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# Economic Policy Responses to the Covid-19 crisis in the Euro Area

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At German Institute for Japanese Studies (DIJ) & German Centre for  
Research and Innovation (DWIH) Tokyo

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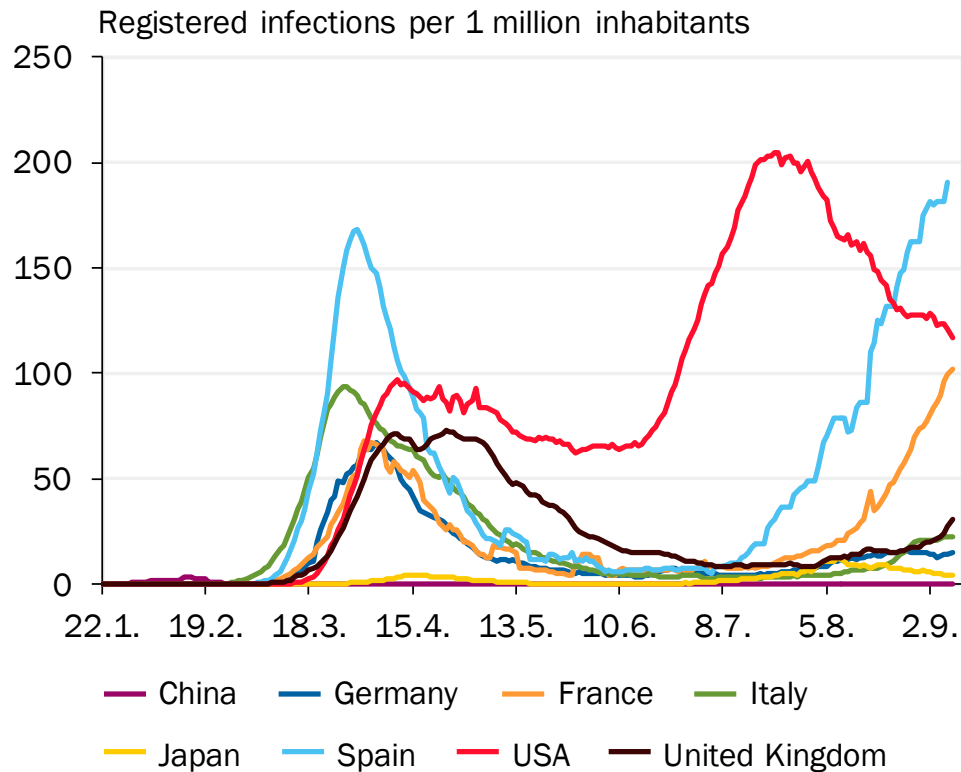
# Contents

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- I. Economic outlook: Clear signs of recovery
- II. Fiscal policy: Bridging support, stimulus package, EU support programmes
- III. Monetary policy: Liquidity, asset purchases, judicial conflict

# Spread of coronavirus: Europe and US

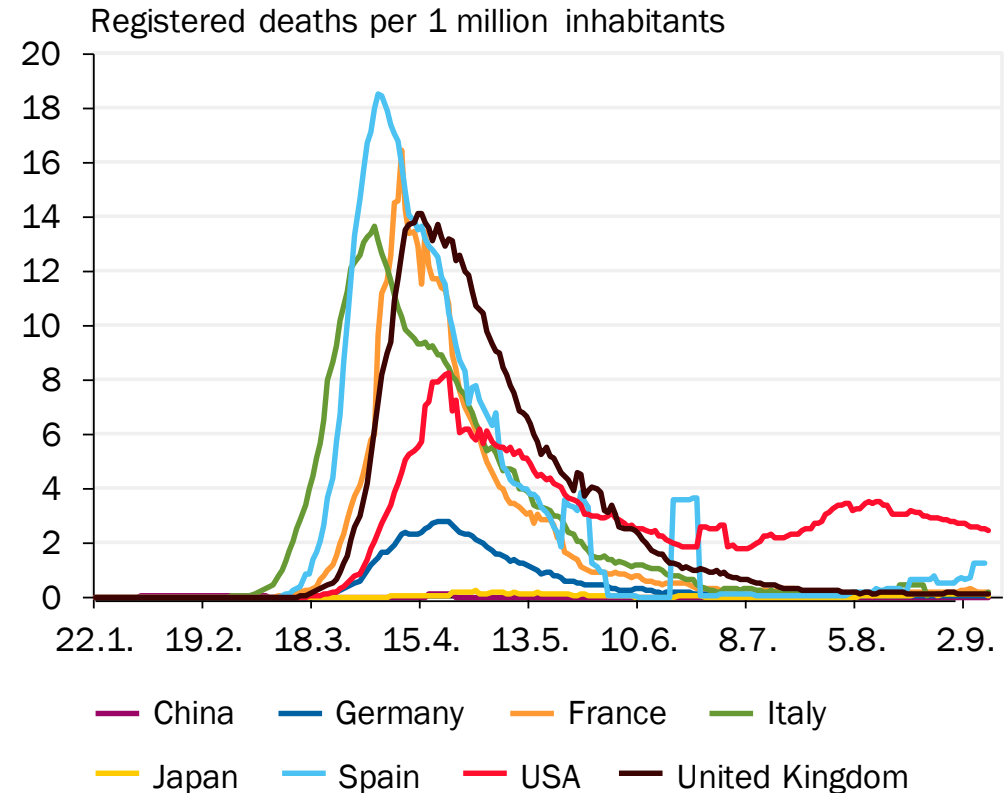
## Developments of registered new infections



Sources: European Centre for Disease Prevention and Control, own calculations

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## Developments of registered cases of death

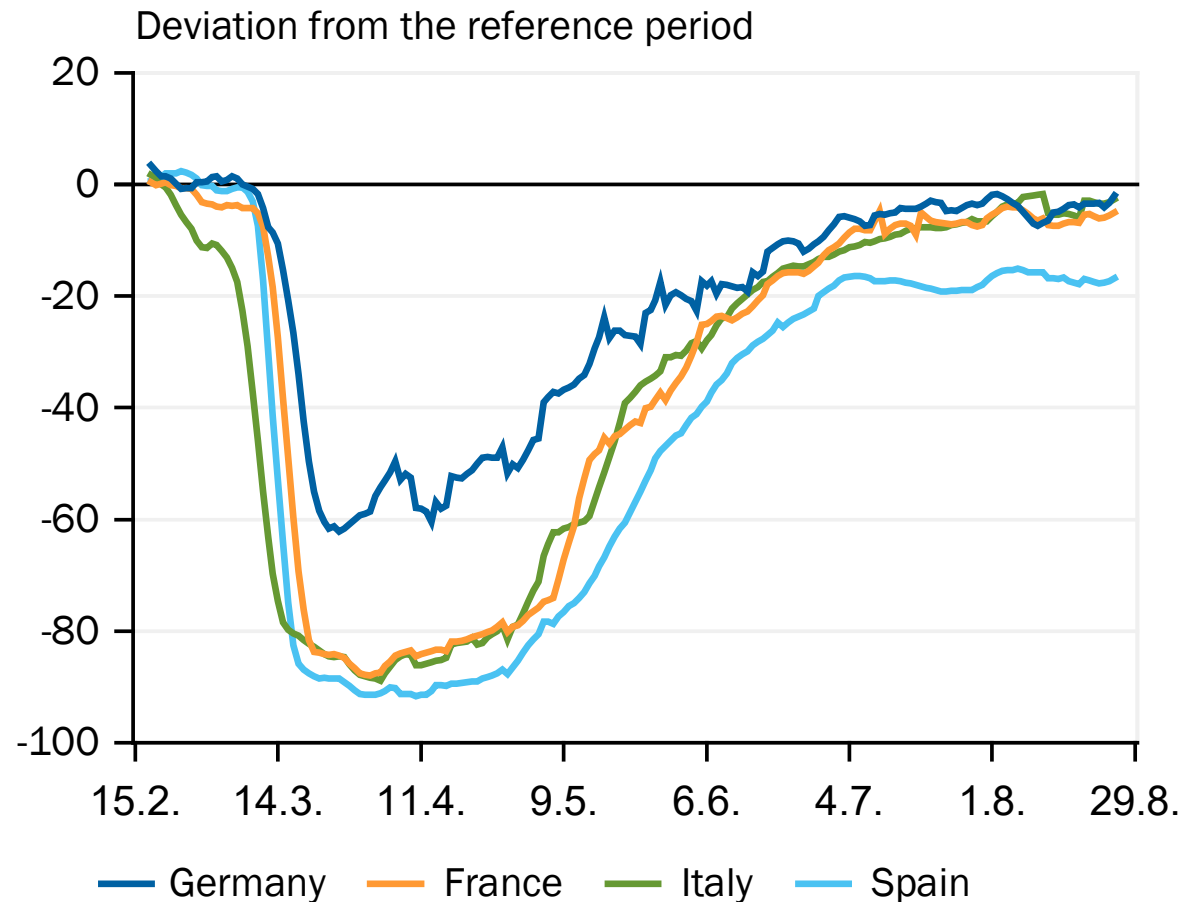


Sources: European Centre for Disease Prevention and Control, own calculations

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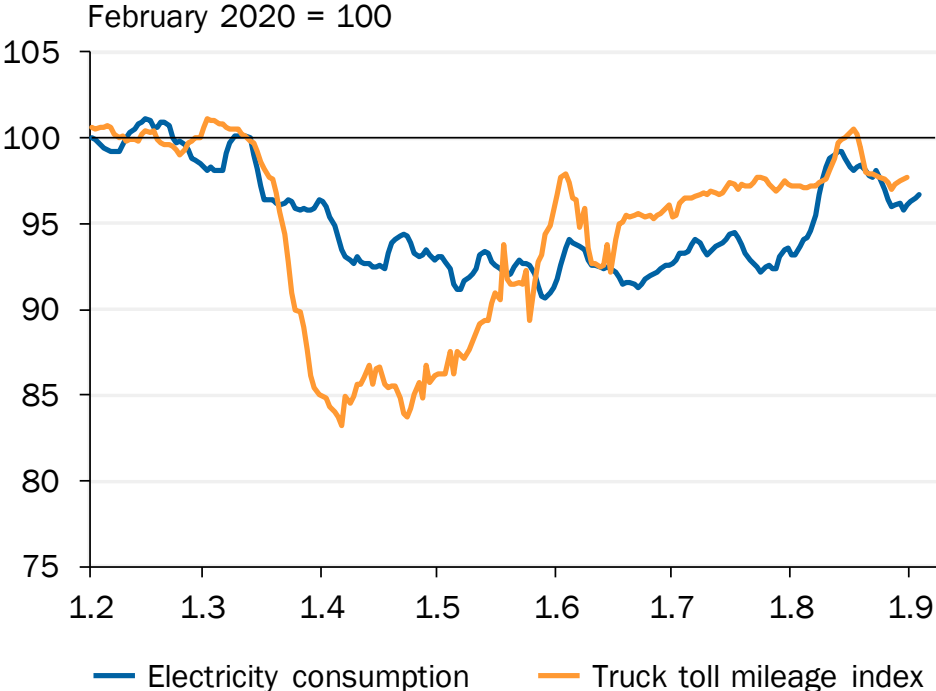
# Real time mobility indicators

## Movement of passers-by in retail trade and leisure



# Germany: clear signs of recovery

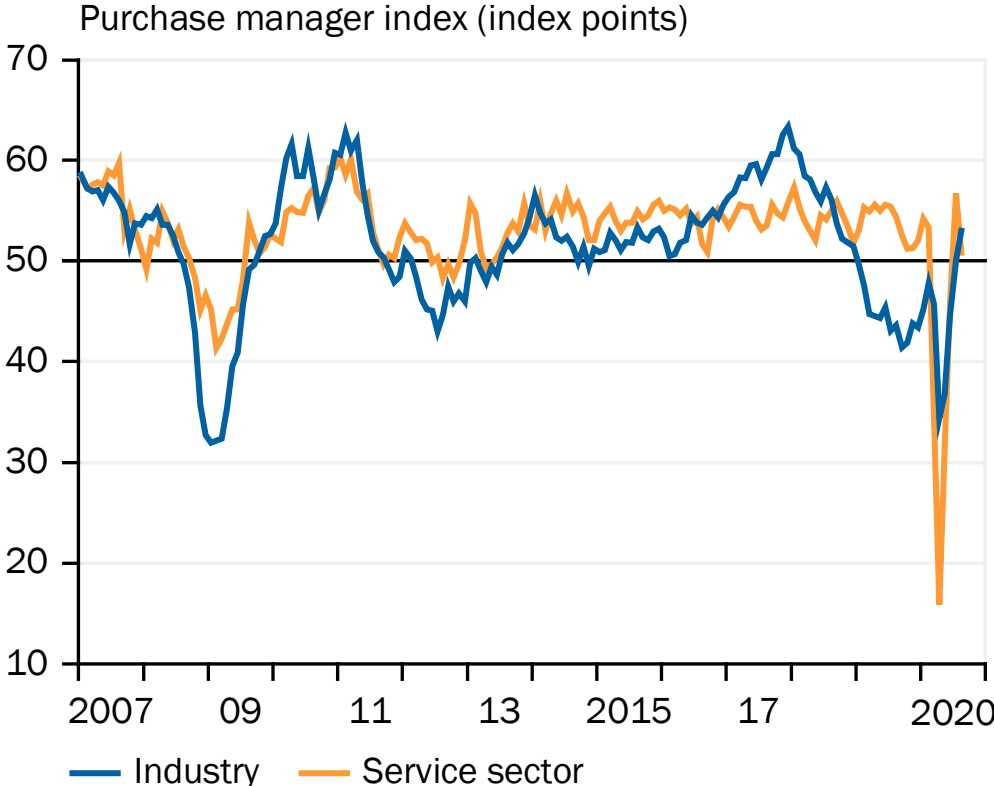
**Electricity and toll data indicate a slow normalisation**



Sources: Deutsche Bundesbank, ENTSO-E, Federal Office for Freight Transport, Federal Statistical Office, own calculations

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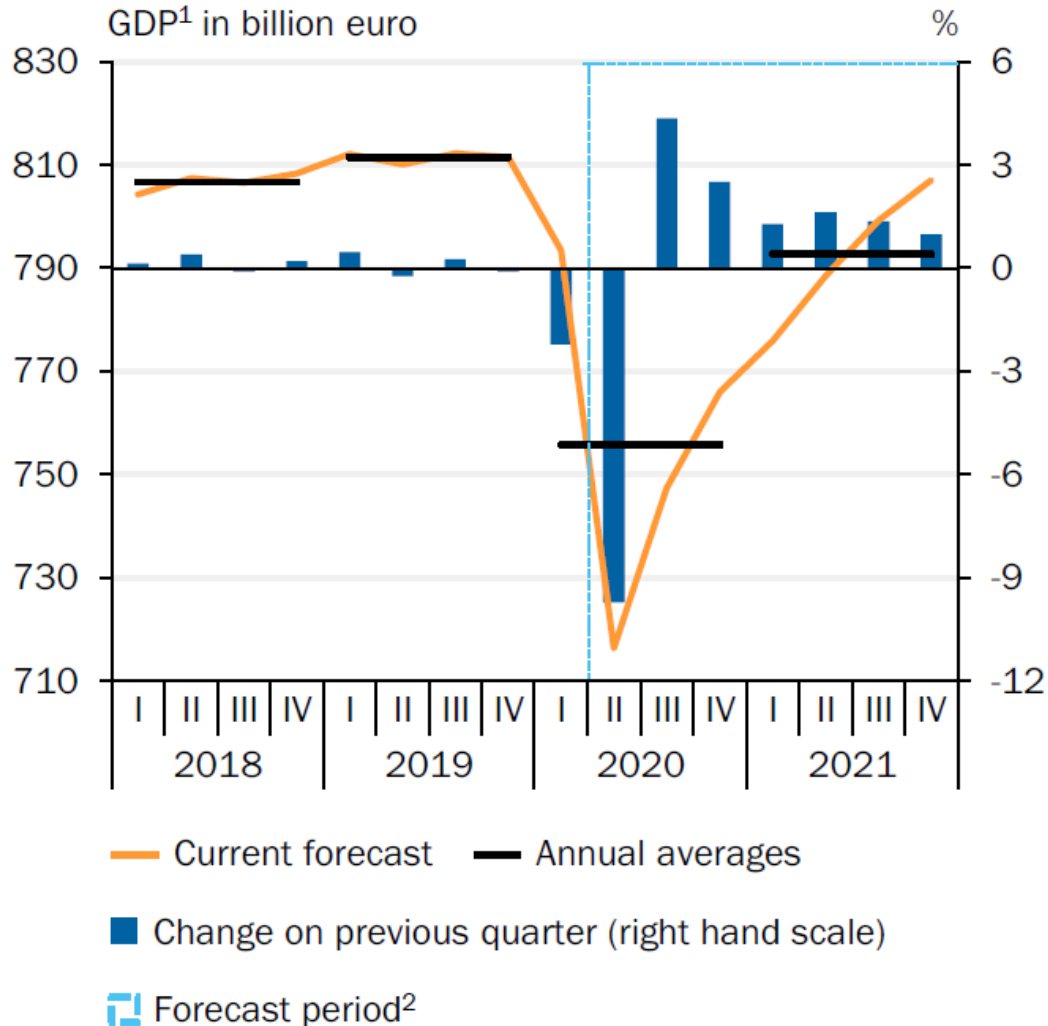
**Sentiment indicators strongly recovered since May**



Source: IHS Markit

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# GCEE Forecast for Germany from June 24, 2020



- GDP growth -6,5 % in 2020 and +4,9 % in 2021
- Development in 2020 in two parts:
  - Up to -10% in first half-year
  - Recovery depends on extent of continuing restrictions, uncertainty, income cuts.
- Deficit 2020/21 : -6% / -3,9%
- Debt-GDP ratio  
2019/20/21: 59,8% / 75,2% / 73,3%

# GCEE GDP growth forecasts: June 24, 2020

## Growth of gross domestic product<sup>1</sup> of selected countries

	USA	China	Japan	United Kingdom	Euro area				
					Total	including:			
						Germany <sup>2</sup>	France	Italy	Spain
2019	2.3	6.1	0.7	1.4	1.3	0.6	1.5	0.3	2.0
2020 <sup>3</sup>	- 6.1	0.3	- 4.4	- 8.8	- 8.5	- 6.9	-11.0	-11.8	-11.5
2021 <sup>3</sup>	4.7	8.8	2.9	4.8	6.2	4.9	8.4	7.0	8.1

1 - Change on previous year in %. Price-adjusted. 2 - Due to the adjustment for calendar effects, the value for GDP growth in Germany in 2020 stated here differs from the unadjusted values stated elsewhere (see Table 4). 3 - Forecast by GCEE. Values are based on seasonal and calendar-adjusted quarterly figures.

Sources: Eurostat, national statistical offices, own calculations

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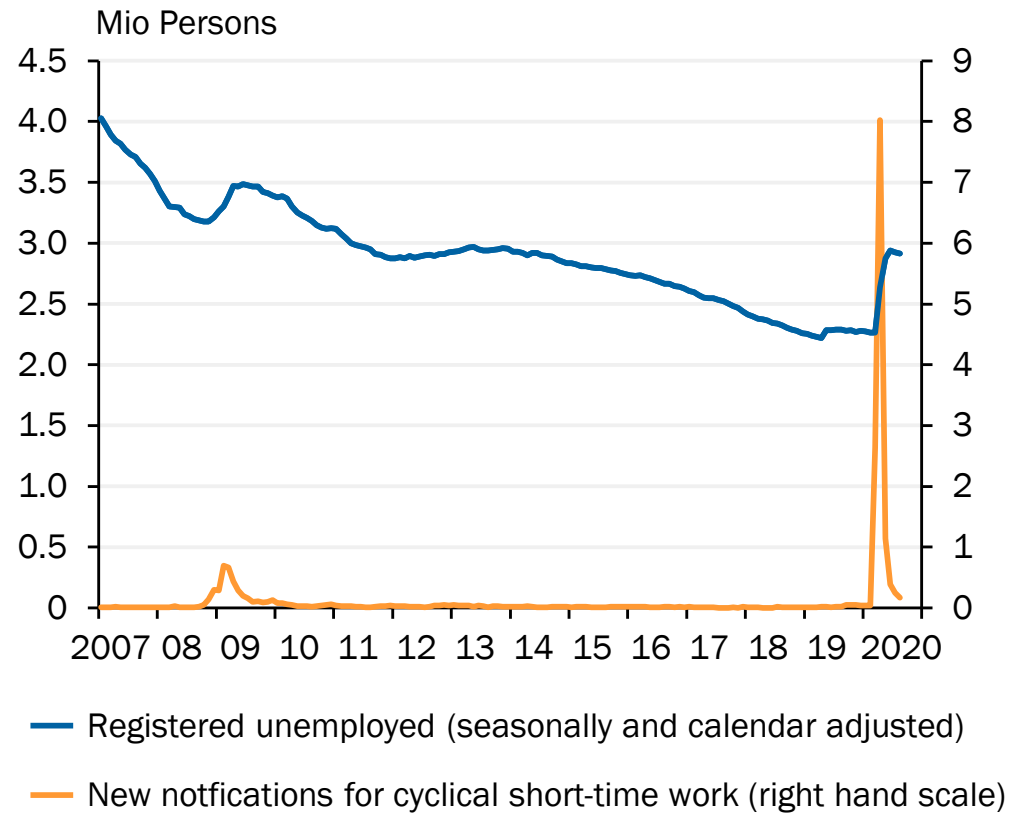
## II. Fiscal policy: Bridging support, stimulus package, EU rescue and support programs

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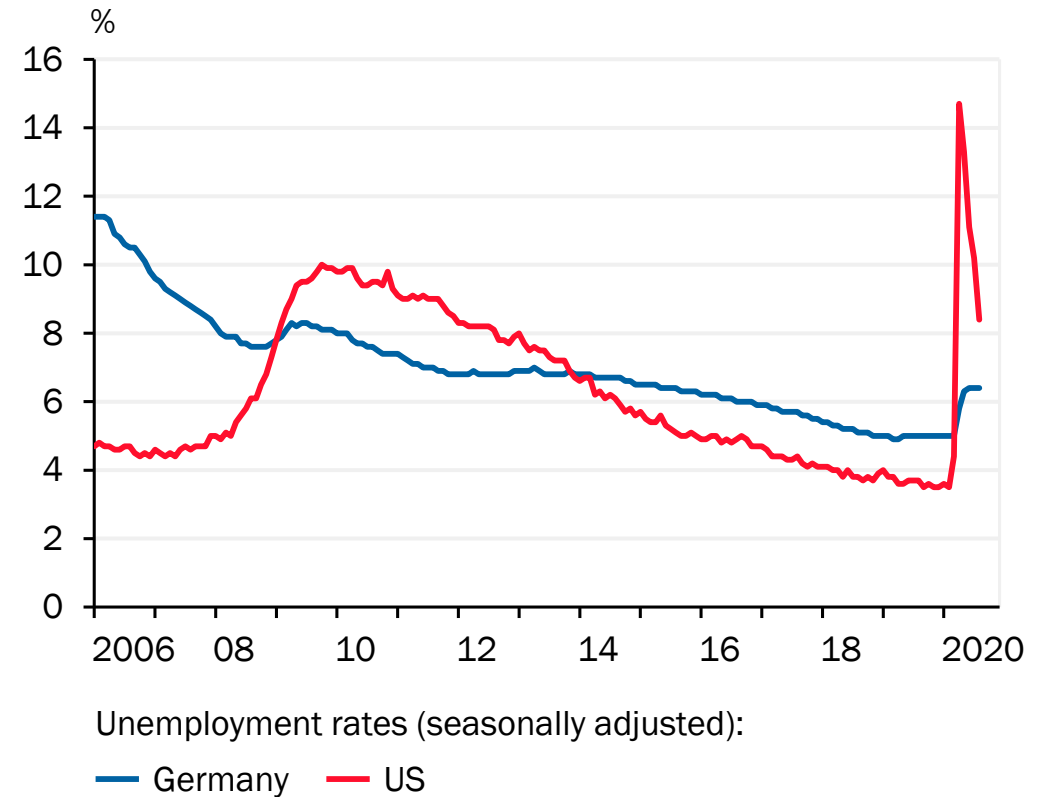
# Automatic stabilizers: Short-time work schemes versus unemployment support (Germany vs US)

## Unemployment and notified short-time work



Source: Federal Employment Agency

## Labor market performance very different in US and Germany

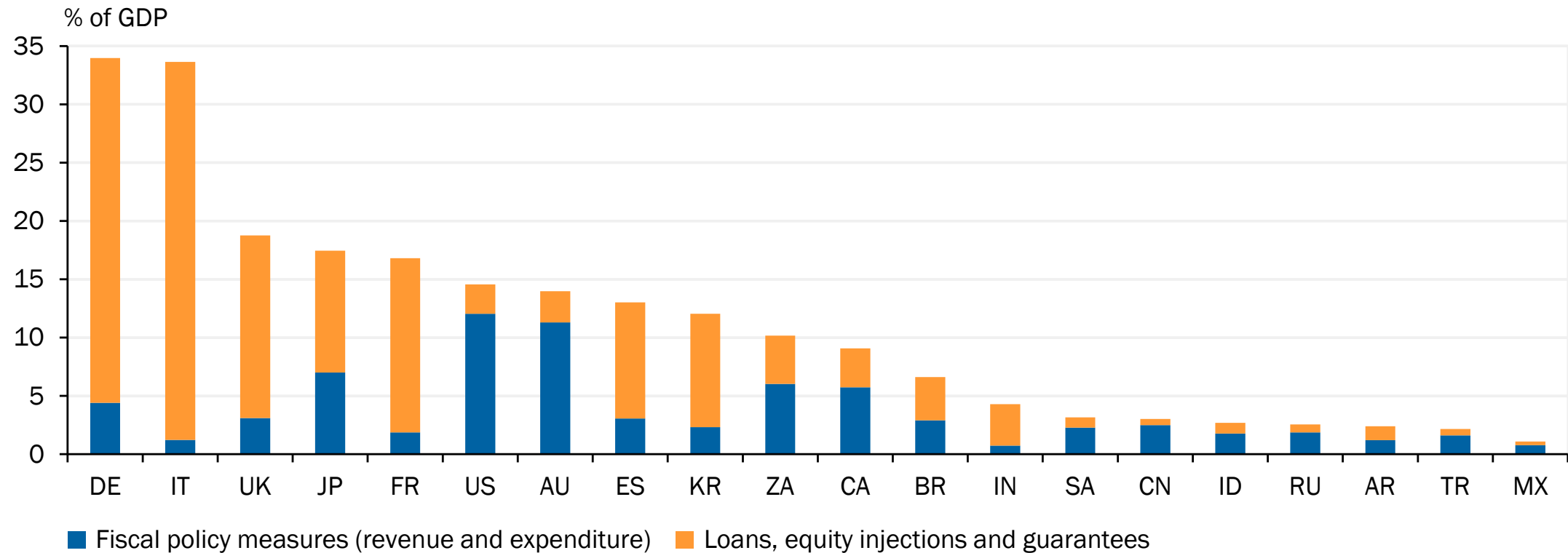


Sources: Federal Employment Agency, US Bureau of Labor Statistics

# Fiscal support measures: comparison by share of GDP

## Fiscal measures in G20 countries in response to Corona pandemic in 2020

Measures announced as of May 13, 2020



Source: IMF

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# Germany: Phase 2 Fiscal stimulus package 2020, 130 bln€, 3,8% of GDP 2019

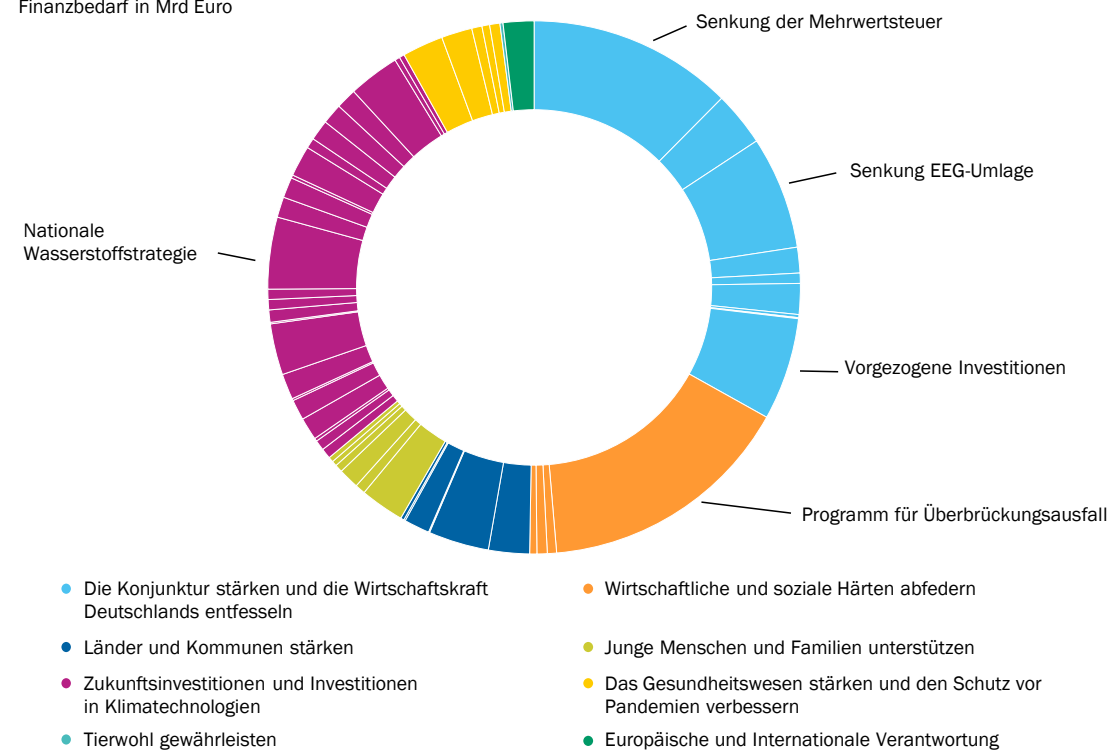
Many different types of measures

- Temporary VAT reduction, 3%
- Reduction of electricity surcharges
- Additional bridging support for companies
- Various public investment (renewable energy, climate change)
- Some transfers for low-income households with children

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Finanzbedarf der Bestandteile des Konjunktur- und Krisenbewältigungspakets

Finanzbedarf in Mrd Euro



Quelle: Koalitionsausschuss

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# EU fiscal support measures

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April 2020: **540 bln €** support package decided (**4,4% of 2019 GDP**)

- Support to mitigate unemployment risks (SURE, 100 Mrd)
- Pan-European guarantee fund for loans to companies (EIB, 200Mrd)
- Pandemic crisis support for member states via credit lines at ESM (ESM, 240 Mrd).

Juli 2020: **750 bln €** Recovery package decided (**6,3% of 2019 GDP**)

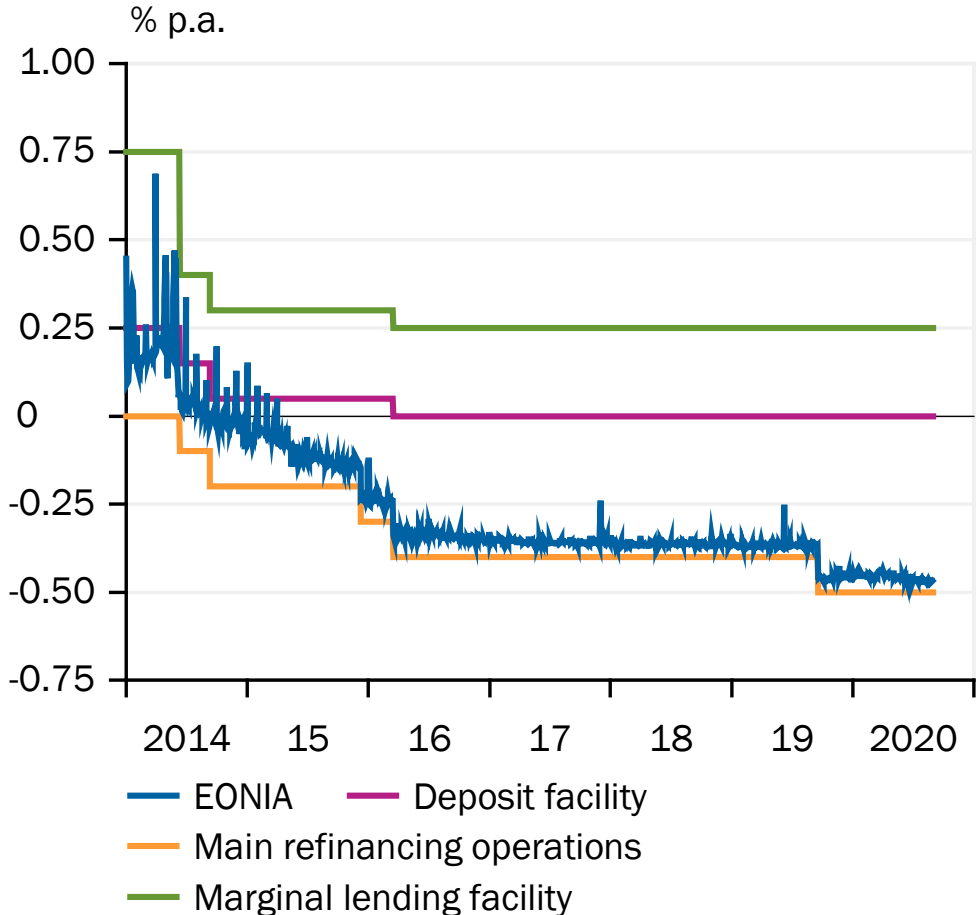
- 390 bln € grants/transfers, 360 bln € loans
- Investment, green and digital transition, reforms, plans must be submitted. Funds will be allotted till 2023 and spent by 2026.
- Distribution key: 70% according to GDP/capita 2019, population 2019, unemployment 2015-2019, 30% by corona crisis impact
- New: borrowing by the EU. Temporary. Repayment till 2058. Planned: new EU income sources (tax on non-recycled plastic packaging, CO<sup>2</sup>- border tax, digital tax).

### III. Monetary policy: Liquidity, asset purchases and judicial conflict

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# ECB: No change in negative policy rates, but

### EONIA and policy rates



Source: ECB

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## .. but nevertheless massive easing by the ECB since March 12, 2020

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**March 12:** Easing of collateral constraints; series of LTRO's; TLTRO III funding conditions eased. APP including PSPP expanded by temporary envelope of 120bln€ on top of 20 bln€ per month since Nov 1, 2019.

**March 18:** 750bln€ Pandemic emergency purchase program (6,3% of 2019 GDP), PEPP until end of 2020. Flexible on time and capital key for government debt. CSPP expanded to non-financial commercial paper.

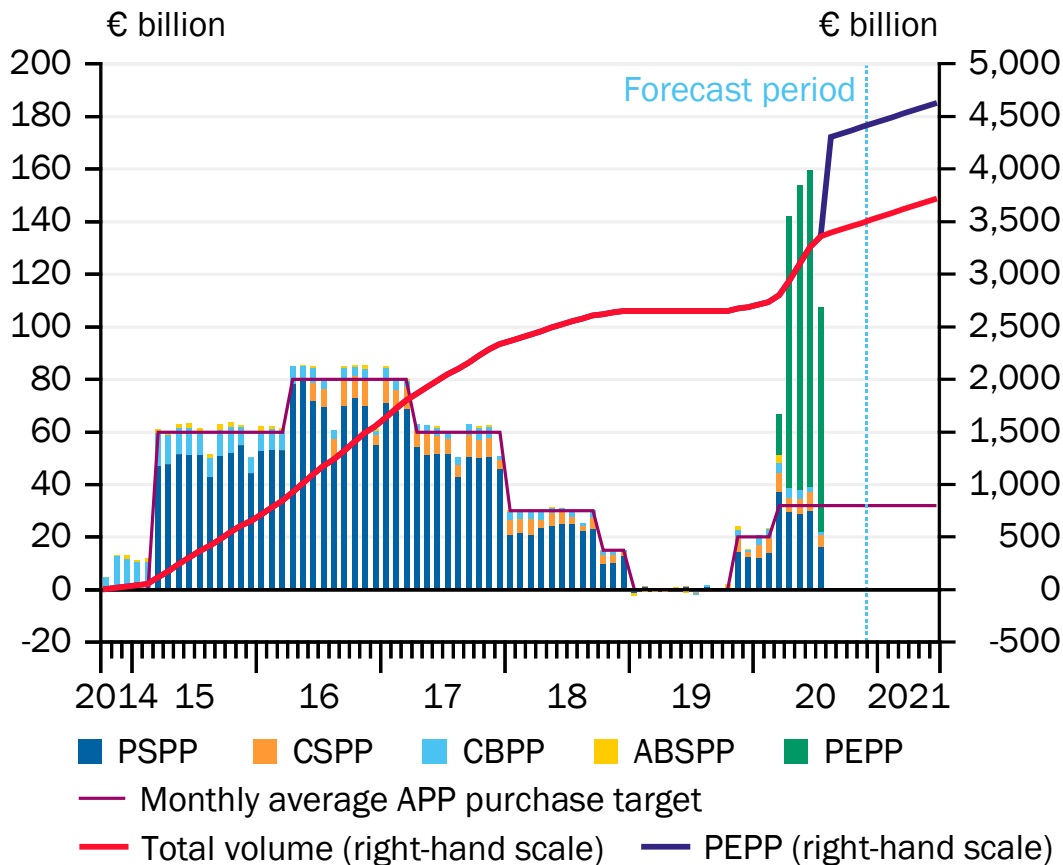
**April 30:** TLTRO III funding conditions eased further. -0,5% and -1% lending criterion is satisfied. New series of 7 PELTRO's.

**June 4:** PEPP increased by 600 bln€ to 1350 bln€, extended to June 21, reinvested at least till June 22. (total 11,3% of 2019 GDP)

(total government deficit forecast is 8,3%)

# ECB: Asset purchases expand rapidly + cheap liquidity for banks

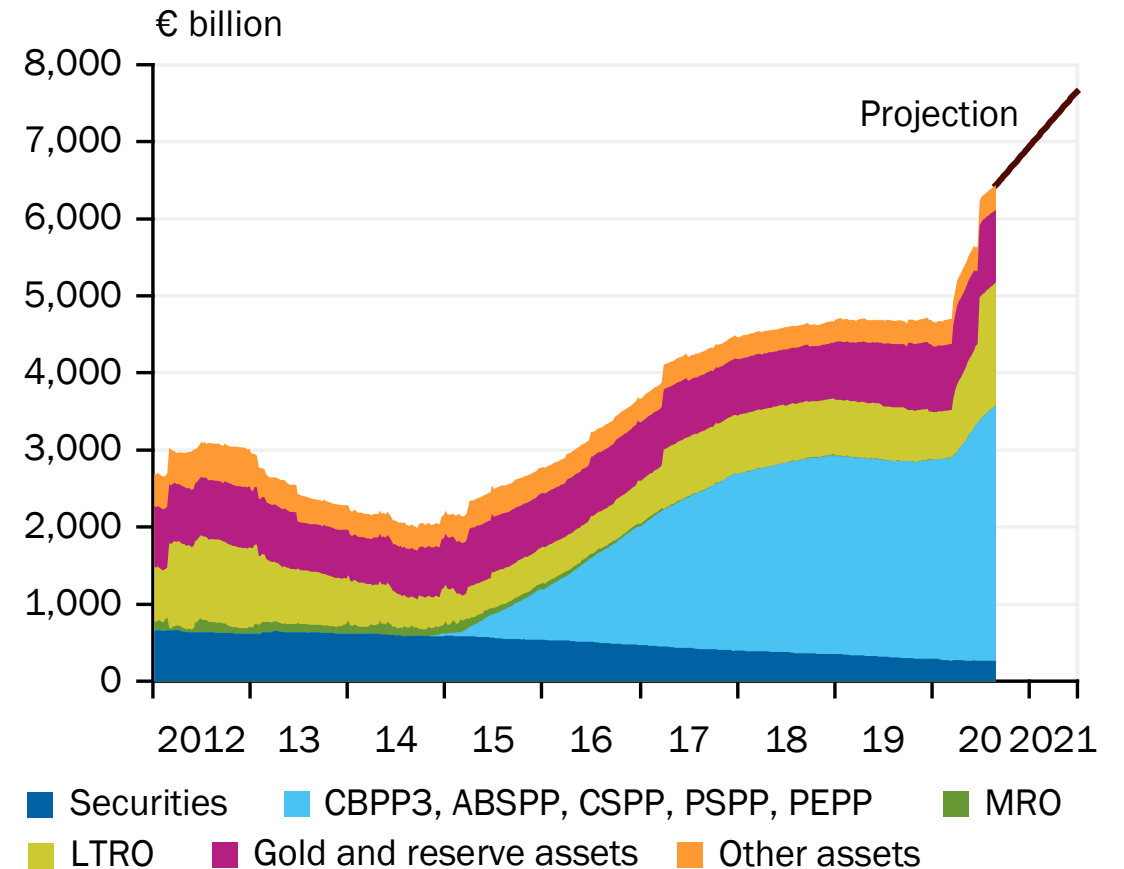
## Massive expansion of the Asset Purchase Programmes



Sources: ECB, own calculations

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## Asset structure



Sources: ECB, own calculations

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# Judicial conflict about proportionality of PSPP



# Concerns about fiscal and monetary policy

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## Fiscal policy

- Further room for fiscal easing depends on financing costs.
- The long-run equilibrium real interest rate may not be that low.
- There is a reversal risk regarding interest rates relative to growth.
- EMU is becoming a borrowing union and transfer union. Yet, control over fiscal policy and liability for debt are not on the same level.

## Monetary policy

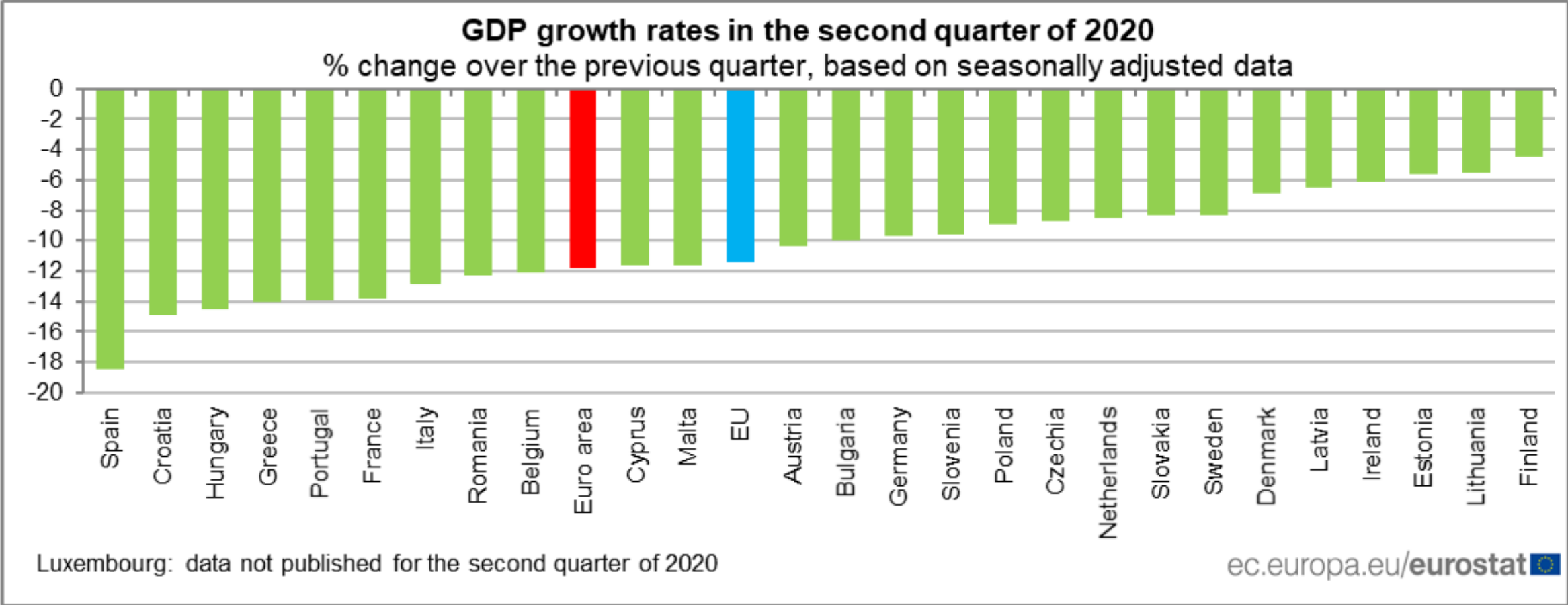
- How to conduct further easing if necessary (buy more, other assets, lower interest rates further, yield curve control)
- There is no exit strategy from asset purchases. Risks of fiscal dominance and financial dominance.



Extra

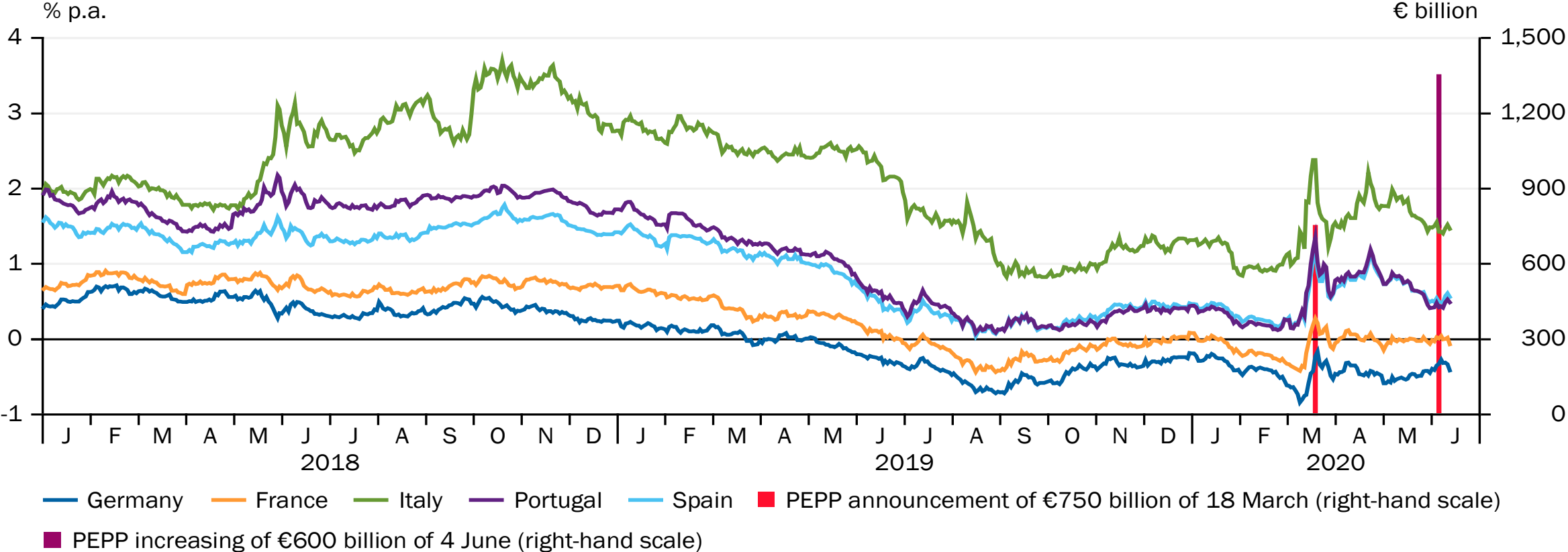


# Comparison of second-quarter growth



# Government bond yields and PEPP

## 10-year government bond yields



Sources: ECB, Refinitiv Datastream

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