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«The Paradigm Shifts In Global Finance»

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The US proprietary usage of the dollar financial infrastructures is here to stay. What then for the Euro and the RMB: appeasing, circumventing, or doubling down?

The Presentation draws on "Far-reaching consequences of US financial sanctions . The Dollar Shortage and the "Triffin Moment". 2019

Abstract

In the post Second War, U.S. Administration has largely increased the use of financial sanctions against other states and non-state actors.

The large expansion of the usage of the dollar in payment and lending, has disproportionally empowered these measures.

Targeted entities, and third parties have endured   disconnection from dollar finance and payments circuits, and large penalties mostly on international banks.

The picture signals increasing uncertainty on the provision of liquidity in the global finance, and the fatigue of the current monetary system based of a single currency.

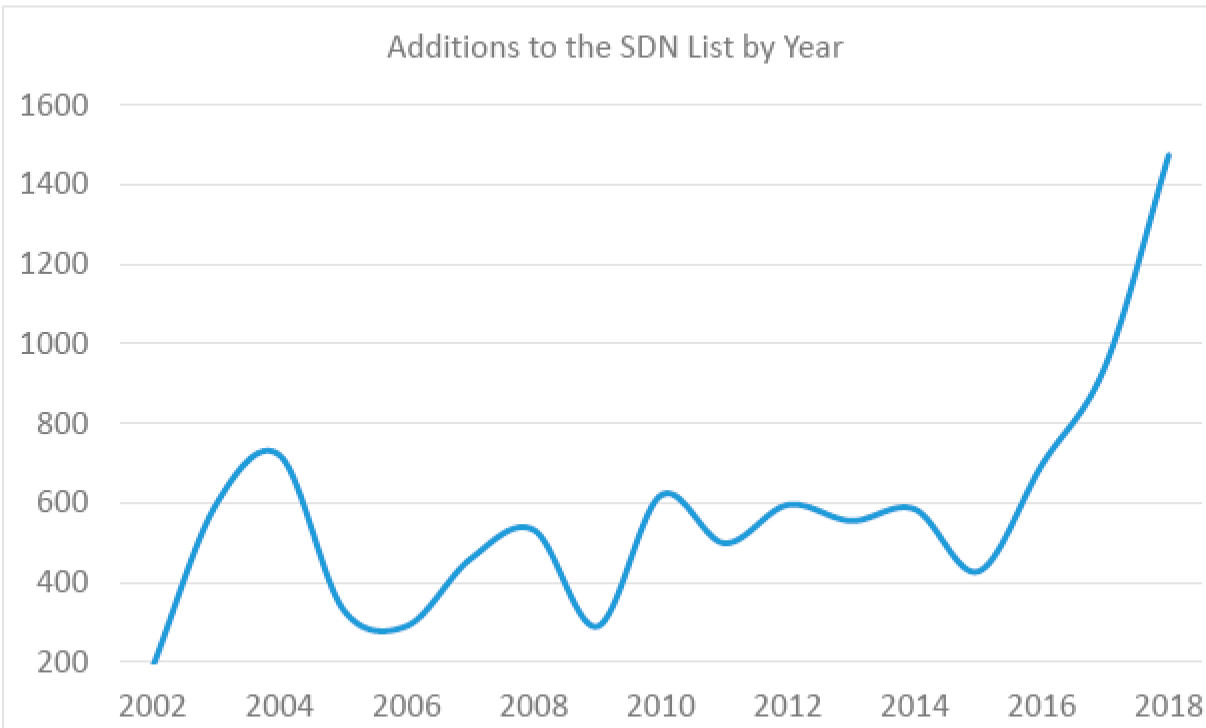
How are policymakers in the EU and China responding to these challenges?

The Office of Foreign Control (OFAC) launched an improved a new and improved tool for searching its Specially designated Nationals (SDN List)

- The SDN List is a compilation of entities and individuals that have been targeted under one or more of Treasury sanctions programs.
- Inclusion on the SDN list generally prohibits U.S. banks from maintaining accounts for those listed.
- U.S. persons could face civil or criminal penalties for engaging in business dealing with them.

US financial sanctions on the rise

- Figure 1. Additions to the SDN List by year.

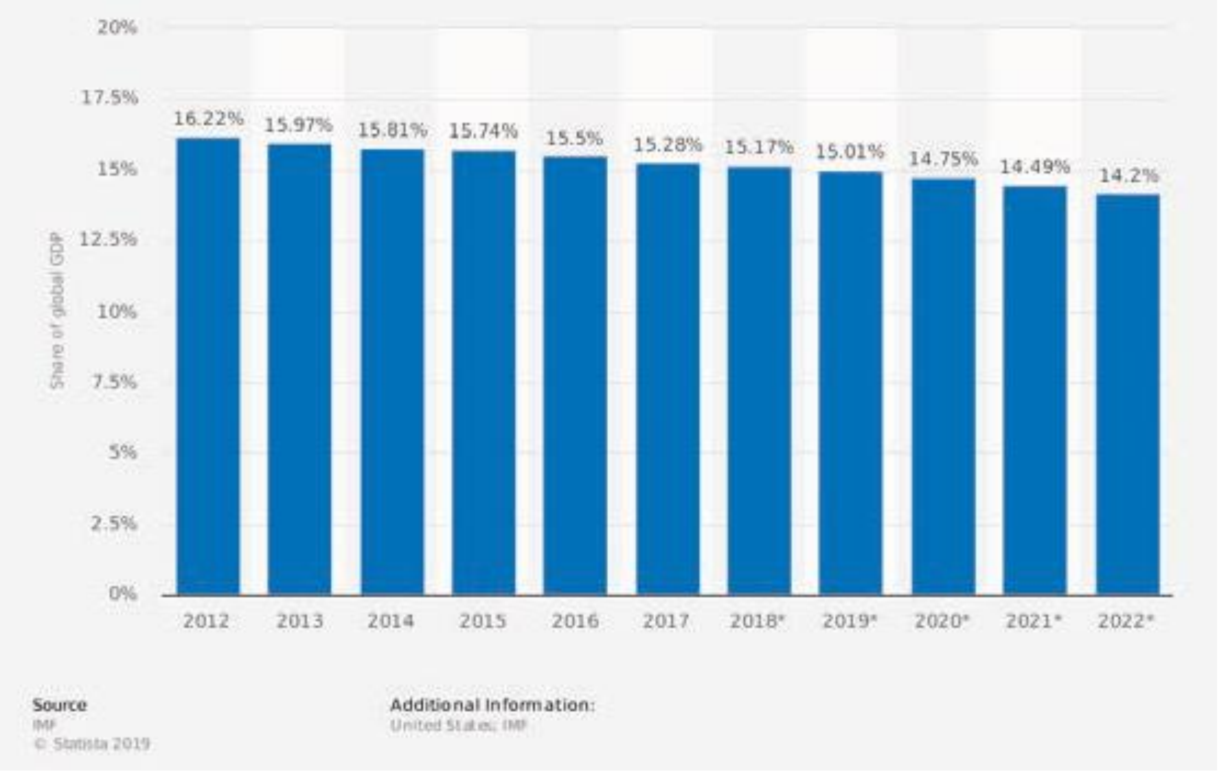


<u>Source</u>: Graph Compiled from Data Released by the Office of Foreign Assets Control

Structural factors behind US over-usage of F-Sanctions.

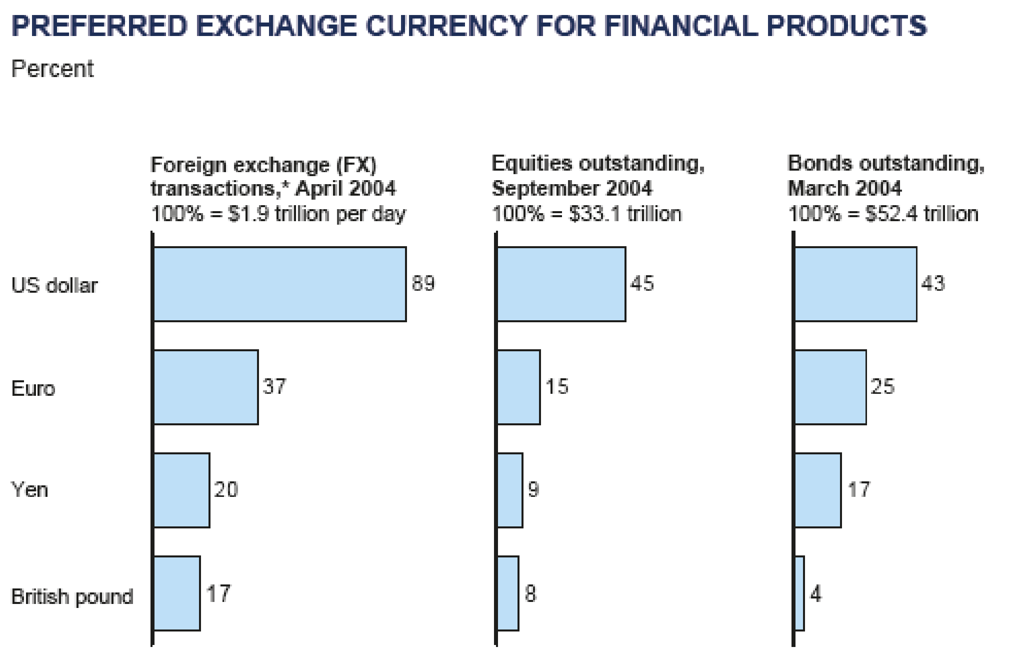
GDP inversely proportional to US supremacy in the global economy, accounts for just about twenty four percent of global GDP, in sharp contrast to the seventies when the share was more than thirty percent

- Figure 2. Share of the US GDP 2012-2022



Dollar the preferred currency of choice in global finance

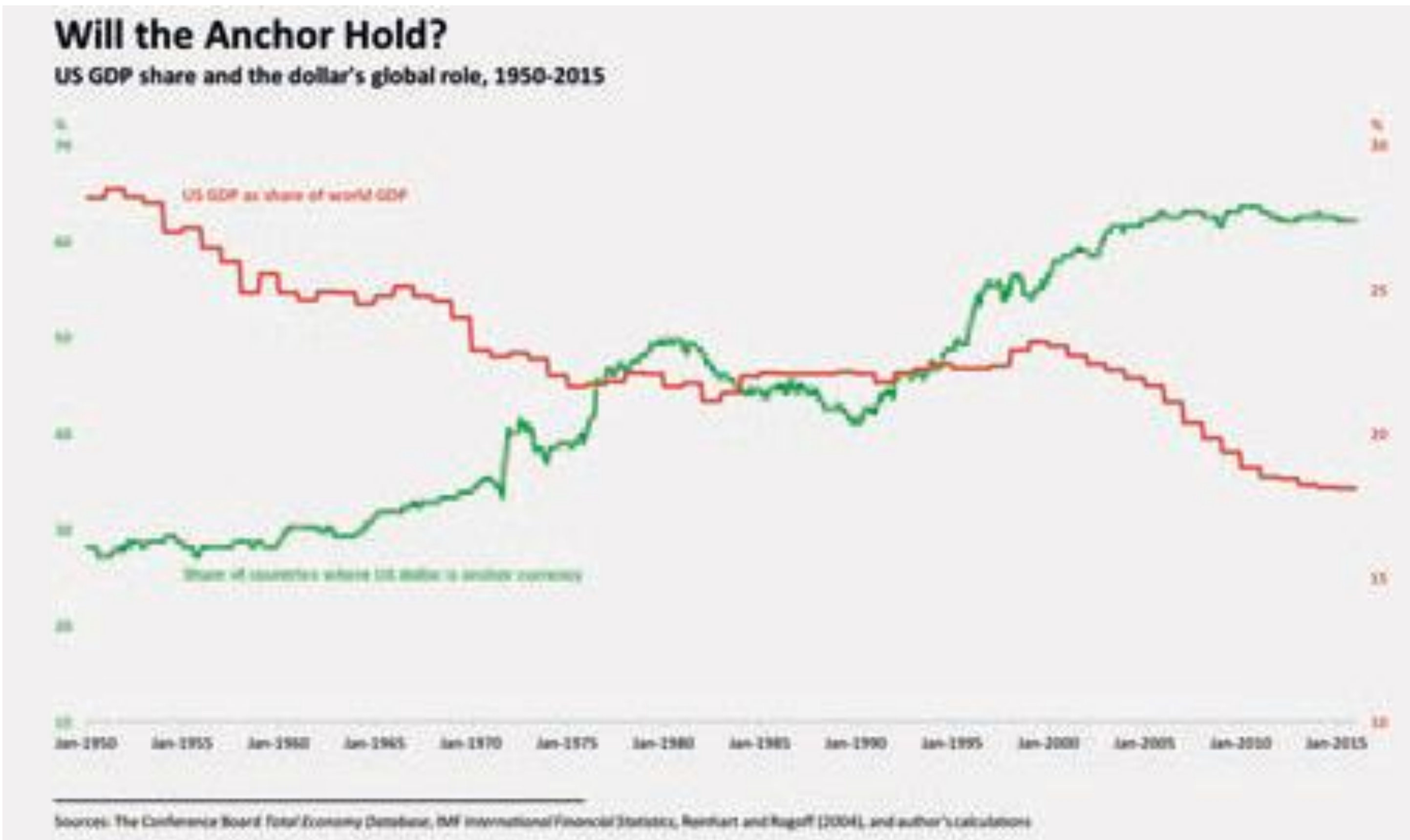
Figure 3. US Dollar the Preferred Exchange Currency for Finance.



* Because there are two currencies in a single FX transaction, the potential total is 200%; the share of other currencies comprise the remaining 37%
Source: McKinsey Global Institute Global Financial Stock Database; Federation of World Stock Exchanges; Bank for International Settlements (BIS)

Reinhart's Mismatch

- Figure 4. **US GDP and Dollar's Global Role**



Three Comments on figures 3 and 4
Downplaying the mighty US statecraft

1. The increased use of financial sanctions is not an expression of U.S. statecraft, which had never failed before.

2, These measures   speak for the U.S.'"perception of diminishing supremacy in the global economy" (Satyajit Das 2018).

3, In reality, U.S. GDP accounts for just about twenty four percent of global GDP, in sharp contrast to the seventies when the share was more than thirty percent.

Financial infrastructures make the backbone of the global financial system, and are crucial for the running of the US dollar standard

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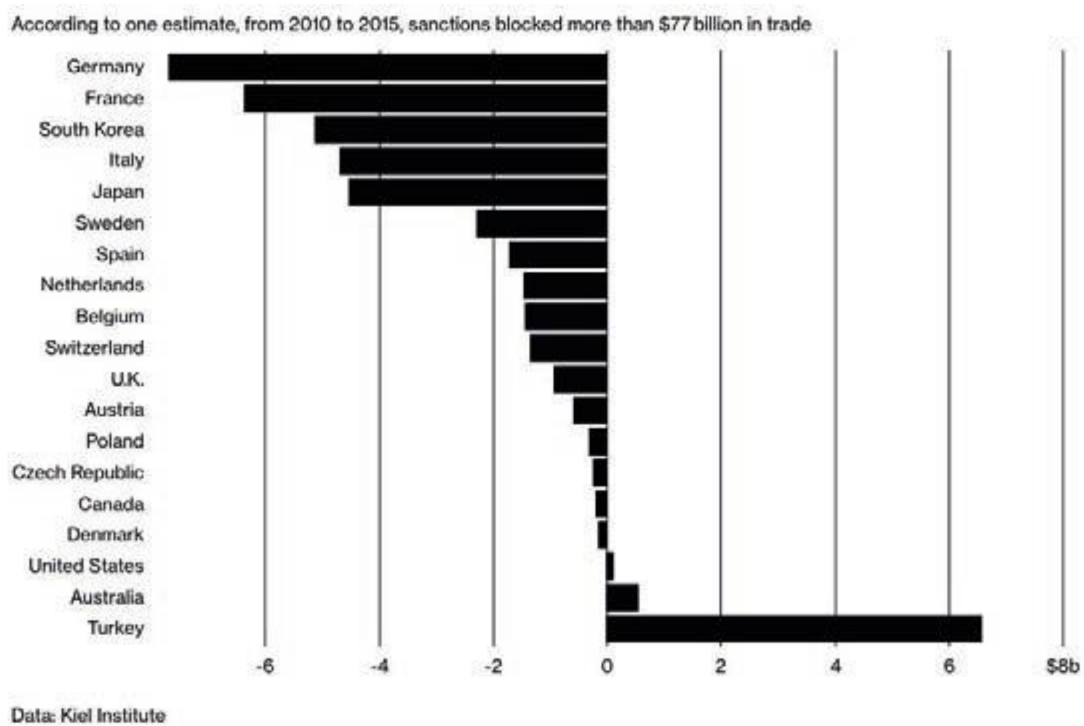
- The global financial system, through which banks and corporations exchange terabytes of financial
- data every day, has been enhanced by massive transnational telecommunications networks since the
- 1960s, largely dominated by U.S. led or controlled institutions (Shen 2018).

- Financial infrastructures “are not only decisive in empowering a currency to be adopted by international actors taking part in international trade but are also crucial for the smooth running of the U.S. dollar standard” (Faudot 2018).

Third parties caught in crossfire
Financial Sanctions on Iran

- Figure 5. **The Cost of Sanctioning Iran (2010-2015)**



Is there the Triffin Moment that a national currency cannot play a global currency role?

- *Leveraging the use of financial sanctions, US Administration overtly aims at causing disconnection from the dollar and the isolation of the targeted and third parties from capital markets.*

- *That stands for a dollar shortage, and brings to the situation typically described in the Triffin dilemma.*

- *When a national currency cannot combine domestic economic and political interests, the sub-optimal supply of liquidity calls for alternate national sources to come in, and allow markets to continue to function* (Eichengreen 2018).

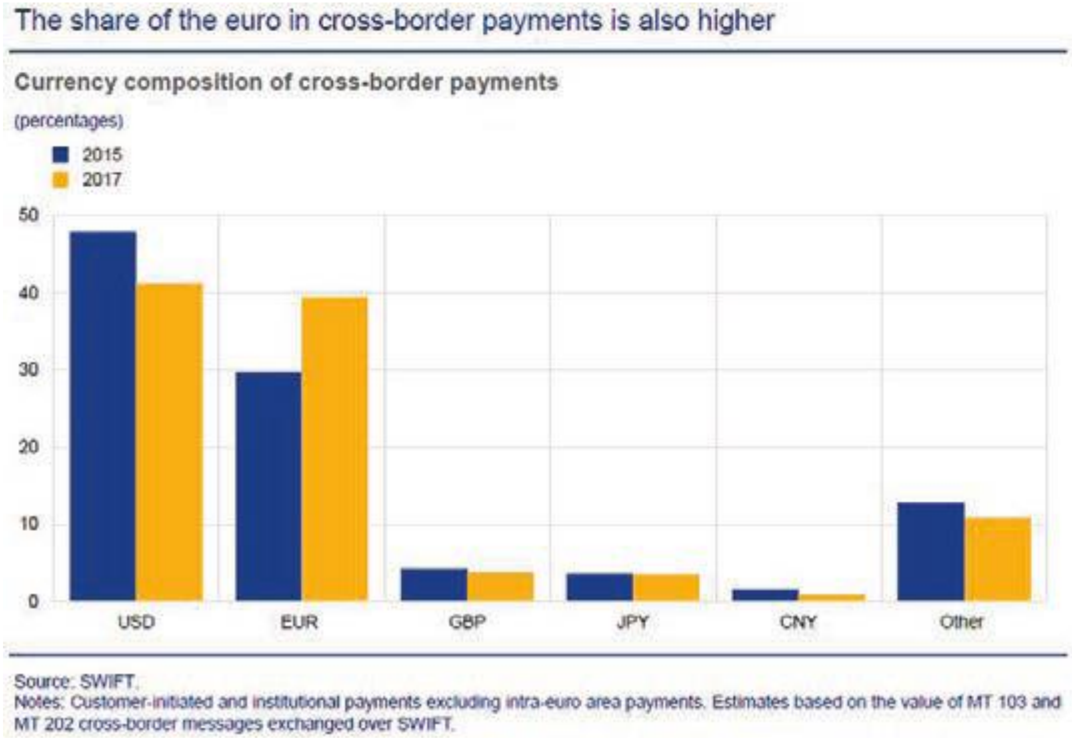
Euro in Cross-Border Payments and FOREX Reserves

Chinese RMB and the Euro used in continent-sized economies, and covering a substantial shares of international trade, still have limited share in Central Banks reserves.

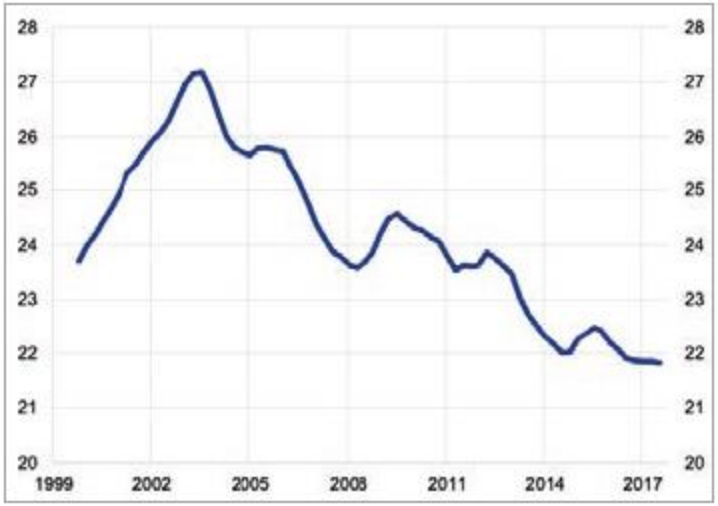
The case is especially relevant for the Euro (Figure 6, 7), as it

Euro in Cross-Border Payments

- Figure 6.



Euro Shares in Forex Reserves (1999-2017)



Source: Benoît Cœuré 2019

Is the euro ready for taking a global role?

- Disconnections from financial markets, deviations of capital flows, and the levying of huge fines are set to generate randomized situations of dollar shortage. Inadequate alternative sources of liquidity have generated uncertainty over the reliability of dollar-oriented institutions, and point clearly to the flaws of current international monetary arrangements (Ocampo 2009).15

- So far, currency inertia and a sub-optimal internationalization of alternative currencies – the euro or the renminbi – have left the international monetary regime still orbiting around the dollar, leaving global liquidity, in terms of dollar liquidity alone, inadequate.
- A fully-fledged internationalization of the euro and the renminbi might alleviate this liquidity crisis, but would be no guarantee of financial stability.

The current state of play hint for alternate currencies entering the global game.

- Option 1. The creation of a “true global currency” on the basis of the IMF’s SDRs . This option implies the parallel circulation of different national and regional currencies, as the latter could continue to circulate
- alongside growing SDR reserves (Ocampo 2019).

- Option 2. Getting down to the nitty-gritty with the full internationalization of the euro and RMB., and creation of appropriate financial infrastructures there are huge costs to bear.

- Both options work fine for a multi-currency system.

- Option 1 raises doubts over whether the U.S. Administration would consent of allowing the dollar primacy to be restrained or dissolved into the IMF’s “true global currency”.

- As for Option 2, the one I like best, implies large investment, expertise, money, and likely attempts of hijacking.
- These options are not mutually exclusive. They may design evolutionary steps towards the multi-currency system: with the first playing the “transitional paradigm” towards the “new end state” of more stable and diversified currencies.

THANK YOU!