

International Forum on
Economic Development and Public Policy



*Fiscal Reform To Support Strong
and Equitable Growth:
Striking The Right Balance*

Shifts in International Thinking On Fiscal Policy

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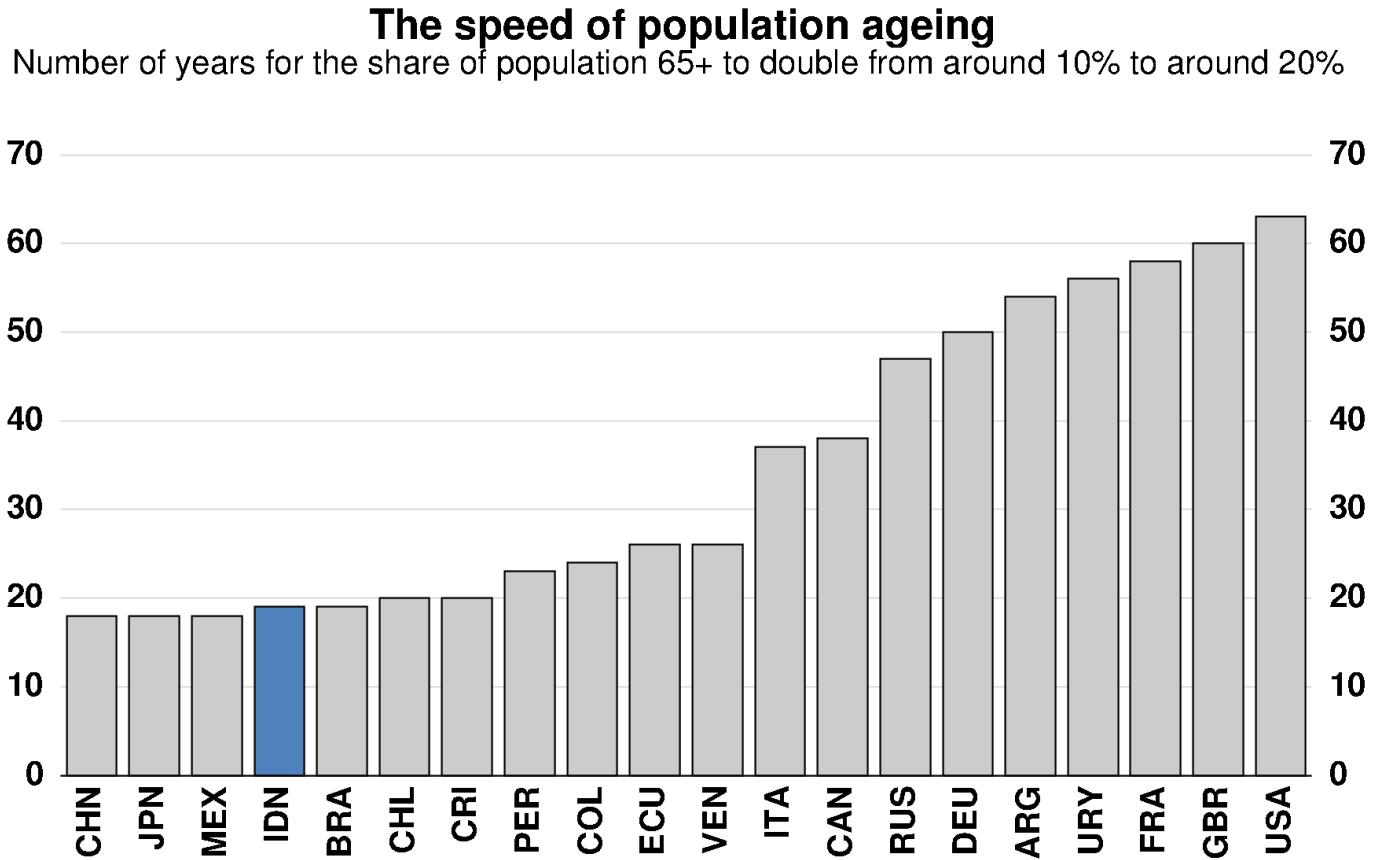


Outline

1. Reasons to revisit fiscal policy:
 - Global financial crisis
 - Trend changes
2. First shift : fiscal policy as a stabilisation tool
3. Second shift : trade-off between stabilisation and sustainability
4. Third shift: moving beyond economic growth
5. Fourth shift : fiscal policy in an uncertain environment



Why should fiscal policy be revisited ?



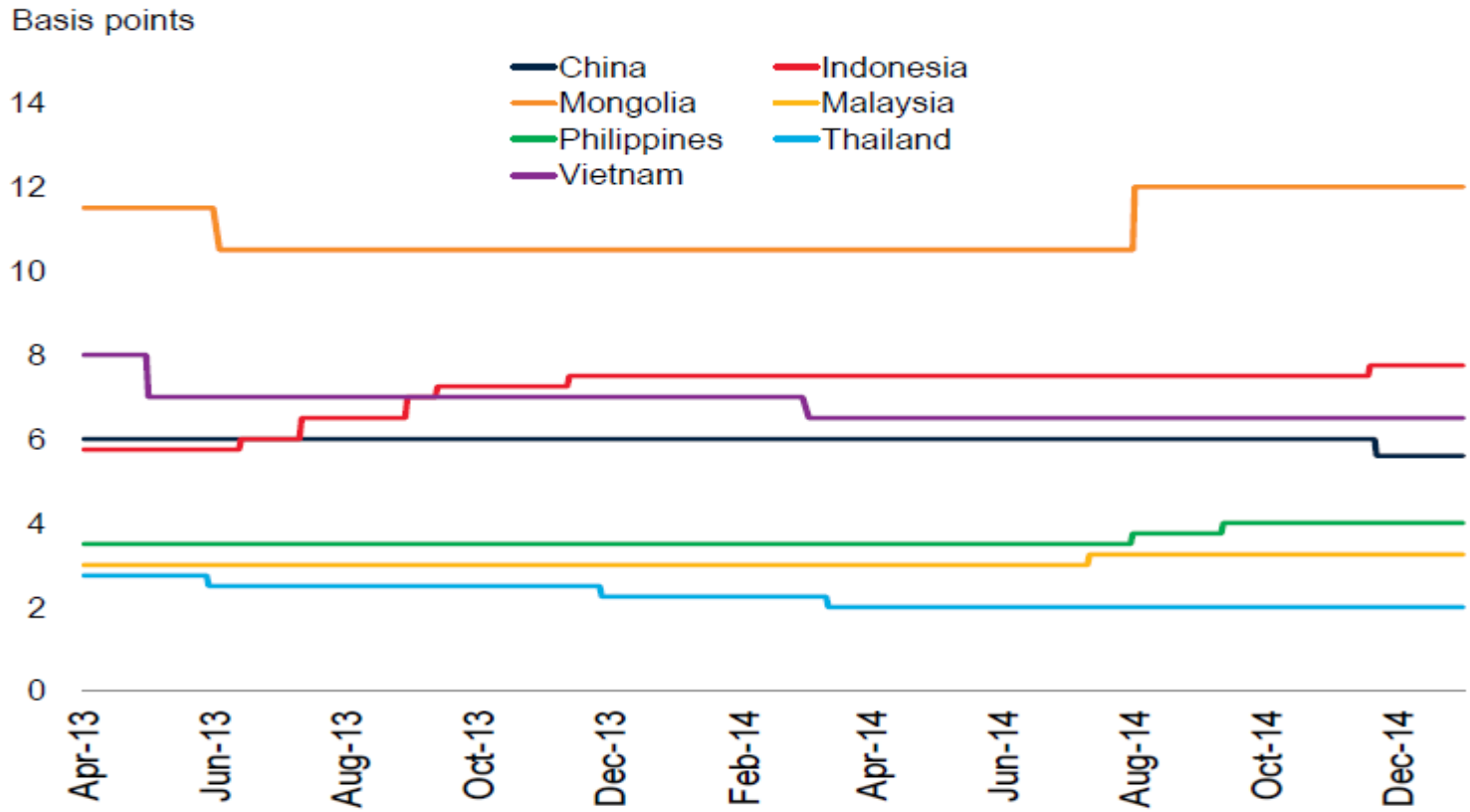
Source: OECD calculations.



Monetary policy has little room for manoeuvre

First shift : stabilisation

Interest rates



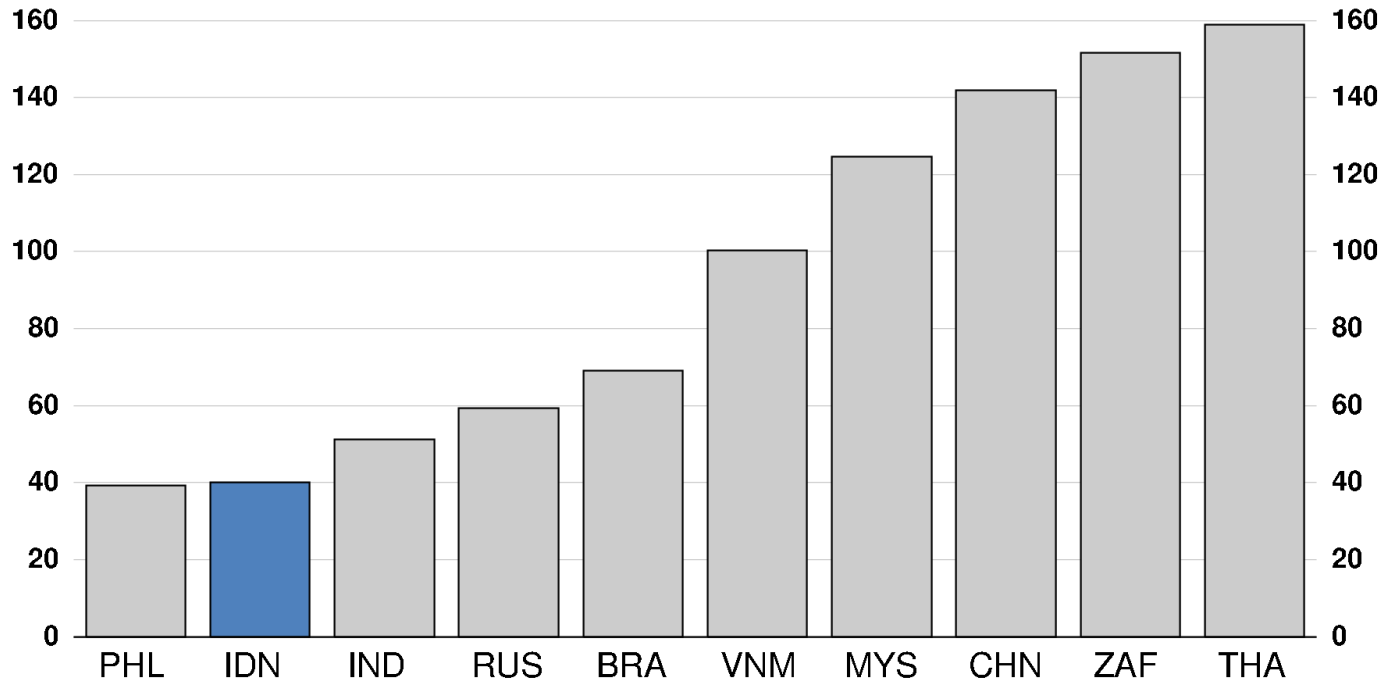
Source: World Bank.



Financial-market deepening is still low

First shift: stabilisation

Domestic credit to private sector
As a % of GDP, 2014

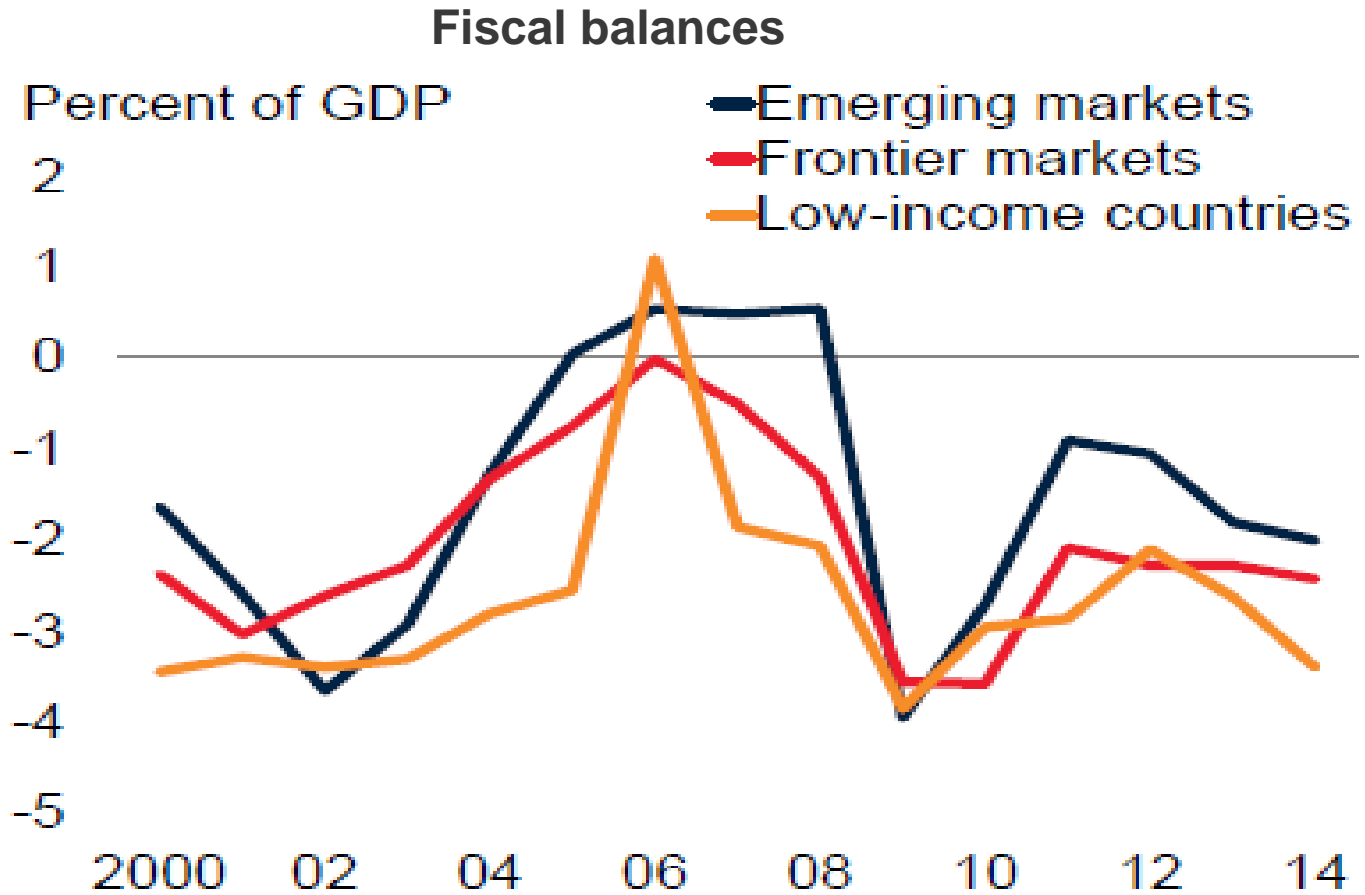


Source: World Bank Development Indicators.



EMEs made greater use of fiscal stimulus during the financial crisis

Second shift : trade-off



Source: World Bank.



Fiscal multipliers are hard to estimate

Fiscal multipliers depend:

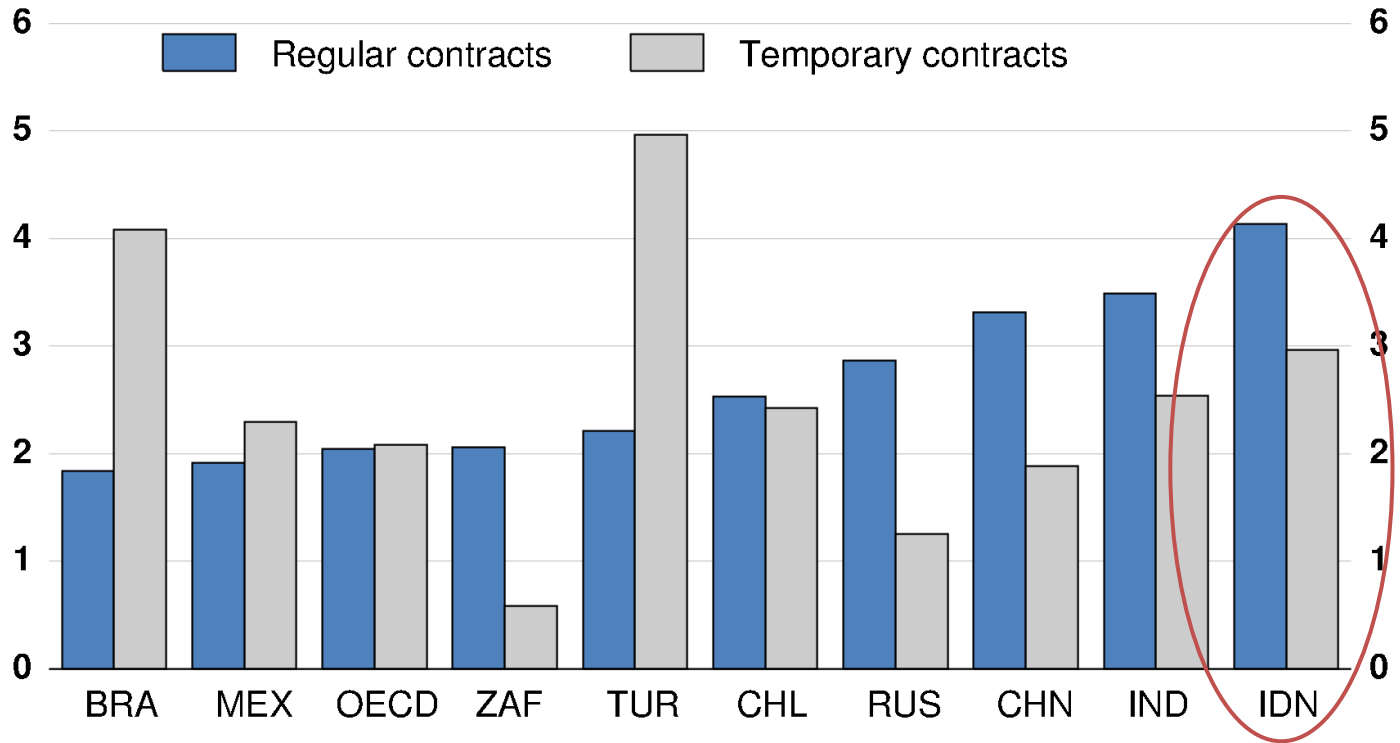
- On whether the measures are temporary or permanent;
- On the structure of the economy: openness, exchange-rate regime, fiscal space, structure of spending and tax, size of automatic stabilisers;
- On the position in the business cycle, monetary policy reaction;
- On the choice of instruments.



Hysteresis also influences the trade-off

Second shift : trade-off

Employment protection legislation, 2013
Index scale of 0-6 from least to most restrictive



Source: OECD (2014), Going for Growth.



The quality of public finances is key

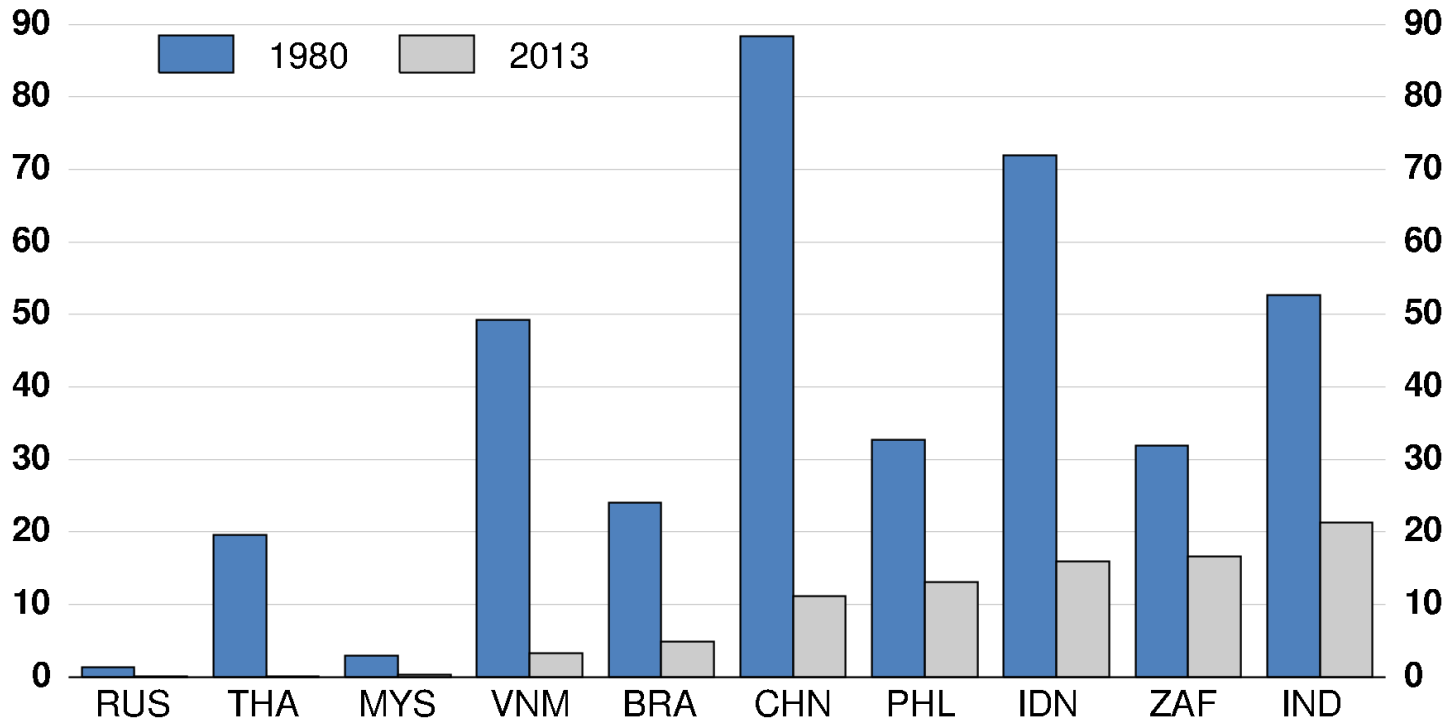
- Good-quality public finances can ease the trade-off between growth and debt dynamics.
- OECD countries have focused on expenditure prioritisations, performance-based budgeting and reforms in the structure of their public administration.
- Emerging-market economies also have to improve tax collection and to address bottlenecks in the implementation of infrastructure projects.



Poverty has markedly decreased in EMEs

Third shift : equity

Poverty headcount ratio at \$1.90 a day, 2011 PPP
As a percentage of population



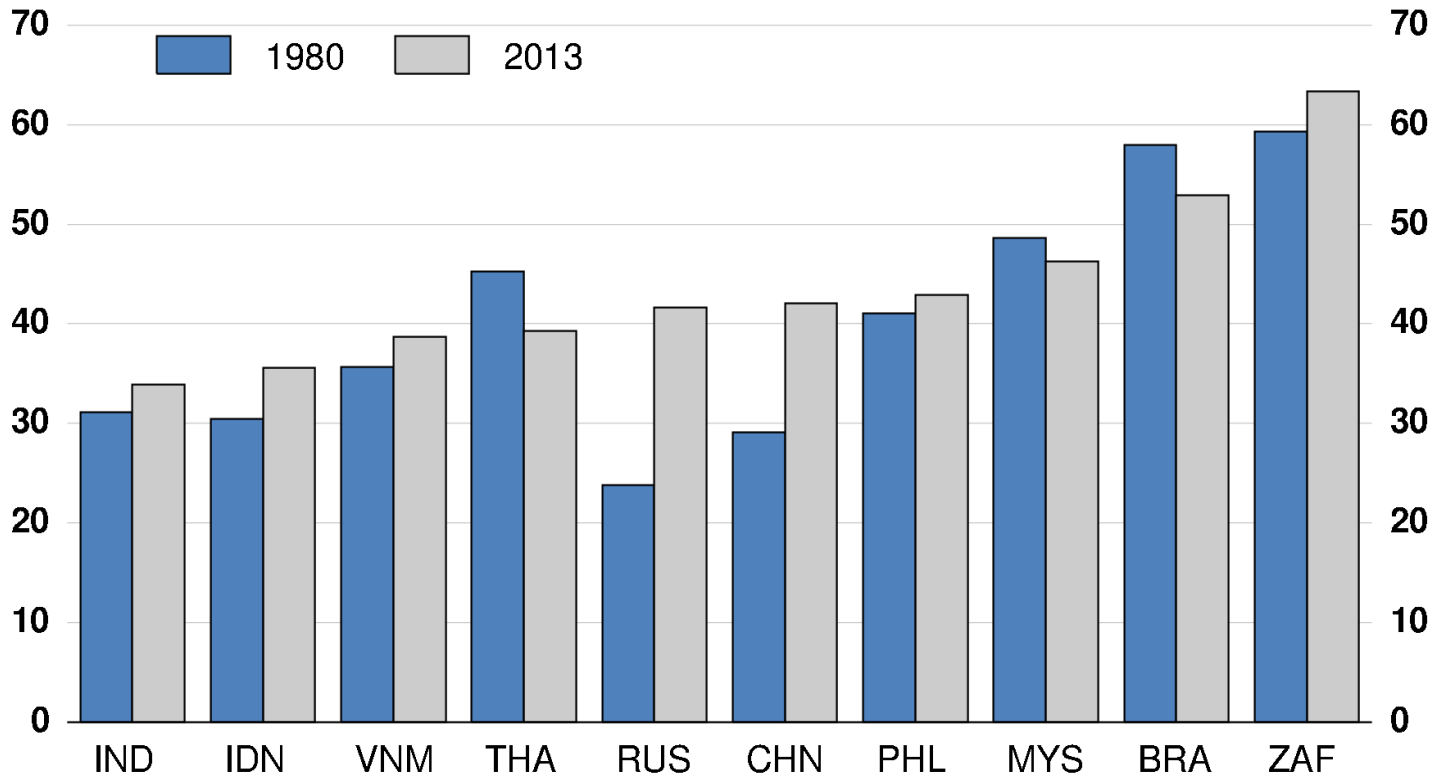
Source: World Bank, WDI.



But inequality has risen

Third shift : equity

Gini coefficients



Source: World Bank, WDI.



Fiscal tools have a different impact on growth and inequality

Third shift : equity

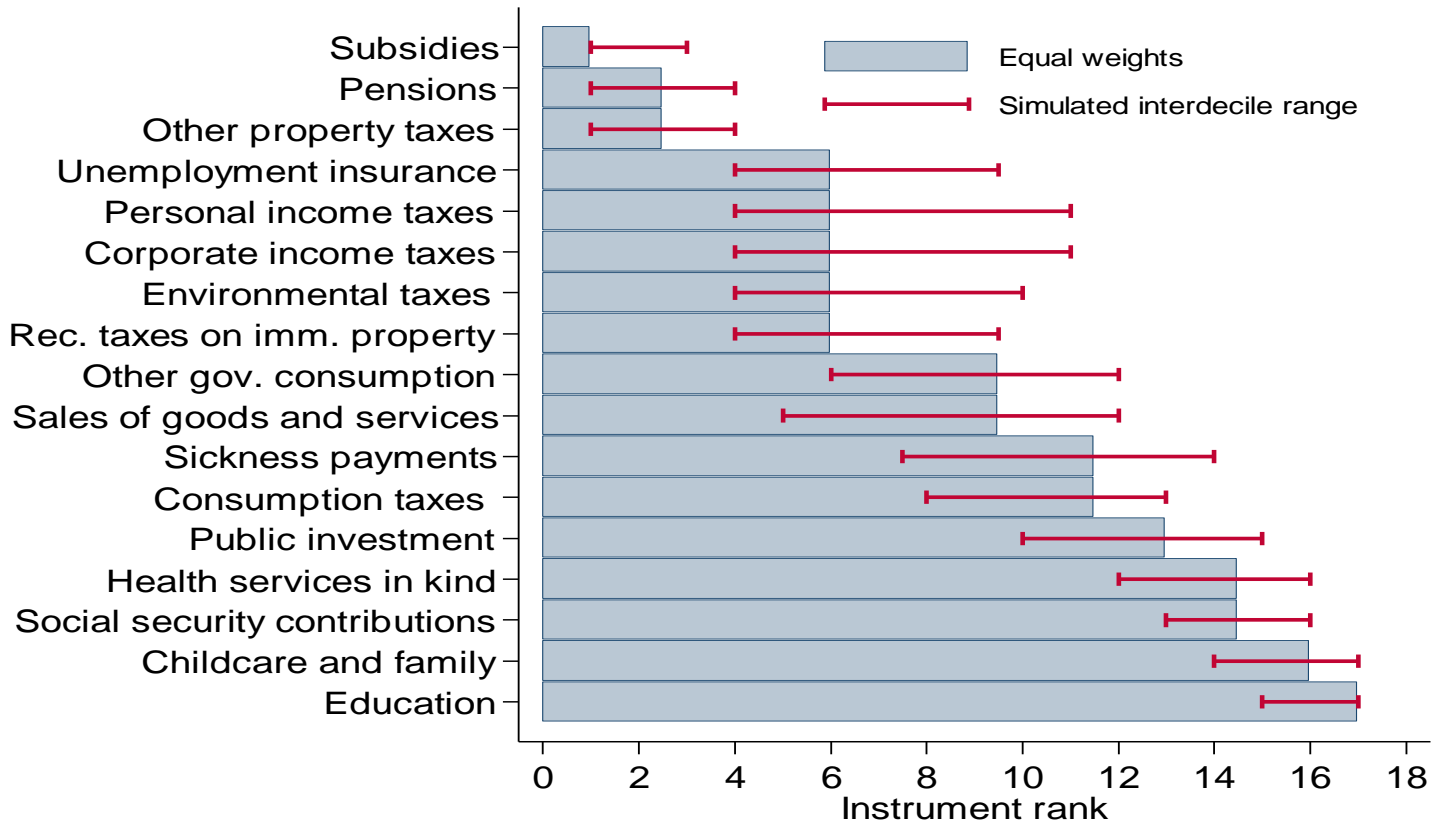
	Growth		Equity	
	Short-term	Long-term	Short-term	Long-term
Spending cuts				
Education	--	--	-	--
Health services provided in kind	--	-	-	-
Other government consumption (excluding family policy)	--	+	-	
Pensions		++		
Sickness and disability payments	-	+	--	-
Unemployment benefits	-	+	-	
Family	-	-	--	--
Subsidies	-	++	+	+
Public investment	--	--		
Revenue increases				
Personal income taxes	-	--	+	+
Social security contributions	-	--	-	-
Corporate income taxes	-	--	+	+
Environmental taxes	-	+	-	
Consumption taxes (other than environmental)	-	-	-	
Recurrent taxes on immovable property	-			
Other property taxes	-		++	+
Sales of goods and services	-	+	-	-

Source: Cournède, Goujard and Pina (2014).



Combining equity and growth in OECD countries

Ranking from most to least desirable instruments of consolidation



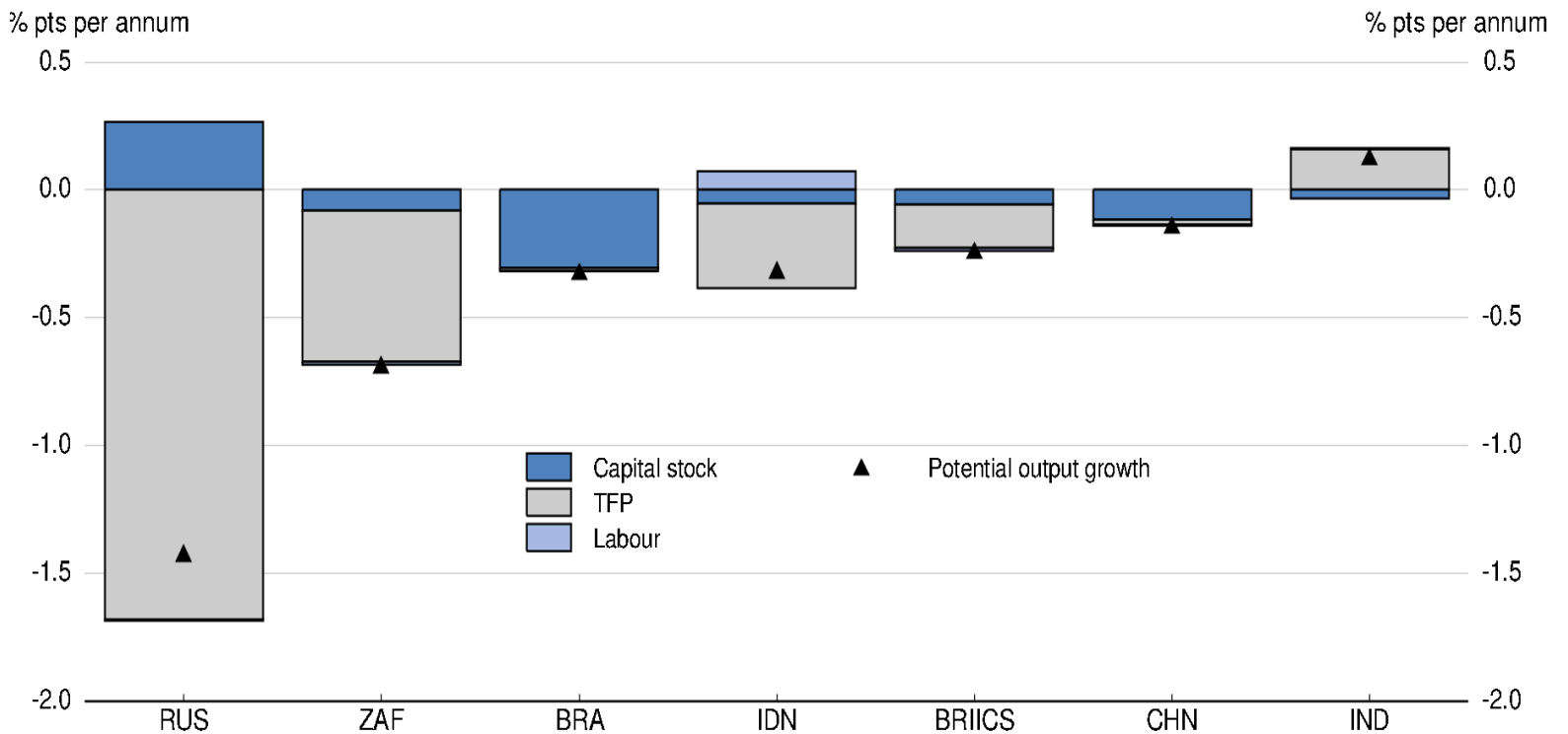
Source: Cournède, Goujard and Pina (2014).



Future potential output prospects are highly uncertain

Fourth shift : uncertainty

Revision to potential output growth for 2016



Source: Economic Outlook (2015).



Uncertainties have implications for fiscal assessments

- Structural balances are hard to use in real time.
- ‘Prudent’ debt targets can account for uncertainties in fiscal frameworks (Fall and Fournier, 2015).
 - Budget balance rules (complemented by an expenditure rule)
- Well-designed escape clauses suspending fiscal rules allow to deal with tail events.



Shifts in the way one think of fiscal policy in recent years

- Fiscal policy is now considered as an important stabilisation tool.
- Fiscal stances depend on the trade-off between stabilisation and sustainability and are country-specific.
- The choice of instruments depends on the respective weights of the growth and equity objectives (/environmental)
- Heightened uncertainties should also be accounted for.



THANK YOU
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