Currency Profile for the Canadian Dollar

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CAD performance against the U.S. dollar:

Current bias for the CAD: ***Negative***

CAD set a six-week low in early February

Past week: +0.40%

Past month: +0.62%

Year-to-date: -0.59%

Sources of CAD strength:

Recent upside surprises to global economic data have fostered a sense of optimism throughout markets and have benefited growth-dependant currencies like the Canadian dollar.

The idea of a North American economic recovery is broadly supportive of Canada's exporters and its economy in general.

While crude oil is well off of its recent peaks, it remains generally well elevated above $70/ barrel.

The relative health of Ottawa's fiscal balance sheet contrasts the disarray of many G7 nations' public finances.

Sources of CAD weakness:

The BOC has flagged the strong Canadian dollar as a key risk to economic recovery. Further signs that CAD appreciation is choking off demand for exports or keeping inflation under target risks ramped up rhetoric from officials.

The tightening of monetary conditions in China in response to inflationary pressures and possible asset bubbles is broadly seen as a negative for commodities and growth-dependant currencies like the CAD.

2009's rally in risk assets appears to have been largely fueled by recovery in the global economy that may prove unsustainable. As government stimulus fades, the risk of another slowdown could weigh on the CAD.

Disappointing trade data for November highlighted the still soft level of demand from the U.S. and raised the risk that currency appreciation could again become a key source of concern for Bank of Canada monetary policy officials.

Monetary Policy: The Bank of Canada has left its key lending rate unchanged at a record low 0.25% since its last 25 basis point cut in April 2009. Since then, domestic and global data have been consistent with a steady, albeit gradual improvement in the economy. Most recent data has shown that Canada's economy emerged from recession in the third quarter by posting a modest 0.4% annualized pace of growth. Retail sales have been surprisingly resilient, falling in only three of the last 11 months, while nearly all measures of housing market activity have show steady improvement, so much so that BOC monetary officials recently dismissed talk of potential asset bubbles forming in Canadian real estate markets. November's GDP showed a relatively healthy 0.4%(m/m) growth rate, suggesting Canada's recovery likely gained momentum in the final quarter of 2009. While encouraging, the recovery in Canada's economy is not yet likely to spur talk of higher lending rates from the BOC. The pace of job losses has slowed markedly from its peak last year, but the unemployment rate remains stuck near a 12-year high and is not likely to drop meaningfully for some time. Moreover, the uneven recovery in the U.S., Canada's largest trade market, should keep policymakers wary of removing monetary accommodation prematurely. Finally, the rise of the Canadian dollar to multi-month highs across the board could once again be flagged as a key risk to recovery and met with condemnation from policymakers who will not want to exacerbate its strength by prematurely tightening monetary policy. Consequently, the BOC is not expected to raise borrowing costs until late in the second half of 2010.

CAD Outlook: *Balance of market opinion:* ***Neutral***

The Canadian dollar has benefited greatly over recent months as a result of signs that the worst of the credit crisis has passed and the resulting improvement in investors' risk appetite. The marked stabilization in the global economy has fostered a sense of optimism among investors, which combined with the massive flood of global liquidity, have pushed commodity prices as well as growth-dependant assets broadly higher. In addition to the rise in the price of crude oil, the CAD has benefited from upside surprises to domestic and U.S. economic data, which have underscored the notion of a North American recovery, one that bodes well for Canada's exporters and its economy in general. Finally, the looine has drawn significant support from the relative health of the nation's fiscal balance sheet. Canada enjoys the lowest national debt of all G7 nations. The CAD should continue to enjoy support in the months ahead, but could become vulnerable in the event of a slide in crude oil prices or additional signs of monetary tightening in China, which investors fear could slow a global economic recovery.

Upcoming critical events:

Feb 10: CA December Trade Balance

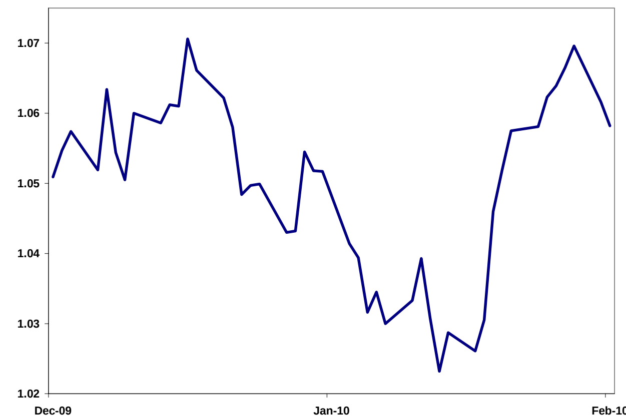
Feb 16: CA December Manufacturing Sales I

Feb 18: CA January CPI

Feb 19: CA December Retail Sales

Mar 2: Bank of Canada Monetary Policy Meeting

Economic indicators	CAD	USD
3-Month Deposit Rate	0.42%	0.36%
GDP (annual rate)	-3.2%(Q3)	5.7% (Q4)
Inflation (annual rate)	1.3%	2.7%
Unemployment	8.5%	10.0%
Trade Balance (US$)	-4.3 bln	-518.4 bln



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