



Canadian Dollar vs US Dollar

By CK Wong 2007.06.18

<http://www.ck-wong.ca/Money%20Matters/canadian%20dollar%20vs%20us%20dollar%2020070618.pdf>

Introduction

One an a half year ago I started to track the parity trend of C\$ vs U\$. The trend line on the Gold and HnCn page http://ck-wong.ca/gold_HnCn.htm) showing a possibility by end of 2007. The weakness of U\$ by design or by economy leads to the same result. What would be the post parity life? Would there be premium over U\$?

Exhibits

The following two charts are the ratio of Western Texas Oil Price to Canadian Dollar and US Dollar.





The first graph shows a trend to go down, may be it try to restore the ratio of 0.55 or even 0.50. The second shows a topping and a gentle downward slope. It is always dangerous to extrapolate what will happen but by examine the MACD we could agree the downward trend of \$WTIC/\$USD is much less possible than the \$WTIC/\$CDW. If Oil continues its upward journey, C\$ will be higher than US\$.

Exchange Exposure

The following table lists the change of various indices which I am going to compute the net gain when invests in US\$ reported companies.

Index	Jun-04	Jun-07	Change	Gain(loss)	Rel. to C\$
\$CDW	72.7	93.5	20.8	28.61%	
\$USD	90.7	82.6	-8.1	-8.93%	
Dow Jones	10400	13651	3251	31.26%	28.47%
S&P 500	257	356	99	38.52%	35.08%
TSX	8500	10470	1970	23.18%	

The table shows an inflationary appreciation of the US stock market. The gain is due to the weakness of the US\$. It is also the result of global Quality of Life improvement that increases the profit of American global companies. The progressive depreciation of the US\$ is not a much of debate so does the status of the C\$ as an oil dollar. The oil price will continue its inverse relationship with the US\$ and the C\$ will have its peg with the oil. It would not be a matter of **if** rather a question of **when** the C\$ will surpass the US\$.

There are a few significant consequence and a few road blocks to achieve that.

1. Higher C\$ will reduce the revenue from American for the Canadian exporter to US. This will drive the profit downward. At the same time, the higher C\$ merchandize will be less in demand. The double blades sword will hurt the bottom line of Canadian manufacturers. Similar scenario is applicable to the energy export. A re-balance will happen and the surge of C\$ would be subsided. The first factor has been diminishing its effect as Canadian exporters are redirecting their business to the more on par Eurozone and Asia which including India and China. The second factor may be compensated with higher oil price and could fuel the rise of C\$.
2. Inflation due to forex profit has been observed for those importers who do not lower their C\$ merchandize price as the US\$ lower. In some situation, it is even increase. The deflation effect of gain in C\$'s exchange rate has not be fully reflected in consumer prices. 2 The Bank of Canada is hawkish to raise interest rate to combat the inflation. To me this will fuel the inflation rate and also pushes the C\$ higher in short term. In long term, the weakening of the non-energy sector economy could bring the C\$ down. This strong polarity effect on Canadian economy will create significant wealth imbalance among province and among people.
3. The world swirls around oil dollar which means trade will be settled using the oil dollar in the last 100 years. Now that Canadian dollar has unofficially becomes the C\$ the next step could be C\$ becomes the international trade settlement currency. If this is the trend, what President Bush proposed to have a North American currency will not happen because it will be dragging the C\$ on its way up. However, I see that may be a far fetch because trade settlement currency must backed by a huge demand and supply economy. Canada economy is just not at the world class in the coming decade. Rather Canadian trading partner China could very possibly because of its fast approaching to number 2 world economy.

Resources

[1] <http://www.stockcharts.com/>

[2] *The Price is Wrong*, Doug Porter, Deputy Chief Economist at BMO Nesbitt Burns, Inc. 2007.