

# TRANSFORMATION OF THE WORLD MONETARY SYSTEM FROM THE GOLD STANDARD TO THE CRYPTOCURRENCY?

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## **ABSTRACT**

*The world monetary system is a mechanism that links the economies of individual countries into a global economy. Therefore, any violations arising in the functioning of the global monetary system lead to significant problems in the development of the economy of separate countries and the world economy as a whole. Historically, the world monetary system passed through four stages in its development. The first world monetary system was the gold standard system. The existence of the gold standard prevented inflation and ensured the equilibrium of balance of payments of states. The next stage was the period of the Genoa currency system. During this period, only some currencies including the British pound sterling and the US dollar began to be considered as gold equivalents. The Bretton woods monetary system was adopted in 1944, which consolidated the leading role of the United States and its currency in the world monetary system, due to the post-war economic power of this country. Under this system, only the US dollar was pegged to gold and exchanged for gold at the request of central banks of other countries. The Jamaican currency system replaced the Bretton woods monetary system in 1971. According to the new system, the rate of the currency of each country began to change according to changes in supply and demand in the foreign exchange market. The modern monetary system is based on the functioning of two currencies, the US dollar and the Euro. Unfortunately, exchange rate fluctuations of these leading currencies negatively affect the economies of other countries. Some experts consider cryptocurrency as the global currency of the future global monetary system. The current situation in the global economy confirms that the world monetary system will inevitably be transformed and this process will be long, ambiguous and possibly not predictable.*

**Keywords:** *Balance of payments, Currency, Cryptocurrency, Global Economy, Financial crisis, Special Drawing Rights, World Monetary System*

## **1. INTRODUCTION**

Turbulence in the global currency and financial markets, the decline of the economic growth in many countries of the world has intensified the contradictions and instability of the development of the world monetary system. Currently global economy is characterized by the dominant role of the US dollar in the Global Monetary System. The US dollar simultaneously performs the functions of both national and world currency. Due to the dual function of the dollar benefits are received by the issuing country, others the states are in the conditions of currency dependence.

## **2. HISTORICAL STAGES OF DEVELOPMENT OF THE WORLD MONETARY SYSTEM**

Historically, the world monetary system went through four stages in its development, and each transition from one system to another was justified by a specific economic and political situation in the world. The first world monetary system was the gold standard system (from 1867 to the 20s of the 20th century), a characteristic feature of which was the adoption of a regime of fix exchange rates. The existence of the gold standard prevented inflation and ensured the equilibrium of balance of payments of states. The next stage was the period of the gold exchange standard (Genoa currency system).

During this period, only some currencies (about 30) including the British pound sterling and the US dollar began to be considered as gold equivalents. The Great Depression (1929-1933) had a negative impact on the world monetary system, in which almost all currencies refused to convert into gold. During this period, gold was considered only as a reserve and payments instrument. Due to the existing economic and political situation in the world, at the end of the Second World War, the question of the formation of a new monetary system was raised again. The Bretton woods monetary system was adopted in 1944, which consolidated the leading role of the United States and its currency in the world monetary system, due to the post-war economic power of this country. Under this system, only the US dollar was pegged to gold and exchanged for gold at the request of central banks of other countries. Actually, the Bretton woods system retained the basic principle of the gold standard: the parity between gold and paper money, and the principle of a fixed exchange rate. In 1971 the Bretton woods system collapsed. The main reasons for the crisis of this system were the unstable and contradictory development of the world economy as a whole, the instability of the balance of payments (the deficit of the balance of payments in some countries and the positive balance of payments in other countries). The growing economic power of the Western European countries and Japan, the decrease in the US gold reserves, the Vietnam War, and the energy crises during this period also contributed to undermining the fundamentals of the Bretton woods monetary system. As a result of the collapse of the Bretton woods monetary system, fixed exchange rates were replaced by floating, which increased the economic and financial crises in the world. The Jamaican currency system replaced the Bretton woods monetary system. According to the new system, the rate of the currency of each country began to change according to changes in supply and demand in the foreign exchange market. In the process of transition to a new monetary system, experts assumed that a floating exchange rate would reduce inflation in a number of countries, and countries would be able to manage their monetary policy. Unfortunately, the forecasts did not come true, the economies of most developing countries weakened even more, and capital outflows and inflation rates increased.

### **3. CURRENT SITUATION IN THE WORLD MONETARY SYSTEM AND PROBLEMS OF ITS DEVELOPMENT**

In the context of changes in the globalizing world economy and the global financial and economic crisis (2007-2011), the basic principles of the Jamaica monetary system have ceased to correspond to new trends in the global economy and the actual system is in deep crisis. The modern monetary system is based on the functioning of two currencies, the US dollar and the Euro. Unfortunately, exchange rate fluctuations of these leading currencies negatively affect the economies of other countries. The dollar is extremely volatile (Fig. 1), which undermines its function as a measure of value in the global economy.

*Figure following on the next page*

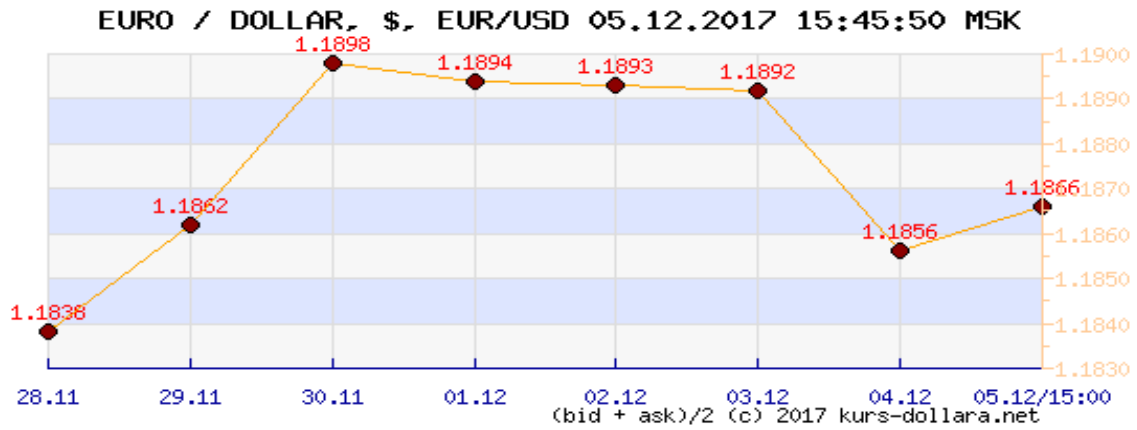


Figure 1: Graph of the dynamics of the euro against the dollar in the Forex market

Currently, the US dollar maintains a leading position in the modern monetary system and in the short and medium period, the dollar will dominate in the reserves of countries. According to the Bank of International Settlements, this currency is the main currency when making currency exchange transactions on an international scale. According to economists, the main strength of the dollar is due to the fact that all oil contracts in the world are made only in dollars. According to the World Bank's forecast, by 2025 the dollar will lose its dominant position and now in the global economy there is one of the most important questions: what currency, or maybe a group of currencies, will replace the dollar? According to experts, the new global monetary system should be based on the principle of multi-currency. None of the currencies in the world today can have monopoly domination. If earlier the global monetary system was mainly determined by the USA, Great Britain, Germany, Japan and France, today increased role of China, India, Russia. Especially the role of the Yuan becomes significant in the construction of a new world monetary system. In November 2015, the Executive Board of the International Monetary Fund completed a five-year review of the basket of currencies constituting Special Drawing Rights (SDR). In result the Board decided that from October 1, 2016, the Yuan will be included in the SDR basket as the fifth currency, because this currency meets all IMF requirements.

Table 1: Weight of currencies in the SDR basket (Press Release: IMF Executive Board Completes the 2015 Review of SDR Valuation)

Period	Dollar USA	EUR	GBP	YPY	Yuan
2011-2015	41,9%	37,4%	11,3%	9,4%	-
2016-2020	41,7%	30,9%	8,1%	8,3%	10,9%

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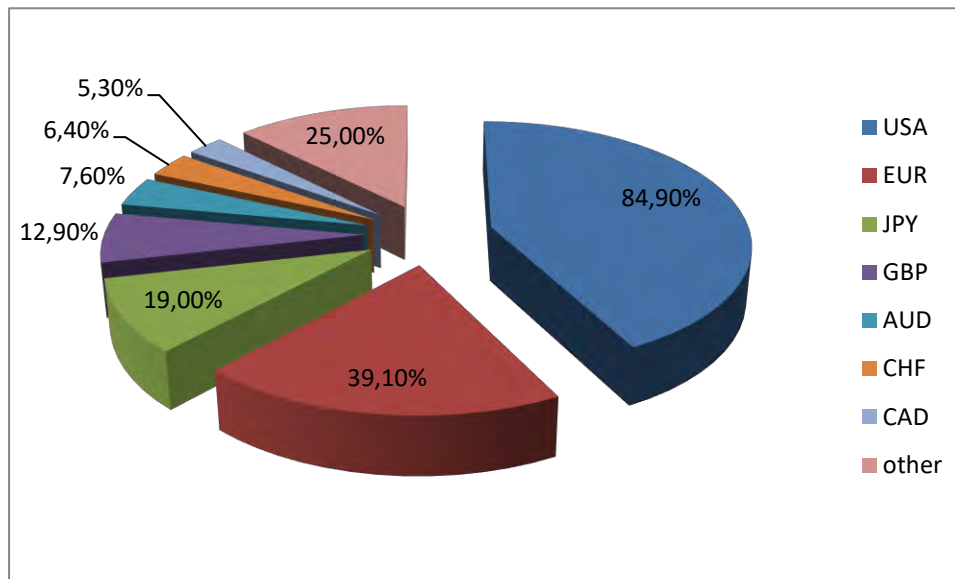


Figure 2: Currency Composition of World FX (IMF, 2017)

Constant fluctuations of the dollar and the euro lead to the formation of regional currencies. For example, “Amero” is a unit regional currency that was planned to be introduced into the territory of the United States, Canada and Mexico. “Afro” is a unit regional currency project developed in West Africa. AKU is an Asian unit currency that is planned to operate in Japan, China, South Korea and the ASEAN countries. The Arab Monetary Fund seeks to use the “Arab dinar” as the collective regional currency of the Arab states. It is predicted that the multicurrency system will replace the current monetary system, which is associated with the rapid growth of developing countries, including the BRICS countries. China has signed an agreement on swap lines with the United Arab Emirates, Japan, South Korea, Malaysia, and Turkey since 2011, thereby expanding the scope of influence of the Yuan. Iran pursues a policy of using national currency in trade relations with partner countries. The transfer of large commodity transactions to national currencies may reduce the dependence of the world economy on the dollar. It is assumed that the multicurrency reserve system will be formed on the basis of two or three currencies (playing the role of reserve at the world level), plus several regional currencies. The “Currency wars” have a negative impact on the world monetary system. The “currency war” refers to the actions of national governments and central banks to artificially lower the exchange rate of the national currency in order to protect their own market from imported goods and create conditions for increasing exports of their own products. Frequent currency crises adversely affect the modern world monetary system. The abolition of currency restrictions within the framework of the Jamaican monetary system has contributed to the growth of international capital mobility, which has become the driving force of currency crises. The main causes of financial crises are:

- the use of currency as an independent asset for investment;
- the predominance of the role of the financial sector in the formation of the public revenues;
- widespread fictitious financial capital;
- acceleration of capital transfer from one foreign exchange market to another;
- limited state regulation of financial markets due to the high degree of integration of various countries into the global economy.

Thus, the global economy is actively seeking solutions to the problems of the monetary and financial system. Unfortunately, the international reserve asset SDR during its existence did not become world money in framework world monetary system.

But experts believe that it is necessary to expand the range of the use of SDRs for mutual settlements between the IMF member countries. The active use of SDR mechanisms can be an alternative to the US dollar as the main currency in the international financial arena. Recently the idea of using precious metals as world currencies has become actual, due to decline purchasing power of the dollar, euro and yen. However, there are several reasons that prevent the use of gold as world money. First, precious metals have the high intrinsic value. This is explained by the fact that it is necessary to spend a part of GDP on the extraction of precious metals. Secondly, the complicated technology of settlements in metals. In order for financial calculations to be made in gold, it must be in cash. Some experts consider cryptocurrency as the global currency of the future world monetary system. Cryptocurrencies have become popular as a result of the rapid development of information technology and the Internet and its circulation does not provide any guarantees. Bitcoin, one of the leading virtual currencies, designed for online payments. Based on the data of Cryptocurrency market capitalizations, the exchange rate of this currency in electronic trading amounted to 15 thousand dollars in December 2017. The cost of cryptocurrency has reached 20 thousand, and again a sharp decline in prices to 13 thousand in January 2018 (Fig. 3),

### Bitcoin Charts



Figure 3: Dynamics of growth in Bitcoin prices (coinmarket.com)

As can be seen from Figure 2. Bitcoin has a spasmodic growth dynamics, which causes heated discussions of experts about its prospects. Some economists believe that the cryptocurrency can recover the principles of the "gold standard" on a global scale, if will be strict state regulation conditions and concerted action of banks. Some states have already begun to actively use electronic money in the economy. For example, Sweden and Norway have announced a complete rejection in the future of the use of cash in circulation. In the UK, Denmark, the Netherlands and Japan began to actively use cryptocurrency. Currently, there is no single strategy for the development of cryptocurrency in the world, but it is important that the competitive development of various electronic money systems should be under the obligatory control of financial regulators. Cryptocurrency can occupy a niche in which their use will be most effective in countries with a developed economy and a stable monetary system. In developing countries with a infant and unstable monetary system, tight controls are needed in the implementation of cryptocurrency. The number of implemented systems should be limited and, if possible, unified.

#### 4. CONCLUSION

As a result of the analysis, we can conclude that in the modern global economy, the US dollar or the currencies of any other countries are not able to perform all the functions of the world currency. Currently, the most acceptable form of functioning of the world monetary system is a multi-currency standard, because are increasing economic role some group developing countries in the global economy (China, India, Brazil). At present, reforming of the IMF and the whole monetary system has been necessary. Thus, the issue of transition to the new monetary system has become very urgent and requires lengthy negotiations between the countries of the world. The current situation in the world economy confirms that the world monetary system will inevitably be transformed and this process will be long, ambiguous and possibly not predictable. Thus, to build a new financial architecture, it is necessary to do the following transformations:

1. To strengthen the global financial system by creating global financial centers and a variety of reserve currencies;
2. To increase the legitimacy of existing financial institutions;
3. To maintain the free choice of exchange rate regime based on liberalism and on interstate regulation.

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