

Fiscal response to the Great Recession

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- I. Fiscal response to the crisis
 - ① Public finance response
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 - ③ Cuts to spending on public services
- II. Was the crisis an opportunity for reforms?
 - ① Tax design
 - ② Public spending
 - ③ Other structural reforms

I. Fiscal response to the crisis

Public finance response

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 - Sizeable fiscal tightening in France, UK and Italy (5-6% GDP)
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 - Reliance on taxation : France and Italy
 - Reductions in public spending : Ireland, Spain and the UK

I. Fiscal response to the crisis

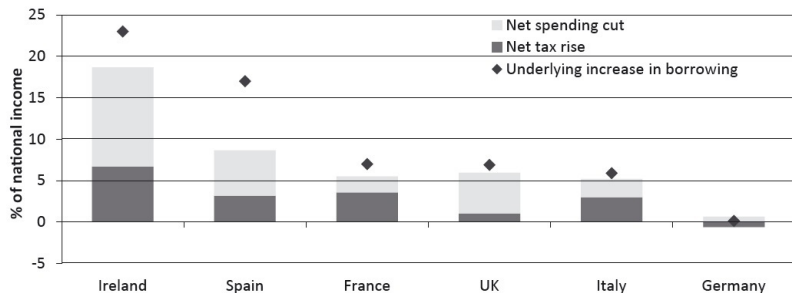
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 - Reductions in public spending : Ireland, Spain and the UK
- **Germany as the outlier**
 - No fiscal tightening
 - Spending cuts used to finance net tax cuts

I. Fiscal response to the crisis

Public finance response

FIGURE 1: Size and composition of post-crisis fiscal policy response up to 2014



Source : Bozio et al (2015), figure 4, p. 416.

I. Fiscal response to the crisis

Tax and benefit changes

- **Increases in taxation in most countries**
 - Increases in the rates of VAT
 - Increases in income taxation targeted at top incomes
 - Increases in social security contributions

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 - Increases in social security contributions
- **Different choices for benefits**
 - No change or some increases in Spain, France and Italy
 - Significant cuts in benefits : UK, Ireland
e.g. cuts in benefits in the UK \simeq 1.7 % GDP

I. Fiscal response to the crisis

Tax and benefit changes

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 - Progressive changes in France in the entire distribution
 - Larger cuts for the bottom half of the population in the UK
 - Constant cuts in Ireland

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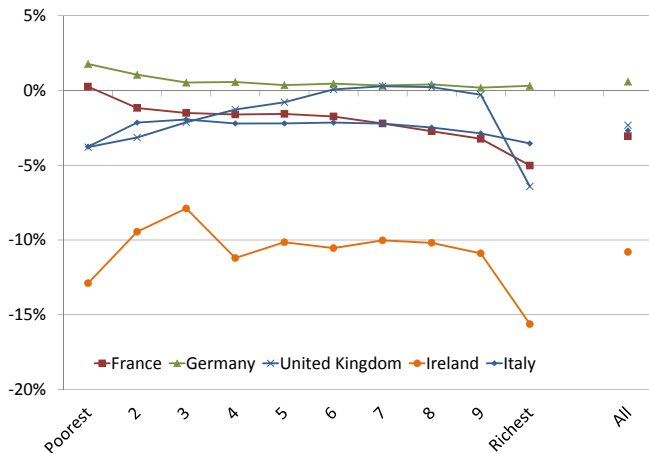
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- **Difference of targeting by household types**
 - In most countries, pensioners less affected (except in Italy)
 - Working age households with children most affected in France and the UK
 - In France, highest income households with children most affected

I. Fiscal response to the crisis

Tax and benefit changes

FIGURE 2: Distributional impact of post crisis fiscal measures implemented by 2014



I. Fiscal response to the crisis

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- **Varying degree of control over spending ?**
 - Difference in the areas targeted can reflect preferences
 - But also marked difference in the way governments control spending
 - e.g. degree of central/local control UK vs Spain
 - e.g. health spending UK vs France

II. Was the crisis an opportunity for reforms?

Tax design

- **Numerous tax reforms, some positive**
 - Increases in intermediate VAT rates (France)
 - Broadening corporate tax base while cutting rates (UK, Spain)
 - Cuts in tax wedge (France)

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 - Increases in intermediate VAT rates (France)
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- **But general negative assessment**
 - Complexity of tax system generally worsened
e.g. French corporate tax credit based on wage bill
 - Instability of measures
e.g. VAT changes in Ireland

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 - Although demographic imbalances is the primary cause
 - Large impact on employment of older workers
- **But few evidence-based spending cuts**
 - Few countries have relied on previous analysis to target spending cuts
 - In most cases nominal freeze has been the main policy
 - Except Spain with the Commission on the reform of public administration

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 - UK and Ireland had flexible labour market and open product market
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 - Timid steps in France, Italy and Spain (labour and product markets)

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- **Budget process**
 - Creation of independent watch-dog in most countries
 - Aim to improve forecasting process underpinning budgets

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 - Limited structural reforms in countries that need it
 - Tax systems still plagued by complexity
- **Better reform in good times ?**
 - With little fiscal space, little room for politically costly reforms
 - Better reform in good times, like Germany ?

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