

# THE DOMINANT CURRENCY FINANCING CHANNEL OF EXTERNAL ADJUSTMENT

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# SUMMARY OF PAPER

Big picture: How do exchange rate shocks affect output?

- ▶ Literature proposes different mechanisms: (i) expenditure switching, (ii) real income, and (iii) balance sheet channel.
- ▶ Most papers are theoretical. Empirical identification is tricky!

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Big picture: How do exchange rate shocks affect **trade through firms**?

- ▶ Literature proposes different mechanisms: (i) expenditure switching, (ii) real income, and (iii) balance sheet channel.
- ▶ Most papers are theoretical. Empirical identification is tricky!
- ▶ This paper provides **empirical test of the balance sheet channel**.
- ▶ It proposes the 2014-15 Colombian peso depreciation as a pseudo-natural experiment.
- ▶ Main hypothesis: firms with a larger share of foreign denominated debt experience a larger decline in production.
- ▶ It exploits the maturity structure of foreign debt to overcome endogeneity of currency choice.

# MAIN SPECIFICATION & FINDINGS

$$\ln(1 + Y_{ft}) = \beta \times FCE_f \times Post_t + controls_{ft} + \epsilon_{ft},$$

where  $Post_t = 1$  if  $t > 2014Q3$  and  $FCE_f$  stands for

1.  $FCL_{ft}$ : outstanding amount of debt in foreign currency as a share of assets in 2014 Q1.
  2.  $LS_{ft,t'}$ : change in repayment value of foreign denominated debt that is due before  $t'$  as a share of assets.
  3.  $WS_{ft,t'}$ : change in repayment value of all foreign denominated debt as a share of assets.
- ▶ Main result:  $\beta < 0$  only for imports.
  - ▶ Results driven by non-exporters  $\rightarrow$  exporting as a natural hedge.
  - ▶ Dynamic version of regression: effect accumulates over time.
  - ▶ Rest of paper: robustness and further evidence of financial frictions.

## SOME REMARKS

Great paper: very important question, detailed data & smart identification strategy.

Summary of my comments

1. Unclear what the liquidity shock truly captures.
  - ▶ Timing and role of expectations.
2. This is a paper about foreign currency financing.
  - ▶ The emphasis on dominant currency is unnecessary.
3. Other minor comments.

## COMMENT I: CONSTRUCTING THE LIQUIDITY SHOCK

$$LS_{ft,t'} = \frac{\sum_{i \in \Lambda_{f,t}^F} \mathbf{1}_{T(i) \leq t'} L_i \Delta e_{t,T(i)}}{A_{ft}},$$

where  $t = 2014q1$  and  $t' = 2015q3$ .

- ▶ Shock is interacted with  $Post_t \rightarrow$  change in value only starting in 2014q3.
- ▶ Arbitrary choice of  $t'$ : Colombian peso keeps depreciating until 2016q1.
- ▶ Is perfect foresight a good assumption? What about heterogeneity of expectations?

## COMMENT II: WHY FRAME IT AS A DCP PAPER?

- ▶ This is a paper about **foreign** currency financing.
- ▶ No need for DCP in the model.
  - \* In fact, model does not feature nominal rigidities.
  - \* Real exchange rate shocks also generate the balance sheet effect.
- ▶ In the data, US is by far Colombia largest trading partner.
  - \* In the aggregate, closer to LCP for imports, PCP for exports.
- ▶ DCP weakens exporting as a natural hedge.
  - \* Depreciation leads to a negligible impact on export quantity.

## OTHER MINOR COMMENTS

- ▶ Foreign currency borrowing is overall small in Colombia (Table 2).
  - \* Results driven by few very large firms?
  - \* Positive correlation between LS and firm size (Table 3).
- ▶ What share of total imports do imported intermediate inputs represent?
- ▶ Preferred placebo test: use share of imported intermediate inputs as dependent variable.
- ▶ Is there evidence that firms with higher shares of exports contract less? Potential to exploit the intensive margin too.
- ▶ In Figure 2, 2014q1 is significantly different than zero while 2014q3 and q4 are not.
- ▶ Quantification exercise is purely speculative.