



Dollarisation Due to Cryptocurrencies

For Prelims: RBI, Dollarisation and De-dollarisation, cryptocurrencies, forex reserves

For Mains: Dollarisation Due to Cryptocurrencies, Effect of Policies & Politics of Countries on India's Interests

Why in News?

Recently, [Reserve Bank of India \(RBI\)](#) told a parliamentary panel that [cryptocurrencies](#) can lead to "dollarisation" of a part of the economy which would be against India's sovereign interest.

What is Dollarisation?

- Dollarisation is a **form of currency substitution**, where dollars are used in addition to or instead of the local currency of a country.
 - Though only tax havens like Liberia and Panama can be defined as 'dollarized' in a true sense, there are many economies dollarised to a large extent.
- In fact, **two-thirds of dollars are held outside the United States** which issues it.
 - Countries which have been victims of hyperinflation like Bolivia have become dollarised too, with over 80% of the currency in use being dollars.

What is De-dollarisation?

- It 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.

How Dollarisation Affects an Economy?

- In spite of its current inflation troubles, **India is far away from dollarisation to this extent**.
 - However, according to some research papers, **Indian EXIM transactions are dominated by dollars**.
- **86% of both Indian imports and exports** are invoiced in dollars.
- **Only 5% of India's imports and 15% of exports** are from and to the US.
 - It shows that **few countries use their own currencies for international transactions**

due to the popularity of the dollar abroad.

What are the Related Concerns?

- **Challenges to the Stability of the Financial System:**
 - Central banks of economies with **high dollarisation, become bodies with no power.**
 - Cryptocurrencies have the **potential to be a medium of exchange and replace the rupee in financial transactions** both domestic and cross border.
 - This is **one of the reasons why RBI has opposed it**, and the Indian finance ministry has backed them by **imposing a 30% crypto tax** on it without officially 'allowing' it in India.
 - This move **aimed to stall Indian rupees going up into purchasing virtual assets** which will then be owned by foreign entities - that cannot be tracked by tax authorities here.
 - The **tax does not apply to individuals** who mine cryptos to earn them but only to those who spend Indian rupees to acquire or trade in it.
- **Threat to Financial Sector of the Country:**
 - Besides being used for **terror financing, money laundering** and **drug trafficking**, cryptos **pose a bigger threat to the stability of the financial system of the country.**
- **Negative Impact on the Banking System:**
 - It will also **have a negative impact on the banking system** as these being attractive assets **people may invest their hard-earned savings** in these currencies which may result in banks having lesser resources to lend.
 - There are an **estimated 15 million to 20 million crypto investors in India**, with total crypto holdings of around USD 5.34 billion.

Way Forward

- 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.

[Source: ET](#)

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