Yale SCHOOL OF MANAGEMENT

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Experiences and Impact of Response to COVID-19 Crisis

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YPFS Pandemic Economic Cycle

Run

Interventions launched to stem a run on liquidity of financial institutions and markets

- Asset purchases
- Swap lines with 14 central banks (including Banco Central do Brasil and the Banco de Mexico) from the U.S. Federal Reserve

Rescue

Programs to preserve SMEs and key industries hardest-hit

Programs to rescue regional and municipal governments

- Colombia federal government provided direct capital injections to local governments

Recession

Fiscal policies increasingly become important in alleviating distress in the face of reduced demand

- Support individuals and households

Macroprudential policies (temporary relaxation of financial requirements with clear guidance)

- Relaxing bank capital requirement rules
- Changes to bankruptcy rules to favor debtors

Maintain the health of the banking system so that they can aid in the next phase

Ensuring the emerging market have enough to maintain their economies

Recovery

Promotion of economic recovery after successful management of infection rate or accompanied by other medical advancement

- Aim to boost household demand and promote job creation (Austria, Germany, South Korea)
- Banks need to emerge from the recession with strong capital structures in order to grow the economy during the recovery

Asset Purchases

- Different from previous crises, emerging market responses included asset purchase programs by central bank (and in some cases first time ever)
- Expressed goal: to avoid the potential adverse effects on financial stability and the deterioration of monetary policy transmission channels (purchases from secondary markets)
- U.S. quickly implemented these programs in March based on its experience during 2007-09 global financial crisis
- Lessons:
  - A balance between incentivizing the participants to reenter the market and minimizing the risk to the central bank (haircuts, interest rates, and fees)
  - Response time is crucial in resolving liquidity problems
  - Ensure that central bank is not undermining the appropriate functioning of targeted markets
    - In giving the Chilean central bank power to purchase debt securities on the secondary market, the bill approved by the Chilean Congress in August emphasizes this is a temporary measure due to the exceptional circumstance.

Support for SMEs

- Unlike past crises, grants, subsidies, forgivable loans, and equity instruments are more common as increasing an SME’s debt burden may not be ideal
  - U.S. Federal Reserve extended loan terms and deferred amortization under Main Street Lending Program
  - Convertible bonds or hybrid instruments (France, Ireland, Germany)
- Targeting assistance too narrowly (i.e. firm eligibility) can slow down the provision of support and will prevent firms that actually need support from receiving it
  - U.S. Paycheck Protection Program (PPP) faced pushback regarding large, publicly-traded recipients
  - EU revised state aid rule that had excluded companies “in difficulty” from SME support to enable start-up tech companies to receive such support
  - Peru lowered credit rating requirements for credit guarantee scheme
- High levels of due diligence required by lenders can limit the overall participation levels
  - UK removed requirement that SMEs prove they were unable to access funding elsewhere
- Strict limitations on how assistance can be used can lead to underutilization and require later changes to the program
  - The U.S. PPP requirement to spend 75% on payroll to be eligible for full forgiveness was reduced after significant pushback

Support for SMEs

- Considering how to provide aid that reaches firms and employees that are not registered is important for countries with large informal sectors
  - Malaysia expanded its emergency grant program for micro-SMEs
  - May be accompanied by support to individuals (Thailand: grant of 5,000 baht per month for three months for informal workers to reach 14.5 million)
- Aligning incentives can encourage more private-sector lender participation
  - There has been an increase in 100% guarantees (initially Japan, Hong Kong, Korea), and EU countries now have 100% guarantees (up from a 90% limit)
  - Countries have increased the ceiling on interest rates (U.S.) and fees banks can charge on credit guarantee programs and lowered fees
- Winding it down: tying support to economic or health indicators can enable a government to quickly support SMEs if conditions change rapidly
  - Spain released funding for its EUR 100 billion credit guarantee scheme in tranches to adapt to changing economic conditions and the needs of the most impacted sectors

Individual and Household Support

- Support to individuals and households is a key component of policy responses at both recession and recovery stages
  - Chile and Peru: focus on support for vulnerable households and unemployed workers as well as preventing further job destruction
- Effective public health measures are essential to allow countries to transition from the recession to the recovery phase
  - Korea limited the shock to the labor market by gaining rapid control over the rate of infection through proactive public health measures while also providing income support to vulnerable households. This allowed it to avoid shutting down its economy.

Multinational Effort

- The EU's macro-financial assistance program to 10 neighboring countries operates in tandem with and to complement IMF disbursements to these countries.
- Following the global financial crisis in 2007-09 all multilateral development banks simultaneously increased their members' capital allocations.
- For 2020, the U.S. Congress authorized the country to participate in the World Bank general capital increase.
- G20 yet to support a new allocation or a reallocation of special drawing rights (SDRs) at the IMF
  - Thus far, the G20 had discussed it, but could not find a consensus on the issue.

- Mission to create, disseminate, and preserve knowledge about financial crises
- Created in 2013, focused on research and study of the global financial crisis; since 2017 shift focus to developing a crisis-fighting playbook; then slight shift again in March this year to focus on responses to covid-19
- Developed a tracker for world-wide covid-responses now having more than 7,000 interventions listed
- Also, we write short posts on certain interventions