Discussion of "Contagion, Interdependence and Global Crises: Evidence from Equity Markets" by Ilyes Abid, Khaled Guesmi, Samir Saadi, Christian Urom

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French Finance Association, 37th International Conference

May 2021

Summary (1)

- Transmission of shocks across 55 equity markets
- Identification: To distinguish Contagion from the U.S. three factors are used:
    - U.S. market factor;
    - Global financial market factor;
    - Domestic market factor;
- Suggests an explanation for the co-movement based on these three factors.

Summary (2)

- Six crisis transmission channels:
  - Country-level banking sector exposure to both the U.S. and the rest of the World;
  - Credit growth;
  - Bank size;
  - Financial stability;
  - Macroeconomic fundamentals;
  - Degree of integration;

- The study uses equity indices from: North America (6), Europe (32), Asia (12), Middle East and North Africa (5) from 1999 – 2018.

Findings

- Increased level of co-movement through exposure to the three factors
- Domestic factor is dominant except in the case of Canada
- Non-fundamental contagion mainly in the U.K.
- Macroeconomic fundamentals work as channels of shock transmission giving rise to “wake-up call” hypothesis.

Key result: Contagion is more severe depending on the quality of domestic economic fundamentals.

- Empirically the paper is doing a good and comprehensive work.

Improvements in the explanation & the identification (1)

- The international literature that studies contagion is vast.

- The introduction contains too much analysis of the literature – it resembles to a literature review. Start with a clear research question in the first paragraph, and then provide the most relevant papers that have studied something similar. Outline your findings and show how do you contribute in the most relevant literature. For example, para. 9 should be para. 1 or 2.

- The empirical results basically find a strong and positive correlation between the variables that measure contagion at most levels of aggregation.

Improvements in the explanation & the identification (2)

- The distinction between interconnectedness and contagion measure seems to be built in mechanically by the definition of measures.

- Is there a conflict between the "wake-up call" hypothesis and interconnectedness? Both are built on the hypothesis that macroeconomic fundamentals are key to cross-country developments / shocks.

Are the factors plausible?

- For the U.S. factor: Include 1-Year and 10-Year Treasury Bonds either as an out-of-sample robustness test or as additional explanatory variables; why MSCI and not S&P 500? Why not U.S. VIX, given that you are using world VIX?

- For the Domestic financial factor: Why do you use the 3-month rate instead of the 1-Year and 10-Year domestic Treasury Bonds?

- Indexes that capture domestic sentiment (e.g., investor or consumer sentiment) can add value to your analysis.

Are the factors plausible?

- The fluctuations in financial and economic activity explained by the three factors are characterized by co-movements of asset prices and economic fundamentals, financial instability or excess leverage of banks with exposures in the U.S. market.

An alternative test: Three factors vs U.S. Monetary Policy factor

- The factors contradict the Global Financial Cycle theory (see Rey, 2013; Miranda-Agrippino and Rey, 2015): US monetary policy is a driver of the Global Financial Cycle.

- How do you contribute on the Global Financial Cycle hypothesis?

- Explicitly compare the coefficient of your variables vis-à-vis the coefficient a U.S. monetary policy variable.

Other Comments

- The role of cross-country bank exposure is unclear, further explanation is needed
- References should be listed by alphabetical order.

Conclusion

- The issue discussed in the paper is interesting and important

- There is a literature that has analyzed contagion and interdependence, however new factors are discussed in this paper.

- Overall, it is a good and insightful work.

- In the current form it needs a few minor improvements.