2. International and Foreign Exchange Markets

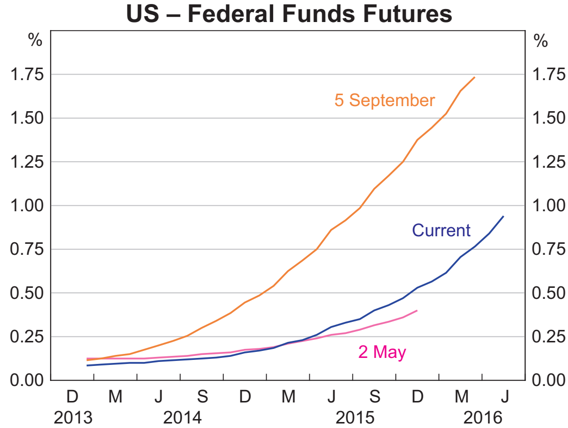
Shifting expectations regarding the future path of US monetary policy remained the focal point for markets over recent months. A widespread expectation that the US Federal Reserve would begin reducing the scale of its asset purchases at its September meeting saw global bond yields rise significantly and equity prices fall over August. In addition, there were significant depreciations of emerging market currencies amid large capital outflows, as well as a depreciation of the Australian dollar. These moves were reversed to varying degrees following a reassessment of the outlook for US monetary policy in response to the Federal Reserve's decision in September to maintain the size of its asset purchases.

Central Bank Policy

Markets had increasingly been expecting the Federal Reserve to announce a reduction in the pace of its asset purchase program following its September meeting, given earlier guidance. In the event, the Federal Reserve refrained from changing its policy at that meeting. It noted that while the economic outlook was little changed from June, when it first signalled an intention to scale back asset purchases, members wanted more certainty about this outlook before changing policy and were mindful of the impact that higher market interest rates were having on US economic activity. The Federal Reserve subsequently kept its asset purchase program unchanged at its October meeting, and continued to note that it is awaiting clearer signs that the current recovery will be sustained before adjusting policy. Most commentators now expect the Federal Reserve to begin reducing asset purchases at its March meeting, which would be the first chaired by Janet Yellen (subject to Senate confirmation).

Anticipation that the Federal Reserve would reduce its asset purchases at its September meeting saw market-implied expectations for the future path of the federal funds rate rise sharply between May and early September, despite repeated statements from the Federal Reserve that it did not expect policy interest rates to rise for a considerable period of time after purchases end (Graph 2.1). Expectations for future policy rates were then revised sharply lower following the September decision to maintain the scale of asset purchases. Markets are now pricing in the first increase in the federal funds rate to occur by November 2015, followed by a further 75 basis points of tightening over the subsequent year. The Federal Reserve has maintained its guidance that interest rates will not rise until the unemployment rate falls to at least 6½ per cent, provided its forecast for inflation one to two years ahead does not exceed

Graph 2.1
US – Federal Funds Futures

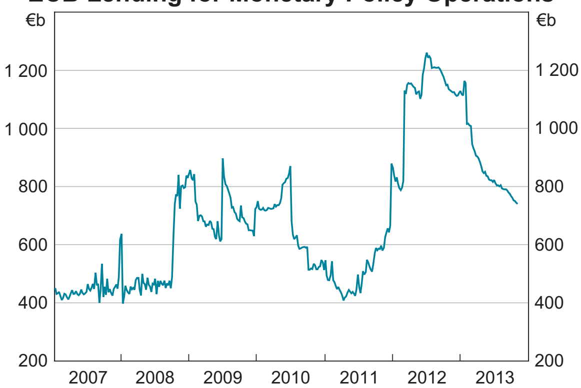


Source: Bloomberg

2½ per cent and expectations remain anchored, and has repeatedly noted that it may not raise rates until unemployment is well below the 6½ per cent threshold.

The European Central Bank (ECB) has maintained its policy stance at recent meetings, and continues to state that it expects interest rates to remain at current or lower levels for 'an extended period'. Lending for monetary policy purposes has continued to decline, falling by more than €60 billion since early August and by over €500 billion since its peak mid last year, as banks prepay loans extended as part of the ECB's long-term refinancing operations (Graph 2.2). The ECB has noted that it is prepared to respond if the resulting decline in liquidity exerts unwanted upward pressure on interbank interest rates.

Graph 2.2
ECB Lending for Monetary Policy Operations



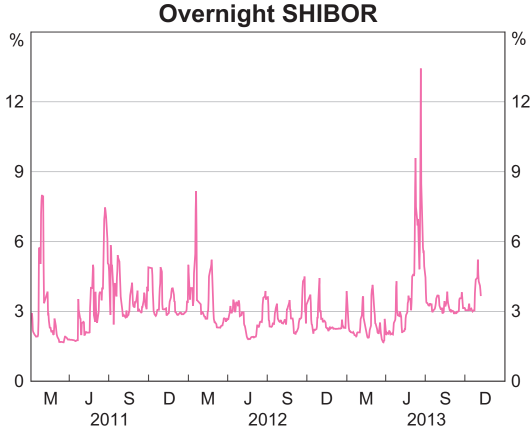
Source: European Central Bank

The Bank of England (BoE) maintained its policy settings and forward guidance at recent meetings, noting that the unemployment rate has declined more rapidly than envisaged in its August *Inflation Report* but that the appreciation of the pound has reduced inflationary pressures. In response to strengthening economic data, the market-implied expectation for the timing of the first increase in its policy rate has been brought forward over recent months to around mid 2015. The BoE also announced a number of operational changes to expand the potential scope of its liquidity provision arrangements, including lengthening the term of its lending to banks and reducing the cost and possible stigma associated with stressed banks temporarily accessing finance via the BoE.

The Bank of Japan (BoJ) has continued to purchase around ¥5–6 trillion of Japanese government bonds (JGBs) per month. This has seen the money base continue to grow rapidly over recent months. The BoJ has stated that the economy is recovering 'moderately', supported by this monetary stimulus, and has argued that it would be 'premature' to consider additional easing at this point.

Conditions in Chinese money markets have been relatively stable since the easing of the tensions that emerged in June. However, the Shanghai Interbank Offered Rate (SHIBOR) has averaged around 75 basis points higher in recent months compared with the year prior to June, and the People's Bank of China allowed liquidity conditions to tighten temporarily in late October (Graph 2.3).

Graph 2.3
Overnight SHIBOR



Source: CEIC Data

Central banks in several developing economies have tightened policy, citing a desire to counter expected pressure on inflation, resulting in part from recent currency depreciations, and reduce exchange rate volatility (Table 2.1). Bank Indonesia (BI) tightened policy by a total of 75 basis points in late August and early September, adding to the 75 basis point tightening earlier this year, citing high inflation, volatility in the rupiah and concerns about the current account deficit. BI also changed a number of other regulations in order to tighten domestic liquidity, attract foreign capital, and increase its ability to control excess liquidity in the interbank market. The Reserve Bank of India (RBI) raised its policy rate in September and October, though in recognition of reduced downward pressure on the rupee it also reversed much of the temporary liquidity tightening measures it had introduced in July. In order to minimise upward pressure on longer-term yields, the RBI has also purchased Indian government bonds and relaxed restrictions on the use of such bonds to meet banks' reserve requirement ratios. The central bank of Brazil tightened policy by 50 basis points in each of August and October, bringing the cumulative tightening since April to 225 basis points, and the central bank of Turkey raised the rate it charges banks on overnight loans by 50 basis points in August.

Table 2.1: Monetary Policy

	Policy rate Per cent		**Most recent change**	**Cumulative change in current cycle**[(a)] Basis points
Euro area	0.50	↓	May 13	–100
Japan[(b)]	na		na	
United States	0.125	↓	Dec 08	–512.5
Australia	2.50	↓	Aug 13	–225
Brazil	9.50	↑	Oct 13	225
Canada	1.00	↑	Sep 10	75
Chile	4.75	↓	Oct 13	–50
China	6.00	↓	Jul 12	–56
India	7.75	↑	Oct 13	50
Indonesia	7.25	↑	Sep 13	150
Israel	1.00	↓	Sep 13	–225
Malaysia	3.00	↑	May 11	100
Mexico	3.50	↓	Oct 13	–475
New Zealand	2.50	↓	Mar 11	–50
Norway	1.50	↓	Mar 12	–75
Russia[(c)]	5.50	↑	Sep 12	25
South Africa	5.00	↓	Jul 12	–700
South Korea	2.50	↓	May 13	–75
Sweden	1.00	↓	Dec 12	–100
Switzerland	0.00	↓	Aug 11	–275
Taiwan	1.875	↑	Jun 11	62.5
Thailand	2.50	↓	May 13	–100
United Kingdom	0.50	↓	Mar 09	–525

	Current monthly asset purchases	**Most recent change**	**Assets on balance sheet** Per cent of GDP
United States	$85 billion	Sep 12	23.0
Japan	¥6 trillion	Apr 13	44.9
United Kingdom	0	Jul 12	25.1

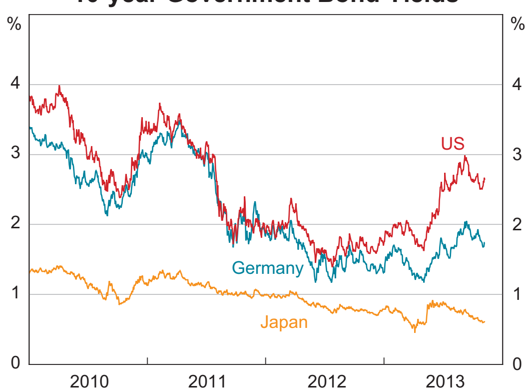
(a) Current rate relative to most recent trough or peak
(b) Since April 2013, the Bank of Japan's main operating target has been the money base
(c) The central bank of Russia changed the interest rate it uses as its policy rate in September 2013
Sources: RBA; Thomson Reuters; central banks

In contrast, the central banks of Mexico, Chile and Israel all eased policy in response to weaker economic activity.

Sovereign Debt Markets

Yields on 10-year US Treasuries rose notably over August and early September, to exceed 3 per cent for the first time in more than two years, in response to firming expectations that the Federal Reserve would begin to scale back its asset purchase program at its mid September meeting (Graph 2.4). However, this move higher was fully unwound over September as markets revised their expectations for future US monetary policy in light of the Federal Reserve's September decision and weaker-than-expected employment data. On net, yields have been unchanged since then, despite temporarily rising in early October as negotiations on the debt ceiling proved difficult. Yields remain 100 basis points higher than in early May.

Graph 2.4
10-year Government Bond Yields

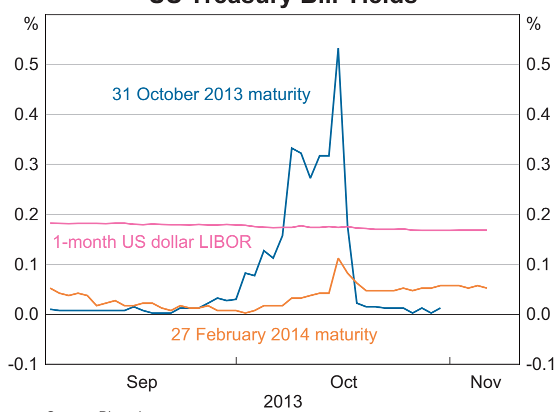


Source: Bloomberg

The inability of the US Congress to agree on a 'continuing resolution' to extend government spending authority beyond 30 September saw 'non-essential' services of the US federal government shut for 16 days in early October, with around one-third of government employees sent on temporary leave. While this attracted little immediate reaction from markets, the US Treasury's forecast that it could not guarantee payment of its obligations to creditors and/or the general public beyond 17 October unless Congress agreed to raise the legal ceiling on the federal government's debt stock created considerable uncertainty in US Treasury markets. In the event, Congress passed legislation on 16 October to provide spending authority until 15 January and suspend the debt ceiling until 7 February.

In response to concerns that this could lead to a delay in payment to holders of some US Treasuries, yields on Treasury bills and bonds maturing between 17 October and mid November rose by up to 60 basis points ahead of the passage of legislation to extend Treasury's borrowing authority (Graph 2.5). Securities maturing at other dates were initially unaffected as US Treasuries do not 'cross-default'. However, as it became increasingly clear that any agreement would only extend the debt ceiling until early 2014, yields on bills maturing around that time also rose notably. These increases – particularly on October and November bills – were largely unwound following the legislative agreement.

Graph 2.5
US Treasury Bill Yields



Source: Bloomberg

Yields on German 10-year Bunds have broadly followed those on 10-year Treasuries. Yields reached 2 per cent in early September for the first time in 18 months but have since declined by around 25 basis points. Yields on UK 10-year Gilts have risen relative to Treasuries and Bunds, alongside stronger UK data.

In contrast, yields on 10-year JGBs have continued to drift down from their peak in May, while volatility in JGB yields has been low. The Bank of Japan continues to exert a sizeable influence on the market, having increased its share of total JGBs outstanding by 4 percentage points since April, to 16 per cent. This rise in its holdings has been matched by a ¥25 trillion reduction in JGB holdings by local banks since the introduction of the Quantitative and Qualitative Monetary Easing program in April. On net, there has been little change in Japanese banks' and other residents' holdings of foreign bonds in recent months.

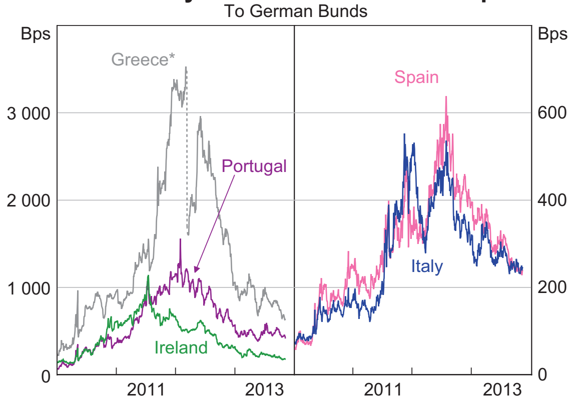
Spreads between yields on long-term bonds issued by the Greek Government and German Bunds have narrowed by more than 200 basis points since early September, while spreads on other euro area periphery countries' bonds narrowed by between 20 and 130 basis points (Graph 2.6). The narrowing of Greek government bond spreads reflects increasing confidence that the government will achieve a primary budget surplus this year and some positive signs of progress on its privatisation program. Indications that the Portuguese governing coalition has become more stable and committed to meeting the requirements under its bailout program contributed to a narrowing of Portuguese spreads. Italian and Spanish spreads drifted lower as threats to the stability of the Italian ruling coalition dissipated and investors grew more comfortable with the progress of 'peripheral' economies. Ireland is expected to successfully exit its financial assistance program at the end of this year, possibly with a precautionary credit line to smooth its transition to full market funding.

Yields on 10-year local currency bonds issued by several emerging market sovereigns have increased notably over recent months, despite receding significantly since the US Federal Reserve's September decision (Graph 2.7). At their peaks in late August, yields on Brazilian, Indonesian, South African and Turkish local currency government bonds had risen by between 250 and 400 basis points, unwinding the declines observed between 2011 and early 2013. Yields on local currency bonds issued by these governments rose somewhat more than those on US dollar-denominated bonds, suggesting some increased premia for currency risk. These increases in yields occurred alongside significant outflows of foreign capital from these and other emerging market economies as investors grew concerned about the difficulties these economies may face in financing large current account deficits when the US Federal Reserve slows its monetary stimulus. While the size of certain countries' current account deficits was the focus of investor attention, exposure to foreign currency borrowing risk, rapid credit growth and/or substantial asset price inflation over recent years also provoked some concern. However,

Graph 2.6

Euro Area 10-year Government Bond Spreads

To German Bunds



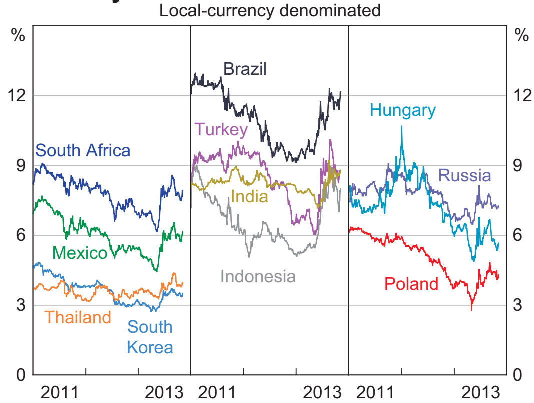
* Data from 12 March 2012 are yields on Greek bonds post first private sector debt swap

Source: Bloomberg

Graph 2.7

10-year Government Bond Yields

Local-currency denominated



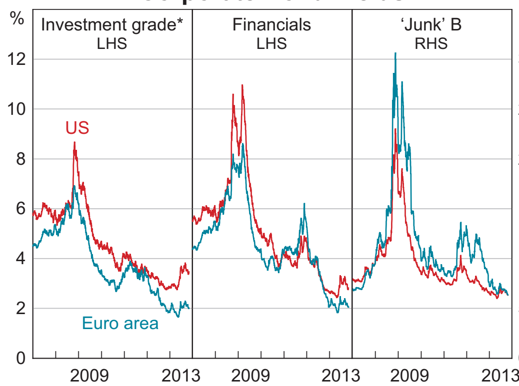
Sources: Bloomberg; Thomson Reuters

a general decline in external debt outstanding, improved macroeconomic policy frameworks and higher levels of foreign currency reserves over the past 15 years suggest that these countries are less vulnerable to a balance of payments crisis than at the time of the Asian financial crisis.

Credit Markets

Credit remains readily available for most corporations in the United States and Europe. Indicative of this, US telecommunications company Verizon issued US$49 billion of investment grade bonds in September – the largest ever non-financial corporate bond issue. Yields on investment grade corporate bonds in the United States and euro area have changed only modestly over recent months, but yields on sub-investment grade securities issued by US and European corporations have declined by 75 and 120 basis points since their recent peaks midyear (Graph 2.8). Spreads between sub-investment grade corporate and sovereign bond yields in the United States and euro area are now narrower than in early May.

Graph 2.8
Corporate Bond Yields

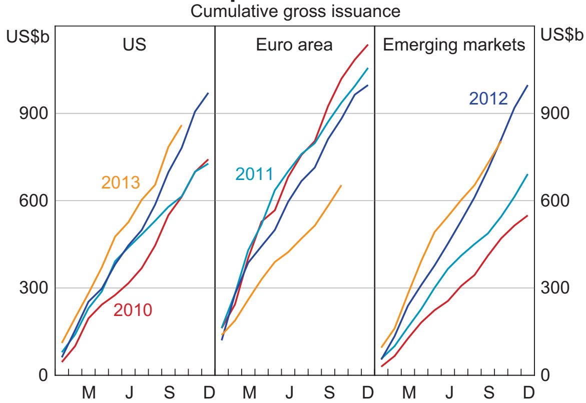


* Non-financial corporations

Sources: Bank of America Merrill Lynch; Bloomberg; RBA

Bond issuance by US corporations has picked up since early September and remains healthy over 2013 (Graph 2.9). In contrast, issuance by euro area corporations continues to be well below that seen in recent years, notwithstanding favourable pricing. Issuance by emerging market corporations has been subdued since June.

Graph 2.9
Global Corporate Bond Issuance
Cumulative gross issuance

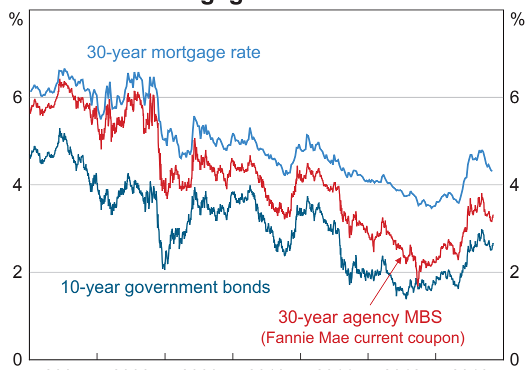


Source: Dealogic

The availability of short-term secured financing in the US tightened notably in the first half of the month due to the possibility of a default on US Treasury bills, which are commonly used as collateral in repurchase agreements (repos). In the week prior to the deadline, Treasury repo rates spiked higher and the volume of transactions using Treasuries as collateral declined – particularly for terms longer than overnight – amid reports that cash lenders were refusing to accept as collateral securities that were vulnerable to a technical default. There were also significant outflows from institutional money market funds that invest only in US Treasuries and/or agency securities; US$56 billion (6 per cent of assets under management) was withdrawn from these funds in the two weeks leading up to the deadline, before reversing around half these flows following the suspension of the debt ceiling. The outflow from such funds in the week of the debt ceiling deadline was the largest weekly outflow since mid 2009.

Yields on US agency mortgage-backed securities (MBS) have moved in response to changes in yields on Treasuries, reaching their highest level in more than two years in early September before retracing by around 50 basis points (Graph 2.10). Nonetheless, yields remain around 100 basis points higher than in early May. US mortgage interest rates have moved in line with yields on agency MBS, and despite their recent decline remain well above the levels observed in 2012.

Graph 2.10
US Mortgage Interest Rates



Sources: Bloomberg; Thomson Reuters

Equities

Global share prices have increased by 5 per cent since the previous *Statement*, with much of this occurring since September, to be almost 20 per cent higher over 2013 to date (Table 2.2). Markets' reassessment of the outlook for US monetary policy has been the most important contributor to recent increases.

Among advanced economies, recent increases have been larger in the euro area than in the United States (Graph 2.11). Nonetheless, US share prices have continued to reach new record highs in recent months. In contrast to similar events in 2011, share prices fell only modestly during the impasse over the US debt ceiling (and quickly reversed these losses following the suspension of the ceiling until next year), while volatility in share prices rose only modestly and briefly.

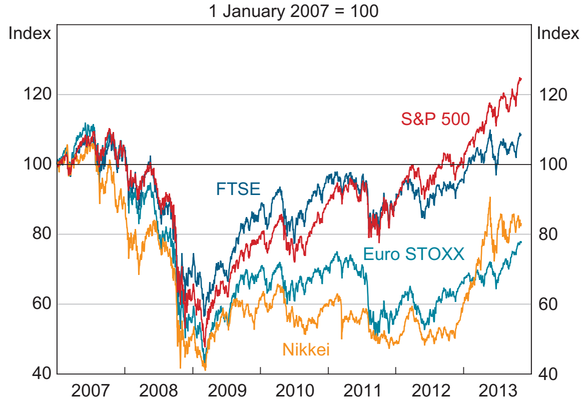
Third quarter profit results for US financial institutions were broadly in line with expectations in aggregate, though varied across institutions. Most banks recorded a decline in profits as a result of reduced earnings from fixed income trading services, due

Table 2.2: Changes in International Share Prices
Per cent

	Since end 2012	Since previous *Statement*
United States		
– S&P 500	24	5
Euro area		
– STOXX	18	9
United Kingdom		
– FTSE	14	4
Japan		
– Nikkei	38	4
Canada		
– TSE 300	8	8
Australia		
– ASX 200	17	8
China		
– China A	–6	5
MSCI indices		
– Emerging Asia	2	8
– Latin America	–5	7
– Emerging Europe	2	9
– World	**19**	**5**

Source: Bloomberg

Graph 2.11
Share Price Indices
1 January 2007 = 100



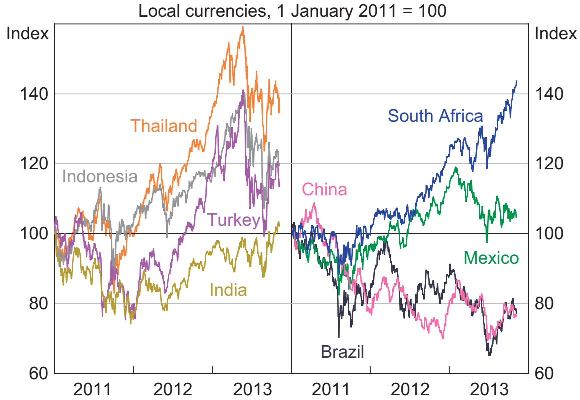
Source: Bloomberg

to low levels of bond trading ahead of the Federal Reserve's September meeting, and a fall in mortgage refinancing volumes following the rise in mortgage interest rates. Partially offsetting these falls, loan loss expenses declined. Euro area banks' underlying profits in the third quarter were quite varied, with a number reporting reduced income from bond trading while others benefited from lower loan loss and other expenses. Both US and euro area banks also raised provisions for litigation expenses, in expectation of fines and compensation payments related to the sale of MBS and insurance, as well as manipulation of interest rate and foreign exchange benchmarks (some of which have already settled). Nonetheless, European bank shares have significantly outperformed other sectors in the region over recent months, rising by almost 20 per cent since late August, with abating political tensions in Italy having a more pronounced effect on the share price of financial institutions than on other companies.

These gains occurred despite the details of the ECB's planned comprehensive assessment of the banking system, which were released in October, being perceived as stricter than initially expected. The ECB will report its findings in November 2014 on three aspects of its assessment: banks' resilience to key balance sheet risks, such as liquidity, leverage and funding risks; a review of banks' asset quality and the risk weights applied to various assets; and a stress test of banks' ability to maintain a minimum 8 per cent Common Equity Tier 1 capital ratio following as-yet-undetermined shocks.

Share prices in developing economies have been buffeted by the shifting expectations regarding the outlook for US monetary policy. The growing expectation that the Federal Reserve would reduce the scale of its asset purchases from September saw share prices fall by more than 10 per cent in some cases between early August and early September (Graph 2.12). However, these declines have since been more than reversed, with the MSCI Emerging Markets Index now almost 10 per cent higher than at the time of the previous *Statement*. Improving Chinese economic data were an additional factor supporting emerging market share prices, including in commodity exporting nations such as Brazil, Russia and South Africa, while the reduced prospect of military action against Syria supported Turkish shares.

Graph 2.12
Emerging Market Share Price Indices
Local currencies, 1 January 2011 = 100

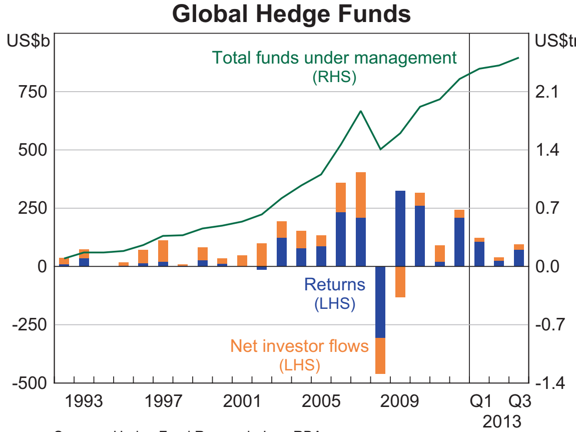


Source: Bloomberg

Hedge Funds

Global hedge funds recorded an average return on investments of 7.1 per cent over the year to September – less than the total return from a balanced portfolio of global bonds and equities (including dividends) over the period – with returns picking up in the quarter to 2.2 per cent. Funds under management increased by 3.9 per cent over the September quarter to US$2.5 trillion, mostly reflecting a positive return from investments (Graph 2.13).

Graph 2.13
Global Hedge Funds

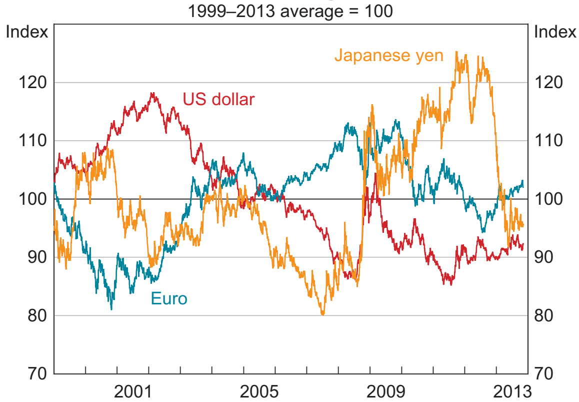


Sources: Hedge Fund Research, Inc.; RBA

Foreign Exchange

Foreign exchange markets have also been influenced by changes in market expectations about the timing of future reductions in the pace of asset purchases by the Federal Reserve. From May to August, the US dollar appreciated modestly on a trade-weighted basis amid growing market expectations that the Federal Reserve would begin to reduce its asset purchases in September. But the Fed's decision to leave monetary policy unchanged at its September meeting, and the uncertainty surrounding the US fiscal situation, have seen the US dollar depreciate against a number of currencies to be slightly lower on a broad trade-weighted basis since the end of August (Graph 2.14, Table 2.3). Foreign exchange market volatility has declined to relatively low levels over recent months, notwithstanding the heightened policy uncertainty in the United States.

Graph 2.14
Nominal Trade Weighted Indices
1999–2013 average = 100



Sources: BIS; Bloomberg; Board of Governors of the Federal Reserve System; RBA

The euro has appreciated by 2 per cent against the US dollar since the end of August but has been little changed on a trade-weighted basis over the period. In contrast, the Japanese yen has been little changed against the US dollar and has depreciated by 2 per cent on a trade-weighted basis over the period. On a trade-weighted basis, the yen nevertheless remains around 4 per cent above its trough in May.

Table 2.3: Changes in the US Dollar against Selected Currencies
Per cent

	Over the past year	Since end August
Indonesian rupiah	19	4
Japanese yen	23	1
South African rand	19	0
Chinese renminbi	–2	0
Canadian dollar	5	–1
New Taiwan dollar	1	–2
Mexican peso	1	–2
Swiss franc	–3	–2
Swedish krona	–3	–2
European euro	–5	–2
Singapore dollar	2	–3
Thai baht	2	–3
Philippine peso	5	–3
UK pound sterling	–1	–4
Malaysian ringgit	4	–4
Brazilian real	12	–4
South Korean won	–3	–4
Indian rupee	15	–6
Australian dollar	9	–7
New Zealand dollar	–1	–8
Majors TWI	**3**	**–2**
Broad TWI	**2**	**–2**

Sources: Bloomberg; Board of Governors of the Federal Reserve System

The US Federal Reserve, ECB, BoJ, BoE, Bank of Canada and the Swiss National Bank have agreed to convert their existing temporary bilateral liquidity swap arrangements into standing arrangements. The bilateral swap network allows foreign currency liquidity to be provided to each jurisdiction (in any of the five currencies foreign to that jurisdiction) provided that both parties to a particular bilateral swap arrangement judge that it is warranted by market conditions.

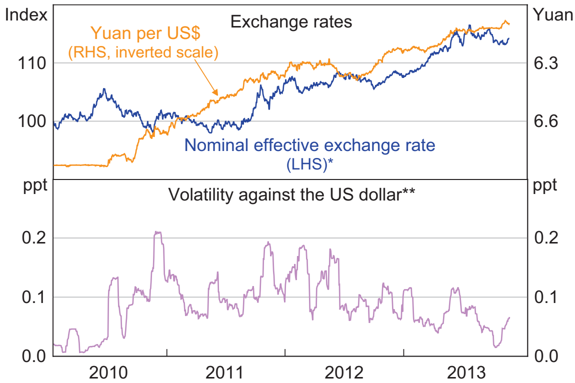
The Chinese renminbi (RMB) traded in an especially narrow range against the US dollar between late August and mid October and, consistent with this, daily volatility in the RMB declined to levels not seen since 2010 (Graph 2.15). Although the RMB has remained little changed against the US dollar for some time, it has depreciated by around 2 per cent on a nominal effective basis since its peak in early July, in part reflecting the appreciation of the euro and the Korean won over the period.

Chinese foreign currency reserves increased by US$166 billion (around 5 per cent) over the September quarter, reflecting net purchases of foreign currency reserves of US$98 billion and positive valuation effects (Graph 2.16). A sizeable share of these purchases appear to have been made in September, which is consistent with the period of unusual stability in the RMB despite reports of increased capital inflows around this time. Most other Asian and emerging market countries' foreign currency reserves have also increased over recent months (discussed below).

Further steps have been taken towards internationalising the RMB. The United Kingdom and Singapore have both been allocated quotas under the RMB Qualified Foreign Institutional Investor (RQFII) scheme, which will allow approved UK- and Singapore-based financial institutions to invest RMB acquired offshore in approved Mainland Chinese securities. The UK and Singapore authorities also announced that there will be 'direct trading' between their respective currencies and the RMB in the onshore market – that is, trading between these currencies without the use of the US dollar as an intermediate currency. In addition, the Chinese authorities have signed or extended bilateral local currency swap agreements with a number of jurisdictions (including the euro area) and simplified regulations covering specific types of foreign investment.

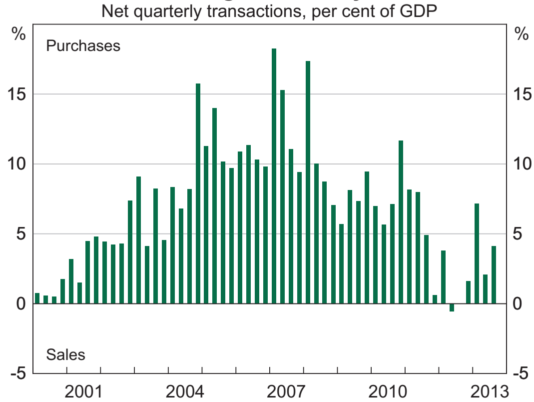
After having generally depreciated between May and August, most other Asian and Latin American currencies have since appreciated against the US dollar, and volatility has receded from elevated levels (Graph 2.17). Most of these currencies nevertheless remain below their end-April levels,

Graph 2.15
Chinese Renminbi



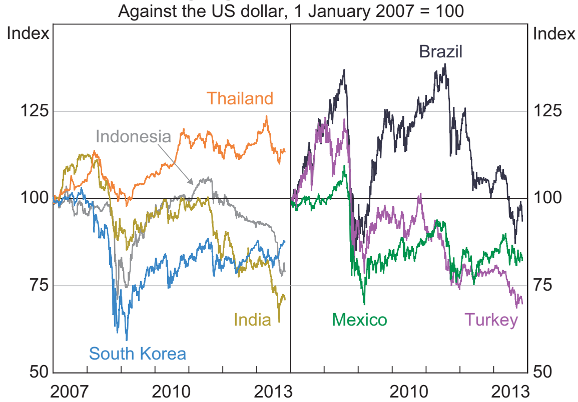
* 1 January 2010 = 100
** Rolling 22-day standard deviation of daily percentage changes
Sources: BIS; Bloomberg; RBA

Graph 2.16
Chinese Foreign Currency Reserves
Net quarterly transactions, per cent of GDP



Sources: Bloomberg; CEIC Data; RBA

Graph 2.17
Emerging Market Currencies
Against the US dollar, 1 January 2007 = 100



Source: Bloomberg

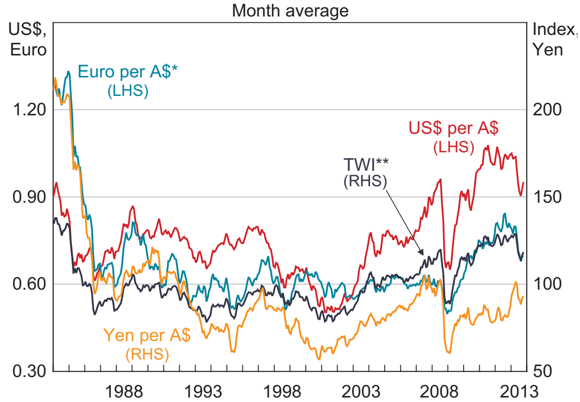
with the exception of the Korean won. In contrast, the Indian rupee and the Indonesian rupiah remain well below their end-April levels, with authorities in both countries announcing further policy measures designed to encourage capital inflows and/or curb volatility in their exchange rates in August and September. These countries have also established or extended bilateral local currency swap agreements with other Asian countries.

Most Asian and other emerging market countries' gross foreign currency reserves have increased since the end of August, consistent with an abatement in depreciation pressures on their currencies and lower exchange rate volatility (Table 2.4). Positive valuation effects related to the depreciation of the US dollar since the end of August are likely to have contributed to these increases. However, a number of countries' gross foreign currency reserves remain below their end-April levels – including Indonesia and India – consistent with reports of sustained intervention in foreign exchange markets by the authorities in these countries between May and August. While the authorities in Brazil continue to intervene in foreign exchange markets to support the local currency, this has primarily been conducted through auctions of derivatives that are settled in local currency and are therefore not included in gross foreign currency reserves.

Australian Dollar

After reaching its lowest level in three years on a trade-weighted basis in early August, the Australian dollar has since appreciated against most other currencies to be around 5 per cent higher in trade-weighted terms (Graph 2.18, Table 2.5). Similar to other currencies, the Australian dollar has appreciated against the US dollar as market participants have adjusted their expectations about the timing of future reductions in asset purchases by the Federal Reserve. The Australian dollar has also been affected by a scaling back of market

Graph 2.18
Australian Dollar
Month average



* Deutsche Mark spliced on to euro prior to 4 January 1999
** Indexed to post-float average = 100
Sources: Bloomberg; RBA; Thomson Reuters; WM/Reuters

Table 2.4: Gross Foreign Currency Reserves
As at end October 2013

	Percentage change since:		Level
	End April	End August	US$ equivalent (billions)
China[b]	4	3	3 663
Russia[b]	1	3	462
Taiwan[a]	3	2	416
Brazil	0	3	367
South Korea	4	4	332
India	–3	3	255
Thailand[b]	–3	2	163
Turkey	–1	4	111
Indonesia	–10	5	90

(a) Official reserve assets (includes foreign currency and other reserve assets)
(b) End September
Sources: Bloomberg; CEIC Data; IMF; RBA

expectations for additional cuts to the domestic cash rate and broadly positive Chinese economic data. In trade-weighted terms, the Australian dollar nevertheless remains around 10 per cent below its April peak, though it is still at a high level.

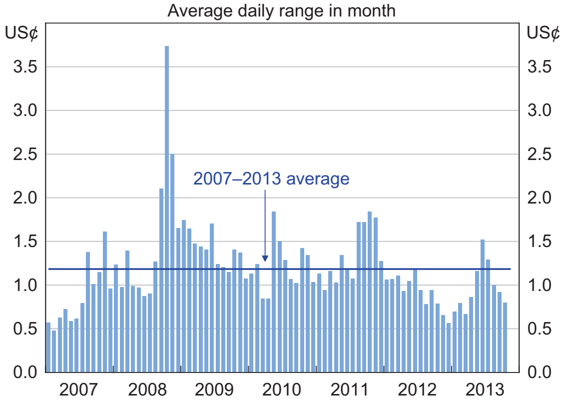
Consistent with developments in other currency markets, intraday volatility in the Australian dollar has declined over recent months and has returned towards the low levels recorded at the beginning of the year (Graph 2.19).

Table 2.5: Changes in the Australian Dollar against Selected Currencies
Per cent

	Since April peak in TWI[(a)]	Since August trough in TWI[(b)]
Indonesian rupiah	6	18
South African rand	4	11
Indian rupee	4	10
Canadian dollar	–7	7
Japanese yen	–11	7
US dollar	–10	7
Thai baht	–3	6
Chinese renminbi	–11	6
Malaysian ringgit	–5	5
Swiss franc	–12	5
European euro	–13	5
Singapore dollar	–9	4
UK pound sterling	–14	2
South Korean won	–16	2
New Zealand dollar	–8	0
TWI	**–10**	**6**

(a) 11 April 2013
(b) 6 August 2013
Sources: Bloomberg; WM/Reuters

Graph 2.19
Intraday Range in AUD/USD
Average daily range in month

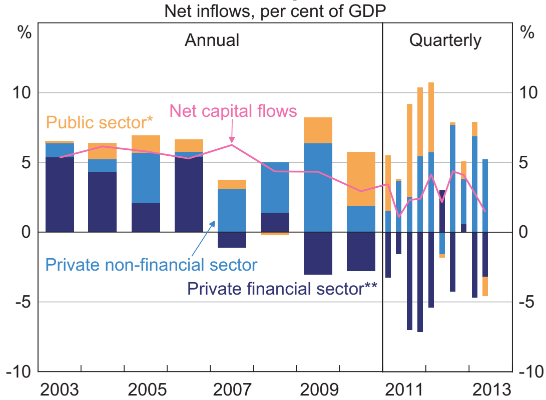


Sources: Bloomberg; RBA

Capital Flows

Net capital inflows to the Australian economy were directed entirely to the private non-financial sector in the June quarter, with relatively large net inflows to this sector also evident throughout the past year (Graph 2.20). The net inflow to the private non-financial sector in the June quarter – which consisted of both debt and equity investment – more than offset a further net outflow from the

Graph 2.20
Australian Capital Flows
Net inflows, per cent of GDP



* Excludes official and other RBA flows
** Adjusted for the US dollar swap facility in 2008 and 2009
Sources: ABS; RBA

private financial sector, as well as a relatively rare net outflow from the public sector. The net outflow from the private financial sector reflected a withdrawal of deposits from the banking sector by foreigners and an increase in loans by the Australian banking sector to non-residents, while the net public sector outflow primarily reflected a net outflow from state and local government debt. In contrast, the foreign ownership share of Commonwealth Government securities was broadly unchanged at 68 per cent as at the end of June, consistent with a small net capital inflow to the national government sector in the quarter.

Australian entities have had a net foreign liability position equivalent to 55–60 per cent of GDP over the past five years or so. However, the latest ABS survey of Foreign Currency Exposure indicates that, after accounting for the currency composition of foreign assets and liabilities and the extent to which they are hedged back into Australian dollars, Australian entities had an effective net foreign currency asset position of a little more than 30 per cent of GDP at the end of March 2013. See 'Box A: Foreign Currency Exposure and Hedging in Australia' for further details.