Long AUD/USD (Long AUD Short USD)

Tan Xin Wei

Entry Point: 0.6200

Targets:

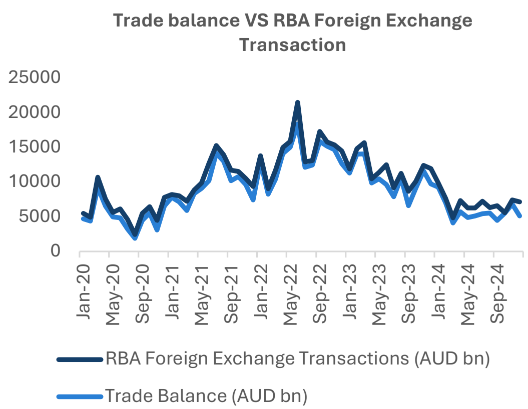
- **Short-term: 0.6600**
- **Medium-term: 0.6800**

Stop Loss: 0.6000

Risk-Reward: 1:2 (short-term), 1:3 (medium-term)

Thesis 1: Australia's stable external balances and robust inflows contrast with growing US structural headwinds.

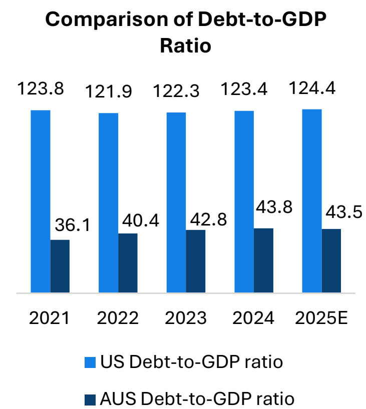
Strong attraction of capital inflows due to stable outlook of Australia



Australia has a stable **budget balance** (1.6% of GDP) and a stable **current account** trend (-1.6% Q3 2024 vs. -1.3% Q2 2024), underpinned by an Aaa credit rating and strong trade ties (33% of exports to China).

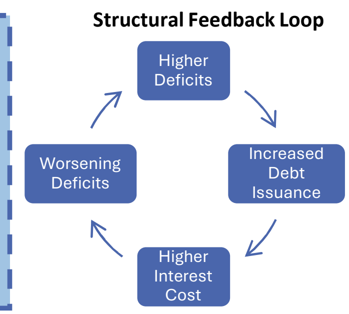
These factors attract inflows, with AUD 20 billion in 2024 Q4 **capital inflows,** supporting the **AUD**.

US structural weaknesses widening fiscal deficit

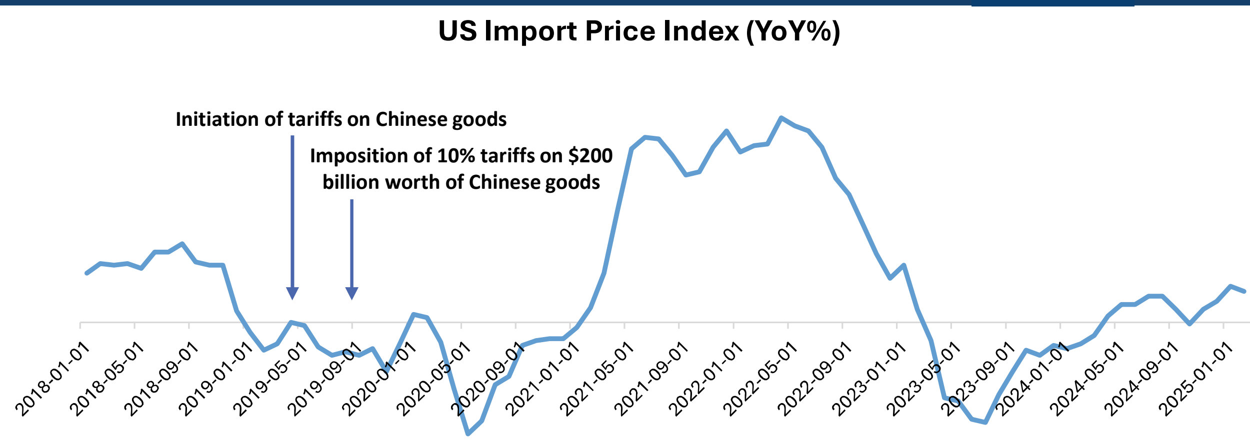


Rising costs for Social Security, Medicare, and Medicaid due to an aging population increased deficits as healthcare and pension costs outpace revenue growth

Even if the Fed cuts rates, the higher U.S. debt-to-GDP ratio means higher borrowing costs. In 2025, interest payments could exceed defense spending.



Over-reaction towards tariffs due to muted effects as proven by 2019 US tariffs



Despite many deem tariffs as inflationary, it is an overstatement as their overall impact on U.S. inflation is often muted due to substitution effects, partial pass-through, and global deflationary forces as compared to the impact of the pandemic in late-2019.

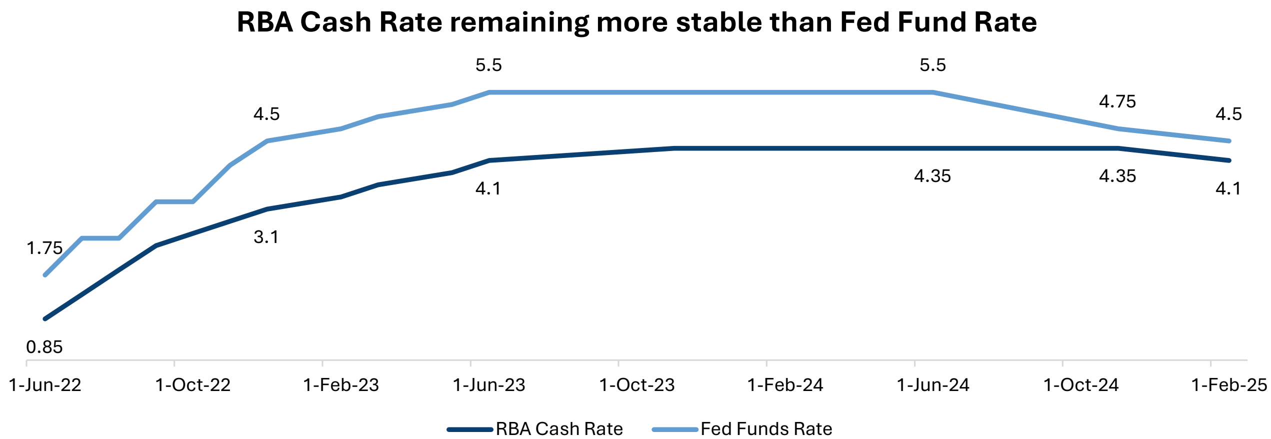
Investors may overestimate their inflationary impact by focusing on headline risks rather than the broader context.

Source: Bloomberg, FRED

Thesis 2: The higher-for-longer rate differential and RBA's cautious easing stance positions AUD to appreciate

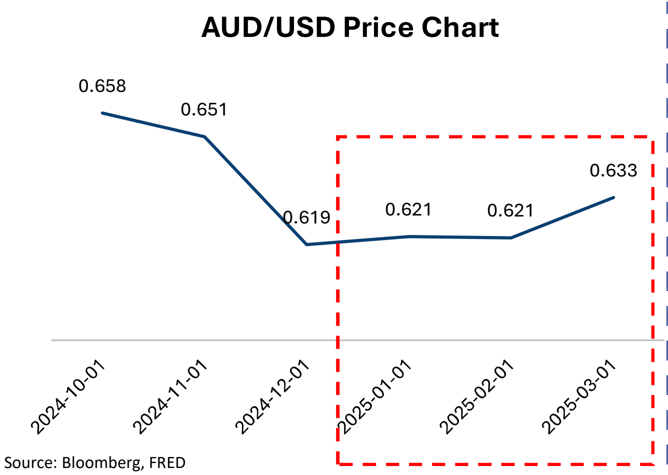
RBA's Predictable Rates Outshine Fed Uncertainty

The RBA cut the cash rate by 25 basis points to 4.10% and that this decision does not pave the way for a series of additional cuts.



Cash rate is expected to remain relatively elevated as RBA will maintain a restrictive stance for longer, AUD is more attractive relative to currencies from economies with more aggressive easing.

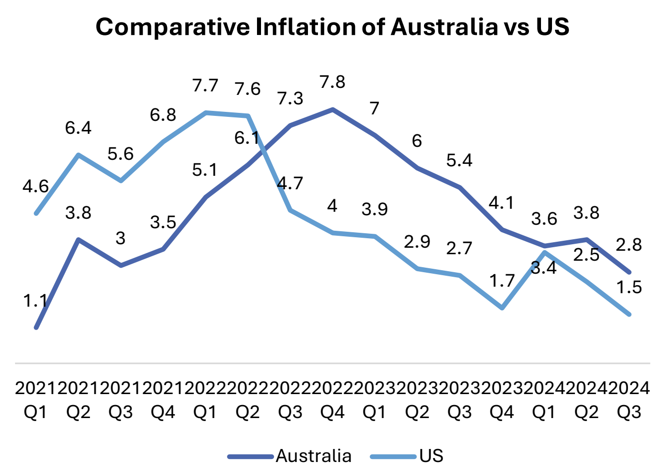
Rate cut defied as AUD strength signals market confidence



Source: Bloomberg, FRED

Despite the rate cut which might traditionally be seen as a negative, the AUD strengthened slightly against the US dollar. This suggests that the market had already priced in the easing and is confident in the underlying fundamentals.

Australia's well-positioned inflation rate



Despite easing from its peak, Australia's inflation remains elevated and sticky, particularly in services and wages, which limits the RBA's scope for aggressive cuts.

U.S. inflation faces downside risks from slowing growth and tighter financial conditions. This divergence supports a higher-for-longer rate differential, making AUD more attractive relative to currencies from economies with more aggressive easing.

Thesis 3: China's growth recovery and Iron Ore demand drives AUD appreciation

Strengthening Correlation between AUD and HSI

Comparing AUD/USD to Hang Seng Index (HK stock market indicator):
AUD has seen to have a historically strong and positive correlation with HSI and is continuously strengthening in 2025 (correlation of +0.65 to 0.75).

Fiscal Divergence between China & US Driving Australia Iron Demand

As USD weakens amid U.S. fiscal risks, investors use AUD as a liquid proxy for China exposure, given capital controls on the RMB.

Recent China rate cuts and property sector bailouts would stabilize growth in 2025

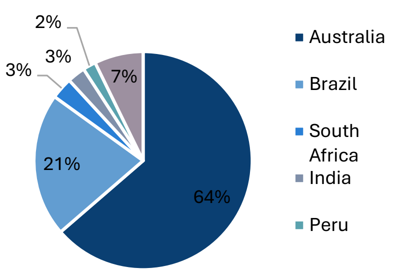
Drive capital into China Commodity-driven growths

Mortgage refinancing initiatives
→ Reviving property market

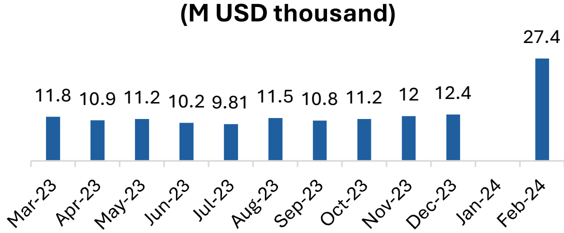
Stimulating steel production
→ Increasing demand for iron ore from Australia

China's Commodity Demand

Import value of iron ore to China



Imports of Iron Ores in China (M USD thousand)



This surge in demand, though softened steel demand, is expected to stabilize prices around US$95-100 per ton. Which hence will bolster Australia's terms of trade and support a healthier fiscal outlook → directly strengthens the AUD.

Source: Bloomberg, FRED, TradingView

Australia Iron Ore & Renewables as Growth Catalyst

Fortescue

BHP

RioTinto

Green Iron Projects

Renewable Energy

High-grade Magnetite Reserves

Safeguard and potentially double iron ore revenue over the long run. Hence provide a decisive tailwind for the AUD.

Potential Catalysts

July 2025
BRICS Summit

If BRICS nations (e.g., China, India) accelerate de-dollarization efforts (e.g., commodity trade in non-USD currencies), the US could face structural headwinds, benefiting AUD.

November 2025
COP30

COP30 could spur global commitments to renewable energy, boosting demand for Australian lithium and copper.

FY2025

In the case where Australia's unemployment rate stays below 4% in 2025 (current: ~4%), the RBA will have less room to cut rates, supporting AUD.