Comments on
"Transmission of the U.S. Subprime Crisis to Emerging Markets: Evidence on the Decoupling-Recoupling Hypothesis"
by M.Dooley and M.Hutchison

NIPFP DEA conference, September 2009

Discussant: Hiroko Oura (IMF)

Questions and focus of the paper

- **Very topical issue**

  —Assessing EM-US decoupling at an early stage of the current global crisis and recoupling particularly after the collapse of Lehman.

- **What is driving?**

  —Change in structural linkages? Or more intense (frequency and magnitude) shocks from the US?

Summary of the paper

- Does US financial/real news impact on daily EM sovereign CDS spreads?
  - OLS regression of CDS spread on news.

…...Yes, especially some post Sept. 08 news

- Is it because of stronger transmission channels or more intense nature of shocks?
  - Measure equity market linkages (correlation) for Feb 07–mid May 08; mid May-mid Sept 08; mid Sep 08-Jan 09.

….correlation increased in the 2nd and 3rd phase across the board.

  - VAR analysis for equities in the US and Mexico.

…..Much larger impulse response from the US to Mexico

Comments on "structural change" discussion

- Some significant news events happened only after Sept. 2008

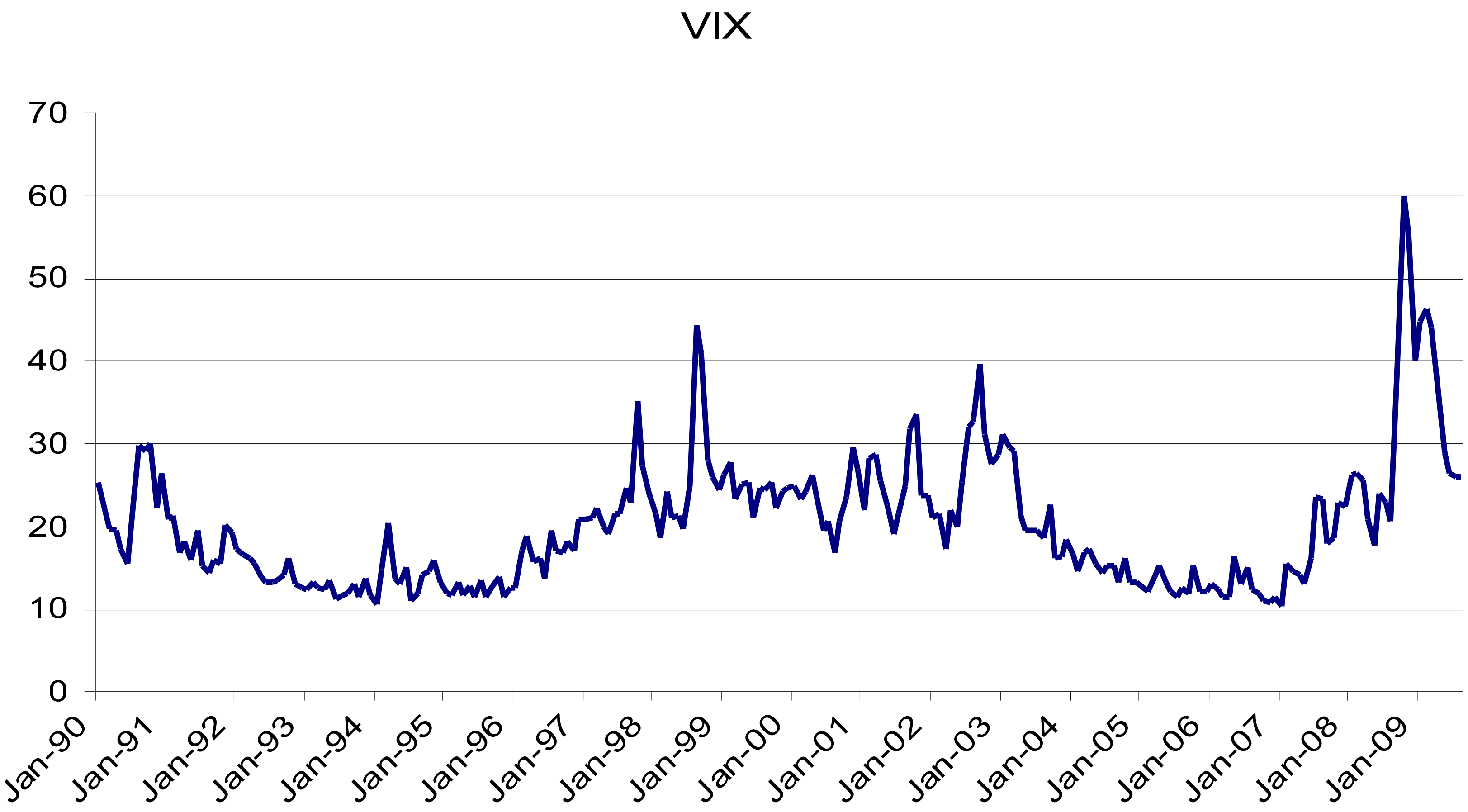
  …. Split sample focusing only on common types of news?

- "Headline" transmission measure possibly masking changing significance of different channels and emphasizing structural change aspect too much? US subprime crisis itself started to spread into the other sector only in fall 2008.
  - Real (growth, macro)
  - Financial markets
  - Policy coordination

…. Measure correlation or and estimate VAR to control for macro and policy coordination factors? (include interest rate)

Comments: correlations are conditional on market volatility

….Forbes and Rigobon JF 2002 type adjustment just for check?



Comments: possible nonlinearity of the transmission (real and financial) rather than structural changes?

- **Ad hoc discussion**

  Various hypothesis on India's real sector's reaction to the US real slowdown

- **Tail risks and extreme value theory**

  High "dependence" when "tail risks" materialize (more than what's indicated by correlation)

  - Correlation:

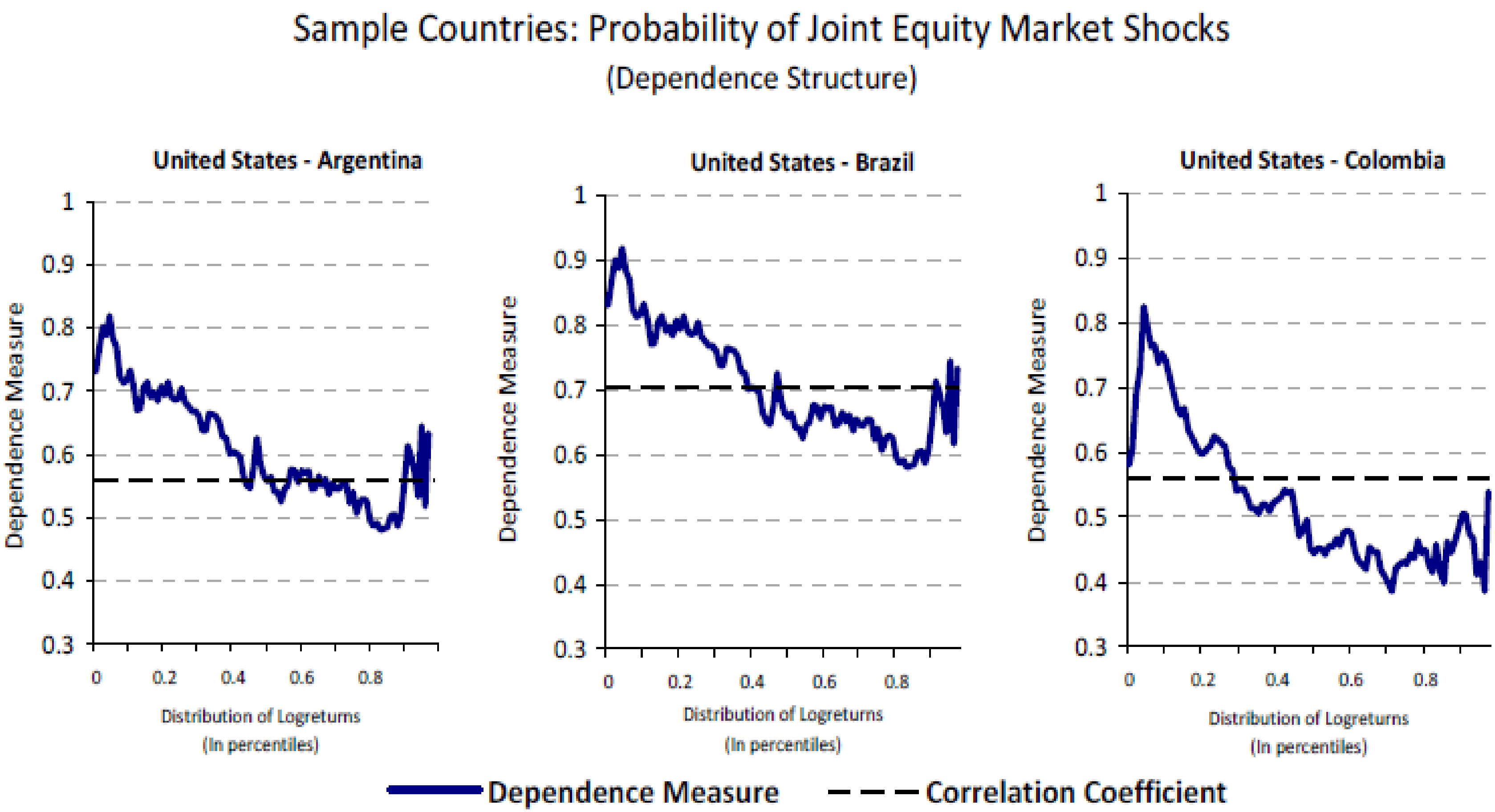
    average comovement across different return levels

  - Dependence:

    comovement for different segments of returns

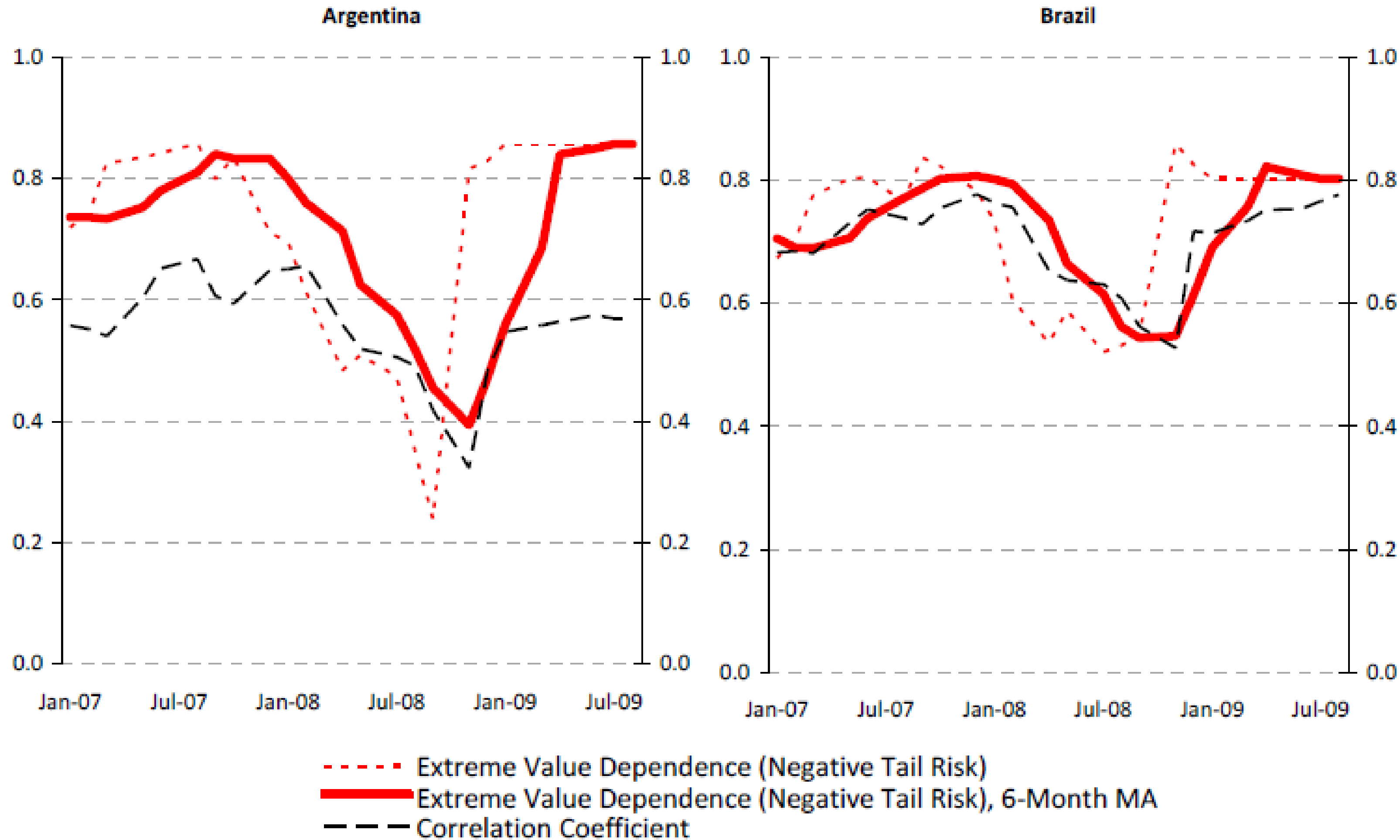
    In "tail" event of extreme sales pressures, stock markets move together more than normal times.

Extreme Value Dependence Measure (A. Jobst (IMF))



ctnd.

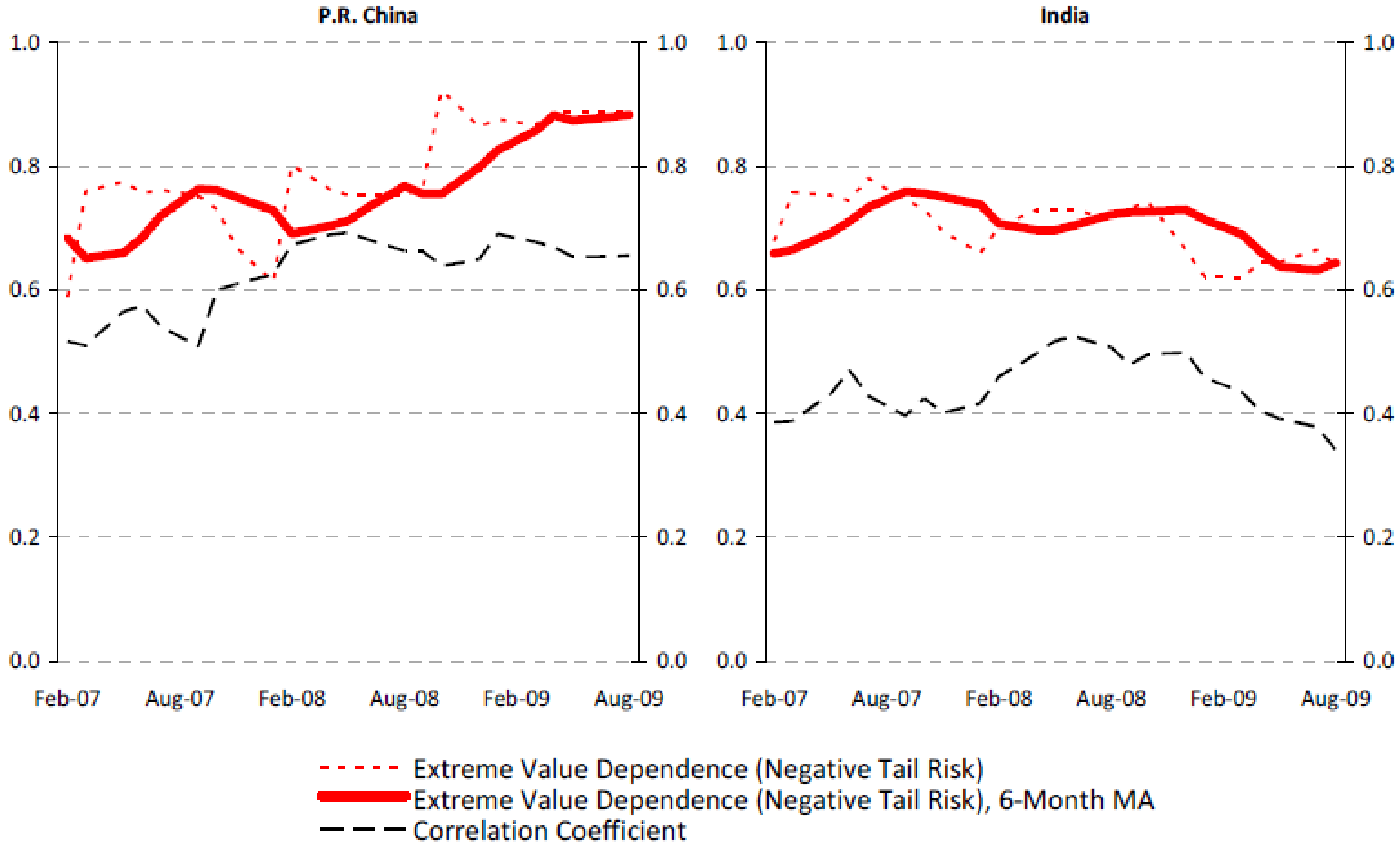
Latin America: Probability of Joint Equity Market Shocks with the United States
(Time-varying Dependence Value)



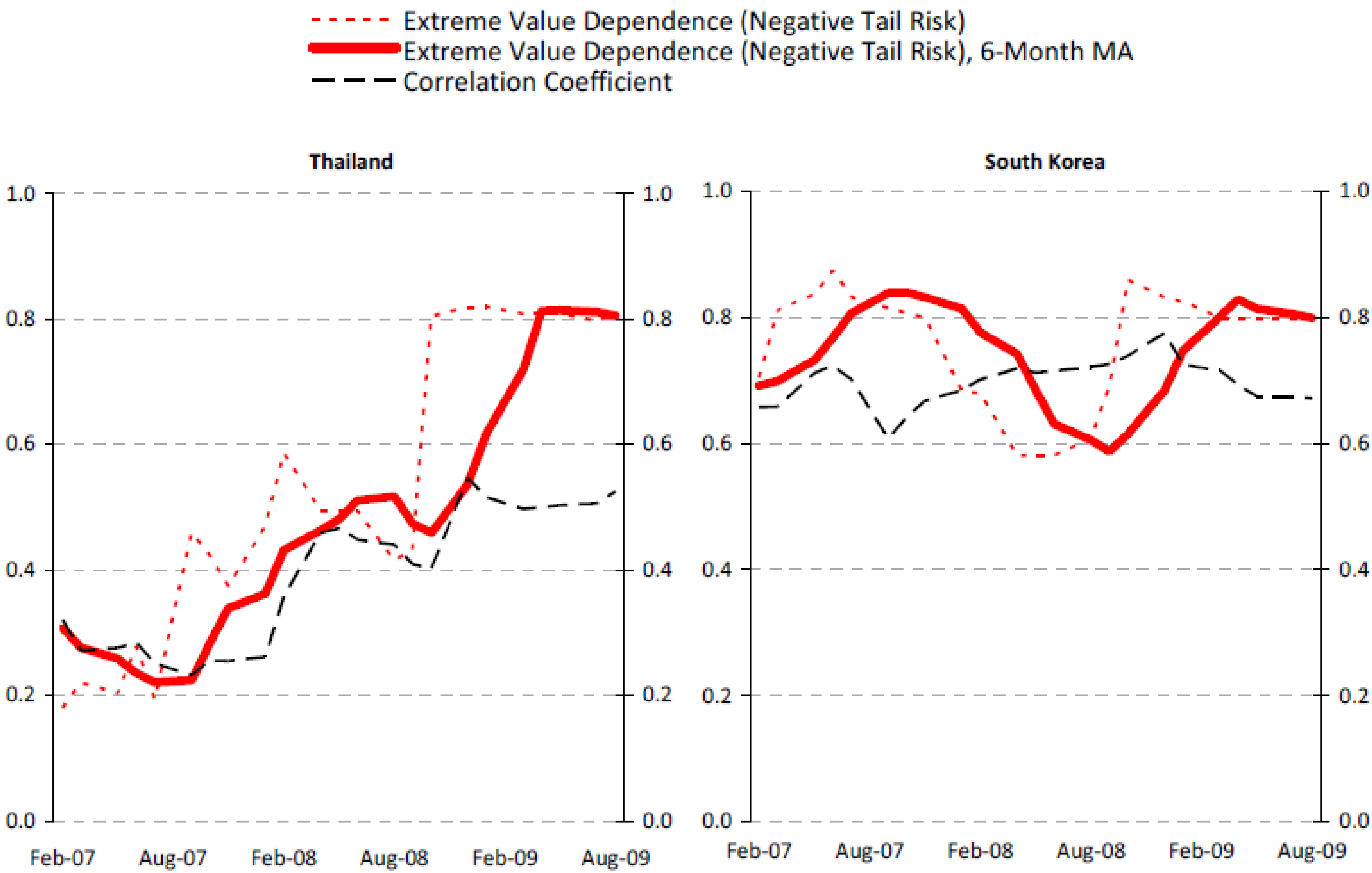
Ctnd.

Emerging Asia: Probability of Joint Equity Market Shocks with Japan

(Time-varying Dependence Value)



Ctnd.



Extreme Value Dependence (Negative Tail Risk)
Extreme Value Dependence (Negative Tail Risk), 6-Month MA
Correlation Coefficient
Thailand
1.0
0.8
0.6
0.4
0.2
0.0
Feb-07
Aug-07
Feb-08
Aug-08
Feb-09
Aug-09
South Korea

Overall…

- Agree: EM are influenced by this US-originated crisis (real and financial) …(?) structural change

- So is this a death notice for “good” policies in the EMs?

  If a series of “preventive policies” can’t stop spillover effects from developed market crisis, what can they do? Do they need to live with it or should additional policy measures be taken?