April 17, 2025

The Dollar Endures: Strength, Stability, and Global Trust

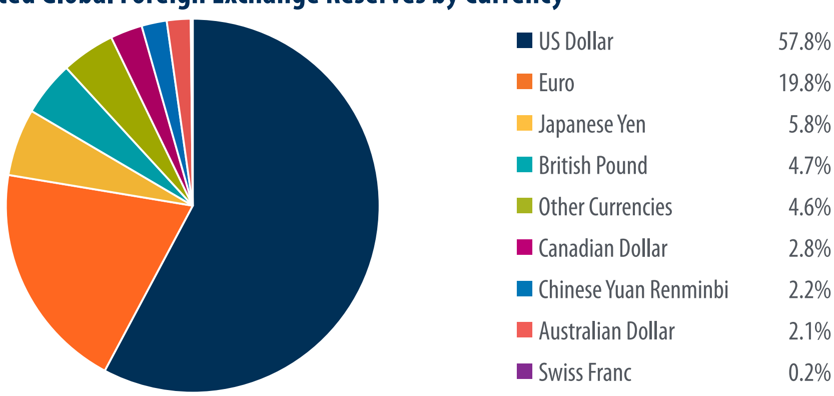
In this week's installment of "Three on Thursday," let's explore some of the dynamics surrounding the United States dollar. In an era of inflation, massive debt, large deficits, and threats of tariffs, there are persistent rumors circulating that the dollar is at risk of losing its reserve currency status. These rumors are stoked by the desire of China (and others) to see this happen. We think these fears are vastly overblown. The U.S. is not strong because the dollar is the reserve currency, the dollar is the reserve currency because the U.S. is strong. Not just in economic might, but in its governance. The Constitution still stands, along with its protections of private property rights and the rule of law, which have created honest, deep and liquid financial markets. The U.S. remains one of the few places where people risk their lives daily to get into, not out of. To provide further insight, we've included three informative charts below.

U.S. Dollar Spot Index

Source: ICE Futures, First Trust Advisors. Quarterly data Q1 1975 – Q1 2025.

Contrary to popular belief, the U.S. dollar has been strengthening—not weakening—over the past five years, as measured by the Dollar Index Spot (DXY), which measures the dollar against a broad basket of currencies. While the index has retreated from its recent high of 109.96 on January 13th, yesterday's reading of 99.4 still places the dollar at a historically elevated level. In times of global uncertainty and economic distress, the dollar remains a trusted store of value and a symbol of safety for investors around the world. Looking ahead, the potential implementation of new tariffs in the U.S. could actually place additional upward pressure on the dollar. Tariffs tend to curb demand for foreign goods, reducing the need for foreign currencies. At the same time, foreign countries may need to increase their purchases of U.S. dollars to sustain trade, further boosting demand. The net result? A stronger dollar relative to its global peers.

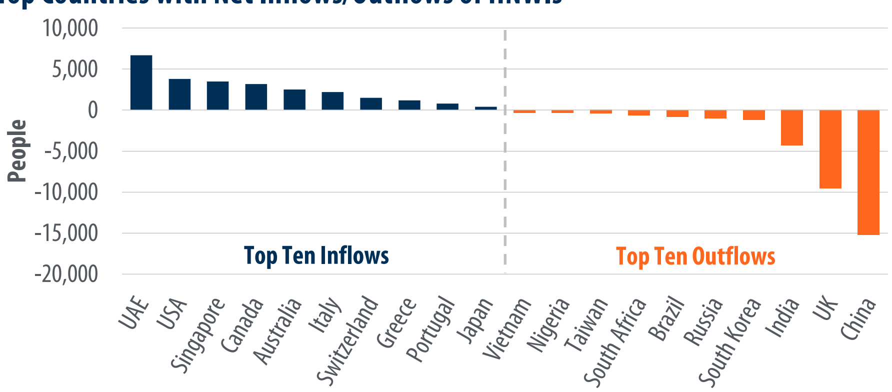
Allocated Global Foreign Exchange Reserves by Currency



Source: International Monetary Fund, First Trust Advisors. Data as of Q4 2024.

The most recent International Monetary Fund (IMF) data through the fourth quarter of 2024 shows that the U.S. dollar comprised 57.8% of official foreign exchange reserves. This was followed by the Euro at 19.8%, the Yen at 5.8%, and the British Pound at 4.7%. The Chinese Yuan stood at a modest 2.2%. It's worth noting that the USD's share of foreign exchange reserves has declined over time; for instance, in 1999, it constituted 71.0% of the total reserves, followed by the Euro at 17.9%, and the Yen at 6.4%. This decrease can be attributed, in part, to foreign reserve managers diversifying their portfolios by including various smaller currencies. Nevertheless, it's evident that the dollar continues to maintain a significant lead as the world's primary reserve currency.

Top Countries with Net Inflows/Outflows of HNWIs



Source: Henley & Partners, First Trust Advisors. Annual data for 2024. **Hight Net Worth Individuals (HNWI)** defined as those with investable wealth of USD 1 million or more.

There is a common belief that China's yuan could potentially replace the U.S. dollar as a new reserve currency, or that the BRICS nations (Brazil, Russia, India, China, South Africa) might create a common currency for trade that could challenge the dollar's dominance. However, you cannot replace a stronger currency with a weaker one. It just doesn't work. Looking at the countries who are seeing the largest outflows of high-net-worth individuals in 2024, China led the list, with a projected net outflow of 15,200 people, followed by the UK, then India. Interestingly, among the top ten countries experiencing the largest outflows of wealthy individuals, half are the BRICS nations. In contrast, the United States has seen the second largest projected increase (+3,800) in high-net-worth individuals. Can a country that can't keep its most productive citizens gain the confidence of other nations to adopt its currency? We think not. The current economic and geopolitical realities suggest that the U.S. dollar's dominance remains robust.