Discussion of U.S. Shocks and global exchange rate configurations

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http://e105.org/e607

JHU & NBER
This paper

- General family: response of asset prices to U.S. macro news
- General perspective: constructive expansion in documented results. That’s a good thing.
- IFM perspective: use broad set of exchange rates
  - Might shed light on exchange rate regimes
  - Show evidence of globalization
  - Say something about imbalances
    Very nice idea
Some useful results

- U.S. macro news matters
  Always a bit puzzling how much, esp. in light of evidence news from other economies doesn’t

- Effects are heterogeneous

- The heterogeneity is associated with some financial variables & bus. cyc. synch. but not trade directly.

- Heterogeneity has fallen over time
Overall

- A good idea nicely executed.
- Comments
  - Random comments on economics
  - Suggestions for nicer econometrics
First sent. conclusion:
Much progress has been made in recent years in establishing the role of macroeconomic fundamentals for the determination of exchange rates.

Important to note limitations on this progress
<table>
<thead>
<tr>
<th>Release</th>
<th>$R^2$</th>
<th>CPI</th>
<th>0.00</th>
<th>FFRate</th>
<th>0.20</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP</td>
<td></td>
<td></td>
<td>0.18</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nonfarm Payrolls</td>
<td></td>
<td></td>
<td>0.21</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Faust, Rogers, Wright, Wang, JME
Economics

- Shocking how little explained
- Could the measured response just be garbage?
- From the response of one market: impossible to tell.
  Can check mutual consistency across many markets
- FRWW, ABDV: check across several kinds of assets
  Anderson, Bollerslev, Diebold, and Vega
- This paper: check across many exchange rates
Implication for this paper

- This paper uses daily data
  large window, lots going on
- I’d like to see $R^2$
- Concerned just measuring, e.g.,
  ◇ Average thing that happened on nonfarm payroll days
    First Friday of month
  ◇ May be lots of correlated first-friday events
A suggestion

- Where appropriate, I’d like to see comparison to estimates on tighter windows
Random comment 2: What should we expect?

- Several places paper says the responses are “remarkably heterogeneous”
- Thought experiment: suppose the paper had said “remarkably similar” instead?
- I can’t even name 64 countries, let alone have an intuition for “remarkably heterog./similar”
What should we expect?

- Simple theory: “jump” in response to news determined by,
  - Short-run fundamentals (trade and financial)
  - Long-run expected response of monetary policy in both countries
- I’d be shocked if not heterogeneous
Suggestion

- Like to see a brief section summarizing both sign and magnitude of what we might expect from conventional model.
Random economics 3: Globalization

- Popular topic
- Much discussion of growing trade and financial links
- Hard to find macro evidence of implications e.g., Faust-Doyle; Stock-Watson; …
- News responses are an interesting place to look
Case of Canada

- Trade share with G-7 tripled b/t 1960-2002 (20 vs. 60 percent)
- Mostly with U.S. after auto agreement and CAFTA
- Bus. cycle correlation with U.S.: no detectable change (Doyle-Faust, REStat.)
5. Correlation of quarterly real GDP growth rates, selected country pairs, rolling five-year periods, 1965–2002

A: ‘English-speaking’ nations

- United States & United Kingdom

- United States & Canada

- Canada & United Kingdom

B: Continental European nations

- Germany & France

- Germany & Italy

- France & Italy

C: ‘English-speaking’ nations & Continental Europe

D: United States & Japan

Note. See note to figure 4.
Suggestion for paper

- General: Look at some specific examples
- Canada is one natural focus
- I suspect smushing together 64 countries is hiding some gems.
Global imbalances may be a big deal

Or to quote Roubini: The sky is falling
That may actually be a paraphrase

Special interest in looking at trade balance announcements
Rolling 4-year Estimates of Response to Surprise Increases in Trade Deficit

Change in euro/$*
Percent

Estimated Effect

U.S. Current Account/GDP**


-0.4 -0.3 -0.2 -0.1 -0.0 0

Change in yen/$*
Percent

Estimated Effect

U.S. Current Account/GDP**


-0.4 -0.3 -0.2 -0.1 -0.0 0

* Change from 15 minutes before to 15 minutes after data release, 1987-2002; one day change, 1980-1986. For 1980-1996, data are for German mark.

** Current account as share of GDP is averaged over 4-year rolling periods.
Econometrics

- I have some critical comments
- Severely limit the usefulness of the existing results in my view
- Easily fixed
Is there heterogeneity?

- The point estimates vary widely
- Even with over 5000 observations, estimates quite imprecise
  often not stat. sig. diff. from zero
- No test is provided on whether they are different from each other
Suggestion

- General: Don’t discuss differences in point estimates without some assessment of sampling fluctuation.
- Specific: The panel approach used later in paper is right one for testing differences.
- From tables 7 & 8 we know at least some differences are stat. sig. almost certainly, the vast majority are not.
Time-variation

- Time-variation is measured using recursive (expanding sample) estimates
- We know the estimates are imprecise
- No evidence of statistically significant variation is provided
  The graphs don’t look much different from what one might see under no underlying change
- In tight windows, FRWW found little stat. sig. variation.
- Need some formal assessment of time variation
The expanding sample approach is a bit odd.
Rolling might be better.
TVP might be better still.
FRWW shows one way to do this.
Final step (Tables 7 & 8) checks if the heterogeneity is systematic
We pool the data and split the countries into 2 groups in various ways
Ask if the pooled coefs. are different for the two groups
For many types of splits, the answer is no.
For hi/lo bus. cyc. variation and hi/lo cross-border financial holdings, we get sig. diff.
Favorite part

- This stuff is great
Pooling seems a bit odd

Paper’s point is “remarkable heterogeneity” not “two types” of responses
Suggestion

- Exploratory: scatter the measured country responses against various variables.
- Exploratory: regress the measured country responses on a bunch of variables.
Less structured suggestion

- Make a matrix of estimated effects
  - Each column is a country
  - Each row is an announcement
- Examine the factor structure of this matrix
None of these suggestions leads to obviously reliably inferences... but they may reveal some structure and suggest a more systematic way to proceed.
General point

- Paper will have most value added if it documents
  - Statistically significant differences
  - That have some (potentially) interpretable structure
- Have an excellent start, but can easily go much further.
Thus,

- I eagerly anticipate an even more interesting paper