

# **Hierarchy and Sovereign Debt:** Crises and Consequences in International Capital Markets

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# *Poor Countries Face a Debt Crisis 'Unlike Anything We Have Seen'*

Dozens of countries that borrowed from private investors have debt payments coming due as their economies have crashed because of the coronavirus.

# Covid-19 and sovereign debt questions

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  - Default
  - Restructure or Relief
- What will be the consequences of debt outcomes?

## What are the consequences of debt outcomes?

- Exclusion from market
- Higher borrowing costs
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- Exclusion from market
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- Empirically: consequences are uneven and not as harsh as expected

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- Not all defaults are the same (Cruces and Trebesch 2012)

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- What about states' relationships with creditors?

# Argument

- U.S. supports to other states: an exchange
- Expectations for bailout (Aklin and Kern 2019)
- Inflow of aid

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- US wants stability: currency and politically

# Empirical Analysis

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- Four main tests:
  1. Pr(Debt crisis onset)
  2. Size of crisis
  3. Cost consequences
  4. Market exclusion

# Defining debt crisis

- Lots of measures of default
- Focus on debt restructuring events
  - Well-defined start/end dates
  - Well-defined outcomes: haircuts
  - 202 events since 1970 (Cruces and Trebesch)

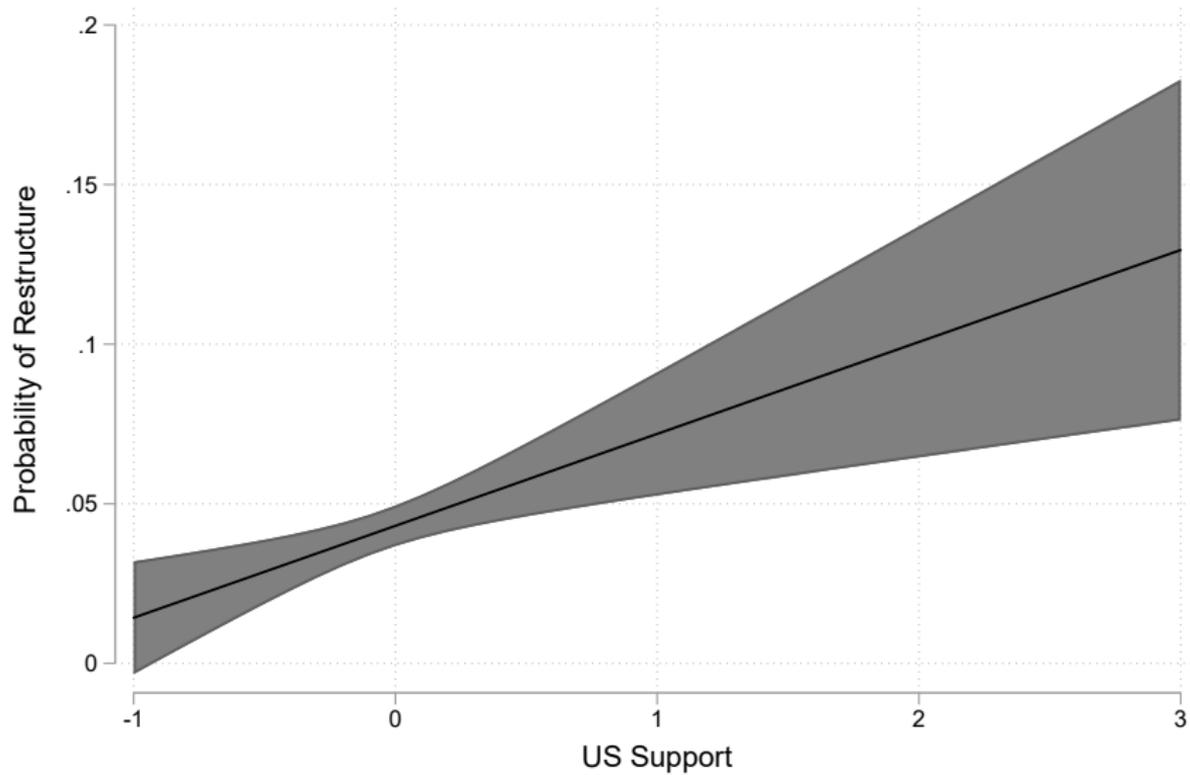
## US Support

- McManus and Nieman's (2019) Bayesian latent measure

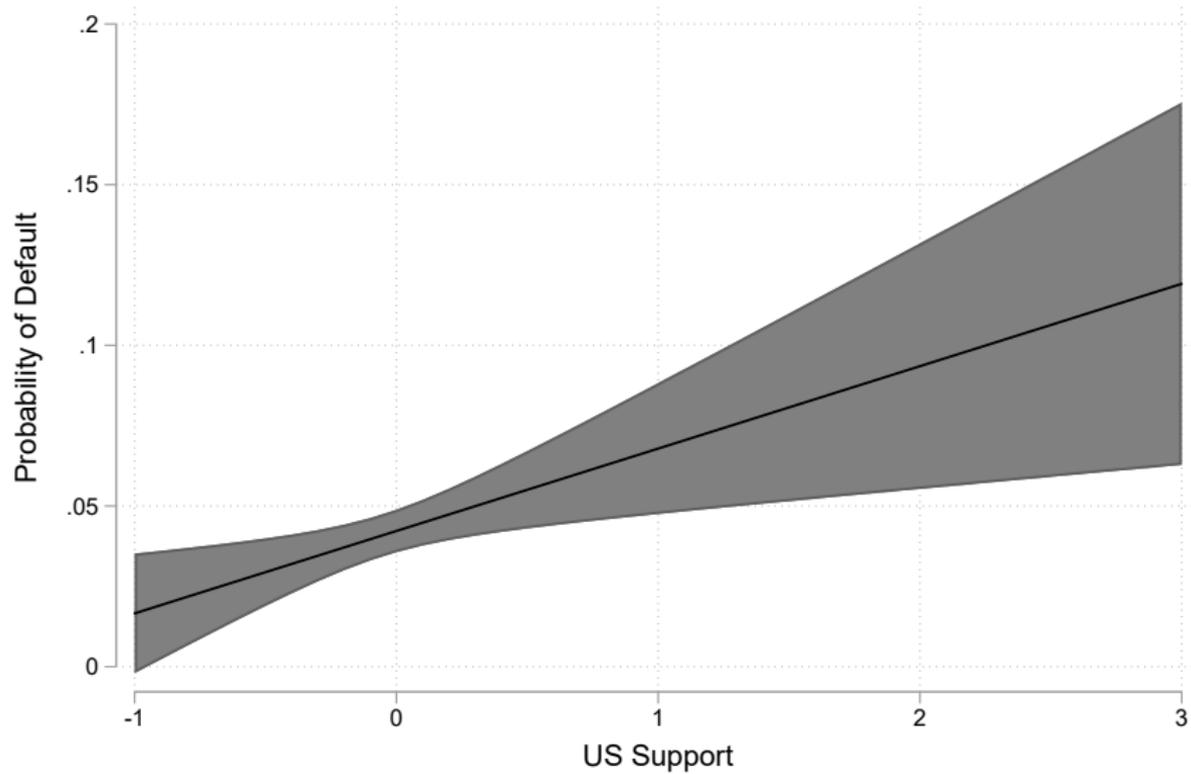
# US Support

- McManus and Nieman's (2019) Bayesian latent measure
- Control variables:
  - GDP, GDP per cap, oil rents, trade, institutions

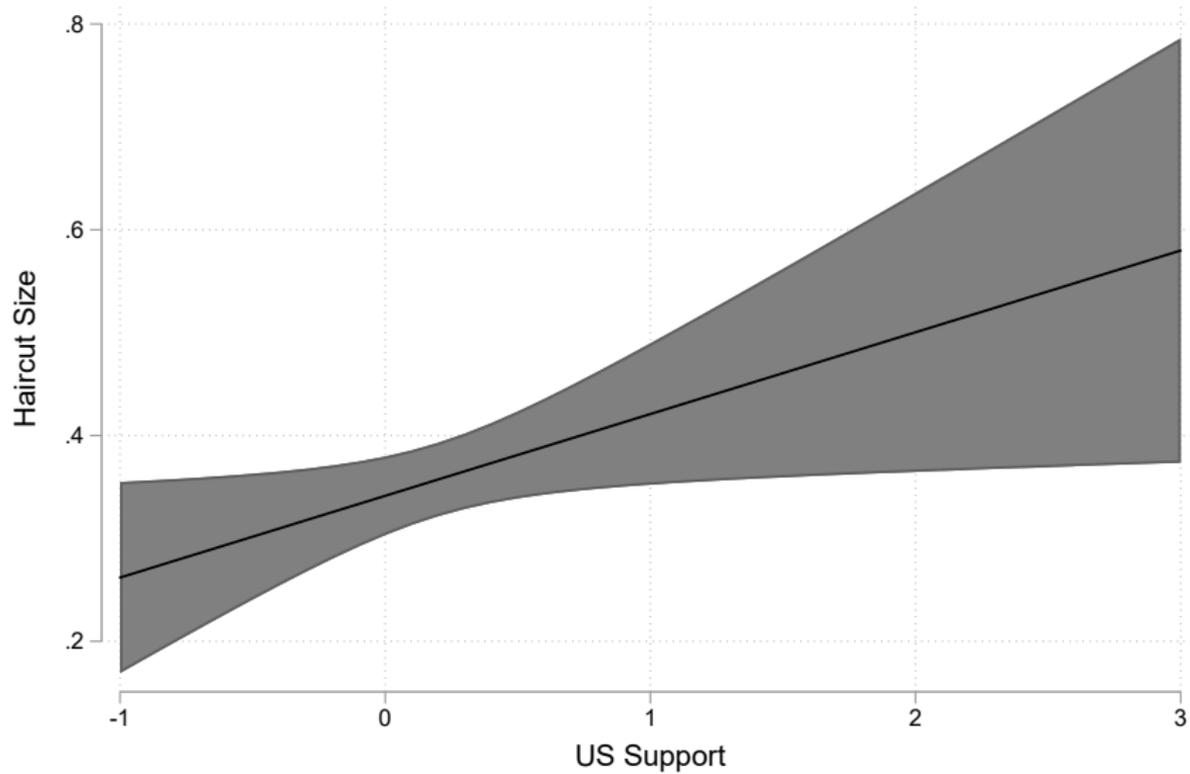
# Test 1



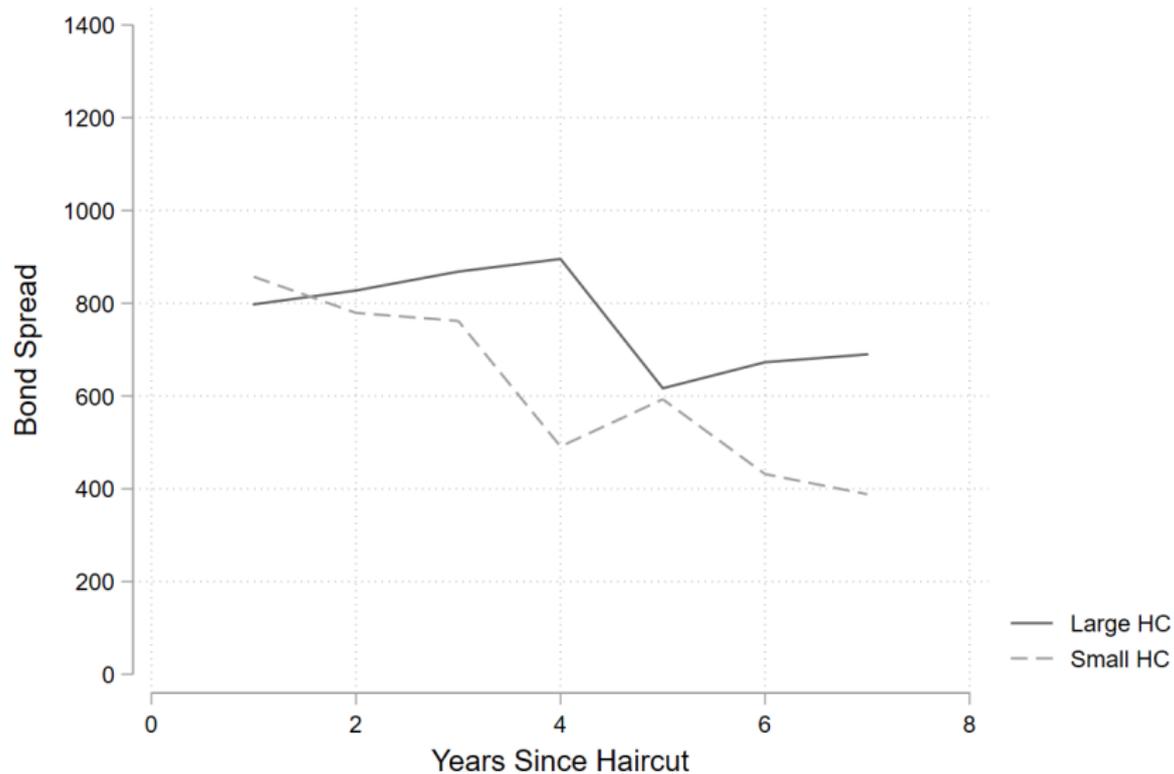
# Test 1a



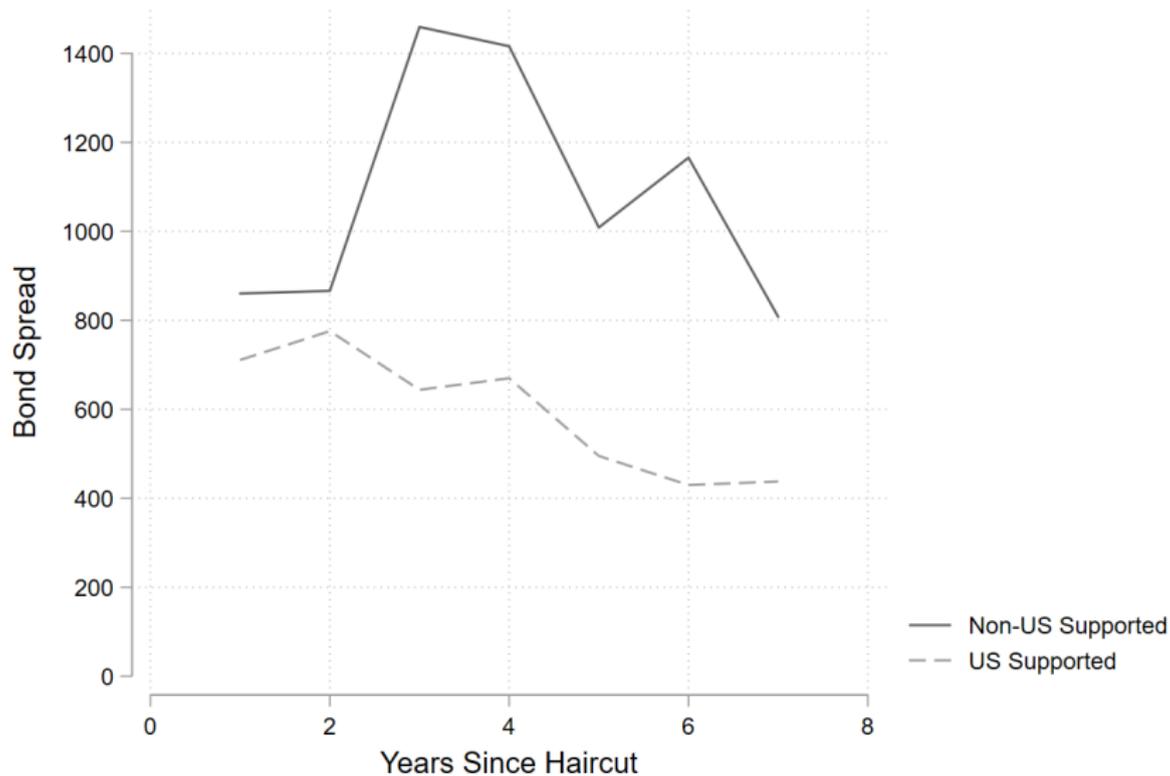
## Test 2



# Test 3



# Test 3: Bond spreads post-crisis



## Test 3

Table: US Support and Bond Spreads

	Full Sample (1)	Post Restructure (2)	Post Restructure (1-7 yrs) (3)
US Support	-142.886* (59.479)	-201.136* (36.412)	-194.300* (56.977)

## Test 4: Re-entry in bond market post-crisis (BMW data)

Table: US Support and Re-entry into Bond Market, Cox Model

	(1)	(2)
US Support	2.569*	2.621*
	(1.071)	(1.128)

## Further tests

- More aid? No\*
- Bailouts? Yes\*

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- Bailouts? Yes\*
- Stabilization of currency

## Discussion

- Bondholders stand to lose
- U.S. support aimed at currency stability
- Post-crisis focus on maintaining, increasing investment