

FX Daily: Trapped between tariffs and a possible ceasefire

FX volatility levels remain close to two-month lows as investors weigh up dominant themes. The possibility of a ceasefire in Ukraine certainly plays a role, judging by the pricing of assets in Eastern Europe. But the threat of tariffs looms large and could easily insert a risk premium back into those currencies in the firing line. Expect more range trading



FX markets are caught between tariffs and the prospect of a Ukraine ceasefire. Pictured: Ukrainian President Volodymyr Zelensky

➔ USD: Tariff threats have diminishing market impact

FX volatility levels are drifting toward the lower end of two-month ranges as major FX pairs consolidate. The tariff threat remains real, although it is having a diminishing impact on markets. President Trump's threat yesterday that the EU (some sectors or the whole bloc?) would be hit with 25% tariffs in April only saw EUR/USD come off 20-30 pips. The FX market now sees a familiar pattern with the threat, and then the deadline subsequently being pushed back. That was on show yesterday with the presumed 4 March deadline for Canada and Mexico to tighten borders being pushed back into early April. In a way, the FX market will now only believe tariffs when they see them.

On the other side of the Atlantic, European asset markets are performing well. Equity benchmarks are touching their highs of the year and we're certainly seeing Ukraine-related markets, such as CEE currencies, Ukraine Eurobonds all bid and European gas prices offered. There must be speculation that Friday's signing of a US-Ukraine mineral deal will ultimately lead to security guarantees and a ceasefire. Of course, this is far from guaranteed.

Within those two defining factors sit internal US developments. We've seen the dollar hit recently on weakness in the US consumer. And a jump today in the US weekly jobless claims data is probably the biggest risk to the dollar in the very short term. The 4Q24 US GDP revision probably won't be much of a market mover. There will also be a continuing focus on the efforts of Elon Musk to trim the US government. Listening to the rhetoric from Washington, there is an overt effort to slim the budget deficit. In fact, the term premium – or the fiscal risk – in the US 10-year Treasury bond has dropped from 70bp to 30bp this year. While lower US yields have weighed on the likes of USD/JPY – a more balanced budget might ultimately be a dollar positive in that lower yields will be good for the stock market, wealth effects and consumption, and also maintain US exceptionalism when it comes to growth.

We are taking the view that the dollar does not have too much further to correct, but we will also take our cue from technical analysis. A double top reversal pattern in USD/CHF threatens a further 2.5% drop in this pair. So it's important that USD/CHF quickly makes it back above the 0.8965/9000 area to negate this pattern.

For DXY, we're looking for support to hold in the 106.00/30 area.

Chris Turner

➔ EUR: February confidence readings today

Despite all the geopolitical noise, EUR/USD has not strayed too far from short-term rate differentials. These have moved in favour of the euro this month as fears over a slowdown in US consumption have prompted the pricing of a slightly more dovish Fed profile. Where EUR/USD goes from here will largely be determined by how the Fed and ECB cycles get re-priced, and whether the EU tariff threat is real. Our baseline view is that tariffs will go into place in April and that any EUR/USD correction above 1.05 does not hold for long.

Perhaps impacting the pricing of the ECB cycle today will be eurozone consumer and business confidence figures for February. Europe has a lot of untapped spending power (savings rates are high) if only confidence would allow that money to be put to work. Another subdued set of confidence figures today could prove a mild euro negative. Also in focus today will be the first look at February CPI in Spain and Belgium, plus the minutes of the ECB's January meeting. The CPI data might be more interesting – particularly if core readings soften a little. This would take some wind out of the ECB hawks.

Barring major surprises in today's data, EUR/USD looks well contained in a 1.0450-0530 range. Look out for month-end flows, however, particularly around the 17CET WMR fix. The substantial outperformance of eurozone equities this month (Eurostoxx +6%, S&P 500 -1%) could lead to some EUR/USD selling as the buy-side rebalances portfolios to desired weights.

Chris Turner

➔ JPY: Far enough for the time being

The drop in US Treasury yields has certainly weighed on USD/JPY. But this pair has also been hyper-sensitive to expected Bank of Japan rate adjustments. The next input here will be tonight's release of the February Tokyo CPI. The headline number is expected to soften a little, but the ex-food and energy number is expected to drift back up to 2.0%. This could continue the momentum toward earlier BoJ rate hikes. And at ING, we think the risk of a 25bp rate hike in May is sorely under-priced at just 20%.

This all sounds yen bullish. Yet our rate strategy team is reluctant to chase the US 10-year Treasury yield down to 4.00% and we suspect that USD/JPY can try and build a floor in the 148.70/149.00 area. Unlike last July/August, speculative positioning has not been excessively short yen – indeed speculative positioning is now getting stretched long yen.

Chris Turner

⬇️ CAD: The resurgent Liberals

The Canadian dollar remains quite soft given the threat of tariffs. These could come for any number of reasons. And the renegotiation of the USMCA looks like a difficult proposition where the stated aim from Washington now seems to be restricting Canada and Mexico's access to third markets, i.e. China. This looks to be a difficult negotiation and one where Washington will use the big stick of tariffs as a threat.

The backlash against Washington's policies in Canada has seen resurgent support for the Liberal party as it stands up to the tariff threat. Politicians around the world might be inspired by the Liberals to stand and fight. This could lead to more pricing of a global trade war, which is bad news for the commodities complex. The next move in the Canadian dollar is probably lower from here, with 1.4250/4280 now the near-term base.

Chris Turner

Author

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE
chris.turner@ing.com

Francesco Pesole

FX Strategist
francesco.pesole@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist
frantisek.taborsky@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. (“ING”) solely for information

purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.