“Exchange Rate Risk in Public Firms”

Discussion

by

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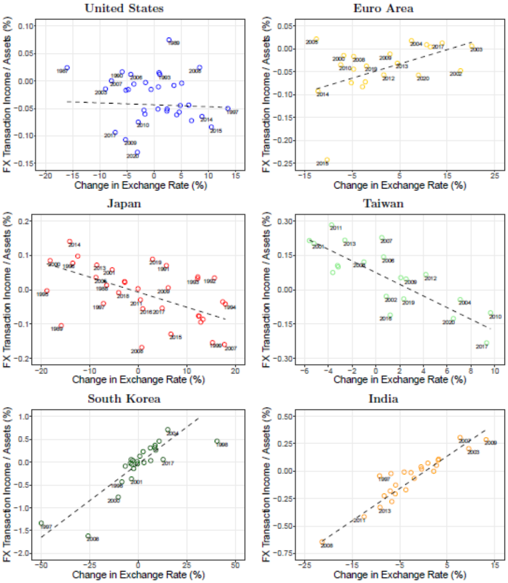
Disclaimer: The views expressed do not necessarily reflect those of the ECB and/or the Eurosystem

Intro

- A very rich & interesting paper!
- Evidence on the pass-through of exchange rates to "firm performance"

What does the paper do?

- FX Transaction Income (FXTI): an accounting-based measure of firm exposure to FX risk
  - covers "monetary items": cash, accounts receivable/payable, loans & debt payments, deferred taxes, etc.)
  - does not cover: inventories, PP&E, goodwill & intangibles, ...
  - net of hedging (very nice feature!)
- country-level aggregates of FXTI co-move with FX rate
  - especially outside US/EA (invoicing!)
  - not always in the same direction


United States
Euro Area
Japan
Taiwan
South Korea
India
FX Transaction Income / Assets (%)
Change in Exchange Rate (%)

What does the paper do?

- At the firm-level, FXTI
  - is economically large: Q75 $\sim$ 0.3-0.7% (5-14%) of assets (profits)
  - variation is well-explained by
    - industry-level net exports
    - FX debt
  - passes through to profits (little "operational" hedging)
  - is reflected in stock returns

Comments

- The results on pass-through of FXTI on profits are very interesting

$$\frac{Income_{i,t}}{Assets_{i,t}} = \alpha_i + \theta_{I(i),t} + \beta \frac{FXTI_{i,t}}{Assets_{i,t}} + \epsilon_{i,t}$$

- A good opportunity to explore heterogeneity?

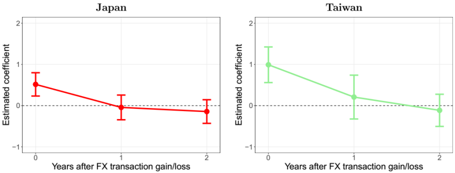
$$\frac{Income_{i,t}}{Assets_{i,t}} = \alpha_i + \theta_{I(i),t} + \beta \frac{FXTI_{i,t}}{Assets_{i,t}} + \gamma \left[\frac{FXTI_{i,t}}{Assets_{i,t}} \times X_{i,t} \right] + \epsilon_{i,t}$$

- In particular, $\beta < 0$ for $Income = Op.\ Income$ (although not always significant)

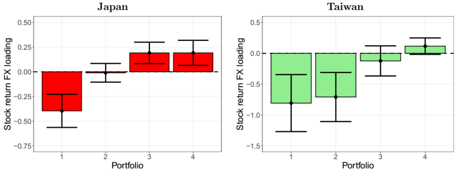
- What firms engage more (are better at) "operational hedging"?

Comments

- FXTI has only a transitory effect on profits



- FX shocks tend to be persistent, but maybe prices & competition adjust quickly
- Q1: What do firms do with the extra profits: invest? pay out?
- Q2: How to square with permanent valuation effects?



Comments

- How are “multi-nationals” treated?
- Nestle produces goods in 79 countries and sells them in 186 countries
- BMW is the largest car exporter of the US
- Can this explain the absence of large effects for EA/US?
- Informativeness of WIOD data?

Additional minor comments

- Low number of obs. for US ($\sim$ 500/year). Why?
- Commodities vs. other inputs?
- Why India, South Korea and Taiwan?
- Only listed (=large) firms. Selection effects?

Additional minor comments

- I very much enjoyed reading the paper!
- rich data, informative analysis, well-executed
- it will be interesting to move beyond profits
- I look forward to seeing the next version