

FX Daily: Markets cautious on tariff risk

Trump said yesterday that tariffs on Mexico and Canada are still on the table ahead of next Monday's deadline. Markets remain reluctant to price that in for now, and some soft US consumer confidence figures today could actually send the dollar a bit weaker. In the eurozone, negotiated wage growth figures should not be a game-changer for the ECB



Source: iStock

⬇️ USD: Dollar might decline today

The dollar found firmer terrain at the start of the week and received some help in late European hours from President Trump's claim that tariffs on Canada and Mexico are moving ahead. The 25% duties were delayed by one month at the start of February, and Monday 3 March is the new deadline to avert a USMCA trade war. As discussed in yesterday's [FX Daily](#), we'd not be surprised to see Trump raise the tariff threat until the last minute to gain negotiating leverage, like in February. Our working assumption remains that 25% tariffs on Mexico and Canada won't materialise, and markets are also pricing in only a modest risk of that happening. We could see FX taking the threat more seriously along the week, so USD/CAD and USD/MXN face near-term upside risks.

On the data side, expect quite a lot of scrutiny on today's Conference Board consumer confidence.

The index jumped in November after the US election but declined in December and January. Consensus is looking at another slowdown to 102.5 from 104.1, with 100 potentially being the pain level for a market reaction. We'll also see the Richmond Fed indices today after regional Fed activity measures (from Chicago and Dallas) came in soft yesterday.

We outlined yesterday how we did not expect this week to have one-way traffic in the dollar. The upside risks for USD today primarily stem from other hawkish comments on tariffs by Trump or other US officials. Barring that, and considering the market's tendency to call the bluff on tariffs, we think the dollar can edge back lower today as consumer confidence risks disappointing. That would feed into a growing narrative of softening consumption, and favour some dovish repricing of Fed expectations.

Francesco Pesole

📈 EUR: Negotiated wages not that key for the ECB

As we suspected, the German election rally in the euro did not last long, as markets were not pricing in a political risk premium before the vote and the key downside risks to the euro remain intact. Chancellor-in-waiting Friedrich Merz is reportedly discussing a quick agreement on EUR 200bn defence spending with its likely coalition partner SPD, following his remarks about Europe's need to gain independence from the US. Our view is that defence spending will not be seen by markets as a channel to revamp stagnant growth in the eurozone and should therefore have limited positive impact on the euro.

The ECB publishes its indicator of the euro area negotiated wages for 4Q24. In 3Q24, the index jumped to 5.4% YoY, although that was primarily due to one-off payments, and ultimately not particularly taken into consideration by the ECB. The Bank's target is around 3%, and while it may take longer for such a slowdown to show in the negotiated wage series, the ECB is seemingly welcoming the slower wage growth in other higher-frequency indicators. For instance, the Indeed wage growth tracker fell sharply to 2.5% in January. We think the bar is relatively high for the ECB to change its stance on the back of today's negotiated wage data, and any positive reaction from the euro may be unwound once the ECB reiterates its dovish commitment.

Anyway, we think EUR/USD could retest 1.050 on the back of some USD weakness today. Still, our view remains bearish on the pair and we target a return to 1.030 in the near term.

Francesco Pesole

📈 GBP: Huw Pill to speak

Bank of England policymaker Swati Dhingra reiterated her dovish position yesterday by stressing that gradual rate cuts will still leave monetary policy in restrictive territory and weigh on the economy. She was one of the two members, alongside Catherine Mann (a hawk turned dove) voting for a 50bp cut on 6 February.

Today, we'll hear some remarks by Chief Economist Huw Pill. He sits on the hawkish side of the spectrum and any dovish comments can have a tangible impact on rate expectations. Last week, Governor Andrew Bailey characterised the uptick in inflation as temporary, but market rate expectations remain rather cautious, with 50bp priced in by year-end. We expect three more cuts this year, also due to the worsening fiscal picture. Anyway, we see EUR/GBP upside as relatively

limited due to the euro's own negative, and think Cable is a much cleaner way to play GBP downside.

Francesco Pesole

AUD: Inflation data could reinforce the RBA's caution

Australia releases January inflation data tonight, and expectations are for a rebound in headline CPI from 2.5% to 2.6%. Markets will look closely at the trimmed mean to gauge whether the sharp decline to 2.7% in December was the start of a broader trend.

We see risks of a relatively hot print tonight which can further endorse the RBA's cautious stance on future rate cuts after kickstarting its easing cycle last week. Alongside inflation, the jobs market provided strong signals in the January report released after last week's rate cut. Employment increased by 44,000, doubling expectations and notably driven entirely by full-time hiring

Risks to growth related to the impact of US protectionism can still lead to three more cuts by the RBA this year, but we think tonight's CPI print can prompt a hawkish repricing in the AUD curve, which currently embeds 50bp by year-end. We expect some support coming the Aussie dollar's way, but like for EUR/USD, we remain bearish on AUD/USD on the back of tariff risk, and target a return below 0.620 in the coming months.

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