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Dollar Signs

By Stuart Thornton

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According to Doug Mudd, the health of the United States dollar has an oversized impact on the rest of the world's economies.

"If the U.S. dollar was to tank, basically the rest of the world would tank," says Mudd, the curator of the Colorado Springs, Colorado-based Edward C. Rochette Money Museum. "It's just like if the U.S. economy catches a cold, a lot of the rest of the world catches the flu. It's because our economy is so large and so concentrated that we automatically have an effect on the rest of the world when things go wrong. When they go well, it helps the rest of the world as well."

The dollar is an integral part of the world market for several reasons. First, it is the official currency of the United States, which has the largest economy in the world. The power of the U.S. economy means the dollar is used to give a relative price for currencies around the world. Also, the costs of some of the global market's most important goods are priced only in dollars.

"The dollar is still the preferred international currency, and so you need to be able to express the price of gold or oil in some form that everyone can accept and use easily," Mudd says. "By having a single currency that is accepted by everyone as the way to express the current value of gold or oil, it makes international trade much easier."

Besides being used by the United States, the U.S. dollar has been adopted as the official currency of ten countries around the world: British Virgin Islands, East Timor, Ecuador, El Salvador, Federated States of Micronesia, Marshall Islands, Palau, Panama, Turks and Caicos, and Zimbabwe.

"In those countries that are using the dollar as the official money, it means they have given up trying to produce their own money and realize the dollar is much more stable," Mudd says.

Dollar Ripples

When the U.S. dollar rises and falls, it causes ripples throughout the world's economies. A rise in the dollar's worth causes U.S.-made goods to be more expensive, compared to products made in other countries. That means other countries can benefit by selling more of their goods in the world market.

Since the United States is one of the major lending countries in the world, the climbing worth of the dollar affects the developing world. Developing countries have frequently borrowed money from the United States, and the rising dollar means that the value of those loans goes up. The loans become more difficult to pay back.

If the price of the dollar falls, it also has impacts on the U.S. economy and the world. As the dollar falls, prices on U.S. goods go down.

“Our own consumers will buy our goods more often, and foreign countries will buy U.S. goods because they are cheaper,” Mudd says.

A falling dollar is a boon to the developing countries of the world because the loans they have taken in from the United States decrease in value and become easier to pay back.

The World’s Bankers

Though the dollar became the unit of money for the United States in 1785, it didn’t become prominent within the world’s economy until the late 1800s. The influence of the dollar in global economic markets was a direct result of the expanding U.S. economy.

“As we developed our international trade, as we started manufacturing more goods, naturally we would be paying for things in dollars, and in preference, purchasing with dollars,” Mudd says.

The curator says that the worldwide importance of the U.S. dollar grew after the end of World War I.

“Almost anywhere in the world, [Great Britain’s] gold sovereign was the standard everyone looked to before World War I,” Mudd says. “World War I was an economic catastrophe for Europe.”

The United States “had gone from being a major debtor to Europe to becoming the major debt holder for Europe by the end of the war. In the 1920s, the U.S. was the major financier throughout the world. Our economy was very, very strong.”

With much of Europe owing the United States money after the war, the standing of the U.S. economy within the world changed.

“We had become the world’s bankers, essentially,” Mudd says.

But it was the next great conflict in Europe that secured the dollar and the U.S. economy’s top-tier position around the world.

“When World War II came around, that really sealed the deal,” Mudd says. “Europe was again in ashes, just a mess. Even the winners were a mess, but we came out of it with a completely undamaged industrial base. Because of the Marshall Plan [the United States’ efforts to restore Europe after World War II] and other things, we rebuilt Europe, and we created markets all over the world that hadn’t existed for us. All of that was based on the dollar, so the dollar became the absolute king of all monetary transactions.”