UNIVERSITÁ DEGLI STUDI DI TERAMO

Economic Crises, Consequences and Recovery (part 2)

Noemi Pace

Facoltá di Scienze Politiche

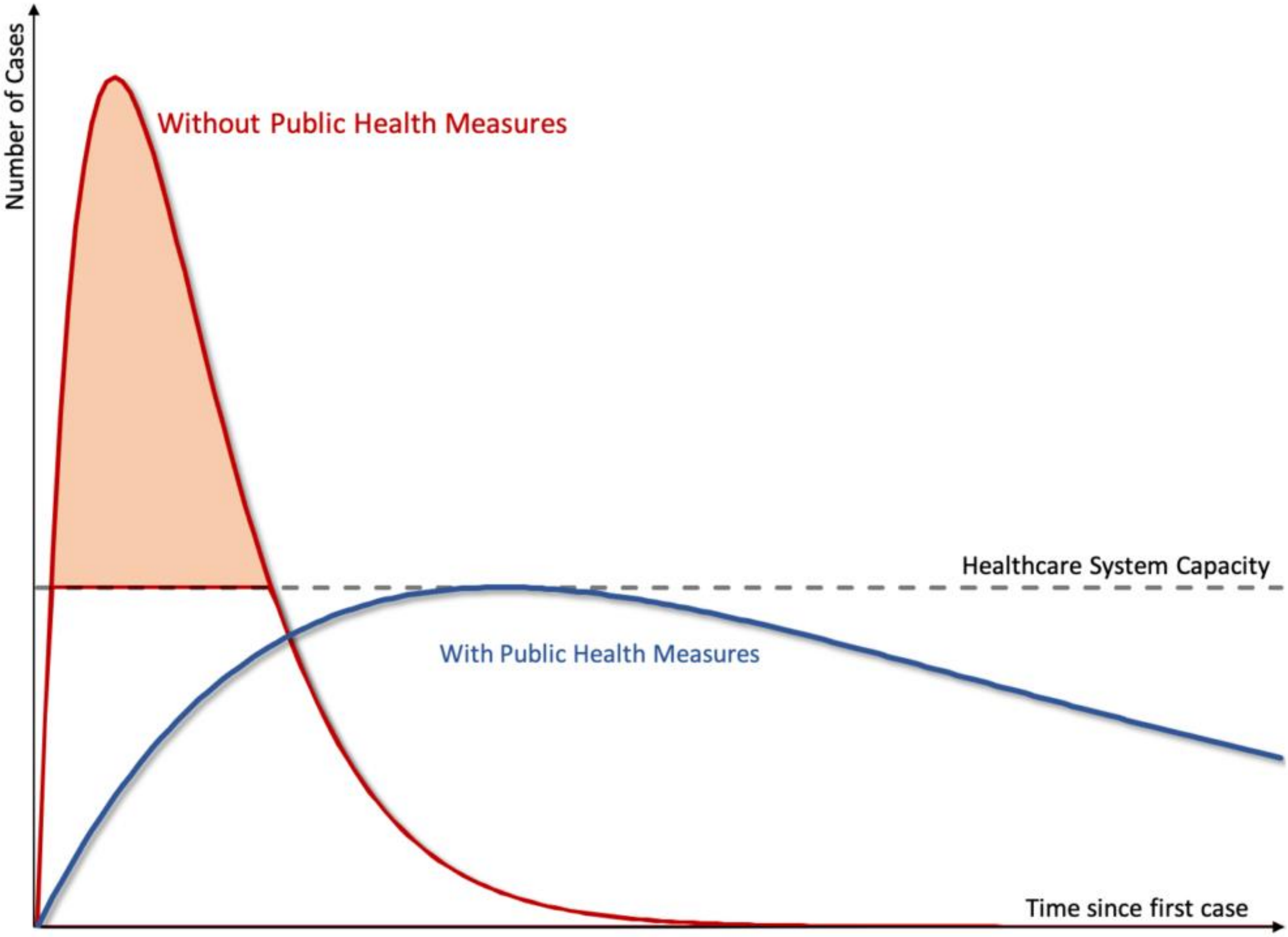
npace@unite.it

Outline

- How Depository banks and shadow banks differ
- Why, despite their differences, both types of banks are subject to bank runs
- What happens during financial panics and banking crises
- How regulatory loopholes and the rise of shadow banking led to financial crisis of 2008.
- How the new regulatory framework seeks to avoid another crises
- **What happens during the COVID-19 crisis**
- **The Great-Lookdown and the recovery phase**

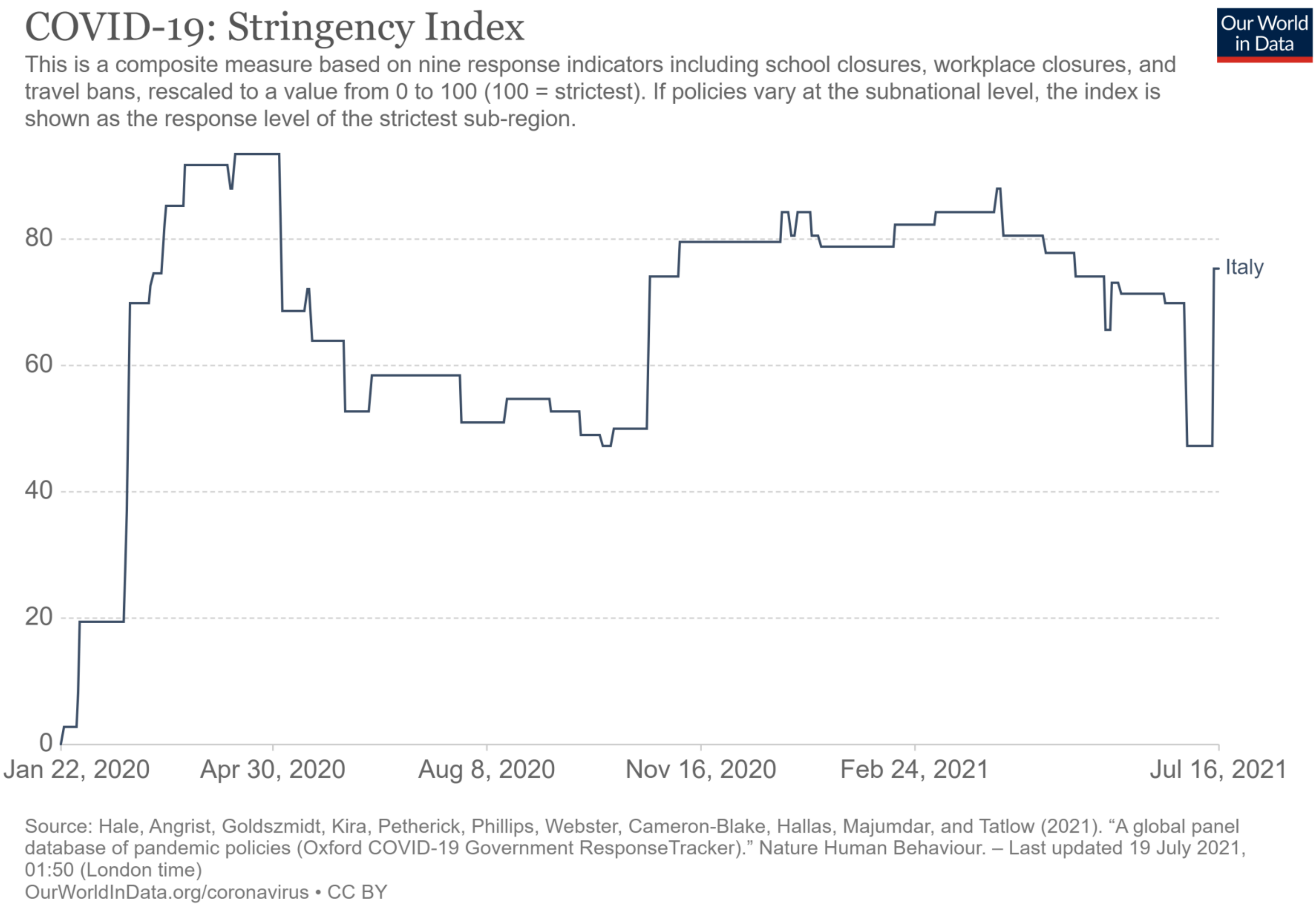
UNIVERSITÁ DEGLI STUDI DI TERAMO

Lockdown e recessione economica

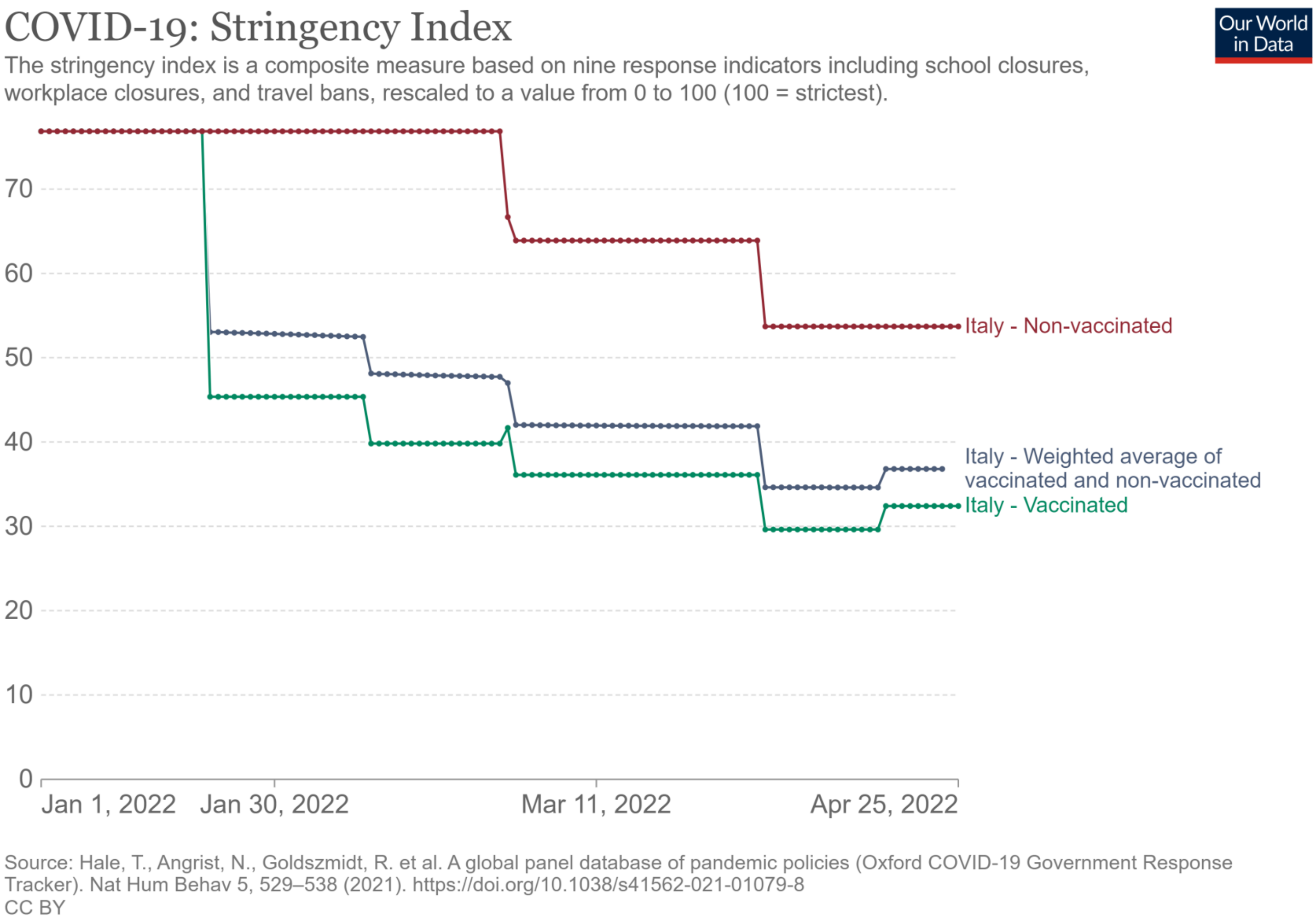


ZANICHELLI

Lockdown e recessione economica

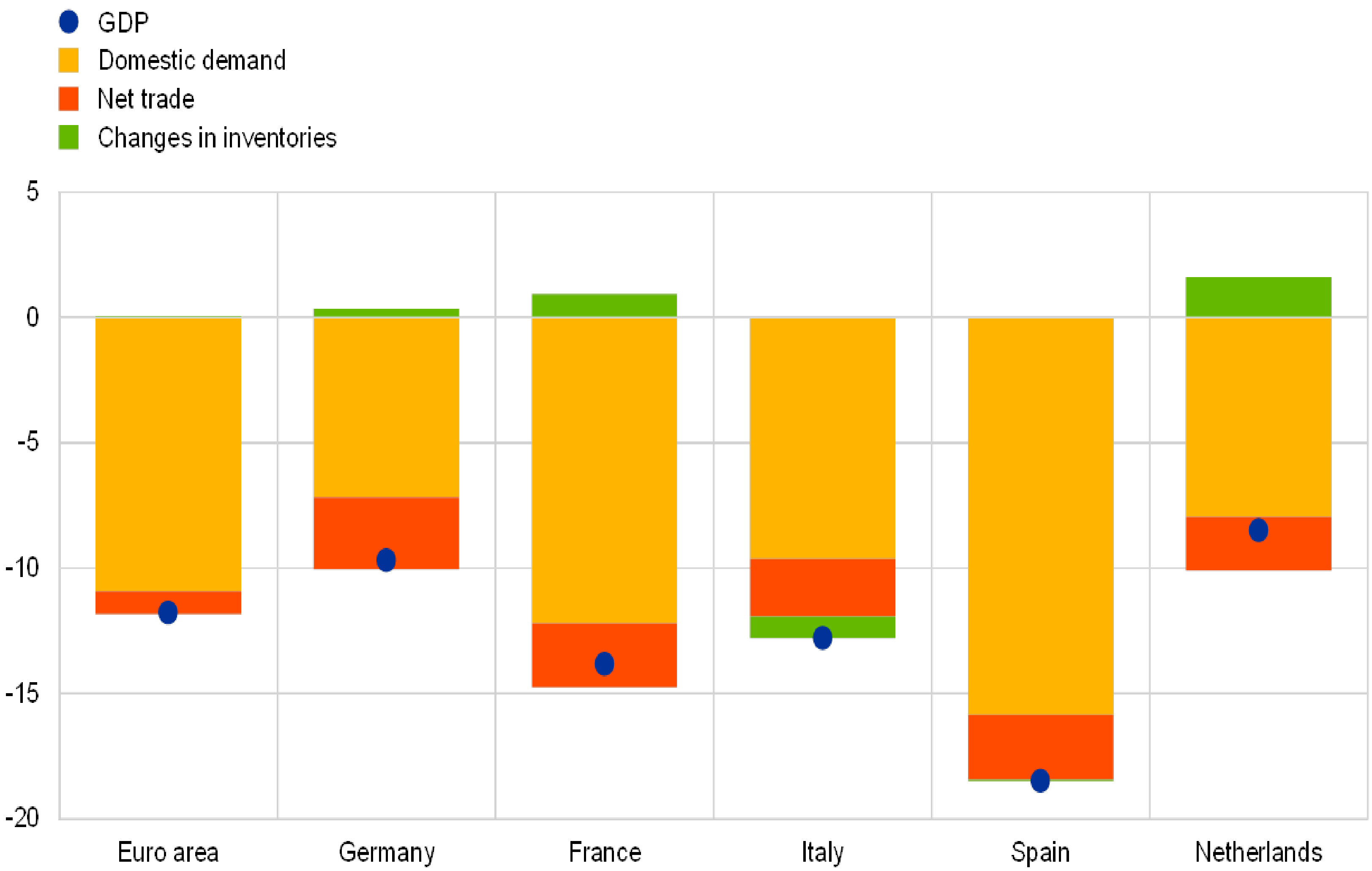


Lockdown e recessione economica



Lockdown and recession (first wave)

Changes in real GDP and contributions of the expenditure components in the second quarter of 2020



Lockdown and recession (second wave)

- Despite the sharp increase in the death toll recorded and the new measures of restrictions on economic activities and travel, the economic indicators turned out to be higher than expected (Conteduca, 2021; International Monetary Fund, 2021).

- Various factors may have led to this reduction in the impact of closures:

1) companies may have adapted to the "new normal" by reducing the risks of disruption in supply chains, ensuring safety in the workplace and finding new ways to distribute their goods and services;

2) the individual responses of the population may have changed: on the one hand, protective measures such as masks and sanitizing gel have become commonplace, reducing the need for social distancing; on the other hand, a certain "lockdown fatigue" may have emerged and compliance with voluntary rules and restrictions may have decreased.

Lockdown and recession (second wave)

3) Government restrictions have been more localized and targeted on specific activities than during the first wave (Conteduca, 2021).

- In particular, since 6 November, the Italian government has implemented a system of regions based on epidemic risk indicators.

- The classification of a region is reviewed every week based on the evolution of the epidemic in the areaInitially, three zones were identified: from yellow (the least limited) to red (the most limited), passing through orange.

- Subsequently, a white zone was introduced to allow for the possibility of a substantial lifting of restrictions in low-risk regions.

Lockdown and recession (second wave)

3) Government restrictions have been more localized and targeted on specific activities than during the first wave (Conteduca, 2021).

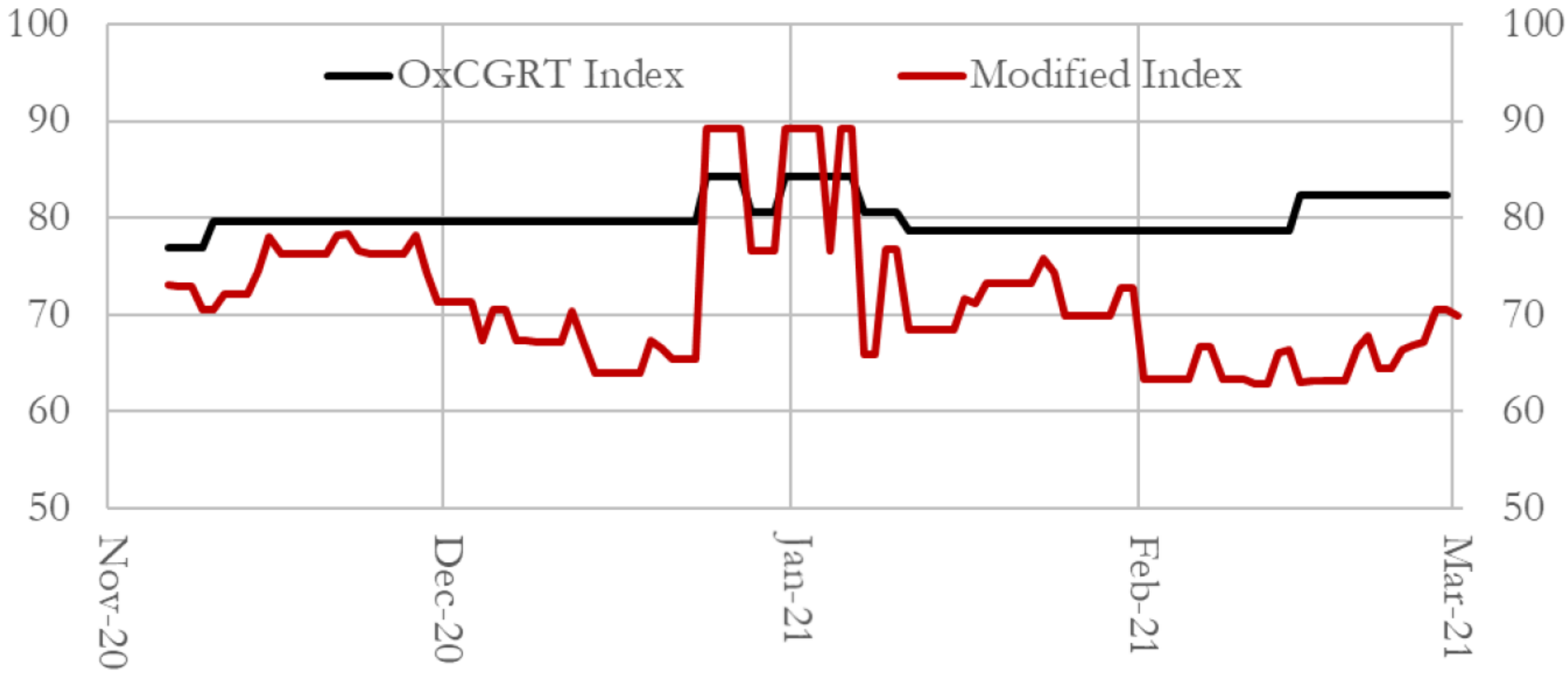
- In particular, since 6 November, the Italian government has implemented a system of regions based on epidemic risk indicators.

- The classification of a region is reviewed every week based on the evolution of the epidemic in the areaInitially, three zones were identified: from yellow (the least limited) to red (the most limited), passing through orange.

- Subsequently, a white zone was introduced to allow for the possibility of a substantial lifting of restrictions in low-risk regions.

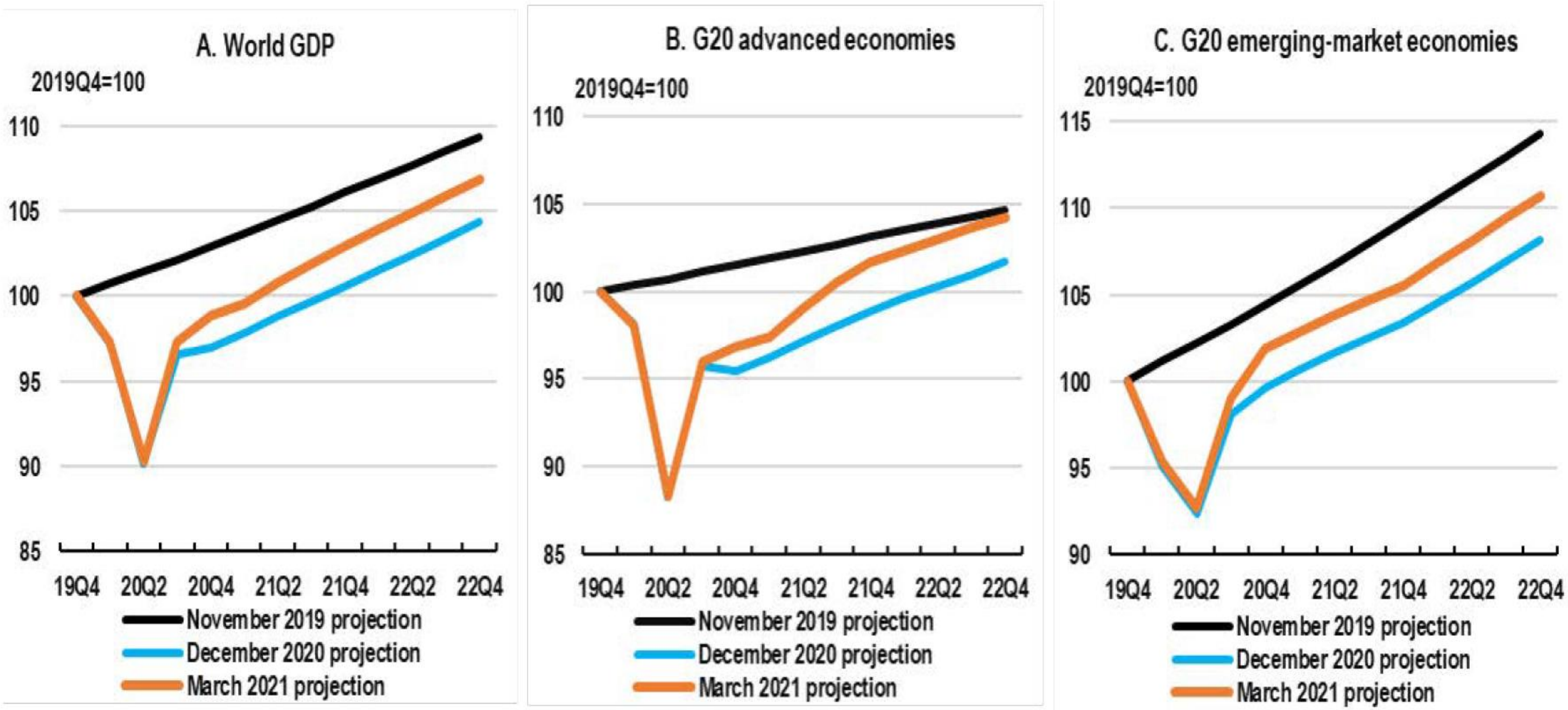
Lockdown and recession (second wave)

Official Stringency Index *vs* Modified Stringency Index Modificato (Conteduca, 2021).



Lockdown and recession (second wave)

GDP growth projection



Fiscal Policy in the European Union/Euro Area

- On December 11, EU leaders finalized the agreement on the EU budget and Next Generation EU (NGEU) recovery package, which will provide additional spending of €750 billion in total, financed by borrowing at the EU level.

- The funds are split between grants (€390 billion) and loans (€360 billion), which will be channeled through a special Recovery and Resilience Facility (RRF) and a top-up to existing EU budget programs.

- Most of the money is set to be committed in 2021-23, with 70 percent of grants to be committed in 2021-22.

Fiscal Policy in the European Union/Euro Area

While the exact allocation of some of the funds remains to be determined, high-debt countries hit hard by the pandemic (e.g., Italy and Spain) and Eastern European countries will be the biggest net beneficiaries from the RRF.

The European Council and European Parliament now need to take steps to adopt the relevant legislation, including the Own Resources Decision, which must also be ratified by member states' parliaments.

As of May 5, 2021, 14 EU member states submitted their Recovery and Resilience Plans (RRP) to the European Commission for financing the RRF.

Fiscal Policy in the European Union/Euro Area

The European Commission’s latest package of about €540 billion (4 percent of EU27 GDP) includes:

(i) allowing the European Stability Mechanism (ESM) to provide Pandemic Crisis Support (based on existing precautionary credit lines) up to 2 percent of 2019 GDP for each euro area country (up to €240 billion in total) to finance health related spending;

(ii) providing €25 billion in government guarantees to the European Investment Bank (EIB) to support up to €200 billion to finance to companies, with a focus on SMEs;

(iii) creating a temporary loan-based instrument (SURE) of up to €100 billion to protect workers and jobs, supported by guarantees from EU Member States.

Monetary Policy in the European Union/Euro Area

At the onset of the pandemic the ECB decided to provide monetary policy support through:

(i) additional asset purchases of €120 billion until end-2020 under the existing program (APP);

(ii) introduced a new liquidity facility (PELTRO), which consists of a series of non-targeted Pandemic Emergency Longer-Term Refinancing Operations carried out with an interest rate that is 25bp below the average Main Refinancing Operation (MRO) interest rate. The PELTROs commenced in May and matured in a staggered sequence between July and September 2021;

(iii) introduced an additional €750 billion asset purchase program of private and public sector securities (Pandemic Emergency Purchase Program, PEPP)

Monetary Policy in the European Union/Euro Area

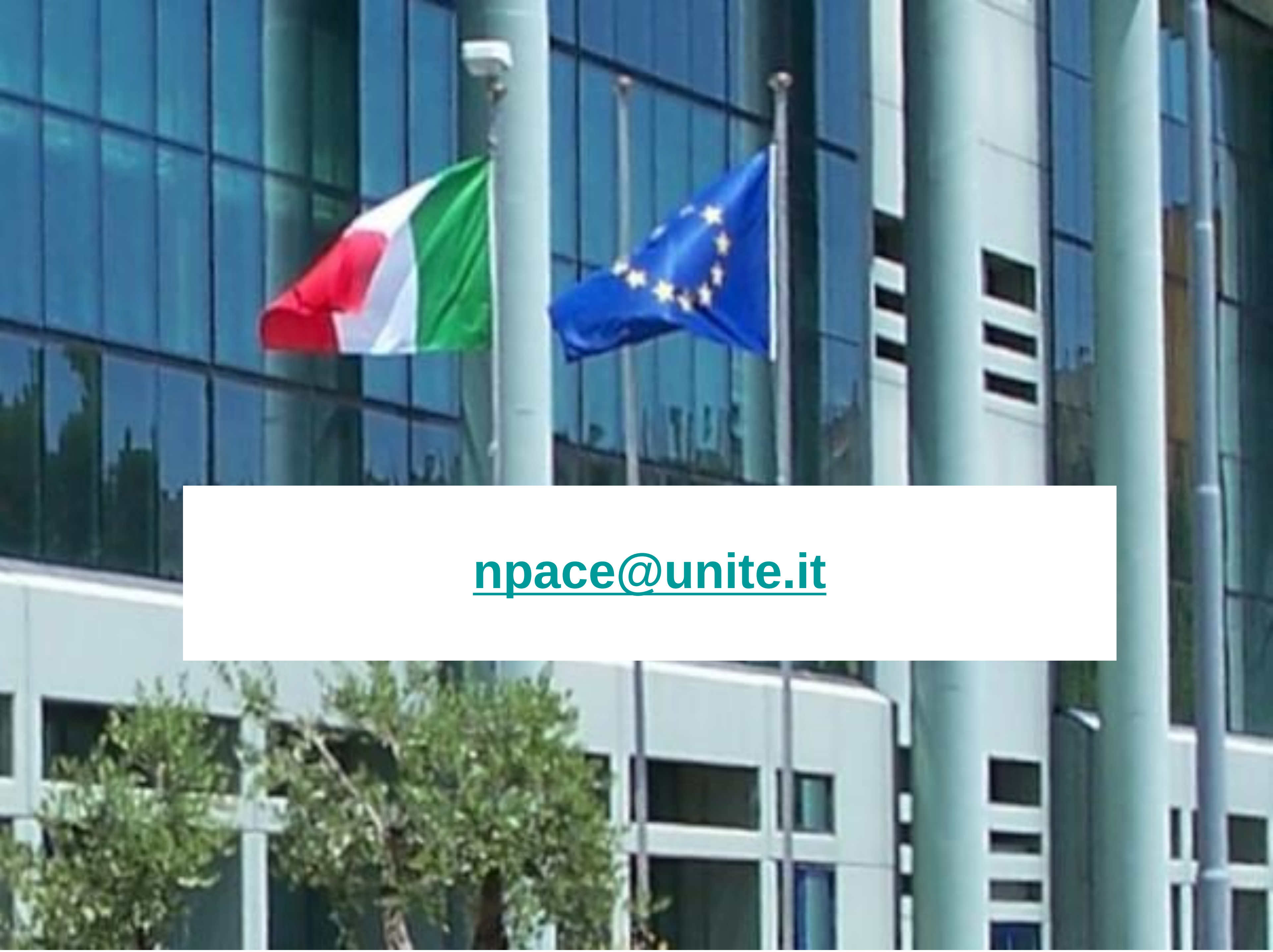
On December 2020, the ECB Governing Council extended the duration and scale of several monetary policy instruments, reflecting a weaker inflation outlook.

The recalibration of the ECB's instruments included:

(i) increase in the Pandemic Emergency Purchase Program (PEPP) by €500 billion to €1,850 billion and extension of its duration by nine months to at least the end of March 2022 (from June 2021);

(ii) extension of the April 2020 collateral easing measures to June 2022.

On March 11, 2021, the Governing Council announced that purchases under the PEPP over 2021Q2 would be conducted at a significantly higher pace than during the first months of 2021 to preserve the favorable financial conditions.



npace@unite.it