Exports and FDI in the presence of downside risk [#]

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Abstract

This study analyzes the impact of downside risk on the flows of exports, affiliate sales, and their joint pattern. The risk, in this study, relates to shocks to country demand in the destination market. The downside risk is measured by the skewness of demand shocks. Using a panel of industry-level data on trade and affiliate sales for a large number of home and destination countries, I find that volatility and skewness of demand shocks affect the flows of exports and affiliate sales, and their joint pattern. By focusing on downside risk, I expose several novel results regarding the effects of uncertainty on the proximity-concentration tradeoff. The results show that more exports, relative to affiliate sales, will flow to the destination market with less downside risk. In addition, I study the interaction between variance and skewness as a measure of risk asymmetry and show that this measure affects the flows of exports, foreign direct investment, and the joint pattern of exports and affiliate sales.

Keywords: Downside Risk, Proximity-Concentration Trade-off, Risk Asymmetry, Foreign Direct Investment, International trade

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