

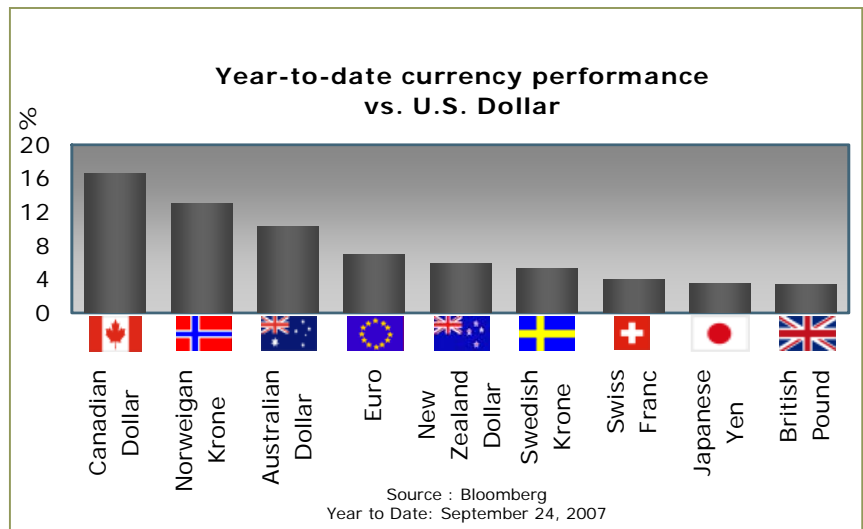


# PARITY AND BEYOND

By: Harvinder Kalirai, Vice-President - Currency Management, CIBC Global Asset Management Inc.  
Elias Haddad, Assistant Vice-President – Currency Management, CIBC Global Asset Management Inc.

The Canadian dollar is the top performing major currency so far this year (chart). This performance suggests that the loonie's strength is not entirely a symptom of a broad-based U.S. dollar decline. The next best-performing currency is the Norwegian krone. Like Canada's, the economy of Norway is also heavily influenced by its oil richness.

The Canadian economy is strong. Consumer spending is growing at an encouraging pace and, given favorable employment and earnings conditions, we expect this strength to continue. Investment spending should also remain a key engine of growth for Canada. The disadvantage of a strong Canadian currency is how it affects an export-based manufacturing sector. To cushion the impact of the rising currency, the beleaguered Canadian manufacturing sector will have to continue to invest heavily in major equipment in an effort to boost productivity.



We believe the Bank of Canada (BoC) can afford to remain on the sidelines and gauge the impact of the U.S. economic slowdown and financial market turmoil before it changes its monetary policy. Inflation expectations in Canada are well founded, and headline inflation, which includes the more volatile food and energy prices, is in the middle of the 1% to 3% range set by Canada's central bank.

We do expect the U.S. economy to experience a soft landing that should allow the BoC to eventually resume its tightening campaign. A soft landing is a rate of economic growth high enough to avoid both inflation and a recession. The BoC tightening and the U.S. Federal Reserve easing would widen the short-term interest rate spread between Canada and the U.S., which would favor the Canadian dollar.

If energy prices keep going up, as we think they will, so will the Canadian dollar. The global demand for Canada's rich resources is being driven by the developing world and not the U.S. Global economic growth is encouraging and demand from Europe and Asia is also robust.

In our view, the path of least resistance for the Canadian dollar is up in relation to the U.S. dollar. However, valuation is getting stretched and the shorter-term technical conditions suggest the Canadian dollar will take the stairs rather than the elevator as it continues its move up. So our currency strategy is to maintain exposure to the Canadian dollar above the benchmark.

*This document has been prepared for the general information of our clients and does not constitute an offer or solicitation to buy or sell any securities, products or services and should not be construed as specific investment advice. The information contained in this document has been obtained from sources believed to be reliable, but we do not represent that it is accurate or complete and it should not be relied upon as such. All opinions and estimates expressed in this document are as of the time of its publication and are subject to change.*