

Comments on *“Global Transmission of FED Hikes: Role of Policy Credibility & Balance Sheets”*

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Brookings Papers on Economic Activity

Washington, DC

September 28, 2023

Key Question

WHY THIS???

Emerging markets have coped with the rate shock surprisingly well

But the real test is yet to come



Source: *Economist*, 10/13/22



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AND NOT THIS???

Taper Tantrum



Source: *Economist*, 06/22/13



My Comments

- 1. Quick Summary
(with editorial comments)**
- 2. The Broader Context:
Emerging Market Resilience**
- 3. Concerns: Data and Estimation**



Quick Summary

1. **Lit Review/framing:** financial channels of transmission of US monetary shocks
 - *Caveat: Trade? Commodities?*



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2. **Data:** key measures of monetary policy credibility and FX exposure
 - *But confidential...*
3. **Estimation :** Local projections of US monetary policy surprises
 - Effect on GDP, CPI, policy rate, ER, UIP deviations, capital inflows
 - 3 main comparisons: (a) for AEs vs EMs
 - (b) EMs with more credibility vs. less credibility
 - (c) EMs with more FX exposure vs. less FX exposure
 - *Lots of results, but some tricky to understand (especially FX exposure)*



Quick Summary

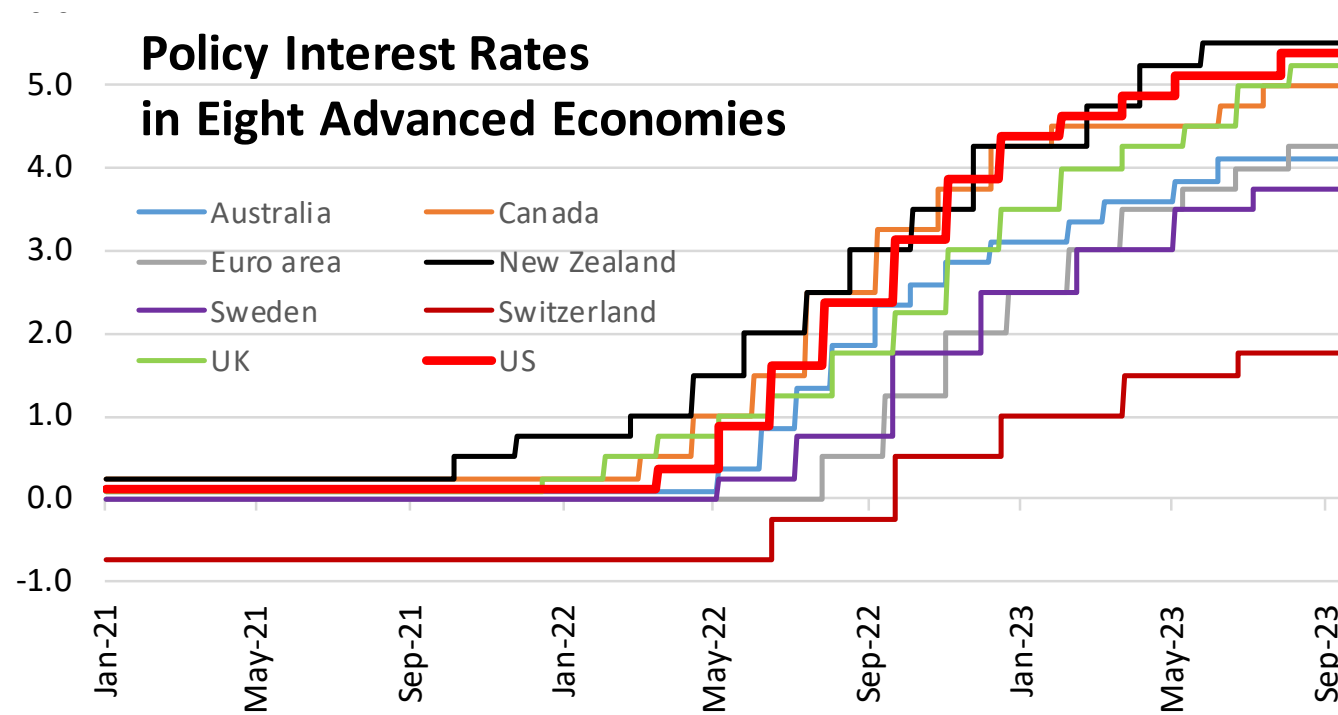
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 - (c) EMs with more FX exposure vs. less FX exposure
 - *Lots of results, but some tricky to understand (especially FX exposure)*
4. **The punchline: Does improved credibility and reduced FX exposure explain the recent resilience of EMs to recent US rate hikes?**
 - *Probably plays a role, but many other factors and just too soon*



The Broader Context:

Emerging Market Resilience

Rapid Global Tightening

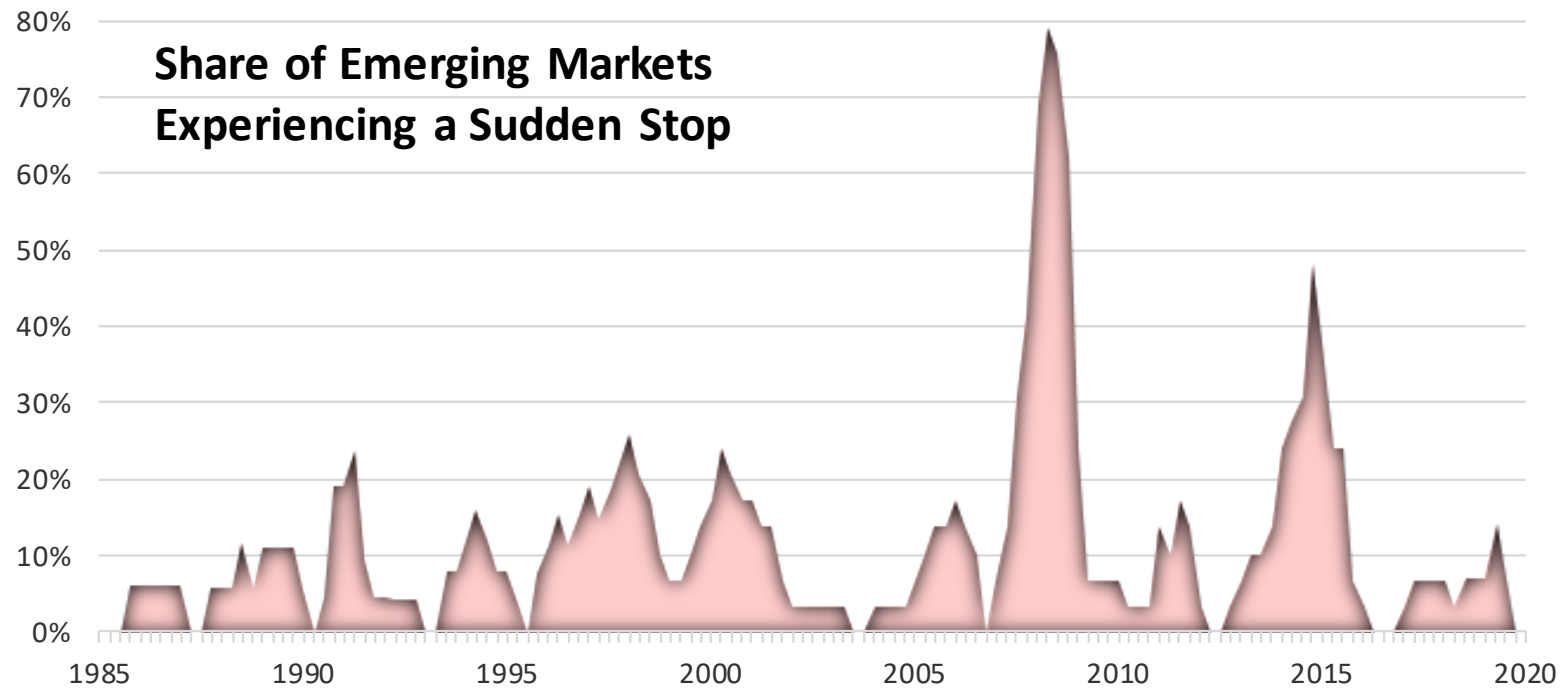


Notes: US policy rate is the average of the range set by the Federal Reserve. ECB is the interest rate on main refinancing operations (MRO).

Source: Bloomberg. Data from 01/01/21 through 09/22/23.



EM Resilience: Fewer “Sudden Stops”

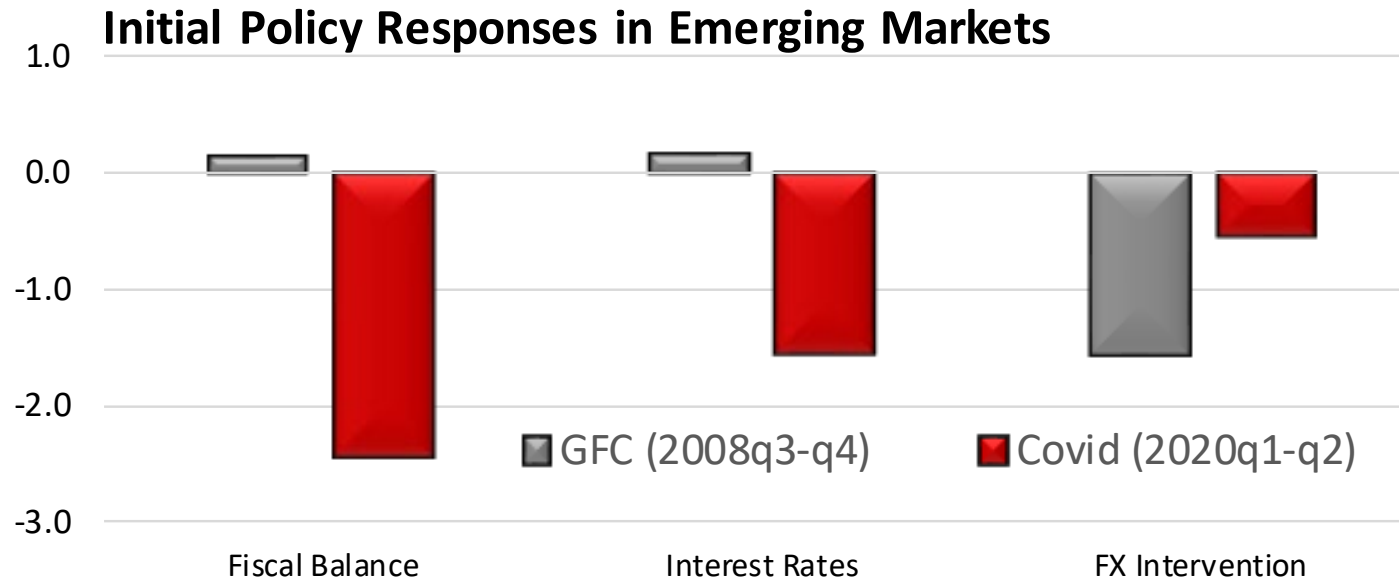


Notes: Data from 1985q4 through 2020q2. A sudden stop is defined as a sharp decrease in gross capital inflows by foreigners relative to a country-specific historic average. See Forbes and Warnock (2012 and 2021) for details.

Source: From Forbes and Warnock (2021).



EM Resilience: *Ability to Use Countercyclical Policy*



Notes: Initial policy response during Global Financial Crisis (GFC) is defined as 2008q3-q4 and for Covid is for 2020q1-q2. Fiscal balance is the change in the primary fiscal balance relative to GDP. Interest rates is the change in the policy interest rate. FX intervention is the change in FX reserves relative to per capita GDP. See Bergant and Forbes (2023) for a discussion of data sources and methodology.

Source: Based on data compiled for Bergant and Forbes (2023).



EM Resilience: Other Explanations?

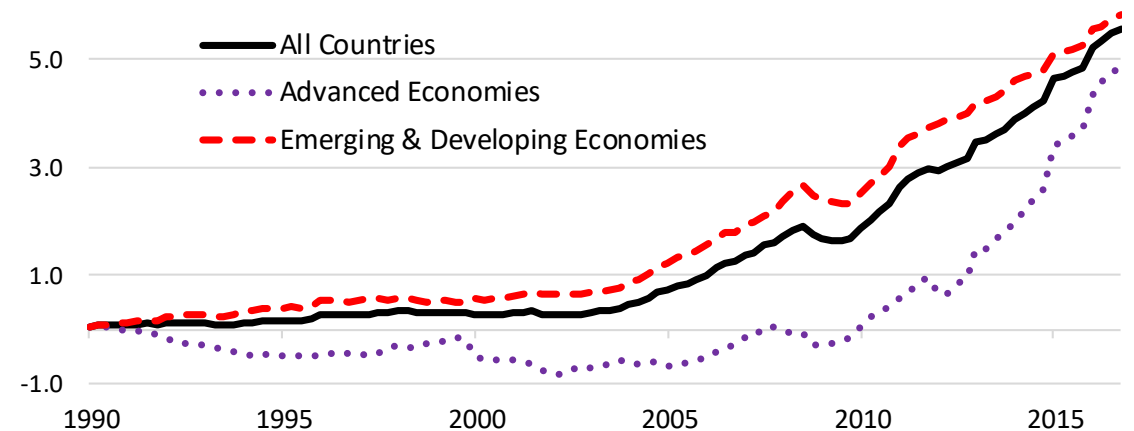
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2. Gross capital inflows ↓



EM Resilience: Other Explanations?

1. Current account deficits ↓
2. Gross capital inflows ↓
3. International reserves ↑
4. Macroprudential regulations ↑

**Average Macroprudential Policy Stance
Annually by Country Group**



Notes: Macroprudential data based on data from Alam et al. (2019). Country classification based on IMF World Economic Outlook database (2018).

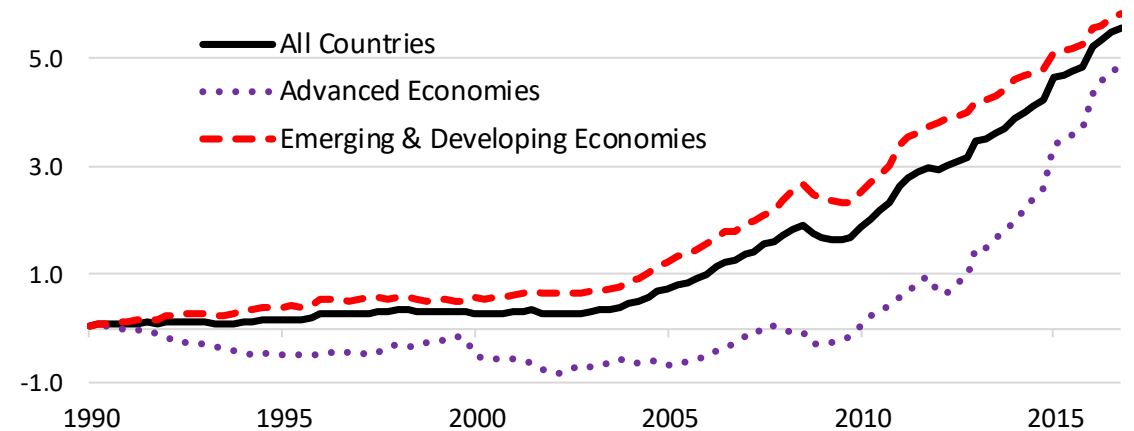
Source: Taken from Figure 1 in Forbes (2021). "The International Aspects of Macroprudential Policy," in *Annual Review of Economics*, Vol 13: 203-228.



EM Resilience: Other Explanations?

1. Current account deficits ↓
2. Gross capital inflows ↓
3. International reserves ↑
4. Macroprudential regulations ↑
5. Central bank credibility ↑
6. Share of borrowing in FX ↓

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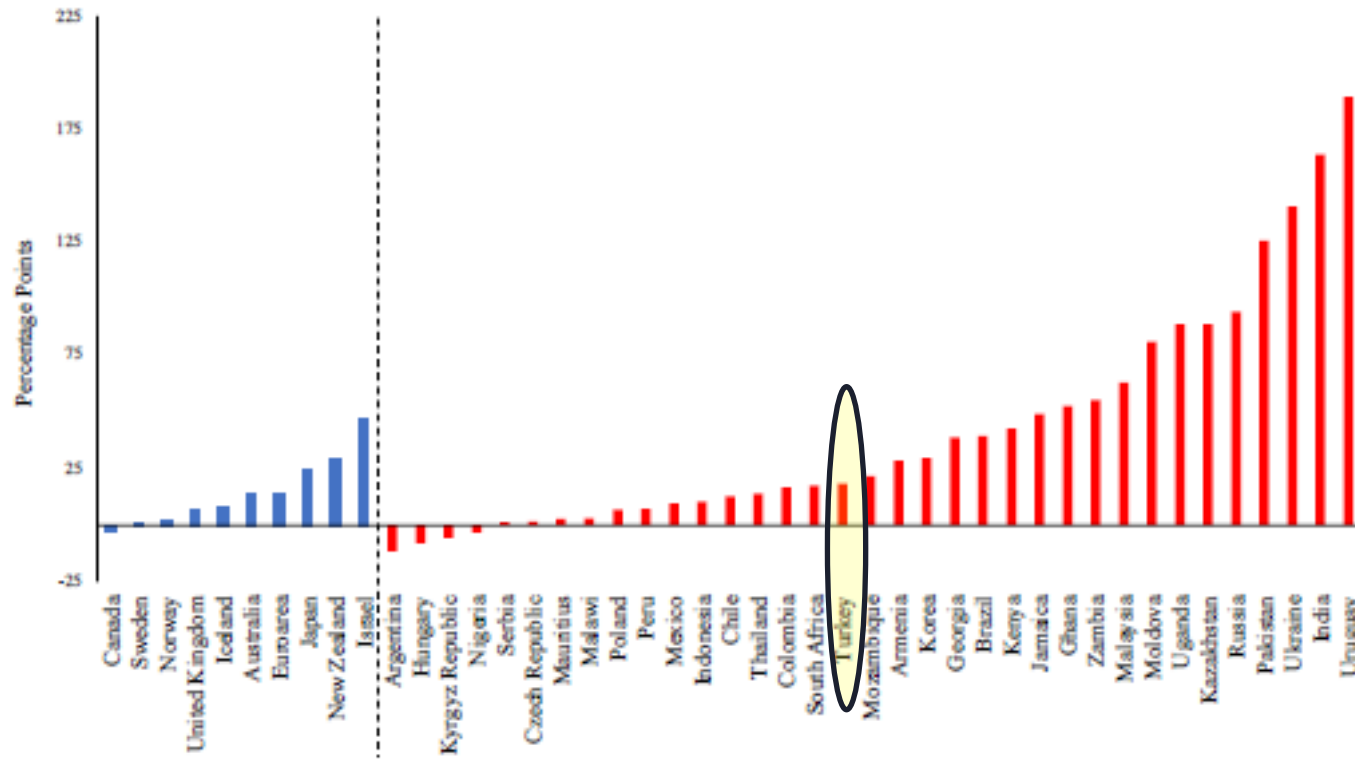


Concerns:

Data Limitations & Approach

Monetary Policy Credibility

Figure 6: Change in Monetary Policy Credibility, 2007-2021



Source: Kalemli-Ozcan and Unsal (2023)

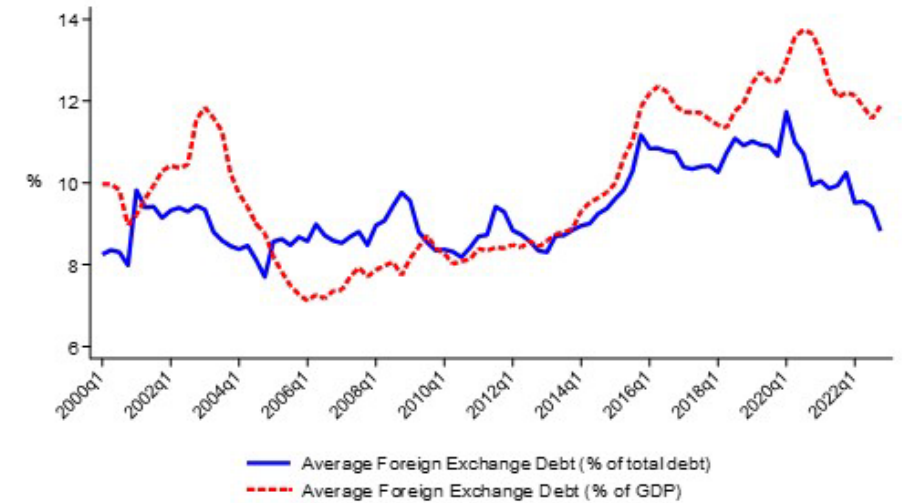
Notes: Percentage change in monetary policy credibility (IAPOC index) of AEs and EMDEs in 2007 (or the earliest starting year) and 2021.



FX Exposure Data

- **Key measure:** US\$ debt / total debt in non-financial private

Figure 2: Corporate Foreign Exchange Debt in Emerging Markets



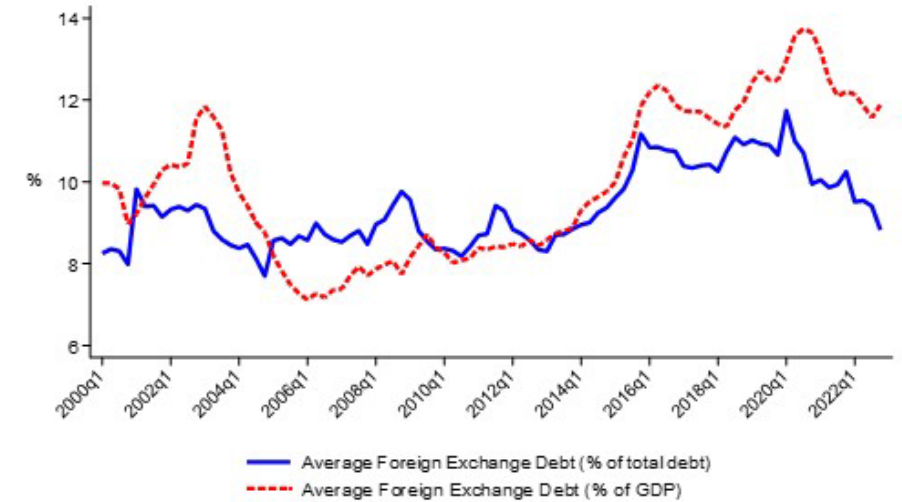
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- **Key measure:** US\$ debt / total debt in non-financial private
- **Missing: Exposure of non-bank financial sector**
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 - Overall exposure to FX—not just as a % of debt?

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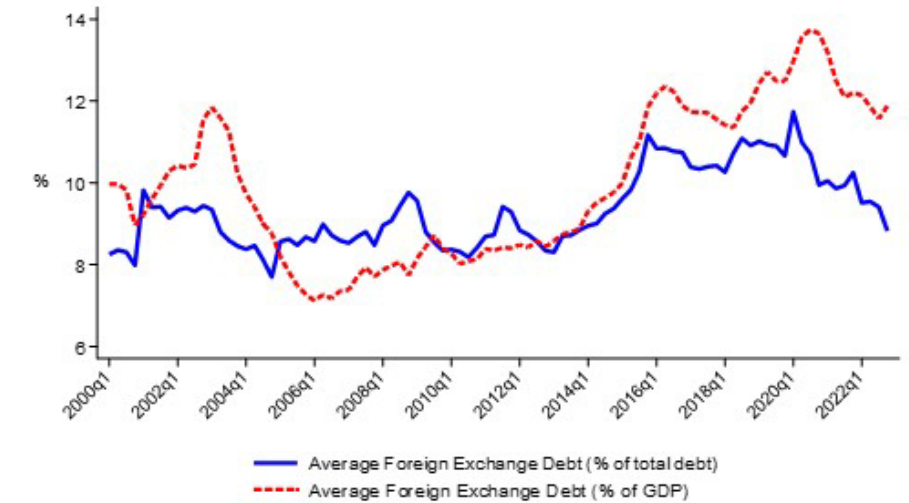
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- **Bigger concern: limited country coverage**
 - Only 13/14 EMs with coverage on FX exposure and credibility?
 - EMs with FX data appear to be different than other EMs
 - And then divide the 13/14 into subgroups for comparisons....

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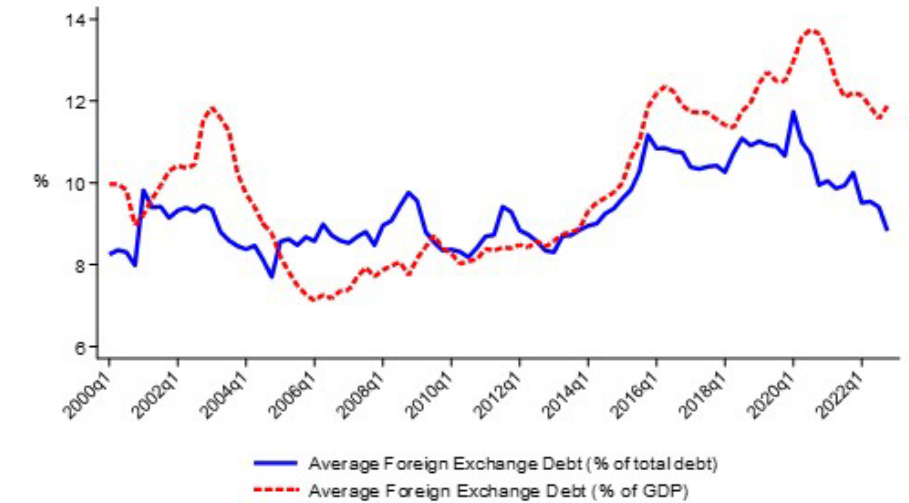
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- **Aggravated by limited time-series for recent US hiking cycle**
 - 1st Fed hike: March 16, 2022, series ends in 2022q4
 - Papers' quick fix? Start hiking window in 2021q1,
 - But too early...US expected "liftoff" of May 2024 & terminal rate= 0.85

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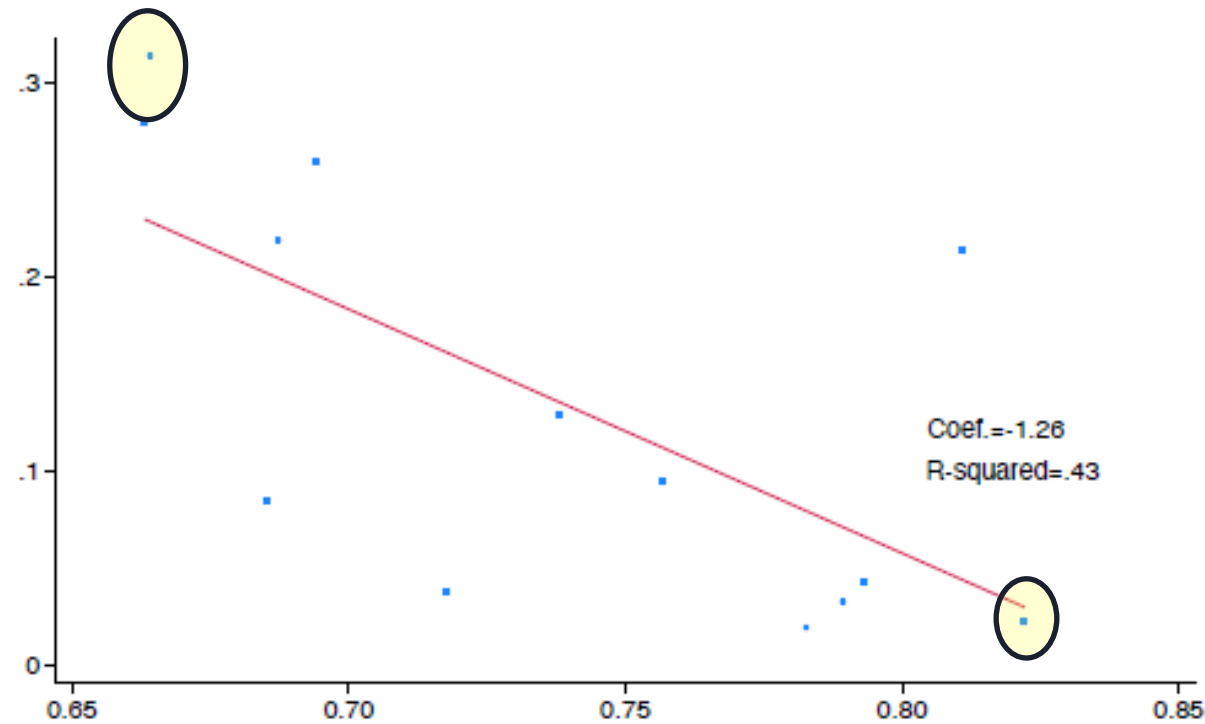


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Omitted Variables

Figure 13: FX debt and Policy Credibility



Source: Kalemli-Ozcan and Unsal (2023)

Notes: This figure shows the correlation between the policy credibility index (x-axis) and the FX debt (y-axis). Coefficient β , significant at 5%, and R^2 from OLS estimates $FXdebt_e = \alpha + \beta * IAPOC_e + \epsilon_e$ are reported.



Final Thoughts

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Warning?



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