



Economic Commentary

How would the Swedish economy be affected by a fiscal tightening in the USA?

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NR 9 2025, 23 October

Summary

The US federal government's debt-to-GDP ratio is near historically high levels. Many observers believe that the US debt trajectory is not sustainable. This Commentary estimates the spillover effects on Sweden of a hypothetical scenario in which the United States pursues a tighter fiscal policy to stabilise its debt. We find that Swedish GDP would be lower while inflation would be moderately affected. Spillover effects to the Swedish economy occur through the trade channel, via lower exports, and the financial channel and its effect on interest rates, exchange rates, stock markets and term premiums. The strength of the transmission to the Swedish economy would depend on several factors, such as the size and design of the US fiscal stimulus, the economic situation and the monetary policy response.¹

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¹ Economic Commentaries are brief analyses of issues with relevance for the Riksbank. They may be written by individual members of the Executive Board or by Riksbank staff. Staff commentaries are approved by the relevant head of department, while Executive Board members are themselves responsible for the content of the commentaries they write.

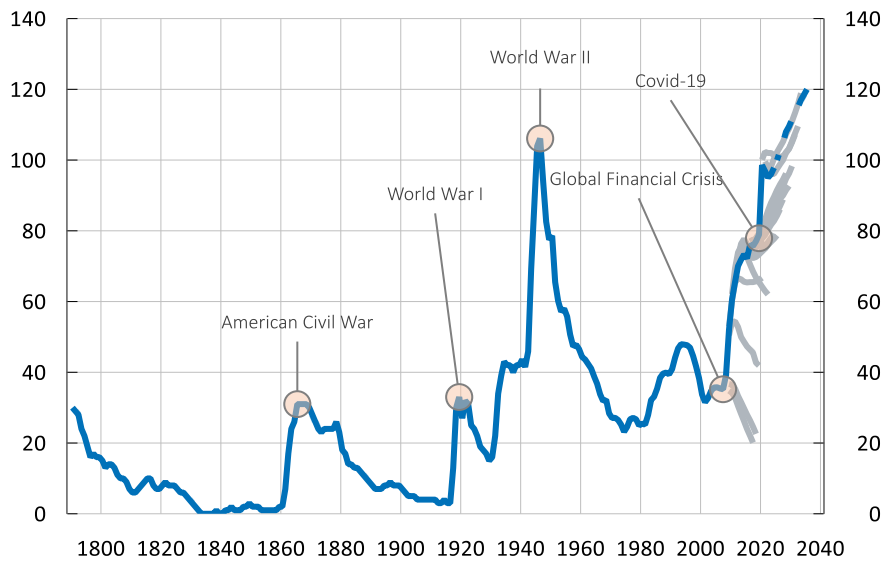
² The author wishes to express special thanks to Ingvar Strid for his assistance with simulations in the macroeconomic model MAJA. I would also like to thank Mikael Apel, Vesna Corbo, Mattias Erlandsson, Caroline Flodberg, Jens Iversen, Ingvar Strid, Anders Vredin and Anna Österberg for valuable comments.

Introduction

The US federal government debt-to-GDP ratio is close to historically high levels and may rise further going forward (Figure 1). The debt-to-GDP ratio has almost tripled to about 100 per cent of GDP since the turn of the millennium. This trend has been driven by budget deficits resulting from high pension and healthcare spending, but it has accelerated due to the costs of support measures related to the financial crisis and the pandemic. An ageing population, rising health care costs and high interest expenditure are expected to keep deficits high in the future.³

Figure 1. US federal government debt-to-GDP ratio

Per cent of GDP



Note: The dashed blue line shows think-tank Committee for a Responsible Federal Budget's (CRFB) projection of the debt-to-GDP ratio from August 2025. It includes the effects of the One Big Beautiful Bill Act (OBBBA) as well as tariffs and other regulatory changes decided until August. The grey lines show the CBO's 10-year projections of the debt-to-GDP ratio from 2007 to 2023.

Sources: CBO (2025), CRFB (2025) and Penn Wharton Budget Model (2023).

Many observers believe that the US debt trajectory is not sustainable.⁴ The US administration also has a stated ambition to reduce budget deficits and thereby stabilise the national debt.⁵ However, analysts are sceptical that the effects of the overall policies decided so far will lead to lower deficits (Figure 2). The special position of the United States in the global economy may also mean that lenders are more accepting of high US debt.⁶

³ See, for example, US Government Accountability Office (2024).

⁴ See, for example, CBO (2024a), Powell (2024), IMF (2024a), US Treasury (2024) and US Government Accountability Office (2024).

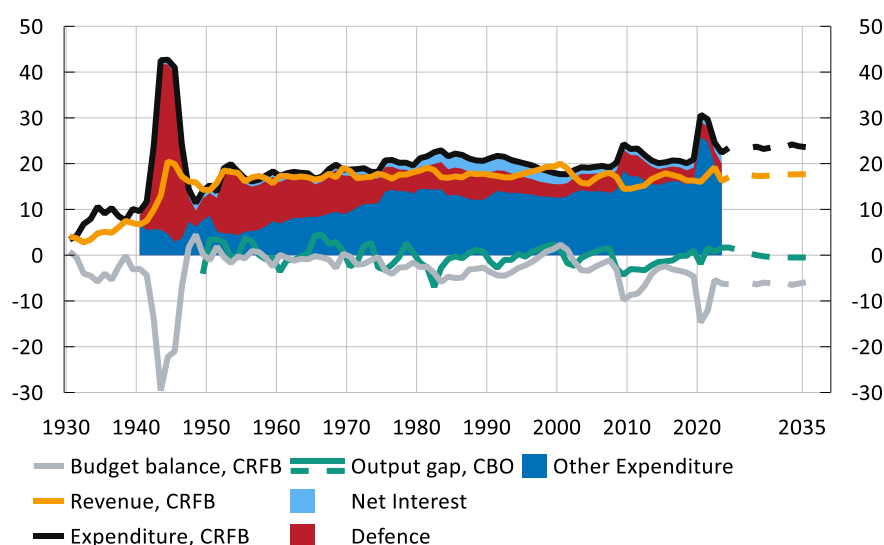
⁵ See, for example, Bessent (2025).

⁶ See, for example, Choi et al. (2024) and Arslanalp and Eichengreen (2023).

Overall, there is little evidence that the US budget deficit will decline significantly in the near term. However, an ever-increasing debt-to-GDP ratio is unsustainable in the long run, and sooner or later measures will have to be taken to stabilise or reduce the debt-to-GDP ratio. Significant action to reduce budget deficits in the United States would affect the US economy. Given the importance of the United States for Swedish exports, and its influence on global financial conditions, this in turn would have spillover effects on the Swedish economy. This Commentary aims to estimate the spillover effects on Sweden in a hypothetical scenario in which the United States pursues a tighter fiscal policy to address debt developments.

Figure 2. Federal revenue, expenditure and budget balance

Per cent of GDP



Note: The dashed lines refer to CRFB's August 2025 projection, see note to Figure 1 for information. Other expenditure consists largely of costs for Social Security, Medicaid and Medicare. Sources: CBO (2025), CRFB (2025), Office of Management and Budget and Macrobond.

The first part of this Commentary briefly describes the channels through which fiscal tightening in the United States could affect the Swedish economy. It then estimates the effects on the Swedish economy of a scenario in which the United States gradually consolidates its public finances, compared with a situation in which the United States does not tighten fiscal policy. The estimates are based on several structural models estimated on US data and on the Riksbank's general equilibrium model MAJA.

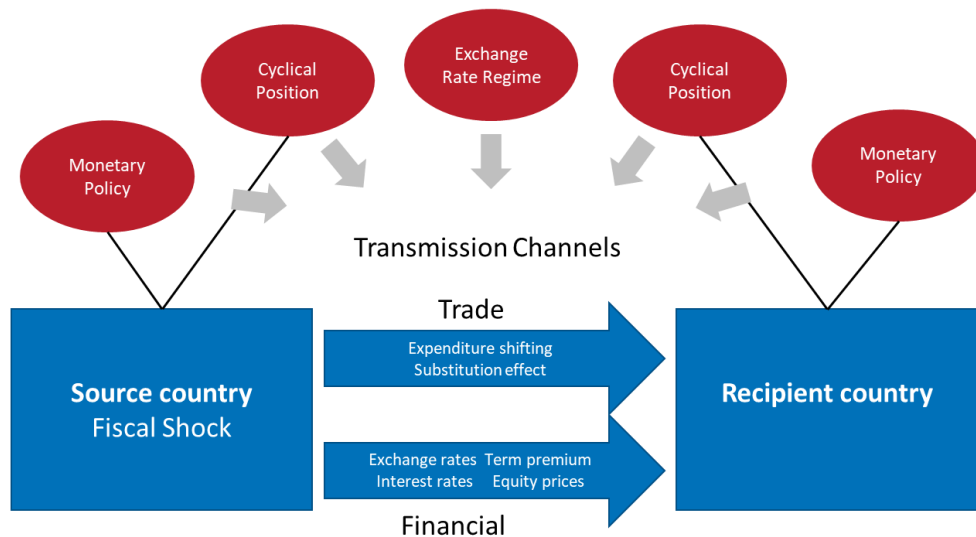
How is Sweden affected by changes in fiscal policy abroad?

Figure 3 shows a schematic diagram of how a fiscal policy change in a source country affects a recipient country in a standard macro model.⁷ Spillover effects go through two main channels: the trade channel and the financial channel. The size of the

⁷ The description of the transmission channels is based on IMF (2017) and focuses on the short-term and medium-term effects. We ignore here changes in tariffs.

effects is also influenced by several other factors, such as the monetary policy stance and the cyclical position.

Figure 3. Schematic diagram of the transmission of a fiscal policy change abroad



Source: IMF (2017)

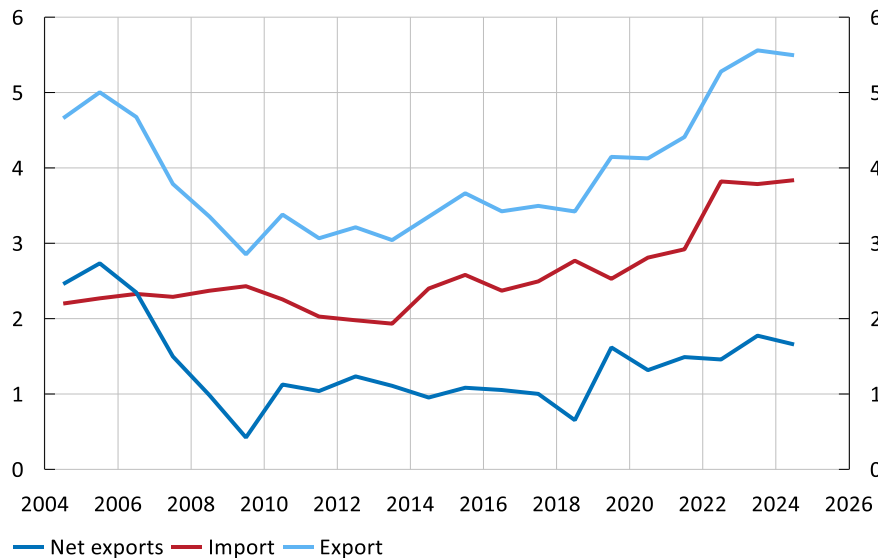
When the US tightens fiscal policy, Swedish exports are negatively affected via the trade channel. The tightening of fiscal policy in the United States reduces domestic US demand, leading, among other things, to lower demand for imports (the expenditure shifting effect). The share of the country of origin in the exports of the recipient country affects the size of this effect. Figure 4 shows that Swedish exports to the United States amounted to 5.5 per cent of Swedish GDP in 2024. In the same year, the United States was the country to which Sweden exported the most services and the third largest recipient of Swedish goods exports.⁸ Fiscal tightening in the United States could also lead to a weaker dollar, and thus a stronger krona.⁹ This has a negative impact on Swedish exports, as a weaker dollar can lead to the United States replacing imported goods and services with domestic American ones (the substitution effect).

⁸ See Camacho et al. (2025) for a description of Swedish trade with the United States.

⁹ In a Mundell-Fleming model, for example, fiscal tightening leads to lower interest rates, a depreciation of the nominal exchange rate in the country of origin and a dampening of domestic price pressures. This causes a real depreciation that dampens import demand in the country of origin, as foreign goods become more expensive.

Figure 4. Swedish trade with the United States

Per cent of GDP



Note: Refers to both exports of goods and services.

Source: Statistics Sweden.

Sweden is also affected by fiscal tightening in the United States via the financial channel and its effect on interest rates, exchange rates, equity markets and term premiums. Spillover effects via this channel can be both positive and negative for the Swedish economy, depending for instance on economic conditions and lender confidence in the US tightening plan. If the plan is deemed credible, tightening could lead to lower term premiums on US Treasury bonds. This in turn could have a stimulative effect on the Swedish economy via lower global market rates and higher asset prices. In this case, the financial channel would work in the opposite direction to the trade channel. If the tightening plan is not considered to be credible, it could instead lead to increased uncertainty and tighter global financial conditions, which would have a dampening effect on the Swedish economy.

The strength of each transmission channel also depends on other factors, such as the state of the economy and the monetary policy response in both the sending and receiving countries. The type of fiscal instrument also has an impact on transmission.¹⁰

What are the effects of fiscal tightening in the United States on Sweden?

The IMF has estimated that a fiscal consolidation equivalent to about 4 per cent of GDP is necessary to put the US debt-to-GDP ratio on a clearly downward trajectory.¹¹

¹⁰ IMF (2017).

¹¹ See IMF (2024b), note that the IMF estimate is based on several assumptions, including unchanged fiscal policy rules.

Here we estimate the effects on the Swedish economy of a scenario in which the United States takes budget-strengthening measures of this magnitude.

The scenario has been calculated in three steps. As a first step, I have estimated the impact of fiscal tightening on the US economy (GDP, inflation and policy rate) using several structural models.¹² To simplify the modelling analysis, the entire US fiscal tightening is assumed to be achieved through lower government consumption.¹³ Government consumption is assumed to decline by one-third of a per cent of GDP per quarter over twelve quarters (i.e. 4 per cent of GDP in total). The effects of the tightening on GDP, inflation and the policy rate in the United States are averaged across a large number of structural macroeconomic models estimated on US data.¹⁴ The average effects on inflation are small, which is in line with the literature on the effects of fiscal policy on inflation.¹⁵ In step two, we have calculated the spillover effects of the US fiscal tightening on the euro area economy, based on estimates from the IMF and others.¹⁶

In the final step, we estimate the spillover effects of fiscal tightening in the United States on the Swedish economy. This part of the calculation is done using the Riksbank's general equilibrium model MAJA, which is a model for Sweden, the euro area and the United States.¹⁷ The total effect consists of the direct effect, from the United States to Sweden, and the indirect effect, from the United States via the euro area to Sweden. In Figure 5, we show the estimated effects of fiscal tightening in the United States on Swedish and US GDP, inflation and the policy rate. Here the fiscal tightening implies a quarterly reduction in government consumption of one-third of a per cent of GDP over 12 quarters.

¹² The number of variables included has been limited to simplify the analysis. A larger set of variables would likely better reflect the full transmission of fiscal tightening, in particular through the financial channel.

¹³ An actual fiscal consolidation would likely consist of tax increases and spending cuts in a variety of areas. CBO (2024b) summarises possible measures to reduce the budget deficit. The composition of a fiscal tightening has an impact on both the effects on the US economy and the international spillover effects. See, for example, the Penn Wharton Budget Model (2024) for an estimate of the long-term effects on the US economy of a package of tax and spending reforms.

¹⁴ These structural models have been compiled in "The Macroeconomic Model Data Base" (MMB version 2.3, www.macromodelbase.com), see Wieland et al. (2016). The calculation uses the average of the effects of a fiscal shock on US GDP, inflation and the policy rate from 36 different models, estimated on US data. In the models, a fiscal shock is defined as an increase in discretionary government expenditure. Based on the findings of Ben Zeev et al. (2023), the effects are assumed to be symmetrical for a reduction in expenditure. For all models, it is assumed that the policy rate (i_t^z) is set according to the policy rule as specified in Smets and Wouters (2007), where $i_t^z = 0,81i_{t-1}^z + 0,93p_t^z + 0,97q_t^z - 0,90q_{t-1}^z + \eta_t^i$ and p_t^z refer to quarterly annualised inflation, q_t^z refers to the quarterly GDP gap and η_t^i to a monetary policy shock.

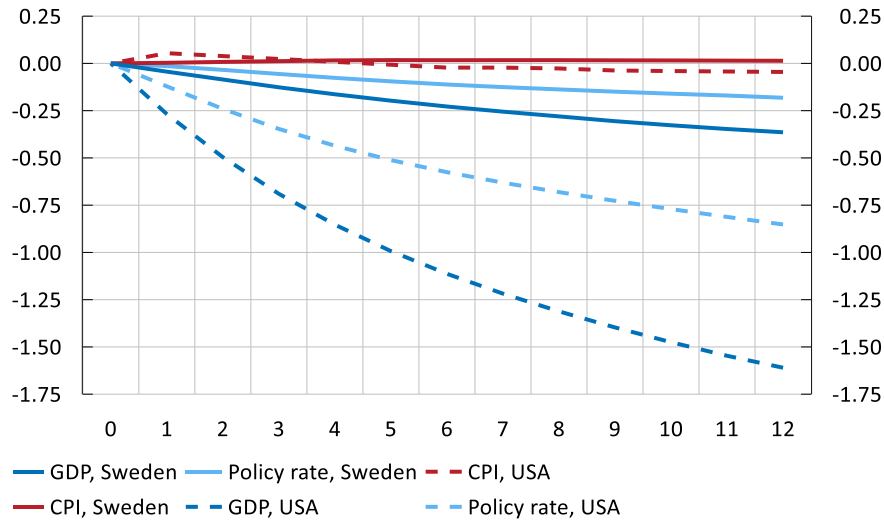
¹⁵ Many studies find small or insignificant inflation effects of a fiscal policy shock, see for example Jørgensen and Ravn (2022) or Checherita-Westphal and Pessoa (2024). Other studies show a greater impact of discretionary fiscal policy on inflation under specific circumstances, such as when it coincides with high resource utilisation and supply shocks, as was the case in the United States during the pandemic; see, for example, CBO (2023).

¹⁶ Spillover effects on euro area GDP are based on IMF (2017) and inflation is based on Hodge et al. (2022). The policy rate approximately follows a behavioural rule as specified in Smets and Wouters (2007).

¹⁷ See Corbo and Strid (2020) for a description of MAJA.

Figure 5. Estimated effect on the Swedish and US economies of a gradual fiscal tightening in the USA

Per cent and percentage points



Source: The Riksbank and own calculations.

In the scenario, lower international demand means that Swedish GDP will be just under 0.4 per cent lower after twelve quarters, compared with a situation where the United States does not tighten fiscal policy. About half of the impact on Sweden is due to the direct effect (from the United States) and half to the indirect effect (via the euro area). The weaker GDP development contributes to lower Swedish resource utilisation and a cut in the policy rate. The impact on inflation is much smaller than the impact on GDP.

To our knowledge, there are no comparable studies that estimate the spillover effects of fiscal tightening in the United States on Sweden. Compared to studies estimating the spillover effects of a US fiscal shock on the EU, our results indicate that a US fiscal shock would affect Swedish GDP slightly more than the EU as a whole.¹⁸ A contributing factor to this could be a greater degree of openness in the Swedish economy, which reinforces the importance of the trade and exchange rate channel.

Concluding discussion

This analysis estimates the impact on the Swedish economy in a hypothetical scenario where fiscal policy in the United States is gradually tightened to stabilise the federal debt-to-GDP ratio. However, the actual effects of fiscal tightening in the United States on Sweden could differ from those estimated here if the economic circumstances are markedly different from those assumed, for example in terms of the monetary policy response and the economic situation in both the source and the recipient country.¹⁹ It should also be noted that, in principle, a country with its own currency can also

¹⁸ For example, compared to IMF (2017).

¹⁹ Warmedinger et al. (2015), for example, discusses how the macroeconomic effects of a fiscal tightening depend on the economic circumstances, so-called state-dependency.

address public finance challenges by having the central bank override the price stability objective and focus instead on financing the budget deficit.²⁰ Such a development would be likely to lead to higher inflation, rising term premiums and international spillover effects.

²⁰ See, for example, Carter and Mendes (2020) and Agur et al. (2022).

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