Discussion of:

The Core, the Periphery, and the Disaster: Corporate-Sovereign Nexus in COVID-19 Times

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WFA
Macro Shocks

"Doom loops" in the eurozone

- **Banks-sovereign** nexus
  - $\rightarrow$ Banks rely on government guarantees
  - $\leftarrow$ Banks hold a large portfolio of domestic sovereign bonds
- Emerged in the eurozone in 2010-12
  - e.g., Italy in Fall 2011 (and Greece and Ireland before)
  - (Temporarily?) broken in July 2012 (OMT speech)

"Doom loops" in the eurozone

- **Corporates-sovereign** nexus
  - $\rightarrow$ Firms rely on government guarantees
  - $\leftarrow$ Sovereigns tax firms

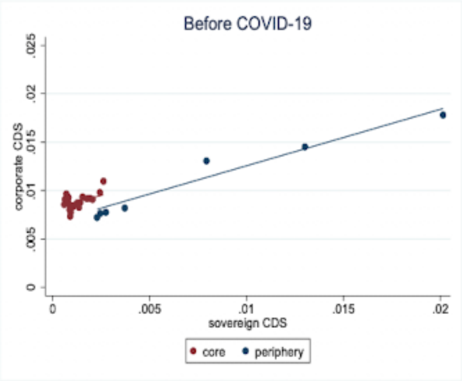
- These feedback loops are a symptom of "fragmentation"
  - We need to understand them and maybe (?) limit them
  - See current debate about an anti-fragmentation tool by the ECB

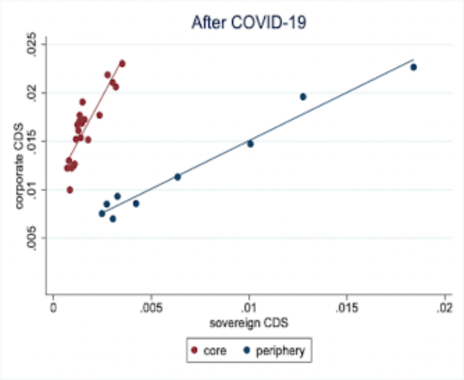
This paper

Corporates-sovereign nexus in the eurozone during COVID-19

1) Always been there in peripheral countries (increased a bit)
2) Emergence of a nexus in core eurozone countries

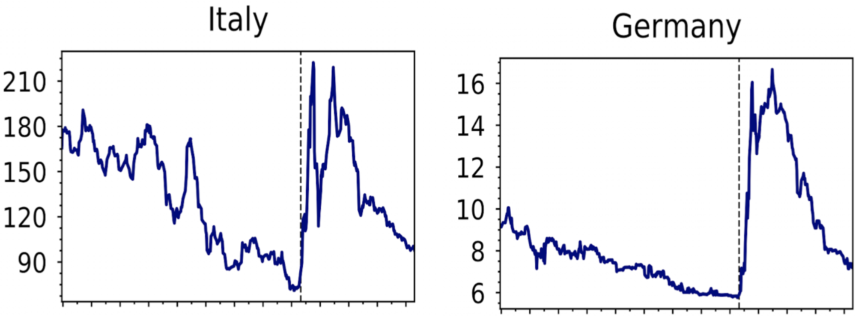
Sovereign and corporate CDS – pre vs. post COVID-19





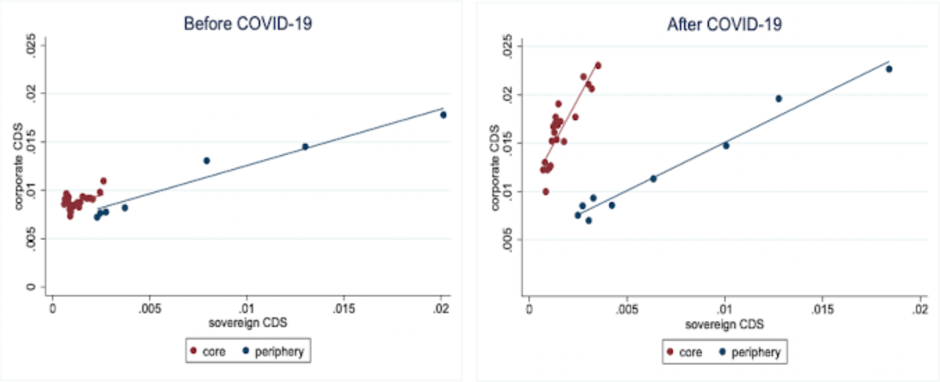
- Clarify binned scatterplot: “Observations are grouped into equal-width bins”
- Periphery: slope doubles (!); Core: significant steepening
- Limited increase in sovereign credit risk in core

Sovereign credit risk in core vs. periphery



- Limited increase in sov. credit risk in the core (even by historical standards in DE)
- At odds with the existence of a *nexus* in core countries after the large shock to firms

Sovereign and corporate CDS – pre vs. post COVID-19



- The paper is more about *fiscal capacity* and corporate CDS (one leg of the nexus)
- Would like to see this scatter plot with fiscal capacity on the x-axis

Identification challenge

- “Firms with high CDS tend to operate in countries with high CDS”
  - Pre-COVID: True only in periphery
  - Post-COVID: True in periphery and core

⇒ emergence of a corporate-sovereign nexus in the core

- “Students underperforming in PISA tests tend to live in countries with high CDS”
  - Pre-COVID: True only in periphery
  - Post-COVID: True in periphery and core

- Challenge: COVID-19 hits *all* firms (and students)
  - Pre-COVID: all firms (and students) were doing pretty well in the core
  - Post-COVID: not any more (school closures, etc)

Actual fiscal support

Country	ΔDebt/GDP
BEL	20.99
DEU	11.16
ESP	29.80
FIN	11.52
FRA	22.24
GRC	36.05
ITA	29.41
NLD	7.46
PRT	21.59

OECD data

- Large fiscal support in peripheral countries (IT, GR, SP)
  - Great data in Kirti, Liu, Martinez Peria, Mishra, Strasky (2022) *"Tracking Economic and Financial Policies During COVID-19: An Announcement-Level Database."*
- To what extent has the ECB support relaxed budget constraints in the periphery?

Other comments

- Firms in periphery are overwhelmingly in telecomm and energy
  - Representative sample? “Strategic” sectors?
- Two-speed periphery in sovereign CDS? IT GR Vs PT SP?
  - Is it again about fiscal capacity?

Overall

- Ambitious and topical paper
- Main comment: Two-way nexus or effect of fiscal capacity on firms' credit risk?
- Possible extensions: role of ECB, explore actual fiscal support, two-speed periphery