United States

State of emergency

The American people and the US economy will no longer be spared the coronavirus pandemic, no more than any other country. Arriving belatedly on US soil and long belittled by President Trump, the virus is now spreading rampantly, to the point that WHO is now preparing to declare the United States the pandemic's new epicentre. With its federal structure, the US has taken a scattered approach, leaving each state to decide whether or not to introduce lockdown measures. Although the White House has closed the country's borders (to the European Union and Canada, among others), it was reluctant to restrict domestic movements of goods and people. Foreseeing recession, the markets have plunged and the central bank has launched a veritable monetary "Marshall Plan".

On 12 March 2020, the tone in Washington was serene even as Italy, already swamped by the epidemic, was strengthening its lockdown measures and former Prime Minister Matteo Renzi was urging Europe to do the same. President Trump was convinced that a vaccine would be rapidly discovered and the virus would disappear quickly, with little propagation[1]. To the contrary, the situation has deteriorated rapidly, to the point that the World Health Organisation (WHO) is preparing to declare the US as the pandemic's new epicentre. As we went to press, the world's number one superpower had reported 280,000 confirmed cases and 7,000 deaths. Covid-19 contamination is progressing exponentially, comparable to the curves already seen in European affected countries.

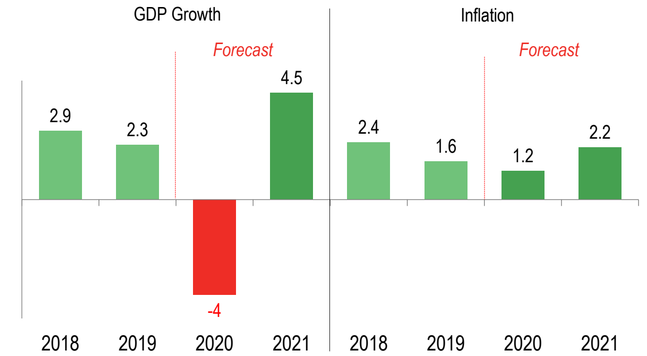
With its federal structure, the US has taken a scattered approach to the pandemic. Since 15 March, the hardest hit states (New York and California) have imposed lockdown measures or social distancing on their residents, limiting the movements of non-essential workers and closing most recreational spaces (bars, restaurants, theatres, sports facilities, etc.) and retail stores. Other states, such as New Jersey, Illinois, Florida and Texas, have followed suit with more or less severity. Despite the President's hopes of seeing "all the churches packing their pews again by Easter", measures have been taken at the local level to protect residents, and only a very small list of places have put no restrictions into place of any kind. The US economy is freezing up. Industrial orders as depicted by the Investment Supply Manager (ISM) index – that is closely correlated with investment and economic activity – fell to 42.2 in March, the lowest level since 2009, and will continue to fall, raising the spectre of a record-breaking contraction of GDP in Q2 2020.

High-risk populations and massive fiscal support

Although the US has a leading-edge healthcare system, it is not well equipped to handle a mass epidemic. The highly-selective system is costly – the US devotes 17 points of GDP to healthcare, the highest among the OECD countries – but its hospital capacity is limited to only 2.8 beds per 1000 inhabitants, two times less than in France and three times less than in Germany. Without universal healthcare coverage, the system provides only limited access to those with no

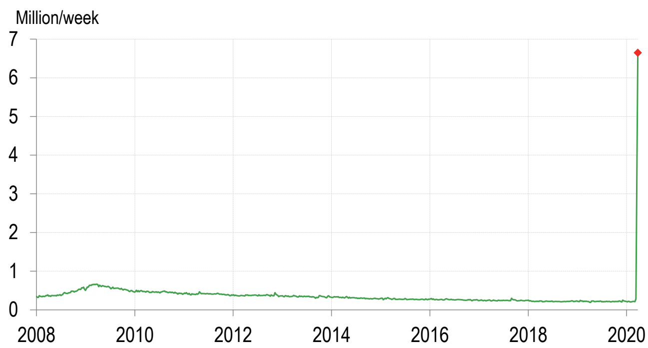
[1] *"It's going to go away […] because of what I did and what the administration did with China, we have 32 deaths at this point. When you look at the kind of numbers that you're seeing coming out of other countries, it's pretty amazing when you think of it". D. J. Trump, 24 February 2020.*

1- Growth and inflation
(Y/Y, %)



Source: BNPP, Interim Forecasts (Before Global Markets updated scenario)

2- Initial claims



Source: US Department of Commerce

3- Coronavirus Aid, Relief, and Economic Security Act (USD mds)

Cash grant to households	**634**
- Tax credit ("checks")	290
- Unemployed (benefits extension)	260
- Various (food stamp, education aid…)	84
Guaranteed Loans	**881**
- Large companies and States	504
- Small and medium size companies	377
Emergency transfers	**400**
- States and local authorities	175
- Hospitals	180
- Disaster Relief Fund	45
Corporate tax cuts and deferred payments	**280**
TOTAL	**2,200**

Source: Committee for a Responsible Federal Budget, BNP Paribas private insurance – i.e. nearly 106 million Americans (1 in 3)[2]. More often than not, health care protection is provided through jobs, and the surge in unemployment (see chart 2) will only increase the population's vulnerability in the face of the pandemic.

Finally aware of the stakes at hand, the Trump administration pushed Congress to pass the Coronavirus Aid, Relief, and Economic Security Act (CARES), an unprecedentedly large fiscal stimulus package (USD 2,200 bn, the equivalent to 10% of GDP or 50% of the annual Federal budget). The bill doubled in size under pressure from the Democrats, who have a majority in the House, to cover the needs of low-income individuals and those who have lost their jobs. In addition to guaranteed loans for companies, which could amount to as much as USD 900 bn, the Federal government will transfer roughly USD 630 bn to American households (see table 3) through tax credits or extended benefits. Using a means-tested system[3], each American household will receive a check from the Treasury for a maximum amount of USD 3,000 each. The Federal government will also top up unemployment benefits, which vary from state to state but which average roughly USD 300 a week, by USD 600 a week during the 4-month period ending 31 July 2020.

Monetary bazooka

The government is preparing to buffer an economic shock which it can no longer deny, and which has been largely foreseen by the markets and the Fed. Starting on 3 March, the Fed began cutting its key rates, slashing them to virtually zero on 15 March[4]. It reactivated the exceptional liquidity facilities that were set up during the 2008 financial crisis. Quantitative easing, the Fed's securities purchasing programme, which had been raised to a maximum of USD 700 bn a year, is now being conducted with virtually no limits (see box 4). These actions, coupled with swap arrangements and concerted actions with other central banks, have helped restore some calm, at least temporarily, in the foreign exchange and bond markets, where the squeeze on USD liquidity has led many currencies to depreciate, and interest rate spreads have widened sharply.

Jean-Luc Proutat
Jean-luc.proutat@bnpparibas.com

4- Monetary Marshall Plan

In the US, reassessment of the risk associated with the prospects of an economic contraction have resulted in a widespread flight to liquidity and requests to convert assets (equities, bonds and shares in mutual funds) into cash, putting enormous pressure on key players for the smooth functioning of the markets, including primary dealers and money market funds. To avoid systemic sclerosis, the Fed re-opened the facilities created during the 2008 financial crisis and positioned itself as the "buyer of last resort" for nearly unlimited amounts.

*- **A series of special financing facilities**. Alongside the exceptional injection of liquidity via repo operations (up to USD 5800 bn from mid-March to mid-April), on 17-18 March the Fed reactivated its Primary Dealer Credit Facility (PDCF) and Money Market Mutual Fund Liquidity Facility (MMLF). Through these facilities, the Fed lends funds in exchange for collateral that has become harder to dispose of and seeks to facilitate debt market refinancing, a vital organ of the economy. But it does not stop there. Through Special Purpose Vehicles (SPV), the Fed will purchase high quality corporate bonds (i.e. with an investment grade rating), not only in the primary market via the Primary Market Corporate Credit Facility (PMCCF) but also in the secondary market via the Secondary Market Corporate Credit Facility, (SMCCF). Using an SPV, it has also reactivated the Term Asset-Backed Securities Loan Facility (TALF) to support the securitisation of new loans to households and small businesses (and prevent it from shutting down).*

*- **Switch to unlimited QE.** This is the most spectacular measure announced so far, and the first to begin to restore calm in the markets. On 23 March, the Fed announced that its securities holdings via the System Open Market Account (SOMA) will be increased by as much as needed to ensure the smooth functioning of the markets. In other words, quantitative easing (QE) would only be limited by the amount of eligible Treasuries outstanding (which are also about to increase sharply) and Mortgage-Backed Securities (MBS), which were expanded to include commercial mortgage-backed securities.*

*- **Swap arrangements.** The squeeze on USD liquidity required central bank action not only because of the situation in the United States. Like in 2008, debt issued in the US, especially corporate bonds, have been recycled globally, especially in the form of exchange-traded funds (ETF), increasing the US dollar refinancing needs of non-American financial intermediaries. In Japan, the eurozone and the UK, the first signs of dollar rarefication appeared with the depreciation of their currencies (demand for USD conversion) and an increase in the cost of swaps. In response, the Fed and five central banks – the ECB (eurozone), BoE (UK)), BoJ (Japan), BNS (Switzerland) and BoC (Canada) – reached an agreement on 15 March allowing currencies to be swapped at a reduced rate (OIS + 25 bp), with USD lending in each jurisdiction of up to 85 days (in addition to the usual 7-day operations). On 19 March, the Fed extended these swap arrangements to include other key central banks around the globe (Australia, New Zealand, Brazil, South Korea, Mexico, Singapore, Sweden, Norway and Denmark, among others).*

Source: BNP Paribas

[2] Of the 106 million Americans without access to private insurance, 78.4 million depend on Medicare (for persons over age 65) and Medicaid (for low-income individuals or families), which provide only partial coverage. 27 million Americans do not have any insurance coverage at all. See Census Bureau, Health Insurance Coverage in the United States: 2018, November 2019.

[3] Revenue of up to USD 99,000 a year for singles, USD 198,000 a year for a couple without children and USD 218,000 a year for a couple with children.

[4] On 15 March 2020 (effective 16 March), the Federal Open Market Committee (FOMC) decided to cut the key fed funds target rate by 100 basis points, to a range of between 0% and 0.25%. The interest on reserves and excess reserves (IOR and IOER) was cut by 150 bp to 0.1%.