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Whither Financial Globalization?

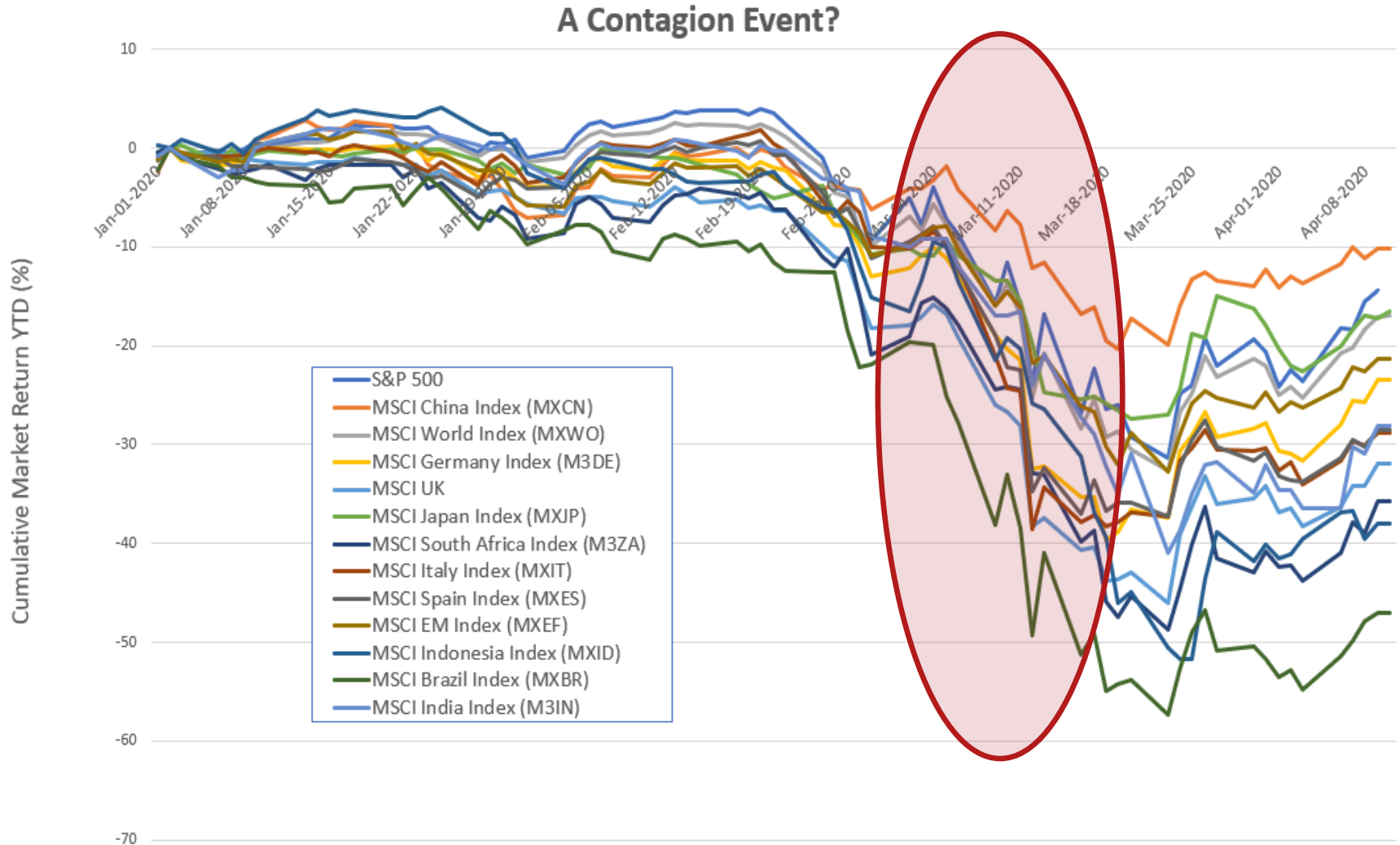
Some Reflections on how COVID-19 Might Shape Global Capital Markets

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*Mayo Center for Asset Management Virtual Seminar Series,
UVA Darden and FMA International, April 17, 2020*



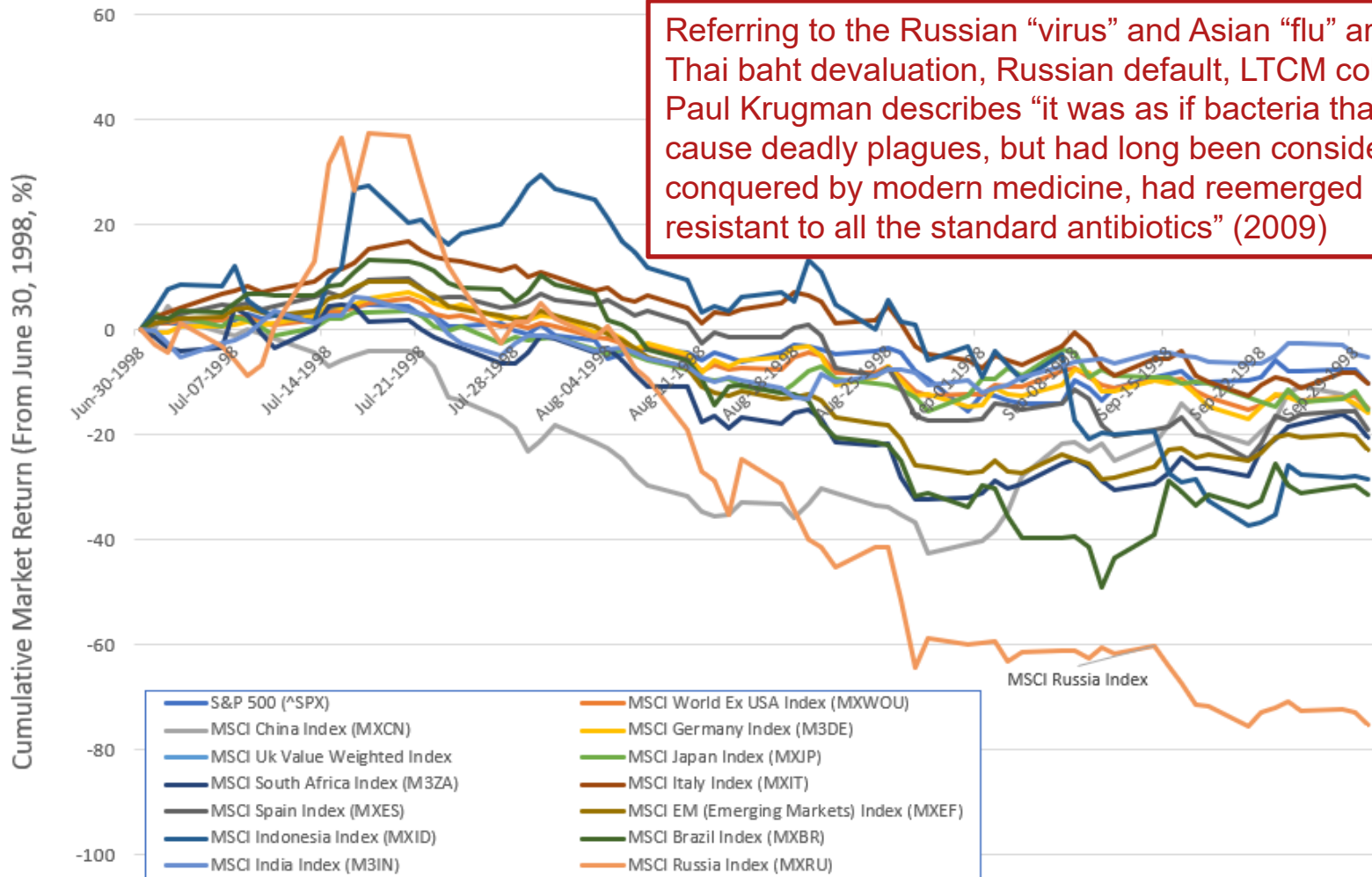
A Time for Reflections on Financial Contagion



A Time for Reflections on Financial Contagion

And Yet Another Contagion Event in 1998!

Referring to the Russian “virus” and Asian “flu” around Thai baht devaluation, Russian default, LTCM collapse, Paul Krugman describes “it was as if bacteria that used to cause deadly plagues, but had long been considered conquered by modern medicine, had reemerged in a form resistant to all the standard antibiotics” (2009)



The Review of Financial Studies

A New Approach to Measuring Financial Contagion

Kee-Hong Bae, G. Andrew Karolyi, René M. Stulz ✉

The Review of Financial Studies, Volume 16, Issue 3, July 2003, Pages 717–763, <https://doi.org/10.1093/rfs/hhg012>

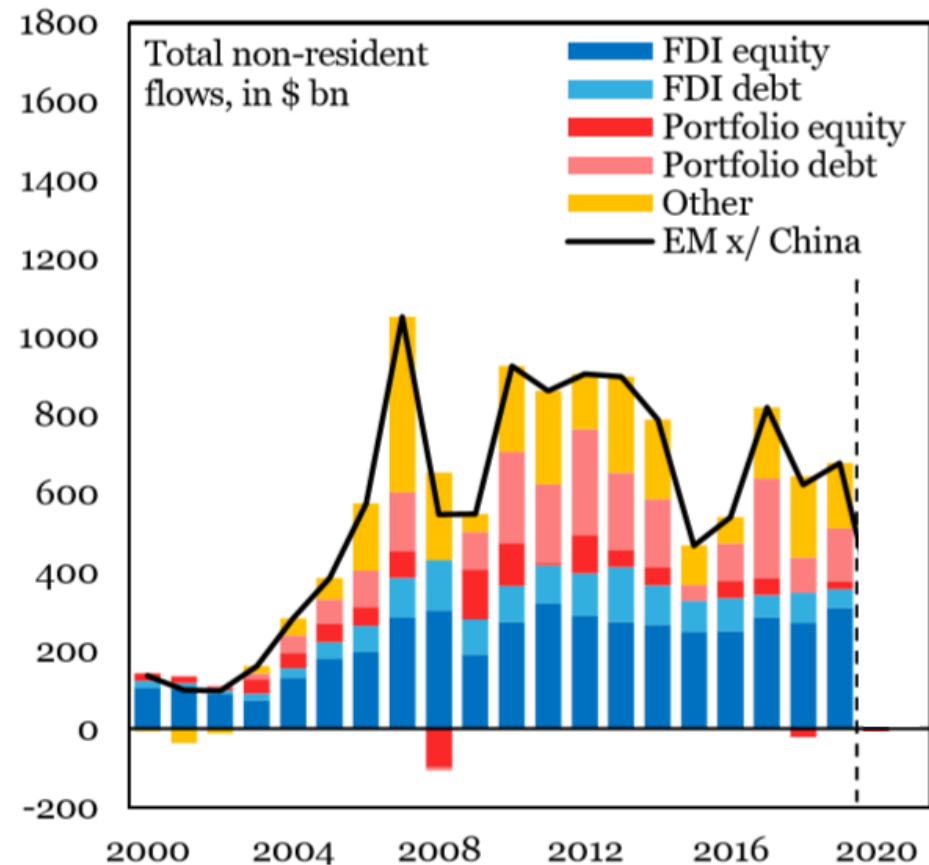
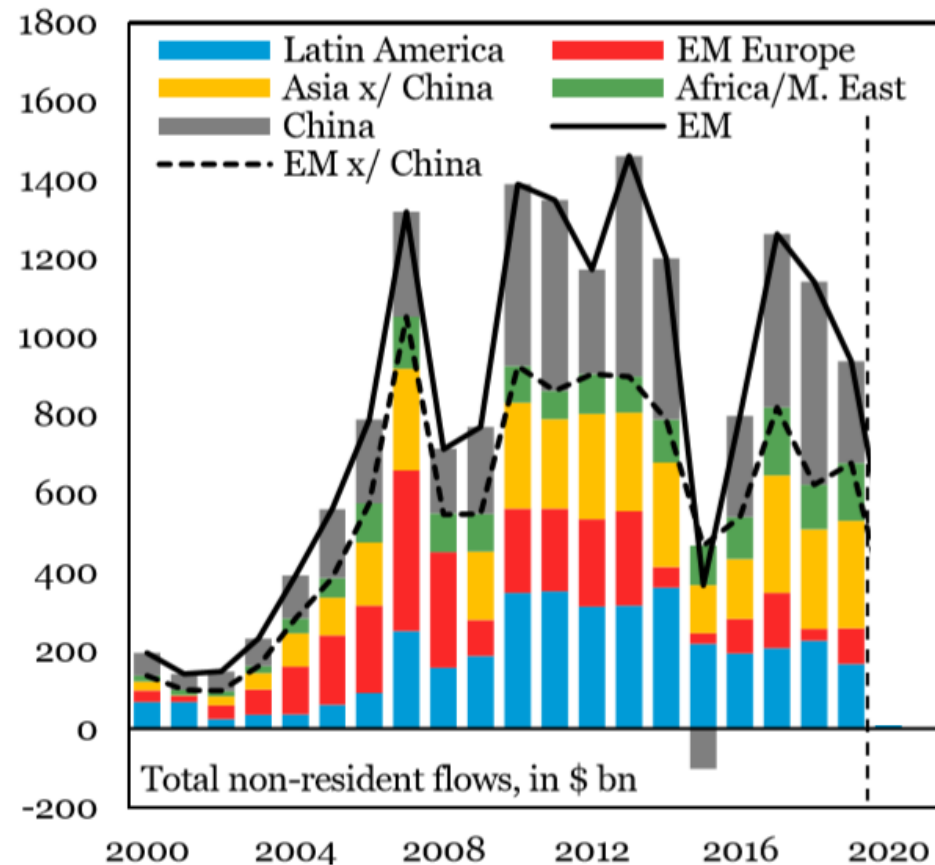
Abstract

This article proposes a new approach to evaluate contagion in financial markets. Our measure of contagion captures the coincidence of extreme return shocks across countries within a region and across regions. We characterize the extent of contagion, its economic significance, and its determinants using a multinomial logistic regression model. Applying our approach to daily returns of emerging markets during the 1990s, we find that contagion is predictable and depends on regional interest rates, exchange rate changes, and conditional stock return volatility. Evidence that contagion is stronger for extreme negative returns than for extreme positive returns is mixed.

Critical Reflections on Bae et al. (2003)

- NOT a model of time-varying correlations in returns
- A multivariate discrete choice model of “infections” of large market returns “exceedances;” “epidemics” *across markets* or “co-exceedances,” and “pandemics” *across regions*
- Daily returns, 17 Asian/LatAm markets, 1992-2000
- Econometrician chooses:
 - Epidemics within regions? Pandemics across regions?
 - Threshold events for an “infection” and “pandemics”
 - Windows of co-exceedances to constitute epidemic
 - Covariates as predeterminants (real & financial)
- Improve on our model for the COVID-19 contagion event?

A Time for Reflections on the Pace of Globalization



While cross-border foreign direct and portfolio flows have receded by 40% since the peak before the Global Financial Crisis **overall**, the pace has continued for EMs, especially FDI.

A New Working Paper



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[René M. Stulz](#)

Ohio State University (OSU) - Department of Finance; National Bureau of Economic Research (NBER); European Corporate Governance Institute (ECGI)

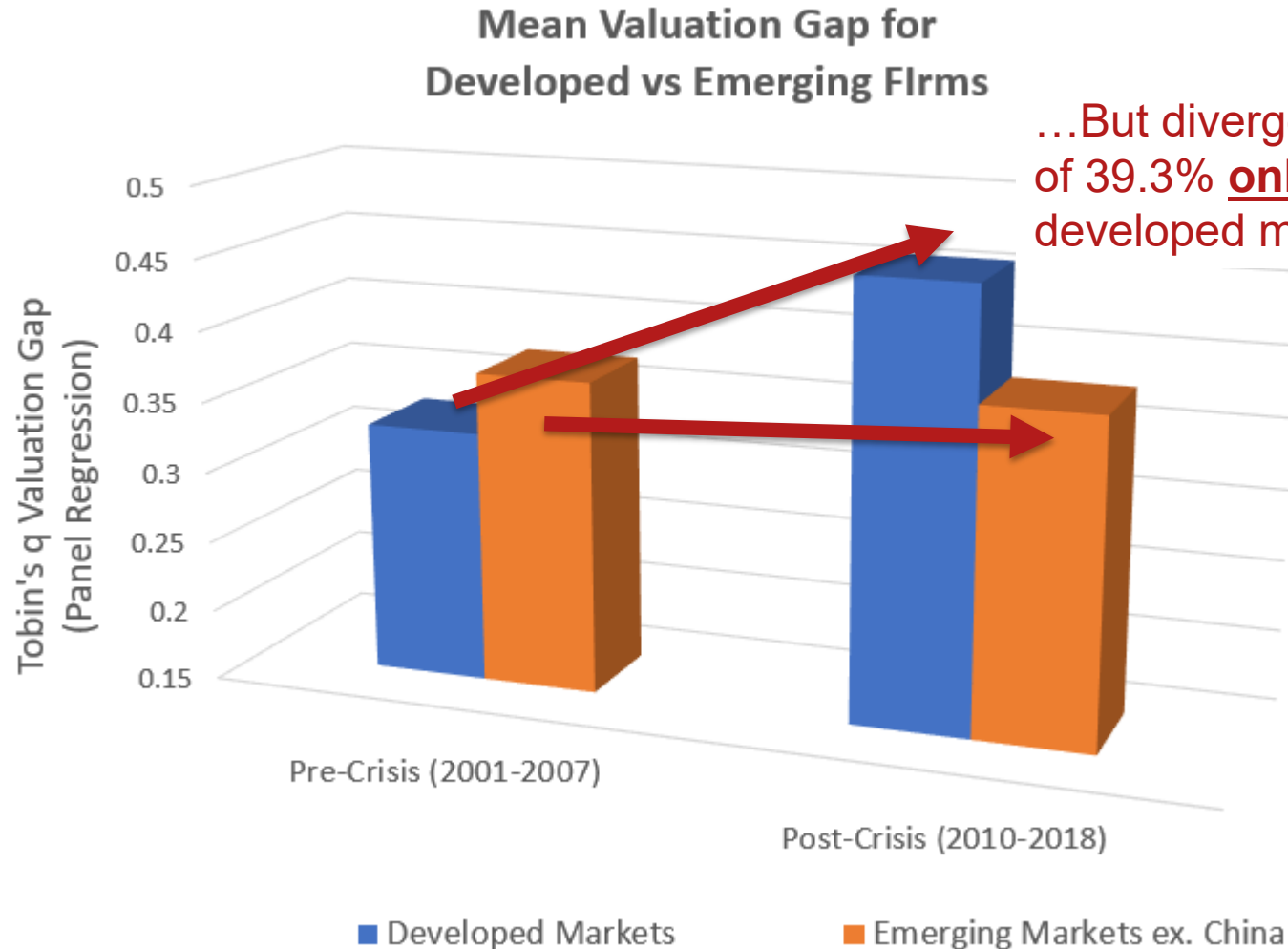
Date Written: April 13, 2020

Abstract

For the last two decades, non-US firms have lower valuations than similar US firms. We study the evolution of this valuation gap to assess whether financial markets are less integrated after the 2008 global financial crisis (GFC). The valuation gap for firms from developed markets increases by 31% after the GFC – a reversal in financial globalization – while the gap for firms from emerging markets (excluding China) stays stable. There is no evidence of greater segmentation for non-US firms cross-listed on major US exchanges and the typical valuation premium of such firms relative to domestic counterparts stays unchanged. However, the number of such firms shrinks sharply, so that the importance of US cross-listings as a mechanism for market integration diminishes.

Keywords: Financial globalization, Tobin's q, corporate valuation, convergence, financial crisis

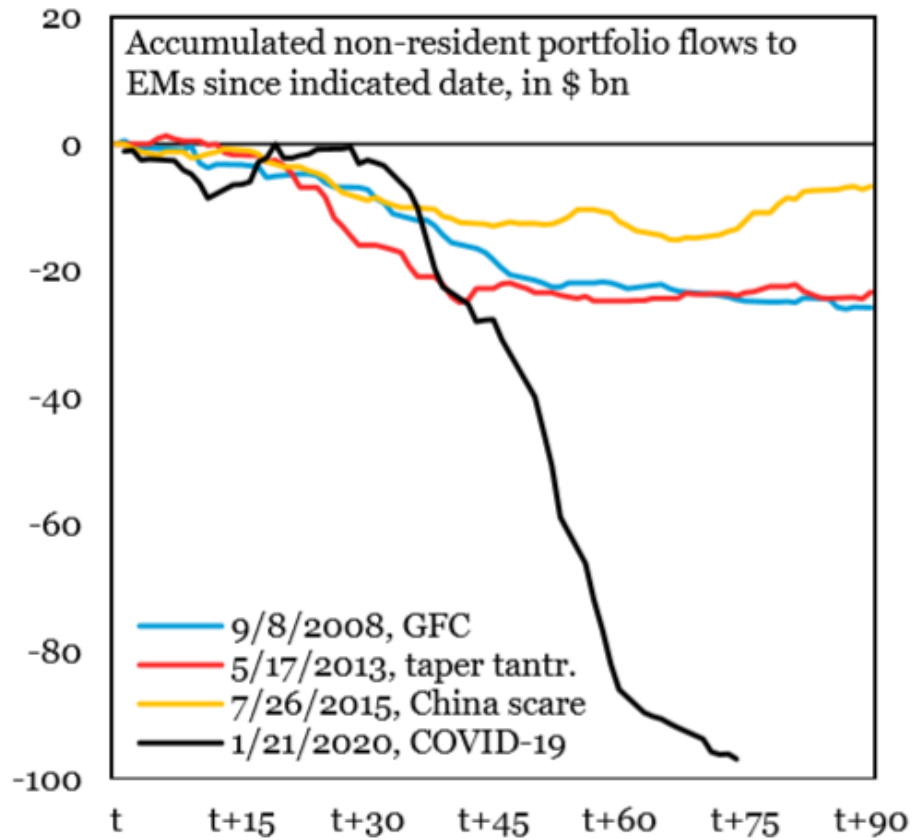
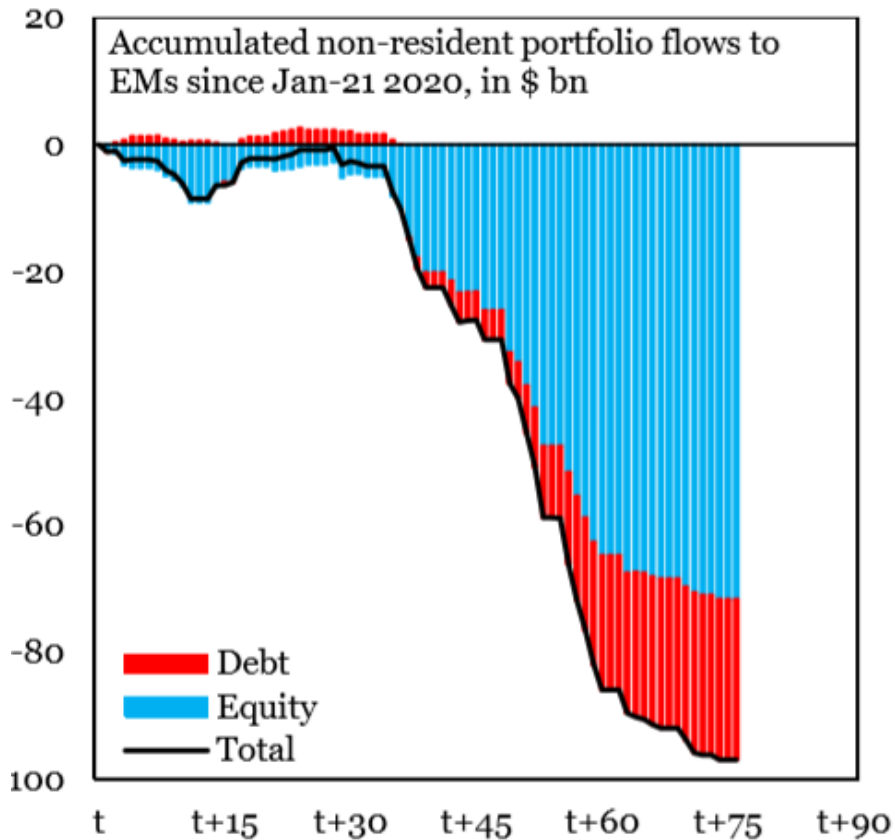
What does the paper find?



What is going on?

- What is **not** associated with EM vs DM gaps...
 - Accounting conventions – capitalizing R&D
 - Shifting industrial composition (tradeable goods, technology, resource sector)
 - Shifting composition by firm attributes (rise of intangible assets, younger vs older firms)
- What **is** associated with EM vs DM gaps...
 - Large decline in propensity of non-US firms to secondarily cross-list on US markets, especially among DMs (402 in 2001 down to 256 in 2018 vs EMs holding steady at 112)
 - Notwithstanding the resilience of “cross-listing premium”
- What might we learn about 2020?

Falling off the COVID-19 Cliff...



Source: Institute for International Finance (J. Fortun and B. Hilgenstock, [IIF Capital Flows Tracker](#) – April 2020, April 1, 2020)

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Thank you!

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[Bae, K.H., G. A. Karolyi, R. M. Stulz, 2003, A new model of international financial contagion, Review of Financial Studies 16 \(3\), 717-763.](#)

[Doidge, C., G. A. Karolyi, R. M. Stulz, 2020, Is financial globalization in reverse after the 2008 global financial crisis? Evidence from corporate valuations, Available at SSRN: <https://ssrn.com/abstract=3574664>.](#)

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