

# Report on Bachelor / Master Thesis

Institute of Economic Studies, Faculty of Social Sciences, Charles University in Prague

<b>Student:</b>	<b>Josef Švéda</b>
<b>Advisor:</b>	<b>Jaromír Baxa</b>
<b>Title of the thesis:</b>	<b>Do markets believe in austerity? Did they ever believe?</b>

## **OVERALL ASSESSMENT** (provided in English, Czech, or Slovak):

*Please provide your assessment of each of the following four categories, summary and suggested questions for the discussion. The minimum length of the report is 300 words.*

### **Contribution**

In his thesis, Josef tests the effects of fiscal announcements on government bond yields. Under conventional wisdom, an announcement of an austerity programme shall be considered as a promise of lower taxes tomorrow, and the refinancing costs of government bond shall decrease. However, it is also known that fiscal consolidation can be self-defeating: When austerity is applied in slack, the GDP might deteriorate, and the overall debt/GDP ratio might increase despite the consolidation effort. In that case, the response of government yields might be perverse, and they might increase, rather than decrease after an austerity announcement.

To find out which effect prevails and when, Josef constructed his own database of fiscal announcements, using text-search in the Factiva database. Then, he performed panel regressions to estimate the effects of announcements on 10Y government bonds of the EU countries.

His results imply that especially during the crisis period, and among the PIIGS countries, fiscal announcements have large, significant and positive effects on government bond yields. In other words, markets did not believe in the positive effects of austerity in the crisis.

These results contribute to the debate of the appropriate role of the ECB in the EU. In particular, whether the ECB shall serve as a lender of last resort for the sovereigns, or the non-bailout clause shall be retained. This debate appears relevant in times when the new ECB's policy framework is being prepared and, at the same time, the ECB's interventions on bond markets were challenged by the German Constitutional Court.

Moreover, the thesis extends the previous findings in the literature in several ways. Notably, the utilization of text-search to create a database of fiscal announcements is new, and it challenges some of the previous results in the literature with results likely affected by selection bias.

### **Methods**

In general, the thesis employs two methodologies. First, it contains a carefully designed text-search experiment, which helps to create a database of fiscal policy announcements. Then, the daily data on bond returns are regressed on a set of covariates and dummy variables „comments“ (indicating a possibility of adoption of austerity policies) and „announcements“ of approved austerity measures. These panel data regressions are, from my point of view, appropriate, and reasonably adopted. The methodology itself is described quite well, and Josef is very transparent in a description of his text-search experiment.

### **Literature**

In line with my expectations.

### **Manuscript form**

The thesis is well-structured, contains many illustrative figures, reasonably written. However, from my point of view, it could be shortened. However, this applies to many diploma theses.

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## Summary and suggested questions for the discussion during the defense

Overall, I'm very enthusiastic about the thesis submitted by Josef Švéda. It is original, it contributes to current policy debates, and the results are challenging leading policies in the EU. Moreover, it addresses some of the issues with previous literature, in particular potential selection bias associated with selection of events used in regressions, by performing an extensive text search to create own database of fiscal announcements. Therefore, I warmly recommend to award the thesis by grade A, and I hope Josef will find some time and energy to shorten the thesis into an academic paper. I believe after some polishing, a paper based on this thesis can be published in a good economic journal, and it deserves to be presented on academic conferences. Such paper shall focus on (i) whether the text search actually matters; (ii) policy implications of the fact that the results are different in the crisis period, namely for the EU periphery.

**Suggested questions:** I think Josef could briefly summarize whether utilization of text-search matters and to present to what extent are the results different when a broader database of fiscal announcements is used.

## **SUMMARY OF POINTS AWARDED** (for details, see below):

<b>CATEGORY</b>	<b>POINTS</b>
<i>Contribution</i> (max. 30 points)	30
<i>Methods</i> (max. 30 points)	29
<i>Literature</i> (max. 20 points)	20
<i>Manuscript Form</i> (max. 20 points)	19
<b>TOTAL POINTS</b> (max. 100 points)	<b>98</b>
<b>GRADE</b> (A – B – C – D – E – F)	<b>A</b>

**NAME OF THE REFEREE:**

**Jaromír Baxa**

**DATE OF EVALUATION:**

**June 5, 2020**

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**Referee Signature**

**EXPLANATION OF CATEGORIES AND SCALE:**

**CONTRIBUTION:** *The author presents original ideas on the topic demonstrating critical thinking and ability to draw conclusions based on the knowledge of relevant theory and empirics. There is a distinct value added of the thesis.*

**METHODS:** *The tools used are relevant to the research question being investigated, and adequate to the author's level of studies. The thesis topic is comprehensively analyzed.*

**LITERATURE REVIEW:** *The thesis demonstrates author's full understanding and command of recent literature. The author quotes relevant literature in a proper way.*

**MANUSCRIPT FORM:** *The thesis is well structured. The student uses appropriate language and style, including academic format for graphs and tables. The text effectively refers to graphs and tables and disposes with a complete bibliography.*

**Overall grading:**

TOTAL	GRADE
91 – 100	A
81 - 90	B
71 - 80	C
61 – 70	D
51 – 60	E
0 – 50	F