

FX FORECASTS

Despite Uncertainty about the US Debt Ceiling, the Greenback Rose in May!

HIGHLIGHTS

- ▶ It may seem surprising that the US dollar appreciated as concerns over US federal debt ceiling negotiations increased in May. Without an agreement between Republicans and Democrats, the United States could have defaulted on some of its payments as soon as early June, though the House and Senate still need to pass the bill. Any other country with this level of risk would likely have suffered a significant currency devaluation.
- ▶ For financial markets, US dollars are akin to the blood flowing in our veins. We'll always need blood to survive, and the financial markets will always need US dollars to thrive, especially in times of high uncertainty. A shift in US monetary policy expectations has also helped the greenback. In March, markets expected the Fed to cut rates earlier in response to the difficulties facing some regional banks. Now, markets are partially pricing in another rate hike given recent limited progress on inflation and the resilience of the US economy.
- ▶ Weakness of other currencies is also helping the US dollar look good. The euro is being hampered by the European Central Bank's more cautious approach to its interest rate hikes despite still-high inflation. European economic data has been sluggish too, with Germany posting two consecutive quarterly declines in real GDP, among other things.
- ▶ The pound sterling is also under pressure. Inflation remains a major headache in the United Kingdom, although the year-over-year headline figure has dropped below 10%. The annualized 3-month change in inflation excluding volatile items such as energy and food prices is more than 12%. That's very high and likely means the Bank of England has more to do. Although additional interest rate hikes are often seen as supportive of currency appreciation, the reality is that economic growth will need to be further curbed to bring inflation down to 2%, which could hurt the pound.
- ▶ The Canadian dollar is currently trading at nearly C\$1.36/US\$ (around US\$0.735)—similar to where it was at the beginning of May—and appreciated as high as C\$1.34/US\$ during the month. The loonie didn't benefit much from commodity prices, but generally positive Canadian economic data helped it maintain its position against the US dollar. Investors aren't ruling out the possibility of another rate hike, especially since inflation was stronger than expected in April.

MAIN FACTORS TO WATCH

- ▶ The US House and Senate now hold the keys to ending the debt ceiling drama. After that, we'll need to keep an eye on inflation and the health of the major economies. This will have an impact on investor risk aversion and interest rate expectations. Our currency forecasts are pricing in a deterioration in economic data, which should underpin the US dollar. We expect US and Canadian key interest rates to remain the same, but monetary tightening will need to continue in Europe. However, this should not be enough to support European currencies against the greenback.
- ▶ The Canadian dollar is expected to weaken slightly in the coming months, ending the summer at around C\$1.39/US\$ (US\$0.72).

Jimmy Jean, Vice-President, Chief Economist and Strategist • Hendrix Vachon, Principal Economist

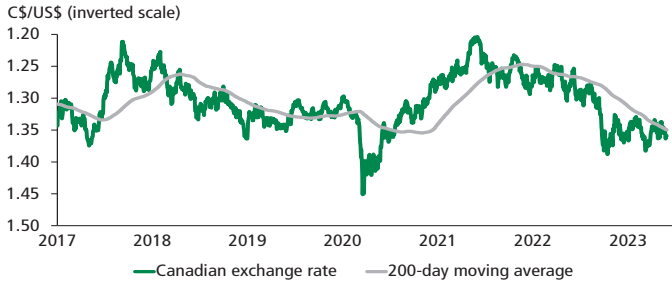
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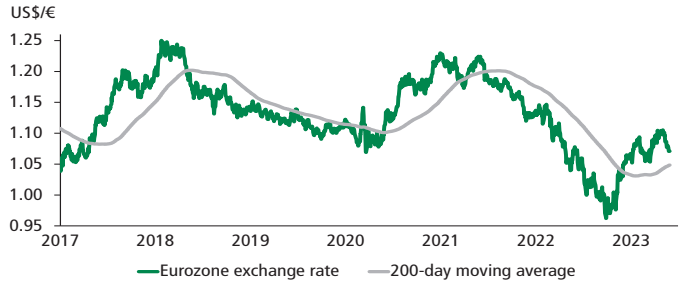
Main Exchange Rates

CANADIAN DOLLAR Exchange rate and trend



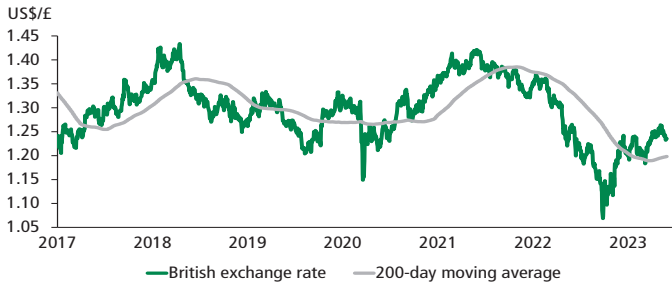
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EURO Exchange rate and trend



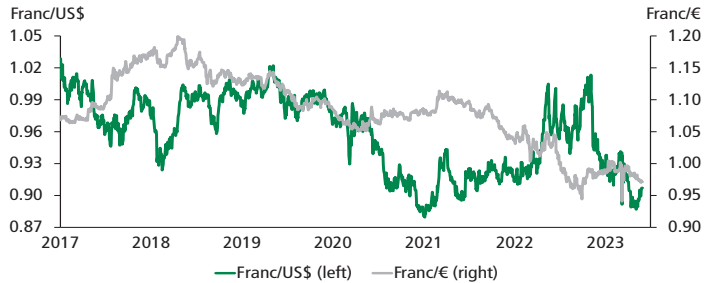
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BRITISH POUND Exchange rate and trend



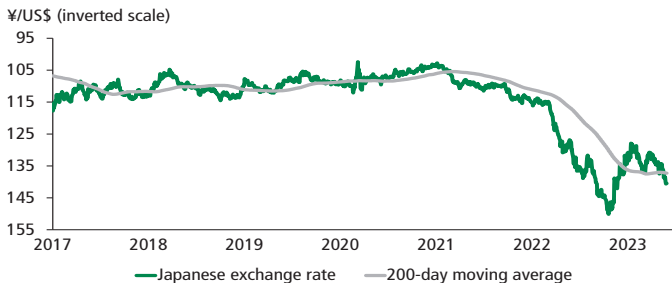
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SWISS FRANC Exchange rate



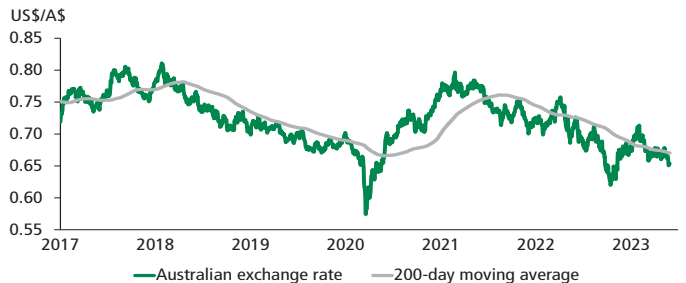
Sources: Datastream and Desjardins Economic Studies

YEN Exchange rate and trend



Sources: Datastream and Desjardins Economic Studies

AUSTRALIAN DOLLAR Exchange rate and trend



Sources: Datastream and Desjardins Economic Studies

TABLE 1
Currency market: Yields

COUNTRY – CURRENCY*	SPOT PRICE		% CHANGE				LAST 52 WEEKS		
	May 29	1-month	3-month	6-month	1-year	High	Average	Low	
Americas									
Argentina – peso	238.2510	7.04	20.58	42.71	99.27	238.2510	168.9549	119.5640	
Brazil – real	5.0085	0.11	-3.57	-5.48	5.87	5.4854	5.1739	4.7309	
Canada – (USD/CAD)	1.3593	0.22	-0.08	0.13	6.53	1.3879	1.3348	1.2537	
Canada – (CAD/USD)	0.7357	-0.22	0.08	-0.13	-6.13	0.7977	0.7492	0.7205	
Mexico – peso	17.5390	-2.77	-3.29	-8.69	-10.46	20.9440	19.3264	17.4695	
Asia and South Pacific									
Australia – (AUD/USD)	0.6538	-1.18	-3.30	-2.24	-8.70	0.7266	0.6758	0.6197	
China – yuan renminbi	7.0730	2.33	2.97	-1.21	5.59	7.3029	6.9118	6.6540	
Hong Kong – dollar	7.8282	-0.27	-0.27	0.23	-0.27	7.8501	7.8385	7.7674	
India – rupee	82.6135	1.06	0.22	1.21	6.43	83.0205	81.1666	77.3985	
Japan – yen	140.45	3.05	3.13	1.26	10.48	150.15	136.66	127.13	
New Zealand – (NZD/USD)	0.6053	-2.15	-3.26	-2.37	-7.39	0.6560	0.6179	0.5565	
South Korea – won	1,324	-1.04	0.09	-0.17	5.43	1,440	1,320	1,220	
Europe									
Denmark – krona	6.9566	2.83	-0.26	-3.38	0.39	7.7519	7.1284	6.7348	
Eurozone – (EUR/USD)	1.0709	-3.00	0.35	3.40	-0.01	1.1053	1.0452	0.9621	
Norway – kroner	11.1075	4.47	7.06	11.01	17.37	11.1075	10.1780	9.3727	
Russia – ruble	80.5000	0.37	7.21	31.32	19.08	82.7500	67.2495	53.4500	
Sweden – krona	10.8070	5.31	3.56	2.14	10.15	11.3655	10.4903	9.7141	
Switzerland – Swiss franc	0.9042	1.58	-3.75	-4.96	-5.51	1.0133	0.9450	0.8869	
United Kingdom – (GBP/USD)	1.2353	-1.72	2.89	2.94	-2.07	1.2646	1.2023	1.0747	

* In comparison with the US dollar, unless otherwise indicated.
Note: Currency table based on the previous day's close.

TABLE 2
Currency market: History and forecasts

END OF PERIOD	2022		2023				2024				
	Q3	Q4	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f	
US dollar											
Canadian dollar	USD/CAD	1.3828	1.3551	1.3516	1.3605	1.3889	1.3699	1.3333	1.2821	1.2500	1.2658
Euro	EUR/USD	0.9797	1.0673	1.0865	1.0700	1.0500	1.0600	1.0900	1.1200	1.1400	1.1500
British pound	GBP/USD	1.1163	1.2029	1.2365	1.2300	1.2100	1.2100	1.2400	1.2800	1.3000	1.3200
Swiss franc	USD/CHF	0.9842	0.9227	0.9132	0.9200	0.9300	0.9400	0.9500	0.9600	0.9600	0.9600
Yen	USD/JPY	144.77	131.13	132.81	135.00	128.00	123.00	117.00	113.00	111.00	110.00
Australian dollar	AUD/USD	0.6404	0.6814	0.6686	0.6500	0.6400	0.6500	0.6700	0.6900	0.7000	0.7000
Chinese yuan	USD/CNY	7.1160	6.8986	6.8690	7.0500	7.1000	7.1000	7.0000	6.9000	6.8500	6.8000
Mexican peso	USD/MXN	20.15	19.49	18.02	18.00	19.00	19.00	18.50	18.00	17.75	17.50
Brazilian real	USD/BRL	5.4063	5.2174	5.0801	5.1000	5.3000	5.3000	5.2000	5.1000	5.0000	4.9000
Effective dollar ¹		123.76	115.79	114.69	116.00	117.00	115.50	112.00	108.90	106.80	106.50
Canadian dollar											
US dollar	CAD/USD	0.7232	0.7380	0.7399	0.7350	0.7200	0.7300	0.7500	0.7800	0.8000	0.7900
Euro	EUR/CAD	1.3547	1.4462	1.4684	1.4558	1.4583	1.4521	1.4533	1.4359	1.4250	1.4557
British pound	GBP/CAD	1.5436	1.6300	1.6712	1.6735	1.6806	1.6575	1.6533	1.6410	1.6250	1.6709
Swiss franc	CAD/CHF	0.7117	0.6809	0.6756	0.6762	0.6696	0.6862	0.7125	0.7488	0.7680	0.7584
Yen	CAD/JPY	104.69	96.76	98.26	99.23	92.16	89.79	87.75	88.14	88.80	86.90
Australian dollar	AUD/CAD	0.8856	0.9233	0.9037	0.8844	0.8889	0.8904	0.8933	0.8846	0.8750	0.8861
Chinese yuan	CAD/CNY	5.1461	5.0908	5.0821	5.1818	5.1120	5.1830	5.2500	5.3820	5.4800	5.3720
Mexican peso	CAD/MXN	14.57	14.38	13.33	13.23	13.68	13.87	13.88	14.04	14.20	13.83
Brazilian real	CAD/BRL	3.9097	3.8502	3.7586	3.7485	3.8160	3.8690	3.9000	3.9780	4.0000	3.8710

f: forecasts; ¹ Trade-weighted against major US partners (January 2006 = 100).
Sources: Datastream, Federal Reserve Board and Desjardins Economic Studies