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## **International Reserves Accumulation: How Much is Too Much?**

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**Abstract:** Following the Asian crisis of 1997/1998, there has been a significant buildup of international reserves holdings in emerging market countries. Most studies have concluded that many emerging market countries accumulated reserves in excess of optimum level. Despite the large accumulation of reserves, many of these countries were reluctant to use their reserves to a substantial degree in the midst of the global financial crisis. The large accumulation of reserves and the reluctances of central banks to use their reserves have raised question whether the international reserves holdings prior the global financial crisis were excessive.

This dissertation addresses the above question by analyzing determinants of central bank reserve holdings. I extend an inter-temporal model of optimum international reserves developed by Jeanne and Ranciere (2006) in several important directions. The model endogenizes both the probability and output costs of sudden stops. It also incorporates the possibility of foreign-currency deposit withdrawals and capital flow retrenchments during a sudden stop - a phenomenon that only recently has been explored in the literature.

The simulation shows that the optimum international reserves estimations are sensitive to model parameters, including the probability and output cost of sudden stops, the foreign currency deposits withdrawals, and the cost of holding reserves. Given the uncertainty of these parameters, the optimum international reserves better to be represented as a range of possible optimum reserve estimations rather than a single point estimation. Based on a range of optimum international reserves estimations of 33 emerging market countries, we found that, on average, the optimum level of international reserves in Eastern Euro and Central Asia countries were higher than that of Asian and Latin American countries. The estimations suggest a considerable variation across countries in deviations of reserves accumulation from optimal levels prior to the global financial crisis. While many Asian countries seem to have over-accumulated reserves, it is less obvious that most Latin American countries accumulated excess reserves. In contrast, almost all of Eastern Europe countries were found to hold too little international reserves throughout this period. The trend continued in the period after the global financial crisis.

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