

# Discussion: The Austerity Threshold by Tim Landvoigt

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## Executive Summary (1/2)

The **austerity threshold** is the debt-to-GDP level above which the government *must* raise surpluses to keep debt risk-free. This paper defines it formally and quantifies it for the U.S. in a globally solved New Keynesian model.

- Threshold is **189%** of GDP under tax hikes and **200%** under spending cuts — both well above the current level
- Safety premia and convenience yields sustain fiscal capacity: reducing risk aversion alone collapses the threshold from 189% to 137%
- The adjustment type matters *today*: tax austerity is inflationary, spending austerity is deflationary.

## Executive Summary (2/2)

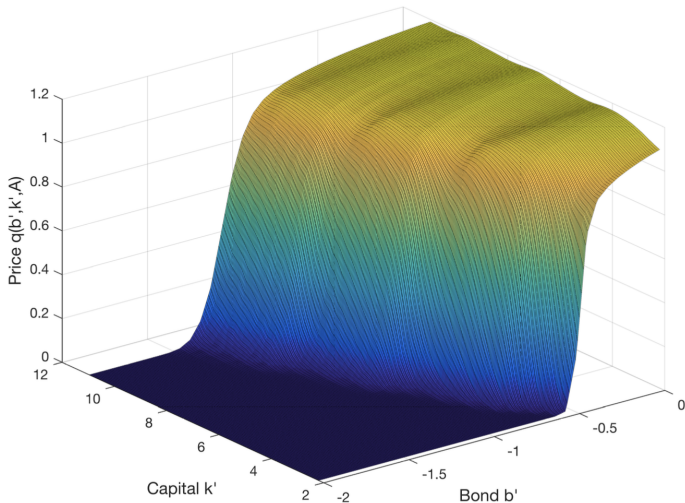
Uncertainty over *which* austerity form will prevail—driven by electoral cycles—reduces fiscal capacity to **127% of GDP**, a level CBO projects will be **breached within the next decade**.

### Policy levers

- **Shorter debt maturity** raises the threshold to 220%, but crowds out investment and reduces welfare
- **Stricter liquidity regulation** raises the threshold to 228%, with the same crowding-out cost
- **Hawkish monetary policy** in austerity raises the threshold to 212% and, unlike the previous two, crowds *in* capital and raises welfare

## A Visual

Representation of austerity threshold - Gordon & Guerron (RED, 2018)



# Comments

- Debt sustainability is a critical issue
- But paper does not show much data
- Here, I provide some empirical information to illustrate state of US

# Comments

## Who holds US debt?

### Major Foreign Holders of U.S. Treasury Securities

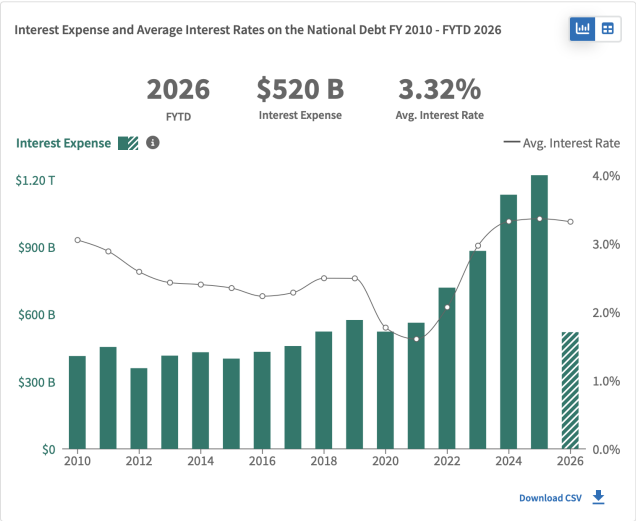
Holdings at end of period, billions of dollars

Country	Dec-24	Mar-25	Jun-25	Sep-25	Oct-25	Nov-25	Dec-25
Japan	1,061.5	1,130.8	1,147.9	1,189.3	1,200.0	1,202.7	1,185.5
United Kingdom	722.8	779.3	855.7	862.1	875.4	889.0	866.0
China, Mainland	759.0	765.4	731.4	699.2	687.7	683.9	683.5
Belgium	374.6	402.1	430.3	463.6	465.5	481.0	477.3
Canada	378.8	426.2	438.2	475.8	419.1	472.2	468.1
Luxembourg	423.9	412.4	404.1	420.6	418.5	425.4	435.1
Cayman Islands	423.0	453.6	440.9	426.9	418.5	427.6	421.2
France	332.3	363.1	373.8	375.5	390.2	376.1	368.9
Ireland	339.4	329.3	317.3	340.0	339.8	340.3	340.7
<b>Top 10 Subtotal</b>	<b>5107.6</b>	<b>5370.4</b>	<b>5446.8</b>	<b>5565.6</b>	<b>5524.2</b>	<b>5611.1</b>	<b>5556.9</b>
<b>Grand Total</b>	<b>8619.3</b>	<b>9054.2</b>	<b>9090.3</b>	<b>9234.4</b>	<b>9230.2</b>	<b>9359.3</b>	<b>9270.9</b>

Source: U.S. Department of the Treasury, Treasury International Capital (TIC) System, Table 5.

# Comments

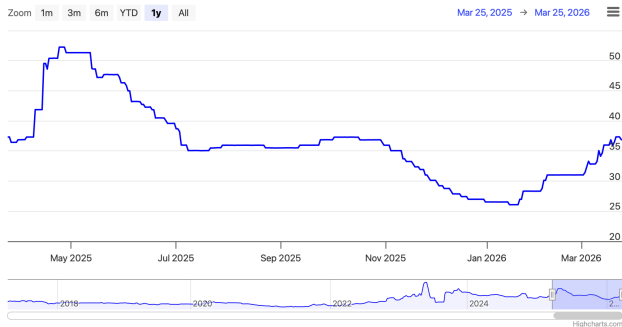
From default literature, we learn debt sustainability is about servicing debt



# Comments

## What if US actually defaults?

- Default literature has not considered this event
- Probability ( $< 1\%$ ) is small but we are in uncertain territory



# Comments

**In context of sovereign default, Gordon & Guerron (2025) highlights importance of:**

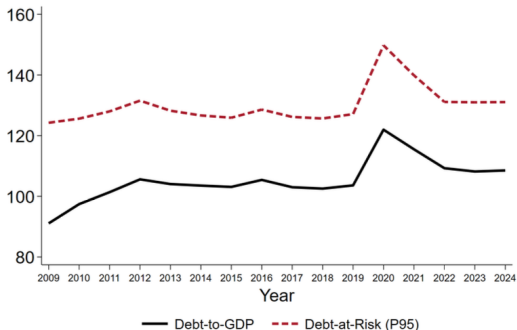
- Bargaining between issuer and holder
- Failure of reaching agreement leads to partial default — haircuts
- And endogenous duration of default episodes
- Cost of default as a result of failed restructuring attempts
- Who holds debt matter: Patient debt holders lead to smaller haircuts

# Comments

## Strong connection to Debt-at-Risk by Furceri et al. 2025

- In a nutshell, paper stresses importance of looking beyond median; right tail of Debt-to-GDP distribution

### A. AEs: Debt-to-GDP and Debt-at-Risk



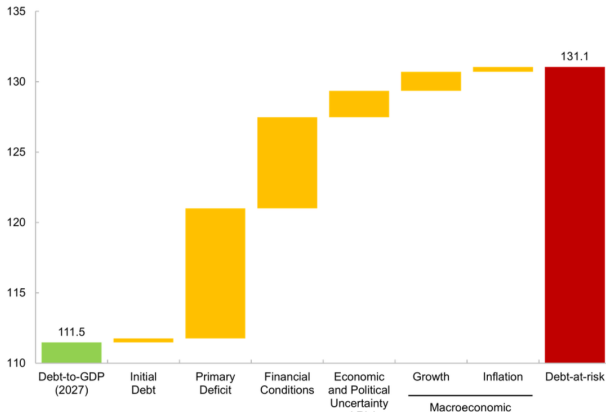
# Comments

## Strong connection to Debt-at-Risk by Furceri et al. 2025

- Different shocks/fundamentals may push economy closer to the tail.

Figure 8: Drivers of Global Debt-at-Risk by Income Groups  
(Percent of GDP)

### A. Advanced Economies



THANKS!