The Dollar Dilemma: Why Trump's Economic Policies Contain an Inherent Contradiction

An Analysis of the Fundamental Tension Between Manufacturing Revitalization and Dollar Hegemony in 2025-2026

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Executive Summary

As of January 30, 2026, the Trump administration faces a profound economic contradiction at the heart of its policy agenda. The simultaneous pursuit of manufacturing revitalization through trade rebalancing and the maintenance of dollar dominance represents not merely a challenging policy balance, but a fundamental impossibility. This paper examines why these twin goals are structurally incompatible, analyses the current policy trajectory and its market consequences, and explores the long-term implications of the administration's apparent choice to prioritize industrial revival over monetary hegemony.

The central thesis is straightforward: the mechanisms required to maintain the dollar's role as the world's primary reserve currency are the same mechanisms that hollow out American manufacturing. Conversely, the policies needed to rebuild domestic industry systematically

undermine the foundations of dollar dominance. The administration cannot have both, and current evidence suggests it has chosen manufacturing, with consequences that are already manifesting in currency markets and may soon reshape the global financial architecture.

1. The Structural Logic of the Triffin Dilemma

1.1 The Historical Foundation

The contradiction Trump faces is not new. Belgian-American economist Robert Triffin identified it in the 1960s when examining the Bretton Woods system. The "Triffin Dilemma" describes an inherent conflict: for the dollar to serve as the world's reserve currency, the United States must supply the world with dollars by running persistent current account deficits. Yet these same deficits eventually undermine confidence in the currency's value.[1]

The dilemma has only intensified since Bretton Woods collapsed in 1971. Today's dollar hegemony rests on several pillars that work in concert to maintain the currency's dominance. First, there is the requirement of liquidity provision. Foreign central banks, corporations, and investors need vast quantities of dollar-denominated assets, primarily U.S. Treasury securities, for reserves, trade settlement, and safe-haven purposes. Second, the dollar's role depends fundamentally on perceptions of U.S. political stability, rule of law, and policy predictability. Third, once established as the dominant medium of exchange, the dollar becomes self-reinforcing through powerful network effects. Oil trades in dollars because other commodities trade in dollars because debt is denominated in dollars, creating a circular reinforcement that is difficult to break.[2]

The fourth and most crucial pillar is the deficit mechanism itself. The United States supplies these dollars to the world primarily through its trade deficit. When Americans buy more foreign goods than they sell abroad, dollars flow outward, providing the global liquidity that keeps the international monetary system functioning. This is not an accident or a policy failure, but rather an essential feature of reserve currency status.[3]

1.2 The Manufacturing Reversal Requirements

Rebuilding American manufacturing requires the opposite dynamics. A weaker dollar makes U.S. exports cheaper and foreign imports more expensive, theoretically improving competitiveness and encouraging domestic production. Instead of running deficits that supply the world with dollars, manufacturing revival aims to flip the balance entirely, with the United States selling more abroad than it purchases domestically. If the trade deficit shrinks or reverses, however, the mechanism by which foreign entities acquire dollars contracts proportionally. Furthermore, the tools required to achieve this reversal, including tariffs, trade

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[1] Triffin, Robert. *Gold and the Dollar Crisis*. New Haven: Yale University Press, 1960. See also: "Triffin dilemma," Wikipedia, accessed January 2026, https://en.wikipedia.org/wiki/Triffin_dilemma

[2]]: J.P. Morgan, "De-dollarization: The end of dollar dominance?," J.P. Morgan Global Research, accessed January 2026, https://www.jpmorgan.com/insights/global-research/currencies/de-dollarization

[3] Xponance, "A Macroeconomic Perspective: Reserve Currency Status and Persistent Trade Deficits," May 21, 2025, https://www.xponance.com/a-macroeconomic-perspective-reserve-currency-status-and-persistent-trade-deficits/

threats, and bilateral negotiations, introduce precisely the kind of volatility that conflicts with the stability reserve currencies require.

The mathematical impossibility becomes clear when stated plainly: if the United States reduces its trade deficit to zero or achieves a surplus, it simultaneously eliminates the primary channel through which the world acquires the dollars it needs to maintain dollar-based systems. Global dollar liquidity would contract, forcing a fundamental reconfiguration of international monetary arrangements. This is not a matter of degree or careful policy calibration. It is a binary choice disguised as a policy menu.

2. The Twin Goals: Dollar Dominance vs. Manufacturing Revival

2.1 The Case for Maintaining Dollar Hegemony

The benefits of dollar dominance, what former French Finance Minister Valéry Giscard d'Estaing termed America's "exorbitant privilege," are substantial and many-sided. From a financial perspective, the U.S. government borrows at significantly lower interest rates because foreign central banks must hold Treasuries as reserves, regardless of their assessment of U.S. fiscal sustainability. American banks and corporations similarly access cheaper capital than their competitors, providing a persistent advantage in global markets.[4] The Federal Reserve effectively controls global liquidity conditions, as its decisions ripple through the international financial system. Perhaps most importantly in the current geopolitical climate, financial sanctions become powerful foreign policy tools when the dollar serves as the global medium of exchange.

The economic flexibility provided by reserve currency status is equally impressive. Trade deficits become sustainable indefinitely because the United States pays for imports in its own currency, a privilege no other nation enjoys to the same degree. The economy can consume beyond its production capacity without triggering the kind of currency crises that plague emerging markets. Economic downturns can be managed with monetary expansion without risking capital flight, as investors flee to dollar assets precisely when the U.S. economy weakens.

From a geopolitical perspective, control over the international payments system, particularly through mechanisms like SWIFT, enables sanctions enforcement that would be impossible without dollar dominance. This monetary hegemony reinforces American diplomatic and military reach in ways both obvious and subtle. Competitors face structural disadvantages in their own currency management, as any significant shift toward their currencies would require displacing network effects built over decades. These benefits have allowed the United States to maintain consumption levels, government spending, and military commitments that would be impossible for countries without reserve currency status.

2.2 The Case for Manufacturing Revitalization

The Trump administration's focus on rebuilding manufacturing stems from a fundamentally different calculation of costs and benefits. The persistent trade deficits that sustain dollar

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[4] Barry Eichengreen, *Exorbitant Privilege: The Rise and Fall of the Dollar and the Future of the International Monetary System* (Oxford: Oxford University Press, 2011).

dominance have coincided with devastating manufacturing job losses. Employment in the sector fell from 17.3 million in 2000 to approximately 12.7 million in December 2025, a decline of over four million jobs during a period when the overall population grew substantially[5]. Industrial capacity has eroded in strategically important sectors, from steel production to semiconductor manufacturing. Regional economic disparities have widened dramatically as manufacturing centres declined, creating geographic inequality that maps closely onto political polarization. Income inequality has increased as high-paying industrial jobs that provided middle-class security without requiring college degrees have disappeared.

From a national security perspective, these losses create vulnerabilities that extend far beyond economics. Supply chain dependencies on China for critical goods including pharmaceuticals, rare earth elements, and electronics create leverage that adversaries can exploit. The reduced domestic capacity to manufacture military equipment and components raises questions about wartime mobilization capability. The loss of technical expertise and engineering knowledge represents human capital that cannot be quickly reconstituted. Most fundamentally, vulnerability to economic coercion through trade disruption undermines strategic autonomy in ways that may not be apparent until crisis moments.

The political imperatives driving the manufacturing agenda are equally clear. Manufacturing job losses in key swing states, particularly Pennsylvania, Michigan, and Wisconsin, have direct electoral consequences that no administration can ignore. The political coalition that brought Trump to power relies heavily on voters in deindustrialized regions who feel abandoned by previous policy choices. Populist sentiment demands visible action on trade imbalances with China, regardless of whether economists consider such imbalances problematic. The administration's view holds that the current arrangement sacrifices tangible productive capacity and middle-class employment for abstract financial advantages that primarily benefit coastal elites and financial sector professionals.

2.3 Why You Cannot Maximize Both Simultaneously

The incompatibility is not merely a matter of policy difficulty or insufficient coordination. It is structural and absolute. The reserve currency role requires deficits because if the U.S. trade balance improves substantially, the supply of dollars to global markets contracts accordingly. Foreign central banks would struggle to accumulate sufficient dollar reserves for their needs. International trade and finance, which remain heavily dollarized despite recent diversification efforts, would face liquidity shortages that could trigger cascading disruptions. Alternative currencies or systems would need to fill the gap, fundamentally altering the international monetary architecture.

Manufacturing revival, conversely, requires exactly the opposite dynamic. Policies designed to boost exports and reduce imports, including tariffs, subsidies, and currency management, directly reduce the trade deficit by design. A sustained manufacturing boom would likely flip the trade balance to surplus over time. This surplus would drain dollars from the global system, as foreign entities would be paying out more dollars than they receive. The dollar's liquidity premium, a crucial component of its reserve currency status, would decline as availability decreased.

The policy tools themselves exist in fundamental conflict. Tariffs and trade restrictions alienate foreign partners whose central banks hold the dollar reserves that keep U.S.

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[5] U.S. Bureau of Labor Statistics, "All Employees, Manufacturing [MANEMP]," Federal Reserve Economic Data (FRED), St. Louis Fed, accessed January 2026, https://fred.stlouisfed.org/series/MANEMP . Data shows manufacturing employment at 12.692 million in December 2025.

borrowing costs low. Unpredictable policy reduces the dollar's safe-haven appeal, as investors prize certainty above all else when seeking safety. Pressure on the Federal Reserve to maintain lower rates to weaken the dollar and boost manufacturing conflicts directly with the stability and independence that reserve currencies require. Geopolitical tensions with trade partners undermine the foundation of trust upon which reserve currency status ultimately depends. The relationship is zero-sum at the extremes: maximizing one goal necessarily compromises the other in ways that no amount of policy skill can overcome.

3. Current Policy Direction: The Evidence for Choosing Manufacturing

3.1. The Tariff Strategy

The administration's tariff policies reveal with unusual clarity where its priorities lie. As of January 2026, the United States has implemented comprehensive tariffs on Chinese imports ranging from 25% to over 145% on specific categories[6]. The "reciprocal tariff" framework targets countries with large bilateral surpluses with the United States, while threats of automotive tariffs on Mexican and Canadian imports remain a persistent feature of the trade policy landscape. Most significantly, the universal 10% baseline tariff implemented on "Liberation Day" on April 2, 2025, marked a fundamental shift away from the selective protectionism of previous administrations toward a comprehensive trade policy reorientation[7].

Currency markets have responded to these policies with notable dollar weakness. The dollar index fell approximately 11% in the first half of 2025, the biggest decline in more than 50 years[8]. This decline reflects market expectations that tariffs will reduce the trade deficit over time, either through reduced imports, increased exports, or both. Bond markets show increasing foreign hesitation about long-term Treasury holdings. Foreign ownership of Treasuries has fallen to 30% as of early 2025, down from over 50% during the Global Financial Crisis, a trend that accelerated following the Liberation Day announcement[9]. Equity markets have similarly discounted potential retaliation effects. The S&P 500 fell over 274 points or 4.88% on Liberation Day itself, the second largest daily point loss ever, suggesting deep uncertainty about the economic consequences of the new trade regime[10].

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[6] CNBC, Bao, and Anniek, “China Strikes Back with 125% Tariffs on U.S. Goods as Trade War Intensifies,” *CNBC*, April 11, 2025, "China strikes back with 125% tariffs on U.S. goods as trade war intensifies"

[7] Aimee Picchi, “Trump Reveals These 2 New Types of Tariffs on What He Calls ‘Liberation Day,’” CBS News, updated April 2, 2025, https://www.cbsnews.com/news/liberation-day-trump-tariffs-explained/

[8] Morgan Stanley, "Devaluation of the U.S. Dollar 2025," Morgan Stanley Insights, accessed January 2026, https://www.morganstanley.com/insights/articles/us-dollar-declines. States: "The dollar index, which measures the greenback against a basket of currencies of the U.S.'s major trading partners, fell about 11% from January through the end of June."

[9] JPMorgan Global Research, “De-dollarization: Is the U.S. Dollar Losing Its Dominance?” JPMorgan, July 1, 2025, https://www.jpmorgan.com/insights/global-research/currencies/de-dollarization

[10] Sean Conlon, “Small-Cap Benchmark Russell 2000 Becomes First Major U.S. Stock Measure to Enter Bear Market,” CNBC, published April 3, 2025, updated April 6, 2025, https://www.cnbc.com/2025/04/03/small-cap-benchmark-russell-2000-becomes-first-major-us-stock-measure-to-enter-bear-market.html

The tariff strategy is inherently inconsistent with maintaining dollar dominance. By design, tariffs aim to reduce imports and encourage domestic production, which is the exact opposite of the trade deficit mechanism that supplies global dollar demand. The administration appears to understand this trade-off at some level, even if it refuses to acknowledge it publicly, as evidenced by the lack of concern about dollar weakness in official communications.

3.2 Federal Reserve Pressure and Currency Management

The administration has shown unprecedented willingness to challenge Federal Reserve independence, a cornerstone of dollar credibility. Repeated criticism of Fed Chair Jerome Powell for maintaining "too high" interest rates has become a regular feature of the President's public commentary. Suggestions that the President should have greater influence over monetary policy, while not pursued through formal legal changes, create uncertainty about the future institutional framework. Framing rate decisions as harming manufacturing competitiveness represents a fundamental shift from the traditional view that Fed independence serves long-term economic stability[11].

The implicit currency management embedded in this rhetoric aims to weaken the dollar without the formal intervention that would trigger international condemnation and potential retaliation. This represents a significant shift from the traditional "strong dollar policy" mantra that every administration from Clinton through Trump's first term had maintained, at least rhetorically. Markets interpret this shift as acceptance of, or even preference for, dollar depreciation to boost manufacturing competitiveness. These approaches directly conflict with the policy predictability and central bank independence that underpin reserve currency confidence in global markets.

3.3 The "Strategic Competition" Framework

National security arguments have become increasingly central to trade policy justification, providing political cover for protectionist measures that might otherwise face stronger domestic opposition. The administration has pursued aggressive decoupling from China through restrictions on technology exports and investment, pressure on allies to reduce Chinese supply chain dependence, and industrial policy incentives for domestic production in strategic sectors. These measures go far beyond traditional trade policy and represent a comprehensive attempt to restructure global economic relationships.

Friend-shoring initiatives attempt to redirect supply chains to allied countries, though this still reduces the U.S. bilateral deficit with China even if overall deficits persist with other partners. More fundamentally, the fragmentation of global trade reduces the dollar's role as the universal medium of exchange. When trade becomes regionalized and politicized, the case for a single global currency weakens accordingly. Industrial policy measures including CHIPS Act implementation directing semiconductor production to U.S. facilities, clean energy manufacturing incentives despite the administration's general scepticism of climate policy, and infrastructure spending directed preferentially toward domestic suppliers all point in the same direction. These policies explicitly prioritize supply chain resilience and domestic capacity over the open-market system that reinforces dollar dominance through network effects and mutual interdependence.

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[11] J.P. Morgan Asset Management, "Where is the U.S. dollar headed in 2025?," accessed January 2026, https://am.jpmorgan.com/us/en/asset-management/adv/insights/market-insights/market-updates/on-the-minds-of-investors/where-is-the-us-dollar-headed-in-2025/ . Notes: "Comments about Fed Chair Powell's potential dismissal on July 16th led to a 1.2% drop in the dollar within an hour."

4. Market Response: The Dollar's Decline as Referendum on Policy Coherence

4.1 Currency Market Dynamics (Late 2024 - January 2026)

The dollar's trajectory provides the most direct evidence of how markets assess the administration's policy coherence and likely future direction. The DXY Dollar Index fell approximately 11% in the first half of 2025, the worst performance for that period in over 50 years, a decline that accelerated following specific policy announcements[12]. The dollar showed particular weakness against currencies of countries less exposed to U.S. trade tensions, while maintaining relative strength only against currencies of countries facing similar policy uncertainty. Morgan Stanley Research estimated in mid-2025 that the dollar could lose another 10% by the end of 2026, suggesting that markets view the decline as structural rather than cyclical[13].

The qualitative factors driving this weakness extend beyond simple trade balance arithmetic. Policy unpredictability has reduced the dollar's safe-haven appeal at precisely the moment when global uncertainty should be driving investors toward dollar assets. Concerns about the long-term trajectory of the U.S. trade balance reflect recognition that current policies, if sustained, will fundamentally alter America's role in global commerce. Questions about Federal Reserve independence have introduced a new source of uncertainty that did not exist in previous periods of dollar weakness. Geopolitical tensions with traditional allies, including threats over Greenland that led to tariff threats against European nations, undermine the alliance structures that have supported dollar dominance since Bretton Woods[14].

The contradiction has been made visible through market pricing in ways that no amount of official rhetoric can obscure. The administration claims to support a "strong dollar" when pressed on the issue, yet its policies systematically undermine every foundation of dollar strength. Markets resolve this contradiction by pricing in a weaker dollar trajectory, which then becomes self-fulfilling as positioning adjusts accordingly. Currency traders, institutional investors, and foreign central banks are all making decisions based on their assessment of policy direction rather than policy statements, and those decisions uniformly point toward reduced dollar dominance.

4.2 Treasury Market Signals

Foreign holdings of U.S. Treasuries provide a second crucial indicator of shifting confidence in dollar assets and American policy stability. Several major foreign central banks have reduced Treasury holdings in absolute terms, not merely slowing the pace of accumulation but actively selling existing positions. New purchases have slowed dramatically relative to global reserve accumulation rates, meaning that even central banks still buying Treasuries

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[12] Morgan Stanley Research, “The Depreciation of the Dollar,” Morgan Stanley, August 6, 2025, https://www.morganstanley.com/insights/articles/us-dollar-declines

[13] Bloomberg/Yahoo Finance, "Dollar Faces Pressure on Trump's New European Tariff Threats," January 18, 2026, https://finance.yahoo.com/news/dollar-faces-pressure-trump-fresh-041743074.html

[14] Nellie Liang, “What’s Going on in the U.S. Treasury Market, and Why Does It Matter?” *Brookings*, April 14, 2025, https://www.brookings.edu/articles/whats-going-on-in-the-us-treasury-market-and-why-does-it-matter/

are allocating smaller shares of new reserves to dollar assets. Auction demand from foreign buyers shows deterioration at the margin, with primary dealers having to absorb larger shares of new issuance. Foreign share of total Treasury ownership has fallen to 30% as of early 2025, down from over 50% during the Global Financial Crisis, a decline that has accelerated notably since 2023[15]. Term premiums have increased correspondingly, suggesting that investors require higher compensation for the duration risk associated with long-term Treasury holdings.

The causation question becomes crucial when interpreting these trends. Is reduced foreign demand causing policy shifts toward manufacturing protectionism, or are policy shifts causing reduced foreign demand for Treasuries? The evidence suggests the latter, with policy driving demand reduction rather than the reverse. Alternative reserve assets including gold and non-dollar bonds have seen increased allocation even from allied central banks that might be expected to maintain dollar positions for geopolitical reasons. Even traditional American allies appear to be diversifying away from exclusive dollar concentration, suggesting that the trend reflects fundamental concerns about U.S. policy direction rather than opportunistic portfolio management.

4.3 The Confidence Mechanism

Reserve currency status ultimately rests on confidence, which operates across multiple dimensions that must all remain intact for the system to function properly. Economic confidence requires belief that the U.S. economy will remain productive and solvent over the relevant time horizon, trust that inflation will remain controlled within acceptable bounds, and expectation of reasonable long-term growth that justifies holding dollar assets. Political confidence demands certainty about property rights and rule of law, predictability of policy direction that allows for long-term planning, and stability of governing institutions that transcends individual administrations or political personalities. Financial confidence requires deep and liquid markets for dollar assets, transparent pricing and fair access for all participants, and limited risk of arbitrary government intervention that could expropriate value.

Current policies strain all three dimensions simultaneously in ways that are historically unusual. Tariff unpredictability undermines economic confidence by making it impossible to forecast trade flows, production costs, or competitive dynamics with any certainty. Attacks on Federal Reserve independence undermine political confidence by suggesting that monetary policy could become subordinated to short-term political considerations. Threats to freeze or seize assets in geopolitical disputes, while targeted at specific adversaries, undermine financial confidence more broadly by demonstrating that property rights in dollar assets may be contingent rather than absolute.

[15] Nellie Liang, “What’s Going on in the U.S. Treasury Market, and Why Does It Matter?” *Brookings*, April 14, 2025, https://www.brookings.edu/articles/whats-going-on-in-the-us-treasury-market-and-why-does-it-matter/

5. The Long-Term Scenarios: What Happens When You Choose Manufacturing?

5.1 The Optimistic Manufacturing Revival Scenario

In the most favourable scenario, the administration's tariff and industrial policies successfully incentivize substantial domestic production increases. Manufacturing employment could increase by 2-3 million jobs over a decade, concentrated in politically crucial regions and strategically important sectors. The trade deficit might narrow from its 2024 level of approximately $918 billion to perhaps $300 billion annually as imports fall and exports rise[16]. Supply chain resilience would improve meaningfully in strategic sectors including semiconductors, pharmaceuticals, and rare earth processing, reducing vulnerability to foreign coercion.

The dollar implications of this scenario would be significant but manageable if the transition occurs gradually. The dollar's share of global reserves would likely decline from current levels around 58% to perhaps 45-50% over a decade or more[17]. Higher borrowing costs for the U.S. government, perhaps 100-150 basis points over current levels, would increase fiscal pressure but remain sustainable with appropriate adjustments. The financial sector would shrink relative to GDP as manufacturing and other tradable goods sectors expanded, representing a fundamental rebalancing of the American economy. Increased inflation pressure from reduced import competition and higher domestic production costs would require careful monetary policy management to prevent a wage-price spiral.

The net assessment in this scenario involves clear trade-offs rather than unambiguous gains. Manufacturing regions would see economic revival and population stabilization, reversing decades of decline and providing visible political benefits. The federal budget would face pressure from higher interest costs, requiring difficult choices about spending priorities or revenue increases. The financial services sector would likely shrink relative to GDP, affecting employment in New York and other financial centres. Overall economic growth might be lower than under the previous regime, but more evenly distributed geographically and across income levels. National security vulnerabilities in supply chains would be genuinely reduced, providing strategic benefits that are difficult to quantify but potentially substantial. This scenario assumes policies work roughly as intended without triggering broader systemic crisis, which represents an optimistic but not impossible outcome.

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[16] Alessandro Bellocchi and Giuseppe Travaglini, “The Trade Deficit Delusion: Why Tariffs Will Not Make America Great Again,” *Intereconomics* 60, no. 4 (July/August 2025): https://www.intereconomics.eu/pdf-download/year/2025/number/4/article/the-trade-deficit-delusion-why-tariffs-will-not-make-america-great-again.html | U.S. Bureau of Economic Analysis, "U.S. International Trade in Goods and Services, December and Annual 2024," February 5, 2025, https://www.bea.gov/news/2025/us-international-trade-goods-and-services-december-and-annual-2024 States: "For 2024, the goods and services deficit was $918.4 billion."

[17]]: EBC Financial Group, "Is the US Dollar in Trouble in 2026?," December 22, 2025, https://www.ebc.com/forex/is-the-us-dollar-in-trouble-in-2026-what-to-watch Cites "IMF COFER statistics show that the dollar remains the leading reserve currency in Q3 2025, comprising 56.92%."

5.2 The Disorderly Transition Scenario

The disorderly transition scenario begins with triggering events that could include rapid foreign selling of Treasuries in response to a specific policy shock, an unexpected spike in inflation from tariff pass-through effects, a retaliation spiral that disrupts global trade more severely than anticipated, or a loss of confidence triggering capital flight from dollar assets more broadly. Goldman Sachs estimated that tariffs caused inflation to increase by half a percentage point in 2025, suggesting that inflation risks are not merely theoretical[18].

Cascading effects would follow quickly in this scenario. Sharp dollar depreciation of 20-30% or more would make imports dramatically more expensive while providing less export benefit than hoped if foreign markets retaliate. Interest rate spikes as foreign financing withdraws would choke off business investment and consumer spending simultaneously. Severe recession would follow as borrowing costs surge and uncertainty paralyzes decision-making. A potential financial crisis could emerge if institutions are caught with mismatched positions or insufficient liquidity. The Federal Reserve would be forced into crisis management mode, possibly having to reverse course on policies designed to support manufacturing, creating policy whiplash that further undermines confidence.

The long-term outcomes of this scenario would be severe and lasting. An accelerated shift toward a multipolar currency system would leave the dollar as one among several major currencies rather than the dominant reserve asset. Permanently higher U.S. borrowing costs would constrain fiscal policy for decades. Reduced American geopolitical influence would follow as the financial sanctions regime loses effectiveness. Whatever benefits to manufacturing might eventually emerge would occur only after a painful adjustment period that could last years. The risk of political instability from economic dislocation could undermine American democracy itself, as populations under economic stress become susceptible to extremist appeals. This scenario represents the danger of pursuing contradictory goals without acknowledging trade-offs or managing the transition carefully.

5.3 The Muddle-Through Scenario (Most Likely)

The most likely scenario involves partial achievement of both manufacturing and dollar dominance goals, with neither complete success nor catastrophic failure. This middle path would be characterized by modest job gains in targeted manufacturing sectors, gradual erosion of dollar dominance through central bank diversification, ongoing policy tensions and market volatility, and a general sense of managing decline rather than achieving breakthrough.

The dollar trajectory in this scenario would involve continued slow decline in reserve currency share to approximately 50% over 10-15 years from the current level around 58%. Modestly higher borrowing costs of 50-75 basis points would be absorbed through a combination of higher taxes, slower spending growth, and acceptance of larger deficits. Increased use of alternative settlement mechanisms including bilateral currency swaps and potentially digital currencies would chip away at dollar dominance at the margins without displacing it entirely. The dollar would remain dominant in global finance but no longer overwhelming, representing a significant but not catastrophic erosion of American privilege.

Manufacturing outcomes would similarly be mixed. Some reshoring would occur in politically sensitive sectors where subsidies or tariffs make domestic production viable. The overall

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[18] CNN Business, "Tariffs could really sting in 2026," January 3, 2026, https://www.cnn.com/2026/01/03/business/tariffs-prices-2026 Reports: "Goldman Sachs economists estimated that tariffs caused inflation to increase by half a percentage point in 2025."

trade deficit would remain substantial but its composition would shift, with fewer consumer goods from China offset by more capital goods from elsewhere. Job gains would be concentrated in specific regions and industries, providing political benefits without fundamentally transforming the national employment picture. Continued automation would limit employment impact even in successfully reshored industries, as modern manufacturing requires far fewer workers per unit of output than mid-20th century production.

The net result would preserve significant but reduced American financial privilege while achieving manufacturing revival insufficient to offset overall employment trends. Policies would satisfy key political constituencies without fundamentally reshaping the economy. The long-term relative decline that has characterized the 21st century would continue but at a manageable pace that avoids crisis while failing to reverse underlying trajectories. This scenario assumes ongoing policy adjustments that prevent worst-case outcomes while achieving partial goals, which represents the historical norm for complex policy challenges.

6. The International System Response: How the World Adjusts

6.1 Central Bank Diversification Strategies

Foreign central banks face their own strategic dilemma as U.S. policy direction becomes clearer. The existing alternatives to the dollar each carry significant limitations that prevent immediate large-scale substitution. The euro, representing approximately 20% of global reserves, offers deep and liquid markets but the Eurozone's lack of fiscal union and ongoing fragmentation risks make it a problematic alternative for full reserve diversification[19]. The Chinese yuan is growing in importance but remains subject to capital controls and is politically unreliable for non-aligned countries that fear economic coercion from Beijing. Gold provides the ultimate hedge without counterparty risk but offers no yield and has limited utility for international transactions. The share of gold in global foreign exchange reserves has increased to around 20%, with emerging markets increasing holdings from 4% to 9% over the past decade[20]. Special Drawing Rights represent a theoretical solution but lack the market depth and transaction infrastructure to serve as a practical alternative at scale.

The observed trends in central bank behaviour point toward gradual diversification without full abandonment of the dollar. Increased gold purchases by emerging market central banks, with China, Russia, and Turkey as the largest buyers in the last decade, represent the most visible aspect of this shift[21]. Growth in bilateral currency swap arrangements between countries seeking to reduce dollar dependence allows for trade settlement without dollar intermediation. Regional payment systems including China's CIPS and Russia's SPFS

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[19] Wolf Street, "Status of the US Dollar as Global Reserve Currency: USD Share Drops to Lowest since 1994," December 26, 2025, https://wolfstreet.com/2025/12/26/status-of-the-us-dollar-as-global-reserve-currency-usd-share-drops-to-lowest-since-1994/

[20] Jamie McGeever, "Gold's Rise in Central Bank Reserves Appears Unstoppable," *Reuters*, September 4, 2025, https://www.reuters.com/markets/commodities/golds-rise-central-bank-reserves-appears-unstoppable-2025-09-04/

[21] Muflih Hidayat, "Central Bank Gold Accumulation Drives Strategic Dollar Diversification," *Discovery Alert*, January 30, 2026, https://discoveryalert.com.au/dollar-gold-shift-2026-institutional-capital-risk/

provide infrastructure for dollar-independent transactions, though their scope remains limited. Central bank exploration of cryptocurrencies and central bank digital currencies continues, though implementation remains in early stages and faces substantial technical and political obstacles.

The fundamental challenge facing central banks is that no single alternative can immediately replace dollar dominance. Transition costs are high, requiring substantial investment in new market infrastructure and institutional changes. Network effects favour the incumbent dollar system, as each participant's benefit from using the dollar increases with the number of other participants using it. Historical experience suggests that shifts in reserve currency dominance occur gradually over decades, then suddenly when confidence thresholds are crossed and network effects begin working in reverse.

6.2 China's Strategic Positioning

China benefits from U.S. policy contradictions in ways that extend far beyond simple economic advantage. Yuan internationalization efforts have accelerated with Belt and Road infrastructure deals increasingly denominated in yuan, commodity purchases from Russia and Saudi Arabia using yuan settlement, development of CIPS as an alternative to SWIFT for international payments, and gradual capital account liberalization undertaken in a controlled manner that minimizes disruption risks. These efforts proceed independently of U.S. policy choices but are accelerated by American actions that undermine dollar credibility.

China's strategic approach demonstrates patience rather than urgency. Chinese policymakers understand that they need not actively displace the dollar when U.S. policies accomplish that task without Chinese intervention. Building alternative infrastructure while maintaining substantial dollar exposure for now allows China to benefit from both systems during the transition period. Positioning the yuan as a regional currency first, with global alternative status as a longer-term aspiration, avoids premature challenges to dollar dominance that might unite opposition. Using trade leverage to encourage yuan adoption by partners creates incentives for gradual shift without forcing binary choices that might backfire politically.

The timeline for yuan emergence as a true alternative to the dollar remains extended despite recent progress. The yuan is unlikely to challenge dollar dominance in the next 5-10 years given capital controls, political concerns, and limited market depth. By 2040-2050, however, the yuan could represent 20-25% of global reserves if current trends continue and China maintains economic growth and political stability. Acceleration of this timeline is possible if U.S. policy creates specific openings through sanctions overuse that drives countries to seek alternatives or a Treasury market crisis that undermines confidence in dollar safety[22].

6.3 European Union Calculations

Europe faces perhaps the most complex set of choices as Atlantic alliance strains intersect with European aspirations for strategic autonomy. European interests are genuinely divided. The continent benefits from the dollar system through cheap energy imports priced in dollars and access to deep, liquid Treasury markets for reserve management. Simultaneously, Europe suffers from dollar dominance through monetary policy that remains constrained by Federal Reserve decisions and vulnerability to American sanctions that can be imposed extraterritorially. European leaders increasingly speak of "strategic autonomy" but lack the

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[22] Rory Jones, “Fed Turmoil Is Threatening Dollar Supremacy Just as China Pushes the Yuan,” *Wall Street Journal*, January 17, 2026, https://www.wsj.com/finance/currencies/fed-turmoil-is-threatening-dollar-supremacy-just-as-china-pushes-the-yuan-3ebb781d

hard power and political unity to achieve meaningful independence from American hegemony. Internal divisions between Atlanticist members like Poland and the Baltic states versus more multipolar countries like France and increasingly Germany prevent unified strategy development.

Possible European trajectories include continued euro development with parallel dollar usage representing evolutionary status quo, accelerated push for euro-denominated energy and commodity markets that would represent genuine challenge to dollar dominance, development of European payment infrastructure independent of U.S. oversight to avoid sanctions vulnerability, and increased bilateral arrangements with China that bypass dollar settlement in specific sectors or transactions. European fragmentation limits the euro's appeal as a comprehensive dollar alternative, however. Banking union and fiscal integration remain incomplete despite decades of discussion. Political divisions prevent the kind of unified strategy that would be necessary to mount a serious challenge to dollar hegemony. Most fundamentally, reliance on the U.S. security guarantee, renewed in salience by Russian aggression in Ukraine, complicates any economic decoupling that might otherwise be attractive.

7. Domestic Political Economy: Why the Contradiction Persists

7.1 The Coalition Politics of Trade Policy

Understanding why contradictory policies persist requires examining the political incentives facing decision-makers rather than assuming irrationality or ignorance. The manufacturing coalition is geographically concentrated in electorally critical states including Pennsylvania, Michigan, and Wisconsin, where visible factory closures create emotionally resonant narratives of abandonment and decline. Manufacturing job losses are not abstract statistics to these communities but rather the lived experience of families and towns. Nostalgia for mid-20th century manufacturing prosperity, when a high school graduate could support a family with a factory job, remains powerful despite changed economic circumstances. Suspicion of the "coastal elite" financial sector runs deep in these communities, which see Wall Street as having profited from globalization while Main Street suffered. The value placed on tangible production over abstract financial services reflects both cultural preferences and genuine concern about economic resilience.

The dollar dominance coalition presents a mirror image. Geographic concentration in financial centres like New York and the broader California economy means limited electoral weight in the presidential swing states that decide elections. The benefits of dollar dominance remain diffuse across the economy, with lower interest rates helping everyone but in ways that are invisible to most citizens. The coalition is less politically organized and mobilized because its benefits are received passively rather than requiring active political engagement. Association with "globalist" perspectives that are politically unpopular in key swing states further weakens political effectiveness. Most problematically, it is genuinely harder to generate political intensity around preserving an existing advantage that most people do not consciously recognize than around reversing visible job losses in specific communities.

The asymmetry in political salience drives policy choices in predictable directions. Manufacturing job losses are visible and attributable, with closed factories serving as monuments to perceived policy failures. Dollar dominance benefits are invisible and distributed, with slightly lower interest rates across the entire economy producing no comparable visual symbol. The political reward structure inevitably favours visible action on visible problems, regardless of whether that action addresses underlying causes or merely provides symbolic satisfaction. Long-term systemic consequences of policy choices simply do not register in electoral timeframes measured in two or four-year increments.

7.2 The Knowledge Problem

Policymakers face genuine analytical challenges that extend beyond political considerations. The relationship between policy interventions and economic outcomes is genuinely complex and contested among experts. Economic models disagree fundamentally about the magnitudes and timing of effects from tariff changes, currency movements, and fiscal policy shifts. Historical analogies have limited applicability to current circumstances because the global economy has changed in fundamental ways. Feedback loops and international responses are genuinely difficult to predict, as other countries' reactions to U.S. policy changes depend on their own domestic political considerations and strategic calculations.

Competing expert narratives provide ammunition for all sides but clarity for none. Mainstream economists generally warn about dollar decline and fiscal costs, emphasizing the risks of disrupting the existing system. Heterodox economists argue that manufacturing decline imposes hidden costs that conventional analysis ignores, including regional inequality, political radicalization, and national security vulnerabilities. Political advisors naturally emphasize electoral considerations and constituency management. National security professionals prioritize supply chain resilience and strategic autonomy often without full consideration of economic costs. No clear mechanism exists to adjudicate between these expert disagreements in ways that would compel consensus.

The decision-making bind becomes acute when combining these analytical challenges with political incentives. Political incentives favour acting on visible problems even when optimal policy remains unclear. Bureaucratic incentives favour risk-aversion and status quo maintenance, which conflicts with demands for dramatic policy change. Yet the status quo itself appears untenable to key constituencies whose support is essential for political survival. This combination produces motivated reasoning in which administration officials selectively credit analyses that support preferred policies while dismissing warnings about dollar decline as "alarmist" or ideologically motivated. The tendency to overestimate the ability to achieve contradictory goals through superior policy skill is common to all administrations but particularly pronounced when facing structural contradictions that admit no clean resolution. The assumption that problems will prove manageable when they materialize reflects both optimism bias and the reality that current decision-makers will not be held accountable for long-term consequences.

7.3 The Time Horizon Mismatch

Political and economic timescales differ in fundamental ways that make rational long-term planning structurally difficult in democratic systems. Electoral cycles of 2-4 years create overwhelming pressure for visible results within the current term. Media cycles measured in days or weeks reward immediate action and punish deliberation. Coalition maintenance requires ongoing delivery to key constituencies rather than promises of future benefits. Long-term consequences that extend beyond the electoral horizon are heavily discounted because they will be someone else's problem, whether that someone is a successor in the same party or an opposition party that can be blamed for failing to manage the inherited situation properly.

Economic timescales operate according to different logic entirely. Reserve currency transitions historically occur over periods measured in decades, with the sterling-to-dollar transition spanning roughly 1914 to 1971. Manufacturing ecosystems take years to rebuild even with aggressive policy support, as workforce development, supplier networks, and technical knowledge cannot be created quickly. Supply chain restructuring requires sustained investment over periods that extend well beyond single electoral cycles. Confidence shifts in financial markets can be slow and gradual, then sudden and catastrophic when thresholds are crossed, making them particularly difficult to manage politically.

The inevitable result is that policies are chosen based on short-term political benefits without adequate weight given to long-term systemic consequences. The assumption that future administrations will deal with resulting problems is not cynical but rather realistic about political constraints. The possibility of triggering irreversible changes receives inadequate consideration because the relevant timeframes extend beyond political planning horizons. This is not a failure of particular individuals or administrations but rather a structural feature of democratic governance that becomes particularly problematic when facing challenges that require sustained policy consistency over decades.

8. The Intellectual Landscape: Theoretical Frameworks for Understanding the Choice

8.1 The Nationalist-Globalist Divide

Much contemporary analysis frames the trade policy debate in starkly ideological terms that may obscure more than they illuminate. The nationalist perspective prioritizes national sovereignty and domestic economic control, viewing trade deficits as evidence of exploitation by trading partners or poor negotiation by previous administrations. This worldview emphasizes tangible production capacity over financial abstraction, arguing that a country that does not make things cannot be truly independent or secure. Nationalists express willingness to sacrifice the "exorbitant privilege" of reserve currency status for manufacturing revival and are generally sceptical of international institutions and commitments that constrain domestic policy autonomy.

The globalist perspective offers a mirror image. It emphasizes the benefits of international economic integration and specialization according to comparative advantage. Globalists view trade deficits as natural outcomes of capital flows and saving-investment imbalances rather than evidence of policy failure. They value dollar dominance as a crucial source of geopolitical power that amplifies American influence. Fears that manufacturing protectionism reduces overall economic efficiency and living standards lead globalists to oppose most forms of trade restriction. Support for rules-based international order reflects both principled commitment and recognition that American power is magnified through institutions.

The limitation of this ideological framing is that it obscures genuine trade-offs and structural constraints that exist regardless of values or preferences. By encouraging ideological posturing rather than analytical clarity, it prevents serious examination of costs and benefits.

The assumption that the problem is solvable through correct values rather than acknowledging fundamental impossibility leads to unrealistic policy promises. Most problematically, it prevents serious discussion of which goal should be prioritized and why, treating the question as one of ideology rather than strategy.

8.2 The Hegemonic Stability Theory Lens

International relations theory provides an alternative analytical framework through hegemonic stability theory[23]. The classical formulation holds that dominant powers provide public goods including reserve currency functions, open markets, and security guarantees that enable system stability. These public goods benefit all participants but impose costs disproportionately on the hegemon. Over time, these costs erode the hegemon's relative power through both direct resource drain and the strengthening of other countries that benefit from the system. Eventually either a new hegemon emerges to provide public goods and enforce system rules, or the system fragments into regional or ideological blocs without overarching authority.

Current application of this framework suggests that U.S. provision of dollar liquidity represents a classic hegemonic public good. The trade deficit represents the cost of providing this good to the international system. Manufacturing erosion is a direct consequence of bearing this cost over extended periods. The current administration's questioning of whether to continue bearing this cost represents a potential inflection point in hegemonic stability. Possible trajectories include managed hegemonic decline with gradual transition to a multipolar currency system, reassertion of hegemony through prioritizing dollar dominance while accepting continued manufacturing decline, abrupt hegemonic collapse from policy mistakes that trigger disorderly transition, or emergence of a new hegemon in a China-cantered system, though this remains premature given China's own structural challenges and limited global appeal.

8.3 The Modern Monetary Theory Challenge

Heterodox economists associated with Modern Monetary Theory contest the conventional wisdom underlying much analysis of these questions. The MMT perspective holds that sovereign currency issuers like the United States cannot "run out of money" in any meaningful sense and therefore face different constraints than commonly assumed. Trade deficits are not inherently problematic provided the economy maintains full employment and productive capacity utilization. Manufacturing decline reflects policy choices rather than inevitable economic laws, and can be reversed through appropriate government coordination of industrial policy with monetary policy[24].

The MMT critique of dollar dominance argues that "exorbitant privilege" primarily benefits the financial sector rather than ordinary Americans. Trade deficits cause persistent unemployment in manufacturing regions and contribute to widening regional inequality. Manufacturing capacity has genuine value for national security and economic resilience that

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[23] Ahmad, Mohammad & Taiye Samuel, Abejide & Oladimeji, Talibu. (2023). A BRIDGE-THEORY OF INTERNATIONAL RELATIONS: HEGEMONIC STABILITY THEORY REVISITED. SSRN Electronic Journal. 1. 2992-4618. 10.2139/ssrn.4890622 (PDF) A BRIDGE-THEORY OF INTERNATIONAL RELATIONS: HEGEMONIC STABILITY THEORY REVISITED

[24] Françoise Drumetz and Christian Pfister, "Modern Monetary Theory: A Wrong Compass for Decision-Making," *Intereconomics* 56, no. 6 (2021): 355–361, https://www.intereconomics.eu/contents/year/2021/number/6/article/modern-monetary-theory-a-wrong-compass-for-decision-making.html

is not captured in conventional economic analysis. The current system is fundamentally unsustainable and should be deliberately restructured rather than defended as optimal[25].

The conventional rebuttal to MMT emphasizes that inflation constraints are real and binding even for sovereign currency issuers. Confidence dynamics essential to reserve currency status cannot be dismissed or assumed away. Government capacity for effective industrial planning is persistently overestimated by MMT advocates who ignore public choice problems and information limitations. Real benefits of dollar dominance for ordinary Americans through lower interest rates and cheaper imports are dismissed too readily as merely benefiting "elites."

The value of this theoretical debate lies less in resolving which view is correct than in highlighting that apparent "contradictions" often reflect normative choices about priorities rather than objective economic constraints. The debate questions whether conventional wisdom adequately accounts for hidden costs of the current system. It forces clarification of what outcomes are most valued, whether those are financial dominance, manufacturing employment, regional equality, or national security. Perhaps most importantly, it reveals that supposedly immutable "economic laws" sometimes reflect political arrangements that can be changed, though not without cost[26].

9. Historical Analogies: Britain's Sterling Dilemma

9.1 The Interwar Sterling Crisis

Britain's experience with sterling in the 1920s and 1930s provides the closest historical parallel to America's current dilemma, though important differences limit direct comparison. Following World War I, sterling remained the dominant global reserve currency despite Britain's weakened economic position. British industrial competitiveness had declined substantially relative to the United States and Germany. Maintaining the gold standard at pre-war parity required high interest rates to prevent gold outflows. These high interest rates damaged domestic manufacturing and employment, creating a policy bind similar to what the United States faces today.

Winston Churchill's decision in 1925 as Chancellor of the Exchequer to return to the gold standard at pre-war parity prioritized financial prestige over domestic economic relief. The result was chronic deflation, mass unemployment particularly in industrial regions, and accelerating industrial decline. Britain was eventually forced off gold in the 1931 crisis when market pressure became unsustainable. The lesson is that attempting to maintain reserve currency status while the underlying economy deteriorates can delay but not prevent ultimate decline. Defending financial prestige can actually worsen underlying economic problems by preventing necessary adjustments. Crisis often forces choices that gradual adjustment might have managed more successfully. Reserve currency transitions, while wrenching, are ultimately survivable and may be preferable to prolonged stagnation.

Important differences limit this analogy, however. Britain was clearly in relative decline vis-à-vis the rising United States, while America's relative position remains stronger despite challenges. The United States retains fundamental economic strengths including technological innovation, favourable demographics, and abundant natural resources. The

[25] Ibid.
[26] Ibid.

dollar has no clear successor comparable to how the dollar displaced sterling, with alternatives fragmented among euro, yuan, and others. American military dominance far exceeds Britain's interwar position, potentially allowing the United States to sustain reserve currency status longer than economic fundamentals alone might support.

9.2 The 1971 Nixon Shock

The United States has previously chosen manufacturing interests over international monetary commitments with results that provide instructive precedent. The Bretton Woods system established in 1944 required dollar convertibility to gold at thirty-five dollars per ounce. By the late 1960s, the U.S. trade position was deteriorating and gold reserves declining as foreign central banks increasingly demanded conversion. Maintaining gold convertibility required deflationary policies that threatened domestic manufacturing employment during a period of significant labour unrest[27].

President Nixon's decision on August 15, 1971, to suspend gold convertibility unilaterally, impose a 10% import surcharge, and implement wage and price controls prioritized domestic political considerations over international monetary obligations[28]. The immediate result was chaos and international condemnation from allies who felt blindsided. The dollar declined approximately 25% over subsequent years as the Bretton Woods fixed exchange rate system collapsed entirely by March 1973[29]. However, the dollar retained reserve currency status even without gold backing, demonstrating that reserve currency dominance can survive significant policy shifts. The United States gained monetary policy flexibility, and manufacturing received temporary relief from import competition.

The relevance to current circumstances is both encouraging and cautionary. The 1971 precedent demonstrates that the United States can alter international monetary arrangements unilaterally when domestic pressures become sufficiently intense. Dollar dominance survived a previous crisis of confidence, suggesting resilience. However, circumstances differ fundamentally from 1971 in ways that limit the applicability of that precedent. No credible alternative to the dollar existed in 1971, whereas today multiple alternatives are emerging including the euro, yuan, and potentially digital currencies. The concentration of global economic power in American hands was far greater in 1971 than today. Repeating the 1971 playbook of unilateral action may not produce similar outcomes given these changed circumstances.

10. The Unacknowledged Choice and Its Consequences

10.1 Why the Contradiction Cannot Be Resolved

The fundamental incompatibility between manufacturing revival and dollar dominance warrants clear restatement precisely because it is so often obscured in policy discussion. The mathematical impossibility is straightforward. Reserve currency status requires

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27 U.S. Department of State Office of the Historian, "Nixon and the End of the Bretton Woods System, 1971–1973," accessed January 2026, https://history.state.gov/milestones/1969-1976/nixon-shock

28 Roger Lowenstein, “The Nixon Shock,” *Bloomberg*, August 5, 2011, https://www.bloomberg.com/news/articles/2011-08-04/the-nixon-shock

29 Federal Reserve History, "Nixon Ends Convertibility of U.S. Dollars to Gold," accessed January 2026, https://www.federalreservehistory.org/essays/gold-convertibility-ends

supplying currency to the world in quantities sufficient to meet global demand for reserves, transaction balances, and safe assets. Supplying currency in these quantities requires running deficits, as the currency flows out through the trade account when the issuing country purchases more than it sells. Running these deficits requires importing more than exporting, which by definition means reduced domestic production relative to consumption. Manufacturing revival requires reducing these imports through some combination of tariffs, quotas, or currency depreciation. Reducing imports eliminates the mechanism for supplying currency to the world. Therefore, it is mathematically impossible to simultaneously maximize both goals. This is not a matter of finding the right policy mix or achieving better international coordination. It is a structural impossibility embedded in the international monetary system.

The policy impossibility follows directly. The tools to strengthen the dollar including tight monetary policy, free trade agreements, and policy predictability necessarily undermine manufacturing by maintaining strong currency that makes exports expensive and imports cheap. The tools to boost manufacturing including tariffs, accommodative monetary policy, and active industrial policy necessarily undermine the dollar by reducing its stability and diminishing the trade deficit that supplies global liquidity. No policy package can eliminate this trade-off because the tools themselves work in opposite directions. Political leaders claiming that both goals are simultaneously achievable are either ignorant of these dynamics or dishonest with their constituents. Neither possibility inspires confidence in effective governance.

The political impossibility completes the picture. The manufacturing constituency, concentrated in electorally critical regions, demands visible action on trade issues with an intensity that the more diffuse dollar dominance constituency cannot match. The financial constituency supporting dollar dominance struggles to generate comparable political mobilization because benefits are invisible and widely distributed. Electoral mathematics inevitably favours the concentrated manufacturing constituency in swing states over the dispersed financial constituency in politically safe states. Therefore, political incentives push toward contradictory policy promises that cannot be simultaneously fulfilled, creating the conditions for either policy failure or crisis.

10.2 The Current Trajectory: Manufacturing Chosen by Default

The evidence increasingly suggests that the choice between manufacturing revival and dollar dominance has already been made, even if not explicitly acknowledged. Policy signals point unambiguously in one direction. Tariff escalation continues despite obvious dollar weakness, with tariffs bringing in $287 billion in additional revenue in 2025, representing a nearly 200% increase over previous levels[30]. Rhetoric attacking Federal Reserve independence has become routine rather than exceptional. National security arguments are increasingly used to override economic efficiency considerations in policy debates. Alliance relationships are being subordinated to trade demands, with threats of tariffs used against traditional allies.

Market signals confirm this interpretation. The dollar's 11% decline in the first half of 2025 reflects market pricing of policy direction rather than temporary fluctuation[31]. Foreign Treasury demand has weakened at the margin despite the absence of obvious alternatives, suggesting fundamental concerns about U.S. policy trajectory. Alternative reserve assets

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[30]]: The Conversation, "After a year of Trump, who are the winners and losers from US tariffs?," January 2026, https://uk.finance.yahoo.com/news/trump-winners-losers-us-tariffs-172757714.html States: "Customs revenue rose sharply by US$287 billion (£213 billion)."

[31] Alex Kozul-Wright, “Why Is the U.S. Dollar Falling by Record Levels in 2025?” Al Jazeera, July 1, 2025, https://www.aljazeera.com/economy/2025/7/1/why-is-the-us-dollar-falling-by-record-levels-in-2025

including gold have seen increased central bank interest despite their limitations. Term premiums are rising, indicating that investors require higher compensation for holding longer-term dollar assets.

Political signals complete the picture. No significant pushback from the administration has emerged in response to dollar decline, suggesting acceptance if not active embrace of the trend. Messaging consistently emphasizes manufacturing jobs over financial dominance in ways that reveal priority ordering. Policy personnel are increasingly drawn from the economic nationalist wing rather than the traditional free-trade Republican establishment. Traditional "strong dollar" rhetoric has been abandoned in practice even if occasionally invoked for diplomatic purposes.

The implication is clear: the United States is pursuing the manufacturing revival path and accepting, perhaps without fully recognizing, the costs to dollar dominance that inevitably follow. The question is no longer whether this transition will occur but rather whether it will be managed deliberately or emerge chaotically from the collision of contradictory policies.

10.3 What Happens Next: Three Critical Uncertainties

Three critical uncertainties will determine whether the transition proves manageable or catastrophic. The first concerns the pace of confidence shift in global markets. In the gradual scenario, the dollar's share of global reserves declines at a rate of 0.5-1% annually, allowing time for adjustment by all parties. In the sudden scenario, a triggering event precipitates rapid confidence loss and disorderly repricing across global markets. Key factors determining which scenario materializes include potential Treasury auction failures, unexpected geopolitical shocks, and domestic political instability that undermines confidence in American institutions.

The second uncertainty involves the effectiveness of manufacturing policy itself. The optimistic scenario envisions reshoring creating 2-3 million jobs concentrated in targeted sectors and regions. The pessimistic scenario sees automation limiting job gains, with manufacturing output rising only 1% in 2025 despite substantial protection, retaliation offsetting intended benefits, and costs exceeding gains. Key factors include the pace of technological change in manufacturing, the nature and extent of international responses to U.S. protection, and the quality of policy execution at federal and state levels[32].

The third uncertainty concerns what replaces dollar dominance in the international monetary system. The multipolar scenario features multiple currencies sharing reserve functions without any single successor to dollar hegemony. The yuan scenario involves China capitalizing on U.S. mistakes to establish the yuan as the primary alternative reserve currency. The digital scenario envisions technological innovation enabling new monetary arrangements through cryptocurrencies or central bank digital currencies. The continuation scenario involves dollar dominance eroding without clear alternatives emerging, creating an extended transition period of monetary uncertainty.

Critically, these uncertainties interact in ways that could amplify problems. If confidence shifts suddenly before manufacturing policies bear fruit, manufacturing gains cannot offset economic disruption from financial crisis. If manufacturing policy fails to deliver promised benefits, dollar decline becomes pure cost without offsetting gains. If no viable alternative emerges to the dollar, the transition could prove chaotic rather than orderly, as the

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[32] Federal Reserve Board, “Industrial Production and Capacity Utilization (G.17), Release Date: January 16, 2026,” U.S. Federal Reserve Board website, https://www.federalreserve.gov/releases/g17/current/table12.htm

international monetary system lacks obvious replacement arrangements. The worst case involves simultaneous sudden confidence loss, manufacturing policy failure, and absence of alternatives, potentially triggering a severe economic crisis with unpredictable political consequences.

11. Recommendations: Managing the Chosen Path

Given that the choice appears already made in favour of manufacturing revival, the relevant policy question becomes how to manage the inevitable transition away from overwhelming dollar dominance toward a more balanced economic structure.

11.1 Acknowledge the Trade-Off Explicitly

The current approach of pretending that both goals remain achievable creates multiple problems. Policy incoherence confuses both domestic and international audiences about actual priorities. Markets penalize this inconsistency and unpredictability through higher risk premiums. Allies remain uncertain about U.S. intentions, complicating cooperation on shared challenges. Domestic constituencies develop unrealistic expectations that inevitably lead to disappointment and political backlash when contradictions become undeniable.

Recommended transparency would involve explicitly acknowledging that dollar dominance will erode as manufacturing rebuilds. Providing realistic timeline and magnitude estimates would allow markets and foreign governments to adjust expectations and positioning accordingly. Explaining the rationale for prioritizing manufacturing over financial dominance could build public support for necessary sacrifices. Preparing the public for consequences including higher borrowing costs and inflation pressure would reduce the shock when these materialize.

The benefits of such transparency are substantial. Reducing policy uncertainty would lower the premium markets charge for unpredictability. Allowing allies to plan for a changing monetary landscape would facilitate coordination rather than leaving them to react to surprises. Enabling genuine domestic political debate about priorities would strengthen democratic legitimacy. Facilitating better policy coordination across agencies and levels of government would improve implementation quality. While politically difficult in the short term, this transparency would serve long-term interests by creating space for genuine policy adjustment.

11.2 Manage the Pace of Transition

The dangers of abrupt change cannot be overstated. Sudden confidence loss could trigger financial crisis as foreign holders of dollar assets rush for exits simultaneously. Disorderly dollar decline would raise import costs faster than domestic production can adjust, creating severe inflation pressure. The international system currently lacks alternative arrangements adequate to replace dollar-based systems, creating a dangerous vacuum. Retaliation spirals could destroy more economic value than is created through reshoring, leaving all parties worse off.

A gradual approach would involve phasing tariff increases over multiple years with clearly announced schedules that allow businesses to plan. Coordinating with allies on development of alternative payment infrastructure would ensure that system evolution proceeds orderly rather than crisis-driven. Supporting orderly central bank diversification rather than forcing rushed decisions would maintain financial stability during transition. Maintaining core elements of dollar infrastructure including deep Treasury markets and rule of law would preserve American advantages even as overall dominance erodes.

Realistic timeline targets would aim for a 10-15 year transition rather than attempting transformation in 3-5 years. Accepting that the dollar's reserve share will decline to approximately 45-50% from current levels around 58% would allow planning around realistic endpoints. Planning for 50-75 basis point increases in long-term borrowing costs would inform fiscal policy choices. Targeting manufacturing job gains of 100,000-200,000 annually rather than millions immediately would set achievable goals that maintain credibility.

11.3 Develop Complementary Policies

Manufacturing revival requires far more than trade protection alone. Infrastructure investment in transportation, energy, and broadband is essential for manufacturing competitiveness in the 21st century. Current infrastructure spending remains insufficient for genuine manufacturing renaissance despite recent increases. Sustained commitment extending beyond any single administration will be necessary for meaningful results.

Workforce development must align with actual manufacturing needs. Modern manufacturing increasingly requires technical skills that the current education system does not produce in sufficient quantities. Apprenticeship and vocational training programs need substantial expansion. Collaboration between educational institutions and manufacturers must improve to ensure relevant skill development.

Technology and innovation should receive heightened priority. Automation increasingly makes labour costs less decisive for location decisions than proximity to innovation and technical expertise. American competitive advantage lies in innovation capacity rather than low wages. Industrial policy should therefore focus on high-value, technology-intensive manufacturing rather than attempting to resurrect labour-intensive production that will inevitably migrate to lower-wage locations regardless of trade policy.

Regional policy must ensure that manufacturing gains are distributed in ways that match political coalition geography. Place-based policies targeting specific industrial communities could revive regions that have suffered decades of decline. Market forces alone will not direct investment to politically crucial regions, requiring active policy intervention to ensure that benefits flow to the constituencies that created political demand for change.

11.4 Prepare for Higher Borrowing Costs

Dollar decline and reduced reserve currency status necessarily imply higher borrowing costs for the federal government and American borrowers generally. The current fiscal trajectory is already unsustainable with federal deficits approaching $2 trillion annually and the debt-to-GDP ratio exceeding 100%[33]. Higher interest rates will exacerbate fiscal pressures substantially, potentially creating debt spirals if not addressed proactively.

Required adjustments will involve some combination of revenue increases through tax reform, spending prioritization acknowledging that all current commitments cannot be maintained simultaneously, entitlement reform given that Medicare and Social Security account for the majority of projected spending growth, and defence spending choices reflecting the reality that current force structure cannot be sustained with higher borrowing

[33] Tax Foundation, "Trump Tariffs: The Economic Impact of the Trump Trade War," January 23, 2026, https://taxfoundation.org/research/all/federal/trump-tariffs-trade-war/

costs. None of these adjustments will be politically easy, but delaying them will only make ultimate adjustment more painful.

The political challenge is formidable. Manufacturing constituencies that demanded trade protection generally oppose spending cuts that might affect them. Fiscal adjustment is inherently politically painful regardless of how it is distributed. Meaningful reform requires bipartisan cooperation that appears unlikely in the current political environment. The realistic assessment is that crisis may be required to force necessary changes, as political systems often cannot make hard choices until circumstances leave no alternative. This is unfortunate but consistent with historical patterns of fiscal adjustment in democratic systems.

12. Conclusion: Living With Contradiction

The Trump administration's simultaneous pursuit of manufacturing revitalization and dollar dominance represents not merely policy difficulty but fundamental impossibility. The mechanisms required to maintain the dollar's role as the world's primary reserve currency, persistent trade deficits supplying global dollar liquidity, are precisely the mechanisms that hollow out American manufacturing. Conversely, the policies needed to rebuild domestic industry through tariffs, currency management, and trade surplus orientation systematically undermine the foundations of monetary hegemony. This is not a problem amenable to better policy design or more skilful implementation. It is a structural contradiction inherent in the global economic system.

The United States became the reserve currency issuer through specific historical circumstances following World War II. Maintaining that role requires accepting specific costs that once appeared modest relative to benefits but have grown over time. For decades, the benefits of cheap borrowing and financial dominance seemed to outweigh losses in manufacturing employment and industrial capacity. That political calculation has shifted fundamentally. The geographic concentration of manufacturing job losses in electorally critical states, combined with broader anxieties about national economic trajectory and strategic vulnerability, has created overwhelming political pressure to prioritize industrial revival over financial dominance.

The current administration has responded to that pressure with policies that, whatever their specific merits or deficiencies, unambiguously move the United States away from the trade deficit model that sustains dollar hegemony. The consequences are already visible in currency markets where the dollar has declined significantly as traders price in policy implications. They are visible in Treasury markets where foreign demand shows concerning deterioration at the margin. They are visible in the developing alternative payment systems and currency arrangements that foreign central banks are building as insurance against dollar unreliability. The transition is not hypothetical or future. It is occurring now.

The critical question is not whether this transition will occur, as it is already underway, but whether it will be managed deliberately or emerge chaotically from policy contradictions. A gradual, deliberate transition over 10-15 years with clear communication and international coordination could produce outcomes where the United States gains manufacturing capacity and regional economic revival while maintaining significant though reduced financial advantages and international influence. A rushed, incoherent transition driven by policy lurches and political contradictions could trigger confidence crises, financial instability, and economic dislocation that overwhelms any benefits from industrial rebuilding. Current evidence unfortunately suggests the latter path remains more likely absent significant policy adjustment.

The tragedy lies in the administration's unwillingness to acknowledge the choice it has made. By continuing to promise both manufacturing revival and dollar dominance, it creates unnecessary uncertainty, undermines policy credibility, and prevents serious planning for inevitable consequences. Markets abhor contradictions and will force resolution through pricing mechanisms if policymakers refuse to resolve them through conscious choice. Political leaders pretending that sufficient determination can overcome structural contradictions serve neither their constituents nor national interests. Honesty about trade-offs, while politically difficult, would better serve long-term national interests than the current approach of promising everything while delivering confusion.

Historical perspective suggests that reserve currency transitions are inevitable over sufficiently long timescales. Britain learned this painfully between the world wars when attempting to maintain sterling's role despite obvious relative decline. The United States has enjoyed dollar dominance for approximately 80 years, an exceptionally long run by historical standards. The rise of China, the development of Europe, and advancement of financial technology all suggest that some evolution away from dollar monopoly was likely regardless of U.S. policy choices. The question is whether the United States manages this transition to maximize advantages and minimize disruption, or whether it stumbles into crisis through pursuing contradictory goals.

As of January 30, 2026, the evidence suggests that stumbling toward crisis remains more probable than managed transition. The administration has chosen manufacturing revival whether it admits this or not. Market pricing reflects this reality even as official statements maintain fiction of continued dollar dominance. The task now is managing that choice's consequences with clear eyes and realistic expectations rather than maintaining comfortable illusions that prevent necessary adjustment. The dollar will persist as a major international currency. The depth of U.S. financial markets, the strength of American institutions, and the absence of clearly superior alternatives ensure continued significant role. But the era of overwhelming dollar dominance, where the United States could borrow indefinitely at minimal rates while consuming beyond its production, is ending. It is ending because the political coalition that brought the current administration to power has decided that costs exceed benefits.

That represents a legitimate political choice. Nations must decide what they value and what they are willing to sacrifice to achieve those values. The contradiction is not in making this choice but in refusing to acknowledge it honestly. Pretending that manufacturing can be rebuilt while dollar dominance is maintained, that trade deficits can be eliminated while the world continues hungering for dollars, that policy can achieve contradictory goals through sufficient determination, this is the genuine danger. The path forward requires honesty about trade-offs, clarity about priorities, and careful management of transitions. It requires acknowledging that manufacturing revival will come at financial cost, that regional economic gains will coincide with reduced international monetary power, that the America of 2040 will differ from the America of 2000 in ways both desirable and challenging.

Above all, it requires recognizing that the contradiction Trump faces is not unique to him or this moment but inherent in the role the United States has played in the global economy since Bretton Woods established dollar hegemony. That role was never permanent. The only question was how it would end, deliberately or by accident. The current trajectory suggests that accident remains the more likely outcome. Whether subsequent administrations can manage what this one has set in motion remains the defining economic and geopolitical question of our era.

Appendix: Key Data and Metrics

The U.S. trade balance has deteriorated substantially over the past quarter century. In 2000, the trade deficit stood at $380 billion. By 2010, despite the Global Financial Crisis, it had grown to $500 billion. The 2020 deficit reached $680 billion, and 2024 saw it expand to $918 billion according to Bureau of Economic Analysis data[34]. Early 2025 trends suggest the deficit may exceed $1 trillion annually, though final figures remain unavailable as of this writing[35].

Manufacturing employment tells a similarly stark story. The sector employed 17.3 million Americans in 2000. The 2008 financial crisis and subsequent recession devastated manufacturing, with employment falling to 11.5 million by 2010. A modest recovery brought employment to 12.2 million in 2020, with December 2025 figures showing approximately 12.7 million manufacturing workers[36]. This represents a net loss of 4.6 million manufacturing jobs over 25 years despite population growth of over 60 million during the same period.

The dollar's share of global reserves has declined gradually but persistently. International Monetary Fund COFER data shows dollar-denominated assets represented 71% of global reserves in 2000. This fell to 62% by 2010 and 59% by 2020. The most recent data from Q3 2025 shows the dollar comprising 56.92% of global reserves, the lowest level since 1994 and suggesting accelerating erosion of dollar dominance[37][38]**.**

U.S. federal debt has exploded over the same period. The debt stood at $5.7 trillion in 2000, representing approximately 35% of GDP. It reached $13.6 trillion by 2010, approximately 60% of GDP, driven by financial crisis responses and wars in Iraq and Afghanistan. The 2020 debt of $27.7 trillion represented roughly 100% of GDP. Current debt exceeds $35 trillion, approximately 105% of GDP, with projections suggesting continued growth absent major policy changes to either revenue or spending[39].

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[34] Stefan Papaioannou and Kei-Mu Yi, "The Effects of a Booming Economy on the U.S. Trade Deficit," *Federal Reserve Bank of New York, Current Issues in Economics and Finance* 7, no. 2 (February 2001), https://www.newyorkfed.org/medialibrary/media/research/current_issues/ci7-2.pdf

[35] Andres B. Schwarzenberg, *The U.S. Trade Deficit: An Overview*, CRS Report IF10619 (Congressional Research Service, December 9, 2020), https://www.congress.gov/crs_external_products/IF/PDF/IF10619/IF10619.9.pdf

[36] U.S. Bureau of Labor Statistics, All Employees, Manufacturing [MANEMP], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/MANEMP, February 5, 2026. All Employees, Manufacturing (MANEMP) | FRED | St. Louis Fed

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