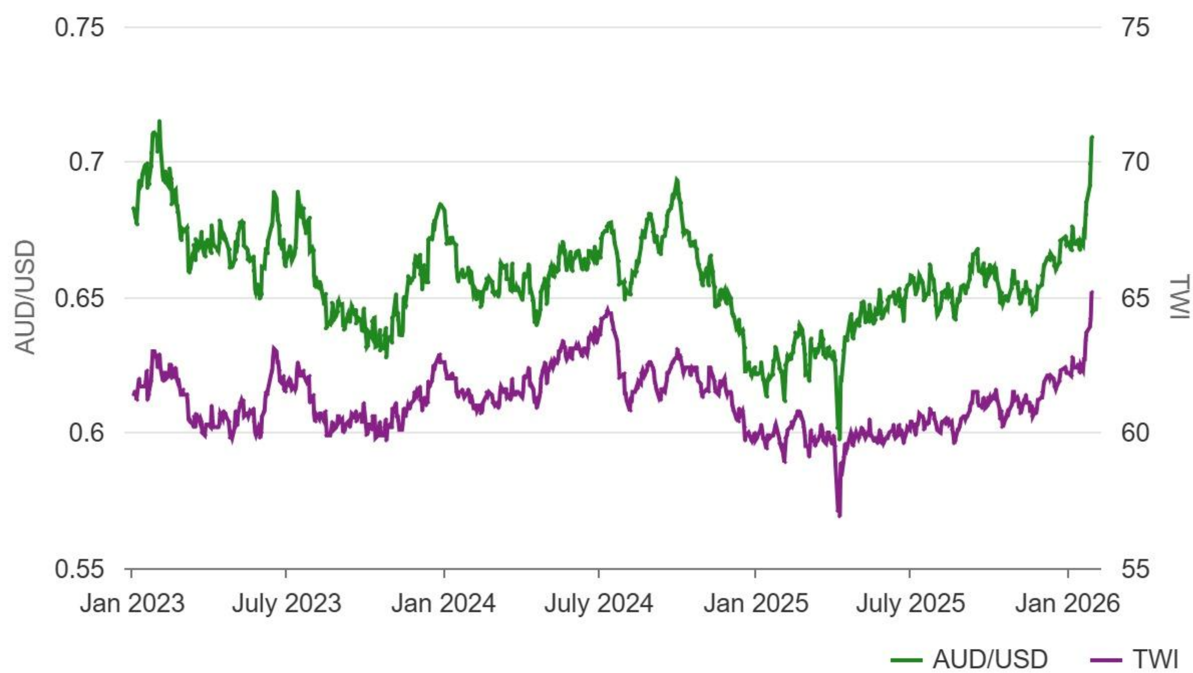
January 2026 - Australian Dollar Outlook

The Aussie Dollar has started 2026 with one of its sharpest one-month rallies in decades, and appears poised for a period of outperformance based on a range of indicators. Our forecasts continue to point to ongoing US Dollar weakness and also some specific factors that should see broader gains on a trade-weighted basis and on a range of A$ cross rates, as follows.

At the start of last year we noted the drivers of a stronger US Dollar that would likely dissipate through the year, so forecast a rally for the AUD/USD to 65 cents by mid-year and to 71 cents by the end of 2025. Pleasingly the mid-year target was achieved, which looked unlikely after the April 'liberation-day' US tariffs saw a plunge to .5910. However our core assumptions that Australia would be least adversely impacted by tariffs and that US trade policy would ultimately undermine the US Dollar, did eventuate. The subsequent moves in the second half of 2025 had similar themes, but the A$ was unable to exceed .6725. This year the AUD rally and the US Dollar selloff accelerated, and as the chart below shows the Aussie has just hit its highest level in 3years, while the Trade Weighted Index is now at an 8 year high.

AUD/USD Exchange Rates and TWI



Sources: WM/Reuters; RBA

From here, I certainly don't expect 'one-way traffic' and the quick one cent pullback from the .7090 high this week is a reminder of the likely volatility ahead, but the drivers of a weaker USD have included:

- Trade policy weakening the US Dollar- tariffs may keep weighing on the $ like the GBP with Brexit.
- Concerns of US Federal Reserve independence, ahead of a new Fed Chair to be appointed.
- Further US rate cuts expected despite evidence that inflation is persistent in the wake of tariffs.

- Diversification of assets by global investors away from the US amid geopolitical tensions.
- US fiscal sustainability given elevated debt levels and the reliance on foreign capital.

Having said this, the US Dollar remains the world's primary reserve currency and has safe-haven appeal, so Warren Buffett's quote 'Never bet against America' is a reminder of the need to be circumspect. Nevertheless, the number of reasons to expect a weaker greenback in 2026 appear to clearly outnumber the reasons to be bullish.

Similarly (beyond US Dollar weakness) there are a number of factors that have driven the Aussie Dollar higher against a range of currencies, evidenced by the 8 year high on the TWI. These include:
- The sudden market expectation of rate hikes, after the recent jump in core inflation to 3.35%.
- The appreciation of a range of key commodity prices, including iron ore, copper and gold.
- Australia has one of the strongest labour markets in the world, with unemployment down at 4.1%.
- Likely outperformance ahead in the AI revolution, given high tech investment and adoption rates.

The appreciation of the price of gold (and silver) has been extraordinarily, building on its safe haven appeal and increasing share of central bank reserves last year amid further geopolitical shocks (Venezuela, Iran and Greenland) and erosion of trust potentially seeing a new Bretton Woods pivot.

All of this is highly relevant for the Aussie Dollar, given Australia produces around 8% of global gold production and (with our AAA credit rating) the appeal of our bonds in this nascent environment of 'de-dollarisation'. It is also a good reminder of the offset that higher commodity prices will provide to exporters fearing a higher exchange rate. Of course volatility in the value of gold and other commodities is expected to persist, but the extent of this precious metal rally thus far is unparalleled.

Technically the AUD/USD has historically experienced its most impressive bull markets after sharp reversals (as we saw in April with the spike to .591 followed by an immediate jump to .645) - like the downside spikes seen during the pandemic (to .551) and the GFC (to .601). The latest rally has broken all technical resistance levels, although a pullback is generally seen after such rapid moves.

The impact of interest rate differentials is generally varied but always relevant for exchange rates, and the prospect of an imminent RBA hike is also feeding into the AUD/USD. Our forecasts have for some months been for no change to the Official Cash Rate for 2026 before a series of hikes next year (not just due to inflation, but also potentially with the 'neutral cash rate' moving higher). However, it's difficult to ignore the latest inflation and jobs data, both adding weight to a more imminent hike. We will see what the RBA Monetary Policy Decide next week, but if our expected hikes are brought forward this also places upside risks to the Aussie Dollar, and rate cuts appear to be off the table.

In summary, we expect the AUD/USD to trade in a new broad range of .675 to .75 for much of 2026, with risks to the topside and similar outperformance on cross rates (especially AUD/NZD, AUD/GBP and AUD/EUR).

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