

Is the Dominance of the US Dollar as a Global Currency being Eroded?

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In recent times, amidst the ongoing conflict between Russia and Ukraine, coupled with the multifarious activities of emerging market nations, the international market once again contemplates whether the long-standing hegemony of the US dollar is under threat. We elucidate the dominant position of the US dollar in the global market through stylized facts pertaining to trade and international financial transactions. Firstly, the world's export share denominated in dollars substantially surpasses the share of exports to the United States, and a similar situation prevails in imports as well. Secondly, although the US dollar's portion of global official foreign exchange reserves has experienced a decline, it still far exceeds the proportion held by other currencies. Lastly, statistics from the Bank for International Settlements reveal that the US dollar continues to reign as the preeminent currency in international banking operations.

Following the outbreak of the Russia-Ukraine conflict, the United States and its allies froze approximately half of Russia's foreign exchange reserves held in US dollars at the central bank, and expelled its major banks from the SWIFT system. These financial sanctions can be viewed as the weaponization of the US dollar. To avoid being constrained by the US dollar, certain central banks have begun diversifying their foreign exchange reserves into multiple currencies and conducting cross-border transactions denominated in their own currencies or other non-dollar denominations. This may expedite the emergence of ongoing proposals for the transformation of the international monetary and financial system. Simultaneously, a series of events indicating a trend towards de-dollarization has occurred among emerging market countries. These include China and France's completion of liquefied natural gas import transactions settled in Chinese yuan, ASEAN's discussions on reducing reliance on the US dollar in trade and financial transactions, and Brazil and China reaching agreements to settle bilateral trade and financing in their respective currencies rather than the US dollar. These measures signify China's pursuit of reducing dependence on the US dollar and its efforts to expand the use of the renminbi as an international reserve currency.

The United States maintains its long-term dominant position in the global market not only due to its economic size but also because of the soundness of its institutional framework, despite its inherent flaws. It has established standards that contribute significantly to its prominence. China's past capital and financial controls restricted the

international use of the renminbi. However, the removal of restrictions on cross-border capital flows and the liberalization of currency exchange have facilitated the international application of the renminbi in financial and trade transactions. Although the proportion of the US dollar in official foreign exchange reserves of various countries has decreased, this primarily stems from the increasing share of non-traditional reserve currencies (defined as currencies other than the US dollar, euro, yen, and pound sterling).

Under the influence of international geopolitical risks, financial market developments, and technological advancements, the global economy may potentially diverge into trade blocs with different political systems, ideologies, and reserve currencies, thereby challenging the status of the US dollar as the dominant currency. However, the potential erosion of the US dollar's position is not likely to come primarily from its main competitors but rather from a broad range of non-traditional reserve currencies serving as alternatives. Additionally, emerging markets, predominantly represented by BRICS countries, are attempting to establish independent trade systems that could pose a long-term threat to the dominance of the US dollar. However, this erosion would require reducing dependence on the US dollar as participation increases. Furthermore, the evolving payment mechanisms could also pose challenges to the dominant position of the US dollar. Consequently, the future outlook may involve the US dollar striving to consolidate its dominance while witnessing changes in the relative importance of non-traditional reserve currencies or digital currencies.

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