

ECONOMIC NEWS

Can the Canadian Dollar Bounce Back?

There has been pressure on the Canadian dollar since mid-April. It went from around US\$0.75 (C\$1.33/US\$) to a bit lower than US\$0.73 (C\$1.37/US\$). One reason for the decline is the drop in oil prices. The benchmark West Texas Intermediate went from almost US\$55 per barrel in mid-April to around US\$45 more recently. Weak oil prices will mean less revenue for the Canadian economy, so the markets are betting against the loonie.

Aside from oil, fears of mounting U.S. protectionism have also affected our currency. First, there were President Donald Trump's verbal attacks on the Canadian supply management system, then the announcement of a tax on lumber. But the icing on the cake was the threat that the United States would withdraw from the North American Free Trade Agreement (NAFTA). Although that did not happen in the end, it certainly aggravated the level of uncertainty about the future of trade relations with the United States.

The difficulties of Home Capital mortgage lender seem to have affected the loonie as well. Even though the company represents just a fraction of the Canadian mortgage market, its problems have had an impact on confidence in the Canadian financial system.

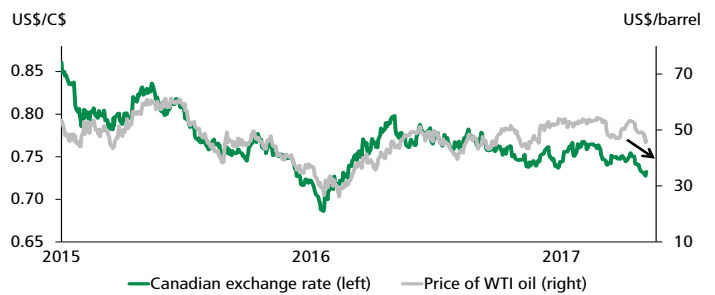
Overall, Canadian economic data remained generally good, which could have benefited the loonie. First-quarter economic growth should be around 4%. On the other hand, job creation slowed in April and inflation fell back below 2%. Add to this concerns on oil prices, protectionism and the financial system, and the current climate is not amenable to anticipations of monetary firming in the country, even though the Bank of Canada (BoC) adopted a more optimistic tone at its meeting on April 12. The difference in interest rates with the United States has grown significantly in recent weeks. Many Canadian rates did not follow the upward trend of U.S. rates.

IMPLICATIONS

The Canadian dollar could remain under pressure for a while longer and test US\$0.72 (C\$1.39/US\$) in the short term. A quick

CANADIAN DOLLAR

Decreasing oil prices is among the negative factors impacting the currency since mid-April



WTI : West Texas Intermediate
Sources: Datastream and Desjardins, Economic Studies

recovery in oil prices would make this scenario unlikely, but would not necessarily bring the exchange rate back to around the US\$0.75 it was at in mid-April.

We are not banking on a sharp rise in U.S. protectionism, but current worries may persist and hurt the Canadian currency. It will be interesting to see how the BoC will incorporate this into its official statement.

Additional elements that should be a short-term drag on the loonie are the likely increase in U.S. key rates in June and an increase in market expectations for the coming Federal Reserve meetings. In this context, the U.S. dollar should undergo generalized appreciation.

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