The effect of depreciation of Canadian dollars on Canadian trade ratio

Xida Ouyang

ABSTRACT

According to the J-curve theory, currency depreciation will worsen a country's current account balance in the short run and promote its external trade in the long run. Canadian dollars have been depreciating recently, which may improve Canadian trade ratio in the future.

Based on Marwah and Klein (1996), this paper studies the effect of a real depreciation of Canadian dollars against the currencies in Japan, the United Kingdom, the United States, Mexico and China, who are the top five trading partners with Canada in 2013. Using STATA and Matlab to conduct an empirical analysis on the quarterly data between the first quarter of 1999 and the first quarter of 2014, this paper reveals that the recent depreciation of Canadian dollars may have a positive effect on Canadian current account balance in the long run, which is consistent with the prediction of the J-curve theory.