



## **The Dollar Trap: How the U.S. Dollar Tightened Its Grip on Global Finance**

*Eswar Prasad*

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The U.S. dollar's dominance seems under threat. The near collapse of the U.S. financial system in 2008–2009, political paralysis that has blocked effective policymaking, and emerging competitors such as the Chinese renminbi have heightened speculation about the dollar's looming displacement as the main reserve currency. Yet, as *The Dollar Trap* powerfully argues, the financial crisis, a dysfunctional international monetary system, and U.S. policies have paradoxically strengthened the dollar's importance.

Eswar Prasad examines how the dollar came to have a central role in the world economy and demonstrates that it will remain the cornerstone of global finance for the foreseeable future. Marshaling a range of arguments and data, and drawing on the latest research, Prasad shows why it will be difficult to dislodge the dollar-centric system. With vast amounts of foreign financial capital locked up in dollar assets, including U.S. government securities, other countries now have a strong incentive to prevent a dollar crash.

Prasad takes the reader through key contemporary issues in international finance—including the growing economic influence of emerging markets, the currency wars, the complexities of the China-U.S. relationship, and the role of institutions like the International Monetary Fund—and offers new ideas for fixing the flawed monetary system. Readers are also given a rare look into some of the intrigue and backdoor scheming in the corridors of international finance.

*The Dollar Trap* offers a panoramic analysis of the fragile state of global finance and makes a compelling case that, despite all its flaws, the dollar will remain the ultimate safe-haven currency.

## **The Dollar Trap: How the U.S. Dollar Tightened Its Grip on Global Finance Details**

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## **From Reader Review The Dollar Trap: How the U.S. Dollar Tightened Its Grip on Global Finance for online ebook**

### **Amrendra Pandey says**

The book is well researched and simple written. Even a non economics people can understand it. The problem lies in the details that this book has gone into. I believe the book could have been edited in better way as there was no need of so many who said what in exact terms. But at the end it is a good book for anyone interested in international monetary economics.

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### **Jason Furman says**

The Dollar Trap is a well written, well argued, clear-eyed presentation of global finance--arguing the thesis that the dollar is locked in as a global reserve currency (if not a unit of account or medium for transactions) because even when the United States economy falters that just increases global uncertainty and sends investors and global central banks into a flight to safety (or, as Prasad argues, a flight to liquidity). In addition to recounting developments, mostly post-2007 and focused on central bank reserves, swaps, and somewhat more broadly on the current/capital account, Prasad also advances some policy suggestions on, for example, a new global insurance system for liquidity that, he argues, would be more effective than the IMF and cheaper than stockpiling ever larger amounts of reserves. Overall less wildly creative than it is clear, would recommend this book as a good primer on the topic.

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### **Parth says**

A very intellectual but still easy to read book.. Enjoyed almost every part of it. Must read if you work in or love the field of macro economics, forex management and global politics.

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### **University of Chicago Magazine says**

Eswar S. Prasad, PhD'92  
Author

From our pages (May–June/14): "The global financial crisis, growing overseas competition, and political gridlock around US economic policy may appear to be taking a toll on the dollar's dominance in the international marketplace. But according to economist Eswar Prasad, these pressures have actually bolstered the hegemony of the iconic greenback. In *The Dollar Trap*, Prasad examines why, despite the emergence of newfangled alternatives like Bitcoin, the dollar-centric system remains too big to fail."

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### **Void lon iXaarii says**

I found this book to be academic from an American government perspective. Though it seemed to me often dry/boring and with an unilateral perspective, that was compensated by the interesting subject matter and the often interesting data it brings. However in my humble opinion the biggest problem I see with it is that it's an academic elegant version of the good old feel good "this time is different" stating that our times/America today is like no other country in history and unique in time and space. While that is obviously true in some technical sense, this brings to mind the old joke: "you're unique and special... just like everybody else".

In terms of the foundation of his reasoning it seems to me like the author only points to the past as far as it agrees with his point, only going back as far as a few decades at the most, and then concluding that therefore all shall continue to remain the same and not change pretty much forever. This is particularly ironic since he himself often points a lot of flaws in the system and how a lot of participants hate it, yet he seems to believe that despite hating it and being disadvantaged by it nobody can break out of this perfect trap, neither individually nor through surprising collective solutions, and thus expects everything to continue as it is in the future. He keeps his prediction safe by never (as far as I found) mentioning whether he has this expectation for years, decades, centuries, or just months. Again ironically he occasionally hedges his words by saying things like of course the \$ will lose its value gradually, but he expects it to fall from trade use but keep its store of value use, which pretty much voids the attacks because it seems to me if it keeps the store of value function... well, pretty much nothing else matters. He also bases a lot of his conclusions on the great international credibility in American institutions, although credibility can evaporate much faster than what it takes to regain it.

Although I tend to have a differing view on the subject I still learned a lot from the book and it probably did me good to be faced with a contrary position to other books I've been reading in recent years on the topic. It shall be interesting to see what happens in the next 10 years. We are living in interesting times... Discworld style :D

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### **Adrian says**

Eswar Prasad of Cornell University makes the case that the crash of 2008 and the ongoing debt crisis, rather than weakening the dominance of the dollar, has in fact strengthened it. As illogical as this would appear on first observation, it really boils down to the lack of clear alternatives to the dollar as a reserve currency. The main competitor, the Renminbi, or Yuan, is hampered by the fact that China has not yet an open capital account, and its rather undeveloped financial system prevent the Renminbi from being ready for primetime. Additionally, the institutional structure of China, with its lack of rule of law, and enforced property rights, have made it not quite as attractive to the US, despite the instability that initially stemmed from the US. The idea of a monetary atom bomb being dropped by China, in the form of offloading of treasuries, is unlikely as the author agrees with others that this could harm China more than the US.

Other alternative currencies, such as IMF Special Drawing Rights, are examined, but IMF SDRs remain undeveloped, and not really a tangible alternative. Gold, on the other hand, is mainly hindered by the fact that it remains so illiquid it could not feasibly replace the dollar.

Prasad's main conclusion is that the Dollar remains attractive to investors for many reasons, not least of which is the institutional structure of the US, and its solid enforcement of property rights.

Prasad's conclusion is not overly positive. The world monetary system is effectively a sandpile, and it could reach tipping point at some unknowable date. However, Prasad cautions against a rush to an alternative to the dollar at this point.

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## **Mayank says**

A fascinating tale of a country's legal tender which helped her in becoming a global power. Its a very good read to understand how america became an exception to logics of economics.

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## **Brad Boyson says**

Wishful thinking

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## **Drew says**

Important for understanding the role of the Dollar in global finance. It is essential to note his data supporting the narrative that the Dollar strengthened in the post GFC world despite what the conservative press / Austrian Economists have purported.

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## **Byunghwan Son says**

It took a while--2.5 years--to finish this book. No, it's a well-written, easy-read book that delivers clear messages with down-to-earth languages. It was precisely because of this high readability of the book that took me so long to finish it--`I can read it up whenever I want.'

The title can be easily misread. The `trap' does not signify the cataclysmic near future that the dollar will throw the current global financial system or the American economy into. Unlike many ominous verdicts on the current monetary system put forth by non-economist pundits, Prasad, an economist, convincingly demonstrates that how the fragility of the system paradoxically drives everybody towards the very centerpiece of the system, the dollar.

The Global Financial Crisis (or perhaps 1997-8 Asian Financial Crisis), for example, undoubtedly exposed how much of a sandpile the US-led global financial system was. The insecurity set off investors scrambling for safe assets. It turned out that the safest assets, however, are dollar-denominated ones. So the more fragile the system is found to be, the more thirsty the market would be for the dollar. Dollar reserves around the world are only to expand in the near future. So it's a trap in a sense that everybody goes back to it as they all want to escape it.

'The end of the dollar' (and the tanking of the US economy along with it) that the dooms-sayers have been spreading since the crisis is an ungrounded fiction in this sense.

After making this extremely simple, but surprisingly convincing, point, Prasad walks the readers through the alleged `alternatives' of dollars. Be it the yuan or a new international coordination mechanism, he argues, all these alternatives fail just one test to replace the current--and increasing--global dominance of the dollar: the sense of safety (or sometimes, liquidity and safety). Yes, it is about the safety all along.

And, in so doing, he elegantly busts the myths non-economist pundits spread: the currency war is, in essence, a result of misperception; gold cannot replace the dollar given its limited liquidity and volatile price levels; China cannot just claim all its dollar denominated assets as doing so would directly undercut its own assets while the Fed can swiftly neutralize its effect.

Towards the end of the book, though, it feels like the story is overstretched a little bit. The idea of global insurance, which Prasad proposes, is supposed to substitute the current individual reserve systems seems to overlook international coordination problem, for example; The Senkaku/Diaiyo issue isn't that serious an issue to set off a regional financial turmoil. But these are rather minor shortcomings that doesn't taint the service the book does to the readership.

Overall, it is a good book. You know, you can read it up whenever you want.

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### **Maytham Abdulraheem says**

The topic is very interesting and the author demonstrated his knowledge , but he goes out of the road very often to discuss some topics that are not clearly linked to his main points . Fortunately I find those side topics in international finance interesting also and learned a lot from it.

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### **Daniel says**

The best book about international economics, currencies, and the reason of the dollar supremacy. All my questions about the anomaly of the dollar being the anchor currency are answered. A must read book for anyone who believe in the impending upending of the dollar-denominated/-dominated world!

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### **Oli Ogbonna says**

Quite illuminating piece from someone who is part of the global financial system. He sounds quite optimistic that the system will not collapse, though he makes it quite clear that the dollar may not rule for ever as the world's reserve currency.

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### **Mehrsa says**

The dollar is the world's currency and the world doubled down on the dollar (counter-intuitively) after the financial crisis that started in the US. The reason is that the fed became the lender of last resort and increased the supply of the dollar to meet demand. And Prasad makes an excellent case that this is the way it will likely remain (absent something catastrophic).

I wish he talked more about how violence plays into the dollar's supremacy. That's something I've been thinking a lot about recently. Maybe I will write something up

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## Brick&rope says

With the recent financial crisis, there is a lot of conversation about the future of the US economy in general, and that of the US Dollar in particular. Either with barely contained glee, or with frustrated hand-wringing, people are on about whether the days of the almighty dollar are up. Eswar Prasad's book takes that question up.

Other books have taken on the subject of the dollar's power in international trade. The most notable one of course has been Barry Eichengreen's *Exorbitant Privilege*. *The Dollar Trap*, in my opinion, stands up to the best.

Prasad lays out the book in four parts - Part One sets the stage for the tale that is about to come. The case is made, from first principles, that the dollar does indeed have a special status in global economics, and that this special status benefits the US economy immensely. Part Two takes on various building blocks of the dollar story, and lays out in some detail how the strengthening of the dollar has gone on over time. Part Three speaks of various global institutions, and how they have participated in either strengthening, or challenging the Dollar's hegemony, and lays out how most efforts of reining in the dollar's power have ended in failure. Finally, in Part Four, Prasad looks at the case for possible contenders for the dollar as primary reserve currency of the world. He looks at the more obvious ones (like the Renminbi), as well as the more exotic ones (world currency, bitcoins etc).

By the end, the case is made convincingly that (a) the dollar is special; (b) there are no real challengers to this status, and (c) times of trouble for the US economy, instead of making the dollar less powerful, have actually strengthened it in a perverse way.

*The Dollar Trap* is clearly written by an erudite academic. The language and narrative style is smooth, while being slightly pedantic in parts. But to be honest, that is what made me love the book. Part Two of the book in particular, where the hood is taken off the currency story, and made accessible to more lay readers, is extremely well written.

Whether you are interested in understanding global currency wars, and want to know what all the fuss about reserve currencies is about, or you just want to be a bit more well informed when you are talking about 'current account deficit', you cannot do a whole lot better than spending a few days with *The Dollar Trap*.

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