Discussion of
Unbalanced Financial Globalization

By Damien Capelle, Bruno Pellegrino

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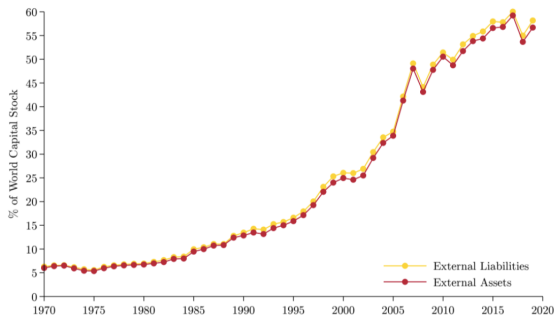May 20th, 2023

Annie Soyean Lee

Johns Hopkins University, SAIS

Motivation

- **Financial globalization** over the last five decades
  - total external A and L ↑ from 5% to 60% of capital stock

Figure 1: External Assets and Liabilities, as % of World Capital Stock

- Little known about its global and long-term effects

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- **Financial globalization** over the last five decades
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  This paper:

- Question: What's the quantitative implications of financial globalization for capital and output allocations across countries?

- Methodology: Wedge accounting, let data speak

A dynamic gravity model of international investment

- **Key assumptions** in the model:
    - Exog. saving rates β_{jt} and labor ℓ_{jt}, natural resources x_{jt}, productivity ω_{it}, production function parameters
    - Bilateral wedges $\tau_{ijt} = \tau_{it,IN} \times \tau_{jt,OUT}$
      $\Rightarrow$ unknown wedges goes down to $2 \times (\#$ of countries$)$

- Wedges, $\tau_{i,IN}$ and $\tau_{i,OUT}$, are calibrated s.t.
  portfolio share of domestic vs. external assets in the data $=$ model

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* **Main quantitative findings**:

  In 2019, compared to the counter-factual economy, we have
    - higher K by 10% for rich and lower K by 20% for poor countries.
    - higher dispersion of output per worker by 8%
    - lower world output by 2%

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- Lack of bilateral portfolio holdings data except recent years

$\Rightarrow$ Impose $\tau_{ij} = \tau_{i,IN} \times \tau_{j,OUT}$ & use external assets and liabilities data

- How much does the assumption matter for the quantitative results?

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  Quick check:

- Bilateral portfolio holdings data are available from early 2000
  (e.g. IMF CPIS available from 2001)

- Still capturing a more rapid increase in external A+L after 2000

- You can do the similar exercises with & without imposing
  $\tau_{ij} = \tau_{i,IN} \times \tau_{j,OUT}$, taking early 2000 as the initial year

- Quantitative results similar with & without the assumption?

Comment # 2 : Logit Asset Demand

$$\pi_{ijt} = \frac{(\tau_{ijt} R_{it})^\epsilon k_{it-1}}{\sum_{\iota}^{I} (\tau_{\iota jt} R_{\iota t})^\epsilon k_{\iota t-1}}$$

- logit asset demand system:
- *effective return $\tau_{ijt} R_{it}$* $\Rightarrow$ portfolio shares π_{ijt}
- no risk? high return + high risk and hence lower portfolio weight? τ_{ijt} might be underestimated for poor countries?
- exog saving rate (supply side), orthogonal to R and τ? why? data evidence?

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- exog saving rate (supply side), orthogonal to R and τ? why? data evidence?
- ϵ is a key parameter in the whole quantitative exercise
- calibrated $\epsilon \approx$ *with-in* asset class demand elasticity in other papers

  $\Rightarrow$ helpful to see how results vary quantitatively with ϵ

Other Questions

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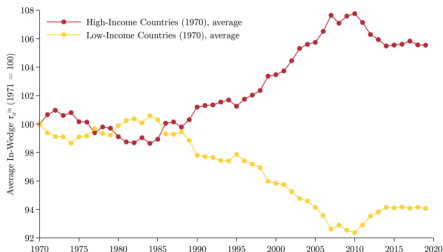## Other Questions

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FIGURE 9: CHANGE IN AVERAGE IN-WEDGES

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Nicely executed paper with very interesting quantitative results!