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We will start with Jeffrey.

Jeffrey FRIEDEN

Great, thank you John. As John has pointed out, the dollar maintains its dominance in international monetary relations, international trade and payments, and there are a variety of reasons, many of which John mentioned. It is due to its historical reserve currency role, it is due to its usefulness as a vehicle currency for international trade and payments, it is due to network externalities so that the more people use the dollar the greater the incentive to use the dollar. However, I am going to focus on a somewhat different angle, I hope within my comparative advantage as a political economist rather than an economist, which is that it also depends on features of America's domestic monetary and financial conditions. The expectation of monetary stability in the US, the expectation of a commitment to low inflation, the expectation of a broad, deep, and stable financial market, and the expectation of a high level of financial and commercial openness have all been important to the international role of the dollar. The dollar relies upon the expectation that American monetary and financial authorities stand behind both the value of the currency and the openness of America's financial market.

All of these are highly political. Dollar dominance has rested in large part on the expectation that the American political order would protect and defend the real value of the US currency, along with the stability and openness of its financial system. Theory and history both tell us that these are central to the international role of any currency, including the dollar. I think that this focus on the importance of the political support for monetary stability, for an open financial system, and for financial stability helps explain the difficulties of the euro, given the unsettled nature of the politics of money and finance within the Eurozone, and the difficulties of the RMB, given the non-transparent nature of politics in China and significant doubts about the stability of the country's financial institutions. It is the domestic political will of the American authorities that I think in many ways stands behind the willingness of people around the world to continue to use the dollar.

Now, for the first time since the 1930s there are some significant questions being raised about the extent to which the United States is in fact committed to the core principles that have underpinned the international role of the Dollar. This is worrying for anyone who is concerned both about the Dollar, but more generally about the international monetary and financial system. We have a historical precedent. In the 1920s and early 1930s the US was the world's largest lender, the world's largest foreign direct investor, the world's largest trading nation. It was also deeply committed to isolationism and deeply hostile to international economic cooperation.

The weakness of the international monetary, commercial, financial order of the interwar period stems in large part from the fact that its most important player was un-involved politically and in many ways hostile to international cooperation. I am sorry to say that it looks like the US has gone back in that direction, and there are indications that it may continue to move in that direction.

This leads us to your final question, which is whether the international monetary system can go on if confidence in American political stability, and American economic and financial leadership, erodes, and if fears about the politicization of the payment system grow. My answer would be that it can go on. We have a very small bit of a precedent, the Cold War. During the Cold War the Soviets and their allies were concerned about the politicization of the payment system, so they began parking their Dollar reserves in London banks to protect them from potential seizure by the American authorities. The result was the Euromarkets, the offshore markets, which have become the basic form of contemporary international finance. There are workarounds that people can come up with on the payments side. However, if this is going to be a longer-term phenomenon that involves an American withdrawal from



its leadership position, or making its leadership contingent on playing by American rules, this will present a problem for the other members of the OECD.

Other members of the G7 or G20 could, if they wanted to, create both a financial system and a payment system that bypassed the US. It would be costly, it would be difficult, but it is doable. In my view, however, it is not a good thing. We would lose a substantial amount of the scale and history of stability that we tend to associate with the US Dollar.

Nonetheless, we have to take stock of what has been happening in the US. What if the reality of American politics continues to give us a United States that is unreliable, populist, economically nationalistic, geopolitically aggressive? Then I think the world has no choice but to move forward without the US. As an American, I am very sorry to say that the probability that the US continues to move in this direction is not zero.