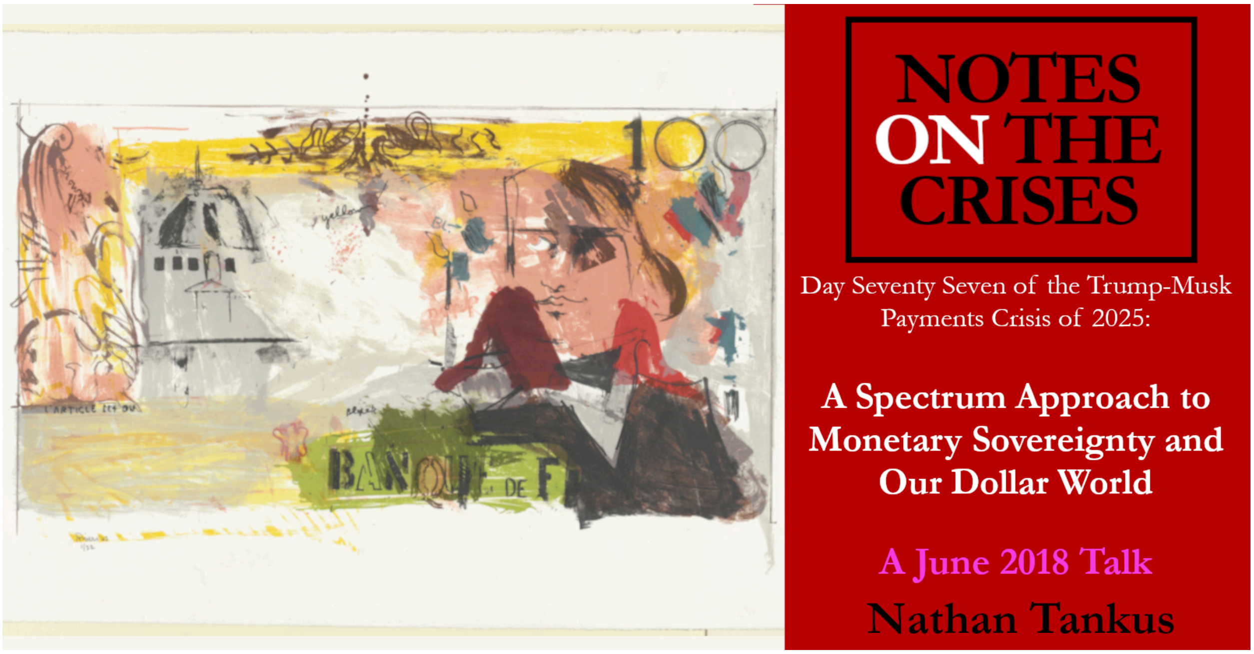
University of Manchester June 2018 talk

Monetary Sovereigns, Monetary Subjects and Monetary Vassals: A Spectrum Approach to Monetary Sovereignty and Our Dollar World



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Hello everyone. It is an absolute pleasure to be here and to be invited to talk on such an interesting and exciting topic- well, at least to me. The classic joke about economics was made by Lyndon Baines Johnson to John Kenneth Galbraith. He said "Did it ever occur to you that making a speech on economics is just like pissing down your leg? It seems hot to you, but not to anybody else?". There's always a danger of that, especially with more specialized topics, but I hope that by the end of my talk you can see the importance of a legal political economy analysis of international monetary economics to the world around you.

It may not be obvious why money is important to international public law, but I think it is crucial. Most discussions of international public law have money and financial relationships as their background. Further, as I'll discuss below, international public law structures the international currency hierarchy in all sorts of ways. On a practical level, discussions of free trade agreements and other such arrangements are always happening in the context of discussions of the "special role" of the dollar. The obvious question that emerges here is how the dollar's special role- labeled dollar hegemony- comes about and I think the answer is in large part the history of international public law and its ongoing structuring of these relationships. My point of view here is coming from an economic- and legal- school of thought called Neochartalism. Thus I should say something about what's relevant in this theory to discussing international monetary economics

The crucial starting focus for a Neochartalist is an inquiry into what monetary objects and/or biophysical resources are receivable in payment of non-reciprocal obligations- whether they be wergild, taxes, fines, fees or tort liabilities. Receivability is just a fancy legal term for what you can pay some obligation with. From there the viewpoint expands to formally reciprocal obligations from bridewealth and student loans to purchasing a metrocard. Most histories of money- which are usually just histories of coinage- do not have this crucial focus and thus don't give a clear idea of how the monetary system under discussion works. In other words, a Neochartalist monetary analysis must begin with the receivability laws. While there is still a lot of history that has yet to be reassessed from a Neochartalist point of view, I have confidence in the power and importance of Neochartalism from my own explorations of the American monetary system from the 16th century to the Civil War.

After examining receivability Neochartalists expand their focus to the process by which monetary objects are created. This is where a focus on monetary sovereignty takes place. By making its own IOUs receivable in payment of taxes and other obligations owed to the state- or "private" actors- a state can gain some degree of monetary sovereignty. The extent and power of that monetary sovereignty depends on the institutional structure of the economy and the international arrangements the state in question has entered into. At this stage it is important to note that it is receivability in general that "back" money and not any particular amount of tax revenues. Thus there is no monetary or tax constraint on the level or composition of deficit spending. The constraint is, as I said above, the institutional structure of a national economy- including its institutional arrangements with the rest of the world. What I want to focus on is the constraints that emerge in the arena of international public law.

In order to do that though, I need to make some more general points about monetary sovereignty in a globalized world. Part of what I think hobbles the discussion of monetary sovereignty is that too often monetary sovereignty is treated as an "either or" proposition. You either got it or you don't. This is odd foremost because such a boolean point of view is becoming less and less popular about money itself. The perspective that has emerged from the last decade, including getting more popular among mainstream economists, is that treasury bonds are "safe assets" in a similar way to central bank settlement balances or physical cash, as well as bank deposits for smaller actors, and one way to talk about this is to speak of the degree of "moneyness" of different financial instruments. In short, what is changing is the treatment of money as a noun towards a point of view that treats money as an adjective. If we see moneyness as a spectrum that different financial assets fall under with some items at the top hierarchy and others closer to the bottom, why not approach monetary sovereignty the same way?

A spectrum approach to monetary sovereignty also emphasizes the inherent interdependency of monetary sovereignty in a globalized world. When you take a receivability point of view in tandem with a balance sheet point of view, dollar hegemony and dollarization are one and the same thing. What I mean is that to say the U.S. has a number of corporations, countries and households who have dollar denominated debts outside of its border is to say that a number of monetary sovereigns have been curtailed in some way. This is even getting more mainstream reporting. Greg Ip at the *Wall Street Journal* recently reported on how the rising dollar exchange rate and rising u.s. Interest rates are squeezing a number of countries whose corporate sectors have heavy dollar denominated debt.

It is the extraordinary amount of dollar denominated debt which at once raises the monetary sovereignty of the United States above all others and pulls down the monetary sovereignty of other countries. This is what makes the U.S. the currency hegemon. Thus, anything that leads to more dollar denominated debts strengthens dollar hegemony and moves away from dollar denominated debt weakens dollar hegemony. However, it would take a truly massive structural change to the way international economics works to transform the current pattern of currency debts such that the U.S. was no longer the currency hegemon. This also means that, from a Neochartalist point of view, reserve currency status is an effect, not a cause, of dollar hegemony. Just as domestically people are willing to save in dollars even if they don't personally have many dollar debts or even pay taxes because they know so many others accept dollars in payment, internationally countries are willing to accumulate dollars because they know dollars are internationally acceptable.

To push forward this analysis I would recommend we expand our vocabulary beyond monetary sovereignty. The first term I'd introduce, which my colleague Raúl Carrillo has emphasized recently, is the term monetary subject. Monetary subject is a way of speaking about the fact that individuals who live in a certain country that issues a certain currency and imposes all sorts of obligations onto us in that currency have a subordinate relation to that monetary sovereign. The monetary sovereign makes the money rules, we just play its game. There are also Monetary vassals, Monetary subjects to one sovereign that, with some degree of voluntarity, pledge themselves to another by taking on foreign denominated debts. This can be an importer who takes on euro denominated trade credit or a corporation seeking supposedly lower interest rates abroad. Finally, there are monetary tributaries, states who obligate themselves to another state as part of a treaty or in order to achieve an objective they think requires foreign currency. It is the monetary tributaries that are clearly the most important to understand from the point of view of international public law.

Another thing that becomes obvious when you put on this analytical lens is that imposed non-reciprocal obligations are not just a matter of monetary sovereigns and monetary subjects. History is replete with examples of States imposing obligations on each other. From the Franco-Prussian war of 1871 to the Boxer Rebellion to, most famously, World War I German reparations, imposed obligations on states have structured monetary sovereignty for potentially thousands of years. In fact, in some ways the international currency hierarchy and its interdependent nature is most obvious in the case of reparations. The losing nations are under an additional burden of a foreign currency denominated debt and the winning ones have a new international backing for their currency. Public law of course does this in less overt ways, such as the *Agreement on Trade-Related Aspects of Intellectual Property Rights* or TRIPS agreements. For countries that are "intellectual property poor" TRIPS imposes a non-reciprocal obligation on them, that they in turn impose on their populations, to not violate international property rights regimes. Further, to get access to those properties they most often need to pay in dollars.

Meanwhile, while the monetary imposition of reparations is a historical topic of interest for understanding international currency hierarchies, monetary tributaries have not gone away. They exist to this very day. One radically under-discussed monetary tributary is the French Colonies of Africa Franc, I mean the African Financial Community Franc (I am sparing you all an american attempt at french pronunciations) i.e. the CFA Franc. Sometimes the difference between colonialism and neocolonialism is exceedingly thin. From the colonial era through the 1990s this monetary union was pegged to the Franc. It then became pegged to the Euro in the transition to the Eurozone. To this very day, the currency reserves of this monetary union are on deposit at the French Treasury. I should mention that 18 months ago a book came out in French entitled *Liberate Africa from Monetary Servitude: Who Profits from the CFA Franc* co-authored by Kako Nubukpo.

Of course, focusing too much on a particularly glaring modern example of a monetary tributary distracts from the main issue- countries in intermediate situations where they're not so overtly pledged to another country or region but nonetheless operate under geopolitical constraints including agreements like TRIPS. We have gotten a lot of discussion of this recently in the past few years as its increasingly recognized that a number of countries have escaped dollar denominated public debts but have corporate sectors with particularly high dollar denominated debts. This puts a lot of pressure on the balance of payments since, as economist Felipe Rezende has pointed out in the Brazilian context, large foreign denominated debts taken today are large flows of interest payments tomorrow. If you forcibly converted monetary vassals into full domestic monetary subjects by redenomination a fall in the exchange rate would reduce interest payment flows relative to foreign denominated income coming in from abroad. By this I simply mean that when the exchange rate changes and you look at everything from the domestic currency point of view, exchange rate movements have no impact on the size of Brazilian Real debts but do increase the domestic size of foreign denominated income. But redenomination or any other kind of legal change that impacts existing debts brings the threat of geopolitical censure and retaliation. After all, the degree of monetary sovereignty is related to the degree of sovereignty itself.

There are a number of different directions the lens of a "spectrum of monetary sovereignty" provides but I will focus on one I think is the most relevant to an international public law audience- financial regulation and other financial policies in the context of international agreements and geopolitical. Clearly, this point of view posits that preserving and expanding monetary sovereignty is a valid and important goal for financial regulation. What policies pursue that end? Attacking the domestic creation of foreign denominated bank deposits is key. Local deposit insurance systems can easily provide for domestic obligations but being responsible for foreign denominated obligations can cause problems. Additionally, not having domestic issuance of foreign denominated monies makes it more difficult for domestic residents to "run" from the local currency. More generally, making foreign denominated debts less domestically protected is an important avenue. On the flip side, making domestic credit more attractive is a way of "competing" with foreign debt. Felipe Rezende has written about how expansions of the Brazilian public development bank's lending displaced some of the desire to seek dollar denominated loans. This opens the question of whether high local interest rates are really an effective way of defending the exchange rate as is commonly believed. Another strategy would be lowering the priority of foreign denominated debts in bankruptcy as well as taxing the origination of new foreign denominated obligations. The trouble as I said earlier is that the more a country attacks the legal enforcement of private foreign denominated debt, such as through lowering its priority in bankruptcy, the more it risks retaliation on the basis of political arguments over expropriation, as well as other less overtly political mechanisms.

Analyzing which strategies for defending or expanding domestic monetary sovereignty incur foreign political risks and how dangerous various different foreign reactions are is an entire area of legal political economy study of extreme importance. There is also an important fallacy of composition to avoid. While it may be the case that some developing countries can advance their monetary sovereignty sufficiently to do major political emancipatory programs, in our current geopolitical context I don't think it's possible for all of them to do so without major political changes in the United States. Dollar hegemony is crucial to the U.S.'s role. Even if some individual suites of policies weren't seen as a threat, the U.S. would eventually intervene to disrupt this process of independent development if it got "too far". To see both the possibilities and limits I think Neochartalism provides the appropriate lens.

The other important arena for international public law is to examine agreements that are supposedly about "free trade" through this lens. There have already been discussions of how things like Investor State Dispute Settlement tribunals reduce sovereignty but from this point of view they also attack monetary sovereignty. As far as I've been able to tell, ISDS liability is all denominated in dollars. Thus from a Neochartalist point of view ISDS is a powerful tool for preserving and strengthening dollar hegemony and puts countries that otherwise have been able to avoid foreign denominated debts in compromised positions. Even if the absolute dollar amounts have not been extremely large in relation to the size of the economies under discussion, the fact that any potential policy change can possibly incur dollar denominated debts changes the policy arena markedly. On the other hand, the more governments try to resist the elements of multilateral agreements like TRIPS or free trade agreements with ISDS in order to protect and advance monetary sovereignty, the more they risk being isolated internationally which has its own economic problems- particularly around international supply chains (which I haven't discussed much but would be happy to discuss more in the Q and A).

Finally, and I really mean finally, foreign denominated trade credit and medium term sources of foreign credit may be necessary for ongoing trade relations. If that's ultimately the case there are strong reasons to want a central clearing entity to manage these relationships and prevent the occurrence of monetary vassals. Examining the history of Regional Payments Unions and Clearinghouses from a Neochartalist point of view is key to bringing that project forward. These arrangements were and are a form of international public law but I think they have been relatively neglected as money itself has been neglected. I'd like to end by saying that while I've pointed a number of areas that need more work, particularly legal work, but there has also been a lot accomplished- especially in the last decade-, and the true power of Neochartalism in my view is all the things that are ripe to be rethought in its context. Thank you.