Fiscal Policy
Dampening Cyclical Fluctuations,
Supporting Inclusive Growth

IMF–ICRIER Conference on Fiscal Policy Achievements and Challenges in Asia—Implications for India

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New Delhi, India
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I. The role of fiscal policy in dampening output fluctuations

II. The challenge ahead: increasing space to support inclusive and sustained growth

   A. Improving efficiency and structure of taxes

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I. The role of fiscal policy in dampening output fluctuations

- In the past decade fiscal policy has become generally more countercyclical
- Discretionary policies have been effective
- Stronger automatic stabilizers could enhance countercyclicality
The fiscal policy response to output fluctuations has become stronger in Asia.

Correlation Between Government Spending and GDP

Pre-2001
The fiscal policy response to output fluctuations has become stronger in Asia.

**Correlation Between Government Spending and GDP**

- Countries: HKG, TWN, SGP, PHL, IDN, CHN, MYS, THA, VNM, KOR, IND
- Regions: Latin America, EME/CIS, Advanced economies
- Period: 2001-2011
Stronger institutions are associated with higher countercyclicality.

Procyclicality and Government Effectiveness
(1980-2011)

- Sample of 60 advanced and emerging economies.
Discretionary policy has helped dampen the cycle...

Selected Asia: Multipliers for Government Spending and Public Investment
(1996:Q2 - 2012:Q1)

Note: ASEAN includes Indonesia, Malaysia, the Philippines, Singapore, and Thailand. For Japan and India, multipliers are the average of VAR estimates and DSGE model simulations.
...which is especially helpful since automatic stabilizers remain low.

**Automatic Stabilizers: 2001–11**
(Correlation between output gaps and cyclical fiscal balance)

Advanced economies excluding Asia

Latin America

EME/CIS

Role of fiscal policy

- TWN
- IDN
- IND
- MYS
- HKG
- SGP
- VNM
- CHN
- PHL
- THA
- KOR
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A. Improving efficiency and structure of taxes

- There is room to reduce complex and poorly targeted tax incentives and enhance revenue administration
- The revenue structure could be made more growth friendly in some economies
Revenues are low in comparison with other economies at the same income level.
Personal income tax yields are relatively low in most Asian emerging and low income economies.

**Yields from Personal Income Tax**
(In percent, 2011 or latest available)

- Yields based on maximum personal income tax rates
- Yields based on middle personal income tax rates

Lower yields than in comparable regions
Yields from corporate income tax are weak in some low income economies and Sri Lanka.

Yields from Corporate Income Tax
(In percent, 2011 or latest available)

Lower yields than in comparable regions
Yields from the VAT or sales taxes are low in some economies.

Yields from VAT or Sales Tax
(In percent, 2011 or latest available)

- Yields from VAT or sales tax (consumption based)
- Yields from VAT or sales tax (overall)

Lower yields than in comparable regions
In some economies, the tax mix could be made more growth-friendly.

**Tax Revenue by Category**
(In percent of total tax revenue, 2011 or latest available)

- Corporate income tax
- Other
- Property tax
- General tax on goods and services

Higher corporate income tax revenue in Asia →
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B. Enhancing public spending composition

• *Public investment can help fill infrastructure gaps*
• *Spending on education and health needs to be scaled up*
• *Subsidies could be gradually replaced by better targeted programs*
Public investment can help fill infrastructure gaps.

Infrastructure and Public Investment

- Advanced and main emerging economies outside Asia

Public Investment to GDP, 2011-12

Infrastructure Score, 2010 (1-7, 7=best)
Public spending on education and health has also been lagging behind.
There is scope to enhance public spending composition and efficiency.
Large subsidies especially on energy

Food and Energy Subsidies
(In percent of total GDP, 2012 or latest available)

Energy  Food and fertilizer

Advanced economies

PHL  VNM  HKG  MNG  TWN  NPL  THA  IND  KOR  LKA  BGD  CHN  MYS  IDN

Food and fertilizer spending.
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Thank You