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Global experience in public debt reduction (on example of Sweden, Switzerland, and Iceland)

■ **Abstract.** Public debt reduction is one of the main objectives of budget policy formation in the current crisis conditions. In this regard, the study of the experience of different countries in this area is relevant. Therefore, the aim of the study was to provide recommendations for reducing the debt burden in the Kyrgyz Republic, based on the experience of other countries. The main methods used in the research were historical, comparison and generalisation. The study analysed the factors affecting the reduction of public debt in the Kyrgyz Republic. It was concluded that the components that can help affect the debt burden in the country are inflation, economic development, and a targeted policy of the state to pay debts. It was shown that in the current realities, countries that are successful in this direction most often use the latter approach. In addition, the situation in Sweden, Switzerland and Iceland was analysed directly and the

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main recommendations were given as to how the Kyrgyz Republic can improve its current situation in terms of debt reduction. These recommendations focused primarily on fighting corruption and improving the situation in the context of institutional development, as well as reducing expenditures to achieve a budget surplus. It was recommended not to increase taxes directly to increase state revenues, but to increase the efficiency of their collection. The data obtained from the results of the study can be used to formulate public policy in the area of public debt and budget management both in the Kyrgyz Republic and in other countries

■ **Keywords:** fiscal policy; inflation; economic growth; budget; management

■ INTRODUCTION

Public debt is a set of financial obligations of the state to its creditors, which can be other countries, international organisations, private investors, and citizens. This indicator arises as a result of borrowing to finance budget deficits, infrastructure projects or other public needs. By using various instruments, such as loans and securities (bonds), the state can cover current budget needs at the expense of future generations. In general, the competent use of such an instrument may become a positive factor in long-term economic development, although at the expense of a negative impact on financial stability. In modern conditions, when after the time of economic abundance in the world the factors causing crisis events (such as COVID-19 virus and military conflicts) have become more evident, it becomes more and more important to improve the financial condition of countries. Thus, analysing public debt policy is relevant.

Many scholars have worked on the assessment of the financial condition of the Kyrgyz Republic. D. Sharipova & A. Kudebayeva (2023) analysed the financial well-being of Kazakhstan and the Kyrgyz Republic between 2011 and 2018. They noted that the Kyrgyz Republic generally experienced an improvement in well-being despite crises and economic and political instability. However, the study remains rather limited as it only assessed data up to 2018. Financial sustainability in the Kyrgyz Republic has also been studied by N. Alymkulova & J. Ganiev (2019), but they focused on the formation of sound monetary policy without studying problems in the context of state budget formation and public debt servicing. A.A. Sherbekova & A.S. Ryspaeva (2021) studied the impact of the COVID-19 crisis on the state of the financial system of the Kyrgyz Republic. They showed the negative trends in the development of the country during this period and concluded that monetary and fiscal policies during this period should be aimed at mitigating the consequences. In particular, the importance of investing in economic recovery was emphasised to sustain the country, restore confidence in markets and contain risks to financial stability. E. Vinokurov *et al.* (2022) assessed the resilience of the Kyrgyz Republic's debt to external shocks. Kyrgyz Republic was shown to be more sensitive to a global recession than to a financial shock, indicating underdeveloped financial markets and a continued dependence on commodity exports and remittances. In this regard, the researchers pointed to the importance of diversifying the economy for its stable development but did not describe clear recommendations for improving the situation in the country. The study of the Kyrgyz Republic's external debt was also conducted by J. Ganiev *et al.* (2020), point to its significant recent growth. The researchers concluded that the country is dependent on foreign revenues, which led them to recommend that

investors should be motivated to invest in instruments other than debt, especially foreign direct investment.

This study uses the results of this analysis to create a recommendation for the Kyrgyz Republic. This will form a better policy for the country in the sphere, strengthening its financial sustainability, including in the face of global crises. Ignoring this component in the management of the state can lead to negative long-term consequences for the country's economy and its social component. Thus, the study aimed to formulate recommendations on public policy in the context of public debt management based on an assessment of the experience of other countries.

■ MATERIALS AND METHODS

The study analyses the level of public debt in the Kyrgyz Republic and assesses the debt management policies of individual countries. In the current conditions of economic development, most countries are characterised by trends related to the growth of the ratio of public debt to gross domestic product (GDP). In this connection, certain countries to which such a trend is not relevant, and which remain developed, were chosen, including: Switzerland, Sweden, and Iceland. The period chosen for the study was 2006-2022 due to the abundance of information to analyse for all countries in this interval; it is also large enough to note the main trends and draw conclusions based on them.

The study used various sources of information to characterise the level of public debt in the countries. For example, data from the Kyrgyz Republic was assessed based on information from the National Statistical Committee of the Kyrgyz Republic (State debt, n.d.). Data on the ratio of public debt to GDP for such countries as Sweden, Switzerland and Iceland were analysed from official data of the website of the international organisation World Bank (GDP (current US\$)..., 2022; Inflation, consumer prices..., 2022). Data from other sources were also used to assess the situation in these countries: in particular, Sweden government budget deficit (2022) to analyse the nominal public debt and the ratio of budget deficit to GDP and Statista (Iceland: Inflation rate..., 2023; Sweden: Inflation rate..., 2023; Switzerland: Inflation rate..., 2023) to assess the inflation rate in the countries. The Countryeconomy website (General government gross debt, 2022) also made it possible to assess information about the situation in terms of public debt in such countries as Kazakhstan, Moldova, Uzbekistan, and Armenia, as states that are similar to the Kyrgyz Republic in terms of their development and are also members of a single international organisation – Eurasian Economic Union (EEU). All constructions and calculations in the study were carried out in Microsoft Excel.

One of the main methods used in the study was the historical one, which was used to assess the situation in this context in retrospect, i.e. based on past data. The comparison was used to assess how the dynamics of public debt differ in individual countries and to draw conclusions about the reasons for changes in this indicator. The graphical method was used to present the data in the form of figures for easier evaluation. The generalisation method, in turn, allowed us to discard all secondary data on the state of public debt in the Kyrgyz Republic and other countries to focus on the main information for concluding the study. The description was used to collect the main data in the study and then characterise them.

■ RESULTS

In general, only a few main reasons can be singled out, due to which a decrease in the level of public debt in the country can be observed. These are direct debt repayment due

to an increase in revenues and decrease in budget expenditures, growth of inflation rate, which leads to depreciation of debt denominated in the respective currency, and rapid economic growth, which increases the level of GDP, and thus reduces the ratio of debt to this value (Butkus *et al.*, 2021). Thus, when assessing the trends related to the reduction of public debt, it is worth assessing the causes of this phenomenon as well. In modern conditions, it may not be difficult to achieve a lower burden on the budget by devaluing the national currency, but it may lead to other kinds of difficulties in economic development together with the discontent of citizens, and therefore, a possible negative social consequences or even political ones can be expected. Such an approach is undesirable and arises rather as a consequence of other economic problems that the state authorities have failed to solve. It is worth assessing the situation in terms of the level of public debt of the Kyrgyz Republic (Fig. 1).

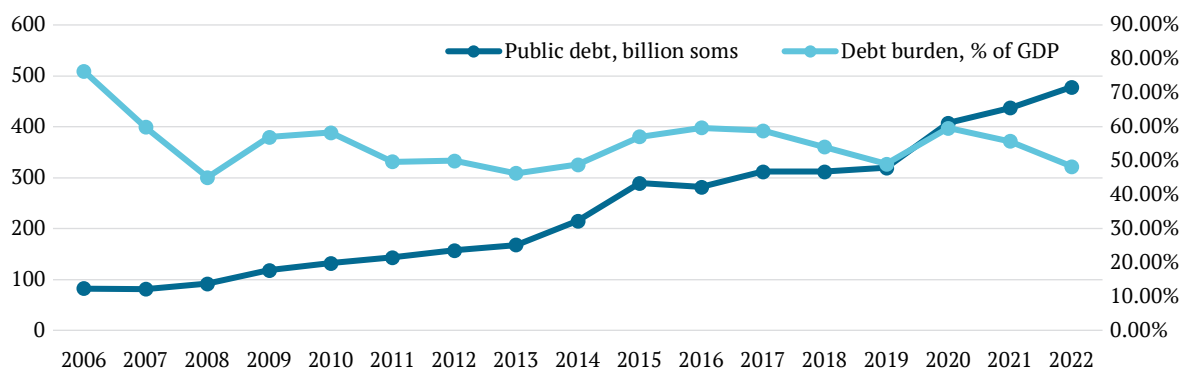


Figure 1. Change in public debt in monetary terms and relation to GDP, 2006-2022

Source: compiled by the authors based on State debt (n.d.), Inflation, consumer prices (annual %) – Kyrgyz Republic (2022)

As can be seen from Figure 1, the country's public debt in monetary terms (KGS billion) is growing, while the burden per GDP is gradually decreasing. Thus, such

trends could be caused by one of two reasons: rising inflation rate or rapid growth of GDP. The relevant data is shown in Figure 2.

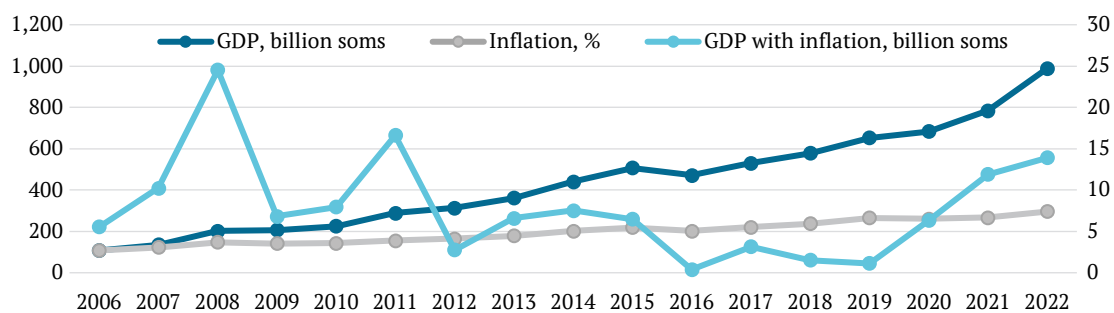


Figure 2. Data characterising the level of GDP in Kyrgyz Republic with and without inflation in KGS and inflation rate, 2006-2022

Source: compiled by the authors based on State debt (n.d.), Inflation, consumer prices (annual %) – Kyrgyz Republic (2022)

As can be seen from Figure 2, the level of GDP in nominal terms in the Kyrgyz Republic increased significantly: by 816%. Nevertheless, in real terms, the change was 174%, which also remains significant. At the same time, the growth in the level of public debt in the country was 73.68% over the selected period. Thus, it is possible to conclude that the reason for the reduction of public debt in the country was high inflation (which cumulatively for the selected period

was at the level of 224%), as well as rapid growth of GDP (by 174% including inflation), but not debt repayments by the state. Although inflation was at sane levels from 2012 to 2019, it increased significantly in 2020 and 2021 due to the onset of the COVID-19 pandemic and continued to rise in 2022 due to the onset of the Russian invasion of Ukraine and the negative effects it brought to the economic development of the Kyrgyz Republic (negative impact of

sanctions, complication of trade interactions, deterioration of the investment climate). It has been noted above that in the long term such trends may hurt the economic well-being of the country as a whole and its citizens in particular (Samus *et al.*, 2023). In this regard, the political authorities of the Kyrgyz Republic should change their

approach to fiscal and monetary policy, directing more efforts to fight inflation. It is also worth evaluating data that would characterise the situation concerning public debt dynamics in countries similar in their characteristics and development features to the Kyrgyz Republic. Such data are shown in Figure 3.

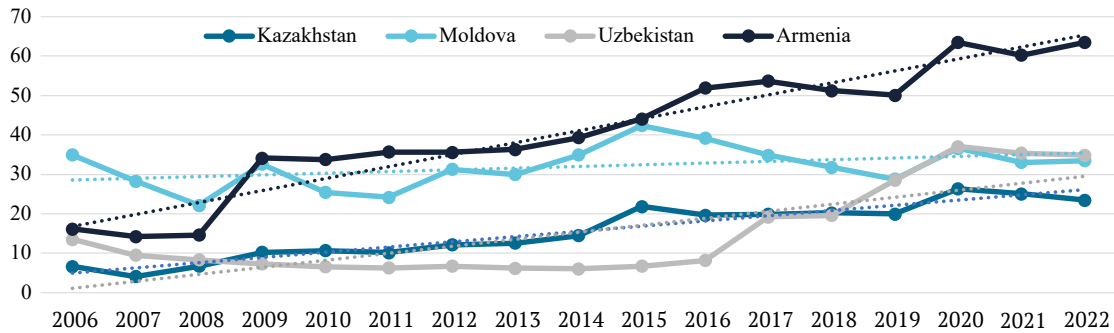


Figure 3. Data on dynamics of public debt-to-GDP ratio in Kazakhstan, Moldova, Uzbekistan, and Armenia, 2006-2022, %
Source: compiled by the author based on General government gross debt (2022)

As can be seen from Figure 3, most of the selected countries have an upward trend in the level of public debt. In particular, such a trend has been observed since 2008, which is associated with the global financial crisis. It is also worth noting that although the level of debt to GDP ratio in these countries is still small, such trends may lead to

negative consequences in the long run. Considering the statistics of public debt of most countries, it shows an upward trend, including concerning GDP. This also applies to developed countries. One of the examples of the reverse situation are such countries as Sweden, Switzerland, and Iceland. The level of their public debt to GDP can be seen in Figure 4.

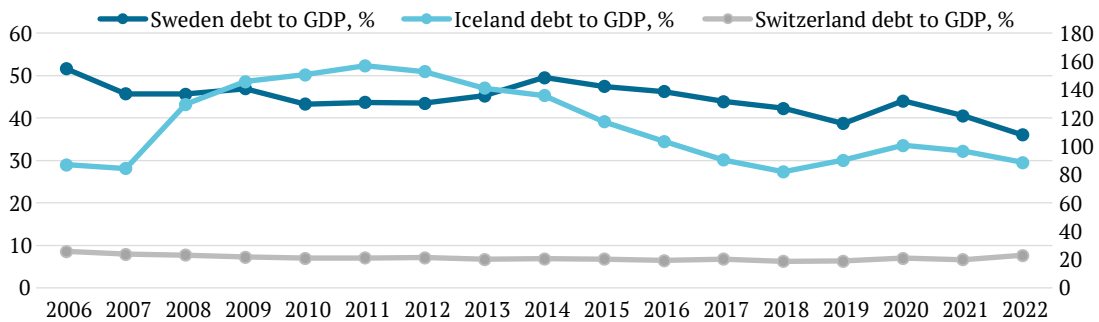


Figure 4. Data on public debt levels in Sweden, Switzerland, and Iceland, 2006-2022
Source: compiled by the author based on GDP (current US\$) – Sweden, Switzerland, Iceland (2022)

As can be seen from Figure 4, the level of public debt in these countries is gradually decreasing. To understand why this is the case, it is worth analysing

inflation, economic growth, and budget deficit in the same way. The situation in Sweden was analysed, which can be seen in Figure 5.

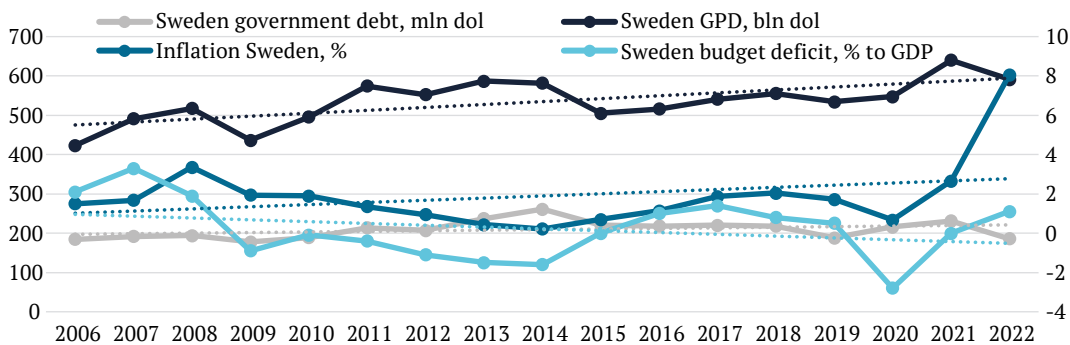


Figure 5. Data on inflation, GDP, public debt, and budget deficit in Sweden, 2006-2022
Source: compiled by the author based on Sweden government budget deficit (2022), Sweden: Inflation rate from 1988 to 2028 (2023)

As can be seen from Figure 5, the overall reduction in the level of debt burden in the country simultaneously accompanied the growth of GDP (by almost 40%); and overall growth in the level of public debt, but by the time of 2022 it was already at the level of the beginning of the period under consideration, i.e. it did not change even in nominal terms; low inflation (at the level of up to 4%

until 2022) and different indicators of the budget deficit, which, depending on the year, could turn out to be both positive and negative.

All this indicates that the reduction in the level of public debt to GDP in the country was caused by an appropriate budget policy. The data on the situation in Switzerland are also worth considering (Fig. 6).

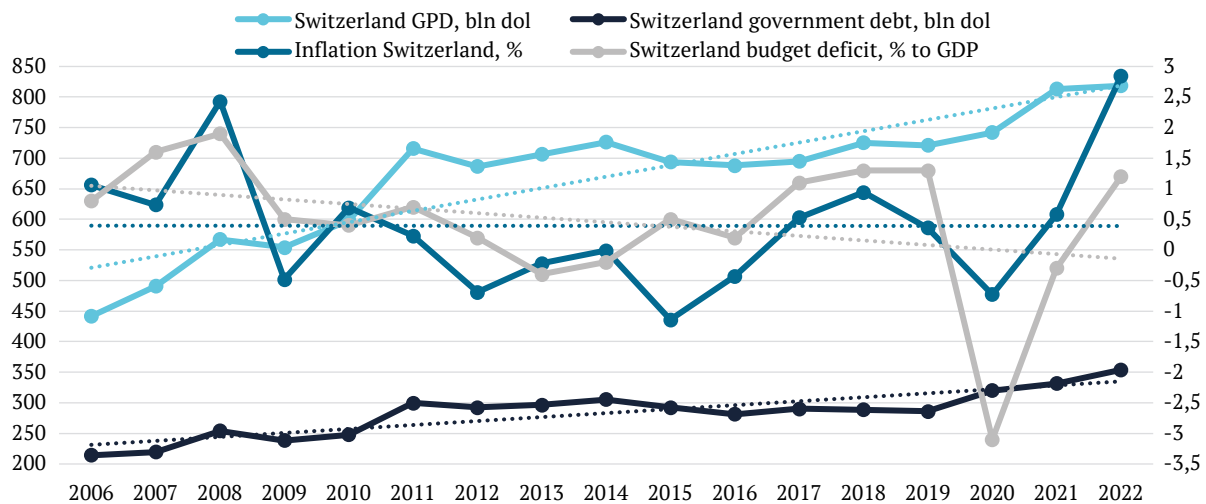


Figure 6. Data on inflation, GDP, public debt, and budget deficit in Switzerland, 2006-2022

Source: compiled by the author based on Switzerland: Inflation rate from 1988 to 2028 (2023)

As can be seen in Figure 6, Switzerland has experienced strong GDP growth, low inflation (deflation in some years), and mostly positive budget deficits. Nevertheless, public debt ratios increased over time, but at a lower rate than GDP (until 2020, when the increase was triggered by the start of

the COVID-19 crisis and subsequently by the start of the Russian full-scale invasion of Ukraine). This indicates that the reason for such trends was both the appropriate fiscal policy and the country's significant economic growth rates. Similar data are worth considering for Iceland (Fig. 7).

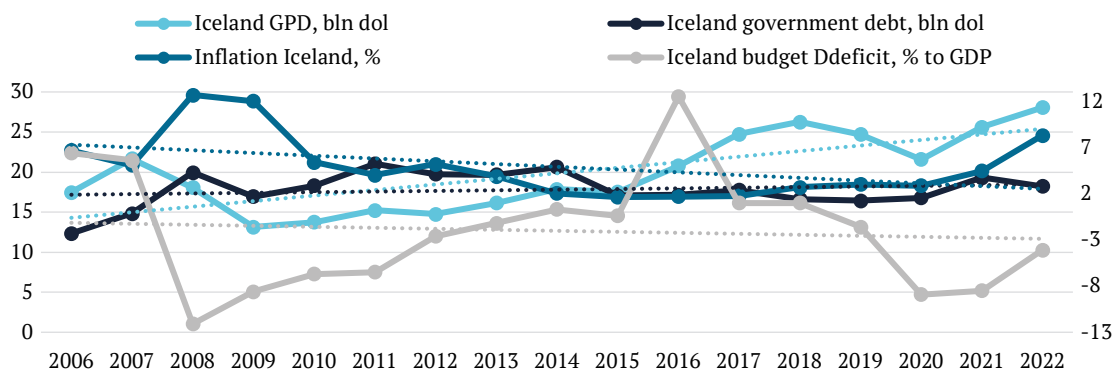


Figure 7. Data on inflation, GDP, public debt, and budget deficit in Iceland, 2006-2022

Source: compiled by the author based on Iceland: Inflation rate from 1988 to 2028 (2023)

In general, the decline in the level of public debt to GDP in Iceland started after 2011. As can be seen from Figure 7, this period of the country's functioning is marked by some key indicators: significant GDP growth; relatively low inflation; a near-zero budget deficit and in 2016 a large surplus (negative values started to emerge from 2020 onwards due to the onset of the COVID-19 crisis); and a decline in the nominal level of public debt. This indicates that the country pursued a strategy of deleveraging directly through loan repayments.

Thus, if a government aims to reduce its debt load, it should do so primarily by reducing public debt directly, rather than through any of the other instruments described in the study. While each situation may be unique, there are still consistent and similar principles to each approach. Thus, the priority to ensure the possibility of debt repayment is a budget surplus or near-zero deficit, because only in case of more inflows than outflows can the state allocate part of the funds to repay the debt. This, in turn, can be achieved either by reducing expenditures or increasing

revenues. Considering the revenue side, it is worth paying attention to the tax component and updating the existing policy in this area. This does not necessarily mean increasing the tax burden on citizens or businesses: revenue can be increased by ensuring that collection efficiency is increased and that businesses come out of the shadows. This also applies to customs, optimising procedures to combat smuggling. Increasing collections is also generally an effective policy, but there are several nuances to it.

The question of how businesses and the population react to it remains, as such steps are often not approved, which can lead to all sorts of consequences. It also increases the likelihood of increase in the shadow economy, increasing the share of enterprises that will try to avoid taxes. To combat the latter, there are appropriate mechanisms, in particular, the introduction of digital technologies and automation of the processes of collecting information and direct payments from entrepreneurs. Nevertheless, they are not yet widespread enough within government structures to eliminate such activities (or in any significant way). It is also worth noting that taxes primarily arise from income generation by businesses, especially exporters, and therefore activities aimed at supporting them are also effective.

Another possibility to achieve a budget surplus is to reduce expenditures. Since the reduction of social benefits is also often an unpopular policy on the part of citizens (moreover, it should be indexed every year, ideally by a level above inflation), the only way out is to reduce the state apparatus as much as possible. State actions should be aimed at optimising internal processes, allowing to reduce unnecessary expenditures, including in the context of projects managed by the government (Assoum & Alinsato, 2023; Dimnwobi *et al.*, 2023). Fighting corruption is also effective: since it is most often caused by excessive cost overruns in the implementation of projects, countering it can either reduce budget expenditures or increase the efficiency of the implemented projects. Both of these outcomes remain acceptable. Finally, it is worth noting that to reduce the debt burden, it may also be important to discuss with creditors what options remain for restructuring it. For example, if the state authorities manage to achieve lower interest rates or lengthen the debt repayment period, its instant redemption, this may make the task of debt repayment much easier.

■ DISCUSSION

In general, it remains acceptable for the Kyrgyz Republic to implement any of the above recommendations. Nevertheless, given the difficulties in the country caused by a rather high level of corruption, it is more effective to reduce costs in the country by ensuring more effective management of civil servants' activities. This can be achieved primarily through the introduction of new technologies, reduction of the role of the state, automation of many processes, staff reduction. Special attention should be paid to the role of the state. Countries with a low level of corruption often have a rather high level of state involvement in the management of economic processes, which may be paradoxical in some ways. The absence (or low influence) of this negative component is due to well-developed institutions and a suitable legal framework, which is also worth paying attention to in the fight against corruption (Baklouti & Boujelbene, 2022). Nevertheless, reducing the role of the state in economic

processes may help to combat this component by making it more difficult for the authorities to act in violation of state laws: however, it should be realised that such practices may only have a temporary effect. In turn, an increase in the tax burden can only lead to a worsening of the situation in this direction. In addition, it is worth considering the possibilities of debt restructuring. It is also worth understanding that such a policy in the country should be based on the real capabilities of the country in the context of how it can withstand the existing crises related to the consequences of the COVID-19 crisis and the complex geopolitical situation in the region (Elberry *et al.*, 2023). In any case, their policy should become such sooner or later if the country's goal is to ensure quality long-term sustainable development.

I. Hussain *et al.* (2022) and A. Aspide *et al.* (2022) analysed the impact of fiscal adjustments on public debt reduction. Their analysis showed that there is a clear relationship between public finance objectives and economic growth and that changes made in fiscal policy are more effective in stimulating economic growth but not necessarily for fiscal sustainability. In addition, they concluded that variables such as GDP growth as well as changes in the political sphere (elections and changes in government) significantly affect the change in the debt level cut-off. The study on public debt in the Kyrgyz Republic also concluded that the economic development of the country plays a significant role in this context. Nevertheless, it is difficult to agree with the conclusion that financial stability and economic growth should be achieved by different instruments of public policy. Thus, if financial stability is lacking, the flow of investment, especially foreign direct investment, may be significantly reduced, which in turn will lead to lower economic growth, and there are many examples of this (Heimberger, 2021; Trusova, 2022). Such assessments require additional analysis to form full-fledged conclusions.

The determinants of public debt reduction in Central and Eastern European countries were assessed by S. Semik & L. Zimmermann (2022). The results of the study showed that in this context the main factors are the importance of fiscal policy framework, economic growth, and the interest burden of the government to achieve a significant debt reduction. It is noteworthy that fiscal adjustments are most successful when they focus on reducing government expenditure, especially by reducing public employee compensation and social benefit payments. The study emphasises the positive impact of high real GDP growth rates on the likelihood of significant public debt reduction, highlighting the need for structural reforms to increase the pace of economic development of countries. The researchers also noted the correlation between changes in interest rates on debt service and its size. Thus, they noted that the higher the interest rates are, the more the public debt will be reduced due to the desire to reduce the growth of costs associated with its servicing. In general, the scientists' conclusions are confirmed by the assessments made within the framework of the study of the debt burden situation in the Kyrgyz Republic. Although economic development does have a positive impact on improving the situation with the level of liabilities in the country, however, to achieve qualitative results it is worthwhile to pursue a targeted policy in this area.

The interaction between public debt and economic growth was assessed by Z. Liu & J. Lyu (2020) and

S.K. Hilton (2021). The scholars noted that high fiscal discipline is crucial for the use of borrowed funds with a focus on priority projects, preferably infrastructure or investment projects. Such activities have a positive impact on the economic development of a country in the long run. Therefore, governments are advised not to expect immediate economic improvement in the short term due to effective debt management, but in the long term, a significant positive effect is expected from these activities. It is also worth being prepared for an increase in inflation in the short term along with an increase in debt levels with expectations of likely changes in the long term. The study on debt burden in the Kyrgyz Republic also concluded that one of the main components that should allow the country to achieve a reduction in the level of budgetary burden should be a directed policy for the payment of liabilities (which is fiscal discipline). It was shown that this is the only way to achieve a sufficiently high level of long-term economic development, which is in line with the conclusions of the study above.

The relationship between public debt and economic development has been studied by S.H. Law *et al.* (2021). Using data from 1984 to 2015, the researchers showed that there is a non-linear relationship between public debt and economic growth. The results emphasise the importance of institutions in influencing the relationship between public debt and economic growth, with better institutions mitigating the negative impact of high public debt on economic growth. In this regard, understanding the levels at which fiscal policy should operate to avoid excessive debt accumulation remains an important component (Broner *et al.*, 2022). The study on the debt burden situation in the Kyrgyz Republic also concluded on the role of institutions in achieving the goals of reducing the level of liabilities in the country. Based on selected developed countries, it was also shown that only through appropriate public policies aimed at debt repayment can sustainable financial development be achieved in the long term.

As part of their study, S. Bernardini *et al.* (2019) studied the experience of public debt reduction using data from the last 70 years. The analysis showed that there were about 30 recent cases where the ratio of public debt to GDP fell by more than 25%. At such times, countries were more likely to have had high inflation and growth rates, fiscal tightening, significant levels of economic development, debt restructuring, or standard methods of adjustment through spending cuts and tax increases (but this became more common after 1980). Some past practices, such as debt repayment through sudden inflation, are too impractical in the current realities, while the method related to cost reduction and tax increases can be considered more than viable. In the case of restructuring, although necessary in some cases, it cannot be used as a holistic method but must be supported by another methodology (i.e. cost reduction and tax increases).

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The study on the public debt situation in the Kyrgyz Republic also concluded that in the current environment, it is possible to achieve qualitative results in the long term only through the implementation of appropriate policies. At the same time, the country in recent years has also seen a trend towards a generally lower debt burden, but it was caused more by inflation and a relatively high level of economic development, which cannot be a sustainable model for the future. Scientists' estimates based on data for the last 70 years only confirm this concept.

■ CONCLUSIONS

Thus, the study identified three main factors that can lead to the reduction of public debt in countries: direct repayment of debt by increasing revenues and reducing budget expenditures; reduction of its real value due to high inflation (debt depreciation); significant economic growth and increase in the level of gross domestic output. The study concluded that in modern realities, the states that have achieved improvements in terms of the state of public debt have used instruments aimed at direct payment. Although there are still opportunities to reduce its impact through economic growth and inflation problems, this is less effective and applicable, given the likely negative short- and long-term consequences of such policies.

The study analysed the situation in terms of public debt of the Kyrgyz Republic: it was shown that generally positive dynamics are characterised by a reduction in the burden, but it was concluded that it was caused primarily by high inflation and significant growth rates. When analysing the EEU member countries, it was shown that they are generally characterised by trends that are more likely to increase the ratio of public debt to gross domestic product. To describe the necessary reforms for the Kyrgyz Republic, the dynamics in Sweden, Switzerland and Iceland were assessed, which also managed to achieve an improvement in the situation with public debt, but without high inflation. Based on this, conclusions were drawn as to what public policy should be in terms of debt management in the Kyrgyz Republic. In particular, it was concluded that there is a need to actively fight corruption and improve institutions in principle. Particular attention was paid to ensuring the effectiveness of public sector management. It remains relevant for future research to find other methods to improve the macroeconomic situation in the Kyrgyz Republic, in particular, to fight inflation, given the crisis in the world and the region.

■ ACKNOWLEDGEMENTS

None.

■ CONFLICT OF INTEREST

None.

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Світовий досвід скорочення державного боргу (на прикладі Швеції, Швейцарії та Ісландії)

■ **Анотація.** Скорочення державного боргу є одним з основних завдань формування бюджетної політики в сучасних кризових умовах. У зв'язку з цим вивчення досвіду різних країн у цій сфері є актуальним. Тому метою дослідження було надання рекомендацій щодо зниження боргового навантаження в Киргизькій Республіці на основі досвіду інших країн. Основними методами дослідження були історичний, порівняння та узагальнення. У дослідженні було проаналізовано фактори, що впливають на скорочення державного боргу в Киргизькій Республіці. Було зроблено висновок, що складовими, які можуть допомогти вплинути на боргове навантаження в країні, є інфляція, економічний розвиток та цілеспрямована політика держави щодо виплати боргів. Було показано, що в сучасних реаліях країни, які є успішними в цьому напрямку, найчастіше використовують останній підхід. Крім того, було безпосередньо проаналізовано ситуацію у Швеції, Швейцарії та Ісландії та надано основні рекомендації щодо того, як Киргизька Республіка може покращити свою поточну ситуацію в плані скорочення боргу. Ці рекомендації були зосереджені насамперед на боротьбі з корупцією та покращенні ситуації в контексті інституційного розвитку, а також на скороченні видатків для досягнення профіциту бюджету. Було рекомендовано не збільшувати податки безпосередньо для збільшення державних доходів, а підвищувати ефективність їх збору. Отримані за результатами дослідження дані можуть бути використані для формування державної політики у сфері управління державним боргом та бюджетом як у Киргизькій Республіці, так і в інших країнах

■ **Ключові слова:** фіскальна політика; інфляція; економічне зростання; бюджет; управління