

Iran's Threat To The Dollar

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As Iran prepares to celebrate its greatest holiday of the year tomorrow, it also celebrates the end of the dollar as an acceptable currency for payment of its oil. Essentially, it will look toward other currencies and commodities.

The charter of the Iranian oil bourse, a commodity exchange that opened in 2008, calls for the commercialization of petroleum and other byproducts in other currencies, primarily the euro, Iranian rial and a basket of other major currencies. Iran sits on one of the largest oil and gas reserves in the world, and it plans to develop an oil market that won't accept U.S. dollars. In fact, Iran has proposed the creation of a Petrochemical Exporting Countries Forum (PECF), aimed at financial and technological cooperation among members, as well as product pricing and policy making in production issues, not unlike those of the Organization of Petroleum Exporting Countries (OPEC).

This issue isn't new; in the last decade, some countries in Latin America, the most "dollarized" region in the world, began introducing measures toward internalizing the risks of "dollarization," developing capital markets in local currencies, and allowing for the de-dollarization of deposits, which all contribute to a decline in dollar-backed credit globally, predominantly in Latin America and the BRIC (Brazil, Russia, India and China) countries.

For several decades, the embracing of the dollar has been the primary source of financial vulnerability that triggered crises in BRIC countries, as well as in Colombia, Indonesia, Vietnam, Egypt, Turkey, and South Africa. The urge to "de-dollarize," or withdraw from U.S. Treasury bills and the dollar, is a direct result of foreign countries' mistrust in Washington's ability to control its massive budget deficits. This, in turn, arises from the fact that dollarization almost invariably undermines monetary policies conducted by foreign states' central banks, limiting their roles as lenders of last resort and creating revenue losses when they print and issue new currency. Foreign countries are realizing that often, dollarization makes them vulnerable to changes in U.S. currency policy.

Ever since President Obama signed one of the most severe sanction bills against Iran, that country appears determined to phase out the dollar as a form of payment for its oil and derived products. If Iran follows through with its decision, it may trigger intense reaction from Washington, especially for the dollar-reserve currency, mainly supported by Saudi Arabia's determination to accept only dollars for oil.

Despite the U.S.-Iran conflicts, the de-dollarization debate has heated up around the world. Is it a realistic global goal? Can Iran and other countries trigger a chain of events that would threaten the dollar's status as the world's premiere reserve currency? What would be the consequences to the U.S., and the world economy, if the dollar were to no longer be OPEC's measure of pricing oil? Certainly, we would no longer be able to brag about having the lowest gasoline prices. They would likely skyrocket, essentially increasing the prices of all other commodities, making life for Main Street more arduous.

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