Commentary

Sovereigns Taking Action to Mitigate Impact of Coronavirus

DBRS Morningstar
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Sovereigns Taking Action to Support Affected Businesses and Households

The global Coronavirus Disease (COVID-19) outbreak and associated public health response will impose a significant cost in terms of lost economic output across the major economies. Nonetheless, governments and central banks are implementing targeted, timely and temporary measures, generally believed to be appropriate at such times, to support affected businesses and households. These measures will be important to sustain the functioning of these economies under the stress of the public health measures. This commentary summarizes the policy responses of some of the largest advanced economies thus far. Additional measures will likely be forthcoming over time, as governments come to terms with the various impacts of containment.

Although the immediate impact of social distancing and widespread travel restrictions cannot be fully offset in the near term, DBRS Morningstar expects the cumulative effects of these measures to support a relatively more robust economic recovery beginning later in 2020. Furthermore, as DBRS Morningstar will outline in a forthcoming commentary on the overall position of the major advanced economy sovereigns heading into the current pandemic, DBRS Morningstar sees most advanced economy sovereigns as having space to implement temporary stimulus measures without an adverse impact on their ratings.

Governments are taking on the financial burden of supporting their populations and businesses, and they are likely to do more

Governments are taking a range of measures to address the diverse impact of the virus. The key measures for select advanced economies are summarized in the Appendix. Government financial balances will deteriorate across global sovereigns this year. In general, there is some built-in tolerance within sovereign ratings – at least those within investment grade – for temporary adverse shocks. The present difficulty is in assessing the expected duration and depth of the shock, which largely depends on the emergency health measures being revised on a weekly or even daily basis in some countries.

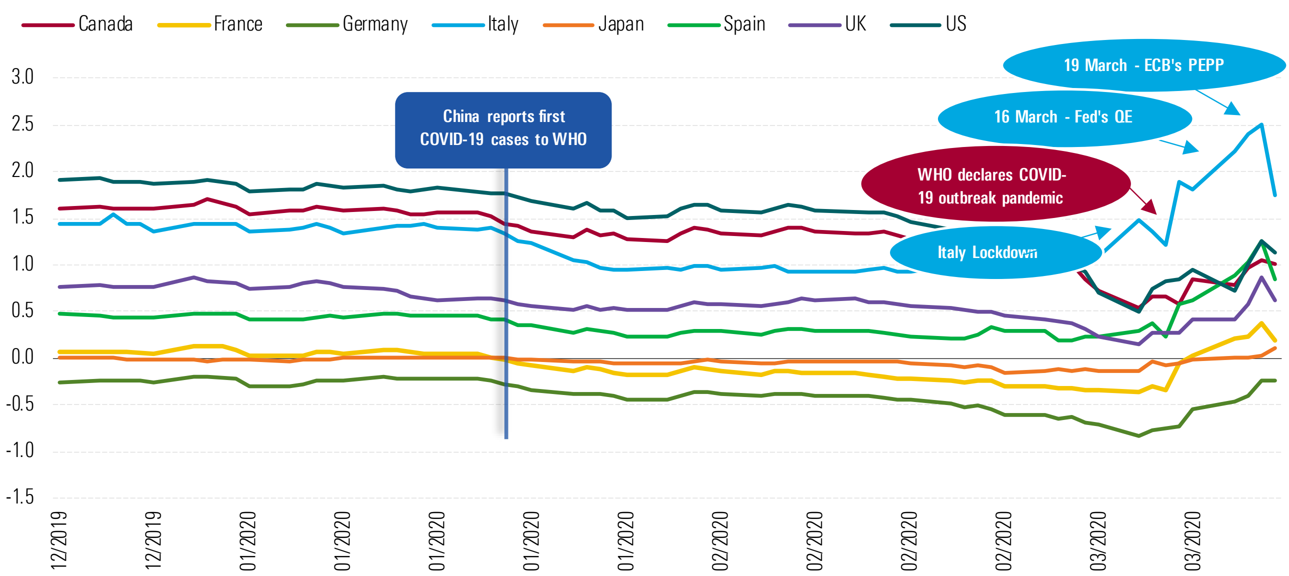
Generally, there is also a tradeoff between 'well-targeted' and 'timely'; indiscriminate support and subsidies will be more costly in fiscal terms, but waiting for individuals to file for unemployment or other support may have deeper economic costs. The responses of individual countries may also complicate an assessment of the relative economic impact: unemployment statistics, for example, will not reveal the extent of labour underutilization, if some authorities have partially absorbed companies' labour costs. Provided demand begins to recover before support runs out, these should not have any adverse effects on medium-term growth – but monitoring the recovery and any lasting implications from this episode will be important for the outlook on sovereign ratings. At a minimum, and relative to *DBRS Morningstar's 2020 Outlook for Global Sovereigns* and our *2019 Year-in-Review*, the likelihood of further imminent upgrades has clearly diminished.

Types of Measures

Government efforts can be divided into three broad categories: support to businesses, support to households, and support to financial markets and intermediaries. For most of the sovereigns discussed within this commentary, the benefit of keeping people employed and viable companies afloat is likely to be of greater value than the burden of added public debt, particularly given the exceptionally low funding rates. Central banks' bond market interventions are providing funding to governments to add new expenditures at zero or very low cost. Important examples are the ECB's likely EUR 1.1 trillion of interventions this year, including the EUR 750 billion Pandemic Emergency Purchase Programme and the US Fed's expanding quantitative easing that includes at least $500bn Treasuries and at least $200 billion in mortgage-backed securities, and now also corporate bonds. Borrowing rates remain low for most advanced countries, even those with somewhat higher rates, like Italy (see Exhibit 1).

Broad based income tax cuts and capital spending polices may be less effective in this environment with extensive curtailment of activity where households are not able to spend nor companies go out and start investment projects. Instead, governments are using a variety of generally temporary measures designed to alleviate the burden on affected households and businesses. Important measures include direct financial transfers to public health systems, other health care providers, and related healthcare support industries (e.g., producers of pharmaceuticals and medical supplies), increasing access to unemployment entitlements, direct cash transfers to households, providing short term tax breaks to companies that temporarily have to shut their doors to customers, and

Exhibit 1 Selected Countries: 10 year Government Bond Yields (%)



Source: Refinitiv/Haver Analytics, DBRS Morningstar.

encouraging financial institutions to offer mortgage and debt repayment holidays. Government loan guarantees and strategic business bailouts can burden financial accounts with contingent liability risks, but are helpful tools to prevent short-term liquidity problems from turning into solvency problems with the associated economic dislocations.

For central banks, cutting policy rates is not enough by itself to support the global economy, as isolated households and closed manufacturing and services companies are not able to raise discretionary spending or start investment projects. We see central banks and financial regulatory authorities playing a key role introducing a variety of supportive measures. Record levels of emergency debt purchase schemes that support zero or low cost fiscal spending, financing schemes to support corporate liquidity and capital relief measures for banks are all helpful to keep the financial system strong to support the functioning of the economy. The risk to inflation is limited at this time, not least because of the severe slump in oil markets. The UK Treasury's COVID-19 Corporate Financing Facility (CCFF) commercial paper purchase programme to support companies' cashflow is another example of supportive measures.

Conclusions

Though visibility around the ultimate duration of containment policies and the spread of the virus is limited, DBRS Morningstar expects the combined weight of government stimulus measures and the determined response of the medical community will help cushion the economic shock. Although the impact on some sectors may take some time to fully reverse, the most severe slump in demand will most likely be limited to a few quarters. Over time, fiscal policy can be subsequently tightened in most countries to restore flexibility to respond to future shocks. While geographies, sectors and households will experience varied impacts, overall we view ongoing government and central bank measures as beneficial to soften the blow. In coming weeks, DBRS Morningstar will provide updates on its assessment of the economic and fiscal impact of coronavirus on its global sovereign ratings.

Appendix: Key Fiscal Measures of Advanced Countries

Country	Key Fiscal Measures
Australia	• Total package of AUD 84 billion. • Includes cash income support measures to households and businesses. • Access to superannuation fund up to AUD 10,000. • 50% guarantee on loans to SMEs (up to AUD 40 billion). • Cash flow support for SMEs and temporary relief from legal action for firms facing financial distress.
Belgium	• Government-backed loan guarantees, burden-shared with the financial sector, for businesses and the self-employed – EUR 50 billion (11% of GDP). • Tax deferrals. • Loan repayment deferrals for businesses, the self-employed and mortgage borrowers. • Some financial support for companies affected. • Temporary wage subsidies for affected workers. • Total package estimated around EUR 8-10 billion (2% of GDP), excluding guarantees.
Canada	• Direct assistance to individuals and firms worth CAD 27 billion (1.2% of GDP). Most of this is cash relief to workers adversely affected by COVID-19 or those who do not qualify for employment insurance. Also increased tax rebates and tax credits for low and middle income families. • Deferred tax payments: postponing CAD 55 billion tax payments by 4 months. • Other measures: six month interest-free moratorium on repayment of Canada student loans.
France	• Broad based measures worth EUR 45 billion spending planned (1.7% of GDP). EUR 35 billion in reduced social security contributions EUR 8.5 billion in support to forced part-time employment. EUR 2 billion in solidarity fund for self-employed. • EUR 300 billion lines of credit to support corporates.
Germany	• State guarantees add to over EUR 1 trillion (just over 30% of GDP). • An Economic Stabilization Fund for large-scale support measures for companies – EUR 100 billion for equity measures and EUR 400 billion for liquidity guarantees (14.6% of GDP). • Additional government-backed credit guarantees for companies through state-owned KfW bank – potentially EUR 553 billion (16% of GDP). • Immediate assistance for small businesses, the self-employed and freelancers – EUR 50 billion (1.5% of GDP). • Broader access to existing low-cost loans and credit guarantees. • Tax deferrals. • Wage subsidies for affected workers. • Increased spending on public investment by EUR 12.4 billion between 2021 and 2024, equivalent to 0.4% of GDP.
Italy	• Higher spending on healthcare and civil protection including hiring doctors and medical equipment – EUR 3.3 bn. • Automatic stabilizers, including extension of a moratorium on first-home mortgages – EUR 8.9 bn. • Tax deferrals. • EUR 0.5 billion of support to civil aviation. • Credit guarantees and liquidity support measures – EUR 6 bn, potentially mobilising around EUR 340 bn.
Japan	• Stimulus package of JPY 400 bn (~USD 3.6bn) aimed at: Prevention of COVID-19 from spreading/ developing medical treatment.

Country	Key Fiscal Measures
	Relief for temporary school closures. Support for shrinking business activities and employment. • PM Abe discussing additional stimulus of a mix of spending and tax cuts.
Netherlands	• Broader access to existing credit guarantees. • Additional temporary guarantees for companies and a potential compensation scheme for impacted sectors. • Tax deferrals. • Wage subsidies for affected workers for three months - EUR 10 billion (1.2% of GDP). • Assistance for self-employed workers – around EUR 4 billion (0.5% of GDP). • Total package around EUR 10-20 billion (1.2-2.5% GDP).
Spain	• First Package: EUR 18 billion, including tax deferrals for SMEs/self-employed, healthcare related spending, and support for the tourism sector. • Second Package: EUR 107 billion of public commitments that could mobilise around EUR 200 billion, including a EUR 100 billion public guarantee for corporates and EUR 5bn of public spending. Facilitating temporary lay-offs, easing conditions for workers and firms under this scheme. • Established a one month moratorium on mortgages for vulnerable households, and a similar one for utility services.
Sweden	• The fiscal package could sum up to SEK 300 billion, if the entire liquidity reinforcement through tax deferrals is used. Government introduced a system of short-term lay-offs, including subsidies/benefits to workers. • State credit guarantees to airlines up to SEK 5 billion and expanded credit guarantee for exporters.
Switzerland	• Liquidity support to workers and SMEs – CHF 10 bn. • Credit Guarantee Program – CHF 20bn. To ensure that SMEs receive bridging / emergency loans from the banks. • Labor market – CHF 10bn. To provide for short time work allowances (if work hours are cut), compensation for the self-employed and people who cannot work because of the country's shutdown of many businesses. • Postponement of social security contributions, payment of VAT, one month debt moratorium.
United Kingdom	• UK Government grants will cover 80% of the salary of retained workers up to a total of GBP 2,500 a month. • GBP 330 bn in government-backed loans and guarantees, equivalent to 15% of GDP. • GBP 30bn of support to public services, vulnerable people and to provide business with tax relief and loans. • Other measures: Mortgage lenders to offer payment holidays of up to 3 months.
United States	• Phase 1: USD 8.3 billion supplemental budget for federal agencies responding to the coronavirus outbreak. • Phase 2: Expansion of COVID-19 testing, established paid leave, expanded unemployment insurance, and increased Medicaid funding. • Phase 3 (pending): Expected to include between $300-500 bn in direct cash payments to individuals, plus additional loan and assistance programs for businesses, states and cities.

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