

The Canadian Dollar outlook for 2021

The rapid reopen

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With the recent move in the Canadian dollar, many investors are wondering as to the direction for the loonie through the remainder of 2021 and into 2022. The Canadian dollar, historically, has moved based on two different factors. One is the price of oil, by using the benchmark for West Texas Intermediate price for crude, and the other one being the interest rate differential, in particular, the two-year government bond yield between Canada and the United States. Over the last six to eight months, the Canadian dollar has appreciated relative to the US dollar because of the gains in the price of oil. As oil prices move up, it tends to lift the Canadian dollar along with it. In the last month, we've also seen upward pressure on the Canadian dollar by the difference in rate expectations between Canada and the United States. What we mean is that the Bank of Canada seems to have backed away from its 2023 commitment before it starts to raise rates. We think that the Bank of Canada can start to raise its overnight rate in the back half of 2022. Now, this is ahead of the US Federal Reserve, and as a result of that difference, we're starting to see that being priced into the Canadian dollar.

Currently, the Canadian dollar is trading just below 83 cents, which is near the top end of our target, as at the end of the first quarter. Given the strength that we're seeing in oil prices and how quickly the US economy and global economy is likely to open up through the remainder of 2021, we believe that the price of oil, again as measured by WTI, is sustainable at the \$65 level, with upward pressure.

Combining our expectation for the Bank of Canada to potentially raise rates ahead of the Fed, and oil prices remaining above \$65 a barrel, our target for the Canadian dollar relative to the US is somewhere between 84 and 85 cents through the remainder of this year, the risk, of course, being to the upside. So for those investors that are thinking about the US dollar versus the Canadian dollar, we do expect the US dollar to continue to weaken this year, giving way to Canadian dollar strength.

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