Discussion of Pierpaolo Benigno's "The International Supply of Liquidity"

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Introduction

- The global currency is a global public good managed by one country

  "*The dollar is our currency, but it's your problem.*"

  (John Connally)

- This paper focuses on one attribute of a global currency, *liquidity*
  - large literature where public provision/management of liquidity is motivated by various frictions (Holmstrom and Tirole, 1998, 2002 and many others)
- This paper focuses on a friction that distorts the supply of liquidity, the issuing country's *market power*
  - the US manages the dollar to maximize US welfare
  - this leads to mercantilist manipulation of dollar liquidity premium

Model

H

$V(q+\phi d)$

F

$V(q^*+\phi^* d^*)$

q and q*: H government debt

d and d*: bank deposits backed by home government debt

- Very elegant model yielding many results
- Global welfare maximization implies that cost of holding liquidity is equal to cost of producing liquidity
  - implies satiation of demand for public liquidity (Friedman rule)
- But a self-oriented hegemon extracts a monopolistic rent from foreigners

A dollar rent?

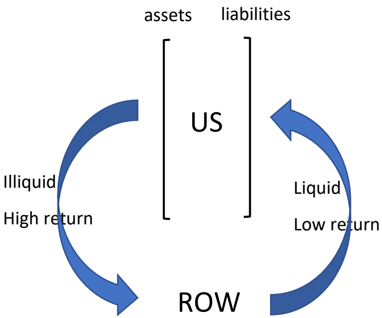
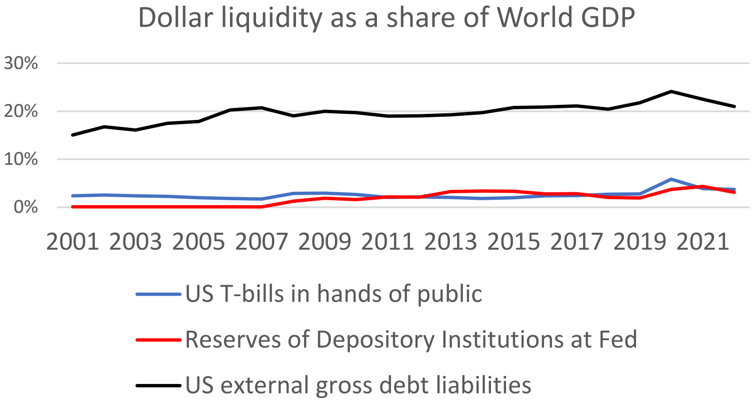


Figure: US as "banker of the world" (Gourinchas and Rey, 2007)

- If US suppliers of liquidity are competitive and unconstrained, supply should be efficient
- If US suppliers are financially constrained, the supply could be too low, allowing the US to extract a rent (not a monopoly rent, though)

A dollar rent?



A dollar rent?

- US Treasury bills: US fiscal policy does not seem to maximize the rent from the convenience yield
  - limited US fiscal capacity could lead to undersupply of liquidity (fiscal Triffin dilemma), but that's a different story
- Fed liquidity was provided pretty generously to US *and non-US* systemic banks in the global financial crisis
  - it would have been both difficult and not desirable to discriminate between US and foreign banks

A dollar rent?

- US Fed is arguably more stingy in its supply of dollar liquidity to foreign central banks
  - Fed swap lines are a tiny fraction of global dollar reserves ($6.5trn in 2022)
- Large demand for dollar reserves in emerging markets is in part due to lack of insurance
- The Fed does not contribute more to the GFSNs in part because of its domestic mandate (more, even anecdotal evidence on this in the paper would be nice)
  - the US is getting a rent from not providing insurance

Conclusion

- There might well be a dollar rent (exorbitant privilege)
- How strategic is the US in extracting this rent?
- Not very much apparently
    - to a large extent the rent seems to be the collateral benefit (for the US) of frictions that generate demand for, and restrict supply of global liquidity
- But the dollar rent is also in part due to the US failure to render assistance

Conclusion

THANK YOU!