Peterson Institute for International Economics

**Decentering the dollar: A conversation**

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**[00:05:24.40] - Adam Posen**

Hello everyone and welcome back to the Peterson Institute for International Economics. I'm Adam Posen, the Institute's president, and we are Coming towards the end of our chock-full of content Spring Meetings week, we have created a bit of a— I don't want to say tradition, but recurring theme. Maury Obstfeld and I have been holding events here every 6 months or so under the heading of Decentering the Dollar. While the phrase hasn't caught on, we still think it's the right phrase. It's not about a collapse of the dollar. It's not about is there appreciation or depreciation of the dollar. It's about whether the fundamental changes in geopolitics, economics, technology, and frankly, the role of the Federal Reserve and other central banks change the role of the dollar in a meaningful way. And so in some sense, this becomes— more pressing if you focus on so-called global imbalances, as this week's official meetings have done. And in another sense, if you see through global imbalances, this is actually one of the more important issues underlying that. Uh, today, however, we're not going to be presenting new research, meaning of course Maury's new research or that of colleagues of ours.

**[00:06:57.00]**

We have plenty of that. But we're taking advantage of a new member of the Peterson Institute community. This is the last time I'll repeat it, but we're delighted to welcome Dr. Klaus Nolte as a distinguished visiting fellow at the Peterson Institute. Previous distinguished visiting fellows include Robert Zellick, Mari Pangestu, who's with us today, Alan Wolfe before he decided he really wanted to work for a living and converted to a senior fellow. And so on. Klaas is, of course, has stepped down last July as president of de Nederlandsche Bank, the Dutch Central Bank, and as chair of the Financial Stability Board. He also served as a member of the ECB's Governing Council, General Council, the European Systemic Risk Board, the IMF's Board of Governors, and the Board of Directors of the BIS. Prior to assuming the presidency of the Nederlandische Bank in 2011, he had a substantial career in various Dutch official positions, as well as a brief stay at the IMF. He has always been frank by official standards, as well as being very substantive-based, and we're delighted to give him an additional venue to keep his foot in Washington and his voice amplified in these matters.

**[00:08:26.38]**

As already mentioned, joining us for this conversation will be Maury Obstfeld, who is the Siegfried Bergstein Senior Fellow at the Peterson Institute. He's been associated with the Institute since February 2019. He's also the Class of 1958 Professor of Economics Emeritus at UC Berkeley, where he taught for quite a while and previously had taught at Harvard, UPenn, and Columbia. Of course, uh, Maury previously served as economic counselor and director of the research department at the IMF, and prior to that, a member of President Obama's Council of Economic Advisers. He's been an honorary advisor to the Bank of Japan's Institute of Monetary and Economic Studies and To this very day, anything that starts with a G has had him as a consultant at some point or another. And we're glad that the e— thus, those of us who start with a P can also get the benefit of his wisdom. So joking and intros aside, I'd like to invite my colleagues up to the podium. We'll stick Klaus in the middle. He's tallest anyway. Start an open discussion, and then, uh, we're glad to have thousands, we hope, joining us online, but also a distinguished in-person audience.

**[00:09:49.04]**

We'll open to questions at some point. Please. So I guess, Klaus, I'll start with getting your views on the obvious broad question, however you want to take it. There seems like there's been a lot of changes around the US economic and specifically monetary macroeconomic regime. There seems to still be no shortage of people buying and holding dollar assets. Do these changes matter? Are they things you're concerned about, or are they things that are epiphenomenal? How do you see the role of the dollar at this point?

**[00:10:48.32] - Klaas Knot**

Well, thank you, Adam, for the questions. But first of all, I also wanted to thank you for the opportunity to join actually the Peterson. It's always good to realize that there is still a place in Washington where the existence of global public goods is acknowledged and where the importance of inter-coordination, international coordination to provide these goods as effectively and as efficiently as possible is underlined. So it is also my honor and pleasure to join the Peterson here.

**[00:11:20.02] - Adam Posen**

Okay.

**[00:11:20.55] - Klaas Knot**

I mean, given the still overwhelming dominance of the US dollar as an international reserve currency, obviously, Everything that happens in the US matters. So the short answer to your question is absolutely, it matters. But the question, I guess, is in what way does it matter? Is it something that is about to collapse, or is it going to lead to sudden changes, or is it more— and that I'm probably of the view of the latter— that there is a potential for a gradual erosion of a status that, of course, has been very carefully built up after World War II. And that has to do with the fact that on the side of the US primarily, there is a bit more reluctance to deliver the kinds of goods that a global hegemon that delivers an international reserve currency would normally provide to the international community. Think about free trade, but also think about security assurances to other parts in the world. And if you look at the criteria that are historically been important for sort of being the provider of an international reserve currency. One of them is, of course, the international rule of law, that you sort of respect a rules-based order, that there is legal certainty about issues, etc.

**[00:12:42.13]**

And I guess there have been some developments here in the US that have put that into question, issues around favoritism, issues around, I think, decline of legal certainty. Another important factor is, of course, that you have an independent central bank that is fully committed to monetary and price stability. On that score, I'm probably a little bit less concerned today than I would have been, let's say, half a year ago, because I do think that also under the new leadership, the Federal Reserve will be led by somebody who is in many, many ways, I think, a central banker by, let's say, education and by training, etc. So, to some extent, I think it could have been worse, let me put it like this. And while, of course, there can always be differences around how easy, how tight monetary policy should be, etc., but I don't think that the Fed sort of is— the commitment of the Fed to monetary and price stability and financial stability will be put in question. So, in that sense, I'm a little bit less concerned now than I was a long time ago. But there are many things that can still continue to still go for the US.

**[00:14:06.28]**

I mean, the returns on investment to be had in the US are still higher than in many, many other places of the world. We also know that there's a lot of path dependency of an international reserve currency. It's You can compare it to the lingua franca. We all speak English. Even after the Brits left the EU, we continue to speak English, right?

**[00:14:25.41] - Maurice Obstfeld**

Right.

**[00:14:27.05] - Klaas Knot**

Well, that's because everybody speaks English. Well, there is, I think, the same reasoning also in the international usage of the dollar. So there might be some changes. And I will also say that I see some potential for the euro, which is the runner-up, which is the number 2, to increase its footprint.

**[00:14:45.01] - Adam Posen**

Yeah, let's come back to that.

**[00:14:46.41] - Klaas Knot**

But it will be a gradual process, and don't expect any revolution here. It will be rather evolutionary.

**[00:14:53.44] - Adam Posen**

That's great, Klaas, and obviously we're delighted to have you in the globalism versus nationalism team that we're pursuing. Maury, you have pretty bluntly been talking about the impact of a number of these issues on the usage, role, stability of the dollar, including last summer you gave the Crockett Lecture BIS and spoke about these things. What's your latest update and latest riposte to those who tell you, "See, no problem.

**[00:15:29.52] - Maurice Obstfeld**

What are you worried about?" Well, I, you know, worry, um, I think there are a number of aspects of worry. General discussion of, you know, will people stop using the dollar? Will it be, you know, supplanted, decentered? We can talk about that. And, you know, I think clearly nothing's going to happen quickly or soon. I think there is a lot of energy in the system to move in different directions and try to insulate from the policy volatility that is coming out of the US, not just in economic policy, but in strategic policy. But there's also the possibility of specific events that could be extremely disruptive with not the dollar at the center, then US Treasuries at the center. Um, you know, my general view is that there, there are four factors that underpin, um, the dollar status. Um, there's, uh, you know, the, the, um, security umbrella that the US has provided to the world since World War II, which it's now called into question or at least made conditional on some sort of reciprocity. There's the rule of law, the institutions, the courts, which

Klaus mentioned. There's macro policy where I have very, very big concerns about both fiscal and monetary policy.

**[00:17:30.05]**

And then, um, uh, Klaas mentioned path dependence. You know, I would refer to network externalities. Um, there's a huge international financial network built on dollar's role, on the depth and breadth of U.S. financial markets, their liquidity. Um, it's very hard to, to disengage from that when everyone else is participating in that. But, you know, the point I would make is that that very advantage of the dollar is also a source of vulnerability for those who are dependent on it. And I think they are becoming more aware of the, uh, the dangers of being exposed to possible, uh, we can call it, you know, predatory actions by the US as it pursues its agenda. So, you know, the signs of decoupling are very small at the moment, but I think they're definitely there. If you look at smaller Asian economies, there's an active project to pursue, you know, more bilateral trading of their currencies. Malaysia, Thailand, China, Singapore have linked their instant payment systems so that it's very easy to make at least retail payments across borders without going through the dollar. Countries there are gradually invoicing less in dollars. Now that means instead of invoicing 90% of your exports to dollars, you're invoicing 80% of your dollars.

**[00:19:12.22]**

But it's a start, and it also reflects some discomfort with the way the dollar functions. So if you, you know, if you invoice your exports in dollars, that's actually a constraint on the effectiveness of the exchange rate as an adjustment mechanism, which is one of the advantages of a flexible exchange rate system. And maybe it's worth it to give that up to, you know, engage in dominant currency pricing if you benefit from network externalities. But if at the same time you're facing vulnerabilities from that, and there are incentives to move away and to say, well, you know, we can actually have better macro performance, you know, at some cost, uh, if we move in that direction. And, uh, you know, again, it's very hard for, for one country to do this, but you have a number of countries in that region that are cooperating and recognize a common problem and that are moving, you know, at least on the margins to address it. So, you know, is the dollar going to go away as the main global currency anytime soon? I think not, but I think there are a lot of stresses in the system.

**[00:20:19.02]**

And, you know, we can talk more about macro policy. I'm sure we might.

**[00:20:22.04] - Adam Posen**

We will. There are so many directions to take this. I just want to flag one thing Maury said, and I was on a panel on international global whatever imbalances at the IMF the other day, and Kristin Forbes was on the panel, and she was, I think rightly, pointing out that there's a distinction between people continuing to use the dollar for commercial purposes or to invest in private sector assets versus being quite as long Treasuries as they once were. And that's a distinction worth making. So before we turn to Europe and other alternatives, Klaas, I mean, without stereotyping you as a Northern European, obviously you've thought a lot about the interactions between fiscal stability and currency stability. And so for, as we think about the US being on, a path of pretty irresponsible, in my view, fiscal policy through the last several years. Where does that start to play in to the currency role and the ability of the US to get financing? Or again, is this separate? It goes on forever.

**[00:21:44.55] - Klaas Knot**

Well, we could do a poll here in the room at what sort of debt-to-GDP level you think No, I think that's impossible to say because I think it needs to be assessed, of course, in the broader context. You also have to look at private saving behavior. Now, the worrying part, obviously, which is there for the US and to some extent also for the UK, is not that there is not only high public indebtedness, but there is also a private savings deficit in the sense of a persistent current account deficit. So that means you are to some extent at the mercy of international capital markets to finance your public outlays. And so the question then is, at what point in time will international capital markets say enough is enough, or at least start charging higher and higher yields, which will then lead to a self-fulfilling negative dynamics toward fiscal unsustainability. I think that, I mean, it's almost impossible to say what is sort of the trigger level. What I can say is that if you look at the amount of fiscal consolidation that would be needed to just stabilize debt levels, these are staggering numbers. I think at Bruegel there was a study for the 27 EU, for the UK, and for the US.

**[00:23:12.56]**

And out of the sample of 29 countries, and yes, UK and US were part of it, 13 countries needed to do more than 3%age points adjustment in the structural primary. 6 countries needed to do more than 5%age points of adjustment in the structural primary deficit. And among these 6 countries were US, UK, France, Poland and two other countries. So, and this is merely to stabilize debt levels. So it's not just a question about levels, it's also the dynamic to hold the current dynamics already requires significant adjustment. If we combine that with the political winds in many of these countries that I mentioned, and by the way, in all the countries, then I think the enormity of the challenge is there. And I think there is still a disconnect between the political discourse in many of these countries and the reality of these numbers.

**[00:24:16.03] - Adam Posen**

Obviously, our cousins at the Peterson Foundation are following this with even more fervor than we are. But Maury, let me push you a little bit on this. So, As Klaus points out, and as our colleagues at Bruegel have done the analysis and others have too, you know, it's not just the US. And if anything, increasing defense spending, increasing spending to deal with demographic shifts, and one would like to have thought increasing spending to improve climate adaptation, all seem to be in the cards for the high-income economies simultaneously. So is this neutral for currencies if everybody goes bankrupt at once, or are there differential effects if we're all starting to run 10% of GDP deficits, or just how should we think about this? Is it always a relative game or does the absolute— numbers matter.

**[00:25:26.11] - Maurice Obstfeld**

Um, you know, obviously, uh, in the aftermath of COVID especially public debts, private debts, you know, around the world are very high. We've seen a rise in real interest rates since the, uh, the pre-COVID period. Um, this puts stress on all debtors, uh, if real interest rates rise further, this is going to be problematic for everyone. How this pans out will really depend on the institutional capacity of different countries to deal with funding problems that might arise. And, you know, that allows me to pivot back to the US on this. I think the US, you know, institutionally is not well positioned. And, you know, for one thing, in addition to the debt-to-GDP ratio, we have severely underfunded Social Security and Medicare systems, which are heading for crisis with no even discussion of how to deal with these. You know, for all the talk in the 1980s about the Reagan deficits. Reagan confronted Social Security insolvency and dealt with it in a way that put it on a firm basis for many years. So, you know, this is a problem for us. You know, I sort of opened up my computer this morning when I woke up and I saw two stories that were relevant.

**[00:27:08.08]**

So on Bloomberg, there's Hank Paulson saying, you know, we're heading toward trouble. We need a plan to deal with the day when, you know, the Treasury won't be able to finance itself. Then there's a story in the FT about the convergence in yields between Treasuries and the suprasovereign agencies, KFW, EIB, it used to be that they would pay much higher interest rates because the treasuries were liquid. Now those have converged, and this is very consistent with a Fiscal Monitor conclusion of a couple of days ago that AAA corporates and treasuries are basically trading at the same rate. So there used to be this liquidity value of treasuries because of their use in collateral, in markets, their central position, which seems to have evaporated just because so many more Treasuries are being shoved into balance sheets as the debt issuance of the US continues. Now, very importantly, the point you raised, Adam, that Kristin made, you know, this is not necessarily a dollar problem. It's a Treasury problem. It's not necessarily about default. It's about liquidity. But, you know, if the Treasury loses its interest rate advantage, that does affect long-term solvency, and that does raise the risk of fiscal crisis, and that does raise the risk of the Fed having to come in and bail out the fiscal authority in some way through inflation, and that is a dollar issue.

**[00:28:58.28]**

So I do think these things are connected. And, you know, frankly, I have more faith in the ECB as a custodian of price stability at this point than I do of the Fed going forward, given the unrelenting legal assaults on its chairman, which I interpret as assaults on the institution.

**[00:29:22.04] - Laura Tyson**

I—

**[00:29:22.28] - Adam Posen**

this is obviously a very touchy issue, and I'm going to come back to it. Just a couple things on these linkages that Maury and Klaus made on the fiscal side. So the first time I was asked to opine on whether Japanese government debt was going to blow up was 1997. And I kept telling people, take the opposite side of that bet, it'll be okay. And those who listened to me actually did pretty well, or at least avoided the widowmaker. The reason I raise this is over time, relating it back to things my colleague said, I came to realize that it wasn't just about the numbers because you could debate about what was the real deficit, what was the real amount of debt, well, how much was on the central bank balance sheet, how much were assets, but ultimately what I think kept both Japan and the US sort of the market's good side, was it was credible that a political system could raise taxes when it needed to. So like Maury mentioned, the fact that Social Security did get a decade or more long reform of the Reagan— in the Reagan era. In Japan, there were the occasional rises in the value-added tax on a permanent basis.

**[00:30:49.46]**

And I think that it wasn't even so much about how much revenue these things generated as they were indications that the regime was capable of putting things back on track when it needed to be. And Alan Auerbach, another distinguished Berkeley person and co-authors made a more formal version of this pointing out that roughly every 10 years the US would undergo some kind of commission or bipartisan presidential thing or congressional action which would sort of right the fiscal balance for 8, 10, 12 years. But we missed that this time. So we were due for it sometime around 2005, 2008. Didn't happen. Hasn't happened since. And so you've got both the fact that we haven't had sort of this course correction, even if it was only medium term, but also the signal that maybe the system isn't working as well. Anyway, so that brings us to alternatives. Um, Klaus kindly came to speak, uh, the last time he spoke on this stage was as a member of the Governing Council as a syndic central banker, and you talked a lot about— I thought very well, why we asked for you to come— about the role of the euro and thinking in terms of sort of a dashboard about the pros and cons of the strengths and weaknesses of euro as a global currency.

**[00:32:26.47]**

Maybe you could reflect on what your thinking is on that at the moment.

**[00:32:31.22] - Klaas Knot**

Actually, in preparation for this conversation, I looked up again what I had said a year ago, and it's surprisingly still okay, actually, to rehash here. I mean, no, if you look at the— if you were to score, quote unquote, the euro area and the euro on a couple of these well-known criteria that you need to have to play an important role as an international or reserve currency, then I would say that the euro has a couple of strengths. I think adherence to the international rules-based order. There's been a lot of criticism about Europe not seizing Russian assets, this and this and that. But I think it's only proof of the fact that this is such a complicated discussion in Europe. It's proof of the fact that we really adhere to the international rules-based order. And that's why we find it so difficult in Europe to take a decision that is more based on might is right, which seems to be the sentiment today in other parts of the world. Secondly, I think the commitment to price and financial stability on the ECB side is undisputed. Undisputed. Again, you can criticize monetary policy and you should always have a discussion.

**[00:33:47.13]**

I feel that's good about monetary policy. But the commitment to price and financial stability, I think, of the ECB is undisputed. So these are there on the positive side of— for the euro. But unfortunately, there are also a couple of arguments which I would put in the basket. External strength is always a reflection of internal coherence and internal integration. And there, I think it becomes a little bit more difficult. We don't reap the benefits, the full benefits of the internal market, and the internal market exists on paper, but if you try to translate the barriers that we still have when it comes to the transfer of goods and services across border within the euro area, if you try to translate these barriers into import tariffs and virtual input or tariffs, then they would be a multiple of what the US administration has been imposing on Europe and other parts of the world. So why is that important for the international reserve position? Well, because it means that we artificially suppress the yields that are to be had from— on investment. So investment in Europe still is yielding, I think, less than, for instance, in a dynamic economy as here in the US.

**[00:35:04.11]**

And if we want to become more attractive as a place to invest, I think this is something that we need to work on. And then, of course, you have the lack of deep integrated capital markets and the capital markets union, on which I think a lot has been written, a lot has been said, and at a very high level of abstraction, I think everybody's in favor. But when it comes to sort of translating that abstraction into concrete action, then the sort of reflexes to protect national processes and national procedures when it comes to insolvency law, when it comes to having sort of your own market overseer, domestically. All these things come to the fore. The fact that you can't have a capital markets union without capitalists. Well, where are capitalists typically coming from? People saving for their old age retirement. But unfortunately, we don't have many pension funds in Europe. We have pension funds in the Netherlands, but the Netherlands is an exception to the rule here. In many European countries, people still save for their old age retirement by putting their money on a bank account. Well, I have nothing against bank accounts, but maybe this is not the best investment opportunity if you really do your investment with a 30, 40, 50 potentially year horizon.

**[00:36:29.13]**

So lack of auto-enrolment, for instance, in pension plans like you have the 401, we have mandatory in the Netherlands. Well, that I don't think would be feasible anymore today if you had to build that system.. But you could have a system with auto-enrolment into pension plans where automatically you would force or incent, I should say, retail investors much more into equity. I mean, if you compare capital markets participation of European citizens versus capital market participation of US citizens, there's almost a factor of 4 in between if you look at the numbers. So these are the things that we can, I think, strengthen, where we can take action, where action is actually also taken, but unfortunately a little bit too slow. But that is something that we absolutely need to do if we want to have ambitions for the euro to become more of an international reserve currency. And what is true for capital markets, unfortunately, is also true for the banking union. We have a banking union when it comes to the official side. So we centralized supervision, we have a sort of centralized resolution mechanism and everything. But if you take a look at what the banks have actually been doing over the last 10 to 15 years, well, just two numbers.

**[00:37:43.53]**

I mean, the amount of sort of credit extended by a bank in a country where it was not headquartered, that amount of credit in 2011 in the euro area was €4 trillion. Today it's €2.5 trillion. So there is less cross-border credit provision within between the euro area of a bank headquartered in €1 area country and extending credit into another one today than there was in 2011. Now, there is more to financial integration than just this one indicator, but it shows that we are not moving in the right direction as it comes to banking union. And the banks are sort of reluctant to really engage into more pan-European banking activities because they feel that the treatment of home host and sort of these local requirements with respect to trapped pools of liquidity, pools of solvency, etc., are not giving them the benefit actually of diversification that they would otherwise enjoy. Well, also that is something that is putting us at a disadvantage. Well, all the three examples I believe we need to tackle even if we are not interested in an international role of the euro, but if we want to foster the international role of the euro, for sure, We need to tackle these issues, and if we are not ready to tackle them, then let's not have too many illusions also on fostering greater euro usage outside.

**[00:39:10.35] - Adam Posen**

Thank you very much. And again, we'll have new things from Klaas in the months to come, but I would recommend folks look at his speech a year ago on the Institute's website as well as the various volumes. Soni Fary and I led for the Institute on the Euro at 5, the Euro at 10, the Euro at 15. Does it have a global role? Um, so let me again go back to Maury for a slightly more academic perspective. Um, so more broadly, in terms of not just the euro's global role, Maury, but we often hear, uh, there is no alternative to the dollar. How valid is that as an argument? Is that just another way of labeling a residual like network externalities that something's keeping the US dollar so overwhelmingly held, or is there something to that? And if so, do you see it changing? How do you think about the there is no alternative?

**[00:40:20.14] - Nicolas Véron**

Target?

**[00:40:21.05] - Maurice Obstfeld**

The two obvious candidates would be the euro and the yuan. You know, the euro is the second largest reserve currency already. There's significant invoicing in euros, so that's mostly in trade with Europe. The yuan is much lower in terms of all the metrics of what a global currency would be. Neither of them on current policies and institutions could replace the dollar. The euro certainly has potential. I think for the yuan, there would have to be a much more thoroughgoing reform, which would involve also opening China's capital markets, things that are simply not going to happen given the nature of the regime. So at present, nothing is positioned to be a global currency. You know, the euro, even with the reforms that Klaas mentioned and even with resolution of the Ukraine problem, which I think is essential for Europe moving forward, even with the fiscal union, which I think is essential for the euro to be a global currency, it might not rival the US. So what we would be heading toward is more something multipolar. You know, basically, you know, instead of having this one global currency which yields great efficiencies, you know, basically the dollar plays the same role in the global economy that domestic monies play within borders.

**[00:42:10.08]**

It's an international money. It's a huge public good. Instead of having that, we would have a multipolar system. So, you know, a number of people, notably recently my friend Paul Krugman, have quoted this paper by Charles Kindleberger from the '60s saying that, you know, the dollar is It's like the English language. You know, if two people who don't speak, speak different languages come together, they're most likely to converse in English if they can converse at all. It's a universal language. And even Kindleberger, when the Bretton Woods system broke down, said the dollar's finished as an international currency. Now, he was wrong about that, but it shows that even these network externalities can be overcome in situations that are sufficiently disruptive. So, you know, what I would see is the, you know, the euro making progress, yuan making a lot of progress, even on current policies, but China's been pushing that very hard and A lot of countries, particularly in Asia, have incentives to hedge on their exposure to the US by getting more deeply involved with, for example, China's international messaging system and other innovations. And the realm of the dollar would just shrink, become less universal than it is.

**[00:43:46.26] - Adam Posen**

Decentered.

**[00:43:48.35] - Maurice Obstfeld**

Decentered. And I think that's what Kindleberger had in mind in the early 1970s when he said the dollar is finished. And indeed, you know, from the standpoint of the late '70s, the dollar was under a lot of pressure. That was reversed largely as a result of US getting inflation under control. But it was an open question. I think we're moving more into that territory now.

**[00:44:18.41] - Adam Posen**

One last round before I open up the questions to our distinguished in-person audience. Um, Maury, we published earlier this week a brief essay or a blog from you about the non-necessity of running current account deficits to being a reserve currency, or alternatively, the reserve currency status of the dollar is not to blame for— but along the way in that essay, you also spoke a bit or wrote a bit about stablecoins and whether the issuance aggressively of the US Treasury or encouragement by the US Treasury of dollar-based stablecoins would or would not make a difference. Could I ask you to just say a few words about that since Treasury Secretary Bessent does seem to think this is a big deal.

**[00:45:14.47] - Maurice Obstfeld**

Well, this is obviously a huge debate, and it's also relevant to sort of financial stability considerations.

**[00:45:23.17] - Adam Posen**

Yes, that's where Klaus comes in next.

**[00:45:26.43] - Maurice Obstfeld**

Address, you know, but the assertion that Treasury Secretary has made and the hope is that the, um, uh, sort of main— mainstreaming of stablecoins that was facilitated by the Genius Act in the US will promote global use of Genius-compliant stablecoins. And these, according to the Genius Act, have to be backed by a limited set of assets. Including short-term bank deposits, but also short-dated Treasuries. And so if global demand— and by this I mean mostly foreign demand, I think Secretary Bessent means mostly foreign demand— increases as much as he has forecast and others have forecast, then you presumably get more demand for Treasuries, and that lowers Treasury yields at the short end, and that enables the, um, the Treasury to borrow more cheaply, and that helps U.S. fiscal solvency. And the Treasury has in fact been to some degree shortening maturities of what it issues, um, so that it can benefit from that and also make these short-term Treasuries available to the market. I think that's very, very optimistic for that to be a big effect because there's a question of how additional this demand would actually be. So, you know, Argentines hold, you know, some $270 billion in dollars that Argentina, if you look at the private sector, including the private sector's net international creditor, they hold all these dollars.

**[00:47:29.38]**

So if they move them into stablecoins, we don't know what assets that's coming from. They could come from banks that are holding treasuries. They could come from treasuries that Argentines are holding. We just don't know. So how much is the increase in the net demand for treasuries? I think it's very unclear. So, you know, it's a nice thought, but it's unclear to me that it's going to pan out. And in fact, in recent months, global demand for stablecoins has been actually flattening out, not been growing as it would have to to meet these forecasts.

**[00:48:10.25] - Adam Posen**

Thank you. So finally, before we turn to the audience, Klaus, anticipate where I was going. As former chair of the FSB, as someone who cares about financial stability, how do you think about the US Genius Act and trying to aggressively promote dollar stablecoins? What are the implications for the world?

**[00:48:29.58] - Klaas Knot**

I want to begin by saying that obvious— for me, it is obvious that if you want to sort of keep your currency as an international reserve currency, obviously B, you can't afford to turn your back to digitalization. I think the whole world digitalizes. Our money and payment systems digitalize. So in that sense, I would have a sort of open mind with respect to the emergence of stablecoins, of tokenized deposits, what have you. But the question, of course, is to what extent should you aggressively push them? And what are the financial stability risks involved? Because I do think there are financial stability risks involved, so I do think that adequate regulation will really be crucial. Now, let me begin by saying I just heard Maury say shortening the maturity of the debt. Well, in my thinking, that's always translated with higher rollover risk. That is on one side. But then the whole structure of stablecoins obviously has some inherent risks themselves, because stablecoins provide runnable liabilities. Stablecoins are the digital analogy to a money market fund, and we know from history that constructs that have runnable liabilities, at some point in time, they will be run, right?

**[00:49:56.06]**

And then What do you do? What is a run? Well, a run is that individuals want to get out of their claims on a private entity and convert it into a claim on a sovereign entity. If the US continues to stick with its currently held position that there will not be a digital dollar, then where is the run? Where are people going to run to? That would be my question one. And that basically relates to financial stability in the US. If the stablecoins are also actively being used to push further dollarization in emerging markets and developing economies, then you might say, well, these economies dealt with dollarization already for a long time, et cetera. What's new under the horizon? Well, what's new under the horizon, that the transaction costs of doing so are much, much lower. And if this leads to a massive increase in dollarization in emerging markets and developing economy, I think it has the potential to destabilize local banking sectors in these countries. So there is a financial stability issue in the US that is akin to the runs on money market funds that you've seen here before. But then at least people— we knew where people ran to.

**[00:51:12.34]**

And in the digital world, I'm still open-minded where people will run to. But then there is the bigger financial stability issue, I think, also for those countries that are on the receiving end of this.

**[00:51:23.52] - Adam Posen**

Thank you very much. Just on that, a few years ago, we had an early presentation by Brundtland, Brundtland, Meyer, James, and Landau of their paper looking ahead on this and flagging what Klaas said about the risk of outflows from the El Salvadors and the Gabon, and not to pick on any one country, but I mean countries where there might potentially be increased appetite and therefore destabilization if the transaction costs go down. I would just point out, and I and others spoke about this at our conference on central bank independence earlier this year, that we have to remember, as Klaas mentioned, as Maury mentioned, with the attacks on the Fed, Part of that has been also a desire that may not be directly an attack, but a greater alignment of the Fed supervisory autonomy, or a diminishment of the Fed supervisory autonomy and capacity, and a greater alignment of that with the administration views. And so I worry in this regard about potentially firms that are issuing these stablecoins, also dabbling in crypto and other assets. Now, we may be saved by the fact that people watch Bitcoin blow up this year and have not kept increasing that, but the risk of creeping definition of what's a systemically important institution and what's an institution that should get a bailout when they say that stablecoins are okay and there's some wall between them and the rest of the firm, when the rest of the firm may be partially owned by members of families of the Trump administration, I think is worth monitoring.

**[00:53:24.35]**

On that happy note, I'd like to open up for questions. Jessica has a traveling mic in front. There's a standing mic in back. As always, I would ask our Peterson fellows to wait to see if someone else is brave enough to ask a question, a guest, and then if not, we'll resort to you. Anyone care to go? Please.

**[00:53:52.26] - Audience**

Arns Ebrechts with Goldman. I have a question about what you were saying, that we're perhaps moving to a multipolar system when it comes to international reserve currencies. When you say that, do you also have in mind that that implies a multipolar world in terms of trading blocks, or do you think it's also possible to have a multipolar system even if we do not see the emergence of a multipolar or a decoupling in terms of international trading?

**[00:54:27.40] - Maurice Obstfeld**

You know, I think the move toward multipolarity in currencies is not necessarily linked to trade relations, although, you know, I mean, in general, you know, if we think of trade as being driven by the gravity model, then trade depends to a great extent on distance. You know, we think that probably currency blocks will be regionally focused, and, you know, there's no contradiction, but the you know, the greater nationalism we've been seeing in trade policy and industrial policy, I think pushes in this— in the same direction. I think it could accentuate the move to a more multipolar financial system. I think one of the fascinating things to think about are the links between, you know, trade fragmentation and financial fragmentation. You know, we— and You know, maybe Klaus will want to address this also, but we've, you know, we've seen obviously huge turmoil in the trade space. We haven't seen quite so much, I think, in the financial space. You know, finance has not become a political flashpoint yet, though I think that may be coming. You know, there have been discussions of, capital flow taxes, of certainly greater strategic considerations in thinking about regulations on FDI, but it hasn't been sort of a large-scale backlash against finance the way it has been against trade.

**[00:56:08.20]**

But maybe that's not that far away.

**[00:56:16.04] - Adam Posen**

Okay, so, I know there are 3 Peterson fellows looking to go, but first let's group questions in pairs of 2. So let's take Laura Tyson, then Nicola Véron, then we can do Joe Gagnon and Cullen Hendricks. And Jacob, you're in my blind spot, so you're in the third round.

**[00:56:35.55] - Laura Tyson**

So I just want to follow up on the fiscal policy challenges for the United States. And I first want to note that The Social Security point, I really wanna go back to Greenspan here because Al Gore was made great fun of back at the, around right before 2000 about the idea of a lockbox for Social Security. We had a surplus developing in the federal government of the United States. And Greenspan said, "The US government should never have a surplus because it would have to invest in things." And we don't want the US government to be investing in any of the private capital in the system. No ownership, no governance, no rights, and therefore no surpluses. I swear, that is what Greenspan said, and it was the argument for no Social Security lockbox. Now, going to the current situation, I think we have to recognize here how complicated it's going to be to get the tax increases that you're suggesting we absolutely need. We've cut non-discretionary spending to almost nothing already. We're building up military spending. It— the only solution here for the US fiscal deficit is a tax increase and a significant one. And this would happen under Democratic leadership, not Republican leadership.

**[00:58:08.16]**

So I'm just gonna make a prediction and ask you what you think. I think that the tax increase is going to be heavily weighted to the very top. Look at what's happening in the western states, the billionaires' taxes, the millionaires' taxes, the special taxes, all because of— and then the wealth taxes. And I wonder if you— how you— I mean, how you think those are going to play out, or do you think there's a possibility? I really guess I'm making a political statement here that These tax increases are going to come under Democrats, and we know something about the way they're going to be structured. They're going to be much more progressive. They're going to be linked to the top, and there's going to be a significant increase as well in corporate income taxes.

**[00:58:55.04] - Adam Posen**

Okay, and over to Nicolas, please.

**[00:59:00.29] - Nicolas Véron**

Thank you. Nicolas Veron at the Institute. My question is about stablecoins because Adam referred to the concerns that have been going back several years, that indeed stablecoins could be disproportionately adopted in the Global South, for lack of a better expression, and lead to loss of monetary policy autonomy there. And to me, at least, the surprise is how little of this has happened. We haven't really observed that, to my knowledge, in major ways so far. That doesn't mean it won't happen, but I would be interested in our two speakers reaction to that observation, if indeed the observation is accurate. Thank you.

**[00:59:43.57] - Adam Posen**

Why don't we start with Maury, just on the— not asking you to be partisan political, but just on the feasibility of tax increase and what form that might take. Klaas is welcome to comment on that if he likes, but then both of you on the lack of apparent outflows that we've seen?

**[01:00:06.48] - Maurice Obstfeld**

Okay, well, I think Laura can speak with great authority on prospects of closing the deficit since you were running economic policy in the US last time that happened. It seems like centuries ago. And indeed, you know, Greenspan was alarmed by the prospect that the Fed would have to buy private sector assets to do monetary policy. And then you sort of fast forward to the global financial crisis.

**[01:00:35.24] - Adam Posen**

Not to mention Intel and various mining stocks.

**[01:00:39.16] - Maurice Obstfeld**

Yeah, now we're way out there. But I mean, I was in a conversation with a Chinese policymaker yesterday who was describing the fiscal problem there being so difficult because while wages are taxed progressively, there's very little tax on capital income. And so the rich don't really pay taxes. And it's like, are you talking about China? So there is definitely scope. And the narrative people tell is, well, if you do that, you'll kill capitalism. You'll kill investment. Growth will go to zero.. And that's just not what's going to happen. So, you know, there are things like the inheritance tax, which, you know, come on. You know, if you have money, you can easily escape taxation and pass on intergenerational wealth. So the, you know, the means are there. It's not going to kill growth, but the political will has not been there. And it may be that it takes a fiscal crisis to make that happen. I don't know what party will confront that crisis. If past is prologue, then the mess will occur under a Republican administration and have to be cleaned up under a Democratic administration. But we don't know. It's in the future.

**[01:02:09.18]**

How far in the future, that we don't know either.

**[01:02:13.48] - Adam Posen**

Why Nicola and I worried unnecessarily about outflows from US dollar stablecoins.

**[01:02:22.48] - Klaas Knot**

Yeah. First, very short comment on US taxation. There has, of course, been a tax increase. It was called an import tariff that for 96% was paid by US customers. So it was a hidden tax increase, but of course, not in any size comparable to, I think, the fiscal needs. It's interesting, Nicolas, your point. That this has not happened so far. I think there is still a general distrust of a lot of citizens in, let's say, digital currencies so far, that in my view is part of the explanation here. Also that some of the governments have taken a very vehement anti-digital stance. Think about India being, I think, the most prominent representative of that. But I would still say maybe so far so good, but don't bank on it, because if digital currencies find their ways more and more into the mainstream— I mean, there is the problem of traditional cross-border payments being cumbersome, being costly, being slow, being unfair, and all the rest of it. And for that, stablecoins seem to be a very— at first sight, a very effective, efficient low cost, probably also because of low controls, and you can have debate on whether the AML/CFT safeguards are truly in place there, but I think the attractiveness will continue to be there.

**[01:03:55.57]**

So the more familiar people will become with digitalization, I guess this could still happen and this debate about monetary policy autonomy will come back in these countries. By the way, interestingly, I also— you didn't talk about the US, but in a way, stablecoins, pushing them as a payment in this instrument, also undermines the singleness of money here in the US and creates a sort of form of competition for who controls the money supply between the Fed and the Treasury. I mean, I'm talking about monetary policy sovereignty.

**[01:04:29.29] - Adam Posen**

OK, we're close to time. So if Joe and Cullen could go to the back mic and ask their questions. Oh, Joe has an actual mic. OK, then Cullen.

**[01:04:39.32] - Joseph Gagnon**

Thank you. Joe Gang Yoon, Peterson Institute. My question really follows on from the first one. You talked about reasons in the US why traders and investors might be moving a bit away from the dollar, but also reasons why no other single currency seems poised to quickly replace the dollar. So we're talking about a multipolar world. My question is, how do you see the welfare effects of that? Losing network externalities, the common language thing that you talked about, is that a meaningful reduction in global welfare or is it a trivial reduction in global welfare or are there even benefits that we aren't talking about that could make it even a better system?

**[01:05:21.53] - Adam Posen**

Thank you. Colin.

**[01:05:23.19] - Cullen Hendrix**

Thank you very much. My question is just a hybrid of what Joe just put on the table and our colleague from Goldman asked earlier. So it's asking you to think about this kind of decline in net welfare that might be associated with a transition away from the dollar affecting the US role as the global sort of, maybe not security guarantor for all, but at least for freedom of navigation on the seas historically?

**[01:05:47.30] - Adam Posen**

Okay, big picture question. We'll go first to Maury and then to Klaus.

**[01:05:52.34] - Maurice Obstfeld**

Well, I wouldn't presume to quantify the loss. I think it is a, efficiency gain to have a single international numeraire and standard for pricing. I tend to think that when flexible exchange rates collapsed, one of the predictions that some made was that it would disrupt the international trade system because of the difficulty of forecasting prices. And maybe the, you know, this global role of the dollar has been a mitigating factor that has greased the wheels of global trade and finance. So I think all those things are there. You know, how much is it worth? You know, I, yeah, I wouldn't want to put a number on it. You know, do I think it's 10% of global GDP?

**[01:06:51.33] - Joseph Gagnon**

No.

**[01:06:52.26] - Maurice Obstfeld**

Do I think it's 0.5% of global GDP? You know, that's in a plausible range, but, you know, we need some, you know, some very careful modeling and calibration to try to come up with a range of estimates.

**[01:07:08.30] - Klaas Knot**

Well, part of the benefits in terms of the convenience yields have, of course, already disappeared. I mean, the examples that Maury gave from today's FT article, I think, already show that there has been a significant reduction in convenience yield on US Treasuries. In Europe, I think, the thinking goes exactly the other way around. We have limited convenience yields, but if we managed to get more integrated capital markets and deeper and more liquid, then actually we think that there could be more convenience yield generated than is currently the case in the Bund curve, which is is the most liquid and the most creditworthy curve that we have, but which is still in size, I mean, in no way comparable to the US Treasury curve. Now, I mean, if the world sort of more polarizes and moves into geo-economic fragmentation and different blocks, that is where I think most of the welfare loss is. If that geoeconomic fragmentation subsequently were to get reflected into also a multipolar currency world, I'm not so sure whether that last step then adds an awful lot of further welfare reductions. The true welfare reductions, in my view, are already created by geoeconomic fragmentation and financial fragmentation that goes with it.

**[01:08:37.45] - Adam Posen**

I appreciate my colleagues and everyone making such thoughtful questions. I would, just in response to Joe and Colin, add one more thought. I think, as I've been arguing, I think people need to conceive some of what the US has been providing as a form of insurance. And I think one way of thinking about— you can call it a golden pot, good— but specifically, the idea that you could park money in treasuries no matter who you are, as long as you weren't a particular, by name sanctioned oligarch, that you could get in and out without really affecting the prices, that nobody, government gatekeeper, again, with a very small exception, was keeping you in and out, and that everybody would accept it, was a safe asset. That is no longer so safe. And for all the reasons that Maury and Klaus have enumerated, there isn't an obvious replacement. And I'm not sure that the convenience yield, while an important aspect, fully grasps that. And so when you think about the massive movement of Chinese official reserves from dollars into gold, when you think about some of the decisions being made by other large pool long-term investors, when you think about the hedging costs being incurred for dollar assets in a way that we haven't seen at least in 40, 50 years.

**[01:10:14.08]**

Again, they're not enormous, but it changes the whole portfolio, I think, in many ways. So if we do that calibration exercise, I would want to include, try to include that aspect. Thank you all for joining us on this Friday of the spring meetings here at the Peterson Institute.