A Market-Based Solution for Fire Sales and Other Pecuniary Externalities*

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Abstract

Pecuniary externalities are removed with market exchanges that internalize agent types’ influence on future prices. Agents choose in the initial period from among various possible prices they want to prevail in the future and buy or sell rights in these market exchanges for future trade. One can think of contemporary exchanges or trading houses, earmarked by these specified future prices. Each agent can choose the exchange it wants without regard to what any other agent is doing. But crucially, the right to trade in each and every exchange is priced. The fee structure has a per unit price and quantity decomposition: a price, as determined by the exchange chosen, times the quantity of type-specific future excess demand, as determined by its chosen future pre-trade position, namely, savings and security holdings, and the chosen future price.

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