COVID Credit Policies Around the World: Size, Scope, Costs and Consequences

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Introduction

- Governments around the world deployed credit polices during the Covid19 pandemic on a historically unprecedented scale
  - Our focus is on credit policies which, like traditional fiscal spending, provided incremental resources to households and firms
    - loan guarantees and direct government lending to firms
    - large-scale forbearance programs (e.g., mortgages, and bank loans to SMEs)
    - Relaxation of regulations that accommodated these policies
- Main goal is measurement—how to size credit programs to evaluate their macro effects alongside fiscal policies?
- Empirical analysis covers credit policies for seven large advanced countries
  - France, Germany, Italy, Japan, Spain, United Kingdom, and United States
  - In dollar terms accounts for > 90% of pandemic credit support globally
  - Developing countries expanded fiscal and credit policies much less

Conceptual questions

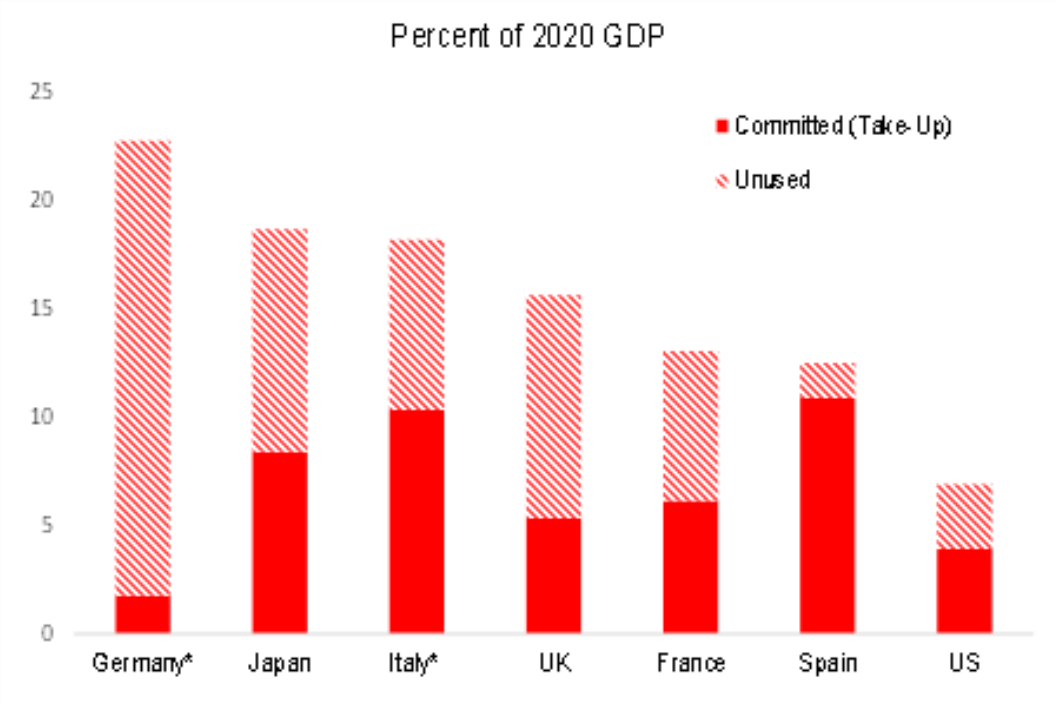
- How to size credit policies to be comparable to fiscal policies for macroeconomic analysis?
  - Unifying concept of “incremental resources provided”
  - Focus on extensive margin effects: relaxation of borrowing constraints
- How to measure subsidy (budgetary) costs?
  - At market or fair value of loan concessions from gov’t
- How should governments account for credit support? How does that compare to current practices?
  - Budgetary cost recognition upfront at fair value; subsequent tracking of take-up, performance, etc.
  - Often off-balance-sheet with no upfront cost recognition; inconsistent reporting of ex post outcomes
- Transmission channels for credit policies?
  - Similar fiscal and monetary policies, via demand-side effects; important interactions with monetary policy
- Multiplier effects?
  - Hard to measure
  - Very elevated savings rates suggests may have been smaller during pandemic than in past recessions

Conceptual questions

- Pros and cons of different credit policies and traditional fiscal policies?
  - Traditional fiscal policies (transfers, tax cuts)
    - Advantages: greater transparency; can be tightly targeted; can reach low-income households & firms that don't participate in credit markets; discipline of budgetary process
    - Main disadvantage is relatively high cost
  - Government loan guarantees and direct lending
    - Advantages: can have high "bang-for-the-buck" when credit markets are disrupted; need to repay helps screen out those not needing money
    - Disadvantages: can have high overhead; limited target efficiency; defaults cost to borrowers and gov't; lack of transparency; long-horizon fiscal risks
  - Forbearance policies (payment holidays, debt moratoriums)
    - Advantages: quick relief with little new bureaucracy; can be targeted fairly tightly; cost may be quite low
    - Disadvantages: only helps existing debtors; often unfunded mandates on private sector = hidden taxes; lack of transparency; may be hard to get payments restarted

Government Loan Guarantees and Direct Loans to Firms

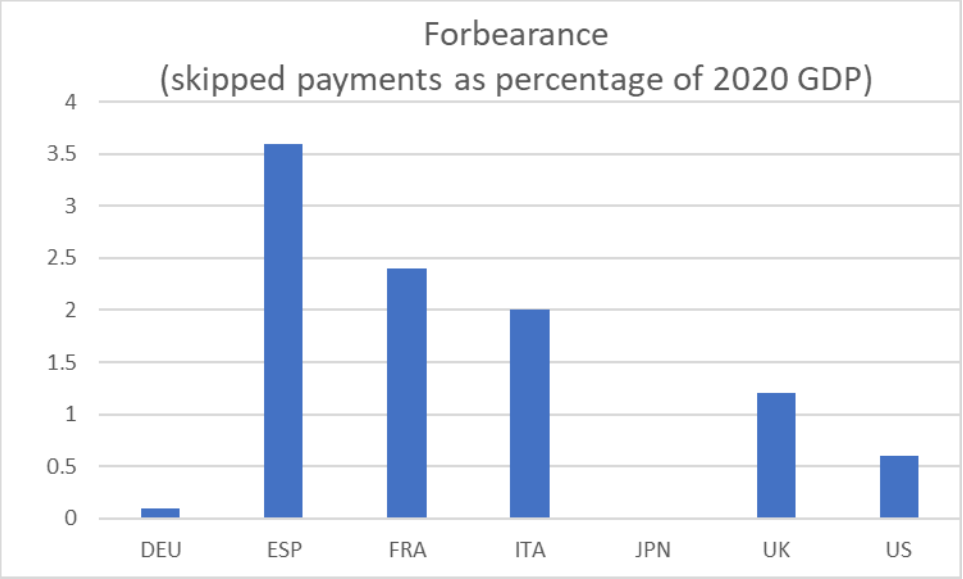
- “Incremental resources provided” measured by principal take-up (Hong & Lucas, 2023)
- Predominantly loan guarantees, many to SMEs
- 80% to 100% guaranteed
- Typical maturities of 3 to 7 years
- Authorized “Envelope” often far exceeded ”take-up”



- Fiscal costs (from Hong & Lucas, 2023) totaled $330 billion ($1.1 trillion including the U.S. PPP)
- Dividing total fiscal cost by total take-up, the average subsidy rate is 37 percent (67 percent including PPP)
- The subsidy rate varies widely across programs as a function of riskiness of target borrowers; size of rate concessions; loan maturity; fees; and other features

Credit forbearance policies

- "Incremental resources provided" equated to estimates of payment amounts skipped
  - May be some offset when implemented with mandates on private sector lenders
- Estimates original to this paper
- Very limited data => may be underestimating
- Largest programs for residential mortgages and bank loans to SMEs; also student loans, auto, …
  - (Rent payment holidays are either fiscal or unfunded mandates on private sector)
- Typically for < 1 year initially; many were extended but most have ended



Regulatory accommodations

To encourage participation in forbearance and loan guarantee programs, certain rules and regulations were temporarily relaxed.

- E.g., in EU application of qualifying moratoria did not automatically trigger forbearance classification or non-performing status of the exposure.

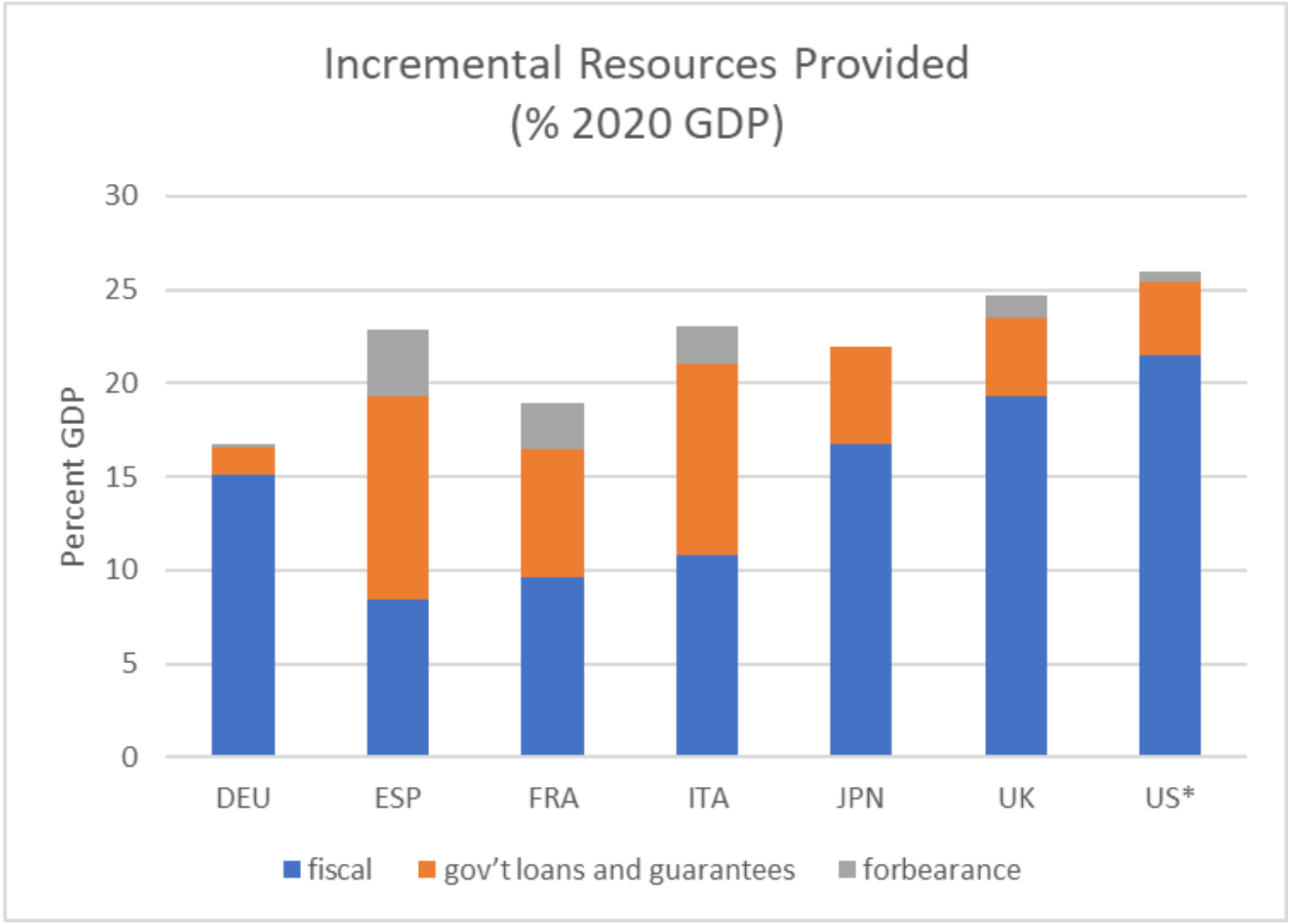
Despite influx of risky borrowers in guarantee programs, banks' reported risk-weighted-assets fell

- EU banks reported average RWAs to be 18% of the exposure value for loans made under public guarantee schemes, whereas the average RWA was 54% for banks' loans to non-financial corporations.

Reduction in risk weights was appropriate from a bank regulatory perspective because the guaranteed loans were in fact low-risk for the banks

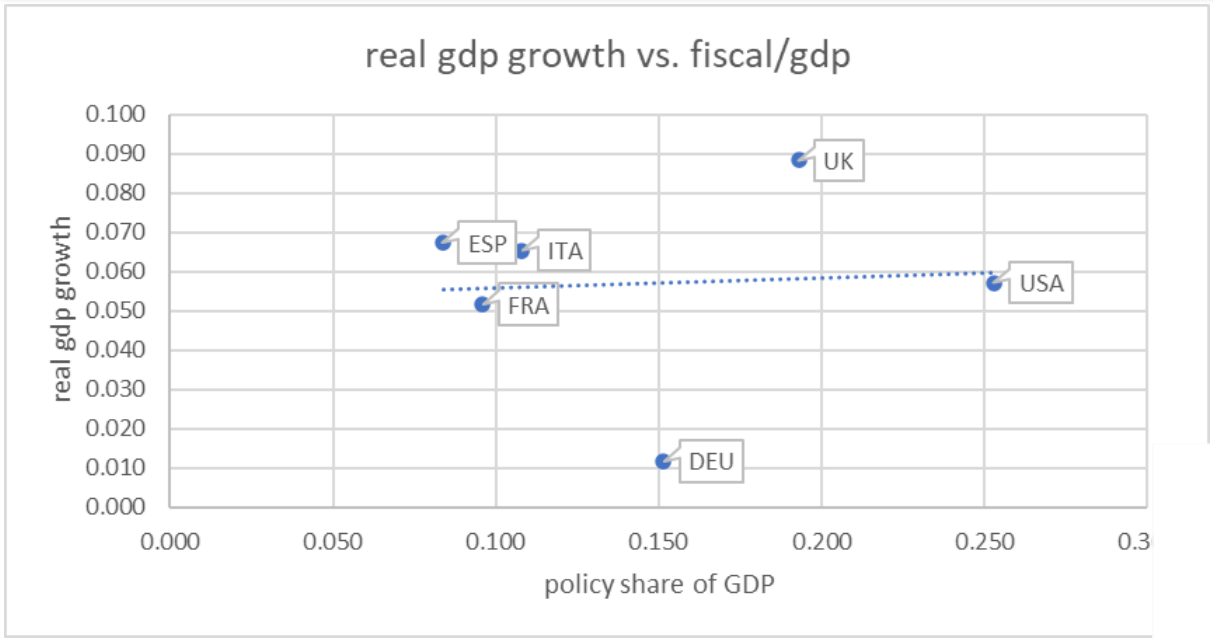
However, a naïve reading of bank health metrics could have given some policymakers the false impression that credit risk in the economy was much lower than it actually was.

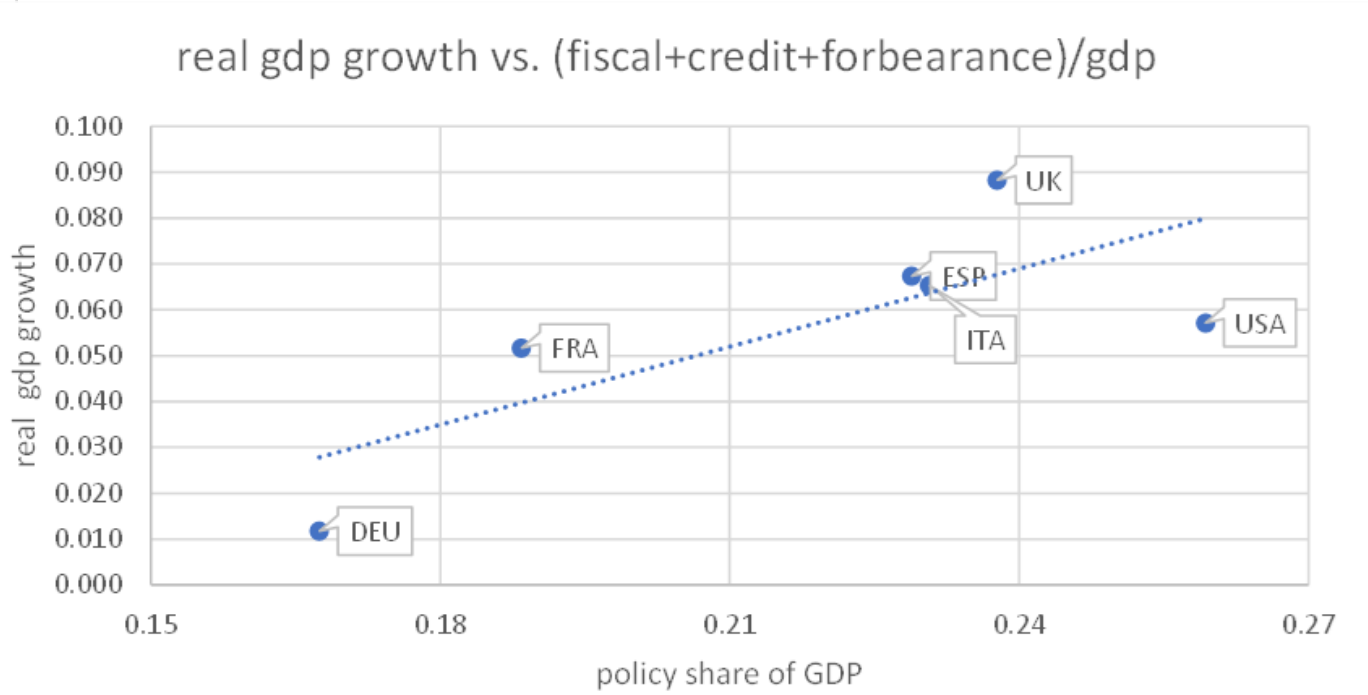
- Sharply rising default rates now reported in EU
- Inflated credit scores in US from student loan moratorium



Average Fiscal	14.5%
Average Fiscal+credit+forbearance	22.0%

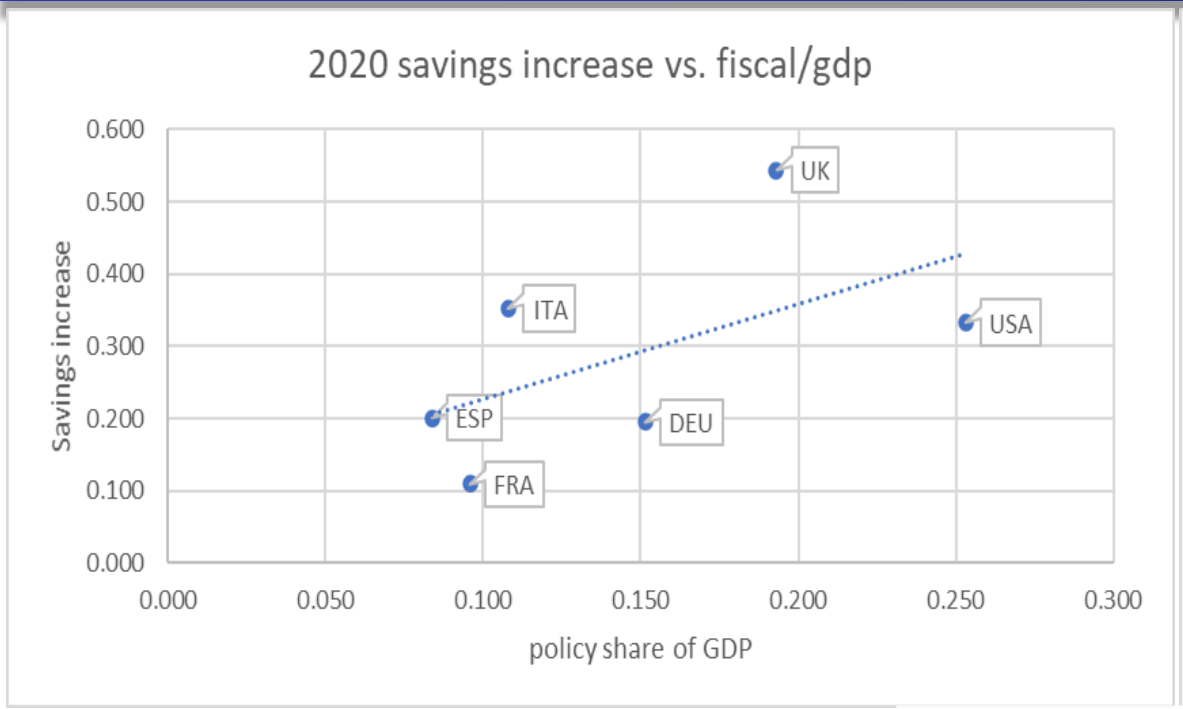
Relation between growth real GDP and alternative policy measures

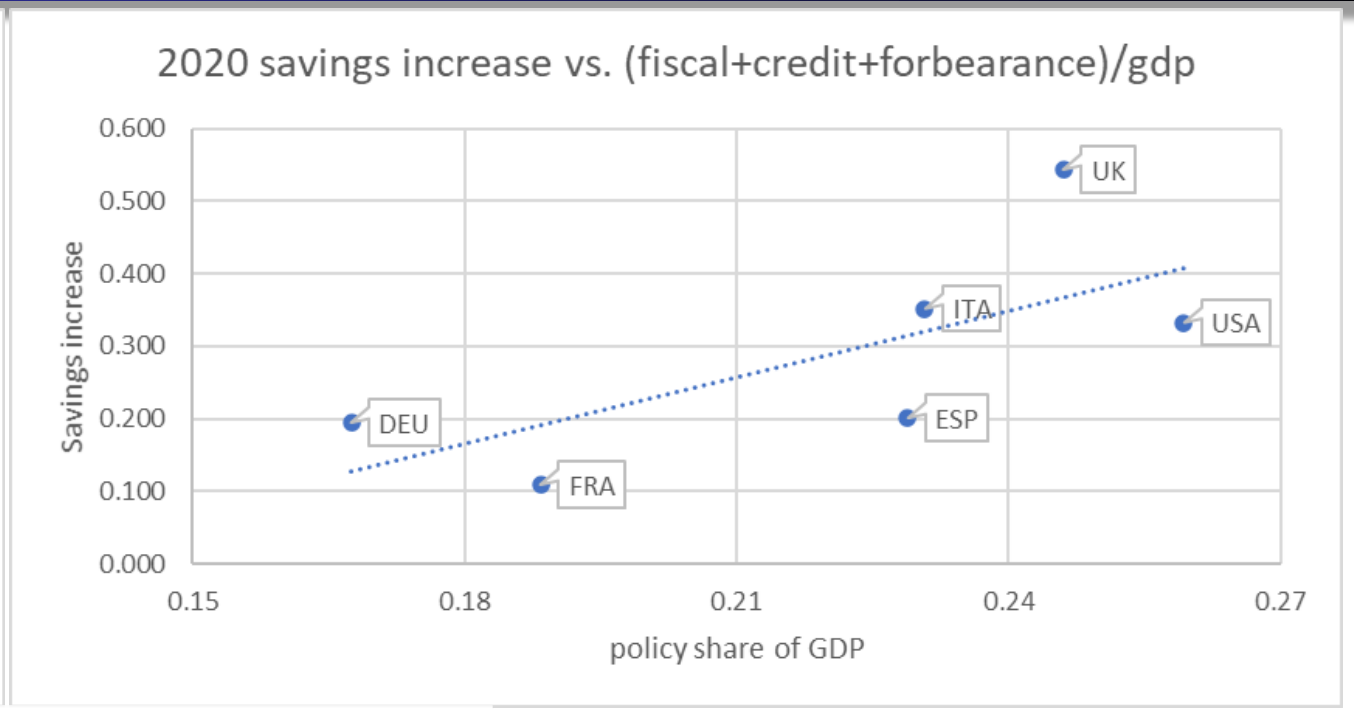


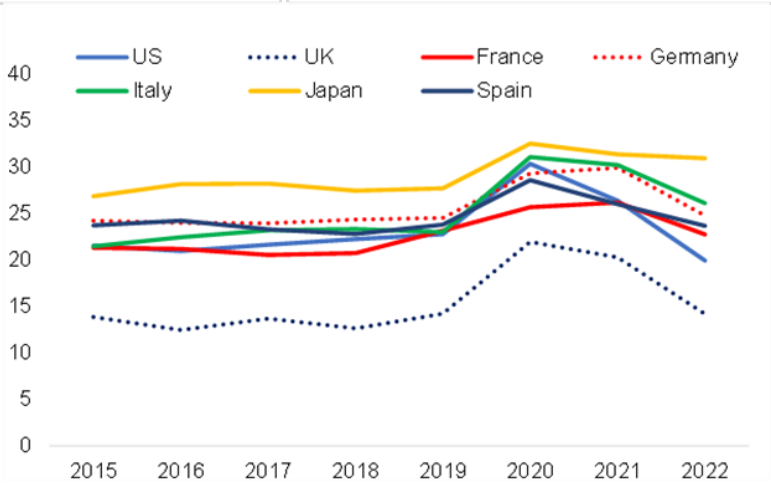


GDP growth is between Q4 2020 and Q4 2021, ex Japan

Relation between growth private savings rate & alternative policy measures

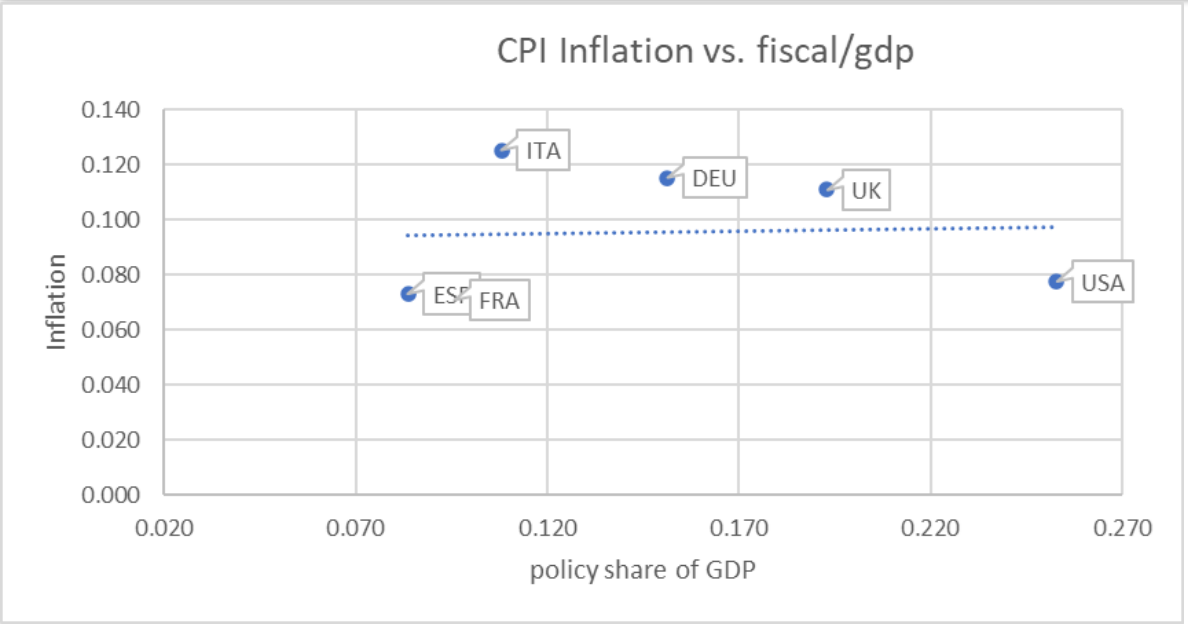


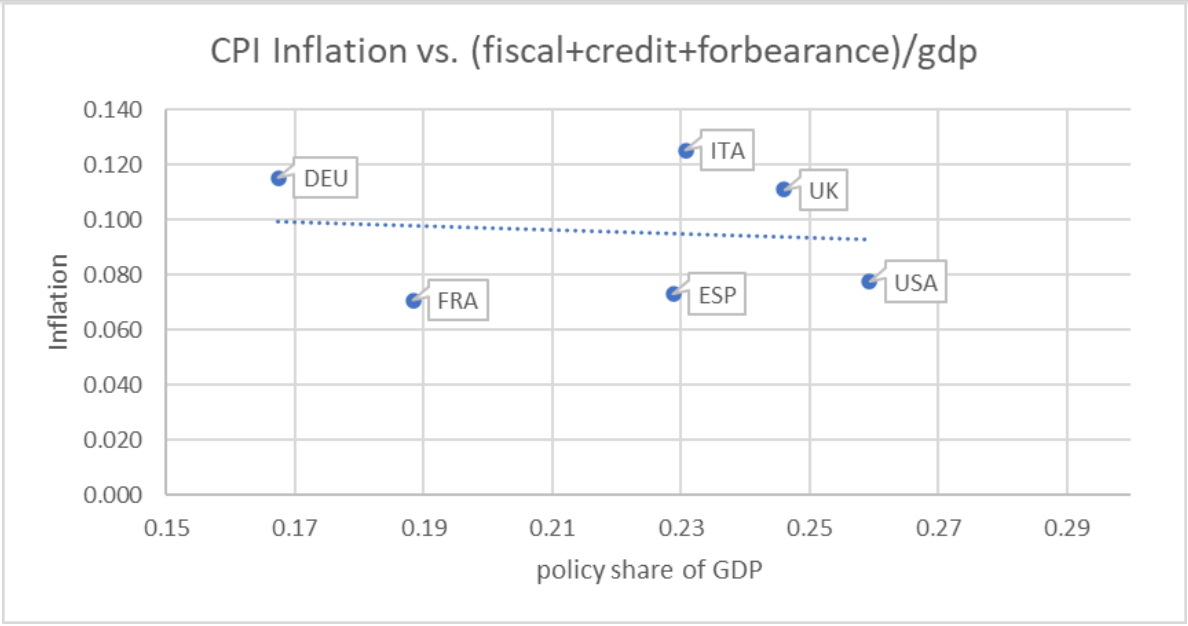




Increased saving is the difference between gross private saving in 2020 and in 2019, divided by 2020 GDP.

Relation between inflation & alternative policy measures





Correlations	(ex Japan)		
	Inflation	Savings	Real GDP
Inflation	1		
Savings	0.51	1	
Real GDP	-0.09	0.65	1
Fiscal	0.17	0.63	0.08
Fiscal+credit	0.06	0.79	0.61
Fiscal + credit + forbearance	-0.1	0.69	0.79

Inflation is the ratio of CPI in October 2021 to the CPI in October 2022 (minus 1)

Conclusions

- **Credit support & forbearance policies injected significant additional funding into advanced economies**
  - Incremental fiscal spending alone averaged 14.5% of GDP, whereas adding credit brings average to 22%
  - Much more uniformity across countries in the combined policies than in their individual components
  - Some evidence of macro effects: Combined policies seem to better explain cross-country differences in real GDP growth and saving rates than does fiscal policy alone, with the caveat of small sample size
- **Our calculations were restricted to large advanced economies because data limitations. Hope is that future researchers will undertake similar analyses for additional countries**
  - Some risks particularly salient for emerging markets: lack of transparency; hidden fiscal risks that are like to materialize when the economy is weak and fiscal resources are scarce; less capacity than advanced economies to evaluate risks and manage future fiscal impacts
- **Economists should give credit policy the standalone status accorded to monetary and fiscal policies**
  - It is much to the detriment of good policy choices that the costs and other information about credit policies are poorly and inconsistently measured and reported on in official statistics