Global Safe Haven

Bonding Foreign and Domestic Owners of the U.S. Public Debt

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Abstract

This paper offers new theoretical and empirical insights to explain the resilience of the U.S. Treasuries market as a safe haven for global investment. Going beyond the standard systemic explanation, the paper highlights the importance

The bottom series in the figure measures the total share of government foreign exchange reserves that are held in USD. Central banks around the world increased the weighted value of the USD against other major currencies. After significant gains in the 1990s, the value of the USD fell over 18 percent from 2001 to 2007. Yet with the beginning of financial turbulence in 2008, the value of the USD held remarkably steady and actually began to . From mid-2008 to mid-2015, the USD increased over 30 percent relative to other major currencies.

Prasad regards the crisis

Thus according to Prasad, dollar strength is due in large part to the continued role played by the U.S. Treasuries market as a safe haven for global investment. Yet the fact that global investors continue to treat U.S. Treasuries as the world's safest asset might itself seem perplexing. After all, the global financial meltdown originated in the U.S. And since then, various developments have compromised the safe haven status of U.S. Treasuries. Most importantly, the U.S. public debt has rapidly increased in the wake of the crisis, and in 2013, breached th

IMF's supranational reserve asset (Helleiner 2014: 68–78). For the first time in three decades, the IMF approved a new issuance of SDRs in 2009, to the tune of approximately $250 billion. Yet even with the most recent issuance, SDRs represent only four percent of global reserve assets and initiatives to further strengthen their role have been met with staunch resistance from the U.S., which holds veto power over IMF decision-making in this area (ibid.:

a low risk appetite and high savings and therefore invests heavily in Treasury securities, either directly or indirectly through their ownership of pension and mutual funds.

Now, according to Prasad (2014: xiv–xv), these domestic owners of the other half of the U.S. public debt constitute a “powerful political constituency”. And he claims that the power and influence of domestic owners of the public debt is amplified precisely because of their age. Older people, he points out, tend to vote in greater numbers. And because many older people also live in swing states such as Florida, they play a key role in determining the outcomes of presidential elections.[9]

Powerful domestic owners of the U.S. public debt would bear a significant cost if the U.S. were to try to inflate away its debt burden. So Prasad’s essential argument is that the interests of foreign and domestic owners of the public debt are united since both have a keen interest in the continued sanctity and creditworthiness of U.S. Treasuries. Foreigners can maintain their confidence in their holdings of U.S. Treasuries thanks in large part to the power and influence of domestic owners, who play a key role in pressuring the federal government to uphold its debt obligations. The analysis therefore points toward a powerful bloc of interests that will continue to support the status quo in global finance, which is underpinned by dollar dominance and the safe haven status of the U.S. Treasuries market.

The Locus of Domestic Power

Prasad’s approach stands out in the massive literature on this subject because he augments the stand wealth and income hierarchy is that it gives us uniform categories through which to explore patterns of inequality across space and time. Although mostly implicit within his work, Piketty suggests that the appropriateness of our chosen statistical categories rests on what

The simple rule of thumb outlined in the previous section links ownership and power, claiming basis, the value of the top percentile's investments in the public debt amounted to well over $1 million.

Rows three and four in Table 1 use measures that allow us to better compare the age and class categories. In the third row we see that the top 3.4 percent of households ranked by net wealth have an ownership stake in the public debt equal to that of households aged 60 and over, which as we saw earlier, represent 33 percent of the population. Finally, the point is further belabored in the fourth row. If we use the top 33 percent of households ranked by net wealth, the same amount of people in the 60 plus grouping, then the ownership of the public debt based on class climbs to 95 percent of the total!

Using our simple rule of thumb to interpret the data in Table 1 it is clear that, in sheer quantitative terms, Obama (Fisher 2008), party affiliation amongst older Americans is actually still quite split. Pew Research Center (2014) polling data shows that party identification is almost evenly divided among those aged 59 and over. 44 percent of those surveyed identified as Republican of lean Republican, while 46 percent identified as Democrat or lean Democrat.

These facts reveal deep divisions among older Americans and bring into question the popular media image of seniors as a juggernaut within U.S. politics (Holladay and Coombs 2004). Unfortunately, instead of investigating the political views of retirees and near-retirees, Prasad ends up merely replicating the empirically suspect view found in the popular media. When we consider the skewed distribution of Treasury securities among older Americans, as well as the heterogeneity of their political preferences, one thing becomes clear: retirees and near-retirees are a highly questionable category for locating the power of domestic owners of the public debt.

What can we say about the cohesiveness of the top one percent as a social group? When it comes to distribution, ownership of the public debt is just as concentrated within the top one percent as it is within our age category. The top 0.1 percent owns roughly a quarter of percentile was also much more likely to contact politicians directly and in SESA interviews often referred to politicians on a first-name basis (ibid.: 54).

Finally, and perhaps unsurprisingly, existing research indicates that cohesion and activism of affluent Americans translates into significant influence over public policy outcomes (Bartels 2008; Gilens 2005, 2012; Gilens and Page 2014

shortage of other safe haven assets), I argued that the existence of powerful domestic owners of the public debt bolsters confidence in U.S. Treasuries. The innovative work of Eswar Prasad categorizes domestic owners of the public debt based on their age, and argues that these owners have significant power in U.S. electoral politics. But the quantitative and qualitative data in this paper indicate that the power of domestic owners of the public debt instead derives from their class position at the top of the wealth and income hierarchy. In particular the research shows that, relative to households aged sixty and older, the top percentile of households have an ownership stake in the public debt that is much more concentrated, have political preferences that are much more cohesive, and exercise political agency that is much more effective.

The results of this research do not alter Prasad's main conclusion. Whether we focus on age or class, we still end up concluding that the interests of domestic owners of the public debt are closely aligned with their foreign counterparts. But the alternative focus on class does draw our attention to other "bonds" between the two categories of owners that are neglected with Prasad's analysis. Focusing on class, it becomes apparent that foreigners not only gain from the existence of powerful domestic owners, but powerful domestic owners gain from the seemingly insatiable foreign appetite for U.S. Treasuries. The powerful "bond" of interests between foreign and domestic owners of the public debt also works to sustain the dominant position of the U.S. within global finance. And, in supplying cheap credit to the U.S. federal government and to U.S. households,

Notes

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