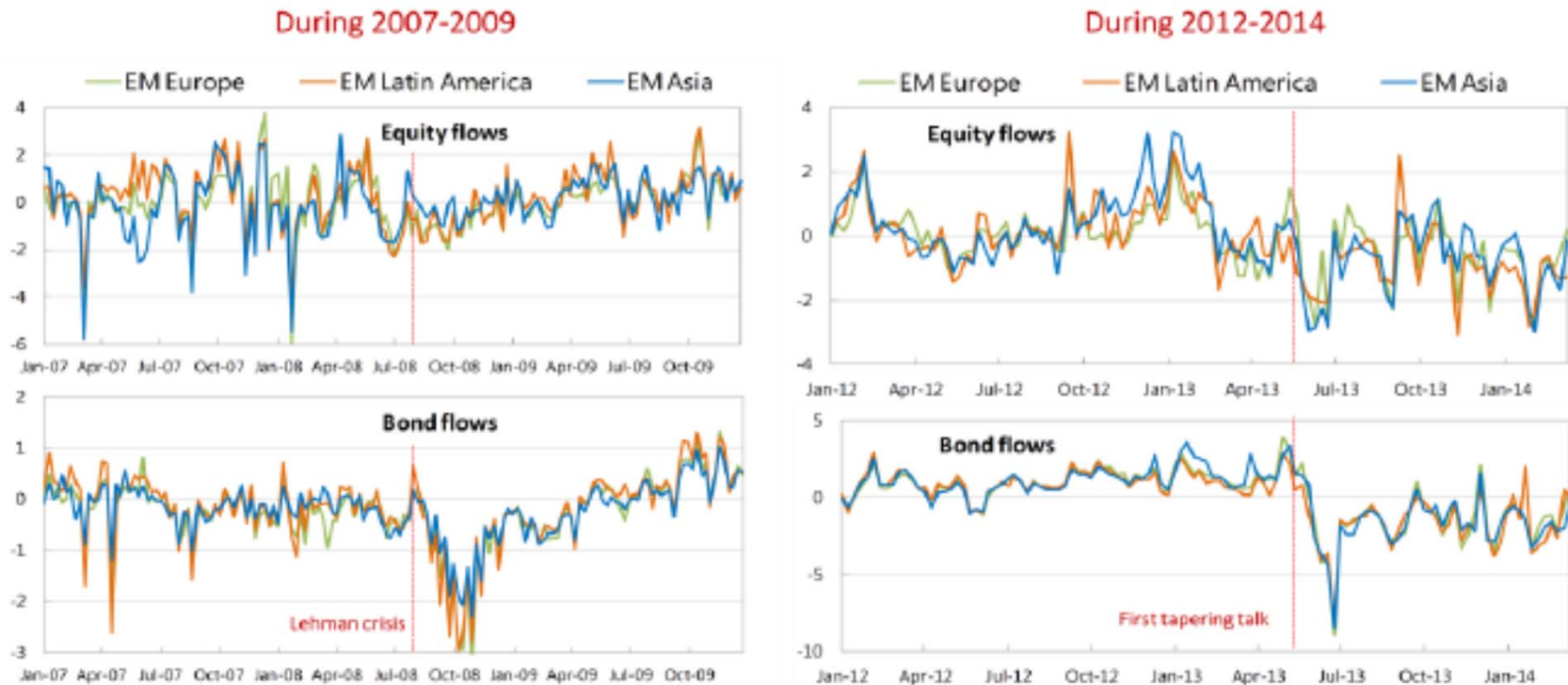


EE452 International Monetary Economics

Topic 3 Applications:
Fund flows and Volatility in Forex Market

Weekly equity and bond flows to emerging markets

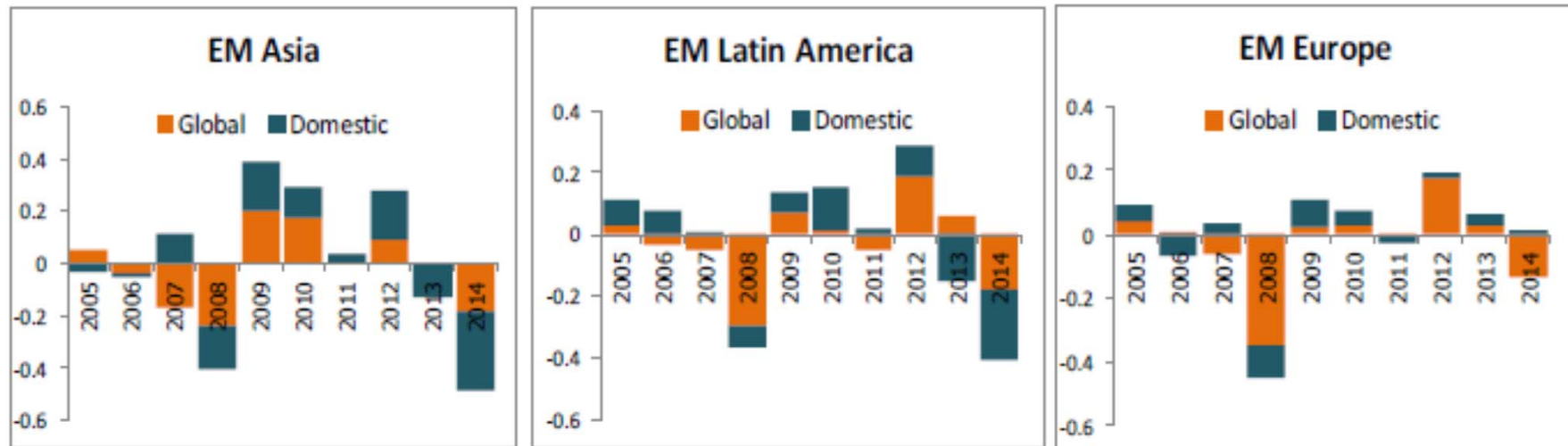


Source: EPFR Database, authors' calculation.

Note: The figure shows the standardized z-scores (subtracting the mean, then dividing by the standard deviation) of weekly equity and bond flows in different emerging market regions.

Source: Ananchotikul and Zhang (2014)

Historical decomposition of total fund flows deviation from trend (Annual average of weekly effects)



Source: EPFR Database, authors' calculation.

Note: The figure shows the historical decomposition implied by VAR results for individual countries and for each type of flows. See endnotes for more details on VAR specification.

Source: Ananchotikul and Zhang (2014)

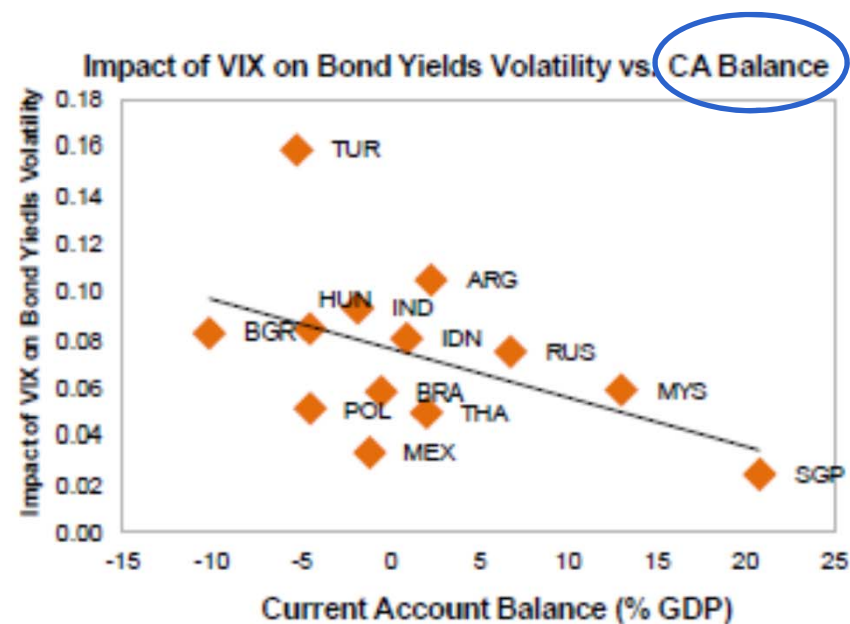
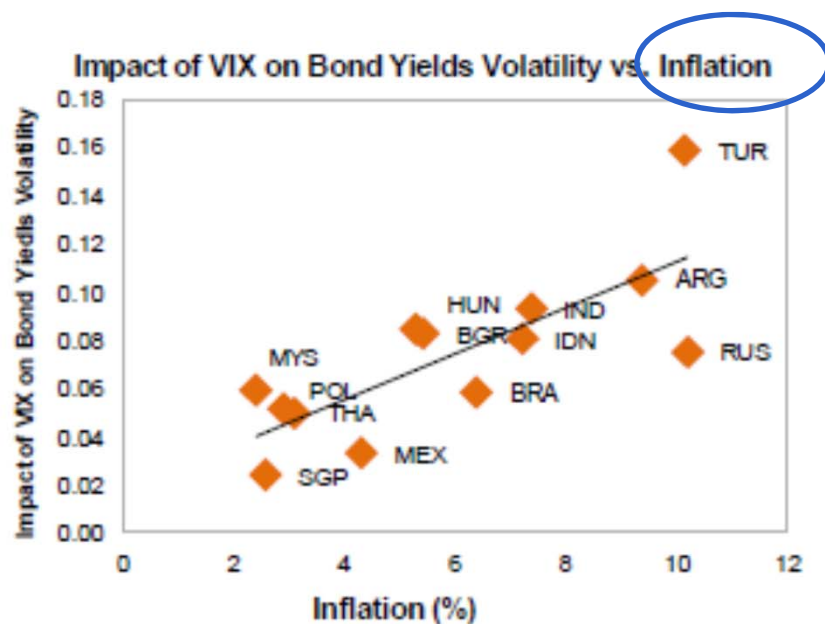
Weekly equity and bond flows to emerging markets

- Trends of weekly fund flows in emerging economies in Asia, Latin America and Europe are similar especially after the global financial crisis.
 - This implies the significant of common factors driving short-term fund flows.
 - Observation: In the short-run, global factors (particularly the Volatility Index (VIX index) and the 10-yr US treasury bond yield) are more influential than domestic factors. \

Fund Flows & Global Risk Aversion

- Ananchotikul and Zhang (2014) study the impacts of fund flows and global risk aversion of 17 countries in Asia, Latin America and Europe on the following variables:
 - Stock Exchange Index
 - Returns to Bonds
 - Exchange Rate

Global risk aversion and Bond yields



Note: The results are from DCC-MGARCH model. 10-year bond yields are used in the analysis. Inflation and current account balance on the x-axis are 2003-12 average.

Source: Ananchotikul and Zhang (2014)

Global risk aversion and Bond yields

- Global risk aversion reflects investors' sentiments. In the short-run, it is highly influential on the asset prices in the emerging economies. (see graphs in slide 6)
 - Economies with relatively low stability (eg., high inflation or high CA deficit) will be more vulnerable to global risk aversion than more stable economies.

Global risk aversion and Bond yields

- For countries with more flexible exchange rate policy, the exchange rate is more likely to be affected by the global risk aversion, but the effects on asset prices are less than in the case of fixed exchange rate system.
 - **Ie., Exchange rate is considered to be the “shock absorber” for the economy.**

Overview of Fund flows in EMs

- During 2003-2014, short-term fund flows are the consequences of VIX index, reflecting investors' global risk aversion in the world market.
 - Capital flows, particularly on portfolio investment (such as stock market or bond market), are considered high-risk investment in the perspectives of the international investors.
 - For the long-term fund flows, they are affected by domestic economic fundamentals, particularly current account balance as well as inflation level.