

Discussion “Learning from History: Volatility and Financial Crises” by Danielsson, Valenzuela and Zer

Nicola Limodio

LSE-Bocconi-Princeton

“Schumpeter, Minsky, and the FCA” Conference

June 2017

Initial Comments

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Great Paper!

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Important Question, Novel Data (60 countries, 200 years)

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"Positive" View of Volatility

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"Positive" View of Volatility

Econometric Model

Research Question

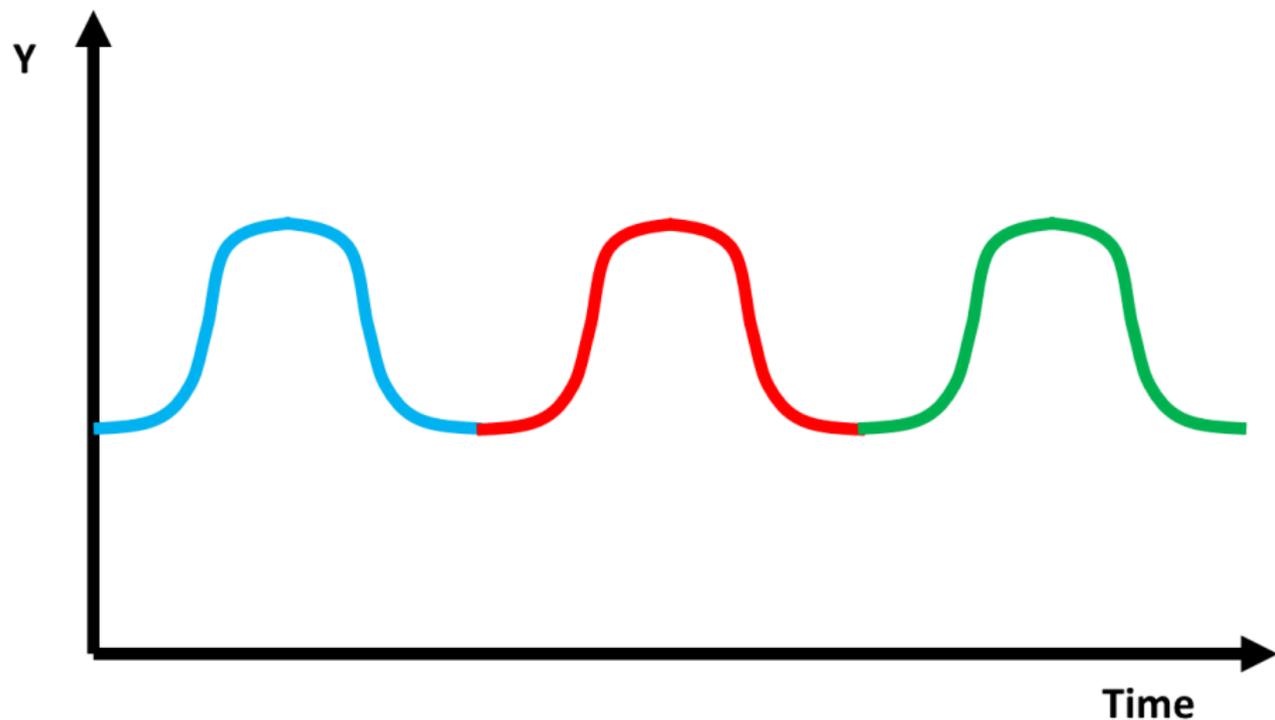
Research Question

How does Volatility affect
the probability of a Financial Crisis?

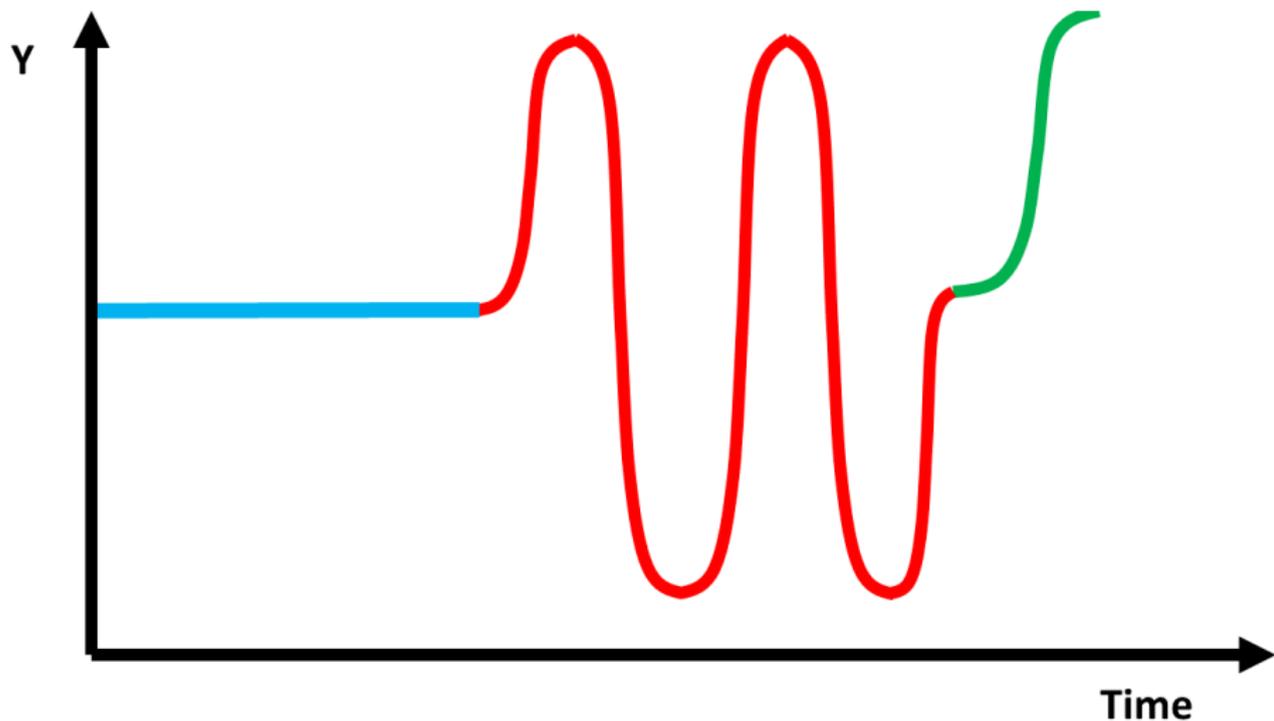
Argument

Naive View - Economy Goes Through Cycles

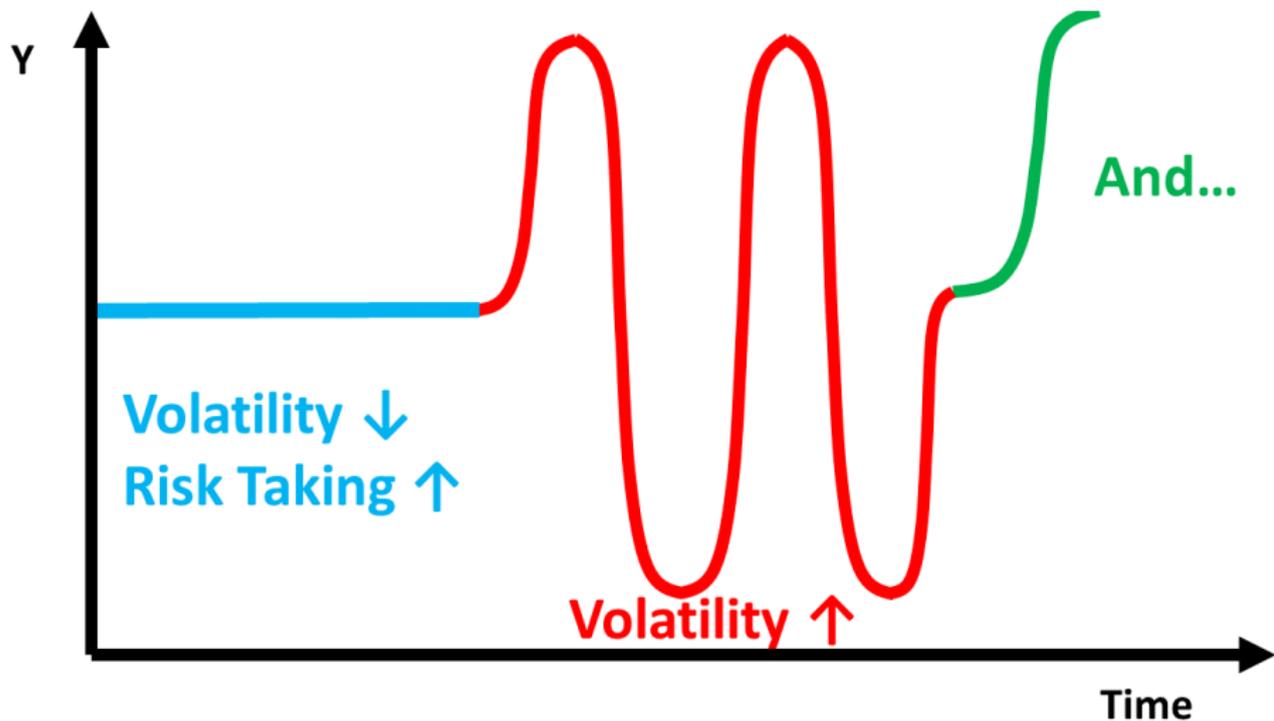
Naive View - Economy Goes Through Cycles



Widespread View - Cycles Not Predetermined



Widespread View - Cycles Not Predetermined



The Big Crash



Mechanisms

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Minsky (1992); Danielsson et al (2012); Brunnermeier & Sannikov (2014)

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3. Volatility \downarrow \rightarrow Long-term rates by banks \downarrow \rightarrow Risky projects \uparrow

Choudhary & Limodio (2017), Natural Experiment in Pakistan

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Low volatility DOES

2. Mechanism

Low volatility → credit build-ups & risk-taking

3. Volatility-Crisis relations increases over time

Bretton-Woods ↓, then speeds up

4. Volatility affects banking crisis and not currency crisis

Comments

“Positive” View of Volatility



“Positive” View of Volatility



Do periods of low volatility predict booms as well as crises?

“Positive” View of Volatility



Do periods of low volatility predict booms as well as crises?

How does low volatility emerge?

**"AFTER ALL, WE
ARE NOTHING
MORE OR
LESS THAN WHAT
WE CHOOSE
TO REVEAL"**



Econometric Model

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Estimated Equation

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Alternative specification: a diff-in-diff volatility, dummy-below zero & interaction

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Possible appendix to study the sensitivity to windsorization

Wrap Up

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→ Important Question, Intuitive Mechanism

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- Important Question, Intuitive Mechanism
- Excellent Data Collection Exercise & Analysis

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- Important Question, Intuitive Mechanism
- Excellent Data Collection Exercise & Analysis
- A Paper with a bright future!

Thank You

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