Working Paper No. 879

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AUTHOR OR EDITOR

Julian A. Parra Carmiña O. Vargas

AUTHORS AND/OR EDITORS

Vargas-Riaño, Carmiña Ofelia

We argue that international lenders take into account that taxes (or subsidies) affect borrowers'

available income for debt repayments. Using an endowment-economy model, we show that by incorporating this fact into the analysis of financial crises from the pecuniary externality perspective, expost interventions are completely ineffective to manage crises and, instead, ex-ante capital controls are useful for correcting the externality that stems from the underestimation of the social costs of decentralized debt decisions.

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Update 10:30 a.m., 03/05/2016