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Fiscal policy and its
implications for monetary
and financial stability

23–24 June 2011





Fiscal policy and its implications for monetary and financial stability

Opening Remarks

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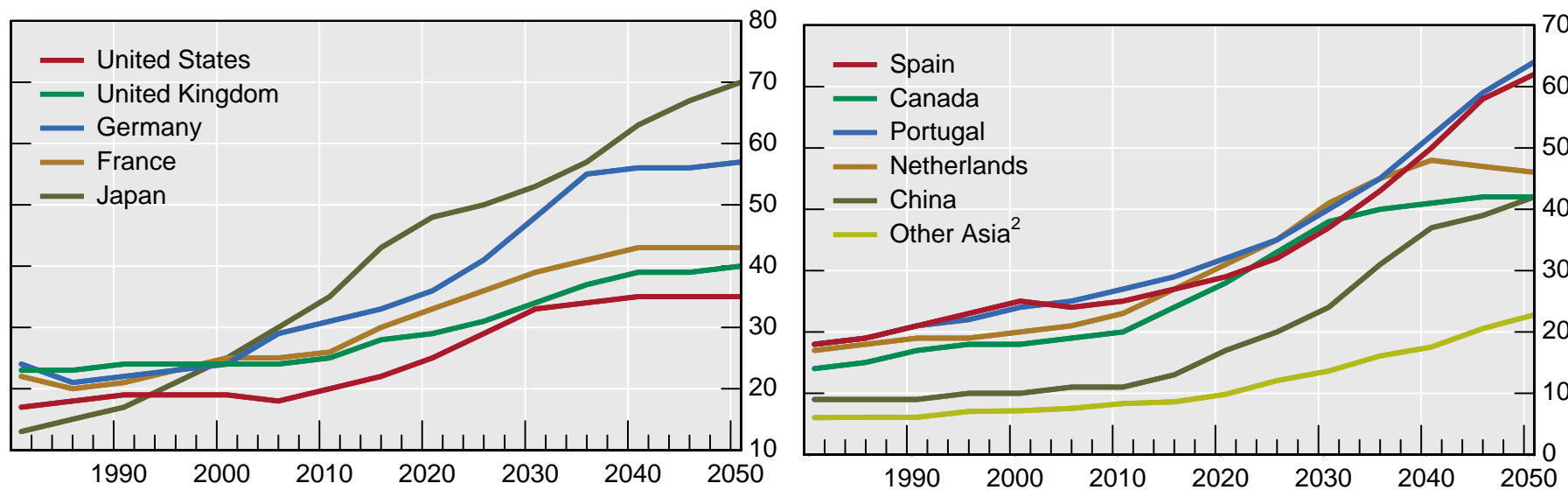
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*Views expressed here are those of the author and do not necessarily reflect those of the BIS.



Graph 1 Old-age dependency ratio¹

In per cent



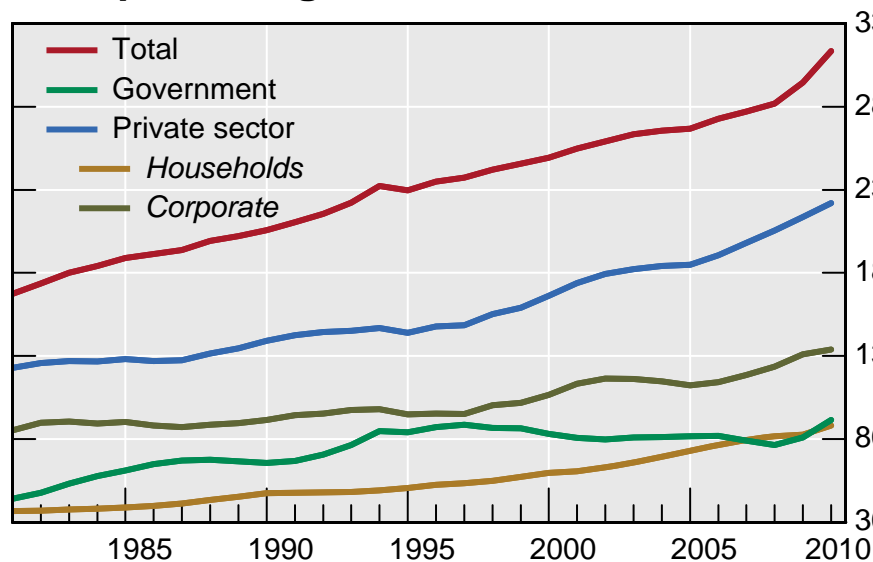
¹ The population aged 65 years or over to the population aged 15-64. ² Weighted average of Hong Kong SAR, India, Indonesia, Korea, Malaysia, the Philippines, Singapore and Thailand by size of population.

Source: United Nation, *World Population Prospects*, the 2010 Revision.

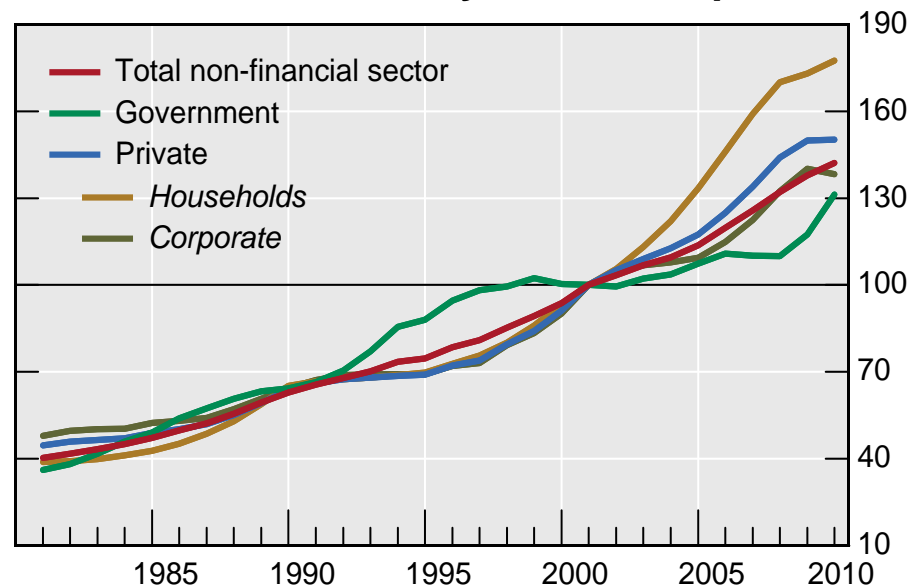


Graph 2 Non-financial sector debt

As a percentage of GDP¹



Real levels, deflated by consumer prices²



¹ Simple averages for 18 OECD economies. ² Rebased to 2000 = 100; simple average of 16 OECD economies, including the United States.

Sources: OECD; national data.



Pre-crisis consensus:

- **Monetary policy:**
stabilise inflation and keep output near potential
- **Fiscal policy:**
automatic stabilizers, foundations for high growth & employment
- **Prudential policy:**
focus on default of individual institutions,
reduce moral hazard problem created by government safety net,
protect depositors



Lessons from the crisis

- **Monetary policy:**
price stability is not enough
(but without it you have nothing)
- **Fiscal policy:**
cyclically balance budgets in normal times are not enough,
insurance against natural and man-made disasters
- **Prudential policy:**
system-wide perspective,
limit systemic risk



How is fiscal policy different?

- More objectives, difficult to quantify
- Trade-offs among a multiplicity of objectives
- Macroeconomic impact not well understood
- Deficit bias arising from short-sightedness



Lessons

- Forward-looking orientation
- Communication and transparency
- Buffers



What can we do?

The minimum

- Independent agencies to assess impact & certify accounting
- Realistic forecast
- Clear communication and disclosure