



WP/19/19

IMF Working Paper

Financial Dollarization of Households and Firms: Does it Differ?

by Juan-Sebastian Corrales and Patrick A. Imam

***IMF Working Papers* describe research in progress by the author(s) and are published to elicit comments and to encourage debate.** The views expressed in IMF Working Papers are those of the author(s) and do not necessarily represent the views of the IMF, its Executive Board, or IMF management.

I N T E R N A T I O N A L M O N E T A R Y F U N D

IMF Working Paper

African Department

Financial Dollarization of Households and Firms: Does It Differ?**Prepared by Juan-Sebastian Corrales and Patrick A. Imam¹**

Authorized for distribution by Gene Leon

January 2019

IMF Working Papers describe research in progress by the author(s) and are published to elicit comments and to encourage debate. The views expressed in IMF Working Papers are those of the author(s) and do not necessarily represent the views of the IMF, its Executive Board, or IMF management.

Abstract Using a newly compiled and extended database from International Financial Statistics, and applying different panel-regression techniques, this paper documents the evolution of households' and firms' dollarization over the past decade. We assess the macroeconomic determinants of dollarization for households and firms and explore differences between high and low-income countries. We find that households' and firms' dollarization in loans and deposits are weakly explained by the currency substitution model, except in low income countries, where inflation plays a significant role. Instead, market development variables such as financial deepening, access to external debt and FX finance as well as other market considerations are key to explain the dynamics of deposits and loans dollarization, regardless of the level of income. These factors can account for a significant fraction of the dollarization, but using a variance decomposition model, there is evidence that a non-negligible portion has yet to be explained. This suggests that there are key determinants for household and firm dollarization that are not fully captured by traditional macroeconomic explanatory variables.

JEL Classification Numbers: E52, F31, E4, F33

Keywords: Dollarization, Household, Firm, Financial deepening

Author's E-Mail Address: jcorrales@fedesarrollo.org.co ; pimam@imf.org

¹ We would like to thank seminar participants, and Gene Leon, Leandro Medina, Kangni Kpodar, Rodolfo Maino, Mahvash Qureshi, Ialy Rasoamanana, Axel Schimmelpfennig, Amadou Sy and Etienne Yehoue for useful comments. The usual disclaimer applies.

Contents	Page
I. Introduction _____	<u>4</u>
II. Literature Review _____	<u>5</u>
III. Dynamics of Households and Firms' Dollarization _____	<u>10</u>
IV. Determinants of Households and Firms' Dollarization _____	<u>17</u>
V. Contributions to dollarization _____	<u>31</u>
VI. Conclusions and policy implications _____	<u>34</u>
 FIGURES	
1. Private Sector Financial Dollarization _____	<u>12</u>
2. Correlation between Loans and Deposits Dollarization. Average 2001-2016 _____	<u>14</u>
3. Correlations: Firms Dollarization and Macroeconomic Variables. Avg. 2001-16 _____	<u>15</u>
4. Correlations: Households Dollarization and Macroeconomic Variables. Avg. _____	<u>16</u>
5. Firms Dollarization. Pooled OLS. Contribution by Determinants _____	<u>32</u>
6. Households Dollarization. Pooled OLS. Contribution by Determinants _____	<u>33</u>
 TABLES	
1. Financial Sector: Loans and Deposits by Sector for all countries _____	<u>11</u>
2. Financial Dollarization by Level of Income*. 2001-2016 _____	<u>13</u>
3. Deposits Dollarization: Firms _____	<u>21</u>
4. Loans Dollarization: Firms _____	<u>22</u>
5. Deposits Dollarization: Households _____	<u>24</u>
6. Loans Dollarization: Households _____	<u>25</u>
7. Deposits Dollarization: Firms. High versus Low Income Countries _____	<u>27</u>
8. Deposits Dollarization: Households. High versus Low Income Countries _____	<u>28</u>
9. Loans Dollarization: Firms. High versus Low Income Countries _____	<u>30</u>
10. Loan Dollarization: Households. High versus Low Income Countries _____	<u>31</u>
 APPENDIX	
Appendix A _____	<u>36</u>
APPENDIX TABLES	
A1.a. Effective Regression Sample for Households Deposits Dollarization _____	<u>35</u>
A1.b. Effective Regression Sample for Households Loans Dollarization _____	<u>36</u>
A1.c. Effective Regression Sample for Firms Deposits Dollarization _____	<u>37</u>
A1.d. Effective Regression Sample for Firms Loans Dollarization _____	<u>38</u>
A2. Sources of Variables _____	<u>39</u>
A3. Summary Statistics of Variables _____	<u>40</u>
A4. Independent Variables Correlation Matrix _____	<u>40</u>
A5. Collinearity Analysis: Variance Inflation Factors and Condition Number _____	<u>41</u>
 REFERENCES	
References _____	<u>43</u>