

Government Deficit and Debt

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What is the difference between deficit and debt?

- When the government spends more than it collects in revenue and runs a **deficit**, it needs to make up the difference through borrowing
- The sum of all that borrowing is the national **debt**



Debt/Deficit to GDP Ratio

- Debt / GDP
- Deficit/GDP
- This measure gives an idea of the ability of a country to make future payments on its debt. If a country were unable to pay its debt, it would default, which could cause a panic in the domestic and international markets.
- The higher the debt-to-GDP ratio, the less likely the country will pay its debt back, and the higher its risk of default.



Stability and Growth Pact

- An agreement among the members of the European Union (EU) that take part in the Eurozone, to facilitate and maintain the stability of the Economic and Monetary Union.
- Based on the Treaty Establishing the European Community, it consists of fiscal monitoring of members by the European Commission and the Council of Ministers and, after multiple warnings, sanctions against offending members.
- The actual criteria that member states must follow:
 1. an annual budget deficit no higher than 3% of GDP (this includes the sum of all public budgets, including municipalities, regions, etc)
 2. a national debt lower than 60% of GDP or approaching that value.



Inflation and increased borrowing

- If the economy is in recession or growing below trend rate, higher borrowing may increase growth, without causing inflation.



Interest rates and increased borrowing

- As the government borrows more money, there are fewer funds available to private investors, and as demand exceeds supply, interest rates rise.



What is the European Economic Recovery Plan?

The objective is to drive a coordinated EU response to the economic crisis, that builds on the unprecedented level of coordination shown in response to the financial market crisis. The priority is to treat the symptoms of the economic crisis and protect jobs and purchasing power in the short-term while also investing in Europe's long-term economic health and in boosting the fight against climate change.

2011 Biggest Offenders

Deficit as a percentage of GDP

- Ireland: 13.4%
- Greece: 9.1%
- Spain: 8.5%
- Cyprus: 6.3%
- Slovenia: 5.6%
- France: 5.2%
- Slovakia: 4.8%
- Nether: 4.7%
- Portugal: 4.2%
- Italy: 3.9%
- Belgium: 3.7% on target to hit 3.0% in 2012

http://europa.eu/rapid/press-release_STAT-12-62_en.htm

Deficit Belgium

http://www.bbc.co.uk/news/business-13366011 Spanish politics: Can Rajo... Spain announces further a... BBC News - Eurozone i...

In graphics: Eurozone crisis

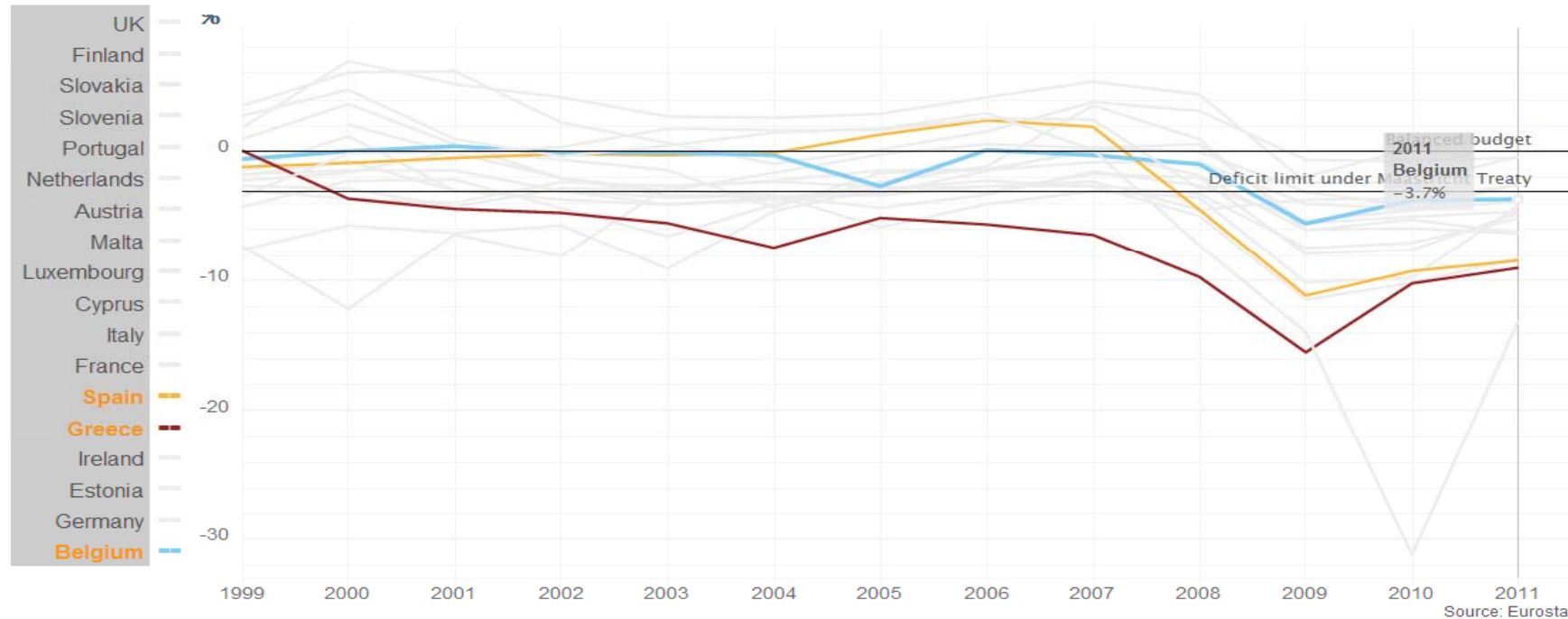
GDP | Unemployment | **Deficit** | Debt

Government annual surplus or deficit

A government's deficit is the amount by which its total spending exceeds its tax revenues. The government typically borrows the difference, adding to its debt. Some governments manage to spend less than they earn, so that they run a positive surplus. This chart shows that surplus (a number above zero) or deficit (less than zero) as a proportion of GDP (the total value of goods and services produced by the economy each year).

Select country to highlight data

Click and drag in the chart to zoom in



What have they done:

- New government took over in December 2011 with austerity measures:
 - Cuts in healthcare
 - Automatic rise in healthcare budget of 4.5% was decreased to 2%
 - Retirement age increased to 62
 - Development co-operation credits are frozen
 - Budget cuts for other ministries such as defense, railways, etc.
 - Increase in postage rates
 - Tax increases for tobacco, alcohol, stock options, & value added tax
 - Reduction in tax deduction for company cars



Additional austerity in May 2012:

- Tax increase in tobacco and investment products
- Postponing delivery of army helicopters
- Promoting generic medicine
- Less aide
- Post office must return \$289.6 million euros of state subsidies

The plan is to continue on the current path.



Resources

- <http://econ.economicshelp.org/2007/05/evaluate-problems-of-high-government.html>
- http://www.wikinvest.com/concept/Interest_Rates
- <http://www.ey.com/GL/en/Issues/Business-environment/EUROZONE-COUNTRY>

Questions?