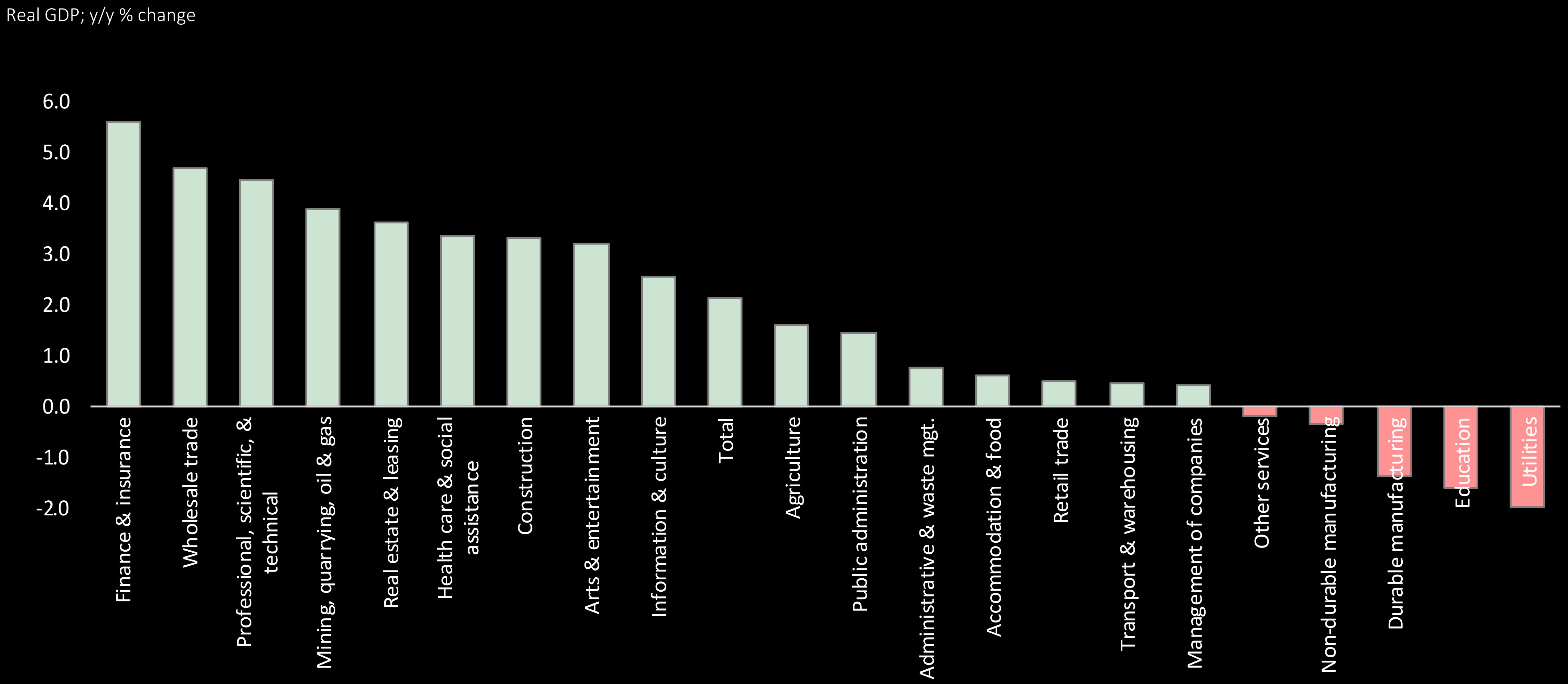
Canadian economic and financial forecast

May 2020 update

Industry leaderboard: Pre-pandemic sector performance

Manufacturing, transport, and utilities were already contracting prior to the economic lockdown



Note: Data as of January 2020.

Source: Statistics Canada. Calculations by Deloitte Economic Advisory.

Macro forecast summary

Base case

- After contracting by an annualized 10 percent in the first quarter of 2020, Canadian economic output is expected to plunge in the second quarter due to the lockdown was applied across all regions of the country and oil prices tumbled lower. Real gross domestic product is expected to contract by over 50 percent in annualized terms during the second quarter.
- However, as the curve of new COVID-19 cases is flattening across much of the country, provincial governments have begun announcing plans outlining the timeline for reopening their economies, with most aiming to begin in May. It should be stressed that the reopening will be staggered and economic activity will remain weak throughout the summer. We expect momentum to build over the course of the third and fourth quarters of 2020, with both projected to register double-digit growth. Despite the strong gains, which will last into next year, we do not expect the level of economic activity to reach its pre-COVID-19 level until early 2022.
- Pandemic containment efforts will be felt across the entire economy, but labour-intensive sectors will bear most of the brunt. Services spending, typically the most stable of the personal expenditure categories, is expected to decline by more than 60 percent (on a compound annual growth rate basis). Household purchases of goods will also slump, but remain supported by purchases of groceries, medications, and personal hygiene products. Purchases of other products will be largely limited to e-commerce.
- The enormous drop in crude oil prices, with the WTI benchmark falling from US$60 at the start of the year to around US$15 per barrel in late April, will halt capital expenditures and lead to a deep contraction in the battered energy sector. Investment in non residential structures will fall to levels unseen since the Great Recession of 2008/09. The glut in oil markets is unlikely to rebalance for some time, limiting any rebound in business investment even after the rest of the economy begins to recover. The recovery in non energy investment will be limited by uncertainty over future demand and sharply deteriorated business finances.
- The unprecedented monetary and fiscal stimulus can't stop the contraction, but should help the economy avoid a depression and lower the risk of deflation. As the recovery unfolds, the Bank of Canada is expected to wind down its liquidity enhancing measures, such as government and corporate debt purchases, but keep interest rates at their exceptionally low level. On the fiscal side, the stimulus announced so far has been dramatic, and there will be further policy announcements as governments at all levels look to stimulate growth during the recovery.
- Despite the unprecedented magnitude of this pandemic-caused contraction, we do not expect the monetary or fiscal stimulus measures will create an inflation problem over the medium term. However, fiscal support measures will result in significantly higher deficits and debt levels across all levels of government. Indeed, the increased leverage will be a major economic impediment in the post-COVID-19 world, as Canadian households, businesses and governments become much more indebted.

Macro forecast table

Base case

TABLE 1: CANADIAN ECONOMIC FORECAST	2019				2020				2021				2019	2020	2021
	Q1A	Q2A	Q3A	Q4A	Q1E	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Real GDP by expenditure															
Gross domestic product	1.0	3.4	1.1	0.3	-10.2	-51.5	19.3	36.7	13.2	8.6	5.8	4.4	1.6	-10.8	9.3
Personal expenditure	2.4	0.4	2.0	1.9	-10.1	-50.7	12.3	38.5	9.6	7.6	5.6	5.1	1.6	-10.9	7.9
• Durables	4.8	-2.6	1.4	-0.2	-12.5	-52.2	15.3	56.1	13.7	9.7	6.1	4.0	0.6	-11.6	11.8
• Services	2.4	1.0	2.3	3.4	-14.3	-62.1	11.4	56.7	11.4	9.1	7.2	7.0	2.1	-15.2	9.3
Residential structures	-3.1	6.4	13.0	1.1	-4.4	-48.7	-12.3	78.3	33.1	20.8	11.6	4.8	-0.6	-8.8	18.7
Nonresidential fixed investment	5.5	-1.4	8.3	-3.1	-8.1	-51.5	-11.1	31.2	21.4	13.3	7.6	4.0	-0.7	-13.8	7.4
• Nonresidential structures	4.4	4.3	11.2	-1.7	-11.8	-57.6	-13.2	-3.3	8.9	7.1	4.5	2.9	0.9	-17.6	-4.1
• Machinery & equipment	42.7	-23.2	-2.6	-13.5	-8.3	-43.1	-8.5	16.7	21.4	8.4	3.7	3.5	-1.4	-16.0	5.2
Government	2.8	0.7	2.1	0.5	2.3	0.9	2.6	3.0	3.0	2.6	2.2	1.9	1.6	1.7	2.6
Exports	-4.0	10.6	-0.6	-5.1	-8.7	-56.6	28.7	57.2	11.3	6.4	4.1	3.3	1.2	-11.3	11.2
Imports	8.3	-4.1	-0.2	-2.5	-5.6	-42.1	21.2	37.9	4.4	2.2	2.0	2.2	0.3	-7.6	7.0
Prices															
Consumer price index (y/y % change)	1.6	2.1	1.9	2.1	1.8	0.7	1.0	1.3	1.5	2.4	2.1	2.1	2.0	1.3	2.0
GDP deflator	4.5	4.5	0.4	4.1	0.6	-2.8	2.4	3.6	2.3	2.0	1.9	1.8	1.9	1.2	2.1
Labour market															
Employment (q/q change in thousands)	3.0	2.6	1.1	0.5	-1.5	-4.1	2.2	3.2	0.7	0.8	0.6	0.6	2.1	-0.3	1.0
Unemployment rate (%)	5.8	5.6	5.6	5.7	6.3	8.4	7.8	7.2	6.8	6.7	6.6	6.5	5.7	7.4	6.7

Notes: Unless otherwise noted, all figures are in compound annual growth rate form.

Source: Statistics Canada. Forecast by Deloitte Economic Advisory, as of April 25, 2020.

Financial forecast table

Base case

TABLE 2: FINANCIAL FORECAST	2019				2020				2021				2019A	2020	2021
	Q1A	Q2A	Q3A	Q4A	Q1A	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Interest rates															
Overnight rate target	1.75	1.75	1.75	1.75	1.48	0.25	0.25	0.25	0.25	0.25	0.25	0.50	1.75	0.25	0.50
3 month GoC T bill yield	1.67	1.66	1.65	1.66	0.21	0.20	0.20	0.20	0.25	0.30	0.40	0.65	1.66	0.20	0.65
2 year GoC bond yield	1.55	1.47	1.58	1.69	0.42	0.35	0.45	0.50	0.55	0.65	0.75	0.85	1.69	0.50	0.85
5 year GoC bond yield	1.52	1.39	1.40	1.68	0.60	0.45	0.50	0.60	0.70	0.80	0.90	1.00	1.68	0.60	1.00
10 year GoC bond yield	1.62	1.46	1.37	1.70	0.71	0.55	0.65	0.75	0.85	1.00	1.10	1.25	1.70	0.75	1.25
Yield curve gradients															
3 month vs. 10 year (percentage points)	0.05	0.20	0.28	0.04	0.50	0.30	0.40	0.55	0.60	0.70	0.70	0.60	0.04	0.55	0.60
2 year vs. 10 year (percentage points)	0.07	0.01	0.21	0.01	0.29	0.20	0.20	0.25	0.30	0.35	0.35	0.40	0.01	0.25	0.40
Foreign exchange															
USD/CAD	1.34	1.31	1.32	1.30	1.42	1.39	1.39	1.38	1.37	1.36	1.35	1.35	1.30	1.38	1.35
US cents	74.8	76.4	75.5	77.0	70.5	71.8	72.0	72.5	73.0	73.5	74.1	74.1	77.0	72.5	74.1

Note: Unless otherwise noted, all figures are in percent form and are quoted as end of period.

Sources: Statistics Canada, Bank of Canada. Forecast by Deloitte Economic Advisory, as of April 25, 2020.

Provincial forecast summary

Base case

- No region will be spared by the recession: the downturn is apparent from coast to coast, with all provinces and territories implementing pandemic containment efforts. But, the depth of the downturn will vary across the country depending on the timing and scope of regional containment efforts as well as the industrial composition.
- Energy-producing regions will be the hardest hit, with the three oil-rich provinces experiencing their second recession in just five years. The Newfoundland and Labrador economy will contract by 14.4 percent this year, posting its fifth annual decline in 10 years. Alberta (-14.1 percent) and Saskatchewan (-12.8 percent) will also experience very deep downturns, with their resource economies slated for a protracted recovery, as capex is halted and energy firms lay-off workers.
- The Maritime provinces will also sustain more severe declines than the nation as a whole. Dependence on tourism and, to a lesser extent, resources, will leave Prince Edward Island (-12 percent), Nova Scotia (-11.8 percent) and New Brunswick (-11.2 percent) vulnerable to the social distancing measures and travel restrictions that prohibit tourism.
- Central Canada will fare slightly better than the nation despite being the beleaguered manufacturing heartland since economic activity in Ontario (-10.1 percent) and Quebec (-10.3 percent) will remain supported by their high-value-added services industries where working-from-home is feasible – particularly the professional, financial, and technical and scientific services. These sectors are smaller in Manitoba (-11.1 percent), which will fare slightly worse.
- British Columbia (-9.3 percent) will outperform the country, posting the only single-digit decline. The slump in its resource and tourism industries is buoyed by ongoing infrastructure projects, preponderance of high-skilled services, healthy provincial finances, and exposure to China.

Provincial forecast table

Base case

TABLE 3: PROVINCIAL GDP FORECAST	2019E	2020	2021
Canada	**1.6**	**-10.8**	**9.3**
British Columbia	1.7	-9.3	10.1
Alberta	0.4	-14.1	8.3
Saskatchewan	0.6	-12.3	9.6
Manitoba	1.2	-11.1	10.0
Ontario	1.6	-10.1	9.3
Quebec	2.8	-10.3	9.1
New Brunswick	0.8	-11.2	9.8
Nova Scotia	1.2	-11.8	10.3
Prince Edward Island	2.7	-12.0	10.8
Newfoundland and Labrador	2.0	-14.4	7.6

Note: All figures are in compound annual growth rate form and market prices.

Source: Statistics Canada. Forecast by Deloitte Economic Advisory, as of April 25, 2020.

Industry forecast summary

Base case

- The current downturn is unprecedented, both in its magnitude and its impact across industries.
- Many of the hardest hit industries during the current downturn are highly cyclical. But, the regulated shutdown of non-essential services has resulted in sharp declines in industries that are not typically very cyclical. Indeed, one of the defining characteristics of this downturn is the weakness in many service industries.
- The highly-cyclical mining, oil, and gas industry, already struggling prior to COVID-19, will see the most acute contraction, with output declining more than one-quarter this year. The energy sector is unique amongst industries in that the impacts of pandemic containment efforts are less supply-side oriented (labour shortage due to social distancing) and more related to a collapse in domestic and foreign demand, which has created a dramatic decline in crude oil prices. With inventories building and storage capacity becoming a challenge, this sector will struggle with a supply overhang even as the global economy improves.
- Manufacturing, also a highly-cyclical sector, is expected to contract by about 16 percent this year as global demand, already soft prior to COVID-19, weakens further as a result of the pandemic eradication efforts. Supply-side issues, such as labour and parts shortages, have also aggravated production in global supply-chain integrated durable manufacturing (-20.2 percent) such as electronics, machinery, and transport equipment; Canadian automotive production fell by one-third in March. Nondurable manufacturing (-11.5 percent) will fare better, supported by resilient demand for food & beverage, chemicals (soap, disinfectant, etc.), and medical supplies (masks, gloves, etc.)
- Construction (-14.2 percent) is another hard-hit cyclical sector. The decline will be tilted toward the residential side as construction sites close and renovation activity is halted. Housing starts remained robust in March, but permitting activity portends a sharp decline in homebuilding.
- Services sectors suffering the largest declines include tourism, hospitality and food services. While some industries that are posting growth—such as critical health care, groceries and pharmacies—the industry aggregates that include these narrowly defined segments are still showing a decline in output. For instance, grocery store sales account for one-sixth of sales in the broad retail category, where many retailers are experiencing shutdowns. While demand for essential health care has increased, the opposite is true for non-essential health care services, as people stay away from clinics and hospitals due to the risks.

Industry forecast table

Base case

TABLE 4: INDUSTRY GDP FORECAST	2019A	2020	2021
Total	**2.3**	**-11.2**	**9.7**
Agriculture	0.4	-3.5	4.1
Mining, oil & gas	-5.0	-26.4	8.9
Utilities	0.8	-7.2	7.8
Construction	-0.4	-14.2	12.5
• Residential	-2.0	-18.2	15.1
Manufacturing	-0.1	-16.1	12.5
• Durables	0.2	-20.2	13.4
• Nondurables	-0.4	-11.5	9.3
Wholesale trade	2.6	-12.3	10.8
Retail trade	1.0	-15.0	11.9
Transportation & warehousing	1.4	-9.7	12.2
Information & culture	2.6	-8.3	9.7
Finance & insurance	2.9	-7.1	11.4
Real estate & leasing	2.7	-2.2	3.4
Professional, scientific, & technical	4.5	-7.6	6.3
Management of companies	-1.0	-8.8	4.9
Administrative & waste management	1.4	-15.8	11.3
Education	2.1	-11.2	13.8
Health care & social assistance	3.2	-2.1	4.5
Arts, entertainment & recreation	2.6	-20.4	18.7
Accommodation & food services	2.4	-14.3	14.1
Other services	1.5	-9.7	8.5
Public administration	2.2	-1.5	2.6

Note: All figures are in compound annual growth rate form and basic prices.

Source: Statistics Canada. Forecast by Deloitte Economic Advisory, as of April 25, 2020.