Discussion of

Collateral Advantage: Exchange Rates, Capital Flows, and Global Cycles

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Motivation

- NFA = Trade balance + **Valuation effects** (Gourinchas-Rey'07a,b,14)
- **Stylized facts** about U.S. int'l capital flows:
  1. leveraged asset position ("*global venture capitalist*")
  2. positive returns in normal times ("*exorbitant privilege*")
  3. transfer to the RoW in bad times ("*exorbitant duty*")
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- **This paper**:
  - i) leverage constraint (Gertler-Kiyotaki'10, Jermann-Quadrini'12)
  - ii) endogenous convenience yields (Engel-Wu'23, Jiang et al.'21)

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- Calibration: κ, κ^* target SS portfolios and convenience yields

$\kappa_h = 0.025$, $\kappa_f = 0.4$, $\kappa_h^* = 0.05$, $\kappa_f^* = 0.32$, $\kappa_{Kh} = \kappa_{Kf}^* = 0.41$, $\kappa_{Kf} = \kappa_{Kh}^* = 0.49$

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   - U.S. bonds are better collateral and earn convenience yield $r_f - r_h = 1\%$
   - equity premium of 5.7% and home bias of 70% in equity
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2. Global financial crisis ($\vartheta_t = \vartheta_t^* \downarrow$):
   - collateral premium $\uparrow$ $\Rightarrow$ U.S. UIP premium $\uparrow$ $\Rightarrow$ USD appreciates $S_t \downarrow$
   - $S_t \downarrow + Q_t, Q_t^* \downarrow +$ high U.S. leverage $\Rightarrow$ U.S. NFA $\downarrow$ (transfer to RoW)
   - tighter credit in the U.S. $\Rightarrow$ deeper recession $C_t, Y_t, I_t \downarrow$
   - valuation effects + rebalancing $\Rightarrow$ retrenchment

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- Assumptions:
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  - cf. with international risk sharing in IM'21: $c_t - c_t^* = -(\psi_t - \psi_t^*) + q_t$

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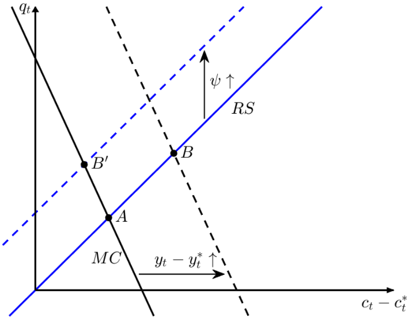

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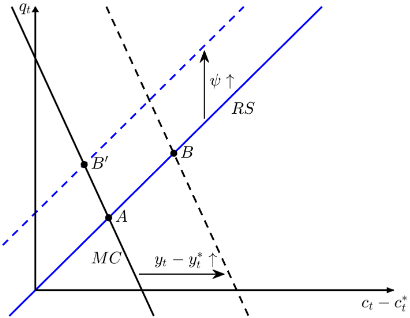

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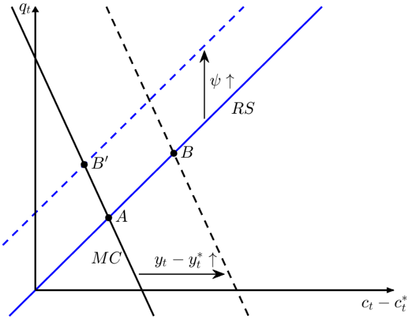

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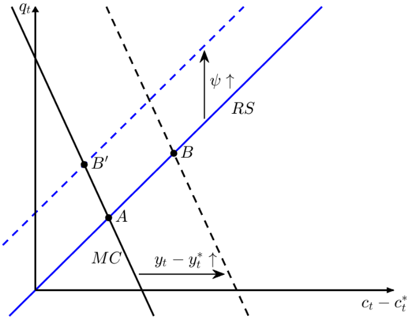

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- nominal/financial frictions $\Rightarrow$ $y_t - y_t^* \downarrow$ and $c_t - c_t^* \downarrow$
- is importance of LCP overemphasized?

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- Maggiori'17 = open-economy version of Brunnermeier-Sannikov'14
  - U.S. banks have less tight constraint
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- **What is different in Devereux-Engel-Wu?**
  - sticky prices + LCP?
  - de-leveraging shock?
  - asymmetric effect across bonds due to κ_i?

Comment #3: UIP vs. CIP

- **Model** with financial constraints $\Rightarrow$ **UIP**$\approx$**CIP**
- **Data**: **UIP**$\gg$**CIP**, often opposite sign (Bacchetta-Benhima-Berthold'23)

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- **GFC** of 2007-2009 might be special (Engel-Wu'22)
  - *use estimated CIP deviations as input and check model predictions?*