

2016 Growth Looks Modest As Canada Becomes "A Tale of Two Economies": TD Economics

TORONTO – The Canadian economy rebounded in the third quarter of 2015, albeit at a moderate pace and with early evidence that fourth quarter momentum has fizzled. This, in combination with a number of ongoing headwinds, will constrain the nation's rate of expansion to less than 2% annually over the next few years. Achieving these comparatively tepid growth rates will depend crucially on external developments, as exports take the driver's seat for the Canadian economy.

A tale of two economies

2015 marked two strong and opposing forces in Canada's economy, which TD Economics anticipates will persist over the next few years. Domestic-oriented growth drivers will continue to be challenged by low commodity prices, high household indebtedness, and a gradual rise in longer-term interest rates. In contrast, the export sector is expected to enjoy solid gains driven by a competitive currency and rising U.S. demand. "Putting the pieces together reveals a picture where Canada's economic fortunes over the coming year are deeply tied to the external environment. Canada is not the master of its destiny as it once was," said Chief Economist Beata Caranci. "Even with the stage set for sustained export growth, our research suggests that growth will be more muted than in past recoveries, so we remain cautious about the overall outlook for the economy."

Business investment to remain the weakest pocket

Within the domestically-oriented areas of the economy, overlapping cycles continue to play out. Business investment is likely to contract further through the first half of 2016 as low oil prices continue to impact energy-related capital spending. Caranci also said that "the household debt cycle is long in the tooth. Credit is not expected to deliver as large a boost to consumer spending growth relative to the past." In addition, housing activity has remained resilient in 2015, but momentum is expected to cool in view of reduced affordability. The result will be consumption growth of about 1.7% on average in 2016-17, below historical averages.

Unemployment rate to hold steady, but sizeable regional variations to persist

Consistent with a modest economic outlook, the job market is likely to remain relatively soft. Employment growth is expected to slow, reflecting the economic adjustment away from resource extraction and housing and towards export-oriented industries. Job growth is expected to average about 10,000 net positions per month through 2016 and 2017. As a result, the unemployment rate is likely to decline only slowly, reaching 6.8% by the end of 2017 (from 7.1% currently).

However, the national trends will continue to conceal large differences in regional job and economic prospects. Caranci noted: "With exports leading the way and the commodity sector in the doldrums, the relative growth drivers continue to favour B.C., Manitoba, Ontario and Quebec, while Alberta is likely to face another difficult year in 2016,"

Not a typical cycle

An interesting feature of the current outlook, noted Caranci, is the large divergence in domestic demand between Canada and the U.S. Typically, trends in total domestic spending – i.e., the sum of spending by consumers, businesses and governments – follow somewhat similar paths on both sides of the border. However, this past year, Canadian domestic demand has slowed to about one-third of the pace recorded stateside and a similar gap is anticipated in the year ahead. These diverging trends will be mirrored in monetary policy, as the Bank of Canada is expected to keep its overnight rate steady until late 2017, even as the Fed tightens its policy settings. Consistent with the divergent policy paths, the near-term pressure on the Canadian dollar is likely to be on the downside, potentially reaching a low of about 71 US cents by early 2016.

Caranci added, "the weak currency will continue to create winners and losers in Canada, but on net, is helping to mitigate the negative impact on national income from low commodity prices and driving the transition to more balanced, export-led growth."

For media inquiries, please contact:

Beata Caranci, VP & Chief Economist,
TD Bank Group
416-982-8067

Derek Burleton, VP & Deputy Chief Economist,
TD Bank Group
416-982-2514