Forex

Economics and Strategy

June 2025

Highlights

By Stéfane Marion and Kyle Dahms

- The U.S. dollar has fallen nearly 8% from its peak, weighed down by tariff uncertainty, rising import costs, and investor caution. Labour market signals are mixed, and inflation pressures persist. Long-term yields remain elevated due to fiscal concerns, including a proposed $2.4 trillion tax bill. While short-term gains are possible amid global volatility, structural vulnerabilities and policy uncertainty continue to undermine the USD's outlook.
- The Canadian dollar rose 3.5% against the greenback in Q2, buoyed by oil prices and U.S. dollar aversion. Yet, weak domestic demand, rising unemployment, and new U.S. tariffs cloud the outlook. We expect the Bank of Canada to go against current expectations and cut rates in July, likely weakening the loonie. Still, Ottawa's latest Throne Speech signals a decisive break from the Trudeau-era approach, positioning Canada to attract private capital. USD/CAD is projected to peak at 1.38 before trending toward 1.34.
- The euro has gained 5% against the USD since April, supported by Eurozone stability, strong exports, and expectations of German fiscal stimulus. However, it now trades well above valuation anchors, diverging from rate differentials. The ECB has cut rates seven times, but with inflation near target and unemployment low, further easing may be limited. Trade tensions with the U.S. and fading speculative momentum pose risks. While diversification away from the dollar supports the euro, its rally appears stretched.

NBC Currency Outlook

		Current	Forward Estimates			
Currency		June 12, 2025	Q2 2025	Q3 2025	Q4 2025	Q1 2026
Canadian Dollar (new forecast)	***(USD / CAD)***	**1.36**	**1.37**	**1.38**	**1.36**	**1.34**
United States Dollar	*(CAD / USD)*	*0.74*	*0.73*	*0.72*	*0.74*	*0.75*
Euro	*(EUR / USD)*	1.16	1.15	1.14	1.16	1.18
Japanese Yen	*(USD / JPY)*	144	145	143	140	138
Australian Dollar	*(AUD / USD)*	0.65	0.65	0.64	0.66	0.67
Pound Sterling	*(GBP / USD)*	1.36	1.35	1.35	1.36	1.37
Chinese Yuan	*(USD / CNY)*	7.17	7.20	7.18	7.14	7.10
Mexican Peso	*(USD / MXN)*	18.9	19.5	20.0	19.8	19.4
Broad United States Dollar [1]		**120.2**	**121.5**	**122.3**	**120.7**	**119.1**

1) Federal Reserve Broad Index (26 currencies)

Canadian Dollar Cross Currencies

		Current	Forward Estimates			
Currency		June 12, 2025	Q2 2025	Q3 2025	Q4 2025	Q1 2026
Euro	*(EUR / CAD)*	1.57	1.58	1.57	1.58	1.58
Japanese Yen	*(CAD / JPY)*	106	106	104	103	103
Australian Dollar	*(AUD / CAD)*	0.89	0.89	0.88	0.90	0.90
Pound Sterling	*(GBP / CAD)*	1.85	1.85	1.86	1.85	1.84
Chinese Yuan	*(CAD / CNY)*	5.27	5.26	5.20	5.25	5.30
Mexican Peso	*(CAD / MXN)*	13.9	14.2	14.5	14.6	14.5

USD: OBBB is not greenback friendly

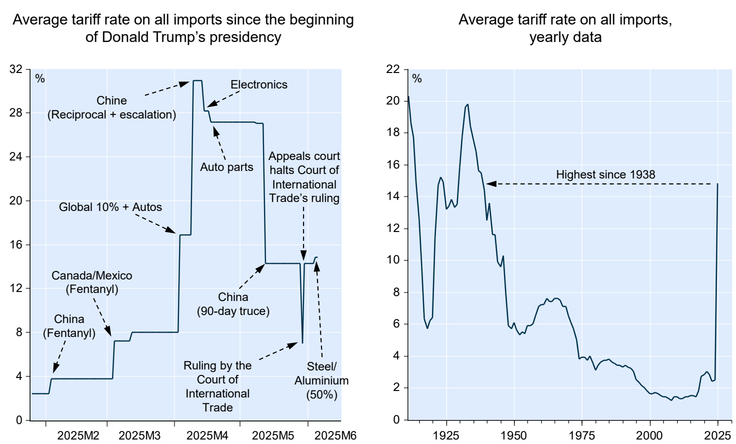
The U.S. dollar continues to weaken, having shed nearly 8% on a trade-weighted basis from its cyclical peak earlier this year (chart).

USD: Greenback continues to slide
Federal Reserve trade-weighted USD (26 currencies)

NBC Economics and Strategy (data via Refinitiv)

Tariff uncertainty remains a key drag on sentiment, undermining investor confidence in U.S. assets. Despite recent signs of de-escalation, the average duty on American imports is still expected to rise sharply in 2025—raising input costs for manufacturers and threatening corporate margins (see chart).

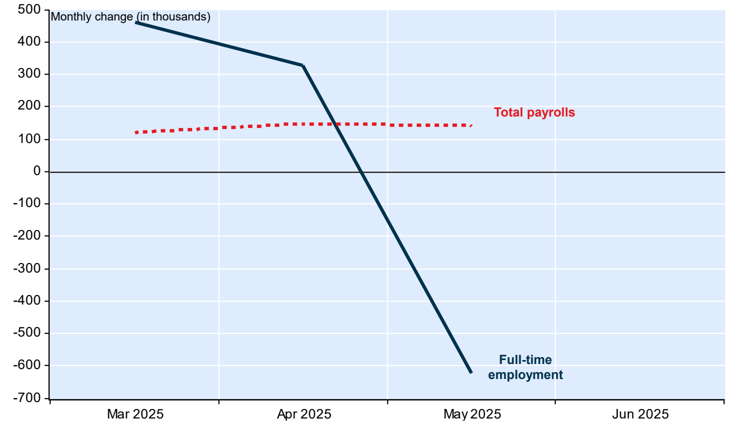
U.S. : Tariff remains elevated even after de-escalation



NBC Economics and Strategy (data via the Tax Foundation and NBC calculations)

Corporations appear to be exercising caution. While payroll data showed a net gain of 132,000 jobs in May, the household survey revealed a sharp loss of over 600,000 positions (see chart).

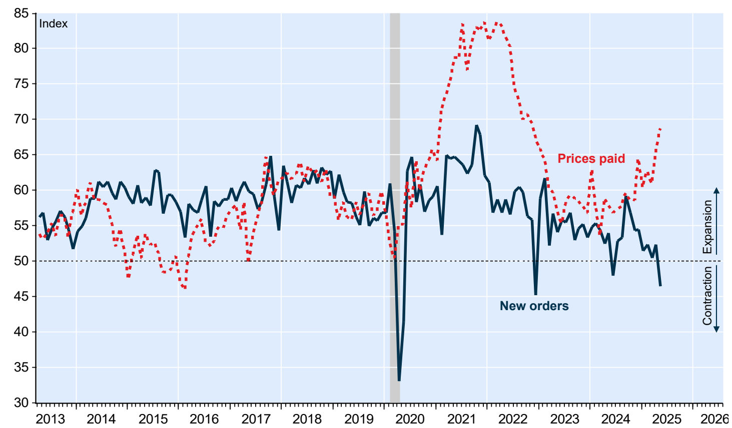
U.S.: Corporations are hiring, but not full-time
Payroll jobs and full-time employment



NBC Economics and Strategy (data via Refinitiv)

This divergence suggests that, amid heightened uncertainty, firms are reluctant to commit to full-time hiring—favoring flexible or temporary arrangements instead. Cost pressures are clearly mounting, as reflected in PMI data: the "prices paid" sub-indices in both ISM services and manufacturing have spiked sharply (see chart).

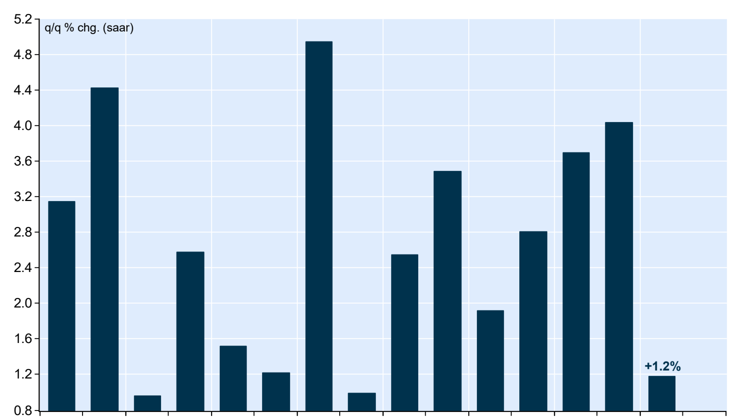
U.S.: Stagflationary vibes
ISM Services Survey



NBC Economics and Strategy (data via Bloomberg)

A further decline in full-time employment would weigh on consumer spending and the broader economy (see chart).

U.S.: Weakest consumption growth in nearly two years in Q1
Real personal consumption expenditures

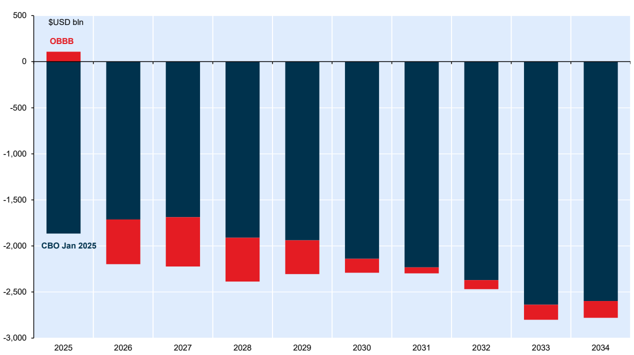


NBC Economics and Strategy (data via Refinitiv)

Meanwhile, the outlook for growth is softening, setting the stage for wider deficits and limited relief from long-term interest rates, as investors demand higher term premia to lend to Uncle Sam. Despite a 21 bp drop in the 2-year Treasury yield since President Trump's election victory in November, the 30-year yield has climbed 47 bps over the same period—highlighting persistent concerns about fiscal sustainability.

While rates may drift slightly lower in the coming quarters, our rate strategists do not anticipate a meaningful move away from the 5% level. That's partly due to ongoing fiscal expansion, now amplified by the "big beautiful" tax bill advancing through Congress. If enacted, it could add approximately $2.4 trillion to the deficit over the next decade, with nearly $1.8 trillion of that red ink accumulating within just five years (see chart)—a trajectory unlikely to reassure investors.

US: The One, Big, Beautiful… deficit!
U.S. deficit projection – CBO baseline and estimated impact of the 'OBBB'



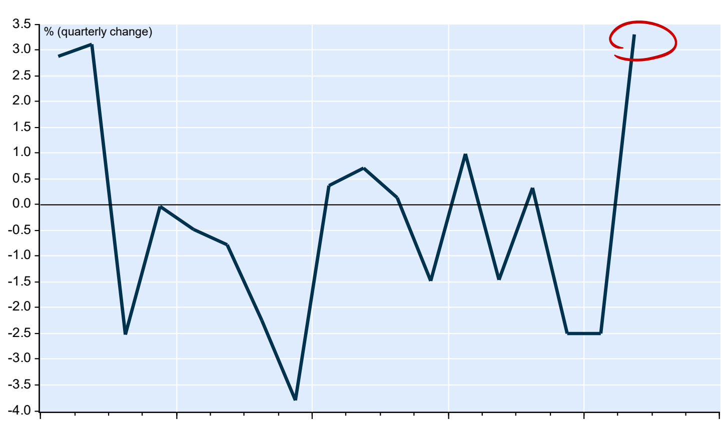
Source: NBC, CBO | Note: 'OBBB' refers to the 'One, Big, Beautiful Bill' / H.R.1 Act

While the USD may experience brief strength in the coming weeks due to potential global market turmoil—driven by cyclical or geopolitical shocks—any such rebound is likely to be short-lived. Without a more coherent and credible framework from Washington for engaging with its allies, the greenback will remain structurally vulnerable. Global investors are increasingly reassessing their U.S. exposure, and absent a shift in policy direction, that trend is likely to continue.

CAD: Momentum meets macro headwinds

The Canadian dollar has been a key beneficiary of U.S. dollar aversion, appreciating nearly 3.5% so far in Q2—its strongest quarterly gain in four years (see chart).

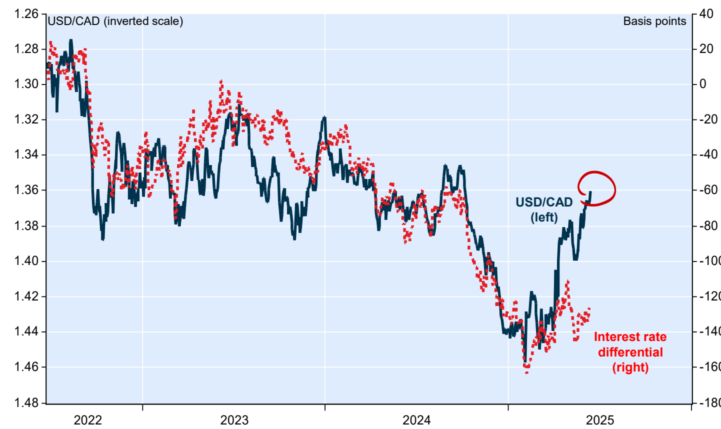
Canada: Loonie surges by the most in 4 years in Q2
USD per CAD



NBC Economics and Strategy (data via Refinitiv)

As a result, USD/CAD reached 1.3602 on June 12—its highest level in eight months. This is a notable milestone, especially considering that the short-term interest rate differential between Canada and the U.S. remains sharply negative (see chart).

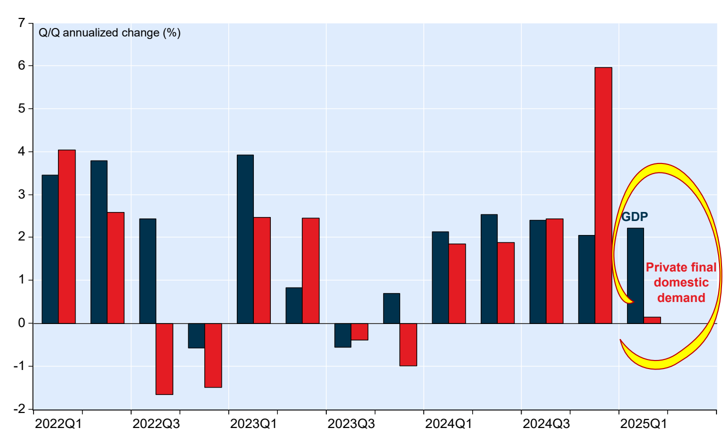
CAD: Loonie defies rate disadvantage
Canada-US exchange rate vs Canada-US spread on 2-year treasuries



NBC Economics and Strategy (data via Refinitiv)

We see limited scope for improvement in the two-year yield spread over the remainder of 2025, given Canada's challenging cyclical backdrop. While the Canadian economy grew at an annualized pace above 2% for a fifth consecutive quarter in Q1—beating both the 1.7% consensus and the Bank of Canada's April forecast of 1.8%—the underlying details of the national accounts raise questions about the durability of this momentum. Much of the growth stemmed from a temporary surge in exports, as U.S. buyers front-loaded purchases of Canadian goods ahead of potential tariff measures. Canadian firms also increased imports, albeit to a lesser extent, resulting in a strong net trade contribution and inventory accumulation. This context highlights why private domestic demand is a more reliable gauge of economic strength: it was essentially flat in Q1, rising just 0.2% annualized (see chart).

Canada: GDP growth masks weakness in private demand
Growth in gross domestic product and in private final domestic demand



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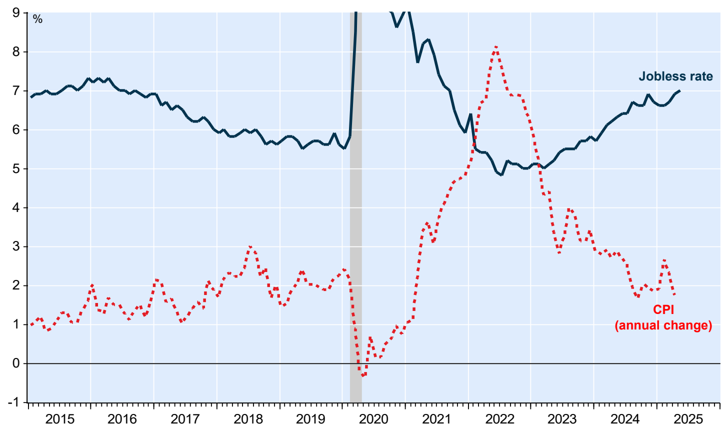
Weak domestic demand is typically a harbinger of labour market stress—and that is becoming increasingly evident. The unemployment rate jumped to 7% in May, a level not breached since 2015 outside the COVID recession. This points to significant excess supply in the economy, a dynamic we believe will continue to keep inflation in check (see chart).

Canada: Higher jobless rate set to contain inflation
Unemployment rate vs. CPI inflation



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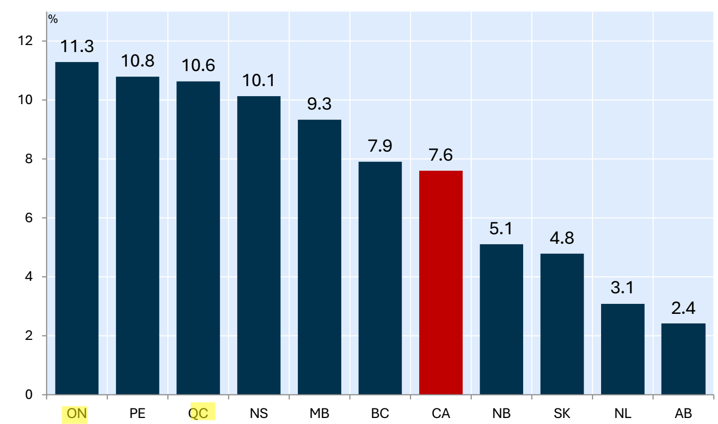
Unfortunately, the threat of U.S. tariffs continues to erode business confidence and hamper private-sector job creation. Washington's recent decision to raise import duties on Canadian aluminum and steel exports has pushed the effective tariff rate on Ontario and Quebec above 10% (see chart).

Canada: Tariff exposures vary by province
U.S. effective tariff rate on Canada and the provinces



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If sustained, this shock is likely to further dampen private final domestic demand in the second half of 2025. In light of this, our rate strategists anticipate that the Bank of Canada will cut its policy rate in July—despite current market pricing assigning only a 30% probability—and see the benchmark rate ending the year at 2%, down from 2.75% today (see **here**). Such a development would likely to lead to depreciation of the Canadian dollar against the U.S. dollar.

Yet, not all is bleak for the Canadian dollar, and we do not anticipate a sharp depreciation, as its trajectory will not be driven by interest rate differentials alone. For one, the renewed armed conflict between Israel and Iran has already led to a rebound in oil prices—a supportive factor for the loonie. For another, the upcoming G7 summit in Alberta presents a strategic opportunity for the Canadian Prime Minister to persuade the U.S. President that a swift resolution to bilateral trade tensions would be a win-win for both countries. Most importantly, we believe the Canadian dollar stands to benefit structurally from Ottawa's latest Throne Speech, which signals a transformative shift toward reindustrialization. The government's commitment to leveraging the resource sector, streamlining regulation, and overhauling military procurement marks a decisive break from the Trudeau-era playbook (see table).

Canada: Throne speech ends Trudeau era playbook
Trudeau 2021 vs. Carney 2025: A side-by-side comparison of throne speech policy orientations

Policy Orientation	Trudeau 2021 Throne Speech	Carney 2025 Throne Speech
Economic Vision	Inclusive, post-pandemic recovery focused on clean growth and social supports.	Transformative G7-leading economy with unified national market and energy dominance.
Regulatory Reform	No major change; emphasis on climate and equity lenses in regulation.	New Major Federal Project Office to cut approval times to 2 years; 'one project, one review'.
Energy Strategy	Cap oil & gas emissions; invest in clean tech and net-zero electricity.	Expand conventional & clean energy; aim to be global energy superpower.
Housing & Affordability	Childcare and rental support emphasized; Housing Accelerator Fund launched.	Double housing construction; GST cuts; Build Canada Homes agency.
Indigenous Participation	Focus on reconciliation; no major economic ownership initiatives.	Double Indigenous Loan Guarantee to $10B; enable ownership in major projects.
Trade Policy	Global trade openness and immigration-led growth emphasized.	Reduce U.S. dependence; build coalitions with like-minded democracies.
Fiscal Policy	Targeted support during pandemic; gradual spending restraint.	Cap spending growth under 2%; balance operating budget in 3 years.
Internal Market	No direct mention of internal trade or mobility barriers.	Remove federal internal trade barriers by Canada Day; $200B productivity gain targeted.
Innovation & Industry Policy	Climate innovation, clean tech manufacturing and zero-emission vehicles.	Massive industrial strategy to drive trades, science, and global innovation leadership.
Immigration Policy	Increase immigration; support family reunification; refugee resettlement leadership.	Cap temporary foreign workers and international students to <5% of population by 2027; restore trust and balance.

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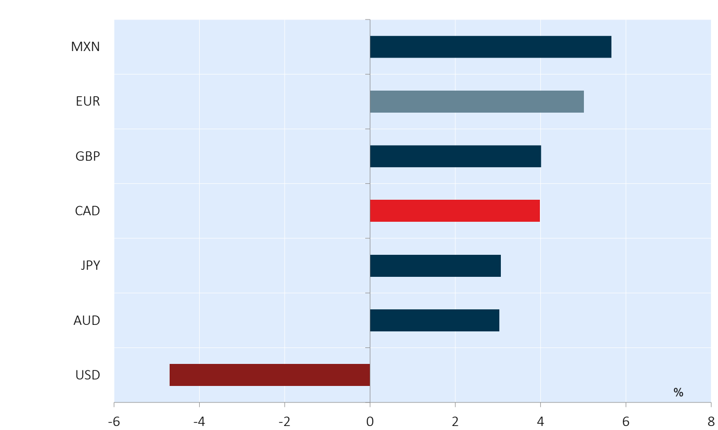
Prime Minister Carney's vision sends a clear signal: Canada is reopening for business and positioning itself to attract private capital. As the new policy direction takes hold, we expect USD/CAD to trend toward 1.34—following a temporary bout of weakness toward 1.38 as markets price in a more aggressive rate-cutting cycle from the Bank of Canada than currently anticipated.

EUR: Resilient, but Stretched

The euro has been trading at its highest levels in over three years throughout the past two months. Since "Liberation Day," heightened uncertainty has weighed on the U.S. dollar, while the euro has benefited from the relative stability and institutional resilience of the eurozone. The common currency's strength is also underpinned by expectations of a forthcoming fiscal impulse from the German government and robust export performance in the first quarter. That said, the euro appears somewhat stretched relative to its underlying fundamentals. Speculative positions have shifted markedly towards being net long, although the pace has begun to moderate. The European Central Bank (ECB) has maintained a dovish stance, delivering a series of rate cuts in response to well-controlled inflation and the potential for modest growth for the remainder of the year.

Since April 2nd, the euro has outperformed the U.S. dollar, appreciating by 5%, while the dollar has declined by 4.7%. Within our basket of currencies we track, the euro ranks as the second-best performer, trailing only the Mexican peso.

World: The dollar has been liberated (i.e.: depreciated)
Spot performance since Liberation Day (April 2nd)



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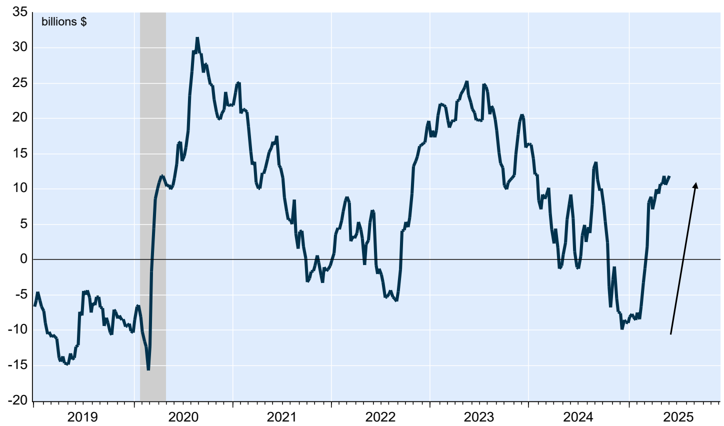
The reversal in speculative positioning since the start of the year has been significant, though that momentum now appears to be fading. The euro, and the broader political framework that supports it, have demonstrated a degree of stability that has likely attracted flows amid recent global volatility.

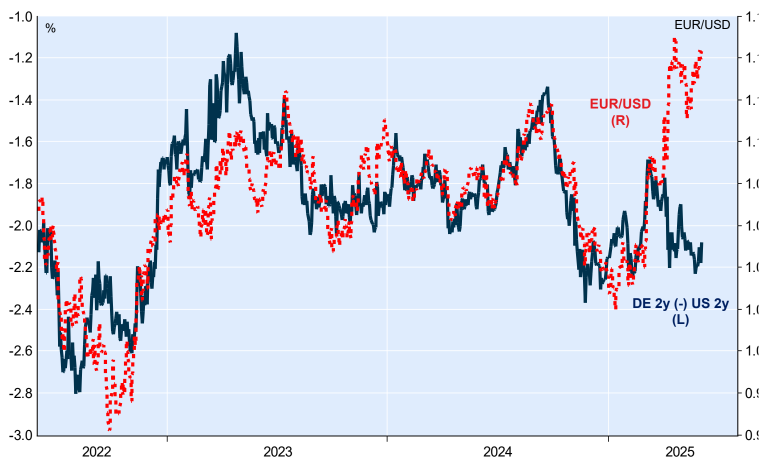
Euro: Speculators are long on the currency
Non-commercial net speculative positions



NBC Economics and Strategy (data via Bloomberg)

Nonetheless, the single currency is increasingly disconnected from key valuation anchors. It is currently trading six cents above its 200-day moving average and has diverged notably from two-year interest rate differentials, which would typically imply a weaker exchange rate.

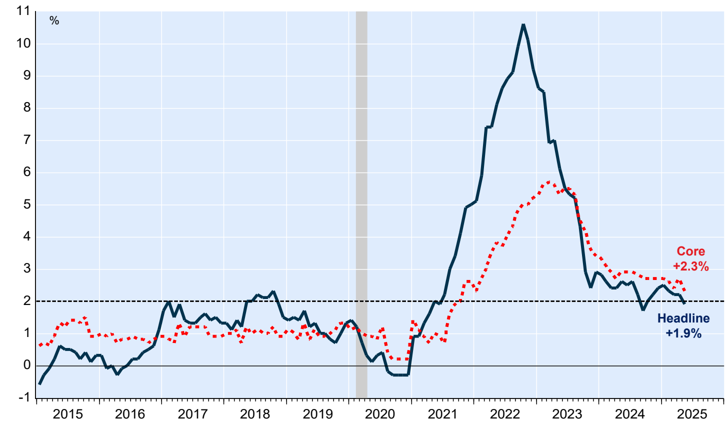
Euro: The currency has detached from fundamentals
2y spread (DE-US) and EUR/USD



NBC Economics and Strategy (data via Refinitiv)

The ECB has now delivered seven consecutive rate cuts as of the June meeting. The Governing Council appeared broadly satisfied with inflation dynamics, with headline inflation stabilizing near the 2% target and core inflation trending in the same direction. While the euro's appreciation may help contain import price pressures, it could also dampen external demand, particularly in the context of rising trade frictions.

Euro: Inflation is essentially on target
Headline and core inflation



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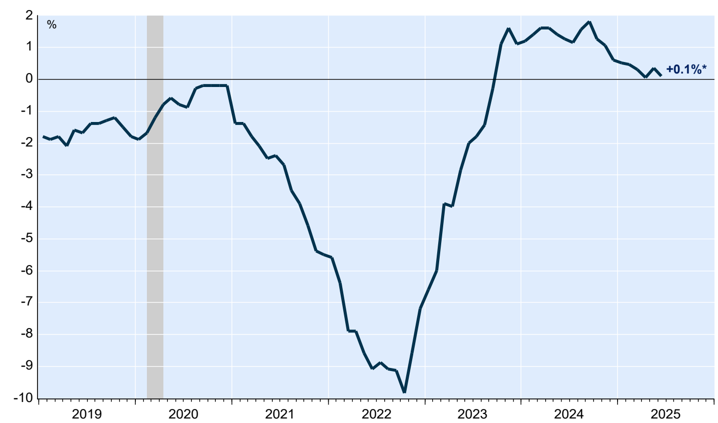
With the latest reduction in the deposit rate, real interest rates are now hovering around neutral.

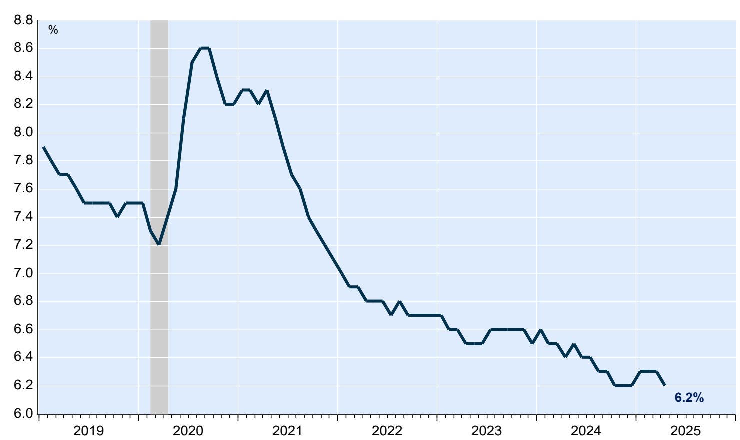
ECB: Not very restrictive following the last cut
Real interest rate (Deposit rate less headline inflation)



*Assumes inflation remains stable in June
NBC Economics and Strategy (data via Refinitiv)

This suggests the ECB may be approaching the end of its easing cycle, a view supported by recent comments as well as continued labor market resilience, with unemployment holding at historic lows.

Eurozone: Unemployment rate is at an all-time low
Eurozone unemployment rate (Last data: April)



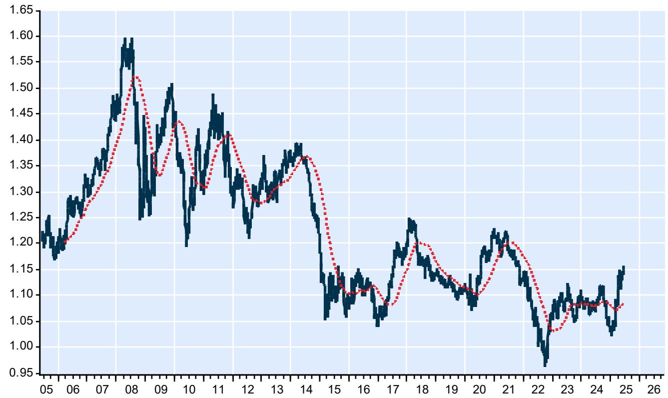
*NBC Economics and Strategy (data via Refinitiv)

However, risks remain. A key date looms with the expiration of the U.S.'s pause on EU tariff implementation (July 9th), and potential retaliatory measures by European authorities scheduled for July 14, should the U.S. proceed. These developments, alongside other macroeconomic headwinds, could weigh on sentiment in the second half of the year. Still, the likelihood of only two additional rate cuts could mean that 2025 will mark the end of divergence between ECB and Federal Reserve policy paths.

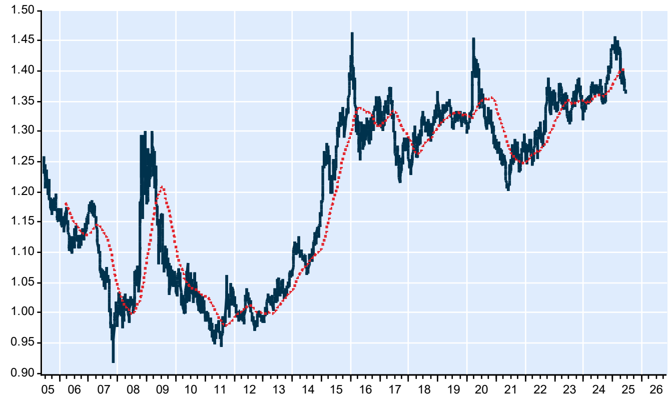
We maintain a cautious outlook on the euro at this juncture. The rally has been swift, and the disconnect from fundamentals warrants a vigilant stance. While upcoming U.S. policy announcements could influence the currency, there is a discernible shift toward diversification away from the dollar. As such, the euro may continue to perform well into the second half of the year, even if growth moderates from its strong first-quarter pace. With monetary policy no longer restrictive, resilience in activity remains a plausible scenario.

Appendix: Spot rates with their 200d MA

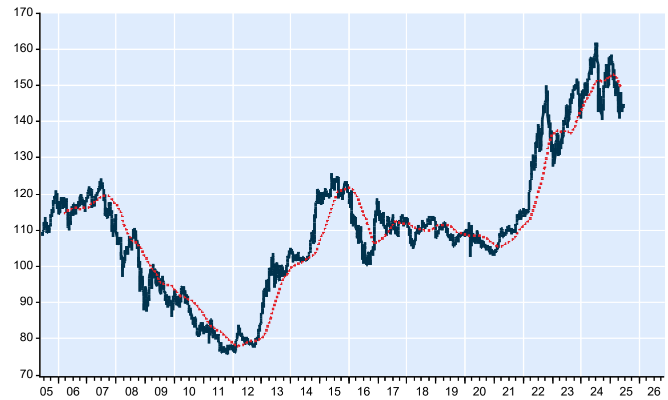
EUR / USD



USD / CAD



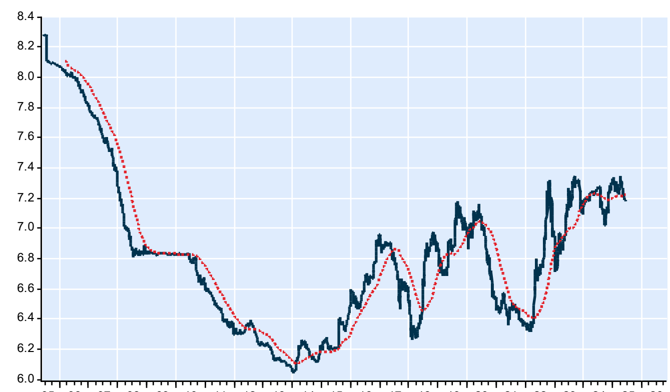
USD / JPY



AUD / USD

GBP / USD

USD / CNY



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