# EXECUTIVE SUMMARY

## Fiscal Policy under Uncertainty

Escalating uncertainty and substantial policy shifts are reshaping economic and fiscal outlooks. Major tariff announcements by the *United States*, countermeasures by other countries, are contributing to financial market volatility, deteriorating prospects, and heightening downside risks. Disinflation has stalled in many countries, and already disappointing growth projections have been significantly downgraded (see April 2025 *World Economic Outlook*), while financial turbulence poses considerable downside risks to growth (see April 2025 *Global Financial Stability Report*). Public finances were already strained, and debt levels were elevated in many countries. Heightened uncertainty regarding tariffs and economic policy, rising yields in major economies, and widening spreads in emerging markets—alongside increased defense spending, particularly in Europe, and a challenging foreign aid landscape—are further complicating the fiscal outlook. Fiscal policy now faces a sharper trade-off between reducing debt, building buffers against uncertainties and accommodating spending pressures, all amidst weaker growth prospects, higher financing costs, and heightened risks.

Fiscal projections are subject to considerable uncertainty given the swift escalation of trade tensions and high levels of policy ambiguity. Based on the April 2025 *World Economic Outlook* "reference point" forecast, global public debt is projected to rise by an additional 2.8 percentage points of GDP by 2025 and approach 100 percent of GDP by the end of the decade, surpassing the pandemic peak.[1] More than one-third of countries are expected to see debt increase in 2025 compared to 2024. Collectively, these economies represent about 75 percent of global GDP and include major players— *China* and the *United States*—as well as *Australia*, *Brazil*, *France*, *Germany*, *Indonesia*, *Italy*, *Mexico*, *Russia*, *Saudi Arabia*, *South Africa*, and the *United Kingdom*.

Risks to the fiscal outlook have intensified since the October 2024 *Fiscal Monitor*. Global debt-at-risk three-years ahead—a metric encompassing all risk determinants to the end of 2024—has increased by 2 percentage points of GDP. In a severe adverse scenario, global public debt could soar to around 117 percent of GDP by 2027, marking levels not seen since World War II and about 20 percentage points above projections for that year.

Debt levels may continue to rise as revenues and output decline due to higher tariffs and increasing uncertainty (April 2025 *World Economic Outlook*). Elevated geoeconomic uncertainties may further increase public debt by pushing up spending, particularly in defense, especially in *Europe*. Tighter and more volatile financial conditions in the *United States* may spill over into emerging market and developing economies, increasing financing costs and lowering commodity prices. Limited improvements in fiscal positions could further exacerbate the risks associated with rising interest rates, at a time when many nations are already grappling with substantial gross financing needs. Higher-than-expected interest rates could crowd out essential spending, including social benefits and public investment, while shortfalls in foreign aid further aggravate financing risks in low-income developing countries. Higher and persistent fiscal deficits in the *United States*, weaker-than-expected domestic demand in *China*, prolonged uncertainty, and stagnant productivity growth would further exacerbate fiscal risks.

[1] The estimates and projections are based on statistical information available through April 14, 2025, but may not reflect the latest published data in all cases. For the date of the last data update for each economy, please refer to the notes provided in the online World Economic Outlook database.

In this uncertain and challenging landscape, countries will need to first and foremost put their own fiscal house in order. A gradual fiscal adjustment, within a credible medium-term framework, is needed in most countries to reduce debt while building buffers against heightened uncertainty. Adjustments should balance the pace of debt reduction with economic growth, tailored to each country's specific circumstances, fiscal space, and overall economic conditions.

Countries with limited fiscal space should prioritize public spending and allow automatic stabilizers to operate fully. Those with room for fiscal maneuver facing significant spending pressures and public investment needs (for example, *Germany*) can utilize this space within well-defined medium-term fiscal frameworks. In the *United States*, substantial fiscal adjustments are necessary to put public debt on a decisively downward path, which will require building social consensus to address ongoing fiscal imbalances. More broadly, advanced economies with aging populations should reprioritize expenditures, advance pension and health care reforms, eliminate inefficient tax incentives, and broaden the tax base. For *China*, on-budget fiscal expansion should help support the economy and lower the current account surplus. Given higher tariffs and the unusually high uncertainty, some additional fiscal support is warranted. Low-income developing countries should stay the course on planned fiscal adjustment in light of financing challenges. For many emerging market and developing economies, rationalizing spending and increasing revenues through tax reform, broadening tax bases, and enhancing revenue administration remain critical priorities.

Medium-term frameworks and modern public financial management systems should anchor adjustment paths effectively and reduce fiscal policy uncertainty. Countries facing new spending needs, particularly in defense, must demonstrate commitment to maintaining the integrity of their own fiscal rules while ensuring transparency. Any permanent increase in fiscal outlays for investment and defense must be accompanied by enhanced spending efficiency, strengthened procurement systems, and improved multiyear fiscal planning and macroeconomic forecasting to ensure realistic assessments of their impacts on economic growth and fiscal positions. Furthermore, these increased outlays should be supported by credible and detailed financing plans that clarify how they will be funded. For countries in debt distress, timely restructuring and coordinated efforts to provide concessional financing are essential, particularly for low-income developing countries. International cooperation and coordinated initiatives to provide concessional financing are vital to prevent undue fiscal tightening, alleviate human suffering, and sustain development efforts in these nations.

The recent volatility in financial markets underscores the need for preparedness against severe economic disruptions. During times of financial instability, fiscal policy can play a crucial role in supporting central banks through direct lending, guarantees, and equity injections, which help mitigate deleveraging and restore confidence. If necessary, governments should provide timely, temporary, and targeted support to businesses and communities affected by significant trade dislocations, ensuring transparency and careful cost management. In cases where trade disruptions become permanent, implementing active labor market policies and skills retraining is essential, with fiscal policy facilitating this transition. Ultimately, maintaining fiscal discipline is vital; failure to do so risks turning fiscal policy from a source of stability into one of turmoil.

Advancing fiscal and structural reforms is essential for reigniting medium-term economic growth (Georgieva 2024) and mitigating growth-debt sustainability trade-offs. Well-designed tax and spending reforms can boost employment and investment. Improving the efficiency of spending—especially on health, education, and infrastructure—can increase an economy's productive capacity.

While fiscal structural reforms are crucial for generating fiscal savings and promoting inclusive growth, public resistance has historically hindered progress. Chapter 2 examines the factors influencing the social acceptability of major expenditure reforms (energy subsidies and pensions). The key finding is that sentiment regarding reforms from major stakeholders—including households, unions, civil society organizations, private sector entities, and opposition groups—plays a crucial role in advancing reforms, and their design is essential for acceptability and success. Building support among households, civil society organizations, unions, and opposition groups is key for advancing significant reform measures. The chapter also highlights that design, timing, and accompanying measures—particularly those alleviating impacts on affected groups—are critical for bolstering public support. Reforms are often considered in challenging macroeconomic environments, where larger, frontloaded measures may be necessary to stabilize the economy and gain public backing. In these circumstances, enhanced governance, trust, accompanying social transfers, and effective communication strategies are particularly important for fostering acceptability. Ownership and political commitment are also essential for building consensus and enhancing the credibility of reforms.