Investment at a Time of High Public Debt

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Cassa Depositi e Prestiti
Investing in tomorrow
Countries entered the new crisis in a worse shape than the previous one...

General Government debts (2007 vs 2019, % GDP)

- **Almost all public debts increased** after the previous crisis

- **In the United States nearly doubled**, while in Spain it nearly tripled

- **Only Germany among developed countries has reduced** its public debt

Source: CDP Think Tank on IMF data.
…a new increase of debt levels is expected at national level…

2009-2011 debt-to-GDP ratio increase, and expected increase between 2019 and 2021 (% GDP)

- G20 public debts are expected to rise
- This is explained by the contraction of GDP and the measures taken to react
- US public debt is expected to grow by almost 40 percentage points

Source: CDP Think Tank on IMF data.
Note: Data are as of June 12, 2020.
...and even supranational solutions involve debt rises

Fiscal measures adopted by the European institutions (€ bn)

- Public debt will also increase at the supranational level
- Debt emission will be equal to 1100 billion in Europe
- The focus will be on investments

Source: CDP Think Tank on ESM, EIB and European Commission data.
According to some, so high public debts are not a problem…

Debt-to-GDP ratio and long-term interest rates of Japan, US and Germany (average, 1905-2016)

- Interest rates in advanced economies have never been as low as today
- Hence, reducing public debt could not be a priority for countries
- Indeed, such low interest rates reduce the pressure on public debts

Source: CDP Think Tank on Jordà-Schularick-Taylor macrohistory database.
...but a fiscal buffer to cope with new risks is required

1. Climate change

2. New wave of pandemic

3. Unequal income distribution and social tensions

4. New financial crisis
So what? We must find a way to cover the investment gaps…

Global estimated infrastructure investment gaps by sector ($ bn, 2016-2040)

- Before the crisis, huge investment gaps already existed globally
- The gap estimated for the period 2016-2040 amounted to almost 15 trillion $
- New investment needs arising in this crisis will add on these investment gaps

Source: CDP Think Tank on Global Infrastructure Hub data.
The Covid-19 crisis had a major impact on the equity position.

- Total losses to be incurred by firms could exceed €720bn in Europe.
- This could reach €1.2trn in the stress scenario.

Source: CDP Think Tank on European Commission data (as of May 2020).
Note: Other includes Digital, Aerospace & Defence, Textile, Renewable Energy, Electronics.
Private sector has resources: households hold liquidity…

- **We need to look for different sources** in order to finance investments

- **Currency and deposits** compose a great percentage of households’ wealth

- **We should find a way to channel** this amount of liquidity to real economy

Source: CDP Think Tank on OECD data.
The liquidity held by institutional investors in OECD countries is nearly 2.7 trillion dollars.

A small part of this liquidity could significantly stimulate private investment.

Furthermore, the "patient" approach of institutional investors allows for long-term initiatives.

Source: CDP Think Tank on OECD data.
Note: data referred to investment funds of Italy, Ireland and the Netherlands are not available.
Key is the role of State. Which role?

- The paying State
- The presiding State
- The promoter State
Remove investment barriers…

Composite indicators of Regulatory Policy and Governance (primary laws, 2017)

- Possible investment barriers from regulation
- Each country could improve its performance in regulatory policy
- Areas to identify ex-ante evaluation (RIA); stakeholder engagement; ex-post evaluation

<table>
<thead>
<tr>
<th>Country</th>
<th>Regulatory Impact Assessment (RIA)</th>
<th>Stakeholder engagement</th>
<th>Ex post evaluation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Turkey</td>
<td>1.31</td>
<td>1.51</td>
<td>0.98</td>
</tr>
<tr>
<td>Japan</td>
<td>2.16</td>
<td>2.22</td>
<td>2.49</td>
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<tr>
<td>France</td>
<td>2.36</td>
<td>2.48</td>
<td>2.57</td>
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<tr>
<td>Italy</td>
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<td>2.57</td>
<td>2.88</td>
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<td>Australia</td>
<td>2.48</td>
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</tr>
<tr>
<td>Canada</td>
<td>2.28</td>
<td>2.88</td>
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<tr>
<td>United States</td>
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<td>Mexico</td>
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<tr>
<td>United Kingdom</td>
<td>3.22</td>
<td>3.28</td>
<td>3.28</td>
</tr>
</tbody>
</table>

Source: CDP Think Tank on OECD data. Note: the maximum score for each category is 4. For the United States, indicators about secondary laws are adopted as all primary laws are initiated by Congress, not by the executive.
Venture capital investments (2019, % GDP)

- Venture capital could be a way to boost investment
- Venture capital investments are not well developed
- Except U.S., venture capital investments are well below 0.2% of GDP in OECD countries

Source: CDP Think Tank on OECD data.
- After 2013, private equity has been continuously growing in Europe.

- Private equity investments in Europe amounted to 83 billion euros in 2019 (94 including Venture Capital).

- However, we can do better.

Source: CDP Think Tank on Invest Europe data.
...public-private partnerships...

Procuring Infrastructure PPPs 2018 average scores by country income group (score 1–100)

<table>
<thead>
<tr>
<th>Country Income Group</th>
<th>Preparation</th>
<th>Procurement</th>
<th>USP</th>
<th>Contract Management</th>
<th>Average</th>
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</thead>
<tbody>
<tr>
<td>High-income</td>
<td>63</td>
<td>77</td>
<td>66</td>
<td>58</td>
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<tr>
<td>Upper-middle-income</td>
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<td>64</td>
<td>63</td>
<td>57</td>
<td></td>
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<tr>
<td>Lower-middle-income</td>
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<td>58</td>
<td>53</td>
<td>52</td>
<td></td>
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<tr>
<td>Low-income</td>
<td>39</td>
<td>54</td>
<td>47</td>
<td>47</td>
<td></td>
</tr>
</tbody>
</table>

- It is important to evaluate the performance of the public sector in public-private partnerships
- According to the World Bank, the higher the income level of the countries, the higher the performance
- Preparation and contract management leave most room for improvement

Note: USP = unsolicited proposal.
...and tax incentives to support R&D spending

R&D tax incentives (2017, % of business enterprise expenditure on R&D)

- Among OECD countries, only 6% of spending on R&D by business enterprises is covered by tax incentives.

- There is a lot of heterogeneity.

- Long-term effects on countries’ GDP could lead to a structural increase in tax revenues.

Source: CDP Think Tank on OECD data.
Note: U.S. data are referred to 2016.
To sum up:

1. **Public debt should be a concern** and national governments will not have much resources to finance the economy in the future. Risky if a new shock arises.

2. Time for a **different role of the State**: create the condition to channel private financial resources toward investment with high positive externalities.

3. Each country has its specificities, but areas as **PPPs, Private equity and venture capital, appropriate tax incentive** are worth to be explored.