

Stablecoins, the GENIUS Act and Europe's Monetary Dilemma

Europe has long lived the paradox of limited monetary power. The euro is the world's second most important currency, supported by well-developed financial markets and managed by a highly credible central bank. Yet when crises strike, liquidity evaporates or geopolitics intrude, banks, firms and governments turn overwhelmingly to the dollar. The passage by the United States of the GENIUS Act, intended in part to reinforce that dominance in the age of digital finance, brings this paradox into sharp relief. It confronts Europe with difficult strategic challenges.

The GENIUS Act is not just a consumer-protection and financial-stability measure. Its sponsors describe it as a tool to “cement” the dollar's global role, “buttress” demand for U.S. Treasuries and ensure that innovation in digital payments remains anchored in the United States rather than migrating abroad. Dollar-linked stablecoins – privately issued, officially regulated claims backed by dollar deposits and Treasury securities – are their chosen instrument. If dollar-linked stablecoins provide cheaper, faster and more reliable cross-border payments than existing alternatives, they will reinforce incentives to invoice trade, hold liquidity and manage balance sheets in dollars. Firms will find it convenient to keep working capital in the currency in which payments clear most easily. Central banks will find it difficult to operate as effective lenders of last resort without access to dollar liquidity. These complementarities – long emphasized in the literature on dominant currencies – have historically locked in prevailing monetary arrangements. That nearly all existing stablecoins are dollar denominated suggests that digital innovation, absent countervailing policy, will reinforce rather than erode the dollar's dominant position.

For Europe, this raises three interrelated concerns. First is exposure to U.S. policy uncertainty. Continued dollar dominance implies continued sensitivity to Federal Reserve decisions, U.S. regulatory changes and domestic American political dynamics over debt sustainability. Second is monetary control. Widespread use of dollar-linked stablecoins within the euro area could weaken the ECB's grip on liquidity conditions. It could complicate financial supervision, taxation and regulatory enforcement. Third, and potentially most important, is vulnerability to financial weaponization. Europe has experienced both sides of sanctions policy. It is also acutely aware that its reliance on dollar-based infrastructure limits its strategic autonomy. The continent's dependence on the dollar-based global payments system could constitute a fatal pressure point.

How should Europe respond? One option is inaction, on the grounds that stablecoins will not, in fact, penetrate mainstream payments. There are reasons for skepticism. Bank deposits in the euro area are insured; stablecoins presumably are not. Episodes such as the Reserve Primary Fund's collapse in 2008 illustrate how quickly assets marketed as safe can lose that status. Fragmentation is a further risk: the proliferation of private tokens tied to particular platforms or ecosystems could undermine the singleness of money and the very efficiency gains that stablecoin advocates promise. And Europe's existing payment infrastructure – SEPA Instant Credit Transfer, TARGET Instant Payment Settlement (TIPS) and evolving cross-border links – is far from static.

There is also a Europe-specific argument for restraint. Unlike many emerging markets and developing countries, the euro area does not face chronic inflation or weak monetary credibility. Historically, currency substitution becomes economically and politically destabilizing only at high inflation rates. From this perspective, the threat posed by dollar stablecoins to the conduct of monetary policy is less than in other parts of the world. Still, Europe's experience with energy

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shocks, pandemic financing and geopolitical stress should caution against assuming that credibility alone insulates Europe's monetary system from technological and political disruption.

A second response would be to attempt to restrict or ban the use of dollar-linked stablecoins. Europe has regulatory capacity and a tradition of assertive rulemaking. But attempting to impose an outright ban would be problematic. Experience suggests that digital asset users are adept at evading legal prohibitions. Even China, with its extensive control over financial transactions and internet access, has not eliminated stablecoin activity. For Europe, an open economy committed to free movement of capital and services, enforcement would be still more challenging. A third option is to encourage euro-denominated stablecoins. This response is perhaps the most appealing insofar as it aligns with Europe's long-standing ambition to internationalize the euro. A regulated ecosystem of euro-linked stablecoins could strengthen the currency's role in trade settlement and financial transactions, particularly in Europe's neighborhood. But cross-border use of euro stablecoins would confront the same structural obstacles that have long limited the euro's global reach: fragmented capital markets, uneven availability of safe assets, and the absence of a single, liquid, pan-European sovereign benchmark comparable to U.S. Treasuries. Programmability designed to satisfy European regulatory requirements may further limit their appeal abroad.

A fourth strategy is to deepen and internationalize fast-payment systems. Instant payments in central bank money, operating on standardized messaging protocols, offer speed, safety and finality without fragmenting liquidity. The Eurosystem's TIPS system is a prime case in point. Linking this system first to non-euro-area European countries, such as Denmark, Sweden and Switzerland, and then to the world beyond Europe could provide an alternative to dollar-based stablecoin rails, particularly for trade with neighboring regions. But negotiations over standards, compliance regimes and data protection are time-consuming, and political distance matters. Europe's regulatory sophistication can become a barrier when attempting to export payment infrastructure. A fifth possible response is a central bank digital currency (CBDC). A retail or wholesale CBDC, if widely adopted and interoperable across borders, could provide a public alternative to private stablecoins while preserving monetary sovereignty. Yet take-up of CBDCs globally has been slow, even where pilots are advanced. Standardization leading to interoperability is difficult to negotiate. Cross-border use raises unresolved questions about governance, jurisdiction and dispute resolution. Europe's caution – understandable given concerns about privacy and financial stability – means that the digital euro is unlikely to displace dollar-based instruments quickly.

What conclusions follow for Europe? First, the GENIUS Act should be read not as a technological inevitability but as a strategic move. The U.S. is using regulation to shape innovation in ways that reinforce existing monetary arrangements. Second, Europe's response cannot rely on a single instrument. Bans are leaky, euro stablecoins face scale constraints and lack first-mover advantages, payment-system links are time-consuming to build, and CBDCs remain unproven.

The prudent course is therefore a diversified approach. Europe should continue to develop the digital euro, explore the creation of well-regulated euro-denominated stablecoins, invest in cross-border linking of instant payment systems and maintain a regulatory framework that limits the systemic risks posed by foreign-currency digital instruments without attempting to eliminate them outright. Monetary power will accrue to those who embed innovation within credible institutions.

The dollar's dominance has survived because the U.S. monetary and financial system has repeatedly adapted to new technologies and new economic and political realities. This was true for example of the transition from the Bretton Woods system to the post-Bretton Woods world. That abrupt transition led the economist and economic historian Charles Kindleberger to conclude in 1976 that the dollar was "dead" as an international currency. He could not have been more wrong. The GENIUS Act is the latest stage in this process of adaptation. Whether Europe emerges as a rule-taker or a rule-shaper will depend not on any single legislative act but on its willingness to confront the constraints and opportunities of an evolving international monetary system.

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