

# Dominant dollar

Its global reserve currency status is set to continue

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Nobel laureate Robert Mundell once said: "Great powers have Great currencies" – It can very well be restated in the contemporary world as: "Great Currencies make Great Powers".

US dollar's dominance continues to prevail by being the most reliable currency anchor over the last eight decades.

International monetary system requires production and distribution of safe assets.

The US has been at the core of that system and enjoying benefits, but the rest of the world has also benefitted by deploying its savings in safe assets. Strong global demand for the dollar-denominated assets remains as the biggest driver of the US' persistent trade deficit and long-run decline of US manufacturing.

In the recent times, there have been discussions about an imminent end of the dollar's domination.

The following are some of the reasons cited for the dollar's decline:

- \* Concerns about the US' ginormous debt mountain and how it could spell trouble ahead

- \* Unease at the US government's overt "weaponization" of the dollar, as US continues to leverage its financial power to punish adversaries, the recent being freezing of Russian reserves in the wake of Russia-Ukraine war.

- \* Emergence of a more decentralized era in global finance with cryptocurrencies and central bank digital currencies.

Most of these prophecies and wishes have been proved wrong. Fundamentally US hegemony had changed levers of direct forms power from inter-governmental channels to indirect forms of private markets.

## US DEBT AND DEFICITS:

Years of elevated budget deficits, have taken the US debt to the historically high levels 330 per cent of GDP.

But the rising debt and deficits are not unique only to US. Across the global economy, governments owe an \$91 trillion, an amount almost equal to the size of the global economy.

By being the major reserve currency of the world, the current level of debt will not lead to a default or result in US dollar losing its dominant role in the global economy but will likely impose eventual costs in the form



**GREENBACK:** Safe asset REUTERS

of lower growth and higher inflation.

## WEAPONISATION OF \$

Over stretched reliance on sanctions to coerce other countries is gradually losing its effectiveness and slowly degrading the most influential tools.

Several countries are resorting to bilateral currency arrangements. But these are too insignificant to dethrone US\$.

## TECH INNOVATIONS

Technological innovations outpace payment and regulatory innovation and lead to a situation where trust in technology replaces trust in sovereign nations. Central Bank Digital Currencies (CBDC) and cryptocurrencies with their blockchain technology are an example.

Despite their initiatives, none of the top seven currencies that represent more than 95 per cent of global reserve currencies have yet launched a digital version. Even if it sees the light of the day, the role of CBDCs is broadly limited to the areas of cross-border payments.

Beyond lack of oversight, there are some fatal flaws in their monetary economics that prevent Crypto currencies from being adopted and widely accepted as a medium of exchange and as a store of value at a large scale.

It is obvious that any emergence of alternative reserve currency would take years if not decades to evolve as a reserve currency needs the backing of large, open credit markets, strong, diversified financial institutions, robust regulatory and legal framework, cohesive Political system and a central bank cognisant of its global responsibility.

As such dominance of US dollar is set to stay for the foreseeable future

The writer is the Chairman of SYFX Treasury Foundation. Views are personal