DAILY
COMMENT

July 27th, 2020

Dollar weakness in context:

1) The USD continues to soften against the DXY basket of other DM currencies. That index is now at its lowest since mid-2018 and towards the lower end of the range that it has occupied since early 2015 (Chart 1: this was when the fundamental rotation began towards a less accommodative Fed and negative rates in most other DM countries). **In Apr, I argued that peak-USD would reflect peak-crisis and that a near-term USD reversal would occur once signs of a rolling global recovery became more visible** (see note attached: *The latest USD surge in context*). **I think this is what has occurred. In that note, I further argued that once this correction has played out there was not a hugely compelling case for sustained USD depreciation in 2020H2-21, in part because neither valuations, relative policies and nor trade imbalances argue for a major move**. Longer-term, I think USD has downside as the role of USD a reserve currency is diminished (this is all part of the US-China power shift narrative), but I'm not sure that this rotation narrative is a good basis for making a *near-term* trading call. The latest EMU fiscal agreement may enhance the euro's safe-haven status, but negative yields put EUR at a disadvantage to gold on this front.

2) Q2 DM GDP data later this week will focus attention on the extent of the C-19 slump, which was really a Mar-Apr event. **Data this morning point to continued manufacturing sector improvement through Jun in both the United States and Europe**. The US durable goods orders report posted a 3.3%m/m, sa rise in new core orders, building on the (downward revised) 1.6%m/m, sa gain in May. Shipments (a proxy for equipment investment) have followed virtually the same pattern (Chart 2). For Q2 overall, shipments were *down* 19.8%q/q, saar; the Jun level was 5% *above* April's, auguring well for Q3 capex. **The Dallas Fed manufacturing index was the weakest of the 3 Jul regionals to date**. The index improved in July, but not at the clip evident in the NY and Philly Fed surveys (Dallas Jul was 0.2-standard deviations (sd) *below* post 2004 average, versus 1.1 and 0.7 sd *above*, respectively, for Philly and NY). It is tempting to suggest that the relative weakness of the Dallas survey reflects damage from the Texan C-19 surge; the other relevant relative driver is the correction in the oil sector.

Chart 1
USD DXY index
weighted USD basket vs EUR, JPY, GBP, SEK, CHF

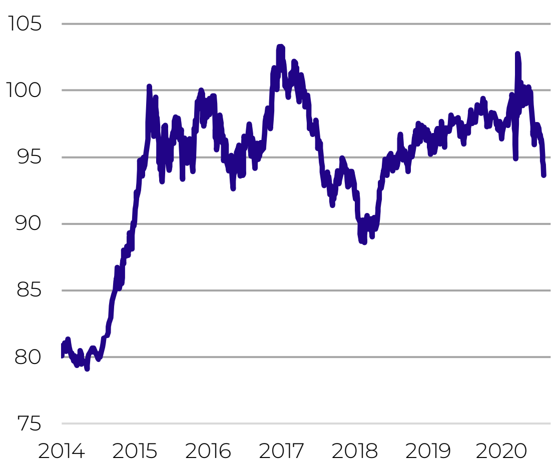
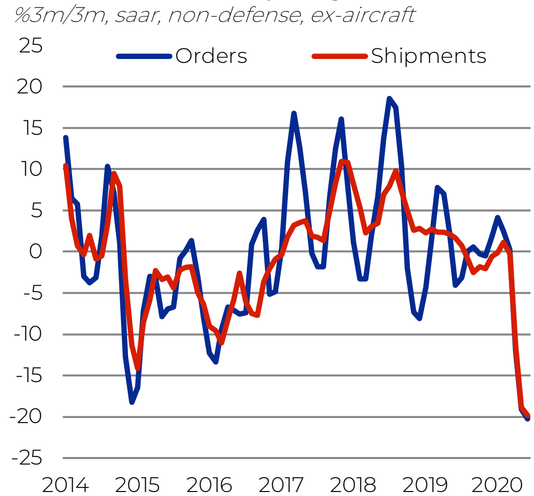


Chart 2
US: trends in core capital goods
%3m/3m, saar, non-defense, ex-aircraft



3) **Germany's Jul IFO survey continued the string of better Euro area data, backing up the outcome of last week's Markit PMI surveys**. The headline index was slightly-better-than-expected, although that reflected **a stronger gain in the expectations component**. This is now back to its long-term average; the current conditions sub-index remains about ¾ sd below its long-run average (the low had been 1.4 below in May; the more manic-depressive expectations sub-component hit a low of -5.8 sd below long-run average in Apr). **By sector, the climate indices all rebounded, with manufacturing remaining the laggard—a pre C-19 condition that has been in place since mid-2018** (Chart 3; onset of US protectionism).

4) **The ECB reported its Jun money and credit data**. M3 growth was 9.2%oya, up from 8.9%oya in May (in the US, Jun M2 growth was 22.9%oya, after 23.1%oya in May). **On the credit-counterparts side, the main boost to both US and Euro area broad money growth came in Mar and Apr, when bank lending to the private sector soared** (Chart 4). US bank lending slowed in May and companies repaid bank debt in Jun. A similar picture was true in the Euro area, where Jun bank lending was close to flat. **So far, the DM outlier is Japan, where the lending surge came later and** (through Jun) **has yet to fade**. This is consistent with Japan's C-19 cyclical pattern of being last-in, last-out (LILO).

Chart 3
Germany: IFO survey by sector
business climate diffusion indices

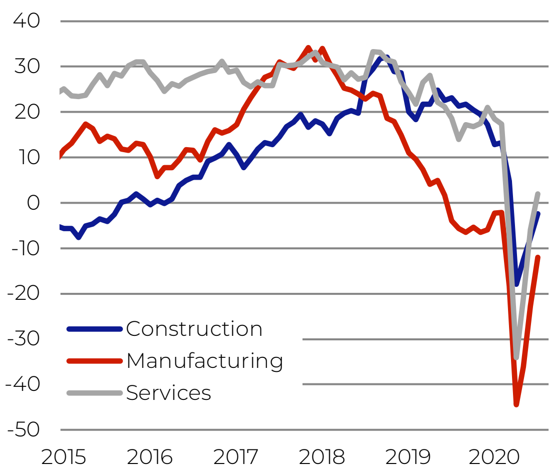


Chart 4
Bank lending to non-financial companies
LC billion, net change per month *¥ trillion*