

# ECONOMIC AND FINANCIAL OUTLOOK

## Through Thick and Thin, the Economy Sails On

By Jimmy Jean, Vice-President, Chief Economist and Strategist

The world remains gripped by major challenges—geopolitical tensions, trade fragmentation, technological disruptions, and polarization—the resolution of which is only just beginning to take shape in some cases. And yet, the global economy refuses to give in. Better still, North American stock markets are showing resilience tinged with sometimes unabashed optimism, as if they had already decided on a future that policymakers themselves cannot seem to pin down.

The economic landscape, however, is far from uniform. While not stalling, growth remains sluggish in most advanced economies, held back by a combination of short-term factors (pressures on purchasing power, uncertainty acting as a tax on industrial investment) and more structural trends (demographic slowdown, high public debt). Energy is driving inflation higher: the four-month conflict in the Middle East has transformed a shipping disruption into a more lasting and rather severe supply shortfall. The June 14 announcement of an agreement to reopen Hormuz caused prices to fall, though not back to pre-conflict levels. Caution remains warranted, as an announced framework is not yet implemented, and the physical restoration of supply will take months, while certain losses (e.g., LNG) will take years to recover. Crucially, however, the shock remains concentrated in the energy sector, without the widespread contagion to supply chains seen in 2022. For now, we are not necessarily seeing a repeat of the post-Ukraine scenario, but depending on how long it takes to return to normal, the risk remains one to watch. Meanwhile, trade uncertainty (led by the fate of CUSMA, and crucially, how much bite it retains) is weighing on investment, particularly in highly exposed sectors and countries, while the enthusiasm for artificial intelligence and technology alone is

driving a disproportionate share of stock market gains and capital expenditures. These narratives are all currently coexisting, without necessarily converging.

Central banks remain caught, to varying degrees, in the uncomfortable trade-off between inflation and growth. In the United States, this dilemma is compounded by a self-inflicted credibility issue: the new Fed chairman, Kevin Warsh, has expressed support for the rate cuts desired by President Trump, even as the US economy remains resilient and inflation is rising. It is true that this resilience stems from more than just demand. Labour productivity there is rising by 2.8% year-over-year, well above the pre-pandemic cycle's pace (around 1.5%), with gains concentrated in sectors with high AI adoption. The status quo, rather than the rate hikes anticipated by markets, could prove to be a defensible balance.

The Bank of Canada faces the inflation-growth dilemma more directly. Core inflation remains under control (core measures are close to target), but the erosion of economic capacity calls for a more nuanced interpretation of the current signs of economic weakness. Keeping the rate at 2.25% is an honest admission of reduced visibility.

In Canada, the situation is all the more complicated because the forces at play result in starkly different regional outlooks. The energy shock is deepening—at least temporarily—the fault lines that were already emerging due to trade uncertainty. Rising energy prices and increased demand from more reliable suppliers are enriching the producing provinces (Alberta, Saskatchewan, Newfoundland) through an oil windfall and improved public

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Jimmy Jean, Vice-President, Chief Economist and Strategist • Randall Bartlett, Deputy Chief Economist • Benoit P. Durocher, Director and Principal Economist  
 Royce Mendes, Managing Director and Head of Macro Strategy • Mirza Shaheryar Baig, Foreign Exchange Strategist  
 Marc-Antoine Dumont, Senior Economist • Tiago Figueiredo, Macro Strategist • Francis Généreux, Lead Economist • Sonny Scarfone, Principal Economist  
 Oskar Stone, Macro Strategy Associate • Hendrix Vachon, Principal Economist • LJ Valencia, Economist  
 Desjardins Economic Studies: 514-281-2336 or 1-866-866-7000, ext. 5552336 • desjardins.economics@desjardins.com • [desjardins.com/economics](https://desjardins.com/economics)

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**BOX****Middle East Conflict: Assumptions**

As anticipated, the United States and Iran appear to have reached a common understanding in June, allowing for the reopening of the Strait of Hormuz, a strategic maritime corridor through which roughly 20% of global oil supply transits. The risk of the agreement collapsing remains, as seen in previous attempts, but markets appear increasingly confident in a lasting resolution to the conflict. A complex logistical operation is now underway, involving the release of more than 800 vessels held in the Persian Gulf and the restart of approximately 15 million barrels per day of production that has been halted since the onset of the conflict. The full extent of war-related damage remains uncertain. As a result, we expect the recovery in Gulf exports and oil production to be more gradual than initially anticipated.

In this context, the price of WTI (West Texas Intermediate) is likely to remain volatile in the short term as the path of global supply becomes clearer. We are therefore maintaining our year-end forecast of US\$80 per barrel.

finance prospects, while Quebec and Ontario are importing inflation without any compensatory growth gains. On the trade front, US pressure is constant, and uncertainty itself is as much a weapon as tariffs, if not more so. There is no indication that this situation will change, whether after the July 1 date for the extension of the CUSMA or after the midterm elections.

Canada's response centres on market diversification, rearmament, and major infrastructure projects. The direction is sound, but the timelines are long and the obstacles significant. There are some purely democratic obstacles, since these projects require trade-offs that institutions take time to resolve, but also resource constraints and the risk of causing crowding-out effects and inflation, if haste leads to poor sequencing of interventions. To quote Thomas Sowell: "There are no solutions, only trade-offs."

Foreign investor interest in Canada appears to be strong, although it is worth noting that it comes mainly from the US and is concentrated primarily in the energy sector. This may not be a coincidence. Elsewhere around the world, what often makes Canada attractive is its access to the US market, the very advantage that current conditions are calling into question. One can no longer sell a gateway to which he no longer holds the key. We therefore need to focus on other strengths to remain attractive, especially since the financing of the US tech build-out is capturing a significant share of global capital. Critical minerals and clean energy are at the forefront of Canada's moat, particularly in Quebec and Ontario, but they cannot replace the need to orchestrate a gain in competitiveness across the entire economy.

What Canada must achieve goes beyond the prevailing self-congratulatory rhetoric: transforming its comparative advantages (clean energy, resources, expertise) into new production capacity,

which requires removing barriers to implementation as much as securing capital. It would be ill-advised to mistake current market optimism for an unconditional vote of confidence in Canada's ability to deliver.

### RISKS INHERENT IN OUR SCENARIOS

The overall geopolitical situation remains difficult, despite a possible resolution of the conflict in the Middle East. The main risk to our scenarios is still that this conflict becomes prolonged or spreads to other countries. Energy prices could be even higher than our central assumption, and supply chains could be further disrupted. Consumer, business and investor confidence may collapse dramatically, which could lead to markedly stronger inflation and subdued economic growth, if not a global recession. Outside the Middle East, tensions remain elevated. Diplomatic and economic relations between the United States and other advanced economies are fragile. While the US Supreme Court struck down some tariffs, the Trump administration is working to replace them, as well as some tariffs that had been temporarily imposed. The threat of new measures is keeping tensions high. Central banks may need to lower their key interest rates if the economy deteriorates more than expected. Conversely, monetary policy may need to be tightened if inflation rises considerably due to spillover from higher energy prices, new tariffs are introduced or supply chain disruptions become more prevalent. Later this year, the focus will also be on the review of the Canada-United States-Mexico Agreement (CUSMA) and the midterm elections, both of which could disrupt the economy. The erosion of institutions in the United States may prompt some global investors to further reduce their exposure to US assets. A sharp correction in the stock market, which has benefited substantially from the AI boom, could shake confidence and trigger a wealth effect shock, while volatility affecting bond, currency and commodity prices could weaken the outlook for the global economy.

**Table 1**  
Global GDP Growth (Adjusted for PPP) and Inflation Rates

%	Weight*	Real GDP growth			Inflation rate		
		2025	2026f	2027f	2025	2026f	2027f
<b>Advanced economies</b>	<b>36.9</b>	<b>1.7</b>	<b>1.4</b>	<b>1.6</b>	<b>2.4</b>	<b>3.0</b>	<b>2.2</b>
United States	14.8	2.1	2.2	2.1	2.7	3.3	2.4
Canada	1.4	1.9	0.6	2.0	2.1	2.6	2.2
<i>Quebec</i>	0.3	0.7	0.3	1.6	2.4	2.6	2.1
Japan	3.2	1.1	0.7	0.9	3.2	2.1	2.2
United Kingdom	2.1	1.4	1.1	1.1	3.4	3.4	2.4
Eurozone	11.5	1.5	0.4	1.2	2.1	3.2	2.1
<i>Germany</i>	3.1	0.3	0.5	1.1	2.2	3.0	2.1
<i>France</i>	2.1	0.9	0.5	1.0	0.9	2.3	1.6
<i>Italy</i>	1.8	0.7	0.7	0.8	1.5	3.1	1.8
Other countries	3.8	1.6	1.7	1.8	2.0	3.0	2.0
<i>Australia</i>	1.0	2.0	1.6	1.7	2.8	4.6	2.8
<b>Emerging and developing economies</b>	<b>63.1</b>	<b>4.4</b>	<b>3.8</b>	<b>4.1</b>	<b>5.1</b>	<b>5.6</b>	<b>4.5</b>
Emerging Asia	33.7	5.6	4.7	4.8	0.9	2.3	2.1
<i>China</i>	19.3	5.1	4.3	4.3	0.1	1.0	1.0
<i>India</i>	8.2	7.7	6.3	6.5	2.2	4.8	4.3
Latin America	5.7	2.1	1.7	2.2	4.2	4.9	3.6
<i>Mexico</i>	1.7	0.5	0.9	1.9	3.8	4.7	3.7
<i>Brazil</i>	2.4	2.6	1.8	1.6	4.8	5.2	3.8
Eastern Europe	8.2	2.2	2.1	2.5	14.1	10.8	8.0
<i>Russia</i>	3.5	1.0	0.9	1.2	8.7	5.5	4.2
Other countries	15.4	3.7	3.7	3.7	12.0	14.0	12.0
<i>South Africa</i>	0.5	1.4	1.3	1.8	3.2	4.0	3.3
<b>World</b>	<b>100.0</b>	<b>3.4</b>	<b>2.9</b>	<b>3.2</b>	<b>4.1</b>	<b>4.7</b>	<b>3.7</b>

f: forecast; PPP: Purchasing Power Parities, exchange rates that equate the cost of a broad basket of goods and services across countries; \* 2024.

World Bank, Consensus Forecasts and Desjardins Economic Studies

## FINANCIAL FORECAST

The Federal Reserve and Bank of Canada are both priced for monetary tightening over the next six months. That said, the Canadian economy remains weak and the spillover from higher oil prices to other goods and services has been limited. Focus is shifting to the ongoing CUSMA negotiations, which present severe downside risks to the economy. Against that backdrop, we don't see the Bank of Canada hiking rates this year. While inflation is higher in the US, the conditions aren't ripe for rate hikes either. The level of interest rates is already elevated and American policymakers will likely prefer to wait out the recent rise in inflationary pressures. Rate differentials have moved further in favour of the US dollar, prompting us to delay our expected appreciation path for the Canadian dollar. Near-term USD strength now appears more likely, particularly if policy divergence is sustained. Equity markets, meanwhile, have absorbed the energy shock with little disruption. Robust US first quarter earnings, particularly in AI-linked sectors, have continued to justify elevated valuations for American equities. In contrast, softer performance in materials (gold) is likely to constrain upside for Canadian indices. Reflecting these dynamics, we now expect the S&P 500 and the TSX to perform broadly in line with each other in 2026.

**Table 2**  
**Summary of Financial Forecasts**

End of period in % (unless otherwise indicated)	2025		2026				2027			
	Q3	Q4	Q1	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
<b>Key interest rate</b>										
United States	4.25	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.50	3.50
Canada	2.50	2.25	2.25	2.25	2.25	2.25	2.25	2.50	2.75	2.75
Eurozone	2.00	2.00	2.00	2.00	2.25	2.25	2.25	2.25	2.25	2.50
United Kingdom	4.00	3.75	3.75	3.75	3.50	3.50	3.50	3.25	3.25	3.25
<b>Federal bonds</b>										
<u>United States</u>										
2-year	3.65	3.49	3.83	4.20	3.85	3.70	3.60	3.55	3.50	3.45
5-year	3.72	3.70	3.94	4.25	4.00	3.85	3.80	3.70	3.70	3.75
10-year	4.13	4.14	4.31	4.45	4.40	4.35	4.35	4.30	4.30	4.35
30-year	4.73	4.84	4.91	4.90	4.95	4.95	4.95	4.90	4.90	4.95
<u>Canada</u>										
2-year	2.47	2.58	2.82	2.75	2.60	2.60	2.70	2.75	2.75	2.75
5-year	2.74	2.96	3.05	3.00	2.85	2.90	2.95	3.00	3.00	3.00
10-year	3.17	3.42	3.46	3.40	3.35	3.40	3.45	3.50	3.50	3.50
30-year	3.61	3.85	3.88	3.80	3.75	3.80	3.80	3.85	3.85	3.85
<b>Currency market</b>										
Canadian dollar (USD/CAD)	1.39	1.37	1.39	1.38	1.39	1.38	1.36	1.35	1.35	1.34
Canadian dollar (CAD/USD)	0.72	0.73	0.72	0.72	0.72	0.72	0.74	0.74	0.74	0.75
Euro (EUR/USD)	1.17	1.18	1.16	1.15	1.15	1.18	1.19	1.20	1.21	1.22
British pound (GBP/USD)	1.33	1.35	1.32	1.28	1.30	1.30	1.32	1.33	1.34	1.35
Yen (USD/JPY)	148	157	159	165	160	155	148	146	143	140
<b>Stock markets (level and growth)*</b>										
United States – S&P 500	6,800 (16.4%)		Target: 7,800 (+14.1%)				Target: 8,800 (+12.5%)			
Canada – S&P/TSX	31,700 (28.2%)		Target: 36,000 (+13.5%)				Target: 40,400 (+12.1%)			
<b>Commodities (annual average)</b>										
WTI oil (US\$/barrel)	76 (60*)		84 (80*)				74 (70*)			
Gold (US\$/ounce)	3,420 (4,100*)		4,790 (5,000*)				5,000 (5,00*)			

f: forecast; WTI: West Texas Intermediate; \* End of year.

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# Overseas

## Global Economic Growth Will Remain Modest in the Near Term

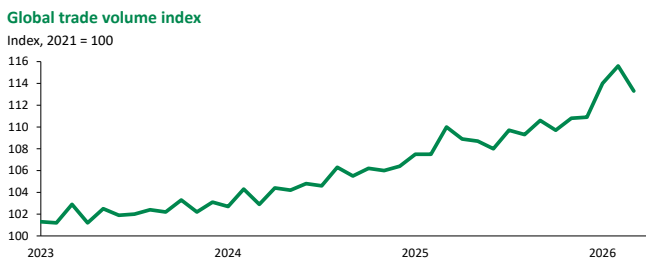
### FORECAST

Although some pockets of weakness have emerged, it is difficult to claim that the global economy materially slowed in early 2026. At the same time, rising energy prices have affected nearly the entire planet. Inflation rates are climbing almost everywhere, and uncertainty is expected to further hinder economic growth. We expect a slowdown to become more evident from the second quarter onwards, and the global economy should be more visibly affected this summer. After gains of 3.4% in 2025, we anticipate growth of 2.9% in 2026 and 3.2% in 2027.

The biggest constraints will once again be higher energy prices, the uncertainty caused by the conflict in Iran and fears about oil supply levels as reserves shrink. Until the war is fully and permanently resolved and ships can pass freely through the Strait of Hormuz, global economic activity will remain under pressure.

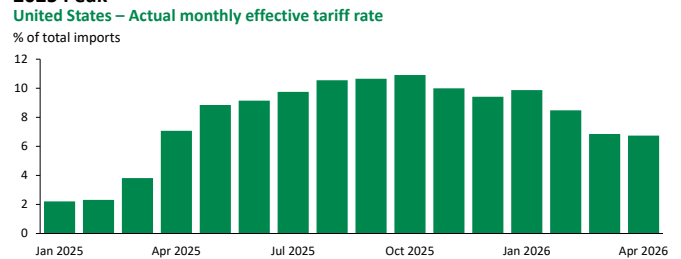
US trade policy will also remain a destabilizing factor, though it seems like international trade flows appear to be adjusting to the shift in dynamics. Despite a decline in March, the volume of goods traded in the first quarter of 2026 increased by 3.5% compared with the previous quarter and by 5.5% year over year (graph 1). Recent trade data from China and the United States do not suggest any recent deterioration. There are several reasons for this growth. First, robust investments in AI, both in the United States and elsewhere, are driving the production and trade of information technology equipment. Second, it appears that countries are adjusting to the tariffs imposed by the United States, with few of them imposing their own permanent barriers to trade. Third, effective US tariff rates have declined significantly since their peak in October 2025 (graph 2). This is in part due to reduced duties on certain products, but the greatest relief came from the US Supreme Court’s decision to strike down the emergency tariffs, which have since been replaced by temporary 10% tariffs. As a result, US import costs have fallen and consequences for foreign producers have been mitigated.

**Graph 1**  
Global Trade Remains Higher than Before the Rise of US Protectionism



CPB - Netherlands Bureau for Economic Policy Analysis and Desjardins Economic Studies

**Graph 2**  
Effective US Tariff Rates Have Declined Significantly from Their 2025 Peak



United States International Trade Commission and Desjardins Economic Studies

It remains to be seen whether Donald Trump’s protectionist impulses re-emerge further down the road. For the time being, our scenarios call for a stable situation that allows trade to continue to grow at a moderate pace.

In the **eurozone**, two elements stand out: the first quarter decline in real GDP and the recent surge in inflation. Real GDP fell 0.2% (non-annualized) over the quarter, its worst result since the start of the pandemic. This performance points to diverging trajectories within the eurozone. Among the major regional economies, France saw its real GDP shrink by 0.1%, while Germany’s real GDP growth accelerated (up 0.3% in the first quarter, after rising 0.2% in Q4 2025). Ireland’s real GDP dropped 12.1%, but this indicator isn’t particularly reliable in that country due to the weight of multinational corporations, especially in the pharmaceutical sector. This abrupt decline clearly weighed on real GDP in the eurozone—without Ireland’s contribution, it would have grown 0.2% instead. All the same, we expect the eurozone’s GDP to grow slowly in the quarters ahead. PMI readings, especially for services, have been down for several months now. Household spending will also need to be monitored, as consumer confidence has declined in response to surging energy prices and weaker real incomes. Medium-term growth will be supported in part by higher military spending by several governments. Inflation hit 3.2% in May, a clear acceleration from two months earlier, when it was still

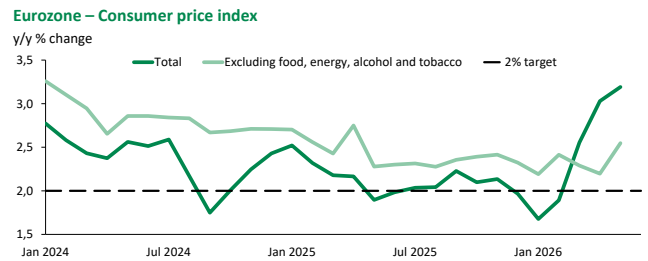
below the European Central Bank’s 2% target (graph 3). The European Central Bank also raised its key rates for the first time since September 2023. As elsewhere in the world, eurozone inflation is expected to slow in tandem with energy prices over the coming months.

We also need to monitor the situation in the **United Kingdom**. The UK recorded the strongest real GDP growth among the G7 countries in Q1 2026, but in April, monthly GDP fell for the first time since August 2025 (graph 4). The May decline in the composite PMI, which fell below 50 for the first time in a year, is also not a good sign. However, the political situation is the most surprising development. Starmer’s government has found itself in a very fragile position, despite the strong Labour Party majority in the House of Commons. Internal struggles could lead to a new government and a new economic program.

In the first quarter, **Japan** posted its best real GDP growth in a year. The gain came primarily from a rally in consumer spending and exports. It remains to be seen whether the momentum will last. Industrial production and the housing sector have faltered recently, and Japanese consumer confidence has been shaken by soaring energy prices. That said, PMIs are holding strong and leading indicators suggest that growth could continue at a solid pace.

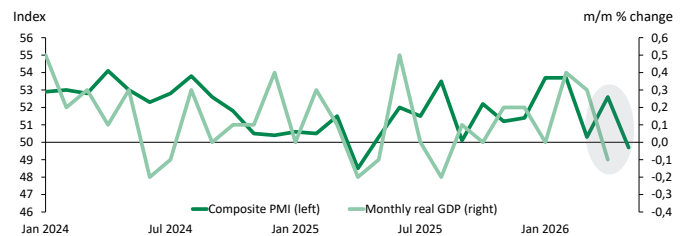
**China’s** Q1 real GDP growth was its strongest quarterly expansion since Q4 2024. That said, the situation was less positive in Q2, particularly for retail sales, reflecting muted domestic demand (graph 5). The property market has yet to recover meaningfully, a situation that has been aggravated by population decline. Fortunately, the Chinese economy continues to benefit from international trade. Exports have continued to grow even though US tariffs remain relatively high (though down from their peak in 2025). After the strong real GDP performance in the first quarter, we expect a bit of a slowdown in the very near term, again due to rising energy prices. We still expect China’s real GDP growth to accelerate starting this fall.

**Graph 3**  
Inflation Has Clearly Accelerated in the Eurozone



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**Graph 4**  
After a Strong Start to the Year, Economic Growth Appears to Be Slowing in the UK



S&P Global, Office for National Statistics and Desjardins Economic Studies

**Graph 5**  
Retail Sales Are Weakening in China



National Bureau of Statistics of China and Desjardins Economic Studies

# United States

## The US Economy Is Once Again Showing Resilience

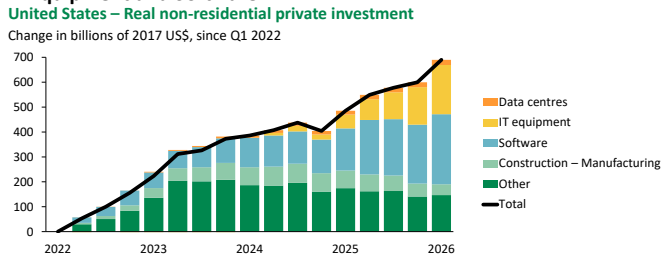
### FORECAST

Despite the challenge posed by higher energy prices, the US economy continues to grow. Real GDP growth is expected to be even stronger in the second quarter than in the first but should slow down slightly thereafter. The artificial intelligence (AI) boom has yet to flag, and it should continue to contribute to investment growth. The labour market has improved in recent months and is expected to remain relatively solid in the coming quarters. According to our base case oil price scenario, US inflation likely peaked in May. Gasoline prices began falling in June, which should also help keep inflation in check.

Annualized real GDP growth accelerated between the last quarter of 2025 (+0.5%) and the first of 2026 (+1.6%). This latest figure seems underwhelming at first glance, since the economy did get a boost from the strong rebound in federal spending after the government shutdown ended last fall. Still, domestic demand increased by an annualized 2.7%, which is one of the best performances we've seen since mid-2024. It was supported by another rise in real investment stemming from the development and deployment of AI. Half of the growth in domestic demand came from investment in technology equipment and software. If real GDP is weaker than demand, it is because these investments have caused imports to pick up.

However, the very strong contributions from the tech sector and AI are masking weaknesses elsewhere in the US economy. Business investments haven't grown outside of these sectors—instead, they've dropped 30% since mid-2024 (graph 6).

**Graph 6**  
For the Past Two Years, Investment Growth Has Depended Entirely on IT Equipment and Software

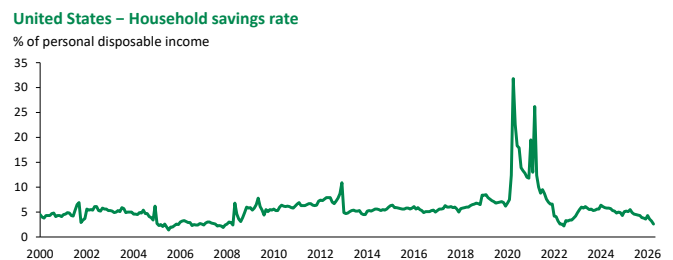


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Real household spending is also faltering, albeit to a lesser extent. In the first quarter, it ticked up an annualized 1.4%, its smallest gain in a year. This underperformance was largely due to a decline in auto sales at the very beginning of the year. The situation has improved in recent months, and real consumer spending rose in March and April, even though the cost of

living was pushed higher by soaring gasoline prices. So while real disposable income for households has fallen 0.6% since February, real spending has gone up 0.4%. This suggests that household consumption is somewhat resilient, in spite of the current circumstances, and that appears to have continued in May, according to retail sales. Households seem to believe that gas prices won't stay this high forever, and in the interim, they're cutting back on savings instead of reducing their expenses. The savings rate dropped to 2.6% in April, its lowest level since June 2022 (graph 7). Before then, you'd have to go back to 2008 to see a savings rate this low. It should also be noted that households have received smaller-than-expected gains from the tax relief measures adopted last year. According to the national accounts, the tax cuts pushed disposable income higher in January, but didn't have much impact in the months that followed.

**Graph 7**  
The Household Savings Rate Has Faltered Recently



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Now, we'll need to see if consumer spending continues to hold up. Household confidence has declined since the start of the war with Iran, but it hasn't dropped as precipitously as feared, given the 56% jump in gasoline prices between mid-February and mid-May. What's more, prices at the pump have been falling over the last month. If this trend continues, consumer confidence should

hold steady or even improve. Sentiment is also being bolstered by the relatively strong stock market performance.

The labour market has also been improving for the last three months, another positive factor. While hiring has been choppy for much of 2025 and early 2026, we've seen more consistent gains since March. In fact, this is the first time in a year that employment has risen for three consecutive months. We expect this new trend to continue in the coming quarters, though at a slightly more moderate pace.

In the quarters ahead, inflation will be largely dictated by energy prices. In our base case scenario, oil and gasoline prices should contribute negatively to month-over-month change in the consumer price index from now on. Year-over-year change should drop below 4% starting in June before gradually sliding to 3%. We don't expect inflation to near the 2% target until spring 2027. The most recent developments in the Middle East are encouraging, but the situation is still uncertain, and energy prices could remain very volatile.

And finally, the Trump administration is still seeking to adjust its trade policy after some tariffs were struck down by the Supreme Court. The 10% tariffs rolled out in late February have

a limited lifespan, in the eyes of the law, but the government is working to replace them with similar tariffs on the grounds that other countries have failed to prevent the import of goods made with forced labour. For now, nothing is really changing. However, other measures could be introduced sooner or later. The outcome of the midterm elections in November could also lead to changes in the Republican administration's economic, budget and trade policies.

**Table 3**  
**United States: Major Economic Indicators**

Quarterly annualized % change (unless otherwise indicated)	2025		2026				Annual average			
	Q3	Q4	Q1	Q2f	Q3f	Q4f	2024	2025	2026f	2027f
<b>Real GDP (2017 US\$)</b>	4.4	0.5	1.6	3.0	1.9	2.1	2.8	2.1	2.2	2.1
Personal consumption expenditures	3.5	1.9	1.4	2.4	1.8	2.1	2.9	2.6	2.1	2.1
Residential construction	-7.1	-1.7	-6.2	1.5	1.5	3.0	3.2	-2.2	-2.5	2.7
Business fixed investment	3.2	2.4	10.1	5.0	5.2	3.3	2.9	4.1	5.6	3.0
Inventory change (2017 US\$B)	-23.9	-15.6	-25.7	7.5	12.5	25.0	43.5	28.5	4.9	36.3
Public expenditures	2.2	-5.6	4.4	2.6	0.4	1.7	3.8	1.1	0.9	1.6
Exports	9.6	-3.2	13.1	7.9	1.9	-0.5	3.6	1.6	5.3	1.6
Imports	-4.4	-1.0	21.1	6.9	3.0	1.7	5.8	2.7	3.6	2.6
Final domestic demand	2.8	0.6	2.7	2.7	2.0	2.2	3.1	2.4	2.2	2.2
<b>Other indicators</b>										
Nominal GDP	8.3	4.2	5.1	6.7	4.6	4.7	5.3	5.0	5.6	4.9
Real disposable personal income	1.0	-0.9	0.8	-2.2	3.2	2.7	2.9	1.7	0.4	2.5
Employment <sup>1</sup>	0.1	-0.2	0.3	1.1	0.8	0.7	1.2	0.5	0.4	0.7
Unemployment rate (%)	4.3	4.5	4.3	4.3	4.3	4.3	4.0	4.3	4.3	4.1
Housing starts <sup>2</sup> (thousands of units)	1,347	1,323	1,418	1,316	1,368	1,373	1,371	1,357	1,369	1,405
Corporate profits <sup>3</sup>	9.3	9.6	12.0	12.5	9.4	4.2	5.1	7.3	9.4	3.9
Personal savings rate (%)	4.4	3.8	3.7	2.7	3.0	3.1	5.5	4.6	3.1	3.4
Total inflation rate*	2.9	2.8	2.7	3.9	3.4	3.2	3.0	2.7	3.3	2.4
Core inflation rate* <sup>4</sup>	3.1	2.8	2.5	2.8	2.6	2.7	3.4	2.9	2.7	2.4
Current account balance (US\$B)	-957	-763	-838	-847	-859	-875	-1,185	-1,116	-855	-897

f: forecast; \* Annual change; <sup>1</sup> According to the establishment survey; <sup>2</sup> Annualized basis; <sup>3</sup> Before taxes; <sup>4</sup> Excluding food and energy.

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# Canada

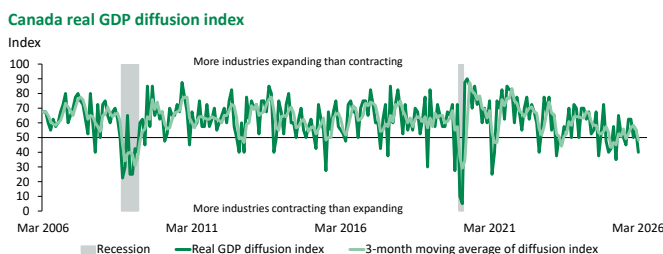
## We're Halfway There, But the Outlook's Still Up in the Air

### FORECAST

Canada's economy contracted by 0.1% annualized in Q1 2026, underperforming both private-sector and Bank of Canada expectations, despite solid household consumption. Near-term growth should improve as consumption and private investment provide support. Higher oil prices, resulting of the fallout of the Iran conflict, are expected to lift energy investment and exports as well as national income, although energy production and transportation constraints persist. At the same time, stronger energy prices continue to push up the inflation outlook. Trade risks also remain, with expanded US metal tariffs and uncertainty surrounding the CUSMA review weighing on the forecast. Slower population growth remains another key headwind. However, fiscal policy should provide offsetting support through tax relief, defence and infrastructure spending, and household transfers. Overall, consumption and government spending are expected to exceed the Bank of Canada's April projection. Despite our more positive growth outlook and higher inflation forecast, we expect the Bank to remain on hold until 2027.

Canada's economy contracted by 0.1% q/q annualized in Q1 2026, coming in well below the private-sector consensus and Bank of Canada's expectations of 1.5% growth. While this is the second consecutive quarterly decline in real GDP, we don't believe the Canadian economy was in a recession to start the year. That's because the weakness was concentrated in a small number of sectors (graph 8). To call a recession, weakness must be broad based throughout the economy. Moreover, despite final domestic demand contracting in Q1 (-0.4%), household consumption growth was solid again in Q1 (1.5%)—further evidence that Canada was not in a recession recently.

**Graph 8**  
Real GDP Weakness Is Not Broad Based Enough Yet to Call a Recession



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Looking to Q2 2026, consumption is likely to contribute positively to growth, especially as [job numbers](#) saw sizeable gains in May. The federal government transferred a one-time \$3.1B to low- and middle-income households on June 5, although much of this should be felt in Q3 as it came late in the quarter. Private investment will probably rebound on the back of renewed residential and non-residential investment. Trade and inventories

remain wildcards, although early indications suggest that [trade](#) is likely to boost Q2 output growth as well.

Looking at the rest of 2026, despite a possible resolution of the conflict in the Middle East, oil prices will likely remain elevated. This should support greater investment in the energy sector, oil exports and incomes in resource-rich provinces. That said, Canada's energy industry faces constraints on production and transportation, which may limit gains from elevated oil prices. While economic momentum should improve, it is also expected to come with stronger inflationary pressures. In particular, our gasoline price outlook has been revised upward, leading to a higher inflation outlook in 2026.

At the same time, fiscal policy is expected to provide meaningful support to the outlook. At the federal level, the [Spring Economic Update](#) pointed to sustained large deficits and increased borrowing to finance tax relief and spending initiatives aimed at strengthening investment and productivity. Growth should also be supported by rising defence spending tied to NATO commitments, alongside continued infrastructure investment. Similarly, [higher budget deficits in many provinces](#) are expected to sustain stronger government spending growth, reflecting elevated operating and capital expenditures. At the same time, federal fiscal transfers to households are likely to support consumption by cushioning disposable incomes. As a result, our outlook for both household consumption and government spending is stronger than the Bank of Canada's [April 2026 Monetary Policy Report](#) projection.

That said, the outlook remains subject to several important headwinds. First is US trade policy. Although the removal of the IEEPA tariffs in early 2026 was welcome news, it has been somewhat offset by the more recent expansion of metal-related tariffs. We've estimated that the average effective tariff rate on US imports from Canada should be roughly

0.1 percentage points higher than in our prior outlook, at around 3.7%, assuming current sector-specific tariffs hold. That said, uncertainty around the outcome of the [CUSMA joint review](#) on July 1, 2026, remains a significant downside risk. Second, [slowing population growth](#) is expected to weigh on labour supply growth and Canada's aging labour force. Given these downside risks to the forecast, [we continue to expect](#) the Bank of Canada to stay on the sidelines until 2027.

**Table 4**  
**Canada: Major Economic Indicators**

Quarterly annualized % change (unless otherwise indicated)	2025		2026				Annual average			
	Q3	Q4	Q1	Q2f	Q3f	Q4f	2024	2025	2026f	2027f
<b>Real GDP (2017 \$)</b>	<b>1.9</b>	<b>-1.0</b>	<b>-0.1</b>	<b>1.5</b>	<b>2.4</b>	<b>1.9</b>	<b>2.0</b>	<b>1.9</b>	<b>0.6</b>	<b>2.0</b>
Final consumption expenditure [of which:]	-1.1	2.7	0.7	1.7	2.5	1.9	2.6	2.4	1.6	2.1
<i>Household consumption expenditure</i>	-0.8	2.9	1.5	1.5	2.5	1.5	2.2	2.4	1.8	1.8
<i>Government consumption expenditure</i>	-2.1	2.3	-1.0	2.6	2.7	2.8	3.8	2.4	1.2	2.8
Gross fixed capital formation [of which:]	1.6	2.8	-4.3	2.0	2.6	3.1	0.7	1.6	0.6	3.1
<i>Residential structures</i>	4.4	-9.4	-7.9	1.8	2.7	3.6	-0.2	0.5	-2.4	2.9
<i>Non-residential structures</i>	-0.9	-1.1	-10.2	1.8	2.7	3.0	-1.7	1.7	-1.6	3.5
<i>Machinery and equipment</i>	-14.2	8.7	10.2	0.8	1.3	1.7	-1.0	-2.4	1.4	2.2
<i>Intellectual property products</i>	-2.0	9.4	13.8	1.9	1.9	1.9	2.2	0.4	5.3	2.1
<i>Government gross fixed capital formation</i>	15.5	24.6	-9.6	3.8	3.8	4.0	6.1	7.2	5.5	4.1
Investment in inventories (2017 \$B)	13.7	-12.6	10.6	8.8	7.4	5.3	6.5	7.4	8.0	3.1
Exports	4.1	6.7	-0.5	3.0	4.0	4.2	0.9	-1.4	1.2	3.4
Imports	-10.9	2.0	12.0	2.8	3.4	3.6	0.7	-0.3	3.0	3.3
Final domestic demand	-0.5	2.7	-0.4	1.8	2.5	2.2	2.2	2.2	1.3	2.3
<b>Other indicators</b>										
Nominal GDP	6.3	3.0	4.6	7.7	4.5	3.7	4.8	4.4	4.6	4.0
Real disposable personal income	-0.3	-0.7	0.1	4.6	1.0	1.5	4.8	1.5	0.9	1.9
Employment	0.0	2.4	-1.0	0.1	0.1	0.6	1.9	1.4	0.3	0.6
Unemployment rate (%)	7.0	6.7	6.6	6.8	6.8	6.7	6.4	6.8	6.7	6.6
Housing starts <sup>1</sup> (thousands of units)	273	255	242	265	253	253	245	259	253	254
Corporate profits* <sup>2</sup>	6.6	4.5	5.3	13.7	10.5	8.7	-2.3	6.2	9.5	3.8
Personal savings rate (%)	4.4	3.7	3.5	4.2	3.8	3.8	5.0	4.4	3.8	3.9
Total inflation rate*	2.0	2.2	2.2	3.0	2.9	2.5	2.4	2.1	2.6	2.2
Core inflation rate* <sup>3</sup>	2.5	2.5	2.1	1.6	1.9	1.8	2.6	2.5	1.9	2.3
Current account balance (\$B)	-5.1	-1.0	-7.2	-8.2	-9.8	-10.0	-15.0	-30.8	-35.1	-42.9

f: forecast; \* Annual change; <sup>1</sup> Annualized basis; <sup>2</sup> Before taxes; <sup>3</sup> Excluding food and energy.  
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# Quebec

## Mixed Signals, More Widespread Weakness

### FORECAST

Following a marked slowdown in 2025, recent data point to uneven economic activity in Quebec in early 2026. The rebound in industrial production should be treated with caution, as inventories remain high and international demand has yet to recover. Current economic conditions aren't strong enough to regain the momentum lost since the start of the trade crisis. Weakness in the goods sector, a more widespread slowdown across industries, a declining working-age population and soft exports all point to limited growth in the near term. Given these circumstances and despite the downward revision of outlooks for Canada as a whole, Quebec's economy should continue to lag behind the national average.

Recent data offer some encouragement, but improvements may be fragile. After a prolonged period of stagnation, real GDP by industry posted its strongest monthly increase in over a year in February. This [rebound](#) should be viewed with caution, though: despite relatively resilient domestic demand, the Canadian economy surprised to the downside in the first quarter. And activity is still below the peak recorded in early 2025. We may just be seeing some catch-up, not a genuine turning point.

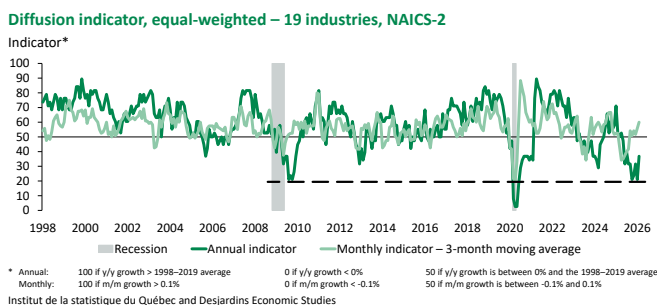
This interpretation would be in line with our projections. Quebec is expected to post one of the slowest growth rates in the country in 2026, if not the slowest, before gradually improving in 2027. All the same, we expect it to lag behind the national average. Even though we've downgraded our forecasts for Canada as a whole, Quebec should still underperform, suggesting there is a structural element to these results.

The industry-by-industry breakdown remains concerning. Since January 2025, goods output has contracted sharply, particularly in manufacturing and construction. While some services-producing industries have advanced, and despite positive contributions from both finance and insurance and wholesale and retail trade, this isn't enough to make up for the ground lost. Weakness is now more widespread, as signalled by the diffusion indicators (graph 9).

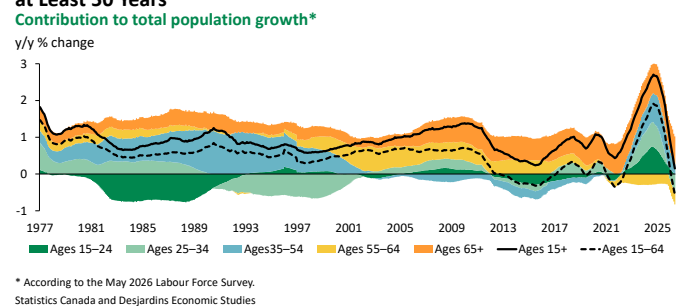
The labour market is also sending mixed signals. [Recent data is volatile](#), alternating between job losses and gains. While the unemployment rate is staying relatively low, this is in part because the labour force participation rate has pulled back. Hours worked also declined year-over-year, a sign of weaker demand that contrasts with the stronger results seen across Canada. Overall, this suggests that employment will gradually hit a ceiling, rather than falling dramatically.

These cyclical factors are being compounded by growing demographic constraints. The working-age population is down 0.6% year-over-year, an unprecedented decline, even during the pandemic (graph 10). This contraction is the result of both slower demographic growth and the aging population. This will directly limit the available workforce and, by extension, growth potential. Public investments planned by the Quebec government, particularly in infrastructure, should lend some support to economic activity, but will not fully offset these headwinds.

**Graph 9**  
Weakness Is Now Widespread

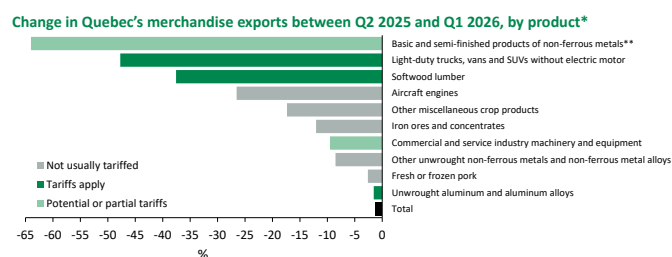


**Graph 10**  
The Working-Age Population Is Experiencing Its Largest Contraction in at Least 50 Years



The external sector is another weak link, consistent with the contraction in the manufacturing sector. Quebec exports have pulled back sharply in recent months, particularly for products subject to US import tariffs (graph 11 on page 12). The decreases

**Graph 11**  
**Quebec Export Volumes of Tariffed Products Are Down Sharply**



\* In constant 2017 \$, seasonally adjusted data – products with negative growth (among the top 20 exported products in 2025, excluding special transactions); \*\* Includes copper wire, which has been subject to tariffs since August.  
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observed for metals and some manufactured goods show how sensitive Quebec's economy is to trade tensions. Foreign demand remains uncertain, so we can expect this fragility to persist in the short term.

Finally, Quebec is not benefiting from higher energy prices, unlike other resource-rich provinces. Instead, these prices are raising costs for consumers and businesses alike and depriving the economy of a growth driver, ultimately [widening the performance gap](#) with the rest of Canada.

Overall, despite some firming in the short term, underlying growth fundamentals remain fragile. The combination of broad sectoral weakness, demographic constraints and an uncertain external environment should keep Quebec's growth below that of Canada.

**Table 5**  
**Quebec: Major Economic Indicators**

Annual average % change (unless otherwise indicated)	2023	2024	2025	2026f	2027f
<b>Real GDP (2017 \$)</b>	<b>0.7</b>	<b>1.7</b>	<b>0.7</b>	<b>0.3</b>	<b>1.6</b>
Final consumption expenditure [of which:]	1.4	2.7	1.8	1.1	0.8
Household consumption expenditure	1.9	2.5	1.6	0.8	1.3
Government consumption expenditure	0.2	3.2	1.9	1.8	-0.1
Gross fixed capital formation [of which:]	-2.9	4.4	1.8	0.8	1.7
Residential structures	-14.6	5.9	7.6	-0.3	1.1
Non-residential structures	4.8	9.4	2.0	1.1	2.7
Machinery and equipment	-3.2	3.6	-4.7	-1.3	2.5
Intellectual property products	5.4	2.6	1.1	2.5	1.9
Government gross fixed capital formation	8.8	-1.0	-2.2	2.8	1.1
Investment in inventories (2017 \$B)	4.5	1.2	0.0	1.1	0.3
Exports	3.9	0.5	-0.9	-0.3	3.3
Imports	0.6	1.8	0.9	1.2	2.4
Final domestic demand	0.5	3.1	1.8	1.1	1.0
<b>Other indicators</b>					
Nominal GDP	4.7	5.9	4.7	3.5	3.8
Real disposable personal income	0.1	4.3	1.6	0.2	1.0
Weekly earnings	3.6	4.5	4.1	2.7	3.1
Employment	2.9	0.9	1.7	-0.6	0.6
Unemployment rate (%)	4.5	5.3	5.6	5.7	5.3
Personal savings rate (%)	6.3	8.3	8.2	7.4	7.4
Retail sales	3.7	2.1	3.4	3.5	2.9
Housing starts <sup>1</sup> (thousands of units)	38.9	48.7	59.9	61.7	61.9
Total inflation rate	4.5	2.3	2.4	2.6	2.1

f: forecast; <sup>1</sup> Annualized basis.

Statistics Canada, Institut de la statistique du Québec, Canada Mortgage and Housing Corporation and Desjardins Economic Studies

## Medium-Term Forecast

# Will the US Productivity Gains from Artificial Intelligence Be Replicated Elsewhere?

The United States is a global leader in developing and deploying artificial intelligence (AI), and its economy is reaping the benefits, mainly in the form of productivity gains. Assuming the current momentum continues, we expect economic growth of around 2% per year for the United States in the medium term. Many countries have been slow to adopt this new technology, including Canada. We do not believe this delay will be made up quickly. We are forecasting economic growth of around 1.8% in Canada in the medium term, even though the country has significant untapped investment potential in several sectors. Population growth should also ramp back up in the medium term, contributing more to economic growth than it is right now. However, we do expect this to vary from region to region. For example, population growth should be slower in Quebec, keeping economic growth under 1.5% in the medium term.

### Finding the Right Balance Between Artificial and Human Intelligence

The rise of AI is undeniably giving a boost to the US economy, but it has also brought its share of challenges, particularly for the labour market. Job creation has slowed. Young skilled workers are having more difficulty finding employment. If AI is deployed too rapidly, more jobs could be eliminated, which would then drag on spending growth. However, we have not included this assumption in our medium-term forecasts.

Instead, we believe that AI will be adopted at a pace that allows for new positions to be created for deskilled workers. Programs to support continuing education and reskilling would be particularly beneficial. But AI can do more than just replace workers; it can also improve their productivity, making employees more efficient and therefore more profitable for companies. From this angle, it's not merely a question of which roles can be automated. Rather, it's an opportunity to create a symbiotic relationship between artificial intelligence and human intelligence. We can expect to see a number of roles transform in the years ahead, much as we did in the 1990s, when the Internet was made publicly accessible.

### AI Isn't the Only Area with Investment Potential

Looking past artificial intelligence, there are a number of other sectors that could support growth in the medium term. The energy sector, for example, must expand to meet rapidly growing demand. While some of this increased demand is linked to the AI boom, a large part of it also comes from the energy transition

and electrification of transport. The mining sector will also need to increase its investments to supply the new value chains that are emerging. Significant investments are also expected in the weapons industry. Geopolitical tensions are heightened and many governments are looking to increase their military budgets.

Given our labour and capital constraints, it's highly unlikely that we'll be able to carry out every project under consideration. After the 2008–2009 financial crisis, demand for credit shrank considerably, which helped keep interest rates low. Those days are well and truly over. The anticipated increase in funding needs will keep interest rates higher.

### Global Trade Dynamics Will Continue to Evolve

Trade flows are still quite volatile, as they have been since the US began imposing new tariffs in 2025. Our medium-term forecasts do not call for any major changes to the tariffs currently in place. We also expect the Canada-United States-Mexico Agreement (CUSMA) to be renewed.

All the same, many companies will continue to diversify their export markets. At the same time, we could see regional trading blocs strengthen, at the expense of a single large global economy. There also seems to be a desire to strengthen ties among like-minded allies with shared social, economic, and democratic values.

The downside to this reorganization of global trade is higher costs. Businesses will need to reallocate capital to develop these new supply chains. And further fragmenting the global economy will reduce the potential gains from globalization. In the end, these obstacles should limit the pace of trade diversification. Our medium-term forecasts suggest only moderate potential on this front.

**Table 6**  
**Major Medium-Term Economic and Financial Indicators**

% (unless otherwise indicated)	Annual average							Averages	
	2024	2025	2026f	2027f	2028f	2029f	2030f	2021–2025	2026–2030f
<b>United States</b>									
Real GDP (% change)	2.8	2.1	2.2	2.1	2.2	2.2	2.0	3.3	2.1
Total inflation rate (% change)	3.0	2.7	3.3	2.4	2.0	2.2	2.0	4.5	2.4
Unemployment rate	4.0	4.3	4.3	4.1	4.0	3.9	3.9	4.2	4.0
S&P 500 index (% change) <sup>1</sup>	23.3	16.4	14.1	12.5	9.5	9.0	9.0	14.3	10.8
Federal funds rate	5.31	4.37	3.75	3.63	3.50	3.50	3.50	3.40	3.58
Prime rate	8.31	7.37	6.75	6.63	6.50	6.50	6.50	6.40	6.58
Treasury bills – 3-month	5.18	4.21	3.64	3.45	3.35	3.35	3.35	3.36	3.43
Federal bonds – 10-year	4.21	4.28	4.38	4.33	4.40	4.40	4.40	3.37	4.38
– 30-year	4.41	4.78	4.93	4.93	5.00	5.00	5.00	3.69	4.97
WTI oil (US\$/barrel)	77	77	84	74	70	70	70	79	74
Gold (US\$/ounce)	2,385	3,440	4,790	5,000	4,875	4,900	4,900	2,274	4,893
<b>Canada</b>									
Real GDP (% change)	2.0	1.9	0.6	2.0	1.9	1.8	1.7	2.6	1.6
Total inflation rate (% change)	2.4	2.1	2.6	2.2	2.0	2.0	2.0	3.7	2.2
Employment (% change)	1.9	1.4	0.3	0.6	0.9	1.1	1.3	3.1	0.8
Employment (thousands)	386	296	61	131	194	242	276	255	181
Unemployment rate	6.4	6.8	6.7	6.6	6.5	6.4	6.2	6.3	6.5
Housing starts (thousands of units)	245	259	253	254	252	261	268	257	258
S&P/TSX index (% change) <sup>1</sup>	18.0	28.2	13.5	12.1	9.2	8.0	8.0	13.5	10.2
Exchange rate (US\$/C\$)	0.73	0.72	0.72	0.74	0.77	0.80	0.80	0.75	0.77
Overnight rate	4.59	2.95	2.25	2.56	2.75	2.75	2.75	2.90	2.61
Prime rate	6.75	4.90	4.45	4.76	4.95	4.95	4.95	5.04	4.81
Mortgage rate – 1-year	7.64	6.30	5.55	5.20	5.10	5.10	5.10	5.66	5.21
– 5-year	6.73	6.23	5.75	5.60	5.40	5.40	5.40	6.01	5.51
Treasury bills – 3-month	4.37	2.58	2.25	2.63	2.75	2.75	2.75	2.80	2.63
Federal bonds – 2-year	3.67	2.61	2.69	2.74	2.80	2.80	2.80	2.79	2.77
– 5-year	3.30	2.83	2.95	2.99	3.00	3.00	3.00	2.69	2.99
– 10-year	3.34	3.24	3.40	3.49	3.50	3.50	3.50	2.81	3.48
– 30-year	3.33	3.57	3.81	3.84	3.85	3.85	3.85	2.97	3.84
<b>Yield spreads (Canada–United States)</b>									
Treasury bills – 3-month	-0.81	-1.63	-1.39	-0.82	-0.60	-0.60	-0.60	-0.57	-0.80
Federal bonds – 10-year	-0.87	-1.04	-0.98	-0.84	-0.90	-0.90	-0.90	-0.55	-0.90
– 30-year	-1.08	-1.21	-1.12	-1.09	-1.15	-1.15	-1.15	-0.72	-1.13
<b>Quebec</b>									
Real GDP (% change)	1.7	0.7	0.3	1.6	1.5	1.4	1.3	3.0	1.2
Total inflation rate (% change)	2.3	2.4	2.6	2.1	2.0	2.0	2.0	3.9	2.1
Employment (% change)	0.9	1.7	-0.6	0.6	0.5	0.5	0.5	2.6	0.3
Employment (thousands)	41	78	-30	28	24	24	25	111	14
Unemployment rate	5.3	5.6	5.7	5.3	5.0	4.8	4.6	5.2	5.1
Retail sales (% change)	2.1	3.4	3.5	2.9	2.5	2.6	2.6	6.6	2.8
Housing starts (thousands of units)	49	60	62	62	62	62	64	55	62

f: forecast; WTI: West Texas Intermediate; <sup>1</sup> Changes are based on end-of-period data.

Datastream, Statistics Canada, Canada Mortgage and Housing Corporation, Institut de la statistique du Québec and Desjardins Economic Studies