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Fiscal Management at a Crossroads: Part 1

The Global Trend of Expanding Government Debt and Its Impact on the Economy

Government debt-to-GDP ratios in major economies have exceeded the 98% threshold, and the fiscal stimulus effect is expected to diminish further going forward.

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Summary

- This report, the first in a three-part series titled "Fiscal Management at a Crossroads," examines the global trend of fiscal expansion and its implications for future economic growth.

- An analysis of the long-term relationship between public finances and the economy across countries and regions indicates that when the government debt-to-GDP ratio exceeds 98%, the effect of fiscal expansion on boosting economic growth rate diminishes. Furthermore, examining the relationship between the government debt-to-GDP ratio and the key drivers of real GDP per capita growth – total factor productivity (TFP) and capital-equipment ratio – reveals that, for both indicators, the threshold at which growth rates plateau is estimated to be a government debt-to-GDP ratio of 105%.

- It is important to note that the global expansion of government debt not only diminishes the effectiveness of future fiscal policy but also has the potential to constrain global economic growth by slowing the pace of technological innovation and capital accumulation.