


**crest**

 FINANCIAL  
SERVICES

# GOING DOLLAR FOR DOLLAR

Snapshot

## Is parity with the US now business as usual?

When the Australian dollar (AU\$) achieved parity and then topped the value of the greenback (US\$) in October and November 2010 there was much excitement in the media.

It took the AU\$ nearly 30 years to hit parity and the hype made it seem a breakthrough had occurred. But what does it really mean? If you are planning to take the kids to Disneyland, it is certainly good news. But if you are selling Australian holidays to tourists from the USA, it's bad news.

Currency fluctuations produce winners and losers because currency values are relative; "parity" means "equal with" because currencies come in pairs — US\$ versus AU\$, AU\$ versus Euro, and so on. It is their relative values which are important, and these are influenced by local and global issues.

## Getting parity into perspective

The AU\$ and the Canadian dollar are both rising against the US\$. That highlights that there are multiple causes of currency fluctuations: in this case, the current strength of two well-managed, resource-based economies versus the weakness of the US economy.

Right now the US is certainly in a tight spot. The economy is struggling to go forward and unemployment remains high. The US Federal Reserve recently decided to inject more cash into the economy by buying its own government bonds, but this is an inflationary strategy that carries an element of risk. Another possible outcome is that the AU\$ will fall in value against the US\$. (Early indications are that this is happening, at least in the short term.)



## A new era — or back to normal?

The key question is whether the AU\$ will remain one-for-one with the US\$ in the longer term. The Australian Reserve Bank thinks our dollar will be at or above parity for the next three years. Other commentators believe that the US Federal Reserve's tactic of increasing the money flow will lead the AU\$ down to the US\$0.90 cent mark within a year.

One Australian economist, Dr Shane Oliver, believes that the AU\$ will be around parity for a decade or more because of the underlying strength of the local economy and our trading position. He argues that, as the graph shows, this was the case for 82 years between 1900 and 1982, and suggests that it was the last 28 years that were abnormal.

## Where to next?

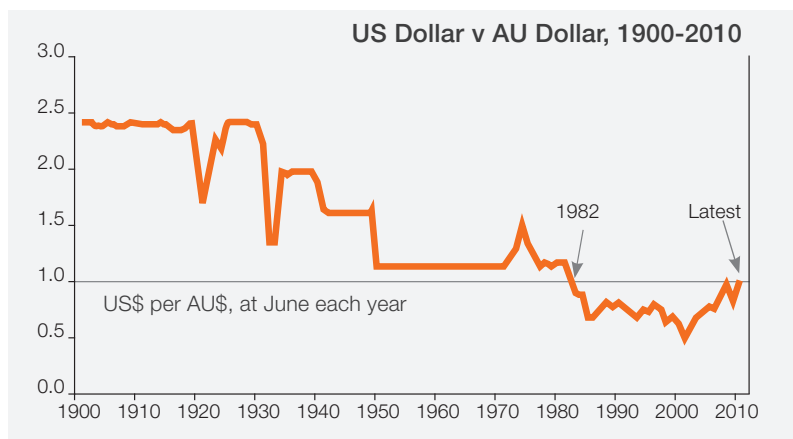
Predictions can't be made but some trends seem clear. The Australian economy is relatively strong and likely to remain that way while there is solid demand for our resources from China, India and other developing economies in Asia. Globally, investors compare

our economy with those of major developed nations and see it as strong and well-managed, with stable inflation and interest rates. With currencies, it is relative strength and performance which are important, and if these factors remain stable, they will support a stronger AU\$.

When dealing with currency, both companies and investors have to consider risk. Do they opt, like BHP Billiton for example, not to hedge currencies or commodity prices but manage risk carefully while remaining open to price movements? Or do they side with Rio Tinto, and take hedged positions? One size does not fit all, no more than any one currency is the investor's perfect answer.

This is an important and often complex issue affecting investment decisions, so we encourage you to contact us and discuss any concerns.

If the pundits are correct and parity becomes standard fare, chances are you'll be able to take the family to Disneyland this coming year — and line up again in a few years' time.



Source: Thomson Financial, AMP Capital Investors