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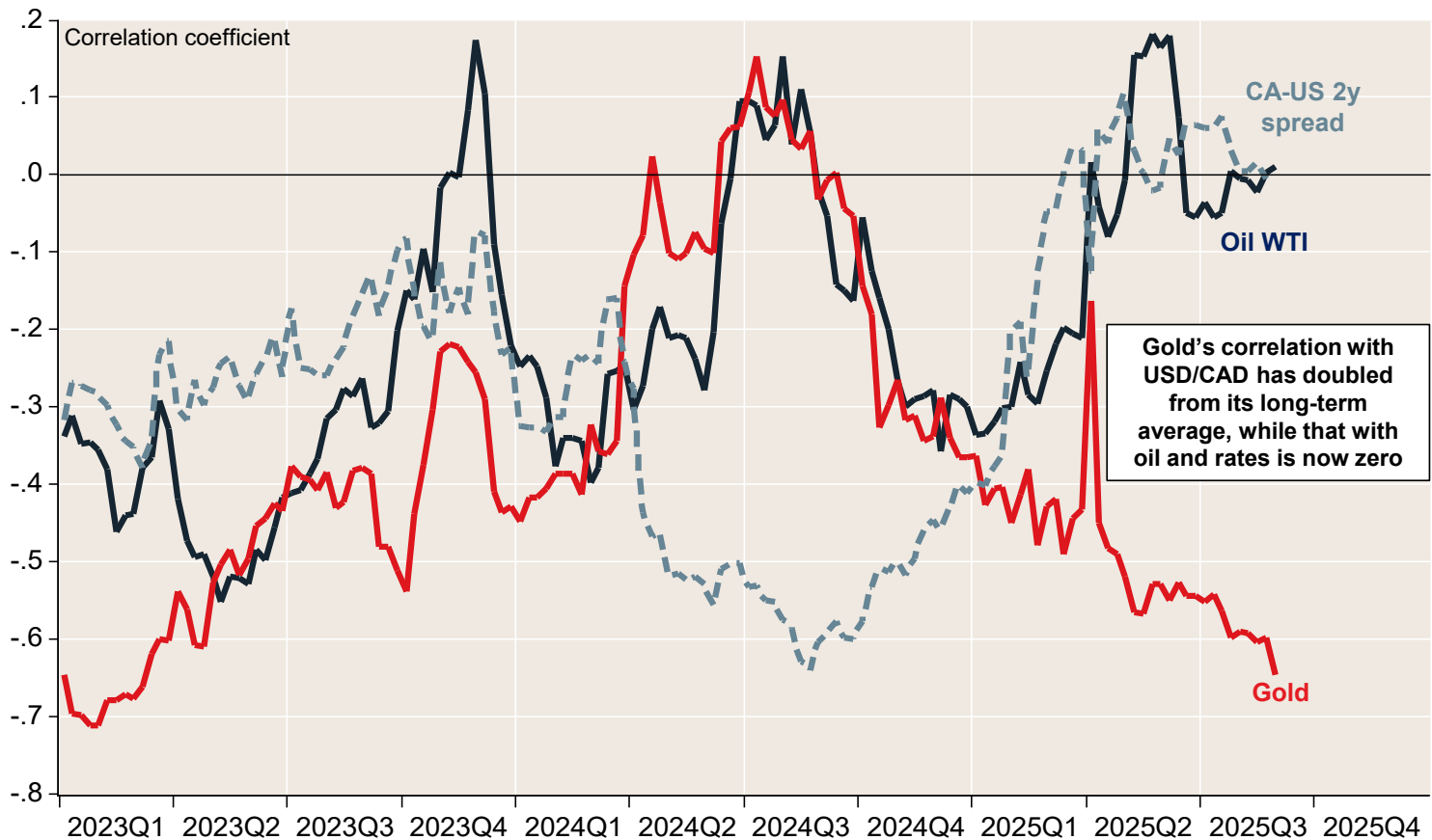
Currency Watch

By Stéfane Marion & Kyle Dahms

Something unusual happened last Friday. Despite a sharp miss on Canadian GDP growth for the second quarter (-1.6% versus -0.5% expected), a further widening of negative U.S.-Canada 2-year spreads, and a drop in oil prices, the loonie managed to finish the day slightly stronger against the greenback. How did the CAD absorb all these negative shocks without losing ground to the USD? The answer lies in bullion. Gold rose nearly 1% on the day, more than offsetting the headwinds from rates and oil. With bullion hitting a new record high, Canada's trade surplus in gold has surged to an unprecedented \$44 billion in the 12 months through June—up from \$30 billion a year earlier. Only crude oil generates a larger surplus (\$111 billion). As today's Hot Chart highlights, daily swings in gold prices have become the dominant driver of USD/CAD. By contrast, interest-rate differentials in 2-year yields and oil price movements show little to no correlation at present. There is no historical precedent for gold exerting such influence over the currency, eclipsing both oil and rates as the primary force behind CAD moves.

Canada: The loonie turns to gold

26-week moving correlations of USD/CAD with gold, oil, and Canada–U.S. 2-year yield spreads



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NBC.EconomicsStrategy@nbc.ca

To contact us:
514-879-2529

Stéfane Marion
Chief Economist and Strategist
stefane.marion@nbc.ca

Matthieu Arseneau
Deputy Chief Economist
matthieu.arseneau@nbc.ca

Jocelyn Paquet
Economist
jocelyn.paquet@nbc.ca

Kyle Dahms
Economist
kyle.dahms@nbc.ca

Alexandra Ducharme
Economist
alexandra.ducharme@nbc.ca

Daren King, CFA
Economist
daren.king@nbc.ca

Warren Lovely
Chief Rates and Public Sector Strategist
warren.lovely@nbc.ca

Taylor Schleich
Rates Strategist
taylor.schleich@nbc.ca

Ethan Currie
Strategist
ethan.currie@nbc.ca

Angelo Katsoras
Geopolitical Analyst
angelo.katsoras@nbc.ca

Nathalie Girard
Senior Coordinator
n.girard@nbc.ca

Giuseppe Saltarelli
Desktop Publisher
giuseppe.saltarelli@nbc.ca

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