

*Comments on*  
*“The Effect of Global Liquidity on Corporate Financing in Mexico”*  
*by*  
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# *Outline*

- Summary of paper
- Global liquidity
- Main result # 1
- Main result # 2
- Main result # 3
- Global liquidity, cont.
- Suggestions for improvement



## *Summary of Paper (1)*

- The paper uses Mexican quarterly credit- and firm-level data covering the 2003 to 2014 period to show that:
  - 1) “increased participation in international bond markets translated into a reduction in domestic credit to these [non-financial private Mexican] firms”
  - 2) “the increase in global liquidity significantly reduced international borrowing costs for large debt-issuing firms in Mexico”
  - 3) “as large firms have turned away from domestic financing sources, commercial banks in Mexico have been able to funnel more resources to SMEs”



## *Summary of Paper (2)*

- In sum, the story of the paper is as follows:
- Increase in global liquidity =>
- International borrowing costs decrease=>
- Large issuing firms obtain more funds abroad=>
- Large issuing firms need less domestic credit=>
- More domestic credit becomes available to smaller firms
- In other words, it's all about global liquidity!



## *Global Liquidity*

- “Global liquidity is an amorphous concept. The Usual Suspect for any event or dynamic too complicated to explain, global liquidity is the Keyser Söze of international finance.” (Carney 2011)
- In other words, it is unclear what the term “global liquidity” means – yet “global liquidity”, or changes in “global liquidity”, is often used as a “catch-all” explanation for all kinds of developments in international finance.



## *Main Result 1 (1)*

- 1) “increased participation in international bond markets translated into a reduction in domestic credit to these firms”
- The results of the binary choice models show that when the cost of issuing a bond abroad decreases relative to the (counterfactual/estimated) cost of issuing domestically then a firm is more likely to issue abroad. (Table 4).
- This does not link participation in international bond markets to a reduction in domestic credit.



## *Main Result 1 (2)*

- The paper shows a plot displaying that external bond issuance to non-financial corporations in Mexico increased dramatically from mid-2009 and onwards while domestic bond issuance as well as domestic credit also increased but at a slower pace (Figure 2), and the paper shows a plot displaying that domestic commercial bank credit in MXN to large firms with debt issuance stalled/declined around 2009 and onwards (Figure 3).
- The paper does not connect the two, i.e. the paper does not investigate a causal relationship, if any, between participation in international bond markets and a reduction in domestic credit.



## *Main Result 1 (3)*

- In fact, since the former (i.e. increase in external funding in particular) is far more pronounced than the latter (i.e. the decline/stall in domestic credit), this might suggest that increased participation in international bond markets has only a limited effect on the amount of domestic credit obtained.
- This points to an interesting and alternative research question, namely: Is it the case that increased availability of (low-cost) external funding increases firms' net-borrowing?





## *Main Result 2 (1)*

- 2) “the increase in global liquidity significantly reduced international borrowing costs for large debt-issuing firms in Mexico”
- The paper defines global liquidity as total credit to non-residents in USD and EUR. This is a very narrow definition of global liquidity that requires some discussion/justification.
- More importantly, yes, the paper finds that global liquidity significantly reduced international borrowing costs for large debt-issuing firms (Table 2). But it also finds that global liquidity significantly reduced domestic borrowing costs for debt-issuing firms (Table 3).



## *Main Result 2 (2)*

- In fact, the effect of global liquidity on international versus domestic bond interest rates appears statistically indistinguishable (coefficient estimates are of the same sign and roughly within two standard deviations of one another).
- If an increase in global liquidity reduces both international and domestic interest rates, and in tandem, the increase in participation in international bond markets does not seem to be driven by changes in global liquidity.
- This is consistent with the results reported in Table 4 where global liquidity is found to be insignificant when estimating the probability of issuing in international bond markets.



## *Main Result 3 (1)*

- 3) “as large firms have turned away from domestic financing sources, commercial banks in Mexico have been able to funnel more resources to SMEs”
- This result comes from regressing “new loans granted to SMEs” (SME) on the focal variable “new bank loans to issuing firms” (Issuer). The estimation results are reported in Table 5.
- Table 5 shows five separate estimations, three of which are IV estimations where the IV replacing Issuer is insufficiently described as “global variables” from “the previous section”.



## *Main Result 3 (2)*

- Two estimations show Issuer to be highly insignificant thereby suggesting that whether or not large firms issue bonds in international markets has no effect on domestic commercial banks' funding of SMEs (i.e. the opposite of Main Result 3).
- The three IV estimations show IV to be highly significant, thus implying the opposite (i.e. as stated in Main Result 3).
- Without properly defining the IV it is not possible to assess the validity of the IV estimations.
- Overall, at best the results seem inconclusive.



## *Global liquidity, cont. (1)*

- What does the paper show about the effect of global liquidity on corporate financing in Mexico?
- Not much:
- Global liquidity does not appear to have an effect on participation in international bond markets
- Global liquidity appears to have the same effect on interest rates in both international and domestic bond markets
- Perhaps it's not all about global liquidity after all?



## *Suggestions for Improvement (1)*

### ■ Presentation

- data: the novelty of the paper is the data set; currently it is impossible for a reader to fully understand the presented analysis due to the lack of a coherent data description. At least provide a table showing summary statistics
- explain the variation in the number of observations included in the various regression models (Example: There are 1130 observations in the logit estimations. Credit-level data shows 226 international bond issuances and 316 domestic bond issuances. Firm-level data shows 232 firms obtained funding from either international or domestic debt issuance. Why 1130?)
- define variables properly; add equation numbers



## *Suggestions for Improvement (2)*

### ■ Structure

- Certain parts of the literature review section clearly belong in the Introduction
- Certain parts of Recent trends in corporate financing clearly belong in a Results section

### ■ Argumentation

- “our preferred estimation is...” Why? Based on what?
- “we assume...” Why? Based on What?
- discuss and justify assumptions; provide an explanation/argument for why estimation “this” is preferred relative to estimation “that” etc.



*Thank you!*

