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Dedollarization: The Role of Expanded BRICS and the Global South

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Abstract:

Dedollarization is accelerating. *Inter alia*, the US-led western sanctions have accelerated the thinking about dedollarization and some tentative actions in the BRICS countries in particular. Further expansion of BRICS has strengthened these tendencies. With support from the other countries in the Global South, dedollarization will receive continuing impetus.

It is one of the main theses of this paper that eventually the US will be forced to settle down to its substantial but reduced role in the Global Economy while a multipolar order replaces the brief ---in historical terms--- the dollar-based US hegemony during the cold war and dollar dominance during the unipolar two decades from 1991 to 2010. However, the pace of this evolution will depend on international politics and strategic foreign policy moves by the major powers and coalitions in both the Global North and the Global South.

Thus a historical nodal point has arisen with the advent of the tragic war in Ukraine and the US hostilities towards China. The sanctions regimes of the US-led Global North have compounded the instabilities in the existing system. As the world system moves towards multipolarity, an opportunity exists for the Global South to construct through partial delinking from the post WW2 financial architecture under US hegemony. Construction of an expanded BRICS-led supra regional financial architecture along with regional financial architectures will be a strategic step forward. Within two decades dedollarization will become a reality. Finally, a new non-aligned movement and construction of genuinely pro-people development programs can also become a reality.

Keywords: Dedollarization, Regional and Cross-Regional Financial Architectures, New Global Financial Architecture, CBDCs, Ukraine, multipolarity, BRICS, expanded BRICS or BRICS-plus, China, Russia, The Global South

1.Introduction

Dedollarization is definitely in progress. If anything, the US-led western sanctions--- particularly against the Russian Central Bank, and financial sanctions in general--- have accelerated the thinking about dedollarization and some tentative actions in the BRICS countries in particular.¹ Significantly, BRICS as a South-led loose informal coalition now includes important oil and gas producers like Iran and Saudi Arabia. Future expansions of this augmented BRICS will happen soon.

These further expansions of BRICS will undoubtedly strengthen the dedollarization tendencies as part of an emerging multipolar global order. It is perhaps safe to say now that barring seismic reverse geopolitical and geoeconomic shifts, further expansion of BRICS with support from the other countries in the Global South, dedollarization will receive continuing impetus.

It is one of the main theses of this paper that eventually the US will be forced to settle down to its still substantial but much reduced role in the Global Economy while a multipolar order replaces the brief ---in historical terms---of the dollar-based US hegemony during the cold war and dollar dominance during the unipolar two decades from 1991 to 2010. However, the pace of this evolution will depend on international politics and strategic foreign policy moves by the major powers and coalitions in both the Global North and the Global South. In what follows, I first develop an outline of a new framework for a Global Financial Architecture beyond the US and Global North hegemony. Then I explore possible dynamic paths of dedollarization within this framework. It is important to underline in this context the uneven development of the international system including the monetary-financial parts of this system.²

¹ See Khan (2023, a-f) for a detailed discussion of these points.

² Khan and Patomäki. (2013) develop an extended and updated framework in the spirit of Keynes and Kalecki. Ontologically, their framework is firmly grounded in critical scientific realism and takes into account the uneven development of the global political economy.

The world has been through repeated financial and economic crises as neoliberal policies for coercive liberalization that served mainly the perceived interests of the Global North--- the US in particular--- unraveled. ³Among the thinkers of the Global South as well as responsible economists from the Global North, if not the earlier Mexican crisis, then certainly the Asian Financial Crisis and the contagion it created unleashed a process of questioning the wisdom of the standard recipe of the Washington consensus. The process of questioning intensified after the 2008 global crisis. This process is still continuing; but the real costs of crises have forced on the policy agenda the question of what kinds of national and international policies and institutions are appropriate during the current period and in the foreseeable future. For the policy makers from the Global South finding an approximately right institutional structure for a new global financial architecture has become even more urgent. Recently, several prime ministers from Africa have directly called for creating a new global financial architecture . What advice can economists from the Global South give to their policy makers at this juncture? Can the Global South and expanded BRICS move towards new types of Regional and Global Financial Architecture(RFA and GFA) as strategic moves away from dollar and other Northern currencies and payments systems play an increasingly important role in the evolving international system?

2. Uneven Development and the Role of Historical Contingencies⁴

The role of structural unevenness in the global economy is particularly important to recognize within the proposed framework of analysis. The range of economies, the types of polities, the institutional capacities and resource endowments including technological progress and capacities for innovation all vary widely. A simple system of gold standard or adjustable peg or free and flexible exchange rate together with free multilateral trade under, say, the WTO arrangement may therefore be simplistic. It may serve the needs of one group of actors, for example, the advanced economies with well-developed financial services sectors, than some others. How best to achieve a synchronized growth and development regime that is perceived to be fair by all is indeed a challenging problem.

It is worthwhile to point out that a unique set of historical circumstances led to the Bretton Woods system that initially was a second best to Keynes's more comprehensive plan for postwar international financial settlements. The White plan from Washington made US dollar the main currency for global financial settlements under US hegemony implemented through the IMF. As the US balance of payments started to show ever larger deficits, partly because of wars but also because of increased US consumption of

³ There is a large and still growing literature on these issues. See for example Stiglitz(1994), Akyuz and Cornford(1995),Bhagwati(1998),Jomo(1998),Cohen(2008), Eichengreen(1999, 2011), Kaminsky and Reinhart (1999),Krueger(2000), Khan (1999a,b; 2002a,b,c; 2004a,b ;2011a-d, 2021a,b;), Azis(1999), and Khan et.al. (2023)

⁴ See the literature cited in the references section at the end of the papers to place the issue of unevenness and institutional change in evolutionary theoretical and historical context. Specific issues ranging from macro instabilities to micro corporate governance, sanctions and critiques of the current system are also cited there.

imported goods, the US suspended the gold window in the early 1970s. Here a second set of unique historical circumstances favoring US financial supremacy came into play.

After the energy---in particular oil--- crisis that followed the war in the middle east in 1973, the US deficit increased even more. The question arose as to how to recycle these “petro-dollars”. Ultimately, Saudi Arabia and other OPEC nations agreed to buy US Treasury bills. Essentially this meant financing the US deficits by recycling the surplus abroad by lending money to US treasury. Thus the exorbitant privilege of the US dollar that De Gaulle had complained about earlier became even more so. The US could merrily get real goods and services by non-gold backed US dollars. This system plus ancillary financial messaging system such as the SWIFT, has meant that unlike other debtor countries, the US can freely spend more than its domestic national income without the kind of painful adjustments resulting in austerity and low growth performance for almost all of the countries in the Global South. But now that period of exorbitant privilege enjoyed by the US may be coming to an end.

3. New Historical Conjuncture: An evolutionary institutional theory perspective

The overarching reason for this is the end of unipolarity. Even when the USSR existed we had two bounded regional systems in the world led by the two great powers, the US and the USSR. They were bounded politically through being hegemonic in their own geographically bounded areas although proxy wars and other contestations over the Global South would continue until the fall of the USSR. Most importantly, since trade and investments were also bounded, especially in the Soviet bloc, the US could exercise hegemony over the Global South by relationships of asymmetric dependencies dominated by the US and the institutions it had set up after WW2.

After the fall of USSR, the US enjoyed a unipolar complete hegemony throughout the 1990s up until the early years of the 21st century. This fact alone can explain why the Global South including Russia and even China accepted neoliberal doctrine and practices. But in China, there was always opposition within the governing circles. I have found this to be the case during my many visits and conversations with the influential policy makers in China from 1991 till now. In particular, when I was at UNCTAD during the global financial crisis, I witnessed some open and angry debates between Chinese neoliberals and their opponents. Now since 2018 at least, the US ruling class seemingly is bent on confrontation with China. Together with the tragic proxy war in Ukraine and indiscriminate use of economic sanctions against Russia, China and other countries by the US and its junior partners including EU and Japan this aggressive stance against China has pushed China and Russia closer. Now these two countries are more willing than before to set up alternative payments mechanisms, and a new modified type of global financial architecture. Will this succeed and how fast can dedollarization and the US hegemonic decline proceed?

In my earlier works including the chapter in my 2004 book on *Global Markets and Financial Crises*, using a theory of evolution of institutions in a complex system, I outlined a plan for formation of a regional financial architecture in Asia and other

regions, and reform of the IMF by making its treatment of surplus and deficit countries symmetric. Given the lack of political will at the IMF and US treasury---despite some pious or perhaps even sincere rhetoric at times---it does not seem that the US or the IMF will take the path of reform. Rather, the recent lenient treatment of the countries that are effectively US vassals and the punishing moves against the Global South countries that dare to declare some semblance of independent policy making, it is clear that my earlier optimism based on institutional economic theory and history as well as evolutionary economics, was misplaced.

Therefore, even in a multipolar system, older institutions like the IMF and World Bank and their European counterparts will largely bow to the US command. Since the Global South can not withdraw from the T-bills based US dollar hegemony at once, if the current manifestation of political will in the BRICS and the Global South strengthen, a gradual delinking over the next two decades will be politically and economically feasible. What is achievable more quickly will be the strengthening of bilateral and regional swap arrangements and formation of both general regional payments mechanisms with “currency-equivalents” like Asian Drawing Rights (ADR)---and even a Global South monetary unit such as an Asian Currency Unit(ACU) in the future---- along with specialized Global South financial institutions like AIIB and Latin American and African regional banks run by experts from the Global South who have both technical expertise and a vision for alternative pro-people development in the Global South.

From the policy perspective, it is important to know if the existence of a Global South based regional financial architecture would be helpful in any way during the future crises. This is really a counterfactual question but vitally important for preserving and enhancing the well-being of people.

In contrast with the behavior of the IMF, within the proposed regional financial architecture, at least the following aspects will be possible on the basis of applying an evolutionary theory of financial instabilities under globalization in a multi-polar system:

1. Through constant regional monitoring the Global South will sense the danger ahead of time. Even a regional monitoring unit alone would have been able to do better than the IMF team in Asia before and during the Asian Financial Crisis.

2. Through constant formal and informal contact with the officials in member governments and the private sector, the proposed regional financial architecture will be able to size up the possible extent of the problem earlier and better than the IMF record so far.

3. Through prompt and early action the proposed regional financial architecture will provide liquidity to the system, and punish bad management in coordinated measures with the national governments.

4. The proposed regional financial architecture will be able to start regional discussions about bankruptcy and work out procedures by keeping in close touch with the history and legal issues facing particular countries.

5. The proposed regional financial architecture will be in a position to use both moral suasion and toughness to keep both regional creditors and debtors in line.

4. Dedollarization under a New GFA in the Multipolar World :

The replacement of the gold standard---and the British hegemony---by the dollar-based system was the result of two world wars and the inter war crises of two decades. The breakdown of the system in 1971 was followed by the 1973 Arab-Israeli war and the agreement by Saudi Arabia in particular to accept a dollar-US T-bills bases international payments system. The current account surpluses of the resource rich Global South countries were generally converted to T-bills in the capital account. The Us dollar thus became the currency of account for all the parts of BoP including the reserve account.

The US from 1973 onwards has had the luxury to run both budget deficit and trade deficit without having to follow expenditure reducing policies. When other currencies such as the Japanese yen were deemed to be undervalued by US policy makers, US exercised hegemonic privilege to pressure the offending countries to revalue. In case of Japan during the 1980s the Plaza accord revalued the yen. The bursting of Japan's bubble economy and subsequent decades long stagnation forestalled the claims of yen to replace US dollar. What we have now, however, is a world of multiple currency transactions that is gaining momentum with the increased use of US and EU sanctions as weapons of power. Ironically, the exercise of such hegemonic power by the US is serving as a spur for the BRICS plus and the Global South to break away from the US dollar-based order.

At present, currency diversification is playing an important role in this accelerated stage of dedollarization. Such currency diversification could and most likely would play a strategic role in reducing dependence on the US dollar. At the minimum, such a strategy will mitigate the market and other risks associated with exclusive reliance on the US dollar by vulnerable countries. But to be successful, the alternative currencies and payment mechanisms must be viable.

The BRICS plus central banks(CBs) have begun to act to make various dedollarization moves viable. It is well known that those CBs that can act with sovereignty(witness China, India and Russia among others) are able to formulate monetary policy in the national interest, manage currency reserves, plan the promotion of alternative payment systems etc. CBs are well placed in such sovereign countries to build institutional international collaboration. One of the most important aspects of such CBs is to promote regional (and for BRICS plus, cross-regional) financial architectures. Clearly the expanded BRICS and the Global South countries are headed in this direction.

It is important to note particularly that central banks of sovereign countries with monetary sovereignty are vital to the project of dedollarization. Through proper and timely adjustment of real interest rates CBs can smooth out business cycles except when there is a liquidity trap. Managing liquidity becomes important particularly at such times and the government has to use fiscal instruments for stimulating investment and consumption as well. Exchange rate policy is another vital area for CBs. Likewise, the CBs are playing important roles in arranging currency swap agreements. Both bilateral

and multilateral arrangements in swaps and other payments mechanisms are important in reducing dollar dependence.

Will the advent of Central Bank Digital Currencies (CBDCs) play a role in dedollarization? Here there are both early mover and network aspects. BRICS-plus countries can play a pioneering role and reap network advantages by setting up swap arrangements etc. But by themselves CBDCs are not panaceas. They have to form a strategic part of a set of coherent and coordinated policies among the BRICS-plus group and more generally, The Global South.

BRICS plus CBs are also playing an increasingly important role in fighting for reforms in the international financial institutions. Generally, these have been geared towards making these institutions more fair.

Promoting a fair multipolar system will require treating dollar as one important currency but not the dominant one. The US will continue to be a great economic power but not the only one. A symmetric payments system will increasingly move towards the use of SDR and ADR like currencies of settlement. Most importantly, the US will no longer be able to live beyond its means by issuing more debt by whatever amounts it wishes because that will require increasing the rate of interest which is tantamount to decreasing the price of T-bonds of various maturities.

On the part of the expanded BRICS and the Global South strengthening financial stability through prudent reserves management and institutional development nationally and internationally in the Global South will be crucial. For this reason, robust risk management, international policy coordination, development of world class financial standards, and capacity building along with technical assistance as forms of South-South cooperation must also be accelerated. Through contingency planning and timely interventions, crisis management will become more feasible. Ultimately, a gradual move towards a genuinely symmetric international payments mechanism where no single currency is dominant will be necessary. A necessary condition for this to happen is the end of US hegemony. The world is indeed moving in this direction. The real question is: will the US agree to a nonviolent end to its dominance? The answer is not clear at this point.⁵ It is absolutely fundamental to recognize the importance of a peaceful transition. In the nuclear age, direct great power violent confrontation could easily escalate into a nuclear war where all will be losers. Therefore, difficult as it might be for the US policy makers to give up adventurism⁶ in a desperate bid to recover from declining hegemony through attempts at dominance, they are unwise moves in the extreme. In fact, these forever wars are already depriving the US citizens from real economic and military security. Negotiations in good faith with full recognition of reality is an urgent necessity under such circumstances.

⁵ See Khan(2023f) for a discussion of the various nuances from a geopolitical perspective.

⁶ As thoughtful realists like Mearsheimer, Walt, Layne and others have pointed out, the US is a rich country which is vulnerable only to nuclear (and now hypersonic and other types of missiles with conventional warheads) attack. Therefore, it has been tempted to go abroad and engage in proxy wars and direct wars against weaker nations. Continuing on this path where great powers like PRC or Russia are involved is a recipe for catastrophe.

5. Conclusions:

Breaking away from the US hegemony requires among other things, a firm move away from the US dollar and other Northern currencies. Ultimately the multipolar emerging international system will require a new, more balanced and fair international monetary order as well. This has been the main thesis of this paper.

The fundamental requirement for financial stability and independence of the Global South at this juncture, therefore, would seem to be the creation of an expanded BRICS including many energy producers that can lead to both supra regional financial architecture for the Global South along with specific RFAs in Asia, Africa and Latin America with enough liquidity and technical expertise. The Asian Development Bank provided quite a bit of liquidity to Korea in particular during the Asian Financial Crisis, but did not even have a monitoring unit when the crisis broke out. Furthermore, the autonomy and integrity of any Global South future RFA, in Asia and elsewhere are issues that need discussion. The relationship between the new RFAs and the IMF also needs to be further specified. These are matters that are of necessity evolutionary by nature.

As I have discussed in my recent papers, in a multi-polar world, there will also be an opportunity to launch a new non-aligned movement from the Global South. What is needed is a combination of bold vision and practical realism supported by the relevant expertise for the benefit of the great majority of the people on our planet.

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