Exporters hit by loonie's rapid rise

By Barrie McKenna and Richard Blackwell
September 15, 2012 – The Globe and Mail

The loonie's sudden spike is the latest threat to the halting Canadian recovery.

Forget Dutch disease. This looks more like Bernanke disease, a direct consequence of U.S. Federal Reserve chief Ben Bernanke's pledge Thursday to keep U.S. interest rates ultra-low and easy money flowing until at least 2015.

The Canadian dollar, which hit a 13-month high Friday of $1.03 (U.S.) before fading a bit, is being forced up as investors shift money into Canada on the expectation that interest rates will stay higher and rise faster than in the United States.

"Canada is essentially importing U.S. weakness via the currency," said Bank of Nova Scotia economist Derek Holt.

The dollar rally, if sustained, may be great news for Canadian tourists, cross-border shoppers and companies that buy foreign equipment or invest overseas.

But it's a huge hurdle for any company exporting to the U.S. or selling overseas in U.S. dollars. One in five Canadian jobs depends on exports.

Even before the latest spike in the dollar, Canadian exporters were hurting.

The merchandise trade deficit swelled in July to $2.3-billion (Canadian), the largest since Statistics Canada began tracking the data in 1971, driven wider by sharp declines in virtually all of the country's major exports. Exports are down 11 per cent since the end of last year.

Previous run-ups in the dollar were triggered by surging prices of oil and gold and other commodities, raising concerns about Dutch disease, a phenomenon marked by dwindling factory activity and an inflated currency.

Not this time.

"This is a real shock to Canadian monetary policy," said McGill University economist Christopher Ragan, who has worked at both the Bank of Canada and the Finance department. "Interest rates are going to be lower than we thought in the U.S. for a long time."

Mr. Ragan said he expects Bank of Canada Governor Mark Carney will almost certainly delay rate hikes here. But he suggested the bank is unlikely to try to weaken the loonie because it would be difficult, costly and distract Mr. Carney from his main job of keeping inflation at bay.

In an interview Friday, Finance Minister Jim Flaherty didn't rule out intervention if the dollar stays above par. But he suggested the strategy wouldn't work for long. The Bank of Canada hasn't tried to actively manage the dollar since the late 1990s.

"The reality is, whatever we did would have a short-term moderate influence – it is not fundamental – unless we ever moved away from a market currency, and that is not going to happen."

"The dollar is another factor taking steam out of the recovery in Canada. Absolutely," added Conference Board of Canada chief economist Glen Hodgson.

"It is going to force management in every organization to look at their business model, wherever they're dependent on the currency." Being a preferred destination for foreign investors is nice, Mr. Hodgson said. But it ripples through the economy as the dollar appreciates.

John Hayward, president of industrial pump maker Hayward Gordon Ltd. of Halton Hills, Ont., said "We adapted to the dollar at par … But when it gets to this level, it's a real problem, particularly with the volatility."

The company, which exports 30 per cent of what it makes to the U.S., said its only option is buy more U.S.-made parts and relocate some manufacturing south of the border.

Wabi Iron and Steel Corp. of New Liskeard, Ont., a manufacturer of custom metal castings, is focusing on innovation and geographic diversification to cope with the high dollar and the weak U.S. economy.

"I'm trying to reach out beyond the U.S. market," president Peter Birnie said.

"The U.S. is important to us, but we need to have other markets. We're pressing pretty hard in Peru and Brazil right now."

The firm, which makes rail cars and skips for the mining industry, is working to distinguish itself by developing products that can haul more ore, faster, from deep underground with the help of engineers at Queen's University.

"If we're going to deal with the high dollar, the only way to compete in the long term is to build a world-competitive mouse trap," he said.