Strong Canadian Dollar: 2 Stocks That Benefit

Description

The Canadian dollar hit a three-month high against the U.S. dollar yesterday. The driving force is the weakening of the U.S. dollar. The American government's stimulus measures are more comprehensive and more expensive than our own. The Federal Reserve has offered nearly limitless support for the economy. This weakens the U.S. dollar and, in turn, strengthens the Canadian dollar.

For most stocks, a stronger Canadian dollar is usually bad. Exporters earn less when the domestic currency appreciates. Canadian corporations with foreign currency reserves also lose some book value. However, certain sectors of the economy benefit from a stronger currency.

Here are two stocks that should see their fortunes improve if the Canadian dollar keeps strengthening in the months ahead.

Importers

Importers can extract better margins if the purchasing power of their currency improves. **Dollarama** (TSX:DOL) and **Canadian Tire** (TSX:CTC.A) are great examples of this. A substantial portion of the goods on their shelves isn't made in Canada; goods are imported, mainly from Asia.

A stronger Canadian dollar decreases the cost of every Made in China bicycle or Made in Bangladesh t-shirt. Meanwhile, Canadian customers pay the same price as before. This widens the profit margin and ultimately benefits shareholders.

Both stocks have steadily climbed over the past few months, as the Canadian dollar gained strength. Dollarama is up 35.5%, while Canadian Tire is up 67.5% since March 23. These gains could hold steady or improve if the Canadian dollar sustains the current price level.

Canadian dollar outlook

Where the Canadian dollar will be by the end of 2020 is hard to predict. However, there are three key factors that seem to be driving the currency for now: the post-COVID economic recovery, the U.S. dollar, and the price of oil.

Jeffrey Gundlach, the billionaire chief executive of DoubleLine Capital, predicts that the U.S. dollar could be weaker as time goes on. He believes the Federal Reserve is printing too much money to support the economy. At the time of writing, the U.S. debt burden has ballooned by $2 trillion in two months and is worth $26 trillion altogether.

Meanwhile, the price of oil is likely to remain stable, as producers in the Middle East come to an agreement. I’m far from an expert on geopolitics and crude oil, but if the agreements holds, the price of oil could remain steady throughout 2020.

Meanwhile, Canada’s economy is slowly but surely bouncing back from the coronavirus lockdown. Housing activity has surged while provinces have been slowly opening up this month. It’s too early to say whether the economy will fully recover soon. However, any strength in the economy is a catalyst for the Canadian dollar.

It seems like our currency could hold onto its strength or even strengthen this year. That’s great for stocks such as Dollarama or Canadian Tire. It’s also good news for nearly anyone else who earns in Canadian dollars but spends in foreign currencies.

Bottom line

The Canadian dollar could remain stable or appreciate for the rest of 2020, according to experts. In that case, importers are the best bet for investors.

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2. Stocks for Beginners

TICKERS GLOBAL

1. TSX:CTC.A (Canadian Tire Corporation, Limited)
2. TSX:DOL (Dollarama Inc.)

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