

 **CANADA**

The Canadian dollar has been tracking oil less closely in the last few weeks

It's often said that the Canadian dollar's current weakness stems from the plunge by oil prices. Since the summer of 2014, the benchmark price per barrel for WTI (West Texas Intermediate) has fallen from around US\$100 to below US\$30. The Canadian dollar simultaneously saw its value dwindle to a cyclical low of US\$0.6808 on January 20. However, the loonie has risen a few cents in recent weeks, with no proportional rebound by crude prices.

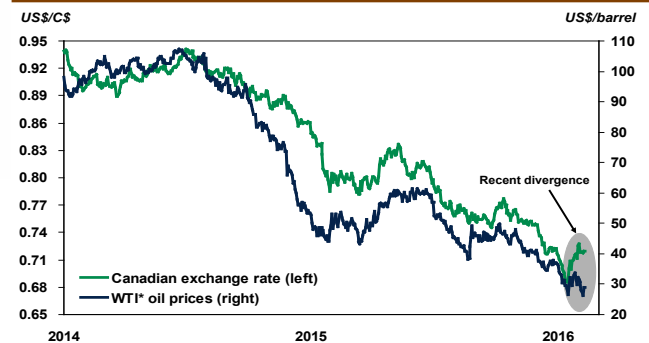
The recent movement shows that the relationship between the Canadian dollar and oil is not infallible. The relationship involves several mechanisms and can change over time. As oil is one of Canada's main sources of export revenue, price movements have a major impact on demand for Canadian dollars, and therefore on the currency's value. Crude prices also influence the loonie through their impact on the economy and interest rates. Higher prices usually augur more sustained economic growth and higher interest rates, thus a rising currency. In contrast, if oil prices are low, the markets will expect softer economic growth in Canada and low interest rates, penalizing the loonie.

Several other factors can dictate the exchange rate, often with the same mechanisms as oil prices. At the start of January, anticipations of monetary easing were very high in Canada due to the fears raised by low crude prices. However, the January 21 monetary policy meeting encouraged the markets to make adjustments as the Bank of Canada seemed in no rush to act. This had a big hand in the Canadian dollar's rebound.

Lastly, we cannot overlook the U.S. dollar's generalized weakness since the start of February, as this is making a number of currencies look good. The greenback's depreciation essentially stems from the drop in monetary firming expectations in the United States due to the uncertain global climate.

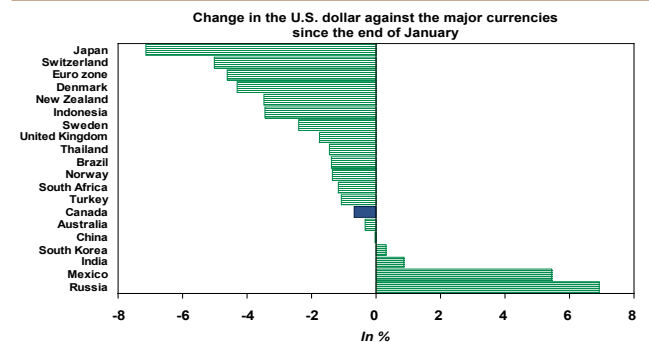
Implications: Although the loonie has not followed oil prices as closely lately, this does not mean they have no

True, the Canadian dollar does track oil prices closely, but it can be influenced by other factors too



* West Texas Intermediate.
Sources: Datastream and Desjardins, Economic Studies

The greenback has been under pressure in recent weeks



Sources: Datastream and Desjardins, Economic Studies

influence on it. The appreciation seen in recent weeks is due to other factors; if oil prices had gone up, the loonie would likely have risen more. We will have to keep a close eye on the greenback's movements in the next few weeks; it could rebound if the markets started expecting again interest rate increases in the United States.

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