

34th Australian PhD Conference in Economics and Business

Discussant remarks:
Exploring network effects during bank
failures in Argentina (E. Carlevaro)

Prasanna Gai
University of Auckland

Essence of the paper

- ❖ An empirical exploration of network contagion during the Argentine banking crisis of 2001-2.
- ❖ Spatial regression analysis suggests that direct linkages between banks mattered during the crisis.
- ❖ Implication — network structure matters for the ability of prudential measures (e.g. bank capital) to guard against bank failure.

How might the paper be improved?

- ❖ **Literature review.**

- ❖ Paper can benefit from a more careful positioning in relation to the (by now) large literature on networks and financial contagion.
- ❖ More careful attention needed on the distinction between “fundamentals” based crises and “sunspot” based crises. And also between “direct” (network links) and “indirect” (firesale) contagion.
- ❖ *My prior:* This paper is about a fundamentals-based crisis, with indirect contagion playing a major / main role.

❖ **The 2001-2 Argentina crisis.**

- ❖ In a paper like this, it is important to document the crisis itself. Provide a narrative that describes how the contagion dynamics unfold and the mechanisms involved. And then relate your model / results back to it.
- ❖ A classic case of a “twin” (e-rate and banking) crisis, e.g. Goldstein (EJ, 2005). Expected to see this interplay more explicitly in the formal modelling. In particular, indirect contagion should be much more virulent / important than in amplifying the crisis. Some of the results hint as much.
- ❖ Tell us more about the (nice) database / properties of the network that you constructed!
- ❖ And tell us about the balance sheet of the typical Argentine bank.

❖ Exogenous network.

- ❖ A restrictive feature of the analysis. Links between banks will be formed endogenously — reflecting strategic preferential attachment behaviour of nodes, and responses to government policy on the exchange rate and LOLR.
- ❖ Again — tell us about the network (e.g. centrality of nodes) etc. The degree distribution is key (Table 1). Relate findings back to results like Gai & Kapadia (Proc. Royal Soc. 2011) and Acemoglu (AER, 2015) on “*robust-yet-fragile*” banking systems.
- ❖ Can track the network over time with partial data and maximum entropy techniques.

- ❖ **Policy discussion.**

- ❖ What does the analysis imply for micro / macro prudential policy design?
- ❖ Would stronger capital buffers have helped Argentina? How high might they have had to be?
- ❖ If network structure is problematic, how might it be “rewired” to promote system stability?

Summing up

- ❖ I enjoyed reading the paper. Once tidied up, it will be a useful contribution to the literature on financial networks and our understanding of crises.