Fiscal deficits (or surpluses) influence economic growth, and public spending can boost productivity through wise investments in infrastructure. However, industrialized countries increasingly view persistent fiscal deficits and the resulting accumulation of public debt as detrimental to long-term growth and competitiveness. Although reducing government expenditures is often politically difficult and can slow growth temporarily, current deficit levels may not be sustainable as industrial countries’ populations grow older.

In the European Union (EU), the absence of widespread, effective programs of fiscal consolidation threatens to limit monetary policy’s independence and credibility. In Japan, calls for fiscal consolidation may become louder once economic growth has recovered more fully from asset quality problems at major financial institutions.

In the U.S., the current-account deficit is sometimes viewed as a source of savings from abroad that partly offsets the fiscal deficit’s drain on private savings. Progress on the fiscal side may permit a more credible monetary policy and, hence, a stronger dollar. In contrast, fiscal and current-account surpluses in the newly industrialized countries (NIC) of East Asia—Hong Kong, Singapore, South Korea, and Taiwan—have been associated with strong growth in both monetary aggregates and real economic activity.