Volume Title: Globalization in an Age of Crisis: Multilateral Economic Cooperation in the Twenty-First Century

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Volume Publisher: University of Chicago Press

Volume ISBN: cloth: 978-0-226-03075-3

eISBN: 978-0-226-03089-0

Volume URL: http://www.nber.org/books/feen11-1

Conference Date: September 15-16, 2011

Publication Date: December 2013

Chapter Title: Comment on "Multilateral Economic Cooperation and the International Transmission of Fiscal Policy"

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Chapter URL: http://www.nber.org/chapters/c12595

Chapter pages in book: (p. 299 - 300)

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.

Reference

Ray, Debraj. 2007. *A Game Theoretic Perspective on Coalition Formation*. The Lipsey Lectures. New York: Oxford University Press.

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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For acknowledgments, sources of research support, and disclosure of the author's material financial relationships, if any, please see http://www.nber.org/chapters/c12595.ack.

national multiplier to what the upper bounds of the domestic multipliers are estimated to be. We must ask ourselves how this could be.

That brings me to my third point, which is where I believe the answer mostly lies. As already mentioned, government spending on goods and services is only a part of overall fiscal measures (transfer payments, tax cuts, etc.) and they are likely to be correlated. To illustrate this point, one needs to look at the current job bill by the Obama administration, which amounts to 450 billion dollars. However, very little of that actually falls within the measure that the authors use. Meanwhile, the Fed is considering a new wave of monetary stimulus, further adding to domestic demand. Consequently, the estimates of around 200–250 billion dollars that these multipliers predict greatly overstate the actual stimulus brought about by just spending on goods and services. In other words, the omission of certain fiscal items and the correlation with monetary policy measures artificially bias the estimate of the multiplier.

Fourth, the time period under study deserves a remark. The years between 1980 and 2007 have not exactly been the high point for discretionary fiscal policy. Until the 1970s we used to practice activist fiscal policy, best epitomized by Nixon's remark: "we are all Keynesians now." Later on, mostly due to long lags of fiscal measures, activist fiscal policy was discredited. Monetary policy came to the forefront with the severe recession and the subsequent recovery engineered by the Fed under Volcker. During the Greenspan years, the Fed remained the protagonist in macroeconomic management by running monetary policy under a Taylor rule. Discretionary fiscal policy was largely off the table, which makes me skeptical about where the authors' measures are coming from. Short of looking at actual Congressional Budget Office documents, like Romer and Romer did, and relying on pure statistical techniques, such as the one devised by Blanchard, I suspect that the measures will be strongly correlated with monetary policy measures, again overstating the importance of fiscal policy.

Fifth and finally, the chapter makes very specific assumptions on agents' behavior by postulating that they anticipate the automatic reductions of fiscal measures in the future. However, a large part of where fiscal changes are coming from in the future is through legislated policies today. Stopping short of incorporating these measures' future impact on spending and taxes, the model thus assumes that only part of future changes will come to be anticipated.