

## OECD Forum 2011: Restoring Public Finances

**The recent economic crisis inflicted substantial damage on the public finances of many countries around the world.**

How can governments restore public finances and promote sustainable growth at the same time? With budget deficits stretched and public debt at historical highs, what is the policy recipe for progress?



Enormous stimulus programmes, bank bail-outs, increased welfare and unemployment payments, and depressed tax receipts weigh heavily on government balance sheets. To make matters worse, some countries were already running substantial deficits before the crisis hit.

The aggregate budget deficit for the OECD is expected to be around 7.5%, but some countries have deficits that run well into the double digits, while public debt levels have soared. Though some countries appear to be handling the fallout of the crisis better than others, growth remains subdued.

One problem is that, in today's global markets, financial difficulties, whether in large countries or even in relatively small developed countries, can affect the entire financial system. The responses also have to be international.

In the face of burgeoning debt and deficits, and investor concerns about countries' ability to repay in some cases, market pressures have also prompted several large economies to announce draconian austerity plans. Others meanwhile have decided to wait, worried that spending cuts would hurt the economy. Some economists have called for increased stimulus spending to prevent anaemic recoveries from reversing back into recession. To be sure, the recovery, where it is taking place, is fragile. But the OECD believes that governments should start reining in their budget deficits from 2011, otherwise the deficits and debt will become counterproductive.

But this leaves governments with difficult decisions. How can they restore public finances and promote sound economic growth at the same time? Where should they cut spending? Is it possible to preserve the quality of vital but expensive public services, such as healthcare and education, while restraining expenditure?

The OECD view is clear. What the recovery needs is for governments to restore order to public finances while enacting reforms in the structure of their economies to enable growth to take hold. These include changes to streamline administration, activate labour markets, improve competition and bolster spending on social security. It means targeting taxes that favour greener growth, and focusing spending on education, innovation, healthcare and infrastructure. And it means doing all of this while continuing to support development aid and investment in poor countries.

Striking the right balance will not be easy, and the fiscal challenge is sure to dominate the global public agenda in 2011.