

# Canadian Economic Outlook

Quarter 1 2024

March 2024



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# Executive Summary

## The Year Ahead: A Slow Road to Recovery

An uncertain economic future continues to be a major concern for Canadians in early 2024, as consumers remain worried about persisting inflation. Household debt, coupled with elevated interest rates, may pose a risk to the financial wellbeing of many Canadians. At the same time, consumers and businesses are expected to exercise caution in spending and investment decisions. Overall, economic growth is expected to continue on a sluggish path in 2024, before gaining pace in 2025.



### Canadian Economic Outlook

- ▶ **Inflationary pressures in the economy are gradually subsiding**, primarily due to tighter monetary policy measures taken by the Bank of Canada.
- ▶ Inflation is projected **to be within the Bank of Canada's target range by mid to late 2024**.
- ▶ **GDP is forecasted to remain flat in Q1 2024**, followed by moderate growth in late 2024 and a rebound in 2025.



### Employment

- ▶ **Labour market tightness is expected to persist throughout this business cycle**, with slower hiring but businesses aiming to retain their current talent.
- ▶ Employment is expected to **grow moderately**, with an **expanding labour pool** as Canada commits to its **immigration policy**.



### Consumer Behaviour

- ▶ Consumption levels are expected to remain flat over the next two quarters as higher interest rates work through the economy.
- ▶ Easing of inflationary pressures in the economy are expected to **support growth in real consumption and wages** over the next two years.
- ▶ However, consumers are **concerned about rising prices**, with retail purchases remaining flat throughout 2023 and savings rates increasing marginally.



### Business Activity

- ▶ **Business sentiment has begun to show signs of improvement but** is still below pre-pandemic levels shown in late 2022 after reaching a five-year high in late 2021.
- ▶ Canadian businesses remain cautious about the economic climate, but are **beginning to exhibit a positive outlook** heading into 2024.

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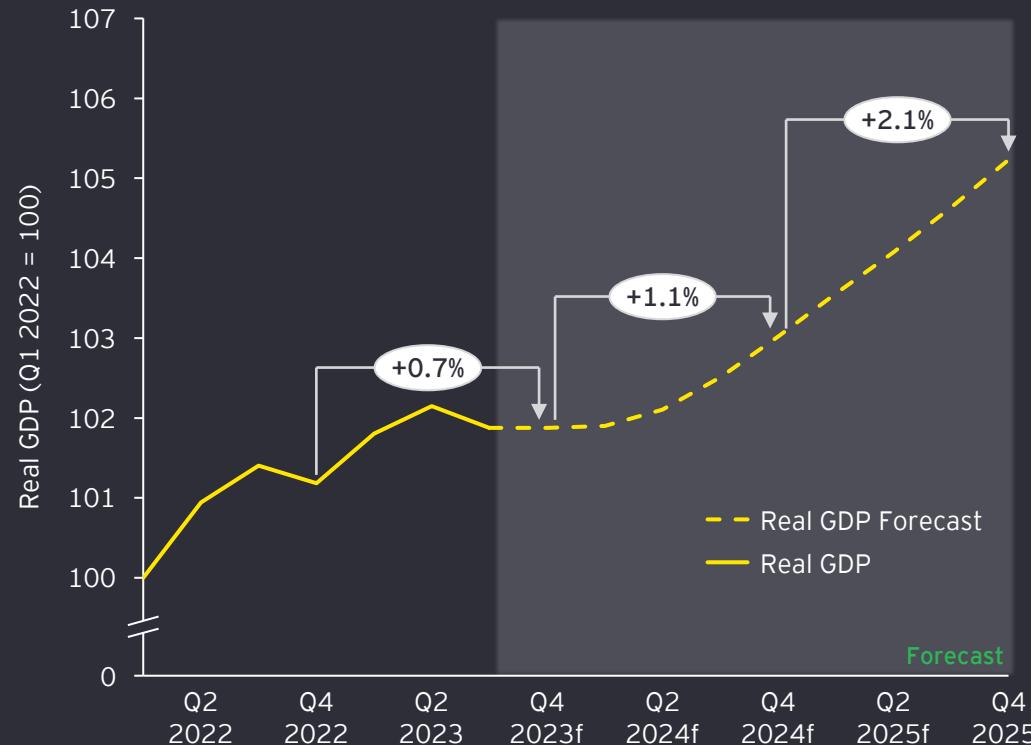
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# Canadian Economic Outlook

GDP growth and inflation are slowing down in the wake of tight monetary policy

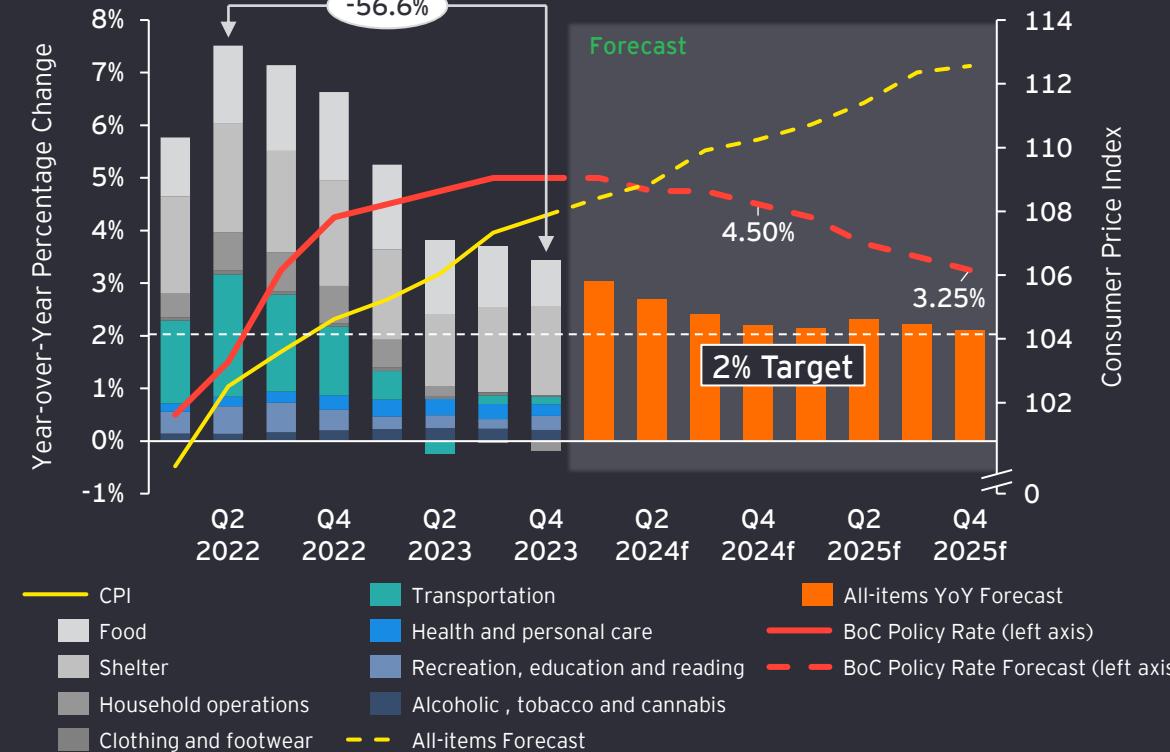
The economy cools in response to monetary policy during early 2024

(Q1 2022 = 100)



- Real GDP plateaued in 2023 as increased policy rates kicked in to curb inflationary pressures, slowing consumption and investment demand.
- It is expected that the economy may exhibit slow growth over the first half of 2024, growing at an average quarterly rate of 0.1%, before accelerating to an average 0.4% rate in the second half of 2024. Growth is expected to rebound in 2025, with the economy forecast to grow at a yearly rate of 2.1%.

CPI growth reduced considerably over the past three quarters (Q1 2022 = 100)



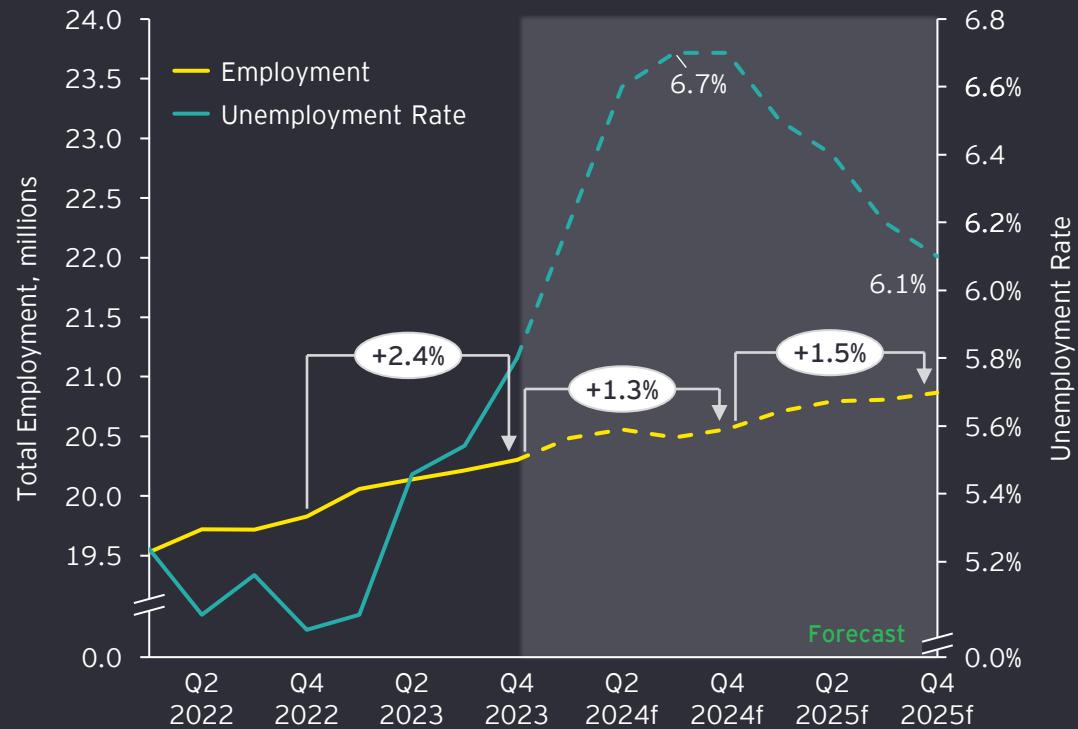
- While inflation remains above the target rate of 2%, a decline in 2023 suggests pressures on prices are easing. However, as of Q4 2024, CPI growth remains over 3%, with rising shelter costs fueling inflationary pressures.
- The inflation rate is expected to continue to ease over the next few quarters, reaching the Bank of Canada's target range by mid to late 2024.

# Employment

Employment continues to increase slowly as labour shortages ease

Employment slowed throughout 2023, with a similar trend expected over the next two years

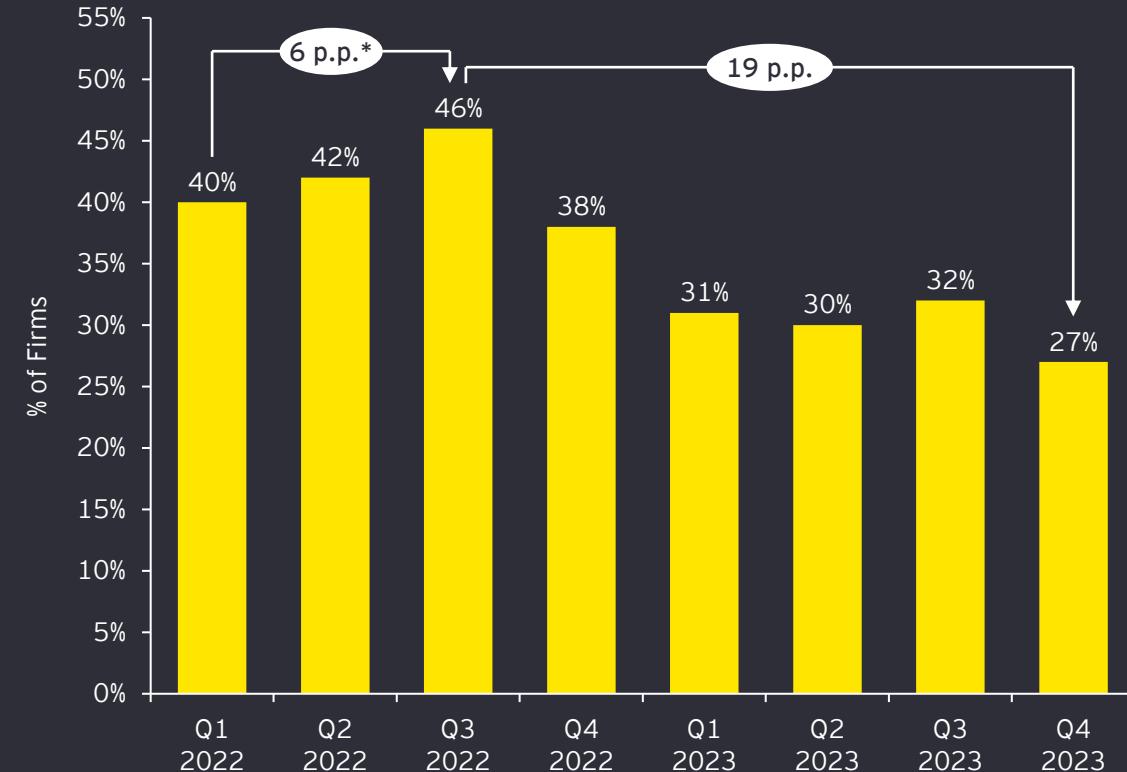
(Employees in Canada aged 15 years or more)



- Since the start of 2023, **employment growth has shown signs of cooling** due to a gradual softening in the labour market. It is expected that employment will continue to grow moderately over the next two years, with an average **annual rate of 1.4%**.
- The **expanding labour force** resulting from government immigration targets. This may lead to higher unemployment rates going into 2024 and throughout 2025.

Persistent labour shortages are easing

(% of firms experiencing labour shortages)



- Labour market pressures eased over the past six quarters** from the post-pandemic high. Despite these trends, over a quarter of firms still claim that they are **experiencing labour shortages** during Q4 2023.

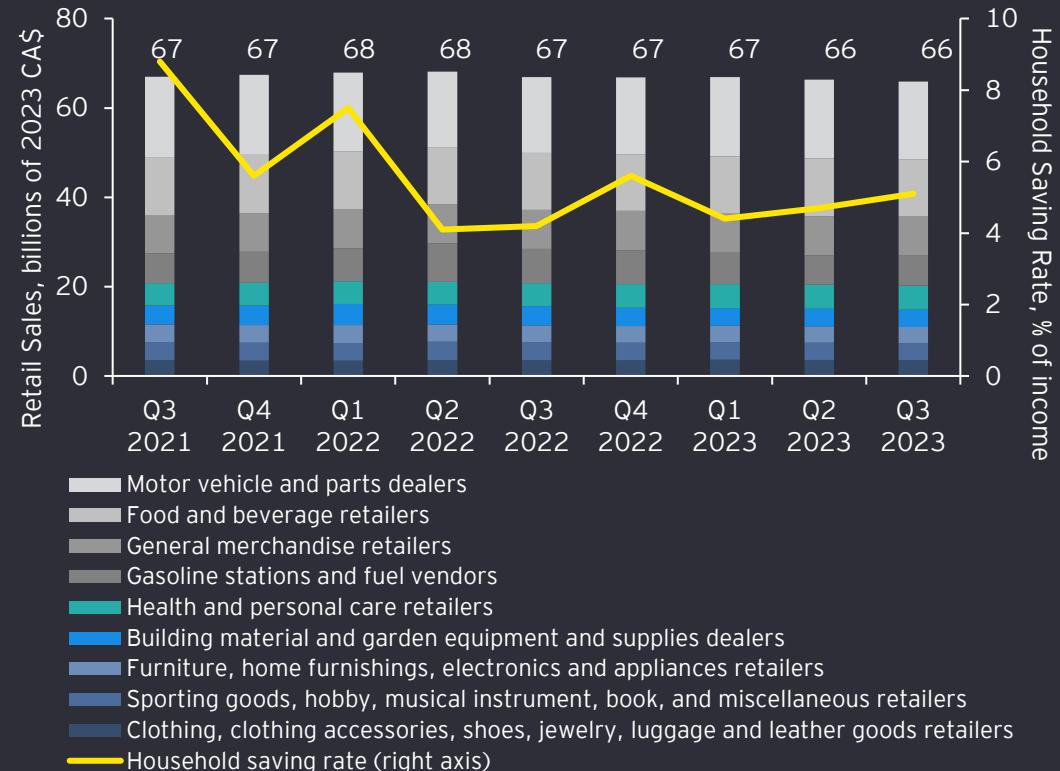
# Consumer Behaviour

Prices are top of mind for Canadian consumers, and cautious spending has kept retail sales flat

Consumers have indicated prices are the most important consideration when making purchases



Retail sales and saving rates have been flat across Canada



- Prices remain a top concern for Canadians, with **more than half of consumers claiming that prices are the most important factor** when making purchases.
- In addition to price, Canadian consumers have expressed **that quality of products and services, health, and sustainable packaging** are amongst their top consumption criteria.

- **Retail sales have remained flat** over the last two years. Household **saving rates decreased** from nearly 9% in Q3 2021 to a low of 4% in Q2 2022, before seeing a marginal increase over the five percent mark in Q3 2023.
- In the last two years, sales have declined for **sporting goods and similar recreational products, furniture, electronics, and appliances, and building materials and supplies**.

# Consumer Behaviour

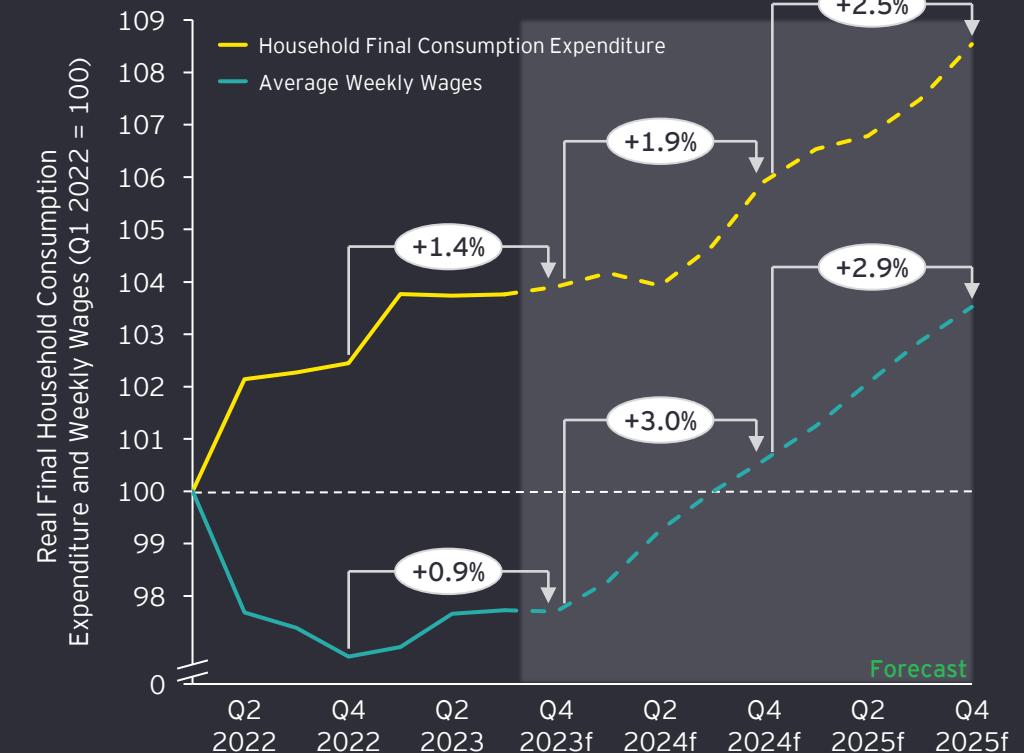
With easing of inflationary pressures, consumption trends are expected to improve in mid to late 2024

Consumer confidence and expectations of inflation have improved over the past year

(consumer confidence: Q1 2022 = 100)



Real household consumption and wages have stabilized and are expected to sustain real growth rates over 2024



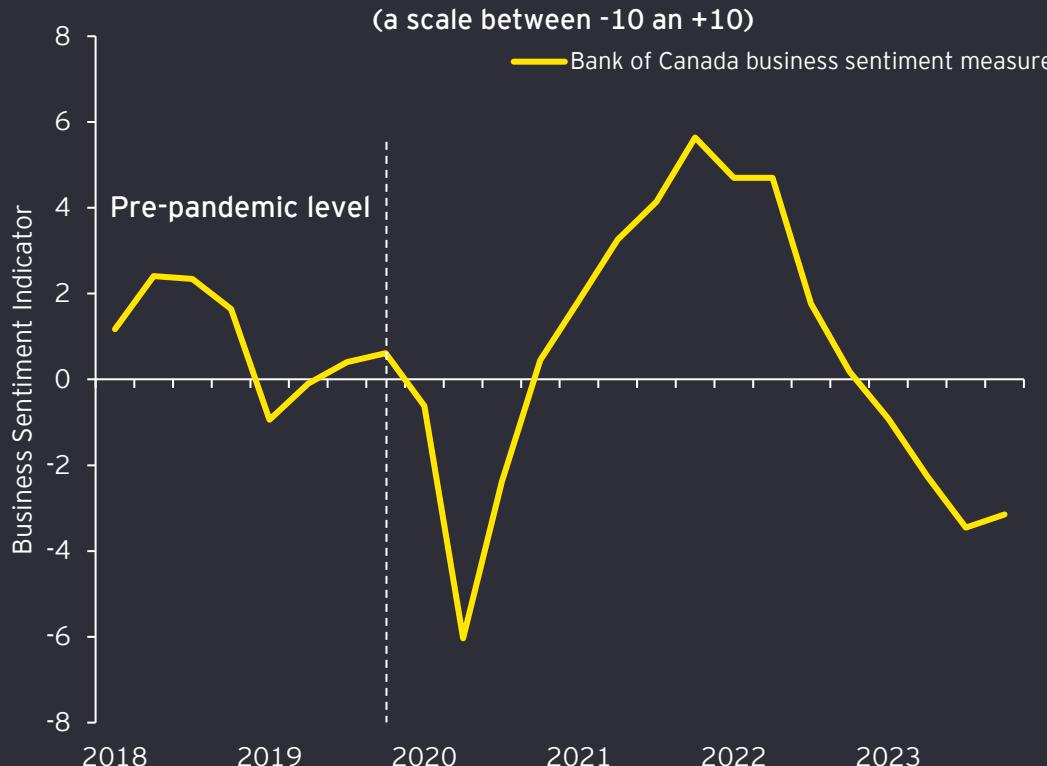
- Following a period of stagnation in 2022, **1 year inflation expectations have improved, stabilizing around 5% during mid to late 2023.**
- Consumer confidence has also improved**, reversing the negative trend displayed in the beginning of 2022.

- Over the past two years, **average real wages have decreased in Canada**, as inflationary pressures constrained household budgets.
- However, as inflationary pressures ease and the economic outlook improves, **real wages and household consumption are expected to increase through 2024** at an average annual rate of 2.9% and 2.2%, respectively.

# Business Activity

Businesses begin to exhibit cautious optimism heading into 2024

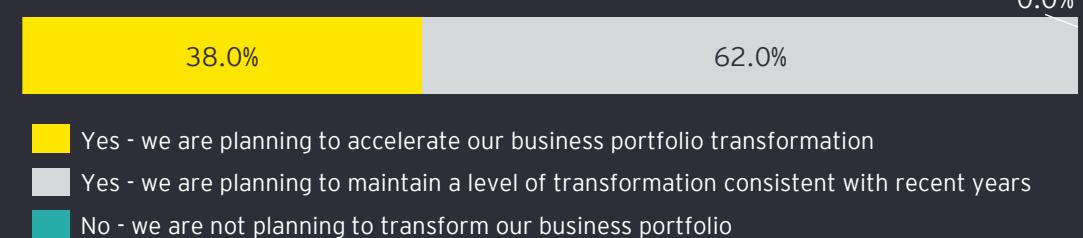
Business sentiment remains below pre-pandemic levels, but shows signs of improvement



- The business sentiment measure released by the Bank of Canada, reflects the **expectations amongst business leaders regarding sales and growth expectations**, as well as the overall business outlook.
- Business sentiment **began showing improvement as 2023 drew to a close**, but levels remains below pre-pandemic levels.

Strategic decision-making takes a positive turn

(% of CEOs surveyed asked if they are planning to transform their business portfolio over the next 12 months)



(% of CEOs surveyed asked if they expect to actively pursue any of the following transaction initiatives over the next 12 months)

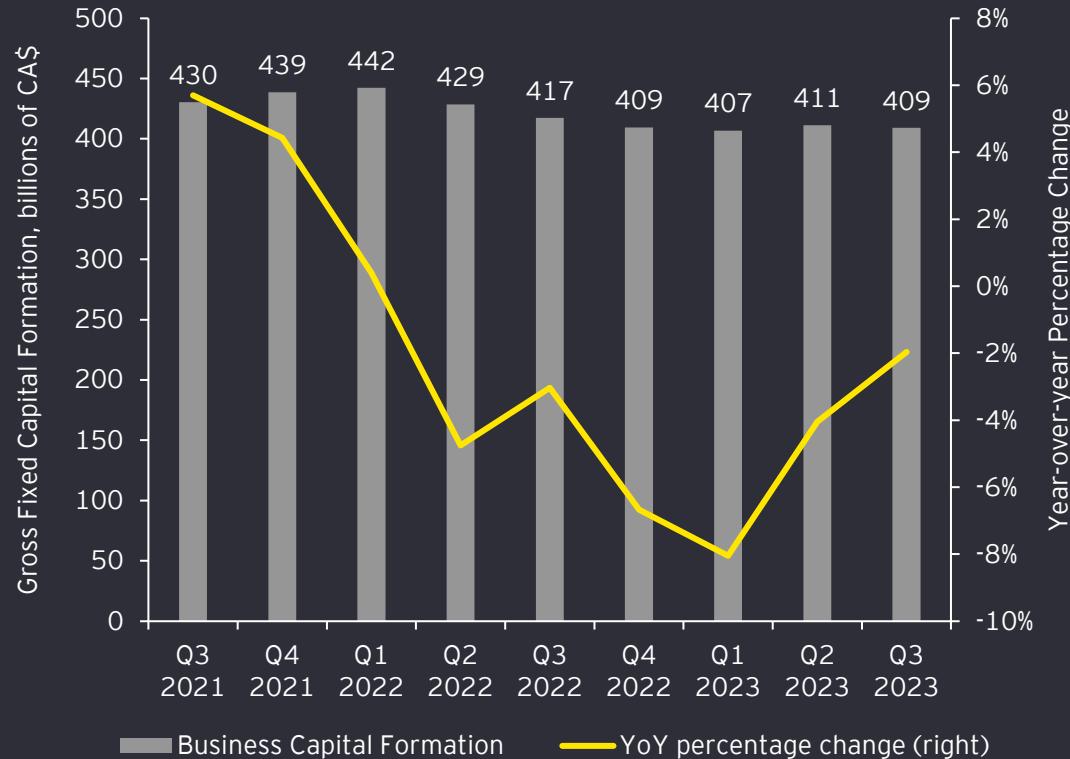


- All Canadian CEOs surveyed by EY indicated that they will be transforming their business portfolio over the next year.
- Looking ahead, leaders are looking towards pursuing M&A, divestments/ spinoffs/ IPOs, and joint ventures. Despite ongoing economic uncertainty, **businesses are adopting a more positive outlook**.

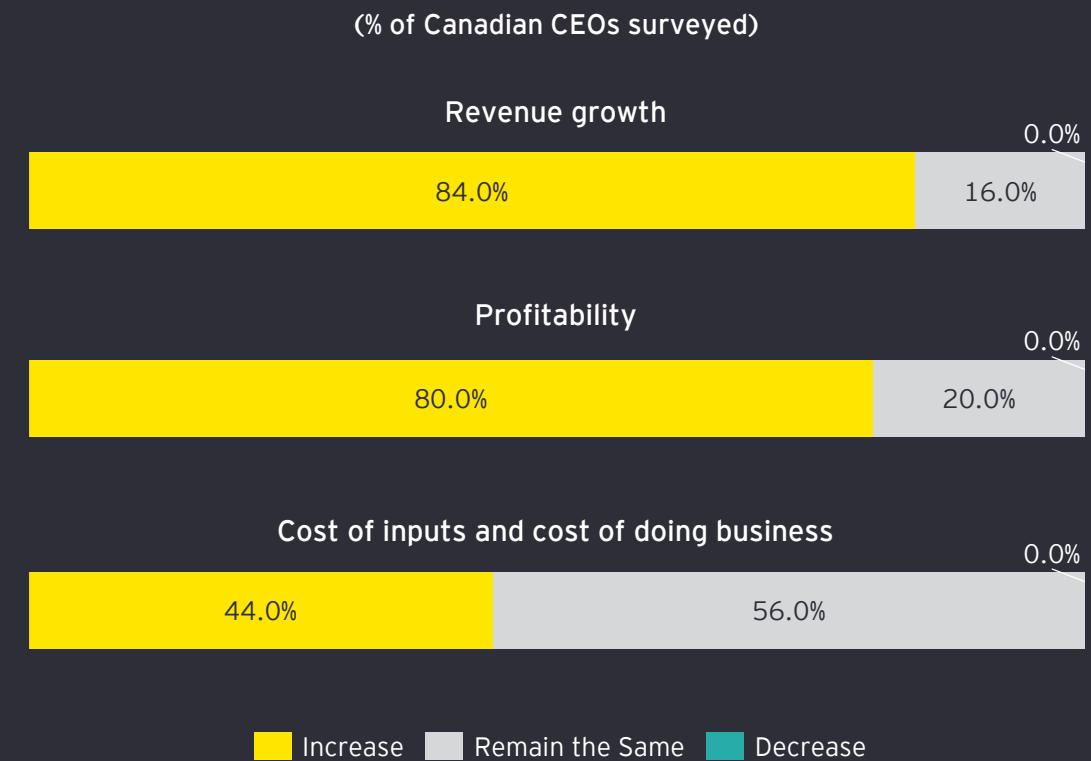
# Business Activity

Businesses begin to exhibit cautious optimism heading into 2024

Business investment behaviour indicated a recovery in 2023



Canadian CEOs show confidence in financial performance despite continued challenges



- Gross fixed capital formation captures the **net value of business investment in non-financial fixed assets**, such as machinery, buildings, and equipment.
- Flat investments throughout 2023 may reflect **uncertainty in the business environment and short-term economic outlook for companies**, who have exercised caution regarding investment and spending decisions. However, the year on year growth shows improvement towards the end of 2023.

- Despite expectations of a continued high inflation and low growth environment, **Canadian CEOs are demonstrating increased optimism for 2024** when it comes to their own revenue growth and profitability.
- **Majority of CEOs report expected increases in revenue growth and profitability**, despite lingering concerns around a continued high inflation environment.

# Key Takeaways

## Effects of monetary policy apparent as the economy begins to adjust

### Themes



Inflation is easing as increased policy rates work through the economy; however, it remains higher than the Bank of Canada's target rate of 2%.



Consumers have been affected by elevated prices and high interest rates; however, inflation expectations are starting to show signs of improvement.



Businesses are showcasing an optimistic outlook despite prevailing economic conditions.

### Economic Considerations for the Future



Employment growth over the 2024-2025 period is expected to be supported by the Canadian government's immigration strategy, with a goal of around 1.5 million new immigrants by 2025.



Household debt is expected to be a key vulnerability, primarily attributed to high residential real estate prices and elevated interest rates.



Canadian businesses are anticipated to closely monitor the evolving economic landscape, as well as global geopolitical risks

### Risk Factors for the Economy



Inflationary pressures and interest rates remain elevated in early 2024



The economy is expected to grow moderately over the next year, which may lead to reduced consumer demand



Tight supply for residential real estate and elevated financing costs are a concern amid high immigration targets

# EY Canada Economics Team

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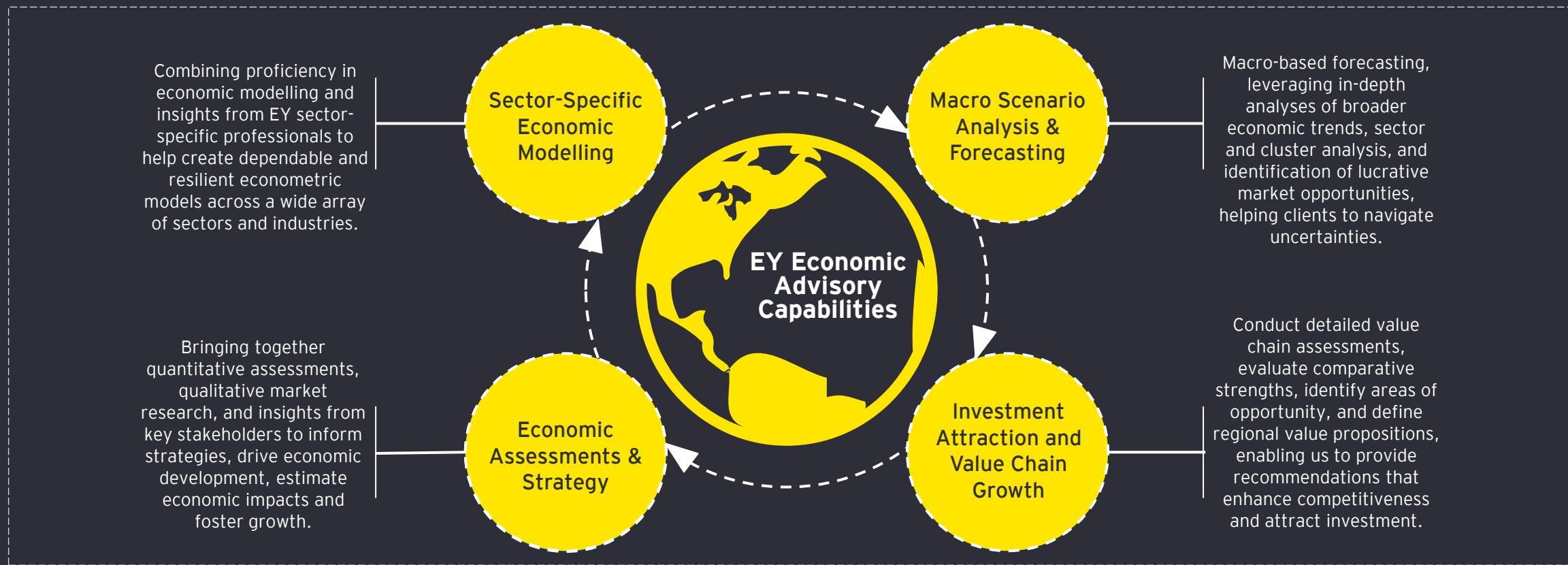


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# About the Economics Team

## Economic Advisory Services

The Economic Advisory services applies economic principles to a wide variety of complex business issues. We develop sophisticated economic models and other quantitative tools grounded in fundamental economic theory to provide measurable insights for EY clients when confronted with business decisions involving operations and strategic planning, economic assessments, market analysis, competitiveness studies, and investment attraction. We believe EY professionals bring several key differentiators which make us appropriately positioned to help deliver against your objectives. Our economists have prepared numerous similar industry and market analysis for public and private sector clients across Canada and globally.



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