A Weak Loonie Is Boosting Canada's Economic Growth

Description

Recent economic data indicates that Canada may have turned the corner and escaped the economic contraction of the first half of 2015. This is despite oil stubbornly remaining below US$50 per barrel, a weak loonie, and declining activity in the energy patch.

Indeed, while it will not all be clear sailing, and the sharp collapse in crude will continue to be a nasty overhang on the Canadian economy for some time, I expect to see an uptick in economic growth.

Meanwhile, the oil rout may have been beneficial for Canada in the long run.

Let me explain.

Now what?

One of the greatest economic impacts to arise from the sustained weakness in oil prices has been the marked depreciation of the loonie against the U.S. dollar. Over the last year the loonie has plunged by almost 15% against the U.S. dollar and, at one point, dipped below US$0.75 cents.

This can be attributed to the precipitous collapse in oil prices. The value of the loonie is closely correlated to the price of crude, which makes up roughly a quarter of Canada's total exports by value.

The sharp devaluation of the loonie set alarm bells ringing for many Canadian investors.

Any Canadian company with a large portion of its debt denominated in U.S. dollars, such as **Barrick Gold Corp.** (TSX:ABX)(NYSE:ABX), **Suncor Energy Inc.** (TSX:SU)(NYSE:SU), and **Canadian Oil Sands Ltd.** (TSX:COS), will see the servicing costs of that debt rise.

It has also caused inflation to rise primarily because it has led to an increase in the price of imported goods, particularly consumer durables and electronics, which is certainly not beneficial for the prospects of retailers.

However, the net end result is that a weak loonie is of considerable benefit to the Canadian economy.

You see, it makes Canadian exports far more attractive to international buyers, and this has helped to boost economic growth over recent months. For August 2015, GDP grew by 0.1% month over month and 0.9% year over year, which, in conjunction with strong economic growth in June and July, should mean that Canada is on track to report an impressive 2.5% 2015 GDP growth rate.

In fact, the weak loonie and the increasing appeal of Canada's exports have been particularly beneficial for Canada's ailing manufacturing sector. The value of manufacturing exports in August shot up by an impressive 16% year over year, driving an uptick in manufacturing activity. The manufacturing sector's share of GDP grew in August by 0.4% month over month and 0.6% year over year.

This can also be attributed to lower input costs for a number of industries thanks to weak oil prices.

More surprisingly, given the doom and gloom surrounding Canada's economy in the first half of the year and poor consumer sentiment, there was also a sharp uptick in retail sales in August. This bodes well for Canada's major retailers and supermarket chains such as **Empire Company Limited** (TSX:EMP.A) and **Loblaw Companies Limited** (TSX:L), which should see increased revenues from improving consumer sentiment.

So what?

A weak loonie is a powerful tailwind for the Canadian economy and has helped to pull it out of a recession. It also stands to benefit those Canadian companies that depend on exports as a key driver of earnings growth.

Most importantly, it has helped to reinvigorate Canada's manufacturing sector and reduced Canada's dependence on the energy patch as a source of economic growth. This will help to shield Canada from a sustained downturn in crude and other commodities.

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