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# Tariff stress likely to weigh on the USD

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**The Trump administration's harsh tariffs and subsequent reversals have damaged market confidence in the USD and USD assets. The sentiment could prove enduring, as consumer and business confidence are likely to take a hit, and prompt more aggressive policy easing. The confluence of these factors suggest that the USD remains a sell on rallies, and is likely to decline over the next few months. We favor using dips in the EUR and JPY to diversify out of the USD, while the AUD offers recovery prospects in 2H2025.**

After a somewhat disconcerting episode of simultaneous weakness in both the USD and US Treasuries (UST) following 2 April, some stability had returned to both markets, at least into the end of last week. The USD index (DXY) had seemed to have found its footing around 99.50/60 after falling from above 104 on 2 April. The EURUSD saw a corresponding surge from below 1.10 to a little below 1.15 before settling in the 1.13-1.14 range. Both broke out of those ranges on Monday, with the DXY falling below 98.50 and the EURUSD rising above 1.15. Prior to Monday, the 10-year UST yield bounced from a 3.87% low to a high of 4.50% high before settling around 4.35%. How then should investors interpret the recent bout market volatility?

At this juncture, it appears that the wider trading ranges are here to stay for the coming months at least. The continued unpredictable adjustments by the Trump administration to its tariff policy seems likely to have enduringly undermined market confidence in the USD, and the damage might not be readily reversed. For now, the main concern is that the 90-day pause in the application of reciprocal tariffs might not lead to enduring agreements across the board. Investors should thus be mindful of the medium-term risks to the USD, along with our preferred currency alternatives.

**EUR, the default alternative to the USD.** As the world's second (to the USD) most liquid currency, the EUR is naturally the first port of call when considering diversifying out of the USD. We think that the USD is likely to be under sustained pressure thanks to the continued policy uncertainty reducing visibility for corporations for the foreseeable future. This in turn is almost certain to lead to weaker business and consumer sentiment data in the near future, which will likely translate into weaker hard data over the medium term. The US Federal Reserve (Fed) is likely to react to this with a restart of its easing cycle in the next few months, and cut its policy rate a total of 75-100 bps this year. The ECB meanwhile is likely to continue easing by another 50bps through 3Q25 before holding steady. Ultimately, the Fed has more room to ease monetary policy than the ECB does, and this should boost the EURUSD over the coming quarters.

We see the USD as a sell on rallies, and expect the EURUSD to mostly move in a relatively wide trading range in the coming weeks. Nonetheless, the USD should come under pressure as US growth expectations slip and if the Fed cuts rates faster. In the very near term, if risk aversion surrounding the economic disruption from the tariffs ebbs, we might see a retracement in the EURUSD. We would use such instances to lighten USD exposure.

**JPY also a good candidate for diversification from USD.** While Japan might be first in line to kick off tariff negotiations with the US, the JPY also provides another avenue for diversification away from the USD. While some sort of tariff agreement is possible, this will likely consist of commitments of increased imports and investment in the US, which could in turn engender some JPY weakness. Any rise in the USDJPY back toward 145-148 would present opportunities to diversify USD holdings into JPY or sell the upside in USDJPY for yield pickup. Our USDJPY target is 142 by March 2026.

**AUD remains attractive despite dip.** We retain our view of a recovery for the AUDUSD in 2H2025 on expectations of positive domestic GDP growth, some additional policy support in China, and more aggressive Fed easing versus the Reserve Bank of Australia (RBA) over the next 12 months. After the AUDUSD plummeted to a five-year low of 0.593 on growth risks from the trade conflict, we have adjusted our forecast to 0.66 (from 0.67) for December 2025, with 0.68 for March 2026 remaining unchanged.

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