

# Fiscal Outlook in Advanced Countries



Carlo Cottarelli

Director

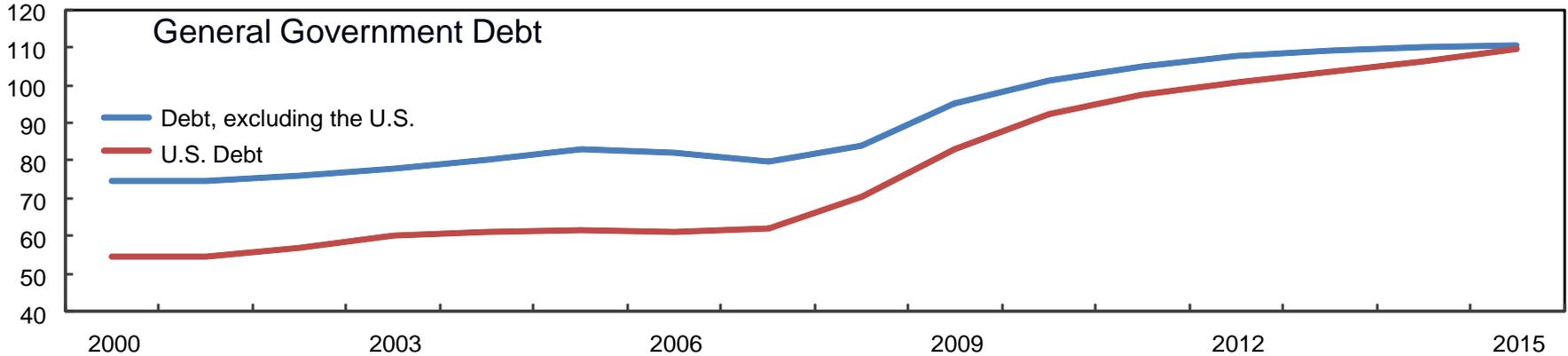
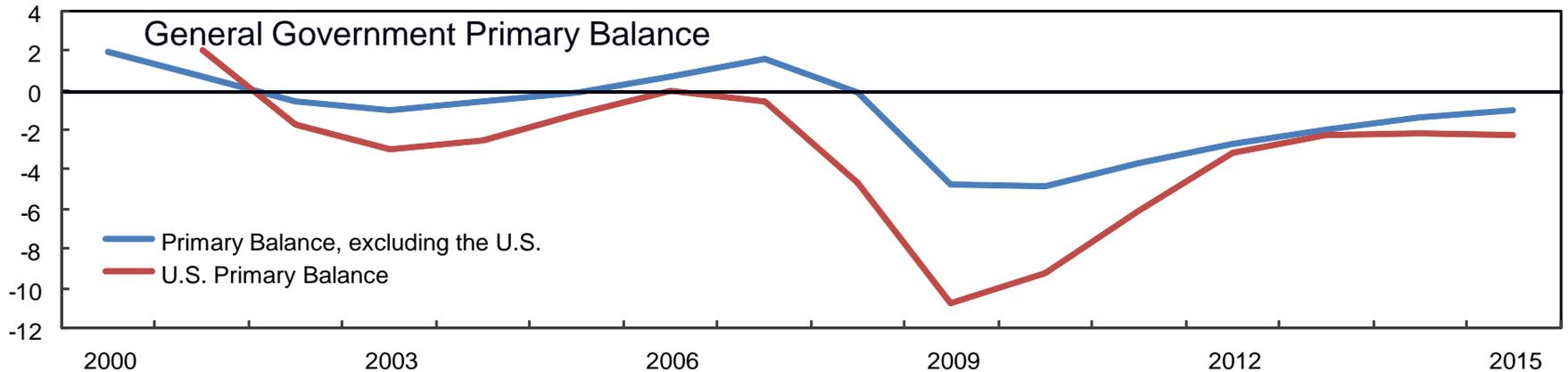
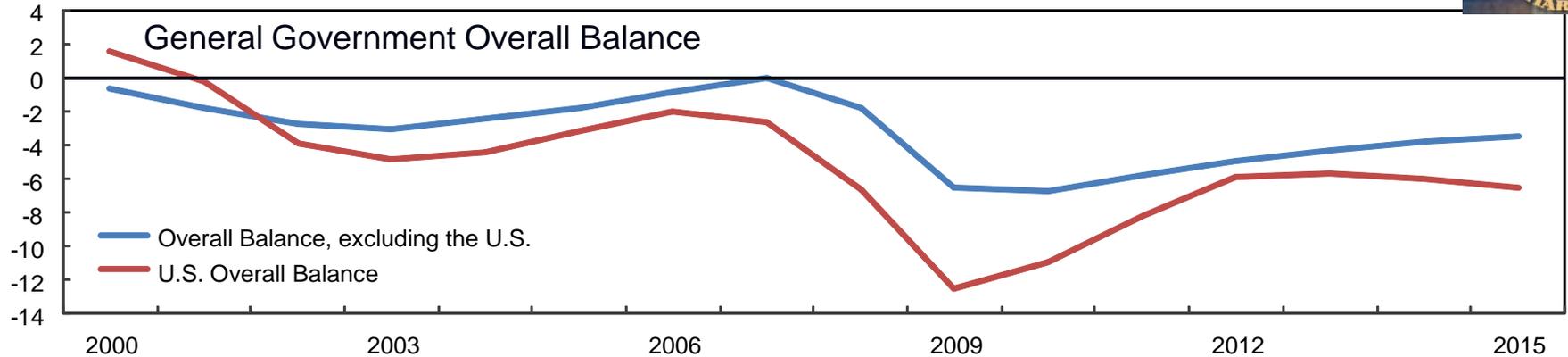
Fiscal Affairs Department

May 26, 2010

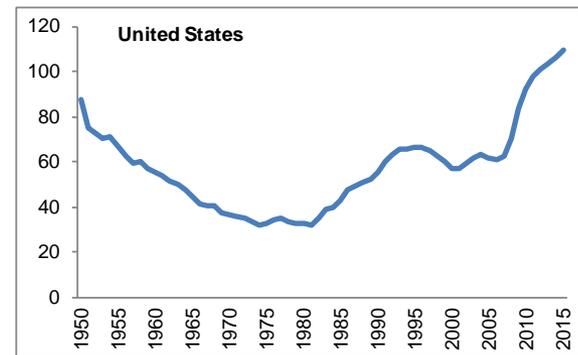
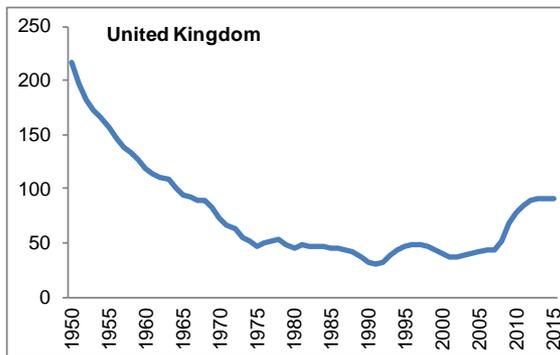
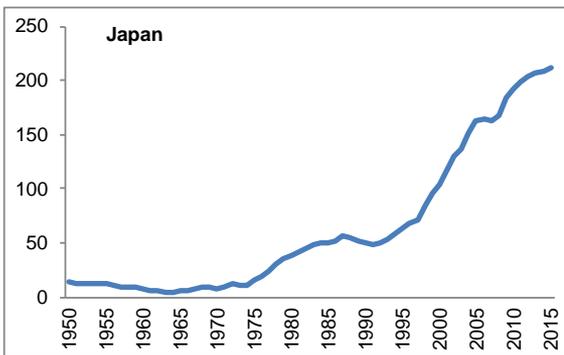
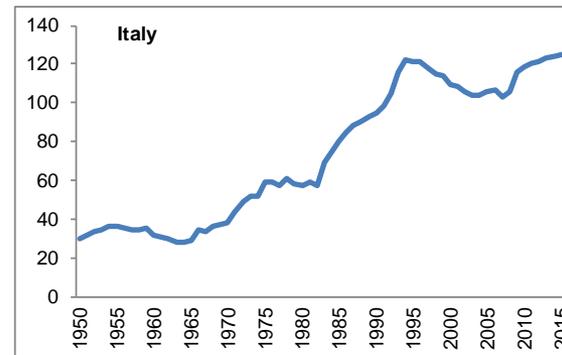
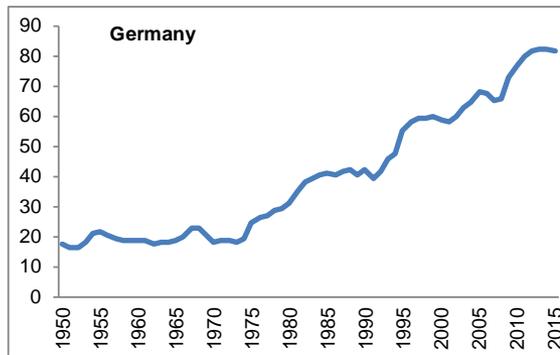
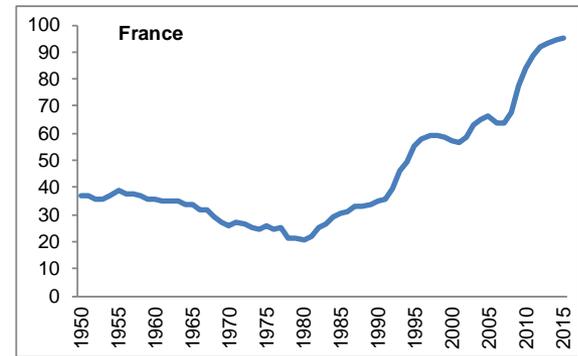
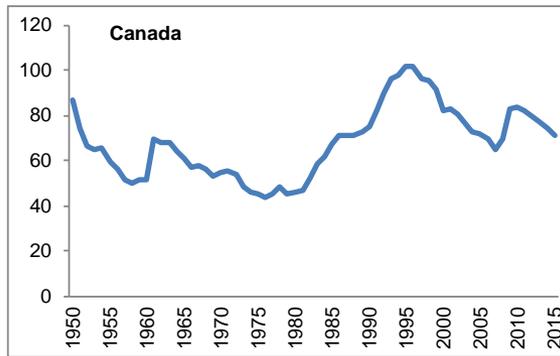
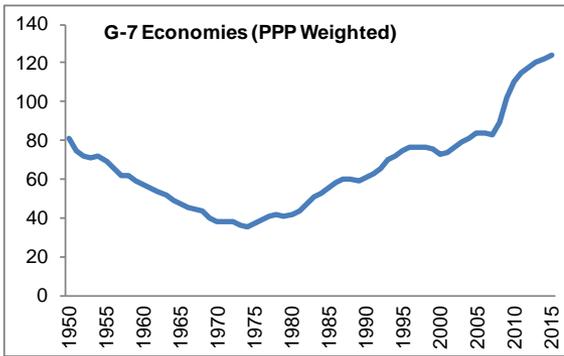
Washington, DC

# Fiscal Outlook in Advanced Economies

(In percent of GDP)



# General Government Gross Debt in G-7 Economies, 1950-2015 (In percent of GDP)





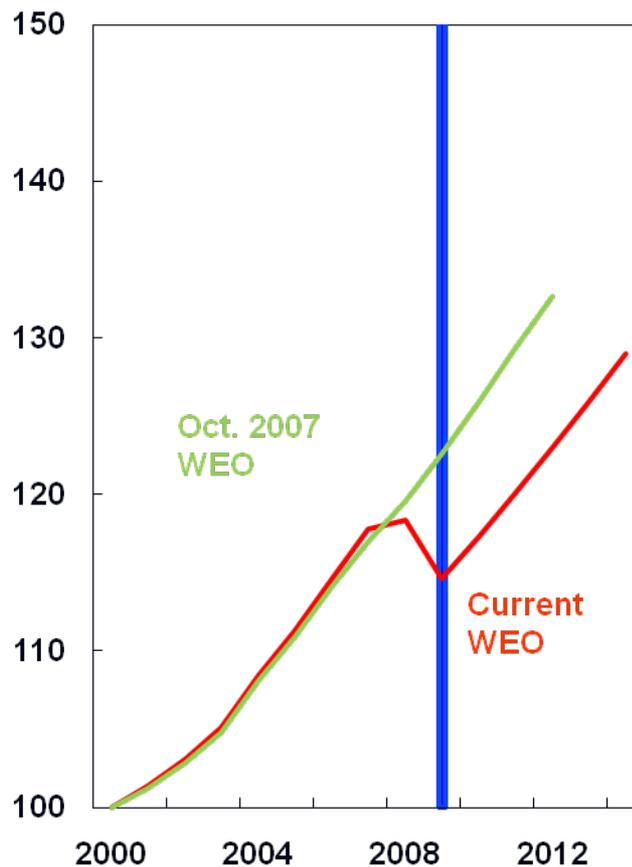
# Risks Around the Baseline Projections

- **Upside Risk:** Revenue could be higher.

# A Look at Output Levels



Advanced Economies  
Real GDP (In levels, 2000=100)





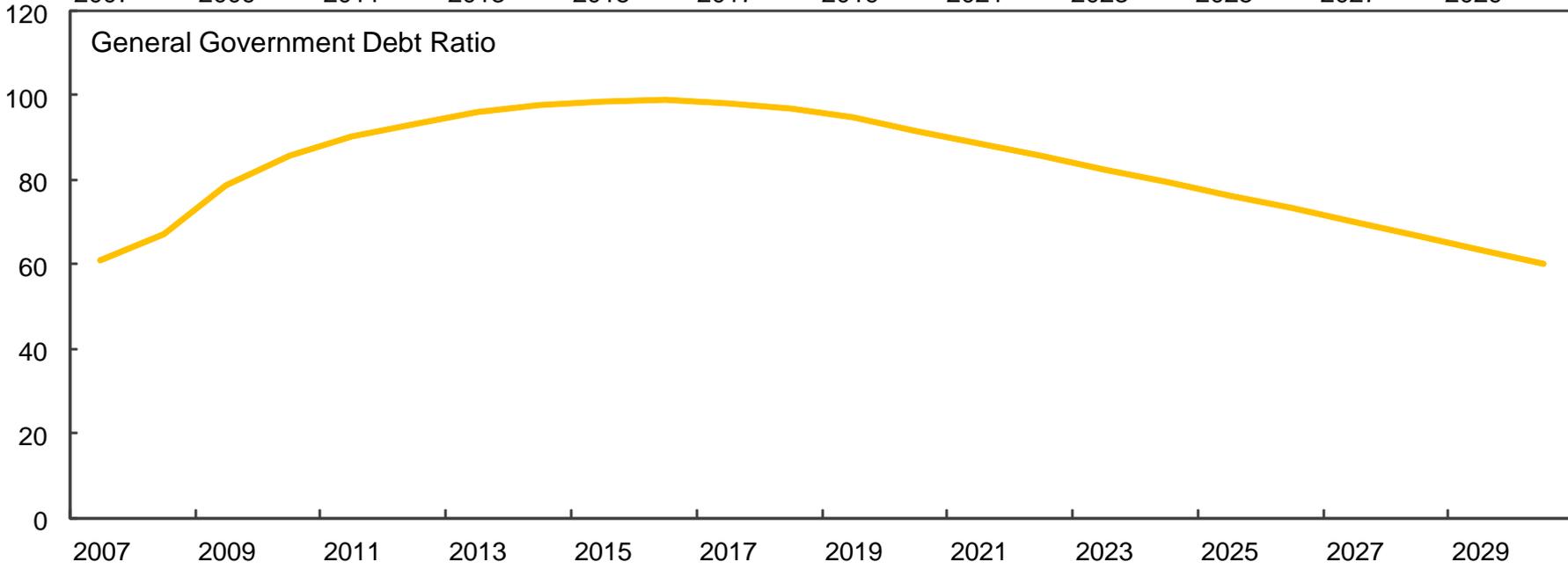
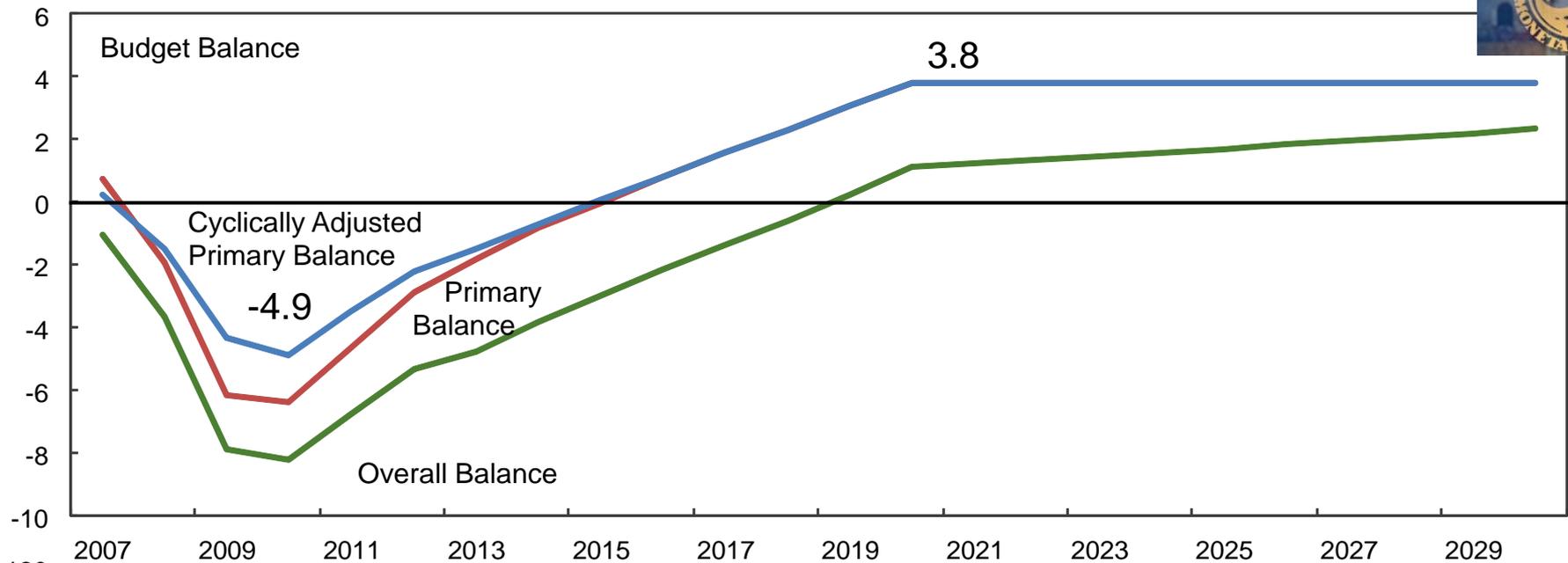
# Risks Around the Baseline Projections

- **Upside Risk:** Revenue could be higher.
- **Downside Risk:** Interest rate-growth differential could be higher.



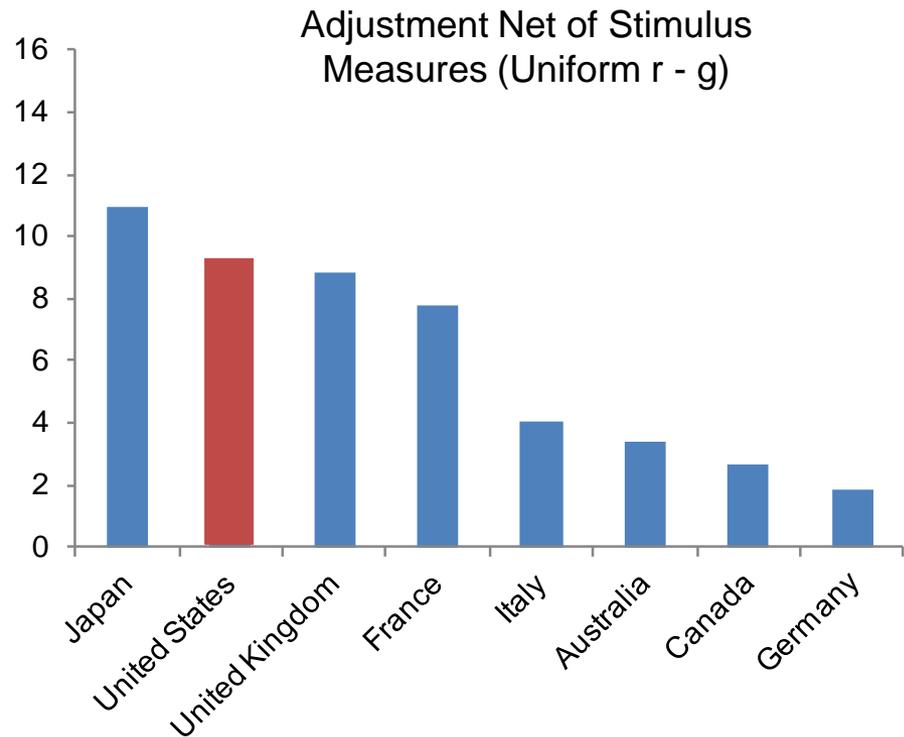
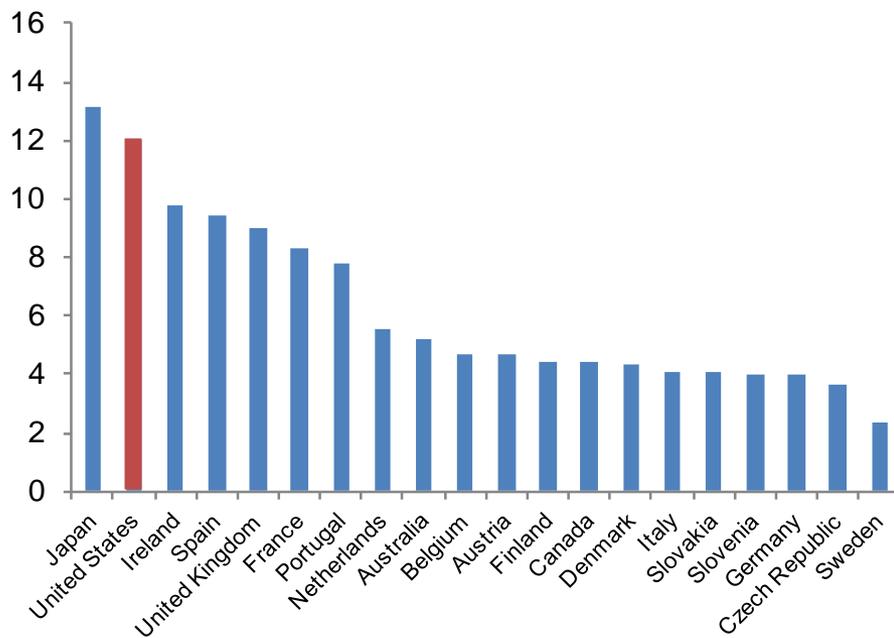
# Fiscal Balances in Advanced Economies

(In percent of GDP)

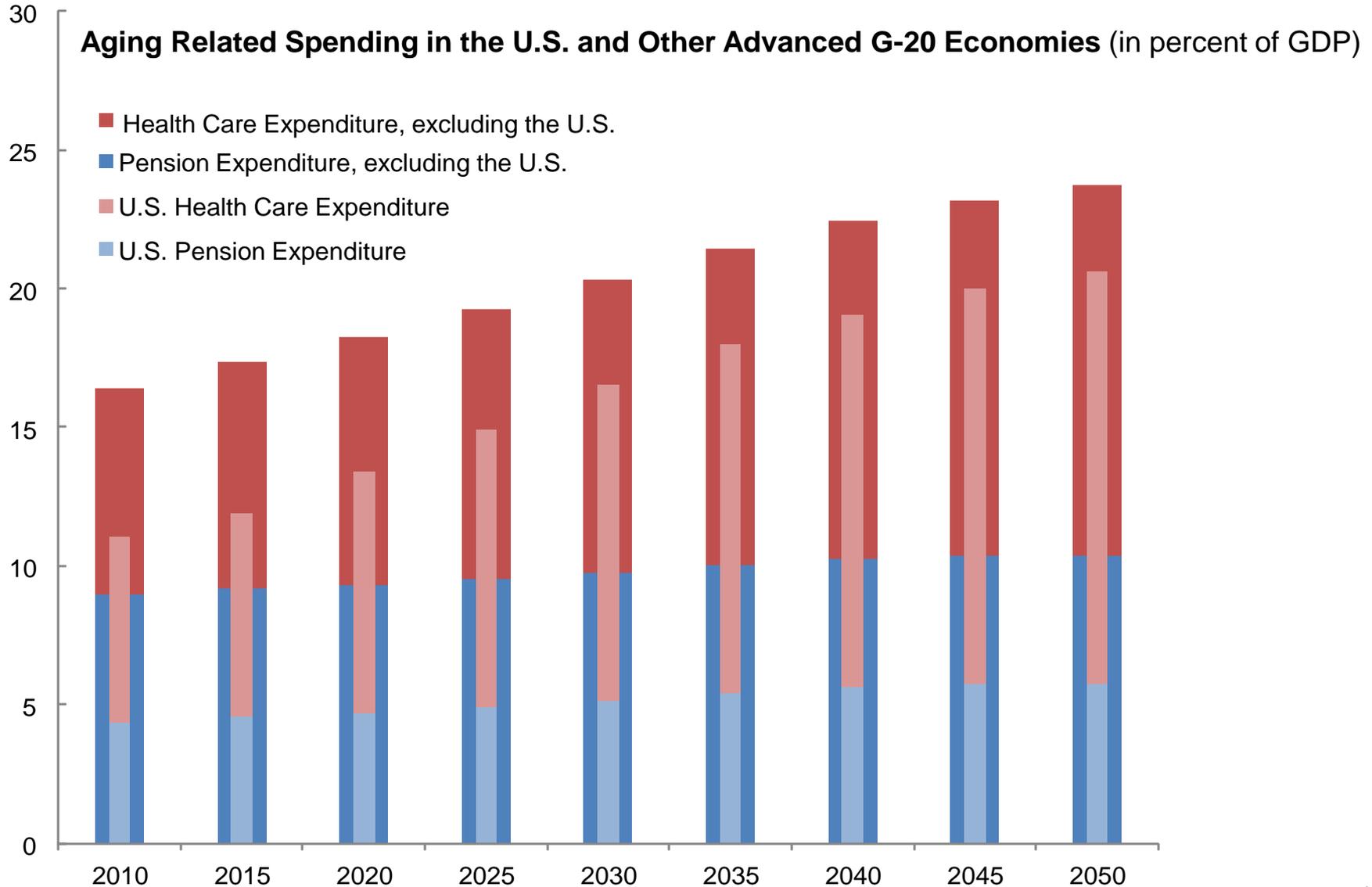




# Illustrative Fiscal Adjustment in Cyclically Adjusted Primary Balance, 2011–30



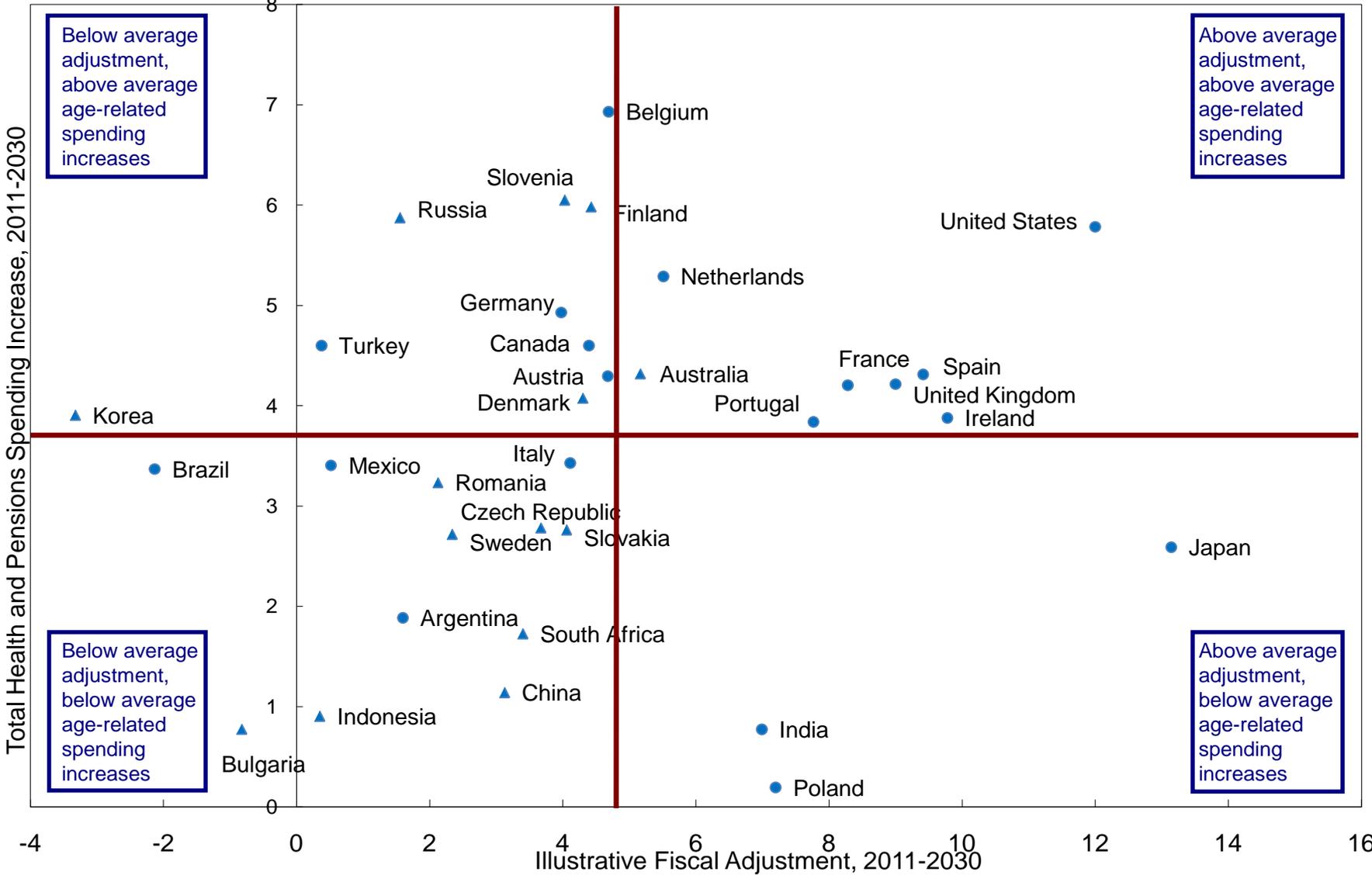
# Fiscal Challenge: Demographic Trends are Unfavorable



# Swimming Far and Against the Tide



Illustrative Fiscal Adjustment and Projected Age-Related Spending Increases in 2011–2030 (in percent of GDP)





**Thank you!**

# A Three-Pillar Strategy for Consolidation

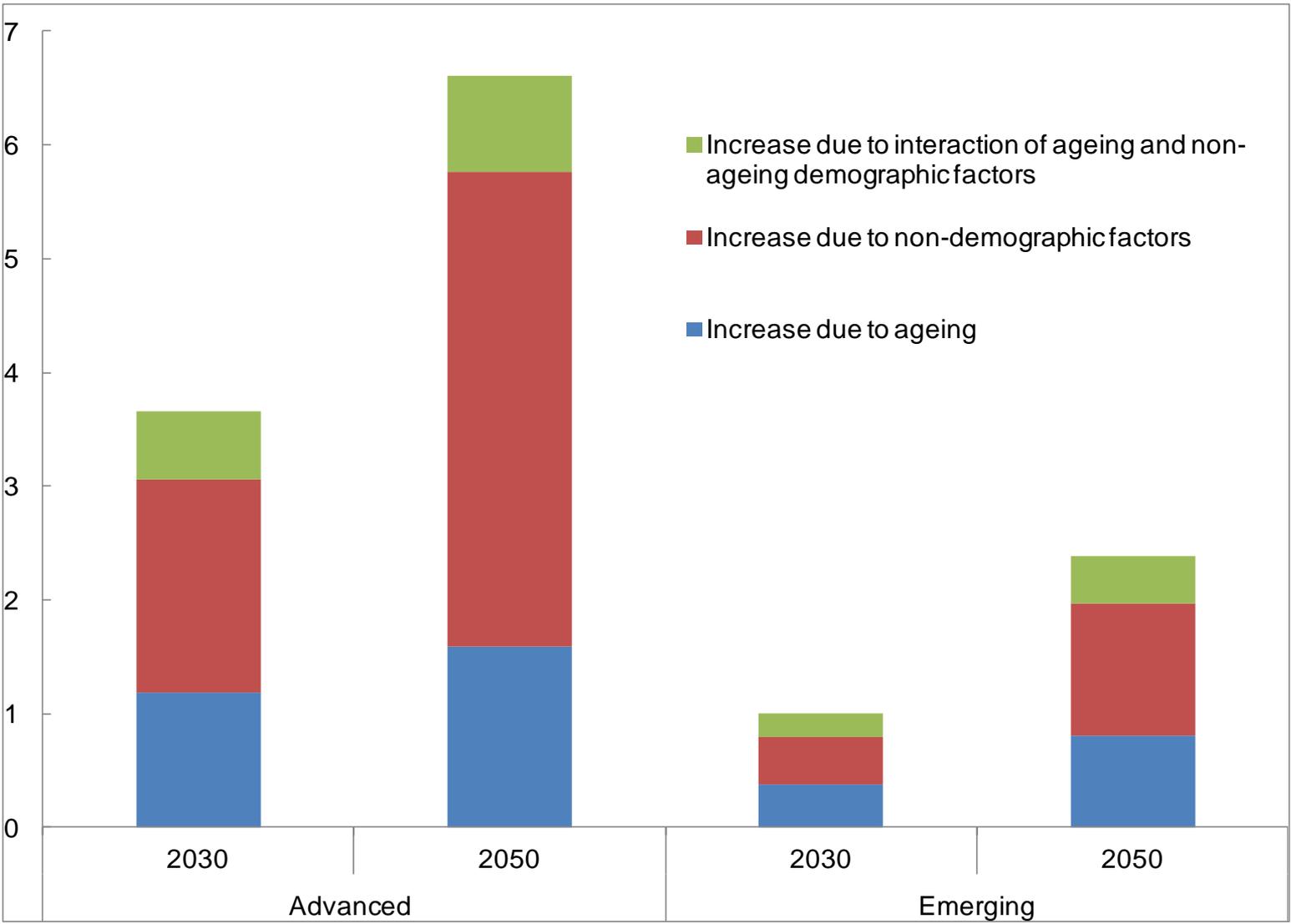


1. Stabilize age-related spending relative to GDP
2. Reduce non age-related spending relative to GDP
3. Raise additional revenues in an efficient and equitable manner

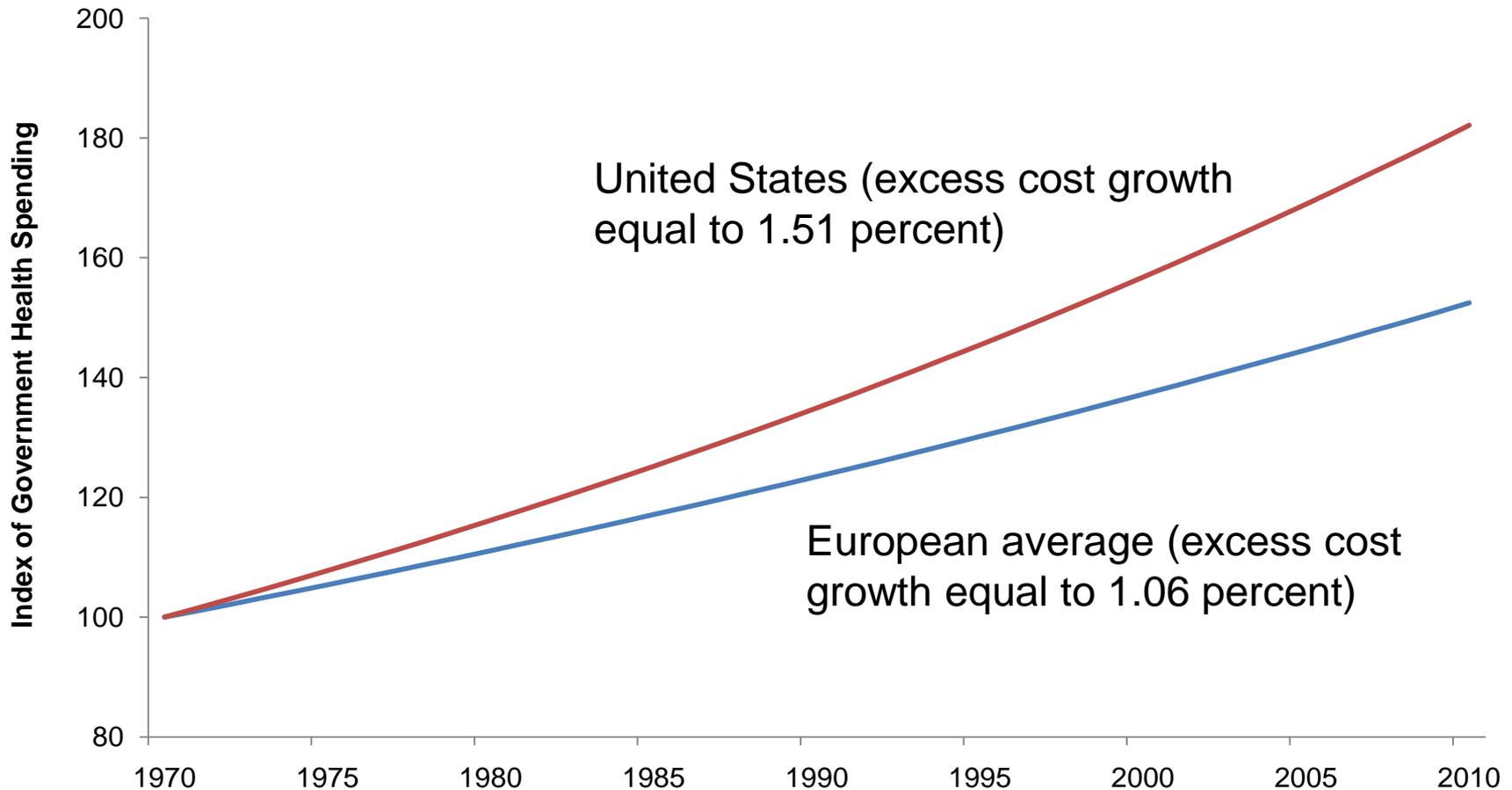


# Increase in Public Health Spending in Baseline Scenario

(In percent of GDP)



# Increase in Government Health Spending Due to Past Rates of Excess Cost Growth



Note: Data on excess cost growth derived from Christian Hagist and Laurence Kotlikoff, 2005, "Who's Going Broke? Comparing Healthcare Costs in 10 OECD Countries" NBER Working Paper 11833

# Supply-Side Measures to Contain Health Spending



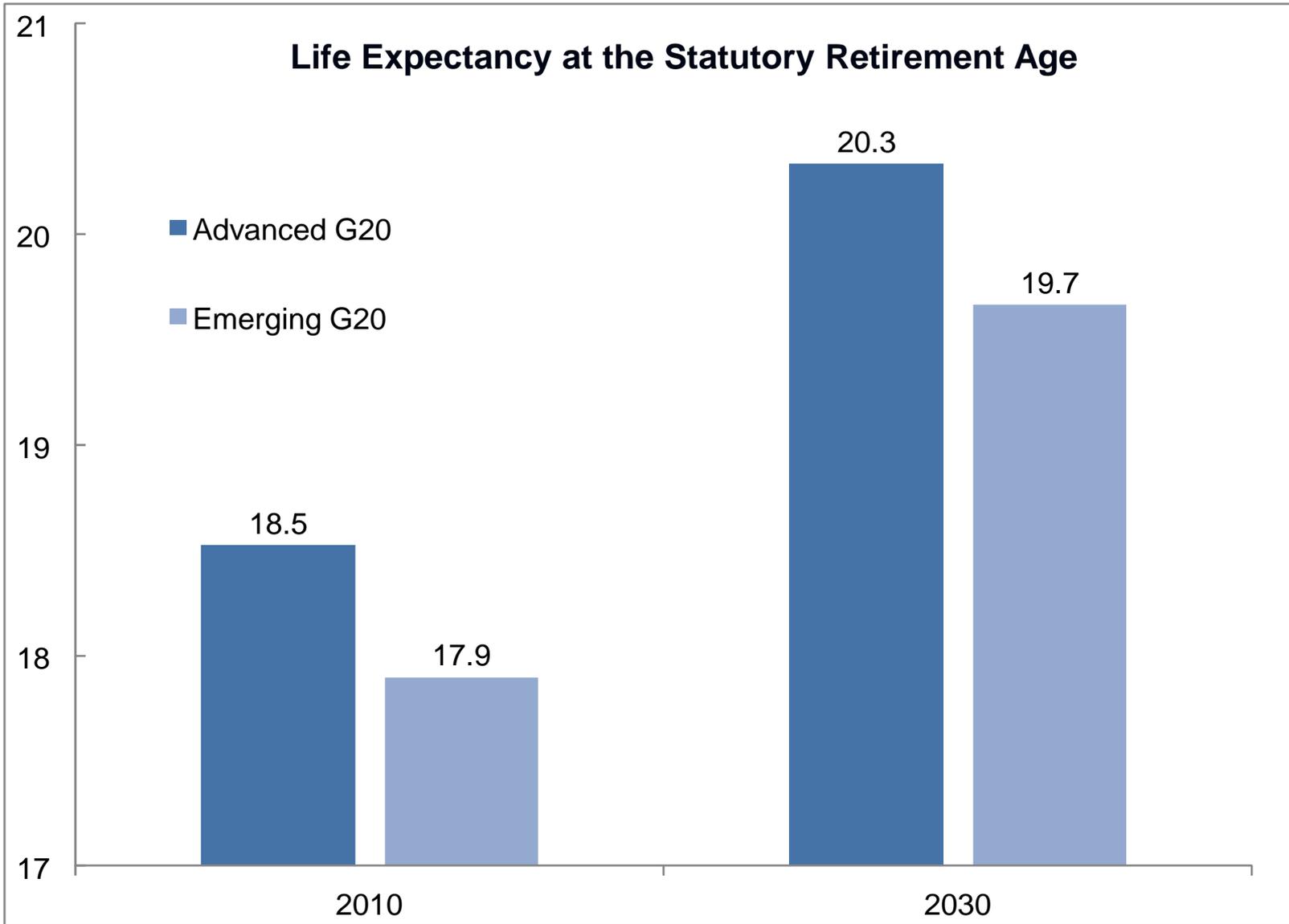
Measures	Rationale
<b>Reimburse providers based on case-based methods or global budgets</b>	Discourage unnecessary services
<b>Implement health information technology</b>	Greater efficiency in service delivery
<b>Strengthen cost-effectiveness analysis of treatments</b>	Improve allocative efficiency
<b>Reduce generosity of publicly financed benefits package</b>	Limit to what public funds can cover



# Demand-Side Measures to Contain Health Spending

Measures	Rationale
<b>Higher copayments</b>	Reduce incentives for excessive use
<b>Reduce tax expenditures for private health insurance</b>	Reduce incentives for excessive use

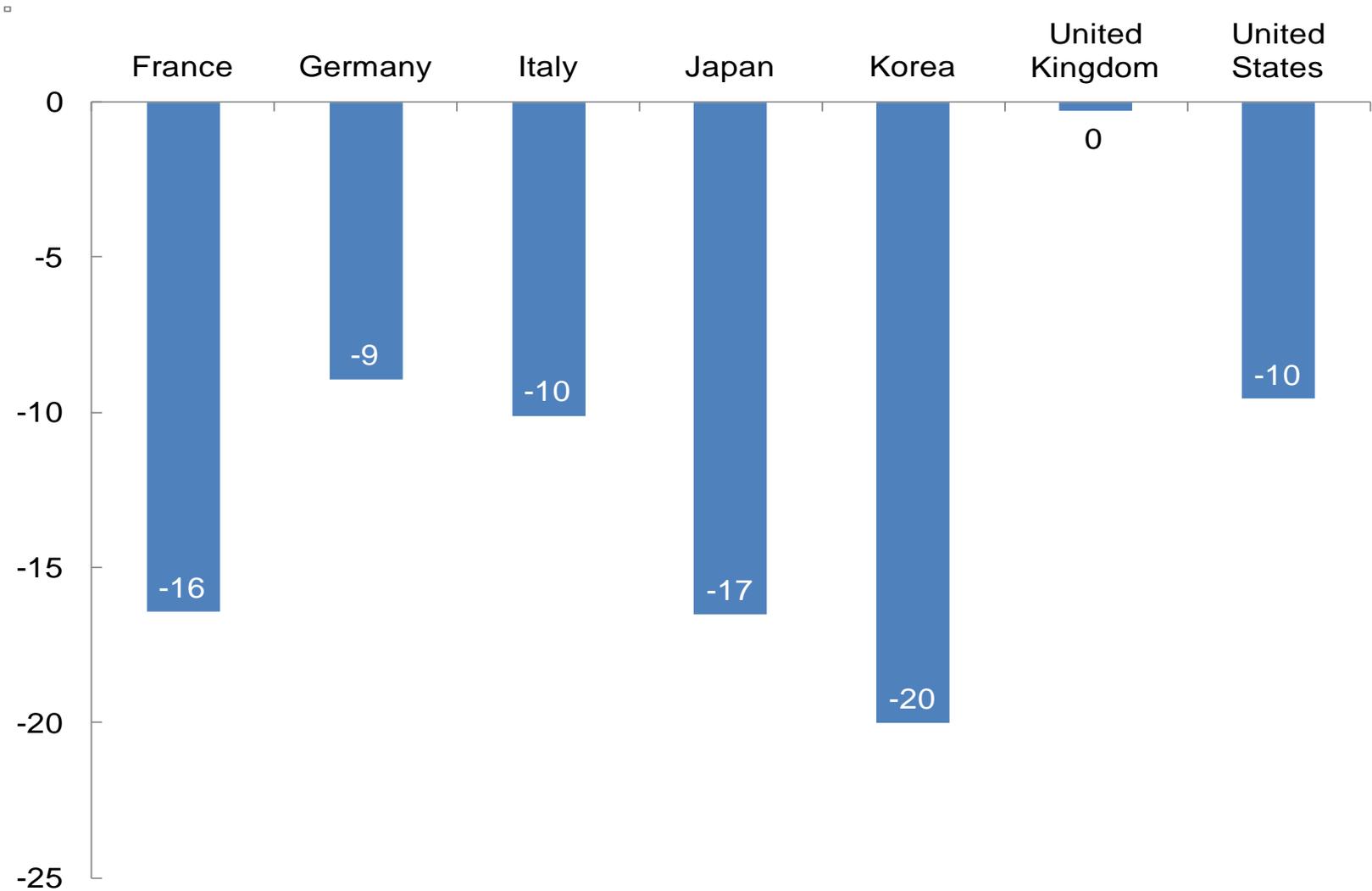
# Pension Reform: Preferred Option is to Increase Retirement Ages



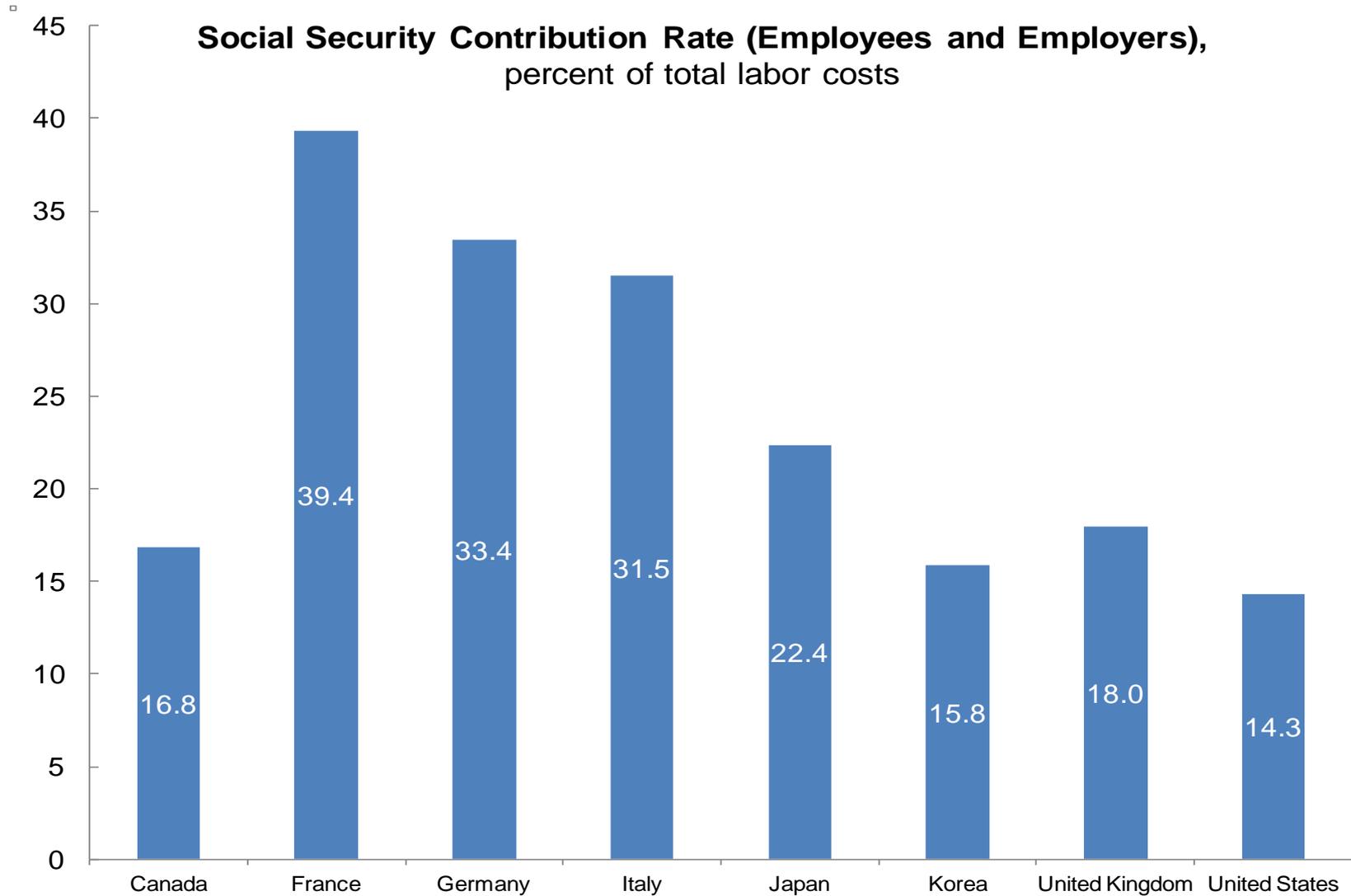


# Other Options: Benefit Reductions

Percentage change in replacement rates, 2010-30



# Other Options: Increases in Contributions

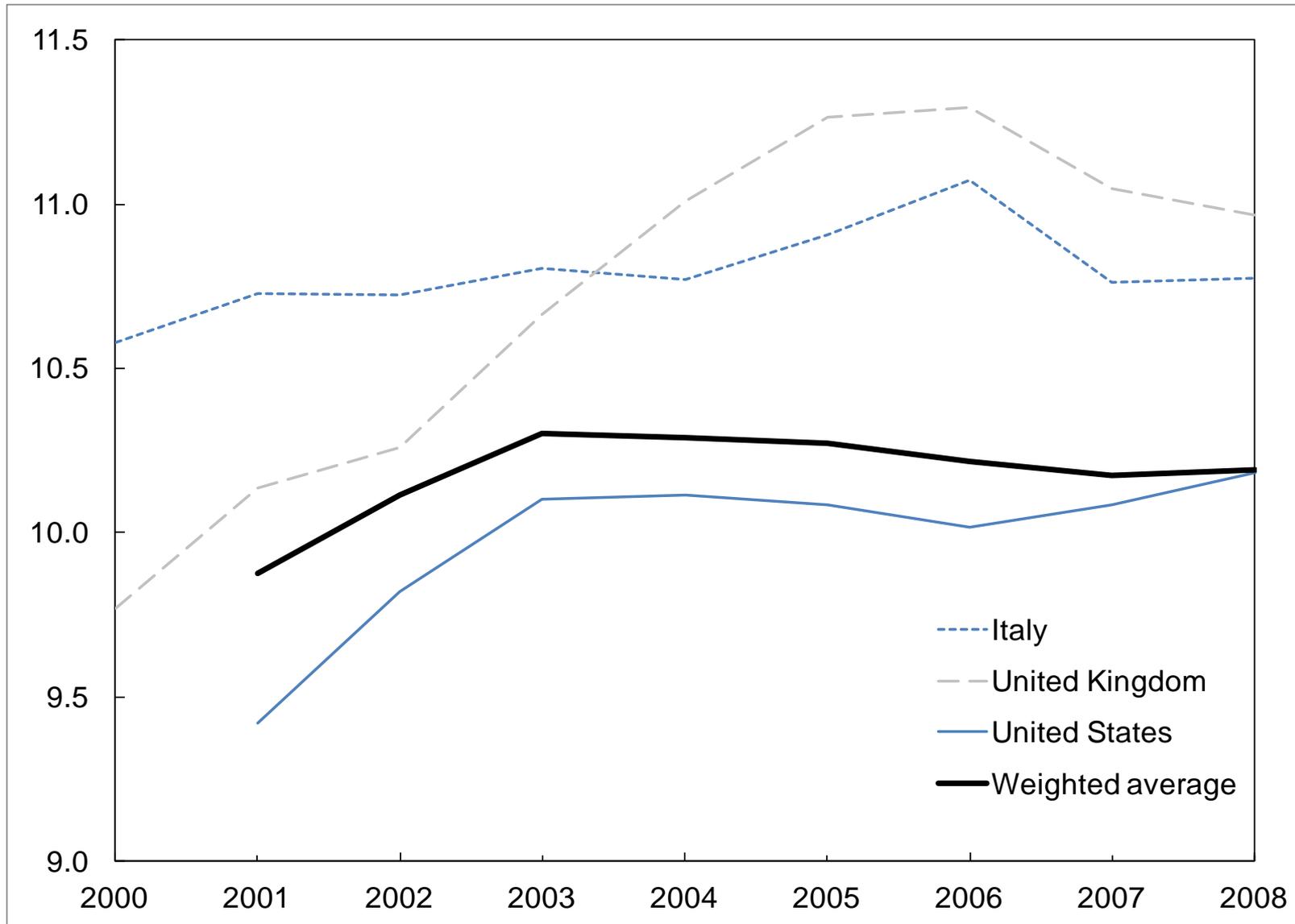


# A Three-Pillar Strategy for Consolidation



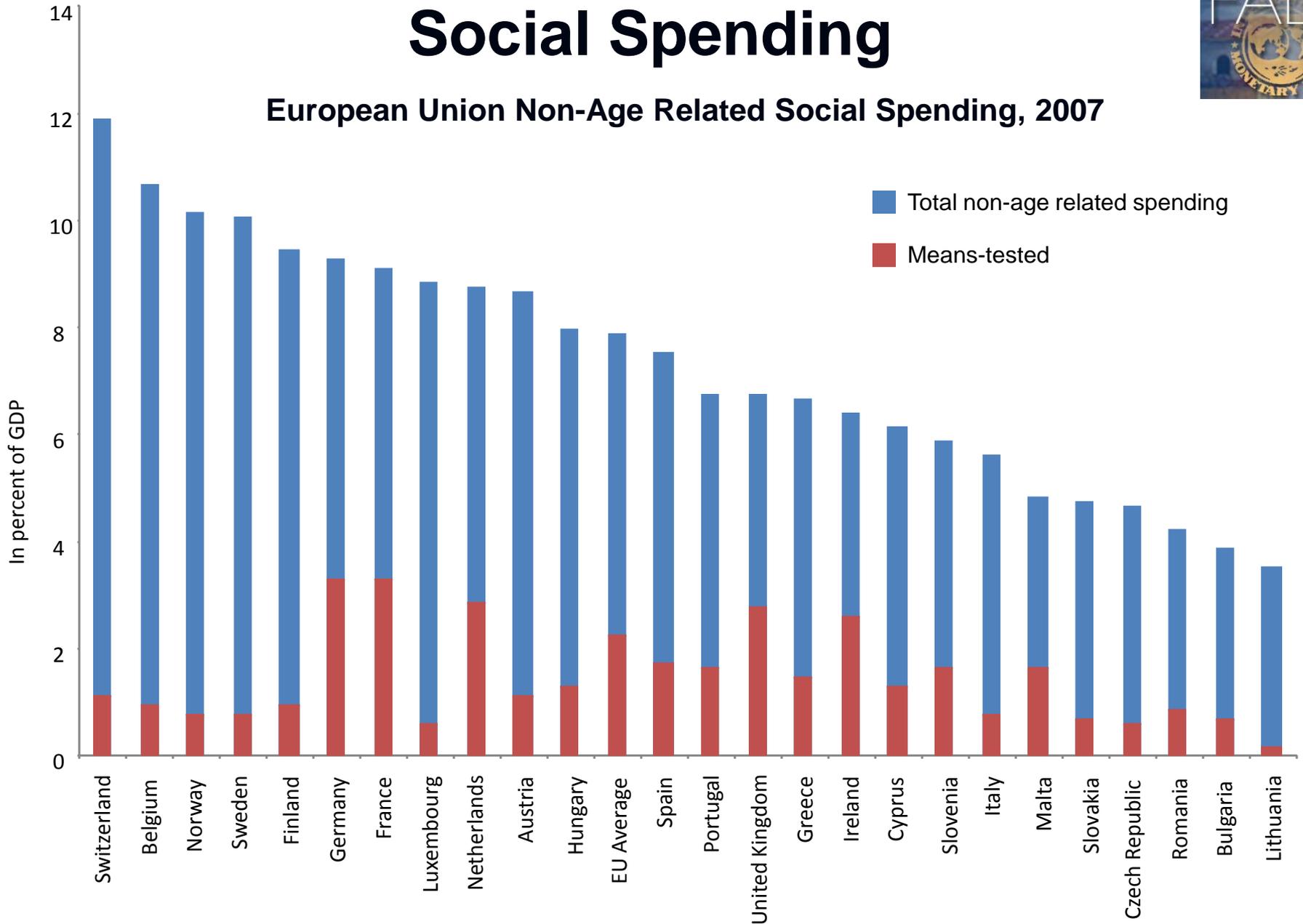
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# Public Sector Wages in Selected G-7 Countries (As share of potential GDP)



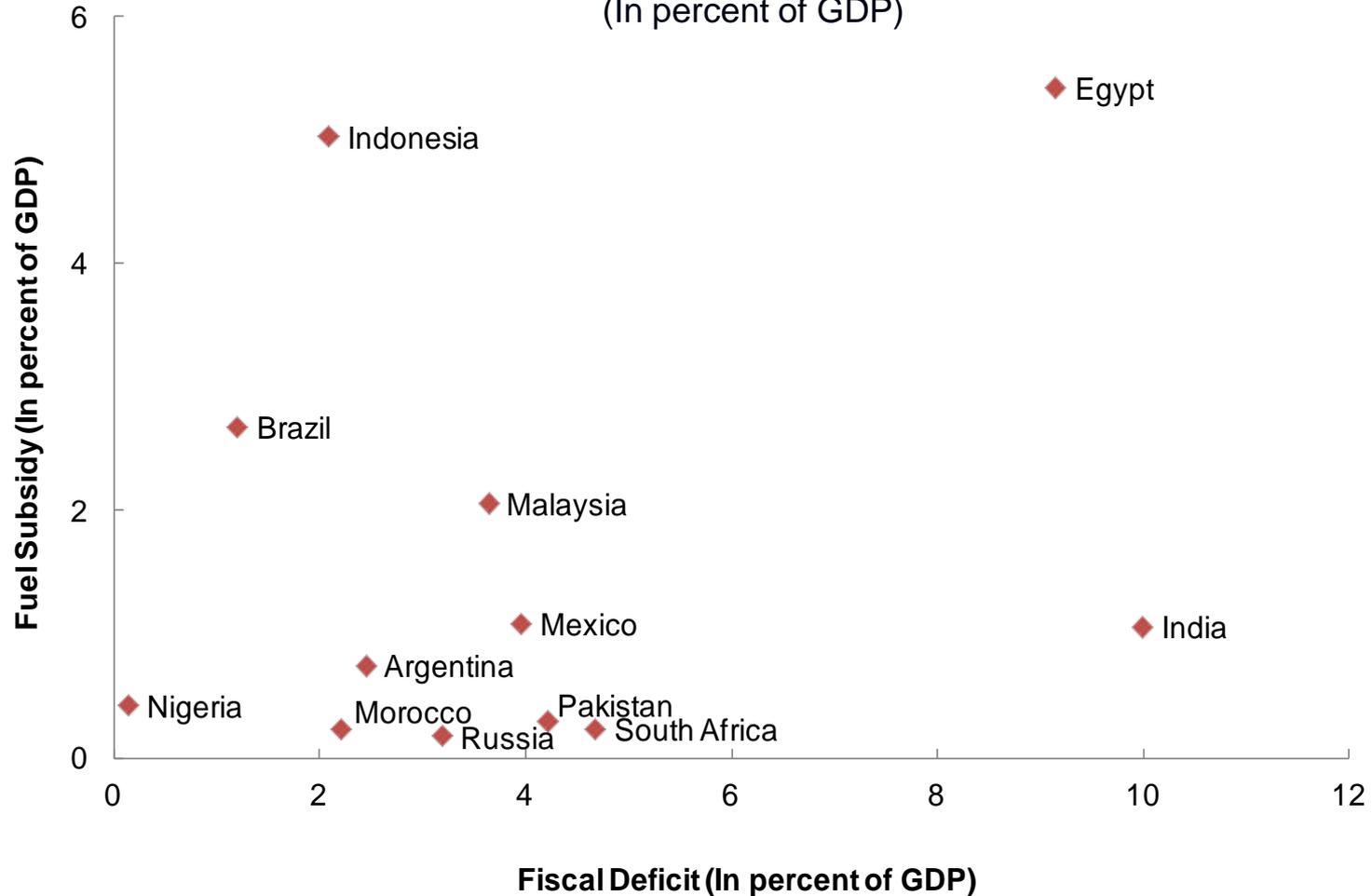
# Social Spending

European Union Non-Age Related Social Spending, 2007



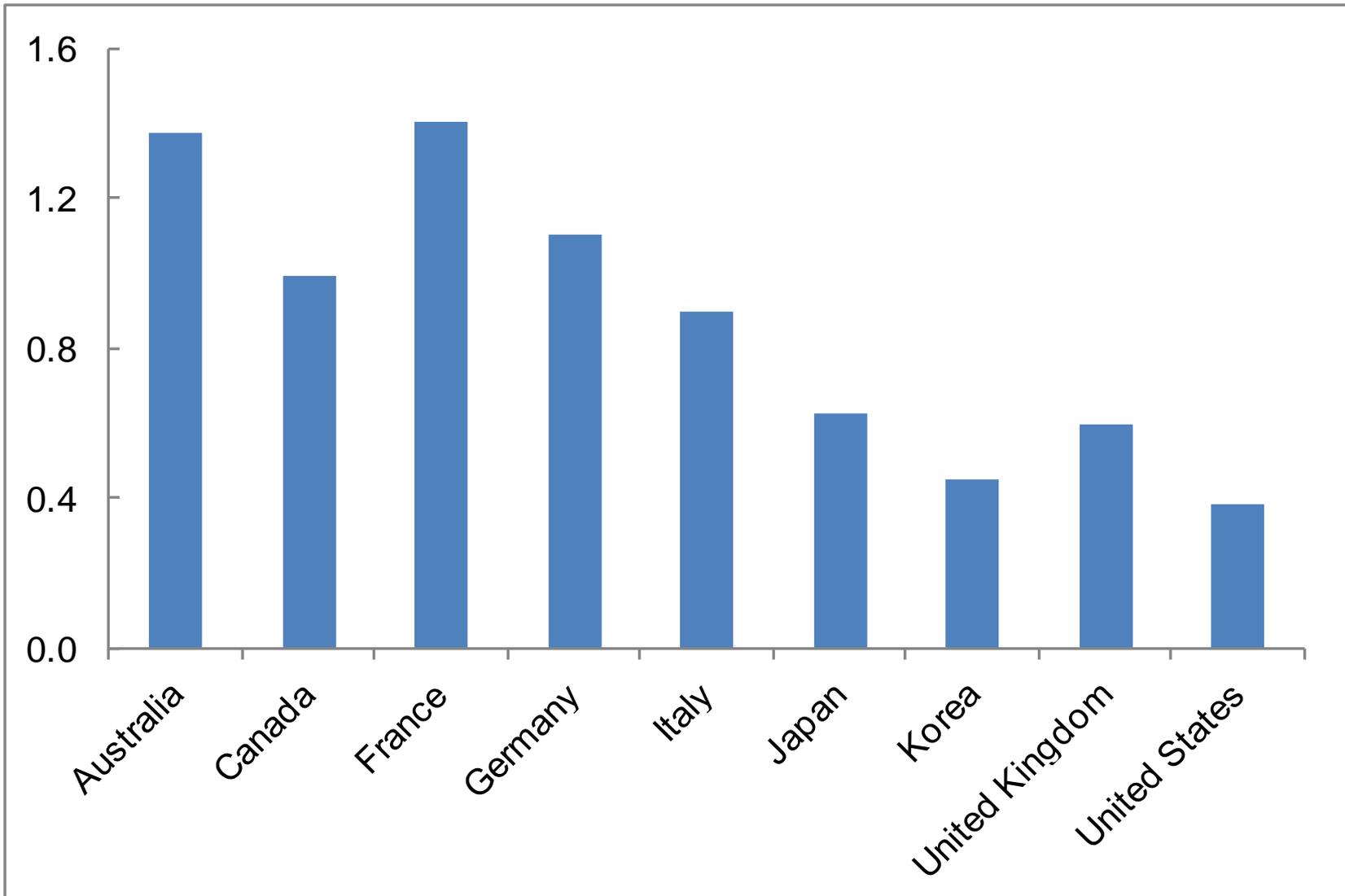
# Fuel Subsidies

**Projected 2010 Fiscal Deficit and Fuel Subsidies in Emerging Economies**  
(In percent of GDP)



# Advanced G-20: Budgetary Subsidies

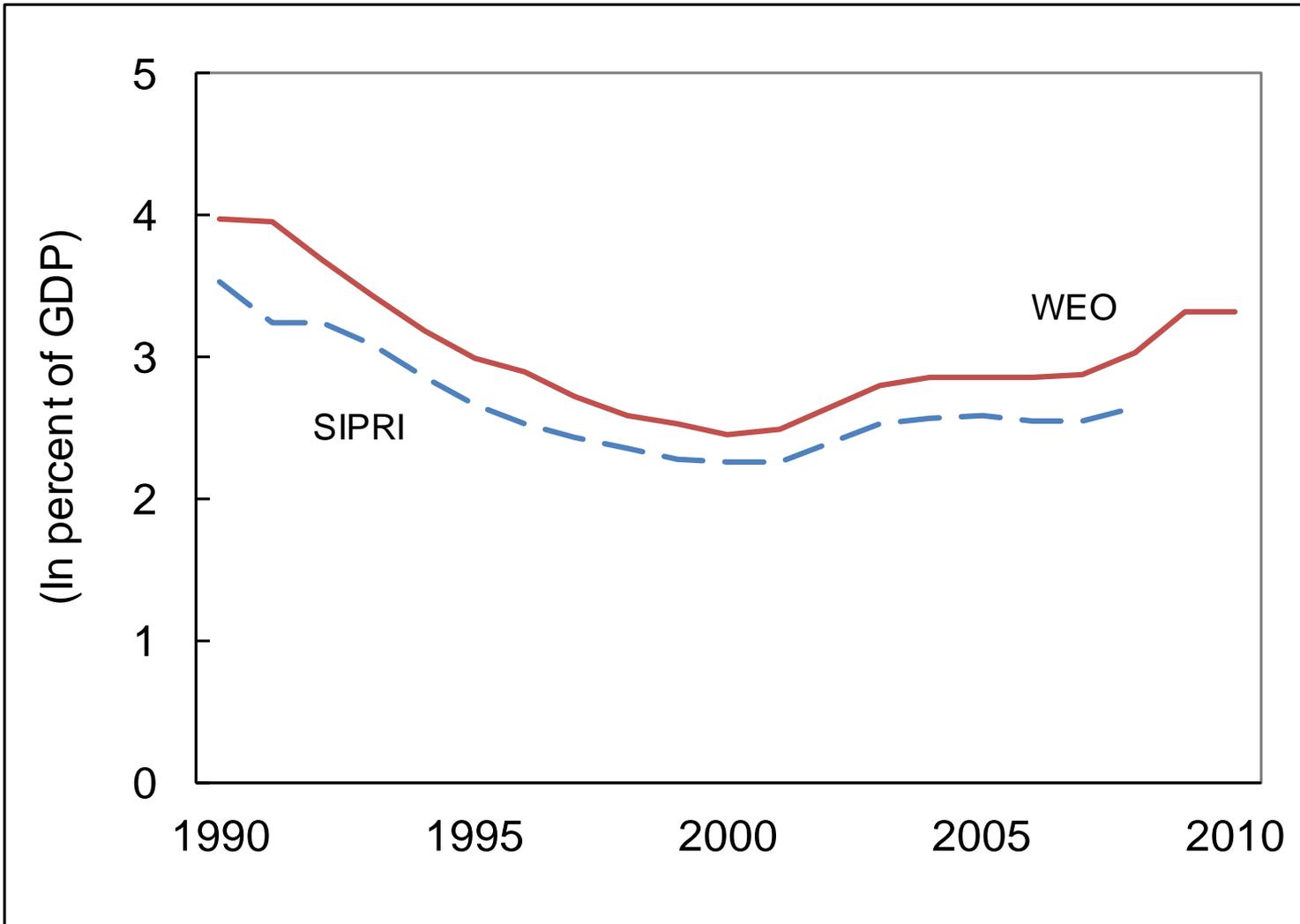
(In percent of GDP)



Source: Eurostat and OECD.

Note: Data for 2008, or nearest year available.

# Military Expenditures in Advanced Economies, 1990-2010



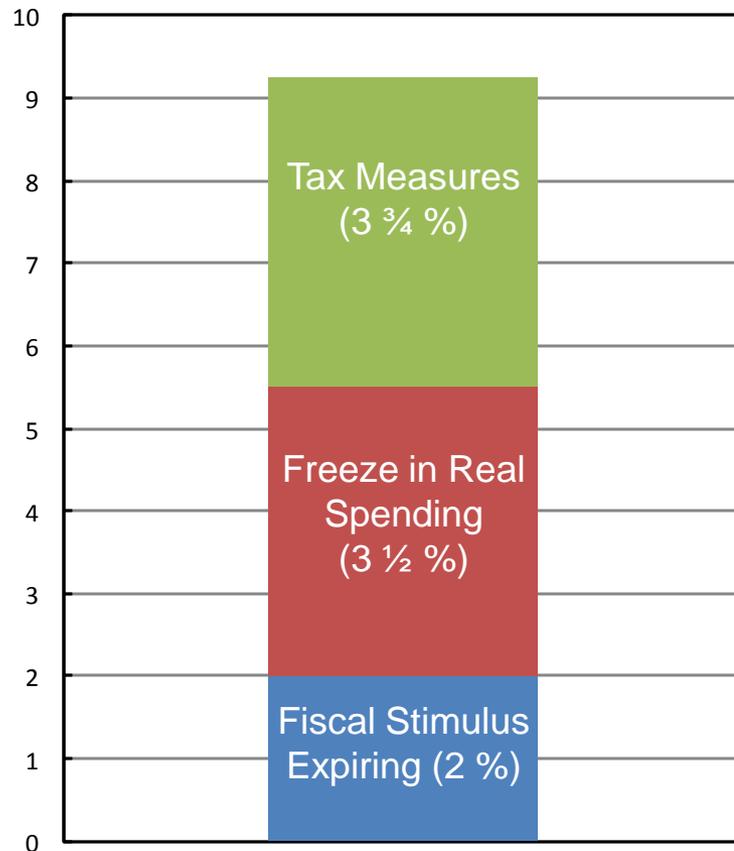
# A Three-Pillar Strategy for Consolidation



1. Stabilize age-related spending relative to GDP
2. Reduce non age-related spending relative to GDP
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# Spending Measures May Not Be Enough

9 ¼ Improvement in Cyclically Adjusted Primary Balance in G-20 Advanced



- Not renewing the stimulus measures
- Freezing real primary spending per capita (excluding health and pension spending)
- ❖ With primary spending at 23% of GDP, real growth rate of 2% ⇒ the primary balance ↑ 3½ % of GDP

# Less Distortionary Tax Measures



## Potential Revenue Increases in Advanced G-7 Countries

PPP weighted averages

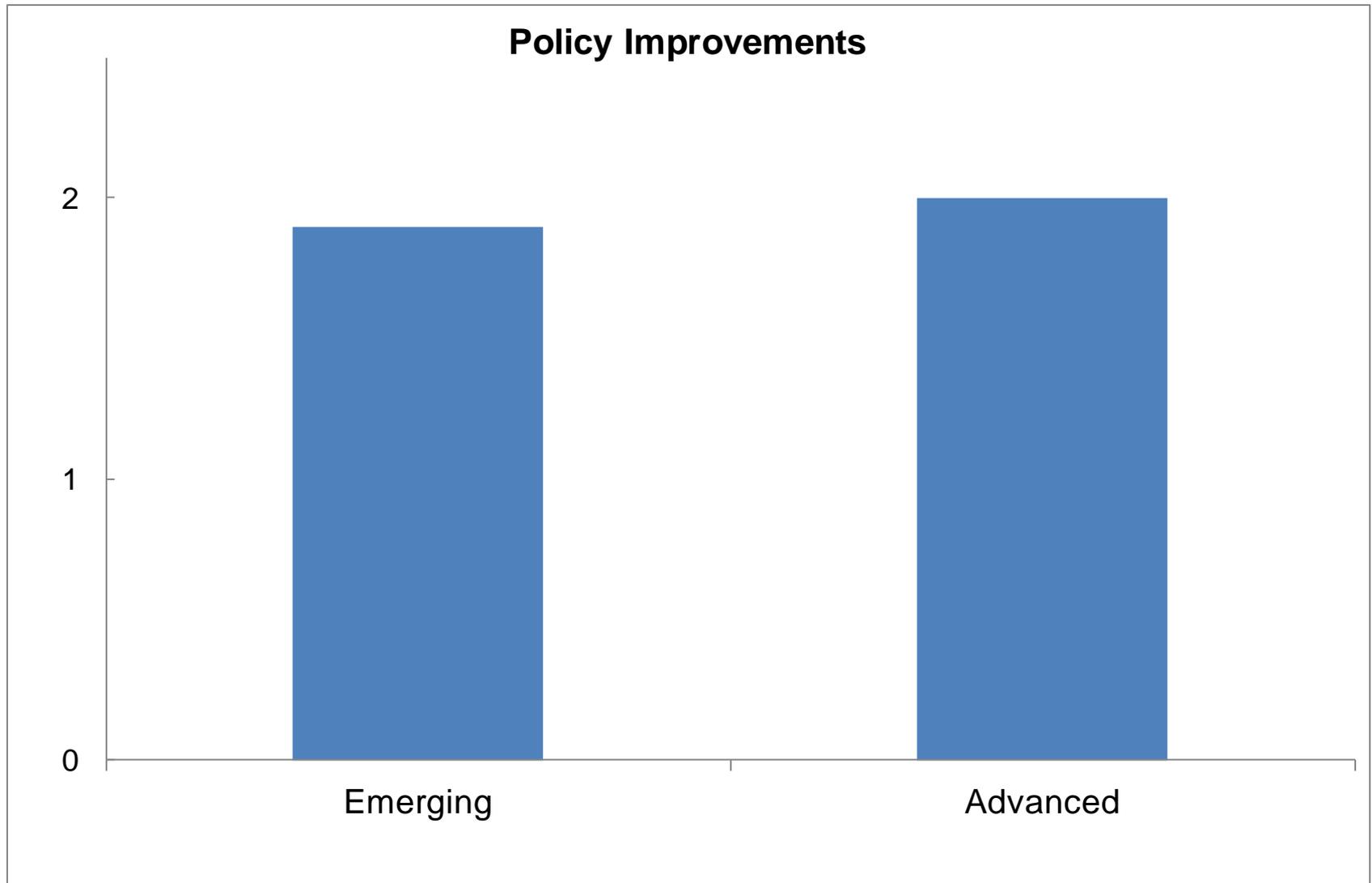
Total Increase in Revenue: 2.8  
percent of GDP

Reduce VAT policy  
gap by half, 1.1

A pie chart with a single blue slice. The slice is labeled with the text 'Reduce VAT policy gap by half, 1.1'. The chart is positioned to the right of the text 'Total Increase in Revenue: 2.8 percent of GDP'.



# VAT – Potential for Policy and Compliance Improvements (In percent of GDP)



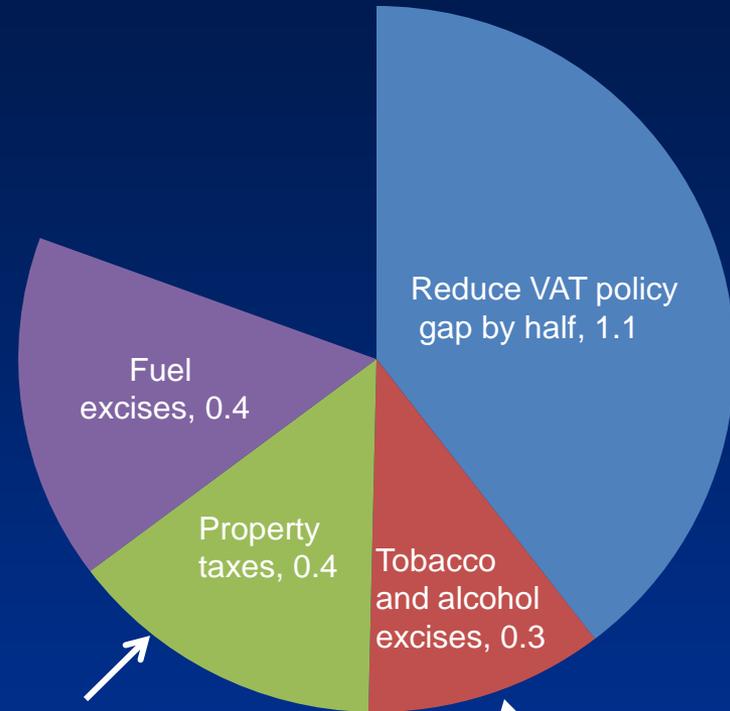
# Less Distortionary Tax Measures



## Potential Revenue Increases in Advanced G-7 Countries

PPP weighted averages

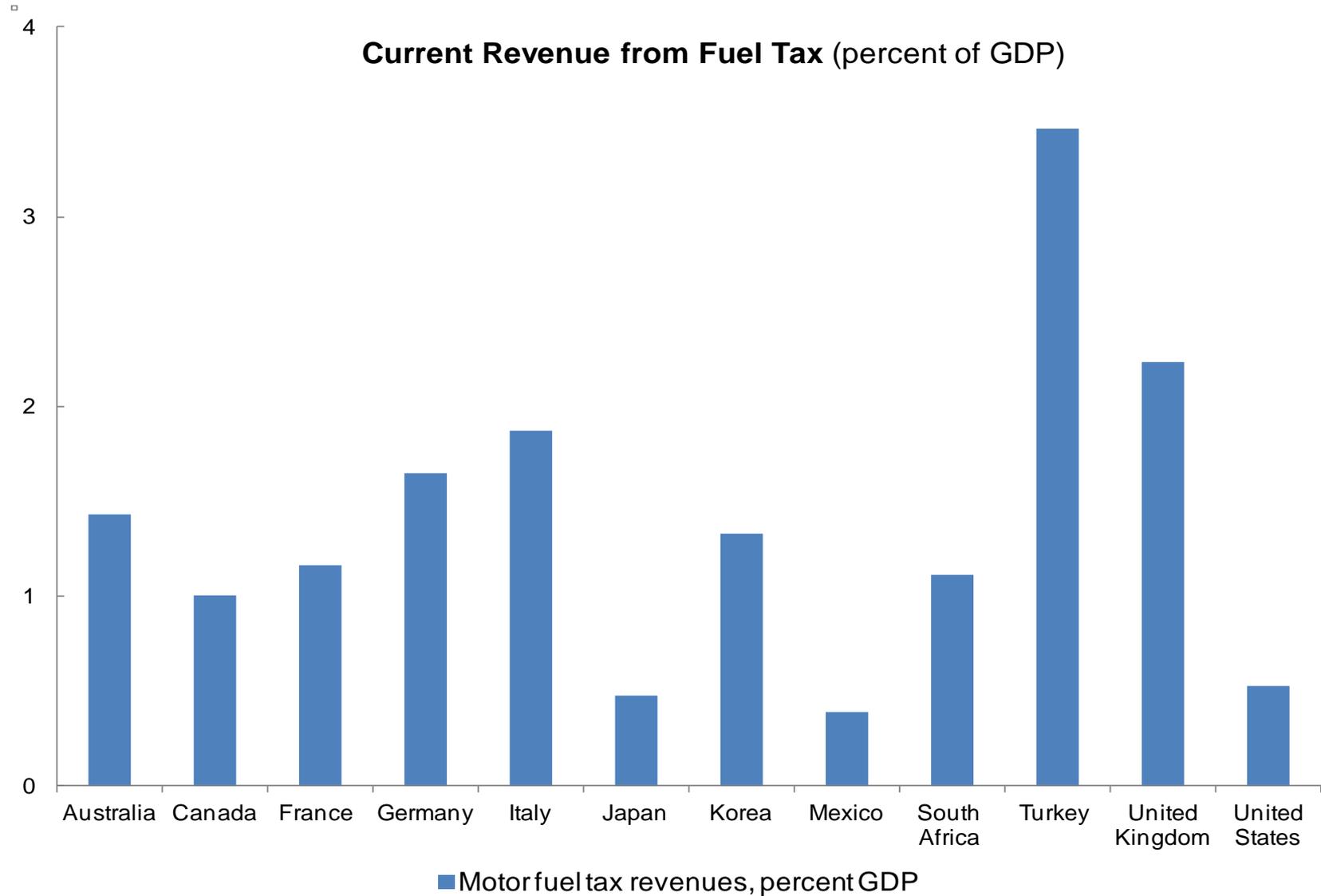
Total Increase in Revenue: 2.8 percent of GDP



Real estate taxes to yield average ratio to GDP existing in the U.S., Canada and the U.K.

Excises to the 2006 average level for countries below the average

# Fuel Taxes – Potential for Raising Revenue



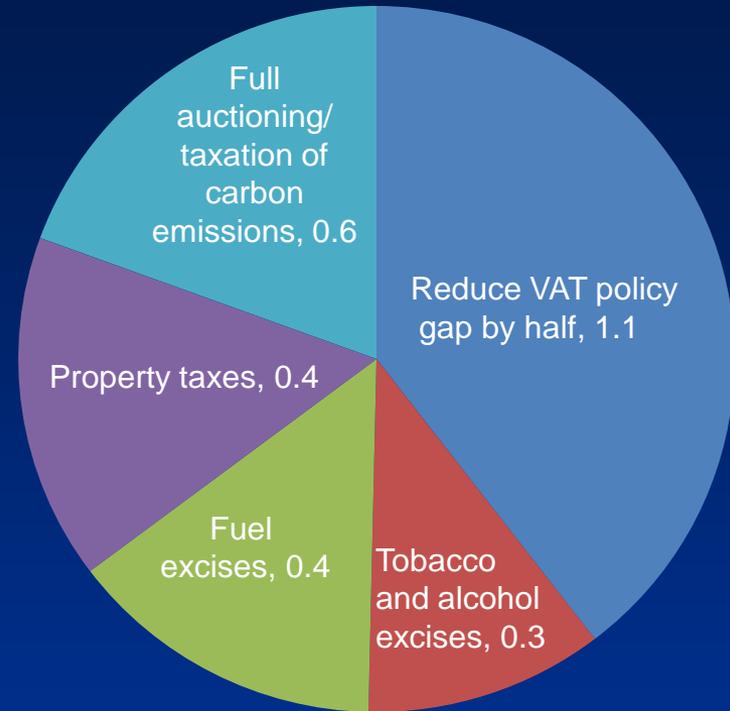
# Less Distortionary Tax Measures



## Potential Revenue Increases in Advanced G-7 Countries

PPP weighted averages

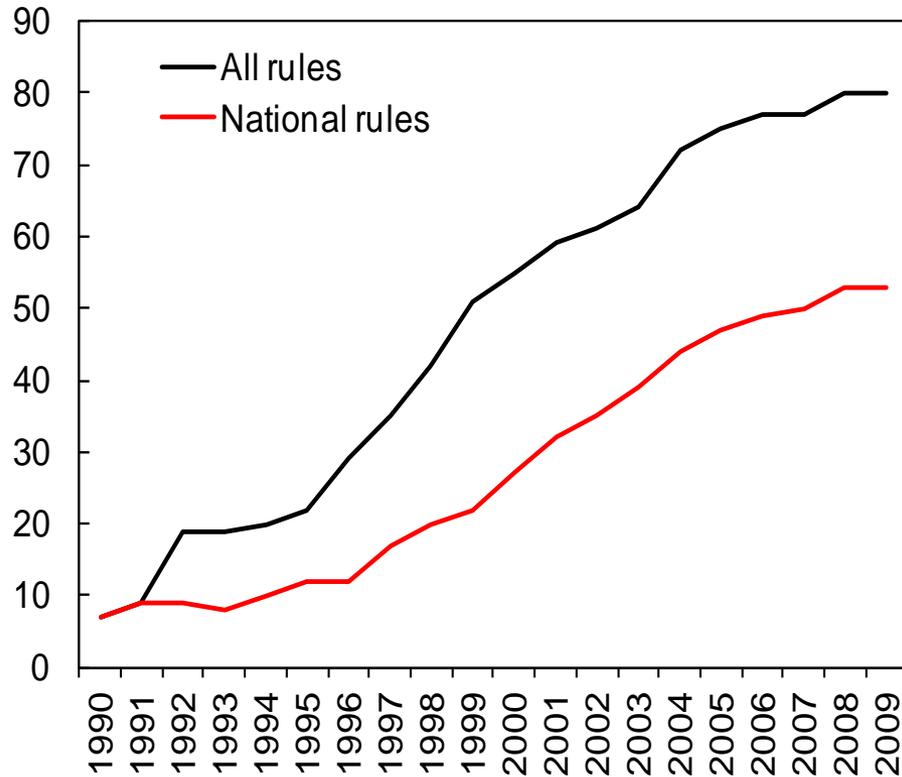
Total Increase in Revenue: 2.8 percent of GDP



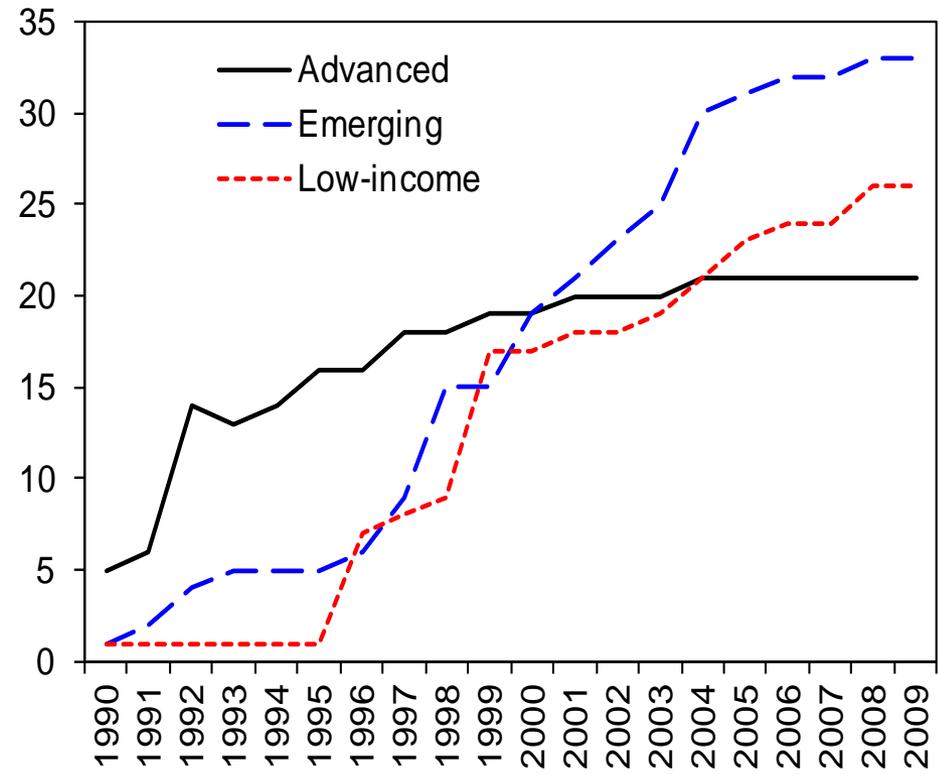
# Fiscal Rules Around the World



Number of Countries with Fiscal Rules



Number of Countries with Fiscal Rules, by Country Group



# Timing of the Exit

<b>Actions</b> \ <b>Timing</b>	<b>2010</b>	<b>2011</b>
<b>Deficit Reductions</b>	<ul style="list-style-type: none"> <li>• EMCs where growth is picking up faster</li> <li>• Any country under pressure from markets</li> </ul>	All other countries
<b>Entitlement Reforms</b>	All countries facing aging pressures	...
<b>Strengthening Fiscal Institutions</b>	All countries	...