INTERNATIONAL MONETARY FUND

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UNITED STATES

July 2021

2021 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR THE UNITED STATES

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2021 Article IV consultation with the United States, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its July 19, 2021 consideration of the staff report that concluded the Article IV consultation with the United States.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on July 19, 2021, following discussions that ended on June 25, 2021, with the officials of the United States on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on July 6, 2021.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for the United States.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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Washington, D.C.

PRESS RELEASE

PR21/224

IMF Executive Board Concludes 2021 Article IV Consultation with the United States

FOR IMMEDIATE RELEASE

Washington, DC – July 22, 2021: On July 19, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with the United States.

The United States (US) has been hit hard by the pandemic, which has tragically resulted in close to 600,000 deaths. Thanks to mask mandates, social distancing, shut down orders and over half the eligible population being fully vaccinated, new cases of COVID-19 and the test positivity rate have both fallen significantly in 2021. The receding case numbers should allow normal activities to resume and provide a substantial economic boost. The US economy is expected to grow by around 7 percent in 2021, as savings are drawn down, demand shifts back to in-person services, and depleted inventories are rebuilt. Disruptive supply and demand mismatches are possible as the economy normalizes, including in the labor market, but these are expected to be transitory, while the significant employment gap should help contain wage and price pressures.

The recovery is being underpinned by strong fiscal and monetary support. The American Rescue Plan was adopted in March 2021 and contained 8.2 percent of GDP in federal spending, in addition to the December fiscal package. Fiscal support to small businesses was extended, as was expanded unemployment insurance, while households received transfers via stimulus checks. These packages have supported demand, helped avoid corporate bankruptcies, and relieved financial stress on households and state and local governments. The Federal Reserve's commitment to allow inflation to overshoot the 2 percent target in the near term has facilitated accommodative monetary policy in an environment of low neutral rates, with clear forward guidance on the path of policy rates, based on actual inflation outcomes and inflation expectations.

The new Administration has proposed an ambitious agenda to address long-standing structural challenges in the US economy. The American Jobs Plan and American Families Plan contain proposals to redistribute resources toward vulnerable households, invest in infrastructure, incentivize human capital accumulation and labor force participation, and improve productivity. A renewed effort is underway to lower carbon emissions and increase resilience to climate change. The Administration has also proposed to offset part of the fiscal cost of its plans by increasing taxes collected from corporations and high income households. Proposed tax reforms include a higher statutory rate of corporate tax, a global minimum tax, as well as increases in the top marginal rate of personal income tax and the rate high income earners pay on capital gains. On a net basis, the Administration's fiscal plans would leave federal government debt 3¼ percent of GDP higher at end-2030.

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

700 19th Street NW
Washington, DC 20431
USA

Executive Board Assessment[2]

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

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

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

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

Directors observed that systemic financial stability risks appear close to the historical average. However, the pandemic has revealed important shortcomings in the functioning-under-stress of systemically important U.S. markets and institutions. Directors urged that serious consideration be given to structural changes in the operation of the Treasury market, key money markets, and prime money market funds.

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

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[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.IMF.org/external/np/sec/misc/qualifiers.htm.

to work constructively with its trading partners to strengthen the rules-based multilateral trading system.

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

United States: Selected Economic Indicators

	2019	2020	2021	2022	2023	2024	2025	2026
			Projections					
Real GDP (annual growth)	2.2	-3.5	7.0	4.9	1.9	1.7	1.7	1.7
Real GDP (q4/q4)	2.3	-2.4	8.0	2.8	1.8	1.7	1.7	1.7
Unemployment rate (q4 avg.)	3.6	6.8	4.4	3.1	3.0	3.0	3.2	3.4
Current account balance (% of GDP)	-2.2	-3.1	-3.8	-3.6	-3.4	-3.0	-2.7	-2.5
Fed funds rate (end of period)	1.7	0.1	0.1	0.2	0.7	1.4	2.1	2.3
Ten-year government bond rate (q4 avg.)	1.8	0.9	1.9	2.4	2.7	2.8	2.8	2.7
PCE Inflation (q4/q4)	1.5	1.2	4.3	2.4	2.4	2.3	2.2	2.0
Core PCE Inflation (q4/q4)	1.6	1.4	3.7	2.4	2.6	2.5	2.3	2.1
Federal fiscal balance (% of GDP)	-4.6	-14.9	-15.1	-8.0	-5.7	-4.8	-4.6	-4.5
Federal debt held by the public (% of GDP)	79.2	100.1	104.9	103.6	104.9	105.8	106.6	107.3

Sources: BEA; BLS; Haver Analytics; and IMF staff estimates.

INTERNATIONAL MONETARY FUND

UNITED STATES

STAFF REPORT FOR THE 2021 ARTICLE IV CONSULTATION

July 6, 2021

KEY MESSAGES

The new administration's policies have put the U.S. economy on a strong footing. An effective vaccine rollout has put the number of new COVID-19 cases on a firmly downward path. At the same time, unprecedented fiscal support is quickly restoring the economy back to full employment and generating positive outward spillovers to the world economy. These efforts have not been costless: the path for public debt is far higher; the current account deficit has grown; and very accommodative financial conditions have led to increased corporate and nonbank leverage and rising valuations across a range of assets. The pandemic continues to weigh heavily on those at the lower end of the income distribution, exposing longstanding inequities in access to quality healthcare and education (many of which have an important gender and racial dimension).

The administration's proposed policy program seeks to address a range of challenges that have long held back the U.S. economy. The pandemic is being viewed as an opportunity to remake the economy with higher productivity, increased labor force participation, and a less polarized distribution of income and wealth. To partially fund the intended increase in federal spending, plans have been developed to close tax loopholes, raise taxes on corporates and higher income households, remake the international system for corporate taxes, and fully resource the Internal Revenue Service. Finally, a renewed effort is underway to lower carbon emissions and increase resilience to climate change.

The size and ambition of the proposed fiscal packages are admirable, but a better targeting of policies would further strengthen their impact on macroeconomic and distributional outcomes. As the appropriations process moves ahead, more could be done to (i) phase out tax credits at lower levels of household income; (ii) prioritize spending toward programs that have the biggest impact on productivity, labor force participation, reducing poverty, and facilitating a shift to a low-carbon economy; and (iii) fully eliminate step-up basis, lower the threshold for paying the estate tax, eliminate the 199A passthrough deduction, and reformulate the business tax as a cashflow tax. Reorienting the administration's tax and spending proposals in this way would likely imply a slower (but more sustained) demand impulse, create a bigger boost to aggregate supply, and, in so doing, lessen the near-term risks posed by a sustained upswing in inflation. Even with improved targeting, additional steps will be needed over the medium term to bring down the public debt both by raising revenues (through a carbon tax, higher taxation of fuels, and a broad-based federal consumption tax) as well as lessening the impact of an aging demographic on future spending. Also, there are important uncertainties surrounding the final size and composition of these proposals, given the need to build political consensus around them.

The Federal Reserve's actions have been highly effective both in the depths of the crisis and in supporting the recovery. While there were risks to introducing the new monetary framework in the midst of COVID-related uncertainty, the low neutral rate of interest and the asymmetries posed by the effective lower bound called for a new approach to policy. The Federal Reserve's new policy framework has helped support a more rapid recovery from the pandemic and rightly commits to a near-term overshooting of the 2 percent longer-run inflation goal (in line with past IMF advice). From a conjunctural perspective, the framework helpfully defers the timing of policy normalization—increasing monetary support as the economy recovers from the COVID-19 shock—while providing clarity on how the Fed intends to achieve its statutory mandate of maximum employment and price stability. In the coming months, the ongoing rapid pace of recovery and expectations of additional fiscal support will necessitate a shift in monetary policy. Managing this transition—from providing reassurance that monetary policy will continue to deliver powerful support to the economy to preparing for an eventual scaling back of asset purchases and a withdrawal of monetary accommodation—will require deft communications, under a potentially tight timeline, to avoid market misunderstandings, volatility in market pricing, and/or an unwarranted tightening in financial conditions.

The unfolding pandemic revealed important shortcomings in the functioning-under-stress of systemically important U.S. markets and institutions. Serious consideration should be given to structural changes in the operation of the Treasury market, key money markets, and prime money market funds. Systemic financial stability risks appear close to the historical average but the very accommodative financial conditions are encouraging continued risk taking, fueling asset valuations, and facilitating rising leverage in the nonbanks and corporates that should be followed carefully.

The pandemic has resulted in a larger current account deficit and left the U.S. external position moderately weaker than the level implied by medium-term fundamentals and desirable policies. The current account deficit is likely to grow further in 2021. Trade restrictions and tariff increases should be rolled back. Doing so, would help support U.S. workers and create more and better American jobs (particularly in light of the domestic efforts that are being proposed to increase productivity, labor supply, and the competitiveness of U.S. producers). "Buy American" provisions should be tightly circumscribed and made consistent with the U.S. international obligations. Currency related trade responses should be avoided. Instead, the U.S. should work constructively with its trading partners to better address the underlying macro-structural distortions that are affecting external positions and to strengthen the rules-based multilateral trading system. Renewed engagement at the World Trade Organization—including restoring the proper functioning of the dispute settlement system—could help facilitate progress on these topics.

As the pandemic effects recede, policymakers will have to cope with simultaneous, ongoing transitions. These arise from an uncertain reshaping of the post-pandemic economy (both in the U.S. and abroad), a transition to a lower carbon economic model, an increasing role for digitalization and technology, and an underlying shift in U.S. demographics toward an older and more diverse population. The flexibility and innovativeness of the U.S. system puts it in a good place to manage these transitions. However, great care should be taken to ensure that these multi-faceted changes do not increase income polarization, further hollow out the middle class, and leave behind a material share of the population (particularly lower-skilled, lower-income workers). It would be a mistake to assume the social and economic impact of these deep-rooted transitions can simply be left to market forces and the hope that a vibrant U.S. economy will lift all boats. Instead, a multi-dimensional policy approach will need to be developed to support rising living standards for all Americans and prevent workers from becoming disenfranchised or detached from the labor force.

Approved By
Nigel Chalk (WHD) and Jeromin Zettelmeyer (SPR)

Discussions were held (virtually) with non-government counterparts during May 17–June 4, 2021 and with government agencies from June 7–25, 2021. The team comprised Nigel Chalk (head), Katharina Bergant, Andrew Hodge, Li Lin, Rui Mano, Andrea Medici, Yannick Timmer, Anke Weber (WHD) and Mico Mrkaic and Elizabeth Van Heuvelen (SPR). Input to the consultation was also provided by Nicoletta Batini, Philip Barrett, Simon Black, Jean Chateau, Niels-Jakob Hansen, Shafik Hebous, Florence Jaumotte, Geoffrey Keim, Alessandro Lin, and Ian Parry. Concluding meetings were held with Chair Powell and Secretary Yellen on July 1, 2021.

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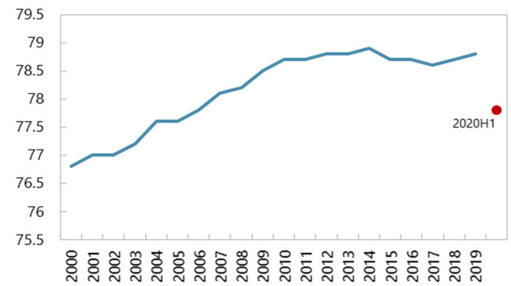
PANDEMIC AND RECOVERY

Life Expectancy at Birth (Years)

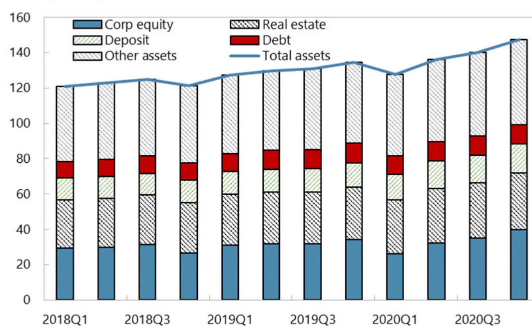


Sources: National Center for Health Statistics; Haver Analytics.

1. **Tragically, the COVID-19 pandemic hit the U.S. hard**. More than 600,000 Americans have died and average life expectancy has fallen. A third wave peaked in early January as new cases reached 300,000 per day, the test positivity rate hit 14 percent, and deaths exceeded 3,000 per day.

2. **However, diligent work over the past year to develop vaccines and the rollout of vaccination programs over the past several months have begun to bring the pandemic under control.** By mid-June, over one-half of the eligible population have been fully vaccinated and both new cases and the test positivity rate have fallen markedly. Nonetheless, the nature of the pandemic has changed globally, new variants are circulating widely, and there has been a shift in hospitalization and mortality toward younger Americans. Furthermore, while vaccines are widely available, individual decisions of whether to take the vaccine have become a more binding constraint.

Households and Nonprofit Organizations Assets (trillion)



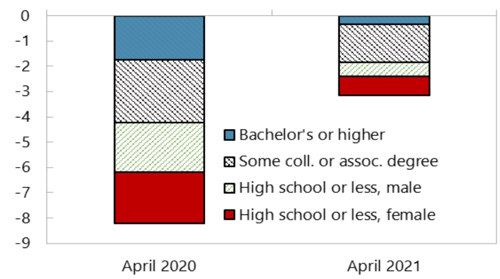
Source: Federal Reserve.

3. **The receding COVID-19 case numbers should provide a substantial boost to activity**. The economy grew by 6.4 percent in the first quarter, despite a 2.6 percent drag from the drawdown of inventories. Boosted by fiscal transfers, real consumption rose above its pre-pandemic peak in March. The household saving rate remains very high and rising prices of financial assets have bolstered household balance sheets. However, the share of services in consumption has fallen from 69 percent in 2019 to 66 percent in 2021Q1, led by particularly sharp declines in transportation and entertainment services. As vaccination rates rise and normal activities resume, this provides a very strong basis for growth in the coming quarters. Savings will be drawn down, demand will return for in-person services, and depleted inventories will be rebuilt. The exact pace and timing of this acceleration is unclear and behavioral stickiness is possible (as preferences for remote modalities endure or concerns about in-person interactions persist). Nonetheless, growth in 2021 is expected to be around 7 percent, the fastest pace in a generation, with modest risks to the upside.

4. **The unprecedented policy response to the pandemic has mitigated hysteresis risks**. Fiscal stimulus packages approved in 2020 and 2021 have provided assistance to businesses through the Paycheck Protection Program (PPP) and other initiatives. This has helped keep the total number of corporate bankruptcies low relative to past history (with increases in Chapter 11

bankruptcies more-than-offset by lower Chapter 13 bankruptcies)[1]. As temporary rent moratoria and policy support expire, there will likely be some corporate failures as the economy adapts to the lasting changes catalyzed by the pandemic. However, this is expected to be a protracted process of resource reallocation rather than a damaging surge in corporate failures. Some business models will become obsolete—particularly in retail, leisure, and entertainment—while new businesses will emerge[2]. The prospect for labor market hysteresis for lower income workers is, as yet, unclear. Labor market conditions for college-educated workers have returned to close to those prevailing at end-2019. However, the employment-population ratio still remains around 3 percent below the pre-pandemic level, largely due to diminished participation and higher unemployment among lower-income, less-skilled workers.

Employment-to-Population Ratio
(ppt deviation from January 2020)



Notes: Ages over 25; data is not seasonally adjusted.
Sources: BLS; IMF Staff calculations.

UNPRECEDENTED FISCAL SUPPORT

A. Discretionary Spending Packages

5. **Following on from the December fiscal stimulus package, the new administration passed the American Rescue Plan, adding 8.2 percent of 2021 GDP to spending.** With COVID-19 continuing to pose a threat, these federal resources were deployed to accelerate vaccinations and expand healthcare coverage; assist the vulnerable and the unemployed; bolster subnational government finances; and support segments of the economy that had suffered the worst effects of the pandemic (e.g. schools, colleges, healthcare providers, mass transit, etc.).

6. **Subsequently, the administration proposed a significant increase in spending through the American Families and Jobs Plans.** The principal goals of these programs are to redistribute resources toward vulnerable households, invest in infrastructure, incentivize human capital accumulation, boost labor force participation, and improve productivity. On June 24, a bipartisan agreement was reached on a US$579 billion in a separate infrastructure bill but the administration has indicated it remains committed to the remaining components of the Jobs and Families Plans that were not incorporated into the bipartisan proposal.

7. **While the American Rescue Plan had many positive features, it could have been better targeted**. A sizable share of the package did not go to relieve immediate liquidity constraints and

[1] At the time of the 2020 Article IV, a corporate stress testing exercise projected that 15 percent of non-energy, non-investment grade debt would face financial distress in 2020. However, stronger growth outturns and the large-scale policy support have resulted in only 2.5 percent of non-energy, non-investment grade debt ending up in default.

[2] New business applications in 2020 were 24 percent above 2019 levels as new opportunities were revealed by the shifts in demand triggered by COVID-19.

other hardships. Rather, resources were disbursed that served to improve household, corporate and subnational government balance sheets at the expense of an increase in the federal debt. An alternative approach would have been to better target the spending. This could include by providing the stimulus payments to a smaller share of the population (e.g. those earning below the median income), to lessen the transfers to state and local governments (meeting their most immediate cash needs but not replenishing their rainy day funds), and to gradually scale back the generosity of supplemental unemployment benefits during the course of 2021 (both to limit "cliff" effects when the benefits expire and to lessen the negative incentive effects from a high benefit replacement rate as labor market conditions improve).

Text Table 1. U.S. Discretionary Spending Packages (US$ billion)

Consolidated Appropriations Act (December 2020)	**868**
Support for small businesses (including Paycheck Protection Plan)	302
One-time stimulus payments	169
Unemployment benefits (including US$300 per week supplement until March)	119
Funding for schools and colleges	82
Public health (including testing and vaccinations)	79
Other (including food assistance, transportation, broadband, banking)	117
American Rescue Plan (March 2021)	**1,850**
Funding for schools, colleges, transit, childcare, food assistance, healthcare, housing	486
One-time stimulus payments	402
Transfers to state and local government	362
Unemployment benefits (including US$300 per week supplement until September)	206
Refundable child tax credit and earned income tax credit	111
Other (including FEMA, support to small businesses, multi-employer pensions)	283
American Jobs Plan (***proposed***)/ **Bipartisan Agreement on Infrastructure Plan 1/**	**2,300 / 579**
Transportation (including electric vehicle charging)	630 / 312
Water, power, broadband, resilience, and environmental remediation	360 / 267
R&D and support for domestic manufacturing	580 / 0
Elderly and disabled care	400 / 0
Housing, federal buildings, schools	330 / 0
American Families Plan (***proposed***)	**2,050**
Extending child tax credit until 2025 and making it refundable thereafter	545
Tax credits and subsidies for childcare costs	305
Paid parental, family, or sick leave	225
Making permanent tax credits to subsidize health insurance premia	200
Universal pre-school	200
Making permanent expanded earned income tax credit	140
Grants for low income students attending college and nutrition	125
Improving college recruitment and retention and other education initiatives	120
Two-years of tuition-free community college	110
Strengthen IRS enforcement	80

1/ While the recently announced Bipartisan Infrastructure Plan includes some of the proposals under the American Jobs Plan, it is not a strict subset of the plan.

8. Many of the policy changes proposed in the American Jobs and Families Plans are aligned with past IMF policy advice. Multi-year investments in power, transportation, telecommunications, and water will all help remove bottlenecks and increase productivity. There is solid empirical evidence also of the societal payoffs—in the form of lower poverty, better health and education outcomes, reduced crime, and increased labor force participation, and higher productivity—from providing high-quality childcare, creating a national paid family leave program, investing in pre-school, expanding access to college for low income students, increasing healthcare coverage, and improving college retention.[3] Furthermore, many of these investments will directly support working mothers (who have long made up a large share of the poor and were hard hit by the pandemic)[4] as well as help black and Hispanic families, who are disproportionately poor. The extent to which these proposals are realized will depend, however, on appropriations and tax policy changes legislated by the Congress.

9. The size and ambition of the Families and Jobs Plan are admirable, but a better targeting of policies would further strengthen their impact on macroeconomic and distributional outcomes. For example, the proposed child tax credit starts to phase out at household income of US$150,000 (for a married couple) and some other types of assistance (like the Child and Dependent Care Tax Credit) are available to households with incomes up to US$400,000. It would be preferable to phase out such assistance at lower levels of household income (e.g. at 300–400 percent of the federal poverty level or at the state-level median income) to lessen their fiscal cost. Doing so would provide resources to make the refundable child tax credit permanent and create the space to permanently expand unemployment insurance to independent contractors, the self-employed, and gig workers. Spending to support domestic manufacturing, invest in advanced semi-conductors, and incentivize the onshoring of supply chains could be recast as investments to encourage innovation (e.g. in basic research) or improve productivity (e.g. by further strengthening human capital or eliminating infrastructure bottlenecks). Finally, the size of proposed support for home and community-based care for the elderly and disabled could be reconsidered. Reorienting spending in this way would likely imply a slower (but more sustained) demand impulse, do more to relieve supply constraints, and, in so doing, reduce the risks posed by a sustained upswing in inflation.

10. Authorities' views. The American Jobs and Families Plans were viewed as transformational, once-in-a-generation investments to reimagine and rebuild the U.S. economy. The American Rescue Plan had already helped millions of families and lifted 5 million American children out of poverty. The Jobs and Families Plans would ensure these gains are institutionalized. The plans had been carefully designed and were well-targeted to address longstanding shortcomings in U.S. infrastructure and the system for social assistance. The full implementation of the proposed policies would create millions of high-quality new jobs and would put the U.S. on a stronger footing to

[3] 38 percent of full-time undergraduate students attending a four-year college do not graduate within six years.

[4] Even prior to the pandemic, almost one-in-four female-headed households and one-in-eight American children were living below the poverty line (even after taking into account the effect of government assistance programs). For an assessment of the impact of COVID-19 on women in the U.S., see S. Fabrizio, D. Gomes, and M. Mendes Tavares "COVID-19 She-Cession: The Employment Penalty of Taking Care of Young Children", IMF Working Paper 2021/058.

compete internationally. Policies were intended to go well beyond building highways, ports and bridges but would also serve to strengthen the social infrastructure of the economy by modernizing schools and childcare facilities, expanding home and community based care for the elderly and disabled, offering paid family leave, and strengthening the safety net to support poorer households. The policies would help reverse the pandemic's impact on labor force participation and, particularly, help women to rejoin and remain in the workforce. The authorities also underlined the administration's strong political commitment not to raise taxes on any family earning under US$400,000 and to provide greater federal support for both poorer households and the broader middle class.

B. Proposed Tax Policy Changes

11. The cost of the additional federal spending is expected to be partially offset by raising taxes on corporates and high-income households. Such tax increases are necessary to prevent the proposed increase in the spending envelope from translating into a faster pace of debt accumulation. The proposals have important implications for the international system of corporate taxation (see Box 1) and include:

- An increase in the statutory corporate tax rate (to 28 percent), partially reversing the rate reduction in the 2017 Tax Cuts and Jobs Act (TCJA) and returning the U.S. to the highest (combined average state and federal) corporate tax rate in the OECD.
- A global minimum tax on offshore profits of U.S. multinationals of 15 percent. The tax would be calculated on a country-by-country basis (significantly reducing the incentive to shift profits to low tax jurisdictions). Deductions would be denied for payments that are made to countries that fail to adopt a strong minimum tax.
- Corporations above a certain size would be required to pay at least 15 percent on the "book income" profits they report to investors in their financial statements.
- The current lower corporate rate on income from foreign sales (FDII) would be eliminated.
- Measures would be introduced to reduce the tax benefits of inversions (i.e., where U.S. corporations seek to obtain tax residence in a lower tax jurisdiction through mergers or acquisitions), to incentivize the "onshoring" of jobs back to the U.S., and to remove tax preferences for fossil fuel companies.
- The top personal income tax rate (for married couples earning over US$622,051) would rise from 37 to 39.6 percent.
- "Qualified" dividends and capital gains would be taxed at the top personal income tax rate (i.e., 39.6 percent plus the existing 3.8 percent Affordable Care Act surtax) for households earning over US$1 million.

- The "carried interest" provision—that allows high income taxpayers to recharacterize labor income as capital gains—would be eliminated.

- The "step-up basis" for capital gains in excess of US$2 million (for a married couple) would be eliminated (to prevent individuals from passing appreciated assets to their heirs without incurring tax on the accumulated capital gains).

- The Internal Revenue Service would be fully resourced to upgrade systems, expand audits, and generally strengthen tax administration.

12. Many of the proposed revenue provisions reflect previous IMF policy advice.[5] Instituting a permanent increase in taxes on corporate profits and on high income households is warranted, especially given the proposed permanent increase in spending obligations. Proposals helpfully include a globally coordinated minimum corporate tax, applied on a country-by-country basis, which will be a crucial step forward in countering the incentives for profit shifting and base erosion. Efforts to disincentivize inversions should help reduce avoidance and eliminating tax preferences for fossil fuel companies will support the administration's goals to reduce greenhouse gas emissions. Excluding deductions paid to countries without a global minimum tax appears consistent with the "undertaxed payment rule" in the OECD's Pillar Two proposals and removing the FDII tax preferences for exporters will create a more level playing field (and avoid a potential WTO challenge). The proposed changes to the personal income tax rightly close loopholes that allow high income individuals to recharacterize labor income and escape tax on capital gains (although step-up basis should be fully eliminated rather than having the proposed US$2 million exemption). There is also a clear need—and potentially large payoff, both in terms of revenues and in improving the equity of the tax system—from increasing funding for the Internal Revenue Service.

13. The combined impact of the various tax provisions on equity-financed investments may incentivize debt finance or deter capital formation. The 28 percent corporate rate and the taxation of dividends and capital gains as ordinary income—when combined with state-level corporate and capital income taxes—will significantly raise the statutory rate on equity-financed investments.[6] The tax burden on equity-financed investments—particularly intangibles which, arguably, were previously undertaxed—will be further increased by the proposed anti-avoidance mechanisms and the global minimum tax. These potential effects on debt bias and capital formation are, however, lessened by (i) the marginal effective rate being much lower than the statutory rate;[7]

[5] See, for example, the 2018 U.S. Article IV Consultation which supported the reduction of the corporate tax from 35 percent although noted that the combination of a lower statutory rate, the expensing of capital spending, and continued deductibility of interest spending represented an overly generous benefit to debt-financed investment. See also N. Chalk, M. Keen, and V. Perry, "The Tax Cuts and Jobs Act: An Appraisal", IMF Working Paper 2018/185.

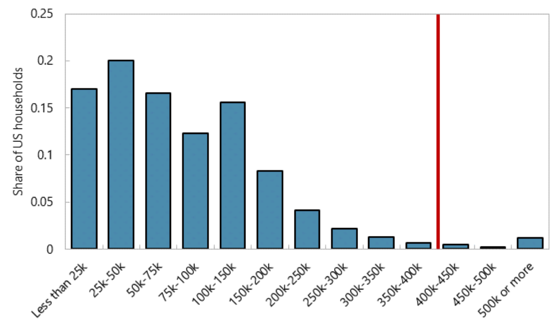
[6] For example, the combined federal and state-level marginal statutory rate on income from equity-financed investments would be as high as 72 percent in California.

[7] The reduction in the statutory rate from 35 to 21 percent was estimated by the Joint Committee on Taxation to have lowered the effective rate on U.S. firms' profits from 16 to 8 percent (U.S. International Tax Policy: Overview and Analysis, March 2021).

(ii) only around one-quarter of equities are currently in the hands of taxable shareholders;[8] and (iii) insofar as the tax is largely incident on rents, the high statutory rate would have a lesser effect.[9] Despite these mitigants, it may still be preferable to tax dividends and capital gains at the same, uniform rate of 20–25 percent in order to align the combined (i.e., corporate plus personal) rate on capital income with the top marginal rate on labor income. This would also lessen the extent to which pass-through entities face a preferential tax rate relative to C-corporations.[10] Also, the concerns around the potential disincentive effects for capital formation could be addressed by reformulating the business tax as a cashflow tax (i.e. by permanently allowing for the expensing of all capital outlays and fully eliminating the deduction for interest spending on newly contracted debt). Finally, prudent planning would suggest the need to build into the fiscal plans a more conservative revenue effect from proposed investments in tax administration.

14. The administration's commitment not to raise taxes on households earning under US$400,000 per year (which encompasses 98 percent of households) represents an important constraint on the options for raising revenue. Without this limitation, further tax policy changes could be considered that raise revenues but without increasing the tax burden for households earning around the median income. These could include:

Household Income in the United States (2019)



Sources: ASEC March CPS; IMF Staff calculations.

- Increasing the reliance on indirect taxes, particularly those that will help achieve the administration's climate goals such as introducing a carbon tax and/or raising federal fuel taxes. A carbon tax would, though, have to be sensitive to its impact on the income distribution, potentially requiring accompanying increases in targeted social assistance.

- Eliminating the current 20 percent (section 199A) deduction for certain types of pass-through income.

- Scaling back poorly targeted tax expenditures such as the income tax exemption for employer-provided health care, the capital gains tax exemptions for individuals selling their principal residence, and the deductibility of mortgage interest and state and local taxes.

In addition, the minimum threshold for the estate tax could be lowered (from the current level of US$23.4 million for a married couple).

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[8] The bulk is held by untaxed entities such as institutional investors (like insurance or pension funds), individual retirement accounts, nonprofits, or nonresidents.

[9] The evidence suggests that the high share of rents in profits was an important factor for why the TCJA corporate rate reduction had relatively small effects on investment (see E. Kopp, D. Leigh, S. Mursula, and S. Tambunlertchai, "U.S. Investment Since the Tax Cuts and Jobs Act of 2017," IMF Working Paper 19/120).

[10] Currently, around one-half of corporate income is taxed as a pass-through (e.g. as a sole proprietor, partnership, limited liability company or S-corporation) at a federal statutory rate of between 29.6 and 37 percent, depending on the type of business income.

15. Authorities' views. Tax policies had been designed with a view to reversing the decline in federal revenue-GDP that was seen over the past five years in order to fund essential federal government programs. It was equitable to have high net worth individuals and corporations bear much of that burden, particularly in light of the lowering of taxes under the 2017 Tax Cuts and Jobs Act. The proposed "Made in America Tax Plan" strikes a good balance between raising revenues and incentivizing job creation and investment. The effective rate on U.S. corporate profits was still low relative to history and was unlikely to be a significant disincentive to new investment, particularly with much of U.S. corporate profit reflecting rents rather than normal returns to capital. The improvements envisaged in tax enforcement and administration would help address tax evasion and make for a fairer tax code. The goal of many of the proposed tax policy changes was to reward work and not wealth, especially by eliminating those loopholes that are being used by corporations and high net worth individuals to reduce their tax liabilities. Finally, the proposed changes to the international corporate tax system were viewed as consistent with OECD proposals and would help reverse the "race to the bottom" in corporate taxes, curtail wasteful profit shifting to low tax jurisdictions, and bring stability to the global tax system. The proposed legislation was viewed as being fully consistent with the U.S. negotiating position in the OECD process.

Box 1. Implications for the International Corporate Tax System

The international aspects of the U.S. proposed tax plan are broadly in line with the OECD's Pillar 2 proposal.[1] The U.S. plan is also consistent with recent moves by other countries to raise the statutory corporate income tax rate (e.g. the U.K.'s increase in the corporate tax rate from 19 to 25 percent). A higher U.S. rate, as well as a global minimum tax, may help coordinate an end to the downward path for corporate tax rates that has occurred internationally. Also, a higher rate in the U.S., relative to OECD comparators, would be consistent with the theory that larger economies can maintain higher tax rates because of their more immobile tax base.

The tax plan raises the effective average tax rate (EATR) on multinationals that are headquartered in the U.S. (largely because of the higher statutory rate and the elimination of a lower tax rate on profits derived from foreign sales that are in excess of 10 percent of the value of depreciable tangible assets). Specifically, it is estimated that the EATR on equity-financed investment into intangibles would rise from 13.6 to 24.8 percent[2]. Other mechanisms proposed in the tax package to deter base eroding payments (e.g. disallowing deductions for payments to low tax jurisdictions) will further increase the EATR.[3]

The average (foreign and U.S.) tax paid by U.S. controlled foreign corporations is currently 9.8 percent for all jurisdictions (and 7 percent if only low-tax jurisdictions are included). As such, a 15 percent global tax would be binding for many U.S. multinationals. In the absence of a global agreement on a minimum tax, these various changes will disincentivize companies from headquartering in the U.S.

Therefore, a coordinated global agreement on a minimum tax will be important to level the playing field internationally. disincentivize jurisdictions from maintaining a low corporate tax rate, and mitigate locational disadvantages from the other tax changes proposed by the administration (including the higher statutory rate, more binding anti-avoidance provisions, and minimum tax on book income). A global minimum tax will help raise the EATR for companies that locate in other jurisdictions which adopt the tax, reducing the EATR differential between the U.S. and other locations (especially if agreement can be reached on a common rate for the global minimum). In this regard, it will be important that the U.S. global minimum tax is assessed on a jurisdiction-by-jurisdiction basis and does not provide an exemption based on assets (i.e., compared to the GILTI provision which was calculated based on a worldwide average and with an exemption equal to 10 percent of the foreign-located, depreciable tangible assets).[4] Such a design will make the tax more binding and independent both of a firm's assets, its allocated expenses, and the share of profits it derives from low tax jurisdictions. Also, denying deductions for payments made to related parties in those low tax jurisdictions that do not have a minimum tax should provide a reinforcing incentive to adopt the global minimum.

[1] The OECD's Inclusive Framework Pillar One seeks to reallocate a share of global residual profits of in-scope multinationals destination countries and Pillar Two seeks to ensure that profits of multinationals are taxed at a globally agreed minimum level.

[2] Based on calculations from Beer, Klemm, and Matheson (2018).

[3] Other provisions in the tax plan may have opposing effects on the EATR. Cost-based R&D tax incentives will lower the EATR but the proposed minimum tax on large corporations' book income increases the EATR.

[4] The exemption had the undesirable effect of incentivizing firms to move fixed assets abroad in order to lower their GILTI tax liability.

THE SHIFT IN THE MONETARY POLICY FRAMEWORK

16. **In August 2020 the Federal Reserve announced important changes to its policy framework**. These included (i) the FOMC would seek to achieve inflation that averages 2 percent over time (following periods when inflation has been running persistently below target, policy would

aim to achieve inflation moderately above 2 percent for some time); and (ii) policy decisions would react to mitigate shortfalls of employment from the FOMC's assessment of its maximum level. Policy would continue to take into account the balance of risks, including systemic risks to financial stability. The change in the framework recognizes that policy would be more frequently constrained by the effective lower bound—due to a decline in the neutral rate—which increases the downside risks to both employment and inflation. As a result of these changes, policy is intended to be more accommodative for a longer period after a negative shock as a means to more-quickly get the economy back to full employment and away from the effective lower bound.

17. The change in the framework is consistent with past IMF advice. Given the decline in the neutral rate of interest, and the asymmetries posed by the effective lower bound, past Article IVs have emphasized that the Federal Reserve should be ready to accept some modest, temporary overshooting of its inflation goal so that inflation approaches the 2 percent medium-term target from above. Doing so would provide valuable insurance against the risks of disinflation and having to bring the federal funds rate back down to the effective lower bound. The flexible average inflation targeting framework provides a clear structure to operationalize this approach to policy. Given the complexity of the U.S. economy and the uncertainties in implementing the new framework, it is appropriate to eschew closely parameterizing the policy framework (e.g. by providing a formulaic time horizon over which inflation will be averaged or specific limits on the amount that inflation will be allowed to overshoot). Instead, the size and duration of the intended overshoot should be data dependent.

18. While there were risks to introducing the new monetary framework in the midst of COVID-related uncertainty, the change in framework has been a timely innovation, helping to redefine the Fed's approach to policy as the U.S. emerges from the effects of the pandemic. The benefits of the framework in the context of the COVID-19 shock were four-fold:

- First, the framework is designed to provide more accommodation over a longer horizon in response to a negative shock. The precommitment to overshoot helps increase expected inflation over the near-term, lowering today's real interest rate and, in so doing, boosting demand.
- Second, the framework allows the Fed to not react pre-emptively based on policymakers' forecasts of inflation and, instead, to place more weight on inflation expectations and realized inflation in its policy calculus. This has proven advantageous at a time when it has been difficult to assess the underlying parameters—such as the natural rate of unemployment or the size of the output gap—that would be needed to accurately predict the path of inflation.
- Third, the new framework embeds clear, outcomes-based forward guidance around the future path of policy rates (i.e., that the federal funds rate will remain at the effective lower bound until inflation rises to 2 percent and is on track to moderately exceed 2 percent for some time).
- Fourth, the more accommodative framework should help repair some of the damage to the income distribution that had been wrought by the pandemic (Box 2).

19. The combination of the new monetary policy framework and the economic boost from fiscal stimulus should be self-reinforcing. The flexible average inflation targeting helps increase the demand impact of the fiscal support by providing more accommodation. At the same time, the large fiscal boost increases the likelihood that inflation gathers sufficient momentum to sustainably exceed 2 percent (something that the U.S. and other advanced economies have struggled to achieve in the post-global financial crisis period). It is worth noting, also, that the impact of the Fed's new framework would be further reinforced by a similar shift in frameworks by other systemic central banks (Box 3).

20. There is a concern, though, that the unprecedented size of the planned fiscal support will significantly compress the timeline for policy normalization. The reopening of the economy will create considerable unpredictability in PCE inflation during the next several months, making it very difficult to divine underlying inflationary trends. At the same time, presuming staff's baseline outlook and fiscal policy assumptions are realized, policy rates will likely need to start rising in late-2022 or early-2023 (with asset purchases being scaled back in the first half of 2022). Managing this transition—from providing reassurance that monetary policy will continue to deliver powerful support to the economy to preparing for an eventual scaling back of asset purchases and the withdrawal of monetary accommodation—will require deft communications under a potentially tight timeline. Mitigating the risks of market misunderstandings, volatility in market pricing, and/or an unwarranted tightening of financial conditions (with all the negative spillovers to the global economy that such outcomes would entail) will require the FOMC to continue clearly telegraphing its interpretation of incoming data and articulating what economic developments mean for policies. The Federal Reserve's commitment—to communicate well in advance its thinking and to ensure that the eventual withdrawal of monetary accommodation is orderly, methodical, and transparent—is very welcome.

21. Authorities views. The substantial decline in the neutral rate over recent decades has left the FOMC with less policy space to cut rates to spur aggregate demand. As such, the policy rate in the U.S. is more likely to be constrained by the effective lower bound than in the past, raising downward risks to both employment and inflation. These developments necessitated a shift in the Fed's framework to more firmly anchor long-term inflation expectations at the longer-run 2 percent goal and to increase the power of monetary policy to quickly return the economy back to full employment after a negative shock. The new Flexible Average Inflation Targeting approach is expected to achieve both these goals. The FOMC's implementation of the framework embeds clear forward guidance with the FOMC committing to begin raising rates only after labor market conditions are in a place that is consistent with maximum employment and inflation has risen to 2 percent and is on track to moderately exceed that level for some time. On the conjuncture, the recent rise in various prices as the economy reopens is expected to have largely transitory effects on inflation, and employment remains well below estimates of its maximum level. As such, the economy is still judged to be a ways away from the FOMC's goals. It is expected that it will take some time before a withdrawal in monetary accommodation would be appropriate, although such determinations will depend on the performance of the economy. Nonetheless, the Federal Reserve remains conscious of the important spillovers from its policy actions and is committed to continuing to clearly communicate its intentions and telegraph at an early stage any prospective shift in asset purchases or policy rates.

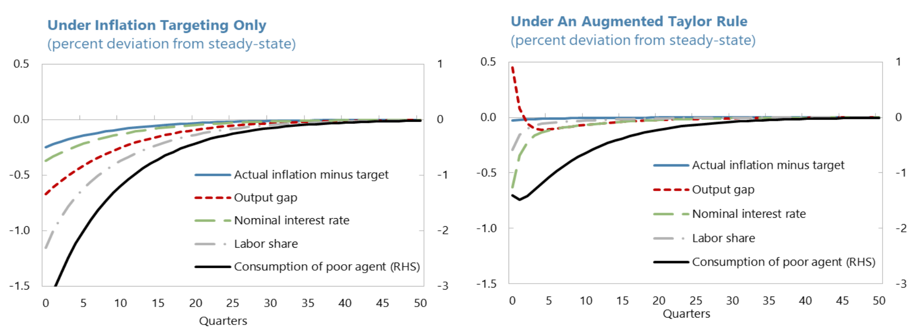
Box 2. Monetary Policy and Consumption Inequality

Traditionally, monetary policy actions are judged against how well they achieve the optimal trade-off between inflation, output, and aggregate labor market outcomes. In a model of heterogenous agents, the *distribution* of consumption across the population becomes an additional consideration for policy, especially in the presence of productivity shocks. The intuition for the distributional impact of such shocks is straightforward: lower income households have relatively low skills, are mostly reliant on labor income, and hold few claims on capital. As a result, a positive productivity shock predominantly benefits higher income households, boosting their returns to both skills and to their holdings of claims on the capital stock. To analyze this intuition, we draw on a two-agent economy with price and wage rigidities[1] and find that:

- ***In theory, welfare outcomes can be improved if monetary policy attaches some weight to the distribution of wages*** (in this model that is captured by policymakers attaching some weight to the labor share of income in addition to inflation and the aggregate unemployment gap). In the face of a positive technology shock, monetary policy would weigh both the resulting boost to aggregate employment but also the negative impact the shock will have on the relative wages of unskilled workers. This would result in policy settings being left at more accommodative levels whereby policymakers tolerate temporarily higher inflation and run the economy hotter (so as to offset the effect of the shock on the wages of lower income workers). Following such an approach would improve distributional outcomes and increase welfare.

- ***The size of the gains from considering the distribution of wage outcomes depends on which policy approach it is compared to.*** The welfare gains are largest when compared to a simple Taylor rule. Welfare gains are more modest, but nonetheless still positive, if the alternative policy is an "optimal control" approach (i.e. where policy minimizes a weighted average of slack and the deviation of inflation from its medium-term target).

Impulse Response to a Positive Technology Shock



Sources: IMF Staff calculations.

Sources: IMF Staff calculations.

The general approach suggested here—which incorporates information on consumption inequality into policy decisions—has parallels in the recent changes that have been made to the Fed's operating framework. Specifically, the new framework (i) explicitly targets an overshooting of inflation following a disinflationary shock; and (ii) reacts only to shortfalls from maximum employment. Both of these features lead to a less pre-emptive approach to policy, a tolerance for temporarily higher inflation, and a willingness to run the economy hot. This analysis does not argue for building consumption inequality into the Federal Reserve's price stability and maximum employment objectives. The insights from such an heterogenous agent model also argue in favor of the Fed's longstanding approach of calibrating policies based on a broad "dashboard" of labor market indicators (including the wage and employment outcomes of lower income households) rather than solely focusing on the level of unemployment.

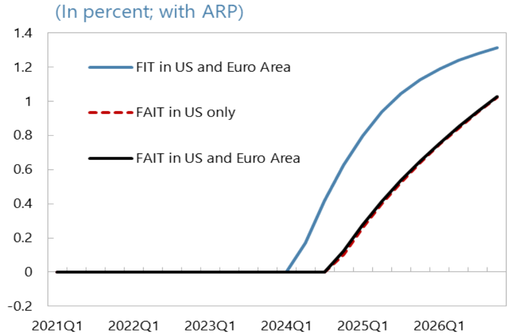
[1] See N-J. Hansen, A. Lin, R. Mano, "Should Inequality Factor into Central Banks' Decisions?", IMF WP 20/196.

Box 3. Spillover Effects From Flexible Average Inflation Targeting

To examine the impact of the Fed's shift in framework from Flexible Inflation Targeting (FIT) to Flexible Average Inflation Targeting (FAIT), simulations were undertaken in the Fed's two-country SIGMA model (calibrated to the U.S. and Euro Area)[1].

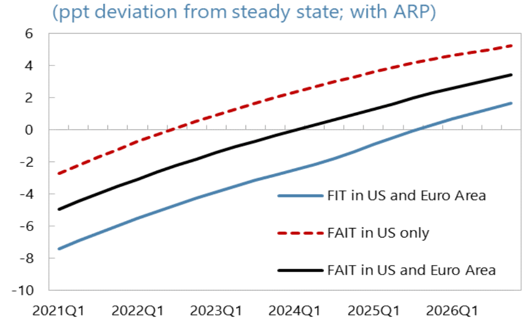
The first thing to note is that the logic of FAIT implies a slower and later pace of normalization in the federal funds rate than under FIT. This more backloaded pace of rate increases supports an overshooting of the 2 percent longer-term goal. Compared to FIT, the lower path for policy rates reduces dollar funding costs, weakens the dollar, and (on net) loosens global financial conditions (creating positive outward spillovers).

Fed Funds Rate
(In percent; with ARP)



Sources: IMF Staff calculations.

Nominal Exchange Rate
(ppt deviation from steady state; with ARP)

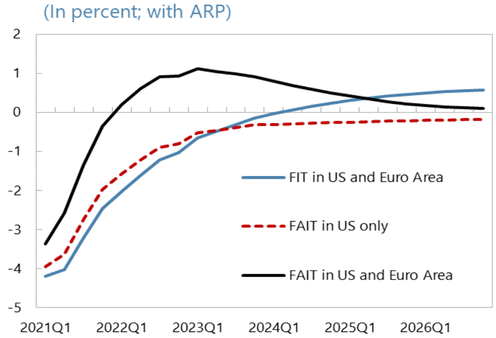


Notes: Positive values indicate US depreciation.
Sources: IMF Staff calculations.

The weaker dollar under FAIT increases U.S. competitiveness and boosts exports. This effect outweighs the higher import demand that arises from stronger U.S. growth. As a result, the U.S. trade balance improves in the near term (by around 0.4 percentage points of GDP relative to FIT) and the positive outward spillovers comparing between FAIT and FIT are relatively small.

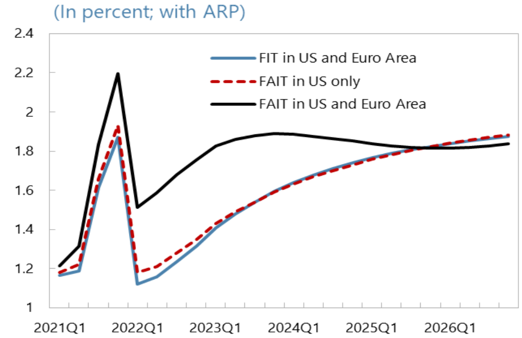
If the Euro Area were to adopt a similar "make-up" monetary policy strategy like FAIT, this would lead to a more prolonged monetary accommodation in the Euro Area. As a result, the dollar would depreciate by less, net external demand from the U.S. would be greater, and both Euro Area output and inflation would be higher. The alternative policy framework would also create positive spillovers to the U.S. As such, the adoption of FAIT policies by both central banks would be self-reinforcing and lead to improved outcomes in both the U.S. and Euro Area.

Euro Area Output Gap
(In percent; with ARP)



Sources: IMF Staff calculations.

Euro Area Core Inflation
(In percent; with ARP)

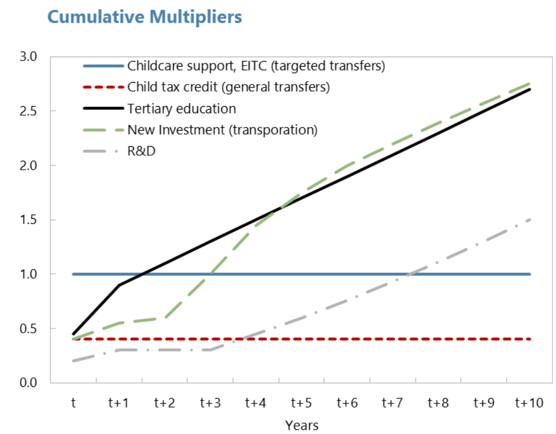


Sources: IMF Staff calculations.

[1] The simulations shown here are based on a baseline incorporating spending under the American Rescue Plan but without the American Jobs and Families Plans.

PUTTING IT ALL TOGETHER

22. The combination of the Rescue, Jobs and Families Plans, in the context of a Flexible Average Inflation Targeting framework, is estimated to add a cumulative 10¼ percent to the level of GDP during 2021–23. The baseline forecast incorporates the effects of both the Jobs and Families Plan based on an assumption that they are passed into law in line with the composition and size described above. Forecasts rely on the empirical and economic modeling literature to define the size of the multipliers for the various policy measures being proposed.[11] The proposed fiscal plans, combined with the more accommodative monetary framework, are expected to reduce unemployment to close to 3 percent and bring labor force participation to pre-pandemic levels by end-2022. Supply-side policies—including infrastructure spending, childcare support, paid family leave, expanded healthcare, and a more generous EITC—are expected to help support labor force participation and productivity over the medium-term, helping to offset an expected demographic downtrend in participation. As a result, potential growth is expected to move up (to around 2 percent) and the level of real GDP would be higher by around 1 percent in 2030. Finally, after taking into account the impact on output and inflation, the three fiscal packages together are expected to add 3-4 percent of GDP to federal government debt by 2026 (see Appendix 2).



[11] The illustrated multipliers represent the (undiscounted) cumulative addition to the level of aggregate demand over a ten year horizon per unit of additional spending.

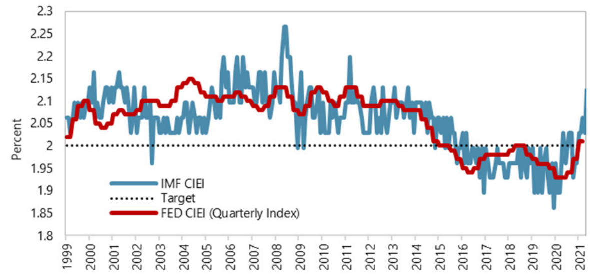
Figure 1. Macroeconomic Impact of American Rescue, Jobs and Families Plans 1/

1/ The change in the core inflation projection in 2021 reflects both the impact of the fiscal package and idiosyncratic relative price movements.

Sources: Haver Analytics; IMF Staff calculations.

23. PCE inflation is expected to rise to around 2½ percent by end-2022. Data points to significant remaining labor market slack[12] which should serve as a safety valve to dampen underlying wage and price pressures. Inflation expectations are also expected to remain well-anchored. Underlying inflation trends will be obscured in the coming months by significant, transitory movements in relative prices which could lead core PCE inflation to temporarily peak later in the year at close to 4 percent. Once these temporary price realignments have passed through the system, tightening labor markets and a persistent positive output gap should allow underlying inflation to rise above the Fed's 2 percent goal in 2022 and remain above for some time. There are, however, important upside risks to inflation that could have systemic implications (see below).

Common Inflation Expectations (as of May 2021)



Notes: Based on a similar methodology and data set as the Fed's CIEI. Data rebased to 10Y SPF PCE equivalent. FED CIEI available up to 2021Q1 at 2.01%.
Sources: Haver Analytics; University of Michigan; Consensus Economics; Federal Reserve; IMF Staff calculations.

24. Strong near-term demand will add to the current account deficit. The U.S. external position is judged to be moderately weaker than the level implied by medium-term fundamentals and desirable policies in 2020 and is expected to weaken further in 2021 (see Appendix 3). Indeed, the current account is expected to register a deficit above 3 percent of GDP until 2024. This current account imbalance is largely driven by the sizable increase in the fiscal deficit. As the fiscal deficit falls, the current account deficit should steadily decline (although much will depend on the pace at which the current, high levels of private savings are drawn down).

25. The spillover impact to global activity from the rapid U.S. rebound is generally expected to be positive, particularly so for Mexico and Canada given their strong trade linkages to the U.S. Although the Treasury yield curve has moved in anticipation of larger fiscal support, most countries are generally benefiting from still-loose global financial conditions and the demand spillovers from the rapid recovery of U.S. consumption and investment. Looking forward, some countries—particularly leveraged EMDEs with weak fundamentals, commodity importers and/or countries with an exchange rate pegged to the U.S. dollar—could, though, face greater pressure in the coming months, especially if dollar funding costs rise abruptly.

26. Authorities' views. The American Jobs and Families Plans, in conjunction with the American Rescue Plan, are expected to provide significant near-term support for the economic recovery, offsetting some of the drag from the expiration of earlier pandemic-related fiscal support programs. In addition, these new proposals may raise productivity and labor force participation, increasing income growth over the medium-term and thereby raising living standards. The recovery is expected to be particularly beneficial for low- and middle-income families with a tightening labor market helping to raise wages and fiscal transfers supporting household income. These policy efforts are

[12] As of May, employment was slightly under 10 million persons below the pre-pandemic trend and the underutilization of labor (as measured by U6) was 10.2 percent, around 3¼ percent above pre-pandemic levels.

expected to have substantial positive spillovers to trading partners and would result, for a time, in an increase in the current account deficit as U.S. demand expands at a faster pace than many of the trading partners. The increase in the U.S. current account deficit could, however, be lessened by greater efforts to boost domestic demand by trading partners. After some near-term volatility in relative prices, inflation was expected to move over the next few years in a way that is in line with the Federal Reserve's objectives under its new Flexible Average Inflation Targeting framework. Longer-term inflation expectations are expected to remain well-anchored at 2 percent.

27. The principal risk facing the U.S. economy continues to emanate from the pandemic (Appendix I). The global infection rate accelerated above its previous peak in April and the threat posed by new variants—that are more infectious and potentially could be resistant to vaccines—is evident. As such, public health efforts in the U.S. need to continue to be applied rigorously, including by targeting populations where vaccination rates are low, and undertaking robust contingency planning to manage another surge of infections. Consideration should be given to establishing a "standing army" for public health to create idle capacity in testing and medical supplies as well as build a rapid-response unit that could be deployed for testing, tracking and treatment of viruses. Furthermore, the U.S. has an important role to play in helping other countries contend with the public health crises, particularly the developing world. This is not only for humanitarian reasons. Prompt international assistance—in the form of vaccines, medical supplies, and public health expertise—will pay dividends for the U.S. itself, lessening the COVID-19 risks ahead. In this regard, recent announcements by the administration of their intent to provide significant quantities of vaccines to other countries are highly commendable.

28. There are downside risks to the outlook from the potential that Congress will legislate a fiscal package that is smaller, or less comprehensive, than the one proposed by the administration. Staff forecasts anticipate an increase in discretionary spending and tax expenditures of US$4.3 trillion over the next decade from the Jobs and Families plans which translates into a cumulative 5¼ percent increase in GDP during 2022–24. These fiscal plans will also have a meaningful, longer-run effect on aggregate supply. Approval of a smaller and/or less effective package of tax and spending would imply less of a boost to both supply and demand and likely, on net, somewhat reduce inflationary pressures and public debt.

29. As the recovery proceeds, disruptive mismatches of supply and demand are possible in the near term. The shortage of key input material, including semiconductors and labor, have already weighed on growth and boosted inflation outturns. Such supply chain constraints are likely to continue creating idiosyncratic, temporary relative price increases. These, in turn, may well lead to volatility in market pricing and make for a more uneven pace of recovery across sectors.

30. An overheating of the U.S. economy that causes a surge in underlying inflation is not a likely outcome but does represent an important risk to both the U.S. recovery and to global prospects (Appendix I and Box 4)**.** A relatively flat trade-off between wage and price inflation and estimates of slack will defray these risks and well-anchored inflation expectations create valuable room for maneuver. Nonetheless, there are forces that could create higher-than-expected inflation:

- A slower rebound in labor force participation—due to public health concerns, retirements, incentive effects from unemployment benefits, or delays in reopening schools and childcare—could create a larger mismatch in the labor market and push wages and prices higher. Historically, such wage pressures have been largely absorbed by corporate profit margins but, given the unprecedented nature of this recession, firms may believe they have greater pricing power, leading to price increases across a range of goods and services that then feed through the supply chain into a faster pick-up in consumer price inflation.

- There are components of the inflation index that have been artificially compressed over the past year because of the unusual COVID circumstances. As these effects fade there could be an unexpectedly rapid pick up in core PCE.

- There is significant uncertainty about how inflation expectations are formed in the U.S. and, as a corollary, there is little evidence on what it would take for expectations to de-anchor upwards. If supply chain disruptions prove to be persistent—set against the backdrop of a pipeline of significant fiscal and monetary support for the economy—then, what are currently believed to be temporary, relative price movements could start to infect inflation expectations and create more broad-based wage and price pressures.

- Finally, the macroeconomic impact of the fiscal stimulus may be larger and more front-loaded than currently assessed (especially given the more accommodative monetary stance). It is worth noting, though, that even with the Jobs and Families Plan, the general government primary balance is expected to register a 7.5 percent of GDP contraction in 2022-23. The size of this fiscal contraction would be larger if Congress legislates a fiscal package that is smaller or more back-loaded than that being proposed by the administration. Alternatively, the expected supply effects (e.g. on labor force participation, new capital formation, and productivity) of the fiscal packages could be smaller or slower to materialize (although forecasts already assume a relatively small and protracted boost to potential that builds over the course of several years). Nonetheless, imbalances resulting from either a more rapid recovery in private consumption or from a different impact of fiscal policies on supply and demand could be larger, leading inflation to move faster and higher than currently forecasted.

31. In the event that these upside risks to inflation are realized, monetary policy will need to adapt quickly. The monetary policy reaction will have the difficult task of differentiating between two possibilities:

- *Relative price adjustments and/or a more front-loaded impact of fiscal stimulus lead to higher realized inflation but medium-term inflation expectations remain well-anchored at the Fed's longer term goal*. In this case, the premium will be on communicating clearly that the changing environment calls for a withdrawal of monetary accommodation. However, the anchored expectations will provide room for maneuver, allowing these policy adjustments to take place along an orderly timeline (i.e., similar to that already incorporated into staff's baseline outlook). While this would imply a somewhat larger, more prolonged inflation overshoot, inflation should still return to the longer run target relatively quickly.

- *High realized wage and price inflation, resulting from a sustained mismatch in supply and demand, proves persistent and causes a de-anchoring of inflation expectations*. This eventuality would necessitate monetary policy quickly changing tack in order to re-anchor expectations. This would mean accelerating the reduction in asset purchases and even having to consider raising policy rates before net purchases have been brought to zero. This would likely create an abrupt shift in financial conditions and risk premia with negative implications at home and abroad.

Clearly, it will be difficult to distinguish, in real time, these two potential out-of-baseline risk scenarios, especially when there is substantial noise from the expected idiosyncratic and transitory shifts in a range of prices. This will likely mean, in the coming months, placing a relatively heavy weight on the evolution of inflation expectations. As the underlying dynamics of inflation become clearer (later in 2021 and into 2022), a greater weight can then be placed on realized inflation in determining the future path for policy.

32. The consequences of a rapid pick-up in inflation could be systemic for both the U.S. and the global economy. If the exhaustion of slack, higher inflation expectations, or a steeper tradeoff between unemployment and inflation create a faster-than-expected rise in inflation, markets would begin to reprice both the path for policy rates and the inflation risk premium embedded in dollar funding costs. This could create an up-front steepening of the yield curve that may precede—or, for some countries, more-than-offset—the positive demand effects arising from the strong U.S. recovery. Risk premia could rise across a range of assets and the resulting abrupt tightening of financial conditions would pressure firms and households (particularly those that are highly leveraged), slowing the recovery or even tipping the U.S. into a renewed downturn. This confluence of events would be bad news for the global economy. A synchronized tightening of global financial conditions at the same time as the U.S. recovery is slowing would hurt almost all countries but would hit particularly hard Canada, Mexico, and those emerging markets with significant gross external financing needs.

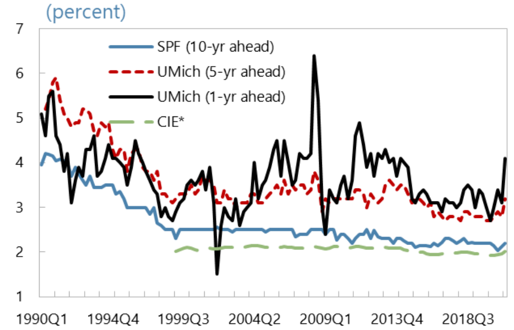
33. Authorities' views. Although unexpected shifts in the trajectory of the pandemic pose an important risk, it was expected that the measures underway to expand vaccinations and contain the virus would significantly mitigate these downside risks. Successful public health efforts may create an upside risk to the path of recovery with demand potentially being faster and more front-loaded than currently expected. An unexpected surge of inflation or a de-anchoring of inflation expectations were viewed as a tail risk but, if realized, would be disruptive. It was expected, though, that the strong credibility of the Federal Reserve would serve to anchor long-term inflation expectations and would dampen any demand-driven wage and price pressures. Nonetheless, the FOMC was committed to acting promptly in the event that there were signs that long-term inflation expectations were becoming de-anchored or if inflation was evolving in a manner that was inconsistent with the Fed's price stability mandate.

Box 4. Assessing Possible Inflation Paths

Following significant volatility in 2021, core PCE inflation (q4/q4) is expected to rise to 2.6 percent by 2023 and then converge to the Fed's 2 percent long-run target from above. In large part, this outlook relies on an assumption that inflation expectations remain anchored (as they generally are assessed to have been since the mid-1990s).

To examine the scope for upside risks to inflation in a general equilibrium setting, simulations are done in the SIGMA model, calibrating the Phillips curve based on the behavior of inflation and unemployment before the Global Financial Crisis. In the model, the Federal Reserve is assumed to follow a flexible average inflation targeting (FAIT) rule with zero as the effective lower bound for the fed funds rate. Simulations from the SIGMA model are complemented by similar exercises using the FRBUS model and the IMF's G20MOD. In general, the path for core inflation demonstrates a modest overshoot, propelled by the American Rescue, Jobs and Families Plans (although G20MOD shows a larger and more persistent inflation impact).

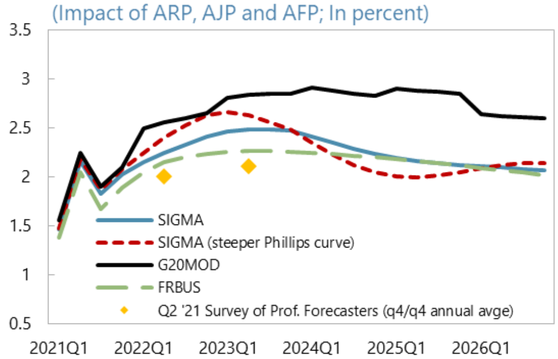
Inflation Expectations
(percent)



*Index of Common Infl. Exp. projected onto SPF (10-yr ahead).
Sources: Philadelphia Fed, University of Michigan and Staff calculations.

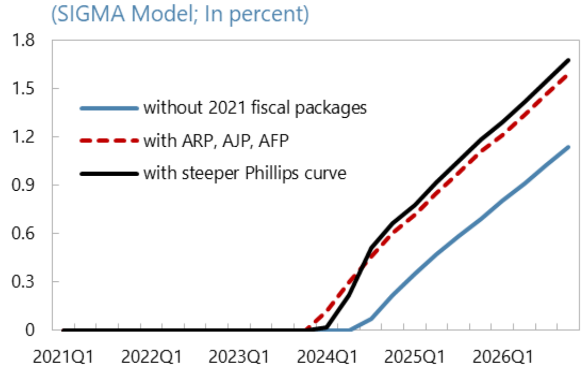
The inflationary impact of a steeper Phillips curve[1] is found to have relatively modest effects in the SIGMA model. In the near term, core inflation would be higher by around 0.4 percentage points. This is largely because the "model-consistent" inflation expectations in the simulation remain well-anchored by the FAIT policy rule. This would suggest that the risks of a sustained pick-up in inflation would likely need to arise from a material shift in expectations (i.e., stronger demand effects or a steeper Phillips curve would likely not be sufficient if expectations remain well-anchored).

Core PCE Inflation
(Impact of ARP, AJP and AFP; In percent)



Sources: IMF Staff calculations.

Fed Funds Rate
(SIGMA Model; In percent)



Sources: IMF Staff calculations.

[1] The parameter determining the impact of higher marginal costs in the model's New Keynesian Phillips curve is calibrated to be around three times larger than in the baseline simulations.

CONTEMPLATING FUTURE FISCAL CONSOLIDATION

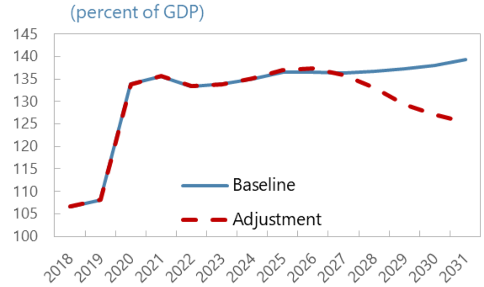
34. The debt-GDP ratio fails to stabilize under the policies assumed in the baseline but the overall risks of sovereign stress are judged to be low and the debt is viewed as sustainable[13] (Box 5 and Appendix II). The planned changes to the tax system will defray some of the impact of higher spending on the deficit and debt but further actions will be needed over the medium-term to bring the debt down. This reflects the impact that the aging population and rising healthcare costs—which over the medium-term are much more important drivers of debt dynamics than the planned fiscal packages—are likely to have on mandatory spending.

35. In addition to the policies described above—i.e., an improved targeting of spending and tax credits to lower income groups, a reduction in tax expenditures, the introduction of a carbon tax and higher fuel taxes, and an increase in the taxation of inherited wealth—further measures should be considered. These could include:

- Introduction of a broad-based federal consumption tax levied at a relatively low rate with the effect on lower income groups offset through increases in targeted assistance (e.g. by increasing food assistance programs, refundable child tax credits, and the EITC).
- Accelerating the planned increase in the retirement age, increasing the progressivity of social security benefits, raising the maximum taxable earnings for social security contributions, and indexing benefits to chained CPI.
- Containing healthcare cost increases through greater cost sharing with Medicare beneficiaries, efficiency innovations (such as expanded telehealth services), incentives to increase price transparency by healthcare providers, tackling market power among health care providers, and increasing competition in drug pricing.
- An increase in the minimum age for Medicare eligibility alongside an expansion of Medicaid and tax credits to ensure that coverage is maintained to elderly, lower income households.

Such actions on both the revenue and spending side should aim to bring the federal primary balance to 1 percent of GDP (a general government primary balance of ½ percent of GDP). In doing so, the general government debt-to-GDP ratio could be put onto a downward path by 2027 (lowering general government debt to 125 percent of GDP by 2030, which is still well above any pre-pandemic level).

General government debt
(percent of GDP)



Source: IMF staff calculations.

[13] In previous consultations, debt was characterized as being "on an unsustainable upward path under current policies". The debt sustainability assessment now reflects the approach taken in the IMF Board-approved definition of public debt sustainability that "the primary balance needed to at least stabilize debt under both the baseline and realistic shock scenarios is economically and politically feasible, such that the level of debt is consistent with an acceptably low rollover risk and with preserving potential growth at a satisfactory level" (see Review of The Debt Sustainability Framework For Market Access Countries, 2021).

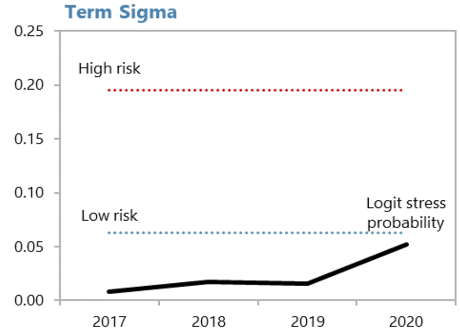
36. Authorities views. The U.S. was viewed as having substantial fiscal space which provided important room for maneuver in its conduct of fiscal policy. While projections suggested that the federal debt-GDP ratio would continue to rise slowly over the medium-term, the path for real interest spending as a share of GDP was expected to remain well below historical levels. This suggests that the U.S. debt servicing capacity did not present a particular constraint, even if debt-GDP were to rise further. Nonetheless, it would be desirable, as the economy gets closer to full employment, for the debt-GDP ratio to start declining so as to rebuild fiscal buffers over the medium-term.

Box 5. The Sovereign Risk and Debt Sustainability Framework: An Application to the U.S.[1]

The new framework finds the overall risk of sovereign stress in the U.S. to be low.

Risk of Sovereign Stress			
	Mechanical signal	***Final assessment***	***Comments***
Overall		Low	Assessment reflects mitigating factors: the strength of institutions, the depth of the investor pool, the role of the U.S. dollar in the international system, and the Fed's stabilizing role.
Near term	Low	Low	
Medium term	Moderate	Low	
GFN:	Moderate	Low	
Fan chart:	Moderate	Moderate	
Stress-test:	*N.A.*		
Long term		*N.A.*	

Determination of Mechanical Near-Term Sigma

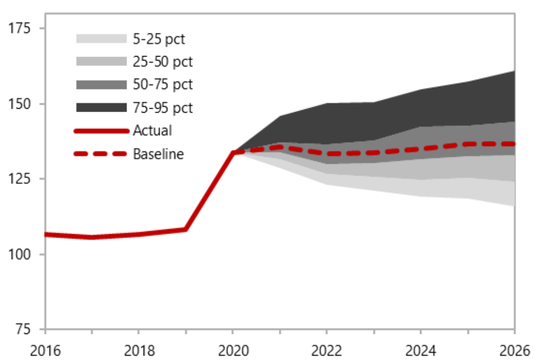


The quality of institutions and absence of history of stress imply a ***low near-term risk of a debt crisis.*** The jump in the debt-GDP ratio in 2020 did, however, lead to a modest rise in the probability of stress during 2020.

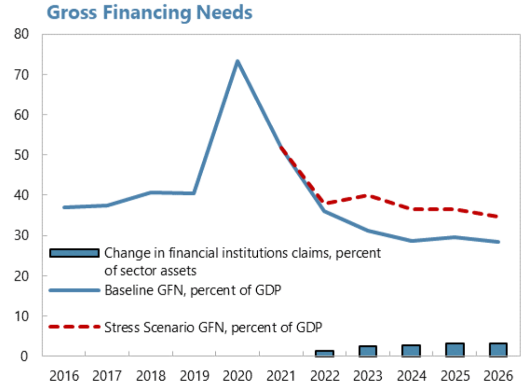
Medium-term risks are low. The fan chart's mechanical signal shows a "moderate" risk as a result of the elevated debt level forecast for 2026 (the probability of debt stabilizing in the next five years is assessed to be only 40 percent).

The mechanical signal indicates the ***risks from gross financing needs module's is moderate.*** The large GFN is a product of a high stock of debt as well as the sizeable issuance of short-term debt (around one third of general government debt has a residual maturity of less than one year). However, non-bank financial institutions are a major holder of general government debt (in part due to the prevalence of defined contribution pension schemes) so that a sudden rise in financing needs should be easily absorbed the U.S. diversified pool of domestic and international investors.

Debt Fanchart (percent of GDP)



Gross Financing Needs



[1] See Review of The Debt Sustainability Framework For Market Access Countries, IMF Policy Paper 2021/003.

THE CHALLENGE OF BUILDING BACK BETTER

37. The U.S. is facing multiple transitions in the coming years that will have important socio-economic implications.

- A ***pandemic*** recovery that likely creates lasting shifts (in the U.S. and abroad) in consumer preferences and in the modalities by which the economy operates.
- The move to a ***low-carbon economy*** will necessitate a significant reallocation of labor and capital (e.g. away from fossil fuels and heavy industry and toward renewables) and, potentially, a very different set of skills.
- A ***demographic transition*** that is already underway with 22 percent of the population is expected to be over-65 by 2040, the number of Americans over-85 expected will double by 2035, and the population will be increasingly racially diverse.
- Finally, ***digitalization*** and other evolving technologies will remake both production and consumption in unpredictable ways.

38. The longstanding flexibility and innovativeness of the U.S. system puts it in a good place to manage these transitions. However, great care should be taken to ensure that these multi-faceted changes do not increase income polarization, further hollow out the middle class, and leave behind a material share of the population (particularly lower-skilled, lower-income workers). A more effective social safety net and broader healthcare coverage will help. So too will increased investments in vocational and academic education. Greater spending on public investment can raise labor productivity and help improve living standards. However, other strategies may well be needed. These could include regional development initiatives to facilitate the transition. There may be a need to subsidize labor mobility (especially if newly created jobs are in areas where the cost of living and of housing is higher). Efforts will be needed to ensure schools and colleges are equipped to provide students with the basic technical and critical thinking skills needed for a fast-changing economy. Also, immigration policies will need to be re-examined to ensure there is the right supply of skills needed to meet the demands of the newly-created jobs.

39. Authorities' views. The administration was committed to ensuring that future economic outcomes were as inclusive as possible. Even before COVID-19, too many American families were struggling to make ends meet and too many Americans had been left behind. Policy was, therefore, singularly focused on ensuring that the old economy's structural weaknesses and inequalities were not repeated. Various strategies would be deployed to support households and to facilitate the transition to a greener, more productive, more competitive, and more equitable economy.

A. Health Care

40. The pandemic exposed serious shortcomings and fractures in the extraordinarily complex U.S. health system. The U.S. health system is very costly (Box 6), fragmented, and with highly unequal access and variable quality. Although the share of the population without health insurance fell markedly after the introduction of the Affordable Care Act, the number of uninsured has been rising since 2016 (adding 2.2 million to the number of uninsured between 2016 and 2019). The uninsured population is typically low income, with at least one worker in the family, and disproportionately black and Hispanic. Also, with over half the population reliant on employer-provided health insurance, millions face the prospect of losing coverage when unemployment surges (as it did during the pandemic).

41. Important steps have been taken in the first few months of the administration to address maintaining and expanding access to healthcare. The American Rescue Plan covered the costs of keeping laid-off workers on their former employer's healthcare plan until September 30. The plan also fully paid for coverage for the lowest income workers, increased premium subsidies for those earning up to 400 percent of the federal poverty level, and capped the costs an individual pays for a benchmark plan. In addition, the American Rescue Plan increased the incentives for states to expand Medicaid (to cover a larger share of low-income households). The administration has reopened the enrollment period for policies sold on the federal health insurance exchange and significantly increased spending to raise public awareness and encourage people to purchase a policy, or even upgrade their existing policy, on the exchange. The early indications are that these efforts are working and that the number of uninsured has been put back on a downward trajectory.

42. Authorities' views. The measures taken under the American Rescue Plan are expected to have an important impact on both the coverage and affordability of healthcare. This was being clearly demonstrated in the number of families signing up for health insurance during the special enrollment period. The administration remains committed to providing people aged 60 or older the option to enroll in the Medicare program. Reforms are also intended to bring down drug prices, including by letting Medicare negotiate payment for certain drugs. U.S. healthcare costs were viewed as very high and this level of spending was not leading to better health outcomes. A number of factors were at work to boost costs including technological innovations that improved health outcomes, adverse incentives created by the pay-per-procedure model, and a lack of transparency in pricing. The increased consolidation of the health sector in recent years was increasing market power, particularly in certain local markets, which was boosting costs. Finally, the uneven quality of U.S. healthcare remains an important concern with lower income communities having less access to high quality care.

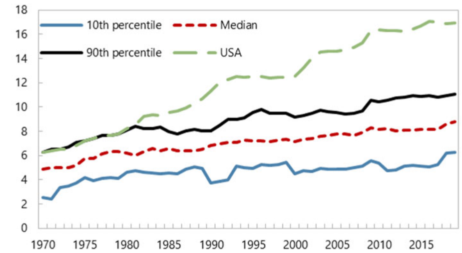
Box 6. The High Level of U.S. Healthcare Costs

Healthcare in the U.S. is the most expensive in the world and the cost gap relative to international comparators has grown over time. About three quarters of the cost differential between the U.S. and OECD comparators is accounted for by inpatient and outpatient care. Despite the significant resources devoted to healthcare, the U.S. underperforms across a range of health outcomes (e.g. life expectancy, population coverage, etc.).

Market power in the U.S. health industry has increased significantly since the 1980s, which has contributed to rising costs.[1] Analysis of micro-data on publicly listed firms in the healthcare sector and hospitals shows that:

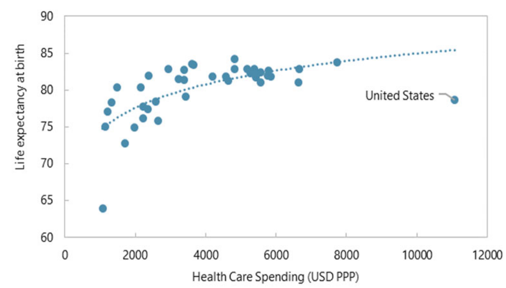
- Overall markups (defined as the ratio of price to marginal cost of production) almost doubled since the early 1980s. Hospital markups have also increased significantly (by more than 6 percent on average) since the late 1990s across U.S. states.
- Rising healthcare sector markups are estimated to account for about one quarter of the increase in per capita healthcare costs in the U.S. since the 1980s.
- Hospital markups alone are responsible for 15 percent of the variation in healthcare spending across states.
- Rising hospital markups are not, however, associated with lower labor costs or insurance markups (suggesting that providers use their market power to raise prices to consumers rather than taking advantage of their monopsony power to lower payments to providers further down the supply chain).
- Physicians' salaries have risen above pace for salaries of non-physicians (even after controlling for years of education and experience).
- The Medicaid expansion has increased practitioner wages suggesting a relatively inelastic supply response to the welcome increase in coverage that resulted from the Affordable Care Act.

OECD Countries: Cost of Healthcare
(Percent of GDP)



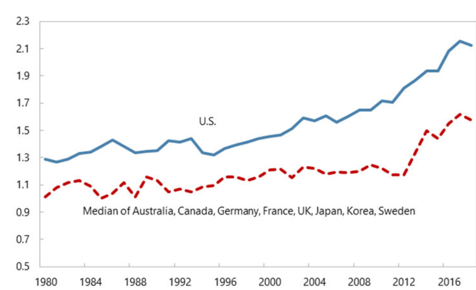
Sources: OECD, IMF Staff calculations.

Life Expectancy and Health Care



Sources: OECD, IMF Staff calculations.

Median Healthcare Sector Markups



Sources: Thomson Reuters, IMF Staff Calculations.

The significant contribution of market power to healthcare costs suggests the need for carefully-considered policy responses. Licensing requirements or limits on the flow of new medical professionals are necessary to underpin the quality of services but have become an increasingly binding constraint to entry that may need to be recalibrated. Similarly, ongoing mergers and acquisitions may offer providers greater scope to engage in non-competitive pricing. This would argue for a more assertive approach to antitrust policies (at both the federal and state level) to identify and counter any restraints of trade that are unreasonably restricting competition in the provision of health services. Lower markups would help increase efficiency but would also lower the burden that healthcare places on the fiscal accounts.

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[1] See L. Lin, M. Mrkaic, and A. Weber, "U.S. Healthcare: A Story of Rising Market Power, Barriers to Entry, and Supply Constraints." IMF Working Paper 21/180.

B. A "Greener" Economy

43. The administration has rejoined the Paris Climate Accord and has committed to reducing net greenhouse gas emissions by 50–52 percent by 2030 (relative to 2005 levels). A principal focus of the administration's plan is to make the U.S. power sector carbon-neutral by 2035 by spurring an expansion of renewables and retrofitting existing thermal and nuclear plants. Investments are also proposed to increase the transmission capacity and resilience of the current electrical grid. In transportation, efforts will be made to tighten fuel efficiency standards, subsidize zero emission cars, build electric vehicle charging infrastructure, invest in public transit, and replace school buses, transit vehicles, and the federal fleet with electric vehicles. To increase the energy efficiency of buildings, resources are proposed to retrofit federal buildings, schools, commercial buildings, and homes for low income households. There are also provisions to support R&D in green technologies as well as remove existing tax preferences for fossil fuel companies.

44. The administration's new impetus to reduce greenhouse gases represents a critical, and very positive, change of direction. While many of the steps that will be needed to achieve the administration's climate goals have yet to be defined, the broad scope of the plans that have already been articulated (and the significant investments that are expected to be made), if realized, will jump-start the transition to a low carbon economy. However, it will be costly and difficult to achieve the administration's climate objectives without a greater focus on carbon pricing (Box 7) and sectoral-based policies to tilt incentives away from carbon-intensive activities (Box 8). In the meantime, as political support is being built for a carbon tax, regulatory actions could be strengthened to increase the disincentives for greenhouse gas emissions. Announced efforts to reduce implicit subsidies for the fossil fuel industry are important. However, a similar approach is needed for the agro-industrial sector (Box 9). Finally, shifting to a low emissions means of generating electricity will be essential to achieve the administration's climate goals (Box 10).

45. Authorities' views. The administration is committed to achieving its revised, nationally determined contribution under the Paris Agreement and work is already underway to ensure the power sector would be carbon-neutral by 2035 and that the economy would have net zero emissions by 2050. Policies are being designed to ensure that tackling climate change and creating well-paying, union jobs go hand-in-hand. At the same time, climate policies would be structured so as to protect public health and advance environmental justice. Substantial investments were being proposed to both mitigate climate change and to improve the economy's resilience to its effects. These include improving the energy efficiency of federal buildings and low-income housing; increasing resilience to wildfires, flooding and drought; building out infrastructure for electric vehicles and electrifying the federal fleet; remediating abandoned oil and gas wells; and investing in climate science and research in clean energy technologies. The administration is also looking for ways to provide incentives for the adoption of conservation practices that reduce emissions and enhance carbon sequestration in soils and ecosystems which should provide meaningful climate mitigation and improve the profitability of agriculture and forestry.

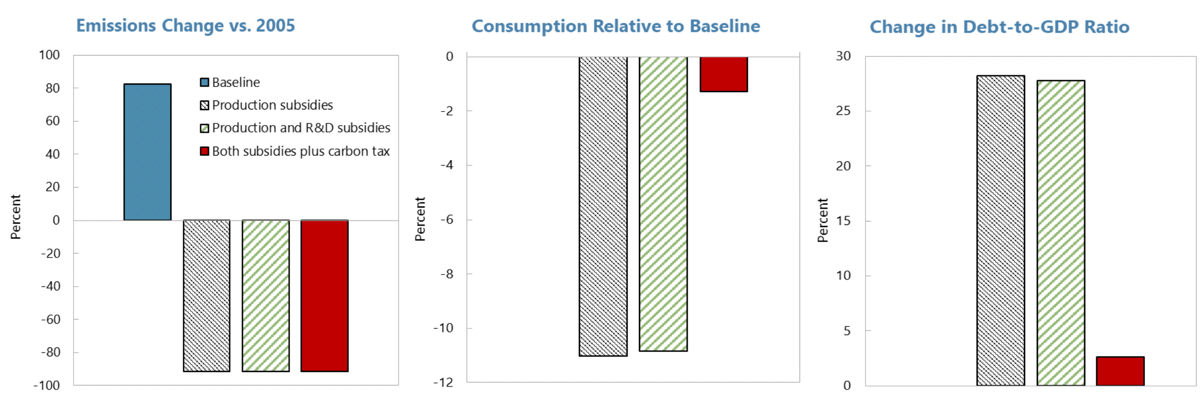
Box 7. Achieving the Administration's Emissions Goals With, and Without, Carbon Pricing

To assess the potential of different policy packages to achieve the administration's climate goals we examine a range of simulations in a macroeconomic climate model with endogenous R&D[1] and find that:

- ***Relying on production subsidies alone to incentivize clean energy is fiscally costly.*** First, unlike pricing carbon, production and R&D subsidies for clean energy add directly to public expenditures. Second, subsidies *lower* the relative cost of clean energy which incentivizes a switch away from high carbon energy but also adds to total energy demand. This energy demand channel makes subsidies less effective, especially in cases where carbon-intensive energy cannot be easily substituted for. Third, the fiscal costs of the subsidies rise over time in proportion to the increased use of clean energy. Deficit-financed subsidies serve to boost aggregate demand but also add 28 percent of GDP to the debt stock by 2050.
- ***Clean energy subsidies can be more effective if combined with carbon pricing***. Carbon pricing is a highly effective policy tool since it raises the overall cost of energy and creates first-order reductions in energy demand. This can then amplify the incentives to shift away from carbon-intensive energy created by subsidies. Front-loaded subsidies (to both R&D and to the production of clean energy), combined with a carbon tax (that starts at US$17 per ton of CO2 and gradually rises by around 9 percent per year), would be able to achieve the administration's targeted reduction in emissions but without adding to debt-GDP.

It is worth noting that the model simulations assume unilateral U.S. actions. The benefits from a comprehensive U.S. approach could also catalyze a more ambitious set of climate policies by other countries. U.S. support for clean energy R&D would also create scale for those investments and have broader positive spillovers, creating new green technologies that could then be adopted by others.

Tax and Subsidy Policies to Achieve the U.S. Emissions Targets



[1] See P. Barrett, "Can International Technological Diffusion Substitute for Coordinated Global Policies to Mitigate Climate Change?", IMF WP 21/173.

Box 8. "Pricing" Policies to Strengthen U.S. Greenhouse Gas Mitigation[1]

As discussed in Box 7, economic efficiency argues for a broad-based carbon tax in the U.S. to integrate carbon charges into federal fuel taxes and extend them to coal, natural gas, and other fossil fuels. Such a tax would provide a robust price signal that would reduce energy demand and redirect investment to cleaner technologies.

Sectoral carbon pricing instruments could, however, provide a helpful, reinforcing complement to such a carbon tax. A promising approach is through feebates that impose a revenue-neutral, sliding scale of fees on activities with above-average emission intensities combined with rebates for activities with below-average emission intensities. Feebates would:

- Promote a reduction in the emissions intensity of a particular sector (for example, feebates may encourage investments in lower-emissions vehicles but without, on aggregate, encouraging people to drive less) that would complement a first-order demand response from a carbon tax.
- Be cost-effective compared to regulatory limits (the latter would need to be complemented by a credit trading scheme to achieve a similar degree of efficiency).
- Create certainty over future emissions prices (especially compared to trading systems where pricing is sensitive to the balance of demand and supply).
- Not impose an additional fiscal cost (unlike the clean technology subsidies discussed in Box 7).
- Avoid an additional tax burden (beyond that created by economy-wide carbon pricing) on the average household or firm.
- Be complementary to regulations in providing market incentives to exceed those regulatory standards.

Feebates in the transportation sector. New vehicle sales could be taxed/subsidized at a rate that is equal to the product of (i) the desired carbon price; (ii) the difference between the vehicle's emissions per mile and the fleet average; and (iii) the average lifetime mileage of the vehicle. Such an approach would provide a more comprehensive incentive to purchase fuel-efficient vehicles than the current system (i.e., electric vehicle subsidies combined with taxes on cars that average less than 16 miles per gallon or CO2 emission rates above 700 grams per mile). A feebate design would have the advantage of building in an automatic reduction in the size of the subsidy for EVs as the average emission rate falls.

Feebates in the power sector. Generators could be taxed/subsidized based on the product of (i) the desired carbon price; (ii) the difference between the generator's CO2 per kWh and the industry average; and (iii) the generator's total output.

Feebates in other sectors. Similar tools could be used to promote greenhouse gas mitigation in industry (similar to Canada's output-based performance standard), for new appliances, and in agriculture. Feebate tools could also provide market incentives for carbon sequestration (e.g. through subsidies for wetlands or forests).

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[1] See I. Parry, "Implementing the United States' Domestic and International Climate Mitigation Goals: A Supportive Fiscal Policy Approach." IMF Working paper 21/57.

Box 9. Meeting the U.S. Climate Goals—The Potential Contribution from Agriculture

During 2019, emissions from U.S. agriculture totaled 669 million metric tons of CO_2-equivalent (10 percent of total U.S. emissions or approximately equal to the CO_2-equivalent emissions of France and Italy combined). U.S. agriculture is fossil fuel-intensive and uses a significant amount of chemical fertilizers and pesticides as inputs. Nearly 80 percent of U.S. agricultural emissions are related to the production of animals and animal feed. These emissions are particularly important because farm animals and their manure, along with the oil and gas industries, are the leading sources of methane emissions (a pollutant that is shorter-lived than carbon dioxide but far more powerful as a greenhouse gas). According to the UN Intergovernmental Panel on Climate Change, rapidly reducing methane is the strongest up-front action available to slow global warming and limit its consequences over the near term.

Various federal policies—including federal payments to supplement farm income, subsidize loans, duties on imported agricultural products, and crop insurance—create distortions that incentivize the overproduction of high-emission crops and animals.[1] In addition, the Renewable Fuel Standard (requiring transportation fuels to contain a minimum biofuel content) adds to agriculture's carbon footprint (by fostering the expansion of industrially-run, chemically-fertilized corn farms) and potentially diverts agricultural capacity away from food production.

The administration's plan for Climate Change and Environmental Justice proposes paying farmers to increase the amount of carbon stored in soil (e.g. by supporting no-till agriculture and the planting of cover crops). A broader, "all-of-government" approach should be considered that examines the full range of federal incentives and restrictions through the lens of their contribution to greenhouse gas emissions. This would both support the administration's ambitious climate goals while offering co-benefits in terms of local communities' jobs, food justice and public health.[2] Potential policies could involve:

- Phasing out agricultural subsidies that incentivize high-emission farming activities (in a similar vein to the administration's commitment to phase out federal subsidies for fossil fuel providers).
- As discussed in Box 8, designing feebate schemes based on farm output and relative emissions intensity.
- Expanding crop insurance subsidies to a broader set of crops and livestock but conditioning them on recipients meeting benchmarks for greenhouse gas emission reductions. The benchmarks could, for example, be calibrated to attain a gradual reduction in the number of livestock over time.
- Federal insurance could be capped for larger agricultural producers so that their additional insurance needs would be met through actuarially-fair insurance from private providers.
- Targeting subsidies and loans to support fishing and marine farming practices that are compatible with marine biodiversity conservation (such as shallow trawlers and/or regenerative ocean farming).
- Providing federal funding for R&D in lower-carbon agricultural practices and to develop more climate-friendly products.

[1] See, among others, B. K. Goodwin and V. H. Smith, 2013; F. Annan and W. Schlenker, 2015; and E. Njuki, 2020.

[2] See, for example, N. Batini, *The Economics of Sustainable Food: Smart Policies for People and The Planet*, Island Press and International Monetary Fund, 2021 and N. Batini, J. Scorse and S. Secchi, "The Role of Economic Policy in Reducing Emissions and Protecting Natural Ecosystems in the U.S. Agriculture, Fisheries and Forestry Sector", mimeo, 2021.

Box 10. The Importance of Prioritizing the Greening of the Power Sector

Remaking the power and transportation sectors will be key to achieving the administration's climate targets. The two account for more than half of total emissions and are highly complementary: low power sector emissions help "green" electric vehicles.

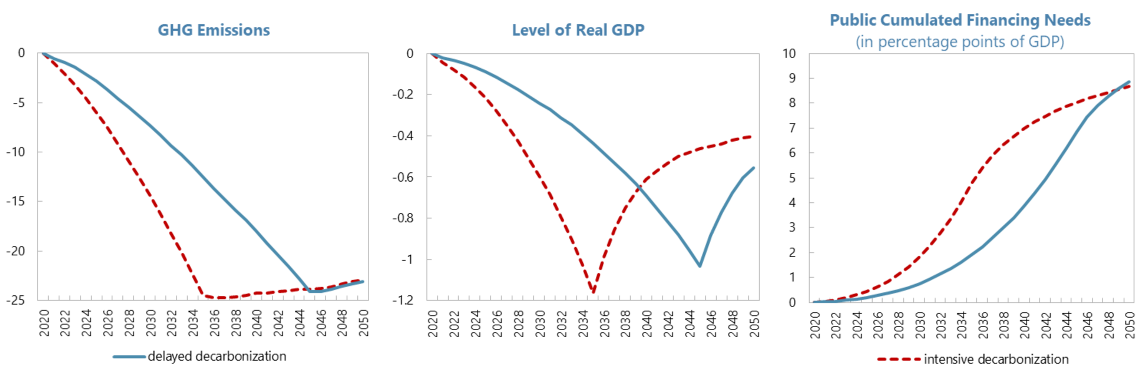
A dynamic computable general equilibrium model[1] is used to simulate two scenarios:

- "Intensive decarbonization" where fossil fuel power generation is phased out by 2035.
- "Delayed decarbonization" where the phase-out is delayed to 2045.

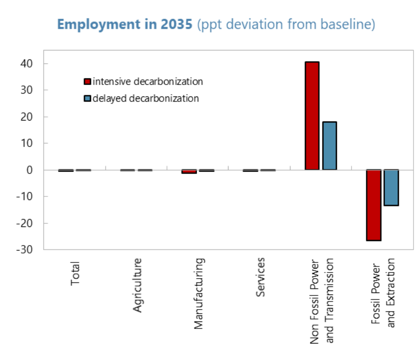
Both scenarios assume a rapid penetration of electric vehicles (see IEA's Sustainable Development Scenario), which, on its own, would lead to higher emissions in 2021–30. Two power sector policies are also assumed: (i) subsidies for wind and solar power generation; and (ii) a Clean Energy Standard that requires a rising path for non-fossil fuel generation.[2] Subsidies are progressively scaled back once the emissions targets are achieved.

Intensive decarbonization achieves the administration 2035 goals for the power sector and carries lower GDP costs and public financing needs by 2050 (relative to the delayed decarbonization scenario). Early decarbonization reduces total emissions by 25 percent relative to the baseline by 2035. Cumulative GDP losses peak at 1.2 percent below baseline in 2035 (i.e. less than 0.1 percentage points of GDP per year). On the other hand, "delayed decarbonization" achieves a mere 13 percent reduction by 2035 with similar GDP losses and cumulative public financing needs by 2050. This reflects the early payoffs from supporting green technologies and the fact that costly subsidies can be phased out at a sooner point under "intensive decarbonization".

Scenarios to Decarbonize the Power Sector (Ppts deviations from baseline)



This transition has limited overall labor effects but implies an important rotation from high- to low-emission sectors. By 2035, fossil fuel sectors could lose around 26 percent of their workforce. Losses are larger for fossil-fueled power generation than for extractive sectors (the latter increase their exports and divert supply to non-power sectors). Renewables and electricity distribution see their employment rise by 40 percent. This significant transition of workers will not be frictionless and is likely to give rise to locational and skills differences that will need to be addressed.



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[1] See D. Van der Mensbrugghe, "The ENVISAGE model", 2020, and J. Chateau et al., "OECD ENV-Linkages Model", 2014.

[2] Subsidies are calibrated to reach emission targets while keeping the Clean Energy Standard at a level that imposes a shadow cost similar to a sector-level carbon tax that rises gradually from zero to around US$70 per ton by 2050. For a set of potential optimal policies, see Stock and Stuart, "Robust Decarbonization of the US Power Sector: Policy Options", 2021.

C. A More Resilient Financial System

46. The unfolding pandemic revealed important shortcomings in the functioning of critical U.S. markets. The Treasury market has long been the deepest and most liquid fixed income market in the world. However, in March 2020, the market showed itself unable to digest the significant shift of assets from prime and tax-exempt funds to money market funds backed by Treasury securities. Unprecedented selling by bond mutual funds, trying to meet investor redemptions, overwhelmed broker-dealer intermediaries facing both balance sheet constraints and internal risk limits. At the same time, foreign official institutions were liquidating reserve assets to provide dollar liquidity to their own markets, market volatility was forcing leveraged investors to exit positions, and margin requirements were increased for investors with derivative exposures. Finally, nonfinancial corporates were active in drawing down their credit lines at banks to prepare for a pandemic-related cash crunch (which further reduced banks' balance sheet space to provide liquidity). All of these forces combined to exacerbate pressures in both Treasury and money markets. The problems in Treasury and short-term funding markets spilled over and created liquidity shortages also in markets for commercial paper, short-term municipal debt, and negotiable certificates of deposit.

47. The confluence of factors quickly forced the Fed to step in to restore market functioning. To short-circuit these fire sale dynamics, the Fed absorbed US$2 trillion in securities over the space of two months and quickly activated a range of facilities to simultaneously inject liquidity across a broad range of markets.

48. Preventing a recurrence of those vulnerabilities that manifested in March 2020 will require a range of changes across markets and institutions.[14] The size of the U.S. Treasury market and its systemic importance argue for robust measures to prevent another episode of market illiquidity that triggers the need for Fed intervention. In this regard, it is of concern that in March 2021 there were signs of a reoccurrence of deteriorating market liquidity. Possible changes that could be considered include:

- *Central clearing of Treasury market transactions.* With broker-dealer balance sheets increasingly constrained (especially relative to the size of the Treasury market), serious consideration should be given to mandating central clearing of all Treasury transactions (with the clearinghouse subject to strict supervisory oversight as well as robust resolution planning).

- *The introduction of a standing repo facility.* To create greater certainty about the availability of market liquidity in times of stress, the Fed could introduce a standing repo facility aimed at a broad selection of well-supervised banks and nonbanks. The existing FIMA repo facility (for foreign official institutions) should also be made permanent.

[14] On, March 31, the Financial Stability Oversight Council discussed the activities and performance of open-ended mutual funds and hedge funds during the COVID crisis. Chairperson Yellen called for an interagency effort to assess potential financial stability risks associated with open-end funds (focusing on liquidity risks) and to diagnose the causes of recent Treasury market disruptions with a view to enhancing market resilience.

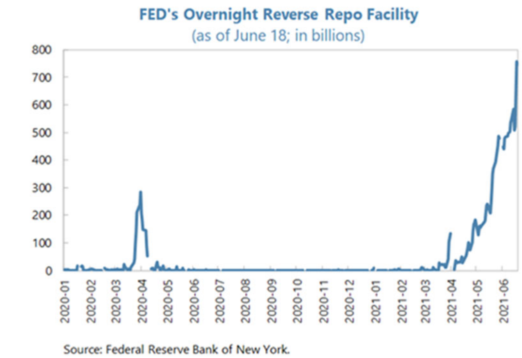
- *Floating net asset value*. Retail prime, institutional government, and tax-exempt money market funds should be required to move to a floating net asset value (so as to mitigate run risks).

- *Stress testing*. There would be merit to subject funds to an annual liquidity stress test—similar to the Fed's supervisory stress test of bank holding companies—to ensure that funds are able to continue operating effectively in a tail-risk scenario.

- *Enhancing fund liquidity*. More liquidity protections could be required from funds, perhaps applied proportionally to the illiquidity of the funds' assets. These protections could include more binding (and possibly countercyclical) liquid asset requirements, pre-determined arrangements that lock-in a proportion of an investor's shares for a minimum amount of time, use of in-kind redemptions to meet withdrawals by institutional investors, swing pricing, and requirements that would temporary gate outflows under certain conditions.

49. Accommodative financial conditions and the rapid pace of economic recovery have encouraged continued risk-taking. Loose financial conditions, that were engineered to support the recovery, have led to an upward surge in asset prices and a compression of risk premia. Most notably, spreads on risky debt have fallen to multi-year lows (although measures of the equity risk premium remain close to historical averages). Corporate leverage is high relative to history although rollover needs are relatively small (only around 5 percent of non-investment grade is due within 1 year as firms have been able to refinance debts at longer maturities and lower costs). Policy support and the longer duration of corporate liabilities have allowed the business sector to weather the COVID shock remarkably well. However, the financial situation of smaller businesses is uncertain with the PPP program potentially masking underlying vulnerabilities.

50. Going forward, rising corporate and nonbank leverage poses a systemic risk. The banking system appears to be in a strong position, despite the very large shock experienced last year. Solid profitability, restrained capital distributions and buybacks, and a relatively small effect of the pandemic on credit quality have ensured that bank capital levels are now above pre-pandemic levels and resilient to even a severe stress test. Banks remain highly liquid and high household savings have increased deposit inflows and reduced funding risks. Credit risks emanating from ongoing structural shifts in commercial real estate are, though, of concern with rising vacancy rates, falling rents, and increasing delinquencies (notably for debt linked to retail and hotels). Also, the phasing out of government support schemes will potentially lead to increased delinquencies but banks have built up loan loss allowances that should allow them to readily absorb such a deterioration of credit quality. On the other hand, leverage in nonbanks has increased and both life insurance companies and hedge funds are exposed to lower-rated corporate debt. This creates the potential for systemic problems to emerge from, or be propagated by, nonbanks. These concerns are not lessened by recent episodes that highlight the incompleteness of the available information on nonbanks' risk profile (including for family offices). In the absence of well-targeted macroprudential tools to manage such risks, consideration should be given to building larger buffers in the more regulated part of the financial system as a second-best substitute.



51. Over the past several weeks there has been a step-up in usage of the Federal Reserve's overnight reverse repo facility.[15] This reflects the drawdown of the Treasury's balance at the Federal Reserve together with the proceeds of the Fed's ongoing asset purchase program, both of which have injected liquidity into the financial system, adding to depository institutions' reserves held at the Fed. However, this increased usage of the facility also potentially more lasting trends such as an increasing desire for banks to shed deposits as they run up against regulatory constraints (notably the supplementary leverage ratio[16] and G-SIBs surcharge). As these resources migrate out of the banks and into money market funds they then enter into reverse repos with the Fed to earn a small spread. Potentially a shortage of short-dated Treasury securities is amplifying these forces. While not of an immediate concern, these trends bear watching since they could signal increasing disintermediation out of the banking system. Also, when the Federal Reserve eventually begins to raise the federal funds rate, it may require much larger overnight reverse repo operations in order to maintain the federal funds rate within the target range set by the FOMC (as an indication, during the 2014–15 period, overnight repos were broadly in the range of US$1–200 billion).

52. The housing market appears to be on a vigorous upward path which could raise financial stability concerns in the event of a reversal. The rate of increase of house prices has tripled relative to before the pandemic, spurred by falling mortgage rates, robust growth in disposable income, and shifting housing preferences, also raising concerns about housing affordability and access to the housing market. However, mortgage debt has grown by a fairly modest amount (around 5 percent y/y) and lending has been concentrated in households with high credit scores. Furthermore, even for vulnerable households that were hit hardest by the pandemic, federal and private sector efforts to temporarily defer loan payments have provided important support and has resulted in a decline of mortgage delinquencies.[17]

53. A range of FSAP recommendations have not been addressed (see Appendix 4)**.** These include: (i) ensuring each FSOC member has an explicit financial stability objective in their mandate; (ii) intensifying efforts to close data gaps, including reporting disclosures of holdings of CLOs and leveraged loans, to reinforce market discipline; (iii) finalizing the arrangements for market-wide circuit breakers and providing greater budgetary autonomy for the SEC and CFTC; and (iv) reviewing

[15] Under the facility, the Federal Reserve sells a security to an eligible counterparty and simultaneously agrees to buy back the same security at a specified price the next day. Eligible counterparties are typically larger banks, government sponsored entities and certain money market funds.

[16] The SLR affects financial institutions with more than US$250 billion in assets, requiring them to hold a minimum ratio of 3 percent of Tier 1 capital against their total leverage exposure. On April 1, 2020, the Federal Reserve announced that it would exempt U.S. banks' Treasury bond holdings and reserves held at Federal Reserve Banks from SLR calculations but this temporary exclusion expired on March 31, 2021.

[17] The Cares Act offered homeowners (whose mortgage was guaranteed by Fannie Mae, Freddie Mac, or Ginnie Mae) up to 12 months in payment deferral if they were experiencing hardship associated with COVID-19. Typically, these missed payments are capitalized and the loan's maturity is extended.

prudential requirements for non-internationally active banks (category III and IV) and ensure they continue to be consistent with the Basel framework.

54. Authorities' views. Overall, financial stability risks were seen as being at moderate levels, although vulnerabilities have been increasing as leverage and risk appetite have risen. Asset price valuations appear elevated, visible in the spreads of lower quality credit and other risk assets. The limited visibility into hedge fund leverage was also of concern. On the other hand, the prospect of widespread corporate failures has declined and household balance sheets have strengthened (although the situation of the most financially vulnerable remains of concern). Banks were viewed as well-capitalized and liquid, having weathered the COVID shock well. On the other hand, hedge fund leverage has risen and there were signs of increased risk exposures in a range of nonbank financial institutions. The market turmoil in 2020 highlighted systemic vulnerabilities in some key asset and funding markets as well as among some types of mutual funds. Ensuring these markets remain robust under stress is a key focus of the financial regulators and the Financial Stability Oversight Council. The lessons from the 2020 experience are now being studied carefully.

D. Gaining From Trade

55. The administration has underscored the need for a "worker-centric" trade agenda that ensures that global trade benefits Americans as workers and wage-earners, not just as consumers. In pursuing these objectives, a removal of the obstacles to free trade would help support U.S. workers and create more and better U.S. jobs (particularly in light of the domestic efforts that are being proposed to increase productivity, labor supply, and the competitiveness of U.S. producers).

56. It is of significant concern, therefore, that many of the trade distortions introduced over the past four years remain in place. In particular, tariffs have been kept on imported steel and aluminum, washing machines, solar panels, as well as a range of tariffs imposed on China. The administration has also committed to prioritizing U.S. producers in public procurement, strengthening the "Buy American" requirements put in place by the previous administration. These policies should be reconsidered. The continued imposition of import tariffs, broad restrictions on imports for national security reasons, and expanded preferences for U.S. producers in procurement serve to undermine the multilateral trade and international monetary system as well as harm the U.S. economy. Trade restrictions and tariff increases should be rolled back and "Buy American" requirements should be tightly circumscribed and made consistent with the U.S. international obligations.

57. The entanglement of trade and currency issues over the last four years represents a significant risk to the multilateral trade and international monetary systems. Over the past year, the U.S. has undertaken investigations on currency-based countervailing duties for China and Vietnam and has released affirmative findings in a Section 301 investigation of Vietnam's currency practices, finding evidence of currency undervaluation that harms U.S. workers and businesses. Furthermore, there is a risk that the pending renewal of Trade Promotion Authority could require enforceable currency provisions in all new U.S. trade agreements. Treating currency undervaluation as a subsidy to be countervailed raises concerns both in the finance and trade spheres. The threat of trade penalties could potentially impinge on monetary policy decisions and discourage exchange rate flexibility, while complicating the effective dialogue that underpins economic surveillance. Furthermore, other countries might pursue a similar approach to link trade and currency, perhaps using their own standards and methodologies, with the potential for a broadening use of trade restrictions and a further increase in trade tensions. Currency-related trade responses should be avoided and enforceable provisions on currency policy should not be attached to U.S. trade agreements. Instead, the U.S. should work constructively with its trading partners to better address the underlying macro-structural distortions that are affecting external positions.

58. There is a clear need to address longstanding global trade and investment distortions in areas such as tariffs, farm subsidies, industrial subsidies, and services trade. The U.S. should work actively with international partners to strengthen the rules-based multilateral trading system and address these longstanding global trade and investment distortions. Renewed engagement at the WTO—including restoring the proper functioning of the dispute settlement system—could help facilitate progress on these topics.

59. Authorities' views. The administration is focused on ensuring a fair international trading system that promotes inclusive and sustainable growth and a rules-based international order. Trade policies should help address the global climate crisis, respect the dignity of work, and ensure that manufacturing supply chains are resilient. Trade policies and trade agreements can also be valuable tools in supporting the administration's climate objectives, combatting exploitative labor conditions and discrimination, and tackling barriers to free and fair trade. Finally, trade policies should be judged by their impact on, and consequences for, U.S. workers and communities including by ensuring they incentivize strong, enforceable labor standards in trading partners to protect workers' rights and security. Unfair practices by U.S. trading partners were standing in the way of these goals. A comprehensive review of trade tariffs and restrictions is being undertaken. Policies relating to currency practices will aim to put effective pressures on trading partners that are intervening in the foreign exchange market to gain an unfair advantage in trade. Finally, on procurement rules, the Administration is currently undertaking a review of U.S. statutory authority as a result of an executive order on strengthening "Made in America Laws", including Buy American provisions. The administration is committed to executing these provisions consistent with the U.S.'s existing international obligations. Nothing in the executive order is inconsistent with existing U.S. rights or obligations under international agreements, such as the Agreement on Global Procurement or U.S. free trade agreements.

E. A More Equitable Society

60. The U.S. has long-faced high rates of poverty (Box 11). The economic expansion prior to the pandemic had put poverty on a steadily downward trend. However, even after a decade of growth, over 38 million Americans were still living below the poverty line (after accounting for the impact of social assistance programs), many of them children, minorities and living in female-headed households.

61. The pandemic hit lower income, lower skilled workers the hardest. In March–April 2020, 11½ percent of those without a college degree lost their jobs (more than twice the rate of those with a college degree). Many of these workers were employed at in-person services and many, particularly women, were forced to drop out of the labor force to take care of young children as schools and day care closed. Food insecurity during the early months of the pandemic doubled for the population as a whole, tripling for families with children.[18] Low-income students suffered the largest learning loss, particularly younger children. Although emergency spending under the CARES Act reduced poverty at the start of the pandemic, by March 2021 the poverty rate was around 1 percent above 2019 levels (although has subsequently fallen due to the impact of spending under the American Rescue Plan). Finally, COVID-related health outcomes have been worse for the poorest households (with higher infection and death rates).

62. The pandemic further increased wealth inequality. Over the past 30 years, median household net worth has fallen in real terms for the bottom 40 percent of the income distribution. Over the same period, the median net worth of the top decile of the income distribution has more than doubled. In addition, the real net worth of the median household was lower in 2019 than it was in 2001. These wealth inequalities grew further over the past year as asset prices accelerated upwards.

63. There have been long-standing racial disparities in economic and social outcomes in the U.S. (Figure 3) These striking differences in outcomes are related to a range of deep-rooted factors. Data suggests that minority households continue to be more likely to live in poorer neighborhoods, send their children to under-resourced school, lack basic health care coverage, face lower socio-economic mobility, be more impacted by climate change, and be victims of violent crime.

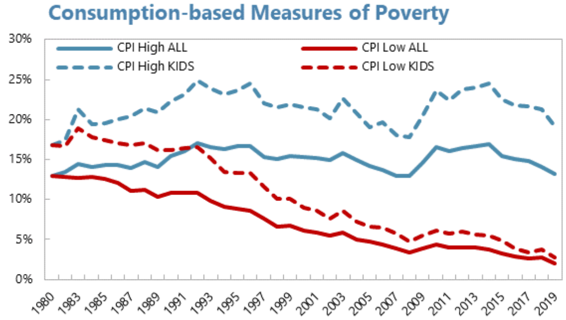
[18] See D. Schanzenbach, and A. Pitts, "How Much has Food Insecurity Risen?" Institute for Policy Research.

Box 11. The Complexity of Measuring Poverty in the U.S.

The U.S. official poverty measure compares a family's income to a poverty threshold that is based on a multiple of the cost of a specific food basket. More recent studies have argued that consumption-based measures of poverty—that draw on household expenditure surveys and attach a consumption equivalent to the value of government assistance—provide a more accurate picture of poverty.[1] Consumption based measures are able to (i) capture non-cash benefits; (ii) account for savings; and (iii) be more accurate (since consumption outcomes are typically better-measured for lower income households than is income).

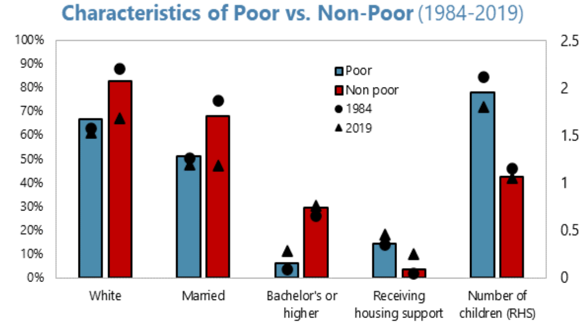
For consumption-based measures, the choice of price index has an important implication for the level of poverty.[2] The sensitivity of poverty measures to price index creates significant uncertainty about how poverty evolves over time. Work by Meyer-Sullivan suggest that poverty thresholds should be indexed at a rate that is lower than CPI which, if accurate, would imply a significant reduction in poverty over time. On the other hand, recent studies have found evidence that those at the lower end of the income distribution face higher, not lower, inflation than is measured by the CPI (the bottom quintile facing around 0.4 percentage points higher inflation than that the top quintile).[3] Relying on a price index that is linked to the consumption pattens of the bottom quintile would mean that the share of the population living in poverty has not fallen materially since 1980.

Consumption-based Measures of Poverty



Notes: Consumption measure excludes education/health as in Meyer and Sullivan (2012). CPI High adjusts CPI U upwards by 0.4 while CPI Low adjusts it downwards by 0.8 (the latter as in Meyer and Sullivan, 2012).
Sources: CE Survey; BLS; IMF Staff calculations.

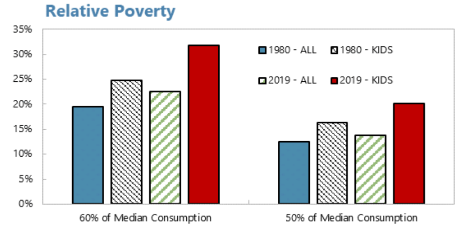
Characteristics of Poor vs. Non-Poor (1984-2019)



Notes: Consumption measure excludes education/health as in Meyer and Sullivan (2012). Bar height represents average values for 1984-2019 time period.
Sources: CE Survey; BLS; IMF Staff calculations.

Other metrics point to a more pessimistic interpretation of the progress that has been made in reducing U.S. poverty over time. For example, food insecurity does not appear to have declined over the last 20 years. Also, relative consumption-based poverty measures—such as the share of the population consuming less than 50 or 60 percent of median household consumption— have been rising over time.

Relative Poverty



Notes: Consumption measure excludes education/health as in Meyer and Sullivan (2012).
Sources: CE Survey; BLS; IMF Staff calculations.

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[1] B. D Meyer and J.X. Sullivan, 2012, "Winning the War: Poverty from the Great Society to the Great Recession" Brookings Papers.

[2] E. R. Berndt, 2006, "The Boskin Commission Report after a Decade: After-life or Requiem?" International Productivity Monitor 12: 61–73

[3] X. Jaravel, 2019, "The Unequal Gains from Product Innovations: Evidence from the U.S. Retail Sector", Quarterly Journal of Economics, 134: 715-83.

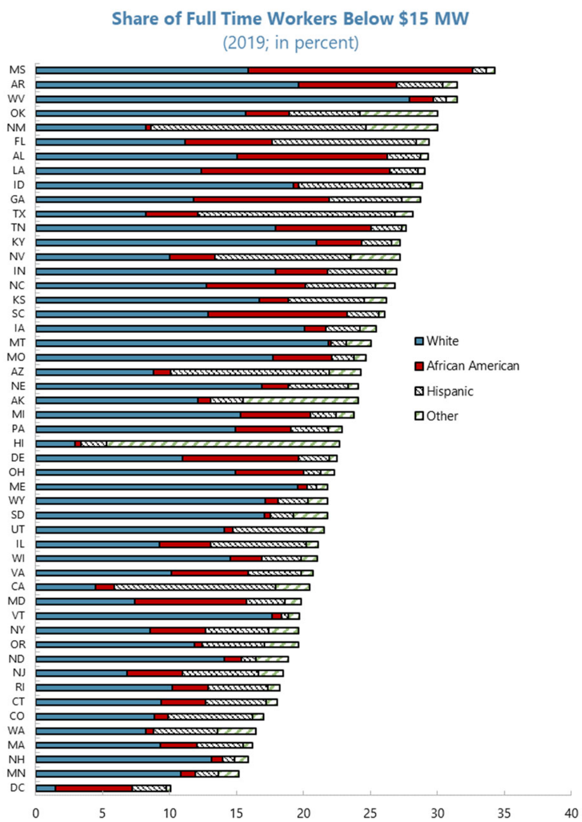
64. The administration has indicated it intends to increase support for those communities that have been historically underserved, marginalized, or adversely affected by persistent poverty. This has been visible in multiple areas. Proposed policy changes aim to increase the progressivity of the tax system and expand spending in areas (like education, childcare, food assistance, and healthcare) that are most incident on those at the bottom of the income distribution. All in all, if realized, these plans would increase the amount of redistribution taking place through federal taxes and transfers. Furthermore, the American Jobs Plan aims to provide 40 percent of the benefits from climate and clean infrastructure projects to disadvantaged communities as well as invest in affordable transportation options for low income families. Finally, the administration has proposed an increase in the federal minimum wage to US$15 per hour (although prospects for legislating such a change are uncertain).

65. Many of the authorities' proposed policies to mitigate poverty and increase social mobility have been advocated for in past consultations. The U.S. has important scope to strengthen its social safety nets and increase the progressivity of its tax system (particularly by closing loopholes that allow high net worth individuals to avoid taxes on labor income, capital income, and inter-generational transfers). Greater attention could be paid to simplifying the multitude of federal, state and local programs to aid the poor and to redesign social programs to remove "cliffs" (i.e., where programs phase-out abruptly as household income rises). To help ensure the benefits of federal tax credits and other assistance are incident on the working poor, there is scope to raise the federal minimum wage.

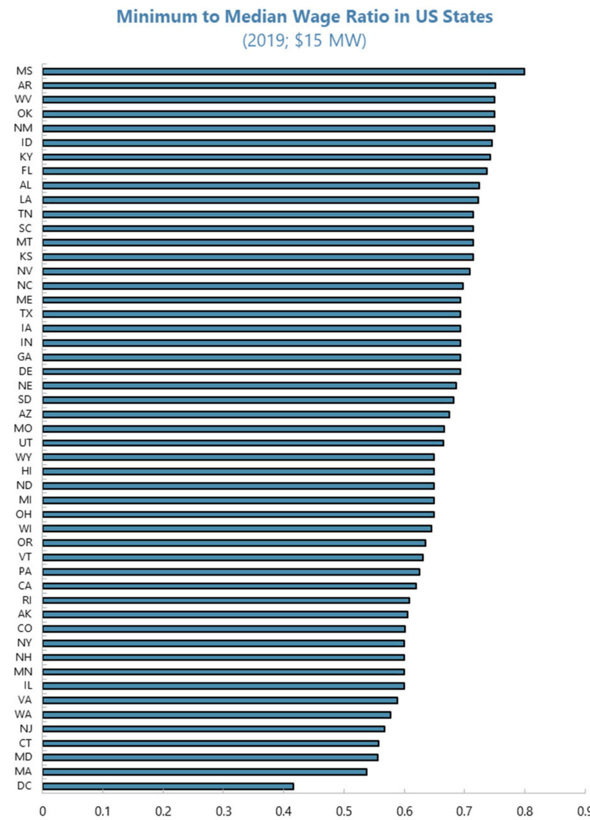
66. Authorities' views. The U.S. faces a series of structural challenges that have resulted in families at the bottom end of the wage distribution seeing their pay stagnate amidst a persistence in gender and racial pay gaps. Minority households continue to have wealth levels that are only a fraction of that held by the average white family. The American Jobs and Families Plan would begin the process of repairing the fractured foundations of the U.S. economy. Although directing a sizable share of the resources in these programs to historically underserved communities will represent an operational challenge, there was a strong commitment, across a range of agencies, to achieve the "Justice40" goal of delivering 40 percent of the benefits of federal investments to disadvantaged communities. Finally, a US$15 minimum wage would be a powerful tool to raise incomes, reduce poverty and restore social equity. Empirical evidence suggests that the employment effects of setting the minimum wage at such a level would be small.

Figure 2. The Potential Coverage of a US$15 Minimum Wage in the U.S.

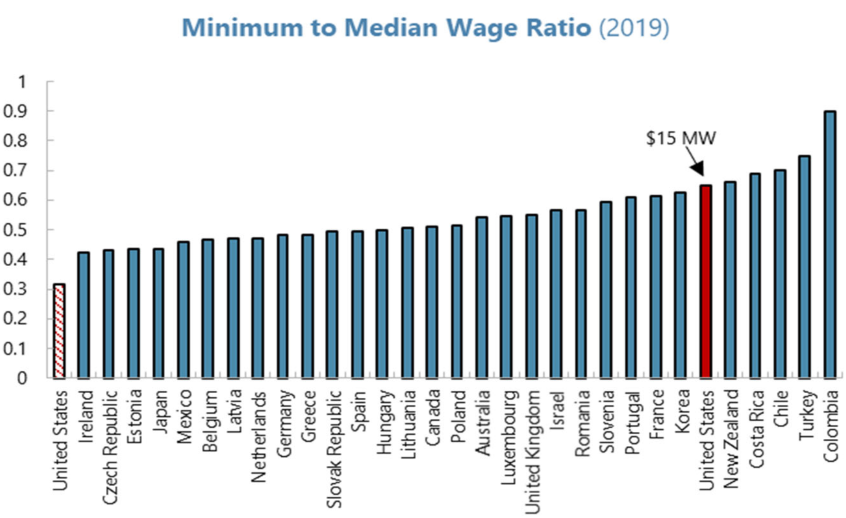
A US$15 minimum wage would be binding for a significant share of the labor force in certain states, particularly for minority workers



In some states, a US$15 would constitute a sizable fraction of the median wage



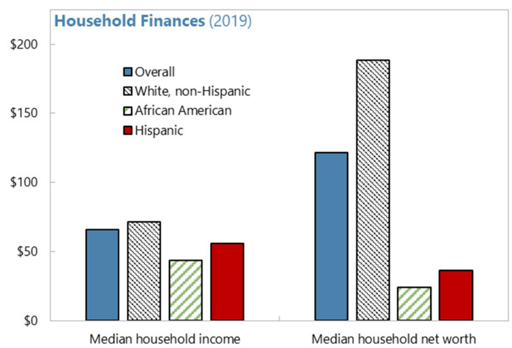
From an international perspective, a US$15 minimum wage would move the U.S. from having one of the lowest minimum wages (as a share of the median wage) to one of the highest among OECD countries.



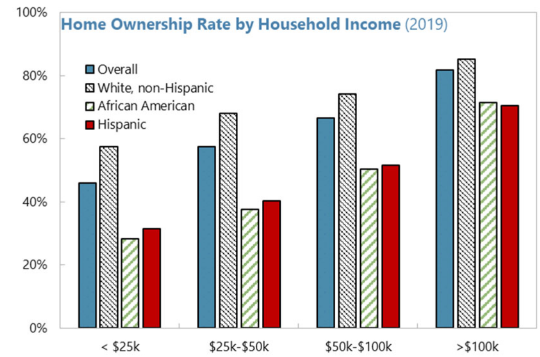
Notes: Sample includes full time wage and salary workers only, excludes the self-employed, ages 16+.
Sources: CPS ORG; EPI; OECD; IMF Staff calculations.

Figure 3. Racial Disparities in Economic Outcomes in the U.S.

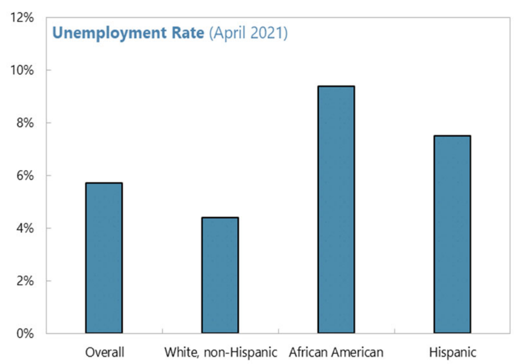
Income and wealth are substantially lower for black and Hispanic households.



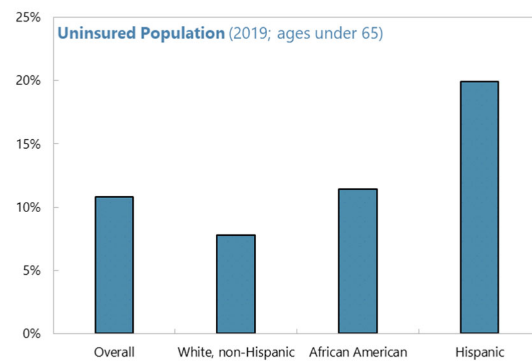
Minorities have lower rates of home ownership, even at relatively high levels of income.



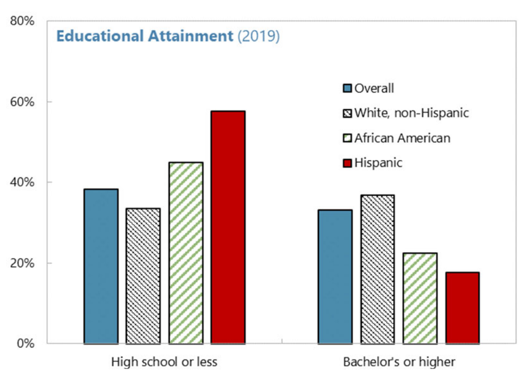
The unemployment rate has been structurally higher for black and Hispanics populations.



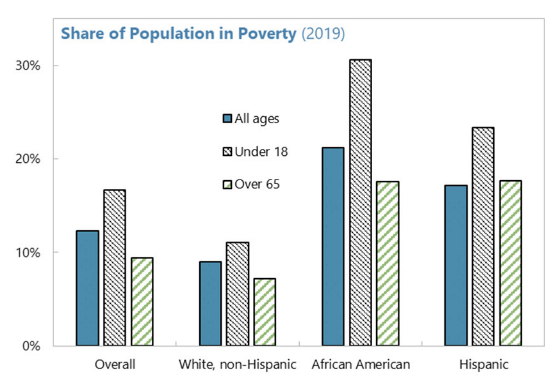
And many minority households lack health insurance.



Educational opportunities and social mobility differ greatly by race.



And African Americans and Hispanics are far more likely to live in poverty.



Sources: U.S. Census Bureau (CPS, ACS); Federal Reserve Survey of Consumer Finances; BLS.

GOVERNANCE AND TRANSPARENCY

67. The United States has further increased its strong enforcement of the U.S. Foreign Corrupt Practices Act (FCPA), maintaining its prominent role in the fight against transnational corruption.[19] The 2020 Phase 4 Report of the OECD Working Group on Bribery in International Business Transactions (WGB) [20] recognized that, from the Phase 3 Report in 2010 up to July 2019, 115 individuals and 174 legal persons have been convicted or sanctioned for foreign bribery and related offences in the United States. This achievement results from a combination of enhanced expertise and resources to investigate and prosecute foreign bribery, the enforcement of a broad range of offences in foreign bribery cases, the effective use of non-trial resolution mechanisms, and the development of published policies to incentivize companies' cooperation with law enforcement agencies. The report identified a large number of good practices and positive achievements, including that the U.S. enforcement authorities have made broad use of other statutes and offences to prosecute payments to foreign government officials and intermediaries either in addition to or instead of FCPA charges. They have also increasingly addressed the demand side of bribery by charging foreign public officials or their associates with money laundering or other offences when they use U.S. financial institutions or otherwise fall under U.S. jurisdiction. The U.S. authorities' concerted efforts to build working relationships and to help build capacity with foreign partners has enabled the law enforcement authorities to better investigate and sanction prominent foreign bribery cases with effective, proportionate, and dissuasive sanctions, while also providing legal certainty to the companies involved. The United States has become a driving force in coordinating and cooperating in investigating and resolving multijurisdictional foreign bribery matters. The Dodd-Frank Act's multi-faceted protections, most notably the SEC's ability to enforce the anti-retaliation provisions, constitute a good practice given that they provide powerful incentives for qualified whistleblowers to report foreign bribery allegations against issuers. Additionally, while small facilitations payments remain legal under the FCPA, U.S. authorities and companies have taken significant steps to raise awareness of the risks associated with this practice.

68. The WGB recommends further strengthening of the U.S. efforts against foreign bribery. Among other recommendations, the WGB found that the United States should consider enhancing protections for whistleblowers who report suspected acts of foreign bribery by non-issuers, continue to evaluate the effectiveness of the Corporate Enforcement Policy and to consider consolidating other FCPA enforcement policy and guidance, continue its efforts to enhance

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[19] In line with the Framework for Enhanced Engagement on Governance, this section provides an update of the OECD's peer review of the United States framework to assess the implementation and enforcement of the Convention on Combating Bribery of Foreign Public Officials in International Business Transactions ("supply side of corruption"). An update on preventing the concealment of the proceeds of corruption will be reported in 2022, which will include coverage of the recently enacted Corporate Transparency Act which sets up a government-maintained registry of beneficial owners for certain U.S. companies.

[20] Information relating to supply-side corruption in this section of the Report draws on the WGB's Phase 4 Report of the United States (2020). The IMF and the United States may have provided additional views and information whose accuracy have not been verified by the WGB or the OECD Secretariat, and which do not prejudice the WGB's monitoring of the implementation of the OECD Anti-Bribery Convention.

transparency regarding the use of Non-Prosecution and Deferred Prosecution Agreements, and apply appropriate AML/CFT obligations to lawyers, accountants, and trust and company service providers related to foreign bribery. Fund staff agrees with these recommendations and urges the authorities to move forward in implementing them.

STAFF APPRAISAL

69. A remarkable recovery. The new administration's policies have put the U.S. economy on a strong footing. An effective vaccine rollout has put the number of new COVID-19 cases on a firmly downward path. At the same time, unprecedented fiscal support is quickly restoring the economy back to full employment and generating positive outward spillovers to the world economy. These efforts have not been costless: the path for public debt is far higher; the current account imbalance has grown; and very accommodative financial conditions have led to increased corporate and nonbank leverage and rising valuations across a range of assets. The pandemic continues to weigh heavily on those at the lower end of the income distribution, exposing longstanding inequities in access to quality healthcare and education (many of which have an important gender and racial dimension).

70. Moving on multiple fronts. The administration's proposed policy program seeks to address a range of challenges that have long held back the U.S. economy. The pandemic is being viewed as an opportunity to remake the economy with higher productivity, increased labor force participation, and a less polarized distribution of income and wealth. To partially fund the intended increase in federal spending, plans have been developed to close tax loopholes, raise taxes on corporates and higher income households, remake the international system for corporate taxes, and fully resource the Internal Revenue Service. Finally, a renewed effort is underway to lower carbon emissions and increase resilience to climate change.

71. Potential improvements to fiscal policies. The size and ambition of the proposed fiscal packages are admirable, but a better targeting of policies would further strengthen their impact on macroeconomic and distributional outcomes. As the appropriations process moves ahead, more could be done to (i) phase out tax credits at lower levels of household income; (ii) prioritize spending toward programs that have the biggest impact on productivity, labor force participation, reducing poverty, and facilitating a shift to a low-carbon economy; and (iii) fully eliminate step-up basis, lower the threshold for paying the estate tax, eliminate the 199A passthrough deduction, and reformulate the business tax as a cashflow tax. Reorienting the administration's tax and spending proposals in this way would likely imply a slower (but more sustained) demand impulse, create a bigger boost to aggregate supply, and, in so doing, lessen the near-term risks posed by a sustained upswing in inflation. Even with improved targeting, additional steps will be needed over the medium term to bring down the public debt both by raising revenues (through a carbon tax, higher taxation of fuels, and a broad-based federal consumption tax) as well as lessening the impact of an aging demographic on future spending. Also, there are important uncertainties surrounding the final size and composition of these proposals, given the need to build political consensus around them.

72. A tricky task for monetary policy. The Federal Reserve's actions have been highly effective both in the depths of the crisis and in supporting the recovery. While there were risks to introducing the new monetary framework in the midst of COVID-related uncertainty, the low neutral rate of interest and the asymmetries posed by the effective lower bound called for a new approach to policy. The Federal Reserve's new policy framework has helped support a more rapid recovery from the pandemic and rightly commits to a near-term overshooting of the 2 percent longer-run inflation goal (in line with past IMF advice). From a conjunctural perspective, the framework helpfully defers the timing of policy normalization—increasing monetary support as the economy recovers from the COVID-19 shock—while providing clarity on how the Fed intends to achieve its statutory mandate of maximum employment and price stability. In the coming months, the ongoing rapid pace of recovery and expectations of additional fiscal support will necessitate a shift in monetary policy. Managing this transition—from providing reassurance that monetary policy will continue to deliver powerful support to the economy to preparing for an eventual scaling back of asset purchases and a withdrawal of monetary accommodation—will require deft communications, under a potentially tight timeline, to avoid market misunderstandings, volatility in market pricing, and/or an unwarranted tightening in financial conditions.

73. Safeguarding financial stability. The unfolding pandemic revealed important shortcomings in the functioning-under-stress of systemically important U.S. markets and institutions. Serious consideration should be given to structural changes in the operation of the Treasury market, key money markets, and prime money market funds. Systemic financial stability risks appear close to the historical average but the very accommodative financial conditions are encouraging continued risk taking, fueling asset valuations and facilitating rising leverage in the nonbanks and corporates that should be followed carefully.

74. External sector. The pandemic has resulted in a larger current account deficit and left the U.S. external position moderately weaker than the level implied by medium-term fundamentals and desirable policies. The current account deficit is likely to grow further in 2021. Trade restrictions and tariff increases should be rolled back. Doing so, would help support U.S. workers and create more and better American jobs (particularly in light of the domestic efforts that are being proposed to increase productivity, labor supply, and the competitiveness of U.S. producers). "Buy American" provisions should be tightly circumscribed and made consistent with the U.S. international obligations. Currency related trade responses should be avoided. Instead, the U.S. should work constructively with its trading partners to better address the underlying macro-structural distortions that are affecting external positions and to strengthen the rules-based multilateral trading system. Renewed engagement at the World Trade Organization—including restoring the proper functioning of the dispute settlement system—could help facilitate progress on these topics.

75. Looking forward. As the pandemic effects recede, policymakers will have to cope with simultaneous, ongoing transitions. These arise from an uncertain reshaping of the post-pandemic economy (both in the U.S. and abroad), a transition to a lower carbon economic model, an increasing role for digitalization and technology, and an underlying shift in U.S. demographics toward an older and more diverse population. The flexibility and innovativeness of the U.S. system puts it in a good place to manage these transitions. However, great care should be taken to ensure that these multi-faceted changes do not increase income polarization, further hollow out the middle class, and leave behind a material share of the population (particularly lower-skilled, lower-income workers). It would be a mistake to assume the social and economic impact of these deep-rooted transitions can simply be left to market forces and the hope that a vibrant U.S. economy will lift all boats. Instead, a multi-dimensional policy approach will need to be developed to support rising living standards for all Americans and prevent workers from becoming disenfranchised or detached from the labor force.

76. It is recommended that the next Article IV consultation take place on the standard 12-month cycle.

Table 1. United States: Selected Economic Indicators
(Percentage change from previous period, unless otherwise indicated)

			Projections					
	2019	2020	2021	2022	2023	2024	2025	2026
National production and income								
Real GDP	2.2	-3.5	7.0	4.9	1.9	1.7	1.7	1.7
Real GDP (q4/q4)	2.3	-2.4	8.0	2.8	1.8	1.7	1.7	1.7
Net exports 1/	-0.2	-0.2	-1.6	-0.7	0.0	0.1	0.1	0.0
Total domestic demand	2.3	-3.3	8.5	5.4	1.9	1.5	1.6	1.6
Final domestic demand	2.3	-2.7	8.2	5.1	1.9	1.5	1.6	1.6
Private final consumption	2.4	-3.9	8.1	4.7	1.4	1.6	1.8	2.1
Public consumption expenditure	1.8	0.3	5.7	3.5	1.8	1.1	1.1	1.1
Gross fixed domestic investment	2.3	-0.8	10.0	7.7	3.6	1.8	1.0	0.4
Private fixed investment	1.9	-1.8	11.1	5.5	3.3	2.6	2.4	2.2
Public fixed investment	4.3	4.3	4.7	18.2	5.0	-1.7	-5.0	-7.8
Change in private inventories 1/	0.0	-0.6	0.2	0.2	0.0	0.0	0.0	0.0
Nominal GDP	4.0	-2.3	10.6	7.9	4.3	4.0	3.9	3.8
Personal saving rate (% of disposable income)	7.6	16.2	15.6	8.9	8.7	9.4	9.7	8.7
Private investment rate (% of GDP)	17.5	17.2	17.9	17.9	18.0	18.0	17.9	17.9
Unemployment and potential output								
Unemployment rate	3.7	8.1	5.5	3.5	3.0	3.0	3.1	3.3
Labor force participation rate	63.1	61.7	62.0	63.0	63.2	63.2	63.1	63.0
Potential GDP	1.6	0.6	2.5	3.1	2.1	2.1	2.2	2.2
Output gap (% of potential GDP)	1.0	-3.1	1.1	3.0	2.9	2.4	1.9	1.4
Inflation								
CPI inflation (q4/q4)	2.0	1.2	4.8	2.6	2.7	2.6	2.5	2.3
Core CPI Inflation (q4/q4)	2.3	1.6	3.9	2.6	2.9	2.8	2.6	2.4
PCE Inflation (q4/q4)	1.5	1.2	4.3	2.4	2.4	2.3	2.2	2.0
Core PCE Inflation (q4/q4)	1.6	1.4	3.7	2.4	2.6	2.5	2.3	2.1
GDP deflator	1.8	1.2	3.4	2.8	2.3	2.2	2.2	2.1
Government finances								
Federal balance (% of GDP) 2/	-4.6	-14.9	-15.1	-8.0	-5.7	-4.9	-4.7	-4.5
Federal debt held by the public (% of GDP)	79.2	100.1	104.9	103.7	105.1	106.0	106.8	107.4
General government budget balance (% of GDP) 2/	-5.7	-14.7	-13.3	-7.4	-5.7	-5.4	-5.3	-5.2
General government gross debt (% of GDP)	108.2	133.6	134.5	132.6	133.3	134.1	134.9	135.6
Interest rates (percent; period average)								
Fed funds rate	2.2	0.4	0.1	0.1	0.5	1.1	1.8	2.3
Three-month Treasury bill rate	2.1	0.4	0.1	0.1	0.5	1.1	1.8	2.2
Ten-year government bond rate	2.1	0.9	1.7	2.2	2.7	2.8	2.8	2.7
Balance of payments								
Current account balance (% of GDP)	-2.2	-2.9	-3.7	-3.7	-3.4	-3.0	-2.7	-2.5
Merchandise trade balance (% of GDP)	-4.0	-4.4	-5.1	-5.3	-5.1	-4.9	-4.7	-4.5
Export volume (NIPA basis, goods)	-0.1	-9.5	7.5	5.3	4.0	2.5	2.2	2.2
Import volume (NIPA basis, goods)	0.5	-6.0	18.3	9.1	3.3	1.3	1.3	1.6
Net international investment position (% of GDP)	-51.6	-67.3	-64.5	-63.5	-64.2	-64.8	-65.1	-65.3
Saving and investment (% of GDP)								
Gross national saving	18.6	17.8	17.4	17.9	18.4	18.6	18.6	18.4
General government	-3.1	-13.1	-10.0	-4.7	-2.7	-2.3	-2.3	-2.6
Private	21.7	30.9	27.4	22.6	21.0	20.9	20.8	21.0
Personal	5.7	13.7	11.7	6.9	6.7	7.3	7.6	6.7
Business	16.0	17.1	15.7	15.7	14.3	13.5	13.3	14.3
Gross domestic investment	21.0	21.0	21.5	22.0	22.2	22.0	21.7	21.3
Private	17.5	17.2	17.9	17.9	18.0	18.0	17.9	17.9
Public	3.5	3.8	3.7	4.1	4.2	4.0	3.8	3.4

Sources: BEA; BLS; FRB; Haver Analytics; and IMF staff estimates.
1/ Contribution to real GDP growth, percentage points.
2/ Includes staff's adjustments for one-off items, including costs of financial sector support.

Table 2. United States: Balance of Payments
(Annual percent change unless otherwise indicated)

			Projections					
	2019	2020	2021	2022	2023	2024	2025	2026
Real exports growth								
Goods and services	-0.1	-12.9	4.9	7.1	5.2	3.8	3.4	3.3
Goods	-0.1	-9.5	7.5	5.3	4.0	2.5	2.2	2.2
Services	-0.1	-19.2	0.0	11.4	7.8	6.4	5.8	5.6
Real imports growth								
Goods and services	1.1	-9.3	16.1	9.5	4.0	2.2	1.9	2.3
Goods	0.5	-6.0	18.3	9.1	3.3	1.3	1.3	1.6
Nonpetroleum goods	1.2	-5.7	19.5	10.1	3.7	1.6	1.5	1.9
Petroleum goods	-6.4	-13.1	-0.2	-3.2	-3.2	-3.2	-3.2	-3.2
Services	3.7	-22.5	5.5	11.8	7.9	6.8	5.4	5.5
Net exports (contribution to real GDP growth)	-0.2	-0.2	-1.6	-0.7	0.0	0.1	0.1	0.0
Nominal exports								
Goods and services	11.7	10.2	10.7	11.1	11.5	11.8	12.0	12.2
Nominal imports								
Goods and services	14.6	13.2	14.8	15.3	15.4	15.4	15.3	15.3
Current account								
Current account balance	-2.2	-2.9	-3.7	-3.7	-3.4	-3.0	-2.7	-2.5
Balance on trade in goods and services	-2.7	-3.2	-4.1	-4.1	-3.8	-3.5	-3.2	-3.0
Balance on income	0.5	0.3	0.4	0.4	0.5	0.5	0.5	0.5
Capital and Financial Account								
Capital account balance	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account balance	-2.2	-3.1	-3.6	-3.7	-3.4	-3.0	-2.7	-2.5
Direct investment, net	-0.8	0.5	-0.3	-0.4	-0.4	-0.4	-0.4	-0.4
Portfolio investment, net	-0.9	-2.3	-1.2	-1.5	-1.5	-1.1	-0.7	-0.7
Financial derivatives, net	-0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other investment, net	-0.3	-1.3	-2.0	-1.7	-1.4	-1.4	-1.5	-1.3
Reserve assets, net	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Errors and Omissions	0.0	-0.1	0.1	0.0	0.0	0.0	0.0	0.0
Net International Investment Position	-51.6	-67.3	-64.5	-63.5	-64.2	-64.8	-65.1	-65.3
Direct investment, net	-8.2	-12.8	-11.9	-11.5	-11.4	-11.4	-11.4	-11.4
Portfolio investment, net	-37.4	-47.7	-44.6	-42.9	-42.7	-42.2	-41.4	-40.7
Financial derivatives, net	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Other investment, net	-8.5	-9.8	-10.8	-11.7	-12.6	-13.5	-14.6	-15.4
Reserve assets, net	2.4	3.0	2.7	2.5	2.4	2.3	2.2	2.1
Memorandum items								
Current account balance (US$ billions)	-472	-616	-849	-920	-881	-822	-770	-737
Non-oil trade balance (% of GDP)	-2.7	-3.1	-4.0	-4.1	-3.9	-3.6	-3.4	-3.2
Foreign real GDP growth	1.7	-5.2	5.2	4.2	2.8	2.4	2.3	2.3
U.S. real GDP growth	2.2	-3.5	7.0	4.9	1.9	1.7	1.7	1.7
U.S. real total domestic demand growth	2.3	-3.3	8.5	5.4	1.9	1.5	1.6	1.6

Sources: BEA; FRB; Haver Analytics; and IMF staff estimates.

Table 3. United States: Federal and General Government Finances
(Percent of GDP)

			Projections										
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
Federal government													
Revenue	16.3	16.3	15.7	18.0	18.5	18.4	18.2	18.7	19.0	18.8	18.7	18.6	18.6
Expenditure	21.0	31.2	30.8	26.0	24.2	23.3	22.9	23.2	23.2	23.2	22.5	23.0	23.2
Non-interest	19.2	29.6	29.4	24.7	22.8	21.6	21.0	21.1	20.8	20.5	19.8	20.1	20.3
Interest	1.8	1.6	1.4	1.3	1.4	1.6	1.8	2.1	2.4	2.7	2.8	2.8	2.9
Budget balance 1/	-4.6	-14.9	-15.1	-8.0	-5.7	-4.9	-4.7	-4.5	-4.2	-4.3	-3.8	-4.3	-4.6
Primary balance 2/	-2.9	-13.3	-13.7	-6.7	-4.3	-3.3	-2.8	-2.4	-1.8	-1.7	-1.0	-1.5	-1.7
Primary structural balance 3/ 4/	-3.0	-10.4	-11.2	-7.5	-5.0	-3.9	-3.3	-2.8	-2.1	-1.9	-1.3	-1.7	-1.8
Change	-0.8	-7.4	-0.8	3.7	2.4	1.2	0.6	0.5	0.7	0.2	0.7	-0.4	-0.1
Federal debt held by the public	79.2	100.1	104.9	103.7	105.1	106.0	106.8	107.4	107.7	108.2	108.1	108.5	109.2
General government													
Revenue	30.0	30.5	29.7	31.8	32.2	32.0	32.0	32.5	32.7	32.6	32.5	32.5	32.5
Expenditure	35.7	45.2	43.0	39.2	37.9	37.4	37.3	37.7	37.9	37.8	37.5	37.9	37.7
Net interest	2.3	2.2	1.5	1.3	1.4	1.6	1.9	2.3	2.6	2.9	3.0	3.1	3.2
Net lending 1/	-5.7	-14.7	-13.3	-7.4	-5.7	-5.4	-5.3	-5.2	-5.1	-5.2	-4.9	-5.4	-5.2
Primary balance 2/	-3.4	-12.6	-11.8	-6.1	-4.3	-3.8	-3.4	-2.9	-2.5	-2.3	-2.0	-2.4	-2.0
Primary structural balance 3/ 4/	-3.9	-8.6	-9.7	-7.3	-5.6	-4.8	-4.2	-3.5	-3.0	-2.7	-2.3	-2.6	-1.5
Change	-0.7	-4.7	-1.1	2.4	1.8	0.8	0.6	0.7	0.6	0.3	0.4	-0.3	1.2
Gross debt	108.2	133.6	134.5	132.6	133.3	134.1	134.9	135.6	136.2	136.9	137.3	138.2	138.8
incl. unfunded pension liab.	135.1	160.4	160.8	158.5	158.8	159.2	159.6	159.9	160.1	160.4	160.4	160.9	161.2

Sources: Congressional Budget Office; Office of Management and Budget; and IMF staff estimates.

Note: Fiscal projections are based on Congressional Budget Office forecast adjusted for the IMF staff's policy and macroeconomic assumptions. Projections incorporate the effects of enacted legislation at the time of the publication of this table and also potential legislation to be passed under the American Jobs Plan and the American Families Plan. Fiscal projections are adjusted to reflect the IMF staff's forecasts for key macroeconomic and financial variables and different accounting treatment of financial sector support and of defined-benefit pension plans and are converted to a general government basis. Data are compiled using SNA 2008, and when translated into GFS this is in accordance with GFSM 2014.

1/ Includes staff's adjustments for one-off items, including costs of financial sector support.

2/ Excludes net interest.

3/ Excludes net interest, effects of economic cycle, and costs of financial sector support.

4/ Percent of potential GDP.

Table 4. United States: Core Financial Soundness Indicators for Deposit Takers
(Percent unless stated otherwise, eop)

	2012	2013	2014	2015	2016	2017	2018	2019	2020
Regulatory capital to risk-weighted assets	14.5	14.4	14.4	14.1	14.2	14.5	14.8	14.7	16.3
Regulatory tier 1 capital to risk-weighted assets	12.7	12.8	13.1	13.1	13.2	13.5	13.8	13.7	14.5
Non-performing loans net of provisions to capital	15.7	11.7	8.8	7.2	6.6	5.7	4.7	4.3	5.2
Non-performing loans to total gross loans	3.3	2.5	1.9	1.5	1.3	1.1	0.9	0.9	1.1
Sectoral distribution of total loans: residents	95.5	95.2	95.6	95.8	96.1	96.0	96.3	96.3	96.7
Sectoral distribution of total loans: deposit-takers	6.0	5.0	4.1	3.6	3.8	3.9	5.5	4.6	6.1
Sectoral distribution of total loans: other financial corporations	4.4	5.2	6.2	6.7	6.7	6.9	7.3	7.8	8.5
Sectoral distribution of total loans: general government	1.1	1.2	1.3	1.4	1.5	1.6	1.5	1.4	1.4
Sectoral distribution of total loans: nonfinancial corporations	32.1	33.3	34.2	35.0	35.5	35.4	35.3	35.4	36.4
Sectoral distribution of total loans: other domestic sectors	51.9	50.5	49.8	49.1	48.5	48.2	46.7	47.1	44.2
Sectoral distribution of total loans: nonresidents	4.5	4.8	4.4	4.2	3.9	4.0	3.7	3.7	3.3
Return on assets	0.3	0.4	0.3	0.4	0.4	0.3	0.4	0.3	0.3
Return on equity	2.7	3.3	2.8	3.0	3.2	2.9	3.4	2.9	3.0
Interest margin to gross income	60.8	63.5	63.7	63.4	65.1	67.0	68.3	66.9	64.3
Non-interest expenses to gross income	63.6	61.7	64.7	60.7	59.6	61.6	58.4	60.4	62.7
Liquid assets to total assets (liquid asset ratio)	13.4	14.5	14.5	13.2	12.8	13.2	12.7	11.8	17.7
Liquid assets to short term liabilities	74.1	88.3	90.0	91.2	98.2	97.7	89.3	84.3	183.6

Source: Haver Analytics.

Appendix I. Risk Assessment Matrix

Risk	Likelihood	Expected Impact if Risk Materializes	Policy Response and Recommendations
Global Risks			
Global resurgence of the COVID-19 pandemic. Local outbreaks lead to a global resurgence of the pandemic (possibly due to vaccine-resistant variants), which requires costly containment efforts and prompts persistent behavioral changes rendering many activities unviable.	**Medium**	**High** Renewed economic disruptions and high unemployment results in subdued consumption and longer-term damage to participation and human capital. Financial institutions' losses impair the availability of credit, with further adverse implications for growth.	Fiscal policy should support the public health response, minimize undue balance sheet dislocations, preserving employer-employee relationships, and support household income. Monetary policy should remain accommodative and support loose financial conditions (including through asset purchases, forward guidance, and the reinstatement of emergency credit facilities).
Disorderly transformations. COVID-19 triggers structural transformations, but the reallocation of resources is impeded by labor market rigidities, debt overhangs, and inadequate bankruptcy resolution frameworks. This, coupled with a withdrawal of COVID-19-related policy support, undermines growth prospects and increases unemployment, with adverse social/political consequences. Adjustments in global value chains and reshoring (partly driven by geostrategic and national security concerns) shift production activities across countries.	**Medium**	**High** Multi-faceted changes to the economy lead to increased income polarization, a further hollowing out the middle class, and leaves behind a material share of the population (particularly lower-skilled, lower-income workers).	The longstanding flexibility and innovativeness of the U.S. system puts it in a good place to manage these transitions. Proposed investments in social safety nets, healthcare, vocational and academic education, infrastructure can help. Could also consider regional development initiatives, subsidies to labor mobility, and immigration policies to meet skills needs.
Widespread social discontent and political instability. Social tensions erupt as a withdrawal of pandemic-related policy support results in unemployment and, amid increasing prices of essentials, hurts vulnerable groups (often exacerbating pre-existing inequities).	**High**	**Medium** Political instability complicates reaching consensus on policies to address the pandemic and achieve economic recovery. Perceptions of social and racial injustice are exacerbated. Public protests feed into COVID infection rates.	Policies to improve the social safety net, support the unemployed, increase resources to healthcare providers, increase health preparedness, and ensure broad access to affordable, quality health care.
Rising commodity prices amid bouts of volatility. Commodity prices increase by more than expected against a weaker U.S. dollar, post-pandemic pent-up demand and supply disruptions, and for some materials, accelerated plans for renewable energy adoption. Uncertainty surrounding each of these factors leads to bouts of volatility, especially in oil prices.	**Medium**	**Medium** Higher commodity prices reduce corporate profit margins, increase household financial stress (particularly for lower income groups), and raise inflation expectations.	Fiscal measures promote green alternatives to fossil fuels. Monetary policy responds assertively to any de-anchoring of inflation expectations.
Cyber-attacks. Cyber-attacks on critical infrastructure, institutions, and financial systems trigger systemic financial instability	**Medium**	**Medium** Disruption is widespread including to supply of	Public and private sectors coordinate their investments in

or widespread disruptions in socio-economic activities and remote work arrangements.		essential goods, payments systems, and financial market infrastructure.	cyber-security measures. Contingency plans developed.
		Domestic Risks	
Supply and demand mismatches. Supply chains disrupted by the pandemic are unable to respond to rapidly returning demand. Labor supply is inelastic due to health concerns, lack of adequate child-care and availability of unemployment insurance.	**Medium**	**High** Wage rises become broad-based. Transitory relative price movements feed into sustained inflation and a de-anchoring of inflation expectations.	Fiscal measures could be designed to incentivize a return to the labor market. Monetary policy looks through higher realized inflation and focus on signs of de-anchoring.
De-anchoring of inflation expectations in the U.S. leads to rising core yields and risk premia. A fast recovery in demand (supported by excess private savings and stimulus policies), combined with COVID-19-related supply constraints, leads to sustained above-target inflation readings and a de-anchoring of expectations. The Fed reacts by signaling a need to tighten earlier than expected. The resulting repositioning by market participants leads to a front-loaded tightening of financial conditions and higher risk premia.	**Medium**	**High** High realized wage and price inflation, resulting from a sustained mismatch in supply and demand, proves persistent and causes a de-anchoring of inflation expectations.	A de-anchoring of expectations would necessitate accelerating the reduction in asset purchases and even having to consider raising policy rates before net purchases have been brought to zero.
Rising vulnerabilities in the U.S. corporate sector. The rising share of risky debt—leveraged loans, high yield bond and private debt—create vulnerabilities. Higher corporate leverage and the migration of risks to nonbank financial institutions result in severe financial strain.	**Medium**	**High** A shock to earnings and/or tighter financing conditions cause leveraged corporates to experience stress, increasing credit spreads, downgrades, and defaults. Weaker debt covenants increase losses when defaults materialize.	Emergency liquidity support to curtail market dysfunction. Limits on dividend distributions and buybacks to preserve capital. Macroprudential tools to address vulnerabilities in the nonbanks.
Note: The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. Conjunctural risks are especially relevant over shorter horizons (up to two years) given the current baseline. Structural risks (omitted from this streamlined version) remain salient over shorter and longer horizons (up to three years).			

Appendix II. Public Debt Sustainability Assessment

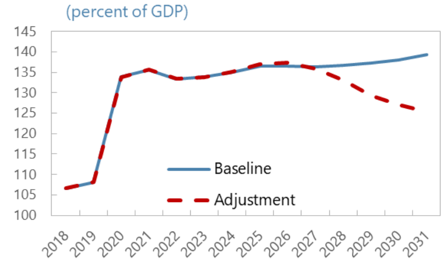
Due to the unprecedented fiscal response to the COVID-19 outbreak, the U.S. budget deficit has increased considerably in 2020 and is expected to stay elevated in 2021. Under the baseline scenario, public debt is projected to stabilize over the medium term as gradually materializing spending under the American Jobs and Families Plans is offset by the implied boost to potential growth. However, age-related spending pressures on entitlement programs will gradually push debt up over the long-run. Gross financing needs are large, albeit manageable given the global reserve currency status of the U.S. dollar. A credible medium-term fiscal adjustment featuring reprioritization of budget programs and revenue-gaining tax reform is needed to put public debt on a downward path. Nonetheless, the risks of debt distress are low and debt is viewed as sustainable[1].

1. Background. An unprecedented scale of fiscal expansion has been introduced in response to the COVID-19 pandemic. As a result, fiscal deficits are projected to stay elevated in the near term.

2. Baseline. The staff's baseline is based on current and likely to be passed laws. Under this baseline, public debt is projected to rise further in 2021 reflecting the automatic and discretionary fiscal responses to the economic downturn which are only partially offset by robust growth. Public debt is to remain elevated in the medium term and to begin rising gradually after 2027 as age-related spending pressures on entitlement programs assert themselves. Federal debt held by the public is projected to increase from about 100 percent of GDP in FY2020 to around 111 percent of GDP in 2030, with general government gross debt rising from about 134 percent of GDP to 138 percent of GDP in the same period.

3. Adjustment scenario. The general government primary deficit was 12.6 percent of GDP in 2020 and is projected at 11.8 percent of GDP in 2021. Nevertheless, gradually raising the primary general government surplus in the medium-term to around ½ percent of GDP (1 percent of GDP for the federal government) would be necessary to return the debt-to-GDP ratio to a lower path. The target primary surplus would have to be larger to bring the debt ratio closer to pre-Great Recession levels by 2030.

General government debt
(percent of GDP)



Source: IMF staff calculations.

4. Debt servicing costs. The fiscal projections benefit from the current favorable interest rate-growth differential, reflecting accommodative monetary policy and the safe-haven status of the United States. Under staff's baseline, the effective nominal interest rate is projected to rise gradually

[1] In previous consultations, debt was characterized as being "on an unsustainable upward path under current policies". The debt sustainability assessment now reflects the approach taken in the Review of the Debt Sustainability Framework for Market Access Countries whereby public debt is "regarded as sustainable when the primary balance needed to at least stabilize debt under both the baseline and realistic shock scenarios is economically and politically feasible, such that the level of debt is consistent with an acceptably low rollover risk and with preserving potential growth at a satisfactory level." This assessment is distinct from whether (or not) the debt stabilizes under policies assumed in the baseline outlook.

from the projected level of 1.6 percent in 2021 to 2.7 percent by 2030, which is close to its 2010–18 average level. Thus, real interest rates will act as a debt-reducing flow over the medium-term.

5. Realism. Baseline economic assumptions are generally within the error band observed for all countries. The baseline fiscal projections and implied near-term adjustment are outliners compared with historical and cross-country experience, but are nevertheless realistic, reflecting the large but temporary fiscal expansion in response to the pandemic.

6. Stress tests. Public debt dynamics are sensitive to growth and interest rate assumptions. An increase of 100 basis points in the sovereign risk premium would raise the public debt ratio to about 141 percent of GDP by 2030, about 3 percentage points of GDP above the baseline. Similarly, were real GDP growth to be one standard deviation below the baseline, the public debt ratio would increase by about 7 percentage points above the baseline. A scenario involving a 1 percentage point of GDP larger fiscal deficit over the next two years would increase public debt ratio by about 4 percentage points above the baseline by 2030. A combined macro-fiscal shock could raise the public debt ratio to as high as 154 percent of GDP by 2030. An exchange rate shock does not have major implications for debt sustainability in the United States given that all debt is denominated in local currency and the reserve currency status of the dollar**.**

7. Mitigating factors. The depth and liquidity of the U.S. Treasury market as well as its safe-haven status represent a mitigating factor for the high external and gross financing requirements.

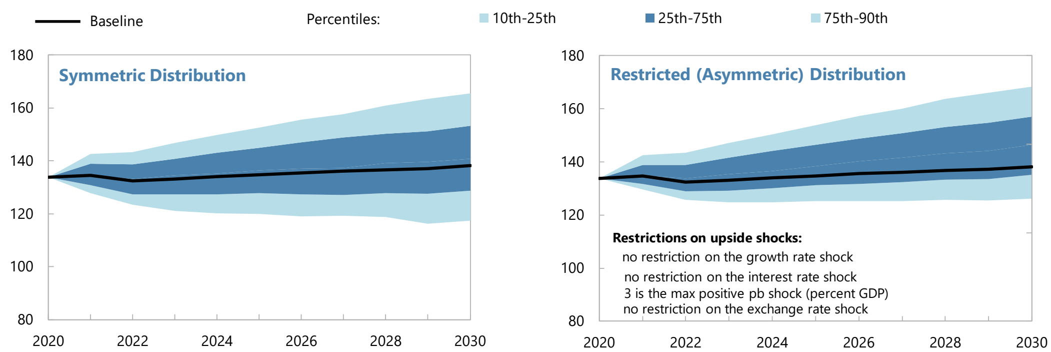
Appendix II. Figure 1. United States: Public DSA—Risk Assessment

Heat Map Baseline (2020-2030)

Debt level 1/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs 2/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile 3/	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

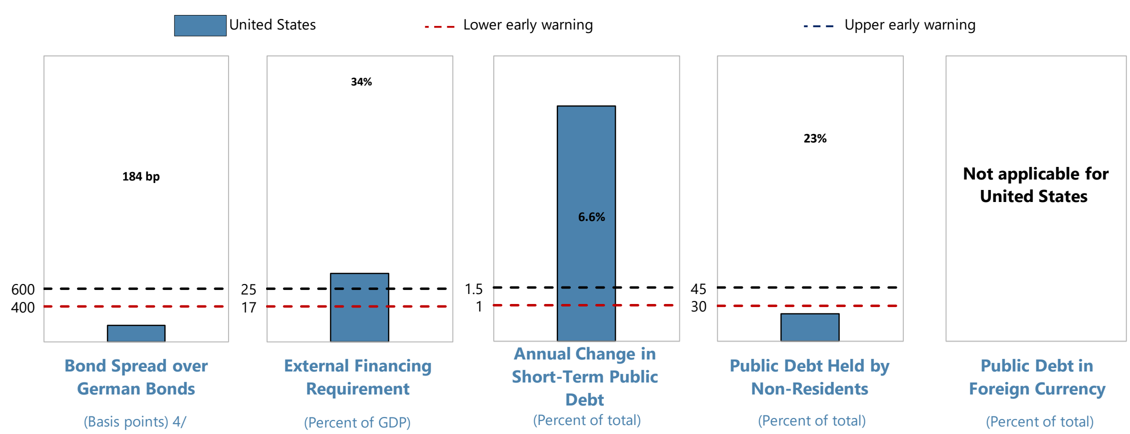
Evolution of Predictive Densities of Gross Nominal Public Debt

(Percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks)



Source: IMF staff

1/ The cell is highlighted in green if debt burden benchmark of 85% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant

2/ The cell is highlighted in green if gross financing needs benchmark of 20% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant

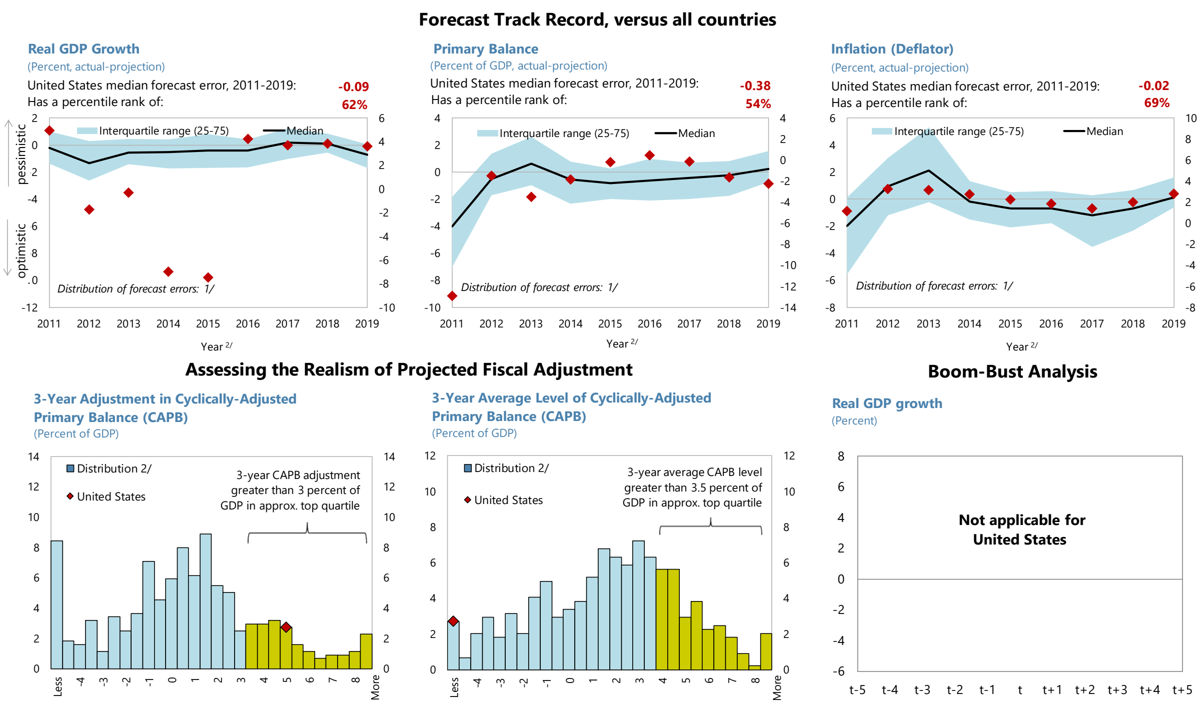
3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.

Lower and upper risk-assessment benchmarks are:

400 and 600 basis points for bond spreads; 17 and 25 percent of GDP for external financing requirement; 1 and 1.5 percent for change in the share of short-term debt; 30 and 45 percent for the public debt held by non-residents

4/ An average over the last 3 months, 20-Mar-21 through 18-Jun-21

Appendix II. Figure 2. United States: Public DSA—Realism of Baseline Assumption



Source : IMF staff

1/ Plotted distribution includes all countries, percentile rank refers to all countries. Projections made in the spring WEO vintage of the preceding year

2/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis

Appendix II. Figure 3. United States: Public DSA—Baseline Scenario

(Percent of GDP, unless otherwise indicated)

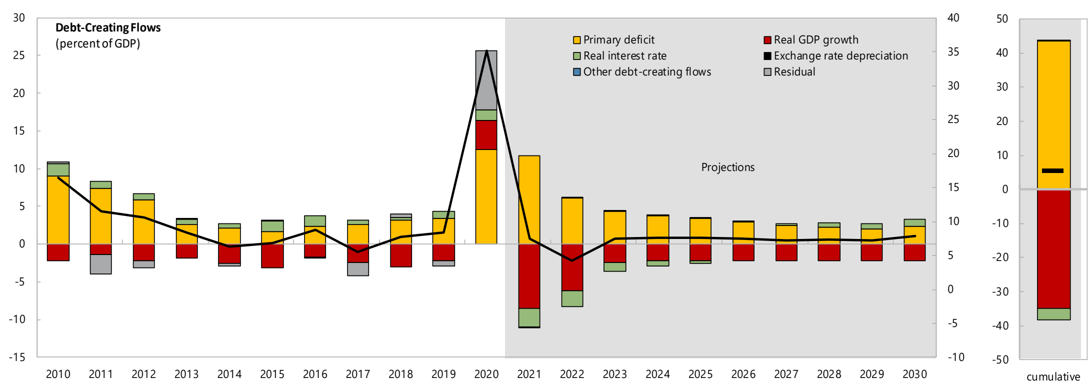
Debt, Economic and Market Indicators 1/

	Actual			Projections									
	2010–2018 2/	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Nominal gross public debt	103.5	108.1	133.8	134.6	132.4	133.1	133.9	134.8	135.5	136.1	136.7	137.1	138.2
Public gross financing needs	38.5	40.4	73.3	51.8	36.1	31.1	28.7	29.6	28.4	28.6	28.5	28.8	28.7
Real GDP growth (percent)	2.3	2.2	-3.5	7.0	4.9	1.9	1.7	1.7	1.7	1.7	1.7	1.7	1.7
Inflation (GDP deflator, percent)	1.7	1.8	1.2	3.4	2.9	2.3	2.2	2.1	2.0	2.0	2.0	2.0	2.0
Nominal GDP growth (percent)	4.0	4.0	-2.3	10.7	8.0	4.3	4.0	3.9	3.8	3.8	3.8	3.8	3.8
Effective interest rate (percent) 4/	2.7	2.7	2.4	1.6	1.3	1.5	1.7	1.9	2.1	2.3	2.5	2.6	2.7

As of June 08, 2020		
Sovereign Spreads		
Spread (bp) 3/		.
CDS (bp)		0
Ratings	Foreign	Local
Moody's	Aaa	Aaa
S&Ps	AA+	AA+
Fitch	AAA	AAA

Contribution to Changes in Public Debt

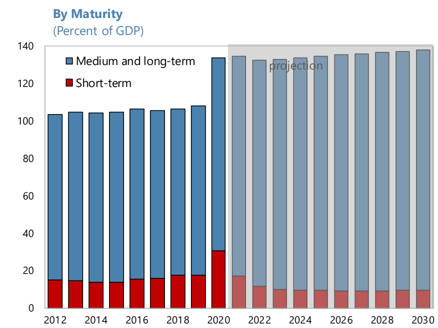
	Actual			Projections											
	2010–2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Cumulative	Debt-stabilizing primary balance 9/
Change in gross public sector debt	2.2	1.5	25.7	0.8	-2.2	0.7	0.8	0.8	0.8	0.5	0.6	0.5	1.0	4.3	-1.4
Identified debt-creating flows	2.8	2.1	17.8	0.8	-2.2	0.7	0.8	0.8	0.8	0.5	0.6	0.5	1.0	4.3	
Primary deficit	4.1	3.4	12.6	11.8	6.1	4.3	3.7	3.4	2.9	2.5	2.3	2.0	2.4	41.3	
Primary (noninterest) revenue and grants	29.9	29.4	30.0	29.3	31.3	31.7	31.6	31.6	32.0	32.3	32.1	32.0	31.9	315.7	
Primary (noninterest) expenditure	33.9	32.9	42.6	41.1	37.4	36.0	35.3	34.9	34.9	34.7	34.4	34.0	34.3	357.0	
Automatic debt dynamics 5/	-1.3	-1.3	5.2	-11.0	-8.3	-3.6	-2.9	-2.6	-2.1	-1.9	-1.7	-1.5	-1.4	-37.0	
Interest rate/growth differential 6/	-1.3	-1.3	5.2	-11.0	-8.3	-3.6	-2.9	-2.6	-2.1	-1.9	-1.7	-1.5	-1.4	-37.0	
Of which: real interest rate	0.9	0.9	1.4	-2.5	-2.2	-1.1	-0.8	-0.4	0.1	0.3	0.6	0.7	0.8	-4.4	
Of which: real GDP growth	-2.3	-2.2	3.9	-8.5	-6.1	-2.5	-2.2	-2.2	-2.2	-2.2	-2.2	-2.2	-2.2	-32.6	
Exchange rate depreciation 7/	0.0	0.0	0.0	…	…	…	…	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Net privatization proceeds	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other liabilities (bank recap. and PSI sweetner)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes 8/	-0.6	-0.6	7.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	

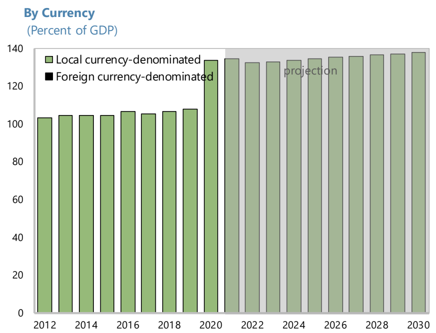


Source: IMF staff
1/ Public sector is defined as general government
2/ Based on available data
3/ Bond Spread over German Bonds
4/ Defined as interest payments divided by debt stock at the end of previous year
5/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation
6/ The real interest rate contribution is derived from the denominator in footnote 4 as r - π (1+g) and the real growth contribution as -g
7/ The exchange rate contribution is derived from the numerator in footnote 2/ as ae(1+r).
8/ For projections, this line includes exchange rate changes during the projection period. Also includes ESM capital contribution, arrears clearance, SMP and ANFA income, and the effect of deferred interest
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year

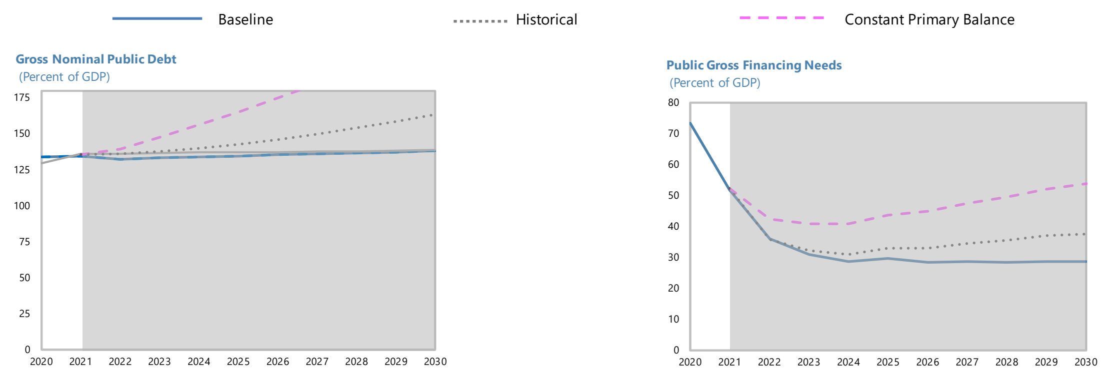
Appendix II. Figure 4. United States: Public DSA—Composition of Public Debt and Alternative Scenarios

Composition of Public Debt





Alternative Scenarios



Underlying Assumptions
(Percent)

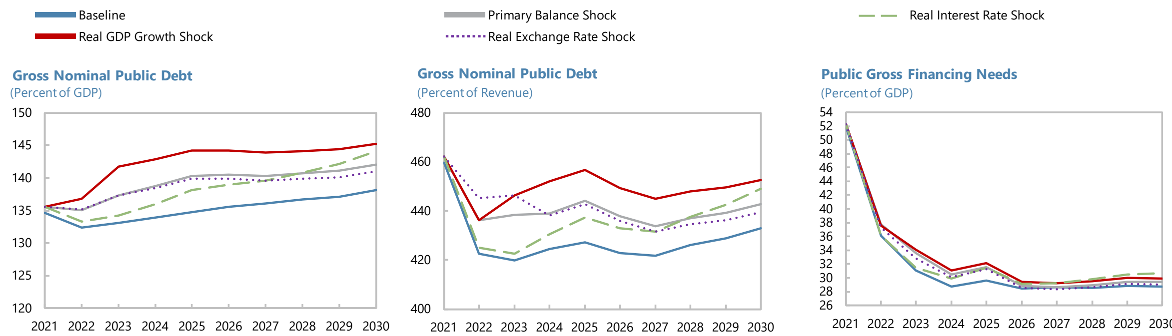
Baseline scenario	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Real GDP growth	7.0	4.9	1.9	1.7	1.7	1.7	1.7	1.7	1.7	1.7
Inflation	3.4	2.9	2.3	2.2	2.1	2.0	2.0	2.0	2.0	2.0
Primary balance	-11.8	-6.1	-4.3	-3.7	-3.4	-2.9	-2.5	-2.3	-2.0	-2.4
Effective interest rate	1.6	1.3	1.5	1.7	1.9	2.1	2.3	2.5	2.6	2.7
Constant primary balance scenario										
Real GDP growth	7.0	4.9	1.9	1.7	1.7	1.7	1.7	1.7	1.7	1.7
Inflation	3.4	2.9	2.3	2.2	2.1	2.0	2.0	2.0	2.0	2.0
Primary balance	-11.8	-11.8	-11.8	-11.8	-11.8	-11.8	-11.8	-11.8	-11.8	-11.8
Effective interest rate	1.6	1.4	1.5	1.7	1.9	2.2	2.4	2.6	2.7	2.8

Historical scenario	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Real GDP growth	7.0	1.7	1.7	1.7	1.7	1.7	1.7	1.7	1.7	1.7
Inflation	3.4	2.9	2.3	2.2	2.1	2.0	2.0	2.0	2.0	2.0
Primary balance	-11.8	-4.4	-4.4	-4.4	-4.4	-4.4	-4.4	-4.4	-4.4	-4.4
Effective interest rate	1.6	1.4	1.9	2.3	2.7	3.1	3.4	3.7	3.9	4.0

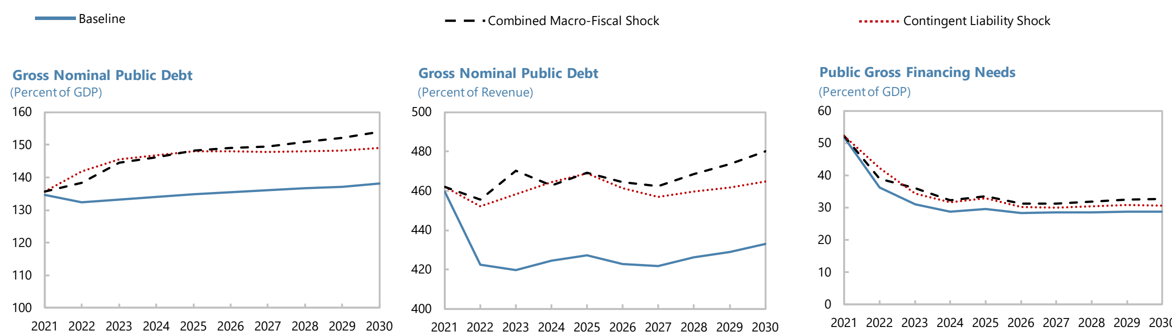
Source: IMF staff

Appendix II. Figure 5. United States: Public DSA—Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions

(Percent)

	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Primary Balance Shock										
Real GDP growth	7.0	4.9	2.0	1.7	1.7	1.7	1.7	1.7	1.7	1.7
Inflation	3.4	2.9	2.3	2.2	2.1	2.0	2.0	2.0	2.0	2.0
Primary balance	-11.8	-7.8	-6.0	-3.7	-3.4	-2.9	-2.5	-2.3	-2.0	-2.4
Effective interest rate	1.6	1.4	1.6	1.9	2.0	2.2	2.4	2.6	2.7	2.8
Real Interest Rate Shock										
Real GDP growth	7.0	4.9	1.9	1.7	1.7	1.7	1.7	1.7	1.7	1.7
Inflation	3.4	2.9	2.3	2.2	2.1	2.0	2.0	2.0	2.0	2.0
Primary balance	-11.8	-6.1	-4.3	-3.7	-3.4	-2.9	-2.5	-2.3	-2.0	-2.4
Effective interest rate	1.6	1.4	1.8	2.1	2.4	2.7	3.0	3.2	3.4	3.5
Combined Shock										
Real GDP growth	7.0	3.0	0.1	1.7	1.7	1.7	1.7	1.7	1.7	1.7
Inflation	3.4	2.6	2.0	2.2	2.1	2.0	2.0	2.0	2.0	2.0
Primary balance	-11.8	-8.3	-6.9	-3.7	-3.4	-2.9	-2.5	-2.3	-2.0	-2.4
Effective interest rate	1.6	1.4	1.8	2.1	2.4	2.7	3.0	3.2	3.4	3.5

	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Real GDP Growth Shock										
Real GDP growth	7.0	3.0	0.1	1.7	1.7	1.7	1.7	1.7	1.7	1.7
Inflation	3.4	2.6	2.0	2.2	2.1	2.0	2.0	2.0	2.0	2.0
Primary balance	-11.8	-6.9	-5.9	-3.7	-3.4	-2.9	-2.5	-2.3	-2.0	-2.4
Effective interest rate	1.6	1.4	1.5	1.7	1.9	2.1	2.3	2.5	2.6	2.7
Real Exchange Rate Shock										
Real GDP growth	7.0	3.9	1.4	1.7	1.7	1.7	1.7	1.7	1.7	1.7
Inflation	3.4	3.2	2.3	2.2	2.1	2.0	2.0	2.0	2.0	2.0
Primary balance	-11.8	-7.1	-5.3	-3.7	-3.4	-2.9	-2.5	-2.3	-2.0	-2.4
Effective interest rate	1.6	1.4	1.5	1.7	1.9	2.1	2.3	2.5	2.6	2.7
Contingent Liability Shock										
Real GDP growth	7.0	3.0	0.1	1.7	1.7	1.7	1.7	1.7	1.7	1.7
Inflation	3.4	2.5	1.8	2.2	2.1	2.0	2.0	2.0	2.0	2.0
Primary balance	-11.8	-11.5	-4.3	-3.7	-3.4	-2.9	-2.5	-2.3	-2.0	-2.4
Effective interest rate	1.6	1.4	1.7	1.8	2.0	2.2	2.4	2.5	2.6	2.7

Source: IMF staff

Appendix III: External Sector Assessment

Overall Assessment: *The external position in 2020 was moderately weaker than the level implied by medium-term fundamentals and desirable policies.* Larger private sector saving has largely offset the 2020 fiscal packages, resulting in a transitory modest deterioration of the CA balance. The deep economic contraction, and ongoing changes in fiscal, trade, and labor-market (including, for example, immigration) policies, add uncertainty to the assessment.

Potential Policy Responses: In the near term, given the unprecedented social and economic fallout from the pandemic, front-loaded fiscal support is needed to ease the burden on households and firms, and to support the economic recovery. Over the medium term, fiscal consolidation will be critical to place debt on a sustainable footing, support external rebalancing, and bring the current account balance closer to its norm. Consolidation should target a medium-term general government primary surplus of about 1 percent of GDP to put the debt-to-GDP ratio on a downward path. Structural policies to increase productivity, including of tradables sectors, such as upgrading infrastructure and enhancing schooling, training, and the mobility of workers, can further contribute to external rebalancing. Tariff barriers should be rolled back, and trade and investment disputes should be resolved in a manner that supports an open, stable, and transparent global trading system.

Foreign Asset and Liability Position and Trajectory	**Background.** The NIIP, which averaged about −42.6 percent during 2015–18, decreased further from −51.6 percent of GDP in 2019 to −67.3 percent of GDP in 2020. Under the IMF staff baseline scenario, the NIIP is projected to remain broadly unchanged through the medium term as the CA balance reverts to its pre-COVID average. **Assessment.** Financial stability risks could surface in the form of an unexpected decline in foreign demand for US fixed-income securities, which are a main component of the country's external liabilities. This risk, which could materialize, for example, due to a failure to reestablish fiscal sustainability, remains moderate given the dominant status of the US dollar as a reserve currency. About 60 percent of US assets are in the form of FDI and portfolio equity claims.				
2020 (% GDP)	NIIP: −67.3	Gross Assets: 153.6	Res. Assets: 3.0	Gross Liab.: 220.9	Debt Liab.: 102.6

Current Account	**Background.** The US CA deficit increased from 2.2 percent of GDP in 2019 to 3.0 percent in 2020 (from 2.0 to 2.7 in cyclically adjusted terms) compared with a deficit of 2.2 percent of GDP in 2015. The evolution since 2015 is explained mostly by deterioration in the non-oil and income balances. In 2020 the trade balance declined slightly from 2019 (−2.7 versus −3.2 percent of GDP) mostly due to changes in the non-oil balance, while the income account declined slightly due to a weaker primary account balance. The large increase in the fiscal deficit (relative to other countries), mostly due to COVID-19, led to only a small increase in the CA deficit in 2020 due to the large increase in private savings. The CA deficit is expected to remain above 2 percent of GDP over the medium term. **Assessment**. The EBA model estimates a cyclically adjusted CA balance of −2.8 percent of GDP and a cyclically adjusted CA norm of −0.5 percent of GDP. The norm increased from −0.7 percent GDP in 2019 due to an increase of 1.3 percent of GDP in the medium-term desirable cyclically adjusted general government fiscal balance. The EBA model CA gap is −2.3 percent of GDP for 2020, reflecting policy gaps (−1.8 percent of GDP, almost all of which, −1.8 percent, corresponds to fiscal policy) and an unidentified residual (about −0.5 percent of GDP) that may reflect structural factors not included in the model. On balance, the IMF staff assesses the 2020 cyclically adjusted CA to be 1.8 percent of GDP lower than the level implied by medium-term fundamentals and desirable policies. This assessment includes an IMF staff adjustor of 0.5 percent of GDP to account for the effects of COVID-19 on the oil, medical, and travel services (including tourism) balances (0.1 percent of GDP each) as well as the shift of household consumption from services to consumer goods (0.2 percent of GDP).						
2020 (% GDP)	CA: −3.1	Cycl. Adj. CA: −2.8	EBA Norm: −0.5	EBA Gap: −2.3	COVID-19 Adj.: 0.5	Other Adj.: 0.0	Staff Gap: −1.8

Real Exchange Rate	**Background.** After appreciating by 2.8 percent in 2019, the REER appreciated by 1.4 percent in 2020. Through the second quarter of 2020, the REER appreciated 4.3 percent in relation to the end of 2019. Despite depreciating in the second half of 2020 by 5.4 percent, as of the end of 2020 the REER was still about 14 percent higher than the average for 2015. As of end-May 2021, the REER had depreciated by 3.9 percent compared to the 2020 average. **Assessment.** Indirect estimates of the REER (based on the IMF staff CA assessment) imply that the exchange rate was overvalued by 8.8 percent in 2020 (applying the estimated elasticity of −0.2). The EBA REER index model suggests an overvaluation of 8.3 percent, and the EBA REER level model suggests an overvaluation of 12.4 percent. Considering all the estimates and their uncertainties, the IMF staff assesses the 2020 average REER to be somewhat overvalued, in the 5.8–11.8 percent range, with a midpoint of 8.8 percent.
Capital and Financial Accounts: Flows and Policy Measures	**Background.** The financial account balance was about −3.7 percent of GDP in 2020 compared with −1.8 percent of GDP in 2019. An increase in net direct investment (0.5 percent GDP) was offset by decreases in net portfolio investments (0.8 percent GDP) and other net investments. **Assessment.** The United States has an open capital account. Vulnerabilities are limited by the dollar's status as a reserve currency, with foreign demand for US Treasury securities supported by the status of the dollar as a reserve currency and, possibly, by safe haven flows.
FX Intervention and Reserves Level	**Assessment.** The dollar has the status of a global reserve currency. Reserves held by the United States are typically low relative to standard metrics. The currency is free floating.

Appendix IV. Implementation of 2020 FSAP Recommendations[1]

FSAP Recommendations	Developments	Status (Implemented, partially implemented, not implemented)
Systemic Risk Oversight and Macroprudential Framework		
Provide an explicit financial stability mandate to all federal FSOC members.	This legislative recommendation has not been implemented.	Not Implemented
Prioritize the development of macroprudential tools to address risks and vulnerabilities in the nonbank sector.	During the March 31st Council meeting, the Secretary identified risks related to nonbank financial intermediation as one of the priorities for the Council going forward. It is important to assess the risks posed by open-end mutual funds and money market funds given that those risks materialized during last spring's market stress. On open-end funds, the Secretary called for an interagency assessment to determine if additional measures should be taken to address the financial stability vulnerability associated with open-end funds, and, if so, to develop recommendations for the FSOC. On money market funds, the Secretary has stated that it is encouraging that regulators are considering substantive reform options for money market mutual funds, and that she supports the SEC's efforts to strengthen short-term funding markets. The Secretary also announced the reestablishment of the FSOC Hedge Fund Working Group to help share data,	Partially Implemented

[1] This annex contains the U.S. authorities' self-assessment of the status of implementation of the recommendations of the 2020 FSAP and is not necessarily the assessment of IMF staff.

	identify risks, and work to strengthen the financial system.	
Intensify efforts to close data gaps, including reporting disclosures of holdings of collateralized loan obligations (CLOs) and repo markets, to reinforce market discipline.	In February 2019, the OFR promulgated 12 CFR Part 1610, a rule regarding "Ongoing Data Collection of Centrally Cleared Transactions in the U.S. Repurchase Agreement Market". Data collection from private entities deemed "covered reporters" began in October 2019. In September 2020, the OFR launched its Short-Term Funding Monitor, which integrates data collected from centrally cleared repo transactions with triparty repo transaction data from the New York Federal Reserve Bank and other existing data sets previously scattered across many sources, into a combined monitor which users can download via a public application programming interface.	Partially Implemented
Banking Regulation and Supervision		
Review prudential requirements for non-internationally active banks (Category III and IV) and ensure they are and continue to be broadly consistent with the Basel capital framework and appropriate concentration limits; and consider extending the full liquidity coverage ratio (LCR) to them.	No material developments to report. As stated in the U.S. Executive Director's statement in the 2020 Article IV, "in recent years, U.S. authorities have reviewed regulation and supervision and have made carefully considered changes to maintain safety and soundness while better aligning enhanced requirements to the risks that specific banks pose to the financial system. This tailoring considers not only asset size but also a number of risk indicators, including cross-jurisdictional activity, reliance on short-term wholesale funding, and off-balance sheet exposures. With this context, we disagree with [IMF] staff's focus on and interpretation of standards regarding non-internationally active banks. Subjecting these banks to G-SIB requirements would impose restrictions that are	Implemented

	disproportionate to their lower risk and impede their ability to facilitate credit to the domestic economy."	
Streamline regulatory requirements and consider rewriting key prudential guidance as regulation.	No material developments to report.	Not Implemented
Introduce heightened standards on the governance of large and complex bank holding companies (BHCs), enhance the related-party framework, introduce rules on concentration risk management, and include more quantitative standards regarding interest rate risk in the banking book.	No material developments to report. As stated in the U.S. Executive Director's statement in the 2020 Article IV, "in recent years, U.S. authorities have reviewed regulation and supervision and have made carefully considered changes to maintain safety and soundness while better aligning enhanced requirements to the risks that specific banks pose to the financial system. This tailoring considers not only asset size but also a number of risk indicators, including cross-jurisdictional activity, reliance on short-term wholesale funding, and off-balance sheet exposures. With this context, we disagree with [IMF] staff's focus on and interpretation of standards regarding non-internationally active banks. Subjecting these banks to G-SIB requirements would impose restrictions that are disproportionate to their lower risk and impede their ability to facilitate credit to the domestic economy."	Not Implemented
Insurance Regulation and Supervision		
Increase independence of state insurance regulators, with appropriate accountability.	It is not substantiated that supervisory independence is undermined if commissioners are appointed and/or elected. Further, recommended reforms at the state government level are beyond the purview of individual state insurance departments. The method of commissioner selection is determined by the legislatures in each state. NAIC has sent this recommendation over	Not Implemented

	to NCOIL, NCSL and to the Legislative Liaisons Bulletin Board for their awareness.	
Require all in-force life insurance business be moved to principles-based reserving (PBR) after a five-year transition period, adjust asset valuation approach to ensure consistency between assets and liabilities, and recalibrate risk-based capital (RBC) to the revised valuation approach.	It would require a very significant effort for life insurance companies to set up PBR modeling for their in-force business. PBR applies only to new business for several reasons: (1) formulaic reserves are generally conservative for in-force life insurance products, and under PBR, whole life policies will generally pass exemption tests and continue to be valued under the old reserve methodology; (2) Term insurance products will move to PBR relatively quickly since they have a limited duration and will expire; and (3) State law prevents new valuations on existing products that have minimum non-forfeiture benefits derived at the date of issue of the contract.	Not Implemented
Develop a consolidated group capital requirement similar to GAAP-Plus insurance capital standard (ICS) for internationally active groups and optionally for domestic groups in parallel with the development of aggregation approaches by the FRB and NAIC.	The FRB and NAIC continue to develop their aggregation approaches, and the United States—along with other interested jurisdictions—is developing an Aggregation Method at the IAIS. The IAIS has developed high-level principles and is working to develop criteria to assess whether the Aggregation Method provides comparable outcomes to the ICS by the end of the monitoring period. No U.S. regulator intends to adopt the ICS in its current form.	Not implemented
Regulation, Supervision, and Oversight of FMIs		
Increase CFTC resources devoted to CCP supervision and strengthen rule-approval process to an affirmative approval with a public consultation.	On December 28, 2020, Congress approved additional resources to the CFTC, https://www.govinfo.gov/content/pkg/BILLS-116hr133enr/pdf/BILLS-116hr133enr.pdf	Implemented

Collaborate to analyze differences in outcomes of CCP risk management practices and adopt an appropriately consistent, conservative implementation of risk management standards across CCPs.	The FRB, SEC, and CFTC, respectively, have implemented regulatory frameworks as mandated by Title VIII of the Dodd-Frank Act and that are consistent with the PFMI. The authorities also continue to actively cooperate, coordinate, consult, and collaborate on oversight of CCPs, including risk management practices. For example, the authorities coordinate and collaborate on examinations of CCP risk management practices as well as on reviews of proposed changes to those frameworks. While acknowledging that CCPs operate in different markets, which may require different approaches to managing risk, the authorities continue to discuss differences in the outcomes of risk management practices at CCPs, with considerations taken for financial stability and market impact.	Partially Implemented
Develop and execute more comprehensive systemwide CCP supervisory stress tests.	Preparatory work to conduct a joint supervisory stress test of CCPs began in 2019. Progress has been temporarily delayed as resources were necessarily diverted to address unprecedented COVID-related developments, but engagement will resume. During the pandemic, the authorities endeavored to address these challenges and their effects on registered entities, including CCPs. The SEC developed a COVID-19 Market Monitoring Group to assist in the SEC's efforts to coordinate with and support the COVID-19-related efforts of other federal financial agencies and other bodies, including the President's Working Group on Financial Markets (PWG), Financial Stability Oversight Council (FSOC) and the Financial Stability Board (FSB), among others. The CFTC led a multi-agency default drill in which CCPs from around the world simulate the default and liquidation of a large clearing member during a period of extreme market stress. This exercise is	Fully Implemented with regard to collaboration and implementation of robust risk management standards. Partially Implemented to reflect continued discussion by authorities.

	designed to quantify the effects of individual CCP actions on the clearing system due to simultaneous liquidations and to identify operational or systemic concerns. The CFTC is also co-chairing an international working group focused on the effects of margin demands on the financial system during the period of extreme market stress in March and April of 2020. See also U.S. FSAP Technical Note: Supervision of Financial Market Infrastructures, Resilience of Central Counterparties and Innovative Technologies (July 2020) ("FMIs appeared so far sufficiently robust to manage surges in volumes and volatility in financial markets during the COVID-19 crisis.").	
Securities Regulation and Supervision		
Give CFTC and SEC greater independence to determine their own resources, with appropriate accountability.	This legislative recommendation has not been implemented.	Not Implemented
Assess financial stability risks related to mutual funds and stable net asset value (NAV) money market funds (MMFs), including through SEC-led liquidity stress testing.	The SEC published a request for comment earlier this year at https://www.sec.gov/rules/other/2021/ic-34188.pdf. On June 11, 2021 the SEC also noted forthcoming work on money market funds in its Annual Regulatory Agenda at https://ww.sec.gov/news/press-release-2021-99. SEC staff also participated in related work in the PWG, IOSCO and the FSB.	Partially Implemented
Conclude implementation of new broker-dealer capital rules; finalization of market-wide circuit breakers, and	Implementation of new broker-dealer capital rules. On June 21, 2019, the SEC adopted final rules addressing the Title VII requirements for, among other things, capital and segregation requirements for broker-dealers;	Fully Implemented (as of October 6, 2021)

delivery of the Consolidated Audit Trail.	the compliance date for this rulemaking is October 6, 2021 See https://www.sec.gov/news/press-release-2019-105. Finalization of market-wide circuit breakers. The market-wide circuit breakers ("MWCB") operate on a pilot basis that expires on October 19, 2021, unless extended or made permanent. The MWCB were triggered four times in March 2020, providing the self regulatory organizations (SROs) and the SEC with an opportunity to assess its performance. SEC and industry assessments are underway. Delivery of the Consolidated Audit Trail. The SEC charged the SROs with developing and building a Consolidated Audit Trail. For information on the SROs' progress, links to the CAT Implementation Plan, which was filed with the Commission on July 22, 2020, as well as the quarterly progress reports ("QPRs") see https://www.catnmsplan.com/implmentation-plan.	Partially Implemented Partially Implemented
Increase scrutiny of new registrants and reduce reliance on self-attestations where applicable.	Whether a registered investment adviser is a newly registered firm is one of the risk factors that the Division of Examinations considers in selecting firms for examination. Newly registered commodity pool operators (CPOs) immediately become eligible for examination utilizing NFA's risk assessment/model function. There are a number of factors that, if present, may result in a newly registered CPO being scheduled for examination including background of firm personnel.	Partially Implemented

AML/CFT		
Legislate to collect beneficial ownership information on formation of U.S. corporations, maintain it, and ensure timely access for authorities.	The AML Act of 2020, which includes the Corporate Transparency Act, was enacted on January 1, 2021, and requires that reporting companies disclose their beneficial owners when they are formed (or, for non-U.S. companies, when they register with a State to do business in the U.S.), and when they change beneficial owners.	Implemented
Ensure that investment advisers, lawyers, accountants, and company service providers are effectively regulated and supervised for AML/CFT in line with risks.	The FATF most recently assessed the United States' progress on these action items as a part of the Third Follow-Up to the U.S. Mutual Evaluation. The United States will continue to engage with the FATF on addressing the gaps identified in that assessment. https://www.fatf-gafi.org/media/fatf/documents/reports/fur/Follow-Up-Report-United-States-March-2020.pdf	Partially Implemented
Systemic Liquidity		
Promote the fungibility of Treasury Securities and Reserves by adjusting assumptions about firms' access to the Discount Window in liquidity metrics.	No changes have been made since the FSAP was conducted.	Not Implemented
Continue to operate regular fine-tuning OMOs.	In the current operating environment, fine-tuning or reserve management OMOs are not needed. The FOMC currently instructs the desk to: Undertake OMOs as necessary to maintain the federal funds rate in a target range of 0 to 1/4 percent. Increase the SOMA holdings of Treasury securities by $80 billion per month and of agency mortgage-backed securities (MBS) by $40 billion per month.	Implemented

	Increase holdings of Treasury securities and agency MBS by additional amounts and purchase agency commercial mortgage-backed securities (CMBS) as needed to sustain smooth functioning of markets for these securities. Conduct repurchase agreement operations to support effective policy implementation and the smooth functioning of short-term U.S. dollar funding markets. This policy has been in place since December 2020.	
Advance arrangements for providing liquidity to systemic nonbanks and CCPs under stress, and reconsider restrictions on bilateral emergency liquidity assistance (ELA) to designated systemically important nonbanks.	No changes have been made since the FSAP was conducted. The Federal Reserve has the ability to provide liquidity to systemic nonbanks under stress through broad-based liquidity facilities under Section 13(3) of the Federal Reserve Act. In addition, for a CCP that the FSOC has designated as systemically important, the Federal Reserve is authorized to provide liquidity on a bilateral basis in unusual or exigent circumstances (among other restrictions). (The recommendation to reconsider restrictions on bilateral emergency liquidity assistance to systemic nonbanks should be directed to Congress.)	Not Implemented
Develop robust and effective backup plans in the event the sole provider, Bank of New York Mellon (BNYM), is not able to settle and clear repo transactions.	The Federal Reserve has conducted outreach to market participants to develop awareness and support for the development of robust plans in the event that BNYM is not able to settle and clear repo transactions. Market participants offered widespread interest and support for this effort. The Federal Reserve has since started discussions to form a working group that would consist of market participants and infrastructures in order to develop and implement these plans.	Partially Implemented
Enhance arrangements to provide liquidity support in	No changes have been made since the FSAP was conducted.	Not Implemented

foreign currencies to banks and designated systemically important CCPs.		
Crisis Preparedness and Management		
Intensify crisis preparedness.	Following the financial crisis of 2008, FSOC was created to identify threats to the financial stability of the country, promote market discipline, and respond to emerging risks to the stability of the nation's financial system. It serves as an effective venue for information sharing and coordination among financial regulatory agencies. FSOC is not intended to serve as the primary responder during times of financial crisis. Rather, its purpose is to identify potential vulnerabilities and emerging threats to financial stability, and to develop recommendations for addressing those risks. While comprised of members who have significant regulatory authority, FSOC is not a regulator. However, FSOC does provide a forum for information sharing and coordination among regulators. FSOC leverages the resources and expertise of its member agencies. For example, a number of financial regulators organize tabletop exercises, and FSOC staff regularly participate in those activities. During the spring 2020 market stress, the federal government's response was timely, forceful, and helped preserve financial stability, as noted in the 2020 FSAP. We believe our experience in the recent crisis shows that crisis preparedness processes are sufficiently robust to	Partially Implemented

	have us well positioned should the federal government need to respond to future market stress. The FBAs led and participated in 2020, and continues to maintain, significant principal and staff-level engagements, both interagency and with foreign jurisdictions, to discuss cross-border issues and potential impediments that could affect the resolution of a G-SIB, including in the context of ongoing trilateral work with U.S., UK, and European financial regulatory authorities. In addition, the FBAs works with staff from the U.S. financial regulatory authorities, and with foreign supervisors and resolution authorities and within international groups, to understand risks, identify resolution options, and address related CCP resolution planning issues.	
Continue to use agency discretion actively to subject a wider array of firms to RRP.	No material developments to report.	Not Implemented
Continue to undertake, at least yearly, Dodd-Frank Act (DFA) Title II plans, resolvability assessments, and crisis management group (CMG) discussions of RRPs and assessments.	The FBAs continue to review RRPs submitted by firms with an increasing focus on testing a range of firms' capabilities that support resiliency, recoverability, and resolvability. The FDIC and FRB also continue to co-chair annual Crisis Management Group (CMG) meetings for U.S. G-SIBs, with the participation of the OCC and SEC, as applicable, and relevant host authorities, to discuss home-and-host resolvability assessments for the firms to facilitate cross-border resolution planning. Further, the FDIC has undertaken institution-specific strategic planning to carry out its orderly liquidation	Implemented

	authorities with respect to the largest G-SIBs operating in the United States. The FDIC continues to build out process documents to facilitate the implementation of the framework in a Title II resolution.	
Extend OLA powers to cover FBOs' U.S. branches; ensure equal depositor preference ranking for overseas branch deposits with domestic deposits; introduce powers to give prompt and predictable legal effect to foreign resolution measures.	This legislative recommendation has not been implemented.	Not Implemented

INTERNATIONAL MONETARY FUND

UNITED STATES

July 6, 2021

STAFF REPORT FOR THE 2021 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By The Western Hemisphere Department (in consultation with other departments)

CONTENTS

FUND RELATIONS

(As of May 31, 2021)

Membership Status: Joined: December 27, 1945; Article VIII

General Resources Account:	**SDR Million**	**Percent of Quota**
Quota	82,994.20	100.00
IMF's Holdings of Currency (Holdings Rate)	60,068.51	72.38
Reserve Tranche Position	22,964.17	27.67
Lending to the Fund		
New Arrangements to Borrow	797.03	

SDR Department:	**SDR Million**	**Percent of Allocation**
Net cumulative allocation	35,315.68	100.00
Holdings	36,766.85	104.11

Outstanding Purchases and Loans: None

Financial Arrangements: None

Projected Payments to Fund [1/]

(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2021	2022	2023	2024	2025
Principal					
Charges/Interest		0.59	0.59	0.59	0.59
Total		0.59	0.59	0.59	0.59

1/ When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Exchange Rate Arrangements. The exchange rate of the U.S. dollar floats independently and is determined freely in the foreign exchange market. The United States has accepted the obligations under Article VIII, Sections 2(a), 3 and 4 of the IMF's Articles of Agreement and maintains an exchange system free of multiple currency practices and restrictions on the making of payments and transfers for current international transactions, except for those measures imposed for security reasons. The United States notifies the maintenance of measures imposed for security reasons under

Executive Board Decision No. 144–(52/51). The last of these notifications was made on June 14, 2021.

Article IV Consultation. The 2021 Article IV consultation was concluded on July 19, 2021 and the Staff Report was published as IMF Country Report No. [21/xxx]. A fiscal Report of Observance of Standards and Codes was completed in the context of the 2003 consultation. The 2021 Article IV discussions took place during June 7–June 23, 2021. Concluding meetings with Chair Powell of the Board of Governors of the Federal Reserve System, and Treasury Secretary Yellen occurred on July 1. The Managing Director, Ms. Georgieva, and Deputy Managing Director Zhang participated in the concluding meetings. A press conference on the consultation was held on July 1, 2021. The team comprised Nigel Chalk (head), Anke Weber, Katharina Bergant, Andrew Hodge, Li Lin, Rui Mano, Andrea Medici, Yannick Timmer (all WHD), Mico Mrkaic and Elizabeth Van Heuvelen (SPR). Ms. Elizabeth Shortino (Acting Executive Director) and Mr. Logan Sturm (Advisor) attended some of the meetings. Outreach included discussions with the U.S. Chamber of Commerce, private sector representatives, and think tanks. Unless an objection from the authorities of the United States is received prior to the conclusion of the Board's consideration, the document will be published.

STATISTICAL ISSUES

As of June 30, 2021

I. Assessment of Data Adequacy for Surveillance	
General: Comprehensive economic data are available for the United States on a timely basis. Data provision is adequate for surveillance, including its coverage, periodicity, and timeliness.	
II. Data Standards and Quality	
The United States is an adherent to the Special Data Dissemination Standard Plus (SDDS Plus) since February 18, 2015, and its metadata are posted on the Dissemination Standards Bulletin Board (DSBB). The United States' latest SDDS Plus Annual Observance Report is available on the DSBB.	No data ROSC has been conducted.

Table 1. United States: Table of Common Indicators Required for Surveillance
(As of July 6, 2021)

	Date of latest observation	Date received	Frequency of data[1]	Frequency of reporting[1]	Frequency of publication[1]
Exchange rates	Same day	Same day	D	D	D
International reserve assets and reserve liabilities of the monetary authorities[2]	2021 M5	Jun 30	M	M	M
Reserve/base money	2021 M5	Jun 22	M	M	M
Broad money	2021 M5	Jun 22	M	M	M
Central bank balance sheet	Jul 1	Jul 1	W	W	W
Consolidated balance sheet of the banking system	2021 Q1	Jun 11	Q	Q	Q
Interest rates[3]	Same day	Same day	D	D	D
Consumer price index	2021 M5	Jun 10	M	M	M
Revenue, expenditure, balance and composition of financing[4]—general government[5]	2021 Q1	Jun 24	Q	Q	Q
Revenue, expenditure, balance and composition of financing[4]—central government	2021 M5	Jun 10	M	M	M
Stocks of central government and central government-guaranteed debt	2021 M6	Jun 30	M	M	M
External current account balance	2021 Q1	Jun 23	Q	Q	Q
Exports and imports of goods and services	2021 M5	Jul 2	M	M	M
GDP/GNP (1st release)	2021 Q1	Apr 29	Q	M	M
Gross External Debt	2021 Q1	Jun 30	Q	Q	Q
International Investment Position[6]	2021 Q1	Jun 30	Q	Q	Q

[1] Daily (D), Weekly (W), Biweekly (B), Monthly (M), Quarterly (Q), Annually (A); NA: Not Available.
[2] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[3] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[4] Foreign, domestic bank, and domestic nonbank financing.
[5] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

Statement by Ms. Shortino, Executive Director, and Mr. Sturm, Advisor on United States
July 19, 2021

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

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

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

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

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

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

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

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

Monetary Policy

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

The FOMC has repeatedly emphasized that the path of monetary policy will be outcome dependent and that it will take into account a wide range of information, including readings on public health, labor market conditions, inflation pressures and inflation expectations, and financial and international developments. At present, inflation has risen, but it is widely recognized that recent inflation readings largely reflect transitory factors and base effects, including idiosyncratic supply and demand factors. Market- and survey-based measures of inflation expectations suggest the Fed's Flexible Average Inflation Targeting regime is working, and expectations are anchored around the 2 percent average inflation target.

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

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

Financial Stability

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

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

International Context

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

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

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

Climate Change

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

The Administration also recognizes that the financial system must be resilient to the risks from climate change, and the FSOC is making this a priority. FSOC members will coordinate domestic regulatory efforts to assess climate-related risks to financial stability, pulling together agency perspectives to assess how climate risks may impact the stability of the entire financial system. Specifically, the FSOC will work with its members to improve climate-related financial disclosures and other sources of data to better measure potentialexposures to climate-related risks. This will complement the work of the SEC, which is currently reviewing existing guidance on climate-related financial disclosures.

Inequality: A Cross-cutting Theme

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

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