

Environmental Policy and Fiscal Consolidation

Topic: Modelling monetary policies

Author: Tobias Heinrich Kronenberg

Many governments are currently trying to reduce public expenditure and/or increase public revenue. Their focus on fiscal consolidation may come at the expense of environmental policy goals, for example in the case of environmentally motivated subsidies. This paper argues that fiscal consolidation can be reconciled with environmental policy if appropriate policies are chosen. Based on a literature survey it assembles a list of “win-win” options. These include, for example, the phasing-out of environmentally harmful subsidies. The effects of five selected policy measures are simulated using an applied general equilibrium model of the German economy.

For each policy measure, we consider the effect on the public budget, the macroeconomic impact (GDP, employment) and some environmental consequences (energy use, GHG emissions, material consumption). The results show that fiscal consolidation can go hand in hand with environmental policy, at least to a certain extent. The paper is partly based on a project commissioned by the Federal Environmental Agency of Germany.