

Morgans track A\$

CONFUSION over what is driving the current behaviour of the Australian dollar has prompted Morgans Financial to issue a review of economic factors at play – and predict the ‘Aussie’ will settle at about US\$0.70 cents by year end.

“Over the last year, we have seen the Australian dollar fall and interest rates fall at the same time,” Morgans research director, Roger Leaning reported.

“Many people are used to the idea that falling interest rates lead to a falling exchange rate. Fewer people are used to the idea that surges in capital investment drive both interest and exchange rates up and down at the same time.



Roger Leaning.

“Commodity price stimulated investment is a good example of how investment affects interest and exchange rates particularly in Australia,” he said. “Back in 1998, commodity prices were at the end of a cycle of long term decline and low levels of mining investment in Australia leading to low long term Australian interest rates relative to US 10 year bonds and a low Australian dollar exchange rate.

“However, cycles come and go and the low commodity prices of the late 90s turned into a multi-year commodity price boom.”

Mr Leaning said this had an unusual, but logical effect.

“By 2010 record high commodity prices attracted record high Australian investment, which in turn led to long term Australian interest rates increasing to a level 2.5 percent higher than

US 10-year bonds and a substantial rise in the value of the Australian dollar,” he said.

“Since 2010, the cycle has rolled over again. A big investment in mining has led to global increases in commodity supply and downward pressure on prices.

“The subsequent decline in mining investment means that long term Australian rates are now falling relative to the US,” Mr Leaning said. “In February 2015, Australian 10 year bond yields were just 0.5 percent higher than US 10 year bonds.

“So it is no great surprise that the Australian dollar is depreciating. Indeed by the end of this year (2015), we forecast Australian cash rates to be 2 percent or lower and expect the Australian dollar to bottom around US\$0.70.”

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Morgans Financial Ltd is a Queensland Leaders Industry expert. ■