

## US Congress scrambles to help smaller virus-hit firms

Monday, April 20 2020

After passing the 2.2-trillion-dollar Coronavirus Aid, Relief, and Economic Security (CARES) Act in late March, Democrats and Republicans are wrangling over making additional money available for the 350-billion-dollar Paycheck Protection Program (PPP), which ran out of money last week, and over a fourth COVID-19 aid package. The package would close loopholes and make improvements to the CARES Act so that money will get to small businesses. However, the parties disagree over whether funding for medical care and other expenses should be included in either the fourth package or the PPP top-up bill.

### What next

Talks between the Senate, House of Representatives and White House could soon lead to a deal. It is expected to include 310 billion dollars for the PPP (including 60 billion for smaller banks), more money for COVID-19 testing and hospitals (100 billion dollars together) and 50 billion dollars for the Economic Injury Disaster Loan programme. Until any package is passed, firms will rely on the CARES Act. Although this apportions half its money to individuals and small businesses, larger firms will find it easier to access the funds. Even with enhanced funding, the support could be too little, too late for many smaller firms on the brink of insolvency.

### Analysis

COVID-19's rapid spread, resultant social distancing and economic dislocation caught most firms by surprise. Smaller firms with tight cash liquidity were particularly vulnerable. Smaller service-oriented firms without online platforms had little time to adapt (see UNITED STATES: COVID-19 labour strike wave will grow - April 8, 2020).

Congress has now passed three aid and stimulus packages, the third being the CARES Act, which originated the PPP, among other measures (see UNITED STATES: Virus will have wide industry effects - March 25, 2020).

### Paycheck Protection Program

The PPP caters to businesses with up to 500 employees and began on April 3 with 350 billion dollars to disburse through US banks.

Senate Republicans wanted to add another 250 billion dollars to the PPP, to keep it solvent. However, Democrats stopped this, as they want to widen eligibility through new legislation. Given the high volume of applications for loans (which will be forgiven if employees are kept on the payroll), and with no COVID-19 vaccine currently, further billions will likely be required.

Speedy distribution of PPP loans is critical to prevent businesses becoming bankrupt, which would make them ineligible for the programme. The PPP relies on the Small Business Administration (SBA)'s network of approved banks and lenders to assess the validity of small business applicants, bypassing the SBA's approval process, which has a reputation for sluggishness in normal times.

Treasury Secretary Steven Mnuchin has promised that banks will make same-day loans. Yet this is unlikely unless the applicant is an existing borrower with the bank. Many of the 1,800 SBA-approved lenders are small community banks, whose systems have never faced the high volume of applications seen under the PPP. The banks are also facing COVID-19 operating challenges themselves.



Statuary Hall, inside the US Capitol  
(Reuters/Jonathan Ernst)

### Impact

- There will be pressure to make unemployment benefits extend beyond July 31.
- Distribution of PPP grants will be hampered by banks' capacity limits and overwhelming application numbers.
- Federal Reserve market intervention akin to 2008 will offset the worst market instability and help capital-market-reliant firms.
- Democrats will push for greater educational, nutrition assistance and frontline medical funding in package four.
- Republicans will support healthcare funding and closing loopholes in package four, but not other Democrat proposals.

The profitability of lenders extending PPP loans is also uncertain; some banks will not participate. Although the CARES Act imposed interest-rate ceilings on these loans at 4.0%, the Treasury has decreed a 1.0% ceiling on current loans, doubled from 0.5% after small lenders' complaints that it would be unprofitable to lend.

It is also unclear whether lenders can sell these loans to investors, although the Fed recently announced the Paycheck Protection Program Lending Facility, which gives PPP lenders the option to have the full amount of their PPP loans refinanced by the Fed.

Another difficulty for small firms is that they may lack the expertise and relationships of larger firms to assemble favourable PPP applications quickly.

### Temporary advantages

The COVID-19 economic shock has also caught many large firms by surprise. However, unlike smaller firms, larger firms have easier access to emergency funding through larger credit lines and capital markets.

Support from the Fed under the CARES Act provides the largest, most creditworthy firms with ongoing access to capital markets through facilities supporting market liquidity (these are the Main Street New Loan Facility, Main Street Expanded Loan Facility, Primary Market Corporate Credit Facility and Secondary Market Corporate Credit Facility).

Firms with geographic spread and an established online platform and delivery network are further advantaged. Those specialising in logistics, pharmaceuticals and food staples, which are swamped with demand in locked-down cities, will emerge stronger and be an attractive prospect for the ballooning millions of unemployed. However, it remains to be seen how many new hires will be permanent.

Larger firms have faced the economic shock by drawing down billions of dollars from their credit facilities. This will sustain many of these firms in coming months, but many firms fear credit downgrades and future borrowing restrictions.

The Fed's action, supported by the Treasury and Congress, will continue to stabilise the broad capital market. However, the largest, most stable firms that borrow from capital markets will benefit most.

The Fed's pledge to purchase US investment-grade bonds in the primary and secondary markets helped spur a record 110 billion dollars of bond issuances from highly rated US corporations in late March. The market for non-investment grade firms with weaker credit ratings has stalled. The CARES Act provides for a similar programme for mid-sized firms regardless of credit rating, which will likely be implemented in coming weeks.

Larger firms also flexed their lobbying power during CARES Act negotiations, epitomised by the late inclusion of a 17-billion-dollar allocation to support firms involved in national security. Hospitality industry lobbyists also carved out an exception for PPP funding for larger restaurant and hotel chains, who are otherwise over the 500-staff threshold. This could further crowd out eligible but smaller firms whose relationships are not as profitable for lenders.

### Talks underway

Discussions are underway on the fourth stimulus package. Democrats want another round of payments to individuals, more money for hospitals and virus testing, more nutrition support and more money for state and local governments.

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Banks issuing PPP grants are already struggling under massive demand

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Larger firms go into the COVID-19 crisis with advantages, but they will not last forever

Republicans support using a fourth package to make improvements on the third, and to improve healthcare provision, but they are wary of allowing Democrats to add new elements that are not necessary to tackle COVID-19, such as including environmental standards as a condition for industry aid money.

Talks are still ongoing, but if a deal is reached, the Senate could vote today on legislation, and the House on Wednesday. Reports overnight suggest the emerging deal has more money for the PPP, hospitals and virus testing, but perhaps not for local governments and nutrition support.

Individual lawmakers tried to hold up the CARES Act and may do so with forthcoming legislation.