Trends and Development of Fiscal and Monetary Policies of G7 Countries During the Post-Pandemic Era

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Abstract. This study aims to provide a comprehensive analysis of the fiscal and monetary policies enacted by the G7 countries in the post-COVID-19 era, and to investigate their impact on economic recovery. This research is set amid the global disruption during the COVID-19 pandemic, which compelled governments around the world to enact unprecedented measures to stimulate economic activity and prevent financial collapse. The objective of our research analysis is to assess the efficacy of these policies in promoting economic recovery while considering the diverse strategies adopted across the G7 nations. The primary research content revolves around a comparative evaluation of monetary strategies—such as interest rate cuts and quantitative easing—and fiscal measures—such as direct payments, loan guarantees, and tax deferments. This study primarily relies on data sourced from major global agencies and central banks, which serve to quantify the effects of these policies on key economic indicators, such as GDP growth, employment rates, and inflation. The study also takes into account recent forecasts from the IMF and OECD, offering a nuanced view of the prospects for economic recovery among the G7 countries. This analysis can be useful in providing a deeper understanding of the complexities involved in policymaking at a macroeconomic level. The analysis identifies notable disparities in the economic recovery rates across G7 countries, which can be attributed to the variations in the scale, scope, and nature of their fiscal and monetary interventions. Consequently, the study offers valuable insights into the requisite policy calibrations necessary for more targeted and effective economic stimulation.

Keywords: Fiscal Policy; Monetary Policy; Economic Recovery; G7 Countries; COVID-19.

1. Introduction

1.1. Background

The economic aftershock of the COVID-19 pandemic continues to linger. Policymakers are now tasked with the challenge of economic recovery after three years of global recession. Representing nearly 40% of global output [1] the Group of Seven (G7) countries play a pivotal role in the global economy. Although the aftershock of the virus has not yet fully dissipated, it is both timely and significant to evaluate the efficacy of earlier monetary and fiscal policies enacted in these countries and to predict the future economic course based on current measures.

Historically, the G7 countries have employed a blend of monetary tools, such as interest rate adjustments, and fiscal strategies like taxation and public spending to respond to systemic economic crises. Immediately after the collapse of the economy in 2008, global organizations such as the International Monetary Fund called for coordinated efforts from the central banks of the G7 countries to continue policy stimulus (International Monetary Fund, 2010). Central banks of Canada, the UK, Japan, the European Union, and the United States all acted swiftly to facilitate liquidity. The goal was to assuage the strain on financial markets and the effect on credit availability for consumers and businesses [2].

The COVID-19 pandemic introduced unique economic complications that were unprecedented and unparalleled in modern history. In 2020, the world economy contracted by 2.8%, while the G7 economies shrank by 4.5%. For comparison, in 2008 the global economy declined by 0.1%, and the G7 contracted by 3.4% [3]. The unprecedented economic turmoil requires fiscal interventions on a commensurate scale. Given the critical nature of these policy decisions, it is imperative to investigate their effects and address existing gaps. This essay sets out to offer insight into the long-term efficacy of monetary and fiscal policies across G7 countries.

1.2. Related research

Amid the unprecedented drop in global economic activity caused by COVID-19, governments have taken swift and extensive actions to support both households and businesses, leading to significant economic impacts [4]. Current literature offers a thorough assessment of the scale of monetary policies enacted by central banks during the pandemic. The scope of policies at the beginning of 2020 was significantly larger than during the 2008 crisis. The median fiscal intervention accounted for 5.4% of total output, compared to just 1.4% during the Great Recession [5]. G7 countries relied heavily on fiscal policies to ease economic pressure. Fiscal packages in the U.S. and Canada accounted for more than 10% of total output, while those in Japan, the United Kingdom, and Germany exceeded 8% [6]. Such interventions proved effective at the initial stage of the pandemic, countering effects on income and poverty rates [7].

These fiscal packages have been proven effective in the early phases, based on multiple research studies. According to Deb et al. [8], an analysis of the impact of various fiscal policies on the economy in 52 countries during 2020 suggests that fiscal policies effectively stimulated the economy, increased confidence, and lowered unemployment. The fiscal measures varied widely due to factors like existing economic safety nets, pre-pandemic fiscal capabilities, the severity of virus outbreaks, and specific policy goals. The commentary further supports these positions, stating that fiscal policies have generally boosted economic growth since the pandemic began, although the effect is expected to wane over time. Different components of fiscal policy, such as unemployment insurance and business subsidies, have varying impacts on GDP [9]. Another report from the IMF also highlights the effectiveness of these measures but points out that the diverse and costly nature of these interventions has led to increased public debt and calls for a long-term, sustainable plan [10]. Increased spending at both federal and provincial levels can be seen in G7 countries like Canada, and the federal government is expected to have a more significant long-term increase in spending levels [11]. Others voice concerns throughout these "temporary" fiscal measures, arguing that they are likely to result in a permanent increase in state power [12]. Additional concerns include the side effects of such policies, pointing to temporary inflation spikes and program inefficiencies [13].

In summary, the fiscal and monetary policies enacted by G7 countries to counteract the impact of the COVID-19 pandemic have had a generally positive effect on economic activity, alleviating economic pressure in the short term. However, as these interventions have been large in scale, they also raise concerns about their long-term sustainability, increasing public debt, and the potential for unintended consequences like inflation and inefficiencies.

1.3. Objective

The goal of this paper is to critically assess the fiscal and monetary policies enacted and implemented by the G7 countries in the post-COVID era. Drawing on current studies and research, this essay aims to gauge the effectiveness of these policies and explore their broader economic implications.

Based on the existing literature, this investigation aims to provide insight into several research questions. First, after almost 4 years of concerted efforts from the central government after the pandemic, how effective have the monetary and fiscal policies implemented by G7 countries been in facilitating economic recovery after the pandemic in the long run? And to what do specific fiscal measures, such as changes in interest rates or other particular stimulus packages affect the economy in terms of key factors including domestic output and employment rates? Secondly, what similarities and differences can be observed in the approach taken by the G7 countries? For instance, how do sizes and scopes of fiscal policies and stimulus packages compare among the G7 countries and are there recurring themes and trends in the monetary policies across these countries? Lastly, on a larger scale, what are the potential economic and social implications of these fiscal policies in G7 countries? Have these fiscal measures impacted income distributions and equality?

Given the inductive nature of this study, it will commence without any pre-formulated hypotheses. The intent is to observe patterns, generate insights, and possibly formulate theories based on the data collected. The research will be mainly exploratory and aims to provide a nuanced understanding of the complexities involved in monetary and fiscal policymaking among the G7 countries. Data used in this research will primarily come from major global agencies and central banks.

2. Development and Trends

2.1. Monetary Policies

The central banks of the G7 countries adopted multi-faceted approaches, including rate cuts, quantitative easing, and various specialized lending programs to provide liquidity and support to their economies. These actions were aimed at easing the financial conditions, ensuring the smooth functioning of markets, and facilitating the flow of credit, all to mitigate the economic impact.

The Bank of Canada (BoC) reduced its policy rate promptly in response to the financial upheaval, cutting 150 basis points to a quarter percent. Also, it initiated a quantitative easing program buying at least $5 billion per week of Government of Canada securities. It also expanded the eligible collateral for liquidity facilities and initiated various programs to support market liquidity. Meanwhile, the Federal Reserve of the U.S. also reduced the rate on a similar scale in basis points (150 points), bringing it down to a range of 0%-0.25%. It introduced a quantitative easing program with an unlimited scope to buy Treasuries and Mortgage-Backed Securities. Various facilities were established or re-established to facilitate the credit flowing to businesses and individuals, and the Fed also increased its currency swap lines with other major central banks. The Central Bank of England (BoE) cut its rate by 65 basis points and this response brought the Basis Rate to the lowest point in history (0.10%). BoE also increased its asset purchase program by £200 billion and introduced a Term Funding Scheme(TFS). TFS provides funding to businesses at a rate close to the Bank Rate. European countries and Japan took a slightly different approach in terms of their interest rates. The ECB left its deposit rate unchanged at -0.5%. It also initiated programs such as the Pandemic Emergency Purchase Programme which amounts to 750 billion euro for asset purchases, later increasing the total purchase volume to €1.1 trillion. Japan Bank of Japan (BoJ) ramped up its asset purchases, particularly of ETFs, doubling the annual pace from ¥6 trillion to ¥12 trillion. It also took additional measures to facilitate corporate financing [14].

2.2. Fiscal Policies

The fiscal response of G7 countries to COVID-19 was significant but varied widely in terms of GDP percentage and the types of programs deployed. From direct payments and unemployment benefits to business loan guarantees and tax deferments, a multifaceted approach was taken to alleviate any financial strains on individuals and businesses.

In North America, Canada allocated an estimated $100 billion (4.2% of GDP) in direct support. This includes Emergency Care Benefits, a one-time GST credit, and a temporary increase in Canada Child benefits [19]. A range of other measures, like business wage subsidies and deferred tax payments, were also introduced. Meanwhile, the U.S. committed $1.6 trillion (7.5% of GDP) in direct support, dispersed in three phases. This included direct payments to individuals, expanded unemployment insurance, and a massive $2.2 trillion for direct spending, loans, and tax relief measures. On the European front, Germany allocated €156 billion (4.5% of GDP) in direct support. An Economic Stabilization Fund was used to extend €200 billion in loans to companies in need. France, similarly, committed €45 billion (2.0% of GDP) in direct support, largely through cuts in social-security contributions and corporate taxes. Bank loans of up to €300 billion were also guaranteed to help businesses. Investing a comparatively smaller percentage, Italy earmarked €25 billion (1.4% of GDP) for direct support, targeting healthcare, workers, and businesses. A €340 billion credit line was set up to inject liquidity into the banking system. The UK also allocated the same percentage of its GDP into direct support, roughly mounting to £30 billion. Specifically, measures included a government loan guarantee scheme and grants covering 80% of workers' salaries if they are retained on the payroll. Japanese authority proposed a fiscal package of ¥56 trillion (10% of GDP). This was meant to cover direct cash support to households and other incentives to businesses impacted by the pandemic [15].

3. Development Post-Pandemic

In the most recent quarter, the macroeconomic landscape among the G7 nations displayed a complex divergence, with some countries outpacing others in GDP growth.

Expected updates to past GDP figures for a major member of the G7 are set to cast its economic rebound from the pandemic in a more positive context than previously thought. However, this recalibration still leaves some countries trailing behind their peers in terms of economic resurgence from pre-pandemic levels. Against this backdrop, recent forecasts from leading global institutions paint a picture of a tepid, globally uneven recovery, with some nations grappling with notably lower projected growth rates in the coming years.

As of the second quarter of 2023, in terms of economic recovery, the United States leads the group with a 6.1% increase in GDP compared to Q4 2019. Canada and Japan are closely aligned, showing gains of 3.5% and 3.4% respectively. The Eurozone yielded mixed results; it has grown by 2.7% overall, but there are disparities among its member states. Italy and France have seen increases of 2.1% and 1.7%. The United Kingdom, with a growth of 1.6%, has managed to rebound. Germany stands out for its tepid 0.2% growth [16].

The International Monetary Fund (IMF) predicted the G7 economies post-COVID; similarly Organization for Economic Co-operation and Development (OECD) also offered a cautious outlook on the pace of economic recovery. Released on July 25, the IMF report indicates that the global growth forecast has seen some improvement, though a recovery that is weak by historical standards. Their data forecasts U.S. growth at 1.8%, Canada at 1.7%, and Japan at 1.4%, while European economies like Italy, France, and the UK lag behind at 1.1%, 0.8%, and 0.4% respectively. Germany is the only G7 nation with a negative growth projection, at -0.3%. On the other hand, the OECD report from June 7 echoes similar sentiments of a tepid global recovery. However, it also highlights concerns about falling inflation rates due to higher interest rates and lower food and energy prices. According to the OECD, the U.S. is expected to grow at 1.6%, Canada at 1.4%, and Japan at 1.3%. Among European countries, Italy leads with a 1.2% growth forecast, followed by the Eurozone and France, both at 0.9% and the UK at 0.3%. Germany stands at a flat 0.0%, indicating stagnation. In summary, both organizations suggest that while there is economic improvement, the recovery is still fragile [17].

The U.S. and Canada have displayed the most robust economic recovery according to the real GDP changes, and both nations opted for aggressive monetary and fiscal policies. The sheer volume of U.S. spending, both in direct payments and in market interventions provided a solid foundation for economic recovery. Meanwhile, Canada's fiscal efforts were no less impressive. The aggressive policies seem to have paid off, but the long-term implications, especially inflationary risks, need to be closely monitored.

The situation in the Eurozone has been more complicated. Germany's tepid GDP change stands in sharp contrast to its enormous fiscal package. The ECB kept its deposit rate low and initiated a Pandemic Emergency Purchase Programme that was worth trillions of dollars, but the meager growth implies these measures may not be enough. France and Italy also lag, despite their fiscal packages that accounted for a significant proportion of their GDPs. This raises questions about whether the scale of intervention was adequate or if structural issues are at play. Similarly in the UK, despite a comprehensive furlough scheme and business loan guarantees, its less than moderate growth suggests that it is facing challenges that are not entirely fiscal or monetary. Japan has a significant fiscal package in place, amounting to roughly one-tenth of its GDP. Despite this, its slow recovery in real

GDP suggests that while the policies have avoided economic contraction, they have not matched the extent seen in North America. This could be due to Japan's other pre-existing economic conditions like an aging population and deflationary pressures, which often make monetary and fiscal policies less effective.

The divergence in economic philosophies between North American and European countries in the G7 is worth being further analyzing to understand the disparate outcomes in their fiscal and monetary policies. One of the most telling indicators of these contrasting philosophies is the size of the central government expenditure relative to GDP. In general, the United States and Canada have smaller central government expenditures as a share of GDP compared to their European counterparts. North American countries' central government spending accounted for only a third of the total GDP while European countries often amount to half. A smaller size of government often translates to more flexibility and the potential to implement bigger packages. In this context, governments in North America are often quicker to deploy aggressive fiscal measures, like tax cuts or direct stimulus payments, to boost economic activity.

Another noteworthy point is that while North American countries are generally believed to be more market-driven than their European counterparts, the fact that the U.S. and Canada have higher levels of Product Market Regulation (PMR) adds a layer of complexity to the analysis. PMR indicators are measures designed to gauge the extent and stringency of regulatory barriers in product markets, primarily within a country but sometimes across a set of countries (OECD). One possible explanation for the paradox of having both a smaller central government expenditure as a share of GDP and a higher PMR is that in North America, regulation is seen as a mechanism to facilitate market efficiency rather than to exert direct government control. Regulations may be targeted at leveling the playing field or creating more competitive environments, rather than directly intervening in the economy. The objectives behind high PMR in North America might also differ from those in Europe. While European regulations often aim for broad social goals like equality, sustainability, or social welfare, North American regulations might be more narrowly focused on economic objectives like promoting competition or preventing fraud. This higher level of PMR in the U.S. and Canada, therefore, doesn't necessarily contradict their smaller government size or their different approach to fiscal and monetary policy, but instead complements and complicates our understanding of these systems [18].

The varying economic performances and future projections of the G7 countries underscore the complex interplay of fiscal and monetary policies in pandemic recovery. Both IMF and OECD forecasts suggest that the road to full economic recovery remains long and full of challenges, with projections indicating tapering growth and even contraction for some. Therefore, a one-size-fits-all policy prescription is inadequate. Each country will likely need to adjust its monetary and fiscal levers based on unique national circumstances, global economic conditions, and ongoing pandemic-related uncertainties. The lessons here are multifaceted: fiscal and monetary tools are crucial but not foolproof, external and internal variables have considerable influence, and we must be cautious to prevent future economic imbalances as countries navigate the uncertain post-pandemic landscape.

4. Conclusion

In conclusion, our study offers an in-depth evaluation of the fiscal and monetary policies undertaken by G7 nations during the period of the COVID-19 pandemic. This analysis reveals a mixture of policy outcomes, which are characterized by varied degrees of economic recovery among the countries. North American nations generally show stronger recoveries, which appear to align with their aggressive fiscal and monetary measures. European countries, despite robust policy interventions, display more modest growth, leading to questions about the adequacy and efficacy of their strategies. Japan's case is particularly intriguing; despite a massive fiscal outlay, the nation's growth is moderate, suggesting that other economic conditions might be at play. Forecasts from global organizations like the IMF and OECD affirm this nuanced picture, pointing to a rather moderate and uneven global economic recovery in the upcoming years for the G7 countries. The overarching lesson that can be taken away from this study is that fiscal and monetary tools are vital but not universally effective; their impact varies significantly based on the specific economic conditions and challenges within each country. Consequently, a one-size-fits-all approach would be undesirable and less effective, underscoring the need for tailored strategies as nations navigate their complex, post-pandemic economic turmoil.

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