Lives and Livelihoods

A Delicate Balance

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Taken aback by a pandemic the world had not seen in seven decades, we are left with no choice but to do our best to protect lives. Hurriedly and feverishly imposed measures, as extreme as total lockdowns, brought about the worst global recession since the Great Depression of the early 20th century. Forecasts suggest a drop of 3-5% in gross domestic product, while growth in Europe is forecast to go down 8-12%. With unemployment hitting unprecedented highs, 1.6 billion workers are negatively impacted by the pandemic. The International Labor Organization expects a loss of around 305 million full-time jobs in the second quarter of 2020, and estimates that one of six young people is now out of the job market as a result of the pandemic. And as companies continue to suffer, more are going out of business and this phenomenon would blow up even further. The Organization expects that the "Lockdown Generation" would face even higher unemployment and lower pay for the next five years. These factors combined lead to uncertainty regarding the true extent and severity of the crisis, causing fear and panic among consumers, investors and the business sector as a whole, intensifying further the economic and social impact of the pandemic.

Countries around the world, with no exception, find themselves striving to meet two objectives simultaneously: protecting lives and maintaining livelihoods. With the growing economic impact of protective and preventative health measures, more efforts are needed to bridge the gap between the two goals to gradually reach an equilibrium that enables a complete resumption of economic activity, without neglecting the precautions necessary to live with the virus until it could be eradicated. Only upon striking this balance can we say that we have, indeed, conquered the "lives-and-livelihoods" paradox.

On a local level, we have suffered a double-blow. Alongside the severe economic repercussions of pandemic-related measures, oil prices also dipped to levels unseen for over two decades. Between the lockdown decision of March 12 and the announcement of the plan for resumption of activity on May 28, 2020, almost three months have passed. According to the plan, complete return of economic activity – barring any setbacks – is slated for early September 2020. This means the lockdown period spans a whole six months. As a result, many private sector companies are facing great liquidity and cashflow difficulties, causing financial solvency issues as severe as bankruptcy. And in view of the inter-connectedness of all economic sectors, the damage threatens to quickly reach even the most stable sectors.

As shown by mobility data and business impact surveys, the number of visitors of retail outlets dropped by 75%, with 45% of all companies forced to suspend business or shutdown altogether, and many more to follow suit most probably in the future. Meanwhile, 44% of landlords also reduced rent as a result of the overall situation, while 64% of those polled reported sentiments of fear, anxiety, and uncertainty.

In general, forecasts suggest a drop in private sector revenue as high as 42%, causing cashflow and liquidity difficulties for corporate bodies. This could cause an increase in default rates, and companies failing to pay would trigger high loan-related losses in the banking sector. Companies are expected to need a total of KD 2.4-3 billion to cover their working capital requirements (such as salaries and rent payments). It is also expected that the prolonged lockdown would bring about layoffs and increase unemployment in the private sector. Amongst all nationals employed in the private sector, 86% of them (62,000 Kuwaitis) work in economic sectors negatively impacted by the crisis. Furthermore, 79% of non-nationals employed by the private sector (1.3 million workers) also work in affected sectors. Closing these companies would disrupt supply chains and cause shortages in both the supply of basic goods and services. The drop in spending and the prevalent uncertainty will also deter future investments.

Any failure to take swift and unwavering action in response to working capital requirements would have grave economic repercussions on companies, particularly on small and medium enterprises (SMEs). The impact would continue to grow as the crisis persists, since the cash flow crunch would force companies – including those previously in a good liquidity position - to shut down for failure to secure financing; either due to increasing financing costs or the banks' reluctance to finance amid fears of growing default risk during the crisis. This could lead to companies' bankruptcies, which, due to the chain effect between economic sectors could thus result in a contraction in non-oil GDP.

The Committee's Mandate

To counter the impact and repercussions of the crisis on the national economy, the Higher Steering Committee for Economic Stimulus (The Committee), formed by the Council of Ministers Resolution (455) on 31 March 2020, and chaired by the Governor of the Central Bank of Kuwait, adopted a proactive approach to realize economic stability throughout the crisis. It laid down and initiated economic stimulus measures to prepare for the economic recovery stage that shall follow once we overcome this crisis. Immediately afterwards, a national economic and structural reform plan needs to be launched and adopted by all the relevant stakeholders.

The Committee listed several measures and governing principles to serve as a framework for all its activities, and they are as follows:

- Introducing immediate remedies that provide practical and swift solutions to protect the national economy supporting economic reform and best possible resource allocation.
- Sharing the burden, as the cost of addressing the current crisis is more than a single party could bear on their own.
- The state shall not compensate parties for lost opportunities for profit, nor for losses due to preventative measures imposed to fight Covid-19; it is not possible to avoid losses or damages completely.
- Financial support is extended with the limited goal of surviving this current period and is only extended to economic entities and companies that enjoyed a strong position, ran with efficiency, and were contributing to the economy prior to this crisis.
- Ensuring that the economic cycle keeps running, so that companies that had suspended business may resume their activity as soon as life goes back to normal.
- Protecting the different segments of the national economy against damage sustained due to interdependence of economic sectors.
- Solutions and remedies provided through the stimulus package are based on currently available data and present conditions. Should the crisis stretch much longer into the future, other remedies would be presented that better correspond to new data and conditions.

To come up with a balanced and comprehensive approach, the committee specified the issues that must be addressed and for which stimulus is needed within four main segments: the household, business, banking, and government sectors. Twenty-two measures had been presented to stimulate the economy, 11 of which were included in Council of Ministers Resolution (455). As for the other 11 measures, some were implemented by CBK and the banks, while others were proposals presented to the Council of Ministers to take the appropriate action.

The Households Sector:

Where this sector is concerned, the committee specified the goal as guaranteeing basic needs, providing financial support, and maintaining job security for nationals. Accordingly, it introduced a set of measures to protect and safeguard the stability of this important sector. Among the measures were guarantees to protect nationals employed in economic sectors impacted by the crisis, whether in the government or private sector, as well as maintaining the stability of prices of food items and medical goods, in addition to depositing of six months' retirement pay (pension) for those eligible. As well as support for salaries covered under Chapter Five[1] of the budget as stated in Council of Ministers Resolution (455), the committee added an item to double the support extended to nationals registered under Chapter Three[2] for six months. This was in addition to guaranteeing a minimum income level that is sufficient to meet livelihood needs for affected workers and the provision of basic humanitarian needs for all those living on Kuwaiti soil. Banks meanwhile took the initiative and implemented a moratorium on personal loans and waived point of sale and ATM fees.

The Business Sector:

To bolster the business sector's resilience, be it SMEs or larger firms, the Committee sought to reduce its financial burden by providing the required cash flow to cover regular contractual liabilities, such as salaries and rent, as companies lost all revenue due to the lockdown. This was accomplished through a set of measures, among which was the deferment of loan payments due to the National Fund for Small & Medium Enterprise Development (National Fund) and the Industrial Bank, plus providing concessionary loans to SMEs through joint National Fund-bank financing according to mechanisms and controls laid down by the Committee. Although this mechanism was approved by the Council of Ministers, implementation was not feasible due to difficulties on the part of the National Fund. Accordingly, the National Fund was officially directed to take the appropriate measures to guarantee support to the vital SMEs segment which falls within its mandate, as the country looks to SMEs for more job opportunities for Kuwaitis and to contribute to the diversification of the national economy.

As for concessional financing for corporate firms and individuals negatively impacted by the crisis, banks had in fact already started extending financing and giving concessions, either in line with this measure or their standing credit policy, and had also injected more liquidity into the sector. Furthermore, the Central Bank of Kuwait instructed the banking sector to abstain from sale of or enforcing of any measures on or liquidating collateral held by banks.

In addition, the Public Institution for Social Security also postponed subscription payments. Government fee waivers were extended to impacted institutions, and banks extended moratoriums on affected customers' loans. The Committee had also communicated with all

[1] Chapter Five refers to Kuwaitis registered with the Public Institution for Social Security as self-employed.
[2] Chapter Three refers to Kuwaitis registered with the Public Institution for Social Security as working for a private sector employer.

government entities urging them to swiftly pay their dues to the private sector and is following up in this regard.

The Committee further proposed an amendment on provisions of the Labor Law that takes into consideration special and extra-ordinary circumstances and gives more flexibility for both employer and employee. It also presented to the Council of Ministers a proposal to postpone evictions of tenants in commercial real estate. Lastly, the Committee proposed setting up courts specialized in economic, commercial, and financial affairs in view of the unique nature of this sector and the real need for judicial expertise in this field, especially amid expectations of an increase in disputes in this field that the court system would have to address upon resumption of activity.

The Banking Sector:

As the financial intermediaries in our national economy and the sector entrusted with the community's savings, it is vital to maintain financial stability and to encourage the banking sector to extend financing. In view of the interdependence among all economic sectors, it is also essential to bolster this segment against fallout from other sectors affected by the current circumstances. Like other segments, the banking sector was affected by the lockdown, which caused a reduction in its capacity to extend financing, and we can also sense some reluctance to offer loans. Two factors are at play and are reducing efficiency of current measures regulating granting of financing; the first is banks' preference – amid the current conditions – for granting financing to big companies with a strong financial position. This excludes a great number of companies affected by the crisis, which are in dire need of financing. The second is the continued gradual drop in banks' willingness to grant financing as the crisis worsens and the cashflow problem escalates, as does its impact on companies' solvency. All this comes as companies face an increasing need for financing. This scenario calls for taking the initiative and introducing comprehensive approaches to bolster this segment's resilience and to incentivize it to extend more financing, which would guarantee sufficient cash flow across economic sectors and guarantee recovery through a comprehensive and integrated approach.

In light of all of the above, the CBK had since March 2020 started to use its policy instruments to strengthen the sector's resilience and to enable it to play a bigger role throughout this crisis; initiating macro-prudential measures and reducing regulatory requirements, thus expanding banks' lending capacity to the range of KD 8-9 billion. It also dropped the interest rate to a historical low of 1.5%, which reduces the cost of financing for entities granted such support and stimulates economic growth. As a result of these steps, the banking sector now has high liquidity levels and maneuvering capacity that enable it to fulfill its duty as financial intermediary.

The Role of the Government:

The role of the government takes on an even greater importance amid the current conditions. The lockdown measures caused an unprecedented shock to both supply and demand, this coincided with a sharp decline in oil prices that brought down government revenues. The Committee was therefore keen to provide maximum support to guarantee that the economy keeps running, while simultaneously reducing cost to public funds to a minimum, through the proper allocation of resources and reliance on measures that have the biggest impact with the least cost possible. Among these measures was drawing up a government financing support and guarantee scheme, which was presented to the Council of Ministers by the Committee on 5 June 2020.

Government financing support and guarantee scheme:

The committee forwarded a proposed government financing support and guarantee scheme to the Council of Ministers to decide and take appropriate action in this respect. The proposal was drawn up after consideration and examination of 35 examples of such schemes from around the world, and examining the stimulus packages that are being implemented worldwide which come to the value of USD 11 trillion, almost 15% of gross global product so far. The result of the examination was that supporting concessional financing and guarantees accounted for 40% of total global stimulus packages. Three main elements were found to be essential for the success of any financing support system in meeting its objective effectively and in timely manner. First: banks must possess and have access to sufficient cash flow and liquidity. Second: interest rates must be attractive and suitable for both lender and borrower, which is achieved by use of monetary policy instruments and subsidizing the cost of financing. Third: banks must be motivated to extend credit amid the current harsh conditions, as they shy away due to apprehension and uncertainty regarding the scope and severity of the crisis. Therefore, countries stepped forward to guarantee loans and partner with banks in shouldering the risks involved.

Inspired by the principles and criteria of regional and international financing support and guarantee schemes, the Committee developed its own scheme which is most suited to the legal requirements in the State of Kuwait, caters to the national economy, and takes into consideration both the conditions of the economy and estimates regarding financing companies' working capital requirements. The Committee recommends introduction of the scheme as one measure targeting both SMEs and companies. This scheme comes in two parts; **the first** relates to concessional financing support while **the second** concerns the State's guarantee of the financing.

Part One: support to cost of financing

This program was designed to support cost of financing (return/interest) granted to SMEs and cost of financing given to companies. In line with the nature of **SMEs** and their unique needs, the scheme subsidizes cost of financing at a maximum of KD 250,000 per customer. This support covers part of the financing where the State shoulders the full cost of the financing for the first two years, 90% of the cost for the third year, and 80% for the fourth.

The scheme specifies the purpose of the financing as meeting periodic contractual dues and expenditures, such as payroll and lease payments, with a term of up to four years. It meanwhile keeps cost of financing at a low level (discount rate as specified by the CBK + 1%), which currently comes to 2.5%. As for eligibility for financing, the program covers SMEs affected by the COVID-19 pandemic that had been performing well and enjoyed a good position prior and excludes entities whose parent companies have alternative sources of financing. The scheme also requires the entity to retain current national staff and meet the Kuwaitis employment quotas to be met by end of 2021 for the relevant sector in which it operates.

As for **companies**, the concessional financing term according to the scheme was specified as three years, not four as with SMEs. Part of the cost of financing is subsidized where the State shoulders the entire cost for the first year and 50% of the cost for the second year, while the beneficiary has to cover the whole cost for the third.

Part Two: guarantee of financing

In addition to subsidizing the cost of financing, the scheme proposes a State guarantee of the financing extended to SMEs to incentivize banks to grant financing. The layout is suited to the local economy where the State guarantees 80% of the principal debt but not the cost of financing. Meanwhile, an annual fee of 0.25% is to be paid to the State to reduce banks' moral hazard and to generate revenue for the government to partially offset the cost of the scheme.

The committee proposed a set of controls and restrictions to guarantee that the financing is spent towards the indicated purposes, most importantly: companies refrain from distributing dividends to shareholders while benefiting from the scheme. They must retain the national staff ratio as of 31 December 2019 and work towards satisfying the target ratio for 31 December 2021, relevant to their respective sector. It is worth noting that this guarantee has several advantages for the economy, for banks and economic entities including the following:

- The actual cost to the government to guarantee financing does not exceed one tenth of the overall financing extended to economic entities.

- Financing is provided to economic entities without direct impact on government funds, since cost is only incurred when debtors default on payment.
- Risk and accountability sharing between the banks and the government allows each to focus on its main role.
- Reducing inflationary pressures that result from direct liquidity injections.
- The scheme caters to specific sectors, comes with specific terms, and is time-bound with a clearly defined deadline.

The Committee has presented this proposal in its final format to the Council of Ministers with the proposed draft law that would regulate the scheme, the next step is putting the matter before the National Assembly for review and the enactment of the law.

Conclusion

As we continue to strive on the two fronts of Lives and Livelihoods, people remain central and while striving to protect them against the pandemic, we should not overlook their livelihoods. This is undoubtedly a colossal and unprecedented challenge, and one that requires bridging the gap and approximating the two tracks towards an intricate balance that allows for a smoothly running economy and a return to the highest levels possible of economic activity without compromising safety measures and preventative health protocols to avoid new waves of infection. This challenge could only be conquered through collaboration and through minding all health recommendations and state-issued controls by all parties in this blessed land, as normality is gradually restored.

A severe pandemic yields lessons to be gleaned. While this is a unique crisis, it brings in tow unique opportunities for us to recalculate our approach, correct structural imbalances, and construct economic components on stronger, firmer foundations so that we may build a brighter future for our homeland and ensure sustainable prosperity for all.

We hope that everyone stays safe.

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