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ECONOMY

Geopolitical Tensions and International Financial Fragmentation

Chapter 2: Continuity and change in the role of international currencies

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Motivation

- Recent events have prompted questions about how the role of international currencies is changing
  - Rise in central bank gold holdings and the recent run-up in the price of gold
  - Novel patterns in the co-movement of the US dollar and other asset prices following the April 2 tariff announcement.
- These events are discussed in detail in Boxes 2.1 and 2.2 of the report!
- Chapter 2 puts these recent events in context and provides a framework for assessing their significance.

Overview of the Chapter

- Lessons from recent theoretical work
- The changing role of international currencies in four areas of the international financial system

1. Official reserves
2. Cross-border lending and borrowing
3. Trade
4. Foreign exchange markets

Key Takeaways

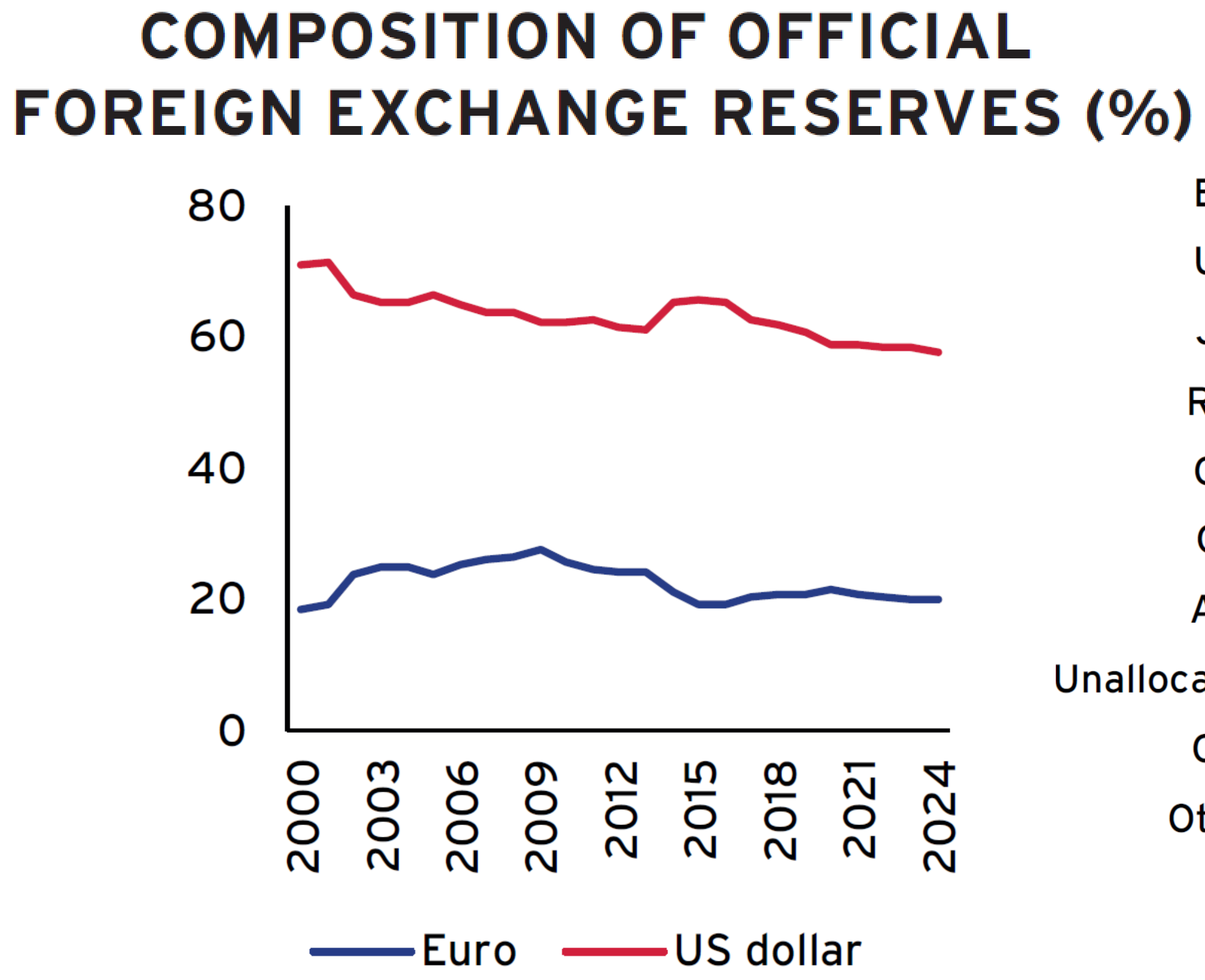
- **Continuity**:
  - Dollar retains its preeminent role across the four areas examined
  - Role of the euro remains stable as well

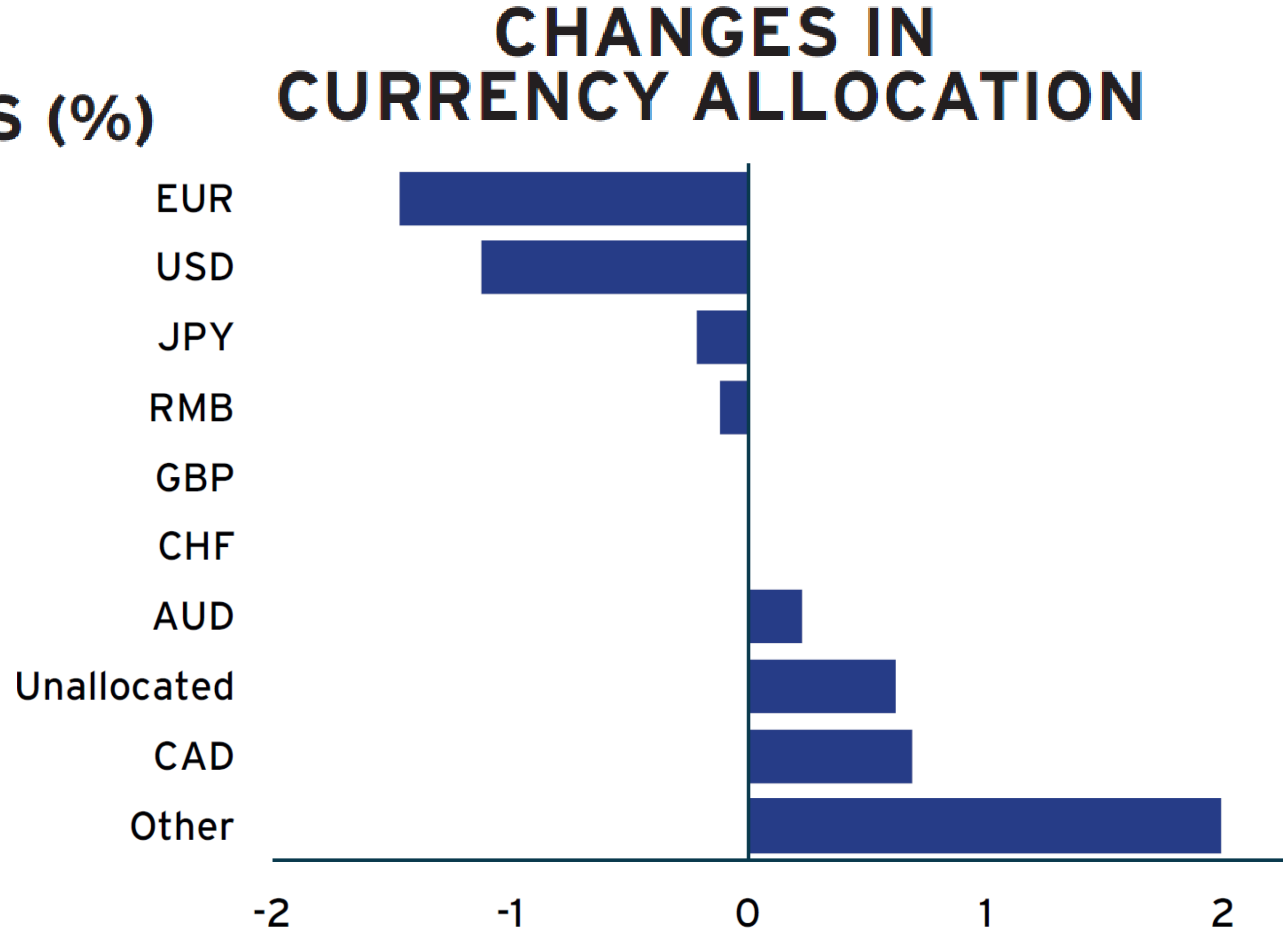
- **Change:**
  - Shifts in the use of international currencies have been driven primarily by economics rather than geopolitics.
  - A few notable instances of geopolitically driven shifts in official reserve holdings and trade invoicing.

Lessons from Recent Theoretical Work

- Strong inertial forces make changes infrequent but not impossible
- Interdependence of currency choice across areas of the world economy
- Policy can play a role in driving changes
- Insights into possible alternative configurations of international currencies

1. Currency Composition of Official Foreign Exchange Reserves

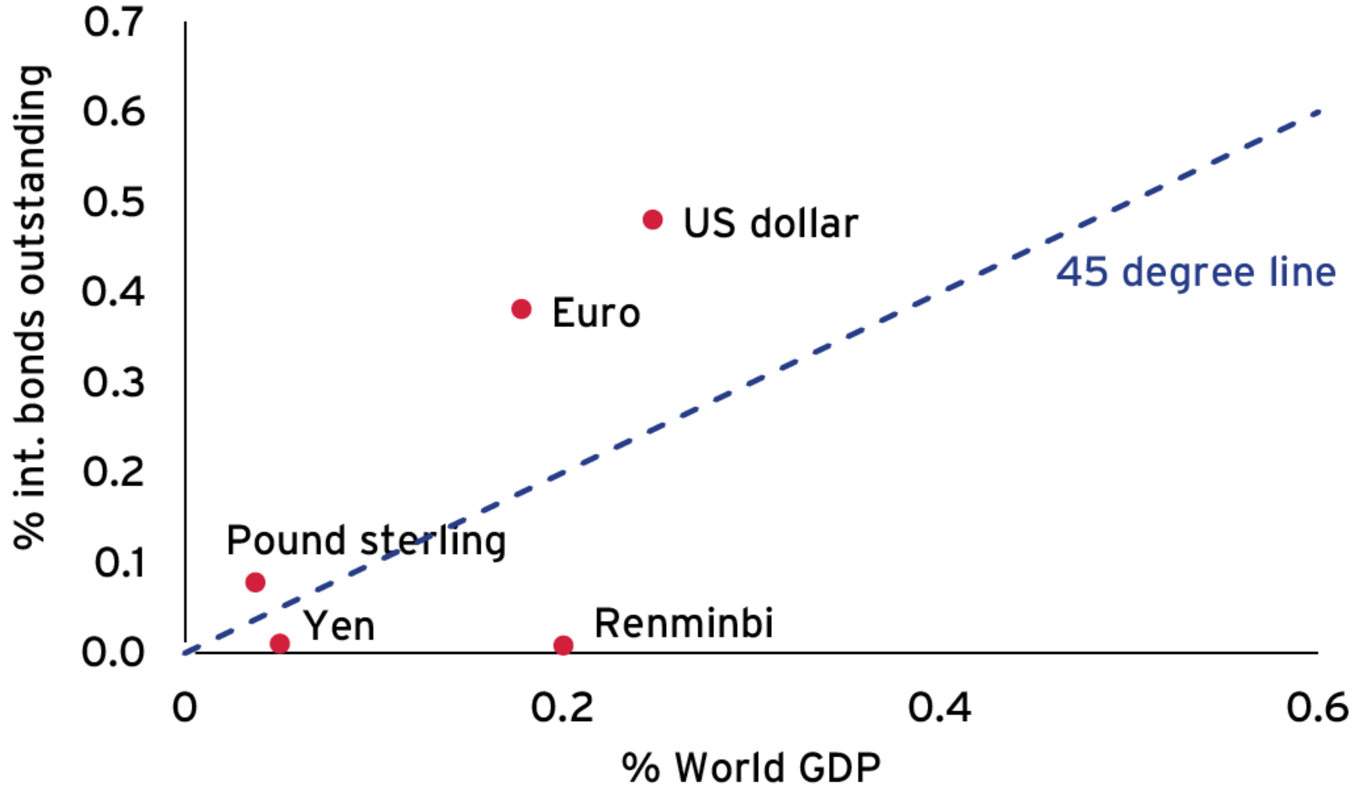




2. The Currency Denomination of Cross-Border Lending

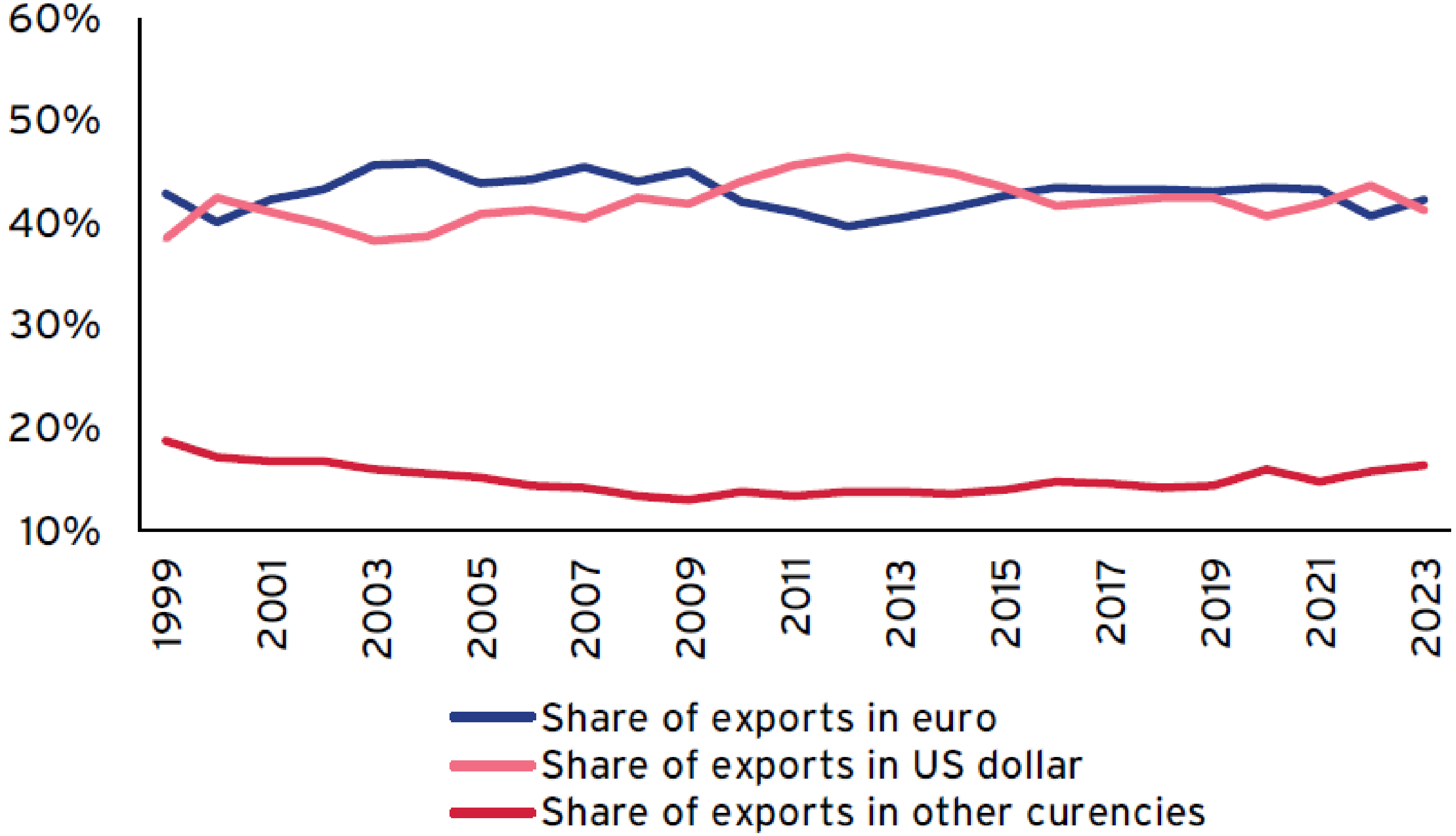
- The dollar and the euro remain dominant.
- Offshore dollar funding markets set the U.S. currency apart.
- Rise in EM borrowing in local currency.

THE OUTSIZED ROLE OF INTERNATIONAL CURRENCIES, 2024



3. International Currencies and World Trade

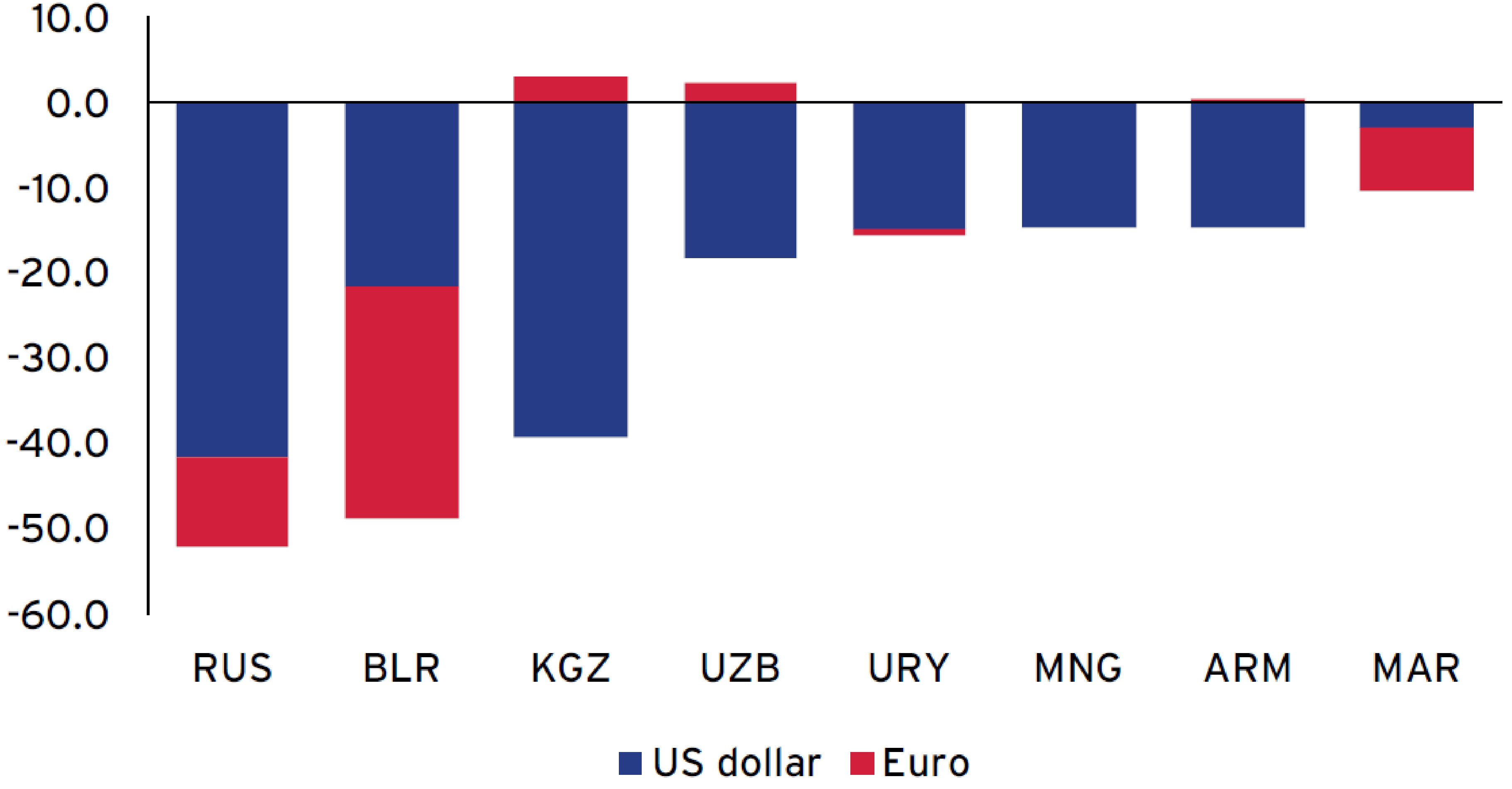
FIGURE 2.7 INVOICING CURRENCY SHARES OF GLOBAL EXPORTS



Source: Boz et al. (2025).

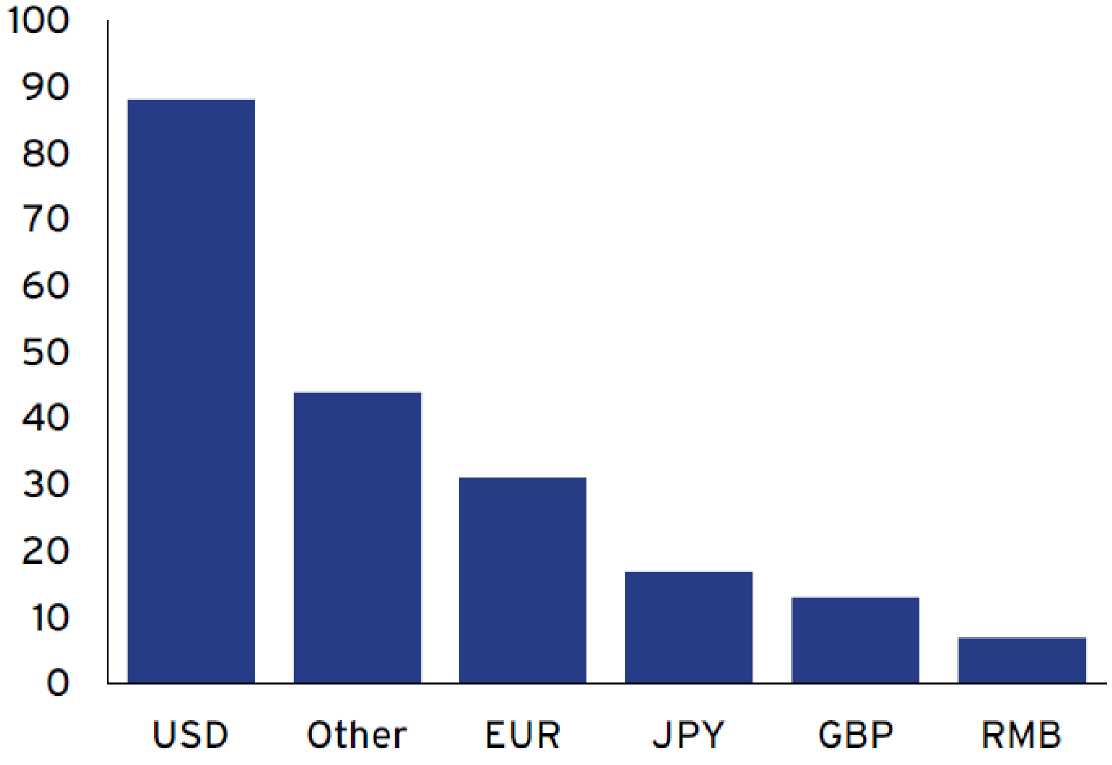
Sanctions drive shifts in invoicing around affected economies

FIGURE 2.9 **CHANGES IN CURRENCY INVOICING SHARES, 2016-2021 (%)**

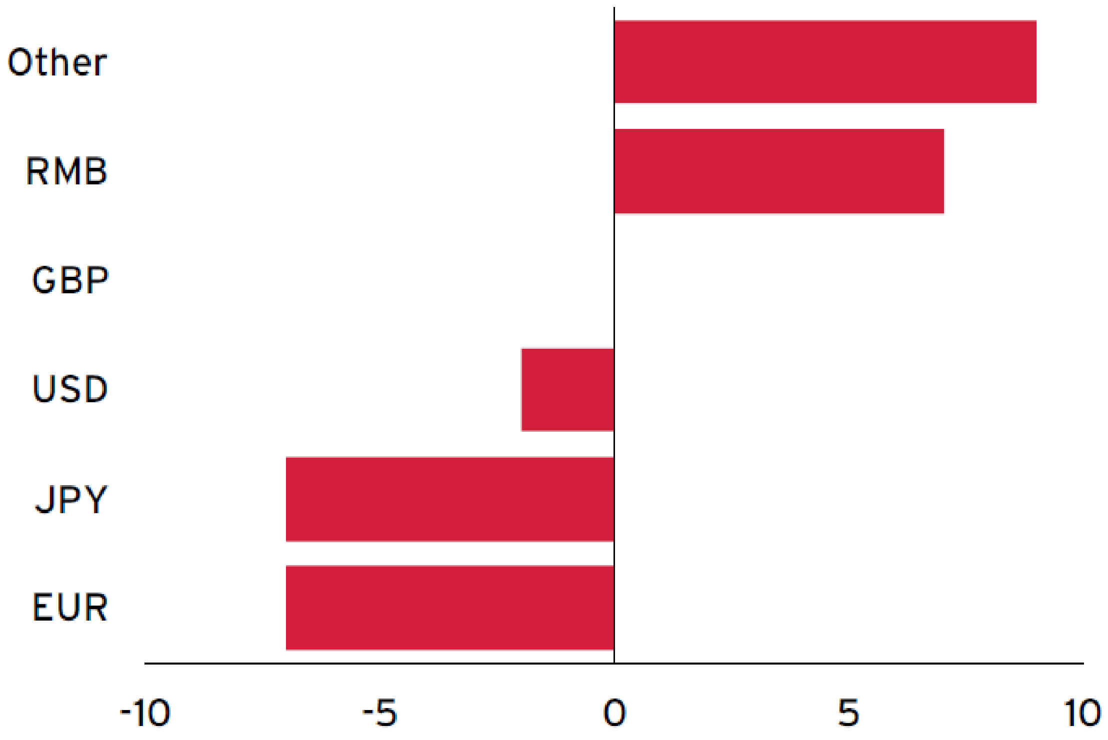


4. International Currencies in Foreign Exchange Markets

a) Share of FX turnover, 2022



b) Change in share of FX turnover, 2001-2022



Source: BIS Triennial Survey.

Conclusions

- Economics generally more important than geopolitics.
  - Rise of **non-traditional reserve currencies** reflects market deepening.
  - **EM local currency borrowing** reflects financial development.
  - More **RMB settlement** of China's bilateral trade.
  - More **trading of EM currencies** as foreign investors hedge local currency exposure.

- But the footprint of geopolitical tension is evident in some areas
  - A few (very few) countries have reallocated reserves away from the dollar.
  - Sanctions have affected patterns of trade invoicing for the economies directly affected.

Thank You!