Trade Idea – Foreign Exchange

Commodity bounce supports Aussie

11th March 2016

AUD rebounds

- On January 18th, concerns over Chinese growth prospects and weakening terms of trade pushed the AUD/USD exchange rate to the lowest level in approximately seven years (30th March 2009). Since 2012, the Australian currency has experienced a relentless decline as the nation’s primary commodity exports of iron ore and coal have suffered from the moderation of Chinese industrial demand. However, in the past two weeks commodity prices and risk sentiment have rebounded from what appears to have been a floor and have supported a 5.8% appreciation of the AUD on a trade weighted basis (see Figure 1). Recent readings of Australian growth, headline inflation and consumer sentiment have also highlighted the success of existing monetary easing measures and the resilience of the Australian economy in the face of an ailing natural resource sector, contributing further to the AUD’s recent strength. In the coming month, we expect momentum from rising commodity prices and positive risk sentiment to persist and the AUD to continue to climb against its major currency counterparts.

Figure 1

Inflation and growth impress

- Prospects for the Australian economy look less gloomy following a recent slew of positive data. The latest growth numbers show that during the three months to December, the Australian economy grew by 3%* (on an annualised basis) and inflation rose to 1.7% (Figure 2). Both results surpassed analyst expectations and reflect the success of recent easing measures in mitigating the impact of falling investment and revenue from the nation’s vast mining sector. While in the longer term the economy still faces challenges, in the near term the backdrop looks strong enough to support a continuation of the recent AUD rally.

*All figures quoted are sourced from Bloomberg unless stated otherwise.
More easing unlikely in the near term

- While the market is currently pricing in further monetary easing this year, it is unlikely that any action will be taken by the Reserve Bank of Australia (RBA) at its April monetary policy meeting. A statement from Glenn Stevens, the RBA governor, made during the last monetary policy meeting explicitly stated that the likely catalyst of any additional easing of monetary policy is “continued low inflation”. With Q1 ’16 inflation data not due until the 27th April, it is unlikely that the RBA will implement further measures before its meeting in May.

Short positioning to unwind further

- Commodity Futures Trading Commission (CFTC) data shows that since mid-February, net speculative AUD positioning turned positive for the first time since September 2014 (see Figure 3). This move has been driven primarily by an increase in speculative longs to multi-year highs and also in part by a fall in speculative shorts. However, speculative shorts remain elevated by historical standards and further unwinding of short positions could support further upside to the AUD against the US Dollar.

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