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Editor's note: As a futurist, **Academy Fellow Hazel Henderson** tries to anticipate surprises. She notes that one such surprise scenario is rooted in the close relationship between oil, dollars, gold, and Europe's euro currency. Currency markets have become very volatile and dependent on the expectations about the future of millions of their investors and speculators. Many curved balls may be in store for the US as countries that formerly held mostly US dollars in their currency reserves begin to diversify into euros as they are perceived to be less risky. **J.S.**

Iraq, the Dollar and the Euro

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Futurists, like me, specialize in "what if" scenarios, outside the box thinking, and trying to anticipate surprises. In even the best-laid human plans, events rarely unfold as predicted -- even by experts. Mostly, these surprises are the result of "blind spots," or because experts use different models or specialized approaches and languages -- making communication difficult. For example, in the unfolding Iraq situation, the Pentagon has its favorite team of re-builders and has clashed with the State Department, vetoing its choice of experts. These competing approaches to Iraq's future are based on different mindsets and skills. Without an integrating overview surprises are more likely.

One such surprise scenario is rooted in the close relationship among oil, dollars, gold and Europe's euro currency. Remember back in 1973, OPEC countries quadrupled the price of their oil and tied it to the US dollar. Over the years, this flooded the world with "petro-dollars," which were recycled through banks as loans. The US dollar reigned supreme as the world's de facto reserve currency. Everyone wanted to own dollars, which were considered as good as gold (even though, since 1972, dollars cannot be redeemed for gold, after President Nixon shut the gold window).

Gold no longer backs the dollar or any other currency. All currencies since 1973 are called "fiat" currencies, backed only by the faith that markets have in a country's government and its economic fundamentals. Central banks that used to keep gold bars in their vaults now have sold much of their precious metal. Now, they try to "manage" their currencies by raising or lowering interest rates, buying and selling them in the open market and other techniques. Gold, for jewelry and as a safe haven, is still popular and trades actively on the world's commodity and futures' exchanges, along with platinum, oil, hogs, coffee, sugar -- and fiat currencies themselves.

These currency, oil and gold markets have become very volatile -- dependent on the expectations about the future of millions of their investors and speculators. Their collective speculations on the future -- of Iraq, US foreign policy toward Israel, Palestine, the Mid-East; oil supplies and exploration, alternative energy sources and technologies (like hydrogen and fuel cells recently espoused by President Bush), the rise of China as the world's manufacturing giant, the expansion of the European Union, and the weather (a big factor in energy consumption) -- all drive today's global financial markets, including the $1.5 trillion of daily currency trading (mostly speculation) in this unregulated "global casino."

In the past year, the US dollar has lost some 20% of its value against the European euro. The Bush Administration has played up the bright side: this cheaper dollar makes it easier for US exporters to sell abroad. The US needs to increase its exports because it has imported its way to a whopping trade deficit (currently at 5.2% of our GDP). Former Treasury Secretary Paul O'Neill dismissed this as "a meaningless concept." But global investors and currency speculators take it seriously, along with the bursting of the US stock market bubble, accounting scandals, heavily indebted corporations and consumers, our almost zero savings rate, the increasing budget deficits due to Bush's tax cuts and the buildup of military spending, the Iraq war, and the new Bush doctrine of preemptive attacks on any country that might threaten our future national security. So they started unloading dollars and US assets. No surprises here.

But the deeper scenario holds many curveballs for the US as countries that formerly held mostly US dollars in their currency reserves began to diversify into euros, where they perceived less-risky fundamentals: Europe's trade surplus, higher rates of savings, less-risky foreign commitments, etc. Furthermore, many countries oppose US military "unilateralism", the Iraq war (which many believe was always about oil and breaking OPEC's grip) as well as US bully tactics at the United Nations, trashing treaties on global climate, the ABM, chemical and biological weapons, the criminal court, etc. Their best non-violent protest strategy was correct portfolio diversification -- exchanging some of their dollar reserves into euros.

Today, the euro has taken its place alongside the dollar as the world's other global reserve currency - now accounting for some 35% of global trade and reserve holdings. This new reality makes for a more stable world and takes the unsustainable burden of sole reserve currency off the US dollar. Clearly, with its enormous open-ended commitments in the global war on terrorism and evil, the US economy cannot at the same time continue to absorb most of the world's exports and remain the locomotive of the world's economic growth.

This new situation seems a surprise to the Bush Administration -- still expanding our overseas commitments, re-building Iraq, offering aid packages to Turkey, Pakistan and other countries whose support is sought, and pushing more tax cuts. While Bush tells the US population to continue shopping, traveling and enjoying the American way of life, federal deficits grow, domestic programs are cut, and half of our states are deep in budget crises.

What happens if global investors continue pulling out of the US and the dollar keeps falling? Many market players expect it to fall another 20%. Other countries that have lost money in the dollar's fall may continue buying more euros. The other shoe may drop. OPEC may decide to officially re-denominate their oil in euros (since most of their customers are in Europe anyway). OPEC economists have been considering this "no-brainer" scenario for sound financial reasons even though they feared US wrath and retaliation. Indeed, many believe that the deeper reason for the US attack on Iraq was its decision in 1999 to require payments for its oil for food program in euros. The US (heavily dependent on imported oil) benefits price-wise and in influencing markets through OPEC's US dollar pricing. Iraq's dinar will also be replaced by dollars -- if the US has its way.

Thwarting Bush's global dollar diplomacy and its designs on breaking OPEC's oil pricing power provide additional reasons for OPEC to switch to payments in euros. This would mean that the US would have to buy euros with dollars before it could buy OPEC oil. The dollar would fall further and the euro would rise. The US economy would adjust to $5-a-gallon gasoline (the average world price). The bad news would be a deeper US recession. SUV owners would suffer, while Toyota and Honda would grab more market-share with their 50-60 mpg hybrid cars.

The good news: US exports would flourish, Detroit would accelerate its own fuel-efficient car production, solar and renewable energy technologies would be fully capitalized as a new sustainability sector of the US economy (providing millions of new jobs). And the Bush Administration would have to pull back from its over-commitment to the global war on evil and shift its priorities to funding education, homeland security and federal grants to help states fund their new mandates.

Hazel Henderson is author of *Beyond Globalization, Building a Win-Win World* and other books (see www.hazelhenderson.com)