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الذهب ، الدولار ، الدينار الإسلامي

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المستخلص

الذهب ، الدولار ، الدينار الإسلامي

The Gold, Dollar, Euro, Islamic Dinar and Endogeneity of Money:
Conceptual Framework and Empirical Evidence

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Summary and Conclusion

The speaker addressed the following five issues:

- The fractional reserve banking system and how it creates instability in the financial system.
- The concept of narrow banking and how it closely resembles the Islamic banking system.
- The role of international currency with special emphasis on the dollar and Euro.
- Comparison and contrast between the Euro, the dollar and the gold standard with an emphasis on how the weakness of fiat unbacked money leads to a natural inclination on Islamic money.
- The weakness of a flexible monetary system and how a fixed or gold standard leads to a stable international monetary standard.
- The merits of an Islamic bimetallic system, and how it can be implemented a la the Murabitun.
- The debate on exogeneity and endogeneity of money, It provides empirical evidence from Iran and Pakistan, the two Muslim countries which have officially declared to run their banking system according to Islamic Shariah.

There are many factors in determining whether a currency will be used in other countries. These factors include openness and size of the economy, the macroeconomic policy environment, and the stability of financial markets. After World War II, all these factors boosted the U.S. dollar as a preferred currency of international markets. There has been a gradual shift away from the dollar in the last few decades with the emergence of Germany and Japan as major economic powers and with their markets opening with great earning potential, causing a decline in the dominance of the dollar. Even with such a decline, the dollar remains the most important international currency.

The introduction of the Euro on New Year's Day in 1999 economically integrated an area Europe roughly the size of the United States economy, providing for the first time a potential challenge to us dominant role as the world's major international currency. Its presence has been felt in the international securities markets, with the greatest surge experienced in 1999. For example, the Euro captured 32.9 percent of international money market instruments in 1999 as compared to the previous Euro-legacy currencies, which accounted for 17.2 percent of the same market in 1998. Despite a decline in 2000 of the Euro's share of international debt securities, the Euro is widely used as an alternative to the dollar in these markets.

It is expected that the use of the Euro will increase with respect to the dollar especially as financial markets in the Euro-zone become more integrated and more liquid. This expectation will occur gradually given that transaction costs are lowered over time as the use of the currency increases in international

trade transactions. There are immediate benefits with the introduction of the Euro. To begin with, stability within the Euro-area has increased the costs to businesses associated with exchange rate risk and fluctuation has been removed, and economic growth has been promoted. Growth in the European economy translates to new opportunities for U.S. business. The Euro will also have the unusual quality of not being issued by a single sovereign government. Along with this historical precedent, a part of Europe will have the same currency for the first time since the Roman Empire.

In order to benefit from a currency used internationally, there are uses that must be satisfied by the currency. These uses are as an invoicing currency (to alleviate costs undertaken by that country on the import side), as a reserve currency (to reduce that country's government's costs to borrow funds), and as a substitute currency (to provide seigniorage benefits which may be offset by the cost of instability). Given these roles of a currency as an international currency, the financial benefits derived from these roles are not entirely clear.

Empirical results show that money supply can be an independent stimulus to the economic activity. VBCM Granger causality tests show that money is non-neutral in the short-run, which is consistent with Keynesian and Monetarists macroeconomic paradigms. Monetary policy can contribute to the price stability in Iran because the variations in price level is mainly caused by its own innovations, and not from real output or money supply. The absence of any significant Granger-causality from real output to price level suggests that excess aggregate demand generated by the increase in income be quickly absorbed by an increase in money supply. The Central bank can easily accommodate the government expenditure on socially projects with an accommodating monetary policy. We suggest in this paper that money matters, but monetary policy by itself is not effective unless there is a co-ordination of fiscal, exchange, trade and monetary policies.

The proponents of the monetary union have suggested that it will do much to integrate a region's commodity, factor and capital markets. By increasing regional-wide competition and revolutionizing financial markets, it will encourage regionalization, mergers and takeovers in the Islamic countries' banking sector and business firms. However, monetary union also has costs. Although the introduction of a single currency will simplify trade between Islamic countries, each country will give up the ability to use monetary policy to influence its economy. No individual country's central bank will be able to set monetary policy independently. And no country in the Islamic Monetary Union will be able to adjust its exchange rate vis-a-vis the others. The optimal currency theory suggests three alternative responses to asymmetric shocks. The first is labor mobility - workers in the affected country must be able and willing to move freely to other countries. The second is wage and price flexibility - the country must be able to adjust wages and prices in response to an economic shock. The third is the presence of an automatic mechanism for transferring fiscal resources to the affected country. Even a casual glance at these countries would indicate that none of these conditions is met in a

proposed Islamic monetary union. There are serious cyclical and structural variations among the economies in the Union. Labor mobility is extremely limited not just between Islamic countries, but within them too. Strong labor unions have also contributed to wage rigidity.

To counter the argument that unbacked currency is more effective in preventing and fighting recessions since the money supply can be controlled more easily than the demand for/and supply of gold, El Diwany (1999) counters that it is the banking system's power to create and destroy money that causes monetary volatility. The state would not have to correct the problems if the banks did not create them in the first place. The global supply of gold has increased by an average of less than 3% per year over the last 250 years. The proponent of gold standard states that they are not in favor of a gold-backed currency, but rather of gold and silver *being* the currency. They dismiss the comment that there is only so much gold and silver in the world by saying the "Allah has provided man with enough resources to last until the Day of Judgment". The growth of the economy that results in higher prices for gold and silver relative to other goods, in other words deflation is not bad since the most developed economies are growing at the rate of less than 3% and such gradual growth would only lead to gradual deflation. To bolster this argument, they offer the example of a chicken costing a *dirham* during the early days of Islam which is about what it costs today. No fiat money has ever held its value so well.

Islamic *dinar* will create a stable financial system. Stability in the value of money is an indispensable goal in an Islamic economy. Maintaining a unit of value without inflation-deflation is the most important aspect of a gold standard. The Bank of England maintained a gold standard from 1717 to 1914, while the United States maintained a gold standard from 1914 to 1971. From 1971 to the present, the world witnessed the worst fluctuations in the value of its currency. Trading money for money is prohibited in Islam. Currency trading can be stopped if the world is back to gold standard. If the world is on gold standard, there is essentially one currency. By establishing a Islamic *Dinar*, the Islamic world could eliminate currency fluctuations and establish a fair and stable financial structure in the world. One first step the Islamic countries can do is to quote the prices of primary commodities in Islamic *Dinar* with the rest of the world. Since 1945, dollar is the invoicing currency for dollar. If OIC countries demanded their oil payments in the form of Islamic *dinar*, all the strengths and purchasing power that dollar gains from being the OIC oil producer's invoicing currency would switch to Islamic *dinar*.