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CURRENCIES

The Dominant Dollar Faces a Backlash in the Oil Market

An estimated 20% of global oil this year was bought and sold in other currencies as Russia and Iran sold cargoes to China and other buyers

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The proportion of the world's oil that is bought and sold in currencies other than the dollar has risen. PHOTO: AL DRAGO/BLOOMBERG NEWS

Some major emerging economies are dabbling in trading commodities without using the dollar, as they seek to reduce their reliance on the U.S. currency.

Faced with U.S. sanctions and other restrictions, Russia and Iran in particular have stepped up oil sales in alternative currencies, and have found buyers in China, India and elsewhere that are happy to buy these exports, often at lower prices.

The need is less pressing for other commodity heavyweights. But some of these countries, including Brazil, the United Arab Emirates and even Saudi Arabia, have recently taken steps laying the groundwork for trade that sidesteps the dollar.

"The U.S. dollar is getting some competition in commodities markets," said Natasha Kaneva, head of global commodities strategy at JPMorgan Chase. She estimated that the proportion of the world's oil that is bought and sold in other currencies has risen to about 20%.

Twelve major commodities contracts settled in nondollar currencies were announced in 2023, compared with seven in 2022 and just two in 2015 through 2021, the bank's data shows. This year's contracts were struck by sellers in Russia and, in one case, the U.A.E. The data relates to physical commodity deals, rather than the trading of futures in financial markets.

This summer, the U.A.E. and India signed a deal to trade in their own currencies, starting with a shipment of Emirati oil bought by an Indian refiner, and paid for in Indian rupees. In the fall, Brazil and China completed their first local-currency commodity transaction, involving a shipment of Brazilian pulp, according to China's state news agency, Xinhua.

And in November, Saudi Arabia and China set up a roughly $7 billion currency-swap line, which the Chinese central bank said would strengthen financial ties and expand the use of local currencies.

The dollar's central role in commodities is one aspect of its broader dominance of global trade and finance. The dollar appears on one side of 88% of all trades in foreign-exchange markets.

Controlling the most important currency has helped the U.S. act as the world's watchdog because threats of exclusion from the dollar-based financial system have had significant weight. If the dollar's dominance were to erode, that could eventually diminish this authority.

The tight links between the dollar and global oil markets date back decades, to a 1945 deal between President Franklin D. Roosevelt and King Abdulaziz Ibn Saud that exchanged Saudi energy supplies for U.S. security guarantees. Over time, many billions of so-called petrodollars earned by oil producers were recycled back into investments such as Treasury bonds, helping boost demand for U.S. assets.

After Russia invaded Ukraine in February 2022, the West slapped Moscow with sanctions that froze its central-bank assets, tried to cap its oil prices and blocked Russian banks from the Swift international payments system. That pushed the Kremlin to develop alternative financial channels.

Seeing a risk that Washington could act similarly in the future, other governments such as China also moved to reduce their dependence on dollar payments.

"This is something other countries are increasingly concerned about," said William Jackson, chief emerging-markets economist at Capital Economics. "Some are seeking to reduce their risk of possible sanctions on the use of dollars in trade. China is trying to act as a geopolitical counterweight."

Oil is at the center of that shift. A so-called shadow fleet has helped redirect Russian oil to buyers in Asia, and Russia's export revenues from the lifeblood industry topped $18 billion in November. Russian oil has been sold in Chinese yuan, Russian rubles, Emirati dirhams and Indian rupees, according to the Institute of International Finance.

Russia became China's top crude supplier in 2023, selling over 2 million barrels a day through July, according to S&P Global. Shipments were largely paid for in yuan. Moscow has also shifted major gas contracts to China, according to JPMorgan.

Iran, which mostly sells oil to China in yuan, also has stepped up exports.

For energy importers, price is a key incentive. Paying in a domestic currency rather than dollars lowers transaction costs, and Russian oil is cheaper than global alternatives. India has emerged as Russia's biggest new energy customer, Kpler data shows, after New Delhi told its largest oil companies to snap up discounted Russian crude.

They have paid in dirhams, yuan and rupees, according to Indian oil executives. Pakistan began paying for Russian oil shipments in the Chinese currency this year, according to JPMorgan. This move coincided with a dollar shortage in the South Asian country.

A far bigger shift would occur if Saudi Arabia, the world's top crude exporter, was to start selling significant quantities of oil in other currencies.

Last year, The Wall Street Journal reported that the kingdom was considering selling some oil in yuan. At this year's World Economic Forum, the Saudi finance minister said his country was open to talking about settling trades using other currencies.

China eclipsed the U.S. as Saudi Arabia's biggest trading partner when the U.S. became more energy independent, and it has deepened political ties with Saudi Arabia.