Will Crypto Save *the* Dollar?

BY LUCREZIA REICHLIN

Trump may have no other choice.

U.S. President Donald Trump's aggressive trade strategy will soon face a fundamental contradiction: imposing tariffs and rejecting multilateralism in the name of protecting American jobs clash with his stated goal of maintaining the dollar's role as the world's dominant reserve currency. Something will have to give, and the dollar—despite its current strength—will most likely take the hit.

The dollar's role as the dominant medium of exchange in global trade has fueled the growth of the offshore eurodollar market. While this market provides the world with much-needed liquidity, it operates beyond the reach of U.S. regulation and thus lacks direct access to the Federal Reserve's liquidity facilities. In times of financial turmoil, the Fed must act as the world's lender of last resort by extending swap lines—essentially short-term loans—to other central banks, enabling them to funnel dollar liquidity to commercial banks facing shortages. As the 2008 and 2020 crises demonstrated, the stability of the international financial system depends on the certainty of the Fed's safety net.

Backstopping the international financial system is, in a way, the price the United States pays for what Valéry Giscard d'Estaing, France's finance minister at the time, famously called the "exorbitant privilege" of the dollar's global hegemony. Over the years, the greenback's status has translated into an enormous and persistent financing advantage for both the U.S. government and U.S. companies.

Other countries, particularly China, have long sought to reduce their dependence on the dollar. Trump's relentless tariff threats, coupled with his apparent willingness to exploit the size and power of the U.S. economy to secure better trade terms, are bound to accelerate these efforts.

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To be sure, that does not necessarily mean that Trump poses a serious threat to the dollar's international standing. After all, no clear alternative to the dollar has emerged. Moreover, this is not the first time that the United States has unilaterally disrupted the global financial system. In 1971, then-President Richard Nixon—perhaps Trump's most obvious historical parallel—abandoned the Bretton Woods system without consulting America's European allies, leaving them to deal with the sudden appreciation of their currencies. Nixon's move, while drastic, worked: the world embraced flexible exchange rates, and the dollar's supremacy was actually reinforced.

But the world looked very different back then. International trade was far less integrated, and economic ties between the West and Soviet bloc countries were virtually nonexistent. The only potential threats to America's economic dominance came from Japan and Europe—both allies that, much like today, were weak and divided. And even under those favorable conditions, the so-called "Nixon Shock" had far-reaching consequences. For example, one could argue that it led to the creation of the euro.

Today, with China and other emerging economies commanding a growing share of global GDP and trade, it is difficult to imagine that efforts to develop payment systems independent of the dollar won't accelerate if Trump continues to weaponize the greenback. Using the threat of tariffs to browbeat countries into compliance—as he did when Colombia briefly refused to accept deportation flights carrying Colombian migrants who had entered the United States illegally—is a surefire way to fuel the search for alternative reserve currencies.

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Trump's enthusiastic embrace of cryptocurrencies suggests that he and his administration see them as a solution to this problem. Stablecoins, backed by U.S. dollars, share many of the characteristics and advantages that once drove the growth of the eurodollar market. Here, too, issuers operate free of regulatory constraints and do not benefit from direct access to the Fed's liquidity facilities, but with the additional advantage—for some—of complete anonymity.

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The combination of stability and secrecy has already made stablecoins appealing to libertarians and criminals. But if scaled successfully, the same characteristics could also make them useful for settling international trade and serving as a repository of global reserves, thereby indirectly reinforcing dollar supremacy.

Of course, such a scenario would not make the global economy any safer. Since stablecoin issuers' balance sheets include short-term Treasury bills and short-term collateralized loans (repos), they are vulnerable to runs—much like money-market mutual funds. Consequently, they require a backstop, which forces them to rely on the certainty of Fed intervention during crises.

This risk may explain Trump's opposition to a Fed-issued central bank digital currency. Such a currency could enhance financial stability but would not guarantee anonymity, making it unpopular with cryptocurrency advocates and, for that matter, commercial banks.

Perhaps that is why Trump has favored a private sector-driven crypto policy. Notably, this approach mirrors Nixon's, who—as the Bretton Woods system unraveled in the early 1970s—rejected a multilateral solution in favor of a unilateral shift to flexible exchange rates. Regardless of Trump's reasoning, such a strategy might be his best chance to preserve the dollar's global status without embracing the multilateralism he reviles. ◆