

FX Forecasts

The Markets Are Pricing Back in a September Rate Cut by the Fed, Shaving Some Value off the Greenback

July 11, 2024

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Highlights

The US economy has slowed, and inflation once again appears to be improving. The ISM Services PMI has slipped below 50, suggesting that the economic slowdown is becoming more broad-based. The job market also shows signs of slackening, including an uptick in the unemployment rate. That said, it's not all bad news for the US economy. The country continues to create about 200,000 jobs each month, and real GDP growth isn't expected to fall much below 2%. But the slower pace of economic growth could well be enough to gradually tamp down inflation and give the Federal Reserve (Fed) room to cut rates. Financial markets recently priced back in an initial rate cut in September, which has helped nudge down the US dollar.

There's also been a lot going on politically. The major currencies were caught between the European elections and the escalating political death match in the United States. Joe Biden's abysmal performance in the June 27 debate forced investors to think about what the US economy could look like next year if Donald Trump comes to power. He's threatening to introduce a number of new tariffs, which could fuel inflation and limit the Fed's ability to cut interest

rates. In the days following the debate, US bond yields temporarily spiked and the greenback appreciated, especially against the Mexican peso and the Canadian dollar.

Meanwhile, the latest inflation figures for Canada weren't quite so encouraging. Inflation ticked back up, confounding analyst expectations of another decline. This weakened the case for the Bank of Canada to go ahead with a second consecutive rate cut in July. But economic activity is still slow in Canada, which should keep disinflationary pressures in place. Recent job market data showed that net job creation stayed flat, while unemployment continued to trend upward. The Canadian dollar is currently trading at around CAN\$1.36/US\$. Over the past few months, that average hovered closer to CAN\$1.37/US\$.

European currencies have been more volatile due to the elections in Europe. The gains made by far-right parties, which are often anti-euro, temporarily fuelled concerns. The snap election in France to counter the rise of the far right also triggered some volatility. The euro briefly traded below US\$1.07 in June, while the Swiss franc enjoyed a short run as a safe haven currency. The Rassemblement National (National Rally) did rather well in the first round of the French election, but its advance was stopped short in the second round, reassuring the markets. However, no party achieved a majority, which means a coalition government must now be formed in France. As for the UK, Labour won a majority government by a landslide. Markets were more enthusiastic about this news, seeing it as the end of a long stretch of political instability in the United Kingdom. The pound surged back above US\$1.28, the upper end of its range for the past few months.

Another currency that has performed well recently is the Australian dollar. We were already aware that the Reserve Bank of Australia had lingering fears over inflation. The central bank has refused to close the door to another rate hike. The most recent inflation numbers were higher than expected, which has increased speculation about a rate hike in Australia, and the AUD/USD pair has settled above US\$0.67.

Main Factors to Watch

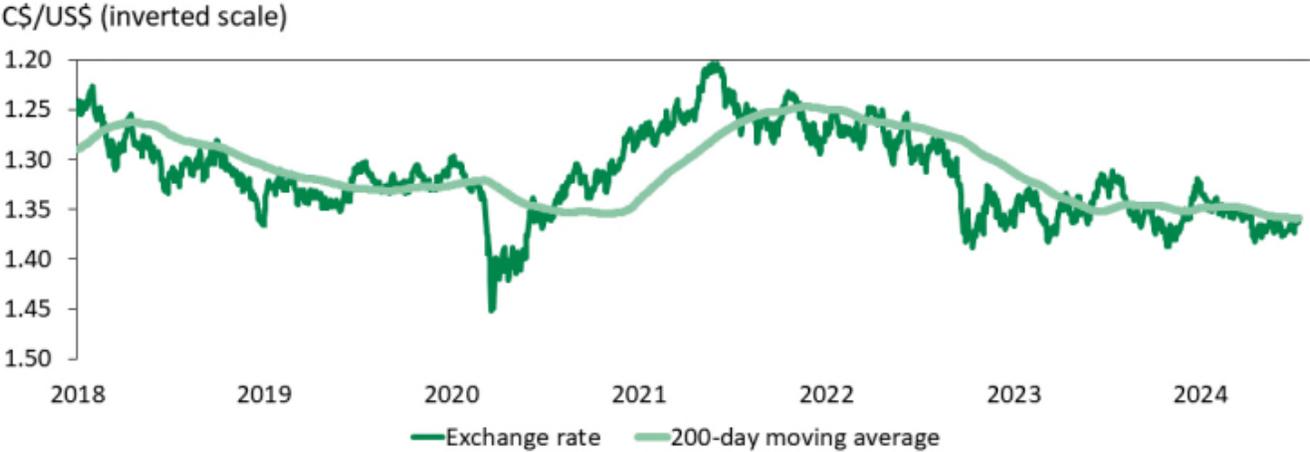
We still expect another rate cut from the Bank of Canada in late July. Since the markets haven't fully priced that in, the Canadian dollar could depreciate

somewhat as a result. The value of the US dollar could also change depending on expectations for the September Fed meeting. We're keeping our forecast for the end of summer at CAN\$1.38/US\$. After that, the loonie could gradually regain some of the ground lost to the US dollar.

What happens with US monetary policy will continue to be a key factor for many exchange rates. We're still not convinced that the Fed would rush into a rate cut in September. We believe it would rather wait until November—after the election and once it sees more compelling signs that inflation is under control. As a result, the US dollar could rally somewhat in the coming weeks.

Main Exchange Rates

Canadian dollar Exchange rate and trend



Euro

Exchange rate and trend



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British pound

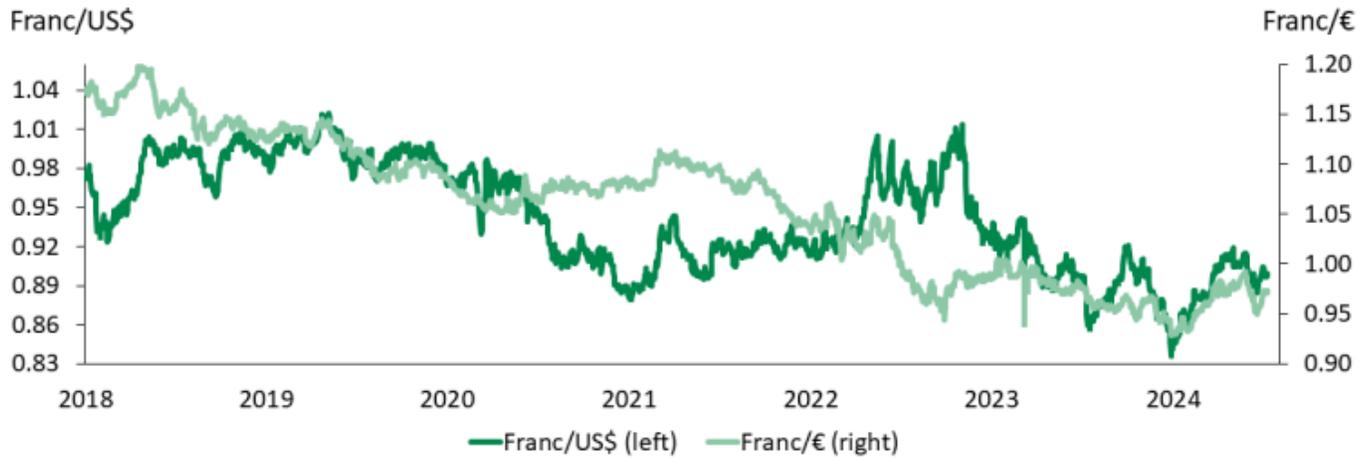
Exchange rate and trend



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Swiss franc

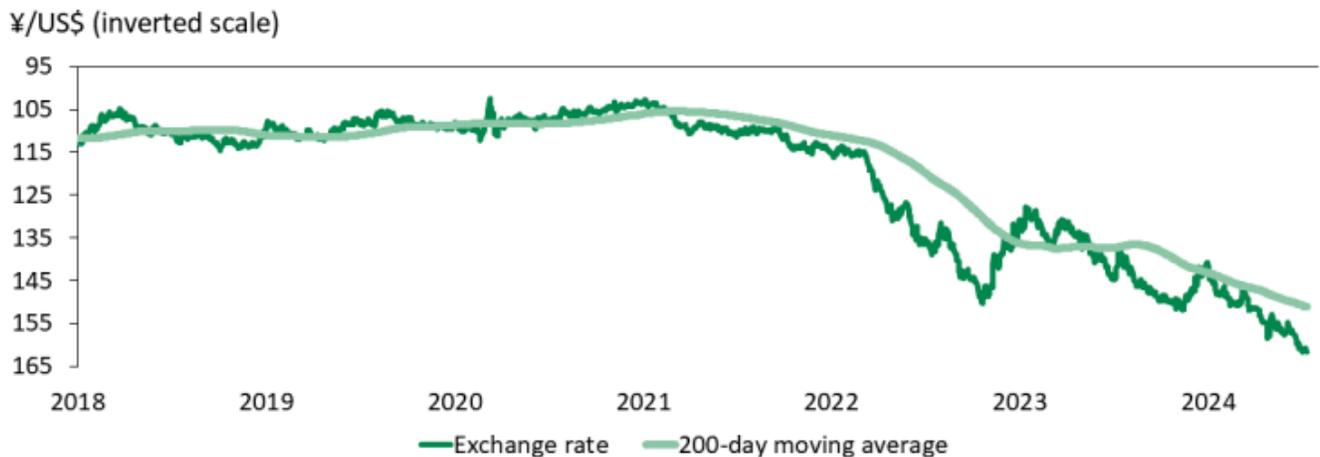
Exchange rate



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Yen

Exchange rate and trend



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Australian dollar

Exchange rate and trend



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Currency Market

Table 1
Yields

Country – Currency*	Spot price	% change				Last 52 weeks		
	Jul 10	1-month	3-month	6-month	1-year	High	Average	Low
Americas								
Argentina – Peso	919.2544	1.97	6.24	12.80	249.99	919.2544	635.0738	262.6510
Brazil – Real	5.3997	0.63	6.59	10.41	10.78	5.6648	5.0189	4.7216
Canada – USD/CAD	1.3620	-1.13	-0.39	1.79	2.59	1.3883	1.3556	1.3113
Canada – CAD/USD	0.7342	1.14	0.40	-1.75	-2.52	0.7626	0.7377	0.7203
Mexico – Peso	17.8430	-3.21	8.23	5.06	4.52	18.8780	17.2440	16.3510
Asia and South Pacific								
Australia – AUD/USD	0.6748	2.08	3.60	0.71	1.08	0.6889	0.6557	0.6292
China – Yuan renminbi	7.2761	0.39	0.58	1.46	0.61	7.3440	7.2261	7.0999
Hong Kong – Dollar	7.8110	-0.02	-0.31	-0.11	-0.22	7.8475	7.8185	7.7913
India – Rupee	83.5200	0.01	0.15	0.59	1.21	83.6645	83.1237	81.7950
Japan – Yen	161.69	2.96	5.55	10.94	14.41	161.70	149.64	138.05
New Zealand – NZD/USD	0.6081	-0.75	1.76	-2.35	-2.06	0.6393	0.6063	0.5803
South Korea – Won	1,385	0.63	2.20	4.89	5.99	1,395	1,336	1,260
Europe								
Denmark – Krona	6.8882	-0.59	-0.81	1.35	1.70	7.1254	6.8960	6.6300
Eurozone – EUR/USD	1.0824	0.83	0.66	-1.31	-1.39	1.1243	1.0814	1.0476
Norway – Kroner	10.7114	0.63	-0.99	3.57	2.20	11.2233	10.6434	9.9603
Russia – Ruble	88.5000	-0.65	-5.30	-1.12	-2.69	101.3000	92.1909	83.5000
Sweden – Krona	10.5439	0.51	-1.55	3.10	-1.97	11.1888	10.6292	9.9405
Switzerland – Swiss franc	0.8995	0.25	-1.37	5.64	1.24	0.9212	0.8875	0.8364
United Kingdom – GBP/USD	1.2830	0.88	2.10	0.73	0.10	1.3119	1.2596	1.2079

* In comparison with the US dollar, unless otherwise indicated.

NOTE: Currency table based on the previous day's close.

Table 2
History and Forecast

End of period	2023		2024				2025				
	Q3	Q4	Q1	Q2	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f	
US dollar											
Canadian dollar	USD/CAD	1.3578	1.3248	1.3540	1.3680	1.38	1.37	1.37	1.36	1.35	1.34
Euro	EUR/USD	1.0588	1.1047	1.0800	1.0718	1.08	1.09	1.10	1.11	1.12	1.12
British pound	GBP/USD	1.2206	1.2748	1.2633	1.2641	1.28	1.29	1.29	1.30	1.31	1.32
Swiss franc	USD/CHF	0.9147	0.8415	0.9007	0.8989	0.90	0.90	0.91	0.92	0.92	0.92
Yen	USD/JPY	149.38	141.07	151.33	160.86	158.00	153.00	148.00	145.00	140.00	137.00
Australian dollar	AUD/USD	0.6435	0.6811	0.6522	0.6668	0.67	0.68	0.68	0.68	0.69	0.69
Chinese yuan	USD/CNY	7.3015	7.0999	7.2213	7.2673	7.30	7.25	7.20	7.15	7.10	7.10
Mexican peso	USD/MXN	17.42	16.97	16.56	18.34	18.00	17.75	17.50	17.25	17.00	17.00
Brazilian real	USD/BRL	5.0073	4.8410	4.9959	5.5586	5.50	5.30	5.20	5.10	5.00	4.90
Effective dollar ¹		117.92	112.81	116.49	117.88	117.20	115.80	114.90	113.80	112.50	111.80
Canadian dollar											
US dollar	CAD/USD	0.7365	0.7549	0.7386	0.7310	0.73	0.73	0.73	0.74	0.74	0.75
Euro	EUR/CAD	1.4375	1.4634	1.4623	1.4661	1.49	1.49	1.51	1.51	1.51	1.50
British pound	GBP/CAD	1.6572	1.6888	1.7104	1.7292	1.77	1.77	1.77	1.77	1.77	1.77
Swiss franc	CAD/CHF	0.6737	0.6352	0.6652	0.6571	0.65	0.66	0.66	0.68	0.68	0.69
Yen	CAD/JPY	110.02	106.48	111.76	117.59	114.55	111.69	108.04	106.58	103.60	102.07
Australian dollar	AUD/CAD	0.8737	0.9023	0.8831	0.9121	0.92	0.93	0.93	0.93	0.93	0.93
Chinese yuan	CAD/CNY	5.3776	5.3594	5.3333	5.3125	5.29	5.29	5.26	5.26	5.25	5.29
Mexican peso	CAD/MXN	12.83	12.81	12.23	13.41	13.05	12.96	12.78	12.68	12.58	12.67
Brazilian real	CAD/BRL	3.6879	3.6543	3.6897	4.0635	3.99	3.87	3.80	3.75	3.70	3.65

f: forecast; ¹ Trade-weighted against major US partners (January 2006 = 100).

Datastream, Federal Reserve Board and Desjardins Economic Studies