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Pivoting from the Dollar: India's Role in the BRICS Strategy for Financial Sovereignty and Local Currency Settlement

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ABSTRACT

The post-Bretton Woods international financial system, characterised by the hegemony of the U.S. dollar, has created systemic vulnerabilities for emerging market economies (EMEs). This paper investigates the persistent challenge of "original sin"—the inability of nations like India to borrow and trade extensively in their own currency—and its profound implications for economic stability and policy autonomy. Focusing on India within the BRICS (Brazil, Russia, India, China, South Africa) framework, this paper argues that the over-reliance on the U.S. dollar for debt issuance and trade invoicing exposes the Indian economy to severe exchange rate risk, imported inflation, and constraints on its monetary policy. Through a comprehensive review of literature and an analysis of India's economic structure, this paper demonstrates how dollar-denominated liabilities and trade settlement mechanisms can amplify external shocks, leading to financial instability. It then critically examines the BRICS bloc's strategic response: the creation of alternative financial institutions like the New Development Bank (NDB) and the Contingent Reserve Arrangement (CRA), alongside a concerted push for a Local Currency Settlement (LCS) system. The paper contends that India's active participation and leadership in these de-dollarisation initiatives are not merely a foreign policy choice but a crucial economic imperative. By fostering a multi-polar currency system, India can mitigate its exposure to volatile capital flows, enhance the international role of the Indian Rupee, and achieve greater economic sovereignty. The conclusion posits that while the path is fraught with challenges, including the U.S. dollar's deep-rooted network effects and internal disparities within the BRICS, India's strategic pivot towards local currency trade is fundamental to securing its long-term growth and development objectives in a multipolar world.

***Keywords**: De-Dollarisation, BRICS, Original Sin, Indian Rupee, Local Currency Settlement, New Development Bank (NDB), Financial Sovereignty, Exchange Rate Risk.*

Introduction

The 21st-century global economic landscape is defined by a gradual but unmistakable shift away from unipolar dominance towards a multipolar distribution of power. At the heart of this transformation lies the BRICS bloc, a coalition of five major emerging economies that collectively represent over 40% of the world's population and a significant and growing share of global GDP. While initially conceived as an investment category, BRICS has evolved into a geopolitical force actively seeking to reshape the norms and institutions of global governance. Central to this ambition is the challenge to the long-standing hegemony of the U.S. dollar, which has served as the world's primary reserve and transaction currency for nearly eighty years.

This dominance, while providing a stable medium for global trade, has created a structural dependency that disproportionately affects nations like India. The core of this dependency is captured by the economic concept of **"original sin"**: the historical inability of most emerging markets to borrow internationally in their own currency (Eichengreen, Hausmann, and Panizza, 2005). Compelled to issue sovereign and corporate debt denominated in U.S. dollars, India, like its emerging market peers, has tethered its economic stability to the fluctuations of a foreign currency and the monetary policy decisions of the U.S. Federal Reserve.

This paper argues that for India, this dollar dependency is not an abstract economic curiosity but a tangible constraint on its development. It creates a perpetual vulnerability to **exchange rate risk**, where a depreciation of the Indian Rupee can precipitate a balance sheet crisis. It fuels **imported inflation** through dollar-invoiced commodity trade, and it curtails the Reserve Bank of India's **monetary policy autonomy**, forcing it to often prioritize currency stability over domestic growth objectives.

In response to these systemic challenges, the BRICS nations have embarked on a coordinated strategy to build an alternative financial architecture. The establishment of the New Development Bank (NDB) and the Contingent Reserve Arrangement (CRA) in 2014 were landmark steps, creating parallel institutions to the World Bank and the IMF. More profoundly, these institutions are at the forefront of a broader push to facilitate trade and investment in local currencies. This paper contends that India's proactive role within this framework is a strategic imperative. The promotion of a Local Currency Settlement (LCS) system and the gradual internationalisation of the Indian Rupee are not just tools for mitigating risk; they are foundational elements of India's ambition to achieve genuine economic sovereignty and cement its position as a leading power in a multipolar world.

This study will proceed as follows: Section 2 reviews the foundational literature on "original sin," dollar dominance, and the initial conception of BRICS as an alternative power center. Section 3 provides a detailed analysis of India's specific vulnerabilities to the dollar-centric system, examining its external debt, trade invoicing patterns, and monetary policy constraints. Section 4 evaluates the BRICS architecture as a solution, focusing on the roles of the NDB, the CRA, and the mechanics of the proposed LCS system. Section 5 discusses India's strategic interests and potential leadership role within these initiatives. Section 6 addresses the significant challenges and roadblocks on the path to de-dollarisation. Finally, Section 7 concludes by summarizing the argument and reflecting on the future of India and BRICS in a rebalancing global financial order.

Literature Review: The Theoretical Underpinnings of Financial Dependency

The current push by BRICS nations towards a de-dollarised financial system is grounded in decades of economic theory and the lived experience of recurring financial crises in the developing world. The literature provides a clear narrative arc, from identifying the core problem of "original sin" to analyzing its consequences and, finally, to conceptualizing institutional alternatives.

- **The "Original Sin" and the Hegemony of the Dollar**

The concept of "original sin," as articulated by Eichengreen, Hausmann, and Panizza (2005), remains the cornerstone of this discourse. They demonstrated empirically that the inability of most countries to borrow abroad in their own currency is a pervasive and persistent feature of the international financial system. This is not necessarily due to a country's history of profligacy or poor policy, but rather to the powerful network externalities of a dominant currency. Global investors prefer to hold assets in currencies that are highly liquid and widely used, creating a self-reinforcing cycle that favors the U.S. dollar. This structural feature creates a fundamental **currency mismatch** on the balance sheets of emerging economies: their liabilities are denominated in a foreign currency, while their assets and revenues are primarily in the local currency.

The literature on currency hegemony further explains the entrenched nature of this system. Prasad (2014), in *The Dollar Trap*, argues that even after the 2008 financial crisis, which originated in the U.S., the dollar's role as a safe-haven asset was paradoxically strengthened. The lack of a viable alternative with financial markets as deep and liquid as those of the United States has meant that countries continue to accumulate dollar reserves, effectively financing the U.S.'s current account deficits. This creates a global financial structure that is inherently biased and prone to transmitting U.S.-centric shocks to the rest of the world.

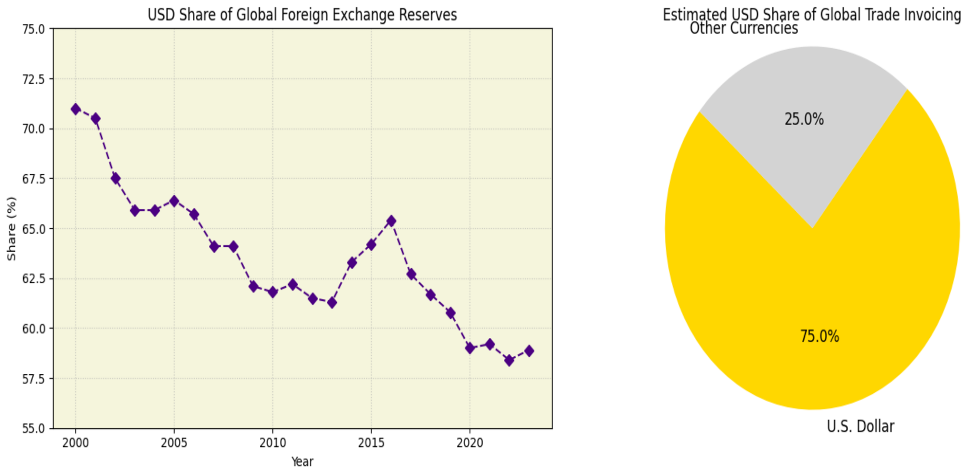


Figure 1: USD Dominance in Reserves vs Trade Invoicing

- **The Consequences: Exchange Rate Risk and Crisis Transmission**

The practical consequences of "original sin" have been extensively documented in the literature on financial crises. Mishkin (1996) provided a seminal analysis of how currency devaluations can trigger financial crises in developing countries through balance sheet effects. A sharp depreciation of the local currency inflates the domestic value of foreign currency-denominated debt, eviscerating the net worth of corporations and financial institutions. This was a central mechanism in the 1997 Asian Financial Crisis. Krugman (1999) formalised this in his "third-generation" crisis models, showing how currency and balance sheet crises are intertwined, leading to a "doom loop" of capital flight, depreciation, and economic collapse.

For India, this literature is particularly salient. Kletzer and Mody (2000) studied India's cautious approach to capital account liberalisation in the aftermath of the Asian crisis, noting that the country's existing external debt vulnerabilities necessitated a gradualist approach. While India has avoided a full-blown balance sheet crisis of the kind seen in East Asia or Latin America, the underlying vulnerability remains a constant concern for its policymakers, as highlighted in numerous reports by the Reserve Bank of India (RBI, various years).

- **The Rise of BRICS as an Institutional Alternative**

The literature on BRICS has evolved from viewing it as a mere acronym for investors to analyzing it as a potential counterweight to Western-dominated global governance. Stuenkel (2015) argues that the primary motivation behind BRICS cooperation is the shared desire of its members for "greater autonomy and the ability to contest the existing global order." This contestation is most visible in the financial sphere.

The creation of the New Development Bank (NDB) and the Contingent Reserve Arrangement (CRA) is a direct institutional response to the perceived inadequacies and biases of the Bretton Woods institutions. As noted by Cooper and Farooq (2016), the NDB's mandate to prioritize lending in the local currencies of its members is a revolutionary feature. It is a direct attempt to create a new source of development finance that does not carry the inherent currency risk of traditional lending from the World Bank or IMF. The CRA, a $100 billion pool of foreign exchange reserves, is designed to provide members with a firewall against the liquidity pressures and capital flight that often precede a full-blown financial crisis, offering an alternative to the often-stigmatised and conditional lending of the IMF. These institutions, therefore, represent the first concrete steps in building a parallel financial safety net.

The Problem Magnified: India's Specific Vulnerabilities to the Dollar Standard

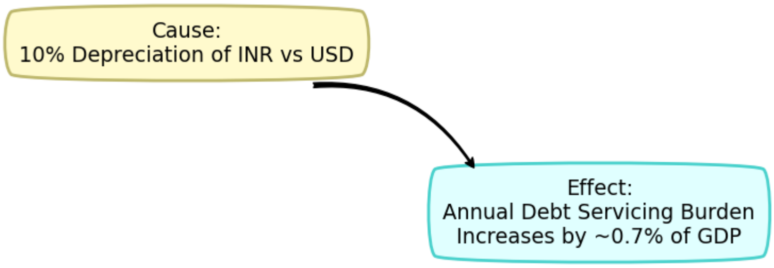
While the "original sin" is a common affliction for emerging markets, its specific manifestations in India are shaped by the country's unique economic structure. India's large and persistent trade deficit, its reliance on commodity imports, and the managed-float exchange rate regime of the Rupee create a distinct set of vulnerabilities that underscore the urgency of de-dollarisation.

- **India's External Debt and Currency Mismatches**

India's external debt, while considered moderate by EME standards, carries significant currency risk. According to the Reserve Bank of India's status reports, the U.S. dollar remains the dominant currency of denomination for India's external debt, accounting for over half of the total stock.

This composition means that India's sovereign and corporate balance sheets are highly sensitive to the fluctuations of the INR/USD exchange rate. A 10% depreciation in the Rupee against the dollar translates into a direct 10% increase in the Rupee-value of this portion of the external debt. This is not a hypothetical risk. During periods of global risk aversion, such as the "taper tantrum" of 2013, the Rupee depreciated sharply, putting immense pressure on Indian corporations with large foreign currency borrowings and forcing the RBI to intervene heavily to stabilize the currency. This intervention comes at the cost of depleting precious foreign exchange reserves.

Figure 4: Impact of INR Depreciation on External Debt Burden



- **The Oil Import Bill and Imported Inflation**

A critical channel through which dollar dominance affects the Indian economy is the invoicing of key imports. India is one of the world's largest importers of crude oil, a commodity that is almost exclusively priced and traded in U.S. dollars. This creates an enormous, and largely inelastic, demand for dollars.

When the Rupee depreciates, the cost of India's oil import bill rises in Rupee terms, even if the global price of oil remains unchanged. This phenomenon is known as **imported inflation**. This price increase feeds directly into domestic transportation and energy costs, creating economy-wide inflationary pressures. This forces the RBI into a difficult position: it may need to raise interest rates to combat this imported inflation, even if the domestic economy is sluggish and requires monetary stimulus. This directly illustrates how dollar invoicing can constrain India's ability to manage its own business cycle.

- **The Asymmetry of Trade Invoicing**

The problem is compounded by the fact that a significant portion of India's exports are also invoiced in U.S. dollars. According to research by Gopinath (2015), this **dominant currency pricing** mutes the traditional benefits of a currency depreciation. A weaker Rupee does not automatically make Indian goods cheaper for American or European consumers if the price is fixed in dollars. While Indian exporters receive more Rupees for their dollar earnings, the price signal that would typically spur greater export volumes is blunted.

This creates a painful asymmetry: a weaker Rupee immediately increases the cost of imports but has a delayed and often muted positive effect on exports. This can lead to a worsening of the trade deficit in the short to medium term, a phenomenon known as the J-curve effect, which is particularly pronounced for a dollar-dependent economy like India.

The BRICS Architecture as a Solution

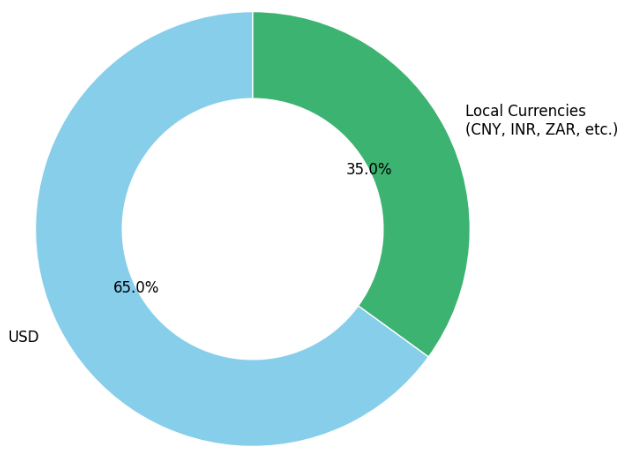
Faced with these deep-seated vulnerabilities, India and its BRICS partners have moved beyond rhetoric to construct a tangible institutional framework aimed at fostering a multipolar currency system. This architecture is designed to create alternatives to the dollar-dominated channels of development finance, crisis support, and trade settlement.

- **The New Development Bank (NDB): De-Risking Development Finance**

The NDB, headquartered in Shanghai, represents the most concrete achievement of the BRICS bloc. Its founding principle is to mobilize resources for infrastructure and sustainable development projects in BRICS and other emerging economies. Its revolutionary feature, however, is its explicit commitment to **lending in local currencies**.

By 2024, the NDB had approved a substantial portfolio of projects in India, many of which were financed in Indian Rupees. For an Indian state government seeking to fund a new metro rail system, for example, borrowing in Rupees from the NDB eliminates the exchange rate risk that would come with a traditional loan from the World Bank. This allows for more predictable long-term financial planning and insulates critical infrastructure projects from global currency volatility. The NDB's "AAA" international credit rating allows it to raise funds in international markets and then on-lend them in the currencies of its members, effectively acting as a financial intermediary that absorbs and manages the currency risk. In doing so, it is making a direct attempt to cure the "original sin" for its member countries.

Figure 5: NDB Approved Financing by Currency Type



- **The Contingent Reserve Arrangement (CRA): A Financial Safety Net**

The CRA is a $100 billion framework designed to provide a financial safety net for BRICS members facing balance of payments pressures. It allows members to access U.S. dollar liquidity during a crisis, thereby helping them to fend off speculative attacks on their currencies and prevent a rapid depletion of their own reserves. While it uses the dollar as its unit of account, its political significance is profound. It provides an alternative to the International Monetary Fund (IMF), where borrowing often comes with stringent policy conditionalities (austerity) and the stigma of economic mismanagement.

The CRA is structured as a system of swap lines, with China contributing the largest share ($41 billion) and India, Brazil, and Russia contributing $18 billion each. While it has not yet been activated, its mere existence provides a crucial buffer, increasing the collective bargaining power of the BRICS nations and reducing their immediate reliance on the IMF in times of crisis.

- **The Push for a Local Currency Settlement (LCS) System**

Beyond these formal institutions, the most dynamic area of cooperation is the push for bilateral and multilateral frameworks to settle trade in local currencies. In 2023, India and the UAE operationalised a landmark agreement to settle bilateral trade in Rupees and Dirhams. Under this mechanism, Indian exporters to the UAE can be paid in Rupees, and vice versa, through a system of "Vostro" accounts. This eliminates the need to buy and sell U.S. dollars for every transaction, reducing costs and risks for businesses on both sides.

India has pursued a similar Rupee-Ruble mechanism with Russia, which gained urgency following Western sanctions on Moscow. Within BRICS, leaders have officially called for the development of a shared payment system, often dubbed "BRICS PAY," as an alternative to the Western-controlled SWIFT network. Furthermore, discussions about a potential **"BRICS currency"**—likely a new digital currency for cross-border trade rather than a replacement for national currencies—have gained traction. While a common currency remains a distant and complex prospect, these initiatives collectively signal a clear and deliberate intent to build a parallel financial messaging and settlement system that operates outside the direct control of the U.S.

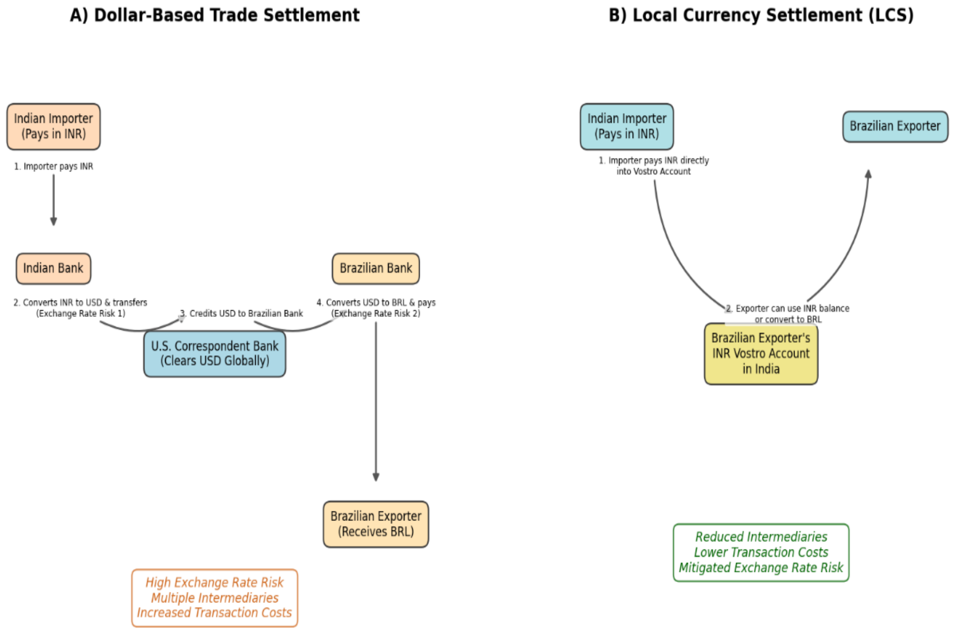


Figure 2: Comparative Trade Settlement Models

India's Strategic Imperative and Role

For India, participating in and leading the BRICS de-dollarisation strategy is not just about financial prudence; it is a core component of its broader ambition to be a "leading power" in the 21st century. The strategic imperatives are threefold: mitigating economic risk, enhancing geopolitical autonomy, and fostering the internationalisation of the Indian Rupee.

- **Mitigating Risk and Ensuring Financial Stability**

The primary driver for India's de-dollarisation efforts is defensive. As outlined in Section 3, the Indian economy's exposure to dollar-denominated liabilities and trade creates a constant source of volatility. By shifting a greater portion of its trade and borrowing into local currencies, India can build a more resilient economy. A system where oil from Russia or the UAE can be purchased in Rupees would significantly insulate the Indian economy from the "imported inflation" that has historically plagued it. Similarly, financing infrastructure through the NDB in Rupees removes a major source of financial risk from public sector balance sheets. This quest for stability is the foundational economic argument for the pivot away from the dollar.

- **Enhancing Geopolitical and Foreign Policy Autonomy**

The dominance of the U.S. dollar is not just an economic phenomenon; it is a powerful tool of American foreign policy. The U.S. Treasury's ability to impose sanctions and cut off access to the dollar-based financial system gives it immense leverage over other countries. For India, which prides itself on a foreign policy of "strategic autonomy," this dependency is a significant constraint.

The development of alternative payment systems and the ability to trade in local currencies provide India with a crucial "financial escape hatch." It allows India to maintain economic relationships with countries that may be under U.S. sanctions, such as Russia or Iran, without being subject to secondary sanctions. The Rupee-Ruble trade mechanism, for example, is a direct manifestation of this strategy, allowing India to continue purchasing Russian oil and defense equipment despite Western pressure. This ability to conduct commerce outside the purview of the U.S. financial system is a core element of strategic autonomy.

- **The Long-Term Goal: Internationalisation of the Indian Rupee**

Beyond the defensive benefits, de-dollarisation offers a historic opportunity for India to promote the international role of its own currency. A world less dominated by a single currency is one where other major currencies, like the Rupee, can play a larger regional and global role.

The benefits of having an international currency are substantial. It would reduce transaction costs for Indian businesses, allow the country to earn "seigniorage" (the profit made from issuing currency), and give Indian financial markets greater depth and influence. The Indian government and the RBI have already taken several steps in this direction, including allowing foreign investors greater access to Indian government bonds and establishing the aforementioned bilateral LCS agreements.

Participating in the BRICS de-dollarisation project serves as a catalyst for this ambition. It creates a coalition of powerful countries that have a shared interest in using each other's currencies. While the Chinese Renminbi is currently the most prominent non-dollar currency within the bloc, a collaborative BRICS framework provides a platform for the Rupee to gain acceptance and liquidity in a controlled, multilateral environment, which is far less risky than a unilateral push for internationalisation.

Challenges and the Road Ahead

Despite the compelling strategic rationale, the path toward a significantly de-dollarised global economy, and a more prominent role for the Rupee, is fraught with formidable challenges. These hurdles are structural, internal to the BRICS, and specific to India's own domestic economy.

- **The Inertia of the Dollar System**

The single greatest challenge is the immense inertia of the dollar-based system. As described by Prasad (2014), the U.S. dollar benefits from unparalleled network effects. Its dominance is sustained by the size, depth, and liquidity of U.S. financial markets, the credibility of the U.S. Federal Reserve, and the general acceptance of U.S. legal frameworks for international contracts. No other currency, including the Chinese Renminbi or the Indian Rupee, currently offers a comparable ecosystem. This means that even if traders and investors wish to move away from the dollar, the lack of a credible, large-scale alternative makes doing so costly and risky.

- **Disparities and Divergences within BRICS**

The BRICS bloc is not a monolithic entity. It comprises countries with vastly different economic structures, political systems, and strategic interests. The most significant disparity is the economic dominance of China, whose economy is larger than that of the other four members combined. This has led to concerns that the push for de-dollarisation may simply result in **"re-yuan-isation"**—a shift from dependence on the U.S. dollar to dependence on the Chinese Renminbi.

For India, this is a major strategic consideration. While it shares a common interest with China in reducing dollar dominance, it is wary of a new system dominated by its regional rival. This tension means that progress on deeper financial integration, such as a common BRICS currency, will be slow and contentious. The future of BRICS financial architecture will depend on its ability to create a truly multipolar system that respects the interests of all its members, not just its largest one.

- **India's Domestic Hurdles**

For the Indian Rupee to play a larger international role, India must address several domestic challenges. The international appeal of a currency is directly linked to the strength and openness of its domestic economy and financial markets.

  - **Capital Account Convertibility:** India currently maintains partial capital account convertibility, meaning there are restrictions on the free movement of capital in and out of the country. While this has insulated India from the worst effects of global financial volatility, a fully internationalised currency would require a more open capital account, which brings its own risks.
  - **Financial Market Depth:** While improving, India's corporate bond and derivatives markets are still not as deep or liquid as those in more advanced economies. Foreign entities holding Rupees need a wide array of safe and liquid assets to invest in.
  - **Macroeconomic Stability:** A continued commitment to controlling inflation and maintaining fiscal discipline is paramount. No country will willingly hold reserves in a currency that is perceived to be at risk of losing its value due to domestic mismanagement.

Conclusion

The global financial order is at an inflection point. The long-standing dominance of the U.S. dollar, while providing a stable anchor for decades, has created systemic vulnerabilities that disproportionately harm emerging economies like India. The "original sin" of dollar-denominated borrowing and trade has left India exposed to exchange rate shocks, imported inflation, and constrained monetary sovereignty. This structural dependency represents one of the most significant impediments to India's stable and autonomous economic development.

In this context, the BRICS bloc's concerted push for a de-dollarised financial architecture is not merely a geopolitical statement; it is a pragmatic and necessary response to the inherent imbalances of the current system. The creation of the New Development Bank and the Contingent Reserve Arrangement, alongside the promotion of a Local Currency Settlement system, represents the most credible effort to date to build a more multipolar and resilient global financial order.

For India, active engagement in this project is a strategic imperative. It is a defensive necessity to mitigate the financial risks that have plagued its economy for decades. It is a crucial step towards achieving genuine foreign policy autonomy in an increasingly complex world. And it is a proactive opportunity to foster the internationalisation of the Indian Rupee, cementing the country's status as a leading economic power.

The road ahead is long and complex. The inertia of the dollar system, internal rivalries within BRICS, and India's own domestic reform agenda are all significant hurdles. However, the trajectory is clear. The pivot away from the dollar, led by nations like India within the BRICS framework, is an essential evolution towards a more balanced, stable, and equitable global economy. The success of this endeavor will be a defining feature of the international economic landscape in the 21st century.

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