

# Debt Ceiling Brinkmanship and Global Financial Diversification

William Clinton Co\*

Department of Economics, The University of British Columbia

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## Abstract

The text of your abstract. 200 or fewer words.

*Keywords:* 3 to 6 keywords, that do not appear in the title

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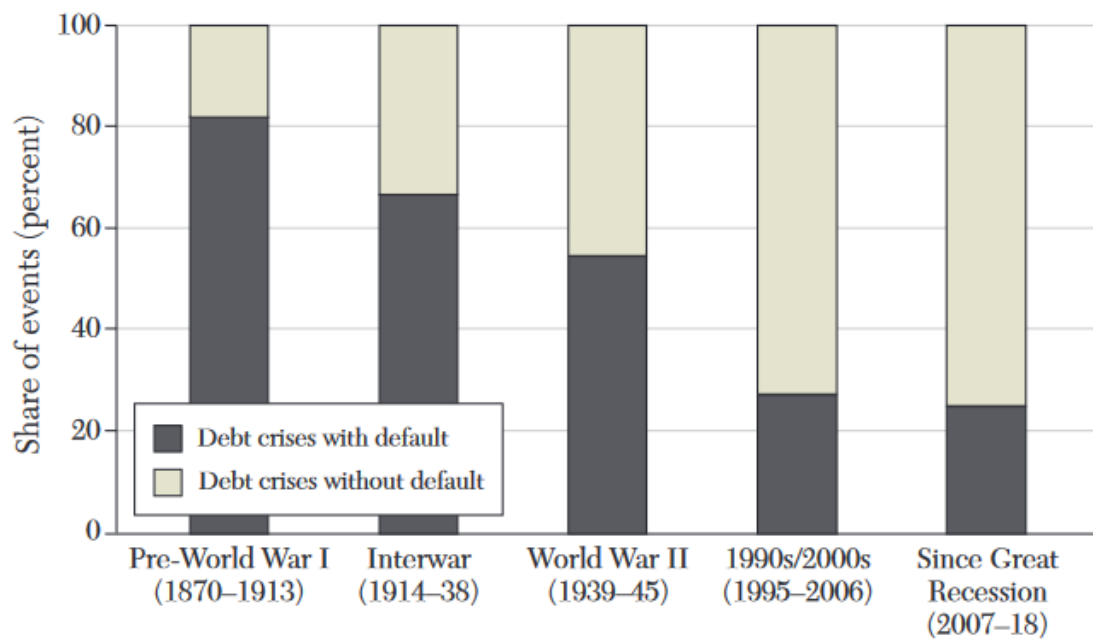
\*Below is an attached research proposal. It starts with an introduction. Followed by relevant data sets along with proposed methodology. Lastly, a game theory model of debt ceiling brinkmanship is proposed.

# 1 Introduction

Constantly increasing public debt has been a recent occurrence throughout recent history [Mitchener & Trebesch \(2023\)](#). This raises the question of how will governments deal with rising debt burdens going forward. As debt increases, cost of borrowing increases. Do governments internalize the increase of cost of borrowing, in the context of debt ceiling brinkmanship? We construct a data set of X-dates, dates where the US government will supposedly run out of money. We then analyze the CDS prices and yield spreads, such that we investigate whether debt ceiling negotiations will settle earlier given a bigger increase in cost of capital. We investigate trends overtime.

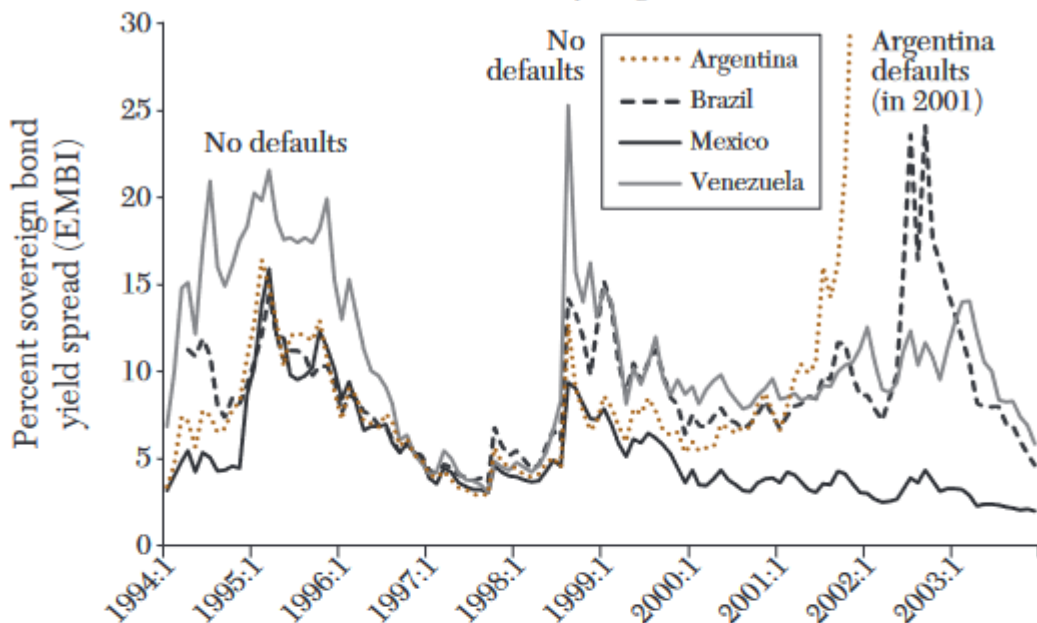
It has also been noted that debt crisis without default has become more common, wherein there was a near missed payment but never a default has a negative effect on output, as exemplified in Greece Portugal and Spain during 2010-2012 [Mitchener & Trebesch \(2023\)](#). Going a step further some have proposed to change the definition of debt crises to yield spreads of 1000 basis points, also known as spread spikes. ([Broner et al. 2013](#), [Aguiar et al. n.d.](#), [Krishnamurthy & Muir n.d.](#))

There has been work on the frequency of debt crisis without default. we study this data set by cite [Meyer et al. \(2022\)](#) as it relates data on debt ceiling brinkmanship [Reinhart & Rogoff \(2008\)](#) we use the definition of 1000 basis points we analyze these in the context of debt brinkmanship taking inspiration from graphs.



*Figure 7. Sovereign Debt Crises With and Without Default (Share of Events in %)*

Panel B: Latin America in the 1990s: only Argentina defaults



Panel C: Eurozone debt crisis: only Greece defaults

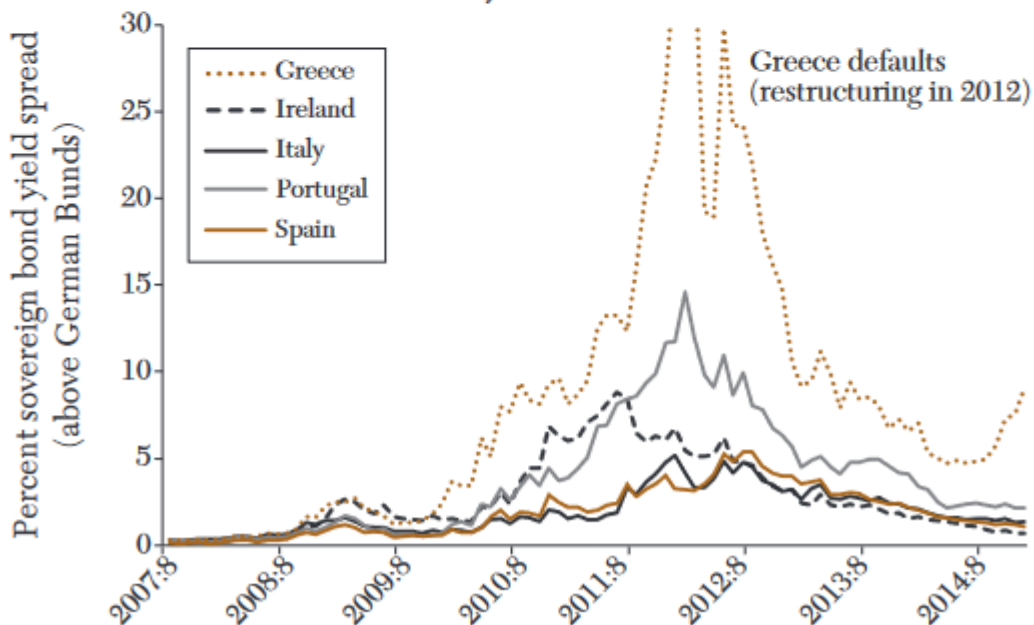


Figure 8. Selected Episodes of Debt Crises without Default

What makes this even more poignant is that the output decline happens in anticipation of a default rather than the default itself [Yeyati & Panizza \(2011\)](#) . Thus we investigate if this link applies to debt ceiling brinkmanship as well.

What makes this an important topic to study is the body of evidence proving a decline in output associated with the high yields that accompanies a debt crisis. There are varying reasons for this such as the relationship between external financing and importers [Mendoza & Yue \(2012\)](#) , the decrease in external domestic firm borrowing([Corsetti et al. 2012](#), [Das et al. 2010](#), [Gourinchas et al. 2016](#)) or the tightening of credit against losses on bank balance sheets([Arellano et al. n.d.](#), [Ferrando et al. 2017](#)). Similarly, we explore this in the context of debt brinkmanship.

There has also been work on how credit rating agencies downgrading reduces leverage and investments [Almeida et al. \(2017\)](#). Similar conclusions were drawn using CDS premia instead of bond yield spreads ([Brutti & Sauré 2015](#), [Bahaj 2020](#)). Similarly, we explore this in the context of debt brinkmanship.

Another pertinent question is the many creditors willing to lend to highly indebted sovereigns. Currently we are in a safe asset shortage, such that we are coming closer to the effective lower bound, wherein central banks could not decrease interest rates any further as needed. This shortage is a key source of fragility in the economy, dubbed the “safety trap”. ? investigate if brinkmanship is a contributor to the shortage of safe assets. If so then there would be an argument to abolish the system on a global welfare standpoint. Taking inspiration from

track how china plays into this . Track Chinese investments.

advanced vs developed

Track advance vs developed economies effects

currency composition-- world currency composition. I track the investment. I track the currencies.

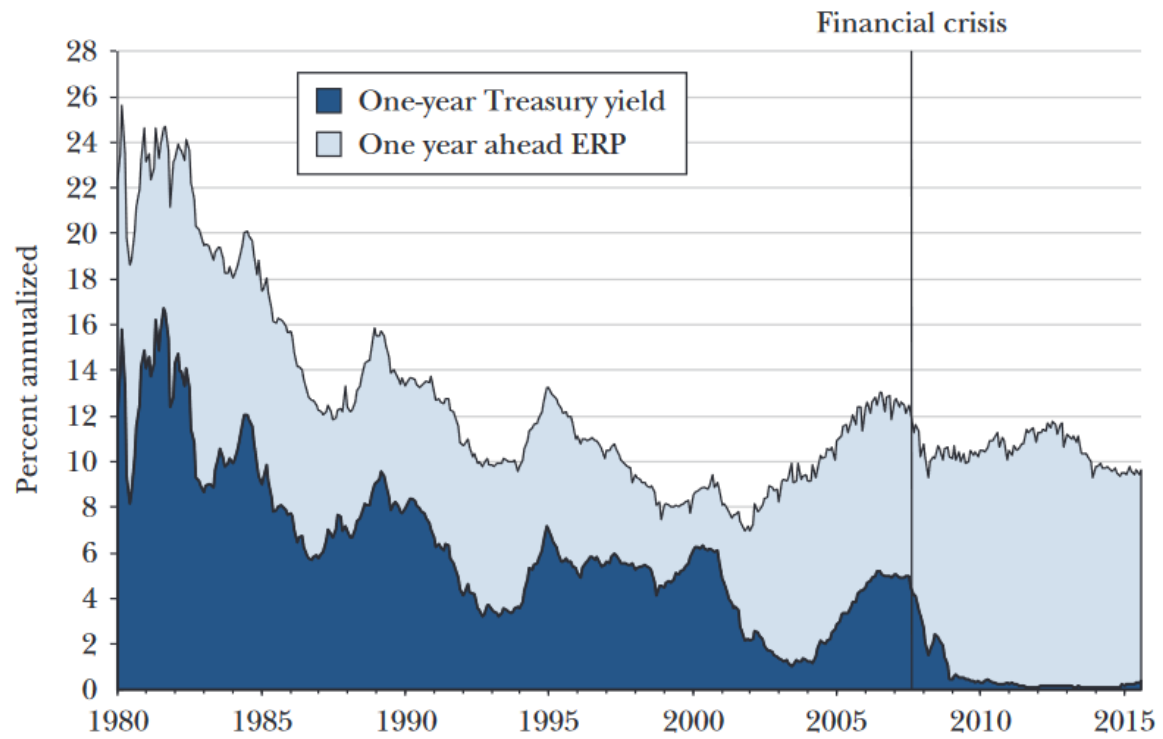
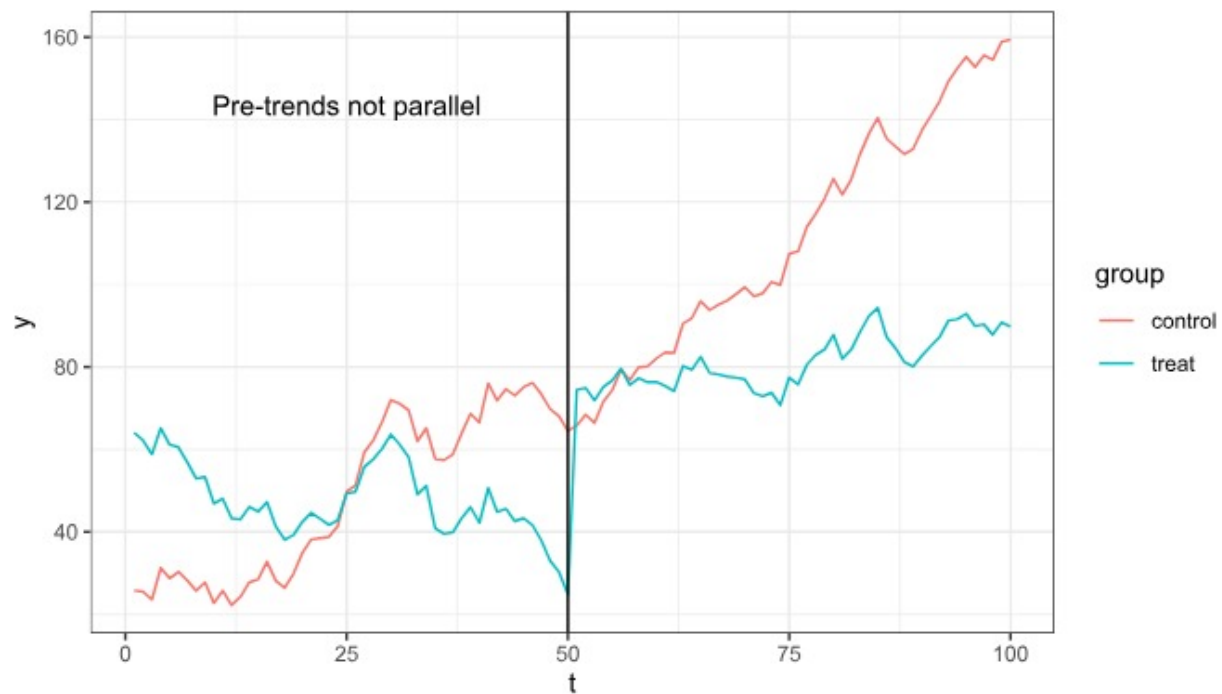


Figure 1: Consistency comparison in fitting surrogate model in the tidal power example.

We use the 1 year expected risk premium vs the 1 year treasury yield to construct a similar graph that marks debt ceiling brinkmanship. Furthermore we construct the graph below with the same variables [Duarte & Rosa \(2015\)](#).



given the outside buying of central banks we look at

. By answering this question we gain insight into the future of larger and larger public debt burdens going forward.

We investigate if its ias a threat to safe asset shortage.

The US treasury yield occupies the status as the biggest and most liquid market, wherein its yield is a signicant determinant of the global factor of yields.

Given that the global factor has become increasingly a more important determinant of yields ,against the specific “country” factor [Mauro et al. \(2002\)](#). thus it becomes important to study this phenomenon.([Rozada & Yeyati 2006](#), [González-Rozada & Yeyati 2008](#), [Longstaff et al. 2011](#))

## 2 Data set

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