Economic Viewpoint
Desjardins Economic Studies
www.desjardins.com/economics
January 8, 2014

Medium-term issues and forecasts

The effects of demographic changes will be increasingly felt

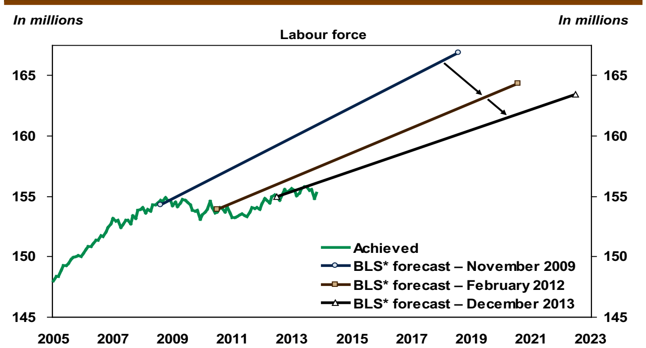
Successive episodes of economic upheaval and financial strain have occurred since the last recession, and while the worst appears to be behind us, many challenges are still clouding the horizon around the world. Among these, the clean-up of public finances will continue to curb economic growth in the years ahead. Profound changes—the aging of the population and limited increases in the labour force—will also impact growth in several countries, but over a longer period of time. As a result, the new expansion cycle will not be as pronounced as previous cycles. In this environment, interest rates are expected to rise but very gradually and will likely plateau at less lofty levels than during the last upward cycle.

INTERNATIONAL ISSUES

The world economic expansion cycle will become more entrenched in the medium term. However, on average, real GDPs' growth rates will be slower than before the 2008 recession and emerging economies will have to rely more on their own domestic demand to grow. Chinese growth is a key issue: the economic reform initiated by the country's new leaders will push China towards a model that relies less on exports and public investments. China and other Asian countries will also grapple with demographic issues. For its part, the European economy will slowly but surely recover from the setbacks caused by the double-dip recession, but the potential of economic growth will remain weak. Public administrations will remain deeply in debt for a long time.

The U.S. economy should slowly shed the shackles imposed by budget austerity and improvements to household balance sheets. The recession and weak recovery have created upheavals on the labour market and demographic changes will have a greater impact. The Bureau of Labor Statistics estimates that the labour force will grow at a slower pace until 2020 than in the past (graph 1), meaning that the participation rate will continue to decline. This is a major issue since it will hold back the U.S. economy's potential growth. Even if job creation is expected to slow down, the jobless rate will continue to decline due to weaker labour force growth. Lastly, inflation will hover above 2% in the medium term, while the housing component will make a bigger contribution to price increases after floundering for several years. Key interest will need to be increased, although only very gradually.

Graph 1 – Growth forecasts for the U.S. labour force revised downwards



* Bureau of Labor Statistics.
Sources: Bureau of Labor Statistics and Desjardins, Economic Studies

CANADIAN ISSUES

The anticipated ramp-up in global demand for commodities should be favourable to Canada's economy in the years ahead. Not only will this be good for exports, but companies should start to invest more heavily to increase their production capacities. Despite the uncertainties that have plagued the oil and gas extraction sector in recent quarters owing to distribution difficulties, everything suggests that solutions will be found.

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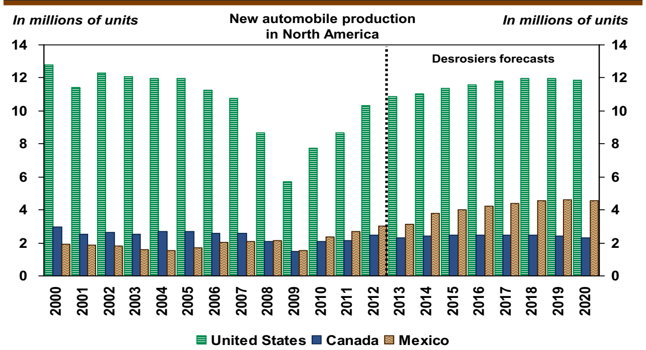
The competitiveness of Canadian companies, especially in the manufacturing sector, will also be a major issue in the years ahead. Investments will be required to boost productivity in an environment where the loonie is poised to stay at a fairly high level. The provinces in Central Canada, the heartland of the country's manufacturing sector, will be hit hardest, and economic growth will be weaker than in the more resource-rich regions. The new automobiles and parts manufacturing sector in Ontario will be challenged by stiff competition, especially from Mexico. The construction of new plants will increase automobile production in Mexico. The increase in Mexican production will therefore meet the bulk of expected growth demand in North America for new automobiles in the next 10 years (graph 2). In this environment, the growth potential for Ontario's automobile industry appears quite limited at the moment and consolidation—not growth—could be the new watchword.

Graph 2 – Production gains in Mexico will meet the bulk of increased demand for automobiles in North America



Sources: DesRosiers Automotive Consultants and Desjardins, Economic Studies

In terms of public finances, Ontario will also grapple with the scope of the sacrifices to be made to get back to a balanced budget as expected by 2017–2018. Ontario and British Columbia will also drive the real estate slowdown expected to take shape in the coming quarters. A slow but steady comeback in residential construction should then take hold, fuelled in most part by an uptick in population.

In Quebec, accelerations in the global and U.S. economies in 2014 will help international trade recover and breathe new life into the province's economy. However, deep structural problems, like demographics, will start to slow down the pace of economic growth and productivity gains will not be able to compensate completely. Quebec's population will age at a faster rate, as the wave of baby boomers was much bigger here than it was elsewhere. In the medium term, the expansion cycle in Quebec will lag behind the rest of North America. After the cyclical rebound expected in 2014 and 2015, when real GDP will temporarily hover around 2% growth per year, economic growth will gradually lean towards 1.5%.

Table 1
United States: medium-term major economic and financial indicators

	Annual average							*Average*	
In % (except if indicated)	2012	2013	2014f	2015f	2016f	2017f	2018f	2005-2012	2013-2018f
Real GDP (var. in %)	2.8	1.7	2.9	3.0	3.2	2.9	2.6	1.5	2.7
Total inflation rate (var. in %)	2.1	1.5	1.7	2.2	2.2	2.1	2.1	2.5	2.0
Unemployment rate	8.1	7.4	6.5	5.9	5.6	5.3	5.0	7.0	6.0
S&P 500 index (var. in %)*	13.4	29.6	6.0	7.9	6.0	5.0	5.0	3.9	9.9
Federal funds rate	0.25	0.25	0.25	0.50	1.95	3.00	3.80	2.04	1.63
Prime rate	3.25	3.25	3.25	3.50	4.95	6.00	6.80	5.04	4.63
Treasury bills—3-month	0.09	0.06	0.15	0.60	2.00	3.05	3.85	1.80	1.62
Federal bonds—10-year	1.78	2.34	3.20	3.70	3.90	4.15	4.30	3.54	3.60
Federal bonds—30-year	2.92	3.45	4.00	4.30	4.50	4.65	4.75	4.21	4.27
WTI** oil (US$/barrel)	94	98	97	100	100	105	110	78	102
Gold (US$/ounce)	1,669	1,411	1,150	1,050	950	900	950	1,007	1,069

f: forecasts; * The variations are based on observation of the end of period; ** West Texas Intermediate.
Sources: Datastream and Desjardins, Economic Studies

Table 2
Canada: medium-term major economic and financial indicators

In % (except if indicated)	Annual average 2012	2013	2014f	2015f	2016f	2017f	2018f	Average 2005-2012	2013-2018f
Real GDP (var. in %)	1.7	1.7	2.3	2.6	2.9	2.7	2.5	1.7	2.4
Total inflation rate (var. in %)	1.5	1.0	1.6	1.8	2.0	2.2	2.0	1.9	1.8
Employment (var. in %)	1.2	1.3	1.4	1.8	1.4	1.2	1.0	1.2	1.3
Employment (K)	202	229	250	317	255	219	188	198	243
Unemployment rate	7.2	7.1	6.9	6.6	6.5	6.3	6.1	7.0	6.6
Housing starts (K)	215	188	181	178	185	190	195	205	186
S&P/TSX* index (var. in %)	4.0	9.6	9.0	10.0	8.0	7.0	6.0	5.8	8.3
Canadian dollar (US$/C$)	1.00	0.97	0.94	0.97	0.98	0.96	0.94	0.93	0.96
Overnight funds	1.00	1.00	1.00	1.25	2.15	2.80	3.45	2.13	1.94
Prime rate	3.00	3.00	3.00	3.25	4.15	4.80	5.45	4.01	3.94
Mortgage rate									
1-year	3.18	3.08	3.15	3.65	4.55	5.10	5.55	4.89	4.18
5-year	5.27	5.23	5.45	6.05	6.35	6.65	6.80	6.08	6.09
Treasury bills—3-month	0.95	0.97	1.00	1.35	2.20	2.85	3.45	2.00	1.97
Federal bonds									
2-year	1.12	1.11	1.35	2.20	2.90	3.30	3.55	2.42	2.40
5-year	1.37	1.63	2.25	3.00	3.40	3.70	3.90	2.89	2.98
10-year	1.87	2.26	3.10	3.60	3.75	3.95	4.10	3.41	3.46
30-year	2.45	2.83	3.45	3.80	4.00	4.15	4.30	3.81	3.76
Canada/U.S. rate spreads									
Treasury bills—3-month	0.86	0.91	0.85	0.75	0.20	-0.20	-0.40	0.20	0.35
Federal bonds—10-year	0.09	-0.07	-0.10	-0.10	-0.15	-0.20	-0.20	-0.13	-0.14
Federal bonds—30-year	-0.47	-0.62	-0.55	-0.50	-0.50	-0.50	-0.45	-0.41	-0.52

f: forecasts; * The variations are based on observation of the end of period.
Sources: Statistics Canada, Canada Mortgage and Housing Corporation and Desjardins, Economic Studies

Table 3
Quebec and Ontario: medium-term major economic indicators

Var. in % (except if indicated)	Annual average 2012	2013f	2014f	2015f	2016f	2017f	2018f	Average 2005-2012	2013-2018f
Quebec									
Real GDP	1.5	1.2	1.8	2.1	1.9	1.7	1.5	1.6	1.7
Total inflation rate	2.1	0.9	1.7	1.9	2.0	2.1	2.0	1.8	1.8
Employment	0.8	1.1	1.2	1.5	1.0	0.7	0.5	1.0	1.0
Employment (K)	31	45	50	60	40	30	20	39	41
Unemployment rate (%)	7.8	7.6	7.3	6.8	6.5	6.0	5.7	7.9	6.7
Retail sales	1.1	1.7	2.7	3.0	2.8	2.5	2.5	3.6	2.5
Housing starts (K)	47	37	37	41	38	35	35	48	37
Ontario									
Real GDP	1.3	1.4	2.1	2.7	2.5	2.5	2.2	0.6	2.2
Total inflation rate	1.4	1.0	1.4	1.7	2.0	2.2	2.0	1.9	1.7
Employment	0.8	1.5	1.4	1.8	1.5	1.2	1.2	0.9	1.4
Employment (K)	52	100	99	123	107	87	88	60	100
Unemployment rate (%)	7.8	7.5	7.4	7.1	6.8	6.6	6.4	7.4	7.0
Retail sales	1.6	2.5	3.2	3.7	4.5	4.8	4.2	3.2	3.8
Housing starts (K)	77	61	57	53	60	64	68	69	61

f: forecasts
Sources: Statistics Canada, Canada Mortgage and Housing Corporation and Desjardins, Economic Studies