



## BANK OF CANADA

# ADJUSTING TO THE APPRECIATION OF THE CANADIAN DOLLAR

### Results of Bank of Canada Business Interviews

October 2004

#### Highlights

During visits conducted between 23 August and 14 September 2004, representatives of the Bank of Canada again interviewed businesses to gauge the impact on their operations of the Canadian dollar's appreciation since the beginning of 2003, as well as their responses. The results underscore those of previous surveys and are summarized below.

- Nearly twice as many firms reported being adversely affected by the appreciation of the dollar as reported benefiting from it.
- Exporting companies were clearly the hardest hit, especially those in manufacturing and natural resources.
- The main negative effects were shrinking profit margins on exports caused by reduced revenues in terms of Canadian dollars, although some firms again reported smaller export volumes. A few companies saw domestic sales decline in the face of increased competition from cheaper imports. Others were affected indirectly via the effect of the appreciation on their clients.
- Firms benefiting from the appreciation of the dollar were mainly in the wholesale and retail trade sector. These firms experienced a reduction in the cost of imported inputs.

The following observations concern the adjustments made by firms to the appreciation of the dollar:

- Approximately 40 per cent of the firms adversely affected did not make any adjustments, since the appreciation had only a minimal effect on their revenues.
- Those harder hit by the appreciation focused their efforts on improving productivity and reducing costs.
- The survey indicates that firms hurt by the dollar's appreciation are almost as optimistic as others about their outlook for future sales. However, they remain less positive than others about the growth of their labour force and investments.
- Among firms benefiting from the appreciation, there was a substantial jump from the last survey in the number citing a reduction in their investment costs.
- The number of firms that benefited from lower input costs as a result of the appreciation has not changed since the April survey, but the magnitude of cost reductions is perceived to be less. As well, fewer firms appear to have passed through the reductions to their output prices.

*Note: This document and the autumn Business Outlook Survey summarize responses obtained during interviews with about 100 businesses across Canada between 23 August and 14 September. Firms were selected to provide a representative profile of the Canadian economy by region, industry type, and firm size. The method of sample selection ensures a good cross-section of opinion. Nevertheless, the statistical reliability of the survey is limited, given the small sample size.*



Chart 1: Effects of Appreciation by Sector

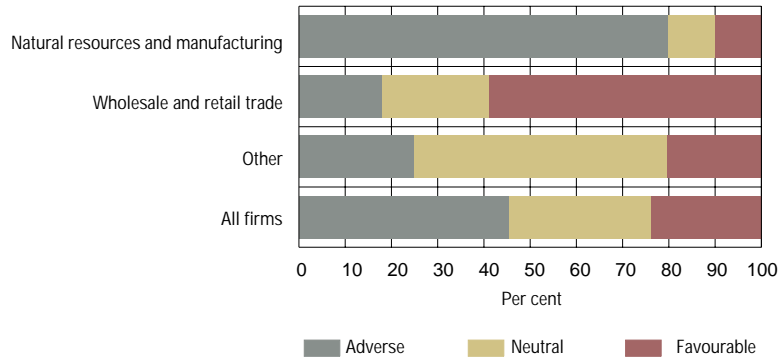
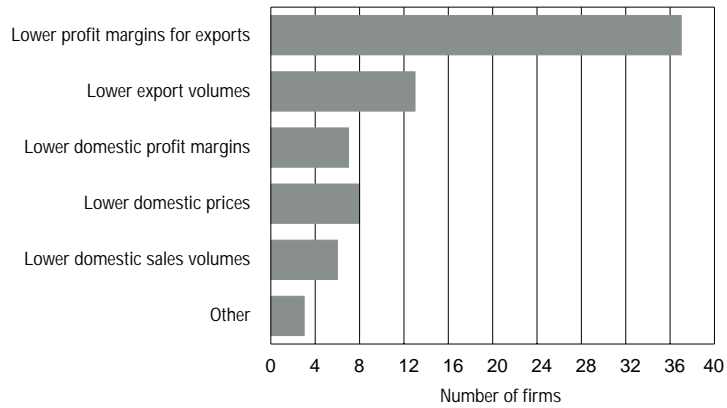


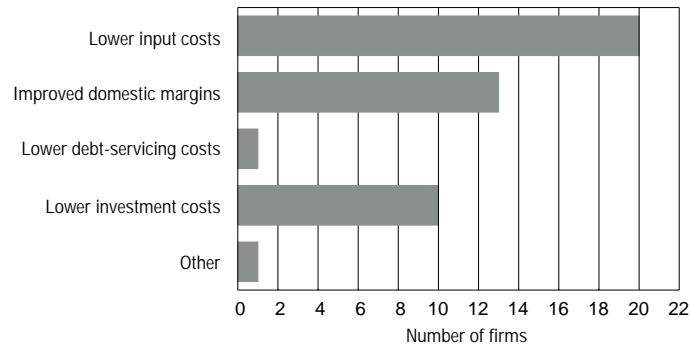
Chart 2: Firms Adversely Affected: Main Effects (46 Firms)



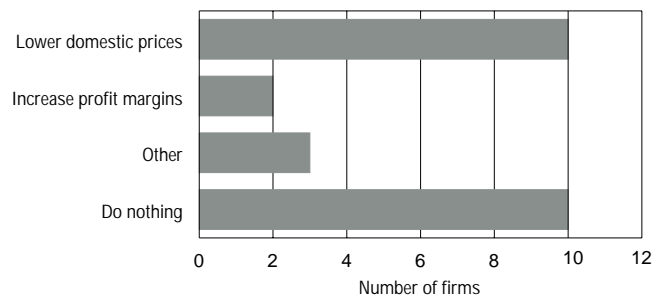
**Chart 3: Firms Adversely Affected: Main Reactions (46 Firms)**



**Chart 4: Firms Favourably Affected: Main Effects (24 Firms)**

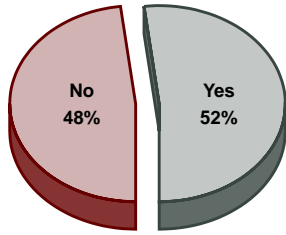


**Chart 5: Firms Favourably Affected: Main Reactions (24 Firms)**



**Chart 6: Exchange Rate Pass-Through**

Since January 2003, has there been downward pressure on your input costs because of the appreciation of the Canadian dollar?



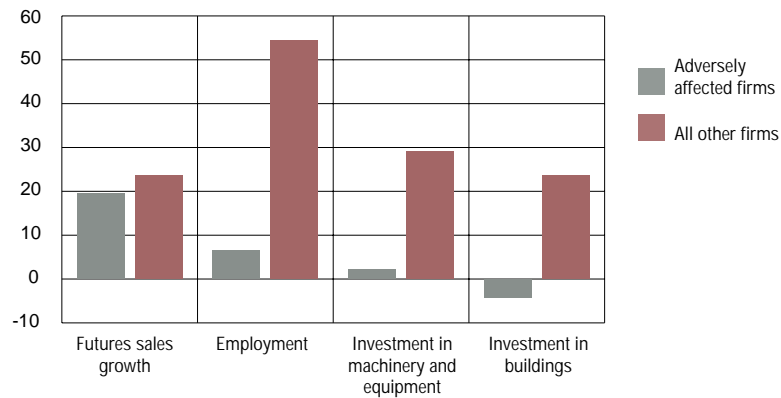
**Magnitude of Cost Reductions**

Magnitude	< 5%	5-10%	> 10%
% of firms	63%	12%	25%

**Pass-Through to Output Prices**

Reactions	Have not reduced	Already reduced
% of firms	65%	35%

**Chart 7: Balance of Opinion<sup>1</sup> on Selected Variables**



1. Percentage of firms expecting faster growth (for sales) or higher levels (for employment and investment) minus percentage of firms expecting slower growth or lower levels over the next 12 months.

