



Exchange Monitor

The Alchemist looks at the current level the A\$/US\$ exchange rate. While some brokers expect the rate to remain steady over 2018, we think that a stronger-than-expected gain is possible

The Aussie Dollar — Not Coming Down Anytime Soon

INTRODUCTION

The Australian dollar traded at a January average of US\$0.795/A\$ and ended the month at US\$0.807/A\$.

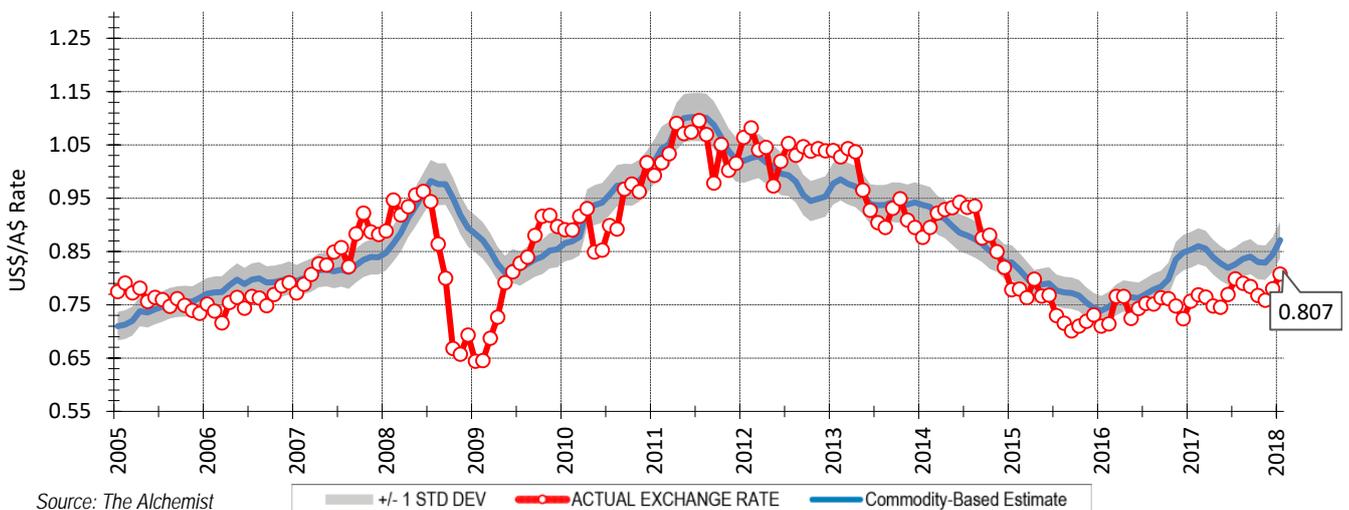
This recent appreciation has largely been due to the broad, positive macroeconomic outlook and the ongoing expectations for an interest rate increases in the near future.

COMMODITY PRICE-BASED EXCHANGE RATE MODEL

- At US\$0.807/A\$, the Aussie dollar sits outside what can be expected from our purely commodity-based modelling.
- It is in RFC Ambrian's opinion, that the Aussie dollar is more fairly valued at US\$0.850/A\$. This reflects the ongoing growth in mining exports and the increase in prices across the commodity sector.

- The recent rally in commodities saw a 17.7% increase in the RBA Commodity Price Index since June 2017, the highest it has been in almost 3.5 years
- This follows an 18-month period of a suppressed Aussie dollar compared to commodity prices, largely driven by contractionary US monetary policy as opposed to Australia's neutral stance.
- Broker consensus has the Aussie dollar at fair value, expecting it to maintain its US\$0.79-0.80/A\$ level throughout 2018 and into 2019, reflecting consensus that most commodities will decline or remain stagnant for the remainder of 2018.
- However, feedback to RFC Ambrian from numerous influential industry analysts and miners, suggests that growth in demand for commodities could drive a greater-than-expected increase in the Aussie dollar. This is in line with our commodities based modelling (see Figure 1).

Figure 1 Commodity-based Estimate for A\$/US\$.



Source: The Alchemist

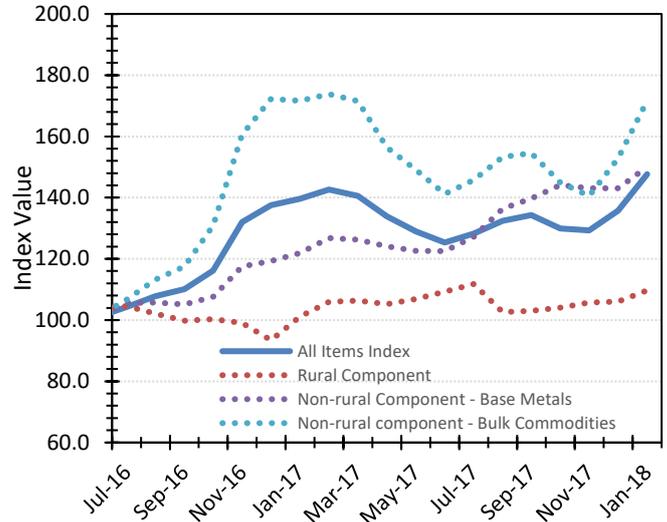
RECENT TRENDS IN COMMODITY PRICES

- With bulk commodities making up 50.5% of the RBA Commodity Price Index (and iron ore being 29.5% of this), it is no surprise the index has rallied in recent months.
- Rural commodities (which make up 14.7% of the index) gained ground in the second half of 2017, although this has had little impact on the overall index.
- Spot Copper and Aluminium are up approximately 16% and 11% since July last year respectively.
- LNG makes up 9.7% of the index, up from 8.8% in March 2017. With the Japan average spot LNG price having risen 96% over the past 6 months to levels not seen since the end of 2014.
- Already commodities are well above the 1Q 2018 consensus values, with little sign of slowing down in the near future.

SUMMATION

It is in RFC Ambrion's view that the recent rally in the bulks and base metals is likely to continue into the near future. This rally in commodities will subsequently provide sustained upward pressure on the Aussie dollar.

Figure 2 RBA Commodity Price Index

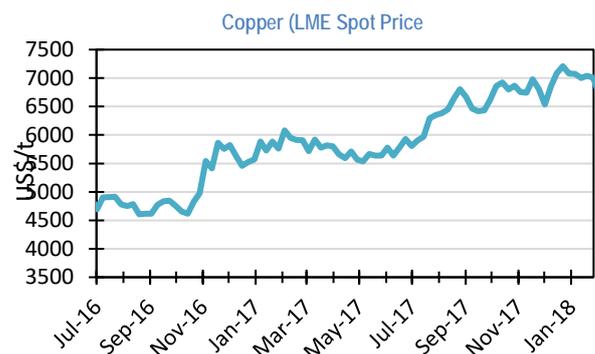
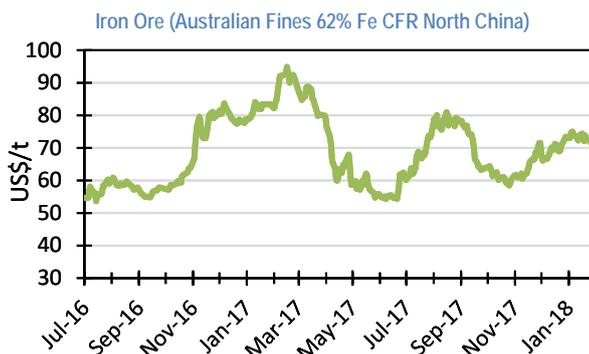
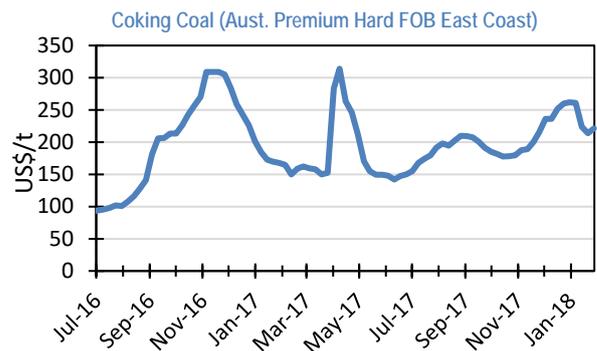
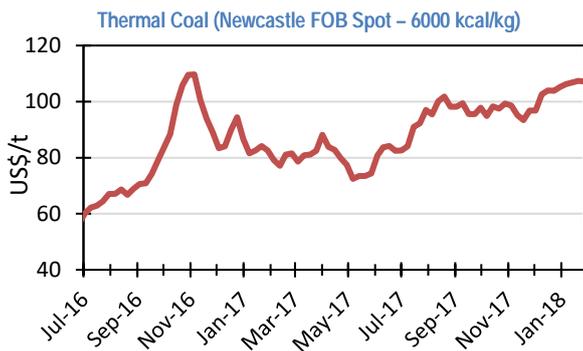


Source: RBA

Table 1 Commodities Consensus Forecasts (US\$/tonne)

	Price 18 'Jan	1Q18	2Q18	3Q18	4Q18	2019
Coking Coal (Aust.)	228.3	177.0	165.3	150.8	146.0	135.7
Thermal Coal (spot)	106.85	86.64	80.60	77.20	76.74	72.31
Iron Ore (N. China)	74.35	67.47	64.77	60.48	60.82	61.41
Aluminium	2243.5	2118	2094	2080	2102	2085
Copper	7032	6658	6673	6646	6588	6713

Source: Consensus Economics (January 2018), Bloomberg



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