Chairman Luetkemeyer, Ranking Member Beatty, and Members on the committee,

Thank you for the opportunity to speak with you today on dollar dominance, federal fiscal mismanagement, and the implications for our nation's economy. I had the honor of serving as the Assistant Secretary for Economic Policy at the Department of the Treasury during the previous administration. In that role, I worked with Members on both sides of the political aisle and the Small Business Administration to quickly implement the Paycheck Protection Program and ensure that the economic devastation that might have resulted from the pandemic was not realized.

As Assistant Secretary, I told my team that the Treasury Secretary proudly states that the dollar will never not be the world's reserve currency and our job at Treasury was to make sure that it is always true. Maintaining that role means engaging in prudent economic stewardship, continuously upgrading the technology supporting the Nation's payment system, and showing restraint in our deployment of unilateral sanctions. Most importantly, we must demonstrate to the rest of the world that we are financially responsible by addressing our unsustainable fiscal path.

To understand why that is the case, we must start with the role of money. Academic literature has identified three purposes of money: (1) facilitate exchanges of goods and services, (2) serve as a store value from when the money is received until it is used, and (3) act as a unit of measurement.

Therefore, one reason the US dollar (USD) is the world's reserve currency comes from international trade. If contracts are settled in dollars, then banks that facilitate payment between international trading partners will want to have dollar denominated assets. According to recent work by the Bank for International Settlements (BIS), "[a]pproximately half of global trade is invoiced in USD, although this share varies widely across regions". Note that this is not because the US is a trading partner for all this trade – the US only accounts for approximately ten percent of global trade flows.

A number of countries also peg their currency to the dollar, meaning that their central bank intervenes in currency markets to keep the exchange rate between its currency and the dollar at a fixed rate. This brings greater stability to their trade with the United States, since it removes currency risk. A challenge this creates is that in order to maintain the peg, the foreign country usually must also adopt the interest rates of the US Federal Reserve, causing interest rate effects here to be exported abroad.

Even in countries whose currencies are not pegged to the dollar, their companies engaged in international trade for non-US involved transactions may invoice in dollars because they want a currency that is easily converted into their home currency and stores value in the interim. According to that same BIS study, "[a]t least 85% of trading in the spot, forward and swap markets features the USD in one leg of the transactions." Our financial markets, including for foreign exchange, are the most liquid markets in the world, meaning that transactions are implemented at low cost with fast execution and minimal price impact. Thus, part of maintaining our role as the world's most transacted currency means keeping our markets open and easily accessible with ongoing improvements in technology that speeds order implementation while safeguarding against cybersecurity threats.

Arguably more important, the demand for dollar denominated trading arises because the value of the dollar has historically remained strong and stable over time. This is where fiscal and monetary policy play key roles. When economic growth is robust and domestic inflation is both low and consistent, the US dollar is stronger and less volatile, thus serving the important second role of money – as a store of value. However, when growth is stagnant and price increases are larger and more variable, dollar denominated assets do not well serve foreign transactors who are looking to mitigate currency risks in international trade. Therefore, a significant threat to dollar dominance arises from the combination of inflation and anemic growth, which results in too many dollars chasing too few goods and services.

During the COVID-19 pandemic, aggressive fiscal policy was essential to ensure that our nation's families and small businesses survived its devastation. However, by January 2021, the economy had nearly fully recovered from the impact of the pandemic – 84% of the lost output and 57% of the jobs lost from the recession had returned. In addition, three vaccines had been developed and their deployment to the American people was beginning.

Nevertheless, Congress and the Administration enacted an additional $1.9 trillion in federal spending, resulting in the highest inflation our nation has endured in forty years. Former Clinton Treasury Secretary Larry Summers characterized the economic policies of this administration as "the least responsible macroeconomic policies we've had in the last 40 years." Additionally, researchers at the San Francisco Federal Reserve published findings that stated, "Fiscal support measures designed to counteract the severity of the pandemic's economic effect may have contributed to this divergence by raising inflation about 3 percentage points by the end of 2021".

Even last year, well after the pandemic had ended, federal spending was still more than 24% of national output, significantly above the 20.3% average that existed between 1980 and 2019. The result is that the most recent version of the Financial Report of the US Government projects debt to be 566% of national output by the end of its 75-year forecast period, compared to approximately 100% today. These levels of deficits and debt erode confidence around the world that the US will continue being the responsible economic steward that earned us status as the world's reserve currency.

Now is the time for Congress to address our unsustainable federal budget. Given the recent, outsized role of the federal government in our economy, growth between Q4 2021 and 2022 was an anemic 0.9%. Inflation is still well above the Federal Reserve's two percent target such that the FOMC is considering further interest rate hikes. These inflation-induced interest rates have resulted in the second, third, and fourth largest bank failures in US history. The Index of Leading Indicators is in recession territory and the staff of the Federal Reserve is predicting a recession.

Yet the President insists on throwing more gasoline on the stagflation fire. Washington directed spending that replaces low-cost, reliable sources of energy with high-cost, unreliable sources of energy simultaneously causes inflation and contraction. The regulatory onslaught of this administration is estimated to have added 231 million paperwork hours and cost our economy $368 billion, again raising prices and lowering output.

We must stop expecting the Federal Reserve alone to mitigate the inflationary impacts of fiscal and regulatory policy. The answer is not higher interest rates that would further undermine the banking system and erode the value of the dollar. Instead, we must reduce federal spending and rescind the regulations that are curtailing economic growth and devaluing the dollar. The Federal Reserve needs help from the Congress and the Administration if it is going to get us back to economic growth, price stability, and dollar dominance.

Continuing our existing fiscal policies will ultimately cause a bond market failure, irrespective of the actions of the Federal Reserve. The US economy can manage the current debt to GDP ratio but there is no consensus among economists on how much further we can viably indebt our nation. On our current path, the forecasted debt level and accompanying money printing will eventually create a crisis of confidence. Fewer international transactions will be traded in dollars. Foreign central banks will further reduce their holdings of dollar-denominated securities, causing interest rates to skyrocket and a loss of dollar dominance in international trade.

Policymakers must return to the responsible fiscal stewardship that made the U.S. the premier economic and financial nation in the world. We must return spending to its historical levels and not crowd out the private sector ingenuity and dynamism that ultimately improves standards of living for our fellow citizens. The American people deserve the opportunity to once again realize the shared prosperity that comes from greater economic growth with low inflation, higher wages, and more control over their own lives. Policies that continue dollar dominance contribute to realizing those outcomes.

I look forward to participating in this important conversation.