

FX FORECASTS

The Canadian dollar's resilience has its limits

HIGHLIGHTS

- ▶ Most currencies have depreciated against the U.S. dollar since Donald Trump's election. The Canadian dollar did not escape at first, but the trend quickly returned to appreciation. A favourable point for the loonie has been the agreement to reduce global oil production. This allows crude oil prices to go from less than US\$45 per barrel in mid-November to over US\$50 per barrel. The Canadian currency was also helped by the release of good economic statistics in Canada and advancement of monetary firming expectations. Markets now expect about 50% probability that the Bank of Canada (BoC) will raise its rates at the end of 2017.
- ▶ The U.S. dollar posted significant new gains after the Federal Reserve (Fed) monetary policy meeting on December 14, even though the key rate hike was fully expected. The surprise is actually in the changes to the Fed's forecasts. It now envisages three rather than two rate increases for 2017. Markets have adjusted their expectations, which has breathed new life into the greenback against all other currencies. The Canadian dollar was not unique, and fell below US\$0.75 (C\$1.33/\$US).
- ▶ The euro has been hit a little harder for the last two weeks. In addition to the U.S. dollar's renewed vigour, we note the effect of the latest decisions by the European Central Bank (ECB). It extended its securities purchase program to December 2017. Even though the pace of purchases will fall from €80B to €60B in April, at the end of the day, the ECB's balance sheet expansion will be considerable. Another important ECB decision was that it has now agreed to purchase bonds with yields below -0.40%. This has heightened downside pressure on short-term rates in Europe, thereby contributing to widening rate gaps with the United States.
- ▶ After depreciating sharply in November, the Mexican peso seems to want to consolidate around 20.50 pesos/\$US. To help, the Banco de México had to tighten its monetary policy.

MAIN FACTORS TO WATCH

- ▶ There is still room for investors to raise their expectations regarding the future trajectory of key rates in the United States. That said, if the Fed waits until June, as we believe it will, before proceeding with its next increase, that could fit with a short period of consolidation of the greenback during the winter. Generalized appreciation would pick up again in the spring.
- ▶ The Canadian dollar could still count on some gains from oil prices, but this might be insufficient to prevent the currency from depreciating, even in the short term. Among other things, we note a high risk of a downward correction in Canadian short-term bond yields. We think expectations that the BoC could raise its key rates at the end of 2017 seem exaggerated. We predict a Canadian dollar at US\$0.71 (C\$1.41/\$US) for the end of next year.
- ▶ Elsewhere in the world, many central banks should remain accommodating. This will be the case especially in Japan and Europe, which should reflect negatively on the currencies in those regions. The pound risks being hard hit again when negotiations on Brexit start.

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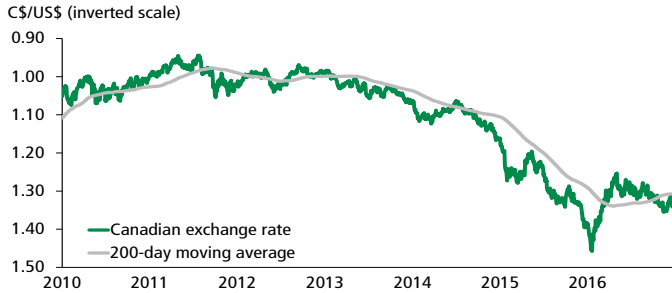
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NOTE TO READERS: The letters k, M and B are used in texts and tables to refer to thousands, millions and billions respectively.

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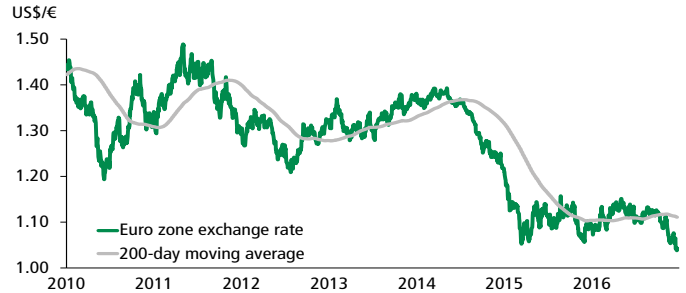
Main exchange rates

CANADA Canadian dollar and trend



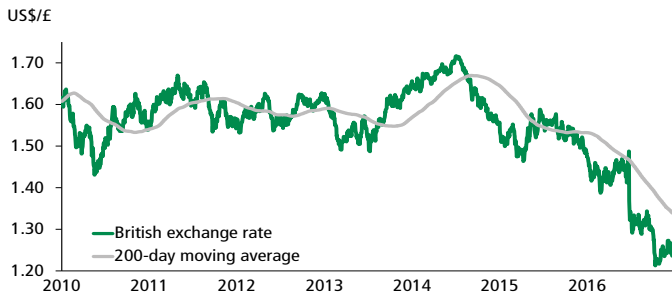
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EURO ZONE Euro and trend



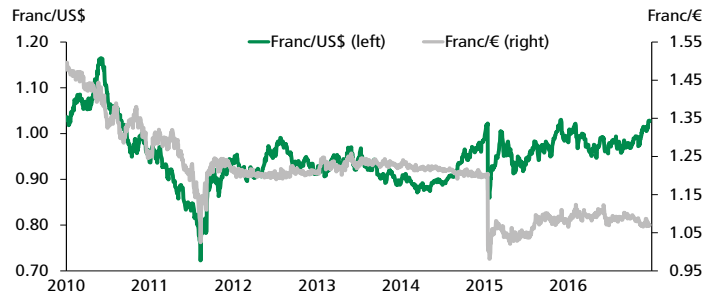
Sources: Datastream and Desjardins, Economic Studies

UNITED KINGDOM British pound and trend



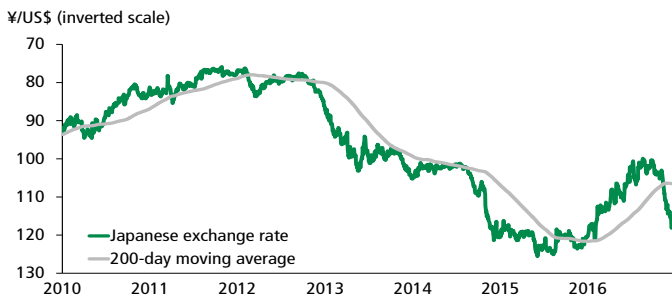
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SWITZERLAND Swiss franc



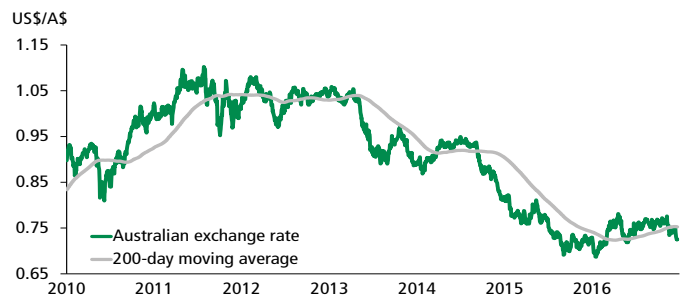
Sources: Datastream and Desjardins, Economic Studies

JAPAN Yen and trend



Sources: Datastream and Desjardins, Economic Studies

AUSTRALIA Australian dollar and trend



Sources: Datastream and Desjardins, Economic Studies

TABLE 1
Currency market: Yields

COUNTRY – CURRENCY*	SPOT PRICE	VARIATION (%)				LAST 52 WEEKS		
	Dec. 21	-1 month	-3 months	-6 months	-1 year	Higher	Average	Lower
Americas								
Argentina – peso	15.8450	2.23	4.67	14.32	24.50	16.0725	14.6853	12.7270
Brazil – real	3.3357	-0.49	2.86	-1.90	-17.30	4.1608	3.5094	3.1186
Canada – (USD/CAD)	1.3399	0.01	1.44	4.57	-4.16	1.4637	1.3268	1.2526
Canada – (CAD/USD)	0.7464	-0.01	-1.42	-4.37	4.34	0.7983	0.7537	0.6832
Mexico – peso	20.4963	-0.14	3.24	9.87	20.04	21.2033	18.5884	17.0747
Asia and South Pacific								
Australia – (AUD/USD)	0.7238	-1.77	-5.06	-2.84	0.67	0.7814	0.7435	0.6866
China – yuan renminbi	6.9422	0.72	4.05	5.34	7.12	6.9603	6.6303	6.4490
Hong Kong – dollar	7.7628	0.09	0.09	0.04	0.14	7.8194	7.7621	7.7502
India – rupee	67.8365	-0.57	1.64	0.31	2.39	68.7835	67.1208	65.9471
Japan – yen	117.55	6.06	17.18	12.22	-3.00	121.19	108.96	99.89
New Zealand – (NZD/USD)	0.6899	-2.37	-6.17	-3.15	2.00	0.7451	0.6961	0.6410
South Korea – won	1,194	0.61	6.59	3.22	1.38	1,239	1,160	1,090
Europe								
Denmark – krona	7.1319	1.89	7.05	7.83	4.31	7.1569	6.7234	6.4525
Euro zone – (EUR/USD)	1.0433	-1.78	-6.35	-7.44	-4.44	1.1518	1.1076	1.0378
Norway – kroner	8.6825	1.61	5.10	4.40	-1.13	8.9520	8.4019	7.9816
Russia – ruble	61.1112	-4.39	-4.91	-4.71	-14.25	84.2412	67.3213	60.6950
Sweden – krona	9.2328	0.15	7.89	11.50	8.62	9.4090	8.5390	7.9588
Switzerland – swiss franc	1.0262	1.69	5.05	7.07	3.41	1.0312	0.9845	0.9513
United Kingdom – (GBP/USD)	1.2374	-0.81	-4.53	-15.66	-16.87	1.4941	1.3627	1.2131

* In comparison with the U.S. dollar, unless otherwise indicated.
 Note: Currency table base on previous day closure.

TABLE 2
Currency market: History and forecasts

END OF PERIOD	2016		2017				2018				
	Q3	Q4f	Q1f	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f	
U.S. dollar											
Canadian dollar	USD/CAD	1.3129	1.3514	1.3699	1.3889	1.3889	1.4085	1.4085	1.4286	1.4085	1.3889
Euro	EUR/USD	1.1238	1.0400	1.0500	1.0300	1.0300	1.0200	1.0100	1.0100	1.0000	1.0100
British pound	GBP/USD	1.2990	1.2400	1.2100	1.1700	1.1500	1.1400	1.1300	1.1200	1.1000	1.1000
Swiss franc	USD/CHF	0.9684	1.0300	1.0200	1.0400	1.0400	1.0400	1.0500	1.0500	1.0500	1.0500
Yen	USD/JPY	101.35	118.00	118.00	120.00	120.00	122.00	122.00	123.00	124.00	125.00
Australian dollar	AUD/USD	0.7664	0.7300	0.7300	0.7200	0.7200	0.7200	0.7200	0.7100	0.7100	0.7200
Chinese yuan	USD/CNY	6.6716	6.9500	6.9500	7.0000	7.0500	7.1500	7.2000	7.2500	7.3000	7.2500
Mexican peso	USD/MXN	19.38	20.50	21.00	21.00	21.50	22.00	22.50	23.00	23.00	23.00
Brazilian real	USD/BRL	3.2459	3.4000	3.5000	3.7000	3.7000	3.8000	3.8000	3.9000	4.0000	3.9000
Effective dollar ¹		90.01	96.50	96.80	98.60	98.80	100.00	100.50	101.10	101.50	100.80
Canadian dollar											
U.S. dollar	CAD/USD	0.7617	0.7400	0.7300	0.7200	0.7200	0.7100	0.7100	0.7000	0.7100	0.7200
Euro	EUR/CAD	1.4754	1.4054	1.4384	1.4306	1.4306	1.4366	1.4225	1.4429	1.4085	1.4028
British pound	GBP/CAD	1.7055	1.6757	1.6575	1.6250	1.5972	1.6056	1.5915	1.6000	1.5493	1.5278
Swiss franc	CAD/CHF	0.7376	0.7622	0.7446	0.7488	0.7488	0.7384	0.7455	0.7350	0.7455	0.7560
Yen	CAD/JPY	77.19	87.32	86.14	86.40	86.40	86.62	86.62	86.10	88.04	90.00
Australian dollar	AUD/CAD	1.0062	0.9865	1.0000	1.0000	1.0000	1.0141	1.0141	1.0143	1.0000	1.0000
Chinese yuan	CAD/CNY	5.0816	5.1430	5.0735	5.0400	5.0760	5.0765	5.1120	5.0750	5.1830	5.2200
Mexican peso	CAD/MXN	14.77	15.17	15.33	15.12	15.48	15.62	15.98	16.10	16.33	16.56
Brazilian real	CAD/BRL	2.4723	2.5160	2.5550	2.6640	2.6640	2.6980	2.6980	2.7300	2.8400	2.8080

f: forecasts; ¹ Trade-weighted against major U.S. partners (1973 = 100).
 Sources: Datastream, Federal Reserve Board and Desjardins, Economic Studies