Season 2- Episode 9

Olga Torres: Thank you for joining us to today for the Torres Talks Trade Podcast. My name is Olga Torres and I'm the Managing Member of Torres Trade Law, a national security and international trade law firm. Today we're going to discuss the political impact of U.S. economic sanctions, and more specifically how the use of sanctions can affect the supremacy of the U.S. dollar in the global financial system.

I have the pleasure of welcoming our guest, Daniel McDowell. Dan is an Associate Professor of Political Science at the Maxwell School of Citizenship and Public Affairs at Syracuse University. He has authored multiple publications in top international relations journals, and his work focuses on international politics, money, and finance. He's also the author of two books, and today in our podcast we're going to focus on his second book, which is titled "Bucking the Buck: US Financial Sanctions and the International Backlash against the Dollar." I believe they can find your book on Amazon, and we'll also show links, where they can find your website. This book focuses on the political risks associated with U.S. financial sanctions and the concept of de-dollarization. Welcome Dan and thank you for joining us today.

Daniel McDowell: Hey, Olga, it's my pleasure. And thank you for having me on your podcast.

Olga Torres: So typically, Dan, we start by giving the audience a little bit of background on your personal background, who you are, and what led you to where you are today. So, if you can start with that, that would be great.

Daniel McDowell: Yeah, absolutely. I'd be happy to sort of give you the quick story of my professional life. I was a PhD student at the University of Virginia, studying international relations as part of a political science program there during the financial crisis.

Olga Torres: Which financial crisis 08?

Daniel McDowell: You're right, I should be more specific. We've had a few, the global financial crisis of 2008. My first year in the PhD program was 2006, so it was in my second year when everything sort of started falling apart and I became very interested in the role of the Federal Reserve providing dollar liquidity to foreign central banks through what are called swap lines.

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And that became a core part of my dissertation research, which turned into my first book. And I start there because as I was working on that topic, I became sort of aware of the fact that around the same time the People's Bank of China, China Central Bank was starting to open up similar swap lines with partner Central banks, mostly in Asia, but then in places in Latin America and other countries around the world. And this was surprising to me because the swap lines with the PBOC provided RMB or Yuan, China's currency, which wasn't really widely used at all at the time. And so I was trying to figure out what was going on. And so my work kind of then trans sort of transferred over into thinking about kind of international currency competition and the potential for China. And the RMB to potentially rival the dollar down the road. And this was again, around 2009. So, not a whole lot of folks were paying attention to it at the time. Now it's becoming really a hot area of business and media coverage. And we're talking about to some extent that today. And so then I was interested in the currency stuff.

And then the sanctions topic became a real interest for me around 2017 I read this report about Jack Lu, Former Treasury Secretary who had given a speech talking about, hey, the more the United States uses sanctions, the more it sort of pushes countries that are targeted by sanctions into other currencies, and we should weigh those costs against the benefits of sanctions. And that's what sort of triggered the idea for the book. So that's sort of a long-winded version of how I got here, all the little ways that I meandered through to this topic.

Olga Torres: Yeah. And it's really interesting because, I mean, as you may know, we practice economic sanctions law, right? So, we assist companies with compliance programs and in some cases also defending potentially against economic sanctions. From my perspective, your angle, it's really interesting because typically we're not really involved in what other countries may be perceiving from a political higher level geopolitical perspective. How do we protect ourselves from the U.S. potentially using economic sanctions as a tool and the foreign policy as a foreign policy instrument to deter certain actions. And we saw that a lot with Russia, obviously that's the newest one.

But, so in your book, when you talk about the de-dollarization, can you explain to our audience what that means and why you believe the use of economic sanctions could and my understanding is your book is not saying that economic sanctions would actually end up in the end of the dollar as such. But you are saying the more that we use it, right? If we're using these tools all the time, then we're going to start seeing more of what we're seeing right now, and we can discuss it later as well. Brazil, saying, why are we always using the U.S. dollar when we're conducting international trade with each other? Let's switch currencies. So, can you talk about that concept and the anti-dollar policies that could happen if we continue using economic sanctions as a tool?

Daniel McDowell: Yeah, I appreciate how you asked that question, Olga, because I think in the sort of current zeitgeist in discussion surrounding the dollar's global role and sort of geopolitics of that de-dollarization is I think often a synonym for the end of the dollar's dominance. And it's often discussed as, again, it's sort of evidence of that's where we're heading. I don't think that's actually true. And you're right, the book, I don't conclude this at all. I think that the dollar has economic and political advantages that will continue to allow it to maintain its position in the coming decades.

De-dollarization to me is distinct from sort of the hierarchy of currencies necessarily. It is really about individual countries in their own policies. So, I would define it as an intentional effort by a government to reduce its dependence on the dollar for cross border payment purposes. And so that would involve trade, which I think for your listeners would be most important. But also, cross border investment purposes, right? So, reserves are investment roles as well. And so yeah, de-dollarization is just right hat intentional effort to try to limit your reliance on the dollar because you recognize that dollar dependence leaves you vulnerable to U.S. financial coercion. So yeah, I think it's important to distinguish it too. You can talk about de-dollarization without having sort of a doomsday scenario for the dollar over the next several years. I'll kick it back to you. I don't know, you might have a more specific follow up.

Olga Torres: Well, something that came to mind as you were speaking. It's really, and this is probably basic, but I think it would be helpful to our audience to understand it. It came to my head when I read an article where Lula de Silva Brazil's President was asking the question like, why do we use the U.S. dollar? And, and I thought to myself, yeah, why is the U.S. dollar used? And I don't know if you have the answer to that, I presume it's somewhat basic. What would be your answer to his question?

Daniel McDowell: Yeah, I mean, look there's, I think there's two ways to answer that. The starting point is just dollar dominance leads to more dollar dominance. That's a circular argument, I recognize that. But the simplest way for me to explain this would be to think in terms of like something like a social network. And so, let's use Twitter as an example. I often use this to make the point. Twitter is something that a lot of people don't like, but they continue to use, right? People might not like it because they don't like Elon Musk. Maybe they don't like particular policies, or the way Twitter handles certain situations. Some people will say, I'm going to leave Twitter, I'm going to go to Mastodon, or I'm going to go to truth social. You name the alternative. And what typically happens is people go to those alternative networks and they find there's just not a lot of activity over there, right? That all the action, all the retweets, all the conversations are happening on Twitter. All the news is being provided on Twitter. And so inevitably a lot of folks would get drawn back to that particular dominant social network. And so that's because right, you have all of the connections there between all the individuals in this case.

So, if we think about the dollar as a cross-border payments currency, the reason the dollar sort of retains that dominance is because it achieved that a long time ago. And everybody's already sort of using, firms are used to accepting payments in dollars. They're working with banks that are clearing in dollars. And everything that we're trading is, not everything, but most things, especially major commodities, are priced in dollars, et cetera, et cetera. And so, it's very difficult to sort of just say on your own, I'm going to just unilaterally go use some alternative countries currency. That's like going over to again, insert the alternative social network and you find out your kind of on your own.

Olga Torres: And people trust the dollar, like they actually trust that currency versus maybe if you go to a different country. Maybe they're not as transparent, maybe their economy is not as, the way the U.S. economy would run. What are your thoughts on that?

Daniel McDowell: Oh, without question. I mean, the other things we could talk about, right? Sort of like that's the first answer to the question is why the dollar is because once you achieve sort of network dominance, in this case, financial network dominance, it's very difficult to sort of upend that, right? But then you could, you could go farther back in the causal chain and say, well, why did the dollar become this dominant currency in the first place? And that's a longer story. Part of it is about the United States sort of economic supremacy at the end of World War II. The rebuilding of the world economy around the Bretton Woods system, which put the dollar at the center of the monetary system, and then the dollar being provided and aid to Europe led to an accumulation of dollars around the world. There's all these sorts of things that you could go back through the tracing of history.

But your point about the role of the government in policy is really critical too, because one reason the dollar is so widely used is because it's so readily available, because dollar markets are so liquid. And one of the reasons that's the case is because the U.S. government has adopted a policy effectively since the early 1970s and even somewhat before that to not regulate or intervene in, say, cross border flows of dollars. There are capital controls used in the United

States, right? It's financial markets in the U.S. are completely open to foreigners, right? You can buy dollar assets. You can sell those dollar assets and liquidate them very easily. There are buyers on every side. Dollars turnover in foreign exchange markets more than any other currency. So, the availability, the efficiency, the low cost of transacting in the currency and the trust in the government to not meddle in your transactions compared to alternatives like let's say China, right? Which we know uses capital controls regularly, right? It's a main part of how they manage their financial system. So, for sure that's a huge part of it as well.

Olga Torres: And yet we're still seeing this trend. And I don't know if it's a trend, but we're at least we're reading about it more, right? I mean, Brazil, China trading in Yuan, I believe. Obviously, Russia, China trading relationship, especially now, Yuan being used. Do you expect the U.S. dollar maybe not losing its dominance, but at least where it will become a little more fragmented, where we're going to really see more of trading relationships, especially if it's not allied countries or countries that fear potential retaliation. Do you expect that to continue and to continue increasing.

Daniel McDowell: I do. Again, I think it's at the margins, right? And it is going to be concentrated in certain pockets of the world, right? Again, with countries, as you mentioned, that are not friendly with the United States or have reason to fear that they might face sanctions in the future. I think the way to think about this, right? We've sort of talked about all the economic advantages and the economic appeal of the dollar, but politics matters even though it's not the main thing, it matters. And for all the reasons why we just said the dollar is economically appealing and attractive. Politics can get in the way and turn out to show a government that despite all these economic advantages, the sort of political disadvantage for you ended up trumping all those benefits. So, for Russia, right? He had all these reserves and dollars and yeah U.S. treasury bonds are the most liquid asset market in the world until the federal government in the United States says you can't sell those, you can't access those, and then they're immediately illicit for political reasons. Or, transacting and trade in dollars is the most efficient way to do things until, American banks won't answer your calls, right? So, politics can make the dollar for certain countries very unattractive.

And so, if you A have been sanctioned, or B think you might be sanctioned in the future because American sanctions don't happen in private. You can go read executive orders on the treasurer's website. You can see the kinds of countries that are being targeted. You know why they're being targeted. Human rights violations, democratic backsliding for foreign policy actions that cut against

U.S. interests. And rational governments are going to recognize if they're more at risk or less at risk. And a rational government would be crazy not to start thinking about and planning for a potential future where sanctions could be used against them, their interests, key officials, key institutions. It doesn't mean you're going to wholesale dump the dollar, right? You really can't do that realistically. But you want to start prepping for that. Even if that just means in smaller ways to have some resilience built in for that potential future.

So, you mentioned Brazil. The first thing I would say that happens is when countries start to recognize the risks is you often hear rhetoric, anti-dollar rhetoric, complaints about the dollar. That awareness of political risk, what I call in the book, political risk in the currency system is sort of the first step. And then what happens after that is governments might want to take that to the next stage and say, okay, now we want to actually try to de-dollarize. Now getting to de-dollarization is another story, but first you have to start thinking about what policies we can implement that could sort of push us in that direction. So, you start to see governments wrestle with different, what I call anti-dollar policies. Policies that are in depth reducing your dependence. Some of these fail, right? They are unsuccessful. But in other cases, you might see some marginal progress. We could talk about Russia. We could talk about China later. Those are countries that we've seen some of that in their own, economic relations.

So, I think that's sort of the linear process that we've seen countries typically go through. So yes, I think we will see more fragmentation, more experimentation. That's another way to think about it with alternative currencies. I don't think that we're anywhere near a world where any of these alternatives are going to be able to compete from a purely economic perspective with the dollar. But again, for countries that are already A sort of at the margins because of sanctions or are worried. You might see more dabbling in that space, and you might see a little bit more scale start to develop in those areas.

Olga Torres: Yeah, and that's really interesting because it reminded me when the Russian invasion started, shortly thereafter, I believe the Chinese government, I think, had advised and that reminds me of the difference between a foreign government trying to de-risk from the dollar. But also, individual players of that country. And in that instance, I think I read an article about China, the Chinese government saying, or telling their businessmen, hey, you may want to be de-risking from the U.S. economy. Or I think in that case it was from the West. Look at what's happening. And I guess in that example it was the oligarchs, right? Your assets get frozen, you cannot use your money anymore. And I don't think I've been tracking it. I wonder if Chinese.

individuals, billionaires, if they took any action on that. I don't know if you have any comment on that.

Daniel McDowell: I don't know about actual executing on that plan, but I remember seeing the same stories. I think the story I remember reading was in the Wall Street Journal. It was effectively saying that the CCP was recommending to top government officials to basically divest of all assets in the United States because again, they were vulnerable to being frozen or confiscated. And yeah, I mean, you got to think about like how the United States uses sanctions on various pressure points against regimes that it wants to target, right? Often we think about it as like the United States has sanctioned Iran or the United States has sanctioned Russia. But actually, it's individuals, it's banks, it's firms, sometimes it's government institutions within those countries, right? Not an entire economy. So, yeah, I mean, a sort of, you look at the playbook, the typical way place that the United States starts is with powerful individuals within the economy. You mentioned oligarchs or officials within the state apparatus. So, in China, given the role of the state and the economy, I think clearly top breaking state officials are probably the ones who are most concerned about their individual risk. And so, the idea of trying to get ahead of that with selling your assets in the U.S. dollar. Again, that seems like a rational thing for a country like China that is, I think, rightfully worried about the potential for sanctions in the future. My suspicion is that those things have probably been acted on. Usually when the Chinese Communist Party tells officials to do something they tend to follow.

Olga Torres: So, yeah. And that would be interesting from an escalation perspective, at least my point of view, especially for example, international trading here we're talking currencies or the use of the dollar. But the more we decouple. I feel like it's just going to lead to more escalation, right? I mean, we don't necessarily want to go full blown war against China. They're like our largest business partner or trading partner, right? But to the extent that we're decoupling more and more that incentive that international trade was supposed to be a world or a globalized world, was supposed to be a world of no wars. And that’s shifting and I suppose world order could actually escalate things, right? Where we would actually have less incentive to cooperate, right? Because we're not trading anymore, or they don't feel that retaliation could actually be effective anymore. They don't have U.S. assets. What are your thoughts on that?

Daniel McDowell: Well, I mean, I think if we look at the deterioration in the U.S. China relationship, which is at this point, I would say probably a 10 or 11 year sort of slow decline into a faster decline over the last few years. I mean, if you go back to the year 2000 Clinton administration before that year, the

Clinton administration in the 90's pushing for China to join the WTO, the vision was that as you said, right? Three economic engagements. You would be able to manage the relationship between what was clearly, even 25 years ago, the sort of power of the future, in Asia. And that trade in commerce and investment would be the way to both A sort of promote warmer relations, but also hopefully push China towards liberalizing its political system as it enjoyed the trappings of capitalism right as it opened up to the world. And instead, of course, what happened is under Xi Jinping especially, right, more centralization of power, we didn't see the market reforms that were promised. And so, I think the idea that it was through economic engagement with China, you would be able to manage the obvious differences in political systems that create some mistrust, a different strategic interest. I think American policy makers and western policy makers more generally have just grown disillusioned with that idea. You could start with the Trump trade war, but then more recently it's getting even more serious with the chip bans and things, which are there's no other way to characterize them other than attempting to contain China's capabilities, strategically, but also to contain its economy and sort of competing in these sectors of the future. And yeah, so without the cooperation on the economic front, I think it does make relations in all the other areas all the more fraud.

Olga Torres: Yeah. Do you foresee, so we're talking about China, Iran, Russia, and why they would want to hedge against the dollar. Makes a ton of sense. Do you think we could be closer to a situation where even allies say I'm thinking about investments, right? Like they always tell you, diversify your portfolio. Try not to put all your eggs in one basket, kind of situation. Do you think we could be at a point in history where, I don't know, I'm making this up, like France or Germany or some of the friendly countries could say, hey, it may make sense to hedge generally against the U.S. dollar, like we have good relationships with the U.S. until we don't. And what would that mean for the U.S. dollar at that point? Because we're definitely seeing it more and more with people that are not friendly to us, right? Like countries that are not our allies. But I wonder if the next step where things become really concerning are when friendly nations, in spite of the history of the U.S. dollar, in spite of us having the infrastructure right. That it would be difficult to swift for example, and people have been relying. But if it gets to the point, and my question to you is, are we close to that point? Have you heard of anything like that? Or no?

Daniel McDowell: Well, actually the interesting thing is, we want to focus on Europe, which I think is a great case to talk about. Things have actually gotten somewhat better on that front, to be honest, from where they were five years ago. So, in 2018, when the Trump administration unilateral unilaterally withdraws from, uh, the Iran nuclear deal, the effect of that was to quote unquote snap back in place the sanctions that the United States had lifted at the time of the agreement being reached in 2015, and those sanctions were not just sanctions on what we call primary sanctions. Telling American banks and financial institutions you can't do business with these Iranian targets. They included secondary sanctions, which are a way to rapidly sort of scale up U.S. sanctions power. I'm sure if you do sanctions enforcement and advice, you are well versed on this, probably well, more than I am.

And so what that does, of course it means that, hey, institutions and businesses in third countries, you have to follow U.S. sanctions law as well, or face being placed on the blacklist. And so, the reaction of European leaders was pretty swift to that decision. You had the German Foreign Minister, the French Finance Minister, you had the European Commission President all coming out saying, we need European independence from the dollar. We need to promote the Euros role globally. It's a big currency too. Why don't we use our currency more? Why are we using the dollar in trade and so forth? And actually, you saw this is kind of a crazy little fact, but Russia had similar feelings because they had been sanctioned starting in 2014, repeatedly in 2015, 2016, I mean literally almost every year up until 2022. I mean, this is the thing, people think Russia was just sanctioned in 2022. No, like this goes back almost a decade. Russia was looking to get out of the dollar too, and you actually had increasing cooperation between Europe and Russia because of course we know prior to the war, Europe was the biggest buyer of Russian energy. And it was the biggest market for Russia. And if you look at the trends, according to Central Bank of Russia data, the dollar's role dropped substantially between 2014 and 2020. Sort of a steady decline in a shift towards using Euros more. And some of that was, I think, a reflection of European frustration with U.S. sanctions as well. I think we've seen an improvement there because the Biden administration has really adopted a clear multilateral approach to Russia. The Biden administration could have gotten ahead of Europe and quickly responded with sanctions that would've put European countries in a tough spot in energy. The Biden administration recognized European dependence on Russian energy. This meant that you had to slow walk those measures and allowed sort of European countries to be leaders in announcing their own sanctions and not just sort of following the United States. And I think that's helped repair some of that damage. But to your scenario, your question about a scenario in the future where that might happen, I mean, you could imagine a future.

Olga Torres: Basically, it has happened, and it could happen again. But it is interesting though because another example of Venezuela, right?

And I believe they started using gold more. And I think Russia too may have been trying to move to gold a little bit.

Daniel McDowell: Yes.

Olga Torres: And I guess that leads to another question, but one comment is, well, people have thought of this before, right? This is not the first time that you hear countries say, okay, we need to hedge against the dollar here. But it hasn't fully had a real impact, so, whether that will ever happen or when that's something that you are monitoring probably closer than I am. But then that also gave me an idea or brought a question to my head on gold and for example, crypto, do you think, I don't know, crypto would have a role to play. I know people at some point, OFAC had expressed concerns that crypto could be used to specifically evade economic sanctions laws by the U.S.

Daniel McDowell: Yeah, I mean, for sure treasury watches those things. Crypto's obviously a place where actors in the shadows can try to hide money or move money.

Olga Torres: And lose money apparently.

Daniel McDowell: Yeah, we need a shot for that. That's a good one. I think there hasn't been a lot of evidence in my research that that's becoming a major focus of governments and we'll mention it just because you asked it. Back around 2018, 2019, Russia and Venezuela were sort of both kicking around the idea of state backed, sort of quasi state back cryptocurrencies for cross-border payments. Venezuela launched something called the Petro, which was an oil backed cryptocurrency. And it completely bombed, it didn't gain any traction whatsoever. And it was sort of advised to do so by the Russian government. My understanding is that Russia was sort of using Venezuela as a test case. Well, let's see if the Venezuelans can pull this off and then if they can, maybe we could try it too.

I think the gold story is a little bit different. That's more on the store of value side than the payment side. It's hard to use physical gold to conduct payments. It weighs a lot, you can't move it around the world very easily, right? But we have seen governments using that more as a way to stash value in gold in their own vaults because it can't be frozen. And then in a worst-case scenario like Nicolas Maduro did you, you fly that around the world. You get cash for it, you fly it back into your country and you can use the cash for, again, getting that into your banking system or perhaps paying off your cronies. There's uses for gold in a total doomsday scenario, but it doesn't really solve your problems. You're in a tough bind if you're resorting to selling physical gold.

Olga Torres: Right, that's interesting. In terms of OFAC have you ever tried to, do you have any communication with treasury, and I mean, have you sent them your book?

Daniel McDowell: I probably should.

Olga Torres: I think you should.

Daniel McDowell: I know, I know several former treasury folks. I didn't talk to anybody at OFAC about this when I worked on it. Hopefully they're aware of the book. I actually just saw this is funny you mention it. I just saw today, Bloomberg got an article that said that the U.S. Treasury is now created, now I'm going to forget the name of it, but they just created a new research unit that studies the effects of sanctions. And I think this is a response to exactly what we're talking about here, that even U.S. Treasury is recognizing that, okay, we're using sanctions more and more. We've got to figure out not just when do they work and when don't they work, but what are the tradeoffs? What are the downstream effects of using sanctions as much as we are? Maybe we should be using them less or only in certain circumstances. I think it's great that they're looking into that. I think it's really important because I think up to now, I do think my own personal view is the United States has used financial sanctions specifically in circumstances where A they were not going to be effective, and B they just sort of politicized the dollar system unnecessarily and then tip off adversaries to start preparing for a future when you might really need them down the road. And so I think they have been misused, quote unquote, to say like, in a way that has, I think, raised questions about the potential effectiveness of them in the future in ways that maybe had they been more circumspect, we would've had those questions.

Olga Torres: Yeah, it reminds me when the agency lists individuals, right, especially designated nationals and when they failed to provide clear guidance as to what will get you de-listed, like what kinds of actions, like if we're taking corrective measures. Which is the whole point of it, right? Like you want the individual to change behavior and the individual is trying to change the behavior, but there's no agency guidance or any kind of idea for what we need to do. It becomes counterproductive, right? So, it kind of reminds me of that. The agency hopefully is aware of that. I do know that they hired economists not too long ago. So, maybe they did read your book.

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What is your advice in terms, and this may be a little bit of a curve ball because maybe you're not as familiar with the trade side of things, but in terms of companies it doesn't sound like we're in any way, shape or form close to stop the use of U.S. dollar, right. But in terms of companies, whether abroad or in the U.S., do you have any advice in terms of monitoring, in terms of potentially hedging for any kind of issues related to the dollar?

Daniel McDowell: Sure. I think the thing I would, I would suggest to folks to sort of pay attention to, maybe they already are, and this gets back to China, which we've talked about and touched on a few times already. China's obviously the world's top trading country, right? More countries, both. China is their number one trading partner than any other country in the world. Despite the Covid zero slowdown and all those things, its commercial presence is enormous. And China's also a country that for obvious reasons, has really raw relations with the United States and I think is legitimately worried about sanctions. So, we think about de-dollarization today, often, it's coupled with conversations about the RMB or Yuan as sort of the alternative and could the RMB top the dollar again, I think that's way premature.

But what I do think we're seeing is policy makers in China becoming A more awakened to the risks of dollar dependence from a political perspective, especially. And RMB internationalization has been a goal of certain segments of the Chinese state for now 15 years. But it has a, I guess you could say it has a sense of urgency behind it. I think that it left right because of the strategic risks. So, what we're seeing, I think is more of a strategic effort on the part of China to promote the RMB in its bilateral training relations. So, to the extent that your clients or folks are engaged in trade with China, pay attention to the interest in Chinese firms to potentially move away from the dollar. I don't think this will happen a lot with American firms. American firms are going to be much more happy to continue using dollars and I don't think Chinese firms are going to completely walk away from the dollar. But I do think we will see, and we have seen over the last five or six-years growth in the RMB's role, especially in trade with China, right? In bilateral trade, which I don't think we'll see third countries using the RMB a lot. Russia maybe they don't really have any.

Olga Torres: Well, Brazil apparently now is, right?

Daniel McDowell: Brazil is with China, right. They're interested, at least they're talking about it. And that's what I mean, right? So, like you might see more trade between Brazil and China settled in RMB, less likely to see like trade between like Brazil and Argentina settled in RMB, right? Like so two third countries probably going to stick with the dollar there. But I do think

China in its own bilateral trade relations would like to move to a world where the dollars will continues to decline because that puts it in, what it views as I think a more resilient, more autonomous position visa vi the U.S.

Olga Torres: Yeah, that's interesting. I didn't think about use of Yuan in context of not involving China. And that's actually a good question. Have you ever heard of that happening?

Daniel McDowell: No. There was a report a couple of weeks back in the Washington Post about a Bangladesh payment to Russia using RMB. That was one of the first I'd really heard of. And that was, I think sort of sanctions related, and I think this is Russia's, again, a unique case because Russia, major segments of the Russian economy don't have access to the dollar system. The yen, they're pretty much cut out of all your major currencies. So, if you want to do business with those segments of the Russian economy, you almost have to look into either rubles or RMB in this case. And that seems to be what happened here because of sanctions concerns. And so, we might see more of that where Russia's conducting a little more of its trade with partners in RMB as well. Again, I think a lot of this really revolves around the sanctions risk. But China is a big economy and if China starts to conduct more of its trade in its own currency, that will start to make some waves that show the RMB sort of catching up in certain ways. I think it's still going to be a small share compared to the dollar, but I expect that's where we're going.

Olga Torres: So other than the dollar, do you think Yuan or where is the euro in all of this? I guess just when you're trading with European nations.

Daniel McDowell: Yeah, with, I intra-European trade, right? So, within the Euro zone. And then countries that are on the border. Euro is the currency. I mean, with trade within that zone. And of course, those countries trade a lot with each other.

Olga Torres: But the closest rival to the dollar, if you had to pick one.

Daniel McDowell: I mean, right now it's the Euro. It has the second largest role in payments. Second largest role, just about all the reserves, trade settlement, all those, right? The Euro is number two and it's been a steady number two, right? But no evidence that it's sort of growing in sort of poised to take on the dollar for that top spot. I think there's more room for growth for RMB. I think Euros sort of got a nice little pocket that it's in and it will continue to be a regional currency that plays sort of a lesser role globally. I think RBM has the potential to, again, in China's own bilateral relations, really grow. It's growing from a lower base than Euro, Euro's already much higher. You know, 35% of say, cross border payments, roughly RMB's at 2%. It has a lot of room to grow.

Olga Torres: Yeah. This is completely unrelated to the topic of the podcast, but I just remember something, a few years back, I think honestly it was under the Obama administration. I went to this conference, I was speaking in Mexico City, and they brought an economist, and he was basically simplifying a lot of very complex macroeconomics and concepts for us. He talked about the U.S. dollar, and I just remember from like an hour-long presentation, I came out of it feeling like, oof, I hope we never stop being the main currency right in the world. But the example he gave, I think at the time we were print, we continue, but we were printing a lot of dollars, right? And he was telling us how much that was. And he gave Argentina as an example, right? And he was like, this is what the U.S. is doing. And this is what Argentina did. When Argentina did it, it created, I mean, it was terrible, right? And he explained well, and the reason that doesn't happen to the U.S. is because the U.S. is still the main currency in the world, the reserve currency. What are your thoughts on that? If he ever, if it ever goes to that where even fragment augmented use of other currencies make the use of the U.S. dollar decline in such a way where it could actually, I mean, I feel like our economy's not the strongest it's ever been. So what do you think that would and maybe that's more of an economy, like someone I should contact someone that is an economist.

Daniel McDowell: Yeah, that’s a good question, and it's one that I think a lot of people have talked about, even in the international relations side of things. It's discussed and certainly economists think about it, it's becoming more debated now. It's interesting. I think the traditional view has always been what you just described, which is it would be quite costly. I mean, this is the, to sort of give an example of the uniqueness of the dollar, sort of what happens when the United States has a crisis. Go back to the global financial crisis. I mean, one of the craziest things that I always remember is how the financial crisis starts here when in the U.S. housing market, right? This is the epicenter of a crisis that spreads around the world. And what does the world do in this moment of panic is everyone rushes into U.S. dollars, in U.S. treasury bonds. Everyone goes into the dollar. The dollar appreciated it got stronger. Any other country, right? That's experiencing a major financial crisis. The opposite happens. The currency crashes. I even read something the other day that was predicting that if the United States defaults on it's a debt because of the debt ceiling it's conceivable the dollar could actually benefit because people would still panic and go into the dollar. Which this just goes to show you sort of this idea that it's like the bulletproof currency.

I mean, I'll give you another example. Back in 2011 or 2013 S and P downgraded U.S. government debt because of another debt ceiling standoff. And typically, when the government's debt is downgraded, borrowing costs up. Crickets. Nothing happened because markets kept, because it just seems like the appetite for dollars and U.S. government debt is just insatiable, right?

So, right. I mean, in a world where the dollar were to sort of fall out of favor and there was some alternative, and that's the main thing. There really isn't an alternative that can absorb that much investment. That is, again, has the confidence, which you spoke about earlier, if there were an alternative and capital begin flowing elsewhere. Yeah, U.S. government borrowing costs would rise. We know that the U.S. government debt's pretty large. If the rate on that debt goes up, then that means there's going to have to come up with that money somewhere, which would mean higher taxes or cutting spending and doing sorts of belt tightening that other countries are very familiar with.

So, I think that that's the view I would say I still ascribe to. I do think there would be some significant costs and pains. We probably don't have time to get into. I think there are some people who are starting to question whether it's always good and maybe there would be some benefits from not having a global currency. But I'm more on the other side.

Olga Torres: Yeah. Same here. Well close closing remarks for our audience.

Daniel McDowell: This has really been a pleasure to have a conversation with someone who works on the sanction’s compliance side. I know we didn't get into a lot of the details in the weeds. I guess I would just say I hope that the 30,000-foot conversation about sanctions is interesting and useful and I think this is a really interesting area to be watching for change in potential developments of new technologies. I mean, we didn't get into things like CBD C and the potential for new technology to maybe alter the cross-border payment, including trade settlement space. It's a fascinating time to be studying these things and watching these things. So, I'm sure you guys do a great job of keeping everybody in the loop on that.

Olga Torres: And do you ever need as you're writing I know you write a lot, you publish a lot. If you ever need assistance with anything related to economic functions or OFAC policies feel free to contact us.

Daniel McDowell: I will call you. Thank you.

Olga Torres: Thank you so much, Dan, for joining today. And thanks to our listeners for tuning in.

Daniel McDowell: It's my pleasure.

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