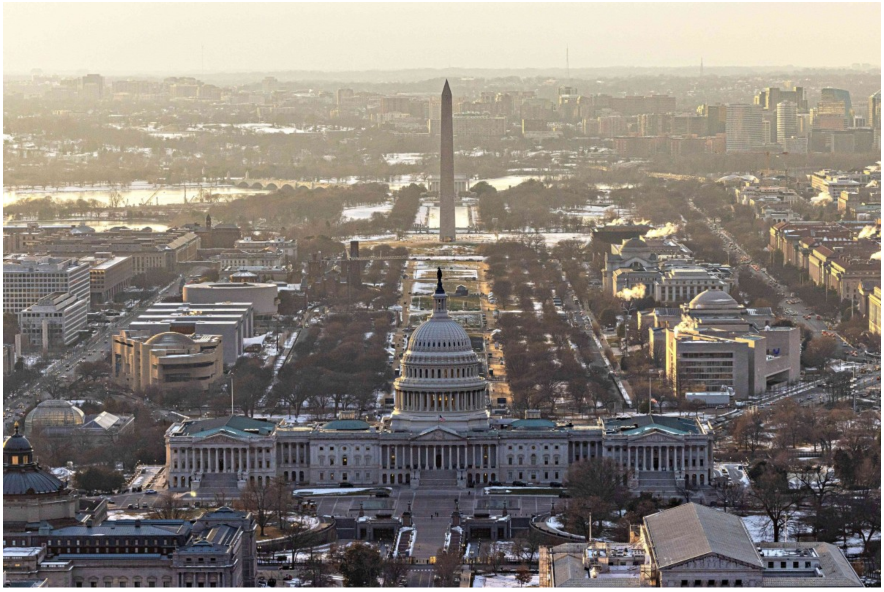
FX Daily: Softer US spending weighs on the dollar

Equity markets are back to where they were, and the dollar is 0.5% softer than when a court ruled the majority of US tariffs illegal on Wednesday evening. An appeals court yesterday intervened in favour of White House policy, but it seems like softer US consumption data in the GDP report made its mark. We have more US personal spending data today



Softer US consumption data and an appeals court ruling have weighed on the dollar as of late

USD: April spending and inflation data in focus

Yesterday's dollar rally didn't last long. It quickly became clear that the Trump administration would pursue other trade laws to enact its tariffs, and later, the US Court of Appeals proposed a delay in the original court ruling that tariffs were illegal. The suggestion now is that a further presentation of evidence could last up until 9 June in the appeals court.

What weighed on the dollar more yesterday seemed to be the US macro data. Personal consumption got revised down to 1.2% from 1.7% quarter-on-quarter annualised in the first quarter GDP release. And a pick-up in initial claims didn't help either. In effect, we saw a return to traditional correlations, where US Treasury yields dropped 5bp and the dollar weakened.

Traditional macro correlations could be in store for the dollar today. The focus here is on the April PCE data. Perhaps most important will be the personal spending number, which is expected to soften to 0.2% month-on-month from 0.7%. Any downside miss here would hit the dollar. The market will also be looking at the price data. This is expected to be very benign, with the core deflator still at 0.1% MoM, bringing the year-on-year rate to 2.5% – the lowest since 2021. This might increase pressure on the Federal Reserve to ease, at a time when the White House is piling the pressure on Chair Jay Powell to cut rates (note the White House briefing on the Trump-Powell meeting yesterday). The topic of the end of Powell's term ending in May 2026 will no doubt start to weigh on the dollar early next year.

Friday is also our day to report on Fed Custody holdings of US Treasuries for foreign official accounts. In the week to Wednesday, these actually rose $10bn. So no evidence this week of a further divestment in US assets. Remember, the Fed thinks it's hedging, not divestment, that has been driving the dollar lower recently.

DXY could make a run back to 98.70 should personal spending disappoint today.

Chris Turner

EUR: Soft activity and prices across the region

While EUR/USD may be rallying on the travails of the dollar, the macro support for the euro is not particularly strong. Today, we've already seen some soft German retail sales data for April (although the March number was revised higher), and later today, we could see the May harmonised CPI data for Germany returning to 2.0% YoY. This would mark perfect timing for next week's European Central Bank meeting, where the market fully prices a 25bp cut in the deposit rate to 2.00%. For reference, the market currently prices 58bp of ECB easing this year versus 50bp for the Fed. That's broadly in line with our house forecasts and suggests interest rate differentials (which currently suggest EUR/USD should be trading lower) may not be moving much from current levels.

As above, the US personal spending data may be the biggest driver of EUR/USD today and may keep it supported in the confines of a 1.1300-1.1400 short-term range.

Elsewhere, Swedish first-quarter GDP has disappointed at -0.2% QoQ and could bring forward expectations for another Riksbank rate cut – now only expected in September. The news is slightly bullish for EUR/SEK.

Chris Turner

JPY: Tokyo inflation data warns of July BoJ rate hike

Tokyo May inflation data surprised on the upside. At the 3.6% YoY, the ex-food reading was the highest since early 2023. As Min Joo Kang outlines here, the data supports her view that the risk of a Bank of Japan rate hike in July is underpriced by the market. Currently, investors only attach a 14% probability to such an outcome.

A hike in July would certainly support the yen. It would also make it a little less expensive for Japanese holders to FX hedge their US assets. This interesting study on FX hedging suggests those investors from a low interest rate region (i.e., Japan) tend to have lower hedge ratios on US assets. Clearly, a reduction in hedging costs would add to the current narrative that the global investor community wants to raise its dollar hedge ratios. We have a 140 year-end forecast for USD/JPY. But the risks are clearly skewed to the downside here.

Chris Turner

CEE: Polish inflation to be released before new president is elected

Most of this week's data in the CEE region is due to be released today. We will see GDP data in the Czech Republic and Turkey this morning. In the Czech Republic, this is the second estimate for the first quarter; we shouldn't see many changes, and the focus will be on the GDP breakdown. The consumer likely remained at the forefront of the economic rebound, while fixed investment remained rather dormant once again. In Turkey, we will only see a flash estimate, where we expect GDP to increase by 2.1% YoY in the first quarter, while there are signs of weakness for the second quarter.

Later today, May inflation will be released in Poland, first in the region as always. Headline inflation should be broadly similar to April at 4.3%, while core inflation probably increased slightly. Upward pressure from core inflation was compensated for by even deeper declines in fuel prices in annual terms, in our view. However, yesterday's announcement of lower household gas prices pulls roughly 0.3ppt off the inflation profile from July – and that should push inflation towards the National Bank of Poland's target even faster than we had previously expected.

More interesting will be the second round of the presidential elections in Poland this weekend. Yesterday's polls show a very tight race with no clear favourite. From a market perspective, the election result will be pivotal for both the future of the current government and the direction of fiscal policy. The outcome will therefore have a medium-term impact mainly on the bond market, while the impact on FX and rates ahead of the curve should fade quickly regardless of the election winner. Given the declining inflation profile, the NBP should deliver rate cuts in any case, negatively weighing on PLN, whose valuation appears quite tight in our view.

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