Research on the Mechanism of Dollarization and De-dollarization under the Global Financialization System (Part 2)

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The financialization of digital capital strengthens the international status of the dollar

In the age of industrial and financial capital, the U.S. dollar has assumed the role of an international currency for pricing, settlement, and reserve purposes. The development of information technology has driven both industrial and financial capital toward digital transformation, fostering a seamless fusion of technology and finance. This convergence has enabled digital capital to spearhead the progressive evolution of the capitalist realm. As the predominant currency within this capitalist world, the U.S. dollar has experienced an amplified and extensive global influence due to digital and financial capital integration. Consequently, it stands a greater chance of supplanting peripheral national sovereign currencies in fulfilling various currency-related functions.

Firstly, digital technology drives the digitization of diverse products and services, manifesting in valuable data information. This data, once commodified, becomes a crucial factor in present-day capitalism, serving as a vital source of surplus value for digital capitalists and a catalyst for the multiplication of digital capital. The amalgamation of digital capital with financial capital leads to the financialization of data information commodities, a process intricately linked to global information channels, with the U.S. dollar and other international currencies playing a pivotal role in this financialization journey. Secondly, the financialization of information data commodities removes temporal and spatial barriers, leading to reduced costs in the flow of various factors. This, in turn, accelerates the worldwide proliferation of capital and amplifies the influence of capital in trade, finance, production, consumption, and other domains. It particularly strengthens the level of capital financialization in these sectors,

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broadening the range of goods that can be assessed and controlled by the U.S. dollar and other international currencies. Thirdly, the rise of digital capital has led to increased and frequent transactions, contributing to the wider adoption of the dollar and reinforcing its status as a dominant settlement currency. Notably, the proliferation of financial activities like high-frequency trading, quantitative investment, and smart investment advisory services relying on digital technology has significantly amplified the scale and frequency of dollar transactions within the financial markets. Moreover, the emergence of various digital currencies, including digital stable coins pegged to the dollar, further intertwines digital transactions with the dollar, expanding the dollar's sphere of influence in pricing. This expansion of the pricing scope, coupled with the growing prominence of the dollar as a settlement currency, reinforces its reserve value.

Institutional Financialization Is the Foundation of Global Dollarization

It is evident that the financialization of commodities and technology has bolstered the international monetary power of the U.S. dollar, thereby strengthening the U.S. government's control over the global economy through dollarization. Nonetheless, this development is contingent upon a series of favorable institutional arrangements that support the financialization, which can be referred to as institutional financialization. The adoption of a financialized institutional design plays a pivotal role in safeguarding the attainment of global dollarization.

Neoliberal ideology dominates the institutional financialization

Following the collapse of the Bretton Woods system and the development of the Jamaica system, international currencies have experienced greater diversity. Consequently, the U.S. dollar has lost its status as the sole settlement currency for major commodities, leading to a decline in international prominence. In response, the United States secured the status of its primary international currency through institutional financialization, ushering in the era of global financialization6.

Institutional financialization refers to a series of mechanisms that uphold and promote financial liberalization, and it is grounded in the ideology of neoliberalism. Neoliberalism is a prevailing ideology advocated by the concentration of financial power in monopoly capital. The global financialization system is central to sustaining this ideology, an intricate institutional framework that serves as its backbone. This institutional arrangement not only reinforces the principles of neoliberalism but also plays a pivotal role in preserving the international dominance of the U.S. dollar.

The LPM (liberalization, privatization, and marketization) reforms have played a crucial role in increasing the international credibility and importance of the US dollar.

Neoliberalism, a prominent economic and political ideology, gained traction during the global stagflation crisis in the mid-1970s and found its early advocates in the United States and United Kingdom. This ideology centers on core principles that significantly influenced policies worldwide. These principles encompass privatization, liberalization, marketization, and internationalization. The global financialization system is firmly established upon the principles of private ownership and liberalization, bolstering the international prominence of the U.S. dollar as the dominant reserve currency (Li & Sun, 2020). Free market thinkers like Milton Friedman, who played a significant role in shaping the financialization system, espoused the belief that a country's economic development rests upon the pillars of "absolute liberalization," "thorough privatization," and "comprehensive marketization" (commonly known as the "LPM" mechanism).

Firstly, they passionately underscored the imperative of liberalizing international economic exchanges and ensuring equitable treatment for domestic and foreign transactions. Achieving this vision necessitated eliminating non-tariff barriers, substantially reducing tariffs, and simplifying tax regulations. Secondly, they diligently pursued privatization policies to divest state-owned assets, effectively privatizing all state-owned enterprises and other valuable properties. This comprehensive privatization approach involved strategic joint ventures, leasing arrangements, share sales, and the complete transfer of property rights. Thirdly, they advocated comprehensive market-oriented reforms in the financial sector, including privatization of state- owned assets in the financial sector, liberalization of interest rates and exchange rates, increased openness of capital markets, free convertibility of capital accounts, and the introduction of short selling mechanisms.

Since the 1980s, many developing countries have undertaken significant "LPM" reforms to remove barriers and restrictions. These reforms have effectively facilitated the global integration of the U.S. dollar and other sovereign currencies, enabling them to harness the labor value from around the world and exert considerable influence over the labor markets in other nations. Consequently, these reforms have played a pivotal role in elevating the international standing and prominence of the U.S. dollar.

The "LPM" mechanism promotes the financialization of goods

The economic stagflation that emerged in capitalist countries during the

1970s was essentially due to the contradiction of capital accumulation, leading to an overabundance of goods and capital, with surplus value that could not be fully realized in the circulation sector. Consequently, financialization in the circulation sector was promoted, encompassing goods and various forms of productive capital. This shift towards financialization led to the rapid dominance of financial monopoly capital in the global economy. The financialization of goods here mainly refers to bulk commodities with typical financial attributes.

Firstly, the pricing of bulk commodities is determined by market mechanisms. The price of goods is jointly determined by their intrinsic value and the forces of market supply and demand, with prices fluctuating around the value. Non- financialized goods, lacking investment value, typically experience minimal price fluctuations since their value is primarily derived from their use value. However, financialized bulk commodities acquire investment value in addition to their original use value. Consequently, their transactions

become more speculative, aiming to generate capital gains. This shift in focus moves the pricing ofthesecommoditiesawayfrombeingdetermined solely by the spot market's supply and demand relationship and towards being influenced by the investment relations of the futures market. American financial capitalists have established standardized futures trading mechanisms in response to this financialization, adhering to financial market trading rules. This development has substantially accelerated the speed of capital turnover and increased the rate of capital profit. It is essential to note that whether it is spot trading or futures trading, American financial capitalists predominantly set the rules governing these markets. Additionally, any currency used to complete the capital cycle must be denominated in dollars due to the significant influence and dominance of the United States in the global financial landscape.

Secondly, the international transmission of bulk commodity prices is determined by market mechanisms. Under the principles of the free flow of capital, the foreign exchange market mechanism determines the international transmission of bulk commodity prices. This mechanism relinquishes the control of countries over the exchange rates between their currency and international currencies such as the U.S. dollar. Consequently, it amplifies the volatility of commodity futures prices in the global financial market. This process enables financial capital to seek profits through speculation and grants developed countries' financial systems the capacity to enter other countries' markets, extracting surplus value at will through the financial market. This increases the frequency of dollar transactions in global markets, expanding the scale of international market transactions.

The "LPM" mechanism promotes the financialization of technology

In technological development, the substantial intervention of capital can serve as a catalyst, offering effective assurances for the continual reproduction of the labor force among innovative workers. This, in turn, acts as a magnet, drawing more labor into the innovative domain and amplifying the likelihood of successful technological innovation. While innovation is undoubtedly important, it is crucial to recognize that the primary objective of capital is not solely focused on innovation but on maximizing profits. Therefore, a significant portion of the outcomes stemming from information technology innovation is directed toward expediting capital circulation and achieving profits. One area where this effect is particularly pronounced is using instant communication technology in financial transactions. This technology has played a pivotal role in promoting the financialization of various goods and capital by enabling the completion of financial transactions in mere seconds.

Once capital is financialized, it undergoes a transformative process enabling it to generate continuous profits and self-replicate through perpetual circulation within the financial sector. The "LPM" policy facilitates technology standardization by streamlining its design, packaging, and valuation processes. This standardized technology is then made available for sale through roadshows. Eventually, the technology transforms into a financial product, enabling it to be freely traded on the financial market, providing opportunities for investors to participate and potentially benefit from its performance and growth.

At this point, technology transforms into a crucial intermediary in the circulation of financial capital. Instead of envisioning long-term profits derived from the industrialization of technology, financial capital, predominantly in the form of venture capital, now prioritizes immediate gains through collateralization, mortgaging, and equity transfer. The phenomenon of financialization within the technology sector has not only fueled the extensive growth of the financial industry but has also accelerated the overall process of economic financialization. Furthermore, it has broadened the realm of the U.S. dollar and other international currencies, making them more indispensable in global markets.

The "LPM" mechanism promotes financial globalization and global dollarization

Privatization, liberalization, and marketization form the bedrock of neoliberal globalization. The unfettered opening of global trade, currency, capital, and talent markets establishes the institutional framework for seamless connections between economies worldwide. Building on this foundation, the application of information technology eliminates the physical distance and barrier between markets, greatly reducing the cost of spatial transfer of financial capital and infinitely expanding its activity space on a global scale, collecting profits from local labor productions. Therefore, the development of globalization fosters the progressive advancement of globalization and the consolidation and monopolization of financial capital, with the specific intention of maximizing the surplus value generated on a global scale. Consequently, globalization has played a pivotal role in facilitating the widespread circulation of the U.S. dollar, culminating in the establishment of a global financial currency system primarily reliant on credit dollars. This phenomenon has led to the dominance of the U.S. dollar, commonly referred to as "dollar hegemony", achieved through a process known as dollarization. In essence, the progression of international market dollar circulation unfolds as follows:

Globalization has played a crucial role in facilitating the widespread circulation of the US dollar.

The Federal Reserve's issuance of U.S. dollars establishes its role as a global currency. Other countries acquire U.S. dollars through currency exchange or selling goods internationally. As a result, the U.S. dollar becomes an international currency, exerting influence over other countries' currencies, financialized goods, and technology. After economic entities in these countries acquire dollars, they return these funds to the United States by acquiring dollar-denominated assets, primarily in the form of bonds. This flow of dollars enables U.S. citizens to purchase goods in the global commodity market for consumption, as the dollar acts as a dominant sovereign currency facilitating international trade transactions. This creates a scenario in which a selected group of monetary policy leaders in the U.S. hold the power to obtain global commodities effortlessly by essentially printing more dollars, as depicted in Figure 2. This phenomenon exemplifies the concept of "dollar hegemony", wherein the U.S. dollar dominates as the world's primary reserve currency. The U.S. can unilaterally alter the dollar's value based on its interests through the Federal Reserve's monetary policy. Consequently, this grants the U.S. a significant advantage in international trade and finance.

The Adverse Effects of U.S. Interest-First Monetary Policy and De-Dollarization Measures

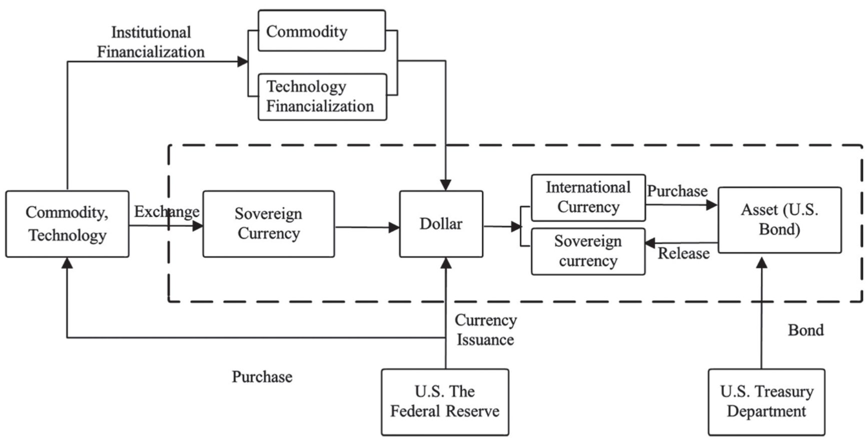
The Impact of U.S. Interest-First Monetary Policy and De-Dollarization Countermeasures

"Under the "LPM" mechanism, the Federal Reserve's interest rate policy adjustments significantly affect the global economy. For example, the Latin

American debt crisis in the 1980s, the Mexican currency crisis in 1994, the Asian financial crisis in 1997, the U.S. subprime crisis in 2007, and the subsequent European debt crisis were affected by interest rate policy adjustments. Starting in 2015, the U.S. interest rate surge led to a substantial capital outflow from certain emerging economies, such as Argentina, resulting in economic recessions.

The U.S. dollar's immense influence and destructive power stem from its international currency status founded on the "LPM" mechanism. When the Federal Reserve raises interest rates to combat inflation and alleviate labor-capital conflicts, it also increases the yields of dollar-denominated assets globally. The cost of dollar-denominated debt also rises accordingly.

Figure 2. The Progression of International Market Dollar Circulation



Consequently, entities facing a dollar shortage curtail dollar financing or repay dollar loans. In contrast, those with dollar surpluses redirect their investments into bolstering their holdings of dollar-denominated assets, such as U.S. Treasury bonds. These economic behaviors result in the repatriation of dollars to the U.S., intensifying capital concentration and consolidation, thereby reinforcing the monopoly grip of financial capitalists.

In peripheral countries, this leads to capital flight, and in severe cases, it triggers financial crises marked by currency devaluation, asset collapses, economic recession, and widespread hardships for the economy. When domestic labor-capital conflicts temporarily ease and financial capitalists reap profit, the U.S. implements quantitative easing through interest rate cuts. The Federal Reserve engages in extensive currency issuance, flooding the global market with a substantial supply of dollars to fulfill the demand for an international reserve currency. During this period, financial capitalists can acquire high- quality assets from peripheral countries at significantly discounted prices through frequent speculation, potentially leading to asset bubbles or an accumulation of excessive debt in these nations. Historically, this process repeats cyclically, ultimately resulting in the value created by labor in peripheral countries gradually transferring into the hands of financial capitalists centered around the United States.

In 2022, the Federal Reserve initiated a series of interest rate hikes, raising rates seven times by the end of December, resulting in a cumulative increase of 4.25%. This time, the interest rate hike was prompted by the surge in inflation resulting from the COVID-19 pandemic and the Russia-Ukraine conflict. However, emerging economies confronted the additional challenge of high inflation and mounting debts, exacerbating the situation of capital outflows. The U.S. prioritizes the dollar's domestic role but overlooks its global currency function. The high-frequency and large-scale interest rate hikes will have devastating consequences for peripheral countries and erode the U.S. dollar's international currency status.

According to statistics, more than 90 financial regulatory authorities worldwide implemented interest rate hikes, influenced by the Federal Reserve's policy, resulting in over 300 times of interest rate increases. These significant interest rate hikes have resulted in higher funding costs, serving as an ominous signal for the onset of economic recessions and indicating potential crises many countries may soon confront. Argentina, once with a high per capita GDP, has been plagued by recurrent economic and financial crises and social unrest following its adoption of privatization and market-oriented reforms rooted in neoliberal economic theory for emerging market countries.

Recommendations for Peripheral Countries' De-dollarization

Alongside the detrimental effects of monetary policy adjustments, the U.S. federal debt had reached nearly $31.4 trillion by the end of 2022, approaching its debt ceiling and accounting for 122% of its annual GDP. Over the past three decades, the purchasing power of the U.S. dollar has depreciated by more than 60%. Approximately 40 countries have been undertaking the process of de-dollarization, employing blockchain technology or currency swaps to circumvent the U.S. dollar in trade and settlement. Indeed, de-dollarization challenges the dominant power of the U.S. and cannot be accomplished overnight. We believe that the related countries can effectively advance the de-dollarization process by prioritizing the following aspects:

Promote the diversification of international currencies to reduce dependency on the U.S. Dollar and its assets

First, rationally allocate international reserves, with eligible countries seeking to increase their gold reserves to improve the structure of international reserves and weaken the U.S. monopoly on gold. Additionally, countries should promptly reduce excessive holdings of U.S. dollar bonds and diversify their international asset allocation. Second, increase holdings of international currencies other than the U.S. dollar and currencies of emerging economies with significant potential to reduce reliance on the U.S. dollar. Third, sign standing swap agreements with closely related trading partners to enhance the use of domestic currencies in trade and finance, thereby stabilizing domestic trade and financial markets. Fourth, actively construct new currency payment systems, building upon existing systems such as the European INSTEX, China's CIPS, and BRICS Pay, and jointly creating, improving, or establishing new international payment systems to compete with SWIFT, ensuring payment independence and security.

Focus on developing the real economy to counter the trend of financialization

Financialization, particularly the formation and development of digital financial capital, is crucial for the U.S. to strengthen its international position in the future. Countries should proactively take measures to address this trend. Firstly, strengthen government regulation to reduce or restrict market investments in purely financial technologies, guiding capital towards research and development of production technologies. Secondly, ensure that advanced technologies developed domestically or introduced from abroad are utilized to develop the manufacturing sector and other real economies, preventing them from becoming speculative financial instruments in the financial domain.

Lastly, regulate the development of digital capital, represented by digital platforms, to curb financialization activities within these platforms, preventing the formation of highly monopolistic and U.S.-controlled digital financial capital.

Fully recognize the harms of absolute "LPM" reforms on a nation

Firstly, countries worldwide, especially emerging economies, should address excessive privatization within their domestic economies and increase the proportion of state-owned enterprises in their overall national economy to effectively control reliance on foreign capital. Secondly, implement moderately liberalized policies for foreign trade, actively engage in industrial adjustments, reduce the scale of export-oriented industries, and lower the economy's external dependence. Implement foreign exchange control policies to limit abnormal capital flows from international financial monopolies. Lastly, key industries vital to the country's well-being should not be fully marketized but directly managed by the government, serving as the foundation for maintaining social stability. This approach helps mitigate the impact of the global financialization system and reduces the shocks caused by adjustments in U.S. monetary policy.

Lessons from China's de-dollarization

According to the general definition of dollarization, China has also been a dollarized country, holding substantial amounts of the U.S. dollar reserve. Given the current geopolitical situation and the frequent sanctions on Chinese companies imposed by the U.S. government, de- dollarization can be a strategic choice for China to guard against significant financial risks and ensure financial security. Based on the mechanisms of dollarization and the experiences of countries that have undergone de-dollarization, China needs to prioritize the following three aspects:

First, exercising control over financial power is fundamental for achieving de-dollarization. Since the reform and opening-up, massive U.S. dollar reserves have been accumulated thanks to the rapid development of China's export-oriented economy. Consequently, the currency issuance and asset pricingpowerhadtobepartiallyrelinquished.In such a context, privatizing most financial assets could potentially lead to the domination of Wall Street-centered financial capital, posing a severe threattoChina'sfinancialsecurity.

Firstly, we should learn from the lessons of "LPM" reform in emerging economies like Argentina and prioritize national economic and financial security in the reform and opening-up. Secondly, financial power as the lifeline of the national economy should not be concentrated in the hands of a few people. During financial reform and development, the dominant position ofthepublicsectorinthefinancialsystemshould be ensured, thereby guaranteeing the supervision and management of financial assets by the broad masses of the people. Lastly, private financial institutions, with their creativity and flexibility, play a crucial role in developing China's financial system. Therefore, they can complement and enhancestate-ownedfinancialinstitutions,jointly becoming a force to safeguard national financial security through strengthening guidance and effectivesupervision.

Secondly, high-quality economic development is a solid foundation for achieving de- dollarization. De-dollarization undermines the fundamental interests of American financial capitalists. Only through achieving high-quality economic development can we fundamentally respond to pressures from various aspects of the United States and achieve true de-dollarization. China should guard against the domestic economy "abandoning reality for the virtual". The financialization of commodities, technology, and other areas has increased profit margins but has not promoted domestic economic growth. Low- quality development is prone to be preyed upon by Wall Street-centered financial capital.

China should guard against the domestic economy "abandoning reality for the virtual".

Furthermore, China should enhance basic research capabilities to achieve breakthroughs in critical core technologies, which drive high-quality economic development. Talent is fundamental for technological innovation. In the long term, China should continue to support domestic universities and research institutes in talent cultivation. In the short term, China can encourage leading Chinese scientists worldwide to return to China while actively attracting outstanding foreign talents from various countries, including Russia, the European Union, and even Sri Lanka, to live in China and engage in advanced scientific research.

Finally, China should promote the application of high technology in the real economy. Financial development and technological innovation are mutually reinforcing. However, both should serve the real economy to promote high-quality development. For example, China can support the development of real industries based on high-tech such as artificial intelligence, big data, blockchain, and quantum communication by establishing industrial funds and cultivating business managers, making emerging industries the growth point of high-quality economic development.

Thirdly, the Renminbi internationalization is a significant step towards achieving de- dollarization. First, increase the proportion of the Renminbi in international pricing and settlement. Both Marxist currency theory and Western financial theory concur that sovereign currencies are not viable as a sustainable long- term international reserve currency. Therefore, the internationalization of the Renminbi should focus on its role in pricing and settlement in international business (Liu & Cheng, 2020). This can be achieved by promoting digital Renminbi transactions in regions like the Belt and Road Initiative, forming a regionalized network of digital Renminbi, and then expanding it to other relevant regions. Second, approach capital account opening with caution. The internationalization of the Renminbi necessitates some level of capital account opening, which entails integration into the U.S.-dominated global financial system (Cheng & Sun, 2015). This process should implement a prudent and gradual approach. During the capital account opening process, international capital inflows and outflows may be magnified several or even dozens of times due to adjustments in international and domestic policies or economic fluctuations. If speculative capital becomes predominant, it can significantly impact China's economy. To counter this, implementing measures such as Tobin taxes and non-refundable reserves can effectively curb speculative capital flows.

Conclusion

In summary, this article drew on Marxist monetary theory to explore the mechanisms of dollarization, its practical consequences, and alternative policies. Viewing through the lens of financialization, the global monetary system, commanded by the U.S. dollar, has traversed through three phases: the gold-dollar framework, the oil-dollar structure, and the institution-dollar scheme. The institution- dollar system, alternatively termed the global financialization system, represents a merging of commodity and financial markets and domestic and international markets realized through neoliberal institutionalization. This has further facilitated the amplification of the international monetary influence of the U.S. dollar.

Overall, financialization potentially amplifies the strength of the sovereign currency, quickens the pace of the international monetary cycle, and advances the global reach of the U.S. dollar through credit and additional tools. From a technological stance, the digitization of capitalism has also expedited this process. Since the 1970s, neoliberalism has been instrumental in both financialization and the internationalization of the U.S. dollar. Major pricing centers, including the New York Mercantile Exchange, London Metal Exchange, New York Commercial Exchange, Chicago Mercantile Exchange, and London Intercontinental Exchange, have the power to determine commodity prices in U.S. dollars, thereby directly swaying the currency choice in other countries' international dealings.

This being said, one could observe a burgeoning movement towards de-dollarization, enabled by blockchain technology and currency swaps that sidestep the U.S. dollar in trade and settlements. This progression can be hastened if many countries abandon the LPM reforms. Such countries, including China, should amplify their financial security and stability by bolstering state oversight and efficient regulation, championing high-caliber economic growth backed by a robust technological framework, curbing technological financialization, and suggesting alternatives to the U.S. dollar, such as the promotion of international monetary diversification and the internationalization of the Renminbi./.

NOTES

1. The countries include Poland, Croatia, Türkiye, Egypt, Hungary, Chile, Mexico, Israel, Belarus, Peru, Romania, Albania, and others.

2. Including countries such as Cambodia, Laos, Myanmar, and Vietnam.

3. In 1974, the United States signed the "Unwavering Agreement" with Saudi Arabia, citing the guarantee of Saudi security, in exchange for the Organization of the Petroleum Exporting Countries (OPEC) designating the U.S. dollar as the sole currency for pricing oil and conducting trade settlements.

4. The large-scale commodification of futures contracts on commodities is a hallmark of the formation of the global financialization system. Energy, as an essential commodity, saw the emergence of futures contracts in the 1970s, and it matured during the 1980s. This indicates that the massive financialization of commodities occurred in the 1980s, around the time of the establishment of the Washington Consensus. As analyzed later in the text, the formation of the global financialization system is built upon the financialization of commodities, with the assurance of the neoliberal regime.

5. Commodity financialization builds upon the use value of a commodity, exploring its potential for investment and financing while incorporating additional financial attributes. These additional attributes can be analogous to those of currency, making commodities with traits such as scarcity, storability, and liquidity suitable candidates for financialization. Non-renewable, exceedingly scarce, highly liquid, and readily storable commodities manifest more pronounced financial attributes. Among these commodities, significant globally demanded items closely interconnected with industrialization, such as crude oil, non-ferrous metals, agricultural products, iron ore, and coal, are commonly referred to as bulk commodities.

6. The fundamental distinction between the global financialized system and other currency systems is rooted in its transformative impact on the traditional demarcation between a nation's commodity market and financial market within the circulation domain. This paradigmatic shift serves to bridge the previously existing gap between commodity and financial markets and culminates in the establishment of a closed-loop structure in the international financial market, commonly referred to as the "commodity-finance- U.S. dollar-commodity" cycle.

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