



Executive Board Minutes 21/74-1

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United States—2021 Article IV Consultation

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Staff: Weber and Chalk, WHD; Zettelmeyer, SPR

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CEDA OGADA
Secretary

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¹ Minutes are the official record of a formal Board meeting in which the Board may adopt decisions and reach understandings related to the business of the Fund. Staff background documents issued before the meeting are the principal basis for the meeting. Preliminary “gray” or “buff” statements by Executive Directors and staff’s responses to Directors’ technical questions are circulated prior to the meeting. Adopted decisions and/or summings up—the Chair’s “sense of the meeting” or policy conclusions/recommendations—are issued after the meeting. The minutes include all these elements, as well as the discussion record (a verbatim transcript of the discussion lightly edited for clarity). Minutes are made public consistent with the IMF’s Transparency Policy and Open Archives Policy.

THE CHAIR'S SUMMING UP

Executive Directors agreed with the thrust of the staff appraisal. They welcomed recent efforts to bring the pandemic under control in the U.S., and noted that the major reduction in COVID-19 cases has combined with strong policy support to put the U.S. economy on a strong footing while generating positive outward spillovers to the rest of the world. Directors cautioned that this progress has come at a cost, significantly increasing the level of public debt and widening the current account deficit. Corporate and nonbank leverage have increased with rising asset valuations. Directors noted that the pandemic had weighed heavily on low income households. Moreover, the outlook remains subject to the evolution of the pandemic and the adoption in Congress of the fiscal measures proposed by the administration.

Directors welcomed proposals by the new U.S. administration to address structural challenges by redistributing resources toward vulnerable households, investing in infrastructure, incentivizing human capital accumulation, boosting labor force participation, and improving productivity. Directors also commended the renewed effort to reduce carbon emissions and increase resilience to climate change. Directors welcomed proposals to help offset the cost of these spending plans by increasing taxes on corporates and high-income households, closing tax loopholes and remaking the international corporate tax system, while increasing resources for the Internal Revenue Service. Directors noted that a better targeting of policies would strengthen their impact on macroeconomic and distributional outcomes, help trigger a bigger boost to aggregate supply, and lessen the risk of a sustained rise in inflation.

Directors observed that the actions of the Federal Reserve have been highly effective at managing the crisis and supporting recovery. The new monetary policy framework rightly commits to a near-term overshooting of the two-percent inflation target. This has facilitated a more rapid recovery and provided forward guidance on how the Federal Reserve will pursue its mandate of stable inflation and full employment. Directors welcomed the Federal Reserve's commitment to communicate well in advance its thinking so that the eventual withdrawal of asset purchases and monetary accommodation is orderly and transparent.

Directors stressed that policy adjustments are necessary to lower the fiscal deficit and put public debt on a gradual downward path over the medium term. They recommended that the authorities consider raising revenues, including through a carbon tax, higher taxation of fuels, and a broad-based federal consumption tax, as well as lessening the impact of an aging demographic on future spending.

Directors observed that systemic financial stability risks appear close to the historical average. However, the pandemic has revealed important shortcomings in the functioning-under-stress of systemically important U.S. markets and institutions. Directors urged that

serious consideration be given to structural changes in the operation of the Treasury market, key money markets, and prime money market funds.

Directors noted that the U.S. current account deficit has increased during the pandemic, and the external position is weaker than implied by medium-term fundamentals and desirable policies. They urged the authorities to roll back trade restrictions and tariff increases. They also urged that currency-related trade responses be avoided. Directors encouraged the U.S. to work constructively with its trading partners to strengthen the rules-based multilateral trading system.

It is expected that the next Article IV consultation with the United States will be held on the standard 12-month cycle.

EXECUTIVE BOARD ATTENDANCE²

K. Georgieva, Chair

Executive Directors

A. Andrianarivelo (AF)
 S. Chodos (AG)
 C. Huh (AP)
 A. Bevilaqua (BR)
 Z. Jin (CC)

D. Palotai (EC)
 A. Buisse (FF)
 R. von Kleist (GR)
 S. Bhalla (IN)
 D. Fanizza (IT)
 T. Tanaka (JA)
 H. Hosseini (MD)

P. Hilbers (NE)
 M. Poso (NO)
 A. Mozhin (RU)

R. Lim (ST)
 P. Trabinski (SZ)
 S. Riach (UK)
 E. Shortino (US)

Alternate Executive Directors

W. Nakunyada (AE)

A. Guerra (CE)
 F. O'Brolchain (CO)

A. Alhosani (MI)

B. Alhomaly (SA)

C. Ogada, Acting Secretary
 S. Kalra, Summing Up Officer
 A. Lalor, Board Operations Officer
 M. Eddy, Verbatim Reporting Officer

Also Present

Communications Department: M. Candia Romano, M. Soto Abril. European Central Bank: K. Nikolaou, R. Rueffer. Institute for Capacity Development: M. Erbenova. Legal Department: N. Rendak. Monetary and Capital Markets Department: H. Kang, J. Nelmes.

² For countries in each constituency, please see the Constituency Codes in the annex.

Office of Risk Management: B. Boulwood. Strategy, Policy, and Review Department: B. McDonald, M. Mrkaic, N. Sheridan, E. Van Heuvelen, D. Velculescu, J. Zettelmeyer. Western Hemisphere Department: K. Bergant, R. Cartaxo Mano, N. Chalk, A. Hodge, L. Lin, A. Medici, Y. Timmer, A. Weber. Office of Executive Directors: C. Cruz, C. Imashov, W. Keller, U. Nielsen. Executive Directors: I. Mannathoko (AE), M. Mahmoud (MI), P. Moreno (CE). Alternate Executive Directors: H. Azal (EC), M. El Qorchi (MD), F. Fuentes (BR), A. Grant (AP), L. Herrera (AG), C. Just (EC), M. Kashima (JA), M. Massourakis (IT), F. Mochtar (ST), R. N'Sonde (AF), O. Odonye (AE), L. Palei (RU), C. Roman (FF), J. Romero (CE), D. Ronicle (UK), B. Saraiva (BR), J. Sigurgeirsson (NO), F. Sylla (AF). Senior Advisors to Executive Directors: W. Abdelati (MI), H. Andrianometiana (AF), K. Badsı (MD), X. Bai (CC), E. Cartagena (CE), M. Choueiri (MI), O. Hendrick (AG), M. Ismail (AE), L. Johnson (AP), S. Keshava (SA), B. Lischinsky (AG), R. Mahabir (BR), D. Ong (ST), C. Quaglierini (IT), J. Rojas (CE), H. Saeed (SA), C. Sassanpour (MD), S. Senich (US), L. Smith (CO), F. Spadafora (IT), N. Thiruvenkadam (IN), R. Velloso (BR), L. Voinea (NE), B. Yoo (AP), M. Zhunusbekova (SZ). Advisors to Executive Directors: A. Abdullahi (AE), F. Al-Kohlany (MI), P. Al-Riffai (MI), A. Arevalo Arroyo (CE), S. Belhaj (MD), A. Biriukv (RU), B. Boostani (MD), I. Bustillo (AG), Campbell (UK), L. Cerami (IT), O. Diakite (AF), F. Dogan (EC), D. Fadhel (MI), V. Lankester Campos (CE), M. Merhi (MI), R. Moral Betere (CE), L. Nankunda (AF), I. Ogihara (JA), A. Olhaye (AF), B. Piasecki (SZ), B. Singh (IN), B. Slettvag (NO), L. Sturm (US), C. Westphal (US), J. Barroso (BR), B. Commaroto-Roverini (US), R. Gindrat (SZ), M. Law (CC), F. Lopez (CE).

DISCUSSION RECORD³

The Chair:

It is my great pleasure today to Chair a meeting on the Article IV Consultation for the United States for 2021. It is a very important economy, not only for the American people, but also in terms of the functioning of the global economy and, therefore, it is not surprising that the Executive Directors have engaged with gray statements. We got 23 gray statements, and we also have received a statement from the European Central Bank (ECB) representative.

Let me open the meeting with a short summary of what I have personally witnessed to be a very engaged Article IV Consultation. There have been very important developments in the United States in terms of the strength of fiscal support, the Fed adopting a new approach to monetary policy, and vaccinations in the United States (U.S.) rapidly scaling up, all of this resulting in a favorable environment for the recovery of the U.S. economy.

I want to thank wholeheartedly the U.S. authorities and Ms. Shortino for the engagement they have had with the team, and for very productive and insightful meetings I had together with the team with Secretary Yellen and Chair Powell. I found tremendous openness in the discussion to share our thoughts and our assessments of what we know and where we are still seeing a degree of uncertainty.

Headline of the consultations: The U.S. economy is on a strong footing as it emerges from last year's very difficult circumstances of, with a high loss of lives and dramatic economic impact, especially on the most vulnerable, businesses, and people. Seven (7) percent projected growth for 2021 is great news for the U.S. economy and also for the world economy. Positive spillovers are already visible, especially for countries that are more tightly integrated with the U.S.

On policy direction, a very significant step up in terms of shaping a more resilient future for the US. I also want to recognize our mission team for the US, Mr. Chalk and the team, and the Board of the IMF. For many years there has been shaping up of policy recommendations and it is very rewarding to see many of them now being integrated into policy packages in the US. I must stress the credit goes to the U.S. authorities, but a small piece of it I

³ Edited for clarity.

think is fair to attribute to the consistency and persistency of our team and the work of this Board.

Among those, are the strengthening of the social safety net by putting in place paid family leave, helping poorer families with childcare, actively deploying child tax credits and the earning of tax credit, and expanding access to education and healthcare. That is especially well-targeted to those that have been marginalized, so expanding opportunities will have a marked impact on productivity and growth over the long term. That is particularly clearly directed to working mothers, Black, Hispanic, and Native American populations.

Changing the corporate tax system, including coordinating on a global minimum tax, one of the big achievements of the G-20 we recently talked about. In addition, removing a range of loopholes and exemptions that have benefited the higher-income households; aiming to overshoot temporarily on the Fed's longer-term inflation goal; and last but not least, prioritizing reducing greenhouse gas emissions and making the U.S. more resilient to the effects of climate change.

Let me finish on the topic of inflation. This has been hotly debated outside the Fund and within our Board, within our staff. Our consultations on inflation were very open with both Chair Powell and with Secretary Yellen. We at this point share the view that the supply side disruptions are the primary reason for inflation accelerating. Therefore, it will be transitory. But we also recognize it and saw it in staff's report, that for this year inflation is going to be in the neighborhood of 4 percent. We would like to see how it shapes up over 2022. Our projections are for 2.5 percent inflation by the end of 2022, but, of course, we all recognize that we are in somewhat uncharted territory. We have never stopped the economy before and then restarted it with so much strength of the support for the recovery, so I would be very interested to hear the discussion today on this topic.

With this, I am going to turn to Ms. Shortino. And, again, my deepest gratitude to her, to the staff in her office, and to the U.S. authorities for very constructive, very open and frank discussions during this year's Article IV consultation.

Ms. Shortino:

I want to commend Mr. Chalk and the entire U.S. Article IV team. It was a very constructive engagement with our authorities. I also want to thank

all Directors for their helpful and insightful gray statements. I am very pleased to see that staff and the Board generally agree that the United States is focused on the right priorities, ending the pandemic, a strong U.S. recovery that will contribute to a global recovery, building infrastructure to modernize the U.S. economy, while supporting families and fighting climate change. I would also note the appreciation for our crosscutting efforts on inequality.

I will just make a few very brief remarks based on some of what we saw in the gray statements. At first, with regards to the outlook, we all agree that the highly effective vaccine campaign has supported the reopening of the U.S. economy, and that is clearly reflected in the consensus forecast, as Chair noted, that were around 7 percent gross domestic product (GDP) growth.

However, there is truly no precedent to the crisis we are experiencing today, and we need to expect that the recovery path may be quite bumpy, whether from a surge in the variants, uncertainty in the labor market, which I would note is still quite short of its pre-pandemic employment levels, or further adjustments in supply chains, but I would assure this Board that my authorities are continuing to monitor all of these developments closely and are prepared to make course corrections as needed.

With regards to the topic of inflation, we also continue to assess that recent inflation is transitory. It is concentrated in certain sectors and driven by idiosyncratic supply and demand factors. That said, the Fed is monitoring these inflation indicators very closely and stands ready to react.

I would also note that it is important that the Fed's flexible average inflation targeting regime is working. Critically, medium-term inflation expectations are stable and anchored around the 2 percent average inflation target.

I recognize that there are concerns around inflation spillovers and a potential tightening of U.S. monetary policy, but I would also note that Chair Powell reiterated to our Congress last week the Federal Open Market Committee (FOMC) is highly committed to effectively communicate any policy changes. And, in fact, I would say just from our interactions, there is a desire by the Fed to over-communicate on this front.

We appreciate the strong support from Directors on our U.S. fiscal and structural reform plans, including the American Jobs Act and American Families Act. As we noted in our buff statement, these are aimed at modernizing the U.S. economy and addressing long-standing structural

challenges. As Managing Director just noted, the vast majority of these measures have been recommended by the Fund and the Board in the past, and they will also provide important support to our efforts on climate change and racial equity.

I did take note of the comments that these programs could have been better targeted, but I would stress that the Administration took great efforts to get help to those that need it the most through these plans, and those are the lower- and middle-income families and those that have been disproportionately affected by poverty and historic legacy of discrimination and racism.

Finally, I would just reiterate that my authorities are firmly committed to multilateral cooperation. We welcome the recent agreement on the Global Minimum Corporate Tax and we are committed to achieving our goals under the Paris Agreement.

Mr. Bevilaqua:

Having issued a comprehensive gray statement, I will make only a few comments for emphasis.

The United States is a very clear example of how the combination of an effective mass vaccination program and aggressive policy support with due consideration of medium-term sustainability constraints can help us to overcome the pandemic. With mobility restored, healthy balance sheets, and supportive financial conditions, economic activity in many sectors is above pre-pandemic levels. Indeed, while the pandemic is still a major downside risk, an overheated economy (under tight supply constraints) is arguably another relevant risk reflecting the highly effective policy response. Both scenarios add significant uncertainty to the global recovery, but we would certainly be in a much worse position had the United States' policy response been less forceful.

In the medium-term perspective, there is room to foster labor market participation and improve productivity drivers to ensure sustainable and inclusive growth.

The jobs and family plans point in the right direction and should provide much-needed support. Moreover, the proposed changes in tax policy add an important fiscal responsibility dimension by ensuring proper funding. In this context, the close engagement with the international community on tax

policy and other issues, including the support to multilateral institutions, is very much welcomed.

We take note of staff's recommendations on the fiscal front. It seems sensible to better target policies on lower-income groups which go to the heart of productivity gains and social inclusion. It also seems appropriate to secure more sources of revenue, including by using a tax policy that better aligns private and social incentives in high-priority areas.

That said, we believe the authorities are very well placed to make responsible judgment calls on the economic and political tradeoffs of policy alternatives within reasonable parameters. Supportive financial conditions are another key element of the policy strategy. The recent review of the monetary policy framework while preserving flexibility introduced a built-in commitment to low for longer under current conditions. Indeed, some degree of overheating is now viewed as a desirable outcome. That said, if overheating comes too strongly and too soon, highly indebted households, firms, and countries may end up facing disruptive financial conditions, and it is reassuring to hear Ms. Shortino stating that monetary authorities are ready to act if it is necessary.

In this context, it is important to keep pushing for reforms, including in areas not currently covered by the Rescue Jobs and Family Plans. Hence, we support the call for more robust liquidity frameworks in non-bank financial institutions and closer engagement on international trade issues, which in the end are also crucial for productivity and inclusion.

The Chair:

I just want to echo what Mr. Bevilaqua said and what we heard from Ms. Shortino: how important it is to make sure that communications on monetary policy in an economy that is recovering and growing faster than projected before is so very important for the rest of the world. We are benefiting from positive spillovers. It would be fair to say that the US moving forward with so much strength is a global public good. It benefits the rest of the world economy, but we have to be mindful of the possibility of monetary policy changing tact a bit sooner, and the communication of this. Thanks to Ms. Shortino for saying the Fed is going to lean more towards over-communicating rather than under-communicating in that context.

Mr. Guerra:

The substantial and monetary policy actions taken by the U.S. authorities have supported a swift recovery from the COVID-19 pandemic and have an extensive positive impact on the world economy. As the Chair stated, it is important for the world what happens in the US.

Since we issued a gray statement, we broadly share the staff assessment, and I will provide only three points reacting to Directors' comments.

First, on the monetary front, we commend the authorities for taking timely actions to introduce a new monetary framework that has proven to be effective in supporting a more gradual policy approach during the pandemic. This has been instrumental, not only for securing the U.S. policy conditions, but also more adequate liquidity conditions in the international financial markets, including very importantly for developing countries and emerging markets.

Going forward, in promoting its maximum employment and price stability goals, as Chair also stated, it will be important for the authorities to continue with a clear and effective communication strategy. We see that in particular the assessment on the inflationary pressures will be complex given the various developments related to the temporary nature of the supply shocks in the context of the pandemic. Nevertheless, in this regard, we strongly believe that the credibility of the monetary framework will serve as an anchor to maintain inflationary expectations in check.

On my second point, on the fiscal front, we agree with the authorities that the proposed plans of the authorities on the programs are not only on spending aimed at solely supporting the economic recovery. They are, in fact, major public undertakings of investment that will contribute to addressing structural problems and build a more resilient and transformative recovery. The objectives are important to underpin a sound and sustainable recovery, modernizing the economy and increasing productivity and addressing climate change and flagging rising inequality. Importantly, these measures should be reflected in increasing potential growth, both in the short term and medium term.

Going forward, it will be instrumental that the authorities plan with sufficient time the necessary fiscal consolidation in the medium-term to

further increase fiscal buffers and set the public debt on a clear downward trajectory. The world needs a healthy U.S. fiscal stance.

Third, on the trade front, it will be important to consider the temporary effects the pandemic is having on the external position of the US. In particular, it would be useful to have a careful analysis of changes in the current position of trading partners that have a temporary nature, and they are expected to reverse to the previous position after the immediate effect of the crisis has faded. We stress that an additional focus should also be given to other trade imbalances that are more protracted in nature and that are deemed to increase in the baseline by staff. We should avoid a situation where if increased trade tensions at the global level would materialize if these imbalances are not reduced accordingly.

In this regard, while commending the authorities for its increased efforts to foster international cooperation in many fronts, it will be instrumental that the US continues to support the strengthening of a rules-based multilateral trading system, including the renewed engagement with the World Trade Organization (WTO).

Finally, on cooperation, we commend and really stress the authorities for their support on the global vaccination efforts that will be instrumental to support the recovery in the future.

The Chair:

The area of trade was one that we had quite a lively discussion. As we would see in the staff report, it is very much in that same spirit, let us make sure that the world economy functions to its fullest by also removing any obstacles to the free flow of goods and services. And, of course, the US is so important for reforming the trade system. Without that reform, we are not going to see trade on all four cylinders.

Mr. Hilbers:

We issued a gray statement and would like to emphasize the following four points.

First, we commend the authorities for their decisive fiscal and monetary response to the pandemic, which had positive spillovers throughout the global economy. We talk a lot about the negative spillovers in the Fund, but let us not forget that there are positive spillovers, as in this case, and the

Chair mentioned it. The countries in my constituency are grateful for the latter. Combined with an effective vaccination campaign, resulting in a vaccination rate of about 70 percent of the adult population, these measures have given a forceful impetus to the economic recovery.

A post-pandemic challenge relates to the gradual monetary policy normalization once the economy is back in full swing. Relevant in that context is that the recent surge in inflation appears to be transitory, driven in particular by supply bottlenecks as the economy reopens. After two decades of low inflation, temporary higher price-level increases affect the reallocation of resources of structural factors that argue for lower inflation remain at play.

Nevertheless, almost nothing in economics is 100 percent certain, and concerns about de-anchoring inflationary expectations should not be ignored. In this context, it is important to carefully communicate or even over-communicate, as Ms. Shortino just mentioned, the implications of the more flexible monetary policy framework.

Another topic that deserves close monitoring is the evaluation of the commercial and residential real estate markets. The perspective of monetary policy normalization could add strain, particularly to the housing market, where prices have been on a steep upward trajectory recently, which could raise financial stability risks. Every time is different, but let us not forget that many financial crisis in history were caused or worsened by imbalances in real estate markets. This is certainly not an exclusive U.S. issue and would be good to also address it more generally in the context of the WEO and GFSR.

Finally, a key challenge for the US, like for other advanced economies, remains the structural transformation to build back better a greener and more inclusive economy. As President Biden recently stated, “Within our climate response lies an extraordinary engine of job creation and economic opportunity ready to be fired up.”

In this context, we welcome the ambitious multilateral path on which the new U.S. Administration has embarked and commend the decision to rejoin the Paris Treaty on climate. America, it is good to have you back.

The Chair:

Mr. Guerra brought up that point here, the important leadership role of the US to vaccinate the world. It is on global taxation reforms that are so critical for the well-being of people everywhere.

Mr. Tanaka:

We issued a gray statement and would like to offer the following remarks for emphasis.

We welcome the rapid and resilient recovery of the United States and the economy from the COVID-19 thanks to the authorities' strong fiscal and monetary policies, which have been unprecedented in times of both quality and quantity under a crisis like no other, as well as the prompt and large-scale vaccine rollout. We commend the authorities' plan to use the opportunity to end the pandemic, to build back better the social network under the American Jobs Plan and American Family Plan with better infrastructure, more support to families, and a foundation to tackle climate change.

On fiscal policy, we commend the authorities' sizable fiscal plan to achieve, according to Ms. Shortino, modernizing the U.S. with higher productivity, brighter digitalization, and increased labor market participation, particularly of women and minorities. Government spending should continue to support the most vulnerable and those most affected by the pandemic. Better targeting on both revenue and spending fronts are warranted to enhance effectiveness and to ensure fiscal consolidation in the medium term.

On the financial front, we commend the Federal Reserve Board (FRB) for deploying all tools to support the U.S. economy and the introduction of the new monetary policy framework based on flexible average inflation targeting.

Going forward, as multiple factors could impact on inflation dynamics, including labor mismatches, supply shortages, and expansionary fiscal policy. We appreciate Chair's commitment with the dialogue with the Secretary and the Chairman. The authorities should be vigilant to press development, whether it is transitory, and communicate carefully its monetary policy stance, as Ms. Shortino fully recognized the importance.

The authorities should also closely monitor financial market developments as monetary and fiscal policy normalize, such as risks to the financial system from zombification and associated spillover risks to emerging economies.

On structural reforms, we commend the Administration for putting forward an ambitious whole of government equity agenda to advance fairness and opportunity. Measures such as increased childcare, financial support for

low-income college students, and expanded health insurance will serve to facilitate the accumulation of human capital and higher labor force participation. We also welcome the return to the Paris Agreement by the United States and commend the authorities' bold comprehensive plan to roll out infrastructure investments, regulatory changes, and youth standards, including the agricultural sector.

The Chair:

One point that perhaps is worth reflecting on is the Fed's coming up with its flexible inflation-targeting framework in a timely manner. It helped out the central banks that have been advancing in that same direction to accelerate their own position in that regard, so it is also leadership in that monetary policy area.

Mr. O'Brolchain:

This consultation provided a number of helpful recommendations to help close the fiscal and external gaps that were opened by the pandemic, address financial sector vulnerabilities, and create a greener and fairer America.

The report also reminded us of just how much the current Administration has been able to achieve in just six months amidst the crisis with largely positive spillovers to the global community, as others have already outlined. That should be a key takeaway here, and the authorities should be commended. Looking at staff's response to the Board's questions, we would underscore the value of the new inflation-targeting framework to strongly anchor long-run inflation expectations, which are under pressure from transitory forces. Here, we reinforce what other speakers have said and also welcome Ms. Shortino's assurances about over-communication.

We would also encourage the authorities to prioritize those Financial Sector Assessment Program (FSAP) recommendations that apply most directly to the vulnerabilities exposed by the pandemic, including developing macroprudential tools for nonbanks.

Staff also helpfully confirmed for us that many of the steps that will be needed to achieve the Administration's climate goals are yet to be defined. We encourage staff to remain closely engaged with the authorities as the climate policy settings firm up.

Lastly, like Mr. Poso in his gray statement, we strongly welcome the ambition to create a national paid family leave program that alongside improved access to childcare would help increase labor force participation among women.

I would like to close with a message from our Canadian authorities. Canada and the U.S. share the longest border in the world at almost 9,000 kilometers, and nearly 1.7 billion in goods and services cross it every single day. For health and safety reasons, that border has been closed to non-Canadians since the onset of the pandemic. Discussion with the U.S. authorities regarding reopening plans are ongoing, but Prime Minister Trudeau recently indicated that Canada could expect to start allowing fully-vaccinated U.S. citizens and permanent residency into Canada as of mid-August for nonessential travel. Canada is looking forward to greeting visitors from its closest partner and ally and continuing extraordinary friendship that has grown deeper and stronger through this crisis.

Mr. Andrianarivelo:

As we have issued a gray statement, I will limit my intervention to three points for emphasis.

First, we commend the U.S. authorities for increasing vaccine discovery, development, and rollout reach, coupled with massive supportive fiscal and monetary policies, explaining the impressive economic rebound underway. The great and rapid adaptation capacity to the shock of the pandemic by the U.S. economy should generate positive spillovers and help foster an effective recovery of the global economy, as it was stated.

Second, with new programs mentioned, it will be important that the authorities remain vigilant to address the downside risks of the worsening of the pandemic and sustain their efforts, including on the public health front to vaccinate more people in the US and the rest of the world.

The authorities should continue to implement supportive macroeconomic policies to strengthen the recovery but better target, and implement tax increases on corporations and high-income households to finance the comprehensive infrastructure plan that the country needs, and reduce the accumulation in public debt in the medium-term.

Third, we welcome the Administration's intention to increase support for the communities that have been historically underserved, marginalized,

and adversely affected by persistent poverty. Besides addressing long-standing structural impediments to structural mobility, as also stressed by Ms. Shortino, it will be essential to strengthen the foundations for growth and resilience, rise in productivity and labor force participation, reduce poverty and income inequality.

Mr. von Kleist:

As we have issued a comprehensive gray statement, I will highlight only three points. First, let me reiterate that we broadly concur with the thrust of the staff assessment. The US is in the midst of a remarkably strong economic rebound, supported by extraordinary fiscal support and expansionary monetary policy.

However, we continue to see substantial downside risks due to possible worse-than-expected developments with respect to the pandemic as well as due to higher-than-expected inflation dynamics. Obviously given the importance of inflation risks for the US and its spillovers on the world economy, we strongly welcome that staff will continually scrutinize and assess developments in this area.

Second, on fiscal policy, we welcome the new Administration's forceful response to the pandemic shock but agree with staff that a more targeted approach, especially to the most vulnerable groups, would have been beneficial. I thank, however, Ms. Shortino for her additional remarks on this issue.

While public debt remains sustainable and debt service and costs are currently low, rising healthcare costs and demographic change justify the timely development of a credible fiscal plan to reduce the level of the national debt over the medium-term.

Lastly, on monetary policy, we welcome the Fed's continued expansionary stance regarding the new monetary policy framework. We understand its merits in providing more flexibility in the mandate, but we also see risks. Allowing the inflation rate to overshoot for longer might be misunderstood as a manifestation of fiscal dominance, which would make the anchoring of inflation expectations thereafter more difficult. Conveying the intricacies of the concept to the wider public might also constitute a major stumbling block in its functioning. Precise communication will thus be very important.

To conclude, like others, we strongly welcome the authorities' renewed international commitment, including on climate policy, and invite them to join further active collaboration in multilateral institutions, such as the WHO, the WTO, as well as international tax issues. We also welcome the recent strong support of global vaccination efforts by the US.

Ms. Riach:

We broadly agree with staff's analysis. The United States' unprecedented policy response has contained the economic impact of the pandemic and is supporting a very welcomed, very strong return to economic growth.

As Chair said, the coordinated policy response has been essential, both for the good of the U.S. people and for the functioning of the global economy. It is unsurprising that many of the questions and many of staff's responses focused on inflation and the risks of an over-heating of the U.S. economy, but I thought that Mr. Bevilacqua put it very well this morning when he recognized the risks of over-heating while making clear that the risks for the global economy of insufficient action from the U.S. authorities would have been far higher.

We agree with staff that the new monetary policy framework has helped to support a more rapid recovery and is being helpful in managing policy from a conjunctural perspective. I agree with Mr. Guerra that the credibility of the U.S. monetary system will serve them and all well going forward.

I also join others in welcoming Ms. Shortino's comments this morning on the Fed's commitment to clear and effective communication. We commend the authorities for unprecedented fiscal support and, in particular, for efforts to focus that response on providing assistance to those who need it most, including strengthening the social safety net and expanding access to education and healthcare. Targeting support to vulnerable groups should remain a focus going forward.

We agree with staff and with other Directors that attention needs to be paid to the fiscal path over the medium-term, and we support the revenue measures being considered by the authorities. As staff say in their answers to questions, the debt-to-GDP ratio will continue to rise over the medium-term regardless of the revenue measures being proposed because of the aging population and rising healthcare costs.

We welcome the focus on climate issues in this report, and the analysis on carbon pricing is particularly helpful. We strongly welcome the United States' return to the Paris Agreement and a commitment to reduce net greenhouse gas emissions by 50 to 52 percent by 2030. This represents a critical and positive shift.

We also welcome the authorities' new commitment to assess the risks that climate change may have on financial stability of the US, as set out by Secretary Yellen.

Mr. Alhomaly:

We issued a detailed gray statement, and therefore I will limit my remarks to a few issues today. First, we welcome the remarkable recovery of the US economy against the backdrop of the authorities' strong policy support. In this context, we are encouraged that the economy appears set to return to full employment sometime in 2022, and we welcome staff's assessment that the sustained pickup in inflation seems unlikely. But looking ahead, the spread of the delta variant in parts of the US is worrisome, and indeed one of the key risks to the favorable economic outlook is the uncertain path of the pandemic, like everywhere in the world, but at the same time, given the relatively high rate of vaccination among the vulnerable population, we are comforted to note that this should limit hospitalizations and therefore reduce the need for containment measures, which in turn mitigate the macroeconomic impact of another surge in cases.

Second, we take note of staff's assessment that the Jobs and Family Plan and other considerations are expected to boost the level of potential output. And, in particular, we welcome the importance placed on expanding access to education, healthcare, and affordable childcare. And we are reassured by Ms. Shortino's comments today that these envisaged measures are expected to support human capital accumulation and higher labor force participation, particularly for those who are disproportionately impacted by the pandemic.

Third, we welcome the commitment of the Federal Reserve towards continued clear communication and early indication of any shifts in asset purchases or policy rates. This, of course, will help in avoiding market volatility and mitigating spillovers, especially in emerging market and developing economies, as mentioned by Mr. Guerra and others today.

Finally, we welcome the US's firm commitment to climate change. However, we do not see any traction for staff's recommendation on carbon taxes and higher taxation of fuel. Staff have also acknowledged that there is a great deal of uncertainty on the extent to which the US will need to rely on carbon pricing. If the main goal is to reduce greenhouse gas emissions, then, of course, there are many other policy options, including regulation standards or subsidies, as rightly underlined in the buff statement.

To conclude, I would like to express my authorities' appreciation to the U.S.'s firm commitment to multilateralism, including the support provided to expedite the vaccine rollout in low-income countries.

Mr. Buisse:

The United States has been implementing a considerable response to the pandemic, which is clearly bearing fruit. The economy is back on a strong footing, which also generates positive spillovers to the world economy.

The deployment of the Building Back Better agenda is key to support families and tackle big challenges, such as climate change and inequalities.

I issued quite a comprehensive gray covering potential growth, inflation, the job market, trade, but let me highlight three points this morning.

First, on the fiscal front, I strongly support the revenue measures being considered by the authorities. Their proposals have important implications for the international system of corporate taxation and their historic agreement reached within the US and the G-20 paved the way for a fairer global taxation.

Additional domestic measures could be considered, notably on indirect taxation, value-added tax (VAT), carbon tax, and fuel tariff increases could be mobilized. Let me just underline that it will be difficult anywhere to increase or create a carbon tax without reducing the revenue to prevent any impact on inequality. That is rightly mentioned in the report.

From a fiscal and environmental point of view, I also see great merits on the rebates schemes described in the report, that if we have the right incentives, it may be socially easier to accept and not by definition less costly than subsidies.

On the expenditure side, I support the recommendations aimed at curbing the rising cost of healthcare while extending the health coverage to

reach universal access. I see much potential in developing competition between suppliers in local markets and increasing transparency. I thank staff for the very useful buff on this.

Second, on climate, I strongly welcome the authorities' new emission targets following the return to the Paris Agreement that must now be operationalized. Investments in building sufficiency in electric vehicles will play a crucial role in this transition. However, I share the views expressed by many of my colleagues and staff that these investments and subsidies will be most effective as a complement to carbon pricing and not as a substitute. Regulatory changes and standards are also an efficient complement to carbon pricing, for instance, limits on greenhouse gas emission from new vehicles or the implementation of feebates, as I discussed.

Lastly, I want to underscore the importance of decarbonization, power of decarbonizing power production. Greening the power sector via nuclear energy or renewable energy is indeed necessary to make electrification of industry and transport relevant to climate policies. It is almost a tautology to say so, but if the electricity is not decarbonized, it is misleading to speak of zero emission vehicles.

My third and last point is on the importance of fighting inequalities and advancing towards a more equitable society. The US has significant scope to strengthen its social safety nets, and I very positively welcome the proposed policy changes that aim to increase the progressivity of the tax system and expense spending in areas that have the most impact on those at the bottom of the income distribution, education, childcare for the system, and healthcare. The American Jobs and Family Plans certainly responds to long-standing structural fragility of the U.S. economy, and I hope they can be implemented soon despite the political uncertainty.

Mr. Palotai:

We would just like to add a few more points. The prompt vaccine rollout and accommodative strong policy response has enabled the rapid rebound of the U.S. economy. However, stagnating vaccination rates and resurgent variants are causing a risk to the outlook.

Like many other directors, we broadly agree with the direction of fiscal policy and measures addressing structural challenges which aim at increasing productivity, labor force participation, and poverty reduction.

However, similar to Ms. Riach, we note that the proposed taxation goals are subject to risks in terms of political acceptance. Therefore, it is key to carefully implement the American Jobs and Family Plans.

On monetary policy, like Mr. von Kleist and others, we note that the authorities should continue to closely assess the inflation developments and take prudent action to avoid further overshooting and ensure that inflation expectations remain anchored.

While upside risks to the inflation outlook have increased, the U.S. economy is still a long way from maximum employment, which makes it more challenging for the Federal Reserve to achieve its statutory mandate. Although the shift to flexible average inflation targeting has had a positive effect on the economic recovery, the new regime also poses some uncertainty for the economic actors regarding the horizon over which inflation is averaged. Therefore, we would see merit in additional parameterization and clear communication in this regard.

We also note that maintaining a good external monetary policy stance can also lead to excessive risk taking, further increasing asset prices and encouraging over-indebtedness. Therefore, close monitoring of unintended side effects and consequences of asset purchases are also warranted. If the recovery remains on a strong footing, a two-speed tapering can also be considered.

Finally, on climate change, we are also encouraged by the authorities' policies regarding strengthened focus on climate action, which requires a holistic approach and further efforts to make the economy greener. The new overarching investment plan should also be considered as an opportunity to pave the way to a low carbon economy.

Mr. Trabinski:

We commend the authorities for the substantial turnaround from the beginning of the pandemic and the remarkable economic recovery that has been initiated. We think that at this stage it is key to ensure that the recovery will not be eroded by mounting inflationary pressures, which will mainly weigh on the living standards of the lower and middle-income households.

Let me make three points for emphasis today. First, on fiscal policy, we are encouraged by Ms. Shortino's assertions in her statement that the fiscal plans under preparation are not just spending programs aimed at stimulating

the economy, but they are rather aimed at supporting the structural transformation and productivity, especially in terms of the much-needed digital, climate, and demographic transitions. It was, I believe, Alexander Hamilton who said that “There is no purpose, to which public money can be more beneficially applied, than to the acquisition of a new and useful branch of the industry; no consideration more valuable than a permanent addition to the general stock of productive labor.” I just wanted to make this statement because it resonates well with the authorities’ plans.

We agree that at this stage tax and spending proposals should be calibrated to generate a slower demand and a higher supply impulse. This will contribute to keeping in check the risk of over-heating the economy. In the medium-term, fiscal adjustment reverting public debt dynamics will be critical.

Second, on the monetary side, the flexible average inflation targeting framework shoots upward growth in the short term. In this context, we note the authorities’ assessment that recent inflation readings largely reflect transitory factors and base effects, including idiosyncratic supply and demand factors.

Going forward, inflation dynamics and inflation expectations will need to be assessed with caution to ensure a well-guided and adequately-paced return to policy normalization.

Third, on international trade, we take positive note of the authorities’ ongoing review of trade tourism restrictions. External imbalances should be addressed by identifying and eliminating unreliable distortions and establishing sound economic fundamentals. We encourage the U.S. authorities to constructively work with trading partners in the context of a rules-based multilateral trading system to better address the underlying macrostructural distortions that are affecting external positions.

Mr. Huh:

Resilience of the U.S. economy is remarkable with an effective vaccine rollout and comprehensive boosting package, the U.S. economy has been growing back in a short period. Even though some bottlenecks in the course of activating supply chains with pent-up demand bring about temporary challenges, the historic public investment packages will transform the U.S. economy to the next level with green productivity and more inclusiveness.

As we issued a gray statement, we would like to briefly highlight three points for emphasis. First, we welcome not only the comprehensive policy response to the pandemic but also the ambitious and timely public investment packages for the infrastructure, jobs and families, for the future of U.S. economy and society.

Just as John Kenneth Galbraith mentioned in his book *The Affluent Society* in 1958, the public investment of the United States has not kept good balance with affluent private consumption in investments, which has resulted in insufficient social infrastructure and worsening inequalities. Successful implementation of tax reforms will be instrumental to mobilize the resources for the long-term investment.

However, we also would like to suggest that the fiscal consolidation should be pursued in the medium- and long-term horizon with the flexibility to minimize possible side effects because it will take time to materialize the productivity and investment from the public investment.

Second, the inflation risk should be well-monitored and future policy changes should be clearly and timely communicated. Any further shift in the policy rates and separate trades can lead to unintended tightening of fiscal conditions with damaging spillovers, in particular, to the developing countries with less debt sustainability.

In this vein, closer and well-communicated policy coordination in global platforms such as G-20 would be highly appreciated, considering serious uncertainties in the global economy with underlying financial instability and unbalanced recovery.

Finally, we support staff's call for reversing trade restrictions and tariff increases and for constructive collaboration with the trading partners to authorize the distortions in the trade flow and investment leadership. We also believe that an open, transparent, and world-based trading system is the best way to ensure fairer and stronger global trade, as Ms. Shortino also mentioned in her introductory comments.

Ms. Lim:

Like many other Chairs, we commend the U.S. authorities' decisive policy responses that have placed the economy on a strong recovery path. The Administration's fiscal agenda for Building Back Better is also commendable

in its ambition to address the countries' long-standing structural issues, including inequality.

We urge the authorities to carefully consider staff's recommendations for better targeting of the policies to strengthen macroeconomic distributional outcomes, especially considering that these measures are not costless and will add pressure to the nation's fiscal balances and public debt trajectories.

Notably, staff in their responses to questions highlighted a variety of impediments, both political and institutional, to better policy targeting during a crisis. For instance, shock handling at the state level and unemployment computer systems. We urge the authorities to work on resolving these impediments to enable more targeted and effective responses to future crisis.

More structurally, like several other Directors, we also urge the authorities to proactively address issues relating to the exceptionally high levels of U.S. healthcare spending, which staff assessed to be arising from structural market-powered-based issues. Market and regulatory reforms are understood to be multi-pronged and will take a long time to implement and bear fruit and are especially critical given the potential substantial impact of fiscal spending amidst the aging population profile. In our opinion, microlevel domestic reforms such as the above also have a role to play in helping strengthen the U.S.'s external position other than recommendations that staff put forth in the report.

On the financial sector, decisive measures by the authorities to help to preserve the stability of the system, and we note that the banking system remains well capitalized and sufficiently liquid. That said, vulnerabilities in relation to elevated asset valuations, such as in the real estate, as mentioned by Mr. Hilbers and Mr. Palotai in their gray statements, will need to be carefully monitored not just in the US but also more broadly.

Finally, we join other Directors in strongly welcoming the authorities' renewed commitment to multilateralism and stepped-up international engagements and commitments in areas such as current change and trade policy.

Mr. Poso:

The first six months of the new Administration have been breathtaking. Like others, we welcome the bold policy response that is supporting a strong recovery, also globally. We have issued a comprehensive

gray statement so I will limit my intervention to a few additional comments and questions.

First, we thank staff for the detailed written responses to our questions on the inflation trajectory and note that staff expect core personal consumption expenditure (PCE) inflation to fall back to around 2 percent by Quarter 1 (Q1) next year. Against this background, I was a little surprised by the formulation in the staff appraisal that the ongoing rapid pace of recovery will necessitate a shift in monetary policy already in the coming months. I would appreciate if staff could explain what kind of a shift in monetary policy they see as necessary already in the coming months, taking into account also staff's rather moderate inflation forecast.

Second, as the increasing debt trajectory needs to be reversed in the medium term, we welcome the authorities' clear ambition to raise the tax-to-GDP ratio through more progressive taxation of individuals and by increasing the corporate tax rate. Here the historic agreement reached within the Organisation for Economic Co-operation and Development (OECD) at G-20 will have important international implications and pave the way for global taxation that is effective and fair.

Third, regarding the measures to tackle rising healthcare costs, we are somewhat skeptical about staff's proposal to increase user contributions and age limits given the already unequal access to high-quality healthcare.

Like Mr. von Kleist and Mr. Sattler in their gray statement, we believe that promoting more competition and reducing inefficiencies in the system would be a more sustainable solution. Staff's comment on this issue would be welcome.

Fourth, we fully support staff's concern that many of the trade distortions introduced over the past four years still remain in place. While we agree with the authorities that it is important to ensure that gains from trade are widely shared and benefit workers, we believe that this is best achieved by domestic policies, complementing an open trade policy.

Finally, we would like to join other Chairs in commending staff for the strong coverage of climate-related policies in the report. We strongly welcome the authorities' ambitious plans to curb carbon emissions following the return to the Paris Agreement, and the steps needed to achieve these goals should now be clearly defined.

While recognizing the different costs countries can take to reduce emissions, we agree with staff that it will be costly and hard to achieve the Administration's climate objectives without greater reliance on carbon pricing.

Mr. Bhalla:

To begin with, we commend the U.S. authorities for the massive vaccination drive which has helped in containing the pandemic and paved the way for a progressive reopening of the economy. We also welcome their efforts in providing vaccines to support other countries and Covid-19 Vaccines Global Access (COVAX).

When the global minimum tax was first proposed, this Chair supported it as a most innovative and desirable tax. We felt that it will arrest unfair international competition. We continue to believe in the desirability of a global minimum tax. We recognize that a global minimum tax is just a proposal at present and needs international cooperation to be enforceable. In this regard, we would like to ask staff for some more details. For example, staff may wish to provide estimates of how many more firms in the U.S. and globally will be taxed at a higher rate than at present.

Other questions for the staff pertain to the forecast of GDP growth and inflation post 2023. U.S. GDP growth averaged 2.3 percent a year between 2011 and 2019. Inflation averaged just 1.8 percent. Over the years 2023 to 2026, the staff is forecasting GDP growth at only 1.7 percent per annum, about a third lower than the recent 10-year average. If realized, this decline will be a historically deep decline in long-term GDP growth. Inflation on the other hand is meant to rise from 1.8 percent to 2.5 percent from 2023 to 2026. The average corporate tax reform is meant to rise from 9.8 percent to 15 percent.

The U.S. economy affects the economy of the world and of world poverty. Some leading scholars like Larry Summers have been warning of secular stagnation, but this is secular stagnation with a twist, the highest increase in secular inflation.

Finally, we have consistently believed in the innovative spirit in the US and in its capacity to find effective solutions to the multiple transitions both in the US and the rest of the world.

Mr. Fanizza:

I would like to thank staff for what I believe is a truly outstanding report that clearly identifies and covers the many issues and provides clarity, granular and practical policy advice. Like Mr. Trabinski, I found it very interesting that in Ms. Shortino's buff statement, she stressed the importance of the support packages as supply packages rather than demand packages. That is the way in which it should be thought. That is very important.

We issued an extensive gray statement so I will try not to add much today. I will provide one additional comment and maybe a question on monetary policy. Let me say again that it is much appreciated, the coverage of the shift of the Federal Reserve to an average inflation targeting framework. I agree with staff's assessment of the expected benefit vis-a-vis the Paris framework at this critical juncture. The report rightly emphasized the role of inflation expectation and the time when monetary policy is expected to remain constrained by the effective lower bound.

The new framework in fact aims precisely at more firmly anchoring long-term inflation expectations at the 2 percent growth, which led me to mandate that it has remained elusive until recently, thereby supporting faster return of the economy to higher level of employment.

Now, the report says there are significant uncertainties of how inflation expectations have fallen in the US, but on the side, I am pretty much relieved that market expectations actually seem to suggest that expectations remain anchored to a level consistent with the Federal Reserve's long-term target. Clearly, expectation based on a survey could be different, but that is an issue that is difficult to reconcile, but I would tend to believe the market expectation. I believe the market.

Nearly everybody stressed the importance of clear communications, and I agree. It is essential. But it may be naive if I look at the inflation in the recent weeks were significant, I should say, inflation surprise was comparing by a decline of long-term rates. I would say the Fed is doing a fantastic job in communication. It will be interesting if staff could elaborate on that if staff believes there are other reasons why interest rates have reacted to the inflation surprise the way it did in the last two weeks.

Mr. Chodos:

We issued a gray statement. We highlighted the points we think were more critical but wanted to make a couple of emphasis assessments. One is that the US has embarked, the new Administration, into bold policy action. I think the most important thing is when someone has that level of understanding of the challenge of its time, it prioritizes its priorities for its preferences eventually.

For instance, we might have a comfortable level of accommodative monetary policy. We might have risky levels of help in terms of helping out the economy. We might have a very ambitious Build Back a Better program. We might have an overly ambitious idea of going back to full employment. We might have a very determined position of reverting more than 30 years of increased inequality in the US, which has affected its own social fabric as well as world aggregate demand, but ultimately, the important thing is to take those bold actions, because without taking some risk, issues are not made. Again, I think that we should focus more on the risk of omission than in risk of action in challenging times.

We have to commend the US authorities for something, and all of this matters together, is for realizing that there are priorities and sometimes priorities have to trump preferences, and then we have to take the best that we have to take in order to have a better resilience and a better policy response. And it is working. The great news is that we can all realize that it is working. I think that having had or been having the success they have, they should be having the leeway to calibrate as much as possible the way that they get out of the monetary policy expansion, the way they get out of the fiscal stimulus, and the way of the focus of targeting on inequality. Of course, a critical element here may be the issue of the tax. Several speakers have highlighted the issue of the global tax agreement. This is critical because if we are going to solve the issue of that, it is going to come from the income side. Again, this is priority over preference.

The Chair:

Mr. Chodos brought up something that came through in many interventions, and it is the opportunity cost of inaction. Of course, that does not mean that we should be negligent to the risks affiliated with action. Many of the questions that were addressed to staff were around how we are going to monitor those risks.

The staff representative of the Western Hemisphere Department (Mr. Chalk):

Let me try to answer questions, and I think Ms. Weber will answer a few as well.

On Mr. Bhalla's point on is this secular stagnation. I think this is a bit of a difference of view in terms of the level versus the growth rate. What we see is that up front, the economy is going to accelerate well above the potential on the supply side for the next few years, and then they will gradually converge back down to potential from above.

In growth rate terms, it looks like they are growing slowly, but on level terms, actually they will be doing very well, and they will remain well above where we were projecting pre-pandemic until after the ten-year forecast window. So that means per capita income will be higher, living standards will be higher. Yes, growth will slow towards potential, but I think in the end, we should judge welfare by the level more than the growth rate. Because they are far above potential that does create its own price pressures that policymakers will have to try to balance.

On the implications of a global tax, I think it is difficult to make that assessment for a few reasons. One is we do not have information on the tax accounts of the large multinational corporations. Those are typically confidential. We can back some out from public data, but we do not have the details of which kinds of deductions, tax benefits, tax expenditures they can take advantage of.

We do believe there is significant room to increase the tax take from U.S. corporations. The corporate tax rate now is 21 percent, but the average effective tax rate on U.S. corporations is closer to 8 percent. So, there is a huge gap between the effective rate and the statutory rate.

If we look at the tax accounts over the last several years, in any given year, around one-third of U.S. multinationals do not pay any tax even though we know they are very profitable. So, their financial accounts show them to be profitable, but their tax accounts show them not paying any tax. I think a lot of it is this profit shifting to low-tax jurisdictions, taking advantage of very generous provisions in expensing of new capital, and various other things, including the debt bias in the tax system. I think those all help with reducing corporations' tax liabilities.

We know that under the proposed tax changes corporations will pay more. We think that particularly companies that are reliant on intellectual property and intangible investments will pay significantly more because those are the types of investments that are very mobile and able to take advantage of profit shifting. However, we will have to see how it all shakes out. Of course, the corporates themselves will be endogenizing their behavior based on the new tax system, so it will be quite complex.

On Mr. Fanizza's questions on inflation and interest rates, I think we are equally puzzled as he is. We expect high inflation and inflation outcomes have been broadly in line with where our forecasts were. But in June, inflation was higher than where the market was pricing it to be and rates went down. It is always hard to predict what the U.S.-fixed income markets will do. But I think, as Mr. Fanizza says, part of it is a product of the credibility of the Fed. The Fed's actions and communications, particularly over the last six weeks, have killed this reflation trade that was taking place. As Mr. Fanizza says, this is an effective use of their communication tools, and we hope that will continue to strongly anchor inflation at the Fed's longer-run goal.

Mr. Poso had some questions on what we mean by shift in monetary policy in the coming months. Under our baseline forecast, we would expect that they would have to start tapering asset purchases at the beginning of next year. If that is true, and there are lots of uncertainties, and this decision should be data dependent, how do we expect to see that shift in policy in the coming months?

The first step we would have thought would be needed was for the Fed to create some optionality to move faster if they needed to move faster. This involves shifting away from an approach where the Fed was committing to maintain support for as long as it takes towards something that is a bit more nuanced. I think that is what we saw in June, and that is what we heard from Chairman Powell when we met during the Article IV. Their idea was to say that they would start talking about asset purchases and discussing that in the Committee. And the market is now viewing every rate, every Federal Open Market Committee (FOMC) meeting from now on as a "live" meeting where potentially they could signal that they are going to change their future approach on asset purchases.

The next step in creating that optionality in the coming months is to change the forward guidance on asset purchases. They framed their asset purchases as making "substantial progress" towards their goals. We are going to hear more about how much the economy has gone toward making that

“substantial progress”. It should be the next change of monetary policy in terms of forward guidance. Eventually, by early next year, we anticipate that they will start to reduce purchases. But obviously it is all very uncertain. They will have to figure it out with the data that is coming in.

A couple of questions came in Mr. Hosseini’s gray statement over the weekend that we did not have a chance to respond to in writing. One was on student debt. Student debt is a big problem in the US. There is about US\$ 1.6 trillion in student debt outstanding. We do not see it as a financial stability problem so much. It is not like the subprime mortgage problem. This is because a lot of this debt is essentially underwritten by the government. Also, unlike subprime mortgages, it is full recourse debt and people cannot walk away from it. They will have to pay it over their lifetimes. In a sense, it is less of a financial stability, but it is more of a macro problem and potentially, it is also a fiscal problem since the debt is a contingent liability to the government. Certainly, we already see it as a macro problem. It is slowing down household formation. It is weighing against consumption patterns of young people. It is having behavioral effects even now because of the debt burden.

Finally, there was one question from Mr. Hosseini on staff’s assessment of the progress on the FSAP. We tried to summarize this in paragraph 53. Essentially it was very hard with a new Administration in office for just a few months to really go into a comprehensive assessment of the FSAP recommendations. There has not been very much progress on the FSAP recommendations, but we anticipate that next year, since there is a lot of things in train, and so next year will be a more appropriate time for us to do a more detailed assessment of how things have gone on the FSAP.

Mr. Jin:

We would like to join other Directors to welcome the authorities’ measures to promote vaccine rollout in the US. I would like to emphasize a few points in my intervention.

First, with inflation rising sharply over the past few months, especially worries on risk are much more lasting and significant inflation is increasing. We can see many relevant debates in recent media reports. If the Fed has to tighten the monetary policy earlier and faster than expected, its impact on asset price, debt sustainability of the corporate sector and the rest of the world could be tremendous. We encourage staff to make more analysis on possible scenarios.

Second, we strongly support staff's view that tariff and non-tariff barriers should be rolled back, and measures should be taken to facilitate rather than block the functioning of the rules-based multilateral trading system. We also share staff's concerns that currency-based countervailing duties pose significant risk and damage to the multilateral trade and international monetary systems and should be rolled back or avoided.

I encourage the authorities to take an open, constructive, and inclusive attitude in dealing with the rise and the convergence of large emerging economies, like my own country. Stick to the market-based and rules-based multilateralism. Stop demonizing its competitors with an end to cover its illegal antimarket trade and economic policies.

There is no doubt that the US is a great country, and I am a friend of American people. I believe that the US can become even greater and continue its economic greatness and appealing to the rest of the world by reforming and elevating itself, engaging in constructive and mutually beneficial competition, and learning from each other with its partners rather than trying to destruct and cripple its competitors.

Third, we welcome the U.S.'s efforts to enhance international cooperation on climate issues, including cooperation in the G-20. At the same time, it is contradictory to set a high standard for other countries to cut emissions while restricting trade of green technologies with the excuse of national security concern. We hope the position of the U.S. on the climate issue will be consistent in all aspects.

The staff representative from the Western Hemisphere Department (Ms. Weber):

There is one question that I would like to respond to, which is on healthcare and how to find a sustainable solution to the rising costs in the United States. This was a focus of this year's Article IV Consultation because healthcare spending accounts for about one-fifth of the economy, so clearly finding a solution there is macrocritical.

The solution will have to be in the form of a multi-pronged approach. There is not just one policy that can be the solution. One proposition that we make in the staff report is to increase the minimum age for Medicare eligibility, but I would like to highlight that we make this recommendation in combination with highlighting that it has to come alongside an expansion of Medicaid and tax credits to ensure that low-income elderly households continue to be covered by insurance.

But there are other policies that can be taken to reduce costs. One clearly is in the area of competition. We have done some analysis. We have found that about a quarter of the increasing costs over the last few decades can be explained by the rising market power in healthcare markets in the US. So clearly a more assertive approach by the antitrust authorities will be welcome, both at the federal and the state level.

We also found some evidence that supply is not as elastic as it could be, especially on the physician side. There are very strict licensing requirements in place in the US, so revisiting some of them could also be helpful to reduce barriers to entry.

Finally, there is a case to be made for more transparency in healthcare markets. Being more aware about some of the prices could help consumers shop for the lowest costs of hospitals and physicians. These recommendations are outlined in greater detail in one of the working papers that is accompanying the Article IV staff report.

Ms. Shortino:

I will make three very quick points. On trade, I just want to reiterate the Administration's trade policy, which does aim to ensure inclusive, equitable, and worker-centered growth. We are carrying out a comprehensive review of U.S. trade tariffs and other measures, but I also want to flag that in that context, the Administration just concluded framework agreements on large civil aircraft with the European Union and United Kingdom, which resulted in a suspension of existing tariffs, so progress is being made on this front.

On climate, I very much welcome the feedback from Directors, but I just want to reiterate that there are many ways to reach emission targets, and we need to be clear right about this.

Finally, on the financial sector, I would agree with staff's assessment that the housing market does have some potential vulnerabilities, but at the same time, it is characterized by lending to high creditworthy borrowers, which very much mitigates the risks. I would also just note that, while asset prices are high, banking system remains well capitalized and our FSAP is closely monitoring non-financial institutions, non-bank financial institutions.

The Chair:

I would just echo what was said about the importance of the US's role for key parameters for sustainable and resilient growth. Trade certainly is one of them, advancing in trade agreements, but also reforming the multilateral trade system is something we have to strive for.

On climate, I agree the stepped-up approach of the US is also important. As we know, staff of the IMF, and I would subscribe to the analysis done by staff, concludes pricing carbon is very important to accelerate action. We do recognize, though, that there has to be acceptance within national regulatory frameworks for the way we go forward and that tax, trade, and regulatory equivalency can all play a role. Most important is to move and to act.

Thanks to Ms. Shortino for the US rejoining the Paris Agreement. And, of course, last but not least, I want to concur with the attention brought today to non-banking financial institutions and that this will continue to be a focus of the U.S. authorities. Of course, the U.S.'s role in that area is very significant.

We had a productive discussion. It is always a pleasure to have the Board engaged but especially when it is on, relatively speaking, a positive posture, a combination of massive fiscal and monetary support and vaccinations leading the US towards record-high level of growth this year.

We did hear from many Directors concerns about some of the long-term structural factors like demography. And, of course, this will continue to engage us and to bring us together to discuss these issues.

The Chair noted that the United States is an Article VIII member, and no decision is proposed.

The Chair adjourned the discussion.

ANNEX

- Gray Statements
- European Central Bank Statement
- Staff Responses to Executive Directors' Technical Questions
- Constituency Codes

DOCUMENT OF INTERNATIONAL MONETARY FUND AND FOR OFFICIAL USE ONLY

BUFF/ED/21/93

July 13, 2021

**Statement by Ms. Shortino and Mr. Sturm on United States
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for their very constructive dialogue with our authorities. We generally concur with the analysis and policy recommendations in the report.

The United States has undertaken historic economic and health responses to the COVID-19 crisis, with the goal of moving the U.S. economy rapidly toward a stronger, greener, more sustainable, and more equitable recovery from the tragedy of the pandemic. A national vaccination effort continues with a focus on overcoming vaccine hesitancy, and the production and distribution of highly effective vaccines in the United States are supporting a broader reopening of the economy. Given the downside risks from the path of the pandemic, public health efforts remain focused on vaccinating as much of the population as quickly as possible, while also providing vaccines and other medical support to other countries. To date, almost 58 percent of adults are fully vaccinated.

The Administration expects growth to be largely in line with the IMF forecast of around 7 percent in 2021 and just under 5 percent in 2022. Fiscal policy continues to provide substantial support to underpin strong aggregate demand, including targeted support to those that need it most: the American Recovery Plan is helping households and businesses bridge the gap to a full recovery. Because of this support, the United States is less likely to suffer the kind of long-lasting impairment that we saw after the global financial crisis, when foreclosures and bankruptcies weighed upon the economy for years. The unemployment rate has fallen and demand for labor is at a record-high, but the labor market will take some time to recover to pre-COVID levels. However, continued progress on vaccinations, reintroduction of childcare, and school re-openings will all contribute to easing of labor supply tightness.

The Administration has prioritized plans that aim to: build infrastructure to modernize the U.S. economy, support families, fight climate change, and address the long-standing impediments and inequities that limit opportunities for social mobility and make everyday life more challenging for many Americans. Ending the pandemic provides the opportunity to “Build Back Better” with better infrastructure, more support for families, and a foundation for a greener future. The American Jobs Plan and the American Families Plan are not spending programs aimed at stimulus – rather they are public investments to modernize the economy, prepare our businesses and workers to be more productive at home and

competitive internationally, and build support and increase security for children and families. Crucially, these plans make important investments in our fight against climate change and address rising inequality.

Fiscal Policy: COVID-19 Recovery, Infrastructure, Jobs and Families

The United States responded to the effects of the COVID-19 pandemic with an unprecedented level of fiscal assistance. The American Recovery Plan has helped low-and middle-income households reach the end of the pandemic with their finances intact and helps position businesses to reopen. Targeted programs are reducing foreclosures and bankruptcies, minimizing the prospect that the housing sector will again weigh upon the economic recovery like it did after the great recession. The Administration made great efforts to target the plan's benefits to lower-middle income families, including the child tax credit, block grants to state-and-local governments, eldercare, and subsidies for childcare.

The Administration's tax plan is designed to better reward labor and strike a balance between raising revenues and incentivizing job creation and investment. The Administration is proposing to return the corporate tax rate to its historical level as part of a comprehensive plan to boost productivity. We agree with staff that a global minimum tax will be a crucial step forward in countering the incentives for profit shifting and base erosion and strongly support the recent OECD Inclusive Framework agreement on this front. International reforms, alongside domestic changes aimed at raising revenue-to-GDP, promoting investment, and reversing a trend of lower corporate tax receipts, will support a more sustainable U.S. tax system and will enhance the profitability and global competitiveness of U.S. businesses.

The Administration is working closely with Congress to finalize the American Jobs Plans and the American Families Plan. Last month the Administration announced a bipartisan infrastructure plan with Congressional leaders, which alone would be the largest such investment in nearly a century. As staff note, these plans will support transformational change in the U.S. economy. Planned infrastructure will include physical infrastructure as well as twenty-first century investments to improve education and health and expand the labor force, especially for women.

Monetary Policy

Since the beginning of the pandemic, the Federal Open Market Committee (FOMC) has deployed all its tools to support the U.S. economy, thereby promoting its maximum employment and price stability goals. As described in the staff report, in August 2020, the FOMC announced a new monetary policy framework, which introduced a modified description of maximum employment and the FOMC's new approach of Flexible Average Inflation Targeting. The FOMC maintained key aspects from its 2012 strategy statement, including striving for maximum employment; a 2 percent longer-run inflation goal; and the importance of taking account of risk to the economic outlook. The FOMC expects to maintain an accommodative stance of monetary policy until the outcomes under its policy framework are achieved.

The FOMC has repeatedly emphasized that the path of monetary policy will be outcome dependent and that it will take into account a wide range of information, including readings

on public health, labor market conditions, inflation pressures and inflation expectations, and financial and international developments. At present, inflation has risen, but it is widely recognized that recent inflation readings largely reflect transitory factors and base effects, including idiosyncratic supply and demand factors. Market- and survey-based measures of inflation expectations suggest the Fed's Flexible Average Inflation Targeting regime is working, and expectations are anchored around the 2 percent average inflation target.

The FOMC announced in June that it would maintain the target range for the federal funds rate at 0 percent to 0.25 percent. Consistent with its strategic framework, the FOMC repeated that it will not raise the federal funds rate target range "until labor market conditions have reached levels consistent with the Committee's assessments of maximum employment and inflation has risen to 2 percent and is on track to moderately exceed 2 percent for some time." Employment remains well below estimates of its maximum level. The FOMC continues to highlight the importance of having longer-term inflation expectations well anchored at 2 percent.

Our authorities are keenly aware of markets' interest in the future trajectory of U.S. monetary policy. The FOMC is also closely monitoring global economic and financial developments and their implications for domestic economic activity, labor markets, and inflation. Staff rightly note that the FOMC is committed to continue to provide forward guidance and to communicate well in advance to help ensure that the eventual withdrawal of monetary accommodation is orderly, methodical, and transparent.

Financial Stability

The U.S. financial system has benefitted from past reforms, including those under the Dodd-Frank Act, that boosted capital and improved resilience to shocks. This resiliency was particularly evident in the early stages of the pandemic. Due to decisive measures by the U.S. authorities, many of the worst fears of widespread bankruptcies and financial instability did not materialize. Banks are well-capitalized and sufficiently liquid, with the largest and most complex having recently completed required stress tests. The United States will continue to monitor closely banks' exposure to commercial real estate, along with other risks such as leverage in nonbanks.

The Administration has developed a robust agenda to enhance the stability of the U.S. financial system. It is working through the Financial Stability Oversight Council (FSOC) to take a well-coordinated approach to addressing financial stability risks. The FSOC is prioritizing a broad interagency effort to address vulnerabilities in the U.S. Treasury securities market. The FSOC is also working to enhance interagency data sharing and improve the FSOC's ability to identify risks related to hedge funds as part of its efforts to assess risks related to nonbank financial intermediation. In addition, U.S. authorities continue to work internationally and domestically to improve the resiliency of money market funds.

International Context

The U.S. economic recovery is significantly contributing to a global recovery, both through the direct provision of vaccines and positive economic spillovers. The United States is committed to supporting developing countries in their fight against the pandemic and reducing the risk of a divergent global recovery. To that end, the United States has pledged to share 580 million vaccine doses internationally, to be allocated to 92 lower-income nations selected by COVAX.

The pandemic and the ongoing uneven global recovery has had significant effects on the U.S. external position. The U.S. current account deficit is likely to widen in the near term as a result of the strong growth in United States relative to our major trading partners. Going forward, it will be important for the rest of the world to do its part in supporting global aggregate demand. In particular, countries with perennial current account surpluses need to step up efforts in support of domestic demand. As always, flexibility in exchange rates and avoidance of excess reserve accumulation will be critical to reducing global imbalances.

The Administration's trade policy aims to ensure inclusive, equitable, and worker-centered growth, while also securing the resilience of supply chains. These efforts will need to be paired with global trade reforms, including at the WTO, and a broad reduction in the large stock of high and unfair trade barriers and practices. Unfair trade practices and other uncompetitive practices by U.S. trading partners have undermined the public's faith in unfettered trade and the rules-based international order. To this end, the Administration is carrying out a comprehensive review of U.S. trade tariffs and other measures. The Administration has also recently concluded framework agreements on large civil aircraft with the EU and the UK, which resulted in the suspension of existing tariffs. U.S. policies relating to currency practices aim to put effective pressure on trading partners that are intervening in the foreign exchange market to gain an unfair competitive advantage.

Climate Change

We welcome the report's strong coverage of U.S. policies towards a greener economy, including incorporation of climate-friendly investments in the American Jobs Plans and the American Families Plan. The United States has returned to the Paris Agreement, and the Administration has announced bold plans to meet its newly-enhanced nationally-determined contribution to fight climate change. The Administration is actively rolling out investments and initiatives to transform the U.S. economy toward a greener recovery, including significant infrastructure investments, regulatory changes, and new standards. These efforts extend to the agriculture sector, where the Administration seeks to take advantage of alignment between climate-smart and climate-friendly practices and good productive agriculture and forestry practices. The United States, like many other countries, has put forward ambitious plans focused on carbon emissions. It is important to recognize the different paths countries will take to reduce emissions, whether it is through regulation, standards, subsidies, or that of carbon markets.

The Administration also recognizes that the financial system must be resilient to the risks from climate change, and the FSOC is making this a priority. FSOC members will coordinate

domestic regulatory efforts to assess climate-related risks to financial stability, pulling together agency perspectives to assess how climate risks may impact the stability of the entire financial system. Specifically, the FSOC will work with its members to improve climate-related financial disclosures and other sources of data to better measure potential exposures to climate-related risks. This will complement the work of the SEC, which is currently reviewing existing guidance on climate-related financial disclosures.

Inequality: a cross-cutting theme

We welcome the report's coverage of income and racial inequality in the United States. The Administration has put forward an initial, ambitious whole-of-government equity agenda that addresses the opportunities and structural challenges that the country faces. The American Rescue Plan's national vaccination program incorporated measures to address racial disparities in COVID-19 outcomes, while supporting American families bearing the brunt of the crisis, including families of color. The American Rescue Plan changed the course of the pandemic for many under-privileged members of the country.

Looking forward, the United States has developed a broad workplan to assess equity in federal agencies and more broadly, engage underserved communities, allocate federal resources to advance fairness and opportunity, and promote equitable delivery of government benefits and equitable opportunities. The Administration also aims to direct a sizable share of new and current resources, including infrastructure investments, to historically underserved communities. The American Jobs Plan and American Families Plan also have targeted programs designed to address inequality and provide a strong foundation for opportunity and inclusion.

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GRAY/21/2045

July 14, 2021

**Statement by Mr. Bevilaqua, Mr. Saraiva, and Mr. Barroso on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for the detailed and insightful report and Mrs. Shortino and Mr. Sturm for their informative statement. We broadly agree with staff's assessment on the outlook and risks and take note that fiscal and monetary policies are consistent with previous IMF policy advice, providing much needed support for the recovery. The ambitious policy program also attempts to lay the foundation for sustainable and inclusive growth and has generated consequential positive spillovers for the global economy. At the same time, while the U.S. continues to play a crucial role in supporting the global recovery, close monitoring of developments and underlying risks is warranted.

A robust recovery underpinned by strong and sustained policy support and a successful vaccination strategy is under way in the United States. With mobility increasing on par with immunization, economic activity in different sectors is safely resuming or surpassing pre-pandemic levels. The new administration's American Rescue Plan has much to its credit, as it doubled down on already large emergency support and funded a massive vaccination drive. The expectation of strong support for infrastructure (Jobs Plan) and labor force participation (Family Plan) has also contributed to the pickup in confidence levels. The accompanying tax package and the net growth effect should in principle mitigate the impact on indebtedness and ensure fiscal sustainability. Monetary policy embraced further accommodation as a built-in feature in its framework, adding complementary support. In a sense, policies have been so successful that overheating has become a meaningful tail risk. That said, the main downside risk in the outlook stems from the still lingering pandemic, with vaccination efforts running against new variants.

We welcome the ambitious public spending plans, combined with the associated fiscal responsibility features. As underscored by Ms. Shortino and Mr. Sturm, fiscal measures have been crucial to bolster the ongoing recovery, including with clear and positive global spillovers. On top of that, the proposed measures could prove instrumental to lift potential growth in the medium run. We welcome the renewed engagement with the international community to reach agreement on corporate tax coordination, constraining profit shifting and

base erosion, with important equity results. Progress in this area is a pre-requisite to implement a successful tax reform and secure at least partial funding for the planned discretionary spending. Indeed, the positive impact on growth and revenues of the envisaged policies translates into very low risks for fiscal sustainability. That said, the lack of domestic agreement on the fiscal package and the remaining coordination hurdles for the international implementation of corporate tax plans add uncertainty to the scenario.

We take note that staff assumes full implementation of all fiscal plans in its baseline scenario, and welcome staff's suggestions for improvement. There is no question that infrastructure investment and innovation (American Jobs Plan), and labor market participation and human capital (American Family Plan) are key to secure higher potential growth. Nevertheless, policies could conceivably be better targeted, with greater focus on lower income groups and more enduring support measures. The accompanying fiscal consolidation efforts could also be better focused or strengthened. We are not convinced by staff's proposal of a cashflow based corporate profit tax and wonder about possible hurdles. We agree with staff that further revenue mobilization measures could support the advance of other policy goals, including on the areas of climate policies and social inclusion.

The Federal Reserve new monetary policy framework complements unconventional policies and forward guidance, clearly adding steam to the recovery. The commitment to keep policy rates low for longer (as soon as policy rates hit the effective lower bound) is now a built-in feature of the policy framework. There is sufficient flexibility to allow timely reaction to labor market and financial stability developments – which is a desirable characteristic from a policy perspective, even if uncertainty is added to the future path of monetary policy. While some degree of overheating is an inherent feature of the new framework, there is a risk that it may start to unfold much sooner than expected. In that scenario, there would be less time to consolidate the productivity gains envisioned by fiscal policies, more spillbacks from weak trade partners, and higher financial stability risks stemming from increased debt levels.

We take note of the dialogue between staff and the authorities on alternatives for structural reforms in some segments. We agree with the authorities that the announced fiscal plans go a long way in advancing the new administration priorities, including on health, social inclusion, and climate policies. There is, of course, ample scope for a constructive dialogue. Two areas not covered in the Rescue, Jobs and Family plans but dully addressed by staff were the financial sector and international trade. On finance, we support staff's call for greater liquidity buffers for a range of non-bank market participants to minimize the need for extraordinary official support to liquidity in the future, and also take note of the authorities' ongoing review of the current framework in light of the stress experienced during the pandemic. On trade, we support staff's call to strengthen multilateral trade and the international monetary system and take positive note of the authorities' ongoing review of trade tariffs and restrictions, as well as the close engagement with the international community on these fronts.

With these remarks, we wish success to the U.S. authorities in their plans.

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GRAY/21/2054

July 15, 2021

**Statement by Mr. Chodos, Mr. Herrera, and Mr. Hendrick on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for an insightful and comprehensive report, and Ms. Shortino and Mr. Sturm for their informative Buff statement. We broadly agree with the staff's assessment and policy recommendations. This is a very important Article IV consultation, which takes place at the start of a new administration, and in the midst of the COVID-19 crisis that has had a profound impact on the United States and the rest of the world. We are encouraged by the bold and frontal approach undertaken by the new administration, which promises to be very supportive for the U.S. economy with positive spillovers for the global economy.

- 1. We congratulate the U.S. authorities for their effective vaccine rollout which is helping to put the U.S. economy back on a strong footing.** The speed of vaccination attained by the administration in its few first months in office is impressive. This outcome, together with a substantial fiscal impulse, has been instrumental in the broader reopening of the economy and a gradual but sustained recovery in employment. Real GDP is expected to rebound to 7 percent in 2021, with a positive output gap of 1.1 percent, and 4.8 percent inflation, which is expected to be short-lived. This progress could be undermined due to the surge of new COVID-19 variants and the dramatic reduction in vaccination rates in the last few weeks. We encourage the authorities to redouble their efforts to overcome vaccine hesitancy, which we see as the main risk to the outlook. Reaching the administration's goal of achieving "herd immunity" will be critical to consolidate economic recovery.
- 2. We welcome the new administration's bold fiscal policies aimed at economic recovery and to address long-standing issues that have long held back the U.S. economy.** Taking the opportunity provided by the pandemic to "Build Back Better" through the infrastructure program, the American Jobs Plans, and the American Family Plan promise to be a turning point, not only to modernize the economy and fight climate change, but also to address the long-standing impediments and inequities that limit opportunities for social mobility, income inequality, poverty reduction, and a more egalitarian society. We take note that staff's baseline scenario and analysis are predicated upon the assumption that Congress will approve these initiatives without a substantial reduction in the envisaged size of those programs.

3. **The proposed tax policy changes to finance the needed additional fiscal expenditure builds on an equitable burden sharing for society and is a growth-friendly approach.** Targeting high-income households and returning corporate tax to its historical level strikes a right balance between raising revenues and incentivizing job creation and investment. We take positive note that many of the proposed revenue provisions reflect previous IMF policy advice. The authorities' support at the international level for a global minimum corporate tax will be a critical component of a successful strategy to avoid the "race to the bottom" by global corporations. Box 1 explains very clearly the importance of reaching an agreement to level the playing field internationally. We take note of staff's concern in paragraph 14 about the authorities' decision not to raise taxes on households earning under US\$ 400,000. *However, from a political economy point of view, this could be a pragmatic policy decision to gather a broad support, considering that 98 percent of households in the U.S. would be below that threshold. Wouldn't that be more efficient than the alternatives explained here, in terms of achieving the overall outcome? Staff's comments would be appreciated.*

4. **We commend the highly effective actions taken by the Federal Reserve during the COVID-19 crisis to provide stability to the markets and support economic recovery.** The change in the monetary policy framework (the new Flexible Average Inflation Targeting approach) introduced by the FOMC in August 2020, amid the uncertainties related to the pandemic, was a bold move. This policy action was also in line with previous IMF advice. However, as recognized by staff in paragraph 30 and shown in Box 4, there are non-trivial risks, including a slower rebound in labor force participation or a higher-than-expected impact of the unprecedented size of the planned fiscal support, which could press the Fed to withdraw monetary support under a potential tight timeline, and it may lead to a faster-than-expected tightening of financial conditions, with all the associated negative spillovers to the global economy. The Risk Assessment Matrix in Appendix I clearly indicates that a de-anchoring of inflation expectations in the U.S. has a medium likelihood with a high expected impact if risks materialize. The corresponding staff's policy advice is a reduction in asset purchases and possible rise of the policy rate before net purchases have been brought to zero. We believe that the scenario of a rapid pick-up in inflation that could be systemic for both the U.S. and the global economy could have a likelihood higher than a "tail event". *Staff's comments would be appreciated.*

5. **The external current account deficit in 2020 has increased and it continues to be explained largely by the fiscal imbalance.** We take note of the assessment, as explained in Appendix II, that the external position was moderately weaker than the level implied by medium-term fundamentals and desirable policies. At the same time, we agree with staff that in the near term, given the unprecedented social and economic fallout from the pandemic, front-loaded fiscal support is needed to ease the burden on households and corporations. In the medium term, fiscal consolidation and putting the public debt-to-GDP ratio on a sustainable path will be needed. However, as discussed in the 2021 External Sector Report, this will need to be accompanied by actions taken in excess surplus economies with fiscal space to achieve a global rebalancing.

6. **We welcome the findings that the financial system remains well-capitalized and sufficiently liquid.** The resilience of the banking system was successfully tested during the pandemic, but in March 2020 a shortcoming in the critical Treasury market was revealed. Despite the fact that it has long been the deepest and most liquid fixed income market in the world, the market was unable to absorb the significant shift of assets from prime and tax-exempt fund to money market funds backed by Treasury securities. The Fed had to absorb US\$ 2 trillion in securities to restore

market functioning. We welcome the FSOC's call for an interagency effort to address these vulnerabilities in the U.S. Treasury securities market. We encourage the authorities to explore staff's recommendations, including the creation of a central clearing of Treasury market transactions and the introduction of a standing repo facility. On the recent FSAP recommendations, we take note of the partial progress, as described in Appendix 4, and encourage the regulatory authorities to press forward with the implementation of critical recommendations.

7. **IMF research has shown the macroeconomic importance of reducing poverty and inequality in member countries, including in the U.S., the richest country in the world.** The simple fact that over the past 30 years the median household net worth has fallen in real terms for the bottom 40 percent of the income distribution, while the median net worth of the top decile of the income distribution has more than doubled is very telling. We are hopeful that the new administration's ambitious plans will be effective in their pursuit of a more equitable society. Staff has made a compelling case since the previous Article IV consultation on the pressing need for poverty reduction and better access to education, health, and job opportunities for a large segment of the poor population. The pandemic further increased wealth inequality, disproportionately affected minorities and women, and underscored long-standing racial disparities in economic and social outcomes in the U.S.

With these comments, we wish the United States and its people every success during these difficult times.

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GRAY/21/2056

July 15, 2021

**Statement by Mr. von Kleist and Mr. Sattler on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for an informative and well-written report. We also thank Ms. Shortino and Mr. Sturm for the additional insights provided in their helpful Buff statement.

We broadly concur with the thrust of the assessment. The United States are in the midst of a strong economic rebound from the 2020 crisis. The rebound is supported by a very effective start of the vaccination campaign, extraordinary fiscal support measures and the widespread lifting of lockdown measures in many states. Real GDP growth is projected to reach 7 percent in 2021 and the labor market is picking up. While broad monetary and strong fiscal support, such as the USD 1.85 trillion American Rescue Plan, have been highly effective in supporting the current rebound, considerable challenges persist. The authorities are facing multiple transformational processes such as post-pandemic behavioral changes, the shift towards a green and more digital economy, as well as demographic developments that may all – next to their influences on growth, productivity and the prospects of achieving climate goals – also exacerbate pre-existing inequalities. We therefore welcome the new administration’s decisive action in the field of social security, taxation, and climate policy as well as the proposed American Families Plan and Jobs Plan, while noting that further structural and well-targeted measures on these various fronts are needed going forward.

Regarding the risks to the economic outlook, we would come to a slightly more cautious assessment than staff. While overall vaccinations and the proposed additional fiscal stimulus give reason for optimism, a stagnating number of COVID-19 cases – albeit on a low level – as well as an unevenly progressing vaccination campaign and the surge of COVID-19 variants still leave room for possible (local) resurgences of the pandemic later this year. In addition, we would assign more weight to the risk that the proposed fiscal packages might not pass Congress in the envisaged configuration, given the likely necessity for political compromise. Underlying inflation pressures may also turn out to be even stronger than the most recently reported, and thus the need for a withdrawal of monetary accommodation may materialize sooner and less gradual than currently expected. Furthermore, there is high uncertainty surrounding the unwinding of the private sector’s excess savings. During the crisis, the private sector not only accumulated savings, but also paid back loans. We also note in this regard that inventory replenishment is currently constrained by substantial delivery bottlenecks.

On fiscal policy, we welcome that the new administration is continuing to respond forcefully to the pandemic shock but agree with staff that a more targeted approach would have been beneficial. While rightly balancing out the pandemic burden for the most vulnerable, some of the measures in the American Rescue Plan could have been more focused specifically on the most vulnerable groups. In this regard, we also share staff's concern that some current proposals might not always address underlying structural issues but rather serve the (short-term) improvement of household, corporate, and subnational governments' balance sheets. The proposed raise of the minimum wage to USD 15 per hour seems reasonable given that productivity growth has been much faster than adjustments to the minimum wage. *Could staff comment on the impact of this raise on the two most pressing issues in the US labor market, i.e. the very large share of long-term unemployed and the strongly over-proportional unemployment share among the young and the African-American community?* In our view, increasing infrastructure investment, as in the recently agreed-upon infrastructure bill and in the original Jobs Plan, also carries considerable potential to counteract economic inequality. We welcome the authorities' tax plans which aim at increasing government revenues to return to more balanced budgets and at closing loopholes in taxation, both domestically and internationally, which should lead to a more equitably spread of the tax burden. On the fiscal impulse, we take note of staff's concern about inter alia a potential overheating of the economy, with resulting further inflationary pressures, and their assessment of a fiscal policy gap of -1.8 percent of GDP in the EBA context. *Against this backdrop, could staff please elaborate on how they assess the precise calibration of the planned additional fiscal support and on the balance of the related risks (in terms of both likelihood and impact)?*

We thus see much merit in the timely development of a credible fiscal plan to decisively reduce the level of national debt over the medium term. While debt remains sustainable and debt servicing costs currently are low, rising health care costs and thus likely additional fiscal strains will emerge as the US society ages and baby boomers retire. On possible ways of tackling rising health care costs, we are more skeptical than staff that increasing health care users' contributions could be a sustainable solution, including for public budgets. Staff rightly notes that access to healthcare is, despite most welcome reforms a few years ago, still "highly unequal" and provided at "variable quality" in the US. In our view, achieving a more lasting and sustainable change would require substantial modifications of the regulatory framework, including efforts to promote more competition in the health market and to reduce inefficiencies in the system.

The continued accommodative monetary policy stance appears appropriate for now, given that the FED assesses the recent rise in the inflation rate as transitory and also considers indications of persistent slack in the labor market. However, we noted with interest the more recent discussion on adjusting the FED's asset purchase program within the FOMC. *Could staff kindly provide its assessment on how to best balance the current policy stance with this discussion and recent inflation numbers, against the backdrop of the global rise of the COVID-19 delta variant?* On the new monetary policy framework, we see merit in providing more flexibility in the FED's mandate, in particular to steer the economy away from the effective zero lower bound. Beyond that, we would be somewhat more cautious: In our view, there is a risk that allowing the inflation rate to overshoot for longer might be misunderstood as a manifestation of fiscal dominance, which would make the task of firmly anchoring inflation expectations again more difficult. Given that the benefits of the new framework crucially hinge on economic agents' anticipation of rising prices after a long period of low inflation, conveying the intricacies of the concept to the wider public might also constitute a major

stumbling block in its functioning. On a different note and as noted by staff, careful communication of changes to the monetary policy stance will be particularly important at the current juncture, and we welcome the FED's commitments in this regard.

We concur with staff that while financial stability has been preserved in 2020, the pandemic has also revealed considerable structural shortcomings in the US Treasury and money markets. We support the authorities' proposed institutional and regulatory changes in this respect. On risks emanating from rising corporate and nonbank financials' leverage, we note that caution seems currently more pronounced on the side of US regulatory authorities than among private sector market participants. With regard to nonbank financials, we were also somewhat surprised by staff's proposal to increase buffers in banks as a second-best substitute for nonbank financial regulation. It appears that such a proposal can at most be a short-term remedy until suitable regulation has been approved. Over the longer-term, it may increase incentives to shift business to the nonbank financial sector and could hence be even risk-intensifying.

On climate policy, we welcome the authorities' commitment to reducing greenhouse gas emissions by at least 50 percent until 2030 (relative to 2005 levels) as well as strengthening measures to mitigate climate change. Rejoining the Paris Accord is an important step not only for accelerating the reduction of greenhouse gases domestically, but also to reinforce and help accelerate international efforts. We agree with staff that to this end shifting subsidies from fossil fuels to green technology would best be accompanied by effective carbon pricing. A carbon tax may be one solution that could also generate a substantial amount of government revenues and thus provide funds to balance exacerbating effects on inequality during the green transition. We also support staff's proposal to focus more on greenhouse gas reductions in the agricultural sector, given its substantial contribution to total US CO₂-emissions. On a side note, we commend staff on their thorough, yet focused climate-change related section in the report and look forward to equivalent analyses in forthcoming Article-IV reports on the other large greenhouse gas emitters, in line with the approach outlined in the Comprehensive Surveillance Review (CSR) and the current climate strategy staff paper.

Finally, we join staff in welcoming the authorities' renewed international engagement and commitments, and invite the authorities to join further active collaboration in multilateral institutions such as the WHO and the WTO. In this context, like staff, we encourage the authorities to reconsider remaining trade restrictions which were introduced in recent years, noting that they seem to harm the US economy both domestically and globally. At the same time, we see an important role for domestic labor market policy to promote relocation and retraining of workers when production patterns change and supply chains move internationally. In this context, we would also caution against conflating trade and monetary policy issues, i.e. discussions on exchange rate (under-)valuation. We agree with staff that such issues should be kept apart as much as possible and would best be dealt with collaboratively in their designated multilateral fora.

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July 15, 2021

**Statement by Mr. Mouminah, Mr. Alhomaly, and Mr. Keshava on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for the insightful report and Ms. Shortino and Mr. Sturm for their informative Buff statement. We broadly concur with staff's analysis and policy recommendations and would like to offer the following comments:

We welcome the remarkable recovery of the U.S. economy with growth in 2021 expected to be around 7 percent and the economy rapidly moving back to full employment against the backdrop of unprecedented policy support. This is a testimony to the longstanding flexibility of the U.S. economy to adapt to shifts in economic environment. The favorable economic developments are also generating positive spillovers to the world economy. In this context, we agree that the extraordinary work over the past year to develop vaccines and the effective rollout of vaccination programs have been key in helping reopen the economy. At the same time, the spread of the Delta variant in parts of the U.S. with low vaccination rate is worrisome and the challenge is how to address vaccine hesitancy among a section of the population. Here, we take positive note of the ongoing effort to cover the unvaccinated people and hope that these efforts will yield the desired results soon. We also appreciate the authorities' continued commitment to multilateralism, including their pledge to share 580 million vaccine doses internationally with 92 lower-income nations through COVAX as noted in the Buff statement.

Following the unprecedented fiscal stimulus in the wake of the pandemic, we agree that the proposed fiscal packages are transformational in nature to help address the shortcomings in physical infrastructure and in the social assistance system. Indeed, given the disproportionate impact of the pandemic at the lower end of income distribution and the longstanding inequality, it is important to focus efforts, including towards strengthening the social safety net, reducing poverty, and expanding access to education, healthcare, and affordable childcare. To pay for the packages with tax increases and other sources of revenue, we take note of the ongoing efforts to build political consensus. Over the medium term, we agree with staff that determined efforts will be needed to bring down the

public debt ratio both by raising revenues as well as moderating future spending. However, we do not see any traction for the staff's recommendation on carbon tax and higher taxation of fuels. If the main goal is to reduce greenhouse gas emissions, there are many other policy options, including regulation, standards, or subsidies, as rightly underlined in the Buff statement. On the international corporate tax system, we appreciate the leadership of the United States in advancing discussions to help reverse the "race to the bottom" in corporate taxes and bring stability to the global tax system.

The Federal Reserve's effective actions in the wake of the crisis and its new policy framework have provided support for a more rapid recovery. In particular, we echo staff's comments that the combination of the new monetary policy framework and the economic boost from large fiscal stimulus/investments should be self-reinforcing. At the same time, we note that although an overheating of the U.S. economy that causes a surge in underlying inflation is not a likely outcome, it does represent an important risk. Indeed, if the recent pickup in inflation does not prove to be transitory, we note in the Risk Assessment Matrix that these developments would necessitate accelerating the reduction in asset purchases and even lead to raising policy rates before net purchases have been brought to zero, which will have important spillovers especially in EMEs. In this context, we welcome the commitment of the Federal Reserve to continue to clearly communicate its intentions and indicate at an early stage any prospective shift in asset purchases or policy rates.

Finally, on trade, we support stronger global efforts to promote international trade and investments and look forward to progress towards strengthening the multilateral trading system. On currency-based countervailing duties, we take note in the Buff statement that "U.S. policies relating to currency practices aim to put effective pressure on trading partners that are intervening in the foreign exchange market to gain an unfair competitive advantage". *In this context, we were wondering whether the IMF's external sector assessment is used as an input for a Section 301 investigation.*

With these remarks, we wish the U.S. authorities continued success.

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GRAY/21/2064

July 15, 2021

**Statement by Ms. Lim and Mr. Ong on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for the well-written report and Ms. Shortino and Mr. Sturm for the informative buff statement. We broadly agree with the thrust of staff's appraisal and would limit ourselves to the following comments.

The US authorities' decisive policy responses, including on the fiscal, monetary and vaccination fronts, have placed the economy on a strong recovery path. That said, the pandemic has taken a heavy toll on the nation, with an elevated fatality rate and a sharp drop in average life expectancy. Policy responses have also not been costless, and in some respects exacerbated long-standing trends including high public debt, current account deficit and corporate leverage. The current administration's ambitious policy proposals to address some of these structural challenges, which broadly align with past IMF policy advice, is welcome. Staff also presented multiple recommendations for better targeting of policies to strengthen macroeconomic and distributional outcomes and support a sustainable uplift in living standards for all Americans. We urge authorities to consider the recommendations carefully also considering the strong positive outward spillovers of a healthy and stable US economy on the global economy.

On monetary policy, the Federal Reserve's policy response has been very effective both during the depths of the crisis and in supporting the recent recovery. We commend the Federal Reserve for the bold decision to introduce the new monetary framework, which is consistent with past IMF advice, in the midst of the COVID-related uncertainty. The new framework has been timely, enabling the Federal Reserve to appropriately provide more accommodation over a longer horizon in response to a negative shock. We echo staff's call for the Federal Reserve to sensitively manage any future withdrawal of monetary accommodation, with due consideration for spillover effects on global financial conditions especially given highly divergent recoveries out of the pandemic globally. The authorities' stated commitment to be cognizant of spillover effects and clear communication is very welcomed. We also appreciate staff' analysis on the topic of inflation, including the well-nuanced policy advice on how monetary policy should adapt differently, depending on whether upside risks to inflation materializes owing to (a) relative price adjustments and/or front-loaded impact of fiscal stimulus or (b) persistent supply-demand mismatches and an associated de-anchoring of inflation

expectations. *Staff highlighted that “there is significant uncertainty about how inflation expectations are formed in the US”. Staff’s further comments on this topic is welcomed.*

On the fiscal front, we echo staff’s commendation for the size and ambition of authorities’ fiscal response to the crisis, which have also generated substantial positive spillovers to the world economy. Staff identified multiple ways in which various policy measures under the American Rescue Plan, American Families Plan and American Jobs Plan could have been better targeted and/or calibrated to enhance their impact both on macroeconomic and distributional outcomes. Authorities’ responses to these calls appear to be fairly light. *Staff’s comments on whether there are specific structural, institutional impediments that inhibit better policy-targeting, and whether there are lessons to be learned for future crisis responses, is welcomed.* In addition, staff highlighted that plans to close tax loopholes, raise taxes on corporates and higher-income households will partially fund the intended increases in federal spending. Nevertheless, the feasibility of US’ domestic corporate tax increases hinges on progress in remaking the international corporate taxation system, a process fraught with difficulties whether in garnering domestic political consensus or overcoming international coordination hurdles. *Could staff comment on the downside risks to the US’ fiscal balance and public debt trajectories if the necessary reforms cannot be achieved?*

On structural issues, we welcome staff’s detailed assessment of, and commend authorities’ ambitions across, various aspects of the US’ “Building Back Better” agenda, spanning healthcare, greening the economy, trade policy and a more equitable society. We especially appreciate authorities’ emphasis, as conveyed in Ms Shortino and Mr Sturm’s buff statement, that these are not spending programs aimed at stimulus – rather they are public investments to modernize the economy, prepare US businesses and workers to be more productive at home and competitive internationally, and build support and increase security for children and families. We take particular note of staff’s coverage on healthcare cost developments in Box 6, identifying structural, market-power based issues that contribute to the exceptionally high levels of US healthcare spending. Left unchecked, these developments will have a substantial impact on fiscal spending especially given the aging population profile. Structural reforms on this front will have to be multi-pronged and accordingly, take a long time to implement and bear fruit. We urge authorities to proactively review these issues, which would have important implications for the country’s medium- to long-term fiscal sustainability even if the current assessment is for public debt to be sustainable.

Lastly on the financial sector, we welcome staff’s detailed assessment of financing stability risks emanating from systemically important US markets and institutions, elevated asset price valuations, rising corporate and non-bank leverage, house price inflation and developments in the Federal Reserve’s overnight reverse repo facility. In our view, this analysis is a good demonstration of a close integration of macrofinancial surveillance into Article IVs. We also welcome Ms. Shortino and Mr. Sturm’s emphasis on the Administration’s robust agenda to enhance financial stability, including the FSOC’s work to address vulnerabilities in the US Treasury securities market and risks arising from non-bank financial intermediation and money market funds. On the 2020 FSAP, we note that a range of recommendations have not been addressed, although this is in part understandable given authorities’ priority on crisis response. We urge authorities to proactively address the findings in due time.

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GRAY/21/2065

July 15, 2021

**Statement by Ms. Mannathoko and Mr. Ismail on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for the informative report and Ms. Shortino and Mr. Sturm for their insightful Buff statement.

After being severely hit by the pandemic crisis, the US economy has rebounded on the back of substantial fiscal and monetary support and effective vaccine rollout. As a result, infection rates declined and employment is recovering, with positive outward spillovers to the global economy. The substantial fiscal expansion has, however, elevated public debt and current account deficits. At the same time, the pandemic continues to pose downside risks to the economic outlook, amplifying inequalities in income distribution and access to quality healthcare and education. We broadly agree with the staff appraisal and provide the following comments for emphasis.

We commend the exceptionally effective vaccination drive in the US over the past six months, which has helped turn around the outlook and improve prospects for the people and economy of the US. We encourage ongoing efforts to counter misinformation and vaccine hesitancy with the goal of reaching herd immunity this year. We also urge the use of official mobile communications to alert the public to the high risks faced by unvaccinated persons as this awareness seems to be receding. We underscore the need to step up public health and education efforts to mitigate scarring and we encourage ongoing measures to address pandemic related risks both domestically and globally.

The authorities' sizable fiscal policy support has helped alleviate the impact of the pandemic on households and businesses. We welcome the American Rescue Plan, which has supported millions of families and lifted 5 million children out of poverty. The ambitious agenda to strengthen social and physical infrastructure envisaged under the Jobs and Families Plans is commendable. We commend the enhanced attention and support for vulnerable and poorer communities to reduce healthcare and education inequities, and poverty. That said, as recovery becomes more entrenched this year, we recommend phasing out blanket benefits

and shifting to a stronger focus on the most vulnerable communities. In this regard, better targeting of fiscal packages to those who are truly in need will support fiscal and debt sustainability, while improving distributional outcomes. Spending should also be prioritized towards programs with high impacts on productivity, labor force participation, and poverty reduction, while facilitating digital and green transformation, including in poorer communities.

We see merit in raising taxes on corporates and high-income households to curb rapid accumulation in public debt. In this vein, we positively note that the proposed changes to tax policy would enhance revenue mobilization and counter incentives for profit shifting and base erosion. The proposed changes would also contribute to reversing the race to the bottom in corporate taxes. We stress the need to ensure that the Internal Revenue Service is fully resourced to implement the proposed changes, including by upgrading systems, expanding audits, and strengthening tax administration. At the same time, further work on the global agreement on a minimum tax will be crucial to level the playing field in international taxation and safeguard revenues in developing regions. Relatedly, aligning the combined corporate and personal tax rates on capital income should help address potential negative effects such as debt bias and disincentives on capital formation, from the various tax provisions on equity-financed investments and anti-avoidance measures.

The new monetary policy framework has been supportive of the recovery while providing clarity on the path of monetary policy and improving distributional outcomes. It is appropriately calibrated to address disinflation risks amid the persistent decline in natural interest rates and asymmetries posed by the effective lower bound. In view of the uncertainties in implementing the new framework and the complexity of the US economy, we note the importance of ensuring that the size and duration of the envisaged inflation overshoot, is data driven, avoiding overly parameterizing the policy framework. We also emphasize that an adept communication strategy will be needed to ensure that the transition from monetary accommodation is effectively managed, this being important to mitigate risks stemming from market misinterpretations, price volatility, and unwarranted tightening of financial conditions. In this vein, we welcome the Federal Reserve's commitment to continued clear communication of its policy intentions and early telegraphing of prospective shifts in asset purchases or policy rates.

The financial sector remains resilient and sound, however, pockets of vulnerabilities emanating from accommodative financial conditions should be closely monitored. We note with concern the increase in pandemic -related fire sales, liquidity pressures and market volatility, amplifying pressures in both Treasury and money markets. While the Fed's swift liquidity injection and activation of a range of facilities helped dissipate these pressures, more actions will be needed to prevent the recurrence of market liquidity pressures, such as mandating central clearing of Treasury market transactions, introducing a standing repo facility, and institutionalizing a move towards a floating net asset value while enhancing fund liquidity and stress testing requirements. At the same time, risks stemming from the

increased exposure in non-bank financial institutions and rising house prices require vigilance.

Accelerating structural reforms to support the transition to a greener, digital, and more equitable economy should remain a priority. To this effect, we welcome the authorities' rejoining of the Paris Climate Accord as well as the creditable climate change agenda, which will facilitate the transition towards a low carbon economy and enhance resilience to climate change. We also encourage the authorities to roll back trade restrictions and tariff increases with a view to supporting US workers and creating more and better jobs in line with efforts to enhance productivity, labor supply, and competitiveness. We also encourage working constructively with trading partners to resolve macrostructural distortions affecting external positions. Stepping up efforts to strengthen the multilateral rules-based trade system and engagement at the World Trade Organization will be crucial to advance progress on resolving these trade disputes.

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GRAY/21/2066

July 15, 2021

**Statement by Mr. O'Brolchain and Mr. Weil on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

Thanks to staff for their excellent and well-balanced report and to Ms. Shortino and Mr. Sturm for their helpful gray in which they underscored that the United States has undertaken historic economic and health responses to the COVID-19 crisis, with the goal of moving the U.S. economy rapidly toward a stronger, greener, more sustainable, and more equitable recovery.

We support the staff appraisal that the U.S.' remarkable recovery has not been costless in terms of increased public debt, a deterioration in the current account balance, exacerbated financial sector vulnerabilities, and increased inequality. However, in just a few months the U.S. administration has put plans in place to tackle much of the fallout of the pandemic while also laying a foundation for a better future. We agree that the principal risk facing the U.S. economy remains the pandemic despite a historic health response from the authorities. Addressing vaccine hesitancy should be an overriding priority. Recognizing that the pandemic will not be over anywhere until it is over everywhere, we commend the U.S. for pledging to share 580 million vaccine doses internationally, to be allocated to 92 lower-income nations selected by COVAX.

The American Recovery Plan, American Families Plan, and bipartisan infrastructure plan represent an unprecedented fiscal response to an unprecedented crisis. These packages will bridge households to a full recovery, support the liquidity needs of businesses seeking to reopen, improve education and health, and boost female labor force participation. We agree with staff that elements of the fiscal response could be better targeted to the neediest households which would improve distributional outcomes and help stabilize debt-to-GDP earlier. On the revenue side, our Canadian authorities strongly commend the authorities for proposing a comprehensive and progressive set of tax proposals, including an increase in the statutory corporate rate, an increase in the top personal rate, a globally coordinated

corporate minimum tax, and a number of loophole closing measures to ensure that corporations and high income individuals pay their fair share. While we are supportive of staff's proposals to raise further revenue in a progressive way (e.g., federal sales tax, eliminating capital gains exemptions, and mortgage interest deductibility) we should also recognize the breadth of what has already been proposed in a very short time. Staff might spell out a longer-term tax policy agenda for the authorities' consideration; one that is sequenced in an incremental and pragmatic way. As the recovery takes hold, debt-to-GDP should be stabilized, in particular in view of significant and unavoidable healthcare costs looming on the horizon and a worsening current account balance. But the authorities rightly point out that real interest spending as a share of GDP is expected to remain well below historical levels which provides some flexibility as to the pace and timing of the eventual consolidation.

Upside risks to inflation may require monetary policy to adjust (too) quickly. Beyond the path of the pandemic, we see the path of inflation as the key risk to the U.S. and global outlook. Higher than expected inflation resulting from structural as opposed to transitory factors could de-anchor inflation expectations. The associated tapering of asset purchases and/or increase in rates could cause an abrupt tightening of financial conditions with damaging impacts on sovereign, corporate, and household balance sheets. While recognizing the caution to be applied to point in time data, the larger-than-expected June CPI increase has only exacerbated these concerns. The new Federal Reserve policy framework comes at an opportune moment in that it defers the timing of policy normalization by hardwiring an overshoot of the 2 percent longer-run inflation goal. Nonetheless, we agree with staff that the Federal Reserve has a tricky task ahead as the recovery and associated fiscal support necessitate a shift in monetary policy. Clear communication about future policy intentions will be key to managing inflation expectations during the recovery.

The pandemic exposed or exacerbated certain financial system vulnerabilities. Given rising nonbank leverage and shortcomings in the functioning of key U.S. markets, we were reassured by the authorities' strong concern over hedge fund leverage as a potential source of systemic risk as well as their commitment to ensuring that key asset and funding markets remain robust under stress. Staff's recommendations for avoiding another episode of U.S. Treasury market illiquidity seem appropriate, in particular the move to a central clearing of all Treasury transactions and the introduction of a standing repo facility. We strongly welcome the authorities' efforts to improve the financial system's resilience to climate risks including through climate-related financial disclosures and by measuring the system's exposure to related risks. We took note of staff's finding that a range of FSAP recommendations have not yet been addressed but see the study of lessons learned from the pandemic as the top priority. *Which FSAP recommendations would respond most directly to the vulnerabilities exposed by the pandemic?*

We welcome the authorities' plans to curb carbon emissions through comprehensive adaptation measures. These include the ambitious and welcome objective of making the power sector carbon neutral by 2035. While recognizing the different paths countries will inevitably take to reduce emissions, we took note of staff's view that it will be costly to achieve the administration's climate objectives without a greater focus on carbon pricing. *What would be the price per ton of GHG emissions required to reach the net zero emissions target by 2050?* Staff's assessment of the authorities' climate plans, and alternative approaches, was comprehensive but we missed the bottom-line assessment of whether the authorities' current/announced policies will ultimately be sufficient to meet their Paris climate commitments. *Staff comments are welcome.* This Article IV consultation is a good example of the integration of climate issues in bilateral surveillance.

The authorities are making equity a key pillar of their agenda including through increased progressivity in the tax system and by deploying programs and investments in underserved and marginalized communities. This is a welcome policy focus, in particular given longstanding wealth inequality which was only exacerbated by the pandemic's disproportionate impacts on lower income and lower skilled workers. Women in particular were forced to drop out of the labor force to assume childcare responsibilities during the pandemic, which underscores the importance of those investments targeted to working mothers that are contained in the American Jobs and Families Plans. Staff have highlighted welcome opportunities to mitigate poverty and increase social mobility, including through strengthened social safety nets and by further increasing progressivity in the tax system. We would also encourage the authorities to consider staff's advice for improving the coverage and affordability of healthcare, in particular through improved competition in the sector.

We strongly endorse staff's recommendations on trade. While many of the U.S.'s top trading partners are no doubt benefitting from positive spillovers from the historic fiscal response to the pandemic, we share staff's concern that many of the pre-pandemic trade distortions remain in place. We encourage the U.S. to show leadership in strengthening the rules-based multilateral trading system.

We welcome the inclusion of an assessment of governance and transparency and commend the U.S. for becoming a driving force in coordinating and cooperating in investigating and resolving multijurisdictional foreign bribery matters.

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GRAY/21/2070

July 15, 2021

**Statement by Mr. Huh, Ms. Johnson, and Mr. Yoo on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for the Article IV report and Ms. Shortino and Mr. Sturm for the comprehensive Buff statement in which they detail the authorities' decisive and sizeable actions to drive a stronger, greener, more sustainable and equitable US economy. The turnaround in the US is remarkable: the policy redirection on a number of fronts has seen an effective vaccine rollout, corresponding reduction in COVID cases, unprecedented fiscal and monetary support that continues to restore the economy, while also providing necessary support to tackle existing challenges and necessary transitions for the US economy. We broadly share the staff's assessment and offer the following comments.

We welcome sizeable and ambitious fiscal policy actions, although political realities may see this ambition reduced. Given the political realities of Congressional approval, such reforms, if achievable, will be significant in terms of the impact on the US economy. Noting that these policies rely on the passage of comprehensive tax policy changes, we therefore tend to agree with staff that elements of the fiscal response could have been better targeted. But as this is the first year of a new administration, we can also understand the authorities' ambitions and recognize the reality that reforms are most likely to be successful in the first year after an election. *Does staff have an estimate of the impact on US growth under a different (or reduced) fiscal and revenue package?* We agree with the authorities that the US continues to have substantial fiscal space, and that fiscal consolidation should only be considered as the economy gets closer to full employment in the medium-term. With this in mind, we note the potential political and implementation difficulties the US may face when considering the staff's (often repeated, but not implemented) recommendations around potential future revenue raising (e.g. a broad-based consumption tax).

Inflation risk is a risk to both the US and global economy requiring careful monitoring and communication. While risky, we note with interest that the authorities seem to have successfully introduced a new monetary policy framework while continuing to deploy all tools to support the economy amidst significant uncertainty. But as the new framework

coupled with the significant fiscal support defers the timing of policy normalization, we therefore agree with staff that the Federal Reserve has a challenging transition ahead, which will need to be handled carefully. We welcome the authorities' commitment to clear communication about future policy changes, which will be key to managing inflation expectations during the recovery. Any sudden shift in policy rates or asset purchases could see a repeat tightening of financial conditions with damaging spillovers for sovereign, corporate and household balance sheets around the world. In this vein, a closer and well-communicated macroeconomic policy coordination in global platforms such as the G20 would be highly appreciated

The pandemic revealed shortcomings in the functioning of US market and rising corporate and non-bank leverage continues to be an area of financial stability risk. We agree with staff that more could be done to fill data gaps in this area, develop prudential tools to address risks and vulnerabilities in non-banks and mitigate liquidity risks in fund management by strengthening stress tests or introducing mandatory liquidity buffers. In addition, given the growing systemic importance of non-banks in the US, public sector backstops, in conjunction with strengthened supervision, to the non-bank sector may need to be reconsidered. We take note of staff's finding that a range of FSAP recommendations have not yet been addressed but see the study of lessons learned from the pandemic as the top priority.

Equity is a clear policy priority for the US administration. The reform agenda is welcome, yet ambitious, and will work towards addressing longstanding structural challenges in the US system. We welcome the authorities' willingness to grasp opportunities to build back better – in tackling necessary transitions needed for the post-pandemic recovery, the move to a lower carbon economy, encompassing necessary digitalization while managing demographic changes. We would also encourage the authorities to consider staff advice for improving the coverage and affordability of healthcare, in particular through improved competition in the sector.

We strongly support staff's call for reversing trade restrictions and tariff increases, and for constructive collaboration with trade partners to address distortions in trade flows and investment decisions. We consider that a more open, transparent and rules-based international trading system is the best way to ensure fairer and stronger global trade. The pandemic underscores the need to avoid policies that distort trade, including tariffs, non-tariff barriers and subsidies. We reiterate that the application of currency-based countervailing duties not only poses a significant risk to the multilateral trading and international monetary systems but would also harm the US economy and have negative spillovers to other countries.

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GRAY/21/2072

July 15, 2021

**Statement by Mr. Hilbers and Mr. Voinea on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank Mr. Chalk and his team for their insightful report and Ms. Shortino and Mr. Sturm for the comprehensive and informative Buff statement. While the U.S. was hard hit by the pandemic, the new Administration has planned and implemented a highly effective vaccination campaign which led to the recovery being strongly underway and normal activities largely resumed.

The massive combined fiscal and monetary support has been instrumental for the U.S. recovery, but also brings positive spillovers to the global economy. The American Rescue Plan is helping low and middle-income households and businesses across the nation bridge the gap to a full recovery. At the same time, the effect of fiscal stimulus measures may be further strengthened by prioritizing spending towards programs that have the biggest impact on productivity, labor force participation, reducing poverty, and facilitating a shift to a low-carbon economy. While debt is not a concern at the current juncture, we agree with staff that additional steps are required to set the debt ratio on a downward trajectory in the medium term.

On tax policy, we welcome the direction towards a more progressive income taxation of individuals, aimed to reward work and not wealth, and benefitting lower-middle income families, including through the child tax credit, block grants to state-and-local governments, eldercare, and subsidies for childcare. We welcome a more equitable contribution of large corporations, including the support for a minimum global corporate tax.

On monetary policy, the swift policy response helped maintain the well-functioning of the U.S. and the international financial system, and preserved liquidity in various EMEs. The revised monetary policy framework increased inflation targeting flexibility and allowed for temporarily higher inflation rates to compensate for longer-lasting episodes of low inflation. However, the inflation dynamics in recent

months need to be assessed with caution; while the hike appears to be transitory, driven by supply bottlenecks as the economy reopens and by one-off demand stimulus measures reflected in higher disposable income, the perspective of a gradual return to policy normalization requires fine tuning as the implications of anchoring inflationary expectations in the U.S. are paramount for the global economy.

In addition, both the commercial and residential real estate markets require close monitoring in light of rapidly changing demand conditions due to the pandemic and other structural factors. In particular home prices have been rising very rapidly which can have financial stability implications.

Finally, we welcome the ambitious path of structural transformation on which the new U.S. Administration has embarked, based on investment prioritization and labor market reforms that would raise the medium and long-term equilibrium and would “build back better” a greener, more digital and more inclusive economy. We wholeheartedly commend the decision to rejoin the Paris Treaty on climate and the important commitments to lower carbon emissions and increased resilience to climate change. Overall, we welcome the return of the U.S. towards multilateralism be it in fiscal cooperation, climate change mitigation, and trade policies, and trust that the positive spillovers of the Administration’s policies will benefit the global economy.

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GRAY/21/2074

July 15, 2021

**Statement by Mr. Andrianarivelo and Mr. Diakite on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for the comprehensive reports and Ms. Shortino and Mr. Sturm for their helpful Buff statement. We broadly share staff's assessment of the recent macroeconomic performance and outlook of the U.S. The economy is displaying an unprecedented potential for strong recovery in 2021 owing to the authorities' commendable response to the pandemic. The impressive vaccines' discovery, development and rollout coupled with massive supportive fiscal and monetary policies are expected to boost GDP growth to around 7 percent in 2021, reflecting the great adaptation capacity to shocks of the US economy. This is positive news given the spillovers that the US economy generates to the rest of the world. However, with new variants emerging, the United States will continue to face the downside risk of a worsening of the pandemic, which will require sustained efforts on the public health front to vaccinate more people not only in the US, but also abroad. The resurgence of inflationary tensions is also a source of concern. In addition, and more fundamentally, there are longstanding structural impediments to potential growth that will need to be addressed to strengthen the foundations for growth and resilience, raise productivity and labor force participation, and reduce poverty and income inequality.

We commend the authorities for the exceptional fiscal response which has been instrumental in mitigating the economic and social fallout from the pandemic. The large scale deployment of federal resources has enabled an effective vaccines campaign, support to businesses and households and made the recession less severe than in other advanced economies. With the uncertainties surrounding the new variants, we see merit in pursuing some of the fiscal stimulus packages, notably those aimed at assisting vulnerable households. We concur that going forward, tax increases on corporations and high income households will be necessary, notably to finance the comprehensive infrastructure plan of the authorities, and reduce the accumulation in public debt. *We would appreciate knowing to what extent staff's growth projections would be altered if the infrastructure, including the "human" infrastructure does not make through the legislative process.* We also encourage carbon

taxation and the transition to a greener economy, and the efforts aimed at closing loopholes that allow the avoidance of taxes, profit shifting and base erosion. We note positively the globally coordinated minimum tax on corporations and *we would appreciate staff's comments on the economic sectors that would be most impacted by this minimum tax on corporations*. We also agree on prioritizing spending to those that have biggest impact on productivity.

Monetary policy should remain accommodative until the recovery takes hold, and there are clear signs of improvement in achieving the FED's unemployment and price stability goals. The flexible new monetary policy framework targeting an average inflation of 2 percent over time gives room for such a policy since inflation has been below target for an extended period of time. We agree with current and past recommendations that with the decline in the neutral rate, some overshooting of inflation in the short term should be accepted to avoid the constraint of the lower effective bound on monetary policy, and allow monetary policy to support better a rebound of the economy following an adverse shock. We therefore find sensible the FED' decision not to tighten monetary policy until there are clear signs of improvement in employment and in the economic sectors which were most hit hard by the pandemic. However, the FED should stand ready to tighten monetary policy if inflation starts to accelerate beyond its expectations. The FED should be commended for its effective transparent and forward looking communication strategy which is essential in anchoring inflation expectations and providing an outcome-based guidance on the future path of policy rates. Such effective communication will be needed when the FED eventually scales back its asset purchasing program.

On the structural challenges to building back better the post-pandemic economy, addressing the rising income polarization and poverty in the United States should be high on the list of priorities, especially considering the disproportionate negative impact that the pandemic has had on the middle class and low income groups. The staff's report figures on racial disparities in economic outcome are very revealing and concerning. This could undermine efforts for more sustained and inclusive growth. In this regard, we welcome the current administration's intention to increase support for the communities that have been historically underserved, marginalized, or adversely affected by persistent poverty, as also indicated in the Buff statement. Other secular constraints will also need to be tackled, including climate change, digitalization and technological changes, and the aging population. We take good note of the recommendations in these areas, notably on the carbon tax and the need for better and more cost-effective education and health systems. The authorities renewed support to multilateralism should be pursued, including the cooperation on free trade which is essential for the stability of the global economy.

With these remarks, we wish the U.S authorities every success in their endeavors.

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GRAY/21/2076

July 15, 2021

**Statement by Mr. Buissé, Mr. Rozan, and Mr. Roman on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for the comprehensive report and Ms. Shortino and Mr. Sturm for the insightful Buff statement. The United States has been implementing a considerable public health and economic response to the pandemic, which is clearly bearing fruit. The authorities' deployment of their "Build back better" multifaceted agenda, to support families and tackle challenges such as climate change and inequalities, has the potential to address long standing fragilities of the US economy. We therefore share the thrust of staff assessment and wish to offer the following comments.

The response to the pandemic has put the economy back on a strong footing. The ambitious vaccine rollout is proving its efficiency to fight the pandemic. Now, reaching out to those who are not yet vaccinated will be a key factor for a full economic recovery. The unprecedented fiscal effort provided much needed support to businesses and households, strengthening the social safety nets. While recognizing the efforts from the authorities to address the challenges of lower-middle income families, we tend to agree with staff that the American Rescue Plan could probably have been better targeted to the most affected individuals and sectors. All in all, the support provided has mitigated hysteresis risks stemming from unemployment and corporate bankruptcies. We note that the total number of corporate bankruptcies remained low relative to historical trend, and staff assessment that there will likely be some corporate failures as temporary rent moratoria and policy support expire: *could staff provide an order of magnitude of potential future bankruptcies and zombie firms? Is there a risk that these bankruptcies would not be smoothly managed?* Finally, we noted that potential GDP has been revised upward, in the short run, which tends to mechanically reduce the assessment of an overheating. Overall, we think however that the impact of the proposed fiscal packages on potential GDP might be lower than what is currently suggested. *Could staff comment on these revisions?*

The proposed American Jobs and Families plans respond to important structural needs of the US economy. We strongly welcome the planned multi-year investment program that will stimulate demand in the short run, help remove bottlenecks and increase productivity in the long run, and we particularly appreciate the solid empirical evidence of the societal payoffs of the plans. *Further comments of the ongoing dynamics in the labor market would*

be welcome, as labor shortages in some sectors coexist with a still low participation rate. The implementation of these plans is however subject to significant political uncertainty, and we therefore look forward to their finalization with Congress

We agree with staff that attention should be paid to the fiscal path over the medium term, notwithstanding the declining cost of financing of the federal government, and we strongly support the revenue measures being considered by the authorities. The proposals have important implications for the international system of corporate taxation, and the historic agreement reached within the OECD/G20 will pave the way for a fairer global taxation. In addition to tax rates, it will be important to reach an ambitious agreement on eligible bases and deductions. Additional domestic measures could be considered to raise revenues, notably increasing the reliance on indirect taxation (VAT, carbon and fuel taxes). On the expenditures side, we support the various recommendations aimed at curbing the rising cost of healthcare, in particular by developing competition between suppliers in local markets and increasing transparency.

On monetary policy, all tools were rightly mobilized to support the economy and fight the effects of the pandemic. Overall, we tend to agree with staff that recent inflation spikes are of a temporary nature, given in particular the relatively low employment rate, but we very much welcome the policy scenarios outlined by staff. The adoption of the flexible average inflation targeting framework in August 2020 should help keeping inflation expectations anchored, and we note the benefits of the framework in the context of the COVID-19 shock. Given the change in the monetary framework in the midst of exceptional fiscal expansion, the Fed will face a delicate challenge of fine tuning its policy reaction going forward – transparent and timely communication will be paramount. We note that markets may have had difficulty understanding the new target – *could staff comment on the risks attached to this?*

Building a more resilient financial system should remain on the agenda, in a context where the health crisis has exacerbated existing vulnerabilities. We share staff's and the authorities' views on the overall resilience of the financial system, but some areas continue to deserve close monitoring. Corporate debt, and its concentration on the riskiest companies could potentially weigh on the recovery. The pandemic has also revealed shortcomings in the functioning of the Treasury and the money markets, requiring Fed intervention. We thus support staff recommendations, such as the central clearing of Treasury market transaction and the introduction of a standing repo facility open to banks and non-banks. We also encourage the development of macroprudential tools to address risks and vulnerabilities in the nonbanking sector and encourage the authorities to implement outstanding FSAP recommendations, particularly reviewing prudential requirements for non-internationally active banks (category III and IV) and ensuring they continue to be consistent with the Basel framework. The financial system must be resilient to the risks from climate change, and we look forward to the work from FSOC and SEC to improve climate-related financial disclosures. We encourage staff to deepen the work on the interlinkage between the financial system and climate in future article IV consultations.

On trade policy, we welcome the recently concluded framework agreements on large civil aircraft with the EU and the UK, but we share staff's concern that many of the trade distortions introduced over the past four years remain in place. We urge the authorities to strengthen the existing rules-based multilateral framework to address

macroeconomic imbalances, rather than relying on retaliatory tariff measures. Renewed engagement at the WTO would facilitate progress on these topics, including by restoring the proper functioning of the dispute settlement system.

On climate, we strongly welcome the authorities' GHG emission reduction targets following their return to the Paris Agreement; they must now be operationalized. The investments being rolled-out in the areas of buildings efficiency and electric vehicles will play a crucial role in this transition. However, we share staff's views that these investments and subsidies will be most effective as a complement to carbon pricing, and not as a substitute. Regulatory changes and standards are also an efficient complement to carbon pricing, for instance regulations on GHG emission for new vehicles (both cars and vans), or the implementation of feebates. We strongly welcome the detailed analysis in the report on climate issues. We share staff's focus on the importance of rapidly greening the agricultural sector, as evidenced in box 9; as in other countries, the American authorities should initiate a transition to less polluting activities, with an approach that promotes the value of ecosystems. The report also rightly emphasizes in box 10 the importance of decarbonizing power production: greening the power sector via nuclear energy and renewable energies is indeed necessary to make the electrification of industry and transport relevant to climate policies.

The report rightly emphasizes the importance of fighting inequality and advancing towards a more equitable society. We share staff's views that the U.S. has significant scope to strengthen its social safety nets and we very positively welcome proposed policy changes that aim to increase the progressivity of the tax system and expand spending in areas that are most incident on those at the bottom of the income distribution (education, childcare, food assistance, and healthcare). While the report highlights various poverty indicators in box 11, it could usefully be complemented by indicators on non-monetary poverty (material and social deprivation) and on poverty perception.

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GRAY/21/2079

Revised

July 15, 2021

**Statement by Mr. Tanaka, Ms. Kashima, and Ms. Ogihara on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for the informative report and Ms. Shortino, and Mr. Sturm for their insightful buff statement.

While the U.S. economy is rapidly and strongly recovering from the COVID-19 crisis, the outlook of the domestic economy and future policies will have a significant impact on the global economy. We welcome staff's comprehensive analysis which gives a valuable insight for the future U.S. and the global economy under great uncertainty.

We commend the authorities for their prompt and large-scale fiscal policies, accommodative monetary policy, the adoption of market stabilization measures, and the swift vaccination rollout. Going forward, **the authorities will need to implement targeted policies, and steadily address mid- and long-term issues such as increasing budget deficits, widening poverty and inequality, and promoting climate-change issues.** Addressing these challenges will be key not only for the U.S. economy but also for the stable growth of the global economy.

While we generally agree with the staff's analysis and policy recommendations, we would like to give comments on the following points.

Economic Outlook

The prompt vaccine rollout and appropriate policy responses enabled the rapid recovery of the U.S. economy, which further contributed to the recovery of the

global economy. We also thank the authorities for their support to facilitate vaccine rollout in other countries. In 2021, the U.S. economy is expected to grow at 7.0%, supported by strong growth in private consumption and investment. With cumulative economic stimulus measures and the monetary policy stance, growth rate is expected to remain high until 2023, after which the potential growth rate is expected to increase somewhat due to infrastructure investment and the implementation of social security and employment measures.

Fiscal policy

We commend the authorities' prompt stimulus measures, which have helped vulnerable groups and businesses and prevented economic and social disruption.

That said, considering the size of cumulative \$6 trillion spending and further plans for the future, the authority should closely monitor its economic effects, multiplier effects of infrastructure spending, and the impact of increased spending on revenue growth. The series of fiscal stimulus package is expected to increase the PB deficit to 14% by 2021 and increase the debt-to-GDP ratio to 105% by end-2021. **In order to ensure sustainable growth, it is essential to reduce the fiscal deficit in the medium term.** While interest payments are currently suppressed due to the low interest rate environment, the authorities should avoid being complacent, and steadily proceed with fiscal consolidation, bearing in mind the possibility of increased interest payment in the case of rise in interest rates.

On the expenditure side, **government spending should continue to support vulnerable households and most affected people.** We support staff's recommendation that government spending should not disincentivize labor participation **but focus on more targeted area to promote higher productivity and efficient resource reallocation, which would lead to a sustainable growth over medium term.** *We would like ask staff to elaborate on staff's recommendations regarding the medical sector on efficiency innovations, price transparency, market approaches for healthcare providers, and drug pricing, including their future prospects and fiscal implications.*

On the revenue side, **we commend the authorities for the tax reform plans, including the international agreement on corporate taxation and the tax hike on firms and high-income households.** Such measures will contribute to preventing tax loopholes and evasion and moving towards fiscal consolidation and would be beneficial for both the US and global economy.

Monetary Policy and External Sector

We commend the FRB's swift policy measures including the establishment on various facilities in response to the pandemic. The new framework adopted in August last year has significantly contributed to the normalization of financial markets by managing disinflationary risks and building up market inflation expectations.

On the other hand, under the current rapid recovery, the authorities should also be mindful of multiple factors that could impact inflation dynamics, such as labor mismatches, supply shortages and expansionary fiscal policies. The increase in asset prices, including the housing market, also needs close attention. We agree with staff that the risk of sustained inflation is low. That said, if such risk materializes, it could have a major impact not only on the U.S. economy but also on the global economy. The FRB needs to keep a close eye on future price trends and communicate carefully regarding price developments and its monetary policy stance. In addition, we commend staff's efforts on analyzing the different effects of monetary policy on heterogenous agents, as analyzed in Box 2. We expect the FRB to continue to carefully communicate its monetary policy keeping such issues in mind as it pursues its mandate of price stability and maximum employment.

We take note of the uncertainties that may arise as the U.S. economy transitions to a recovery state and monetary and fiscal policies normalize, such as increase in dollar funding costs and risk premiums and the impact on highly leveraged corporate and non-bank sectors. Furthermore, significant repricing in various financial markets could arise as a result of increase in long-term interest rates due to higher inflation expectations. The risk of zombification related to corporate debt markets and the associated spillover risks of repricing to emerging economies should also be noted. In addition, as noted by staff, the authorities need to address the vulnerabilities in the U.S. Treasury Market exposed by the pandemic through establishing central clearing and permanent repo-facilities.

With regard to the external sector, although a large increase in the budget deficit was offset to some extent by private savings in 2020, the current account deficit is likely to widen further in 2021. In this regard, **we agree with staff that the authorities need to strengthen fiscal consolidation and make use of the rules-based multilateral trading system to contribute to employment and productivity.**

Structural Policies

As the economy recovers from the pandemic, the authorities should address medium- and long-term issues such as climate change, digitalization, and demographic changes and inequality, which were also pre-pandemic challenges.

At the same time, as pointed out by staff, structural reforms consistent with the post-crisis situation are required, to address changes in consumer preferences, social modalities and necessary skills, as well as inequalities in access to healthcare services and education that were further exacerbated by the pandemic.

As for climate change policies, we welcome the return of the U.S. to the Paris Agreement. Also, with regard to sustainability investment, we commend the authorities' comprehensive plan including disaster prevention as well as climate change mitigation. Authorities need to closely monitor the impact of environmental regulation on firm activities and price developments, as such regulations could broadly impact industries and lead to human and capital resource reallocation. We note the different views between staff and the authorities regarding the benefits of carbon tax. Besides explicit policy like carbon tax, the authorities could adopt other measures including regulatory approaches, preferential political treatment for renewable energy or other measures to achieve "Net Zero by 2050". Appropriate and applicable combination of policies should be determined according to each country's specific situation.

As for the labor market, we are concerned about the scarring effect of the pandemic and the long-term impact of COVID-19 on structural changes in the labor market; in particular, the impact on women who were forced to leave their job due to the closure of schools and students who missed out on educational opportunities. *Could staff comment on various measures taken by the authorities to facilitate the accumulation of human capital and participation in the labor force?*

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GRAY/21/2081

July 15, 2021

**Statement by Mr. Pösö and Mr. Slettvag on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for the report and Ms. Shortino and Mr. Sturm for their informative Buff statement. We broadly agree with staff's appraisal and policy recommendations and would like to offer the following comments for emphasis.

The US authorities have acted forcefully to mitigate the health and economic costs of the pandemic, and we welcome the new administration's policy program aimed at a greener, more sustainable, and equitable recovery. The proposed fiscal packages go a long way in addressing longstanding shortcomings in U.S. infrastructure and the social welfare system, and we see large benefits from expanding access to high-quality childcare, schooling, and healthcare, alongside investments in power, transportation, and telecommunication. We welcome the ambition to create a national paid family leave program that, alongside improved access to childcare, will help increase labor force participation among women and support working mothers who have been hard hit by the pandemic. We note that the combination of the American Rescue, Jobs and Families Plans is estimated to add a cumulative 10 ¼ percent to the level of GDP by 2023, close to the optimal fiscal stimulus of 10 ½ percent suggested by Staff's "Buffer-Stock" model-analysis in last year's Article IV. *Has staff done any updated model simulations on optimal fiscal stimulus to account for changes in assumptions as regards, for example output gap, multipliers, or interest rates?*

Some fiscal plans could be better targeted to improve macroeconomic and distributional outcomes. We support staff's proposals for a reorientation of the tax and spending plans in a way that can give a more gradual and sustained demand impulse, create a bigger boost to aggregate supply, and reduce poverty. In particular, we see a case for phasing out tax credits at lower levels of household income to create space for making the child tax

credit permanent and permanently expand unemployment insurance for independent contractors and self-employed.

We find the changed characterization of the public debt sustainability appropriate given the low debt servicing costs and the special characteristics of the US sovereign debt market, including its depth, liquidity, and safe-haven status. The rising medium-term public debt trajectory in the baseline is nevertheless concerning, and measures to reverse this increase and rebuild fiscal buffers are warranted:

- **Tackling market power among health care providers and increasing competition in drug pricing could significantly lower the burden on fiscal accounts.** We note that the impact of an aging population and rising healthcare costs are the most important drivers of the debt dynamics in the medium term. We acknowledge that the authorities will have a challenging task in lessening the impact of an aging demographic on future spending, but would caution against containing healthcare costs through large increases in cost sharing or the minimum age for Medicare eligibility given the importance of maintaining affordable coverage for elderly and lower income households. Rather, with healthcare in the U.S. being the most expensive in the world, with a significant increase in market power and mark-ups in recent decades (as noted in Box 6), efforts could be concentrated on increasing efficiency and reducing fiscal costs through more assertive antitrust policies and increased competition.
- **The introduction of a carbon tax and higher fuel taxes would be beneficial both in facilitating the transition to a lower carbon economy and yielding substantial fiscal revenues.** We welcome the administration's strong commitment to reduce greenhouse gas emissions but share staff's view that this will be costly and hard to achieve without greater focus on carbon pricing. We appreciate the analysis in Box 7 that shows how the use of a carbon tax in combination with clean energy subsidies would be able to achieve the administration's targeted reduction in emissions without adding to the debt to GDP ratio. Moreover, we encourage the authorities to consider sectoral carbon pricing instruments, such as feebates, to reduce the emission intensity in particular sectors, as discussed in Box 8.

On monetary policy, we commend the Fed for the forceful measures it has implemented since the outbreak of the pandemic. We agree with staff that the new monetary policy framework is a timely innovation that will help redefine the policy approach as the U.S. emerges from the pandemic. The framework will support the recovery by allowing for more accommodation over a longer horizon, helping to overcome the challenges caused by the low natural rate of interest and the effective lower bound. Nevertheless, as the new policy

framework is not yet closely parameterized, it could give rise to increased uncertainty regarding the duration and timing of the intended overshoot and complicate the eventual withdrawal of monetary accommodation. Managing this outcome-dependent transition, under a potential tight timeline, will continue to require careful communication to avoid market volatility and unwarranted tightening in financial conditions.

The Fed must be prepared to adapt quickly if upside risks to inflation are realized. We agree with staff's assessment that significant labor market slack will most likely dampen underlying wage and price pressures for some time. Assessing the inflation pressure is, however, challenging at the current juncture due to the significant and exceptional transitory movements in relative prices, and it will be crucial to closely monitor underlying prices once temporary effects pass through the system. *What is staff's reading of the most recent inflation numbers, showing y/y growth of 4.5 percent for core inflation? How much more can the core CPI increase from the June level in the second half of 2021 to be in line with staff's forecast for the year as a whole?* We welcome the analysis in Box 4, showing modest effects on inflation from stronger demand or a steeper Philips curve, but note that these results depend largely on inflation expectations being well anchored. As staff notes, a situation with de-anchoring of expectations would leave the FED with much less room to maneuver, and it would have been useful to also consider scenarios where expectations do not remain anchored when assessing possible inflation paths and policy responses.

Moreover, **sustained labor supply and demand mismatches could add to increasing cost pressures.** Recent data from the labor market indicate a record high mismatch, with the number of vacant positions rising to about the same level as unemployment, just above nine million. This raises concerns that inelastic labor supply over time could push wages and prices higher than assumed in staff's forecast, and we have already seen that sequential compensation growth has been firm, in spite of a jobs shortfall of almost eight million relative to last February. *Could staff elaborate on why they consider the mismatch in the labor market transitory, including what they see as the main drivers behind the inelastic labor supply? Does staff consider that fiscal measures could be better calibrated to incentivize a return to the labor market? Has there been any signs that labor markets recover more rapidly in states that have ended expanded unemployment insurance?*

The US financial sector has proven resilient and flexible during the pandemic, but vulnerabilities have increased with rising leverage and risk-taking. Corporate borrowing rose to unprecedented levels already before COVID-19 and has jumped further during the pandemic, constituting a key vulnerability that could amplify shocks to the economy. Rising leverage among corporates, as well as in nonbanks and vulnerable households, should be monitored carefully and we encourage the authorities to move forward with the

implementation of the FSAP recommendations that have not been addressed. We note that rollover needs for non-investment grade corporates are relatively small but would have welcomed a broader assessment of the vulnerabilities in the sector. *How does staff assess the vulnerabilities in the corporate sector now, as compared to before the pandemic?*

Steps should be taken to ensure the stability of globally systemically important U.S. market segments. We have noted with concern the episodes of rapidly deteriorating market liquidity in the U.S. Treasury market during the pandemic, and support staff's call for structural changes in the operation of the treasury market, key money markets, and prime money market funds to prevent the recurrence of these vulnerabilities.

Trade barriers are ineffective in reducing bilateral trade imbalances and risk harming the US economy. Many of the trade distortions introduced in recent years remain in place, and we are concerned that these measures, together with an expanded preference for domestic producers in procurement, could undermine multilateral trade and the international monetary system, and harm the US economy. We note that a comprehensive review of trade restrictions and tariffs is being undertaken, and encourage the authorities to roll back trade barriers and work with international partners and the World Trade Organization to modernize and strengthen the rules-based multilateral trade system in a way that would be beneficial to both the global recovery and the US economy. We agree with staff that currency-related trade responses should be avoided, and that the US should work constructively with its trading partners to better address the underlying distortions that are affecting external positions.

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GRAY/21/2084

July 15, 2021

**Statement by Mr. Guerra and Ms. Arevalo Arroyo on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for the comprehensive analysis of the United States economy and Ms. Shortino and Mr. Sturm for their helpful Buff statement. The unprecedented fiscal and monetary policy actions taken by the U.S. authorities have supported a swift recovery from the COVID-19 pandemic and have had an extensive positive impact on the world economy. We broadly share the staff assessment and policy recommendations and will provide the following comments for emphasis.

Policies undertaken by the authorities will contribute to addressing structural problems and to building a more resilient and transformational recovery in the aftermath of the pandemic. The national vaccination effort, which is advancing at a rapid pace, will contribute to the reopening of the economy and a faster recovery. On the fiscal front, the proposed plans of the authorities, as stated in the Buff, are not only spending programs aimed at solely supporting the economic recovery, but rather, said programs should be regarded as major public investments. Undertaking these investments will help to modernize the economy and increase productivity, while addressing climate change challenges and tackling rising inequality. We note the authorities' plans to implement a broad tax plan to close tax loopholes and raise taxes on corporates and higher-income households. In this regard, we agree with staff on the need to take additional steps over the medium term to bring down public debt, including by lessening the impact of demographic trends on future spending. We note, as reported in the DSA presented by staff, that even as debt is viewed as sustainable, there will be increasing spending pressures on entitlement programs. *Can staff elaborate on the assessment regarding the effect of the American Jobs and Families plans on the potential growth of the US economy?* This will be instrumental in ensuring public debt stabilizes in the medium-term and fiscal space is further increased.

The monetary authorities have used a broad set of tools that have been effective in averting a deeper crisis and have contributed to securing a stronger recovery. The implemented policy actions have also been instrumental in securing more adequate liquidity conditions in international financial markets, including for emerging and developing countries. We commend the authorities for taking timely actions to introduce a new monetary framework that has proven to be effective in supporting a more gradual policy approach during the pandemic. Going forward, in promoting its

maximum employment and price stability goals, the authorities should continue with a clear and effective communication strategy in order to avert unwarranted tightening in financial conditions. The strategy to scale back support will have to be carefully managed and adapted to the changing circumstances, particularly if the swift economic recovery continues and additional fiscal support is agreed and implemented. The assessment of the inflationary pressures will be complex given the various developments related to the temporary nature of supply shocks in the context of the pandemic. *The strong credibility of the monetary framework will serve as an anchor to maintain inflationary expectations. In this regard, can staff comment on recent developments in medium-term inflationary expectations?*

Safeguarding financial stability will be an important undertaking as the extraordinary policy support package is phased out. We concur with staff on the need to consider changes to address shortcomings in the Treasury market that surfaced during the unprecedented stress of the pandemic. In this regard, we welcome that the authorities are already prioritizing a broad interagency effort to address vulnerabilities in the U.S. Treasury securities markets and are taking further actions to work internationally and domestically to improve the resiliency of money market funds. *Regarding developments in the mortgage market, can staff elaborate on the potential risks given the rapid increase in house prices? Has any recent analysis been done by staff using the house-prices-at-risk methodology? What macroprudential measures are the authorities implementing to deal with potential risks in the housing market?*

Going forward, it will be important to consider the temporary effects that the pandemic is having on the external position. In particular, it would be useful to have a careful analysis of changes in the current account positions of trading partners that are of a temporary nature and that are expected to revert to previous positions after the immediate effects of the crisis have faded. While commending the authorities' increased efforts to foster international cooperation – including on climate change issues – it will be instrumental that the U.S. continues to support the strengthening of a rules-based multilateral trading system. A renewed engagement with the World Trade Organization will be instrumental in this regard.

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GRAY/21/2085

July 15, 2021

**Statement by Mr. Trabinski and Mr. Gindrat on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We broadly agree with the staff's assessment of the US economic developments. The authorities' policies have initiated a remarkable economic recovery. Effective measures by the authorities led to an impressive turnaround from the situation at the beginning of the pandemic. These policies, however, came at the cost of a considerable worsening of the debt path, higher twin deficits, and increased vulnerabilities in financial markets. Large shifts in demand coupled with less vigorous adjustment of the supply-side could give rise to imbalances and unwarrantedly persistent inflationary pressure.

In order to ensure a long-lasting macroeconomic impact, the unprecedented fiscal response should now be recalibrated. Addressing structural challenges like weak infrastructure, low productivity, and non-inclusive growth, will require tax and spending proposals that should focus on generating a slower demand and higher supply impulse, to help reduce risks of a sustained upswing in inflation. Importantly, as outlined in the DSA baseline scenario, the debt-to-GDP ratio fails to stabilize under the American Jobs and Families Plans. The implementation of a credible medium-term fiscal adjustment that helps reverse the public debt path is therefore crucial.

The Fed's transition to flexible average inflation targeting (FAIT) should support growth in the short term. In August 2020, the Fed transitioned to FAIT to address downside risks to employment and inflation. This new policy framework could support domestic demand in the short term. The slower pace of policy normalization should also result in weakening the dollar, increasing US competitiveness, and boosting exports.

Given a highly accommodative monetary and fiscal policy, the risks of overheating of the US economy and a surge in underlying inflation has risen. Several factors could generate higher-than-expected inflation. First, a slower rebound in labor force participation could create wage and price pressures, which could accelerate in case supply chain disruptions prove to be persistent. Second, the macroeconomic impact of the fiscal stimulus may be larger and more front-loaded than currently assumed. If these upside risks to inflation materialize, we agree with staff that monetary policy would need to adapt quickly.

We encourage the authorities to remain committed to an open and rules-based trading system. We concur with staff that US workers and jobs would be best served by incentives to increase productivity, labor supply and competitiveness. A reduction in trade restrictions and lower tariffs would be helpful in this context. External imbalances should be addressed by identifying and eliminating underlying distortions and establishing sound economic fundamentals. We encourage the authorities to constructively work with trading partners in the context of a rules-based multilateral trading system to better address the underlying macro-structural distortions that are affecting external positions.

Safeguarding financial stability will be important to ensure a smooth economic recovery. Although the financial sector is well capitalized and appears to be resilient, the very accommodative financial conditions are a risk for financial stability. Asset valuations are sharply increasing, and financial leverage has risen. Both developments should be monitored carefully to prevent systemic stress, which could occur in case of a badly received reduction in the accommodative stance by the Fed. We also see the substantial risk taking in the non-banking sector as an important vulnerability in the financial system. Macroprudential regulations should be strengthened to limit the scope for further risk-taking. Full implementation of FSAP recommendations would further help increase the sector's resilience.

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GRAY/21/2088

July 15, 2021

**Statement by Ms. Riach and Ms. Campbell on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for the reports for the 2021 Article IV consultation and Ms. Shortino and Mr. Sturm for their Buff statement. We broadly agree with staff's assessment.

Policy response to the crisis

The United States' effective vaccine rollout combined with an unprecedented policy response has contained the economic impact of the pandemic and is quickly restoring the economy back to growth. We agree that uncertainty around the shape and pace of the recovery is much lower than this time last year and risks to growth are now to the upside. This positive picture is set against a worsening two-track global recovery driven by dramatic differences in vaccine availability, infection rates and the ability to provide policy support. In this context, this paper provides useful analysis to helps us better understand potential positive and negative spillovers from the United States to the rest of the world.

Fiscal Policy

We commend the authorities for unprecedented fiscal support which has continued to provide substantial assistance to households, businesses and state and local governments. We note that this package of support, if fully enacted, is estimated to add 10.25% to the level of GDP during 2021-23 at a cost of an additional 3-4 percent of GDP to federal government debt by 2026.

The American Rescue Plan (ARP) effectively deployed resources to accelerate vaccinations, expand healthcare coverage, assist the vulnerable, unemployed and segments of society that had suffered the worst effects of the pandemic and bolster subnational government finances. However, we agree with staff that the American Rescue Plan could have been better targeted

to the most vulnerable groups. Whilst the report discusses the significant impact of the pandemic on low-income groups in terms of labor markets, and notes that absolute poverty has increased, we would have welcomed more discussion and evaluation of how the large and generous income support programs under the ARP and the Consolidated Appropriations Act operated across the income distribution. This could help inform lessons learned in terms of the tradeoff for countries between ease and speed of policy support and targeting those most in need.

We welcome the analysis in the paper of the American Job's Plan (AJP) and the American Families Plan (AFP) proposals from the Administration and the extent to which they align with previous Fund advice. This is helpful given the live debate on these proposals in Congress. *Given these debates are ongoing does the Fund have a view on the relative economic importance of the "hard" infrastructure investment versus the "social" infrastructure investment?* Finally, we see some downsides to including these two proposals in the baseline forecast given that the negotiations with Congress are at an early stage and there is still significant uncertainty around final size, composition and timing. We would be interested in whether staff considered an alternative approach.

Monetary Policy

We commend the Federal Reserve for continued accommodative monetary policy to support the recovery from the Covid-19 crisis. We agree with staff that, whilst there were risks to introducing a new monetary framework in the midst of pandemic related uncertainty, this new policy framework helped to support a more rapid recovery and has been helpful in managing policy from a conjunctural perspective. In relation to the new framework, we were interested in the link made in the report between average inflation targeting and inequality. *Could staff comment on whether the Fund will recommend this approach to other advanced economy central banks?*

We agree with staff that managing the transition from policy support to the withdrawal of monetary accommodation will require deft communications under potential tight timelines, particularly if upside risks to inflation are realized. We welcome the Federal Reserve's commitment to communicate its thinking well in advance and to ensure that the eventual withdrawal of monetary accommodation is orderly, methodical and transparent. This is important given the potential spillovers if global financial conditions were to tighten sharply and we agree with staff that the consequences of a rapid pick-up in inflation could be systematic for both the US and the global economy. *In light of this, could staff elaborate on any work they are planning to further explore the drivers of inflation expectations and associated risks?*

Climate

We strongly welcome the United States' return to the Paris Agreement and the commitment to reduce net greenhouse gas emissions by 50-52 percent by 2030. This represents a critical and positive shift. We welcome the focus of these issues in this report and the analysis on carbon pricing is helpful. As is the case for other countries, this is a historic opportunity to use the recovery from Covid-19 to accelerate the shift to a lower carbon economy and adopt fiscal policies that will help to facilitate a more environmentally sustainable growth model. *In the spirit of mainstreaming climate into the Fund's macro surveillance work, have staff assessed the macroeconomic impacts of the climate elements of the American Rescue Plan and the American Families and Jobs Plans?*

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GRAY/21/2094

July 15, 2021

**Statement by Mr. Fanizza and Mr. Spadafora on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for an excellent report and Ms. Shortino and Mr. Sturm for their candid and quite useful Buff statement. The Covid-19 pandemic has severely hit the United States. Lower income and lower skilled workers have suffered the most, and wealth inequality has further increased. Policy support has been effective in cushioning the impact of the pandemic and in paving the way for a robust recovery. As elsewhere, a resurgence of the pandemic – driven by more infectious and potentially vaccine-resistant variants – remains the main risk facing the U.S. economy. Like after the Great Recession, monetary policy normalization represents a key challenge, because of both the risk of jeopardizing the recovery and its possible significant adverse international spillovers. We appreciate the staff's analysis and support the policy recommendations. We offer a few comments:

- The U.S. authorities should be commended for including in their discretionary spending packages several measures that are transformative in nature and aim at improving key economic and social outcomes. These measures are likely to foster supply-side effects on: (a) labor force participation; (b) new capital formation; (c) and productivity. We are also pleased that many of the adopted policy measures are in line with past IMF advice.
- We see merits in the staff's recommendation to better target some policies not only to further strengthen their impact on supply-side and distributional outcomes, but also to lessen the impact on public finances. We particularly support the view that some resources could be redirected to make permanent both the child tax credit and the expanded unemployment insurance (UI)'s coverage to independent contractors, self-employed and gig workers; the latter measure would help increase the UI system's historically low reciprocity rate.
- We welcome that in staff's assessment the overall risks of sovereign stress are now judged to be low and the public debt is viewed as sustainable, despite the increasing debt-to-GDP ratio under the staff baseline. We support staff's view that further actions – along the lines suggested by staff in paragraph 35 – will be needed over the medium-term to reduce the public debt-to GDP ratio and counter the impact of aging population and rising

healthcare costs on mandatory spending. *In footnote 13 staff seem to characterize the “IMF Board-approved” definition of public debt sustainability as a novelty, while in fact it has been present in this form ever since the first staff papers on debt sustainability was published as early as 2002¹. Staff’s comments are welcome.*

- We agree with staff that the introduction of the flexible average inflation targeting has been a timely innovation that will help to create scope for monetary policy action even when the effective lower bound constrains policy action. In the midst of the pandemic, the possibility of allowing an overshooting of the Fed’s medium-term inflation target for a longer period has worked to defuse possible deflationary expectations.
- Like after the Great Recession, the timeline of monetary policy normalization constitutes a major challenge, not only for the possible risks of derailing the recovery, but also because of its potential for significant adverse international spillovers. We commend staff for the thorough and clear discussion in paragraph 30 on the possible sources of higher-than-expected inflation. We agree with the authorities that despite the recent spike in PCE inflation, it is too early to take action, because of both its large temporary component and the substantial slack in the labor market.
- We support the staff’s recommendations to address the vulnerabilities in the US Treasury and money markets.
- We share the staff’s analysis on the multiple transitions facing the U.S. economy in the coming years and their important socio-economic implications. We recognize that the flexibility and innovativeness of the U.S. economy are built-in stepping stones toward successful transitions; however, we join staff in emphasizing that risks of an increase in income polarization that may leave behind a material share of the population need particular attention.
- Finally, adding carbon pricing instruments among the policy toolkit to tackle climate change would greatly reinforce the authorities’ post-pandemic transformational drive and effectively help achieve domestic and global climate goals. We commend staff for the clear and comprehensive coverage of the challenges towards a greener U.S. economy.

¹ International Monetary Fund (2002), *Assessing Sustainability*.

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GRAY/21/2096

July 15, 2021

**Statement by Mr. Mohieldin, Mr. Alhosani, and Ms. Abdelati on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for a balanced and detailed report and Ms. Shortino and Mr. Sturm for their informative statement. We agree that recent policies have put the U.S. economy on a strong footing and that they seek to lay the foundations to address challenges that have afflicted the U.S. economy. We also recognize the substantial positive spillover effects for the global economy.

We agree that unprecedented fiscal support, combined with accommodative financial conditions, and an effective vaccine rollout, have together helped restore economic activity, paving the way for a sizeable expansion, estimated at 7 percent in 2021 and 5 percent in 2022. We also agree with staff that these policies have not been costless, and that the undesirable side effects include a higher path for public debt, a larger current account deficit, rising valuations across a range of assets, and increased leverage for corporates and nonbanks. Close monitoring of developments and underlying risks is therefore warranted and will need to be addressed.

As was highlighted in the 2020 Article IV consultation, the pandemic weighed more heavily on those who have lower incomes—the costs of the crisis are borne disproportionately by the poor and vulnerable. It has exposed deep inequities that have long afflicted the U.S. We therefore very much welcome that the administration is viewing their current policy program as an opportunity to address these challenges and move the economy to higher productivity levels, increased labor force participation, and a less polarized distribution of income and wealth—and increase access to social services and opportunities including for women and poorer households. Staff's analysis points to the difficulty of measuring poverty indicators but concludes that it remains high.

We therefore see merit in the direction of fiscal policies to close tax loopholes and raise taxes on higher income households and corporates, which could reverse the decline in federal revenue to GDP and secure some funding to advance the other policy goals including on the areas of social inclusion and climate policies. However, we also agree with staff that a better targeting of policies would further strengthen the impact on both macroeconomic and distributional outcomes. We support prioritizing spending towards programs that have the

biggest impact on productivity, labor force participation, reducing poverty, and facilitating a shift to a low-carbon economy.

Staff also makes a set of recommendations on the phase out of tax credits, eliminating the step-up basis, lowering the estate tax threshold and reformulating the business tax. *In this regard, we would welcome staff views on the potential adverse effects of the proposed global minimum tax on offshore profits of U.S. multinationals, as well as the proposed measures to incentivize “onshoring of jobs back to the U.S., especially on operations and investments in emerging markets and developing countries.* While the proposed measures hold promise of lifting potential growth, and staff assumes full implementation of all fiscal plans in the baseline scenario, we recognize the remaining hurdles to secure domestic agreement. The combination of strong support for infrastructure from the Jobs Plan and for labor force participation from the Family Plan have already contributed to building confidence, and the accompanying tax package would mitigate the impact on indebtedness to the extent that it supports higher growth as envisaged.

We share staff’s praise for the highly effective actions taken by the Federal Reserve throughout the crisis and in supporting the recovery. The new monetary policy framework was smoothly introduced and has increased monetary support as the economy recovers from the pandemic and is in line with past IMF advice for a near-term overshooting of the 2 percent longer-run inflation goal. As recognized by the Fed, the ongoing rapid pace of recovery, and expected additional fiscal support, may well necessitate a shift in monetary policy. We welcome the commitment of the Federal Open Market Committee to continue to communicate shifts in policies to avoid misunderstandings that could lead to volatility in market pricing or unwarranted tightening in financial conditions. Rising leverage in nonbanks and corporates also needs to be followed carefully, and we welcome the robust agenda developed through the Financial Stability Oversight Council (FSOC) to address financial stability risks and to address vulnerabilities in the US. Treasury securities market and those related to nonbank financial intermediation. *Are there reasonable prospects for greater liquidity buffers for non-bank market participants to mitigate the need for official liquidity support in the future?*

The focus of policies is rightly placed on achieving a sustainable, green, and modernized economy. Managing ongoing transitions with an eye to reducing inequities will be important. Policy makers need to address the increasing role of digitalization and technology, the transition to a lower carbon economy, and the underlying shift in demographics—in a way that does not leave some segments of the population behind. The U.S. system is well-placed to face ongoing transitions, given its flexibility and innovativeness. We welcome staff’s detailed coverage of climate policies and commend the administrations’ commitment to achieving its revised nationally determined contribution (NDC) under the Paris Agreement and to ensure the power sector would be carbon neutral by 2035.

We note that the Risk Assessment Matrix assigns the highest likelihood of risks to widespread social discontent and political instability—and calls for policies to improve the social safety net, support the unemployed, and increase health resources. It is also important to contain and reduce the high level of US healthcare costs, which is the most expensive in the world. The staff calls for a multidimensional policy approach that will be needed to support rising living standards for all. We trust that the Families Plan will address the long-

standing shortcomings in the U.S. system, and look to staff to monitor the shaping of such policies and their impact in the coming period.

On international trade, the U.S. has a major role to play in strengthening multilateral trade and the international monetary system. We positively note the engagement with the international community, and the ongoing comprehensive review of trade tariffs and restrictions. We also take positive note of the pledge to share 580 million vaccine doses internationally.

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GRAY/21/2098

July 15, 2021

**Statement by Mr. Bhalla and Mr. Natarajan on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

1. We thank the staff for the detailed report and Ms. Shortino and Mr. Sturm for the comprehensive Buff. We commend the US authorities for their sustained effort in healthcare and the successful roll out of the vaccination program which has resulted in significant fall in new COVID-19 cases and test positivity rate. Improvement in the pandemic situation, coupled with exceptional fiscal support measures has provided a tremendous boost to the economic recovery with potential positive spillovers to the global economy. While the crisis has revealed the resilience of the country's institutions under extraordinary stress, it has also provided important lessons of the systemic shortcomings in their functioning. As the pandemic effects recede, the authorities need to manage the key transitions – demographic, digitalization, and climate change. Like the staff, we believe the inherent innovativeness and flexibility of the country's system will help to address these transitions.
2. After the pandemic-induced contraction in 2020, the economy is on a sound path of recovery and is expected to achieve about 7 percent growth in 2021. Witnessing a healthy growth in the first quarter, the economy is expected to grow stronger as vaccination rates rise and normal activities resume. Share of services in consumption has fallen but is expected to revive with normalization of in-person services.
3. The exceptional fiscal support measures have helped to improve health care coverage and support to households, vulnerable, unemployed, small businesses, and the corporate sector. The American Rescue Plan has provided support measures to the tune of US \$ 1850 billion to accelerate vaccination and expand healthcare coverage, support to schools and colleges, food, housing, unemployment benefits and transfers. The proposed American Families Plan focuses on investment in infrastructure, human capital, and support to vulnerable households. In a similar vein, American Families Plan proposes tax credits for childcare, nutrition, universal pre-school, and grants to

- college students. We welcome these efforts and the multi-year investment in infrastructure which will help to improve productivity and increase labor force participation. We agree with the authorities that these gains are “institutional” and encourage better targeting of policies to strengthen their impact.
4. The cost of the fiscal measures is expected to be partially funded by raising taxes on high-income households and corporates. Proposals for increase in corporate taxes include increase in statutory corporate tax rate, minimum tax on book income profits, and minimum tax on offshore profits of US multinationals. On the personal tax front, proposals include an increase in the top income tax rate, taxing qualified dividends, taxing capital gains at top personal income tax rate and eliminating certain benefits in capital gains. We note that the staff has suggested raising tax revenues by increasing the reliance on indirect taxes. *Could the staff comment on the merit of this suggestion as indirect taxes are considered regressive with adverse impact, particularly on the poor?*
 5. On the monetary policy front, we commend the policy framework of the Federal Reserve which is intended to be accommodative for a longer period. The flexible average inflation targeting framework provides scope for temporary overshooting when the inflation approaches 2 percent and could be effective in returning the economy to full employment. We agree that the benefits of the approach include accommodation over a longer horizon in response to adverse shocks and placing more weight on inflation expectations. Inflation is expected to increase to above two percent by end-2022 and in case of steeper rise in inflation, the authorities have committed to act promptly. The size of the fiscal and monetary measures also weighs heavily on managing the transition wherein the monetary policy will continue to provide required support while preparing for the eventual withdrawal of monetary accommodation. The adverse fallout of this on the financial conditions, market pricing and spillover on the global capital flows needs careful consideration and deft management.
 6. The treasury and money markets were subject to enormous stress due to shifting of assets, liquidation of reserve assets by foreign official institutions and drawing down of credit lines by non-financial corporates at the time of onset of the pandemic. The banking system has remained resilient given its sound capital distribution, profitability, and credit quality. Though the prospects of widespread corporate failures have diminished, risk due to hedge fund leverages, exposure of nonbank financial institutions and credit risks in the commercial real estate sector have

increased. *Could the staff comment on the measures taken or envisaged to mitigate the risks arising from rise in hedge fund leverage?*

7. In the external sector, the current account deficit is expected to rise driven by a sizable increase in the fiscal deficit. We agree with the staff that there is a need to address the longstanding global trade and investment distortions in areas such as tariffs, service trade, farm subsidies and industrial subsidies by engaging with the concerned stakeholders. We take note of the administration's focus on ensuring a fair international trading system based on inclusivity, sustainability and rules-based international order and recognize the commitment in executing the domestic priorities consistent with the existing international obligations.
8. In managing the multiple transitions facing the country, we strongly welcome the authorities' commitment to use the current opportunity for 'building back better'. The pandemic has created lasting shifts in consumer preference along with transitions due to climate change, demographic changes, and digitalization. We appreciate the focus of the authorities in addressing the old economy's structural weaknesses, inequalities, and long-standing disparities in social and economic outcomes. In this regard, we believe that the innovativeness and flexibility of the US system will facilitate this transition towards a greener, more productive, and more equitable economy and society.
9. We wish the people and the authorities of the U.S success in their endeavors.

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GRAY/21/2099

July 16, 2021

**Statement by Mr. Palotai, Mr. Azal, Mr. Just, and Mr. Dogan on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for their insightful reports, and Ms. Shortino and Mr. Sturm for their informative Buff statement.

The US authorities' strong policy in response to the pandemic has paved the way for a robust recovery in 2021. We commend the authorities for the speedy and well-coordinated vaccination program which has enabled a quick reopening of the economy. The underlying structure of the economy based on private consumption has supported a significant bounce back of growth. The American Rescue Plan together with the American Jobs and Families Plans have also provided immediate financial relief to vulnerable segments of the population and countered financial insecurity of many households. We also see the envisaged further stimulus measures as essential to boost productivity and growth potential, including through a lasting green recovery. We understand that the authorities would like to avoid the mistakes of previous recoveries that withdrew support either too quickly or relied too heavily on the monetary policy leg. We are confident that the authorities will be able to succeed with their ambition for a more vibrant and inclusive economy, which will also be for the good of the global economy. We appreciate that the authorities are trying to promote multilateral solutions to global problems; however, this also needs to include an open and rules-based international trading system. We welcome the authorities' focus on trade distortions.

We commend staff for an excellent report that clearly spells out the complex tasks the authorities are facing to manage multiple transitions, for which well-sequenced and coordinated policy measures are needed to address both the structural challenges and the underlying vulnerabilities.

We concur with staff's analysis that the combination of fiscal, financial and monetary policies would reduce the unemployment rate to pre-pandemic levels and boost potential growth over the medium to long term, raising real GDP growth by 1 percent in 2030.

While fiscal policy packages are an important component for supporting the recovery and addressing bottlenecks, fiscal risks stemming from an aging population and

implications from building political consensus on redistribution warrant attention. While we are broadly supportive of the US trying to catch up with other advanced economies in terms of redistributive policies, there is a possible mismatch between the proposed increase in the spending envelope and planned increase of taxes on corporates and high-income households which could undermine broad-based political acceptance, in addition to higher debt accumulation. Therefore, careful budgetary planning and implementation is crucial. We welcome staff's analysis on tax incidents, particularly on equity financed investments and capital formation. *We would appreciate staff's insight whether the recent agreement on global corporate taxation will create a level-playing field between the foreseen higher statutory rates of the corporate taxation and taxation of large multinational enterprises. We wonder about the possible impacts on incentivizing debt financing and whether they would lead to changes in intersectoral or interregional investment decisions?* We note that the broad-based support schemes could possibly enhance job opportunities and mobilize businesses through increased public investments. In view of the significant infrastructure investment needs, effective crowding in of the private sector and of private capital appears crucial. We also see merits in a slight recalibration of the fiscal policy packages to facilitate more digitalization in the economy but also to significantly strengthen cyber resilience.

The accommodative monetary policies should continue to support economic activity and help get the economy back to full employment. However, we see monetary policy as the biggest challenge going forward. While we are broadly supportive of the revised monetary policy strategy which is now dependent on outcomes in economic data rather than the traditional forecast-based approach, this switch in strategy has come at a time of possible more deeper structural economic changes such as the functioning of the labor market with uncertainty over skills mismatches or different propensities to come out to work, which could change quickly if the health crisis were to take a turn for the worse. In addition, there are ongoing changes in supply chains, inventory management and transportation. While these effects could still only result in a transitory increase in inflation, the authorities need to be mindful of cascading effects and that a rise in inflation can be persistent, which could increase the possibility of a financial shock to a financial system that has been conditioned for the persistence of low and stable inflation. Much will therefore depend on the Federal Reserve's appropriate judgement that a surge in inflation is indeed transitory. We welcome that the Buff statement underscores the importance of continued clear communication about policy changes, and particularly about the withdrawal of monetary accommodation, which is warranted to reduce possible cliff effects and spillover impacts towards domestic markets and other countries.

While financial sector stability risks were manageable during the pandemic, vulnerabilities have also been revealed. Given the systemic importance of the US financial markets, we strongly encourage staff and the authorities to closely monitor and address potential financial sector risks. While the banking sector remains well capitalized and appears resilient, risks in elevated asset price valuations, notably real estate in certain regions as well as continuing high corporate indebtedness need to be carefully monitored, in particular in the second tier of banks. We support the Federal Reserve's supervisory stress test of bank holding companies and agree with staff that the funds (i.e. open-ended mutual funds, and hedge funds) should be subject to an annual liquidity stress test to ensure their

resilience. We also ask the authorities to make further progress in developing macroprudential policies for the non-bank financial sector given its increasing significance.

Finally, we commend the authorities for the renewed focus on climate action, which is an important signal to the global efforts. We fully share staff's concern that relying exclusively on subsidies and regulation will not suffice to make sufficient progress on the authorities' climate ambition, which ideally should be supplemented by a price on carbon. We also see price on carbon as the better signal for the private sector to redirect activities and spur technological innovation. However, we do not share the idea by staff that a tax on carbon should be used to reduce high debt levels but rather to finance a green and just transition.

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GRAY/21/2100

July 16, 2021

**Statement by Mr. Jin and Mr. Bai on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for the comprehensive and helpful reports and Ms. Shortino and Mr. Sturm for their informative Buff statement. We broadly agree with staff's assessment on the U.S. economy and appraisal on macroeconomic policies. We would like to make the following comments.

The new administration's efforts in promoting vaccine rollout has effectively contained the COVID-19 pandemic in the United States. This is encouraging and would significantly support the authorities' efforts to revive the economy.

We agree with staff's assessment on the outlook of the U.S. economy and potential downside and upside risks. While it is important to ensure that supportive policies are well-targeted and able to reach the most affected households and firms, we also encourage the authorities to address a range of deep-rooted social and economic issues in the ongoing transitions of the U.S. economy.

On fiscal policy, we welcome the authorities' unprecedented efforts to provide fiscal assistance to workers, households, and businesses and boost the economic activities. We take positive note that the authorities' proposed fiscal actions are tailored to lower-middle income families. We agree with staff's assessment that these extraordinary fiscal efforts have not been costless: the path for public debt is far higher, and the current account deficit has grown. Nevertheless, comparing with the high public debt levels in some other advanced economies, a temporary rise in public debt in the U.S. should not be a big concern, particularly when we take account of the current negative real interest rates and potential higher tax revenue.

On monetary policy, we take positive note that the Fed has introduced the new monetary framework. We notice staff's view that the current uptick of inflation is transitory.

However, with inflation rising sharply over the past few months, especially with the expectation of further fiscal stimulus, worries on the inflation risk is increasing within U.S. economists and business leaders. Former Treasury Secretary Summers has been seriously concerned about prices rising out of control. According to a recent report in the New York Times, corporate executives are also preparing for a longer spell of inflation. Jamie Dimon of JPMorgan Chase said that inflation was “a little worse than the Fed thinks.” The CFO of PepsiCo said the food and beverage giant was likely to raise prices soon. *We just saw and felt the U.S. inflation running at a 13-year high in June. Could the inflation trend last longer than “transitory,” and would the Fed raise the policy rates sooner and faster than expected? Staff’s comments are welcome.*

Moreover, another round of sudden capital flow reversal could be triggered in some Emerging Markets and Developing Countries (EMDCs) due to an abrupt tightening of global financial conditions. Against this backdrop, we welcome the authorities’ commitment in continuing to provide forward guidance and to communicate well in advance with the markets. *Is the Fed’s future trajectory of monetary policy the same as staff’s baseline scenario projection? Staff’s comments are welcome.*

On external sector and trade policy, we welcome the authorities’ commitment to an international trading system that promotes inclusive and sustainable growth. We need to point out that some practices introduced and maintained by the administrations have been inconsistent with the spirit of the rules-based multilateral trading system, such as broad restrictions on imports for national security reasons, and restrictions on normal transactions in both current and capital accounts. We fully agree with staff that these measures undermine the multilateral trade and international monetary system, as well as harm the U.S. economy. Therefore, we strongly support staff’s call for rolling back trade restrictions and tariff increases. We take note that there is a different view between staff and authorities on policies relating to currency practices. We share staff’s concern that currency-based countervailing duties pose significance to the multilateral trade and international monetary systems. We encourage the authorities to discuss reforms in a constructive and inclusive manner through the WTO and other multilateral frameworks.

On climate change, we are encouraged to see the authorities’ efforts in transforming the U.S. into a greener economy. We pay close attention to the authorities’ ambitious plan in reducing carbon emissions, and welcome the U.S. colleagues’ efforts to enhance international cooperation on the climate issue, including cooperation with the People’s Bank of China and other members in the G20. At the same time, it is contradictory for the authorities to set a high standard for other countries to cut carbon emissions, while restricting trade of green technologies to large emerging market economies for national security reasons. These restrictions on green technologies should be avoided in order to facilitate the global carbon emission reduction. We hope the position of the U.S. administration on climate should be consistent in all aspects, and not distorted by

geopolitical factors. We also encourage staff to promote and monitor free trade and flow of green technologies.

With these remarks, we wish the authorities all the best in these challenging times.

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GRAY/21/2101

July 17, 2021

**Statement by Mr. Hosseini and Mr. Sassanpour on United States
(Preliminary)
Executive Board Meeting 21/74
July 19, 2021**

We thank staff for an excellent paper: the report's analytical depth, its broad and thorough coverage, and its balanced assessment are impressive. We also thank Ms. Shortino and Mr. Sturm for their helpful Buff statement.

We laud the new US Administrations' transformational policy shift on multiple fronts to address a number of deep-seated problems in the United States, including income inequality, racial disparity, women and child welfare, aging population, healthcare and education gaps, infrastructure degradation and, importantly, climate change. We also commend the new US Administration's resolute early action to bring the COVID-19 pandemic under control, reversing halting policies of the last administration that entailed untold and unnecessary costs in terms of lives and livelihoods. We agree with the thrust of the staff appraisal and limit ourselves to the following.

1. Significant progress had already been made until very recently in the battle against the pandemic through a broadly successful vaccination campaign. Victory was in sight before the recent spread of the Delta variant of the virus and the unsettling sharp rise in infection and death rates. Vaccine hesitancy is an issue, and the fairly large unvaccinated population is a breeding ground and a human laboratory for mutations and deadlier variants. At the same time, vaccines are expiring on the shelves when there are many millions in poorer countries with no access to vaccines. We welcome the US government's decision to increase its vaccine donations to a large number of needy countries, as indicated in the statement of Ms. Shortino and Mr. Sturm, and encourage other countries with surpluses to follow suit.
2. The US authorities' unprecedented policy response has placed the economy on a firm footing with significant positive spillovers globally. Not only a strong recovery is in train, but it is also becoming more inclusive, greener, and forward looking. Specifically, the sizable

fiscal plans, including those pending legislative approval, are aimed at boosting demand in near term but, equally importantly, increasing the economy's aggregate supply response in the longer run through higher productivity, greater digitalization, and increased labor market participation, particularly of women, young minorities and older workers. We agree with staff that the effectiveness of fiscal packages could be enhanced through better targeting on both revenue and spending fronts. We also recognize that legislative passage of some of the proposals by the current Congress could be challenging, including those related to carbon taxation and estate taxes. We hope a political consensus would develop soon on both the "hard" and "human" infrastructure plans, given the urgent needs.

3. The Fed's change in the monetary policy framework at the peak of the pandemic was risky but has paid off and is supporting the recovery and moving the economy closer to full employment after a significant negative shock. We agree with staff and the authorities that the recent sharp pick-up in inflation is likely to be temporary as there is still a sizable employment slack. Financial markets also seem to have taken the recent price developments in stride and the new inflation framework appears to have been digested well by markets, with the apparent belief that inflation expectations are firmly anchored around 2 percent. De-anchoring of inflation expectations would, however, be very problematic, requiring quick policy adjustments, perhaps within a limited time frame. Given the broad global implications of an earlier and more abrupt monetary policy normalization, clear and timely communication with markets is critical.

3. The Fed's timely action restored market functioning after pressures emerged early in the crisis. However, prompted by historically easy financial conditions, there are potential signs of vulnerability reflected, inter alia, in unabated surge in assets prices—including housing—greater risk appetite, and increasing corporate leverage, all of which merit close monitoring. We would have also welcomed staff's assessment of potential fragilities associated with the large stock of student debt and any plans contemplated by the US authorities to ease the pressure on the educated young. We encourage the authorities to fully implement the 2020 FSAP recommendations. Noting that Appendix IV reflects the authorities' self-assessment, we would have welcomed staff's own assessment.

4. Poverty and widening income and wealth inequality, already palpable in the world's richest country before the crisis, were materially exacerbated by the crisis. These—education, healthcare, mother and child welfare, food security, and race relations—are long-standing, multi-dimensional issues, and we welcome the Administration's intent to address them with vigor at the root. The intention of providing a sizable share of the benefits from climate change and clean infrastructure projects to disadvantaged communities is novel and commendable. We also welcome the proposed US\$15/hour federal minimum wage that would particularly benefit women, young and minorities, with apparently limited adverse employment impact.

5. The United States has been at the forefront of free trade, barring the last four years. With the recognition that trade and technology restrictions do not address the underlying macro-structural distortions, we urge the US authorities to work closely with their trading partners to roll back these restrictions and help strengthen the rules-based multilateral trading system under the auspices of the WHO. We also like to stress that bilateral trade sanctions and payments restrictions typically entail costs at both ends and are generally ineffective.

**Statement by Rasmus Rueffer (ECB representative) and Kleopatra Nikolaou
on United States - Article IV Consultation 2021
(Preliminary)**

IMF Executive Board Meeting

19 July 2021

We thank staff Ms Shortino and Mr Sturm for their Buff Statement and the Staff for their reports.

Following an unprecedented collapse in economic activity due to the pandemic, the US economy is recovering fast. As Staff suggests, the prospects are for rapid growth in 2021 and 2022. Such progress is underpinned by effective vaccine roll-out and unprecedented policy support, including the recent American Rescue Plan adopted in March. This progress notwithstanding, the precise growth path is also subject to considerable uncertainties, including the size and timing of adoption of new fiscal packages, and the pace of consumer spending adjustment following the re-opening of the economy. At the same time, we agree with Staff that a resurgent pandemic is the primary risk factor, both domestically and internationally, and a continued active public health approach is warranted. As regards developments in inflation, while the current sharp rise in inflation is likely to be largely temporary (driven by base effects and a surge in prices of a few product categories that is linked to the re-opening of the economy), the risk of a more persistent rise in US inflation has increased and needs to be monitored carefully given the sizeable fiscal stimulus in the pipeline as well as the supply disruptions that have arisen and might be more persistent than currently anticipated.

We agree with Staff that the fiscal policy response was timely and helped in minimising the negative effects of the pandemic on economic activity. The recent fiscal packages adopted (American Rescue Plan) and proposed (American Jobs and Families Plans) are an ambitious and coherent set of initiatives, with much sound analytical underpinning. Multi-year investments to upgrade infrastructure and fill social welfare gaps have a potentially high pay-off, while measures to reduce social exclusion, broaden educational access and improve childcare can have large positive impacts (a more detailed discussion on the fiscal multipliers underlying Staff's analysis would have been useful). In addition, an increase in public investment should also contribute to reducing the emission-intensity of US growth. We agree with Staff that effective targeting should also be an important consideration. For example, a closer targeting of these policies to lower income groups could be associated with a stronger growth impact. While the fiscal policy response provided important tailwinds for the recovery, the impact on the debt-to-GDP ratio has been significant. As also suggested by Staff, attention should be paid to the medium-term fiscal impacts of demographic change and healthcare costs, as well as to the high sensitivity of debt trajectories to growth and interest rates.

Given that the US, like other economies, is facing multiple transitions (recovery from pandemic, green, digital, demographic), we welcome the Staff focus on structural measures proposed by the new administration and stress that implementation will be key. We agree with Staff that a range of flanking measures will be needed beyond higher public investment to ensure that these transitions are successfully managed. In addition, complex, multi-annual programmes that involve multiple domains require careful implementation and policy coordination to ensure the prospective benefits are realized. We welcome and fully support the Staff conclusion that trade restrictions and tariff increases should be rolled back and the rules-based multilateral trading system be strengthened.

We concur with Staff that the Federal Reserve's actions have been highly effective in addressing the crisis and supporting the recovery. The Federal Reserve's new monetary policy framework adopted last year leaves it with sufficient flexibility to support the recovery and deal with any increase in inflationary pressures. We share Staff's views that managing the transition towards withdrawing monetary accommodation will require very careful communication. The effective functioning of core markets for the transmission of monetary policy, notably the Treasury market, is essential and we welcome Staff's attention to relevant issues in that respect and would see room for additional analysis.

While financial stability risks currently do not seem to be exceptionally high, vulnerabilities have increased, calling for close monitoring of developments. Strong fiscal and monetary policy support have bolstered corporate and household balance sheets and supported financial stability at the current juncture. However, loose financial conditions have also encouraged risk taking, increased leverage and asset valuations. As policy support is withdrawn, increased delinquencies could adversely impact banks' balance sheets, and some highly leveraged corporate balance sheets could come under pressure. Therefore, we agree with Staff that such developments, and the related financial stability risks, should be monitored carefully.

United States—Staff Report for the 2021 Article IV Consultation
Responses to Technical Questions Posed by Executive Directors in Advance of
EBM/21/74—July 19, 2021

Staff's responses to technical questions are below.

Macroeconomic Outlook

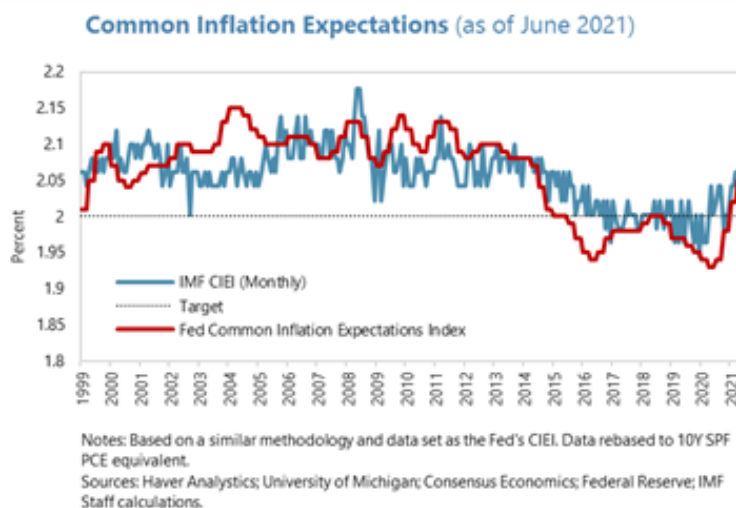
- 1. The scenario of a rapid pick-up in inflation that could be systemic for both the U.S. and the global economy could have a likelihood higher than a “tail event”. Staff’s comments would be appreciated.**
 - Staff considers a sustained pickup in inflation to be unlikely. However, given the range of uncertainties it is difficult to assess, quantitatively, how far out in the “tail” this risk is. Inflation expectations continue to be well-anchored, there is sizable remaining slack (around 10 million jobs would have to be created to return the employment-population ratio to the pre-pandemic level), and data consistently shows a very flat trade-off between slack and PCE inflation. These factors will weigh against a sustained rise in underlying inflation.
 - It is worth noting also that fiscal policy will tighten substantially in 2022 (even if the proposed Jobs and Families Plans are passed into law) which will weigh against wage and price inflation (although it is expected to be offset by a drawdown in private savings and a strong return of private demand).
 - Given the importance of the inflation risk for the US and world economy, it will need to be continually scrutinized and assessed (especially over the remainder of this year when it will be difficult to get a clear reading from inflation data due to the ongoing realignment in a range of relative prices).
- 2. What is staff’s reading of the most recent inflation numbers, showing y/y growth of 4.5 percent for core inflation? How much more can the core CPI increase from the June level in the second half of 2021 to be in line with staff’s forecast for the year as a whole?**
- 3. We just saw and felt the U.S. inflation running at a 13-year high in June. Could the inflation trend last longer than “transitory,” and would the Fed raise the policy rates sooner and faster than expected? Staff’s comments are welcome.**
 - Core CPI inflation in the second quarter (q/q, non-annualized) was about 0.15 percentage points higher than the projection contained in the Article IV staff report. Around half of the

inflation in June (and the full amount of the amount by which second quarter inflation exceeded staff forecasts) can be attributed to price increases in used motor vehicles. In addition, supply-demand mismatches in leisure and travel (rental cars, hotel accommodation, airline tickets) are pushing prices up. Median CPI, however, has moved by far less (2.2 percent y/y in June) indicating the degree to which core and headline inflation is being driven by large movements in a relatively small subset of prices.

- Despite this modestly higher CPI inflation, staff continue to expect core PCE inflation to be around 4 percent by the end of the year. Relative price movements are likely to feed through during the remainder of this year. By 2022Q1, sequential core PCE inflation is expected to fall back to around 2 percent (q/q annualized). There is, though, significant uncertainty both in mapping CPI changes into PCE as well as in the future prospects for the ongoing shifts in relative prices.

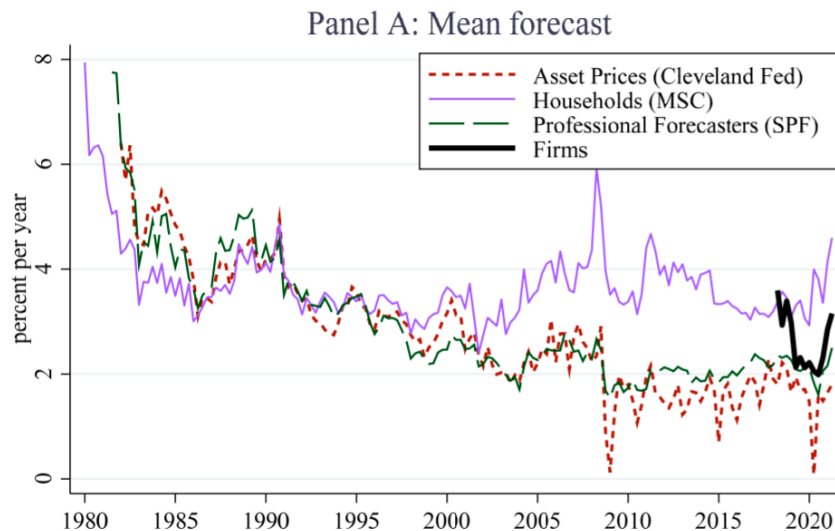
4. The strong credibility of the monetary framework will serve as an anchor to maintain inflationary expectations. In this regard, can staff comment on recent developments in medium-term inflationary expectations?

- Medium term inflation expectations remain relatively stable. Market-based measures have increased modestly this year, with five-year inflation expectations implied from Treasury Inflation-Protected Securities (TIPS) at around 2.5 percent since March 2021 (note TIPS price expected headline CPI inflation, not PCE inflation which is how the Federal Reserve's longer run 2 percent goal is framed). Consumer surveys of inflation expectations (University of Michigan) show that five-year inflation expectations have been around 2¾ percent during 2021, compared with 2½ percent in 2020. The 2021Q2 reading of the Federal Reserve's Common Index of Inflation Expectations, a useful measure that encompasses a number of indicators of inflation expectations projected onto PCE, shows inflation expectations to be stable at 2.05 percent.



5. Staff highlighted that “there is significant uncertainty about how inflation expectations are formed in the US”. Staff’s further comments on this topic are welcomed.
6. In light of this, could staff elaborate on any work they are planning to further explore the drivers of inflation expectations and associated risks?
- A series of academic papers shows that firms and consumers are largely inattentive to inflation and to signals from monetary policy.¹
 - The evidence suggests firms typically predict inflation that is significantly different from the Federal Reserve’s inflation target of 2 percent but they are uncertain about their inflation forecasts. Inflation expectations are often specific to the industry of the firm.
 - Consumers over-rely on price changes of goods in their personal grocery bundles when forming expectations about aggregate inflation.
 - Inflation expectations of professional forecasters and financial markets participants are highly correlated and appear to be more well-anchored and less volatile.

Figure 1. One-Year-Ahead Inflation Expectations for Different Agents.



Source: Candia, Coibion, Gorodnichenko (2021)

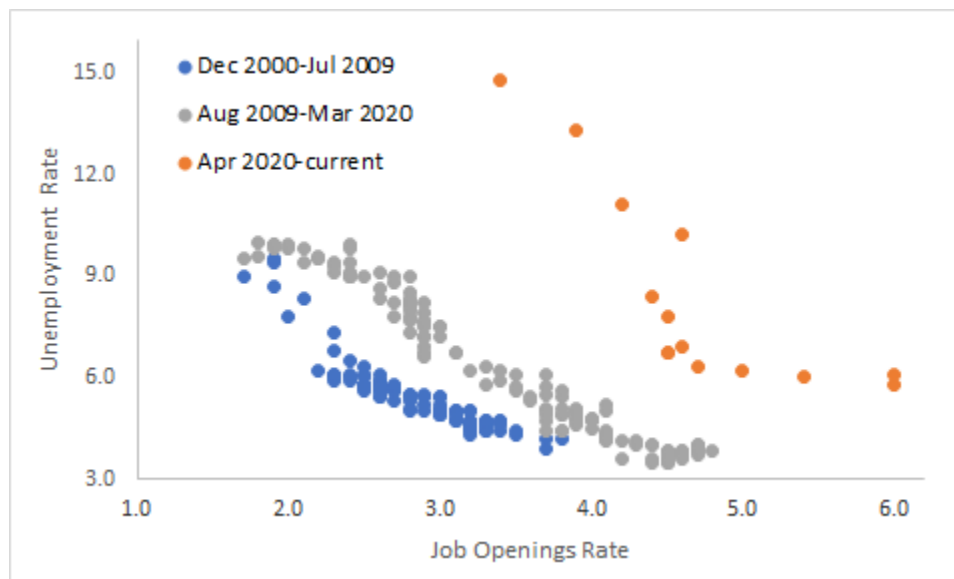
7. We note that potential GDP has been revised upward, in the short run, which tends to mechanically reduce the assessment of an overheating. Overall, we think however

¹ See for example https://eml.berkeley.edu/~ygorodni/CCG_SoFIE.pdf ; <https://eml.berkeley.edu/~ygorodni/CGR.pdf>; <https://www.nber.org/papers/w9796>; https://faculty.chicagobooth.edu/~media/faculty/michael-weber/shopping_inflation.pdf

that the impact of the proposed fiscal packages on potential GDP might be lower than what is currently suggested. Could staff comment on these revisions?

- 8. Can staff elaborate on the assessment regarding the effect of the American Jobs and Families plans on the potential growth of the US economy?**
 - In the short run, the increase in the level of potential GDP reflects: (i) the lifting of constraints on the utilization of capital and labor arising from the COVID-19 related lockdown and prevention measures; (ii) less-than-expected corporate bankruptcies and business failures (which reduces hysteresis and ensures the capital stock remains deployed in production). The resulting near-term increase in potential output implies a complete unwind of the reduction in potential GDP (of about 3 percent) arising from the effects of the pandemic.
 - Over a longer horizon, potential output is boosted by the provisions of the Jobs and Families Plans. A range of research studies underline the importance of childcare support, universal pre-school and more generous earned-income tax credit in supporting higher labor force participation, particularly for women, minorities, and lower income workers. The demand effects from the fiscal packages will also help tighten labor markets, increase wages, and further incentivize participation. These labor market effects will be complemented by improvements in labor productivity arising from investments in physical infrastructure, access to tertiary education, and basic research and development. At a 10-year horizon, the level of potential output is expected to be 1 percent higher as a result of the Jobs and Families Plans.
 - The estimation of potential output and the output gap is subject to a high degree of uncertainty. As a result, in assessing the degree of slack in the economy, staff relies more on examining labor market prospects. To restore the pre-pandemic level of the employment-population ratio would require the net creation of around 10 million jobs. This suggests that substantial slack remains in the economy. There are uncertainties, however, on the lasting impact of health concerns and the recent increased rates of retirement on labor force participation. Despite this, the economy looks set to return to full employment sometime during the course of 2022.
- 9. Further comments of the ongoing dynamics in the labor market would be welcome, as labor shortages in some sectors coexist with a still low participation rate.**
- 10. Could staff elaborate on why they consider the mismatch in the labor market transitory, including what they see as the main drivers behind the inelastic labor supply? Does staff consider that fiscal measures could be better calibrated to incentivize a return to the labor market? Has there been any signs that labor markets recover more rapidly in states that have ended expanded unemployment insurance?**

- The lack of movement in labor force participation rate since mid-2020 likely reflects the ongoing health concerns, the need for workers to provide child and family care, the increase in household buffers as a result of federal transfers as well as rent and mortgage moratoria, and the potential disincentive effects of the enhanced unemployment benefits. It is difficult to disentangle these various factors.
- There may also be some matching frictions at play as workers rotate between sectors and also geographically. As one indication of these structural changes, the U.S. Beveridge curve shows a significant shift since March 2020 (much larger than the shift that occurred following the global financial crisis).
- The factors hampering labor force participation should subside, as the vaccination program makes further progress, schools and childcare reopen, and the pandemic-related unemployment benefits programs expire. Labor market matching process may also improve as hiring can be conducted in person and a tighter labor market raises wages. There is not yet data available to judge the impact of some states discontinuing the expanded unemployment insurance.
- In terms of policy design, the supplemental benefit could have been designed differently with an embedded automatic stabilizer whereby the generosity of the supplement declines as the unemployment rate falls and/or as vaccination coverage expands (rather than expiring in September 2021).



- 11. Could staff comment on the impact of [a minimum wage increase] on the two most pressing issues in the US labor market, i.e. the very large share of long-term unemployed and the strongly over-proportional unemployment share among the young and the African-American community?**

- An increase in the federal minimum wage would help mitigate poverty and ensure that the benefits of an expanded earned income tax credit are incident on the working poor, and not the employer.
- A higher minimum wage changes would particularly benefit the young, women, and minorities who are over-represented among lower income workers. As shown in Figure 2 of the staff report, in about 20 states half or more of full-time workers that earn below US\$15 are minorities (African Americans, Hispanic and others).
- However, a minimum wage of US\$15 (which would also apply to tipped workers) could have significant employment effects in some states. The Congressional Budget Office's estimates that 1.4 million jobs could be lost from a US\$15 minimum wage (although the uncertainty bounds on this estimate are very wide). A US\$15 minimum wage would imply the minimum wage will exceed 50 percent of the median wage ratio in almost all states and exceed 70 percent of the median wage in 10 states. Comparing to OECD countries, the U.S. would move from having one of the lowest minimum wages (as a share of the median wage) in the OECD to one of the highest. The literature is ambiguous on the likely size of the employment effects when the minimum wage encompasses such a large share of the workforce. Also, there is little empirical literature on the impact of a expanding the minimum wage to tipped workers. The uncertainty surrounding the employment effect is especially large in the current circumstances when the labor market for lower skilled, lower income workers is in the midst of repairing from the pandemic, especially for those sectors like restaurants and leisure that have a relatively high share of tipped workers.

Fiscal Policies

- 12. Could staff please elaborate on how they assess the precise calibration of the planned additional fiscal support and on the balance of the related risks (in terms of both likelihood and impact)?**
 - 13. Given these debates are ongoing does the Fund have a view on the relative economic importance of the “hard” infrastructure investment versus the “social” infrastructure investment?**
 - 14. Does staff have an estimate of the impact on US growth under a different (or reduced) fiscal and revenue package?**
 - 15. We would appreciate knowing to what extent staff's growth projections would be altered if the infrastructure, including the “human” infrastructure does not make through the legislative process.**
- Staff estimates that, combined, the American Jobs and Families Plans would add 5¼ percent, cumulatively, to the level of GDP over the 2022-24 period. The American Jobs

Plan, which contains the proposed physical infrastructure investment, would add around 3¼ percent to the level of GDP over the 2022-24 period. The American Families Plan, which mostly contains the “human infrastructure” components, will add 2 percent to the level of GDP over the 2022-24 period. Detailed effects are shown in Figure 1 of the staff report.

- Undertaking a different package of measures would change the estimated effects but outcomes would depend very much on the composition of the revenue and spending sides of the package. To analyze the output effects, the measures under the American Jobs Plan are allocated into four categories: new capital projects, maintenance, R&D and others. Similarly, provisions of the American Families Plan are categorized as targeted transfers to households, untargeted transfers to households, tertiary education, government consumption. Finally, tax measures are split into increases in the corporate tax burden, taxes on high-income households, and improvements in tax administration. Multipliers are attached to each type of measure drawn from median estimates in the empirical and theoretical literature. Forecasts assume that the spending plan will be executed over multiple years, in line with the timing outlined in the President’s Budget and both demand and supply effects will take time to build. The macro forecasts build-in the effects of a steady withdrawal in monetary support (with policy rates starting to rise at end-2022).
- It is worth noting that the effects of the proposed fiscal measures are highly uncertain. Staff forecasts were informed by separate exercises to simulate the fiscal packages using the Fund’s G20MOD and the Federal Reserve’s SIGMA model. These effects were shown in the staff report (Box 4) and highlight the significant uncertainty around the size and timing of the macro effects.

16. Staff’s comments on whether there are specific structural, institutional impediments that inhibit better policy-targeting, and whether there are lessons to be learned for future crisis responses, is welcomed.

17. From a political economy point of view, [the authorities’ decision not to raise taxes on households earning under US\$ 400,000] could be a pragmatic policy decision to gather broad support, considering that 98 percent of households in the U.S. would be below that threshold. Wouldn’t that be more efficient than the alternatives explained here, in terms of achieving the overall outcome?

- The greatest impediment to a more targeted fiscal package appears to be linked to political dynamics and the garnering of sufficient support in Congress for the legislation.
- The administration has committed not to raise taxes on any household earning less than US\$400,000. This constrains the consideration of a range of alternative or additional fiscal measures (including a phase out at a lower income level of the child tax credit, increases in

fuel taxes, introduction of a federal carbon tax, eliminating regressive deductions and simplifying the personal income tax).

- There are also institutional impediments to better targeting. For example, the state-level unemployment insurance systems exclude the self-employed and gig workers. Also, the computer systems for administering unemployment insurance at the state level are often antiquated and do not lend themselves to a more targeted design of benefits (e.g. targeting a particular replacement rate for the individual rather than providing a lump-sum supplement which can push the replacement rate above 100 percent for lower income households).

18. Could staff comment on the downside risks to the US' fiscal balance and public debt trajectories if the necessary reforms cannot be achieved?

- A smaller spending package could in the end be legislated which would lead to a less steep accumulation of debt. On the other hand, some of the proposed revenue measures may not be supported in Congress which would increase the deficit and result in a faster rise in the debt-GDP ratio.
- However, for a broad range of potential different size and composition of the fiscal legislation, the debt-GDP will continue to rise over the medium-term, driven by demographic changes. The U.S. has fiscal space to absorb this rising debt path so there is time to adjust the trajectory of the debt over the medium-term through the types of revenue and spending changes suggested in paragraph 35 of the staff report.

19. Could staff comment on various measures taken by the authorities to facilitate the accumulation of human capital and participation in the labor force? (Mr. Tanaka, Ms. Kashima, and Ms. Ogihara)

- A range of measures have been legislated (under the CARES Act, the Consolidated Appropriations Act of 2021 and the American Rescue Plan) to support the reopening of childcare facilities, to fund school districts, and support the retention of workers (e.g. through the Paycheck Protection Program and employee retention tax credit).
- The American Jobs and Families Plan proposes substantial increases in childcare and elderly care support, universal pre-school, two years of free community college, support for low-income students attending four-year colleges, an enhanced earned income tax credit (which should encourage work for low-income individuals without children), expanded health insurance coverage and health insurance premium subsidies, and paid family leave. A range of research studies underline the importance of the above measures in supporting human capital accumulation and higher labor force participation, particularly for women, minorities, and lower income workers.

20. In footnote 13 staff seem to characterize the “IMF Board-approved” definition of public debt sustainability as a novelty, while in fact it has been present in this form ever since the first staff papers on debt sustainability was published as early as 2002. Staff’s comments are welcome.

- In the past, the U.S. Article IV assessed debt to be unsustainable *under current policies* (i.e. that debt-GDP continues to rise throughout the medium-term due to population aging). Footnote 13 aims to clarify the distinction. However, staff have always judged that there is a feasible set of policies that would reduce the debt-GDP ratio over time. In each Article IV, staff has specifically recommended such a set of tax and spending policies that would restore a downward path for the debt-GDP ratio and has shown the debt path under those alternate set of policies.

21. Has staff done any updated model simulations on optimal fiscal stimulus to account for changes in assumptions as regards, for example output gap, multipliers, or interest rates?

- Staff have not updated the optimal fiscal stimulus assessment from the 2020 Article IV. The economic outturn for 2020 was better than staff expected during the 2020 Article IV, the vaccination progress in 2021 has been faster, and the authorities also introduced additional fiscal stimulus in the Consolidated Appropriation Act and the American Rescue Plan. This suggests that there is little remaining justification for further “stimulus” to return the economy more quickly to full employment to mitigate the effects of hysteresis.
- The proposed American Jobs Plan and American Families Plan, however, are viewed more as supply-side reforms (even though they will also provide near-term demand stimulus). As such, the motivations are different from the optimal stimulus calculations in the 2020 Article IV.

22. We would appreciate staff’s comments on the economic sectors that would be most impacted by this [global] minimum tax on corporations.

- Many large U.S. headquartered multinationals, in a range of different sectors, pay a very low (or zero) effective tax rate. These companies take advantage of various provisions built into the U.S. tax code to reduce their tax burden (e.g. accelerated depreciation, preferential tax treatment of stock options, tax breaks for R&D or renewable energy investments, the tax advantaged use of debt-financing). U.S. companies also pursue various profit shifting techniques—largely, but not exclusively, linked to moving their intellectual property to low tax jurisdictions—so as to reduce their tax obligations. The global minimum tax would curtail the ability of companies to pursue such strategies (with the largest impact likely on companies most reliant on intellectual property).

23. We would appreciate staff's insight whether the recent agreement on global corporate taxation will create a level-playing field between the foreseen higher statutory rates of the corporate taxation and taxation of large multinational enterprises. We wonder about the possible impacts on incentivizing debt financing and whether they would lead to changes in intersectoral or interregional investment decisions?

- The Fund has long supported a global minimum corporate tax to reduce incentives for base erosion and profit shifting. Given the size of the U.S. economy and its domestic market, the U.S. can likely sustain a higher statutory corporate income tax rate than the global minimum without creating meaningful incentives to relocate the headquarters of U.S. corporations (since location decisions go well beyond tax considerations). The proposed tax reform also contains provisions that would further disincentivize "inversions".
- Nonetheless, the overall impact of proposed changes on regional, international, or sectoral allocations of capital are difficult to predict with any accuracy. It is clear, though, that a global minimum tax will lessen the incentives to relocate activities and intellectual property to low tax jurisdictions.
- The higher statutory rate would increase the incentives to debt finance (since the interest would be deductible at a higher marginal rate). Also, the intention to increase the dividends and capital gains tax levied at the individual level will further increase incentives to debt finance projects (rather than using equity finance).

24. In this regard, we would welcome staff views on the potential adverse effects of the proposed global minimum tax on offshore profits of U.S. multinationals, as well as the proposed measures to incentivize onshoring of jobs back to the U.S., especially on operations and investments in emerging markets and developing countries.

- The global minimum tax, by reducing the scope for profit shifting, will increase the tax burden on U.S. corporations, particularly on mobile intellectual property. However, insofar as the profits derived from such intangible investments are "rents" (rather than normal returns to capital) this higher tax rate should not significantly dissuade new investments.
- The U.S. Treasury "green book" proposes a tax credit equal to 10 percent of the eligible expenses paid or incurred in connection with onshoring a U.S. trade or business. The expenses paid or incurred would be limited to those associated with the actual relocation of the trade or business and would not include capital expenditures or costs for severance pay. As such, this is likely to provide an only limited benefit to firms that relocate activities back to the U.S.

25. We note that the staff has suggested raising tax revenues by increasing the reliance on indirect taxes. Could the staff comment on the merit of this suggestion as indirect taxes are considered regressive with adverse impact, particularly on the poor?

- As noted in paragraph 35 of the staff report, an increase in indirect taxes would have to also ensure the effects on lower income groups are offset through increases in targeted assistance (e.g. by increasing food assistance programs, refundable child tax credits, and the EITC).

Monetary Policy

26. Could staff kindly provide its assessment on how to best balance the current [monetary] policy stance with this discussion [of asset purchases] and recent inflation numbers, against the backdrop of the global rise of the COVID-19 delta variant?

- The ongoing rapid pace of recovery and expectations of additional fiscal support will necessitate an eventual shift in monetary policy. Staff forecast that asset purchases will be scaled back in early 2022 and policy rates will be increased starting in late 2022 or early 2023. However, policies will need to be data dependent and be framed in terms of progress to the Fed's longer run goals.
- A worsening of the pandemic, due to the COVID-19 Delta variant, presents a risk to the outlook as discussed in paragraph 27 of the staff report. However, the relatively high rate of vaccination among the vulnerable population should limit hospitalizations and deaths. This will reduce the need for containment measures, mitigating the macroeconomic impact of another surge in cases. There is a more problematic downside if existing vaccines become ineffective against a new variant. This would lead to a rise in mortality and have more serious consequences for activity.

27. Could staff comment on the risks attached to [markets misunderstanding the new monetary policy framework of the Federal Reserve]?

- The new monetary policy framework of the Federal Reserve seems well understood by financial markets. There is important uncertainty though on the path for inflation and employment in the coming months. Data releases, therefore, could lead to volatility in the US\$ yield curve and other market pricing.
- The market's longer term inflation expectations appear to be anchored at a level that is consistent with the longer-run goals of the Federal Reserve (although there have been shifts in market pricing, potentially linked to shifts in risk premia). If anything, the new framework appears to have more-strongly anchored longer run inflation expectations at 2 percent.
- In any case, continued clear communications and an early telegraphing of changing path for policies will help avoid market volatility and undue shifts in financial conditions.

28. Could staff comment on whether the Fund will recommend [flexible average inflation targeting] approach to other advanced economy central banks?

- Staff have consistently recommended in the U.S. case that it would be beneficial to allow some overshooting of their inflation targets, after periods of below-target inflation. This should help the economy return to full employment after an adverse shock and reduce the risk of labor market scarring and a persistent increase in income inequality. The arguments would seem to carry through to other central banks with strong independence and credibility (although the Fund makes these assessments on a case-by-case basis).
- Staff are not recommending using monetary policy to explicitly target a reduction in inequality. Rather, an overshooting framework such as flexible average inflation targeting is beneficial from a macro perspective *and* has the advantage of also helping to address income inequality since it results in a deferral of the normalization of policy and allows the central bank to run the labor market hotter, prolonging the expansion and helping to increase the wages of lower income workers (which appears to occur at the later stages of the expansion). However, by the same token, such monetary accommodation may well increase wealth inequalities (by loosening financial conditions and raising asset prices which is largely incident on wealthier households).

29. Is the Fed's future trajectory of monetary policy the same as staff's baseline scenario projection? Staff's comments are welcome.

- The Fed's future trajectory is data dependent. The path of policy rates expected by the median of FOMC participants in June had two rate increases by end-2023. Staff forecasts anticipate one additional rate increase by end-2023. 8 of the 18 participants expect rates to be either at or above staff forecast for the federal funds rate by end-2023.

Trade

30. In this context, we were wondering whether the IMF's external sector assessment is used as an input for a Section 301 investigation?

- The External Sector Assessment is not used in the Section 301 investigation. U.S. Treasury has its own methodology to determine currency undervaluation which the Department of Commerce takes into account in making its assessment.

Financial Stability

31. Are there reasonable prospects for greater liquidity buffers for non-bank market participants to mitigate the need for official liquidity support in the future?

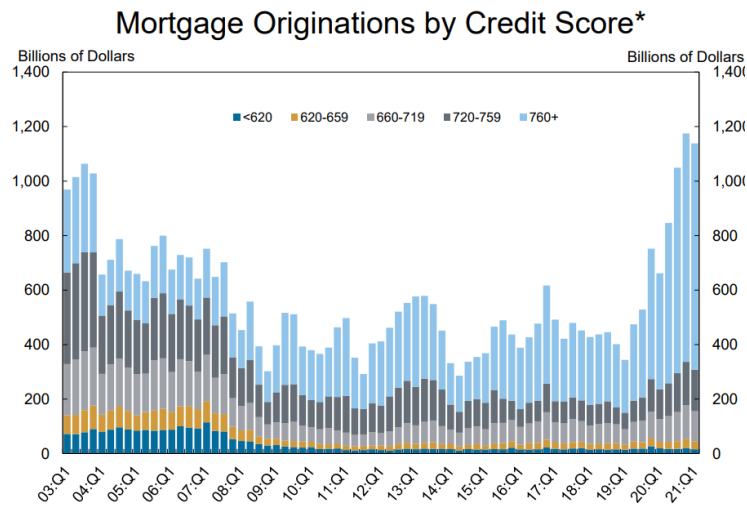
- Addressing structural vulnerabilities and strengthening liquidity buffers for non-bank financial institutions is high on the authorities' agenda. The President's Working Group Report from December 2020 lays out several options for money market funds including more binding (and possibly countercyclical) liquid asset requirements, pre-determined arrangements that lock-in a proportion of an investor's shares for a minimum amount of time, use of in-kind redemptions to meet withdrawals by institutional investors, swing pricing, and requirements that would temporarily gate outflows under certain conditions. On March 31, 2021, Chairperson Yellen asked for an interagency assessment to determine if additional measures should be taken to address financial stability risks associated with open-ended funds (focusing on liquidity risks), and if so, to develop recommendations for the Financial Stability Oversight Council.

32. Which FSAP recommendations would respond most directly to the vulnerabilities exposed by the pandemic?

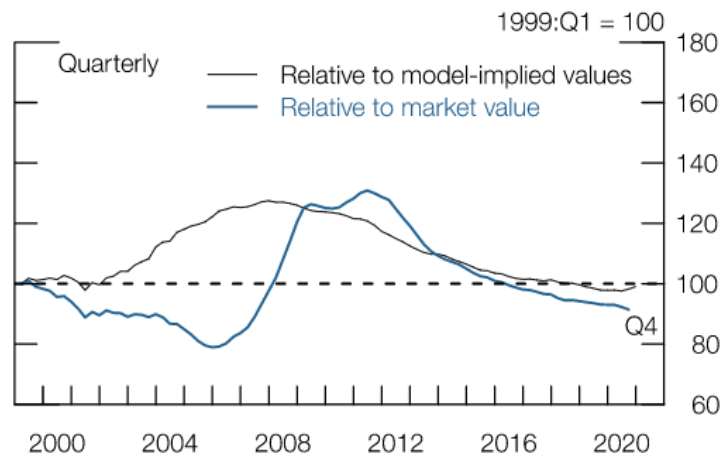
- The FSAP outlined several steps to mitigate vulnerabilities in the nonbank sector. These include developing macroprudential tools for, and increasing buffers in, nonbanks. The FSAP also recommended moving all retail prime, institutional government, and tax-exempt money market funds to a floating net asset value. The FSAP also argued for liquidity stress tests of funds to ensure that operations can continue effectively in a tail-risk scenario.

33. Regarding developments in the mortgage market, can staff elaborate on the potential risks given the rapid increase in house prices? Has any recent analysis been done by staff using the house-prices-at-risk methodology? What macroprudential measures are the authorities implementing to deal with potential risks in the housing market?

- Despite the rapid increase in house prices, risks appear to be relatively contained. Recent mortgage origination is predominately in the high credit score segment (see chart) and credit scores of new mortgages have been improving. The decline in interest rates has made mortgage payments more affordable and the rebound in the labor market (combined with steps to temporarily defer mortgage payments during the pandemic) has lessened the risk of delinquencies. Housing leverage is also at relatively low levels as high rates of household saving have been used, in part, to repay debt.
- The U.S. has in place regulatory requirements aimed at preventing borrowers from over-extending themselves. The Ability-to-Repay and Qualified Mortgage Rule dissuade lenders from originating loans to borrowers with high debt-to-Income ratios. Defusco et al. (2020 in the Review of Economic Studies) show that this regulation has succeeded in reducing household leverage.



2-13. Estimates of Housing Leverage



34. Could the staff comment on the measures taken or envisaged to mitigate the risks arising from rise in hedge fund leverage?

- Hedge funds entered 2020 with higher than historical leverage. Although there was significant deleveraging during the COVID-induced market turbulence, some very large funds continue to have high leverage and are highly interconnected with financial markets and banks.
- Macroprudential tools for non-bank financial institutions are limited but risks can be mitigated by applying stress tests to hedge funds and improving data coverage to understand their interconnections within the financial system.

- Secretary Yellen has re-established the FSOC's hedge fund working group to better share data, identify risks, and work with other agencies to strengthen oversight.

35. Could staff provide an order of magnitude of potential future bankruptcies and zombie firms? Is there a risk that these bankruptcies would not be smoothly managed?

36. How does staff assess the vulnerabilities in the corporate sector now, as compared to before the pandemic?

- As noted in paragraph 4 of the staff report, some corporate failures are expected but this is expected to resemble a protracted process of resource reallocation rather than a damaging surge in corporate failures.
- At the time of the 2020 Article IV, a corporate stress testing exercise projected that 15 percent of non-energy, non-investment grade debt would face financial distress in 2020. However, stronger growth outturns and the large-scale policy support have resulted in only 2.5 percent of non-energy, non-investment grade debt ending up in default. It seems likely that bankruptcies will look more like the normal churn of business failures, perhaps with higher incidence of failures in certain sectors where technology is proving particularly disruptive (e.g., retail) or in some leisure sectors where the effects of the pandemic are more lasting.
- Banks expect losses from defaults to be moderate. Banks did build up relatively large loan loss provisions during the pandemic to cover loan defaults by struggling business and households. However, more recently these provisions are being partially reversed amidst reduced concerns about bankruptcies.

Climate Change

37. What would be the price per ton of GHG emissions required to reach the net zero emissions target by 2050?

38. We missed the bottom-line assessment of whether the authorities' current/announced policies will ultimately be sufficient to meet their Paris climate commitments. Staff comments are welcome.

- The level of the price of carbon necessary to achieve the United States' Nationally Determined Contributions is highly dependent on other policies that are put in place including the level and type of spending to facilitate emission goals as well as the regulatory environment (e.g. the level of carbon pricing needed to achieve zero emissions in the power sector will be highly dependent on whether, or not, it is complemented with a clear energy standard for the sector or a cap-and-trade system for power generators).

- There is a great deal of uncertainty on the extent to which the U.S. will need to rely on carbon pricing given that many of the steps that will be needed to achieve the administration's climate goals have yet to be defined.
- The staff report includes various different quantitative scenarios. In Box 7, analysis shows that even relatively low carbon prices have a large marginal effect on emissions. The model simulation finds that front-loaded subsidies (to both R&D and to the production of clean energy), combined with a carbon tax (that starts at only US\$12 per ton of CO₂ and gradually rises to around US\$72 by 2050), would achieve the administration's targeted reduction in emissions. Box 10 highlights the importance of prioritizing emissions reduction in the power sector (intensive decarbonization, where fossil fuel power generation is phased out by 2035, provides the best path to achieve the administration's climate goals).
- During the consultation, discussions with specialist NGOs, think tanks and consultancies highlighted the difficulty of measuring the emissions mitigation trade-offs among a range of different policies and how important will be the interconnections between various policies.

39. In the spirit of mainstreaming climate into the Fund's macro surveillance work, have staff assessed the macroeconomic impacts of the climate elements of the American Rescue Plan and the American Families and Jobs Plans?

- The American Rescue Plan consisted mainly of transfers (to households, unemployed, schools and universities, and states/other government) and therefore limited climate elements.
- The American Jobs Plan includes significant green investments that – if legislated by Congress – would have a direct impact on U.S. emissions. The administration is pursuing spending of around US\$750bn on electricity infrastructure and green energy, R&D for climate technology, public transports, and more energy efficient public buildings. An additional USD 70bn are planned for adaptation measures (focusing on environmental remediation and infrastructure resilience).
- The effects of the American Families and Jobs Plans have been incorporated into staff's macroeconomic framework.
- The staff report also includes several simulations of macroeconomic effects of different climate policies. Box 7 shows the effects of different carbon pricing and subsidy policies on consumption as well as debt-to-GDP. Box 10 offers a simulation of different decarbonization scenarios and their effects on real GDP and employment.

Health

40. We would like ask staff to elaborate on staff's recommendations regarding the medical sector on efficiency innovations, price transparency, market approaches for

healthcare providers, and drug pricing, including their future prospects and fiscal implications.

- The analysis performed by staff indicates that increases in market power in the healthcare sector have contributed to price increases in the healthcare sector. For this reason, efforts to apply anti-trust laws and to curb oligopolistic behavior would help. Also, having an agency responsible for monitoring and oversight of healthcare markets could have beneficial effects to increase competition and market innovation.
- Price transparency that provides consumers with accurate and timely information about price, quality, costs, and provider networks can help them make better choices and make markets more competitive and could also help increase efficiency innovations. Some progress was made on pricing transparency during the last administration, requiring hospitals to post prices for the various services they provide.
- Drug prices are not the main contributor to the overall high cost of US healthcare. However, there is price discrimination in the U.S. drug market and the U.S. typically pays more for a range of medications than other advanced economies. Increased competition in the sector and some changes to patent laws (e.g., rules that allow existing drugs whose patents are expiring to be combined and the combination to be re-patented) could help put downward pressure on drug prices and ease the fiscal burden.

CONSTITUENCY CODES

OEDAE

Angola, Botswana, Burundi, Eritrea, Eswatini, Ethiopia, The Gambia, Kenya, Lesotho, Liberia, Malawi, Mozambique, Namibia, Nigeria, Sierra Leone, Somalia, South Africa, South Sudan, Sudan, Tanzania, Uganda, Zambia, and Zimbabwe

OEDAF

Benin, Burkina Faso, Cameroon, Central African Republic, Chad, Comoros, Democratic Republic of Congo, Republic of Congo, Côte d'Ivoire, Djibouti, Equatorial Guinea, Gabon, Guinea, Guinea Bissau, Madagascar, Mali, Mauritania, Mauritius, Niger, Rwanda, São Tomé & Príncipe, Senegal, Togo

OEDAG

Argentina, Bolivia, Chile, Paraguay, Peru, and Uruguay

OEDAP

Australia, Kiribati, Korea, Marshall Islands, Federated States of Micronesia, Mongolia, Nauru, New Zealand, Palau, Papua New Guinea, Samoa, Seychelles, Solomon Islands, Tuvalu, and Vanuatu

OEDBR

Brazil, Cabo Verde, Dominican Republic, Ecuador, Guyana, Haiti, Nicaragua, Panama, Suriname, Timor-Leste, and Trinidad and Tobago

OEDCC

China

OEDCE

Colombia, Costa Rica, El Salvador, Guatemala, Honduras, Mexico, and Spain

OEDCO

Antigua and Barbuda, The Bahamas, Barbados, Belize, Canada, Dominica, Grenada, Ireland, Jamaica, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines

OEDEC

Austria, Belarus, Czech Republic, Hungary, Kosovo, Slovak Republic, Slovenia, and Turkey

OEDFF

France

OEDGR

Germany

OEDIN

Bangladesh, Bhutan, India, and Sri Lanka

OEDIT

Albania, Greece, Italy, Malta, Portugal, and San Marino

OEDJA

Japan

OEDMD

Afghanistan, Algeria, Ghana, Islamic Republic of Iran, Libya, Morocco, Pakistan, and Tunisia

OEDMI

Bahrain, Egypt, Iraq, Jordan, Kuwait, Lebanon, Maldives, Oman, Qatar, United Arab Emirates, and Yemen

OEDNE

Andorra, Armenia, Belgium, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Georgia, Israel, Luxembourg, Moldova, Montenegro, Netherlands, Republic of North Macedonia, Romania, and Ukraine

OEDNO

Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway, and Sweden

OEDRU

Russian Federation and Syrian Arab Republic

OEDSA

Saudi Arabia

OEDST

Brunei Darussalam, Cambodia, Fiji, Indonesia, Lao People's Democratic Republic, Malaysia, Myanmar, Nepal, Philippines, Singapore, Thailand, Tonga, and Vietnam

OEDSZ

Azerbaijan, Kazakhstan, Kyrgyz Republic, Poland, Serbia, Switzerland, Tajikistan, Turkmenistan, and Uzbekistan

OEDUK

United Kingdom

OEDUS

United States