

Worrying Implications of “Libra” for the International Monetary System

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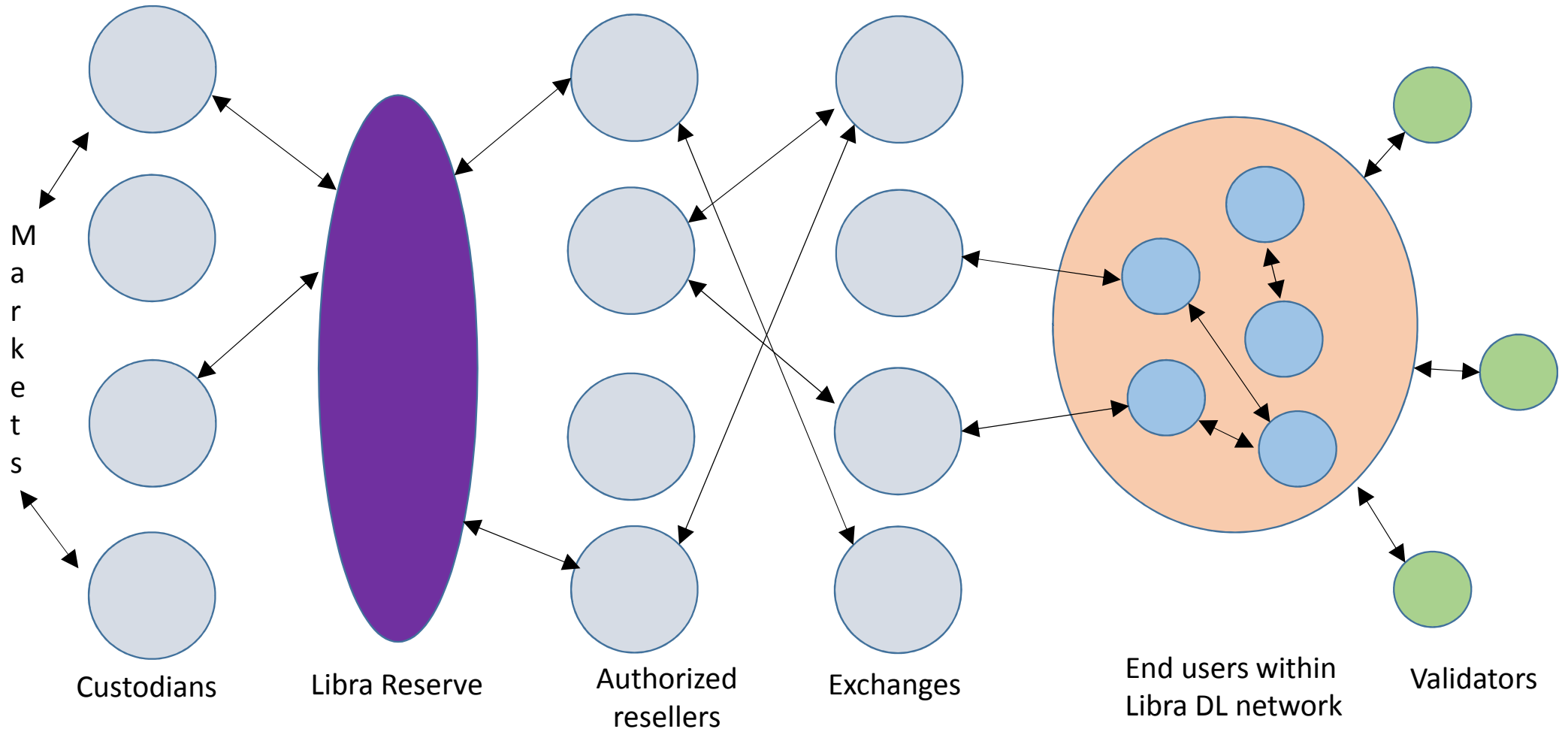
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Facebook's promise

To build on its network to sponsor:

- “a simple global currency and financial infrastructure that empowers billions of people”
- “designed and governed as a public good”
- “its value will remain relatively stable over time”
- “fully backed by a reserve of real assets” – floating NAV mutual fund
- “freedom to easily transmit funds across borders” – important in view of high costs and low speeds of cross-border payments, high costs of remittances
- “new opportunity for responsible financial services innovation”

Ostensible Libra architecture



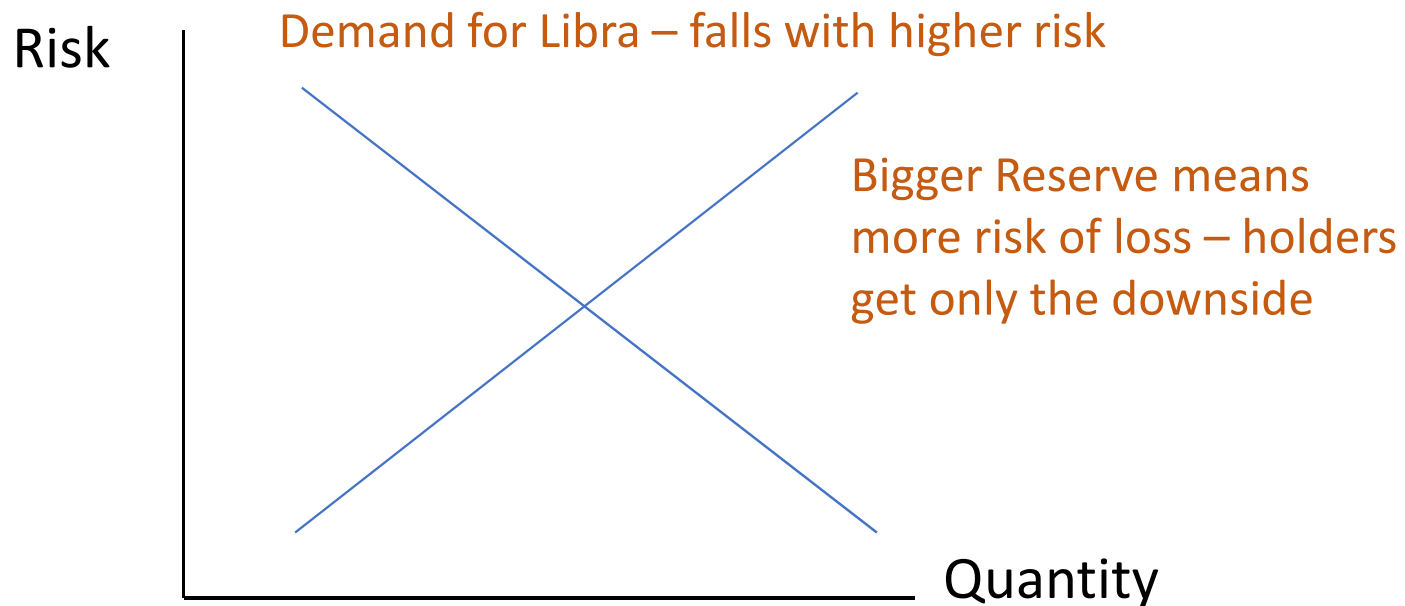
Promise versus reality?

- Faster, frictionless solutions within currency areas are evolving quickly – e.g., PSD2 and TARGET Instant Payment Settlement (TIPS) in Europe, India's Unified Payment Interface; real or “synthetic” CBDC?
- Apart from some retail capability (Paypal's Xoom), cross-border payment and settlement remains problematic
- Coordination between national systems would require intergovernmental coordination on interoperability, regulation, etc. – how likely today?
- For international currency-to-currency transfers, unclear how much going through Libra will reduce costs (see the previous slide). Netting mechanism?
- Only within the Libra loop is payment transfer frictionless, but ...
- For larger countries, domestic payments and money will continue dominant, especially as Libra fluctuates vis-à-vis major currencies – but: constraints on negative policy rates?
- If MMFs build on system to offer interest on “idle” Libra, consumer risks rise

Risks

- It is smaller, poorer, more open economies that risk Libraization
- This is colonization: Facebook can better extract revenues to exploit its large user base in these countries – where otherwise, advertising revenue is low – countering their growth challenges in advanced economies
- Policy discipline on poor-country governments? But also (i) less effective monetary policy and (ii) risk of multiple-equilibria currency runs
- Libra reserve will be held in “safe” assets including short government bonds – risks exacerbating global safe asset shortage, lowering world r^*
- Per DB, ~27% of global bonds have negative yields – though US dollar bonds will dominate, Libra Reserve will be tempted into riskier assets
- Will Libra Reserve balance sheet be “auditable and transparent”? Portfolio rebalancing could destabilize markets, worsen potential for self-fulfilling events, create risk of front-running
- Temptation to leave “narrow banking” model?

Equilibrium Libra supply?



- Q will be inefficiently big, since individual holders will not internalize their actions' effects on the riskiness of the Libra Reserve portfolio
- Just adds to a strong case for regulation – with cross-border coordination