Forex Focus: Asian Risks For Aussie Now

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A DOW JONES NEWSWIRES COLUMN

LONDON (Dow Jones)--By her successful negotiations with the mining companies last week, Australia's new prime minister Julia Gillard has helped to remove a major obstacle to Aussie dollar gains.

However, the Australian currency now faces a new and possibly larger obstacle to extending its rally: China.

Or to be exact, probably China and the rest of Asia.

Last week, while Gillard was accepting a reduction in the proposed tax on surplus mining profits to 30% from 40% and keeping the mining companies happy, most major Asian countries were reporting a distinct fall in manufacturing activity.

Frederic Neumann, a co-head of Asian economic research at HSBC in Hong Kong, notes that activity in Asia has started to level off.

In a piece of research entitled "It Sure Ain't Pretty," Neumann noted that purchasing managers' surveys across the region are "pointing south" and that leading indicators have "turned the wrong way as well."

So just while Gillard may have been convincing mining companies not to up stakes and knock the Australian economy flat on its back, evidence was rolling in that export markets in Asia for the commodities they produce may be shrinking.

Neumann insists that the data aren't evidence of a double-dip recession, and are only a sign that restocking is fading and that the impact of earlier fiscal stimuli is wearing off.

But there are other reasons to fear that Asian growth in general isn't going to be as strong as it used to be.

Chances are that as inflationary pressures start to increase, central banks across the region will start raising interest rates and putting a further cap on growth prospects.

Having said this, there is still plenty reason not to lose faith in the Aussie just yet.

Despite the recent rise in global aversion towards risk, which put the Aussie on the back foot, the Australian economy is still likely to outperform its G-10 counterparts.

As a sharp decline in the U.S. dollar against most other major currencies late last week showed, yield differentials are becoming more important again.

So even if Australian interest rates fail to rise as fast as previously anticipated, fears of a double dip recession in the U.S. mean that rates there all also remain low for longer and differentials should remain in favor of the Aussie.

This could all help to lift the Aussie at least a little more to $0.87 but there are few forecasters suggesting that the Australian currency's upward path will extend much beyond there just now.

See the Australian dollar's recent performance against the U.S. dollar:

http://www.dowjoneswebservices.com/chart/view/4217

Early Monday in Europe, the Aussie was up a little, at $0.8456 by 0645 GMT, from $0.8421 late on Friday in New York, according to EBS.

There was a small improvement in market sentiment, with the Nikkei gaining 0.7% on the day, after last Friday's confirmation that U.S. non-farm payrolls declined in June.

The dollar itself was up at Y87.92 from Y87.70 while the euro was down a little at $1.2538 from $1.2543. The single currency also rose to Y110.24 from Y109.56.

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Reuters   USD/DJ

Thomson   P/1066 or P/1074

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