

Central Banker to the World: Foreign Reserve Management and U.S. Money Market Liquidity

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Summary

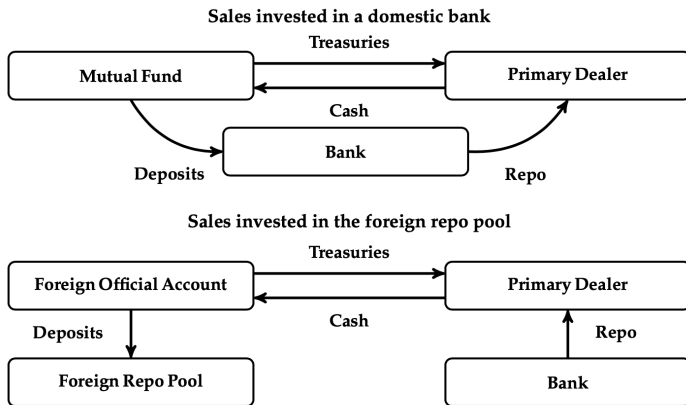
Can foreign central banks affect the U.S. money market liquidity?

- Yes, if they sell UST and enter into a Fed reverse-repo facility.

Summary

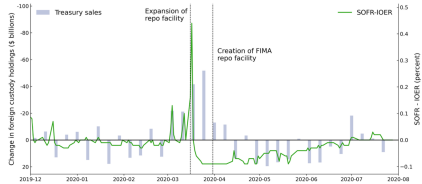
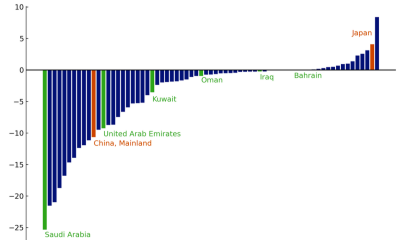
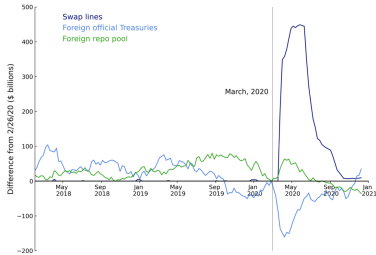
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Summary

- Key focus: oil exporters with dollar pegs.



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Build a simple two period two country model.

- Shocks to net export drive the incentive to do portfolio rebalancing.
- Inability to sell UST in some state of the world gives precautionary motive to prepare reserves ex ante.
- Deposit requirements are frictions justifying dollar liquidity.

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Empirical evidence is consistent with the model predictions.

- Use oil volatility as instrument for the interest rate differential.
- Interest rate differential predicts spread and UST sales.

Comment 1

General comments

- Interesting paper
- A nice contribution to the literature

Key insights

- Foreign central bank reserve managements can affect US domestic liquidity.

The results largely make sense.

Congratulations on the JIE publication!

Comment 2

- The mechanism is more general than “the oil exporter CB manages FX”.
- When “anyone” sells UST and moves dollar outside the domestic system.
- Foreign CBs are more likely to do so (?).
 - ▶ Is it due to existence of foreign reverse repo pool?
 - ▶ Reasons other than oil/terms-of-trade shocks (China).
 - ▶ Further cross-sectional test will be helpful.
- Is there a general approach to estimate the size of this channel?
 - ▶ Run a VAR with foreign UST sale and foreign reverse repo pool.

Comment 3

Policy implications

- In general, does this channel have welfare implication?
- I wonder whether this provides an additional way to think about the spillover and spill-back effects for Fed policy.
- Quantitatively, how large is this additional channel?

Very nice paper! Enjoyed reading it.