23 April 2025

Markets in a Minute

Key highlights

- **Dollar declines:** The weakness of the dollar is a notable market reaction to the start of President Trump's second term, but the economic impact is likely to fall more heavily on the U.S.
- **Will it weaken more?** A weaker dollar could be an area President Trump agrees with his advisers on – if the U.S. wants to weaken the currency, there are ways for investors to benefit.
- **Trade talks begin:** Japan was the first country to begin trade talks with U.S. President Trump announcing that the talks had seen big progress, although details were scant. More talks are expected over the coming month.

Watch the latest Markets in a Minute video

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"The unorthodox strategy the U.S. has adopted of fighting all its trading partners simultaneously has meant that the economic impact is likely to fall more heavily on the U.S. than on other countries."

The dollar declines

One of the most notable features of the Trump 2.0 market reaction has been the weakness of the dollar. This is notable because in previous periods of financial stress, the dollar has tended to strengthen.

Any weakness felt by the U.S. is often assumed to be felt even more harshly by its trading partners as it's transferred to them via the global financial system. An important difference in this period of stress compared with previous ones is the unorthodox strategy the U.S. has adopted of fighting all its trading partners simultaneously. As a result, the economic impact is likely to fall more heavily on the U.S. than on other countries.

The U.S. tariff strategy has already pivoted. It's still broad, but now specifically targets China with the deepest measures while, allegedly temporarily, applying a baseline 10% tariff to all other countries. A key question is whether this could change from being a principally U.S. problem to becoming a principally 'all-other-countries' problem. There's also the question of whether the start of trade talks will see the U.S. negotiating on a weaker dollar through some kind of accord.

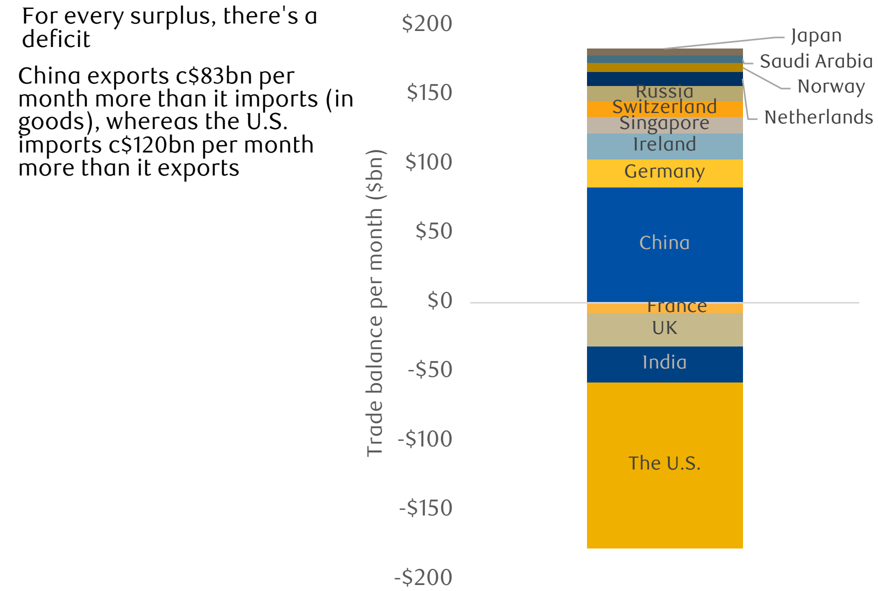
Continued overleaf

Figure of the week

2.25%

The European Central Bank cut its Deposit Facility Rate (interest rate) by 0.25%.

Global trade balances



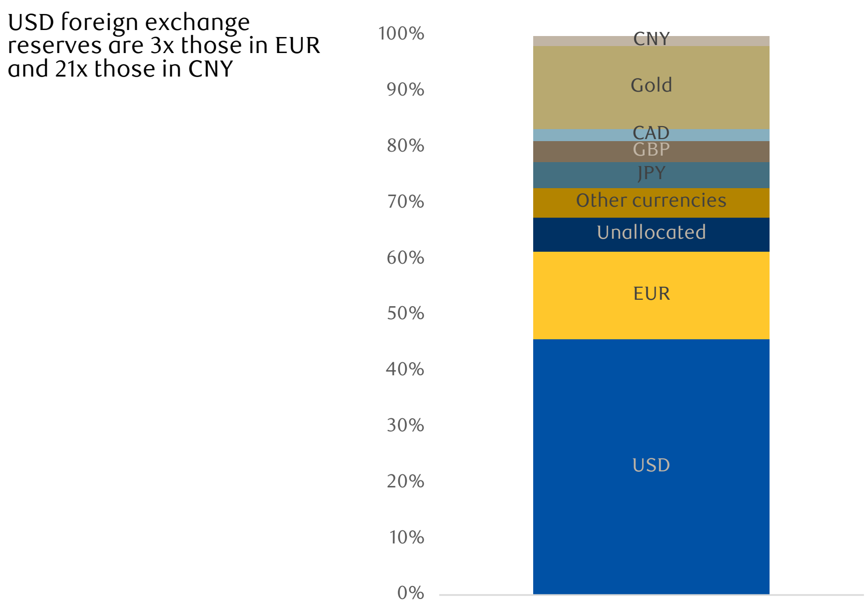
Source: IMF, LSEG Datastream

Some of President Donald Trump's advisers see the devaluation of the dollar as a policy goal. This is because the *Pax Americana*, which has existed since the end of the Second World War, has since been shown to bear some economic costs (perceived or real) for the U.S.

Most notably, the establishment of the Bretton Woods Agreement cemented the U.S. dollar as the reserve currency of the global financial system. It required other countries to accumulate foreign currency reserves in dollars. An inadequate supply of dollars would restrict the amount of trade that could take place, but trading partners need to get those dollars from somewhere and the only possible sources are loans, U.S. foreign aid, or earning them through trade.

So, initially the U.S. needed to supply the world with dollars, which it did through the Marshall Plan (aid) and running trade deficits, eventually undermining the dollar's convertibility into gold. While the currency stability implicit in the Bretton Woods Agreement ended during the 1970s, the use of the dollar as a reserve currency remained.

Global foreign exchange reserves are largely invested in dollars



Source: IMF, LSEG Datastream

"If the U.S. does want to weaken the dollar, there are ways for investors to benefit. That would happen if foreign central banks reduced the weightings to dollars within their foreign exchange reserves. A beneficiary would be gold, which has been very strong."

During the 1980s, this caused the dollar to appreciate relative to other currencies. The Plaza Accord – a joint agreement between France, West Germany, Japan, the United Kingdom, and the United States – was signed, in which all participants agreed to intervene to weaken the dollar.

Stephen Miran, the Chair of President Trump's Council of Economic Advisers, has previously published a plan for a Mar-a-Lago Accord, with the objective of bringing about a weaker dollar. A weaker dollar could be an area in which the president and his advisers are in agreement.

However, a weaker dollar seems likely to imply higher borrowing costs (less foreign ownership of treasuries), which would bring real costs to U.S. taxpayers.

If the U.S. does want to weaken the dollar, there are ways for investors to benefit. That would happen if foreign central banks reduced the weightings to dollars within their foreign exchange reserves. A beneficiary would be gold, which has been very strong.

Gold, which had once accounted for around 60% of foreign exchange reserves, fell to just 6% during the financial crisis and gradually rose until 2024, when its growth sped up, reaching nearly 15% once more.

Various actions may have motivated this. Many developing world economies have held large U.S. dollar foreign currency reserves, but reliance on the dollar exposes them to sanctions that the U.S. might wield in the future.

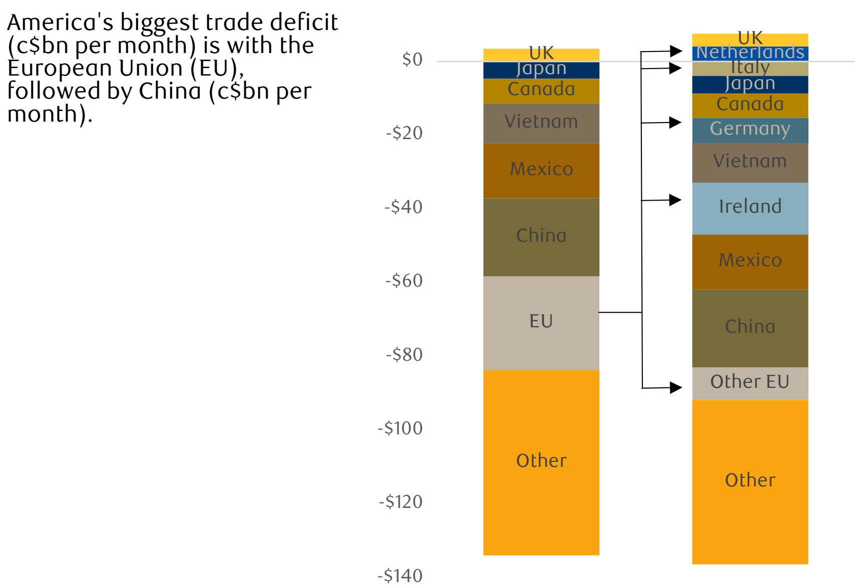
The U.S. president's recent apparent disregard for key federal institutions, such as the judiciary and the independent central bank, is concerning and could potentially weaken the dollar even further.

This was brought into sharp relief around the Easter weekend, when President Trump made a series of comments and social media posts insulting and expressing his dissatisfaction with Federal Reserve Chairman Jay Powell.

Added to this is the possibility that current day America no longer wants the central role in the global trade and financial system that American economist Harry Dexter White negotiated for at the Bretton Woods conference.

The trade talks begin

The U.S. runs a trade deficit



Source: IMF, LSEG Datastream

The first round of trade talks began last week. Japan is the first government to be granted the opportunity to negotiate with the U.S. According to mercantilists, Japan has been a longstanding adversary to the U.S. In fact, it was Japan that inspired President Trump to publish his open letter calling for protectionism in 1987.

President Trump announced that the talks had seen big progress, although details were scant. Ryosei Akazawa, Japan's Economic Revitalisation Minister, said more talks will take place this month and that the currency wasn't discussed. That's a surprising development because Japan's alleged currency manipulation has been a constant source of President Trump's ire.

The resolution of trade issues with Japan may take months and it remains to be seen how many concurrent trade negotiations the U.S. is prepared to run. Japan alone will not materially change the size of its trade deficit.

Coming up this week

- **Tariff announcements:** Being forced into a U-turn doesn't seem to have dimmed President Trump's appetite for tariffs. He continues to promise sector-specific measures, including ones covering the semiconductor supply chain.
- **April's provisional global purchasing managers indices:** Surveys have shown weakness until now, which hasn't yet been followed through in 'hard' economics data.
- **UK retail sales:** UK inflation data last week was helpfully soft. However, this could reflect weakness in the economy. Retail sales numbers should hold up based upon the release of the British Retail Consortium's shop sales survey data earlier last week.