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A restart of the dollar rally?

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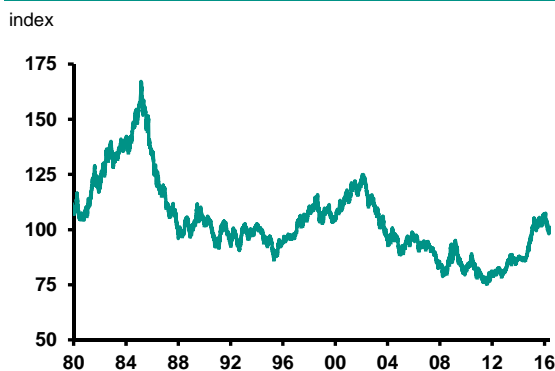
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- **Recent recovery of the dollar not likely to last**
- **Germany's ZEW economic sentiment declines**
- **.... while the details of Q1 GDP suggest that part of the strength was a one-off**

Dollar has recovered since the end of April ...

The US dollar weakened by around 8.5% from February 2016 up to the end of April 2016. It will not come as a surprise that commodity prices and emerging market currencies rallied strongly during this period. However, since the end of April, the dollar has been on a recovery path (+3%) and emerging market currencies and commodity prices (especially metals) have fallen considerably. Precious metal prices have retraced by 4 to 12%. However, oil prices have remained resilient. The upward adjustment in Fed interest rate expectations since 12 May and better-than-expected US data have played crucial roles in this market behaviour.

Calculated effective exchange rate US



Source: Bloomberg, Bank of England

... but this is expected to be a temporary recovery

Is this a re-start of the US dollar rally? In short, no. We see this movement mainly as a short-term US dollar recovery. We continue to hold the view that the multi-year dollar uptrend is over and has turned negative. Short-term waves of strengthening do not change this overall outlook as long as the US dollar does not break above the 200-days moving average. In addition, if the Fed were to hike rates this year (not our base case), it will be gradual. A 25bp rate hike by the Fed this year is now roughly priced in by financial

markets. In addition, US real yields (taking into account inflation expectations) will likely decline. This will weigh on the dollar. So, the near-term upside in the US dollar is limited in our view. What would change the overall US dollar picture is aggressive Fed rate hikes responding to a strong economy. We think this is unlikely.

Germany's ZEW economic sentiment declines ...

The ZEW economic sentiment indicator edged lower in May. It fell to 6.4, down from 11.2 in April, but still above the levels of February and March. The survey measures the expectations of economists and analysts about the German economy during the next six months. The survey results for May are in line with a slowdown in GDP growth to more modest levels following the surprisingly strong 0.7% qoq expansion in Q1, with the value of the expectations component well below its long-term average value of almost 25. Indeed, we expect the German economy to grow at a rate of around 0.4-0.5% qoq in the second half of this year. In Q2, growth could turn out somewhat weaker though, as there will probably be some payback for the strength in Q1.

... while the details of Q1 GDP indicate that one-off positive factors were at play

The details of Q1 GDP growth in Germany were published on Tuesday. They showed that the 0.7% qoq growth rate was due to strong domestic demand, whereas net exports shaved 0.1 percentage point off growth. Fixed investment was particularly buoyant in Q1. Investment in machinery and equipment expanded by 1.9% qoq and construction investment by 2.3%. That said, growth in construction investment was lifted by the exceptionally mild winter and will probably weaken in Q2. Also, domestic orders for machinery, which tend to be a good leading indicator for fixed investment, slowed down sharply in Q1 (to -1.0% qoq, down from +0.7% in 2015Q4), boding ill for investment growth in Q2.

Day	Date	Time	Country	Key Economic Indicators and Events	Period	Latest outcome	Consensus	ABN AMRO
Monday	23/05/2016	01:50	JP	Merchandise trade exports - % yoy	Apr	-6.8	-10.4	
Monday	23/05/2016	06:30	NL	Consumer confidence - index	May	1		3
Monday	23/05/2016		EC	Composite PMI output	May P	53.0	53.2	53.1
Monday	23/05/2016	10:00	EC	PMI services - index	May P	53.1	53.3	53.2
Monday	23/05/2016	10:00	EC	PMI manufacturing - index	May P	51.7	51.9	51.8
Monday	23/05/2016	12:15	US	Fed's Bullard speaks in Beijing (v)				
Monday	23/05/2016	14:00	US	Fed's Williams speaks in New York				
Monday	23/05/2016	15:45	US	Markit - Flash PMI	May P	50.8		
Tuesday	24/05/2016	00:30	US	Gfed's Harkker Speaks on Economic Outlook				
Tuesday	24/05/2016	08:00	DE	GDP - % qoq, final and details	1Q F	0.7	0.7	
Tuesday	24/05/2016	09:00	EC	ECB's Praet speaks				
Tuesday	24/05/2016	11:00	DE	ZEW index (expectation economic growth)	May	11.2	12.2	13.0
Tuesday	24/05/2016	13:00	TR	Repo rate - %	May 24	7.5	7.5	
Tuesday	24/05/2016	14:00	HU	Base rate - %	May 24	1.1	0.9	
Tuesday	24/05/2016	16:00	US	New homes sold - % mom	Apr	-1.5	1.6	1.3
Wednesday	25/05/2016	10:00	DE	Ifo - business climate - index	May	106.6	106.7	106.7
Wednesday	25/05/2016	15:00	US	FHFA house price index - % mom	Mar	0.4	0.5	0.5
Wednesday	25/05/2016	15:00	US	Fed's Harker speaks				
Wednesday	25/05/2016	16:00	CA	Policy rate - %	May 25	0.5	0.5	
Wednesday	25/05/2016	17:40	US	Fed's Kashkari speaks on energy and Monetary Policy (nv)				
Wednesday	25/05/2016	20:00	US	Fed's Kaplan speaks				
Wednesday	25/05/2016		EC	ECB's Praet and Knot speak in Madrid				
Thursday	26/05/2016	10:30	GB	GDP - % qoq	1Q P	0.4		
Thursday	26/05/2016	11:15	US	Fed's Bullard speaks (v)				
Thursday	26/05/2016	14:30	US	New durable goods orders - % mom	Apr P	1.3	0.2	
Thursday	26/05/2016	16:00	US	Pending home sales - % mom	Apr	1.4	0.7	0.8
Thursday	26/05/2016	18:00	US	Fed's Powell speaks about Economy (v)				
Friday	27/05/2016	01:30	JP	CPI - % yoy	Apr	-0.1	-0.3	
Friday	27/05/2016	14:30	US	GDP - % qoq annualised	1Q S	0.5	0.8	0.9
Friday	27/05/2016	16:00	US	Univ. of Michigan cons. confidence - index	May F	95.8	95.8	96.0
Friday	27/05/2016	19:15	US	Yellen speaks at Harvard University at Radcliffe Day				

Source: Bloomberg, Reuters, ABN AMRO Group Economics (we provide own forecasts only for selected key variables and events)
FOMC (v) voting; (nv) non voting

Find out more about Group Economics at: <https://insights.abnamro.nl/en/>

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