

A Bear Unleashed:

Implications of Putin's War on Canada's Economy

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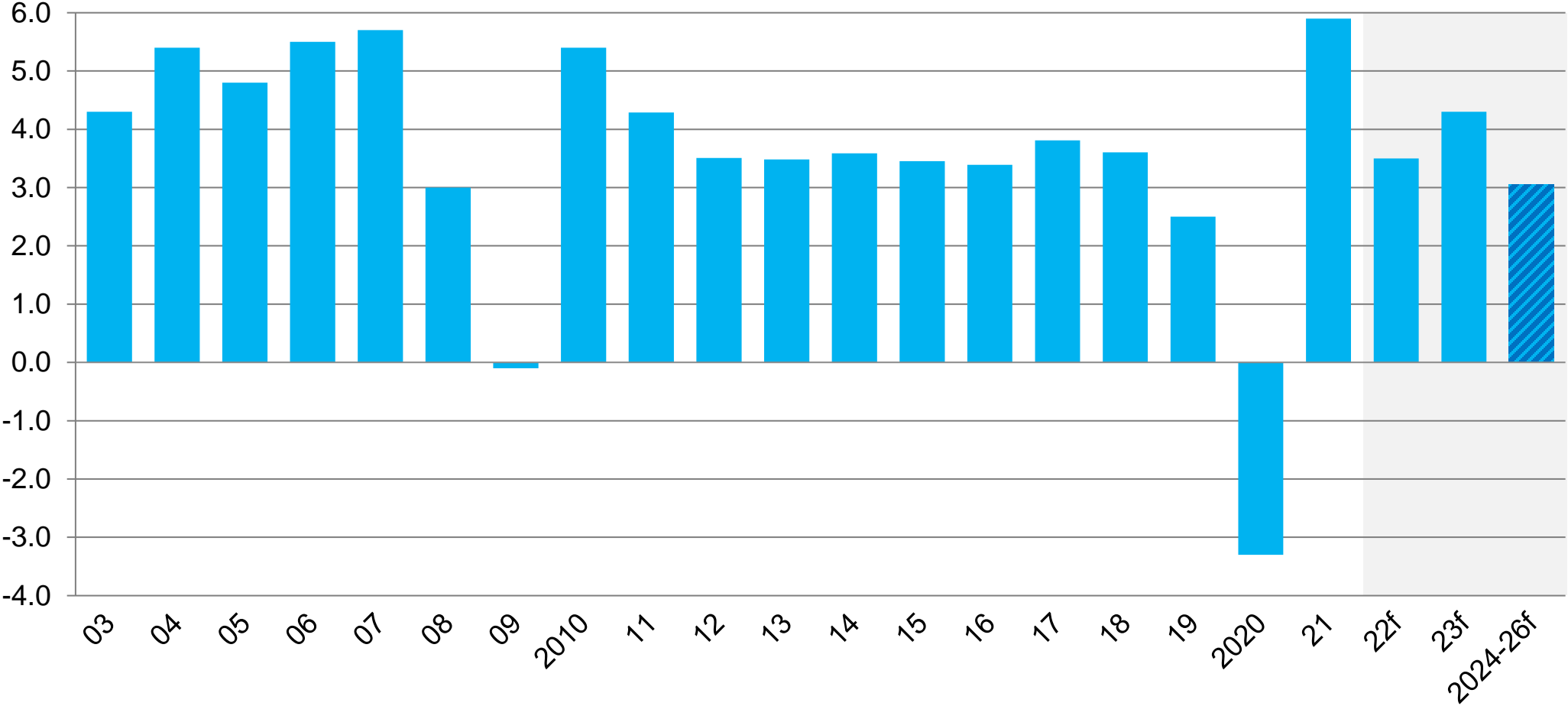
World Outlook—Near Term Fraught with Risks



- The war in Ukraine has led us to lower GDP growth this year from 4.4 to 3.5 per cent—assuming the war remains confined to Ukraine’s borders and doesn’t drag on for much longer. Risks, not surprisingly, are all on the downside.
- The stress in global supply chains and ongoing shortages of goods and commodities due to the pandemic will get worse because of the war. Ukraine and Russia are major suppliers of grains, oilseeds, natural gas, crude oil, metals and minerals.
- The world’s major central banks face difficult policy choices. Most have started to increase interest rates to contain inflationary pressures. The price shock caused by the war could derail inflation expectations and force much tighter monetary policy.
- A darker scenario for the global economy from a prolonged war could result in a world-wide-recession. If, for instance, NATO and other countries place an embargo on all Russian oil exports, world oil prices could surge even higher, and push the world into recession as central banks are forced to ramp up interest rates to contain inflation.
- COVID-19 and variants continue to pose near-term risks to the outlook, especially in China.

War Leads to Weaker Global Growth

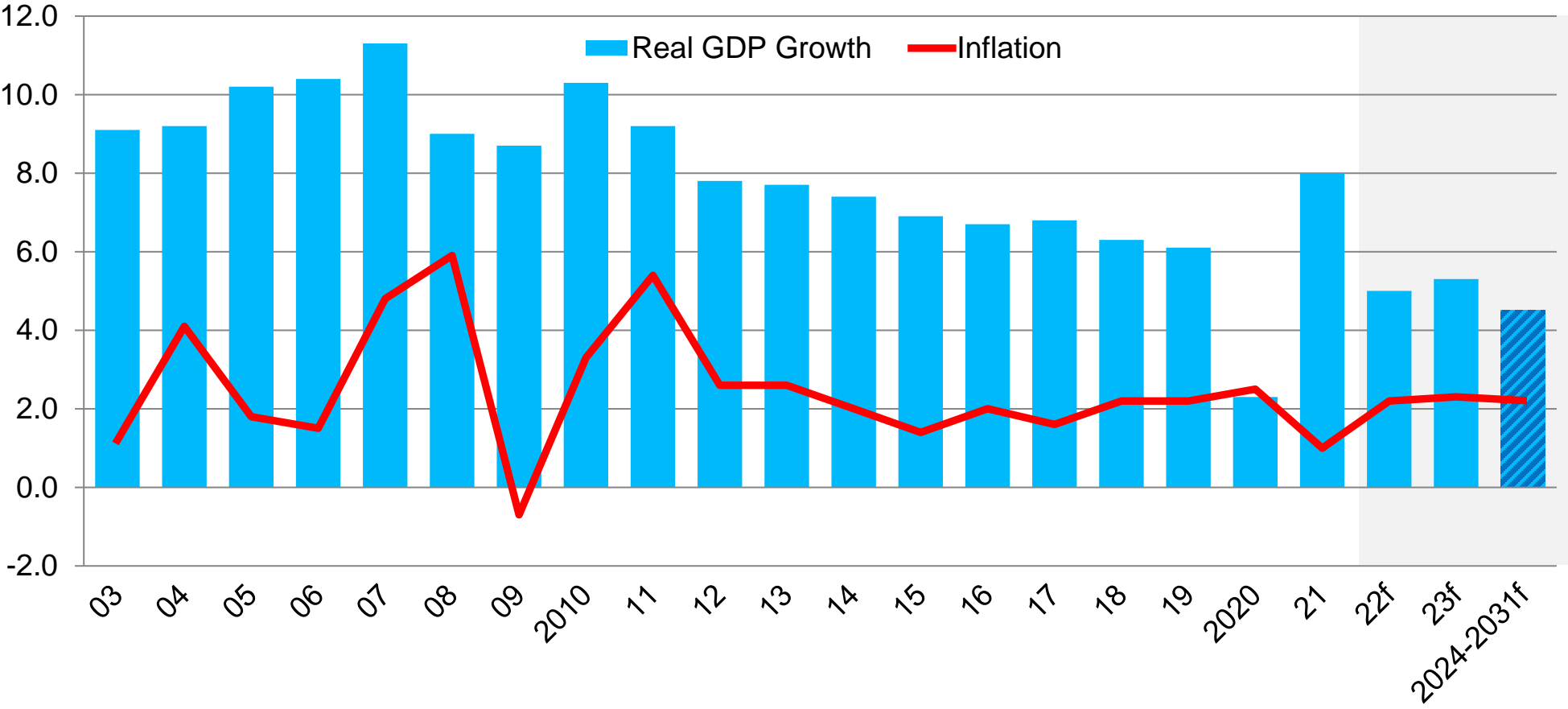
world real GDP growth, per cent change and average annual per cent change



Sources: International Monetary Fund; Consensus Economics; The Conference Board of Canada.

China's Economic Slowdown

real GDP, per cent change and average annual per cent change

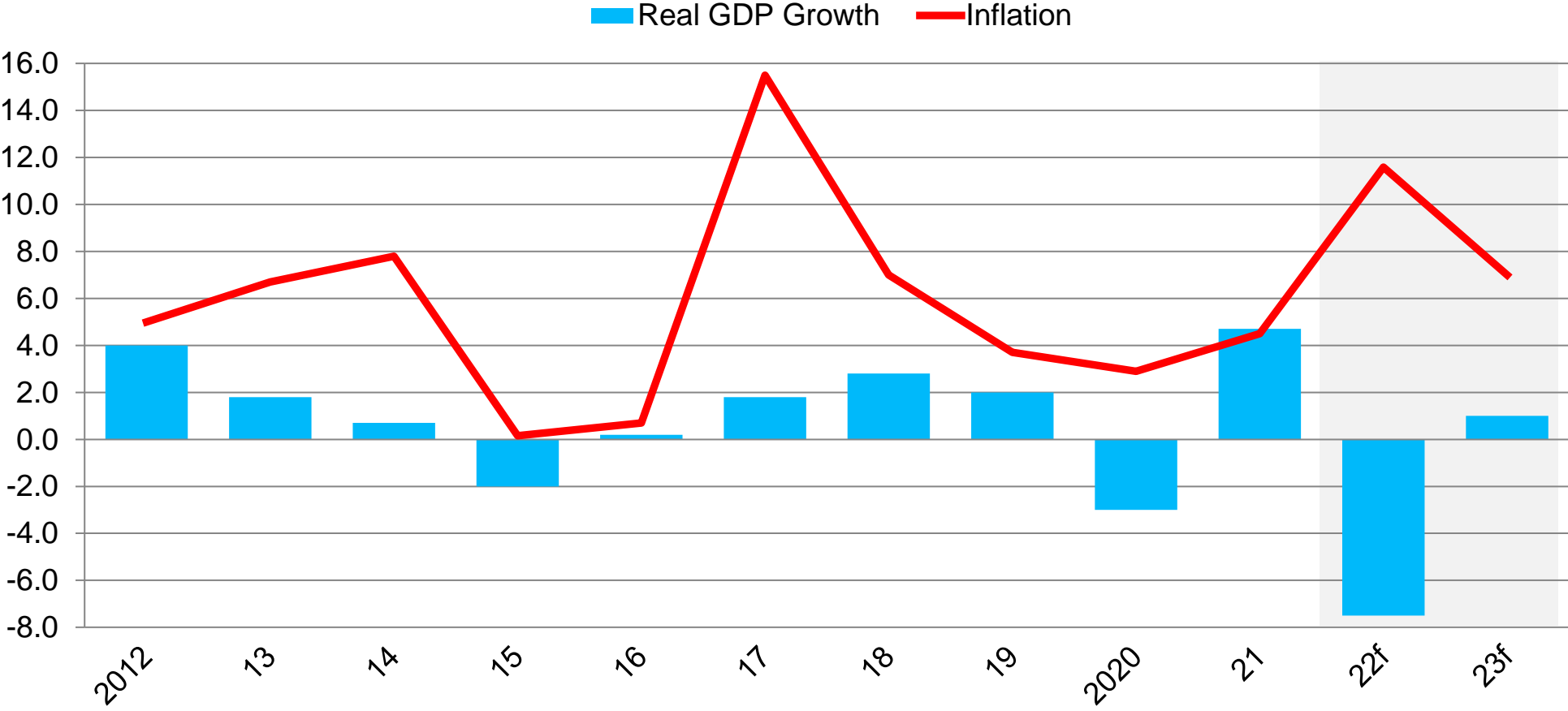


Source: Consensus Economics.

Sanctions Push Russia into a Severe Recession



real GDP, per cent change



Source: Consensus Economics.

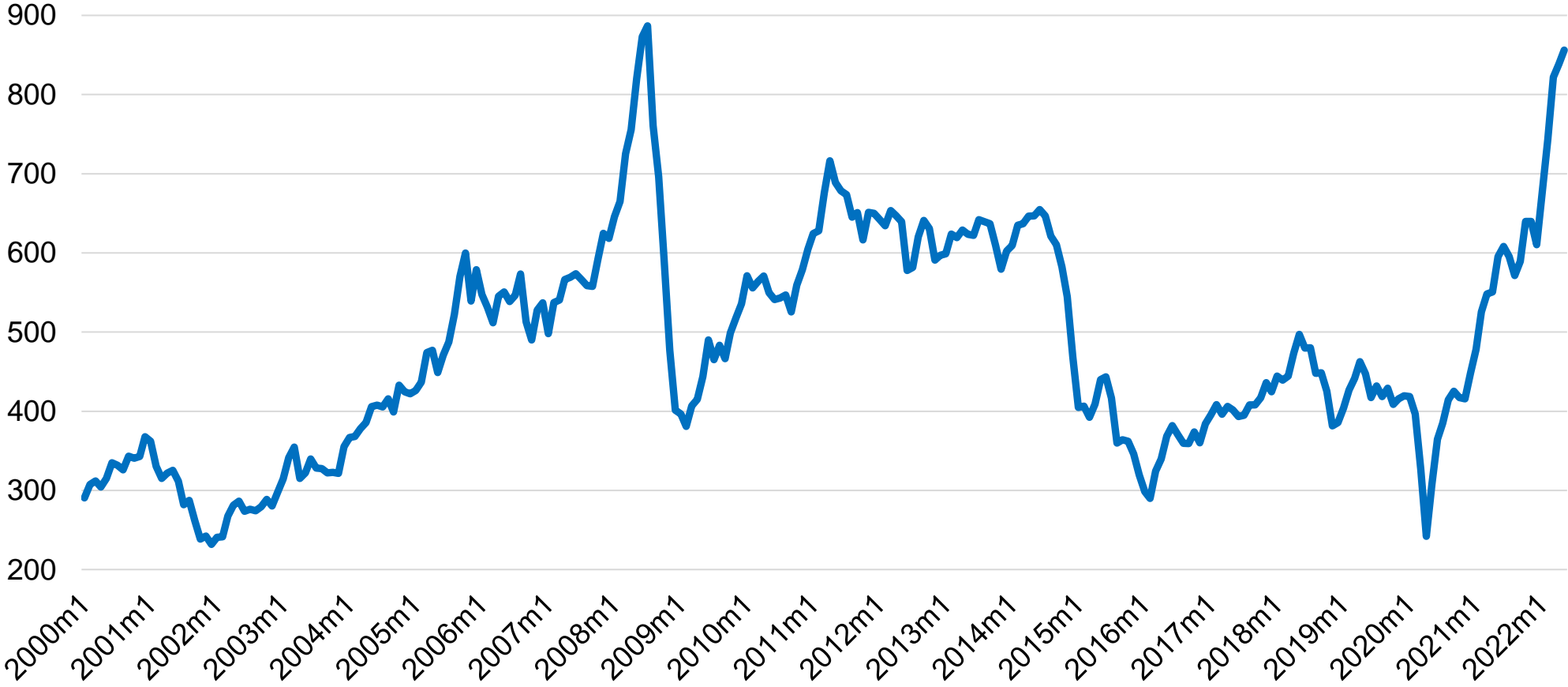
The War in Ukraine



- Vladimir Putin's war is a tragedy that has resulted in thousands of innocent civilian lives lost and millions displaced. Ukrainians and Russians are being killed in battle, and Ukraine's cities and infrastructure are being turned to rubble. The economic fallout for both countries is devastating, and the effects will be felt globally.
- The economic fallout is a massive commodity price shock. Unless Putin is overthrown, we assume that sanctions will persist, and commodity prices will remain elevated over the medium term.
- For many countries, including Canada's important trading partners, the war will have a significant negative impact on consumer spending and real GDP.
- The net impact for Canada is almost neutral because raw material and agricultural producers and exporters benefit from higher prices.
- A refugee crisis, post-war rebuilding and expanded military spending will add to public spending and debt.

Commodity Prices Spike

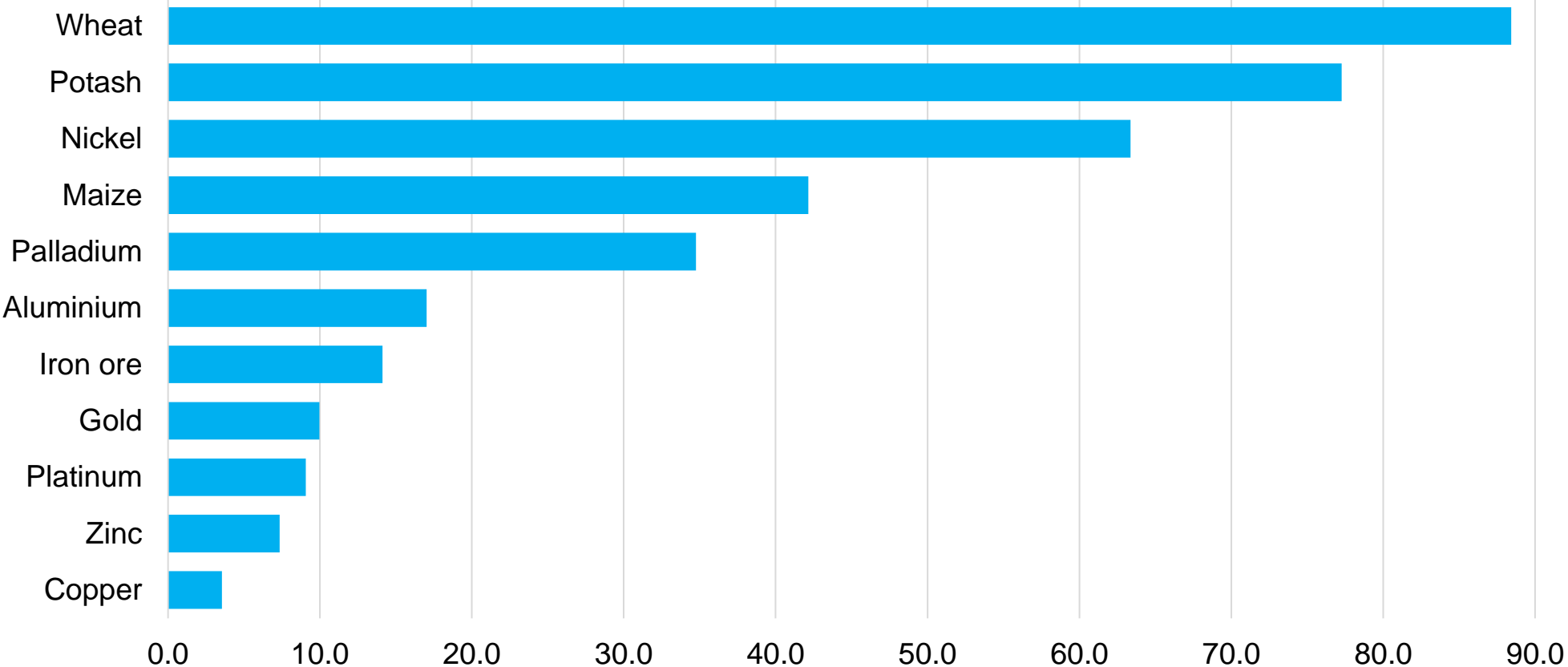
(Bank of Canada commodity price index; to May 2022; 1972m1 = 100)



Source: <https://www.bankofcanada.ca/rates/price-indexes/bcpi/>

Commodity Prices Excluding Energy

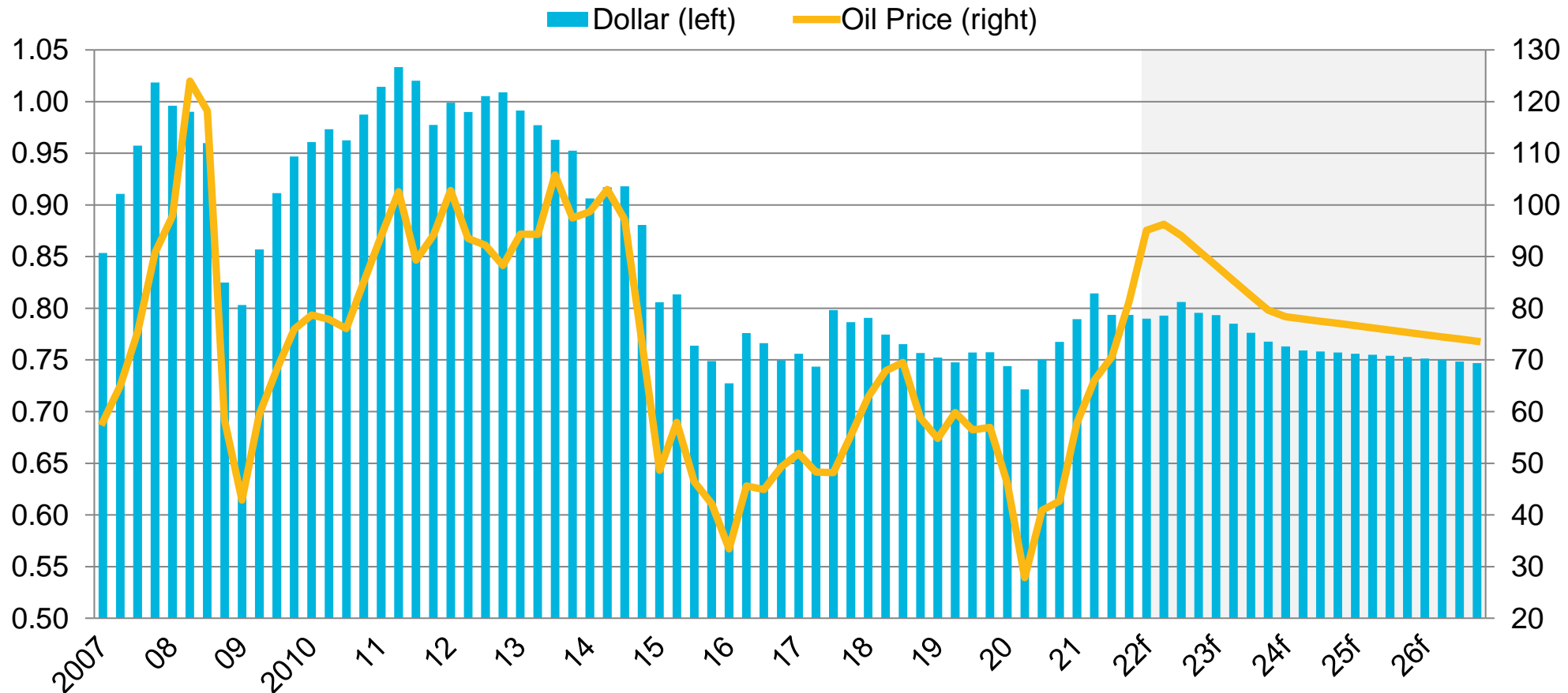
per cent change in USD, Feb 24 to Mar 14 over average of January 2022



Source: OECD at <https://www.oecd.org/economic-outlook/>

Oil's Wild Ride

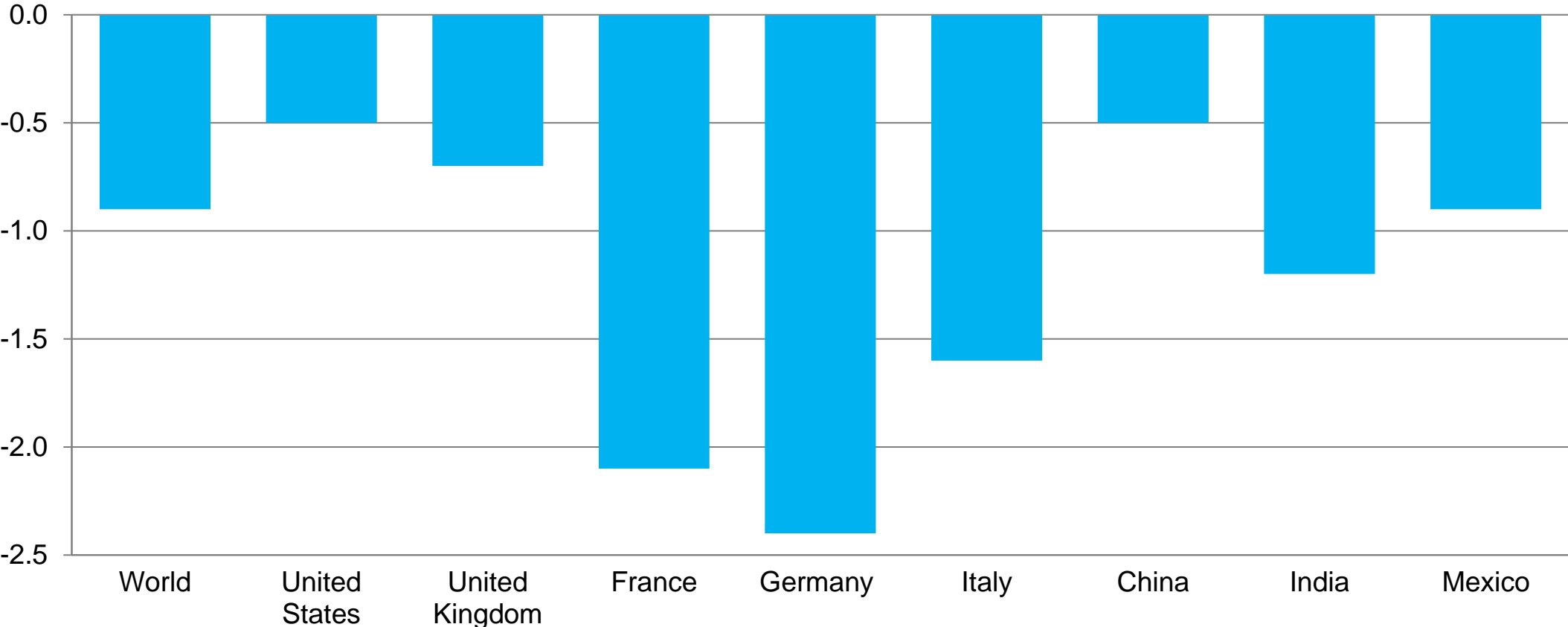
(WTI \$US, \$US/\$C)



Sources: U.S. Energy Information Administration; Statistics Canada; The Conference Board of Canada.

Russia Ukraine War Impacts by Country in 2022

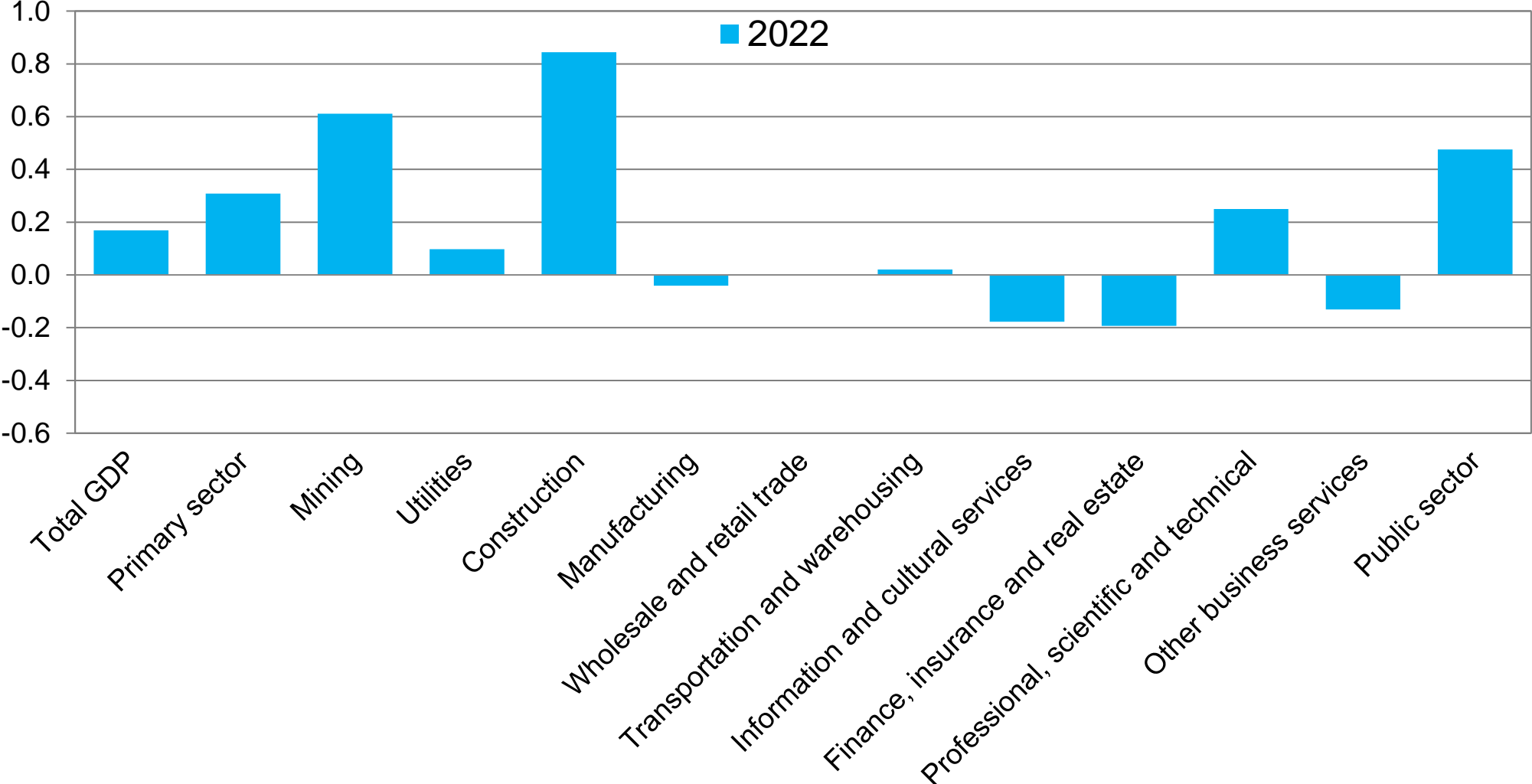
Real GDP impact, per cent



Source: Conference Board Inc estimates using Oxford Economics Global Economic Model

Impact on Canada

real GDP impact, per cent



Source: The Conference Board of Canada.



United States Economy

Rebound Exposes Supply Constraints

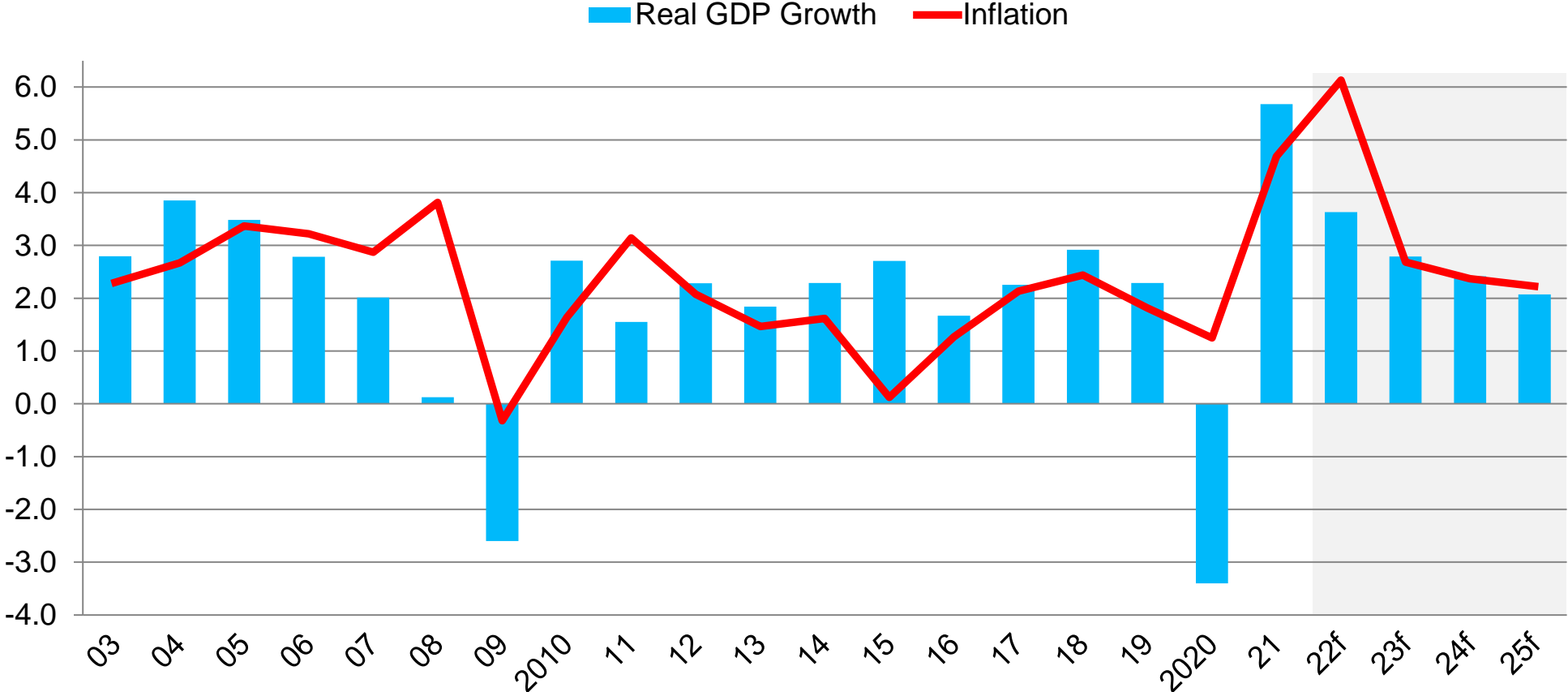
U.S. Outlook



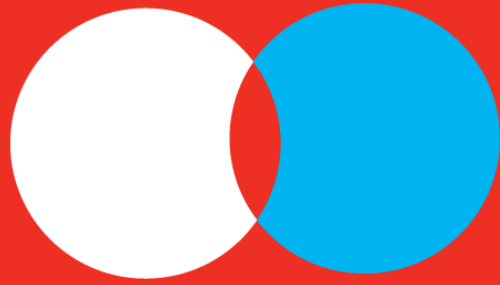
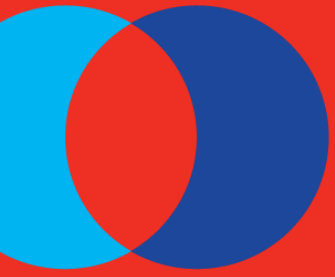
- The U.S. economy has recovered from the pandemic disruption much faster than anticipated. We expect real GDP to expand by 3.6 per cent this year and 2.8 per cent in 2023.
- Omicron has had a far less severe impact on the economy than originally anticipated. Over the first three months of the year, employment surged by 1.6 million and the unemployment rate fell to 3.6 per cent in March. The war should have little impact on U.S. labour markets.
- Inflation is skyrocketing, bolstered by soaring gasoline prices and higher food prices linked to drought conditions in the Western part of the country and, most importantly, the ongoing disruption in global supply chains.
- The Fed is tightening down on monetary stimulus, but it may be difficult to beat back inflation expectations.
- To date, consumers have shrugged off the effects of higher inflation and continued to spend—possibly dipping into the excess savings built up during the recession.

Weaker but Still Solid Growth

United States real GDP and inflation, per cent change



Sources: BEA; The Conference Board of Canada.



Canada's Outlook

Short-term gain, long-term pain

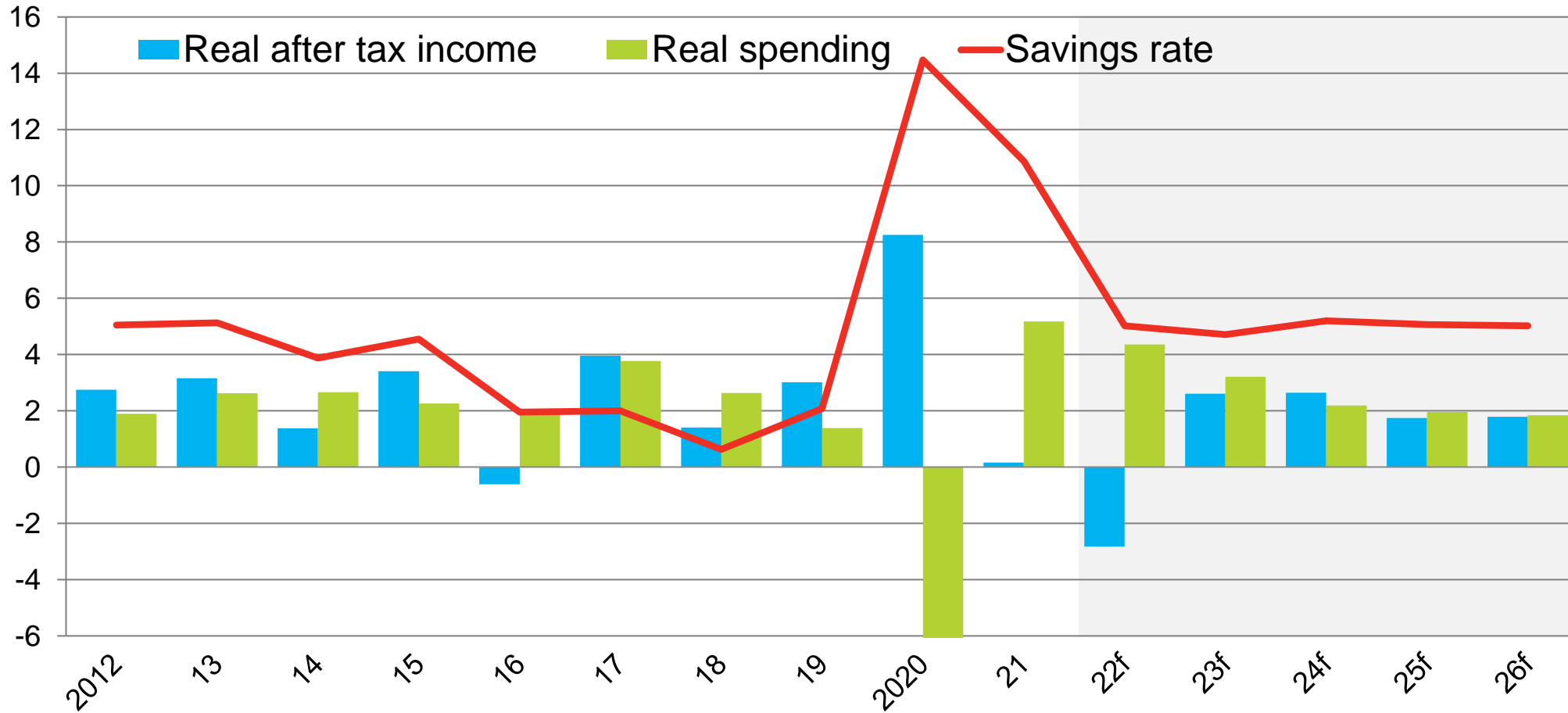
Like no Other Recession



- Massive fiscal support has allowed most households and businesses to come through the pandemic unscathed, despite the deep recession and job losses
- Household balance sheets are in great shape—labour market recovery will boost confidence and consumer spending
- Business profits soar to peak levels but spending on structures and machinery is lagging
- Exports and resource prices bolstered by global recovery
- We may finally see borders reopening, helping to boost tourism, air transportation and aerospace manufacturing sectors

Record Growth in Household Income

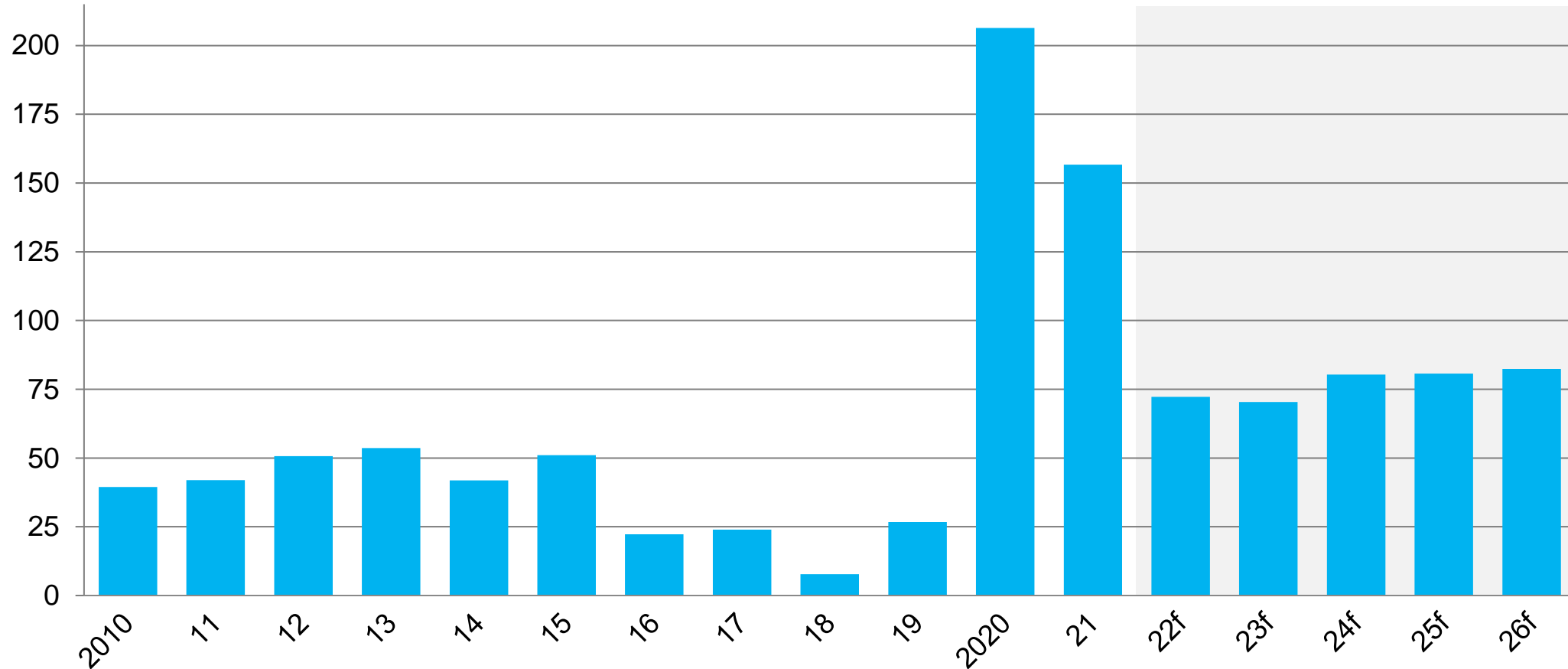
per cent change, per cent (savings rate)



Sources: Statistics Canada; The Conference Board of Canada.

Household Balance Sheets Swell

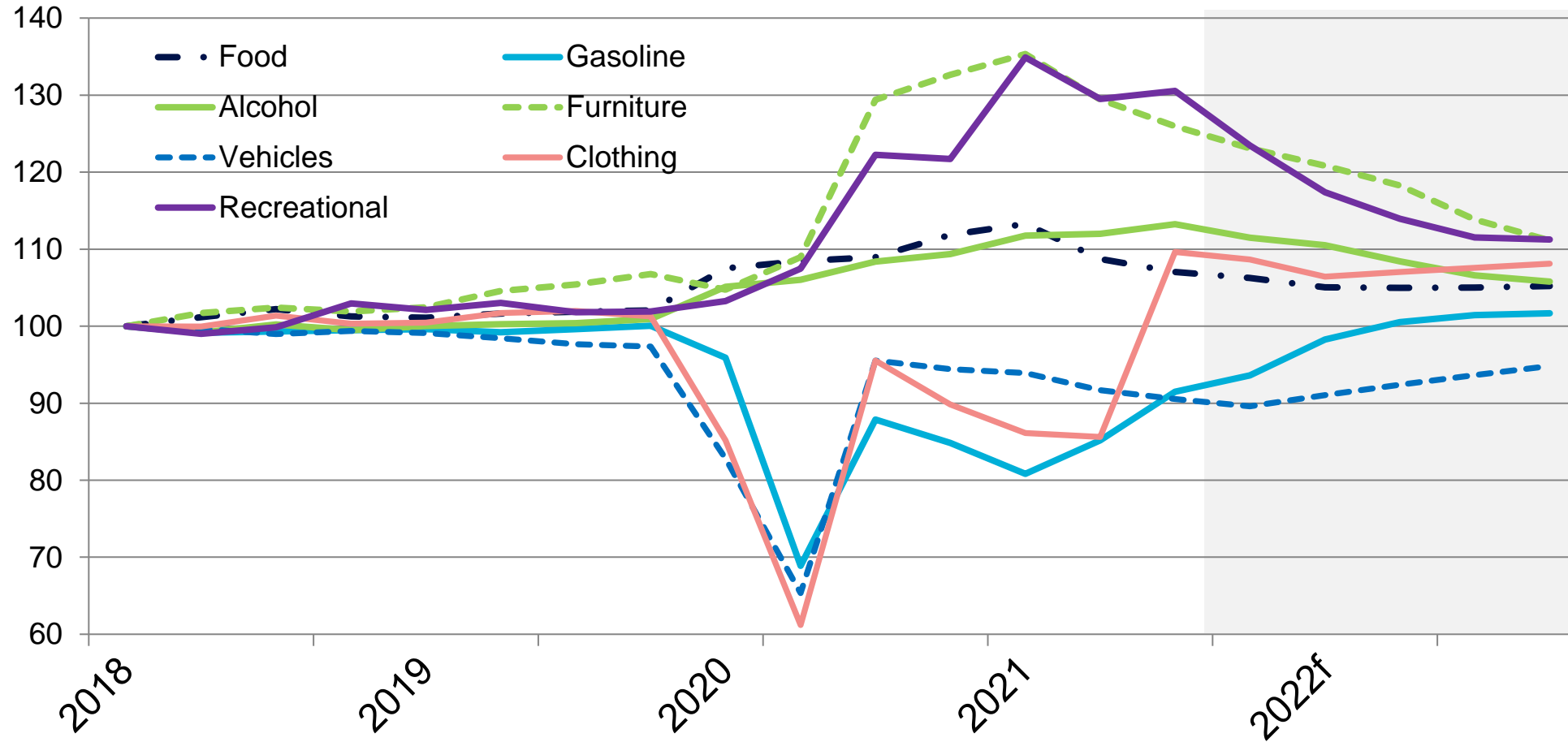
aggregate household net savings, \$ billions



Sources: Statistics Canada; The Conference Board of Canada.

Boom-bust segments should converge

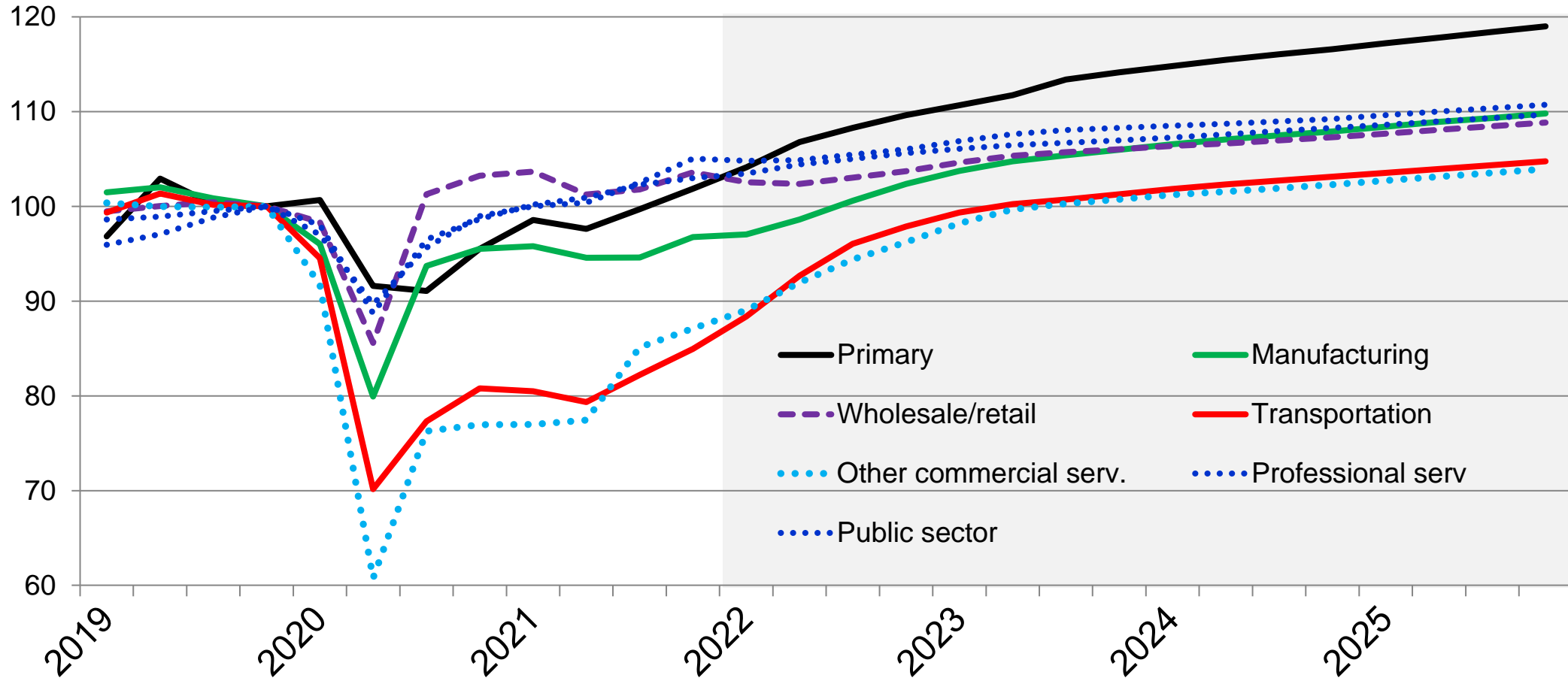
Real consumer spending by category, indexed to 2018Q1=100



Sources: Statistics Canada; The Conference Board of Canada.

Economic Rebound by Industry

Real GDP, selected industries, indexed to 2019Q4 = 100



Sources: Statistics Canada; The Conference Board of Canada

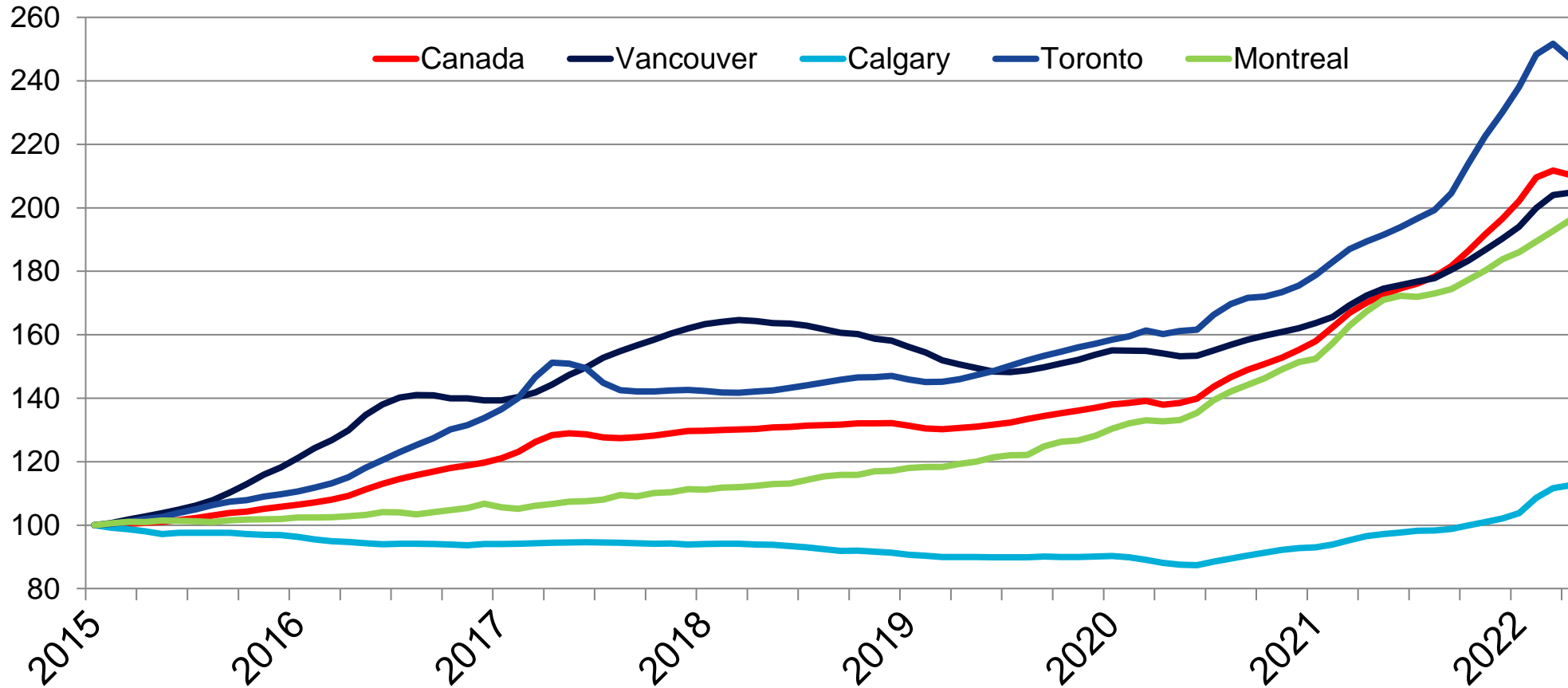
Telework and Frothy Real Estate Markets Prompt Homeowners to Take on More Debt



- Households reduced their credit card and line of credit balances by \$10 billion and \$12 billion respectively
- They, however, took on more mortgage and home equity line of credit (HELOC) debt, causing total credit liabilities to increase by \$184 billion between the fourth quarter of 2021 and 2020
- The rise of interest rates and drying up of government support, may pose a threat to household financial health as more disposable income is needed to service debt payments
- This will become evident over the next three to five years as mortgages come up for renewal

Home Price Boom Starting to Subside

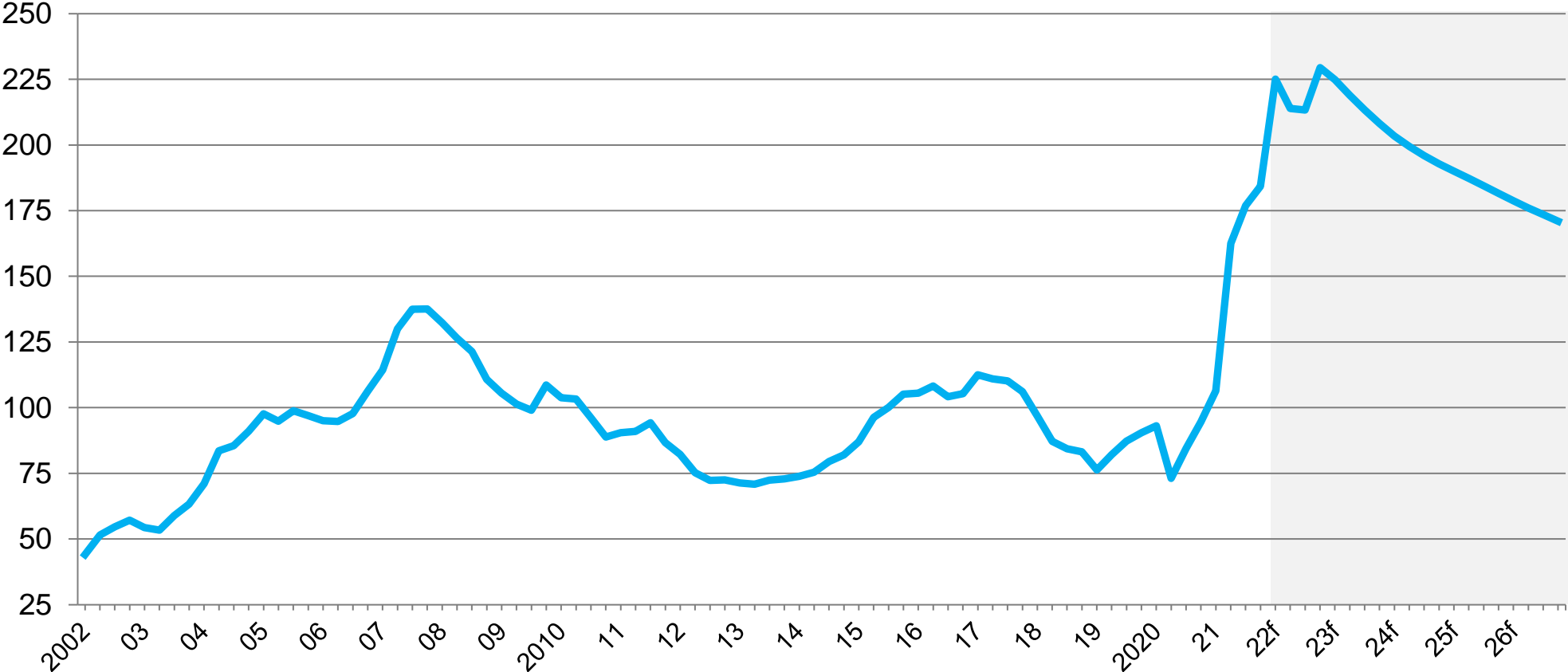
MLS HPI; January 2015 =100; seasonally adjusted; monthly to April 2022



Source: Canadian Real Estate Association.

Total Household Debt Accelerates

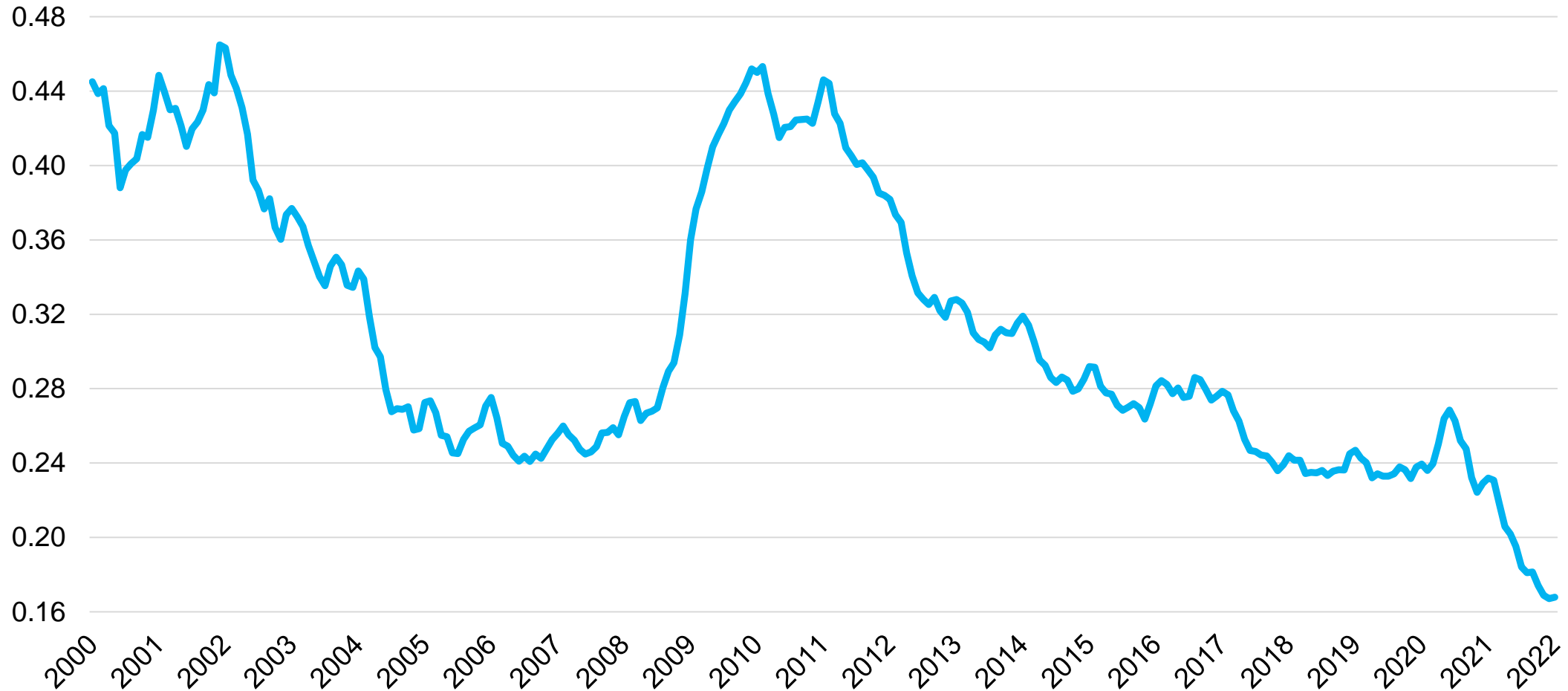
year-over-year change in the annual stock of debt, quarterly, \$ billions



Sources: Statistics Canada; The Conference Board of Canada.

Delinquency Rates Are at Rock Bottom

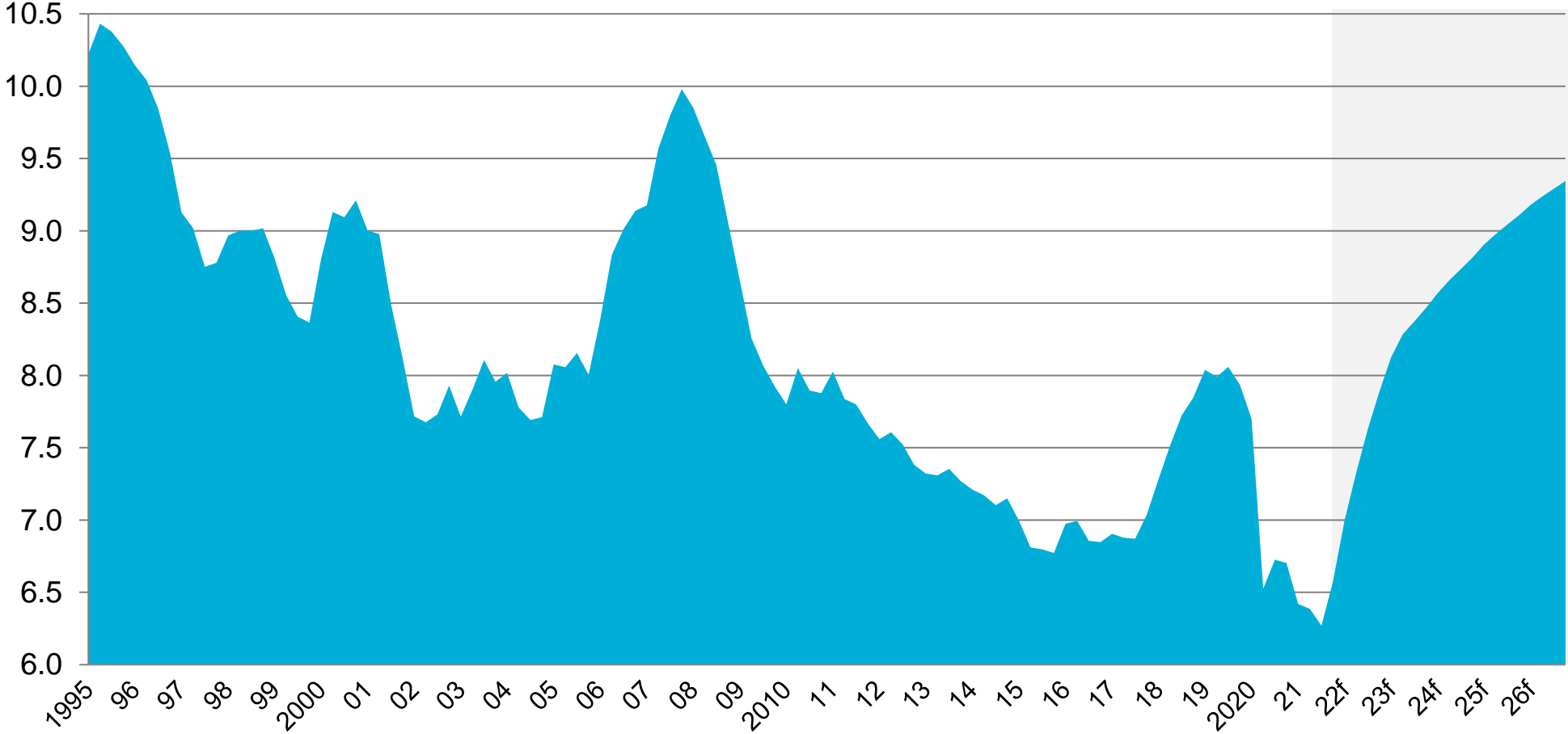
Mortgages in arrears, monthly to January 2022, per cent



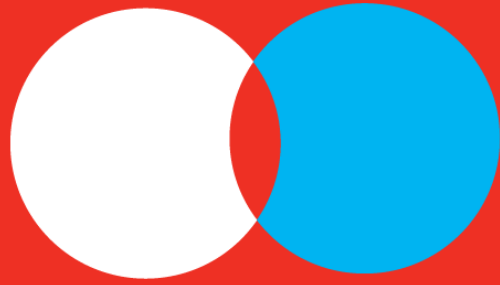
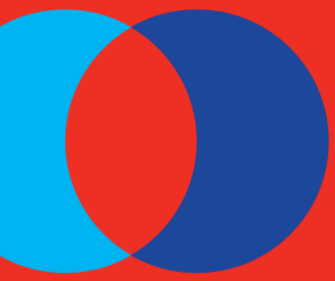
Source: Canadian Bankers Association.

Interest Payments will Take a Bite out of Income

Mortgage and consumer debt service as a share of disposable income, per cent



Sources: Statistics Canada; The Conference Board of Canada.

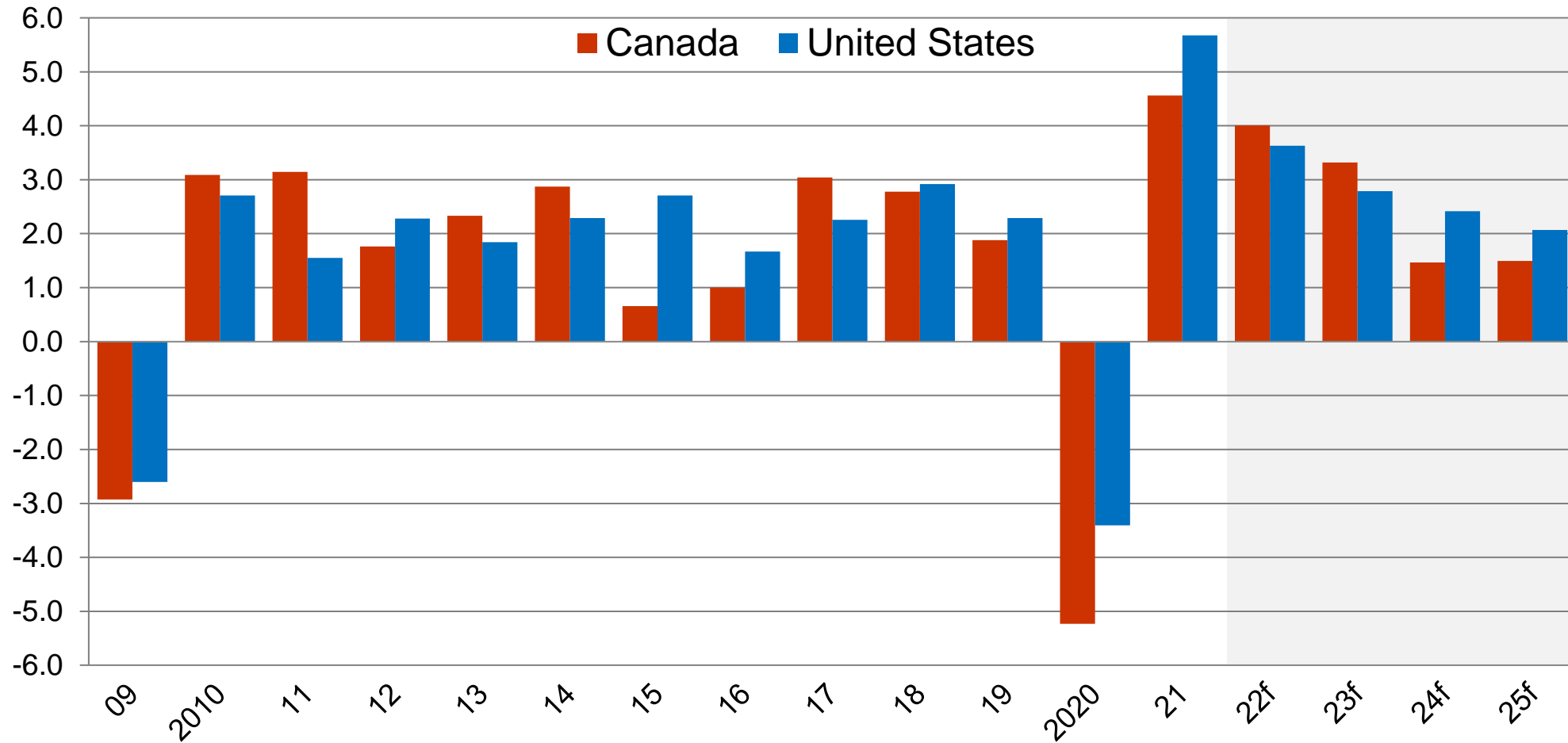


Structural Challenges Erode Growth Potential

A Rebound in Private Investment and Immigration are Needed

Roaring 20's Recovery will be Short Lived

Real GDP growth, per cent change



Sources: Statistics Canada; NBER; The Conference Board of Canada.

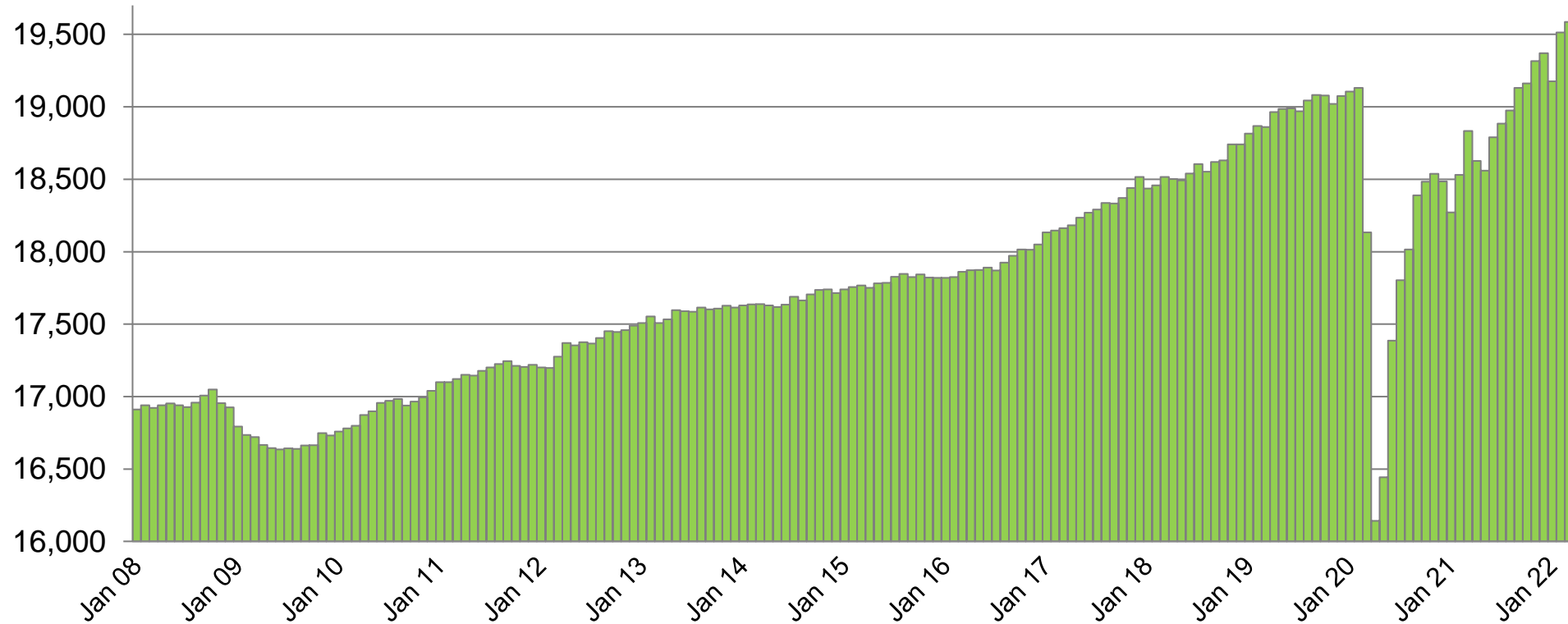
Workforce Implications



- Decline in immigration and non-permanent residents has significantly slowed labour force growth
- Employment has rebounded, despite continued difficulties in some industries and occupations
- Labour markets have tightened markedly, even in comparison to 2019 (a boon year for labour markets)
- Retirements are about to explode and will keep labour markets tight even as immigration numbers recover

Employment Recovers

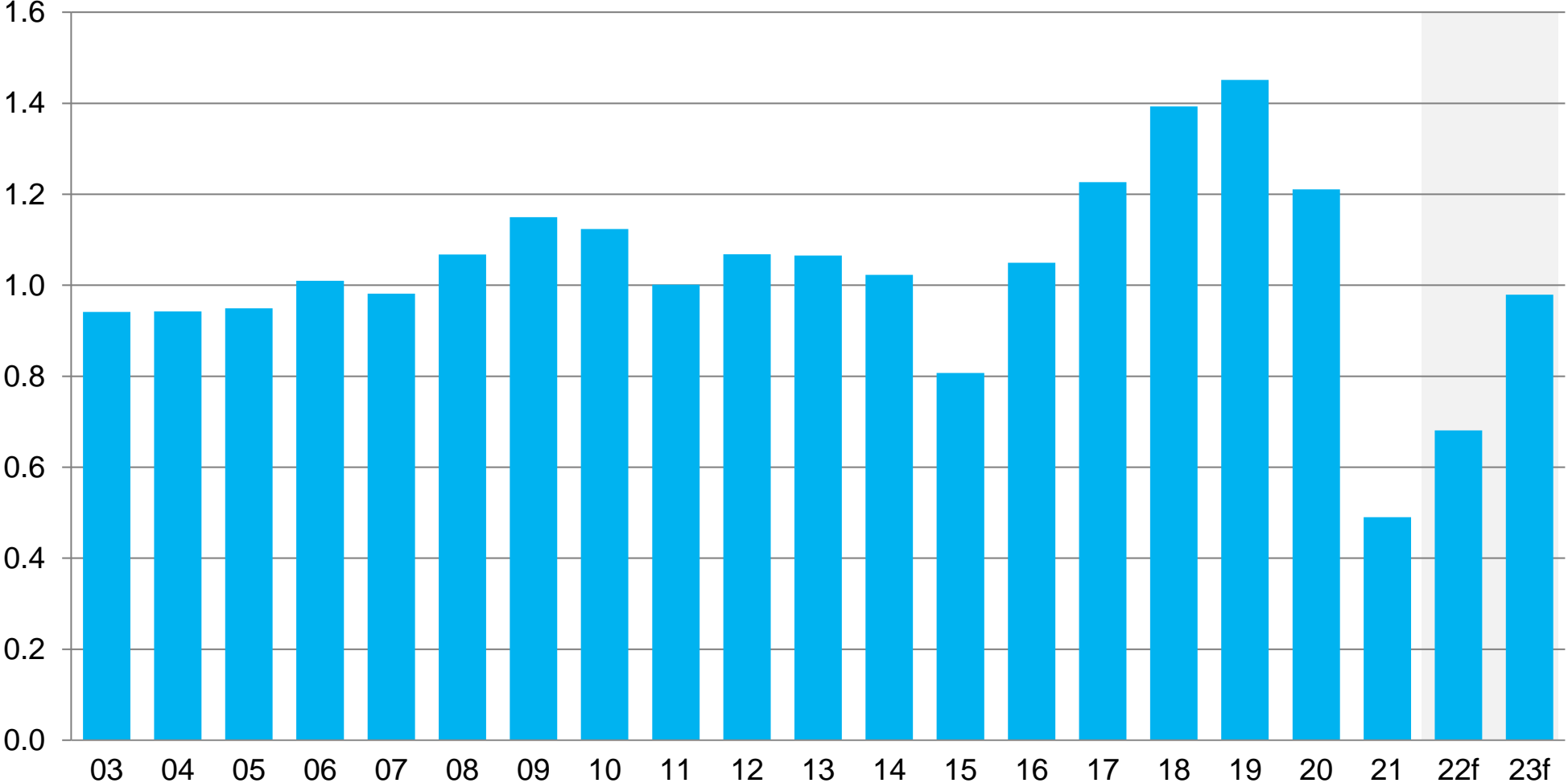
Canada's employed, thousands



Source: Statistics Canada Table: 14-10-0287-01.

COVID-19 put a Halt to Immigration

annual population growth



Sources: Statistics Canada; The Conference Board of Canada.

Job Vacancies On the Rise Especially for Some Occupations



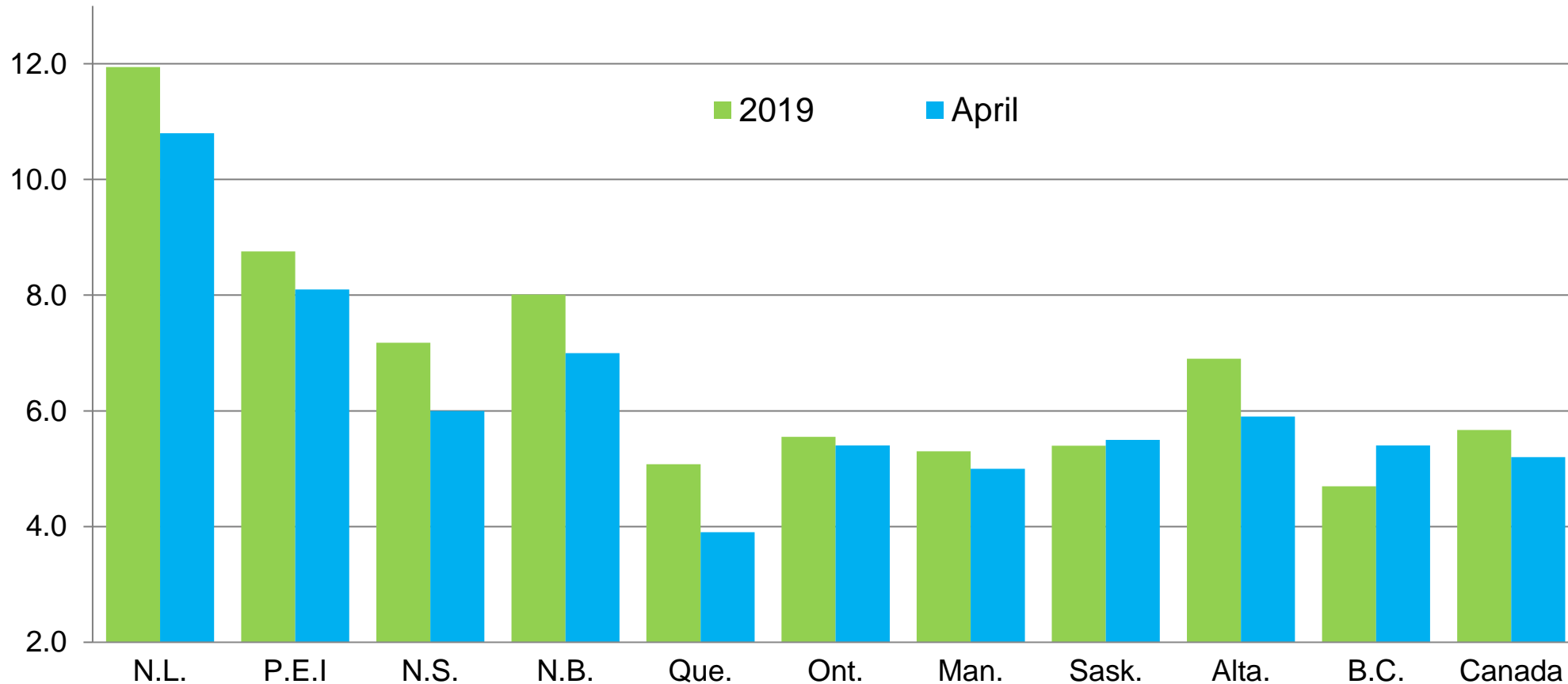
Selected job vacancies, number of vacancies and per cent change from 2019 to 2021

	Average 2019	Average 2021	per cent change	Offered wage increase
Total, all occupations	539,809	778,378	44.2	6.8
Business, finance and administration occupations	58,294	82,564	41.6	4.5
Health occupations	39,235	73,478	87.3	5.7
Occupations in education, law and social, community and government services	34,201	50,969	49.0	2.5
Trades, natural resources, manufacturing, utilities	142,635	205,605	44.1	7.8
Sales and service occupations	181,594	257,123	41.6	6.4

Sources: Statistics Canada Table 14-10-0356-01; The Conference Board of Canada.

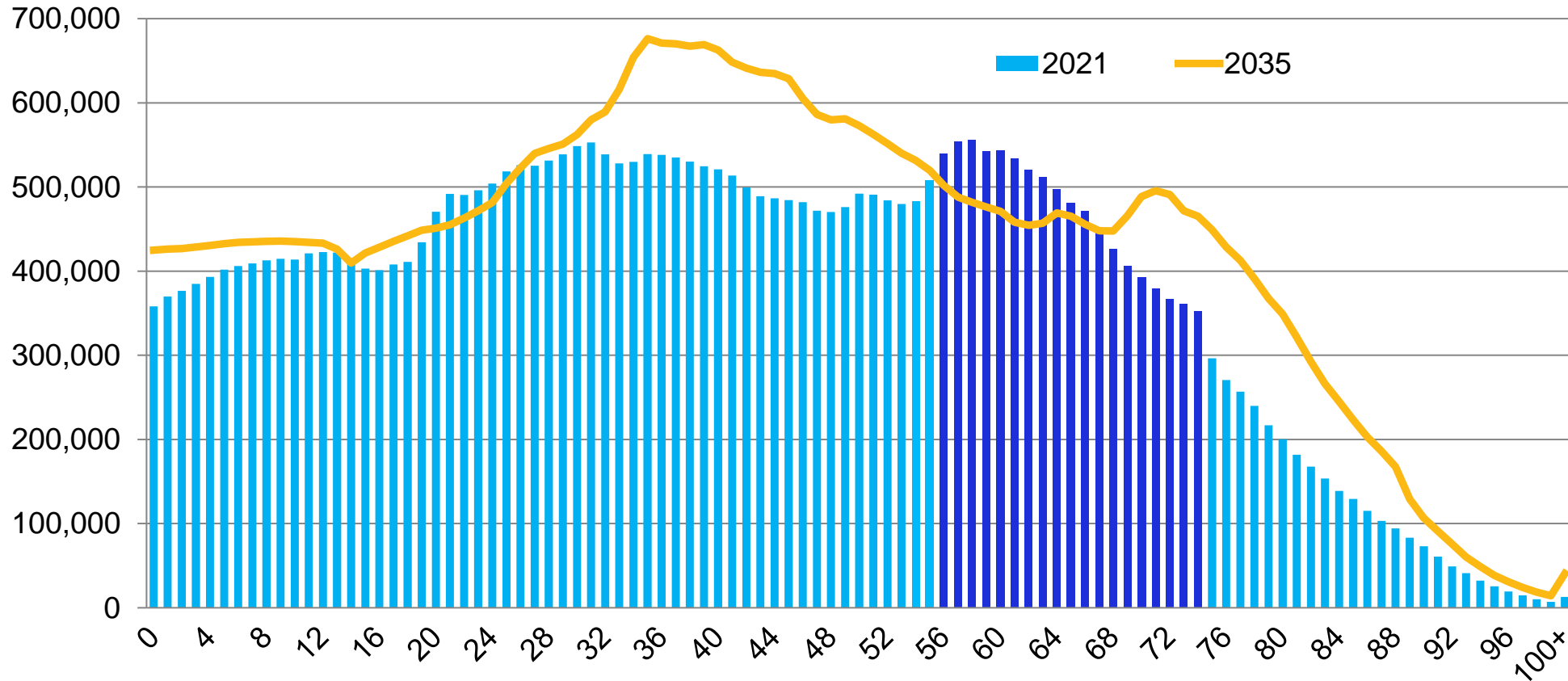
Labour Markets Tight in Many Provinces

Unemployment rates by province, per cent



Source: Statistics Canada Table: 14-10-0287-01.

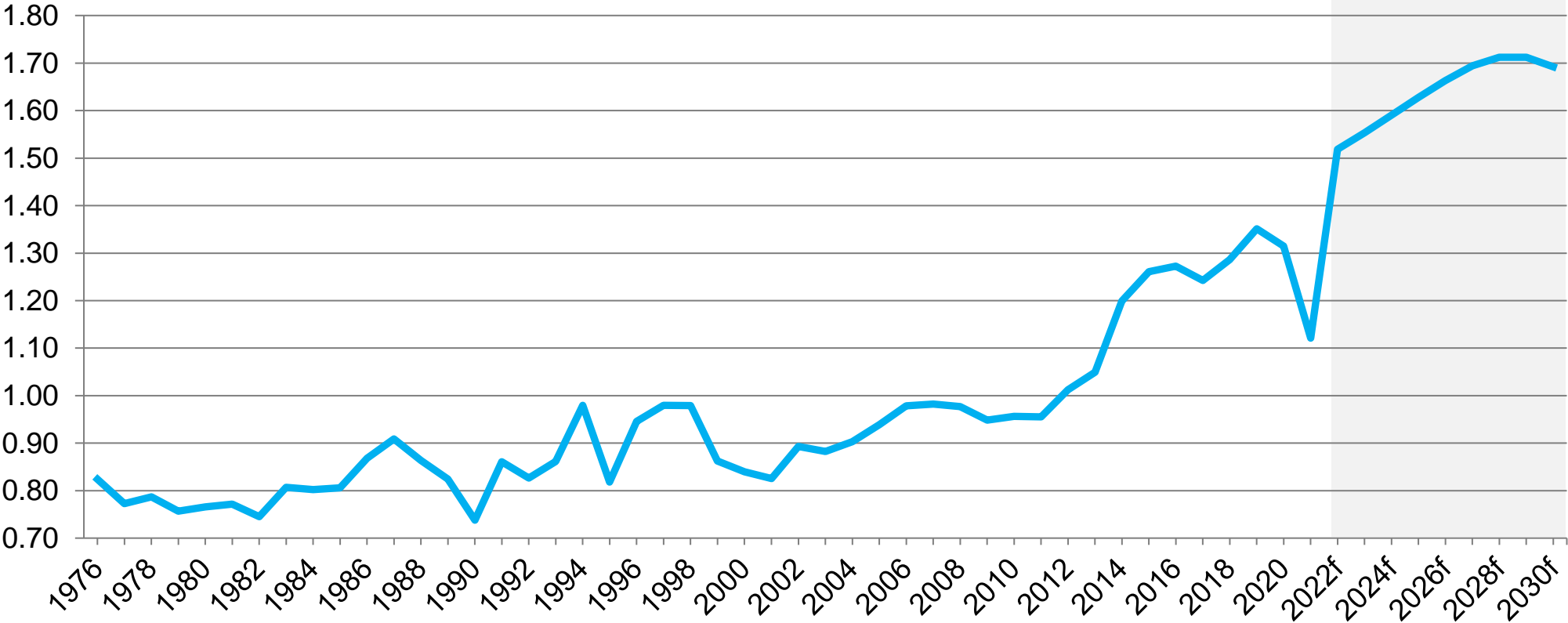
Population distribution by age, 2021 and 2035



Sources: Statistics Canada; The Conference Board of Canada.

2022—The Year of the Retiree

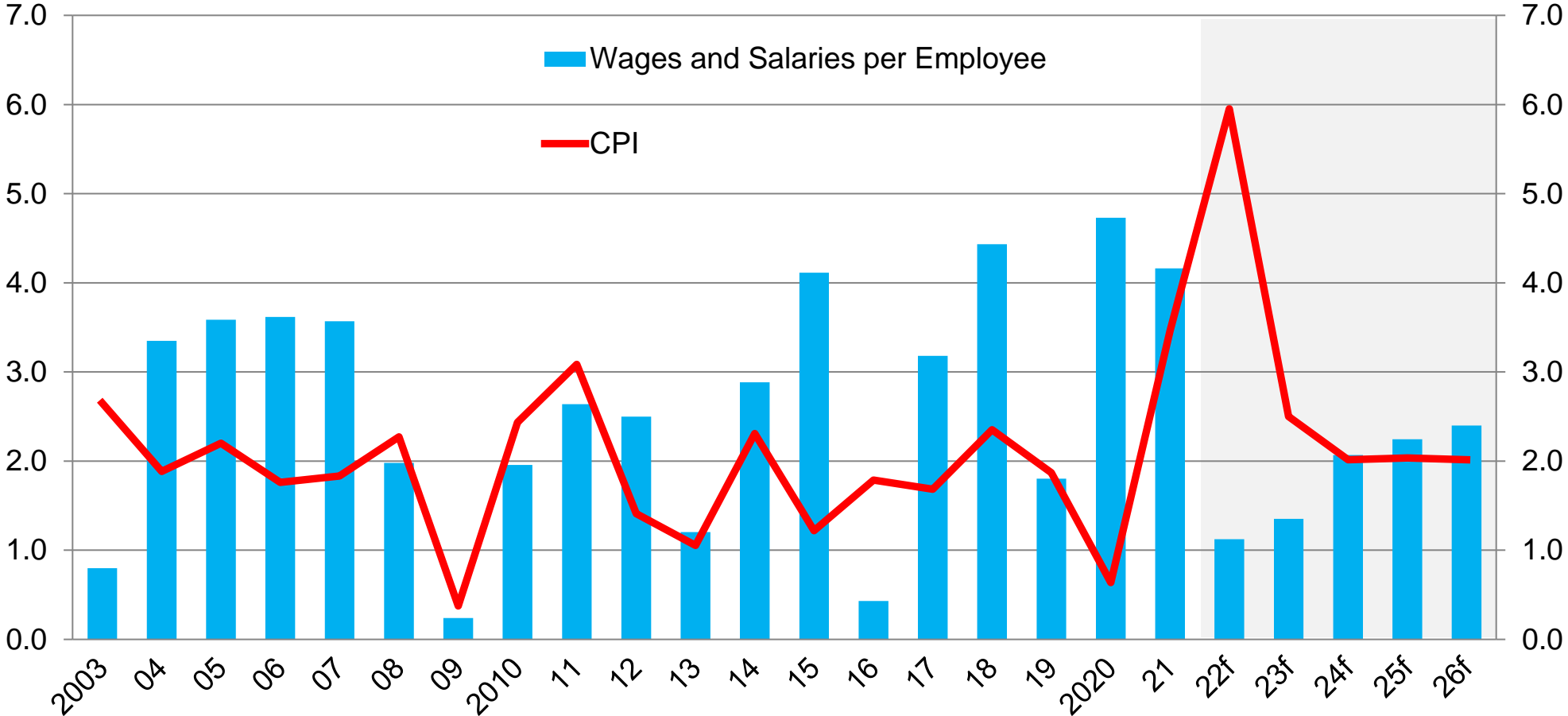
retirements as a share of labour force, per cent



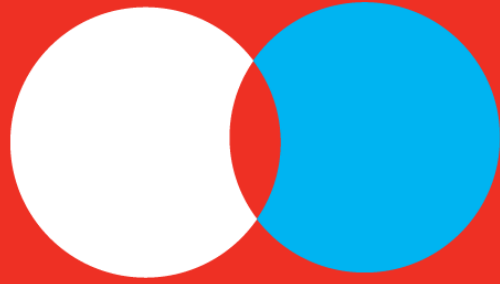
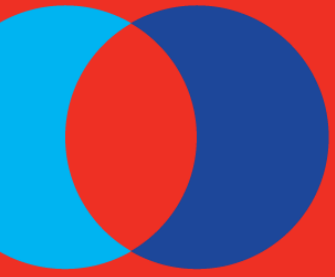
Sources: Statistics Canada; The Conference Board of Canada.

Inflation not Expected to Carry into Wages

per cent change in consumer prices and wages



Sources: Statistics Canada; The Conference Board of Canada.



Private Investment and Trade

Prospects were already dim pre-COVID

Business Bankruptcies are Down but Structural Changes will Weigh on Finances for Many



- Decreased sales have left a higher proportion of small businesses in a particularly fragile position
- Support was provided to small businesses through CEBA and CEWS, among other programs
- Close to 900,000 small businesses were approved for CEBA and CEBA expansions loans (additional \$20,000 on existing CEBA loan)
- The CEWS program supported more than 36 million employees of small and medium sized businesses, who received over \$52 billion—businesses with 25 or fewer employees received \$19 billion of this sum
- Once government support programs run their course, loans come due for repayment, and interest rates begin to rise, there is a risk that we would observe an elevated rate of default

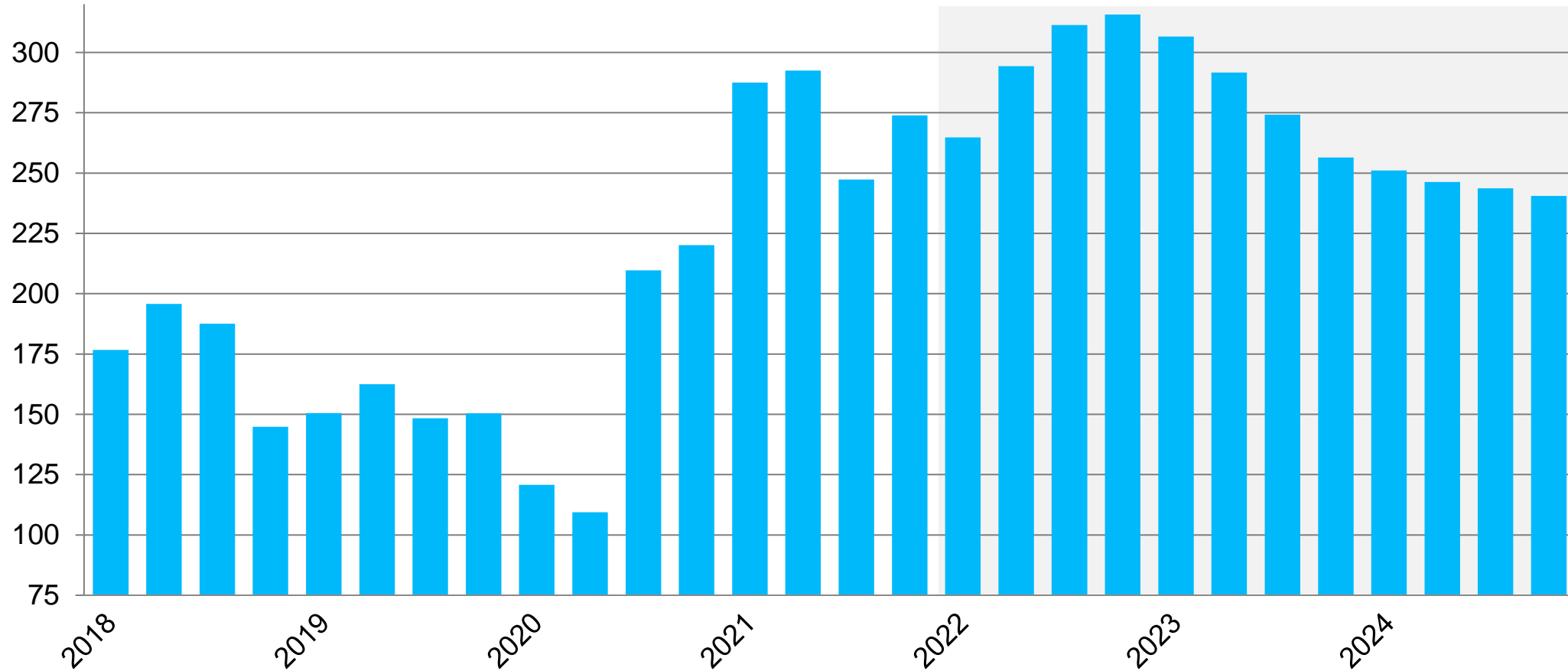
Telecommuting will change the face of Canada's Major Cities



- Downtown office vacancy rate increased 6 percentage points since pre-pandemic—from around 10 per cent in 2019 to 16 per cent today
- As more companies finalize a strategy for the new office design, we can expect to see a further increase in vacant office space in Canada's major urban areas
- Office vacancies may be slow to increase as tenants have kept their leases until they gain a better understanding of their office needs going forward
- Still, we estimate that freed up office space as a percentage of net rentable area could be anywhere between 12 and 32 per cent, depending on what portion of the current additional 3 million teleworkers remain in their home offices (15 to 25 per cent) and the square footage per office worker (130 to 200 square feet)
- Could be partially offset by the need for more office space per worker as we come out of the pandemic but the implications for downtown activity will be substantial

Profits Hit a Record but will Investment Follow?

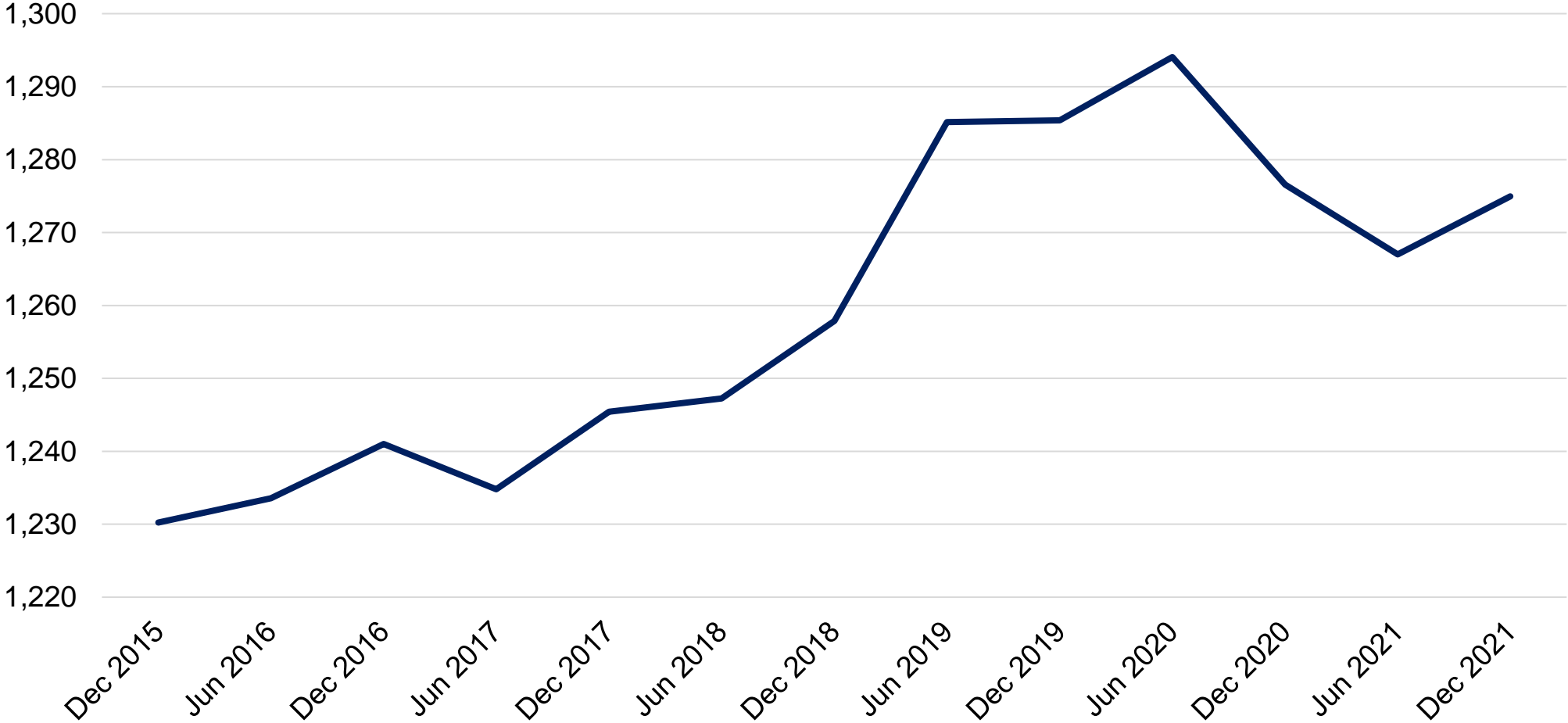
corporate profits in Canada before taxes, \$ billions



Sources: Statistics Canada; The Conference Board of Canada.

Small Business Count Peaked in 2020

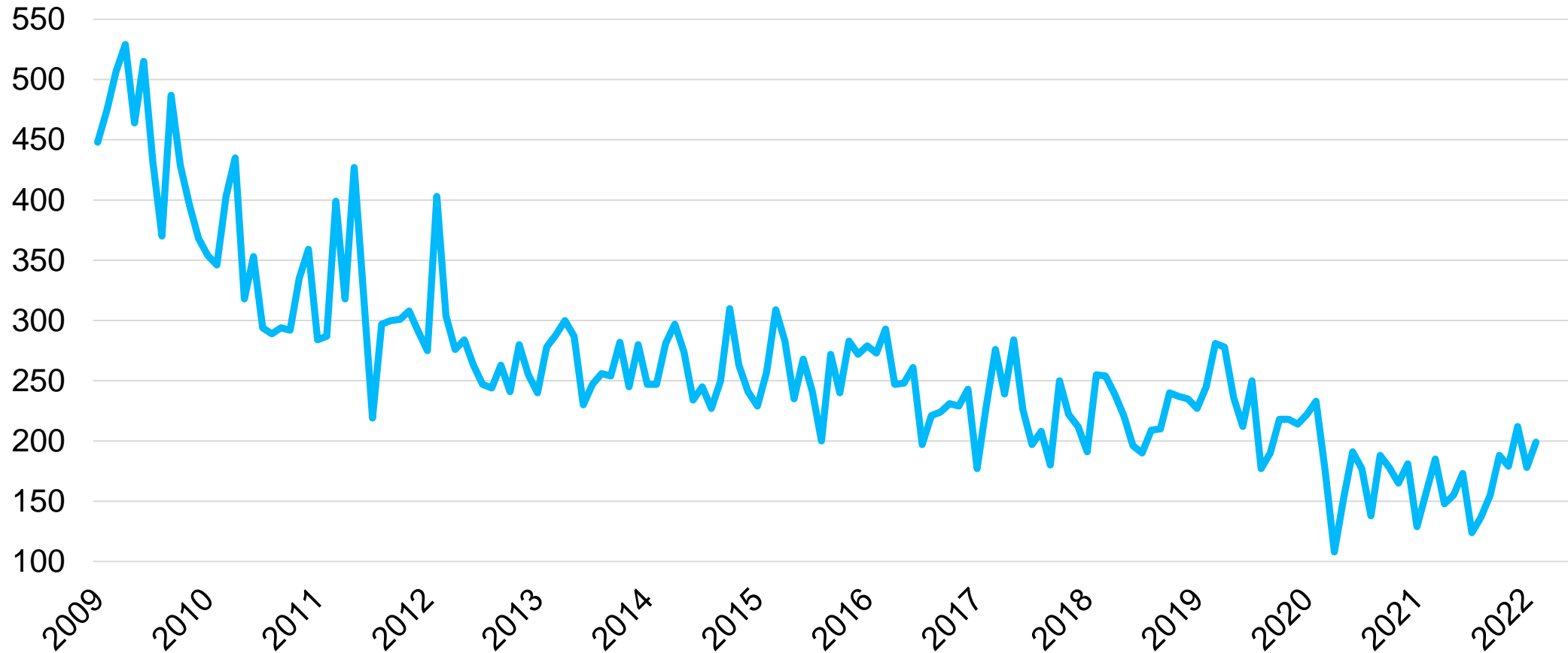
Number of businesses with 1 to 99 employees; 000s; biannual survey



Source: Statistics Canada Table 33-10-0214-01.

Business Bankruptcies Inching Up?

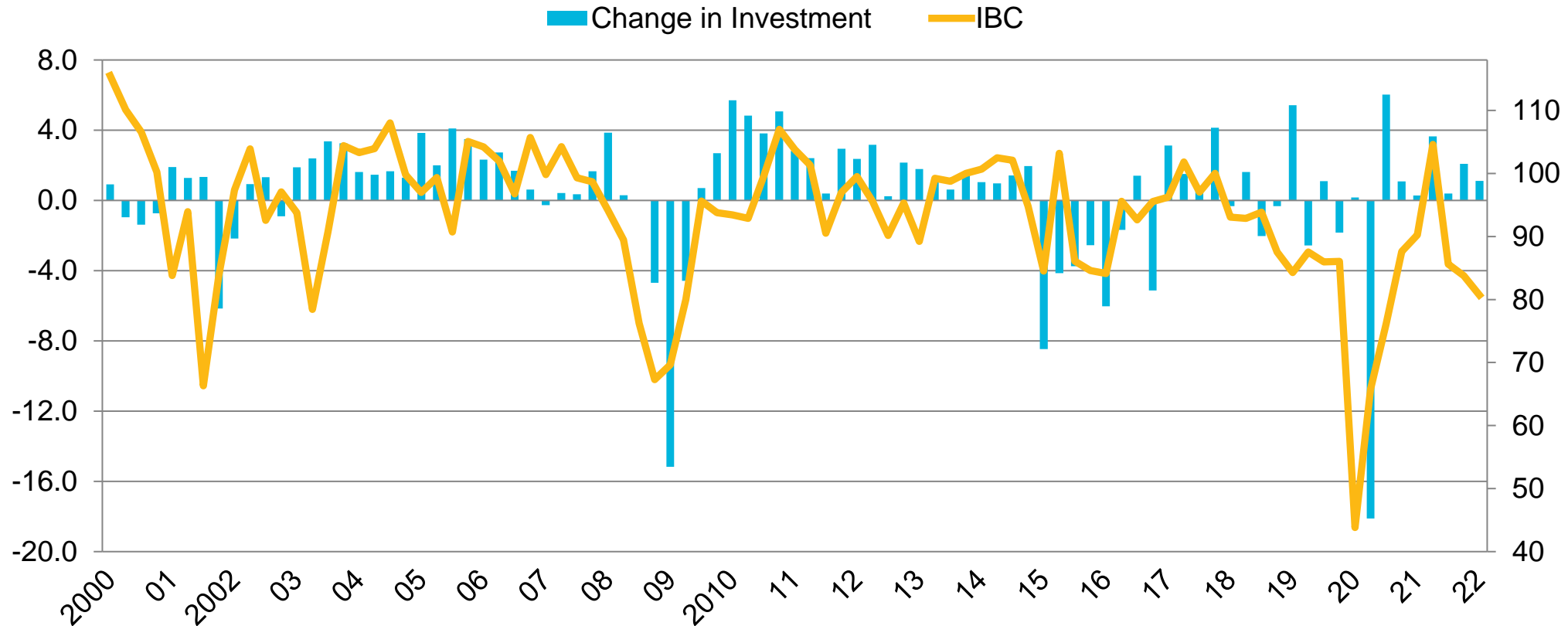
Business bankruptcies in Canada, monthly to February 2022



Source: Office of the Superintendent of Financial Institutions (OSFI).

Index of Business Confidence

Private plant & equipment investment (quarterly percentage change, left scale); Index (2002=100, right scale)



Sources: Statistics Canada; The Conference Board of Canada.

Cost of Labour and Capital Holding Back Investment

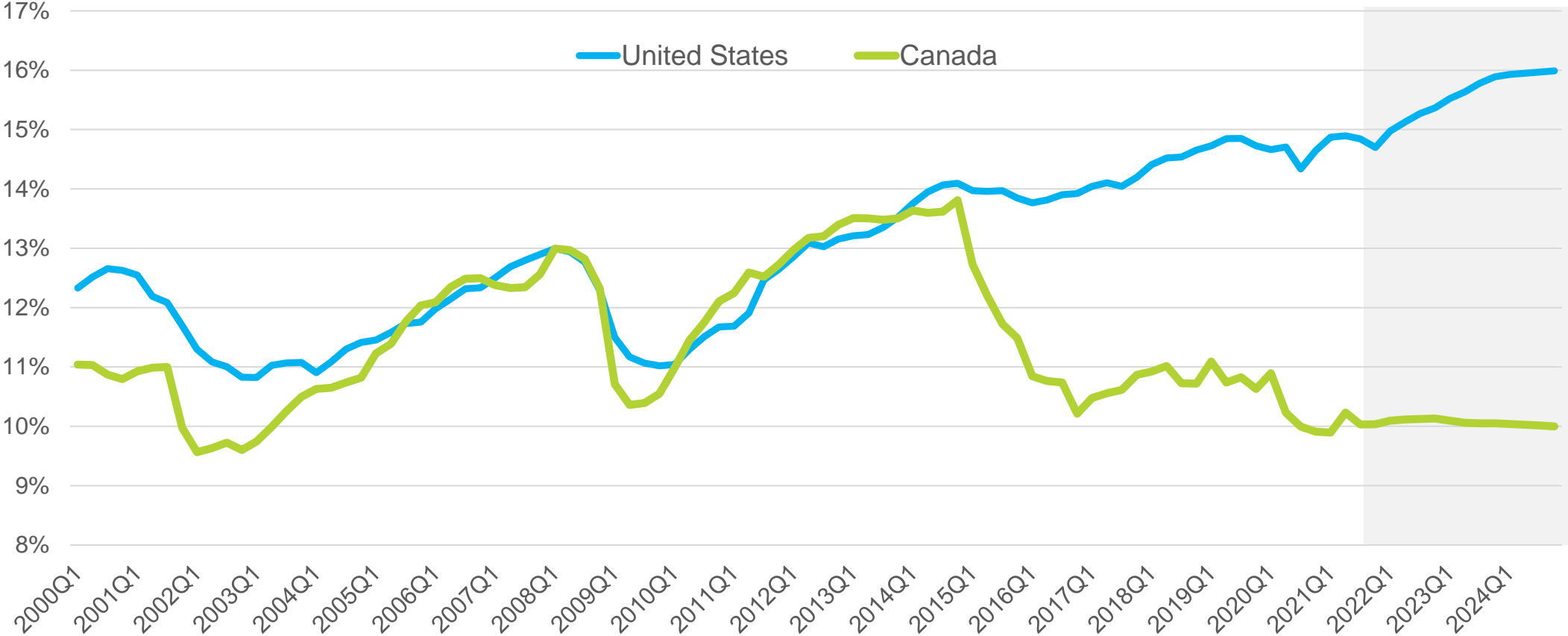
factors, if any, currently adversely affecting the level of your planned expenditures in Canada;
per cent of survey responses



Source: The Conference Board of Canada.

Canada's Investment in the Doldrums

real business investment as a share of GDP; per cent



Sources: Statistics Canada; Bureau of Economic Analysis.

The Bottom Line...



- Canada's near-term growth will remain strong as effects of COVID-19 wane
- High resource prices will boost profits and exploration, but new development may be slow to increase
- Longer-term, Canada's economic prospects are held back by capacity constraints because of weak growth in private investment and labour force
- Resource sectors could benefit from lasting energy and supply-chain transitions, but private investment is needed
- Household and government debt will hold back future spending

Are There Silver Linings?



- Despite weak investment Canada's productivity performance has improved in recent years
- Knowledge based workforce, employment in professional services is driving growth; employment for those with university education has increased strongly through the pandemic
- The Pandemic has accelerated tech adoption in many sectors, this provides an upside risk to Canada's longer-term prospects
- Adoption of technology, telehealth could help governments deliver public services more effectively

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