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U.S. Fiscal Policy After the
Financial Crisis and Recession
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Key Lessons for U.S. Fiscal Policy from the Recent Experience

- Stronger automatic stabilizers probably would have reduced the output and employment losses from the financial crisis, especially because monetary policy became constrained by the zero lower bound on interest rates.

- Having the budget deficit and debt low enough before the crisis to allow for discretionary fiscal actions was crucial for resolving the financial crisis and mitigating the harm of the subsequent recession.
The budget deficit will fall sharply in the next few years.

Debt is currently higher relative to GDP than it has been in more than 50 years, but it is not especially high compared with the historical experience of debt in other countries.
Estimated Budgetary Effects of ARRA

Billions of Dollars

Total Effect on the Deficit
Revenues
Mandatory Outlays
Discretionary Outlays

Given current law and certain changes to that law that are broadly supported by the Administration and Congress, the budget deficit and debt are on a worrisome path—unsustainable in the long run and posing growing risks even during the next several years.
Budget Deficit or Surplus

Percentage of GDP

With Tax Cuts Extended and AMT Indexed

1970s 1980s 1990s 2000s 2010s

Actual  Projected
Rising Debt Burden

Percentage of GDP

Actual

Projected

Tax Cuts Extended and AMT Indexed

Baseline
Debt Burden Across Countries in 2007

Source: OECD.
Putting U.S. fiscal policy on a safe path would probably require significant changes in spending, revenues, or both.

Changes of the required magnitude could have important economic and social effects.

Given the political and substantive difficulties in making significant policy changes, determining what those changes will be is an urgent task for policymakers.
If the Goal Is to Balance the Budget in 2020

The Scale of the Problem

Deficit If Tax Cuts Are Extended and AMT Is Indexed

The Scale of Possible Solutions

Individual Income Tax

Defense

Other Mandatory Spending and Nondefense Discretionary Spending

Social Security, Medicare, Medicaid, and Health Insurance Subsidies

(Trillions of dollars)
Projected Federal Spending in 2020 Under CBO’s March Baseline

- Medicare (17%)
- Net Interest (14%)
- Defense (15%)
- Medicaid (8%)
- Other Spending (23%)
- Social Security (22%)