



The Wave of De-Dollarisation

This editorial is based on [“Why ‘De-Dollarisation’ is Imminent”](#) which was published in Indian Express on 17/03/2022. It talks about the efforts being made by the countries to reduce the prominence of USD in global commerce.

For Prelims: SWIFT (Society for Worldwide Interbank Financial Telecommunication), Forex Reserves, International Monetary Fund (IMF), Special Drawing Rights.

For Mains: De-dollarisation - causes, Global/Russia and China’s efforts for de-dollarisation, Way Ahead for India in de-dollarisation.

The weaponization of trade, the imposition of sanctions and the exclusion from [SWIFT \(Society for Worldwide Interbank Financial Telecommunication\)](#) by the US could trigger a **faster de-dollarisation** as countries displaying diplomatic and economic autonomy will be wary of using US-dominated global banking systems.

The **US dollar, which is the world’s reserve currency, can see a steady fall** in the current context as leading central banks may look to diversify their reserves away from it to other assets or **currencies like the Euro, Renminbi or gold**.

The notion of de-dollarisation sits well in the thought **experiment of a multipolar world** where each country will look to enjoy **economic autonomy in the sphere of monetary policy**.

What is and Why De-Dollarisation?

- De-dollarisation refers to reducing the dollar’s dominance of global markets. It is a process of substituting US dollar as the currency used for:
 - Trading oil and/ or other commodities
 - Buying US dollars for the [forex reserves](#)
 - Bilateral trade agreements
 - Dollar-denominated assets
- The dominant role of the dollar in the global economy **provides the US a disproportionate amount of influence** over other economies. The US has for long used imposition of sanctions as a tool to achieve foreign policy goals.
 - The de-dollarisation is driven by the desire to **insulate the Central Banks of the Countries from geopolitical risks**, where the status of the US dollar as a reserve currency can be used as an **offensive weapon**.

What are the Causes of Dollar’s Prominence?

- The US dollar sealed its position in the **early 1970s** with a **deal with the oil-rich Kingdom of Saudi Arabia** to conduct global energy trade in dollars.
 - The status of the dollar was **enhanced by the collapse of the Bretton Woods system**; it essentially eliminated other developed market currencies from competing with the USD.
- Currently, about 60% of foreign exchange reserves of central banks and about **70% of global trade is conducted using USD**.
 - The psychological angle to considering the USD as a “safe-haven” asset is that people continue to view the currency as a relatively risk-free asset.
 - Additionally, sudden dumping of dollar assets by adversarial central banks will also pose balance sheet risks to them as it will erode the value of their overall dollar-denominated holdings.
- Apart from the Euro and gold, most other foreign currencies have some inherent risks associated with them.
 - For instance, with the historically “neutral” Switzerland joining the EU in imposing sanctions on Russia, it eliminates the Swiss Franc from being an asset that can work as a hedge against economic sanctions.

What are the Efforts for De-Dollarisation?

- Leading geopolitical adversaries of the US — Russia and China — have already started this process of de-dollarisation.
 - Efforts are underway for the possible introduction of a new Russia-China payment system, bypassing SWIFT and combining the Russian SPFS (System for Transfer of Financial Messages) with the Chinese CIPS (Cross-Border Interbank Payment System).
 - The [ongoing war in Ukraine](#) and the subsequent economic sanctions will trigger central banks to go back to their drawing boards to reassess their dependency on the dollar.
- Russia had started its three-pronged efforts towards de-dollarisation in 2014 **when sanctions were imposed on it for the [annexation of Crimea](#)**.
 - Russia **reduced its share of dollar-denominated assets to about 16%** in 2021.
 - It also **reduced its share of trade conducted in USD** by prioritising national currencies in bilateral trade.
 - The use of USD in Russia’s exports to [BRICS](#) crashed from about 95% in 2013 to less than 10% in 2020.
- China aims to use trading platforms and its digital currency to promote de-dollarisation. It has established RMB trading centres in Hong Kong, Singapore and Europe.
 - In 2021, the People’s Bank of China submitted a “Global Sovereign Digital Currency Governance” proposal at the Bank for International Settlements to influence global financial rules via its digital currency, the e-Yuan.
 - The [International Monetary Fund \(IMF\)](#) has already added Yuan to its [SDR \(Special Drawing Rights\)](#) basket in 2016.
 - However, the **lack of full RMB convertibility will hinder China’s de-dollarisation ambition**.

What is India's Scenario in this Regard?

- India has also had to work out alternative arrangements, including a **barter arrangement, with certain sanctioned countries** in the past.
 - More recently, India and Russia are said to be considering the use of the Chinese yuan as the reference currency to facilitate oil trade between the two countries.
- **Issue:** Like Chinese renminbi, **Indian rupee is not yet fully convertible** at the exchange markets.
 - Non-convertible currency creates difficulties for participating in the international market as the transactions take longer routes for processing.
 - Non-convertibility implies an uneasy access to capital, less liquidity in the financial market, and less business opportunities.
- **Solution:** Similar to China and Russia, India can also look towards having a digital currency in the near future, and some signs for this are already visible.
 - India can also look towards having an increased share of euros and gold in its foreign exchange reserves.

- India has several options for initiating its de-dollarization process. Starting from Russia-India transactions, trade with Iran, **EAEU**, BRICS and **SCO** members in national or digital currencies can also become a reality in near future.
- A drop in the dollar's stature is inevitable as major economic powers like China and India rise.
 - The rise of Asia as an economic powerhouse will raise the importance of currencies like the Yuan and the Indian rupee.
 - The frequent use of the US dollar as a potential weapon for achieving foreign policy objectives will no doubt accelerate the process of de-dollarisation.
 - Further, currency convertibility is an important part of global commerce as it opens trade with other countries and allows a government to pay for goods and services in a currency that may not be the buyer's own.

Conclusion

- The US dollar is still the favoured currency for trade because no other currency is liquid enough. Even if a currency does, there would be apprehensions in nations about that currency becoming a mirror of the US dollar.
- A mere change in regime along with having to bear the same manipulations albeit from a different country is not what the world wants. The only way forward would be to **diversify the currency market with no one currency claiming hegemony.**

Drishti Mains Question:

"The frequent use of the US dollar by the USA as a potential weapon for achieving its foreign policy objectives w

Previous Year Question:

Q. Recently, which one of the following currencies has been proposed to be added to the basket of IMF's SDR? (2016)

- (a) Rouble
- (b) Rand
- (c) Indian Rupee
- (d) Renminbi

Ans: (d)

Q. Consider the following statements: (2019)

1. Most of India's external debt is owed by governmental entities.
2. All of India's external debt is denominated in US dollars.

Which of the statements given above is/are correct?

- (a) 1 only
- (b) 2 only
- (c) Both 1 and 2
- (d) Neither 1 nor 2

Ans: (d)

Q. The problem of international liquidity is related to the non-availability of? (2015)

- (a) Goods and services
- (B) Gold and silver
- (C) Dollars and other hard currencies
- (D) Exportable surplus

Ans: (c)

Q. Consider the following statements: (2019)

1. Purchasing Power Parity (PPP) exchange rates are calculated by comparing the prices of the same basket of goods and services in different countries.
2. In terms of PPP dollars, India is the sixth largest economy in the world.

Which of the statements given above is/are correct?

- (a) 1 only
- (b) 2 only
- (c) Both 1 and 2
- (d) Neither 1 nor 2

Ans: (a)

Q. Which of the following is/are treated as artificial currency? (2010)

- (a) ADR
- (b) GDR
- (c) SDR
- (d) Both ADR and SDR

Ans: (c)