Discussion of
Chapter 6: Reducing Debt Short of Default

By Tom Best, Oliver Bush, Luc Eyraud, and Belen Sbrancia
Discussion by Margaret M. Jacobson
Indiana University

Sovereign Debt: A Guide for Economists and Practitioners
International Monetary Fund
September 14, 2018

Summary

- **Question**: how can governments reduce public debt?
- Paper focuses on strategies available to governments who have decided to reduce debt-to-GDP
- *Does not* focus on:
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- **Contribution**: synthesize the trade-offs and effectiveness of debt reduction policies
  - Relies on economic research, outcomes of episodes
  - Conclusions: debt reduction policies can be costly

    $\Longrightarrow$ dampen short run growth, fuel political headwinds

Findings

- Change in public debt-to-GDP:

$$\Delta d_t = \frac{1}{1+g_t} \underbrace{(i_t - \pi_t - g_t)}_{\substack{\text{Interest-growth} \\ \text{differential}}} d_{t-1} + \underbrace{pb_t}_{\substack{\text{Primary} \\ \text{balance}}} + \underbrace{sfa_t}_{\substack{\text{Stock-flow} \\ \text{adjustment}}}$$

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- Monetary policy: moderate/temporary surprise inflation works best
- Financial repression: effective in an era of favorable growth, inflation, & negative real interest rates

Comments

- Accessible, well thought out, comprehensive yet nuanced
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- Clear focus, contribution
- Appeals to simple, standard models and frameworks
- Incorporates both model based and empirical evidence

Suggestions

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  - What worked to reduce debt? Costs vs. benefits
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  - Chari et al. (2018): only optimal without commitment, reduces default temptation when debt held by banks
  - Scheer et al. (2017, fig. 2): declining debt-to-GDP exerts downward pressure on inflation and output

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