Catalytic IMF? A Gross Flow Approach (by Erce and Riera-Crichton)

Discussion

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Barcelona, 17 June 2015
The Paper: New Approach

- question: does IMF intervention catalyze capital inflows?
- existing answers: maybe ...or maybe not
- Aitor and Daniel: what do you mean by capital inflows?
  - split by country of origin
    \[
    \text{Net Capital Inflows} = (\text{net})CI\ Foreigners - (\text{net})CO\ Domestics
    \]
  - split by country of origin and gross flow
    \[
    \text{Net Capital Inflows} = (CI - CO)Foreigners - (CO - CI)Domestics = (In - Out)Liabilities - (Out - In)Assets
    \]
  - estimate the effects of IMF intervention on each term
The Paper: New Results

\[ \text{Net Capital Inflows} = (\text{net}) CI \ Foreigners - (\text{net}) CO \ Domestics \]
\[ = (\text{In} - \text{Out}) Liabilities - (\text{Out} - \text{In}) Assets \]

- net CIF fall after IMF intervention
  - fall in gross inflows by foreigners (In Liabilities)
  - react on impact
  - net CIF react more when IMF+banking/currency crisis

- net COD fall after IMF intervention
  - rise in gross inflows by domestic (In Assets)
  - react 2 quarters after
  - net COD react more when IMF+sovereign defaults

- most of action through "other investment" flows: a banking story?
Empirical Strategy

- 2-stages IV strategy:

\[
\text{IMF}_P = \alpha_i + \delta_t + \gamma Z_{it-1} + \varphi X_{it-1} + \varepsilon_{it}
\]

\[
Y_{it} = a_i + d_t + ct + \sum_{n=1}^{4} b_n \text{IMF}_P_{it-n} + \sum_{n=1}^{4} f_n X_{it-n} + u_{it}
\]

- \(\text{IMF}_P\) = 1 if country \(i\) had IMF intervention in year-quarter \(t\), 0 otherwise
- \(Z_{it-1}\) \(\in\) political + geo-strategic determinants of IMF intervention
- \(X_{it-1}\) = real GDP growth, interest rates, capital controls, crises

- dynamic cumulative effects as in Jordà et al (2014):
  - estimate with LSDV a dynamic equation for \(\Delta Y\) and plot IRF \(h\) quarters after IMF intervention
  - instrument \(\text{IMF}_P\) as before
IV vs OLS: not just a matter of bias

- OLS estimates = diff-in-diff ($IMF_{-}P_{it} \in \{0.1\}$)
  - identify the effect of IMF intervention off before/after change in $Y$
  - may control for prior trends etc. to clean identification

- IV estimates $\neq$ diff-in-diff ($\overbrace{IMF_{-}P_{it}}^{[0.1]}$)
  - identify the effects of expectations over IMF intervention
  - can’t tell apart anticipation from event effect

IV vs OLS: what to do about it?

- show OLS too, and compare
- show $\overbrace{IMF_{-}P_{it}}$ vs $\overbrace{IMF_{-}P_{it}}$ and each $\hat{b}_n$ (not just $\sum_{n=1}^{4} \hat{b}_n$)
- use $\overbrace{IMF_{-}P} = 1$ for $t$ of intervention, $\overbrace{IMF_{-}P}$ $n$ quarters before
  - tell apart anticipation from event
  - trending vs trend breaking effect of IMF intervention
Empirical Strategy: Comments

- "project" effects backwards?
  - role of expectations

- what’s the role of crises per se?
  - reverse causality?
  - instrumenting the interaction term as well?

- minor points on IV
  - is the instrument valid? tests missing...
  - how do controls in $X$ correlate with $IMF_P$ and $Y$?
  - would this help explain the results/ tell an interesting story?
Comments: Interpreting the Results

- net COD react more when IMF + sovereign defaults:
- corralito, and/or fear thereof?
  - massive outflows before intervention and repatriation/no action after
    - what drives the adjustment: domestic outflows (maybe inflows)
- repatriation of domestic sovereign debt?
  - banks sell foreign and buy domestic sovereign debt during crisis
    - what drives the adjustment: domestic inflows (+ foreign outflows)
- to tell the stories apart:
  - IRFs for all 4 gross flows
  - distinguish $IMF_P$ expectations vs $IMF_P$ event
  - look at flows for different instruments
Comments: Interpreting the Results

- net CIF react more when IMF+banking/currency crisis
  - still, mainly through banks?
  - freezed interbank lending?
  - a role for trade credit?
  - some action through portfolio investment?
  - a role for the exchange rate?

- banking story: "normal" times vs crises

- what about the intensive margin?
  - size of IMF intervention and gross capital flows adjustment
Conclusions

- new and sensible approach
- interesting results!
- lots of new insights
- leaves me eager to learn more about the banking story