The Global Fiscal Outlook

Carlo Cottarelli
Director, Fiscal Affairs Department

March 19, 2013
What Happened in 2008?
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![Dow Jones Industrial Index (2007-08)](image)
What Happened in 2008?

Dow Jones Industrial Index (2007-08)

What Happened in 2008?
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A New Role for Fiscal Policy
A New Role for Fiscal Policy

This was not an ordinary recession
A New Role for Fiscal Policy

This was not an ordinary recession

Real GDP Growth (2000-09)

World

Advanced

Dienstag, 19. März 13
A New Role for Fiscal Policy

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A New Role for Fiscal Policy

- This was not an ordinary recession

- Recession turned into a demand recession
A New Role for Fiscal Policy

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- Recent recession turned into a demand recession
A New Role for Fiscal Policy

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- Recession turned into a demand recession
A New Role for Fiscal Policy

- This was not an ordinary recession
- Recession turned into a demand recession
- Monetary lever was not working

Federal Funds Rate (2007-present)
General Government Gross Debt

Advanced Economies, 1880-2013 *(Percent of GDP)*

Dienstag, 19. März 13
General Government Gross Debt

G7 Economies, 1970-2007 (Percent of GDP)

Canada

France

Germany

Italy

Japan

United Kingdom

United States

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General Government Deficits

Advanced Economies, 2000-09
General Government Deficits

Advanced Economies, 2000-09

- Headline deficit, percent of GDP
- Structural deficit, percent of potential GDP

Dienstag, 19. März 13
General Government Gross Debt

Advanced Economies, 1880-2013 (Percent of GDP)

2007 Level
General Government Gross Debt

Advanced Economies, 1880-2013 (Percent of GDP)

2007 Level

Dienstag, 19. März 13
Why is the Fiscal Outlook Worse than After WW2?
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Most of the fiscal adjustment then consisted of cuts in military spending.
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- There was no pressure on pension and health care at the horizon
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**Advanced Economies: 2010-50 (Percentage points of GDP)**

- Health care
- Pensions

Dienstag, 19. März 13
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**Advanced Economies: Population between Ages 15-64**

1950=100
Most of the fiscal adjustment then consisted of cuts in military spending.

There was no pressure on pension and health care at the horizon.

Growth rate of the labor force was much higher than we project now.

Advanced Economies: Population between Ages 15-64

- 1950=100
- 2010=100
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Why is the Fiscal Outlook Worse than After WW2?

- Most of the fiscal adjustment then consisted of cuts in military spending
- There was no pressure on pension and health care at the horizon
- Growth rate of the labor force was much higher than we project now
- Financial sector in most advanced economies was repressed
25 Advanced Economies
Group 1: Declining or stable debt

(General Government)

<table>
<thead>
<tr>
<th>Country</th>
<th>Deviation from debt in 2007, percentage points of GDP</th>
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<tbody>
<tr>
<td>CZE</td>
<td>0</td>
</tr>
<tr>
<td>DNK</td>
<td>-4</td>
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<tr>
<td>KOR</td>
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<tr>
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</tr>
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<td>KOR</td>
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Dienstag, 19. März 13
Group 1: Declining or stable debt

(General Government)

Deviation from debt in 2007, percentage points of GDP

Headline deficit, percent of GDP

KOR
DEU
CHE
FIN
SWE

Deviation from debt in 2007, percentage points of GDP

-10  5  20  35  50  65  80  95

2008

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Group 1: Declining or stable debt

Dienstag, 19. März 13
Group 1: Declining or stable debt

(General Government)

Deviation from debt in 2007, percentage points of GDP

Dienstag, 19. März 13
Group 1: Declining or stable debt

<table>
<thead>
<tr>
<th>Country</th>
<th>2011 Deviation from debt, percentage points of GDP</th>
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<tr>
<td>KOR</td>
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<td>CZE</td>
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<tr>
<td>DNK</td>
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Dienstag, 19. März 13
Group 1: Declining or stable debt

(General Government)

Headline deficit, percent of GDP

Deviation from debt in 2007, percentage points of GDP
Group 1: Declining or stable debt

(General Government)

Deviation from debt in 2007, percentage points of GDP

Headline deficit, percent of GDP

CZE
DNK
KOR
SWE
DEU
CHE
FIN

Deviation from debt in 2007, percentage points of GDP

2013

0
10
20
30
40
50
60
70
80
90
100

Dienstag, 19. März 13
Group 2: Some small increase in debt at relatively low levels

Headline deficit, percent of GDP

Deviation from debt in 2007, percentage points of GDP

(General Government)
Group 2: Some small increase in debt at relatively low levels

(General Government)

<table>
<thead>
<tr>
<th>Year</th>
<th>AUS</th>
<th>AUT</th>
<th>CAN</th>
<th>NDL</th>
<th>SVK</th>
<th>AUT</th>
<th>NZL</th>
<th>SNK</th>
<th>EST</th>
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<td>0.0</td>
</tr>
</tbody>
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Dienstag, 19. März 13
Group 2: Some small increase in debt at relatively low levels

(General Government)

Headline deficit, percent of GDP

Deviation from debt in 2007, percentage points of GDP
Group 2: Some small increase in debt at relatively low levels

[Graph showing deviation from debt in 2007 and headline deficit, percent of GDP for various countries.]
Group 2: Some small increase in debt at relatively low levels

(General Government)

Deviation from debt in 2007, percentage points of GDP

Headline deficit, percent of GDP
Group 2: Some small increase in debt at relatively low levels
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(General Government)

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<thead>
<tr>
<th>Country</th>
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Dienstag, 19. März 13
Group 2: Some small increase in debt at relatively low levels
Group 3: Debt higher than 90 percent of GDP and rising

(General Government)
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(General Government)

Dienstag, 19. März 13
Group 3: Debt higher than 90 percent of GDP and rising

(General Government)
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Dienstag, 19. März 13
Group 3: Debt higher than 90 percent of GDP and rising

(General Government)

Deviation from debt in 2007, percentage points of GDP

2011
Group 3: Debt higher than 90 percent of GDP and rising

(General Government)

Headline deficit, percent of GDP

Deviation from debt in 2007, percentage points of GDP

2012

GRC ITA JPN GBR FRA PRT ESP USA IRL BEL

Dienstag, 19. März 13
Group 3: Debt higher than 90 percent of GDP and rising

(General Government)

Headline deficit, percent of GDP

Deviation from debt in 2007, percentage points of GDP

2013
Group 3: Debt higher than 90 percent of GDP and rising

Dienstag, 19. März 13
Group 3: Debt higher than 90 percent of GDP and rising

(General Government)

2013

70 % of Advanced Economies and 43 % of world GDP

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UK: Illustrative Adjustment Needs: 60% of GDP by 2030

2013-30 Cyclically Adjusted Primary Balance, percent of GDP

2013-30 Gross Debt, percent of GDP

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Across Different Scenarios: CAPB in 2030 and Required Adjustment Needs, 2013-30

2030, CAPB

2013-20, Required Adjustment

- Italy
- Portugal
- Ireland
- Spain
- Belgium
- United Kingdom
- United States
- France
Across Different Scenarios: CAPB in 2030 and Required Adjustment Needs, 2013-30

2013-20, Required Adjustment

2030, CAPB

Japan
Increase in Entitlement Spending, 2010-30

(Percentage points of GDP)
Two Requirements to Ensure a Low $r-g$

- Structural reforms to raise potential growth
Effects on debt of boosting growth by 1 percentage point

Debt, percent of GDP vs. Year

Dienstag, 19. März 13
Effects on debt of boosting growth by 1 percentage point

Dienstag, 19. März 13
Two Requirements to Ensure a Low $r-g$

- Structural reforms to raise potential growth
Two Requirements to Ensure a Low $r-g$

- Structural reforms to raise potential growth
- Strategy to keep interest rates under control
Four Components to Keep Interest Rates Low:
Four Components to Keep Interest Rates Low:

Medium-term fiscal plan and strong fiscal institutions
Four Components to Keep Interest Rates Low:

Medium-term fiscal plan and strong fiscal institutions

Average CDS Spreads, 2008-11

High Income
Middle Income

Linear (High Income)
Linear (Middle Income)

R² = 0.25032
R² = 0.04893

IMF Index of Fiscal Transparency
Four Components to Keep Interest Rates Low:

Medium-term fiscal plan and strong fiscal institutions
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Medium-term fiscal plan and strong fiscal institutions
Four Components to Keep Interest Rates Low:

- **Medium-term fiscal plan and strong fiscal institutions**
- **Appropriate pace of fiscal adjustment**

Dienstag, 19. März 13
Four Components to Keep Interest Rates Low:

Appropriate pace of fiscal adjustment
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- Appropriate pace of fiscal adjustment
- Magnitude of the initial fiscal imbalances
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- Magnitude of the initial fiscal imbalances
- Intensity of market pressures
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- Appropriate pace of fiscal adjustment
- Magnitude of the initial fiscal imbalances
- Intensity of market pressures
- State of the economy
Four Components to Keep Interest Rates Low:

- Medium-term fiscal plan and strong fiscal institutions
- Appropriate pace of fiscal adjustment
Four Components to Keep Interest Rates Low:

- Medium-term fiscal plan and strong fiscal institutions
- Appropriate pace of fiscal adjustment
- Appropriate tools to implement fiscal adjustment
Four Components to Keep Interest Rates Low:

Appropriate tools to implement fiscal adjustment
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Fiscal tools should make fiscal adjustment credible and conducive to growth
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Appropriate tools to implement fiscal adjustment

Fiscal tools should make fiscal adjustment credible and conducive to growth

Need to reform entitlement spending
Four Components to Keep Interest Rates Low:

- Medium-term fiscal plan and strong fiscal institutions
- Appropriate pace of fiscal adjustment
- Appropriate tools to implement fiscal adjustment
Four Components to Keep Interest Rates Low:

- Medium-term fiscal plan and strong fiscal institutions
- Appropriate pace of fiscal adjustment
- Appropriate tools to implement fiscal adjustment
- Relaxed monetary policy
United Kingdom: Financing of deficit by BoE

Flow of Central Bank Financing Over Deficit, percent

2009-12
Thank you!