

Impact of Macroeconomic, Political, and Institutional Factors on the Structure of Government Debt in the Emerging Market Countries

Discussion

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SNB-CEPR Conference
Foreign Currency Related Risk Taking by Financial
Institutions, Firms and Households

Overview of the paper

- ▶ This paper aims to identify the determinants of various dimensions of the debt structure of emerging market economies.
- ▶ The analysis is based on a novel dataset on central government debt covering 19 emerging markets from 1980 to 2005. The availability of time-series data for different cross-section units naturally calls for panel data estimation.
- ▶ The main message of the paper is that macroeconomic volatility, political instability and poor institutions hinder the development of the domestic debt market. The author also concludes that domestic original sin is on the way out partly as a result of stable policies and lessons learned from previous debt crises.

General remarks

- ▶ The paper addresses very important issues. The sequence of emerging market crises at the turn of the century has taught us that the structure of public debt - notably its maturity and currency denomination - is a good indicator of the likelihood and the depth of crises. These crises have led us to consider not only external debt as a source of vulnerability, but also domestic debt.
- ▶ The paper follows a very clear structure and is highly readable (thank you!). However, it is probably a bit imbalanced. The sections on the data and the results are sometimes too short, while the section presenting stylized facts is rather long. The paper may benefit from some rebalancing, with relatively less attention on the stylized facts.

Explanatory variables

- ▶ Several explanatory variables take the form of indices: inflation stability, exchange rate stability, or political stability. These indices sometimes encompass more than one specific variables. As such, they have limited practicability for policy recommendations. Why not controlling directly using some macro variables (say nominal exchange rate volatility)?
- ▶ The relationship between some explanatory variables and the structure of debt is unclear. How exactly does the quality of bureaucracy affect the structure of public debt? Isn't the rule of law a key determinant? Isn't there a way to test more directly the importance of politics: government duration, elections, etc.

Explanatory variables

- ▶ Can we exclude external determinants? The dependent variable is defined so that the residual share is a well-defined concept. The residual of the share of domestic debt in total debt is therefore external debt. These two concepts are, in a way, two sides of the same coin! And since external factors affect the share of external debt in total debt, don't they also, by the definition of the dependent variable, affect the share of domestic debt in total debt?

Methodology

- ▶ In order to limit multicollinearity among regressors, one proxy from each category of regressors is chosen. This approach is largely arbitrary and estimation results may depend on the particular proxy chosen. I would suggest to use a general-to-specific approach, first including all explanatory variables and then using simple F tests to narrow down the specification. This is both more transparent and addresses the concern about multicollinearity. Moreover, this approach can be used for each of the dependent variables in turn; the effect of each regressor may differ across different dimensions of the structure of debt.

Methodology

- ▶ The motivation for using a censored Tobit model is that some countries do not issue DLTF debt in certain years. Thus, there are a lot of zeros for the dependent variable! But if the dataset consists of *stocks* of debt for each year, a zero does not mean no issuance of debt... but a zero stock of debt! Does the dataset provide information on issuance or the stock of debt?

Endogeneity and interpretation

- ▶ The paper does not address the issue of endogeneity. Some aspects of the structure of debt may affect macroeconomic volatility, and possibly political stability. The maturity and currency denomination of debt are two indicators of emerging market vulnerability. Beyond the standard statistical problems of bias and inconsistency, endogeneity also complicated the interpretation of the results.
- ▶ When endogeneity is an issue, can we confidently conclude that original sin is on the way out as an outcome of successful macroeconomic policies? What if both macroeconomic stability and the disappearance of original sin were caused by the recent benign international financial conditions? Could original sin come back now... even if stable macro policies persist?