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Perspectives for Mittelstand businesses in the COVID-19 pandemic.
Part 2: Challenges for the Mittelstand

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1 Preface

Since the spring of 2020, the pandemic has posed major challenges for the Mittelstand – and there is currently no end in sight. Initially, the economic restrictions were in the focus, but over time the – potential – societal and individual effects are also coming into view. One problem in estimating the impact of the pandemic on Mittelstand enterprises is large variety of different ways in which they are affected. Obviously, they are directly affected by economic upheavals as a result of the current pandemic situation. Only a relatively small proportion of companies can completely escape the negative effects of the pandemic and even profit from them.

In addition, the administration has been prescribing measures with varying intensity to contain the health and economic damage caused by Sars-CoV-2, since the beginning of the pandemic. These measures are also likely to affect a large number of companies: Almost all companies had to develop and implement hygiene concepts. For the vast majority of Mittelstand enterprises, however, the resulting consequences are likely to be minor. However, this does not apply to all companies: Those operating in infection-critical areas had to accept in some cases severe restrictions or even long-lasting forced closures. Finally, the personal component for the entrepreneurs must not be disregarded. They themselves and their families are also subject to health threats in the course of the pandemic or have to fear for the survival of their company or the jobs of (some of) their employees.

In this paper, we address these economic, societal and personal challenges for Mittelstand enterprises and explore the possible consequences for them in all their diversity.

2 The impact on the Mittelstand

2.1 The impact on the Mittelstand economy

Not surprisingly, the extent to which the entire economy is affected increases with the duration of the pandemic: initially, around 40 % of the surveyed companies stated that they had been (strongly) negatively affected (cf. IAB 2020). This fell slightly in the summer of 2020 and then increased again. Currently, more than 50 % (53 %) are (strongly) negatively affected. As expected, the sectoral differences are considerable. Trade and particularly the hospitality industry are very strongly affected, while the construction industry is almost not affected at all.

The share of businesses whose liquidity reserves will last for a maximum of two more months has risen from 28 % at the beginning of the pandemic to 32 % at present. The situation is particularly precarious in the hospitality industry, where almost 60% of businesses have only low reserves. It should be noted that the survival rate of businesses in the hospitality industry tends to be below average (cf. IfM Bonn 2021) and is also subject to seasonal fluctuations. The trade sector is also strongly affected (increase from 26 % to 38 %). The sharp increase in the number of affected businesses in the logistics sector is striking: the percentage share rose from approx. 22 % at the beginning of the pandemic to currently 44 %.

According to the results of the special surveys of the KfW Mittelstand Monitor (cf. Schwartz/Gerstenberger 2020a; Schwartz/Gerstenberger 2020b), turnover losses in Mittelstand enterprises at the beginning of the pandemic were particularly frequent in “other services” and trade, among smaller firms with up to ten employees and among the liberal professions. A large-scale survey of solo self-employed persons conducted by Verband der Gründer und Selbstständigen (VGSD) in spring 2020 illustrates this considerable impact on the smaller self-employed[1]. Monthly turnover had fallen by more than 75 % for almost 60 % of them; more than a third (35 %) expected this phase to continue for more than half a year (cf. Bertschek/Erdsiek 2020). 80 % suffered a decline in turnover of more than half; in the particularly affected sectors such as gastronomy, accommodation, art, culture and recreation, the decline in turnover was more than 75 % for nine out of ten self-employed persons (cf. Stiel et al. 2021). A large proportion already assumed in spring 2020 that they would have to fall back on their old-age provision. One in four was even considering it probable that they would have to give up their solo self-employment in the following twelve months; this was particularly the case in consumer-related sectors (cf. Bertschek/Erdsiek 2020).

According to the special evaluations of the KfW Mittelstand Panel, the Mittelstand sector is still highly affected, but it is declining. At the beginning of 2021,

[1] More than 16,000 full-time solo self-employed between the ages of 24 and 65 were surveyed. The survey was conducted by the VGSD in cooperation with ZEW Mannheim and the Research Centre for Mittelstand busineses at the University of Trier. Cf. Bertschek/Erdsiek (2020).

the proportion was lower than in spring 2020, despite the ongoing stringent anti-pandemic measures: while 80 % of SMEs were affected in April 2020, the figure decreased to 68 % in January 2021. This was only marginally higher than in September 2020 with 63 % (cf. Schwartz/Gerstenberger 2021, p. 2). 29 % of companies have not at all been affected by the crisis so far; and the initially massive impact of sales slumps has also fallen significantly at the beginning of the year (45 %, compared to 58 % in April and 61 % in June 2020). On the one hand, this could be due to the fact that companies have successfully adapted their business models to the "crisis conditions" – examples are cited in Welter et al. (2020). On the other hand, it also indicates that the anti-pandemic measures taken in combination with the aid programmes have successfully limited the damage caused by the pandemic in macroeconomic terms.

The survey results of the KfW Mittelstand Panel also indicate a considerable fundamental resilience on the part of the Mittelstand: despite the pandemic situation, which has now lasted for over a year, the vast majority of Mittelstand enterprises are still convinced that the situation will return to normal in the near future. Only 17% of companies are skeptical in this regard (cf. Schwartz/Gerstenberger 2021). Although the proportion of pessimists has risen since last summer (then 8 %), the majority of Mittelstand companies are nevertheless (at least cautiously) optimistic about the future. However, the crisis will leave its mark on the Mittelstand businesses. Liquidations have occurred and will continue to do so in the future. But even here the question must be asked to how far these company closures can be attributed causally to Sars-CoV-2 and are not part of a "normal" churning in the corporate landscape.

2.2 The impact on Mittelstand entrepreneurs

The individual affectedness of entrepreneurs goes beyond the immediate – short- and long-term – economic consequences for their entrepreneurial activity or the company. It must not be underestimated but must be taken into account when considering the overall economic and societal damage. It is possible that these may even be higher because some entrepreneurs with a solid business may soon give it up because they no longer see any prospects for the future.

In addition to the economic effects, Wach et al. (2020) name the following factors as possible emotional and cognitive stressors for entrepreneurs: Threats to their own health and that of their family members, more difficult access to work-related networks that can also provide emotional support, changes in the company's working conditions. This is likely to be compounded by worries about their own workforce in Mittelstand companies with employees.

In April 2020, the immediate consequences of the first lockdown measures on the life satisfaction of the population were analysed (cf. Ahlheim et al. 2020). Compared to the population as a whole (minus 1.15 points), the self-employed showed significantly higher declines in life satisfaction (minus 1.43 points). Not surprisingly, this decline in life satisfaction was even higher among those who experienced income declines due to the pandemic or even had to close down altogether (minus 1.81 points). Life dissatisfaction was even higher among the solo self-employed (minus 1.92 points), generally among self-employed women (minus 1.85 points) and even with minus 2.29 points among the negatively affected self-employed women. It also showed that the self-employed feel more vulnerable: Around 55 % of them feared major financial consequences. By comparison, among all respondents this was 42 % (cf. Windsteiger et al. 2020, p. 590, cited in Alheim et al 2020).

It is true that the economic situation of the solo self-employed and micro-enterprises has become worse in the course of the pandemic, according to a recent Schufa survey from March 2021 (https://www.schufa.de/ueber-uns/verantwortung/schufa-risiko-kredit-kompass/schufa-risiko-kreditkompass.jsp). Compared to the population as a whole (38 %), they also had to accept much greater declines in their household income (70 % self-employed, 64 % micro-enterprises) – whereby dissatisfaction with the financial situation has risen again, especially among the self-employed: from 50 % in October 2020 to 60 % in March 2021. Nevertheless, a large part of the self-employed and micro-enterprises are still positive about the future of their business: More than 60 % of the solo self-employed and three quarters of the micro-enterprises assess the future of their own business as (very) secure.

This optimism of entrepreneurs was also shown in a smaller survey by Wach et al. (2020), which was conducted from mid-April to the beginning of May 2020[2]: Almost three quarters of the solo self-employed and over 80 % of SMEs in Saxony, as well as around two thirds of respondents in the rest of Germany, expected their business to recover from the crisis at that time. Obvi-

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2 The report of the follow-up survey, which was conducted from 4 December 2020 to 15 January 2021, is currently being written.

ously, the situation for the majority of entrepreneurs is less dramatic than it sometimes appears from the media presentation, which often focuses on particularly affected companies/industries. It is to be assumed that many entrepreneurs have meanwhile made their production and sales processes „pandemic-proof" on their own initiative.

3 Economic and societal damage

The frequently heard view that health and the economy are conflicting goals falls too short. Dorn et al. (2020) already showed by means of model calculations that a complete abandonment of anti-pandemic measures would be associated with considerable economic damage. Strictly speaking, a distinction must be made here between damage caused by the pandemic and damage caused by the anti-pandemic measures: The uncertainties, declines in demand and absenteeism due to illness or quarantine that accompany the pandemic definitely also harm the economy. These damages affect the entire economy and society. However, they can be reduced through anti-pandemic measures. These measures, on the other hand, also cause burdens. Although these only affect some sectors of the Mittelstand economy, they affect them all the more severely and are therefore often met with incomprehension by those affected. From an overall economic perspective, these measures are nevertheless sensible according to the Hicks-Kaldor criterion, provided that the pandemic damage is reduced to such an extent that it would at least hypothetically be possible to fully compensate those affected by the measures.

In the public discussion about relaxation, often only the harmful, economic consequences of the anti-pandemic measures are discussed. However, the resulting lower costs of being less affected by the pandemic are often forgotten. These costs tend to be inconspicuous, as they affect many companies a little, while the measures affect (relatively) few companies or sectors very strongly. Ideally, the anti-pandemic measures reduce the impact of the pandemic on the Mittelstand enterprises, for example by preventing high sickness levels in the workforce. However, the companies that are strongly affected by the anti-pandemic measures, i.e. those sectors that are currently unable to carry out their business activities, do not necessarily benefit from the positive effects of the measures: When the company is closed, the low sickness rate of the workforce is irrelevant. This leads to dissatisfaction in large parts of the Mittelstand sector.

In order to assess the challenges for the Mittelstand, a correct differentiation must therefore be made between the companies affected by the pandemic and those affected by the measures. Both negative and positive effects of the anti-pandemic measures on the Mittelstand economy would also have to be considered. However, when considering the economic and societal damage in quantitative terms, it is not possible to distinguish whether it was caused by the pandemic itself or is a consequence of the anti-pandemic measures: For example, one can look at the development of unemployment or short-time work in the hospitality industry. It is not possible to distinguish between what is due to declining demand as a result of cautious customers and what is due to administratively ordered closures. The following key figures of economic developments can therefore only be a synthesis.

Furthermore, many effects defy precise quantification. For example, at the present time it is not possible to precisely quantify the societal burden of additional pandemic-related illnesses or quarantine times. Even a rough calculation shows that the damage would have to be considerably higher and would have assumed unimagined proportions if the pandemic had proceeded unchecked. For example, with an incidence of 200 cases per 100,000 inhabitants and an assumed average of five close contacts per infected person, around 800,000 employees subject to social security contributions would be lost every day due to isolation or quarantine.

The impossibility of quantification also applies in principle to many other negative consequences of the pandemic. It is clear that – especially in the spring of 2020 – there was a drop in demand as a result of the increased uncertainty. However, we can only speculate on how demand would have developed without the curbing measures taken – or even if more restrictive measures had been taken. Since a considerable proportion of entrepreneurs belong at least to the extended risk group,[3] there have certainly also been distortions due to sudden changes at the top of the company as a result of the illness or death of the entrepreneur. None of this can be meaningfully quantified. Nevertheless, such circumstances are relevant with regard to the damage caused by Sars-

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3 Contrary to popular belief, it is not possible to clearly separate the at-risk group from the rest of the population. As Levin et. al. (2020) show in a meta-study on the dependence of infectious mortality on age, the risk increases largely linearly with age. For example, the risk of a 50-year-old relative to a 20-year-old is increased by about the same factor as that of an 80-year-old relative to a 50-year-old.

CoV-2. In the following, an attempt will be made to show at least some indications of the extent of the pandemic-related damage.

The first step is to take a look at the **development of the employment situation**: Has there been an increase in unemployment (including short-time work) in the course of the Covid-19 pandemic and, if so, which sectors of the economy have been particularly affected?

Seasonally adjusted unemployment rose sharply in spring 2020 from 5.0 % in March to 6.4 % in June. This was followed by a slight decline, which continued during the second lockdown. Currently (February 2021), the figure is 6.0 %. This is significantly higher than the previous year's value (5.0 %). As expected, the decline in employment in the hospitality sector was particularly marked (- 10.1 % compared to the same month last year). Only a slight decrease in employment was recorded in the service sectors. In trade, the employment situation is even practically unchanged compared to the same month of the previous year (as of December 2020) (cf. Bundesagentur für Arbeit 2021). The number of people in (notified) short-time work exploded in the early phase: within two months there was an increase from 40,000 to over 8 million claimants. After a significant decline in the following months to just under 110,000 persons in September 2020, the number of notified short-time work increased again in the course of the second wave of the pandemic. However, this new increase was much lower than in spring 2020 and reached its (provisional) maximum of just under 1 million people in January 2021. It is striking that the manufacturing sector – in contrast to spring 2020 – is currently only using short-time work to a relatively small extent. Short-time work is currently being used heavily in trade and in the service sector. In the hospitality industry, short-time work is currently used much less frequently than during the first pandemic phase (cf. Bundesagentur für Arbeit 2021a).

A number of questions arise, particularly with regard to the future of employment relationships in the Mittelstand sector. Basically, one of them is even the question of whether the pandemic will cause the Mittelstand to lose what makes it special, namely their long-term orientation: (How) Will the pandemic change employment relationships in the Mittelstand enterprises? What will happen to apprenticeship training, which has so far been supported disproportionately by Mittelstand enterprises?

Value added: Calculations by the Ifo Institute point to massive reductions in value added due to the lockdown regulations that have been in force since December 2020 (cf. the figures quoted in Baumann et al. 2021, p. 24): The restrictions on the hotel and catering industry, stationary retail trade and numerous social service providers result on average in weekly lost revenue of almost 2.5 billion euros. However, the number of Mittelstand enterprises is particularly high in the hotel and restaurant industry and in the service sector, so that the loss of value added for the Mittelstand as a whole is likely to be disproportionately high as a result. Most affected by value-added losses is the manufacturing industry, thereof above all the automotive (10.7%) and pharmaceutical industries (-11.3%) as well as mechanical engineering (cf. Bunde 2021).

Finally, it can be assumed that the economic recovery that has become apparent in the meantime has not been able to take hold, especially among the self-employed and micro-enterprises. Moreover, in many cases these segments only have relatively modest resources, so that their reserves tend to be used up more quickly than is the case with larger companies. Particularly in connection with their individual affectedness, it is therefore to be assumed that the share of business closures among the solo self-employed and micro-enterprises could be disproportionately high in the further course of the pandemic. Dörr et al. (2021), for example, assume that the aid money paid or the temporary suspension of the obligation to file for insolvency has led to a reduction in the number of insolvencies, especially among micro-enterprises, but that this will hardly be sustainable in the long term. With the increasing duration of the pandemic, a growing number of company closures can therefore be expected. If this were to happen, the diversity that makes up the Mittelstand would be reduced to some extent.

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