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Comment Domenico Siniscalco

The chapter by Corsetti and Müller provides interesting evidence on the international spillovers of fiscal policy. The analysis is based on the literature on fiscal multipliers and it aims to measure the transmission of discretionary fiscal policy from one large “base country” (the United States) to other important regions (the UK and the eurozone). By comparing VAR models

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with simulations of a business cycle model, the chapter reaches three related conclusions:

1. The internal and cross-border effects of fiscal policy can be sizable, with cross-border multipliers ranging from 0.5 to 1.
2. Internal and cross-border effects, or spillovers, are not “mechanical,” but depend on the expectations of fiscal and monetary adjustment in the longer run.
3. Long-term bond prices reflect such expectations about the adjustment after the stimulus.

As a consequence, a discretionary fiscal stimulus in a big country can work on a global scale; the transmission mechanism is not only based on foreign demand and trade, but also on the financial channel just described. In particular, if governments lack credibility, the fiscal adjustment must overshoot to ensure the desired outcome.

The main results of the chapter, in my view, have both theoretical and policy implications. On the theoretical ground, the existence of international spillovers of fiscal policy calls for an international coordination of policies, which rests on the interdependence among countries and takes into account real as well as financial transmission channels. Such coordination should take place among global macro regions (as in the example provided by the authors), as well as within integrated currency areas such as the eurozone. As the game theoretic literature on coalition formation shows, the scope for cooperation among countries is bigger when the interdependence is higher (Ray 2007). And this is the case in the presence of monetary as well as non-monetary externalities. The argument, of course, works in the case of a fiscal stimulus, and even more in the opposite case of fiscal austerity. Within this framework, the existence of the cross-border effects of fiscal policy impacts the slope of the reaction functions among players (countries) and hence the gains from cooperation.

On the policy grounds, by highlighting the financial transmission channel of fiscal policy, the chapter provides a framework to discuss recent developments. For example:

1. The cross-border effects of public investment and public spending plans by some emerging markets.
2. The persistent high-risk premia in sovereign bond markets, and the need for super-austerity programs to correct them, in countries that traditionally lack in fiscal discipline, as a way to restore credibility and ensure a more efficient working of fiscal policy.
3. The rationale for controlling national adjustment programs within the eurozone (the so-called “fiscal union”).

As usual in the literature on fiscal multipliers, one can discuss the empirical robustness of the main numerical results. And the chapter could be pol-

ished in some theoretical features. But overall, Corsetti and Müller provide a fruitful framework to think about the fiscal policy response to the current crisis in an interdependent global economy. As Martin Feldstein observes, the arguments presented by Corsetti and Muller should definitely be part of technical background materials for G20-like meetings, and I add Ecofin and eurozone meetings as well. The discussion in global as well as European policy forums, in fact, mostly rests on the idea of interdependence among countries, but the channels of transmission of shocks and adjustment are not always clear.

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Comment Martin Feldstein

Although the wider issue of fiscal, monetary, and banking coordination lies beyond the scope of this chapter, the arguments and findings presented here should definitely be a part of technical background materials for G20-like meetings in the future. Specifically, how fiscal changes in country A affect output in country B is an issue of utmost importance for policy coordination. In my discussion, I would like to emphasize that government spending on goods and services is only a part of total government expenditure. This is especially so in the American case, where social transfers such as health-care expenditure and transfers to states make up most of government spending. Nevertheless, the findings borne out from the VAR analysis presented in the chapter are definitely interesting, and I shall discuss them in five points.

First, I must point out that the authors have made a very brave effort in entering the fiscal multiplier debate, which is one of the most controversial topics among macroeconomists. Upper bounds for the fiscal multiplier estimate tend to be around 0.5, or in other words: an increase in government spending by 1 dollar is expected to raise output by 50 cents at most. Considering the fact that imports to the United States only make up 15 percent of GDP and only a part of these imports originate from the UK and the eurozone, the cross-national impact is likely to be limited.

This expectation, which is my second point, is in stark contrast to the empirical findings of the chapter. These findings reveal a comparable cross-

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