



# Estimating the output gap in real time: Top-down vs. bottom-up

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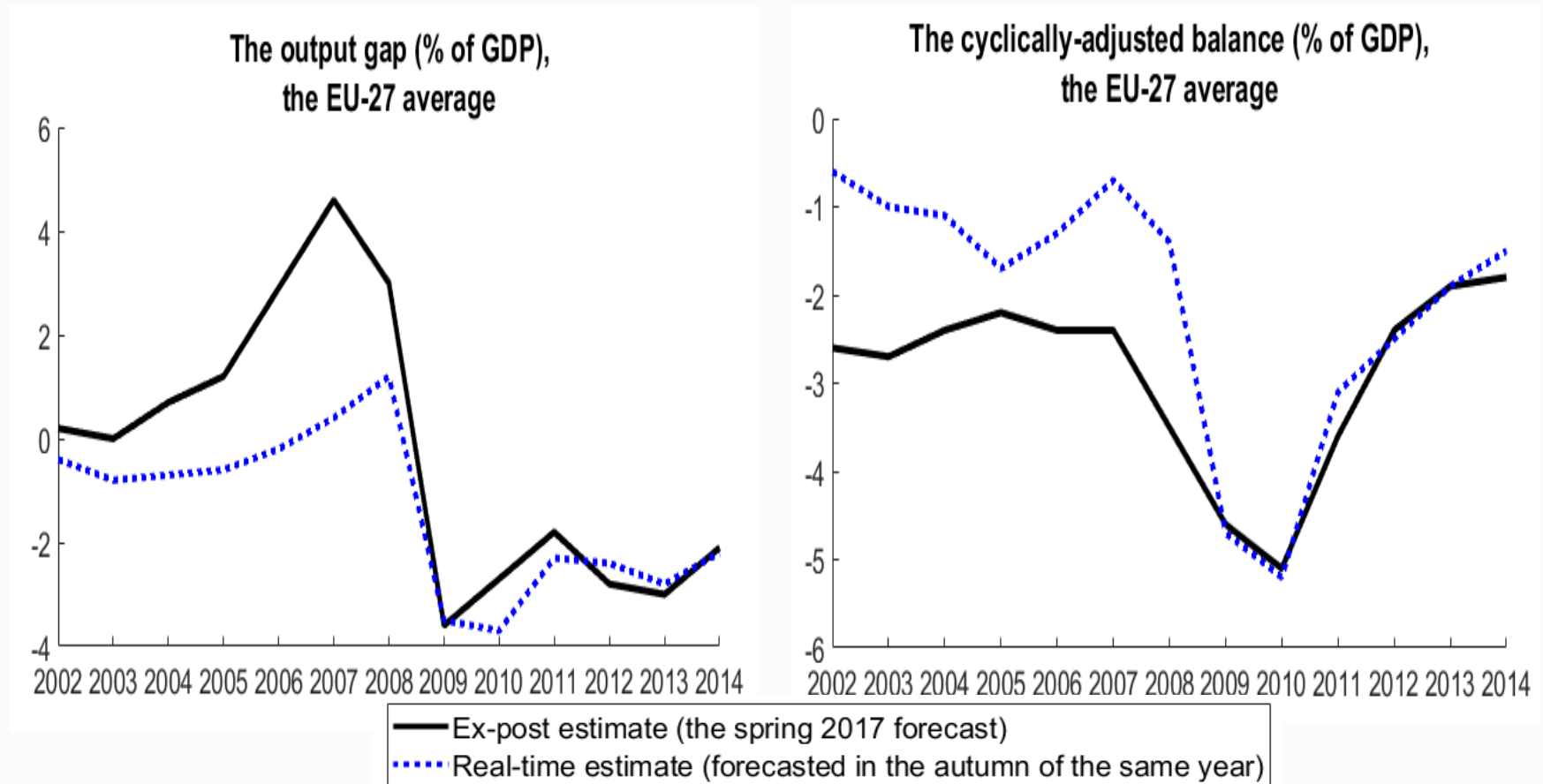
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# Real-time uncertainty affects the EU's key fiscal policy indicators

EC's real-time vs. ex post estimates of the output gaps.

Corresponding revisions of the cyclically-adjusted balance.



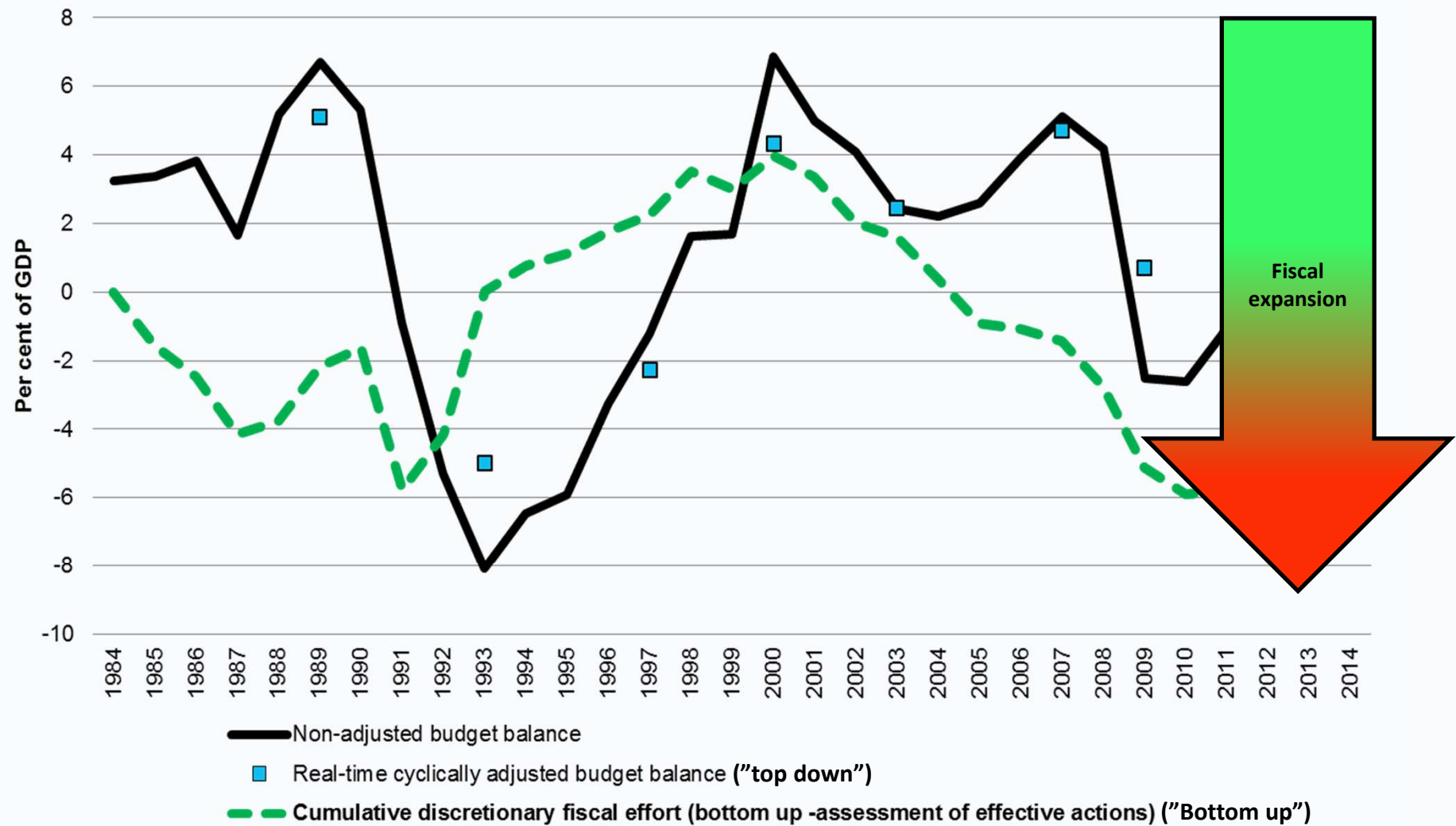
# Real-time uncertainty and fiscal policy - key findings

- Cyclically-adjusted indicators less useful, less countercyclical policy, higher cost of the business cycle.
- Unavoidable problems, but some remedies:
  1. Precautionary savings
  - 2. the “bottom-up” fiscal indicators**
  3. Anticipation of the fiscal policy feedback

# “Bottom-up” vs. “top-down” indicators

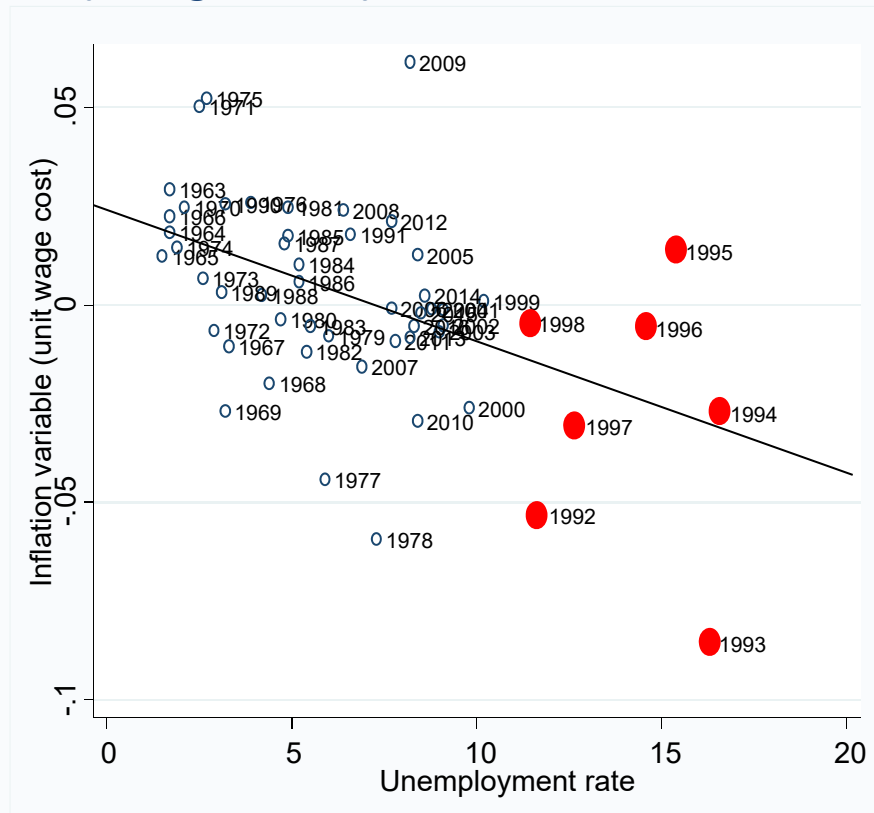
- How useful are the EU’s alternative structural balance (SB) indicators?
  - Case Finland 1984-2014, including the Finnish Great Depression of the 1990s (FGD).
- Methodological alternatives.
  - “Top-down”: SB based on the output gap and the elasticity of revenue and cost items (the Commission’s production function methodology).
  - “Bottom-up”: Expenditure growth net of discretionary revenue measures (actual decisions) compared to medium-term potential GDP growth (the bottom-up measures in the SGP)

# “Bottom-up” provides more countercyclical guidance

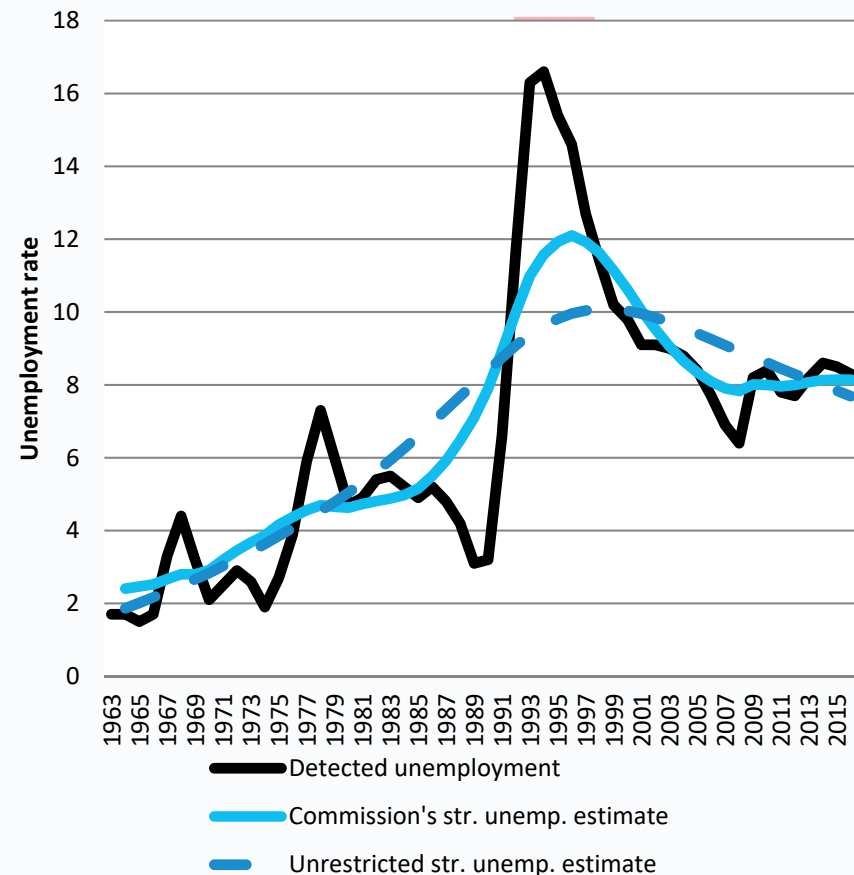


# A closer look on the "top-down" methodology: the structural unemployment

Inflation is a poor indicator of cyclical unemployment (during the FGD), and its use results in ...



high estimates of the structural unemployment that are amplified by parameter restrictions.



# Thank you for your attention!

## More details:

### The optimal fiscal policy.

- Kuusi (2017): Output gap uncertainty and the optimal fiscal policy in the EU. Firstrun deliverable 2.7.

### The EU's alternative fiscal indicators.

- Kuusi (2017): Does the structural budget balance guide fiscal policy pro-cyclically? Evidence from the Finnish Great Depression of the 1990s. The National Institute Economic Review, No. 239.

### The design of EU's medium-term fiscal plans.

- Kuusi (2017): Finding the Bottom Line: A Quantitative Model of the EU's Fiscal Rules and their Compliance. Firstrun working paper.