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A Weaker Dollar Fits Trump's Plan

CAPITAL ACCOUNT

By Greg Ip

President Trump's disclosure Tuesday that he was pleased with a weaker dollar should in theory not matter. His preferences are well-known and words shouldn't move markets unless backed by action.

In this case, though, expect action to back these words. Last week, the Federal Reserve on behalf of the Treasury made inquiries on the value of the yen, seen as a prelude to selling dollars in exchange for yen, possibly in cooperation with the Japanese authorities.

On Wednesday, Treasury Secretary Scott Bessent said the U.S. hadn't intervened. But he has previously brought up currency values with his counterparts in Japan and South Korea. On Tuesday, Trump complained that China and Japan "always wanted to devalue."

—Note

Ordinarily, intervention can't sustainably alter exchange rates unless backed by economic fundamentals— most important, monetary policy. There, too, the odds favor a lower dollar. Trump plans to appoint a new Fed chair who will cut rates to boost growth and the stock market, not raise them be--cause of the hypothetical risk that tariffs, a weak dollar or low unemployment pose to inflation.

Thus, the dollar's decline isn't run-of-the-mill market noise, but the natural result of the U.S. giving priority to the dollar's domestic role over its global one. This doesn't by a long shot spell the end of its reserve status. But it is another tremor shaking up assumptions about the global economy.

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The last concerted effort by the U.S. to lower the dollar's value was the Plaza Accord in 1985 with other major nations, followed by the Louvre Accord in 1987 to arrest its decline. Since then, dollar policy has mostly consisted of benign neglect: rhetorical support for a strong dollar without any action.

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The dollar is the world's reserve currency, the preferred unit for cross-border trade and finance, and for storing wealth. This makes it easy for the U.S. to issue trillions of dollars of Treasury debt.

Note Note

But foreign demand for that debt tends to push the dollar higher, worsening the U.S. trade deficit and undermining manufacturing. In other words, the trade deficit and the world's demand for Treasurys are two sides of the same coin.

"Prior Administrations prioritised capital markets performance and believed that the deindustrialisation of the US was a necessary side-effect of a more efficient global economy," Stephen Jen, a currency strategist with Eurizon SLJ Capital, wrote this week. He added that Trump rejects this consensus, seeing reindustrialization as necessary to national security.

Before the 2024 election, Stephen Miran, later a White House adviser and now a Fed governor, floated a "Mar-a-Lago" accord in which other countries would agree to weaken the dollar in exchange for tariff relief. The proposal went nowhere, but its spirit lives on.

While Bessent on Wednesday repeated the "strong dollar" mantra, Trump himself has never subscribed to it, telling the Journal in 2017, "I think our dollar is getting too strong…That will hurt ultimately."

In Trump's view, a strong dollar, like higher interest rates, interferes with his priorities: faster growth, reshored manufacturing and a smaller trade deficit.

Historically, the dollar appreciated when the U.S. economy outperformed. That's what happened in the decade before Trump's election in 2024 and investors assumed that would continue under his policies. Even his tariffs were seen as positive for the dollar, since exchange rates tend to offset tariffs' effects.

But in April, when Trump imposed steep tariffs on almost everyone, that traditional relationship broke down. Optimism about artificial intelligence has since de-livered better-than-expected economic growth and stock market records. Yet the dollar has ground lower and gold, a hedge against a falling dollar, has soared.

Trump's trade wars and threat to annex Greenland, and his demands that the Fed bend to his political priorities, have shaken confidence in international relations and U.S. institutions. Investors have responded by trying to reduce exposure to the dollar without reducing exposure to U.S. stocks, such as through hedging.

For a decade, the dollar "has been a one-way trade," said Ajay Rajadhyaksha, global chair of research at Barclays. "Suddenly, it seems that might be stopping. If the U.S. administration is comfortable with a weaker currency, which it seems like it is, the dollar is no longer a one-way trade. That changes everything."

There could be near-term benefits to the U.S. economy. While currency depreciation and tariffs both discourage imports, a lower currency also boosts exports, without the uncertainty and distortions that tariffs entail.

Note

But there are potential costs. Research has found investors are willing to give up some return to own "safe" assets such as dollar-denominated Treasury bonds, which are backed by the strength of the U.S. government. This safety premium lowers the U.S.'s borrowing costs.

Since April, that premium has eroded, said Hanno Lustig, a finance professor at Stanford University. "Investors are slowly starting to worry about the safety of Treasurys," he said. They aren't concerned about default, but perhaps that the U.S. will let inflation rise to reduce the real value of its debts, he added.

Note

A lower dollar could also add to inflation through imported goods and commodity prices, which are denominated in dollars and tend to rise when the dollar falls. Oil prices are up so far this year and mortgage rates are roughly flat, even as Trump seeks to bring both down.

What won't happen: panic selling of the dollar of the sort that has brought smaller countries to their knees. Whatever its flaws, the world has no alternative as a reserve currency. That is one assumption about the world that looks safe.

