September 29, 2021
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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 19/53-1

9:00 a.m., June 21, 2019

1. United States—2019 Article IV Consultation

Documents: SM/19/139 and Correction 1; and Correction 2; and Supplement 1 ; and Supplement 1, Correction 1

Staff: Chalk. WHD; Leigh, WHD; Haksar, SPR

Length: 2 hours, 1 minute

Executive Board Attendance

C. Lagarde, Acting Chair

Executive Directors	Alternate Executive Directors
D. Mahlinza (AE)	
M. Raghani (AF)	
G. Lopetegui (AG)	
N. Ray (AP)	
A. Tombini (BR)	
Z. Jin (CC)	
L. Villar (CE)	
L. Levonian (CO)	
	C. Just (EC)
H. de Villeroché (FF)	
S. Meyer (GR)	
	M. Siriwardana (IN)
D. Fanizza (IT)	
M. Kaizuka (JA)	
J. Mojarrad (MD)	
	W. Abdelati (MI), Temporary
	N. Jost (NE), Temporary
T. Ostros (NO)	
	L. Palei (RU)
M. Mouminah (SA)	
A. Mahasandana (ST)	
	P. Trabinski (SZ)
S. Riach (UK)	
	P. Pollard (US), Temporary

J. Lin, Secretary
O. Vongthieres, Summing Up Officer
V. Sola, Board Operations Officer
M. McKenzie, Verbatim Reporting Officer

Also Present
Communications Department: R. Elnagar, M. Henriquez, W. Murray, P. Wang. European Central Bank: K. Nikolaou, R. Rueffer. Independent Evaluation Office: L. de Las Casas Perez de Orueta, C. Rustomjee. Legal Department: K. Christopherson Puh, S. Dawe, C. El Khoury, G. Rosenberg. Middle East and Central Asia Department: P. Barrett. Monetary and Capital Markets Department: M. Erbenova, D. King, F. Wendt. Secretary's Department:

P. Cirillo, J. Lin. Strategy, Policy, and Review Department: R. Cartaxo Mano, D. Cerdeiro, P. Garcia Martinez, V. Haksar, V. Klyuev, N. Meads, E. Van Heuvelen. Western Hemisphere Department: Y. Abdih, C. Caceres Lievano, N. Chalk, E. Kopp, D. Leigh, S. Tambunlertchai, P. Williams. Executive Director: A. Mozhin (RU). Alternate Executive Director: R. Alkhareif (SA), J. Di Tata (AG), A. Guerra (CE), N. Heo (AP), A. McKiernan (CO), P. Moreno (CE), K. Obiora (AE), M. Psalidopoulos (IT), H. Razafindramanana (AF), D. Ronicle (UK), P. Rozan (FF), B. Saraiva (BR), J. Sigurgeirsson (NO), K.Tan (ST). Senior Advisors to Executive Directors: Z. Abenoja (ST), M. Alle (AF), A. Muslimin (ST), M. Choueiri (MI), S. Evjen (NO), K. Karjanlahti (NO), S. Keshava (SA), Y.Liu (CC), O. Odonye (AE), J. Shin (AP), F. Spadafora (IT), A. Tivane (AE), G. Vasishtha (CO), J.Weil (CO), C. Williams (CO). Advisors to Executive Directors: A. Abdullahi (AE), M. Albert (FF), D. Andreicut (UK), A. Arevalo Arroyo (CE), K. Badsi (MD), S. Bah (AF), S. Buetzer (GR), X. Cai (CC), D. Crane (US), P. Dhillon (IN), J. Essuvi (AE), D. Fadhel (MI), J. Garang (AE), U. Latu (ST), M. Merhi (MI), M. Mulas (CE), L. Nankunda (AF), A. Park (AP), A. Srisongkram (ST), A. Urbanowska (SZ), D. Vogel (AG), S. Yoe (ST), S. Alavi (MD), F. Antunes (BR), K. Hennings (BR), K. Lok (CC), J. Montero (CE), A. Tola (SZ).

1. UNITED STATES—2019 ARTICLE IV CONSULTATION

Mr. Rosen, Ms. Pollard and Ms. Crane submitted the following statement:

The U.S. economy remains robust, entering its longest expansion on record and with encouraging trends in labor force participation, productivity and wage growth, notably for the lowest earners. Real GDP grew 3.1 percent in Q1 2019, well above private forecasts, with growth well supported by accelerating private investment, and by our tax and regulatory relief policies. In April 2019, the U.S. unemployment rate reached a 49-year low of 3.6 percent, where it remained in May. Importantly, the Administration's policies have drawn workers back into the labor force in numbers that have helped offset downward pressure from population aging and supported a downward trend in poverty, which is nearing its historic low. Consistently solid productivity gains—including annualized productivity growth of 3.4 percent in Q1 2019—have driven real wage gains. Real average hourly wages grew 1.4 percent in the year to April 2019. Headline PCE inflation, the basis of the Federal Reserve's inflation objective, rose 1.5 percent in the year to April 2019. Measures of consumer and business sentiment remain strong, indicating continued favorable economic prospects.

In this context, we thank staff and management for the constructive engagement with our authorities during the Article IV consultation. We value the IMF's surveillance role and the opportunity to discuss our economic policy priorities and reflect on staff's recommendations. We broadly agree with staff on the importance of translating economic growth into improved social outcomes, of remaining vigilant about financial stability risks, and of bending the curve of our public debt over time. We take note that IMF staff find the Federal Reserve's monetary policy to be appropriate at this juncture. We would like to elaborate on our perspective on these issues, including how our current policies are making inroads on key challenges, and areas where we see things differently from staff.

Economic Outlook. We appreciate IMF staff's recognition of the current strength of the U.S. economic expansion, but we are more optimistic than staff about the prospects for our tax and regulatory reforms to support growth in the coming years. We believe that latent productivity in the U.S. economy is considerably higher, previously held back by the deep slack of the Great Recession, an uncompetitive tax code, and costly regulation. We have now considerably reduced those drags. Moreover, the Administration expects that its policies to encourage work—such as reforms to social programs, strengthening skills training, and supporting greater labor mobility— could support faster growth in the labor supply and productivity. Taken together, these policies will boost real economic growth to about 3 percent annually this year and over the medium term.

Staff's analysis of the tax reform misses important prospective supply side effects. Staff argues that increased U.S. investment to date can be largely explained by demand-side effects, and posits that supply side effects from tax reform may have been blunted by rising corporate market power. The Administration believes that with regulations related to the tax reform still being finalized, the investment-enhancing impact of the reform is only in its initial stage. We expect continued strength in investment over time, rather than the near-term fading expected by staff. We are also more optimistic about the lasting impact of continuous efforts to reduce the regulatory burden on the private sector.

Fiscal Sustainability. We recognize the long-term challenge of addressing our public debt and the Administration is approaching the issue on two fronts. First, our supply-side reforms will durably raise potential growth which will improve our debt-GDP dynamics. Second, the Administration's planned reduction in non-defense discretionary spending, combined with healthcare and welfare reforms, will help stabilize public debt levels over the medium term and return the primary balance to a modest surplus position by 2024. Given continued low global interest rates and high U.S. GDP growth, we believe this has been an opportune time to create space for bold reforms to spur investment and private sector growth, avoiding the trap of a "new normal" of low GDP growth in the aftermath of the Great Recession.

Social Outcomes. The Administration is focused on ensuring that the U.S. economy is working well for all Americans. We acknowledge the past trend of rising income inequality, while noting that technological innovation and globalization make this a challenge across advanced economies. We see stronger wage growth and increased labor force participation as fundamental to improving welfare and inclusion. Importantly, lower income employees are seeing faster wage growth than high-income earners—nominal wage growth for the lowest decile has grown faster than median wages for the past two years. In addition, the recent tax reform included provisions to support low-income workers and families, including an expanded Child Tax Credit and retention of the Earned Income Tax Credit. We are encouraged by recent trends in the supplemental poverty rate, which has declined from its post-Great Recession peak of 16.1 percent in 2011 to 13.9 percent in 2017, while real median household income has been on an upward trend in recent years.

Our social welfare policies are focused on sensible reforms to move able-bodied individuals from welfare to work, and to focus the social safety net on those who need it most—the elderly, children and the disabled. We agree with staff that paid family leave and more access to quality child-care would better support working parents and the Administration has made proposals in its budget presentation to Congress. We also agree that healthcare inflation needs to be tackled, and the Administration has proposed policies to address the rise in drug costs in particular, to make inroads in this area. Some other Administration priorities in line with recommendations from IMF staff are skills training including formal apprenticeship programs and investments in science, technology, engineering, and math (STEM) education programs.

We agree with the IMF that opioid abuse remains a major concern, and we appreciate the acknowledgement of federal, state, and local efforts in the Managing Director's press remarks. The Administration is working aggressively to combat the opioid crisis. Since declaring a public health emergency in 2017, our authorities have been pursuing a strategy comprised of the following elements: (1) improving access to treatment and recovery services; (2) promoting use of overdose-reversing drugs; (3) strengthening our understanding of the epidemic through better public health surveillance; (4) providing support for cutting edge research on pain and addiction; and (5) advancing better practices for pain management. We agree with staff that scaling up successful local level programs could be a promising way forward, and note that the Administration is seeking to use federal programs to drive progress forward.

External Sector and Trade. The U.S. current account deficit has been in the range of 2–2.5 percent of GDP in recent years, as services and income surpluses partially offset a larger deficit in traded goods. The evolution of the current account balance over the medium term will depend on global demand for U.S. exports and the strength of the U.S. economy, including the continuing effect of the recent tax reform measures on U.S. competitiveness.

The fundamental goal of our trade policies is to achieve free and fair trade globally. The Administration's focus is on addressing unfair trade practices around the world that are impeding stronger and more balanced U.S. and global growth. To achieve balanced and fair trade, we must address the significant imbalances in global trade that stem in part from unfair trade policies and high trade barriers abroad. The President's trade policies will set the stage for long-term economic growth, not only in the United States, but globally.

The Administration places high priority on securing Congressional passage of the United States-Mexico-Canada (USMCA) Trade Agreement, which will modernize these important trading relationships and promote growth throughout North America.

Monetary Policy. Our monetary authorities have stated that they will continue to execute U.S. monetary policy in a data-dependent manner, putting a premium on clear communication. In March 2019, the FOMC announced additional information on its plans for balance sheet normalization. Specifically, beginning in May, the Federal Reserve slowed the pace at which it is gradually reducing its holdings of Treasury securities, and the process of reducing the size of its balance sheet will conclude by the end of September. The Federal Reserve will continue to shift the composition of its balance sheet away from agency debt and mortgage-backed securities consistent with its longer run goal of primarily holding Treasury securities.

We recognize the importance of ensuring clear communication by the Federal Reserve, but IMF staff's suggestions in this area may not help. In recent years, we have seen that the median projections from the Summary of Economic Projections (SEP) can be misinterpreted as a firm plan for policy, despite policymakers' communications to the contrary. However, we are not convinced that publishing a consensus forecast in a quarterly monetary policy report would remedy this problem. In fact, such a report could reinforce this misinterpretation, even if the report highlights risks around a central scenario. In our view, the minutes of the FOMC meetings, including the SEP materials, already provide a great deal of information about the outlook and the attendant risks and uncertainties.

We appreciate staff's positive findings on the timeliness of the Federal Reserve's ongoing review of its monetary policy strategy, but question staff's recommendation on the operating framework. IMF staff call for "a more holistic picture" of the evolution of the operating framework, but most of the key decisions about the operating framework have already been announced, and the remaining technical details may not be of importance to the broader public.

Financial Stability. We view financial stability risks as moderate and believe that our financial regulatory and supervisory institutions are responding appropriately to the evolution of risks. We agree with staff that U.S. banks are well capitalized and asset quality is generally good. We would not characterize financial conditions as being extremely loose, however.

While term premia are near record lows, the spreads for a range of assets do not appear to us to be unusually narrow, nor is the VIX unusually low—particularly when using a longer time horizon than the past five years for comparison. The fundamental backdrop for the credit market is favorable and, while issuance of leveraged loans has grown, interest coverage ratios are generally in line with long-term trends and default rates remain quite low. Investor appetite for leveraged loans is within historical measures and shows no evidence of concentration issues. From our perspective, the post-crisis period has been marked by a gradual return to normal levels of risk appetite after the record level of risk aversion in the financial crisis period.

Nor do we believe that the tailoring changes made in recent years have inappropriately weakened standards. Recent tailoring of financial regulations has focused on better calibrating risk and compliance burden, especially for smaller, non-systemic financial institutions without diminishing the safety and soundness of the financial system. We believe that appropriately calibrated regulation is not mutually exclusive, nor inconsistent, with a prospering economy. The U.S. reforms maintain the key post-crisis reform efforts adopted for the largest and most complex banks: strengthened capital standards, robust supervisory regime –stress tests, stronger liquidity requirements, resolution planning, and a range of other enhanced prudential standards. The Federal Reserve's stress testing (DFAST and CCAR) scenarios have been extremely tough in recent years, with several banks being forced to revise their capital plans.

We have made important steps to build resilience in non-banks and have seen improved liquidity risk management in funds. The SEC introduced new liquidity requirements in 2016 and stress testing for money market mutual funds as part of its 2014 money market mutual fund reforms. IMF staff's recommendation that all asset managers be subject to liquidity provisions and stress testing is inconsistent with the aforementioned reforms and the business model of investment advisers, which generally act as agents and not as principals.

While there are concerns in the leveraged loan market, there are also mitigating factors, including the reduction of liquidity risks by the long lock-up periods of collateralized loan obligations (CLOs), significantly longer tenors compared to pre-crisis levels, and higher percentage of proportion of equity tranches for CLOs than pre-crisis. The Financial Stability Oversight Council (FSOC) has also provided an institutional mechanism to address the issue and coordinate among Council member agencies with supervisory or regulatory responsibilities, which continue to monitor the potential effects of developments in the leveraged lending market on their respective regulated entities and markets. The Federal Reserve, Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency review and assess risk in leveraged lending, as well as other lending types, through their Shared National Credit (SNC) Program.

Moreover, the FSOC has issued proposed interpretive guidance that would prioritize an activities-based approach to addressing systemic risks to financial stability arising from nonbank financial companies rather than entity-based designations, using the latter only if identified risks cannot be appropriately addressed through an activities-based approach. Such an approach should more holistically address risks to financial stability and minimize the potential for competitive distortions in financial markets.

The bottom line is that the U.S. financial system is clearly stronger and much better positioned to withstand a shock or an economic downturn than it was before the crisis and that proposed regulatory reforms maintain the core protections for resilience in our banking and financial system. We look forward to more in-depth engagement with staff on financial sector issues through the Financial Stability Assessment Program (FSAP) for the United States, which is already underway.

Anti-Corruption. We value the IMF's work on governance and anti-corruption and welcome the IMF's analysis of the supply side of corruption in advanced economies, including the United States. We agree with staff on the importance of keeping the proceeds of foreign corruption out of the U.S. economy. We would underscore U.S. prosecutorial efforts and the use of sanctions designations and corruption-related advisories to communicate corruption-related risks and obligations to financial institutions, government, and non-governmental organizations. The Administration remains committed to working with Congress on legislation to strengthen the collection of beneficial ownership information.

Mr. Ostros and Mr. Evjen submitted the following statement:

We thank staff for another excellent report on the U.S economy. We are again impressed by the independent and candid analysis and policy advice. We also thank Mr. Rosen, Ms. Pollard, and Ms. Crane for the informative buff statement. We broadly agree with staff's appraisal and policy recommendations and would like to offer the following comments for emphasis.

We recognize the strength of the U.S. economy which is still growing above potential and in its longest expansion in recorded history. We positively note that an average of 2 million jobs per year have been created over the course of the expansion since 2009. Real wages are rising, including at the lower end of the income distribution.

Despite the strong macroeconomic performance, the benefits from the long expansion have not been shared as widely as they could. We note that income and wealth inequality have increased, poverty remains high, social mobility has eroded, and education and health outcomes are discouraging. Addressing these challenges by supply-side measures would facilitate more inclusive growth, raise the potential of the economy, and help achieve fiscal sustainability. Unless measures are taken, we are concerned we will see a missed opportunity for the U.S to address the medium- and longer-term imbalances and challenges that weigh on its economic outlook.

On fiscal policy, we share staff's view that the U.S. public debt is on an unsustainable path. We note that the estimated fiscal costs of the Tax cuts and Jobs Act have risen significantly from the time of approval and that evidence suggests that businesses have either saved or distributed to shareholders much of the tax windfall. We highlight the need for the U.S. to adopt measures on both the revenue and expenditure sides to ensure that public finances are on a sustainable path over the longer-term. We agree that there is a menu of policy options to address the unsustainability and encourage the authorities to explore the measures proposed by staff (in paragraph 26 of the report), for example increasing the federal revenues by putting in place a broad-based carbon tax, a higher federal gas tax, containing healthcare cost inflation, and front-loading the planned increase in the retirement age. The set of policies should allow the debt-to-GDP ratio to fall, create fiscal space to support low- and middle-income households, and address social inequalities.

We agree that further increases in the federal funds rate should be deferred until there are greater signs of wage or price inflation. We found the box on hysteresis very interesting – suggesting that an accommodative monetary policy at a late stage in the expansion may have positive long-run supply-side benefits. However, with growth above potential and presumably little slack in the labor market, capacity constraints and wage growth obviously need to be monitored closely. Accelerating inflation further ahead will require policy rates to rise faster than currently anticipated, in turn causing volatility and tighter financial conditions which may weaken growth prospects both in the U.S. and globally.

On financial stability, we strongly support staff's call for enhancing the current risk-based approach to regulation, supervision, and resolution. We agree that the medium-term risks to financial stability have risen. Corporate leverage is historically high, commercial NPLs are rising, risk premia are low, asset valuations rich, and financial conditions are loose. We note staff's view that there has been little institutional response to counter the growing risk. On the contrary, the recent tailoring of financial regulation has led to a steady easing of regulatory constraints. Hence, the financial regulation and oversight may seem to be going in the wrong direction. We also note that the buff statement has a different and more positive view on the recent tailoring of financial regulations. Could staff be more specific on what kind of institutional response they would have preferred to see in order to counter the growing risks to financial stability?

We also want to reiterate the need to strengthen regulation and supervisory oversight of nonbanks and to address data blind spots that impede a full understanding of financial system risks. We look forward to the FSAP for the U.S. which we assume will look more deeply into these issues.

We fully support staff's recommendation for the U.S. and its trading partners to work constructively towards ensuring a more open, more stable, and rules-based international trading system. It is imperative that the trade tensions between the U.S. and China are quickly resolved through a comprehensive agreement that strengthens the international system. We stress that trade barriers are harmful for global trade and ineffective in reducing bilateral trade imbalances. Rather the pro-cyclical U.S. fiscal policy is contributing to a weaker current account and thereby conducive to widening global imbalances.

Mr. Tombini, Mr. Saraiva and Mr. Antunes submitted the following statement:

We thank staff for the detailed and insightful report. We also thank Mr. Rosen, Ms. Pollard and Ms. Crane for the useful statement. The United States' economy continues on a strong growth trajectory. Early signs that the ongoing economic cycle could be close to exhaustion were offset by the more accommodative stance adopted by the Fed since January 2019, which added to lasting effects of the expansionary fiscal policy. While continued growth in the U.S. has positive spillovers for the world economy, rising risks need to be closely monitored, especially as the space for counter-cyclical monetary and fiscal policies in the event of a sudden reversal of economic conditions is limited.

The booming economic activity offers a renewed opportunity to address pressing social challenges. The ongoing growth cycle is the longest in the history of the United States, with the economy operating close to full employment for several years. Unemployment rates are remarkably low, real wages have been rising and forecasts indicate continued economic growth over the following years, albeit at a more modest pace. We take note that the authorities diverge from staff's projections and envisage a more optimistic medium-term scenario, expecting growth to remain at or above 3 percent. That notwithstanding, ten years of continuous growth delivered disappointing social results, ranging from declining life expectancy to persisting poverty, stagnant socioeconomic mobility and wealth and income polarization. We encourage the authorities to carefully consider policies to address pressing social demands, while ensuring continuous fiscal sustainability.

Fiscal policy has been the mainstay of economic expansion more recently, with significant impacts both on the demand and the supply sides. The key role played by the Tax Cuts and Jobs Act (TCJA) in fostering the current growth momentum is beyond dispute. Nevertheless, the medium and long-run fiscal consequences of the TCJA remain unclear. While staff takes a cautious stance in relation to the supply-side effects of the TCJA, the authorities underscore the sizeable productive energy that has been released by the more business-friendly tax system. Such divergent views on the potential growth of the U.S. economy over the medium term are at the root of the discrepant analysis of debt sustainability. Under a baseline scenario, grounded on current laws, staff's analysis clearly asserts that the current debt path is unsustainable. However, the impact of the TCJA may prove to be long-lasting, structurally improving competitiveness and boosting investments. As the DSA shows, a one percentage point difference in growth sustained over time would go a long way in determining the sustainability of the public debt.

Fed's change in stance was instrumental to create a more supportive growth environment both in the U.S. and worldwide, but financial stability risks are rising. Risks stem more immediately from the overleveraged corporate sector, whose debt has grown under deteriorating underwriting standards. Short-term risk of a reversal in financial conditions seem small at this point. Its effects, however, could be significant, unleashing perverse real sector-financial-fiscal dynamics. Continuous monitoring and improvement of prudential regulation and supervision, in line with a skillful macroeconomic management, will be crucial to mitigate financial risks over the medium term. For the countries that have been benefitting from the positive spillover of these more supportive conditions, the opportunity should be seized to enhance resilience and build buffers.

Persistent low inflation after the long economic expansion challenges analysts and policy makers, hence we welcome the Fed review of its monetary policy framework and look forward to staff's assessment of its results. As neutral interest rates have declined markedly, there is a real risk that monetary policy may lose traction in future recessions due to the challenges posed by the effective lower bound. Therefore, we welcome the Fed's ongoing "Review of Monetary Policy Strategy, Tools, and Communications". Even modest changes in the strategic approach to monetary policy may be highly consequential both in the U.S. and abroad, given the dollar's role as international reserve currency. Clarity regarding the strategy and the tools employed by the Fed to deliver on its institutional mandate is crucial, since eventual framework updates may have a meaningful impact on shaping market behavior along the cycle. In particular, the possible adoption of "makeup" strategies, with a view to accommodate temporary inflation overshooting within a long-term inflation horizon, requires careful and transparent communication. Could staff assess the systemic effects of the changes being considered by the Fed in the context of the monetary policy framework review?

Contrary to expectations, strong economic activity did not result in a further deterioration in the U.S.' external position. Current account deficits have steadily hovered slightly above 2 percent of GDP, despite booming domestic demand induced by the expansionary fiscal policy. This unanticipated outcome derives mainly from the substantial gains in productivity in shale gas and oil production, which have turned the U.S. into the world's largest producer of oil and natural gas. Indeed, the U.S. is set to become a net exporter of petroleum products in the near future, with momentous effects on the external sector and the baseline conditions of the international energy market as a whole. Nevertheless, staff still sees the possibility of rising external imbalances, as trade and current account deficits are expected to widen over the next few years. Given the unparalleled size of the U.S. economy, efficiently correcting for imbalances, if they become unsustainable, may require a global approach, with a concerted effort by key economies in re-equilibrating their savings-investment balance.

The United States has an irreplaceable role in promoting a rules-based international trade system. Given its size and leadership, the U.S. has been determinant in shaping the contemporary international trade framework. Its continuous commitment to the core principles of the World Trade Organization is paramount for a functional world economy. The aggregate benefits of a well-functioning, rules-based international trade system are well established in the economic literature. Accordingly, we second staff's calls for the U.S. and its trading partners to engage in constructive dialogue to strengthen the international trade system and correct emerging distortions.

Mr. Doornbosch and Mr. Jost submitted the following statement:

We thank staff for the comprehensive set of papers and Mr. Rosen, Ms. Pollard, and Ms. Crane for their informative buff statement. We welcome the very strong economic developments in the United States, including impressive developments on the labor market. Unemployment is at record lows and an average of 2 million jobs were created annually in recent years. We broadly agree with staff's assessment on the near-term economic outlook and the identified downside risks. We remain concerned about procyclical and unsustainable fiscal policies and believe that rising inequalities should be addressed. A strained political economy environment seems to render decision-making more difficult, including in the field of fiscal policy.

Despite the continued impressive economic performance, including strong private sector growth, fiscal indicators point to unsustainable fiscal policies, which remain of concern. High debt levels, a persistent structural primary deficit–compounded by pro-cyclical fiscal policy–add to these sustainability concerns. Given the US' central role in the global economy and international financial markets, this policy position not only poses risks to the US but could impact the membership more broadly, should these risks materialize. We encourage the authorities to take appropriate measures, as fiscal room for maneuver is slowly melting away. Accumulation of public debt also raises questions regarding intergenerational equity in America. We appreciate that Mr. Rosen, Ms. Pollard, and Ms. Crane's statement acknowledges challenges in this context. Regarding staff's recommendation on public finances (i) we would be interested to hear whether staff sees consolidation options on the expenditure side, as the recommendations in paragraph 26 seem to focus mostly on revenue side measures. (ii) Could staff elaborate what 'chained inflation' refers to? What is the indexation base? On a different note, this year's Government shutdown illustrates the challenging political economy the United States is currently facing. Does staff believe that such occurrences have a long term, structural, impact on the economy? Finally, we would have welcomed a somewhat more granular analysis of the labor market, including on participation rates and alternative measures of labor underutilization.

Given the robust economic developments, we believe that there is an economic case for more pronounced investment in human capital and public infrastructure. In order to ensure the US economy's competitiveness and resilience going forward, we believe that public resources should be used to prepare for future challenges, including those ensuing from technological change. Investment in infrastructure –including but not limited to transportation– should be pursued. We welcome the authorities' ongoing commitment to doing so. Growing inequalities, reduced social mobility and weak educational outcomes are likely to hamper productivity, competitiveness and potential growth. In this sense, we agree with the trust of staff's assessment that investment in human capital remains necessary. Well-designed educational policies can contribute to a successful adjustment of the US labor force to global trends and pressures. There is no doubt that US universities and US companies remain among the most innovative and successful and continue to attract human capital from across the globe. At the same time, and while not directly linked, we believe that more could be done to improve educational outcomes in society more broadly. In addition to economic upsides, we believe that sharing economic successes both within and across generations is desirable from an equity perspective. While we acknowledge political economy barriers in the present context, on both the state and federal levels, we are of the opinion that the federal government has a role to play in providing resources aimed at improving human capital and public infrastructure, not least because it can have a strong signaling effect and attract private resources at an important juncture of economic development.

We welcome staff's finding that the US financial system remains healthy – but close monitoring of risks remains warranted, in particular given the size and interconnectedness of the US financial system. We share staff's assessment of key risks faced by the financial sector, including the build-up of leverage in the corporate sector and the increasing stocks of student loans. Overall, financial stability risks for the medium-term are rising, warranting a continued prudent oversight by the authorities. In that sense, the financial oversight regime could be continuously adjusted, for instance, by further enhancing the current risk-based approach to regulation, supervision and resolution. It remains important to monitor non-banks and address potential blind spots. In this context we take positive note that many steps have already been taken regarding money market funds and repo markets. Similarly, we welcome the ongoing work to address vulnerabilities and better understand interlinkages and improve risk management. We also welcome the authorities' efforts to continue working with the FSB, BIS and other international institutions. We look forward to the conclusions of the ongoing FSAP exercise, which will be a good opportunity to discuss the US financial market and existing risks in more detail.

We support staff's view that the US should work with its trading partners towards strengthening the open, rules-based international trading system. We agree with staff that trade barriers are ineffective in addressing current account imbalances and counterproductive in terms of raising living standards. Multilateral reductions in tariff and non-tariff trade barriers bring lasting net benefits and improved aggregate macro-economic conditions. We are of the view that adverse redistributive consequences of free trade should be addressed through domestic policies, such as active labor market policy, broad access to high quality education, social safety nets and tax policy. Similarly, we endorse staff's view that addressing external imbalances also requires a policy strategy to put public debt on a downward path and taking supply-side measures to improve US competitiveness.

Mr. Ray and Ms. Preston submitted the following statement:

We thank Staff for the concise report and Mr. Rosen, Ms. Pollard and Ms. Crane for the buff statement. In the US, unemployment is at a 50-year low, real wages are at long last rising, and productivity growth seems to be recovering. We broadly agree with staff's assessment of the outlook and risks. But with U.S. macroeconomic policy seemingly needing to navigate some challenging circumstances over the next few years we would have preferred a sharper focus on these core issues in the report.

We strongly support a more open, more stable, and more transparent, rules-based international trade system and call on all parties to work constructively to address distortions. Trade tensions and policy uncertainty threaten global activity. Staff's key message is that higher tariffs and export restraints reduce both Chinese and U.S. GDP and create negative spillovers to other countries. Given this is a first order issue, we would have preferred that this was given more prominence in the report. We note the authorities stated intention to achieve a more fair, balanced, and reciprocal trading arrangement with China given their concerns around technology transfer, intellectual property rights, cyber theft, subsidy practices and market access. Staff's analysis shows that the Administration's current approach is unlikely to be successful given tariff measures are ineffective at containing bilateral trade deficits. Did staff discuss with the authorities' alternative approaches to achieving their objectives? Box 4 notes that an important step forward in the global trading system could be made if a U.S.-China trade deal is able to multilaterally eliminate some existing trade restrictions and distortionary policies. Quantification of the positive impact that such a trade deal could generate would be a useful addition to the discussion and could help with gaining traction on trade issues. Staff comments are welcome.

Looking ahead, the Federal Reserve faces a complex period that will be increasingly challenging to successfully navigate. As staff set out in the report's introduction, against the backdrop of a strong labor market, real wage increases and recovering productivity growth (and pro-cyclical fiscal policy and higher prices owing to tariff increases) – it is remarkable that inflation remains so low. Given staff advice that further increases in the policy rate should be deferred until there are clearer signs of wage or price inflation, further efforts are needed to understand stubbornly low inflation outcomes and staff's continued focus on this issue would be welcome. Given recent developments and a slowing of domestic demand growth has staff's assessment of the current stance of monetary policy changed? We are also concerned that the potential for political pressure to weigh on, or be perceived to weigh on, the Federal Reserve's independence appears to have gone unnoticed in the report.

Previous Fund advice was that pursuing procyclical fiscal policy will elevate the risks to the U.S. and global economy and that the planned expansion in the fiscal deficit should be reversed. Staff also expected that, in light of the fiscal stimulus, the Federal Reserve would need to raise policy rates at a faster pace to achieve its dual mandate. Why has the sizable fiscal stimulus not had the expected impact? Will staff update their assessment of the estimated impact of the Corporate Income Tax Cut?

Despite real GDP per capita being at an all time high, the continued decline in income mobility experienced by an increasing number of Americans is a serious concern. Indeed, the outcomes presented across the range of social indicators explored are troubling. Notwithstanding that these are important issues, we see this perhaps as a missed opportunity and would have found it helpful if staff could have quantified the negative macroeconomic consequences of these domestic policy choices, including the impact on potential GDP growth. Trusted advice deeply anchored in robust economic analysis is the Fund's comparative advantage and, in this case, could help to achieve greater traction with the authorities. In the same vein, we found specific policy advice on health and education (including from paragraph 21 onwards) puzzling. It is not clear to us that the Fund is best placed, nor has the expertise, to be giving such granular advice in these areas.

Staff's bottom line is that it is more urgent than ever to ensure that any further changes to the financial oversight regime not only preserves but enhances the current risk-based approach to regulation, supervision and resolution. We fully support this view. Staff are right to point out the need to strengthen oversight of non-banks, address continued data blind spots and carefully monitor historically high corporate debt. In this regard we welcome the authorities ongoing work to better understand interlinkages, manage vulnerabilities and improve risk management practices within financial institutions. We encourage continued efforts in these areas and look forward to a fuller discussion of these topics in the FSAP.

Lastly, we note that the Staff assessment is that the U.S. will become a net exporter of petroleum products by 2022. We understand that the authorities' view is that the US will become a net exporter by 2020. It would be helpful to understand what is driving the difference between these projections. Staff comments are welcome.

Mr. Gokarn submitted the following statement:

We thank staff for the very comprehensive and analytical report and Mr. Rosen, Ms. Pollard and Ms. Crane for their candid buff statement. We note that the buff points out a number of differences between staff appraisal and recommendations and the authorities' assessments. We broadly agree with the staff appraisal on many issues, so we would like to focus or remarks on a few issues, particularly some on which there are differences in views.

The US economy is performing very well currently, with relatively fast growth and very low unemployment and, despite this, no significant inflationary pressures. However, staff believes that this situation will not prevail, with growth moderating to below 2 percent over the five-year projection period. On the other hand, authorities argue that the current growth rate will persist because of the impact of recent policy initiatives on the economy's potential growth rate. A key factor in resolving this debate is whether investment activity increases, both in the private and public sectors. In various sections of the report, staff have identified potential deterrents to investment - fiscal constraints, trade tensions, etc. However, authorities emphasize the beneficial effects of the new corporate tax regime on corporate investment. Could staff assess the relative strengths of these two sets of factors? Is there a reasonable scenario in which investment accelerates sufficiently to support the higher growth trajectory?

On the fiscal front, staff assesses that the public debt to GDP ratio will rise from about 78 percent currently to about 84 percent five years hence. However, the federal fiscal deficit will be slightly lower than it is today, while the general government deficit will be significantly lower. Even though the increase in the debt ratio seems to be moderate, it is expected to have a significant impact on interest rates, particularly at the short end. The yield curve is projected to flatten significantly as a result, although it will remain positively sloped. Could staff provide an intuitive explanation for this development?

On monetary policy, we note staff's recommendation that the status quo on policy rates should be maintained until inflationary pressures are more apparent. While the recommendation seems to be unexceptionable, it perhaps needs to be viewed in the context of the output gap, which, the report implies, is currently positive. Keeping in mind the difference of views on the potential growth rate, could staff comment on why inflationary pressures are subdued in such an output gap scenario? Is there merit in recommending gradual increases in the policy rate proactively, both in anticipation of inflationary pressures building up and to create more policy space in the event of downside risks materializing?

With regard to financial stability, we note staff's concerns about the build-up of risks in the relatively lightly regulated segments of the financial sector and the build-up of corporate debt. Authorities have indicated their intent to strengthen regulation where it is needed, but question staff's assessment of the changes in regulations relating to banks and other relatively tightly regulated segments. The premise here is that the regulatory framework that emerged from the financial crisis has proved to be too restrictive and the buffers that, for example, banks have now built up their risk-taking capacity. Since increasing fund flows to businesses is key to sustaining growth, could staff comment on the growth vs. risk trade-offs implied by the recent regulatory changes?

On the external sector assessment, we note that the external position of the US is moderately weaker than is suggested by fundamentals and appreciate the increasing importance of energy exports in the current account. However, the main focus of the staff analysis and the accompanying working paper is the impact of tariff increases. Staff's analysis is quite unambiguous in stating that recent tariff actions will have a negative impact on all countries involved. Authorities argue that the primary objective of these actions is to induce countries that engage in unfair trade practices. While we fully accept the principle of free and fair trade, we also believe that this is best accomplished in a multilateral, rules-based framework and we therefore endorse staff's recommendation that working to improve the framework may provide a more robust and less costly solution.

On structural issues, we appreciate the rich analysis provided in the paper on a range of issues. A central theme running through several of the analytical exercises is the nature and causes of inequality. The fiscal consequences of these issues are well brought out, clearly demonstrating macro criticality. We focus on one of these issues, the entrenchment of a bimodal pattern in the labor market. This has been an emerging pattern for a while and is clearly not confined to the US. There is a clustering of jobs at relatively low wages and one at relatively high incomes, with little mobility between the two modes. What is striking in this report is the increasing incidence of college graduates in the low-wage mode, indicating that, for at least some disciplines, there are insignificant returns to an investment in college education. Against this backdrop of structural features of the labor market, staff recommendations on education and training seem reasonable, but are focused on the supply side of the labor market. It's not clear that these initiatives will address structural constraints to wage immobility. Could staff comment?

With these remarks, we wish the US authorities the best in their endeavors.

Mr. Lopetegui and Mr. Di Tata submitted the following statement:

We thank staff for the comprehensive report and Mr. Rosen, Ms. Pollard, and Ms. Crane for their insightful buff statement.

The United States should be commended for the impressive performance of its economy, which is experiencing the longest expansion in recorded U.S. history. As noted in the staff report, the damage caused by the financial crisis has been repaired, unemployment is at its lowest level in 50 years, real wages are rising driven by higher productivity growth, and inflation remains subdued. Staff projects real GDP growth at 2.6 percent in 2019, before slowing gradually to a potential rate of 1 ¾ percent over the next few years. The authorities, however, expect growth to remain at or above 3 percent over the medium term, supported by the recent tax and regulatory reforms and by the administration's policies to encourage faster growth in labor supply and productivity. Could staff elaborate further on these differences of opinion with the authorities? In particular, we would welcome staff's comments on the authorities' view that the investment-enhancing impact of the tax reform is only in its initial stage and that efforts to reduce the regulatory burden would have a strong lasting impact on growth. As a general point, despite the differences of views on some issues discussed during the consultation, we welcome the authorities' broad agreement with staff on the importance of translating economic growth into improved social outcomes, remaining vigilant about financial stability risks, and reducing the public debt over time, as expressed in the buff statement.

Both staff and the authorities recognize the important challenge of addressing public debt sustainability. However, this is a policy area where there are differences of opinion, with the authorities putting greater emphasis on the impact of supply-side reforms on reducing the federal government deficit by raising potential growth. In this regard, in light of the uncertainty about the ultimate effect of supply-side reforms, we tend to agree with the more cautious approach recommended by staff, which relies on gradually strengthening the primary fiscal position. The administration plans to reduce non-defense discretionary spending, in combination with healthcare and welfare reforms, to help stabilize public debt levels and return the primary balance to a modest surplus by 2024. Could staff comment on the possible characteristics of these measures and their implications for social spending and income distribution?

The benefits from the economic expansion experienced in the last decade have not been widely shared, although wages at the bottom-end of the income distribution have started to grow faster. Average life expectancy is falling, income and wealth inequality have increased, poverty has fallen but remains above levels in other advanced economies, and education and health outcomes are disappointing. We notice philosophical differences between staff and the authorities regarding the role of social welfare policies. However, we can identify several areas of agreement, including the need to provide paid home leave and broaden access to childcare; tackle healthcare inflation by addressing the rise in drug costs; aggressively combat the opioid crisis; and strengthen skills through apprenticeship programs and improved education in math and hard sciences. Other areas identified by staff that are worth considering are listed in paragraph 21 of the report. Improving educational outcomes and tempering healthcare costs constitute very important challenges.

Regarding monetary policy, we agree with the Fed's cautious approach. As noted in the report, falling inflation, anchored expectations, and continued uncertainties, among other things, argue in favor of a pause before further changes in monetary policy, a course of action that will have positive outward spillovers to other countries. Could staff discuss the reasons behind the flattening of the Phillips curve, as well as the level of the natural rate of unemployment used to calculate the unemployment gap in Box 8? Also, could staff clarify what is meant at the end of paragraph 36 by saying that "the decisions on the size of the Fed's balance sheet are technical in nature and not to be interpreted as a change in the monetary policy stance"? On a separate matter, we notice that the Treasury yield curve has inverted, which frequently constitutes a sign that markets are expecting growth difficulties down the road. Staff's comments on this issue would be welcome.

With respect to the financial sector, there is agreement between staff and the authorities that U.S. banks are well capitalized and asset quality is generally good, but that nonfinancial corporate leverage is high. In this context, staff notes that an abrupt reversal of the current accommodative financial conditions could create a significant downturn in economic activity, with negative outward spillovers. Staff also emphasizes its concern about the recent easing of financial regulations, underlying the need to ensure that any further changes in this area enhance the risk-based approach to regulation, supervision, and resolution. In addition, staff sees a need to strengthen the oversight of nonbanks. Although the authorities recognize that the issuance of leveraged loans has grown, they also note that interest coverage ratios in the corporate sector are strong and liquidity positions remain healthy. The authorities are also of the view that the recent tailoring of financial regulations has focused on recalibrating risk and reducing the compliance burden and has not inappropriately weakened regulatory standards. In addition, the authorities have indicated that important steps have already been taken to build non-bank resilience. Could staff elaborate further on these differences of views, as well as on its assertion that "little progress has been made in reforming the housing finance system or the government sponsored enterprises"? We trust that the ongoing FSAP would help clarify the risk map and could possibly narrow the differences of views between staff and the authorities.

The external current account deficit remains moderate and is explained largely by the fiscal imbalance. We take note of the assessment that the external position is moderately weaker than implied by fundamentals and desirable policies, and that the real effective exchange rate remains somewhat overvalued. We concur with staff that fiscal adjustment would reduce the U.S. external imbalance and the risk that it grows over time. However, it is important to highlight that domestic policy efforts in this direction in the U.S. need to be accompanied by demand-supportive efforts elsewhere (ideally, in excess surplus countries with appropriate policy space) to avoid downward output pressures globally. A continued improvement in the oil balance and further structural reforms to improve productivity and competitiveness will also help narrow the U.S. external imbalance. We also support the call by staff to encourage the U.S. and its trading partners to work constructively towards addressing distortions in the global trading system and avoid relying on welfare-deteriorating tariffs. Could staff comment on the timeline for approval of the U.S.-Mexico-Canada Agreement (USMCA)?

We recognize the U.S. prosecutorial efforts and the use of sanctions and corruption-related advisories to communicate corruption-related risks and obligations to financial institutions, governments, and non-governmental organizations. In particular, we would like to acknowledge the cooperation provided by the U.S. authorities to Argentina, including through the Argentina-United States Dialogue on Illicit Finance and investigations of high-profile corruption cases. Looking forward, we encourage the authorities to continue working with Congress on legislation to strengthen the collection of beneficial ownership information and to better address money laundering risks in high-end real estate.

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

Mr. Meyer and Mr. Buetzer submitted the following statement:

We thank staff for its comprehensive and insightful report and broadly concur with the appraisal. We also thank Mr. Rosen, Ms. Pollard, and Ms. Crane for their buff statement. The U.S. economy has experienced almost a decade of expansion and the unemployment rate has declined to historic lows. At the same time, it is worth noting that pro-cyclical fiscal stimulus has played a crucial role in the strength of recent GDP growth. With fiscal effects fading, we share staff's outlook of a weaker expansionary GDP path over the medium term. Overall, downside risks have substantially increased. Financial risks may materialize and trade conflicts could escalate further.

We share staff's concern about the sustainability of the U.S. fiscal position. Recent tax cuts and increased spending will continue to negatively affect public finances on top of rising expenditure needs due to population aging. In our view, staff could have discussed the challenge of substantial pension liabilities, that several U.S. states face, in greater detail. According to staff calculations, a gradual increase of the federal government primary balance to about 1¾ percent of GDP (or 1 percent for the general government) would be needed to put the debt-to-GDP ratio on a downward path.

In this context, we appreciate staff's valuable list of recommendations for sustained medium-term fiscal consolidation, including inter alia measures to put the social security and health systems on sounder footing. We want to emphasize that structural reforms focusing on the increase of potential growth, such as improving the public infrastructure or a skills-based immigration system, would also facilitate fiscal consolidation.

Regarding the budgetary process, bipartisan cooperation on the sustainability of the federal fiscal framework as proposed by staff would be highly valuable. Specifically, the replacement of the existing debt ceiling with a medium-term fiscal objective would likely help to reduce risks stemming from politically induced uncertainty that weigh on the U.S. outlook.

We share staff's concerns that the business tax provisions of the TCJA have so far fallen short of expectations in lifting business investment, suggesting that their impact on potential growth could be materially less than initially projected. We also agree with staff that a significant portion of the benefits from the corporate tax cuts actually seem to have been channeled to share buybacks and dividend payments.

The Federal Reserve has managed the process of monetary policy normalization carefully. We acknowledge staff's concern that increases in policy rates at this stage bear the risk of triggering an abrupt tightening of financial conditions, which could damage growth and employment prospects. However, we have confidence in the Fed's ability to balance potential risks to economic growth and inflation carefully. Furthermore, we would be more cautious in advising the Fed to allow for some (temporary) overshooting of its inflation target.

We share staff's view that the Fed's data dependence approach and clear, forward-looking communication is vital to avoid negative external spillovers through abrupt revaluations of asset prices. In this respect, we appreciate the Fed's decision to conduct a press conference after every FOMC meeting as of 2019 to further increase transparency. The Fed's ongoing review of its monetary policy strategy, its tools, and its communication is an important process given the likelihood of downside economic risks and the asymmetries imposed by the effective lower bound in future economic downturns. We agree with staff that greater clarity with regard to the expected evolution of the operating monetary policy framework would be valuable.

We broadly agree with staff's assessment that the U.S. financial system is relatively healthy, but that medium-term risks to financial stability are increasing, which also implies increased risks of outward spillovers. In particular, we want to emphasize the risks associated with the historically high level of corporate leverage and with the loosening of lending standards. In this respect, risks stemming from the leveraged loan market should be carefully monitored. Most of the new corporate debt issuance has the lowest investment grade rating (BBB), which poses a significant risk in the event of downgrades in a future recession. Against this backdrop, we agree with staff that the FSOC should continue its efforts to respond to emerging threats to financial stability. In this respect, it would be beneficial to strengthen the resources of the Office of Financial Research.

Furthermore, we stress the importance that the U.S. maintains its engagement in developing the international financial regulatory architecture and remains committed to agreed international standards. While the tailoring of regulatory requirements for banks according to their size and risk profile can be reasonable, it is important to maintain a robust financial regulatory regime as well as a level-playing field for domestic and foreign institutions. Moreover, we are in concordance with staff that the oversight of nonbanks needs strengthening, that greater headway in reforming the housing finance system would be desirable, and that continuing data blind spots should be addressed.

According to the external sector assessment, staff expects the U.S. current account deficit to rise over the next years against the background of a strong economy and the fiscal stimulus. Moreover, this deficit would be appreciably higher, were it not for the U.S. increased reliance on domestic oil and natural gas production.

Addressing the current account deficit by tariff hikes will most likely have detrimental effects to both the U.S. and the world economy. Higher tariffs would lead to higher costs of imported goods, lower the purchasing power of households, and distort the market allocation of resources. We agree with staff that supply-side policies – e.g. improving the public infrastructure or the outcome of education – are necessary to increase competitiveness and could lead to a more balanced trade position. Given the contribution of U.S. fiscal policies to global imbalances, fiscal consolidation measures would also be important in this respect.

We strongly appreciate staff's call for a joint effort to strengthen the international trade system towards a more open, more stable and more transparent rules-based framework. Overall, gains from international trade have proven to be substantial. Protectionist tendencies put at risk the achievements of globalization in the past and pose a danger to prosperity, not only in the U.S. but worldwide.

Resolving trade tensions should therefore have the highest order of priority. Further intensification of tensions needs to be avoided as these can cause significant disruptions to global value chains, to the multilateral trading system, and ultimately to the global economy as a whole.

We appreciate staff's detailed analysis of socioeconomic outcomes and indicators that show a troubling picture. As pointed out in the staff report, income and wealth distributions are increasingly polarized, poverty rates remain close to their pre-crisis level, life expectancy is declining, and social mobility is weakening. Recommendations by staff on addressing these issues, including through improving education and health care outcomes, seem suitable not only to help raise living standards for low- and middle-income households, but also to support productivity and potential growth. In particular, we support the idea of expanding apprenticeship and vocational programs.

Lastly, we welcome the voluntary assessment under the IMF's Enhanced Governance Framework on the supply and facilitation of corruption. We acknowledge the prosecutorial efforts of the authorities to tackle corruption and their commitment to further strengthen legislation in this regard, as also underscored in the buff statement by Mr. Rosen, Ms. Pollard, and Ms. Crane. We encourage the authorities to address identified weaknesses in governance and transparency frameworks.

Mr. Kaya, Mr. Just and Mr. Stradal submitted the following statement:

We thank staff for their comprehensive and candid report, and Mr. Rosen, Ms. Pollard, and Ms. Crane for their helpful buff statement. Growth in the US remains solid and the ongoing expansion is breaking the historical records with unemployment at a very low level, while the inflationary pressures are conspicuously missing. We broadly agree with the thrust of the staff appraisal.

We take note of the significant difference in the growth expectations between staff and the authorities' views expressed in the buff statement. While the former estimates the potential growth rate at around 1.75 percent, the latter expect 3 percent growth in the medium term. We are skeptical about the notion of latent productivity that was previously held back by post-recession slack, the uncompetitive tax code, and costly regulation, and will now be unleashed. The useful comparison of economic forecasts on page 6 of the Report shows that the Congressional Budget Office's and the US Federal Reserve's (Fed) growth forecasts are also closer to staff's estimate in the outer years. Such a major difference in potential output growth assumption obviously radically alters the debt sustainability calculations as it compounds.

We concur with staff that the fiscal position is not sustainable. The procyclical fiscal stimulus delivered in early 2018 heightened the urgency of fiscal consolidation. While we agree with the authorities that the current low long-term government bond yields provide an opportunity for growth enhancing investments, we are not convinced that the 2017 Tax Cuts and Jobs Act was the right vehicle to achieve this. A combination of both revenue and expenditure measures will be needed to steadily reduce the public debt ratio while creating space for infrastructure and human capital investments. In their absence, the debt ratio is set to steadily climb towards the historical highs reached in 1946. Staff offers a menu of policy options and we particularly underscore the importance of health care system reforms, as the combination of suboptimal outcomes and elevated costs points to a fundamental dysfunction of the current health care financing model.

Reforms of the budget process are long overdue. The flaws in the federal budget process have become self-evident over the past decade, with delayed federal funding and government shutdowns repeatedly dialing up uncertainty, with knock-on effects on economic activity and social outcomes. Simplification, increasing remoteness from the electoral calendar, reducing fiscal myopia, and replacing the debt ceiling with automatic adjustment rules should be the key planks of the reform.

A pause in the monetary tightening cycle seems warranted at the current juncture. The puzzle of robust growth, low unemployment, and low inflation is not unique to the US economy, and we encourage staff to continue to dig deeper in search of the underlying causes. Against the backdrop of anchored inflation expectations, the recent deceleration of core inflation, and heightened policy uncertainty, we think a wait-and-see approach is prudent. Nevertheless, the wage growth developments in the late stage of the cycle call for a continued close monitoring. We are concerned by the growing political pressures aimed at influencing the Fed's monetary policy stance and reiterate the criticality of preserving the independence of the monetary authority for maintaining macroeconomic stability. We invite staff to comment.

We welcome the ongoing review of the Fed's monetary policy strategy, tools, and communication. However, we are confounded as the buff statement states that "most of the key decisions about the operating framework have already been announced, and the remaining technical details may not be of importance to the broader public." Meanwhile, the paragraph in the Staff Report reflecting the authorities' views reads:

Officials did not want to pre-empt the broad-based assessment of monetary strategy, tools, and communications that was already underway but did expect the findings of this review to be considered by the FOMC in the latter part of this year and could lead to evolutionary changes in the framework.

Could staff comment on their understanding of the timeline of the review?

We welcome staff's finding that the financial system appears healthy, but the assessment is balanced by a note of caution that financial stability risks are on the rise. We take note of the recent tailoring of financial regulation aimed at a more risk-based calibration of oversight. Given the length of the financial cycle and the associated phenomena of stretched valuations, as well as increasingly lenient lending standards, we do not think the timing is appropriate. The overall financial stability risks, including from money laundering, continue to be difficult to assess as the supervisory and regulatory architecture remains fragmented. We look forward to the findings of the ongoing Financial Sector Assessment Program, which will hopefully shed more light on the interlinkages and risk exposures among the different segments of the complex US financial system.

Finally, we reiterate our concern that the escalation of the continuing trade conflicts between the US and its main trading partners poses one of the main risks for global economic growth. We thank staff for the Working Paper on trade wars and trade deals which provides more analytical heft to the assessment of economic costs of trade wars, the risks associated with a trading system fragmentation, and the value chain disruptions. The main findings are summarized in Box 4 of the Staff Report and normally, the in-depth analysis would be part of the report as a Selected Issues Paper. Could staff comment why they chose a different format in this case?

Mr. Kaizuka and Mr. Komura submitted the following statement:

We thank staff for the informative report and Mr. Rosen, Ms. Pollard, and Ms. Crane for their insightful statement.

We appreciate the staff's comprehensive analysis on the U.S. economy. Considering large impacts of the U.S. policy changes on the global economy, we are of the view that the staff's analysis, including spillover effects, is useful for prospecting the global economy going forward.

Overall, the U.S. needs to further enhance its potential growth while making the fruits of growth widely shared. In addition, the U.S. should avoid creating negative shocks on the own economy by heightening uncertainty of policies, for example, trade policy, as the room for maneuver of macroeconomic policies may have been narrowing due to elevated public debt level and lower natural interest rates. Reducing uncertainty of policies is also critical for stable growth of the global economy.

As we broadly concur with the thrust of the staff appraisal, we would like to offer some comments as follows:

Growth and Social Outcomes

The U.S. economy will achieve the longest expansion in recorded history in July. Staff forecasts that growth is expected to remain 2.6 percent in 2019 and moderate toward its potential rate, 1.75 percent, thereafter. Meanwhile, the U.S. administration expects that growth remains at or above 3 percent over the medium-term. Could staff comment on the reasons for this more optimistic outlook that the administration raises in the authorities' views and the buff statement?

Strong growth has been lowering unemployment rates and raised real wages, especially for lower earners. However, social indicators, including declining life expectancy which opioid abuse contributes, rising income inequality, and eroded social mobility, also highlight that challenges remain in the U.S. on how the fruits of growth could be shared widely. The U.S. needs to take necessary measures to make its strong growth more inclusive. In this regard, we broadly support staff's recommendations for supporting the poor, tempering healthcare costs, and improving primary education. In addition, we welcome that the U.S. has been working to combat opioid crisis.

Fiscal Policy

Fiscal policy should aim to put the unsustainable public debt on a downward path while increasing fiscal space for policies to promote investments in human and increase medium-term growth. To this end, we take note of the staff's estimation that primary fiscal surplus of around 1.75 percent of GDP is needed. Staff recommends the U.S. to consider federal tax measures, such as a consumption tax, a gas tax, and a carbon tax. The U.S.

administration is of the view that a reprioritization of federal spending can bring primary fiscal surplus of around 1.8 percent of GDP by 2029 without increasing in federal taxes. Future Article IV consultations should discuss specific measures, considering how much each measure would create savings, to draw a credible and concrete path for fiscal consolidation over the medium-term.

On Tax Cuts and Job Act (TCJA), we would like to highlight the following points:

While it includes many positive steps, the U.S. administration has been implementing TCJA where the U.S. economy is considered to be beyond full employment. TCJA, together with increases in spending, has been adding burdens to an already-unsustainable public debt and putting upward pressure on the current account deficits.

We note that the evidence so far indicates that business have either saved or redistributed to shareholders much of the tax windfall while the usage for capital and R&D spending has been relatively limited.

We find it interesting that increases in corporate market power may decrease the elasticity of investment to tax changes. The series of reforms included in the TCJA would not only have impacts on personal consumption and investment in the U.S., but also provoke other countries' reactions in tax rate changes, and eventually affect the global economy through trades and capital flows by altering global demand and allocation of production. We encourage staff's further analysis on quantitative spillover effects of the TCJA, with taking into account the factors above comprehensively, as data becomes available.

We agree with staff that indexing social security benefits to chained inflation would be useful to contain ageing related spending. As highlighted in the G20 Fukuoka Meeting, all countries, including U.S., would face population ageing at some point of time. Staff can enrich policy discussions on population-ageing issues by referencing practices of other countries in Article IV consultations. For example, the Japanese pension system may have some useful implications to consider specific design of indexing social security benefits to chained inflation. In particular, Japan has introduced "Macroeconomic Indexation" which automatically adjusts benefits label reflecting demographic factors since 2004 to avoid imposing an excessive burden on younger generations while to secure the appropriate benefit level and to secure fiscal sustainability.

Monetary Policy

As there exist several uncertainties in the U.S. economy, including its own trade policy, the Fed should carefully weigh the balance of potential risks to employment and inflation. In executing its monetary policy decisions, it is important to keep the principles of data dependence and clear communication as well as pay close attention to market reactions, to avoid a surge in market volatility.

Financial Sector

We note that U.S. banks are well capitalized and asset quality is generally good. In 2019, expected more accommodative stance of major central banks has rebounded asset prices and contained volatility. At the same time, accommodative financial environment also heightens vulnerabilities in leveraged corporates. The U.S. authorities should closely monitor them and avoid lowering corporate earnings and tightening financial environment by heightening uncertainty of policies, for example, trade policy.

Trade Policy and External Sector

While the U.S. has traditionally maintained a very open trade regime and has got many benefits from it, the administration has taken broad-based trade actions. These measures could not only undermine the global trading system based on the WTO rules, but also have serious negative impacts on the global economy through the increase of uncertainty for firms and market disruption by worsened investor sentiment. Moreover, these negative effects are expected to be amplified under the current multi-layered global value chain structure.

We agree on the importance of reducing market distortions and unfair trade measures, especially in emerging markets and low-income countries as the latest WEO emphasizes that there remain high trade barriers in those economies, adversely affecting global growth. Although it is necessary to rectify unfair trade measures, counter protectionist measures benefit no countries. Instead, countries, including the U.S., need to maintain and strengthen an open and rule-based multilateral trade system through ongoing WTO reforms. Furthermore, to mitigate downsides for trade-affected workers, policy efforts should focus on training, temporary income support, and job search assistance.

To mitigate trade tensions, staff should continue to deliver messages that they adversely affect the global economy, including the U.S. economy, as done in the recent G20 surveillance note. At the same time, we consider that since the U.S. well understands benefits of international trade and investments, it may also be beneficial to discuss this issue from other aspects, considering the administration being interested in forced technology transfer and weak protection and enforcement of intellectual property rights. In this context, we would like to hear how staff discussed during missions with the administration to recommend it of not taking bilateral trade actions? In addition, we would like to invite staff’s comments on the possible impacts of the effectuation of USMCA on the global and U.S. economy as well as the impacts of imposition of tariffs on imports from Mexico.

In assessing external balances, we note the importance of monitoring all components of the current account, including service trade and income balances. In the G20 Fukuoka Meeting, countries agree that in the spirit of enhancing cooperation, carefully calibrated macroeconomic and structural policies tailored to country-specific circumstances are necessary to address excessive imbalances. In this regard, we agree with staff that the U.S. external imbalance will need to be addressed through fiscal adjustment and supply side reforms.

Countervailing Duties

We agree with staff on the problems about countervailing duties proposed by the Department of Commerce. Furthermore, we consider it problematic that the Department of Commerce has rooms to make different judgements from the U.S. Treasury although the proposal supposes that the U.S. Treasury would be consulted regarding the analysis of undervaluation. Exchange rate issues should be exclusively discussed among currency authorities. In this respect, the proposal will seriously undermine credibility of existing frameworks to deal with those issues among currency authorities, which would threaten exchange rate stability and adversely affect macroeconomy and financial stability.

In the proposal, IMF’s equilibrium REER is expected to play an important role for the analysis of undervaluation. Originally and fundamentally, the equilibrium REER is supposed to be used for analyzing macroeconomy and current account balance. In this context, we would like to know staff’s candid view on the possibilities that the equilibrium REER would be used for decisions on countervailing duties which would deviate from the original and fundamental purpose.

Mr. Villar submitted the following statement:

We thank staff for its comprehensive report and Mr. Rosen, Ms. Pollard and Ms. Crane for their helpful and very interesting buff statement. We take positive note of the recent economic performance by the U.S. economy, with a record-breaking period of growth, large productivity gains, low unemployment, higher wages, and tamed inflation. We also notice that fiscal imbalances and debt unsustainability pose salient risks for the medium-term economic outlook, with potential negative spillovers for other economies. As stated on past discussions, we strongly support staff's assessment that for the global economy to function well, it should rely on a more open, stable, and transparent, rules-based international trade system. We concur with staff's view that trade barriers are likely to be ineffective at containing bilateral trade deficits and will be harmful to the U.S. and global activity. We broadly agree with staff's assessment and offer the following comments:

Fiscal Policy and Framework

The US public debt appears to be in an unsustainable path. As pointed out in the report, the structural primary deficit has steadily deteriorated and the overall fiscal balance expected for 2019, -4,2 percent of GDP, is large in the context of a cyclically buoyant economy. We broadly share staff's analysis that the reduction in the corporate cost of capital, while budgetary costly, proved to have a relatively minor impact on capital formation. This implies that policy adjustments are needed to lower the fiscal deficit and to put public debt on a gradual downward path over the medium term. As mentioned in the buff statement, we take note that the Administration believes that with regulations related to the tax reform still being finalized, the investment-enhancing impact of the reform is only at its initial stage. A continued monitoring of results will be key to assess these alternative views and the need for policy adjustments.

Monetary Policy

We agree that monetary policy decisions should continue to be data-driven, but we are not convinced by staff's argument that "the path for policy rates should accept some temporary overshooting of the Federal Reserve's inflation goal." Data dependence and continued policy accommodation are appropriate recommendations that do not require overshooting the inflation rate target. Fine-tuning this target could instead create confusion and hamper the expectations-anchoring process.

We welcome FED's ongoing review of the operating framework for its monetary policy strategy, tools, and communications. Beyond possible changes in the policy strategy, we agree with staff that changes in the operating framework for monetary policy could simplify it and enhance its effectiveness. Nevertheless, the authorities should set the pace and design specific changes to take place to reach this objective. Could staff elaborate on the benefits of returning to the point target at this conjuncture and the analysis that supports this recommendation?

Trade/External Sector

We see with concern that trade uncertainties remain high, creating negative consequences for the US and for global economic activity. Besides the direct impact on trade, the uncertainties created by announcements that entail shifts in trade policy are taking a toll on foreign direct investment. The latest UNCTAD data show that both global FDI and FDI in the US fell in 2018 for a second consecutive year. Also, trade policy uncertainty related to the imposition of tariffs can have a detrimental and long-lasting effect on global value chains and weaken the case for securing free trade agreements. On the latter, we are encouraged to see in the buff statement that the US Administration places high priority on securing Congressional passage of the United States-Mexico-Canada (USMCA) Trade Agreement.

We concur on the importance of a well-designed US-China trade agreement for the global economy. In this vein, we want to stress the need to avoid a managed trade deal focusing exclusively on reducing the bilateral trade imbalance between these two economies that could create new structural rigidities detrimental for the rest of the world. We very much welcome staff's analysis in Box 4 that estimates the global macroeconomic effects of a US-China trade dispute and that highlights the risks associated with a fragmentation or even a complete breakdown of the trading system. We would like to know if staff has explored how this trade dispute could impact other macroeconomic variables in the U.S. economy (e.g. inflation, interest rates, productivity, labor market, etc.) We also wonder if staff has estimates of the impact of the trade measures that could be imposed in a few weeks by the US to all its automotive imports.

Financial Sector

We concur with staff's assessment that whereas the financial system has shown robust performance recently, medium-term risks are building up. In this context, we take note that recent tailoring of financial regulation constraints may have a negative procyclical impact as they ease capital standards and other requirements to non-systemic financial institutions. Could staff comment on the proposed measures to tailor prudential standards based on size and complexity? Is this related to proportionality in banking regulation and supervision? How will this be applied to foreign entities? We also agree with staff that oversight of non-banks should be strengthened. We welcome that staff and the authorities highlight that other salient vulnerabilities include the potential for a destabilizing cybersecurity event.

Structural Reforms

Despite the US recent positive economic performance, the staff´s report shows that the benefits from this decade-long expansion have not been shared as widely as they could have. The interesting analyses on the decades-long rise in income and wealth inequality, the secular decline in socioeconomic mobility and other social indicators are troublesome. While the analysis is welcome, we find that the advice in this regard was very specific and more prescriptive than usual Fund's practice. We are encouraged by the relevance placed by the authorities to address these difficult challenges, as explained in the buff statement.

We were surprised to see in paragraph 27 of the report a positive view on a skills-based immigration reform, which may imply discriminatory treatment against poorer and less educated people. Moreover, from the point of view of its productivity impact, the spillover effects of this type of policy on source countries, i.e. brain drain, should be also considered.

Mr. Inderbinen, Mr. Trabinski and Mr. Tola submitted the following statement:

The U.S. economy has continued on a solid growth path, but challenges lie ahead. Growth in the first quarter of 2019 was stronger than expected, boosted by inventories and net exports, while private sector demand has slowed. However, based on the latest indicators for economic activity, risks to growth have increased. Trade tensions, particularly with China and Mexico, have continued to escalate over recent months and present a key risk not only to the U.S., but also to the global growth outlook. Overall, headwinds to medium-term growth prospects may be larger than previously assumed.

We welcome the policy options proposed by staff to put the debt-to-GDP ratio on a downward path. Debt is expected to further increase, as expenditures, primarily aging-related spending, continue to rise. Moreover, the fiscal cost of the Tax Cuts and Jobs Act (TCJA) has risen according to the most recent estimates, and there is a lot of uncertainty related to its potential spillovers. Unfavorable public debt dynamics could reduce the policy space to tackle social inequalities, address infrastructure needs, and implement the structural reforms necessary to enhance productivity. All these factors call for policy actions to reverse the current negative debt dynamic, and we welcome staff's recommendations in this regard.

We welcome the policies suggested by staff to improve welfare and inclusion. In this regard, we agree with staff that improving the provision of social welfare will also contribute to raising labor productivity levels and aggregate demand in the future.

Addressing the external imbalances of the U.S. will primarily depend on domestic policy action. We agree with staff that containing bilateral trade deficits will unlikely be achieved through tariff measures. On the contrary, unilateral trade measures, as well as counter measures, will harm the global economy and disrupt confidence. Trade tensions should be addressed in a cooperative manner through a multilateral, rules-based approach, with the goal to preserve an open and free global trading system. In addition, as staff points out, addressing the U.S. current account deficit will likely primarily depend on adjustments of U.S. domestic policies. In this regard, as indicated on p. 45 of the report, more transparency in staff's assessment of the U.S. external balance and the decomposition of the cyclically adjusted current account gap would be helpful. In particular, we would welcome staff's comments on the decomposition of the fiscal policy gap of -0.4 percent of GDP for 2018 between its domestic and foreign components.

The current monetary policy stance is appropriate, given the recent weakness in inflation and the high uncertainty surrounding the growth outlook. The Fed has communicated the key details of the evolution of the operating framework clearly. Could staff comment on why they nonetheless see a need for greater clarity of the expected evolution of the operating framework for monetary policy?

Financial regulations should reflect the size and complexity of institutions. As a response to the global financial crisis, regulations have become more stringent and more complex. The larger capital and liquidity buffers have made the financial system significantly more stable. Hence, it is key to avoid a rollback of these achievements. At the same time, it is important to consider the principle of proportionality to make sure that small banks do not carry a disproportionate regulatory burden. In this respect, we agree with the authorities that tailoring financial regulation can increase effectiveness and efficiency. This is particularly the case for banks that are primarily active domestically. For banks operating internationally including the G-SIBs, it is key to maintain a level playing field, particularly regarding capital and liquidity requirements, which should be applied consistently across jurisdictions.

The U.S. financial system appears sufficiently strong to handle potential losses from corporate debt risk. As staff rightly points out, and as underlined by the authorities, record levels of corporate debt present a key risk to U.S. financial stability. At the same time, in view of the overall healthy U.S. financial system, decent corporate profits and low borrowing costs, this risk appears manageable for the time being. In this context, we consider the recent U.S. institutional response to financial stability risks as appropriate.

Ms. Mahasandana, Mr. Tan, Mr. Mahyuddin and Ms. Yoe submitted the following statement:

We thank staff for the well-written report, and Mr. Rosen, Ms. Pollard and Ms. Crane for their informative buff statement. The US economic growth has been resilient in the past decade, weathering both domestic policy tightening and external shocks. The global economy has benefitted from the record long economic expansion in the US. Nevertheless, the US continues to face significant challenges such as income and wealth polarization and eroding social mobility that could threaten long-term growth. Additionally, heightened policy uncertainty clouds the outlook, with spillover implications for other economies. In this regard, we also welcome staff's discussion on the spillover effects from the US domestic policies. Overall, we support the staff appraisal and offer the following comments for emphasis.

With the US economy estimated to be operating above potential, it is now opportune and prudent to undertake fiscal consolidation. The authorities reiterated its plans to stabilize public debt and return the primary balance to a modest surplus position over the medium-term through a two-pronged approach: supply side reform to raise potential growth and planned reduction in non-defense discretionary spending. However, they also acknowledged that bringing down public debt to a more sustainable level remains a long-term challenge. We welcome staff's comments on the progress of the budget plan, and the impact on public finances. We also seek staff's comments on the traction of Fund advice on addressing the US public debt, and the feasibility of the proposed policy options. Notwithstanding the high public debt burden, the US continues to meet its high gross financing needs given the depth and liquidity of the US Treasury market and its safe haven status. We wonder if the debt sustainability assessment is relevant for the US, or whether it may be worthwhile to consider how other factors such as market depth of US Treasury or investor profile would impact US debt sustainability.

We welcome the authorities' thoughtful focus on helping low-income households become more self-sufficient through productive employment and targeting the social safety net at those who need it most. The strong economic expansion has not led to a meaningful improvement in social outcomes and socioeconomic mobility continues to be eroded. At the same time, technological innovation and globalization could widen income inequality, displacing the vulnerable from employment. As such, greater emphasis on promoting active labor market policy for able-bodied individuals to move from welfare to work is critical. Such efforts are likely to deliver more durable improvements to social outcomes, by raising potential growth without exacerbating the fiscal burden. We welcome staff to comment on policies that can encourage and promote employment among the low income to address poverty and inequality.

Adherence to the principles of data dependence and clear communication on the fed funds rate remains critical to avoid volatility in financial conditions or negative spillovers to the rest of the world. We note the need for greater signs of wage or price inflation for further increases in the Fed funds rate to gauge the balance of risk to both inflation and employment outcomes. To this end, we welcome the authorities' assurances that they will continue to execute its monetary policy in a data-dependent way, with greater emphasis on clear communication. Nonetheless, we note the authorities' concerns regarding staff's recommendation to publish the central economic scenario in the quarterly monetary policy report, given that such scenario can be misinterpreted as a firm view. We welcome staff's comments and further elaboration on this recommendation.

The recent heightening trade tensions draws global concerns. Trade barriers are harmful and ineffective in addressing unfair trade practices globally or shortcomings of trade rules. A vicious cycle of retaliatory measures affects market confidence and will be harmful to the US and to global growth momentum. In this regard, we support staff's calls for the US to engage in constructive dialogue with its trading partners to correct any emerging disagreement, while continuing to display a leadership role in promoting a rules-based international trade system. Moreover, staff's recommendation that the US external imbalance needs to be addressed through fiscal adjustment and supply side reforms that improve productivity and competitiveness is consistent with Fund advice on focusing on well-tailored macro-structural policies.

We are watchful of the spillover effects of financial stability risks in the US. An extended period of accommodative financial conditions has led to a buildup of corporate leverage. We note staff's assessment that medium-term risks to financial stability are rising alongside weakening underwriting standards and asset quality. While interest coverage ratios and liquidity positions of the corporate sector remain healthy, can staff comment on the leveraged corporates' capacity to withstand earnings shocks or a tightening of financial conditions. It would also be useful for staff to outline the transmission channels through which the corporate debt risks would affect financial stability and growth in the US and in countries that are most exposed. Staff noted that there has been little institutional response to counter the growing financial stability risks. We welcome staff's comments and recommendations on the measures needed to address financial stability risk, for instance to curb excessive corporate leverage or buildup of vulnerabilities in the non-bank sectors.

Ms. Levonian, Ms. McKiernan and Ms. Vasishtha submitted the following statement:

We thank staff for their candid report and Mr. Rosen, Ms. Pollard and Ms. Crane for their comprehensive buff statement.

The US economy continues to expand at a robust pace. Labor market conditions remain strong, with solid job gains in recent months and the unemployment rate at near-historical lows. Real wages have been rising on the back of productivity gains, while inflationary pressures remain subdued. We agree with staff that the most significant policy challenge is to address deteriorating social outcomes while gradually reducing the general government deficit. A deepening of ongoing trade tensions and a sharp tightening of financial market conditions pose important downside risks to the US economy, with spillover implications for other economies. We broadly agree with the thrust of the staff appraisal and offer the following comments for emphasis.

Procyclical fiscal policy has led to a further deterioration of public debt dynamics, with general government debt reaching 107 percent of GDP in 2018. We concur with staff's main fiscal policy recommendation to lower the fiscal deficit and put public debt on a gradual downward path over the medium term. Such a fiscal anchor (i.e., debt-to-GDP ratio on a downward path) provides a good balance between the flexibility required to undertake productive investments and ensuring medium-term fiscal sustainability. This is crucial since, under current policies, public debt is expected to continue to rise, particularly as aging-related spending rises. We appreciate the menu of policy options suggested by staff to address the unsustainable fiscal position and the shortcomings of the U.S. budgetary process, but note that the staff report does not give a sense of the authorities' views on these recommendations. Staff comments would be welcome.

We echo staff's emphasis on the importance of a more open, stable, transparent, and rules-based international trade system for a well-functioning global economy. Resolving trade tensions in a co-operative manner should be the highest priority. The U.S. and its trading partners should work together constructively to better address distortions in the international trading system. We welcome the emphasis placed by the US Administration on securing Congressional approval of the USMCA trade agreement, which will reduce uncertainty and enhance data transparency in certain sectors.

We particularly appreciate staff's approach of drawing upon the analytical pieces in recent World Economic Outlook reports and other quantitative studies to highlight the significant negative repercussions of trade tensions and restrictive trade policies. However, it is not clear to what extent staff's baseline growth forecast incorporates the impact of the already implemented tariff measures and the effects of uncertainty around potential new measures. A more fulsome discussion of how these measures affect the current outlook would have been useful.

The US has made significant efforts to strengthen the financial oversight architecture since the Global Financial Crisis, making it better positioned to withstand shocks relative to the pre-crisis period. Nevertheless, medium-term financial stability risks have increased. In the banking sector, regulatory reforms and improved risk management practices since the crisis have strengthened the resilience of U.S. banks. While tailoring certain regulatory requirements for smaller, non-systemic financial institutions may be reasonable, we agree with staff that the risk-based approach to regulation, supervision, and resolution should not only be preserved, but also enhanced.

Vulnerabilities continue to build in the corporate sector and among non-bank financial intermediaries: corporate leverage is historically high, the share of commercial non-performing loans is rising, and underwriting standards are deteriorating. Although the debt-service capacity of U.S. firms has improved since the crisis, an abrupt tightening of financial conditions could result in significant downside risks for investment, job creation and economic activity. This, in turn, could have significant spillovers onto other economies. We urge staff and the authorities to continue to monitor these financial vulnerabilities closely.

Despite strong macroeconomic performance, social indicators for the United States reveal some disturbing trends, some of which are common across advanced economies. Social mobility has deteriorated, average life expectancy has fallen below that of other G7 economies, income and wealth polarization have increased, poverty rates remain higher than other advanced economies, and education and health outcomes are discouraging. We agree with staff that a multi-pronged strategy is needed to address these social trends while ensuring that the associated fiscal costs are appropriately balanced by raising revenues and tackling entitlement spending. In this context, we welcome the authorities' focus on strengthening economic prospects for the middle class and encourage them to further integrate inclusive growth considerations into policy design and implementation.

Mr. Fanizza and Mr. Spadafora submitted the following statement:

We thank staff for an informative report and Mr. Rosen, Ms. Pollard and Ms. Crane for their candid buff statement. We broadly agree with the thrust of the staff appraisal.

The overarching goal of the U.S. authorities is to safeguard the favorable macroeconomic outcomes, while improving their inclusiveness, in a context of still strong growth and low inflation. To this end, two priorities stand out: (a) resolving the detrimental trade tensions in a globally-beneficial and timely way; and (b) making growth more welfare-improving.

On trade, we encourage the U.S. authorities and their main trading partners not to spare efforts to achieve soon a cooperative solution to tensions that could damage the global outlook and make it difficult to sustain the so far impressive US economic performance. In fact, the global economy has already started to feel the adverse impact of ongoing trade tensions, mainly through increased uncertainty. We believe that the best way for the Fund to contribute to defuse these tensions is to redouble its efforts to help countries address global imbalances, which if unattended are bound to further fuel calls for trade protectionism.

On social outcomes, we welcome staff's innovative emphasis on the macroeconomic impact of some disappointing social indicators, which should however be placed in the context of increased labor-market participation and declining unemployment – as pointed out by Mr. Rosen, Ms. Pollard, and Ms. Crane in their buff statement. Nevertheless, we believe tackling these issues has now become essential to make the authorities' pro-growth policies both sustainable and credible. Of course, giving implementable policy advice on how to address these issues is not an easy task. The risk that well-meaning policies produce adverse unintended consequences is always present. Therefore, we much appreciate that staff did not include any of the policy options discussed with the authorities in the staff appraisal. However, we would like to stress the importance of finding ways to curb the growth of healthcare costs, which have increased much faster in the US than anywhere else and cannot be explained only by demand pressures from population aging.

On monetary policy, we agree with the staff's recommendation to pause before further increasing in the policy rate. The inflation outlook has significantly changed since last year; the chances for positive price surprise have dwindled, despite an increasingly positive output gap and a stronger labor market. In fact, forward-market rates point to expectations of future cuts in the Fed rate, which have been somewhat validated by the tone of the FOMC statement on June 19th. We are somewhat surprised that the report does not even mention the possibility of a rate cut. We would have liked staff to discuss the arguments in favor and against it. We would appreciate staff comments on the issue.

The increasing public-debt burden is certainly a source of concern. We take note of the authorities' intention to stabilize the debt-to-GDP ratio through a combination of non-defense expenditure restraint and supply-side reforms that would lift potential growth. The staff's assessment is much less sanguine. First, we are wondering whether staff's views on the lack of evidence of a favorable impact of the tax reform on investment in 2018 have some bearing on their skepticism on potential output prospects. We would recommend caution on that, because supply-side effects of tax reforms take time to be felt. Second, while we certainly welcome the candor of the staff's assessment, we would have expected a stronger analytical background to explain the labeling of the fiscal position as "not sustainable", given the US prominence in financial markets and the global economy. We would welcome staff's comments

The US financial system appears overall healthy, but financial stability risks are increasing. While we understand that the financial system is now on much stronger footing than it used to be, we share staff's concerns on the deterioration of underwriting standards at this late stage of the credit cycle and the relaxation of some financial regulation. We also support the call for strengthening the oversight of nonbanks and welcome the authorities' efforts in addressing data gaps. Nevertheless, we would have liked to see a deeper discussion on the role that macroprudential policies could play in managing macro financial risks and their interaction with the monetary policy stance. Would a loosening of the monetary policy stance warrant a more active role for macroprudential policy?

Mr. Mozhin and Mr. Palei submitted the following statement:

We thank staff for a concise report on the economy of the United States supported by the references to the Fund's flagship publications and working papers. We also thank Mr. Rosen, Ms. Pollard and Ms. Crane for clarifying the authorities' views on key issues. The U.S. economy continues to perform well, with 2018 real GDP growth close to 3 percent and unemployment rate at an extremely low level. The PCE inflation is close to target, and current account deficit is relatively small. The authorities and staff agree that the fruits of economic growth did not benefit all strata of the society and social outcomes fell short of the achievements in other advanced economies. We also note the agreement on the short-term economic outlook, as it is seen as positive and robust. At the same time, the views differ greatly on the reasons for the recent performance and on the medium-term prospects of the economy. This divergence in views is troubling, since the developments in the U.S. economy play such an important role on the world stage.

While the U.S. administration believes that lower tax burden, deregulation of the economy and other structural reforms will have large supply-side effects and ensure potential annual growth of about 3 percent, the Federal Reserve, the Congressional Budget Office, and staff offer much more cautious growth projections. We tend to agree with staff that current growth is mostly due to a temporary demand stimulus, and the economy is functioning above potential.

If potential growth remains close to the historic levels and the recent productivity increase is mostly driven by the business cycle, the administration's fiscal projections are overly optimistic. According to staff, fiscal relaxation made the current fiscal position and debt dynamics unsustainable. Medium-term fiscal consolidation calls for well-known and well-articulated measures.

While staff see fiscal policy as overly expansionary, they fully support the current stance of monetary policy. Last December the Federal Reserve seemed to be on course toward steady normalization of the monetary policy signaling its intentions to increase policy rates. However, in January the monetary authorities signaled their concerns about the state of the economy and hurried to reassure market participants of their readiness to prevent excessive market volatility and possible sharp tightening of financial conditions. Today eight members of the FOMC projected a rate cut in 2019.

Given that fiscal policy is very expansionary and, according to staff, financial stability risks are contained, we feel that an additional elaboration on the policy mix would be useful. In this regard, we note that the Fund's former Chief Economic Counsellor, former U.S. Treasury Secretary and many other experts argue forcefully for revisiting the relative roles of monetary and fiscal policies considering the growing evidence of persistently low neutral interest rates and stubbornly low inflation[1]. The experience of Japan and, more recently, of the Euro Area, indeed, should be a source of concerns for policy makers and the Fund. In this respect, we recall that immediately after the global financial crisis the Fund took a very firm stance on the need for decisive fiscal consolidation in most advanced economies, but at a later stage favored a much more lenient approach. Are we now running the risk of a similar shift in the institutional view? Staff comments would be appreciated.

We welcome the decision by the Federal Reserve last November to conduct a broad review of its strategy, tools, and communication practices. We look forward to the results of this important undertaking. The review was inspired and informed by the best practices in other advanced economies. In this respect, do staff think that an independent review by external experts rather than an internal exercise would be even more useful?

A strong state of the economy, together with the effects of the changes in the energy balance and low interest rates on current account, seem to make

[1] https://piie.com/blogs/realtime-economic-issues-watch/secular-stagnation-requires-rethinking-macroeconomic-policy

the U.S. relatively resilient to the hikes in global policy uncertainty. At the same time, we agree with staff's analysis and position on the costs and benefits of fueling multiple trade disputes and other forms of unilateral approaches to resolving real or perceived challenges.

With respect to the above, we note in paragraph 41 of the report that the Department of Commerce may be enabled to impose countervailing duties if it judges that currencies are undervalued in some trading partners. Like staff, we are concerned about this new development. We would ask staff to elaborate on the risks of conflicting opinions between the Department of Commerce and the U.S. Treasury, as well as the Fund's work reflected in the External Sector Report and other products.

The report has a separate section on governance and transparency. It would not be an exaggeration to say that almost everybody is aware of the current U.S. administration's long-standing commitment to "drain the swamp". This popular idiomatic expression refers to domestic issues rather than transnational. It implies the need to address the abuse by lobbyists of the decision-making process, to deal with the revolving door practices, and to improve relations between the executive and legislative branches. Unfortunately, it seems to us that in this section staff missed an opportunity to address serious issues of governance. At the same time, we note that in other parts of the report staff referred to some of the most obvious challenges in this area, such as "the dysfunction inherent in the U.S. budget process" (paragraph 28, page 28).

Mr. Mojarrad submitted the following statement:

We thank staff for a well-written report which underscores the strong performance of the U.S. economy and provides a candid assessment of challenges it is facing. The report's analysis of poverty issues, income and wealth inequality, and the macroeconomics of health, education, and the opioid crisis in the U.S. is indeed commendable, and we encourage staff to expand on them in future consultation reports or in stand-alone studies. We are in broad agreement with the staff appraisal while taking note of the authorities' perspective on some issues where there is divergence of views, as elaborated in the informative statement of Mr. Rosen, Ms. Pollard, and Ms. Crane.

The current position and the near-term prospects of the US economy are very favorable with robust activity, rising wages, and historically low unemployment. These trends had been in train for a few years, but were reinforced more recently by the strong countercyclical 2018-2019 fiscal expansion, very supportive financial market conditions, and relaxation of regulations. Notwithstanding the strong fiscal impulse and the buoyant economic activity, the current account deficit has been steady in the past few years, in part due to the dramatic change in the domestic energy landscape. Going forward, however, we agree with staff that the expected unwinding of the fiscal stimulus beginning in 2020, the escalation of global trade conflicts, slow gains in productivity, and political cycle uncertainties will not support sustained activity at current rates over the medium term, and that growth is expected to moderate to a sub-par potential fairly quickly. The long-standing supply-side measures that could boost productivity and growth materially—notably much-needed investment in public infrastructure, health and education, and environment—are not likely to materialize soon enough as there is neither a clear political consensus nor could such spending be accommodated without worsening an already unsustainable public debt situation, in the absence of a major revenue effort. Moreover, the response of capital and R&D spending to the 2017 tax relief package has been disappointing.

The U.S. fiscal position and public debt profile are causes for concern. It is difficult to ascertain to what extent the Administration's planned reduction in non-defense discretionary spending, and healthcare and welfare reforms could improve the underlying fiscal position and "bend" the public debt curve without worsening the social outcomes in the absence of additional revenue measures. To that end, the introduction of fuel-related taxes that would help erase part of the large U.S. carbon footprint merits careful consideration. We also support staff's recommendations to overhaul the inherently inefficient budgetary process.

As documented in the staff report, the robust aggregate income and employment growth has masked the deteriorating social outcomes and the growing income, wealth, and spatial disparities, and the erosion of socioeconomic mobility over the last five decades. Stopping the growing divergences and narrowing the gaps decisively require a multi-pronged approach. The underlying causes of disparity are mostly structural in nature where cyclical factors such as rising wages and employment cannot fundamentally address. We welcome the Administration's plans to address the healthcare inflation and aggressively fight the opioid crisis and urge the U.S. authorities to build on the significant gains in health insurance coverage made possible by the Affordable Care Act.

The Fed's "pause" and its increasing dovish undertone are, in our view, appropriate as we believe that the balance of risks is now narrowly tilted to the downside with the global growth momentum faltering, the economic costs of the global trade conflict becoming more visible, and with geopolitical risks worsening worldwide. Inflationary expectations are firmly anchored, PCE inflation is muted, and there are continued downside risks to staff baseline forecasts, but that could change quickly in the event of a major, prolonged commodity price shock. The Fed should stand ready to change its bias and act accordingly depending on how the balance of risks changes. In any event, as also stressed by staff, Fed's clear, forward-looking communication is critical to avoid volatility in U.S. financial markets and the ensuing negative spillover effects globally. The credibility of monetary policy ultimately hinges on the credibility of the Fed, which in turn is grounded in the Fed's long-standing immunity from political pressure.

The staff assessment that the share of non-performing commercial loans is rising, regulatory constraints are easing, and underwriting standards are weakening—at the time when corporate balance sheets are highly leveraged—underscores rising medium-term financial risks and is a cause for concern. Also concerning is the absence of effective institutional response. We share staff views that further changes in financial oversight should seek to strengthen the current risk-based approach to regulation, supervision and resolution. The high and rising student debt also seems to be emerging as a potential source of vulnerability. We welcome staff comments and encourage staff to explore the issue in more depth in future studies. The staff report flags the need to strengthen the financial oversight of nonbanks and hints at data blind spots related to their activities. We appreciate staff further elaboration.

The escalating costs of the U.S.-China trade conflict on the disputing parties as well as tertiary partners have been well documented by the staff report and the most recent WEO. There are even spatial equity dimensions with the poorer states within the U.S. suffering the most from the adverse consequences of tariffs. There are undoubtedly trade-distorting policies and unfair trade practices that the WTO cannot effectively arbitrate within its existing framework. But, as indicated by staff (Box 3), it is only through a multilateral, rules-based approach that these practices and policies could be eliminated; a trade deal that only seeks to reduce the bilateral trade deficit potentially creates new structural rigidities. Further, it is widely acknowledged that tariffs are not likely to be effective in correcting bilateral trade deficits and will be damaging to the U.S. with substantial negative cross-border spillovers. We are also concerned about the U.S. proposal to impose countervailing duties on countries subsidizing exports by maintaining an undervalued exchange rate as verifying undervaluation could involve subjective judgment and the measure is likely to invite retaliatory action.

In May and November 2018 and May 2019, the U.S. Administration imposed bilateral trade and payments sanctions on Iran, and extra-territoriality on Iran's trading partners. In the past, the U.S. had imposed bilateral restrictions—on Iran as well as other members—on national security grounds by invoking the Executive Board Decision No. 144-(52/51). It appears that the Fund was not notified—ex-post or ex-ante within the required 30 days—of the imposition of the May and November 2018 and May 2019 sanctions, and hence these sanctions were not legally grounded in the Decision No. 144. As such, the U.S. seems to be in violation of its obligations under Article VIII. Staff elaboration will be appreciated. More generally, the sanctions have disrupted trade and payments for many members, undermining the smooth functioning of the global payments and settlement system as enunciated in Article I of the Articles of Agreement.

Mr. Mouminah, Mr. Alkhareif and Mr. Keshava submitted the following statement:

The U.S. economy is performing exceptionally well and on track to achieve the longest expansion on record. We are also pleased that the labor market remains remarkably robust with very low unemployment and rising labor force participation. Indeed, it is noteworthy that an average of 2 million jobs per year have been created over the course of this expansion. In addition, we welcome solid productivity gains and rising wages, in particular, for the lower-income workers, which along with an expansion of the Child Tax Credit and a focus on skills training should help in improving social outcomes. We thank staff for their candid assessment of the U.S. economy and Mr. Rosen, Ms. Pollard, and Ms. Crane for their helpful buff statement. In this context, we take note of the disagreement between staff and the Administration on medium-term growth projections.

Putting public debt on a gradual downward trajectory over the medium term remains an important priority. Here, we take note of the Administration's fiscal strategy, anchored by supply-side reforms and a reduction in nondefense discretionary spending combined with healthcare and welfare reforms, to help stabilize the public debt ratio. Achieving these objectives would require significant efforts and, therefore, close vigilance and timely policy adjustments, as appropriate, would be important. Upgrading public infrastructure is a longstanding recommendation to help raise potential output and, in this context, we are encouraged by the Administration's aim to leverage federal spending to generate substantial investment by state, local, and private providers up to $2 trillion over the course of the next 10 years. We look forward to positive outcomes on this front.

The Federal Reserve's continued commitment to the principles of data dependence and clear communication is welcome. Indeed, this is crucial to avoid excessive volatility in financial conditions or negative spillovers to the rest of the world. The announcement of continued pause to further changes in monetary policy seems appropriate in light of the current economic conditions and risks. We also look forward to the outcome of the ongoing review of monetary policy strategy, tools, and communications to assess how it can best continue to achieve and maintain maximum employment and price stability.

The financial system is healthy but continued vigilance is essential to safeguard financial stability. Here, we take positive note of the staff's assessment that U.S. banks are well capitalized and asset quality is generally good. On high debt levels, it is comforting to note that much of this debt (for both households and firms) is at low interest rates and long duration, indicating less burdensome debt service. We are also reassured by efforts to strengthen resilience in nonbanks. Since a robust financial system oversight in the U.S. also has positive spillovers on the rest of the world, it is important to preserve the gains made in strengthening the financial oversight structure since the global financial crisis. In this connection, it is not clear why staff considers that the tailoring of financial regulations based on size and complexity (Box 2) will weaken standards. Comments would be appreciated. We look forward to the outcome of the ongoing FSAP.

On trade, we are encouraged by recent efforts to resolve trade disagreements in a cooperative manner and look forward to positive outcomes. We also agree on the importance of strengthening the rules-based, multilateral trading system. We welcome the U.S., Mexico, and Canada (USMCA) Trade Agreement and look forward to speedy congressional approval.

Finally, we welcome the comprehensive coverage of issues related to governance and transparency. This is part of the Fund's analysis of the supply side of corruption in advanced economies. We take positive note of U.S. efforts in this area.

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

Ms. Riach, Mr. Ronicle and Ms. Andreicut submitted the following statement:

We thank staff for the detailed report and Mr. Rosen, Ms Pollard and Ms Crane for their insightful buff statement. We broadly agree with the staff assessment. The U.S. economy continues its longest expansion in recorded history, with strong GDP growth, unemployment at a record low and real wages finally rising. We commend the authorities for this impressive performance. At the same time, we note the significant difference of view between staff and the authorities on the forecast for the coming years and the worrying evidence that social indicators have not kept up with the positive macroeconomic picture.

We strongly agree with staff views that a well-functioning global economy needs a more open, stable and transparent rules-based international trade system. We hope that the US and its trading partners can work constructively going forward.

Macroeconomic and financial sector developments

We congratulate the authorities on a sustained growth performance, one which has repaired the damage inflicted by the global financial crisis and has so far been resilient to both domestic policy tightening and to external shocks. We also note the welcome productivity improvements in the US economy. We would be interested in any staff reflections on how the US has achieved stronger productivity growth when many of its advanced economy peers have struggled.

Despite this positive trajectory, a number of vulnerabilities are building. While the US financial system is generally in good health, the rapid growth of corporate leverage stands out as a clear risk. We are encouraged by the authorities' commitment to better understand interlinkages and improve risk management practices, and we would urge the authorities to remain vigilant. Looking at the financial sector more broadly, we also encourage the authorities to ensure that any further changes in financial regulation continue to place an emphasis on a risk-based approach to regulation, supervision and resolution.

A further vulnerability facing the US economy concerns the fiscal front, with the structural primary deficit of the federal government having steadily deteriorated since 2016. This has led to an increase in the debt-to-GDP ratio, with debt expected to continue rising in the medium-term. Staff note that the ratio is on an unsustainable path. While we agree that the authorities need to address the fiscal deficit, we would be interested in staff views on the factors that need to be take into account when determining US debt sustainability. Staff do mention mitigating factors in the annex to the report, but we wonder if they shouldn't place more weight on the fact that the US is a global reserve currency. Would this mitigating factor paint a less concerning picture about US debt? We would also be interested in staff views on the ongoing academic debate on debt sustainability.

Finally, we welcome the commitment from the US monetary authorities to continue to execute US monetary policy in a data-dependent manner, putting a premium on clear communication. We urge them to continue to undertake this responsibility using all the tools at their disposal, in line with their mandate.

Trade

Trade uncertainties remain high, bringing risks both for the US and global economy. The US dollar is the global reserve currency and the performance of its economy has significant impact on the rest of the world. We continue to believe that trade barriers are harmful for global trade and are unlikely to be effective in reducing bilateral trade imbalances.

Continued trade tensions and the imposition of further tariffs could have a significant negative impact on the US economy. With growth expected to moderate in 2020, wage costs putting pressure on profits and some concerns about medium-term financial stability, trade shocks could have a significant effect at this point in the economic cycle.

We welcome staff analysis on 'Outward Spillovers to Trade Tensions' (Box 4). It is useful to see the impacts trade tensions can have on global supply chains as well as on the domestic US economy at state level. It would have been interesting to see also what the impacts of trade distortions are on consumers, long-term productivity and investment. Staff could consider these aspects in future work. Finally, we would also encourage staff to explore further with the current administration its stated aims of the tariffs- namely that of leveling the playing field and protecting intellectual property rights.

Social indicators

We thank staff for their insightful overview of social indicators and agree that the findings on average life expectancy, income polarization as well as poverty, are both striking and concerning. We welcome staff's calls for the authorities to take action going forward.

Nonetheless, as Mr Rosen notes in his buff statement, some recent data has been more positive with signs that the record-long expansion is beginning to have genuine benefits for sectors of society that have traditionally had lower engagement in the labour market. For instance, the unemployment rate for African Americans hit its lowest point since the early 70s, while unemployment among those with less than a high school diploma is at historic lows. We also see evidence that low wage workers are increasingly experiencing the wage-benefits of the expansion. In 2018, wage growth in low-wage industries was 4.4 percent, while it did not exceed 3 percent in middle- and high-wage industries. These emerging positive signs show that endangering the expansion, through shocks such as further trade tariffs, could undo some of the good news thus far.

Energy

We take note of the rapid transformation in the US energy industry over the past decade, with the US expected to become a net exporter of petroleum products by 2022.

Staff note that the US oil and gas sector could serve as a global shock absorber. We wonder whether this view needs some further caveats. We understand that OPEC still holds much of the world's spare capacity and can produce barrels at a much lower price relative to the US. We also wonder whether, over the long-term, investment in new oil supply will be sufficient to give the US such a significant shock-absorbing role.

Given the well documented impact of carbon emissions, we urge the US authorities to consider non-fossil fuel options to further supplement their energy supply.

Mr. Mahlinza and Mr. Tivane submitted the following statement:

We thank staff for the insightful report and Mr. Rosen, Ms. Pollard, and Ms. Crane for their helpful buff Statement.

The U.S. economy continues to grow on a steady path, supported by growth-friendly policies. This encouraging trend is accompanied by benign labor market conditions, robust private sector activity, and anchored inflation expectations. In the near term, tax and regulatory reforms will continue to propel economic growth, and further boosting wage and productivity growth. While the risks to the near-term outlook are broadly balanced, the escalation of ongoing trade disputes and an abrupt reversal of the current supportive financial conditions could negatively weigh on growth. Against this backdrop, the U.S. authorities should seize the window of opportunity from the cyclical upswing to address pressing challenges – which include, reversing the upward trend in debt dynamics, supporting supply-side reforms, and improving social and distributional outcomes.

Despite this growth, we are concerned about the lagging social and distributional outcomes. The strengthening in the U.S. economy seen over the past several years has yet to translate into improved social and distributional outcomes, particularly for the most vulnerable population. We appreciated staff's continued focus on these issues in the report and note the authorities' commitment to more forcefully address these challenges through reform measures aimed at bolstering job creation and supporting low-income workers and families. We take note of staff's recommendations to tackle these challenges and would appreciate comments on the feasibility of implementing the proposals in the current environment.

We urge the authorities to take proactive policy actions to tackle the rising debt dynamics as a core part of their fiscal strategy. While the 2017 Tax Cuts and Jobs Act (TCJA) has contributed to the recent economic upswing, its impact on the country's debt and deficit dynamics needs to be kept in check. This is particularly important given its potential negative spillover risks to the global economy and amplification of global imbalances. We believe that the current economic upswing provides a window of opportunity to address the debt challenges while simultaneously deploying a range of revenue-enhancing reforms to create room for infrastructure spending that can lift competitiveness and productivity. In addition, we see merit in staff's proposals to raise fiscal space to address entitlement outlays and federal programs aimed at improving social and distributional outcomes.

We welcome the Federal Reserve's continued adherence to the principles of data-dependence, clear and forward-looking communication of monetary policy. We concur with staff's views that given the sustained expansion of economic activity coupled with muted inflation pressures, deferring the timing and size of future adjustments to the federal funds rate may be appropriate to sustain positive supply-side effects. We take positive note of the Fed's ongoing assessment of the monetary policy strategy for meeting its dual mandate. We also encourage the U.S. authorities to step up efforts to shield the financial system against risks that could arise from leveraged corporates and the nonbank financial institutions – including through further enhancements to the risk-based approach to regulation, supervision, and resolution.

We are concerned that the protracted trade policy uncertainties remain a significant source of risk to the global economy. The results of staff's research, which indicate that the U.S. administration's decision to impose tariffs targeting specific sectors of its major trading partners could lead to sub-optimal outcomes both to the U.S. and its major trading partners, are worrisome. This could significantly disrupt critical global value chains; affect global production and consumption patterns; and undermine the rules-based international trading system. We wish to underscore that a viable solution to achieve free and fair trade globally, should be underpinned by constructive and good faith negotiations under the existing WTO framework. We therefore encourage the U.S. authorities to continue working constructively with international trade partners to buttress the rules-based, multilateral trade system.

Finally, we want to thank staff for the assessment of governance and transparency in the AIV report and the authorities for their commitment to address concealment of proceeds of corruption in the US economy. We also welcome the commitment to work on potential legislative solutions to address gaps in the collection of beneficial ownership information.

Mr. de Villeroché, Mr. Castets and Mr. Rozan submitted the following statement:

We would like to thank staff for their very clear report and genuine analysis, as well as Mr. Rosen, Ms. Pollard and Ms. Crane for their insightful buff statement. Given the significance of the US economy on the rest of the world, and the worldwide spillovers created by its fiscal, monetary, financial and trade policies, the comprehensive analysis led by staff is particularly welcome. While the economy is experiencing a record period of growth, it appears to be at the price of significant fiscal and social imbalances, and in a context of rising vulnerabilities. In this regard, we particularly thank staff for the attention dedicated to inequality and poverty trends. We share the thrust of the staff's appraisal and would like to make the following comments for emphasis:

While the United States is recording its longest expansion in recorded history with record low unemployment, downside risks have increased. Growth is set to moderate as the temporary measures linked to significant tax cuts and the expansionary fiscal policy wear-off. Downside risks have increased with rising trade tensions, a maturing business cycle and significant uncertainties are weighing on the outlook, both in the US and in the global economy. We would like to thank staff for their thorough analysis of social outcomes in the US, which paints a worrying picture of rising, multidimensional inequalities. We note that these inequalities, which have been reinforced by the US tax reform, are having negative effects at the macroeconomic level, as pointed out by staff. We are generally supportive of the broad range of reform orientations highlighted by staff on providing family-friendly benefits, better supporting the poor, expanding the coverage and addressing costs of the healthcare system, and improving education outcomes. Further inclusion of these issues in bilateral surveillance is particularly necessary, in line with the Framework on Social Spending. In addition, it would have been useful to compare the results of each statistics with other developed countries.

We continue to be concerned by recent decisions of the authorities on trade, and encourage the authorities to remain committed to a rules-based and open trade regime. As highlighted by staff in Box 4, ongoing bilateral trade tensions with China are likely to create a drag on certain US industries and states. This adverse impact could be amplified by adjustment costs, negative effects on labor and capital formation and policy uncertainty. Consistently with the conclusion of the April 2018 WEO, the US external imbalances would be more effectively addressed through a fiscal adjustment, as well as supply side reforms to improve competitiveness. Indeed, staff projects and increase of both the current account deficit and the trade balance deficit. Continued work by staff on the assessment of the impact of trade tensions will be particularly important going forward.

We remain concerned by the procyclical nature of the fiscal stimulus. The combined impacts of the 2017 Tax Cuts and Jobs Act and the increase in spending are weighing on public finances. Moreover, the former has not triggered the supplementary investments it was designed to unlock, with a significant portion of the benefits being reverted to shareholders. This confirms staff’s projection that tax cuts would not automatically pay for themselves. We also found the finding, presented in box 7, that only 20 percent of the increase in corporate cash balances for S&P 500 firms has been used for capital and R&D spending quite telling.

While the definition of public debt unsustainability is subject to discussion, the still significant deficit in a context of relatively elevated growth, the rapid upward debt trajectory, and the lack of political consensus on a fiscal strategy to put debt on a downward path is concerning. Given the low level of public spending, and the significant infrastructure and social needs highlighted by staff, cutting expenditure could harm the long-term growth outlook as well as social fairness. Against this background, raising revenues appears inescapable to put debt on a downward trajectory while answering the high infrastructure and social needs. We agree with staff that a carbon tax and a federal sales tax are promising options. Going forward, while we commend staff for the range of policy options proposed, we would encourage them to more precisely present the revenues that could be generated through those measures, to inform policy makers. Additionally, on carbon pricing, it would be helpful to cover the mechanisms created at the state levels, such as California, to inform the potential articulation between federal and state levels carbon pricing mechanisms – staff comments are welcome.

On the monetary policy, we share staff's views on the fact that the monetary policy has appropriately paused, in the face of low inflation, well-anchored expectations, and continued uncertainties on the outlook. We notice that inflation expectations have been revised downwards recently despite a context of expansionary fiscal and monetary stances. Moreover, what is perceived as an overall tight situation of the labor market did not translate into higher prices in a context of a flattened Philips curve. Could staff indicate what are the main drivers in its view of persistently low inflation levels and whether slack might have been underestimated? Could staff compare the drivers of such a subdued inflation to those of also persistently low inflation levels in the Euro Area? Going forward, prudent and clear communication on the Federal Reserve's policy path will be particularly important, to better anchor expectations and avoid large swings in financial conditions.

While the financial system resilience improved due to the reforms implemented after the financial crisis, attention should be paid to the rising medium-term financial stability risks highlighted in the report. In particular, attention should be paid to the high-level of corporate leverage, weakening underwriting standards, elevated valuations across a range of asset classes, and a surge in leverage loans. The recent tailoring of the US financial regulatory and supervisory framework does not address these concerns, and has generally resulted in an easing of regulatory constraints, as highlighted by staff. We encourage the authorities to strengthen their financial oversight regime and to ensure the comprehensiveness and responsiveness of their macroprudential framework. In particular, we agree with staff that there is room to strengthen the oversight of nonbanks and address data gaps, to have a full view of spillovers channels. In this regard, we would welcome staff comments on the shift in the FSOC doctrine, whose approach to oversight is now activity-based, and no longer entity-based. We also encourage authorities to introduce a comprehensive liquidity risk management framework for asset managers. Finally, we encourage the authorities to address the serious weaknesses identified by the FATF regarding entity transparency to make sure that foreign corrupt officials cannot hide their assets in the US.

On structural reforms, the report does not develop past analysis on competition intensity and the rise of market power. In an answer to our question on the WEO analytical chapter on rising corporate power, staff acknowledged that additional work would be needed to assess whether weaker competition law and policy aggregate caused larger increase in markups in the United States than in Europe over the past decade. Does staff consider additional work on that issue?

Mr. Raghani and Mr. Alle submitted the following statement:

We thank staff for an informative report and Mr. Rosen, Ms. Pollard, and Ms. Crane for their insightful buff statement.

We commend the U.S. authorities for maintaining a robust and historically long economic expansion. Alongside the record strong growth, other macroeconomic indicators display buoyancy; unemployment is at a 50-year historic low, inflation is subdued, and real wages are rising. Prospects are also reassuring with the economy expected to continue to grow above potential. The authorities should be encouraged to take advantage of such an opportune time to address the challenges facing the economy. In this vein, long-term measures are warranted to reduce the fiscal deficit and curb the public debt. Developments in the financial sector need to be monitored for potential reversal of conditions and risks to the economy and outward spillovers. As well, efforts on the social front should address equality/equity issues to sustain long-term growth. On the global stage, an imperative lies in easing trade tensions as positive negotiations outcomes would benefit the U.S. growth and the rest of the global economy. We support the conclusion of the Article IV consultation and would offer the following comments.

Additional measures are warranted to balance the fiscal costs of the Tax Cuts and Jobs Act (TCJA) with the expected yields. The TCJA was one of the major achievements of the current administration and was expected to be a source of important yields from an unleashed American economy. We are therefore concerned by the troubling outcomes presented by staff for the following reasons:

While on a positive note, the fiscal expansion has supported economic activity and hence a close to 3 percent growth in 2018, the fiscal cost of the TCJA is worrisome. Staff estimate it to rise to US$1.9 trillion (10 percent of current GDP) over the 2018-2027 period. In addition, the fiscal stance would contribute to exacerbate further the already upward trend of the public debt-to-GDP ratio. We urge the authorities to break this vicious cycle by bringing the fiscal position to a sustainable path.

According to staff, and contrary to TCJA's expected outcomes, the rise in investment that occurred in 2018 does not result from the corporate tax cut, but rather from an increase in aggregate demand. We understand from Mr. Rosen, Ms. Pollard, and Ms. Crane's buff that the authorities do not share this view. Do staff have further comments? Second, the TCJA was supposed to be paired with a number of deregulations to unleash the American economy. Do staff have any update on the major deregulations being finalized?

While noting the positive demand spillovers that the U.S. fiscal policy has had to other countries, a reversal in fiscal impulse could have adverse impact on overseas' indicators including sovereigns. This is a threat to some frontier market economies, including African countries which heavily issued dollar-denominated sovereign bonds in recent years.

Going forward, we welcome the assurances provided by the authorities on their objective to reach a federal primary surplus of 1.8 percent of GDP by 2029 through a reprioritization of Federal spending. The budgetary process should also be improved, including by avoiding government shutdowns, which adversely impact the U.S. economy and create negative outward spillovers for the global economy.

We welcome the authorities' approach to monetary policy which is geared towards quick and flexible adjustments to support the economy. Their readiness to adjust policies based on markets signals is praiseworthy; and the improved market sentiment and lessened risk aversion that followed such commitment by the Fed Chair in early January, is reassuring. Going forward, we share the views that the Fed's continued adherence to market data, the balancing of risks and a clear and forward-looking communication strategy are critical to prevent volatility in financial conditions and negative spillovers to the world economy.

While taking good note of a healthy financial system, we encourage the authorities to keep a close eye on sources of vulnerabilities. In this vein, high corporate leverage and significant stock of student loans require heightened vigilance. Steps should be taken to prevent abrupt changes in financial conditions while oversight institutions should be enhanced to respond to related threats. We are reassured by the authorities' actions in this regard, including efforts to better understand interlinkages and improve risk management practices within financial institutions; as well as steps taken to improve the effectiveness and efficiency of financial regulations.

While making effort to ease trade tensions, a combination of measures is warranted to address external imbalances. We understand that higher domestic energy production, relatively low returns on U.S. bonds and buoyant global equity markets have benefitted the current account in 2018. However, the authorities should take more structural measures to control the anticipated rise of the current account deficit. In this regard, we are reassured by the agreement between staff and authorities that trade restrictions alone would not address the U.S external imbalance. Therefore, we call for comprehensive measures to address the root causes of these imbalances, including reducing the fiscal deficit, stepping up supply-side reforms to boost productivity and competitiveness.

Regarding trade tensions and tariff hikes, we urge all parties to engage in trade negotiations while aiming win-win outcomes that are beneficial to global trade. An open, rules-based and well-functioning international system for trade is a public good. On the opposite, trade tensions fueled by unilateral decisions have a disruptive impact on the global economy with adverse spillovers to others as seen in recent developments.

While we commend the authorities for the rise in real per capita GDP to historic levels, more effort is warranted to improve social outcomes. The rise in real per capita GDP of almost 10 percent above its pre-GFC level is praiseworthy. We are of the view that the momentum of economic expansion should translate into improved social outcomes, which could further trigger a virtuous cycle of high productivity. We take good note of the progress made on health insurance coverage thanks to the Affordable Care Act. But, steps should be taken to improve outcomes regarding poverty, equality, income distribution, income mobility, especially for the middle class, and intergenerational equity. We encourage the authorities to take advantage of ideas put forward by prominent scholars to address those issues and implement reforms and programs accordingly.

Similar efforts are needed to respond to severe diseases and the drug pandemic, which contribute the most to diminish longevity and to the declining life expectancy compared to peer advanced countries. We also call for an emphasis on lifting the bottlenecks in the education system to maintain the long-term supply of productive skilled labor to the economy while reducing the macroeconomic costs of "poor" social outcomes.

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

Mr. Geadah and Ms. Abdelati submitted the following statement:

We thank staff for an insightful balanced assessment and Mr. Rosen, Ms. Pollard, and Ms. Crane for an informative buff statement. While the U.S. economy has enjoyed a long spell of expansion, prosperity has not been shared as evenly as it could. We share concerns raised by staff regarding the discouraging education and health outcomes, high poverty relative to other advanced economies, falling life expectancy, and increased income and wealth polarization. We consider staff's focus on the troubling social outcomes to be appropriate, as well as looking into the sustainability of the fiscal position, rising medium-term fiscal stability risks to the U.S. and globally, unaddressed financial vulnerabilities, and the need to support a stable trading system. However, we missed a discussion of climate change policies especially in light of their global implications.

As highlighted by staff, an abrupt reversal of current monetary policies poses downside risks to the U.S. and others. The lack of wage and price pressures has provided a respite from rising interest rates as policy makers continue to gauge the relative risks for inflation and employment outcomes. This has been also a welcome respite for the rest of the world.

However, the extended period of monetary accommodation has contributed to rising asset prices, and to corporate vulnerabilities that are elevated by historical standards. As noted by staff, not only no policy actions were taken to counter these risks, but there has been a steady easing of regulatory constraints as outlined in Box 2. The authorities acknowledge the potential vulnerabilities created by the prolonged credit expansion for the non-financial corporate sector. While they view the risks as mitigated by strong interest coverage ratios and healthy liquidity positions, nevertheless they acknowledge the risk of an increase in default rates and downward pressures on asset prices which would weigh on growth. Recognition of these risks will hopefully lead to policy actions in the near future. Staff also sees a need for greater clarity in how the operating framework of monetary policy will evolve. We note that the authorities do not see a need for change at this time, and wonder if there was a discussion of changes down the road.

U.S. public debt has been assessed on an unsustainable path for some time, and the authorities have opposed a medium-term fiscal plan as was recommended in the past. Rising health and social security spending needs will further add pressure on the fiscal deficit, which has been increasing since 2016. We recognize that the depth of the U.S. treasury market as well as its safe-haven status represent a mitigating factor for the high gross financing requirement of 29 percent of GDP. Could staff elaborate on the shift away from U.S. Treasuries, including by China and Russia, and the possible risks from a continuation of this trend?

Staff provides a sobering account of the deterioration in social outcomes. It is sad to know that nearly one-third of the population decide not to seek medical treatment because of high cost, when the U.S. has the highest per capita income among OECD countries. We also note that the share of the population without health insurance declined by half to less than 9 percent of the population. Nevertheless, life expectancy is low compared to peers and has recently declined. Educational outcomes are also weak compared to peers and relative to the high level of spending. We welcome and strongly support staff's recommendations in paragraph 21, which we consider critical to strengthen human capital, increase labor force participation, boost productivity, and raise growth.

We join the MD and others in calling for an end to trade tensions between the U.S. and China, and for working constructively to better address distortions in the trading system.

Mr. Jin and Ms. Liu submitted the following statement:

We thank staff for the comprehensive report and Mr. Rosen, Ms. Pollard, and Ms. Crane for their informative buff statement. We broadly agree with staff's assessment on the U.S. economic performance and appraisal on macroeconomic policies. The U.S. economy has experienced steady growth over the last decade, coupled with robust job creation. Unemployment rate has been low, and inflation pressure has remained subdued. Despite these dynamics, potential risks and challenges in the economy could undermine longer-term growth. Escalating trade tensions could also pose significant uncertainties and risks to the global economy, creating disruptive financial market volatilities, which will be detrimental to the U.S. economy as well.

On fiscal policy, the expansionary and pro-cyclical fiscal policy has further caused deterioration in the government's fiscal deficit, exacerbated public debt, and widened external imbalances. Meanwhile, the worsening public debt dynamics, in addition to aging related spending, could further constrain fiscal space to address social issues. Therefore, we agree with staff that policy measures should be taken to adjust the fiscal position and put public debt on a downward and sustainable path. We believe that such policy adjustments, together with other supply-side measures, should help create fiscal space to strengthen fiscal resilience, address social inequalities, and promote inclusive growth. Staff's analysis indicates that the fiscal cost of the U.S. tax reform is high. One year after the U.S. tax reform, the rise in investment is largely explained by demand-side effects rather than supply-side effects, and we take note of the different views between the authorities and staff on this issue. We encourage staff to continue to work on the issues such as the role of rising market power in explaining investment to tax changes. When analyzing debt sustainability, a more appropriate approach should be used to distinguish between stock and flow. We wonder what conclusions on debt sustainability can be made based on the Debt Service/GDP ratio and the Debt/National Wealth ratio. Staff's comments are welcome.

On monetary policy, against the backdrop of subdued inflation pressure and low unemployment rate, we are of the view that further changes in policy rate should be data-dependent and be based on objective judgement. Meanwhile, due to the significant spillover effects of the Fed's policy stance on the global economy, in particular its impacts on the exchange rate and capital flows in emerging market economies, close attention should be paid to market reactions. In this regard, effective and clear communication with markets is critical to avoid creating excessive volatility in financial markets and unexpected spillovers to the rest of the world.

On the financial sector, we agree with staff's assessment on the rising medium-term financial stability risks. Although the financial system appears healthy, historically high corporate leverage, expanding non-bank financial sector, and pro-cyclical regulatory policies are sources of concern. Strengthening the oversight of non-banks and data sharing among regulatory bodies is necessary to guard against financial risks. We would like to know the risk profile of the non-bank financial sector and its interconnections with the banking sector. Staff's comments are welcome.

We welcome staff's analysis and recommendations on social issues. The increased income and wealth polarization, falling life expectancy, and discouraging education and health outcomes are among the major concerns in the U.S. These have also resulted in negative effects at the macroeconomic level, including lower productivity and repercussions on the fiscal position. It is necessary to emphasize that the underlying problems in the U.S. economy are mainly caused by domestic reasons, especially the failure to compensate the loser by the winner during the globalization process. Therefore, such issues should be addressed through the adjustment of domestic structural policies. We agree with staff's recommendation to provide family-friendly benefits, expand health care coverage, reduce costs, and improve education to release the suppressed aggregate demand and allow more people to share the benefits of the decade-long expansion of the real economy.

On trade issues, we support staff's call for a more open, stable, and transparent rules-based international trade system. We also support the Fund's view that trade balance should be viewed from a multilateral, rather than bilateral, perspective. It is a serious mistake to resort to, or threaten to use, large scale tariffs to address bilateral trade issues. These unilateral and coercive approaches have seriously damaged the multilateral trade system and will backfire on the U.S. economy.

The U.S. is the most powerful country and one of the most advanced market economies in the world, but there is huge room to improve and reform. We fully share staff's concern about the countervailing duties proposed by the Department of Commerce. Currency manipulation should be judged by a neutral multilateral institution, such as the IMF, rather than by individual countries. It is also necessary to point out that market mechanism and fair competition in the U.S. economy have been eroded and distorted by excessive government intervention from time to time. The media has widely reported many cases, including the excessive use of national security, as a tool to interfere with normal market transactions and block foreign competitors, the formation of market power of big companies, the implicit collusion and conflict of interest between government regulator and private companies as revealed by the case of Boeing 737 MAX 8, and the repeated and abusive use of systemically important financial infrastructures as tools to impose disruptive unilateral sanctions. The labor market could be distorted by visible and invisible discrimination, which has put the minorities at a great disadvantage. The Medicare system has mobilized a large portion of national wealth and resources, but generated less satisfactory results as reflected by the declining life expectancy. The very long standing unresolved and controversial issue is the subsidy in American's agriculture sector. Agricultural products are a fundamental factor of input in the entire value chain. The subsidy is generating far-reaching effects that go far beyond agriculture itself. More alarmingly, a senator has recently filed legislation that would deprive some foreign companies' legitimate rights to patented technology. These various distortions and interventions could have reduced the domestic welfare and damage or distort American companies' competitiveness internationally.

We hope staff can do more in-depth analysis on these important structural issues. Staff's comments are welcome.

The representative from the European Central Bank submitted the following statement:

We thank staff Mr. Rosen, Ms. Pollard and Ms. Crane for their buff Statement and the Staff for their report and selected issues papers.

We fully support Staff on their view that the US should work constructively with its trading partners towards strengthening the open, rules-based international trading system. Resolving trade tensions should have the highest priority. In that respect we would like to point to the recent G20 Finance Ministers and Central Bank Governors Communiqué, which highlights the need to address intensified trade tensions and to improve the functioning of the WTO.

We broadly agree with Staff on the macroeconomic outlook of the United States. The economy is still growing above potential, unemployment is at historical lows, whereas inflationary pressures remain contained. However, economic activity is set to moderate as temporary tailwinds from sizeable tax cuts and higher government spending are fading.

Looking forward, risks to the outlook are tilted to the downside, exacerbated further by recent events. In particular, near-term downside risks have increased considerably with the re-escalation of US-China tensions, which could have a material impact on financial markets (such as an abrupt reassessment of financial market frisks and a sudden tightening of US and global financing conditions), create significant disruption to global value chains and lead to a precarious weakening of the multilateral trading system. Overall, trade and technology-related tensions with China together with pervasive uncertainty around US trade policy are increasingly weighing on market sentiment and business confidence, dampening growth prospects in the US and globally.

We concur with Staff's positive assessment of the financial system's health as a whole, while noting that medium-term financial stability risks have increased. We stress, in particular, the risks associated with record debt levels in the non-financial corporate sector and their deteriorating quality, as evidenced in the increasing share of corporate bond issuance rated at the lowest investment-grade rating (BBB). In addition to the Staff's analysis, we emphasise the risks stemming from the leveraged loan market, which has been increasingly characterised by highly-leveraged issuers, limited liquidity, and reduced creditor protection. High leverage and the weakening in corporate credit quality may lead to adverse macro-financial feedback loops in a scenario of a slowdown in economic activity or a tightening in financial conditions. Moreover, we agree with Staff that asset valuations remain historically high in several markets, suggesting elevated investor risk appetite.

On the external sector, we broadly agree with Staff's assessment of the US current account position, which appears moderately weaker than implied by medium-term fundamentals. Given the macroeconomic nature of the underlying saving-investment imbalance, we strongly agree with Staff that trade barriers are ineffective in addressing current account imbalances. Moreover, they are counterproductive in terms of raising living standards. We endorse Staff's view that addressing external imbalances requires a policy strategy which places public debt on a downwards path and adopts supply-side measures to improve US competitiveness.

We agree with Staff that the US fiscal position has deteriorated due to the recent pro-cyclical fiscal stimulus. The budgetary impact of the 2017 Tax Cuts and Jobs Act (TCJA), which was frontloaded in 2018, provided a temporary boost to economic activity but will continue to weigh on public finances in the medium term. Increasing aging-related spending will add to these pressures. We caution that the projected increase in the government debt level raises fiscal sustainability concerns and reduces policy buffers in the event of an economic downturn. In line with Staff's recommendations, we encourage the authorities to adopt revenue and expenditure measures that ensure the sustainability of public finances over the longer term. Such measures should also aim at raising medium-term growth prospects (including through public infrastructure investment), while also ensuring that concerns over social inclusion are considered.

We see merit in Staff's view that monetary policy should adhere to the principle of data dependence and clear, forward-looking communication. Clear and timely communication to financial markets is important to avoid undesirable volatility and mitigate the risk of sharp swings in financial conditions. We remain, however, sceptical about Staff's recommendation to aim at an overshooting of the inflation target. While inflation should over time both under- and overshoot the inflation goal in a symmetric manner, aiming ex-ante at an overshoot may be more complicated and less effective than described in the report. Looking further ahead, the ongoing review of the

Fed's monetary policy strategy, tools and communications should provide useful insights into how the Fed can best continue to deliver on its dual mandate.

Ms. Pollard made the following statement:

Good morning, everyone. I wanted to touch on a few issues that have been raised in the gray statements before we begin this morning.

Mr. Mojarrad, in his gray statement, reminds us of the importance of member countries meeting the obligations of the Articles of Agreement, an issue this chair has repeatedly stressed. Inn May 2018, the president announced that the United States was withdrawing from the Joint Comprehensive Plan of Action (JCPOA). Then in August, the president announced payment restrictions, which became effective in August and November. As the responses to technical questions mentioned, we notified the Fund of these restrictions in September 2018, in line with our obligations and in line with Decision 144.

Like other countries, we do not have a perfect record of notifying within the 30-day guidelines but try to do our best. Earlier this week, we were preparing a notification to the Fund, based on a May 2019 executive order. When we learned from the Legal Department (LEG) of Mr. Mojarrad's concerns, we paused and consulted with U.S. Treasury to ensure that we had a comprehensive list of restrictions, which we then circulated yesterday. As a result of Mr. Mojarrad's concerns, we have strengthened our procedures and hope that we will meet the 30-day deadline going forward. I appreciate that.

Several gray statements asked about the Federal Reserve's review of monetary policy strategy, tools, and communications that was announced in November 2018. The review takes as given that the Federal Reserve's statutory mandate will remain as it is and also takes as given the 2 percent inflation target. That said, it has two distinct parts. The first is looking at the operating framework. The second is the strategy review.

On the operating framework, the discussion has focused on technical aspects of policy implementation; that is, what interest rate to target and how. Traditionally, the Federal Reserve has used open-market operations to target the federal funds rate.

After the global financial crisis, in a framework where there are ample reserves, it has decided to shift to using the interest rate on excess reserves to target the federal funds rate. It has decided that it will continue that process. That is the part that has been mostly complete and where there will only be some technical adjustments. The review part is a broader conversation. Topics of discussion have been about how best to communicate the policy objectives to fulfill the dual mandate.

Finally, I want to highlight a few macroeconomic issues that have been raised that are relevant, not just to the United States but to other economies as well. One of those is the idea of how close the United States is to potential. The staff argue that we have been operating above potential for the last several years, yet we see that there is no indication of overheating in the economy, which has led us to think that there may be still some slack in the economy.

If you look at labor force participation rates, although they have risen in the past year, they are still actually below what they were prior to the crisis. This is true even when looking at prime age workers, those aged 25 to 54. This issue and also the issue of why inflation has been so persistently low did come up in conversations, particularly at the Fed, and so they were part of the Article IV discussions.

With that, I look forward to your remarks.

The Chairman noted that there had been no stricto sensu breach of the rules because there was not a hard-wired rule.

Mr. Meyer made the following statement:

I could now start, as one would usually do, by indicating how strong the U.S. economy is doing, what a strong position it is in—and, indeed, it is—and then go on to the risks. But I wanted to start differently and to start with the main issue that we all see.

We strongly share the staff's call to strengthen the international trade system toward a more open, more stable, and more transparent rules-based framework. Protectionist tendencies are not helpful. They can endanger welfare gains. Resolving trade tensions should—as basically all Directors have indicated—have the highest order of priority.

I am under no illusion that our report and the summing up will change the position that the U.S. President might have and his view. But maybe we gain traction—and this is what we should really do going forward. All those who understand and share the view that the staff has put out and that Directors share, and those in the U.S. administration should help to contain and to convince, so that the biggest issue that we all have to face at the moment might be at least mitigated.

I have two more points
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On the external assessment, there are many views. Fiscal consolidation being important, I wanted to make one point, that I appreciate is made in the report. That is the point that international trade is not a zero-sum game but, rather, enables win-win situations. That is the indication in paragraph 10. To reduce the current account deficit, that it will be also important to have supply-side reforms that improve productivity and competitiveness. I wanted to highlight that. It is important in the context of the external sector.

My last point is on the high and rising public debt. We fully share the view that fiscal consolidation is necessary, also in helping to reduce external imbalances. The list that the staff pointed out is appreciated by us. The elephant in the room—also mentioned by many Directors—is the question: Where is potential growth? How strongly can the United States grow? There are different views between the staff and the authorities. In this context, the composition and the quality of public finances will be key, given the troubling social outcomes that are being described in the report.

In view of the worrying findings on health, education, and poverty, we were somewhat surprised to learn that the authorities are planning to cut spending on these items further while simultaneously raising security-related spending. We would, therefore, be interested to hear more about that rationale from staff or from Ms. Pollard in her final remarks.

Mr. Mojarrad made the following statement:

Like many other Directors, we were very impressed by the quality of the report and the staff's candid assessments of economic dimensions of poverty, the opioid crisis, and other troubling social outcomes in the United States.

I would also like to thank Mr. Rosen, Ms. Pollard, and Ms. Crane for their informative buff statement and the clear articulation of the administration's perspectives. We also wish Mr. Rosen all the best and a quick recovery.

In our gray statement, we have expressed our views on key issues, but I would like to elaborate on a few points.

The snapshot pictures and the near-term prospects for the U.S. economy are very favorable. These positive trends have been in train for a few years, post-global financial crisis, but have been reinforced more recently by very supportive financial conditions, significant fiscal stimulus, and regulation relief. We agree with the staff that a host of factors—including an escalation of trade conflicts and the expected unwinding of the fiscal stimulus as early as next year and the election cycle uncertainties—are unlikely to support sustained 3 percent GDP growth over the medium term.

Risks to the outlook are tilting to the downside, a view also seemingly supported by the latest Fed communications. In our view, the Fed's long pause for an increasingly dovish undertone is appropriate under the current circumstances.

Let me also stress that monetary policy is not the right instrument to compensate for missteps in trade policy. In any event, the credibility of monetary policy and, hence, the Fed, is critically grounded in the Fed's longstanding independence and immunity from political interference.

In our gray statement, we raised the issue of U.S. sanctions on Iran. Before elaborating, I would like to express my gratitude to the Legal Department (LEG) staff for their professional views and hard work over the past two days and appreciate Ms. Pollard's clarification.

Following our query two days ago about the U.S. restrictions on Iran under the provisions of Executive Board Decision No. 144, Mr. Rosen issued a notification to the Fund, followed by the Secretary's notification to the Board, and a supplementary staff statement on the issue, all in quick succession late yesterday.

In addition to Iran, the notifications also covered the U.S. sanctions on Nicaragua and Venezuela under the provisions of Decision No. 144, which requires the members imposing restrictions to notify the Fund in advance whenever possible and as promptly as circumstances permit, but no later than 30 days after imposing the restrictions.

Yesterday's notification in all three cases was issued more than the 30 days after the adoption of the restrictions. I would appreciate the staff's clarification on the consistency of the notification with the provision of Decision No. 144.

Decision No. 144 covers restrictions that are solely related to the preservation of a member’s national or international security, but the determination of its legitimacy lacks an international legal context and is entirely at the discretion of the restrictions-imposing member.

The decision also stipulates that: “Unless the Fund informs the member within 30 days after receiving notice from the member that it is not satisfied that such restrictions are proposed solely to preserve such security, the member may assume that the Fund has no objection to the imposition of the restrictions.” Could the staff elaborate on the procedure leading to a Fund decision and any precedents?

To conclude, the recent delays have brought to the surface the shortcomings of this antiquated decision, dating back to August of 1952. This chair, supported by some other chairs, called for a review of the decision in a Board meeting a few months ago. As far as I know, no review has taken place in the last 67 years. Maybe the time is now.

Mr. de Villeroché made the following statement:

I will start by saying that the recent economic outlook that we see in the United States is impressive, with very strong growth, very strong developments in the labor market, and inflation remaining low.

We concur with the staff that we regret that the U.S. authorities are not taking advantage of this very favorable conjuncture to address the deep-rooted challenges that we see and which are well framed in the report. Those being: The rise of income inequality for the level of development of the United States; some poor social indicators, some of them even being more deteriorated than we expected; and macroeconomic imbalances, with a lack of savings in the economy at large; and the situation of the public finances. Let me come to some of these issues.

I will start with the public finances. We acknowledge that the question of the procyclicality of the fiscal stimulus could be a bit debated, since we have a huge uncertainty on potential growth and the output gap level. We have continued to think that it is procyclical and that the current fiscal deficit will need to be addressed sooner than later.

We think that more should be done on taxation to increase revenues in the United States. We see as well that the current tax reforms had gains for shareholders, but its impact on spending and investment—research and development spending and investment was not high enough and was not as expected. The quality of the stimulus may be questioned a bit.

Going to monetary policy. It needs to remain independent, but more broadly, data-dependent. We understand that all central banks are struggling with the current situation of inflation. We do not have much to comment on this. It came as a surprise that we did not have more inflation in the United States recently.

Coming to the financial sector, we see the rise of medium-term stability risks, as highlighted in the report, the high level of corporate leverage, a weakening of the underwriting standards, and the high valuation in a wide range of asset classes. The relaxing or the tailoring of regulatory rules could increase these risks in that context. The other side of the financial sector, as a whole, including non-bank actors, should definitely be the core of the strategy of the authorities.

I will end with the external sector. I associate myself with the remarks of Mr. Meyer. Using the threat of tariffs as a negotiation tool, has implications on global trade, on the global outlook, if it is used repeatedly. We do not think that it has positive implications as well on the rules-based multilateral trade system. We are highly critical of the logic of a zero-sum game on these issues.

Mr. Lopetegui made the following statement:

The United States should be commended for the impressive performance of its economy, which is experiencing the longest expansion in recorded history. As noted in the staff report, the damage caused by the financial crisis has been repaired. Unemployment is at its lowest level in 50 years. Real wages are rising, driven by higher productivity growth. Inflation remained subdued. The U.S. economy remains at the forefront of global innovation, not only in tech but also as demonstrated by the impressive expansion of oil and gas production, which will make the country an energy exporter in the near term, a development probably unthinkable a decade ago.

Especially in light of Ms. Pollard's comments, looking ahead, we would welcome more work on potential output in the United States and the effects of the tax reform and deregulation.

Despite the differences of view on some issues discussed during the consultation, we welcome the authorities' broad agreement with the staff on the importance of translating economic growth into improved social outcomes, remaining vigilant about financial stability risks, and reducing the public debt over time, as expressed in the buff statement.

The authorities recognize the important challenge of addressing public debt growth and aim at gradually strengthening the primary fiscal position. We welcome the policy plans mentioned in the buff statement. Like Mr. Mouminah, we are encouraged by the administration's aim to leverage further spending to generate substantial investments over the next 10 years, which will contribute to higher potential growth.

We are encouraged by the recent developments in the labor market which, if sustained, will contribute to an improvement of social indicators to consolidate a reversal of a trend that has been observed for some time. We agree with the authorities that a strong social policy stance with full employment. Looking ahead, improving educational outcomes and tempering health care costs constitute very important challenges.

With respect to the financial sector, there is agreement that U.S. banks are well capitalized and asset quality is good, although non-financial corporate leverage is high. We trust that the authorities will remain vigilant of emerging risks, including in non-banks, while pursuing the laudable objective of reducing the compliance burden on the smaller non-systemic institutions operating domestically.

We look forward to the results of the ongoing Financial Sector Assessment Program (FSAP), which will help clarify the risk map.

The external current account deficit remains moderate, contrary to previous expectations, and it is explained largely by the fiscal imbalance. We take note of the staff's external assessment and would concur that fiscal adjustment would reduce the U.S. external imbalance and the risk that it grows over time. However, it is important to highlight that domestic policy efforts in this direction in the United States need to be accompanied by demand-supportive fiscal efforts elsewhere, ideally in excess surplus countries with the appropriate space, to avoid downward output pressures globally.

We also support the call by the staff to encourage the United States and its trading partners to work constructively toward addressing distortions in the global trading system and to avoid relying on welfare-deteriorating tariffs.

Finally, I thank the American authorities again for their strong support in fighting illicit finance and corruption in Argentina.

Mr. Kaizuka made the following statement:

We take positive note that the U.S. economy is in its longest expansion in recorded history, with the unemployment rate being at a historical low level and inflationary pressures being subdued.

Since we issued a comprehensive, lengthy gray statement, I would like to highlight a few points for emphasis.

First, on the social outcomes, enhancing social welfare is a key macro-critical issue for the United States, and thus, it is sensible to put the focus on this particular issue in this Article IV consultation. Despite the positive macroeconomic outcomes, the benefits have not been shared as widely as they could have been in the country. This social challenge is one of the key drivers behind the current U.S. policy formulation on trade and immigration. Social protection is now a global common agenda, existing in advanced economies, emerging markets, and low-income countries (LICs).

We can learn much from certain policy recommendations in this staff paper and encourage the staff to continue focusing on the analytical work on social outcome issues in the U.S. Article IV and also in other Article IV consultations.

Let me turn to trade. We agree with the U.S. authorities that there are still high trade barriers and impediments, especially in emerging markets and developing countries (EMDCs). Reducing those barriers and enhancing the intellectual property rights protection and abolishing the mandatory technological transfer requirements are critical issues to enhance global growth through a free, fair, and open trade and investment regime. All the member countries, including my country, work together to reduce those barriers and impediments. Having said this, we strongly believe that those challenges should be addressed not in bilateral deals but preferably in the multilateral framework, including that of the World Trade Organization (WTO).

On the countervailing duties—I cannot be flexible on this particular point, because I have precise instructions from my authorities—we concur with the staff. The countervailing duties now proposed by the Department of

Commerce contain many problems, as indicated in the staff paper. Furthermore, we have a serious concern that the Department of Commerce could have room to make a different judgment from that of the U.S. Treasury. We are afraid that this would undermine the established trust and confidence for the currency authorities' consultation framework.

On top of that, we agree with the staff that the deviation in the real effective exchange rate (REER) from the estimated norm can result from a diverging cycle and monetary position but also from unbalanced macroeconomic policy and structural distortion, thus, the imposition of a duty could not be a remedy for the problem. In a hypothetical case, where the countervailing duties are to be adopted, their implementation and enforcement should be handled with extreme caution and in a very restrictive way.

Mr. Fanizza made the following statement:

I thank Ms. Pollard for her useful remarks, particularly on the monetary policy side, and for the buff statement. The staff has done a very good job. The paper is well crafted, entertaining, and that does not happen often. Kudos to the staff. I enjoyed reading it.

At the risk of sounding like a broken record, my main concern is monetary policy and the attention that we pay to it. The main recommendation of the paper is to wait to increase the rates. That is the bottom line. Now the debate, the discussion is about the arguments in favor and against reducing the rate. I would have liked to find a discussion, if not a clear position. A clear position would have been preferable, but at least a discussion and an input from the Fund to the authorities to get to the right decision. We should try to make an effort to play a more active role on monetary policy issues.

Believe me, I am not convinced that the interest rates should go down, but we see that, from yesterday's meeting, the hint is that it will happen, so we will need to deal with it. That is one issue that I wanted to raise.

The second is that I found the discussion on social issues interesting, well done. I cannot say that I agree with the staff's recommendations. These are incredibly complicated issues. What I appreciated is that the staff refrained from making any recommendation in the staff appraisal, which means that they understand that these are things that cannot be taken lightly. There are many macro economists that have sound techniques and look at large number of data in order to come to a conclusion, and we are not in that position. Nevertheless, the discussion is welcome.

I would have liked to have seen a more balanced approach, maybe a bit less of that, a bit more of monetary policy. I always have the impression that these issues crowd out monetary policy.

On fiscal policy, I liked the paper. But still, like one famous former colleague of ours puts it: Sustainability is in the eyes of the investors. What does that debt really mean? Furthermore, I would have liked to understand better why staff comes to that conclusion. The real issue is the output gap.

Again, I sound like a broken record. But now I think there is a broad consensus that we do not have the right tools.

Mr. Mahlinza made the following statement:

First, we see the strengthening of the U.S. economy as an opportunity to tackle pressing challenges, including improving social and distributional outcomes and deploying a range of policies to support low-income workers and families. We are, therefore, pleased with the authorities' commitment to more forcefully take on these challenges. We also share the Directors' views that an appropriately calibrated fiscal strategy, geared toward deepening revenue-enhancing reforms, is essential to create room for pro-growth and redistributive policies.

Second, we support the calls for decisive policy actions to reverse a deterioration of public debt dynamics. This is important, given the U.S. economy's systemic importance to the global economy. In this context, striking the right balance between the need to address the debt vulnerabilities while improving fiscal space for policies aimed at boosting productivity and competitiveness is greatly encouraged.

Third, we reiterate our call for urgent action to address the ongoing trade disputes in a constructive and cooperative manner to promote free and fair global trade. We encourage the U.S. authorities and their partners to continue working constructively to promote a rules-based multilateral trade system.

Lastly, we thank the staff for their analysis on the supply side of corruption and commend the authorities for their commitment to push forward with the prosecutorial efforts while working cooperatively with other jurisdictions to prevent the concealment of corruption proceeds in the United States.

Mr. Just made the following statement:

We congratulate the U.S. authorities on the longest economic expansion in recorded history. However, the downside risks have recently increased and are dominated by the periodic ratcheting up of the trade conflict, which jeopardizes the global economic activity. We share Mr. Meyer's general points on this issue. These risks also make the Fed's job even more complex, as reflected in the sharp turnaround and its signals on the monetary policy stance.

Going forward, a clear communication on the results of the monetary policy framework review will be important to prevent unintended spikes in market volatility, stabilize market expectations, and also to minimize spillovers to global capital markets and capital flows.

We reiterate our strong support for central bank independence that serves the United States, as well as many other countries, extremely well. We appreciate Ms. Pollard's earlier remarks on this.

The deteriorating fiscal position is also our main medium-term concern. The United States has a higher debt-carrying capacity due to the reserve currency status of the dollar and the ensuing debt of the U.S. Treasury markets. Nevertheless, it is important to put in place measures that stabilize and eventually reverse the trends long before the limit starts to be questioned.

We welcome the authorities' acknowledgement of the challenge but view their reliance on supply-side measures intended to permanently enhance the potential growth as overly sanguine. On the contrary, the productive core and medium-term growth potential of the United States may be a collateral damage of this policy.

The resource envelope of public infrastructure investment has dwindled. The opioid epidemic is undermining current productive capacity, while health and education outcomes point to a continuation of this trend. Despite the current enviable economic figures, the average American has little to show for it and may not in the future. Therefore, the envisioned expenditure cuts should be carefully designed not to deepen inequality further and to prevent the American Dream from becoming increasingly defunct.

Finally, we welcome the overall good health of the banking sector. By recognizing the principle of proportionality, we caution against further regulatory easing at this phase of the financial cycle but also to prevent the perception of a regulatory light approach in the United States from gaining traction globally.

As we have recently noted in our other discussions, the non-bank financial sector is a blind spot in our financial sector surveillance. Therefore, we encourage the staff to pay attention to mapping the interlinkages among the many segments of the very complex and sophisticated U.S. financial system during the ongoing FSAP. We acknowledge the significant data challenges and that this will require an extra effort by the authorities. However, the findings of such an exercise could prove extremely valuable for the U.S. authorities to help them integrate the fractured regulatory architecture into supervisory practice and, thus, mitigate risks to financial stability. It will also be valuable for the membership, as it would help to adapt the FSAP so that it continues to be of relevance.

Mr. Tombini made the following statement:

The U.S. economy has repeatedly surprised most skeptics with the robustness of its ongoing growth cycle. Very low unemployment and inflation rates have coexisted for years, keeping interest rates at historically low levels. This fortunate circumstance generates positive spillovers for the world economy. Nevertheless, questions regarding the sustainability and the long-term consequences of the ongoing expansion cycle emerge. Our views were detailed in our statement, so I will just take the opportunity to touch on three points.

First, as we see it, the broad economic strategy of the present U.S. administration is being predicated on three pillars; namely, the regulation and business facilitation, tax reforms, and infrastructure investments. Indeed, the three pillars seem closely related. To unleash the productivity gains expected from the friendly regulatory framework and the substantial tax cuts, it will be necessary to sustain a higher level of investment in infrastructure over time. In this case, the announced plans to revamp infrastructure will have an important macro-critical impact.

My first question to the staff is, where are we in this third leg of the strategy? I missed the analysis on infrastructure investment in the United States, although we know that not much has happened compared to the other two pillars. But I would like to see what our view is today on this issue.

Second, let me commend the excellent work done by the staff on the background paper, "Hysteresis in Labor Markets." The paper makes a convincing case for lasting impacts on the labor market caused by economic booms going beyond short-term demand side effects. In fact, the unusual dynamism of the labor market in the United States may be improving the allocation of scarce labor resources, privileging highly productive sectors with lasting supply-side gains. If that is the case, the challenge for the authorities is to facilitate this resource reallocation and to guarantee that adequate skills are available. I would like to see, what was the policy recommendation by the staff, taking also into consideration a point made by Mr. Villar on the potential for brain drain in attracting skilled labor into the U.S.

Third, a point made by Mr. Just and touched on by Ms. Pollard has to do with monetary policy. We see the low level of interest rates for a long time has raised issues concerning a potential decompression of term premia, leading to a snapback of the yield curve, therefore, having an impact beyond the United States. My question is, what is our expectation regarding this review of strategies, tools, and communication in the strategy for monetary policy in the environment of the effective lower bound?

What is the view of the staff on the makeup strategies? Do you think this is a credible alternative going forward? Because if that is the case, it will help to prevent spikes in the yield curve in the coming years when the normalization of monetary policy in the United States is resumed.

Finally, I would like to finish by echoing the point made by several Directors about the importance of U.S. commitments to a rules-based international trading system.

Mr. Jost made the following statement:

As stated in our gray statement, one of our main concerns is regarding fiscal policy. We believe that high and increasing debt levels pose important fiscal risks if they remain unaddressed. We appreciate that the buff statement acknowledges those risks explicitly, and we encourage the authorities to take appropriate measures, as sustainability concerns persist and room for maneuver is slowly melting.

Second, like others, we support the staff's view that the United States should work with its trading partners toward strengthening the open, rules-based international trading system. In an increasingly interconnected world, we acknowledge that important redistributive effects occur and often impact the political economy landscape in our countries. We are, however, of the opinion that such developments can and should be addressed through domestic policies, rather than by restricting free trade. Similarly, we believe that a policy strategy to put public debt on a downward path would also contribute to addressing external imbalances.

The United States' role in the global economy and international financial markets remains central. If domestic risks were to materialize, this could have important negative spillovers. We, therefore, welcome past and ongoing efforts to consistently adjust financial regulation and supervision. That being said, we would also like to acknowledge that positive developments in the United States also do have favorable spillovers. In that sense, and while we believe that there is a rationale to share the recent economic successes more broadly on the national level, we welcome and commend the authorities for the strong performance of the U.S. economy in recent years, as illustrated by the impressive job creation data.

Mr. Ostros made the following statement:

The U.S. office argues well and in good spirits, but I do think that the take on the U.S. economy from the staff has the upper hand in that discussion. It is very well rooted.

Like Mr. de Villeroché, I think it is very positive, the strong growth and continued success in the labor market, but at the same time, it is a pity that the U.S. authorities do not take advantage of this very strong conjuncture to solve some of the structural issues that they face.

First, I agree with the staff that fiscal adjustments are needed to put public debt on a downward path and, thereby, reduce the current account deficit and, thereby, also contribute to reducing global imbalances. Imposing trade barriers are ineffective in reducing trade imbalances and are very harmful to global growth. It seems like the message from the Spring Meetings of "do no harm" has not really been adhered to by the U.S. authorities. We see the tendencies of real consequences in the world economy, not least the slowing down in manufacturing that is troublesome for all of us. Fiscal tightening and reforms that improve productivity and competitiveness are more effective measures than tariffs. I do associate myself strongly with Mr. Meyer, Mr. Tombini, and others in their call for open and rules-based trade.

Second, I agree with the staff that financial stability risks are rising. Leverage in the corporate sector is building up. A large share of this debt is not borrowed directly from commercial banks but through issuance to the capital markets. At the outset, one could expect that the banking sector's exposure to this debt is limited. At the same time, we see the tendency of a loosening up of the regulations and supervision in some fields. All of them are well argued individually, but it seems to be a procyclical deregulation tendency. This reminds me of the period before the financial crisis, where we also thought that banks were insulated from the mortgage debt. What is the staff's assessment of the possible feedback effects of debt defaults on the corporate sector into the banking system? That would be interesting to hear.

Thirdly, I found the box on positive hysteresis effects for monetary policy shocks very interesting. It puts everything we learned as students upside-down. If such positive hysteresis effects are significant, one would assume that we can lower the non-accelerating inflation rate of unemployment (NAIRU) by conducting an expansionary monetary policy when the economy is operating at full capacity. It is a bit of an unusual take on monetary policy. In the U.S. case, I do not see that the risks are elevated. The United States has a very strong track record on monetary policy and high credibility. But it would be interesting to hear from staff—and not least Mr. Haksar—on what is the conclusion for monetary policy advice more generally from this box? Is this U.S.-specific? Is that something that you consider for the euro area or other major constituencies? That is an important discussion in that case.

Lastly, I expect that the tax reform has had some positive supply-side effects on growth, but it is questionable to what extent the reform facilitates inclusive growth. As I read the report, the staff have not found any signs of trickle-down effects so far. A thought experiment could be that, if we had used these types of fiscal resources not to have an unfinanced tax reform but to have put these resources into education, infrastructure, poverty reduction, my guess would be that the productivity effect would have been more significant than what we see from the corporate tax reform.

Mr. Trabinski made the following statement:

It is encouraging to see strong economic growth in the United States, complemented by high job creation and an increase in real wages. However, we take note of increasing risks, especially in the financial and fiscal sectors of the economy, as well as those stemming from trade tensions. As we issued a gray statement, allow me to elaborate on a few additional points today.

While the U.S. finance system appears to be capable of handling potential losses from corporate debt risk, rising medium-term risks to financial sector stability stemming from, an example, data blind spots or student loans warrant a special focus from financial sector oversight. We see merit in strengthening the supervision of non-banks and welcome the authorities' work on analyzing the existing vulnerabilities and tackling interlinkages. We also encourage the authorities to further strengthen the Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) requirements.

Second, while the United States has been playing a crucial role in promoting a rules-based international trade system, it is important, as indicated by staff and many of my colleagues who already spoke or will be speaking today, to foster thoughtful and continuous dialogue between the U.S. authorities and their main trading partners to avoid distortions. Specifically, it is crucial to abstain from measures that harm the global economy and undermine economic confidence. In this regard, we are grateful to staff for providing a detailed analysis of the trade tensions enclosed in the report and for issuing an excellent working paper on trade wars and trade deals, which explains the global impact of the potential changes in the U.S. trade policies.

Third, on a more technical side, we would appreciate it if the future tables on the balance of payments, selected economic indicators, and the Federal Government finances would include pre-2018 data for reference.

Finally, we appreciate the staff's elaboration on the supply-side measures that could raise potential growth while reducing the size of policy adjustment needed to put debt on a firm downward path. We would, nevertheless, appreciate a more detailed update on the progress achieved so far in introducing structural reforms, as this topic is only partially covered in the report, with some references to the 2017 Article IV consultation. Could the staff indicate whether any of the past recommendations on the structural side were picked by the authorities?

Also, we have a more general question regarding the proposed budget appropriation for public infrastructure. Could the staff shed some light on the potential structure of this envelope, specifically whether it would feed new investment projects or, rather, would be dedicated to infrastructure updating and upgrading.

Mr. Villar made the following statement:

We are encouraged by the buff statement of Mr. Rosen, Ms. Pollard, and Ms. Crane, in which they value the Fund's surveillance role and the constructive engagement of the staff and management with the U.S. authorities.

We take positive note of the recent economic performance by the U.S. economy, with a record-breaking period of growth, large productivity gains, low unemployment, higher wages, and tamed inflation. The report shows that U.S. public debt is on an unsustainable path and that fiscal imbalances pose salient risks for the medium-term economic outlook, with potential negative spillovers for other economies.

We broadly share the staff's analysis, that the reduction in the corporate taxes, while budgetarily costly, prove to have a relatively minor impact on capital formation. We take note from the buff statement that the administration believes that the investment-enhancing impact of the reform is only at its initial stage. A continued monitoring of results will be key to assess these alternative views and the need for policy adjustments.

We also agree with the staff and with the authorities that monetary policy decisions should continue to be data-driven. However, we are not convinced by the staff's argument that the path for policy rates should accept some temporary overshooting of the Fed's inflation goal. Data dependence and continued policy accommodation are appropriate recommendations that do not require overshooting the inflation rate target. Fine-tuning this target could, instead, create confusion and diminish the anchoring expectations process.

We strongly support the staff's assessment that for the global economy to function well, it should rely on a more open, stable, and transparent rules-based international trade system. We concur with the staff's view that trade barriers are likely to be ineffective at containing bilateral trade deficits and will be harmful for the United States and for global activity.

Trade policy uncertainty related to the imposition of tariffs can have a detrimental and long-lasting effect on global value chains, weaken the case for securing free trade agreements, and discourage FDI from the United States in other countries and from other countries in the United States.

A final point on immigration policy. We were surprised to see, in paragraph 27 of the report, a positive view on the skills-based immigration reform in the context of productivity discussions. This type of reform may imply discriminatory treatment of poorer and less-educated people. Moreover, from the point of view of its productivity impact, the spillover effects of this type of policy on source countries, brain drain from developing countries, should also be considered by the Fund.

Ms. Mahasandana made the following statement:

I will limit my comments to three points.

First, we congratulate the authorities on the resilient economic performance and the record low unemployment. Prudence reminds us that the authorities should use this opportune time to continue to address the unsustainable public debt and other long-term structural issues affecting productivity and inequality, while further promoting medium-term financial stability.

Second, we also would like to highlight that the favorable U.S. economic performance has its benefits to the global economy, including for members of our constituency, given that the United States is one of the leading trading partners and investors globally. Nonetheless, as the saying goes, when the United States sneezes, the global economy catches a cold. Therefore, we encourage the U.S. authorities to continue their efforts in addressing policy gaps to sustain the growth and macroeconomic stability in the United States, as well as to contribute to global stability.

We also welcome the staff's work to continue highlighting the spillover effect of the U.S. policies and would look forward to a richer analysis in future reports.

Finally, I would like to echo the points on international trade that many Directors raised in their gray statements and also in their oral interventions, that the United States has an irreplaceable role in promoting a rules-based international trade system. The U.S. commitment to the core principle of the WTO is paramount for the functioning of the world economy, particularly for countries that are dependent on trade activities. We join the staff and other Directors in calling for the United States to play this global leader role in resolving trade tensions.

Mr. Ray made the following statement:

It is in our training that the better things are, the more we start to worry. In that regard, I do worry a bit about the focus on the expansion's duration, partly because expansions do not die of natural causes. They are usually killed by an exogenous shock or a policy failure or a combination of the two. I worry a bit about the policy failure.

Also, this expansion—while relatively long by U.S. standards, not by some others—has been relatively slow. I do wonder whether that is partly contributing to some of the uncertainties that we see. At this point, that is the common theme that I take away, that there is just a lot of uncertainty around. There is uncertainty about where the U.S. economy is and uncertainty about policy. There is uncertainty about what potential is, what the NAIRU is, where the neutral rate is, why inflation remains so low, why we have not seen the productivity kick that we would normally see in a U.S. expansion. There is uncertainty over trade policy, the degree of sustainability or otherwise in the fiscal path, and monetary policy, as Mr. Fanizza stressed. With so much uncertainty around, it does make me wonder whether we are really prepared for and are really deeply thinking about how some of these things might play out and how they might affect the rest of us.

The Fund operates in a saturated market, providing policy advice to the U.S. authorities, most of which the U.S. authorities happily ignore. But the Fund's assessment of the United States is incredibly important to all of us, particularly given the U.S. global role. In this sense, I would encourage the staff to continue to explore the analytical uncertainties that are puzzling so many of us.

I want to emphasize four points.

On trade, I join others and strongly support Mr. Meyer's points. I do not think I need to say any more.

On monetary policy, it is clear that the Fed faces an extremely challenging task. It is going to be a complex period ahead over the next few years. It will be very difficult for them to navigate. Complicating this task, as Stan Fisher has pointed out on many occasions and Paul Krugman explained only yesterday, is this unusual pressure being put on the Fed by the ultimate U.S. authority. It does seem that there is a bit of a role for the Fund in calling that out and the possible implications of it.

On fiscal policy, it is not clear how unsustainable the debt position is. This seems to be an area where it would benefit from more analysis. There is an active debate outside of this building about where it is. The Fund's contribution to that should be firmly based in careful analysis.

Lastly, we found the staff's work on social outcomes rather novel, and there were very serious issues that were explored. We do wonder about the expertise of staff to make policy recommendations as specific as "to design Federal programs to provide greater support for science, technology, engineering, and mathematics programs," but we did find this part of the report interesting. Some of the outcomes, though—including, dare I say it, on life expectancy—reflect social preferences in the United States. But there is one that particularly concerned me that does not, and that is the thing that stood out. Despite record levels of real GDP per capita, income mobility continues to decline. A few decades ago, 90 percent of 30-year-olds earned more than their parents at the same age. These days, this is closer to 50 percent. This seems to be a very worrying trend for U.S. living standards and could have deep, longstanding implications, including political implications

Ms. Riach made the following statement:

Let me start by commending the authorities on the remarkable growth performance of the U.S. economy. But as Mr. de Villeroché said, it is unfortunate that the authorities have not taken the opportunity presented to make more progress on social outcomes. That being said, we do recognize some progress, in particular, on the employment indicators for those who have traditionally had lower engagement in the labor market. Therefore, we urge the U.S. authorities to build on the progress that has been made and to focus on the composition of public spending and also to avoid unnecessary economic shocks, including trade shocks.

On trade, I join other Directors in welcoming the staff's view that a well-functioning global economy needs a more open, stable, and transparent rules-based international trade system. I align myself with Mr. Meyer's view, that while our summing up will not change the president's position, nonetheless, there is an obligation on all of us to continue to make the case at every opportunity. The staff paper and the working paper on trade wars and trade deals are helpful here, including in providing some evidence for those discussions.

I did want to finally say a word about the report itself. Mr. Fanizza has said that he found it entertaining. It did feel like the tone of the report was somewhat different from many of the reports we look at. We appreciate the staff's candid analysis and advice. I recognize that this must be a tricky country to comment on and particularly a tricky report to write, given that, once again, we have such a divergence of views between staff and the authorities, including on growth prospects.

There is always a need for the Fund to balance the need for candid advice with the need to continue a constructive engagement with all our members, including our largest shareholder. We often talk about the need for staff to recognize the political economy in the countries in which they work, and this is just as true for the United States as it is for any other countries.

My message is that it is important for staff to pick their fights. I welcome the analysis on trade and the analysis on social indicators, but some of the tone of this report was, to my view, not quite right. To give a particular example, when we see the staff view that any successful fiscal package will likely require steps to institute a federal carbon tax, that just seems so far away from where the current U.S. administration is, that we do ask them to remember the political economy.

Mr. Siriwardana made the following statement:

Like many other Directors, we commend the authorities for achieving the impressive performance in the U.S. economy in the recent past. We would like to make three points for emphasis.

First, on the fiscal situation, the projection of the unsustainability of the public debt in the absence of significant changes on the expenditure side raises potential conflicts with the objective of addressing inequalities. This relies to a significant extent on expenditure programs, at least in its initial phases. Under the circumstances, the recommendations that will help streamline the entitlement programs are well taken. Making such programs more efficient is an unavoidable part of the solution. However, this needs to be accompanied by tax increases, according to the staff. Given that this needs to be accompanied by tax increases, given the overall move toward lowering taxes on all fronts, this does not seem to be a particularly realistic expectation. We wonder whether there is enough room to improve efficiency on entitlement programs without relying on tax increases. If not, the fiscal policy trajectory may be a cause for some concern. We invite the staff to comment on this.

On monetary policy, we find the case for a standing repo facility persuasive, as it provides a tried and tested mechanism for smoothing liquid fluctuations. However, the existence of such a facility does not automatically make an argument for a transition to the rate on this facility as the policy rate.

The federal funds rate has served the system well in this function. Just as in the case of flexible inflation targeting, a range, rather than a point target, gives the central bank a degree of flexibility in dealing with what it considers to be [TRANS HISTORIC ANGIENCE] without sending premature signals for a policy change. Could the staff elaborate on the benefits of the suggested change?

Changes in the trade strategy, as many Directors indicated, particularly with the bilateral actions beginning to replace actions through the multilateral framework, are rightly judged by the staff to potentially have adverse effects on all parties. Benefits for third countries from trade diversion may be offset by financial turbulence and the waning of confidence. Like the staff, we urge a return to the multilateral framework as a solution to trade issues, using the instruments within the framework or developing new ones to address unfair and distortionary practices. Needless to say, potential transitions to a complicated network of bilateral trade arrangements will prove to be extremely costly for all countries. In this context, we urge a speedy resolution of bilateral issues that, among other things, hinder the efficiency of the global settlement system.

Mr. Raghani made the following statement:

The U.S. economy has been growing strongly and is now in its longest expansion in recorded history. This performance is commendable, especially in times of ups and downs, witnessed in growth outcomes across advanced countries. Other U.S. macroeconomic indicators are also in good territory, and prospects are broadly favorable. There is no better time to take on the challenges that pose downside risks to the outlook, and the authorities should be encouraged to do so.

One of the most important of these challenges, as pointed out by most Directors, is the level of public debt. A credible strategy to bring it down requires decisive actions on the fiscal deficit. We welcome the authorities' planned reduction in spending in this regard. At the same time, an effort on the revenue side, given the long period of growth, could have helped the consolidation strategy.

We would encourage the authorities to undertake in due course an assessment of the yields of the Tax Cuts and Jobs Act against its high fiscal cost and to make changes, if warranted, to put debt on a sustainable path. In the same vein, the authorities should explore additional revenue measures, as those suggested by staff.

Regarding the financial system, we share the concerns raised by Mr. Ostros, Mr. Tombini, and others, on the rising medium-term risks to financial stability. While we welcome the staff's analysis in this regard and the preliminary assurances given in the buff statement of Mr. Rosen and his colleagues on the progress made in strengthening the financial sector, we look forward to a more in-depth discussion at the time of the Board meeting on the FSAP.

On social outcomes, the staff provided a detailed analysis and made recommendations regarding the further steps needed to address poverty, inequality, and issues related to income distribution and income mobility, especially for the middle class. These recommendations add to the other valuable policy options put forward by prominent scholars over the past years. The U.S. authorities are encouraged to tap this large amount of knowledge and take actions to further improve social outcomes for raising productivity and boosting competitiveness.

Finally, we join many other Directors in calling on the U.S. authorities and their trading partners to fully engage in negotiations to put an end to the current trade tensions and tariff hikes. The benefits of a more open, stable, and rules-based international trading system for all countries and for global growth is beyond dispute.

On the contrary, recent developments have shown clearly enough how disruptive trade tensions can be to the individual economies, let alone the adverse spillovers to others. We, therefore, call for concerted efforts to ease those tensions for the good of the global economy.

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

Mr. Mouminah made the following statement:

First, we commend the U.S. authorities for the exceptional performance of the U.S. economy, with solid growth, record level unemployment, and rising wages, especially for lower-income workers. But more efforts could be made to improve social outcomes. The robust growth of the U.S. economy continues to have a positive spillover effect to the rest of the world. However, we should remain vigilant to the risks.

Second, we take positive note that the financial system is healthy, and risks are being closely monitored. We welcome the clarification provided by the staff on the written response to our questions on the tailoring of the financial regulations. Tailoring is appropriate, as it is more important to focus on the robust oversight of the systematically important institutions. We look forward to continued initiatives to strengthen the oversight of non-banks.

Finally, on trade, like other Directors, we agree on strengthening the rules-based multilateral trading system. We welcome the recent efforts to resolve the trade tensions in a cooperative manner and look forward to a positive outcome in this area since this has a profound impact on the global economy.

Mr. Jin made the following statement:

We broadly agree with the staff's assessment on the U.S. economic performance and appraisal on macroeconomic policies. We have issued a gray statement and would make a few more comments.

The U.S. economy has experienced steady growth over the last decade, coupled with robust job creation and low inflation. We should congratulate the authorities for these achievements.

On fiscal policy, when analyzing debt sustainability, a more appropriate approach should be used to distinguish between stock and flow. We wonder what conclusions on debt sustainability can be made, based on the debt-service-over-GDP ratio and the debt-to-national-wealth ratio. The staff's comments are welcome.

On monetary policy, further changes in the policy rate should be data-dependent and be based on independent objective judgment.

We welcome the staff's analysis and the recommendations on social issues. It is necessary to emphasize that the underlying social problems in the U.S. economy are mainly caused by domestic reasons, especially the failure to compensate the loser by the winner during the globalization process. Therefore, such issues should be addressed through the adjustment of domestic structural policies, mainly.

On trade issues, we support the staff's call for a more open, stable, and transparent rules-based international trade system. We also support the Fund's view that the trade balance should be viewed from a multilateral rather than a bilateral perspective. It is a mistake to resort to or to threaten to use large-scale tariffs to address bilateral trade issues. These unilateral and coercive approaches have seriously damaged the multilateral trade system and will backfire on the U.S. economy.

We fully share staff's concern about the countervailing duties proposed by the Department of Commerce. We believe that currency manipulation is a concept that should be judged by a neutral multilateral institution, such as the Fund, rather than by individual countries. It is also necessary to point out that the market mechanism and fair competition in the U.S. economy has been eroded and distorted by some government interventions from time to time, including the excessive use of national security as a tool to interfere with normal market transactions and to block foreign competitors, the formation of the market power of big companies, the implicit collusion and conflicts of interest between government regulators and private companies, and the repeated use of systemically important financial infrastructures as tools to impose disruptive unilateral sanctions.

The existence of labor market distortions has put the minorities in a disadvantageous position. The efficiency of the Medicare system needs to be improved significantly.

Agricultural products are a fundamental factor of imports in the entire value chain, and America has the natural endowment and a comparative advantage in agricultural products, while its agricultural subsidies are generating far-reaching effects that go far beyond agriculture, itself.

We are also concerned that, recently, legislation has been filed that could deprive some foreign companies a legitimate right to patented technology.

These various distortions and interventions could have reduced the domestic welfare and damaged or distorted American companies' competitiveness internationally. We hope the staff can do a more in-depth analysis on these important structural issues.

Mr. Mozhin made the following statement:

We have issued a written statement; therefore, I can be very brief.

On fiscal policy issues, social policy issues, and especially trade policy issues, I fully share the views expressed by Mr. Meyer and also reiterated by many other Board members.

I also agree with Mr. Mojarrad, that the 1952 Decision No. 144 needs to be reviewed. The review of this decision is long overdue.

Finally, I have another technical question which I failed to raise in my written statement, and that is on the composition of the public debt in the United States. There are two measures of public debt in the main table on page 41. One is federal debt held by the public in percent of GDP, and that is 77.8 percent for 2018. Then another measure is general government gross debt which is 106.8 percent of GDP. The difference between the two is almost 30 percent of GDP. I am curious, what is the composition of that 30 percent? How much is the Fed? How much is the states? How much is the extra-budgetary funds, if any?

Ms. Levonian made the following statement:

Let me first congratulate the authorities for the continued solid performance of the U.S. economy, which really rests, among other things, on its dynamism, strong institutions, productivity, rule of law. Sustained and robust U.S. growth has important positive spillovers for the global economy and, needless to say, for our constituency. Canada, in particular, has benefitted from a long history of a strong partnership between the two countries, building on our common borders, history, as well as trade and investment. I am just going to focus on three points and be brief.

First, as others have mentioned, the global economy has been dealing with trade-related uncertainty for quite some time now, and it could get a significant lift if the trade tensions were to resolve. We urge the United States and its other trading partners to work together constructively and to recommit to the rules-based international trading system.

Second, the U.S. financial system appears overall healthy. While the banking system appears resilient, risks have increased in the corporate sector and non-bank financial institutions. Given the size and the interconnectedness of the U.S. financial system, it is important to monitor these risks closely and to analyze their implications. The ongoing U.S. FSAP will be a timely opportunity for this.

Lastly, we appreciate the staff's candid analysis and policy advice but would have liked to have seen a bit more elaboration in certain areas. For instance, the staff assessed the risk to the outlook as broadly balanced. While the important downside risks are clearly articulated, there is hardly any discussion of the upside potential that broadly balances the risks. The staff's comments would be welcome.

It would also have been useful to see more discussion on the appropriate policy mix in an environment of persistently low inflation and neutral rates.

With that, I wish the authorities very well.

Ms. Abdelati made the following statement:

I only want to make one point to echo what was said by several Directors—Messrs. de Villeroché, Kaizuka, Just, Ostros, Ray, and others—on the worrisome social outcomes, given the U.S. position in the world economy and the opportunity at this conjuncture to act to address important social challenges. We commend the staff for the coverage of this topic, and we hope to see more efforts by the authorities in these areas.

The Deputy Director of the Western Hemisphere Department (Mr. Chalk), in response to questions and comments from Executive Directors, made the following statement:[2]

Let me start with some of the fiscal questions. There were questions on whether the adjustment in the United States could be done through spending alone. We have done various different scenarios. We show one such scenario of adjustment in the staff report. We find it very hard for the United States to do the adjustment that will be needed purely on the spending side. This is why we advocate for revenue measures. The question is, how politically realistic is it that these revenue measures would come forward?

It is certainly true that the Republican administration and the Republicans in Congress are pretty strongly opposed to any kind of tax increase. They do not regard tariffs, by the way, as a tax increase, so they get a carve-out for that. But that belies where the political dynamics are in the United States. We have seen significant increases, for example, in the gas tax

[2] Prior to the Board meeting, SEC circulated the staff's additional responses by email. For information, these are included in an annex to these minutes.

at the state level, even in very Republican districts. We have seen quite a lot of bipartisan support for a carbon tax.

While it looks difficult for tax increases to come through, it is all part of a political economy as to what they are linked to. There is quite a lot of support on both sides of the aisle for increases in some form of energy tax, if it were used to fund infrastructure spending.

The one thing which does still seem to be an anathema in the United States is a federal VAT. That is where the really strong opposition is. But for carbon taxes—we have talked to the American Petroleum Institute, which has shifted its position in support of carbon taxes. The staff had produced a book around two years ago, extolling the virtues of carbon taxes, with significant coverage for the United States.

As Mr. de Villeroché had asked in his questions, there is, at the state level, quite a lot of support for environmental taxation, particularly cap-and-trade-type systems which, in the northeast and in California, have generated quite a bit of revenue.

That brings me on to infrastructure. Where are we with infrastructure? You may be aware that the U.S. has an infrastructure week every four or five months. It seems very difficult, from a political economy perspective, to get agreement though. The agreement is not on whether there is a need for infrastructure. Everybody agrees there is a need for infrastructure investment in the United States. That is both in new infrastructure but particularly in the maintenance of the existing stock of infrastructure. The problem is how to pay for it, with one side of the aisle insisting that the payments come through reductions in other spending items, particularly the discretionary/non-defense spending, which is really only a quarter of the federal budget. On the Democrat side, there is more appetite for revenue increases, particularly gas tax increases, to Fund infrastructure.

The president's budget does not include a large amount of new infrastructure spending. There is some reallocation away from the highway trust fund into more discretionary infrastructure spending. But there has been discussion, including during the Article IV consultation, of a significant increase in infrastructure spending. But those discussions broke down in May, so the prospects look remote for that.

In terms of the social spending plans of the administration, to be fair, the president's budget does have quite a significant cut in social spending proposed. This has not been legislated by the Congress. There is very little support in Congress for those reductions.

Their views is that there is a lot of inefficiency and fraud in the existing social spending programs of the United States. It is very hard to substantiate how much that is the case. Their second position is that they want to have much larger work requirements on certain social spending, which would certainly reduce the level of social spending.

We take a different view. Rather than work requirements, there should be more work incentives. We have highlighted in the report the need to get rid of some of the cliffs in social spending, which are strong disincentives to work, particularly at the lower end of the income distribution.

The third view from the administration is to push more of the funding of the social spending down to the state level. The way to do that is to basically assume block grants for a number of the social programs, particularly those food supplementary programs and Medicare, which would be given to the states but at a lesser level than the current federal funding or what the current expected federal funding would be for those programs. That pushes the obligations more to the state level. Then it is up to the individual states whether they want to meet those social obligations. There are, obviously, different experiences across the states, depending on the administration of those states.

None of that seems to really address the questions we have raised in the report about trying to reverse some of the negative social outcomes that we see in the United States.

Turning to monetary policy. Where is the review of monetary policy? The chair has expressed to us, and has expressed also in public, that the Fed views this change in monetary policy, strategy, and communications to be an evolutionary process. We do not expect large changes, but they are certainly looking at everything. What we may see coming out of it, perhaps, is some changes in their communications strategy and the modalities for communications. We have raised in the report some recommendations on communications, to move away from the dot plot and to have a more consistent forecast. There may be some discussion of whether they should ex ante commit to overshoot their medium-term inflation goal, particularly if they are at the effective lower bound, whether there would be some value in that. Maybe there are some different modalities for the balance sheet policy, particularly if they are at the lower bound, of different tools they might have on the balance sheet.

We are watching it carefully. We have been following some of the conferences that have been held. We expect, by the time of the next Article IV consultation, there will be some more clarity on what will come out of that, and we will report to the Board then.

In response to the question on the feedback from the corporates into the banking system, a cursory assessment would show that the banks really do not have a huge exposure to the high levels of leverage in the corporate sector. Much of this has been securitized and is being held by the non-banks. Banks also do not seem to have a very large exposure to the non-banks themselves, at least in a direct way. But this does get to the question of the data gaps in the system. We do not know what the interconnections and the interlinkages are between the banks and the non-banks. I do not think it is the fact that just the Fund does not know. The administration also has struggled to try to get their arms around that data. The Office of Financial Research has had a multi-year program to try to build a better picture of interlinkages and connections through markets, particularly through the non-banks and insurance. It is an open question. We are certainly looking at it in the FSAP. But there is a risk that we will find, if things go badly in the corporate sector, that some of those problems will end up somewhere on bank balance sheets. However, it may not necessarily be bank balance sheets in the United States. Perhaps on the bank balance sheets in some of the other countries around the table.

On the structural reforms, where are we in terms of the things that the staff have recommended over the years? The U.S. administration right now is focused really on two broad areas of structural reforms: deregulation and reducing taxes. That is the main game in town.

We are fine with deregulation. We see a very complex system of regulation, particularly at the federal and the state level, with overlaps between the two, where sometimes the federal regulations are binding, sometimes the states are binding. There is a lot of scope to streamline and reduce that. We have to be conscious of the side effects of those changes though, particularly for things like the environmental regulations and some of the labor market regulations. But we do see some scope to improve the system, and we have recommended that in the past.

On the tax reform, as we reported last year, there were positive developments in the tax reform that we supported in terms of reducing itemized deductions, capping interest deductions on mortgages, reducing the corporate tax rate, moving toward a cash flow tax, and allowing for expensing. Many of those things we supported. But there is still a big agenda of structural reforms that are outstanding.

On the other indicators of debt, we do look at many different indicators of debt. They all do not look great, and they are all certainly worsening. If you look at debt-service-to-GDP ratios in the United States, they have gone from around 25 percent to close to 35 percent from before the financial crisis to now. If you look at our Debt Sustainability Analysis (DSA), the traffic light box of the usual Fund template is pretty red. They do not score well on many indicators of gross financing needs, on the level of the debt. If we take a comprehensive look at different indicators of the U.S. fiscal position, they are concerning. However, they can finance that fiscal position, and they do have the fiscal space to expand the fiscal policy because they can finance at very low cost. But it does concern us that debt will go up and up. People do focus on the federal government debt, but if we also put a line in the staff report on the general government debt, including the unfunded pension liabilities, those are 140 percent of GDP. It is not a small number. You have to take quite an expansive look at what the obligations of the federal government are and the ability to pay those obligations.

There was a question on the risks and why do we see the risk as balanced? There are three areas where we do see upside. We see trade as a two-way risk. It is creating uncertainty now, and it is weighing on financial conditions now. Potentially, that problem could be resolved in a reasonable way, and that would be an upside risk to the U.S. economy.

Second, on the fiscal, we do not build in any increase in the federal spending associated with the sequester limits, the caps. We expect that somewhere between now and maybe October, there will be a political consensus to raise Federal spending, which we have not built into our forecast, and that would be another upside risk.

Then there is this question of tax cuts. We came out with a view from the tax cuts that there was relatively little evidence of supply-side effects from the tax cuts. However, it is also very early. We do see it as a possibility that once the tax regulations are fully in place and a lot of the uncertainty about how they operate diminishes, we could see a better picture on business investment, as the businesses endogenize those tax cuts. Our discussions with the corporations had a flavor of that, they were not doing much right now in terms of restructuring their operations because they still feel there is some uncertainty in the tax system, itself. But that does not mean that they will not act on those incentives that are in place in the tax system once they better understand them and once they feel that there is some stability in the tax system.

The Chairman asked the staff whether corporate profits had been repatriated as some in the U.S. administration had predicted.

The Deputy Director of the Western Hemisphere Department (Mr. Chalk), in response to further questions and comments, made the following additional statement:

> We have seen a book value repatriation of profit from the corporations. We have not seen that as a corresponding capital inflow in the United States because our assessment was that most of the money was sitting in the United States in the first place, that even money being held in an Irish bank, for example, was re-intermediated through the global financial system and finally ended up in U.S. corporate debt markets because they were liquid. We did not see a large capital inflow. We did not see an appreciation of the dollar. But the corporations have basically booked those profits, and they have freed them up. As we discussed in the staff report, a lot of that is being now used to change the capital structure of the corporations.

The staff representative from the Western Hemisphere Department (Mr. Leigh), in response to questions and comments from Executive Directors, made the following statement:

> I will address the question from Mr. Ostros and Mr. Tombini on hysteresis. Thank you for the questions about Box 9 and the accompanying working paper, which fits into an emerging constellation of evidence that economic booms and busts could have a longer-term effect than we traditionally expect.
>
> There has been work at the Fund by former Economic Counsellor Olivier Blanchard, former Chair Yellen, current Chair Powell. They have all alluded to this possibility and the emerging evidence.
>
> Why might that be? Why might recessions have longer-term scars on economies than we thought? Why might booms have longer-term effects? When there is an economic boom and there are more jobs, people gain very valuable work experience that is going to increase their human capital throughout their careers. More people who were formerly discouraged come in and get valuable work experience. Also, during the booms, there can be a

procyclical response of investment and investment into innovation and R&D. All of these things will have a long-lasting effect.

What are the policy implications? It is too early to come to a firm assessment. We need to do more analysis on what is driving, what are the mechanisms, how does this differ across countries? I would allow myself to make one tentative policy implication, which is that if there is hysteresis, then policymakers need to be asymmetric. When there is a downturn, they must be very rapid to stop the pain, to stop the long-term scars. But also, when there is an expansion going on, there is some scope for more accommodation than we would traditionally think. What does this mean specifically for monetary policy today? It is possible that continued policy accommodation could generate lasting positive supply-side effects, as those scarce labor force resources are allocated more efficiently and as participation increases. The challenge for policymakers is to keep vigilant and to judge when this margin of supply-side improvement is being exhausted.

There was one more question I will address from Mr. Mozhin on the arithmetic of the general government debt. Absolutely, 107 percent total general government debt, of which federal debt held by the public is 78 percent of GDP, and then the residual, those nearly 30 percentage points of GDP, that is mainly state and local government debt. That is 21 percentage points of GDP. The remaining 9 percentage points of GDP is in non-marketable debt. That is reported in the flow of funds. It includes items not included in federal debt held by the public, such as trade payables and certain commercial loans to the government.

The Deputy Director of the Western Hemisphere Department (Mr. Chalk) noted that the staff would be making a correction to make the risk assessment matrix consistent with the global risk assessment matrix.

The staff representative from the Strategy, Policy, and Review Department (Mr. Haksar), in response to questions and comments from Executive Directors, made the following statement:

To respond to Mr. Ostros' question, Mr. Leigh has put it very well. On the question of hysteresis and the implications of monetary policy, there is a discussion of it in the U.S. paper. It is a very interesting paper. There is growing literature on the topic as well. We will have to look at it closely and see whether this is something that extends in other cases as well. The paper is based on cross-country evidence, but we would like to see it being explored in more detail for the euro area and other contexts as well. That will be part of our ongoing work.

The staff representative from the Legal Department (Ms. Christopherson Puh), in response to questions and comments from Executive Directors, made the following statement:

I thank Mr. Mojarrad for his questions. These are very important ones, and I am very happy to have the opportunity to clarify these points for the Board.

On your first question, with respect to the 30-day period, I would like to clarify that Decision No. 144 does not establish a maximum 30-day period. What it establishes is a guidance under the term ordinarily within 30 days. Therefore, it is possible under the legal framework to go beyond that time.

With respect to your questions, as to the procedures when there are objections to the measures notified under 144 and the precedence that a legal framework has a procedural set of rules that apply to any objection when a member introduces or imposes exchange restrictions under Article VIII sections 2(a) and 3. This is contained in the rules and regulations under rule H, H-2 and H-3. Yes, there have been three precedents.

These procedures take the form of a complaint. The rule established that if a member considers that another member has introduced restrictions that are inconsistent with Article VIII, a complaint must be filed or can be filed. Then the Board promptly, upon receipt of the complaint, can start arrangements for consultations with the relevant members, and then the matter is brought to the Board for a discussion and resolution.

In the past, we have had three cases: one in 1979, another in 1986, and then in 1992. These took the form of complaints under rule H-2. The Board took the necessary actions and, following the consultations with the relevant members and the discussions at the Board, in those three cases, the measures notified by the member were approved by the Board.

Mr. Mojarrad made the following statement:

I just wanted to thank the clarification by the staff. Also, the explanation by Ms. Pollard this morning was perfectly acceptable to us.

On the procedures, I do not know if there is a timeline. It seems to me that other members have 30 days or more. This is not clear. But the whole point is that this decision is so outdated. There is a lot of ambiguity. Then we would just ask to review this, because many things are not really clear to us in case that the member is using this. That is what we ask for, in view of this decision.

Ms. Pollard made the following concluding statement:

Let me begin by thanking Mr. Chalk, Mr. Leigh, and their team for their engagements during these consultations. We have worked with Mr. Chalk for so long that we sometimes think he should be an honorary American, although his British humor belies that.

I also want to thank my Board colleagues, both for their thoughtful gray statements and for their discussions this morning. I could spend hours having a discussion, but we all have other things that we have to do today, so that may be for another time and maybe over a beer.

That being said, I want to pick up on several things. I appreciate Mr. Ray's comments on reminding us that other nations have actually had much longer expansions than this. His country is one that comes to mind.

I thank Ms. Mahasandana for noting the role of the United States. My colleague Ms. Levonian called us an elephant, and in many ways, we are an elephant. I would extend that to being difficult to ignore.

In listening to some of the comments today, I am reminded that we are very much an open, a transparent, an incredibly diverse country, both in terms of our people, in terms of our landscape; and despite the beauty of our people and the beauty of our landscape, we wear our warts for all to see. Like an elephant, sometimes we throw dung on ourselves, and it makes us easy to criticize. But this is incredibly important, and we would not be the people we are and would not be the country we are if we did not accept that criticism and use it to improve ourselves. So I appreciate that.

Mr. Lopetegui referred to the innovation of the United States, and Ms. Riach was talking about giving advice to the federal level that will not be taken. Yet our states are the areas where a lot of this innovation occurs. As Mr. Chalk mentioned, even on issues like the environment, there are many things going on at the state level and that focusing simply on the federal level, as you are required to do, means that you do not get to see some of that innovation that is going on. Often, it is at the state level where this innovation occurs, and then finally, kicking and screaming, it is brought up to the federal level. That will continue to be where we see changes over time.

I have just a few points on the economy. The economic data are very positive. Many of us are surprised at how long the expansion has continued and are trying to grapple with how long it will go on and what is behind that.

Yesterday, the first quarter current account data were revised down to show that there was actually a smaller deficit. It now has declined from the previous estimate of 2.8 percent of GDP in the first quarter to 2.5 percent of GDP. I just want to underscore the points made by Mr. Tombini and Mr. Lopetegui. That being said, we do realize that we need to address imbalances, and it will have to come from both surplus and deficit countries.

The issue on the supply-side effects of our tax reform is something that is an open question. We would be happy to engage with staff in the coming years on that.

Fiscal and debt sustainability, we recognize we need to address the trajectory of our public debt. This is an issue that is being discussed and will continue to be discussed.

On the financial sector, I want to make a point on leveraged loans that many Directors raised in their gray statements. I want to highlight that these loans are performing very well, with low default rates. That being said, there is much greater caution in the market now. We are not seeing an overhang of supply. As Mr. Chalk pointed out, many of these risks are not showing up in the banking sector. But this is something that we will engage with the FSAP team as we go through that process this year.

I just want to make a few points on trade, on countervailing duties, and then on social outcomes.

On trade, the Chairman mentioned on Wednesday in her trip report that she was a guest on *The Daily Show* this week. We appreciated that you took the time there to recognize that U.S. trade policies are aimed at addressing key distortions in the trading system, including subsidies for forced technology transfer and intellectual property rights. She did also mention that she disagreed with the imposition of tariffs, which I appreciate. But I want to highlight that these were imposed only after many years of seeking to address these unfair trade practices through other channels, including the WTO, and these failed to produce results. However, the objective of the United States is free and fair global trade. We are hopeful that we will be able to reach an agreement with our Chinese counterparts on mutually beneficial trade.

Then to the point raised by Mr. Kaizuka and Mr. Jin on these countervailing duties and currencies, I want to point out that the draft rule is open for public comments until the end of June, and then Treasury will be devising its methodology to implement the rule. Treasury has not made decisions yet on the details of the methodology but intends for it to be consistent with the analysis in the foreign exchange report.

I also want to highlight that, in the concluding meeting with Secretary Mnuchin, he did say that Commerce will look to the U.S. Treasury for the purpose on the currency part. We certainly hope that will be the case.

Finally, on social outcomes, let me begin by noting that, in the United States, we have never had a belief in economic equality. We have always believed in equality of opportunity. Therefore, our view has always been that there may be intragenerational inequities but that generations should have this mobility. In some ways, it pains me to hear the comments by Mr. Just and by Mr. Ray on the failure of the American Dream and this rising income inequality.

My own family's story is very much one of the American Dream. My father was an immigrant to this country. He had less than a high school education. He was always a blue-collar worker. He had six kids, of which I am the fifth. Every one of us went on to higher education. Therefore, we saw this huge mobility. As a mother of two, I worry about the future.

These are important issues. They are issues, however, that are being talked about and talked about loudly. You will certainly hear this more and more over the next year.

Progress is being made, as the prolonged recovery has raised living standards and wages, particularly at the lowest end and also with respect to minorities. But whether that will be enough or not, we will see.

Let me conclude by saying, although we do not often listen to the Fund, it is important for the IMF to contribute to the policy debates on key macro issues. Let me stop there and conclude, again, by thanking staff and thanking my Board colleagues.

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

The following summing up was issued:

> Executive Directors agreed with the thrust of the staff appraisal. They welcomed the continued robust performance of the U.S. economy, which is about to mark its longest expansion in recorded history. They noted the achievements of low unemployment, rising real wages, and subdued inflation. Economic prospects remain favorable and risks were viewed to be broadly balanced. Nevertheless, Directors observed that public debt is on an unsustainable path, trade tensions and uncertainties are continuing, and medium-term risks to financial stability are rising. Continued vigilance, prudent macroeconomic policies, and supply-side reforms would be critical to securing strong, balanced, and inclusive growth, generating positive spillovers to the rest of the world.
>
> Directors called on the authorities to address external imbalances through fiscal adjustment and supply-side reforms that enhance productivity and competitiveness. They encouraged the United States to work constructively and cooperatively with its trading partners to address distortions in the trading system and resolve trade tensions in a manner that promotes a more open, stable, and transparent rules-based international trade system.
>
> Directors underscored the need to ensure that the benefits of the strong economy are broadly shared. They considered it a priority to address rising income inequality and improve social outcomes. To this end, they encouraged initiatives to reform the educational system, healthcare, and social programs. Specifically, Directors recommended expanding the Earned Income Tax Credit, providing family-friendly benefits, and improving healthcare coverage while tempering costs.
>
> 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 possible options to better control entitlement spending and raise indirect taxes. They considered that these efforts would create fiscal space to expand needed investments in infrastructure and human capital. They also saw scope for further improving the budgetary process.

Directors welcomed the Federal Reserve's pause in interest rate adjustments. They agreed that any further increases in the federal funds rate should be deferred until there are clearer signs of wage or price inflation. In this regard, they appreciated the authorities' continued adherence to a data-dependent approach and clear, forward-looking communication. Directors also welcomed the authorities' readiness to consider refinements to the monetary policy framework following the Federal Reserve's review of its monetary policy strategy, tools, and communication.

Directors observed that the financial system appears healthy, with well-capitalized banks. However, risks are building up among leveraged corporations and, possibly, in the nonbank sector. An abrupt reversal of supportive financial market conditions could weigh on real activity and job creation, with negative outward spillovers. Directors emphasized the importance of enhancing the risk-based approach to regulation and supervision, strengthening the oversight of nonbanks, and addressing remaining data gaps.

Directors welcomed the authorities' voluntary participation in the Fund's enhanced governance framework on the supply and facilitation of corruption. They encouraged continued efforts to improve entity transparency and beneficial ownership information.

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

APPROVAL: October 6, 2021

CEDA OGADA
Secretary

Annex

The staff circulated the following written answers, in response to technical and factual questions from Executive Directors, prior to the Executive Board meeting:

Outlook

1. ***Could staff elaborate further on these differences of opinion with the authorities? In particular, we would welcome staff's comments on the authorities' view that the investment-enhancing impact of the tax reform is only in its initial stage and that efforts to reduce the regulatory burden would have a strong lasting impact on growth. (Lopetegui and Di Tata). Could staff comment on the reasons for this more optimistic outlook that the administration raises in the authorities' views and the buff statement?***

- Staff forecasts are based on current policies and envisage growth moderating over the medium term toward a potential of around 1¾ percent (as the effects of the fiscal expansion fade). The authorities believe that a 3 percent growth rate is possible based on current and proposed future policies, including further deregulation and an ongoing impact of the 2017 tax changes which will spur capital formation and productivity changes.
- Our preliminary assessment of the business tax changes in the Tax Cuts and Jobs Act (TCJA) is outlined in Box 7 and the referenced working paper. The impact on growth so far from the tax changes appears to largely arise from the demand side stimulus with little evidence of additional supply side effects. However, the effects of such tax changes may manifest in investment decisions over time. Staff will be revisiting the impact of the tax changes as more data becomes available.

2. ***We notice that the Treasury yield curve has inverted, which frequently constitutes a sign that markets are expecting growth difficulties down the road. Staff's comments on this issue would be welcome.***

- Yield curve inversion has been a reliable recession indicator in past cycles and may well have predictive power today. Indeed, the historical empirical relationship between the yield curve and GDP outcomes is already incorporated into the estimated Growth at Risk results that are cited in the staff report (showing rising risk of low or negative growth over the next three years). It is, however, also possible the reliability of the slope of the yield curve as a predictor of recession may have shifted post-global financial crisis given the structural changes that have compressed term premia globally (including balance sheet policies of systemic central banks, financial regulatory changes that have increased the demand for high quality liquid assets, and increased foreign ownership of Treasuries by foreign reserve managers and sovereign wealth funds).

3. ***This year's government shutdown illustrates the challenging political economy the United States is currently facing. Does staff believe that such occurences have a long-term structural impact on the economy?***

- Government shutdowns negatively impact economic growth and has negative outward spillovers on the global economy including by increasing uncertainty and eroding confidence and sentiment. It is difficult to identify a long-term structural impact on the economy.

Fiscal policy

4. ***We recall that immediately after the global financial crisis the Fund took a very firm stance on the need for decisive fiscal consolidation in most advanced economies, but at a later stage favored a much more lenient approach. Are we now running the risk of a similar shift in the institutional view? Staff comments would be appreciated.***

- Staff has consistently take a view that the path of fiscal policy in the U.S. is unsustainable and that adjustment to lower the primary balance will be needed over the medium-term to put the debt-GDP ratio on a downward path.

5. ***Why has the sizable fiscal stimulus not had the expected impact? Will staff update their assessment of the estimated impact of the Corporate Income Tax Cut? According to staff, and contrary to TCJA's expected outcomes, the rise in investment that occurred in 2018 does not result from the corporate tax cut, but rather from an increase in aggregate demand. We understand from Mr. Rosen, Ms. Pollard, and Ms. Crane's buff that the authorities do not share this view. Do staff have further comments***

- ***The authorities emphasize the beneficial effects of the new corporate tax regime on corporate investment. Could staff assess the relative strengths of these two sets of factors? Is there a reasonable scenario in which investment accelerates sufficiently to support the higher growth trajectory?***
- The fiscal stimulus has supported growth but, as discussed in the staff report and accompanying working paper, the effectiveness of the corporate income tax may have been eroded by countervailing factors such as trade policy uncertainty, the complexity of the new tax code (and possibly the lack of implementing regulations and uncertainties over whether the code will persist in its current form), and increased market power among corporates. However, the supply side effects of such tax changes may become more visible in investment decisions over time. Staff will be revisiting the impact of the tax changes as more data becomes available.

6. ***The TCJA was supposed to be paired with a number of deregulations to unleash the American economy. Do staff have any update on the major deregulations being finalized?***

- Deregulation has been a priority for the administration, with numerous actions having taken place in the environmental, financial, healthcare, and telecom areas. However, in some cases, the binding regulation is at the state level so it makes it difficult to assess the impact of these deregulation efforts on the economy.

7. ***Regarding staff's recommendation on public finances (i) we would be interested to hear whether staff sees consolidation options on the expenditure side, as the recommendations in paragraph 26 seem to focus mostly on revenue side measures. (ii) Could staff elaborate what 'chained inflation' refers to? What is the indexation base?***

- A balanced fiscal consolidation is needed that combines both revenue and spending measures. Revenue measures include those in paragraph 26 of the staff report but the report also argues for changes to social security and healthcare programs as well as policies such as skills-based immigration reform that will also support the fiscal position.
- Chained inflation here refers to chain-weighted CPI which changes the consumer basket each month to account for patterns of substitution as prices vary through time. Social Security benefit payments are currently indexed to the CPI for Urban Wage Earners and Clerical Workers which updates the consumer basket every two years. This measure of inflation has risen on average by about 0.25 percentage points more quickly per year than the chained CPI. Indexing benefits to the chained CPI would therefore reduce federal spending obligations by slowing the average cost-of-living adjustment in each subsequent year the benefits are paid.

8. ***The administration plans to reduce non-defense discretionary spending, in combination with healthcare and welfare reforms, to help stabilize public debt levels and return the primary balance to a modest surplus by 2024. Could staff comment on the possible characteristics of these measures and their implications for social spending and income distribution?***

- The administration's budget proposal argues for eliminating duplicative or inefficient programs, defunding lower priority programs or those that lack measurable outcomes (e.g., some health profession training programs or the Community Development Block Grant), introducing work requirements for certain programs, and improving control of the payment of various benefits to reduce fraud. Insofar as such efforts strengthen the effectiveness and efficiency of the safety net, support labor force participation, and allow for a reprioritizing of spending to the most effective programs this could improve social outcomes. However, there is a risk that such changes may either generate less savings than forecast in the budget or exclude vulnerable citizens from social assistance programs.

9. ***We would welcome staff's comments on the decomposition of the fiscal policy gap of -0.4 percent of GDP for 2018 between its domestic and foreign components.***

- The -0.4 percent (net) fiscal policy gap in the EBA assessment has a contribution of -1.0 p.p. from domestic fiscal adjustment offset by +0.6 p.p. from foreign fiscal adjustment.

10. ***While we agree that the authorities need to address the fiscal deficit, we would be interested in staff views on the factors that need to be take into account when determining US debt sustainability. Staff do mention mitigating factors in the annex to the report, but we wonder if they shouldn't place more weight on the fact that the US is a global reserve currency. Would this mitigating factor paint a less concerning picture about US debt? We would also be interested in staff views on the ongoing academic debate on debt sustainability.***

- The reserve currency status of the USD has provided strong demand for U.S. Treasury debt and gives the U.S. fiscal space. However, staff views the expected path of debt under current policies to be unsustainable and, over the medium term, the U.S. will need to undergo an important fiscal adjustment to put the debt-GDP on a downward path over the medium term.

11. ***We welcome staff's comments on the progress of the budget plan, and the impact on public finances. We also seek staff's comments on the traction of Fund advice on addressing the US public debt, and the feasibility of the proposed policy options.***

- A spending deal for the 2019-20 fiscal year is currently being negotiated in Congress. There is general agreement in Congress and the Executive that the public debt is on an unsustainable path and that a sustained improvement in the primary fiscal balance over the medium term will be needed. However, there are important differences of view on the policies that should be undertaken to achieve this adjustment (as noted in the staff report, the administration prefers to undertake the adjustment entirely on the expenditure side).

12. ***Even though the increase in the debt ratio seems to be moderate, it is expected to have a significant impact on interest rates, particularly at the short end. The yield curve is projected to flatten significantly as a result, although it will remain positively sloped. Could staff provide an intuitive explanation for this development?***

- Staff's interest rate projections are driven by the inflation-employment trade-off at the short end of the yield curve and an expected decompression of the term premium feeding into longer term interest rates.

13. ***We wonder if the debt sustainability assessment is relevant for the US, or whether it may be worthwhile to consider how other factors such as market depth of US Treasury or investor profile would impact US debt sustainability. While we***

certainly welcome the candor of the staff's assessment, we would have expected a stronger analytical background to explain the labeling of the fiscal position as "not sustainable", given the US prominence in financial markets and the global economy. We would welcome staff's comments

- The deep and liquid market for US Treasury securities and the U.S. status as a reserve currency offer the U.S. an ability to finance its fiscal deficits at low cost. However, staff view is that a continually upward path for the debt-GDP ratio in an indication the current fiscal policies are unsustainable (even though the U.S. currently has the fiscal space to pursue such a set of policies).

14. We appreciate the menu of policy options suggested by staff to address the unsustainable fiscal position and the shortcomings of the U.S. budgetary process, but note that the staff report does not give a sense of the authorities' views on these recommendations. Staff comments would be welcome.

- The authorities do not intend to increase federal taxes to achieve the adjustment outlined in the President's budget. Rather they believe reductions in non-defense discretionary spending will be able to achieve their targeted adjustment. On the budgetary process, the administration supports an increase in the debt ceiling but did not provide a view on other recommendations for changing the budgetary process (noting that these decisions are with Congress and not the Executive).

15. On carbon pricing, it would be helpful to cover the mechanisms created at the state levels, such as California, to inform the potential articulation between federal and state levels carbon pricing mechanisms – staff comments are welcome.

- California has a cap-and-trade program for carbon dioxide that applies to large electric power plants, large industrial plants, and fuel distributors (which make up around 85 percent of California's total greenhouse gas emissions). Emission allowances are issued by both free allocation (based on the efficiency of each plant) and quarterly auctions. The system applies to CO_2, CH_4, N_2O, HFCs, PFCs, SF_6, NF_3 and other fluorinated greenhouse gases. The emission targets are set to be halved between 2015 and 2030.
- In addition, Connecticut, Delaware, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Rhode Island, and Vermont have formed a Regional Greenhouse Gas Initiative which limits carbon dioxide emissions from power plants through a cap-and-trade program. The emission allowances are distributed via quarterly auctions and the cap is targeted to decline by around 40 percent between 2015 and 2030.

Monetary policy

16. Could staff assess the systemic effects of the changes being considered by the Fed in the context of the monetary policy framework review?

- So far there are no concrete proposals to changes to the monetary policy strategy, tools or communications arising from this review. Certainly, given the importance of the Fed in the global economy and its potential impact on policy and market expectations, there could well be systemic effects. However, Federal Reserve leadership has indicated they expect the outcome of the review to evolutionary without large shifts in their framework.

17. Given recent developments and a slowing of domestic demand growth has staff's assessment of the current stance of monetary policy changed?

- Global uncertainties and the lack of visible inflationary pressures provide a strong case for a wait-and-see approach to policy. This will allow policymakers to garner more information on the likely impact of policy uncertainties and judge whether there are more tangible underlying signs of wage and price inflation. The Fed is advantaged by the fact that inflation expectations are well-anchored, there is a flat trade-off between slack and inflation in the U.S., and over the past several years the idiosyncratic shocks to inflation have been predominantly to the downside.

18. Keeping in mind the difference of views on the potential growth rate, could staff comment on why inflationary pressures are subdued in such an output gap scenario? Is there merit in recommending gradual increases in the policy rate proactively, both in anticipation of inflationary pressures building up and to create more policy space in the event of downside risks materializing?

- Subdued inflationary pressures are a product of a number of factors including a relatively flat Phillips curve, lower healthcare inflation (partly attributable to the changes under the Affordable Care Act), and a series of idiosyncratic relative price shocks. Abdih et. al., 2016, "What is Keeping U.S. Inflation Low: Insights from a bottom-Up Approach," IMF Working Paper WP/16/124 provides a summary.
- At this stage, the downside risks to inflation and the asymmetries posed by the effective lower bound argue for policy rates to be set in a way to allow some temporary overshooting of the Federal Reserve's inflation goal. Given the apparent lack of inflation momentum in recent data achieving such an overshoot will likely require leaving the federal funds rate at current levels, at least for the next few FOMC meetings and possibly beyond. Staff's baseline forecast anticipates growth to be above potential both this year and next and both core and headline PCE inflation to modestly overshoot 2 percent in 2020.

19. Could staff discuss the reasons behind the flattening of the Phillips curve, as well as the level of the natural rate of unemployment used to calculate the unemployment gap in Box 8?

- The Phillips curve has been flat but stable since the mid-1990s largely as a result of the strong anchoring of inflation expectations and the credibility that has been built up by the Federal Reserve. The natural rate of unemployment used to calculate the unemployment gap in Box 8 is the series constructed by the congressional budget office.

20. ***Also, could staff clarify what is meant at the end of paragraph 36 by saying that "the decisions on the size of the Fed's balance sheet are technical in nature and not to be interpreted as a change in the monetary policy stance"?***

- The FOMC's balance sheet normalization principles indicate that the Fed is not using changes in the pace of the run-down of its balance sheet as an active tool to change monetary policy conditions. Rather their objective has been to allow the balance sheet to decline passively while minimizing the impact on market interest rates and the yield curve. The Fed sees the level of the Fed funds target range as the main indicator of the policy stance.

21. ***Officials did not want to pre-empt the broad-based assessment of monetary strategy, tools, and communications that was already underway but did expect the findings of this review to be considered by the FOMC in the latter part of this year and could lead to evolutionary changes in the framework. Could staff comment on their understanding of the timeline of the review?***

- The review includes outreach to and consultation with a broad range of people and groups interested in the U.S. economy. The Reserve Banks have been holding a series of "Fed Listens" events around the country, with a town hall format, to hear perspectives from representatives of business and industry, labor leaders, community and economic development officials, academics, nonprofit organization executives, and others. In addition, the Federal Reserve System sponsored a research conference on June 4-5, 2019, at the Federal Reserve Bank of Chicago, with academic and non-academic speakers from outside the Federal Reserve System.
- In the coming months, the Federal Open Market Committee will discuss economic research and the perspectives offered during the Fed Listens events and their findings will be reported to the public during the first half of 2020.

22. ***Could staff elaborate on the benefits of returning to the point target at this conjuncture and the analysis that supports this recommendation?***

- The Fed successfully signaled its monetary policy stance through announcing a point target up until December 2008. Central banks commonly express their policy rate in terms of a single rate as opposed to a range as this provides the greatest clarity to markets and the wider economy on the expected policy stance (and avoids ambiguity about where within the range the central bank prefers to keep the policy rate). Clarity supports the transmission of policy along the yield curve as markets need only focus on the future level of the target rate (which should in turn reflect emerging data relevant to the growth and inflation outlook) as opposed to the possibility of a change future level of short-term interest rates within a target range for the policy rate.

23. ***Could staff comment on why they nonetheless see a need for greater clarity of the expected evolution of the operating framework for monetary policy?***

- Providing markets greater clarity on the nature of the medium-term operating framework that the Federal Reserve will deploy will help markets understand better how they can manage their liquidity and organize their liquidity management functions. This will aid monetary transmission through reduced interest rate volatility and more stable money market liquidity conditions.

24. ***We note the authorities' concerns regarding staff's recommendation to publish the central economic scenario in the quarterly monetary policy report, given that such scenario can be misinterpreted as a firm view. We welcome staff's comments and further elaboration on this recommendation.***

- To bolster its communication efforts, the Fed could consider publishing a quarterly monetary policy report, that is endorsed by the FOMC and which conveys more detail about the majority view of the FOMC on the outlook, policies, and the nature of uncertainties around the baseline. Such a report may also convey dissenting views within the FOMC as well as broader information on how the FOMC thinks about policy reactions in plausible, non-baseline scenarios. This would complement the "dots" (i.e., the individual FOMC member's quantitative assessment of future macroeconomic variables and policy interest rates) and provide a more systematic way for the Fed to convey the majority FOMC view. It is not intended to be a invariant predictor of future policy and the FOMC would remain data dependent, altering its path for policy rates as the outlook for employment and inflation (as well as the distribution of risks around that outlook) change through time.

25. ***We are somewhat surprised that the report does not even mention the possibility of a rate cut. We would have liked staff to discuss the arguments in favor and against it. We would appreciate staff comments on the issue.***

- Global uncertainties and the lack of visible inflationary pressures provide a strong case for a wait-and-see approach to policy, pausing further changes in monetary policy to give policymakers time to gauge the balance or risks to inflation and employment. Staff's current baseline envisage an economy that continues to grow above potential in 2019-20 and inflation that rises slowly above 2 percent. However, if the outlook were to deteriorate relative to this forecast, as some of the downside risks identified in Box 8 materialize, then the case for a reduction in the policy rate would strengthen. Similarly, if there were greater evidence that inflation expectations were drifting down, this could also motivate a reduction in the policy rate.

26. ***We welcome the decision by the Federal Reserve last November to conduct a broad review of its strategy, tools, and communication practices. We look forward to the results of this important undertaking. The review was inspired and informed by the best practices in other advanced economies. In this respect, do staff think that an***

independent review by external experts rather than an internal exercise would be even more useful?

- The review will draw on the views and perspectives of a broad range of people—including representatives of the business community, labor leaders, academics, think tanks, nonprofit organization executives, among others. These views and perspectives are being solicited through a series of Fed Listens events around the country. At the same time, the Federal Reserve system recently sponsored a conference at the Chicago Fed, with presentations from academic and experts from outside the Fed on their assessment of the Fed's strategy, tools, and communications. A broad range of views from outside of the Fed are being brought to bear and, given the nature of the review, this appears to be a more appropriate structure than an independent review by external experts.

27. Could staff indicate what are the main drivers in its view of persistently low inflation levels and whether slack might have been underestimated? Could staff compare the drivers of such a subdued inflation to those of also persistently low inflation levels in the Euro Area?

- Low inflation levels are a product of a number of factors including a relatively flat Phillips curve, lower healthcare inflation (partly attributable to the changes under the Affordable Care Act), and a series of idiosyncratic relative price shocks. Abdih et. al., 2016, "What is Keeping U.S. Inflation Low: Insights from a bottom-Up Approach," IMF Working Paper WP/16/124 provides a summary.
- Examining different measures of labor market slack does little to change the contribution of slack to wage growth as we broaden the concept of slack (see Abdih and Danninger, 2018, "Understanding U.S. Wage Dynamics," IMF Working Paper WP/18/138).
- Abdih et. al., 2018, "Understanding Euro Area Inflation Dynamics: Why So Low for So Long?" IMF Working Paper WP/18/188) documents that, despite closing output gaps and tightening labor markets, core inflation has remained low in the euro area primarily due to the persistence of inflation outturns (even as slack has fallen). In the U.S., inflation is much less persistent but, rather, idiosyncratic relative price shocks that have been skewed negative have played a bigger role in lowering inflation outcomes.

Exchange rate

28. We would like to know staff's candid view on the possibilities that the equilibrium REER would be used for decisions on countervailing duties which would deviate from the original and fundamental purpose.

- As the staff report indicates, allowing for the imposition of countervailing duties on countries that are viewed as using currency undervaluation as a subsidy to their exporters would raise significant questions of how to judge the degree of such undervaluation and the consistency of such an approach with international commitments, including at the WTO. It may also have implications for the conduct of monetary policy and further escalate trade disputes.

- Staff has consistently highlighted the importance of multilateral approaches to resolve trade disputes and global imbalances. External assessments, including of exchange rates, need to be undertaken in a multilaterally consistent way, taking into account countries' macroeconomic and structural conditions. The Fund's ESR provides that multilaterally consistent approach. Deviations in the CA or REER from estimated norms can result from diverging cyclical and monetary positions, but also from unbalanced macroeconomic policies and structural distortions.

Trade

29. Box 4 notes that an important step forward in the global trading system could be made if a U.S.-China trade deal is able to multilaterally eliminate some existing trade restrictions and distortionary policies. Quantification of the positive impact that such a trade deal could generate would be a useful addition to the discussion and could help with gaining traction on trade issues. Staff comments are welcome.

- Analysis published by staff has pointed to the benefits of multilateral trade liberalization. The November 2018 report for the G-20 on Strong, Sustainable, Balanced and Inclusive Growth indicated that reducing trading costs for services by 15 percent could increase G-20 GDP by about ½ percent over the longer term, with those countries with high shares of services in their trade benefitting the most.

30. Staff's analysis shows that the Administration's current approach is unlikely to be successful given tariff measures are ineffective at containing bilateral trade deficits. Did staff discuss with the authorities' alternative approaches to achieving their objectives?

- Staff encouraged the authorities to work constructively with trading partners to address distortions in the trading system, including addressing the need for the multilateral trading system to adapt. At the same time, staff argued for a reduction in the fiscal deficit as a means to lowering the U.S. external imbalance.

31. We note that the Staff assessment is that the U.S. will become a net exporter of petroleum products by 2022. We understand that the authorities' view is that the US will become a net exporter by 2020. It would be helpful to understand what is driving the difference between these projections. Staff comments are welcome.

- According to the EIA, the U.S. is set to become a net exporter of energy by 2020 and a net exporter of petroleum products by 2021 (this has been corrected in the staff report from 2022). However, prior to 2021 the U.S. is projected to become a net exporter of petroleum products on a monthly basis (i.e., in December 2020).

32. Could staff comment on the timeline for approval of the U.S.-Mexico-Canada Agreement (USMCA)?

- On Thursday, May 30th, the U.S. Administration submitted to the U.S. Congress the draft statement of administrative action. Under Trade Promotion Authority, at least 30 days after this date must pass before the Administration can submit to Congress the implementing legislation. Please refer to the Congressional Research Service (Figure I) for the steps and timeline that would then follow.
- Mexico signed the USMCA on June 19, 2019.

33. We thank staff for the Working Paper on trade wars and trade deals which provides more analytical heft to the assessment of economic costs of trade wars, the risks associated with a trading system fragmentation, and the value chain disruptions. The main findings are summarized in Box 4 of the Staff Report and normally, the in-depth analysis would be part of the report as a Selected Issues Paper. Could staff comment why they chose a different format in this case?

- For a number of years the U.S. has issued the analytical work underpinning the Article IV consultation as working papers rather than as a Selected Issues Paper.

34. We would like to hear how staff discussed during missions with the administration to recommend it of not taking bilateral trade actions?

- As highlighted in the staff report, staff encouraged the authorities to work constructively with trading partners to address distortions in the trading system, including addressing the need for the multilateral trading system to adapt. At the same time, and as mentioned in the report, staff emphasized the importance of a well-functioning WTO dispute settlement system.

35. We would like to invite staff's comments on the possible impacts of the effectuation of USMCA on the global and U.S. economy as well as the impacts of imposition of tariffs on imports from Mexico.

- The reduction in trade uncertainty that would come from approval of the USMCA is welcome. A recent IMF working paper provides estimates of the impacts of USMCA.

36. We would like to know if staff has explored how this trade dispute could impact other macroeconomic variables in the U.S. economy (e.g. inflation, interest rates, productivity, labor market, etc.) We also wonder if staff has estimates of the impact of the trade measures that could be imposed in a few weeks by the US to all its automotive imports.

- Thus far tariffs have not had a large effect on consumer price inflation but have increased import price indexes. Academic studies, however, estimate non-negligible effects on households (see e.g. NBER Working Paper 25672). The analysis in Box 4 suggests that tariffs can be disruptive at the sectoral level, thus potentially generating large sectoral labor-market adjustment costs (even if the effects are less visible at the macro level). The October 2018 WEO analyzes the potential effects of tariffs on autos and auto parts.

37. It is not clear to what extent staff's baseline growth forecast incorporates the impact of the already implemented tariff measures and the effects of uncertainty around potential new measures. A more fulsome discussion of how these measures affect the current outlook would have been useful.

- Staff's baseline forecasts have incorporated the effects all tariffs that have been currently applied. It is, however, difficult to capture the effect of uncertainty around future tariff policy (and staff have viewed this as creating both upside and downside risks to the forecast—see Box 8).

Financial sector

38. Could staff be more specific on what kind of institutional response they would have preferred to see in order to counter the growing risks to financial stability? We welcome staff's comments and recommendations on the measures needed to address financial stability risk, for instance to curb excessive corporate leverage or buildup of vulnerabilities in the non-bank sectors.

- As highlighted in paragraph 7 of the staff report, attempts to address data gaps with regards to the nonbank sector, the introduction of a liquidity management framework for asset managers, and reform of the housing finance system would be welcome. In addition, in the past the U.S. regulators have issued guidance on growing risks (e.g. on leveraged loans) which may prove useful. Credit risk retention could be applied at the loan origination level (i.e., at the time of syndication) to align interests across intermediaries and end investors. Alternatively, macroprudential tools could be used for highly leveraged firms (similar to those applied to households) where overall debt is systemically high (although this may be difficult to apply in the U.S. context outside of the banking system).

39. Since increasing fund flows to businesses is key to sustaining growth, could staff comment on the growth vs. risk trade-offs implied by the recent regulatory changes?

- U.S. companies enjoy deep, liquid and efficient corporate debt markets. Bank funding plays a secondary role in the (average) firm's capital structure. Since Dodd-Frank, banks have been subject to stringent documentation and risk management requirements that have improved the average quality of loans and reduced defaults. At the same time, there are few signs of businesses facing restricted access to capital or that these regulatory changes have exacted a large effect on economic growth outcomes.

40. Could staff elaborate further on these differences of views [on financial sector related risks], as well as on its assertion that "little progress has been made in reforming the housing finance system or the government sponsored enterprises"? It is not clear why staff considers that the tailoring of financial regulations based on size and complexity (Box 2) will weaken standards. Comments would be appreciated.

- The tailoring of financial regulations has been a product of a reassessment, in light of outcomes, of the regulatory regime put in place under the Dodd-Frank Act. Staff see, on the whole, that tailoring as appropriate and it has preserved the robust oversight of systemically important institutions. Nonetheless, this does represent a modest easing of prudential requirements and regulatory oversight at a time when the financial cycle is maturing.
- Government sponsored enterprises are still under conservatorship, and there are no specific plans to change the nature of these enterprises (including through changes to the capital retention plans or the design of the regulatory framework that applies to these institutions).

41. Could staff comment on the proposed measures to tailor prudential standards based on size and complexity? Is this related to proportionality in banking regulation and supervision? How will this be applied to foreign entities?

- The Federal Reserve has proposed tailoring as outlined in Box 2 based on the size of assets, cross-jurisdictional activity, short-term wholesale funding, nonbank assets, and off-balance sheet exposure. The Federal Reserve is considering a similar framework for foreign banks calibrated to the risks these foreign institutions pose to the U.S. financial system. No details of that framework have been released.

42. While interest coverage ratios and liquidity positions of the corporate sector remain healthy, can staff comment on the leveraged corporates' capacity to withstand earnings shocks or a tightening of financial conditions. It would also be useful for staff to outline the transmission channels through which the corporate debt risks would affect financial stability and growth in the US and in countries that are most exposed.

- The share of highly indebted speculative-grade firms (i.e. with greater than 5 times debt-to-EBITDA) in new debt issuance has grown rapidly and new deals include looser covenants and lower loss absorption capacity. On the other hand, companies have extended maturities and have refinanced their obligations on favorable terms (given recent compression in yields and risk spreads). The ongoing Financial Sector Assessment Program (FSAP) would analyze in greater detail—including through stress tests—some of the risks posed by leverage lending and associated structured products and their transmission channels through the financial system.

43. Would a loosening of the monetary policy stance warrant a more active role for macroprudential policy?

- To the extent that a loosening monetary policy stance signals softening economic conditions and increased financial stability risks, macroprudential policy can play a role to ensure that the financial sector can withstand potential headwinds from a slowing economy.

44. The high and rising student debt also seems to be emerging as a potential source of vulnerability. We welcome staff comments and encourage staff to explore the issue in more depth in future studies.

- The increase in student debt in recent years is a source for concern. It is worth nothing that this is less of a financial stability issue and more of a macroeconomic and fiscal concern. A large share of this debt is financed by the government and the debt is weighing on consumption decisions of younger cohorts (including whether to buy a house or an automobile).

45. The staff report flags the need to strengthen the financial oversight of nonbanks and hints at data blind spots related to their activities. We appreciate staff further elaboration.

- Compared to banks, nonbanks are either not or loosely regulated and supervised. Therefore, these firms are not required to report data and information to authorities like banks would do. As a consequence, information about risks in the nonbank sector are lacking. Outside of the banking system, for instance, there is only limited information on leverage and maturity transformation, which clearly complicates any risk assessment.

46. In this regard, we would welcome staff comments on the shift in the FSOC doctrine, whose approach to oversight is now activity-based, and no longer entity-based.

- The U.S. Treasury has proposed steps to increase the transparency and analytical rigor of the FSOC's designation process. These include cost-benefit analysis and making available more guidance for financial institutions that are designated as systemic. In assessing systemic risks, evaluations would be based on an activity-based framework and designation would be used only as a last resort (when systemic risks cannot be sufficiently mitigated through other means). These changes have the potential to strengthen the designation process but much will depend on how they are executed. Moving to an "activity-based approach" gives the authorities more flexibility in responding to risks and shocks. An entity-based approach limits public action to those firms that are under an agency's mandate.

Structural issues

47. Against this backdrop of structural features of the labor market, staff recommendations on education and training seem reasonable, but are focused on the supply side of the labor market. It's not clear that these initiatives will address structural constraints to wage immobility. Could staff comment?

- The supply-side measures recommended by staff do not directly affect mobility. However, by raising human capital and skills, workers will be more productive and more likely to participate in the labor force. This will raise lifetime incomes, help meet the emerging skills gaps in the U.S. economy and facilitate greater upward social mobility.

48. We welcome staff to comment on policies that can encourage and promote employment among the low income to address poverty and inequality

- The staff report outlines many such policies to support employment among lower income households. These include providing means-tested support to defray childcare costs, addressing cliffs in social assistance programs and better-coordinating programs between Federal and State governments and across different providers, expanding the Earned Income Tax Credit to make it more generous and with broader eligibility (effectively providing public subsidies to lower income households who work), raising the federal minimum wage, expanding coverage of social assistance programs (currently less than one in four families with children eligible for Temporary Assistance for Needy Families (TANF) receive cash assistance and only one quarter of low-income families eligible for housing assistance actually receive it), and investing in vocational training programs.

49. We would be interested in any staff reflections on how the US has achieved stronger productivity growth when many of its advanced economy peers have struggled.

- U.S. productivity growth has, on balance, been similar to that in the other G7 economies (see https://www.oecd.org/sdd/productivity-stats/oecd-compendium-of-productivity-indicators-22252126.htm).

Major seven countries

	1995-2000	2000-2005	2005-2010	2010-2014	2014-2018
Canada	1.9	1.2	0.6	1.3	0.7
France	1.8	1.5	0.3	0.9	0.7
Germany	1.9	1.4	0.7	1.1	0.7
Italy	1.0	0.1	-0.2	0.3	0.0
Japan	2.3	1.7	0.6	0.8	0.9
United Kingdom	2.4	2.1	0.7	0.0	0.6
United States	2.3	2.5	1.8	0.3	0.7

50. ***We appreciated staff's continued focus on lagging social and distributional outcomes in the report and note the authorities' commitment to more forcefully address these challenges through reform measures aimed at bolstering job creation and supporting low-income workers and families. We take note of staff's recommendations to tackle these challenges and would appreciate comments on the feasibility of implementing the proposals in the current environment.***

- Secretary Mnuchin indicated to staff in the concluding meeting that he does not anticipate any legislation being approved before the 2020 election to tackle this range of issues.

51. ***In an answer to our question on the WEO analytical chapter on rising corporate power, staff acknowledged that additional work would be needed to assess whether weaker competition law and policy aggregate caused larger increase in markups in the United States than in Europe over the past decade. Does staff consider additional work on that issue?***

- Rising corporate market power continues to be an important issue. Staff intends to continue exploring ways to add to policy discussions and the existing literature.

Other

52. ***In May and November 2018 and May 2019, the U.S. Administration imposed bilateral trade and payments sanctions on Iran, and extra-territoriality on Iran's trading partners. In the past, the U.S. had imposed bilateral restrictions—on Iran as well as other members—on national security grounds by invoking the Executive Board Decision No. 144-(52/51). It appears that the Fund was not notified—ex-post or ex-ante within the required 30 days—of the imposition of the May and November 2018 and May 2019 sanctions, and hence these sanctions were not legally grounded in the Decision No. 144. As such, the U.S. seems to be in violation of its obligations under Article VIII. Staff elaboration will be appreciated.***

- On May 8, 2018 the United States announced the ceasing of the United States participation in the Joint Comprehensive Plan of Action (JCPOA) and its intention to re-impose sanctions that have been lifted or waived under JCPOA starting on August 7 and November 5, 2018 after a period of 90 and 180 days respectively. Executive Order 13846 of August 6, 2018 specifies the United States' intention to impose payments and other sanctions from August 7 and from November 5, 2018. On September 11, 2018 the United States notified the Fund pursuant to the procedures of Decision No. 144-(52/51) of restrictions on payments and transfers under Executive Order 13846 (EBD/18/42). Moreover, in May 2018, the United States has also made designations of certain non-US persons pursuant to Executive Order 13224, and such order was previously notified to the Fund under Decision 144(52/51) (EBD/02/45) . In accordance with the Fund's policy on payments restrictions for security reasons set forth in Decision No. 144-(52/51) since no objection was raised during the 30-day period following the notification of said Orders to the Board, any exchange restrictions imposed pursuant to the referred Executive Orders 13846 and 13224 have been approved.

- The measures adopted under the May 8, 2019 Executive Order 13871 on imposing sanctions with respect to iron, steel, aluminum and coper sector of Iran have been notified to the Fund only on June 20, 2019 under the procedures of Decision No. 144-(52/51) and therefore any exchange restrictions arising from such Executive Order would be unapproved at this time.