Banking Sector Exposure to Global Financial Cycle and Sovereign Debt Crises

João Pedro Rudge Leite Jefferson Martinez Saavedra

November 18, 2024

[Draft Coming. It will be available at the link]

Abstract

We investigate how exposure to the global financial cycle influences credit cycles and sovereign default risk in emerging markets. We document that emerging markets with financial sectors more reliant on foreign funding exhibit greater sensitivity to the Global Financial Cycle, proxied by the U.S. stock market volatility index (VIX). During periods of heightened global risk premium, these economies experience reduced lending and rising CDS spreads for their governments. Our model connects these phenomena, emphasizing the macro-financial linkages between global capital flows and domestic credit dynamics in emerging economies.