PROVINCIAL ECONOMIC FORECAST

TD Economics

September 29, 2016

REGIONAL DIVERGENCE TO DIMINISH

Highlights

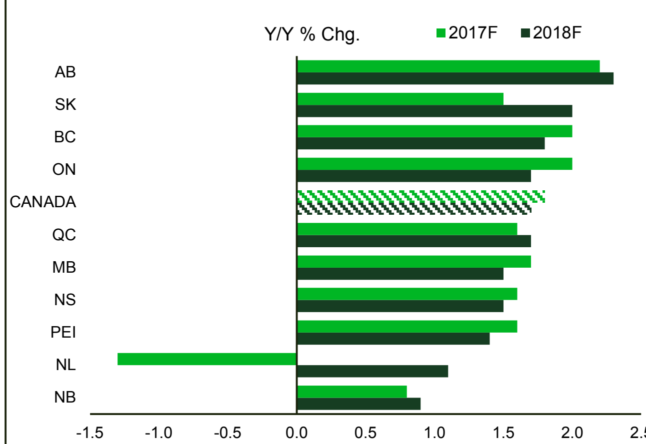
- For the second straight year, the overriding theme in 2016 remains the unusually large gap in economic performances between the top performing provinces (B.C. and Ontario) and those at the bottom of the charts (Alberta, Newfoundland and Labrador, and Saskatchewan).
- However, the regional divergence should begin to diminish next year, as most resource-based economies begin to bounce back – albeit from very low levels – and a cooling in the housing market takes some steam out of B.C. and Ontario. The recovery in Newfoundland and Labrador will be delayed until 2018, as the economy is still facing several headwinds.
- By 2018, Alberta and Saskatchewan will sit at the top of the leaderboard with growth at or above 2%. However, for these provinces, this is a muted rebound compared to past experiences. Meanwhile, growth in Ontario and B.C. will fall short of 2%.
- In the remaining provinces, the picture of subdued growth in the 0.5-2% range will remain in place. This is in line with the longer term cruising speeds in these regions, which continue to be challenged by weak population growth.

For the second straight year, the overriding theme in 2016 remains the unusually large gap in economic performances between the top performing provinces (B.C. and Ontario) and those at the bottom of the charts (Alberta, Newfoundland and Labrador, and Saskatchewan). The weak oil price environment has continued to take its toll on the struggling oil-producing regions, particularly with respect to investment in the sector. Meanwhile, robust housing markets and related spillover effects are providing an enormous boost to the leaders, masking the disappointment seen in manufacturing and exports.

Looking ahead, the next two years will likely shape up differently, with growth differentials poised to narrow. Oil-related investment will stabilize after a two-year tailspin and an expected gradual uptick in oil prices to above US$50 per barrel. Bouncing up from the bottom, Alberta and Saskatchewan will move back to the coveted position of sitting at the top of the leaderboard in 2018, marked by growth at or above 2%. However, for these provinces, this is a muted rebound compared to past experiences, and will barely bring the level of GDP back to that recorded in 2014. The recovery in Newfoundland and Labrador will take even longer to materialize, although the province will return to positive growth territory by 2018.

On the flip side, housing-led strength has already begun to fade in British Columbia, and Ontario's all-important Toronto market is expected to follow suit in 2017, but to a lesser degree. The anticipated moderate correction will not be enough to severely dampen economic activity, but it will be sufficient to dip growth back down below 2% by 2018. Critical to this forecast is that exports take up the growth-baton in both provinces, with better momentum stemming from the recent improvement in U.S. demand.

CHART 1: REAL GDP GROWTH BY PROVINCE



Source: Statistics Canada. Forecast by TD Economics as at September 2016.

Outside of these five provinces, the picture of subdued growth

Beata Caranci, VP & Chief Economist, 416-982-8067
Michael Dolega, Director & Senior Economist, 416-983-0500
Dina Ignjatovic, Economist, 416-982-2555

@TD_Economics

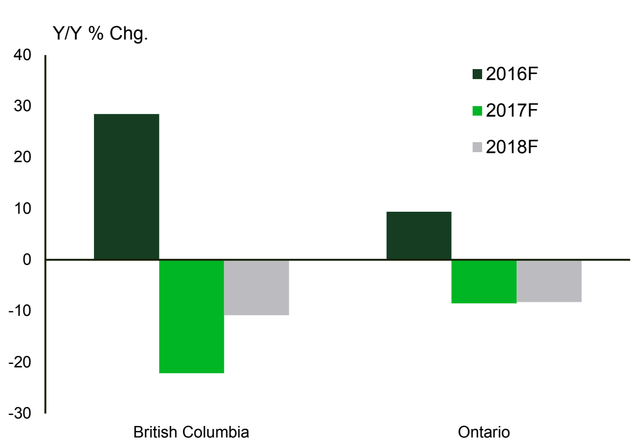
in the 0.5-2% range will remain in place next year and in 2018. This is in line with their modest longer-term cruising speeds and reflects economies that have been relatively immune to the same cyclical forces buffeting Ontario, B.C. and the oil-driven provinces. Increases in infrastructure spending, manufacturing and tourism will help support economic activity in these regions. However, in general, weak population gains will critically challenge their upside potential.

Housing to knock B.C. and Ontario off the top

The housing market has been a key driver underpinning the expansion in Canada's fastest growing regions of B.C. and Ontario. With activity expected to moderate over the next 1-2 years, this recent source of growth advantage is likely to transform into one of disadvantage.

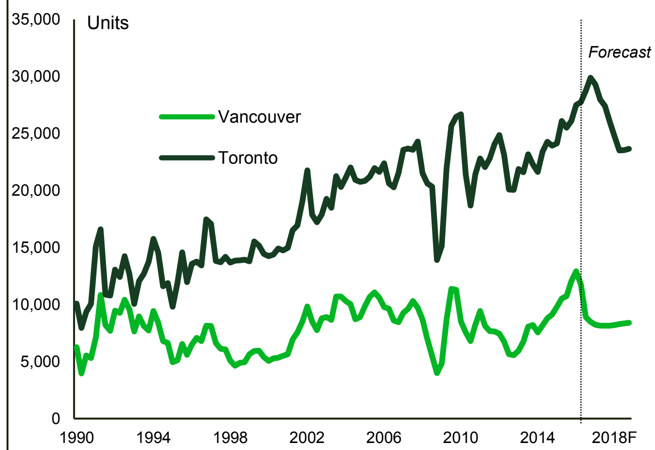
B.C. – and Vancouver in particular – is no stranger to the cyclicality of the housing market. And after three strong years of defying gravity, a down cycle appears underway. While new home construction is up by about 40% so far this year – a welcome development given the limited supply – the pace is unsustainable and is likely to be unwound, with double digit declines in housing starts expected in 2017 and 2018. Moreover, signs that sales are losing momentum have already surfaced – with August's 18% plunge pushing sales below year-ago levels for the first time in more than three years. This sizeable decline was due in large part to the implementation of the foreign buyer's tax that came into effect at the start of the month. While some of this extreme weakness may reverse in the coming months, the new tax should keep a lid on sales into at least early-2017. What's more, the recent cooling in the market may also spook domestic buyers, limiting both demand and price growth next year.

CHART 2: HOUSING STARTS



Source: CMHC, TD Economics.

CHART 3: EXISITING HOME SALES



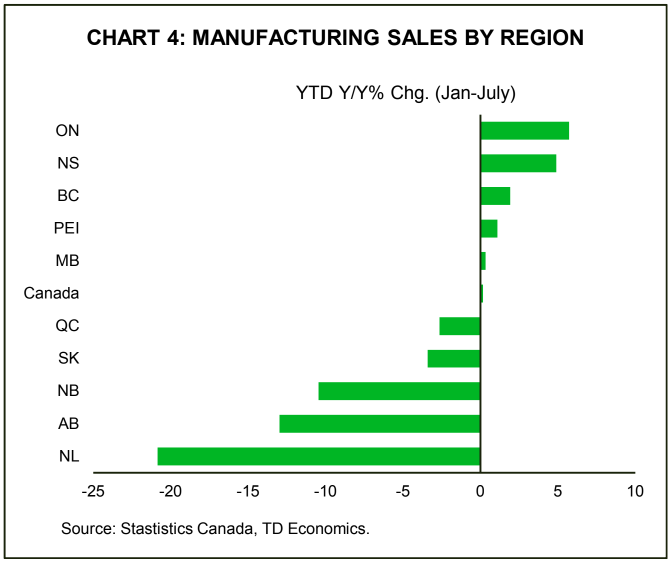
Source: CMHC, TD Economics

In contrast, sales and prices in Ontario – particularly Toronto – have remained on a tear, and demand may strengthen even further as foreign buyers shift away from Vancouver following the implementation of the new tax. However, affordability is eroding quickly and the current pace of sales and price growth is unsustainable. As such, the market is ripe to cool by the second half of next year. Homebuilding activity in the province – which is expected to rise by 9% this year – is set to decline sharply over the next two years, also weighing on economic growth.

As their housing markets come down from the stratosphere, B.C. and Ontario will be looking to other sectors to drive growth. Manufacturing and exports should provide some support, in line with economic activity south of the border. But, challenges remain. The expiration of the Softwood Lumber Agreement in October could mean that B.C.'s lumber sector is hit with tariffs if a new deal is not reached. In Ontario, the manufacturing sector will likely be held back due to the planned closure of a GM plant in Oshawa next year. So, while the manufacturing sector as a whole should be supportive of growth in the coming years, the strength won't be sufficient to completely counteract waning activity in the housing market. After advancing by close to 3% this year, overall growth in these provinces is set to slide to a still healthy 2% in 2017, and just under that in 2018.

Manufacturing and construction to prop up Manitoba and Quebec

Increased demand for Canadian-made goods will also support manufacturing in Manitoba and Quebec, which has been quite disappointing so far this year. Indeed, after



a strong start to 2016, manufacturing in Manitoba has been trending down over the last few months. This should reverse course in the second half of this year and into 2017, in line with an uptick in the U.S. economy.

Manitoba's economy will also be supported by growth in non-residential construction, as a number of key infrastructure projects are on tap, including those related to new hydro development, transmission lines, and pipelines, as well as a number of commercial projects in Winnipeg. On the flipside, the recent unexpected closure of the Port of Churchill may provide some modest offset to growth, as it could hinder transport and trade that would typically move through the port. While slowing from this year's 2.3% pace, Manitoba is still expected advance at a decent clip of 1.7% in 2017 and 1.5% in 2018.

In Quebec, manufacturing has been on the rise in recent months, but has yet to make up all the ground lost earlier in the year. Increased demand for exports should help to pull manufacturing output in the province higher, although recent announcements regarding temporary shutdowns in the aerospace industry will contribute to volatility in the sector. The domestic economy appears to be holding up well, with home and auto sales recording decent growth of 8% and 4% through August, respectively. This is likely to continue, as the economy gains some momentum and the unemployment rate edges down below 7% – levels not seen since prior to the recession. Construction, while soft this year, should also be supportive of growth, as housing starts are expected to rise solidly. All told, growth is expected to rise above 1.5% in 2017 and 2018.

Slow but steady in the East

The Maritime Provinces have not experienced the cyclical swings that have been apparent in most other regions. Economic activity has picked up somewhat in 2015-16, but remains quite subdued, and further gains will be limited by the aging population. Still, each province has some sectors that will help to keep growth steady throughout the forecast horizon.

Nova Scotia's economy is forecast to accelerate this year, thanks in large part to a rise in shipbuilding activity, as this is the first full year of operation. Going forward, manufacturing is expected to remain healthy, which combined with an uptick in residential construction will be growth-positive. Consumer spending should also hold up, with the unemployment rate set to edge down over the course of 2017. Overall, we expect Nova Scotia's economic growth to remain steady throughout the forecast period at around 1.5%.

Economic activity in New Brunswick has been sluggish this year, due in part to slowing petroleum manufacturing, the closure of a potash mine and declines in both residential and non-residential construction. The bright spot is perhaps the consumer, with retail trade up by 7% during the first half of the year and home sales continuing to recover from the 7-year slump that began back in 2008. A sharp increase in new home starts next year should help to lift economic activity; however, growth is expected to remain quite soft at just under 1% in 2017 and 2018.

PEI has been working to boost tourism, and it seems to be paying off. The province is enjoying another great year, with overnight stays up 12% during the first seven months of the year, and all signs pointing to further strength in August. The low Canadian dollar has resulted in an increase in travelers from the U.S., as well as more visitors from within Canada. This has fed into stronger retail sales. With the Canadian dollar unlikely to gain much strength over the forecast horizon, these trends are likely to remain in place going forward, helping to keep economic growth relatively stable at around 1.5% through 2018.

Recovery lies ahead for oil-producing provinces

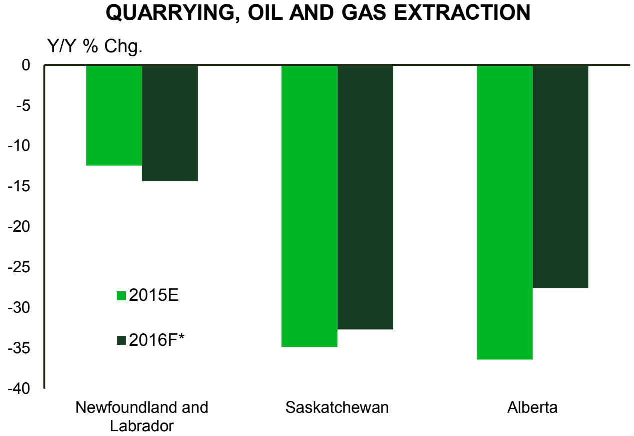
Energy producing provinces have continued to struggle this year, with another annual contraction expected for each. However, stabilizing oil prices should correspond to stabilizing oil-related investment – the Achilles heel for these provinces over the last two years. In fact, even holding capital spending flat would be supportive for growth based on the accounting of GDP. As such, the oil-driven economies are ripe for a modest recovery.

Alberta was hit hardest this year, with the wildfires taking a significant chunk out of economic output during the second quarter. This development, together with the ongoing reverberations on spending and investment from the low oil price environment, will likely leave the decline in economic activity for the year at just over 3%. The unemployment rate shot up to a 22-year high of 8.6% in July before edging back down. But, that jump was largely due to an increase in the labour force rather than a flood of job losses.

The good news for Alberta is that the worst is in the rear view mirror. With oil production having been restored by July, and reconstruction efforts having already begun, the second half of the year promises to be better. Reconstruction in Fort McMurray will continue into next year. This, in combination with rising oil production from new oil sands projects set to come online later this year and in 2017, will be key in bringing Alberta's economy out of recession. Indeed, economic growth is expected to rise above 2% in 2017 and 2018. While certainly an improvement, the pace of growth is only about half that recorded coming out of the previous recession and economic activity will still fall short of 2014 levels.

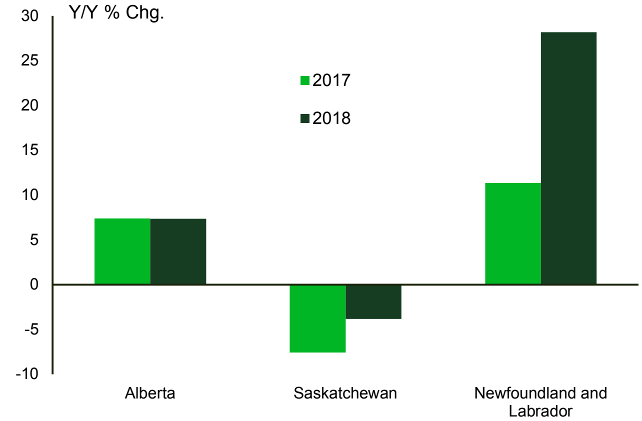
The recovery in Saskatchewan set to begin next year will be more subdued than that in Alberta given that its recession was not as deep and oil production in the province is expected to continue falling. However, potash production should edge up over the next two years to offset some of the output lost in New Brunswick and to meet increased demand spurred by the low prices. Moreover, despite lower prices, agriculture output is expected to remain healthy. Construction is likely to support growth over the forecast horizon as well, as it gets some lift from infrastructure and maintenance projects. In 2018, Saskatchewan's economy is set to gain further traction, in line with gradually recovering commodity prices and some improvement in the job market.

CHART 5: CAPITAL SPENDING ON MINING, QUARRYING, OIL AND GAS EXTRACTION



*Note: 2015 is preliminary and 2016 is spending intentions.
Source: Statistics Canada, TD Economics.

CHART 6: OIL PRODUCTION FORECAST



Source: CAPP, TD Economics.

Economic growth in the province is expected to reach 2% in 2018, ranked second in the country after Alberta.

This year's 0.6% contraction in Newfoundland and Labrador is expected to be a quarter of that recorded over the last two years. However, the province is faced with several headwinds that will lead to a larger contraction of 1.3% next year. Indeed, a number of capital projects have wound down, which will weigh on investment next year. Meanwhile, the fallout from the provincial government's austere budget – which included widespread tax increases – is set to hinder domestic demand and limit public spending.

That said, there is a light at the end of the tunnel, with an economic recovery expected to begin in 2018. The upturn will stem largely from increased oil production, as a new project is set to come online at the end of next year. This should help to bring economic activity back into the black, although growth in the province will remain among the weakest across the country.

Bottom Line

After widening in 2016, regional divergence in economic growth should begin to diminish next year. Most resource-based economies will begin to bounce back – albeit from very low levels – and a cooling in the housing market will take some steam out of B.C. and Ontario. A revival of the rotation in growth towards manufacturing and exports should provide some offset to the softness in residential investment; however, it won't be enough to prevent growth in these economies from slipping below 2% in 2018. This will allow Alberta and Saskatchewan to sit at the top of the leaderboard that year; however, the pace of growth in these economies will be muted – particularly when compared to that following the previous recession.

SUMMARY TABLES

REAL GROSS DOMESTIC PRODUCT (GDP) Annual average per cent change					
	2014	2015E	2016F	2017F	2018F
CANADA	2.5	1.1	1.1	1.8	1.7
N. & L.	-2.0	-2.1	-0.6	-1.3	1.1
P.E.I.	1.5	1.5	1.7	1.6	1.4
N.S.	0.6	1.1	1.5	1.6	1.5
N.B.	-0.3	1.9	0.5	0.8	0.9
Québec	1.5	1.1	1.3	1.6	1.7
Ontario	2.7	2.6	2.7	2.0	1.7
Manitoba	2.3	2.3	2.3	1.7	1.5
Sask.	1.9	-0.9	-0.4	1.5	2.0
Alberta	4.8	-3.5	-3.2	2.2	2.3
B.C.	3.2	3.3	3.1	2.0	1.8

E|F: Forecast by TD Economics as at September 2016.
Source: Statistics Canada / Haver Analytics

NOMINAL GROSS DOMESTIC PRODUCT (GDP) Annual average per cent change					
	2014	2015E	2016F	2017F	2018F
CANADA	4.3	0.5	1.4	3.3	3.6
N. & L.	-4.2	-6.0	-2.1	-0.3	3.3
P.E.I.	3.8	2.6	2.7	2.6	3.5
N.S.	1.3	2.8	2.3	2.8	3.2
N.B.	0.6	2.6	0.6	2.0	2.8
Québec	2.5	1.6	1.7	3.0	3.3
Ontario	4.1	3.6	3.6	3.5	3.6
Manitoba	3.5	3.5	3.0	2.7	3.6
Sask.	-0.9	-1.5	-0.3	3.4	4.0
Alberta	9.1	-9.4	-5.5	4.1	4.3
B.C.	4.7	4.9	4.6	3.2	3.0

E|F: Forecast by TD Economics as at September 2016.
Source: Statistics Canada / Haver Analytics

EMPLOYMENT Annual average per cent change					
	2014	2015	2016F	2017F	2018F
CANADA	0.6	0.9	0.6	0.5	0.5
N. & L.	-1.7	-1.0	-0.8	-0.7	0.0
P.E.I.	-0.1	-1.1	-2.3	0.2	0.2
N.S.	-1.1	0.1	-0.5	0.1	0.2
N.B.	-0.2	-0.4	-0.4	-0.2	0.3
Québec	0.0	1.0	0.5	0.7	0.4
Ontario	0.8	0.7	1.0	0.8	0.7
Manitoba	0.1	1.5	-0.4	0.6	0.5
Sask.	1.0	0.6	-0.8	0.7	0.6
Alberta	2.2	1.2	-1.7	-0.2	0.7
B.C.	0.6	1.3	2.8	0.5	0.3

E|F: Forecast by TD Economics as at September 2016.
Source: Statistics Canada / Haver Analytics

UNEMPLOYMENT RATE Annual, per cent					
	2014	2015	2016F	2017F	2018F
CANADA	6.9	6.9	7.0	6.9	6.8
N. & L.	11.9	12.8	12.8	12.9	13.1
P.E.I.	10.6	10.4	10.8	10.7	10.6
N.S.	9.0	8.6	8.5	8.3	8.1
N.B.	9.9	9.8	9.8	10.2	10.0
Québec	7.7	7.6	7.2	6.8	6.7
Ontario	7.3	6.8	6.7	6.6	6.6
Manitoba	5.4	5.6	6.1	6.0	5.8
Sask.	3.8	5.0	6.2	6.1	5.9
Alberta	4.7	6.0	8.0	8.0	7.7
B.C.	6.1	6.1	6.0	6.0	6.2

E|F: Forecast by TD Economics as at September 2016.
Source: Statistics Canada / Haver Analytics

CONSUMER PRICE INDEX (CPI) Annual average per cent change					
	2014	2015	2016F	2017F	2018F
CANADA	1.9	1.1	1.7	2.2	2.0
N. & L.	1.9	0.4	2.2	2.6	2.2
P.E.I.	1.6	-0.6	1.7	2.4	2.1
N.S.	1.7	0.4	1.6	2.3	2.1
N.B.	1.5	0.5	2.1	2.2	1.9
Québec	1.4	1.1	1.0	1.8	2.0
Ontario	2.3	1.2	1.9	2.1	2.0
Manitoba	1.8	1.2	1.8	2.2	2.1
Sask.	2.4	1.6	1.6	2.6	2.2
Alberta	2.6	1.2	1.5	2.6	2.3
B.C.	1.0	1.1	1.9	2.1	1.9

E|F: Forecast by TD Economics as at September 2016.
Source: Statistics Canada / Haver Analytics

RETAIL TRADE Annual average per cent change					
	2014	2015	2016F	2017F	2018F
CANADA	4.6	1.3	3.7	3.6	3.6
N. & L.	3.4	0.2	2.8	3.1	3.2
P.E.I.	3.3	2.3	6.2	3.5	3.8
N.S.	2.3	-0.6	3.6	3.4	3.4
N.B.	3.8	2.4	3.7	3.1	3.3
Québec	1.7	0.5	3.7	3.6	3.5
Ontario	5.0	4.2	4.8	3.8	3.3
Manitoba	4.3	1.5	5.2	3.6	4.2
Sask.	4.6	-3.5	2.1	2.0	3.8
Alberta	7.5	-4.6	-0.9	4.2	4.0
B.C.	5.6	6.0	6.2	4.1	3.8

E|F: Forecast by TD Economics as at September 2016.
Source: Statistics Canada / Haver Analytics

HOUSING STARTS Thousands of units					
	2014	2015	2016F	2017F	2018F
CANADA	189.2	193.6	193.7	179.9	175.0
N. & L.	2.2	1.8	1.5	1.4	1.5
P.E.I.	0.5	0.5	0.6	0.6	0.6
N.S.	3.0	3.9	3.4	3.7	3.9
N.B.	2.3	1.9	1.7	1.8	2.3
Québec	39.3	36.8	36.5	38.6	41.8
Ontario	58.6	68.8	75.3	68.6	63.2
Manitoba	6.2	5.6	5.4	5.8	6.1
Sask.	8.3	5.2	4.7	4.6	4.6
Alberta	40.5	37.5	24.1	23.3	23.0
B.C.	28.3	31.5	40.5	31.5	28.1

F: Forecast by TD Economics as at September 2016.
Source: CMHC / Haver Analytics

HOUSING STARTS Per cent change					
	2014	2015	2016F	2017F	2018F
CANADA	0.7	2.3	0.0	-7.1	-2.7
N. & L.	-23.6	-19.0	-12.7	-9.5	9.6
P.E.I.	-19.3	5.0	3.5	6.9	-2.1
N.S.	-21.9	27.2	-12.7	8.9	5.9
N.B.	-18.9	-15.2	-12.7	6.2	26.7
Québec	4.5	-6.3	-1.0	5.7	8.2
Ontario	-3.8	17.5	9.4	-8.9	-7.9
Manitoba	-17.6	-9.3	-3.1	6.3	4.8
Sask.	0.2	-37.2	-9.9	-1.5	-0.2
Alberta	12.4	-7.4	-35.7	-3.5	-1.3
B.C.	4.5	11.4	28.4	-22.1	-10.9

F: Forecast by TD Economics as at September 2016.
Source: CMHC / Haver Analytics

EXISTING HOME SALES Thousands of units					
	2014	2015	2016F	2017F	2018F
CANADA	480.3	506.4	537.1	505.1	483.4
N. & L.	4.1	4.3	4.3	3.8	3.7
P.E.I.	1.4	1.7	2.1	2.1	1.8
N.S.	8.9	9.2	9.6	10.2	10.5
N.B.	6.3	6.7	7.1	7.0	6.9
Québec	70.6	74.2	77.9	81.7	85.4
Ontario	205.0	224.6	242.6	228.9	200.8
Manitoba	13.8	14.0	15.1	14.9	15.0
Sask.	13.9	12.4	11.5	11.6	11.9
Alberta	71.8	56.5	51.1	49.3	50.0
B.C.	84.0	102.5	115.7	95.7	97.3

F: Forecast by TD Economics as at September 2016.
Source: Canadian Real Estate Association

EXISTING HOME SALES Per cent change					
	2014	2015	2016F	2017F	2018F
CANADA	5.2	5.4	6.1	-5.9	-4.3
N. & L.	-4.7	3.7	0.4	-11.7	-0.6
P.E.I.	-3.2	20.8	24.0	-0.3	-13.3
N.S.	-2.3	2.8	4.4	6.3	2.4
N.B.	-0.1	6.5	6.1	-1.0	-1.3
Québec	-0.8	5.0	5.0	4.9	4.5
Ontario	3.9	9.5	8.0	-5.7	-12.2
Manitoba	0.3	1.7	7.5	-1.1	0.8
Sask.	2.4	-10.8	-7.3	0.8	3.1
Alberta	8.6	-21.3	-9.6	-3.4	1.4
B.C.	15.2	22.0	12.8	-17.2	1.7

F: Forecast by TD Economics as at September 2016.
Source: Canadian Real Estate Association

AVERAGE EXISTING HOME PRICE Thousands of C$					
	2014	2015	2016F	2017F	2018F
CANADA	407.3	441.2	484.6	475.7	475.2
N. & L.	284.4	276.2	259.9	250.5	243.0
P.E.I.	165.4	164.1	181.8	178.4	173.1
N.S.	213.3	217.8	215.2	217.5	217.6
N.B.	161.0	159.2	163.2	163.3	162.2
Québec	271.4	275.4	283.5	299.3	312.9
Ontario	429.5	461.6	524.1	551.1	552.3
Manitoba	264.7	268.2	275.4	281.1	285.2
Sask.	297.9	296.1	298.0	297.4	300.7
Alberta	399.9	391.5	393.0	391.0	391.3
B.C.	570.4	637.2	673.5	604.1	613.7

F: Forecast by TD Economics as at September 2016.
Source: Canadian Real Estate Association

AVERAGE EXISTING HOME PRICE Per cent change					
	2014	2015	2016F	2017F	2018F
CANADA	6.7	8.3	9.8	-1.8	-0.1
N. & L.	0.2	-2.9	-5.9	-3.6	-3.0
P.E.I.	6.6	-0.8	10.8	-1.9	-3.0
N.S.	-0.7	2.1	-1.2	1.0	0.1
N.B.	-0.2	-1.1	2.5	0.1	-0.7
Québec	1.4	1.5	2.9	5.6	4.5
Ontario	7.0	7.5	13.5	5.2	0.2
Manitoba	1.5	1.3	2.7	2.1	1.5
Sask.	3.6	-0.6	0.6	-0.2	1.1
Alberta	5.2	-2.1	0.4	-0.5	0.1
B.C.	6.1	11.7	5.7	-10.3	1.6

F: Forecast by TD Economics as at September 2016.
Source: Canadian Real Estate Association