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Introduction to the Agenda

- The adoption of national currencies in global trade has long been a central issue in international economics. In an increasingly interconnected world, trade serves as a critical driver of economic growth, and currency policies significantly influence the balance of global trade. Historically, dominant currencies like the U.S. dollar and the Euro have facilitated much of international trade due to their stability and wide acceptance. However, the reliance on a few currencies creates both opportunities and challenges for countries involved.

- For nations, maintaining trade in their own national currencies can provide greater economic autonomy and reduce dependence on external exchange rate fluctuations. Recently, countries like China and Russia have pursued efforts to promote the use of their own currencies, such as the yuan and ruble, in international transactions, highlighting the potential shift in global trade dynamics. Yet, widespread adoption of national currencies in global trade poses hurdles, including currency volatility, lack of liquidity, and the complexity of creating mutual trust between trading partners.

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- This agenda aims to explore the viability, benefits, and risks of integrating more national currencies into global trade systems, and to assess the potential impact of these policies on economic stability and international relations.

Background and History

1. The Gold Standard

- The Federal Reserve Act of 1913 created the Federal Reserve Bank to respond to the unreliability and instability of a currency system that was previously based on banknotes issued by individual banks. The U.S. economy surpassed that of the United Kingdom, though world commerce still centered around the U.K., with transactions taking place in British pounds.

- The majority of developed countries pegged their currencies to gold as a way to stabilize currency exchanges. When World War I broke out in 1914, many countries suspended the gold standard to pay their military expenses with paper money, which devalued their currencies. Britain held to the gold standard to maintain its position as the world's leading currency and found itself borrowing money for the first time during the third year of the war.

- The United States became the lender of choice for many countries that wanted to buy dollar-denominated U.S. bonds. Britain abandoned the gold standard in 1931, which decimated the bank accounts of international merchants who traded in pounds. The dollar replaced the pound as the leading reserve currency.

2. The Bretton Woods Agreement

- Most countries paid in gold, making the U.S. the owner of a majority of gold by the end of the war. A return to the gold standard became impossible as countries depleted their reserves.

- Delegates from 44 Allied countries met in Bretton Wood, New Hampshire, in 1944 to develop a system to manage foreign exchange that would not disadvantage any country. The delegation decided that the world's currencies would no longer be linked to gold but pegged to the U.S. dollar. Known as the Bretton Woods Agreement, it established the authority of central banks, which would maintain fixed exchange rates between currencies and the dollar. In turn, the United States would redeem U.S. dollars for gold on demand.

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Countries had some degree of control over currencies in situations where the values of their currencies became too weak or too strong relative to the dollar. They could buy or sell their currency to regulate the money supply.

3. The World's Reserve Currency

- The U.S. dollar was officially crowned the world's reserve currency and backed by the world's largest gold reserves thanks to the Bretton Woods Agreement. Instead of gold reserves, other countries accumulated reserves of U.S. dollars. Needing a place to store their dollars, countries began buying U.S. Treasury securities, which they considered to be a safe store of money.

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Past International Actions

1. European Monetary System

- The European Monetary System (EMS) was an adjustable exchange rate arrangement set up in 1979 to foster closer monetary policy cooperation between members of the European Community (EC). The European Monetary System (EMS) was later succeeded by the European Economic and Monetary Union (EMU), which established a common currency, the euro.

  - The European Monetary System (EMS) was established to stabilize inflation and stop large exchange rate fluctuations between these neighbouring nations, with the intended goal of making it easy for them to trade goods with each other.

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  - The EMS was established through the introduction of the European Currency Unit in 1979. The ECU served as a basket currency, representing a weighted average of member currencies.

- The EMS was created in response to the collapse of the Bretton Woods Agreement. Formed in the aftermath of World War II (WWII), the Bretton Woods Agreement established an adjustable fixed foreign exchange rate to stabilize economies and consolidate global financial power among the Western Allied nations. When it was abandoned in the early 1970s, currencies began to float—fluctuating in market value relative to one another—which prompted members of the EC to seek out a new exchange rate agreement to complement their customs union.

- The EMS's primary objective was to stabilize inflation and stop large exchange rate fluctuations between European countries. This was part of a wider, overall goal of fostering economic and political unity in Europe, which ultimately paved the way for a common currency, the euro. Currency fluctuations were controlled through an exchange rate mechanism (ERM). The ERM was responsible for pegging national exchange rates, allowing only slight deviations from the European currency unit (ECU)—a composite artificial currency based on a basket of 12 EU member currencies, weighted according to each country's share of EU output. The ECU served as a reference currency for exchange rate policy and determined exchange rates among the participating countries' currencies via officially sanctioned accounting methods.

- Criticism of the EMS: Under the EMS, exchange rates could only be changed if both member countries and the European Commission were in agreement. This was an unprecedented move that attracted a lot of criticism.

1. De-Dollarization Efforts

- The U.S. dollar is the world's primary reserve currency, and it is also the most widely used currency for trade and other international transactions. However, its hegemony is in question, especially in light of the ongoing Russia-Ukraine crisis. "The risk of de-dollarization, which is a periodically recurrent theme throughout post-war history, has returned into focus due to geopolitical and geostrategic shifts. the U.S. sanctions on Russia have made some countries wary about being too dependent on the greenback. In addition, against a backdrop of rising interest rates, a strong U.S. dollar is becoming more expensive for emerging nations, leading some to trade in other currencies.

- The reserve status of the dollar is declining more rapidly than commonly acknowledged, with numerous analysts overlooking the significant exchange rate fluctuations from the previous year. The global share of the greenback in reserves decreased last year at a rate ten times faster than the average speed observed over the past twenty years, as several nations sought alternative options following the sanctions imposed due to Russia's invasion of Ukraine. Accounting for exchange rate adjustments, the dollar has experienced an approximate 11% decrease in market share since 2016, doubling that figure since 2008.

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Background Guide

Bilateral trade agreements

- **India-Russia:** Before 1991, Soviet Union and India traded in rupee-ruble exchange during Cold War. Mutual trading between India and Russia is done mostly in rubles and rupees instead of dollars and euros. In March 2022, India and Russia entered for a Rupee–RubleTrade Arrangement. India is buying Russian oil in U.A.E. dirham and also in roubles.

- **Pakistan:** The power minister of Pakistan announced that the country is considering using yuan to pay for its imports of Russian crude oil.

- **Australia/Russia/Japan/Brazil/Iran:** It made agreements with Australia, Russia, Japan, Brazil, and Iran to trade in national currencies. It has been reported that in the first quarter of 2020 the share of the dollar in the bilateral trade between China and Russia fell below 50 percent for the first time. In 2011, Japan made an agreement with China to trade in national currencies. Sino-Japanese trade had a value of US$300 billion.

- **France-China:** In a significant development, it has been reported that a French company has conducted a transaction with China National Offshore Oil Corporation recently, exporting liquefied gas (LNG) and accepting payment in Chinese yuan. The mentioned transaction highlights the growing trend of de-dollarization, which is also making its way into the European Union

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Analysing the Issue

- Global economic ties are undergoing a significant transformation, reminiscent of the post-Cold War era. Recent shocks, such as the COVID-19 pandemic and Russia's invasion of Ukraine, have prompted countries to revaluate their trading partners and economic dependencies. Foreign direct investment flows are increasingly influenced by geopolitical considerations, and nations are exploring alternatives to the U.S. dollar in international transactions and reserve holdings.

- While this shift toward economic resilience is understandable given recent events, it could lead to a retreat from global cooperation and a reversal of the gains achieved through globalization. The COVID-19 pandemic and Ukraine conflict have highlighted the risks of overreliance on specific trading partners and currencies.

Challenges of Adopting a National Currency

- **Initial Costs**

1. **Implementation Expenses:** Adopting a national currency requires substantial investments in printing new banknotes, updating accounting systems, modifying price tags, and conducting public awareness campaigns.

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2. **Institutional Development:** Establishing a central bank, financial regulations, and monetary policy frameworks can be expensive and time-consuming.

- **Economic Volatility**

1. Exchange Rate Fluctuantions:
A newly introduced national currency may experience significant fluctuations in its exchange rate, impacting trade and investment.

2. Inflationary Risks: Ineffective management of the national currency can lead to inflation, particularly if the central bank lacks experience or credibility.

Case Studies

- **The Chinese Renminbi Joins the SDR Basket: A Milestone in Global Economic Integration**

- The International Monetary Fund (IMF) has added the Chinese renminbi (RMB) to the basket of currencies that comprise the Special Drawing Right (SDR), an international reserve asset created to supplement member countries' official reserves. This significant milestone marks a major step towards the integration of the Chinese economy into the global financial system.

- The decision to include the RMB in the SDR basket reflects China's growing role in global trade and the increasing international use of the renminbi. It also acknowledges the progress made in reforming China's monetary, foreign exchange, and financial systems, as well as the advancements in liberalizing and integrating its financial markets. The inclusion of the RMB is expected to further support the international use and trading of the renminbi.

- While data disclosure is not a formal requirement for inclusion in the SDR basket, the IMF generally expects issuers of reserve currencies to meet high transparency standards. China has taken positive steps to increase data disclosure and participate in multilateral data initiatives, such as reporting the currency composition of its reserves to the IMF and collaborating with the Bank for International Settlements on reporting Chinese banking sector statistics. These efforts will enhance the acceptance of the RMB among official holders of foreign exchange reserves.

- The inclusion of the RMB in the SDR basket consolidates its internationalization process. This process demands a strong and transparent financial system, including deep and liquid financial markets, a certain degree of capital account openness, predictable macroeconomic outcomes, credible institutions, and a reliable rule of law. By strengthening the RMB's internationalization, China can contribute to the global economy's stability and resilience.

- Furthermore, the inclusion of the RMB in the SDR basket enhances its attractiveness as an international reserve asset, promoting the diversification of global reserve holdings. This can help mitigate risks associated with over-reliance on a single currency and contribute to a more balanced global financial system.

Ecuador's Dollarization

- In 2000, Ecuador made a significant economic decision by adopting the U.S. dollar as its national currency, abandoning its own currency, the sucre. This move was primarily driven by the sucre's rampant hyperinflation, which had destabilized the economy and eroded living standards. Additionally, Ecuador sought to integrate more deeply into the global economy, particularly with the United States, its main trading partner.

- Dollarization offered several benefits, including reduced transaction costs, increased price stability, and greater attractiveness to foreign investors. By adopting the dollar, Ecuador eliminated exchange rate risks and facilitated trade with the United States. Moreover, the stable U.S. dollar helped curb inflation and boost investor confidence. However, dollarization also came with certain drawbacks. Ecuador relinquished its monetary policy autonomy, meaning it could no longer set interest rates or control its money supply. This made the country more vulnerable to external economic shocks, particularly those originating from the United States. Furthermore, Ecuador's economic sovereignty was diminished, as it was less able to address domestic economic problems using monetary policy.

- In conclusion, Ecuador's experience with dollarization provides valuable lessons about the potential benefits and drawbacks of adopting a foreign currency. While it achieved significant economic stability, it also sacrificed some degree of economic sovereignty and became more vulnerable to external economic shocks.

The U.S. Dollar's Global Influence

- The U.S. dollar's pervasive influence on the global economy is undeniable. As the world's reserve currency, it plays a central role in international trade, finance, and investment. Its exchange rate fluctuations can have far-reaching consequences for countries around the globe.
- When the U.S. dollar strengthens, it generally leads to lower export prices for U.S. goods and higher import prices for other countries. This can impact trade balances, as countries may find it more difficult to export their goods and services competitively. Additionally, a stronger dollar can contribute to inflationary pressures in countries that are heavily reliant on imports.
- Conversely, a weaker U.S. dollar can make exports from other countries more competitive, boosting their trade balances. However, it can also lead to higher import prices for countries that rely on imported goods and services, potentially fueling inflation.
- Beyond its impact on trade, the U.S. dollar's dominance also shapes the global financial landscape. Many international transactions, including trade, investment, and debt financing, are denominated in U.S. dollars. This can make countries that are heavily reliant on the dollar more vulnerable to economic shocks originating from the United States.

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Questions a resolutions should address in respect to the agenda

A resolution on the "Adoption of National Currencies in Global Trade" should address several critical questions to ensure a comprehensive and effective approach to the issue. These questions guide the debate toward feasible solutions, acknowledging both the potential benefits and the challenges of using national currencies in international trade. Here are the key questions a resolution must answer:

- - What criteria should be used to determine the suitability of a national currency for global trade
  - Should factors like economic stability, inflation rates, and liquidity be considered when promoting the use of a currency in global markets?

- - How can countries promote bilateral or multilateral trade using national currencies?
  - What agreements or frameworks should be established to ensure trust and cooperation between countries using their national currencies for trade?

- - What role should international financial institutions, such as the IMF and World Bank, play in facilitating the transition to national currencies in trade?
  - Should these institutions provide technical assistance, risk management, or financial incentives to encourage national currency adoption?

- - How can countries mitigate the risks associated with currency volatility and instability?
  - What measures (e.g., currency swap agreements, foreign exchange reserves, hedging strategies) can be adopted to protect countries from the negative impacts of fluctuating exchange rates?

- - How should international trade agreements and contracts be structured to support the use of national currencies?
  - What legal frameworks or trade mechanisms need to be adjusted to accommodate trade in national currencies?

- - What impact will the adoption of national currencies have on smaller or developing economies?
  - How can the interests of less stable economies be protected to ensure they are not disproportionately affected by changes in global currency policies?

- - How can countries overcome the infrastructural and technological barriers to supporting the use of multiple currencies in global trade?
  - Should the international payment system (e.g., SWIFT) be adapted to accommodate diverse national currencies, and how can this be achieved?

Answering these questions will provide a strong foundation for a resolution that balances the needs of economic sovereignty with the requirements of a stable, secure, and efficient global trade system.

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Links for Research

- https://www.imf.org/en/Research
- https://www.investopedia.com
- https://www.supermoney.com/encyclopedia/national-currency
- https://www.cfr.org
- https://www.brookings.edu
- https://tradecouncil.org/the-evolution-of-global-trade-policies-and-their-economic-impact

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