US dollar explainer

What a weaker dollar means for investors

August 2025

US dollar under pressure

World's reserve currency is facing headwinds

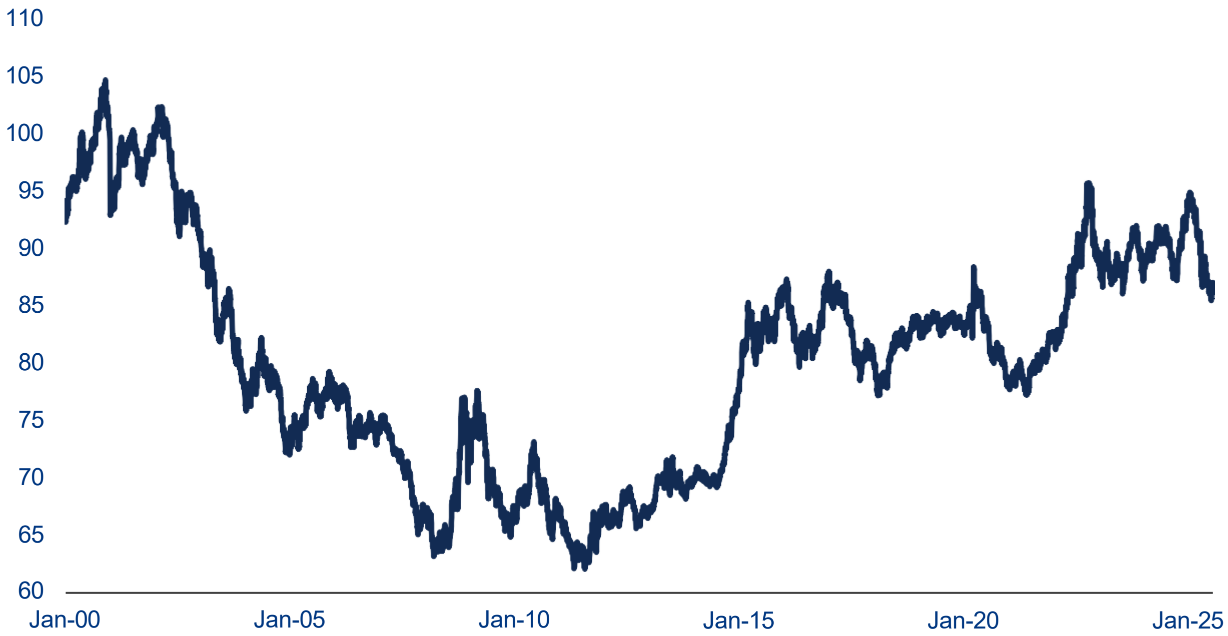
- Long considered a safe-haven and a symbol of US financial dominance, the dollar's status is starting to be questioned.
- After many years of impressive gains, the currency has come under significant pressure so far in 2025.
- The dollar has lost more than 7% of its value against a broad basket of its trading partners.* Compare its fate with the euro, which has appreciated by 12%.

US dollar accounts for nearly

60% of global foreign exchange reserves**

Dollar at its lowest level since 2022

US dollar trade weighted index



Source: Bloomberg. Data as at 16 July 2025.

*As of 16 July 2025. **According to IMF data up to the end of 2024.

Allianz Global Investors

What is pushing the dollar lower?

We see several factors contributing to the dollar's slide:

1. Weaker growth

- Dollar strength since the 2008 financial crisis was built on the US economy performing better than other countries.
- But US growth contracted in Q1 2025.
- Imports surged as companies bought foreign goods ahead of the onset of US tariffs.
- However, setting aside these short-term dynamics, the underlying pace of consumer demand appears to be softening while inflationary pressures have risen. This increases the risk of stagflation or recession ahead.

2. Less friendly US policy

- The US administration thinks a weaker dollar would benefit US manufacturing – other nations could buy US goods more cheaply.
- New policies on trade and immigration have also contributed to investor uncertainty about the US outlook.

The One Big Beautiful Bill Act may swell the US budget deficit to around

USD 2.5 trillion

by 2034*

3. Tarnished safe-haven value

- In the past, the dollar and US Treasuries protected portfolios during equity market downturns by rising in value. But that did not happen during the equity market sell-off post "liberation day" in April 2025.
- Instead, the dollar and longer-dated Treasuries also fell, prompting many non-US investors to add additional currency hedging on their US exposure.

*Source: Committee for a Responsible Federal Budget

What does a weaker dollar mean for markets?

The dollar holds significant sway in markets, influencing economic performance, return expectations, valuations and currency risk.

Upside

- Periods of dollar weakness have often been associated with cyclical recoveries in the global economy. For non-US companies and countries dependent on US capital markets, it is easier to raise capital when the dollar is weaker because their assets are valued more highly.
- A lower dollar also makes it easier for countries with high exposure to the US to lower interest rates. Asian countries may benefit as lower domestic rates can boost growth.

Downside

- The high weight of US assets in many investor portfolios means a declining dollar can act as a drag on performance. Currency hedging costs for portfolios may rise.
- Investors may need to actively consider greater diversification, something that has been challenging as performance has been concentrated among a small group of leaders in equity markets.
- A weaker dollar can make imports to the US more expensive, potentially raising prices. This can make it more challenging for the US Federal Reserve to cut interest rates.

USD 26 trillion

= foreign ownership of US dollar assets*

*Source: US Federal Reserve, 30 June 2024.

Looking ahead, what is the outlook for the dollar?

The dollar is still overvalued and we anticipate a decline in value against major peers over the medium term.

We expect the euro to trend higher against the dollar, with 1.20 the first target. We see two factors supporting our outlook:

1. European strength

- Plans for increased government spending by new German Chancellor Friedrich Merz have served to boost growth expectations in the euro area (versus a deteriorating picture in the US).
- In the longer term, the prospect of higher defence spending may also further support the euro, via stronger growth and improved investor confidence.

2. US uncertainty

- Do not write off the US: its tech leadership makes it a portfolio staple and it remains an unparalleled place to do business. The US's currently higher interest rates (versus other G10 countries) should support the dollar.
- However, the value of these higher interest rates may be undermined by frequent attacks on the Federal Reserve's independence by US President Donald Trump, who is pushing for lower rates.

Where should I invest when the dollar is weaker?

Given prevailing dollar weakness, we see opportunities across asset classes*:

Equities	**Emerging market equities** are aided by strong momentum and solid fundamentals helped by a weaker US dollar, improved earnings prospects and supportive policy conditions.
Fixed income	We maintain a preference for **euro zone sovereign bonds** over US Treasuries, helped by weaker inflation and the asset class's emerging safe-haven appeal.
Currencies	US dollar fragility is still the dominant theme in currency markets. **We stay positive on the euro and the Japanese yen**, benefitting from dollar weakness and supportive fundamentals.
Commodities	**Gold** has reached record highs, and we think it will continue to receive a boost from a weaker dollar and strong buying from central banks.

The US's investment case remains strong: Investors can't avoid the US. A high return on capital, AI leadership, favourable demographics and huge economy make the US an integral part of many portfolios. But for non-US investors, declines in the dollar can put pressure on holdings weighted in the currency, affecting the overall portfolio value. Investors can consider managing these risks by hedging their dollar exposure.

*As of July 2025.

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