

End of the dollar era

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CHAKLADER MAHBOOB-UL ALAM

CONFRONTATIONAL words have recently been exchanged between the United States and China over their respective currencies. During Mr. Geithner's confirmation process as the new treasury secretary, in a written reply to a question raised by Senator Schumer from New York, Geithner said: "President Obama, backed by conclusions of a broad range of economists, believes that China is manipulating its currency."

This brought a quick response from China. Mr. Zhou, the governor of China's central bank, insinuated that China might want the US dollar to be replaced by a new "super sovereign reserve currency," called SDRs, as the world's reserve currency, i.e., to move to a global reserve currency with a stable valuation benchmark that will not belong to any single nation.

Even though, since then, both sides have toned down their confrontational language serious doubts about the sustainability of the US dollar as the world's predominant reserve currency in the future have been expressed by

some experts.

Thanks largely to the profligate spending habits of the Americans, China has built up huge trade surpluses over the last decade. At the same time, there have also been substantial inflows of foreign capital. As a consequence of these two phenomena, billions of dollars have flooded into the country during this period.

Under a floating exchange rate system the value of China's currency would have risen, making its exports more expensive. China's exports would therefore, have declined.

On the other hand, for the same reason, imports would have become cheaper and therefore would have risen. But in order to continue with the export-based economic development of the country, China pursued a policy of keeping the value of its currency as low as possible. To achieve this objective, China often intervened in the foreign exchange market.

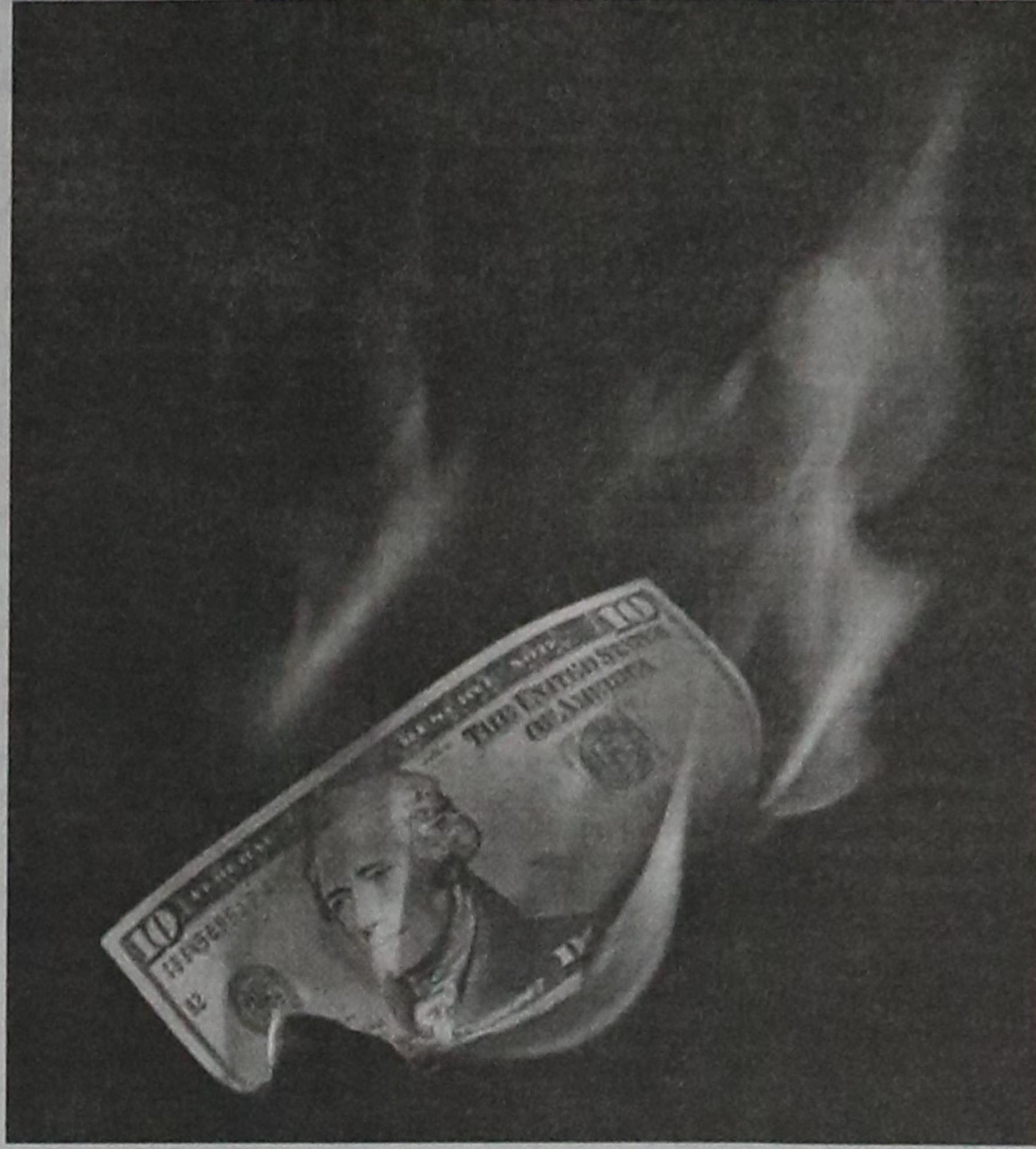
American consumers became addicted to China's cheap products and China became dependent on America's over-consumption to finance its rapid industrialisation. Thus, the trade gap

between the US and China kept growing. In the process, China also piled up a huge amount of American currency. Now the Chinese leaders were faced with a problem: What to do with the mounting pile of dollars?

Besides buying and stockpiling commodities like iron ore, crude oil, grain, gasoline, diesel and sugar, which are priced in dollars, China has been using part of its stockpile to increase its gold reserves (recently published statistics show that Chinese gold reserves have grown to 1054 tons from 600 tons in 2003). But most of its stockpile of dollars was used to satisfy America's ever-increasing addiction to debts (budget deficits, bank bail-outs etc.) by buying up different types of US government bonds. Thus, China turned itself into America's largest creditor.

After the recent sub-prime mortgage meltdown in the US, the Chinese have been concentrating more on US Treasury bonds by getting rid of the debt of US government-sponsored organisations like Fannie Mae and Freddie Mac and buying more Treasuries. The result has been a huge stockpile of US Treasury bonds -- nearly \$2 trillion -- in China's hands.

Actually, the size of China's dollar holdings has become a major problem for both the governments. If China feels that it is becoming too risky to lend any more money to the US government and cuts back drastically on its purchases of US treasury bonds, it would cause the interest rates in the US to rise -- delaying



But as long as China runs a big current account surplus its reserves will rise. In order to keep the value of the yuan low, a significant part of its reserves will be kept in dollars. If it wants to reduce the size of its dollar holdings by selling part of it, it will cause the value of the dollar to fall, which would in turn cause a huge capital loss for China.

This extraordinary situation has led many experts to wonder how long the dollar will be able to maintain its position as the world's major reserve currency.

As Prof. Kennedy of Yale University has pointed out: "The United States possesses around one-fifth of the world's GDP, but its own paper provides around 75% of world's exchangeable currency reserves. This is a worrying imbalance, especially when Washington is relying upon foreigners to cover its enormous federal deficits. This is an obvious capitalist contradiction -- that is, when the national forces of production differ so markedly from international shares of tradable currency, something is going to crack. And that something will be the latter."

I tend to agree with Professor Roubini, one of the very few American economists who saw through the bubbles and predicted the crisis long before the actual meltdown, when he says: "While the dollar's status as the major currency will not vanish overnight, we can no longer take it for granted. Sooner than we think, the dollar may be challenged by other currencies, most likely the Chinese renminbi."

Chaklader Mahboob-ul Alam is a Daily Star columnist.

Useful no more?

the economic recovery of the country and perhaps that of the world.

On the other hand, China has found itself in a catch-22 situation. It wants to

maintain the value of its dollar investments steady and lower its dollar exposure but, at the same time, wants to keep the value of the yuan as low as possible.

The coming "jaw-jaw"

Indo-Pakistan talks are sure to be resumed. But it is hard to find a basis for expecting success -- unless the Indians accept the ideas that Pervez Musharraf floated in recent years.

M.B. NAQVI

DR. Manmohan Singh has formed another government and his party looks like lasting the next five years with little real challenge. There are expectations in both India and Pakistan that talks between the two estranged neighbours will resume soon. What is to be expected?

The Indians and Pakistanis have been

talking with each other for long. They have also fought three wars and two major skirmishes. Indo-Pakistan negotiations began from the days of Jawaharlal Nehru and Liaquat Ali Khan.

These were meaningful and resulted in concrete agreements that held for long. After that, the Kashmir dispute has made the relationship complicated. Even so, the various Pakistan rulers kept saying to Indian government leaders:

"Let's settle this issue in our lifetime; otherwise it will be very hard to find a solution."

Prime Minister Mohammad Ali of Bogra, for instance, carried a message of good wishes of Governor General Ghulam Mohammad with him. Nehru listened and listened some more, but the effort failed. Other emissaries from Ghulam Mohammad also went to Delhi but nothing succeeded.

When Ayub Khan came to power, the impulse to suggest agreements to India had not subsided. Ayub Khan briefly met Jawaharlal Nehru at Karachi Airport and proposed joint defence between Pakistan and India, apparently off the cuff. Nehru's reply was sharp and crisp: "Joint defence against whom?"

Thereafter, there was little communication between India and Pakistan until 1964, when marathon talks between Sardar Swaran Singh and Zulfikar Ali Bhutto went through six rounds.

Although a more or less authentic rumour said that a format for final agreement had been arrived at in the last round, no agreement emerged. The 1954 volte faced by Nehru on the question of agreed plebiscite in Kashmir was decisive. Thereafter, India has kept declaring that Kashmir is an integral part of India.

Nehru's statement of 1954 virtually killed all prospects of a peaceful Kashmir settlement, though, for Pakistanis, Kashmir was the main dispute. If talks did not succeed, war between the two countries was likely. And it did come soon enough -- in 1965 -- and was fairly decisive. Foreign diplomats said: "After this there will be no war over Kashmir, though wars might take place on other

issues."

The East Pakistan crisis brought on the second India-Pakistan war, which Pakistan lost even more decisively. East Pakistan became Bangladesh as a result. Pakistan lost some land in West Pakistan and gave too many POWs to India.

Pakistan had to agree to all the terms India dictated. A year and a half after this war, Zulfikar Ali Bhutto and Mrs. Indira Gandhi signed the Shimla Agreement in July 1972. That ensured stable peace for 18 long years.

One of the byproducts of the 1971 war was Islamabad's renewed determination to get even with India. The thinking was simple. The only way to equalise was to go nuclear. The whole world at the time thought that possession of nuclear weapons meant acquiring a deterrent.

Bhutto started, or rather intensified, an old atomic plan, and he made two agreements. The first was with France to buy a reprocessing plant so as to obtain plutonium, the raw material for the Bomb. The second was to make Canada help build Karachi's nuclear power plant.

But Pakistan's atomic program was greatly helped later by finding a new route to the Bomb; by enriching uranium. Dr. Abdul Qadeer Khan set up an enrichment plant and succeeded in producing highly enriched uranium that could and did make the Bomb. Bomb-making itself is no great deal, but one has to have enriched uranium or plutonium, which are hard to obtain.

In 1984, Dr. Qadeer Khan disclosed that Pakistan had mastered the technology of enriching uranium. Later reports said that, in fact, Pakistan had made the first Bomb in 1984. In any case, Pakistan was

able by November 1986 to threaten India with a nuclear riposte if it did go ahead with the rumoured invasion of Pakistan under cover of the Brasstacks Exercise. The deterrence associated with the still-unacknowledged Bomb worked.

Both India and Pakistan implicitly believed that nuclear weapons were the ultimate weapons, and possessing them made one immune from any serious threat. This illusion of nuclear bombs providing reliable deterrence lasted until 2002 when Indian ideas changed, though not before India had suffered a whole decade of jihad in Kashmir, which inflicted heavy casualties on Indians and Kashmiris.

Pakistan's strategy was to inflict a thousand cuts on India in the assurance that it would not employ either its superior conventional forces or its own nuclear weapons against it.

Pakistan had also teamed up in the 1970s with the west in overthrowing a pro-Soviet regime in Kabul -- a regime which the west saw as having violated the hoary understanding between Britain and Czarist Russia in which Afghanistan was to remain a neutral buffer state permanently. Those rules of the famous Great Game had survived 1917 Russian Revolution and the passing of the sceptre of western imperialism from UK to the US in 1946.

The US and UK refused to allow it and went to war to detach Afghanistan from the Soviet sphere, in which highly anti-Soviet (Islamic) manpower was provided by Pakistan while the west provided money, equipment, logistics and guidance.

Pakistan helped win this war. In the

process, Islamabad learnt the technique of asymmetrical warfare and acquired 200,000 to 300,000 trained holy warriors -- the mujahideen -- whom it later employed in Kashmir in the 1990s. Now these men are a great nuisance because they have become allies of a later version of the mujahideen -- the Taliban. Pakistan was hoisted on its own petard.

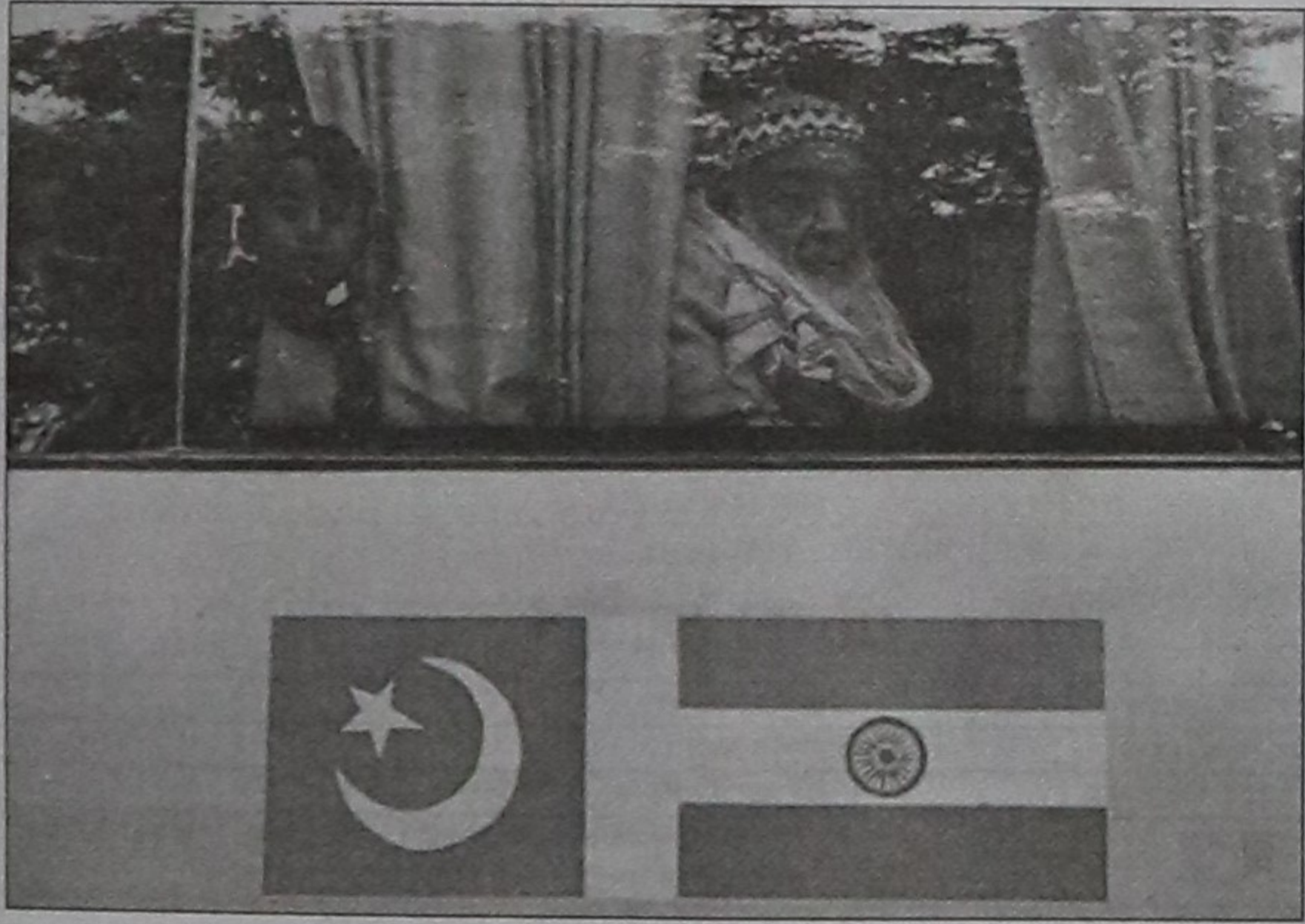
But after 1989, the mujahideen had nothing to do and could be employed in Kashmir, so thought the adventurous Pakistani generals. For the warriors it was a jihad and Pakistan served its own purposes of trying to oust India from Kashmir. Holy warriors were sent into Kashmir after the Afghan jihad. This jihad, jointly with Pakistani volunteers, kept India engaged in irregular warfare for over a decade, and ended in mid-2002. But this design failed.

The point to note here is that the Indian leadership did overcome both its fears and restraint. Indian PM A. B. Vajpayee ordered the Indian army to invade Pakistan despite its Bomb. How did the Indians get rid of their fear of Pakistan's nuke deterrence?

The Indians claimed that Pakistan did not pose any threat to India because India had a larger stock of nuclear weapons. These two deterrents cancel each other out. The only effective instrument in a war would be the conventional forces, in which India had the undoubted superiority.

Indo-Pakistan talks are sure to be resumed. But it is hard to find a basis for expecting success -- unless the Indians accept the ideas that Pervez Musharraf floated in recent years.

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Talk for peace.

The government's prerogative to act

Some observe that the government is occupied with lesser matters, turning a cold shoulder to our mundane woes. But, it has the prerogative and responsibility to decide priorities as per its vision, with regard to the inherited mess and the myriad issues that afflict the citizenry.

MD. ALI AKBAR

THE PM, with experience of governing in her first stint in power, is well aware of what she is supposed to do in this term. She knows about her job, and launched her fresh stint with a new-look cabinet amid plaudits, thus making a good beginning. And then, her government has gone about doing what it deems fit to bring in order and put the polity back on the rails. Without debating the degree of success till date, we ought to agree that the government is keen to get its act together.

Some observe that the government is occupied with lesser matters, turning a cold shoulder to our mundane woes. But, it has the prerogative and responsibility to decide priorities as per its vision, with regard to the inherited mess and the myriad issues that afflict the citizenry.

Undeniably, the government has no

way to ignore the hard issues of everyday life, whatever else it does. At the same time, it is pledge-bound to let the rule of law prevail, right the piled up wrongs, and deliver justice in cases where it was denied by the previous regimes. So, water, power, et al, are not just what governance is all about.

With many knotty issues, including the BDR conundrum, it has to carve a way-out by handling them adequately. The government, presumably, knows what to do, what not to do, and when to do, just as "the weaver knows best where the shoe pinches."

But some tend to complain that the government has busied itself with more tricky issues than it, perhaps, is capable of dealing with. Some others charge it with opening up some old riddles that they say have potential to trigger new controversies. Should the government, then, sleep over illegal arms trafficking, abuse of public money, and grenade

attacks?

The opposition denounces the government for bringing up some non-issues (?) and straying from the pressing crises of water and power. In fact, the government is quite concerned about ending these problems, which are, admittedly, none of its making.

Strangely, the opposition leader alleges that the government is selling off sovereignty by deciding to join the "Asian Highway," whereas experts foresee big economic gains from the highway connectivity. Given the democratic right, the opposition must criticise and put public welfare concerns in the forefront, but it must be guided by pragmatic thinking rather than a jaundiced view of everything.

Some other steps by the government have drawn cynical reactions. The government is often blamed for politicising administration as it seeks to inject dynamism in its functioning by reshuffling. The blame seems ill-conceived, as the government has to remedy the mismatch in administration owing to the much-discussed, wholesale politicisation by the jote regime.

In all fairness, the officers who are competent and aligned with the government's scheme of working need to be placed in the right positions. The government has taken upon itself to do

justice to those who had been politically or otherwise victimised previously.

As is the case with a new government, officers of proven capability and reputation are being placed in sensitive positions. It is worthwhile to transfer the underperformers to the lesser spheres, and to put aside the recalcitrant who impede rather than help implement policy decisions.

Then, there is the long pending issue of the '71 war crimes trial. Our yearning for the promised trial must be fulfilled, which only the anti-independence elements will disrelish. A quarter is playing it out as a ploy to divide the nation. Is that not aimed to forestall the long-awaited trial? How long will the unmitigated, emotional burden of failing to punish the war criminals torment the national psyche?

Those who have had to so long suppress their heart-burning for avenging the brutal killing of their loved ones in 1971 will have solace after due punishment is meted out. As the nation has woken up to the issue, holding the trial will further cement our national bonds.

Next, follow the ongoing re-investigation of the mysterious 10-truck load of arms, and dastardly bombings at public rallies and cultural gatherings. As the enquiries are digging out incredible



So much to do.

details of criminal apathy to putting the culprits on trial, the wisdom behind the move is being widely hailed.

Then, faced with the re-emerging threat of militancy, the government's clampdown on Islamic extremists and the hunt to uncover their networks and hideouts have been pretty relieving. But the opposition leader accuses the government of undermining our global image through

frantic anti-militant operations. Could the government stay blind to the menace? Should the militants be given a free rein?

Ultimately, won't we be benefitted if the administration is attuned to deliver, the motherland is connected with other Asian countries, and the scourge of militancy and the despicable legacy of misrule and injustice are removed?

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