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

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Governments around the world deployed credit policies 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
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
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
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
Increased saving is the difference between gross private saving in 2020 and in 2019, divided by 2020 GDP.
Relation between inflation & alternative policy measures

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

Correlations (ex Japan)

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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