

Discussion of

“Searching for Yield Abroad: Risk-Taking through Foreign Investment in U.S. Bonds”

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Do investors outside the U.S. search for yield in the U.S. bonds market?

- In the aftermath of the financial crises, global monetary policy turned very expansionary to support the economic recovery.
- In advanced economies, rates of return for safe assets are at historically low levels.
- Investors can purchase riskier assets domestically and abroad, to ensure the profitability of their portfolios.
- Lower rates of return for safe assets outside the U.S. might result in search for yield in the U.S. bonds market.

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Advantages of this empirical investigation

- The authors use detailed security-level data for 33 countries for the period 2003 to 2016.
- They can study, for each country, the effects of domestic interest rates on the holdings of U.S. corporate bonds.
- External financing by U.S. bond issuers is very small, which helps estimate the search for yield in the data.

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Fig. 1: Foreign purchases of U.S. bonds during 2003–2016

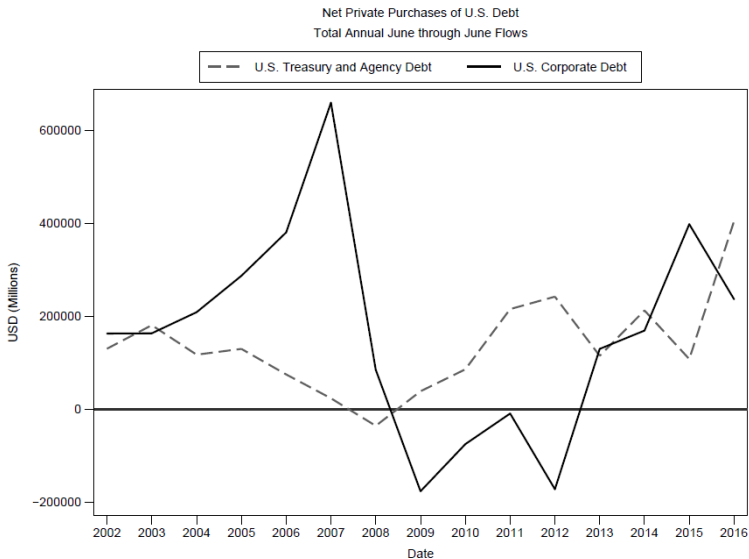


Fig. 4: Newly-issued U.S. corporate bonds held by foreign investors per rating bin, 2004 vs 2016

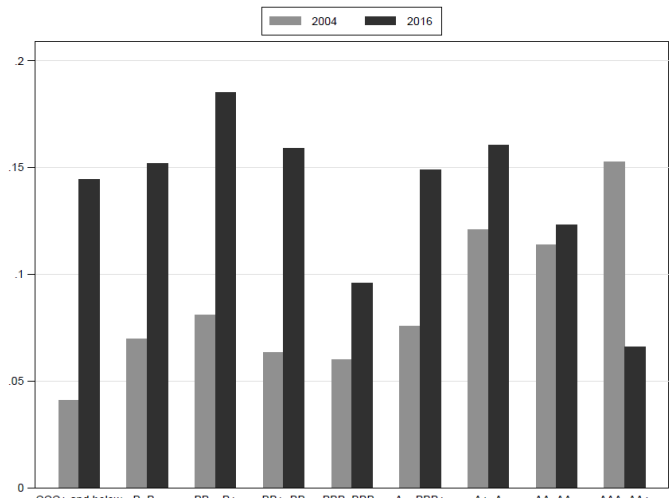


Fig. 5: Sovereign yields by country during 2003–2016

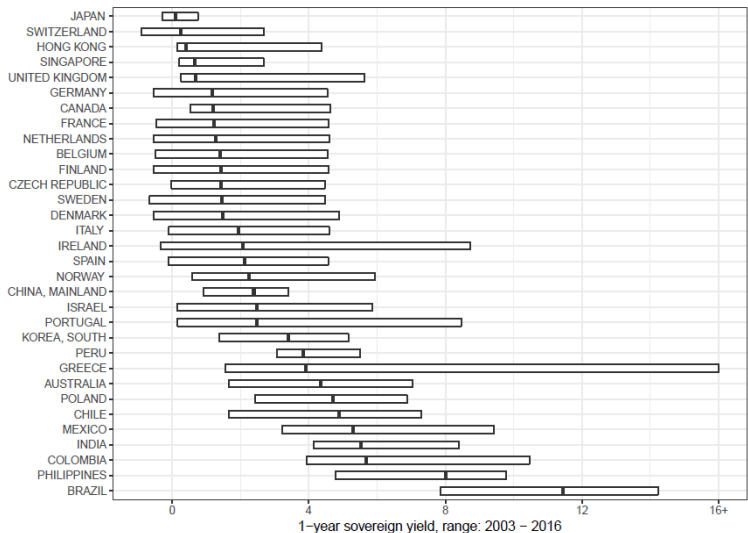
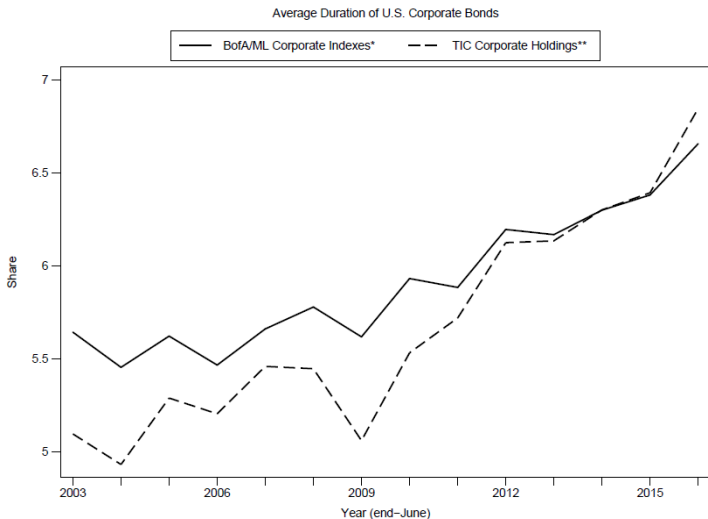


Fig. 9: Foreign portfolio of U.S. corporate bonds: average duration



* Weighted by market value of bond outstanding ** Weighted by total foreign holdings

Empirical specification used to investigate search for yield

$$\begin{aligned} \Delta H_{i,j,t}/\text{Outstanding}_{i,t} = & \beta_0 + \beta_1 \text{Risk}_{i,t} + \gamma \text{Risk}_{i,t} \Delta \text{Sov}_{j,t} + \\ & \theta_1 \Delta \text{CDS (US)}_t \text{Risk}_{i,t} + \theta_2 \text{Traded share}_{i,t} + \\ & c_{j,t} + \epsilon_{i,j,t} \end{aligned} \quad (1)$$

- $\Delta H_{i,j,t}/\text{Outstanding}_{i,t}$: change in holdings in time t by country j of bond i relative to bond i 's outstanding amount
- $\text{Sov}_{j,t}$: investor home sovereign yield
- $\text{Risk}_{i,t}$: yield-to-maturity (or split into yield spread and duration)
- CDS (US)_t : market price of U.S. corporate credit risk
- $\text{Traded share}_{i,t}$: log of the share of trading volume in TRACE in the bond's outstanding amount
- $c_{j,t}$: country*time fixed effects

Baseline results: scaled change in holdings decreasing in the interaction terms, which is suggestive of search for yield

	Bond yield		Spread and duration	
	(1)	(2)	(3)	(4)
Bond yield	0.045*** (0.003)	0.057*** (0.004)		
D.Sov × Bond yield	-0.023*** (0.003)	-0.027*** (0.003)		
D.CDS (US) × Bond yield	-0.031*** (0.002)	-0.032*** (0.002)	-0.032*** (0.002)	-0.033*** (0.002)
Traded share		0.044*** (0.007)		0.044*** (0.007)
Bond spread			0.054*** (0.003)	0.067*** (0.004)
Duration			-0.008*** (0.001)	-0.009*** (0.002)
D.Sov × Bond spread			-0.023*** (0.003)	-0.027*** (0.003)
D.Sov × Duration			-0.010*** (0.002)	-0.013*** (0.002)
Observations	304283	250459	304283	250459
R-sq	0.23	0.26	0.23	0.26
Time-Country FE	Yes	Yes	Yes	Yes

Similar results for the impact of the level of the rates

	Bond yield			Spread and duration		
	(1) Full Sample	(2) Low	(3) High	(4) Full Sample	(5) Low	(6) High
Bond yield	0.057*** (0.004)	-0.020*** (0.006)	0.130*** (0.005)			
D.Sov × Bond yield	-0.027*** (0.003)	-0.065*** (0.008)	-0.021*** (0.003)			
D.CDS (US) × Bond yield	-0.032*** (0.002)	-0.027*** (0.003)	-0.040*** (0.002)	-0.033*** (0.002)	-0.026*** (0.003)	-0.043*** (0.002)
Traded share	0.044*** (0.007)	0.040*** (0.007)	0.032*** (0.010)	0.044*** (0.007)	0.041*** (0.007)	0.027*** (0.010)
Bond spread				0.067*** (0.004)	-0.027*** (0.006)	0.151*** (0.006)
Duration				-0.009*** (0.002)	0.009*** (0.002)	-0.031*** (0.003)
D.Sov × Bond spread				-0.027*** (0.003)	-0.070*** (0.008)	-0.020*** (0.003)
D.Sov × Duration				-0.013*** (0.002)	0.006 (0.004)	-0.016*** (0.002)
Observations	250459	125078	125381	250459	125078	125381
R-sq	0.26	0.33	0.23	0.26	0.33	0.24
Time-Country FE	Yes	Yes	Yes	Yes	Yes	Yes

The results are economically significant

- Search for yield has important policy implications regarding financial stability and monetary policy.
- Nice paper, thank you!