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INSIGHT

Fiscal and Monetary Policy Initiatives by Major Economies to Address COVID-19

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Overview

In response to the pandemic-related collapse in global economic growth in the first half of 2020, national governments, central banks, and international organizations adopted unprecedented fiscal, monetary, and other measures to stabilize financial markets and stimulate growth. The policy responses directed at the initial liquidity crisis in the financial sector have also significantly raised government debt levels, pushed unemployment rates to their highest levels in a generation, and reduced global economic growth by an estimated 3.0% to 6.0%. The human costs in terms of lives lost could permanently affect global economic output in addition to the cost of rising poverty levels, lives upended, shuttered businesses, and increased social unrest.

Given the evolving nature of the health crisis, the economic crisis may persist longer than most forecasters previously have assumed. A resurgence of cases in the United States, Europe, Asia, and Africa has pushed some policymakers to reimpose restrictions, delaying economic recovery. Second quarter U.S. gross domestic product (GDP) data indicates that economic output fell by 33% at an annual rate.

The challenge for policymakers is one of implementing targeted policies that address what had been expected to be short-term problems without creating distortions in economies that could outlast the impact of the virus. Many policymakers, however, have been overwhelmed by the quickly changing nature of the health crisis that has turned into a global trade and economic crisis.

The IMF recently concluded that a number of preexisting vulnerabilities could interact with the pandemic to affect the timing and strength of the global economic recovery. These vulnerabilities include corporate and household debt levels in developed and some emerging economies that could become unmanageable in a prolonged recession; rising insolvencies testing the resilience of the banking sector; additional stresses affecting nonbank financial institutions; and some developing economies facing high external financing requirements.

Should these crises persist, policymakers may initiate additional fiscal and monetary measures. Such measures, however, are likely to present policymakers with difficult choices given the economic resources that already have been expended and could include weighing the demands of households, firms, and sub-

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national governments seeking public assistance. In particular, liquidity constraints in the pandemic's initial phase could be succeeded by such challenges as firm bankruptcies, rising unemployment as short-term wage supplements expire, home foreclosures and evictions, and lost tax revenues for state and local governments.

Fiscal Policy Response

As a fiscal response, governments have provided direct support to the health sector, households, and firms, although the size and scope of the programs vary by country. As indicated in **Table 1,** these measures broadly include

- wage and income supplements to households, including expanded unemployment insurance;
- tax cuts and deferrals to households and businesses;
- direct payments to households and;
- other payments to businesses.

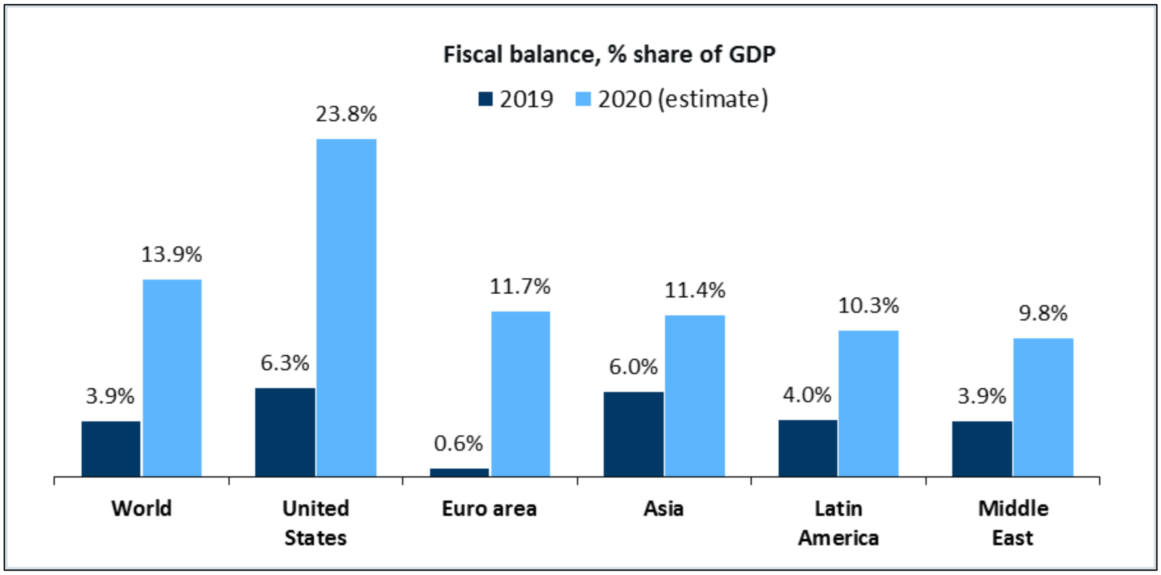
The U.S. Congress approved historic fiscal spending packages; other governments abandoned traditional borrowing caps to increase fiscal spending in order to sustain economic growth. EU members recently agreed to support a €750 billion pandemic economic assistance package. In March, President Trump signed three major pieces of legislation providing similar assistance (P.L. 116-123), (P.L. 116-127), and (P.L. 116-136). International organizations have taken steps to provide loans and other financial assistance. Consumers in the United States and Europe have sharply increased their savings, potentially blunting the economic impact of fiscal spending.

The International Monetary Fund (IMF) estimated that government spending and revenue measures to sustain economic activity adopted through mid-June 2020 amounted to $5.4 trillion and that loans, equity injections and guarantees totaled an additional $5.4 trillion, or a total of $10.8 trillion. The IMF estimated the increase in budget deficits by governments globally would rise from 3.9% of global GDP in 2019 to 13.9% in 2020, as indicated in **Figure 1**.

Among developed economies, the fiscal deficit to GDP ratio is projected to rise from 3.3% in 2019 to 16.6% in 2020; the U.S. ratio is projected to rise from 6.3% to 23.8%. Developing economies' ratio is projected to rise from 4.9% to 10.6%.

Figure 1. IMF Projected Government Budget Deficits (Fiscal Balances) Relative to GDP

In percentage shares of Gross Domestic Product



Source: *World Economic Outlook Update*. International Monetary Fund, June 24, 2020, p. 20. Created by CRS.

Note: Data for 2020 are estimates.

Monetary Measures

Among central banks, the Federal Reserve has taken extraordinary steps to address the growing economic effects of COVID-19, again effectively serving as the global lender of last resort, reflecting the role of the dollar as the dominant global reserve currency. Similarly, other national central banks and monetary authorities adopted a range of monetary and prudential measures (**Table 2),** although central banks lack the policy measures to address the health crisis itself. Central banks initially provided liquidity through changes in interest rates and bond-buying operations, including

- forward guidance;
- lowering interest rates and reserve requirements;
- announcing new lending and financing facilities;
- expanding asset purchases;
- extending foreign exchange swaps; and
- relaxing some prudential measures, including capital buffers and, in some cases, countercyclical capital buffers, adopted after the 2008-2009 financial crisis.

Central banks acted as a lender of last resort through lending to banks, but also as buyers or lenders of last resort for private sector securities, in many cases engaging in activities previously considered off-limits.

Prudential Measures

Various central banks also engaged in prudential measures, or regulation and supervision to ensure the soundness and adequacy of capital buffers of individual banks through capital requirements (micro prudential) and financial regulations that address the stability and systemic risk of the financial system as a whole (macroprudential). The Financial Stability Board (FSB) concluded that actions to date to support the global financial system have worked effectively to contain the financial and economic impact of the pandemic, although the crisis is not yet over.

Table 1. Elements of Announced Fiscal Measures to Address COVID-19

	Advanced Economies							Emerging Market Economies							
Measures	US	JP	DE	FR	IT	ES	GB	BR	CN	ID	IN	KR	MX	RU	ZA
Measures supporting the health sector															
	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x
Measures supporting households															
Targeted transfers a	x	x	x	x	x	x	x	x	x	x	x	x		x	x
Other labor income support b	x	x	x	x	x	x	x	x	x	x	x	x		x	x
Wage subsidies	x	x	x	x	x	x	x	x	x		x	x		x	x
Tax cuts	x	x	x	x		x			x	x	x	x		x	x
Tax deferral	x	x	x		x	x	x				x	x	x		x
Measures supporting firms															
Tax deferral	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x
Liquidity support c	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x
Tax cuts	x	x	x		x	x	x	x	x	x	x	x		x	
Targeted transfers		x	x	x	x		x		x	x				x	x

Source: *Annual Economic Report 2020*, Bank for International Settlements, June 2020, p. 24, based on data collected by the International Monetary Fund and the Organization for Economic Cooperation and Development.

Notes: a. Includes cash and in-kind transfers to affected households. b. Extended unemployment and sick leave benefits. c. Non-budgetary measures such as equity injections, asset purchases, loans and debt assumptions or government guarantees and contingent liabilities. US: United States; JP: Japan; DE: Germany; FR: France; IT: Italy; ES: Spain; GB: Great Britain; BR: Brazil; CN: China; ID: Indonesia; IN: India; KR: South Korea; MX: Mexico; RU: Russia; ZA: South Africa.

Table 2. Selected Central Bank and Prudential Measures to Address COVID-19

		Advanced economies							Emerging market economies							
Type of tool	Measures	US	EA	JP	GB	CA	AU	CH	BR	CN	ID	IN	KR	MX	TH	ZA
Interest rate	Policy rate cut	x			x	x	x		x	x	x	x	x	x	x	x

Lending liquidity	Gen. liquidity provision a	×	×	×	×	×	×	×	×	×	×	×	×	×	×	×
	Specialized lending	×	×	×	×		×	×	×	×		×	×	×	×	
Asset purchases/ sales	Government bonds	×	×	×	×	×	×				×	×	×		×	×
	Commercial paper	×	×	×	×	×							×			
	Corporate bonds	×	×	×	×	×							×		×	
	Other private securities b		×	×		×										
FX swap/ intervention	USD swap line		×	×	×	×	×	×	×				×	×		
	FX intervention							×	×		×	×	×	×		
Prudential rules and regulations	Capital requirements	×	×	×	×	×	×	×	×	×	×	×	×	×		×
	Liquidity requirements	×	×	×	×	×	×	×	×	×	×	×	×	×	×	×
	Payout restrictions		×		×	×	×	×	×		×	×	×	×	×	×
	Market functioning c		×	×	×	×	×	×	×	×	×	×	×	×	×	×

Source: *Annual Economic Report 2020*, Bank for International Settlements, June 2020, p. 23.

Notes: a. Repo and reverse repo operations, standing facilities, modified discount window and lower reserve requirement ratio. b. Asset- and mortgage-backed securities, covered bonds and exchange-traded funds. c. Shortselling bans and circuit breakers. US: United States; EA: Euro Area; JP: Japan; GB: Great Britain; CA: Canada; AU: Australia; CH: Switzerland; BR: Brazil; CN: China; ID: Indonesia; IN: India; KR: South Korea; MX: Mexico; TH: Thailand; ZA: South Africa.

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