

CREI Lectures in Macroeconomics 2016

The Economics of Sovereign Debt and Default

Mark Aguiar
Princeton University



November 2-4, 2016 at 13:00
CREI, UPF Ciutadella Campus



Centre de Recerca
en Economia Internacional



Ramon Trias Fargas, 25-27
E-08005 Barcelona
Tel. (34) 93 542 13 88
Fax: (34) 93 542 28 26
crei@crei.cat
www.crei.cat



Centre de Recerca
en Economia Internacional

CREI Lectures in Macroeconomics

The Centre de Recerca en Economia Internacional (CREI) is a research centre sponsored by Universitat Pompeu Fabra (UPF) and Generalitat de Catalunya. It is located on the main UPF campus in Barcelona.

The CREI Lectures in Macroeconomics is a series of biennial lectures, with support from Princeton University Press. They are given by a “young senior scholar”, who has recently made a major, focused contribution to macroeconomics or international economics. The lectures will provide a high-level summary of recent work that has already had a large impact on the profession. Princeton University Press has agreed to publish a series of CREI Lectures in Macroeconomics.

Mark Aguiar

Mark Aguiar is the Walker Professor of Economics and International Finance at Princeton University.

Professor Aguiar received his PhD in economics from MIT in 1999. He began his academic career at the University of Chicago’s Graduate School of Business before moving to the Federal Reserve Bank of Boston in 2004 and then to the University of Rochester in 2006. He moved to Princeton in 2011.

Professor Aguiar’s research addresses issues in open- and closed-economy macroeconomics. Professor Aguiar has studied emerging market business cycles, sovereign debt, the political economy of capital taxation, and growth. His recent research on sovereign debt concerns self-fulfilling debt crises and equilibrium maturity choice. He has also investigated life-cycle consumption, time allocation, and trends in labor supply.

Professor Aguiar is co-editor of the *American Economic Review*. He has previously served on the board of editors for the *American Economic Review*, the *Review of Economic Dynamics* and *AEJ: Macroeconomics*. Professor Aguiar is a research associate at the National Bureau of Economic Research.

Some of his recent publications include:

- “Fiscal Policy in Debt Constrained Economies,” (with Manuel Amador), *Journal of Economic Theory*, January 2016, vol. 161, 37–75.
- “Coordination and Crisis in Monetary Unions,” (with Manuel Amador, Emmanuel Farhi, and Gita Gopinath), *Quarterly Journal of Economics*, November 2015, vol. 130, 1727–1779.
- “Has Consumption Inequality Mirrored Income Inequality?,” (with Mark Bills), *American Economic Review*, September 2015, vol. 105, 2725–2756.
- “Time Use During the Great Recession,” (with Erik Hurst and Loukas Karabarbounis), *American Economic Review*, August 2013, vol. 103, 5, 1664–1696.
- “Deconstructing Life Cycle Expenditure,” (with Erik Hurst), *Journal of Political Economy*, June 2013, vol. 121, 3, 437–492.

The Economics of Sovereign Debt and Default

The recent debt crisis in Europe has renewed interest in sovereign debt and default. The lecture series will present a general framework that allows one to explore the implications of limited commitment, incomplete markets, and impatience for debt dynamics and sovereign spreads. The insights gleaned from the analytical models will be related to the data as well as a standard quantitative model that has become a popular platform for analyzing the economics of sovereign default. These lectures are co-authored with Manuel Amador.

Lecture 1 This lecture will first lay out key empirical facts on default, debt dynamics, and bond spreads. A particular focus will be the extent to which “fundamentals”, such as output and global risk factors, are correlated with sovereign spreads. Aguiar will then present a general theoretical framework of a small open economy that will be used throughout the lecture series. The lecture will highlight the core assumptions regarding the operation of sovereign bond markets that distinguish different strands of the literature.

Lecture 2 This lecture will explore the incentives to borrow and save in the presence of limited enforcement. The focus will be on how equilibrium bond prices, provide an incentive for the government to

reduce debt. Aguiar will then explore the role of maturity in debt dynamics with a focus on the possibility of self-fulfilling crises due to the issuance of longer maturity bonds. Aguiar will discuss how the multiplicity introduced by longer maturity bonds runs counter to the conventional wisdom regarding the relative safety of longer maturity debt, and then highlight the novel policy implications for a lender of last resort that wishes to select the “good” equilibrium. At each stage of the analysis, Aguiar will also discuss calibration and computation of a quantitative version of the general model. The analytical results will then be compared to the equilibrium outcomes in the richer quantitative model.

Lecture 3 This lecture discusses the economics of maturity choice. Aguiar will introduce an analytical model of maturity choice and present a planning problem that highlights the relative efficiency of short-maturity bonds. The lecture will then show how the planning problem relates to maturity choice in a competitive equilibrium. The analysis will then be extended to an environment in which traditional rollover crises are possible. Using this framework, Aguiar will discuss how a sovereign trades the vulnerability of short-term bonds to runs against the efficiency properties of short maturities when “fundamental” defaults remain a threat.

The CREI 2016 Lectures will take place on November 2nd, 3rd and 4th, at 13:00, in the auditorium of Mercè Rodoreda building (room 23.S05), Universitat Pompeu Fabra, Ciutadella Campus, Ramon Trias Fargas, 25.

Due to limited seating availability, participants should register in advance with crojas@crei.cat