

# ECONOMIC & FINANCIAL OUTLOOK

## 2023 Started Off Relatively Strong, but Rate Hikes Will Start to Bite in the Second Half of the Year

### HIGHLIGHTS

- ▶ By the looks of most economic indicators, the global economy is holding up pretty well. Trade growth remained slow early this year, but China’s reopening seems to be paying off now. China’s real GDP growth came in at an annualized 9.1% in the first quarter after the government scrapped most lockdown measures. Meanwhile European PMIs are trending upward, especially on the services side, suggesting the economy continued to grow in the first quarter of 2023. But interest rate hikes are expected to bite later this year. While headline inflation is easing just about everywhere, core inflation—which strips out food and energy—remains sticky.
- ▶ In the US, consumer spending slowed in February and March, but January’s strong gain should mean a solid quarterly print that contributes positively to first quarter real GDP. The economy is also being supported by the labour market, with employers adding just over a million jobs in the first three months of the year. The banking sector issues that emerged in March could hobble the economy. Consumer credit is holding up for now, but business credit appears to be slowing.
- ▶ The Canadian economy continues to demonstrate unexpected resiliency despite high borrowing costs, still-elevated inflation and financial market volatility. Consumer spending had a strong start to 2023 in the face of economic headwinds, supported by a tight labour market, solid wage gains and surging population growth. These factors have also acted to support a tentative stabilization in the Canadian housing market. However, we remain of the view that interest rates will persist in weighing on economic activity in Canada. And when combined with a sluggish economy south of the border, growth is likely to slow considerably though 2023, ultimately culminating in a recession in the second half of the year. The contraction in economic activity will put upward pressure on the unemployment rate into 2024, dampening wage growth in the process. Along with the rapidly slowing pace of inflation, this should prompt the Bank of Canada to cut its policy rate before the end of this year, ultimately bringing it down to roughly its long-run neutral rate by the end of 2024.
- ▶ Quebec’s economy has been up and down since mid-2022. Real GDP fell an annualized 1.3% in the third quarter, then rebounded 1.9% in Q4 as consumer spending picked up. The year ended on a high note, with households receiving a cheque from the Quebec government for between \$400 and \$600 in December and wages and jobs posting strong growth. It’ll be a different story in 2023. Consumers will really feel the pinch of high interest rates, especially as the government has announced significantly less financial support. Consumer spending will slow, the housing market will continue to correct and businesses will face global economic headwinds. We could see several quarters of real GDP contraction and a slight softening of the labour market this year before the economy starts to recover in 2024.

### CONTENTS

Highlights and Main Changes.....	1	Risks Inherent in Our Scenarios.....	2	Financial Forecasts.....	3
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## RISKS INHERENT IN OUR SCENARIOS

Inflation is showing signs of slowing, but it remains high around the world and could even rebound in some countries. This could prompt central banks to continue raising interest rates or keep them higher for longer. Significant further tightening remains the biggest risk to the global economy. The economic slowdown may therefore still turn out to be worse than expected, despite some more positive data recently. If things get more difficult for the global economy, Canada could see weaker exports and worsening terms of trade. Higher unemployment and interest rates could also mean a bigger housing market correction in Canada. So far, Europe's economy has avoided a deepening energy crisis, but it may continue to struggle to meet its energy needs and will remain vulnerable to price fluctuations due to the war in Ukraine. The war continues to inject uncertainty into our forecast, particularly for commodity prices. Diplomatic tensions between the US and China could lead to additional trade restrictions. The fallout from the turmoil in the US banking sector could take the form of even tighter credit conditions and more economic trouble. Some US financial institutions could see lower ratings and higher borrowing costs. A deeper economic slowdown could result in more bankruptcies and sharper price corrections in a number of asset classes. We'll also be keeping an eye on US debt ceiling talks, which promise to be fraught. They could also drive further volatility in bond yields and the US dollar as the default deadline approaches. But if the global economy deteriorates sharply, risks are tilted more to a rapid appreciation of the US dollar, especially against the currencies of countries considered more economically and financially fragile. This could increase some vulnerabilities and spark foreign debt crises.

**TABLE 1**  
**World GDP growth (adjusted for PPP) and inflation rate**

%	WEIGHT*	REAL GDP GROWTH			INFLATION RATE		
		2022	2023f	2024f	2022	2023f	2024f
<b>Advanced economies</b>	<b>38.7</b>	<b>2.7</b>	<b>0.7</b>	<b>1.1</b>	<b>7.1</b>	<b>4.4</b>	<b>2.4</b>
United States	15.7	2.1	1.1	1.4	8.0	3.8	2.4
Canada	1.4	3.4	1.1	0.7	6.8	3.1	2.0
<i>Quebec</i>	0.3	2.8	0.3	0.7	6.7	3.4	1.9
Japan	3.7	1.0	0.4	0.8	2.5	2.1	1.2
United Kingdom	2.3	4.1	-0.2	0.4	9.1	6.7	2.9
Eurozone	11.9	3.5	0.5	0.6	8.4	5.5	2.5
<i>Germany</i>	3.3	1.9	-0.1	0.5	6.9	6.2	2.8
<i>France</i>	2.3	2.6	0.4	0.5	5.2	4.8	2.4
<i>Italy</i>	1.8	3.8	0.3	0.7	8.2	6.4	2.3
Other countries	4.2	2.9	0.9	1.4	5.8	4.2	2.3
<i>Australia</i>	1.0	3.7	1.6	1.4	6.6	5.3	3.0
<b>Emerging and developing economies</b>	<b>61.3</b>	<b>3.6</b>	<b>3.5</b>	<b>4.0</b>	<b>8.4</b>	<b>6.9</b>	<b>4.6</b>
North Asia	26.8	4.0	5.6	5.1	4.1	3.8	3.3
<i>China</i>	18.6	3.0	5.7	4.9	2.0	2.5	2.4
<i>India</i>	7.0	7.0	5.6	6.0	6.7	5.0	4.9
South Asia	5.1	5.4	4.0	4.4	4.8	3.8	2.8
Latin America	5.8	3.4	1.0	1.9	9.1	5.4	4.0
<i>Mexico</i>	1.8	3.1	1.1	1.7	7.9	5.1	4.0
<i>Brazil</i>	2.3	3.0	1.0	1.6	9.5	5.5	4.3
Eastern Europe	8.1	0.4	0.2	2.4	27.0	16.7	10.4
<i>Russia</i>	3.3	-2.1	-2.0	1.1	13.8	6.1	4.9
Other countries	15.5	3.6	2.2	3.3	10.4	11.7	7.5
<i>South Africa</i>	0.6	2.1	0.7	1.8	7.0	5.7	4.8
<b>World</b>	<b>100.0</b>	<b>3.3</b>	<b>2.4</b>	<b>2.9</b>	<b>7.9</b>	<b>5.9</b>	<b>3.8</b>

f: forecasts; PPP: Purchasing Power Parities, exchange rate that equates the costs of a broad basket of goods and services across countries; \* 2021.  
 Sources: World Bank, Consensus Forecasts and Desjardins Economic Studies

## FINANCIAL FORECASTS

Stress on the financial system has eased since the last update as policy makers shored up confidence by introducing several liquidity facilities. Economic data on the margin has continued to show some signs that monetary policy is beginning to have its intended effect on demand. Although inflation has moved lower, it remains well above central bank target ranges, and this is keeping the threat of further rate increases alive. As a result, yields have moved higher by 15–30bps in North America. Priced-in terminal rates remain below where they were before the banking crisis, reflecting concerns that further tightening of lending standards will come later this year, essentially reducing the need for higher policy rates. We continue to expect the Bank of Canada to remain on the sidelines, while the Fed is likely to raise rates one last time before pausing. The rebound in risk sentiment has lifted risk assets and the Canadian dollar, although there remain plenty of headwinds going forward. Quantitative tightening continues to drain liquidity from the system and is expected to have a more pronounced effect going forward as the ownership of sovereign securities shifts from central banks to private hands at a faster pace.

**TABLE 2**  
**Summary of financial forecasts**

END OF PERIOD IN % (UNLESS OTHERWISE INDICATED)	2022		2023				2024			
	Q3	Q4	Q1	Q2f	Q3	Q4f	Q1f	Q2f	Q3f	Q4f
<b>Key interest rate</b>										
United States	3.25	4.50	5.00	5.25	5.25	5.25	4.50	3.50	2.75	2.75
Canada	3.25	4.25	4.50	4.50	4.50	4.25	3.50	3.00	2.50	2.50
Eurozone	1.25	2.50	3.50	4.25	4.25	4.25	4.00	3.50	3.00	2.50
United Kingdom	2.25	3.50	4.25	4.75	4.75	4.75	4.50	4.00	3.50	3.00
<b>Federal bonds</b>										
<u>United States</u>										
2-year	4.26	4.54	4.15	4.10	3.85	3.70	3.40	3.20	2.80	2.70
5-year	4.08	3.97	3.62	3.60	3.50	3.40	3.20	2.95	2.80	2.70
10-year	3.80	3.83	3.48	3.50	3.45	3.35	3.05	2.95	2.90	2.80
30-year	3.76	3.94	3.66	3.65	3.55	3.40	3.05	2.95	2.90	2.85
<u>Canada</u>										
2-year	3.79	4.06	3.74	3.80	3.45	3.15	2.90	2.85	2.55	2.40
5-year	3.32	3.41	3.02	3.10	2.95	2.80	2.75	2.60	2.50	2.35
10-year	3.16	3.30	2.90	2.95	2.85	2.75	2.70	2.65	2.60	2.50
30-year	3.09	3.28	3.02	3.05	2.90	2.80	2.75	2.65	2.50	2.40
<b>Currency market</b>										
Canadian dollar (USD/CAD)	1.38	1.36	1.35	1.37	1.39	1.37	1.33	1.28	1.25	1.27
Canadian dollar (CAD/USD)	0.72	0.74	0.74	0.73	0.72	0.73	0.75	0.78	0.80	0.79
Euro (EUR/USD)	0.98	1.07	1.09	1.08	1.06	1.08	1.10	1.13	1.15	1.16
British pound (GBP/USD)	1.12	1.20	1.24	1.22	1.19	1.21	1.24	1.28	1.31	1.33
Yen (USD/JPY)	145	131	133	128	124	120	115	113	111	110
<b>Stock markets (level and growth)*</b>										
United States – S&P 500	3,840		Target: 3,650 (-4.9%)				Target: 3,900 (+6.8%)			
Canada – S&P/TSX	19,385		Target: 19,000 (-2.0%)				Target: 20,350 (+7.1%)			
<b>Commodities (annual average)</b>										
WTI oil (US\$/barrel)	95 (80*)		76 (74*)				82 (83*)			
Gold (US\$/ounce)	1,800 (1,815*)		1,860 (1,870*)				1,740 (1,670*)			

f: forecasts; WTI: West Texas Intermediate; \* End of year.  
 Sources: Datastream and Desjardins Economic Studies

**TABLE 3**  
**United States: Major economic indicators**

QUARTERLY ANNUALIZED % CHANGE (UNLESS OTHERWISE INDICATED)	2022		2023				ANNUAL AVERAGE			
	Q3	Q4	Q1f	Q2f	Q3f	Q4f	2021	2022	2023f	2024f
Real GDP (2012 US\$)	3.2	2.6	2.0	-0.3	-1.3	-0.3	5.9	2.1	1.1	1.4
Personal consumption expenditures	2.3	1.0	4.5	0.0	-0.8	0.0	8.3	2.7	1.6	1.3
Residential construction	-27.1	-25.1	-7.0	-4.2	-7.8	-5.9	10.7	-10.6	-13.8	0.2
Business fixed investment	6.2	4.0	1.5	0.6	-3.3	-2.2	6.4	3.9	1.4	1.9
Inventory change (US\$B)	38.7	136.5	65.0	10.0	-40.0	-65.0	-19.4	125.0	-7.5	-8.7
Public expenditures	3.7	3.8	1.9	1.5	1.5	1.5	0.6	-0.6	2.1	1.2
Exports	14.6	-3.7	4.4	-1.0	-1.5	-0.5	6.1	7.1	2.5	1.1
Imports	-7.3	-5.5	4.8	-3.0	-4.5	-3.0	14.1	8.1	-2.0	0.4
Final domestic demand	1.5	0.7	3.1	0.1	-1.1	-0.3	6.7	1.7	1.0	1.3
<b>Other indicators</b>										
Nominal GDP	7.7	6.6	6.0	1.8	1.5	1.8	10.7	9.2	4.8	3.7
Employment <sup>1</sup>	3.4	2.5	2.7	1.4	-0.1	-1.3	2.9	4.3	1.9	0.0
Unemployment rate (%)	3.6	3.6	3.5	3.6	3.9	4.4	5.4	3.7	3.9	5.1
Housing starts <sup>2</sup> (thousands of units)	1,450	1,398	1,395	1,328	1,250	1,237	1,605	1,554	1,303	1,327
Total inflation rate*	8.3	7.1	5.8	4.0	3.1	2.6	4.7	8.0	3.8	2.4
Core inflation rate* <sup>3</sup>	6.3	6.0	5.6	5.0	4.1	3.3	3.6	6.1	4.5	2.5

f: forecasts; \* Annual change; <sup>1</sup> According to the establishment survey; <sup>2</sup> Annualized basis; <sup>3</sup> Excluding food and energy.  
Sources: Datastream and Desjardins Economic Studies

**TABLE 4**  
**Canada: Major economic indicators**

QUARTERLY ANNUALIZED % CHANGE (UNLESS OTHERWISE INDICATED)	2022		2023				ANNUAL AVERAGE			
	Q3	Q4	Q1	Q2f	Q3f	Q4f	2021	2022	2023f	2024f
<b>Real GDP</b> (2012 \$)	<b>2.3</b>	<b>0.0</b>	<b>2.7</b>	<b>0.5</b>	<b>-1.1</b>	<b>-0.7</b>	<b>5.0</b>	<b>3.4</b>	<b>1.1</b>	<b>0.7</b>
Final consumption expenditure [of which:]	1.1	2.1	4.9	2.4	1.3	1.2	5.4	4.0	2.8	1.5
Household consumption expenditure	-0.4	2.0	5.6	2.5	1.0	1.1	5.1	4.8	3.0	1.6
Government consumption expenditure	4.8	2.4	3.4	1.9	1.8	1.4	6.4	2.0	2.4	1.4
Gross fixed capital formation [of which:]	-6.5	-2.5	1.6	-1.5	-2.5	-1.7	7.4	-1.5	-2.3	0.8
Residential structures	-18.9	-8.8	-6.1	-7.5	-5.3	-2.3	14.9	-11.1	-10.1	1.0
Non-residential structures	9.4	10.2	5.9	3.3	-1.7	-5.2	0.8	8.0	4.9	-0.4
Machinery and equipment	-4.7	-27.6	5.6	2.0	-4.0	-1.3	9.9	7.6	-4.1	0.4
Intellectual property products	5.1	11.6	6.3	2.0	2.0	2.0	4.0	0.6	5.7	2.1
Government gross fixed capital formation	-6.2	11.9	9.1	2.1	1.8	1.9	0.9	2.1	4.1	1.8
Investment in inventories (2012 \$B)	52.1	22.3	7.1	1.3	-2.2	-4.2	-4.1	37.8	0.5	-4.9
Exports	10.6	0.8	10.7	2.3	-2.4	-3.2	1.4	2.6	4.4	0.4
Imports	-2.0	-14.6	7.2	1.8	0.1	-0.2	7.8	7.2	0.9	1.9
Final domestic demand	-0.8	1.0	4.1	1.4	0.4	0.5	5.8	2.7	1.6	1.4
<b>Other indicators</b>										
Nominal GDP	-2.5	-2.7	-0.1	0.5	-0.2	0.1	13.6	11.0	0.2	2.2
Employment	-1.3	2.2	4.7	0.0	-1.7	-0.7	5.0	4.0	1.6	0.8
Unemployment rate (%)	5.1	5.1	5.0	5.5	6.3	6.9	7.5	5.3	5.9	6.7
Housing starts <sup>1</sup> (thousands of units)	281	259	225	195	188	185	271	262	198	187
Total inflation rate*	7.2	6.7	5.2	3.0	2.5	1.9	3.4	6.8	3.1	2.0
Core inflation rate* <sup>2</sup>	5.4	5.3	4.8	3.7	3.1	2.7	2.3	5.0	3.5	2.3

f: forecasts; \* Annual change; <sup>1</sup> Annualized basis; <sup>2</sup> Excluding food and energy.  
Sources: Datastream and Desjardins Economic Studies

**TABLE 5**  
**Quebec: Major economic indicators**

ANNUAL AVERAGE % CHANGE (UNLESS OTHERWISE INDICATED)	2020	2021	2022	2023f	2024f
<b>Real GDP (2012 \$)</b>	<b>-5.0</b>	<b>6.0</b>	<b>2.8</b>	<b>0.3</b>	<b>0.7</b>
Final consumption expenditure [of which:]	-3.3	5.9	3.6	2.8	1.5
<i>Household consumption expenditure</i>	-5.7	5.4	4.7	3.2	1.5
<i>Government consumption expenditure</i>	2.0	7.3	1.4	2.0	1.7
Gross fixed capital formation [of which:]	-1.0	7.2	-4.0	-6.4	-1.1
<i>Residential structures</i>	2.8	12.9	-11.4	-13.6	-0.1
<i>Non-residential structures</i>	0.6	-1.5	0.9	-5.8	-2.3
<i>Machinery and equipment</i>	-15.1	20.3	1.3	-8.9	-0.1
<i>Intellectual property products</i>	0.1	7.1	-1.3	0.0	1.9
<i>Government gross fixed capital formation</i>	0.5	-3.5	1.6	5.6	4.6
Investment in inventories (2012 \$M)	-6,550	-431	6,783	-2,000	500
Exports	-7.8	2.9	4.2	0.1	1.3
Imports	-7.9	6.8	6.2	1.1	2.1
Final domestic demand	-2.9	6.2	1.9	0.8	1.0
<b>Other indicators</b>					
Nominal GDP	-1.9	11.8	10.0	2.1	2.1
Real disposable personal income	7.2	1.9	1.9	0.7	1.0
Weekly earnings	7.9	2.9	4.1	3.9	3.1
Employment	-5.4	4.3	3.0	1.8	-0.6
Unemployment rate (%)	8.9	6.1	4.3	4.5	6.0
Personal savings rate (%)	17.4	14.6	11.9	7.8	6.9
Retail sales	0.7	14.4	8.5	3.6	3.5
Housing starts <sup>1</sup> (thousands of units)	54.1	67.8	57.1	44.0	49.0
Total inflation rate	0.8	3.8	6.7	3.4	1.9

f: forecasts; <sup>1</sup> Annualized basis.

Sources: Statistics Canada, Institut de la statistique du Québec, Canada Mortgage and Housing Corporation and Desjardins Economic Studies

**TABLE 6**  
**Major medium-term economic and financial indicators**

% (UNLESS OTHERWISE INDICATED)	ANNUAL AVERAGE							AVERAGES	
	2021	2022	2023f	2024f	2025f	2026f	2027f	2018–2022	2023–2027f
<b>United States</b>									
Real GDP (% change)	5.9	2.1	1.1	1.4	3.0	2.4	2.1	2.1	2.0
Total inflation rate (% change)	4.7	8.0	3.8	2.4	2.3	2.2	2.1	3.6	2.6
Unemployment rate	5.4	3.7	3.9	5.1	5.0	4.8	4.5	4.9	4.6
S&P 500 index (% change) <sup>1</sup>	26.9	-19.4	-4.9	6.8	7.5	4.0	4.0	9.3	3.5
Federal funds rate	0.25	1.86	5.05	3.75	2.75	2.75	2.75	1.37	3.41
Prime rate	3.25	4.86	8.05	6.75	5.75	5.75	5.75	4.37	6.41
Treasury bills – 3-month	0.05	2.09	4.90	3.40	2.60	2.60	2.60	1.32	3.22
Federal bonds – 10-year	1.43	2.96	3.50	3.00	2.70	2.70	2.70	2.07	2.92
– 30-year	2.05	3.12	3.65	3.00	2.85	2.85	2.85	2.48	3.04
WTI oil (US\$/barrel)	68	95	76	82	82	80	78	65	80
Gold (US\$/ounce)	1,800	1,803	1,805	1,740	1,565	1,600	1,600	1,607	1,662
<b>Canada</b>									
Real GDP (% change)	5.0	3.4	1.1	0.7	2.3	2.1	1.8	1.6	1.6
Total inflation rate (% change)	3.4	6.8	3.1	2.0	2.0	2.0	2.0	3.0	2.2
Employment (% change)	5.0	4.0	1.6	0.8	2.2	1.7	1.4	1.4	1.5
Employment (thousands)	903	750	307	157	451	341	302	260	311
Unemployment rate	7.5	5.3	5.9	6.7	5.8	5.6	5.5	6.8	5.9
Housing starts (thousands of units)	217	271	198	187	228	241	235	234	218
S&P/TSX index (% change) <sup>1</sup>	21.7	-8.7	-2.0	7.1	7.0	5.0	5.0	4.5	4.4
Exchange rate (USD/CAD)	0.80	0.77	0.73	0.78	0.78	0.77	0.78	0.77	0.77
Overnight funds	0.25	1.95	4.50	3.05	2.25	2.25	2.50	1.18	2.91
Prime rate	2.45	4.14	6.70	5.25	4.45	4.45	4.70	3.38	5.11
Mortgage rate – 1-year	2.80	4.43	6.20	5.20	4.55	4.45	4.60	3.52	5.00
– 5-year	4.79	5.64	6.50	6.45	6.05	5.90	5.95	5.18	6.17
Treasury bills – 3-month	0.11	2.18	4.30	2.80	2.25	2.20	2.50	1.15	2.81
Federal bonds – 2-year	0.48	2.90	3.65	2.75	2.30	2.30	2.45	1.49	2.69
– 5-year	0.95	2.78	3.05	2.60	2.30	2.30	2.50	1.60	2.55
– 10-year	1.36	2.77	2.95	2.65	2.40	2.40	2.55	1.75	2.59
– 30-year	1.85	2.81	3.00	2.65	2.40	2.40	2.55	2.01	2.60
<b>Yield spreads (Canada – United States)</b>									
Treasury bills – 3-month	0.06	0.09	-0.60	-0.60	-0.35	-0.40	-0.10	-0.17	-0.41
Federal bonds – 10-year	-0.07	-0.19	-0.55	-0.35	-0.30	-0.30	-0.15	-0.32	-0.33
– 30-year	-0.20	-0.31	-0.65	-0.35	-0.45	-0.45	-0.30	-0.48	-0.44
<b>Quebec</b>									
Real GDP (% change)	6.0	2.8	0.3	0.7	2.0	1.7	1.5	1.9	1.2
Total inflation rate (% change)	3.8	6.7	3.4	1.9	2.0	2.0	2.0	3.0	2.2
Employment (% change)	4.3	3.0	1.8	-0.6	2.0	1.6	1.1	1.1	1.2
Employment (thousands)	177	130	80	-25	90	75	50	49	54
Unemployment rate	6.1	4.3	4.5	6.0	5.1	4.4	3.8	6.0	4.8
Retail sales (% change)	14.4	8.5	3.6	3.5	5.5	5.2	5.0	5.7	4.6
Housing starts (thousands of units)	68	57	44	49	51	52	53	55	50

f: forecasts; WTI: West Texas Intermediate; <sup>1</sup> Changes are based on end-of-period data.

Sources: Datastream, Statistics Canada, Institut de la statistique du Québec, Ontario Ministry of Finance, Canada Mortgage and Housing Corporation and Desjardins Economic Studies