# Discussion: "Sovereign Debt Overhang ... " by Tamon and Hyungseok

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# Executive Summary


**Empirical Contribution:**

Compile an impressive dataset on public expenditures for emerging economies.

Understand public expenditures during debt restructuring episodes.

→ Public investment shows **U-shaped** dynamics.

→ In contrast, public consumption & transfers a quick **v-shaped** recession.

→ **U-shaped** dynamics in public investment linked with delayed restructurings.

# Executive Summary (contd.)

**Theoretical Contribution:**

Authors propose a rich sovereign default model with **public capital and expenditures** and renegotiation.

→ If capital is low, sovereign delays debt renegotiation after default.

→ Tight fiscal budget and exclusion leads to slow capital accumulation, which delays renegotiation.

Without access to international markets, no way to speed up capital accumulation.

→ Public capital induces three forces: *autarky*, *smoothing*, and **renegotiation**.

# Comments – Empirical

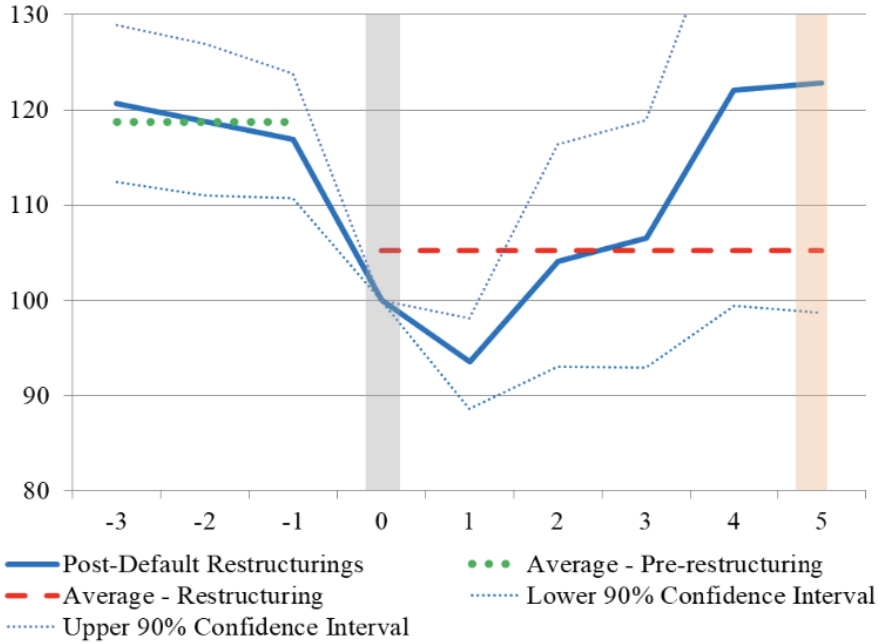
- No mention to **private capital**. How does it compare to public capital? More on this in theory comment.
- Many (most?) recessions are debt-crisis contractions (at least in Ecuador).

  Mention what countries are in non-debt crisis exercise. Are results statistically significant?
- More robustness checks in empirical section.

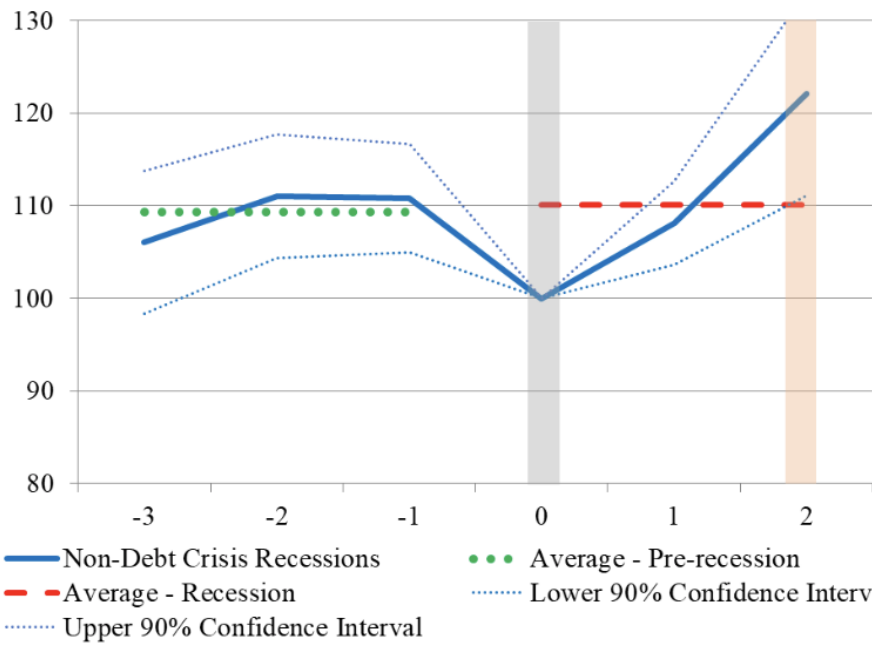
# Comments – Empirical (contd.)

Figure 1: Public Investment

(i) Restructurings

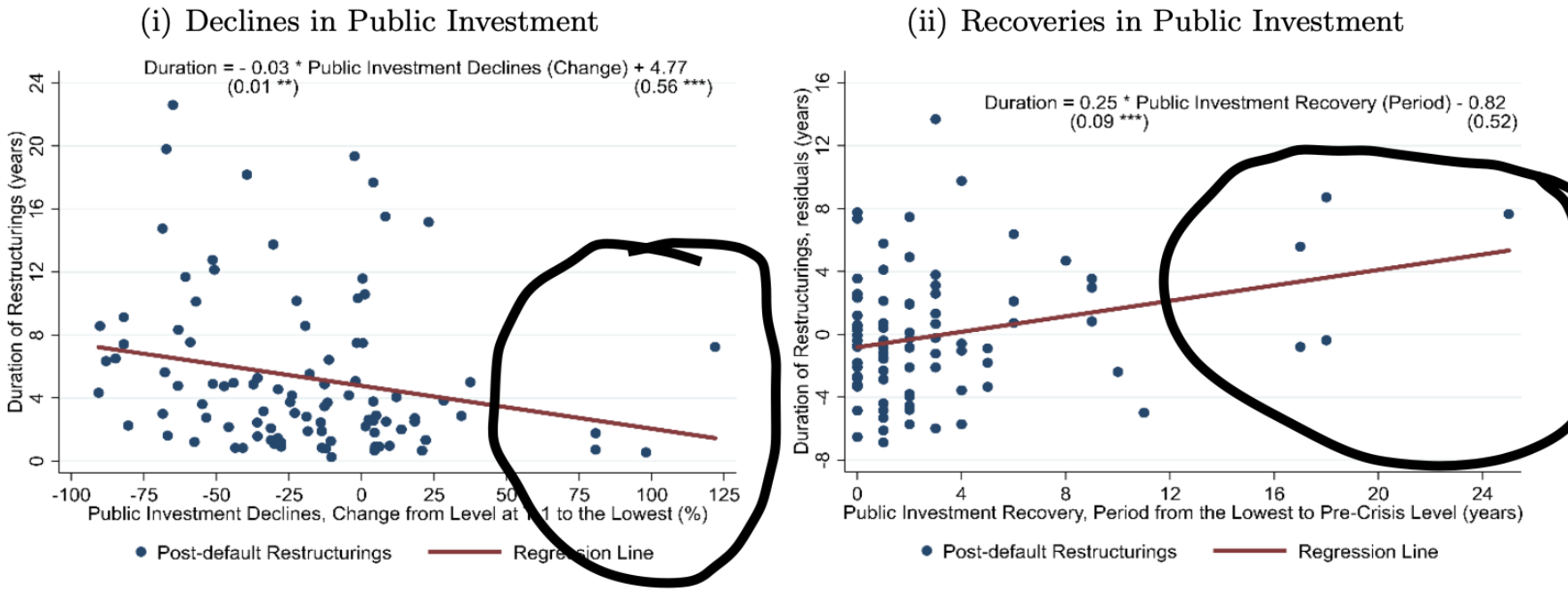



(ii) Non-debt Crisis Recessions



# Comments – Empirical (contd.)

Figure 4: Declines and Recoveries in Public Investment and Duration of Restructurings




- (Technical comment: Use Hamilton's filter.)

# Comments – Model


- What is role of public capital?
- In model, $k_t^g$ is input in production function

$$a_t \ell_t^{\alpha_l} \left(k_t^g\right)^{\alpha_k} \left(k_t^p\right)^{(1-\alpha_l-\alpha_k)}.$$

- Authors assume that public capital is **essential**. That is, $k_t^p = \left(k_t^g\right)^{\alpha}$.
- Simplifies model because $k_t^g$ is state variable.
- Is public capital the relevant variable for bond holders? Private capital is absent in calibration.

# Comments – Model (contd.)

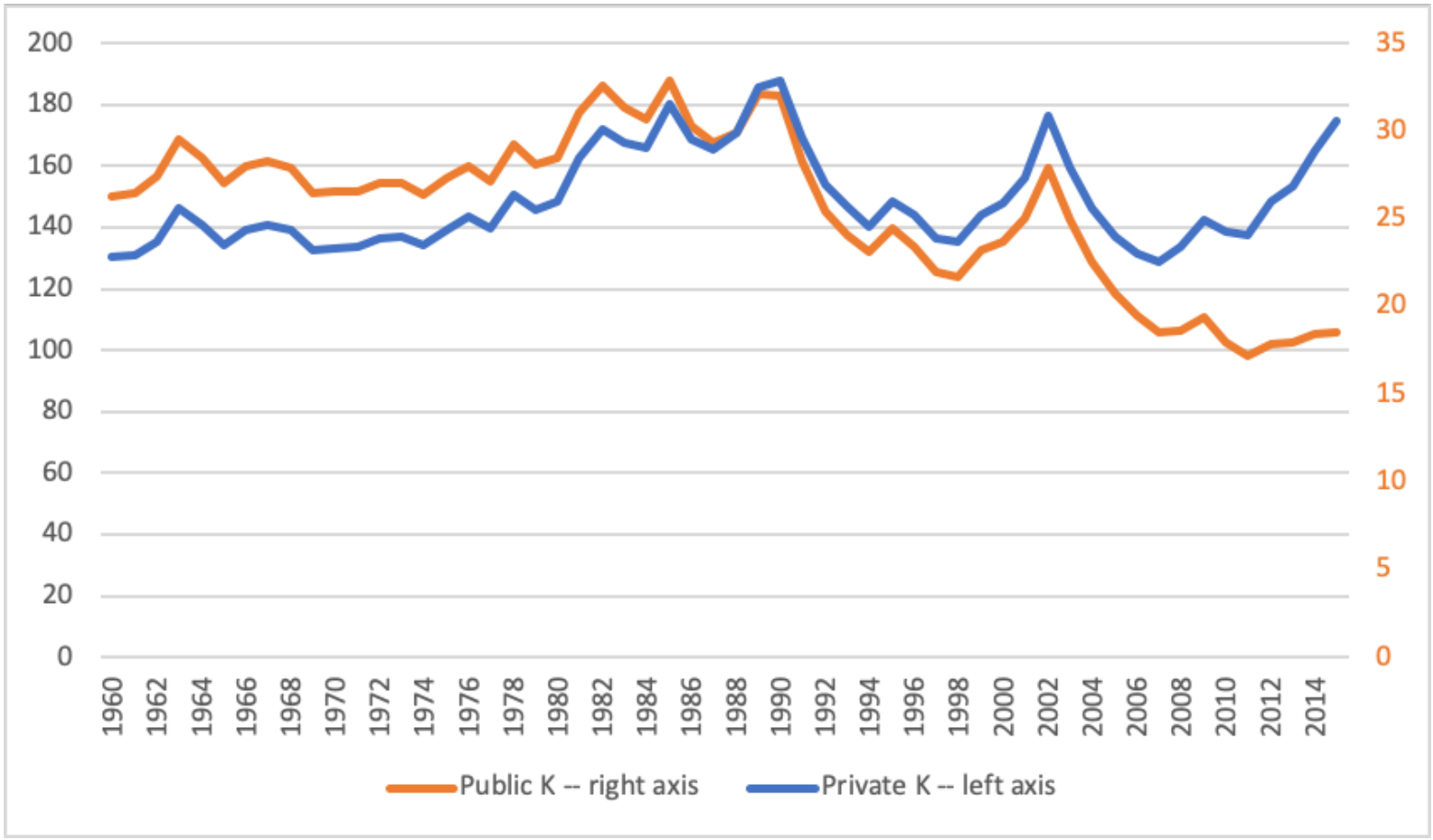



Figure: Capital as share of GDP

# Comments – Model (contd.)

- Public capital is also in the form of **schools, hospitals, parks, swimming pools, etc**.

  Hence, one could think of situations in which $k_t^g$ is part of utility: $U(c_t, \ell_t, k_t^g)$ or $v(g_t, k_t^g)$, or both.

- If we were modeling human capital accumulation, $k_t^g$ would be part of the production function of knowledge.

- Better to have one paper that studies on public capital in SOE with default?

- Then reintroduce renegotiation.