Interest Charges and Sustainability Challenges: The Case of OECD Countries

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Abstract

Servicing public debt is a significant budgetary burden. In the sense that the payment of interest charges is a liability on the balance sheet of the public budget and affects fiscal policy. Interest charges can sometimes become a burden if they crowd out private activities. In order to analyse and understand the determinants of the debt burden and its impact on the sustainability of public finances, the present work focuses on OECD countries. It is noted from the literature that the factors that determine interest charges are macroeconomic (inflation, GDP growth and interest rates) and public finances (primary balance and public debt). After analysing a panel of 33 OECD countries and using ordinary least squares (OLS), we find that public debt, inflation and long-term interest rates are positively correlate with interest charges. An increase in any of these variables leads to an increase in debt charges. On the other hand, a growth in GDP is negatively associated with interest charges. Indeed, an increase in GDP generates enough revenue to meet the repayment of debt charges. According to the empirical analysis, we can say that, despite the large and growing debt-to-GDP ratio of major OECD countries, interest charges are not a threat to the sustainability of public finances. However, it is important for these countries to reduce the ratio of public debt to GDP, because in the face of the many challenges (health, ageing population, etc.) that are looming on the horizon, an increase in interest rates could bring with it considerable burdens that would threaten the budgetary balance of these states.

Key words: Interests Charges, Public Debt, Sustainability**.**