Economy

Dollarisation and Economic Shifts

Tags:

- **GS Paper - 2**
- **Effect of Policies & Politics of Countries on India's Interests**
- **GS Paper - 3**
- **Monetary Policy**
- **Liberalization**

For Prelims: Dollarisation, Inflation, Exchange rates, Monetary policy, De-dollarisation, India's Trade agreements, Special Vostro Rupee Accounts

For Mains: Major Challenges Related to Dollarisation, Reasons for Rise in De-dollarisation Practices.

Why in News?

Argentina, plagued by **severe inflation and widespread poverty, faces a pivotal moment. Dollarisation is** seen as a **potential remedy for the country's economic challenges.**

- The recently elected President of Argentina promises to replace the **Argentine Peso with the dollar. However,** the immediate implementation of dollarisation seems unlikely due to the scarcity of dollar reserves in Argentina.
- **Dollarization** is the **use or adoption of the United States Dollar** as the primary currency in a country**, replacing or supplementing the local currency.**

How Dollarisation can Save an Economy?

- **Stabilizing Inflation:** Dollarisation can potentially **curb hyperinflation by introducing a stable**

currency, breaking the cycle of rising prices fueled by uncontrolled money supply. This stabilization fosters confidence in the economy, encouraging investment and consumer spending.

- **Enhanced Trade Opportunities:** A dollarized economy incentivizes **a focus on export-oriented strategies.**
    - With a stable currency, **foreign investors are more inclined to engage,** fostering foreign trade. This orientation towards exports can bolster economic growth and stability.
  - **Long-Term Planning:** A stable dollar value allows for better long-term economic planning. Businesses, **both local and international, can make more accurate forecasts** and investments without being hindered by the volatility of a depreciating domestic currency.
- **Reduced Speculative Risks**: Dollarisation can **mitigate speculative risks associated with fluctuating exchange rates.**
    - This stability can attract foreign investors, as they perceive reduced risks, ultimately promoting capital inflow and economic growth.
- **inancial Discipline:** By **relinquishing control of monetary policy, dollarisation forces governments to rely on fiscal policies for economic stability.**
- **This shift may encourage more prudent fiscal management**
    - , potentially curbing government overspending and promoting **economic discipline.**

Experience of a Fully Dollarized Economy: Ecuador

- Ecuador's journey provides valuable insights. Despite **initial political upheaval** following dollarisation in **2000**, the **nation experienced significant economic progress.** Reduced inflation rates, lowered debt ratios, and improved social welfare showcased the potential benefits of such a move.

- However, **Ecuador's success was not solely due to dollarisation.** Booming oil and gas reserves during the 2000s contributed significantly to economic growth. Furthermore, expanded government intervention and social spending played a crucial role in sustaining prosperity.

What are the Major Challenges Related to Dollarisation?

- **Policy Constraints:** Dollarisation significantly **limits a country's ability to independently manage monetary policy.**
    - Loss of **control over money supply** and interest rates can hamper the government's capacity to respond to economic downturns.
- **Economic Shock Vulnerability:** With a fixed currency, **dollarized economies might become more vulnerable to external economic shocks.**
    - They lack the flexibility of adjusting exchange rates to counterbalance sudden changes in the global economic environment.
    - The situation in Greece is a warning example of issues associated with adopting a foreign currency.
        - Although there was some **growth after Greece started using the euro**, the **Eurozone crisis** showed the problems of using a currency without having control over its policies.
        - Greece had to accept **strict budget cuts** and financial help in return for using the euro.
- **Limited Export Competitiveness: Loss of control over the exchange rate** can restrict a country's ability to **use currency devaluation as a tool to enhance export competitiveness.**
- **Inability to Address Internal Imbalances:** Dollarisation **may not address internal structural issues within the economy.**

- Dependency on a foreign currency might **overshadow the need for internal reforms**, such as **productivity improvements or addressing income inequality,** crucial for sustained economic development.

Note

In 2022, the IMF observed that central banks around the globe **were not maintaining the same levels of reserves in the US dollar,** as they had done in the past.

What is De-dollarisation?

- **About: De-dollarisation** refers to a **deliberate or unintentional process** undertaken by a country or region to **reduce reliance on the US dollar** in its financial system or economy.
    - This can involve various measures aimed at decreasing the use of the dollar in **transactions, reserves, trade,** or as a standard for pricing goods and services.
- **Reasons Associated:** Governments might **pursue de-dollarisation for several reasons,** such as reducing **exposure to the impact of US monetary policy, asserting economic sovereignty, mitigating the effects of dollar fluctuations,** or seeking greater independence in global finance.
- **Strategies for De-dollarisation:** It can include diversifying currency reserves, promoting the use of alternative currencies in trade agreements, **establishing currency swap agreements, or encouraging the use of regional currencies** in financial transactions.
    - For instance**, in March 2023,** the RBI put in place the mechanism for rupee trade settlement with as many as 18 countries.
        - Banks from these countries have been allowed to open Special Vostro Rupee

Accounts (SVRAs) for settling payments in Indian Rupees.

Conclusion

Dollarisation, when **coupled with effective domestic policies**, can pave the **way for economic success**. However, Its efficacy **hinges on nuanced policy execution**, balancing the advantages of **stability** with the need for independent economic strategies.

UPSC Civil Services Examination Previous Year Question (PYQ)

Q. Recently, which one of the following currencies has been proposed to be added to the basket of IMF's SDR? (2016)
(a) Rouble
(b) Rand
(c) Indian Rupee
(d) Renminbi
Ans: (d)

Biodiversity & Environment

Global Marine Life and Oceans Warming

Tags:

- **GS Paper - 3**
- **Environmental Pollution & Degradation**

For Prelims: Tropicalisation, Climate Change, Oceans Heating, Mediterranean Sea, Greenhouse Gas Emissions, Coral Bleaching, Solar Radiation.

For Mains: Impact of ocean warming and sea level rise on marine biodiversity.

Why in the News?

Recently, a study published in the journal **'Trends in Ecology and Evolution'** highlighted that climate change is making the oceans warmer, and as a result, **tropical marine species** are shifting from the **equator towards the poles.**

- The **temperate species** are receding as it gets too warm, they face **increased competition** for **habitat,** and **new predators.**

How Does Climate Change Cause Tropicalisation as per the Study?

- **Tropicalisation:**
  - **Climate change** is causing a **marine phenomenon** known as **tropicalisation,** where **tropical species** expand their range while **temperate species retract.**
    - **Temperate species** are receding as it gets too warm, they face **increased competition** for **habitat**, and **new predators** arrive on the scene.
  - This **global shift** is altering ocean ecosystems, biodiversity, and could **impact the global economy.**
  - The first instance of this process was identified in the Mediterranean Sea.
  - The **Mediterranean Sea** is considered as a **"tropicalisation hotspot"** due to an increase in tropical species.
- **Species Dispersal due to Climate change:**
  - **Climate change** has altered the **physical factors** that affect species dispersal, such as ocean currents in areas that **separate tropical/subtropical** and temperate regions.
  - These **warm-water boundary currents** are heating faster than the global seawater average, facilitating the **poleward movement of species,** and reinforcing the **retraction of temperate species.**
  - **Example:** Range-expanding tropical damselfishes and temperate reef fishes have been documented

altering their feeding and social behaviors to allow for coexistence,

- **Evolution of New Traits:**
  - Changes in how species interact can result in the evolution of new traits or behaviors due to the close connection between **ecology** and **evolution**.

What is Ocean Warming?

- **About:**
  - The **ocean absorbs** most of the excess heat from greenhouse gas emissions, leading to **rising ocean temperatures.**
- **Reason:**
  - **Greenhouse Gas Emissions:** The burning of fossil fuels (coal, oil, and natural gas) for energy, deforestation, and industrial processes releases significant amounts of greenhouse gasses, including carbon dioxide (CO_2), methane (CH_4), and nitrous oxide (N_2O), into the atmosphere. These gases trap heat, leading to a **warming effect** on both the atmosphere and the oceans.
  - **Carbon Dioxide Absorption:** Oceans act as a vast reservoir that absorbs a significant portion of the excess **carbon dioxide** from human activities. While this absorption helps mitigate climate change on land, it also results in the **warming of the ocean itself.**
  - **Solar Radiation:** Changes in solar radiation, though a minor contributor compared to human-induced factors, can influence ocean temperatures over long periods.
  - Impact:
  - Coral Bleaching: Elevated temperatures can cause corals to expel the symbiotic algae living in their tissues, leading to coral bleaching.

- Prolonged bleaching weakens corals and makes them more susceptible to diseases, posing a significant threat to **coral reef ecosystems.**
- **Sea Level Rise**: **Warmer ocean temperatures** contribute to the **thermal expansion of seawater.** This, along with the melting of polar ice caps and glaciers, leads to rising sea levels, which can result in coastal erosion and increased **vulnerability of coastal communities.**
- **Disruption of Marine Food Webs:** Changes in **ocean temperatures** can alter the **distribution** and abundance of marine species, affecting the structure of marine food webs. This can have cascading effects on fisheries and the **livelihoods of communities** dependent on them.
- **Ocean Acidification:** The absorption of **excess carbon dioxide** by the oceans leads to **ocean acidification**. Acidification can harm marine organisms with **calcium carbonate skeletons or shells,** including **corals, mollusks,** and some **plankton,** affecting the entire marine food chain.

Conclusion

Global marine species shift due to climate-induced tropicalization, exemplified in the Mediterranean as a "hotspot." Ocean warming from factors like greenhouse gasses causes coral bleaching, sea level rise, and disruptions to marine food webs. Threatening biodiversity, coastal communities, and economies, urgent climate mitigation is crucial to preserve ocean health.

UPSC Civil Services Examination, Previous Year Questions (PYQs)

Mains

Q1. Assess the impact of global warming on the coral life system with examples. (2017)

Q2. 'Climate change' is a global problem. How India will be affected by climate change? How Himalayan and coastal states of India will be affected by climate change? (2017)

Q3. Discuss global warming and mention its effects on the global climate. Explain the control measures to bring down the level of greenhouse gases which cause global warming, in the light of the Kyoto Protocol, 1997. (2022)