

Review paper

UDC: 339.72

doi:10.5937/ekonhor1801075J

PERSPECTIVES OF THE INTERNATIONAL MONETARY SYSTEM

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During the 20th century, the dollar gained the status of the world's most important currency. Therefore, the Bretton Woods International Monetary System was based on the dollar. However, in the 1970s, the situation changed significantly - demand for dollars declined, the currencies of the most important European countries became convertible, the volume of international trade increased greatly, international capital flows were liberalized, the external convertibility of the dollar to gold was abolished, and the currencies began to fluctuate. In this way, the original Bretton Woods international monetary system ceased to exist. In addition to the changes, the functioning of the international monetary system is greatly impacted by the fact that the United States recorded an increasing amount of current account deficits from year to year and, in the 1980s, moved from the position of the net creditor to that of the net debtor, that the euro was created on the soil of the EU and that China became the world's largest exporter and one of the largest (if not the largest) world economies. For this reason, the theoretical assumptions of the international monetary system are systematized in the paper, the role of other world currencies is examined, and the question of why the dollar continues to be the dominant world currency is answered.

Keywords: Bretton Woods International Monetary System, dollar, euro, yuan, world currency

JEL Classification: F31, F32, F33, F62, F65

INTRODUCTION

The status of the world currency is not entirely defined by the relative size of the country and its presence in international markets. For this reason, although the United States surpassed Great Britain in size in the early phase of the 20th century, at that time the dollar failed to take over the leading currency role

from the pound sterling; however, this happened later (Goldberg, 2011). The Bretton Woods International Monetary System emerged after the Second World War, when it became clear that the former, in some way, self-regulating version of the gold standard could not last. Insufficient reserves to guarantee the convertibility of the total paper money to gold have in the meantime conditioned the emergence of the gold-bar and gold-foreign exchange standard. At the same time, the events during and after the First and the Second World Wars contributed to the United

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States becoming a military, economic, financial and technological power, so it should not be surprising that the dollar nevertheless became the most important world currency of the 20th century. The following two facts were crucial: there was hunger for dollars and there was the convertibility of dollars to gold. Simply, the dollar became the world money - the foreign exchange parity of other currencies was expressed in dollars, international payments were made in dollars, prices were invoiced in dollars, monetary reserves were kept in dollars, the savings were kept in dollars and the gold exchange system became the gold and dollar system.

However, already in the early 1970s, a lot changed - the currencies of the most important European countries became convertible, the volume of international trade increased multiple times, international capital flows were liberalized, the foreign convertibility of the dollar to gold was abolished, currencies started fluctuating - in a way, the original Bretton Woods International Monetary System ceased to exist. Nevertheless, in addition to all of these changed circumstances and the fact that the United States record an enormous foreign trade and budget deficit from year to year, the dollar continues to enjoy general confidence in the world and is accepted as a means of payment, account, and reserves. Thus, in the 21st century, the dollar remains (for now) the most important world currency. The question arises as to how this is possible when no one likes the dollar standard. Although many years have passed since the abandonment of the original Bretton Woods International Monetary System, no other has been officially established. It is considered necessary that certain reforms should be made - to create an international monetary system that will reduce the impact of the dollar and take into account all of the new changes in international economic relations. According to R. Triffin (1978), when it comes to the international monetary reform, there are two main approaches - a monetary reform at the world level and a regional monetary cooperation or integration. For now, the creation of some kind of world money seems unlikely - it is not known who would create it, nor is it known who would control it. Simply, there is no consensus at the global level. On the other hand, there are thoughts on the creation of a kind of multi-

currency international monetary system, where, owing to their position in the international economic order, the euro and the Chinese yuan should take their positions.

The aim of this paper is to clarify the theoretical assumptions about the existence of the Bretton Woods International Monetary System and to also point out the significance of the changes that have occurred in the meantime.

According to the abovementioned aim of the research, the following hypothesis can be singled out as crucial:

H: Despite the facts that there was the abolition of the foreign convertibility of the dollar to gold, that the euro was created as the common currency of the eurozone, and that China became the world's largest exporter, the dollar remains the most important world currency.

The qualitative methodology based on the study and descriptive analysis of the research problem will be used in the paper. The research study will examine the relevant foreign and domestic literature based on the theoretical generalizations and experiences of the authors who have dealt with the subject matter. Starting from the relevant literature, whether, in addition to all of the changed circumstances in the international monetary system, the dollar remains dominant, i.e. what is needed in order for other currencies (primarily the euro and the yuan) to create a multi-currency international monetary system, will be analyzed.

The rest of the paper is organized as follows: the most important characteristics of the original Bretton Woods International Monetary System will be discussed in the second part of the paper; the third part deals with the causes and consequences of the imbalance in the current accounts of certain countries; the fourth and the fifth parts examine the potential of the euro and the yuan as international currencies, while the sixth part is dedicated to the impact of globalization on the international monetary system. The drawn conclusions are presented in the seventh part.

THE ORIGINAL BRETTON WOODS INTERNATIONAL MONETARY SYSTEM

Classical economists argue that money has its three functions - it serves as a means of exchange, as a unit of account, and as a value guard. The role of international money is the same - it is used for settling international payments, fixing prices and is kept as liquid assets for international transactions. An additional dimension is provided by the difference in the behavior of the private sector and central banks. Based on the abovementioned, the dollar, as the most important international currency, can be said to perform six functions. The dollar as a means of exchange in the private sector represents the intermediary between the currencies, while with the purchase and sales by the central banks it represents the currency used for an intervention in the market. Trade agreements denominated in dollars represent the dollar as the invoice currency (in the private sector), while the central bank uses it to express a local currency in dollars (pegged it to the dollar - exchange rate). Finally, if viewed as a value guard, private individuals keep liquid assets denominated in dollars (some sort of a banking role), while central banks keep the dollar as a reserve currency (Krugman, 1984).

As long as there was a complete exchange of the dollar to gold, central banks accumulated dollar assets and the Bretton Woods Monetary System operated smoothly. Confidence in the US willingness to convert dollars to gold influenced an increase in the share of the dollar in foreign-exchange reserves. However, at the beginning of the 1960s, the problem of long-term confidence in the sustainability of such a system appeared. Due to an increase in the world central banks' dollar assets, the amount of dollar reserves surpassed the US gold reserves, which prevented the American Central Bank (FED) from repurchasing all of the dollars (if foreign central banks wanted to replace all of their dollar reserves with gold) (Kovačević, 2015). In this manner, the United States was forced to abolish the foreign convertibility of the dollar to gold, thus destroying one of the pillars of the original Bretton Woods International Monetary system. In the following period, it was a system that was increasingly gaining in trust - it was necessary

to believe in the stability of the dollar. As soon as there would be a disturbance, a crisis of confidence, such a system would no longer work properly. On the other hand, the significant use of the dollar is exactly what led to this instability of the system. The growing need for international liquidity was satisfied with an increasing amount of dollars, which remained outside the US, which, on the other hand, increased the US balance of payments problem. The cumulation of the US balance of payments deficit and the increase in foreigners' dollar receivables have led to reduced confidence in the dollar. Such a situation can be said to be one of the significant disadvantages of this established international monetary system (a "factory error", as some authors point out) - the currency of a country with a large (and increasing) deficit should enjoy general trust in the world and be accepted there as a means of payment, accounting, and reserves (Jovanović Gavrilović, 2012).

At that point, the question arose as to the position of the dollar after the end of dollar to gold convertibility, i.e. whether the dollar would remain to be the generally accepted currency and whether the US would continue to be able to finance the current account deficit without cover. However, the US used its influence over the OPEC countries (primarily Saudi Arabia) and committed them to sell oil exclusively in dollars. Instead of gold, oil ("black gold"), as the driver of the world economy and trade, has become the backbone of the modified international monetary system. Given the fact that there was no fixed link between oil and the dollar, the United States was allowed to lead a more loose fiscal policy, and due to the so-called Petrodollar standard, the dollar remained the most important world reserve currency (Filipović i Garić, 2014).

Some economists believe that a lack of the diversification of reserve currencies is the weakness and vulnerability of such an international monetary system, as this can lead to a lack of liquidity, excessive privileges, erroneous capital flows and the encouragement of a weak fiscal discipline in the countries whose currency is used as the reserve. However, according to others, the dominance of several currencies is good and the dominant

currencies provide high-quality and safe assets during a financial crisis. Nevertheless, regardless of these opposing attitudes, the global economy is becoming increasingly multipolar. Significant structural changes have supported this transformation - including the rapid expansion and the increased connection of the global economy and financial markets. In this context, the key question is whether the transformation of the global economy will result in a more diversified reserve currency system (Tovar & Nor, 2018)?

The conclusion is that there is a great paradox about the use of the dollar. Although no one likes the dollar standard, the dollar continues to be used. The country that fixes its exchange rate against the dollar will tend to intervene in the foreign exchange market in dollars and accumulate reserves in dollars. This country will choose the dollar for commercial and financial transactions, thus limiting the risk of a foreign exchange rate (Farhi, Gournchas & Rey, 2011). Despite the turbulence in markets around the world and significant fluctuations in the value of the dollar in the past period, the importance of the dollar has not significantly decreased (neither if used as a currency linked to the value of the domestic currency nor as an international reserve currency) (Goldberg, 2010). For this reason, the established procedures of clearing and the mechanism of international payments help the dollar to retain the position it gained in international trade. As the main monetary mechanism, it ensures that international trade remains in some way multilateral, rather than narrowly bilateral. Simply put, this system is still too valuable to be lost and too difficult to be replaced (McKinnon, 2013).

THE CAUSES AND CONSEQUENCES OF A LARGE IMBALANCE IN THE CURRENT ACCOUNTS OF CERTAIN COUNTRIES

The imbalance in the current account of certain countries is one of the key macroeconomic imbalances that significantly influenced the emergence of the last financial crisis. In most cases, the imbalance is concentrated in a small group of regions or countries, but the right picture is obtained if we look

at the countries concerned. Due to the size of its own economy, the US and the US current account deficit can pose a major problem for the sustainability of the existing system. There is no clearly defined limit of the sustainability of the current account deficit. Simply, someone's deficit will be sustainable as long as creditors have confidence in debtors. However, some economists believe that a current account deficit greater than 5% of the GDP is a problem. In 2006, the US current account deficit exceeded that limit and reached nearly 6% of the US GDP. At that time, the deficit accounted for about 75% of the current account surpluses of Germany, Japan, China and all of the world's other surplus countries (Obstfeld & Rogoff, 2005). By definition, a current account deficit (surplus) is equal to negative (positive) net savings. In this way, the global imbalance can be seen as the continuing financing of the US consumption by the net savings of the surplus countries.

The global imbalance has allowed global aggregate demand to keep pace with the rapid expansion of the global aggregate supply (primarily) due to the integration of China and India into the world economy (Adams & Park, 2009). In those years, the two most important things that affected the large US current account deficit were the increase in the US demand for foreign goods and the increase in foreign demand for US assets (Blanchard, Giavazzi & Sa, 2005). Many economists regard this kind of global inequality as unsustainable. It is considered that, if foreigners (governments and the private sector) cease to buy dollar assets for some reason, this may trigger a significant decline in the value of the dollar in foreign exchange markets and jeopardize the ability of the US to borrow from abroad. At the same time, although foreign central banks keep almost one-half of the outstanding US Treasury securities, the United States is one of the few countries that can borrow even more, because it borrows in its own currency and because it is immune to the usual risk faced by other debtor countries, whose debts are in a foreign currency. In addition, there is a possibility that the FED will print enough money to repay the debt (McKinnon, 2013).

Surprisingly, despite some political and economic disagreements with the United States, it can be

concluded that China has become more or less inadvertently the pillar of this established dollar standard. This assertion is reflected in the following (McKinnon, 2013):

- The snowball effect: The great expansion of Chinese trade with other emerging markets and countries producing primary products throughout the world, where the dollar is both the invoice currency for goods and the clearing currency for making international payments. This reduces transaction costs and increases the liquidity of dollar-based markets.
- The macro-stabilization effect: Since 1994, China has succeeded in following a countercyclical fiscal (credit) policy so as to stabilize its own GDP growth at a higher level, which somewhat buffers the cyclical instability emanating from the United States.
- The finance effect: China provides finance for the large US fiscal deficit. If, following China, foreigners collectively ceased to buy Treasury bonds and other dollar assets, a credit crisis in the United States would ensue.

There is no unanimous opinion about the impact of China on the world economy. While some economists

believe that China has already become the leading economic power, there are those who consider it is necessary for many years to pass so that, realistically speaking, the Chinese influence could be greater than (above all) the American. Certainly, China has become the largest creditor of the United States, and the following figures support the fact that in the 21st century, viewed through the relationship between the two countries, much has changed in terms of the redistribution of economic power in the world.

Figure 1 displays the movement of the GDP in the two countries between the years 2000 and 2017, measured in the current prices, according to the purchasing power parity. Although at the beginning of the observed period China's GDP was 2.7 times smaller than that of the US, in only 15 years China's GDP became larger, and in 2017, according to the IMF's estimates, this difference was almost 4,000 billion dollars. In the observed period, China's GDP grew 6.25 times, whereas America's GDP only grew 1.88 times. The only indicator that the US is still far ahead of China is the GDP *per capita* (also the current prices, according to the purchasing power parity) - Figure 2. According to the International Monetary Fund's (IMF) estimates in 2017, the GDP *per capita* in the United States was 59,495.34 dollars, and 16,624.41 dollars in China. Nevertheless, there

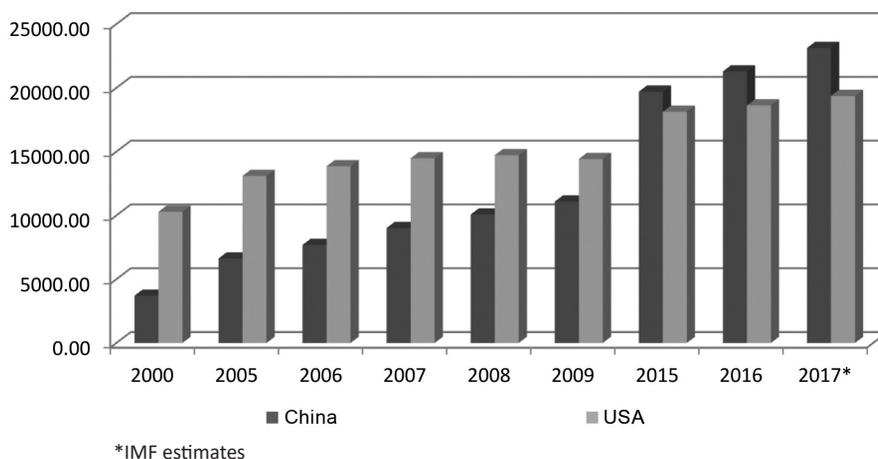


Figure 1 The GDP, the current prices, the PPP, in billions of dollars

Source: International Monetary Fund, 2017

is also a significant difference here when comparing the increase at the beginning of the observed period. The GDP *per capita* in China increased 5.7 times and in the United States there was only an increase of 1.63 times; so, the conclusion is that this difference is decreasing. Based on the above data, it is noticeable that the financial crisis had significant consequences for the US economy - there was a decline in these indicators in certain years in the United States, while China has been experiencing constant growth. Figure 3 best illustrates the aforementioned redistribution of economic power. The share of these two economies

in the global GDP increased (according to the IMF's estimates) in the observed period by over 5% and amounted to around 33.55%. However, this increase occurred as a result of a reduced share of the US GDP by more than 5% (from 20.62% to 15.29%) and a significant increase in the share of China's GDP of almost 11% (from 7.42% to 18.26%). In addition to the significantly high share of China's GDP, based on the above data, it can be concluded that there has been an increase in the concentration of economic power, so that the EU GDP, together with that of these two countries, represents about 50% of the world's GDP.

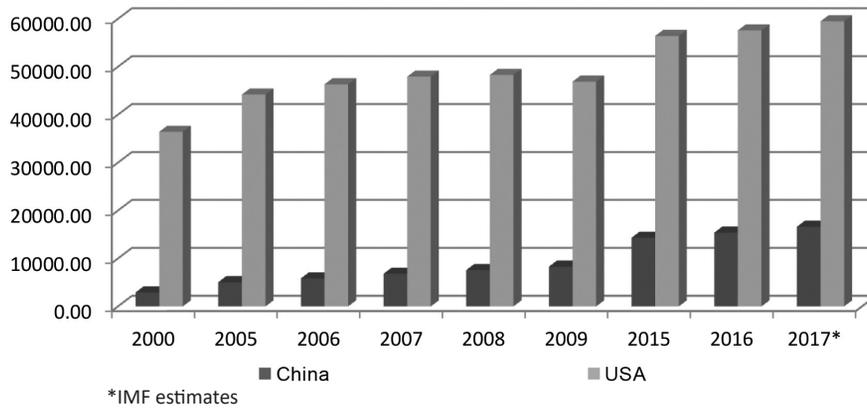


Figure 2 The GDP *per capita*, the current prices, the PPP, in dollars

Source: International Monetary Fund, 2017

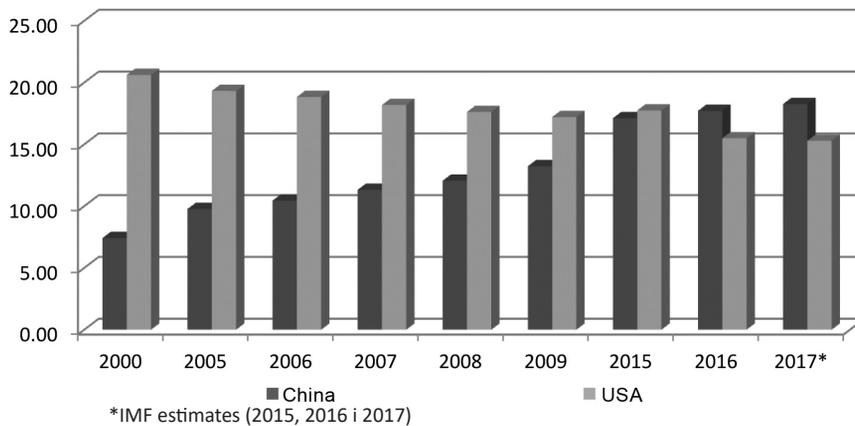


Figure 3 The GDP (PPP), the share in the world GDP

Source: International Monetary Fund, 2017

The following Figures 4, 5, 6 and 7 show why the abovementioned large imbalance in the current accounts of certain countries exists. Theoretically, in the long run, one country should spend as much as it produces, and invest as much as it saves. However, in practice, this is usually not the case, and therefore there are deficit countries and surplus countries. Due to the size of their economies, the US and China are very important representatives of these groups. In the observed period, investments in China amounted

to an average of 42.19% of the GDP, whereas in the United States they amounted to only 21.83% of the GDP. At the same time, in China, savings accounted for the GDP at an average of 47.23%, unlike those in the US, where this share was 17.05%. The asymmetric position of these two superpowers is obvious - China has a significant surplus for foreign investments (it invests most of it in the US Treasury securities), whereas the US investment activity largely depends on someone else's money. China invests most in the

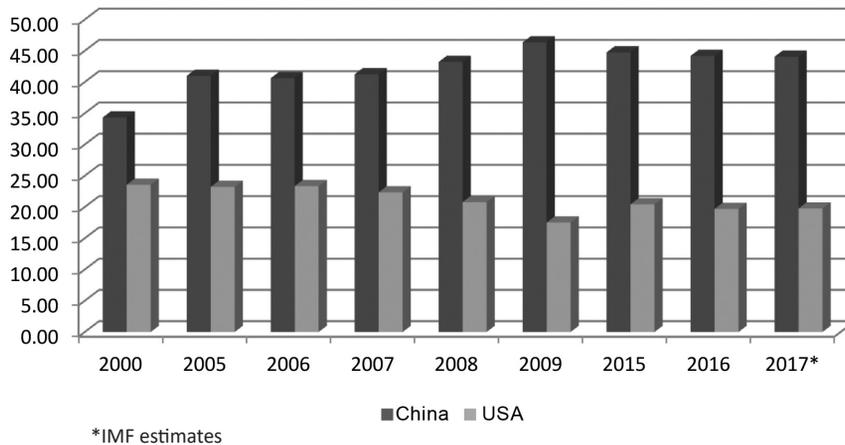


Figure 4 The total investments, in % of the GDP

Source: International Monetary Fund, 2017

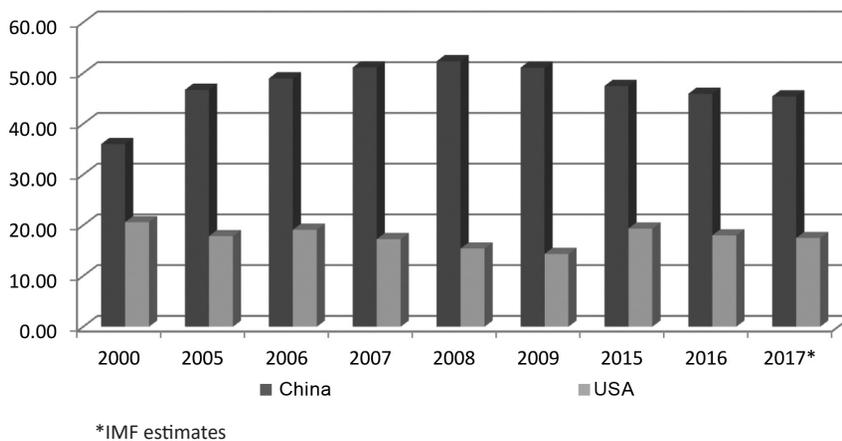


Figure 5 Gross national savings, in % of the GDP

Source: International Monetary Fund, 2017

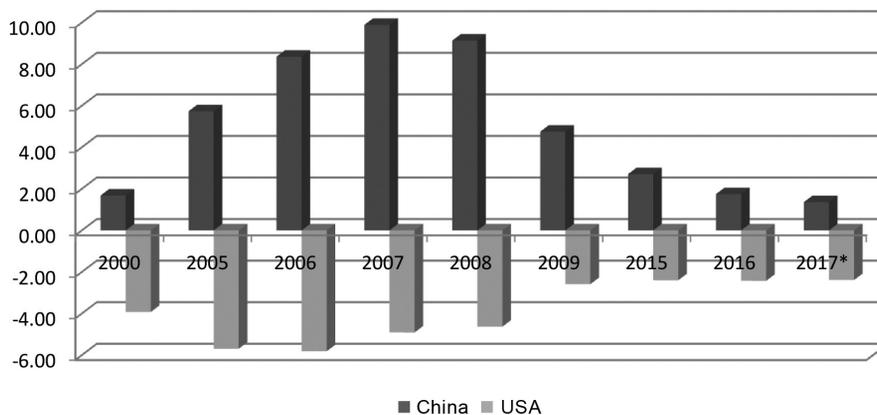
US financial market due to the dollar status and the fact that it is the most developed market in the world. This raises the liquidity of the market and reduces the level of the interest rate in the market. However, in this way, the consumption of the US economy is generated, which is largely compensated for by import from China. On the other hand, China increases demand for the dollar and leads to the appreciation of the dollar against the yuan, which makes the yuan even more underestimated, and China's exports to the US market even more competitive. Precisely this (un)proven underestimation of the yuan is one of the key points of the dispute between these two countries (Filipović i Garić, 2014).

The public debt of both countries has increased - it could be said to have doubled compared to the beginning of the observed period. However, the starting points were different - in 2001, the total public debt in China amounted to 24.38% of the GDP, and the IMF's estimates for 2017 amounted to 47.61% of the GDP. In the United States, the public debt amounted to 53.022% of the GDP in 2001, and as of 2012, it was over 100% of the GDP, and the estimates for 2017 amounted to 108.14% of the GDP (China has a significant share in this debt, of course). Thus, the above-stated fact that China is currently one of the world's largest investors and creditors of the US is confirmed. On the other hand, in the observed

period, the United States constantly consumed more than they produced, which is reflected in the current account deficit (Figure 6) and the net international investment position (Figure 7). Although the current account deficit after the global financial and economic crisis was reduced and amounted to about 2.5% of the GDP, in 2005 and 2006, the deficit was over 5% of the GDP, so the question of its sustainability could be raised. In particular so when we look at the absolute amount of the deficit - in those years, it was about 800 billion dollars. The data are even more important when the net international investment position of the US is included in the analysis. The US switched from the position of the international net creditor (in 1980, the net international investment position amounted to a maximum of 296.8 billion dollars) to the position of the international net debtor in 1989 (33.7 billion dollars). Since then, the US debt was rising steadily to reach a maximum of 8,318.4 billion dollars in 2016. Given the size of the US economy, the good thing is that, in relative terms, it is still not such a large amount (about 45% of the US GDP).

THE POTENTIAL OF THE EURO

The common European currency (the euro), introduced by 11 countries (currently 19), has been



*IMF estimates

Figure 6 The current account balance, in % of the GDP

Source: International Monetary Fund, 2017

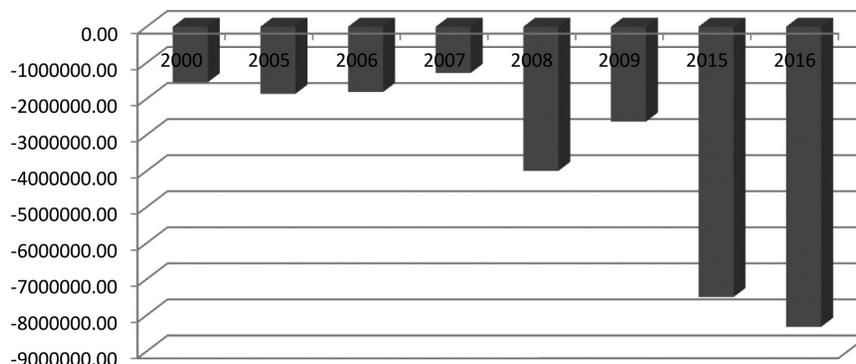


Figure 7 The net international investment position of the US, in millions of dollars

Source: Bureau of Economic Analysis, 2018

seen by its creators (and the wider economic public) as the currency that should stop and reduce the dollar's dominance as a world currency. The euro has taken its position in the international market and is the most important currency after the dollar. However, after all these crisis years, it has become obvious that the euro had been introduced before all the necessary conditions were met. During the introduction of the euro, its creators were probably aware of the fact that this was incomplete and a semi-solution. Namely, the greater economic and political integration of the eurozone countries should take place or its breakdown will occur. The introduction of the euro should not be the goal, but a means to achieve greater goals. It was considered that the introduction of the common currency would accelerate economic integration and prepare a favorable ground for deeper political integration; however, instead of that, there were opposite effects - the growth rates were not at a satisfactory level, the divisions still remain. If the *GDP per capita* is taken as one of the basic indicators of the economic progress of a country (or, in this case, of a group of countries), when it comes to the eurozone, the data are devastating - between 2007 and 2015, the decline in the real *GDP per capita* of 1.8% was recorded in the eurozone (simultaneously, there was an increase in the US by more than 3%, although the global financial and economic crisis emerged in the USA) (Štiglic, 2016). In addition, although the new Member

States recorded higher growth rates than the old member countries, a low starting point was the major problem; therefore, there is still the division between "the core" and "the periphery", "the west" and "the east", and "the north" and "the south". In addition to economic inequalities and the problems created by such a situation, there are disagreements on the other, very important issues that make the functioning of the EU, and especially the EMU, more difficult. Currently (the beginning of 2018), great pressure can be said to be created by the problems concerning the independence of Catalonia, the withdrawal of Great Britain from the EU, and the influx of migrants. The Great World Financial Crisis revealed certain weaknesses of the EMU, and for several years after that, the euro was losing its significance as a world currency. Only in 2016 was the recovery recorded and did the euro record an increase in the share in the total world foreign exchange reserves (according to the constant foreign exchange rate, after 6 years of reduction in the share (from 22.3% in 2009), in 2016 an increase (19.7%) was recorded compared to 2015 (19.4%) and global payments (from 29.4% of the share in 2015 to 31.3% in 2016) (ECB, 2017).

In order for the euro to continue to strengthen its role in the international monetary system, it is necessary to overcome the problems of the state debts of the peripheral member states, carry out

reforms, primarily in the fiscal field, and create sufficiently reliable assets (the euro bond) that will be able to match the depth of the US financial market. Investors continue to have great confidence in the US government bonds and because of their high liquidity and security they practically identify them with money, as the most liquid asset (Kovačević, 2011). Because of all of the abovementioned, Dž. Štiglic believes that, in order for the eurozone to survive, and later even further jeopardize the position of the dollar, it is necessary to carry out the structural reforms of the eurozone itself: to establish a banking union, consolidate the debt, create a common framework for stability, lead the right convergence policy that will lead to structural realignment, promote full employment and growth for the whole of Europe and have full commitment to common prosperity. The agreement on the banking union has been reached - in addition to joint supervision, it is necessary to have joint deposit insurance and joint problem solving (the same procedures for banks that cannot fulfill their obligations).

However, it is essential that a common regulatory system be set up in the right way - not to act as an automatic destabilizer, but to, with certain (greater) authorities and adequate instruments, stimulate expansion (limit lending) where necessary. Debt consolidation should also be approached cautiously. Any form of successful economic integration certainly implies some sort of assistance that stronger countries provide to the weaker (stronger member states must be aware of that).

In doing so, it is extremely important to properly use this consolidated debt - limit it if necessary, spend it on investment exclusively in certain parts of the economy (e.g. the infrastructure and education), and for any over-indebtedness to comply with the prescribed procedure. The fulfillment of the Maastricht criteria have proved insufficient to maintain the stability of the eurozone as a whole, so that the common framework for stability implies action in the following directions: the fundamental reform of the Maastricht convergence criteria (primarily through the creation of a common fiscal framework), a collective action for solving the basic problems through the Stabilization

Solidarity Fund, commitment to progressive automatic stabilizers, increasing the flexibility of the monetary policy, the introduction of regulations to control market-generated instabilities, and leading a stabilizing fiscal policy.

The real convergence policy involves the adoption of certain measures that will discourage countries from maintaining a surplus of current accounts. Achieving the current account balance for the region as a whole is not good enough. Individually, this can mean that there are countries with both a surplus and a deficit, which can lead to problems in time (primarily with respect to the financing of the deficit) so that the goal should be to prevent excessive imbalances within the eurozone. Full employment and continuing growth are the major problem for the eurozone. Change in the ECB's authorization is highlighted as the key macroeconomic reform that should enable a solution to this problem. Instead of only focusing on inflation, the ECB should, with its wider authorization, allow the financial sector to operate in the direction of crediting primarily productive parts of the economy, thus encouraging full employment, growth, and stability. Commitment to common prosperity means that we need to work on eliminating the growing inequality problem that is present everywhere in the world. The fact is that the economic, legal and political frameworks of the eurozone do not allow the mitigation of this problem. In other words, the free flow of goods and capital, without tax harmonization, reinforces the problem (Štiglic, 2016).

THE INTERNATIONALIZATION OF THE YUAN

The growing role of Asia in the world economy (primarily the position of China - the world's largest exporter and the dynamic growth of the Chinese economy) has contributed to the increase in the internationalization of the yuan and an attempt to reduce the impact of the dollar. As there were attempts in the 1980s and 1990s to internationalize the yen, it is considered that in the 21st century China has taken certain steps leading to the gradual

internationalization of the yuan. The National Bank of China sees the complete convertibility of the yuan as a process consisting of three steps:

- the yuan as a global trading currency - as the yuan develops as a trading currency, companies outside China will gradually become used to using it for paying for goods and services;
- the yuan as a global investment currency - the goal is to allow more free investment of the yuan. Investors will be able to use their reserves in the yuan across the border. Global companies want their earnings in China to be convertible to other currencies;
- the yuan as a global reserve currency - the government wants the status of its currency to match the position of the country that is becoming an economic leader.

In a way, China wants to challenge the dollar as a reserve currency (Love and Chen, 2017). Although the complete internationalization of the yuan is probably still far away (the question arises as to whether China wants this now and how long should it take this to achieve), it is certain that what has been done is changing the situation on the international scene. The growing role of the yuan is primarily reflected in the fact that exporters can invoice the goods they sell in the yuan, gradually opening the gate for a foreign capital inflow (the yuan is used for the calculation of investments through offshore zones), bilateral swap arrangements in the yuan are created with the central banks of the main trading partners, enabling the calculation and payment in the yuan in mutual trade and spreading the circle of currencies which the yuan is directly exchanged for without the intermediation of the dollar (Kovačević, 2014).

In the last two years, two very important things have happened, both in favor of the internationalization of the yuan - the International Monetary Fund has included the yuan into the basket of the currencies that determine the value of special drawing rights and the European Central Bank, as one of the most powerful central banks in the world, has invested a certain portion of its foreign exchange reserves in the yuan, selling a small portion of dollar receivables. It is part

of the ECB's strategy to diversify its foreign exchange reserves and add China's currency. Although this investment represented only about 1% of their total foreign exchange reserves (of around 68 billion euros), and the dollar still makes up the majority of the foreign exchange reserves of this institution, this was the major incentive for China. This points to the growing confidence in the yuan market as a world reserve currency and the acceptance of China as a global economic power in Europe. For this reason, the yuan is accepted by an increasingly greater number of countries as a reserve currency. However, this still does not mean that the yuan will become the dominant reserve currency instead of the dollar (even the euro) in a near future (Figure 8). As an accounting unit, it is used for about 2% of international payments, although the share of China's GDP in the world in the last few years has been much higher and has amounted to over 17%. Although the largest trader in the world, China only accounts for 20% of its foreign trade in the yuan, which is much less than about 60% of the eurozone foreign trade in euros, or about 40% of Japan's foreign trade in the yen (Huang, 2017).

The international role of the yuan is considered to still be limited in comparison with the dollar and the euro. The further internationalization of the yuan will depend on whether China will succeed in diverting the economy from investment to consumption in order to avoid a medium-income trap. In addition, the still-present restrictions in the capital account diminish the attractiveness of the yuan for foreign investors (Kovačević, 2015).

The full convertibility of the yuan, i.e. its being a reserve currency to a proper extent, requires further work in the following areas: maintaining economic stability in terms of stable economic growth, a stable exchange rate, and a low inflation rate. China is increasing its share in world trade and an increase in the size of its national economy is important to its trading partners, which clearly justifies a greater use of the yuan; deepening capital markets and accelerating the integration of its own and offshore capital markets; increasing efforts to create solid and reliable legal and regulatory frameworks. The internationalization of the yuan is a decisive goal of the national policy

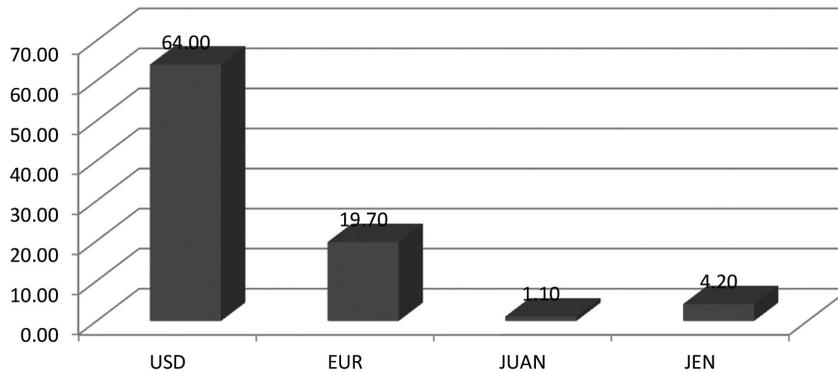


Figure 8 The percentage share of the most important currencies in the world foreign exchange reserves, 2016.

Source: ECB, 2017

of China's government, which is taking place at a faster pace than expected. In the upcoming period, the improved industry infrastructure, reinforced financial regulations, well-structured deposit insurance schemes, improved market-driven exit mechanisms for financial institutions etc. (Huang, 2017) should be expected.

THE IMPACT OF GLOBALIZATION ON THE INTERNATIONAL MONETARY SYSTEM

Over the past half-century, globalization has had a significant (primarily positive) impact on people's lives. The problem is that the resulting gains are not evenly distributed at either the regional or the national level. Over time, an increase in international trade and financial openness has happened in parallel. On the one hand, financial connections in the form of international payments and loans have greatly facilitated trade, whereas at the same time the accumulation of international assets and liabilities has occurred. All of this has made the countries that are more open-minded become more financially open. The relationship between real and financial openness developed with the degree of integration and development. In this context, we can speak of the three phases of globalization so far. The first, the most basic phase involved trade in goods and finished products and correspondingly

simple international financial links, such as cross-border payments. The second phase involved more complex trade and financial links. It involved trade in semi-finished products and services, linked to the fragmentation of production between the countries that was led by efficiency and with the corresponding financial arrangements. The third phase concerned the increasing use of financial transactions to actively manage balance sheet positions. All of the three phases of globalization share some common elements. One of them is the use of the world currency.

As the dominant world currency, the dollar is used for the denomination of not just about one-half of the world trade, but also about one-half of global cross-border banking receivables and over 60% of the foreign currency assets of central banks, as well as over 90% of transactions in the foreign exchange market. As a result, the dollar continues to play the key role in determining global financial conditions. Globally active financial institutions are another common element. They function in many countries, across continents. Due to their international presence and sophistication, they facilitate the transfer of funds and financial risks at a global level. The balances managed at a consolidated level create close international financial links (Bank for International Settlements, 2017). The major problem is the growing separation between the real and the financial sectors, significantly higher turnover in financial markets and an insufficiently good regulation at the global

level. On the one hand, new financial instruments and significant financial transactions enable easier financing, whereas on the other hand, this leads to a faster transfer of problems between certain parts of the market.

In addition to all of the foregoing changes that occurred in the international financial market, according to the data of 2016, the dollar remains the world's most important currency (Figure 9). Although it has managed to rank the second, the euro, as the unique European currency, has not yet created a major synergy effect and is still too far behind the dollar. On the other hand, as far as the Asian block is concerned, it is notable that there is no unity (the yen is still present), the internationalization of the yuan has only recently started and it needs time to pass for China's yuan to achieve a more significant share.

CONCLUSION

Globalization, present in all segments of society, greatly influences the significant spillovers of the monetary policy effects between countries. For this reason, the strengthening of international cooperation, as well as the occasional joint actions of monetary authorities, has become inevitable. The important question of how the international

monetary system will develop in the coming period remains. Will the euro and the yuan be able to expand their influence? Will this be a sustainable process and will this happen by reducing the impact of the dollar? In addition, some new instruments, such as virtual currencies (primarily bitcoins), can also be a form of a challenge in the upcoming period.

At present, the dollar can be said to still have the two major advantages when retaining the central role in the international monetary system is concerned (even if China's economy is considered to be larger than America's). The first advantage is that the existence of single dominant international money is considered as a natural monopoly and that the introduction of the second or third reserve currency would raise the administrative costs of making international payments between different countries around the world. Second, there is a great advantage for the national currency that already has the status of an international currency. When most banks in private transactions use the dollar as an intermediate currency in exchange for a second and third currency, transaction costs decrease in these markets and their liquidity increases as well. With this decrease in costs, the remaining banks are attracted to using the dollar (McKinnon, 2013).

As far as Europe is concerned, it must act collectively in order to move forward (and as quickly as possible).

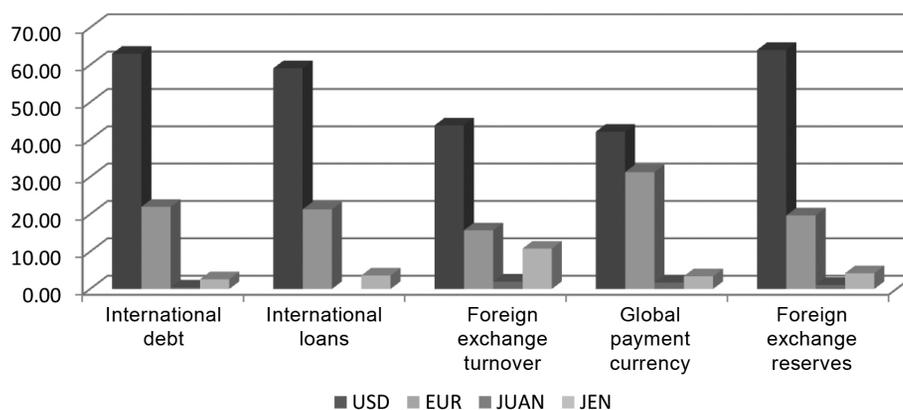


Figure 9 The percentage share of the most important currencies in the international monetary system, 2016.

Source: ECB, 2017

The goal is for the EU as a whole to be greater than the sum of its parts (individual countries) in economic, social, technological, commercial and political terms. The euro as a common currency, or the EMU, can be very important on this path. However, in order for this to happen, serious economic and political reforms are necessary.

China's yuan is obviously increasing its international impact, especially among the BRICS countries. In spite of that, we still cannot speak of an Asian block linked to the yuan. However, some kind of the transition of the international monetary system from the bipolar (the US dollar and the euro) to the tripolar currency block (including the yuan) is obviously in progress.

In addition to the fact that a lot has changed since the beginning of the Bretton Woods International Monetary System and that it is constantly criticized for the significant benefits that the United States has for the reason of the fact that the dollar has the key role in the international monetary system and global liquidity, it is concluded that the position of the dollar as the most important world currency has not yet been endangered, which confirms the established hypothesis. The liquidity, reliability and depth of the US financial market continue to put the US government securities at the forefront. Although developing countries and countries in transition increase the amount of foreign exchange reserves (as a response to the increasingly more frequent crises and a faster transfer of these crises) and want to make the currency diversification of their assets, the above presented facts enable the dollar to retain the position of the dominant currency of the world's foreign exchange reserves (Kovačević, 2014). Although the US current account deficit is large and there is the so-called "factory error" when the dollar is concerned (having confidence in the currency of a country that has a huge current account deficit), a conclusion can be drawn that the position of the dollar does not depend on the abovementioned deficit as much as it does on the fact that no other currency is still significantly increasing its share in the international financial market.

ACKNOWLEDGEMENT

This paper is part of the Integrated and Interdisciplinary Research Project (No. III 47005), funded by the Ministry of Education, Science and Technological Development of the Republic of Serbia.

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Received on 16th March 2018,
after revision,
accepted for publication on 23rd April 2018.

Published online on 26th April 2018.

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