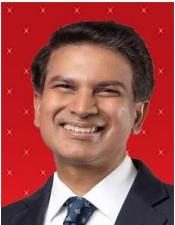


# Macro Insights Weekly

## Trade war and USD

Group Research

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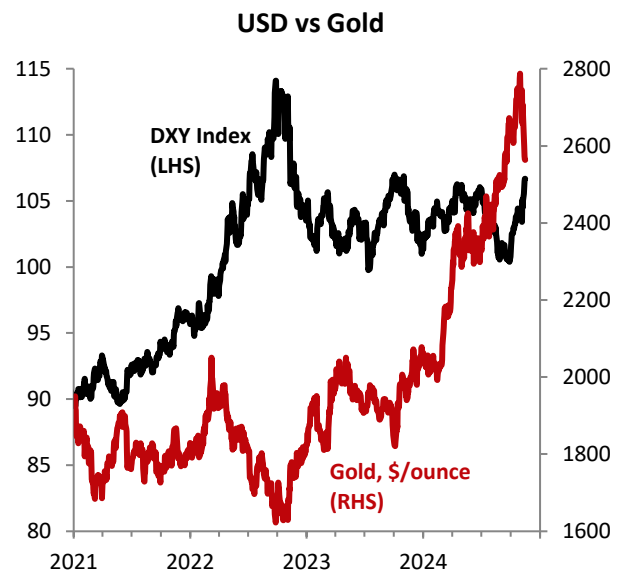
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- *There is a near-term and a medium-term scenario for the US dollar. We make cases for a near-term bull and medium-term bear.*
- *Expectations of tariffs and tax cuts have fuelled a frenzy of US stocks and USD buying.*
- *Markets have also begun scaling back rate cut expectations, pushing the dollar higher.*
- *But for the medium term, views on inflation, fiscal, equity markets, and geopolitics are material.*
- *Asset price crash and financial instability next year could be dollar negative.*
- *If tariffs bring down US imports, exporters will have less USD to buy treasuries, a USD negative.*

### Chart of the Week: USD and gold

The USD has soared since the US elections, reflecting expectations of higher tariffs and relatively fewer Fed rate cuts. In contrast, gold has sold off, reversing its relentless year-long rise. We think these dynamics are unlikely to last beyond the near term. Trump 2.0 will likely come with plenty of adversarial moves to provide motivation to those wanting to diversify away from the USD. This would mean a weaker dollar and stronger gold once the post-election market frenzy abates, in our view.

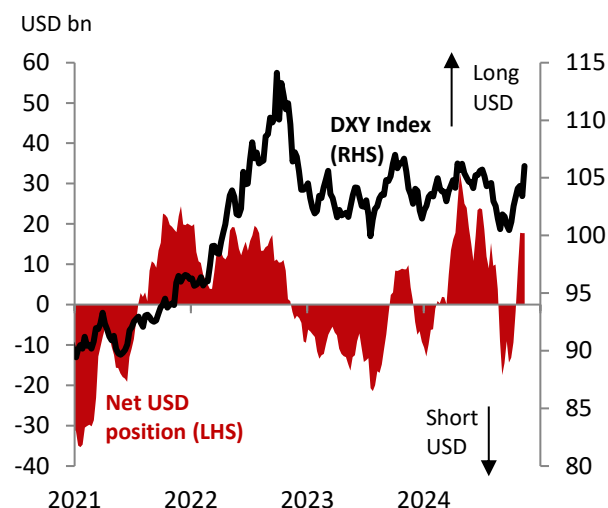


Source: Bloomberg, DBS

**Commentary: Trade war and USD**

There is a near-term and a medium-term scenario for the US dollar. The near-term one came into play vigorously with Donald Trump's election on November 5. Trump trades are on full swing presently, with soaring cryptos, equities, and USD, while the fixed income market has sold off. These trades are pricing in policy support for the cryptos, tax cuts, tariffs, and fiscal expansion. Speculation around the US dollar has been changing since the September Fed meeting, but a decisive return of dollar bulls has materialised only in recent days.

It's not all about Trump. The markets have begun questioning the Fed's desire and ability to cut rates. Even without Trump's policies, latest data point to (i) an economy growing robustly, tracking 2.5% growth, (ii) moderate inflation dynamic, but still way higher than the Fed's 2% target, and (iii) still-strong labour market, with high employment and positive real wage growth. These point to little urgency for accommodation, giving the Fed the room to wait and see how far it needs to go with rate cuts in the coming months. As expectations coalesce around a higher terminal rate in this cycle, that is fodder for dollar bulls.

**Speculative positioning on USD**

Source: Bloomberg, DBS

Past the euphoria of Trump trades, however, a more challenging outlook awaits the dollar. Nominal interest rate differentials are not the only factors driving the dollar, medium term views on inflation, government bond issuance, equity markets, and geopolitics are also material. Considering these, **we look at some reasons to be a medium-term dollar bear.**

The dollar could come under pressure **if there is an asset market crash and/or if treasury issuance balloons**, reducing the attractiveness of US assets. Under such a scenario, Fed policy rates may have to come down even if the battle against inflation is not fully over, which would be a clear negative for the dollar.

Additionally, **weaponisation of the dollar** in recent years has given global central bankers and treasuries the motivation to look for alternative assets on the margin, while the private sector has turned increasingly enthusiastic about cryptos and gold. An assertive Trump administration on a variety of matters of geopolitics could add further fuel to this dynamic.

Finally, **the matter of US twin deficits.** In recent years, US fiscal deficit has been running at 5-6% of GDP. A third of the US treasuries issued to finance these deficits are purchased by foreign buyers, whose supply of dollars comes from the counterpart of US current account deficit, which has been running at 2-3% of GDP lately. Now, if Trump's tariffs succeed in compressing imports, lowering the trade and current account deficits, there will be less dollars for the rest of the world to recycle. Dollar's outlook would be suspect in that scenario, in our view.

Taimur Baig

**FX: Trump Trade may lose momentum**

**The DXY Index rebounded by 5.9% to 106.7 in the past 1.5 months**, following its 4.8% decline to 100.8 in 3Q24. The 107.3 high in October 2023 will be a significant resistance level, and **DXY may correct lower if the Trump Trade loses momentum**. The rallies in the S&P 500 Index and Bitcoin stalled around 6k and 90k, respectively, last week. The Atlanta Fed GDPNow model projected US GDP growth slowing to 2.5% in 4Q24 from 2.8% in 3Q24. The US Treasury 2Y yield entered a 4.24-4.37% range last week. Since Trump's victory, the futures market has reduced the odds of a December Fed cut to 58% from 80%. On November 21, let's see if Fed Governor Michelle Bowman joins her colleague's optimism for inflation to return to the 2% target and rates to decline further towards neutral in 2025. Bowman dissented September's 50 bps cut but supported November's 25 bps cut.

**Doubts may arise over President-elect Trump's ability to deliver on his election pledges.** For example, Trump pledged to bring a swift end to the war in Ukraine. Last week, the Kremlin denied reports that Trump called Russian President Putin not to escalate the war in Ukraine. Over the weekend, Russia launched a massive missile strike across Ukraine, its largest coordinated attack since early September.

**The market's Trump Trade assumption will be tested** – that the Trump administration will be unbridled in delivering its campaign promises. Although the Republicans hold 53/100 seats in the Senate, some of Trump's controversial cabinet nominees will face intense scrutiny during the bipartisan confirmation hearings. However, the newly elected Senate majority leader sees the option to allow for recess appointments.

**GBP/USD has a trendline support level of around 1.2570.** Appearing before the Parliament's Treasury Committee on November 19, Bank of England Governor Andrew Bailey and his colleagues will likely reaffirm their gradual approach to removing monetary policy restraint. Having lowered the bank rate by 25 bps in August and November, the OIS sees quarterly rate cuts to 4.25% by mid-2025. Following the Chancellor's budget announcement on October 31, the BOE forecasted inflation rising and staying above the 2% target until 2027, based on its assumption for rates to decline to 3.7% by 4Q25. On November 20, UK CPI inflation should rebound to 2.2% YoY (0.5% MoM) in October from 1.7% YoY (0% MoM) in September. While CPI core inflation is expected to moderate to 3.1% YoY from 3.2%, it remains above the 2% target.

**AUD/USD appears oversold below 0.65** relative to where Asian currencies and commodity prices are. We expect no surprises in tomorrow's Reserve Bank of Australia minutes for the November 5 meeting. Last Friday, RBA Governor Michele Bullock confirmed it would be some time before inflation returns sustainably to the 2-3% target. Although CPI inflation fell to 2.1% YoY in September, trimmed mean inflation remained high at 3.2%. The unemployment rate was unchanged at 4.1% for a third month in October after peaking at 4.2%. The futures market sees the RBA delaying rate cuts to 2Q25.

We will release our Annual India report later, containing our rationale for USD/INR, to rise to 86 in 4Q25 from 84 at the end of 2024.

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