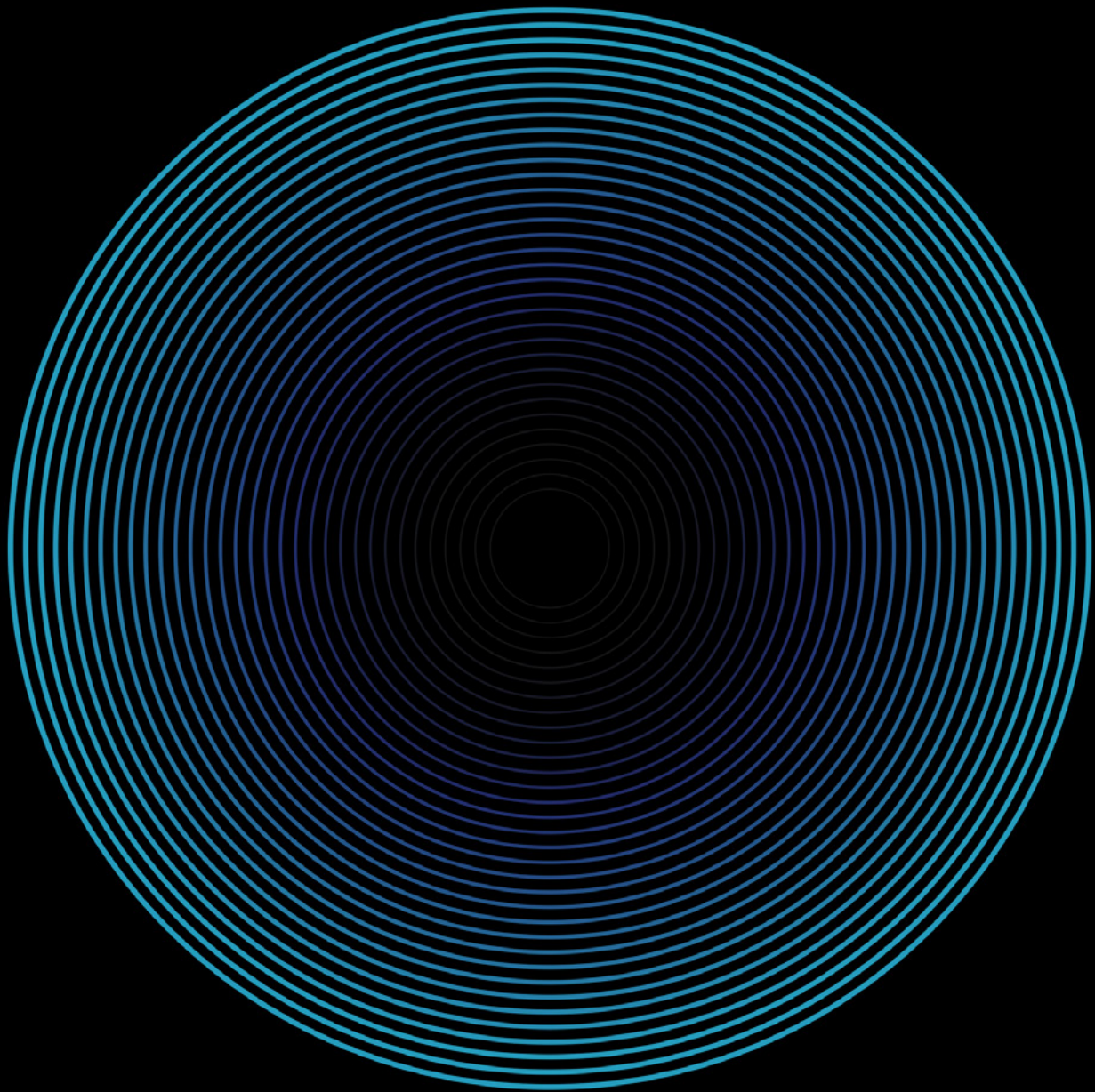
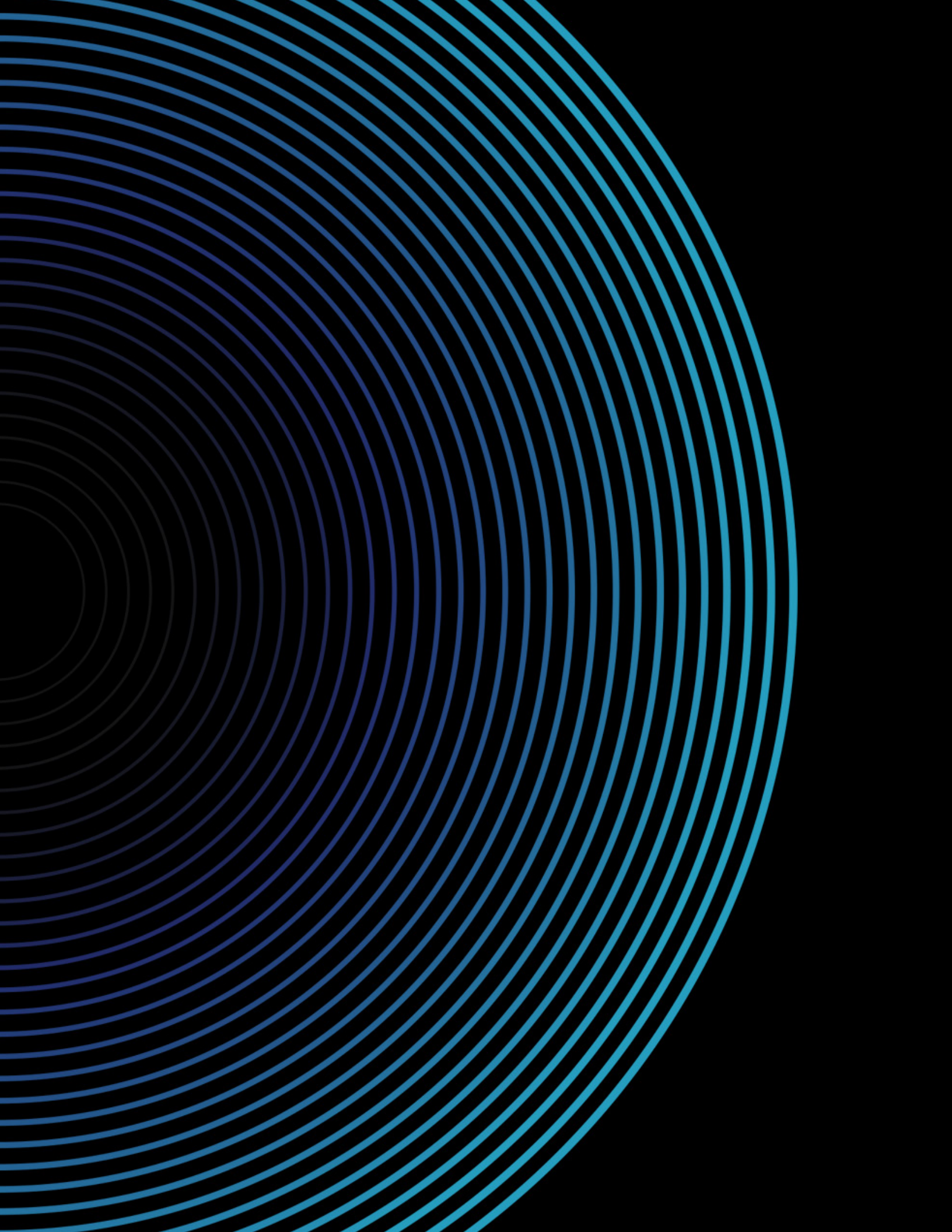


Deloitte.



Dark clouds bring rougher seas
Economic outlook: January 2019



Introduction

2019 is expected to be a year of economic transition, both internationally and in Canada. A key theme from the inaugural Deloitte economic forecast in October was that the North American economy is in the late stages of a business cycle. Since the forecast's publication, economic and financial developments have only reinforced that view.

Global economic growth appears to have peaked in 2018, and the base case forecast is for growth to moderate in 2019 and 2020. The US economy will continue to outperform other advanced economies in terms of the absolute pace of expansion, but it will experience the greatest degree of slowdown among them over the next two years. Canadian economic growth will gear down from close to 2 percent in 2018 toward 1.6 percent in 2019.

One key development since our last forecast has been an oil price correction. Although crude oil prices should recover from their recent lows, a sustained lower level of prices and production will have a negative impact on Canadian economic growth in 2019.

The **economic cycle** risks increase in 2020, as fiscal drag is expected to weigh significantly on US economic growth. This would have a negative impact on integrated North American supply chains. Consequently, Canadian economic growth is projected to drop to 1.3 percent in 2020.

Storm clouds are gathering on the horizon in the form of key downside risks to the outlook. Further US protectionism and international retaliation could weaken global growth and lower commodity prices. A possible disorderly UK exit from the European Union could have detrimental economic and financial consequences. Financial market volatility and equity market weakness may persist due to a further rebalancing of monetary policy by some key central banks, particularly the US Federal Reserve. And, markets may become more worried about looming fiscal challenges in many emerging market and advanced economies, including in the United States.

While the downside risks have risen, we advise Canadian businesses to not overreact. The most likely scenario is that 2019 will be a year of more modest economic growth. Although the Bank of Canada has suggested that it will ultimately need to raise the overnight rate to between 2.50 and 3.50 percent, its estimate of neutral monetary policy, we favour the bottom of that range due to a structurally slower trend of economic growth that reflects the impact of demographics from an aging population. And, given the risks, we have only incorporated a 50 basis point increase in the overnight rate to 2.25 percent in 2019 and no change in 2020.

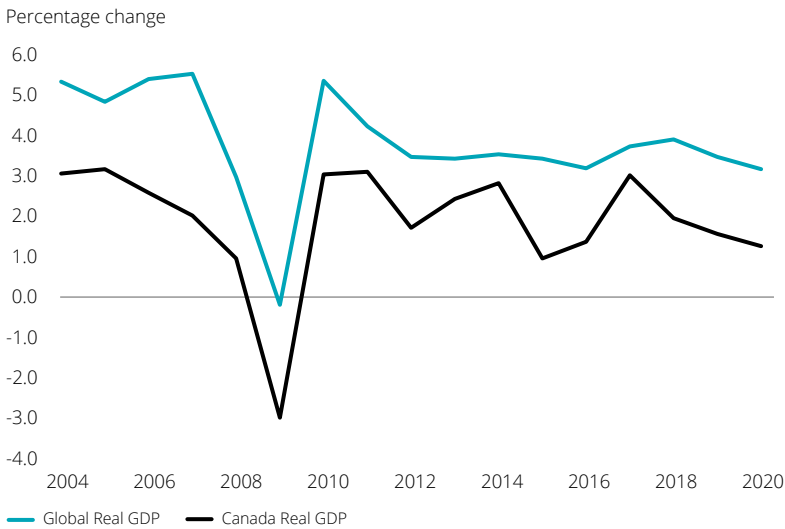
Bank of Canada Governor Stephen Poloz has frequently described the conduct of monetary policy as an exercise in risk management. In other words, if the Canadian economy slows materially,

interest rates will not rise as much as in the base case forecast. The Canadian dollar will also act as a shock absorber for the economy. Indeed, as economic prospects have diminished, the Canadian dollar has weakened. The exchange rate is expected to fluctuate between 73 and 76 US cents over the forecast.

Financial market sentiment was negative in late 2018, with markets fixated on the risks of slowing global growth and a possible inversion of the US yield curve, which is a traditional recession signal. It's likely that financial market sentiment became too negative, so markets and commodity prices are likely to reverse some of their recent losses. However, it's important to be mindful that we're in the late stages of a business cycle and a greater economic slowdown appears to be in the cards in late 2019 and 2020. Specifically, US economic growth is projected to drop towards a 1.0- to-1.5 percent pace next year. Weaker US demand will dampen economic growth in Canada and feed through trade and financial linkages around the globe.

Despite the downside risks, organizations still need to be building for the future—making key investments, developing their talent, and growing their businesses. A riskier economic environment should not be allowed to paralyze or delay decision-making. At this stage, businesses should be bracing for slower economic growth but also considering how they will cope with the next business cycle when it finally occurs.

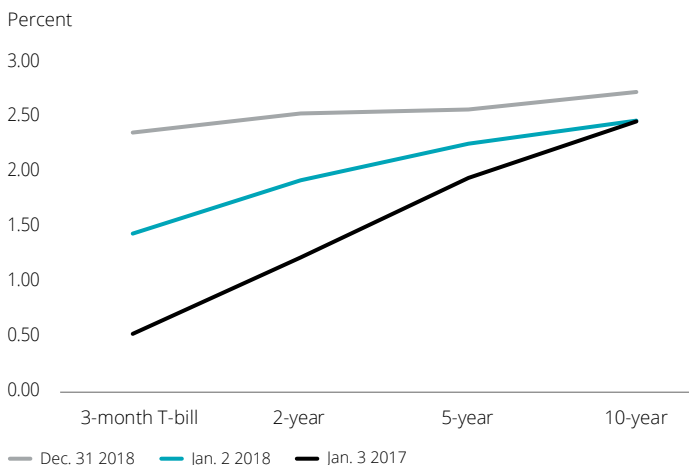
Global and Canadian economic growth outlook Real GDP



Sources: Haver Analytics, IMF, Statistics Canada. Forecast by Deloitte.

Despite the downside risks, organizations still need to be building for the future—making key investments, developing their talent, and growing their businesses.

US government yield curve



Sources: Haver Analytics, Federal Reserve Board.



International outlook

Global growth starting to cool

The global economy had good momentum heading into 2018, and the pace of growth remains healthy despite the many signs that the pace of expansion is moderating. This is due to an important distinction between the trend and the level. Yes, the pace of world economic expansion is cooling, but much of the downshifting in advanced economies is a moderation toward more sustainable rates of growth. In emerging markets, the prospects for slower growth reflect the fallout from the US-China trade dispute that is dampening economic growth prospects in both of these nations and adversely affecting other countries through their international supply chains. Emerging economies are also being affected by financial strains created by negativity in global markets about the economic outlook.

Purchasing manager indexes for manufacturing in many advanced and developing countries have increasingly signaled weaker economic growth ahead. Some of this will be related to the imposition of US tariffs and retaliation by other countries, but it also reflects lower-demand growth in many advanced economies and weaker growth in emerging markets. To maintain the 2018 pace of growth, stronger productivity supported by robust business investment was required in the advanced world. This didn't happen. Protectionism, worries about BREXIT, financial market strains created by a strong US dollar, and the rebalancing of US monetary policy are among the factors that have tempered the willingness of organizations to make large capital outlays.

Moreover, the economic tracking for growth in many countries has diminished. Japan posted a small contraction in the third quarter of 2018, and its pace of expansion in 2019 should come in at a little under 1 percent. Economic growth in the Eurozone has slowed

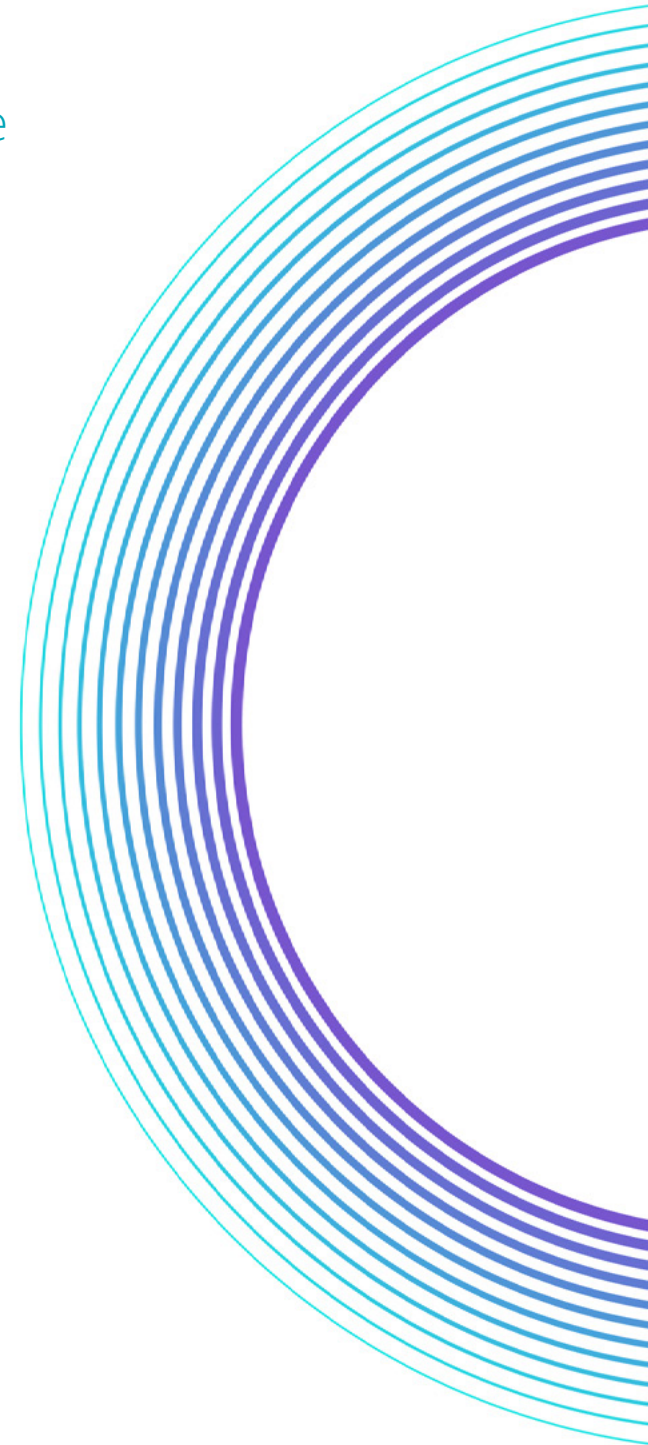
steadily over the course of 2018. The German economy posted modest 1.7 percent annualized growth in the third quarter, while the Italian economy recorded a 1.5 percent annualized contraction. Italy is likely to experience a technical recession when the economy contracts again in the fourth quarter of 2018. France has outperformed—its economy expanded by more than 3 percent annualized in the third quarter—but it's also expected to slow in 2019, to below 2 percent. The UK economy delivered a decent performance in 2018 but the outlook is clouded by risks related to the implementation of BREXIT in early 2019.

The emerging market economies are also in the process of losing some momentum. China is managing a difficult balancing act: policymakers are deploying targeted stimulus in response to a slowing economy while also trying to avoid significant credit expansion that could fuel domestic imbalances. So far, this approach has been working, and the rate of economic growth came in at 6.5 percent year-over-year in the third quarter of 2018. However, the United States-China trade dispute is likely to continue. There's a high probability the Trump Administration will implement further tariffs on Chinese exports to the United States. Meanwhile, the Chinese government is likely to maintain its efforts to limit credit-fueled growth in an attempt to deleverage the economy. As a result, we expect real GDP growth to slow to around 5.6 percent in 2019 and slip to 5.3 percent in 2020.

China's economic slowdown will feed through its international supply chains, weakening growth in countries with strong export exposure to its market. The further moderation of China's growth will also affect demand for raw materials, acting as a headwind on commodity prices—although, much of this development is likely already priced into commodity valuations.

We remain concerned about the second half of 2019 and 2020 due to slower US growth and its knock-on effects to the world economy.

Negative sentiment over the economic outlook has also been adversely affecting capital flows to some emerging market economies, weakening growth prospects. Financial markets are worried about the impact of the US Federal Reserve rate increases, which have been creating global financial strains through higher global interest rates and a strong US dollar, as well as a possible escalation of the United States-China trade dispute. In late 2018, financial market sentiment appeared to be excessively negative. The outlook for 2019 is for a moderation of global economic growth. However, we remain concerned about the second half of 2019 and 2020 due to slower US growth and its knock-on effects to the world economy.





Details of the US outlook

The US boom will end

The US economy was firing on all cylinders in 2018, with real GDP growth tracking a gain of close to 3 percent. In 2019, the pace of US expansion will likely continue to exceed that in other major advanced economies, but this will mask a more substantial deceleration in the pace of growth in the United States. Whereas fiscal policy has been providing a meaningful lift to real GDP this year, the fiscal impetus will have faded by the end of 2019.

The impact of US tariffs will also contribute to slower economic growth. While protectionist measures may defend jobs in select sectors that benefit from less international competition, the broader economy will suffer from higher prices for tariff-affected imports and retaliatory tariffs imposed on US exports. Moreover, the lack of slack in the US economy, including an unemployment rate at a five-decade low, sets the stage for the Federal Reserve to continue tightening monetary policy. The Fed funds rate is expected to climb by 50 basis points to 3 percent by the end of 2019. This will take monetary policy to a neutral stance.

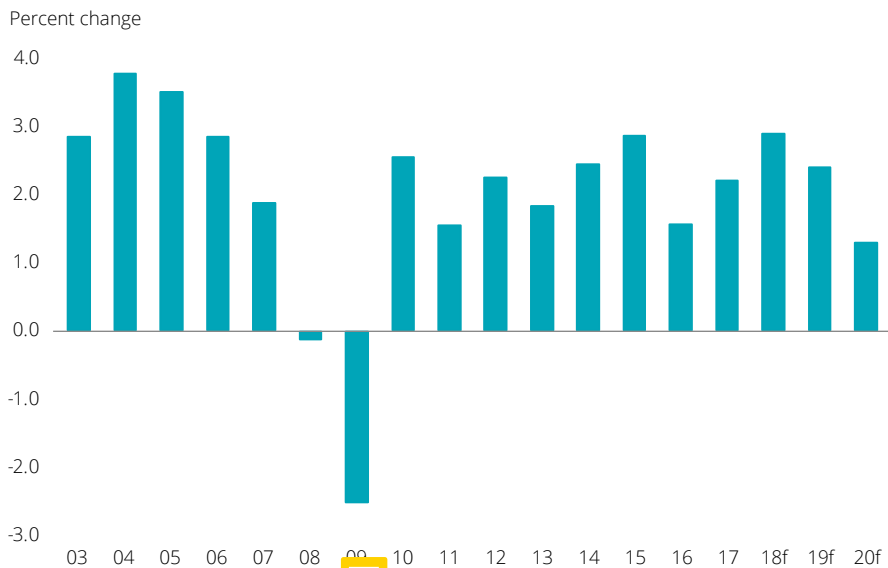
With this backdrop, US economic growth is projected to slow from 2.9 percent in 2018 to 2.4 percent in 2019, which will mask a deceleration to below a 2 percent annualized pace by the fourth quarter of 2019.

Moreover, economic growth could drop to between 1.0 and 1.5 percent in 2020.

A key question is how US President Donald Trump will respond to the slowdown in economic growth as the 2020 presidential election nears. Given that the two houses of Congress are now divided in terms of party control following the 2018 mid-term elections, it's hard to imagine reaching an agreement to new fiscal measures that will shore up growth. Indeed, the US government will need to raise the debt ceiling in March and pass appropriation bills for 2020, which creates fiscal risks in the near-term before tackling large new fiscal stimulus options.

Further fiscal initiatives would, in addition, raise the country's already considerable and rapidly rising fiscal deficit and debt, a looming long-term challenge that the United States will eventually have to face. As fiscal policy shifts from stimulus to drag on the economy, a major risk is that President Trump may announce new protectionist measures as a show of strength before the 2020 election. Such an escalation of the tariff war would be a negative development for both the US and global economy.

US economic growth
Real GDP



Sources: Haver Analytics, Bureau of Economic Analysis. Forecast by Deloitte.



Details of the Canadian outlook

A crude shock

At the time of our October forecast report, West Texas Intermediate (WTI) crude oil was priced at US\$76 a barrel. Global oil inventories were broadly in balance, but Alberta was receiving a discount of around US\$17 on its Western Canada Select (WCS) crude oil.

Since then, the financial market sentiment soured. Equities corrected and WTI crude oil prices plunged, dropping towards US\$45 per barrel, reflecting fears of slowing global economic growth that could reduce oil demand and create an inventory buildup. There was also a sense that oil sanctions were not lowering the supply from Iran by as much as expected. The drop in WTI was bad enough but the price for WCS fell by even more, widening the spread between the two greatly. At one point during November, Alberta was receiving less than US\$14 a barrel for oil priced in WCS.

The persistent gap in the price between WTI and WCS is partly due to the fact Alberta has only one customer for its crude: the United States. Furthermore, the shale oil revolution in the US led to a dramatic increase in oil production in the country, weakening demand for Alberta oil exports and therefore the price it receives. Another factor contributing to the price gap is Canada's inability to get pipelines built, which constrains Alberta's ability to move its crude oil and therefore leads to excess supply. Meanwhile, the province can't tap rising overseas demand because it's landlocked.

These factors have been weighing on WCS prices for years. But the spread between WCS and WTI prices was worsened by negative financial market sentiment about slower global growth prospects and temporary refinery shutdowns.

The oil price correction, similar to the equity correction, is likely overblown. Global economic growth may have peaked in 2018 but it's still likely to be healthy in 2019. Moreover, OPEC announced a production cut in December, and further production reductions are likely if prices don't recover. Consequently, WTI is forecasted to average US\$58 per barrel in 2019. The following year, weaker global demand growth is expected to be offset by supply

reductions to limit the impact on prices. While WTI crude oil prices are lower than in our last forecast, the Alberta response to the decline in prices is equally key for the province's economic outlook.

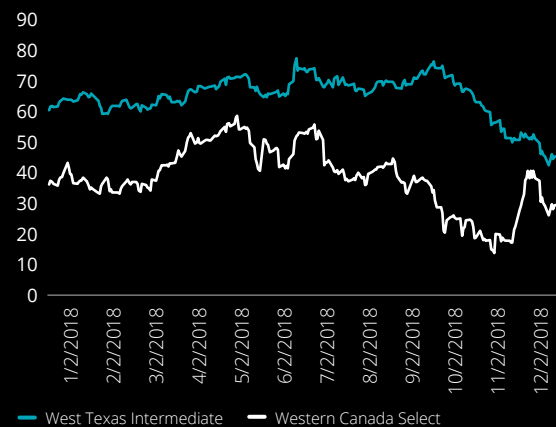
Faced with no good options, the Alberta government responded in a non-traditional way by announcing on December 2 that it would be requiring a curtailment of crude oil production. The objective is to reduce production by 9 percent (325k barrels per day relative to peak production), with the reduced supply intended to bolster local oil prices. The curtailment will start in January 2019 but ease over time.

The market reaction at the time of writing has been significant, with the WTI-WCS spread narrowing significantly. This will improve the price received by many Alberta producers, and may limit the downside to investment activity and employment in the oil patch. However, the production reduction will lower the province's real GDP, since it measures the volume of goods and services being produced. The result will reduce economic growth by between half to one full percentage point.

This impact on Alberta will be felt in overall Canadian real GDP, lowering growth by 0.2 percentage points.

North American benchmark crude oil prices

US dollars per barrel



Sources: Haver Analytics, Bloomberg.

Canada's economic moderation

The Canadian economy shifted down a gear in the third quarter, but the pace of expansion was still healthy and above the country's long-term sustainable rate. Real GDP growth dropped from 2.9 percent annualized in the second quarter to 2.0 percent annualized in the third quarter. The result was exactly in line with our projection in the October edition of the [Economic outlook](#). That said, the details of the latest national accounts reveal weaker results than the [headline](#) of solid economic growth suggested.

Consumers and real estate are contributing less

A key theme from our last forecast was that heavily indebted consumers with little pent-up demand for big-ticket purchases could not be the engine of growth going forward. Nor could real estate add as much to the economic expansion. Both of these trends were evident in the recent data. Household expenditure growth fell to a modest 1.2 percent in the third quarter. Auto sales were a particular source of weakness, but the moderation in growth of outlays was broadly felt across most other categories of consumer spending as well.

Consumer spending growth should be a bit stronger in the next couple of quarters, but we expect expenditure to average 1.5 percent growth in 2019 and 1.4 percent in 2020. This will reflect more modest employment growth, compensation gains in line with or slightly above the rate of inflation, and relatively flat real estate markets that will dampen big-ticket household purchases like furniture and appliances.

Resale housing market activity was dampened significantly in 2018 by the implementation of new mortgage stress tests at the start of the year. These stress tests require that buyers qualify for mortgages as if interest rates were two percentage points higher than the transaction rate. Some buyers were pushed out of the market, particularly in the least affordable cities. The far greater impact was reducing the size of mortgage being qualified, which lowered the price point for

transactions and reduced the average price of homes being sold. Home sales declined in most markets, but so too did listings.

As a result, the sales-to-listing ratios declined in Canada's major markets and this limited the negative impact on resale home prices. The fallout of the mortgage income stress test has waned over time, but resale activity has also felt a headwind from rising interest rates. The weaker real estate demand has also been felt in new home construction. Looking ahead, national average home sales and prices are expected to be relatively flat as will the pace of new home construction, reflecting modestly higher borrowing costs, limited household willingness to take on significantly greater debt, and weaker economic conditions.

Business investment disappointed in third quarter, but should firm up

Due to the high indebtedness of Canadian households, there has been long-standing hope for a transition in the drivers of economic growth from consumer spending toward business investment and exports. There were signs that this was taking place in late 2017 and early 2018. Regrettably, the trend stalled, with the pace of business investment slowing the second quarter of 2018 and then declining in the latest data. Investment in non-residential structures fell by an annualized 5.2 percent while investment in machinery and equipment fell by an annualized 9.8 percent in the third quarter.

The outturn was disappointing, but there are reasons to believe the contraction is temporary.

First, the large drop in machinery and equipment in the third quarter was partially due to a 51-percent plunge in aircraft and transportation equipment, a volatile component that is unlikely to have a repeat performance. It may have been that the aircraft purchases were simply delayed.

Second, the latest data don't show the business response to the new United States-Mexico-Canada Agreement (USMCA) free trade deal. Although it still has to be ratified, implying that political risk is still present, it's highly probable that it will be implemented. With the uncertainty on trade policy lifted, one would expect some delayed investment to occur in the coming quarters.

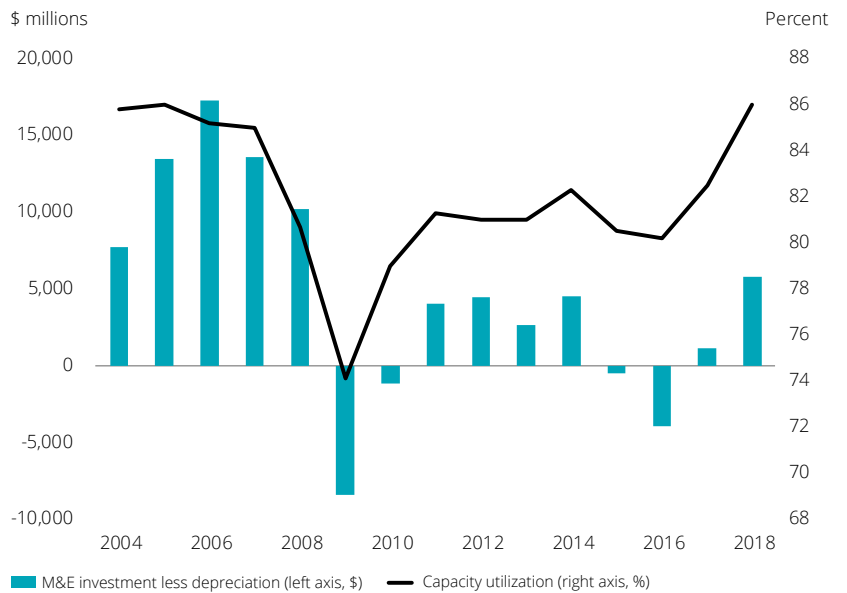
Third, businesses need to invest to meet future demand. Business investment in recent years has been weak, particularly if new outlay in machinery and equipment is assessed after removing depreciation in Canada's capital stock. And, firms are operating at high levels of capacity.

Fourth, the Government of Canada announced in its Fall 2018 economic and fiscal update that it was allowing firms to write off investments at an accelerated rate. This lowered the marginal effective tax rate on investment, making new investments less expensive.

Accordingly, we expect stronger business investment to start making a greater contribution to economic growth. However, the rate of investment growth will be constrained by meagre investment in the energy patch and a cyclical slowdown in the North American economy in 2020.

Business investment and capacity utilization

Business investment in machinery and equipment less depreciation



Sources: Haver Analytics, Statistics Canada.

Exports supported by foreign demand, weak Canadian dollar

Net international trade contributed to Canadian economic growth in the third quarter, but it did so in a disappointing way. Net trade is the difference between exports and imports, and imports plunged almost 8 percent annualized in the quarter. This reflected the weakness in consumer spending but, more importantly, the decline in business investment. Exports only rose by a modest 0.9 percent annualized in the same timeframe.

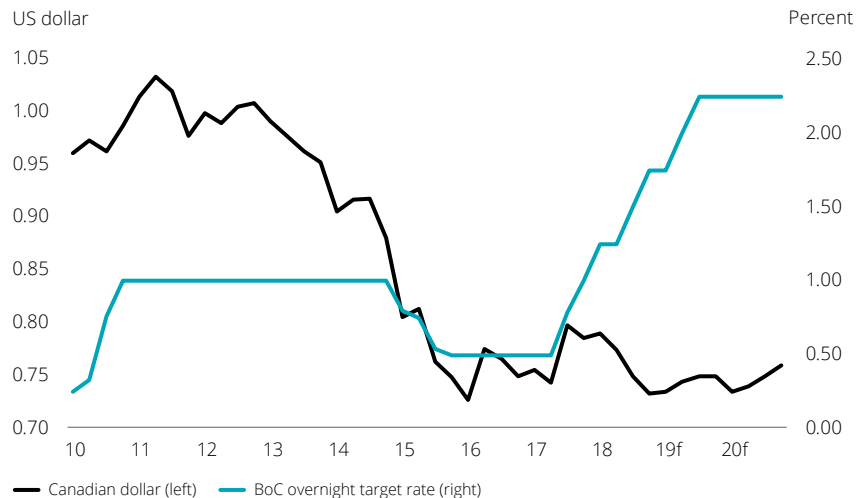
Trade performance should improve in the fourth quarter of 2018 and in 2019. Although global growth is moderating, it should remain healthy and support export growth. One factor that will constrain shipments is the Alberta government’s measure to limit oil production in that province, but non-energy exports should be healthy. Meanwhile, import growth will return as Canadian companies import machinery and equipment and consumers keep their wallets open, albeit spending at a lower rate.

The Canadian dollar should also help net trade. The loonie lifted to 78 US cents in October amid news of the USMCA deal, then weakened as oil prices fell and markets grew worried about global growth prospects.

At the end of December, the currency stood at 73.30 US cents, helping export competitiveness and making imports more expensive. The forecast for the Canadian dollar is tied to changes in commodity prices and differential in short-term interest rates between Canada and the United States. With respect to the former, we expect commodity prices to rise in early 2019 but then face headwinds from slower global growth in 2020.

Meanwhile, little change is expected between the spread on US and Canadian interest rates. We see the currency fluctuating in a range of 73 to 76 US cents over the forecast horizon. In terms of risks, if the global economy disappoints and stumbles, the Canadian dollar will be weaker than in the base case forecast. Conversely, if the global risks do not manifest, the US dollar looks overvalued relative to most other currencies, which could provide some upside to the loonie.

Outlook for short-term interest rates and CAN dollar



Sources: Haver Analytics, Statistics Canada. Forecast by Deloitte.

Canadian summary with a regional dimension

Putting together all the pieces of the Canadian outlook, the emerging picture is one of a national economy that will experience more moderate economic growth of 1.6 percent in 2019 but perhaps a more substantial slowdown to 1.3 percent growth in 2020. Regional performances, however, will vary in coming year.

In Alberta, lower oil prices and production curtailment measures are likely to drop provincial economic growth from 2.3 percent in 2018 to around 1.3 percent in 2019. This is a particularly regrettable outcome, given that the province experienced a deep recession in 2015 and 2016.

The Atlantic provinces will post slower rates of expansion than Alberta, but this is largely because of aging demographics constraining sustainable growth in the region to an annual pace of around 1 percent. The projections may therefore seem low but they represent a respectable performance in the coming year.

Quebec's pace of expansion will be close to that of the national rate, but this is an above-average performance for the province. It suggests continued challenges for businesses from tight labour markets.

Ontario's growth will also be near the national average, which is an inevitable outcome since it's the largest

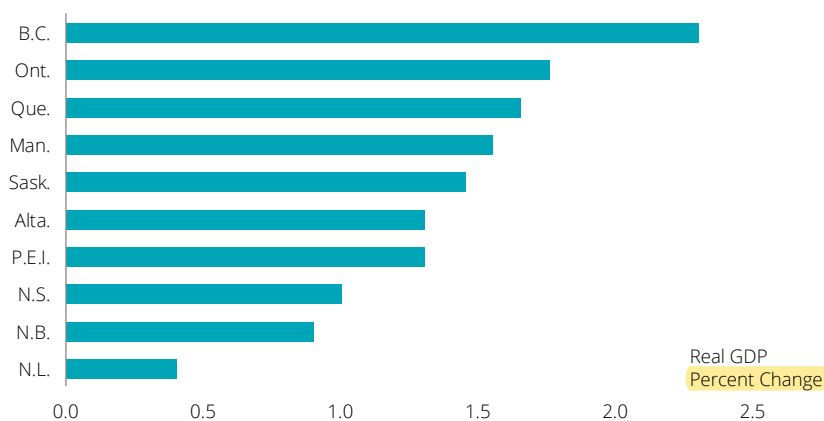
province in the federation. A key development in the last quarter, however, was the announcement of the likely GM closure of its Oshawa plant in 2019, the effects of which would ripple out to the auto sector more broadly. The GM decision was part of a broad restructuring brought on in part by technological change, which raises a question about the extent to which traditional manufacturing can be a major driver for Ontario's economic growth in the future. Ontario is particularly vulnerable to an economic slowdown in late 2019 and 2020.

Manitoba will grow a bit below, but close to, the national average. This reflects the diversified nature of its economy, which means it will be shaped by general macro trends.

Saskatchewan could feel the headwind of lower energy prices, but its economy is expected to get a lift from agriculture to post a gain of 1.5 percent in 2019.

BC should top the provincial leaderboard, with growth of 2.3 percent in 2019. While US trade exposure will be a negative for the 2020 outlook, the westernmost province will receive a boost over the forecast from the construction of a \$40 billion liquefied natural gas pipeline and processing plant.

Provincial economic outlook 2019



Sources: Haver Analytics. Forecast by Deloitte.

Canada: economic forecast

	2018				2019			
	Q1A	Q2A	Q3A	Q4F	Q1F	Q2F	Q3F	Q4F
Economic activity								
Real GDP (\$2012)	1.7	2.9	2.0	1.7	1.5	1.5	1.3	1.4
Personal expenditure	1.4	2.3	1.2	1.4	1.5	1.5	1.5	1.3
• Durables	1.4	0.6	-2.7	0.8	1.3	1.2	1.2	1.0
• Services	2.0	3.3	1.4	1.4	1.6	1.6	1.5	1.4
Residential investment	-7.9	-0.1	-5.9	0.5	1.0	0.5	0.0	0.0
Business investment	4.9	0.3	-6.5	1.5	1.4	1.2	0.9	0.9
• Non-residential construction	5.7	0.3	-5.2	1.2	2.0	1.8	1.5	1.4
• Machinery and equipment	25.5	2.0	-9.8	4.5	1.6	1.7	1.8	1.8
Gov't expenses and investment	2.3	1.2	1.9	1.9	1.9	1.8	1.5	1.5
Exports	2.3	13.0	0.9	2.0	2.0	2.4	2.0	0.6
Imports	4.7	5.9	-7.8	2.2	2.1	2.2	1.8	1.2
Prices								
CPI (year-over-year)	2.1	2.3	2.6	2.0	1.6	2.0	2.0	2.0
GDP deflator	1.5	1.5	3.0	1.0	1.2	1.6	2.4	1.6
Income								
GDP at market prices	2.9	4.6	5.0	2.7	2.7	3.1	3.7	3.0
Personal income (year-over-year)	5.0	4.3	3.2	3.2	3.2	3.2	3.5	2.9
Pre-tax corporate profits (year-over-year)	-3.6	5.6	18.8	12.8	12.9	7.4	3.3	1.3
Labour market								
Employment	0.1	0.7	1.3	1.5	0.8	0.6	0.5	0.4
Unemployment rate (%)	5.8	5.9	5.9	5.7	5.7	5.7	5.8	5.9

* Quarterly data is presented in quarter over quarter annualized percent change, annual data is year over year percent change, unless otherwise noted.

Sources: Statistics Canada, Haver Analytics. Forecast by Deloitte.

	2020				2018F	2019F	2020F
	Q1F	Q2F	Q3F	Q4F			
Economic activity							
Real GDP (\$2012)	0.9	1.3	1.6	1.6	2.1	1.6	1.3
Personal expenditure	1.2	1.4	1.7	1.7	2.2	1.5	1.4
• Durables	1.0	1.2	1.3	1.4	1.7	0.6	1.1
• Services	1.4	1.6	1.9	2.0	2.6	1.6	1.6
Residential investment	-1.0	-1.5	0.5	0.5	-1.0	-0.3	-0.4
Business investment	0.1	0.2	1.4	1.5	2.5	0.2	0.7
• Non-residential construction	1.0	1.1	1.8	2.0	3.2	0.7	1.4
• Machinery and equipment	1.0	1.2	2.0	2.2	7.9	0.7	1.5
Gov't expenses and investment	1.6	1.6	1.7	1.7	3.0	1.8	1.6
Exports	0.2	1.2	1.8	2.0	3.2	2.5	1.1
Imports	1.0	1.2	1.6	1.8	3.3	1.0	1.4
Prices							
CPI (year-over-year)	1.8	1.6	1.7	2.0	2.2	1.9	1.8
GDP deflator	1.4	1.5	1.6	2.1	1.9	1.7	1.7
Income							
GDP at market prices	1.9	2.8	4.2	3.6	4.1	3.3	3.0
Personal income (year-over-year)	2.8	2.7	3.0	3.1	3.9	3.2	2.9
Pre-tax corporate profits (year-over-year)	0.4	2.9	3.0	11.8	8.2	6.0	4.5
Labour market							
Employment	0.1	0.3	0.8	1.2	1.2	0.9	0.4
Unemployment rate (%)	6.0	6.0	6.1	6.1	5.8	5.8	6.1

Canada: financial forecast

	2018				2019			
	Q1A	Q2A	Q3A	Q4F	Q1F	Q2F	Q3F	Q4F
Interest rates								
Overnight rate %	1.20	1.25	1.47	1.69	1.75	2.00	2.25	2.25
3-month T-bill %	1.10	1.26	1.59	1.64	1.70	2.00	2.28	2.20
2-year government bond %	1.77	1.91	2.21	1.86	1.95	2.15	2.35	2.30
5-year government bond %	1.96	2.06	2.33	1.88	2.00	2.25	2.40	2.35
10-year government bond %	2.09	2.17	2.42	1.95	2.10	2.40	2.55	2.45
Yield curve								
10-year-3-month %	0.99	0.91	0.83	0.31	0.88	0.83	0.83	0.79
10-year-2-year %	0.32	0.26	0.21	0.09	0.15	0.25	0.20	0.15
Canadian dollar								
USD/CAD	1.27	1.26	1.29	1.31	1.36	1.36	1.34	1.33
US cents	79.06	77.45	75.00	73.30	73.50	74.50	75.00	75.00

* Historical data is period average, forecasts are period end.

Sources: Statistics Canada, Haver Analytics. Forecast by Deloitte.

	2020				2018F	2019F	2020F
	Q1F	Q2F	Q3F	Q4F			
Interest rates							
Overnight rate %	2.25	2.25	2.25	2.25	1.69	2.25	2.25
3-month T-bill %	2.20	2.20	2.20	2.20	1.64	2.20	2.20
2-year government bond %	2.28	2.30	2.35	2.40	1.86	2.30	2.40
5-year government bond %	2.30	2.35	2.40	2.45	1.88	2.35	2.45
10-year government bond %	2.40	2.45	2.50	2.55	1.95	2.45	2.55
Yield curve							
10-year-3-month %	0.78	0.73	0.72	0.65	0.31	0.79	0.65
10-year-2-year %	0.12	0.15	0.15	0.15	0.09	0.15	0.15
Canadian dollar							
USD/CAD	1.33	1.36	1.35	1.33	1.31	1.33	1.33
US cents	73.50	74.00	75.00	76.00	73.30	75.00	76.00

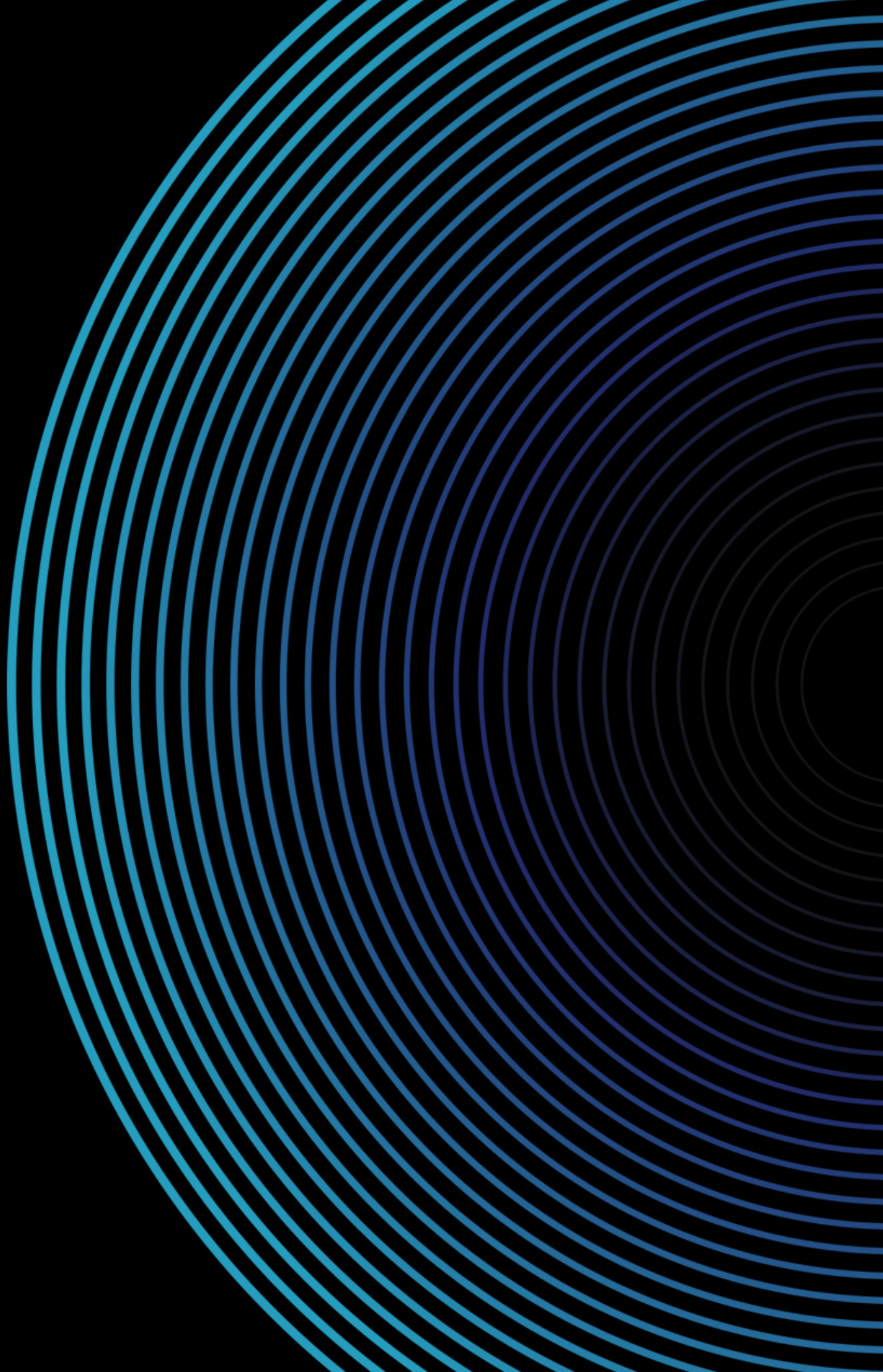
Concluding remarks

With the arrival of a new year, it's natural to wonder what's in store. We expect 2019 to be a year of economic moderation internationally and in Canada. Domestic economic growth should be modest at close to 1.6 percent. The outlook for 2020 is more ominous, as a significant US slowdown is likely to pull Canadian economic growth down to 1.3 percent.

Storm clouds are gathering on the horizon in the form of key downside risks. Further US protectionism and international retaliation, a potentially messy UK exit from the European Union, and increased market volatility could, taken together, contribute to weaker global growth, lower commodity prices, and detrimental economic and financial consequences around the world over the next couple of years.

It's also important to be mindful of where we are in the business cycle. History tells us that the typical economic recovery and expansion is eight to 10 years long. It has now been a decade since the last downturn, so the current business cycle is long in the tooth. This is part of the reason the financial market sentiment became negative in late 2018. A downturn is not in the base case Deloitte economic forecast, but we are monitoring the risks closely.

While the downside risks have risen, we advise Canadian businesses to not overreact. A riskier economic environment should not be allowed to paralyze or delay their decision-making. Firms should continue building for the future—making key investments, developing their talent, and growing their businesses. At this stage, they should be bracing for slower economic growth but also considering how they'll cope with the next business cycle when it finally occurs.



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