

**Discussion of
“Sovereign Defaults at Home and Abroad”**

by Aitor Erce, Enrico Mallucci, and Mattia Picarelli.

Joao Ayres

Inter-American Development Bank

**IMF/ECB Workshop on Fiscal Policy and Sovereign Debt
April 2024**

Main goal of the paper:

- Stylized facts on external vs domestic debt restructurings.

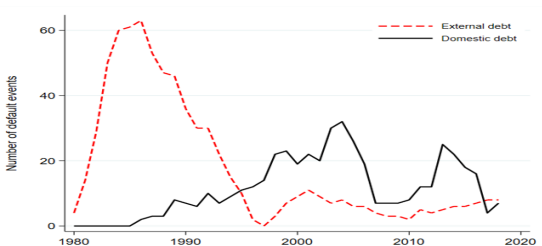
It explores two datasets:

- External restructurings: Asonuma and Trebesch (2016).
- Domestic restructurings: Erce, Mallucci, and Picarelli (2022).
- With some extra data work to make them comparable.

Main stylized facts:

- Defaults at home and abroad are equally frequent.
- Governments default selectively.
- External defaults are larger and take longer to resolve.
- Face value reductions are less frequent.
- Preemptive restructurings are becoming more frequent.
- Domestic defaults associated with larger creditor losses.
- Occur in different macro-financial and political environments.

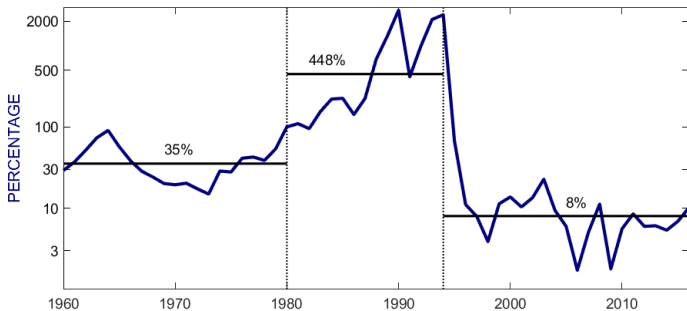
How much should we rely on historical averages?



- Are external and domestic debt restructurings equally frequent?
- Message: jurisdiction does not offset the incentives to default.
- How do the other stylized facts change over time?

How to think about default on domestic debt?

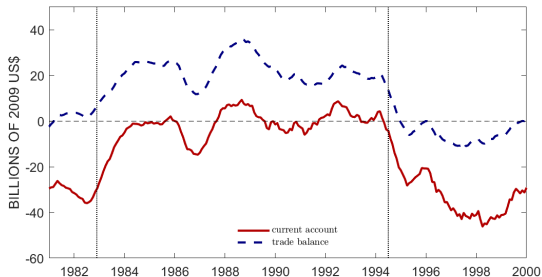
Figure: Annual inflation in Brazil



- There are many forms to (partially) default on domestic debt.
- Inflation was much higher in the 1980s (domestic default...).
- It explains the rise of inflation and currency indexation.

Domestic default and access to foreign capital markets

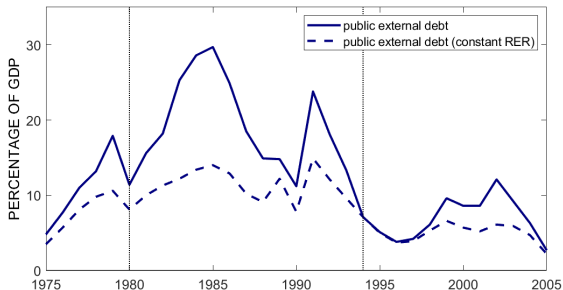
Figure: Current account and trade balance in Brazil



- In Brazil, the external debt crisis lasted from 1982 until 1994.
- The current account balance was around zero in that period.
- Domestic defaults not associated with large external adjustments.
- Should we expect the same with access to foreign capital markets?

RERs and the volume of restructured external debt

Figure: Current account and trade balance in Brazil



- What is the effect of real exchange rate (RER) depreciations?
- The depreciation increased the debt service in the 1980s.
 - What was the share of external debt in total debt service?
 - Did the jurisdiction of the debt matter in the 1980s?

Why focusing on the jurisdiction of the debt?

- What is jurisdiction in a model? The restructuring process?
- How far could we go with only different debt jurisdictions?
- Alternatives: currency denomination, residence of creditors.
- In practice, triple coincidence.

Debt heterogeneity (array of default options)

- Heterogeneity in external debt:
 - bank loans, debt securities, official debt, etc.
- But also heterogeneity within domestic debt instruments:

Table: Federal government debt securities in Brazil in December 2019

instrument	indexation	share (%)	(% share held by	
			pension funds	foreign investors
NTN-F, LTN	nominal bonds	32	8	30
LFT	policy rate	40	21	1
NTN-B	inflation	25	50	2

Preemptive restructurings on domestic debt

- How do preemptive restructurings relate to future restructurings?
- Paper provides longer time series on these restructurings.

Wrapping up

- Very interesting paper.
- It provides a great picture on external/domestic restructurings.
- But researchers should use the stylized facts with caution!