



ESRB

European Systemic Risk Board

European System of Financial Supervision

Financial stability implications of COVID-19 support measures

**SUERF E-workshop in
cooperation with KfW:**

**COVID-19 and government firm
rescue measures: best practices,
current challenges, and the way
forward post-corona**



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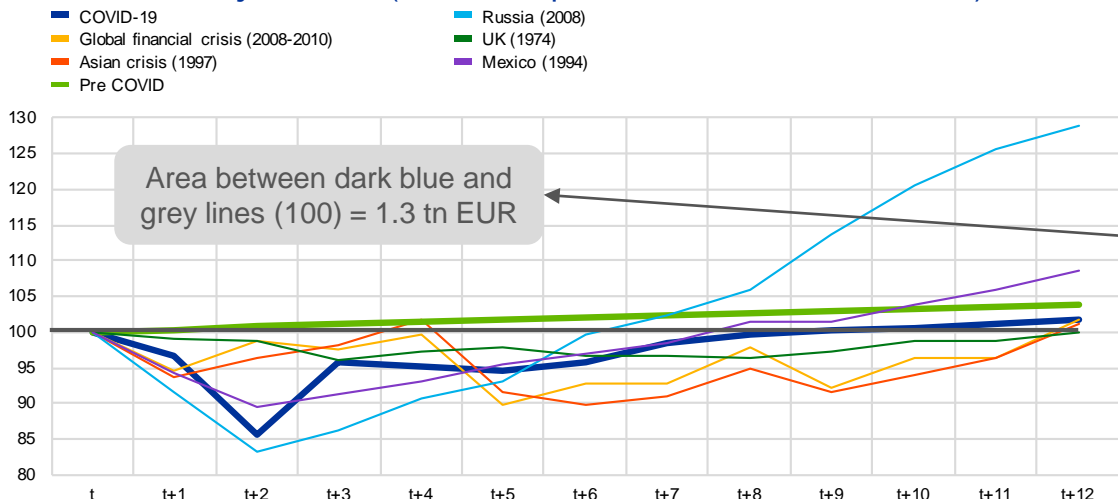
Key findings

- 1. To support the real economy during the COVID-19 pandemic, governments have provided swift and unprecedented support packages.**
 - This has provided crucial relief to households and non-financial corporations.
 - The financial system has continued to provide funding to the real economy, and loan losses have remained limited.
 - At the current juncture, credit markets are strongly supported by fiscal policy.
- 2. The longer the crisis lasts and the weaker the economic recovery will be, losses to the non-financial sector could spill over to financial sector balance sheets.**
 - Deleveraging of banks might lead to adverse feedback loops.
 - Cross-border banking activities might be particularly affected by deleveraging.
 - There are trade-offs between supporting the economy and maintaining support for too long.

The COVID-19 crisis has brought about a significant economic shock

- In comparison to previous crises, the expected cumulative output loss caused by the COVID-19 pandemic is significant (loss of around 10% of EU GDP).
- Faster recovery than during GFC and Asian crisis expected. The Q4 2019 level is expected to be reached by Spring 2022.

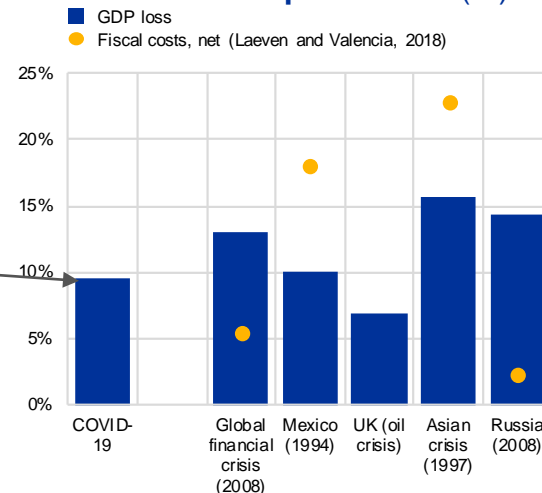
Quarterly output loss of the COVID-19 pandemic and comparison with other major crises (index, last period before recession = 100)



Source: Eurostat, European Commission, Haver Analytics and ESRB Secretariat calculations.

Notes: the blue line represents q-o-q real GDP growth in the EU until Q4-2020 (t+4) and then the Winter Economic Forecast by the European Commission. Pre-COVID represents the estimated real GDP growth path in December 2019, according to the projections by the European Commission (growth for the last four quarters is forecasted to be constant at 0.3%). Global financial crisis refers to the EU real GDP growth path. The Asian crisis is computed as the average of Indonesia, Japan, South Korea, Malaysia, Philippines and Thailand. Real GDP growth for other crisis and countries is calculated in national currencies to avoid distortions by exchange rates.

Estimation of GDP losses for the COVID-19 and other past crises (%)



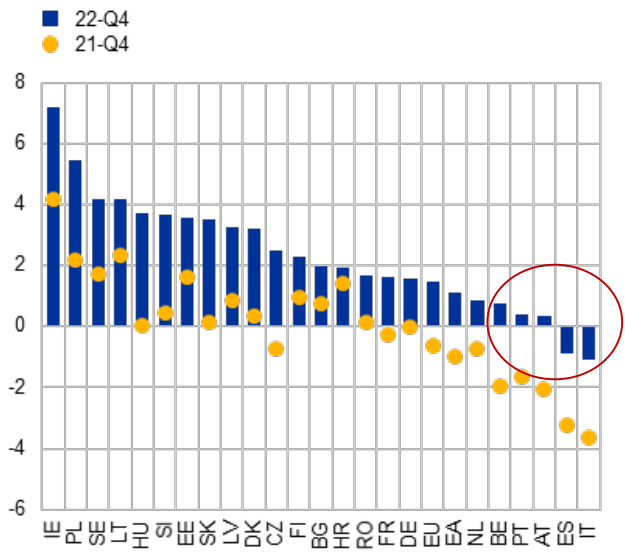
Source: Eurostat, European Commission, Haver Analytics, ESRB, Laeven and Valencia (2018) and ESRB Secretariat calculations.

Note: GDP loss computed as the accumulated sum of the differences between quarterly GDP in the 12 quarters of a crisis and GDP of the quarter immediately before the crisis, as a percentage of four-periods accumulated GDP at the onset of the crisis. Net fiscal costs, as reported by Laeven and Valencia (2018) are expected to be an approximation to the support received by the economy. The Asian crisis is computed as the average of Indonesia, Japan, South Korea, Malaysia, Philippines and Thailand. No data on fiscal costs is available for the UK economy during the oil crisis and the EU during the global financial crisis is the average of the net fiscal costs incurred by EU countries (excluding UK).

Recovery prospects vary significantly across EU Member States

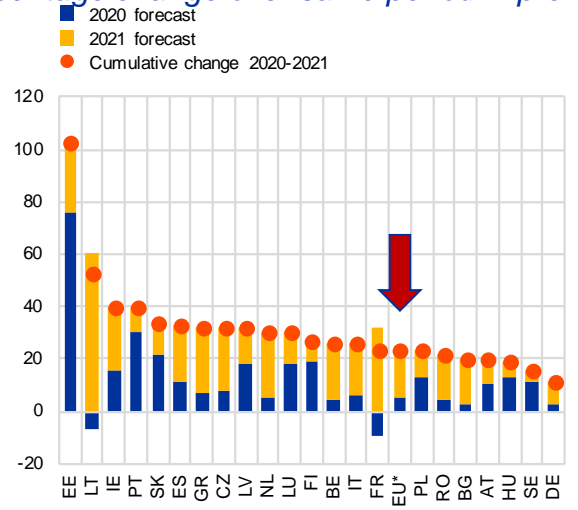
- Italy and Spain are forecast to reach the pre-crisis real GDP level only in 2023.
- The heterogeneity of growth prospects is also reflected in the expected growth in the number of insolvencies, albeit the relationship is weaker or even non-existent in some countries.

GDP forecasts for a selection of global economies
(Index: 2019 Q4 = 0)



Source: EC Winter 2021 forecast and ESRB Secretariat calculations.
Notes: No GDP quarterly forecasts are reported for CY, EL, MT and LU.

Insolvency forecasts for 2020 and 2021
(Percentage change over same period in previous year)

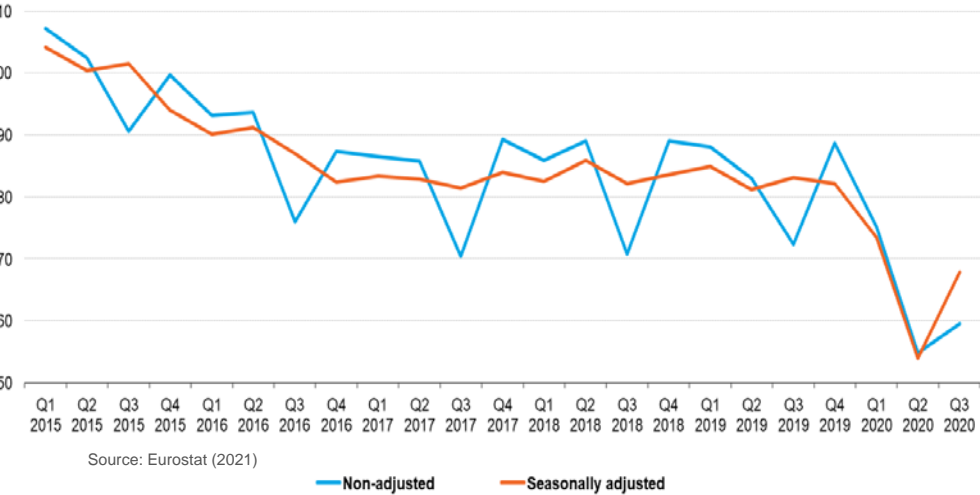


Source: Euler Hermes and Allianz Research. Notes: Forecast for DE, FR, ES, IT and NL based on a revised version of the Euler Hermes and Allianz Research report dated 24 September, other countries based on previous report dated 16 July. EU* refers to GDP-weighted sample of countries shown in the chart.

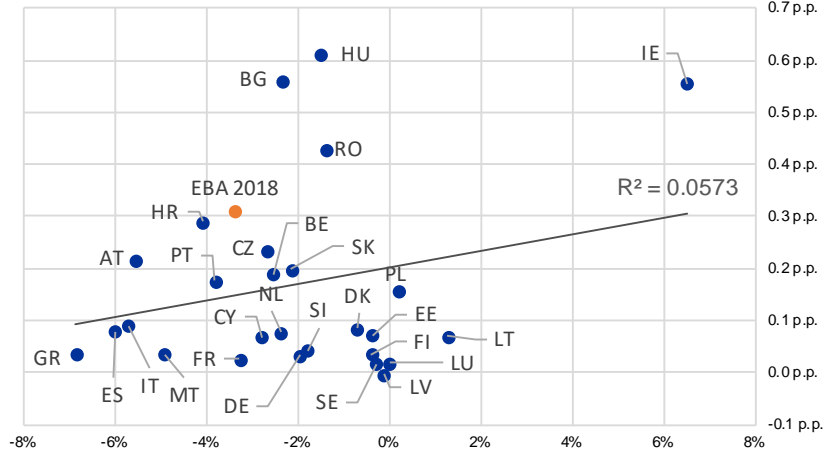
Policy support has so far prevented mass corporate insolvencies

- Bankruptcies in the EU have so far decreased compared to the seasonally adjusted level.
- Banks' provisions for IFRS stage 2 loans are highly heterogeneous across countries and – contrary to expectations – not strongly driven by the country-specific size of the COVID-19 shock.

Declarations of bankruptcies in the EU, 2015-2020



Forecast GDP growth 2020-21 (x-axis, %) and change of provisions for stage 2 loans (y-axis, percentage points)



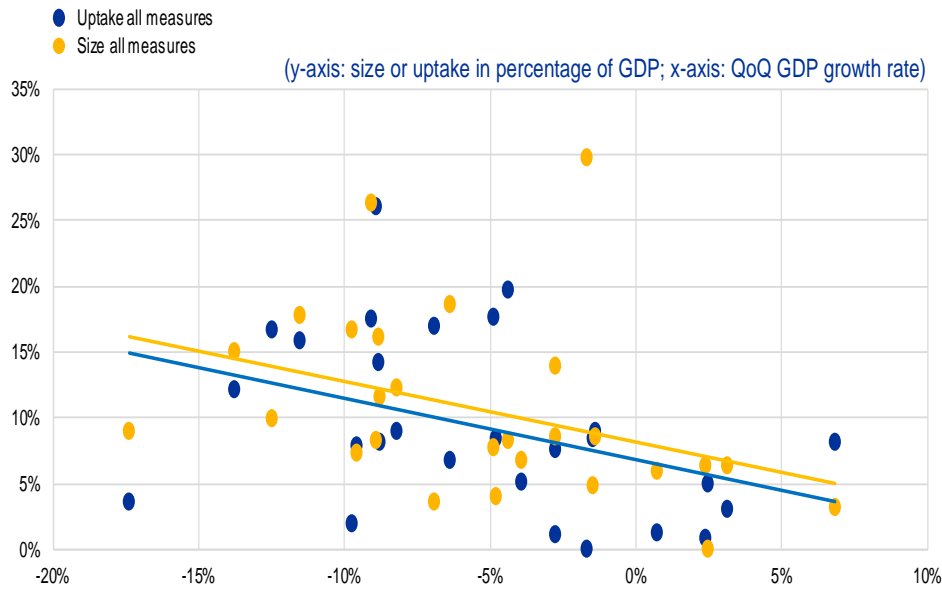
Source: EBA Risk Dashboard, EC Winter Forecast and ESRB Secretariat calculations.
 Notes: Dots represent the change in provisions for stage 2 loans (share of stage 2 loans multiplied by coverage) as reported in the EBA Risk Dashboard, between Q4 2019 and Q3 2020. EBA 2018 refers to the adverse stress test scenario. Cumulative GDP growth in 2020 and 2021 in the 2021 EC Winter Forecast.

Fiscal support has been broad and swift, with differences in types of programs and uptake across country

- Liquidity measures such as moratoria and public guarantees until September 2020 were more important than solvency measures.
- Despite significant heterogeneity, countries hit harder have bigger programs and larger uptake

	Total uptake (bn EUR)	Total size announced (bn EUR)	Total uptake (% GDP 2019)	Total size announced (% GDP 2019)
Moratoria	838		5.0%	
Public guarantees	435	1,580	2.6%	9.5%
Public loans	66	57	0.4%	0.3%
Direct grants	112	327	0.7%	2.0%
Tax deferrals	77	170	0.5%	1.0%
Tax reliefs	13	75	0.1%	0.4%
Public support for credit insurance	n.a.	227	n.a.	1.4%
Total	1,541		9.2%	
Total w/o moratoria	704	2,436	4.2%	14.6%

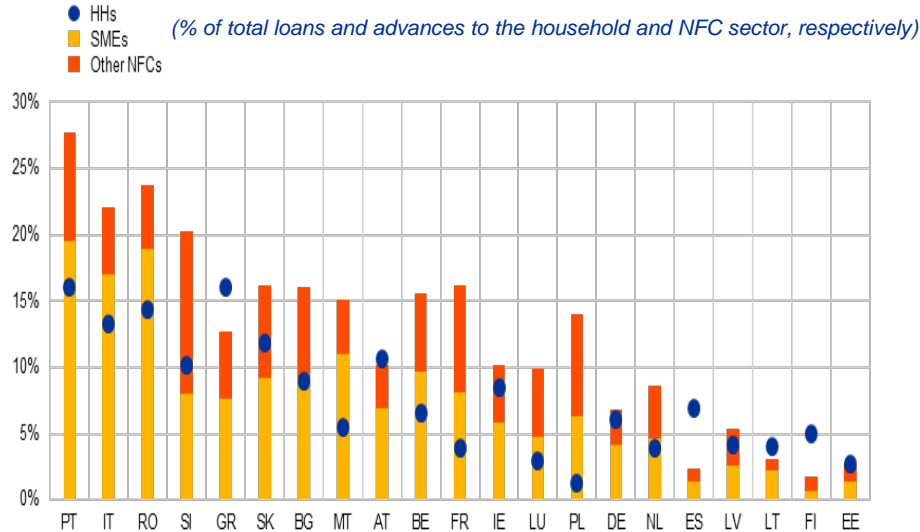
Source: Recommendation ESRB/2020/08 (refer. date 30 Sep 2020), ECB (MNA, BSI, CBD).
 Note: Total size announced refers to field 1.1.01, and Total Uptake to field 2.2.10 for all measure apart from tax reliefs and tax deferrals, where field 2.2.12 was used. Reporting data gaps exist – results should be interpreted with caution.



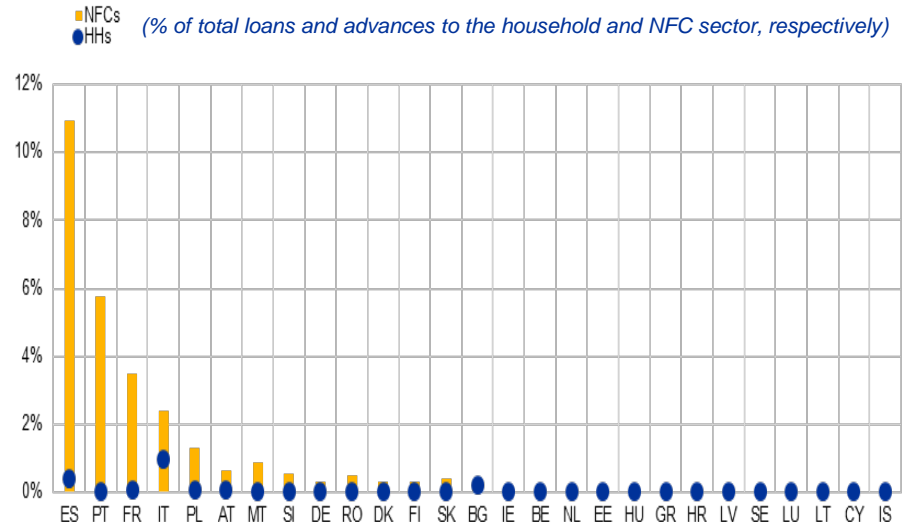
Source: Recommendation ESRB/2020/08 by 31 October 2020 (reference date 30 Sep 2020), ECB (MNA)
 Note: Announced size (field 1.1.01) and uptake (field 2.2.10) for all measures combined as a share of 2019 GDP on the y-axis. Quarter-on-quarter GDP growth from Q1 2020 to Q2 2020 on the x-axis. Based on 28 countries (IS, LI and NO are excluded).

While moratoria serve both NFCs and households, public guarantees are mostly extended to NFCs.

- The share of loans under moratoria to total loans for most countries is higher for NFCs than for HHs and strong for SMEs.
- Public guarantees had an uneven impact across European countries and banks. Most of the support is extended to NFCs.



Source: EBA, ESRB calculations (reference date June 2020).
 Note: Countries are sorted according to the share of loans under moratoria in total loans and advances to households and NFCs. The values correspond to the mean value for banks in the given country. Values for CY – 45% for HHs, 53% for SMEs and 17% for Other NFCs are not shown for presentational reasons.

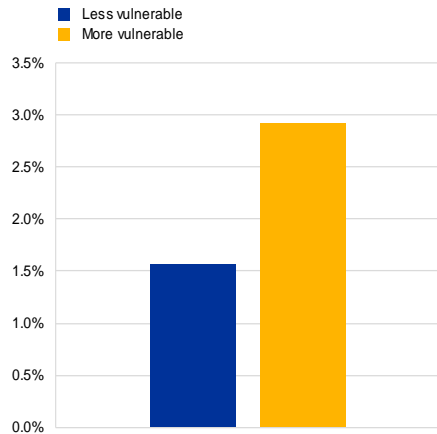


Source: EBA, ESRB calculations (reference date June 2020).
 Note: Countries are sorted according to the share of loans under moratoria in total loans and advances to households and NFCs. The values correspond to the mean value for banks in the given country. CY – 45% for HHs, 53% for SMEs and 17% for Other NFCs – left out for presentational reasons.

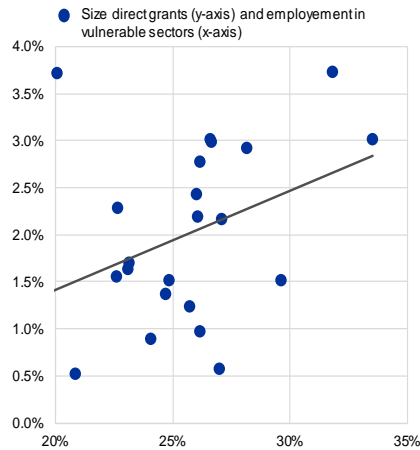
More vulnerable sectors and countries have benefitted from the support measures, but face a higher risk of an early withdrawal of support

- Countries with high employment in vulnerable sectors rely more on direct grants.
- The uptake of moratoria is positively correlated with pre-crisis debt levels.

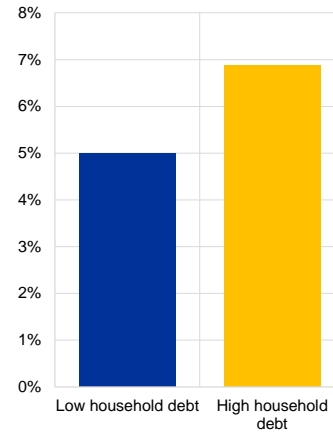
(Direct grants)



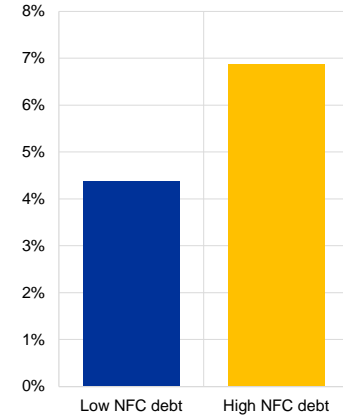
(Direct grants)



(Moratoria)



(Moratoria)



Source: Recommendation ESRB/2020/08 by 31 October 2020 (reference date 30 Sep 2020), ECB (MNA)
 Note: Announced size (field 1.1.01) as a share of 2019 GDP on the y-axis for the three graphs. Vulnerability is defined as the share of employment in the NACE sectors G, H, I, R, T, U in Q4 2019. The bar plots depict the median over the lowest (highest) quartile of the vulnerability metric as "less vulnerable" ("more vulnerable"). The scatterplot compares the announced size of direct grants (as a share of 2019 GDP; y-axis) to the vulnerability metric (a higher share means higher vulnerability; x-axis). All graphs based on 28 countries (IS, LI and NO are excluded).

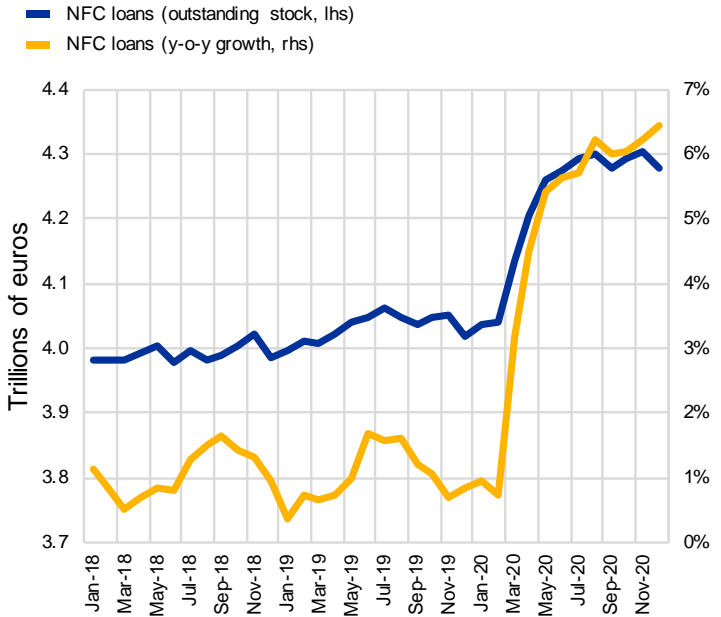
Source: Recommendation ESRB/2020/08 by 31 October 2020 (reference date 30 Sep 2020), ECB (MNA)
 Note: Uptake (field 2.2.20) of moratoria, public guarantees and loans as a share of 2019 GDP on the y-axis. Median over countries in the lowest (highest) quartile of household ("HH") or NFC debt over GDP in Q4 2019 as "low debt" ("high debt") on the x-axis. All graphs based on 28 countries (IS, LI and NO are excluded).

Following the surge in Q2, lending to the private sector decelerated in H2 2020

- The outstanding stock of NFC loans has been broadly stable in H2.
- Mortgage lending to HH continued to gradually accelerate in the course of 2020, while consumer lending collapsed – in line with the propensity to increase precautionary savings.

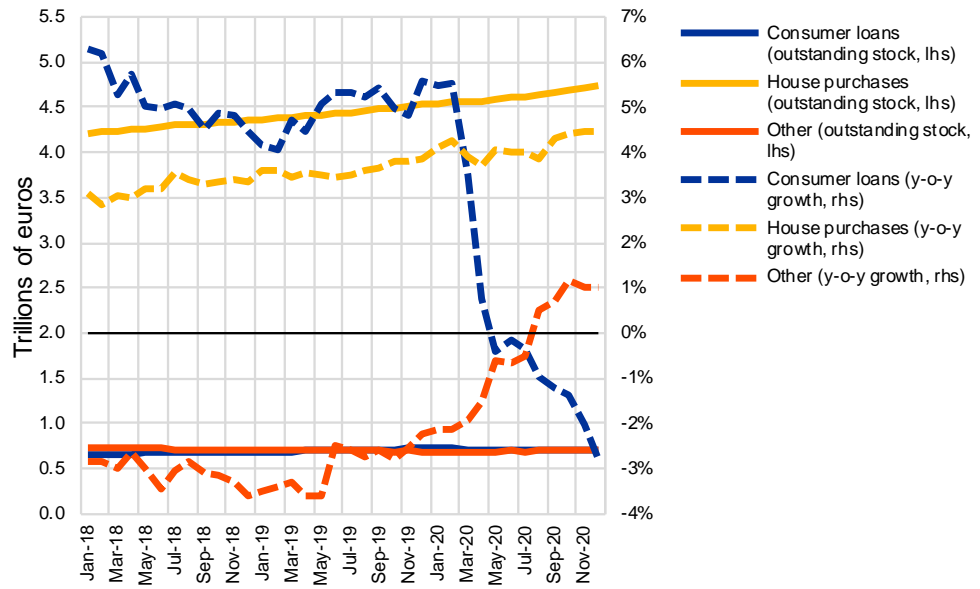
Outstanding loans to NFCs

(growth rate and stock)



Outstanding loans households

(growth rate and stock)



Source: ECB Balance Sheet Items and ESRB Secretariat calculations.
Notes: Euro area aggregates.

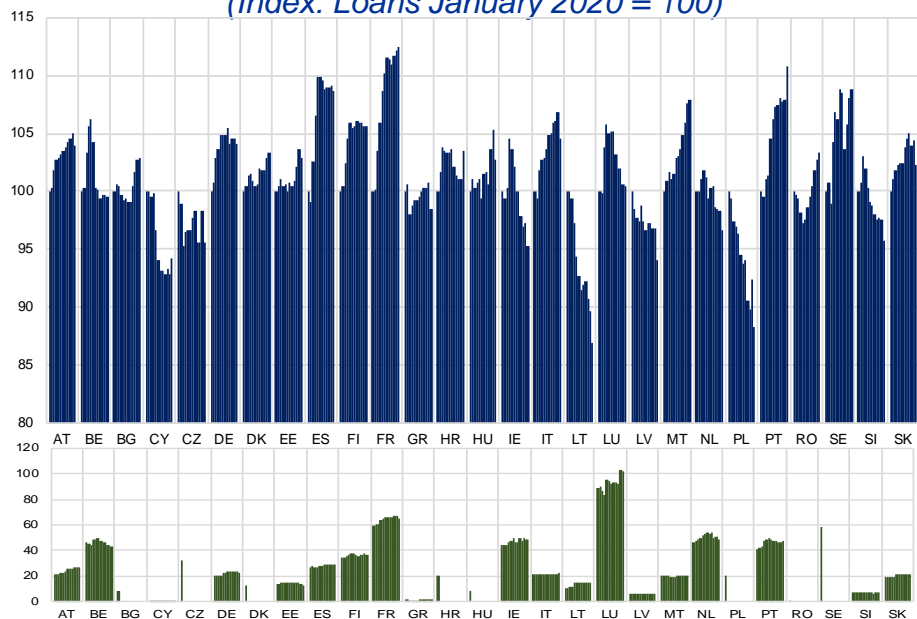
Source: ECB Balance Sheet Items and ESRB Secretariat calculations.
Notes: Euro area aggregates.

Bank lending in 2020 characterised by large cross-country heterogeneity

- In few countries (CY, CZ, GR, IE, LT, PL, SI) lending to NFCs and households decelerated in the course of 2020, while others reported large increases in lending to NFCs (ES, FR, PT, SE) or to households (BE, BG, LU, SE).

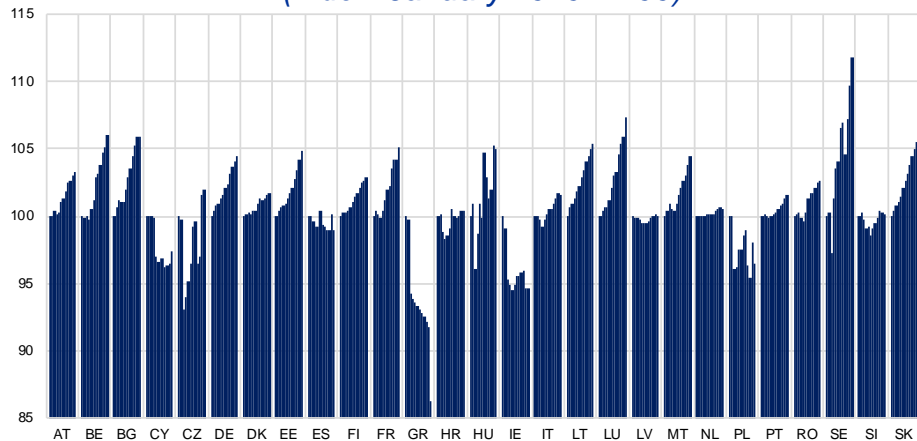
Outstanding amounts of loans (blue bars) and of debt securities issued (green bars) in the domestic economy, non-financial corporations, Jan 2020- Dec 2020

(Index: Loans January 2020 = 100)



Outstanding amounts of loans to households in the domestic economy, Jan 2020 - Dec 2020

(Index: January 2020 = 100)



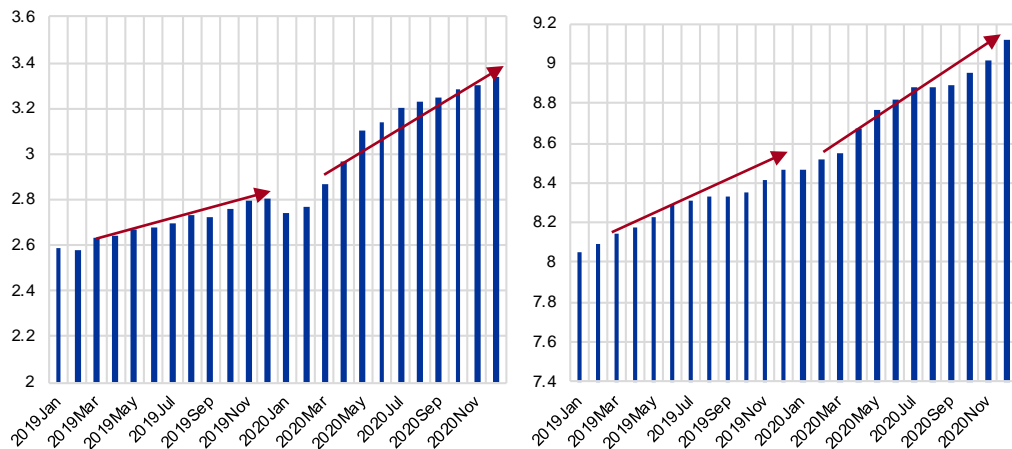
Source: ECB Balance Sheet Items, ECB Securities Statistics and ESRB Secretariat calculations.

Notes: the blue bars show the outstanding amount, at the end of each month in 2020, of loans to non-financial corporations and to households, indexed to January 2020 = 100. The green bars show the outstanding amounts of debt securities issued by non-financial corporations, between January and December 2020, indexed to loans to non-financial corporations in January 2020 = 100. For debt securities, data is available on a monthly basis only for euro area countries.

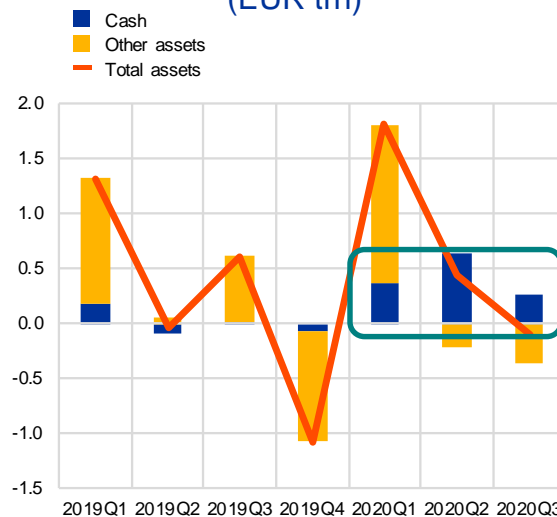
Economic agents increased their holdings of liquid assets

- Deposits of NFCs and households significantly increased since the onset of the pandemic (despite the low level of interest rates).
- Euro area banks increased their cash holdings by more than EUR 1tn to build a buffer in the face of heightened uncertainty.

Outstanding amounts of deposits by non-financial corporations (left-hand side) and by households (right-hand side) on domestic banks (EUR trn)



Changes in cash and other assets (EUR trn)



Source: ECB Balance Sheet Items and ESRB Secretariat calculations.

Notes: outstanding amount of deposits of households and non-financial corporations, for the EU 27 for the period January 2018 to December 2020.

Source: SSM supervisory data and ESRB Secretariat calculations.

Notes: based on supervisory information published by the SSM on the banks under its direct supervision.

Policy priorities for addressing risks in the NFC sectors

- Continue public support measures until the economic recovery is firmly entrenched on the back of the rollout of vaccinations.
- Gradually move to more targeted support measures to avoid supporting (i) companies that can operate without public support; and (ii) unviable companies.
- Increasingly complement liquidity support with equity support for viable, but already highly indebted companies (potentially in the form of quasi-equity injections, subsidies and the restructuring of debt to banks and other creditors).
- Address deficiencies in bankruptcy frameworks; implement preventive restructuring; strengthen capacity/efficiency of the judiciary to be able to handle a surge in bankruptcies.

Thank you for your attention

For more information at the ESRB website:

<https://www.esrb.europa.eu/home/search/coronavirus/html/index.en.html>

Database of public support measures

A new publication

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implications of support
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real economy from the
COVID-19 pandemic
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