WEST WINDS

Opinion and commentary from the prairies **15-02-13**

A friend of mine sells cars for a living. To be more accurate, he sells trucks, with the occasional car or SUV in the mix at a ratio of about 15:1 trucks to other vehicles. After all, he works for a rural prairie Ford dealership. The other day I asked him how business was, and to my surprise he said “pretty good”. That’s a little counterintuitive, because with the collapse of oil prices many of his potential customers are either worried about their jobs or have recently lost their jobs in the 2015 round of oil patch layoffs. Buying a new vehicle is something you do when you’ve been promoted or landed a new job, not when you’re facing unemployment.

So I asked him who was buying trucks these days. He replied, “think about who has the money”.

“While, ranchers for one, coming off a season of record calf prices”, I remarked.

“To some extent, but there’s only so many of them, and once they all have a nice pickup, that’s about it. Who else?”

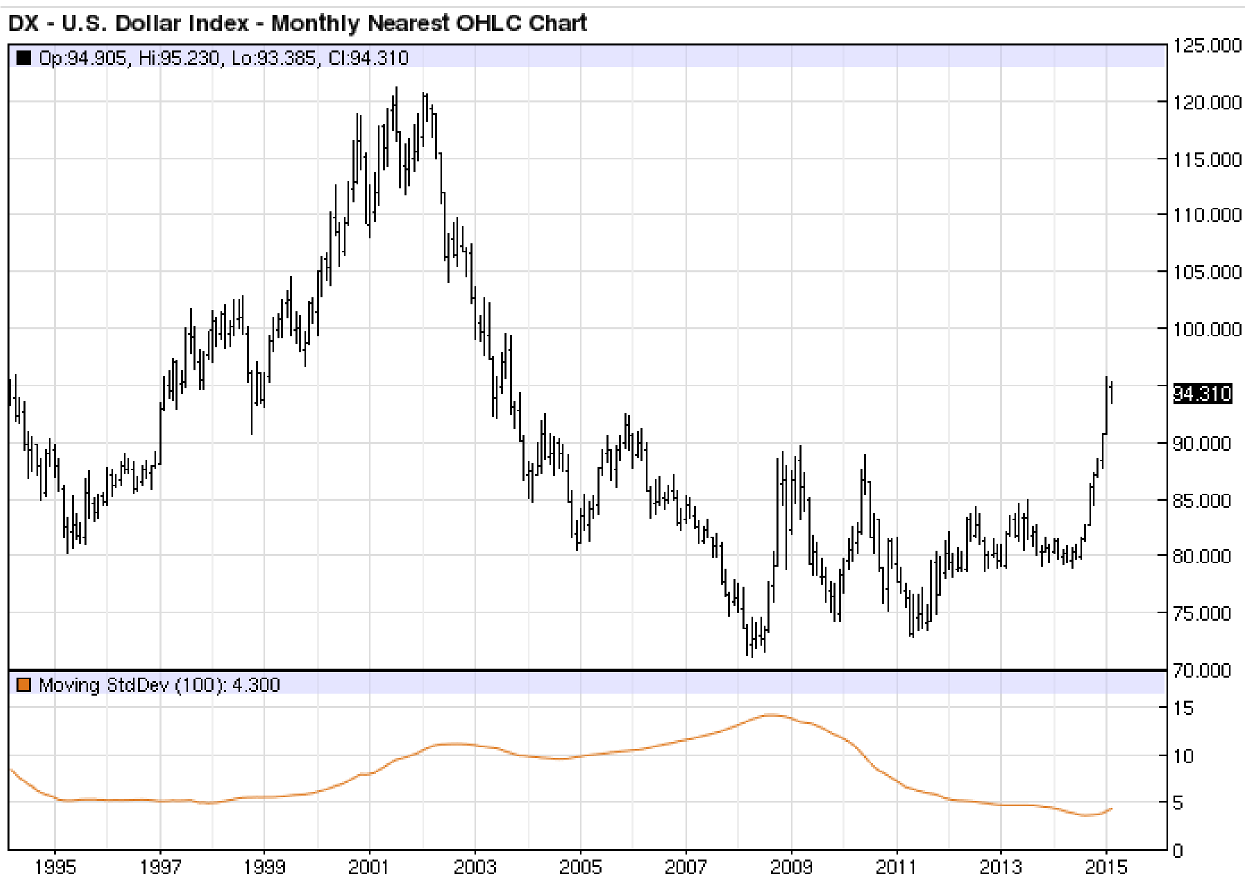
After a brief pause I remarked “Americans. Their economy is doing better than ours and the US dollar is surging.”

“Exactly,” my friend replied. It turns out US buyers are snapping up used pickups on the prairies like wings at a Super Bowl party. The last time this happened was back near the turn of the century, when the Canadian dollar was on a sustained downtrend. At the peak of the last US buying frenzy, it was almost impossible to find a good quality used pickup on the prairies. Used farm machinery prices also surged, as American buyers drove up the prices at auctions. Now, with a 25% currency advantage once again, the hunt for Canadian bargains is back on.

Sustained US dollar strength ahead?

Most people reading this article are probably more interested in the Canadian meat business than the used truck market on the prairies. You are also probably well aware that the exchange rate has a huge impact on your business, both day to day and more importantly in the long term. A sub-80 cent dollar is going to go a long ways towards making Canadian meat and livestock operations of all types more competitive with their US counterparts. Indeed, most of the current prairie livestock infrastructure was built on the premise of a weaker dollar. Not the strongest foundation to build on, to be sure, but of course hindsight is always 20:20.

One way to think about a currency is the price the global market places on an overall economy and its assets. I am reminded of a trip to Bolivia in my youth, and seeing peasant women hawking baskets full of paper currency valued at several thousand pesos to the dollar. Obviously, the world at that time was not clamoring to acquire Bolivian assets. But since about mid-2014, with the end of quantitative easing in the US, the surge in US equities, and some notable setbacks in other world economies (Japan, Europe, Russia, etc.) there has been quite a run on US currency. (The lower loonie is more about US strength than Canadian weakness). As impressive as the run-up so far has been, a 25 year chart-based analysis shows that we are far from any historical extremes in US dollar strength at this point (Barchart.com).



At this point I would like to offer up some third party analysis from a US source, Fidelity Investments. In my view, the Canadian dollar analysis provided by our chartered banks and other financial experts is too Canada-centric and often misses the bigger picture. As I have already claimed, this is not really about the loonie but rather all global currencies compared to the US dollar. The following is an excerpt from the January 16, 2015 version of ***Fidelity Viewpoints***. The commentators are each responsible for equity funds valued in the 100s of millions. Of course that doesn't mean they are always right, but I do respect their opinions.   If you read the investor's commentary, you might come to the conclusion that good 'ol boys from the US will be busy buying pickups on the prairies for a while to come.

Hogan: The consensus certainly seems to be that the U.S. dollar will stay strong and likely get stronger in 2015. Anyone want to differ from that consensus?

Derek Young (President, Global Asset Allocation, and Vice Chairman, Pyramis Global Advisors): If you look at central bank policy, with the U.S. tightening while other major economies are doing the reverse, it suggests we'll have a stronger dollar for an extended period. We're only two or three years into this strengthening cycle. Although past performance may not be indicative of the future, the last one lasted much longer, from 1994 to 2001.

DeSantis (Equities): At that time, the U.S. benefited from a wave of globalization. Companies were able to drive costs down while revenues went up due to increased U.S. demand, which created a huge tailwind for their earnings and the equity market. What makes the current dollar's position seem even more unique is that last time this happened, the Germans (euro) were also trying to maintain the strength of their currency. Now, virtually no currency union or country is really trying to do that. Hence, I think the surprise might not be that consensus is wrong, but that the dollar strengthening cycle goes further, or lasts longer, than most people expect.

Cohen (Equities): It's always a little worrying to be part of the consensus view, but I have to admit I see a lot of reasons for the dollar to continue appreciating and very few for it to go the other way.

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