Discussion of “International Spillovers and Local Credit Cycles” by Y.S. Baskaya, J. di Giovanni, S. Kelemli-Ozcan, M. F. Ulu

Arnaud Mehl
Paris, 30 June 2017

The views expressed here are those of the authors and do not necessarily reflect those of the ECB or the Eurosystem
Descriptive stats

- 1 related JIE paper
- 4 talented economists
- 6 prestigious commentators
- 13 presentations in conferences and seminars
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....

• 53 million observations!

No great comments left!
My discussion

• Praise
Clear story...

↓ VIX  ➞  ↑ K flows  ➞  ↓ i  ➞  ↑ Credit
Praise

- Clear story...

\[ \downarrow \text{VIX} \Rightarrow \uparrow \text{K flows} \Rightarrow \downarrow i \Rightarrow \uparrow \text{Credit} \]

- Very polished paper
- Highly granular data
- Clear theory and identification strategy
- Economically important effects (40% of observed cyclical credit growth!)
- Policy relevant ("financial trilemma")
My discussion

- Praise
- 3 points

↓ VIX ➔ ↑ K flows ➔ ↓ i ➔ ↑ Credit

Minor quibbles on instrument choice
My discussion

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- 3 points

Philosophical remarks on capital flows

Minor quibbles on instrument choice

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Philosophical remarks on capital flows

Minor quibbles on instrument choice

Comments (perhaps) interesting but likely outside the scope of the paper
Minor quibbles on the instrument (VIX)

• Poorer signals since 2008 crisis?
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- GARCH forecast of volatility
- Implied volatility (VIX)
- Risk premium

Events: Lehman, Greece, China, Brexit, Trump
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- Poorer signals since 2008 crisis?
- Old-fashioned?
  - Dollar index (Shin) or EPU (Bloom and co) better measures?
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• Dirty metric of risk aversion?
  - Why not Bekaert et al. as baseline/instrument?
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(Bekaert, Hoerova, Lo Duca, JME, 2013)
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• Uncorrelated with local risk?
  o Local Turkey risk globally systemic? (“Fragile 5”)
Minor quibbles on the instrument (VIX)
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- US index ill-suited for a European country like Turkey?
  - Role of (deleveraging of) European banks
  - VStoXX?
Minor quibbles on the instrument (VIX)

Currency composition of Turkey’s debt liabilities (2012) (updated from Lane & Shambaugh, 2010)

- US dollar: 61%
- Euro: 32%
- Japanese Yen: 7%
• **US index ill-suited for a European country like Turkey?**
  - *Role of (deleveraging of) European banks*
  - *VStoXX?*

• **Valid instrument?**
  - *Heuristic test (beta IV ≠ beta OLS) vs…*
  - …*Power test: “F > 10” rule of thumb misleading (KP test more “kosher”)*
  - …*Orthogonality test: Sargan/Hansen overidentification test (if # instruments sufficient)*

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  - Can VIX (Z) influence credit (Y) independently from capital flows (X) ? (e.g. “animal spirits” induce banks to lend more)

\[ X \rightarrow Y \]
\[ Z \]
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  o Portfolio flows more sensitive than FDI to risk aversion shocks?
  
  o Analogies with your JIE paper
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• Bias in capital flow data due to “passive” allocation?
  o Capital flows to EMEs/Turkey no matter what due to need to stick to portfolio benchmarks
Philosophical remarks on capital flows

(Ahmed, Curcuru, Warnock, Zlate, 2016)

Normalized relative weight measure flat, suggesting that changes in portfolio shares were due to the strong performance of EME equity markets (in dollar terms), not to an active increase in portfolio allocations to EME equities.
(Perhaps) interesting comments but outside the paper’s scope

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  - *Do banks borrow more from syndicates?*
  - *Do banks issue bonds?*
  - *Do banks receive*
  - *In which currency?*
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• Policy trade offs?
  – Loss of external competitiveness (if TRL loans) vs. financial stability problems (if FX loans)