

FX FORECASTS

Can the US Dollar Keep the Rally Going?

HIGHLIGHTS

- ▶ The stars aligned for a US dollar rally in August and September. Mounting fears about economies like China sent investors into a more cautious stance, which typically helps the US dollar—the world’s leading safe haven currency. Meanwhile US economic data has remained strong, with real GDP growth expected to come in around 4% in the third quarter. That has translated into higher interest rates. Bond yield spreads between the US and a number of countries have widened, providing additional support for the greenback. And according to its own projections, the Federal Reserve may raise the fed funds rate once more before the year is out, then cut very little in 2024.
- ▶ The Canadian dollar is holding up better than the currencies of most major advanced and emerging economies. After losing just over 2% in August, the loonie posted a small gain in September. High oil prices are propping up the Canadian dollar, offsetting lower prices for several other commodities. The loonie is also benefiting from a slight narrowing of yield spreads between the US and Canada after inflation came in a bit higher than expected recently. The Bank of Canada hasn’t closed the door to further rate hikes either.
- ▶ European currencies aren’t faring as well. The economic data out of Europe hasn’t been as rosy, and while inflation remains high, it has been trending sharply lower of late. This has meant a slower rise in bond yields. The Bank of England announced a surprise rate pause on September 21. The pound started the month trading at around US\$1.26, but it’s now at about US\$1.22. The Swiss National Bank also surprised with a hold, hurting the franc. The European Central Bank raised its key interest rates by 25 basis points this month, though it signalled that could be the last increase if the economy and inflation evolve as expected.
- ▶ The Japanese yen is nearing its October 2022 high of 150 yen/US\$. The Bank of Japan (BoJ) loosened its yield curve control in July, but that hasn’t stopped the yen from sliding. US yields have simply gone up faster than their Japanese counterparts, and the BoJ has yet to lift its main policy rate from -0.1%.

MAIN FACTORS TO WATCH

- ▶ The US dollar could give back some of its recent gains in a hurry if economic data starts hinting at a slowdown. That’s what our forecast calls for, and it would also mean lower US bond yields. In the very short term, we’ll have to keep an eye on Congress to see if it can avert a government shutdown by passing the necessary spending bills by the end of September. If it can’t, we could see the US economy slow more sharply.
- ▶ The Canadian dollar and other currencies stand to benefit from lower US bond yields. However, we expect Canada’s economy to slow as well, which would send its bond yields lower too. We also don’t think oil prices will stay high for much longer. Bottom line? The Canadian dollar could weaken slightly by the end of the year, but we still think it will rebound later in 2024 as the global economy and commodity prices strengthen.

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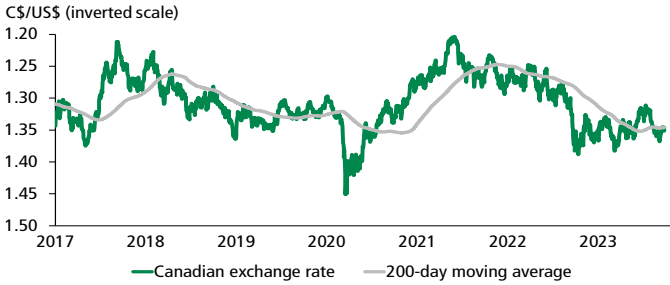
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NOTE TO READERS: The letters k, M and B are used in texts and tables to refer to thousands, millions and billions respectively.

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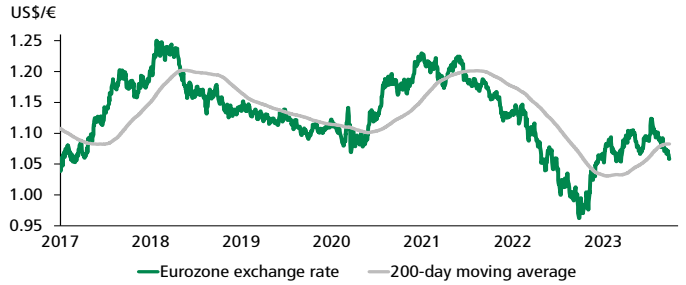
Main Exchange Rates

CANADIAN DOLLAR Exchange rate and trend



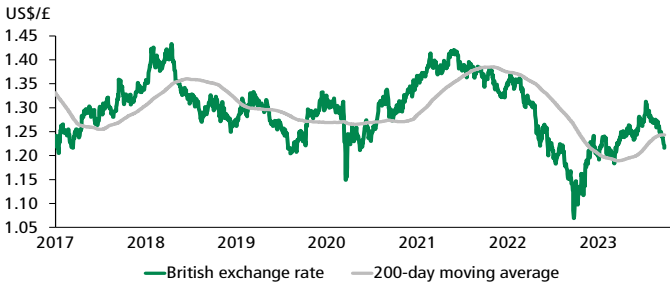
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EURO Exchange rate and trend



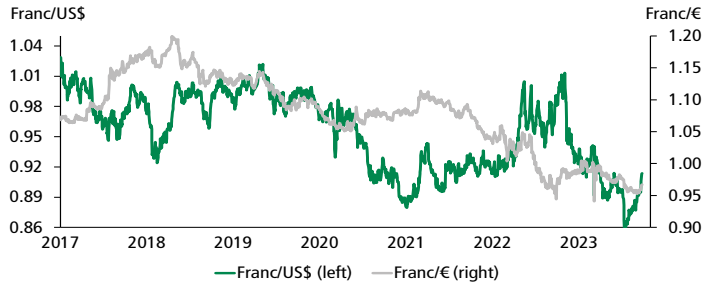
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BRITISH POUND Exchange rate and trend



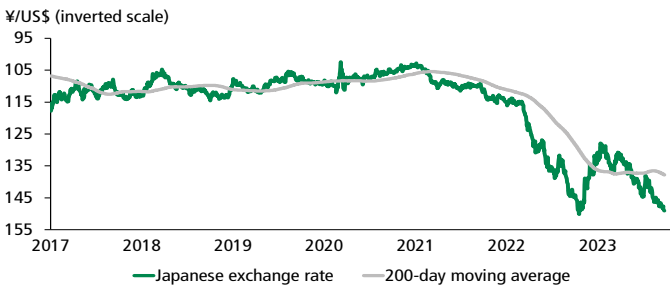
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SWISS FRANC Exchange rate



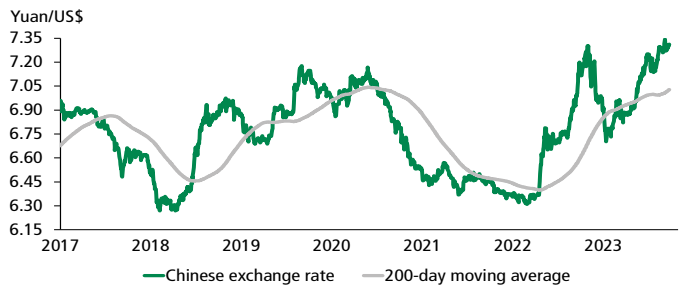
Sources: Datastream and Desjardins Economic Studies

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	% CHANGE					LAST 52 WEEKS		
	Sep 26	1-month	3-month	6-month	1-year	High	Average	Low	
Americas									
Argentina – peso	350.0192	0.01	37.47	70.18	139.81	350.0341	222.3723	145.9580	
Brazil – real	4.9650	1.50	3.93	-5.39	-7.31	5.4632	5.0769	4.7216	
Canada – (USD/CAD)	1.3491	-1.05	2.54	-1.95	-1.41	1.3879	1.3490	1.3113	
Canada – (CAD/USD)	0.7412	1.06	-2.48	1.99	1.43	0.7626	0.7413	0.7205	
Mexico – peso	17.4210	3.63	1.56	-5.83	-14.34	20.3370	18.3227	16.6405	
Asia and South Pacific									
Australia – (AUD/USD)	0.6397	-0.07	-4.11	-3.75	-0.93	0.7136	0.6654	0.6197	
China – yuan renminbi	7.3113	0.29	1.02	6.45	2.49	7.3440	7.0531	6.7030	
Hong Kong – dollar	7.8214	-0.28	-0.11	-0.36	-0.36	7.8501	7.8313	7.7674	
India – rupee	83.2550	0.71	1.56	1.11	2.00	83.3150	82.2712	80.5045	
Japan – yen	149.07	1.81	3.87	14.05	2.98	150.15	138.93	127.90	
New Zeland – (NZD/USD)	0.5945	0.68	-3.60	-4.16	5.45	0.6506	0.6129	0.5565	
South Korea – won	1,349	1.76	3.22	4.19	-5.78	1,440	1,318	1,220	
Europe									
Denmark – krona	7.0529	2.15	3.29	1.84	-8.86	7.7519	6.9909	6.6300	
Eurozone – (EUR/USD)	1.0584	-1.73	-2.98	-1.66	9.70	1.1243	1.0661	0.9621	
Norway – kroner	10.8177	1.03	0.84	3.44	0.05	11.1864	10.4081	9.7166	
Russia – ruble	96.5000	1.47	13.36	25.12	67.46	101.3000	77.5686	57.6250	
Sweden – krona	10.9945	-0.56	2.46	5.48	-3.12	11.3655	10.6345	10.1615	
Switzerland – Swiss franc	0.9137	3.00	2.10	-0.46	-7.80	1.0133	0.9191	0.8577	
United Kingdom – (GBP/USD)	1.2169	-3.05	-4.26	-0.48	12.77	1.3119	1.2244	1.0747	

* In comparison with the US dollar, unless otherwise indicated.
Note: Currency table based on the previous day's close.

TABLE 2
Currency market: History and forecasts

END OF PERIOD	2022		2023				2024				
	Q3	Q4	Q1	Q2	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f	
US dollar											
Canadian dollar	USD/CAD	1.3828	1.3551	1.3516	1.3238	1.3514	1.3699	1.3699	1.3333	1.3158	1.3158
Euro	EUR/USD	0.9797	1.0673	1.0865	1.0910	1.0600	1.0700	1.0700	1.0900	1.1100	1.1200
British pound	GBP/USD	1.1163	1.2029	1.2365	1.2714	1.2200	1.2300	1.2500	1.2800	1.3000	1.3200
Swiss franc	USD/CHF	0.9842	0.9227	0.9132	0.8946	0.9200	0.9000	0.9100	0.9200	0.9300	0.9400
Yen	USD/JPY	144.77	131.13	132.81	144.34	150.00	140.00	130.00	120.00	117.00	115.00
Australian dollar	AUD/USD	0.6404	0.6814	0.6686	0.6667	0.6400	0.6400	0.6400	0.6600	0.6700	0.6700
Chinese yuan	USD/CNY	7.1160	6.8986	6.8690	7.2523	7.3000	7.4000	7.4000	7.3000	7.2000	7.1500
Mexican peso	USD/MXN	20.15	19.49	18.02	17.13	17.50	18.25	18.25	18.00	17.75	17.75
Brazilian real	USD/BRL	5.4063	5.2174	5.0801	4.8189	5.0000	5.2000	5.3000	5.1000	5.0000	4.9000
Effective dollar ¹		123.8	115.8	114.7	114.5	118.1	116.7	115.3	111.9	110.1	109.3
Canadian dollar											
US dollar	CAD/USD	0.7232	0.7380	0.7399	0.7554	0.7400	0.7300	0.7300	0.7500	0.7600	0.7600
Euro	EUR/CAD	1.3547	1.4462	1.4684	1.4443	1.4324	1.4658	1.4658	1.4533	1.4605	1.4737
British pound	GBP/CAD	1.5436	1.6300	1.6712	1.6830	1.6486	1.6849	1.7123	1.7067	1.7105	1.7368
Swiss franc	CAD/CHF	0.7117	0.6809	0.6756	0.6758	0.6808	0.6570	0.6643	0.6900	0.7068	0.7144
Yen	CAD/JPY	104.69	96.76	98.26	109.03	111.00	102.20	94.90	90.00	88.92	87.40
Australian dollar	AUD/CAD	0.8856	0.9233	0.9037	0.8826	0.8649	0.8767	0.8767	0.8800	0.8816	0.8816
Chinese yuan	CAD/CNY	5.1461	5.0908	5.0821	5.4784	5.4020	5.4020	5.4020	5.4750	5.4720	5.4340
Mexican peso	CAD/MXN	14.57	14.38	13.33	12.94	12.95	13.32	13.32	13.50	13.49	13.49
Brazilian real	CAD/BRL	3.9097	3.8502	3.7586	3.6402	3.7000	3.7960	3.8690	3.8250	3.8000	3.7240

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