Public sector deficits and macroeconomic performance

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Abstract

In the 1980s chronic public sector deficits forced countries to undertake fiscal adjustment. The need to face hard choices continues in the 1990s. But the problem is not a simple and easily diagnosed one with an obvious solution. Rather, public sector deficits have had widely differing consequences; high inflation in some countries, low inflation but also low investment and growth in others, and in still others no evident short-term macroeconomic spillovers. This book presents the findings of a World Bank research project designed to shed light on the complex dynamics of public sector deficits. It includes an in-depth examination of eight countries: Argentina, Chile, Colombia, Cote d'Ivoire, Ghana, Morocco, Pakistan, and Zimbabwe. These cases are analyzed within a comprehensive theoretical framework elaborated for the study and in conjunction with cross-country data from a larger set. The book draws the following conclusions. The ways chosen to finance deficits - money creation, debt, or arrears - go far to explain medium-term financial and macroeconomic imbalances, but in the short term these relations are blurred. Deficits tend to be bad for growth; they increase financial and price instability and crowd out private investment. Public saving typically reduces private saving only slightly; increasing public saving is a very effective policy instrument for raising national saving. Fiscal adjustment

Other subjects

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Other information

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PDF | On Jan 1, 1994, Klaus Schmidt-Hebbel and others published Public Sector Deficits and Macroeconomic Performance. It is often emphasised that monetary seigniorage financing of public sector deficits is technically a “free lunch” if the economy has not attained the full employment levels. However, conservative macroeconomic policies in many emerging and developing economies, especially in the last two decades, have moved away from seigniorage financing to debt financing of deficits to give greater autonomy to the central banks. Against this backdrop, the paper analyses the fiscal and monetary policy co-ordination in India by constructing a monetary seigniorage Laffer curve.