JEEA Volume 13-3, June 2015

Abstracts

JEEA-FBBVA Lecture 2014: Sovereign Debt Sustainability in Advanced Economies  
Fabrice Collard, University of Bern, Michel Habib, University of Zürich, Swiss Finance Institute and CEPR and Jean-Charles Rochet, University of Zürich, Swiss Finance Institute, and Toulouse School of Economics/IDEI

We develop a measure of maximum sustainable government debt for advanced economies. How much investors are willing to lend to a country’s government depends on the country’s expected primary surplus, the level and volatility of its rate of growth, and how much debt the government expects to be able to raise in the future for the purpose of servicing the debt it seeks to raise today. We provide a simple formula that computes a country’s maximum sustainable debt (MSD) as a function of four easy-to-estimate parameters. We further compute a country’s theoretical probability of default (PD) as a function of its debt-to-GDP ratio. We finally calibrate our measures for 23 OECD countries and test the relation between sovereign yield spreads and our theoretical PD at prevailing debt levels. We find it to be strongly statistically significant. (JEL: H63)

Common Components of Risk and Uncertainty Attitudes Across Contexts and Domains: Evidence from 30 Countries  
Ferdinand M. Vieider, WZB Berlin Social Science Risk and Development Unit, Mathieu Lefebvre, Center, University of Montpellier 1, LAMETA, Ranoua Bouchouicha, Henley School of Business, University of Reading, Thorsten Chmura, Nottingham University Business School, Rustamdjan Hakimov, WZB Berlin Social Science, Michal Krawczyk Center University of Warsaw and Peter Martinsson, University of Gothenburg

Attitudes towards risk and uncertainty have been indicated to be highly context-dependent, and to be sensitive to the measurement technique employed. We present data collected in controlled experiments with 2939 subjects in 30 countries measuring risk and uncertainty attitudes through incentivized measures as well as survey questions. Our data show clearly that measures correlate not only within decision contexts or measurement methods, but also across contexts and methods. This points to the existence of one underlying ‘risk preference’, which influences attitudes independently of the measurement method or choice domain. We furthermore find that answers to a general and a financial survey question correlate with incentivized lottery choices in most countries. Incentivized and survey measures also correlate significantly between countries. This opens the possibility to conduct cultural comparisons on risk attitudes using survey instruments. (JEL: D0, D81, C90, J10)

Relationship Lending During a Financial Crisis  
Enrico Sette, Bank of Italy and Giorgio Gobbi, Bank of Italy

This paper studies whether relationship lending mitigates the transmission of the Lehman default shock to the supply of credit in Italy. Exploiting the presence of multiple banking relationships, we control for banks’ and firms’ unobserved characteristics. Results show that the growth of credit itself is higher and its cost lower the shorter the distance between the bank and the firm, the longer the relationship and the higher the share of credit held by the bank. Credit growth by relationship lenders is 4.6% higher than that by transactional lenders; the increase in the cost of credit is 50 basis points lower. The positive effect of relationship lending on credit supply increased during the crisis, compared to a pre-crisis period. The beneficial effect of relationship lending is weaker if the relationship lender is more exposed to the financial crisis, especially when lending to weaker borrowers. (JEL: G21, G01)
Economies of Scale and the Size of Exporters
Roc Armenter, Federal Reserve Bank of Philadelphia and Miklós Koren Central European University

How important are economies of scale in exporting? We argue that firm size cannot be the main determinant of export status if a model is to be consistent with the observed number and size of exporters. Instead, we need a lot of variation independent of firm size to reconcile the model with the data. We show the augmented model also has markedly different implications regarding the margin of adjustment in the event of a trade liberalization: Most of the adjustment is through the intensive margin and productivity gains due to reallocation are halved. (JEL: F12)

The International Transmission of Volatility Shocks: an Empirical Analysis
Haroon Mumtaz, Queen Mary College and Konstantinos Theodoridis, Bank of England

This paper proposes an empirical model which can be used to estimate the international transmission of volatility shocks. Using this model we estimate that a one standard deviation increase in the volatility of the shock to US real GDP leads to a decline in UK GDP of 1% relative to trend and a 0.7% increase in UK CPI relative to trend at the two year horizon. Using a non-linear open economy DSGE model, we find that these empirical estimates are consistent with the response to a perturbation to the volatility of foreign ‘supply’ type shocks, while an increase in the volatility of demand shocks has a negligible impact. (JEL: F42, F47, C32)

The Failure to Predict the Great Recession. A View through the Role of Credit
Maria Dolores Gadea Rivas, University of Zaragoza and Gabriel Perez-Quiros, Bank of Spain

Much has been written about why economists failed to predict the latest crisis. Reading the literature, it seems that this crisis was so obvious that economists must have been blind not to see it coming. We approach this failure by looking at one of the key variables in this analysis, the evolution of credit. We compare the conclusions reached in the recent literature with those that could have been drawn from an ex ante analysis. We show that the effect of credit on the business cycle cannot be exploited from a policymaker’s point of view. (JEL: C22, E32)