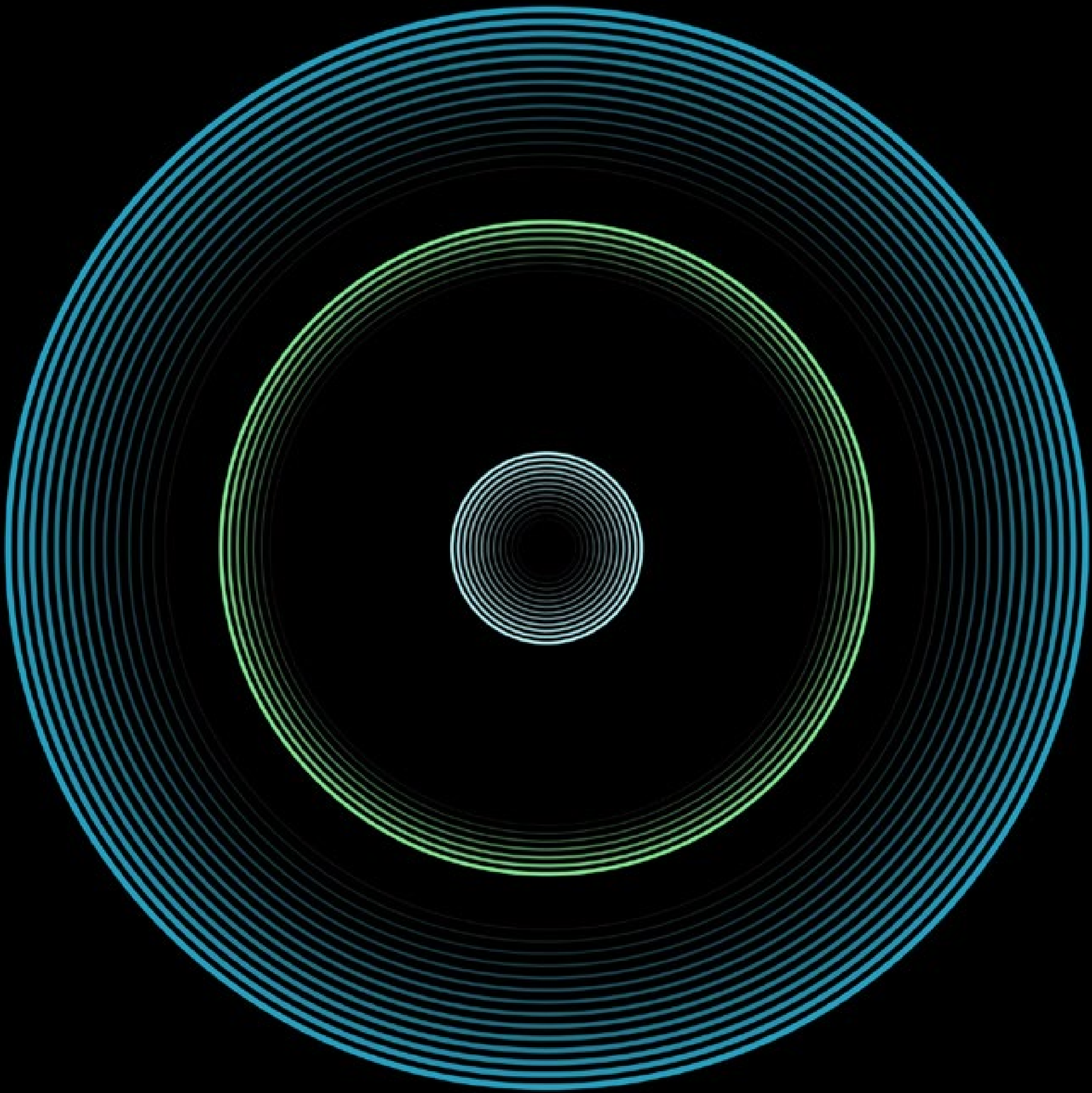
Deloitte.



Economic outlook

Singing the late cycle blues

Introduction

It is well known that economies go through regular fluctuations; this is called the business cycle. There are recessions, when firms cut production and scale back on costs, including staff, which creates economic slack. Then the tide turns, setting the stage for recovery and subsequent expansion. Expansions absorb the slack that was created during the downturn, with businesses ultimately producing at high levels of capacity and with unemployment rates dropping to historically low levels. This is the late stage of the business cycle—and it's where the North American economy stands today.

The signs are everywhere you look. The US equity market is now the longest bull market in history; the US unemployment rate is below 4 percent; the Federal Reserve is raising interest rates; and the US yield curve is so flat that investors worry about it inverting and sending a recession signal. In Canada, the signs are less prevalent but still present, including an unemployment rate at close to a four decade low and a central bank gradually raising rates.

At this point in the business cycle, we stand at a crossroad: Either strong economic growth will continue causing the economy to overheat and create inflationary pressures, or economic growth will slow to a more moderate and sustainable rate of expansion. Deloitte Economic Advisory anticipates the latter scenario playing out.

The US economy is tracking robust growth of around 3 percent this year, with fiscal stimulus from large tax cuts contributing to the rapid expansion. However, the Federal Reserve is likely to continue gradually raising interest rates, US tariffs on imported goods will be a drag on growth, and the temporary boost from fiscal policy will diminish next year. By 2020, the United States will face considerable fiscal drag, and this is expected to lead to much slower economic growth there. Meanwhile, the European and Japanese economies are also facing diminishing economic slack and a reduction in monetary stimulus that is likely to temper growth. As the advanced economies slip down a gear, global economic growth is likely to lose some momentum. Many emerging economies are likely to experience higher inflation, created by currency depreciation and other factors like tariffs (in the case of China), and this will lead to tighter monetary policy. The result will be a slowdown in global economic growth, which will create a headwind for commodity prices and limit Canadian export growth.

In Canada, too, the late-stage narrative will play out. Growth in domestic demand is poised to diminish, as consumers and real estate cannot continue to be the engines of economic growth that they have been in the past. However, the Canadian economic story is more nuanced than that of the United States. The commodity correction that depressed economic growth in resource-rich provinces in 2015 and 2016 means that there is still economic slack in these regions. Some provinces – including B.C., Ontario, and Quebec – were less affected, and have been delivering solid economic growth for quite some time. And, the resource provinces have been recovering since the start of 2017. This helps to explain why the national unemployment rate is hovering at close to a 40-year low and the Bank of Canada has been edging interest rates higher.

However, the pace of Canadian economic growth is in the process of slowing. After expanding by 3 percent in 2017, growth this year will drop towards 2 percent. In 2019, the economy is expected to deliver a gain of less than 2 percent and growth could drop down to 1.4 percent in 2020 as the global economy slows and US demand in particular, softens.

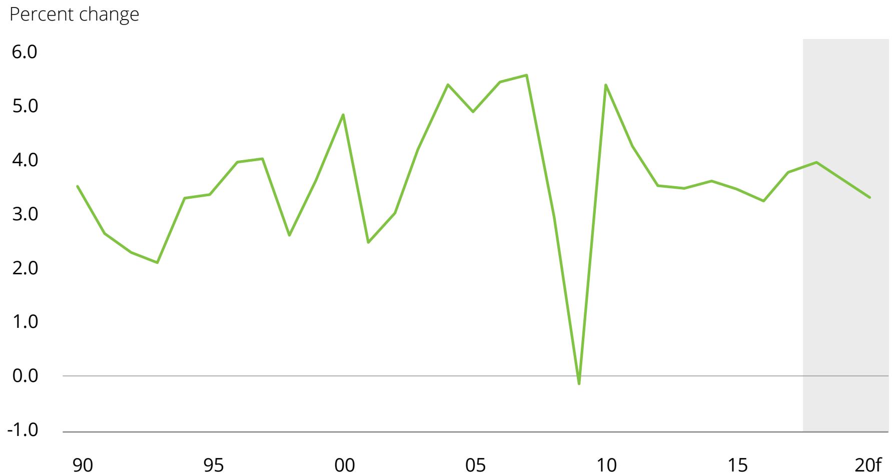
At the time of writing, a tentative negotiation of a triparty North American trade deal (USMCA) to replace NAFTA eliminates a key risk to the Canadian economic outlook, but US protectionism is still a key risk to the global economy. America's tariffs on products from around the world are having a negative, though limited, impact on global economic growth. However, if the tariffs are significantly expanded and other countries retaliate, the result could materially weaken the global economy—and this would feed through to Canada. So, beyond the late business cycle slowdown that seems to be in the cards, the political risks are elevated at the moment.

"By 2020, the United States will face considerable fiscal drag, and this is expected to lead to much slower economic growth."

International outlook

The world economy is delivering solid, broad-based growth, and is tracking a gain of around 3.8 percent in 2018, but growth is expected to slow to 3.5 percent in 2019 and drop to 3.2 percent in 2020.

World economic growth has strengthened
Global real GDP



Source: International Monetary Fund; forecast by Deloitte.

The US economic cycle will play a key role in how the story unfolds. The US is leading the growth rankings of advanced economies, with real GDP likely to climb 3 percent this year. The large tax cuts announced early in the year are boosting consumption, investment, and job creation. The tax stimulus has come at a time when the economy was already firing on all cylinders. Job creation has been strong and the unemployment rate has dropped to levels that economists generally consider to be full employment. This strong performance has led the Federal Reserve to gradually tighten monetary policy.

In 2019, the pace of US economic growth should slow toward a 2 percent pace as the tax stimulus declines. However, in late 2019 and into 2020, fiscal drag will become substantial. The simple fact is that if you give the economy a big fiscal boost one year and don't have a matching boost the next year, this mathematically leads to a slower pace of economic growth. Indeed, fiscal drag could knock 0.7 percentage points off of economic growth in 2020, which will reduce the US rate of expansion to well below 2 percent. Retaliation to US tariffs already announced could also lower US growth by 0.2 to 0.4 percentage points, with additional downside if the tariff war escalates further.

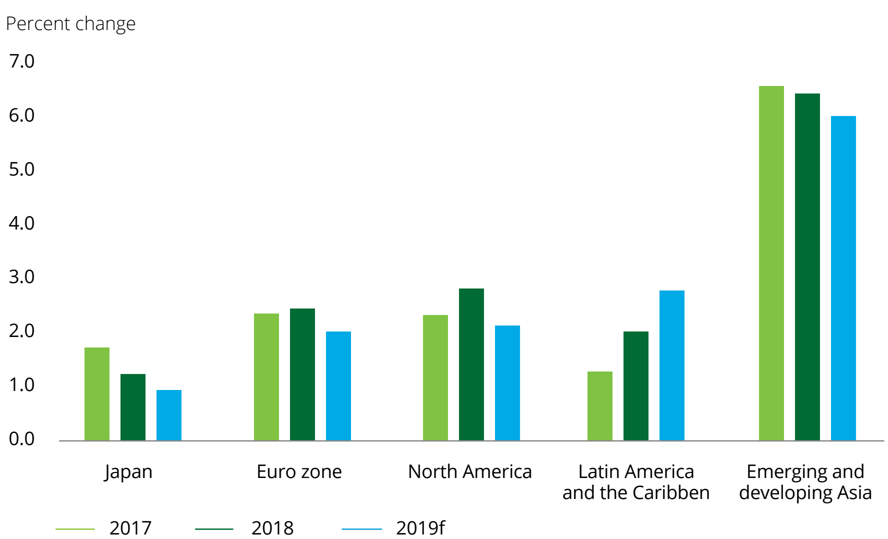
In Europe, the euro-area should deliver a solid gain this year, but declining economic slack should lead the European Central Bank to wind down its bond-buying program and consider raising interest rates in 2019. The pace of euro-zone growth is anticipated to slow from 1.8 percent in 2018 to 1.6 percent in 2019, and cool a bit further the year after. The UK economy has been expanding at a respectable pace, but Brexit risks continue to loom as it negotiates a divorce from the European Union. Japan's economy, after a strong gain in 2017, should trend back down toward the 1 percent pace, which is its long-term sustainable pace due to the demographic pressures of an aging workforce.

All told, economic growth in advanced countries is poised to moderate, and there should be a similar story in emerging markets. Strains have developed in emerging markets in 2018, with particular problems in a number of countries, such as Turkey and Argentina, that reflect localized issues. However, the combination of higher US interest rates and weak emerging market currencies has created an upside risk to prices in many developing countries, and this could lead to a tightening of monetary policy. This will create financial pressures that are expected to temper growth in many developing nations. In the case of China, US tariffs also pose a clear and present danger. Growth in developing countries in aggregate should come in at close to 5 percent in 2018, but trend lower in 2019 and 2020. Indeed, China's economic growth should drop from 6.5 percent this year to below 6 percent over the next two years.

The number-one risk to the world outlook is an escalation of the global tariff war. US protectionism has led to increased duties on a number of imported products. So far, the economic consequences are limited, but they could increase. Each round of American tariffs leads to an equivalent response by those affected, and if the tariff cycle continues, it could undermine global economic growth. The US duties are being applied on the grounds of a security threat as a means of circumnavigating World Trade Organization tariff limits. This is a dangerous precedent. It would deeply undermine the world trade order if other countries were to follow suit.

A second risk is the global rebalancing of monetary policy. As the Federal Reserve gradually raises the fed fund rates further in 2019, US bond yields will rise, and this, in turn, will lift global bond yields because fixed-income products globally tend to trade as a spread to US yields. As other central banks join the tightening cycle, they will need to be mindful of the risks, and rate increases will need to be done incrementally, not only to contain inflation but also to limit the impact of higher interest rates on the economic expansion. The base case forecast assumes this happens smoothly, but there are clearly financial and economic downside risks.

Expansion is broadly based, poised to cool
Regional real GDP

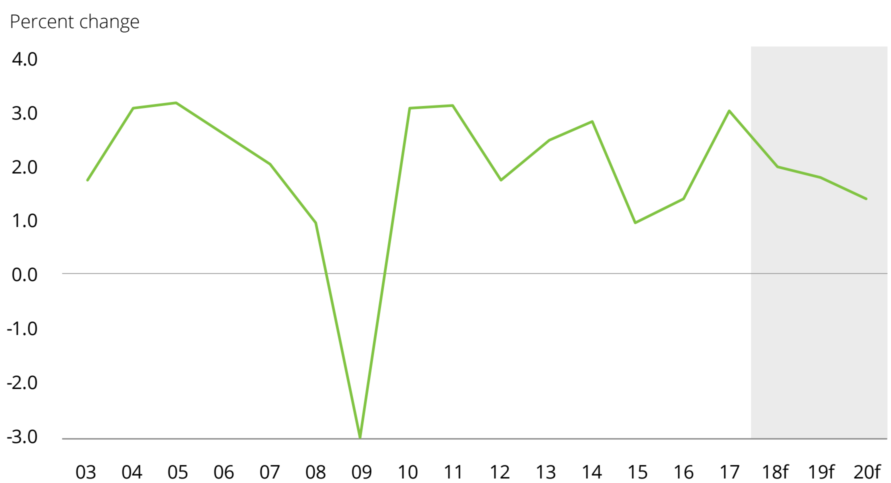


Source: International Monetary Fund, Forecast by Deloitte.

Details of the Canadian outlook

The Canadian economy grew by a strong 3 percent in 2017, but decelerated significantly in the second half of the year. This created a soft handoff heading into 2018, and economic growth was modest in the first quarter. After a strong second quarter, the pace of economic growth in Canada is poised to moderate.

Canadian economic growth to gear down
Canada real GDP



Source: Statistics Canada; Haver Analytics; forecast by Deloitte.

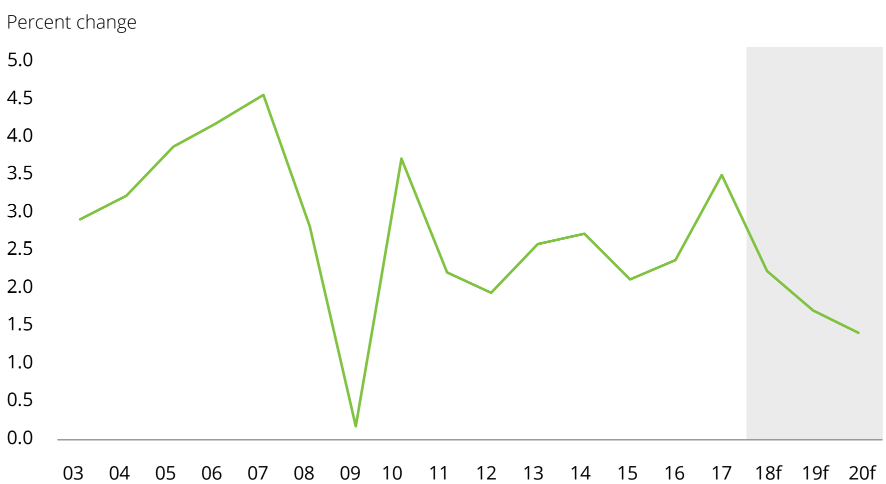
For many years, economists have called for a rotation in the drivers of economic growth. During the recovery and expansion since the last recession, consumers and real estate have been fuelling much of Canada's gains. However, consumers are now heavily indebted, and real estate affordability has deteriorated, particularly in Canada's largest urban centres. In early 2018, however, consumer spending moderated, and real-estate activity declined in reaction to new mortgage stress-testing regulations and rising interest rates. In contrast, business investment and exports increased their contribution to growth in the first half of this year. This was a welcome development.

The outlook appears less promising, however. Consumer spending should grow at a pace slightly below 2 percent, and new home construction is expected to soften in response to higher interest rates and weaker buyer demand. Although businesses are operating at high levels of capacity utilization, they are likely to be cautious in new major capital outlays. This reflects business uncertainty related to US protectionism, but also concerns about competitiveness. Investment in non-residential structures as well as machinery and equipment should increase, although not at a strong pace. Similarly, Canadian exports should grow at only a moderate rate in 2019, partly reflecting the loss of market share in many of Canada's major export markets, and export growth is expected to slow further in 2020 as US demand wanes. All told, economic growth is anticipated to drop to slightly below 2 percent next year and head down to 1.4 percent in 2020.

Consumers to keep spending, but at a more moderate pace

Over the past decade, the Canadian consumer has been the key driver of economic growth. Wallets have been kept open by strong job creation, declining unemployment, rising personal income, low interest rates, and strong real estate markets. But, the pace of spending is about to cool.

Consumer spending to moderate
Real personal consumption expenditure

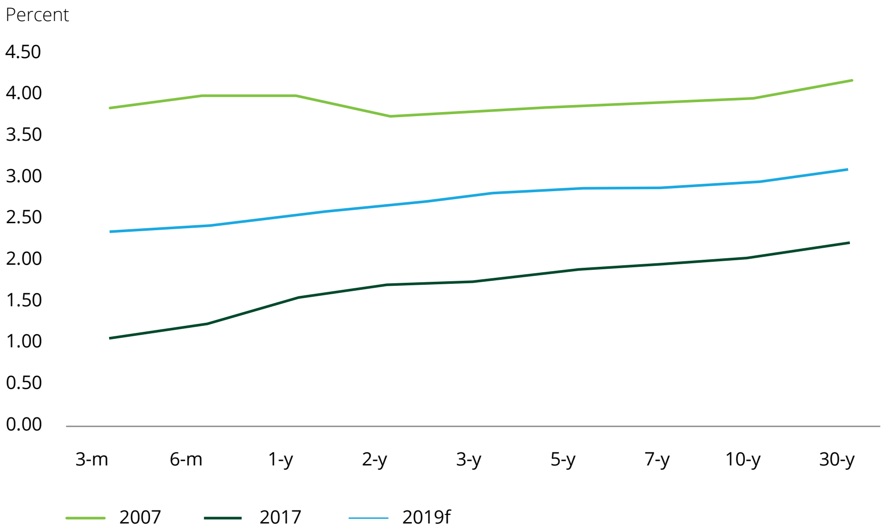


Source: Statistics Canada; Haver Analytics; forecast by Deloitte.

In 2018, the consumer narrative is still positive but there are headwinds that will constrain spending growth. First, consumers are likely to be reluctant to ramp up their debt levels further. Since the last recession, Canadians have funded a significant amount of spending and investment through debt financing, particularly real-estate related borrowing. Consequently, debt as a share of real personal disposable income has climbed to lofty levels. The share of after-tax income going towards servicing debt is also elevated. Looking ahead, households are expected to constrain their debt growth as rising interest rates lift debt-servicing costs. The Federal Reserve will be raising interest rates, boosting US bond yields. That will lead financial markets to push Canadian bond yields higher, and this is likely to boost fixed mortgage rates in Canada. Meanwhile, the Bank of Canada is expected to raise the overnight rate by a quarter point later this year, and then tighten monetary policy by a further 75 basis points in 2019, which will raise variable mortgage rates.

Interest rates to rise

Government of Canada yield curve



Source: International Monetary Fund, Forecast by Deloitte.

A second headwind on consumer spending will be relatively flat real estate markets. The imposition of income stress tests on all mortgages originated at federally regulated institutions, which encompasses the major banks, led to a pullback in Canadian real-estate market activity, particularly in the largest and most expensive Canadian cities. In the past, the impact of regulatory changes on markets have lasted for some six to nine months, and then subsided. This appears to be happening in the Greater Toronto Area. New headwinds on real estate will come from slowing economic growth, which will constrain job creation, and from gradually rising interest rates. The result will be weak residential fixed investment (i.e., new home building) and relatively flat existing home sales in 2019. These trends will constrain consumer spending on housing-related items such as furniture and appliances.

A final factor weighing on consumption growth is the lack of pent-up consumer demand. During periods of economic weakness, households tighten the purse strings and limit their spending; while in periods of recovery and expansion, households make up for their prior thriftiness, and spending grows quickly. In provinces hit hard by the 2014-2015 commodity correction, pent-up demand was created. However, consumer spending surged in 2017 and the continued growth in 2018 has absorbed a lot of that pent-up demand. In parts of the country that were less affected by the commodity cycle, consumers have had their wallets open for a long time. This can be illustrated in statistics such as the record level of auto sales.

There is one accounting issue that will occur in the final quarter of this year: the addition of legalized cannabis to the economic accounts by Statistics Canada. This will boost consumption in the fourth quarter, but it will be an artificial increase, since it's taking something that is currently off the books and adding to the official statistics.

All told, the general trend will be toward slower personal consumption growth, which is projected to increase by 2.2 percent this year, cool to 1.8 percent in 2019 and slip to 1.4 percent in 2020. This will weigh on aggregate economic growth, because consumption accounts for more than half of the economy.

Greater investment is needed

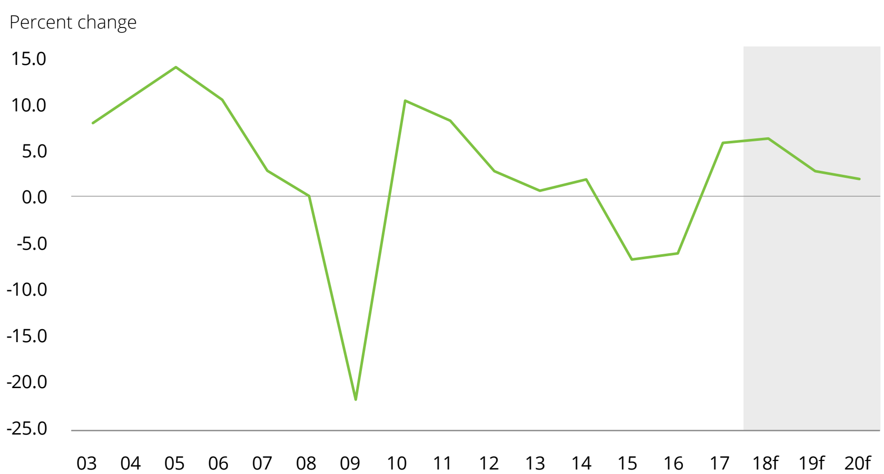
Residential investment is likely to experience a small decline this year due to the cooling in real-estate markets caused by the new mortgage regulations, recent increases in mortgage rates, and expectations of further increases in borrowing costs. Reduced willingness of consumers to grow personal debt will also limit housing activity, and, consequently, new residential construction. While the rising population—fuelled in large part by immigration to the major urban centres, low unemployment, and rising personal income—will provide underlying support to real estate activity. But, these fundamentals limit future weakness rather than fuel strong buying. The shifting demographics—in particular, the aging population—is expected to weigh on home prices both in cities that are less able to attract immigrants and in rural areas.

Investment in non-residential structures experienced a strong increase in the first quarter of 2018, but lost momentum in second quarter. Firms are reporting that they are running at high capacity, so some additional investment in non-residential structures should be on the horizon. However, businesses are being cautious in their investment plans.

After two very strong quarters of growth, business investment in machinery and equipment (M&E) stalled in the second quarter 2018. However, capacity pressures should encourage businesses to invest in M&E. Canadian businesses tend to invest less in capital per worker than their international peers, and business cautiousness as well as weaker growth prospects in North America may temper the pace of expansion in capital spending. M&E investment should advance by roughly 8 percent this year, due to a remarkably strong first quarter, but slow to around 3.2 percent growth in 2019, and subside to 2.4 percent in 2020.

Government investment declined in the second quarter of 2018, but was still up 5.4 percent year over year. The federal government committed to large-scale funding of infrastructure in its last two budgets. In 2016 and 2017, government investment rose 5.1 percent and 3.8 percent, respectively. These are solid increases, but still represent only a gradual rollout of the planned infrastructure investment. The delays reflect planning and approvals but also the need to partner with provinces on many projects. The federal government is still committing the full amount of funds, and provinces do need to upgrade and expand their infrastructure. So, further gains in this category are expected over the forecast.

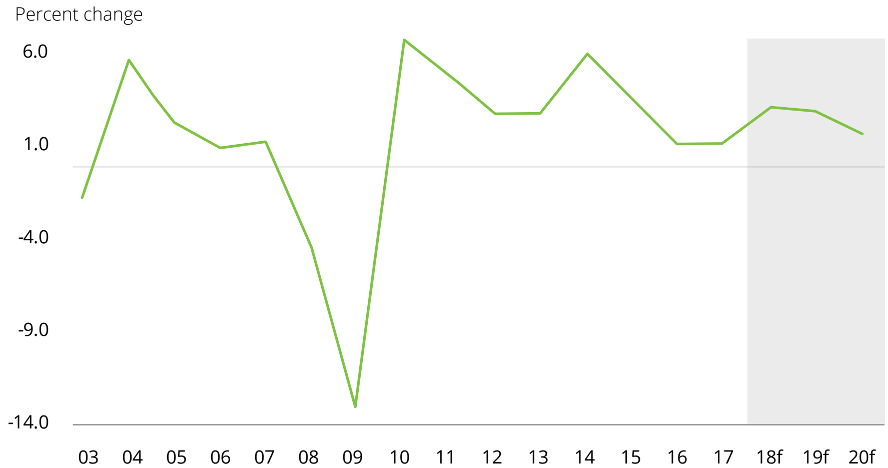
Business investment needed due to capacity limits
Business investment, machinery and equipment



Source: Statistics Canada; Haver Analytics; forecast by Deloitte.

Export prospects tied to global demand

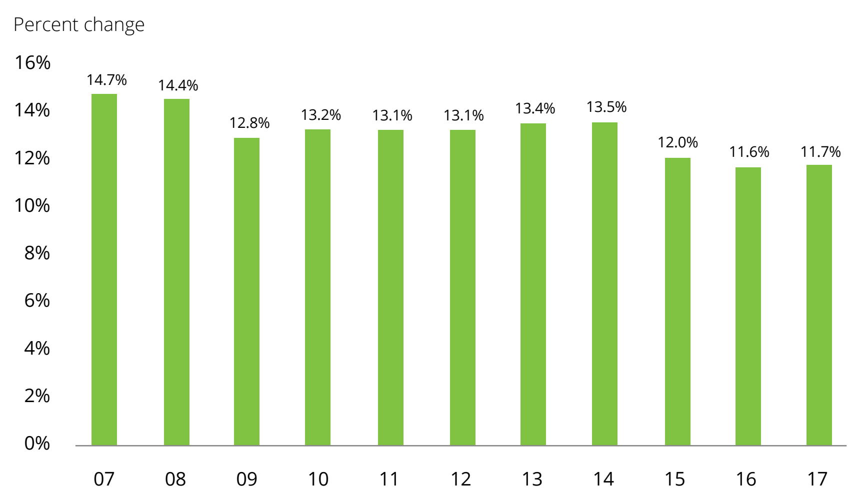
Exports picking up, could be better
Real exports



Source: Statistics Canada; Haver Analytics; forecast by Deloitte.

Exports delivered an impressive increase of more that 12 percent annualized in the latest quarter. Looking forward, Canadian exports will be supported by rising foreign demand, including a robust US economy and increasing global demand for commodities, and a Canadian dollar below 80 cents. But, the pace of export growth will be constrained by the loss of market share in many key international markets. Exports are particularly vulnerable in 2020, when the U.S. economy is likely to experience significantly slower growth due to fiscal drag caused by the loss of tax stimulus. Canadian exports are expected to grow at 3.0 percent in 2018, slowing to 2.8 percent in 2019 and 1.7 percent in 2020.

Canada losing market share
Canada export share of US imports



Source: Census Bureau; Haver Analytics.

Canada is a small, open economy. As a result, import growth is tied to growth in final domestic demand and movements in the foreign exchange rate. As economic growth in Canada slows, so too should import growth. Import growth is expected to trail export growth in 2019, which should lead to a narrowing in Canada's trade and current account deficits. But a reversal is expected in 2020, when US economic growth subsides.

US-Mexico-Canada Agreement (USMCA)

News that a tentative tri-party trade deal to replace NAFTA has been negotiated is unambiguously positive for the Canadian economic outlook. One can debate over the terms reached; but, if passed, the successful agreement lifts a cloud of uncertainty that had been hanging over the Canadian economy that was likely deterring investment. It also averts US tariffs on Canadian autos and parts that would have been very damaging to the economy. USMCA regrettably does not create greater free trade across the member countries. For example the terms of the auto section are expressed as restrictions, but ones that the Canadian auto sector can meet. The critical point is that the deal blunts protectionism and constitutes terms that all parties can live with for years. Canada made concessions, but every trade deal involves trade-offs that have domestic economic consequences. In the end, Canada maintains open access to the US market, the largest in the world and the destination for 70 percent of Canadian exports. It also the Chapter 19 dispute resolution mechanism that was a line in the sand for the Government of Canada as a means of recourse if the US applies anti-dumping or countervailing duties on Canadian products.

Inflation to remain in abeyance

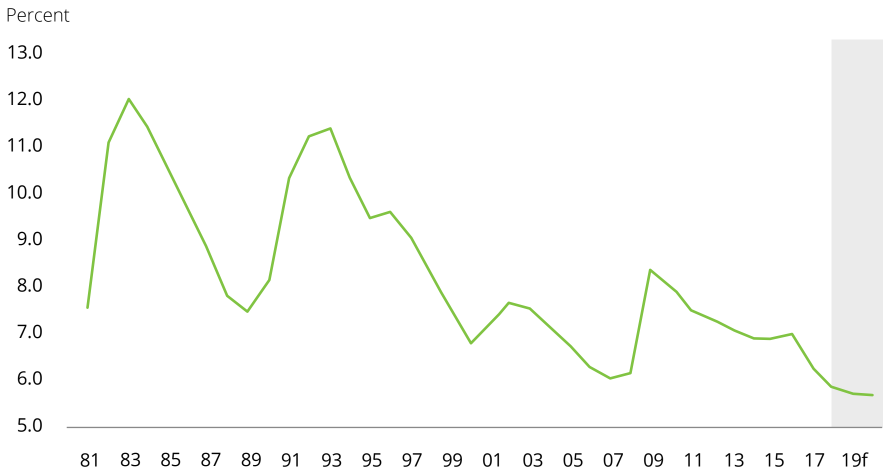
Inflation measured by the year-over-year change in the consumer price index stood at 3 percent in August, which is at the top of the Bank of Canada's target range of 1 to 3 percent. The Bank views a number of temporary factors as pushing up headline inflation, such as the rise in gasoline prices and the impact of a weaker Canadian dollar. Meanwhile, core measures of inflation that exclude some of the volatile components are sitting very close to the Bank's 2 percent mid-point target. Over the forecast horizon, headline inflation should trend downwards as economic growth moderates, interest rates rise, and energy prices dip slightly. Downside risks to inflation will be present in 2020 when economic growth in North America loses momentum.

Labour markets

Canadian job creation has been strong, but is clearly decelerating. After creating 336,500 jobs in 2017, the monthly pattern in 2018 has been very choppy, and by the end of the summer job creation had stalled temporarily. The prior robust pace of employment creation pushed the unemployment rate down to a 40-year low of 5.8 percent in the first half of the year. Typically, such a low rate of unemployment would create concerns about a possible rise in inflation. But, the Bank of Canada is not unduly worried, and for good reason.

Unemployment rate down to a **40** year low of **5.8%** in the first half of the year.

40-year low unemployment rate
Canada national unemployment rate



Source: Statistics Canada; Haver Analytics; forecast by Deloitte.

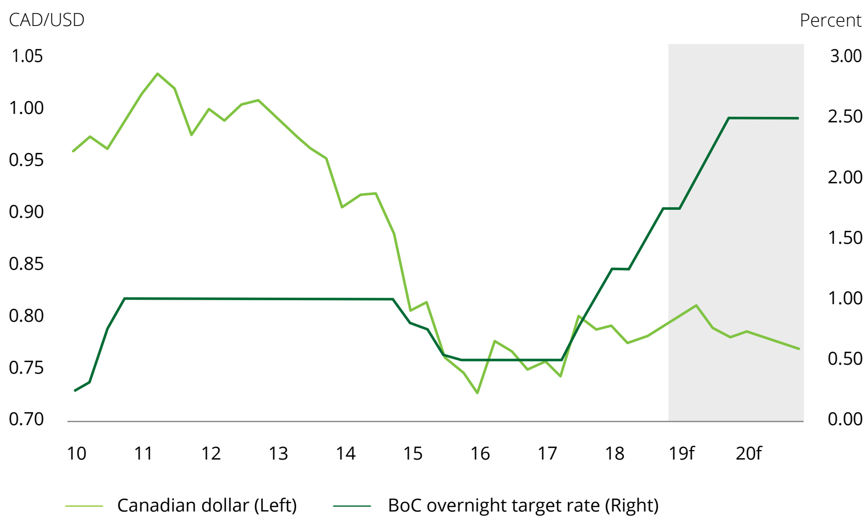
First, demographics are distorting the historical comparison, since retiring baby boomers exit the job market and leave the labour force. The effect of lower employment and lower labour participation by boomers will tend to lower the unemployment rate.

Second, tight labour markets can fuel inflation through rising wages that get passed along to consumers. However, the low unemployment rate does not appear to be creating significant wage growth. From the start of this year until May, there were signs that wage growth was picking up, and it reached 3.9 percent year over year for permanent employees. But over the three months ending in August, wage growth has slowed to 2.6 percent. The weakness in wages is a bit of a conundrum, but it likely reflects several factors. They include technical change and low interest rates that have made capital cheap, and limiting bargaining power for many middle-skill workers for whom there is lower labour-market demand. Nevertheless, sustained low unemployment should ultimately nudge wages up, and this is why the Bank of Canada will need to gradually tighten monetary policy.

Interest rates and Canadian dollar

The temperate rise in wages provides some breathing room for the Bank of Canada. The Bank estimates that the neutral level of interest rates, which are neither providing stimulus to the economy nor applying the brakes, is an overnight rate of 2.50 to 3.50 percent. Accordingly, the declining slack in the labour market calls for the Bank to reduce the amount of monetary stimulus being provided, but the tame wage picture means that it need not hike rates quickly and aggressively. The Bank of Canada is expected to increase the overnight rate by 25 basis points in late 2018 and a further 75 basis points by the end of 2019. This tightening of monetary policy should boost Canadian bond yields, as will rising US bond yields. However, slower economic growth in 2020 should lead the Bank of Canada to hold off on raising interest rates further.

BoC to raise rates less than Fed, creating headwinds for Canadian dollar
Canadian dollar and Bank of Canada overnight rate



Source: Bank of Canada; Haver Analytics; forecast by Deloitte.

The Canadian dollar exchange rate to the US dollar received a lift from news that a tentative North American trade deal was reached. In terms of the outlook, the value of the loonie should be shaped by trends in commodity prices and by changes in interest-rate spreads caused by central bank policy changes. In 2019, the Canadian dollar may not get much of a lift from commodity prices and the upside to the currency may be limited by the Federal Reserve tightening policy by more than the Bank of Canada. In 2020, a weaker US dollar, reflecting poorer US economic prospects, should help the loonie strengthen a bit further but slower global growth may weigh on commodity prices. These offsetting forces will create volatility in the exchange rate, but leave it on average between 78 and 82 US cents.

Canada economic outlook

	2018				2019			
	Q1A	**Q2A**	**Q3F**	**Q4F**	**Q1F**	**Q2F**	**Q3F**	**Q4F**
Economic activity								
GDP at market prices	3.1	5.1	4.4	4.7	3.8	3.6	3.4	3.3
Real GDP ($2007)	1.4	2.9	2.0	2.5	1.7	1.6	1.6	1.7
Personal Expenditure	1.0	2.6	1.9	2.4	1.6	1.3	1.5	1.4
• Durables	1.5	2.1	1.6	1.5	1.2	1.0	1.1	1.2
• Services	1.7	3.2	2.4	2.2	1.8	1.7	1.6	1.5
Residential Investment	-10.5	1.1	0.5	-0.5	-0.8	-1.0	-1.2	-1.6
Business Investment	11.4	1.9	2.8	3.3	3.1	3.0	2.7	2.0
• Non-res contruction	8.2	2.2	3.0	3.2	2.9	2.5	2.6	1.8
• Mach. & Equip.	16.4	1.4	2.6	3.6	3.5	3.6	3.0	2.3
Government Exp. & Invest.	2.8	1.0	1.0	1.7	2.7	2.1	2.0	1.9
Exports	2.4	12.3	1.6	2.1	2.3	2.5	2.6	2.0
Imports	4.2	6.5	0.8	1.9	2.0	2.2	2.1	1.8
Prices								
CPI (Yr/Yr)	3.6	1.1	2.9	2.6	2.2	2.0	1.9	1.8
GDP deflator	1.7	2.1	2.4	2.2	2.1	2.1	1.8	1.6
Income								
Personal income	3.7	4.4	4.6	4.3	4.4	3.8	4.0	3.9
Pre-tax corporate profits	0.3	11.8	3.8	7.4	5.0	4.8	2.5	0.1
Labour market								
Employment	0.1	0.7	1.0	1.1	1.3	1.0	1.0	0.8
Unemployment rate (%)	5.8	5.9	6.0	6.1	5.8	5.7	5.8	6.0

* Quarterly daia is presented in Q/Q annualized percent change, annual data is Yr/Yr percent change, unless otherwise noted.

Source: Statistics Canada, Haver, Forecasts by Deloitte.

	2020				2018F	2019F	2020F
	Q1F	**Q2F**	**Q3F**	**Q4F**			
Economic activity							
GDP at market prices	3.3	2.6	2.7	3.3	4.1	3.8	3.1
Real GDP ($2007)	1.6	0.9	1.1	1.4	2.0	1.9	1.4
Personal Expenditure	1.3	1.4	1.5	1.4	2.2	1.8	1.4
• Durables	1.0	0.7	0.8	0.9	1.8	1.3	1.0
• Services	1.4	1.6	1.7	1.7	2.7	2.0	1.6
Residential Investment	-2.0	-3.0	-1.0	1.0	-0.3	-0.6	-1.6
Business Investment	1.6	1.6	1.7	1.8	6.4	2.9	1.9
• Non-res contruction	1.2	1.0	1.5	1.6	5.3	2.7	1.6
• Mach. & Equip.	2.2	2.4	2.0	2.0	8.2	3.2	2.4
Government Exp. & Invest.	1.7	1.5	1.7	1.7	2.6	1.9	1.8
Exports	1.1	1.5	1.7	2.3	3.0	2.8	1.7
Imports	1.6	1.6	2.0	2.0	4.3	2.1	1.8
Prices							
CPI (Yr/Yr)	1.8	1.7	1.7	1.7	2.6	2.0	1.7
GDP deflator	1.7	1.7	1.6	1.8	2.1	1.9	1.7
Income							
Personal income	3.0	2.6	3.0	3.3	4.6	4.2	3.3
Pre-tax corporate profits	-0.2	-0.5	6.0	6.5	4.1	5.0	1.6
Labour market							
Employment	0.5	0.5	0.6	0.7	1.2	1.1	0.7
Unemployment rate (%)	6.0	6.1	6.3	6.4	6.0	5.8	6.2

Canada financial outlook

	2018				2019			
	Q1A	**Q2A**	**Q3F**	**Q4F**	**Q1F**	**Q2F**	**Q3F**	**Q4F**
Interest rates								
Overnight rate %	1.25	1.25	1.50	1.75	2.00	2.25	2.50	2.50
3-mth T-bill %	1.10	1.26	1.55	1.70	1.98	2.05	2.35	2.35
2-Yr Gov't Bond %	1.78	1.91	2.21	2.30	2.35	2.45	2.55	2.55
5-Yr Gov't Bond %	1.97	2.07	2.33	2.40	2.45	2.53	2.61	2.59
10-Yr Gov't Bond %	2.09	2.17	2.42	2.55	2.60	2.65	2.70	2.65
30-Yr Gov't Bond %	2.23	2.20	2.42	2.65	2.70	2.75	2.80	2.75
Yield curve								
10Yr-2Yr %	0.31	0.26	0.21	0.25	0.25	0.20	0.15	0.10
Canadian dollar								
USD/CAD	1.26	1.29	1.29	1.27	1.25	1.23	1.27	1.28
U.S. cents	79.06	77.45	77.24	79.00	80.00	81.00	79.00	78.00

*All values are end of period.

Source: Statistics Canada, Haver, Forecasts by Deloitte.

	2020				2018F	2019F	2020F
	Q1F	**Q2F**	**Q3F**	**Q4F**			
Interest rates							
Overnight rate %	2.50	2.50	2.50	2.50	1.75	2.50	2.50
3-mth T-bill %	2.35	2.35	2.35	2.35	1.70	1.98	2.05
2-Yr Gov't Bond %	2.50	2.45	2.45	2.50	2.30	2.35	2.45
5-Yr Gov't Bond %	2.55	2.49	2.50	2.60	2.40	2.45	2.53
10-Yr Gov't Bond %	2.58	2.52	2.55	2.65	2.55	2.60	2.65
30-Yr Gov't Bond %	2.68	2.64	2.65	2.75	2.65	2.70	2.75
Yield curve							
10Yr-2Yr %	0.08	0.07	0.10	0.15	0.25	0.25	0.20
Canadian dollar							
USD/CAD	1.27	1.28	1.29	1.30	1.27	1.28	1.30
U.S. cents	78.50	78.00	77.50	77.00	79.00	78.00	77.00

Concluding remarks

After a stellar 2017, the Canadian economy will deliver solid performance this year. Economic growth will be slower, but this represents a gearing down to a more sustainable pace of expansion. In 2019, the pace of expansion should remain moderate at close to, or slightly below, 2 percent. If the tentative new North American trade deal is ratified, the near-term downside risks to the outlook will have lessened. With this backdrop, the Bank of Canada is expected to gradually raise interest rates. Prospects in 2020 look more challenging. It is likely that the loss of fiscal stimulus and higher US interest rates will lead to significantly slower US economic growth. Canada is integrated into North American supply chains and economy. Accordingly, Canada is anticipated to import weaker economic growth. The slower pace of growth may be viewed as disappointing, but this is what the late stage of a business cycle looks like if inflationary pressures are avoided.

To achieve a better outcome, Canada needs to boost the economy's potential to sustain stronger growth over the long-run. As Deloitte has highlighted in its past research, this is ultimately about improving our competitiveness, productivity and innovation. It also includes unlocking the potential of the Canadian labour force, particularly under-represented groups such as women, immigrants, Indigenous people and people with disabilities. The strong partnerships between business and policymakers required to achieve this are beyond the scope of this near-term economic outlook.

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