

> Thursday, January 28th, 2021

12:30 - 14:00

FINANCE RESEARCH SEMINAR

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EMPOWERING CHANGEMAKERS FOR A BETTER SOCIETY

“TESTING FOR THE VALIDITY OF W IN GVAR MODELS”

A joint work with Angelo Luisi

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ABSTRACT

Global VARs are one of the most established econometric frameworks to analyse cross-country/markets interconnections. Nevertheless, they are based on pre-specified channels of interdependence (proxied by the matrix of distance W) that are never empirically tested. This paper develops a simple Likelihood Ratio Test for the validity of the proposed channels, assesses its asymptotic size and power, and proposes a bootstrapped alternative to avoid finite sample distortions. In the empirical application regarding euro area sovereign bond yields modelling, the most popular channels get rejected. The nonrejected W outlines the importance of contagion and flight-to-quality mechanisms even before the sovereign debt crisis.

Keywords: Global VAR, Structural VAR, Likelihood Ratio Test, Interdependence