

FX FORECASTS

Will the Loonie Continue to Soar?

By Hendrix Vachon, Senior Economist

HIGHLIGHTS

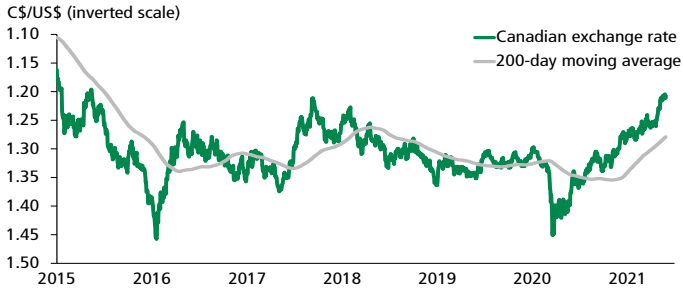
- ▶ The Canadian dollar recently surpassed US\$0.83, its highest point since May 2015. Several things have helped lift the loonie. Among these, the prices of commodities are very high. This makes the terms of trade more favorable for Canada, which is a major exporter of commodities. Then there's the rather encouraging economic situation. Canada managed to get through the second and third waves of the pandemic without too much scars. The coming months should be even better, with the vaccination campaign well underway and several provinces announcing their plans to lift the lockdown. The loonie is also benefiting from the fact that the Bank of Canada (BoC) has already begun to adjust its monetary policy and that a first interest rate hike looks likely next year.
- ▶ Many other currencies also rose against the U.S. dollar recently. Since the beginning of April, the U.S. effective exchange rate has been on a downward trend. This is consistent with decreasing uncertainty in several countries and lower demand for U.S. assets deemed secure. Higher inflation in the United States isn't helping either the greenback, especially if investors feel that this trend could last several years. Added to this that the Federal Reserve (Fed) is maintaining a dovish bias. The Fed still believes that the rise in inflation will be temporary and that attention should be mostly focused on the job market. As it turned out, April's disappointing job figures proved the Fed right. It now remains to be seen if May's job figures will be a repeat of April's.
- ▶ The euro regained most of the ground it lost in February and March, when the third wave of COVID-19 hit Europe especially hard. It's currently back trading around US\$1.22. In contrast to the Fed, the European Central Bank seems more open to adjust its monetary policy in a few quarters. Still, the road to a normalized monetary policy still seems longer in the euro zone. Not only will asset purchases have to be dealt with, but also negative interest rates.
- ▶ The United Kingdom didn't see a third wave, and its economy is rebounding faster than that of most of its European counterparts. Still, the positive impact on the British currency seems to be fading. The pound sterling rose against the euro until early April, but, since then, the GBP/EUR exchange rate seems to have settled around 0.86 £/€. However, the pound did manage to gain against the U.S. dollar recently to reach US\$1.42 for the first time since April 2018.
- ▶ The trend among emerging-country currencies remains uneven against the U.S. dollar. For example, the Chinese yuan appreciated slightly, and the exchange rate dropped below 6.40 yuan/\$US for the first time since June 2018. The Mexican peso is currently struggling to trade below 20 peso/\$US. With inflation running at more than 6.0%, it's increasingly becoming a serious problem for Mexico.

MAIN FACTORS TO WATCH

- ▶ It will be interesting to follow the Fed's future statements. An announcement of a reduction in its asset purchases could help stabilize the greenback against many currencies.
- ▶ The Canadian dollar may have a hard time posting further gains in the coming quarters. Not only would it be surprising to see commodity prices remain at such high levels, but it would also be surprising to see the BoC in an even greater hurry to adjust its monetary policy. Moreover, the expectations surrounding the Canadian economy is already fairly optimistic. While we may still see some movement past the US\$0.83-mark, stabilization, even a slight depreciation, seems more likely by the end of the year.

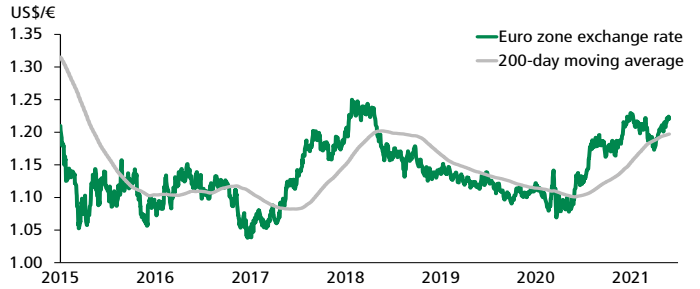
Main Exchange Rates

CANADIAN DOLLAR Exchange rate and trend



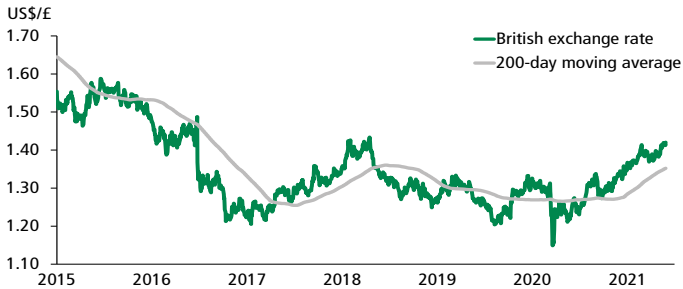
Sources: Datastream and Desjardins, Economic Studies

EURO Exchange rate and trend



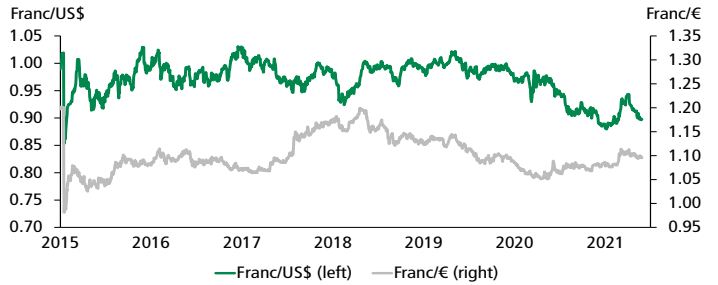
Sources: Datastream and Desjardins, Economic Studies

BRITISH POUND Exchange rate and trend



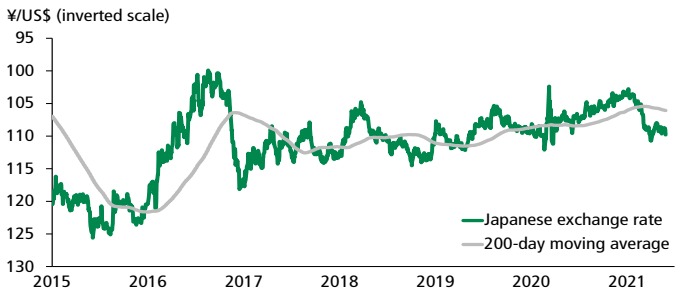
Sources: Datastream and Desjardins, Economic Studies

SWISS FRANC Exchange rate



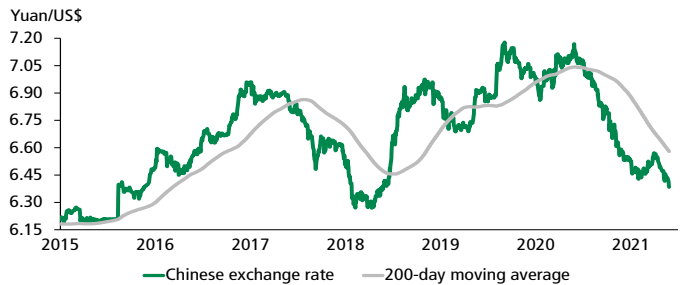
Sources: Datastream and Desjardins, Economic Studies

YEN Exchange rate and trend



Sources: Datastream and Desjardins, Economic Studies

CHINESE YUAN Exchange rate and trend



Sources: Datastream and Desjardins, Economic Studies

TABLE 1
Currency market: Yields

COUNTRY – CURRENCY*	SPOT PRICE	VARIATION (%)				LAST 52 WEEKS		
	May 27	-1 month	-3 months	-6 months	-1 year	Higher	Average	Lower
Americas								
Argentina – peso	94.5246	1.27	5.23	16.64	38.27	94.5246	81.5063	68.3614
Brazil – real	5.2625	-3.25	-5.57	-1.23	-0.92	5.8099	5.3996	4.8940
Canada – (USD/CAD)	1.2078	-2.66	-4.60	-6.92	-12.61	1.3822	1.2957	1.2050
Canada – (CAD/USD)	0.8280	2.73	4.82	7.44	14.43	0.8299	0.7718	0.7235
Mexico – peso	19.9685	0.01	-4.50	-0.57	-11.02	23.1460	20.9686	19.5880
Asia and South Pacific								
Australia – (AUD/USD)	0.7747	-0.25	0.53	4.87	17.00	0.7968	0.7384	0.6621
China – yuan renminbi	6.3833	-1.54	-1.42	-2.94	-10.97	7.1697	6.6853	6.3833
Hong Kong – dollar	7.7604	-0.02	0.05	0.12	0.07	7.7850	7.7552	7.7496
India – rupee	72.7100	-2.52	-1.66	-1.66	-4.23	76.4000	73.9223	72.3800
Japan – yen	109.82	1.03	3.02	5.47	1.94	110.73	106.29	102.74
New Zeland – (NZD/USD)	0.7293	1.16	0.79	3.81	17.99	0.7435	0.6876	0.6181
South Korea – won	1,118	0.69	-0.49	1.33	-9.43	1,240	1,144	1,082
Europe								
Denmark – krona	6.0984	-0.84	-0.99	-1.97	-9.96	6.7732	6.2835	6.0350
Euro zone – (EUR/USD)	1.2202	0.99	0.52	2.12	11.20	1.2301	1.1851	1.0973
Norway – kroner	8.3389	0.80	-3.64	-5.62	-15.48	9.8663	8.8702	8.1837
Russia – ruble	73.3650	-2.01	-1.57	-3.55	2.77	80.7600	74.3332	68.3550
Sweden – krona	8.2742	-1.21	-1.91	-2.58	-14.04	9.6257	8.6627	8.1660
Switzerland – swiss franc	0.8978	-1.64	-0.83	-0.77	-7.44	0.9700	0.9145	0.8794
United Kingdom – (GBP/USD)	1.4192	1.99	1.51	6.34	16.20	1.4211	1.3327	1.2213

* 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	2020		2021				2022				
	Q3	Q4	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f	
U.S. dollar											
Canadian dollar	USD/CAD	1.3321	1.2734	1.2560	1.1976	1.2048	1.2195	1.2195	1.2121	1.2048	1.1976
Euro	EUR/USD	1.1727	1.2236	1.1753	1.2200	1.2200	1.2100	1.2100	1.2100	1.2000	1.1900
British pound	GBP/USD	1.2928	1.3670	1.3797	1.4200	1.4200	1.4300	1.4300	1.4300	1.4400	1.4500
Swiss franc	USD/CHF	0.9186	0.8808	0.9410	0.9000	0.9100	0.9300	0.9300	0.9400	0.9500	0.9600
Yen	USD/JPY	105.47	103.26	110.72	109.00	110.00	110.00	111.00	111.00	111.00	112.00
Australian dollar	AUD/USD	0.7163	0.7695	0.7598	0.7800	0.7800	0.7800	0.7800	0.7900	0.7900	0.8000
Chinese yuan	USD/CNY	6.7908	6.5267	6.5527	6.3500	6.3000	6.3000	6.3000	6.2500	6.2500	6.3000
Mexican peso	USD/MXN	22.11	19.89	20.44	19.80	19.50	19.50	19.25	19.25	19.25	19.50
Brazilian real	USD/BRL	5.6404	5.1964	5.6970	5.2000	5.0000	5.2000	5.1000	5.1000	5.2000	5.4000
Effective dollar ¹		107.08	102.59	105.22	101.40	101.70	102.00	102.20	102.30	102.50	102.80
Canadian dollar											
U.S. dollar	CAD/USD	0.7507	0.7853	0.7962	0.8350	0.8300	0.8200	0.8200	0.8250	0.8300	0.8350
Euro	EUR/CAD	1.5621	1.5580	1.4762	1.4611	1.4699	1.4756	1.4756	1.4667	1.4458	1.4251
British pound	GBP/CAD	1.7221	1.7406	1.7329	1.7006	1.7108	1.7439	1.7439	1.7333	1.7349	1.7365
Swiss franc	CAD/CHF	0.6896	0.6917	0.7492	0.7515	0.7553	0.7626	0.7626	0.7755	0.7885	0.8016
Yen	CAD/JPY	79.17	81.09	88.15	91.02	91.30	90.20	91.02	91.58	92.13	93.52
Australian dollar	AUD/CAD	0.9542	0.9798	0.9543	0.9341	0.9398	0.9512	0.9512	0.9576	0.9518	0.9581
Chinese yuan	CAD/CNY	5.0978	5.1256	5.2171	5.3023	5.2290	5.1660	5.1660	5.1563	5.1875	5.2605
Mexican peso	CAD/MXN	16.60	15.62	16.27	16.53	16.19	15.99	15.79	15.88	15.98	16.28
Brazilian real	CAD/BRL	4.2342	4.0809	4.5358	4.3420	4.1500	4.2640	4.1820	4.2075	4.3160	4.5090

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