

Our Views

Dominance of US Dollar: change is imperative

Having been a regular attendee at the ET Awards program almost since its inception, I must say that ET has been raising its own bar of excellence in every manner. The selection of the winners, the management of the awards ceremony, the hand-picked audience, are a given now. What captivates the audience is also how frank, open, and transparent conversations take place at this forum between the captains of the corporate India, the policy makers, and the leaders of the country.

This year, during the panel deliberations at the Awards on Friday night, several interesting and varied topics came up. This included a discussion about the over-dependence on the US Dollar (USD) as a reserve currency and its ramifications.

To share a quick perspective on the history of world trade, the phases of the Gold Standard, and how the USD reached the dominating position it is at today, in the decades before the first world war, international trade was conducted and settled using physical gold. Post World War I, international indebtedness increased, and the gold standard only exacerbated economic difficulties. Currencies like British pound sterling and USD started taking centre stage in international trade. Post World War II in 1944, US with highest gold reserves amongst nations had already set its dominance on the world economy making USD as dominant currency around the world. One could go to a bank in the US and exchange USD for gold.

In the evening of Sunday, August 15th, 1971, US President Nixon announced to the world the de-linkage of USD to gold. It meant that one could no longer exchange printed USD with gold. It gave the US an unprecedented ability to print paper currency to fund its requirements. Immediately following this event, the US stock market went up almost 25% in a short period.

In my view, USD dominance is a real issue because it gives unlimited and far-reaching powers to the US. For example, a US sanction on a country not only cripples its international trade, but it can also hurt the overall economy including the life of a common man. However, in the short term, there doesn't seem to be an alternative to USD anywhere in the world. It has been close to a century since the USD and the US dominated the world economy and a conversation around change is an imperative. It is indeed time the world started discussing this issue.

The natural question therefore is "what is the alternative". With Euro coming in 1999, it was expected to offer an alternative. However, given the current situation and the debt position of the European economies, it may be daydream until Euro zone also became a fiscal zone. British pounds, after having dominated trade for a couple of centuries has now completely lost its sheen. Given the current UK economic situation, no country would like to keep its reserves in pounds.

Post 2016, with RMB's inclusion into SDR (Special Drawing Rights) by IMF along with USD, Pounds, Euro, and Yen, the second largest economy in the world, China, may also throw its hat in the ring. However, given the general lack of trust, transparency, democracy in China and its own economic woes, there has been a significant withdrawal from RMB in the recent years. Finally, even crypto has its own challenges.

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Given the lack of an alternative, USD continues to be a strong reserve currency. The latest example of Zimbabwe accepting USD as its prime local currency indicates that weaker economies would still depend on the USD.

With no alternative currently in sight, in my view, bilateral/ multilateral alliances would emerge and grow over time. For India to play its part, we should focus on two things. Drawing lessons from US President Nixon's famous speech on Aug 15th, 1971, wherein he said, "Strength of the nation's currency is based on the strength of the country's economy" we should continue to strengthen our economy. Once we are an economically strong nation, our currency will automatically become strong and appear in the list of alternatives. Secondly, meanwhile we should continue to focus on regional and bilateral alliances to reduce our dependence on USD.

On a lighter note, if I were to draw an analogy from the current Indian political scenario, even if one would want to look for an alternative to our National Government (am not suggesting that), there doesn't exist one. Therefore, one looks for some regional alliances which may lead to an alternative.

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