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## Liquidity Loans as an Element of Support for the SME Sector during the COVID-19 Pandemic in the Area of Central Pomerania

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**Abstract:**

**Purpose:** The aim of the article is to present the significance and the forms of state aid addressed to the SME sector in the time of economic crisis caused by an epidemic shock.

**Design/Methodology/Approach:** The article analyzes the conditions for supporting micro, small and medium-sized enterprises in the form of liquidity loans addressed to enterprises in Poland. Moreover, the size and structure of 46 loans granted to entrepreneurs from the area of Central Pomerania (Poland) were examined. Descriptive statistics measures, the Pearson correlation coefficient and linear regression measures were used to analyze the support granted in the form of liquidity loans.

**Findings:** The conducted analyses indicate that liquidity loans are a very attractive form of supporting entrepreneurship in the conditions of a pandemic. This form of support is mainly used by the smallest enterprises (micro-enterprises) and there is a certain risk that this form of aid will also be of interest to companies that have not suffered too much from the crisis caused by the pandemic.

**Practical Implications:** The results indicate that the value of the granted liquidity loans is small, therefore they should only provide emergency aid in the initial stage of the epidemic.

**Originality/Value:** The research findings can be used by institutions responsible for distributing loans and by the European Union Member States for designing the distribution of funds in order to support business after the end of the epidemic.

**Keywords:** Liquidity loans, small and medium enterprises, economic crisis, COVID-19 pandemic.

**JEL Codes:** H25, H27, H81.

**Paper type:** Research article.

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## 1. Introduction

The sector of small and medium-sized enterprises (SME) is a sector influencing the development of national economies. SMEs are very important for the development of society and regions because they guarantee the income and paying capacity of the population, as well as ensure a competitive balance in the business environment (Razumovskaia *et al.*, 2020).

SMEs make a significant contribution to generating the gross domestic product of developed economies (GDP). For example, in Poland, they generate nearly three-quarters of Polish GDP, and micro-enterprises have the largest share in its creation. The number of people working in the SME sector in 2018 was nearly 10 million. Enterprises operating in the SME sector mostly use their own sources of financing. According to data for 2017 - 73.4% were funds from own sources, and only 10.4% were funds from loans (Polska Agencja Rozwoju Przedsiębiorczości, 2020).

The COVID-19 pandemic originating in China has led to a very rapid increase in the number of coronavirus cases in all continents of the world. Due to the high risk of virus transmission, many countries have been forced to enter a lockdown (shutting down certain sectors of the economy). As a result, a crisis arose whose effects had health, social and economic dimensions (Napierała *et al.*, 2020).

The economic crisis caused by the COVID-19 pandemic differs from the crisis that occurred in 2008-2009. The current crisis was caused by administrative decisions concerning restrictions on the free conduct of economic activity and the closure of certain sectors of the economy (tourism, hotel industry, catering, transport, etc.). Consequently, many governments of developed economies have decided to introduce measures to help companies weather the difficult times of the pandemic and rebuild their competitiveness after the pandemic ends (Tetlow and Dalton, 2020; Grima *et al.*, 2020; Khan *et al.*, 2020).

The pandemic shock caused huge changes in the economic structure on both the demand and supply sides. On the demand side, there has been a decline in labor supply as workers have to be quarantined or look after their dependent children. The need to maintain a "social distance" has resulted in a decline in utilizing production capacity. In addition, there has been a disruption of supply chains due to problems with the supply of raw materials and goods. On the demand side, on the other hand, consumers have experienced a significant reduction in income and fear of contracting the virus, which has an impact on reducing spending and consumption. Enterprises have been hit by a drastic drop in income, which is seriously impacting liquidity shortages (OECD, 2020).

Previous studies show that SMEs are more exposed to the negative effects of a pandemic than large enterprises (Juergensen *et al.*, 2020). For example, a survey conducted among entrepreneurs in Chile shows that 54.9% of companies were

prepared to face a pandemic "just for a while" (Umaña-Hermosilla *et al.*, 2020). Research on US small businesses shows that 50% of businesses have cash reserves that will last less than 15 days (JPMorgan Chase & Co., 2020). On the other hand, the results of research conducted in British companies indicate that 41% of British small businesses have had to close since the beginning of the pandemic, and 35% of companies are not sure whether they will reopen (FSB, 2020). The financial problems of small enterprises result primarily from having small cash reserves for the so-called "rainy day" and difficult access to external financing.

Faced with the threat of losing payment capacity by enterprises, governments very quickly launched aid measures to help companies stay in business at this most difficult time. The scale of this aid is enormous. Enterprises in Poland will be able to benefit from credit guarantees and micro-loans worth PLN74 billion (3.3% of GDP) and a liquidity program worth PLN100 billion (4.5% of GDP) launched under the Polish Development Fund (International Monetary Fund, 2020).

The aim of the article is to present the significance and the forms of state aid addressed to the SME sector in the time of economic crisis caused by an epidemic shock. The following scope of research was adopted for the purpose of achieving this goal:

1. Review of research results to date on the impact of the COVID-19 pandemic on the functioning of micro, small and medium-sized enterprises in selected countries.
2. Analysis of the conditions for supporting micro, small and medium-sized enterprises with the help of liquidity loans in Central Pomerania in Poland.
3. Analysis of the size and structure of support granted in the form of liquidity loans for micro, small and medium-sized enterprises from the area of Central Pomerania.

## **2. Materials and Methods**

The proposed scope of the study required an appropriate approach to the conducted research. The problem of the impact of a pandemic shock on the functioning of SMEs is a new and current problem. The aim of the study indicated in point 1 was to systematize the knowledge about the economic effects of the pandemic in micro, small and medium-sized enterprises. The review of the current research results in this area was made on the basis of the analysis of articles available in the following databases: Scopus, Web of Science and ProQuest Central.

The next stage of the study (scope of research in point 2) was to systematize the knowledge about the conditions that need to be met when obtaining and settling liquidity loans intended for SMEs. The analysis covered the regulations and contest documentation of loans granted by Koszalin Regional Development Agency (Koszalińska Agencja Rozwoju Regionalnego S.A.) (KARR) and the Association of

Social and Economic Initiatives in Białogard (Stowarzyszenie Inicjatyw Społeczno-Gospodarczych w Białogardzie) (SISG). These are institutions that have signed an intermediary agreement with the West Pomeranian Regional Development Agency and deal with granting liquidity loans for the SME sector in Central Pomerania.

As part of the research scope indicated in point 3, a detailed analysis of the size and structure of liquidity loans granted by KARR and SISG as of 5.10.2020 was carried out. According to the information provided by both institutions, a total of 46 enterprises were supported with a total value of PLN5,842,89.74 (Figure 1).

**Figure 1.** General characteristics of liquidity loans granted by Koszalin Regional Development Agency and the Association of Social and Economic Initiatives in Białogard

KARR	SISG
total available money - 3.157.094,74 PLN loans granted - 3.057.894,74 PLN 28 submitted applications	total available money - 6.315.000 PLN loans granted - 2.785.000 PLN 23 submitted applications

*Source:* Own study based on data provided by KARR and SISG.

The sources of financing of the liquidity loan are funds from the West Pomeranian Development Fund and own resources of the intermediary institution (KARR, SISG). The purpose of the liquidity loan is to mitigate the negative effects of reducing the financial liquidity of micro, small and medium-sized enterprises from the West Pomeranian Voivodeship, caused by the COVID-19 epidemic, by improving their access to external sources of financing.

Descriptive statistics measures (mean, median, standard deviation) were used to analyze the support granted in the form of liquidity loans. The relationship between the size of employment and the value of the loan obtained was also analyzed. For this purpose, the Pearson correlation coefficient and linear regression measures were used.

### 3. Results

#### a. *The impact of the COVID-19 pandemic on the functioning of micro, small and medium-sized enterprises in selected countries*

The already year-long COVID-19 pandemic has had numerous consequences in social and economic life. Many researchers analyze the effects of the pandemic on the functioning of enterprises. Research conducted in the field of SMEs in the time of the COVID-19 pandemic most often focuses on the problem of diminishing revenues and deteriorating financial results in selected industries.

According to research conducted in British companies, sectors such as logistics, construction and agriculture were most affected by the pandemic in the SME sector. In these sectors, over 90% of SMEs indicated a decrease in revenues. The sectors least affected include science, finance, insurance and education (Albonico *et al.*, 2020).

The results of research conducted in the SME sector in Austria, Germany and Spain show that entrepreneurs from Austria and Germany expect a decrease in turnover by 20%. Meanwhile, Spanish companies estimate a higher decline in turnover: 25-30% in industry, 38-44% in retail and services. Research shows that in the service sector, the tourism industry will suffer the most, in particular accommodation companies: Germany - turnover decrease by 52%, Spain - 70%, and travel agencies and tour operators: Spain - turnover decrease by 63%, Austria - 69%. The difficult situation due to the pandemic will also affect services in the field of food and beverages (restaurants and cafes). The estimated decrease in turnover is: Austria - 38%, Spain - 54%. In the retail sector the biggest drop in turnover concerns the sale of motor vehicles and other services, with Spanish entrepreneurs losing the most - a turnover decrease by 50%, and German entrepreneurs - 20%. Meanwhile, in industry the largest drops in sales are expected in companies producing durable goods: in Germany - 20%, Spain - 42% (García *et al.*, 2020).

Research in the hospitality industry also shows that the pandemic is adversely affecting business performance. The analyses carried out in Polish city hotels in the period from January 5 to March 14, 2020, i.e., before the lockdown, showed a decrease in revenues by 28% compared to the previous year, and a decrease in occupancy by 25% (Napierała *et al.*, 2020).

Other studies conducted among Austrian companies show that SMEs, which are affected by the COVID-19 crisis, act very carefully, limiting operations, investment and employment. It should also be emphasized that companies that have not been directly affected by the lockdown are also at risk of losing profitability and liquidity due to participation in the supply chain (Hölz and Schmidt-Dengler, 2020).

Research conducted in South Africa shows that the revenues of SMEs in the food sector will decrease by 10%-30%, while the most dramatic situation is in the alcoholic beverages sector, where revenues decreased by as much as 60%. So far, 117,600 jobs have been lost in the alcohol industry due to the pandemic, while 13% of the craft beer sector is in the process of closing stores (Telukdarie *et al.*, 2020).

The COVID-19 pandemic has also had a negative impact on the transport sector. For example, public transport companies in Australia saw passenger reductions in subways and trains by 46%. Meanwhile, air transport was largely non-existent due to border closure. Australia's International Airlines revenue is expected to decline by 31.5% because of this (Munawar *et al.*, 2021).

The situation of the SME sector in Russia is also unfavorable. Approximately 11% of SMEs suffered from a complete lockdown. Taking into account the interrelationships between enterprises and the multiplier effect, as many as 3.4 million small and medium-sized enterprises are at risk of closure (64.2% of all SMEs). Industries that may suffer from the multiplier effect account for almost 77% of the total revenues of the SME sector. Thus, the catastrophic scenario of a 50-60% reduction in SME turnover could lead to a decline in Russia's GDP by around 10% in the second quarter of 2020 (Razumovskaia *et al.*, 2020).

In Chile, in terms of effects on economic development, a decline in demand for goods and services resulting from isolation of people was identified. Tourism and leisure services are among the most vulnerable sectors in this country. In terms of the labor market, while teleworking has been implemented to facilitate home activities, it has contributed to the exclusion of the most vulnerable rural sectors due to resource scarcity and all kinds of restrictions that prevent access to the internet (Umaña-Hermosilla *et al.*, 2020).

According to economists from various countries, the COVID-19 pandemic could lead to a wave of corporate insolvencies. Companies from the tourism, hotel, catering, entertainment and art industries are most exposed to this risk. Another sector with a high risk of default in many countries is the trade sector (the highest risk was rated in the USA and the lowest in Africa and the Middle East). In the case of the manufacturing sector, economists assess the risk of insolvency as moderate (Boumans *et al.*, 2020).

*b. Analysis of the conditions for supporting micro, small and medium-sized enterprises with liquidity loans in Central Pomerania*

Liquidity loans granted by Koszalin Agency of Regional Development and the Association of Socio-Economic Initiatives in Białogard are repayable instruments aimed at micro, small and medium-sized enterprises conducting their business or having their seat in the West Pomeranian Voivodeship. The purpose of the liquidity loan is to mitigate the negative effects of reducing the financial liquidity of companies affected by the COVID-19 pandemic by improving their access to external sources of financing. In particular, service industries (transport, tourism, culture, hotel industry, food and retail services) are preferred for support.

The condition for receiving the loan is to have creditworthiness and to be in arrears in terms of taxes and other public law obligations. Moreover, the enterprise is required to provide adequate security for the loan.

Enterprises may apply for a loan in the amount of PLN25,000 to PLN250,000, with the lowest loan value being granted to the smallest companies that keep simplified tax records in the form of tax on registered income without deductible costs or flat rate tax. The loan repayment period can be up to 5 years. It is also worth emphasizing that the borrower may apply for a grace period in the repayment of

principal and interest for a period of 6 months. The regulations of the liquidity loan indicate that the funds should be spent within 180 days from the loan disbursement and may be used for:

- 1) current needs in financing of working capital, related to the conducted business activity,
- 2) liabilities resulting from the conduct of current operating activities that arose after January 1st, 2020, which are indisputable, are not covered by enforcement or court proceedings and are not expired,
- 3) covering current expenses related to salaries and costs of maintaining premises,
- 4) purchase of commercial goods,
- 5) expenditure on the purchase of fixed assets directly related to counteracting the COVID-19 pandemic in the amount of up to 30% of the loan amount.

Liquidity loans are granted on more favorable terms than market terms. The entrepreneur does not bear a commission for granting the loan, while the interest rate consists of the EU base rate plus a margin. According to the information provided by the SISG, the interest rate on the loan as of October 5th, 2020 was 1.44% per annum.

The support provided to borrowers in the form of a liquidity loan takes the form of *de minimis* aid. This means that the company must meet the conditions set out in Commission Regulation (EU) no. 1407/2013<sup>4</sup>. Support provided to a single enterprise may not exceed the limit of EUR200,000 within three tax years (for the transport sector this limit is EUR100,000). To the application for a liquidity loan, the entrepreneur should attach a document containing information on the amount and form of *de minimis* aid received in the year of applying for the loan and in the 2 preceding years.

*c. Analysis of the size and structure of support granted in the form of liquidity loans for micro, small and medium-sized enterprises in the area of Central Pomerania*

According to data obtained from KARR, by 5th October 2020, the institution granted 23 loans for the amount of PLN3,057,894.74, which is 96.8% of the allocated pool of funds. 28 applications for a liquidity loan were submitted to the institution, of which 4 were rejected and 1 application was at the stage of its examination. All loans were taken out for a period of 60 months.

Moreover, according to the information provided by the SISG, by 5th October 2020, the institution granted 23 loans for the amount of PLN2,785,000, which means that

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<sup>4</sup>Commission Regulation (EU) No 1407/2013 of 18 December 2013 on the application of Articles 107 and 108 of the Treaty on the Functioning of the European Union to *de minimis* aid (Official Journal of EU L 352 from 24.12.2013).

the pool of available funds was used at the level of 44.1%. All entrepreneurs who submitted applications received support. Taking into account the size of the enterprise, the majority of enterprises were micro-enterprises (87%). Most loans were taken for a period of 60 months (82.6%). Other loans were taken for 48 months (8.7%) and 36 months (8.7%).

At a later stage, the data on loans granted by KARR and SISG are analyzed jointly. Table 1 summarizes the basic data on liquidity loans granted in the area of Central Pomerania.

**Table 1.** Basic statistical measures concerning loans granted in the area of Central Pomerania (N=46)

Description	Number of companies	Industry structure (in %)	Average loan amount (PLN)	Median loan amount (PLN)	Loan standard deviation (PLN)
Services	18	39,1	103 333	80 000	72 896
Trade	15	32,6	142 667	100 000	91 976
Food and hospitality	6	13,0	175 000	175 000	75 000
Construction	4	8,7	110 500	83 500	84 043
Manufacturing	2	4,3	164 947	164 947	64 947
Sports and recreation	1	2,2	21 000	-	-
<b>Total</b>	<b>46</b>	<b>100,0</b>	<b>135 881</b>	<b>100 000</b>	<b>85 437</b>

*Source:* Own study based on data provided by KARR and SISG.

From the industry point of view, companies from the service sector received the most liquidity loans - 39.1%. A slightly smaller share of loans was granted to companies from the trade sector - 32.6%. It may come as a surprise that the industry that suffered the most from the lockdown, i.e. food and hospitality industry, accounted for only 13% of loans granted. The lowest number of loans was granted to manufacturing enterprises (4.3%) and companies from the sports and recreation sector (2.2%).

The average value of a loan in the examined group of enterprises was PLN135,881, with the highest average value of a loan in the food and hospitality industry (PLN175,000), manufacturing (PLN164,947) and trade (PLN142,667). It can therefore be concluded that these industries reported the greatest demand for cash. Demand for cash below the average loan amount was reported by construction companies (PLN110,500) and companies from the sports and recreation sector (PLN21,000).

The median value of a liquidity loan shows that half of the companies obtained funds to make current payments below PLN100,000, while the remaining half took out loans with a value above PLN100,000. The highest values of the median loan

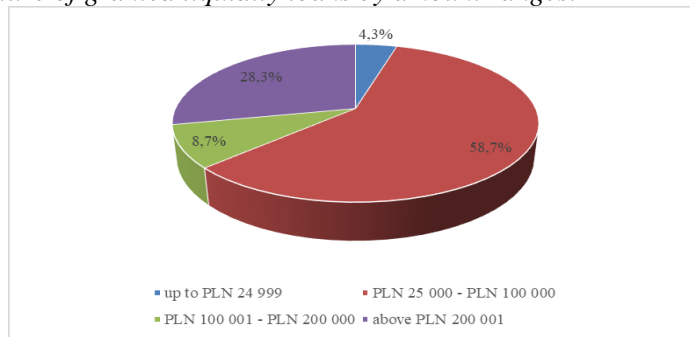


occurred in the food and hospitality industry as well as manufacturing - the median values were respectively: PLN175,000, PLN164,947 and were the same as the values of average loans. The lowest median value was recorded in the services sector (PLN80,000) and construction (PLN83,500).

The standard deviation for the examined loans is very high and amounts to PLN85,437. This standard deviation represents a very large dispersion around the average loan value. A high variability of the value of loans was recorded in all industries.

Figure 2 shows the structure of the value of the granted liquidity loans. As can be seen, the largest share of loans were loans in the range from PLN25,000 to PLN100,000 - 58.7%. Second in terms of the value of granted loans were loans above PLN200,001, the share of which was 28.3%. Only 4.3% of all loans were loans up to PLN24,999.

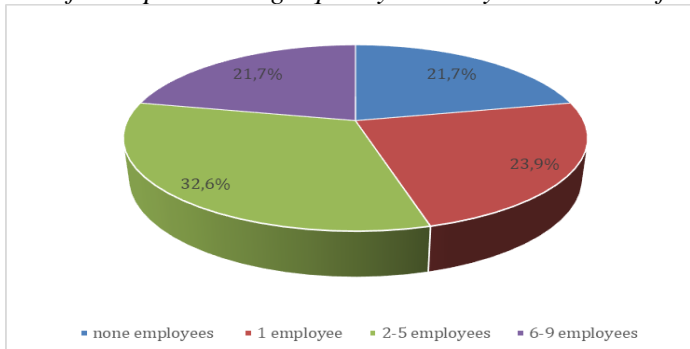
**Figure 2.** Structure of granted liquidity loans by amount ranges.



**Source:** Own study based on data provided by KARR and SISG.

Figure 3 shows the structure of enterprises using liquidity loans, taking into account the number of employees converted into full-time jobs.

**Figure 3.** Structure of enterprises using liquidity loans by the number of employees

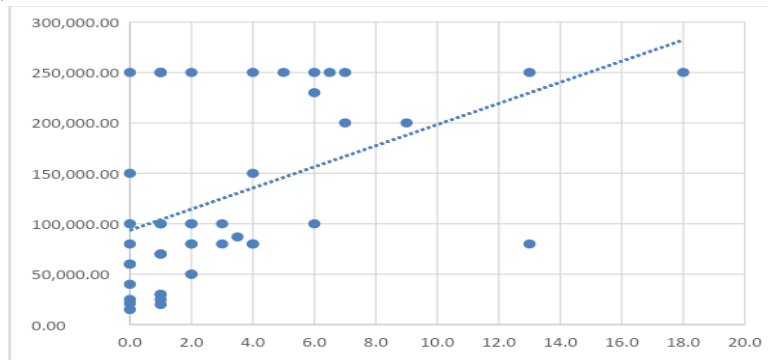


**Source:** Own study based on data provided by KARR and SISG.

The analysis of Figure 3 shows that the dispersion of enterprises in terms of the number of employees was small. In the group of enterprises that used liquidity loans, the largest share was held by companies employing 2-5 employees. This group accounted for almost a third of all companies. In turn, nearly a quarter of borrowers were represented by companies employing 1 employee. The self-employed and companies employing 6-9 employees constituted the same share in the surveyed population - 21.7%

In order to measure the relationship between the number of employees and the value of loans granted, the Pearson correlation coefficient was calculated. On the basis of the performed calculations, a moderate correlation was observed between the number of employees and the value of loans granted - the correlation coefficient was 0.47. Taking this correlation into account, a linear regression model was developed as shown in Figure 4.

**Figure 4.** Linear regression model - the size of employment and the amount of the loan granted



*Source:* Own study based on data provided by KARR and SISG.

Based on the analysis of Figure 4, a significant distance between the results and the trend line was found. The constructed model  $y=10.478x+9357$  with  $R^2=22.2\%$  explains the relation only to a small extent. Therefore, it can be concluded that the value of the loans granted depends on the size of employment only to a small extent.

#### 4. Discussion

The COVID-19 pandemic is a global problem that affects all areas of social and economic life. The introduced limitations of the social distancing, decrease in demand, limitation of supplies and production, and, consequently, a decrease in sales revenues have led to a situation in which even profitable enterprises have problems with paying their current liabilities. Under these conditions, state support is essential to ensure that the companies most affected by the pandemic can survive this difficult period. One form of state aid are liquidity loans.

Based on the presented research results, it can be concluded that in Central Pomerania, mainly micro and small enterprises used liquidity loans. Most of the companies (90.2%) that applied for a loan received it.

It may come as a surprise that the companies most affected by the lockdown benefited less from liquidity loans. In the studied group of companies using loans, only 13% of enterprises belonged to the food and hospitality sector. This may be due to the fact that only companies that have creditworthiness can take advantage of loans, and a loan for companies in this industry may not be available due to low turnover or lack of turnover at lockdown. In such conditions, a more appropriate form of support may be a subsidy and an exemption or partial exemption from paying public-law obligations.

The average value of the liquidity loan was PLN135,881, while the median value of the loan was PLN100,000. It may be argued that this loan value is too low to hold the business until the end of the pandemic. Such liquidity loans can only be a temporary solution in the initial phase of a pandemic.

Considering the three phases of business support during the current epidemic crisis - 1) rescue, 2) recovery, 3) restructure - liquidity loans, in addition to deferral and reductions of taxes and direct subsidies, are an important element of phase 1. In the rescue phase, it is necessary to protect enterprises from the inevitable decline in income and to protect business capital and economic ties that determine the structural strength of the economy (Wilkes and Bailout, 2020). Rescuing enterprises is important because companies have specific human and intangible capital that determine the driving force of the economy. The collapse of enterprises would lead to the loss of competitive potential of the economy. Therefore, in the rescue phase, it becomes necessary to provide enterprises with sufficiently quick support to rescue solvent enterprises that have problems with financial liquidity (Tetlow and Dalton, 2020).

Government support for companies after the end of the COVID-19 pandemic, i.e. in the recovery and restructuring phase, will be as important as in the rescue phase, but in this case other aid instruments should be used. During this period, loans aimed at investment and development should be more important than non-repayable subsidies or redemption of public law liabilities. Therefore, the state should concentrate aid resources on enterprises that will have development potential and, in the long run, will be able to independently strengthen their competitive potential in the new economic structure (post-COVID).

Previous studies on the evaluation of forms of government support show that emergency liquidity assistance (ELA) is perceived as the most effective form of saving the economy during the COVID-19 crisis. In addition, experts from the European Union, the US and other developed economies rate this form of aid the highest, while the countries of underdeveloped economies (e.g., Asia, Latin

America, Africa) believe that healthcare support should have a higher priority. The results of the same research indicate that experts in different countries are divided over which form of ELA is more appropriate: a loan or a non-refundable grant. For example, experts from Portugal, France, Belgium, France, Italy, Greece, Ireland, Austria and Romania favored grants. However, in Sweden, Finland, Bulgaria, Denmark, Poland, Slovenia, Latvia, the Czech Republic, Slovakia, Germany, Spain and the Netherlands, loans are considered more desirable (Boumans *et al.*, 2020).

Research on the assessment of individual aid measures shows that in Russia the most desirable measures to support SMEs are deferment of tax payments for 6 months (excluding VAT), deferral of loan repayment for 6 months and repayment holidays in the insurance premium for 6 months (Razumovskaia *et al.*, 2020). Meanwhile, US experts are more skeptical about the effectiveness of temporary tax deferrals (Boumans *et al.*, 2020).

## 5. Conclusions

The COVID-19 pandemic has caused many negative effects that pose a huge threat to the functioning of enterprises, in particular enterprises from the SME sector. The most serious effects caused by the pandemic include: decrease in revenues, loss of payment capacity, increase in debt, limitations in the supply of raw materials and goods, the need to change the work organization of employees (restrictions on the number of people, employee rotation, remote work), problems with access to the labor force (isolation, quarantine of employees) and changes in consumer behavior (decrease in the value of purchases of certain goods and services). As a consequence, there was a risk that many companies would not survive the lockdown and would have to shut down their businesses.

In such conditions, the role of the state is of great importance, which should provide appropriate solutions that, on the one hand, will allow enterprises to survive this difficult period, and, on the other hand, enable the reconstruction and restructuring of the business model after the pandemic is over.

One of the aid measures that allow enterprises to maintain business are liquidity loans. The analyses show that this is a solution addressed to the smallest enterprises (micro-enterprises) that have been negatively affected by the lockdown. From the point of view of an individual enterprise, the scale of the aid granted is small, which means that it is temporary and sufficient only for a certain period of time.

The analyses also show that companies whose industries were not subject to the lockdown also benefited from liquidity loans in Central Pomerania. Therefore, there is a certain risk that this form of aid will also be of interest to companies that have not suffered too much from the crisis caused by the pandemic, but due to more favorable terms of such a loan compared to a bank loan, they will compete for a loan with companies that will be in a much worse financial situation.

Another problem is the adequate availability of information on the possibility of obtaining help during the COVID-19 pandemic. Intermediary institutions which distribute aid funds (grants, loans) should conduct informational campaigns, online meetings, webinars, press advertisements, and advertisements in social media in order to reach enterprises that need this aid the most. Otherwise, taxpayers' money may be wasted.

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