General Discussion of 'Monetary and Fiscal Institutional Arrangements: Have We Got Them Backwards?'

The discussion was focused on whether the idea of an 'independent' monetary–fiscal authority made practical sense given the significant areas of debate in fiscal policy – and the prevalence of political economy concerns.

The first set of questions was around whether current institutional settings in the United States already sufficiently corresponded to this – with the constraint of Congressional Budget Office (CBO) projections and monetary policy that is contingent on the stance of fiscal policy providing a rational basis for monetary–fiscal coordination. One participant noted that in an environment of low interest rates (specifically a real interest rate below the real growth rate), persistent primary deficits would be consistent with such coordination.

However, Dr Leeper noted that CBO projections have pointed to an explosive process for debt in the past and, with the COVID-19-related low interest rates rising, these projections are likely to show the same in the future. As a result, they do not appear to provide an anchor to rational policy setting – there is no 'feedback' from these projections and monetary policy setting into fiscal policy. Further questions focused on two areas: where are fiscal rules possible and credible? and where does this imply research on the nature of fiscal policy should be focused?

Several participants noted that the clearest areas for such fiscal rules were related to long-run fiscal rules, with an independent fiscal authority responsible for – and thereby taking the blame regarding – the transition path for those rules. As a result of this, such an agency would be responsible for estimating the appropriate size and structure of fiscal stimulus in the same way that current monetary authorities provide a path of interest rates.

Dr Leeper noted that such rules can be successfully applied – but that this isn't the type of coordination that is being discussed when it comes to integration with monetary policy, which is itself short term. Instead it is the concept of optimal fiscal stimulus itself which could be objectively defined and targeted.

Several participants disagreed about the ability to objectively describe either the distribution or the size of an appropriate fiscal stimulus. State-contingent fiscal policy can help by augmenting existing automatic stabilisers, but there is a distributional dimension to fiscal policy, which is not necessarily appropriate to separate from politicians and the political process.

There was also disagreement between participants on the speed with which existing fiscal policy can adjust to changes in circumstances (including the issue of time inconsistency), and the degree of knowledge that is available – or could be gleaned through research – with regard to the optimal level of any fiscal stimulus.

One participant noted that further integration of fiscal and monetary policy risks undermining the ability to anchor expectations or protect the independence of cyclical policy, which increased the risk of coordination on a 'bad equilibrium' with rising sovereign debt and pressure to keep interest rates low. Such a technocratic agency then faces a greater risk of capture.