on bailouts highlights a number of significant dilemmas and necessary trade-offs regarding the design of public policies. Various questions remain open:

- Public Finances: What is the balance which need to be achieved between the "health" of public finances and the rescue of a country's productive basis?
- Size: Do bailouts need to be restrained to a limited number of "strategic" companies in order not to disrupt market-driven industrial restructuring processes? To what extent and in which cases "creative destruction" should be maintained in order to avoid a new generation of "zombie" firms deteriorating economic efficiency, productivity and competitiveness? Should SMEs be included in bailout policies and how?
- Criteria: Do governments need to set criteria for selecting the companies to be supported? For example, what would be the appropriate balance, given the finite nature of fiscal resources, between a) large and small enterprises, b) high and low value-added sectors/activities, c) between services (e.g. tourism) and other sectors considered as more "productive" and "resilient" following the pandemic? To what extent the issue of the social and climate/environmental footprint of businesses must be taken into account and how?
- Conditionalities: Is it sound to introduce conditionalities on companies receiving state support such as environmental commitments? If so, at what stage of the economic cycle? How demanding and binding should these conditions be? Is there a trade-off between the speed and intensity of the economic recovery on the one

hand and, on the other hand, the compliance to environmental and other public policy objectives that will determine the sustainability of future economic growth?

- State Ownership Policy: Should the public sector maintain the shares that it will acquire as a result of bailout plans in order to ensure sufficient support and monitoring of business model transformation or should it withdraw as soon as possible in order to avoid market distortions? What should be the role and rights of the state as a shareholder? Can ownership policy of the state be a relevant tool in the current crisis?
- Competition: How does bailout influence market competition? On the one hand, bailouts can induce competitive distortions both at the national and European level. On the other hand, non-bailouts of firms in countries more impacted by the crisis and with fewer fiscal margins can rise inequalities further across member states, increase market concentration and harm the European Single Market.
- Public Policies: Lastly, is there a need to mobilise and enhance public actors (agencies, development banks, wealth funds, research institutes, etc.) to support business restructuring and transition towards sustainable activities?

3 MAPPING THE PUBLIC DISCUSSION

The review of the public debate and recent literature on the above issues highlight both elements of agreement and disagreement.

3.1 COMMON GROUND

Overall, opinions expressed in the public discussion seem to converge on the following issues:

- First, the need to protect the productive system and employment from the impact of a recession that is not reduced to purely economic factors is widely acknowledged. The protection of the "social value"[12] of enterprises requires the

[12] The creation of new business after the crisis will: a) induce much higher costs in comparison with the cost of protecting existing productive capacities, b) be subject to uncertainties, c) require time. Blanchard, O., Philippon, T., Pisani-Ferry, J. (2020) 'A New Policy Toolkit Is Needed as Countries Exit COVID-19 Lockdowns', Peterson Institute for International Economics, Policy Brief 20-8, June 2020.

partial and provisory suspension of policies and arguments that fall within the logic of "creative destruction". The extent and duration of this suspension is however subject to different interpretations and is evolving according to developments in various fields (economy, public policies, pandemic crisis).

- During recent months, more and more opinions in favour of direct state equity capital injection aiming at maintaining solvency emerged in the public sphere. This trend though seems to be declining now.
- There is a consensus on the necessity to establish objective criteria for the selection of companies to be supported in order to protect countries against wider systemic risks arising from increasing public debt levels. Nevertheless, opinions differ on the criteria to be established.
- The prioritisation of companies of strategic importance for the economy, national security and self-sufficiency in basic goods and employment is largely accepted (e.g. energy, telecommunications, pharmaceutical industry, arms industry).
- There is a rather broad agreement on the importance –according to the experience of previous bailouts- of the speed and size of the intervention to avoid the "too little - too late" syndrome.
- Finally, it is broadly accepted that partnerships between public development agencies, banks and other entities based on clear roles, rules and procedures are necessary to ensure a flexible, effective and timely management of the volume of cases that the State will need to cope with.

3.2 CONFLICTING APPROACHES

Despite a relative consensus on the above points, significant up to fundamental differences can be observed in five key areas.

Magnitude of bailouts

The extent and objectives of bailouts seems to be an issue of growing discrepancies. Following the rejection of the 'Solvency Support Instrument' by the European Council in July, opinions expressed in the public sphere on the impact of the crisis tend to move gradually from the necessity of extensive bailouts to the necessity of policies for the "anticipation and management of change"[13]. Restructurings may gain in legitimacy as an instrument for avoiding bankruptcies and insolvency and are implicitly associated with the necessity to withdraw from sectors belonging to the "old economy" (heavy industry) or to reduce the importance of sectors which proved non-resilient during the pandemic crisis (e.g. tourism) in order to develop activities of higher productivity and innovation such as telecommunications, artificial intelligence and green technologies[14]. It should be mentioned that this approach neglects the transformational potential of conventional economic activities, namely the greening of their productive procedures and products, their diversification towards new sustainable activities and the improvement of their resilience against economic, health, climatic and geopolitical risks. Overall, the increasing acceptance of market-based internal restructurings causes serious concerns given the rising number of severe cases[15] across European countries and sectors as documented, for example, by the European Restructuring Monitor database[16].

Selection of companies and sectors

Opinions differ on the criteria to be set for the eligibility of companies and industries in need of (capital) support. These differences are largely due to the choices made by each country regarding its model of economic development. The oil and gas industry is more likely to be perceived as a legitimate candidate for bailouts in the U.S than in the European countries, who are generally more inclined towards the selection of activities contributing to climate neutrality. Perceptions also differ for example regarding SMEs. For example, opinions in Greece during the last decade of structural adjustment have systematically blamed SMEs for the economy's structural weaknesses (low productivity and innovation, contribution to the growth of non-tradable sectors, role in undeclared work and tax avoidance). Approaches of this

[13] Kirton-Darling, J., Barthes, I. (2020), 'Anticipating the Covid-19 restructuring tsunami', Social Europe, 3.9.2020.
[14] Münchau, Wolfgang, 'Europe needs to avoid a 'decade of forbearance', Financial Times, 30.8.2020.
[15] See for example restructuring cases leading to redundancies of thousands of workers such as Fraport, Booking.com, Marks and Spencer, Continental, MAN Energy Solutions.
[16] Restructuring events database, European Foundation for the Improvement of Living and Working Conditions.

nature have more generally a direct impact on the shaping of bailout programmes in favour of (or exclusively for) large enterprises. On the opposite, some analysts focus on the importance of value chains and network of SMEs as key-drivers for the protection of employment and productive capacities, advocating thus for their inclusion in bailout policies.

Contradictions between various criteria also tend to complicate policy-making and public discussions. In case of businesses facing for example long-standing economic difficulties before the pandemic, the criteria of economic sustainability may conflict with the "large employer" criteria or with the importance of some sectors and companies for strategic issues and the local economy. Similar contradictions are often observed between environmental and social dimensions. In other words, tackling the economic impact of the pandemic has made imperative and urgent the necessity to provide comprehensive, clear and consensual responses to critical challenges such as climate change mitigation and adaptation, the issue of "just transition" and the societal impact of the 4th industrial revolution (4IR) and the digital economy.

The issue of conditionalities

Significant discrepancies are also observed regarding both the necessity of setting social and environmental conditionalities as well as regarding their time of introduction, extent, binding nature etc. Many of the recent conditionalities associated with climate goals do not seem to bring significant changes beyond existing objectives, obligations and commitments of businesses[17]. Moreover, when they do, the degree to which they are truly binding is questioned[18]. The same remark has been made for other conditionalities which have been announced by governments such as the relocation of industrial units (e.g. France/car industry) or the exclusion of companies associated to tax heavens (e.g. Poland, France, Denmark, Belgium)[19]. The real outcome of announcements made by government officials regarding the

[17] 'Air France's bailout 'climate conditions' explained', Transport & Environnent, 3.6.2020.
[18] Delépine, J. (2020), 'Quelles contreparties exiger des entreprises aidées?', Alternatives Economiques, 28.5.2020.
[19] A common definition of tax heavens is based on the "EU black list". However, as mentioned by the Tax Justice Network, "All iterations of the EU's blacklist since the first list in 2017 have never covered as much as 10 per cent of the world's financial secrecy services".

regulation of dividends, bonuses and shares buybacks will need to be assessed[20]. Beyond these rather unambitious, unclear or weak conditionalities, arguments in favour of the absolute prioritisation of an -as much as possible- strong economic recovery could gain in influence among policy-makers[21]. Under this approach, conditionalities are deemed counterproductive with the exception of clauses imposing “aggressive” restructuring plans aiming at restoring profitability through job cuts, reduction of wages and other benefits for employees, etc. For example, the Troubled Assets and Relief Programme (TARP) implemented in the U.S during the 2008-2009 crisis enforced such plans in the automobile sector (e.g. General Motors, Chrysler)[22].

The role of the state as a shareholder

Lastly, fundamental differences are observed in terms of the rights, the role and the legitimacy of the state as a shareholder following bailout and recapitalisations. The state is often perceived as an actor leading to systematic deviations from efficient and profit-maximising management and to distortions of market competition. In other words, state participations are considered to be inherently associated with the risk of “politicisation” of the economy. On the opposite, the idea of a state assuming the role of a long-term investor in companies with the aim to foster restructuring procedures and innovation towards more sustainable activities has been expressed both in Europe and the U.S in public discussions[23].

[20] ‘France puts dividends payments into ‘confinement’ amid COVID-19 crisis’, Euractiv, 30.3.2020. Pay no dividends Bank of England tells City institutions’, Evening Standard, 4.6.2020. ‘UK bailout scheme companies barred from paying bonuses and dividends’, Financial Times, 19.5.2020. ‘Germany wants firms to suspend dividends for virus aid’, Bloomberg, 30.3.2020.

[21] Wilkes, G. (2020) ‘Bailout for business after coronavirus’, Institute for Government’, IfG Analysis, April 2020.

[22] Abate C., Elgouacem, A., Kozluk, T., Stráský, J. Vitale, C. (2020) ‘State ownership will gain importance as a result of COVID-19’, VoxEu, 7.7.2020. Canis, B., Webel, B. (2013) ‘The Role of TARP Assistance in the Restructuring of General Motors’, Congressional Research Service.

[23] Hockett, R. (2020) ‘The US must take equity stakes in the companies it rescues’, Financial Times, 28.3.2020. Mazzucato, M. ‘We Socialize Bailouts. We Should Socialize Successes, Too’, New York Times, 1.7.2020.

4 CONCLUSION: THE EMERGENCE OF COMPETING APPROACHES

Combined, the above points of disagreement can be translated into two diametrically opposed and competing approaches about the qualitative and quantitative features of bailout policies[24].

4.1 BAILOUT WITH MAINTAINING OF BUSINESS-AS-USUAL TERMS ("MINIMUM SHORT-TERM INTERVENTION")

The first approach opts for short-term interventions with no voting rights for the state based on the experience of the recapitalisation of financial institutions during the crisis of 2008-2009. Public intervention is apprehended as a factor inherently distorting the economy and the market (a temporary "necessary evil"). Under this approach, the introduction of significant and binding social or environmental conditionalities tends to be perceived -for the time being- as unnecessary burden. Some countries with poor records regarding their commitment towards international climate targets and agreements may even proceed unconditionally to the support of carbon-intensive companies. Overall, any real and binding conditions of social and environmental nature are deemed counterproductive and jeopardising the intensity of economic recovery. As a result, the agenda of sustainable development has a minor role within the bailout agenda and is therefore assigned to market mechanisms at a later stage of the recovery. Bailouts focus on selected "too big to fail" or strategic companies. Correspondingly, small and medium enterprises tend to be excluded from the scope of bailout policies. Maintaining a degree of "creative destruction" in the market is also believed to contribute to the recovery of the economy and the elimination of distortions arising from the operation of less efficient enterprises (mainly small and medium), "zombie firms"[25] or industrial sectors considered to be on an irreversible declining path before the pandemic crisis[26]. In this direction, fiscal

[24] Someone will observe in the public discussion "intermediary approaches" combining elements of the "minimum short-term" and "active long-term" interventions.
[25] Natixis, "Zombie firms rather than corporate bankruptcies?", Natixis Flash Economics, 27 May 2020, No 644.
[26] Münchau, Wolfgang, 'Europe needs to avoid a 'decade of forbearance', Financial Times, 30.8.2020

resources should therefore be allocated to activities for the support of redundant staff, re-skilling and re-education.

4.2 BAILOUT AS A MEAN FOR THE SUPPORT OF BUSINESS MODEL TRANSITIONS ("ACTIVE LONG-TERM INTERVENTION")

The second approach sets clear criteria for companies to be included in bailout policies. The aim of the public intervention is to take advantage of the current situation to support actions for the transformation of companies and the productive system towards resilient, sustainable and knowledge-intensive activities in order to cope with critical climate, technological, social and other "mega-trends". This process requires a structured and steady contribution of the state through modern development agencies and policies that operate on the basis of high professional criteria and conditions of transparency such as public development banks, public wealth funds and agencies, bodies for the support of small and medium enterprises, micro-credit institutions, instruments for the transfer of businesses to employees, etc. In this context, public authorities focus on capital provision for SMEs through specially tailored policies and tools (equity or equity-like mechanisms). Overall, the state exercises its full rights as a shareholder. Instead of being limited to a simple lender of last resort, the state is called upon to regain its role as an "investor of first resort"[27] to support major societal transformations and goals such as the green transition or to recover a certain intervention capacity (beyond the regulatory one) through participations in companies operating in oligopolistic markets of key-importance for economic, social and territorial cohesion such as energy, transport, telecommunications and the digital economy[28]. This role is considered as the only relevant policy option for securing the long-term interests of taxpayers, strengthening the resilience of the economy and, consequently, minimising the fiscal and socio-economic risks of new unpredictable crises.

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[27] Mazzucato, M. '[We Socialize Bailouts. We Should Socialize Successes, Too](#)', New York Times, 1.7.2020.

[28] Eustathopoulos, Y., Lampropoulou M., (2018) '[Nationalisation - Privatisation: beyond the «either/or» dilemma. Towards the emergence of mixed regulation patterns?](#)', Institute for Alternative Policies, February 2018.

	Minimum short-term intervention	Active long-term intervention
Criteria for the selection of enterprises	• Solvent before the pandemic	• Solvent before the pandemic • Support to business models which are compatible with the values and priorities of sustainable development • Exclusion of companies connected to tax heavens
Conditionalities	• Rejection of binding and demanding conditionalities (except standard restructuring plans involving redundancies) • Creating conditions of accelerated growth as soon as possible is an absolute priority	• Bailout and capital injection in companies is a window of opportunity for accelerating structural change in business models and economic sectors • Imposition of strong social and environmental conditionalities (e.g. non lay-off clauses, reduction in GHG emissions, etc.)
Role of the state as a shareholder	• Clear limitations regarding the participation of the state in the capital of businesses (withdrawal as soon as possible) • No voting rights	• Voting rights • The state as a shareholder becomes an investor of first resort for the support and monitoring of transitions towards more sustainable activities in line with national and European development priorities
Actors involved in the implementation of bailouts	• Bailouts and capital injections implemented through private bank intermediation	• Public / National Development Banks • Wealth funds and public participation agencies • Public Agencies and bodies for SMEs • Private banks
Support of SMEs	• Clear prioritisation of too-big-to fail and strategic companies • Maintaining of market discipline as a channel for restructuring less efficient sectors/businesses	• Design of special tools for SMEs (capital support, provision of expertise and financing for the transition of business models)
Transition & transformation of the economy	• At a later stage and based on market tools and incentives	• Priority of bailouts and based on new partnerships between the public and private sectors
Interest of tax payers	• Fast recovering of the fiscal cost of bailouts through special arrangements (nonconvertible preferred stock/warrants)	• The state receives dividends from its participation in the stock of businesses • The long-term interests of tax payers are promoted through the increase of the resilience and sustainability of the economy which lower the probability of new crisis and their potential economic, social and fiscal impact.
Dividends, buybacks & bonuses	• Strict regulation of dividends and bonuses is not considered necessary • High dividends are perceived as a positive market sign enhancing the prospect of a fast and strong economic recovery	• Strict regulation of dividend policies for enhancing equity, protecting employment and economic activities and tackling cases falling under the “privatisation of profits – socialisation of losses” scheme.

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