

## Mexico playing hardball

Can President Trump be talked down from his protectionist perch at the G7? Finance ministers made little progress last weekend and now Mexico looks set to announce retaliatory tariffs



### USD: Trade discussions are key near-term

The near-term focus for financial markets is very much whether President Trump can be talked down from his protectionist perch by fellow G7 leaders at their weekend meeting in Quebec. The omens so far aren't good, with finance ministers making little progress last weekend and major trading partners (Mexico) looking set to announce retaliatory tariffs. At a time when US activity remains strong and the Federal Reserve looks set to push on with tightening, it looks very hard to call the resumption of the benign dollar bear trend that we saw in the second half last year and early this year. Additionally, we struggle to see any appetite for carry trade strategies given, at this stage, the likelihood of a sharp pick-up in market volatility in late June and into July on retaliatory trade measures – particularly between the EU and the US. We, therefore, see the dollar staying bid against selected high yielders (particularly the Mexican peso) and tend to see the dollar index in a 94-95 range.

### MXN: Retaliatory trade measures from Mexico & elections set to weigh

Having been one of the victims of Trump's steel tariffs last week it looks as though Mexican officials

have given up on the idea of any progress on Nafta and instead are considering retaliatory tariffs. Reports suggest Mexico will impose a 20% tariff on about US\$1bn of pork imports from the US. The news comes on the same day the US Senate Majority whip suggested that there was no time in the US political calendar for Nafta discussions this year. These moves will fan fears that Trump will announce the US pulling out of Nafta. At the same time, Mexico is headed towards Presidential elections on 1 July, where the populist AMLO has a commanding lead in the polls. As we've seen in Italy, market complacency over an expected populist government can quickly be unwound and USD/MXN can easily push to 20.50 near term.

## EUR: Newly appointed Italian PM Conte speaks at 14:00 CET

Some calm has returned to European bond markets and the ECB's low purchases of Italian debt in May clearly look to be technical (there was a big re-investment in German debt) rather than political. With regards to Italy, prime minister-designate Giuseppe Conte makes his first parliamentary address at 14:00 CET today. No doubt he'll try to carefully balance the populist government's agenda for flat taxes and higher social spending versus the EU's fiscal rules, but any missteps could hit BTPs again. Better eurozone retail sales data released today should be supportive for the euro, but EUR/USD may struggle to break 1.1720/1850 resistance.

## GBP: UK government running out of time on Brexit

The British pound has stayed relatively soft on news that the government will not present its blueprint on Brexit ahead of the June 28/29 EU summit. Time appears to be running out. Look out for UK PMI services and a speech by the Bank of England's Jon Cunliffe today. Cable could dip to 1.3250.

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