RECHERCHE ET EXPERTISE
SUR L'ECONOMIE MONDIALE

CEPII

Fiscal Monitor 2025 Chap. 1: Spending Smarter

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- "*This Fiscal Monitor explores how governments can* ***improve economic growth prospects*** *by enhancing the efficiency and composition of* ***public spending***"

- Renewing an old debate in (endogenous) growth theories (e.g. Barro, 1990)

- This chapter: an extensive investigation
  - addressing many dimensions of the problem
  - introducing new global data sets on the efficiency and rigidity of public spending
  - based on both micro(-firm)-level and macro analyses,
  - with theoretical framework for long-term analysis

- Results obviously make sense, esp. for developing countries.

Analyses happen "*within a fixed spending envelope*", "allocating well" means "reallocating", i.e., winners and losers.

➔ This raises non-trivial issues.

- Political economy of those reforms ;
- Less redistributive policies, more trouble related to inequality ;
- Incidentally, this brings important questions about the definition of efficiency and "(in)efficient spending" ;
- Also, reallocating spending to support long-run growth would mean less short-run support (EA…).

Political economy of public spending (re-)allocation

- Devoting more resources to R&D, education… **all other things equal** implies curbing spending devoted to social transfers, such as, e.g. pensions…

- This echoes current debates on pension reforms in several advanced economies, especially France.

- Pensioners vote, and tend to vote more than other segments of the population – at least in France.

- **In that context, how can policymakers implement the redirection of public spending you prescribe?**

Implications of less redistributive policies

- Curbing spending devoted to social transfers implies **more income inequality.**

- Of course, this is not the Chapter’s main focus, which is about boosting growth – income inequality mentioned once (p.14).

- But inequality increases household debt: Kumhof et al. (AER, 2015), Perugini et al. (CambJE, 2015), Bazillier et al. (EER, 2021).

- Excess (household) leverage triggers financial crises: Buyukkarabacak and Valev, JBF, 2010 ; Jorda, Schularick and Taylor, EP 2016

Implications of less redistributive policies

- Financial crises =
  - huge short- and long-run GDP costs (permanent decrease in tax base)
  - massive government interventions requiring dozens of additional GDP percentage points of public debt (good bye fiscal space…)

- More inequality = more political polarization, and the risk of having policymakers not that much interested in education, health, R&D…

- **In a few words: beware of GE effects! You may well end up using your additional GDP points derived from more R&D, education, infrastructures… to pay, e.g., for financial crises, or subsequent bad economic policies…**

- Roughly, efficiency is defined as **maximizing output**.

- Many environmental policies aim to reduce energy consumption. This will probably reduce GDP.
  - **Should we label those policies as inefficient?**

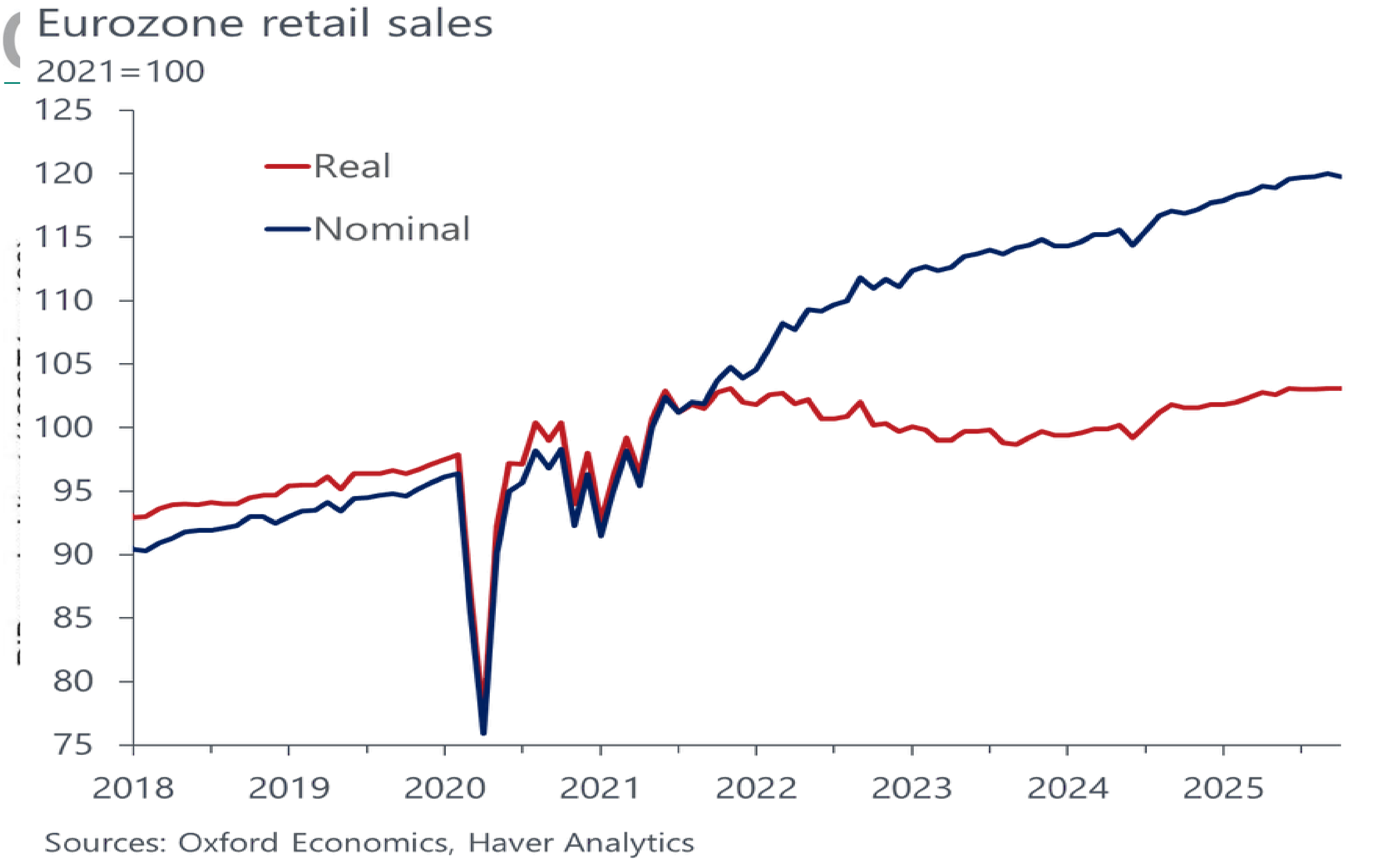
- Also, undesirable side/GE effects of those policies can generate HUGE inefficiencies (see prev. slide).

- A suggestion: as an alternative to output, it could be useful to assess to which extent those policies affect, e.g., life expectancy, Human Development Index…

- Also, the boundary between efficient and inefficient spending is sometimes delicate.

- For example, the Chapter regularly emphasizes the necessity to contain the wage bill, while pointing that teaching staff should be spared.

- Shouldn't this also apply to researchers, medical workers…? Their wage bills are part of efficient spending, according to the classification of the Chapter.



Gap EA-US widens since 2011-2012, when the US started having continuously expansionary fiscal policies…

Specific EU issues

- I am not saying we should give up on « spending smarter » for plain fiscal stimulus! The diagnosis of too much public debt remains broadly valid.

- But my two cents is that the constant spending envelope is probably a too tight constraint for EU/EA.

- We should aim (at least in the EA/EU) for what you suggest, together with (moderate) fiscal stimulus backed by monetary policy.

- Again, a great and stimulating Chapter!

- Many thanks for your attention, looking forward to the discussion.