

the leverage cycle and the US dollar then become clearer.³

Maggiore (2010, 2011) provides a risk-sharing perspective on periodic dollar shortages which builds on the net external portfolio of the United States, whereby the United States holds risky assets of other countries but its liabilities are in the form of debt. In contrast to Maggiore’s approach (which maintains the triple coincidence), our paper is partial equilibrium in nature and addresses just the banking system in isolation. We address the fact that within the global banking system, banks based in the United States (many of them with European headquarters) are net creditors to banks elsewhere (Shin (2012)).

Our analysis applies irrespective of whether the local bank is separately owned from the global bank, or whether the local and global banks belong to the same banking organisation. Cetorelli and Goldberg (2012a, 2012b) provide extensive evidence using bank level data that internal capital markets serve to reallocate funding within global banking organisations. Further details are discussed in a BIS (2010) study that describes how the branches and subsidiaries of foreign banks in the United States borrow from money market funds and then channel the funds to their headquarters for on-lending to other parts of the world. Schnabl (2012) presents empirical evidence on the international transmission of liquidity shocks through the banking sector.

2.2 Model

To depart from the “triple coincidence” of national income boundary, decision making unit and the currency area, our model is explicitly built around the balance sheets of international banks that may straddle traditional national income boundaries. The model components follow the structure of the global banking system in Figure 3. We begin first with the regional demand for credit.

³Shin (2014) provides a more detailed description of the breakdown of the “triple coincidence” in international finance. Borio, James and Shin (2014) show that the breakdown of the triple coincidence is a repeated historical theme in international finance.