Question marks emerge over dollar supremacy

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The latest round of financial turmoil—the collapse of the Silicon Valley Bank (SVB), the second largest bank failure in monetary terms in US history and the forced takeover of Credit Suisse—has again raised long-standing issues about the stability of the global financial system and role of the dollar as the world's reserve currency.

Questions were raised a year ago when US and European sanctions, imposed after the launching of military operations in Ukraine by the Putin government, resulted in the freezing of around $300 billion in financial assets held by the Russian central bank.

While there was little public comment on the US-directed action, able to be imposed because of the global role of the dollar, it sent a shiver of fear through the central banking world. If it could happen to Russia, then it could happen to any country that crossed the US path in the future.

And there was already the experience of Iran where the US under the Trump administration was able to enforce unilateral sanctions, despite the objections of European powers, because of dollar supremacy.

Writing in the *Washington Post* last month, columnist Fareed Zakaria, noted that while it got limited media coverage, the most interesting outcome of the talks between Russian President Vladmir Putin and China President Xi Jinping were the comments of Putin after the summit.

"We are in favour of using the Chinese yuan for settlements between Russia and the countries of Asia, Africa and Latin America," he said.

Zakaria commented that the implication of the statement was that "the world's second-largest economy and its largest energy exporter are actively trying to dent the dollar's dominance of the international finance system."

He dismissed the prospect that another currency would replace the dollar as the global currency, but there was a "more likely scenario" that it could "suffer weakness by a thousand cuts."

There are indications that such a process is underway. China and Russia are now conducting two thirds of their trade, which has increased significantly, in their own currencies.

China has made a deal with Saudi Arabia that it can pay for oil purchases in yuan, the first time in almost 50 years that the Saudis have been prepared to accept anything other than dollars as payment for oil.

The French company TotalEnergies has just done a deal with China for the purchase of a cargo of LNG denominated in yuan.

Brazil, the largest Latin American economy, for which China is its largest trading partner coming in at around $150 billion a year, is embracing the yuan.

Last week China and Brazil announced they would use their own currencies to settle their trade accounts, effectively ditching the dollar for bilateral relations. It was also decided that Brazil would sign on to an international payments system which Beijing is trying to set up as an alternative to the US-dominated SWIFT international payments and messaging system.

None of these developments mean that King Dollar is about to be dethroned, but they do signify an acceleration in a long-term process. The proportion of dollars in central banks currency reserves has fallen from 72 percent in 1999 to 59 percent today.

While its position in trade transactions is weakening, the dollar continues to dominate financial markets. It comprises 90 percent of all foreign exchange transactions and about two-thirds of the issuance of securities is conducted in dollars.

But the series of financial storms in the US, the latest of which is the collapse of SVB and concerns of over the stability of middle-sized banks whose holdings of US Treasury bonds have lost significant market value because of the Fed's interest rate hikes, is causing nervousness.

In his comment piece, Zakaria cited an observation by investor and financial analyst Ruchir Sharma on the latest turmoil.

"Right now, for the first time in my memory, we have an international financial crisis in which the dollar has been weakening rather than strengthening. I wonder of this is a sign of things to come," Sharma said.

If that were the case then it was a cause for worry, Zakaria noted.

In an earlier article, he pointed to what he called the "inflexibility" of US foreign policy which increasingly consisted of making demands and issuing threats and condemnations all which "evokes the inertia of an aging empire."

The inflexibility in foreign policy, deriving from the conception of the unipolar status of the US, was even more evident economically.

"America's politicians have gotten used to spending seemingly without any concerns about deficits—public debt has risen almost fivefold from roughly $6.5 trillion 20 years ago to $31.5 trillion today. The Fed has solved a series of financial crashes by massively expanding its balance sheet twelvefold, from around $730 billion 20 years ago to about $8.7 trillion today. All of this only works because of the dollar's unique status. If that wanes, America will face a reckoning like none before."

There is only one case in economic history where the currency of one imperialist power has replaced that of another – the displacement of the British pound sterling by the US dollar.

Throughout the 19th century during the global rise of capitalism, sterling was the basis of the international financial system. That role ended when the British financial dominance was severely eroded by World War I.

The dollar did not become the dominant global currency as a result of agreements and negotiations, but attained this position after two world wars through which the US became the preeminent imperialist power.

The two world wars were punctuated by vicious currency and trade conflicts in the 1930s during which the world was divided into rival economic and financial blocs.

Like Britain before it, the US is now an "aging empire" amid indications, only at the early stage to this point, that something akin to the blocs of the 1930s is returning to the global economy. The consequences will be no less violent as the US seeks to thwart any undermining of dollar supremacy by both financial and military means.