HM Treasury

UK experiences on Balance sheet review: Fiscal Response to COVID19

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Why the UK is carrying out a balance sheet review?

Balance sheet increasingly used for microeconomic policy interventions (loans, guarantees)

- Increases fiscal risk for government and size of the balance sheet in order to borrow to invest

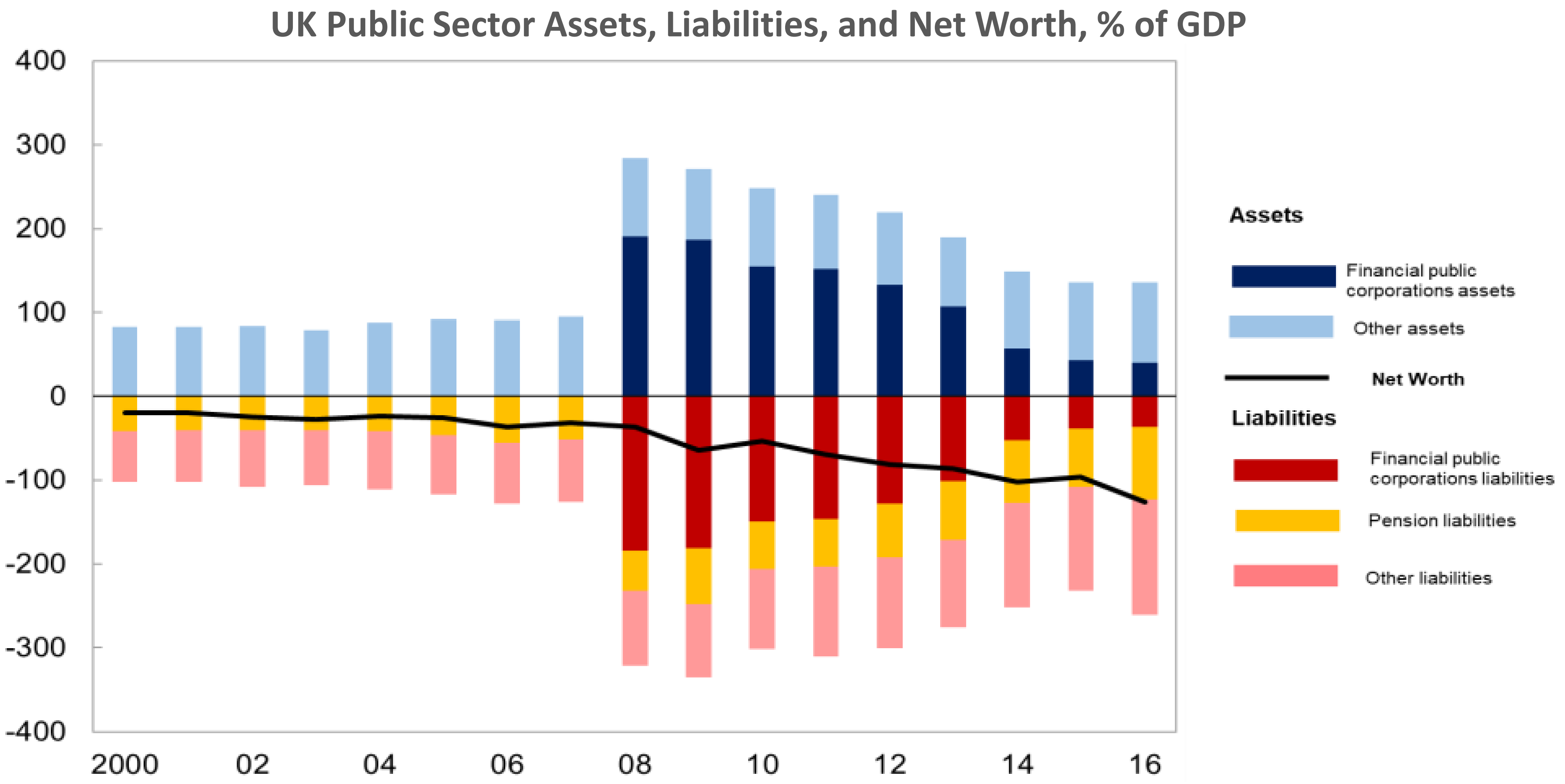
Increasing focus on balance sheet in managing the public finances

- Is net worth strengthening or weakening?
- Opportunity to consider management of assets and liabilities and strengthen long-run fiscal sustainability

Good data now available

- Whole of Government Accounts (WGA) provides comprehensive data on assets and liabilities across the public sector and clearer data on ownership
- Increasing use of this data by independent bodies to scrutinise government policy

Context: the nature of the UK's balance sheet changed substantially since the 2008/2009 Global Financial Crisis



Source: IMF with Whole of Government Accounts data, to notice the UK Office for National Statics does also publish data on the balance sheet, statement of operations and statement of other economic flows for public sector compliant with the Government Finance Statistics Manual 2014, see online at: https://www.ons.gov.uk/economy/governmentpublicsectorandtaxes/publicsectorfinance/datasets/internationalmonetaryfundsgovernmentfinancestatisticsframeworkinthepublicsectorfinancesappendixe

We have provided unprecedent support to the economy which has impacted our finances, however the cost of inaction would have been higher

Our economic response to covid19

- The first phase of our economic response has seen us taken unprecedented steps to support the economy through the crisis; keep as many people as possible in their existing jobs, support viable businesses to stay afloat and protect the incomes of the most vulnerable.
- These measures aim to protect the productive capacity of our economy and to enable a strong and sustainable recovery from this crisis.

Impact on our finances

- The Office for Budget Responsibility has estimated that the direct cost to government of the response to Coronavirus will be above £120 billion in 2020-21.
- On top of this, substantial support in the form of guarantees and loans has been made available. The total exposure of covid19 contingent liabilities schemes is over £300bn[1]. According to Office for Budget Responsibility loans guarantees expected losses in 20/21 are £5bn[2].

Recovery targeted response

- Not taking these steps would result in the temporary effects of the Covid-19 virus leaving permanent scars in our economy. Although we are spending unprecedented amounts, the consensus both in the government and among external economists is that not spending at these levels would cause even more damage.

1 OECD, Coronavirus country policy tracker. See online at: https://www.oecd.org/coronavirus/country-policy-tracker/
2 OBR, Coronavirus analysis. See online at: https://obr.uk/coronavirus-analysis/

We are improving our understanding of the data and analytical and institutional capabilities

Schemes data collection and publication

- The policy teams are establishing **regular reporting on exposures and take-up** via the UK development bank for SMEs financing, the UK central bank, private lenders and others
- While this was difficult at the beginning because of the pace with which schemes were created, policy teams were able to create innovative and timely approach to meeting our immediate data needs, now **regular reporting to the UK Treasury has been formalised and is now been implemented**
- The UK central bank, UK Treasury and other ministries publish statistics on coronavirus support for business and individuals on a regular basis[1]
- The Office for Budget Responsibility publishes and updates regularly their coronavirus analysis[2]

Analytical and institutional capability and expertise

- Individual bodies can perform stress-testing on their contingent liabilities
- We are **building the capability to perform portfolio risk assessment and stress-testing** on the UK portfolio in collaboration with actuaries and credit risk experts.
- We are increasing the expertise to manage and invest in equity.
- At a central level we are starting to collate:
  - Sector/industry size/firm level credit default data analysis
  - Technical/advisory support on credit risk analysis

1 Gov.uk, Statistics on coronavirus support for business and individuals. See online at: https://www.gov.uk/government/collections/statistics-on-coronavirus-funding-for-business
2 OBR, Coronavirus analysis. See online at: https://obr.uk/coronavirus-analysis/

In the medium to long run there is a need to create the right environment to manage an expanded balance sheet

How do we ensure interventions are value for money for taxpayers?

- Interventions should be value for money (vfm) for the taxpayers in the long run
- To ensure vfm we might need to impose conditions or constraints for accessing support
- Interventions that support economic growth are good for the balance sheet

What are the risks of an extended balance sheet?

- Interventions will increase debt
- The increase in less conventional assets and liabilities might make the balance sheet more volatile and impact fiscal metrics
- Schemes conditions might results in the classification of businesses into the public sector balance sheet and on national statistics

How should we mitigate this risk via our fiscal policy?

- The fiscal framework could reflect on the expanded balance sheet impacts
- Fiscal risks associated with these loans and the businesses we lend to are in scope for the UK Treasury fiscal risk function to consider