Discussion: Avdjiev, Du, Koch and Shin (2017): «The dollar, bank leverage and the deviation…»

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Disclaimer: Views expressed should not be interpreted as reflecting those of Norges Bank.
The Triangle

- Stronger dollar widens CIP-devs and contracts XB-dollar lending
Generality and interpretation of results?

- Suggested relationships based on general arguments/model

Focus on:

- Empirical validity of relationships over time, interest rates data?
- Empirical validity of relationships across countries/currencies?
- Is there an alternative interpretation of data?
Dollar and cross-currency basis

Correlation absent pre-crisis, appears post-crisis

EURUSD 5y basis swap

USDEUR spot (higher values=stronger USD)
Need to look for post-crisis factors

- Deviations and correlation emerge post-crisis

- What has changed since the crisis?
  - ....financial regulations and transactions costs
  - risk-conciuosness, and risk premia
  - Monetary policies: ZLB, QE,…

- Unconventional policies behind unconventional deviations and correlations?
The XC-basis and the credit spreads - reflects their gap?

Credit spreads in EUR (financials 5-7 years, Barclays index)
Credit spreads in USD (financials 5-7 years, Barclays index)
EURUSD basis swap 5y (rhs)
XC-Basis largely reflects credit spread gap?

Source: Syrstad (2017)
Central banks’ balance sheets and spreads?

Source: Syrstad (2017)
Central banks’ balance sheets and dollar?

Source: Syrstad (2017)
Central bank policies behind USD and Basis?
Strong dollar or fall in commodity prices?

4 commodity currencies in the sample; (NOK, CAD, AUD, NZD)

- Strong dollar, fall in dollar-denominated commodity prices
- Fall in commodity prices, strong dollar bilaterally
- Two negative shocks to banks’ balance sheets in commodity producers
- Overstate the importance of dollar for banks equity and funding conditions in commodity producers?
Strong dollar, fall in commodity prices

Source: Naeimi (2013)

Source: Bloomberg, Global Financial Data, AMP Capital
Fall in commodity prices, strong $ bilaterally
Dollar and commodity producers
Mixed results for commodity currencies

- When substantial revenues in USD and costs in local currency, strong dollar eases funding conditions for borrowers, and their banks?
- Outweigh the effects of fall in commodity prices on banks’ equity and funding conditions?
- Explain why the results for commodity currencies are mixed?
Strong dollar good for commodity producers?
An alternative interpretation of results?

CB policies → USD → Commodity prices

XC-Basis → USD → XB-$lending
In summary

- An important paper with many interesting and striking results

- Robust to extensions of information set?
  - Other interest rates data
  - Unconventional policies
  - Commodity prices.
Appendix
Similarly in the case of yen...
Funding costs, spot and BOJ Balance sheet
«Funding uncertainty» and VIX

Source: Larsen (2017)
Strong USD raises funding uncertainty?

«Funding uncertainty» count in Norwegian business daily (DN)

Source: Larsen (2017)