FEDERAL RESERVE BANK *of* NEW YORK

International Roles of Currencies and Financial Market Drivers

Panel remarks by Linda Goldberg

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Views expressed are those of the author and do not necessarily reflect the position of the Federal Reserve Bank of New York or the Federal Reserve System.

Overview of remarks

Key roles of international currencies

Traditional determinants of international currency status

Additional considerations:

- Focus on what conditions lead currencies/ assets to provide liquidity exactly when it is needed.

Key roles of the currencies

1) Anchor currency for exchange rate systems worldwide

2) International reserve currency

3) Currency for denominating international financial transactions

    (extra role for as benchmark in setting rates/terms)

4) Currency for denominating and settling international trade

5) International cash holdings

Traditional determinants

Historically, discussions of key international currencies within the international monetary system have focused on

- country size,
- economic stability,
- openness to trade and capital flows internationally,
- the strength of country institutions.
- Inertia also plays a role.

Post-crisis lessons for international currencies

What additional considerations support currencies/assets being able to provide liquidity exactly when needed?

- sovereign bond market liquidity,
- foreign exchange market function,
- financial stability reforms,
- fiscal space.

"New thinking on reserve currency status: Why is financial stability essential for key currencies in the international monetary system?"

Linda Goldberg, Signe Krogstrup, John Lipsky, Hélène Rey, VOX column July 2014 http://www.voxeu.org/article/new-thinking-reserve-currency-status

International reserve status and safe assets

Delinking sovereign and banking crises through financial stability reforms: the logic

- For a currency to have international reserve status, related assets must be useable with minimal transaction price impact and maintained value in times of stress.
- If the risk of banking stress or failures is substantial, and the potential fiscal consequences strong, the safety of sovereign assets is compromised exactly at times of financial stress, through contingent fiscal liabilities related to systemic banking crises.
- Monies with reserve currency status need low probabilities of twin sovereign and financial crises.
- Financial stability reforms, alongside fiscal prudence, can help protect the safety and liquidity of sovereign assets.

Thank you!