

Lessons Learned in Designing and Implementing Support for Small Businesses

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Original post [here](#).

One month into the biggest global bailout of small businesses in history, countries have started to adjust their initial programs to make them more effective. Small and medium sized enterprises (SMEs) account for [90 percent of businesses](#) and a majority of employment opportunities across the world. Even during non-crisis times, many SMEs face constraints in accessing financing. Governments are working to provide exceptional support during the COVID-19 pandemic in order to prevent bankruptcies, unemployment, and a deeper recession.

All countries face the same challenge: how to quickly get funds to the businesses that need them. In response to the challenge, governments have adopted a variety of interventions (see the YPFS blog [here](#)). In this post, we evaluate interventions designed to support SMEs and present nine lessons learned.

Lessons Learned

1. Demand has far exceeded most programs' initial budgets
2. Aligning incentives can encourage more private-sector lender participation
3. Leveraging existing agencies can get money to SMEs faster
4. Including both bank and nonbank lenders can account for multiple sources of SME financing
5. Targeting assistance too narrowly can slow down the provision of support
6. Streamlining the application process can speed up distribution of funds
7. Small businesses may face challenges meeting fixed costs that programs don't cover
8. Some programs inherently require, or benefit from, additional programs
9. Businesses will likely need further government support

1. Demand has far exceeded most programs' initial budgets

In many countries, demand from SMEs for assistance has outstripped the amount governments initially made available. In response, governments have increased the overall allocation of funds to these support programs. In some instances they have also increased the amount available to individual SMEs.

Overall allocation

[Italy](#), a country that suffered particularly early and deeply from COVID-19 has dramatically increased the amount of funds available for loan guarantees. On March 17, the Italian government announced a EUR 100 billion (\$109 billion) loan guarantee program. On April 14, the EC approved a four fold increase (up to EUR 500 billion) of the original program and

announced a new program for the self employed and smaller companies with an unspecified allocation.

In less than two weeks, on April 16, the United States [expended](#) the full \$349 billion Paycheck Protection Program (PPP). On April 22, congressional leaders [reached a deal](#) with the administration to infuse the PPP with an additional \$310 billion.

[Switzerland](#) doubled its initial loan guarantee program allocation from CHF 20 billion (\$21 billion) to CHF 40 billion. [Spain](#) increased its original EUR 100 billion SME support program by EUR 20 billion.

Participation limit

Many countries have increased not only the amount of total funding available in a support program, but also the individual business participation limit. For example, the government of [Singapore](#) increased the maximum loan amount available under its Temporary Bridging Loan Program from SGD 1 million (\$700,000) to SGD 5 million. When [Italy](#) added a new program specifically targeting smaller companies and the self-employed it increased the size of loans eligible for a 100% state guarantee from EUR 25,000 under the previous program to EUR 800,000 in the new one.

2. Aligning incentives can encourage more private-sector lender participation

When the government channels funds through the financial system, it has to ensure that the lenders are properly incentivized to lend the funds to the SMEs.

Guarantee Percentage

Many countries have had to increase the government guarantee rate on the loans they are asking the banks to offer to SMEs. When [Germany](#) expanded its loan guarantee program, it increased the guarantee rate from between 80% and 90% up to 100% after banks were reluctant to take on new risks in the current economic environment. [Singapore](#) increased guarantee rates on a variety of its programs from 80% to 90%. [Colombia](#) increased its guarantee rates from 60% to 90%.

Interest Rate Ceiling

Many governments set interest rate ceilings on the loans that banks offer to SMEs under credit guarantee programs. However, setting this rate ceiling too low can make banks unwilling to participate. The US's PPP [initially](#) set the interest rate at 0.5% but later had to increase the rate to 1.0%.

Waiver for Individual Bank Participation

[Wells Fargo](#) had been lending under the PPP, but it was constrained by an outstanding restriction on balance sheet growth due to previous misconduct. The Federal Reserve temporarily waived the growth restriction on Wells Fargo to allow Wells to issue more loans under the PPP. Because Wells Fargo is an important lending channel for small businesses, this waiver incentivizes it to continue to participate, which will help its small business customers that need funding receive it.

3. Leveraging existing agencies can get money to SMEs faster

Some governments avoid the challenge of structuring programs to appropriately incentivize private sector banks by leveraging pre-existing government agencies that provide loans directly to small businesses without needing to use the banking system as an intermediary. This can lead to quicker delivery of emergency funds.

In response to the COVID-19 crisis some of these countries have increased funding to these agencies to allow them to provide substantially more loans directly to small businesses. For example the [Business Development Bank of Canada](#) announced a CAD 10 billion program that will provide up to CAD 2 million working capital loans with flexible repayment terms to small businesses. [MicroFinance Ireland](#) initiated a new program that provides loans to businesses with less than 10 employees if they have been rejected for financing by a bank. The [European Investment Bank](#), the lending arm of the European Union, has announced a EUR 25 billion credit guarantee program, part of which will be distributed by European countries' development banks.

The US [tasked](#) its Small Business Administration (SBA) agency with the administration of much of its support programs. This includes the PPP as well as direct grants and loans under the SBA's Economic Injury Disaster Loan program. The SBA deployed more than \$350 billion in support to SMEs in two weeks and is expected to deploy a similar amount in the coming days.

4. Including both bank and nonbank lenders can account for multiple sources of SME financing

Because many SMEs do not have existing loans, credit lines, or relationships with traditional banks, some programs include lenders beyond traditional commercial banks or target lenders with expertise to lend to small businesses.

For example, many SMEs in Switzerland do not have bank loans and only bank with [PostFinance](#), the financial services subsidiary of the national postal service, which does not traditionally lend. The Swiss government is temporarily allowing PostFinance to issue loans under its credit guarantee program.

In the PPP, the Small Business Administration (SBA) provides the guarantees, but the financial system issues the loans. Eligible lenders of SBA loans now [include](#) non-bank-entities like PayPal, Square, and Intuit. In the proposed emergency legislation, which appropriates an additional \$310 billion for the PPP, \$60 billion is earmarked for small, midsize, and community lenders, as these lenders typically reach [more of the smaller businesses](#) compared to the large national lenders.

On [April 17](#), the British Business Bank (BBB), which administers the United Kingdom's Coronavirus Business Interruption Loan Scheme (CBILS), announced that a new lender was accredited to lend under the scheme. The new lender, Funding Circle, is the first newly accredited marketplace lending platform in CBILS and is the largest online small business loan provider in the UK. The BBB has accredited additional lenders since the launch of CBILS and will continue to accept applications from new lenders in order to expand the funding options for SMEs.

5. Targeting assistance too narrowly can slow down the provision of support

Policymakers face a trade off between specificity and efficiency in providing support to SMEs.

In general, programs that target specific types of firms require more administrative processes. For example in the United Kingdom, the CBILS was initially limited to borrowers who had failed to secure standard commercial financing. This not only limited the scope of the support but also added administrative burden for lenders and prolonged the process. [Some firms](#) complained that banks were offering standard financing with high interest rates instead of loans under the scheme. In the first two weeks of the program, 130,000 inquiries were received but only 983 loans were approved. The amendment to CBILS eliminated the requirement, thus expanding the eligibility criteria. The UK also announced a credit guarantee scheme for larger companies when the CBILS program was amended, in order to fill the [financing gap](#) for companies that could not participate in CBILS or access the Covid Corporate Financing Facility (CCFF).

Many countries limit programs to firms up to a certain size or maximum turnover. For example, the [Paycheck Protection Program](#) in the US restricts usage to employers with 500 or fewer employees. However, the SBA released additional guidance regarding eligibility to clarify that firms that meet the statutory and regulatory definition of a “small business concern” with more than 500 employees are eligible. The [US program](#) has faced backlash after some larger companies were reported to have received loans under the program, and [Financial Times analysis](#) shows that eighty publicly-traded companies, with ability to raise capital elsewhere, received aid.

6. Streamlining the application process can speed up distribution of funds

By eliminating complexity from the application process, programs can distribute funds to small businesses quickly.

In the United States, small businesses apply directly to their lender. These institutions are responsible for the application process and can utilize their existing interface and online systems though the SBA provides a template application. Thus, borrowers approach the lender, and lenders then [submit information to the SBA](#). However, speed will depend on existing bank infrastructure, system, and staff. In the US where the PPP operates on a “first-come-first-serve” basis, the speed at which an individual lender can process applications influences which small businesses receive aid.

In Switzerland, the government provides a standardized application online which applicants fill out and then take to the lender. The government anticipates that the application should take approximately 10 minutes to complete. In some cases, applicants have reported receiving funds less than an [hour](#) after completing the application. Because credit risk assessments are waived, the Swiss government announced actions to prevent fraud on [April 3](#). The Swiss [guarantee organizations](#) confirm that the loan agreements comply with the requirements and cancel loans that are duplicates or wrongly applied. The loans are also checked systematically by linking VAT and other data to the information provided by companies.

In contrast to the 10 minute application in Switzerland, some countries require more detailed documentation in applications and feature more complex processes. Applications vary across lenders, but in programs with less than a 100% guarantee, lenders bear a portion of the risk. Because of this, credit and risk assessments are often required, but these processes are more time consuming. In Italy, this is cited as a reason why funds are not flowing quickly. Thus, the application process can be a bottleneck to distributing funds

7. Small businesses may face challenges meeting fixed costs that programs don't cover

Some countries establish criteria and restrictions on how funds can be used, which can leave some small businesses with the challenge of finding financing to cover the gap. In the United States, the [Treasury](#) requires that at least 75% of the value of a forgivable loan issued under the PPP will be used for payroll expenses. Some [firms worry](#) that this support does not go far enough, especially for firms with high rent costs. Employee compensation is capped at an annualized \$100,000 per employee under the PPP. Other countries developed or expanded wage subsidy programs which are specifically designed to cover payroll costs.

In Denmark, the government [announced a program](#) to cover a certain percentage of fixed costs of companies that have been impacted by the COVID-19 pandemic. The government will cover between 25 to 100% of fixed costs. Denmark also announced a wage subsidy program for firms forced to decrease work hours of employees or temporarily lay them off. By providing support for fixed costs in addition to payroll expenses, Denmark addresses a gap faced by other programs.

8. Some programs inherently require, or benefit from, additional programs

Providing support to one type of business or one sector of the economy sometimes disadvantages a different business or sector. Governments have had to introduce a number of complementary programs in tandem or introduce new programs in response to outcomes from previously announced programs.

Funding for Lending and Guarantees

A number of countries have paired credit guarantee programs with funding for lending programs. These programs are designed to increase the incentives to lenders to issue the guaranteed loans. In general these programs work by accepting loans to small businesses (often the very ones issued under the credit guarantee programs) as collateral for funds from the central bank or ministry of finance.

In the US, the Federal Reserve has two sets of programs that serve this purpose: the [Paycheck Protection Program Lending Facility](#) and the [Main Street Lending Program](#). The Bank of England introduced the [Term Funding Scheme](#). The [Australian](#) government introduced two such programs, one administered by the Reserve Bank of Australia for depository institutions and another administered by the Office of Financial Management for non-bank lenders.

Debt Moratoriums and Guarantees

By introducing debt moratoriums, the government effectively shifts the risk from the SME to the lender, who in turn often requires assistance. In [Italy](#), the government paired its six month debt moratorium with a government guarantee equal to 33% of suspended payments if 18 months after the end of the moratorium a debtor remains unable to pay.

9. Businesses will likely need additional government support

To a larger degree than seen in past crises, many countries are providing direct grants for businesses in response to the COVID-19 crisis. Recent [research](#) from the Federal Reserve Bank of New York shows that fewer than 1 in 5 small businesses in the US can continue normal operations with their cash reserves if they experience a two-month revenue loss. Credit

guarantee programs and additional lending can assist businesses with immediate cash flow needs, but the programs will only be effective if underlying macroeconomic conditions improve quickly; otherwise, they only [delay insolvency](#). Beyond increased adoption of grants, credit guarantee programs are more generous, with the [EU allowing](#) 100% credit guarantees and multiple countries waiving risk assessments. Generous loan guarantee programs have similar characteristics to grants in terms of limited diligence but still increase the overall debt burden for firms, which some firms may not be inclined to accept given the uncertainty of long-term economic conditions and future revenues.