Weaker Loonie Hurts Canadians More Than It Helps

This week the Canadian dollar dropped below 90 cents US. Good news, say some economists, for the Canadian economy. But in reality, the negative impact of a weaker loonie will likely outweigh any benefits.

It's a myth that devaluation of the Canadian dollar broadly stimulates the economy and leads to prosperity. In fact, a weaker loonie triggers higher domestic prices, which hit consumers in the wallet, and higher importing and financing costs, which hurt businesses and government. You can read more about this in the analysis *Economic Consequences of the Lower Canadian Dollar.*

For example, certain commodities—such as gasoline—are priced in US dollars. So when the loonie drops, people pay more at the pumps.

The cost of doing business will also increase. Canadian businesses import 55 per cent of their machinery and equipment. When faced with higher prices, businesses will buy less machinery and equipment, and consequently limit production, which may limit employment opportunities and hurt worker wages.

Canadian governments, meanwhile, will pay more when managing debt denominated in US dollars, particularly provincial governments and their utilities (i.e. natural gas or electricity), which issue the most bonds denominated in non-Canadian currency.

However, there are benefits—albeit overstated, in some cases.

Exporters benefit from a lower exchange rate. Why? Because Canadian exporters exchange goods for US dollars, so when the loonie is relatively low, those US dollars, when repatriated, buy more Canadian dollars.

But even for exporters, the benefits of a lower exchange rate are likely to be limited, because market demand is the primary driver of exports—not the relative strength or weakness of the loonie.

Moreover, exporters may rely too heavily on a depreciating dollar, which can lead to investments that only make sense with a weaker loonie.

Canadian natural resource industries should benefit most from a lower Canadian dollar. Oil and gas firms, for example, export much more than they import, so a weaker loonie will boost their bottom line.

For individual Canadians, anyone invested abroad will pocket more Canadian dollars when those investments are brought back home.

However, this is a dubious benefit to the Canadian economy because it rewards people for not investing in Canada, and consequently, lowers the value of all assets in the country.

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