

Global Rates and FX Viewpoint

De-dollarisation: Fire sale?

De-dollarisation: is this the moment?

- Weaker USD and the “fire sale” in UST’s is placing the focus back on the role of USD as the global reserve currency. We look at the latest IMF COFER data.
- Drivers: US twin deficits; inflation; higher US rates; trade uncertainty & bifurcation are combining to undermine USD reserve status.
- De-dollarisation extends beyond just reserve manager flows. Global payments system continues to dominate trade flows despite emergence of alternatives.

In this rapidly changing global environment, investors have begun to refocus on the role of USD. Our primary source has traditionally been the IMF COFER data, but events are overtaking the data which is not capturing the current zeitgeist. Whilst there has been some evidence of a shift away from USD in recent year, it is important to remember that this has taken place against the backdrop of US exceptionalism and strong gains in USD. Now, with the aura of invincibility having been shattered, question marks are once again being raised on the viability of the USD as a reserve currency. Bottom line: evidence of accelerated de-dollarisation supports our structurally bearish view on USD. (Kamal Sharma)

USTs: limited net buying by CBs in past year.

The Mar-a-Lago accord (MLA) argues for coordinated USD de-valuation to improve US manufacturing competitiveness + simultaneous terming out of UST reserve assets (to avoid higher tariffs & ensure US national security benefits). MLA policy implementation would result in lower US rates, a steeper UST curve, & cheaper long-dated UST bonds vs the OIS path. We assign low probability to MLA implementation, but it carries large downside risk for UST reserve manager demand. (Mark Cabana)

EUR bonds: conditions in place to increasingly benefit.

The three technical factors that have constrained reserve managers’ EUR allocation over the past fifteen years are now no longer there (sovereign crisis, negative rates and limited free float). The EUR is in a good position to fully benefit a reduction in USD dominance in trade flows, international payments, and/or FX turnovers. If the share of EUR reserves were to be increased to 25% (2011-12 levels) over four years, it would imply that reserve managers could absorb 20% of yearly net supply in EGB space. (Sphia Salim)

Gold: optimal allocation suggests additional CB buying

Continued buying suggests correlations changed. Scope for more given what central bank reserve managers are saying plus the fact that from an optimal asset allocation, exposure to Gold should be higher. The motivation of individual central banks for owning gold may vary, but many reserve portfolios have one thing in common: de-dollarization has been a common tenor. (Michael Widmer)

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Rates and FX Research
Global

Kamal Sharma
FX Strategist
MLI (UK)
+44 20 7996 4855
ksharma32@bofa.com

Sphia Salim
Rates Strategist
MLI (UK)
+44 20 7996 2227
sphia.salim@bofa.com

Mark Cabana, CFA
Rates Strategist
BofAS
+1 646 743 7013
mark.cabana@bofa.com

Alex Cohen, CFA
FX Strategist
BofAS
+1 646 743 7015
alex.cohen2@bofa.com

Meghan Swiber, CFA
Rates Strategist
BofAS
+1 646 743 7020
meghan.swiber@bofa.com

Michael Widmer
Commodity Strategist
MLI (UK)
+44 20 7996 0694
michael.widmer@bofa.com

See Team Page for List of Analysts

Glossary

BRIC: Brazil, Russia, India, China
CB: central bank
CPIS: Coordinated Portfolio Investment Survey
ECB: European Central Bank
IMF: International Monetary Fund
MLA: Mar-a-Lago accord
OIS: Overnight Indexed Swaps
OTC: Over the counter
PBoC: People’s Bank of China
QT: Quantitative Tightening
UST: US Treasury

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Cracks in USD Exceptionalism

Kamal Sharma

MLI (UK)

ksharma32@bofa.com

Sphia Salim

MLI (UK)

sphia.salim@bofa.com

The de-dollarisation thesis has played an important role in our research on reserve manager behaviour in recent years. Whilst the topic has important long-run implications for the role of USD as the world's major reserve currency, it has only intermittently piqued market interest. However, against the backdrop of various macro and geopolitical crosscurrents, the status of USD as the world's reserve currency is back on the agenda. The current tumult in FX and fixed income markets and the evolving nature of the USD-UST correlation (see: [Liquid Insight: Rhyming FX correlations 08 April 2025](#)) has sharpened the focus on whether the risk-off segment of the "USD-smile" is still valid.

The term "de-dollarisation" has often been (narrowly) used to describe a shift in global reserve manager holdings away from USD towards other currencies/assets. But de-dollarisation is a broader concept which essentially suggests a reduced role for the USD in global transactions – be they financial (cross-border payments; trading exchanges; commodities) or trade (corporate invoicing). So, whilst de-dollarisation is an important discussion point for reserve management, the depth and breadth of moving away from USD as the notional anchor is also significant.

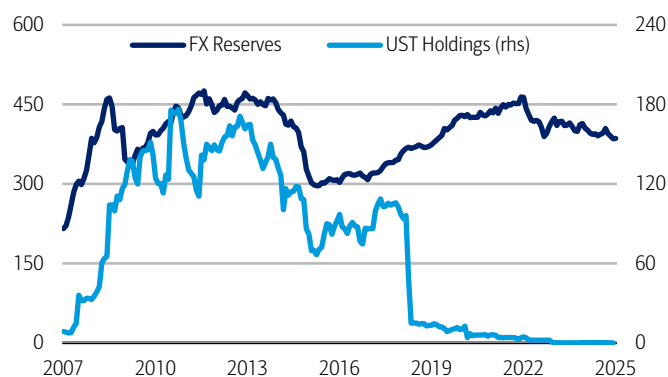
This note is divided into the following sections: firstly, we look at the latest available data on global FX reserve holdings and composition before moving onto analysing a broader set of metrics to assess whether there has been a shift against USD dependency. We then turn to the fixed income markets, highlighting reserve managers activity in UST space and the yet to be seen benefits of "de-dollarisation" for euro-denominated bonds, before concluding by looking at gold which remains the favourite diversifier, creating interesting changes in market correlations.

COFER data – signs of slow grind away from USD

IMF Composition of Foreign Exchange Reserves (COFER) data is commonly held up by markets as the gold standard in gauging the extent to which de-dollarisation is taking place. The composition of FX reserves is seen as key in assessing confidence in the USD.

Exhibit 1: Russia FX Reserves vs UST holdings (\$bn)

Russia divested UST holdings in 2018 and diversified

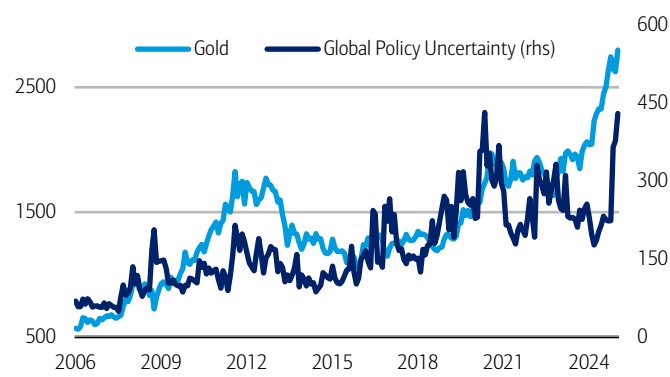


Source: BofA Global Research, Bloomberg

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Exhibit 2: Global Policy Uncertainty vs Gold Price

Rising policy uncertainty has driven higher gold price



Source: BofA Global Research, Bloomberg

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The focus on reserve manager flows has gained renewed focus in recent years for mainly geopolitical reasons and was brought under the spotlight following financial sanctions imposed on Russia and an increasingly bifurcated global trading environment (BRICs nations facilitating payment systems in local currencies rather than USD). The motivations for large reserve shifts are thus for non-altruistic political reasons, driven by



the need to ring fence rather than based on strict economics. Russia's decision in 2018 to divest its US Treasury Holdings is a case in point (Exhibit 1).

Russia provides a valuable insight into the motivations of reserve managers when shifting currency allocations. It underlies the growing importance of factoring geo-political variables such as political uncertainty as critical input into those decisions. We discuss the role of gold in this process in more detail below. We do not think that the rise in gold in recent years alongside rising global policy uncertainty is a coincidence.

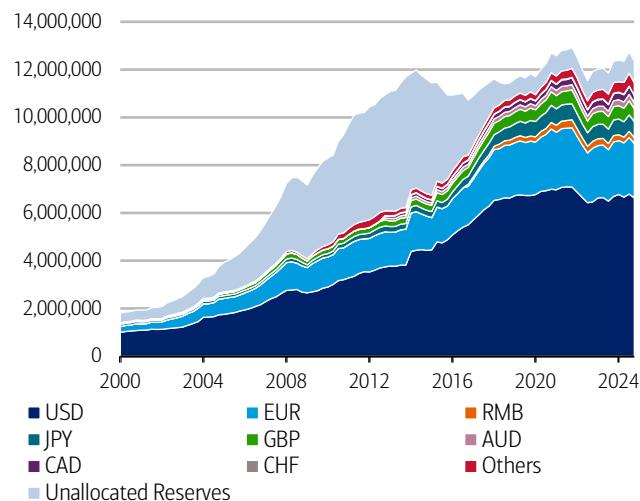
Whilst geo-politics are becoming an increasingly important element in the reserve manager framework, macro considerations are still a significant factor in their reaction function. Our research has increasingly focused on the worrying developments in G10 internal and external balances. In a recent note ([Global Rates and FX Viewpoint: Do twin deficits matter for rates & FX? 17 Feb 25](#)) we address this issue and how it may impact FX/Rates performance. By virtue of its status as the dominant reserve currency and lack of notional fiscal anchor, we think the channel through which there will be an impact on the currency is a correction of the 20%+ overvaluation rather than a regime shift.

Outright look at COFER data suggests USD still dominant...

The broad contours of the latest COFER data from the IMF is presented in Exhibit 3 & Exhibit 4. The headline number, without valuation adjustments (see below) shows that USD dominance remains intact, accounting for over half the total of global FX reserves.

Exhibit 3: IMF composition of foreign exchange reserves (\$)

The value of FX reserves exceeded \$12.5trillion, with over half held in USD

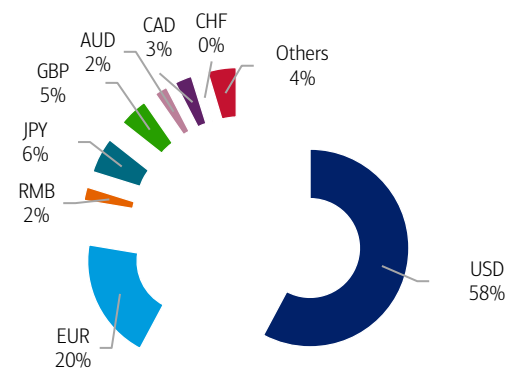


Source: BofA Global Research, Bloomberg, IMF

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Exhibit 4: Current composition of reserve manager holdings (%)

USD retains leading role as world's currency



Source: BofA Global Research, Bloomberg, IMF

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... but a slow & steady de-dollarisation is ongoing ...

Although still dominant, the USD share has been steadily declining over the past decade, from c.66% in early 2015, to less than 58% as of 3Q24 (data for 4Q24 due this month).

More importantly, we believe that the decline in the USD share can't be attributed to a relative depreciation in USD holdings. In fact, we estimate that pure FX, bond & equity valuation adjustments would have taken the USD share higher since 2020 (Exhibit 5).

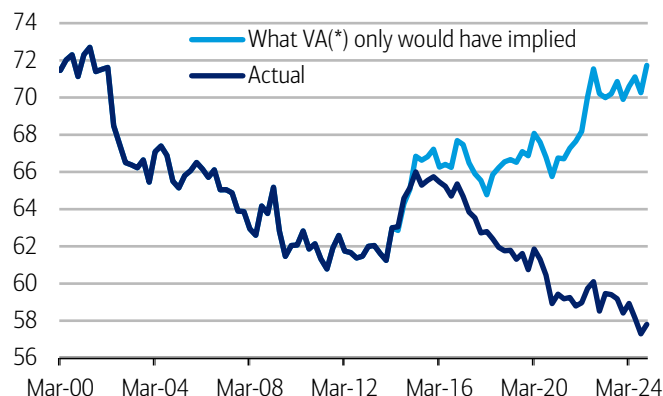
This implies that there was either an active shifts of reserves out of USD into other currencies (ie larger buying in other currencies), or periods of greater net selling of USD reserves in either processes of FX interventions or diversification into gold.

We acknowledge that these estimates are based on many assumptions regarding the breakdown of FX holdings by type. We show most recent ones in Exhibit 6. They are mostly based on estimates derived from the IMF's Coordinated Portfolio Investment Survey (CPIS), which breaks down reserve managers' exposures to different economies

by type of assets. To illustrate the effect of these assumptions: If, for example, USD holdings of cash were lower than we assumed in 2021, then the selloff in bonds would have had a greater (negative) impact on the implied VA share of USD.

Exhibit 5: USD share in COFER's allocated reserve portfolio

FX, bond & equity valuation adjustments alone would have raised USD share



Source: BofA Global Research, IMF. VA = BofA estimates for Valuation adjustments since 2Q14
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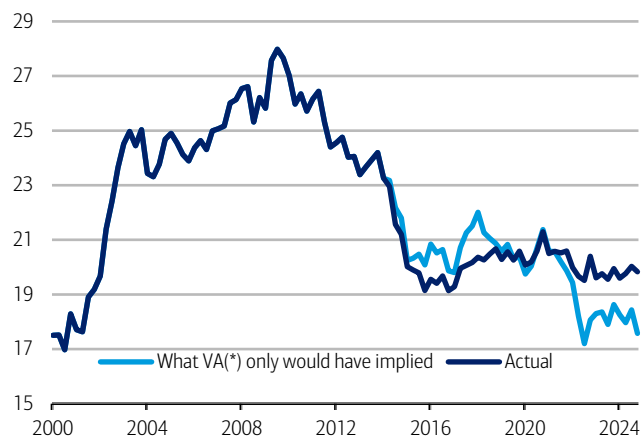
EUR and GBP saw modest benefits from de-dollarisation...

Much analysis has been devoted to the question of an alternative to the USD's reserve status, not least by the IMF themselves¹. The key point to much of this analysis is as follows: whilst there has been an erosion in the USD's status as a reserve currency, this has had limited benefits for the other two "core" reserve currencies next in line:

- EUR holdings have remained relatively stable around 20% (Exhibit 7).
- GBP failed to maintain its third position in the list of allocated FX reserves, as its share increased only marginally from 4.5% to 5% while JPY share rose (Exhibit 8).

Exhibit 7: EUR share in COFER's allocated reserve portfolio

Besides resilience in 2022, EUR share moved roughly inline with VAs



Source: BofA Global Research, IMF. (*) VA = BofA estimates for Valuation adjustments since 2Q14
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Valuation adjusted (VA) data paints roughly a similar picture. The jump in the GBP share relative to what VAs would have implied in 2015 may be due to a large move of reported reserves out of the un-allocated bucket. It's in 2022 that we find some resilience in the EUR and GBP allocation, when the strength of the USD would have naturally driven a rise in USD share vs drop in EUR and GBP shares. The "resilience" could be the result of

Exhibit 6: BofA assumptions made on the composition of FX reserves. Used to estimate valuation adjustments from one quarter to the other

Assumptions for 2024. We mainly use CPIS data as ref for debt securities

	USD	EUR	RMB	JPY	GBP	AUD	CAD	CHF
Deposits				7-17%				0-20%
Equities & investment fund shares				3-13%				20-40%
Debt securities				80%				60%

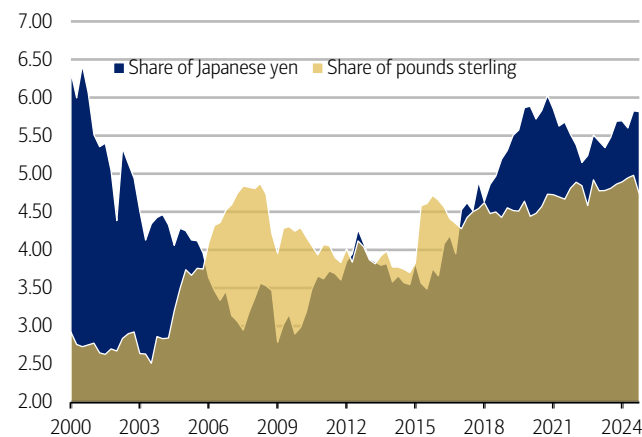
% of Debt securities, that are <1y (3Q24)	10%	11%	32%	44%	12%	4%	14%	90%
% of Debt securities, that are >1y (3Q24)	90%	89%	68%	56%	88%	96%	86%	10%
Bond index used for price chgs in >1y debt	GOQ0	EG00	GOCN	G0Y0	G0L0	G0T0	G0C0	G0S0

Source: BofA Global Research, IMF CPIS

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Exhibit 8: GBP and JPY battling for 3rd position in FX reserve shares

GBP share increased only marginally while JPY share to early 2000s levels



Source: BofA Global Research, IMF COFER

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¹ Dollar Dominance in the International Reserve System: An Update (Serkan Arslanalp, Barry Eichengreen, Chima Simpson-Bell, June 2024).



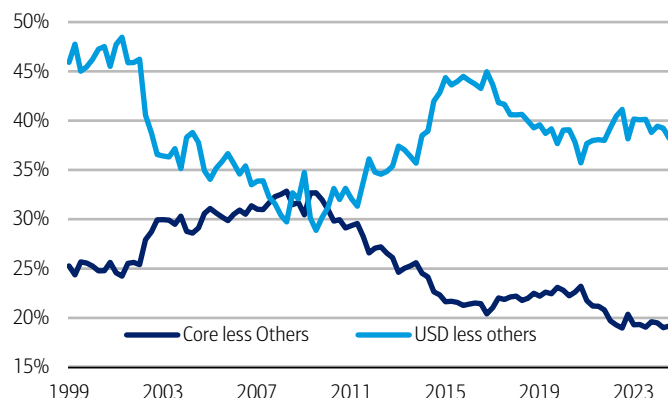
reserve managers rebalancing their portfolio and/or FX intervention centred on USD selling. But aside from 2022, the evolution of the EUR share appear relatively consistent with what VAs would have implied, ie no active shift into EUR reserves.

... but de-dollarisation has benefited other currencies

The reserve shift suggests a greater degree of diversification across more currencies than a concentration amongst traditional core reserves. Allocations towards non-core reserve currencies rose almost in lockstep with the decline in USD holdings (Exhibit 10).

Exhibit 9: “Other” Currencies vs USD and Core

Rise in other currencies comes at the expense of core & not USD

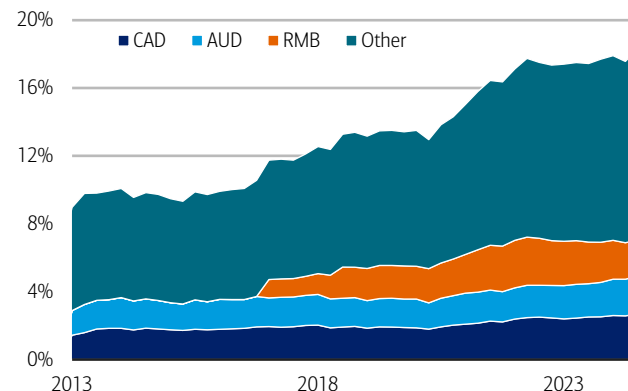


Source: BofA Global Research, Bloomberg

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Exhibit 10: COFER holdings of “other currencies”.

“Other” currencies have benefited from the fall in USD holdings.



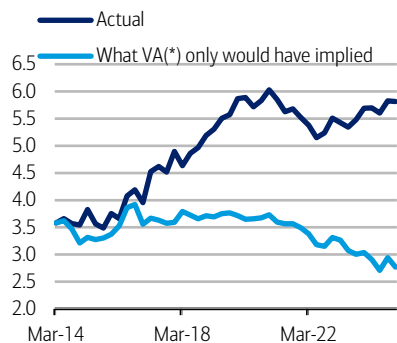
Source: BofA Global Research, Bloomberg, IMF

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The “other currencies” include KRW and Scandinavian currencies, which have risen in prominence due to improved liquidity conditions in local markets. But we also note that the share of JPY, CAD and AUD all increased by more than pure valuation adjustments would have implied (Exhibit 11 to Exhibit 13).

Exhibit 11: JPY share in allocated reserves

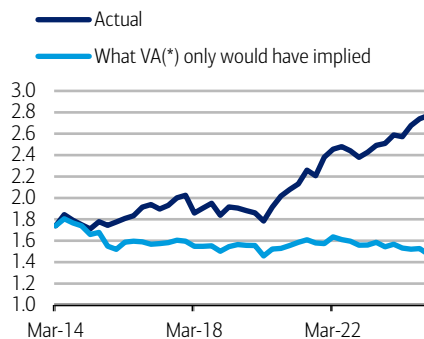
Share of JPY increased beyond what VA implied



Source: BofA Global Research, IMF COFER. (*) VA = BofA estimates for valuation adjustments, BofA est. since 2Q14
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Exhibit 12: CAD share in allocated reserves

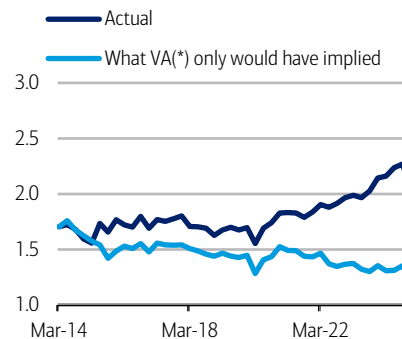
Share of CAD increased beyond what VA implied



Source: BofA Global Research, IMF COFER. (*) VA = BofA estimates for valuation adjustments, BofA est. since 2Q14
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Exhibit 13: AUD share in allocated reserves

Share of AUD increased beyond what VA implied



Source: BofA Global Research, IMF COFER. (*) VA = BofA estimates for valuation adjustments, BofA est. since 2Q14
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IMF COFER data shows some evidence of a shift away from USD, and one that could accelerate against the backdrop of geopolitical risks which weaponise the USD. So far, traditional reserve currencies have not been the main beneficiaries of the shift away from USD. Reserve managers appear to have diversified into a broader set of currencies as liquidity improves in their respective markets. If de-globalisation and trade bifurcation are the direction of travel, the evolution of trade

relationships built away from the US can play a key role in the composition of reserves. We believe conditions are in place for the EUR to start benefiting more.

Is COFER the final word on de-dollarisation?

The simple answer to the question is no. COFER data does not provide the complete picture on whether a regime shift is underway. COFER data remains backward looking and the composition of reserves may be driven by mutually exclusive factors compared to payments and trade factors. However, changes to payments and trade factors can impact (decisions on) future FX reserve composition.

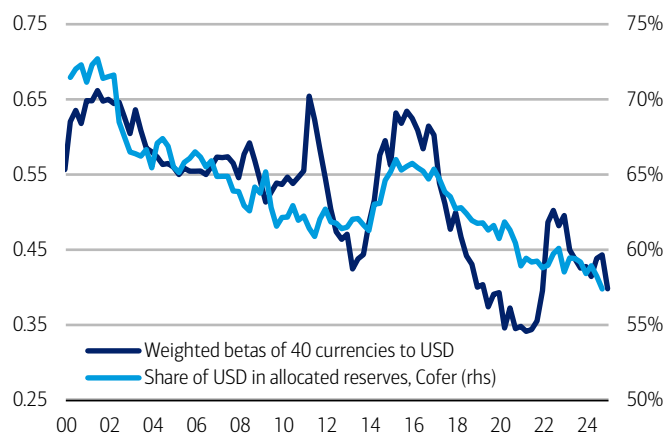
We have seen over the past 5-10y a decline in the weighted beta of global currencies to the USD, indicating less reliance on USD, which in itself can explain developments in the COFER data (Exhibit 14). However, there is little evidence, so far, of a major change in the microstructure of trade finance and payments channels. Those continue to be dominated by the USD.

Though payments and trade finance channels may not attract the same headline noise as COFER for the investment community, we think this is a significant factor in assessing if there has been a step shift away from the USD. Recent efforts by the BRICS economies to create an alternative payments platform hint at further weaponisation of USD via the payments channel (BRICS PAY).

Whilst USD dominates as the global payments currency of choice, the rise in CNY payments in over the last 10yrs is noteworthy. We present our findings in Exhibit 15 using data provided by SWIFT. "Other currencies" flagged above have also gained increased prominence such as SGD, PLN and HKD. GBP payments have declined perhaps against the backdrop of Brexit. Note that we have excluded EUR payments flows due to infrastructure changes in payments processes.²

Exhibit 14: Weighted beta estimate of global FX correlation to USD.

Global dependence on USD has been declining

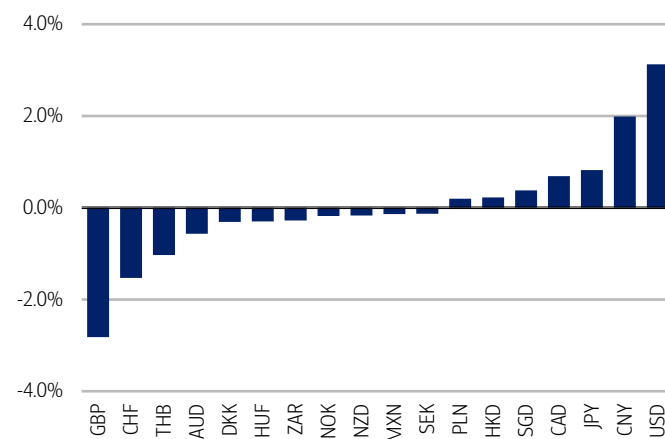


Source: BofA Global Research, Bloomberg

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Exhibit 15: Change in global payments currencies 2015-2025.

USD payments share increased, but CNY share has risen from low levels.



Source: BofA Global Research, Bloomberg, SWIFT

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² The euro as a global currency: a payments perspective; ECB Economic Bulletin, Issue 2/2024



US rates

Mark Cabana, CFA

BofAS

mark.cabana@bofa.com

Meghan Swiber, CFA

BofAS

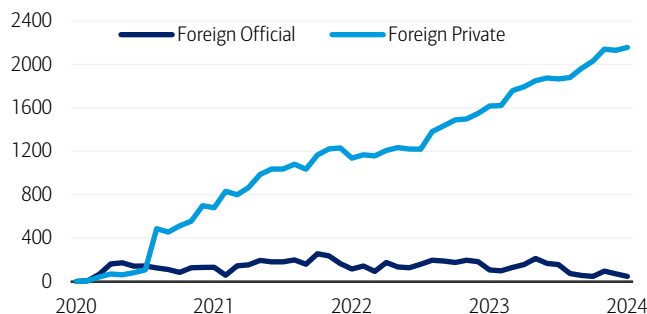
meghan.swiber@bofa.com

Limited UST demand from foreign officials

Another area to see reduced support for official UST holdings is in the Treasury TIC data. TIC data continues to show a steady divergence between foreign official and private demand for UST post-pandemic. Foreign official demand remains weak with \$60bn outflows in 2024 and \$24bn selling in Dec '24 (Exhibit 16).

Exhibit 16: Cumulative UST flows from foreign investors (\$bn)

Foreign private buying far outpaced official sector who has turned net seller

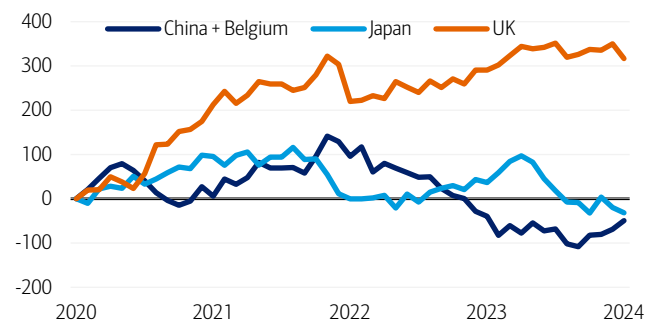


BofA Global Research, Bloomberg, TIC, note: references the valuation-adjusted flow

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Exhibit 17: Cumulative UST flows from foreign investors (\$bn)

China + Belgium have turned to net sellers since end of 2022, Japan is a net UST seller; UK also saw UST selling in Dec



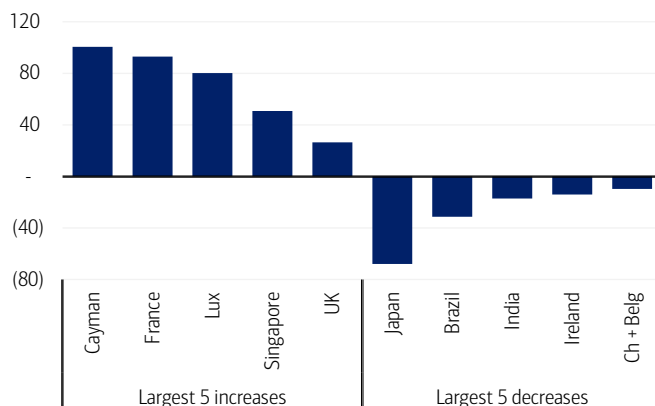
Source: BofA Global Research, Bloomberg, TIC, note: references the valuation-adjusted flow

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Looking at the flows in 2024, we find that the largest buying of USTs came from Cayman Island and Luxembourg (Exhibit 18). These suggest hedge fund basis trades remain active and that private sector UST demand has been largely driven by leveraged funds activity rather than official reserve accumulation. Japan stands out in TIC data with large UST selling flows since Jul '24 and a \$68bn reduction in UST holdings in 2024. This contrasts with data from Japan's MoF showing large buying of USTs by private Japanese investors (c.\$90bn in 2024). BoJ FX intervention could be part of the explanation.

Exhibit 18: Largest change in UST holdings by country in 2024(\$bn)

Cayman, France & Lux largest buyers while Japan was the largest seller in

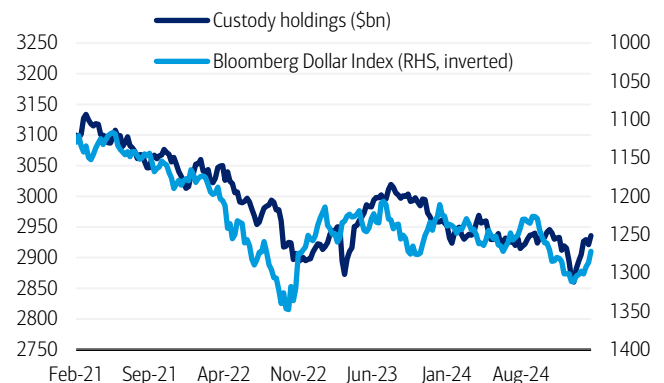


Source: BofA Global Research, Bloomberg, TIC

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Exhibit 19: Weekly UST custody holdings, foreign official (\$bn)

Custody holdings unchanged on the week



Source: BofA Global Research, NY Fed

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More generally, we believe that official investors have been net sellers in recent years in big part due to US dollar strength (Exhibit 19). Any renewed USD appreciation pressures can see foreign official demand weaken further.



Another headwind for official sector demand is more aggressive trade policy under the Trump administration. As shown in Exhibit 20 sharp selling pressures from China occurred during the second part of Trump's first term when trade policy & tariffs became more of a focus. The most aggressive selling occurred between July '18 and December '19 when the DXY traded within a 1% range. Beyond USD appreciation, more hawkish trade policy could support selling from the official sector.

Exhibit 20: Mentions of "trade" in Fed Beige book and change in China + Belgium UST holdings

As trade policy became more aggressive during Trump's first term, China sold more UST holdings

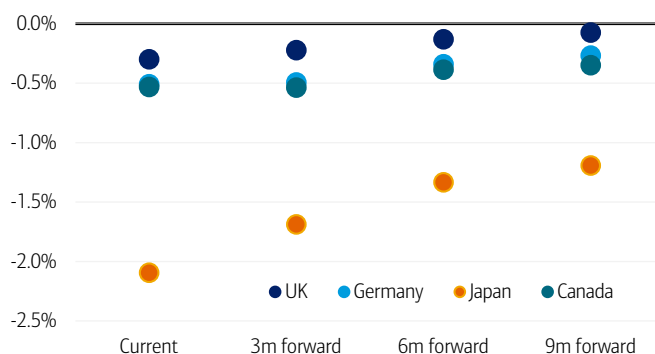


Source: BofA Global Research, Federal Reserve, TIC

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Exhibit 21: FX hedged pickup of TSYs versus local alternatives implied by forwards

Market pricing suggests relatively flat pickup for UK, German, and Canadian investors but deeply negative for Japan



Source: BofA Global Research, Bloomberg. Note: pickup vs 10y local alternative except Japan which is relative to 20y JGB using 3m forward FX hedge

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Tariffs risk worsening foreign bid.

Tariffs and more hawkish trade policy support incremental risks to the foreign bid. The uptick of trade concerns in Trump's first term coincided with China selling UST holdings (Exhibit 20). The most aggressive selling occurred between July '18 – December '19 when the DXY traded within a 1% range so was unlikely related to rebalancing flows. If tariff policy does help to close the trade deficit as intended, this also reduces the need for foreign buyers to allocate towards USD assets like Treasuries. While the relationship is relatively weak, periods of a narrower trade deficit have often occurred alongside foreign selling/ more modest buying (Exhibit 23).

Exhibit 22: Mentions of "trade" in Fed Beige book and change in China + Belgium UST holdings

As trade policy became more aggressive during Trump's first term, China sold more UST holdings

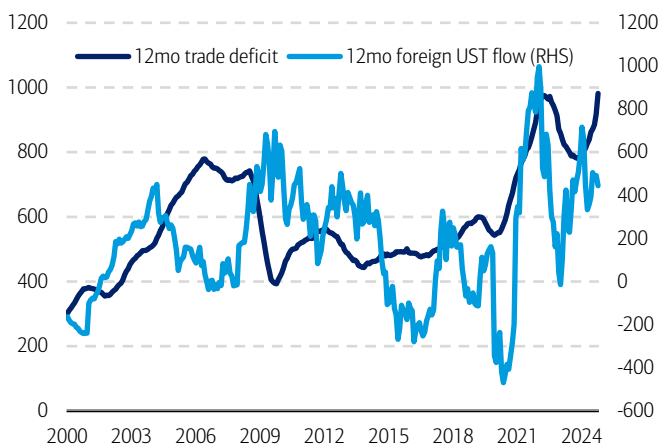


Source: BofA Global Research, Federal Reserve, TIC

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Exhibit 23: Trade deficit and foreign UST flow (\$bn)

Not a strong relationship, but periods of lower deficit have corresponded with less foreign demand



Source: BofA Global Research, Bloomberg

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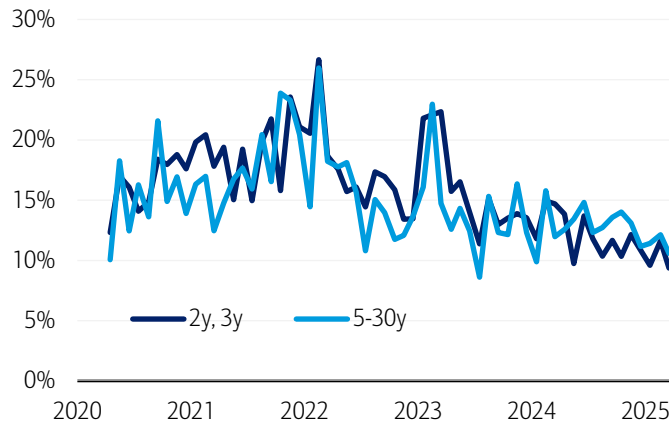


Foreign investors show low auction participation.

Demand shifts are particularly in focus alongside this week's auction calendar. Treasury data has shown a continued reduction in foreign participation in auctions over recent years with investment funds largely closing the gap (Exhibit 24 and Exhibit 25).

Exhibit 24: Avg foreign investment at auction (all nominal coupons)

Participation has decreased to around 10%

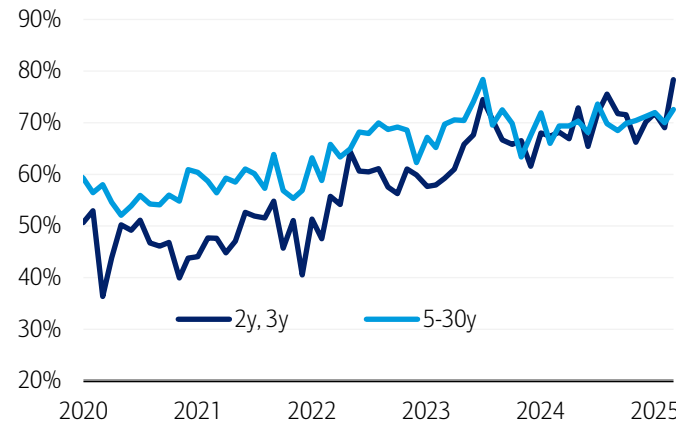


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Exhibit 25: Investment fund – average auction allotment

Participation has increased to around 75%



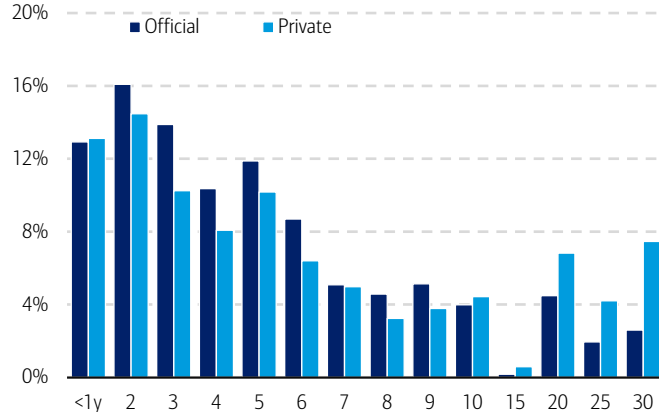
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If foreign investors were to pullback further, this effect may be more dominant across tenors at the front end and belly of the curve where foreign holdings are concentrated (Exhibit 26).

Exhibit 26: Maturity distribution of foreign Treasury holdings (years)

Official WAM of holdings is about 5.5y, private WAM is around 7y

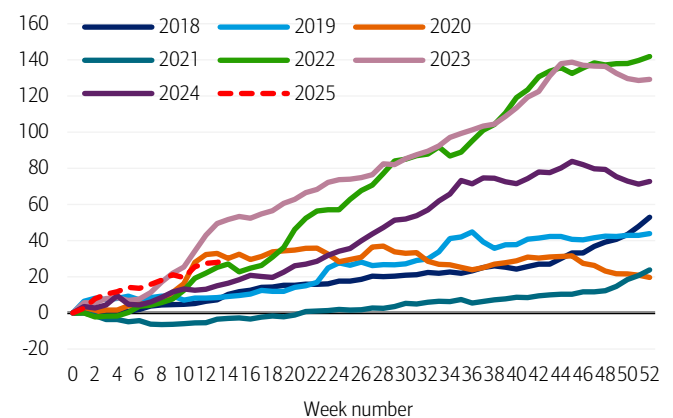


Source: BofA Global Research, US Treasury

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Exhibit 27: Sovereign fund inflows by year (\$bn)

2025 inflows trending higher than most years ex '20 and '23



BofA Global Research, EPFR

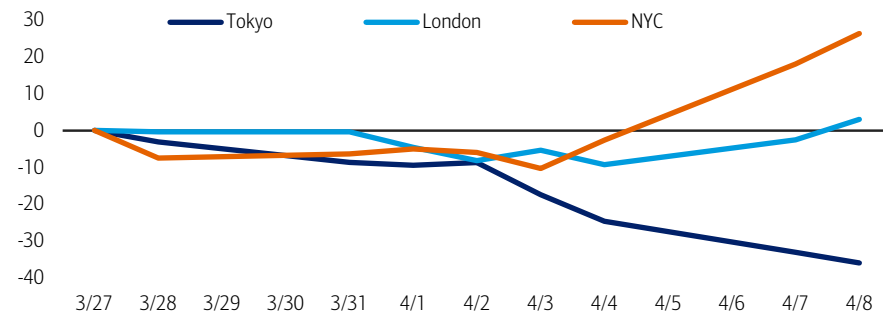
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Foreign investors unlikely to be only seller

We are receiving questions on potential foreign investors selling being behind the sudden reversal and rise in UST yields on Apr 7-9. We believe foreign investors are unlikely the only seller driving recent price action ([Confidence test for treasury buyers, 9-Apr](#)). In fact, treasuries have largely rallied in Asia sessions since the end of March and selling was concentrated in NY trading hours (Exhibit 28). CNY/ CNH depreciation vs the USD on the week is also inconsistent with reserve manager selling of USTs.

Exhibit 28: Cumulative change in 10y UST yield by trading session

10y has largely rallied in Tokyo session and sold off during NYC trading hours (as of NY close 4/8)



Source: BofA Global Research, Bloomberg; note: assumes 4pm-2am for Tokyo, 2am – 7am for London, 7am – 4pm for NYC.

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Still, we will watch weekly NY Fed custodial holdings for evidence of accelerated foreign investor selling in our weekly flows report (see: [US Rates Watch: Flows](#)).

Other risks to UST reserve demand could come from broader large scale policy changes, such as the Mar-a-Lago accord (MLA). The MLA argues for coordinated USD de-valuation to improve US manufacturing competitiveness + simultaneous terming out of UST reserve assets (to avoid higher tariffs & ensure US national security benefits). On net, we might guess MLA policy implementation would result in lower US rates, a steeper UST curve, & cheaper long-dated UST bonds vs the OIS path. We assign low probability to MLA implementation, but it carries large downside risk for UST reserve manager demand. For detail see: [Mar-a-Lago accord: framing & impact](#).

On the other hand, private foreign demand for USTs will be more of a function of fund inflows & investor duration views vs carry opportunities. Otherwise, FX hedged pickup of USTs is not currently attractive for foreign investors, and forwards do not imply a more favorable dynamic in the months ahead (Exhibit 21).

Overall, we believe that foreign private demand can remain robust as long as fixed income fund inflows remain elevated. We pencil in \$400bn of UST foreign buying in '25. This is a modest cooling from the assumed \$500bn in buying we assumed for 2024 ([UST supply & demand in '25](#)).



EUR bonds: untapped potential

Sphia Salim

MLI (UK)

sphia.salim@bofa.com

Several factors limited scope for significant increase in EUR allocation

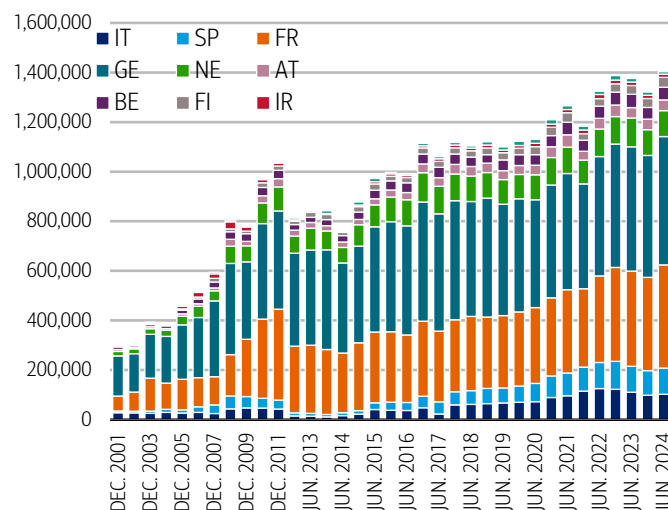
Shortly after its inception, through the Global Financial Crisis, the EUR appeared a clear contender to challenge the USD, with its share of reserves at nearly 30%. The sovereign debt crisis has, however, been a significant roadblock for EUR reserve status and since then, reserve managers have maintained a more limited 20% share of EUR holdings in their portfolios. As a result, it didn't stand out relative to other currencies in the recent de-dollarisation phase, with the share of EUR as % of FX reserves not deviating significantly from what valuation adjustments implied, until very recently.

We believe that the 3 factors have constrained reserve managers in terms of EUR allocation over the past fifteen years:

1. The surge in credit risk in periphery space. This drove a collapse in allocations to Italian and Spanish bonds in 2012-15. However, with the normalisation in spreads, allocations to the periphery have grown back to an even higher share now, according to IMF CPIS data (Exhibit 29),
2. The ECB's negative interest rate policy, with many reserve managers unable to buy negatively yielding bonds. This is now in the past, and, if anything, the most recent price action (US risk-off vs fiscal hopes in Europe) has now taken European yields to historically attractive levels vs USTs (Exhibit 30)
3. The limited availability of EUR-denominated govt bond paper, following the start of ECB Quantitative Easing. This has also fully reversed now as ECB started QT and at the same time deficits remained elevated (Exhibit 31).

Exhibit 29: Debt securities held by official institutions, reported in IMF's CPIS database and adjusted for FX and market valuations (mln €)

Increased holdings of Euro Area debt securities, as overall FX reserves grew

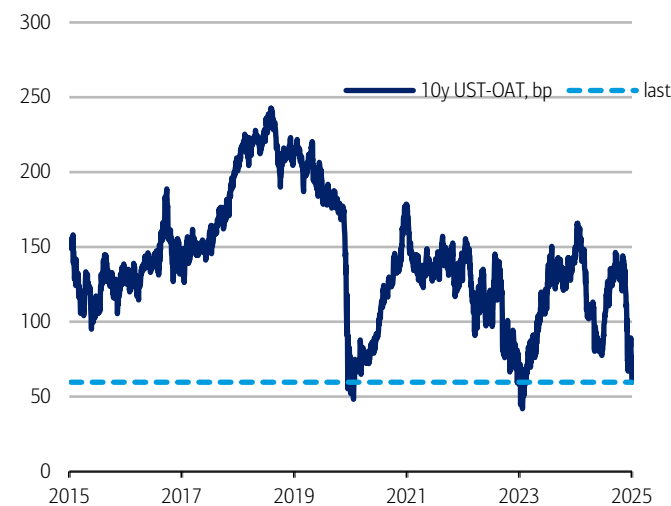


Source: IMF's CPIS database, BofA Global Research Estimates

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Exhibit 30: Yield differential between 10y USTs & 10y French bonds

French yields are around most attractive levels vs UST yields of past 10 years



Source: BofA Global Research. Last as of 4-Apr

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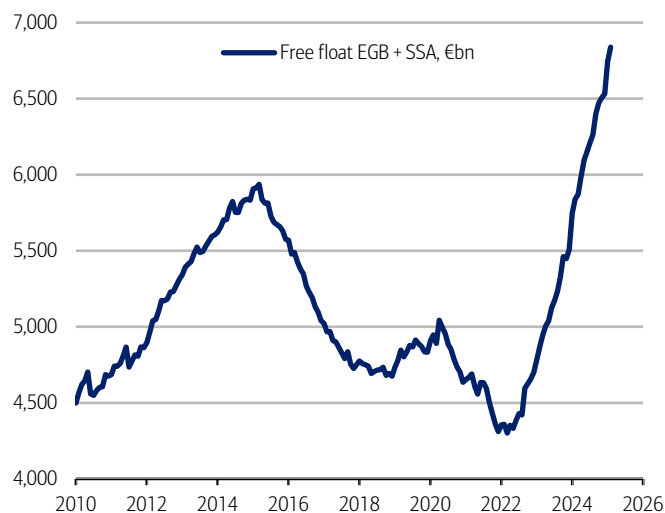
The limited increase in share of EUR holdings despite improvements on three fronts suggests that there is untapped potential. It may be that the improvements on (2) and (3) are too recent, and that the global geopolitical situation has been too uncertain.



However, with geopolitics now moving against increased dependency on the US, and the trade system moving away from US dominance (with scope for increased direct trade links between other markets), the EUR could start to play a greater role in international markets with increased use for trade payment and in foreign exchange turnovers. The fact that the above 3 technical factors acting against the EUR have dissipated means that the bar for this process to translate into higher EUR share in FX reserves is low.

Exhibit 31: Free float of Euro govt & SSA bonds >1y (bn EUR)

The free float in 1y+ bonds (ie amount not held by the ECB) has surged to above 2015 highs, as QT and continued net issuance have offset years of QE.



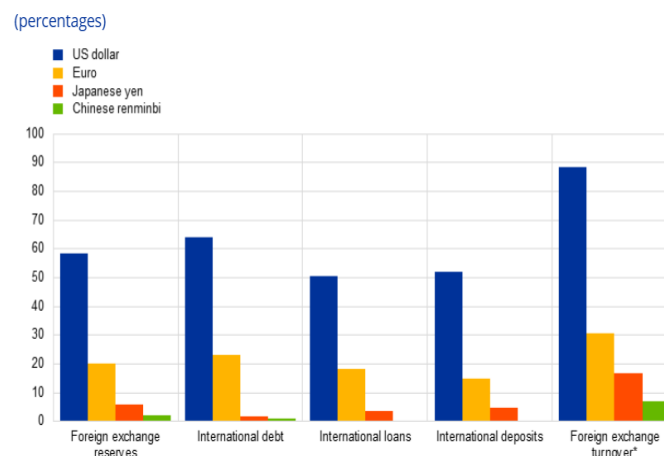
Source: ECB, ICE, BofA Global Research

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Exhibit 32: Relevance of USD, EUR, JPY & RMB in international system

The share of EUR in FX reserves = consistent with that in international debt, deposits and FX turnovers.

Snapshot of the international monetary system



Source: ECB, BIS, IMF, CLS Bank International, Ilzetzki, Reinhart and Rogoff (2019) and ECB calculations. Notes: The latest data on foreign exchange reserves, international debt, international loans and international deposits are for the fourth quarter of 2023. Foreign exchange turnover data as of April 2022. *Since transactions in foreign exchange markets always involve two currencies, foreign exchange turnover shares add up to 200%.

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Lastly, the announcement of a new instrument to European finance defence spending via EU issuance (the SAFE programme) marks another step in establishing EU bonds as a more permanent of the European bond market. Net EU bond issuance for the NGEU programme was going to end after 2026, with bonds being rolled until 2058. Now, with the SAFE programme, net new issuance will extend until 2030, with bonds maturities and refinancing extending potentially to around 2070.

If central banks were to increase the share of EUR holdings back to 25% (around 2011-12 levels), this would imply net flows of c.\$600bn into EUR, out of other currencies, all else equal. Spread over 4 years, this would imply that foreign reserve managers could consistently absorb over 20% of the yearly net supply in Euro Area government bonds.

Gold: the great beneficiary

Michael Widmer

MLI (UK)

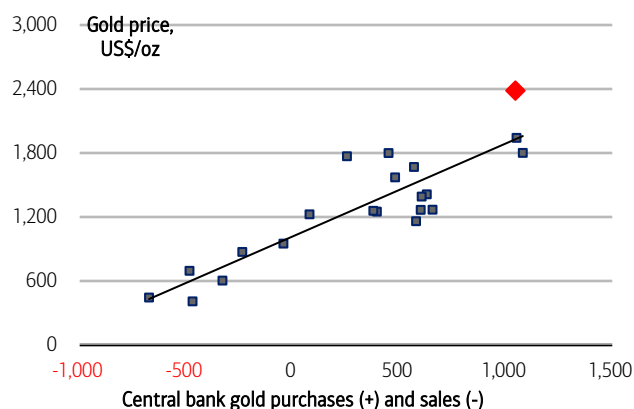
michael.widmer@bofa.com

Record gold demand last year.

The World Gold Council highlights in its gold demand trends for CY2024 that "Total gold demand (including OTC investment) rose 1% y/y in Q4 to reach a new quarterly high and contribute to a record annual total of 4,974t. Central banks continued to hoover up gold at an eye-watering pace: buying exceeded 1,000t for the third year in a row, accelerating sharply in Q4 to 333t (Exhibit 33). Annual investment reached a four-year high of 1,180t (+25%). Gold ETFs had a sizable impact: 2024 marked the first year since 2020 in which holdings were essentially unchanged, in contrast to the heavy outflows of the prior three years", see Exhibit 34.

Exhibit 33: Gold prices and central bank purchases

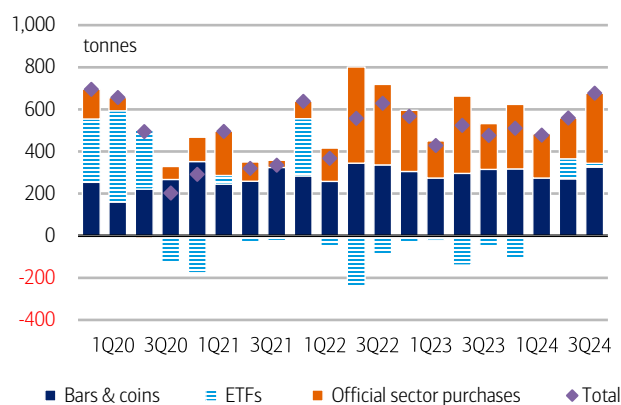
The gold price rally has been accompanied by rising central bank gold purchases



Source: World Gold Council, Bloomberg, BofA Global Research
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Exhibit 34: Breakdown of investment demand

Central banks remain key gold market participants

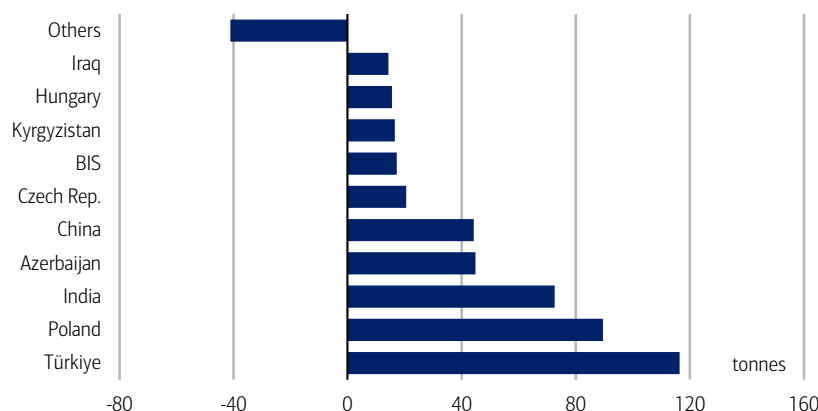


Source: World Gold Council, Bloomberg, BofA Global Research
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Exhibit 35 illustrates central-bank gold activity, showing that purchases have come through from a range of reserve managers in the past year. We expect steady buying from monetary authorities also this year, although there are concerns that purchases may weaken somewhat after a phenomenal 2024.

Exhibit 35: Central bank gold purchases in the past year

Reserve managers in Europe and Asia have been key gold buyers



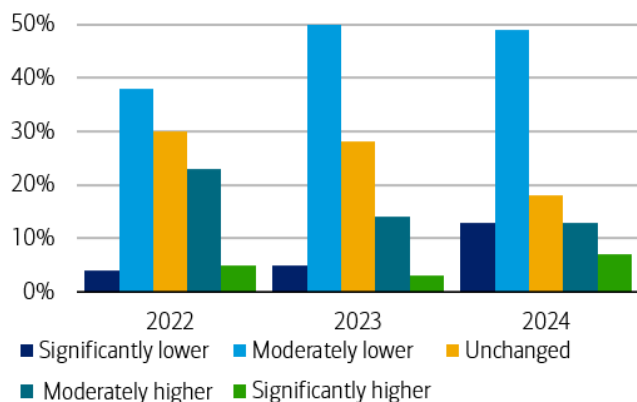
Source: World Gold Council, BofA Global Research
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USD share in reserves falling, concerns over Treasuries**China keeps reducing USD holdings**

The motivation of individual central banks for owning gold may vary, but many reserve portfolios have one thing in common: de-dollarization has been a common tenor, as Exhibit 36 shows. Reflecting this, gold's share in the reserve portfolios is set to rise (Exhibit 37).

Exhibit 36: What proportion of total reserves (foreign exchange and gold) do you think will be denominated in US dollars 5 years from now? (2022-2024 responses shown)

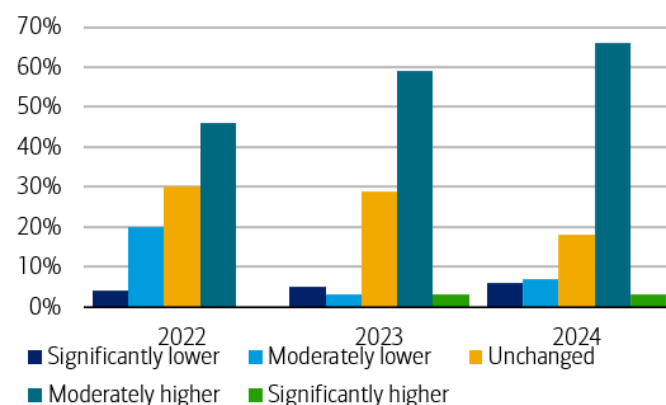
Central Banks expect USD reserves to decline further



Source: World Gold Council, BofA Global Research
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Exhibit 37: What proportion of total reserves (foreign exchange and gold) do you think will be denominated in gold 5 years from now? (2022-2024 responses shown)

Central Banks see gold holdings increasing



Source: World Gold Council, BofA Global Research
BofA GLOBAL RESEARCH

China has been one of the biggest official gold buyers in recent years. Indeed, while the share of USD in its portfolio has declined (Exhibit 38), the PBoC has steadily diversified its reserves, lifting the share of the yellow metal in total reserves to 5.5% in 4Q24 (Exhibit 39).



Exhibit 38: China, USD of foreign exchange reserves

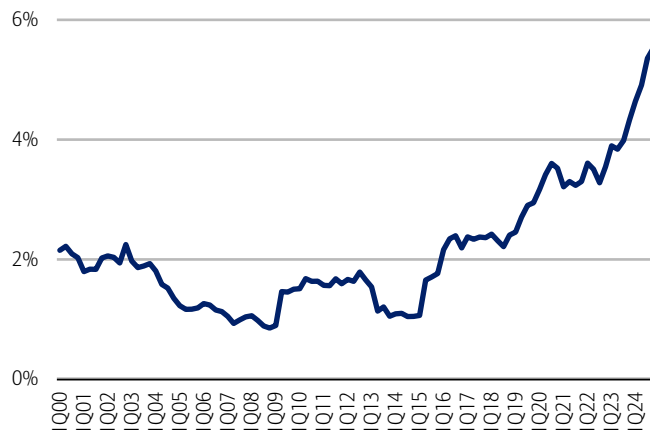
The share of USD in China's foreign exchange reserves has declined



Source: Bloomberg, BofA Global Research
BofA GLOBAL RESEARCH

Exhibit 39: China, gold of total FX reserves

China has increased the share of gold in its reserves

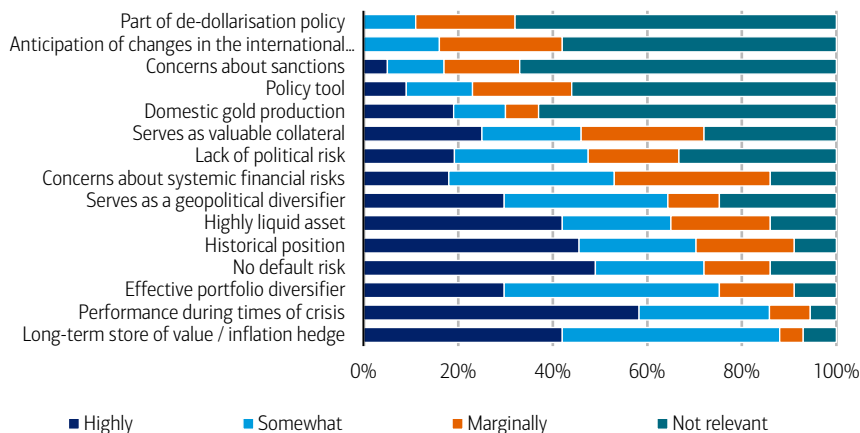


Source: World Gold Council, BofA Global Research
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What other motives make gold attractive as a reserve asset? The World Gold Council outlines that 83% of central banks hold gold as part of their total international reserves. While in prior years, gold's "historical position" was the top reason for central banks to own it, it dropped to number five in the most recent survey. Meanwhile, the top reason for central banks to own gold is "long-term store of value / inflation hedge" (88%), followed by "performance during times of crisis" (82%), "effective portfolio diversifier" (75%) and "no default risk" (72%).

Exhibit 40: How relevant are the following factors in your organization's decision to hold gold?

When it comes to gold holdings, long-term store of value / inflation hedge, performance during times of crisis and effective portfolio diversifier all matter



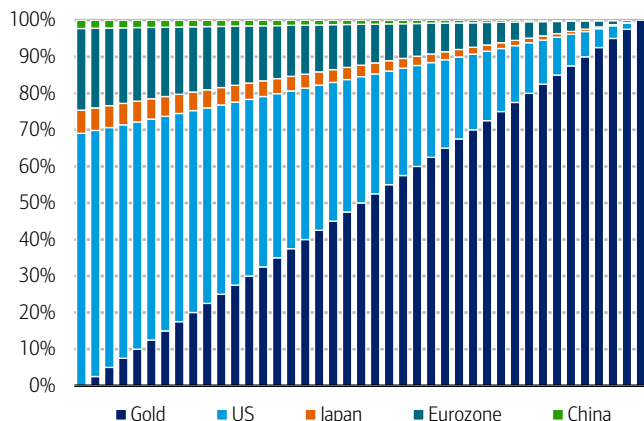
Source: World Gold Council, BofA Global Research
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Gold share should be +20% in an "efficient" central bank

Looking at gold as an effective portfolio diversifier, central banks have an 11% gold allocation in their FX reserves, from 5.5% in 2000, so investment in the yellow metal has already come a long way. Yet, central banks could diversify further. Exhibit 41 is the starting point of our analysis, gradually increasing the share of gold in an "average" central bank portfolio. Exhibit 42 then looks at info ratios, showing portfolios are most efficient at gold holdings of around 30%.

Exhibit 41: Central bank portfolio

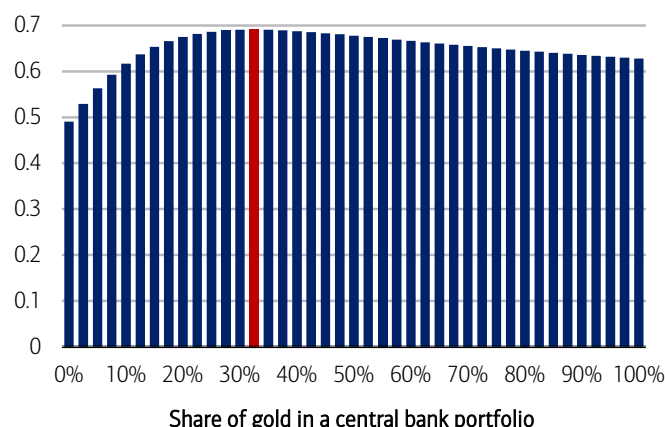
Our analysis assumes that central bank increase gold holdings gradually, while proportionally reducing the share of other currencies



Source: IMF, BofA Global Research
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Exhibit 42: Info ratios at different gold holdings in central bank portfolios

Info ratios peak when the share of gold in an average central bank portfolio hits around 30%



Source: Bloomberg, IMF, BofA Global Research
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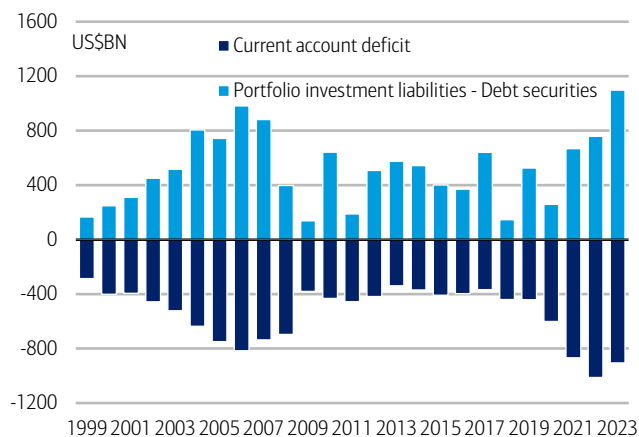
Gold has benefitted from a confluence of factors

Concerns about whether America First means America Alone

President Trump is looking to boost US manufacturing and rebalance US external accounts. Exhibit 43 picks up on this, highlighting that trade deficits have been mirrored by capital inflows, especially in debt securities. Put differently, rising US imports have increased global supplies of dollars. This, along with the depth of US capital markets, enabled central banks to keep adding USD to reserve portfolios. The dynamic is also reflected in Exhibit 43, which shows that foreign holdings of US Treasuries has steadily pushed higher.

Exhibit 43: US current and capital account

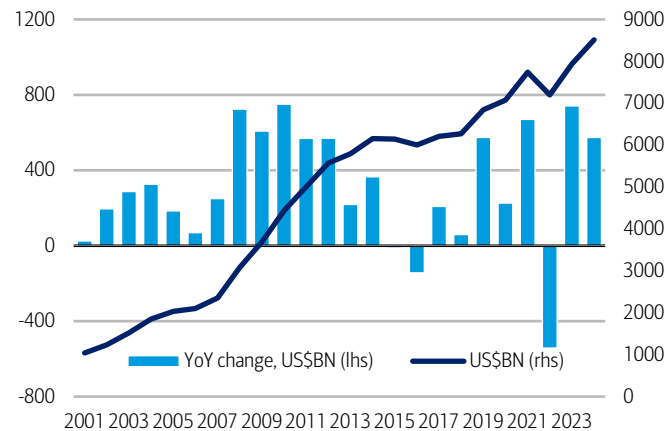
Capital inflows have mirrored current account deficits



Source: Bureau of Economic Analysis, BofA Global Research
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Exhibit 44: US Treasury, major foreign holders

Foreign holdings of US Treasuries have steadily moved higher



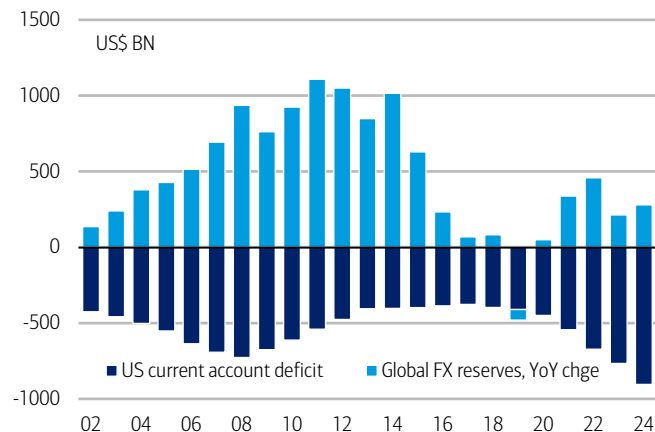
Source: Bureau of Economic Analysis, BofA Global Research
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Hence, more balanced external accounts may make it harder for foreign central banks to keep increasing USD purchases (Exhibit 45). Of course, there is also the question on the incentive for countries to keep using the dollar as the main currency, if the US is to become more inward-looking. Accompanying that are concerns about whether “America First” morphs into a policy of “American Alone”, which could prompt further diversification of FX reserves; a process that has been under way for a while, as the following charts show. Gold has already been and may continue to be a net winner.



Exhibit 45: US current account deficit and global FX reserves

US current account deficits have been mirror images of global FX reserves



Source: Bloomberg, World Gold Council, BofA Global Research
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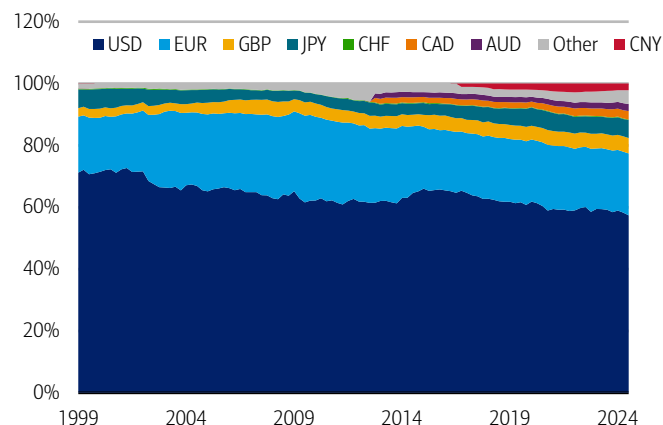
The US has benefited enormously from issuing the global reserve currency: the seigniorage and ample capital flows have helped keep domestic interest rates low. Hence, while the Administration is still intent on reducing trade deficits, officials have been increasingly vocal that the USD should retain its predominant role:

- President Trump mentioned that "We are going to require a commitment from these seemingly hostile Countries that they will neither create a new BRICS Currency, nor back any other Currency to replace the mighty US Dollar or, they will face 100% Tariffs".
- More concisely, US Treasury secretary Scott Bessent said that "critically, we must ensure that the US dollar remains the world's reserve currency."

Tensions between the outcomes of different policies, and the uncertainty accompanying it, have been supportive for gold, as Exhibit 48 shows.

Exhibit 47: Time series of currency composition.

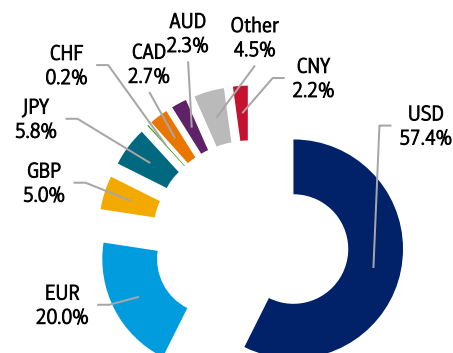
USD remains dominant but has seen share decline



Source: Bloomberg, IMF, BofA Global Research
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Exhibit 46: Current composition of reserve manager holdings (%)

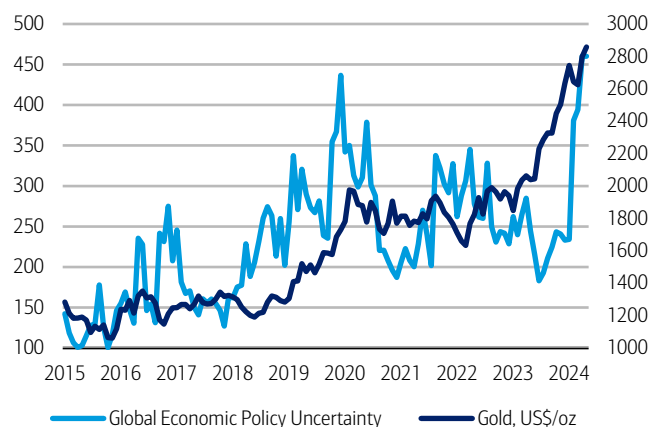
USD retains leading role as world's currency with more than half of reserve managers' holdings



Source: Bloomberg, IMF, BofA Global Research
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Exhibit 48: Global policy uncertainty and gold prices

Gold prices rallied as global policy uncertainty has risen



Source: Bloomberg, BofA Global Research
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Research Analysts

Mark Cabana, CFA

Rates Strategist
BofAS
+1 646 743 7013
mark.cabana@bofa.com

Alex Cohen, CFA

FX Strategist
BofAS
+1 646 743 7015
alex.cohen2@bofa.com

Sphia Salim

Rates Strategist
MLI (UK)
+44 20 7996 2227
sphia.salim@bofa.com

Kamal Sharma

FX Strategist
MLI (UK)
+44 20 7996 4855
ksharma32@bofa.com

Meghan Swiber, CFA

Rates Strategist
BofAS
+1 646 743 7020
meghan.swiber@bofa.com

Michael Widmer

Commodity Strategist
MLI (UK)
+44 20 7996 0694
michael.widmer@bofa.com

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