POLICY SPOTLIGHT

Safeguarding Dollar Dominance

Why US fiscal reform is essential to preserve global economic leadership

THOMAS HOENIG | SEPTEMBER 2025

In an era of escalating geopolitical uncertainties, central bankers and financial leaders are grappling with profound questions about the future stability of the global economy. As the US reassesses its domestic policies, trade relationships, global commitments, and international alliances, what are the potential implications for dollar dominance?

In the short term, the answer is quite straightforward: **The dollar will remain the world's reserve currency. Its status may be less certain in the long term, however.** Reserve currency status is not a birthright but a privilege that is earned, and one that can be lost through arrogance and neglect.[1]

The Dollar's Global Role

As the US pivots away from international involvement and adopts policies that favor less open trade, its relations with other countries are increasingly strained. These developments have raised questions about security agreements, introduced unsettling trade disputes, and created new uncertainties about the future global economic order. They have also caused other nations to be less sanguine about US dollar dominance.

For decades, the dollar has been the linchpin of the international financial system—a status cemented by the Bretton Woods Agreement of 1944. This agreement established the dollar as the world's primary reserve currency, initially backed by gold and later sustained by the sheer economic might of the US. **Despite the recent turmoil, the dollar still accounts for over half of the world's trade invoicing and about two-thirds of official foreign exchange reserves, and it still serves as the dominant currency for more than half of**

[1] See Thomas Hoenig, "U.S. Dollar Durability," *FinRegRag*, July 9, 2025, https://www.finregrag.com/p/us-dollar-durability. Scan the QR code below for the full analysis, including sources.

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global GDP. The dollar's status has facilitated trade, investment, and financial stability, providing a reliable store of value and medium of exchange.

Tariff Wars and the Dollar

For now, the dollar's reserve currency status remains robust. But it is not without its challenges, and there are clear signs of growing discontent. Recent US tariffs have triggered growing resentment among trading partners. Imposed harshly and unpredictably, the tariffs threaten global economic stability.

As a result, the world is showing increased frustration with the US and the power of its dollar. As early as 2019 Mark Carney, then governor of the Bank of England and now prime minister of Canada, delivered a significant speech in which he revisited the idea of reducing dollar dominance. More recently, Christine Lagarde, president of the European Central Bank, questioned the dollar's dominance and advocated for a global reserve system that incorporates a mix of leading currencies. Emerging economies have also voiced their goal of being less dependent on the dollar. These developments, while nascent, could gain momentum if US trade relationships sour and trade agreements stall, potentially ending in a more fragmented global economy and currency landscape.

US Debt Financing: The Dollar's Achilles' Heel

While US tariffs may handicap global growth and create resentment among trading partners, the true long-term threat to dollar dominance lies in a loss of confidence in the US economy and its policies. Since 2007, government expenditures—driven by entitlement programs, defense spending, and interest on the national debt—have increased the national debt itself. Without meaningful fiscal reform, federal debt could exceed $55 trillion within the next decade. Such expenditures significantly increase the supply of US government debt, and while the foreign sector has historically been a dependable buyer, there is no guarantee this demand will persist. **As US debt rises and trade dynamics shift, foreign appetite for dollars may diminish, placing pressure on domestic buyers.** As supply exceeds demand, interest rates will have to rise to attract investors.

Unfortunately, Congress has learned that the Federal Reserve System (Fed) can serve as a standing facility capable of creating trillions of new dollars to absorb public debt, temporarily suppressing interest rates. If this practice continues, the Fed will enable Congress to spend beyond sustainable limits, perpetuating the cycle of debt accumulation. The immediate effects may be an inflationary boom, but the dollar will lose value and its appeal as a reserve currency.

A Better Choice

The global economic system must evolve toward a more balanced framework. Policymakers must establish clear rules to govern trade and financial conduct. **For the US to maintain its leadership role and the dollar's dominance, it must more responsibly manage its economy in the decades ahead.** If the US continues to prioritize short-term goals and accumulate massive debt, its economic influence will gradually erode along with the dollar's global role.