Investment Insights

A Bridge to Recovery

The U.S. Federal Reserve and Congress are taking swift actions to provide liquidity and assurance to the markets amid the current COVID-19 crisis. Unlike during the Financial Crisis in 2008-2009 where monetary and fiscal responses were slow, and often underwhelming, the Federal Reserve has taken broad and aggressive monetary actions with interest rate policy and direct injections of liquidity into the capital markets, and Congress has passed a broad fiscal stimulus package worth more than $2 trillion.

The economic and financial impact from the spread of COVID-19 are unlike anything we have seen. Global and domestic economies are being brought to a screeching halt as governments respond to the virus by effectively shutting down economic activity. These steps are the proper response to the pandemic at this juncture, however, they are having a negative impact on the economy in the near term. These actions will result in a shorter impact from the virus, meaning economies can reach a recovery phase more quickly.

The quick response from monetary and fiscal authorities will not allow us to avoid an economic slowdown, but it will be an important part of providing the proper environment for the U.S. economy to rebound as the spread of COVID-19 slows and then subsides. We need to be ready for some abysmal economic numbers over the next few weeks. Jobless claims will rise exponentially and the overall unemployment rate will increase significantly. Measures of economic activity, including GDP, are expected to decline precipitously. The silver lining inside all of this negativity is the knowledge that we are taking the actions now to manage the virus, which will allow the economy to begin expanding again sooner.

Fiscal Stimulus Plan

The $2 trillion stimulus package from Congress includes components to support areas most impacted by the pandemic and the actions required to mitigate the spread of the virus. These components and the approximate corresponding funding are outlined below.

Households **$500 billion**	Tax refunds: $250 billion Expanded unemployment insurance: $250 billion Expands unemployment benefits to 39 weeks and includes an additional $600 per week in unemployment benefits for 4 months. $1,200 in direct payments (additional $500 per child) for those with incomes up to $75,000; phased out entirely for those with incomes above $99,000.
Small Businesses **$367 billion**	Small Business Lending/Grants: $350 billion Community Lending: $17 billion

Corporate Lending Facility **$500 billion**	$500 billion fund, including $425 billion for loans to the Fed and $75 billion for industry loans. Will include oversight from an inspector general and a congressionally appointed 5-person panel. Companies that receive government aid must agree to halt stock buybacks for the entire time they receive the aid, plus one year. Also includes restrictions on employment cuts.
Special Purpose Vehicle (SPV) Lending Facility **$425 billion**	Treasury funds for corporate loans, Fed purchases of municipals & corporate bonds and secondary mortgage market. The Fed will leverage this money at about 10-1, making actual liquidity of over $4 trillion dollars available.
Distressed Grants/Loans **$75 billion**	Oversight by a 5-member board, with funding as follows: Airlines $50 billion Air Cargo $8 billion "National Defense" Boeing $17 billion
Corporate Tax Changes **$100 billion**	Net operating loss (NOL) 5-year carryback Interest deduction at 50% of EBITDA Employee Retention Tax Credit
Healthcare Response **$150 Billion**	Hospitals: $100 billion
Aid to State/Local Governments **$150 billion**	Expanded unemployment eligibility and payments
Education **$30 billion**	Student Loan deferrals

Fed's Policy Move

The Federal Reserve has also taken significant measures to provide liquidity and normal functioning to the markets. Each funding facility is outlined below.

Unlimited Treasury and MBS Purchases	*Supports normal market functioning and transmission of monetary policy.* The Central Bank will purchase Treasuries and agency mortgage-backed securities in the amounts needed to support smooth market functioning and effective transmission of monetary policy to broader financial conditions and the economy. In addition, the FOMC will include purchases of agency commercial mortgage-backed securities in its agency mortgage-backed security purchases.
Money Market Mutual Fund Liquidity Facility	*Provides liquidity to money market funds.* This facility allows the Fed to lend to eligible financial institutions to purchase money market assets from money market funds (prime, single state, or other tax exempt money market funds) that are trying to sell to meet redemptions.

(continued)	Collateral that is eligible for pledge includes U.S. Treasuries, guaranteed Agency securities, securities issued by U.S. government-sponsored entities; as well as commercial paper, U.S. municipal short-term debt, and variable rate demand notes (VRDNs), with some restrictions. This facility opened on 3/23/20 and will close on 9/30/20, with $10 billion funding from the Treasury to the Fed to leverage purchases.
Commercial Paper Funding Facility	*Provides backstop short-term funding for high-quality corporate issuers.* The CPFF is a credit facility to a special purpose vehicle (SPV) that will serve as a funding backstop to facilitate the issuance of term commercial paper by eligible issuers. The Treasury has committed a $10 billion equity investment in the SPV. The SPV will purchase from three-month U.S. dollar-denominated commercial paper through the New York Fed's primary dealers. Eligible issuers are U.S. issuers of commercial paper, including municipal issuers and U.S. issuers with a foreign parent company. The SPV will cease purchasing commercial paper on March 17, 2021, unless the Board extends the facility.
Primary Dealer Credit Facility	*Provides overnight and term loans with maturities up to 90 days.* This facility will provide recourse loans to primary dealers in exchange for a broad range of collateral for funding with maturities up to 90 days. It is intended to support the credit needs of households and businesses by expanding the ability of primary dealers to gain access to term funding. In contrast to the facilities of similar nature in 2008 and 2010, this facility will provide term loans (up to 90 days), versus only overnight loans during the financial crisis. This facility is only available to primary dealers, who will pay the discount rate at the time of the loan, regardless of loan maturity date. Eligible collateral includes a broad range of investment grade debt securities, including commercial paper and municipal bonds, and a broad range of equity securities. The PDCF will remain available to primary dealers for at least six months, or longer if conditions warrant.
Primary Market Corporate Credit Facility	*Supports corporate credit markets through backstop funding for high-quality debt of eligible U.S. companies.* This facility will serve as a funding backstop for corporate debt issued by eligible issuers that can be used to buy new issue corporate debt if primary markets are not willing or capable of accommodating this supply. Under the facility, the New York Fed will lend to a special purpose vehicle (SPV) that will purchase qualified bonds directly from eligible issuers and provide loans to eligible issuers. Eligible issuers are companies headquartered in the U.S. and with material operations in the U.S. This facility opened on 3/23/20 and will close on 9/30/20, with $10 billion funding from the Treasury to the Fed to leverage purchases.
Secondary Market Corporate Credit Facility	*Supports corporate credit markets by providing liquidity for corporate bonds.* This facility will serve as a secondary market backstop for corporate bonds of eligible issuers that can be used to maintain liquidity in the corporate bond market. Under the facility, the New York Fed will lend to a special purpose vehicle (SPV) that will purchase qualified corporate bonds and corporate bond ETFs in the secondary market.

(continued)	Eligible assets are corporate bonds that are rated at least BBB-/Baa3 and a maturity of five years or less at time of purchase. This facility opened on 3/23/20 and will close on 9/30/20, with $10 billion funding from the Treasury to the Fed to leverage purchases.
Term Asset-Backed Securities Loan Facility	*Supports the flow of credit to consumers and businesses.* This facility was authorized to help meet the credit needs of consumers and small businesses by facilitating the issuance of asset-backed securities and improving market conditions for ABS. Under the facility, the New York Fed will commit to lend to a special purpose vehicle (SPV), with the Treasury to make an equity investment of $10 billion in the SPV. Eligible borrowers are all U.S. companies that own eligible collateral and maintain an account relationship with a primary dealer. It began (again) on March 23, 2020 and will function as a funding backstop to facilitate the issuance of eligible ABS until September 30, 2020.

Disclosures

Source: U.S. Federal Reserve, Strategas

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