Discussion of “Invoicing Currency Concentration and Currency Risk Premia” by Bengui & Sander

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[a]The views expressed herein are those of the authors and do not indicate concurrence by the Federal Reserve Bank of Boston, the principals of the Board of Governors, or the Federal Reserve System.

Summary of Findings

- Paper argues that invoicing currency concentration can explain cross-section of interest rates, currency risk premia, and carry trade.
- Currency invoicing concentration affects consumption risk and the role of different country bonds for hedging this risk.
  - Countries with higher share of invoicing in dominant currency provide superior hedges, hence lower interest rates
- Paper argues that invoicing concentration is novel and primal factor compared with previously documented country size or trade centrality.
  - Basic intuition is that large countries have a higher share of their consumption denominated in own currency.

Overview of Discussion

Comments on Model

Comments on Empirics

Comments on Model

Comments on Empirics

Recap on Model Structure

- Two-period multi-country rigid-price model
- Households have log-linear utility in consumption and labor
- Firms produce goods using (domestic) labor only and are subject to country-specific productivity shocks
- Consumption bundles is aggregate of goods from many origin countries
- Bilateral trade invoicing (DCP, PCP, LCP) is source of shock transmission
- Arrow-Debreu securities used for synthetic asset pricing of bonds

Comments on Key Assumptions

- The following assumptions are made for analytical tractability:
  1. Prices for internationally traded goods are completely fixed
  2. No other production factors than labor (esp. no internationally sourced intermediate inputs or capital)
  3. Monetary policy assumed to fix marginal cost of domestic production $\Rightarrow$ wage is proportional to productivity shock
- Can the authors discuss what happens when you allow for
  1. alternative price adjustments
  2. exposure through supply side

Comments on Model

Comments on Empirics

Paper provides some empirical support for model

- Paper tests the following two main predictions from the model:
  1. Bilateral consumption correlation related to invoicing currency shares
  2. Currency concentration is driver of country risk premia
- Authors look at 20 countries (which?) from 1990–2020:
  - Interest rate differential measured by forward premia (CIP deviations?)
  - Currency invoicing shares from Boz et al. (2020), mapped into consumption invoicing shares.
  - Consumption invoice concentration and correlation constructed under i.i.d. assumption for productivity shocks.

Where is the identifying variation?

- Show summary statistics:
  1. Esp. for variables computed using model structure (show impact of shock calibration)
  2. Report both within and between variation of each variable
  3. Given small cross-section, just report statistics by country
  4. Would be nice to see regression results using within-country variation
- Bring data closer to model (and vice versa?):
  - Need to better control for factors that are not in the model (e.g., trade in production factors).
  - Gross import invoicing share vs net share, or even added-value based?
- Clarify sample and variables for each table, calculation of standard errors, etc.

Conclusion

- Neat model to highlight novel, interesting channel that can explain cross-country differences in key variable of interest in international finance
- My main suggestions are to bring the empirics closer to model and to discuss impact of key assumptions.
- Overall, nice contribution to the international finance literature.