Why the Loonie Will Remain Weak and What to Do About it

Description

As the Canadian dollar marches down towards US$0.70, a strong recovery is looking increasingly unlikely. We take a closer look at why and how you can take advantage as an investor.

Why the loonie appears stuck

In a recent poll by *Reuters*, 50 foreign exchange strategists expect the Canadian dollar to trade for US$0.72 by the end of this year. That would be only a modest recovery from current levels.

And there is reason to be skeptical about the loonie. The biggest factor, of course, is oil prices, which have shown few signs of recovering. The other key determinant is interest rates; the United States Federal Reserve is expected to keep raising its benchmark rate this year, while its Canadian counterpart is expected to keep rates flat.

Normally in such circumstances, you would expect a weak Canadian dollar to be self-correcting. Exporters (including energy companies) are benefiting from the weak Canadian dollar, which ideally would boost sales to the United States until the loonie returns to a more reasonable level.

But in reality, that's not what we're seeing. One reason is that other currencies are performing terribly, too. For example, the Russian ruble has declined by more than half versus the U.S. dollar over the past two years. That's made Russian production of oil and other commodities very competitive.

Another reason is that Canada remains a high-cost jurisdiction for many products. For example, Ontario has lost 300,000 manufacturing jobs over the past 15 years as plants shut down or move to lower-cost countries. No matter how weak the loonie gets, most of those jobs are not coming back. So there's little reason to expect the loonie to bounce back either.

How to take advantage

If you've been holding some of your investments in U.S. dollars, then good for you. This alone has provided a nice boost.

But even if you haven’t, you may want to think about holding some U.S. dollar-denominated stocks. This doesn’t necessarily mean opting for American companies, since many Canadian firms have American listings as well. Even some modest U.S. dollar holdings could shield you from a further weakening loonie.

Secondly, you could opt for stocks with significant American exposure. For example, if you’re looking at the Canadian banks, **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD) is likely the one that benefits most from a strong greenback thanks to its U.S. exposure.

Another option is to buy Canadian exporters that benefit from a weak loonie. Names that immediately come to mind include **Magna International Inc.** (TSX:MG)(NYSE:MGA) and **CAE Inc.** (TSX:CAE)(NYSE:CAE). These companies should benefit even if the Canadian dollar stays flat going forward, and they also benefit from low oil prices. They are a great way to diversify your portfolio, especially if you hold some energy stocks.

CATEGORY

1. Investing

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2. NYSE:MGA (Magna International Inc.)
3. NYSE:TD (The Toronto-Dominion Bank)
4. TSX:CAE (CAE Inc.)
5. TSX:MG (Magna International Inc.)
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bensinclair