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The Role of Gold in Currency Markets

Towards a Return to the Fixed RateRegime After Five Decades

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. The role of gold in the world economy in general and currency markets in particular is significant. This paper is divided into four parts. Part I deals with the gold standard and associated theories.   Part II deals with the gold exchange system, also known as the Breton Woods system, and its collapse in 1971. Part III deals with evolution of the euro in the nineteen nineties and its steady decline on the one hand and the possible impact of Brexit on the pound sterling in the recent years. Part IV examines the need for dispensing with the the out-dated Special Drawing Rights in its present composition and recommends its replacement by the US dollar. In the process it lays down a road map to move towards a possible return to the gold exchange standard or the fixed

exchange system with the adjustable peg in the medium term.

Part I

Gold Standard

Down the ages, gold standard has been one of the most significant exchange rate systems across the world. It signifies a system under which a nation (1) declares its currency unit to be equivalent to some fixed weight of gold, (2) holds gold reserves and will buy or sell gold freely at the price so proclaimed, and (3) puts no restrictions on the export or import of gold.[1] The benefit of a gold standard is that money is backed by a fixed asset and provides a 'self-regulating and stabilizing effect on the economy.' The governments can only print as much money as its currency holds gold. This discourages not only inflation, which is too much money chasing too few goods but government budget deficits, trade deficits and government debt, which cannot exceed the supply of gold. Further, more productive nations are directly rewarded: more they export, more they could accumulate gold.[2]

1914-1923

The price of gold has remained remarkably stable during long periods of time. Sir Isaac Newton, the famous physicist, in his capacity as the Master of the UK Mint, fixed the price of gold roughly equivalent to $20 per troy ounce of gold in 1717 and it remained at this level for the 200 years until 1914. The only exception was during the Napoleonic wars from1797 to 1821.

The official US gold price has changed only four times from1792 to the present. Starting at $19, 75 per troy ounce, raised to $20.67 in 1834, and $35 in 1934 in 1972, the price was raised to $38 and then to $42.22 in1973. A two-tiered pricing system was created in 1968, and the market price for gold has been free to fluctuate since then as shown in Tables I and II. Table I gives the gold prices from 1833 to 2011. Table II gives details of gold prices from 2012 to 2019. A careful appreciation of gold prices from 1833 to 1971 on the one hand and the behavior of gold prices in the post 1971 era constitute the quintessence of the proposal advocated in this paper, namely abolish the out-dated relic called the Special Drawing Rights(SDR) at the International Monetary Fund . And return to the fixed exchange rate or the Breton Woods system where the value of a currency is determined by the price of gold and the dollar only.

Before World War I, the four largest economies---the United States, Britain, Germany, and France—had operated their monetary system with about $5 billion worth of gold among them four major economic powers, far in excess of what was necessary to sustain its economy. The amount of new gold mined during the war was small; by 1923, monetary gold had increased only to $6 billion. Even after the post-war deflation, prices in the United States and the U.K., were still 50 percent higher than before the war, which meant that in effect the real purchasing power of gold reserves had contracted by almost 25 percent.[5] 1923, the United States had accumulated close to $4.5 billion of the $6 billion in gold.

The gold standard had served as a source of inspiration for exploration of gold: discovery of the New World in 1500s by Spain and European countries in search of gold and the Gold Rush in California and Alaska in the 1800s. While the size and health of a country's economy is assessed with reference to its supply of gold and it works to the advantage of the U.S. which happens to be the world's second largest gold mining country after South Africa. Most gold mining in the US occurs on federally owned lands in twelve western states, with Nevada being the primary source. Australia and Canada and several developing countries are also major gold producing countries.

Since the real value of monetary gold (that is the quantity of real commodities that the gold will buy) is unchanged, according to Hume, losing half or nine-tenths of a nation's gold is of no concern if the nation ends up with a balanced reduction of all prices and costs. Since the real value of monetary gold (that is the quantity of real commodities that the gold will buy) is unchanged, according to Hume, losing half or nine-tenths of a nation's gold is of no concern if the nation ends up with a balanced reduction of all prices and costs. Since the real value of monetary gold (that is the quantity of real commodities that the gold will buy) is unchanged, according to Hume, losing half or nine-tenths of a nation's gold is of no concern if the nation ends up with a balanced reduction of all prices and costs. Since the real value of monetary gold (that is the quantity of real commodities that the gold will buy) is unchanged, according to Hume, losing half or nine-tenths of a nation's gold is of no concern if the nation ends up with a balanced reduction of all prices and costs. Since the real value of monetary gold (that is the quantity of real commodities that the gold will buy) is unchanged, according to Hume, losing half or nine-tenths of a nation's gold is of no concern if the nation ends up with a balanced reduction of all prices and costs. During the period 1880-1913, countries used to define their respective currencies in terms of a fixed quantity of gold, which paved the way for establishing the fixed exchange rate system among the countries following the gold standard.

According to mercantilists, the government should try to stop the alleged drain of gold by placing tariffs and quotas on imports, subsidize exports, and introducing several other interferences. Although this theory was attacked by none other than Adam Smith, the theory provoked probably the most vehement criticism from David Hume, one of the earliest proponents of the quantity theory of prices. Hume firmly held that all countries could not be simultaneously losing gold. According to Hume’s quantity theory of prices, the overall price level in an economy is directly proportional to the supply of money. Under the gold standard, gold formed an important part of the money supply- either directly, to the form of gold coins, or indirectly when governments used gold as backing for

The result of Hume's four-pronged gold-flow mechanism was to improve the balance of payments of the country losing gold and to worsen that of the country gaining the gold. In the end, equilibrium of international trade and finance would be reestablished at new relative prices, which keep trade and international lending in balance with no net gold flow. This equilibrium was a stable one and required no tariffs or other governmentintervention.[4]

During the period 1880-1913, countries used to define their respective currencies in terms of a fixed quantity of gold, which paved the way for establishing the fixed exchange rate system among the countries following the gold standard. By fixing the price of a commodity in ounces of gold, gold was accepted as the common world currency dispensing with the foreign exchange rate problem. Once in the gold standard, countries resorted to the practice of issuing gold coins incorporating the emblem of the state to guarantee their purity and weight. The issuance of gold coins also helped doing away with the distinction between domestic trade and foreign trade since everything could be paid for in gold.

The Gold Exchange or the Breton Woods System

The International Monetary Fund (IMF) was John Maynard Keynes's prescription to establish a permanent institution that could exercise constant surveillance over the exchange rate system of the member countries to avoid the phenomenon of competitive devaluation in the future. The IMF, however, could be formally established only in 1944 after the end of the Second World WarwThe United States, Britain, and their major allies gathered in Bretton Woods, New Hampshireunder the leadership of Keynes and H.D. White. The conference, besides agreeing to establish the International Monetary Fund and the World Bank, designed a framework for managing exchange rates known as the Breton Woods system. Keynes might have once called gold a "barbarous relic "as he believed it was bound to go back to the soil. The fact, however, remains that gold did stage a comeback even during Keynes's own time. As it was felt that the gold standard was too inflexible and served to deepen economic crises, the

Breton Woods system established parity for each currency in terms of both the U.S. dollar and gold. While the parity of the dollar was pegged only in terms of gold, initially at $35 per ounce of gold, other currencies were defined in terms of both gold and the dollar. For example, the parity of the British pound was set at 12.5 pounds per ounce of gold; this implied an official exchange rate between the dollar and the pound of $35/12.5=$2.80 per one pound. When one currency got too far out of line with the appropriate or "fundamental" value, the parity could be adjusted. The German mark was adjusted upward or downward on several occasions, while the British pound was devalued from $2.80 per one pound to $2.40 per one pound in 1967.

Great Depression

The stock market crash in black October of 1929 coupled with the competitive devaluation indulged in by Great Britain and France led to the Great Depression of the nineteen thirties resulting in worldwide unemployment. In December 1930, Maynard Keynes, in the article, *The Great Slump of 1930,* described the world as living in "the shadow of one of the greatest economic catastrophes of modern history": during the previous year, industrial production had fallen to 30 percent in the United States, 25 percent in Germany, and 20 percent in Britain. Over 5 million in the U.S, 4.5 million in Germany, 2 million in Britain were jobless. Prices of coffee, cotton, rubber, and wheat had fallen by more than 50 percent after the stock market crash in October 1929. Three of the largest primary producing countries, Argentina, Australia and Brazil had abandoned the gold standard and let their currencies devalue. Keynes recognized that to revive the economy, a central bank should have enough stock of gold, which was the basis for extending credit under the gold standard. Owing to investor confidence, capital was flowing out of countries like Britain and Germany with modest gold reserves into countries with large gold reserves like the U.S. and France. The year 1930 witnessed shipment of gold totaling to $300 million across the Atlantic into the U.S. Federal Reserve system.

Liquat Ahmed, in his Lords *of Finance: the Bankers who Broke the World* (2009) drew attention to the flow of gold into France, the only country in Europe that had remained immune to the world economic storm.[5] The decision of EmieMroreau, Governor of Banque de France, to keep the franc pegged at a low rate had made the prices of French goods attractive. During 1929 and 1930, a total of $500 million of gold had flown into France. By the end of 1930, the Banque de France had accumulated a gold reserve of over $2 bullion, three times that of the Bank of England. As a result, unlike other countries like Britain and Germany, money was easily available in France and people continued with consumer spending while business

Au Printemps, the well known department store at Paris was booming. The number of persons collecting unemployment benefits in France was only 1, 90,000 compared to 4.5 million in Germany and million in Brirtain.[6]

As an answer to solving the ill effects of the Great Depression on the U.S. economy, George Warren, a relatively unknown Professor of farm management at Cornell University, had argued that if commodity prices fell owing to shortage of gold, one way to raise them was to raise the price of gold, which meant that the dollar needed to be devalued. The notion of devaluation provoked sharp opposition from Roosevelt's Economic Advisors who felt that this would not be the right action considering the vast gold reserves of the U.S. Roosevelt, however, went ahead and decided to take the dollar off gold standard.

Samuelson sums up the advantages of the Breton Woods system in the following paragraphs:

The Breton Woods system was a fixed but adjustable exchange rate system. By creating a fixed but adjustable system, the designers of Bretton Woods hoped to have the better of two worlds. They could maintain the stability of the gold standard, a world in which exchange rates would be predictable from one month to the next, thereby encouraging trade and capital flows. At the same time, they would simulate the adaptability of flexible exchange rates, under which persistent relative price differences among countries could be adjusted to by exchange rate changes rather than by the painful deflation and unemployment necessary under the gold standard.

During the period from1944 to 1971, the world was on a dollar-gold standard. With the U.S. dollar as the key currency, most international trade and finance were carried out in dollars and payments were generally made in dollars. Exchange-rate parities were set in terms of dollars and private and government reserves were kept in dollar balances:

The world economy thrived during this period. The industrial nations began to lower trade barriers and to make all their currencies freely convertible. The economies of Western Europe and East Asia recovered from war damage and grew at spectacular rates. But recovery contained the seeds of its destruction. Dollars began to pile up abroad as Germany and Japan developed trade surpluses. Meanwhile, U.S. deficits were fuelled by an overvalued currency, trade deficits, and growing overseas investment by American firms. Dollar holdings abroad grew from next to nothing in 1945 to $50 billion in the early 1970s.

By 1971, the amount of liquid dollar balances had become so large that governments had difficulty defending the official parities. People began to lose confidence in the 'almighty dollar.' And the lower barriers to capital flows meant that billions of dollars could cross the Atlantic in minutes.

The system worked quite well through the fifties and the early part of sixties until the Vietnam War took a toll on the US economy. By the late sixties, the foreign central banks started losing confidence in the dollar and preferred gold instead, which led to a serious erosion of US gold reserves. In 1971, President Nixon, besides ending the Vietnam War, also broke the Bretton Woods agreement, refusing to exchange any more gold for the dollar [7]

To maintain the superiority of the dollar, however, the U.S., as the founder of NATO, started using its military power, to provide free world-wide security demanding its allies to continue to accept dollars for all their international transactions. Further as the largest shareholder of the IMF and the World Bank, the US had the final say in their policy prescriptions for countries in need of assistance. If the Latin American countries and the African nations wanted money from the IMF, they were required to devalue their respective currencies in relation to the dollar and privatize industries mainly to repay their dollar debts, that too to private US banks. Above all, the U.S. was able to ensure that the OPEC countries, particularly Saudi Arabia, to price oil in dollar terms. In exchange the U.S. would provide free security to Saudi Arabia against any external aggression. Thus oil pricing in dollars greatly helped the U.S. to preserve its dollar as the world's reserve currency despite the fact that the dollar was no longer backed by adequate gold reserves. Further the policy of trade deficits and budget deficits followed by the U.S. over the last four decades also made the exporting countries solely dependent on the American monetary system. : The surge in gold prices witnessed twelve years ago was nothing but a reflection of the deterioration of the dollar: when the oil price was scaling new heights every day, the OPEC countries justified the price hikes to their being paid in a steadily depreciating dollar currency.

The phenomenon of global inflation which we have witnessed in Europe and the worldwide since 1971 could also be traced to the dollar. Between 1945 and 1965, total dollar supply gre*w* by 55 percent and that was the golden period of low inflation and stable growth. After the break with the gold in

1971, dollar supply expanded by more than 2000 percent between 1971 and 2001.

Part II

Return to the Gold Standard

Alan Greenspan, former Chairman the US Federal Reserve, who had been the Chairman of the Council of Economic Advisers from 1974 to 1977, a period that witnessed hectic changes in the price of gold. published an interesting article nearly forty years ago on the possibility of a return to the gold standard. It is interesting to note that several issues that Greenspan pointed out in this article are still relevant.[8]

At the outset Greenspan noted, “In years past a desire to return to a monetary system based on gold was perceived as nostalgia for an era when times were simpler, problems less complex and the world not threatened with nuclear annihilation. But after a decade of destabilizing inflation and economic stagnation, the restoration of a gold standard has become an issue that is In the absence of the gold standard, there is no way to protect savings from confiscation through inflation

Greenspan noted that budget deficits and large federal borrowings would be difficult to finance under a *gold standard* since heavy claims against paper dollars cause few technical problems for the Treasury can legally borrow as many dollars as Congress authorizes. Once in the *gold standard*, unlimited dollar conversion into gold, the ability to issue dollar claims would be severely limited. The federal government would be forced either to increase taxes or lower the expenditure to finance federal deficits. Greenspan saw the immediate problem of restoring to a *gold standard*was fixing a gold price that was consistent with market forces: if the offered price for gold by the Treasury were to be too low, or subsequently proves to be too low, heavy demand at the offered price could deplete the gold reserves at the Fort Knox in no time. With no gold available in the reserves, gold will be taken off the*gold standard.*On the other hand, if the initial gold price were to be set very high, Fort Knox would be flooded with gold, which in turn would add to commercial bank reserves and consequently lead to expand money supply with the inflationary implications associated with increase in money supply

Greenspan recognized that the only seeming solution was for the U.S. to create a fiscal and monetary environment that could in effect make the dollar as good as gold, namely, stabilize the general price level and by inference the dollar price of gold bullion itself. He also noted that a gold-based monetary system would necessarily prevent fiscal imprudence as the 20th century history had clearly demonstrated. Greenspan knew that once achieved, the discipline of the *gold standard*would surely reinforce anti-inflation policies, and make it far more difficult to resume financial profligacy: the redemption of dollars for gold in response to excess federal government-induced credit creation would be a strong political signal.; even after inflation is brought under control, the extraordinary political sensitivity to inflation would remain.

Greenspan believed that the major roadblock to restoring the*gold standard*was the problem of re-entry: with the vast quantity of dollars worldwide laying claims to the U.S. Treasury's 264 million ounces of gold, an overnight financial system. After elaborating the advantages of the *gold standard,* Greenspan concluded that the Treasury gold notes could set a standard in terms of prices and interest rates that could put additional political pressure on the administration and Congress to move expeditiously toward non-inflationary policies. To Greenspan, gold notes could be a case of reversing Gresham's Law; good money could drive out bad currency's value relative to the dollar.[9]

Nathan Lewis wrote in*Forbes* on November 16 2018 that the gold standard did not disappear in 1971 but only went underground. Although officially gold standard might have been dismissed as superstitious non-sense Nathan Lewis notes that the system has worked well for centuries.

Part III

Aftermath of the Second World War

In the wake of the end of the Second World War, France's Jean Monnet had argued that elimination of intercontinental conflicts could be achieved only through economic integration. In 1951, he emerged as the chief architect of the *European Coal and Steel Community*, which was probably the most significant step taken towards economic integration of Europe. According to him it was only through monetary and economic union that "the political union which is the real goal" could be achieved.It was realized that political boundaries were not necessarily coterminous with the geographical boundaries of coal and iron ore and that the bargaining power for striking commercial deals could considerably be enhanced if the countries having these raw materials could form a regional bloc rather than negotiate commercial deals as individual countries. Franco Pavoncello, President of Rome-based John Cabot University, wrote in May 2011: The way to build the new union was through incremental steps toward economic integration that would one day lead to political integration."

The Second World War left behind such s great devastation that led all the countries in Europe to think on the need for greater economic and political union in Europe that culminated in the Treaty of Rome signed in 1957. Under this Treaty France, Germany, Italy, Belgium, the Netherlands and Luxembourg established the *Common Market* and the *European Economic Community* (EEC), abolished trade tariffs between members. The *Single European Act* in 1986 which was the first revision of the Treaty of Rome facilitated the development of an internal European market, allowing for free exchange of capital, goods and people). Though the same year also witnessed introduction of euro dollars, the European Commission did not contemplate a single currency for Europe. By 1970, the Werner Report to the Council and the Commission on the Realization by Stages of Economic and Monetary Union in the Community, which saw monetary union as the key step towards political union, proposed a single currency by 1980. The Report approved in 1971 envisaged linking the various currencies of Europe through the '*snake in the tunnel'*, the first attempt at European monetary cooperation; April 1972 saw launching of the currency alignment, nicknamed "the snake "setting a limit of 2,25 percent on deviations between members. Though Britain was a founder member of the '*snake'*, it was forced out of the system in just six weeks against the backdrop of its devaluation (1967) coupled with insufficient reserves to defend the parity Since Germany's *Bundesbank* held vast reserves, the *'snake'* finally ended up more of a Deutsche Mark currency bloc than a distinct single currency. France left the union in 1974, rejoined in 1975 and withdrew again in 1976. Sweden and Norway left the currency bloc in August 1977 and September 1978 respectively. In 1978, Sir Donald McDougall's report warned that it would be reckless to create a single currency unless Europe was first given an all-powerful government with the power to tax and to make a massive transfer of resources from the richer states to the poorer.

Evolution of the euro

The seeds for the euro were sown on March 1, 1973 when the then West German Chancellor Willy Brandt, during a meeting in Bonn with the British Prime Minister Edward Heath, took everyone by surprise when he came up with the idea that the member states of the European Community should join a "common float" against the dollar, linking their currencies and pooling their reserves to defend their parities. This should be seen against the backdrop of U.S. President Nixon's unilateral announcement on August 15, 1971 that the United States would no longer exchange gold at the fixed rate of US $ 35 for an ounce of gold. It also needs to be understood that since the gold standard was too inflexible and served to deepen economic crises, the Breton Woods system had established parity in terms of both gold and the US dollar. While the parity of the dollar had been pegged only in terms of gold, initially at $35 per ounce of gold, other currencies were defined in terms of both gold and the dollar. For example, the parity of the British pound was set at 12.5 pounds per ounce of gold. This implied an official exchange rate of $2.80 per one pound. When one currency went out of line with the "fundamental value', the parity was adjusted. While the German mark was adjusted upward or downward on several occasions, the British pound was devalued from $2.80 per one pound to $2.40 per one pound in 1967. As Samuelson correctly noted, "…. The ability to adjust exchange rates when fundamental disequilibrium arose was the central distinction between the Breton Woods system and the gold standard…."[10]

In 1971, the United States faced balance of trade deficits for the first time since the First World War. Under Breton Woods, it was the responsibility of the United States to rectify the imbalances in its international position. The U.S. was left with two options, either to cut spending within the United States or cut military spending in Viet Nam. A cut in domestic spending would have led to a severe recession in the country. In 1971, Paul Volcker, who was later to become Chairman of the Federal Reserve, headed an Administrative Committee, concluded that financing for U.S. deficits “has permitted the United States to carry out heavy overseas military expenditure and to undertake other foreign commitments” and an important goal was to “free foreign policy……from constraints imposed by weaknesses in the financial system.” Nixon therefore had no option other than to end the war in Viet Nam.

There was a great deal of support to the view within the US that if the system of controls on capital movements were scrapped, the US would be able to maintain its position as a major economic power in the arena of global economy. Due to its important role in the international monetary system, other nations were keen on holding to their dollar holdings. John Connelly, the Treasury Secretary in the Nixon administration, before a European audience, said, “The dollar may be our currency but it is your problem” and to an American audience he said, “Foreigners are out to screw us. Our job is to screw them first.”

The Breton Woods system of fixed exchange rates was designed to bring stability to currency markets. Since major currencies were tied to the U.S. dollar, other countries essentially adopted U.S. inflation rates. Left with no other alternative, on August 15, 1971 the world was taken by surprise by the unilateral announcement by President Nixon that the United States would no longer exchange gold for the dollar.

The international monetary system or the Breton Woods system had been founded on the firm commitment by the United States to redeem international dollar holdings for gold at the fixed rate of $35 per ounce. Nixon had not taken any of the capital powers into confidence while taking such a momentous decision making a major departure from the agreement concluded at the Breton Woods in 1944.

The next important stage was the establishment of the European Monetary System (EMS) in 1978, which limited exchange rate fluctuations between member countries. Kindelberger noted, “It introduced the European Currency Unit as a parallel currency, provided two measures to aid in narrowing fluctuations of national exchange rates, constituted a European Monetary Fund, and provided a system of credit facilities for mutual payments support”.[11] Since the membership of the EMS was voluntary, the system witnessed Britain joining the system and leaving it in 1982 while France remained with the EMS but wanted to leave it in 1982 when Francois Mitterrand was elected. President. Greece joined the European Monetary System in 1984, while Portugal and Spain joined in 1988. The net result was a bunch of currencies that were strongly tied to the Deutsche Mark, like the Belgian Franc, Dutch Guilder, and several peripheral currencies, like the Italian Lira which had problems in maintaining their currency’s peg to the Deutsche Mark.

It was the Delor’s report (1988) recommending a gradual move towards a single currency provided the basic framework for the Maastricht Treaty, signed in 1992, which established the timetable for the putting the euro in place on January 1, 1999. This could not have been accomplished without the strong political leadership provided by Francois Mitterrand and Jacques in France and Helmut Kohl in Germany. Nineteen of the twenty-nine EU members are part of the euro zone, while other EU members, including Bulgaria, the Czech Republic, Hungary, Poland and Romania, are required by the Treaty to join later. Demark and the United Kingdom were exempted from joining the euro zone.

Under the Maastricht Treaty *convergence criteria*and the *Stability and Growth Pact* of 1997, member states had to ensure inflation below 1.5 percent, fiscal deficit below 3 percent of GDP and the debt to GDP ratio of less than 60 percent. While several countries had to undertake strict budgetary reforms in order to meet these criteria, in practice, however, these criteria were more honored in their breach than observance. This was attributable to the over enthusiasm of the EU authorities to expand the membership of the euro zone, overlooking such serious lapses. In his book *Greece’s Odious Debt* Jason Monolopoulos, notes

…… . There was shockingly weak due diligence in assessing the suitability for the entry into the euro and equally weak application of the few rules that were supposed to police its operation…12

September 1992 witnessed a speculative attack on the European Rate Mechanism (ERM) caused by the rejection of the Maastricht Treaty by a Danish referendum leading to devaluations by Britain and Italy resulting in Britain withdrawing from the system. Though Britain, Denmark and Sweden had opted out of the single currency, both Britain and Denmark had decided to fix their currency to the euro and retained their right to join the euro zone at a later date. The speculative attack reinforced the desire of Italy and other countries to join the stability of the euro rather than be left to the uncertainties of a floating currency.

Birth of the euro and its early success

The developments during the last twenty years since January 1 1999, when the euro was launched are quite significant. Till the birth of the euro, there was no alternative to the dollar. When the euro was in place in 1999, its value was fixed at 1.1743 dollar to a euro. Though the euro was introduced as the common currency on January 1, 1999, synthetic historical prices using a weighted average of the precious currencies have been computed to show that the euro /US dollar reached an all time high of 1.87 in July, 1973 and an all time low of 0.70 in February 1985. Even though there is not much oil in the euro region, policy makers in Europe had taken care to see that the euro was backed by a significant amount of gold. Therefore, when the gold price was rising, there was corresponding strengthening of the new currency. The European Commission claimed that adoption of the single currency, euro, led to a savings of 0.5 percent of GDP within two years of its launch as compared to use of multiple currencies.

The euro got an unexpected boost when Saddam Hussein, President of Iraq converted US$2 billion, received from the United Nations under the food-for-work program, into euros in November 2000 purely to avoid the money from being frozen. This was quickly followed by countries like Iran and Venezuela who started demanding euros for their oil. As a result, the value of the dollar registered a steep fall and around mid-2002 the exchange rate stood at US$ 1.5 to one euro. This possibly led to the U.S. attack on Iraq in early 2003. When Baghdad was attacked, the euro was available for 92 cents just for a day. That support for the US operations in Iraq came only from the non-euro UK, with the entire euro region keeping cool, should also not be overlooked.[13]

In 2002, the euro was worth $ 0.87 As the US debt grew 60 percent, the dollar fell 40 percent and by December 2007, one euro was equal to $1.44. In 2008, the dollar strengthened 22 percent businesses were hoarding dollars during the global melt down and by end of the year the euro was equal to $ 1.39. During 2009, the dollar fell 20 percent due to debt fears and by December the euro was equal to $1.43. After the Greek debt crisis broke out in 2009, the dollar started strengthening to $1.32 in December 2010 and to $ 1.2973 in /December 2011. The trend, however, was reversed in 2012 and 2013 when the dollar weakened and it declined to $ 1.3186 in December 2012 and to $ 1.3779 in December 2013. In 2014 when investors started fleeing the euro zone the dollar strengthened to $1.21 in 2014 and $1.05 in March 2015.

The euro lost 0.0867 or 7.35 percent against the dollar during the last twelve months from $ 1.18 in January 2015 to $1.08 in January 2016. The euro touched an all time of $1.60 to one euro on April 22 2008.Since then the euro has weakened considerably. This is because the future of the European Union as well as the euro was in doubt during the Greek debt crisis. Further the European Central Bank lowered its interest rates. This lowered interest rates for any one saving or lending in euro lowered the value of the currency itself. When ECB announced its version of quantitative easing the euro plunged to $ 1.10In March 2015.

In 2007, the European Union surpassed the United States as the world’s largest economy. Between 2002 and 2008 the euro rose 63 percent against the dollar. While the decline of the euro started once the ECB raised interest rates rather prematurely fuelling fears of a deep recession, the euro-zone debt crisis accelerated the euro’s downward trend. The euro did recover in 2013 but by the end of 2014 the euro declined to $1.20

The value of the euro depends on three factors; 1) ECB’s interest rate 2) debt levels of individual countries like Greece 3) strength of the European economy. When growth is strong and when interest rates are rising, the foreign exchange traders push up the price but some other traders who also read the same data bid the price down on the premise that its value will decline. The complex interaction of these factors determines the value of the currency at any given point of time. Despite its volatility, the EU allows the euro’s value to be decided by the foreign exchange mark

With the euro trading in the region of $1.08, the day in 2007, the European Union surpassed the United States as the world’s largest economy. Between 2002 and 2008 the euro rose 63 percent against the dollar. While the decline of the euro started once the ECB raised interest rates rather prematurely fuelling fears of a deep recession, the euro-zone debt crisis accelerated the euro’s downward trend. The euro did recover in 2013 but by the end of 2014 the euro declined to $1.20

Greece's Debt Problem

The euro worked satisfactorily as long as long as the eleven countries that joined the euro zone in 1999 kept their fiscal deficit within the parameters of the Maastricht Treaty, namely, three percent of their respective GDP. The problem for the euro started when countries like Greece were admitted into the zone. On November 15, 2004, Greece admitted it joined the euro in 2001 on the basis of figures that had shown its budget deficit to be much lower than it really was. In fact, Greece had already declared that its public debt had breached the European Union cap between 2000 and 2003, since the cost of hosting the 2004 summer Olympics had touched 7 billion euros.

Since the potential exit of Greece from the euro zone or what is popularly called ***Grexit*** might have had disastrous consequences for the entire euro zone, in May 2010, the European Commission, European Central Bank and the International Monetary Fund established the *European Financial Stability Facility* to provide a bailout loan of $163 billion to Greece in exchange for strict austerity measures coupled with tax hikes. A second bailout plan for roughly $ 178 billion was made available to Greece in October 2011. Under this package private holders of Greek debt accepted a fifty percent write off. The fall out of the austerity measures was that the Prime Minister George Papandreou had to step down in favour of the Technocratic National Government in 2012. In November 2012 the bailout terms were again renegotiated that included lower interest rates for Greece's loans.

The first step in any stabilization programmed from the IMF for any similarly placed country like Greece would be devaluation of the currency. In the case of Greece, however, this was ruled out since the euro could not be devalued just for the sake of one country facing serious debt problems in the euro zone.

When the IMF approved a loan package of euro 45 billion in 2010 for Greece all the developing countries on the IMF Executive Board had argued that the banks should also share the costs of the crisis and they should cancel some of their debt, rather than bailing out the banks but they were totally ignored by Europe and USA. Managing Director of the IMF Christine Laggard had also repeated her call for debt relief. According to Sarah -Jayne Clifton, since 2010, IMF, European governments and the European Central Bank had lent 252 billion euros to Greece out of which, 232 billion euros were spent on debt payments, bailing out Greek banks and paying 'sweeteners' to speculators to get them to accept the 2012 debt restructuring, an obvious reference to the commission paid to

Goldman Sachs for the swap deal.[15]Greek lawmakers have recently approved the economic reforms demanded by its international creditors that include rising retirement age, cutting pensions, liberalizing the energy market, opening cosseted professions, enlarging property tax base and pushing forward the dormant program to privatize state assets. Even as this program was contemplated in July 2015, the former Finance Minister Yantis Varoufakis had fore-warned:" the programme will go down in history as the greatest disaster of macroeconomic management ever." According to former Chairman of Federal Reserve Prof. Ben Bernanke, failure of European economic policy had played a significant role in the Greek debt

While this package was expected to pave way for Greece to receive the first 2 billion euros from the bailout program, it had already hit the road block. Since Greece's debt crisis began in 2010, most international banks and foreign investors had sold their Greek bonds and other holdings they were no longer sensitive to what was now happening in Greece. At the height of the crisis a few years ago it was thought if Greece were to exit the euro zone it might trigger a global financial disaster whose dimensions could be larger than the collapse of the Lehman Brothers in September 2008. According to the *New York Times,* however, if the ***"Grexit"*** were to happen now, the consequences might not be all that catastrophic.[16]. In a way the euro zone could even be better off without a country that leaned constantly on its neighbor's support. In the circumstances it is high time Greece is permitted to leave the euro zone and issue its own currency.

Other euro zone countries affected by the crisis

The banking crisis which was at the root of the global meltdown in the United States in 2008 did not spare Ireland whose banks suffered heavy losses from the housing sector when the Government decided to support the financial system. In November 2010, Ireland sought $112 billion package from the EU-IMF in exchange for several austerity measures. This led to one of the worst severe recessions in the euro zone when output declined by 10 percent and unemployment rose from 4.5 percent 10 13 percent in 2010.

In the case of Portugal since foreign debt- financed deficit amounted to 10 percent of GDP in 2009, the country would collapse once the foreign investors withdrew their money. The country needed $116 billion bailout package. As the country had to implement severe austerity measures, it fell into its deepest recession in its history.

By the end of 2011, the debt crisis spread to Europe's third largest economy, Italy. Since bail out was not feasible for Italy's $2.6 trillion in public debt, Italy's Prime

Minister Silvio Berlusconi had to step down making way for the Economist Mario Monti credited with carrying out several reforms in the fiscal sector. In the 2013 general elections, the Democratic Party won the elections narrowly and had a number of leaders including Matteo Renzo, the youngest Prime Minister Italy ever had but they found it impossible to pull out Italy from recession.

Like Ireland, Spain faced a problem in its housing sector and required a bail out. In 2012, euro zone funds to the tune of $123 million were made available to Spain by EU leaders. In the case of France, unemployment rose to 11 percent which weekend its competitive position. In early 2013, Cyprus's banking collapsed in the wake of the flight of foreign capital that left bulk of the financial sector insolvent. The problem got compounded since the Cypriot Banks were holding the devalued Greek bonds. In March 2013, Cyprus received $13 billion bailout that resulted in the closure of the country's largest bank, Laski, and several wealthy depositors lost all their money.

Most politicians in the euro zone are keen, nay, desperate to stay together since the euro represents their political ideal that will ensure peace and prosperity throughout Europe. The political protagonists of the euro visualize the zone evolving into a federal state with greater political power, As for economic reasons, while hard –working German voters may resent the transfer of their tax money to other countries that enjoy early retirement and shorter work-weeks, the German business community supports paying taxes to preserve the euro as it recognizes that German businesses benefit from the fixed exchange rate that prevents other euro-zone countries from competing with Germany by developing their currencies.

In fact, several investors had been quietly diversifying their investment funds to euros before the crisis began in Greece. They eventually recognized that the problems of the peripheral countries were not a problem for the euro and should be reflected in country-specific interest rates rather than in the euro's value. The result was a rising euro and a renewed shift of portfolio balances to euros from dollars.

Pedro Solbes, Executive Chairman of FRIDE (a European think tank for global action (and former Spanish Minister of Economy) chose to hail the euro as a joint success that enabled a long period of growth and price stability in Europe. Without the euro, Europe might have witnessed an increase in protectionism, which would in turn have aggravated the impact of the crisis in Europe and elsewhere... According to Hans-Werner Sinn, President of Germany's Ifo Institute of Economic Research, survival of the euro depends on whether

European countries implement political and private debt constraints that effectively limit capital flows[17]

While huge capital exports brought a slump to Germany, the countries at the southern and western peripheries overheated with the bust and boom resulting in current accounts and surpluses and deficits respectively. According to Sinn, what Europe needed a crisis mechanism that would help to prevent a crisis in the first place and mitigate it when it occurs. Such a system was proposed five years ago at the European Economic Advisory Group at the Centre for Economic Studies and the IFO Institute for Economic Research. The plan envisaged a three-stage rescue mechanism that distinguishes between a liquidity crisis, impending insolvency, and offered specific measures at each stage. The system was expected to allow Germany to gradually appreciate in real terms by living through a boom that generates higher wages and prices and thus reduces the country's competitiveness, while cooling down the overheated economies of the south such that the resulting wage and price moderation would improve their competitiveness. As a result, European trade imbalances would gradually reduce.

According to Barry Eichengreen, Professor at the University of California Berkeley, Europe's budget deficits were largely a result of the continent's "festering banking crisis."

The whole euro area would benefit from stronger discipline on borrowers and lenders. He had cautioned that this could not be achieved by imposing German debt ceilings continent-wide. He held that ECB could refuse to buy more Greek, Irish and Portuguese bonds only if the banks were adequately capitalized.[18]

. Martin Feldstein, Chairman of the US Council of Economic Advisers under President Reagan and currently George F. Baker Professor of Economics at Harvard has rightly held that the creation of the euro was an economic mistake. Right from the start it was clear that imposing a single monetary policy and a fixed exchange rate on a heterogeneous group of countries would lead to higher unemployment and persistent trade imbalances.[19]Further, the single currency coupled with independent national budgets produced massive fiscal deficits in countries like Greece, while the sharp drop in interest rates in several countries in the wake of the launch of the euro caused excessive private and public borrowing that eventually created banking and sovereign debt crises in Spain, Ireland and elsewhere.

Julian Knight has envisaged several possible scenarios for the euro. The experiment with the euro has shown that economies of varying dimensions like Germany and Greece cannot stay together. While economists would like weaker countries like Greece, Portugal and Ireland to leave the euro zone and reintroduce their own currencies. politicians, prefer all the countries in the euro zone to stay together in which case stronger countries like Germany would come to the rescue of weaker countries and the European Central Bank which administers the euro, would buy the government debt of the most troubled countries like Greece, Portugal, Ireland and more recently Italy, [20]

In the limited break up scenario for the euro, Greece, Portugal and Ireland would leave the euro zone and reissue their own currencies, In the substantial break up scenario, countries like Belgium and Italy would also leave the euro zone, As Julian Knight rightly notes, "although all members of the euro zone are meant to be equal, some are more equal than others": [21]With the presence of giants like Germany and France in the euro zone, small economies like Malta and Estonia could exert very little influence on events in the euro zone. Once the weaker countries leave the euro zone, France and Germany would remain in the euro zone. Even though the survival of the euro will require large fiscal transfers from countries like Germany and France to those euro zone countries with large debts and chronic trade deficits, the euro, according to Professor Feldstein, is likely to survive for both political and economic reasons.

In my view, the euro has still a future if the membership of the euro zone could be confined to the eleven countries that joined the euro zone on January 1, 1999 namely, Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain and show its door to Greece. If other members like Slovenia, Cyprus, Malta, Slovakia, Estonia, Latvia are able to contain their fiscal deficit below three percent they could be permitted to continue in the euro zone. Countries that are not able to contain their fiscal deficit should be allowed to leave the euro zone and issue their own currencies.

In this connection one should note that it may not be possible for the euro to emerge as a major reserve currency replacing the dollar. Since the mid-20th century, the U.S. dollar has practically been the de facto world currency. 1996, the dollar accounted for approximately two thirds of the world's foreign exchange reserves. Further, several of the world's currencies are pegged against the dollar. In spite of all the precautions taken by the European Union for the euro like sufficient quantity of backing of gold, the fact remains that the dollar continues to dominate the global currency reserves and the oil producing countries in the Gulf like Saudi Arabia prefer to price all the petroleum products only in the US dollar. The euro zone has hardly any oil reserves. It is not therefore surprising that even after the introduction of the euro in 1999, the US dollar accounted for nearly 64 percent of the global currency reserves as compared to 27 percent held in euros. According to Robert Gilpin, 40 to 60 percent of international financial transactions are denominated in dollars[22]. As long as the oil continues to be priced in US dollars, the chances of the euro becoming a rival reserve currency to the US dollar are extremely thin.

The developments over the last three years have raised the questions on the continuance of the euro as the single currency of the European Union and if one should consider an alternative to the euro as a single currency not just for Europe alone but across the globe.

US Dollar: the de facto World Currency

In spite of the all the precautions taken by the European Union for the euro like sufficient quantity of backing of gold, the fact remains that the dollar continues to dominate the global currency reserves and the oil producing countries in the Gulf like Saudi Arabia prefer to price all the petroleum products only in the US dollar. The euro zone has hardly any oil reserves. Since the mid 20th century, the U.S. dollar has practically been the de facto world currency. According to Robert Gilpin, 40 to 60 percent of international financial transactions are denominated in dollars. For decades, the dollar has been the world's principal reserve currency and in 1996, the dollar accounted for approximately two thirds of the world's foreign exchange reserves. Further, many of the world's currencies are pegged against the dollar. Countries like Ecuador, El Salvador and Panama have adopted the U.S.dollar as their currency. Even after the introduction of the euro in 1999, the dollar accounts for nearly 64 percent of the global currency reserves as compared to 27 percent held in euros.

The euro currency is used by 19 out of 29 countries in Europe. But, the developments in countries like Greece during the last sixteen years have provided enough fodder to speculate on the possible extinction of the euro in the foreseeable future. According to Werner Bonadurer, Professor of Finance, at W.P. Carey School of Business at Arizona State University in Tempe, the likelihood of a full scale collapse of the euro remains very remote but the impossible has become possible, and it is necessary to think about the unthinkable. A total collapse, though remote, in Bonadurer's view, could lead to multi-year depression in Europe and several years of recession in the U.S.[23] Terry Connelly, Dean Emeritus of the Ageno School of Business, at Golden Gate University, San Francisco, holds that the impact of collapse of the euro on the U.S. economy could be much worse than the Great Depression since it would have the potential of triggering even a greater one worldwide. "A rush of financial assets out of the euro zone would play havoc with currencies and the price of oil." A collapse, Connelly predicts could destroy interbank lending worldwide. "A run on banks around the world would freeze credit markets, making it difficult for businesses to borrow money." [24] According to James Sagner, Associate Professor at the School of Business the University of Bridgeport, Connecticut, uncertainty about the euro's future is driving down the currency's value relative to the dollar[25]

In his article, **in** the *Washington Post* Robert J. Samuelson notes that while the euro has not achieved its central goal of increasing economic growth and strengthening public support for European political institutions, just the opposite has happened.: the economies of the all those countries that adopted the euro have lagged behind the U.S. in growth; in 2019 the growth is projected at 1.6 per cent for the euro zone as compared to 2.6 per cent for the United States.[26] E. Martin Feldstein's view that the creation of the euro was an economic mistake was

referred to earlier.

Brexit and the Pound Sterling

Market Insights observed that the 2016 vote in favour of Brexit created utter chaos for the British pound, comparable only to the immediate aftermath of World War II or

Black Wednesday. Subsequently, the transition process has been a roller costar ride for the pound sterling.

Crunch Time, an article published in *The Economist* (August 2018), points out that of 140 odd currencies tracked by the data provider, Bloomberg, pound sterling depreciated against more than 120 currencies since the referendum. In the weeks following the Brexit referendum in June 2016, the pound sterling lost 10 percent of its value. On a trade-weighed basis, it lost 50 percent of its value since April 2018. Fall of the pound below $1.28 on August 10, 2018 was the lowest decline in a year. The prospect of leaving the European Union has adversely affected the sentiments for the British currency. The protagonists of Brexit, however, hold that a cheaper pound sterling will make the British products more competitive in foreign markets. While this is reflected in 7 percent increase in exports, the *Economist* feels this is more due to a general pick up in global trade than to greater currency competitiveness. Over the same period, average G 7 countries have witnessed much stronger export growth than Britain. Considering the fact that half of Britain's food requirements comes from overseas, import bill of Britain has gone up substantially thanks to a weak pound. Inflation has been above Bank of England's target of 2 percent since early 2017. The purchasing power of working age benefits that have been frozen in cost terms until 2020 has fallen steeply.

Samuel Tombs of Pantheon Macroeconomics holds that in the event of no-deal Brexit, the pound will fall to $1.15, the lowest in three decades and advises Britain to reach a sensible agreement with the European Union

In the January 31, 2019 issue of *The Economist*, Markets and Brexit: Squeal at No Deal,notes that the pound has risen whenever it looked like Brexit was being softened or postponed, and weakened when it looked like negotiations were deadlocked. : on January 29th when a proposed amendment to postpone the Brexit was defeated in the British Parliament, the pound fell by a cent against the US dollar but it quickly bounced under the hope that Britain and the European Union would reach some kind of deal before the deadline March 29, 2019 set for the departure of the United Kingdom from the European Union.

In the event of a no-deal Brexit, the currency markets are likely to take the biggest hit. While Adam Cole at Royal Bank of Canada anticipates a 10 percent decline in the pound, David Page at Axe, an insurance group, expects the pound to fall to $1.10 to 1.15 from its current level of $ 1. 31 and to parity with the euro which is currently trading at 87.2 pence. David Owen at the Jefferies, an American Bank, visualizes the possible repeat of the mid-1980s level of $1.05 to the pound. While the authorities will try to limit disruption to trade that might minimize the extent of the pound's fall, the slower growth and lesser foreign direct investment are likely to weaken the pound. The November 2018 report of the Bank of England suggests that no-deal Brexit would lower output but raise inflationary pressures. While the Bank of England may raise interest rates to strengthen the pound if inflation were to rise quite high,KlumPickering of Berenberg, a German investment bank, observes" Raising interest rates in the event of a hard Brexit would be the equivalent of losing a leg and deciding the best way to regain balance is chopping off the other."

Though government bonds might be risk free, their yields will fall in the event of no deal Brexit. Britain badly needs foreign investment to finance its current account deficit which was 3.9 percent of GDP last year Owen thinks that investors are also worried about the possible risk of a Labour Government under Jeremy Corbyn. A survey by Bank of America Merrill Lynch found that investors have never been so negative about the London market in the past twenty years. In the event of a no deal -Brexit the British stocks will fall by 25 percent while the European stocks by 10 percent, according to a forecast by the index group, MSCI.

As seen from the above analysis, several economists are agreed that a no-deal Brexit is going to be disastrous for the pound sterling. The British Prime Minister's moves to renegotiate the deal should be seen against this backdrop. The only silver lining to the cloud is that Britain while joining the European Union did not adopt the euro currency in the place of the pound sterling. The Brexit chaos led to the resignation of the British Prime Minister Teresa May on May 25 and a new Prime Minister Boris Johnson assumed charge in the month of July, 2019.

Arguments for a Global Common Currency

According to David Francis, if the market that trades about $1.2 trillion worth of currencies in a day were to disappear, it would save companies and individuals hundreds of billions of dollars a year in foreign exchange and hedging costs. Secondly, according to David Francis, no country would have a balance of payments problem or need to maintain reserves of foreign assets, like currency or bonds to counter dramatic fluctuations in the market. The end of currency fluctuations would also stabilize international business as manufacturers on both sides of the Atlantic would no longer have to adjust to huge changes like the slide in the value of the euro from $1.17 initially in 1999 to 83 cents in 2002 and now to $1.11. [28]

Viability of a Common Currency

The adoption of a common currency is rather a prolonged process. One should only recall how much time it took for the euro zone countries in Europe to evolve a common currency which was in place on January 1, 1999 after almost eleven years of preparatory work that started in 1988. Strict targets were fixed in the Maastricht treaty and Stability and Growth Pact 1997 and until the targets for fiscal deficits were achieved, the common currency could not be in place.

The exchange rate of a currency depends on several economic indicators like the inflation rate and the interest rate differentials. Let us assume for a moment that India wants to adopt the U.S. dollar as its national currency in the place of the Indian rupee. Let us also assume that the inflation rates in both U.S. and India are identical. But is it just possible to keep the interest rates as low as in the U.S. within the framework of administered rates of interest for Post office deposits and the Public Provident Fund where the rates are in the region of 7 to 8 percent. The banks in India cannot get any deposits from the public if the interest rates offered by them are not either equal or higher than those available for post office deposits or non-banking financial institutions. If a major currency cannot be adopted in just one other country whose economic indicators are different from the U.S., where is the question of evolving a common global common currency for the whole world?. History is replete with the disastrous consequences of countries which tried to link their currencies to the U.S. dollar? When one of the African countries linked its currency to the dollar, its currency started appreciating when the dollar was appreciating, the country's export competitiveness took a severe beating and the country was left hardly with any foreign exchange to meet its import bill.

Merits of a Global Common Currency:

Consolidation of Currencies and Regional Groups

Former Federal Reserve Chairman Paul Volcker had observed that a truly globalized world economy needed a global currency. In 2014 Volcker called for a new Bretton Woods agreement that could create a new coordinated international monetary and financial system and establish new rules that could guide to create a new global currency that could replace the dollar.[29] About eighteen years ago, Robert Mundell, a noted economist and Nobel Laureate, known for his supply-side economic theory, did consider a plan of action for a world currency along with a small group of economists and officials.[30] there have been moves in the past to consolidate currencies, the ***euro*** being the most obvious example. Eight former French colonies in Africa have long shared a common currency. Since 1981, the Eastern Caribbean Central Bank had provided the EC dollar to about a dozen island nations, including Antigua, Barbuda, Dominica, Montserrat and St.

Lucia. The Gulf Cooperation Council has been contemplating a common currency for Saudi Arabia, Kuwait, Bahrain, Oman, Qatar and the United Arab Emirates. The West Africa Monetary Zone had programmed to introduce the *euro* to Ghana, Gambia, Sierra Leone, Guinea and Nigeria. In my article published in the *Outlook* (2003), the concept of a common currency for the SAARC countries ----India, Bangladesh, Pakistan, Sri Lanka, Bhutan and Nepal was floated by the author of this paper.[32]

Special Drawing Rights (SDRs) at the IMF

The Special Drawing Rights (SDR) is an international reserve asset created by the International Monetary Fund (IMF) in 1969 to support the Bretton Woods' fixed exchange rate system. After the collapse of the Breton Woods fixed exchange system in 1971, the SDR was redefined as a basket of certain select currencies. The U.S. dollar value of the SDR was calculated as the sum of the specific amounts of four currencies valued in U.S. dollars on the basis of exchange rate quoted at noon each day in the London market. It has limited uses like determination of fees by the International Postal Union and as a spin off, to determine the roaming charges for the mobile telephones in certain regions except Europe

In 1971, when the United States faced balance of trade deficits for the first time since the First World War, the then US

President Nixon had no option except to end the war in Viet Nam. The SDR should have become extinct in the wake of Nixon's decision in August 1971 not to exchange dollar for gold at the fixed exchange rate of $35 per ounce of gold but it has continued till date with modifications from time.The SDR basket of 16 currencies from 1974 to 1980 was replaced in 1981 by a basket of five currencies --- US dollar, Deutsche Mark, French Franc, British pound, and Japanese yen. After the euro was in place in January 1999, the SDR basket included only four currencies: the dollar, the euro, the pound and the yen. The SDR basket was expanded in 2016 to accommodate the yuan as the fifth currency.

The 'SDR' was making news during October-November 2009 in the context of international opinion gathering momentum in favour of a common global currency.

At the annual meetings of the International Monetary Fund and the World Bank at Istanbul in October 2009, UN Under-Secretary-General for Economic and Social affairs, ShaZukang called for a new reserve currency instead of the US dollar, rather a global reserve currency to end dollar supremacy which has allowed the United States the privilege of building a huge trade deficit: "Important progress in managing imbalances can be made by reducing the reserve currency country's privilege to run external deficits in order to provide international liquidity. It is timely to emphasize that such a system also creates a more equitable method of sharing the seignior age derived from providing global liquidity." According to ShaZukang, greater use of a truly reserve currency such as the IMF's Special Drawing Rights (SDRs) enables the seignior age gained to be deployed for development purposes.

Advocates for a global common currency have been suggesting the SDR as alternative for the US dollar as the reserve currency, it should be realized that it would not be possible to adopt the SDR as a universal currency as adoption of a currency whose value is determined on a daily basis at a particular location will pose practical problems for daily transactions across the globe with numerous time zones. Further the SDR whose value is determined from a currency basket which does not include several important currencies like the Canadian dollar, Australian dollar, Singapore dollar, and the Indian Rupee would not be easily acceptable to many countries. Lord Meghnad Desai has been a strong advocate for including the four Rs--------namely, the Ruble, the Rand, the Reminbi and the Rupee in the SDR basket. The proliferation of several currencies in the SDR basket was highlighted in an article in the *Hindu Business Line* in December 8, 2015.[33] The Chinese currency yuan or the Reminbi was added as the fifth currency in the SDR Basket from October 2016. The question that arises in our minds is what could be the global common currency? The choice could be among the four currencies that make up the SDR.

The Proposal

My proposal in this paper is twofold. First, one can easily see that out of the five currencies in the SDR basket, both the euro and the pound sterling are in deep trouble and continuance of the SDR as an international reserve asset in its present composition seems no longer viable. The other two currencies, yen and yuan, do not enjoy a clean track record. Both Japan and China have manipulated their respective currencies in the past to boost their respective exports. In 1985, the Japanese yen at 220 to a US dollar had almost killed the US auto industry till President Ronald Reagan imposed import quotas on Japanese cars when the Yen rose to 120 to a dollar. The IMF should have removed the yen from the SDR Basket in its 1986 review. Had it been done the yuan would not have found its way into the SDR basket in 2016. This leaves out only the dollar. It is high time that the International Monetary Fund Executive Board discusses this issue and replaces the outdated SDR with just one currency, the US dollar. Replacement of the SDR by the US dollar would signal a return to the fixed exchange rate regime or the Breton Woods system where the value is determined by just the gold and the dollar.

The merits of the fixed exchange system have been *described* in Part I of this paper by extracting extensively from Samuelson.

In an article, From Dollar to e-SDR published in the *Business Standard* on May 1, 2018, Andrew Sheng and Xian Geng at the Asia Global Institute, University of Hong Kong, have put forth a case for an e-SDR as the quintessential reserve asset that would be fully backed by other reserve currencies with the advent of crypto currencies. The authors have advanced political, rather than economic arguments, for their prescription: the US President Trump's threats of trade and currency wars are fuelling fears that the US dollar could become a weapon in geo-political disputes. There are, however, no takers for this proposal. [34]

If the IMF were to adopt the US dollar as its reserve currency by giving up the SDR, it will take us closer to gold exchange standard but not in it s entirety. It should be appreciated that the U.S. does not even have enough gold, at current rates, to pay off the portion of its debt owed to foreign investors. China, Japan and other countries own $3.2 trillion in U.S. Treasury debt but there is only $223 billion at $914 per ounce total in gold reserves at Fort Knox. Therefore, it is just not possible for the U.S. to transform itself to a gold exchange standard on its own strength only. But in the event of the U.S. emerging as a common global currency, then all the gold owned by the countries joining the dollar zone plus the gold stock held by the IMF should be available to back the dollar. According to the estimates of the World Gold Council, at the end of the year 2001, all the gold mined till that point of time amounted to 45,000 tones. If one goes by the national gold reserves, USA accounts for the maximum quantity of gold: USA (8,138.50 tones), Germany (3,412.60 tones), IMF (3,217.60 tones), France (2,508.80 tones), Italy (2,451.80 tones), Switzerland (1040.10 tones), Japan (765.20 tones), Netherlands (621.40 tones) and China (600.00 tones). India' stock of gold rose up to 550 tones ten years ago after the purchase of 200 tones from the IMF. Governments across the globe hold close to 30.000 tones. If countries like Canada, Australia, Japan and Singapore were to join the dollar zone, the US dollar backed by gold holdings of all those countries adopting the dollar as their currency, one could hope to return to the gold exchange system, which would help put economies of the dollar zone countries on the right track. In fact, France should return all the gold that it exchanged for the dollar in the late nineteen sixties and the early seventies that compelled President Richard Nixon to take the historic decision in 1971 causing collapse of the international monetary system.

In order to achieve this and sustain the gold exchange standard it may be necessary to have a central fiscal authority for the entire dollar zone that could exercise constant vigil over the fiscal policy of member countries. Prior to launching of the Euro, Marco Cangiano and Eric Mottu, in an IMF Working Paper (December 1998) had argued that as monetary union would generate pressures for closer economic integration, there would be a need for a central fiscal authority for the euro zone area. This case for a central fiscal authority would become even stronger in the event of putting a common global currency in place.[30] No country would easily surrender their powers of taxation to a central authority but if they want to have a currency which would be linked to gold, certain amount of compromise would be necessary. At best they may have to agree to a central coordinating mechanism which could exercise surveillance over the fiscal deficits of the countries in the common currency area.

Once the US dollar replaces the single reserve currency, the dollar could qualify to be a common currency for a select number of countries. Even after the introduction of the euro in 1999, the dollar accounts for nearly 64 percent of the global currency reserves as compared to 27 percent held in euros, with 40 to 60 percent of international financial transactions being denominated in dollars.[31] If both the United Kingdom and the European Union were to adopt the US dollar as their currency it will lead to a substantial amount of savings in terms of conversion and transaction costs for payments to the gulf countries to pay for their oil which is priced in dollar. As in the case of the Maastricht Treaty for the euro, the US Federal Reserve in close coordination with the IMF should evolve specific criteria for admission of countries into the dollar zone Apart from the eleven countries who joined the euro zone in 1999 and Britain, the dollar zone could cover counties like Canada due to its sheer proximity to the United States, Australia and Singapore provided they satisfy the prescribed criteria to be prescribed for the purpose. Adoption of the US dollar is bound to lead to substantial savings for the dollar zone countries. The replacement of the Special Drawing Rights would signal a return to the fixed exchange rate regime or the Breton Woods system where the value is determined by just the gold and the dollar. As the merits of the fixed exchange rate have been spelt out in detail by Samuelson in the early part of this paper the advantages of going back to the fixed exchange rate system appear to be a desirable alternative.

Tables I and II at the end of the paper show how the gold prices have risen beyond one's imagination in the post 1971 era when the Breton Woods system was abandoned and the exchange rate was subject to the values of currencies in the SDR basket. The comparison of gold prices between pre-1971 and post 1971 is really striking and gives enough justification to go back to the Breton Woods system of a fixed exchange rate regime where the value of a currency is determined with reference to the dollar and gold only.

TABLE I

Prices of Gold 1833 to 2011

Year	Average Price
1833-49*	18.93
1850	.18.93
1851	18.93
1852	18.93
1853	18.93
1854	18.93
1855	18.93
1856	18.93
1857	18.93
1858	18.93
1859	18.93
1860	18.93
1861	18.93
1862	18.93
1863	18.93
1864	18.93
1865	18.93
1866	18.93
1867	18.93
1868	18.93
1869	18.93
1870	18.93
1871	18.93
1872	18.94
1873	18.94
1874	18.94
1875	18.94
1876	18.94
1877	18.94
1878	18.94
1879	18.94
1880	18.94
1881	18.94
1882	18.94
1883	18.94
1884	18.94
1885	18.94
1886	18.94
1887	18.94
1888	18.94
1889	18.93
1890	18.94
1891	18.96
1892	18.96
1893	18.96
1894	18.94
1895	18.93
1896	18.98
1897	18.98
1898	18.98
1899	18.94
1900	18.96

Year	Average Price
1901	18.98
1902	18.97
1903	18.95
1904	18.96
1905	18.92
1906	18.90
1907	18.94
1908	18.95
1909	18.96
1910	18.92
1911	18.92
1912	18.93
1913	18.92
1914	18.99
1915	18.99
1916	18.99
1917	18.99
1918	18.99
1919	19.95
1920	20.68
1921	20.58
1922	20.66
1923	21.32
1924	20.69
1925	20.64
1926	20.63
1927	20.64
1928	20.66
1929	20.63
1930	20.65
1931	17.06
1932	20.69
1933	26.33
1934	34.69
1935	34.84
1936	34.87
1937	34.79
1938	34.85
1939	34.42
1940	33.85
1941	33.85
1942	33.85
1943	33.85
1944	33.85
1945	34.71
1946	34.71
1947	34.71
1948	34.71
1949	31.69
1950	34.72
1951	34.72
1952	34.60

Year	Average Price
1953	34.84
1954	35.04
1955	35.03
1956	34.99
1957	34.95
1958	35.10
1959	35.10
1960	35.27
1961	35.25
1962	35.23
1963	35.09
1964	35.10
1965	35.12
1966	35.13
1967	34.95
1968	39.31
1969	41.28
1970	36.02
1971	40.62
1972	58.42
1973	97.39
1974	154.00
1975	160.86
1976	124.74
1977	147.84
1978	193.40
1979	306.00
1980	615.00
1981	460.00
1982	376.00
1983	424.00
1984	361.00
1985	317.00
1986	368.00
1987	447.00
1988	437.00
1989	381.00
1990	383.51
1991	362.11
1992	343.82
1993	359.77
1994	384.00
1995**	383.79
1996	387.81
1997	331.02
1998	294.24
1999	278.98
2000	279.11
2001	271.04
2002	309.73
2003	363.38
2004	409.72

Year	Average Price
2005	444.74
2006	603.46
2007	695.39
2008	871.96
2009	972.35
2010	1,224.53
2011	1,571.52

*Prices from 1833-1994, World Gold Council. Taken from Timothy Green's *Historical Gold Price Table*, London prices converted to U.S. Dollars.

77 **Prices from 1995-2008, Kitco.com, based on the London PM fix.

TABLE II on Gold Prices (2012-2019)

Year	Average Price in US $
2012	1664.00
2013	1201.50
2014	1199.25
2015	1060.20
2016	1151.70
2017	1296.50
2018	1281.65
2019	1495.38

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