

Debt and Economic Growth

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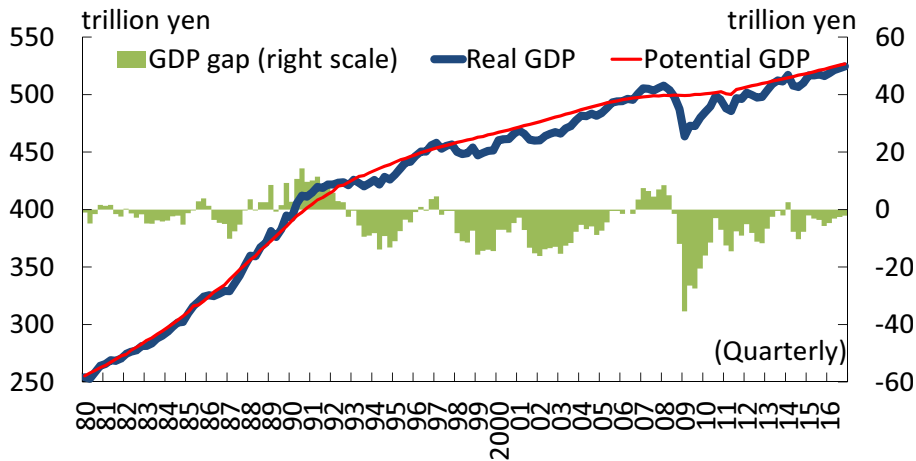
June 2, 2017 @ JEF-APRC, Stanford 2017

Japan

- 1980s High economic growth (Boom): Asset bubbles
- 1990s Low economic growth (Stagnation): Nonperforming loans
- 2000s Low economic growth (Stagnation): Public debt

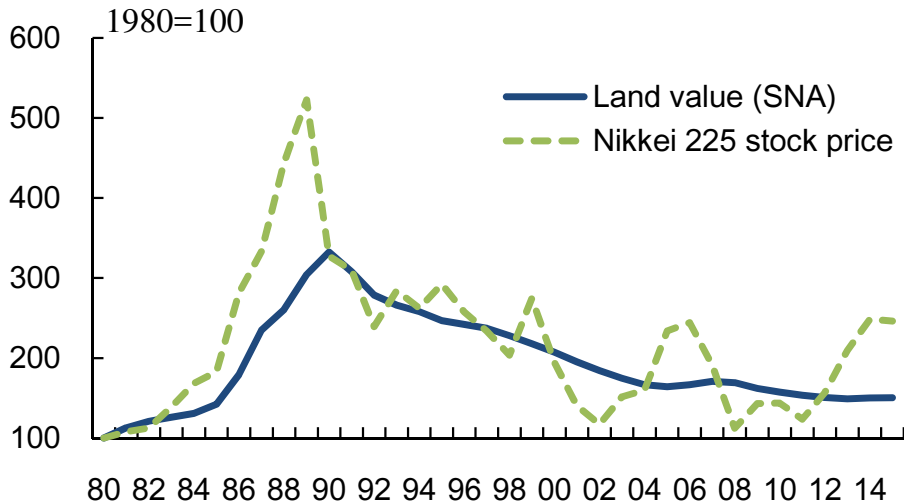
“Secular stagnation” in Japan

Real and potential GDP



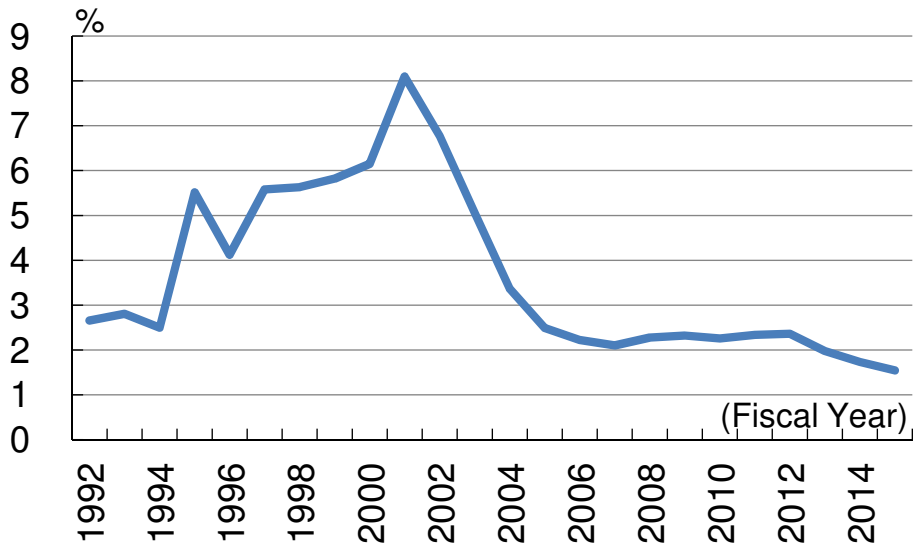
Sources: Cabinet Office, Government of Japan, “Annual Report on National Accounts”

Asset prices: land and stocks



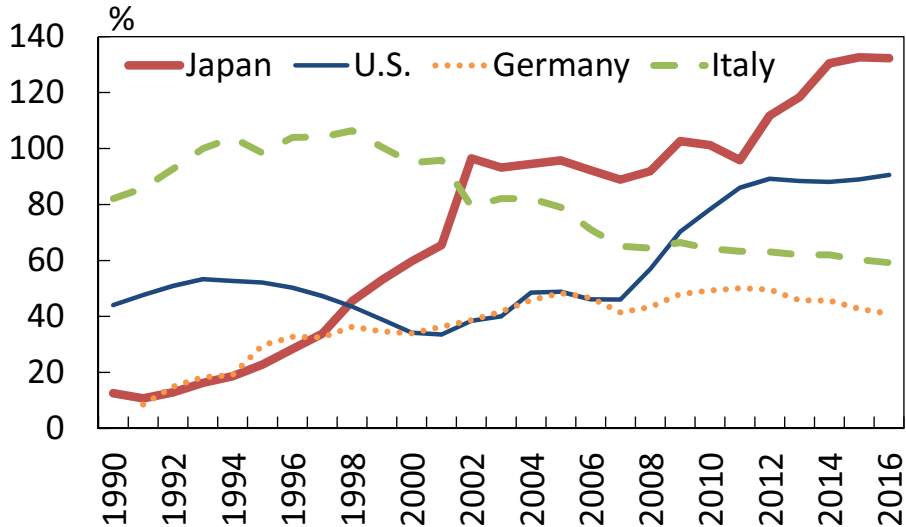
Sources: Cabinet Office, Government of Japan, "Annual Report on National Accounts", The Nikkei.

Nonperforming loans-to-GDP ratio



Sources: Financial Services Agency, *Status of Non-Performing Loans*; Cabinet Office, Government of Japan, *Annual Report on National Accounts*.

Public debt



Source: OECD, Economic Outlook No.100

Does excessive debt depress the economy persistently?

- Debt in private sector
- Borrowing constraints on inter-temporal debt b and intra-temporal debt σ , which finances the working capital

- $b \leq \theta S$

Kiyotaki-Moore 1997

Temporary effect

- $\sigma \leq \theta \max \{S - b, 0\}$

Jermann-Quadrini 2012

Temporary effect

- $\sigma \leq \phi y(\sigma) + \max \{\theta S - b, 0\}$

Kobayashi-Shirai 2017

Permanent effect

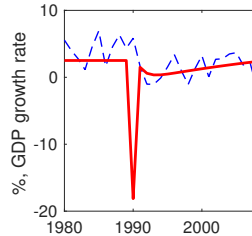
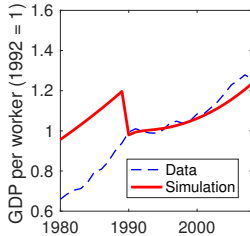
Debt in private sector can cause secular stagnation: simulation

Kobayashi and Shirai (2017)

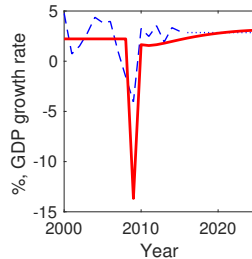
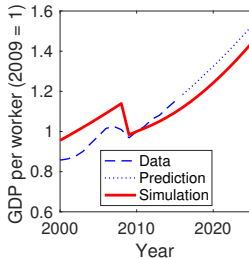
LV

growth rate

Japan



US

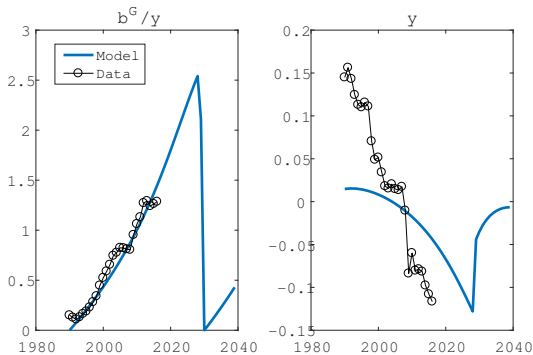


Tail risk of public debt

- Nonperforming loans disappeared in 2000s in Japan
- Public debt is exploding in 2010s
- Tail risk depresses the economy persistently
 - Gourio (2013)
 - Kozlowsky-Veldkamp-Venkateswaran (2015)
- Tail risk for Japan = Debt crisis = Hyperinflation
 - Persistent stagnation **today** may be caused by **future** risk of tail event
 - Tail risk is “growing”
 - ⇒ Not only *level* but also *growth rate* of GDP is depressed

Simulation and data (Japan)

- Kobayashi and Ueda (work in progress)



Conclusion

- Private-sector debt may cause persistent stagnation
 - Japan 1990s
 - United States 2010s?
- Public-sector debt may cause persistent stagnation
 - Japan 2010s?
- Debt reduction (public/private) may enhance economic growth
 - Corporate or household debt
 - Bank recapitalization and write-off of nonperforming loans
 - Debt forgiveness and restructuring of the borrowers
 - Government debt
 - Fiscal consolidation by tax hike and budget cut
 - Inflation tax, i.e., monetary easing

Reference

- Kobayashi and Shirai (2017) “Debt-ridden borrowers and economic slowdown”

- Kobayashi (2017) “Persistent economic slowdown and debt-ridden borrowers” *VOX column*
<http://voxeu.org/article/persistent-economic-slowdown-and-debt-ridden-borrowers>