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

Comments on Hong and Lucas

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How Do Credit Programs and "Regular" Fiscal Policies Differ (& why should we care?)

- Authors: budgetary effects are different
  - Regular fiscal policies: impact effect = cost
  - Credit policies: loans, even if subsidized or with deferred payments, have a net cost < (usually <<) impact effect; issue is how to measure

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  - Bush (1992) withholding tax change
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- This is also true even when enacted policy changes don't have this pattern initially
  - We account for this automatically when using a VAR or local projections to study the effects of policy changes

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  - Bush (1992) withholding tax change
  - True also for "real" policy changes, e.g., bonus depreciation
- This is also true even when enacted policy changes don't have this pattern initially
  - This would also be true of credit programs, to the extent that initial changes lead to subsequent ones

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- Credit policies may help relax temporary borrowing constraints
- But this is not the apparent motivation for many credit policies adopted during COVID (e.g., student loans)

How Do Credit Programs and "Regular" Fiscal Policies Differ (& why should we care?)

- Credit policies are treated differently in the budget
  - Addressing this was an objective of the Federal Credit Reform Act of 1990
  - Authors argue that this reform didn't go far enough because discounting assumptions overvalue future repayments
  - But most countries do far less, which could tilt decisions toward the use of credit programs

How Do Credit Programs and "Regular" Fiscal Policies Differ (& why should we care?)

- Credit policies are treated differently in the budget
- Budget treatment may also have encouraged use of forbearance polices imposed on the private sector
  - Hidden taxes and transfers reduce measured program size
  - The may also appear efficient when taking the form of capital levies

What the Paper Finds

- Credit program impact varies a lot from "envelope" size among seven countries studied in depth
  - Credit programs seem to be substitutes for regular fiscal policies, in the sense that the sum of impact effects varies much less across countries than either fiscal policies or credit policies alone
- But we don't know the reason(s) for differing reliance on one or the other
  - US relied more on direct fiscal policy
  - Is that because of budget treatment?

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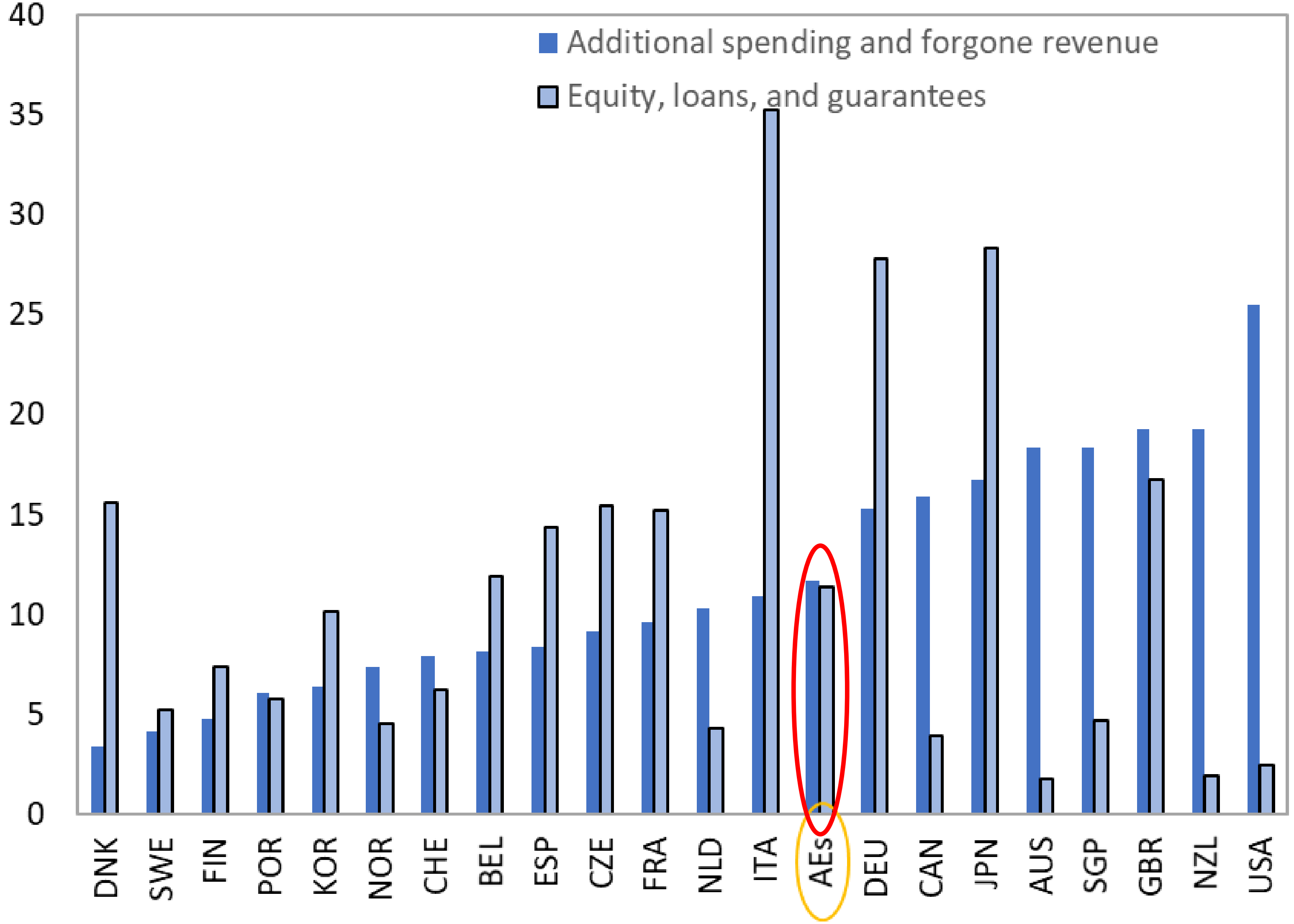
  - It appears (based on IMF data) that emerging economies relied <u>relatively</u> less on credit policies, even while doing less overall

Figure 1. Discretionary Fiscal Response to the COVID-19 Crisis in Selected Economies

(Percent of GDP)



Source: IMF Fiscal Monitor Database (October 2021)

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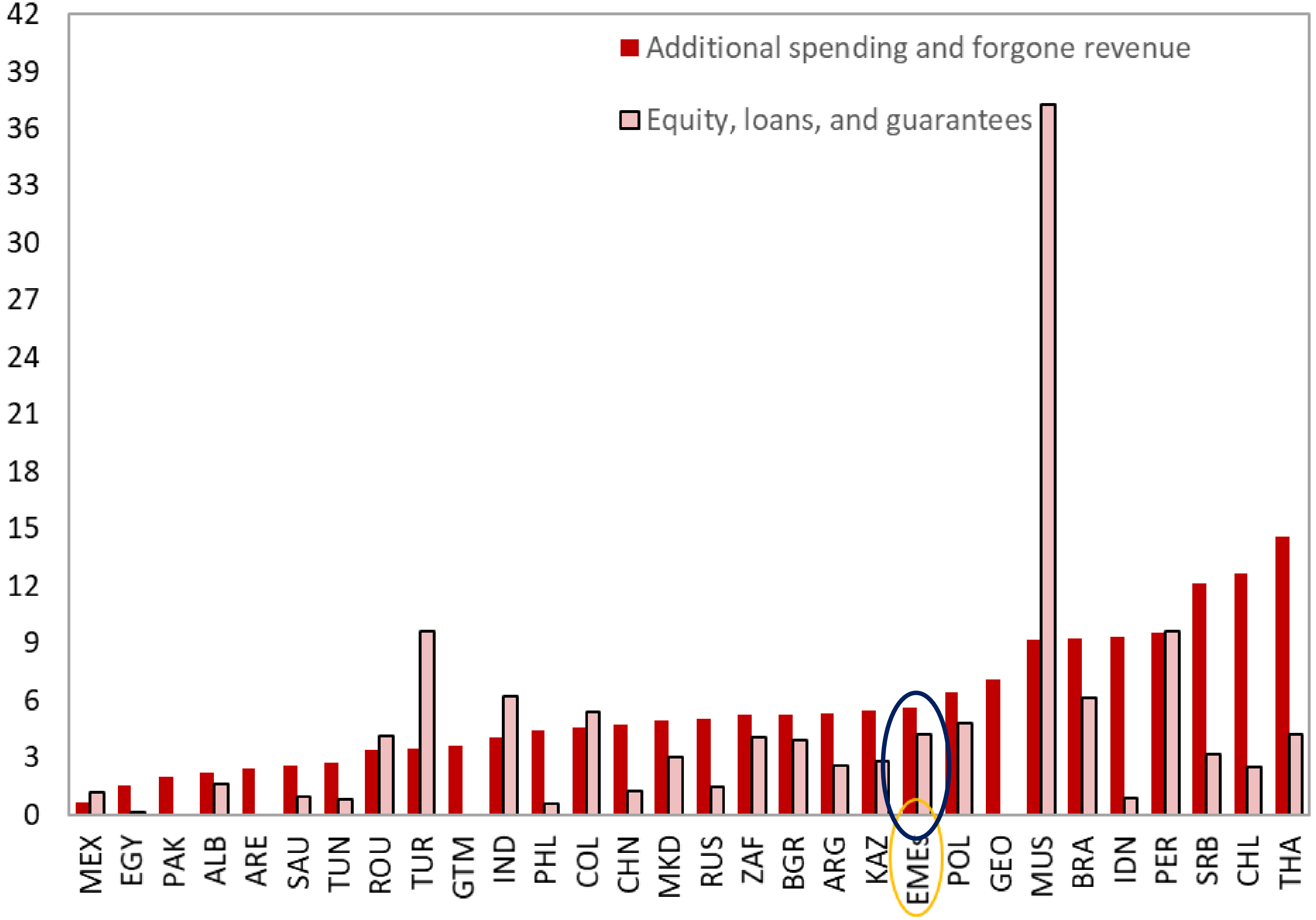

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- But we don't know the reason(s) for differing reliance on one or the other
  - It appears (based on IMF data) that emerging economies relied <u>relatively</u> less on credit policies, even while doing less overall
  - Is that because of weaker financial infrastructure?

What the Paper Finds

- Strong correlation between GDP growth from 2020:4 to 2021:4 and fiscal + credit policy impact size
- Low correlation between GDP growth and just fiscal policy size
- Strong correlation between increases in private saving between 2019 and 2020 and both fiscal and fiscal + credit policy sizes
- No relationship between policy size and CPI inflation 2020:10 to 2021:10

Issues with Interpretation of Results

1. Endogeneity

- Why were fiscal policies adopted?
  - Reverse causality a potential problem
  - Looking at delayed output effect (e.g., starting in 2020:4) might help – correlation with fiscal policy more negative if start in 2020:2 – but there isn't a simple solution without some independent source of policy variation

Issues with Interpretation of Results

2. Small sample

- Correlations between fiscal policy and GDP growth quite different for a larger set of advanced economies
  - For annual 2020-2021 growth, correlation is -.53 for these seven countries, +.06 for 31 advanced countries (including these seven)

Issues with Interpretation of Results

3. Correlation vs. regression

- If wish to measure impact (and why else would we consider correlations), want $\rho \frac{\sigma_Y}{\sigma_X}$, not ρ.
- Coefficient of GDP growth on F+C policy impact = 0.57 (s.e. = 0.33)

Conclusions