The US, Economic News, and the Global Financial Cycle
by Boehm & Kroner

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This presentation does not reflect the views of the Bank of Italy
Summary

• Brilliant and simple idea
  • Great work on the dataset
  • Analysis very proficiently executed

• Few concerns

• Potential improvements on interpretation of results and historical narrative

• Short summary and then comments
This Paper

1. **US macro surprises** important **driver** of **global equity** prices
   - 12 crucial variables identified
   - Equity response similar in US and foreign countries
   - Large explanatory power at low frequency (Altavilla et al., 2017 JME)

2. **Mechanism & interpretation**
   - GFC driven by **US shocks** and **not common shocks**
     \[ \downarrow \]
     US equities relative inelastic to foreign surprises
   - Responses driven by **risk-taking behavior** of investors
Concern I: Surprises

• Surprises from financial market do not always have good econometric properties

1. FOMC surprises are predictable (Ramey, 2016; Miranda Agrippino & Ricco, 2021 AEJ:Macro)
   ⇓
   Regress surprises on lagged factors

2. Stock returns drift prior to FOMC (Neuhierl & Weber, 2021 WP)
   ⇓
   Regress surprises on past returns

• Is this an issue in this case? Perhaps for the low frequency analysis.
  • Explanatory power could be inflated
Concern II: Global Shocks

- Authors show that foreign shocks do not affect US equity

- Two concerns
  1. Other G7 economies are relatively small compared to the US

    ↓

    what about Euro Area or China surprises?

  2. US surprises could be better measured than foreign ones

    ↓

    this could explain larger statistical significance/explanatory power
Concern III: Real linkages

- Authors show that foreign equity response increases with financial openness

- What about testing whether real linkages can explain elasticity of returns to US surprises?

\[ \downarrow \]

di Giovanni & Hale (2021, WP): global production network explain the response of foreign equity returns to US monetary policy surprises
Interpretation

• Net of previous concerns results are really sharp
• Can we improve the interpretation and narrative?

**Stock Price Decomposition (Boyd et al., 2005)**

\[ \Delta q_{i,t} \approx c_i \left[ \Delta g_{i,t} - \Delta ep_{i,t} - \Delta r_{i,t} \right] \]

- Use 10-year govt. bond yield to estimate \( \Delta r_{i,t} \)
- Stock & bond yield co-movement informative about dominant channel
- If \( \text{cov}(\Delta q_{i,t}, \Delta r_{i,t}) < 0 \) ⇒ interest channel dominant
- If \( \text{cov}(\Delta q_{i,t}, \Delta r_{i,t}) > 0 \) ⇒ cash flow & risk premium channel dominant
Interpretation

• Combine macro surprises from **event-studies** with **structural identification** framework
  
  • Karadi and Jarokinsky (2020, AEJ:Macro)
  
  • Cieslak and Schrimpf (2019, JIE)

Cieslak and Huan (forth, JFE)

Identify cash flow, monetary news and risk premia shocks in daily VAR.