Discussion of
Chapter 6: Reducing Debt Short of Default

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Discussion by Margaret M. Jacobson
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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:
  - Safe levels of debt, *when* debt reduction is warranted
  - Strategies to avoid high debt levels
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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 ➞ dampen short run growth, fuel political headwinds

Best, Bush, Eyraud, and Sbrancia (2018)
Findings

Change in public debt-to-GDP:

\[
\Delta d_t = \frac{1}{1 + g_t} (i_t - \pi_t - g_t) d_{t-1} + pb_t + sfat
\]

- Interest-growth differential
- Primary balance
- Stock-flow adjustment

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- **Fiscal consolidation:** direct, requires careful policy design
- **Growth-enhancement:** small increases have a sizable impact, hard to achieve growth accelerations
- **Monetary policy:** moderate/temporary surprise inflation works best

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■ Fiscal consolidation: direct, requires careful policy design

■ Growth-enhancement: small increases have a sizable impact, hard to achieve growth accelerations

■ Monetary policy: moderate/temporary surprise inflation works best

■ Financial repression: effective in an era of favorable growth, inflation, & negative real interest rates

Best, Bush, Eyraud, and Sbrancia (2018)
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Comments

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

- This paper: top down
  - What worked to reduce debt? Costs vs. benefits
- Discuss bottom up (Mauro, ed, 2011)
  - Success rate of debt reduction policies?
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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


