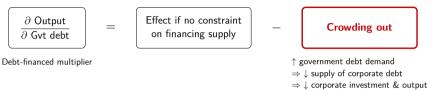
The Crowding Out Effect of Local Government Debt: Micro- and Macro-Estimates

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Motivation

► Government debt may adversely affect private sector via financial crowding out effect



- Challenges to empirical quantification:
 - Government debt: (1) is **endogenous**; (2) affects firms via **multiple channels**
- ► This paper: Quantify crowding out effect of local government bank debt on corporate credit, investment and output
 - Local government bank debt is large and growing:
 - Over 1990-2019, local government debt-to-GDP ↑ from 12% to 22% (G20 countries)
 - 80% of local government debt = bank debt
 - Identification strategy to isolate financial crowding out

Methodology

Data: French credit registry over 2006-2018

- 1. Identification: causal reduced-form evidence
 - $-\uparrow$ Local government borrowing from a given bank
 - $\Rightarrow \downarrow$ Corporate loans by that bank?
 - ⇒ ↓ Investment for that bank's borrowers?
 - → Isolate crowding out

2. Aggregation: model

– Estimated cross-sectional effects ⇒ Aggregate output loss?

Main findings

- 1. Existence: Local government loans crowd out corporate loans
- **2.** Quantification: $\uparrow \in 1$ local government loans $\Rightarrow \downarrow \in 0.2$ aggregate output
- 3. Determinants: More severe when borrowing from more constrained banks
 - → Mode of financing of government debt matters

