## Challenge to public debt sustainability

Maximum sustainable level of public debt (Blanchard, 1985):  $\hat{d} = \frac{s*}{r-y}$ 

#### In the next 5Y:

**S** \* : maximum politically feasible primary surplus  $\downarrow$  : rise in defence, public investment, healthcare spending

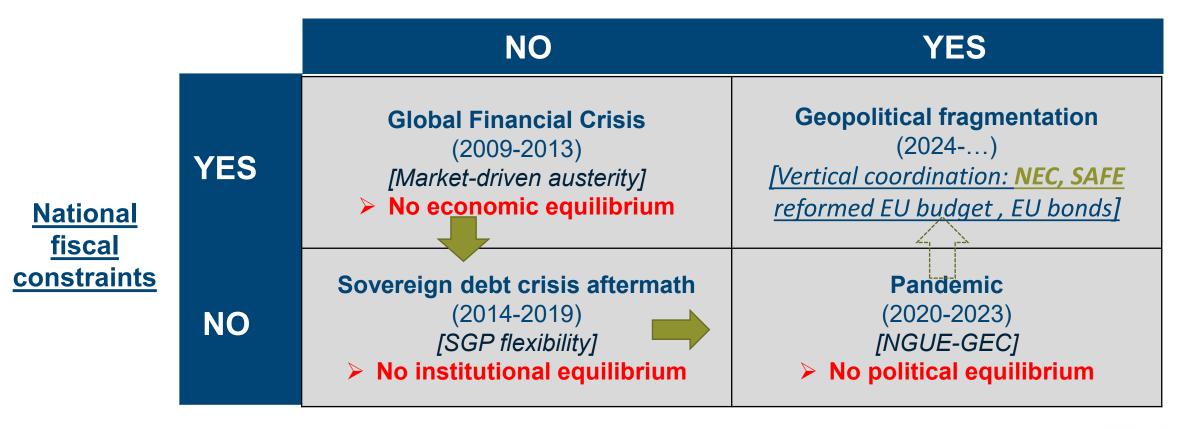
r: average interest rate on public debt : effect of end of ultra low interest rates

y: ↓ demography, AI (?)

 $\hat{d}$  goes down. If  $d > \hat{d}$  the debt keeps increasing unless....

### Vertical fiscal policy coordination

#### **Central Fiscal Capacity**





# Incentivising national defence spending

(red: countries in EDP)

### **National Escape Clause**

		NO	YES
<u>SAFE</u>	YES	Cyprus, <b>France</b> , <b>Italy</b> , <b>Romania</b> , Spain	Belgium, Bulgaria, Croatia, Czech Republic, Denmark, Estonia, Finland, Greece, Hungary, Latvia, Lithuania, Poland, Portugal, Slovakia
	NO	Austria, Ireland, Luxembourg, Malta, Netherlands, Sweden	Germany, Slovenia

