

Moral Hazard and Financial Crisis

Evidence from US Troop Deployments

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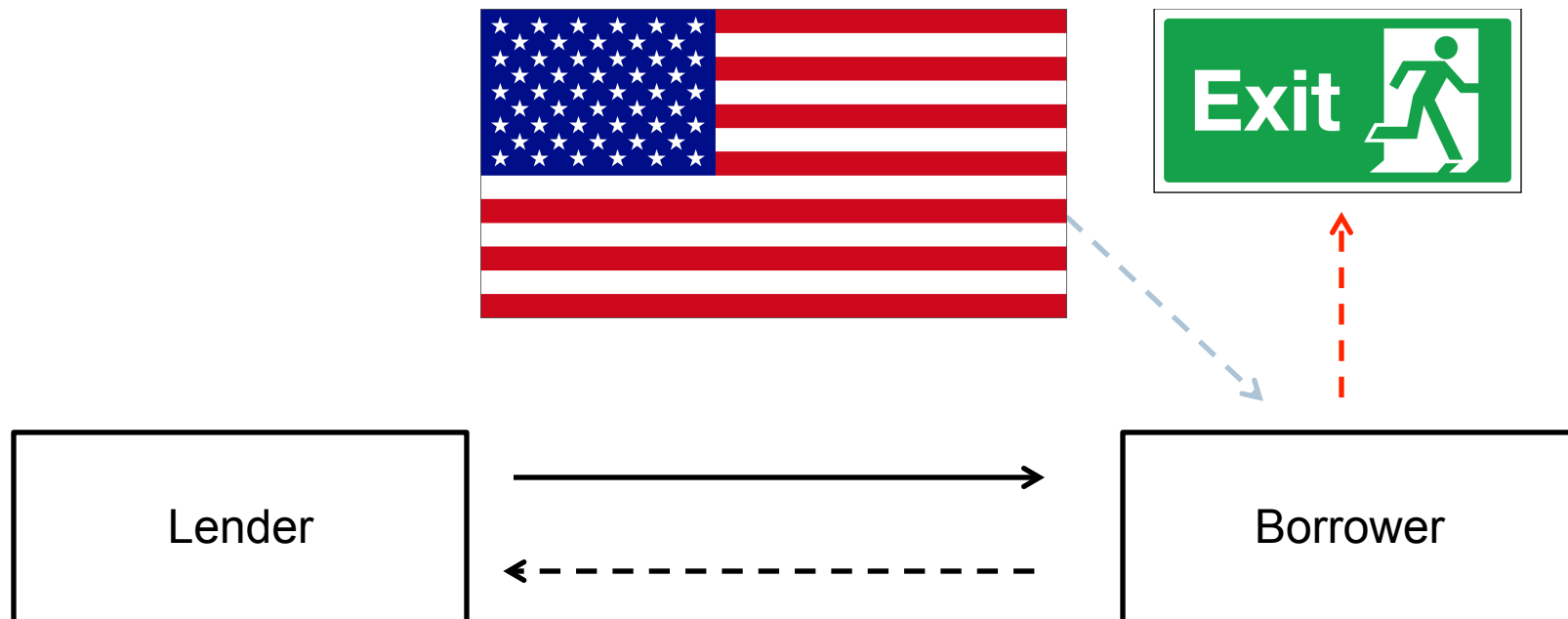
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- ▶ Sources of financial crisis
- ▶ Role of international moral hazard
- ▶ Little empirical evidence so far

Theory



- ▶ **Theoretical Mechanism**
 - ▶ U.S. troops → Riskier policies → Financial instability
- ▶ **Effect of U.S. troops on**
 - ▶ financial regulation (deposit insurance, capital openness)
 - ▶ macroeconomic policies (interest rates, FX)
 - ▶ financial crises (R&R)

Empirical Approach

Dependent Variable	Definition
Financial Crisis (R&R)	coded as 0,1
Independent Variable(s)	
U.S. Troop Deployments	$\log(\text{U.S. Troops}), (t-1)$
Control Variable(s)	
Macroeconomic Controls	GDP per capita, GDP growth, Service Sector
Political Controls	Democracy
Policy Similarity	UN voting, UN security council membership
Fixed Effects	Country, Time

Results

	All	All	Non-OECD
U.S. Troops, log (t-1)	0.03** (0.00)	0.05** (0.02)	0.07** (0.02)
Control Variables		√	√
Country FE	√	√	√
Time FE	√	√	√
Observations	2904	1655	933

1% increase in U.S. troops → 3-7% increase in probability of financial crisis

Results

	I-Rate	FX	Deposit	Cap. Open.
U.S. Troops, log (<i>t-1</i>)	-0.82** (0.34)	7.22** (3.22)	0.04** (0.02)	0.03 (0.02)
Control Variables	√	√	√	√
Country FE	√	√	√	√
Time FE	√	√	√	√
Observations	2527	1929	1711	3328

Conclusion

- ▶ Moral hazard poses a significant policy challenge.
- ▶ US troops are a proxy for moral hazard.
- ▶ Reforms of IFIs and bailout lending might be ineffective.

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Thank You 

Robustness Checks

- ▶ **Simultaneity Bias/Reverse Causality**
 - ▶ Pre- and post financial crisis comparisons show a decrease in U.S. troops.
 - ▶ Removing all countries in a civil or international conflict.
 - ▶ Causal channels are inconsistent with reverse causality.
- ▶ **Policy Similarity**
 - ▶ Including variables capturing political similarity do not affect our results.
- ▶ **Case Selection**
 - ▶ Results hold when considering different time frames and regions.
- ▶ **Measurement**
 - ▶ Results are robust to different specifications of the dependent and independent variable(s).