Fiscal Policy for a Changing Global Economy

Elif Ture
Economist
Fiscal Affairs Department
Main Messages

Chapter 1: Fiscal Policy for a Changing Global Economy

• Amid slowing global growth and elevated public debt, prepare for the next downturn, balancing growth and sustainability objectives.

• Upgrade fiscal policy to adapt to shifting demographics, advancing technology, and rising global economic integration.

• Sustainable and inclusive growth requires improving tax-transfer policies, and more and better investment in people and infrastructure.

Chapter 2: Curbing Corruption

• Fight corruption by building strong and transparent fiscal institutions that promote integrity and accountability.
A Fast-Changing Global Economy
Global growth has slowed, and projected recovery is precarious.

### Real GDP Growth, 2017-20 (Percent)

<table>
<thead>
<tr>
<th>Year</th>
<th>Advanced Economies</th>
<th>Emerging Market Economies</th>
<th>Low-Income Developing Countries</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2.4</td>
<td>4.9</td>
<td>5.0</td>
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<tr>
<td>2017</td>
<td>2.2</td>
<td>4.6</td>
<td>4.6</td>
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<td>2018</td>
<td>1.8</td>
<td>4.3</td>
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<tr>
<td>2019</td>
<td>1.7</td>
<td>4.8</td>
<td>5.2</td>
</tr>
<tr>
<td>2020</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: IMF, April 2019 World Economic Outlook.
Fiscal expansions since the global financial crisis have yet to be reversed.

General Government Fiscal Stance and Cyclical Position, 2007-18

Advanced Economies

- Structural primary balance (percent of potential GDP)
- Output gap (percent)

Emerging Market Economies

- Primary balance (percent of GDP)
- Primary balance in 2009 (GFC)
- GDP growth rate (percent, right scale)

Low-Income Developing Countries

- Primary balance (percent of GDP)
- GDP growth rate (percent, right scale)

Source: IMF, World Economic Outlook database.

Note: The averages are weighted by PPP-adjusted nominal GDP in US dollars. GFC = global financial crisis; PPP = purchasing power parity.
Public debt vulnerabilities are higher today than before the financial crisis.


**Advanced Economies**

**Emerging Market Economies**

**Low-income Developing Countries**

Source: IMF, World Economic Outlook database.
Meanwhile, per capita income growth has trended down and inequality remains a concern.

Real GDP per Capita Growth and Income Inequality, 1970-2018 (Percent)

Advanced Economies

Emerging Market Economies

Low-income Developing Countries

Sources: IMF, World Economic Outlook database; Standardized World Income Inequality Database; and IMF staff estimates.

Note: The averages are weighted by PPP-adjusted nominal GDP in US dollars. PPP = purchasing power parity.
Shifting demographics are straining public finances.

Old-Age Dependency Ratio, Population Growth, and the Median Age, 1950-2050

Advanced Economies

Emerging Market Economies

Low-income Developing Countries

Source: UN World Population Prospects.
Rapid technological progress has favored some and left out many.

Evolution of Labor Income Shares since 1995 (Percent of GDP)

By Country, 1995 vs 2014

By Skill Level, 1995-2009

Advanced Economies: Shifting Gears to Fiscal Easing
Advanced economies has shifted gears to near-term fiscal easing.

**Advanced Economies: General Government Deficit and Debt (Percent of GDP)**

**Structural Primary Balance, 2012-24**

- Italy
- Euro area
- United Kingdom
- United States
- Japan
- AEs 25th percentile
- AEs 75th percentile

**Drivers of Change in Debt, 2007-18**

- Nominal exchange rate
- Inflation
- Stock-flow adjustment
- Change in debt to GDP
- Primary deficit

Source: IMF, World Economic Outlook database.
Note: AEs = advanced economies.

Sources: IMF, World Economic Outlook database; and IMF staff estimates.
Interest rates are at historic lows but risk sentiment could shift abruptly.

Advanced Economies: Interest Rates (Percent)

10-Year Bond Yields, 2007-19

Projected Growth-Adjusted Interest Rates, 2019-24

Source: Bloomberg, IMF World Economic Outlook database.
Over the medium term most plan to adjust, yet some will see debt rising.

Advanced Economies: Change in General Government Deficit and Debt Burden (Percent of GDP)

Structural Primary Balance, 2018-24

Gross Debt and Interest Bill, 2018-24

Source: IMF, World Economic Outlook database.
Note: Data labels in the figure use International Organization for Standardization (ISO) country codes. MT = medium term; ST = short term.
Emerging Markets: Consolidation on Hold
Emerging market economies are pausing fiscal consolidation.

### Emerging Market Economies: General Government Deficit and Debt (Percent of GDP)

#### Overall Balance, 2012-24

- **EMMIEs**
- **Oil exporters**
- **Non-oil exporters**

#### Gross Debt, 2012-24

- **EMMIEs**
- **Oil exporters**
- **Non-oil exporters**

*Source: IMF, World Economic Outlook database.*
Financial conditions tightened in 2018, adding to public debt levels.

Emerging Market Economies: Change in Public Debt Burden, 2018

10-year US Dollar Bond Yields, 2018-19 (Percent)

Drivers of Change in Debt, 2017-18 (Percent of GDP)

Source: Bloomberg Finance L.P.
Note: AEs = advanced economies; EMMIEs = emerging market and middle-income economies; G20* Group of Twenty.

Source: IMF, World Economic Outlook database.
Despite recent easing, emerging markets remain vulnerable to rapid changes in financial conditions.

Emerging Market Economies: Impact of Tighter Financial Conditions on Public Finances

Spread over 10-year US Treasury Bond Yields, 2018-19
(Basis points)

Response to Potential Stress in Global Financial Markets
(Percentage points of GDP)

Source: Bloomberg Finance L.P.

Note: bps = basis points; EM = emerging market. Data labels in the figure use International Organization for Standardization (ISO) country codes.

Actual sovereign spreads as of March 29, 2019.
Low-Income Developing Countries: Fiscal Expansion Slows
Deficits and debt seem to have stabilized in low-income developing countries.

Low-Income Developing Countries: General Government Deficit and Debt (Percent of GDP)

Overall Balance, 2012-24

Gross Debt, 2012-24

Source: IMF, World Economic Outlook database.
Note: LIDCs = low-income developing countries.
Yet, risk of debt distress is higher and debt service consumes ever more taxes.
Quality of spending has worsened, while facing large development needs.

Low-Income Developing Countries: General Government Spending Trends and Needs (Percent of GDP)

Change in Expenditure, 2012 vs 2018

Spending Needed to Achieve SDGs, 2030

Source: IMF, World Economic Outlook database.
Note: LIDCs = low-income developing countries.

Source: Gaspar and others (2019).
SETTING THE RIGHT COURSE
FOR FISCAL POLICY
PREPARE FOR THE NEXT DOWNTURN...

...BALANCING GROWTH AND SUSTAINABILITY OBJECTIVES
Fiscal restraint is required for most, but there are exceptions.

High debt economies need to rebuild buffers, particularly if

- Output exceeds potential (United States)
- Borrowing costs are high and financing needs are large (Brazil, Italy)
- Enhancing market access remains important (Argentina)

Limited, high-quality fiscal stimulus is warranted, if

- There is fiscal space and risk of a sharper slowdown (Germany, Korea)
- Coupled with a credible medium term adjustment plan (China, Japan)

LIDCs should support development objectives, particularly if

- Financing conditions permit (Myanmar, Tanzania).

Fiscal easing should complement monetary accommodation, if

- A severe and prolonged downturn depresses inflation outlook (euro area)

China should avoid large-scale, investment-led, off-budget stimulus with low returns (Percent)

Sources: CEIC; China Public Finance Statistical Yearbook; Li and Mano 2019; and IMF staff estimates.
ADAPT TO GLOBAL TRENDS...

...BY INCLUSIVE & GROWTH-FRIENDLY BUDGET RECOMPOSITION
1- Shift expenditures to high quality investment in physical and human capital.

Net Acquisition of Non-Financial Assets (*Percent of GDP*)

![Net Acquisition of Non-Financial Assets Graph](image)

Source: IMF, World Economic Outlook database.

Additional Spending Needed to Achieve SDGs (*Percent of GDP*)

![Additional Spending Needed to Achieve SDGs Graph](image)

Note: Increase only reflects additional spending need for 1/ electricity 2/ roads. Source: Gaspar and others (2019).
2- Cut wasteful subsidies to make room for productive investment.

Energy Subsidies, 2017 (Percent of GDP)

Efficient Fuel Pricing

Raising fuel prices gradually to efficient levels through taxes could generate additional revenue of up to $3.2 trillion (4 percent of global GDP) over the long-term.

Source: Coady and others, forthcoming.
3- Expand the budget envelope thru PFM reforms and revenue mobilization.

It's not only what you owe, it's also what you own…

Better management of public financial assets and nonfinancial corporations could yield up to 3 percent of GDP a year in additional revenue.

Tax Revenue, 2017 (Percent of GDP)

Source: Gaspar and others 2019.
4- Enhance international cooperation, including to avoid tax wars.

**Profit Shifting, 2013**

<table>
<thead>
<tr>
<th></th>
<th>Non-OECD</th>
<th>OECD</th>
<th>Non-OECD</th>
<th>OECD</th>
</tr>
</thead>
<tbody>
<tr>
<td>In billions of USD</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In percent of GDP</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Crivelli, De Mooij, and Keen (2016).

**Tax Competition: CIT Rates, 1990-2018 (Percent)**

Source: IMF Fiscal Affairs Department Tax Policy Rates Database.

**BEPS helps but incomplete, digitalization intensifies challenges, unilateral measures undermine cooperation…**

**Alternative futures, several now at the table of OECD:**

- **Minimum tax proposals:** Close to current arrangements, but susceptible to unilateral action.
- **Move to destination-based taxation:** Effective, but legally difficult, adverse spillovers if unilateral.
- **Move to formulary apportionment:** Addresses profit shifting, but not tax competition. Requires much coordination.
CURBING CORRUPTION
Corruption in government is like a house with leaking pipes.

What is Corruption?

**Definition**

The abuse of public office for private gain.

**Types**

Administrative (uses laws for private gain)

State capture (alters laws for private gain)

**Measurement**

Control of corruption index based on surveys of perception
Corruption makes tax and spending policies less effective and fair.

Corrupt Countries Collect Less Tax

The least corrupt governments collect 4% of GDP more in tax revenues than countries with the highest levels of corruption.

Corruption prevents people from benefiting fully from the wealth created by their country's natural resources.

Learn more in the latest Fiscal Monitor.
Corruption siphons taxpayers’ money away from schools, hospitals, roads...

Corruption hurts education
Students in countries with less corruption have higher test scores.
(test scores; global average = 100)

Sources: Patrinos and Angrist (2018); Worldwide Governance Indicators; and IMF staff estimates.
Note: Test scores for school-age students are harmonized across sources. The correlation remains significant when controlling for other factors, including GDP per capita.

An emerging market with low corruption wastes public spending half as much as does one with high corruption.

Learn more in the latest Fiscal Monitor.
Fighting corruption requires political will to build strong and transparent institutions that promote integrity and accountability.

<table>
<thead>
<tr>
<th>Fiscal institutions that matter for corruption control</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Tax Complexity (time)</strong></td>
</tr>
<tr>
<td><strong>Red Tape (time)</strong></td>
</tr>
<tr>
<td><strong>Red Tape (procedures)</strong></td>
</tr>
<tr>
<td><strong>Time for VAT Refund</strong></td>
</tr>
<tr>
<td><strong>Labor Tax Rate</strong></td>
</tr>
<tr>
<td><strong>Time for Tax Audit</strong></td>
</tr>
<tr>
<td><strong>Fiscal Transparency</strong></td>
</tr>
</tbody>
</table>

Note: Bold cells denote institutions that are statistically significant after controlling for GDP per capita.
Source: IMF staff estimates, Orbis, Worldwide Governance Indicators.
Policymakers need to put fiscal houses in order, by

• **Preparing for the next downturn**, balancing growth and sustainability objectives. This means rebuilding buffers for most high debt economies.

• **Upgrading tax and spending policies** to adapt to shifting demographics and advancing technology in an ever-integrating global economy.

• **Fighting corruption** through strong and transparent fiscal institutions that promote integrity and accountability.

• **Enhancing international cooperation** to mitigate tax avoidance, climate change, and corruption, and to achieve the SDGs.
### Table 1.1. General Government Fiscal Balance, 2012–24: Overall Balance (Percent of GDP)

<table>
<thead>
<tr>
<th>Year</th>
<th>Projections</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>-3.7</td>
</tr>
<tr>
<td>2013</td>
<td>-2.8</td>
</tr>
<tr>
<td>2014</td>
<td>-3.2</td>
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<tr>
<td>2015</td>
<td>-3.4</td>
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<tr>
<td>2016</td>
<td>-3.4</td>
</tr>
<tr>
<td>2017</td>
<td>-2.9</td>
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<tr>
<td>2018</td>
<td>-3.1</td>
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<tr>
<td>2019</td>
<td>-3.1</td>
</tr>
<tr>
<td>2020</td>
<td>-3.1</td>
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<tr>
<td>2021</td>
<td>-3.1</td>
</tr>
<tr>
<td>2022</td>
<td>-3.0</td>
</tr>
<tr>
<td>2023</td>
<td>-2.9</td>
</tr>
<tr>
<td>2024</td>
<td>-2.9</td>
</tr>
</tbody>
</table>

### Table 1.2. General Government Debt, 2012–24 (Percent of GDP)

<table>
<thead>
<tr>
<th>Year</th>
<th>Projections</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>7.8</td>
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<tr>
<td>2013</td>
<td>7.4</td>
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<tr>
<td>2014</td>
<td>7.8</td>
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<tr>
<td>2015</td>
<td>8.2</td>
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<td>2016</td>
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<td>2017</td>
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<td>8.3</td>
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<td>8.3</td>
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<td>2022</td>
<td>8.4</td>
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<tr>
<td>2023</td>
<td>8.5</td>
</tr>
<tr>
<td>2024</td>
<td>8.5</td>
</tr>
</tbody>
</table>

**Note:** All country averages are weighted by nominal GDP converted to US dollars (adjusted by purchasing power parity only for world output) at average market exchange rates in the years indicated and based on data availability. Projections are based on IMF staff assessments of current policies. In many countries, 2016 data are still preliminary. For country-specific details, see "Data and Concepts" and Tables A, B, C, and D in the Methodological and Statistical Appendix.

1 For cross-country comparability, expenditure and fiscal balances of the United States are adjusted to exclude the imputed interest on unfunded pension liabilities and the imputed compensation of employees, which are counted as expenditures under the 2008 System of National Accounts (2008 SNA) adopted by the United States, but not in countries that have not yet adopted the 2008 SNA. Data for the United States in this table may thus differ from data published by the US Bureau of Economic Analysis.

2 Including financial sector support.

**Source:** IMF staff estimates and projections.

**Note:** All country averages are weighted by nominal GDP converted to US dollars (adjusted by purchasing power parity only for world output) at average market exchange rates in the years indicated and based on data availability. Projections are based on IMF staff assessments of current policies. In many countries, 2016 data are still preliminary. For country-specific details, see "Data and Concepts" and Tables A, B, C, and D in the Methodological and Statistical Appendix.

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2 Including financial sector support.
<table>
<thead>
<tr>
<th></th>
<th>2010</th>
<th>2020</th>
<th>2021</th>
<th>2019</th>
<th>2020</th>
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<tbody>
<tr>
<td></td>
<td>Maturing Debt</td>
<td>Budget Deficit</td>
<td>Total Financing Need</td>
<td>Maturing Debt</td>
<td>Budget Deficit</td>
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<tr>
<td><strong>Australia</strong></td>
<td>1.6</td>
<td>1.5</td>
<td>5.0</td>
<td>2.6</td>
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<td>3.3</td>
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<td><strong>Germany</strong></td>
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<td>-0.7</td>
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<td>9.5</td>
<td>7.4</td>
<td>1.1</td>
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<td>20.5</td>
<td>4.6</td>
<td>25.1</td>
<td>20.5</td>
<td>4.4</td>
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<tr>
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<td>16.5</td>
<td>2.6</td>
<td>16.1</td>
<td>16.5</td>
<td>2.4</td>
</tr>
</tbody>
</table>

**Sources:** Bloomberg Financial L.P. and IMF staff estimates and projections.

**Note:** For another countries, data on maturing debt is based on general government debt, which includes debt from different levels of government. For country-specific details, see “Data and Conventions,” and Table 3 in the “Methodological and Statistical Appendix.”

1 Assumes that short-term debt outstanding in 2019 and 2020 will be financed with new short-term debt maturing in 2020 and 2021, respectively. Countries are divided into three groups based on their medium-term debt maturing in 2019 and 2020: (1) countries whose debt maturing in 2019 and 2020 is less than 50% of their general government debt outstanding at the end of 2019;

2 Data refers to general government debt, which includes debt from different levels of government.

3 For cross-country comparability, expenditure and fiscal balance of the United States is adjusted to exclude the imputed interest on unfunded pension liabilities and the imputed compensation of employees, which are counted as expenditures under the 2010 System of National Accounts (2010 SNA) adopted by the United States, but not in countries that have not yet adopted the 2008 SNA. Data for the United States in this table may thus differ from data published by the US Bureau of Economic Analysis.

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<table>
<thead>
<tr>
<th></th>
<th>2019</th>
<th>2020</th>
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<tr>
<td></td>
<td>Maturing Debt</td>
<td>Budget Deficit</td>
</tr>
<tr>
<td><strong>Argentina</strong></td>
<td>12.7</td>
<td>2.7</td>
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<tr>
<td><strong>Brazil</strong></td>
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<td>7.3</td>
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<td><strong>Chile</strong></td>
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<td><strong>United States</strong></td>
<td>16.2</td>
<td>2.7</td>
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<tr>
<td><strong>Average</strong></td>
<td>6.1</td>
<td>3.8</td>
</tr>
</tbody>
</table>

**Sources:** IMF staff estimates and projections.

**Note:** Data in the table refer to general government data. For some countries, general government deficits are reported on an accrual basis. For country-specific details, see “Data and Conventions,” and Table 3 in the “Methodological and Statistical Appendix.”

1 Assumes that short-term debt outstanding in 2019 and 2020 will be financed with new short-term debt maturing in 2020 and 2021, respectively. Countries are divided into three groups based on their medium-term debt maturing in 2019 and 2020: (1) countries whose debt maturing in 2019 and 2020 is less than 50% of their general government debt outstanding at the end of 2019;

2 Data refers to general government debt, which includes debt from different levels of government.

3 For cross-country comparability, expenditure and fiscal balance of the United States is adjusted to exclude the imputed interest on unfunded pension liabilities and the imputed compensation of employees, which are counted as expenditures under the 2010 System of National Accounts (2010 SNA) adopted by the United States, but not in countries that have not yet adopted the 2008 SNA. Data for the United States in this table may thus differ from data published by the US Bureau of Economic Analysis.