Comments for the workshop on "Currency Hierarchy, Macroeconomic Policies and Development Strategies"

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3 November 2014
Freie Universität Berlin

Paper 1: Keynes at the Periphery, by Fritz, Prates and de Paula

Focus of comments:

1. **Idea of hierarchy: the idea itself, and commonalities and differences among the papers**
2. Theoretical interventions, policy questions
   - Audience: academic and policy arenas
   - Did anyone else get there first?
   - Who might be interested in listening?
   - Journal possibilities for publication

The idea itself

- 4 steps from the Taylor rule, and from the plain vanilla DSGE model:
  1. Monetary policy is not all that matters, so does fiscal policy
  2. But open economy forces (the exchange rate) also affect macro outcomes
  3. And policy should encompass more than monetary-fiscal policy – sectoral, labor-market, etc.
  4. Yet here the choices are more stringent if and when a nation is not at the top of the currency hierarchy

The idea itself

- 3 steps from "chartist," "fundamentals" and "sunspot" models of exchange rates:
  1. Both structure and expectations matter, it's not either/or; and structural VARs or VECMs etc. are not enough
  2. We have a deeper conception of what structure is (Harvey/Kaltenbrunner – rigidities matter) and what drives expectations (uncertainty)
  3. And policy should encompass more than monetary-fiscal policy – sectoral, labor-market, etc.
  4. Yet here the choices are more stringent if and when a nation is not at the top of the currency hierarchy

The idea itself

- 3 steps from a number of Keynesian formulations (exchange-rate/interest-rate models):
  1. Monetary, fiscal, and exchange policy all have to be considered together
  2. And policy should encompass more than monetary-fiscal policy – sectoral, labor-market, etc.
  3. Yet here the choices are more stringent if and when a nation is not at the top of the currency hierarchy

The idea itself

- 3 steps from a number of international political economy (IPE) models:
  1. The interdependence of monetary, fiscal, and exchange policy choices with economic dynamics
  2. And policy should encompass more than monetary-fiscal policy – sectoral, labor-market, etc.
  3. Yet here the choices are more stringent if and when a nation is not at the top of the currency hierarchy

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1. 

International Financial Instability in a World of Currencies Hierarchy

Terzi, Andrea; Monetary and Exchange Rate Systems: A Global View of Financial Crises, 2006, pp. 3-21, Cheltenham, U.K. and Northampton, Mass.: Elgar

Subjects: Monetary Systems; Standards; Regimes; Government and the Monetary System; Payment Systems ; International Monetary Arrangements and Institutions ; International Lending and Debt Problems ; Financial Institutions and Services: General

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2. 

Academic Journal

Financing Development: Removing the External Constraint

Bougrine, Hassan; Seccareccia, Mario; International Journal of Political Economy, Winter 2009-2010, v. 38, iss. 4, pp. 44-65

Subjects: Macroeconomics: Consumption; Saving; Wealth ; Capital; Investment; Capacity ; Macroeconomics: Production ; Money and Interest Rates: General ; Monetary Systems; Standards; Regimes; Government and the Monetary System; Payment Systems ; Current Account Adjustment; Short-term Capital Movements ; Economic Development: Financial Markets; Saving and Capital Investment; Corporate Finance and Governance

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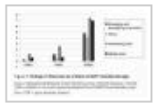


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3. 

Book

The geography of money

Cohen, Benjamin J.; 1998, pp. xiii, 229, Ithaca and London: Cornell University Press

Subjects: International Monetary Arrangements and Institutions

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4. 

Book

Monetary and Exchange Rate Systems: A Global View of Financial Crises

Rochon, Louis-Philippe; Rossi, Sergio, eds.; 2006, pp. xxvi, 267, Cheltenham, U.K. and Northampton, Mass.: Elgar

Subjects: International Finance: General ; Aggregate Factor Income Distribution ; International Financial Markets ; International Linkages to Development; Role of International Organizations ; Economic Development: Financial Markets; Saving and Capital Investment; Corporate Finance and Governance

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New Open Economy Macroeconomics

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Biography

Ph.D. from Yale (1992), his contributions range from theoretical and empirical work on fiscal and monetary policy, to analyses of currency and financial crises and their international contagion. Serves as co-editor of the Journal of International Economics, Programme Director at Centre for Economic Policy Research in London, and scientific consultant to the Bank of England and the European Central Bank.

Abstract

The New Open Economy Macroeconomics refers to a vast body of literature embracing a new theoretical framework for policy analysis in open economy, with the goal of overcoming the limitations of the Mundell-Fleming model, while preserving the empirical wisdom and policy friendliness of traditional analysis. Starting in the early 1990s, NOEM contributions have developed general equilibrium models with imperfect competition and nominal rigidities, to reconsider conventional views on the transmission of monetary and exchange rate shocks; they have contributed to the design of optimal stabilization policies, identifying international dimensions of optimal monetary policy; they have raised issues in the desirability of international policy coordination.

Keywords

Open economy models; exchange rates; stabilization policy; Mundell-Fleming

The New Open Economy Macroeconomics (henceforth NOEM) is a leading development in international economics starting in the early 1990s. Its objective is to provide a new theoretical framework for open economy analysis and policy design, overcoming the limitations of the Mundell-Fleming model, while preserving the empirical wisdom and the close connection to policy debates of the traditional literature. The new framework consists of choice-theoretic, general-equilibrium models featuring nominal rigidities and imperfect competition in the markets for goods and/or labour. In this respect, the NOEM has tight links with related agendas pursued in closed-economy macro, such as the 'new neoclassical synthesis' and the 'neo-Wicksellian' monetary economics. The assumption of imperfect competition is logically consistent with the maintained hypothesis that firms and workers optimally chose prices and wages subject to nominal frictions, as well as with the idea that output is demand-determined over some range, in which firms (workers) can meet demand at non-negative profits (surplus).

NOEM models differ from the Mundell-Fleming approach, in at least two notable dimensions. First, all agents are optimizing, i.e. households maximize expected utility and managers maximize firms' value. The expected utility of the national representative consumer thus provides a natural welfare criterion to carry out policy evaluation and design. Second, general-equilibrium analysis paves the way towards further integration of international economics as a unified field, bridging the traditional gap between open macro and trade theory.

From a historical perspective, NOEM was launched by Obstfeld and Rogoff (1995), although Svensson and Van Wijnbergen (1989) had also worked out a model with NOEM features as an open economy development of Blanchard and Kiyotaki (1987).

A specific goal of the NOEM agenda is that of achieving the standards of tractability which made traditional models so popular and long-lived among academics and policy makers. For instance, many contributions have adopted the model specification by Corsetti and Pesenti (2001), which admits a closed-form solution by virtue of some educated restrictions on preferences (Tille 2001 explains the relation of this model with Obstfeld and Rogoff 1995). At the same time, the NOEM literature has promoted the construction of a new generation of large, multi-country quantitative models by international institutions and national monetary authorities. A leading example is the Global Economic Model (GEM) of the International Monetary Fund (see e.g. Laxton and Pesenti 2003).

The following text first introduces a stylized NOEM model. Based on this model, it then provides a short selective survey of the NOEM literature, and its main advances in the analysis of the international transmission mechanism and policy design in open economies.

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Journal of Monetary Economics 50 (2003) 1109–1146

MONETARY ECONOMICS

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Monetary rules for small, open, emerging economies ☆

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Abstract

This paper develops a variant of the IMF's Global Economic Model suitable to analyze macroeconomic dynamics in open economies, and uses it to assess the effectiveness of Taylor rules and inflation-forecast-based (IFB) rules in stabilizing variability in output and inflation. Our findings suggest that a simple IFB rule that does not rely upon any direct estimates of the equilibrium real interest rate and places a relatively high weight on the inflation forecast may perform better in small open economies than conventional Taylor rules.


FROM OUT OF SPACE.... A WARNING AND AN ULTIMATUM!
THE DAY THE EARTH STOOD STILL

Klaatu barada nikto

Since the release of the movie, the phrase "Klaatu barada nikto" has appeared repeatedly in fiction and in popular culture. … No translation was given in the film. [Perhaps] the famous phrase is a "safe-word" … used during the diplomatic missions such as the one Klaatu and Gort make to Earth. With the use of the safe-word, Gort's deadly force can be deactivated in the event the robot is mistakenly triggered into a defensive posture. … the theme has evolved into a "staple of science fiction that the machines charged with protecting us from ourselves will misuse or abuse their power." In this interpretation, the phrase apparently tells Gort that Klaatu considers escalation unnecessary.

International dimensions of optimal monetary policy ☆

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Received 22 April 2002; received in revised form 24 May 2004; accepted 22 June 2004

Abstract

This paper provides a baseline general equilibrium model of optimal monetary policy among interdependent economies with monopolistic firms and nominal rigidities. An inward-looking policy of domestic price stabilization is not optimal when firms' markups are exposed to currency fluctuations. Such a policy raises exchange rate volatility, leading foreign exporters to charge higher prices vis-à-vis increased uncertainty in the export market. As higher import prices reduce the purchasing power of domestic consumers, optimal monetary rules trade off a

Does the Exchange Rate Belong in Monetary Policy Rules? New Answers from a DSGE Model with Endogenous Tradability and Trade Frictions*

Michael Kumhof
International Monetary Fund

Douglas Laxton
International Monetary Fund

Kanda Naknoi
Purdue University

July 2007

Abstract

This paper develops a 2-region DSGE model that integrates the theory of comparative advantage or endogenous tradability into a monetary model with nominal and real rigidities. We find that without endogenous tradability there is no role for the exchange rate in optimized monetary policy rules. But with endogenous tradability the exchange rate can play a much more fundamental role in facilitating or slowing down adjustments in the real economy, and it enters the optimized policy rule.

JEL Classification Numbers: C51; E31; E52

Keywords: Monetary Policy; Taylor Rule; Flexible Exchange Rates;

They come in peace – with fully loaded DSGE models…

Contents lists available at ScienceDirect

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journal homepage: www.elsevier.com/locate/jme

Sovereign risk and belief-driven fluctuations in the euro area ☆

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ABSTRACT

Sovereign risk premia in several euro area countries have risen markedly since 2008, driving up credit spreads in the private sector as well. We propose a New Keynesian model of a two-region monetary union that accounts for this "sovereign risk channel." The model is calibrated to the euro area as of mid-2012. We show that a combination of sovereign risk in one region and strongly procyclical fiscal policy at the aggregate level exacerbates the risk of belief-driven deflationary downturns. The model provides an argument in favor of coordinated, asymmetric fiscal stances as a way to prevent self-fulfilling debt crises.

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Post-Keynesian contexts: paper 1

- Stock-flow consistent modeling: sectoral balances without theory
  - A "currency hierarchy" could be introduced as a "speed bump" constraint in world with two (+) interacting SFC-defined countries. [See Lavoie/D
- Dynamic "open-economy" models of interest-rate/exchange-rate interaction, with focus on convergence or divergence over time (Oreiro, Lima, etc.)
  - Exchange rate is either fixed or flexible and adjustable; the idea of sensitivity to the conditions that may underlie 'resilience to runs' and thus 'exploitable or calculable elasticities' is assumed.
  - One way of looking at a "currency hierarchy" approach is that it would bring a *variable* exchange-rate elasticity (if monetary-policy is parameterized) or *variable* monetary-policy-effect (v.v.), wherein

In a monetary economy, all assets, including money, have specific attributes that together determine their own rate of interest (r_a), or their total expected return:

$$(1)\ r_a = a + q - c + l$$

where "a" is the expected appreciation (or depreciation) of the asset, "q" is the expected quasi-rent (or yield), "c" is the carrying cost, and "l" is the liquidity premium, which is the power of disposal that confers a potential convenience or security (Keynes, 1936, Ch.17).

Under the Keynesian perspective adopted here, the key currency is placed at the top of the hierarchy because it has the highest degree of liquidity. The currencies issued by the other core countries are in intermediate positions, and are also liquid currencies, yet with a smaller degree of liquidity than the key currency. At the opposite end are the currencies issued by emerging countries, which are non-liquid currencies (Andrade and Prates, 2013). The liquidity premium of these currencies is lower than that of the key currency and of those in the middle, labelled here as Northern currencies $l_s < l_n$ (n = North, s = South).

3.2. Asymmetric financial integration

The main features of the current international monetary and financial system are: (i) the fiduciary dollar as the key currency, on the top of the currency hierarchy; (ii) the floating exchange rate regime; (iii) almost free capital mobility; (iv) the dynamics of the current international financial system, governed by financial globalisation (Prates, 2005).

3.1. Currency hierarchy

In an open monetary economy, agents hold different financial assets denominated in a specific currency because they favourably estimate their total expected returns. Since these assets are held as a portfolio capital asset, equation (1) above can be used to represent this behaviour. For example, if $r_{an} > r_{am}$, then the asset denominated in currency n tend to appreciate relatively to the asset denominated in currency m. Thus, the process of price determination of these "currency assets" can be represented through the variables of this equation. Thus, we understand the variables a, q, c and l as attributes of assets denominated in a specific currency (Andrade and Prates, 2013).

Pricing of currency assets is peculiar due to their distinctive traits. Under the Keynesian assumption of uncertainty, short run capital gains govern transactions in the currency markets, and expectations concerning the future evolution of exchange rates are the main determinants of the current rates (Davidson, 1982; Harvey, 2009). In particular, variable a, the expected appreciation of the currency, will tend to be highly unstable and subjective. Variable c, the carrying cost, can be specified for currencies as the financial openness of a country.

We conclude this section with two lessons for our discussion. The first one is the higher vulnerability to external shocks of peripheral emerging countries than centre countries turns out such economies more prone to cost-push inflation. The second lesson is that exchange rate movements pose some essential challenges to emerging economies' monetary authorities, considering the strong influence of the exchange rate on domestic inflation in these countries and also the effects of exchange rate volatility on real variables. While the higher vulnerability to external shocks is associated with the very peripheral condition, the essential challenges posed by exchange rate movements stem ultimately from the position of their currencies at the lower end of the currency hierarchy.

Post-Keynesian contexts: paper 1

exchange rate = f(currency hierarchy determinants)

Currency hierarchy = g(liquidity premia)

Liquidity premia = h(perceived uncertainty, hegemonic power)

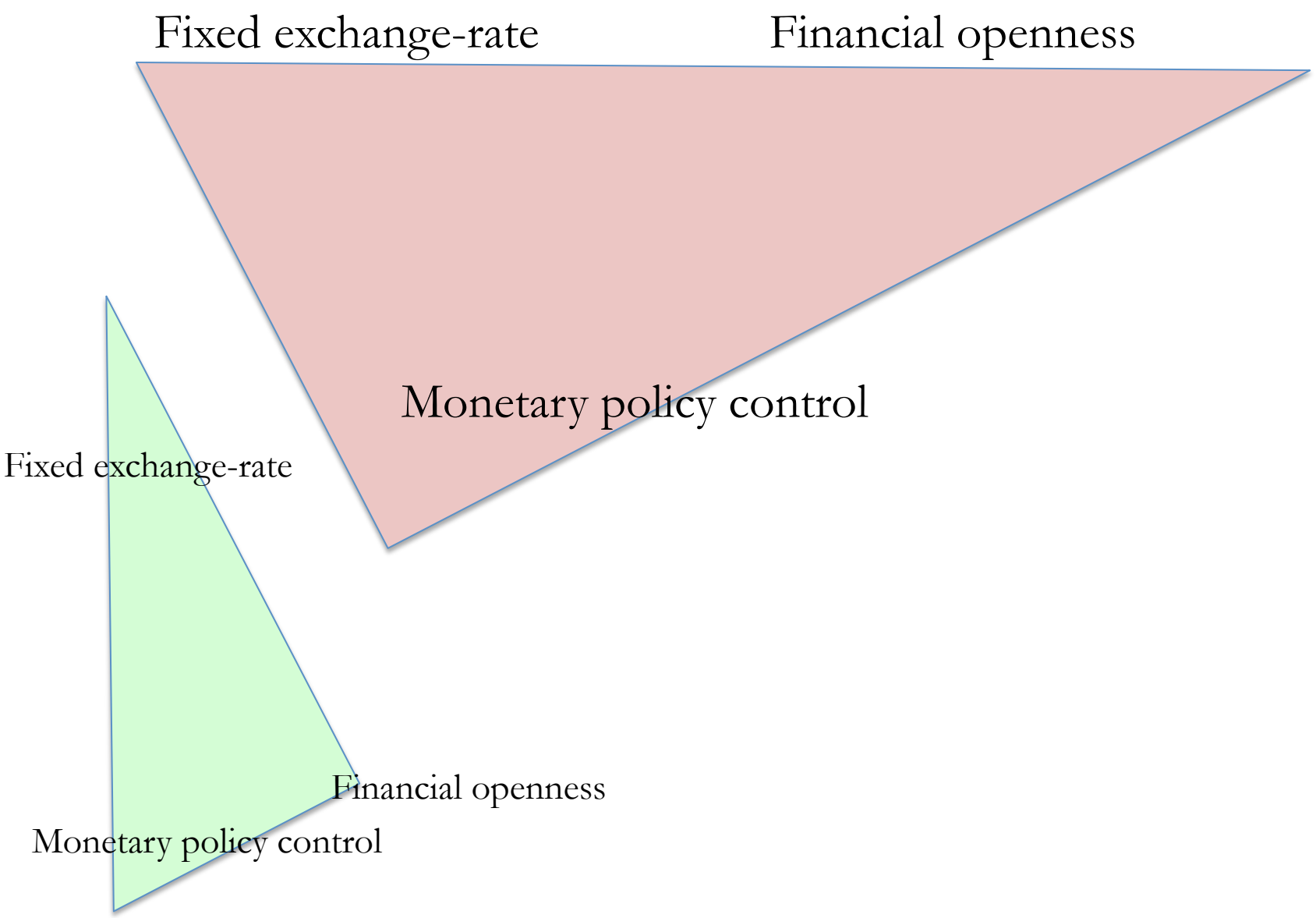
$(a_s + q_s - c_s) > (a_n + q_n - c_n)$ since $ls < l_n$

So do we have: Keynesian theory derived from/linked to uncertainty, but not power, sovereignty issues … or is there? Could we interpret the liquidity premium as a rent?

Whereas

International political economy approach is linked to distribution of global power, ignores uncertainty and market conditions (liquidity)?

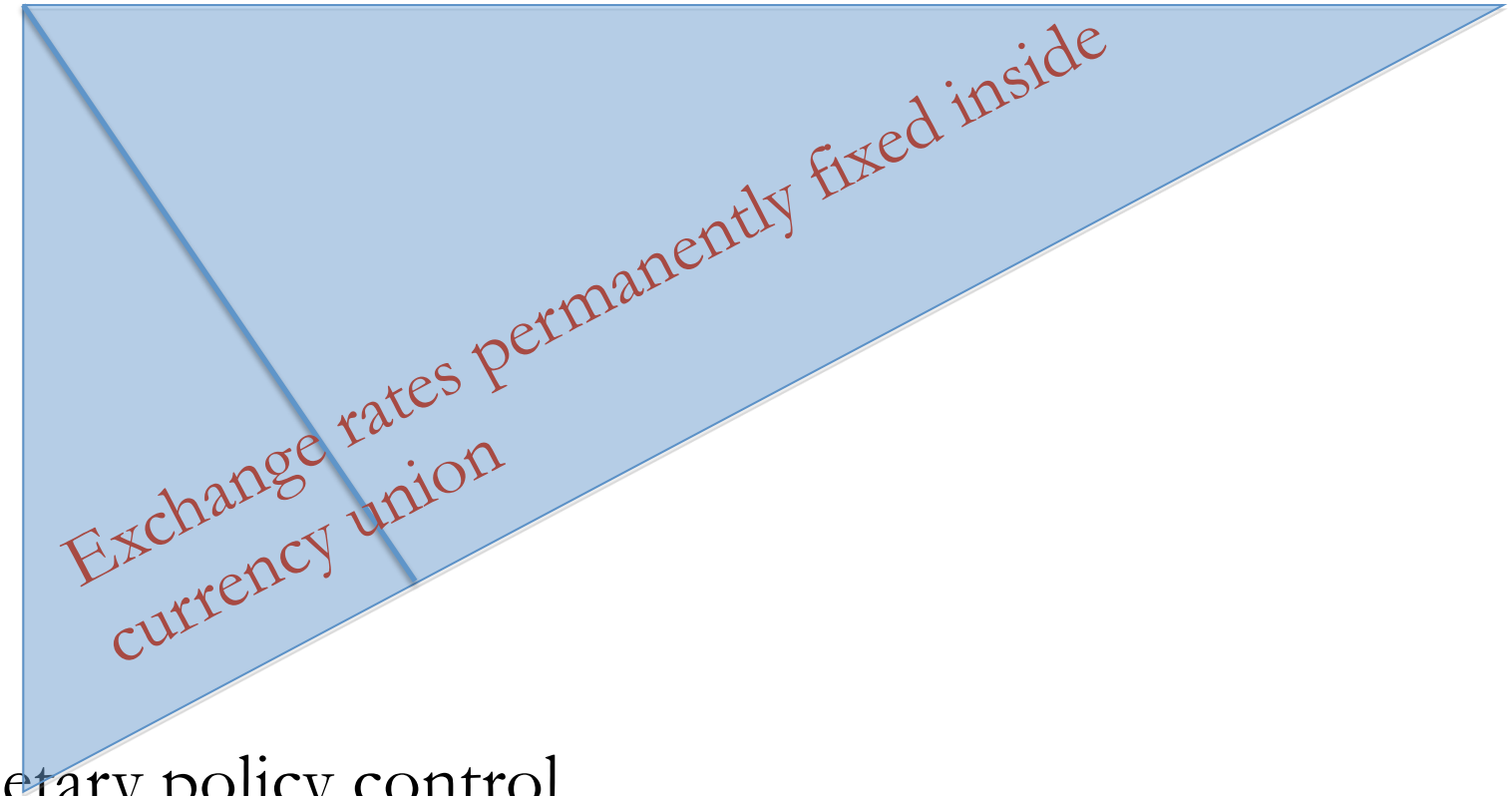
A world economy of Mundell-Fleming trilemmas



A currency union solution in a world M-F trilemmas

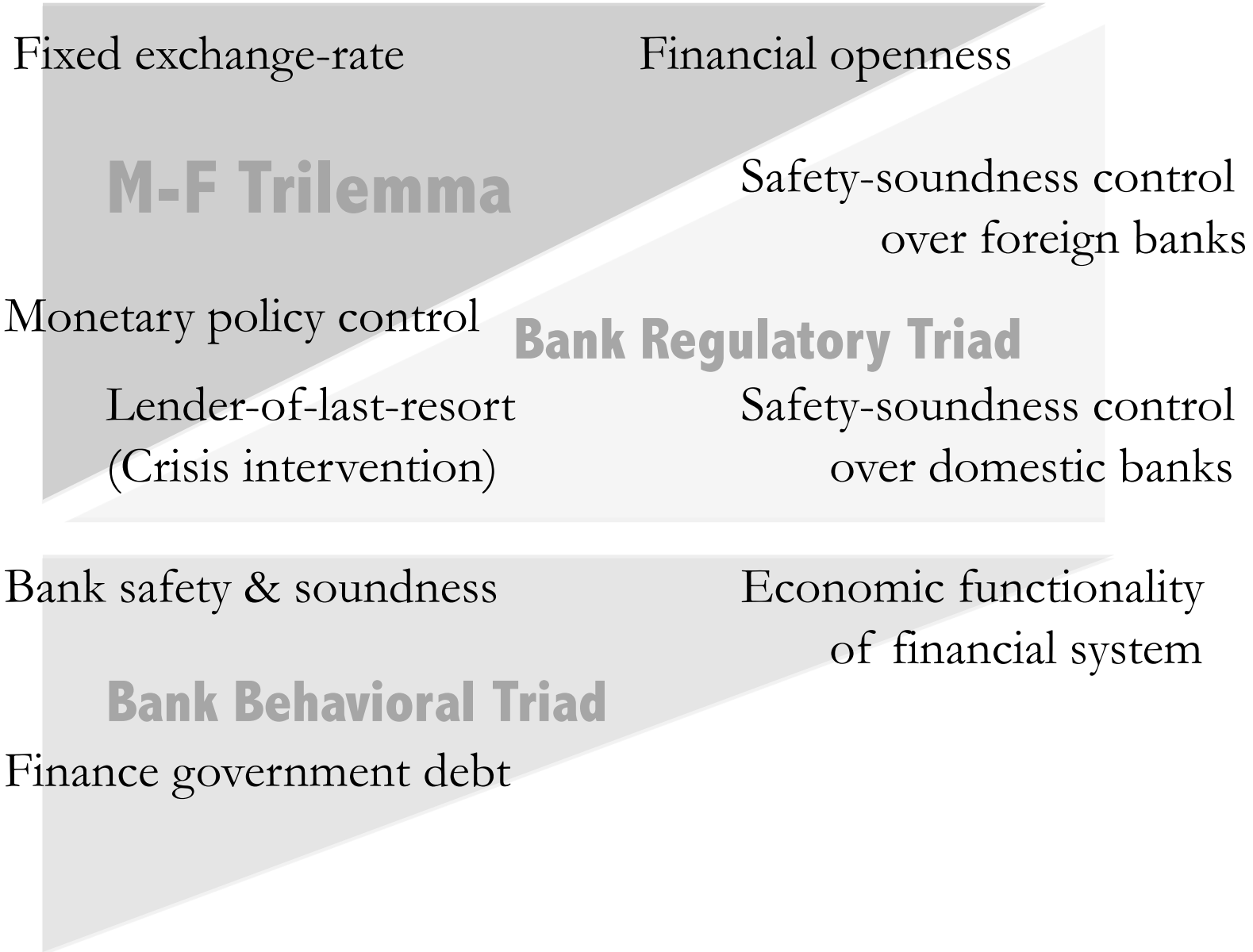
Fixed exchange-rate

Financial openness



Monetary policy control

Figure 1: A micro-macro framework for financial structure



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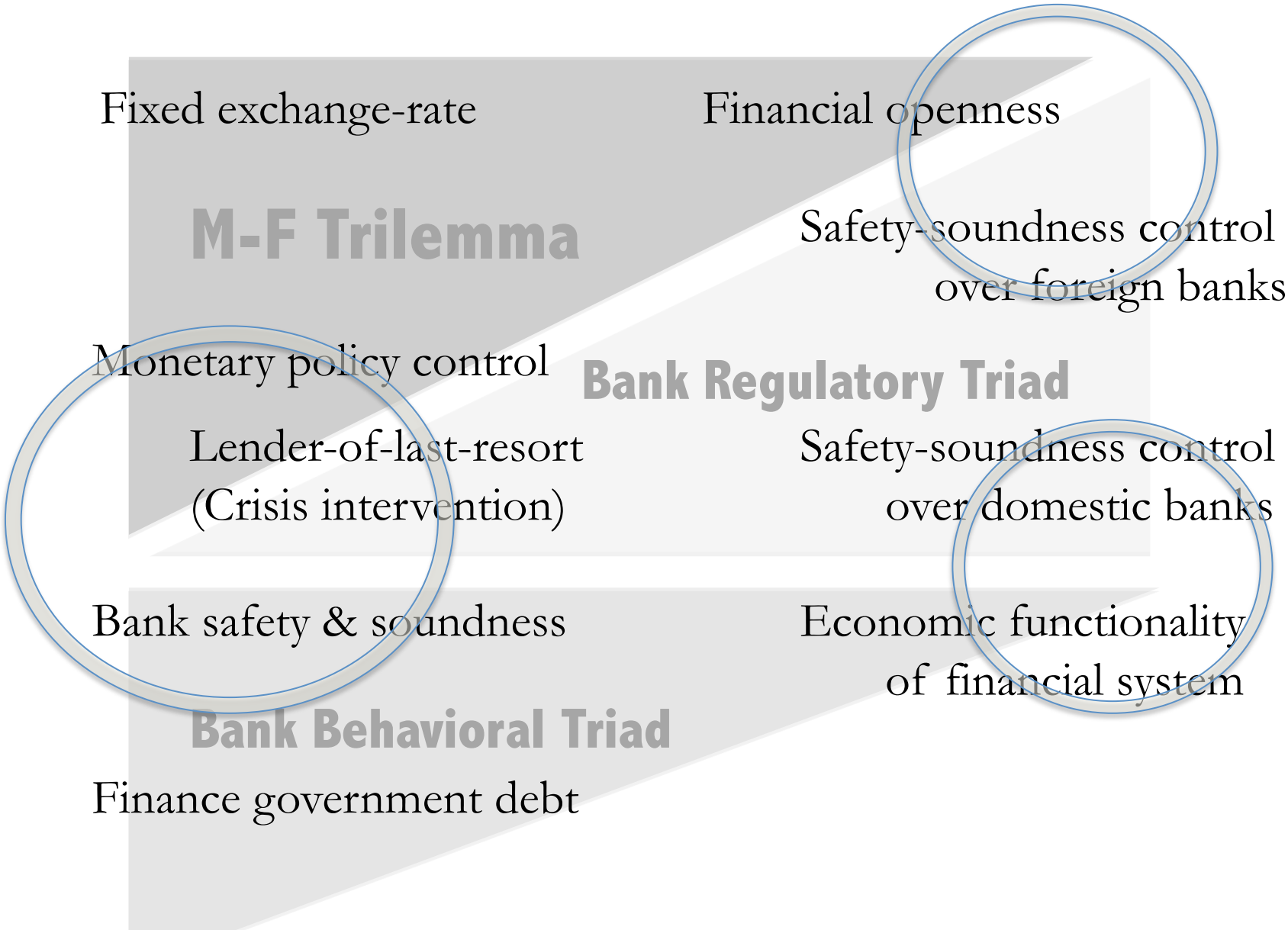
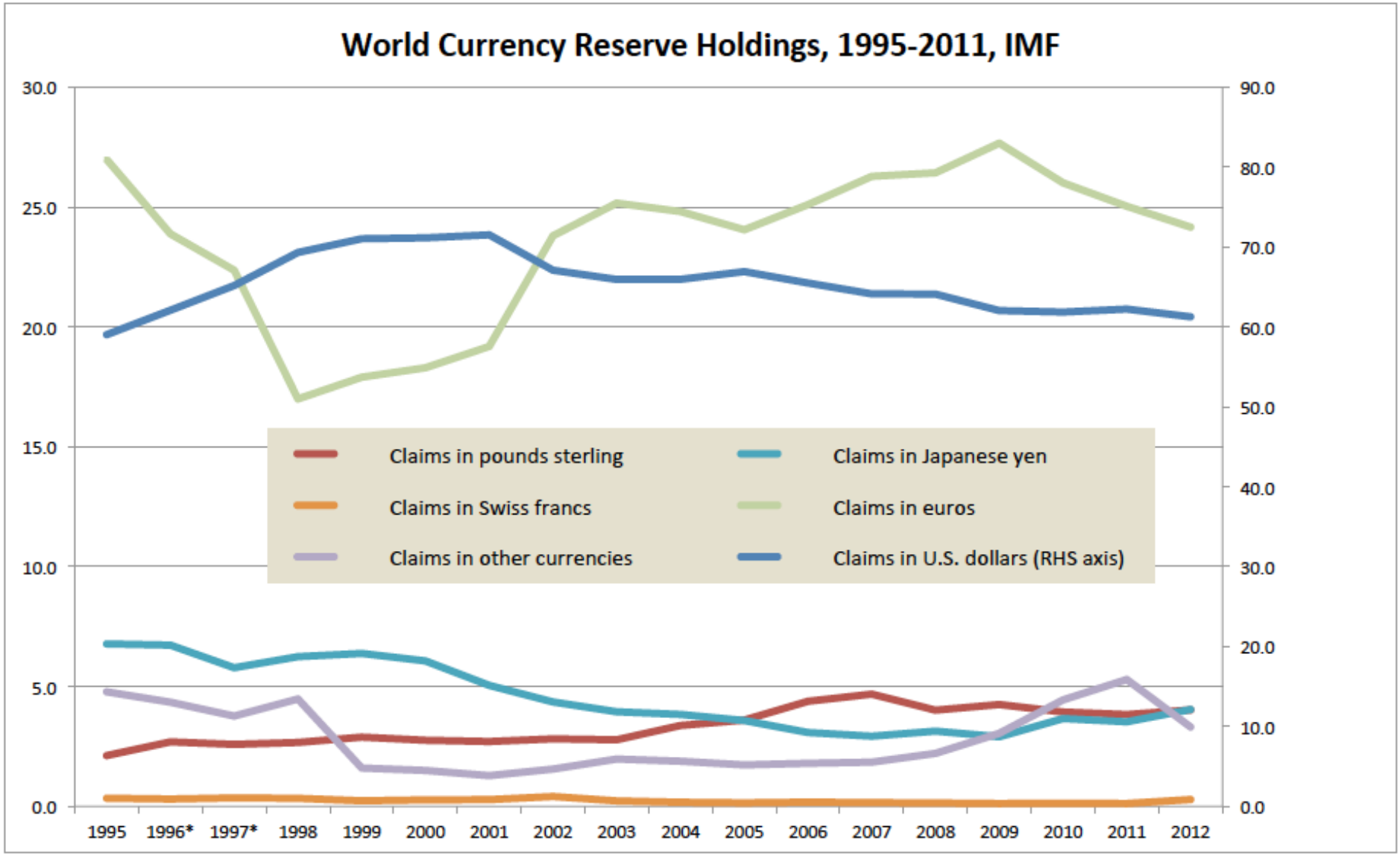
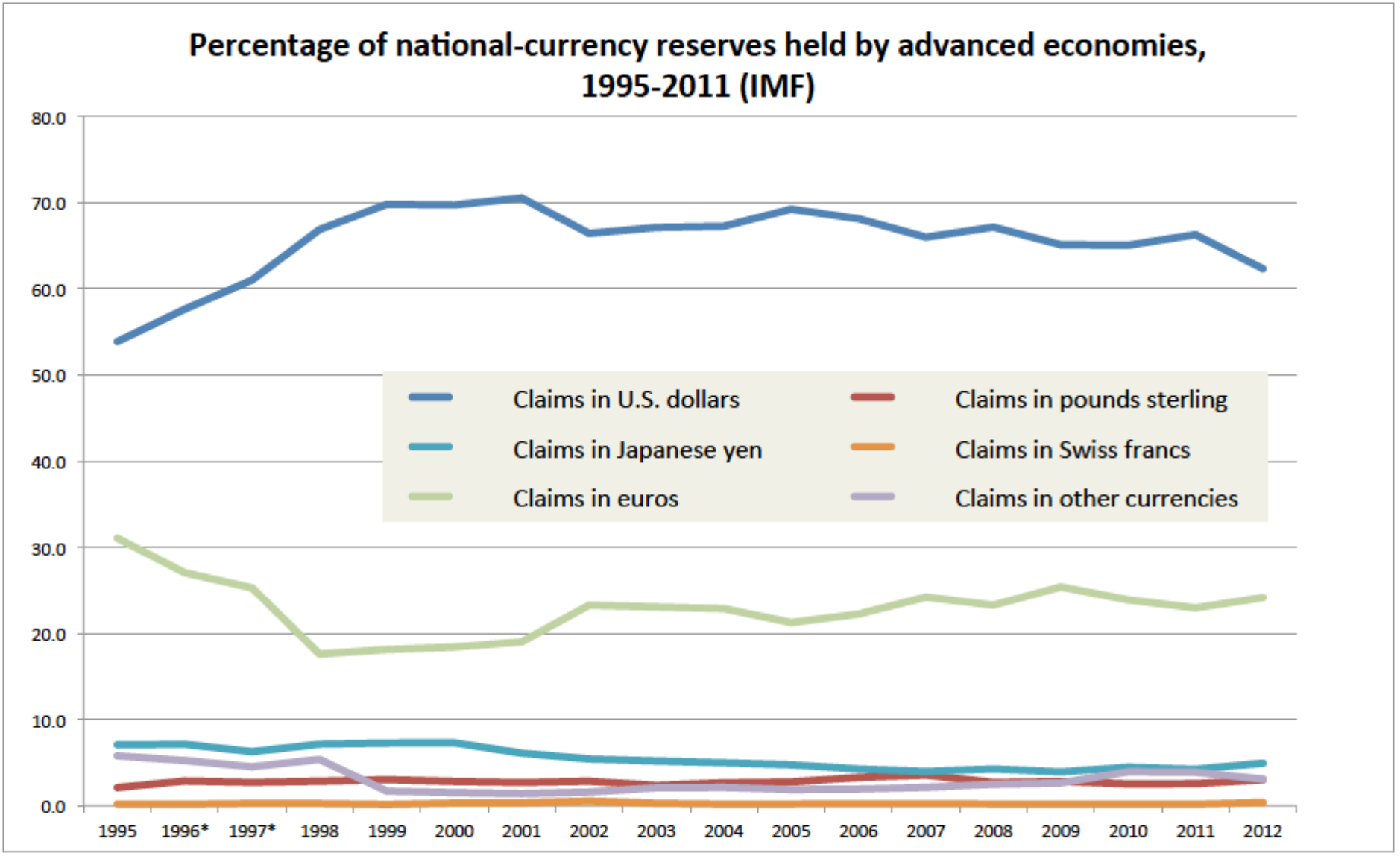


Is there a 'band' of liquidity, varying from highest for reserve currencies to zero, with some in-between?

			Degree of currency liquidity		
			High		low
Degree of control over cross-border capital mvmts and of economic/ monetary oversight	Free entry of foreign capital	LLR capacity present		***here***	
		LLR capacity missing			***here***
	Controls on capital mvmts	LLR capacity present			***here***
		LLR capacity missing			***here***

But this raises the key question: is there a differential amount of LLR capacity for different countries, or is it 1-0, that is, some have LLR, others don't?


World Currency Reserve Holdings, 1995-2011, IMF
30.0
25.0
20.0
15.0
10.0
5.0
0.0
90.0
80.0
70.0
60.0
50.0
40.0
30.0
20.0
10.0
0.0
1995
1996*
1997*
1998
1999
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
Claims in pounds sterling
Claims in Japanese yen
Claims in Swiss francs
Claims in euros
Claims in other currencies
Claims in U.S. dollars (RHS axis)


Percentage of national-currency reserves held by advanced economies, 1995-2011 (IMF)
80.0
70.0
60.0
50.0
40.0
30.0
20.0
10.0
0.0
1995
1996*
1997*
1998
1999
2000
2001
2002
2003
2004
2005
2006
2007
2008
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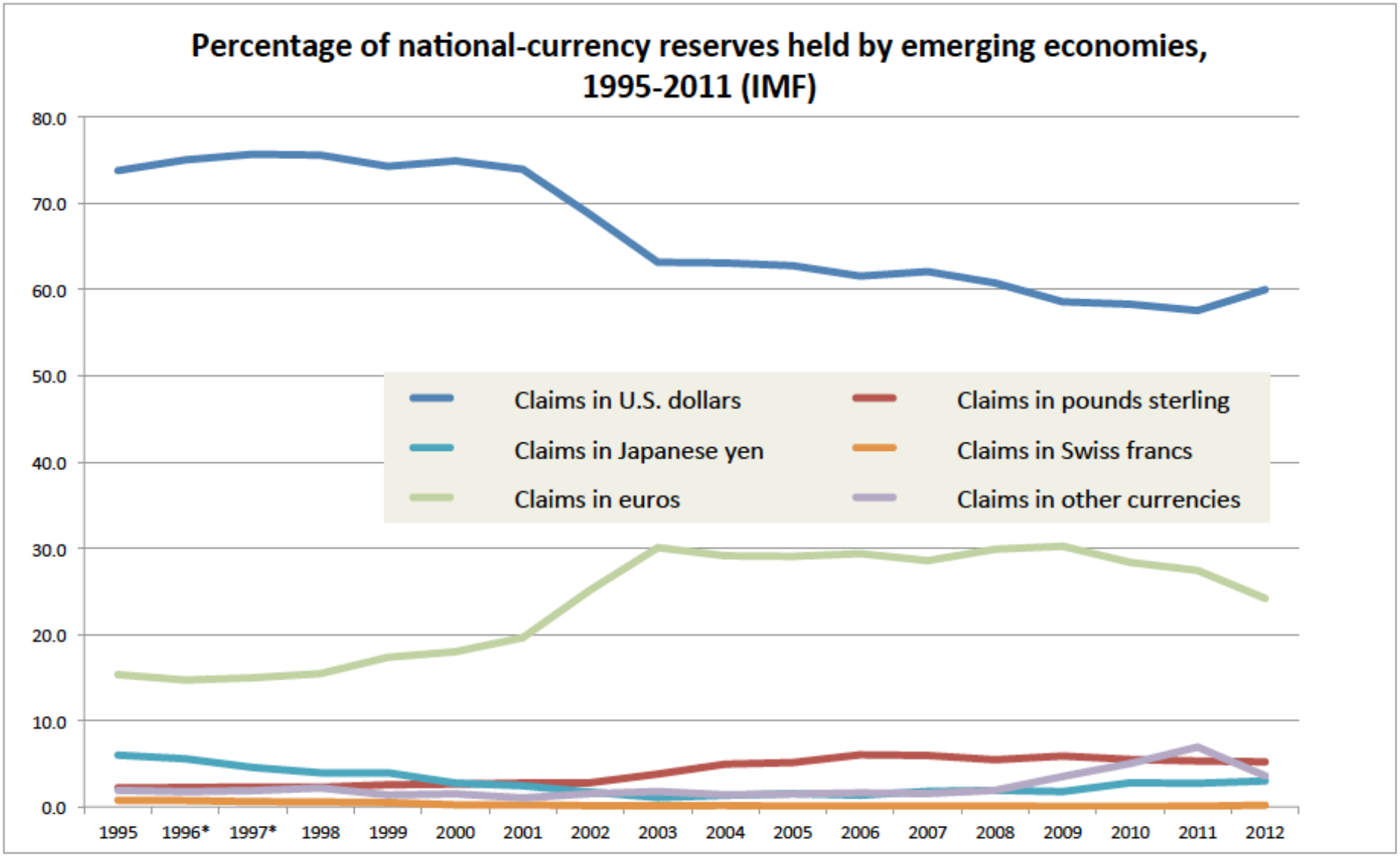
2011
2012
Claims in U.S. dollars
Claims in pounds sterling
Claims in Japanese yen
Claims in Swiss francs
Claims in euros
Claims in other currencies


Percentage of national-currency reserves held by emerging economies, 1995-2011 (IMF)
80.0
70.0
60.0
50.0
40.0
30.0
20.0
10.0
0.0
1995
1996*
1997*
1998
1999
2000
2001
2002
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2004
2005
2006
2007
2008
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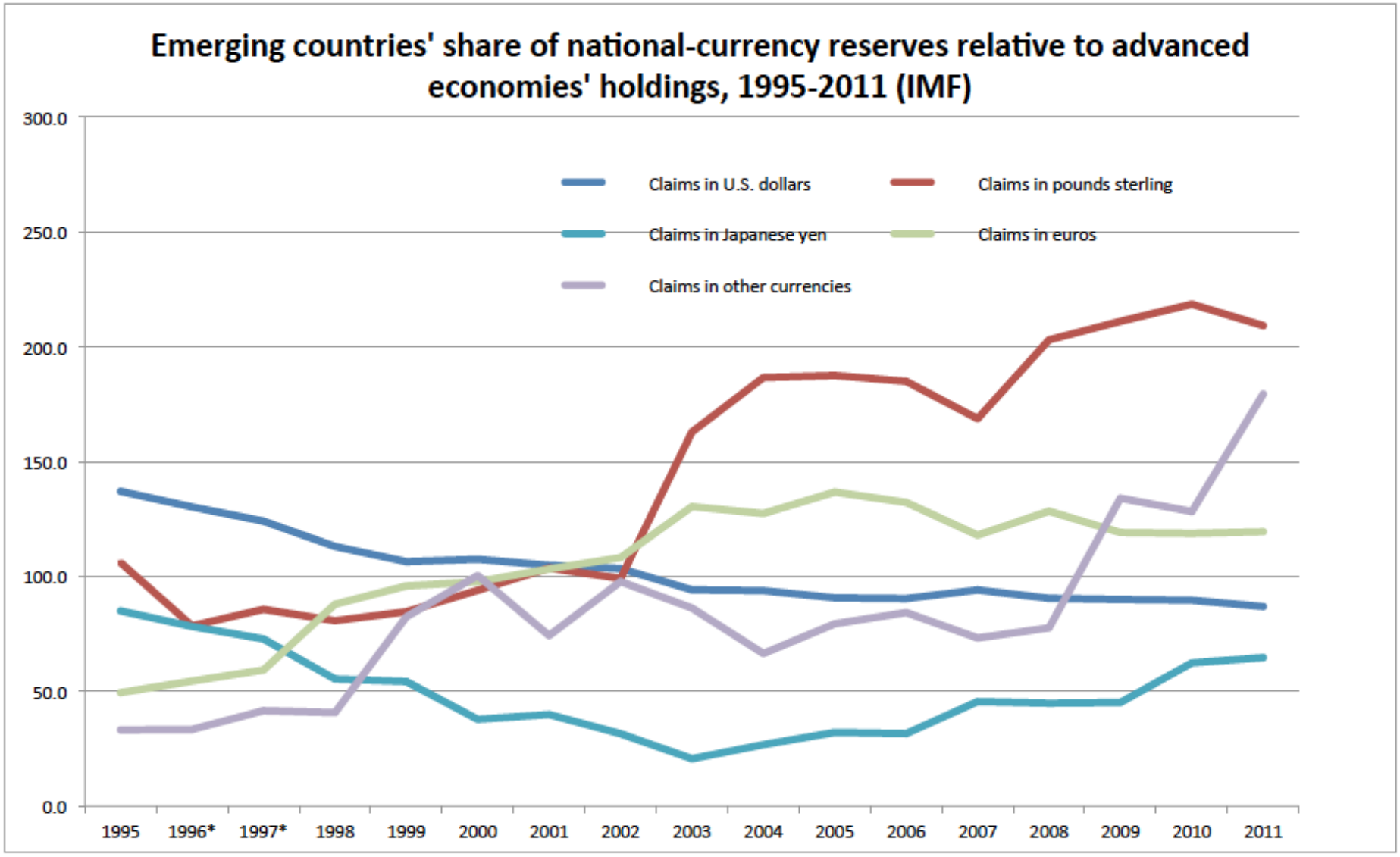
2012
Claims in U.S. dollars
Claims in pounds sterling
Claims in Japanese yen
Claims in Swiss francs
Claims in euros
Claims in other currencies


Emerging countries' share of national-currency reserves relative to advanced economies' holdings, 1995-2011 (IMF)
300.0
250.0
200.0
150.0
100.0
50.0
0.0
Claims in U.S. dollars
Claims in pounds sterling
Claims in Japanese yen
Claims in euros
Claims in other currencies
1995
1996*
1997*
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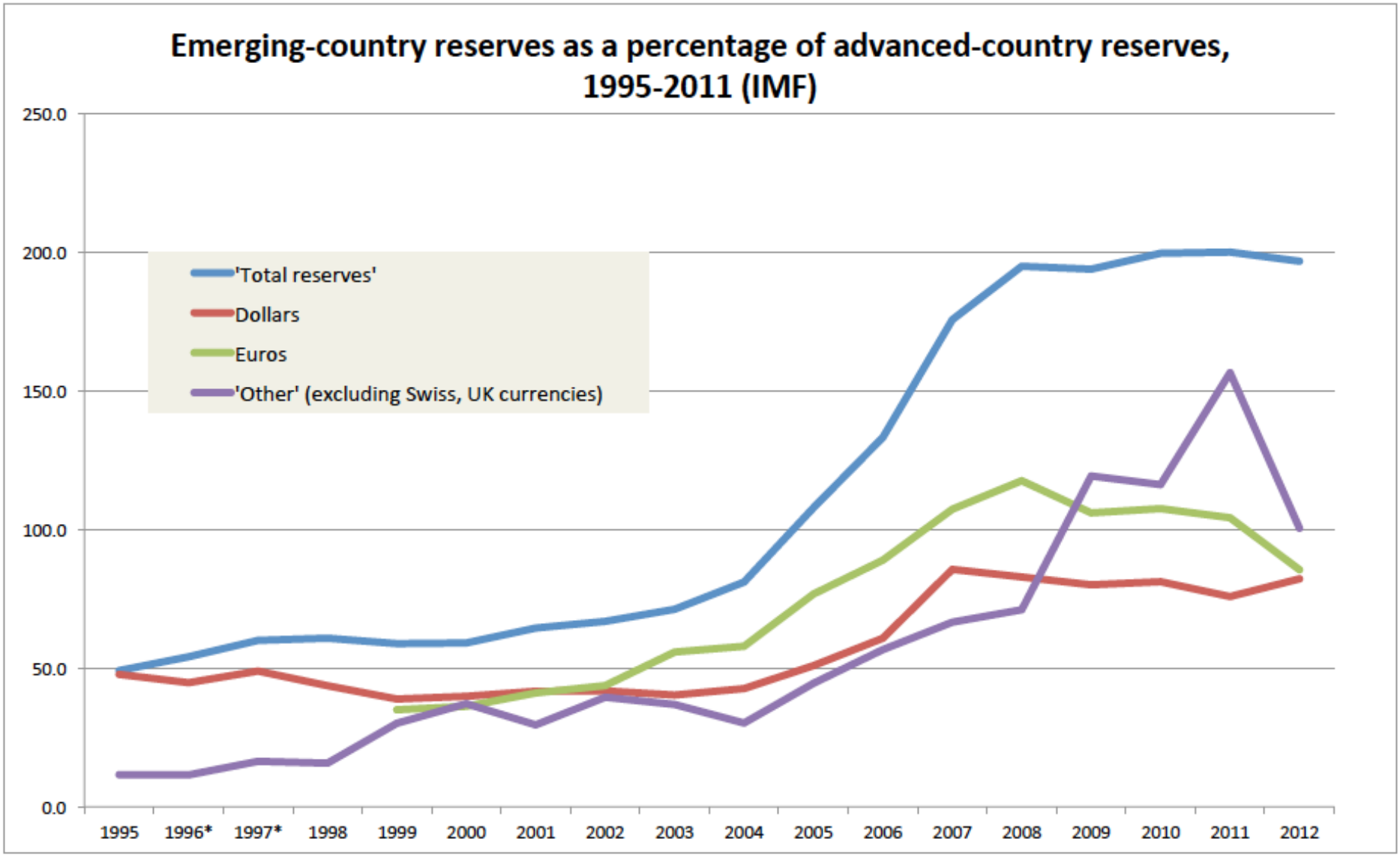
2010
2011


Emerging-country reserves as a percentage of advanced-country reserves, 1995-2011 (IMF)
250.0
200.0
150.0
100.0
50.0
0.0
'Total reserves'
Dollars
Euros
'Other' (excluding Swiss, UK currencies)
1995
1996*
1997*
1998
1999
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012

Is there a 'band' of liquidity, varying from highest for reserve currencies to zero, with some in-between?

			Degree of currency liquidity		
			High		low
Degree of control over cross-border capital mvmts and of economic/ monetary oversight	Free entry of foreign capital	Large reserve base		***here***	
		Small reserve base			***here***
	Controls on capital mvmts	Large reserve base	***Here***		
		Small reserve base			***here***

Another approach to the key question: is it size of reserves or the capacity of a central bank to protect the nation's financial system from a run, that is more important? Again, is it 1-0 - some have it, some don't?

Paper 2: An Asset Price Theory of Exchange Rates, by Priewe

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ER theoretical contexts: paper 2

The "crisis of exchange rate theory" is, first of all, that there is no ER theory per se. It is fit into other boxes:

- Keynes: wary of it, no clear theoretical take
- Purchasing power parity: equilibrium through goods-market arbitrage … vs.
- Portfolio theory: global wealth equilibration
  - If EFM theory is followed, little to say; exchange rates follow underlying conditions…
- Davidson: the elasticity of "unanchored" expectations of cross-border-asset-holding asset owners.
  - Issue of speculation is sidelined here ….

A macro structural approach to exchange rates: Which cross-border flow drives which?

This "GDP/national balance" has a border-crossing term:

$$I + (G-T) = S \mathbf{- (X-M)}$$

Now recall our border-crossing balance:

$$X - M = - S_F + \Delta R$$

Substitute the latter into the former so all the information is captured in one expression. Rearranging:

$$I + (G-T) = S \mathbf{+ S_F - \Delta R}$$

A 'master' equation: "what must be financed" = "what is available to finance it with."

- Every spatial area has to solve this problem, in each time-period. The exchange rate emerges within this nexus; or if it is fixed, transmits 'imbalances' elsewhere in system.

A market-balances approach to cross-border flows: which drives which?

The 'master' equation: "what must be financed" is reinterpreted into "determinants of prices based on available savings/wealth"

$$I + (G-T) = \mathbf{S + S_F - \Delta R}$$

$$S = S(r_1, r_2, \ldots r_{F1}, r_{F2}, \ldots)$$

$$S_F = S_F(r_1, r_2, \ldots r_{F1}, r_{F2}, \ldots)$$

Allocations of domestic and foreign savings across available asset classes, with efficiency achieved when movement is freest; then

$$e = [\Sigma(d_i) - \Sigma(d_{Fi})] - [\Sigma_F(d_i) - \Sigma_F(d_{Fi})]$$

So here we invisibilize the macro-balance problem, and bring into focus the efficient price problem.

- Now we can investigate the behavioral determinants behind the actions of domestic and foreign buyers, focusing on things such as habit persistence, and so on.
- You can add on an equilibrium (structureless) macro framework here

Using a Bayesian Approach to Estimate and Compare New Keynesian DSGE Models for the Brazilian Economy: the Role for Endogenous Persistence*

Marcos Antonio C. da Silveira†

Keywords: New Keynesian models; price indexation; habit formation; Bayesian econometrics.
JEL Code: E32, E52, F41.

New Keynesian dynamic stochastic general equilibrium (DSGE) models have been developed for monetary policy analysis in open economies. For this purpose, the basic model must be enriched with the sources of nominal and real rigidities which are capable of explaining the observed output and inflation persistence. Under this perspective, we use the Bayesian approach to estimate and compare alternative model specifications for the Brazilian economy with respect to two endogenous persistence mechanisms widely supported by the international empirical literature: habit formation and price indexation. Using data for the inflation target period, we conclude for the relevance of both mechanisms, although the evidence is unexpectly less robust for price indexation. Furthermore, impulse-response functions are built to describe the dynamic effects of domestic and foreign real and monetary shocks.

Metroeconomica 62:3 (2011) 434–458
doi: 10.1111/j.1467-999X.2010.04116.x

A BEHAVIOURAL FINANCE MODEL OF EXCHANGE RATE EXPECTATIONS WITHIN A STOCK-FLOW CONSISTENT FRAMEWORK

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University of Ottawa

(July 2010; revised October 2010)

ABSTRACT

The paper combines behavioural finance to a stock-flow consistent model of a two-country economy in the portfolio tradition, with imperfect asset substitutability. 'Conventionalists' and 'chartists' set their expectations of changes in exchange rates based on some assessed fundamental value and past trends, respectively. We find that exchange rate expectations have a significant effect on exchange rate movements and trade account balances during the traverse and in steady states. A flexible exchange rate regime will continue to provide stabilizing properties, as long as the proportion of chartist actors relative to other agents is not overly large.

Using a Bayesian Approach to Estimate and Compare New Keynesian DSGE Models for the Brazilian Economy: the Role for Endogenous Persistence*

Marcos Antonio C. da Silveira†

Keywords: New Keynesian models; price indexation; habit formation; Bayesian econometrics.
JEL Code: E32, E52, F41.

New Keynesian dynamic stochastic general equilibrium (DSGE) models have been developed for monetary policy analysis in open economies. For this purpose, the basic model must be enriched with the sources of nominal and real rigidities which are capable of explaining the observed output and inflation persistence. Under this perspective, we use the Bayesian approach to estimate and compare alternative model specifications for the Brazilian economy with respect to two endogenous persistence mechanisms widely supported by the international empirical literature: habit formation and price indexation. Using data for the inflation target period, we conclude for the relevance of both mechanisms, although the evidence is unexpectly less robust for price indexation. Furthermore, impulse-response functions are built to describe the dynamic effects of domestic and foreign real and monetary shocks.

2008

Exchange Rate Dynamics Redux

Maurice Obstfeld

University of California, Berkeley

Kenneth Rogoff

Princeton University

We develop an analytically tractable two-country model that marries a full account of global macroeconomic dynamics to a supply framework based on monopolistic competition and sticky nominal prices. The model offers simple and intuitive predictions about exchange rates and current accounts that sometimes differ sharply from those of either modern flexible-price intertemporal models or traditional sticky-price Keynesian models. Our analysis leads to a novel perspective on the international welfare spillovers due to monetary and fiscal policies.

JPE, 1995

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What drives international financial flows? Politics, institutions and other determinants ☆

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ABSTRACT

This paper uses a large panel of financial flow data from banks to assess how institutions affect international lending. First, employing a time varying composite institutional quality index in a fixed-effects framework, the paper shows that institutional improvements are followed by significant increases in international finance. Second, cross-sectional models also show a strong effect of initial levels of institutional quality on future bank lending. Third, instrumental variable estimates further show that the historically predetermined component of institutional development is also a significant correlate of international bank inflows. The results thus suggest that institutional underdeveloped can explain a significant part of Lucas [Lucas, Robert E. 1990. "Why Doesn't Capital Flow from Rich to Poor Countries?" American Economic Review (Papers and Proceedings), 80 (2): 92–96. 1990] paradox of why doesn't capital flow from rich to poor countries. The analysis also does a first-step towards understanding which institutional features affect international banking.

Sovereignty Regimes: Territoriality and State Authority in Contemporary World Politics

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2005, Annals of AAG

I propose a concept of effective sovereignty to argue that states participate in sovereignty regimes that exhibit distinctive combinations of central state authority and political territoriality. Two basic conclusions, drawing from recent research in political geography and other fields, are that sovereignty is neither inherently territorial nor is it exclusively organized on a state-by-state basis. This matters because so much political energy has been invested in organizing politics in general and democracy in particular in relation to states. Typically, writing about sovereignty regards sovereignty as providing a norm that legitimizes central state authority. Unfortunately, little or no attention is given as to why this should always entail a territorial definition of political authority and to why states are thereby its sole proprietors. The dominant approach continues to privilege the state as the singular font of authority even when a state's sovereignty may be decried as hypocrisy and seen as divisible or issue-specific rather than "real" or absolute. I put forward a model of sovereignty alternative to the dominant one by identifying four "sovereignty regimes" that result from distinctive combinations of central state authority (legitimate despotic power) on the one hand, and degree of political territoriality (the administration of infrastructural power) on the other. By "regime" I mean a system of rule, not merely some sort of international protocol or agreement between putatively equal states. I then examine the general trajectory of the combination of sovereignty regimes from the early nineteenth century to the present. The contemporary geography of currencies (specifically exchange-rate arrangements) serves to empirically illustrate the general argument about sovereignty regimes. Finally, a brief conclusion suggests that the dominant Westphalian model of state sovereignty in political geography and international relations theory, deficient as it has long been for understanding the realities of world politics, is even more inadequate today, not only for its ignoring the hierarchy of states and sources of authority other than states, but also because of its mistaken emphasis on the geographical expression of authority (particularly under the ambiguous sign of "sovereignty") as invariably and inevitably territorial. *Key Words: states, effective sovereignty, territoriality, sovereignty regimes, dollarization.*

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Dollar hegemony: A power analysis

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ABSTRACT

The dollar has been the world's first currency since the end of World War II, possibly since the inter-war period, and is the leading currency today. A growing chorus of observers believes this dollar-centered order is coming to an end. While much commentary revolves around changes in the distribution of power, measures are only loosely related to the material basis for currency dominance. A proper understanding of the dollar's global role requires a quantitative assessment of the United States' monetary capabilities and currency influence relative to potential rivals. Moreover, while there is general recognition that a shift in power capabilities away from the United States is an insufficient, although necessary, condition for the prevailing currency hierarchy to reverse, there exists no systematic exploration of how power is exercised when converting monetary capabilities into currency influence. This paper offers a systematic assessment of the monetary capabilities and currency influence of all countries in the world as well as an analysis of how the three faces of power sustain dollar hegemony.

In sum, indicators for monetary capability are: a country's GDP output; trade; capital market (including financial openness) and defense expenditures.

Currency influence is a term I use to characterize the extent to which a specific currency is used internationally. Even when greater use of the dollar is due to weak economic fundamentals it is still a sign of the dollar's influence relative to other currencies. For example, when the

In sum, indicators for monetary capability are: a country's GDP output; trade; capital market (including financial openness) and defense e

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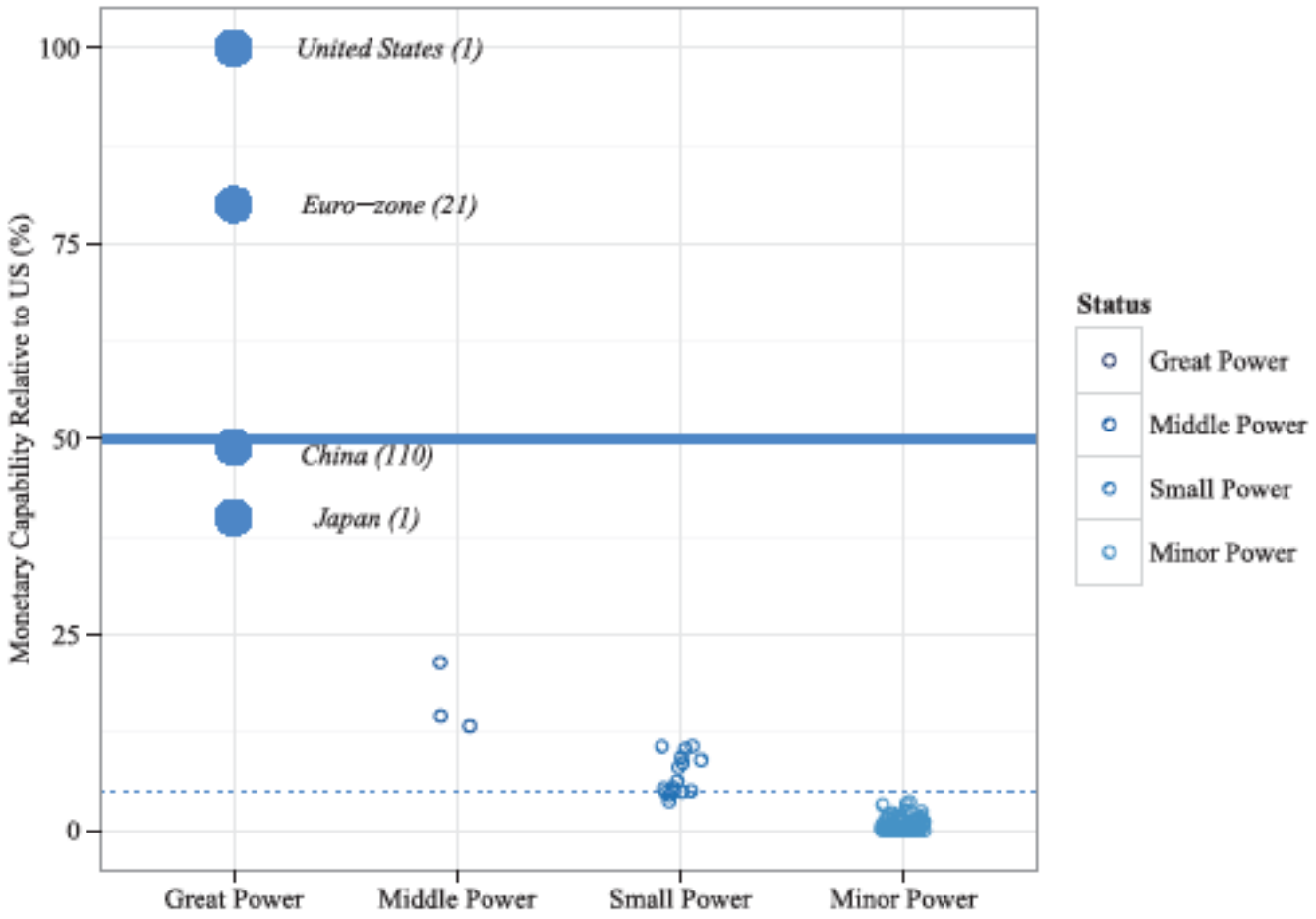

Figure 1 The world's share of monetary capabilities relative to the United States, 2010. *Note*: Rank order of financial openness in brackets using Ito and Chinn (2013).

A Keynesian perspective (Priewe)

Existing approaches …		Market-interaction dynamics	
		Informed/ "efficient" arbitrage	Behaviorally driven, conventions and confidence involved
Macro-structure (including effective demand) important	Exchange-rate fixed in structural model		
	Exchange rate set as a residual effect of structural diff's		Keynes…?
	Exchange rate varies with uncertainty		Davidson

A Keynesian perspective (Priewe)

- A new approach:
  - The financialization of exchange rates
    - Currency risks
    - Derivatives markets
    - Position-taking based on: “trial and error”

A Keynesian perspective (Priewe)

Existing approaches …		Market-interaction dynamics	
		Informed/ "efficient" arbitrage	Behaviorally driven, conventions and confidence involved
Macro-structure (including effective demand) important	Exchange-rate fixed in structural model		
	Exchange rate set as a residual effect of structural diff's	*PPP-"Funda-mentals"*	Keynes…?
	Exchange rate varies with uncertainty		Davidson ***Trending, trial and error***

Misalignment, multiple equilibria arise from this tension