Canadian dollar's rapid gain spells trouble for exporters

By Eric Atkins
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Like any farmer, Jeff Nielsen keeps an eye on the weather, hoping for an end to the hot, dry spell that hit parts of the Canadian prairies this summer.

He's also watching the Canadian dollar, which has risen by 10 per cent against the U.S. currency since May and threatens to erode the hard-won export markets Western growers and other exporters rely on.

The loonie's rise gained traction after the Bank of Canada's decision in July to raise lending rates for the first time in seven years at a time the U.S. Federal Reserve Board paused its rate hikes amid low inflation.

"Everybody wants a stronger dollar, from the consumer side. But on the export side, there's definitely going to be a hurt," said Mr. Nielsen, the president of the Grain Growers of Canada, who grows wheat, barley and canola on 1,400 acres near Olds, Alta.

Avery Shenfeld, chief economist at CIBC World Markets Inc., said Canada's rise in interest rates has made the country's currency more attractive to investors.

"This has the greatest negative impact on exporters, particularly those without a lot of import content in what they sell," Mr. Shenfeld said. "That would include not only manufacturers, but also the domestic tourism sector."

Retailers and importers benefit from the Canadian dollar's stronger buying power. There are less obvious winners, as well: interest-rate sensitive sectors such as real estate and consumer durable goods, Mr. Shenfeld said.

The currency's gain makes it less likely the central bank will raise interest rates again in the fall, because it has the effect of dampening economic activity and inflation, Mr. Shenfeld said.

However, Canadian companies that do business in the United States will feel the pinch. Both major Canadian railways, Canadian Pacific Railway Ltd. and Canadian National Railway Co. said the strengthening dollar is adding to the uncertainty in the second half of the year.

At CP, which gets 15 per cent of its revenues from U.S.-only freight and 31 per cent from cross-border shipping, every 1 cent rise in the Canadian dollar cuts revenue by about $26-million a year. At the same time, the company's debt ratio would improve and expenses would decrease by $13-million, according to a company presentation to investors.

CN said last week a 1 cent rise in the Canadian dollar costs it $30-million in profit. Even as the growth in freight outpaces that of its rivals, the company said it is not raising its forecast for the full year, pointing to currency headwinds in addition to uncertainty over freight volumes.

Calgary-based WestJet Airlines Ltd. said a stronger loonie would reduce U.S.-dollar-denominated expenses such as aircraft leases, some maintenance costs and airport fees, in addition to plane purchases. And as the Canadian dollar rises, trips abroad become more affordable.

"If the Canadian dollar is higher as a result of rising interest rates resulting from healthy inflation and a healthy economic outlook, then we will generally see more travel by Canadians, which improves our results over time," WestJet spokeswoman Lauren Stewart said.

The Canadian dollar on Friday traded above 80 cents (U.S.), which is the upper end of Mr. Shenfeld's estimate for the year.

A halt to the dollar’s ascent suits Mr. Nielsen, the grain grower, just fine.

“If [the loonie] were to rise substantially, we’d be in serious trouble,” he said, adding a stronger Canadian dollar drives down such expenses as fuel and farm equipment.

Canada is among the top wheat producers in the world, exporting almost half of the 57 million tonnes of grains harvested in the 12 months ending July 29, according to the International Grains Council.

But export volumes are little changed since 2008 and prices have remained low amid large global crops and new competition from Russia and other growers in the Black Sea region.

The rising dollar won’t help, even in a season where unfavourable weather is propping up prices.

Mr. Nielsen said market speculators have been particularly active this summer, exaggerating the wild price swings that stemmed from the drought in the U.S. Northern Great Plains.

Mr. Nielsen sold 30 per cent of this year’s crop even before a seed went in the ground. It’s a common practice and a gamble that he won’t lose his grain in a hailstorm and have to buy out the contract. But it ensures a steady flow of cash in the months ahead and reassures his bank. And at times of a rising dollar, it’s also an inadvertent hedge against falling crop prices.