

Executive Summary of the article: “*Oil Price Risk and Financial Contagion*” by Guesmi, K., Abid, I., Créti, A., Chevallier, J.

The literature by Bekaert, Harvey & Ng (2005, *J Business*) typically features several sources of risks in international financial markets, related to regional or world market risks, in addition to exchange rate dynamics. This paper extends the conceptual framework to include another source of risk coined “oil price risk”. This latter exposure to contagion stems from trades in physical goods incorporating oil itself, or from financial trades seeking high returns associated with “paper” oil. As such, the paper embraces a more complete approach of risks on financial markets, extended to the up- vs. downside risks attached to commodities.

In essence, the paper features the full-fledged Bekaert et al. (2005)’s model, by resorting to a three-factor model with time-varying loadings (the U.S. market return, the WTI oil price and the regional equity portfolio return). Monthly OECD stock market data are collected over the period from January 1991 to April 2015. The total variance is decomposed for each source of risk (including oil price risk). Contagion tests are formally implemented contrasting stable vs. turmoil times. Dynamic conditional correlations are derived for the beta parameters, with exact computation of the multivariate matrices.

Oil price risk is shown to be a factor as important as contagion – defined classically since Forbes & Rigobon (2002, *J Finance*) as excess correlation that is not explained by fundamental factors. The sensitivity of each region (North America, European Market Union, Non-European Market Union, Asia-Pacific) to oil prices is depicted in the paper. This view reveals strong interconnections with the USA, taken as a proxy of world risks. Such “oil price risks” should therefore be explicitly accounted

for by individual investors, macro-prudential policies, exchange-traded, hedge- and quant-funds trades.