

## CAD: Markets turning more bullish

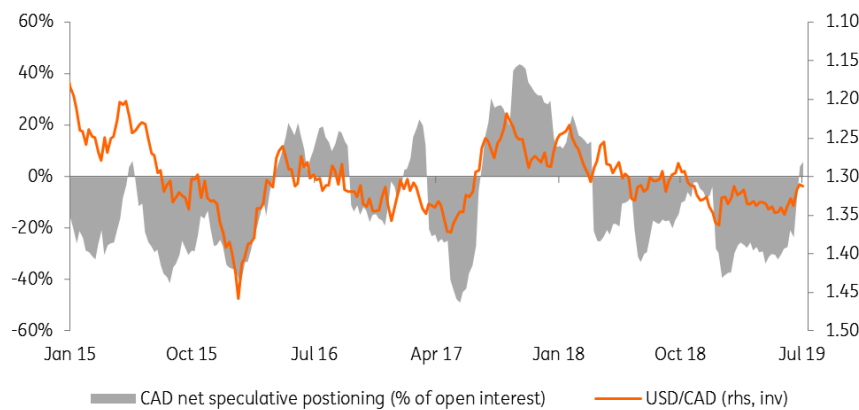
Net positioning in the Canadian dollar has jumped into long territory in July. We expect markets to be reticent to enter additional long-CAD positions for now, although we maintain a long-term bearish bias on USD/CAD



Source: iStock

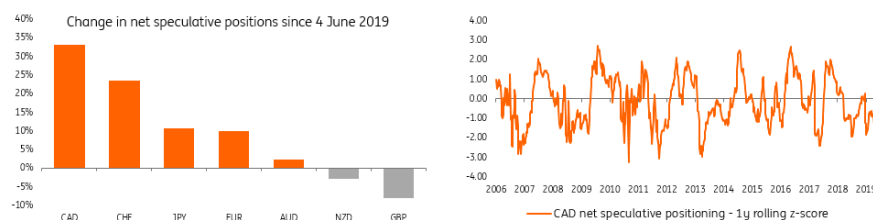
### Markets have turned increasingly optimistic on CAD

CFTC commitment of traders data showed how in July – for the first time since 1Q18 – long combined speculative positions on CAD have outnumbered the shorts (Fig. 1). This comes as investors have gradually abandoned their bearish views on CAD and slashed short positions in the past month. On 4 June, market shorts on CAD were 27% of open interest, whereas the latest numbers show net longs amounting to 6% of open interest. No other currency in the G10 space has displayed such a marked upside move in net speculative positions in the same period (Fig. 2).



Source: CFTC, Bloomberg, ING

Market sentiment on the loonie has been diverging compared to other commodity currencies such as the Australian and New Zealand dollars. This is likely due to the divergence in monetary policy. The Reserve Bank of Australia delivered back-to-back rate cuts in June and July while the Reserve Bank of New Zealand has maintained an easing bias after cutting in May. In contrast, the BoC has maintained a neutral policy stance. When normalising the data through rolling 1y z-scores (Fig. 2), the magnitude of CAD short-covering in recent weeks appears even sharper. This could suggest that a deeper move into net long territory is not imminent. In particular, we suspect that as long as the threat of another escalation in US-China trade tensions lingers - and given the already meaningful move in CAD in the past few weeks - investors may refrain from entering heavily bullish positions on CAD. If anything, positioning might suffer from a light downward correction in the short-term.



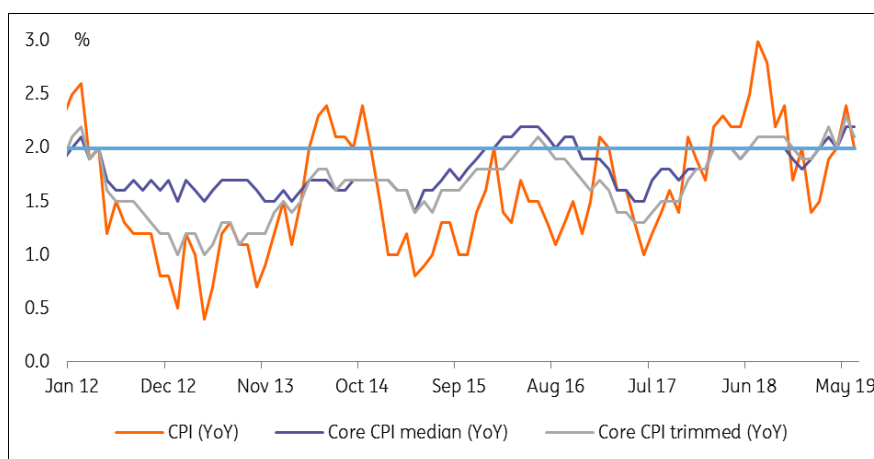
Source: CFTC, Bloomberg, ING

## What lies ahead for the loonie?

Yesterday's CPI numbers confirmed that robust price growth remains a strong point in favour of a neutral BoC stance on monetary policy. Headline inflation decreased from 2.4% to 2.0% in June (as widely expected), but all core measures have remained above the 2% BoC target mid-point. We believe the Bank of Canada will not decrease policy rates at least for the next 18 months, particularly when considering that:

- The BoC did not raise rates as fiercely as the Fed in the past few years and can therefore take its time before following any Fed easing
- The labour market remains tight: June's decrease in jobs was all due to the part-time segment, while wage growth peaked
- The outlook for oil remains constructive after the OPEC+ output cuts
- The USMCA deal should soon be ratified, with reservations from US Democrat gradually

fading



Source: Bloomberg, ING

A possible re-escalation in trade tensions between the US and China indeed has the potential to dampen appetite for risk-sensitive currencies such as CAD, but we expect the mix of factors mentioned above to provide some support to the currency, keeping any upside in USD/CAD limited. We forecast that the recent downward pressure on the currency pair will resume in 4Q19, when we expect trade tensions to abate, crude prices to peak and US-Canada policy divergence to linger. Accordingly, we do not exclude another upward move in the CAD positioning indicator towards the end of the year, when USD/CAD should start to test the sub-1.300 area.

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