KredEx extraordinary measures for companies to relieve the impact of corona crisis

Are the extraordinary loans for projects of national importance provided in a transparent and well-considered manner?

Summary

How has the corona crisis changed the outlook for the Estonian economy?

1. The coronavirus, which began to spread globally at the end of 2019, posed economic difficulties, rise in unemployment, and social risks to the Estonian people, companies and the state. The restrictions (in movement) implemented by the state in the spring of 2020 to control the pandemic promised to pose a major negative impact, especially on tourism and leisure activities, but also on industry, services, and general economic activity more broadly. As a small and open economy, Estonia also depended a lot on the situation and decisions of its neighbours and trade partners.

For your information

In October 2020, there were about 50,000 unemployed in Estonia, which is almost 20,000 more than a year earlier.

2. The outlook for Estonia's economic development deteriorated rapidly against the background of the spread of the virus. While in the autumn of 2019 the Ministry of Finance forecasted economic growth of 2.2% in 2020, the estimate published in the spring of 2020 predicted an economic contraction of 8%. The Ministry of Finance did not forecast the expected impact of the corona crisis on unemployment in detail but noted that the labor market will inevitably suffer a severe setback in the crisis (see Table 1).

The pandemic has shown that,

in a crisis situation, public debt can multiply in one year

Table 1. Selected economic and financial indicators in 2019 and their forecast for 2020 by the Ministry of Finance

	2019	forecast for 2020 in September 2019	forecast for 2020 in April 2020	forecast for 2020 in September 2020
Real GDP growth rate (%)	5.0	2.2	–8.0	–5.5
Nominal fiscal position of the government sector (% of the GDP)	–0.3	0.0	–10.1	–6.6
Debt load of the government sector (% of the GDP)	8.4	8.0	21.9	18.2
Unemployment rate (%)	4.4	5.2	Not presented	7.5
Real growth of average salary (%)	5.1	3.4	0.0	1.3

Source: The Ministry of Finance, Eurostat, Statistics Estonia; data as of 18.10.2020

How did the government decide to respond to the corona crisis?

3. As a result of the discussions that took place in March and April 2020, the Government of the Republic took the position that the state must take an active role and, in addition to ensuring the functioning of the health care system, also support business and the labor market with additional economic measures. This meant higher expenditures from the treasury than planned, but also lower revenues due to tax cuts and benefits, among other things. With the supplementary budget adopted on 15 April 2020, the Parliament of Estonia authorized the government to finance (incl. via borrowing) the deficit resulting from the economic downturn and to implement crisis aid measures. This will result the treasury's negative annual cash flow of almost €3.8 billion [1].

How has the corona crisis changed the outlook for public finances?

4. Extraordinary expenses and declining revenues also changed the outlook for public finances in 2020. If the year started in the hope of keeping the government sector's revenues and expenditures equal, then, when adopting the supplementary budget, the Ministry of Finance forecasted a budget deficit of about 10% of the GDP. According to the April forecast by the Ministry of Finance, the loans being taken and the bonds being issued to finance expenditures in excess of revenues were to raise the debt load of the government sector to almost 22% of the GDP by the end of 2020, with the decline in the GDP. According to the forecast published by the Ministry of Finance in September, the economic and financial situation this year is unfolding slightly better than feared (see Table 1), but, on the other hand, the recovery from the crisis will probably be slower in the coming years[2].

Which extraordinary measures by KredEx does the state support enterprises with?

5. In order to mitigate the corona crisis and its effects, the state started to implement a total of 37 (extraordinary) measures under the supplementary budget for 2020, which are divided between seven areas of government. The guarantees and loans being issued through the KredEx Foundation (hereinafter KredEx) are one of the central state measures to support entrepreneurship.

6. An enterprise can apply for a guarantee by KredEx to take a new loan from a commercial bank, or change the repayment schedule of an existing loan, for example, apply for a longer payment holiday, change the repayment term, etc. If the bank does not finance an enterprise, it is possible to apply for a direct loan from KredEx. In total, KredEx has got five extraordinary guarantee measures with different conditions and three loan measures[3]. €850 million was allocated from the supplementary budget of 2020 for the implementation of the KredEx extraordinary measures. The exact costs of the state depend on the behaviour of enterprises and banks as well as on economic development (see also Sections 16–18; 26–27; 38).

What requirements did the Government of the Republic set for the measures by KredEx?

7. Following the entry into force of the supplementary budget for 2020, on 28 April 2020 the Government of the Republic adopted a regulation (hereinafter the general regulation) establishing "general conditions for all aid measures, whatever their legal form, to be established by the Minister responsible for the field of activities (hereinafter the measure) related to the mitigation of the crisis and the resulting state of emergency related to the spread of the coronavirus causing COVID-19, and to the resolution of the state of emergency."[4]."

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[1] The Ministry of Finance pointed out in the forecast, providedwith the supplementary budget, that the impact of the economic downturn and the extraordinary measures on the fiscal position of the government sector will be 10.1% of the GDP, or about €2.6 billion, but it must be taken into account that this amount will be increased by the treasury's expenditures (such as financing transactions) which do not affect the fiscal position. According to the Ministry of Finance, the negative cash flow of the treasury, as a whole, will reach more than €3.7 billion in 2020. https://www.valitsus.ee/sites/default/files/2020._aasta_lisaeelarve_eelnou_seletuskiri.pdf

See Table 3, Page 9.

[2] https://www.rahandusministeerium.ee/et/riigieelarve-ja-majandus/majandusprognoosid

[3] See Annex 1 for an overview of the list of the measures.

[4] https://www.riigiteataja.ee/akt/128042020019?leiaKehtiv

8. The general regulation stipulates, inter alia, that the allocation of a compensation, an allowance, or a financial instrument under the measure must be transparent and non-discriminatory, ensuring equal treatment of the target group entities. The relevant ministries must also co-operate in the development and implementation of the conditions of the measure. In addition, the general regulation lays down other requirements as to the types, content, reporting, and disclosure of the measure.

What did the National Audit Office analyse?

9. Based on the supplementary state budget for 2020 and the general regulation of the referred government, the National Audit Office has analysed in particular the following:

- how the KredEx extraordinary measures for enterprises were designed, what the state wants to achieve with their implementation, and how it monitors the results;
- whether the procedural and decision-making process of the KredEx aid measure named "Extraordinary loan for projects of national importance" is clear, transparent at the level of both KredEx, and the Government of the Republic, and creates preconditions for equal treatment of enterprises;
- how many enterprises have applied for and received support from the KredEx extraordinary measures, and whether it meets the expectations set by the state when developing the measures.

10. The National Audit Office emphasizes that it analysed only the grounds for granting the aid to enterprises through KredEx (conditions of the measures), and the process of how loan applications for projects of national importance were processed and how the decision was made, but not each individual decision of the Government of the Republic and its (political) justification. The National Audit Office will continue to monitor the implementation of the measure named "Extraordinary loan for projects of national importance" and has decided to prepare a separate analysis[5], in order to find out the circumstances of supporting specific projects.

11. In order to compile the overview, the National Audit Office sent written questions together with a request for material to KredEx and the Ministry of Economic Affairs and Communications (hereinafter the MEAC). It also analysed the relevant materials submitted to the Government of the Republic and met with the vice-chancellor for economic development of the MEAC. The focus of the overview is primarily on the development and implementation of the KredEx measure named "Extraordinary loan for projects of national importance"[6].

What did we notice as a result of the overview, in summary?

12. The Parliament and the Government of the Republic allocated almost a billion euros for the KredEx measures, leaving the purpose of the state intervention and the assessment of the results unclear. The interest or need for KredEx's aid among companies has so far turned out to be several times smaller than forecast. The mere spending of money should not be a goal, but in order to assess and target the need for the KredEx measures more accurately, the reasons for the low interest of entrepreneurs must be better learnt, and the market monitored. It is understandable that, at the beginning of the state of emergency, the supplementary budget and the crisis aid measures were designed under time pressure and limited information, but the performance of the KredEx measures also needs to be assessed, especially now that many agreements between entrepreneurs and banks made in the spring have expired or are expiring.

13. It is unclear from which source the loans are granted for projects of national importance. If the projects of national importance are financed from the measure referred to by KredEx, then the Parliament has not given permission for this with the supplementary budget for 2020. The activities of KredEx in establishing the conditions of the loan measure for projects of national

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[5] „Procedure for loan applications related to the corona crisis at the Rural Development Foundation and KredEx".

[6] https://www.kredex.ee/covid19/meede/erakorraline-laen-riiklikult-olulistele-projektidele/

importance and reviewing the applications, as well as the activities of the Government of the Republic in making loan decisions, have been largely nontransparent. Entrepreneurs have not been fully informed of the change in the terms of the measure. Therefore, it is uncertain whether the current process ensures equal treatment of target group enterprises and the best use of public money.

14. In the opinion of the National Audit Office, in order to use the KredEx measures more efficiently and effectively, it is necessary to agree upon, among other things, what benefits the state expects from the implementation of the KredEx measures. Also, whether to focus on guarantees instead of loans in the future, and whether and under what conditions it is justified to continue with the loan measure for projects of national importance. The financing of loan projects of national importance must be clarified, and it must be ascertained that the loan is granted as prescribed in the explanatory memorandum to the 2020 Supplementary Budget Act submitted to the Parliament.

In his reply to the National Audit Office, **the Minister of Foreign Trade and Information Technology** found that the concerns and proposals set out in the overview undoubtedly deserve discussion. The Minister also explained the spring circumstances of the establishment of the KredEx extraordinary measures for enterprises, and what is being done to respond appropriately to the corona crisis. The Minister assessed the activities of KredEx in processing loan applications for projects of national importance to be transparent considering the circumstances. Read the Minister's reply in full on page 26 of the overview.

In the reply to the National Audit Office, **the Member of the Management Board of KredEx** also found that the concerns and proposals set out in the overview undoubtedly deserve discussion. According to the representative of KredEx, they cannot agree with the statement that the terms and conditions of the loan measure for projects of national importance have been changed without informing the target group entrepreneurs, as several seminars have been organized for the entrepreneurs to introduce the terms and conditions of the measure. In addition, according to KredEx, the terms of the measure have not been substantially changed since its start. According to the Member of the Management Board of KredEx, it cannot be accepted that applying for and receiving money from the loan measure for projects of national importance has been nontransparent. KredEx also emphasized that the source of the loan measure for projects of national importance is not revolving loan allocated with the supplementary budget, but the measure for the purchase of shares in strategic enterprises. Read the KredEx representative's reply and the National Audit Office’s comment thereto on page 27.

The National Audit Office welcomes the discussion concerning the KredEx measures. The National Audit Office holds to the view that applying for and receiving money from the loan measure for projects of national importance has been largely nontransparent, mainly for two reasons: 1) When compiling the overview, KredEx did not explain substantially to the National Audit Office how the socio-economic impact of the loan applications of national importance is assessed, and how the proposal to the Government of the Republic, as to which application is nationally important and which is not, is made; 2) the materials submitted to the Government of the Republic for making loan decisions show that in the case of at least one and the most financially weighty proposal, KredEx would have needed more time to make a considered proposal. The National Audit Office finds that, if the projects of national importance are financed from the measure referred to by KredEx, this is in conflict with what the Parliament granted in the 2020 supplementary budget. The explanatory memorandum to the supplementary budget explicitly states that the measure referred to by KredEx finances the purchase of shares in strategic enterprises or expands the share capital of state-owned enterprises and does not provide a loan.