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Economic and regulatory support policies and exit strategies

What role for Central Banks in the crisis, from emergency decisions to green recovery?/ Euromed

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Good morning, let me first thank the invitation to participate in such and interesting forum. It is a great pleasure for me to be part of this roundtable in which we will share an overview of the support policies implemented by public authorities to mitigate the consequences of the global pandemic and also the subsequent exit strategies for those measures.

In fact, the pace and degree of intensity in withdrawing the support plans currently in force, are going to play a key role in the recovery of the economic growth and in the potential risks that may impact on financial stability.

Nevertheless, before dealing with this crucial issue, let me recall the set of measures taken and how they have been articulated.

We must acknowledge that the swift and coordinated response by economic authorities in the fiscal, monetary and prudential areas has been key to prevent that the pandemic shock, becomes more persistent, widespread and, potentially systemic, with more negative financial stability consequences.

Fiscal, monetary and prudential measures have played key roles in the crisis response, but I would like to focus my intervention on the measures specifically targeted to support credit.

On the **fiscal side**, authorities sustained firms and households' incomes by injecting liquidity into companies by means of payment deferrals on tax obligations and ensuring basic supplies. In the case of households, by providing for temporary staffing adjustments and, in case that was not possible, by reinforcing unemployment benefits.

The reaction of central banks has also been crucial to keep **monetary policy transmission** channels fully operational and avoiding the fragmentation of financial markets. In the euro area, the implementation of new long-term refinancing operations under very favourable conditions, and the extension of the asset purchase programme, were key to preventing any tightening of economies' financing conditions against a background of strongly increasing public sector financing needs.

At the **micro and macro-prudential level**, a coordinated response took place: enabling the use of capital buffers, limiting profit distributions, allowing for some flexibility in prudential regulation, preventing a mechanistic and pro-cyclical application of accounting standards, while at the same time recognising actual impairment, etc. All these measures have allowed to sustain the supply of financing to the private sector while maintaining banks' solvency position in adequate levels.

Furthermore, **moratorium loan programmes and public loan guarantee schemes** have been approved across countries, enabling households and firms to finance the liquidity needs derived from lockdown restrictions. As an example, in Spain mortgage and consumer loans under moratoria reached around €55 billion. Banking exposures coming from public guarantee loans granted to domestic firms and individual business persons exceed €100 billion, around 19% of total bank exposures to the firm sector

Even though these measures have been tailored by each country to adapt them to the specific needs and main characteristics of the economic agents, the coordination in

implementation has played a crucial role. For instance, at the European level, the guidelines provided by the European Banking Authority ensuring the fulfilment of basic conditions by moratorium programmes have allowed banks across the union to benefit from a favourable prudential treatment of the loans included in those programmes.

Having said that, as the progressive improvement in health conditions continues (success of vaccination policies), and economic activity picks up, there is a need for the above measures to be reviewed and gradually adapted to the current situation. Whereas they should be maintained long enough to sustain recovery, amendment and progressive withdrawal is required to avoid the current dependence on public intervention.

This dependence might distort resource allocation, postpone necessary structural adjustment, drain fiscal resources and, in the end, increase public debt, depressing investment and growth.

At the European Banking Authority level, the application for new loan moratoria with prudential benefits has already expired. A significant proportion of loan moratoria in European countries have expired in 2021 so far (in Spain 91%). The state guarantees on loans will have a more medium-term effect at least in some cases, as relatively long maturities and program sizes contribute to cover also financing needs in the recovery phase. The weight of state guaranteed loans over total bank lending to firms will decline gradually as new regular production of bank loans accumulate over time.

This gradual withdrawal should be combined with targeted measures if financial stability risks materialize in the recovery phase. A gradual shift form general to targeted measures, in particular, granted to SMEs or to hardest-hit sectors can be the options in this adaptation process. Support measures can also be tailored to discriminate between viable and non-viable borrowers.