CIBC Asset Management

MARKET SPOTLIGHT - AUGUST 2021

Revisiting currency – Traditional meets crypto

The global return to normal has begun. The global economy is steadily improving, even though a sharp rise in COVID cases over the last month, especially among the unvaccinated, has the potential to stall near-term progress. The many crosscurrents we're experiencing—different central bank moves, uneven pandemic progress across various regions, unpredictable consumer behaviour—have potential implications for many financial markets, including the currency market. In this edition, we talk currencies and revisit our near-term forecast for the Canadian dollar.

We're also kicking off a new monthly series that will attempt to answer readers' most-commonly-asked questions about cryptocurrencies. If you're considering an investment in crypto you'll probably want to know how crypto works, whether it's just a passing trend and what are the mechanics of dealing in crypto?

If you have questions on crypto that you'd like to see answered in future editions, please email me using "Crypto Question" in the subject line.

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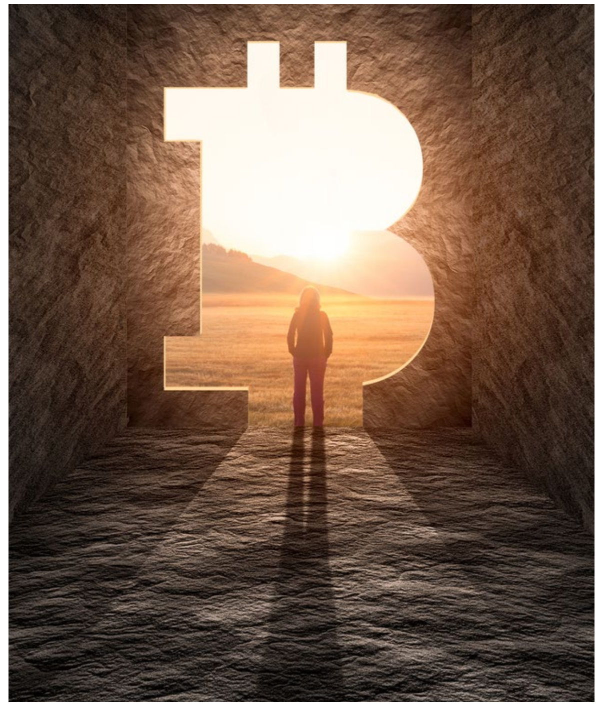

Update on the Canadian dollar

Luc de la Durantaye
Chief Investment Strategist

As we mentioned in our recent edition of Perspectives, the global economy continues to expand and grow as reopening continues. That's supportive for trade and supportive for commodity prices and oil—all relative positives for the Canadian dollar. Canada's trade balance recently swung back into the black (see below), while, in contrast, the U.S. economy continues to have a large current account deficit—a fundamental negative which creates downward pressure on the greenback.

The loonie remains undervalued versus the U.S. and we may see the Canadian dollar stabilizing around current levels (around 79.5) and possibly appreciating from there. We could perhaps reach an 82–83 cents Canadian dollar in the shorter term.

While we believe the U.S. dollar will decline over the longer term, it may be supported in the short term against the currencies of some other major economies (e.g. the European economy, the Japanese economy and even the Chinese economy). The U.S. could start removing stimulus and tightening the monetary environment a bit, which could lead to range trading for the U.S. dollar relative to the euro, yen and the Chinese renminbi.

For the euro, the European Central Bank (ECB) just reviewed its inflation target and seemed to be adopting a bit more dovish policy. They'd do this to achieve their inflation target—a target they've missed for over 10 years. That would put a little bit of downward pressure on the euro, and we could see the euro as one of the weaker currencies over the next six to 12 months.

Canadian trade balance swings back into the black

Canada's trade balance swung back into the black in a big way in June. The more than $3bn surplus (the largest since 2008) was a huge surprise given that all of the professional forecasters surveyed were expecting a modest deficit. It was driven by a massive 8.7% increase in exports, with 9 of 11 product sections increasing in June. It was helped by higher prices, but most of the gains came from volumes. The 23% increase in energy exports was largely attributable to higher real exports of crude oil.

Source: CIBC Capital Markets as at August 5, 2021

CryptoCorner: Answering your questions

Michael Sager
Vice-President, Multi-Asset and Currency Management

Will cryptocurrency become a widely used medium of exchange?

Yes, on a limited basis. But outside of periods of heightened speculative interest, the growth of Bitcoin transactions has so far been relatively muted.

Merchants who accept bitcoin as a means of payment often immediately convert it into fiat currency[1], given its high volatility and average settlement confirmation delays of 10 minutes (i.e. this is the time it takes to verify a new block of bitcoin transactions).[2]

Here are factors that could limit cryptocurrency's adoption as a medium of exchange:

- Fiat currencies are already entrenched in existing payment systems and they'll likely be hard to dislodge. Existing payment systems are also evolving to resist the threat posed by cryptocurrencies.
- Major economies may be introducing their own versions of digital currency (Central Bank Digital Currencies or CBDCs) as a digital version of cash.
- The length of time involved in a Bitcoin transaction makes its adoption impractical for a physical retailer. Online retailers could be more likely to accept crypto as neither party involved in a transaction has to physically wait for it to clear.
- There's low payment processing capacity for cryptocurrency versus established networks. For example, the Bitcoin network can process around 10 transactions per second, compared to a capacity of 65,000 transactions per second on VisaNet.[3]

Cryptocurrency is a digital asset designed to work as a medium of exchange. Individual coin ownership records are stored in a ledger in a form of computerized database using strong cryptography to secure transaction records, control the creation of additional coins, and verify the transfer of coin ownership. It typically does not exist in physical form (like paper money) and is typically not issued by a central authority.[4]

Blockchain is the digital platform behind Bitcoin and other cryptocurrencies. It is intended to create faster, more efficient ways to transmit, receive, and track orders using secure data.[5]

Coming in September CAM Market Spotlight: *Bitcoin supply Is limited - Is that a good thing?*

[1] Fiat money is currency that a government has declared to be legal tender but is not backed by a physical commodity. Examples include the Canadian dollar, U.S. dollar, euro, Japanese yen.
[2] Statista (2021), https://www.statista.com/statistics/793539/bitcoin-transaction-confirmation-time/
[3] https://usa.visa.com/dam/VCOM/download/corporate/media/visanet-technology/aboutvisafactsheet.pdf
[4] https://en.wikipedia.org/wiki/Cryptocurrency
[5] https://www.investopedia.com/blockchain-4689765