

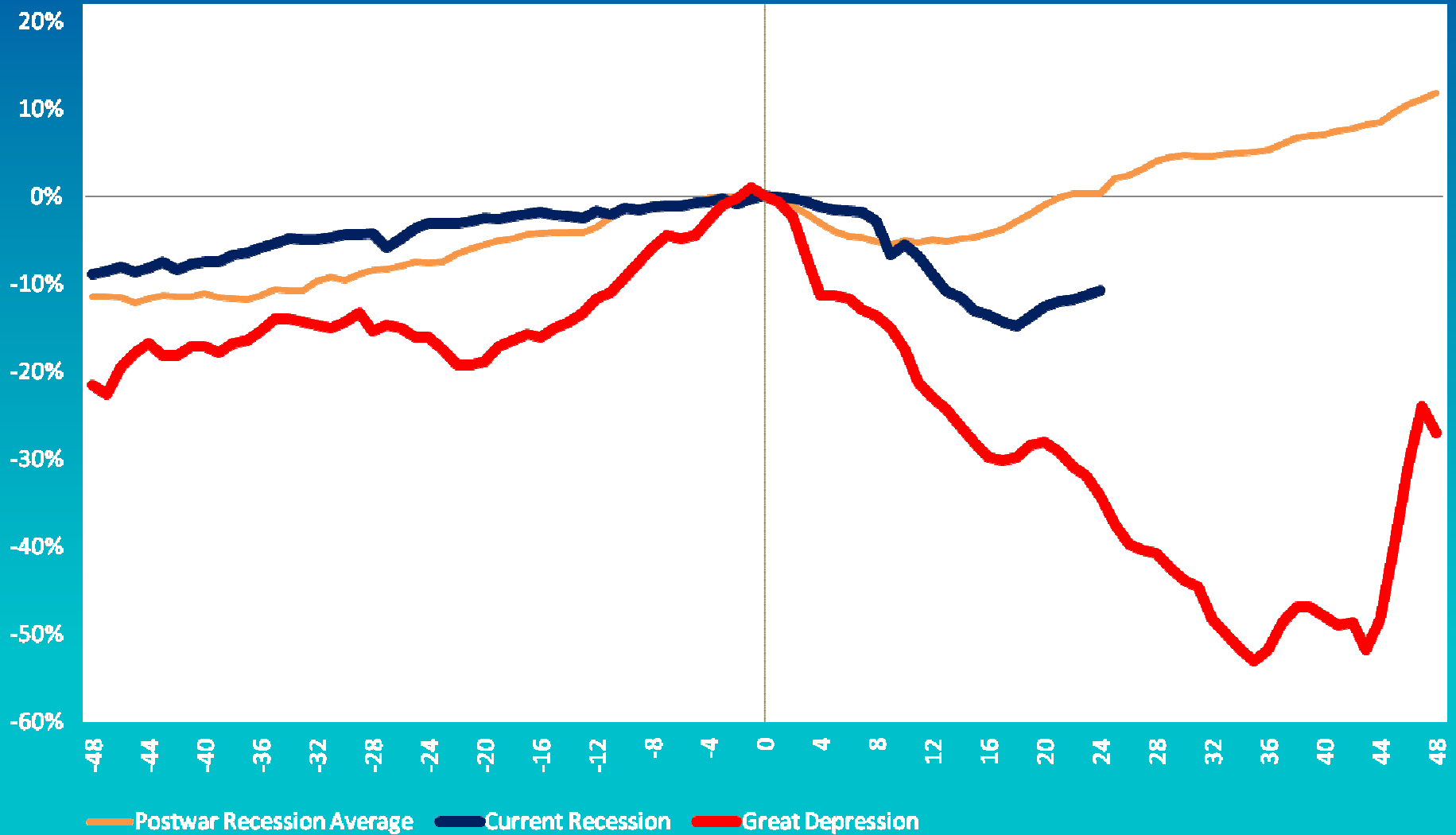
# The Dollar Dilemma

Dr. Benn Steil  
Council on Foreign Relations

26th Annual CBOE Risk Management Conference  
Naples, Florida  
March 8, 2010

# Industrial Production

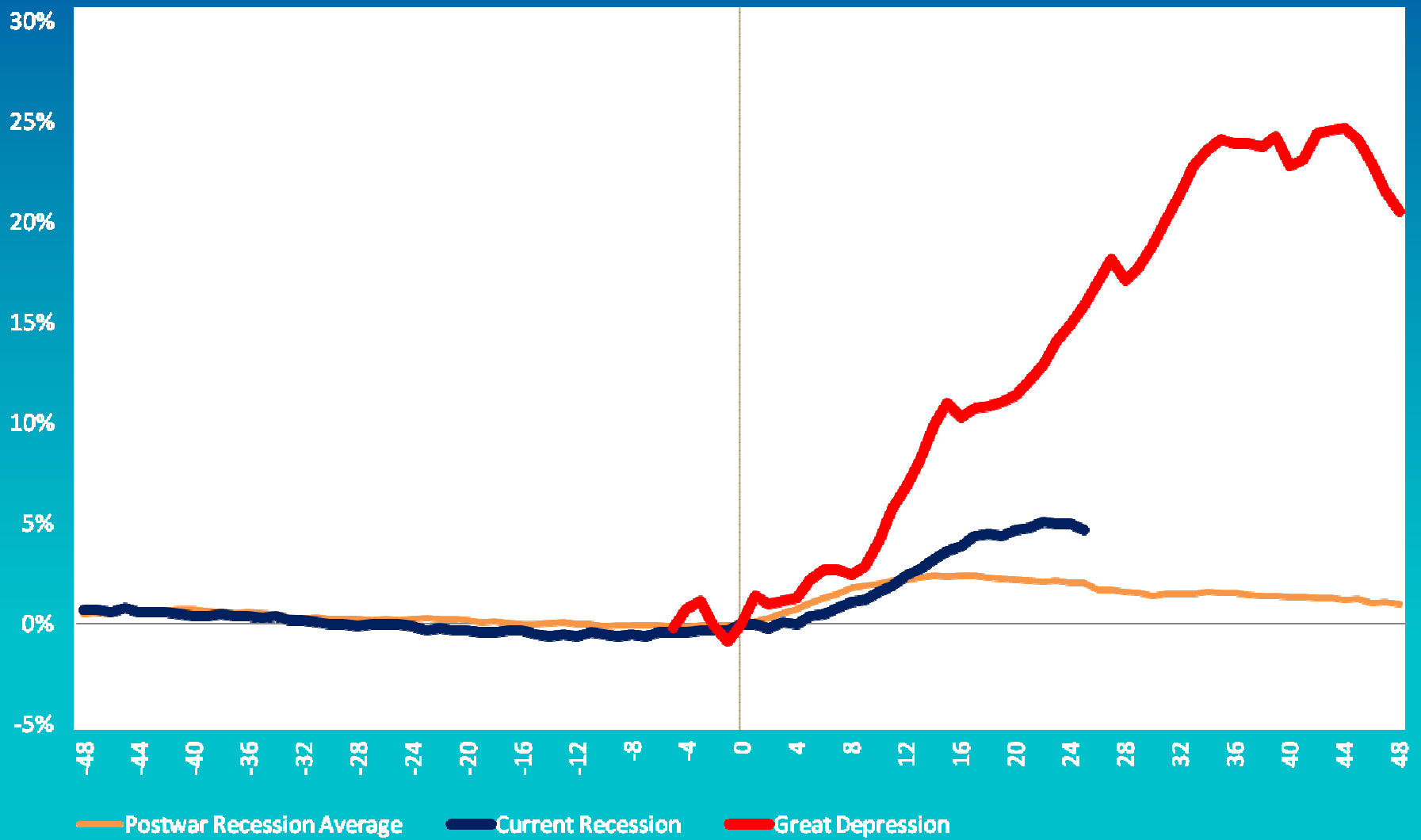
## Relative to Start of Recession



Data Sources: Federal Reserve Board, National Bureau of Economic Research.

# Unemployment

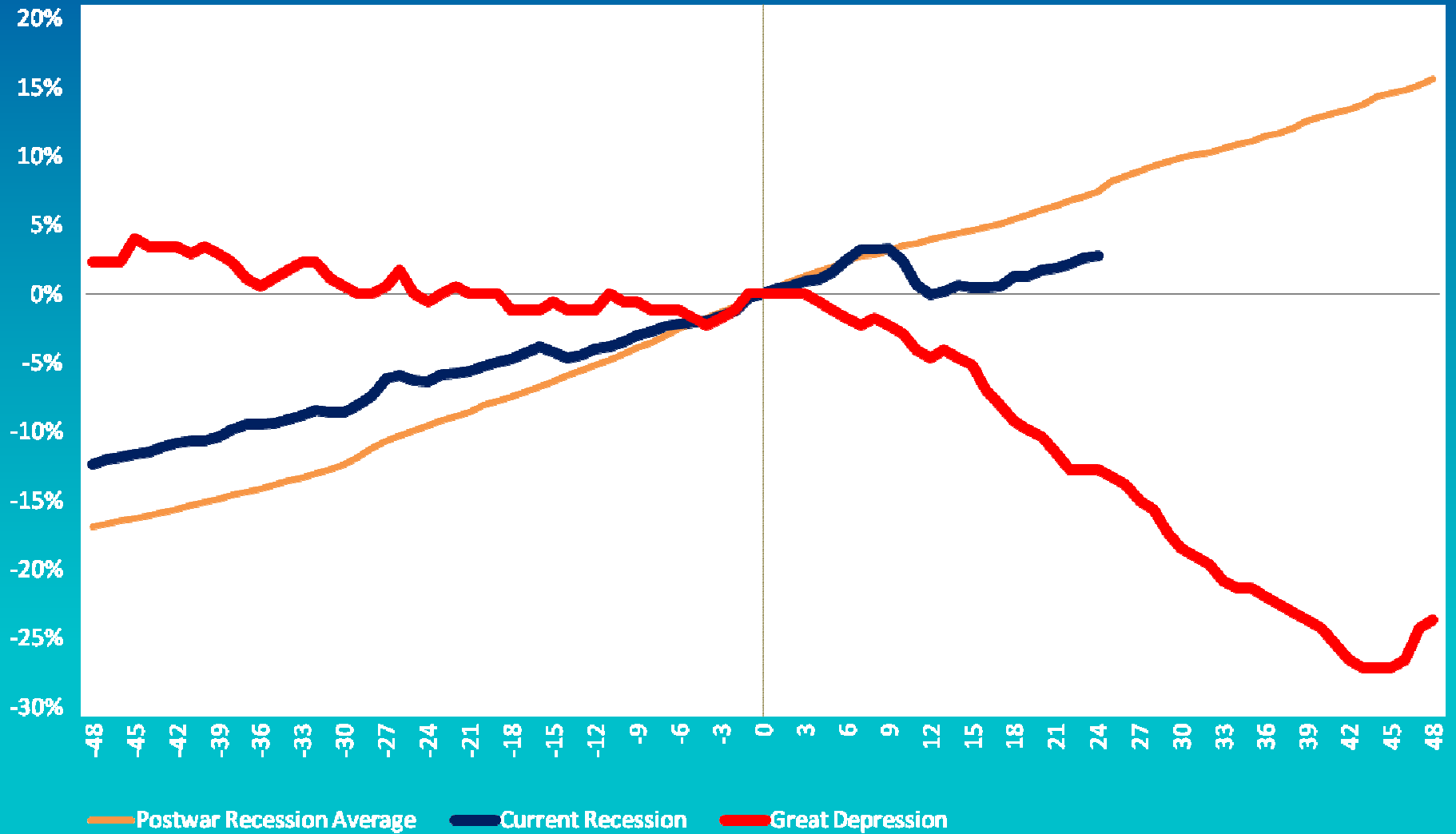
## Change in Unemployment Relative to Start of Recession



Data Sources: Bureau of Labor Statistics, National Bureau of Economic Research.

# Inflation

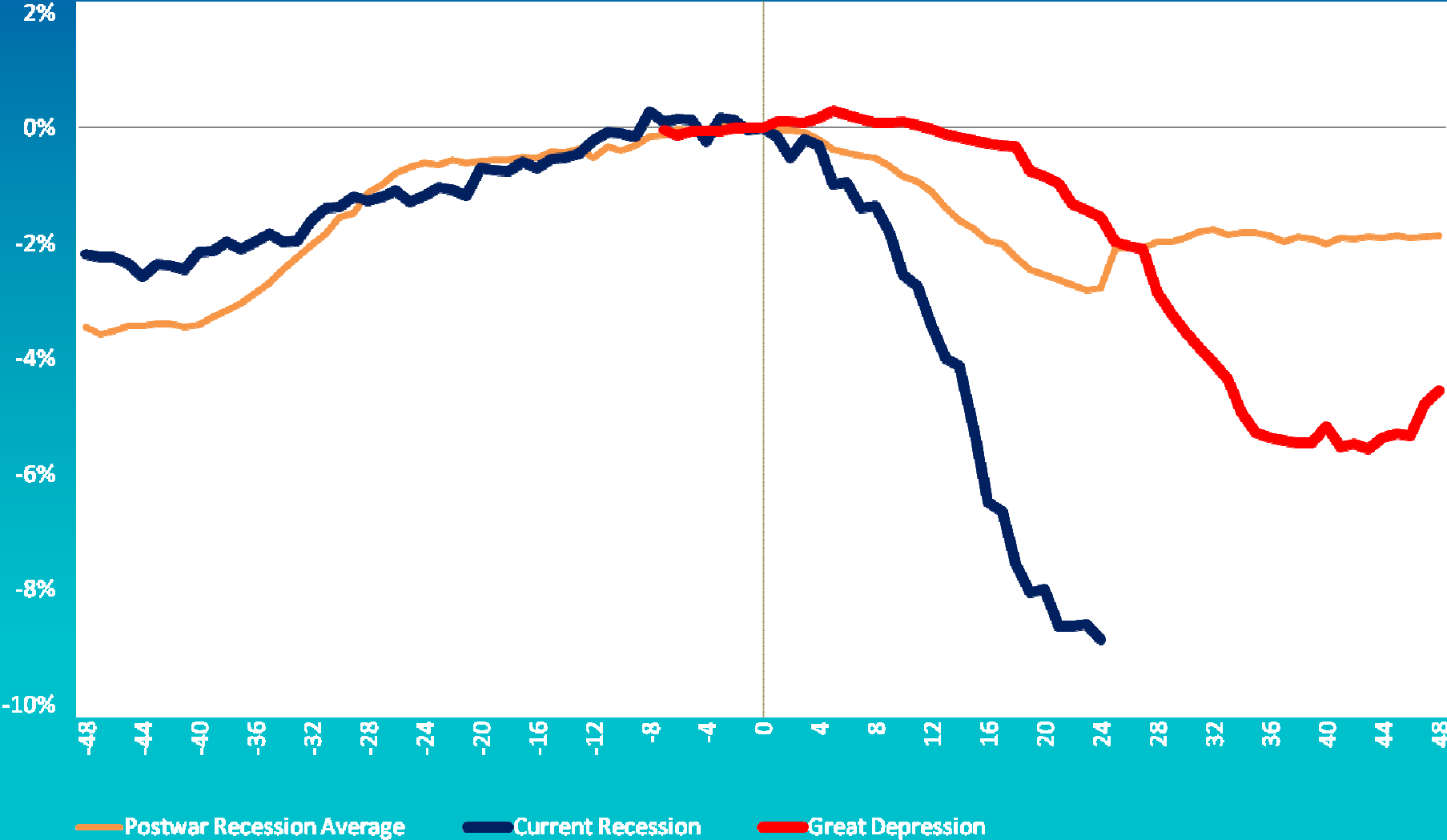
Price Level Relative to Start of Recession



Data Sources: Bureau of Labor Statistics, National Bureau of Economic Research.

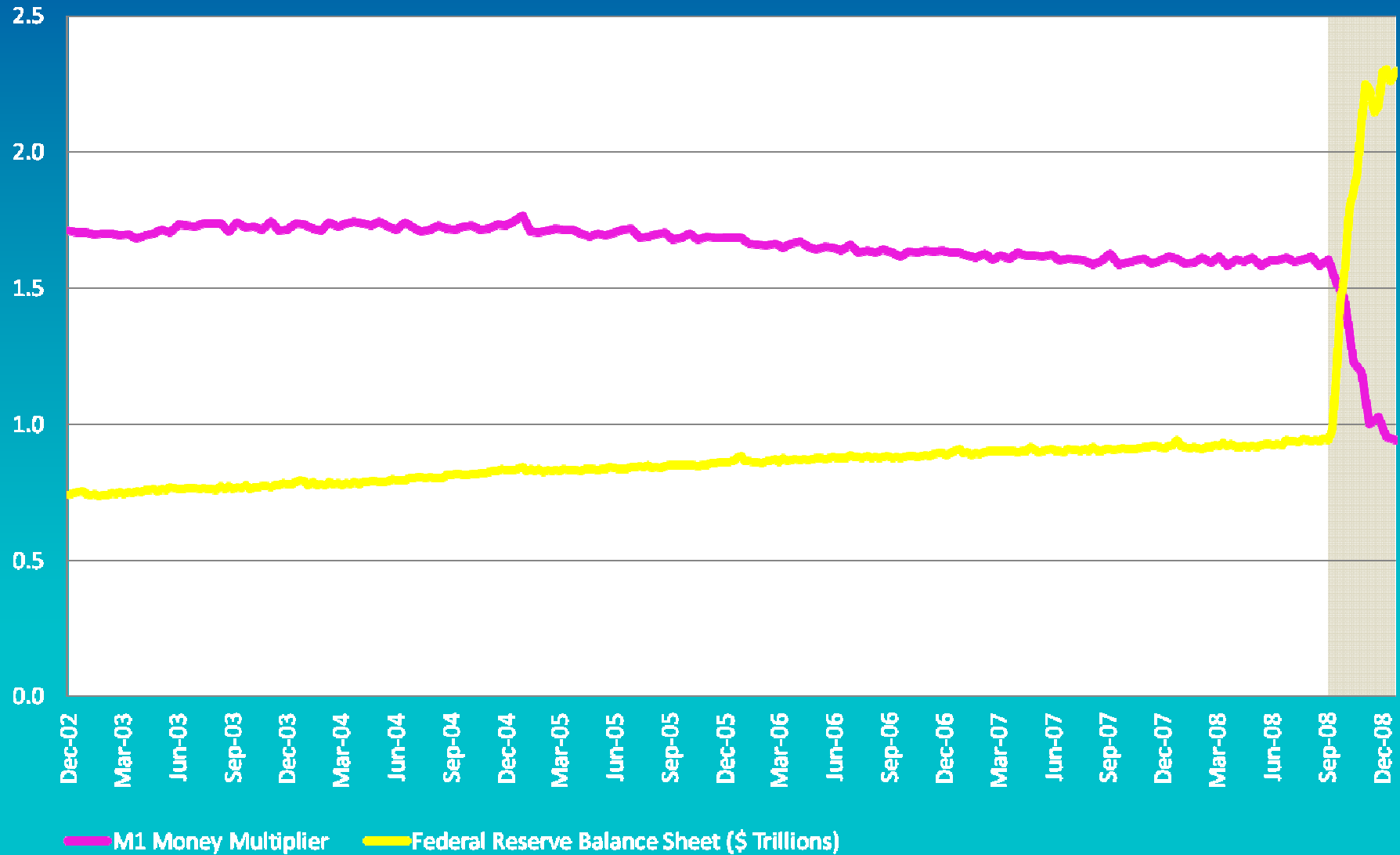
# U.S. Federal Budget

Deficit Relative to Start of Recession, % of GDP



Data Sources: U.S. Treasury, National Bureau of Economic Research.

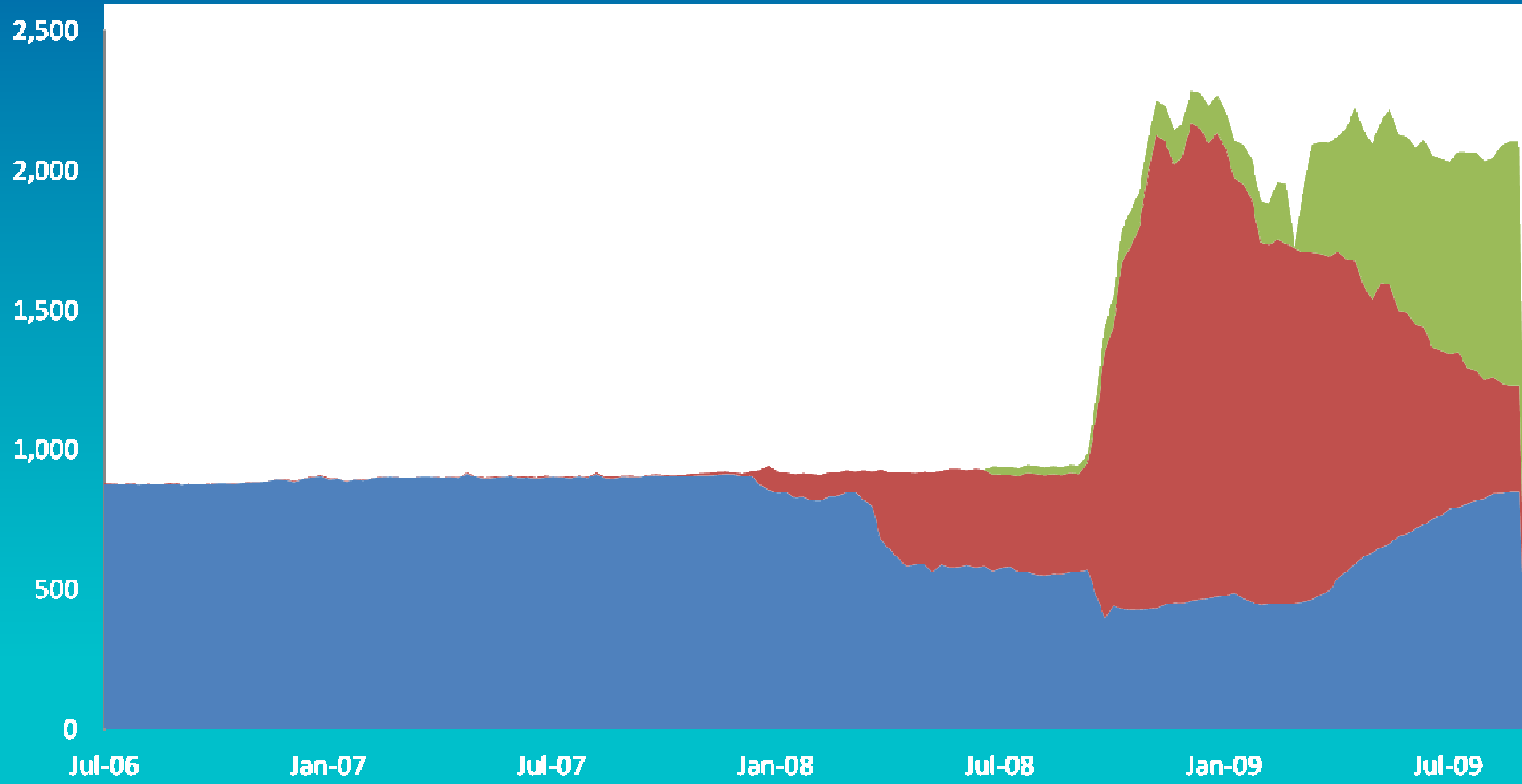
# Fed Balance Sheet vs. the Money Multiplier



Data Sources: Federal Reserve Release H4.1, Federal Reserve Bank of St. Louis.

# Federal Reserve Balance Sheet

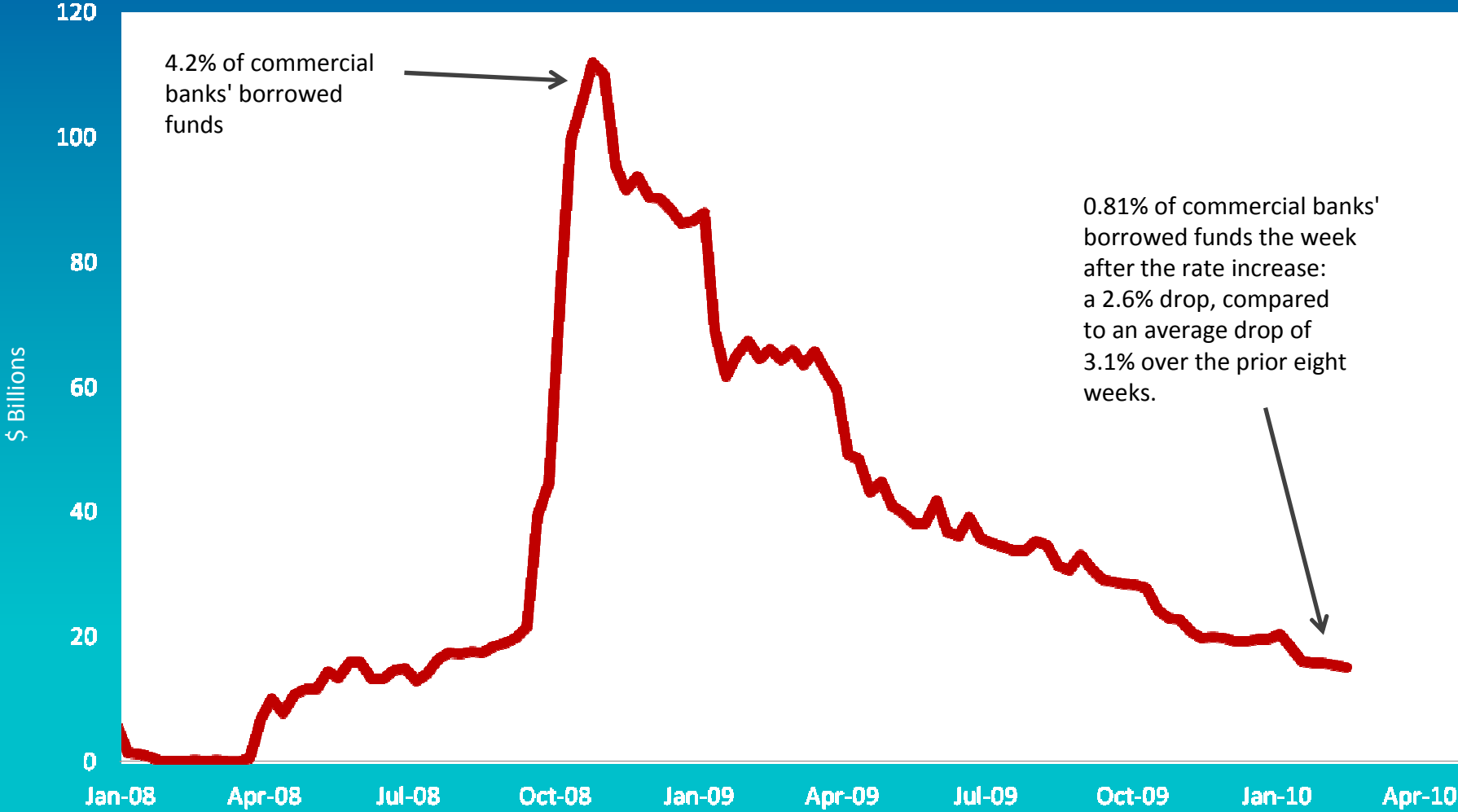
\$ Billions



■ Harder to Unwind Risky Assets ■ Risky Assets ■ Traditional Assets

Data Source: Federal Reserve Board.

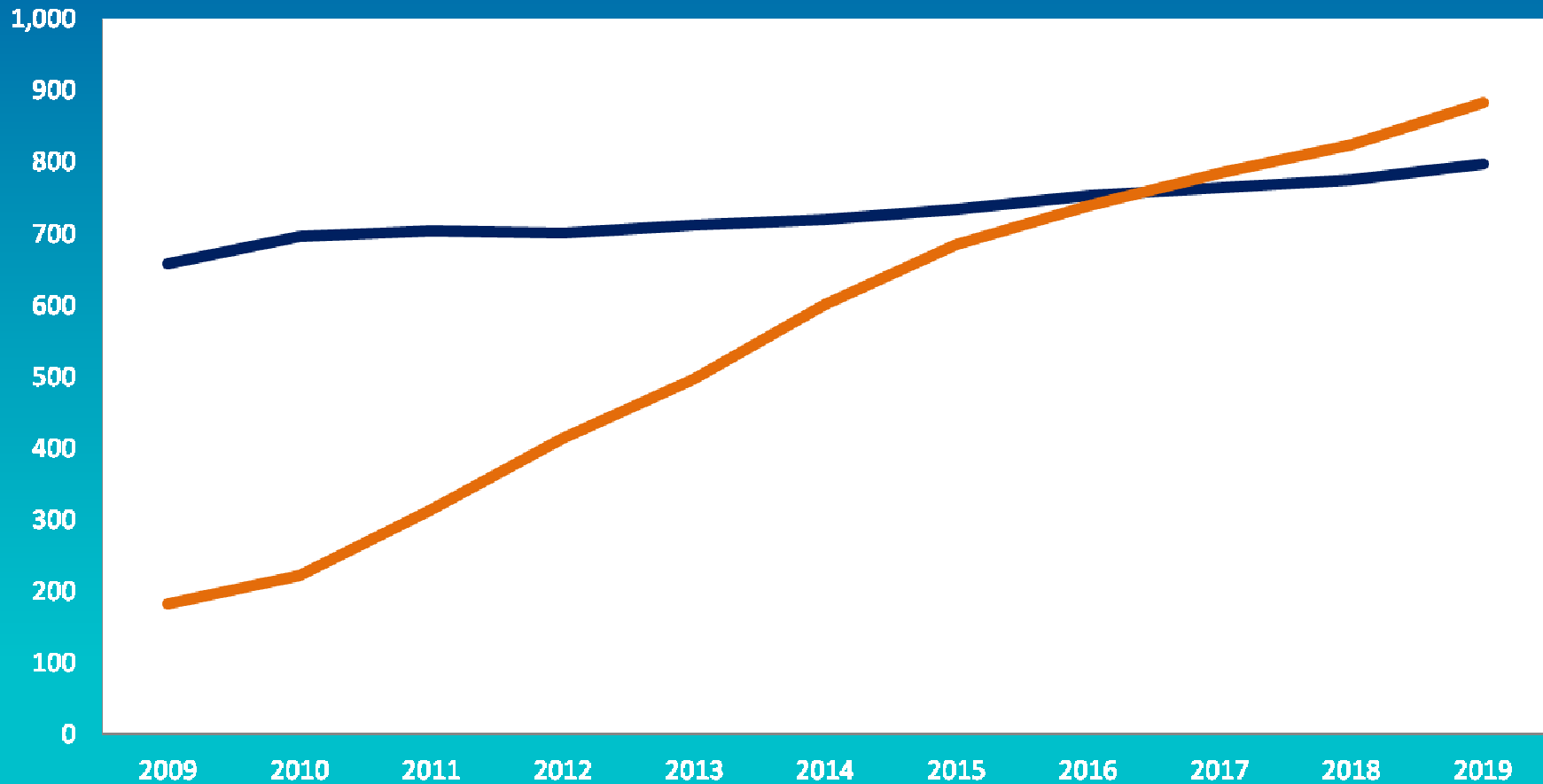
# Discount Window Credit



Data Source: Federal Reserve Release H4.1.

# Debt Service to Surpass Defense Outlays

\$ Billions

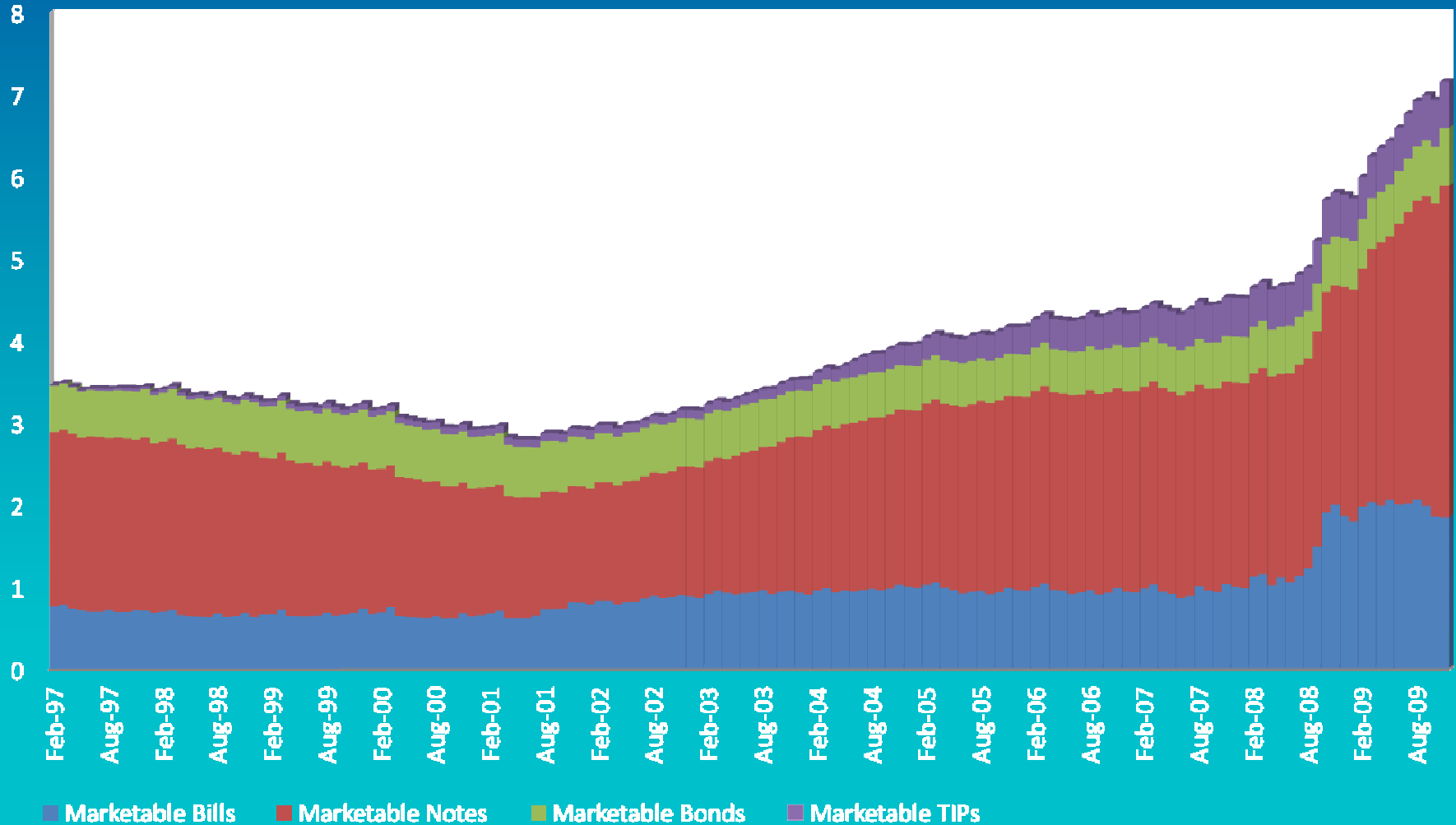


— Discretionary Defense Outlays — Net Interest Outlay\*

\*Using average of the top 10 interest rate projections of the Blue Chip Economic Forecast.  
Data Source: Congressional Budget Office.

# U.S. Debt Distribution by Type

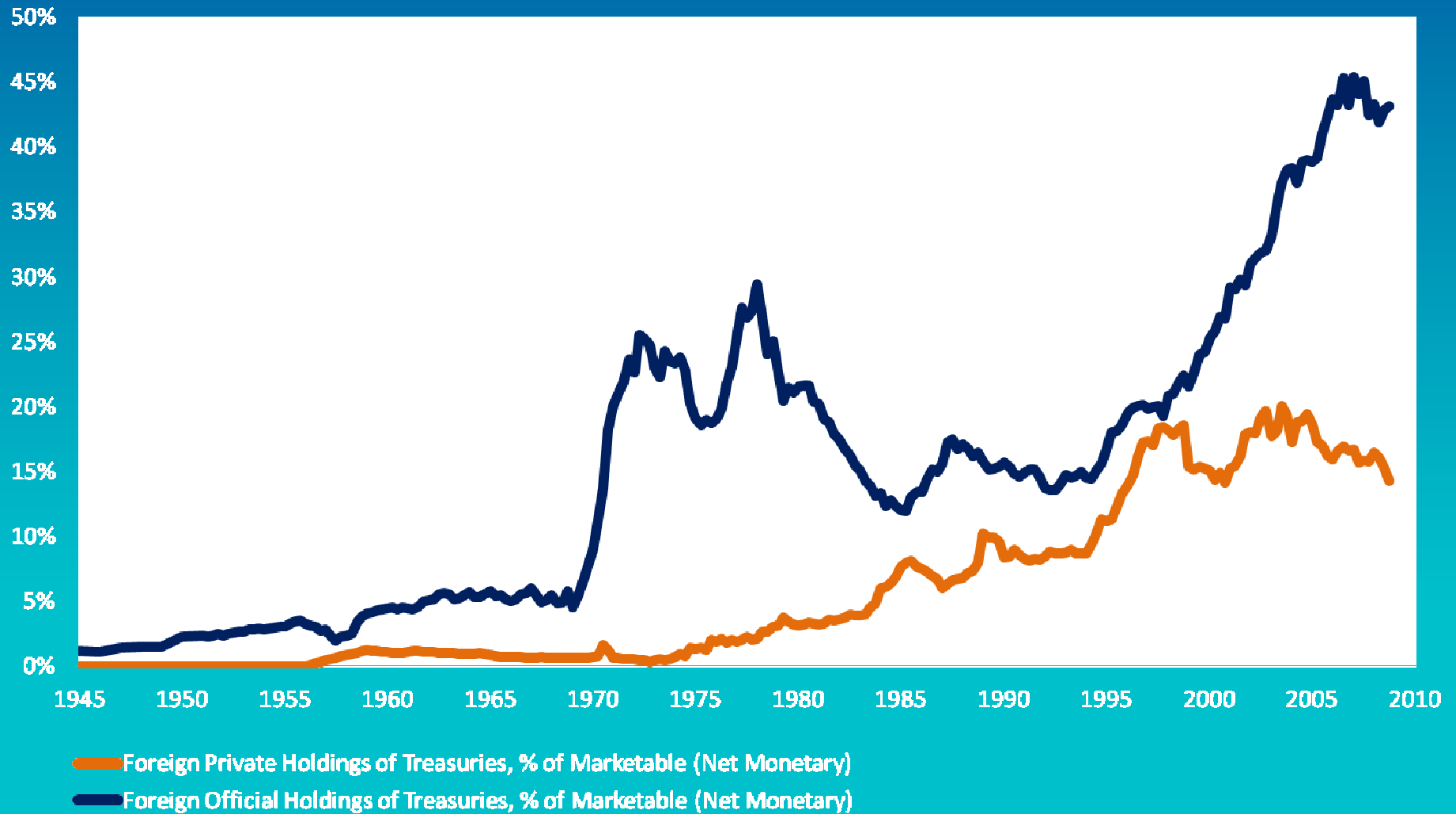
\$ Trillions



Data Source: U.S. Treasury.

# Foreign Ownership of U.S. Treasuries

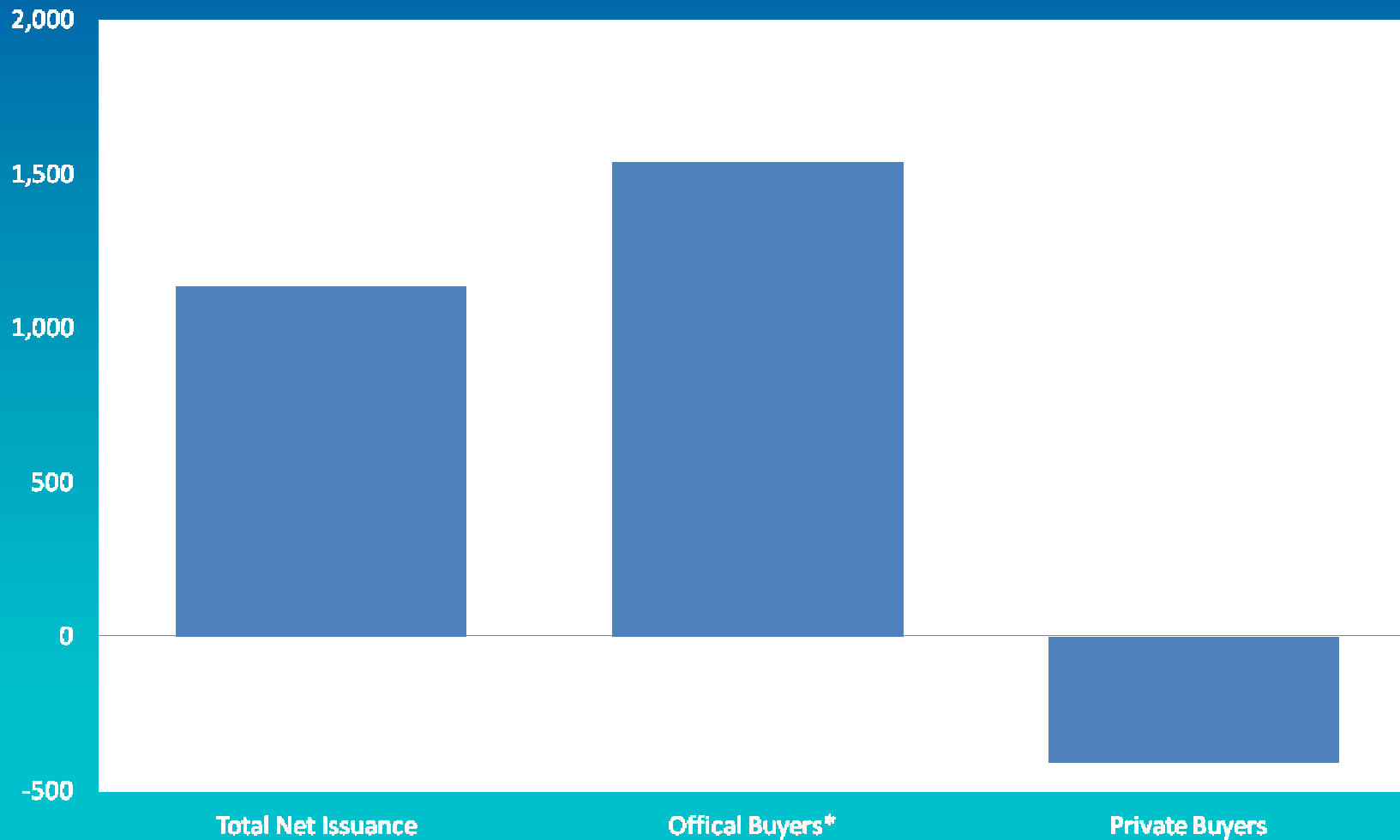
Since 1945



Data Source: Federal Reserve.

# Who is Buying U.S. Government Debt?

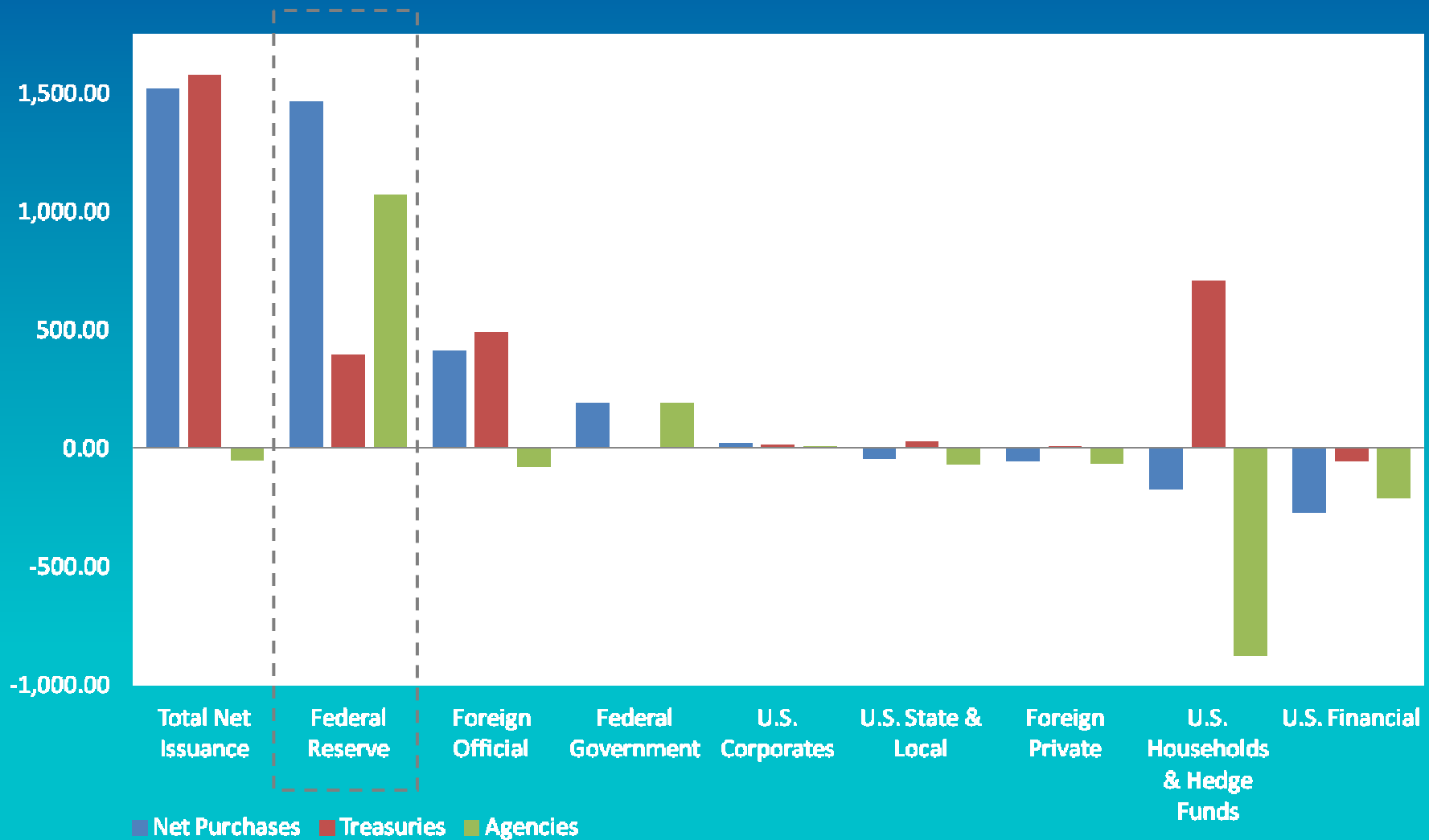
Through 3Q 2009, Annualized Flow, \$ Billions



\*Federal Reserve, Foreign Official, and Federal Government.  
Data Source: U.S. Federal Reserve.

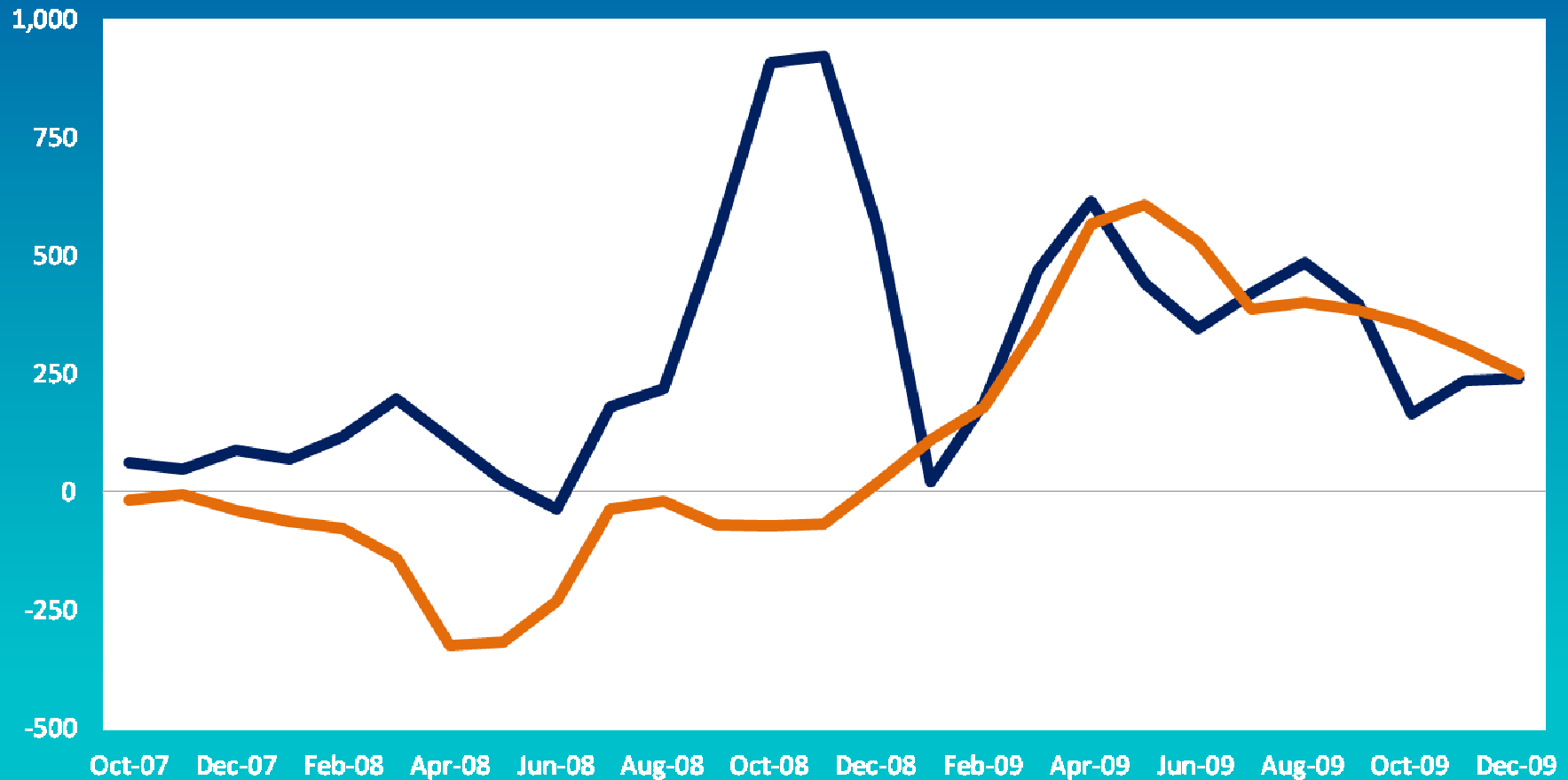
# Who is Buying U.S. Government Debt?

Through 3Q 2009, Annualized Flow, \$ Billions



Data Source: U.S. Federal Reserve.

# What happens when the Fed stops buying government debt?

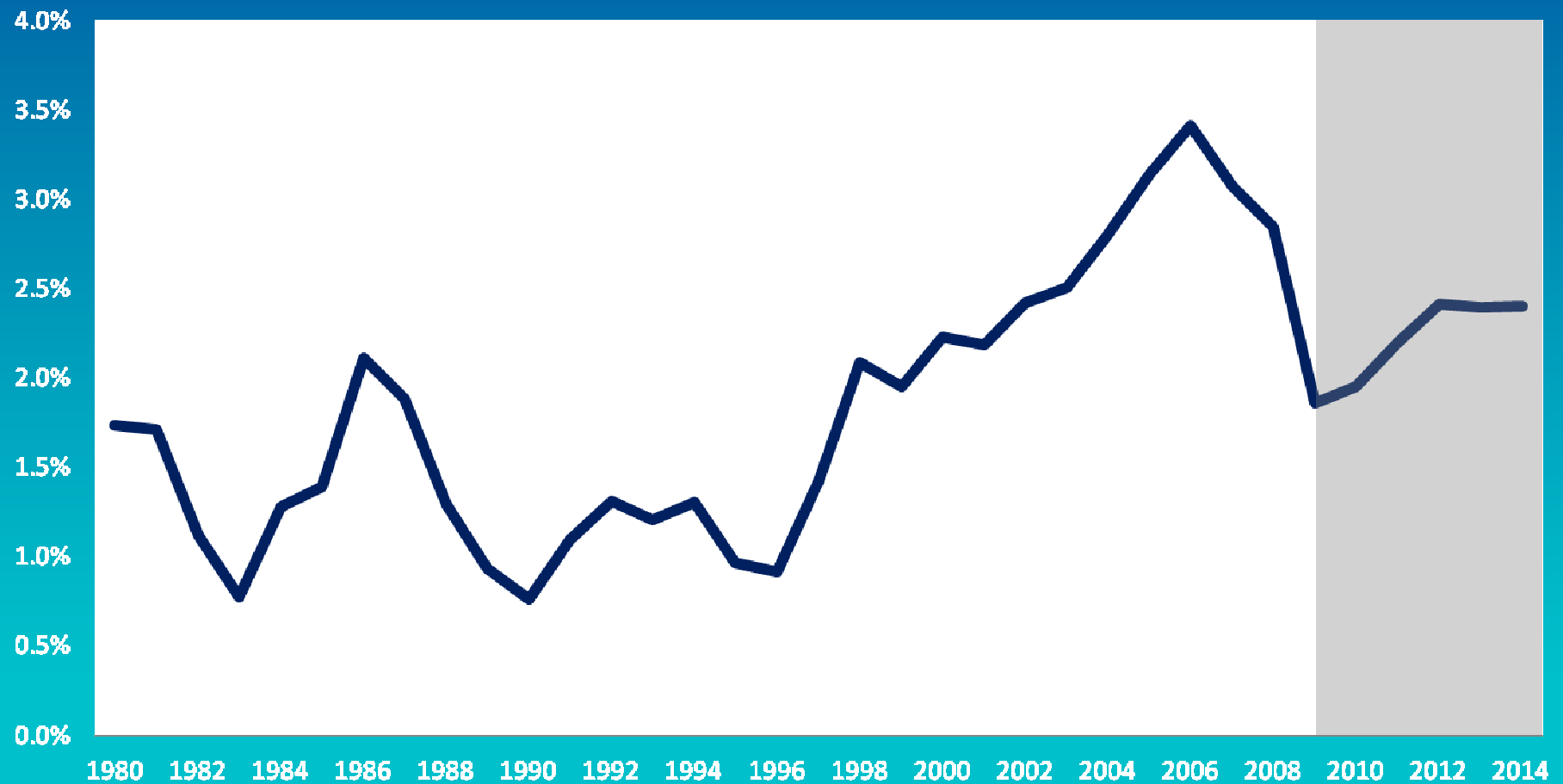


— Marketable Treasuries Outstanding Stock, 3-month change, \$ Billions  
— Federal Reserve Total Government Securities\*, 3-month change, \$ Billions

\*Agency Debt, Agency MBS, and Treasuries.  
Data Sources: U.S. Treasury, Federal Reserve.

# Global Imbalances

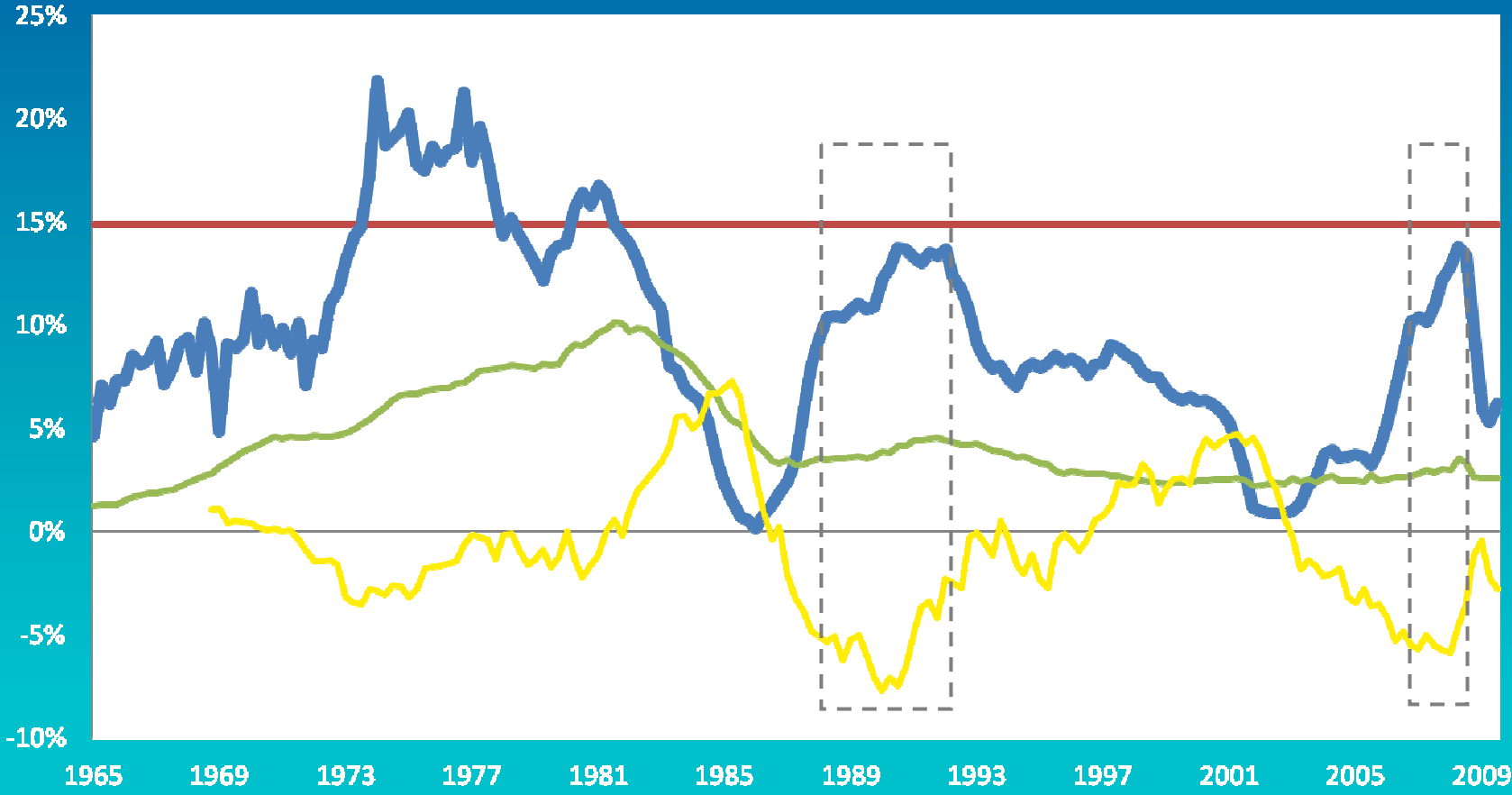
Sum of Absolute Value of IMF Major Regions' Current Accounts as a % of World GDP



Regions are Africa, Asia and Pacific, Europe, Middle East, and Western Hemisphere.  
Data Source: IMF World Economic Outlook, October 2009.

# Export Ambitions

5-year annual growth rates

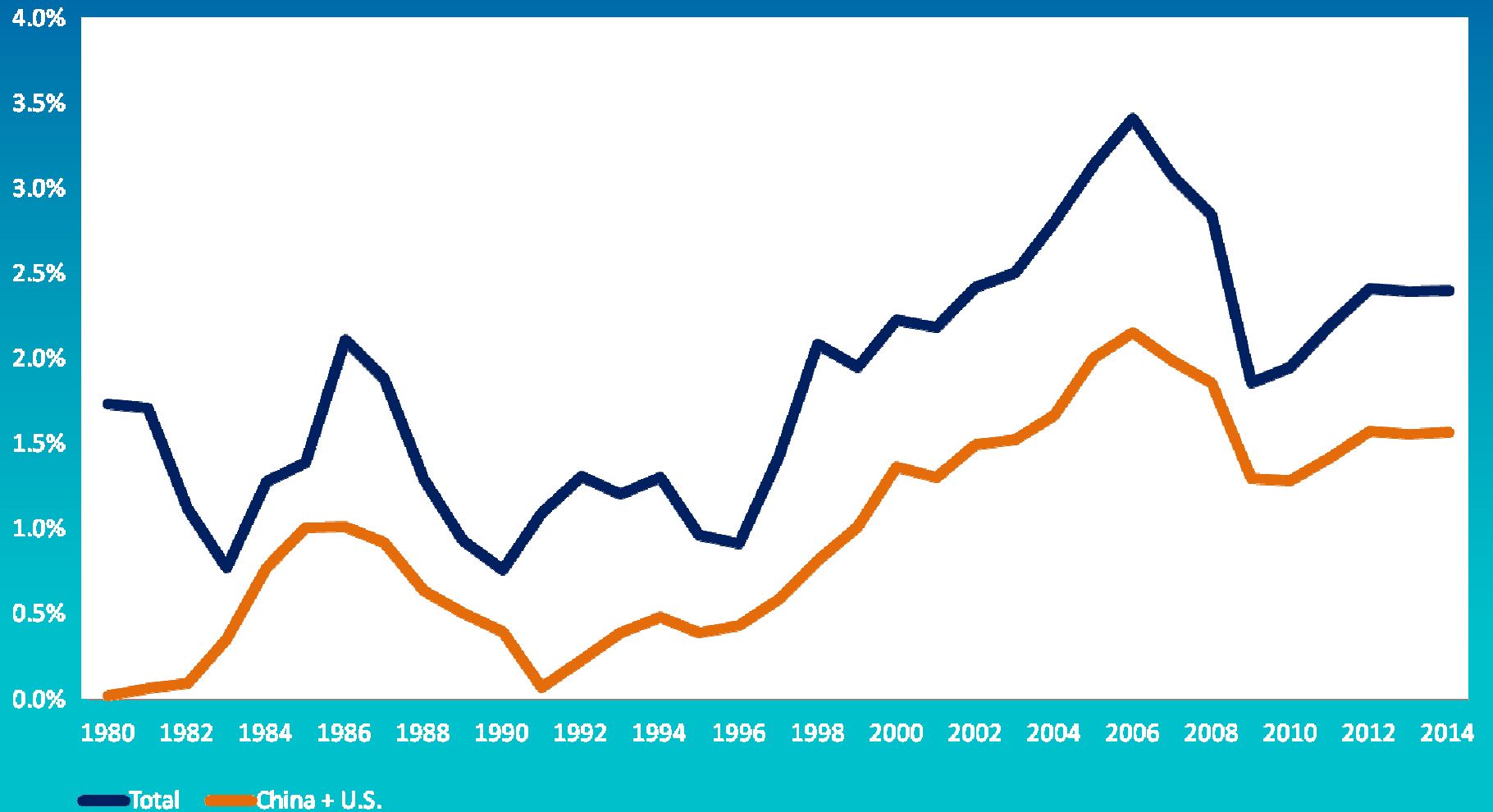


— Required Growth to Double Exports — Export Growth — Inflation — U.S. Real Exchange Rate

Data Sources: Bureau of Economic Analysis, Bank of International Settlements, Bureau of Labor Statistics.

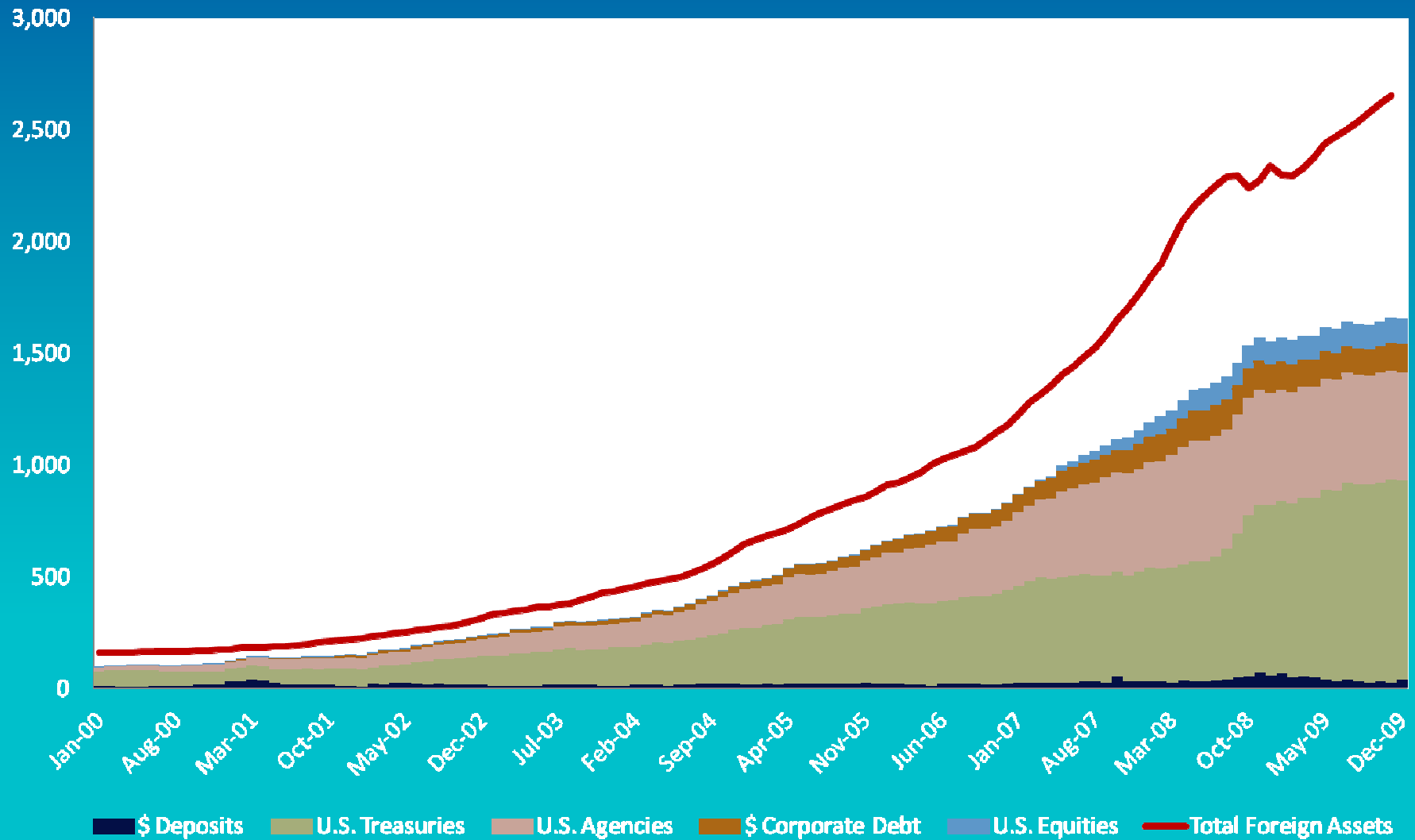
# Global Imbalances

Sum of Absolute Value of IMF Major Regions' Current Accounts as a % of World GDP



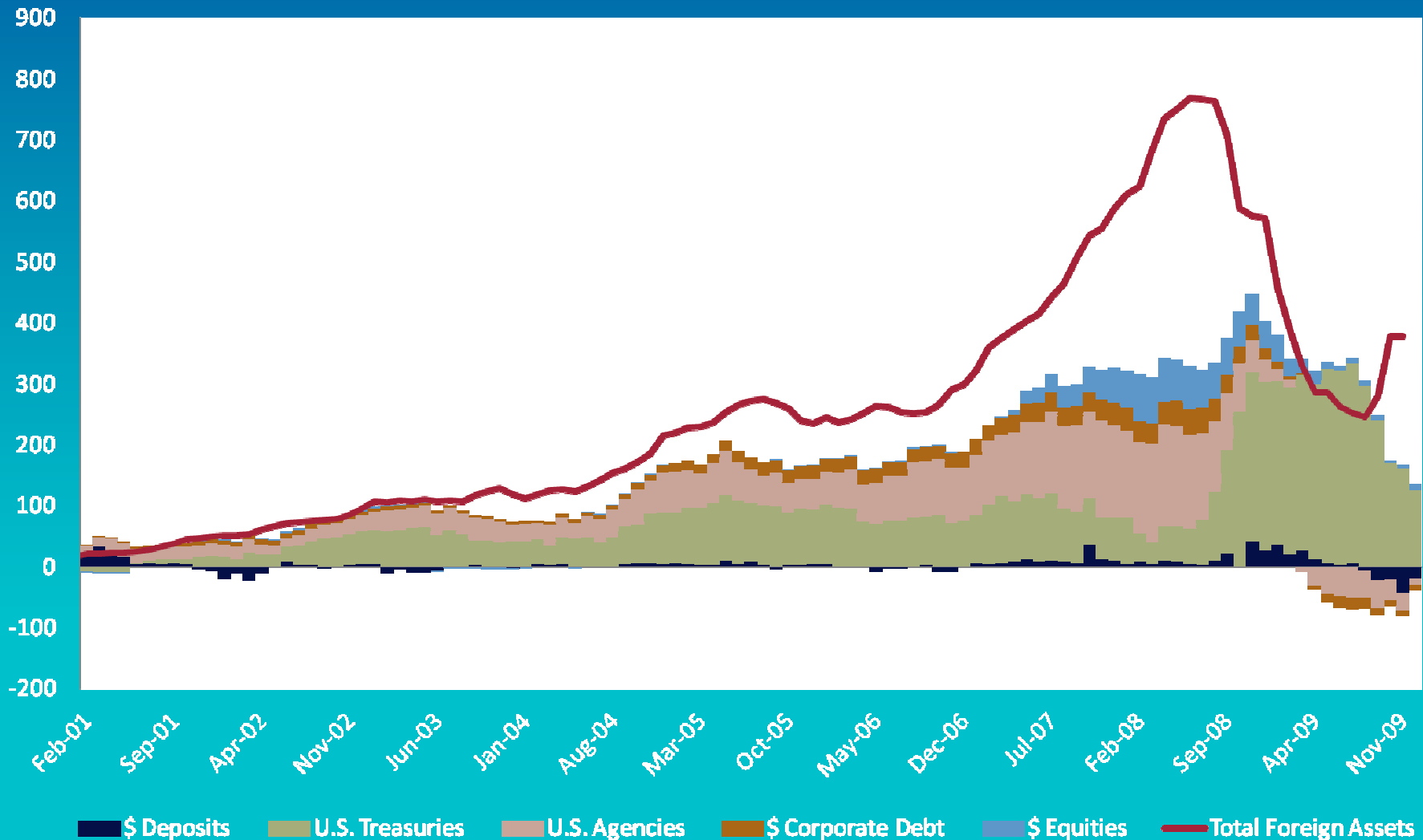
Regions are Africa, Asia and Pacific, Europe, Middle East, and Western Hemisphere.  
Data Source: IMF World Economic Outlook, October 2009.

# China's Total Foreign Assets vs. U.S. Financial Assets (\$ Billions)



Data Sources: People's Bank of China, U.S. Treasury International Capital System.

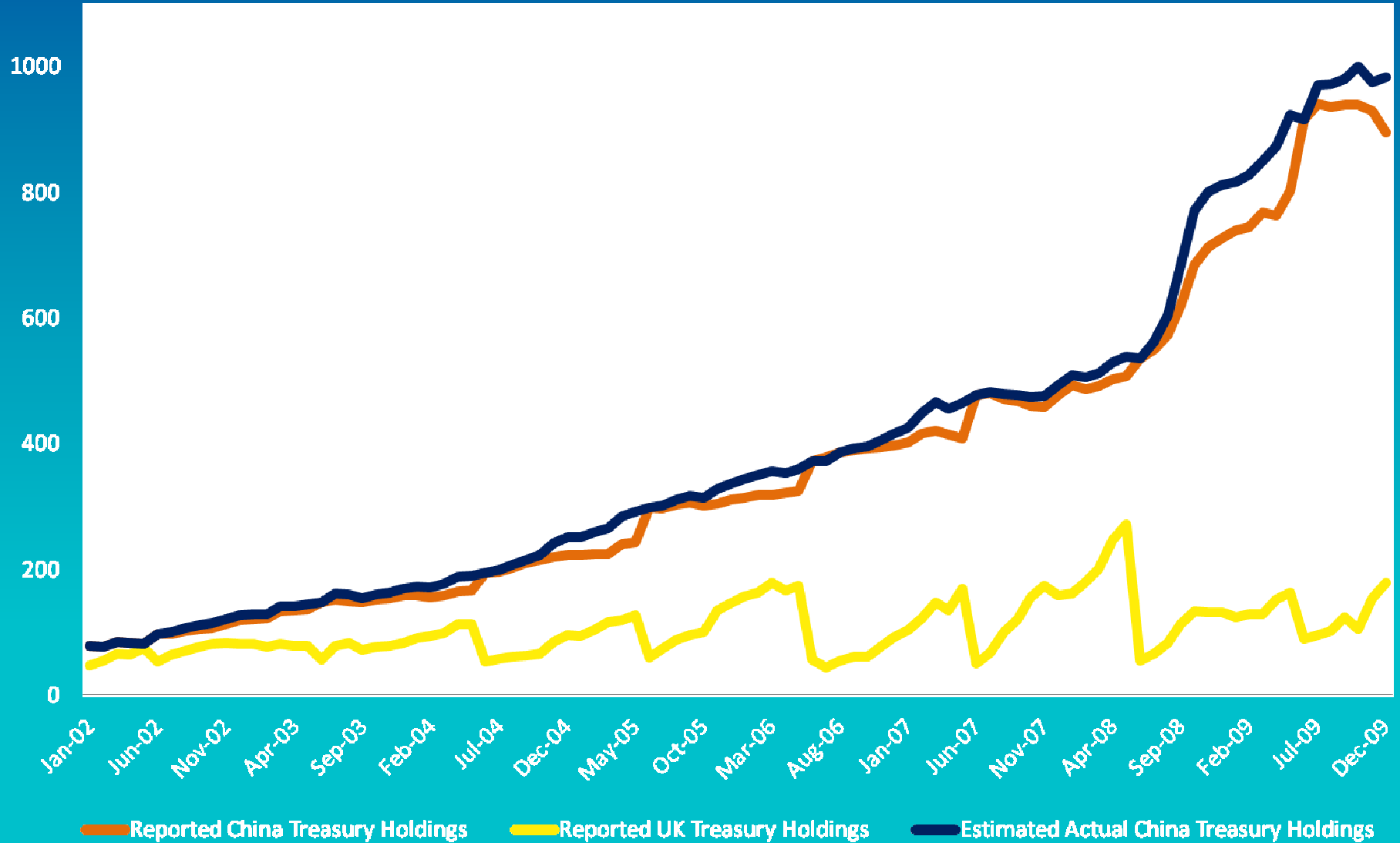
# 12-Month Change in China's Total Foreign Assets vs. U.S. Financial Assets (\$ Billions)



Data Sources: People's Bank of China, U.S. Treasury International Capital System.

# China's Hidden Treasury Purchases

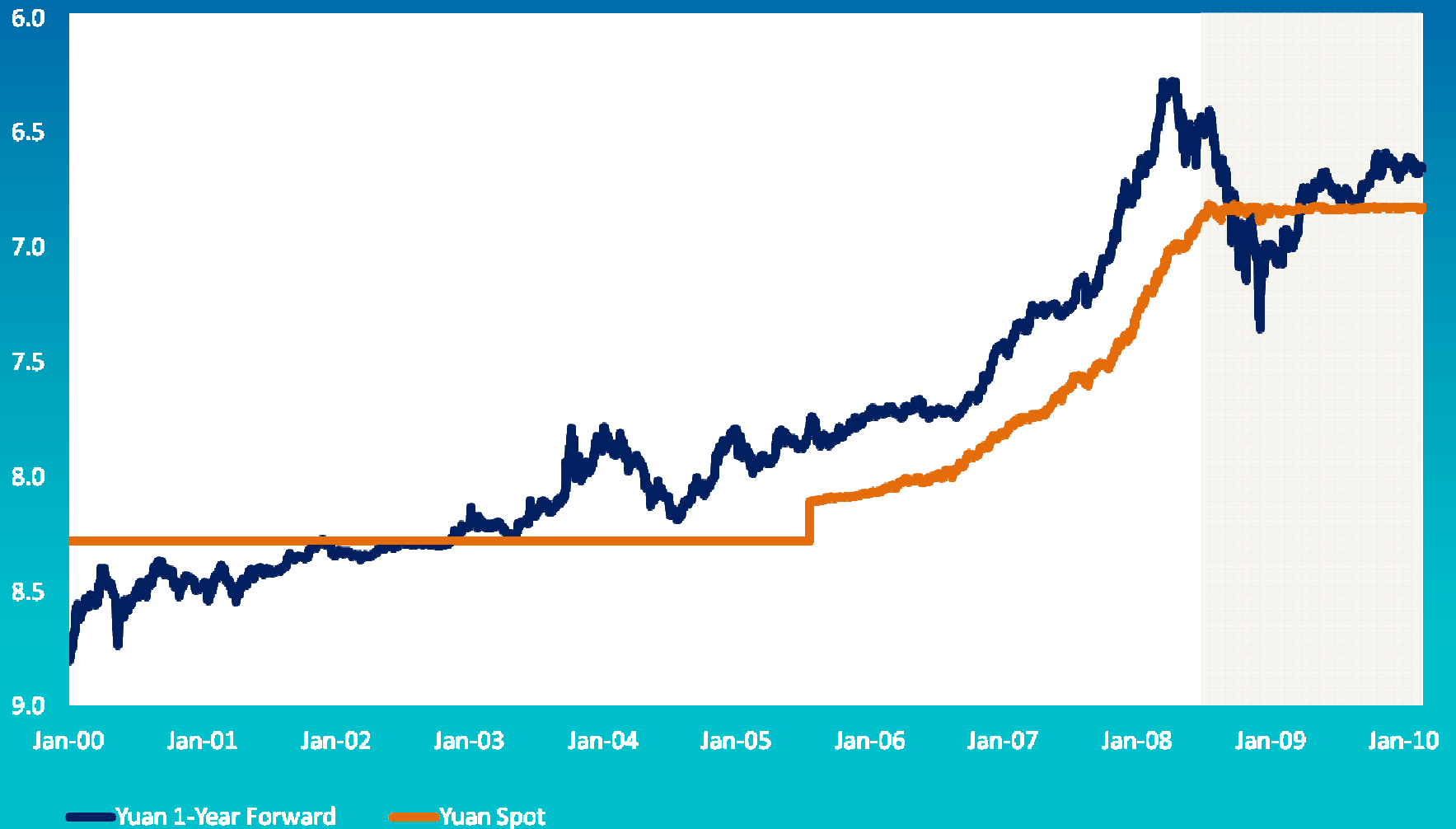
\$ Billions



Data Source: U.S. Treasury International Capital System.

# Re-pegged

## Chinese Currency vs. Dollar



Data Source: Bloomberg.

# Imbalances: China vs. U.S.

- China's position:
  - Debtor must adjust
  - U.S. must tighten monetary and fiscal policy
- U.S. position:
  - Creditor must adjust
  - China must float exchange rate

# Is U.S. Policy Consistent?

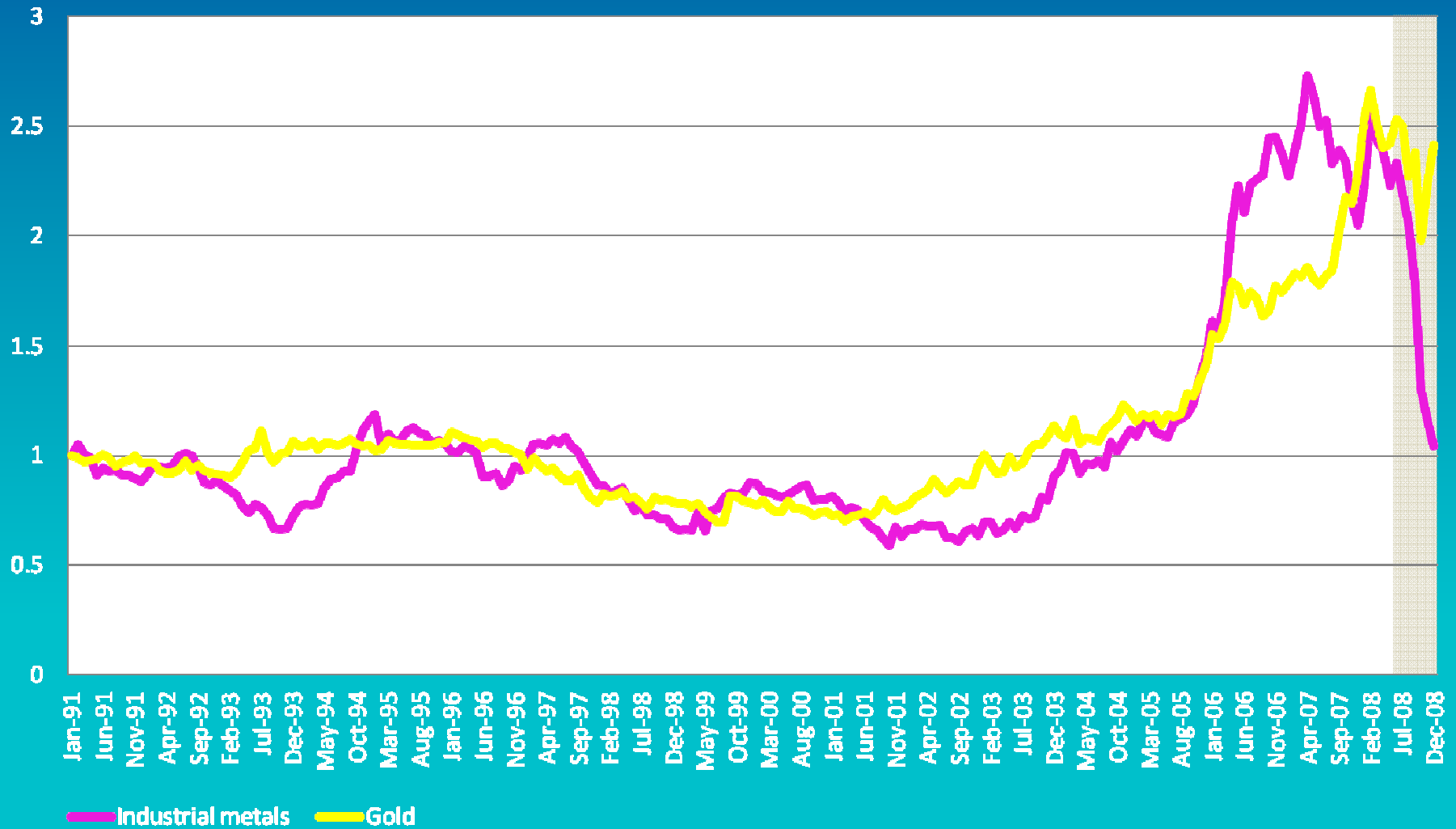
- Bretton Woods, 1944: U.S., as creditor, demands fixed exchange rates and debtor adjustment
- Robert Rubin, 26 May 1998:
  - “China, by maintaining its exchange rate policy, has been an important island of stability in a turbulent region.”

# Alternatives to the \$

- €
- Barter
- **Gold**

# Is Gold a Metal or Money?

Gold and Industrial Metals, January 1991 - December 2008

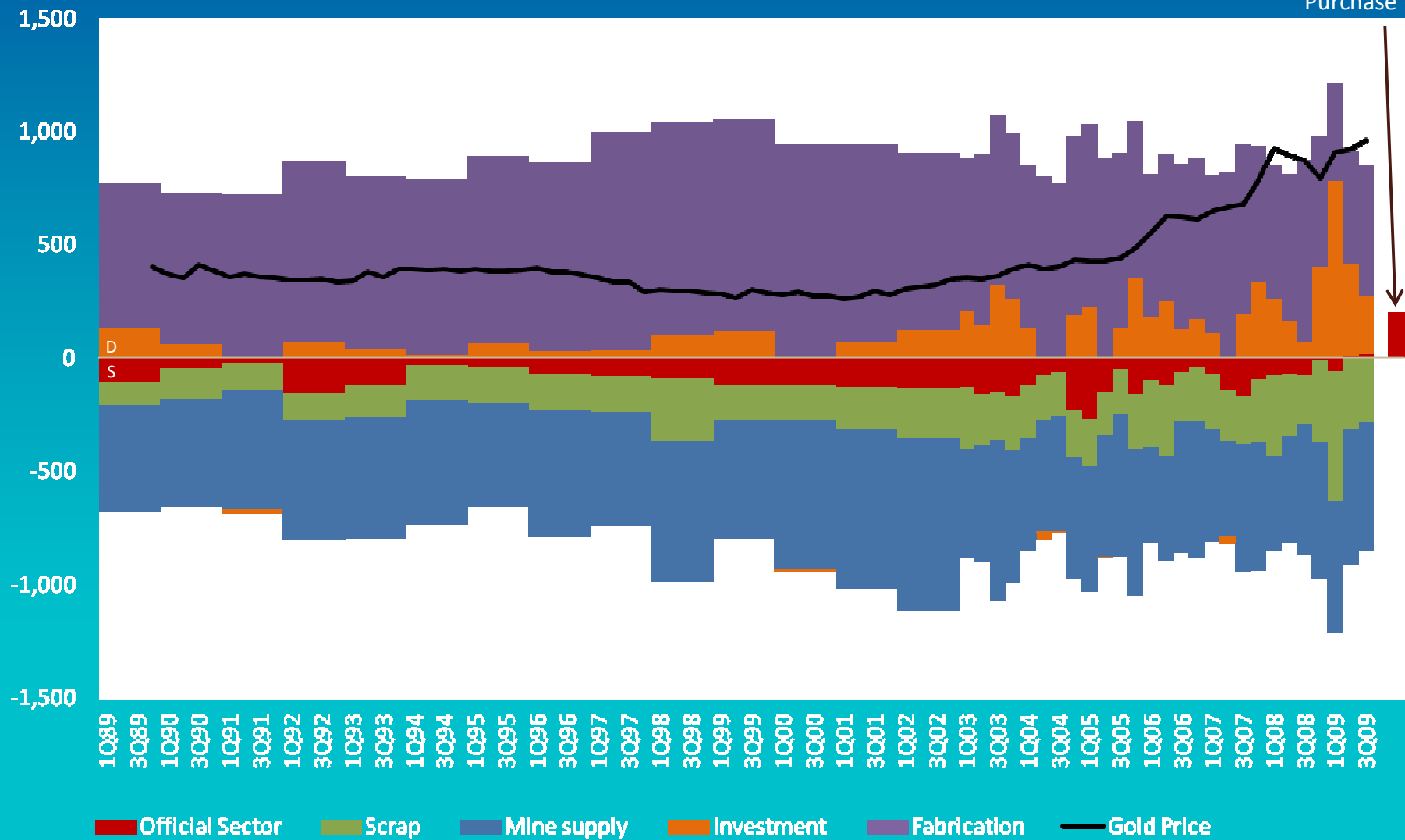


Data Source: Bloomberg.

# Gold Supply and Demand

Quarterly, Tons

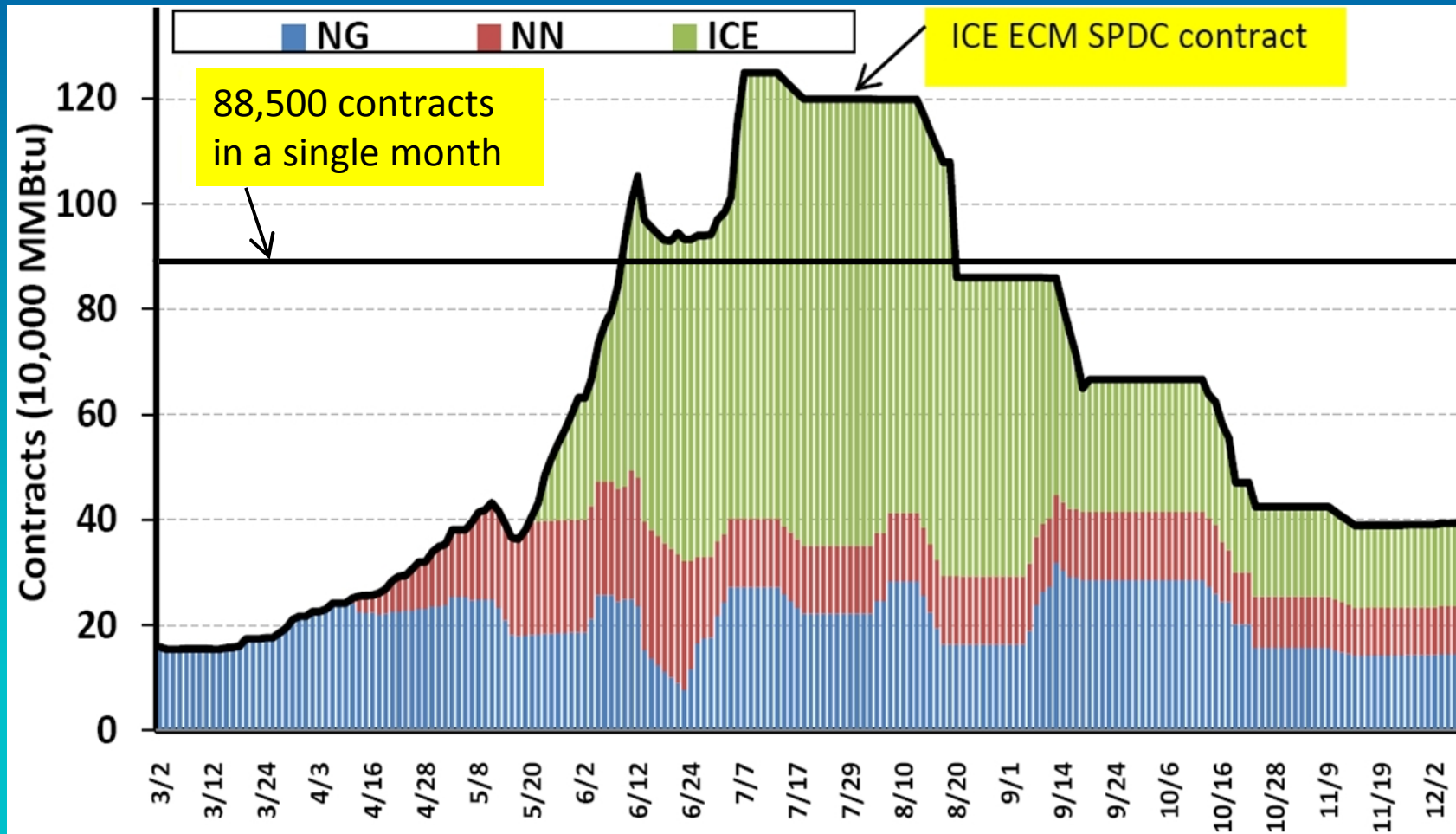
India's 4th-Quarter Purchase



Data Source: GFMS.

# Position Limits

UNG Fund open interest positions



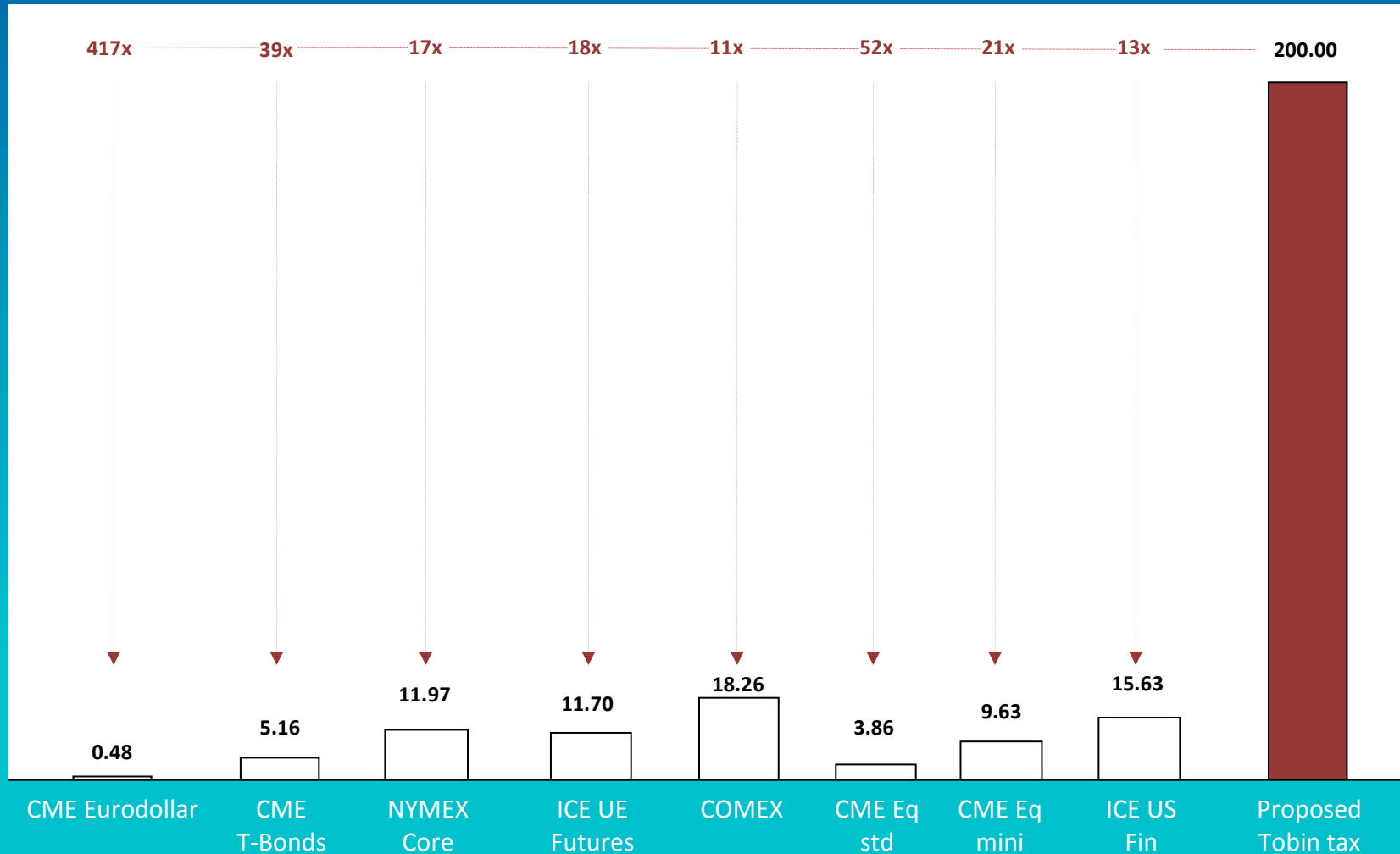
2009

Source: ERDesk, Efficient Frontiers.  
Data Source: CFTC.

# Tobin Tax

## Derivatives exchange fees

Rate per million of value traded



Source: ERDesk, Efficient Frontiers.

Data Source: CME.