

# 26-9 Taking geopolitically motivated US swap lines too far would harm the dollar and Fed independence

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June 2026

**Note:** The authors thank Nishtha Agrawal for research assistance and Gregory Auclair, Olivier Blanchard, Kimberly Clausing, Nell Henderson, LSF Editorial, Mark Sobel, Edwin M. Truman, and Steven R. Weisman for helpful comments. All opinions and errors are their own.

The Trump administration’s quest to reshape the international trade system has not stopped at seeking tectonic changes that put “America first.” President Donald Trump has also claimed the license to deploy discretionary tools of economic statecraft—carrots as well as sticks—in pursuit of economic or geopolitical ends. The president’s nonstop tariff threats display sticks aplenty, but Trump has offered carrots too. One that is gaining prominence is the offer of US dollar liquidity to favored nations. Most recently, the administration is considering a dollar swap line request from the [United Arab Emirates](#) (UAE), which would be hard to rationalize on purely economic grounds. The UAE request follows the grant of a swap line to Argentina in October 2025, with the stated goal of influencing its legislative election later that month.

In a world of growing geopolitical fault lines, such requests and the temptation to accede to them on short-term foreign

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policy grounds could become more common. In the past, one might have drawn comfort from America's long history of institutional capital accumulation designed to limit abuses. The Trump administration's unprecedented flouting of norms, alliances, and even laws in the service of narrow political and financial advantages suggests that previous understandings may no longer provide adequate safeguards.

This Policy Brief surveys how the United States has provided dollar liquidity through the US Treasury and the Federal Reserve. But the appropriate mode of liquidity injection depends on the economic, financial, and geopolitical contexts. The paper suggests a framework to minimize the risks of excessive politicization when US financial authorities provide dollar liquidity backstops abroad. The Policy Brief concludes that the Treasury is the more appropriate lending conduit when geopolitical concerns dominate, but that Fed dollar provision should primarily be targeted toward global financial stability objectives and normally be more insulated from short-term foreign policy motives. Until now, political abuses of these loan facilities have been constrained to some degree by laws, norms, and intergovernmental understandings, but compliance can no longer be assumed, and so more formal guardrails are needed.

## **BENEFITS AND RISKS IN US CRISIS LENDING**

Since the 1920s, the US government has occasionally offered dollar liquidity to foreign countries through the US Treasury or the Federal Reserve System. It has often been motivated by geopolitical as well as financial stability objectives, which need not be at odds and have generally coincided when both are in play. Typically, countries that are financially integrated with US markets and operate under similar market-based systems have been US allies—or at least not adversaries—and their economic well-being promotes a range of US interests without any offsetting strategic disadvantages.

US crisis lending serves several purposes. For countries facing financial distress, rapid dollar loans can help avert economic and political disaster. But beyond this obvious foreign policy rationale for crisis lending, rapid US support when global credit seizes up encourages financial institutions worldwide to rely on the dollar for lending and funding. Thus, the safety net that the United States

augments through its currency swaps underpins the dollar's international dominance among currencies while promoting general financial stability. Recognizing this role, the Fed has offered liquidity swap lines to foreign central banks since the Global Financial Crisis (GFC), expanding their scope as needed during global liquidity crunches. This has served America's long-term foreign policy goals in several ways. A more prosperous world is more stable politically, and the global dollar gives the United States unique advantages, not the least of which (unfortunately also subject to abuse) is a wide extraterritorial reach of financial sanctions (Fishman 2025).

Many countries play the currency swap game to deepen bilateral economic or political ties—China being a notable devotee—and more politicization may be inevitable for the United States, too, in an increasingly turbulent foreign policy arena. But as the issuer of the hegemonic currency, America is in a league of its own and arguably has a unique responsibility. While it is common to assert that the United States can issue dollars without cost and in unlimited amounts, serious longer-term harms are possible if geopolitical pressures on dollar liquidity provision go too far. Some of these harms occur because a pattern of policy license can shape structure in unintended ways.

Two specific structural risks are concerning. The first is a reduction in the independence of the Federal Reserve, perhaps under force of a new Treasury-Fed accord that could tighten Treasury control over the central bank's foreign currency dealings and facilitate their greater use as a foreign policy tool. The second risk, related to the first, is a reduction in the dollar's global role, as countries "de-risk" their dollar dependence. The Fed cannot operate independently of US long-term foreign policy interests, of course, but its independence has served those interests well in the postwar era. Excessive pressure to pursue short-term political goals will undermine the Fed's longer-term effectiveness.

## **THE TREASURY, THE FED, AND GLOBAL DOLLAR LIQUIDITY**

Trump's most striking early deployment of dollars for geopolitical ends was the US Treasury's announcement in September 2025 that it planned to negotiate a \$20 billion swap framework agreement

to aid Argentina's President Javier Milei, who faced the mutually reinforcing perils of a currency crisis and electoral defeat. Argentina is not of systemic economic importance to the United States or to the regional economy, but the Trump administration viewed the political success of Milei, an ideological ally, as a critical step in its plans to extend US sway throughout Latin America—the so-called [Trump corollary](#) to the Monroe Doctrine. Loans from the US Treasury's Exchange Stabilization Fund (ESF), collateralized by Argentine pesos and coupled with unprecedented [direct US peso purchases](#) in the Buenos Aires market, provided the “bridge” to a Milei electoral victory that Treasury Secretary Scott Bessent had predicted.

The US Treasury's currency swap for Argentina was devised on the fly. Very different are the Federal Reserve's uncapped standing liquidity swap lines with five advanced-economy central banks: the Bank of Canada (BOC), the Bank of England (BOE), the Bank of Japan (BOJ), the European Central Bank (ECB), and the Swiss National Bank (SNB). The Fed simply creates the dollars it lends, accepting as collateral currencies that foreign central banks similarly create. At the end of the swap's term, the transaction is reversed, at the initial exchange rate (so there is no currency risk). Although the foreign central banks will generally use their borrowed dollars to support their own financial institutions' dollar needs, they, and not the Fed, bear any credit risk. During past crises, the Fed extended limited temporary swap lines to several central banks that are less systemically consequential than these “elite five,” but that still could affect US and global financial stability in a time of stress. The Fed also maintains separate limited swap lines with its trade area partners, Canada and Mexico.

In contrast, the ESF can draw only from a limited fund of about \$220 billion, which constrains its potential as a global last resort lender of dollars. That sum is not nearly enough to handle a potential financial crisis of global scale. There are several ways to measure the offshore dollar market, but one measure, the US dollar claims of non-US banks, reached [more than \\$16 trillion](#) by 2023 and continues to grow. Only the Fed can backstop a market this size and thereby support the dollar's global currency dominance.

The torrent of coercive commercial actions and threats from the Trump administration has raised fears abroad that the US government might commandeer the Fed's powerful swap lines in pursuit of immediate economic or political wins. This has been the pattern with tariffs, for example. Swaps could be offered in return for favors (carrots) or withdrawn in acts of punishment (sticks). Responding to these fears, [then-Fed Chair Jerome Powell](#) [insisted](#) in July 2025 that “we still have the same authorities, and we’re still prepared to use them in situations where it’s within our legal authorities and where we think it makes sense.” But Powell’s judicious formulation leaves a considerable gray area where the executive branch could push the weaponization of swap lines disturbingly far. Worse still, the “legal authorities” Powell cites [could be diluted further](#) were the Supreme Court ever to apply to the Fed its “unitary executive” doctrine, which holds that Congress cannot make executive branch agencies independent of the president.

It is very common for finance ministries to have formal responsibility for countries’ international financial relations, including exchange rates and foreign exchange intervention, whereas the central bank is responsible for the policy interest rate. For the United States, the Treasury formulates its leading international role [as follows](#): “The Secretary of the Treasury is the chief international monetary policy official of the United States. The Federal Reserve has separate legal authority to engage in foreign exchange operations. The Federal Reserve’s foreign exchange operations are conducted in close and continuous consultation and cooperation with the Secretary to ensure consistency with US international monetary and financial policy.”

An inescapable trade-off exists between Treasury interventionism in foreign exchange and the autonomy of monetary policy because the exchange rate is a key channel of monetary policy transmission. The potential conflict is generally resolved in inflation-targeting countries through an implicit division of labor: Independent central banks prioritize their domestic price stability mandates, and their exchange rates mostly float. The Treasury and the Fed have long followed this arrangement cooperatively, but for the issuer of the world’s leading reserve currency, the standard accommodation leaves room for future discord over Fed foreign currency swaps.

## FOREIGN EXCHANGE IN A NEW TREASURY-FED ACCORD?

While the newly installed Fed chair, Kevin Warsh, did not explicitly discuss Fed swap facilities in his April 21, 2026, Senate confirmation hearing, his response to a question about the dollar's global role contained little to reassure worried US allies.

Warsh [repeated](#) the conventional mantra that the Fed's responsibility is over interest rates, whereas the Treasury oversees international finance; but he went on to affirm that "the economic statecraft agenda led by Secretary Bessent and Secretary [Marco] Rubio is an important one." The Fed would "work with them," he continued, because such support would be "outside the conduct of monetary policy" and therefore would not compromise the Fed's independence or its core mission. In later [answers to senators' questions](#), he elaborated his belief that although the Fed is independent in monetary policy, "Fed officials are not entitled to the same special deference in areas affecting international finance, among other matters."

Even within the narrower domain of monetary policy, a trade-off can arise between the Treasury's financing preferences and the central bank's ability to manage the composition of its balance sheet. Coordination between the Treasury and the Fed has been quite close in recent decades, but Warsh and Bessent nonetheless see a problem and wish to resolve it in favor of the Treasury. However, because Fed swap lines by definition lead to foreign exchange operations as well as balance sheet changes, it is not far-fetched that in the "[new Treasury-Fed accord](#)" that Warsh [has floated](#), Bessent could assert the Treasury's primacy over all US swap arrangements. That could push the Fed toward a more geopolitically motivated allocation of swap lines.

The same day as Warsh's testimony, President Trump confirmed that a swap line requested by the UAE was under consideration. That disclosure, and Bessent's Senate testimony the next day, led to some [retroactive parsing](#) of the incoming Fed chair's vague promise to cooperate with US economic statecraft. Bessent endorsed the utility of ESF or Fed swaps for countries such as the UAE and other Gulf and Asian countries that he said had requested them. His remarks and [subsequent social media posts](#) left the mode and criteria under which support could be provided unclear, though

he referred in general terms to the need to support the dollar's international role.

It did not take long for UAE Trade Minister Thani bin Ahmed al-Zeyoudi to clarify that the UAE had specific arrangements in mind, namely to access US funding on the same terms as the ECB and the other four central banks with standing Fed swap arrangements. As for the motivation, [he said](#), “It is an elite matter. It is not about bailing out.” Indeed, the UAE's holdings of international reserves exceed the size of the ESF, and its net international asset holdings are believed to be at least three times its GDP. Establishing a “gold-plated” Fed swap line simply to bolster a favored ally's sense of prestige—in the absence of even a potential shortage of dollars—would push the US central bank far out of its previously accepted lane.

## MODES OF US DOLLAR LIQUIDITY SUPPORT

Discussion of the UAE request highlights the different modes of bilateral US dollar support in crises. The main ones are funding in some form from the ESF; Fed swap facilities that are situational, temporary, and limited in size; and standing unlimited facilities that only the elite five central banks enjoy.<sup>1</sup> In the latter two types of operations, the Fed effectively acts as a lender of last resort (LOLR) for dollars.<sup>2</sup>

The United States can alternatively provide financial support through loans or loan guarantees approved by Congress—for example, the Marshall Plan or aid to Ukraine—but congressional processes are slower and not suited for fast-moving crises. Based on congressionally preapproved funding, the United States also participates in multilateral crisis lending through the International Monetary Fund (IMF). IMF support can come in various ways, some faster than others, but all involving explicit or implicit US backing through its participation in IMF financing.

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1 We also discuss below the Foreign and International Monetary Authorities facility and support delivered through the International Monetary Fund.

2 See, for example, Farhi, Gourinchas, and Rey (2011); Landau (2014); and Obstfeld (2009).

Different modes of dollar liquidity provision by the United States should serve distinct purposes and warrant mode-specific guardrails. In the remainder of this brief, we review the precedents, costs, and benefits of the different approaches to crisis interventions. We follow with recommended best practices for US bilateral lending to reduce potential costs.

## The ESF

The recent uses of the ESF to benefit Argentina and possibly the UAE and other countries have brought renewed attention to this little-known facility within the US Treasury. The Argentina swap line was used to stabilize the exchange rate of the peso, but without requiring Argentina to make arguably necessary policy changes (Sobel 2025). In the UAE case, it [has been argued](#) that, given its large central bank and sovereign wealth fund balance sheets, the country does not need ESF support at all. These controversies are only the most recent debates over ESF operations. Concerns that the executive branch uses the ESF to go around Congress to carry out bailouts are long-standing and motivate a renewed bipartisan congressional effort to tighten the rules around Treasury support.

The ESF was established in 1934 through the Gold Reserve Act to promote exchange rate stability as various countries abandoned the gold standard during the Great Depression (Henning 1999; Schwartz 1997). From the Treasury's standpoint, a key advantage of the ESF is the ability to act expeditiously and quietly, without entering inevitably slow budgetary appropriations processes and without much intrusive congressional supervision.<sup>3</sup> From the outset, the Treasury secured broad discretion in conducting ESF operations, although this has been frequently challenged in Congress. The Treasury's primacy in international financial matters dates from the Gold Reserve Act, which also centralized the US gold reserve fully under the Treasury's ownership.

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3 For a discussion of ESF finances and operations, see the US Treasury website: <https://home.treasury.gov/policy-issues/international/exchange-stabilization-fund/finances-and-operations>.

The ESF's tool kit has included direct foreign exchange intervention, loans, and swaps.<sup>4</sup> Its first foreign exchange intervention was in 1934 to support the dollar against the French franc. Although it was created to stabilize the international value of the US dollar, from the beginning the ESF served both the economic and geopolitical interests of the United States. The ESF's first bilateral stabilization agreement was with Mexico in 1936, when a loan was provided. An operation with China followed a few months later. In both cases, President Franklin D. Roosevelt and Treasury Secretary Henry Morgenthau—in the spirit of Secretary Bessent's hopes today—intended to leverage ESF lending into warmer political relations with a broader dollar-based currency bloc of countries (Flores Zendejas and Nodari 2025). Between 1936 and 1961, the ESF had exchange stabilization agreements with 12 Latin American countries (Henning 1999), reflecting a mix of financial and geopolitical motivations.<sup>5</sup>

Starting in 1961, as the US balance of payments swung into deficit and the dollar's gold convertibility came into question, the ESF was used extensively to defend the dollar. The need for the ESF to intervene in foreign exchange markets abated with the shift in the global financial system to flexible exchange rates, although ESF foreign exchange support operations continued, notably with participation in multilateral support schemes for the British pound sterling and the Italian lira during the 1970s.

The ESF played an important role in the resolution of the developing country debt crisis during the 1980s when it was used to provide bridge loans to countries undertaking debt restructurings. It has also offered bridge finance to countries awaiting loans from the multilateral financial institutions.<sup>6</sup> This was the case for Uruguay in August 2002—the last ESF foreign credit stabilization

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4 At present, aside from some loans related to domestic operations, the ESF maintains only two swap lines (Argentina and Mexico), with zero balances, and no foreign loans.

5 During the late 1930s and early 1940s, ESF loans in Latin America were motivated by President Roosevelt's Good Neighbor Policy (Flores Zendejas and Nodari 2025).

6 The ESF was also used for bridge loans to help clear the arrears of Liberia (2008) and Sudan (2021) to the IMF and the World Bank.

operation before Argentina last year. Unlike the 2025 agreement with Argentina, the Uruguay loan covered a funding gap of only a few days before an IMF disbursement, in a context of significant regional financial stress.<sup>7</sup>

More recently, the ESF was used for temporary financial support for some purely domestic operations. During the GFC, for example, the ESF was used to guarantee some money market funds. Likewise, during the COVID-19 pandemic, it was used under the Coronavirus Aid, Relief, and Economic Security Act to cover any losses to the Fed from the facilities that were created to cope with the pandemic. Both practices were subsequently prohibited by Congress.

The scale of ESF operations led to attempts to put it under congressional supervision and modify what Schwartz (1997) called “the secrecy in which both the ESF and the EEA [the UK Exchange Equalization Account of 1932] were designed to operate.” In 1977, Congress amended the 1934 Gold Reserve Act to tighten the reporting requirements for ESF operations. For loans of duration greater than six months, the president was now required to notify Congress in writing of the “unique or emergency circumstances” justifying the loan. Further legislation in 1978 mandated a detailed monthly financial statement. In March 1995, after the large loan to Mexico earlier that year to stabilize its currency, President Bill Clinton submitted to Congress a [detailed justification](#) of the loan’s national interest rationale and terms, consistent with the 1977 legislation.<sup>8</sup>

The Trump administration has not done this in the case of Argentina because the 1977 amendment applies only to ESF financial commitments of duration above six months. This loophole has allowed the recent set of ESF transactions involving Argentina to remain opaque, even though they have played out [over several months](#). Moreover, after the Treasury’s exchange

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7 Between 1936 and 2002, the ESF was used 125 times in total. See US Department of the Treasury, “[Exchange Stabilization Fund History](#).”

8 Congress then passed temporary legislation to constrain the ESF further. In effect until October 1997, the legislation discouraged the Clinton administration from offering ESF help to Thailand during its crisis in the summer of 1997. Some have argued that the absence of US support worsened Thailand’s plight while sending an adverse signal that encouraged speculation against other Asian currencies (Henning 1999).

stabilization agreements with foreign countries come into force, they must be reported promptly to the congressional foreign affairs committees by the State Department under the general disclosure requirements of the [Case-Zablocki Act](#) of 1972, which apply to all binding executive branch agreements (Henning 1999). So far, Bessent has declined to do so, [apparently invoking “national security” grounds](#), although a classified transmission of the report is mandated in such cases.

### **Federal Reserve reciprocal swaps**

Despite creative leveraging by the Treasury, the ESF’s limited resources could only go so far in supporting the dollar as US balance of payments troubles intensified during the 1960s. The Fed’s balance sheet offered opportunities outside of direct congressional control. At its January 23, 1962, meeting, the Federal Open Market Committee (FOMC) endorsed the Fed holding deposits of convertible foreign currencies and engaging in foreign exchange transactions on an “experimental” basis. By the end of the year, the Fed had entered into reciprocal currency agreements with nine foreign central banks and the Bank for International Settlements (Bordo, Humpage, and Schwartz 2015a). These arrangements were all temporary and limited in funding. As part of that mission, the Fed has also extended limited temporary swap lines during crises to several central banks that are less systemically consequential than the elite five but still affect global financial stability in periods of stress.

Prior discussions within the FOMC show the novelty of this approach for the Fed—though not for many foreign central banks. One concern within the FOMC was that Congress might view the Fed as effectively adding to ESF resources and thereby facilitating a Treasury end run around the congressional power of the purse. Another was the legality of the idea in the absence of specific congressional authorization—though eventually, justification was found in sections 12A(c) and 14(e) of the Federal Reserve Act. A major concern was the coordination of Fed and Treasury objectives in the operation of foreign exchange intervention (Cross and Truman 1990). In a comment echoed by several participants, Philadelphia Fed President Karl R. Bopp (who was a professional economist, not a lawyer or banker) worried at the [September 12,](#)

1961, [FOMC meeting](#) that “in the longer run . . . a possible conflict between Treasury policy and Federal Reserve policy in this area could develop. This was a thing to keep in mind in considering the basis on which any program would be entered into; that is, the sense in which the Treasury could direct Federal Reserve operations in this field even though Federal Reserve funds were used.”

This concern was about the key issue of Federal Reserve independence: If the Treasury indeed had primacy in international financial matters, then a Fed capacity in the area would give the Treasury some degree of control over the Fed’s balance sheet.

The Fed reciprocal currency arrangements of the Bretton Woods era could be drawn on by either party and were usually activated by US borrowings of foreign currencies. But sometimes the ESF lent dollars when foreign currencies came under speculative pressure, notably sterling. In the former case, the Fed was defending the dollar, unlike in more recent swaps aimed at resisting dollar appreciation. The Fed would swap dollars for a foreign currency and simultaneously use the foreign currency to buy dollars back from the same central bank. In this way, the foreign central bank transformed some of its “naked” dollar reserves into reserves covered by the swap’s exchange rate guarantee, which might in turn reduce its desire to exchange dollars for scarce US gold. Even when the Fed rushed in to help an ally such as Britain, the moves were generally defensible on pure financial stability grounds. A disorderly British devaluation, it was argued, could destabilize the entire fixed exchange rate system and eventually rebound onto the dollar. This turned out to be the case, as the 1967 UK devaluation triggered a period of growing unease in foreign exchange markets.

As with the ESF, the motivation for Fed reciprocal swap lines changed with the effective end of the US gold convertibility commitment in August 1971 and the advent of floating exchange rates in 1973. Still, the network remained in place and was used. Geopolitical considerations sometimes influenced the terms. In June 1979, for example, Mexico requested a near doubling of its swap line (which dated from the 1960s), to be announced at or before an upcoming meeting of the presidents of Mexico and the United States. Mexico claimed it had no immediate need for financial support. [Senior Fed staff advisers](#) were skeptical of using

the facility for political reasons, as were several FOMC members. For example, Fed board governor Philip E. Coldwell [remarked](#), “I think there is a politicizing of this swap line arrangement that we have fought, especially with such countries as [redacted] wanted a swap line because they wanted to be a part of the club. Mexico now wants to be a part of a bigger club.” Two months later, however, under Paul Volcker’s chairmanship for the first time, [the FOMC approved](#) Mexico’s request. Extensive redactions in the transcript unfortunately hide the FOMC’s full reasoning, but clear concerns about the precedent being set remained.

In 1982, it was Mexico that kicked off the developing country debt crisis of the 1980s—worries about its financial position can be found in the FOMC transcripts just cited—and the country remained a focus for the Fed. By the end of 1998, however, no industrial country had drawn on a reciprocal swap since 1981 (Sweden). In consultation with the network member countries, the Fed ended the reciprocal swaps save for Mexico and Canada, which fell under the North American Framework Agreement (NAFA) of 1994 that went into effect shortly after the North American Free Trade Agreement (NAFTA). A key consideration in dismantling the network was that it was largely seen as supporting foreign exchange intervention, whereas most members had become comfortable with more freely floating exchange rates (Truman 2014), which became less volatile as inflation-targeting monetary regimes spread.

### **Post-GFC liquidity swaps**

Partly supported by the success of the floating-rate system, international financial markets were expanding in scope and depth, raising a new economic rationale for dollar liquidity provision. The decade from 1998 to 2007 saw a global explosion of international financial intermediation and leverage. The dollar’s role as the predominant funding currency posed a systemic vulnerability for banks and other financial institutions worldwide if dollar liquidity were to dry up.

Emerging market economies, having recently experienced not only the “Tequila Crisis” sparked by Mexico in 1994–95 but also serious crises around Brazil, Russia, and several Asian countries, accumulated vast precautionary dollar reserves. Richer countries

remained more complacent. Financial tensions that would ultimately metastasize in the GFC emerged during the summer of 2007 and persisted. At the end of the year, the Fed established six-month swap agreements with the ECB and the SNB, based on the authorities already invoked back in 1962.

As Goldberg, Kennedy, and Miu (2011) point out, “The idea of using a [central bank (CB)] swap facility to address money market dysfunction and achieve broader financial stability contrasted with the goals of most prior CB swap agreements, which had been used primarily as tools of foreign exchange policy.”<sup>9</sup> The swap lines were gradually expanded in size and country coverage; the month after the Lehman Brothers collapse in September 2008, the Fed uncapped the swap lines of the BOE, BOJ, ECB, and SNB and responded affirmatively to swap line requests from four emerging market economies—Brazil, Korea, Mexico, and Singapore—subject to additional safeguards (Lowery, Sheets, and Truman 2020).<sup>10</sup>

Despite the sizable dollar stockpiles these countries held, the FOMC recognized the four emerging market economies as systemically important and vulnerable to capital account volatility

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9 That said, the swap lines probably discouraged an even larger dollar appreciation than the one that the prevailing dollar funding scarcity caused. Conversely, the reciprocal swap lines of the 1960s were eventually used to channel liquidity to the offshore eurodollar market, in a preview of current practices (McCauley and Schenk 2020). Fed liquidity swaps are distinct from reciprocal arrangements in that only one party—the foreign central bank—draws liquidity, but the Fed pays no interest and holds its foreign currency receipts at the foreign central bank. In a reciprocal swap arrangement, either country can draw the other’s currency (possibly subject to conditions). See Bordo, Humpage, and Schwartz (2015b); as these authors put the distinction between the Bretton Woods and the post-GFC swaps, “What started out as a device to provide central banks with cover for unwanted dollar positions had returned as a way to finance global lender-of-last-resort operations in U.S. dollars.”

10 These swap lines were for drawings up to \$30 billion per country. Mexico’s was separate from its much smaller swap lines under NAFTA, which are with both the ESF (capped at \$9 billion) and the Fed (capped at \$3 billion). The NAFTA swap line with the Fed is a reciprocal facility. Canada also has a NAFTA swap line with the Fed, capped at \$2 billion.

should markets perceive them to be running down their reserves. Moreover, the Fed's "seal of approval" alone could help stabilize capital flows. In remarks to the [FOMC at its meeting October 28-29, 2008](#), Nathan Sheets, head of the international division, laid out the Fed staff's case for liquidity swap lines. It is worth reproducing in full:

We see the case for these swap lines as resting on three important observations. First, each of these economies has significant economic and financial mass. Mexico, Brazil, and Korea are all large economies with GDP of around \$1 trillion, and Singapore is a major financial center. Given the structural interconnectedness of the global economy and the financial fragilities that now prevail, a further intensification of stresses in one or more of these countries could trigger unwelcome spillovers for both the U.S. economy and the international economy more generally. Our interdependencies with Mexico are particularly pronounced. Second, these economies have generally pursued prudent policies in recent years, resulting in low inflation and roughly balanced current account and fiscal positions or, in the case of Singapore, sizable surpluses. Accordingly, the stresses that these countries are feeling seem largely to reflect financial contagion effects from the advanced economies, including sharp reductions in risk appetite, rapid deleveraging by global investors, and a drying up of liquidity in dollar funding markets. Third, there is good reason to believe that swap lines with the Federal Reserve would be helpful in defusing the economic and financial pressures that they now face. These lines would promote financial stability by helping to ensure that financial institutions and corporations in these countries have access to dollar liquidity.

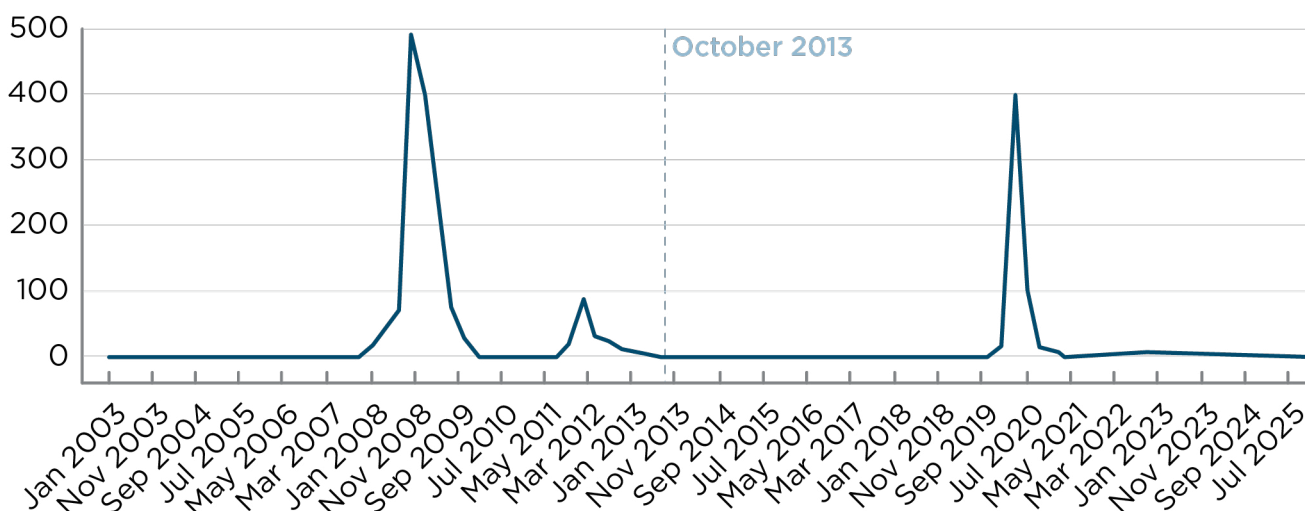
The renewed swaps expired in February 2010, only to be resuscitated in May 2010 for the elite five central banks—the ones most systematic for global financial markets—as the Greek debt crisis metastasized to a broader set of European sovereigns and to private funding markets. Those swap lines were made standing facilities in October 2013 in the wake of the euro crisis, and temporary swaps were extended to nine additional central banks, including the four emerging market central banks singled out in 2008, as the spread of COVID-19 unleashed financial panic in March 2020. All these additions to the swap network were justified on

purely economic grounds; all expired at the end of 2021. Figure 1 shows outstanding swap drawings on the Fed since 2003.

Figure 1

### Outstanding Federal Reserve liquidity swaps

billions of US dollars



Source: Board of Governors of the Federal Reserve System via Federal Reserve Economic Data.

### Gold-plated Federal Reserve swaps

The elite five central bank swaps lines are currently gold-plated because they are uncapped and permanent subject to formal annual renewal by the FOMC; they can be activated at any time by mutual consent. At the [October 29–30, 2013](#), FOMC meeting that approved them, System Open Market Account (SOMA) manager Simon Potter presented the staff case as follows: “Standing swap lines would reduce uncertainty among market participants as to whether and when these arrangements would be renewed and would limit the risk that decisions regarding the renewal of these arrangements would be misinterpreted.”

The five major central banks all oversee sizable economies or financial sectors with high governance standards and strong frameworks for macroeconomic and financial stability. Their financial sectors are highly integrated with that of the United States. The swap lines also fulfill an important function for

the recipient and world economies. The euro crisis made clear the centrality of the dollar for funding decisions worldwide, the breadth and complexity of funding markets, and their possible fragility. The Fed's 2013 decision was viewed as supporting the dollar ecosystem by communicating the certainty of LOLR support and removing the risk that the removal or extension of support might destabilize markets. Although difficult to see in [figure 1](#) (page 16) compared with the big spikes during crises, the BOE, BOJ, ECB, and SNB continually make small drawings on their liquidity lines to smooth conditions in their onshore dollar funding markets.<sup>11</sup>

The UAE has asked for admission to this elite club, but it fails to meet the admission criteria. Extension of a gold-plated Fed swap line would require FOMC approval but would be contrary to the criteria the committee has used in the past, even for temporary capped swap arrangements.

The UAE is at best a regional financial power and not economically systemic for the United States or other industrial countries. Moreover, its governance arrangements, including for its financial sector, raise serious concerns.<sup>12</sup> Being battered in the war with Iran, it is seeking to restore the luster of Dubai as a financial center and of its economy as a destination for foreign investment. It is also seeking leverage in its regional feud with Saudi Arabia, which could equally well request comparable treatment. Extension

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11 The BOC has no need to do so because its main banks are effectively part of the domestic US wholesale funding system. As noted above, use of dollar swaps for intervention in offshore dollar markets has its roots in the Bretton Woods era, as McCauley and Schenk (2020) discuss.

12 The UAE has long been a major conduit for money laundering operations. A 2020 Financial Action Task Force (FATF) report was critical of the UAE in this regard, including for its weak international cooperation (FATF 2020). There have been improvements on regulation and enforcement, and the UAE was removed from FATF's gray list in 2024. But important risks remain, including with real estate transactions, the *hawala* money transfer system, and the [gold trade](#). The IMF has welcomed recent improvements but further efforts are needed, especially because the UAE has become a leading hub for virtual assets (it has multiple virtual asset jurisdictions: onshore, offshore, and free-trade zone).

of a Fed swap would essentially be on foreign policy grounds (Sobel 2026). That risks politicizing the Fed in ways it has long resisted, and for good reason.

### **The Foreign and International Monetary Authorities facility**

Another support for foreign official holders of Treasuries is the Foreign and International Monetary Authorities (FIMA) facility of the Federal Reserve. In principle open to all countries, this facility allows foreign official holders to exchange Treasuries for cash under repurchase agreements. The FIMA facility is of considerable benefit to the United States; it promotes use of the dollar as an international currency, lowers Treasury borrowing costs, and there is no risk because it is fully collateralized by the Treasury's own liabilities. The facility was opened during the COVID-19 "dash for cash" in March 2020 and became a standing facility in July 2021 (see Choi et al. 2022). While always available, its main utility is during market stress episodes.

### **Multilateral crisis lending (in which the United States participates)**

The United States also supports the global financial safety net through its participation in the IMF. The IMF is the principal provider of multilateral support to countries in financial difficulty. IMF lending could be in place of, or as a complement to, ESF and Fed resources. The IMF can provide financing to its members through its standing lending facilities for specific countries or through a general allocation of special drawing rights (SDRs), which are distributed to all members in proportion to their IMF quota shares and can be exchanged for freely usable currencies, including dollars.<sup>13</sup>

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13 SDR allocations require 85 percent of the IMF's voting power. The United States can block SDR allocations given it holds a 16.5 percent voting share. Countries can exchange their SDRs for dollars with the ESF, if the ESF chooses to do so. In turn, the ESF can, under the SDR Act of 1968, monetize its SDRs for dollars with the Fed by issuing SDR certificates at a zero interest rate (thus affecting the US money supply unless the Fed sterilizes). The most recent IMF SDR distribution was in August 2021 (of about \$650 billion) to help members overcome the impact of the COVID-19 epidemic. The allocation faced [concerns](#) in Congress because it benefited some US adversaries, such as China, Iran, Russia, Syria, and Venezuela.

Multilateral lending has certain advantages and disadvantages. IMF lending could require corrective policy measures by the borrowing country and rely on the Fund's large balance sheet and its ability to borrow from member countries.<sup>14</sup> Moreover, IMF lending can help maintain global financial stability, which in times of crisis alleviates some of the pressure on global dollar financing system, and the smooth functioning of the market for US Treasury instruments.

A key drawback of Fund arrangements, however, is the length of time it may take to reach agreements on policies with the borrower—except for countries who have prequalified for the IMF's liquidity lines, such as the Precautionary and Liquidity Line, the Flexible Credit Line, and the Short-Term Liquidity Line. And even these have had limited success due to possible concerns about stigma.<sup>15</sup> Moreover, lending by the IMF inevitably involves the specific national interests of other members, especially the Fund's largest shareholders. Such considerations were evident, for example, in delays in IMF lending to the United Kingdom during the Suez Crisis of 1956 (Boughton 2000), more than one loan to Ukraine and Argentina, and the IMF's failure to lend to Iran during the COVID-19 epidemic (Mazarei and Loungani 2023).

Notwithstanding these realities, the consultations and processes leading to IMF loans and programs are relatively transparent, and IMF management and staff are accountable to the Fund's Executive Board, whose members in turn report to national authorities. Moreover, the IMF took steps after the various bouts of crisis—including the Mexico devaluation of 1994, the Asian financial crisis, and the GFC—to correct the shortcomings in its surveillance and lending operations to better detect and address possible crises. On surveillance, the IMF has improved its monitoring of developments and risks related to exchange rates, capital markets, and financial sectors. The Fund has also promoted better preparation and timely dissemination of economic information and supported more rigorous standards and codes, such as for fiscal management. To address the

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14 The IMF can borrow from its member countries through the New Arrangements to Borrow and Bilateral Borrowing Arrangements.

15 Introduced in 2020, the Short-Term Liquidity Line had [limited uptake](#) and will wind down in 2027.

need to tailor its policies to specific country conditions, including through the Integrated Policy Framework of 2020, the Fund has been improving its lending operations by streamlining its conditions for financial support and accelerating the availability of resources.

These improvements, together with the generalized move toward floating exchange rates among emerging market economies, help explain the low usage of the ESF for credit stabilization operations after 2002.

## **HOW FAR DOES THE FED'S INDEPENDENCE PROTECT ITS AUTHORITY OVER SWAPS? THE FOREIGN CURRENCY ACCORDS**

The [1951 Treasury-Fed Accord](#) ending the Treasury's wartime fiscal dominance is rightly celebrated; however, there have been two significant Treasury-Fed accords around exchange rate policy since the Fed returned to foreign exchange operations during the early 1960s. The discussions and deliberations surrounding these suggest to us that they provide at best an imperfect defense against weaponization of Federal Reserve swap lines by the executive branch.

The "first accord" dates from December 18, 1961, when Treasury Secretary C. Douglas Dillon wrote as follows to Fed Chair William McChesney Martin after the Treasury had requested the Fed to lend its balance sheet to join in reciprocal currency arrangements (Cross and Truman 1990). In the letter, Dillon pledges to respect the Fed's independence (see the final sentence, where the emphasis is added):

If the Federal Reserve decides to undertake foreign currency operations, the Treasury and the Federal Reserve will both need to recognize in advance, of course, that they will have to feel their way; that effective methods of operations and effective working relationships between them can only be worked out gradually; and that they need to learn together the best ways of carrying our mutual responsibilities for a sound dollar internationally. *In such an effort, the Treasury on its part would naturally want to avoid impinging on the independence of the Federal Reserve System within the Government.*

Consistent with Dillon's assurances, the FOMC began to formulate self-imposed authorization instruments to govern the

parameters of its foreign exchange operations, which were renewed annually. In March 1962, Martin communicated his understanding to the chair of the House Banking and Currency Committee (Cross and Truman 1990):

We must recognize that Congress has given the System responsibility for exercising its own judgement in monetary matters, free from control by any Executive Department. Therefore, if the occasion should ever arise that the Secretary of the Treasury should ask the Federal Reserve to engage in foreign exchange operations which in our judgement were financially unsound, we would have to refuse. On the other hand, the Federal Reserve obviously must operate within the framework of the established foreign financial policy of the United States. Therefore, even if the Federal Reserve believed that certain operations in foreign exchange were desirable to protect the dollar, we would refrain from engaging in them if the Secretary of the Treasury or the National Advisory Council on International Monetary and Financial Problems advised us that the operations would conflict with United States foreign financial policy.

The FOMC guidelines evolved over time, but one—the Foreign Currency Directive (FCD) of 1966—had to be revised in 1976 to recognize the post-Bretton Woods floating exchange rate system, as would be codified in the second revision of the IMF Articles of Agreement agreed earlier that year. The [directive](#) agreed upon after the FOMC’s December 1976 meeting was painstakingly negotiated with the Treasury, resulting in the “second accord” (which largely reaffirmed the Fed’s understanding at the time of the first). The wording in the first paragraph of the directive has remained virtually the same ever since and coincided exactly with the Treasury language cited above:

System foreign currency operations shall be conducted:

- A In close and continuous consultation and cooperation with the United States Treasury;
- B In cooperation, as appropriate, with foreign monetary authorities; and
- C In a manner consistent with the obligations of the United States in the International Monetary Fund regarding exchange arrangements under the proposed IMF Article IV.

The FOMC discussion of the draft FCD indicates the Fed's beliefs about its freedom of action. Chair Arthur Burns introduced the draft by alluding to the negotiations with the Treasury: "The Foreign Currency Directive is a very brief document, but every noun and every verb and every proposition has been accorded the most loving care over several months." During the debate, he went on to say, "I, for one, have taken the position, and have so testified, that whereas our independence in the domestic area is complete, as far as foreign operations are concerned, foreign policy is, under our Constitution, a prerogative of the President. And if we engage in a foreign transaction, we therefore should do so only if we have the assent of the Treasury."

The opinion of the committee was that the Fed could not take a foreign currency action over the Treasury's objections. On the other hand, given the Fed's independence under the Federal Reserve Act (Richardson and Wilcox 2025), it would be justified in refusing a Treasury foreign exchange request in conflict with its congressional mandate. This is the same position Chair Martin had taken in the 1962 passage quoted earlier.

From the start, Fed leaders were concerned that participation in the foreign exchange markets—the Treasury's domain since the Gold Reserve Act—could compromise the Fed's independence in domestic monetary policy. Indeed, over many decades there has been resistance within the FOMC (e.g., Broaddus and Goodfriend 1995). But divorcing the Fed from exchange rate matters has never been a realistic option. During the 1960s, maintaining the dollar's gold peg was not only central to the foreign financial policy of the United States, but it was also viewed as necessary for global monetary stability. In the modern era, global use of the dollar is a first-order reality, which leaves the Fed with little choice but to act as a global LOLR. As Lowery, Sheets, and Truman (2020) explain in the context of the GFC,

Fed policymakers were forced to make difficult judgments as they sought to balance their explicit domestic mandate, the constraints of historical precedent, and their commitment to the stability of the global financial system as the issuer of the world's premier reserve currency. The key connection between these considerations was inescapable evidence that, without Fed action,

disruptions abroad would feed back into the US economy. The swap line program—with developed and developing countries alike—reflected the Fed’s efforts to balance these considerations.

Given the Fed’s inevitable involvement in foreign currency matters, some understanding between the Treasury and Fed is necessary. Our read of the current state of play as it applies to swap lines is that the Fed has agreed to seek Treasury assent before extending a new swap line and possibly before approving drawings from an existing one, but the Treasury could not insist that the Fed extend a swap line or allow a drawing contrary to the FOMC’s judgment.

This compromise still leaves several avenues through which the executive branch could weaponize swap lines. It could withdraw its assent for existing swap lines or for drawings from them. It could bring about, over time, a more compliant FOMC willing to agree to a new accord. In the extreme, it could sponsor an amendment to the Federal Reserve Act explicitly limiting the Fed’s independence, for example, by advance resolution of any conflicts between the Fed’s domestic mandate and the Treasury’s foreign currency objectives in the latter’s favor.

With all this, the Supreme Court’s unitary executive doctrine is a Damoclean sword hanging over the Fed, as it could lead the court to declare the central bank’s independence an unconstitutional delegation of executive power. There could be further developments in this direction soon.

## **POLICY CONSEQUENCES AND RECOMMENDATIONS**

Swap lines provided through the ESF and the Fed have served important functions. Historically, they have allowed the United States to provide quick liquidity support to partner countries, especially during global financial crises, thus safeguarding the effective functioning of the US and international financial systems. They have lowered the chances of disruptive sales of US Treasuries by foreign central banks and financial institutions, helping to avoid large movements in global interest rates and exchange rates. They have also helped to support the primacy of the dollar in international trade and finance. Finally, they have broadly

served the foreign policy interests of the United States. But recent developments have raised old and new concerns about ESF and Fed swaps and liquidity lines.

What are the appropriate roles for the Treasury and the Fed in providing emergency dollar liquidity? The primary domains for ESF and Fed liquidity support should be distinct, and overstepping the boundary too frequently and too far carries significant risks to the independence of US monetary policy and the international role of the US dollar.

### **The ESF**

Overall, the ESF has allowed the US Treasury to provide rapid support to emerging market and other economies, especially because IMF programs could take long to agree and involve some stigma for the borrowing countries. The ESF is also integral to facilitating US transactions with the IMF, the World Bank, and their memberships, including transactions in which countries convert SDRs into dollars, thereby operationalizing the SDR's function as an international reserve asset.

Even though it fell largely into disuse for international operations between 2002 and 2025, the ESF remains an essential part of the US tool kit for global economic stabilization and for promoting US foreign policy interests. Both of these rationales could become more prominent in the current geopolitical environment, the former because greater fragmentation in international markets could lead to more frequent financial distress.

The risk lies in more frequent use of the ESF for narrow and possibly partisan political gains. An expectation that Treasury largesse flows selectively to countries willing to deliver short-term political or commercial favors could hasten global financial fragmentation, which already seems likely to rise. Such a perception could also damage the long-term foreign policy interest of the United States. Because the ESF operates at the discretion of the president and the secretary of the Treasury, it can be much more vulnerable to these dangers compared with Fed swap and liquidity lines that are administered by an independent FOMC. If the ESF is to be an effective tool in promoting multilateral financial stability, which is very much in the overall geostrategic interest

of the United States, it is therefore important to address this and other more long-standing concerns, such as (1) the transparency of its operations and its exposure to losses; (2) circumvention of congressional budgetary processes; and (3) bailing out countries without insisting on needed corrective policies. To this end, we recommend consistent application of the following guardrails:

- 1 Limit the main tasks of the ESF to foreign exchange intervention and the provision of swaps and short-term loans. Exceptional circumstances aside, the ESF should not provide medium-term loans to countries; it should leave such lending to the IMF, with which it should coordinate as it did historically.
- 2 Govern foreign exchange interventions, loans, and swaps with clear principles, such as not supporting insolvent countries or those with unsustainable exchange rates and not undermining the operations of the Fed and international financial institutions.
- 3 Discuss needed, expedient, and practicable conditionality with countries, including commitment to an IMF program.
- 4 Promptly state to Congress the economic stability and foreign policy rationale and terms for ESF foreign exchange interventions, on loans of any maturity, and all swap framework agreements.

A [bill](#) recently proposed by Senators Chuck Grassley (R-IA) and Jeanne Shaheen (D-NH) would helpfully tighten up the reporting requirements for ESF actions, but we would amend the provision requiring at least 24 hours advance notice for any foreign assistance. In a fast-moving crisis, even a brief delay in necessary assistance could be destabilizing. Simultaneous notification of the relevant congressional committees together with prompt ex post briefings should suffice to ensure accountability.

Accountability is especially important because ESF interventions will inevitably be more heavily influenced by foreign policy considerations. To anchor expectations in financial markets worldwide, it is important that these considerations reflect, as much as possible, a bipartisan consensus on long-term US geostrategic goals rather than more contested short-term objectives (such as swaying an upcoming foreign election).

## Fed swap lines

Modern (post-2007) Fed swap lines are extended at the discretion of the FOMC and under its self-imposed guidelines. The Fed consults with the Treasury and possibly other parts of the executive branch before extending specific swaps. For example, in extending special and temporary swap lines to Brazil, Korea, Mexico, and Singapore in 2008, the Fed sought advance assent from both the Treasury and the State Department (Lowery, Sheets, and Truman 2020).

However, Fed autonomy over swaps cannot be taken for granted as a safeguard against weaponization.

In general, delegating decisions over Federal Reserve swap lines to the independent Federal Reserve brings at least three advantages:

- 1 Allowing politicized decisions over Fed swap lines would communicate that Fed liquidity support can come with strings attached. International use of the dollar would fall, as governments and businesses would not want to be highly exposed to mercurial liquidity support sometimes burdened with ex post conditionality. For the US standpoint, this would be an undesirable structural change in the world economy.
- 2 This delegation leaves the Fed's balance sheet under the Fed's control, not the Treasury's, thereby safeguarding central bank independence. Although it is true that the Fed can always sterilize the pure monetary impact of any Treasury-directed swap transactions, these transactions still impact bond markets and hence financial conditions; furthermore, they risk confusing markets if they run counter to the tenor of monetary policy. As we saw, this is a long-standing concern, going back to the 1961 FOMC discussions of support for the Treasury's efforts to support the dollar within the Bretton Woods system through the ESF.
- 3 The Fed's staff, particularly in the board's International Finance Division and at the New York Fed, are likely to have an advantage in assessing global needs for swap facilities.

We believe that when geopolitical interests are dominant rather than market functioning and stability per se, the proper intervention tool for the US government is the ESF, not the Fed's balance sheet. While limited, ESF resources are likely to be sufficient in such

contexts because they are, almost by definition, unlikely to occur during generalized financial crises. Should the ESF's current assets not suffice for the likely scope of future projects, the Treasury should approach Congress in advance to appropriate additional funds and submit to the resulting accountability.

Whether temporary or standing, Fed swap facilities are, in contrast, a key component of the US and global financial systems and should be deployed under the highest standards, with the least vulnerability to political distortion. This mode of deployment is also broadly consistent with the long-term foreign policy interest of the United States, just as, for example, the IMF's role is.

Sheets's 2008 presentation to the FOMC, discussed above, points to three tests that we believe any candidate for a Fed swap line should meet:

- 1 significant global economic or financial weight and interconnectedness;
- 2 a record of good governance and prudent policies resulting in low inflation and well-managed fiscal and current account outcomes;
- 3 the need for and likely success of the swaps in meeting the need.

These tests are all economic in nature; none is geopolitical. The Fed's staff is well positioned to make these determinations, although the Fed, of course, must be accountable to Congress for its stewardship of all aspects of monetary policy, including swaps.

None of this is to suggest that close coordination over global liquidity problems between the Fed and the Treasury is inappropriate or unnecessary. On the contrary, US economic policy will be more effective if the agencies' relationship is close and cooperative, as has been the norm historically.<sup>16</sup> The red line that

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16 Open political attacks on the US central bank coming specifically from the Treasury Department have been relatively rare, with exceptions including those of [Roger B. Taney](#) and [Bessent \(2025\)](#). In addition, Treasury-Fed relations were exceptionally fraught in the period leading up to the Accord of 1951. Treasury Secretary John W. Snyder [proclaimed](#) that "the delusion that fractional changes in interest rates can be effective in fighting inflation must be dispelled from our minds."

compromises central bank independence when crossed is for the Treasury effectively to commandeer the Fed's balance sheet.

Similar considerations apply to foreign exchange intervention. While increasingly rare in recent years, US currency interventions have, for the most part, been carried out jointly between the ESF and the Fed on an equal basis. It is recognized that the Treasury secretary is responsible for US international financial policy, yet the Fed is legally bound to pursue a congressional mandate that does not explicitly reference the dollar's foreign exchange rate. The Fed can decline to join in intervention—and has—when intervention runs counter to its primary mandate.

For example, if the Fed is tightening monetary policy while the Treasury seeks a weaker dollar, the Fed would risk confusing markets by joining the ESF's dollar sales, even if it were to sterilize their pure monetary impact. Moreover, the operation would likely fail to weaken the dollar, given a tightening domestic monetary stance, exposing the Fed to a loss of credibility that might ultimately damage its independence (Broaddus and Goodfriend 1995). Such conflicts have been rare, but like potential conflicts over swaps, they would require a legislative resolution if they became frequent.

A far-reaching 1990 Federal Reserve System task force report on foreign exchange intervention summarized the place of Fed-Treasury cooperation as follows (Cross and Truman 1990):

Though it may have an “independent” legal authority to undertake foreign exchange operations, in practice [the Federal Reserve] must and does operate in close consultation with Treasury consistent with the Secretary of the Treasury's responsibility for the international financial policies of the United States. The Federal Reserve brings to the consultative process a technical competence in financial matters, a background in and knowledge of monetary developments, an ability to participate in the financing of any operations, and very importantly, an independence and authority in monetary policy.

“Close consultation” does not mean subservience. It is the Fed's “independence and authority” that would be compromised if the Treasury were to push political considerations to the fore

in the allocation of Fed swap lines, to the detriment of the Fed's effectiveness and the dollar's global role.

## CONCLUSION

Only the Fed can be a global LOLR in dollars—not the Treasury. Yet if the supply of nonpoliticized LOLR services falls, so will the demand for dollars. Governments and markets will retreat from dollar exposure. In this way, repeated geopolitical exploitation of the dollar's central role will lead to structural financial market changes adverse to American interests. Moreover, the process will ultimately undermine Fed independence, harming US price stability and accentuating the dollar's global retreat. In the long run, it therefore may not be costless for the United States to provide dollars. Let the Treasury be the main responder when geopolitical objectives are dominant—subject to domestic political guardrails and accountability—while the Fed maintains its independence and global stewardship, from which the United States and the world benefit.

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