US History

Rise of the US Dollar: Where the Greenback Meets the Black Gold

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Abstract

This essay examines the rise of the US dollar as the world's primary reserve currency, from its origins in the Bretton Woods gold standard to the establishment of the petrodollar system. It challenges the neoliberal narrative of market-driven dominance by highlighting the US government's strategic maneuvers. Key to this shift were the Joint Mission, the Technical Cooperation Agreement, and a confidential add-on deal between 1974 and 1975, all crucial in steering Saudi Arabia toward exclusive dollar pricing for oil. The analysis supports that the Joint Commission's economic tactics effectively influenced OPEC's adoption of the dollar, reinforced by the US military's strategic support and pressure. Declassified documents uncover a recycling mechanism that allowed Saudi Arabia to reinvest oil revenues in US bonds, circumventing standard market practices and concealing its debt profile, a practice that persisted for decades. The financialization of oil yielded profound political and economic consequences, such as elevated Saudi geopolitical power, impacts on US manufacturing, and a rise in national debt. The US government's decision to maintain the petrodollar system in the late 1970s affirmed the dollar's critical status as the primary global reserve currency, solidifying American hegemonic power in subsequent years. Analyzing the historical context is essential for understanding the influence of the US dollar on the global economy and the ongoing efforts of the Federal Reserve to combat inflation.

Introduction

In response to the COVID-19 pandemic, the US Federal Reserve launched an unprecedented "open-ended" Quantitative Easing (QE) program in March 2020, which aimed to shore up the US economy amid widespread global economic turmoil.[1] This initiative doubled the Federal Reserve's balance sheet from March 2020 to December 2021, marking a historic monetary intervention.[2] Yet Jerome Powell, Chair of the Federal Reserve, asserted throughout 2020 and much of 2021 that inflation was under control.[3] Historically, this assertion held: for over 40 years, the Federal Reserve had been able to print money without incurring substantial inflation rates and employed financial means to uphold a strong dollar.[4] This is largely due to the privilege of the US dollar as the world's primary reserve currency for international transactions. Examining the history of how the US dollar attained this global role can enhance our understanding of the new international economic order and the battle against inflation.

The US dollar has held this privilege since the end of World War II. While neoliberal scholars attribute the establishment of "dollar hegemony" to the natural workings of free markets, this essay emphasizes the substantial roles played by the US government.[5] Through economic incentives, military engagements, and covert diplomatic maneuvers, the US significantly shaped the trajectory of the dollar's dominance in the global financial system. Numerous debates regarding dollar supremacy have occurred throughout history and continue to

[1] Alessandro Rebucci, Jonathan S. Hartley, and Daniel Jiménez, "An event study of COVID-19 central bank quantitative easing in advanced and emerging economies," In *Essays in honor of M. Hashem Pesaran: Prediction and Macro Modeling,* vol. 43 (2022): 291-292, https://doi.org/10.1108/S0731-90532021000043A014.
[2] Congressional Research Service, "Federal Reserve: Tapering of Asset Purchases," January 27, 2022, accessed December 20, 2023, https://crsreports.congress.gov/product/pdf/IN/IN11792. The Federal Reserve's balance sheet has expanded significantly since the introduction of QE measures, increasing from $4.31 trillion in March 2020 to $8.76 trillion by December 2021.
[3] Phillips Smialek J, "The Fed chair strikes a wary tone on inflation, but says this isn't the time to raise interest rates," *The New York Times*, Oct. 22, 2021, https://www.proquest.com/blogs-podcasts-websites/fed-chair-strikes-wary-tone-on-inflation-says/docview/2584324534/se-2.
[4] Daniel Sargent, *A Superpower Transformed: The Remaking of American Foreign Relations in the 1970s* (Oxford University Press, 2014), 299-300.
[5] For the theory of "free markets," see Robert Aliber, *The International Monetary Game* (New York: Basic Books, 1987). The neoliberal views are echoed in the works of various scholars, as demonstrated in Paul Volcker and Toyoo Gyohten, *Changing Fortunes: The World's Money and the Threat to American Leadership* (New York: Times Books, 1992).

inform the discourse and policies of the United States into the 21st century.

Background: Bretton Woods and the Early 1970s Challenges

The Bretton Woods Agreement, signed in July 1944 at Bretton Woods, New Hampshire, marked the inception of the US dollar's dominant role in the global financial system. Crafted during the United Nations Monetary and Financial Conference, the agreement was the result of intricate negotiations among representatives from 44 countries.[6]

Often understated is Harry Dexter White's instrumental role in the establishment of the Bretton Woods system.[7] As the American Chief International Economist and Director of Monetary Research, White masterminded the plan to position the US dollar as the *sole* reserve currency in the creation of the International Monetary Fund (IMF).[8] The "dollar for gold" standard marked a notable departure from John Maynard Keynes's concept of a new artificial international currency, the "bancor."[9] Keynes, acclaimed in the field of economics, also functioned as an unpaid adviser to the UK Treasury at the time.[10] During the multilateral negotiations at the conference, the United States' economic status as the primary creditor nation during World War II proved instrumental in propelling White's plan.[11] Ultimately, the Bretton Woods system culminated in a fixed exchange rate of $35 per ounce of gold, with other currencies pegged to the US dollar.[12] This arrangement heralded the inception of the "dollar-gold" system, officially establishing the US dollar's position in the international economy.

For over 15 years, the Bretton Woods system underpinned the US dollar's dominance in the global financial order.[13] In 1960, however, economist Robert Triffin illuminated its impending downfall by

[6] United Nations Monetary and Financial Conference, *Articles of Agreement: International Monetary Fund and International Bank for Reconstruction and Development* (Bretton Woods, NH, 1944), 96-97, accessed December 20, 2023, https://fraser.stlouisfed.org/files/docs/historical/martin/17_07_19440701.pdf.
[7] Benn Steil, *The Battle of Bretton Woods: John Maynard Keynes, Harry Dexter White, and the Making of a New World Order* (Princeton: Princeton University Press, 2013), 3-7.
[8] Ibid., 214-216.
[9] Richard Gardner, *Sterling-Dollar Diplomacy in Current Perspective: The Origins and the Prospects of Our International Economic Order* (New York Chichester, West Sussex: Columbia University Press, 1969), 71-100.
[10] Steil, *The Battle of Bretton Woods*, 142.
[11] Ibid., 151-154.
[12] United Nations Monetary and Financial Conference, *Articles of Agreement*, 4.
[13] Barry Eichengreen, *Exorbitant Privilege: The Rise and Fall of the Dollar and the Future of the International Monetary System* (Oxford: Oxford University Press, 2011), 57.

introducing the "Triffin Dilemma."[14] He posited that a surplus of US dollars was necessary to facilitate global trade and economic expansion; however, this would eventually diminish confidence in the dollar's value, thus threatening the system's sustainability. By the early 1970s, this predicament materialized, with the United States facing a depletion of gold reserves to support the dollar's global role.[15] Escalating costs of social programs and military engagements, particularly the Vietnam War, further exacerbated the issue.[16]

Amid these challenges, starting in 1965, key European nations such as France, Britain, and Germany began exchanging substantial amounts of dollars for gold, further straining the Bretton Woods system.[17] In response, the IMF introduced Special Drawing Rights (SDRs) in 1969, echoing Keynes' original proposal.[18] However, the reform was too late and fell short of expectations: over the next decade, SDRs accounted for less than 9 percent of global reserves, a marginal figure compared to the overwhelming 77 percent held in US dollar reserves.[19]

In 1971, President Richard Nixon unilaterally decided to "close the gold window," preventing foreign governments from exchanging their dollars for gold.[20] This action, aligned with Keynesian economic principles, signaled the end of the Bretton Woods system. The "Nixon shock" ushered in the era of the US dollar functioning as a "fiat currency," no longer tied to gold.[21]

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[14] Robert Triffin, *Gold and the Dollar Crisis* (New Haven: Yale University Press, 1960), 175-207.
[15] Beth Yarbrough and Robert Yarbrough. *The World Economy: Trade and Finance* (London: Dryden, 1994), 641. By the beginning of 1971, the United States had accumulated over $70 billion in dollar liabilities, far exceeding the gold reserves held at $12 billion.
[16] John Williamson, *The Failure of World Monetary Reform, 1971-74* (New York: New York University Press, 1977), 31-32.
[17] Michael Hudson, *Global Fracture: The New International Economic Order* (London: Pluto Press, 2005), 9-31.
[18] Williamson, *The Failure of World Monetary Reform*, 24-25.
[19] Akinari Horii, "The Evolution of Reserve Currency Diversification," *BIS Economics Paper* no. 18 (Basle: Bank for International Settlements, December 1986): 7, accessed December 20, 2023, https://www.bis.org/publ/econ18.pdf.
[20] Transcript of a video of the televised speech, "The Challenge of Peace: President Nixon's New Economic Policy," delivered August 15, 1971, available at *The American Presidency Project*, https://www.presidency.ucsb.edu/documents/address-the-nation-outlining-new-economic-policy-the-challenge-peace, accessed December 20, 2023.
[21] Thomas Costigan, Drew Cottle and Angela Keys, "The US Dollar as the Global Reserve Currency: Implications for US Hegemony," *World Review of Political Economy* 8, no. 1 (Spring 2017): 104-122.

Moreover, following US support for Israel in the 1973 Yom Kippur War, the Organization of Petroleum Exporting Countries (OPEC) enacted an oil embargo against the US, leading to a significant devaluation of the dollar.[22] The oil price surged fourfold between October 1973 and January 1974, triggering an economic crisis due to America's high dependency on oil imports, which averaged approximately 6.26 billion barrels daily.[23] This situation emphasized the crucial relationship between the United States and Saudi Arabia, as the desert kingdom provided the majority (52 percent) of oil imports from Middle Eastern suppliers.[24]

Birth of the Petrodollar System: Economic Incentives and Military Tactics

Neoliberal economists argue that the establishment of a new "oil-dollar" standard was driven by "free markets."[25] The argument proceeds as follows. First, despite the breakdown of the Bretton Woods system, the US dollar maintained its primacy in international transactions, commanding a significant share of global trade and finance.[26] Then, in January 1974, the Nixon administration took a significant step by abolishing all capital controls, to facilitate capital flows and promote financial globalization.[27] This deregulation, emblematic of the US government's neoliberal shift, was credited with significantly bolstering "the United States as an international financial center."[28] Consequently, the petrodollar arrangement emerged as a widely accepted norm internationally. It is essential, however, not to disregard the *proactive* role played by the US government in influencing the final decisions of OPEC countries, particularly Saudi Arabia.

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[22] Alan Blinder, *Economic Policy and the Great Stagflation* (New York: Academic Press, 1979), 103. The inflation rate exceeded 10 percent in the period from the 1973 oil embargo until the end of 1974.
[23] See data in Volcker and Gyohten, *Changing Fortunes*, chap. 7. The import average can be calculated by US Energy Information Administration, "Annual Energy Review 2011" (Sep. 2012): Table 1.1, accessed December 20, 2023, https://www.eia.gov/totalenergy/data/annual/pdf/aer.pdf.
[24] Ulrich R. Kohli and Edward R. Morey, "The US Demand for Foreign Crude Oil: A Translog Approach," *The Journal of Energy and Development* 12, no. 1 (1986): 116 (Table 1), https://www.jstor.org/stable/24807797.
[25] Volcker and Gyohten, *Changing Fortunes*, 136-162.
[26] Horii, "The Evolution of Reserve Currency Diversification," 42-43. The US dollar remained the dominant currency in international financial markets, comprising approximately 70 percent of total international banking liabilities.
[27] John M. Lee, "Impact of New Capital Outflow," *The New York Times*, Feb. 3, 1974, https://www.proquest.com/historical-newspapers/impact-new-capital-outflow/docview/119956957/se-2.
[28] Sargent, *A Superpower Transformed*, 130.

Beginning in 1974, President Nixon, along with Secretary of State Henry Kissinger and Secretary of the Treasury William Simon, initiated a series of diplomatic actions to mend relations with Saudi Arabia.[29] Numerous meetings took place in 1974, culminating in a significant turning point on June 8, when Kissinger and Crown Prince and Deputy Prime Minister Fahd signed a far-reaching *Joint Statement*. Before the cameras, both parties declared that the agreement "heralded an era of increasingly close cooperation," marking a pivotal moment in the two countries' relationship.[30] David Holden and Richard Johns, in their book *The House of Saud*, described it as "the most far-reaching agreement of its kind ever concluded by the US with a developing country. It had the potential to entrench the US deeply in the Kingdom, fortifying the concept of mutual interdependence."[31] Subsequently, the formal signing of the *Technical Cooperation Agreement* (TCA) by the US and Saudi governments on February 13, 1974, marked yet another crucial step in implementing the objectives outlined in the Joint Statement during the initial five-year period.[32]

What, then, was the primary aim of the US government in redefining its bilateral relations with Saudi Arabia? Simply put, it sought to mandate that all forthcoming oil sales by Saudi Arabia be valued exclusively in US dollars. This resulted in the establishment of the "Dollars for Oil" system, replacing the obsolete "Dollars for Gold" system.[33] Despite the US dollar no longer being backed by gold, the petrodollar system bolstered its global economic position. Consequently, the US dollar became the world's first fiat currency to assume the global reserve role.[34]

To elucidate the connection between the greenback and black gold, it is essential to recognize that oil, an indispensable commodity for

[29] David E. Spiro, *The Hidden Hand of American Hegemony: Petrodollar Recycling and International Markets* (Ithaca: Cornell, 1999), 107-110.
[30] Bernard Gwertzman, "'Milestone' Pact Is Signed by US And Saudi Arabia," *The New York Times*, June 9, 1974, https://www.proquest.com/historical-newspapers/milestone-pact-is-signed-us-saudi-arabia/docview/119904759/se-2.
[31] David Holden and Richard Johns, *The House of Saud: The Rise and Rule of the Most Powerful Dynasty in the Arab World* (New York: Holt, 1981), 357.
[32] Government Accountability Office, *The US-Saudi Arabian Joint Commission on Economic Cooperation* (Washington, DC: GPO, 1979), 11, accessed December 20, 2023, https://www.gao.gov/products/id-79-7.
[33] Duccio Basosi, "Oil, Dollars, and US Power in the 1970s: Re-viewing the Connections." *Journal of Energy History/ Revue d'Histoire de l'Énergie*, # 3 (June 2020): 2, https://energyhistory.eu/en/node/192.
[34] Costigan, Cottle, and Keys, "The US Dollar as the Global Reserve Currency," 104-122.

global economic growth, played a pivotal role in international trade.[35] With the inception of the petrodollar system, most nations found themselves in need of US dollars to secure their oil supply. However, exchanging their domestic currencies for US dollars came with substantial transaction costs. A more cost-effective and sustainable practice was for "[o]ther nations, which could not print dollars, … to sell their goods and services to the United States in exchange for dollars."[36] The US thus benefited from an advantageous *double-loan* scenario: it not only printed dollars to acquire oil from oil producers but also generated money to purchase European goods and services.[37] This led the greenback to assume a pivotal role in global commodity trading. Moreover, the artificial demand for petrodollars ensured that, even with continued money printing in America, the value of the US dollar would *not* undergo a drastic depreciation – a principle that continues to hold today. This transformation marked the evolution of the US into an "empire of consumption."[38]

The pivotal question arises: what prompted Saudi Arabia to make the definitive choice of pricing all oil sales *exclusively* in dollars? Traditionally, Saudi Arabia invoiced oil sales in a diverse basket of currencies, including approximately 25 percent in British pounds sterling.[39] However, Saudi Arabia opted to completely abandon the British currency in favor of the US greenback. As disclosed in a recently declassified telegram, Saudi's unexpected move even surprised US Ambassador James Atkins.[40] The lack of Saudi archival materials poses challenges for reaching a conclusive interpretation. However, the deployment of economic incentives and military strategies by prominent figures within the US administration, including Kissinger, Simon, and their contemporaries, appeared to have facilitated the establishment of the petrodollar system.

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[35] David Hammes and Douglas Wills, "Black Gold: The End of Bretton Woods and the Oil Price Shocks of the 1970s," *The Independent Review* IX, no. 4 (Spring 2005): 501–511.
[36] Spiro, *The Hidden Hand*, 132-133, 161.
[37] Ibid., 121.
[38] Charles S. Maier, *Among Empires: American Ascendancy and Its Predecessors* (Cambridge: Harvard University Press, 2007), 238-284.
[39] Terry Robards, "Saudis Reassure Britain on Pound," *The New York Times*, Dec. 14, 1974, https://www.proquest.com/historical-newspapers/saudis-reassure-britain-on-pound/docview/120156924/se-2.
[40] Telegram from Ambassador Akins at Jidda to Secretary of State Kissinger, "SAMA Agrees to Purchase Treasury Issues", Dec. 12, 1974, accessed December 20, 2023, https://aad.archives.gov/aad/createpdf?rid=270129&dt=2474&dl=1345, Access to Archival Databases (AAD).

First, a cornerstone organization, largely conceived by Kissinger, materialized following the Joint Statement in June 1974.[41] This entity, the *United States-Saudi Arabian Joint Commission on Economic Cooperation* (hereinafter referred to as the *Joint Commission*), was created to foster economic cooperation in tandem with oil trade.[42] It was one of only two commissions directly affiliated with the Department of the Treasury, rather than the Department of State or the Department of Commerce, owing to its unique financial and commercial role.[43] In a digest from the Government Accountability Office (GAO), the high-level critical goals of the Joint Commission were outlined as follows:

> The United States-Saudi Arabian Joint Commission on Economic Cooperation, established on the heels of the Arab oil embargo and price increases, (i) fosters closer political ties between the two countries through economic cooperation; (ii) assists Saudi industrialization and development while recycling petrodollars; and (iii) facilitates the flow to Saudi Arabia of American goods, services, and technology.[44]

The specific functions of this somewhat opaque entity remain elusive. Yet, insights into the commission's activities, particularly toward the conclusion of the TCA's initial five-year term, can be indirectly gleaned. The US government directed special attention to the Joint Commission, prioritizing projects that would yield "highly visible, tangible results" in Saudi Arabia.[45] According to a GAO report, by September 1978, 16 projects, amounting to approximately $800 million, were in progress under the Joint Commission. These projects spanned various sectors, including manpower training, agriculture, electronic services, highway transportation, and other critical elements of Saudi infrastructure development.[46] The scale of the economic aid and collaboration was

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[41] Henry Kissinger, "Joint Statement on Saudi Arabian-United States Cooperation. Washington, D. C. June 8, 1974," *Middle East Journal* 28, no. 3 (1974): 306.
[42] Government Accountability Office, *The US-Saudi Arabian Joint Commission on Economic Cooperation*, 5.
[43] Spiro, *The Hidden Hand*, 89, 123. The other exception was the Iranian Commission, which was also assigned to the Department of the Treasury.
[44] Government Accountability Office, *The US-Saudi Arabian Joint Commission on Economic Cooperation*, 5.
[45] US Congress. House, Committee on Government Operations, Subcommittee on Commerce, Consumer, and Monetary Affairs, *Federal Response to OPEC Country Investments in the United States (Part I: Overview)* (Washington, DC: GPO, 1981), 1107.
[46] Government Accountability Office, *The US-Saudi Arabian Joint Commission on Economic Cooperation*, 25 (Table 4).

reflected in the dramatic rise in US exports to Saudi Arabia, which surged from $400 million in 1973 to $4.9 billion by 1979.[47]

The effectiveness of the economic measures worked wonders. Throughout much of 1974, OPEC considered adopting a basket of currencies for oil pricing, including IMF's SDRs.[48] However, Saudi Arabia leveraged its status as the leading producer in OPEC to sway the group toward pricing and selling oil in US dollars.[49] By 1975, US dollars had become the standard currency for oil trade among all OPEC countries.[50]

US military influence appears to have been another contributing factor in shaping Saudi Arabia's decision. Following the Joint Statement, the US bolstered military cooperation with Saudi Arabia, pledging to protect against Israel through various military means, including arms sales, information sharing, and military training, among other strategies.[51] A specialized joint military commission was established to ensure the kingdom's security.[52] By the conclusion of the first 5-year term of TCA, it was estimated that this commission had approved arms sales totaling $3.5 billion to Saudi Arabia, encompassing advanced weapons and equipment.[53]

Meanwhile, the US had maintained a stance of pressure toward Saudi Arabia before the signing of the TCA. For example, US Secretary of Defense James Schlesinger declared that there was a "risk" of employing military power against the Arabs.[54] In January 1975, Henry Kissinger, during an interview, stated that the US "could not rule out

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[47] William G. Miller, *William Miller's Subject Files*, 88, accessed December 20, 2023, https://fraser.stlouisfed.org/archival/6012/item/584036, Jimmy Carter Library.
[48] Occasionally, OPEC brought up proposals of switching to a basket of currencies; see, for example, the discussion in "OPEC Might Switch to S.D.R.'s If Dollar Plummets, Official Says," *The New York Times*, Aug. 4, 1977, https://www.proquest.com/historical-newspapers/opec-might-switch-s-d-r-if-dollar-plummets/docview/123400751/se-2.
[49] Costigan, Cottle, and Keys, "The US Dollar as the Global Reserve Currency," 110.
[50] Jahangir Amuzegar, "OPEC and the Dollar Dilemma," *Foreign Affairs* 56, no. 4 (1978): 740-750, https://doi.org/10.2307/20039989.
[51] Government Accountability Office, *Perspectives on Military Sales to Saudi Arabia*, 19-21, Oct 26, 1977, accessed December 20, 2023, https://www.gao.gov/products/id-77-19a.
[52] Gwertzman, "'Milestone' Pact."
[53] Toby Craig Jones, "America, Oil, and War in the Middle East," *Journal of American History*, no. 1 (2012): 212.
[54] Drew Middleton, "A Word to the Arabs---'Risk'---Is Kicking Up a Storm," *The New York Times*, Jan. 12, 1974, https://www.proquest.com/historical-newspapers/word-arabs-risk-is-kicking-up-storm/docview/119986758/se-2.

completely the use of military force against oil-producing nations" in the event "where there is some actual strangulation of the industrialized world."[55] Indeed, the beginning of 1975 witnessed a surge in articles across various US newspapers and magazines, advocating for armed intervention to seize oil fields in the Middle East.[56] According to US Ambassador James Akins, Kissinger was the orchestrator behind these publications. Whether these threats were bluffs or not, they instilled a sense of unease and fear in the Middle East, as noted by Akins, and seemed to achieve their intended effect.[57] In mid-February 1975, the Saudi government formalized the TCA, laying the groundwork for the implementation of the Joint Commission's goals.[58]

Remarkably, recently declassified documents reveal that Saudi's decision was also significantly influenced by an "add-on" deal between the United States and Saudi Arabia, a 41-year-old secret that remained undisclosed until 2016.[59]

Enhancing Petrodollar Recycling: Unveiling the Secret "Add-on" Arrangement

Under the new "dollar-for-oil" system, oil-producing nations amassed significant petrodollar surpluses, yet their "low capacity" made it difficult to absorb these funds solely through imports.[60] Anwar Ali, the head of Saudi Arabia's central bank in 1973, remarked, "We are sinking under a sea of billions of dollars."[61] Therefore, there was a need to reinvest the surpluses back into oil-importing countries, a process known as *petrodollar recycling*.[62] The US, Japan, Britain, and other Western

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[55] Bernard Gwertzman, "Kissinger Speaks of Force as Last Step 'In the Gravest Emergency' Over Oil," *The New York Times*, Jan. 3, 1975, https://www.proquest.com/historical-newspapers/kissinger-speaks-force-as-last-step-gravest/docview/120615103/se-2.

[56] Sargent, *A Superpower Transformed*, 154.

[57] US Department of State, "Airgram from the Ambassador to Saudi Arabia (Akins) to the Department of State," *Foreign Relations of the United States, 1969–1976, Volume XXXVII: Energy Crisis, 1974-1980* (Washington, DC: GPO, 2001), accessed December 20, 2023, https://history.state.gov/historicaldocuments/frus1969-76v37/d52.

[58] Government Accountability Office, *The US-Saudi Arabian Joint Commission on Economic Cooperation*, 11.

[59] Andrea Wong, "The Untold Story Behind Saudi Arabia's 41-Year US Debt Secret," *Bloomberg*, May 30, 2016, accessed December 20, 2023, https://www.bloomberg.com/news/features/2016-05-30/the-untold-story-behind-saudi-arabia-s-41-year-u-s-debt-secret.

[60] Committee on Government Operations, *Federal Response*, 333 (Appendix 2A).

[61] Sargent, *A Superpower Transformed*, 139.

[62] Committee on Government Operations, *Federal Response*, 235.

industrialized countries all engaged in this fierce "battle for the petrodollar [deposits]."[63]

A prevailing neoliberal interpretation of petrodollar recycling posits the 1970s as a time when OPEC's financial resources were deposited into Western commercial banks, which then lent money to oil-consuming nations.[64] Throughout this process, the appeal of dollar-denominated assets was attributed to the forces of "free market" dynamics.[65]

However, in 1999, David Spiro's research revealed the US government's unilateral maneuver to guide petrodollar recycling by *directly* transacting its government bonds with Saudi Arabia.[66] His findings indicated a covert "add-on" deal between the United States and Saudi Arabia to funnel Saudi oil revenues into the US bond market, an agreement whose details and execution had long been shrouded in mystery.[67] It was not until 2020 that political scientist Duccio Basosi shed new light on the matter, by unveiling a declassified telegram from Ambassador Atkins to Kissinger, dated December 12, 1974. This document offered definite proof of the special arrangement's existence and formalization date:

> The Saudi governor accepted the proposal to have a new confidential relationship through the Federal Reserve with the treasury borrowing operation. When announcement of an issue is made, SAMA will be queried as to its interest in purchasing additional amounts of the same issue at the average price of the auction. Certificates for these additional amounts will be issued and probably deposited in one of the banks on deposit for SAMA. In the event that SAMA wishes to dispose of these issues ahead of their date of maturity for any reason, notification will be given Treasury at least two days ahead so that market forces can be evaluated and an offer made to SAMA if judged necessary to prevent disruption of the ordinary market in such issues.[68]

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[63] Spiro, *The Hidden Hand*, 94-95.
[64] Bessma Momani, "Gulf Cooperation Council Oil Exporters and the Future of the Dollar," *New Political Economy* 13, no. 3 (2008): 301.
[65] Basosi, "Oil, Dollars, and US Power in the 1970s," 3-4.
[66] Spiro, *The Hidden Hand*, 37.
[67] Ibid., 105-116.
[68] Telegram from Ambassador Akins at Jidda to Secretary of State Kissinger, "SAMA Agrees to Purchase Treasury Issues." Reproduced in Basosi, "Oil, Dollars, and US Power," 8.

The operation brought significant benefits to the United States. Recycling petrodollars into the US Treasury provided a reliable flow of funds without exerting undue price pressure. This influx of capital could be redistributed to correct economic imbalances, finance development projects, and alleviate America's deficits.[69] In this manner, it promoted steady growth of the US economy with minimal inflationary impact, at least until the implementation of "open-ended" QE during the pandemic.[70] Ironically, while the oil crisis and the rise of OPEC facilitated "the largest nonviolent transfer of wealth in human history" from industrialized states to developing nations, petrodollar recycling led to roughly 70 percent of Saudi surplus assets ending up in the US Treasury.[71]

Given the unavailability of the add-on agreement's specific details to the public, this essay turns to indirect sources, such as Congressional hearings and reports from governments and organizations, to provide substantial evidence of at least *two* significant commitments made by the US in December 1974.

Throughout the negotiations, the Saudi government placed significant emphasis on "the necessity of confidentiality" regarding its investments.[72] In response, the US Treasury orchestrated a discreet and sophisticated system for the acquisition of US debt. Fragments of this arrangement can be discerned through a 1979 Congressional investigation, prompted by concerns surrounding the notable expansion of OPEC's investments in US financial institutions:

> The specific arrangement with Saudi Arabia assuring confidentiality of OPEC assets ... included a system, through the Federal Reserve Bank of New York, where Saudi purchases of US Treasury securities could be

[69] Momani, "Gulf Cooperation Council Oil Exporters and the Future of the Dollar," 301-302.
[70] Rebucci, Hartley, and Jiménez, "An event study of COVID-19 central bank quantitative easing in advanced and emerging economies," 2-14.
[71] See Steven A. Schneider, *The Oil Price Revolution* (Baltimore: Johns Hopkins University Press, 1983), 1 ("the largest nonviolent transfer"). For the estimate, see Nathaniel Sher, "The 1973 Oil Embargo and US-Saudi Relations: An Episode in New Imperialism" (Thesis, Oberlin College, 2017), 54, accessed December 20, 2023, https://digitalcommons.oberlin.edu/honors/192.
[72] Telegram from Ambassador Akins at Jidda to Secretary of State Kissinger, "SAMA Agrees to Purchase Treasury Issues."

> handled outside the regular market, but at prices determined by the regular auction.[73]

The mechanism can be delineated into three fundamental components. Firstly, the "add-on" arrangements enabled the Saudi Arabian government to *bypass* the conventional bidding process and acquire bonds discreetly, enabling substantial purchases of securities outside standard markets.[74] Secondly, Secretary Simon's assertion that "[a]t no time was Saudi Arabia given securities at preferential rates"[75] was factually incorrect. In typical bond markets, increased demand leads to higher prices and lower interest rates.[76] In contrast, the Saudis were offered fixed "add-on" deals without bidding, at rates surpassing market rates.[77] Lastly, the aforementioned Joint Commission serves as the principal conduit, operating as "an important channel for recycling petrodollars and promoting US business."[78] Within the commission, an Interagency Action Group was established, with a pronounced focus on facilitating petrodollar recycling.[79]

With these three components of the add-on in place and the signing of the TCA, Saudi's initial purchase of $2.5 billion in Treasury securities commenced through the Federal Reserve Bank of New York in February 1975.[80] Later, the "add-on" facilities were extended to include other OPEC nations, providing them unique advantages in US investment markets.[81]

Furthermore, the add-on agreement seemingly included a "nondisclosure policy" that persisted for more than forty years. The US Treasury intentionally concealed the financial transactions between Saudi Arabia and the US Government, hampering efforts to track petrodollar investments. For instance, during a press conference in May 1979, when

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[73] US Congress. House, Committee on Government Operations, *The Adequacy of the Federal Response to Foreign Investment in the United States* (Washington, DC: GPO, 1980), 120-121.
[74] Ibid., 121.
[75] Committee on Government Operations, *Federal Response*, 117.
[76] Spiro, *The Hidden Hand*, 109.
[77] Committee on Government Operations, *The Adequacy*, 120.
[78] Miller, *William Miller's Subject Files*, 59.
[79] Government Accountability Office, *The US-Saudi Arabian Joint Commission on Economic Cooperation*, 18.
[80] US Congress. House, Committee on Government Operations, Subcommittee on Commerce, Consumer, and Monetary Affairs, *The Operations of Federal Agencies in Monitoring, Reporting on, and Analyzing Foreign Investments in the United States (Part 2: OPEC Investments in the United States)* (Washington, DC: GPO, 1979), 77. Further details are available in the Memorandum to the Secretary of State.
[81] Spiro, *The Hidden Hand,* 125.

queried about the lack of transparency regarding the Saudi Arabia Trust Account, the Treasury responded, "[t]he holdings of the Saudi Arabian Trust Account with Treasury are excluded … because the investments represent *prepayments* … through the US-Saudi Arabian Joint Commission and not financial investments."[82]

In particular, the US Treasury aggregated Saudi Arabia's assets with those of other oil exporters and then obscured the data by categorizing transactions based on *regions*, avoiding the disclosure of specific country-by-country holdings.[83] This evidence can be found in a study by the Committee on Government Operations referenced below:

> [a]n extensive review of documents ... reveal[s] beyond question that there is an agreement with Saudi Arabia and Kuwait to keep their US assets secret by publishing OPEC country investments in general regional categories, such as 'Other Asia' and 'Other Africa.' This policy of nondisclosure has been applied so that Federal agencies or groups needing information about these countries' assets are regularly denied it.[84]

The official reason for this confidentiality, according to Assistant Secretary of the Treasury Fred Bergsten, was that holdings by official foreign institutions from the primary oil-producing nations in the Middle East constituted 90 percent or more of the total assets for each of these countries. Consequently, disclosing data on a country-by-country basis would essentially reveal the assets of these official institutions within each respective nation.[85] William Simon assumed a pivotal role in negotiating the add-on arrangement from July to December 1974.[86] In a conversation with an auditor, the former Secretary of the Treasury stressed that that "this regional reporting was the *only* way in which Saudi Arabia would agree to the deal for add-ons."[87]

Remarkably, a series of GAO inquiries spanning from the late 1970s to the early 1980s did *not* result in any disclosure of statistics regarding Saudi investment.[88] Throughout the years, the Treasury consistently cited the International Investment and Trade in Services

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[82] Miller, *William Miller's Subject Files*, 68. Emphasis added.
[83] Basosi, "Oil, Dollars, and US Power in the 1970s," 8.
[84] Committee on Government Operations, *The Adequacy*, 119-120.
[85] Government Accountability Office, *The US-Saudi Arabian Joint Commission on Economic Cooperation*, 36.
[86] Spiro, *The Hidden Hand*, 88-91.
[87] Committee on Government Operations, *The Operations*, 80. Emphasis added.
[88] Basosi, "Oil, Dollars, and US Power," 8.

Survey Act of 1976 and Executive Order 12065 of 1978 to maintain that neither the State Department nor the Central Intelligence Agency required data on OPEC finances to fulfill their respective duties.[89] In March 2016, the US Treasury released Saudi Arabia's $117 billion of US Treasuries for the first time since 1974, though some speculate that Saudi Arabia may have held even more US debt.[90] This belief is well-founded, as in April 2016, Saudi Arabia cautioned the US that it could potentially divest up to $750 billion in US Treasuries if Congress passed a bill that might hold the kingdom accountable for the September 11 attacks.[91]

Before concluding this section, it is worth noting that amidst the negotiations with the US Treasury, Saudi Arabia also engaged in discussions with the British Chancellor of the Exchequer, Denis Healey.[92] However, it was during Healey's three-day visit from December 9 to 12, 1974, that the add-on deal was struck, resulting in the complete switch to the US dollar from the British pound. Although the precise details of the petrodollar recycling battle are not fully transparent, our analysis suggests that US commitments such as exclusive pre-auction purchasing, preferential rates, and assurances of confidentiality may have significantly influenced Saudi Arabia's decision.

The confidential add-on agreement and the Joint Commission facilitated the petrodollar recycling system, bolstering the prominence of the greenback in the international monetary landscape. However, these developments also raised concerns and triggered debates.

Debates and Maturation of the Petrodollar System

The discussions surrounding "dollar hegemony" have a rich historical lineage. Interestingly, in the 1970s, notably more politicians and economists resisted the petrodollar system, recognizing the

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[89] See Wong, "The Untold Story," and Tad Szulc, "Recycling Petrodollars: The $100 Billion Understanding: OEC," *The New York Times*, Sept. 20, 1981, https://www.proquest.com/historical-newspapers/recycling-petrodollars-100-billion-understanding/docview/121679742/se-2.

[90] Wong, "The Untold Story."

[91] Mark Mazzetti, "Saudi Arabia Warns of Economic Fallout if Congress Passes 9/11 Bill," *The New York Times*, Apr. 15, 2016, https://www.proquest.com/blogs-podcasts-websites/saudi-arabia-warns-economic-fallout-if-congress/docview/1781288478/se-2.

[92] UK Parliament, "Saudi Arabia (Chancellor's Visit)", HC Deb 13 December 1974, vol 883 cc982-8, accessed December 20, 2023, https://api.parliament.uk/historic-hansard/commons/1974/dec/13/saudi-arabia-chancellors-visit.

considerable costs of establishing a new international monetary order, a stance that contrasts with today's prevailing views.

From a political perspective, escalating concerns were voiced by members of Congress and federal officials over secretive foreign investments perceived as threats to the American national interest.[93] Senator Abraham Ribicoff, in a congressional hearing, emphasized that "[t]he recycling of petrodollars as a solution to exorbitant oil prices is a myth. It is also a vicious cycle."[94] He expressed concern that "the feudal monarchies of Arabia [would] buy up the basic industries of the United States while pauperizing the rest of the Western World."[95] Despite lacking immediate evidence of dangers from foreign investments, a June 1978 CIA memorandum expressed concerns about Saudi Arabia using its wealth as a "political weapon," potentially compromising US economic stability.[96] A GAO study captured the prevailing sentiment: "We question the ability of the executive branch to detect such a threat in a timely manner, should it occur."[97]

Economically, the petrodollar system, while strengthening the US dollar and enhancing financial market liquidity, primarily benefited financial institutions that served as the principal channels and recipients of capital inflows.[98] Hence, it was unsurprising that in 1979, when Congress sought disclosures of Gulf Cooperation Council assets in the US, Paul Volcker, then Chairman of the New York Federal Reserve Bank, was among the few to express his dissent: "It is hard to see what interest, including that of disclosure, would be served in that event but there would be obvious drawbacks from the standpoint of US financial markets and institutions, and perhaps repercussions on the dollar itself."[99]

American manufacturers and workers, on the other hand, largely bore the costs.[100] Economic adviser Robert Hormats communicated to

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93 Szulc, "Recycling Petrodollars."
94 US Congress. Senate, Committee on Government Operations. Permanent Subcommittee on Investigation, *Recycling of petrodollars* (Washington, DC: GPO, 1974), 7.
95 Ibid., 9.
96 Committee on Government Operations, *Federal Response*, 980.
97 Government Accountability Office, *Changes Needed to Improve Government's Knowledge of OPEC Financial Influence in the United States* (Washington, DC: GPO, 1979): v, accessed December 20, 2023, https://www.gao.gov/assets/emd-80-23.pdf.
98 Eichengreen, *Exorbitant Privilege*, 173.
99 Government Accountability Office, *The US-Saudi Arabian Joint Commission on Economic Cooperation*, 48
100 Tilford, Simon, and Kundnani, "It Is Time to Abandon Dollar Hegemony," *Foreign Affairs*, July 28, 2020, accessed December 20, 2023,

Kissinger the negative consequences of an overvalued dollar, noting, "[a]n overvalued dollar has meant that US exports have fallen far below imports, which has had serious effects on US employment and has caused an increase in US investment abroad – also having a serious effect on jobs in this country."[101] The petrodollar's impact on the physical industries mirrored historical struggles during the Bretton-Woods era, especially in raising the prices of domestic goods in international markets.[102] Simultaneously, this system led to a surge of cheaper imports, which in turn contributed to job losses in manufacturing and an increase in debt in the United States.[103] By contrast, countries like Germany capitalized on this transition. Trade surpluses in these nations enabled them to buy energy at more affordable rates by leveraging significant dollar reserves. This, combined with lower labor costs, reduced their production expenses and strengthened their competitiveness across manufacturing and other industries.[104]

During the Carter Administration, the adverse effects of the petrodollar system became increasingly evident within the US government. Specifically, Secretary of the Treasury Michael Blumenthal and President's Assistant for National Security Affairs Zbigniew Brzezinski recognized that the US dollar's role as a global reserve currency had led to significant economic disadvantages for the United States. In a memorandum to President Carter, Brzezinski highlighted that:

> the United States was bearing a large and unfair burden as a consequence of the fact that oil is priced in dollars... [Germany and Japan] are becoming 'cheap energy' countries which gives them a strong competitive edge in other areas of industry and international trade, aggravating

https://www.foreignaffairs.com/articles/americas/2020-07-28/it-time-abandon-dollarhegemony.

[101] US Department of State, "Memorandum from Robert Hormats of the National Security Council Staff to the President's Assistant for National Security Affairs (Kissinger)," *Foreign Relations of the United States, 1969–1976, Volume III: Foreign Economic Policy; International Monetary Policy, 1969-1972* (Washington, DC: GPO, 2001), 965, accessed December 20, 2023, https://history.state.gov/historicaldocuments/frus1969-76v03/d174.

[102] Edwin L. Jr. Dale, "Investing Abroad Receives Backing: Senate Inquiry Is Told Such Deals Do Not Eliminate US Workers' Jobs," *The New York Times*, Apr. 27, 1960, https://www.proquest.com/historical-newspapers/investing-abroad-receives-backing/docview/114996337/se-2.

[103] Eichengreen, *Exorbitant Privilege*, 180-181.

[104] Amuzegar, "OPEC and the Dollar Dilemma," 747.

> the problem of trade balances and putting further pressure on the dollar.[105]

Following this, Brzezinski commissioned an analysis to investigate the possibility of shifting from the US dollar to a basket of currencies, including SDRs, for oil pricing. Despite his conviction that pricing oil in dollars was not a wise action, the final decision, made in June 1979, was to uphold the existing system. However, it is essential to recognize that this decision was reluctant, as adopting an alternative approach would have put the US at a disadvantage, as elaborated in the text below:

> [Secretary of] State, [Secretary of] Treasury, CEA [Council of Economic Advisers] and Henry Owen believe that dollar pricing should be maintained for two reasons: (i) An announcement that dollars were no longer being used as the unit of account in paying for oil would trigger selling of dollars on the foreign exchange markets. So we would suffer. (ii) It is hard to see any offsetting gain, since OPEC would probably raise prices in SDR terms, as necessary to recover revenue losses, if the SDR appreciated relative to the dollar.[106]

Brzezinski's reasons underlined the crucial factor in the decision-making – the dollar's central position in exchange markets and its role as a global reserve currency.

Based on available sources before Reagan's presidency, this seemed to be the last official attempt to abolish the petrodollar system. As the dollar-oil standard stabilized and operated smoothly, the dollar's status as the primary world reserve currency and the primary international currency persisted, reaching about 65 percent of reserves in

[105] US Department of State, "Memorandum from the President's Assistant for National Security Affairs (Brzezinski) to President Carter, NSC Weekly Report #95, Washington, May 3, 1979," *Foreign Relations of the United States, 1977–1980, Volume III: Foreign Economic Policy* (Washington, DC: GPO, 2013), 653, accessed December 20, 2023, https://static.history.state.gov/frus/frus1977-80v03/pdf/frus1977-80v03.pdf.
[106] US Department of State, "Memorandum from the President's Assistant for National Security Affairs (Brzezinski) to President Carter, NSC Weekly Report #100, Washington, June 8, 1979," *Foreign Relations of the United States, 1977–1980, Volume III: Foreign Economic Policy* (Washington, DC: GPO, 2013), 661, accessed December 20, 2023, https://static.history.state.gov/frus/frus1977-80v03/pdf/frus1977-80v03.pdf.

1979.[107] Since 1979, the dollar's share of reserves has never fallen below 50 percent.[108]

As the 21st century unfolded, historians have consistently argued that the US dollar's reserve status is the *foremost* driver in American hegemonic power, not merely an auxiliary factor.[109] Political economists contended that the strategic role of the US dollar significantly benefited the United States, particularly in addressing national debt, budget deficits, and the maintenance of military bases.[110] Additionally, due to the US dollar's prominent role as a world reserve currency, the United States has continued to hold a central position in the global trading system.[111]

Conclusion

The Bretton Woods agreement initially established the US dollar's preeminence in global finance by tying it to gold, but its sustainability was compromised by inherent structural flaws known as Triffin's dilemma, culminating in its collapse after the 1971 "Nixon Shock."

The analysis conducted in previous sections challenges the neoliberal assertion that market forces dictated the emergence of the oil-dollar standard, pointing instead to significant US governmental influence. Central to this were the formation of the Joint Mission, the signing of the Technical Cooperation Agreement, and a clandestine supplementary deal, pivotal in steering Saudi Arabia to price oil exclusively in dollars.

Although a more complete picture requires additional sources from Saudi Arabia, it is evident that the Nixon-Ford administration's strategy – a blend of economic incentives, military support, and secret diplomacy – was instrumental in crafting the petrodollar system and guiding its recycling process. The Joint Commission's economic measures were pivotal in convincing Saudi Arabia and other OPEC

[107] US Department of the Treasury, "Appendix 1: An Historical Perspective on the Reserve Currency Status of the US Dollar," 2, Oct 1, 2009, accessed December 20, 2023, https://www.hsdl.org/c/view?docid=748157.
[108] Ibid., 1.
[109] Michael Hudson, *Global Fracture*, 9-31. Also see Susan Strange, "The Persistent Myth of Lost Hegemony," *International Organization* 41, no. 4 (1987): 555. Hudson emphasizes the US dollar's reserve status as central to American hegemony. Conversely, earlier research like Strange's 1987 work assigns it a more modest role among factors of US dominance.
[110] Costigan, Cottle, and Keys, "The US Dollar as the Global Reserve Currency," 116.
[111] National Intelligence Council, "Global Trends 2040: A More Contested World," 49, March 2021, accessed December 20, 2023, https://www.dni.gov/files/ODNI/documents/assessments/GlobalTrends_2040.pd.

members to embrace dollar-based oil pricing. Meanwhile, US military efforts offered both security and strategic leverage, essential for the finalization of these agreements.

Moreover, declassified documents reveal a secret "add-on" agreement between Saudi Arabia and the United States to funnel petrodollars directly back into the US bond market, a strategic move that fostered sustainable growth and curbs inflation. This deal granted Saudi Arabia special advantages in circumventing normal competitive bidding processes and obscured its US debt holdings, practices that continued for decades.

The transformation of crude oil from its fundamental role as a fossil fuel to a "financial instrument" consolidated the US dollar's position as the global reserve currency.[112] This financialization brought political concerns, particularly fears of Saudi Arabia exploiting black gold as a political weapon. Additionally, it had mixed economic repercussions. While beneficial to financial institutions and large businesses, the petrodollar system strained US manufacturing, leading to job losses, increased imports, and higher national debt and deficits. Despite these challenges, the US chose not to shift to a basket of currencies for oil pricing in the late 1970s, a decision that paved the way for the stabilization and smooth operation of the petrodollar system. The continuation of dollar hegemony remains pivotal for US economic prosperity, foreign relations, and national security. Understanding this transition from the gold-dollar standard to the petrodollar system sheds light on the US dollar's enduring influence in international finance, as well as the Federal Reserve's ongoing efforts to maintain a strong, inflation-resistant currency.

[112] Daniel Yergin, *The Quest: Energy, Security and the Remaking of the Modern World* (New York: Penguin Press, 2011), 323.

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