

2.3 Measures to stabilize the financial system and revitalize the economy in major countries

In response to the impact stemming from the financial crisis, many countries have adopted a succession of measures designed to stabilize financial markets and to revitalize the economy via expansionary fiscal policies.

2.3.1 Measures to stabilize the financial system

In an attempt to relieve the credit crunch caused by the US subprime mortgage crisis, a number of central banks cut policy rates to ease credit market strains. On 8 October 2008, the Fed and five leading central banks took a coordinated action to lower interest rates. In addition to conventional interest rate policies, central banks in major countries implemented an array of the so-called non-conventional policies to inject funds into financial markets.

Furthermore, national governments in major countries actively implemented a series of policy measures to enhance the soundness of financial institutions' balance sheets so as to facilitate their on-going operations, including: (1) providing guarantees for deposit and non-deposit debt of financial institutions; (2) strengthening the capital structure of individual financial institutions; and (3) revitalizing financial institutions' assets (Table 2.1).

Table 2.1 Measures to enhance the soundness of financial institutions' balance sheets in selected countries

Measure	Country
1. Guarantees for deposit and non-deposit debt of financial institutions	
(1) Guarantee on deposits	
· Blanket guarantee on deposits	US (non-interest bearing deposits), Germany, Singapore, Hong Kong
· Raise insurance amount on deposits	US (interest bearing deposits), UK, South Korea
(2) Guarantee on non-deposit debts	
· Guarantee on inter-bank call loans	Germany
· Guarantee on bill/bond debts issued by banks	US, UK
2. Strengthen financial institutions' capital structures through stock purchases or direct capital injections.	US, UK, Germany, Switzerland
3. Revitalize financial institutions' assets	
(1) Guarantee on financial institutions' loans or other assets.	US, UK, Japan
(2) Enhance credit guarantee facilities for small and medium enterprises.	US, UK, Japan, South Korea

Source: Official government websites in selected countries.

Meanwhile, the G-7, the IMF and the European Union (EU) undertook large-scale cooperative and coordinated actions. The IMF, in an effort to assist members devastated by the financial crisis, has provided special financing of up to US\$50 billion to Ukraine, Hungary, Iceland, Pakistan, Latvia, Belarus, El Salvador, Serbia and Armenia since November 2008. In February 2009, Japan committed to loan up to US\$100 billion to IMF for supplementing its financial resources, which in turn will assist its members to weather the current global crisis. The April 2009 G-20 summit members also agreed to treble resources available to the IMF to US\$750 billion.

The current financial crisis originated from the US. This, together with the fact that the US and the UK are both key international financial centers and pivotal derivatives market hubs, has led to a more severe impact on the financial markets and financial institutions in these two countries. The following summarizes the main measures undertaken by the governments of these two countries to stabilize their financial systems.

US measures to stabilize the financial system

The Fed has taken an easy monetary policy stance since September 2007. It has cut the federal funds target rate ten times to reach the level of 0.0%~0.25% and used innovative funding facilities⁶ to increase market liquidity. It also signed currency swap agreements with fourteen foreign central banks, including Australia, Brazil, Canada, Denmark, the UK, the EU, Japan, South Korea, Mexico, New Zealand, Norway, Switzerland, Sweden, and Singapore, to mitigate the elevated pressures stemming from financial turbulence in the short-term US dollar funding market. On 18 March 2009, the Fed announced that it would purchase up to US\$750 billion of agency mortgage-backed securities, US\$100 billion of agency debt, and US\$300 billion of long-term treasury securities.

In October 2008, the Fed and the US Treasury coordinated to take the first round of financial relief measures, including the Troubled Asset Relief Program (TARP) and the Temporary Liquidity Guarantee Program (TLGP). The Obama administration in February 2009 announced the second round of relief measures – the Financial Stability Plan (FSP) – due to concerns over the continued occurrence of substantial losses by financial institutions.

⁶ The new funding facilities aim to inject liquidity into financial institutions and specific credit markets, which include Term Auction Facility (TAF), Term Securities Lending Facility (TSLF), Primary Dealer Credit Facility (PDCF), Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility (AMLF), Commercial Paper Funding Facility (CPFF), Money Market Investor Funding Facility (MMIFF) and Term Asset-Backed Securities Loan Facility (TALF).

Troubled Asset Relief Program (TARP)

In mid-September 2008, Lehman Brothers filed for bankruptcy protection, and both Citibank and American International Group (AIG) were in financial distress. In response, the House of Representatives on 3 October 2008, passed the Emergency Economic Stabilization Act of 2008 (EESA), aiming at stabilizing financial markets. Under the Act, the US Treasury was authorized to launch the TARP within the budget limit of US\$700 billion.

The primary focus of the TARP was initially to purchase troubled assets from financial institutions. But difficulties in assessing the value of impaired assets, and concerns over persistent and sizeable losses in some financial institutions, caused the Treasury to set up a voluntary Capital Purchase Program (CPP) as part of the TARP and spend up to \$250 billion to provide direct capital injections into financial institutions. Through this program, the Treasury has injected capital into major institutions such as AIG, Citibank and Bank of America since October 2008.

Temporary Liquidity Guarantee Program (TLGP)

In addition to purchases of stakes in banks through capital injection, the Federal Deposit Insurance Corporation (FDIC), on 14 October 2008, launched the TLGP with intent to strengthen depositors' and investors' confidence. Under the program, the FDIC offers a three-year guarantee for newly-issued senior unsecured debt of eligible institutions on or before 30 June 2009⁷. Furthermore, it also provides a guarantee for non-interest bearing deposit transaction accounts held at FDIC-insured institutions⁸. The deposit guarantee will expire on 31 December 2009.

Financial Stability Plan (FSP)

Due to concerns over deficiencies in the TARP, the Treasury put in place the FSP so as to improve weaknesses in previous relief measures, to strengthen the financial system, to lay the foundation for economic recovery and to support the feeble real estate market. The FSP consists of six major financial initiatives (Table 2.2) with a scale of up to US\$2 trillion to address the troubled assets problem and mitigate credit strains.

⁷ On 17 March 2009, the Board of Directors of the FDIC voted to extend the debt guarantee part of the TLGP from 30 June 2009 through 31 October 2009.

⁸ On 3 October 2008, the FDIC temporarily raised the insurance amount on interest-bearing deposits from US\$100,000 to US\$250,000 per depositor before the implementation of the TLGP.

Table 2.2 US Financial Stability Plan

Item	Measure	Content
1	Financial Stability Trust	<ol style="list-style-type: none"> 1. Requiring major financial institutions to undergo a comprehensive stress test. Firms that fail to pass the assessment are eligible to obtain capital from the Capital Assistance Program (CAP), while any investment made by Treasury under the CAP will be placed in a new entity of the Financial Stability Trust. 2. Increasing transparency and disclosure of exposures on the balance sheets of financial firms.
2	Public-Private Investment Fund	<ol style="list-style-type: none"> 1. On a scale of up to US\$500 billion ~ US\$1 trillion. 2. Putting public and private capital side-by-side to purchase troubled assets, and in turn lead to restoring the financial sector to normal operation. 3. Target: (1) nonperforming loans; (2) troubled asset-backed securities.
3	Consumer and Business Lending Initiative	Expanding the reach of the Term Asset-Backed Securities Loan Facility (TALF), coupled with a bold expansion of its size up to US\$ 1 trillion from US\$200 billion, to enhance the effectiveness of the stimulus for consumer and business lending.
4	Transparency and Accountability Agenda -Including Dividend Limitation	<ol style="list-style-type: none"> 1. All firms that intend to use government funds through the FSP are required to submit a plan of how they strengthen their lending capacity and commit to participate in mortgage foreclosure mitigation programs. 2. All firms that receive new capital assistance are restricted from paying common dividends, repurchasing shares and pursuing acquisition.
5	Affordable Housing Support and Foreclosure Prevention Plan	<ol style="list-style-type: none"> 1. Driving down overall mortgage rates through the Fed's purchase of government-sponsored enterprise (GSE) mortgage-backed securities and GSE debt. 2. Committing US\$50 billion from the TARP to enable monthly payment reductions and loan modifications for distressed mortgage borrowers.
6	A Small Business and Community Lending Initiative	<ol style="list-style-type: none"> 1. Use of the Consumer and Business Lending Initiative to finance AAA- rated Small Business Administration (SBA) loans. 2. Temporarily raising the guarantee for SBA loans to 90%; reducing fees for SBA lending; and less burdensome processing of loan applications.

Source: The US Department of the Treasury.

UK measures to stabilize the financial system

Against the backdrop of the US subprime mortgage crisis spreading to the UK, and with a view to addressing a deterioration in liquidity and asset quality, the Bank of England (BOE) has acted to boost market liquidity by cutting policy rates nine times to 0.5% since December 2007, and by creating an array of new funding facilities⁹.

In addition, for the sake of preventing spillovers from the financial crisis and easing the credit constraints of the banking industry, Her Majesty's Treasury (the Treasury) announced the first round of bailouts in October 2008, including the Bank Recapitalisation Scheme and the Credit Guarantee Scheme (CGS). These relief measures, however, were far from effective as most of the government's funds were still kept in the banking system with the result that they failed to play their role of financial intermediary. Consequently, in January 2009, the Treasury launched the second round of relief measures, which included the Asset Purchase Facility (APF), the Asset Protection Scheme (APS), and extending the CGS application period and expanding its scope of guarantee.

Bank Recapitalisation Scheme

On 8 October 2008, the Treasury introduced the Bank Recapitalisation Scheme requiring eight major financial institutions to have a buffer of capital above the minimum requirement. A recapitalisation fund worth £50 billion will be used by the Treasury to inject capital into those large firms unable to raise required funds from the market. On 13 October 2008, the Treasury announced that it would spend £37 billion to make capital investments in the Royal Bank of Scotland (RBS), Lloyds TSB and HBOS through purchases of common shares and preferred shares. In November 2008, the UK government announced the establishment of UK Financial Investments Limited (UKFI) designed to manage all the government's share holdings in banks to safeguard the interests of taxpayers.

Credit Guarantee Scheme (CGS)

In addition to capital injections through purchases of shares, and in order to restore public and investor confidence in banks, the Treasury further announced on 13 October 2008, that it would implement the CGS, which aims to expand the coverage of debt guarantees from deposit debts (£50,000 per bank per depositor) to non-deposit debts (such as certificates of

⁹ The measures include the Special Liquidity Scheme (SLS) allowing banks to temporarily swap their high quality but illiquid mortgage-backed and other securities for UK treasury bills from the Bank of England with the aim of improving banks' liquidity positions. This scheme expired on 30 January 2009, and was replaced by the Discount Window Facility and Asset Purchasing Facility (APF).

deposit and commercial paper), to ensure that banks have sufficient funds to maintain normal lending operations. On 15 December 2008, the Treasury announced an extension of the guarantee period under the CGS to being effective from April 2012 until April 2014.

Asset Purchase Facility (APF)

The BOE was authorized by the Treasury to purchase a range of high quality government bonds and private sector assets through the implementation of the APF, with the aim of increasing the money supply and relieving the strain in capital markets. The losses incurred on the BOE's operation of the APF, wherever possible, will be subsidized by the Treasury.

Asset Protection Scheme (APS)

The Treasury launched the Asset Protection Scheme to provide protection against losses on banks' eligible troubled assets with the intent to make financial institutions more willing to lend and continue their normal lending operations. A fixed proportion of losses, incurred on future loss events related to protected assets, will remain with banks and the government will cover 90% of the remaining losses.

Extending application period for CGS and widening its scope of guarantees

In the face of tightening credit conditions in banks, the Treasury promulgated to extend the application period for the CGS to 31 December 2009, from 9 April 2009, and widen the reach of credit guarantees to AAA- rated asset-backed securities, with a view to reinforcing the scheme.

2.3.2 Measures to revitalize the economy

The IMF, in response to spillovers from the financial crisis to the real economy, appealed to national governments to undertake vigorous fiscal policies to bolster weakening aggregate demand. Since 2008, the US, UK and major Asian countries have actively implemented expansionary fiscal policies and launched a variety of macroeconomic stimulus packages, including: (1) offering tax cuts or tax rebates to stimulate private consumption; (2) expanding public expenditures; (3) promoting employment; and (4) supporting the housing market. The scale of these packages exceeds 2% of GDP in their corresponding countries (Table 2.3).

The US

In addition to tax cuts of up to US\$100~150 billion in the Emergency Economic Stabilization Act of 2008, President Barack Obama signed the 2009 American Recovery and Reinvestment Bill into law on 17 February 2009, with measures included in the bill worth US\$787.2 billion, or 5.5% of GDP. The bill mainly consists of public expenditure, tax relief and protection of the vulnerable, with shares of 39.2%, 36.6% and 24.2%, respectively.

Other Countries

Since September 2008, the UK government has carried out a series of stimulus measures, including Homeowners Support Package (£1 billion), Economic Stimulus Package (£20 billion), and Infrastructure Plan (£10 billion). Meanwhile, some advanced countries (e.g. Japan and Germany) and emerging Asian countries (e.g. China, South Korea, and Singapore) have also successively introduced wide-ranging economic stimulus plans in an effort to boost domestic economic growth.

Table 2.3 Economic stimulus in selected countries

Country	Measure	Release date	Amount	Total amount to GDP (%)		Time frame	Content
US	The American Recovery and Reinvestment Act of 2009	2009/2	US\$787.2 billion	5.54	(5.5)	2 years	The act will spend up to: (1) US\$308.5 billion, or 39% of total funds, in public expenditure, infrastructure, science and education; (2) US\$288.3 billion, or 37% of total funds, for providing tax cuts to individuals and corporations; and (3) US\$190.4 billion, or 24% of total funds, for direct payment in individual, household and medical insurance.
	National Service Bill	2009/3	US\$5.7 billion		(0.04)	5 years	To provide a US\$5.7 billion fund within five years for: (1) helping the poor; (2) improving education; (3) promoting energy efficiency; (4) enhancing health care; and (5) looking after veterans.
UK	Homeowners Support Package	2008/9	£ 1 billion	2.2	(0.1)	1 year	Includes: (1) reducing the thresholds of housing tax breaks; (2) offering interest-free mortgages for first-time, low-income home buyers; and (3) offering a “sale and rent back” option for those who can not sustain their mortgages.
	Economic Stimulus Package	2008/11	£ 20 billion		(1.4)	2 years	Includes: (1) tax cuts; (2) assistance for low-income families; and (3) expansion of public expenditure.
	Private Finance Initiative Infrastructure Project	2009/1	£ 10 billion		(0.7)	2 years	Includes: (1) rebuilding or refurbishing thousands of national schools in different levels and in turn to create 100,000 job opportunities for the construction industry; (2) deploying environmentally-friendly infrastructure, including renewing rail networks and increasing investment in environmentally-friendly industries; and (3) making a wide range of investments in optical fiber networks.
Germany	The first economic stimulus plan	2008/11	€ 32 billion	3.4	(1.3)	2 years	Includes: (1) providing tax exemptions for car buyers; (2) subsidizing the refurbishment of home appliances aiming to promote energy efficiency; (3) financing to SMEs; and (4) implementing public infrastructure construction.

Country	Measure	Release date	Amount	Total amount to GDP (%)		Time frame	Content
	The second economic stimulus plan	2009/1	€ 50 billion		(2.1)	2 years	The package focuses on public infrastructure. It also includes: (1) tax cuts; (2) reducing health insurance premiums; and (3) offering special support to car manufacturers.
Japan	Comprehensive immediate policy package	2008/8	¥2 trillion	5.3	(0.3)	2 years	Includes: (1) lessening the medical burden of the elderly; (2) supporting the working capital of SMEs; and (3) establishing disaster contingency plans.
	Measures to support people's daily lives	2008/10	¥5.9 trillion		(1.2)	2 years	Includes: (1) providing households with fixed-sum benefits; (2) reinforced measures for non-regular employees; (3) supporting nursing for children and the elderly; (4) reducing the highway toll; and (5) providing tax incentives for enterprises to encourage investment in energy-saving and new energy equipment.
	Immediate policy package to safeguard people's daily lives	2008/12	¥4 trillion		(0.8)	2 years	Includes measures to: (1) support employment; (2) pursue tax reform; and (3) support people's daily lives.
	Policy package to address economic crisis	2009/4	¥15.4 trillion		(3.0)	1 year	Includes: (1) establishing a social safety net for dispatched workers; (2) supporting financing for enterprises; (3) promoting solar power generation; (4) improving medical services; and (5) assisting local governments to develop regional economies.
China	Measures to increase domestic demand and stimulate economic growth	2008/11	RMB 4 trillion	12.0		2 years	Includes: (1) expanding low-income housing; (2) improving rural infrastructure; (3) reinforcing major infrastructure for railways, highways and airports; (4) enhancing health, culture and education; (5) improving ecological environment; (6) pursuing science and technology innovation, and industrial structure adjustment; and (7) pushing post-earthquake rebuilding.
South Korea	Economic stimulus package	2008/11	14 trillion won	10.1	(1.5)	1 year	Includes: (1) revitalizing local economies; (2) promoting industrial investment through tax preference and regulatory reform; (3) animating the housing market; and (4) assisting SMEs and low-income families.

Country	Measure	Release date	Amount	Total amount to GDP (%)	Time frame	Content	
	Green economic stimulus package	2009/1	50 trillion won		(5.6)	4 years	To create new jobs through the development of the green business sector, such as energy-saving industry, low carbon transport and green building.
	Supplementary budget for job creation	2009/3	28.9 trillion won		(3.0)	1 year	Includes: (1) creating employment opportunities; (2) supporting SMEs; (3) revitalizing local economies; (4) developing potential industries; and (5) supporting the livelihoods of low-income families.
Singapore	Growth dividends and GST subsidy	2008/11	S\$5.06 billion	10.1	(2.1)	5 years	Includes: (1) dispensing additional growth dividends of up to S\$1.06 billion to Singaporean citizens, while low-income families will receive more; and (2) providing S\$4 billion for the subsidy of the goods and services tax (GST) over five years.
	Resilience Package	2009/1	S\$20.5 billion		(8.0)	2 years	Includes: (1) offering job training and preventing unemployment; (2) providing loans by banks; (3) providing subsidies and preferential taxes for corporations; (4) supporting households; and (5) investing in infrastructural construction, education, and medical and health care.

Sources: IMF, World Bank and official websites in selected countries.