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**Dollar in Retreat, Euro on the Rise: Tariffs,
Stablecoins, De-Dollarization, and the ECB's
Dilemma**

By

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31 July 2025

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Dollar in Retreat, Euro on the Rise: Tariffs, Stablecoins, De-Dollarization, and the ECB's Dilemma

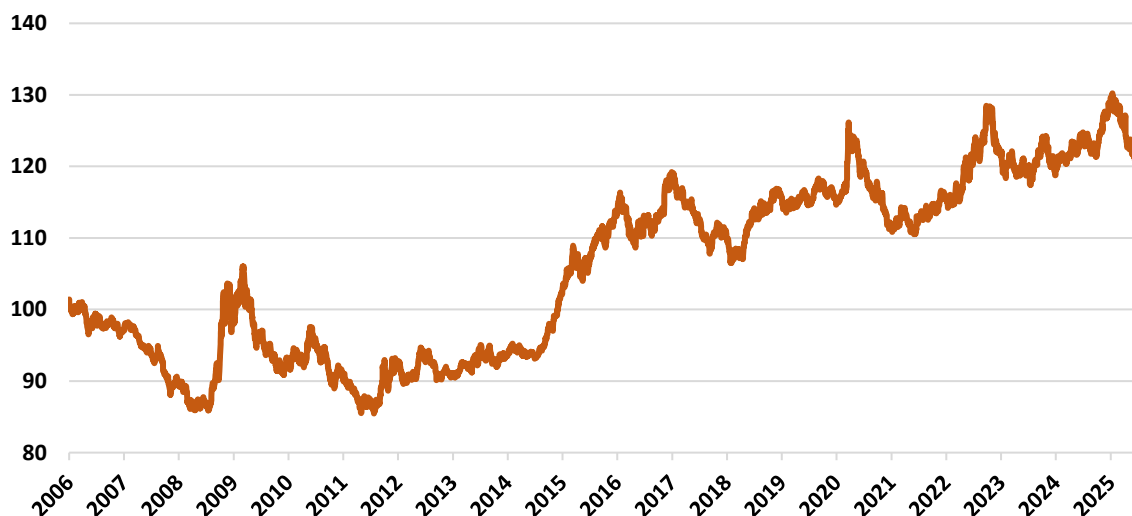
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Executive Summary

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- ✦ The US dollar has fallen to multi-year lows, driven by Trump's tariff policies, fiscal uncertainty, and growing investor doubts about US economic governance.
- ✦ In this context, the euro's recent strength should not be seen in isolation, but rather as a mirror of the dollar's relative fall.
- ✦ Markets interpreted tariffs not as strategic tools but as signs of policy volatility, undermining confidence in the dollar and triggering capital outflows.
- ✦ Trump's political pressure on the Federal Reserve and proposed fiscal expansions (e.g., "One Big Beautiful Bill") have deepened concerns about debt sustainability.
- ✦ Rising US debt and geopolitical instability have led investors—especially in Asia—to reduce their exposure to US assets, with gold hitting record highs as a safe haven.
- ✦ ECB President Lagarde argued that the weakening dollar opens space for the euro to gain global relevance—if backed by reforms, deeper capital markets, and military credibility.
- ✦ A 14% rise in the euro risks pushing inflation below target and hurting exports, putting pressure on the ECB to consider rate cuts despite ongoing trade uncertainty.
- ✦ BRICS nations and the Global South are accelerating efforts to reduce reliance on the dollar, building parallel financial systems and institutions.
- ✦ The US is turning to financial innovation, notably dollar-backed stablecoins under the GENIUS Act, to preserve dollar dominance by generating new foreign demand for Treasuries.
- ✦ Despite its recent appreciation, the euro's global ascent is constrained by Europe's economic stagnation and lack of safe euro-denominated assets.
- ✦ The dollar's retreat is not a collapse but a realignment; the euro may gain regional ground, but the broader trend points to a multipolar global monetary system.

Key Picture: Nominal Broad US Dollar Index (Index Jan 2006=100)



Source: FRED

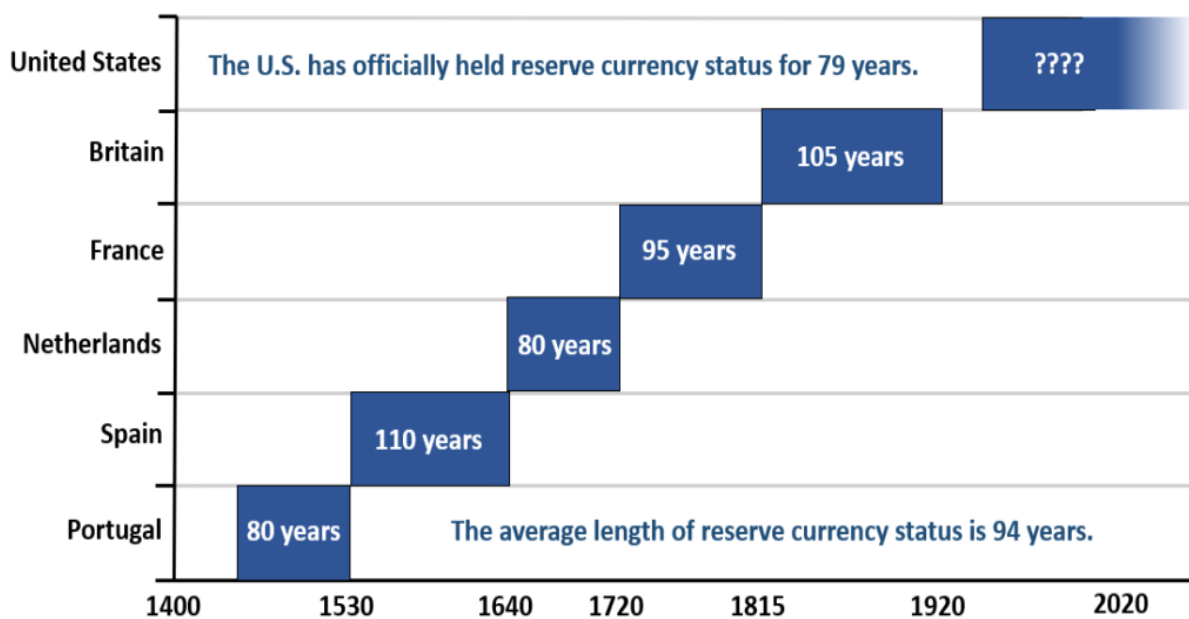
Introduction

At the recent ECB's annual conference in Sintra, Portugal, [a recurring question](#) dominated the conversations: Is the era of dollar dominance coming to a close after barely 80 years (**Figure 1**)? For decades, the US dollar has enjoyed an "exorbitant privilege" controlling the supply of the world's main trading and financial currency. Yet the [dollar has recently fallen to its lowest levels](#) since the early days of the Trump administration, raising questions about its long-term trajectory. Mostly analysts point to [rising tariffs and policy uncertainty](#) as the main culprits. In this context, ECB President Christine Lagarde is capitalising on the battered dollar to promote the ["euro's moment"](#).

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During the conference, Lagarde suggested the euro could emerge as a viable global alternative. [Lagarde argued](#) that for the euro to become a true global alternative, Europe must develop deeper and more liquid capital markets, strengthen its legal framework, and back its open trade ambitions with credible security capabilities.

Figure 1: History of Reserve Currency Status



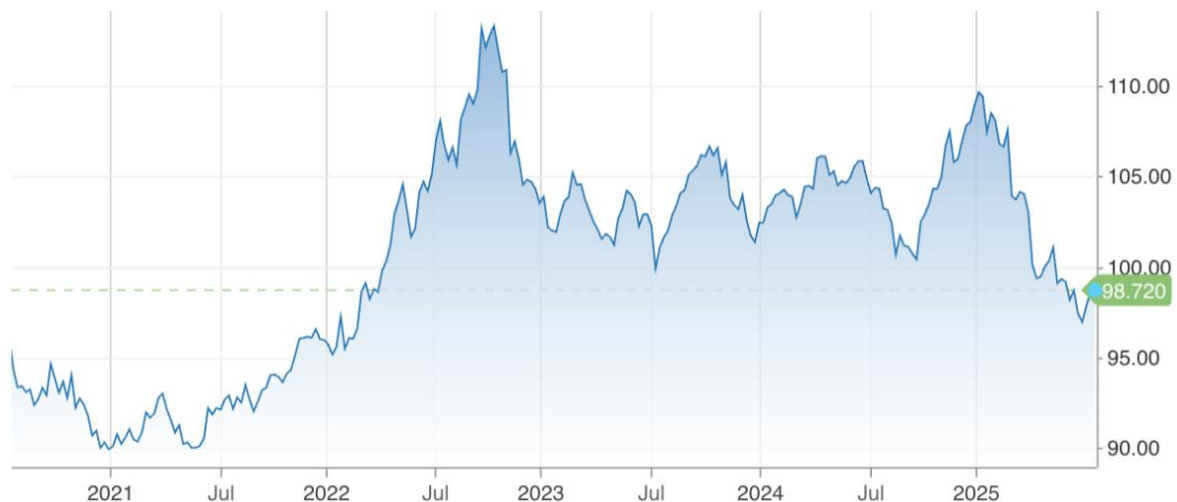
Source: [Smedley Financial](#)

What's Behind the Dollar's Decline?

Contrary to expectations from many economists, [including those within the administration](#), the "Liberation Day" tariffs triggered a sharp drop in the dollar and a brief spike in Treasury yields. This diverged from textbook theory, which holds that tariffs reduce import demand, limit the global supply of dollars, and thus cause the dollar to appreciate. Bessent argued in defense of the tariffs: a 10% levy could be offset by a 4% appreciation in the dollar, minimizing the impact on consumer prices. In theory, as imports decline, fewer dollars are exchanged for foreign currencies, creating upward pressure on the dollar's value. This dynamic, Bessent suggested, would prevent tariffs from being fully passed on to US consumers.

In practice, however, markets interpreted the tariffs not as a strategic tool but as a sign of growing policy unpredictability. Instead of tightening global dollar liquidity, the move spooked investors, weakened the dollar, and raised doubts about US economic stewardship. At first glance, the recent drop in the US dollar might seem dramatic. The greenback is down [roughly 10%](#) since the beginning of the year, including a sharp 4.5% fall in April alone (**Figure 2**). Back in 2011, a similar downgrade by S&P triggered a rally in the dollar and a drop in Treasury yields, as the Eurozone crisis made US assets the safest haven. But in 2025, the response was markedly different. Markets had already been rattled by the tariff announcements.

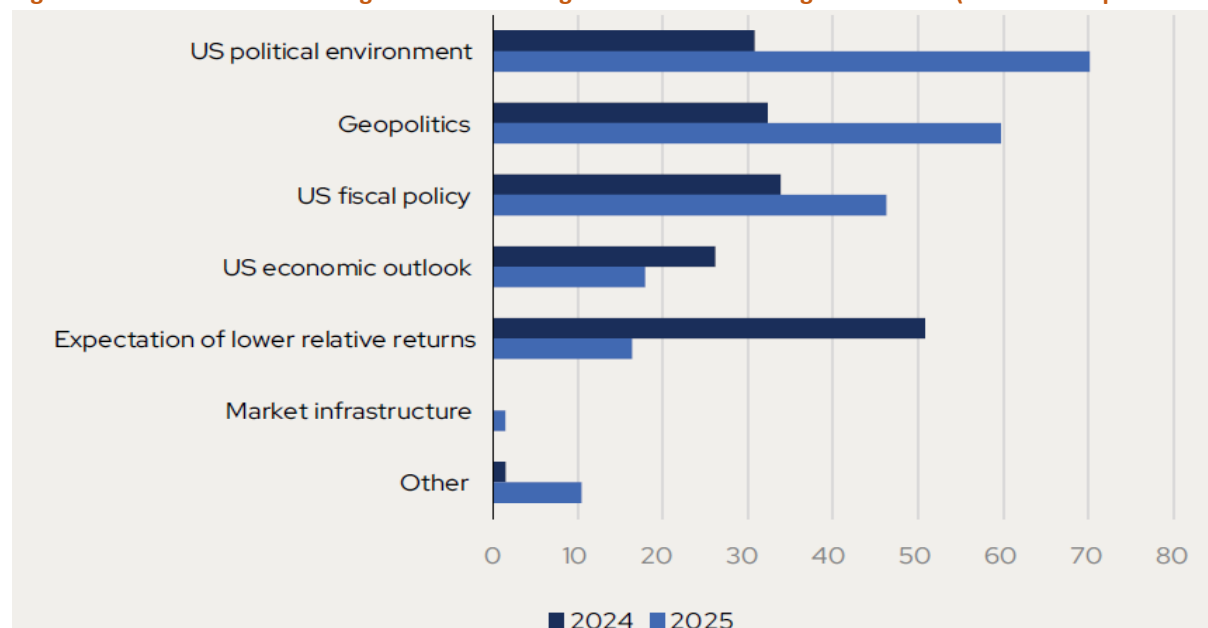
Figure 2: US Dollar Index



Source: Investing.com

Polls suggested that the US political environment is among the key factors behind the decision by investors to divest from USD-denominated assets (Figure 3). President Trump's erratic tariff strategy and repeated attacks on the Federal Reserve's independence have eroded confidence in the dollar as a safe haven. Economists are also uneasy about his proposed "[One Big Beautiful Bill](#)," which would extend 2017 tax cuts, slash welfare spending, and significantly expand public borrowing. [The non-partisan CBO estimates](#) it could US debt by \$3.3 trillion by 2034, pushing the debt-to-GDP ratio well above current levels.

Figure 3: Which Of The Following Factors Discourages You From Investing In The USD? (Share Of Respondents)



Source: OMFIF GPI 2024-25 Survey

Investor concerns over fiscal sustainability have already triggered [an exodus from US Treasuries](#), sending yields higher and weakening the dollar. The dollar selloff was further intensified by a global loss of confidence following Trump's April 2 tariff announcement, which sparked a [\\$5 trillion drop](#) in US equity values in just three days. A steady stream of reports points to shifting sentiment: [China exploring alternatives to US Treasuries](#), [Japan hinting its US bond holdings could become a bargaining chip](#), and concerns that [Asian countries may reduce their \\$7.5 trillion exposure to US assets](#). While trade tensions with China have since cooled, investor appetite for dollar assets remains subdued.

Meanwhile, gold prices have hit record highs amid central bank buying, reflecting growing fears of dollar devaluation. With Trump pushing for aggressive rate cuts, markets are now pricing in two to three Federal Reserve reductions by year-end, further narrowing the yield advantage of US assets and adding downward pressure on the currency.

Yet some perspective is needed. The dollar's current level is largely a correction from historically high valuations over the past few years (**Figure 2**). When viewed over a longer horizon, the dollar remains broadly stable against major currencies like the euro, the pound, the yen, and the renminbi. In fact, the dollar index today is not far from where it stood a decade ago, even after the latest round of tariff shocks.

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Thus, the recent weakness of dollar should be viewed not only in short-term trade tensions and more in underlying macroeconomic trends. The US economy is clearly losing momentum, and attention is now turning to the Federal Reserve. GDP shrank in Q1 2025, and while growth is expected to continue, it will likely be slower than in previous years.

This pressure is also playing out politically. Fed Chair Powell has so far resisted calls to cut rates aggressively, concerned that Trump's tariff policies could stoke inflation. But the President has publicly criticized Powell, even demanding his resignation, hoping to install a more compliant Fed chief who would slash rates quickly.

Inside the Fed, the debate is intensifying. The FOMC remains divided between those favoring higher rates to contain inflation and those advocating cuts to counteract the economic slowdown. But expectations are mounting that the Fed will lean toward easing in the months ahead. Such a move would narrow the interest rate gap between the US and other advanced economies, especially Europe and Japan, reducing the yield advantage of holding dollar-denominated assets. That, in turn, makes the dollar less attractive to global investors and helps explain why it has softened against its peers.

Global Euro Moment

This is context in which ECB President Lagarde suggested the euro could emerge as a viable global alternative to the US dollar, citing a shift in investor preferences toward regions seen as reliable security partners. "The ongoing changes create the opening for a 'global euro moment'," she said. The euro shares many of the dollar's strengths: an open capital account, deep financial markets, a robust banking system, and a central bank willing to backstop markets. What it has lacked is a pool of safe euro-denominated assets, but recent fiscal expansion, joint issuance, and shifting geopolitical dynamics may begin to close that gap. European policymakers, including Lagarde, recognize that the euro's global role must be earned through structural reforms. Lagarde emphasized that for the euro's global role to expand, Europe must pair economic openness with stronger military capabilities to reinforce its alliances.

A claim that the euro could replace the dollar may reflect more hope than reality given Europe's persistent economic stagnation. Still, a weakening dollar does not necessarily signal the end of its hegemonic role. What's more likely is gradual regional displacement, with the euro as the leading beneficiary. Replacing the dollar in trade invoicing is easier than in cross-border lending, where deep capital markets matter most. Here, China's renminbi faces limitations: despite its growing trade role, it lacks full capital account convertibility and globally accessible financial infrastructure. Still, China could build a regional lending bloc using the renminbi and digital systems shielded from US oversight—seen in Washington more as a geopolitical challenge than an economic one. Meanwhile, proposals for a BRICS currency remain symbolic; without a unified central bank, such a project lacks credibility.

Thus, the recent strength of the euro is less a sign of renewed European vitality and more a reflection of the dollar's relative decline, driven primarily by internal dynamics within the United States. Rather than a surge in confidence in the eurozone's economic fundamentals, investors are reacting to growing unease over US fiscal sustainability, erratic trade policy, and institutional uncertainty.

De-Dollarization Accelerates: How BRICS and Stablecoins Are Redrawing the Financial Map

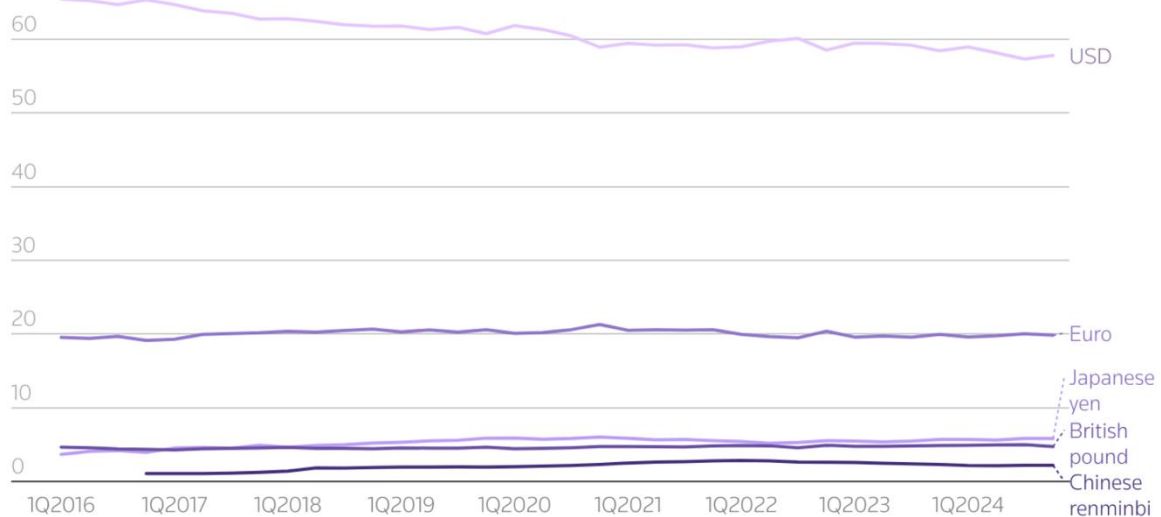
Trump's re-election already intensified de-dollarization efforts, deepening global unease over US dominance, prompting even traditional allies in Europe to question their dependence on Washington. Confronted with aggressive trade policy, unraveling security arrangements, and an increasingly weaponized dollar, both European and Global South countries are exploring ways to de-risk their economies from US financial hegemony. This includes pursuing de-dollarization strategies and building parallel institutions to enhance autonomy over trade, finance, and security. And obviously, [BRICS is leading this shift](#).

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In response, Washington is experimenting with new tools—most notably US-backed stablecoins—to reassert dollar dominance in global financial infrastructure. On June 17, the Senate passed the [GENIUS Act](#), backed by heavy crypto-sector lobbying, laying the groundwork for US-regulated dollar-based stablecoins. These digital assets, pegged to the dollar and backed by US Treasuries, aim to expand global dollar use and create “trillions” in new foreign demand for US debt helping to suppress borrowing costs, [according to crypto czar David Sacks](#).

However, as mentioned, the dollar's share of global reserves has steadily declined, now standing at 58%—its lowest level in decades—yet it remains significantly higher than the euro's 20% share (**Figure 4**).

Figure 4: Quarterly Share of Holdings of Foreign Reserves



Source: [Reuters](#)

Hence, talk of replacing the dollar is premature, especially after the GENIUS act has legalised stablecoins and they will become the centre of the new global financial architecture. As recently discussed in one of our Fin-Tech and Digital Asset primers, digital payments infrastructure are becoming a vector to extend geopolitical influence across the globe (**Figure 5**).

Euro Appreciation and the ECB's Policy Dilemma

ECB officials are increasingly concerned that the euro's rapid appreciation could cause inflation to fall below the 2% target and hurt European competitiveness. The euro has risen about 14% against the dollar this year (**Figure 6**), before the recent repricing following the US-EU trade “deal”, which was largely seen as EUR negative. At the ECB's retreat in Sintra, Vice President Luis de Guindos warned that a move beyond \$1.20 could be problematic, though manageable for now.

A stronger euro could soon justify further rate cuts due to disinflation and export weakness. [Latvian central bank chief Martins Kazaks](#) echoed this, noting that continued euro strength could tilt the ECB toward another cut, potentially bringing the deposit rate to 1.75% this year. Lithuania's Simkus emphasized the speed of

appreciation, not the level, as a key concern. Bundesbank's Joachim Nagel and Estonia's Madis Muller both downplayed the risk, noting the euro remains within historical norms. Meanwhile, Portugal's Mario Centeno highlighted the euro's rising global profile, especially in debt markets, as a positive development.

Figure 5: Payment Systems As a Vector of Geopolitics



Source: pay.uk 2024

The ECB kept the deposit rate unchanged at 2.00% on Thursday, July 24, in line with consensus and market expectations. President Lagarde reiterated a data-dependent stance and kept the door open for a possible move in September, while avoiding firm guidance due to limited incoming data.

ECB policy favours responding to enacted measures and communication has been unified, with most Governing Council members stressing that the ECB is in a "good position." Even hawkish voices like Schnabel suggest the bar for further cuts is high. The ECB has downplayed near-term inflation undershooting as long as medium-term expectations remain anchored. June minutes noted policy should become less reactive, with only large shocks warranting a response.

Figure 6: US Dollars to Euro Spot Exchange Rate



Source: FRED

The euro's sharp rise in 2025 is also squeezing European corporate earnings, with second-quarter profits expected to decline as a stronger currency and weakening demand hit sales and margins. Manufacturers are also bracing for potential tariffs, which, combined with the euro's appreciation, make EU exports less competitive.

This combination will be painful for exporters, as higher dollar prices reduce US market share. The US-EU trade deal wasn't reassuring for the EU, as it showed lack of leadership and coordination. [The EU exported over €500 billion in goods to the US last year](#), including 750,000 vehicles and 12% of Airbus planes. Rising prices could erode competitiveness, especially for firms like Volkswagen, Mercedes-Benz, and Airbus.

Conclusion

The dollar's recent decline reflects more than short-term volatility, it marks a deeper shift in the global monetary order. Triggered by Trump's tariff policies, rising fiscal risks, and political pressure on the Fed, the weakening dollar has prompted investors and governments to reconsider their reliance on US assets. While the dollar still dominates global reserves, its appeal is fading, and alternatives are gaining traction.

In this context, the euro's recent strength should not be seen in isolation, but rather as a mirror of the dollar's relative fall. Much of the euro's appreciation stems from declining confidence in US economic management, rather than a fundamental shift in European growth prospects. Thus, the euro's rise is best understood as a passive revaluation against a retreating dollar.

Amid this shift, the euro has re-emerged as a potential contender. At the ECB's Sintra conference, President Lagarde framed this as a "global euro moment," calling for deeper capital markets, stronger institutions, and military credibility to support the euro's global role. But eurozone economic stagnation and the scarcity of safe euro-denominated assets continue to limit the currency's international reach.

The ECB now faces a delicate balancing act: managing a strong euro that risks pushing inflation below target, while avoiding premature rate cuts amid tariff uncertainty and export weakness. Meanwhile, de-dollarization efforts—from BRICS coordination to central banks reducing US exposure—are accelerating. Washington's response has taken the form of financial innovation, notably dollar-backed stablecoins under the GENIUS Act, designed to create new global demand for US debt and preserve monetary primacy.

What lies ahead is not the end of the dollar's dominance, but its gradual recalibration. The euro, under the ECB's cautious but ambitious stewardship, may emerge as the leading regional alternative—but the broader system is clearly transitioning toward greater monetary multipolarity.