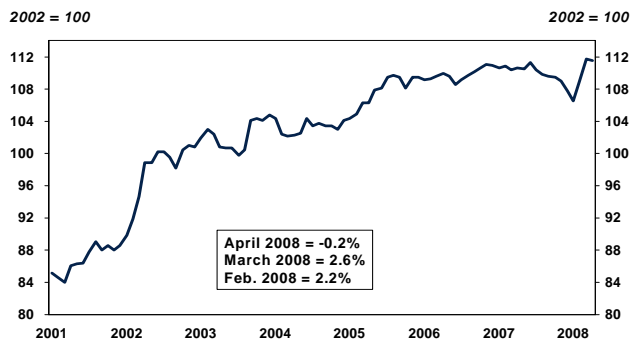


Québec's economy: Is the DLI's turnaround just a flash in the pan? Second straight gain in April (+0.1%)

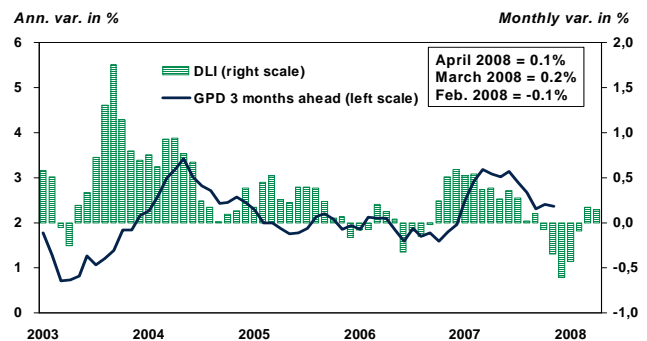
With roadblocks to Québec's economy piling up, the second increase in the Desjardins Leading Index (DLI) provides a ray of hope. This timid improvement in the DLI is not enough to augur stronger economic growth in the next three to six months, of course. In fact, Québec's economy has probably not yet bottomed out. For one thing, international exports continue to pull back on the problems in the American economy, along with the strong loonie and global competition. As the economic recovery has been put back until next year in the United States, foreign trade will continue to suffer. For another, surging gas prices and the labour market's recent deterioration could cast a shadow over consumer spending. Although individuals have gotten some solid tax relief, consumer spending can be expected to lose some steam. Domestic demand could feel the pinch if it takes a while for gas prices to come down and employment does not recover quickly. In other words, it would be premature to rejoice about the DLI's improvement when the clouds are gathering over Québec.

Consumption Component



Source: Desjardins, Economic Studies

Desjardins Leading Index



Sources: Institut de la statistique du Québec and Desjardins, Economic Studies

CONSUMERS

The tax relief to households stimulated consumer spending at the beginning of 2008. The effect of the GST and tax cuts was short-lived, however; retail sales dipped in February (-0.4%) and March (-3.1%) after January's bounce (+2.8%).

In May, surging gas prices shook consumer confidence. Confidence is closing in on the low point recorded in the fall of 2005, in the wake of hurricanes Katrina and Rita. Prices jumped over \$1.40 a litre for several days, profoundly shaking consumers, who cut their spending on goods. If prices stay at these levels, this behaviour could reoccur.

Keep an eye on developments in the job market, as well. 19,800 jobs were lost in April, and the jobless rate came back up to 7.6%, acting like a cold shower. To date, the Québec economy's resilience has primarily been founded on consumer spending, and there is a very real risk of flagging.

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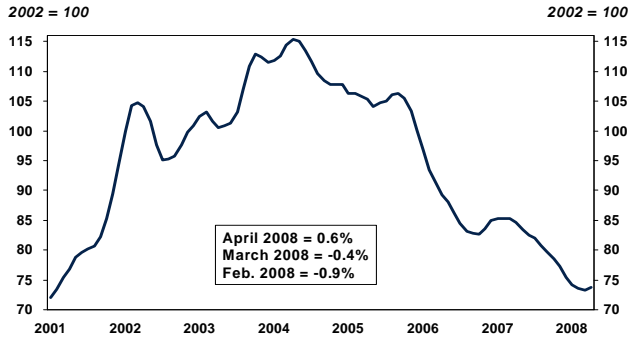
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NOTE TO READERS: The letters **k**, **M** and **B** are used in texts and tables to refer to thousands, millions and billions respectively.

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Housing Component



Source: Desjardins, Economic Studies

HOUSING MARKET

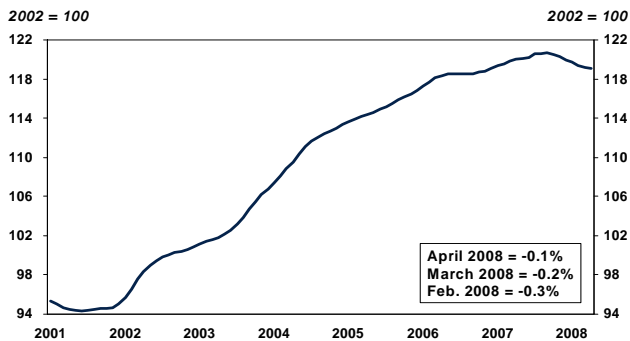
The cut to mortgage rates and strong new construction early this year helped the housing component go up 0.6% in April. This was not enough to turn the down trend around, and the housing sector will flag over the next few months. Starts will dip to 45,000 units this year from 48,533 units in 2007.

Existing home sales are gradually moving off their 2007 peak. In Q1, the number of transactions fell 2.6% from the final quarter of 2007. Even though mortgage rates have come down, buying a home is not very affordable, historically speaking. Relative high prices are helping to make the market moderate, encouraging demand to shift toward less pricey products.

EXPORTS

International goods exports fell 0.2% in real terms from February to March of 2008. The slight dip takes the drop for the first quarter to 6.0% from the same period in 2007.

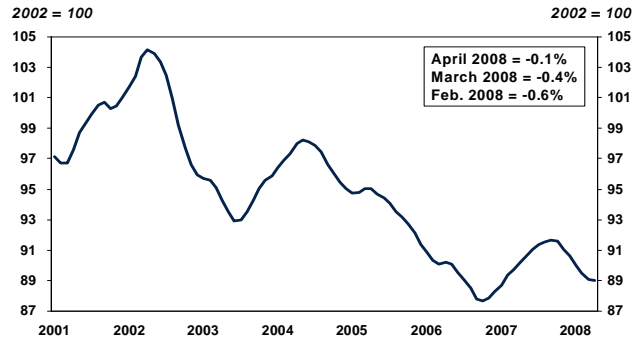
Exports Component



Source: Desjardins, Economic Studies

Although Québec's international exports staved off a tumble in March, thanks to the surge by aerospace, the downward movement is well entrenched. The American economy, which is grappling with a severe slowdown, a dollar close to parity and global competition will keep times tough for exporters.

Financial Component



Source: Desjardins, Economic Studies

FINANCIAL MARKETS

The Québec-30 stock market index got the second quarter off to a positive start, posting a monthly increase of 3.3% in April. The increase helped offset the drop in the DLI's financial component.

The Bank of Canada slashed its key interest rates by 50 basis points on April 22, taking the total reduction since December to 150 basis points. This decision is due to Canada's economic problems, which were confirmed by the first quarter's contraction by real GDP (-0.3% on an annual basis). The drop in economic activity, which could be a first step toward a recession, will encourage the Bank of Canada to lower its key rates further on June 10.

The ongoing monetary easing will help Québec's economy get through this period of uncertainty, though it will not save it from a sharper slowdown. The first quarter will be positive, thanks to January's 0.8% gain in real GDP and February's stability. The slide in consumer confidence and labour market deterioration will now tilt the risks to our economy to the downside.

Hélène Bégin
Senior Economist

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