

# HOW TO DEAL WITH THE PUBLIC DEBT. AN ALTERNATIVE TO THE MAINSTREAM

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## ABSTRACT

The paper proposes an alternative approach to the problem of public deficits and debts. This alternative approach is inspired by the past contributions of four economists: Keynes, Domar, Lerner and Hicks.

A fundamental indication coming from all these economists is that the public debt cannot be regarded and dealt with as if it were essentially the same as the private debt. In particular, it is no true that the public debt must be necessarily extinguished.

In the present situation, many hold that the problem of public debt must be solved by raising the economy's growth rate. But many also believe that higher growth rates can be obtained by 'freeing' the economy from the 'interference' of the state, which means to reduce the public debt and deficits.

This paper, in the tradition mentioned above, follows a different route. Higher growth rates can be achieved thanks to a significant and permanent role of the public sector. This, however, does not mean that the economy must experience an ever-growing ratio of the public debt to GDP.

The paper shows that it is possible to stabilise the ratio of the public debt to GDP even though the government runs primary deficits. This result is obtained by choosing a composition of public spending associated with a growth rate larger than the interest rate on the public debt.

The analysis is essentially based on the idea that public expenditure can be disaggregated into two components: 'productive' expenditures, which positively and directly affect the economy's growth rate; 'unproductive' expenditures, which do not affect the growth rate directly.