



# **Fiscal Consolidation in America: the Policy Options**

## **Comments to Altshuler & Bosworth**

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# What is A&B's goal?

Two-fold goal:

- to evaluate the options for fiscal consolidation in future years
- to place those options “within the context of a continuing tradeoff between the objective of an improved fiscal balance and desires to restore the economy to high levels of employment

## What do A&B discuss?

- Economic outlook and the challenges that it raises for fiscal and monetary policy
  - trade-off between budget reduction and support to growth
- Lessons from the international experience with fiscal consolidation programmes
- Baseline projection for the US budget outlook
- Options for fiscal consolidation over the medium-term
  - expenditure reduction
  - revenue increases

# What do A&B conclude?

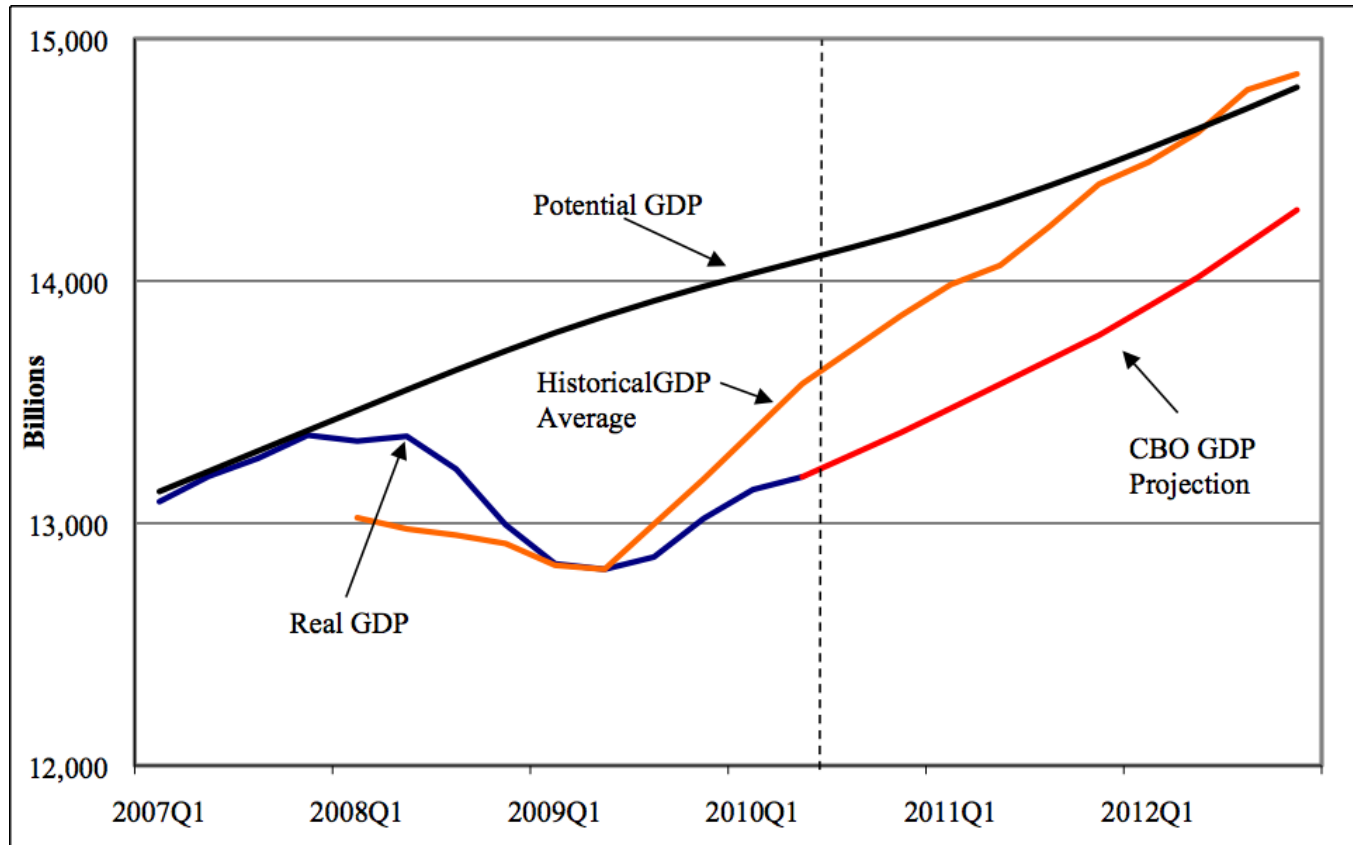
- Policy options are limited:
  - monetary policy → limited impact
  - Fiscal policy → political constraints both domestically and internationally (problems with coordination/cooperation)
- Current budget policies will fast increase the public debt as a share of GDP
- Action to bring back the federal budget into balance will require large structural changes in both expenditures and revenues
- The US need to consider a broader range of new revenue sources

## This is a 'three-papers' paper

A few suggestions:

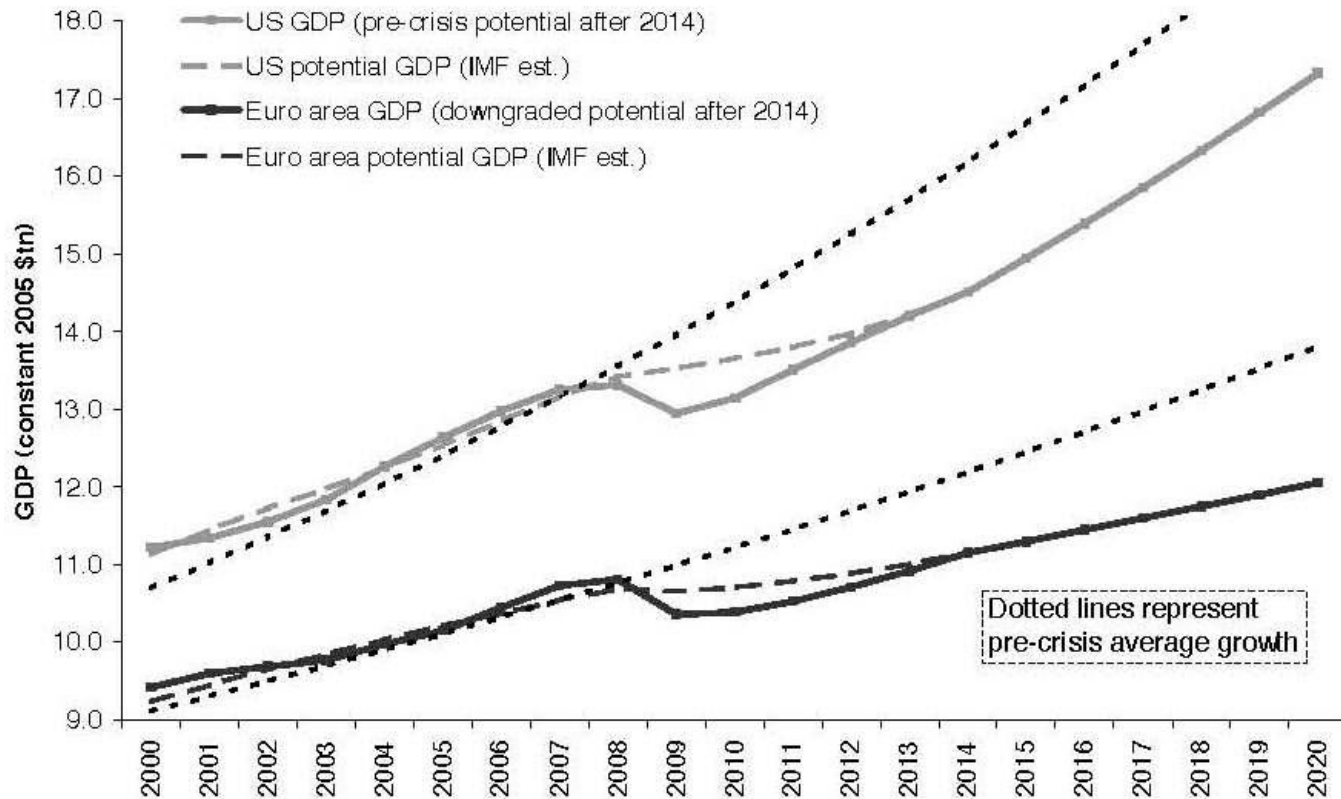
- Focus on economic outlook and challenges for policies within the context of global rebalancing, **or**
- Focus on fiscal consolidation and tax reform in the US and discuss lessons from other countries - i.e. Sweden and Canada, **or**
- Draw scenarios based on fiscal consolidation and tax reform, and assess the impact on growth

# Alternative paths to recovery



# Pre-crisis and post-crisis growth trends for the US and the euro area

Figure 2: pre-crisis and post-crisis growth trend for the US and the euro area



Source: IMF data and estimates by Chatham House International Economics

# Can the US afford to go 'solo'?

- The US is the only major country with a further fiscal stimulus
  - Less need to please the “bond vigilantes”: USD as the key reserve currency and ‘safe haven’
  - But the tools used may not be the most appropriate and risk fuelling international tension
  - And potential loss of impact through imports
- A&B suggest that any additional stimulus measures need to be temporary and integrated with a coherent long-term plan of fiscal consolidation

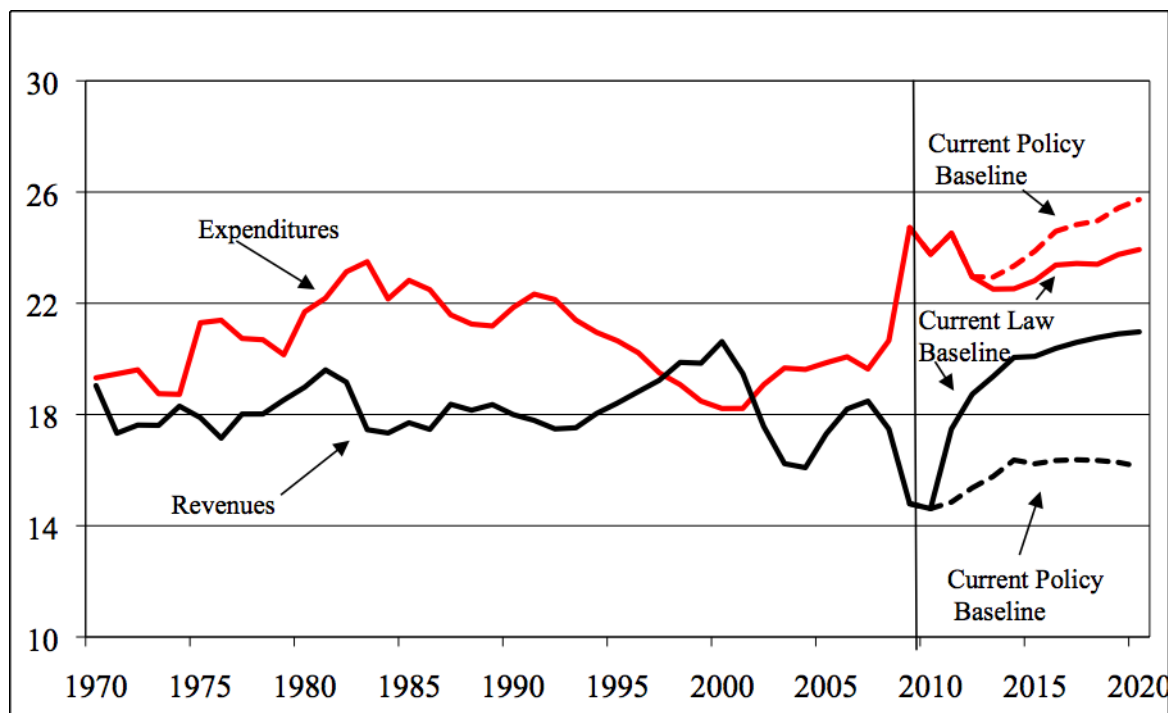


# **There are three lessons from the international experience**

- Credible and transparent rules
- Need for an enforcement mechanism
- Flexibility and robustness in the response to unforeseen shocks

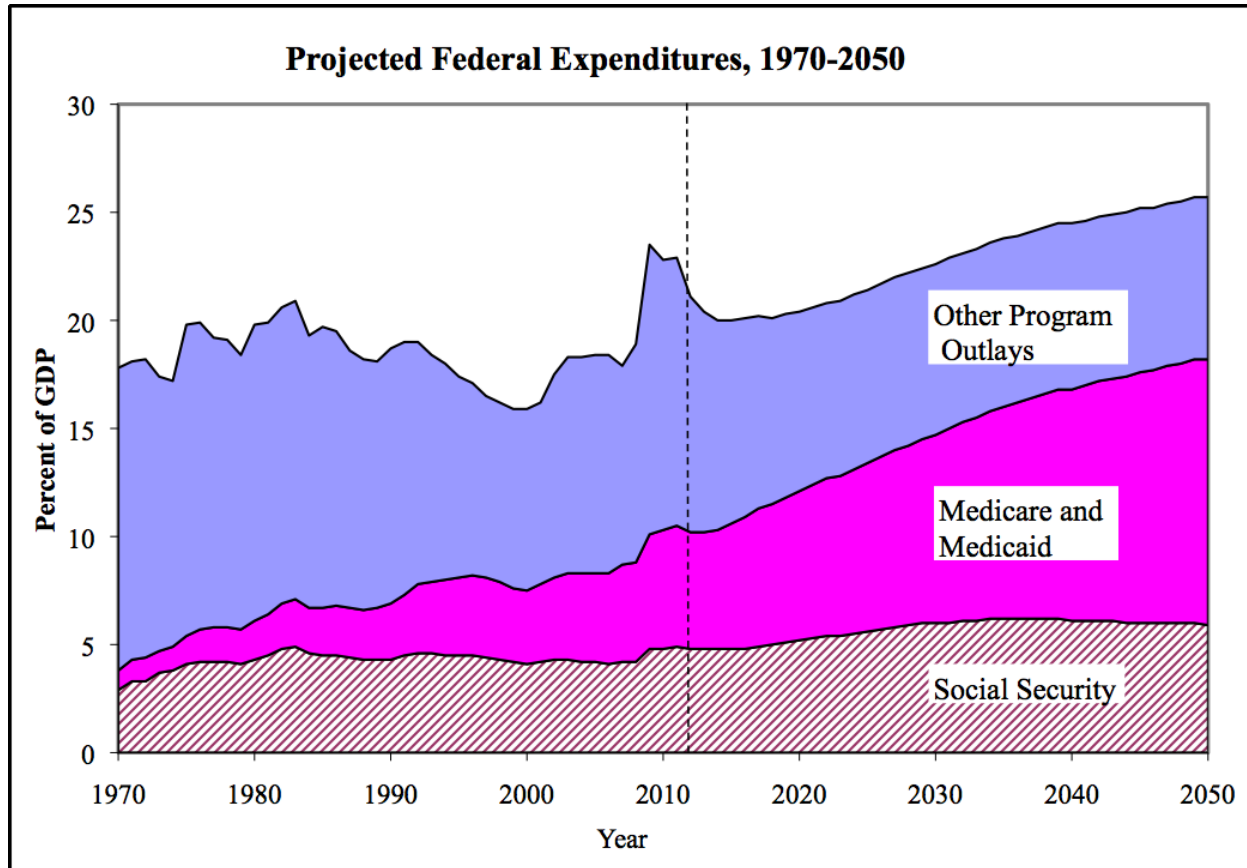
# The budget outlook (short term)

## Federal Revenues and Expenditures, 1970-2020 (% of GDP)



# The budget outlook (long term)

## Projected Federal Program Outlays, 1970-2050 (% of GDP)



# The US needs to look at new revenues sources

- Higher revenues within the current framework of the individual and corporate income tax
- VAT tax
- Tax on carbon emissions
- Tax reform programme based on the three previous points

# Is revenue increasing feasible?

Policy	Measures	Goal	Feasibility
Increase revenues the existing ind and corp income tax	Ind. in. tax rates	little impact	difficult
	Corp income tax	little impact	difficult
	Tax expenditure reform	good	difficult
Adopt VAT	VAT	complicated design	difficult
Adopt green tax	Tax on carb emission	Revenues do not go against goal	difficult
	Raise tax on gas	good	difficult

**Thank you**

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