Liquidity Management in normal times

- Optimum currency area from the “price-stability” perspective

- Central friction: price and wage rigidities

- Debate:
  1. Microeconomic benefits of a single currency
  2. Loss of independent monetary policy
     Endogeneity?

- Externalities and the quality of policy-making
Liquidity Management in crisis periods

- Optimum currency area from the “lender-of-last-resort” perspective

- Central friction:
  1. Fragility due to the mismatch of maturities
  2. Interconnected balance sheets

- Policy externalities:
  1. Ex-ante or crisis prevention stage (deposit insurance, capital requirements, …)
  2. Ex-post or crisis management stage (injecting liquidity, assessing losses for banks, …)
Crisis, what type of crisis?

- Non-fundamental movements in asset prices (NPV valuation?, liquidation of good projects?, …)

- Central friction: Future rents do not provide enough liquidity

- Effects of asset bubbles are potentially good:
  1. Improve the functioning of financial markets
  2. Facilitate efficient investment and growth

But there might be bad bubbles and there is fragility

- Ex-ante or crisis prevention stage (supporting asset prices? …)

- Ex-post or crisis management stage (public insurance? …)
For large diversified economic and monetary unions, such as the euro area:

1. How helpful is the literature of optimum currency areas for the understanding by national policymakers of the longer term challenges?

2. In your view what are the longer term challenges for monetary policy in such an environment?

3. What structural policies or reforms are in your view most effective to foster the longer term functioning of these areas?