Atlanta Fed Conference Policy session 3: The US dollar in the international financial system

Antoine Martin
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Antoine Martin
Member of the Governing Board
Swiss National Bank
Outline of talk

• Brief remarks on Robert McCauley’s paper
• Importance of US dollar funding for non-US GSIBs
• Some aspects of SNB’s handling of Credit Suisse liquidity crisis in March 2023
• Central bank swap lines and FIMA repo facility as sources of liquidity backstop
• Preliminary lessons learned
Remarks on “The offshore dollar and US policy” by Robert McCauley

– Chronicle joint evolution of (very large) offshore US dollar money markets, esp. eurodollar markets, and of policy measures taken to stabilize market functioning

– Main thesis: System of CB swap lines supports functioning of offshore dollar money markets, in part by strengthening ability of foreign CBs to act as LoLR

– Agree with Bob’s main thesis

– This presentation: Complement Bob’s analysis by discussing a recent use of the Fed’s Foreign Institutions and Monetary Authorities (FIMA) repo facility
Two suggestions on Bob’s paper

1) Add a mention of post-9/11 use of swap lines between Fed and ECB

2) Clarify the purpose of the swap lines:
   − Primary purpose of swap lines: “counter severe global dollar funding strains”
   − Not designed to enable Fed to act as the international Lender of Last Resort (LoLR)
   − Instead: The swap lines and similar facilities enable other central banks to act as LoLR
How do central banks exercise their Lender of Last Resort function?

- Basic recipe for containing banking crises since 1873:
  - Bagehot’s Rule: “Lend quickly and freely, at a high rate, against good banking securities”
- Bagehot’s Rule still applies, but with a crucial adaptation for GSIBs: “lend freely” not only in the home currency but in other currencies, and especially in US dollars
Some aspects of the Credit Suisse (CS) crisis of March 2023

− At the end of 2022, CS was (still) one of the 30 GSIBs
− Like the other GSIBs, CS funded itself not only in Swiss francs but also in many other currencies, including the US dollar
− In March 2023, CS experienced a deep crisis of investor confidence and a sharp run on its deposit base
− By 20 March 2023, SNB had provided CS with CHF 168 bn equiv. (USD 182 bn equiv.) in emergency liquidity. Almost half of the total was disbursed in USD
− SNB relied mainly on Fed’s FIMA repo facility to source USD liquidity
Foreign Institutions and Monetary Authorities (FIMA) repo facility

- First set up in late March 2020, at height of money market turmoil caused by Covid pandemic
- Extended twice, and made permanent in July 2021
- Account holders: Central banks and foreign institutions
- Obtain temporary dollar liquidity by engaging in repos with the FRBNY
- Collateral: U.S. Treasury securities
- So far, FIMA has been used heavily only once
Key differences between CB swap lines and FIMA repo facility as liquidity backstops

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<th>CB swap lines</th>
<th>FIMA repo facility</th>
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<tr>
<td>Membership</td>
<td>Limited set of central banks</td>
<td>Open to a broader group</td>
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<tr>
<td>Purpose</td>
<td>Ease strains in global funding markets</td>
<td>Alternative source of US dollars to asset sales</td>
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<td>Security/Collateral</td>
<td>Currencies of CBs engaged in the swap. E.g., EUR or JPY vs USD</td>
<td>U.S. Treasuries</td>
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<td>Delivery time</td>
<td>T+1 (T+0 <em>may</em> be possible)</td>
<td>T+0 <em>guaranteed</em></td>
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<td>Currency; Provider of</td>
<td>In principle, currencies of all participating central banks</td>
<td>US dollar; Federal Reserve</td>
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<td>liquidity</td>
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Preliminary lessons learned from the CS crisis

- Exercising the LoLR function over a GSIB can involve having to provide prodigious amounts of liquidity in both the home currency and in US dollars
- Importance of assuring operational readiness and well-established lines of communication at operational level, for both the initiating CB and the Fed
- Advantages of FIMA repo facility: “no questions asked”, no “stigma”, open to a broader set of central banks
- Not related to Bob’s paper but important: Wholesale funding of banks can dry up much faster than most regulatory models assume is the case
Thank you for your attention.