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Monetary policy at crisis times

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Abstract: Working in a financial crisis environment is one of the most stressing tasks for a central banker. In order to diffuse a financial crisis, preventive policies, are of vital importance yet they cannot remove all disruptions that could lead to a crisis. Therefore, when a crisis emerges, risk management is of crucial importance. Risk management requires the utilisation of all available monetary policy instruments, as well as many unconventional instruments that would otherwise be considered as unacceptable in normal times. The paper discusses which actions a central bank should take at a down of a crisis,, including the instruments from the "psychological arsenal" such as crisis PR and deposit insurance.

Keywords: central bank, monetary policy, crisis, monetary policy instruments, crisis PR.

JEL Clasification: E52 and E58

1. Introduction

Financial crises have become the key challenge for central banks in modern times. During 20th century, lessons on the separation of the real from the monetary sector were learnt (Arestis and Sawyer, 2004), thus hyperinflations have become extremely rare.

There are many causes that can lead to a financial crisis, but whenever they appear, they are highly costly to a society. The banking crisis in Japan was estimated at about 20% of GDP (Caprio, 2003) while according to the World Bank estimate (2001), fiscal expenses of the banking crisis in 1980s and 1990s exceeded one trillion US dollars in developing countries only. Dages (2004) estimated that, as of the late 1970s, there were 117 systemic banking crises in 93 countries and 51 small banking crises in 45 countries. All banking crises brought about significant fiscal losses, which averaged 19% of GDP. Neither developed countries nor transition economies were exempt of banking crisis. The costs of the global financial turmoil are still unknown, but this has undoubtedly been an expensive crisis.

Crises have existed in the past and they will appear in the future. Many factors resulted in their appearance, but generally, as L. Santa (2007) stressed, they were the result of inefficient and imperfect functioning of financial markets, as well as asymmetric information emerging in markets. Central banks cannot prevent the appearance of all crises, but they may and have to be prepared to minimize their costs and to act preventively.

During the past decades, many developed countries were supportive of liberalism, which meant more freedom for private companies, less oversight and regulation and a greater role of the market. There is much evidence supporting the hypothesis that financial markets, if left on their own, will not automatically strive toward optimum conditions. Also, incomplete and asymmetric information may lead to wrong selection and formation of unbalanced prices. The problem of the wrong selection that appears before a loan is disbursed points to the fact that companies with most risky projects are highly likely to underestimate the riskiness of their projects in order to find investors. The nature of a market economy is to strive for higher profits, that is, market share increase. In case of financial institutions, profit maximisation could lead to risk underestimation. Thus the changed environment in the last few years has been the source of potential instability, leading to greater challenges for central bankers and the roots of the global financial crisis can be traced there.

At the onset of the global financial crisis, central banks, especially the Fed, did not properly respond to the crisis and underestimated the risks arising from bank failures in early 2007. Before that, central banks had mainly focused on preserving financial stability and, as the IMF working paper “Central Banking Lessons from the Crisis” (2010) indicates, central banks were neither sufficiently focusing on the financial system development nor on vulnerabilities piling up in the system. Although central banks recognized the appearance of price bubbles, it was believed that no monetary policy instrument is needed as a response, which facilitated the culmination of disturbances.

Box 1 – Government Programmes for Supporting Financial Sectors during the Global Financial Crisis

The **USA** passed a support programme worth 790 billion US dollars. Of this amount, some 250 billion dollars were designated for the buyout of bank shares to be transferred to the state ownership and the remaining 540 billion dollars to be used for the buyout of commercial securities. With a view to stimulating interbank lending, the Treasury guaranteed all new debts of banks over three years. The USA guaranteed all non interest-bearing deposits (mostly of SMEs), while the limit for other deposits was raised from 100,000 to 250,000 dollars.

France prepared a support package worth 360 billion euros. Some 40 billion euros were for state-owned companies to take over portions in problematic banks, while 320 billion euros were for guarantees on new loans with maturity up to 5 years. Besides, French government announced the payout of 10.5 billion euros to the group of six largest national banks (Crédit Agricole (3 billion euros), BNP Paribas (2.55 billion euros), Societe Generale (1.7 billion euros), Crédit Mutuel (1.2 billion euros), Caisse d'Epargne (1.1 billion euros) and Banque Populaire (950 million euros), with a view to overcoming the financial crisis effects. The state assistance was subject to limitations of top managers' salaries and bonuses.

Germany prepared a support package worth 500 billion euros. Some 400 billion euros for guaranteeing interbank lending, 70 billon euros for "cleaning contaminated balance sheets" of banks, 20 billion euros for covering potential losses from issued guarantees and 10 billion euros for takeover of doubtful assets. This state assistance was subject to the maximum top manager's salary of 500,000 euros and the cancelation of bonuses. The Government provided blank guarantee for all deposits (before that, deposits up to 20,000 euros were guaranteed).

Spain presented 100 billion euros worth support package. The entire amount was aimed at guaranteeing interbank borrowings in 2008. This programme was extended to 2009. It has foresees the possibility buyout of bank shares by the state. The level of guaranteed deposits increased from 20,000 to 100,000 euros.

Italy prepared a support package worth 20 billion euros. The concrete purpose of funds was not specified, leaving the possibility of increasing the amount by purpose, which was done in November 2008 when the package was increased to 80 billion euros, but not only to support the financial system, but the economy and households as well.

Austria adopted a support package worth 100 billion euros. Of the total amount, 85 billion euros were for guarantees for interbank loans, and the remaining 15 billion euros for bank recapitalizations. The level of guaranteed deposits was increased from 20,000 euros to 100,000 euros.

The **Netherlands** prepared 220 billion euros worth support package. Some 200 billion euros were designated for interbank loan guarantees and 20 billion euros for bank re-capitalizations.

Great Britain allocated 500 billion pounds as a guarantee for banking loans and increased banks' capital by 50 billion pounds. The UK Government intervened with 37 billion pounds to recapitalize three major banks (Royal Bank of Scotland, HBOS and Loyds TSB).

Source: Dimitrijević, B. and Fabris, N. (2010), Markoekonomija, Educons Univerzitet.

Soon afterwards, the role of central banks started to be seriously re-examined. How could they allow so large misbalances and fail to react to them? Were they also "dreaming"? Or, as one central banker said, "how can it be that radar was not connected to missile defence"? The crisis opened a dilemma of should central bank lean against emerging financial imbalances or bubbles by raising policy interest rates (IMF, 2010). Despite the common stance that leaning may increase inflation volatility and that it may lead to significant expenses (Bank of England, 2009; Gerlach, et al 2009, Ostry et al, 2010.), the global financial crisis has shown such a stance to be wrong. Although it may seem unrealistic that central banks can prevent all financial bubbles and all possible crises, they can still react due to growing misbalances and price bubbles because, as Crockett (2002) indicated, a burst of asset price bubble may cause financial disruptions over and beyond the wealth loss represented by declining asset prices.

There are those that claimed that central banks were actually misguided by low inflation artificially maintained at low level and with the emergence of China and India on the global scene and the flow of hundreds of millions of new workers willing to work for very low wages from these countries.

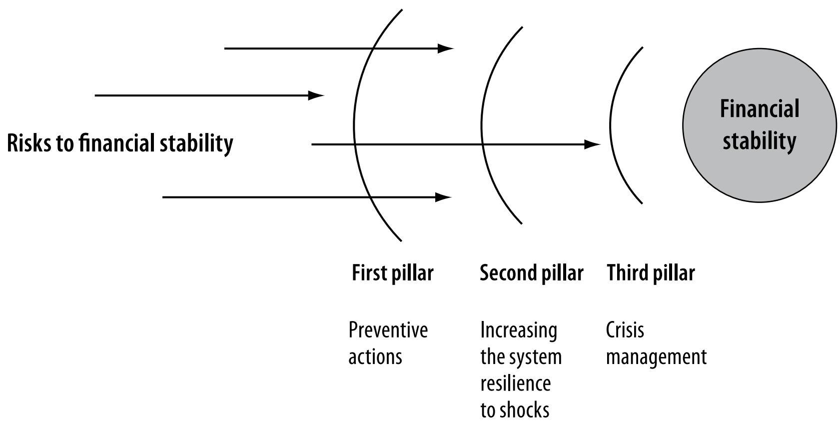
The higher propensity to Asian economies to save meant that a significant growth in demand in the USA was not inflationary or, as Gerlach et al (2009) stated, the period until the global financial crisis appearance had been called the "golden age" of central banks.

It is more likely that central banks remained "dormant" due to low inflation rate, as central banks' primary objective. The Governor of the Bank of England, Mervyn King (2005), spoke of monetary policy as "boring",[1] but central banking has surely become "interesting" again since mid-2007.

2. The Role of a Central Bank during Crisis Times

The primary objective of a central bank is to act preventively in order to avoid the appearance of a crisis, i.e. to preserve financial system stability. As Iwata (2006) points, a central bank has to react in the situation where the probability of event is low, yet the damage to economy could be quite large if it materializes. We may speak of three lines of defence. The first one is prevention, the second one is increasing the system resilience to shocks, and the third one is crisis management. All three dimensions are equally important.

Figure 1: Three financial stability defence pillars



Source: Disveld, P., 2010, „Strengthening Macro-prudential Supervision".

With a view to preventive acting, a quality supervision process is of utmost importance. Examining the causes of the banking crises on a sample of 29 countries, Caprio and Klingebiel (1998) determined that inadequate banking supervision was present in 90% of the banking crises. Of course, supervision is not the cause of banking crises, but its role in their prevention is indisputable.

[1] He meant that decisions on interest rates became very predictable.

Nevertheless, if a crisis appears, a central bank should use all available instruments to minimize its adverse consequences and contribute to its expedient resolution. The central bank becomes the key institution during a financial crisis. With regards to the global character of the financial system, crises become less national and more global, as confirmed by the recent global financial crisis. Therefore, international coordination of monetary and economic policies in general has an increasing importance during crisis times.

The key task of a central bank during a crisis is to preserve the system's liquidity and prevent massive bank failures in order to preserve financial stability. This is an important lesson learned during the Great Depression in 1930s. In those years central banks wrongly responded. To wit, restrictive monetary policies were followed and central banks allowed massive bank closures and did not take any significant actions to neutralize a decline in the money supply (Jakšić et al, 2012). It was assumed that this was the market "combat" and that bad institutions would disappear and be replaced by sound institutions. However, the massive disappearance of banks led to a panic wave and a pressure on other banks, which additionally deepened the crisis. A similar thing happened during the crisis in Argentina when it proved that massive bank closures only aggravated the crisis resolution because it completely undermined the banking system credibility (Blejer, 2003). Therefore, it is not surprising that the focus of monetary policy instruments significantly changed in the 20th century (Bindseil, 2004).

During a crisis, a central bank should enable commercial banks the access "cheap" liquid funds with a view to preserving the banking system stability. In such a situation, additional liquidity facilities are necessary as the regular approach in normal times is not appropriate.

The first step during a crisis is usually a decrease of the reference interest rate and the introduction of new liquidity "lines". Thus, at the beginning of the global financial crisis, many central banks reacted by reducing their reference interest rates to the historical minimums, as shown in box below. Moreover, countries where commercial banks allocate significant amounts for the mandatory reserve requirements should consider the possibility of decreasing the reserve requirements as that would increase available liquid funds in banks.

Box 2 - Movement of the Reference Interest Rates of the Major Central Banks during the Global Financial Crisis

ECB

On 14 December 2011, the ECB decreased its reference interest rate by 0.25 percentage points to stay at 1%, and thus it recorded the historical minimum for the second time after May 2009. In 2011, the ECB increased the interest rate twice due to growing risks to price stability. However, after regular economic and monetary analyses, the ECB decided to decrease the interest rate.

Period*		Fixed interest level, %
2011	14 Dec	1.00
	9 Nov	1.25
	13 July	1.50
	13 Apr	1.25
2009	13 May	1.00
	8 Apr	1.25
	11 Mar	1.50
	21 Jan	2.00
2008	10 Dec	2.50
	12 Nov	3.25
	15 Oct	3.75
2000	9 Jun	4.25
	28 Apr	3.75
	17 Mar	3.50
	4 Feb	3.25
1999	5 Nov	3.00
	9 Apr	2.50
	22 Jan	3.00
	4 Jan	3.00
	1 Jan	3.00

** The ECB reference interest rate has not changed from June 2000 to 15 October 2008.*

Bank of England

On 5 March 2009, the Bank of England decreased its reference interest rate by a half percentage point to 0.50%, which is the historical minimum. During 2010 and 2011, the Bank of England also kept the interest rate at the historical minimum, neglecting the Government's concern for the growing inflationary pressures.

	Date of change	Rate, %
2009	5 March	0.50
	5 February	1.00
	8 January	1.50
2008	4 December	2.00
	6 November	3.00
	8 January	4.50
	10 April	5.00
	7 February	5.25
2007	6 December	5.50

FED

In December 2008, due to problems in the financial market that were spilt to the real economy, FED decreased its reference interest rate to a record low ranging between 0% and 0.25%. With a view to boosting a low economic growth in the USA, the FED decided to maintain the reference interest rate at a record low and not to change in 2011 as long as the unemployment rate is high.

Date	Change in basis points		Level, %
	increase	decrease	
2008			
16 Dec	…	75-100	0-0.25
29 Oct	…	50	1.00
8 Oct	…	50	1.50
30 Apr	…	25	2.00
18 Mar	…	75	2.25
30 Jan	…	50	3.00
22 Jan	…	75	3.50
2007			
11 Dec	…	25	4.25
31 Oct	…	25	4.50
18 Sep	…	50	4.75

Source: Kozarić, K. and Fabris, N. (2012) Monetarno-kreditna politika. Sarajevo: Studio Switch

The activation of the lender of last resort function will be necessary if classic liquidity facilities prove to be insufficient to solve problems. From the preventive aspect, a central bank should transform a portion of its reserves into a liquid form in order to make them readily available to the banking sector.

Conventionally, the role of a lender of last resort involves ensuring liquidity support only against prime collateral. However, few prime types of collateral are available during the crisis because if being in the possession of such collaterals, banks themselves are able to cash them in (Kozarić, Fabris, 2012). Thus, low quality collaterals have to be accepted during a crisis. All central banks, more or less, did so during the global financial crisis, and the table below shows how the major central banks dealt with it.

Table 1: Collaterals in Selected Central Banks

	Eligible Asset Classes of Selected Central Banks[1]					
	Public securities[3]		Private assets			
	Domestic currency	Foreign currency	Corporate bond	ABS[4]	Short-term bank debt	Bank Loans
Fed						
OMO[2]	eligible	added	added	added	added	added
Standing facility	eligible	eligible	eligible	eligible	eligible	eligible
ECB	eligible	added	expanded	eligible	expanded	eligible
BoE	eligible	expanded	added	added	not eligible	not eligible
BoJ	expanded	added	expanded	expanded	not eligible	expanded
BoC						
OMO	expanded	added	added	not eligible	added	added
Standing facility	eligible	added	eligible	not eligible	eligible	added
RBA	eligible	not eligible	added	added	expanded	not eligible

1 "Eligible" indicates that the asset class has been eligible since the pre-crisis and no change has been made. "Added" indicates that the asset class had not been eligible before the crisis but was made eligible during the crisis. "Expanded" indicates that the asset class has been eligible since the pre-crisis and the eligible type of security was expanded during the crisis. "Not eligible" indicates that the asset class has continued to be ineligible through the crisis period.

2 The term auction facility of the Fed is included in OMOs as its profile is close to OMOs of other central banks such as the ECB and BoJ.

3 Public securities are bonds issued or guaranteed by central or local governments or government agencies.

4 Asset backed commercial paper was made eligible by the BoC.

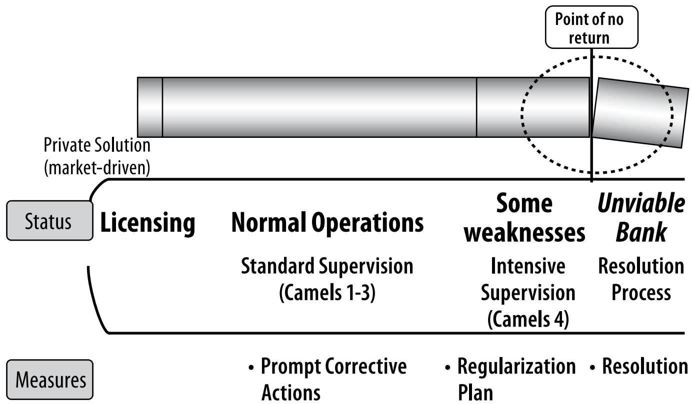
Source: IMF (2010), Central Banking Lessons from the Crisis, Washington.

Since the mistrust into the banking system increases during a crisis and bank runs may be expected, it is important that a central bank's treasury has sufficient cash holdings.

If the crisis escalates and threatens to result in bank failures, it is necessary that the central bank and the government jointly consider the "banking system rescue" plan. In any case, a preferred solution should be market resolution, but often it is not the real option during the crisis. To wit, during crisis times, we have the interest in investing decreasing due to higher risks on one hand, while on the other hand, failure of banks not classified as systemic may lead to panic. Then temporary nationalization or recapitalization of bank by the state is recommended. In general, financial support to a bank may be provided through cash injections, a loan, purchase of assets, placement of deposits, recapitalization or nationalization of banks.

Central bank's or state assistance is usually subject to certain conditions and it requires the adoption and implementation of bank resolution plans, limitations to wages, prohibition of bonus payments, suspending of shareholders' rights, relieving of duty of the management, and the like.

Figure 2: Different stages in a bank life



Source: CBCG (2011), Contingency Plan, Podgorica: CBCG.

The situation in problem banks should be resolved as soon as possible in order to:

- prevent contagion,

- preserve financial stability and public confidence into the banking sector, and
- limit losses of the state and/or tax payers.

With a view to solving the problem, bridge banks are sometimes established. These are temporary financial institutions founded for the purpose of accepting deposits and sound assets of one or few failed banks. A bridge bank may be allowed to take over all or some segments of banking operations like new lending and extending loan repayments. Non-performing assets are liquidated or transferred to an asset management company. If it is expected that a bridge bank would be sold to a solvent bank in the near future, the government may decide not to inject any capital into that bridge bank and thus the bridge bank arrangement becomes potentially cheap.

When a bank situation is resolved swiftly, costs are lower and the value of assets and franchise are protected. Allowing problem banks to continue pursuing their business causes market disturbances and increases moral hazard. Any delay and stalling would certainly increase the costs of the problem bank resolution.

It is believed that the FED made a great mistake when it allowed the Lehman Brothers collapse, which lead to even faster crisis spreading. Reasons for this decision are not clear even today. The failure of Lehman Brothers deepened the confidence crisis in almost all U.S. financial institutions. Other investment banks, Goldman Sachs and Morgan Stanley, suffered enormous pressures and faced the risk of their own failure. Bank of America took over Merrill Lynch, which later proved as not so good decision for Bank of America. During a crisis, bank failures do not lead to the financial system purification but, on the contrary, to the crisis deepening.

During the global financial crisis, in almost all developed countries direct capital injections into systemic banks resulted in *de jure* or *de facto* nationalization of large portions of the financial intermediation system. It became clear that traditional central banking toolbox was inadequate during the extraordinary circumstances of a credit crisis. With many banks trying to sell their collaterals, the prices of collateral went downwards and liquidity issues turned into severe solvency problems. In such a situation, central banks stepped away from the well-known historical role of the lender of last resort and it was necessary to turn to other unconventional instruments.

Box 3 – Major Bank Acquisitions during the Global Financial Crisis

List of large banks that went on bankruptcy or were overtaken is quite impressive. The list contains some of the world's largest banks, which were bearers of the global financial system in the previous period. The following table shows some of the most important banks that faced difficulties and had to be overtaken.

Table 2: Selected acquisitions of large banks

Date	Name	Acquirer	Type of company	Value
22.02.2008.	Northern Rock	Her Majesty's Government	Mortgage bank and bank operating exclusively with population	n.a.
01.04.2008.	Bear Stearns, New York City	JPMorgan Chase, New York City	Investment bank	$2,200,000,000
06.07.2008.	Catholic Building Society	Chelsea Building Society	Housing-saving cooperate	£51,000,000
01.07.2008.	Countrywide Financial, Calabasas, California	Bank of America, Charlotte, North Carolina	Second grade mortgage loans	$4,000,000,000
14.07.2008.	Alliance & Leicester	Banco Santander SA	Mortgage bank and bank operating exclusively with population	£1,260,000,000
26.08.2008.	Roskilde Bank	Danmarks Nationalbank (Danish Central Bank)	Mortgage bank and bank operating exclusively with population	$896,800,000 (kr4,500,000,000)
08.09.2008.	Derbyshire Building Society	Nationwide Building Society	Housing-saving cooperate	£7,100,000,000
08.09.2008.	Cheshire Building Society	Nationwide Building Society	Housing-saving cooperate	£4,900,000,000
14.09.2008.	Merrill Lynch, New York City	Bank of America, Charlotte, North Carolina	Investment bank	$44,000,000,000
16.09.2008.	American International Group, New York City	United States federal governmentA	Insurance company	$85,000,000,000

17.09.2008.	Lehman Brothers, New York City	Barclays plc	Investment bank	$1,300,000,000
18.09.2008.	HBOS	Lloyds TSB	Diversified financial services	$21,850,000,000
26.09.2008.	Washington Mutual, Seattle, Washington	JPMorgan Chase, New York City	Housing – saving cooperative	$1,900,000,000
26.09.2008.	Lehman Brothers	Nomura Holdings	Investment bank	$2
28.09.2008.	Bradford & Bingley	Her Majesty's Government (Mortgage Assets) Banco Santander SA (Savings Liabilities)	Diversified financial services	£21,100,000,000
28.09.2008.	Fortis	Government of the Netherlands (Dutch assets including ABN AMRO) BNP Paribas (Belgian and Luxembourg assets)	Diversified financial services	€11,200,000,000
30.09.2008.	Dexia	The Belgian, French and Luxembourg governments	Public finance and retail trade	n.a.
03.10.2008.	Wachovia, Charlotte, North Carolina	Wells Fargo, San Francisco, California F	Investment and retail bank	$15,000,000,000
07.10.2008.	Landsbanki	Icelandic Financial Supervisory Authority	Commercial bank	n.a.
08.10.2008	Glitnir	Icelandic Financial Supervisory Authority	Commercial bank	n.a.
09.10.2008.	Kaupthing Bank	Icelandic Financial Supervisory Authority	Commercial bank	n.a.
09.10.2008.	BankWest (subsidiary of HBOS)	Commonwealth Bank of Australia	Bank	£1,200,000,000
13.10.2008.	Sovereign Bank, Wyomissing, Pennsylvania	Banco Santander SA	Bank	$1,900,000,000

22.10.2008.	Barnsley Building Society	Yorkshire Building Society	Housing – saving cooperative	£376,000,000
24.10.2008.	National City Bank, Cleveland, Ohio	PNC Financial Services, Pittsburg, Pennsylvania	Bank	$5,580,000,000
24.10.2008.	Commerce Bancorp, Cherry Hill, New Jersey	Toronto-Dominion Bank, Toronto, Canada	Bank	$8,500,000,000
04.11.2008.	Scarborough Building Society	Skipton Building Society	Housing – saving cooperative	n.a.

Source: CBCG (2008). Chief Economist Report (January - September 2008). Podgorica: CBCG.

If a central bank and the government do not dispose with sufficient funds for crisis resolution, the option to be considered is possible arrangement with the IMF. During the global financial crisis, the IMF reacted relatively swiftly and provided recovery funds to many countries.

During crisis times, many other unconventional instruments may be applied in the cooperation of a central bank and the government such as: guarantees for interbank loans, buyout of bad assets, temporary limitations to capital flows, buyout of private and government securities by the central bank[2] and the like. It is important that activities of the central bank and the government are coordinated because that has positive effects on expectations.

In normal times, central banks should prepare contingency plans. The objective of such a plan is to allow a central bank to act in case of contingencies and/or a bank crisis or a systemic crisis in an efficient, effective, consistent and comprehensive manner. Such plans usually define:

- crisis events involving the central bank,
- early warning indicators,
- crisis management principles,
- preventive actions,

[2] The FED's balance sheet during the global financial crisis increased from some 800 billion dollars to over 3 trillion dollars in just few months. Other large central banks faced similar situation since they were forced to buy huge debts in order to preserve some liquidity in the system. The reason for that was partially the lack of confidence among banks that resulted in the central bank's becoming the main partner of private banks and the central intermediary in the money market.

- prevention and mitigation of crisis effects,
- strategies for managing banks in crisis,
- crisis scenarios,
- crisis communication, and
- crisis simulation exercises.

The key task of a central bank should be preventive actions to avoid crisis and aggravation of financial stability. Therefore, with a view to ensuring the earliest possible identification of a crisis symptoms, the central bank should analyse the macroeconomic environment on an ongoing basis; analyse and assess the systemic risk factors; analyse and assess financial condition in all banks in the system; conduct stress testing of banks; on the basis of collected information, timely identify problem banks and request the banks to submit their contingency plans and recovery and resolution plans. Central banks should pay due attention to over-rapid growth of some banks, the appearance of price bubbles in any of the market segments, risk management in the banking system, as well as to liquidity and solvency of every individual bank.

2.1. Measures from the "Psychological Arsenal" – Crisis PR Communication

Important actions also include measures from the so-called "psychological arsenal" which are used to diffuse panicking. The crisis PR is of utmost importance. Through its releases, media appearances and the choice of adequate instruments, a central bank should try to diffuse the panic both with the population and the financial markets.

During the crisis, PR gains importance since an adequate and well-designed communication strategy may reduce the panic and focus public expectations on desired direction. The need for information increases during a crisis. All stakeholders (employees, suppliers, investors, clients, the media, law-makers...) would demand far more information than in regular times. They want to know the "real time info", to know how an organization is dealing with the crisis, what the consequences are, and how it would all look like when the crisis is over.

There are four key factors for successful crisis communication:

1. Those performing crisis communication tasks must dispose of all relevant information on the event – they have to `rule` the information;
2. PR services have to be prepared for crisis situations in advance and to have the crisis communication plan ready. Thus, for example, successful finan-

cial institutions often revise these plans annually and many even carry out crisis communication simulations in order to examine the plans' efficiency;

3. Delegation of duties must be clear – crisis communication teams have to be prepared and established long before the crisis appearance. Timing is one of the most important things in crisis communication – usually, there is no time for establishing teams, staff training and assignment of duties during a crisis
4. Proactivity– create news and not wait to become a piece of news. Otherwise, it would be very difficult to control a crisis.

Every successful crisis communication plan should contain the following elements:

- **Crisis headquarters** – the primary step for a successful crisis resolution is establishing a crisis headquarters which shall, upon collecting all relevant information on the crisis event, make key decisions through joint consultation of its members. In addition to people from a company's management and experts in this area, this headquarters must also involve public relations officers.
- **Internal communication plan in crisis situation** – with a view to achieving efficient communication, each employee should know whom to forward information and with whom to communicate during the crisis.
- **Spokesperson** – institutions should delegate a person which would communicate information to the public. The selection of a quality and experienced person is implied, since such a person shall give credibility and strength to messages sent to the public. Similarly, a good crisis communication plan means communication solely via the spokesperson and/or other channels envisaged in the crisis communication plan. It does not take much but the media representatives receiving few contradictory pieces of information from the same organization regarding the same issue and the public confidence into the institution and the creditability of statements of its officials disappear, and thus the very effectiveness of the crisis communication plan.
- **Drafting scenarios and crisis simulation** – simulations (mostly accompanied with the assessments by independent public relations experts) are very useful since they allow companies to test their crisis communication strategies and to notice and correct potential shortcomings. When the crisis really emerges, there is usually no time for corrections, and planning fallacy means great damage.

- **Determining the target public** – it is very difficult to identify all types of public that the company should address. Neglecting just one important target group may have immense consequences.
- **Defining the key messages per public** – each public addressed by the company has its interests and priorities, which means that messages have to be tailored to meet the public needs.
- **Determine the most effective communication methods** – depending on the crisis type, the timing and the media which should be addressed have to be known, as well as the best way of communication (press conferences, individual statements, press releases).
- **Communication urgency and preciseness** – the following three key questions have to be answered:
  - What has happened?
  - What are we doing about it?
  - What shall we do?

  Sincerity and sympathy should be shown when answering these questions. Any arrogance, insincerity, and particularly lying are unacceptable. A lie, no matter how alluring it may be at the moment, is the worst thing the spokesperson (or any other person in charge of issuing statements) may afford. In most cases, a lie is revealed and since the same common life rules apply to public relations, the corporate image, confidence, and complete reputation disappear.
- **Analysis of crisis communication effects** – the follow-up of the media headlines and their analysis may help re-examine the crisis communication plans, their efficiency, and in learning lessons for future activities.

The category of psychological arsenal instruments also includes increasing the amount of guaranteed deposits in order to reduce bank runs. During the crisis, the EU increased the coverage of guaranteed deposits, first from 25,000 euros to 50,000 euros and later on to 100,000 euros. Although many countries did not have enough funds to guarantee all insured deposits, these measures had a strong psychological effect and slowed down deposit outflows. In case of the "protected event", it is important to ensure a swift compensation of guaranteed deposits in order to prevent panic.

It is particularly dangerous that people queue outside banks in order to withdraw their money. During one of the previous crises, the USA solved the problem by installing many ATMs literally over night to prevent queuing (Fabris, 2006).

3. Conclusion

Crises have existed in the past and they will reappear in the future. Changes in the modern global system have made crises less national, and vulnerability sources have increased. Therefore, coordination of monetary policies is of utmost importance. During a crisis, a central bank should have the key role regardless of whether or not it is responsible for financial stability or whether or not it is the regulatory authority.

The focus should be put to preventive actions, but when a crisis appears, adequate crisis management becomes necessary. The intervention at the beginning of the crisis reduces costs and shortens its duration. It is completely wrong not to intervene and expect that the market itself would resolve the crisis, since bank failures during the crisis shall not lead to market purification but to deterioration of the financial system credibility.

It would be important for a central bank to have well-prepared contingency plans (including the crisis PR) before a crisis appears. Unconventional instruments, usually unacceptable in normal times, should also be used during the crisis. To wit, in such conditions, interests rates are relatively ineffective in stimulating aggregate demand, while increases in risk aversion may override the stimulus to consumption and investment of low real interest rates (IMF, 2009). This means that we should not flinch from bank nationalization, expanding liquidity facilities, accepting low-quality collaterals, buyout of bad assets, limiting certain capital flows, state guarantees for some transactions and the like, which surely does not exclude standard monetary policy instruments. It is of utmost importance to reassure the public that the crisis is under control, that is, to perform adequate PR activities. The paper, also, shows what a central bank should do during the crisis.

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