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Restraining Yourself: The Implications of Fiscal Rules for Economic Stabilization

| Published: 01 March 1995

| Volume 42, pages 32–48, (1995) [Cite this article](#)
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Abstract

State budgets played a significant macroeconomic role in the United States during the 1970s and 1980s. Their cyclical responsiveness was affected by the severity of statutory and constitutional fiscal restraints. Moving from no fiscal restraints to stringent restraints lowered the fiscal offset to income fluctuations by roughly 40 percent. Simulations indicate that a reduction in aggregate fiscal stabilizers of this size could lead to a significant increase in the variance of aggregate output.

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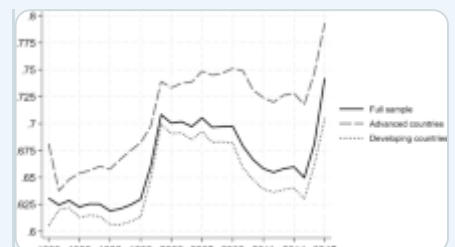
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Cite this article

Bayoumi, T., Eichengreen, B. Restraining Yourself: The Implications of Fiscal Rules for Economic Stabilization. *IMF Econ Rev* **42**, 32–48 (1995). <https://doi.org/10.2307/3867339>

Published

01 March 1995

Issue date

01 March 1995

DOI

<https://doi.org/10.2307/3867339>

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