Discussion of Corporate Debt Structure with Home and International Currency Bias by Maggiori, Neiman, and Schreger

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This Paper: Facts

Two facts using data from Maggiori, Neiman and Schreger (2020 JPE):

1. Investors tend to lend either in their own currency or in one of two international currencies (USD/EUR).
2. When firms issue debt, they begin with issuing in their own currency. The largest issuers then pivot to the USD/EUR.

This Paper: Model

Interpret these facts using a Melitz-Style model, where (i) each firm faces downward sloping demand for its debt in a given currency (ii) firms can pay a fixed cost to borrow in multiple currencies.

1. Only most productive/largest firms borrow in multiple currencies.
2. These large firms have a lower (average) cost of capital.
3. Lower (average) cost of capital for firms headquartered in a country that issues the international currency.

$\Rightarrow$ Another *kind* of exorbitant privilege, particularly for small and medium-sized firms based in the US (who would otherwise not be productive enough to borrow internationally)

Comments

- Part of a broader and very successful "Global Capital Allocation Project."
- Project provides data on asset holdings (demand), security-level data on bond holdings by mutual funds around the world – "home currency bias".
- This paper takes an important step to start thinking about effects on **allocations**:
  - Lower cost of capital by issuing in multiple currencies
  - Lower cost of capital for US firms.
  - "Quantity" exorbitant privilege.
- Put this in the broader context of how FX and currencies interact with capital accumulation.

FX and Capital Accumulation

- Firm should install just enough capital for its expected marginal product of capital to equal the required rate of return to capital:

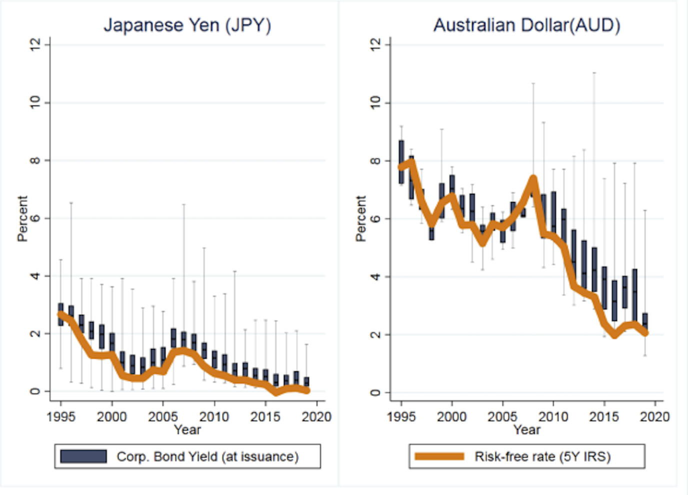
$$\mathbb{E}\left(MPK_{i,c}\right) = r_c^f + RP_{i,c}$$

1. **Currency risk** literature: safer currencies have lower risk-free rates.
   r_c^f vary across countries and depend on FX regime.
   Lustig & al. 2011; Hassan 2013; Ready & al. 2017; Richmond 2019; ...

$\Rightarrow$ Firms in countries with safer currencies accumulate more capital.

UIP Violations and Firms' Borrowing Costs (Richers, 2020)

- UIP violations pass through 1:1 to local firms' borrowing costs.



UIP Violations and Firms' Borrowing Costs (Richers, 2020)

- UIP violations pass through 1:1 to local firms' borrowing costs.
- CIP violations and sovereign default premia do not.

	$y_{i,t}^{j,d} - r_t^{\$,d}$		
	(1)	(2)	(3)
$r_t^{j,d} - r_t^{\$,d}$	1.091***	0.917***	0.918***
	(0.102)	(0.017)	(0.015)
CDS Differential	0.125		
	(0.130)		
CIP violation			0.036
			(0.056)
N	16,918	13,728	24,255
R^2	0.66	0.89	0.88
Maturity-Year FE	Y	Y	Y
Sector-Year FE	Y	Y	Y
Controls: Firm Characteristics	Y		
Firm-Month FE		Y	Y

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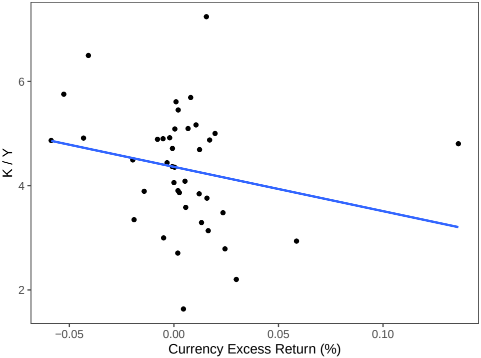
Currency Risk and Capital Allocation



We observe this strong negative relationship between capital accumulation and currency excess returns in the data at an aggregate level.

FX and Capital Accumulation

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$$\mathbb{E}\left(MPK_{i,c}\right) = r_{w,i}^f + RP_{i,c} \text{ for large firms}$$

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   r_c^f vary across countries and depend on FX regime.

   Lustig & al. 2011; Hassan 2013; Ready & al. 2017; Richmond 2019; ...

$\Rightarrow$ Firms in countries with safer currencies accumulate more capital.

2. **This paper**:

- Ability to issue in USD/EUR lowers cost of capital.
- An extra "quantity" exorbitant privilege for US and EU firms.

Advantage from Foreign Borrowing (Richers, 2020)

- Firms in countries with lower interest rates have lower ROA.
- Firms that issue internationally have lower ROA.

	$\overline{ROA}_{i,t+5}$		
	(1)	(2)	(3)
$r_t^j - r_t^\$$	0.570***	0.520***	0.527***
	(0.100)	(0.073)	(0.085)
$(r_t^j - r_t^\$) \cdot \mathbb{I}_{i,t}^{\text{Foreign Issuer}}$	-0.343*	-0.310*	-0.305*
	(0.173)	(0.163)	(0.155)
$I_{i,t}^{\text{Foreign Issuer}}$			-0.16
			(0.377)
N	8,740	7,910	7,910
R^2	0.24	0.27	0.27
Firm-level Controls		Y	Y
Sector-Year FE	Y	Y	Y

Conclusion

- Great paper.
- Important agenda: link between FX and capital accumulation.
- Lower cost of capital for firms in high interest rate currencies that are able to issue internationally.
- Read the paper!