Financial Group
German Savings Banks and Giro Association

The second Covid wave is rolling: Accompany structural change with a sense of proportion!

CORONA - NEWSLETTER

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The economists of the Savings Banks Finance Group take a look in this issue at the economic-policy implications of the resolutions decided upon by Federal Chancellor Merkel and the heads of Germany's 16 state governments on 16 November 2020:

- It is now looking likely that Lockdown 2.0, with further contract restrictions, will be continuing over the winter of 2020/2021. During this phase, the existing economic-policy stance ought to be maintained. The economic-policy measures which have been implemented in order to overcome the pandemic should remain temporary and carefully targeted. New economic-policy measures should not follow immediately.
- The sustainability of public finances must not be put under disproportionate strain. As in the case of the health-care system, overburdening resources would entail steep social costs. Germany's sound financial standing prior to the coronavirus crisis has so far enabled the country to avoid a goal conflict between health promotion and -financial feasibility. It would be wrong to carelessly squander such a favourable pole position. The road map providing for this year's temporary reduction in value-added tax to expire on 1 January 2021 must be adhered to, not least because an expensive extension would hardly provide any additional stimuli for the real economy.
- Municipal finances need to be strengthened so as to be shipshape for the future trajectory of the pandemic in the years 2021 and 2022. Many support measures are, as yet, only available during 2020, and it is crucial to extend these stabilisation measures with municipal investments in mind. This likewise remains important from the point of view of small and medium-sized businesses and from the perspective of next year's economic recovery.
- The Covid-19 crisis is characterised by a high degree of uncertainty - uncertainty about how the tally of infections is going to develop in the coming months, but also uncertainty about whether pre-crisis business models are still viable. The process of creative change will - and must - take place in the corporate sector as well. It is therefore important to allow corporate insolvencies on a sustainable basis. Only if the challenge posed by structural change is met will it be possible to adjust at an early date to the permanently altered framework conditions resulting from the lessons of the coronavirus crisis and to shape the future on the basis of new business models.

Excursus

A rise in corporate insolvencies is looming on the horizon

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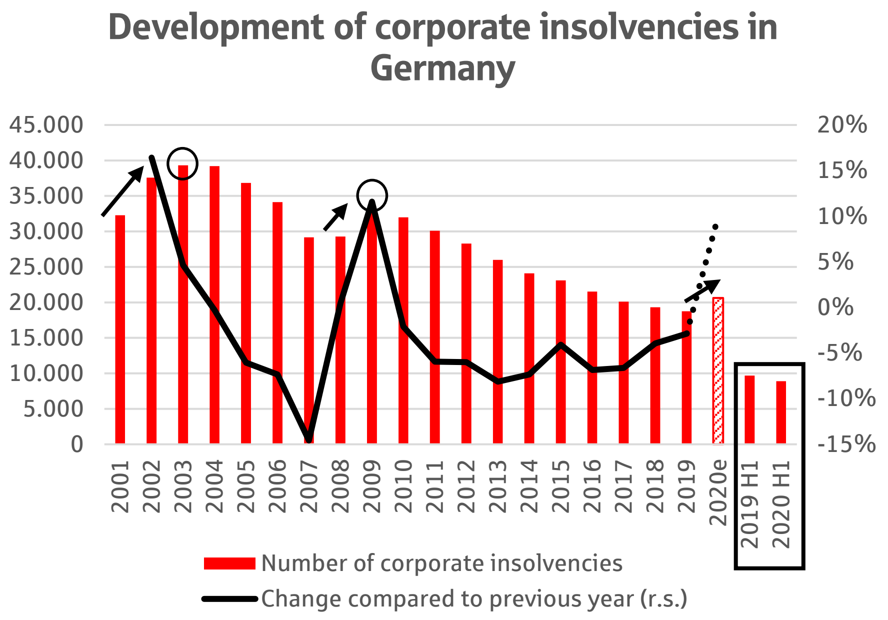
Since the beginning of October, the temporarily suspended obligation for illiquid German companies to file for insolvency has been in force again. Only in the case of over-indebtedness does the relaxation of Germany's insolvency law continue to apply until the end of the year. The Federal Employment Agency is bracing for an increasing number of insolvencies and has earmarked EUR 1.6 billion in insolvency payments for the coming year - the planned 2020 budget for such "insolvency money" worked out at EUR 950 million.

In view of the very low current level, an increase in insolvencies - especially among smaller companies in particularly affected sectors such as catering and tourism - is very plausible. However, this negative effect will be mitigated by the availability of extensive government support measures such as the (now extended) short-time working allowance and bridging loans. The sound financial policies of many companies and low interest rates have also helped to keep insolvency figures low so far.

Companies are benefiting from a solid starting position, low interest rates and support measures



Source: Creditreform, Euler Hermes, LBBW Research Trend in

Due to the low figures for the previous year, a further increase in the 12-month insolvency rate is to be expected through until March 2021 merely on account of baseline effects. In view of this, Moody's is assuming that the peak will not be reached until the first quarter of 2021. In contrast to the situation prevailing during the financial crisis of 2008/09, corporate interest outlays did not rise dramatically in the second quarter of 2020. Companies are benefiting from the persistently low interest-rate level as well as from the recovery in risk spreads. Moreover, the slump in earnings did not prove as severe as feared. A look at median values reveals that the corporate sector still had scope to cover interest expenditure even in Q2 2020, which was presumably the weakest quarter from the corporate-earnings viewpoint.

According to a survey relating to the S-Mittelstands-Fitness Index published in September 2020, three-quarters of corporate customer advisors at Germany's savings banks expect that less than two percent of their SME corporate customers will be compelled to file for insolvency over the next six months - regardless of the above-mentioned temporary suspension of the obligation to file for insolvency (https://www.dsgv.de/sparkassen-finanzgruppe/publikationen/zukunft-mittelstand-2020.html).

Despite the massive deterioration in economic prospects brought about by the outbreak of the coronavirus crisis, companies continue to have favourable access to bank loans. In September 2020, lending rose by 7.3% year-on-year. Such growth in lending is being supported not least by low-cost refinancing from the European Central Bank: in July, European banks took up the record amount of EUR 1.31 trillion via the ECB's long-term tender TLTRO III. In contrast to the financial crisis of 2008/09, there is currently no threat of a widespread credit crunch - even if individual companies may well have a hard time of it.

Disclaimer

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Note
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