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Abstract

We analyze whether the global financial cycle (GFC) affects local credit supply and the real effects, and whether local unconventional policies can attenuate such spillovers. For identification, we exploit GFC shocks, differential bank reliance on global funding, local central bank interventions in FX derivatives, and three matched administrative registers in Brazil: the register of foreign credit flows to domestic banks, the credit register, and the matched employer-employee register. We show that after the announcement of US Quantitative Easing tapering by Bernanke in May 2013, which is associated with massive FX depreciation and increased volatility, domestic banks with larger foreign liabilities reduce the supply of credit to firms, in turn reducing employment. However, these negative effects are attenuated after the Central Bank of Brazil announces a large intervention in the FX derivatives market, which consists in supplying insurance against FX risks – hedger of last resort. In addition to these two subsequent shocks, we also analyze a panel over 2008-2015. Banks with larger foreign liabilities cut credit supply after US Dollar appreciation or after an increase of FX volatility (even for US FX changes with EMs excluding Brazil). Moreover, the FX effects on credit supply and real effects are mitigated after the FX intervention of the central bank, thereby confirming that the policy of hedger of last resort has been effective in decreasing local economy spillovers to global financial conditions. Our results have important implications for international macro-finance models and policy.

JEL Classification: E5, F3, G01, G21, G28

Keywords: foreign exchange, monetary policy, central bank, Bank credit, Hedging

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