

*OECD 2004 Economic Survey
of the United States*

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The OECD's view of the major challenges facing the US economy

- Reduce public dissaving by strengthening budgetary discipline and placing the public retirement and health-insurance systems on sound financial footings.
- Ensure policy settings are consistent with an orderly unwinding of the external deficit, based on a strengthening of national saving and exports, rather than weaker investment and growth.
- Lock in price stability and adapt the central bank's communications policy to the new low-inflation environment.
- Continue to re-build financial-market confidence by vigorously implementing and enforcing corporate governance and accounting reforms.
- Further enhance product-market competition to maintain higher productivity growth.
- Avoid protectionism and continue to build support for free trade.

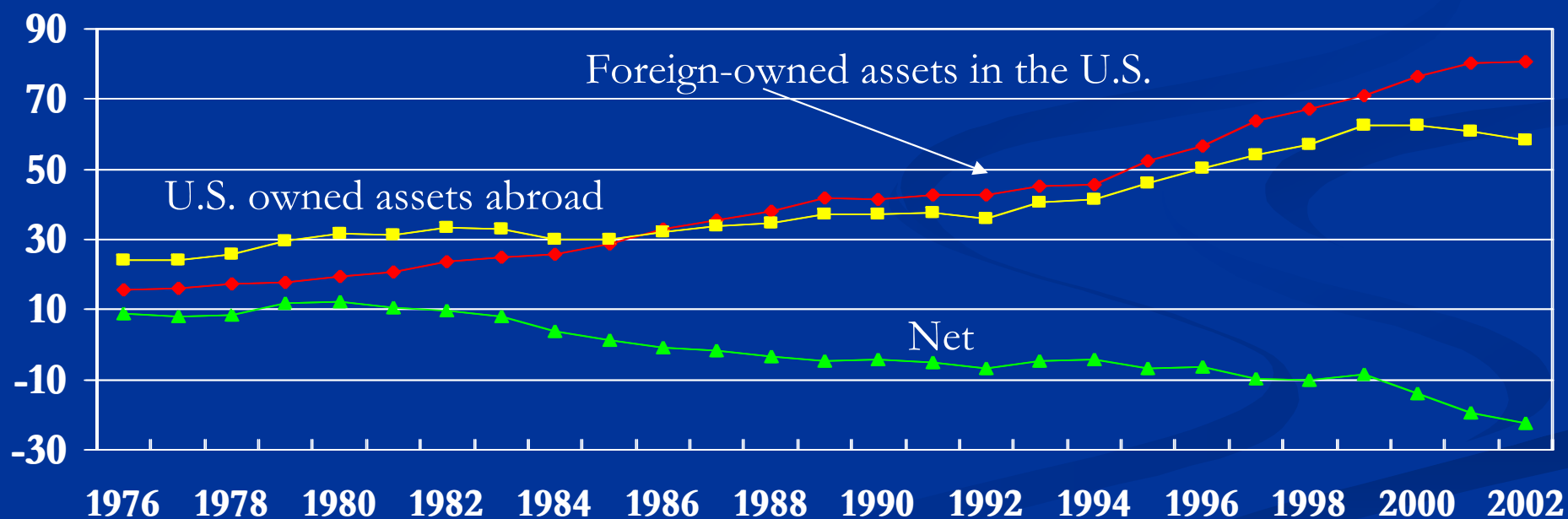
Near-term Outlook

	2004		2005	
	OECD	April consensus	OECD	April consensus
Real growth	4.5	4.6	3.7	3.7
Inflation (PCE deflator)	1.3	(similar)	1.1	(higher)
Unemployment rate	5.5	5.6	5.2	5.3
Current account	-562	-580	-604	-582
General government balance (% of GDP)	-4.9	(similar)	-4.1	(higher)
Federal funds rate	1.2	(lower)	2.8	(lower)
Ten-year Treasury rate	4.4	(similar)	5.3	(lower)

Coping with the external deficit

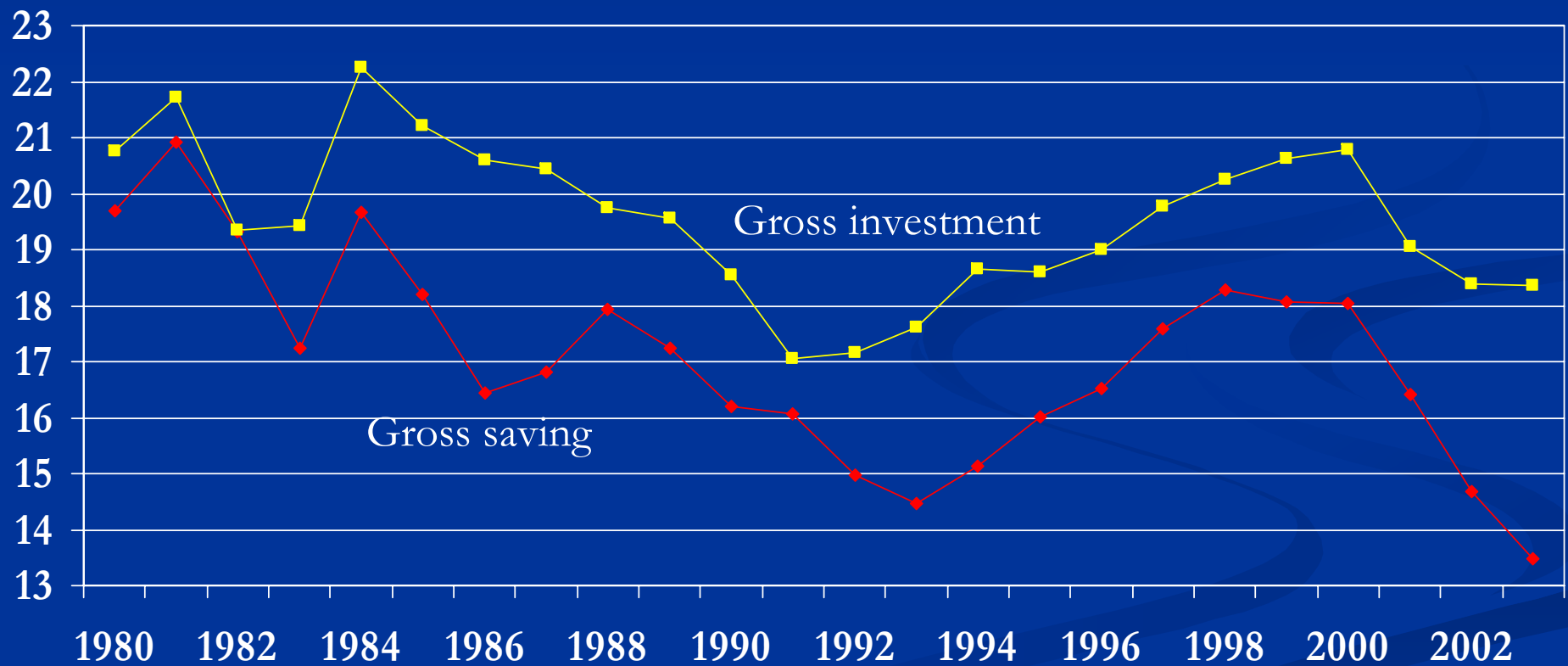
- Deteriorating net international investment position

Current cost, per cent of GDP



The external deficit reflects a trend decline in saving

Per cent of GDP



Ensuring fiscal sustainability and budgetary discipline is crucial

- Resolving the budget problem may well ease the pressure on the external deficit
- Recent official baselines are not unbiased forecasts?
- The economy will not be able to grow its way out of the current imbalance
- Spending restraint in the next few years is absolutely necessary but entitlement spending pressures are looming longer on the horizon
- Revenue increases may prove necessary

Maintaining price stability

- Exit strategy from recent overriding goal: sustainable expansion
- Focus on effective communications
 - Faster release of FOMC minutes
 - More frequent and expanded forecasts and risks
- Strengthening the policy framework
 - Quantification of the price stability objective

Other challenges

- Trade policy
 - Multilateral versus regional/bilateral liberalisation
 - The current debate on outsourcing
 - Trade disputes – steel, lumber, FSCs, textiles, agriculture
- Energy/environment
 - Fuel economy (CAFÉ standards)
 - Climate change
 - Clear Skies

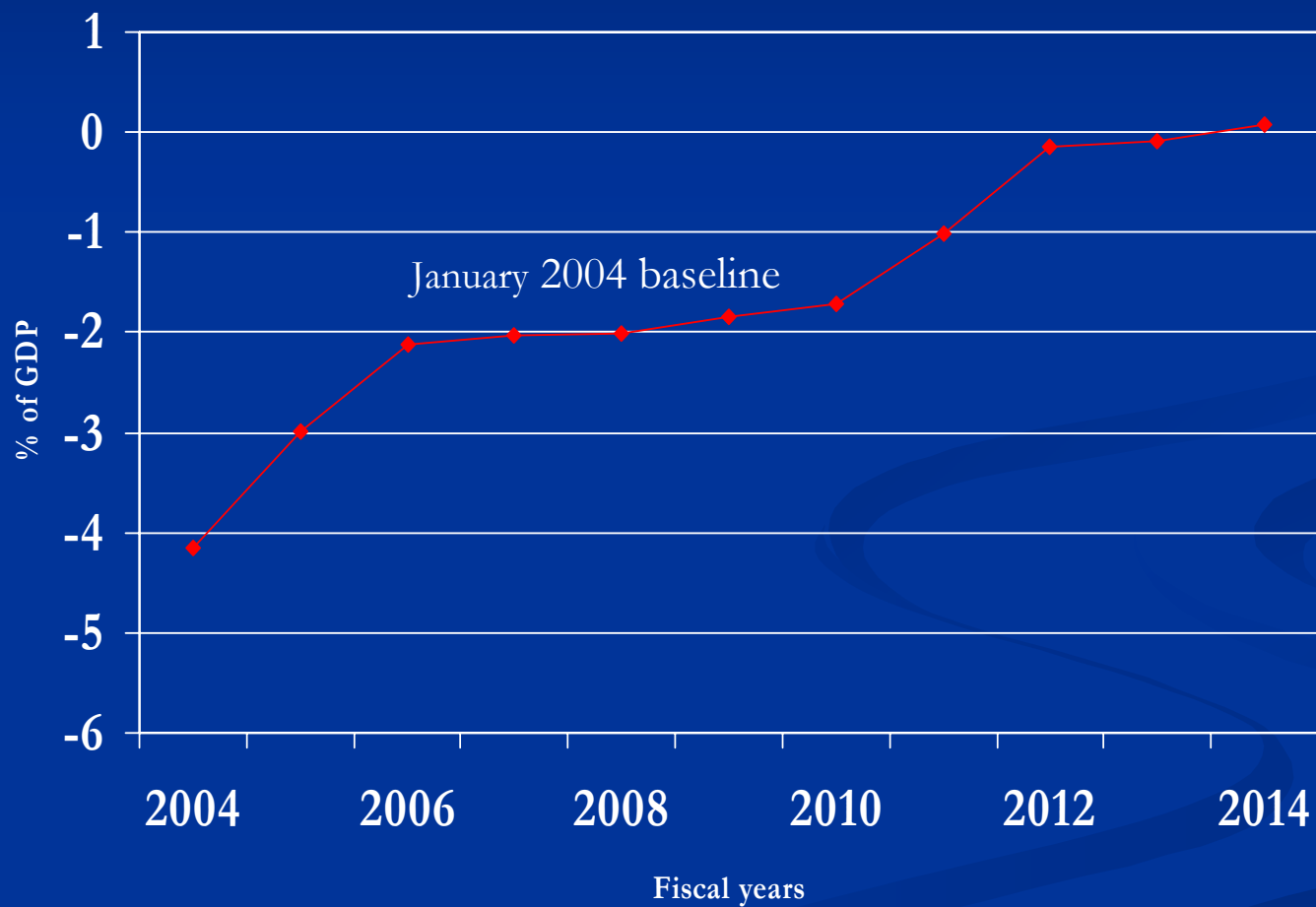
■ Social/equity aspects

- Health care costs rising and coverage falling
- Welfare caseloads staying down
- Poverty rates rising again

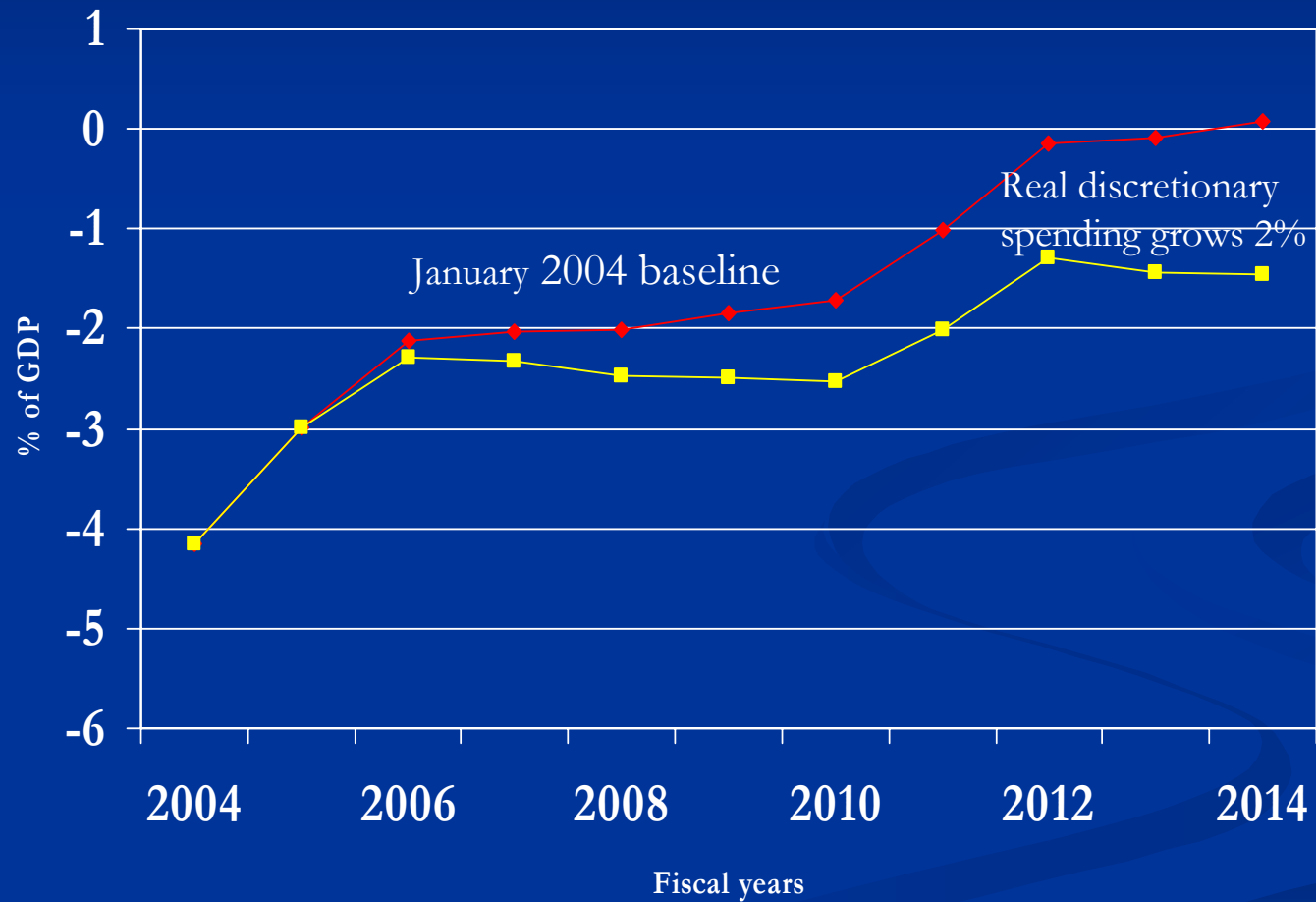
■ Education

- Poor outcomes : NCLB Act
 - Is it adequately funded ?
 - Is it going to achieve its goal ?

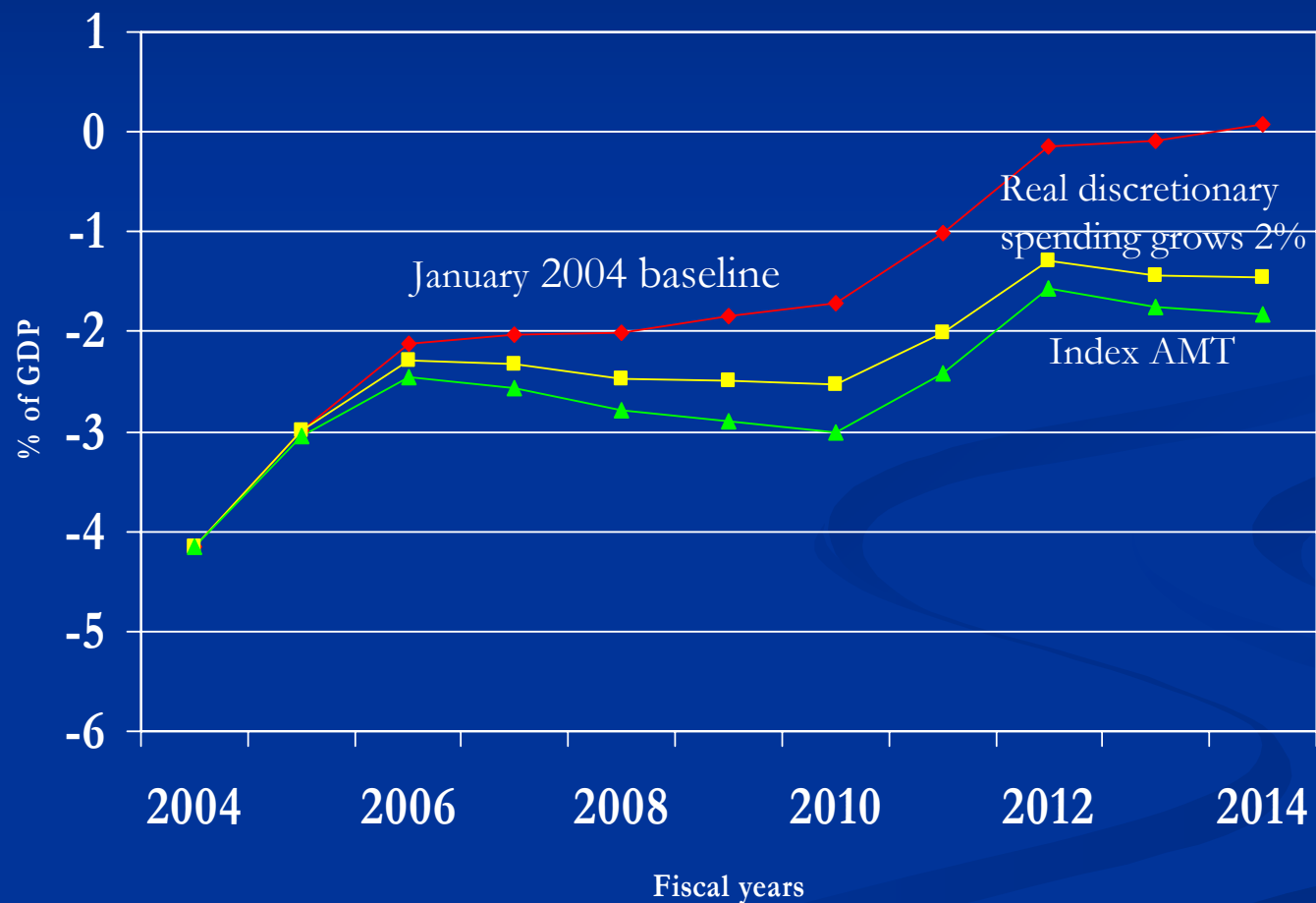
Budget outcomes under alternative policies



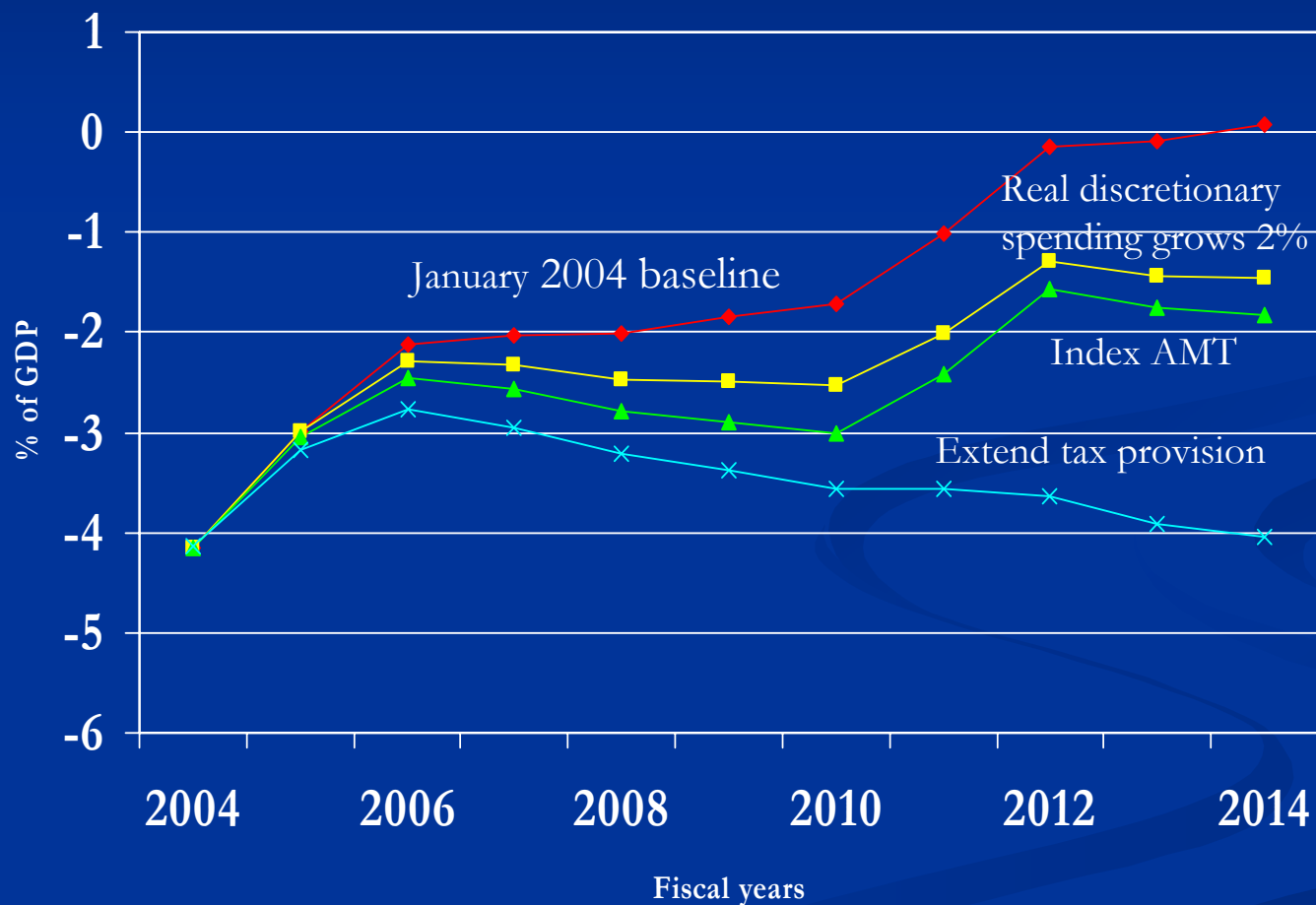
Budget outcomes under alternative policies



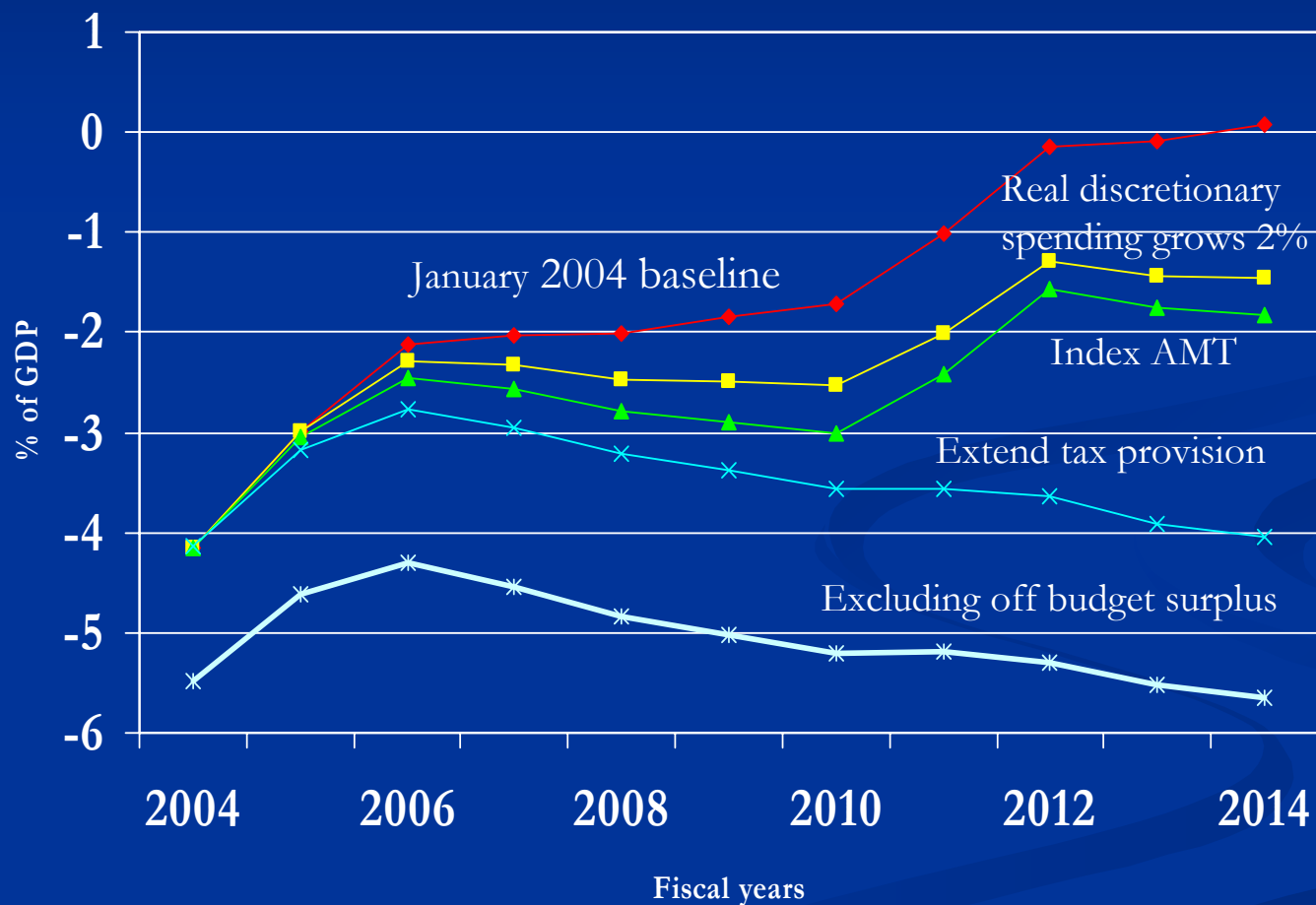
Budget outcomes under alternative policies



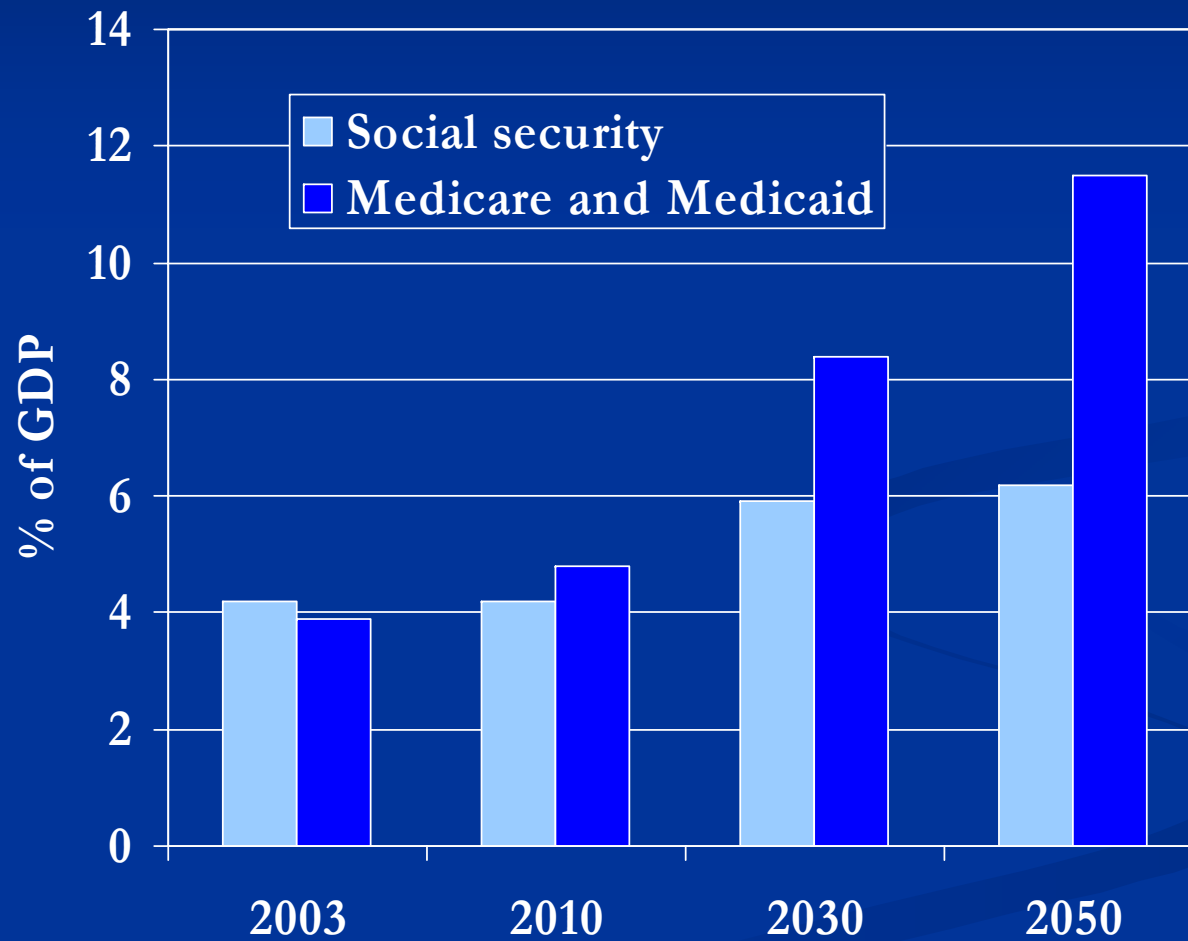
Budget outcomes under alternative policies



Budget outcomes under alternative policies



Long-term projected entitlement spending



Long-term projected entitlement spending

- As time progresses, cost of restoring the programmes to balance will rise rapidly. Hence, policy action is urgently needed.
- Safeguard Social Security through combination of revenue increases and benefits reductions.
- Future excess cost growth in Medicare and Medicaid is highly uncertain.
- PDB has considerably worsened Medicare's financial condition.
- Allowing greater scope for authorities to negotiate drug prices might reduce projected drug cost increases.

Budgetary discipline must be restored

- Deficit must be reduced if benefits from recent tax cuts are not to be overwhelmed by adverse consequences of deficits and higher debt.
- Curbing outlays is important.
- If budget cannot be balanced through spending cuts alone, revenues should be raised in least distorting manner:
 - Broadening tax bases.
 - Shifting to expenditure tax by introducing nationwide federal VAT.
- Reinstating expired BEA provisions, including PAYGO rules for mandatory outlays and revenue measures, would help.

Improving confidence and reducing distortions in financial markets

- Corporate governance and accounting scandals
 - Sarbanes-Oxley Act
- Under-funding of defined benefit corporate pension plans
 - Financial difficulties at PBGC
- Unequal playing field for housing GSEs (Fannie Mae, Freddie Mac)

Enhancing competition to sustain higher productivity growth

- Competitive forces are strong
 - Good economic performance
- Regulatory regimes are mostly appropriate despite some policy mistakes
 - Anomalous exemptions from competition law or jurisdiction
 - Patent litigation and review process
 - Telecommunications reform
 - Electricity sector reform

Thank You for your attention

- For more information:
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