COVID-19, Central Banking and Employment
Steering Policies Towards a Just Transition

A briefing paper for the ITUC

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Highlights

- Before the COVID-19 pandemic, central banks focused on delivering price and financial stability and most no longer considered employment as part of their mandate
- The COVID crisis means that central banks are now once again playing a crucial role in shaping economic responses, including in terms of supporting employment
- In their crisis response frameworks, many central banks have implemented targeted support policies for employment, mostly in the SME sector, but also to indirectly support individuals who lost employment
- Going forward, these targeted programmes could be extended to offer support for those most vulnerable in the current crisis and facing unemployment in other sectors
- Moving from the rescue to the recovery phase, it is vital to ensure that all crisis recovery measures are aligned with the need to achieve a just transition to sustainable development
- A particular focus should be on investment in job creation and skills development in sustainability-enhancing sectors, along with social protection support for workers in sectors whose transition has accelerated (e.g. oil and gas industries)
- In order to 'build back better', it is important to further strengthen monetary-fiscal alignment to utilise the existing opportunities to ensure a more resilient recovery

1. Central banking and employment: In theory

First and foremost, most central banks are mandated to achieve and maintain price and financial stability. However, while price stability is the sole objective for some central banks, the mandates of others include references to general economic conditions, including growth and employment alongside stability. In practice, however, most central banks no longer consider the maintenance and creation of employment as explicitly part of their mandate.

Traditionally, for central banks that are concerned with the unemployment rate (such as the Federal Reserve), policy interest rate changes are seen as the primary and often only available monetary policy instrument that can indirectly affect the unemployment rate. In this framework, if central banks accept employment as a secondary objective, they can support employment, provided that inflation remains low and stable, by keeping the interest rates low until the unemployment rate reaches its natural level. It is noteworthy that 2012 marked the first time that the US Federal Reserve announced that it tied its interest-rate policy to a numerical employment target (Bernanke, 2012). In this context, the non-accelerating inflation rate of unemployment (NAIRU) is the theoretical

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level of unemployment below which inflation would be expected to rise. The conduct of monetary policy under the assumption of a NAIRU would then involve allowing just enough unemployment in the economy to prevent inflation rising above the target or target range.

Before 2008, many central banks subscribed to a strict ‘one-target (price stability)-one-instrument (interest rate)’ framework, formalised in the ‘inflation targeting’ approach under which a pre-announced inflation target is to be met, leaving no room for secondary targets such as employment. According to this approach, other goals, such as growth, development, employment or poverty reduction, are seen as inappropriate policy targets and are rather understood to be by-products of an inflation-focused approach to monetary policy that achieves general economic stabilisation. Whether this has been the case in practice has been widely questioned (eg. Epstein 2007). The inflation targeting approach has also received considerable critique in the wake of the Financial Crisis of 2008, following which financial stability has been accepted as an additional target for central banks or supervisors to be addressed through macroprudential policy (Blanchard et al. 2012).

The Financial Crisis of 2008 exemplifies how in times of crisis, central banks have often adapted their approaches and introduced policy frameworks and instruments deemed previously ‘unconventional’. This change of practice in response to a shock can also be observed in the current policy response of central banks to the severe economic contraction that has been caused by the COVID-19 pandemic.

2. The COVID crisis response of central banks: Has there been a focus on employment?

The economic crisis caused by the response to the COVID-19 pandemic has caused governments to implement far-reaching economic rescue measures, some at an unprecedented scale. Governments have rushed to introduce fiscal rescue packages and have since engaged in discussing how to design appropriate fiscal recovery packages.

Central banks and financial supervisors are also playing a crucial role in shaping the responses to the crisis brought about by the COVID-19 pandemic in both the immediate stabilisation phase and the subsequent recovery phase (Dikau et al. 2020). Many central banks have, apart from lowering interest rates, moved quickly to extend their collateral frameworks to include a broader variety and quality of assets, implemented new or scaled up existing quantitative easing programmes, and introduced various targeted and non-targeted additional (re)financing and purchase facilities. Central banks and supervisors have also eased countercyclical capital buffers and regulatory standards in an effort to encourage lending and investment. A general, more indirect contribution to employment can be seen in the large scale monetary and supervisory easing policies that have been implemented with the aim of providing liquidity and low-cost funding to the real economy through the financial system.

Furthermore, a significant number of central banks have implemented crisis response policies that are aimed more directly at supporting employment and two broad categories can be differentiated. First, these policies have, first and foremost, taken the shape of supportive lending facilities to protect employment in the Small and Medium-sized Enterprise (SME) sector, which is the largest source of jobs in all economies. These facilities come in different shapes, but have the overall aim of ensuring that SMEs can borrow at lower interest rates and that banks have additional incentives to provide these loans. Looking beyond COVID, these measures hint at a possible role for central banks in addressing the climate transition needs of the labour market.

Secondly, another step taken by central banks and supervisors has been to request commercial banks to offer targeted loan payment moratoriums and/or plans for the deferral of repayments without interest or penalty for individuals that have lost their jobs or whose salaries have been affected due to COVID-19. This also extends to requesting banks to refrain from blocking customers’ accounts if a customer has lost his or her employment.

3. Central Bank COVID Response Programmes: Examples of Employment-related Measures[2]

1) Support for SMEs to protect employment

Reserve Bank of Australia (RBA)

To allow banks to lend more to SMEs during the period of disruption caused by COVID-19, the RBA has established a term funding facility of at least A$90 billion (USD 65 billion) for access to three-year funding at 25 basis points. The RBA has recently expanded the Term Funding Facility (TFF) to A$200 billion (USD 145 billion) and extended the access through June 2021. In addition, the Australian Banking Association announced that Australian banks will defer loan repayments for small businesses affected by COVID-19.

People's Bank of China (PBC)

The PBC has expanded its re-lending and re-discounting facilities by RMB 1.8 trillion (USD 270 billion) to support manufacturers of medical supplies and daily necessities, micro-, small- and medium-sized enterprises (MSEs) and the agricultural sector, as well as a reduction of their interest rates. Targeted reserve requirement ratio cuts for large- and medium-sized banks that meet inclusive financing criteria that benefit MSEs, as well as additional cuts for eligible joint-stock banks and for small- and medium-sized banks that support SMEs have been implemented. There has been an expansion of policy banks' credit extension to private firms and MSEs of RMB 350 billion (USD 52 billion) and the introduction of new instruments to support lending to MSEs, including a zero-interest "funding-for-lending" scheme worth RMB 400 billion (USD 60 billion) to finance 40 percent of local banks' new unsecured loans.

Monetary Authority of Hong Kong

Key measures to provide financial reliefs include the introduction of low-interest loans for SMEs with 100 percent government guarantee valued at HK$70 billion (USD 10 billion) and measures by banks to the extent permitted by their risk management principles, including delay of loan payment, extension of loan tenors, and principal moratoriums for affected SMEs, sectors, and households as appropriate.

Central Bank of Hungary (MNB)

On April 7, an SME lending programme was announced (FGS GO!) to support firms through interest rate subsidy. Subsequently, MNB relaxed the facility's conditions to allow for the use of loans for investment abroad and to broaden the conditions for the borrowing of working capital loans. MNB further raised the amount available under the program to HUF 750 billion (USD 2.5 billion) from HUF 450 billion (USD 1.5 billion) previously. Measures were also taken to provide financial relief to households and corporate borrowers, including the provision of a grace period of repayment of loans to the Growth Funding Facility (subsidized lending to SMEs supported by the MNB), the extension of short-term loans to businesses, and a repayment moratorium on all existing loans, corporate and retail, until the end of this year, with a reprofiling of debt payment thereafter to avoid an increase in monthly payments.

Bank of Russia (CBR)

CBR has introduced temporary regulatory easing for banks intended to help corporate borrowers. Forbearance regarding provisioning for restructured corporate and SME loans will apply to all sectors, not only those affected by COVID-19. The CBR has introduced a RUB 500 billion (USD 6.5 billion) facility for SME lending. This is in addition to the already allocated RUB 150 billion (USD 2 billion) to provide loans to SMEs to support and maintain employment. Another RUB 50 billion (USD 650 million) will be allocated for similar purposes to borrowers who do not have SME status. On April 27, the interest rate on CBR loans aimed at supporting lending to SMEs, including for the urgent need to support and maintain employment, was reduced from 2.5 to 2.25 percent.

2 The selection of case studies is based on a keyword search of the IMF Policy Response to COVID-19 tracker for 'employment', 'salary' and related terms.

2) Support for individuals due to job loss or reduced salary

Central Bank of Bahrain

The central bank is requesting banks to offer a six-month deferral of repayments without interest or penalty and to refrain from blocking customers' accounts if a customer has lost his or her employment.

Central Bank of Malaysia (BNM)

BNM announced that the banking industry will provide a targeted loan payment moratorium extension and provision of repayment flexibility to borrowers affected by COVID-19. Individuals who have lost their jobs in 2020 and have yet to find a job will be offered an extension of the loan moratorium for a further three months by their bank. Furthermore, individuals who are still employed but whose salaries have been affected due to COVID-19 will be offered a reduction in loan instalment in proportion to their salary reduction, depending on the type of financing. In addition, banks have also committed to provide repayment flexibility to other individuals and all SME borrowers affected by COVID-19. In addition, banks have also committed to provide repayment flexibility (e.g. allowing temporary interest-only payments and lengthening the repayment period) to other individuals and all SME borrowers affected by COVID-19.

Bank of Russia (CBR)

The parliament approved a law that guarantees the possibility for affected citizens and SMEs to receive deferrals of loan payments for up to six months and CBR recommended banks to pursue the same approach to retail loan restructuring as stipulated in the law (fast approval or rejection, restructuring from the application date, no penalties during the consideration period).

State Bank of Vietnam (SBV)

The SBV has issued guidelines to commercial banks to reschedule loans, reduce/exempt interest, and provide loan forbearance. As of mid-September, banks have registered a credit package totalling VND 300 trillion (USD 13 billion and about 3.8 percent of GDP) at lower interest rates, and supported 1.1 million customers (with outstanding loans of nearly VND 2,300 trillion (USD 100 billion)) by rescheduling repayment, exempting and reducing interest on existing debts, and extending new loans. Affected firms are eligible to concessional loans from Vietnam Social Policy Bank (VSPB) with no interest for making salary payment to their workers who temporarily stopped working. The total loan value is planned at VND 16.2 trillion (USD 700 million and around 0.2 percent of GDP).

4. Moving Forward: Enabling a Just and Sustainable Recovery

In the COVID-19 crisis, central banks' crisis response interventions have played an important role in mitigating unemployment through general monetary and supervisory easing measures and through more direct support for the SME sector. However, their response has not yet been calibrated to support a sustainable recovery from COVID-19 – one that would accelerate the transition to a net-zero and resilient economy and one that is also inclusive and reduces inequalities.

Central banks recognise the need to 'build back better', but as the INSPIRE Sustainable Crisis Response Toolbox has shown, direct linkages between the economic, the environmental and the employment dimensions are embryonic at best (Dikau et al., 2020). Leading research highlights the value of targeting both fiscal and monetary responses are steered towards a productive and balanced portfolio of investments in people, nature and physical infrastructure (Hepburn et al. 2020).

Currently both, governments and central banks are missing out on the opportunity to utilise the significant size and shaping power of recovery policy packages to build back better and accelerate a just transition to sustainable development. Doing this could also benefit from further monetary-fiscal alignment.

Next steps for central banks could include the following:

- Effective recovery policies will have to address the existing societal and political concerns, including unemployment, poverty alleviation and inequality (Hepburn et al. 2020)

- The current range of SME employment programmes should be extended to offer support for those most vulnerable in the current crisis and investing in environmental upgrading

- All crisis response measures should be aligned with the need to achieve a just transition. A particular focus should be on job creation, skills development and decent work in sustainability-enhancing sectors of the economy, not least as a way of supporting workers and communities in sectors and regions where the crisis is proving disruptive (e.g. oil and gas, aviation, retail).

- Central banks can support the investment by governments in job-creating investments in sustainable infrastructure and nature restoration through sovereign bond purchases and other instruments, thereby addressing immediate unemployment from COVID-19, as well as the long-term structural shifts from accelerated action on climate change and biodiversity.

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