Search for Yield in Large International Corporate Bonds

(Calomiris, Larrain, Schmukler, Williams)

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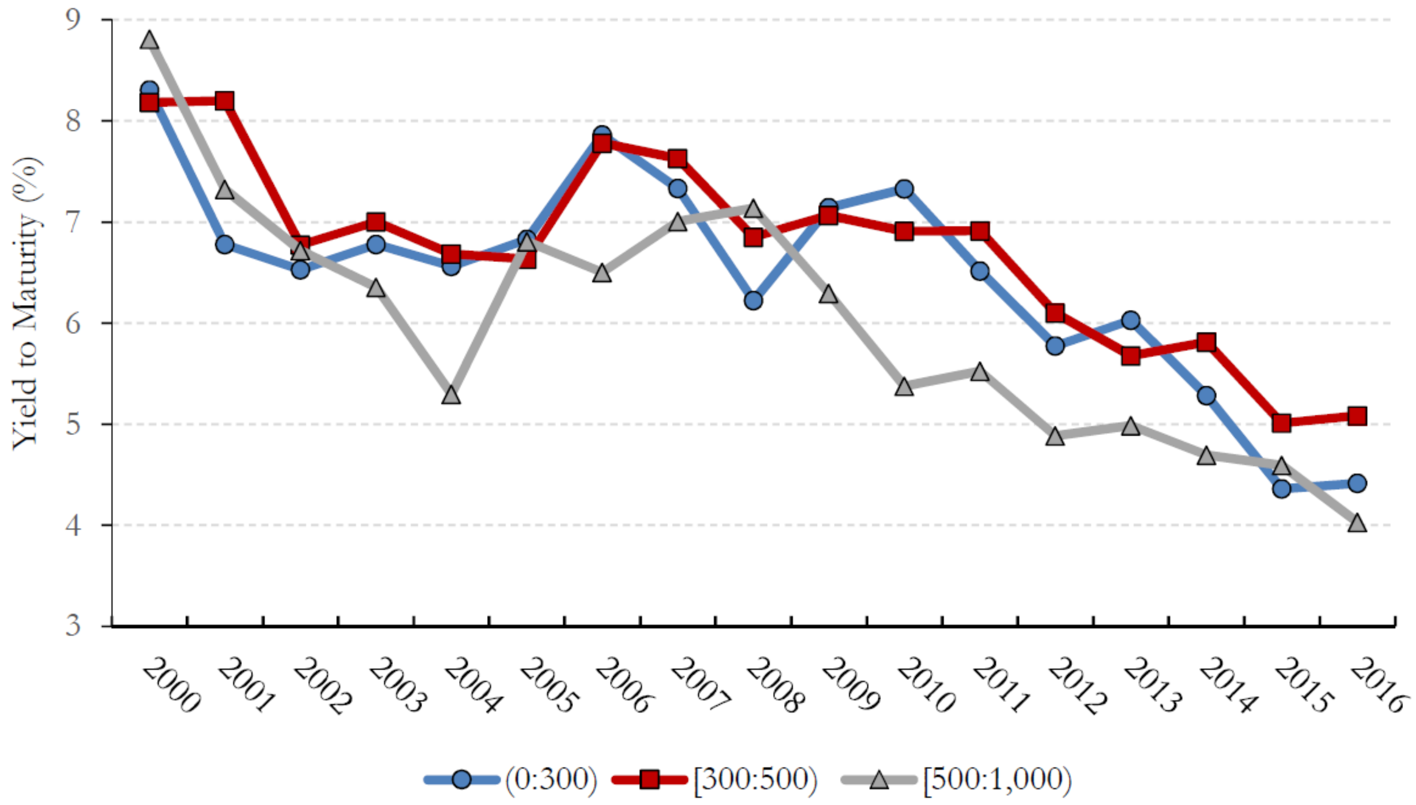
Theoretical Premise

- Post 2008, cyclical and monetary policy conditions in AEs led to greater demand for EM assets
- ⟶ Less specialized and inexperienced managers enter this markets
- ⟶ Greater reliance on indexes ⟶ greater preference for index-eligible bonds
- ⟶ Spread around cutoff issuance size ($500M) increases
- ⟶ Firms issue more than they need to benefit from rate reduction
- ⟶ Effects greater in countries with attractive carry trades

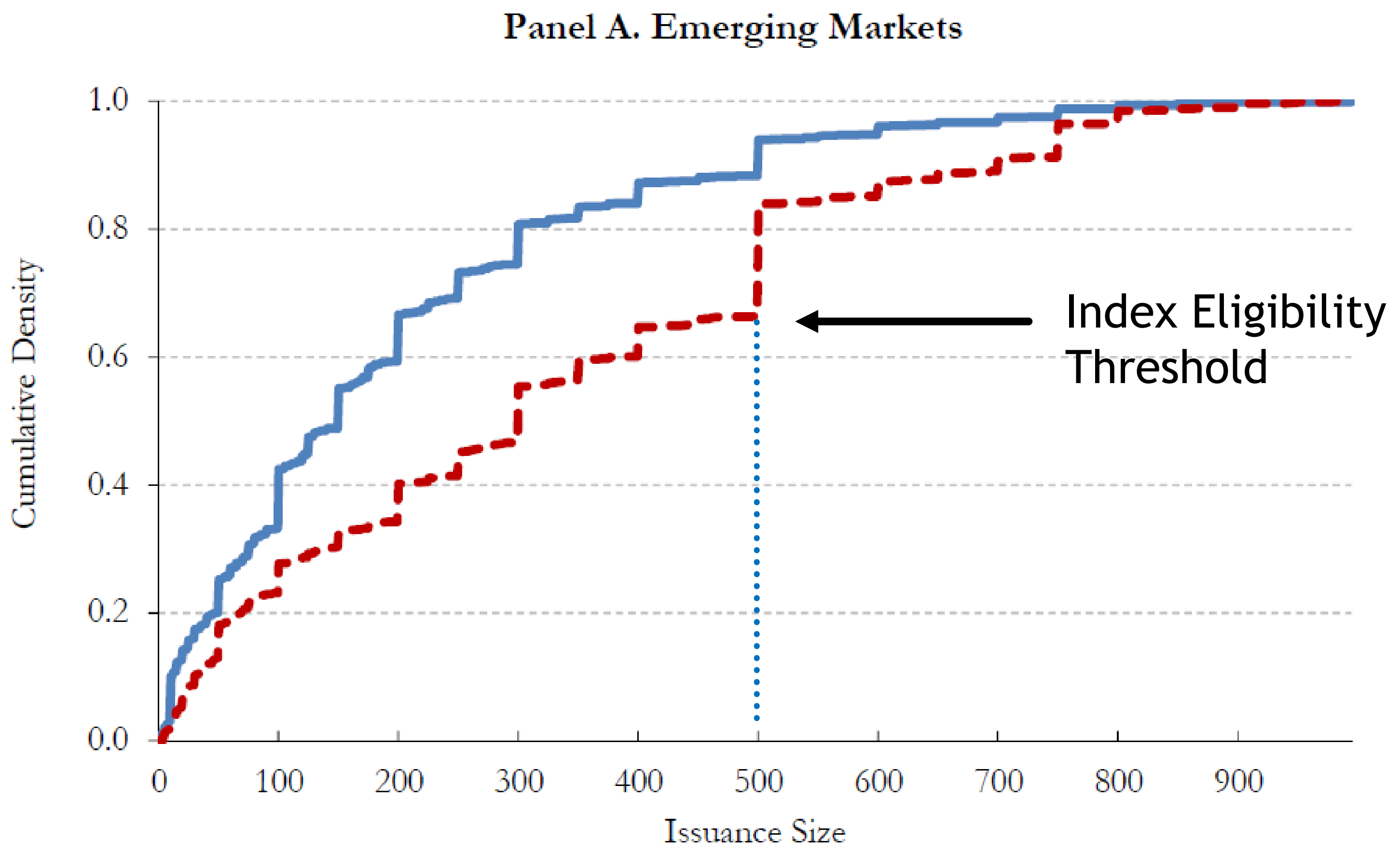
Background: Drop in EM Corporate Yields



Decline in yields starts well before GFC (QE etc.). But sharp drop for large issuance post 2008

What about 2000-2004? Role for MP cycle beyond post-GFC period

Evidence of Increased Bunching at Threshold



Generalized shift toward larger issuances. More pronounced for middle of distribution

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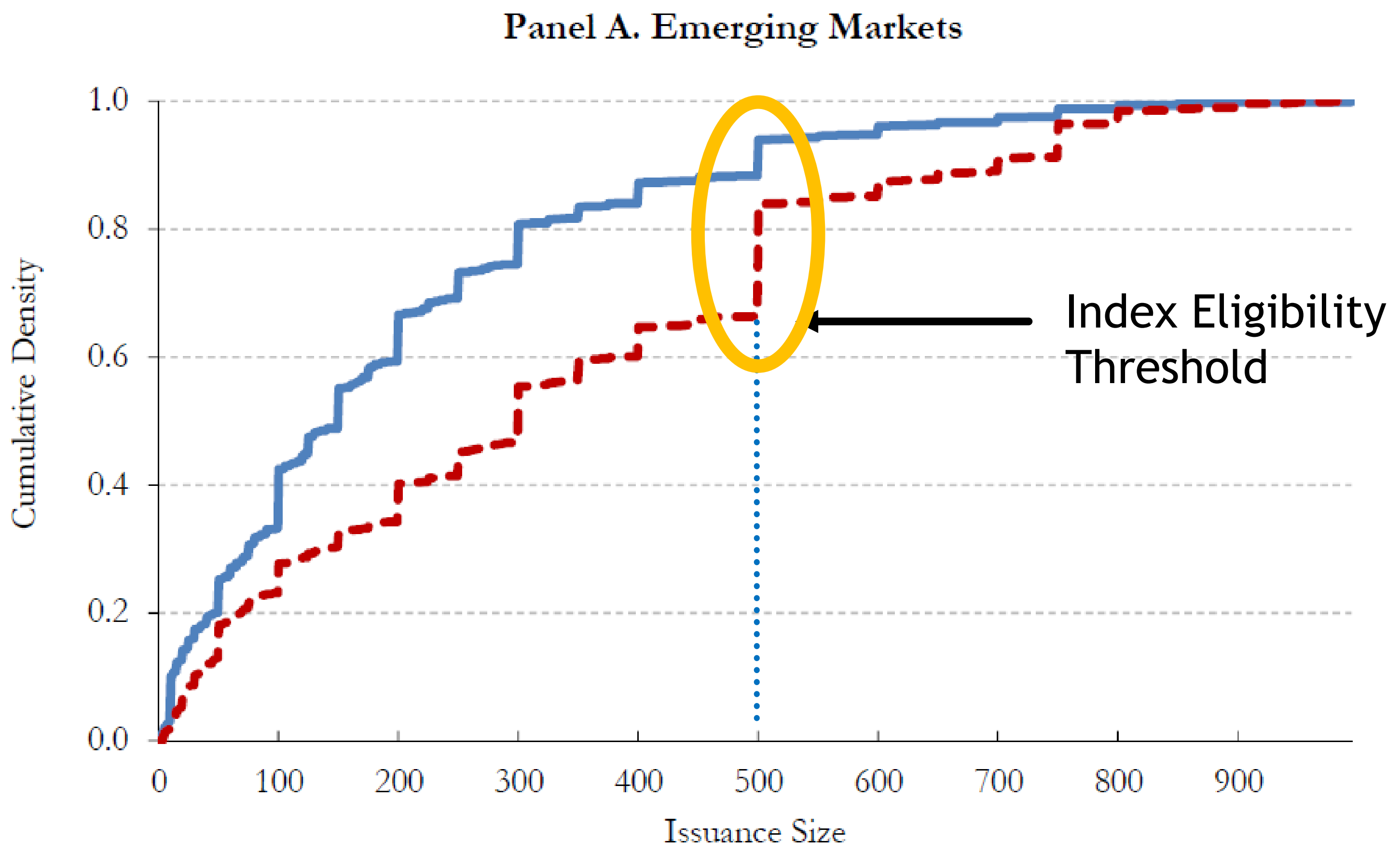

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Role of non-specialized funds

- Reasonable hypothesis that “cross-over” funds would rely more on index than specialized ones
- Finding: greater relative holdings of >$500M bonds
- But wouldn’t specialized fund fill the void (arbitrage)?
- Why not look more directly at whether in countries where cross-over funds have greater presence the spread around $500 is greater?
- Also country-specific regressions (at least for large markets)? FE take care of levels, but not trends/deltas. At least interact FE with post2008 dummy.
- Country level regressions would also be interesting to see if the effect is driven by particularly information-sensitive markets.

Relevant interest rate benchmark

- Firms from countries with a more attractive carry trade (adjusted for volatility) tend to issue more >$500M bonds
- Why should country-specific carry matter? Firms could invest the “extra” cash anywhere, including in the US
- An alternative interpretation is that local rates are the opportunity cost of not borrowing from abroad
  - If so shouldn’t we focus on the spread (Y*-Y) and look at how it evolved over time?
- Is this just picking up the cycle?

Nitty-Gritty Stuff

- Difference in post-2008 yield coefficients for $\beta400$-$\beta500$ seems to come from a positive premium in $\beta400$ rather than a negative one for $\beta500$ (Table 3)
  - Indeed, I think there would be a similar result for $\beta400$-$\beta300$
  - What is the story here?
- Placebo test (uses variable rate bonds not index-eligible): why just for issuances? Ok variable rates, but could look at how they are trading.
- Was the index-eligibility threshold ever changed? If so, it would provide a nice experiment opportunity.
- Does it matter what firms do with funding?
  - Look at whether cash on balance sheet affects yields

Conclusions

- Very interesting and well executed paper
- Highlights importance of index eligibility at corporate level
- Critical interaction with monetary/financial conditions at center
- Opportunity for further insights by looking at more disaggregated specifications