

Canadian dollar (USDCAD)

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USDCAD hasn't closed outside the 1.31 to 1.35 range in over 4 months. Canada's widening growth deficit with the US has offset the recovery in oil prices. A quick break above 1.35 is possible, but the market is already long. We expect USDCAD to remain around current levels through the election, but there is a good chance the election becomes a CAD-positive factor as candidates compete on plans to boost competitiveness and growth. We don't expect either the BoC or the Fed to move over the next 12M.

FX Strategy Team View	1M	3M	6M	9M	12M
USDCAD spot	1.34	1.34	1.31	1.30	1.29
EURCAD spot	1.49	1.46	1.43	1.43	1.46
GBPCAD spot	1.74	1.69	1.62	1.65	1.70
Fed base rate	2.25 - 2.50%	2.25 - 2.50%	2.25 - 2.50%	2.25 - 2.50%	2.25 - 2.50%
BoC base rate	1.75%	1.75%	1.75%	1.75%	1.75%

Bullish USDCAD factors

- The growth gap between the US and Canada appears to have widened in H1 of 2019. Long-term investment flows follow growth; Canada could end up with lower growth potential if this isn't addressed, but thus far the policy response has been subdued.
- The election is now inside of 6M away. Foreigners usually start hedging elections when they are 3-6M out. This should put upward pressure on USDCAD within the next 3M.
- Canada may prefer NAFTA to USMCA/CUSMA and hope the latter never gets ratified, but if Canada's most important trade relationship ends up in limbo until after the US's 2020 election, that is the worst of all outcomes. Unfortunately, with the US political situation, limbo appears to be the most likely scenario.

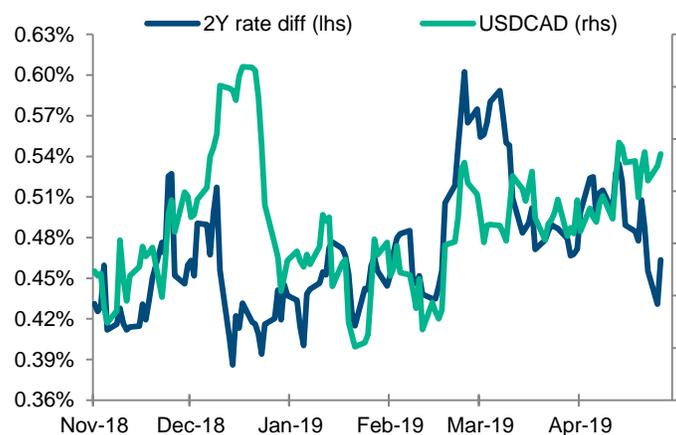
Bearish USDCAD factors

- Canada's oil basket has risen substantially in 2019 but it hasn't helped CAD much (yet). The price of our proxy for Canada's oil production basket suggests USDCAD should be much lower. USDCAD is also a bit too high relative to the 2Y interest rate differential (see chart).
- A Nanos poll from May 3 has the Conservatives 3% ahead of the Liberals. The Conservatives have now led in the polls for 3M. The election looks tight enough that the parties may end up campaigning on competing 'competitiveness plans'.
- Canada's twin sin score narrowed to 3.7% in 2018; it should hold about there in 2019. That's a stark contrast to the US. The US's 2018 twin sin score widened to -6.6% in 2018 and is expected to balloon further to -7.2% in 2019.

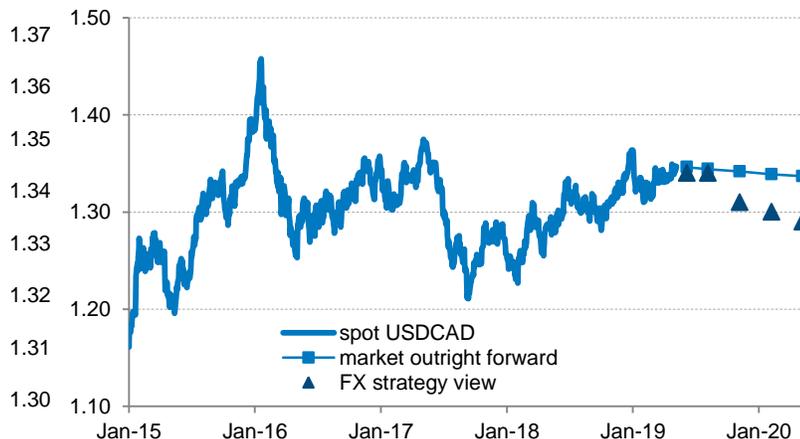
Canada FX fundamental facts

- **CAD FX weights:** 2016 BIS volume weight 6.3% (6th); BBDXY weight 11.4% (3rd); 2019 Fed's broad USD index weight 13.6% (3rd)
- **Population and per capita GDP:** 37mn, USD 46,733/year nominal or 49,936 IMF PPP-adjusted for calendar 2018 (USDCAD 1.30)
- **Next general election:** A Federal election must be held on or before October 21, 2019
- **Prime Minister:** Justin Trudeau (since Nov-15)
- **Finance minister:** Bill Morneau (since Nov-15)
- **Central bank governor (Bank of Canada or BoC):** Stephen Poloz (since Jun-13)
- **Central bank objective:** inflation targeting (since 1991) with a target of 2.0% and a +/- 1% band
- **Inflation:** Total CPI 1.9% YoY for mAR-2019; +1.9% YoY avg of 3 core CPI measures; median forecast for 2019 is 1.8%
- **GDP growth rate:** 1.1% YoY for February index; 1.8% for 2018; median forecast for calendar 2019 is 1.8%
- **Current account balance:** -2.8% of GDP for 2018; median forecast for 2019 is -2.7% of GDP
- **Budget balance:** -0.9% for 2018; median forecast for 2019 is -0.8% of GDP
- **Sovereign credit:** S&P rating AAA (stable); Moody's rating Aaa (stable); 5Y CDS 30bps (-2bps YTD)

USDCAD vs its 2Y swap rate differential



USDCAD price history, forward curve and our outlook



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