

Economic and Financial Outlook

A Recession is Likely as Trade War Impacts Loom

March 20, 2025

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Highlights

- The full and final scope of the Trump administration's trade policies has yet to be determined. The economic and financial outlook presented here is based on the first policy elements that have been implemented, namely higher tariffs on imports from China, an additional 25% tariff on steel and aluminum and new tariffs on Mexico (25%) and Canada (25% on all goods except 10% on energy). But it's clear that President Trump is just getting started. Despite temporary exemptions on CUSMA-compliant goods, we can expect more protectionist measures to come. Consequently, our forecast predicts the United States will end CUSMA exemptions in April while simultaneously imposing reciprocal tariffs of 25% on imports from other countries. We expect some relief in early 2026, with tariffs being reduced from 25% to 10% (0% for energy). That said, we'll update our economic and financial scenarios as the burgeoning trade war evolves.
- US trade policy is disrupting both the American and global economies. These changes, even the ones that haven't yet been implemented, are already triggering a reaction. Financial markets, businesses and households are showing heightened anxiety. Estimated US real GDP growth was revised lower for the first quarter, but it's also been downgraded for future quarters, with the possibility of a recession now looming. Meanwhile, US trade policy is expected to drive up inflation. For the most part, global economic forecasts have also been revised downward. But Chinese authorities seem fairly optimistic, and China's real GDP growth may prove relatively resilient despite the increase in US tariffs on Chinese goods.
- With US tariffs ratcheting up, we are of the view that Canada's economy is likely to experience a recession starting as early as the second quarter of 2025. US economic policy is expected to hold back trade, investment, job creation, consumption and growth here in Canada. That will be exacerbated by the pre-existing headwinds of rapidly slowing population growth and an impending spike in mortgage renewals at higher interest rates. Retaliatory tariffs will further deepen the economic drag while forcing inflation higher. However, with pain being felt south of the border as well, we anticipate the US administration will ease up on tariffs on imports from Canada starting in early 2026, allowing the Canadian economy to rebound somewhat. That said, the level of economic activity is unlikely to recover fully from the tariff shock as uncertainty and some customs

duties remain in place. And while there have been some early signs of progress on reducing structural barriers to economic growth, such as internal trade barriers, we'll remain skeptical until we see substantive change.

- Since tariffs on Canadian goods vary depending on the type of product, their impact on Quebec's economy in 2025 will be harsher than the national average. We expect real GDP to contract for three quarters, with growth returning in early 2026 once some trade barriers have been lowered. But uncertainty will curb investment in export-oriented manufacturing sectors, which will make for a fragile recovery. Slower population growth will also sap economic momentum, serving as a cap on the unemployment rate, which should reach 7% by early next year. Next week's 2025–2026 budget will provide further details on how the government will support sectors affected by the reduction in trade, as well as its willingness to address weakness in the export sector by accelerating some planned investments.

Risks Inherent in Our Scenarios

The first few months of Donald Trump's second term have triggered a massive spike in uncertainty all over the world. Although the president has already put forward a number of protectionist measures, that uncertainty has been amplified by his postponement of some tariffs and additional threats, as well as questions over how far other nations will go to retaliate. Furthermore, the other policies implemented by the new Trump administration, especially regarding immigration and the federal government apparatus, could send the economy into a tailspin. Even though we've already revised our forecasts, further adjustments will be needed as we get more clarity. Notably, President Trump has threatened to use economic measures to coerce Canada into seeking statehood. The nature of these potential measures is still in question. As for inflation, although it's currently close to target in many countries, an escalating trade war could catapult it higher. Unemployment could also spike in many nations, depending on the scope of the trade war. There's also a lot of uncertainty over how much room central banks have to cut interest rates if their economies are hit by stagflation. The weakening of US regulatory authorities could lead to financial excesses and ultimately imbalances, to say nothing of the potential environmental and even public health issues that could result. We also need to keep an eye on whether the Federal Reserve manages to maintain its independence over the long term. Governments around the world have been hit by political crises, which could further undermine their ability to respond to economic downturns while keeping public finances on solid footing. Bond markets may react by sending yields soaring. Trends in the global economy, financial markets and commodity prices could become increasingly unstable if the geopolitical backdrop and economic environment deteriorate further.

Table 1**Global GDP Growth (Adjusted for PPP) and Inflation Rates**

%	Weight*	Real GDP growth			Inflation rate		
		2024	2025f	2026f	2024	2025f	2026f
Advanced economies	37.7	1.6	0.9	0.9	2.6	2.7	2.4
United States	14.8	2.8	1.0	1.1	3.0	3.2	2.9
Canada	1.3	1.5	1.1	1.0	2.4	2.3	2.5
<i>Quebec</i>	0.3	1.5	0.9	0.7	2.3	2.6	2.3
Japan	3.4	0.1	1.1	0.4	2.7	2.6	1.8
United Kingdom	2.2	0.9	0.4	0.6	2.5	3.1	2.6
Eurozone	11.9	0.8	0.6	0.6	2.4	2.4	2.1
<i>Germany</i>	3.2	-0.2	-0.3	0.2	2.3	2.5	2.1
<i>France</i>	2.3	1.1	0.4	0.4	2.0	1.7	1.9
<i>Italy</i>	1.9	0.5	0.4	0.5	1.0	2.1	1.9
Other countries	4.1	1.5	1.3	1.6	2.5	2.1	2.2
<i>Australia</i>	1.0	1.0	1.4	1.9	3.2	2.8	2.9
Emerging and developing economies	62.3	3.9	3.5	3.6	7.3	5.1	4.0
Emerging Asia	32.8	5.2	4.8	4.5	2.0	1.9	2.3
<i>China</i>	18.8	5.0	4.6	4.0	0.2	0.6	1.1
<i>India</i>	7.9	6.4	6.0	6.0	5.0	4.5	4.7
Latin America	5.8	2.3	1.2	1.5	4.2	4.5	3.9
<i>Mexico</i>	1.8	1.5	0.0	1.2	4.7	4.0	3.8
<i>Brazil</i>	2.4	2.9	1.5	1.3	4.0	5.3	4.3
Eastern Europe	8.5	3.4	2.0	2.4	19.3	12.6	8.4
<i>Russia</i>	3.5	4.1	1.2	1.3	8.4	6.5	4.7
Other countries	15.2	2.1	2.4	2.9	16.4	10.8	7.9
<i>South Africa</i>	0.5	0.6	1.1	1.6	4.4	4.1	4.5
World	100.0	3.0	2.5	2.6	5.5	4.2	3.4

f: forecast; PPP: Purchasing Power Parities, exchange rates that equate the cost of a broad basket of goods and services across countries; * 2023.
World Bank, Consensus Forecasts and Desjardins Economic Studies

Financial Forecast

Given the heightened likelihood of prolonged trade war with the United States, the Bank of Canada will likely need to ease policy rates more than initially forecast. The revised outlook sees the central bank cutting rates to 1.75% this cycle. During a typical recession central bankers would have eased policy further, but rising inflation expectations will keep central bankers wary of delivering too much stimulus. Yields have fallen across the curve, reflecting the elevated downside risks to the Canadian economy.

Proposed trade and immigration policies are also increasing downside risks stateside. But, since inflation still hasn't normalized and inflation expectations are rising sharply, the FOMC will ease policy at a much slower pace than the Bank of Canada. Our outlook now sees the FOMC cutting its policy rate by 75 basis points this year.

The Canadian dollar has depreciated due to tariff and recession fears. However, the increasing likelihood of a US recession has also undermined the US dollar, keeping USDCAD in a broad trading range. Looking ahead, we see a balanced risk outlook for USDCAD, with the worst likely over for the loonie. As we now anticipate the US economy

to enter a recession, the Federal Reserve may need to cut rates more than the market currently expects, leading the US dollar to depreciate against a wider range of currencies, including the loonie. We are also monitoring the reciprocal tariff announcements on April 2, as a significant tariff hike on Canada could cause currency volatility.

With downside risks to the US economy rising, the outlook for US equities is much weaker and should see global equities continue to outperform as result.

Table 2
Summary of Financial Forecasts

End of period in % (unless otherwise indicated)	2024		2025				2026			
	Q3	Q4	Q1f	Q2f	Q3f	Q4f	Q1f	Q2f	Q3f	Q4f
Key interest rate										
United States	5.00	4.50	4.50	4.25	4.00	3.75	3.75	3.75	3.50	3.50
Canada	4.25	3.25	2.75	2.50	2.00	1.75	1.75	1.75	1.75	1.75
Eurozone	3.50	3.00	2.75	2.50	2.00	2.25	2.25	2.25	2.25	2.00
United Kingdom	5.00	4.75	4.50	4.25	4.00	4.00	4.00	3.50	3.75	4.00
Federal bonds										
<u>United States</u>										
2-year	3.68	4.24	3.95	3.85	3.70	3.50	3.45	3.40	3.40	3.35
5-year	3.56	4.38	4.00	3.90	3.85	3.80	3.65	3.60	3.55	3.55
10-year	3.78	4.57	4.20	4.05	4.00	3.95	3.80	3.75	3.70	3.70
30-year	4.13	4.79	4.45	4.30	4.25	4.20	4.05	4.00	3.95	3.90
<u>Canada</u>										
2-year	2.91	2.93	2.45	2.25	2.00	1.85	1.95	2.15	2.25	2.35
5-year	2.73	2.96	2.55	2.35	2.25	2.25	2.35	2.40	2.45	2.50
10-year	2.95	3.23	2.85	2.60	2.55	2.65	2.65	2.65	2.70	2.70
30-year	3.13	3.33	3.10	2.85	2.80	2.80	2.80	2.80	2.85	2.85
Currency market										
Canadian dollar (USD/CAD)	1.35	1.44	1.43	1.42	1.43	1.42	1.40	1.40	1.39	1.38
Canadian dollar (CAD/USD)	0.74	0.70	0.70	0.70	0.70	0.70	0.71	0.71	0.72	0.72
Euro (EUR/USD)	1.12	1.04	1.09	1.10	1.08	1.08	1.08	1.08	1.07	1.06
British pound (GBP/USD)	1.34	1.25	1.30	1.30	1.28	1.25	1.25	1.25	1.25	1.25
Yen (USD/JPY)	143	157	148	145	145	140	140	135	135	130
Stock markets (level and growth)*										
United States – S&P 500	5,882 (23.3%)		Target: 5,800 (-1.4%)				Target: 6,600 (+13.8%)			
Canada – S&P/TSX	24,728 (18.0%)		Target: 25,000 (+1.1%)				Target: 27,500 (+10.0%)			
Commodities (annual average)										
WTI oil (US\$/barrel)	77 (70*)		68 (68*)				68 (68*)			
Gold (US\$/ounce)	2,390 (2,625*)		2,975 (3,050*)				2,955 (2,885*)			

f: forecast; WTI: West Texas Intermediate; * End of year.

Datastream and Desjardins Economic Studies

Forecast Tables

Table 3

United States: Major Economic Indicators

Quarterly annualized % change (unless otherwise indicated)	2024		2025				Annual average			
	Q3	Q4	Q1f	Q2f	Q3f	Q4f	2023	2024	2025f	2026f
Real GDP (2017 US\$)	3.1	2.3	0.1	-0.5	-0.4	1.5	2.9	2.8	1.0	1.1
Personal consumption expenditures	3.7	4.2	1.2	-1.2	-0.8	1.8	2.5	2.8	1.5	1.2
Residential construction	-4.3	5.4	6.5	-0.1	-4.1	-2.9	-8.3	4.2	1.1	-1.8
Business fixed investment	4.0	-3.2	5.6	-4.1	-3.8	0.1	6.0	3.6	0.2	-0.2
Inventory change (2017 US\$B)	57.9	10.2	75.0	-75.0	-50.0	-50.0	33.1	39.4	-25.0	10.0
Public expenditures	5.1	2.9	1.6	1.5	1.6	1.1	3.9	3.4	2.3	1.4
Exports	9.6	-0.5	1.8	-5.1	-6.0	-2.8	2.8	3.2	-0.4	0.5
Imports	10.7	-1.2	24.8	-27.8	-5.4	-4.0	-1.2	5.4	0.1	-0.4
Final domestic demand	3.7	3.0	2.1	-1.1	-1.0	1.3	2.7	3.0	1.4	0.9
Other indicators										
Nominal GDP	5.0	4.8	2.9	2.4	2.7	5.5	6.6	5.3	3.7	3.9
Employment ¹	0.9	1.3	1.4	0.3	-0.4	-0.7	2.2	1.3	0.7	-0.1
Unemployment rate (%)	4.2	4.1	4.1	4.2	4.4	4.7	3.6	4.0	4.3	4.9
Housing starts ² (thousands of units)	1,332	1,388	1,417	1,345	1,320	1,305	1,421	1,367	1,347	1,279
Total inflation rate*	2.7	2.7	2.8	2.7	3.5	3.9	4.1	3.0	3.2	2.9
Core inflation rate ³	3.3	3.3	3.2	3.2	4.0	4.4	4.8	3.4	3.7	3.4

f: forecast; * Annual change; ¹ According to the establishment survey; ² Annualized basis; ³ Excluding food and energy.
Datastream and Desjardins Economic Studies

Table 4

Canada: Major Economic Indicators

Quarterly annualized % change (unless otherwise indicated)	2024		2025				Annual average			
	Q3	Q4	Q1f	Q2f	Q3f	Q4f	2023	2024	2025f	2026f
Real GDP (2017 \$)	2.2	2.6	1.8	-1.3	-0.4	-0.3	1.5	1.5	1.1	1.0
Final consumption expenditure [of which:]	4.5	4.4	2.1	0.5	0.6	0.7	2.0	2.6	2.2	1.1
<i>Household consumption expenditure</i>	4.2	5.6	1.9	-0.3	-0.1	0.2	1.8	2.4	2.0	0.9
<i>Government consumption expenditure</i>	5.4	1.4	2.8	2.5	2.4	2.1	2.2	3.2	2.8	1.9
Gross fixed capital formation [of which:]	-0.8	9.9	-0.8	-3.2	-0.8	0.1	-1.6	0.1	0.9	1.1
<i>Residential structures</i>	6.4	16.7	-3.8	-5.9	1.4	2.6	-8.5	-1.1	1.4	2.6
<i>Non-residential structures</i>	1.3	2.7	-1.0	-3.2	-2.6	-1.2	3.2	-1.8	-0.2	-0.2
<i>Machinery and equipment</i>	-27.4	17.9	-0.8	-9.4	-9.9	-9.2	-2.7	-2.1	-3.5	-3.7
<i>Intellectual property products</i>	6.5	2.3	1.9	1.5	1.1	0.9	4.0	-0.1	2.3	1.1
<i>Government gross fixed capital formation</i>	4.3	6.7	3.2	3.3	3.7	4.3	4.8	7.2	4.3	4.6
Investment in inventories (2017 \$B)	18.1	-1.5	-11.5	-2.0	0.2	-0.5	25.5	14.4	-3.5	-10.7
Exports	-0.8	7.4	12.7	-17.7	-8.8	-4.8	5.0	0.6	-1.3	1.5
Imports	-1.2	5.4	5.6	-9.2	-5.6	-2.7	0.3	0.6	-0.7	1.2
Final domestic demand	3.3	5.6	1.4	-0.4	0.3	0.5	1.1	2.0	1.9	1.1
Other indicators										
Nominal GDP	4.3	6.4	4.1	0.5	1.5	1.4	2.9	4.6	3.5	2.6
Employment	0.8	1.9	2.4	-2.8	-1.6	-0.7	3.0	1.9	0.4	0.2
Unemployment rate (%)	6.5	6.7	6.7	7.4	7.7	8.0	5.4	6.4	7.5	7.4
Housing starts ¹ (thousands of units)	238	248	239	237	234	231	242	245	235	217
Total inflation rate*	2.0	1.9	2.4	2.1	2.4	2.5	3.9	2.4	2.3	2.5
Core inflation rate ²	2.5	2.1	2.6	2.8	2.9	3.0	3.9	2.6	2.8	2.6

f: forecast; * Annual change; ¹ Annualized basis; ² Excluding food and energy.
Datastream and Desjardins Economic Studies

Table 5**Quebec: Major Economic Indicators**

Annual average % change (unless otherwise indicated)	2022	2023	2024f	2025f	2026f
Real GDP (2017 \$)	3.4	0.6	1.5	0.9	0.7
Final consumption expenditure [of which:]	4.6	0.7	2.3	1.9	0.8
<i>Household consumption expenditure</i>	5.5	1.8	2.4	1.7	0.3
<i>Government consumption expenditure</i>	2.4	-1.7	2.3	2.4	1.9
Gross fixed capital formation [of which:]	-2.3	-3.7	-0.1	1.2	1.5
<i>Residential structures</i>	-11.1	-15.1	1.2	4.4	3.1
<i>Non-residential structures</i>	3.7	5.9	0.7	-2.0	0.0
<i>Machinery and equipment</i>	11.6	-6.3	-3.4	-1.8	-1.0
<i>Intellectual property products</i>	6.3	4.2	1.8	1.7	0.9
<i>Government gross fixed capital formation</i>	-2.4	7.2	0.0	0.8	1.9
Investment in inventories (2017 \$B)	11	6	3	0	0
Exports	2.0	4.0	2.0	0.2	-2.9
Imports	6.9	-0.8	1.6	0.5	-1.3
Final domestic demand	3.0	-0.2	1.8	1.8	0.9
Other indicators					
Nominal GDP	8.7	5.0	5.4	3.7	2.6
Real disposable personal income	1.1	0.1	4.1	-0.3	0.5
Weekly earnings	4.1	3.6	4.4	4.2	1.3
Employment	3.1	2.9	0.9	0.8	-0.3
Unemployment rate (%)	4.3	4.4	5.3	6.0	6.6
Personal savings rate (%)	9.3	7.8	9.7	8.0	8.4
Retail sales	8.5	3.7	1.8	3.2	4.3
Housing starts ¹ (thousands of units)	57.1	38.9	48.7	53.0	54.0
Total inflation rate	6.7	4.5	2.3	2.6	2.3

f: forecast; ¹ Annualized basis.

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	
	2023	2024	2025f	2026f	2027f	2028f	2029f	2020–2024	2025–2029f
United States									
Real GDP (% change)	2.9	2.8	1.0	1.1	1.7	1.8	1.9	2.4	1.5
Total inflation rate (% change)	4.1	3.0	3.2	2.9	2.1	2.2	2.0	4.2	2.5
Unemployment rate	3.6	4.0	4.3	4.9	4.8	4.5	4.0	4.9	4.5
S&P 500 index (% change) ¹	24.2	23.3	-1.4	13.8	4.5	4.8	6.1	6.1	5.6
Federal funds rate	5.20	5.31	4.13	3.63	3.25	3.25	3.25	3.25	3.50
Prime rate	8.20	8.31	7.13	6.63	6.25	6.25	6.25	6.25	6.50
Treasury bills – 3-month	5.28	5.18	3.94	3.43	3.14	3.10	3.20	3.20	3.36
Federal bonds – 10-year	3.96	4.21	4.05	3.74	3.65	3.65	3.65	3.65	3.75
– 30-year	4.09	4.41	4.30	3.98	3.80	3.75	3.75	3.75	3.92
WTI oil (US\$/barrel)	78	77	68	68	68	68	68	68	68
Gold (US\$/ounce)	1,943	2,385	2,975	2,955	2,915	2,880	2,778	2,665	2,901
Canada									
Real GDP (% change)	1.5	1.5	1.1	1.0	2.0	1.8	1.7	2.6	1.5
Total inflation rate (% change)	3.9	2.4	2.3	2.5	2.3	2.2	2.0	3.4	2.3
Employment (% change)	3.0	1.9	0.4	0.2	1.2	1.1	0.9	1.7	0.7
Employment (thousands)	593	382	78	34	250	231	195	332	157
Unemployment rate	5.4	6.4	7.5	7.4	6.8	6.4	6.4	6.8	6.9
Housing starts (thousands of units)	242	245	235	217	226	243	263	248	237
S&P/TSX index (% change) ¹	8.1	18.0	1.1	10.0	5.5	5.6	5.8	5.8	5.6
Exchange rate (US\$/C\$)	0.75	0.70	0.70	0.72	0.74	0.77	0.77	0.80	0.74
Overnight rate	4.74	4.59	2.25	1.75	2.13	2.63	2.75	2.75	2.30
Prime rate	6.94	6.75	4.45	3.95	4.33	4.83	4.95	4.95	4.50
Mortgage rate – 1-year	7.14	7.63	5.00	4.60	4.70	4.80	4.85	4.85	4.79
– 5-year	6.68	6.72	6.00	5.80	5.80	5.85	5.95	5.95	5.88
Treasury bills – 3-month	4.74	4.37	2.09	1.79	2.15	2.61	2.70	2.70	2.27
Federal bonds – 2-year	4.27	3.67	2.14	2.18	2.48	2.68	2.80	2.80	2.45
– 5-year	3.57	3.30	2.35	2.43	2.61	2.76	2.80	2.80	2.59
– 10-year	3.36	3.34	2.66	2.68	2.81	2.85	2.85	2.85	2.77
– 30-year	3.28	3.33	2.89	2.83	2.88	2.90	2.90	2.90	2.88
Yield spreads (Canada–United States)									
Treasury bills – 3-month	-0.54	-0.81	-1.85	-1.64	-0.99	-0.49	-0.50	-0.50	-1.09
Federal bonds – 10-year	-0.60	-0.87	-1.39	-1.06	-0.84	-0.80	-0.80	-0.80	-0.98
– 30-year	-0.81	-1.08	-1.41	-1.15	-0.92	-0.85	-0.85	-0.85	-1.04
Quebec									
Real GDP (% change)	0.6	1.5	0.9	0.7	1.9	1.6	1.5	1.6	1.3
Total inflation rate (% change)	4.5	2.3	2.6	2.3	2.0	1.9	1.7	3.6	2.1
Employment (% change)	2.9	0.9	0.8	-0.3	1.1	0.9	0.8	1.3	0.7
Employment (thousands)	128	39	38	-15	51	44	40	53	31
Unemployment rate	4.4	5.3	6.0	6.6	5.9	5.5	5.1	5.8	5.7
Retail sales (% change)	3.7	1.8	3.2	4.3	4.7	4.0	3.1	6.0	3.9
Housing starts (thousands of units)	39	49	53	54	55	55	55	53	54

f: forecast; WTI: West Texas Intermediate; ¹ Changes are based on end-of-period data.

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