The Fed is going to have to rethink its global role

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The writer is vice-president and chair of international economics at the Atlantic Council Josh Lipsky

The most difficult decisions facing the US Federal Reserve, and its new chair Kevin Warsh, in the months ahead won't be where to set the federal funds rate. Instead, it will be finding a way to navigate the central bank's unofficial mandate to protect global economic stability.

Since the 2008 financial crisis, the Fed has become the world's lender of last resort, and it is a role the leadership of the US central bank has welcomed.

The template was created in late 1998 and early 1999, during the Asian financial crisis, by Fed chair Alan Greenspan, working with Treasury secretary Robert Rubin and his deputy, Lawrence Summers. The trio helped contain the economic fallout.

In 2007 and 2008, as the global financial crisis was developing and dollars were in high demand, Ben Bernanke vastly expanded the use of "swap lines" — a tool through which the Fed gives dollars to a foreign central bank in return for its local currency. By 2009, 14 central banks had joined its network.

The arrangements were initially limited to a select group of trusted central banks who played key roles in the global economy and the tool was supposed to be temporary. But it never went away and swaps became a seemingly permanent fixture of the Fed's firefighting arsenal. In 2026, far removed from the financial crisis and the pandemic, the Fed still has five active swap lines.

Of course, the concept behind them is that the Fed makes decisions based solely on liquidity need and the reliability of partner central banks. But given the way Donald Trump has treated allies, particularly those in Europe, America's friends have started to wonder quietly if the same kind of lifeline might be available in the next financial crisis.

A report last year noted that, after the confrontation over Greenland, European officials had been "gaming out" scenarios where dollars would be cut off during a dispute with the president.

Warsh has done little to allay European concerns so far. In his written response to questions from the Senate, he made clear that the Fed's work in international affairs doesn't come with the same independence as its interestrate-setting function. Translation? Geopolitics — and national security priorities — may affect who gets our help.

The issue is not theoretical — just look at what is happening at the US Treasury, where Scott Bessent has used its own swap lines as geopolitical tools — whether to support the Milei government in Argentina or potentially to aid Gulf allies during the war in Iran.

Meanwhile, in minutes released from the last Fed meeting, a group of governors pushed for the permanent extension of the Fed's swap lines to America's most trusted allies in Europe and Asia, as opposed to a yearly renewal process.

No decision has yet been made. And Warsh is right to acknowledge that the Fed's international role is fundamentally different from its congressional mandate to fight inflation and maximise employment. When America's central bank helps stabilise the finances of another country, it is not just making an economic decision; it is making a foreign policy one as well.

Previously the Fed has tried to insulate itself from geopolitics to ensure the US dollar is treated as a safe haven, no matter the conflicts of the moment. But the best way for it to respond to the current situation is not to ignore geopolitics and certainly not to cut off allies in a crisis. That approach would benefit China, which already has at least 30 active swap lines of its own and counting.

Instead, it should shore up shaky trust with transparency. By creating a new framework under which swap lines are used and issued — one that combines financial stability, a central bank's ability to repay and, yes, foreign policy considerations — the Fed can ensure that countries don't start looking elsewhere.