

Comments on Erik Feyen, Swati Ghosh, Katie Kibuuka and Subika Farazi:

**“Global liquidity and external bond issuance in emerging
markets and developing economies”**

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The views expressed in this presentation are strictly personal and do not necessarily reflect those of Banco de España.

Structure of comments



1. Conclusions
2. Setup and objectives
3. Data
4. Sample
5. Literature, theoretical framework and specifications
6. Robustness tests and interpretations
7. Conclusions

General comment

- Very promising paper that may become important contribution to the literature
 - Very few empirical studies on impact global factors on bond issuance emerging and developing economies (EMDEs) (Lo Duca, Nicoletti and Martinez, ECB WP, 2014)
 - Use of two impressive data-sets
 - Large amount of results
- => Many ideas from paper

Main conclusions paper



- Global factors matter greatly for external bond issuance by EMDEs
- Improvements in global liquidity as proxied by US financial conditions indicators:
 - Increase propensity of EMDE external bond issuance
 - Decrease EMDE external bond yields and spreads
 - Raise EMDE external bond maturity
- Support for risk-taking channel of exchange rate appreciation (Borio and Zhu, 2012; Bruno and Shin (2015a, 2015b))

Setup and objectives paper



- Very ambitious paper:
 - All issuing sectors (financial, non-financial, sovereign)
 - 2 large and complex datasets
 - 5 empirical research questions:
 - Explain determinants of propensity to issue
 - Explain determinants of bond yields
 - Explain determinants of bond maturity
 - Country \Leftrightarrow global determinants
 - Risk-taking channel

=> Authors can touch only the surface in several instances

Data

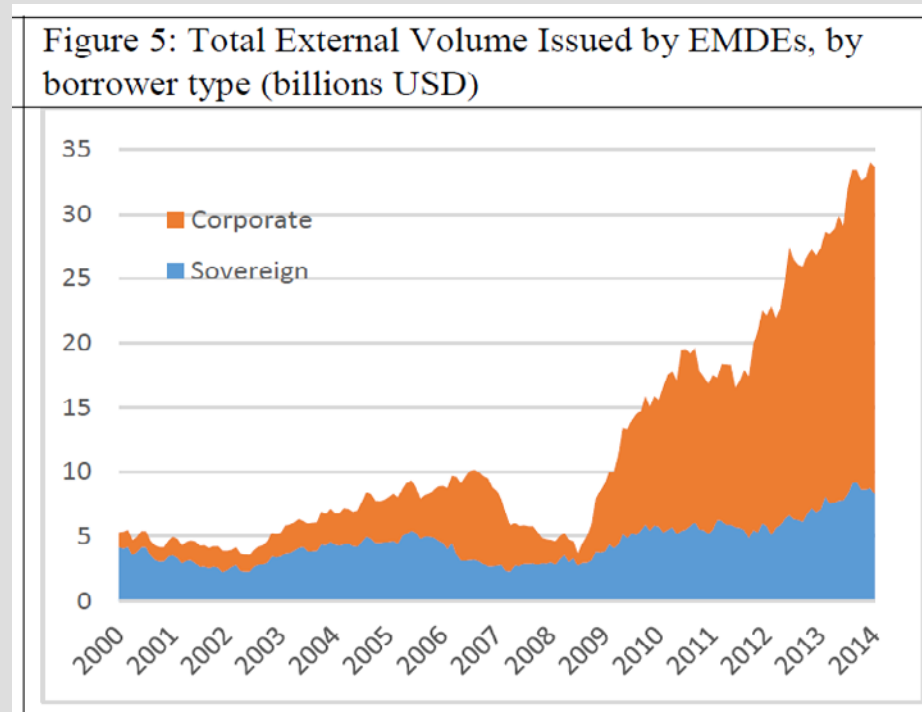
- 2 data-sets:
 - Country-industry panel: 71 countries, 7 industries, monthly data 2000-2014, around 84,000 observations.
 - Bond tranches data-set: 6,925 bond tranches.
- ⇒ reader has to understand many data dimensions.
- Understanding data description challenging at times:
 - Figures 4-9, 15: disconnect monthly data charts and annual figures text.
 - Abbreviations; figures/tables incl./excl. China.
 - Post-crisis 2009-2014 ⇔ Post-crisis 2011-2014.
- Figures 12-14, maturing amounts 2015-2035 ⇒ academic research or policy paper? Suggest to streamline.

Data

- Which definition of external bonds is used?
- Issues:
 - Which criterion is followed: nationality of issuer, country of domicile of issuer, etc.
 - Includes international bond issuance by offshore financial vehicles (often located in NL/LU/IE) of EME firms as ultimate parent company? Important especially for BRA, MEX, RU and South-Africa.
 - See Alberto Fuentes and José Maria Serena, “How EME firms borrow in international bond markets: Regulation and credit risks”, Banco de España, 2015.

Sample

- All externally issued bonds issued by banks, non-bank financial corporations, non-financial corporations and sovereigns.
- First question:



Since 2009, surge in corporate issuance: If you want to investigate role of global liquidity, why include sovereigns?

Literature and specifications

- Empirical and theoretical investigations of the financing decisions of non-financial firms and the funding decisions of banks are treated separately => different mechanisms and channels [Van Rixtel, Romo Gonzalez and Yang, BIS WP, 2015, forthcoming].
 - Non-financial firms, external finance: bank debt; debt securities; equity; trade credit => *choice/trade-off between debt and equity*. CF literature always excludes banks.
 - Banks: retail deposits; interbank loans; debt securities; CB liquidity [*direct link to global liquidity*]; [equity] [*regulatory*] => *choice/trade-off between deposits and wholesale funding/CB liquidity*. Huge literature on role deposits.
- => paper has no discussion at all of determinants of bond issuance by either banks, NFCs or sovereigns.

Literature and specifications

- Role of internal capital markets of global banks: many EMDE banks are owned by banks from advanced economies => how does global liquidity work here?
=> the moment you include banks, the mechanisms and channels become very blurred.
- Specification of yield and maturity equations: no discussion and disconnect with corporate finance (CF) literature.
- Specification yield (Table 5): maturity as control.
- Specification maturity (Table 6): yield not included as control => CF literature: “market timing” to current or expected interest rates important for issuance maturity.
- Specification second model excluding Chinese issuance (Tables 5 and 6): Estimation without domestic pull factors?

Literature and specifications



- Importance of financial reform and international liberalization: 71 EMDEs, speed and path of financial reform should vary substantially across these countries, may be highly significant for access to international bond markets.
- Specifications of interaction country characteristics with global factors (Appendix 3): 60 additional regressions ...

Robustness tests and interpretation

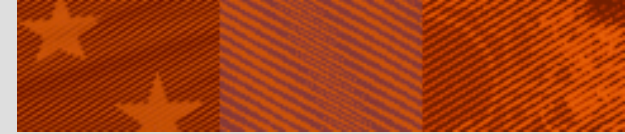
- Discussion of statistical properties and statistical robustness tests.
- Robustness tests using alternative explanatory variables:
 - Paper uses MOVE, country-period fixed effects, US EPU index
 - Domestic pull factors are very general, do not differentiate between different categories of issuers
 - Domestic pull factors with yearly frequency: Use higher frequency financial market variables, given monthly frequency regressions?
 - Domestic monetary policy excluded: obviously important for funding decisions banks but also for NFCs; not part of global liquidity?

Robustness tests and interpretation



- Possible existence of selection bias: some corporations and sovereigns are excluded from the sample by self-selection, as they decided not to issue. To test for selection bias, apply Heckman's 2-stage correction (Heckman, 1974, 1976 and 1979). See Eichengreen and Mody (1998b).
- Literature suggests that bond redemptions are important in driving new bond issuance ("roll-over" channel) (Morris and Shin, 2009; Admati and Hellwig, 2013). For corporate sector possibly not crucial, given surge in issuance in recent years, but may be very important for sovereign issuance.

Robustness tests and interpretation



Alternative hypotheses:

I. Fuertes and Serena (2015):

I. Weaker EME NFCs issue in less regulated markets (US 144A, Eurobond markets).

II. *Propensity to issue bonds by EME NFCs in these markets has increased significantly since the financial crisis: Regulation vs. global liquidity?*

II. Global trend towards direct finance: Disintermediation vs. global liquidity?

III. China?

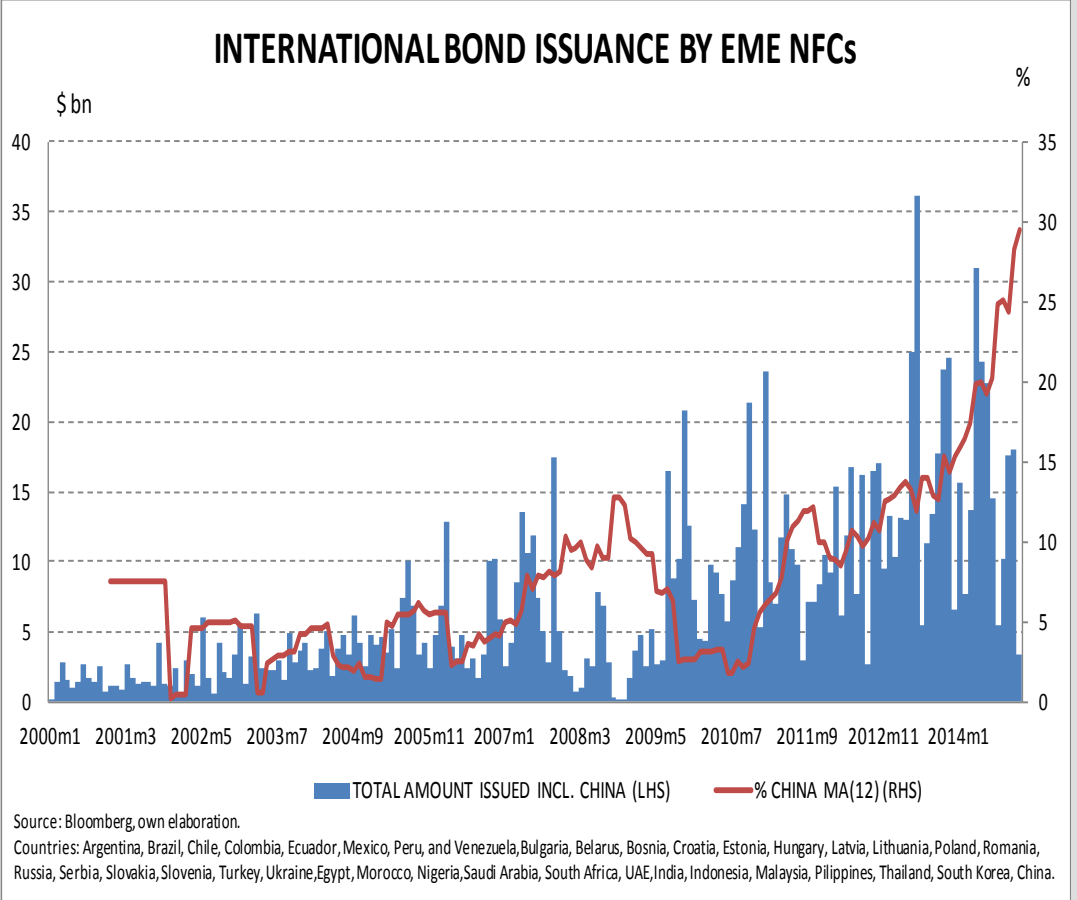
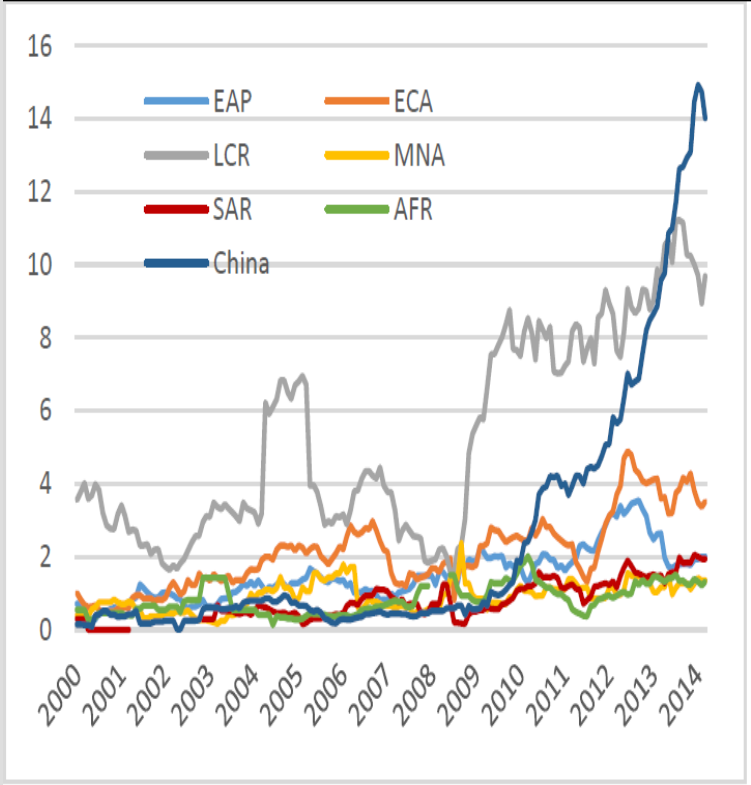
IV. Other?

Robustness tests and interpretation



China: How does global liquidity explain the surge in Chinese issuance? Share of 10% in 2011 to 30% in 2014.

Figure 4: Total External Volume Issued by EMDEs (billions USD)



Source: Bloomberg, own elaboration.
 Countries: Argentina, Brazil, Chile, Colombia, Ecuador, Mexico, Peru, and Venezuela, Bulgaria, Belarus, Bosnia, Croatia, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Russia, Serbia, Slovakia, Slovenia, Turkey, Ukraine, Egypt, Morocco, Nigeria, Saudi Arabia, South Africa, UAE, India, Indonesia, Malaysia, Philippines, Thailand, South Korea, China.

Fuertes and Serena (2015)

Conclusions

- Promising paper with lot of potential to exploit impressive datasets
- But focus:
 - In-depth analysis of issuance by separate sectors (financials/banks, NFCs, sovereigns) (80,000 obs ...)
 - Think about appropriate specifications (literature)
 - Forget about explaining yield and maturity in this paper
- Robustness tests:
 - Statistical properties
 - Choice of explanatory variables
 - Alternative hypotheses