



While both crosses have now fallen a long way relative to our models, we would now expect these models to keep trending lower. Given the respective levels of the two crosses (and our AUD view below), we prefer to go short NZD/CAD. Indeed we are now more cautious on NZD more widely, as most of the good news appears priced in following its rally in recent months (see Figure 4).

In terms of AUD, our view remains that the global monetary environment argues against looking for anything more than short-term weakness. Reinforcing this were the Chinese monetary data for April, which showed a further pickup in M2 Money growth – this has generally been bullish for AUD in recent years. Moreover, our Chinese team remains more bullish on the Chinese growth outlook than the market consensus, looking for 8.2% growth in 2013 and 8.9% growth in 2014, against a market consensus of 8.0% growth in both years. It is notable then that other “China plays” such as Hang Seng H-shares and copper prices have started to trend higher recently, indicating a greater confidence in the outlook for Chinese demand (see Figure 5). This should soon start to bolster AUD.

One of the other key drivers of our resilient-AUD view has been the expectation of ongoing mining-related FDI inflows (see for instance *FX Daily: On-Hold RBA Lifts AUD, But FDI Inflows And G3 Policy Remain Key Supports*, 5 March 2013). Despite recent negativity on the mining investment outlook, the ABS’s Q1 Capex survey suggested an increase in mining investment would be seen in 2013/14, with a lift in building and structures investment offsetting an expected decline in machinery and equipment investment. While this may prove too optimistic, it suggests mining investment is hardly about to fall off a “cliff”. In terms of what this means for AUD, even if there is little growth in mining investment, it is likely to remain at an extremely elevated level for some quarters to come. Additionally, as mining investment rotates from an import-heavy machinery and equipment focus to a local-expenditure-heavy building and structures focus, the AUD-intensity of this spending may well increase. This argues that the need for resource firms to continue to generate substantial FDI inflows will likely remain intact.

As to how we prefer to express this AUD view, one relatively consistent dynamic in FX options markets is the tendency of AUD/USD options to skew towards puts on AUD/USD declines (see Figure 6). We would take advantage of this dynamic by buying a vanilla AUD/USD 1.02 call (around 70 pips at time of writing), expecting it to resume trading in the 1.02-1.06 range that had until very recently held for most of 2013.

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Figure 4: The good news in NZ is more than fully priced



Source: Deutsche Bank, Bloomberg Finance LP

Figure 5: Many China plays are now getting a boost



Source: Deutsche Bank, Bloomberg Finance LP

Figure 6: Taking advantage of option market dynamics to buy a vanilla AUD/USD 1.01 3-month call on this dip



Source: Deutsche Bank, Bloomberg Finance LP