



# THE STATUSES OF DE-DOLLARIZATION IN THE INDIAN ECONOMY

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## **Abstract:**

Diversification away from the US dollar is intended to protect economies from geopolitical risks. Much has been written about how the weaponization of trade, the imposition of sanctions, and the US's exclusion from SWIFT could accelerate de-dollarization because countries with diplomatic and economic autonomy will be wary of using US-dominated global banking systems. This school of thought contends that this will also cause a shift in the overall global forex market framework, as potential foreign policy coercion or sudden disruptions will not sit well with countries, prompting them to investigate how to build bulwarks. The US dollar, the world's reserve currency, may continue to fall in value in the current environment as leading central banks seek to diversify their reserves away from it and into other assets or currencies such as the Euro, Renminbi, or gold. The concept of de-dollarization fits well in the thought experiment of a multipolar world in which each country seeks economic autonomy in the realm of monetary policy. The main objective of the study is to understand and examine the opportunity and challenges of de-dollarization on the Indian economy.

Keyword: de-dollarization, impact, challenges,

## **1. INTRODUCTION:**

The Reserve Bank of India (RBI), the country's central bank was announced an arrangement to allow trade settlements between India and other countries in rupees, the move is intended to promote global trade growth, with a focus on Indian exports, as well as to support the growing global trading community's interest in the Indian rupee. In terms of traditional international trade settlement, observers believe the arrangement is intended to facilitate trade with Russia and countries facing Western sanctions. Nonetheless, the timing is opportune for India to implement rupee-based trade settlement, which coincides with emerging markets' call for de-dollarization. At the moment, the West's restrictions and disruptions to global supply chains as a result of its abuse of dollar hegemony are putting pressure on the world economy to reconsider the role of the dollar in the international trade system and seek new alternatives to restore normal trade exchanges.

The introduction of rupee payments from India could be a further step toward de-dollarization. Because India is not the only Asian economy experiencing or anticipating difficulties in settling trade with other countries, its solution this time may even help boost the rupee's status in the regional trade network. While the use of rupees in foreign trade may help reduce the pressure on foreign exchange reserves, with the rupee approaching a new historical low of 80 against the US dollar on Tuesday, the weakening currency may cause uncertainty in the actual operation of the rupee payment. If the rupee's stability against other major currencies cannot be guaranteed, countries that accept rupee settlement will be subject to greater exchange rate risk, potentially resulting in massive losses if the rupee's value falls. In this regard, India's rupee settlement system still has a lot of work to do if it wants to gain more acceptances in the global trade system, such as maintaining the rupee's general stability and strengthening settlement pilots with neighboring economies. On the other hand, India's adoption of rupee settlement means that competition among global settlement currencies will heat up in the future. With the international food and energy crises worsening, an increasing number of countries are forced to use the ruble to purchase food, energy, or fertiliser from Russia. Furthermore, due to the Yuan's consistent performance, countries such as Saudi Arabia are reportedly considering accepting the Yuan as payment for oil sales to China. Global miners are also reportedly enthusiastic about selling iron ore to China in Yuan. With more currencies likely to join the trade settlement circle, whether within the BRICS or G20 frameworks, it is time to think about how to create a new mechanism for countries that require an alternative trade settlement system to strengthen cooperation.

## 2. OBJECTIVES:

- To understand the de-dollarization in world scenario.
- To examine the opportunity and challenges of de-dollarization in Indian.

## 3. METHODOLOGY

The study is based on the secondary data was collected from various published and unpublished data such as newspapers magazines books and reports of the RBI etc.

## 4. CONCEPT OF DE-DOLLARIZATION

De-dollarization refers to reducing the dollar's dominance of global markets. It is the process of replacing the US dollar as the trading currency for oil and/or other commodities. Buying US dollars for the forex reserves, bilateral trade agreements, and dollar-denominated assets. The dominant role of the dollar in the global economy provides the US with a disproportionate amount of influence over other economies. The US has for long used the imposition of sanctions as a tool to achieve foreign policy goals. The de-dollarization is driven by the desire to insulate the central banks of the countries from geopolitical risks, where the status of the US dollar as a reserve currency can be used as an offensive weapon.

In the early 1970s, the US dollar solidified its position with an agreement with the oil-rich Kingdom of Saudi Arabia to conduct global energy trade in dollars. The status of the dollar was **enhanced by the collapse of the Bretton Woods system**; it essentially eliminated other developed market currencies from competing with the USD. Currently, about 60% of the foreign exchange reserves of central banks and about **70% of global trade are conducted using the USD**. The psychological angle to considering the USD as a "safe-haven" asset is that people continue to view the currency as a relatively risk-free asset. Furthermore, sudden dumping of dollar assets by adversarial central banks will put their balance sheets at risk by eroding the value of their overall dollar-denominated holdings. Apart from the Euro and gold, most other foreign currencies have some inherent risks associated with them. For instance, with historically "neutral" Switzerland joining the EU in imposing sanctions on Russia, it eliminates the Swiss franc as an asset that can work as a hedge against economic sanctions.

## 5. MOMENTS OF DE-DOLLARIZATION

During the early 1990s, the ratio of foreign currency deposits to total deposits fell by more than 15 percentage points in Vietnam, Russia, and Chile. The trend, however, was reversed for a few years, and the ratio of dollar deposits has only recently begun to fall again, particularly in Russia and Vietnam. Whereas in the early 1980s, dollar deposits accounted for more than half of total deposits in Israel, deposit dollarization in 2004 reached only 15%, and Ecuador was not very dollarized in the first half of the 1990s. (Levy Yeyati 2006).

The sanctions imposed by the West on Russia in February 2022 effectively cut Russia off from the dollar economy. As a result, a market that does not use dollars has emerged. The BRICS countries have been debating various options for developing a new international currency. It remains to be seen what China will do. The PBoC owns more than \$1 trillion in US Treasury debt, and it is unlikely that the Chinese would be willing to lose that much money in order to dethrone the US dollar. A gradual divestment that does not disrupt markets is much more likely. Saudi Arabia is another major player in international financial markets. Relations between the Kingdom and the US appear to have deteriorated to some extent, with Russian officials maintaining close contact with Saudi authorities. The petrodollar system is well known to be heavily reliant on the Saudis' insistence on receiving payment in dollars, as do many other major oil producers. Geopolitical considerations play an important role in how financial equilibrium functions in this case. If the Chinese and Russians are successful in weaning Saudi Arabia away from the US, the forex markets may undergo significant changes as there will be much less demand for US dollars. The truth is that de-dollarization has appealed to more than just Russia. Brazil, China, India, Iran, Libya, North Korea, South Africa, Syria, and Venezuela all want to de-dollarize their currencies, albeit for different reasons. Taking the argument to a higher level allows for the consideration that the Ukraine conflict has accelerated the movement away from the USD and paved the way for the development of an alternative or alternatives to the American currency and the process of establishing a bipolar financial world in which the USD area is confronted with another exchange system in the East and South. Australia, Canada, the European Union, Israel, and New Zealand form a separate bloc from the rest of the world, along with the United States.

Leading geopolitical adversaries of the US—Russia and China—have already started this process of de-dollarisation. Efforts are underway for the possible introduction of a new Russia-China payment system, bypassing SWIFT and combining the Russian SPFS (System for Transfer of Financial Messages) with the Chinese CIPS (Cross-Border Interbank Payment System). The **ongoing war in Ukraine** and the subsequent economic sanctions will trigger central banks to go back to their drawing boards to reassess their dependency on the dollar. Russia had started its three-pronged efforts towards de-dollarization in 2014, **when sanctions were imposed on it for the annexation of Crimea**. Russia **reduced its share of dollar-denominated assets to about 16%** in 2021. It also **reduced its share of trade conducted in USD** by prioritising national currencies in bilateral trade. The use of USD in Russia's exports to the **BRICS** crashed from about 95% in 2013 to less than 10% in 2020. China aims to use trading platforms and its digital currency to promote dedollarization. It has established RMB trading centres in Hong Kong, Singapore, and Europe. In 2021, the People's Bank of China submitted a "Global Sovereign Digital Currency Governance" proposal to the Bank for International Settlements to influence global financial rules via its digital currency, the e-Yuan. The **International Monetary Fund (IMF)** has already added Yuan to its **SDR (Special Drawing Rights)** basket in 2016. However, the **lack of full RMB convertibility will hinder China's de-dollarization ambition**.

## 6. DE-DOLLARIZATION AS A SCENARIO IN INDIA

Previously, India had to work out alternative arrangements, such as a barter agreement, with certain sanctioned countries. Recently, it has been reported that India and Russia are considering using the Chinese yuan as a reference currency to improve bilateral oil trade. In the exchange markets, the Indian rupee, like the Chinese renminbi, is not yet fully convertible. Non-convertible currency makes international trade more difficult because transactions take longer to complete. Non-convertibility implies difficult capital access, lower financial market liquidity, and fewer business opportunities. India, like China and Russia, may have a digital currency in the near future, and some signs of this are already visible. India can also strive for a higher proportion of euros and gold in its foreign exchange reserves. India has several options for starting the de-dollarization process. Trading in national or digital currencies with Iran, EAEU, BRICS, and SCO members will become a reality in the near future, beginning with Russia-India transactions. The dollar's value will inevitably fall as major economic powers such as China and India rise. Asia's rise as an economic powerhouse will boost the value of currencies like the Yuan and the Indian rupee. The frequent use of the US dollar as a potential weapon for achieving foreign policy goals would undoubtedly hasten the de-dollarization process. Furthermore, currency convertibility is an important aspect of global commerce because it allows a government to pay for goods and services.

## 7. IMPACT OF DE-DOLLARIZATION

**Reduce trade volatility and risk:** The "de-dollarization" of several central banks is imminent, driven by the desire to insulate them from geopolitical risks, where the status of the US dollar as a reserve currency can be used as an offensive weapon. **As an alternative to economic sanctions,** asduce demand for the USD, ressanctions. a relative depreciation of the currency and imported inflation in the United States. **Push for globalisation Reduce the spillover effect of an economic crisis in one country on the global economy.**

## 8. CHALLENGES OF DE-DOLLARIZATION

Finding alternatives to the dollar with the right amount of availability, acceptability, and stability given the psychological bias, the world will continue to prefer the USD as a "store of value" and a "medium of exchange," fulfilling the basic functions of money. A sudden dumping of dollar assets by adversarial central banks will also put their balance sheets at risk by eroding the value of their overall dollar-denominated holdings. No complete proof of sanctions—increasing reliance on the euro and thus greater vulnerability to EU sanctions; Finding the true exchange rate—the US dollar serves as the link currency for calculating the value of any two currencies. a new international payments system that could operate as an alternative to the US-dominated SWIFT, as international trade needs a payment and financial system to take place. Due to the dollar's continued primacy as the medium of exchange in international currency markets, selling euros in exchange for rubles is likely to be difficult without going through the dollar, as Iran learned a few years ago. Increase economic autonomy

## 9. DE-DOLLARIZATION AND INDIA

India is currently among the most dollarized countries (in invoicing) and hence relatively difficult to switch to other modes given the economic and political relationship with the USA. However, while others accumulate dollars from trade surplus earnings, India maintains a large forex reserve despite importing less than it exports. In India's case, the dollar reserves come through infusions of foreign direct investment (FDI) and foreign portfolio investment (FPI), which reflect the confidence of foreign investors in India's growth prospects. Thus, India is less impacted by economic sanctions imposed by the USA. Just like the Chinese renminbi, the Indian rupee is also not yet fully convertible at the exchange markets. While this means that India can control its burden of foreign debt and the inflow of capital for investment purposes in its economy, India remains vulnerable to policy changes by other nations' monetary policies that are beyond India's own control. For instance, it has been often highlighted that a tightening of US monetary policy leads to capital outflows (capital flight) from India, thus impacting India adversely.

**Alternatives:** Rather than shifting dependence from the USD to another currency such as the euro or yuan, backing currency with "old gold" will not solve the problem but will re-enact the pre-Bretton Woods crisis. Agreements on currency swaps A central bank digital currency (CBDC) that does not use the US dollar. China proposed to the Bank for International Settlements a "Global Sovereign Digital Currency Governance" proposal in order to influence global financial rules through its digital currency, the e-Yuan. a global currency or a system similar to the IMF's SDR. introduction of a new Russia-China payment system that bypasses SWIFT in favour of combining the Russian SPFS (System for Transfer of Financial Messages) and the Chinese CIPS (Cross-Border Interbank Payment System). National electronic payment systems, such as Russia's MIR or India's UPI.

## 10. CONCLUSION

The US dollar is still the preferred currency for trade because no other currency is liquid enough. Even if a currency did exist, nations would be concerned about it becoming a mirror image of the US dollar. A mere change in regime along with having to bear the same manipulations, albeit from a different country, is not what the world wants. The only way forward would be to **diversify the currency market so that no one currency claimed hegemony**. Analyzing the experiences of nations that have lowered their dollarization levels seems intriguing. Their tactics can be divided into two categories: A more hands-off approach based on strong macroeconomic performance and the stability (or appreciation) of the local currency is preferable to a more hands-on approach based on administrative efforts to discourage dollarization. Overall, the issue of dollarization is complex enough that it is unlikely that universally applicable regulations can provide a solution. On the one hand, it is possible to claim that macroeconomic solutions are required because it is obvious that dollarization has macroeconomic roots. The so-called "hysteresis" surrounding the dollarization process, on the other hand, suggests that government participation is a key tool.

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