

Discussion of Raddatz & Schmukler

Ajay Shah

March 16, 2012

Finance is changing

The old classification:

- Asset pricing
- Corporate finance.

Emerging classification:

- Markets and prices
- Financial intermediaries
- Financing of firms
- Household finance.

This paper

- A remarkable new dataset
- Enables attacking a series of important questions about international mutual funds
- Striking, gloomy answers.

Investors



Behavioural biases

Agency problems

Fund managers



International
finance pathologies

Country

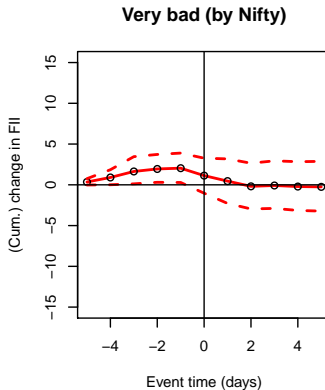
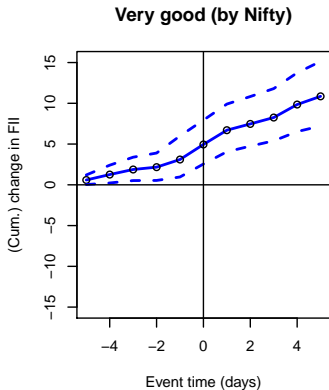
Who is the smart money?

- This paper shows international MFs are not the smart money, buying at fire sale prices
- They exacerbate the selling pressure in times of trouble and vice versa
- They are the liquidity demanders, not the liquidity providers
- Question 1: Does this damage their returns and how much?
- Efficient trades are being left on the table
- Question 2: Who takes these?
- Other foreigners – or locals? Hedge funds?
- I.e., who makes that excess return?

Estimation strategy

- A little nervous about the linear models that are being estimated.
- Can we analyse interesting events in the data using the event study methodology?
 - Country crises dates
 - Elections
 - Stock market and currency volatility?
 - Extreme low returns for a fund
 - Extreme high returns for a fund
 - Extreme events on the local index and on the local exchange rate
 - Extreme events on the local EMP
- Is behaviour in normal days different from behaviour in more extreme days?
- Our work: Responses to extreme days is a bit different.

Example: all foreign investors and extreme days of Nifty



So who is the smart money?

Are all countries alike?

- When investors take money away from an international MF, what would it do?
 - 1 Borrow to meet redemptions, sell index futures, liquidate slowly
 - 2 Sell more liquid markets
 - 3 Sell more liquid markets quickly, gradually sell off less liquid markets

More liquid markets → more extreme behaviour by such funds.

A research frontier

- EPFR data is making possible the study of funds investing in countries
- It would be interesting to go within the country and explore similar questions about individual firms.

Thank you.