

What does the charging US dollar mean for you?

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Newspaper headlines have been dominated by stories of the soaring Australian dollar in recent weeks - but what does it really mean for the economy, and what impact does it have on you and your mortgage?

In recent weeks the Aussie dollar has strengthened against the US dollar, reaching the high 90s and briefly crossing the \$1.00 barrier on October 15.

But just why is the Australian dollar so strong, and what does it mean for our economy?

The value of the Australian dollar largely depends on the strength or weakness of the US dollar, as the AU is viewed as an alternative investment to the greenback.

The weakness of the US economy has served to drive our dollar higher. Our rebounding economy – complete with six RBA interest rate increases in the last 12 months – has also helped the Australian dollar rise, as higher rates attract foreign investors who are looking for better returns.

Dr Shane Oliver, chief economist and Head of Investment Strategy at AMP, says currencies are “always volatile”, and while there’s no guarantee that our dollar will stay strong, it is highly probable that it will remain at or above the US dollar in the coming months.

“With the US dollar likely to remain under pressure, the Reserve Bank of Australia (RBA) remaining on track to raise interest rates further, and Australia’s terms of trade at a near 60-year high, it is likely that the Australian dollar will settle above parity over the year ahead – probably around the US\$1.10 level,” Oliver says.

“Of course, if global growth collapses anew, then all bets are off and a plunge back below US\$0.80 would be possible – but this is unlikely.”

All of this is great news if you plan on holidaying in the US any time soon, or if you plan to shop for US goods or services online – there are some whopping bargains to be had, from electronics through to fashion and jewelry.

It’s also fairly good news if you’re a mortgage holder.

In the minutes of the Reserve Bank’s October meeting, the Board commented on the strength of the Australian dollar, noting that it had appreciated by almost 4% in the past month, and that “the appreciation of the exchange rate represented a tightening of domestic financial conditions”.

Federal Treasurer Wayne Swan commended the central bank for noting the “beneficial effects” of the high dollar, and described it as “an important shock absorber” for our economy.

The fact that the RBA mentioned the currency as a factor in keeping interest rates on hold for October was “very important”, says Westpac’s chief currency strategist Robert Rennie.

After all, the Reserve Bank is aiming to keep a lid on inflation – and “were the currency to continue appreciating, that does some of the work for them,” Rennie says.

In other words, the strong Aussie helped to stave off a rate rise in October, and it may help to do the same in November.

However, borrowers are being warned not to hold their breath. The general consensus is that we should expect a lift in rates at some stage in the next few months.

“The central bank retains a strong bias to raise interest rates again,” Oliver confirms. Whether this happens on Melbourne Cup Day or in early December remains to be seen.

