

Non-technical summary of GDN RRC14 paper

Revisiting the Role of Public Debt in Economic Growth: the Case of OECD Countries

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The abstract

The paper empirically explores the factor of public debt which considerably changes the mechanism that transmits fiscal policy effects to economic activity in the short term. We empirically examine and determine:

- the turning point of debt-to GDP ratio;
- the impact of levels of indebtedness in public sector on current economic growth for a panel dataset of 36 countries (31 OECD member states and 5 non-OECD EU member countries).

The evaluation gives us an important understanding on the current indebtedness situation by determining the threshold values for our sample of countries, which indicates a possible non-linear and concave connection between indebtedness levels in the public sector and economic growth in the short term.

The sample is divided into subgroups distinguishing between:

- developed economies, covering the period 1980–2010; and
- emerging economies, covering the period 1995–2010.

To evaluate a possible negative correlation and concave functional form between public debt and potential economic growth, we employ a panel estimation on a generalized economic growth model augmented with a debt variable, while also considering some methodological issues like the problems of heterogeneity and endogeneity.

The results suggest that:

- at low levels of public debt the impact on growth is positive, whereas beyond a certain debt turning point a negative effect on growth prevails;
- the debt-to-GDP turning point is:
 - i. between 90% and 94% for developed economies;
 - ii. between 44% and 45% for emerging countries.

Therefore, we can confirm our hypothesis that the threshold value for the emerging economies is lower than for the developed ones in our sample.

Keywords: fiscal policy, public debt, economic growth, panel analysis, turning points, OECD.