

Collapse of the Petrodollar Looming

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The announcement by President Putin of a Russian bourse trading oil and gas in Roubles threatens the stability of the US Dollar far more than Iran's bourse alone would do, and continues the slide in relations between the old Cold War foes.

In his annual State of the Nation address to both houses of parliament on 10 May 2006, [Novosti reports](#) President Putin said that work on making the Rouble an internationally convertible currency would be completed by 1 July 2006, six months ahead of schedule. To promote the currency, he announced that an oil and gas stock exchange will be created in Russia, that would trade in Roubles.

"The rouble must become a more widespread means of international transactions. To this end, we need to open a stock exchange in Russia to trade in oil, gas, and other goods to be paid for in roubles." – Putin

Russia's oil exports represent 15.2% of the world's export trade in oil, making it a much more significant player than Iran, with 5.8% of export volumes. Russia also produces 25.8% of the world's gas exports, while Iran is still only entering this market as an exporter.

[GlobeAndMail.com is reporting](#) that President Chavez of Venezuela is considering following Iran's move towards pricing oil in Euros. Venezuela has 5.4% of the export market, although since the bulk of his country's exports are of heavy oil to the US, where it needs special facilities to process it, it would be a very brave or foolhardy President that told the US to buy its oil in Euros, or else ... Nevertheless, you can see the attraction for any country wanting to apply some pressure on the world's superpower. And where Venezuela leads, Bolivia may not be far behind. You can see how this could quickly get out of control.

While the Iranians have been suffering numerous delays in implementing their bourse, Russia could have their oil market up and running almost as soon as their currency market is ready to take on the work load, which might only be a few months away.

Some commentators on the Iranian proposal have suggested that the impact on the US Dollar would not be so great because the greenback is used for all sorts of trade, not just oil, so 5.8% of the international oil trade is really only a small part of the bigger picture. This argument looks a bit weak if both Russia and Iran will be lowering the demand for Dollars to buy oil and gas.

In order to counter the reduced demand for US Dollars, the standard control lever available to the Federal Reserve is to increase interest rates, over and above what it was going to be doing. This has the usual unwelcome consequences of dampening the US economy, and squeezing people with mortgages, which in turn leads to rising wages, falling house prices and a slump in the construction industry.

At the same time, lower demand for Dollars will weaken its conversion rate, making imports more expensive. With rising wages, fuel bills and debt-servicing feeding through into prices for home-produced goods, the stage is set for either an inflationary spiral or a recession. In the short term, the inflationary route always looks to be the less painful, but it can only lead eventually to a crisis of confidence in US Dollars, when traders abandon the paper and rush for the exit.

US-Russian relations slide

It cannot have escaped the notice of the Russians that this announcement is a poke in the eye for the US. So its timing can hardly be an accident, coming less than a week after US Vice President Dick Cheney's address to a conference in Vilnius, Lithuania, where he attacked Russian energy policy, in front of an audience of European heads of state.

"No legitimate interest is served when oil and gas become tools of intimidation or blackmail, either by supply manipulation, or attempts to monopolise transportation", Cheney said, referring to the Ukrainian gas cut-back (that Ukraine provocatively passed on to the downstream customers in western Europe). The next day Russian Foreign Minister Sergei Lavrov fired back "[the] U.S. vice president should be informed that for the last 40 years neither the U.S.S.R. nor the Russian Federation has ever broken a single contract for oil and gas supplies abroad."

The antagonism continued to verberate when Lavrov met US Secretary of State Condoleezza Rice at a foreign ministers' summit in New York on Iran's nuclear programme. As well as criticising Cheney's comments, Lavrov also attacked Rice's number three, Nicholas Burns, for his criticism of Russia's assistance with Iran's Bushehr nuclear facility. "This meeting isn't going anywhere", snarled Rice, perhaps angry that the rebuke of Burns reflected badly on her.

Burns himself was probably a bit cranky after his trip to Moscow in April, when he publicly asked Russia not to go ahead with the sale of Tor-M1 mobile anti-missile missiles to Iran, only to be bluntly rebuffed by Russian Chief of Staff, General Yuri Baluyevsky.

Meanwhile the world looks on, hoping that the great powers really know what they are doing, and that World War 3 won't start because of a subtle miscalculation in brinkmanship.

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