Discussion of
Claessens Kose Terrones
“How Do Business and Financial Cycles Interact?”

Frank Warnock

FRBNY Conference
“Global Dimensions of the Financial Crisis”
What the paper sets out to do (1)

- Systematically dates recessions/recoveries and fin’l upturns/downturns for a long, broad dataset (44 countries, 1960 or 1978 until 2009).
  - Identify turning points in macro and financial variables using a Harding/Pagan business cycle dating algorithm.
  - Label severe episodes
    - Fin’l up/downturns in 1^{st} and 4^{th} quartiles are labeled disruptions and booms.
What the paper sets out to do (2)

• Analyze the interactions between business and financial cycles.
  - Synchronization (concordance stat), conditional likelihood of being in a recession when also financial disruption
  - Are recessions (recoveries) associated with financial disruptions (booms) different?
  - Is there an empirical link between duration and amplitude of recessions/recoveries and financial market events?

• Say something about the current episode.
  - Was the severity of 2007-09 recessions to be expected based on the extent of financial market disruptions?
Main results (1)

- The systematic coding of financial upturns/downturns and booms/disruptions

- FCs longer and sharper than BCs
  - Recessions/recoveries typically last 4-6 quarters; Financial downturns/upturns can be 6-18 quarters
  - Recessions/recoveries: change in GDP of 2-9 percent; Financial downturns/upturns changes of 6 to 60 percent
Main results (2)

• BCs and FCs synchronized, with BCs being more synchronized with credit and house price cycles than with equity price or exchange rate cycles
  - 80% of the time, the credit and business cycles are in same phase.
  - About twice as likely to be in a recession (recovery) if in a credit crunch (boom).

• FCs play an important role in shaping recessions and recoveries
  • Recessions assoc w/ fin’l disruptions longer/deeper.
  • Recoveries assoc w/ rapid FC recovery stronger.
The paper’s contribution

• Across a large set of countries, systematically identify BC and FC episodes and explore their interactions.

• Much of the literature focuses just on the recession phase or on a limited set of countries.
  - Example: CKT (2009 EP). For OECD countries, focuses on recessions and finds that recessions assoc. w/ credit crunches and house price busts longer/deeper.

• Much of the literature identifies FC episodes in a manner that is subject to debate (see, for example, Reinhart Rogoff v. Lopez-Salido Nelson).
  - This paper uses an easily understood econometric approach.
What I’d like to see more of

• It is mentioned in the conclusion that the stylized facts present a challenge for theorists.
  - I’d prefer some reweighting toward implications for existing theories. Flesh this out more.

• The paper is still focused on the recession/downturn episodes (and the periods immediately following…the recovery/upturn).
  - The periods just prior to recessions/downturns are also important.
“…abnormal increase in gross flows should be a warning sign.”


Forbes and Warnock (2010)
“…abnormal increase in gross flows should be a warning sign.”

This of course ended in mass retrenchment…

Forbes and Warnock (2010)
My take on the paper

• Carefully executed paper, exhaustive attempt to systematically create important stylized facts on BC and FC episodes.

• The paper is useful for
  - empiricists looking to code recession/recovery and fin’l upturn/downturn episodes in a wide range of countries.
  - theorists looking for stylized facts to inform their modeling.
The final slide

• It’s an important topic

• Empiricists and theorists will find it useful.

• I enjoyed the paper.