THE MONETARY POLICY OF CENTRAL AND EAST EUROPEAN COUNTRIES DURING THE CORONAVIRUS CRISIS

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Abstract: *The current pandemic crisis is a unique challenge, with several economic and social consequences experienced by the entire world. In order to prevent the spread of the coronavirus, the affected states have established a series of social distancing measures and even quarantine measures. They had huge implications on the global economy. This paper focuses on the main monetary policy decisions taken by Central and East European banks in the current pandemic crisis. The response of economic policies to this crisis were remarkable. The CEE countries have implemented measures which aimed at four main objectives: honoring, first and foremost, the urgent needs of the health sector, supporting economic activity and employment, maintaining monetary and financial stability and paving the way for future recovery. We believe that central banks have responded quickly in the current crisis, in many cases, the decision being made long before the official measures have clarified the scale and seriousness of the crises.*

Key words*:* monetary policy, monetary strategies, pandemic crisis, Central and East Europe.

JEL Classification Codes: E42, E52, E58.

1. INTRODUCTION

The current pandemic crisis is an unique challenge, with several economic and social consequences experienced by the entire world. The SARS-COV-2 virus (also known as COVID-19) can affect the entire humankind and does not care about the individuals' age, gender or nationality. The elderly are the most affected by this virus and it comes with a high risk of developing serious diseases due to the physiological changes that occur with aging and poor health conditions.

In order to prevent the spread of the coronavirus, the affected states have established a series of social distancing measures and even quarantine measures. These measures had huge implications on the global economy. According to the General Manager of the BIS, Augustin Carstens (2020), „the Covid-19 pandemic and the induced global lockdown are a truly historic event. Never before has the global economy been deliberately put into an induced coma. This is no normal recession, but one that results from explicit policy choices to avoid a large-scale public health disaster. The unique character of this recession poses unfamiliar challenges."

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2. GLOBAL MONETARY POLICIES TAKEN AGAINST THE PANDEMIC CRISIS

Globally, central banks (and particularly, FED, ECB and BOJ) have responded to the economic crisis which has occurred as a result of the pandemic crises by implementing a series of monetary instruments, both conventional and unconventional, in order to fight the possible recession. The central banks started to inject money in the economy, in order to provide the necessary liquidity to households and businesses. They immediately maintained negative interest rates and aggressively expanded the quantitative easing programmes. Looking at these recent actions taken by the central banks and their response to the pandemic crisis, we believe that they have learned the lessons from the global financial crises (2007-2008) and their decisions were not taken tardily.

According to Lagarde, C. (2020) „COVID-19 has delivered the largest shock to the European economy since the Second World War. Key macroeconomic indicators have plunged on a scale and at a speed previously unseen. Industrial production fell by 18% month-on-month in April. Durable goods production was down by almost 15% in the same period and new car registrations dropped by around 50%. If the ECB's baseline macroeconomic scenario for 2020 is borne out, the euro area will lose as much output in two quarters as it had gained over the previous 15 years – and growth will not recover in full until the end of 2022".

The pandemic emergency purchase programme (PEPP) against the COVID-19 pandemic is an unconventional monetary policy measure initiated in March 2020 in order to counter the major risks to the monetary policy transmission mechanism and the outlook for the European Monetary Union posed by the coronavirus outbreak. According to the ECB, this is „ a temporary asset purchase programme of private and public sector securities". In order to support national governments, the ECB expects to issue between 1 trillion and 1.5 trillion euros, money which will translate into additional debt. In order to fight the possible bankruptcies that may occur due to the fall of small and medium-sized enterprises by the end of 2020, together with the difficulties that large enterprises may experience in 2021, the ECB had decided to increase the volume of asset purchases from 750 billion to 1.350 billion euros by July 2021.

These being said, the most common measures taken by central banks, both in developed and emerging countries against the financial and economic crisis following the coronavirus pandemic were represented by the assets purchasing programmes.

3. THE MONETARY POLICY OF CENTRAL AND EAST EUROPEAN COUNTRIES DURING THE CORONAVIRUS CRISIS

In Central and East Europe (CEE), a series of countries (Croatia, Poland and Romania) have implemented assets purchasing programmes. The first CEE state to announce the acquisition of government bonds was Croatia (March 13, 2020). The National Bank of Poland announced on March 17 that it will begin a large-scale bond purchase programme, while in Romania, the National Bank announced (March 20, 2020) that it will acquire government securities at its discretion from the secondary market. The Czech National Bank also obtained, in mid-April 2020, the legal mandate to purchase assets.

At the beginning of 2020, the economic conditions in Central and Est European countries were relatively favorable. The outbreak of the SARS-COV-2, in the winter of 2019, escalated quickly into a global pandemic crisis by the spring of 2020. The countries responded to these public health challenges through a series of measures such as closing the borders and imposing mass restrictive measures. Although most CEE countries, initially, were not hit as hard as the Western European countries by the virus, they decided to take immediate action, given that they have open economies. The impact of the coronavirus pandemic has dramatically changed the outlook for the global economy, and the measures designed to stop the pandemic taken by the governments had negative effects on the global trade, as well as on the pattern of production and consumption. In the following paragraphs, we will present the monetary policy measures taken by the selected Central and East European countries. We decided to analyze four of the CEE countries, namely Poland, Czech Republic, Hungary and Romania, because these countries have the same monetary policy objective (price stability), the same monetary strategy (inflation targeting), as well as regimes based on floating or controlled exchange rates.

Under the extraordinary monetary policy meeting of the Czech National Bank Board (March 16, 2020), the central bank adopted a series of first measures to attenuate the impact of the pandemic crisis on businesses and households. In this meeting, the council decided to reduce the two-week repo rate by 0.50 pp. to 1.75%. At the same time, it was decided to reduce the Lombard rate to 2.75% and the discount rate to 0.75%. Subsequently, on March 26, the Czech National Bank decreased the rates even further, the two-week repo rate reaching 1%, the Lombard rate 2%, and the discount rate 0.05%. Following a new macroeconomic forecast made by the Bank's Council, it was decided (May 7, 2020) to continue the process of reducing the main monetary policy rates used by the Czech economy, as it follows: the two-week repo rate decreased to 0.25%, the Lombard rate decreased to 1% and the discount rate remained at 0.05%.

The National Bank of Czech Republic has allowed banks to postpone the rates of customers who have temporarily lost their income due to the coronavirus pandemic. The central bank also reduced the repayment rate of countercyclical capital on bank loans from 1.75% to 1%, which meant that banks needed less capital for each loan given to the domestic economy. This has resulted in more possibilities to lend money to companies and individuals affected by the pandemic, and if necessary, the central bank is willing to completely remove that buffer. In Figure 1 is presented the evolution of the main monetary policy rates used by the National Bank of Czech Republic.

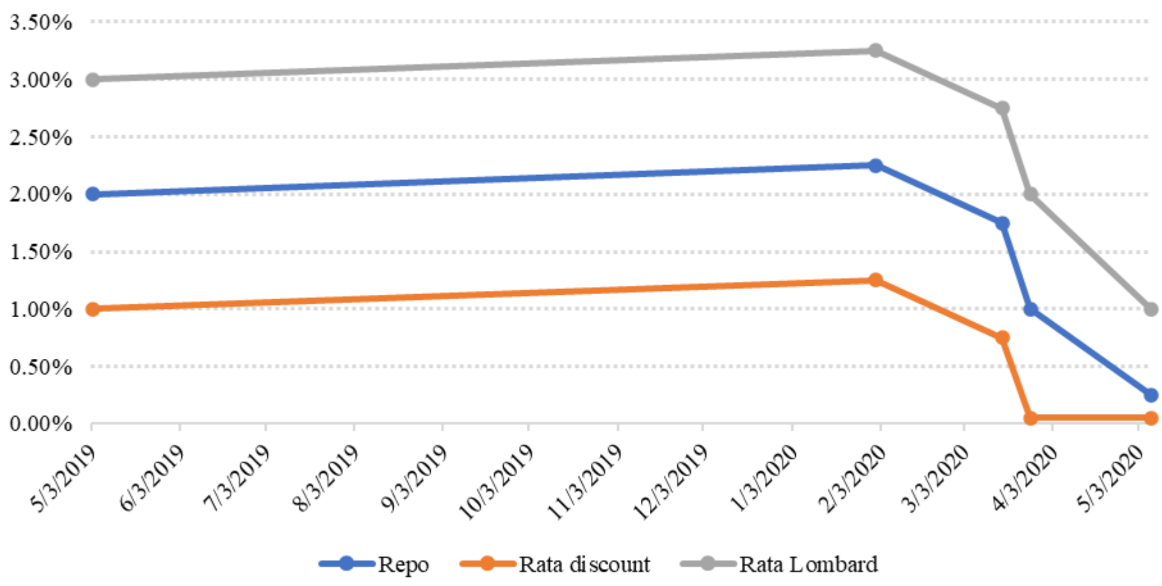

Figure 1. The evolution of the main monetary policy rates used by the National Bank o Czech Republic (March 2019 – March 2020)

Poland was no exception to the pandemic crisis, as it was in the case of the global financial crises of 2007-2008, when the Polish economy suffered the least damage, being the only country in the European Union which did not enter a recession. The Polish economy experienced a slowdown in terms of economic growth (from 3.2% in the forth quarter of 2019 to 2% in the first quarter of 2020), together with a slowdown in consumption growth and investment growth (1.2% in the fourth quarter of 2019, compared to 3.3.% the forth quarter of 2019, respectively, 0.9% in the first quarter of 2020, compared to 6.1% in the fourth quarter of 2019). Under these circumstances, the situation on the labor market has deteriorated, the number of jobs has decreased, and the unemployment rate has increased from 5.1% in March 2020 to 6.1% in May 2020.

In this regard, the National Bank of Poland eased the monetary policy strategy by reducing the reference rate from 1.5% to 0.1%. Likewise, government-guaranteed bonds and debt securities purchases were made on the secondary market. In Table 1 we are presenting the main changes made by the National Bank of Poland in terms of monetary policy rates.

Table 1. The evolution of the National Bank of Poland monetary policy rates (March 2020 - May 2020)

Date	Reference / refinancing rate	Credit facility interest rate - Lombard rate	Deposit facility interest rate	Rediscount rate	Discount rate
March 4, 2020	1,50%	2,50%	0,50%	1,75%	-
March 17, 2020	1,00%	1,50%	0,50%	1,05%	1,10%
April 8, 20020	0,50%	1,00%	0,00%	0,55%	0,60%
May 28, 2020	0,10%	0,50%	0,00%	0,11%	0,12%

The coronavirus pandemic also had a severe economic impact on the Romanian economy. As a result of the consumption structure changes and the social distancing measures, the annual inflation rate decreased to 3.05% in March 2020 and 2.68% in April 2020, compared to December 2019, when the annual CPI was 4%. The lowest level registered by the inflation rate was recorded in May 2020 (2.26%), but the descending trend did not last, and it rose to 2.58% in June 2020. According to the National Bank of Romania (2020), „the economic growth decelerated visibly in the first quarter of 2020 – to 2.4%, from 4.3% in the previous quarter – even if in the first two months of 2020, the economic growth remained particularly robust. At the same time, the trade deficit has accelerated considerably, due to a higher decline registered in terms of goods and services exports.

In Romania, the first meeting of the National Bank Board of Directors regarding the coronavirus pandemic took place on March 20, 2020. During this meeting, the National Bank decided to reduce the monetary policy interest rate to 2% (from 2.5%), to decrease the interest rate for the lending facility to 2.5% (from 3.5%) and to maintain the deposit facility interest rate at 1.5%, in order to narrow the symmetrical corridor formed around the monetary policy interest rate from 1% to 0.50%. Other measures taken by the central bank consisted in the purchase of a series of government securities on the secondary market, as well as providing liquidity to credit institutions through repo operations. Further, on May 29, 2020, the Romanian central bank decided to reduce the monetary policy interest rate by 0.25 pp. (from 2% to 1.75%) and the rates related to permanent facilities (from 2.50% to 2.25% for the lending facilities, respectively, from 1.50% to 1.25% for the deposit facility). This decrease continued, thus, on August 5, 2020, BNR decided to decrease the most important monetary policy rates by another 0.25 pp. keeping a corridor of 0.50%. In this respect, the monetary policy interest rate decreased to 1.50%, the lending facility rate decreased to 2% and the deposit rate facility decreased to 1%. Moreover, the European Central Bank, together with the Romanian National Bank, agreed on a repo line designed to provide liquidity in euros to Romanian financial institutions so that they can cope with any liquidity needs that could arise from the market dysfunctions caused by the pandemic crisis.

The Hungarian National Bank has also adjusted its monetary policy instruments in order to reduce the negative effects of COVID-19 on money market and real economy. The monetary policy instruments adjustment was driven by the efforts made in order to achieve the following macroeconomic and financial stability objectives:

- ensuring liquidity as a result of the turmoil felt by the money market in the first phase of the crisis;
- influencing short-term yields in a flexible way to revise the operational framework which affects short-term yields as a result of the confidence crisis triggered by the pandemic and uncertainty about perspectives;
- ensuring increasingly important long-term returns and the introduction of tools in order to support them.

Among the measures taken by the Hungarian Bank we can emphasize several measures to support companies in difficult situations or which are prone to face difficulties caused by the pandemic. In this regard, the National Bank of Hungary has requested banks to apply a moratorium on the payment of corporate loan installments and announced a moratorium on the payment in installments of loans granted by the Growth Financing Scheme. Withal, the bank decided to extend the range of eligible guarantees for corporate loans. On 4th of May 2020, The Hungarian National Bank launched a series of government securities purchase programmes and mortgage bonds purchase programmes in order to strengthen the transmission of monetary policy. Regarding the minimum required reserves, starting with March 2020, it was decided that this requirement could be infringe without to sanction credit institutions. This measure was taken to increase the banking system liquidity. On April 7, the Monetary Council has made the interest rate corridor symmetrical, by keeping the monetary policy rate at 0.90%, the deposit facility rate at -0.05%, while the lending facility increased from 0.90% to 1.85%. Likewise, the National Bank of Hungary, together with the European Central Bank, agreed to set up a liquidity-providing repo line so that the Hungarian financial institutions could address potential liquidity needs due to market failures caused by the pandemic crisis.

Due to the gradual removal of restrictions, in May 2020, both global economy and European economy have begun to recover. However, the economic environment continues to be characterized by uncertainties as a result of the coronavirus pandemic intensification and further possible restrictive measures which may arise as a result. In Table 2, we present, as a synthesis, the most important measures taken by the analyzed Central and East European central banks, as a result of the pandemic crisis.

Table 2. The measures taken by the CEE central banks against the pandemic crisis

Monetary policy decisions	Czech Republic	Poland	Romania	Hungary
Decreasing monetary policy rates	√	√	√	√
Liquidity support	√	√	√	√
Repo line (provided by the ECB)	-	-	√	√
Launch of securities acquisition programmes on secondary markets	-	√	√	√
Reducing the amortization rate of countercyclical capital on bank loans	√	-	-	-
Postpone the rates of bank loans	√	√	√	√

3. CONCLUSIONS

We can conclude that, in the second quarter of 2020 the economic activity decreased significantly, as a result of the measures taken to prevent the spread of the COVID-19 virus. The unemployment rate has risen globally, while the economic growth has declined considerably in some countries, whereas in other countries there has been a decline in terms of gross domestic product. Given the uncertain situation in which we are in, we believe that this pandemic crisis could lead to an even more significant slowdown in many economies, both in developed, but especially in developing countries. However, the measures taken by the Central and East European countries have improved the financial conditions, mainly driven by the recent cuts made in terms of monetary policy rates.

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