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Cover; Contents; I. Introduction; II. Theory; A. How does financial regulation affect the response of the current account to output shocks?; III. Empirical methodology and data; A. General methodology; B. Identification of net output shocks; Tables; 1. Sign restrictions; C. Estimation and inference; D. Data; IV. Empirical results; 2. Country sample; A. Robustness; V. Conclusion; References; Appendix; A. Appendix; A.1. Deriving the linearized budget constraint; A.2. Derivation of the current account reaction function with external habits and a constant world real interest rate
A.3. Derivation of the current account reaction function with internal habits and a constant world real interest rate A.4. Derivation of the current account reaction function under a stochastic time-varying world real interest rate and no habitual consumption; Figures; 1. Size of current account imbalances; 2. Financial deregulation index; 3. Current account persistence; 4. Impulse response functions to log level net output shock - financial regulation; 5. Impulse response functions to log difference net output shock - financial regulation
6. Impulse response functions to log level net output shock - capital account openness 7. Impulse response functions to log difference net output shock - capital account openness; 8. Impulse response functions to log level output shock - financial regulation controlling for fx regime; 9. Impulse response functions to log difference output shock - financial regulation controlling for fx regime; 10. Impulse response functions to log level output shock - capital account openness controlling for fx regime
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Sommario/riassunto

This paper examines the relationship between financial regulation and the current account in an intertemporal model of the current account where financial regulation affects the current account through liquidity constraints. Greater liquidity constraints decrease the size and persistence of the current account response to a net output shock. The theory is tested with an interacted panel VAR model where the coefficients are allowed to vary with the degree of financial regulation. The current account reaction to an output shock is 60% larger and substantially more persistent in a country with low financial regulation than in one with high financial regulation.