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Canadian dollar seen up in one year if economy avoids hard landing - Reuters poll

By Fergal Smith

TORONTO (Reuters) - The Canadian dollar is set to rally over the coming year, after a period in which it consolidates its recent gains, as an expected slowdown in economic activity stops short of a hard landing for the economy, a Reuters poll showed on Wednesday.

FILE PHOTO: A Canadian dollar coin, commonly known as the "Loonie", is pictured in this illustration picture taken in Toronto January 23, 2015. REUTERS/Mark Blinch

Since early March the Canadian currency has rallied about 3% against its U.S. counterpart as worries the global banking crisis would lead to a credit crunch eased and the U.S. dollar lost ground against a basket of major currencies.

A surge this week in the price of oil, one of Canada’s major exports, has added further momentum for the currency. It touched on Tuesday its strongest intraday level in almost seven weeks, near 1.34 per U.S. dollar, or 74.63 U.S. cents.

The median forecast of nearly 50 currency analysts was for the loonie to weaken to 1.35 per U.S. dollar in three months' time, compared to 1.34 expected in last month's forecast. But it was then expected to rally to 1.30 in a year, which is a gain of 3.5%.

"It's basically a reflection that you get the moderation in (economic) growth ... more of a soft landing than a hard landing, and so the CAD can do okay in that environment," said Mazen Issa, senior FX strategist at TD Securities.

"But if the U.S. (outlook) becomes particularly precarious, if lending conditions tighten significantly ... then we could have a little more problems globally."

The Bank of Canada is ready to step in with support if the banking system comes under severe strain, but now it is not even close to being worried about the health of the financial system, Deputy Governor Toni Gravelle said last Wednesday.

Next Wednesday, the central bank is due to make an interest rate decision and update its economic forecasts. Money markets and economists expect the benchmark interest rate to be left unchanged at a 15-year high of 4.50% after the BoC paused its hiking campaign last month.

Other central banks, such as the U.S. Federal Reserve, may also soon pause.

"I think it's an environment where the (U.S.) dollar loses a bit of its edge," Issa said. "It will give up some ground on the rate differential side."

The gap between Canada's two-year yield and its U.S. equivalent was trading on Tuesday at 27 basis points in favour of the U.S. bond, its narrowest gap since early January.