

A BRICS Reserve Currency?

Description

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The new BRICS reserve currency can act in concert with the stronger role performed by BRICS national currencies to take on a greater share of the total pie of currency transactions in the world economy, writes Valdai Club Programme Director [Yaroslav Lissovolik](#).

The issue of the creation of a BRICS reserve currency has taken on particular significance in recent months after President Putin declared that the creation of such a currency was in the process of discussion. This was followed by a series of statements coming from Russia's legislative branch on the expediency of creating a new reserve currency — most recently from the Federation Assembly speaker Valentina Matvienko. While the debate on the possibility of creating such a reserve currency is only starting in Russia and more broadly across the global economy, the implications of such a move on the part of the BRICS could have transformational consequences for the global financial system. [category economics/statistics]

Initially, the proposal to create a new reserve currency based on a basket of currencies of BRICS countries [was formulated](#) by the Valdai Club back in 2018 — the idea was to create an SDR-type currency basket composed of BRICS countries' national currencies as well as potentially some of the other currencies of BRICS+ circle economies. The choice of BRICS national currencies was due to the fact that these were the among the most liquid currencies across emerging markets. The name for the new reserve currency — R5 or R5+ — was based on the first letters of the BRICS currencies all of which begin with the letter R (real, ruble, rupee, renminbi, rand).

The recent debates concerning the prospects for the creation of a new reserve currency focused more on the risks, fragilities and outright impossibility of the R5 project. Less attention has been accorded to estimating the benefits (including in terms of hard figures) to BRICS economies and EM more generally. There has also been scant attention with respect to the actual modalities of launching the BRICS reserve currency.

What is clear at this stage is that the BRICS reserve currency will not be created to replace the national reserve currencies of the BRICS economies — rather it will complement these national currencies and

will serve to improve the possibilities for more EM currencies to attain reserve status. Accordingly, the attainment of high trading shares among the BRICS economies is a desirable but not altogether an indispensable condition for launching the new reserve currency. In fact, the new BRICS currency does not have to service all trade transactions among BRICS economies in the very near term. Initially, the new BRICS currency could perform the role of an accounting unit to facilitate transactions in national currencies. In the longer run, the R5 BRICS currency could start to perform the role of settlements/payments as well as the store of value/reserves for the central banks of emerging market economies.

Within the composition of the R5 currency basket the share of the Chinese renminbi may be initially set at a relatively high level in order to take advantage of the already advanced reserve status of the Chinese currency. This share may be reduced progressively in stages later on along with the inclusion of new EM national currencies. Outside of the BRICS economies some of the potential candidates that with time could be included into the R5+ currency basket may feature the Singaporean dollar or the UAE's dirham.

One of the potential risks associated with the use of EM currencies in reserves is their high volatility. The basket mechanism of the BRICS reserve currency will allow for reducing some of this volatility via averaging out the exchange rate dynamics of currencies that follow different market trends — if the currencies of Russia, South Africa and Brazil follow the commodity cycle, the opposite is true with respect to commodity importers such as India and China.

Importantly, the scope for employing the new reserve currency in the world economy is sizeable given the tremendous potential for de-dollarization. The new BRICS reserve currency can act in concert with the stronger role performed by BRICS national currencies to take on a greater share of the total pie of currency transactions in the world economy. This greater role can be gradually extended from servicing foreign trade transactions to investment flows across the developing world. In line with the original R5 concept developed by Valdai Club in 2018 one of the possible venues for boosting the use of national currencies and the BRICS reserve currency could be the creation of a platform for regional development banks in which BRICS economies are members. Such a platform could develop a portfolio of common/integration projects that may be financed in national currencies.

In the end, the launching of a new reserve currency if successful will impart a transformational effect on the international financial system. The Central Banks in the global economy are experiencing a notable shortage of reserve currencies in managing their reserve holdings. In this respect, the emergence of additional reserve currencies from among the EM economies will serve to expand the possibilities for diversifying reserve holdings and reducing the vulnerabilities associated with the dependence on a narrow range of currencies. The R5 project can thus become one of the most important contributions of emerging markets to building a more secure international financial system.