EUI ROBERT SCHUMAN CENTRE

Discussion of:

Gorodnichenko and Obstfeld's

"You only live twice: financial inflows and growht in a Westward-Facing Ukraine"

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Thick, Targeted Paper

Monumental task of rebuilding post-war Ukraine

Drawing on history, theory and empirical evidence, policy strategy:

- 3 goals: reconstruction, productivity/technology, repatriation/reallocation
- 1 overarching distortion: (external) borrowing constraint
- 1 priority: finance rapid accumulation of **pledgeable K**
- 2 instruments: time-varying (decreasing) consumption tax; investment subsidy

Pledgeable capital, security anchor (NATO), institution-plus anchor (EU)

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Thick, Paper

2. International aids vs investment inflows: do they promote growth?
3 and 4. Ukraine short history and comparison with peer groups => priority to capital inflows (correlation with investment and catching up to technological frontier);
    - Population and human capital
    - Inflows of Resources
        - FDI
        - Official lending and grants
        - Remittances
        - Accession to NATO and EU
    - Productivity/technology
    - Growth Accounting (productivity, capital, demographic)
    - Remittances
5. Three growth models (borrowing constraints, innovation/human capital, re-patriation of refugees)
6. “Next Steps”

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Going backward: (a) how much capital is needed?

$40b current dollars per year, over 10 years

- $20b reconstruction of housing, energy utilities, transport infrastructure
- $20b for convergence to peers (50% to avoid divergence)

Of which 25b public investment (within ‘absorptive capacity’)

External only?

Domestic resources (leveraging, financial deepening)

Allocation efficiency

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Smoothing vs. (TF)P

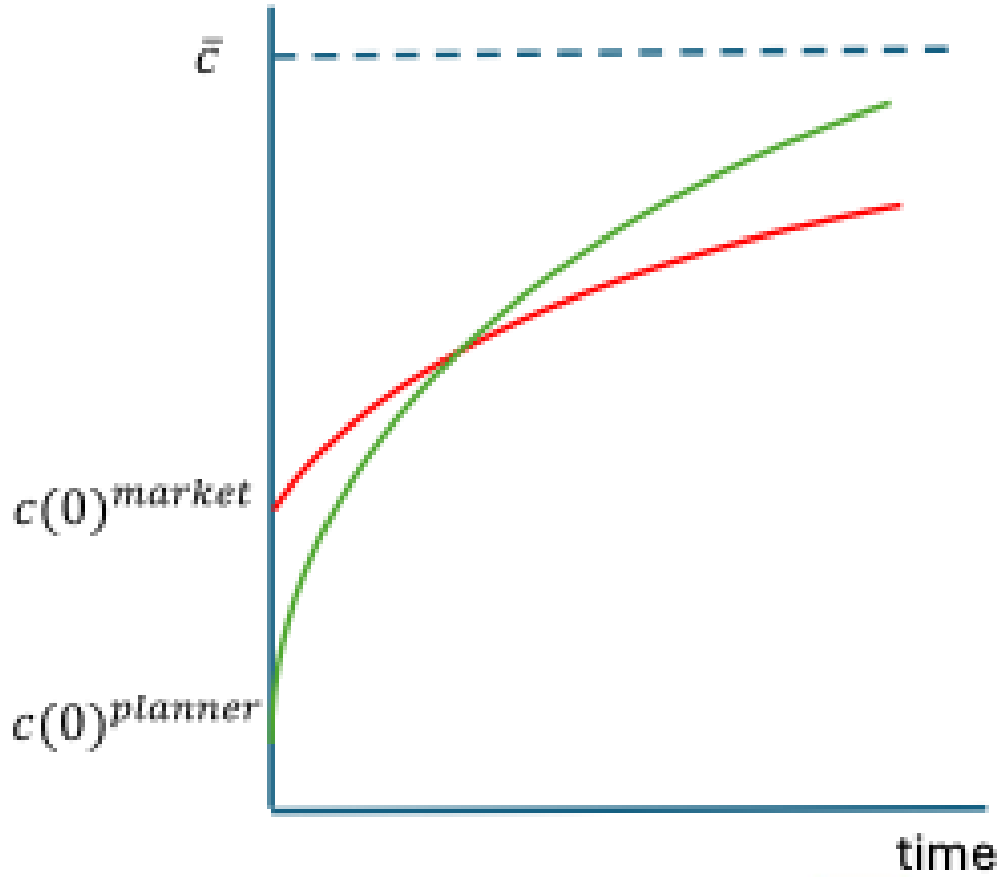
$\bar{c} = \bar{y}\text{-}\delta\bar{K}\text{-}\gamma r\ \bar{K}$

Consumption tax supports planner, but does not affect steady state consumption

Only faster convergence => relatively small smoothing gains

Key is TFP---outside the model (Gourinchas Jeanne 2006)

Figure 16. Planner and Market Consumption Paths.



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Capital—Infrastructure and Public Goods vs productive

Barro (1990) (in my version JEDC 1997)

$$y=A[Kg]\ f(f,k)$$

- Dynamics similar, but finance likely differs
  - FDI for infrastructure? Fees?
  - Debt financing against future tax revenue
- FDI ?
  - Static externality => investment subsidy, to foreign-owned firms?
- Also in the background: sectoral model, relative price dynamics
  - Capital inflow/ external adjustment hardly ‘immaculate’ (Williamson) => terms of trade

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Starting point: debt overhang

Public debt>100% (2025)

- ¾ held by foreign official creditors (EU then IMF WB etc)
- Internally held by domestic banks (hence financial fragility)

Private external claims 11% of public debt (2025)

- restructured sovereign liabilities ($20.5b eurobonds restructured in 2024)

In spite of Extraordinary Revenue Acceleration (ERA) programme, IMF Extended Fund Facility (EEF), and even accounting for the Merz (2025) proposal, some debt write down and extension unavoidable.

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Evolving policy regime

Road map needed

- Capital controls likely needed upfront---but FDI requires two-way flows.
- More in general --- inflows increasing in “capacity”
- Exchange rate adjustment vs. misalignment
  - Liquidity arrangements (self-insurance via reserve accumulation too costly)
- Fiscal regime: Declining VAT to encourage saving---but which end-point model?
  - Sustainable internal and external debt
  - Financing by leveraging, domestic/international guarantees and value-at-risk likely

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Exchange rate and macroeconomic stability

Baxter Stockman revisited European sample

Unconditional moments after applying a quadratic trend. Quarterly data from 1999:Q1 to 2021:Q4. Average moments across countries in the respective group, weighted by number of observations in the regime per country. Only countries that peg or float, respectively, for at least half of the sample (Corsetti et al. 2023)

Table 3: Business cycle moments in the data

	euro area			float			peg		
Volatility & correlation									
	σ_x	$\rho_{x,gdp}$	$\rho_{x,x_{-1}}$	σ_x	$\rho_{x,gdp}$	$\rho_{x,x_{-1}}$	σ_x	$\rho_{x,gdp}$	$\rho_{x,x_{-1}}$
gdp_t	2.5	1.00	0.68	3.5	1.00	0.79	5.2	1.00	0.90
r_t	0.9	0.56	0.93	2.1	0.40	0.90	1.6	0.29	0.88
π_t	0.4	0.39	0.34	0.7	0.31	0.42	0.7	0.35	0.35
Δe_t	–	–	–	3.9	-0.01	0.14	0.8	-0.04	0.12
Comovement with EA									
				ρ_{x,x^*}	ρ_{x,gdp^*}		ρ_{x,x^*}	ρ_{x,gdp^*}	
gdp_t				0.75	0.75		0.67	0.67	
r_t				0.60	0.27		0.47	0.18	
π_t				0.44	0.24		0.58	0.35	
Δe_t				–	-0.02		–	-0.04	

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To conclude

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