ECONOMIC VIEWPOINT

Desjardins Provincial Outlook:

A Housing vs. Commodities Rematch in 2024

By Marc Desormeaux, Principal Economist

Summary

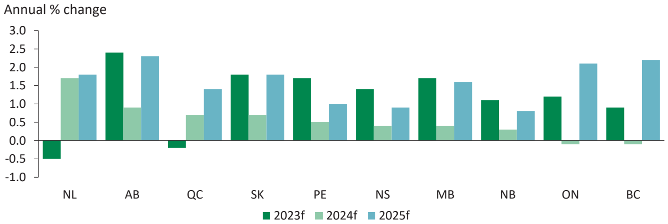
- Our core view has not changed: the Canadian provinces most exposed to housing and other interest-rate-sensitive sectors will feel the coming economic downturn most acutely, whereas commodity producers will be less vulnerable. We think this contrast will become starker in 2024.
- We also still think almost all regions of Canada will experience slowdowns in 2024 in response to sharply higher borrowing costs and weaker expansions among our trading partners. Later this year, rate cuts should help the economy rebound.
- Following an oil sands maintenance period last year, the strong late-2023 handoff for crude production should support economic growth in Alberta in 2024.
- The fiscal environment has become more challenging in several provinces, but fiscal policy could be more stimulative than previously anticipated this year.
- Amid decades-high population growth, it's become clearer that declining GDP per capita—and by extension a lower standard of living—is a problem across the provinces. Outside Quebec, Ontario and BC, the downward trend in per-person output during the last several years is particularly striking.

OVERVIEW

Housing vs. Commodities, Round 2

We still think the provinces most exposed to housing and other interest-rate-sensitive sectors will feel the coming economic downturn most acutely, whereas commodity producers will be less vulnerable (graph 1). But even now, we still haven't felt the full effects of previous rate hikes. As such, we think almost all regions of Canada will experience slowdowns in 2024 as a result of sharply higher borrowing costs and weaker expansions among our trading partners. Towards the end of this year, we expect rate cuts to spark an economic rebound that will continue into 2025.

Graph 1
Oil-Producing Provinces Will Avoid the Worst of the 2024 Downturn



f: forecast
Statistics Canada, Institut de la Statitique du Québec, Ontario Ministry of Finance and Desjardins Economic Studies

When the Facts Change…

We did have to update some provincial growth projections based on recently released data, however. Even though Q3 was particularly weak outside Quebec and Ontario, information released since then suggests a bounce-back in economic activity in the fourth quarter, especially in Alberta. Those handoffs—following port and oil sands disruptions—should help headline growth rates for Alberta and BC in 2024. And while Ontario's GDP gains continue to beat the national average, we see signs of weakness for the coming quarters. Finally, we've revised Quebec's growth forecast meaningfully higher for the year 2024. This largely reflects a bounceback effect, as the public-sector workers that were on strike at the end of 2023 returned to work in January.

At the time of writing, many local housing markets also look to be rallying entering 2024. Softening economic activity should weigh on housing demand in the months ahead, but if buyers flood the market in anticipation of falling bond and mortgage rates, that could prompt further forecast tweaks next quarter.

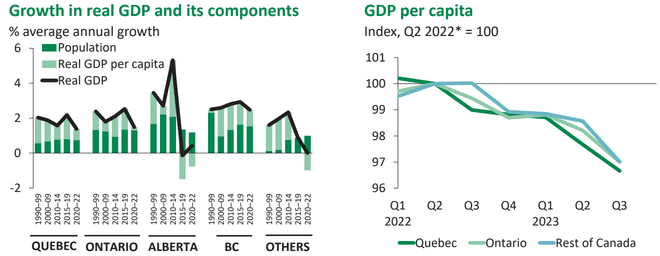
Surging Population, Falling GDP per Capita

Population-induced support for headline economic growth has continued to mask deeper weakness since our last outlook. GDP per capita is a broad measure of economic wellbeing, and it fell again in the third quarter. Diminished contributions from productivity growth represent a longstanding trend across Canada's provinces, but the recent pace of per-person output declines is approaching rates previously recorded only during recessions (graph 2). We don't see much opportunity for improvement soon. Even before the recent cap on international students was announced, we thought Canada's non-permanent resident (NPR)-fuelled headcount surge would cool. That cooling could exacerbate the slowdown in provinces like Quebec, Ontario and BC where NPRs have contributed to a significant share of the demographic expansion. But absent bigger contributions from oil and gas sector investment—the traditional driver of Canadian productivity gains—productivity growth should remain elusive in the shorter term. We think this industry will support Canadian expansion in the coming years, but not return to early-2010s highs. This call is in line with Alberta government and Alberta Energy Regulator forecasts.

The Fiscal Environment Is Challenging, but Policy Could Become More Stimulative

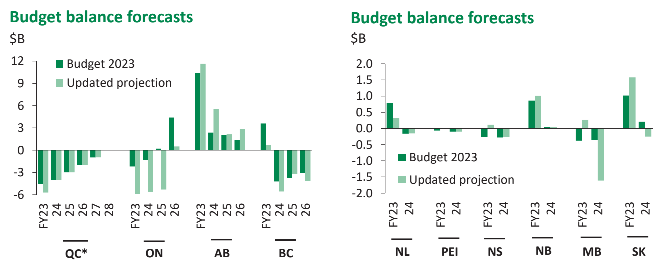
Although many provinces projected worse-than-previously-anticipated fiscal prospects in their fall 2023 updates (graph 3, read our coverage here), that has mixed implications for economic growth. On the one hand, there's less of a buffer entering the upcoming period of economic weakness, and some plans for tax and fee relief could be put on hold. That smaller buffer occurs amid an already challenging fiscal environment where, in many cases, growth in government spending is expected to lag the rate of population expansion.

Graph 2
The Population Boom Continues to Mask Economic Gloom



* Peak for national-level GDP per capita
Statistics Canada, Institut de la Statitique du Québec, Ontario Ministry of Finance and Desjardins Economic Studies

Graph 3
Provincial Budget Balances Are Expected to Be Worse



* After deposits into the Generations Fund
Provincial budget documents and Desjardins Economic Studies

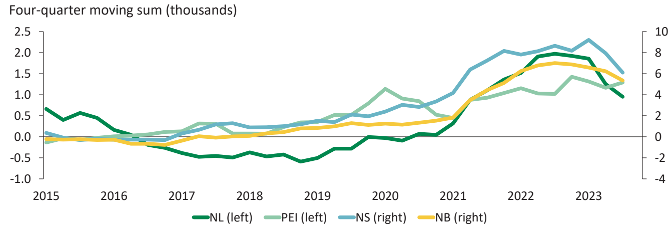
But tax cuts are still on the table in some regions. Moreover, the start of delayed infrastructure projects and increases to some provincial capital plans could help the expansion this year.

ATLANTIC CANADA

Population growth will continue to anchor the Atlantic Region's economic prospects, and the outlook on this front is mixed. On the one hand, relative to other regions in Canada, all four Atlantic provinces have little dependence on non-permanent residents as a source of headcount gains. That means less risk that falling NPR admissions will amplify the economic slowdown as the labour market cools. Yet interprovincial migration from Ontario—a key source of growth during the pandemic—continues to decline as remote work arrangements become less common (graph 4).

Graph 4
Migration from Ontario to Atlantic Canada Has Peaked

Net interprovincial migration from Ontario*

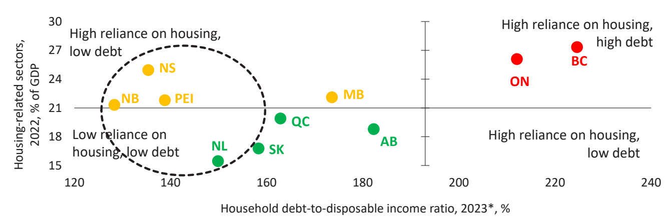


* Positive indicates net inflow from Ontario, negative indicates net outflow to Ontario
Statistics Canada and Desjardins Economic Studies

The good news for Atlantic Canada is that its households are far less indebted than those elsewhere in the country (graph 5). That means the impact of higher interest rates isn't likely to be as severe as in some other provinces.

Graph 5
Low Household Indebtedness Serves Atlantic Canada Well as Rate Hikes Bite

Household indebtedness and housing exposure by province



* Based on Q1 and Q2 data
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As always, Newfoundland and Labrador's economic trajectory is dominated by oil production. Accounting for about 20% of output on The Rock in 2022—more than in any other province—oil production is set to rise significantly in 2024 with the Terra Nova offshore field on track to return to full production after a multi-year shutdown. Alongside support from capital outlays on various other mining sector projects, that should lift our easternmost province's expansion to the top of the provincial growth table this year. Meanwhile the hydrogen industry presents long-run growth potential for the province.

Perhaps the most significant development in Prince Edward Island since our last outlook was another boost to infrastructure spending plans. The government now projects a 15% increase in outlays this fiscal year—versus a prior forecast of just 2%—which should complement still-strong population gains. Trade prospects are less positive considering our expectations of softer US and Chinese growth in 2024. External shipments also won't get the same boost from the end of an American ban on potato exports this year. And tourism spending should be hurt by still-high interest rates and inflation.

In Nova Scotia (NS), construction activity will be key. Though not immune to the drag from higher interest rates, elevated input costs and labour shortages, housing starts and residential building investment proved resilient, especially at the end of 2023. An ambitious capital plan—so far on track to reach the total spend projected in early 2023— should lift non-residential construction activity going forward. One question is whether we'll see meaningful job losses in rate-sensitive financial services or tech, for which NS is a regional hub. So far, there is little evidence of that.

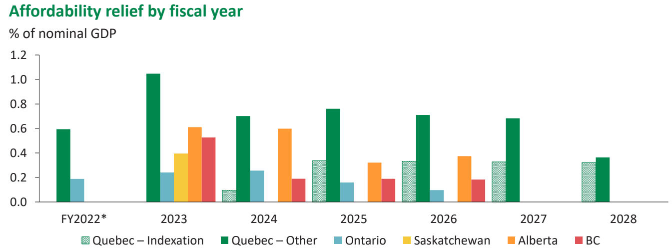
New Brunswick's (NB) economy stands out within Atlantic Canada for its reliance on commodities. With the Saint John refinery—Canada's largest—under strategic review, prospects for exports of staple petroleum products are muted. However, following last year's decline, our forecast for greater stability in crude values bodes well for the sector's growth. The same goes for US housing starts and the province's lumber industry. NB's fiscal position remains an area of strength—the province kept the books balanced throughout the pandemic—and plans to boost infrastructure spending should blunt the effects of the coming economic slowdown.

QUEBEC

Following last year's so-called "technical recession," Quebec's economy finds itself at the intersection of multiple forces that should propel stronger-than-average growth in 2024. Unlike in Ontario and BC where many housing projects were financed before rates and economic growth became less supportive, residential investment in Quebec was immediately hit by higher borrowing costs last year. Weakness in late 2023 provided a weak handoff for Q1 2024, but we also anticipate stronger homebuilding activity in Quebec than in those other jurisdictions this year. Hydroelectricity exports are an important piece of Quebec's trade profile. They were down in 2023 due to poor weather, but should rebound this year. Perhaps most significantly, return to work following public sector labour negotiations should support growth in the first half of this year. That said, population growth in Quebec has lagged that of most other provinces, a trend we expect to continue in 2024.

While *La Belle Province* certainly won't be immune to the effects of still-high interest rates, its households start the year with some advantages. A still-tight job market should limit layoffs as the Canadian economy undergoes a mild recession early in 2024. That looks to have supported modest gains in household consumption, even under the weight of sharply higher borrowing costs. Affordability measures implemented by the provincial government—by far the most generous in any Canadian region (graph 6)—have also helped and should continue to provide spending room going forward.

Graph 6
Quebec Has Offered Plenty of Fiscal Support for Households



* FY: fiscal year
Finance Canada, provincial budget documents and Desjardins Economic Studies

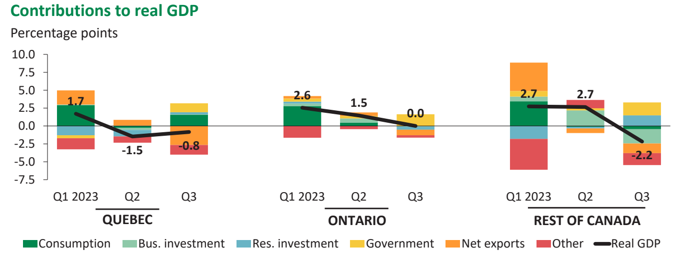
ONTARIO

Another quarter, another GDP outperformance in Canada's largest province. Ontario's flat real GDP print in Q3 2023 beat the 1.5% national decline, with support from government spending and non-residential investment activity (graph 7). Nominal GDP growth was also tracking higher than assumed in the November 2023 budget update, setting up better-than-forecast tax revenues this fiscal year.

But there were many signs of weakness in the data as well. Despite surging population growth, household consumption fell, which is unusual outside recessions. At the same time, residential investment plunged. Both components should continue to struggle under the weight of sharply higher interest rates in early 2024. Last year's post-pandemic boost to auto production and exports is also on track to fade this year. And downward revisions to the household saving rate leave consumers with less of a financial cushion than we previously thought.

Many of Ontario's housing markets begin 2024 with some momentum, but that's a double-edged sword. Sales and price gains in Toronto and some nearby centres rallied strongly in December 2023, at least partially supported by a decline in bond and mortgage rates. But that will likely further limit affordability. According to the CMHC, Ontario is dealing with the biggest supply shortfall of any province. We also expect housing starts to fall this year given that much of last year's building activity was financed when interest rates were lower.

Graph 7
Ontario's Growth Weakened, but Continued to Beat Canada's in Q3



Statistics Canada, Institut de la Statitique du Québec, Ontario Ministry of Finance and Desjardins Economic Studies

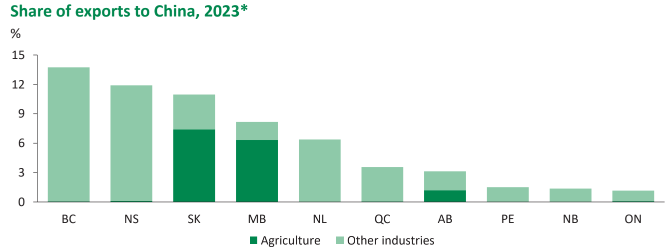
MANITOBA AND SASKATCHEWAN

We still expect Manitoba and Saskatchewan's economies to outperform the national average in 2024. For both provinces, relative housing affordability and relatively little exposure to interest rates should limit the economic slowdown. One lingering question surrounds the key agricultural sector. More normal production levels following last year's drought should support the expansion in 2024, but inclement weather increasingly presents downside risk in this respect. So does the prospect of slowing growth in the important Chinese export market (graph 8).

With some of the strongest growth rates in full-time employment and hours worked in any province last year, Manitoba's economy carries solid momentum into 2024. The province should continue to benefit from planned investments in the mining and manufacturing sectors. The biggest change since our last provincial outlook may well be on the fiscal side. Impacted by downward revisions to its tax base and drought-induced income losses at Manitoba Hydro, the province forecasts a much larger than previously expected deficit for the current fiscal year. That leaves less room to offer economic support if conditions dictate and may put hydro rate relief announced during the recent election campaign on ice.

Ongoing drought conditions have also hurt Saskatchewan's public finances, but we nonetheless think the province will perform better than most this year. Although the outlook for potash prices and production is uncertain, we anticipate that uranium output will continue to rise at the McArthur River and Cigar Lake mines. While the government revised its forecasts for oil production lower in its mid-year update, output in the sector is still on track to rise steadily over the next few years. Moreover, capital investment related to the $7.5B Jansen potash mine should continue into 2024. Finally, Saskatchewan begins this year with one of the tightest job markets in any province, which should limit layoffs as the overall economic backdrop softens in the first half of this year. However, Alberta's strong expansion looks to be increasingly drawing workers in—as seen in many prior oil price booms. Continuation of this trend could limit the ability of Saskatchewan firms to fill job openings going forward.

Graph 8
China Is an Important Export Market for Prairie Agricultural Producers



* Based on January to November data
Statistics Canada and Desjardins Economic Studies

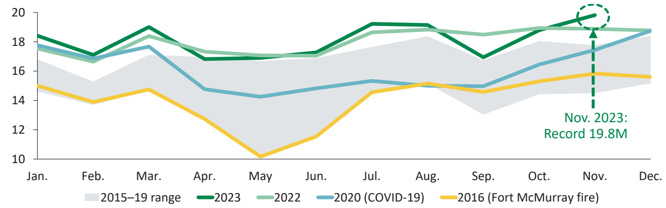
ALBERTA

Entering 2024, we still expect Alberta to be one of the fastest-growing provincial economies. The particularly deep real GDP contraction outside Ontario and Quebec in the third quarter suggests that the oil sands maintenance period we previously identified meaningfully impacted the expansion at that time. However, the subsequent rise in oil production to record levels (graph 9) suggests a rebound is well underway. Indeed, despite marking down current-year bitumen output forecasts in its November 2023 fiscal update, the provincial government made no change to next year's target, implying stronger-than-previously-anticipated growth in 2024.

Our forecast for WTI oil prices near US$80/barrel this year is supportive of energy sector activity. And the TransMountain Pipeline, expected to be in service later this year, should help Alberta oil prices.

The outlook remains strong outside the oil and gas sector. Petrochemicals and renewable energy projects are progressing, while a weak Canadian dollar continues to help provincial manufacturers. With support from the fastest population growth in the nation, home sales in the Calgary and Edmonton markets remain well above pre-pandemic levels. Looking ahead, tax cuts estimated at $3.6B (0.2% of GDP)—promised during last year's election campaign—could further juice consumer spending if enacted.

Graph 9
Alberta Oil Production Has Rebounded Strongly from the Maintenance Period
Alberta oil production
Million cubic metres



Alberta Energy Regulator and Desjardins Economic Studies

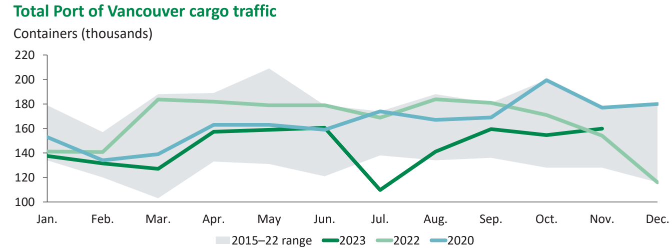
BRITISH COLUMBIA

We still think Canada's westernmost province will be among the most impacted by the ongoing interest-rate-induced economic slowdown. BC remains Canada's most housing-oriented provincial economy, and its households are the most indebted. Weak labour market and retail sales data released since our last provincial outlook continued to point to an economy particularly impacted by the accumulated effects of higher borrowing costs. As we've noted in the past, softening growth in China could prove challenging for trade given BC's close economic ties to that country. However, our expectations of greater stability in natural gas and forest product prices following last year's decline are more auspicious.

That said, BC's economy is building some momentum at the time of writing. With the Port of Vancouver strike over, container volumes have bounced back (graph 10). Homebuying activity also rallied to close out 2023 as bond rates came down. Still, we suspect that softer economic conditions will weigh on housing demand this spring before the Bank of Canada lowers rates.

Public finances remain an area of strength. Low levels of government debt leave room for economic support as needed. And from a growth perspective, the start of infrastructure project activity that was delayed last year could boost the expansion in 2024.

Graph 10
Shipping Activity Has Normalized Following the Port Strike



Port of Vancouver and Desjardins Economic Studies

SUMMARY FORECAST TABLE

TABLE 1
Canada: Major economic indicators by province

% CHANGE (UNLESS OTHERWISE INDICATED)	2020	2021	2022	2023f	2024f	2025f
Real GDP growth – Canada	**-5.0**	**5.3**	**3.8**	**1.1**	**0.2**	**2.0**
Newfoundland and Labrador	-4.8	1.0	-1.7	-0.5	1.7	1.8
Prince Edward Island	-3.0	8.4	2.9	1.7	0.5	1.0
Nova Scotia	-4.5	5.9	2.9	1.4	0.4	0.9
New Brunswick	-3.6	5.3	1.1	1.1	0.3	0.8
Quebec	-4.7	6.7	2.5	-0.2	0.7	1.4
Ontario	-4.5	5.4	3.9	1.2	-0.1	2.1
Manitoba	-4.1	1.3	3.3	1.7	0.4	1.6
Saskatchewan	-4.3	-0.7	6.0	1.8	0.7	1.8
Alberta	-7.8	4.6	5.0	2.4	0.9	2.3
British Columbia	-3.1	7.1	3.8	0.9	-0.1	2.2
Nominal GDP growth – Canada	**-4.0**	**13.4**	**11.8**	**2.3**	**2.2**	**3.0**
Newfoundland and Labrador	-10.2	18.5	6.8	-4.0	3.9	1.6
Prince Edward Island	0.3	14.9	9.3	2.6	2.0	2.0
Nova Scotia	-1.4	10.0	7.1	2.1	1.6	1.9
New Brunswick	-1.8	10.9	7.4	1.4	1.9	1.7
Quebec	-1.8	11.6	8.4	3.5	3.2	3.3
Ontario	-2.1	9.8	9.2	4.1	1.4	3.6
Manitoba	-2.2	9.2	8.6	2.4	2.2	2.8
Saskatchewan	-8.0	13.9	29.2	-1.8	2.9	1.3
Alberta	-14.4	24.9	22.0	-0.9	3.2	1.8
British Columbia	-0.5	15.8	11.0	1.8	1.9	3.3
Total inflation rate – Canada	**0.7**	**3.4**	**6.8**	**3.8**	**2.5**	**2.0**
Newfoundland and Labrador	0.2	3.7	6.4	3.3	2.3	2.0
Prince Edward Island	0.0	5.1	8.9	2.9	2.1	2.0
Nova Scotia	0.3	4.1	7.5	4.0	2.7	2.0
New Brunswick	0.2	3.8	7.3	3.5	2.2	2.0
Quebec	0.8	3.8	6.7	4.5	2.8	2.0
Ontario	0.6	3.5	6.8	3.8	2.4	2.0
Manitoba	0.5	3.2	7.9	3.6	1.9	2.0
Saskatchewan	0.6	2.6	6.6	3.9	2.3	2.1
Alberta	1.1	3.2	6.5	3.3	2.4	2.1
British Columbia	0.8	2.8	6.9	4.0	2.5	2.1
Employment growth – Canada	**-5.6**	**5.0**	**4.0**	**2.4**	**1.1**	**2.3**
Newfoundland and Labrador	-6.4	3.6	4.3	1.8	1.3	1.4
Prince Edward Island	-3.5	4.1	5.3	5.6	1.0	1.6
Nova Scotia	-4.6	5.6	3.6	2.7	1.1	1.8
New Brunswick	-3.0	3.2	2.7	3.3	0.9	1.6
Quebec	-5.4	4.3	3.0	2.4	0.5	1.9
Ontario	-5.4	5.2	4.6	2.4	1.0	2.5
Manitoba	-4.3	3.7	3.2	2.5	1.3	2.2
Saskatchewan	-5.0	2.6	3.5	1.8	1.4	2.3
Alberta	-7.0	5.5	5.2	3.6	1.8	2.6
British Columbia	-6.2	6.2	3.1	1.6	1.2	2.4
Unemployment rate – Canada	**9.7**	**7.5**	**5.3**	**5.4**	**6.8**	**6.5**
Newfoundland and Labrador	14.5	13.1	11.2	9.9	10.6	10.5
Prince Edward Island	10.7	9.9	7.5	7.4	8.8	8.7
Nova Scotia	9.9	8.6	6.6	6.3	7.5	7.3
New Brunswick	10.3	9.1	7.2	6.6	7.9	7.8
Quebec	8.9	6.1	4.3	4.4	5.6	5.3
Ontario	9.8	8.1	5.6	5.6	7.3	7.0
Manitoba	8.2	6.4	4.5	4.8	5.9	5.7
Saskatchewan	8.3	6.5	4.7	4.8	6.0	5.8
Alberta	11.4	8.5	5.8	5.9	7.0	6.7
British Columbia	9.1	6.5	4.6	5.1	6.6	6.3

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