

Flash Economics


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The power given to countries that issue an international currency should drive the euro zone and China to develop their currencies' international currency status

The example of the United States and the dollar illustrates the power given to a country that issues a dominant international currency: capacity to obtain extraterritoriality for this country's laws and decisions (sanctions); "exorbitant privilege" that makes it possible to finance the external and fiscal deficits without any difficulty.

For the euro zone, the development of the euro's international status would require creating synthetic euro-zone debt, if it cannot be a eurobond.

For China, the development of the renminbi's international status would require the development of financial assets in renminbi available for non-residents, which would require a shift from financing via bank credit to financing in financial markets.

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The power given to the United States by the dollar's reserve currency status

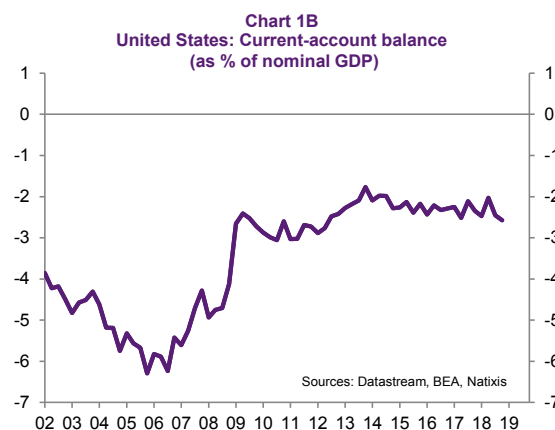
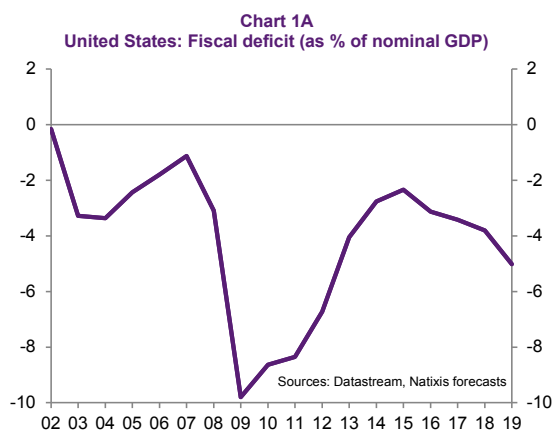
The dollar's dominant reserve currency status (Table 1) enables the United States to:

Table 1: Structure by currency of central banks' foreign exchange reserves (as %)

Year	U.S. dollars	Euros	Pound sterling	Yen	Swiss francs	Other currencies*	o/w			
							Australian dollar	Canadian Dollar	Renminbi	Other
2002	68.52	21.79	2.83	4.95	0.34	1.57	-	-	-	-
2003	66.18	24.74	2.66	4.35	0.23	1.84	-	-	-	-
2004	66.72	23.80	3.09	4.28	0.20	1.91	-	-	-	-
2005	65.89	24.37	3.73	4.12	0.15	1.76	-	-	-	-
2006	65.78	24.54	4.32	3.48	0.16	1.71	-	-	-	-
2007	64.43	25.58	4.75	3.08	0.16	1.99	-	-	-	-
2008	63.37	26.16	4.66	3.48	0.15	2.17	-	-	-	-
2009	62.88	27.26	4.20	2.96	0.12	2.58	-	-	-	-
2010	61.92	26.54	4.11	3.33	0.11	3.98	-	-	-	-
2011	61.37	25.87	3.96	3.66	0.15	4.99	-	-	-	-
2012	61.50	24.06	4.04	4.09	0.21	6.10	1.46	1.43	-	3.21
2013	61.76	23.81	3.90	3.84	0.26	6.44	1.71	1.76	-	2.97
2014	63.97	22.25	3.75	3.59	0.24	6.20	1.68	1.78	-	2.74
2015	65.64	19.71	4.43	3.66	0.27	6.28	1.64	1.77	-	2.77
2016 Q1	65.46	19.55	4.63	3.68	0.19	6.48	1.72	1.81	-	2.96
2016 Q2	65.22	19.41	4.54	4.10	0.18	6.55	1.70	1.83	-	3.02
2016 Q3	64.70	19.67	4.39	4.21	0.18	6.85	1.80	1.91	-	3.14
2016 Q4	65.36	19.14	4.34	3.96	0.17	7.04	1.69	1.94	1.07	2.34
2017 Q1	64.68	19.28	4.27	4.54	0.17	7.07	1.77	1.90	1.07	2.33
2017 Q2	63.83	19.95	4.41	4.63	0.17	6.99	1.75	1.93	1.07	2.24
2017 Q3	63.52	20.06	4.49	4.52	0.17	7.22	1.77	2.00	1.12	2.33
2017 Q4	62.72	20.16	4.53	4.90	0.18	7.50	1.80	2.03	1.23	2.44
2018 Q1	62.78	20.36	4.67	4.59	0.17	7.43	1.70	1.86	1.40	2.47
2018 Q2	62.39	20.25	4.47	4.86	0.16	7.86	1.70	1.90	1.83	2.42
2018 Q3	61.94	20.48	4.49	4.98	0.16	7.95	1.69	1.95	1.80	2.52
2018 Q4	61.69	20.69	4.43	5.20	0.15	7.84	1.62	1.84	1.89	2.48

Sources: IMF, Natixis

- Establish **extraterritoriality for US law**, which applies to all those who use the dollar;
- Ensure that the **sanctions** it takes against certain countries are efficient and applied by all;
- **Finance its fiscal and external deficits without any difficulty (Charts 1A and B).**



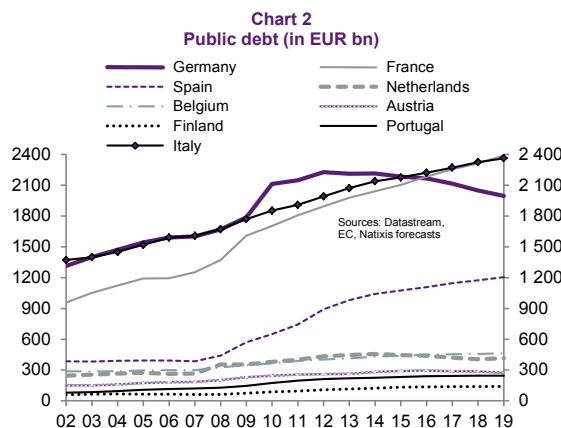
The dollar's international role is therefore an important factor of the United States' diplomatic and economic power.

The zone euro and China should therefore try to have a dominant reserve currency

The same desire for power should lead the euro zone and China to try to have a dominant international reserve currency, which is not the case currently (Table 1).

How could the euro zone and China achieve this objective?

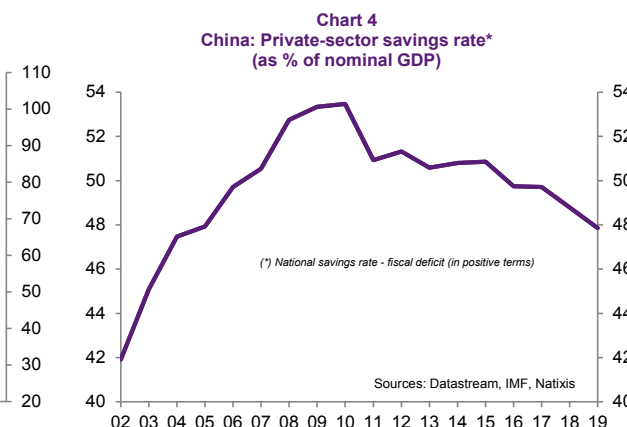
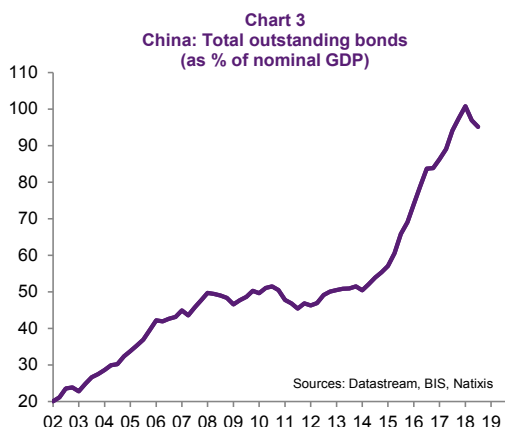
1. The euro zone's problem is the segmentation of public debt markets (Chart 2); each country's public debt has a different rating, a different interest rate, a different risk, and different liquidity.



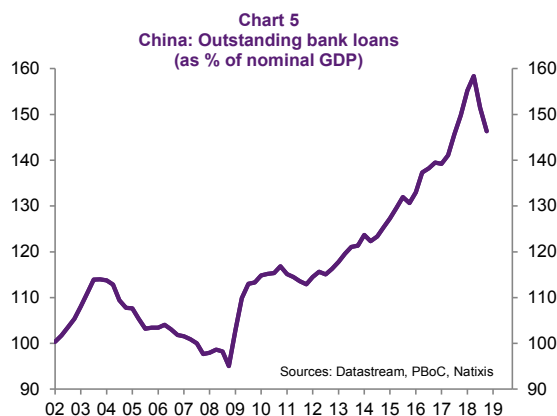
To increase international demand for euro-zone debt, a single debt of the euro zone as a whole would have to be created.

Since this cannot be eurobonds, which is rejected politically, it would have to be synthetic euro-zone debt based on individual countries' national debt.

2. China's problem is the small size of financial assets in renminbi available for non-residents (Chart 3), all the more as, due to the very high savings rate of the Chinese (Chart 4), these assets are held by domestic investors.



For the renminbi to become a large international reserve currency, the renminbi bond debt market would therefore have to be developed, which in particular would require replacing bank financing of companies and local authorities (Chart 5) with financial market financing.



Conclusion: A necessary strategy for the zone euro and China

To increase their economic political power, the euro zone and China should issue a large international reserve currency.

For the euro zone, this would require creating a unified euro-zone (possibly synthetic) debt; for China, to increase the amount of bond debt in renminbi available for non-residents, which would require replacing bank credit financing with bond financing.

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