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‘Large’ vs. ‘Small’ Players: A Closer Look at the Dynamics of Speculative Attacks

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Abstract

What is the role of “large players” like hedge funds and other highly leveraged institutions in speculative attacks? In recent theoretical work, large players may induce an attack by an early move, providing information to smaller agents. In contrast, many observers argue that large players are in the rear. We propose a model that allows both the large player to move early in order to induce speculation by small players, or wait so as to benefit from a high interest rate prior to the attack. Using data on net positions of “large” (foreigners) and “small” (locals) players, we find that large players moved last in three attacks on the Norwegian krone (nok) during the 1990s: The ERM-crisis of 1992, the NOK-pressure in 1997, and after the Russian moratorium in 1998. In 1998 there was a contemporaneous attack on the Swedish krona (sek) in which large players moved early. Interest rates did not increase in Sweden so there was little to gain by a delayed attack.

JEL Code: F31, F41, G15.

Keywords: speculative attacks, microstructure, international finance, large players.

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1 Introduction

The problem of connecting currency crises to fundamentals has led to a discussion of possible manipulation of exchange rates. In the public debate concerning currency crises many, e.g. politicians, have denounced hedge funds and other highly leveraged institutions, especially foreign, for manipulating exchange rates during speculative pressure. In contrast, many market observers have argued that both fundamentals and large players may play a role.

The different views are reflected in the development of the theory on currency crises. In the first generation model of Krugman (1979), the collapse of the exchange rate is inevitable due to deteriorating fundamentals. The second generation models, e.g. Obstfeld (1986), show that there may be a multiplicity of equilibria, leading to the possibility of self-fulfilling expectations of attack. If the market believes that an attack will be successful, everyone attacks, making it too costly for the central bank to defend the currency even with strong fundamentals. Hence, the initial belief is confirmed in the attack. The second generation models cannot, however, explain the timing of the attack. Morris and Shin (1998) show that the multiplicity of equilibria is due to common knowledge of the fundamentals, and that only adding a small amount of noise to the players' signal on fundamentals results in a unique equilibrium where the timing of the attack can be determined.¹

Corsetti, Dasgupta, Morris, and Shin (2004) extend the model of Morris and Shin by introducing a single large player that might have superior information. By moving early the large player can signal his information to the small players, thereby inducing an attack. However, based on experiences from the ERM and Asia-crises, Tabellini (1994) and the IMF (1998) argue that large players move in the rear in currency crises because they want to benefit from positive interest rate differentials. We extend the Corsetti et al. model by incorporating this benefit from a late attack in the analysis, making the large player's entry decision depend on the size of the various gains and costs. An early attack will provide a signal to the small players, just as in the Corsetti et al. model, but at the cost of moving to a currency with lower interest rate. By waiting to the last stages of the attack, the large player may profit from the higher interest rates. The latter alternative is best if the attack is sufficiently likely so that an early signal is viewed as unnecessary.

To explore the model empirically, we consider three cases of speculative pressure on the Norwegian krone (NOK), and one case for the Swedish krona (SEK). The Norwegian cases are: (i) The attack during the ERM-crisis in December 1992; (ii) the attack in January 1997; and (iii) the attack after the Russian moratorium in August 1998. The third crisis is also our Swedish case. In 1992 Norway had a fixed exchange rate, while

¹The Morris and Shin (1998) result have spurred a number of contributions where the aggregate information is endogenized, and where multiplicity may arise, see Angeletos, Hellwig, and Pavan (2006, 2007), Angeletos and Werning (2006) and Hellwig, Mukherji, and Tsyvinski (2006).

the exchange rate was a managed float in 1997 and 1998. Sweden had officially a floating exchange rate regime in 1998, but had intervened on several occasions since the ERM-crisis in 1992–93. In these situations, speculators may take currency positions in the belief that monetary authorities will change the monetary regime, or at least allow for a considerable change in the exchange rate, in the near future.²

For Norway we have weekly data on spot and forward currency trading by Norwegian banks with Norwegian customers and foreigners. Anecdotal evidence from the Norwegian market suggests that the foreign investors are leveraged institutions, or “large players”, while locals can be viewed as “small players”. This seems particularly reasonable for periods of speculative pressure where foreigners can raise more funds than locals. In Sweden several banks, assigned as “primary dealers”, report to the Sveriges Riksbank their buying and selling of spot and forward against locals and foreigners. Conversations with central bank officials indicate that these two data sets may cover as much as 80-90% of all trading in NOK and SEK.

Our results suggest that the behavior of large and small players differs before and during speculative attacks. In line with the observations of Tabellini and the IMF, we find that large players moved last during the three attacks on the Norwegian krone (NOK). Regression analysis also indicates that the trading of large players is most important for triggering the actual attack. This is consistent with our theoretical model, which predicts that if the probability of a successful attack is high, large players will choose to move late if there is some gain from waiting, e.g., a high interest rate differential. However, during the attack on the Swedish krona (SEK) in 1998, it was the large players that moved early. This is consistent with our model as in this case interest rate differentials did not increase during the attack, so there was little to gain for the large players by a delayed attack.

To our knowledge only few papers empirically address the role of large players. Wei and Kim (1997) study the importance of large players using the Treasury Bulletin reports. They find that trading by large players adds to the volatility of exchange rates, and argue that hedge funds act like “noise traders” in the Korean market. ? use the same data, and compile more informal information about a number of speculative events. They find support for the role of large players and some indications of the presence of asymmetric information. Cai, Cheung, Lee, and Melvin (2001) also use the Treasury Bulletin data and find that the trading of large players contributes to volatility during the unwinding of the yen-carry trade in 1998.

Unlike the studies above, we have information on net positions of *both* large and small players in the periods around a speculative attack. Further, the source of our data covers almost the total market for the currencies under investigation. With long time series on trading we can also analyze several distinct relevant episodes. Finally,

²See e.g. Calvo and Reinhart (2002) who argue that even if a country officially adopts a “flexible” exchange rate, they often tend to limit the fluctuations of the exchange rate.

while the former studies have focused on the Asian markets we focus on two European economies. This adds a new dimension to the empirical findings in this field.

In section 2 we present the model and discuss some empirical implications. Section 3 contains a description of our data and the institutional framework of the exchange rate regime. Section 4 describes the empirical methodology and our results. Section 5 concludes.

2 The Model

Corsetti, Dasgupta, Morris and Shin (2004) (henceforth CDMS) analyze a model with a large player and a continuum of small players.³ In their analysis of sequential trading CDMS consider the alternative where the large player speculates first, so as to create a signal affecting the behavior of the small agents. As mentioned by CDMS, the IMF, and Tabellini, however, there is empirical evidence indicating that large players are in the rear, rather than at the front, in speculative attacks. Here we extend the theoretical framework of CDMS by allowing for a richer timing structure, where the large player may gain from an early or a late speculation.⁴

We want to capture the following concerns: A player may want to start speculation at a early stage, in the hope of providing a signal to other players, and thus induce other players to join the attack and thereby increase the probability of success. Such early speculation involves trading costs, and possibly also a negative interest rate differential since one is leaving the high interest rate currency. Alternatively, the player may wait to a late stage in joining the attack, when there is more information as to whether the attack succeeds. Late speculation involves lower costs due to a shorter time with a negative interest rate differential. However, late speculation also involves the risk of being too late, either that the speculative attack fails and it is no longer possible to join and support it, or that the devaluation takes place before the late speculation, removing the possibility to profit. Furthermore, late speculation requires that one follows the market closely, and has the ability to trade rapidly.

To explore these concerns, we follow CDMS and consider an economy where the central bank aims at keeping the exchange rate within a certain interval, either a well defined, publicly known, narrow target zone, or a less explicit dirty float policy. There is a single large player, and a continuum of small players indexed to $[0, 1]$. The players may attack the currency by short selling the currency, i.e. borrow domestic currency and sell it for dollars. The small players taken together have a combined limit to short selling the domestic currency normalized to 1, while the large player has access to

³We use “player[s]” in the rest of the paper, instead of, e.g., trader[s].

⁴Two related papers are Bannier (2005) and Guimarães and Morris (2007). Bannier shows that, by adding a public signal in a model otherwise close to CDMS, large players are more important when public signals are weak. Guimarães and Morris show that the larger funds the players in general can raise the more likely is a successful attack.

credit allowing him to take a short position up to the limit $L > 0$.

In contrast to CDMS, we assume that trade may take place in three periods. In period 1 and 2, there is a cost $t \in (0, 1)$ per unit of short selling, reflecting trading costs and possible interest rate differential.⁵ The costs are normalized so that the payoff to a successful attack on the currency, leading to a devaluation/depreciation of the currency, is given by 1, and the payoff from refraining from attack is 0. Thus, the net payoff for small players of a successful attack on the currency is $1 - t$, while the payoff to an unsuccessful attack is $-t$.

Finally, players also have the possibility to wait by speculating until the attack takes place, which we refer to as period 3. The benefit from waiting until this late stage is that one saves the loss of the interest rate differential that is incurred by a longer speculation period. For notational simplicity, without affecting the qualitative results, we thus set the unit trading costs in period 3 to zero. However, waiting till the last stage also involves disadvantages. First, if the attack is failing, it is too late to join and support the attack, as other players are then reverting their speculative positions. Second, if the attack succeeds, there is a probability $q > 0$ that one is too late, after the exchange rate has fallen, and thus is not able to benefit from the attack. Finally, having the option of late speculation involves a fixed cost $z > 0$, independent of the size of the speculation, reflecting costs associated with information and trading ability.

Following CDMS, we let the strength of the economic fundamentals of the exchange rate regime be indexed by a random variable θ .⁶ This can be interpreted as a reduced form of the central bank reaction function, indicating how much reserves the bank is willing to use in the defense. If the fundamentals support the current regime, i.e. are strong, the central bank is willing to use more reserves in the defense. The strength of the speculative attack is measured by the amount used by the players attacking the currency. Whether the current exchange rate regime is viable depends on the strength of the economic fundamentals relative to the strength of the speculative attack.

Given the fixed costs involved to be able to speculate in period 3, the small players are too small to profit, thus they will choose to do their speculation in the periods before. However, for the large player, the savings on trading costs and interest rate differential are sufficient to cover the fixed information costs, thus the large player may want to trade in period 3. For simplicity, we assume that the large player will incur these fixed costs for his other business activities, so we do not incorporate these costs in the further analysis.

Note that the assumption that speculation in period 3 cannot affect whether the attack succeeds, involves a vast simplification of the analysis. With this assumption,

⁵Ideally, one would want to endogenize the interest rate during the attack, along the lines of Hellwig et al. (2006) and Tarashev (2007). However, in these papers there is no role for the large player, and combining these two elements is a challenging task, that is beyond the scope of the present paper.

⁶The fundamental's (improper) prior distribution is uniform over the real line.

there is no need for other players to make forecasts about the large player's behavior in period 3. However, the assumption also involves a clear element of realism; if an attack is seen not succeed, many players may revert their positions, and the attack will fail even if the large player increases his speculation.⁷

As noted by CDMS, there is no gain for small players from speculating in period 1, as this involves less information, and each of them is too small to affect the behavior of the others. On the other hand, for the large player, speculation in period 1 is better than speculation in period 2, as speculation in period 1 encourages speculation by the small players. For the large player there is nothing to learn from waiting till period 2, as the small players will not speculate in period 1.

Under these assumptions, whether a speculative attack is successful depends on the speculation in periods 1 and 2, relative to the strength of the economic fundamentals. Let ξ denote the mass of small players that speculate, and λ denote the speculation of the large player in period 1.

Then the exchange rate will fall if and only if

$$\xi + \lambda \geq \theta. \tag{1}$$

If $\theta < 0$ the exchange rate will depreciate irrespective of whether a speculative attack takes place. We therefore restrict attention to the case where $\theta > 0$.

2.1 Information

The small players observe a private signal that yields information about the fundamentals as well as the amount of speculation of the larger player. A typical small player i observes

$$x_i = \theta - \lambda + \sigma \varepsilon_i, \tag{2}$$

where $\sigma > 0$ is a scaling-constant to the variance of the signal x . The individual specific noise ε_i is distributed according to a smooth symmetric and single-peaked density $f(\cdot)$ with mean zero, and $F(\cdot)$ as the associated c.d.f. The noise ε_i is assumed to be i.i.d. across players. Note that the small players cannot distinguish the information they obtain about the fundamentals from the information about the speculation of the larger player; they only observe a noisy signal of the difference between the two. This assumption simplifies the analysis considerably. It also captures an element of realism: while rumors may give small players a strong indication whether large players trade, there is no disclosure requirements in FX markets so the small players cannot know the extent of large players' trade. Furthermore, a large player may

⁷Note that the assumption that many small players may revert their position if the attack fails, is not inconsistent with our assumption that they will not incur the fixed costs of continuous monitoring to be able to speculate in period 3. Even if none of the small players follow the market continuously, at each point in time there will always be some of the small players who follow the market at that time, and these players may revert if the attack does not succeed.

have an incentive to encourage the belief that he trades, to induce speculation by other, suggesting that small players should be careful when interpreting such loose information. Here we take this position to the extreme, by assuming that small players cannot distinguish trade by the large player from other information.

The larger player observes

$$y = \theta + \tau\eta, \quad (3)$$

where $\tau > 0$ is a scaling-constant to the variance of the signal, and the random term η is distributed according to a smooth symmetric and single-peaked density $g(\cdot)$ with mean zero. To obtain explicit solutions, we assume further that $g(\cdot)$ is strictly increasing for all negative arguments, and strictly decreasing for all positive arguments. $G(\cdot)$ is the associated c.d.f. We assume that noise in the information is sufficiently large that for the large player, the probability that an attack will be successful is always strictly positive.

2.2 Analysis

As usual in such models, we solve by use of backwards induction. Whether the attack is successful is determined in period 2, thus we may start by considering the action of the small players in this period, given the prior decision of the large player in period 1. Then we consider the decision of the large player whether to initiate an early attack. An eventual late attack by the large player will be the residual of his credit L after any early speculation.

Following CDMS, we will assume that the small players follow trigger strategies in which players attack the currency if the signal falls below a critical value x^* .⁸ As in the analysis of CDMS, there is a unique equilibrium which can be characterized by two critical values $(\theta - \lambda)^*$ and x^* , where the former captures that the currency will always collapse if the fundamental θ , less the early speculation of the large player λ , is below the critical value, while the latter is the critical value in the trigger strategy of the small players.

These critical values can be derived in the same way as in the analysis of the benchmark case in section 2.2.1 of CDMS. First we consider the equilibrium given the trigger strategies, then we consider the optimal trigger strategies. Given the trigger strategy, a small player i will attack the currency if his signal $x_i \leq x^*$. The probability that this occurs is a function of the true state of the economy, $\theta - \lambda$, as follows

$$\begin{aligned} \text{prob}[x_i \leq x^* | \theta - \lambda] &= \text{prob}[\theta - \lambda + \sigma\varepsilon_i \leq x^*] \\ &= \text{prob}\left[\varepsilon_i \leq \frac{x^* - (\theta - \lambda)}{\sigma}\right] = F\left(\frac{x^* - (\theta - \lambda)}{\sigma}\right). \end{aligned}$$

⁸CDMS show that there are no other equilibria in more complex strategies.

Since there is a continuum of small players, and their noise terms are independent, there is no aggregate uncertainty as to the behavior of the small agents. Thus, the mass of small players attacking, ξ , is equal to this probability. As $F(\cdot)$ is strictly increasing, it is apparent that the incidence of the speculative attack is greater, the weaker the strength of the economic fundamentals, less the early speculation of the large player $(\theta - \lambda)$.

A speculative attack will be successful if the mass of small players that speculate exceeds the strength of the economic fundamentals, less the early speculation of the large player, i.e. if

$$F\left(\frac{x^* - (\theta - \lambda)}{\sigma}\right) \geq \theta - \lambda.$$

Thus, the critical value $(\theta - \lambda)^*$, for which the mass of small players who attack is just sufficient to cause a devaluation, is given by the equality

$$F\left(\frac{x^* - (\theta - \lambda)^*}{\sigma}\right) = (\theta - \lambda)^*. \quad (4)$$

For lower values, where $\theta - \lambda \leq (\theta - \lambda)^*$, the incidence of speculation (the left hand side of (4)) is larger, and the strength of the fixed exchange rate (the right hand side of (4)) lower, implying that an attack will be successful. Correspondingly, for higher values, where $\theta - \lambda > (\theta - \lambda)^*$, the incidence of speculation is lower, and the strength of the fixed exchange rate larger, implying that an attack will not succeed.

Let us then derive the optimal trigger strategies of the small players. A player observes a signal x_i , and, given this signal, the success-probability of an attack is given by

$$\begin{aligned} \text{prob} [\theta - \lambda \leq (\theta - \lambda)^* | x_i] &= \text{prob} [x_i - \sigma \varepsilon_i \leq (\theta - \lambda)^*] \\ &= \text{prob} \left[\varepsilon_i \geq \frac{x_i - (\theta - \lambda)^*}{\sigma} \right] = 1 - F\left(\frac{x_i - (\theta - \lambda)^*}{\sigma}\right) = F\left(\frac{(\theta - \lambda)^* - x_i}{\sigma}\right), \end{aligned}$$

where the last equality follow from the symmetry of $f(\cdot)$, $F(v) = 1 - F(-v)$. The expected payoff of attacking the currency for player i , per unit of speculation, is thus

$$\begin{aligned} (1 - t)F\left(\frac{(\theta - \lambda)^* - x_i}{\sigma}\right) - t\left(1 - F\left(\frac{(\theta - \lambda)^* - x_i}{\sigma}\right)\right) \\ = F\left(\frac{(\theta - \lambda)^* - x_i}{\sigma}\right) - t. \end{aligned}$$

In an optimal trigger strategy, the expected payoff of attacking the currency must be zero for the marginal player, i.e. the optimal cutoff x^* in the trigger strategy is given by

$$F\left(\frac{(\theta - \lambda)^* - x^*}{\sigma}\right) = t. \quad (5)$$

To solve for the equilibrium, we rearrange (5) to obtain $(\theta - \lambda)^* = x^* + \sigma F^{-1}(t)$. Substituting into (4), we get

$$(\theta - \lambda)^* = F\left(\frac{x^* - (x^* + \sigma F^{-1}(t))}{\sigma}\right), \text{ or}$$

$$\begin{aligned} (\theta - \lambda)^* &= F(-F^{-1}(t)) \\ &= 1 - F(F^{-1}(t)) = 1 - t. \end{aligned}$$

Thus, the critical values are

$$(\theta - \lambda)^* = 1 - t, \text{ and} \tag{6a}$$

$$x^* = 1 - t - \sigma F^{-1}(t). \tag{6b}$$

These critical values correspond to the critical values in CDMS, the only novelty being the addition of the early speculation of the large player λ .

Before proceeding, let us briefly describe the economic outcome so far. As noted above, there is no aggregate uncertainty as to the behavior of the small players. All players observing a signal $x_i \leq x^*$ will attack. If $\theta - \lambda \leq (\theta - \lambda)^*$, the speculative attack will be successful. If $t < \frac{1}{2}$, then $F^{-1}(t) < 0$ (recall that as f has mean 0, so $F^{-1}(\frac{1}{2}) = 0$), so that $x^* > \theta - \lambda$. Thus, in this case a small player will attack even if he observes a signal $x_i \in ((\theta - \lambda)^*, x^*)$, i.e. even if he observes a signal that implies that the probability of success is below $\frac{1}{2}$. The expected profits is nevertheless positive as the gain from a successful attack in this case is greater than the loss from an unsuccessful one.

We then consider the decision of the large player of whether to speculate in period 1, and if so, by how much. As there is no aggregate uncertainty in the behavior of the small players, the large player can anticipate their speculation perfectly. From (6) a devaluation will take place if the fundamental $\theta \leq \theta^* \equiv 1 - t + \lambda$. This will yield the opportunity to a profit from additional late speculation in period 3, so that the total speculation is L . However, there is also a risk, occurring with probability q , that the speculation in period 3 comes too late, so that the large player only profits from his early speculation λ .

The probability that an attack succeeds can be written as

$$\begin{aligned} \text{prob}[\theta \leq 1 - t + \lambda | y] &= \text{prob}[y - \tau \eta \leq 1 - t + \lambda | y] = \\ &= \text{prob}\left[\frac{y - \lambda - (1 - t)}{\tau} \leq \eta | y\right] = G\left(\frac{1 - t + \lambda - y}{\tau}\right), \end{aligned}$$

where we again use the symmetry of the distribution. The expected payoff by attack-

ing in the amount $\lambda \geq 0$ at an early stage is thus

$$E\pi = G\left(\frac{1-t+\lambda-y}{\tau}\right)(L(1-q)+\lambda q) - t\lambda,$$

The first order condition for an interior solution λ^* is

$$\frac{\partial E\pi}{\partial \lambda} = g\left(\frac{1-t+\lambda^*-y}{\tau}\right)\frac{1}{\tau}(L(1-q)+\lambda q) + G\left(\frac{1-t+\lambda-y}{\tau}\right)q - t = 0. \quad (7)$$

As $E\pi$ is a continuous function of λ , defined over the closed interval $[0, L]$, we know that there exists an optimal amount of early speculation λ , that maximizes the expected profits. However, the optimal λ is not necessarily unique, nor is it necessarily interior, given by the first order condition. In fact, if the costs of early speculation, t , are sufficiently small, the optimal early speculation is equal to the credit constraint L . Furthermore, if the risk that the late speculation is too late, q , is sufficiently large, then the optimal early speculation is either zero or equal to the credit constraint L .

Proposition 1 *i. For given values of the other parameters, there exists a critical value for the costs of early speculation $\underline{t} > 0$ such that if $0 < t < \underline{t}$, then the optimal early speculation is equal to the upper constraint, $\lambda = L$*

ii. For given values of the other parameter, and for any given $\kappa > 0$, there exists a critical value $\bar{q} < 1$ such that if $1 > q > \bar{q}$, then the optimal early speculation is either approximately zero or approximately equal to the upper constraint, $\lambda < \kappa$ or $\lambda \in [L - \kappa, L]$.

The proof is in Appendix A. The intuition for these results are as follows. If early speculation is very cheap, t small, early speculation inducing small players to speculate is clearly the more profitable alternative. As the large player is risk neutral, he will then speculate to his limit L . Likewise, if late speculation is very likely not to succeed, either the large player abstains from speculation, or he speculates by the full amount in period 1. In this case, it can not be optimal to speculate less than the credit constraint, because if speculation involves positive expected profits, increasing the early speculation will be even more profitable.

The further analysis of the model is rather involved. To make some progress, we restrict attention to the limit case where there is no risk associated with late speculation, i.e. that $q = 0$. Then, the expected payoff by attacking in the amount $\lambda \geq 0$ at an early stage reads

$$E\pi = LG\left(\frac{1-t+\lambda-y}{\tau}\right) - t\lambda,$$

and the first order condition for an interior solution λ^* is

$$\frac{\partial E\pi}{\partial \lambda} = Lg\left(\frac{1-t+\lambda^*-y}{\tau}\right)\frac{1}{\tau} - t = 0. \quad (8)$$

Note first that if $Lg(o) \frac{1}{\tau} - t < o$ (which is equivalent to $g(o) < \frac{\tau t}{L}$), then it is never optimal to speculate early, as this implies that $\frac{\partial E\pi}{\partial \lambda} < o$ for all y and λ (recall that the density $g(\cdot)$ has its maximum for the argument zero). The intuition is straightforward: if the gain from a successful speculative attack (L) is too small relative to the cost of speculation (t) and the effect of attempts to induce a speculative attack ($g(\cdot)$ and τ), then it will never be profitable to try to induce a speculative attack. In the sequel, we shall assume that $g(o) > \frac{\tau t}{L}$, implying that it will be profitable to induce a speculative attack under some circumstances, as will be discussed below.

The second order condition for an interior solution is

$$\frac{\partial^2 E\pi}{\partial \lambda^2} = L \cdot g' \left(\frac{1-t+\lambda^*-y}{\tau} \right) \frac{1}{\tau^2} < o.$$

From the second order condition it follows that the optimal λ^* must satisfy $\frac{1-t+\lambda^*-y}{\tau} > o$, so that $g'(\cdot) < o$.⁹

Restricting attention to the interval $\frac{1-t+\lambda^*-y}{\tau} > o$, so that $g'(\cdot) < o$, and hence the inverse of $g(\cdot)$ is defined, we can solve (7) for the optimal λ :

$$\begin{aligned} \frac{1-t+\lambda^*-y}{\tau} &= g^{-1} \left(\frac{\tau t}{L} \right), \text{ or} \\ \lambda^* &= y - (1-t) + \tau g^{-1} \left(\frac{\tau t}{L} \right). \end{aligned} \quad (9)$$

Let y^{L^o} be the value of y for which the optimal early speculation λ^* is zero, i.e.

$$y^{L^o} = 1-t - \tau g^{-1} \left(\frac{\tau t}{L} \right). \quad (10)$$

Proposition 2 *Assume that $q = o$ and $g(o) > \frac{\tau t}{L}$.*

- i. Then there exist critical values y^{Hi} and y^{L^o} such that if the signal of the large player y is below or above these critical values, $y \leq y^{L^o}$ or $y \geq y^{Hi}$, then the optimal strategy is not to speculate early, i.e. set $\lambda = o$.*
- ii. If $y \in (y^{L^o}, y^{Hi})$, the optimal strategy is to speculate early, setting $\lambda = \lambda^* > o$, where λ^* is given by (9).*
- iii. A marginal change in the speculation costs t has an ambiguous effect on the optimal early speculation by the large player, λ^* .*

The proof is in Appendix B. The intuition behind the proposition is the following. If the signal of the large player y is low (below y^{L^o}), reflecting that the fundamentals θ is low, the large player will view a devaluation as so likely that he will not find it

⁹For $\frac{1-t+\lambda^*-y}{\tau} < o$, we have $g'(\cdot) > o$ implying that $\frac{\partial^2 E\pi}{\partial \lambda^2} > o$, so that a solution to (7) would be a local profit minimum.

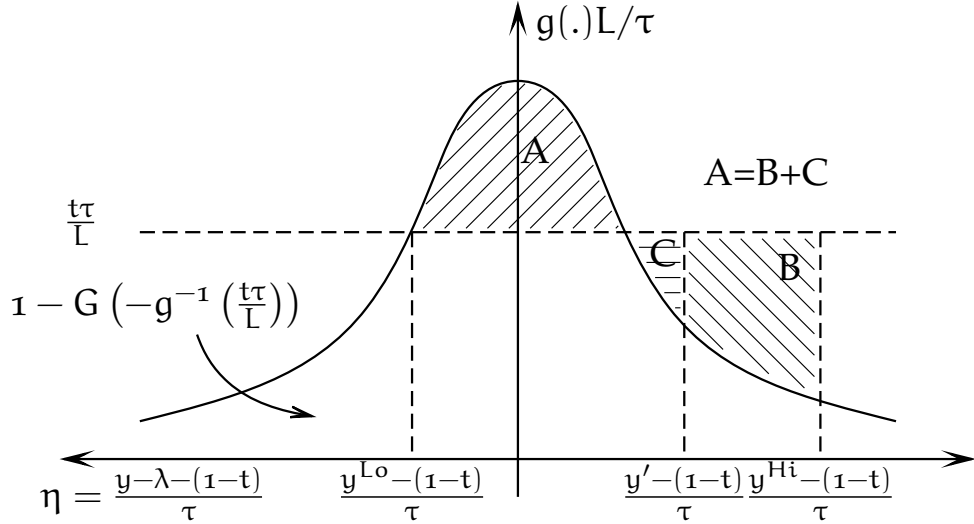
profitable to incur the costs by early speculation, even if this would increase the probability of a devaluation. Nor will the large player find it profitable to speculate early if the signal of the large player y is high (above y^{Hi}), reflecting that the fundamentals θ is high, as in this case it will be too costly to raise the probability of a devaluation. However, for interior values of y , the gain from increasing the probability of a successful speculative attack by an early speculation of the large player is sufficiently large to outweigh the costs, and the large player will indeed speculate early. Note that (9) and (10) yields $\lambda^* = y - y^{Lo}$, implying that the optimal early speculation λ^* is increasing one for one in the signal y in the interval (y^{Lo}, y^{Hi}) , starting at zero for y^{Lo} and reaching its maximum for y^{Hi} . However, for $y \geq y^{Hi}$, optimal early speculation is zero.

The large player's choice of early speculation is illustrated in Figure 1. Assume that the large player observes a signal $y' \in (y^{Lo}, y^{Hi})$. If the large player does not speculate early, a devaluation will nevertheless take place if the fundamentals are sufficiently low, which, given the signal y' , requires that the noise term $\eta \geq \frac{y' - (1-t)}{\tau}$. In Figure 1, this probability is captured by the area below the bell shaped density function $g(\cdot)$ that is to the left of the signal (although in the figure, we multiply $g(\cdot)$ by L/τ so that it is measured in revenue terms, i.e. it represents the expected marginal revenue from speculation). If the large player makes a marginal early speculation, the expected marginal revenue is $g(\frac{y' - (1-t)}{\tau}) \frac{L}{\tau}$ which is lower than the marginal cost t (given by the horizontal dashed line), thus a marginal early speculation will not be profitable. However, if the large player makes a larger early speculation, the marginal revenue curve comes above the marginal cost line, implying that if the player speculates early, the marginal profits from increasing the speculation is positive, as seen by the area A being larger than the area C. The optimal early speculation is given by $\lambda^* = y' - y^{Lo}$, where expected marginal revenue $g(\frac{y' - \lambda - (1-t)}{\tau}) \frac{L}{\tau}$ is equal to marginal costs t . Thus for all $y \in (y^{Lo}, y^{Hi})$, early speculation in the optimal amount, ensuring that $y - \lambda = y^{Lo}$, will be profitable for the large player. However, for a signal y^{Hi} , the expected gain from early speculation, even in the optimal amount, is zero. This is illustrated in Figure 1, by area B+C (the loss from some early speculation where expected marginal revenue is below marginal costs) is equal to area A (the gain from additional early speculation where expected marginal revenue is greater than marginal costs). For higher values of y , early speculation is too costly.

Hence, the optimal early speculation λ^* is strictly increasing in the interval (y^{Lo}, y^{Hi}) , starting at zero for y^{Lo} and reaching its maximum for y^{Hi} , and then falls to zero again for $y \geq y^{Hi}$.

The ambiguous effect of an increase in the speculation costs on the amount of early speculation reflects two opposing effects. On the one hand, higher speculation costs will reduce speculation by small players, inducing the large player to do more early speculation himself (cf. equation (9)). On the other hand, higher speculation

Figure 1: Early speculation (λ) by large player



Note: Marginal cost of early speculation ($\frac{t\tau}{L}$) is given by the dotted horizontal line. The bell-shaped curve, $g(\cdot)L/\tau$, represents the marginal gain. For $y \in (y^{Lo}, y^{Hi})$ the optimal strategy is to speculate early, setting $\lambda = \lambda^*$. If the large player observes y' , the gain from speculating early in the amount $\lambda^* = y' - y^{Lo}$ is indicated by area A minus area C.

costs make it more costly to speculate early, which has a dampening effect on early speculation. Higher variance in the signal of the large player also has ambiguous effects. With more accurate information, there is less uncertainty for the large player on whether the early speculation will induce a successful attack. This will lead to more early speculation when this is indeed profitable, and less early speculation, when it is less profitable.

3 Data and description of crises

We begin by briefly describing our data, before we give a description of the crises we are studying.

3.1 Trading data

Norges Bank and Sveriges Riksbank collect data from market making banks on net spot and forward transactions with different counterparties. From Norges Bank we have weekly observations on Norwegian market making banks' trading with foreigners, locals, and the central bank.¹⁰ Foreign participants are typically dominated by financial investors, especially in periods of turbulence. In the data set from Sveriges Riksbank we have weekly observations on both Swedish and foreign market making banks' trading with non-market making foreign banks and with Swedish non-bank customers. The first group represents financial investors (see Bjønnes, Rime, and Solheim, 2005). We will henceforth refer to locals as small players and foreigners as large

¹⁰Foreigner and local are defined by their address. Trading is calculated based on end-of-week net positions, corrected for exchange rate movements.

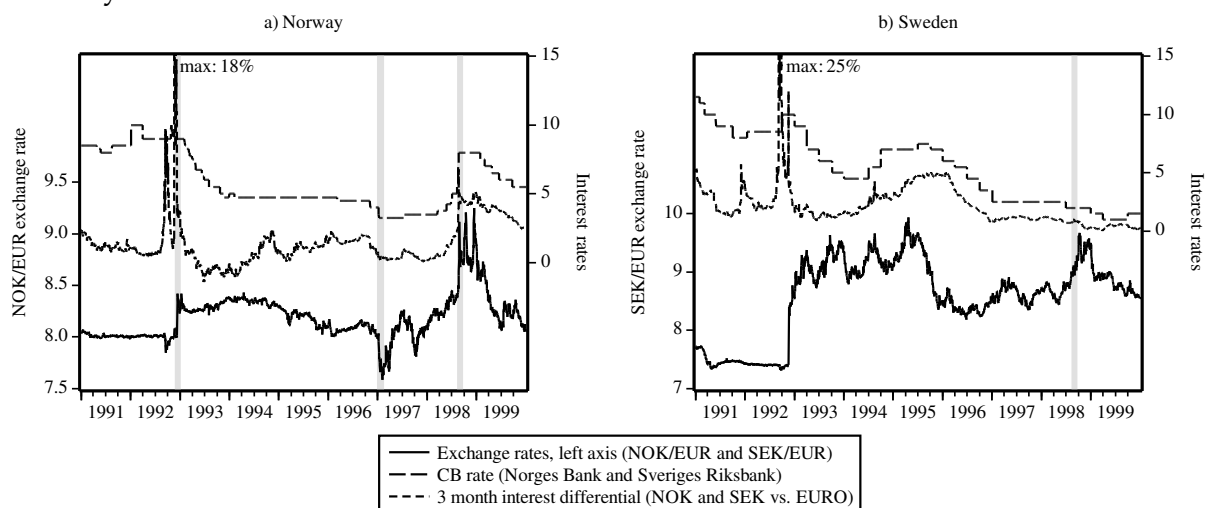
players.

The Norwegian data distinguish between spot and forward. The Swedish data also contain swap and option volumes, in addition to purchases and sales of spot and forward contracts. For Norway we have observations from 1991, while the Swedish data set starts in 1993. Further information about the two data set will be given in the discussion of the three crises below. Descriptive statistics for the Norwegian transactions are shown in Table 4 and 5 in the appendix, both for the whole period with data and for the specific crises.

3.2 Three crisis periods in Scandinavia

In this section we give a brief overview of the three crisis periods that we analyze: (i) the ERM-crisis and the depreciation of the Norwegian krone in December 1992; (ii) the appreciation of the Norwegian krone in January 1997; and (iii) the crisis in both Norway and Sweden following the Russian moratorium in August 1998. Figure 2 shows the NOK/EUR and SEK/EUR exchange rates, together with the Norwegian sight deposit rate and the Swedish discount rate and the 3-month interest rate differential against Germany for the two countries, from the beginning of 1990 until the end of 2000.¹¹

Figure 2: Exchange rate, Central bank rate, and 3-month interest rate differential: Norway and Sweden



Note: Daily observations on exchange rates, measured along the left axis, and central bank rate and interest differential, along the right axis. Exchange rates are local currency pr. euro, using ECB conversion rate for deutsche mark vs euro. Interest rate differentials are local interbank interest rate less German interbank interest rate. Shaded areas indicate the crises.

The key dates for the attacks can be identified e.g. from the financial press. In addition we have created the usual “crisis index” used to identify events with special pressure on the exchange rate (see e.g. Eichengreen, Rose, and Wyplosz, 1995, for a description). The crisis index, which take into account that speculative pressure may

¹¹The euro was introduced Jan. 1, 1999. Using euro-rates implies that we use the NOK/DEM and SEK/DEM exchange rates adjusted for the DEM/EUR-conversion.

materialize through interest rate changes instead of exchange rate changes, also identifies these three periods. The index identifies several single events, but these three periods are the only clusters of events.¹² The descriptive statistics on flows confirm that there are major movements in the expected direction during the identified events.

3.2.1 The ERM-crisis: 1992

The 1992-event has the features of a “traditional” currency crisis. Prior to 1992 both Norway and Sweden had pegged their exchange rates to the ECU, with a fluctuation band of $\pm 2.5\%$ and $\pm 1.5\%$ respectively. From Figure 2 we see that during 1991 and until October 1992 the Norwegian exchange rate was stable (around a level of 7.65 against the ECU). In September first Finland and Italy, and later the UK, were forced to abandon their fixed pegs.¹³ Sweden withstood an attack in September, but chose to devalue in late November after increasing interest rates to 500%. Under the speculative pressure during the fall of 1992, Norges Bank repeatedly increased its key rate to reduce capital outflows. On December 10, 1992, Norges Bank was forced to abandon the fixed ECU-rate. The exchange rate stabilized in the interval between 8.3 and 8.4 against the ECU, implying a change of about 10% from middle rate to middle rate.

In Figure 3 we see the levels of net positions in spot and forward for small (locals) and large (foreigners) players in the period from May 1992 to January 1993. One of the most striking features of this figure might be how stable these positions are throughout the first part of 1992. The only position that reveals a change is large players’ (foreign) forward. Here we see a trend out of NOK-holdings from early August 1992. At this time the interest rate differential was very small. The holdings do, however, stabilize in October 1992. In November 1992 speculative activity emerges in two forms: Small players sold NOK spot and large players (foreigners) sold NOK forward. This is as one should expect. Locals have a larger part of their portfolio in NOK, and should therefore be able to sell NOK spot, while foreigners presumably hold a more limited amount of NOK spot.

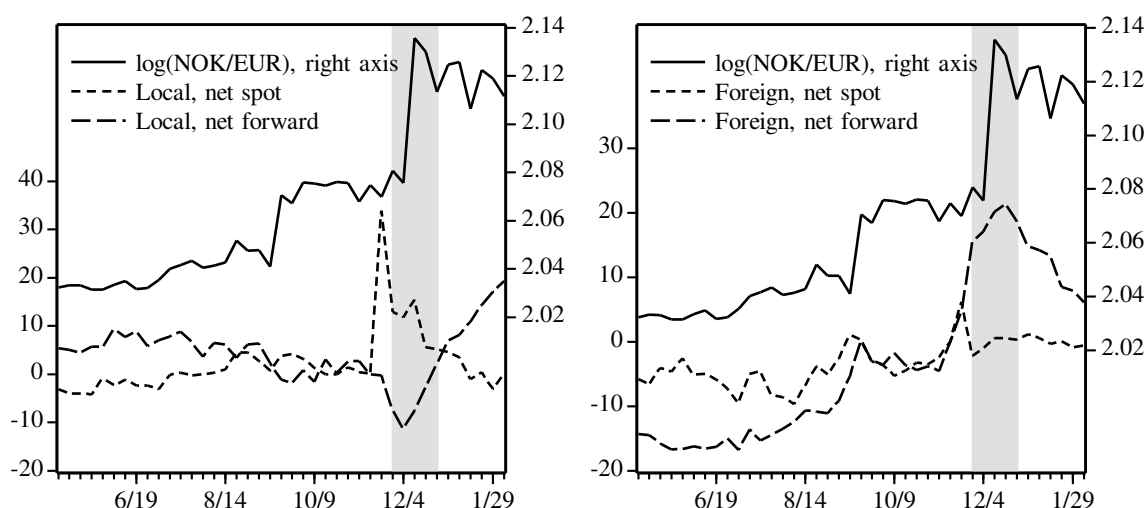
3.2.2 The Norwegian crisis: 1997

In the aftermath of the ERM-crisis Norway and Sweden chose different monetary policy regimes. Sweden adopted a formal inflation target of 2% in 1993. Norway, on the other hand, chose a managed float regime. Norges Bank had an obligation to stabilize the exchange rate, but only in a medium-term sense. Extreme measures to hold the

¹²The results for the crisis index is reported in the appendix.

¹³For an excellent account of the ERM-crisis, see ?. Finland, Sweden and Norway were not part of the ERM, but were still regarded by the market as part of it due to their unilateral pegs to ECU as a first step of joining EU.

Figure 3: The exchange rate and the level of net positions: Norway during the ERM-crisis.



Note: Exchange rates measured along the right axis and positions on the left axis. A negative position indicates a net holding of NOK. Grey areas indicate the crisis-sample.

exchange rate within bounds in the short term were not to be used.¹⁴

In January 1997 there was speculation inducing an appreciation of the Norwegian krone. The cost of a DEM in NOK fell by more than 5% over a period of 14 days with the largest changes on Jan. 8th – 10th, while the SEK/DEM was largely unaffected. Pressure against NOK had been building for some time prior to this. A number of newspaper reports referred to the role of foreigners speculating in a Norwegian appreciation during the fall of 1996. For instance, on November 5, 1996, the leading business newspaper in Norway (Dagens Næringsliv) reported that foreign analysts “believe in stronger NOK”.¹⁵ Already on the next day, Norges Bank lowered its key rate. According to newspapers, Kjell Storvik (the governor of the central bank) hoped that this would reduce the interest in NOK among foreign investors.¹⁶ On November 29, 1996, Dagens Næringsliv states that

[f]oreigners have again thrown themselves over the Norwegian krone. [...] People in the market [...] believe that the strengthening is a result of foreign investors now believing NOK is so cheap that it is a good buy.¹⁷

The speculators believed that a strong Norwegian economy and emerging inflationary pressure would force the Norwegian government to change from a managed

¹⁴The monetary policy regulation from May 6, 1994, stated: “... monetary policy instruments will be oriented with a view to returning the exchange rate over time to its *initial range*. No fluctuation margins are established, nor is there an appurtenant obligation on Norges Bank to intervene in the foreign exchange market.” Emphasis added. Norway officially introduced an inflation target of 2.5% in March 2001.

¹⁵Mathiassen (1996).

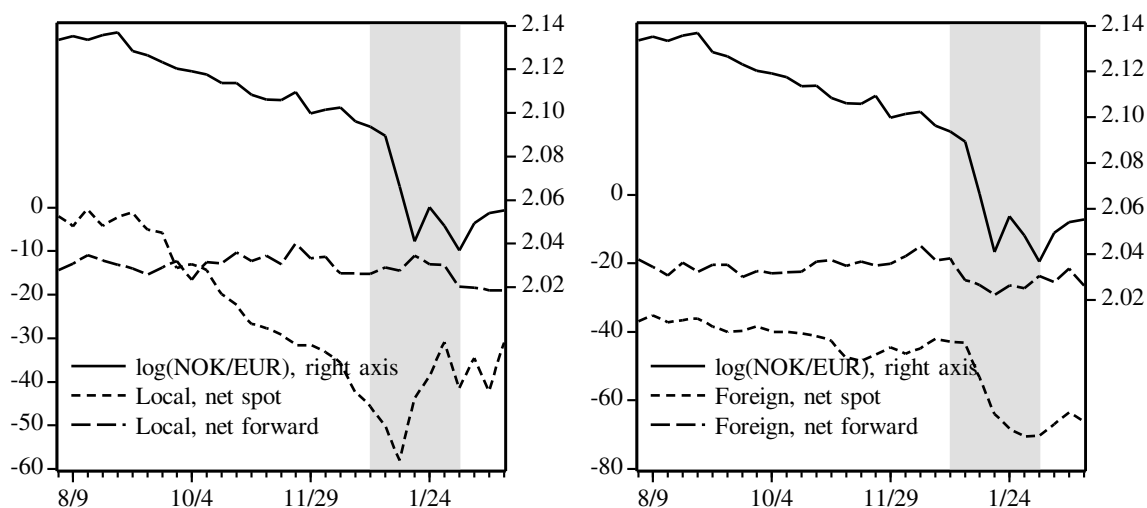
¹⁶Næringsliv (1996).

¹⁷Haug (1996).

float to an inflation targeting regime. Inflation targeting would allow Norges Bank to set interest rates higher to fight inflation and dampen a potential boom, with little regard for a potentially steep appreciation of the NOK. Norges Bank instead defended the exchange rate by lowering its key rate and intervening in the market.

Figure 4 shows the NOK/DEM exchange rate and the level of net positions during the period from August 1996 to February 1997. First, note that there is no movement in the forward positions over this period. Second, we see that the exchange rate was trending down from early September 1996. In the period from September to December small players (locals) accumulated spot foreign currency positions as the exchange rate was appreciating. Large players (foreigners) did not change their net positions. During the speculative attack in the first weeks of 1997, the central dates were January 6-7, 1997, large players (foreigners) were buying NOK spot. At this time small players (locals) were selling NOK spot.

Figure 4: The exchange rate and the level of net positions: The Norwegian 1997-crisis.



Note: Note: Exchange rates measured along the right axis and positions on the left axis. A negative position indicates a net holding of NOK. Grey areas indicate the crisis-sample.

3.2.3 The Russian moratorium crisis: August 1998

The 1998-crisis in Norway and Sweden took place at the same time as Russia declared a debt moratorium, which was the starting point of a period with substantial international financial turbulence and uncertainty. Russia experienced a boom during the mid-1990's, not least due to high oil prices. However, in June 1998 Russia began to experience balance-of-payment problems as oil prices had fallen substantially through the year.¹⁸ Russia turned to negotiations with the IMF and international creditors, and, after severe problems, an agreement was reached on the evening of Sunday, July 12. In the ten days prior to this agreement the central bank of Russia had sold USD 1.6

¹⁸Oil prices fell from USD 17 at the beginning of 1998 to an average price of USD 12.50 in the period June-October 1998.

billion in attempts to stabilize the exchange rate. During August the crisis reemerged, and on August 17 the Russian president Boris Jeltsin announced a reform package including a possible devaluation of the rouble. The result was a meltdown of international confidence. On August 24 Russia declared a moratorium on all debt payments. This event triggered massive international uncertainty. Investors withdrew money from small currencies, including the NOK and SEK, and countries with a high share of raw material exports were hit especially hard.

In Norway market participants had for some time expected a change in the monetary regime, from a managed float to inflation targeting. During the spring of 1998 Norway experienced a slowdown in growth, and many argued for monetary and fiscal stimulus in order to spur growth.¹⁹ A change to inflation targeting was expected to have resulted in lower short-term interest rates in order to stimulate growth, and thus a weaker currency. The international and domestic turmoil together triggered large movements, with the largest on the 24th and the days immediately following.

The reaction functions of Norges Bank and Sveriges Riksbank are partly revealed when we look at Figure 2. We see that while Norges Bank increased its key rate as the NOK/DEM depreciated in July and August, Sveriges Riksbank did not adjust its key rate in response to changes in the exchange rate during this period. This is a clear indication of two very different monetary policy regimes. A key implication is that in Norway delayed speculation would involve a benefit from the interest rate differential. In contrast, in Sweden, there was no increase in the interest rate and thus no reason to postpone speculation.

Figures 5(a) and 5(b) show NOK/DEM and SEK/DEM exchange rates and the level of net positions during the period from May 1996 to December 1998. Again we see that in Norway small players (locals) were accumulating foreign currency spot during the summer. When the large players (foreigners) attacked in August they did so in the forward market. This sale of NOK was matched by small players (locals) buying NOK forward. In Sweden the large players (foreigners) were selling SEK in July and August, with a peak around the Russian moratorium. Small players (locals), on the other hand, were taking the other side as there were no intervention by the Sveriges Riksbank.

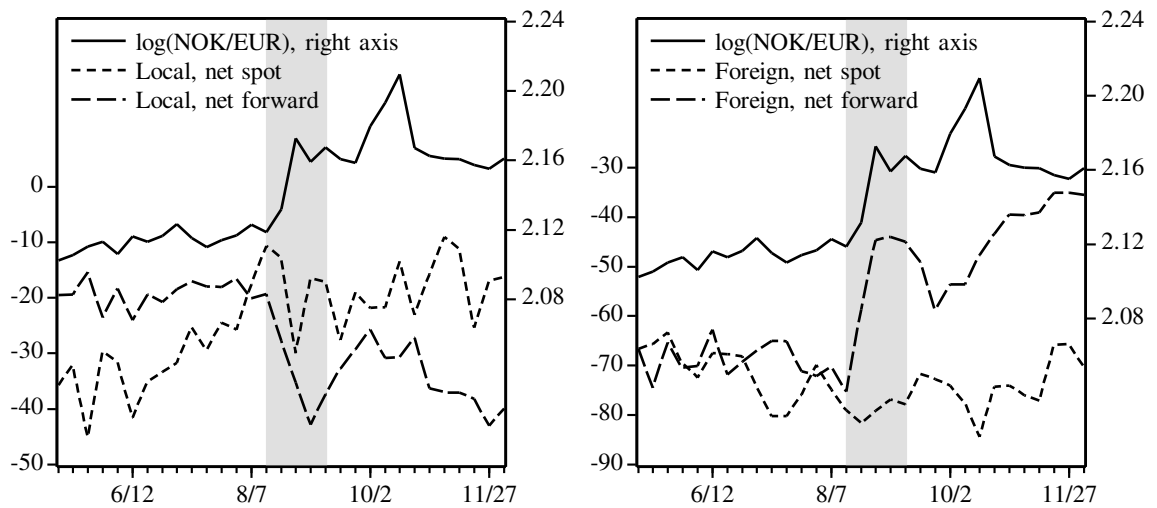
3.3 Macroeconomic fundamentals

The description above is consistent with the evolution of key macroeconomic fundamentals that receive attention in the financial press and industry, see Figures 6 and 7 for Norway and Figure 8 for Sweden (the crises are indicated with vertical lines).

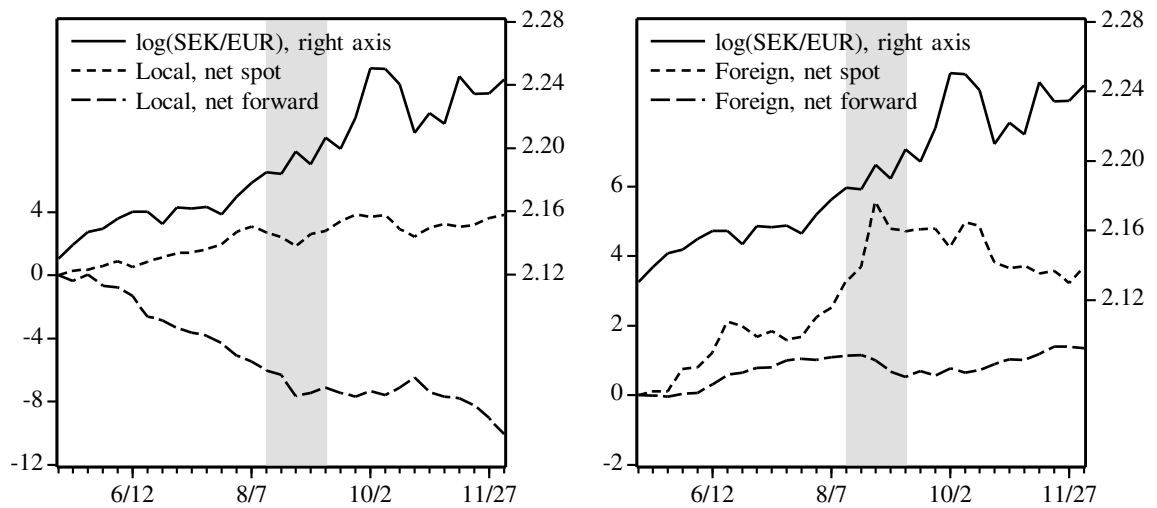
We observe that in 1992 and 1998, all the business and consumer surveys displayed in Figure 6 indicated a downturn of the Norwegian economy. In 1992 markets may

¹⁹Norway's leading indicator peaked in December 1997, and decreased during 1998 (see Figure 7 in the next section).

Figure 5: The exchange rate and the level of net positions: The 1998 Russian moratorium crisis in Norway and Sweden.



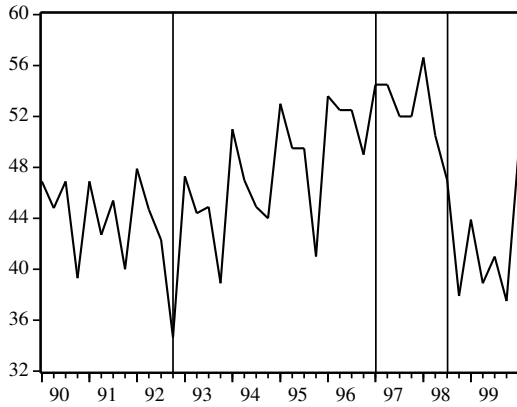
(a) Norway



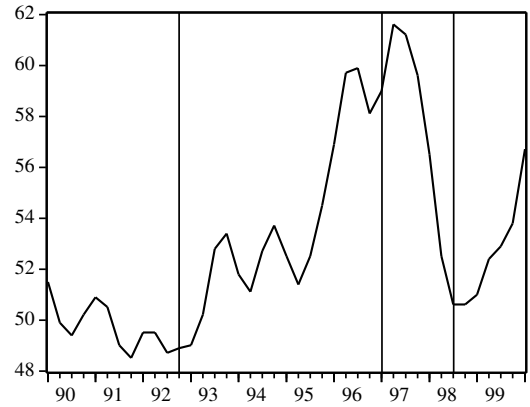
(b) Sweden

Note: Exchange rates measured along the right axis and positions on the left axis. A negative position indicates a net holding of local currency, i.e., NOK or SEK. Grey areas indicate the crisis-sample.

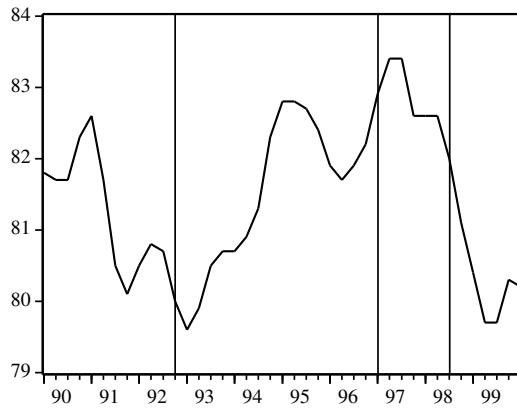
Figure 6: Quarterly survey data on Norwegian economy



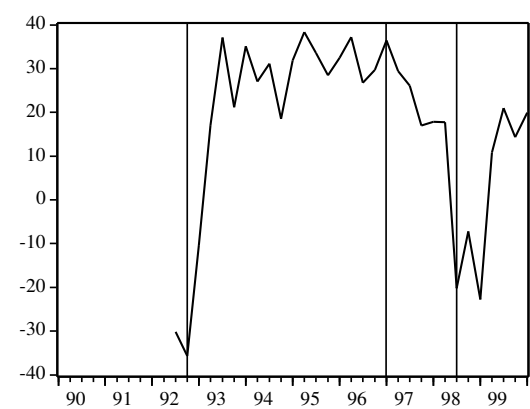
(a) Business survey: Expected employment in manufacturing



(b) Business survey: Expected stock of orders in manufacturing



(c) Business survey: Capacity utilization in manufacturing



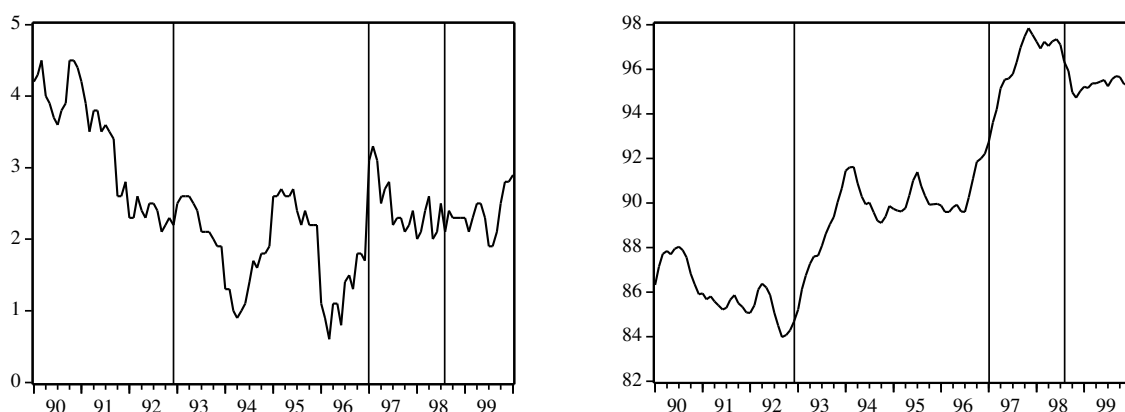
(d) Consumer survey: Expected economic situation next 12 months

Note: Statistics Norway is source for a)-c), while d) is from TNS Gallup. a) and b): Increasing index above 50 indicates increasing growth. c) Percent of utilization. d) Positive values indicate that a majority have replied "better" while negative values indicate that a majority have replied "worse". Horizontal lines indicate the crises.

have expected that Norway would devalue in order to spur growth via increase exports. Furthermore (not shown), Norway's competitiveness had deteriorated due to higher inflation than Germany and other ECU-countries for a long period, and due to the devaluations of other countries during the ERM-crisis.

In 1998, the sharp fall in business and consumer surveys also fuelled the debate of a change in the policy regime for Norway. While the level the composite leading indicator was still high compared to the average over the 1990s (see Figure 7), it fell markedly. However, at this time the influence from the Russian moratorium crisis was clearly also an important factor.

Figure 7: Monthly data on Norwegian economy



(a) Consumer Price Index: Year-on-year change

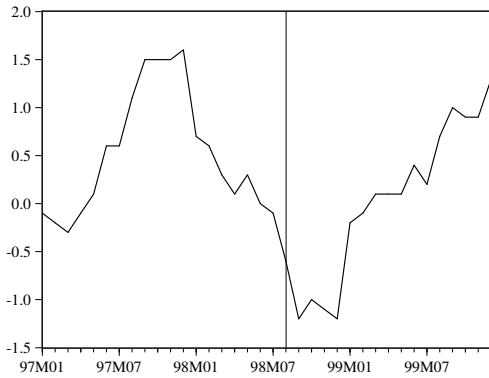
(b) Composite leading indicator

Note: Source for a) is Statistics Norway, while for b) OECD. The composite index contains the following components: Retail sales; Job vacancies; Judgment on capacity utilisation; New export orders; Share prices; and Yield on government bonds. Horizontal lines indicate the crises.

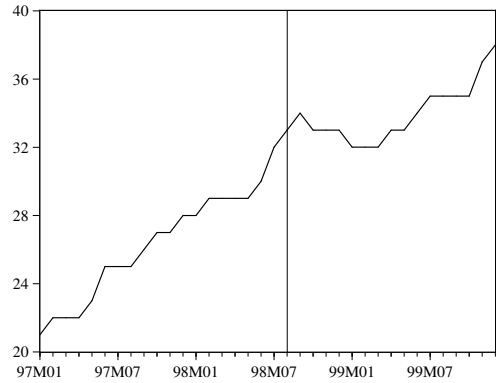
Sweden had in August 1998 been through a period of decreasing inflation. However, this did not go together with an slump. Rather, expectations about employment growth over the next 12 months were high. The Riksbank, an inflation-targeting central bank at the time, could expect that this could lead to wage increases, and thereby inflation picking up. In August 1998, a depreciation of the SEK/EUR could contribute in this process. Hence, the Riksbank had few motives for changing their target interest rate.

Business and consumer surveys indicated a strong boom in the Norwegian economy in 1997. Inflation started to rise sharply, see panel (a) in Figure 7, yet the interest rate was kept low to avoid appreciation of the krone. In this situation, several observers and chief economists argued publicly that the monetary regime should be changed to Inflation Targeting, to allow for a hike in interest rates. This would most likely have lead to a marked appreciation of the krone.

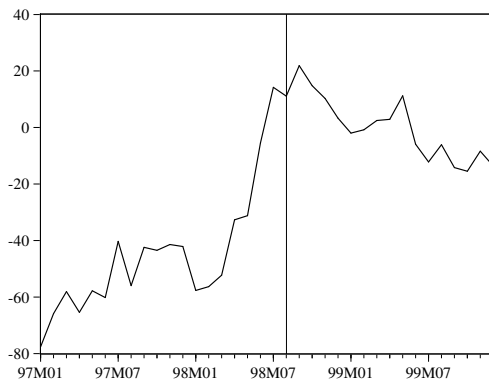
Figure 8: Monthly data on Swedish economy



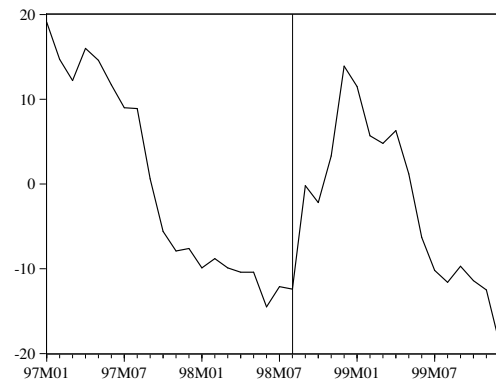
(a) Consumer Price Index: Year-on-year change



(b) Riksbank forecast: New jobs



(c) Business survey: Employment expectations



(d) Consumer survey: Expected unemployment next 12 months

Note: Sources are: Graph a), Statistics Sweden; graph b), Sveriges Riksbank; graph c) and d), DG ECFIN. Graph b) shows thousands of persons in new jobs, while positive numbers in graph c) and d) indicate that more people have replied that the variable in question will increase. Horizontal lines indicate the crisis.

4 Results

Before reporting the result, let us briefly discuss the empirical implications of the model, in view of the data that is available to us. The key predictions of the model are as follows: If fundamentals are weak, i.e., a successful attack is very likely, large players will move in the rear in order to reap the interest rate benefit (if any), while small players will move early. If fundamentals are stronger, or the interest rate benefit is small, large players may move early as well in order to induce small players to join in on the attack. If early speculation is sufficiently cheap, the large player may speculate early only. In this case it will be the small players that trigger the exchange rate change. Since foreigners can raise more funds on short notice we will treat foreigners as large players.

We have identified four specific events, three in Norway and one in Sweden. For the three cases in Norway we argue that the fundamentals were consistent with a speculative attack taking place. Furthermore, we have argued that an attack did indeed occur in all four cases. Fundamentals, i.e., support for the current exchange rate regime, were stronger in Sweden, and gives us some possibility to test the theory. We have good data for trading behavior, so we can report results as to (i) The sequence of move of the large and small players, and (ii) which players trigger the actual change in the exchange rate. However, while we can argue that the fundamentals were weak enough for a successful attack to take place, we do not know whether the fundamentals were weak or strong in relation to the predictions of the theoretical model, i.e., whether the large player found an attack very likely or less likely.²⁰ Nor do we observe the signal of any of the players. This implies that some of the predictions of the model cannot be tested for. One variable we do observe, however, is the interest rate differential. Thus, this variable will be key in the empirical tests below.

To test for the sequence in the speculative attacks we will use the statistical concept of Granger causality. Granger causality is not an economic definition of causality, but might be useful to distinguish between which group of players move first or last.

There is *absence* of Granger causality from x to y if estimation of a variable y on lagged values of y and lagged values of x are equivalent to an estimation of y on only lagged values of y . This can be expressed as

$$y_t = \alpha_0 + \sum_{i=1}^k \alpha_i y_{t-i} + \sum_{i=1}^k \beta_i x_{t-i} + \varepsilon_t, \quad (11)$$

where the variable x *does not* Granger cause y if the joint hypothesis of $\beta_1 = \dots = \beta_k = 0$ is not rejected. If this hypothesis is rejected for say x in the equation for y ,

²⁰Ex post we can conclude that the episodes studied are the major successful attacks during the period, which gives us a hint that actual fundamentals were not too strong. Furthermore, since the signal of the large player is unbiased we can use observed fundamentals to infer what signals the large players may have received. The discussion in Section 3 indicates that fundamentals were quite weak.

while not rejected in case of y in a similar equation for x , we say we have one-way Granger causality from x to y .

When choosing the sample for the Granger causality test we take the crisis dates as our starting point. We end the samples as soon as there are any signs that the exchange rate has stabilized, i.e., when the crisis is over. The beginning of the sample is determined similarly, and in addition adding observations in the beginning to ensure that the sample is sufficiently long for statistical analysis. This balances the need for a sufficient number of observations without mixing crisis periods and calm periods.

The results from the Granger causality tests are shown in Table 1. We regress the first-difference of the net position used in the attack (flows), as seen from the graphs of Figs. 3 to 5, on lags of small's (locals) flows and large's (foreigners) flows. We use dummies to differentiate between crisis period and pre-crisis period, and p-values are in parenthesis. Number of lags are determined from the Schwarz and Akaike information criterions.²¹ In the appendix we present a similar system using all flows which confirm the results.²²

For the three Norwegian crises we see that lagged speculation of small players during the crisis-period has a significant positive effect on the speculation of large players, while the lagged speculation of large players has no significant effect on the small players' speculation. Thus, small players Granger cause large players. This is in line with the model since in all three cases interest rate differentials changed in such a way to make it more costly to speculate early, implying that large players might gain from delaying the attack.

For the Swedish 1998-crisis there is some evidence that large players Granger cause small players, as lagged speculation of large players is significant in the small player regression. This result is also consistent with the model since large players (foreigners) did not have a gain from waiting as Sveriges Riksbank did not increase interest rates; hence risk-adjusted gains by moving late were lower. In Sweden, no change in monetary policy was expected, indicating a higher fundamental θ , and a higher signal y . On the other hand, lower Swedish interest rates meant that speculation costs were lower, i.e. lower t . For small players, high θ and low t have opposing effects, leaving the impact on speculation indeterminate. For large players, however, it follows directly from (9) and the proof of the Proposition in the appendix, that, keeping the sum of the signal and the speculation costs, $y + t$, constant, an increase in speculation costs leads to less early speculation by the large player. In other words, in the speculative attack in Sweden, where interest rates were low, we would expect more early speculation by the large player. When compared to the results from Norway this

²¹We choose lags based on the shortest positive lag selected by these two criterions. The weekly frequency employed makes us prefer to use shorter lags in order to match the theoretical model.

²²A summary of other results for the crisis and pre-crisis periods, for different lag-structures and VAR-formulations, and for method robust to outliers, indicate that the results are rather robust, and is available upon request.

Table 1: Granger causality test for flows: Crisis and pre-crisis

Note: Difference of net-position (flows) used for speculation by large and small players estimated within a system on lagged flows of large and small players, with dummies for pre-crisis period and crisis period. p -values in parenthesis. All equations use one lag, except for both Norway and Sweden in 1998 where we use two lags of small's trading in the large-specification during the crisis-period and pre-crisis period, respectively. In Norway, small players (locals) always speculate in spot, while Large players (foreign) speculate with spot in 1997 and with forward in 1992 and 1998. For the Swedish 1998 crisis we estimate using difference of spot position for Large players and difference of forward position for Small players. Significance at 1%, 5%, and 10% are indicated using ***, ** and *, respectively.

	Norway						Sweden		
	1992		1997		1998		1998		
	Large	Small	Large	Small	Large	Small	Large	Small	Small
Constant	0.352 *(0.09)	0.177 (0.44)	-0.305 (0.13)	-1.092 *(0.07)	-0.441 (0.33)	0.789 (0.14)	0.010 (0.92)	-0.244 *** (0.00)	
Crisis: Large, lagged	0.357 ** (0.02)	0.098 (0.71)	0.573 *** (0.00)	-0.721 (0.11)	0.030 (0.91)	-0.009 (0.98)	-0.153 (0.41)	0.350 ** (0.03)	
Crisis: Small, lagged	0.208 *** (0.00)	-0.420 *** (0.00)	0.184 ** (0.04)	-0.401 ** (0.03)	0.341 *** (0.00)	-0.379 *** (0.00)	-0.190 (0.39)	0.332 (0.13)	
Crisis: Small, 2nd lag					0.316 ** (0.01)				
Pre-crisis: Large, lagged	-0.208 ** (0.01)	-0.021 (0.82)	-0.268 *** (0.00)	-0.136 (0.33)	-0.080 (0.39)	0.017 (0.94)	0.388 * (0.07)	-0.263 * (0.05)	
Pre-crisis: Small, lagged	0.014 (0.91)	-0.124 (0.22)	0.077 ** (0.03)	-0.315 *** (0.00)	0.141 (0.34)	-0.403 *** (0.00)	0.094 (0.75)	0.048 (0.83)	
Pre-crisis: Small, 2nd lag							0.490 *** (0.00)		
adj.R ²	0.23	0.13	0.21	0.12	0.03	0.11	0.07	0.06	
Durbin-Watson	2.17	2.23	1.91	1.80	1.88	2.29	2.08	2.06	
Observations	81		70		71		71		
Crisis-observations	41		30		31		31		
Crisis period	May 1, 1992 – Feb 2, 1993		Aug 9, 1996 – Feb 28, 1997		May 8, 1998 – Dec 4, 1998		May 8, 1998 – Dec 4, 1998		

indicates that the locals did not move early in Norway due to better information.

Finally, a comparison of the pre-crisis and crisis part of Table 1 we see that the pattern discussed above is not representative for the pre-crisis periods. The coefficient on lagged flow of large players is negative in the pre-crisis period of all three attacks on Norwegian krone, while it is positive during the crisis-periods. In 1997 there is positive feedback from the small players to the large in the pre-crisis period, but since the large players' own lagged flow is negative we can not call this speculative herding. This is consistent with the idea of the model that trading sequences during an attack are different from non-crisis periods.²³

The second question is to identify which group was most active during the actual crisis. To investigate this question we use the following strategy. We regress changes in the exchange rate on contemporaneous changes in flows and macro variables. Due to problems of multicollinearity we run separate regressions for small (locals) and large (foreigners) players.

The sample is selected in the same way as in the Granger causality-analysis. We use the same observations as above, but since we also estimate flow effects outside of the actual crisis we merge these three periods. The focus is on what happens during the actual speculative attack. Hence, for each crisis we create dummies that equal one the week before the actual attack and the largest changes around the official date, and zero otherwise. This gives us three crisis-observations (dummy equals one) for 1992 and 1998, and four for 1997. Tables 2 and 3 report the regressions for Norway and Sweden respectively.

In the regressions we include the 3-month interest rate differential against Germany and the log-differenced oil price as macroeconomic variables. The rows labeled "Spot" and "Forward" report the coefficients and t-values for flows outside the actual crisis, while the other rows are the effect of flow in the different crisis. For Sweden we only consider the 1998-crisis.

From the informal discussion as well as the Granger causality analysis above, we would expect that large players (foreigners) were instrumental in the three Norwegian crises. This should be reflected in significant and positive coefficients, as players buy currency (positive flow) when speculating on a depreciation (positive change in the exchange rate), and sell when speculating on an appreciation. In the 1992- and 1998- crises, foreigners speculated forward (as they have less spot available), while they used spot in the 1997-appreciation crisis.

We would also expect that the small players' (locals) flow is insignificant in all three crisis in the case of Norway, and at least not positive. From Table 2 we see that these expectations are largely borne through. In addition, the large players' (foreigners) spot flow is significant and positive for the 1992-crisis, and some of the small

²³Table 6 in the appendix show that the results for the crisis and pre-crisis period are robust when using all flows, both spot and forward.

Table 2: NOK-regressions

Note: Regression of NOK-return on first-difference of flows, interest differential and first-difference log oil price. *t*-values in parenthesis below coefficient estimates. Flow-impact during crises are constructed using a dummy on flows.

	$\Delta\log(\text{NOK}/\text{EUR})$	
	on Foreign flows	on Local flows
Constant	-0.00013 (-0.17)	0.00046 (0.50)
Interest rate diff	-0.00062 (-1.07)	-0.00240 (-3.77) **
Oil price	-0.02894 (-1.45)	-0.03162 (-1.47)
92-crisis, spot	0.00839 (3.75) **	-0.00147 (-1.39)
92-crisis, forward	0.00687 (4.29) **	0.00432 (1.68)
97-crisis, spot	0.00226 (3.31) **	0.00088 (1.10)
97-crisis, forward	0.00034 (0.23)	-0.00903 (-2.50) *
98-crisis, spot	0.00238 (1.15)	-0.00183 (-4.01) **
98-crisis, forward	0.00167 (4.44) **	-0.00152 (-2.20) *
Spot	-0.00053 (-1.76)	0.00056 (3.00) **
Forward	0.00026 (0.82)	-0.00007 (-0.20)
AR(1)	-0.22184 (-2.06) *	-0.06703 (-0.59)
adj.R ²	0.41	0.35
DW	2.11	2.04

Table 3: SEK-regressions

Note: Regression of SEK-return on first-difference of flows, interest differential and first-difference of log oil price. *t*-values in parenthesis below coefficient estimates. Flow-impact during crises are constructed using a dummy on flows.

	$\Delta \log(\text{SEK}/\text{EUR})$	
	on Large's flows	on Small's flows
Constant	0.0005 (1.02)	-0.0001 (-0.20)
Interest rate diff.	0.0174 (5.24) **	0.0189 (5.56) **
Oil price	-0.0175 (-1.99) *	-0.0180 (-2.01) *
98-crisis, Spot	0.0033 (0.66)	0.0027 (0.18)
98-crisis, Forward	-0.0078 (-0.29)	-0.0070 (-0.71)
Spot	0.0079 (5.82) **	-0.0058 (-4.18) **
Forward	0.0067 (5.59) **	-0.0037 (-2.70) **
AR(1)	-0.1829 (-4.11) **	-0.1513 (-3.41) **
adj.R ²	0.14	0.12
DW-stat.	2.00	1.99

players' (locals) flows are significant and negative for the 1997 and 1998-crises. Negative coefficients imply that the small players (locals) are providing liquidity to the large players (foreigners) during the actual attack.

For Sweden we do not find any significant effects during the 1998-crisis. Given the evidence that large players (foreigners) Granger caused small players (locals) we would expect that at least the small players (locals) were positive and significant. However, Figure 5 seems to suggest that it is the large players that are most active in the crisis week, and that the period when the SEK actually jumped was somewhat later.

For Norway, we see that the strength of the correlation differ between the three events. For the 1992-case we find a size effect of forward flow is 0.69% per billion NOK sold, or about 5% per 1 billion USD equivalent.²⁴ For the 1997-event we find the spot-effect to be about 1.6% per 1 billion USD equivalent. For the 1998-event we find the effect of forward to be approximately 1.2% per 1 billion USD equivalent. As a comparison, Evans and Lyons (2002) report an effect from order flow to the DEM/USD exchange rate of about 0.5% per 1 billion USD equivalent. The larger effect of given currency trade on the exchange rate that we find seems reasonable given that the NOK/DEM market is much smaller than the DEM/USD market, and that such periods we are studying here is reflected by higher uncertainty than the more normal period

²⁴The average NOK/USD rate over the period 1992-2000 was 7.4.

studied by Evans and Lyons. The lower numbers for 1997 and 1998 might be due to increased liquidity, less rigid monetary regimes, and possibly that external events were more important than changes in currency positions during these events.

5 Conclusion

We study the dynamics of speculative attacks. The problem of connecting currency crises to fundamentals has led to a discussion of possible manipulation of exchange rates, especially by large foreign players like hedge funds and other highly leveraged institutions. To analyze this we extend the model of Corsetti et al. (2004) by incorporating the costs and benefits of "early" versus "late" speculation by the large player. The model of Corsetti et al. (2004) predicts that large players may move early in an attack in order to induce small players to attack. It has, however, been argued by Tabellini (1994) and the IMF that large players move in the rear in currency crises in order to reap the benefit from higher interest rate differentials.

In our model the large players may choose to speculate early, incurring trading and interest rate costs, but also providing a signal to the small players, possibly inducing them to speculate. However, the large player may also choose to wait with the speculation, reaping the benefit of a positive interest rate differential while waiting, but also missing the opportunity to influence the smaller players, as well as risking being too late to join the attack. The smaller players will not speculate as early as the large player, as they cannot affect the behavior of other players. Nor will they want to incur the costs of continuous monitoring that is required to be able to join the speculation at a late stage.

The predictions of the model are the following: If there is no gain from speculating late, e.g. no interest rate differential to be gained, the large player will only speculate early. If there are gains from late speculation, the strategy of the large player depends on his signal of fundamentals. If fundamentals are very weak, implying that a successful attack is very likely, the large player will do all the speculation late as the gain from providing a signal to the small players is too small to cover the loss of the positive interest rate differential. If fundamentals are stronger, the large players may choose to speculate early with some of their funds. Unless the large player does all the speculation early, it will be the change in position of the large player, doing late speculation, that will be the one that triggers the attack.

The implications of the model are then tested using data on net positions of large (foreigners) and small (locals) players in Norway and Sweden for the following four speculative attacks during the 1990s: The ERM-attack in 1992 on the Norwegian krone; the 1997 appreciation crisis in Norway; and the August 1998 crisis following the Russian moratorium. In the latter case we can also compare with Sweden, using similar data, which also experienced speculative pressure but followed a different

strategy than the Central Bank of Norway. The sequence of trading is tested with Granger causality tests, while the triggering of the attacks is tested with regression analysis. We find that small players lead the large players in all cases except the 1998-crisis in Sweden. This is in line with the model since the Norwegian central bank used interest rates to defend the krone in all cases, while the Swedish central bank did not change its interest rate during the depreciation crisis in 1998. Hence, while there was a gain for the large players by delaying the attack in Norway, there was no gain by delaying the attack for large players in Sweden. The regression analysis shows that it was the large players that triggered the attack in all cases. We can not condition on the signal of the players in the regressions. The fact that all attacks were successful may, however, indicate that fundamentals in Norway in all three cases were in the region where large players preferred to move in the rear.

This paper is to the best of our knowledge the first that is able to study speculative attacks with data on the positions of both large (foreign) and small (local) players.

A Proof of Proposition 1

Proof. *i.* Note from (7) that for $t = 0$, $\frac{\partial E\pi}{\partial \lambda} > 0$ for all λ , as the other terms are always positive. Thus, for $t = 0$, $\lambda = L$ is optimal. By continuity of $\frac{\partial E\pi}{\partial \lambda}$, it follows that $\frac{\partial E\pi}{\partial \lambda} > 0$ for all λ , also for sufficiently small positive values of t . Let \underline{t} denote the supremum of all t for which $\frac{\partial E\pi}{\partial \lambda} > 0$ for all λ . It follows that $\lambda = L$ is optimal for all $t < \underline{t}$.

ii. Consider first the case where $q = 1$. If expected profits is negative for all $\lambda > 0$, then clearly $\lambda = 0$ is optimal. If there exists a $\lambda' > 0$ for which expected profits is positive, i.e. $E\pi(\lambda') = \left(G\left(\frac{1-t+\lambda'-y}{\tau}\right) - t \right) \lambda' > 0$, it follows that $\left(G\left(\frac{1-t+\lambda'-y}{\tau}\right) - t \right) > 0$. Thus, in this case we know that the derivative of the expected profits,

$$E\pi'(\lambda) = \left(G\left(\frac{1-t+\lambda-y}{\tau}\right) - t \right) + G'\left(\frac{1-t+\lambda-y}{\tau}\right) \frac{\lambda}{\tau} > 0 \quad \text{for all } \lambda \geq \lambda'$$

as both terms are strictly positive for $\lambda \geq \lambda'$. It follows that if it is possible to obtain positive expected profits by early speculation, then the large player wants to speculate by the maximum feasible amount L . Thus, it follows that for $q = 1$, the optimal λ is either zero or equal to L . By continuity of $E\pi$ it follows that for any given $\kappa > 0$, we can always choose a q sufficiently close to unity that the optimal λ is either within $[0, \kappa]$ or within $[L - \kappa, L]$. ■

B Proof of Proposition 2

We begin with a few definitions. The expected payoff given an early speculation λ^* is given by

$$\begin{aligned} E\pi^* &= L \cdot G\left(\frac{1-t+\lambda^*-y}{\tau}\right) - t\lambda^* = \\ &L \cdot G\left(g^{-1}\left(\frac{\tau t}{L}\right)\right) - t\left(y - (1-t) + \tau g^{-1}\left(\frac{\tau t}{L}\right)\right), \end{aligned} \quad (12)$$

where we use Equation (9) to substitute out for λ^* .

The expected payoff from not speculating early, yet entering at a late stage in the amount L (at zero cost), is

$$E\pi^0 = L \cdot G\left(\frac{1-t-y}{\tau}\right). \quad (13)$$

Proof. Consider first the interval $y < y^{Lo}$. In this interval we know that $\frac{\partial E\pi}{\partial \lambda} = L \cdot g\left(\frac{1-t+\lambda-y}{\tau}\right) \frac{1}{\tau} - t < 0$, as it follows from the derivation above that

1. $\frac{\partial E\pi}{\partial \lambda} = 0$ for $y = y^{Lo}$ and $\lambda = 0$.
2. $g'(\cdot) < 0$ for all $y < y^{Lo}$ (as $g(\cdot)$ is strictly decreasing for all positive arguments, and $\frac{1-t-y^{Lo}}{\tau} > 0$)

It follows that in this interval the optimal early speculation is zero, $\lambda = 0$ (as we do not allow negative speculation)

We then restrict attention to $y > y^{Lo}$. Define the difference between the profit under optimal early speculation and the profit with no early speculation $W(y) \equiv E\pi^* - E\pi^0$. Using (12) and (13), we obtain

$$W(y) = L \cdot G\left(g^{-1}\left(\frac{\tau t}{L}\right)\right) - t\left(y - (1-t) + \tau g^{-1}\left(\frac{\tau t}{L}\right)\right) - L \cdot G\left(\frac{1-t-y}{\tau}\right).$$

We have that $W(y^{Lo}) = 0$, as it is optimal to set the early speculation to zero for $y = y^{Lo}$. Furthermore, note that the derivative of W in the point $y = y^{Lo}$ is also zero, i.e.,

$$\begin{aligned} \frac{\partial W(y^{Lo})}{\partial y} &= -t + L \cdot g\left(\frac{1-t-y^{Lo}}{\tau}\right) \frac{1}{\tau} \\ &= -t + L \cdot g\left(\frac{1-t - (1-t - \tau g^{-1}(\frac{\tau t}{L}))}{\tau}\right) \frac{1}{\tau} = -t + L \frac{\tau t}{L} \frac{1}{\tau} = 0. \end{aligned}$$

Consider first the interval for y satisfying $\frac{1-t-y^{Lo}}{\tau} > \frac{1-t-y}{\tau} \geq 0$. It is clear that in this interval $\frac{\partial W}{\partial y} > 0$, since $g(\cdot)$ is strictly decreasing for positive arguments, implying that $g(\cdot)$ is greater for smaller arguments (i.e., for $y \geq y^{Lo}$). It follows that $W(y) > 0$ in this interval; this implies that it is profitable to speculate early in a quantity $\lambda^* > 0$ in this interval.

Then consider all y satisfying $\frac{1-t-y}{\tau} < 0$. We have

$$\frac{\partial^2 W}{\partial y^2} = -L \cdot g' \left(\frac{1-t-y}{\tau} \right) \frac{1}{\tau^2} < 0,$$

implying that W is strictly concave. As W clearly goes to minus infinity as y converges to infinity, there is a unique value y^{Hi} for which $W(y^{Hi}) = 0$. Thus, for $y > y^{Hi}$, then $W(y) < 0$, implying that early speculation is not profitable, i.e. set $\lambda = 0$. However, in the interval $y \in (y^{Lo}, y^{Hi})$, $W(y) > 0$, implying that early speculation is profitable, in the amount λ^* .

The derivative of the optimal early speculation λ^* with respect to speculation costs t is

$$\frac{\partial \lambda^*}{\partial t} = 1 + \tau g^{-1'} \left(\frac{\tau t}{L} \right) \frac{\tau}{L}$$

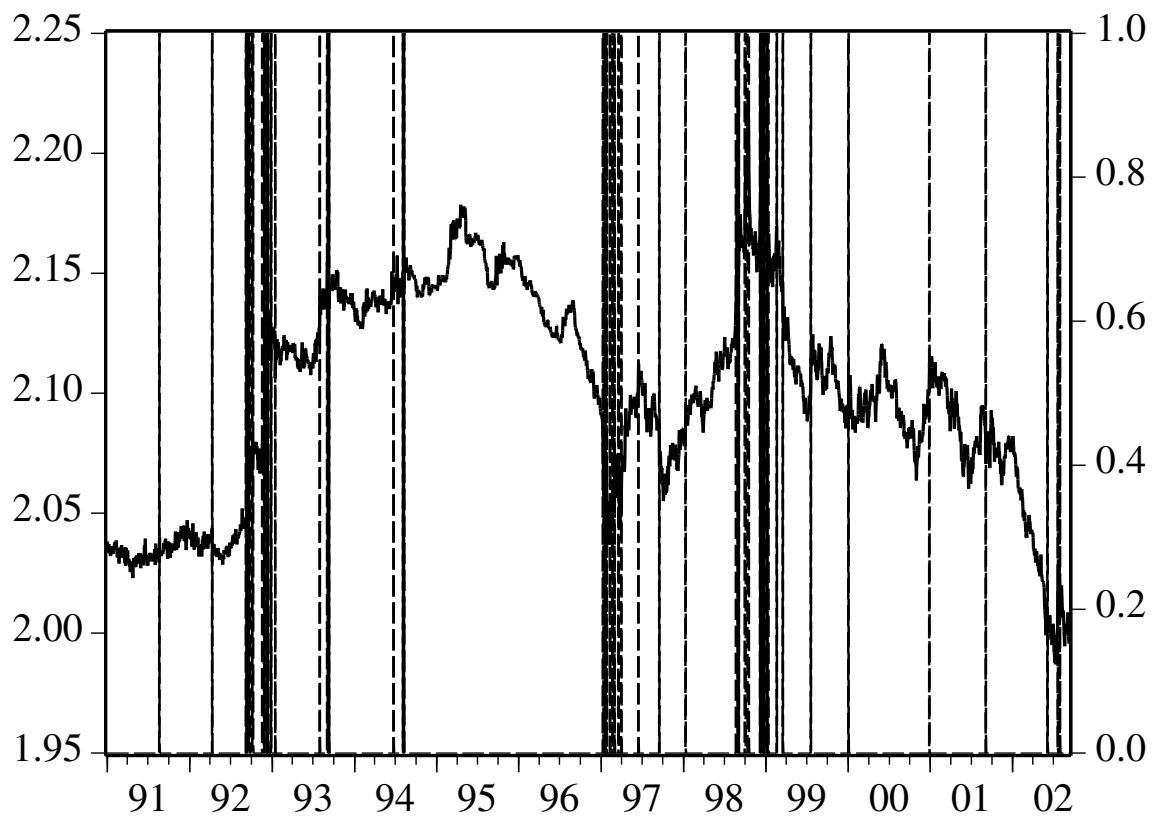
where the first term is positive and the second negative, implying that the sign is indeterminate (we have no restrictions ensuring whether the second term is greater or smaller than unity in absolute value). Correspondingly, the derivative of the optimal early speculation λ^* with respect to the noise of the large player's signal τ is

$$\frac{\partial \lambda^*}{\partial \tau} = g^{-1} \left(\frac{\tau t}{L} \right) + \tau g^{-1'} \left(\frac{\tau t}{L} \right) \frac{t}{L}$$

where again the first term is positive and the second negative, implying that the sign is indeterminate. ■

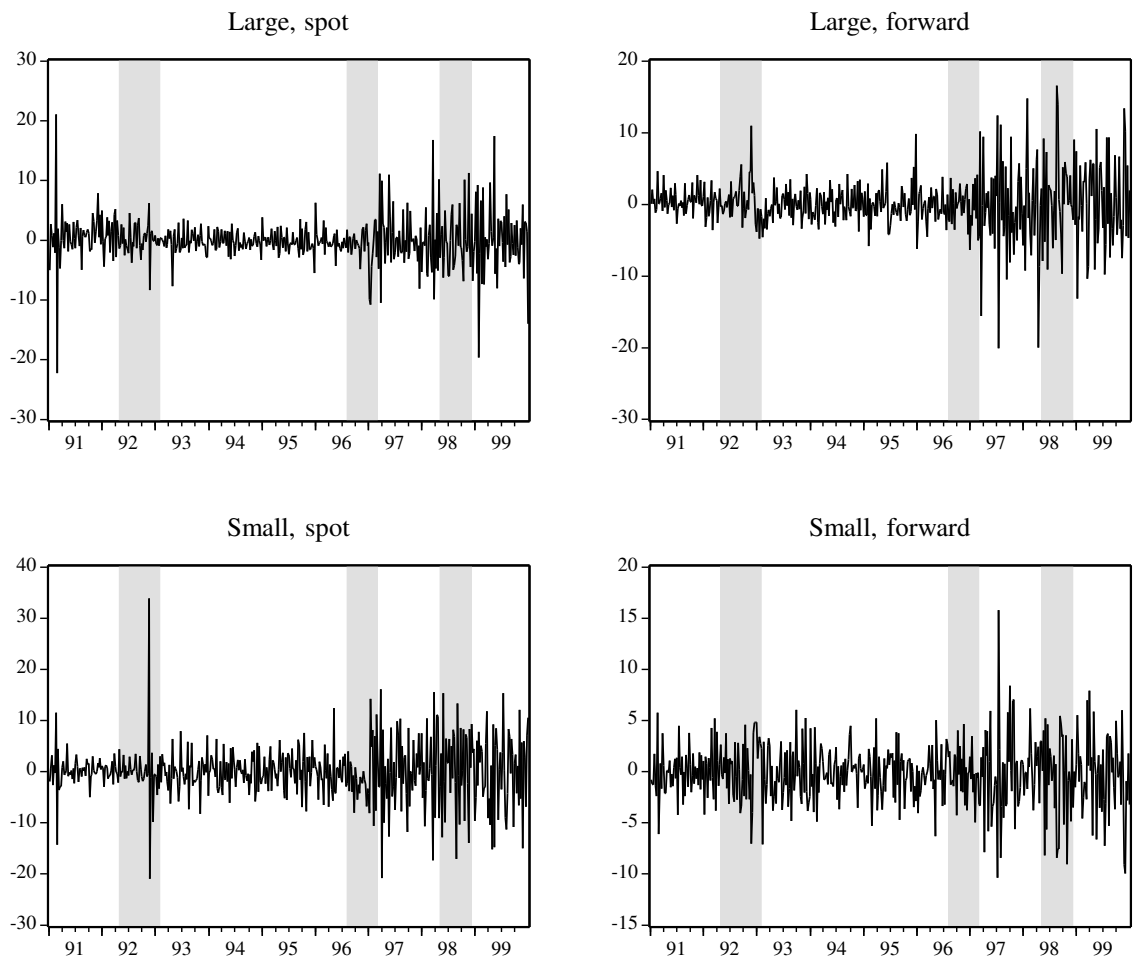
C Figures and Tables

Figure 9: Crisis index



Note: Log of NOK/EUR on left axis and crisis index on right axis. The crisis index is measured as $INDEX = \Delta \log NOK/EUR + \frac{\sigma_{\Delta \log NOK/EUR}}{\sigma_{\Delta \log INDEX}} \Delta \log INDEX$. Events are cases where the value of INDEX exceeds the mean of index ± 2 standard deviations of INDEX. The three crisis studied in this paper are the three periods with most high values on the index.

Figure 10: Flows: Norway



Note: Graphs show net purchases ("flows") of Large and Small players in spot and forward. Positive numbers indicate net purchases of foreign currency ("EUR"). Areas in grey indicate the crisis periods used in the empirical analysis.

Table 4: Descriptive statistics and correlations matrixes: Positions

Note: Descriptive statistics for positions (panel a), and correlation matrix between flows (panel b), over the whole sample, and each of the crisis-periods as defined in Table 1.

		Large		Small			
		Spot	Forward	Spot	Forward		
Whole sample	a)	Mean	-35.61	-23.16	-14.07	-11.69	
		Median	-30.89	-18.85	-10.56	-3.67	
		Maximum	6.22	21.38	33.87	19.36	
		Minimum	-88.15	-75.22	-62.92	-64.24	
		Std. Dev.	26.00	16.74	15.68	17.75	
		Observations	470	470	470	470	
	b)	Large spot	1				
		Large forward	0.817	1			
		Small spot	0.482	0.589	1		
		Small forward	0.781	0.556	0.394	1	
	1992	a)	Mean	-3.20	-3.36	2.18	4.34
			Median	-3.50	-4.54	0.33	5.40
			Maximum	6.22	21.38	33.87	19.36
			Minimum	-9.66	-16.77	-4.18	-11.33
Std. Dev.			3.39	12.38	6.67	6.01	
Observations			41	41	41	41	
b)		Large spot	1				
		Large forward	0.742	1			
		Small spot	0.610	0.523	1		
		Small forward	-0.186	-0.312	-0.532	1	
1997		a)	Mean	-47.88	-22.15	-26.06	-13.67
			Median	-43.13	-21.90	-30.11	-13.11
			Maximum	-35.14	-15.04	-0.36	-8.40
			Minimum	-70.63	-29.34	-58.10	-19.06
	Std. Dev.		11.58	3.20	16.32	2.61	
	Observations		30	30	30	30	
	b)	Large spot	1				
		Large forward	0.583	1			
		Small spot	0.610	0.188	1		
		Small forward	0.440	0.166	0.232	1	
	1998	a)	Mean	-73.38	-56.75	-24.10	-27.06
			Median	-74.11	-58.82	-24.46	-25.69
			Maximum	-63.34	-35.07	-9.09	-15.38
			Minimum	-84.40	-75.22	-45.03	-43.04
Std. Dev.			5.44	13.62	9.23	8.81	
Observations			31	31	31	31	
b)		Large spot	1				
		Large forward	-0.136	1			
		Small spot	-0.603	0.510	1		
		Small forward	0.130	-0.926	-0.581	1	

Table 5: Descriptive statistics and correlations matrixes. Flows

Note: Descriptive statistics for flows (panel a), and correlation matrix between flows (panel b), over the whole sample, and each of the crisis-periods as defined in Table. Numbers in bold indicate the variables discussed in Section 3. 1.

		Large		Small				
		Spot	Forward	Spot	Forward			
Whole sample	a)	Mean	-0.04	0.05	0.03	-0.16		
		Median	-0.28	-0.07	0.04	-0.06		
		Maximum	21.05	16.58	33.87	15.80		
		Minimum	-22.25	-20.06	-20.97	-10.38		
		Std. Dev.	3.78	4.03	5.45	3.05		
		Observations	469	469	469	469		
		b)	Large spot	1				
	Large forward		-0.128	1				
	Small spot		-0.254	-0.308	1			
	Small forward		0.098	-0.336	-0.090	1		
	1992		a)	Mean	0.09	0.49	0.18	0.40
				Median	-0.13	-0.17	-0.13	0.73
				Maximum	6.22	10.95	33.87	4.84
		Minimum		-8.37	-4.77	-20.97	-7.05	
Std. Dev.		2.46		2.79	6.76	2.90		
Observations		41		41	41	41		
b)		Large spot		1				
	Large forward	-0.071	1					
	Small spot	0.630	-0.094	1				
	Small forward	0.084	-0.601	0.105	1			
	1997	a)	Mean	-0.98	-0.25	-0.97	-0.16	
Median			-0.67	0.10	-1.96	-0.19		
Maximum			3.47	4.14	14.23	4.65		
Minimum			-10.81	-6.38	-10.61	-4.95		
Std. Dev.			3.27	2.72	5.71	2.32		
Observations			30	30	30	30		
b)			Large spot	1				
		Large forward	0.165	1				
		Small spot	-0.371	-0.372	1			
		Small forward	-0.130	-0.395	0.214	1		
		1998	a)	Mean	-0.21	1.07	0.54	-0.56
				Median	-0.94	0.50	0.80	0.06
				Maximum	11.25	16.58	15.37	5.45
Minimum				-6.87	-9.70	-17.08	-9.04	
Std. Dev.	4.58			5.93	8.07	4.49		
Observations	31			31	31	31		
b)	Large spot			1				
	Large forward		0.076	1				
	Small spot		-0.597	-0.523	1			
	Small forward		0.055	-0.372	-0.211	1		

Table 6: Granger causality test on all flows: Norway, 1992, 1997 and 1998

Note: Difference of net-position (flows), both spot and forward, of large and small players estimated within a system on lagged flows of large and small players, with dummies for pre-crisis period and crisis period. p -values in parenthesis. All equations use one lag, except in 1998 where we use two lags of small's spot trading in the large-specification during the crisis-period.

		1992								
		Small spot		Small forward		Large spot		Large forward		
Crisis	Constant	0.359	(0.18)	0.339	(0.09)	0.649	(0.01)	0.284	(0.14)	
	Small spot	-0.631	(0.00)	-0.153	(0.04)	-0.241	(0.00)	0.186	(0.01)	
	Small forward	-0.505	(0.09)	0.009	(0.97)	0.009	(0.95)	-0.159	(0.16)	
	Large spot	0.968	(0.17)	0.185	(0.49)	0.196	(0.23)	0.113	(0.66)	
Pre-crisis	Large forward	-0.197	(0.67)	-0.363	(0.05)	-0.102	(0.45)	0.273	(0.10)	
	Small spot	0.031	(0.78)	0.240	(0.24)	0.295	(0.21)	-0.365	(0.00)	
	Small forward	0.117	(0.25)	-0.437	(0.00)	0.022	(0.90)	-0.150	(0.14)	
	Large spot	-0.140	(0.12)	-0.040	(0.77)	-0.160	(0.34)	0.331	(0.00)	
		Large forward	-0.003	(0.99)	0.191	(0.20)	-0.004	(0.99)	-0.267	(0.01)
adj.R ²		0.19		0.15		0.06		0.26		
DW		2.29		2.14		2.03		2.19		
		1997								
		Small spot		Small forward		Large spot		Large forward		
Crisis	Constant	-1.195	(0.03)	-0.342	(0.25)	-0.320	(0.12)	0.056	(0.84)	
	Small spot	-0.328	(0.00)	-0.130	(0.02)	0.241	(0.01)	0.276	(0.00)	
	Small forward	-0.188	(0.51)	-0.446	(0.02)	0.060	(0.78)	0.086	(0.47)	
	Large spot	-0.771	(0.12)	-0.107	(0.06)	0.545	(0.00)	0.101	(0.13)	
Pre-crisis	Large forward	0.543	(0.15)	-0.254	(0.06)	0.538	(0.03)	-0.243	(0.00)	
	Small spot	-0.425	(0.00)	0.209	(0.11)	0.035	(0.55)	-0.082	(0.49)	
	Small forward	-0.519	(0.01)	-0.013	(0.92)	-0.218	(0.03)	-0.061	(0.68)	
	Large spot	-0.199	(0.29)	0.090	(0.68)	-0.266	(0.16)	-0.297	(0.32)	
		Large forward	-0.113	(0.46)	0.067	(0.45)	-0.015	(0.93)	-0.373	(0.12)
adj.R ²		0.14		0.10		0.29		0.13		
DW		1.86		1.95		1.84		1.89		
		1998								
		Small spot		Small forward		Large spot		Large forward		
Crisis	Constant	0.995	(0.12)	-0.079	(0.87)	-0.582	(0.18)	-0.115	(0.86)	
	Small spot	-0.513	(0.03)	0.093	(0.48)	-0.013	(0.96)	0.312	(0.02)	
	Small forward	-0.486	(0.09)	-0.257	(0.22)	0.136	(0.64)	-0.396	(0.35)	
	Large spot	0.127	(0.67)	0.011	(0.96)	-0.083	(0.66)	0.056	(0.71)	
Pre-crisis	Large forward	-0.289	(0.53)	-0.371	(0.00)	0.067	(0.84)	-0.073	(0.73)	
	Small spot	0.118	(0.53)	-0.119	(0.37)	-0.381	(0.00)	0.187	(0.52)	
	Small forward	0.159	(0.58)	-0.047	(0.67)	-0.247	(0.22)	0.036	(0.90)	
	Large spot	1.075	(0.00)	-0.012	(0.95)	-0.897	(0.00)	0.125	(0.66)	
		Large forward	0.353	(0.00)	-0.114	(0.37)	-0.178	(0.07)	-0.008	(0.95)
		Small spot, 2nd lag						0.412	(0.03)	
adj.R ²		0.22		0.11		0.14		-0.01		
DW		2.20		1.84		1.99		1.99		

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