

DISCUSSION OF “DOES POLITICAL PARTISANSHIP CROSS BORDERS? EVIDENCE FROM INTERNATIONAL CAPITAL FLOWS”

BY KEMPF, LUO, SCHAFFER, TSOUTSOURA

MARIASSUNTA GIANNETTI (STOCKHOLM SCHOOL OF ECONOMICS, CEPR, AND ECGI)



BACKGROUND

- International capital does not chase (enough) investment opportunities—Lucas Paradox (1990)
- Drivers of international capital flows
 - Familiarity, trust, culture....
 - Information exchange and news (Portes and Rey, JIE 2005)
 - Patriotism (Morse and Shive, JFM 2011)
 - Bilateral relationships (Gupta and Yu, 2007)
- Investors do not select assets merely based on risk and returns
 - Asset characteristics matter beyond risk and returns (e.g., Grinblatt, Mark, and Matti Keloharju, 2001; Huberman, 2001)
 - **Awareness** matters
 - Sort of **homophily** in asset selection—which goes beyond the ability to overcome information asymmetry



WHAT KIND OF HOMOPHILY MATTERS?

- Cultural similarity (Giannetti and Yafeh, 2012)
- An important component of culture is political partisanship and can be measured at the individual level
 - Kempf and Tsousoura, 2020; Dagostino, Gao, and Ma, 2021 etc.
- This paper uses political partisanship to explain I) international syndicate loan issuance II) mutual fund investment III) FDI



DRIVERS OF INTERNATIONAL INVESTMENT-AN ALTERNATIVE CANDIDATE

Bilateral relations

The EU holds regular talks on financial regulation with its key economic partners, in particular the USA, Japan, China, Canada, India, Russia and Brazil. Convergence with EU rules on financial services and capital movements is also part of membership negotiations with candidate countries.

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Bilateral relations on insurance

Bilateral dialogues on capital

Regulatory dialogues and high level meetings on financial services regulation

The European Commission and EU governments hold regular talks on financial regulation with the USA and other international partners. The goals of these talks are

- monitoring regulatory developments
- identifying potential spill-over effects of legislation in each other's jurisdictions



PARTISANSHIP AND BILATERAL RELATIONSHIP- WHAT ARE WE CAPTURING?

- To what extent is political partisanship related to countries' **bilateral relationships**?
 - Nationalistic investors withdraw in periods of deteriorating interational relationships
 - Partisanship→ It depends on the political affiliation of the investors within a country
- How does the **colour of the US administration** affect the response?
 - In most of the tests, political partisanship is measured at the US investor level
 - Distance decrease for a Republican investor; is the effect on outward investment more or less pronounced if the current administration is also Republic or Democratic?
 - **The partisanship bias would imply that Republicans are more inclined to invest in countries that become more ideologically aligned when the administration is Democratic**
- Does the effect depend on **news coverage** of the election in the US?



METHODOLOGY, QUESTION I: EMPIRICAL MODEL

$$Investment_{iect} = \alpha_{ect} + \alpha_{iec} + \beta Distance Increase_{iec} \times Post_{ect} + \epsilon_{iect},$$

- Why is the post election period only two years?
 - Temporary effect makes sense if the variable is a stock –Portfolio share in the mutual funds analysis
 - Less if we consider flows—loan issuance etc.
 - Are a few lucky clients being granted credit in the post election euphoria? Of banks always lend more to politically aligned countries?
 - Given the different specifications, currently the syndicated loan tests and the mutual fund tests tell different stories



METHODOLOGY, QUESTION II: DEFINITION OF THE TREATMENT

- How is the treatment defined
- Distance varies from zero to 6
- Distance can increase or *decrease*, but the treatment is defined as a dichotomic variable
- Explore both increase and decrease!
- Or use change in distance and explore asymmetric effect of increase and decrease
- Be clear about the control sample?
 - Decrease, stay the same and no election?
 - Make sure that you are not overstating the effects as republican and democratic investors change their place (Berg, Reisinger and Steitz, 2021)



CONCLUSION

- Political partisanship is an important component of personal identity
- ...can help us to explain how personal identity affects economic exchange and equilibrium allocations
- Comments
 - Use discontent with domestic political colour in the home country to distinguish from bilateral relationships
 - Clarify/sharpen the empirical framework

