real GDP, according to forecasters, will likely be closer to 2.5%, or about $500 billion. “In an aggregate sense, there are considerable resources pledged to combat the crisis, which should continue to be helpful in 2021,” he said.

He also noted that the fiscal response drove personal income up to an all-time high in the second quarter, which is the opposite of what normally happens in a recession.

Adapting to the Pandemic
Adaptation to the new mortality risk has been much faster than initially expected so far, and macroeconomic outcomes have been considerably better than originally expected, Bullard said.

“This outcome has been supported by exceptionally effective monetary and fiscal policies,” he said. “Despite this success, downside risk remains substantial, and continued execution of a granular, risk-based health policy will be critical in the months ahead.”

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- **November 10, 2020**. Article. "Monetary Policy and Fiscal Policy Responses to the COVID-19 Crisis," Federal Reserve Bank of St. Louis *Regional Economist*, Fourth Quarter 2020.

Monetary Policy and Fiscal Policy Responses to the COVID-19 Crisis

The COVID-19 health crisis has been a substantial shock to the U.S. economy, with the negative economic impact mostly concentrated, thus far, in March and April. The Fed’s monetary policy response and the fiscal policy response during the initial phase of the current crisis were swift and significant. In my view, these policies were successful in helping many parts of the nation’s economy respond effectively to the first wave of the pandemic.

Monetary Policy Response

During the early part of the crisis in the U.S., particularly in March, financial market stress rose dramatically. For the week ending March 20, the [St. Louis Fed Financial Stress Index](https://fred.stlouisfed.org/series/stlfsi2)reached its highest level observed since December 2008, which was in the midst of the financial crisis. Even the U.S. Treasury market, which is considered the deepest and most liquid market in the world, showed signs of stress and was somewhat illiquid in March 2020.

The Federal Open Market Committee (FOMC) convened on Sunday, March 15—two days before a regularly scheduled meeting—and took action, much like it has done in many past emergencies and other particularly difficult situations. That it wasn't willing to wait two days for its regularly scheduled meeting illustrates both its sense of urgency and recognition of how quickly conditions can change in a pandemic.

At the meeting, the FOMC reduced the target range for the federal funds rate to near zero. The FOMC also discussed other types of interventions that could be done, including emergency lending and purchases of different kinds of assets. These interventions were subsequently undertaken by the Board of Governors and the Treasury Secretary.More information about [these 13(3) facilities](https://www.federalreserve.gov/funding-credit-liquidity-and-loan-facilities.htm)can be found on the Federal Reserve Board of Governors website.

Some of these emergency funding programs—authorized under Section 13(3) of the Federal Reserve Act—went beyond what was done during the financial crisis of 2007-09. The Fed programs initiated during the pandemic were designed to provide backstop funding to a wide variety of markets, including the corporate bond market, which was not included in 13(3) programs during the financial crisis. Providing backstop funding for these markets reassures investors that the Fed will be a participant of last resort, albeit at prices that would not be all that attractive in ordinary times. But having these programs in place ensures trading occurs in these markets, thereby preventing them from freezing up entirely.

The backstop lending programs were successful in stemming an incipient financial crisis during the March-April time frame. Levels of financial stress have declined and are now back to pre-pandemic levels observed in January and February 2020.

Fiscal Policy Response

In March 2020, given the emerging pandemic public health crisis and accompanying national, state and local guidance, high-contact businesses and industries began temporary closures and other businesses sent employees to work remotely. This was a collective investment in public health, and in such situations the appropriate policy is to compensate those who are most disrupted.

As such, U.S. fiscal policy was designed to keep people whole and make sure they would be able to pay their bills as the country was trying to get the pandemic under control. Some of the ways households and businesses were compensated included:

- Supplemental unemployment insurance benefits
- Pandemic unemployment assistance for workers who would not be eligible for unemployment insurance under normal programs, such as independent contractors, self-employed workers and gig economy workers
- The Paycheck Protection Program, which provided forgivable loans to small businesses

Between the Coronavirus Aid, Relief, and Economic Security (CARES) Act and other legislation, Congress authorized borrowing more than $3 trillion. The total value was equivalent to about 14.5% of U.S. GDP in the fourth quarter of 2019. Thus, the fiscal package during the current crisis has been substantial and much larger than the fiscal package enacted in 2009.

One piece of evidence that the fiscal response was successful is that personal income increased in the second quarter of 2020—the opposite of what normally occurs during a recession. Even though the U.S. economy experienced its biggest contraction on record, with real GDP declining by 31.4% at an annual rate, personal income rose during this period because the government borrowed money and gave it to businesses and households that were disrupted.

While this process has been understandably uneven, the spirit of the intervention was to move quickly and to try to get people the compensation they would need to pay bills and maintain their lifestyles during this period.

Adapting to the COVID-19 Risk

Since the initial phase of the pandemic crisis, we have learned more about the disease, and households and businesses have been adapting to the new mortality risk in the economy. Many companies have been able to reestablish their businesses and revenue streams by adopting measures to keep their customers and workers safe, much as we saw during the second quarter with essential retail services. Thus, while a need for support still remains, the need is reduced from what it was before because some people have been able to get back into the workplace and some businesses have been able to continue to produce.

Of course, downside risks to the economy remain, and the crisis could take unexpected twists and turns. But so far, the monetary policy and fiscal policy responses to the pandemic have been very effective—a financial crisis during the initial shock was avoided, and the U.S. economy has responded very well to the policy actions that were taken.

For instance, while the unemployment rate remains elevated, it has been declining at a faster pace than in the previous recovery, driven by the spike and subsequent decline in temporary layoffs. In addition, after such a large decline in the second quarter, real GDP increased by 33.1% at an annual rate in the third quarter of 2020, according to the initial estimate from the U.S. Bureau of Economic Analysis. That growth rate is substantially better than what forecasters initially expected in the March-April time frame. In that sense, the recovery has been better than what people dared hope for in the beginning of this crisis.

Endnote

1. More information about [these 13(3) facilities](https://www.federalreserve.gov/funding-credit-liquidity-and-loan-facilities.htm)can be found on the Federal Reserve Board of Governors

website.

The Regional Economist offers insights on regional, national and international issues. Views expressed are not necessarily those of the St. Louis Fed or Federal Reserve System.

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- **October 21, 2020**. Remarks. Bullard Discusses U.S. Economy, Policy, Inflation during Virtual Event, Federal Home Loan Bank of Des Moines Leadership Summit.

  Bullard Discusses U.S. Economy, Policy, Inflation during Virtual Event

  October 21, 2020

  St. Louis Fed President James Bullard discussed a variety of topics related to the U.S. economy during a virtual fireside chat at the Federal Home Loan Bank of Des Moines Leadership Summit.

  Bullard shared his views on the monetary and fiscal policy responses to the COVID-19 crisis; improvements in health outcomes and economic outcomes since March and April; and expectations for strong GDP growth in the third quarter and for above-trend growth in the following two quarters.

  He also discussed various aspects of inflation, including what the FOMC's move to flexible average inflation targeting means for monetary policy; factors that suggest inflation may move somewhat higher in the quarters and years ahead; and the measures of inflation that he prefers to follow.

  Other topics that Bullard talked about include asset bubbles, the labor market, wealth and income inequality, federal debt, and digital currencies.

- **October 16, 2020**. Panel Discussion. Bullard Discusses Fed's Monetary Policy Framework during Virtual Panel, Reinventing Bretton Woods Committee Panel Series.