GlobalResearch
Center for Research on Globalization

China-Ruble Settlement and the Dollar System

By F. William Engdahl
Global Research, October 24, 2017

Region: Asia, Russia and FSU, USA
Theme: Global Economy, Intelligence

The Peoples' Bank of China has just announced a payment-versus-payment (PVP) system for Russian ruble and Chinese yuan transactions. The stated aim is to reduce currency risks in their trade. The only conceivable risk would be from the US dollar and potential acts of US Treasury financial warfare to damage Russian-Chinese trade which is becoming very significant in volume and value. By December it should reach $80 billion, a 30% rise over 2016. Yet there is more to this seeming technical move by China and Russia than meets the eye.

The official announcement, posted on the website of the China Foreign Exchange Trade System (CFETS) adds the enormously significant note that CFETS plans to introduce similar PVP systems for yuan transactions with other currencies based on China's Belt and Road initiative.

This confirms what I discussed in an article I posted in April 2016, namely that the grand design behind China's Belt, Road Initiative (BRI) has an integral gold-based currency component that could change the global balance of power in favor of the nations of Eurasia, from Russia and the nations of the Eurasian Economic Union to China and across all Asia.

Earlier termed the New Economic Silk Road, the BRI is a vast network of high-speed rail linkages being constructed criss-crossing the countries of Eurasia including Central Asia, Mongolia, Pakistan, Kazakhstan and, of course, the Russian Federation and extending to Iran, potentially to Turkey and East Africa. Altogether at present some 67 countries are participating or have asked to join the ambitious project whose total cost could run into trillions of dollars and will transform global trade. HSBC estimates that the BRI infrastructure project, which today encompasses countries generating almost one-third of global GDP, will generate an additional $2.5 trillion worth of new trade annually This isn't chump change for the world economy. It's a game-changer of the first order.

Building a dollar reserve currency

Academic presentations of currency theory and of reserve currency theory tends to be boring beyond at least my patience. This direct currency settlement move by China and Russian, however, is one of the most dynamic game-changing developments since Washington's Treasury and Wall Street banks came up with the US Dollar system at Bretton Woods in 1944.

It's not about reducing currency risks in trade between Russia and China. Their trade in own currencies, bypassing the dollar, is already significant since the US sanctioned Russia in 2014—a very foolish move by the Obama Administration Treasury. It's about creating a vast new alternative reserve currency zone or zones independent of the dollar.

The American Century domination that Time-Life publisher Henry Luce proclaimed in 1941 came into being at the end of the war. In 1945, as the bombs stopped falling over Europe and Japan, President Harry Truman made clear to England that there would be no place for the British Empire as a rival, cancelling US Lend-Lease credits and demanding bankrupt Britain repay its war debts to Washington, as well as demanding a dramatic reduction in world trade conducted in Pound Sterling, then still about 50% of total world trade. The British based their hopes of rebuilding their Empire on their Commonwealth and its Sterling Preference trade region.

For Washington and Wall Street after 1945 there was room for only one dominant monetary power, the United States. Britain was forced to swallow its huge arrogant pride and turn to the newly-created International Monetary Fund and to, step-by-step, dismantle the colonies of the British Empire beginning with India for financial reasons. That opened the door for the dollar hegemony over the world economy outside the communist countries. Since 1945 the power of the United States as global superpower has rested on two pillars—the most powerful military and the dollar as undisputed world reserve currency allowing Washington to control the world economy.

In 1944 the Federal Reserve held over 70% of world monetary gold as part of its reserves. Every other currency was pegged to the dollar. The dollar alone was fixed to gold. A dollar-hungry postwar world in the 1950s desperately needed dollars to finance reconstruction. The dollar began its ascent as the currency held by world central banks as reserve currency or anchor currency, helped by the fact that OPEC countries agreed to sell their oil only for dollars. Most world trade financing was done in dollars.

Nixon and the Great Dollar Inflation

Under Bretton Woods, the US Federal Reserve guaranteed that other countries holding dollar reserves could exchange them for US Federal Reserve gold at any time. By the end of the 1960's that began to break down as France and other countries demanded gold in exchange for what they saw as inflated US dollars. US industry was rusting from lack of new investment and US Federal deficits were soaring because of the Vietnam War. Other nations were no longer willing to accept that the "dollar was as good as gold." They demanded the gold, not "as good as."

After the "Nixon Shock" when President Nixon tore up the Bretton Woods Agreement in August 1971 to let the dollar float, free of any redemption in gold, the world had little choice but to accept inflated paper dollars, an inflation that soared with the 1973 oil price shock engineered by Secretary of State Henry Kissinger, and the Rockefeller faction in US politics. The gold-dollar convertibility suspension was a Washington reaction to the fact the central banks of France, Germany and other OECD countries demanded more and more hard gold from the Fed for their paper dollars and US gold reserves were in danger of being depleted.

Here began the roots of the most extraordinary global great inflation in history. Beginning the US budget deficits during the Vietnam War in the 1970s and the 400% oil price rise by 1974, a price that Washington's Treasury in a secret deal with Saudi Arabia in 1974-75 insured would be paid by the rest of the world in dollars, the world dollar supply grew astronomically. Dollars in global circulation, no longer redeemable in gold, rose by 2,000% between 1971 and 2015. Production of real goods did not rise anywhere near 2,000%.

The fact that the dollar remains the most significant foreign central bank reserve currency, still some 64% of all world reserves at present, with the Euro at 20% the closest rival, gives the US Government an extraordinary advantage.

Since 1971, the US has run budget deficits for 41 of the past 45 years, the sole exception being four years in the 1990's when the Baby Boom generation reached peak income and peak Social Security Trust Fund tax payment. The Clinton Treasury made an accounting manipulation to count this one-off effect as general Treasury tax income, a fraud. Every other year since 2001 the US Budget has resumed huge deficits, exceeding $1.4 trillion in 2009 alone, as in $1,400 billion, during the financial crisis that began in 2008. In 2000, before the dollar break with gold, the US deficit was $3 billion.

Rightly so, other countries see this as an enormous disadvantage. Their US dollar Treasury bond investments for their own central bank reserves are becoming worthless paper. Because they are more or less forced to invest the trade surplus dollars earned from their exports in secure US Treasury bonds or bills or similar US securities, the annual inflow of China central bank dollars—of Japanese trade surplus dollars, of Russian dollars before 2014, of German and other trade surplus countries—allows the US Treasury to keep interest rates abnormally low. That also allows Washington to finance those deficits with no major stress. This year the US deficit reached an impressive $585 billion.

In effect, China and Russia in recent years finance the US military budget by buying US bonds and bills that allow the Treasury to finance that deficit without raising interest rates. The cynical irony is that that US military budget financed by Russia and China's need to hold dollar reserves against potential currency wars by Washington as was done against Russia after 2014, is aimed at controlling Russia and China, and ultimately at destroying their economies.

If the Trump tax cut legislation now becomes law, the US deficits will hit the moon. This is the backdrop to better understand what China and Russia and allied countries are preparing in order to reduce their vulnerability to what is on a ballistic trajectory to a bankrupt global dollar reserve system. If China, Russia, and other allied countries of Eurasia, most especially countries of the Shanghai Cooperation Organization and prospective members such as Iran and Turkey turn to bilateral arrangements like China and Russia to settle trade, bypassing the US dollar, the dollar as world reserve currency domina will fall, and other currencies will replace it. The Chinese Yuan is the leading candidate. The Ruble as well.

Yuan Reserve Status

The newest move to a direct settlement of bilateral trade between China and Russia with other countries along the new Silk Road being brought into the system is a major foundation stone in creation of a viable alternative to the US dollar as an anchor reserve currency.

A decade ago such an idea was dismissed by Western economists as preposterous. They claimed it would be decades before the world would accept the Yuan as a reserve. The yuan was not convertible.

In 2016 China was admitted by the International Monetary Fund as one of the five leading currency components of IMF Special Drawing Rights calculated in a currency basket. That step gave the yuan a major boost in international acceptance.

Before 2004 the yuan was not allowed outside China. Since that time the Chinese monetary authorities have laid a careful foundation for internationalization of the yuan. According to the Society for Worldwide Interbank Financial Telecommunication (SWIFT), RMB internationalization is taking place in three phases—first as use for trade finance, then for investment, and long term as reserve currency. Now that "long term" is looking remarkably short-term as China exceeds all conventional economists' expectations with internationalization of its yuan. This prospect of the yuan becoming a global anchor or reserve currency exceeding the share of the Euro in the next few years is what has the US Treasury, the Federal Reserve and Wall Street banks alarmed, to put it mildly.

In a 2016 report the HSBC bank reported that since 2012 the Yuan RMB has become the world's fifth most widely used payment currency.

Two years ago, in October 2015, China initiated the China International Payments System (CIPS). While it has signed a cooperation agreement with the dominant SWIFT, it gives a potential option in event of US sanctions on China to function independent of SWIFT. In 2012 Washington pressure on the private Belgian-based SWIFT international bank clearing system, through which virtually every international transaction between banking institutions goes, to block international clearing for all Iranian banks, froze $100 billion in Iranian assets overseas and crippled her ability to export oil. The point was not missed in either Beijing or in Moscow, especially when some foolish US Congressmen called for SWIFT exclusion against the Russian banks after 2014.

In March of this year, Elvira Nabiullina, Governor of Russia's central bank, stated:

> "We have finished working on our own payment system, and if something happens, all operations in SWIFT format will work inside the country. We have created an alternative."

Creating the new currency architecture

The financial demands of China's vast Belt Road Initiative reach into the trillions of dollars. Alone in Asia the Asia Development Bank estimates investment of $8 trillion is needed over the coming years to lift those economies into efficient growth. Beijing's founding of the Asian Infrastructure Investment Bank (AIIB) last year was a major step towards securing international financing for the BRI project.

In April 2016 China announced its decision to establish the Shanghai Gold Exchange, under the Peoples' Bank of China, as a major international center for the pricing of gold and gold trading in yuan, with settlement in physical gold between bullion banks, refiners, producers and trading houses. Added to this is China's decision to launch a daily yuan-denominated price fix on gold that could ultimately displace the dominant London gold fix, a system that has been accused of manipulating world gold prices downward for years.

In announcing its Belt Road Initiative the Chinese government, in a little-noticed comment, declared that the routes of its high-speed railway projects through the countries of Eurasia will connect now remote, inaccessible regions known to have large unmined gold reserves, to the world markets via the BRI.

What China with Russia are doing is not about attacking the US dollar to destroy it. That is highly unlikely and would benefit no one. It's rather about creating an independent alternative reserve currency for other nations wanting to protect themselves from the ever-more frequent financial attacks by the US Treasury and Wall Street banks and hedge funds. It is about building a crucial element of national sovereignty because the dollar system today is being used to ravage the economic sovereignty of the rest of the world. As Henry Kissinger allegedly said during the 1970's,

> "If you control the money you control the entire world."

The statement by the Chinese government now that its China-Russia direct payment-versus-payment settlement system will be extended to other countries of the BRI adds another brick in the careful building up of this alternative monetary system, a gold-backed alternative, independent of the politically-explosive US dollar system, that could insulate the nations of Eurasia from Washington and EU financial warfare in the coming years.

This is what has Washington in a dither. Their options are fading by the day. Military, financial, cyberwarfare, color revolution–all are increasingly impotent from a country that allowed its own industrial and manpower base to be destroyed in the interest of a financial oligarchy. That was how the Roman Empire collapsed in the Fourth Century, as did the British between 1914 and 11945, and as did every empire in history based on debt slavery.

F. William Engdahl is strategic risk consultant and lecturer, he holds a degree in politics from Princeton University and is a best-selling author on oil and geopolitics, exclusively for the online magazine "New Eastern Outlook."

This article was originally published by New Eastern Outlook where the image was sourced.