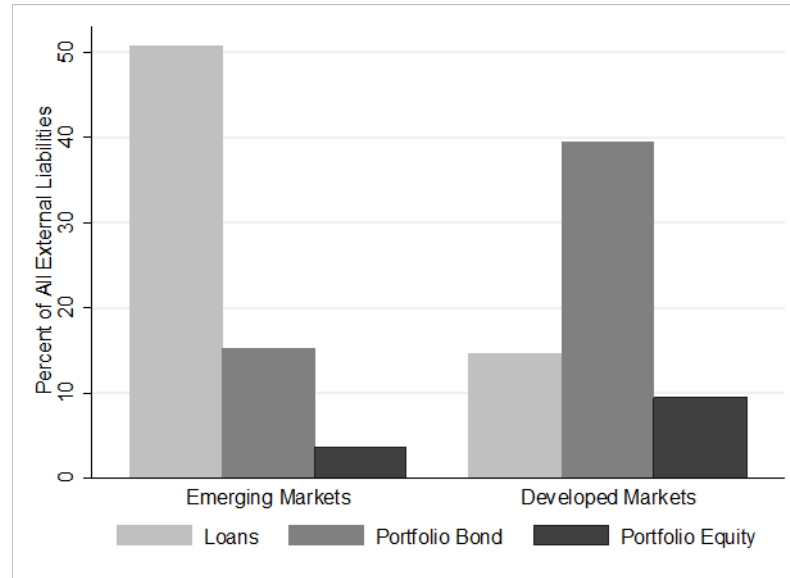


U.S. Monetary Policy and Emerging Markets Credit Cycles

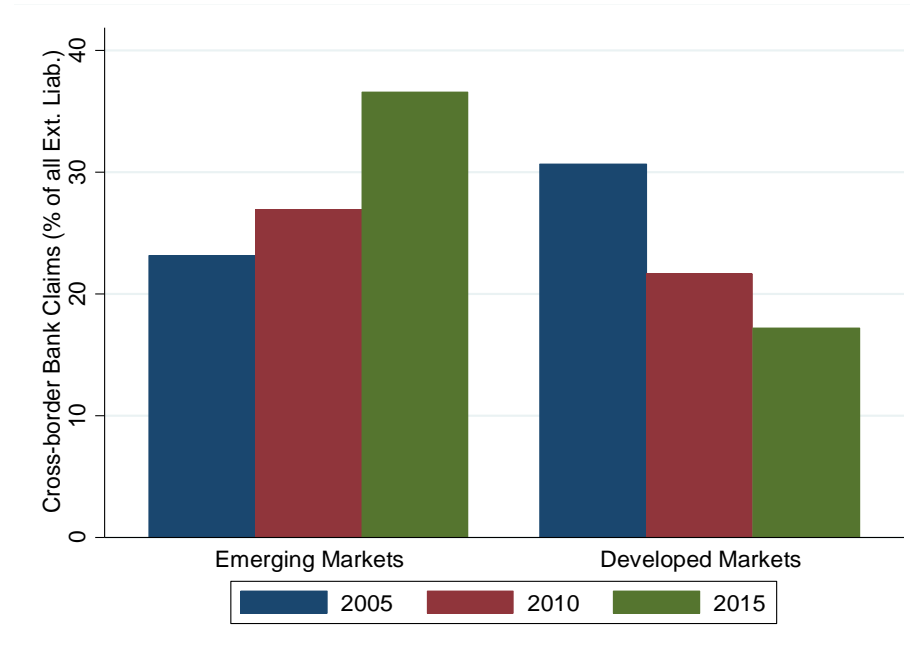
Falk Bräuning (Boston Fed) and Victoria Ivashina (Harvard University)

The views expressed in this paper are those of the authors and do not necessarily represent the views of the Federal Reserve Bank of Boston or the Federal Reserve System.

- Fact #1: For EMEs, foreign bank lending is the key component of cross-border capital flows



- Fact #1: For EMEs, foreign bank lending is the key component of cross-border capital flows



Syndicated credit: over 80% of loans are provided by foreign banks in EMEs vs. less than 50% for DMEs (see paper, Figure III)

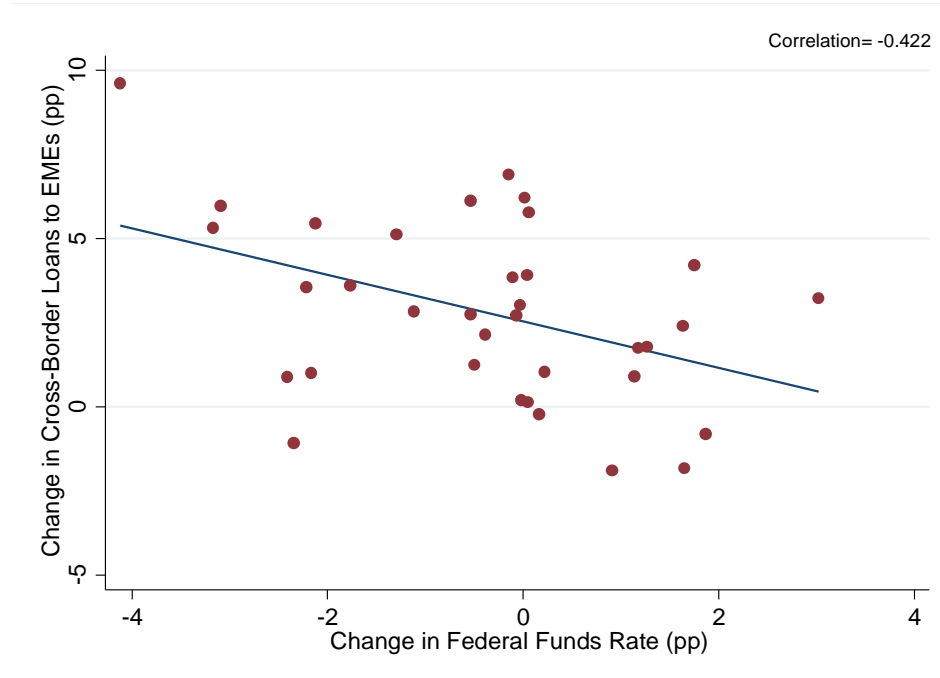
- Fact #2: Much of the foreign banks' lending is in USD

| | Cross-Border Loans (Source: DealScan) | | | | | | Cross-Border "Bank Claims" (Source: BIS) | | | | |
|----------------------|--|-------|------|------|-------|--|---|-------|------|------|-------|
| Currency: | USD | EUR | GBP | JPY | Other | | USD | EUR | GBP | JPY | Other |
| Region: | | | | | | | | | | | |
| EME: Africa | 88.8% | 5.3% | 0.1% | 0.8% | 4.9% | | 65.5% | 12.7% | 3.9% | 1.0% | 16.9% |
| EME: Americas | 91.3% | 1.1% | 0.0% | 0.7% | 6.9% | | 75.6% | 4.4% | 0.2% | 1.7% | 18.2% |
| EME: Asia | 69.7% | 1.3% | 0.7% | 4.2% | 24.0% | | 51.9% | 5.0% | 0.3% | 1.3% | 41.5% |
| EME: Europe | 56.0% | 30.9% | 0.0% | 0.6% | 12.5% | | 31.9% | 38.8% | 0.5% | 1.1% | 27.7% |
| DME | 69.8% | 19.7% | 5.0% | 0.7% | 4.8% | | 43.3% | 36.9% | 4.9% | 4.9% | 10.1% |

- Currency breakdown of syndicated cross-border loans to EME borrowers based on outstanding claims. All claims include also bond and equity holdings. Claims at 2016:Q3. Source: DealScan, BIS, Authors' calculations.

Stable over time: see paper Figure IV

Focus: Cross-border Loans to EMEs and U.S. Monetary Policy



- Figure shows relationship between cross-border loans to emerging market economies (EMEs) and U.S. monetary policy. Annual data from 1980 through 2015. Source: IMF, Authors' calculations.

Identification of Channel with Loan-Level Data

Syndicated loan data: global issuance, 1990-2016 (119 EMEs)

With loan-level data (as opposed to aggregate macro data) we know:

- the identity of the bank (lender) and firm (borrower)
- the loan conditions (volume, maturity, etc.)
- the currency of the loan

Allows us to better identify the effect of U.S. monetary policy on dollar loan supply by global banks to EME borrowers

Related Literature

- Rey (2013)
- Miranda-Agrippino and Rey (2015)
- McCaulay, McGuire and Sushko (2015)
- Takas and Temesvary (2016)

-
- Forbes and Warnock (2012)
 - Fratzscher (2012)
 - Ahmed and Zlate (2013)

- Baskaya et al. (2017) – Turkey
- Altunok et al. (2017) – Turkey
- Peydro and Ruiz (2015) – Mexico
- Demirguc-Kunt, Horvath and Huinga (2017) – Syndicated data

Cross-border Lending at Bank-Firm Level

Table II: Baseline results (unit of observation: Loan x Lender)

| | (1) | (2) | (4) |
|--|-----------------------|----------------------|----------------------|
| U.S. Interest Rate | -0.144*** (-11.49) | -- | -- |
| U.S. Interest Rate * DME | -- | -0.090*** (-9.98) | -- |
| U.S. Interest Rate * EME | -- | -0.194*** (-9.66) | -0.081*** (-7.69) |
| U.S. Term Spread * EME | -- | -- | -- |
| U.S. Shadow Rate * EME | -- | -- | -- |
| EME | -- | -0.951*** (13.43) | -- |
| Fixed Effects | -- | -- | |
| Borrower (D_i) | -- | -- | Yes |
| Bank * Quarter (D_{jt}) | -- | -- | Yes |

From (4), U.S. rate increases by 1 pp →
additional decrease in EME lending by 8 percent

Cross-border Lending at Bank-Firm Level

Table II: Baseline results (unit of observation: Loan x Lender)

| | | | | | Pre-ZLB Period | ZLB Period |
|--|-----------------------|----------------------|----------------------|-----------------------|---------------------|---------------------|
| | (1) | (2) | (4) | (5) | (6) | (7) |
| U.S. Interest Rate | -0.144*** (-11.49) | -- | -- | -- | -- | -- |
| U.S. Interest Rate * DME | -- | -0.090*** (-9.98) | -- | -- | -- | -- |
| U.S. Interest Rate * EME | -- | -0.194*** (-9.66) | -0.081*** (-7.69) | -0.164*** (-12.71) | -0.074** (-3.41) | -- |
| U.S. Term Spread * EME | -- | -- | -- | -0.158*** (-6.80) | -0.092** (-3.08) | -- |
| U.S. Shadow Rate * EME | -- | -- | -- | -- | -- | -0.068** (-2.75) |
| EME | -- | -0.951*** (13.43) | -- | -- | -- | -- |
| Fixed Effects | -- | -- | | | | |
| Borrower (D_i) | -- | -- | Yes | Yes | Yes | Yes |
| Bank * Quarter (D_{jt}) | -- | -- | Yes | Yes | Yes | Yes |

Holds across all geographical regions
 Similar result if using aggregate BIS data

Cross-border Lending at Bank-Firm Level

Table II: Baseline results (unit of observation: Loan x Lender)

| Banks' Loan Exposure to U.S.: | < 10% | < 5% | < 5% | < 5% | < 5% | < 5% |
|--|----------------------|--------------------|-----------------------|-------------------------------|--------------------------------|----------------------------------|
| Borrowers: | | | Non-Tradable Industry | Sectors with Low Export Share | Country with Low Trade Overall | Country with Low Trade with U.S. |
| | (1) | (2) | (3) | (4) | (5) | (6) |
| U.S. Interest Rate * EME | -0.159*** (-5.58) | -0.078* (-1.79) | -0.091** (-1.99) | -0.181*** (-2.69) | -0.092** (-2.09) | -0.348*** (-5.71) |
| U.S. Term Spread * EME | -0.186*** (-4.29) | -0.112* (-1.76) | -0.135** (-2.02) | -0.073 (-0.26) | -0.092 (-1.51) | -0.517*** (-5.97) |
| Fixed Effects: | | | | | | |
| Borrower (D_i) | Yes | Yes | Yes | Yes | Yes | Yes |
| Bank * Quarter (D_{jt}) | Yes | Yes | Yes | Yes | Yes | Yes |

Cross-border Lending at Bank-Firm Level

Table II: Baseline results

| | "High-Yield Market" Defined Using: | | | | | | | |
|---|------------------------------------|------------|----------------------|----------------------|----------------|----------------|----------------|----------------|
| | GDP Growth | GDP Growth | Interest Rate Spread | Interest Rate Spread | Equity Returns | Equity Returns | Country Rating | Country Rating |
| | (1) | (2) | (3) | (4) | (5) | (6) | (7) | (8) |
| U.S. Interest Rate * High-Yield Market | -0.002** | -0.006*** | -0.003*** | -0.004*** | -0.024* | -0.031 | -0.007*** | -0.014*** |
| | (-2.05) | (-3.00) | (-5.65) | (-3.65) | (-1.68) | (-0.80) | (-6.45) | (-7.92) |
| U.S. Term Spread * High-Yield Market | -- | -0.007* | -- | -0.001 | -- | -0.013 | -- | -0.012*** |
| | | (-1.97) | | (-0.92) | | (-0.20) | | (-4.49) |
| High-Yield Market | 0.014*** | 0.036*** | 0.014*** | 0.019*** | 0.025 | 0.065 | -0.063*** | -0.010 |
| | (2.71) | (3.08) | (5.36) | (2.91) | (0.35) | (0.31) | (-5.23) | (-0.69) |
| Fixed Effects: | | | | | | | | |
| Borrower (D_i) | Yes | Yes | Yes | Yes | Yes | Yes | Yes | Yes |
| Bank * Quarter (D_{jt}) | Yes | Yes | Yes | Yes | Yes | Yes | Yes | Yes |

Financial openness (conditional on country rating) magnifies the impact (Table VII)

Cross-border Lending at Bank-Firm Level

Table V: Specialness of U.S. monetary policy

| Loan Currency: | USD | USD | USD | USD | EUR |
|--|-----------|-----------|---------------------------------------|-----------|---------------------------------|
| | | | Non-U.S. Banks, Non-U.S. Borrowers | | U.S. Banks, Non-EU Borrowers |
| | (1) | (2) | (3) | (4) | (5) |
| Euro Interest Rate * EME | -0.147*** | -0.018 | -0.034 | -- | -0.228** |
| | (-7.82) | (-0.57) | (-0.86) | | (-2.37) |
| Euro Term Spread * EME | -0.036 | 0.030 | 0.046 | -- | -0.136 |
| | (-1.25) | (1.10) | (1.17) | | (-0.71) |
| U.S. Interest Rate * EME | -- | -0.191*** | -0.187*** | -0.196*** | -0.029 |
| | | (-5.64) | (-4.00) | (-4.05) | (-0.21) |
| U.S. Term Spread * EME | -- | -0.223*** | -0.263*** | -0.343*** | -0.136 |
| | | (-5.34) | (-4.42) | (-4.21) | (-0.71) |
| Fixed Effects: | | | | | |
| Borrower (D_i) | Yes | Yes | Yes | Yes | Yes |
| Bank * Quarter (D_{jt}) | Yes | Yes | Yes | Yes | Yes |
| Observations | 113,277 | 113,277 | 51,091 | 16,809 | 210 |
| R-squared | 0.825 | 0.826 | 0.843 | 0.887 | 0.940 |

Borrower-Level Impact

Table VIII: Substitution between local and foreign lenders at firm level

| Dependent Variable: | (Log) Borrowing Amount (USD) | | | | | Interest Rate Spread (bps) | | |
|---------------------------------|---|-------------|-----------|-----------|-----------|----------------------------|-----------|--|
| | Firm-Quarters with Foreign and Domestic Lenders | | | | | | | |
| | Foreign Banks | Local Banks | All Banks | All Banks | All Banks | All Banks | All Banks | |
| | (2) | (3) | (4) | (5) | (6) | (7) | (8) | |
| U.S. Interest Rate * EME | -0.075*** | -0.085*** | -0.079*** | -0.024*** | -0.036*** | 3.855*** | 9.402*** | |
| | (-4.51) | (-6.61) | (-5.54) | (-2.65) | (-3.10) | (2.72) | (4.61) | |
| U.S. Term Spread * EME | -- | -- | -- | -- | -0.023 | -- | 10.007*** | |
| | | | | | (-1.20) | | (2.82) | |
| Fixed Effects: | | | | | | | | |
| Borrower (D_i) | Yes | Yes | Yes | Yes | Yes | Yes | Yes | |
| Quarter (D_t) | Yes | Yes | Yes | Yes | Yes | Yes | Yes | |
| Observations | 24,754 | 24,754 | 24,754 | 40,134 | 40,134 | 30,829 | 30,829 | |

Foreign Bank Reliance of EME Firms

Table IX (Sample: EME firms only)

| Dependent Variable: | (Log) Borrowing Amount (USD) | | Interest Rate Spread (bps) | | Probability of Refinancing | |
|--|------------------------------|---------|----------------------------|------------|----------------------------|-----------|
| | (3) | (4) | (5) | (6) | (7) | (8) |
| Past Foreign Bank Reliance | 0.155** | 0.200 | -6.111 | -75.645*** | 0.044 | 0.232*** |
| | (2.10) | (1.11) | (-0.62) | (-3.57) | (1.02) | (2.74) |
| Past Foreign Bank Reliance * U.S. Interest Rate | -0.035* | -0.042 | 2.867 | 14.430*** | -0.023** | -0.057*** |
| | (-1.67) | (-1.19) | (1.18) | (3.78) | (-2.37) | (-3.29) |
| Past Foreign Bank Reliance * U.S. Term Spread | -- | -0.017 | -- | 25.392*** | -- | -0.067** |
| | | (-0.27) | | (3.42) | | (-2.52) |
| Fixed Effects: | | | | | | |
| Borrower (D_i) | Yes | Yes | Yes | Yes | Yes | Yes |
| Quarter (D_t) | Yes | Yes | Yes | Yes | Yes | Yes |

Reliance is fraction of the last loan funded by foreign banks

1 SD (0.32) → \$28 million drop for 25 bps increase in rate

1 SD → 1.2 bps drop for 25 bps increase in rate(vs. 16.3% mean)

1 SD → 0.2 bps drop for 25 bps increase in rate(vs. 16.3% mean)

Conclusions

- We provide new insights into the transmission of U.S. monetary policy to emerging markets credit cycle
 - Channel operates through U.S. dollar lending of global banks
- A typical U.S. monetary easing cycle, EME borrowers experience a 32-percentage-point greater increase in the volume of loans issued by foreign banks than do borrowers from developed markets, with a similarly large effect upon reversal of the U.S. monetary policy stance