COVID-19 AND THE RESPONSE OF CENTRAL MONETARY AUTHORITIES

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Abstract. *The spread of the coronavirus epidemic is causing turmoil in financial markets' functioning. This sudden shock required for a massive policy response. The actions of central banks have emphasized their critical role in crisis management process. The scope of this article is to emphasize policy actions taken by central banks from some selected countries, including the Republic of Moldova.*

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During the present crisis, central banks have responded quickly, in most cases even faster than official measures have announced the crisis' scale and severity. Their response indicates that central banks learned the lessons of the past global financial crisis, when delayed action resulted in severe consequences for the world economy. Within policy measures promoted during the pandemics, central banks focused on large-scale government debt's purchases as well as credit support extension for business (mostly SMEs).

These extraordinary monetary policy actions are designed exclusively to safeguard economic and financial stability, and do not amount to fiscal deficit financing.

For the comparison of policy conduit on behalf of other central authorities, the following examples can be mentioned:

a) The Bank of Japan: The Bank has enhanced monetary easing since March, 2020, implementing the following three measures: 1) implementation of the Special Program to support business financing (total funding budget 110 trillion GPY) with the scope to purchase CP and corporate bonds within about 20 trillion GPY, as well as to encourage lending by financial institutions (about 90 trillion GPY)4; 2) an ample provision of yen and foreign currency funds for the stabilization of the currency market; 3) regulatory responses in order to ensure financial system stability - the full implementation of the finalized Basel III standards has been delayed by one year, and banks have been encouraged to use their capital and liquidity buffers. Moreover, the Bank announced an easing of regulation on the leverage ratio requirement (Haruhiko, K., 2020).

b) Central Bank of England: launched a 200 billion GBP asset purchase program; reduced the reference interest rate twice a week, from 0,75% to 0,25%, and subsequently to 0,1%, which is the lowest in the bank's 325-year history; increased the size of its bond purchase program by 200 billion GBP to a total of 645 billion GBP. Also, more funding is granted to banks that increase their lending, as well as additional support is afforded to banks that offer more landing to small and medium-sized companies. The central bank closely cooperates with the Government to support large businesses by offering them cash for their corporate debt. At the same time, the UK banks have agreed that they will not pay any dividends to their shareholders that were still due from 2019, and will not pay any new dividends until the end of 2020 (TaylorWessing., 2020).

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[4] *These include a scheme in which the government takes the credit risk of lending by financial institutions to small and medium-sized firms and the Bank provides funds to those financial institutions on favorable terms*

c) The Czech National Bank: has reduced all basic interest rates in three steps. It first lowered the key two-week repo rate by 0.5 percentage point on 16 March 2020, then by another 0.75 percentage point on 26 March 2020 and by another 0.75 percentage point on 7 May. The two-week repo rate is currently set at 0.25%, the Lombard rate at 1.00% and the discount rate at 0.05%. The CNB allowed banks to postpone loan instalments where clients temporarily lose their income due to the coronavirus epidemic or preventive measures. The CNB has lowered the countercyclical capital buffer rate on bank loans located in the Czech Republic from the current 1.75% to 1% with effect from 1 April 2020. This decision means that banks will need less capital for every loan provided to the domestic economy (Jan Syrovátka, 2020). Also, the CNB has called on banks to withhold dividend payments or refrain from other steps which might jeopardize their capital resilience. Clients of banks may postpone loan instalments by three or six months, it is possible to postpone instalments of both consumer and business loans, including mortgages agreed and drawn before 26 March 2020. The CNB allowed banks to postpone loan instalments where clients temporarily lose their income due to the coronavirus epidemic or preventive measures. Banks will work individually with individual clients to determine the reasons behind their payment problems to adjust the repayment schedules for their loans accordingly. This will apply provided that clients' problems are only temporary and their ability to repay a loan in the future has not been fundamentally jeopardized.

Speaking about the Covid-19 manifestation in Republic of Moldova, in response to the challenges of COVID-19, both the Government and the National Bank of Moldova have already taken some action, by adjusting the budget, preparing a package to support the private sector and moderating monetary policy.

The NBM has started to gradually reduce rates on the main monetary policy instruments, in order to support the level of liquidity in the banking system. Thus, the Executive Committee of the National Bank of Moldova (NBM) decided, by unanimous vote, to reduce the base rate applied to the main short-term monetary policy operations by 0.25 percentage points to 2.75 percent annually (NBM, 2020). This decision is stimulating and is aimed at achieving the fundamental objective of the National Bank, as well as supporting the lending process to support aggregate domestic demand and thus the national economy. For the comparison with interventions made by other central monetary authorities related to the cutting of the base interest rate, we can mention: Turkey – 2%; Canada, USA, Norway, Romania – 1,5% respectively; Brazil – 1,25%; Hong-Kong – 1,14%; United Kingdom – 0,65%; Australia, Poland, Russia – 0,5% (Visual Capitalist., 2020).

As for the norm of required reserves from the means attracted in freely convertible currency, it will be increased by 1,5 p.p. up to 30,0% of the calculation basis, for the application periods 16 October to 15 November 2020 and 16 November to 15 December 2020 respectively (NBM, 2020). The Decision further balances the application of this monetary policy instrument to optimize financial intermediation. in the banking sector and strengthen the transmission mechanism of monetary and foreign exchange policy.

Also, the NBM exchanged views on dividend and bonus policies of commercial banks, noting that, as a matter of principle, moderation is a sound concept in the current pandemic context. NBM has recommended the commercial banks to refrain from distributing dividends to shareholders and other forms of capital distribution until at least 30 September 2020. The decision comes with the scope to keep banks sufficiently well-capitalized and stable.

We note that the National Bank of Moldova practically follows some of the actions taken by central banks in foreign countries, in order to maintain the stability of consumer prices, protect the economies of the population, encourage lending, which is plausible, but still is not sufficient when combatting the effects of Covid-19 on the national economy.

The monetary policy of the NBM, although gradually relaxed in recent period, remains relatively restrictive due to the high level of the reserve requirement. In actual conditions induced by COVID-19, such a high level of the reserve requirement deprives the economy of significant volumes of liquidity that could be directed towards the private sector. Thus, the reduction of the norm of required reserves will make the businesses to take possession of liquidity through easier bank credits. Also, it is necessary to give up the operations of selling the NBM certificates, in order to stimulate the banks' orientation towards Government lending.

Conclusions: In current circumstances induced by the Covid-19 pandemics central banks should participate in monetizing the government deficits, although in the past very few central banks would admit this. In time, governments will have to decide not to manage in the best way very high levels of public sector dept. Also, what still remains important is to maintain interest rates and bond yields at low levels.

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