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Economic Outlook 2024

Outlook 2024

The year 2023 will likely be remembered for the global easing of inflation from levels not seen in decades and central banks pushing their policy rates to new heights not seen since the global financial crisis. While interest rates remain low by historical standards, there are concerns regarding their impact on the economy.

Nevertheless, economic activity in 2023 in many countries has been more resilient than expected at this time last year, with many of the main economies avoiding a recession and the associated deterioration in the labour market.

As we look at 2024, many of the concerns and themes regarding the economic outlook for 2023 will remain the same. Specifically we wonder:

- Will we have a recession?
- Will inflation be vanquished?
- Will central banks cut interest rates?
- Will we see a sharp correction in the housing market?
- How will households fare in a higher interest rate environment?
- Will Alberta continue to outperform the rest of the country?

In general, we expect a mild recession in Canada in 2024 and for Alberta to outperform the rest of the country in most scenarios. However, the outlook remains uncertain, with many risks on the horizon. Hence, while hoping for the best, we need to be aware of and prepared for the worst.

At a glance

Inflation globally is easing, driven by a normalized supply chain and lower energy prices. Central banks are expected to ease monetary policy in 2024 as growth and inflation moderate. While headline inflation is projected to reach 2%, core inflation may take longer to meet the Bank of Canada's target.

Inflation & Interest Rates

Inflation is easing globally due to normalization in the global supply chain, lower energy prices, and the impact of tighter monetary policy on growth.

With growth and inflation moderating rapidly in many countries, the main central banks are expected to be able to ease monetary policy in 2024.

Inflation is expected to moderate further in 2024, with headline inflation expected to reach 2% around mid-year. However, measures of core inflation are expected to take longer to return to the Bank of Canada's (BoC) target.

The combined effects of reduced inflationary pressures, slower growth, a rise in the unemployment rate and slack within the economy should provide the desired conditions for the BoC to cut interest rates in the second quarter of 2024. Further cuts are expected in the year's second half, ending 2024 at 4.0%.

Growth & Hard or Soft Landing

Growth in the US is expected to continue to outperform its Canadian counterpart. In Canada, growth is expected to be 0.3% in 2024 and a recession is very likely given the sluggish growth expected in the coming quarters. Moreover, as the population continues to grow rapidly, GDP per capita will likely continue to contract in the first half of the year.

Whether the economy goes through a soft or a hard landing depends on whether we only see a hiring freeze or broad-based layoffs in 2024.

Households

Households are expected to remain the main drag on growth in 2024, as they remain under financial pressures. Rising consumer insolvencies also remain a concern, and this dynamic could change rapidly if the labour market deteriorates and there are significant layoffs.

Households in Alberta are facing challenges due to higher interest rates and a more significant decline in purchasing power in recent years. Already, insolvencies in the province are at their highest level on record, meaning there could be further negative impacts in Alberta should the Canadian economy experience a hard landing.

In 2024 the housing market is also expected to weaken, especially in the first half of the year, as high interest rates exacerbate the impact of high prices. This situation will lead to some decline in house prices, especially in overvalued markets.

Alberta

In Alberta, continued strong population growth and tailwinds from robust energy prices mean that the province is expected to grow faster than its counterparts. Nevertheless, growth will slow in 2024, reaching 1.8%.

Investment in Alberta is expected to remain solid in 2024, with increases in the oil and gas sector and in residential investment in reaction to the high prices and low inventories. The housing market in Alberta, especially Calgary and Edmonton, is expected to outperform the rest of the country, supported by strong migration and better affordability.

Global trends

Inflation is expected to continue to moderate in 2024. Monetary tightening efforts will lead to slower growth and a gradual building up of excess supply in the economic system. Moreover, commodity prices are expected to be relatively stable.

In 2023, global inflation eased after the 2022 surge, but concerns linger over persistently high levels. Major central banks, like the Federal Reserve and the European Central Bank, engaged in significant tightening. The interplay between quantitative tightening, government debt issuance, and interest rates adds complexity to the global economic landscape. Varying growth prospects and geopolitical risks, including the situation in Gaza and the 2024 U.S. presidential elections, further contribute to uncertainty in global economic trends.

Inflation: easing, but concerns remain

The global rise in inflation in 2022, due to the combined impact of higher energy prices, supply chain disruptions and a strong recovery in demand, has led to one of the sharpest monetary tightening cycles in decades.

Inflation moderated significantly in most countries in 2023, as energy prices stabilized and subsequently declined compared to the year before. Oil prices have been volatile this year, trading between $65 and $95, but below the average of about $95 of 2022. Similarly, other commodity prices have been below last year's levels for months.

In addition, many of the supply constraints affecting the global economy in 2022 have eased in 2023. The global supply chain has normalized substantially, reducing the production delays and scarcity of many inputs. The global transportation and logistics system has also returned to a more regular situation and transportation costs, especially for container shipments, have returned to around their pre-pandemic levels. Similarly, labour shortages have eased and are no longer as acute as they were; however, they remain elevated by historical standards.

All these developments have eased inflationary pressures. Nevertheless, inflation remains too high for comfort in many countries. This is especially true for measures of core inflation. Elevated wage growth and higher inflation expectations in many countries suggest that inflationary pressures could be more persistent than anticipated and more challenging to bring down. As a result, central banks remain vigilant and unwilling to declare victory in their fight against inflation.

Inflation is expected to continue to moderate in 2024. Monetary tightening efforts will lead to slower growth and a gradual building up of excess supply in the economic system. Moreover, commodity prices are expected to be relatively stable, as weaker growth will reduce global demand and restrain prices.

In Canada, despite a sharp moderation from 5.9% to 3.1%, inflation remains elevated, and measures of core inflation are still above the Bank of Canada's (BoC) target. Inflationary pressures remain broad, with more than half of the Consumer Price Index (CPI) basket increasing at more than 3% and more than a third at more than 5%.

In addition, the momentum in price changes, as measured by the three-month annualized change in prices, remains consistent with inflation between 3.0% and 3.5%, depending on the measure of core inflation. Wage growth remains elevated, close to 5% year-over-year, which could lead to more persistent inflation than expected.

Inflation should gradually moderate in 2024, as weak growth and a rising unemployment rate create some slack in the economy. However, progress towards the BoC's 2% target could be slow.

Global monetary tightening is most likely over

Many central banks continued to tighten monetary policy in 2023, with the Federal Reserve, the European Central Bank (ECB), the Bank of England, the BoC, the Reserve Bank of Australia, and many others increasing their policy rates in 2023 to levels not seen in more than a decade, in many cases.

Since mid-2022, the ECB increased its policy rate from 0% in mid-2022 to 4.50%; this is the highest level for interest rates since 2001. Similarly, the Bank of England has increased its policy rate to 5.25%, a level not seen since the eve of the financial crisis. The Federal Reserve also hiked its policy rate to its highest since the early 2000s. In Canada, the BoC raised its policy by 50bp in 2023, pushing it from 4.50% to 5.00% in the first half of the year, the highest level for the policy rate since 2001. Similarly, real interest rates in most industrialized countries have continued to increase as inflation moderates.

In addition to the monetary tightening measures of central banks, global financial conditions also tightened as longer interest rates increased to levels not seen in more than a decade. This upward shift in the global yield curve translates into higher borrowing costs for businesses and consumers. For example, the 5-year rate in Canada increased about 140bp since the beginning of the year to 4.40% in October, a level not seen since 2007. As a result, the BoC estimates that the effective interest rate for consumers and businesses are close to 7%, its highest since 2001.

While interest rates remain low by historical standards, there are concerns regarding their impact on the economy. With inflation easing and expectations that it will ease further in the next few years, many central banks believe that further rate increases are becoming less needed and interest rates may have peaked.

There are also questions regarding the outlook for the yield curve going into 2024, after a significant increase in 2022 and 2023. Longer-term interest rates have eased somewhat in recent weeks as financial markets expect a slowdown of the economy and the end of central banks' tightening cycles.

We have likely seen the peak in long-term interest rates in this cycle. Weaker global growth next year and an increased likelihood of rate cuts by major central banks are likely to continue to weigh on the yield curve and longer-term rates. However, some factors could keep the yield curve higher or could push it higher.

1. **Many central banks continue to conduct "quantitative tightening,"**; this refers to reducing the size of their holding of government bonds accumulated during the pandemic to support growth. Central banks are not actively selling these bonds, but rather reinvesting the proceeds from maturing bonds, therefore the government will need to find buyers. For example, the Federal Reserve bond holding reduction over the past year is equivalent to a little over $900bn. In Canada, it is estimated that the BoC will reduce its holdings of government bonds by $56bn in 2024, representing about 30% of its holdings and about 11% of the planned gross issuance of Government of Canada Bonds next year. This reduction in central bank holdings could lead to lower demand for these bonds at a time when issuance is planned to increase, pushing the prices lower and the yields higher.

2. **There are concerns that issuance of government debt, especially in the US, will continue to increase.** The federal government debt in the US is expected to reach about 100% of GDP, and the deficit is expected to be almost 6% of GDP. There are concerns that investors will demand higher returns in exchange for holdings US Treasuriesor simply shy away from purchasing these bonds for other assets, thereby pushing longer-term interest rates and the yield curve higher.

Given the links between US and Canadian markets, higher bond yields in the US would most likely translate into higher interest rates in Canada, despite a better fiscal situation. Moreover, if concerns regarding the fiscal situation in the US lead to smaller foreign flows into US Treasuries, it could lead to a weaker US dollar, likely resulting in a stronger Canadian dollar.

While the focus has been mainly on the price of money, i.e., interest rates, there has also been a tightening in monetary policy via the quantity of money, i.e., much slower growth in money aggregates. While the link between money aggregates and economic activity is uncertain and volatile, broad money aggregates, like M2 and M3, are increasing at or close to their slowest past in decades. For example, M2 in the US is declining 3.6% y-o-y, the first decline since the early 1960s and the biggest since the Great Depression. In Canada, both

preferred measures from the BoC, namely M1+ and M2+, are growing at their weakest rates since the data was available in 1968. Based on monetary theory, such a low growth level is likely to suppress nominal growth.

There are many questions regarding the economic impact of sharp monetary tightening and higher interest rates after a decade of historically low interest rates. With inflation expected to moderate in 2024 and the impact of past monetary tightening slowing the economy, some rate cuts are expected next year. However, any reduction in the policy rate is likely to be modest, and interest rates are likely to be higher than in recent years for an extended period.

Global growth

Although economic activity slowed in many countries, it has been more resilient than expected over the past year. Nevertheless, business activity indicators like the Purchasing Manager Indexes (PMI) do show that many economies are slowing and economic activity is contracting in others, especially in Europe. Growth in 2024 is expected to be much lower than pre-pandemic average in most regions, especially in the developed countries. Despite slower growth, the labour markets of major economies have remained resilient and unemployment rates have barely increased; this may be due to the high level of vacancies and continued labour shortages.

In China, growth has slowed after an initial economic spurt at the beginning of the year as the country recovered from several pandemic-related restrictions on economic activity. Continued property sector issues are leading to increased uncertainty and a decline in sentiment. Moreover, the export sector faces headwinds from the reshoring and relocation of production by some manufacturers, as evidenced by the declining share of China in US imports.

Despite a further slowdown in 2024, growth in the US is expected to continue to outperform Canada. The main reason for the better growth prospects in the US is that American households are less sensitive to higher interest rates and other negative shocks than in Canada.

After avoiding a recession so far despite a substantial energy shock in 2022, growth across Europe is slowing rapidly, and the economy may have contracted in the second half of 2023. This is the result of a fast tightening in financial conditions in the region. A further slowdown of the economy is expected in 2024 and the risk of a recession in the area is elevated.

The US economy has been robust in 2023, with growth averaging about 3% so far this year. Strong consumer spending, supported by robust employment growth and the savings accumulated during the pandemic, has been an important source of strength. Growth is expected to decelerate in 2024 as past monetary tightening impacts consumers and businesses. A big question for the US economy remains whether it will be a soft or a hard landing; this will be dependent on the health of the labour market and consumers.

Despite a further slowdown in 2024, growth in the US is expected to continue to outperform Canada. The main reason for the better growth prospects in the US is that American households are less sensitive to higher interest rates and other negative shocks than in Canada. US households are much less indebted than Canadian ones; debt to disposable income in the US is about 95% v.s. 180% in Canada. As a result, the debt-service ratio, the share of disposable income used to repay debt (obligated principal repayment and interests), is much higher in Canada at about 15% compared to the US at 10%. Moreover, as most mortgage debt in the US is fixed for 30 years, many households in the country will not have to renew their borrowing at higher rates. This is a sharp contrast to the situation in Canada, where approximately 25% of mortgages will need to be refinanced at higher interest rates, according to our calculations. This situation likely explains why consumer confidence in Canada remains well below its equivalent in the US.

Geopolitical risks in 2024 include ongoing conflicts in Ukraine and Gaza, plus the upcoming US elections. Escalation in Gaza may impact global economy and oil prices. Polls favoring Trump raise concerns for international policies and Canada's economy, based on past experiences.

Geopolitical risks

Geopolitical risks were already high in 2023 with the continued war in Ukraine. However, the situation in Gaza over the past few months and the upcoming US presidential elections in 2024 are increasing these risks.

The conflict in Gaza could quickly spread to neighbouring countries or lead to more active involvement of other parties. As such, there is a risk that countries that form the Organization of the Petroleum Exporting Countries (OPEC) may be willing to use oil to pressure Western countries into action to help Palestinians. This would be similar to the actions of oil-producing countries in the early 1970s during the Yom Kippur war which led to the first oil shock in 1973. A surge in oil prices would have a detrimental impact on the global economy, leading to a jump in inflation at a time when households have already seen a big decline in their purchasing power.

The upcoming US presidential election also increases the level of political uncertainty. While the official candidates won't be determined until the end of the primaries mid-year, recent polls suggest that former President Trump is the preferred Republican candidate and would likely win against President Biden. While much can change between now and Election Day in November 2024, the prospect of another term for Trump raises concerns regarding the potential impact on international policies, from trade to diplomacy and domestic economic policy. For Canada, the experience from his first presidency should serve as a warning of the potential negative impact of election outcomes south of the border.

Outlook for Canada

Despite inflation moderation in 2023, the Bank of Canada remains cautious, with persistent wage growth concerns. Slower growth, rising unemployment, and global factors are expected to ease inflationary pressures.

Economic activity has been weak since the second quarter of 2023, with GDP barely increasing over the period. Although this is due, in part, to reduced consumer spending, business investment and export weakness, higher interest rates are the leading cause of this underperformance.

As shown previously (see *What happened to the recession? The role of the policy stance and demographic*), history suggests that a downturn usually occurs five to seven quarters on average after monetary policy enters restrictive territory. With the policy rate having been pushed above neutral in late 2022, it suggests a high probability of a recession in the first half of 2024.

Similarly, real interest rates have continued to increase as inflation continues to moderate, even as the policy rate remains unchanged. Moreover, historically weak money supply growth reinforced the restrictive nature of monetary policy. This has led to a sharp deceleration in credit towards the private sector, both for households and corporations.

In addition, the strong increase in population also hides the extent of the underlying weakness in the economy. As such, GDP per capita declined in four of the past five quarters and is currently about 1.7% lower than pre-pandemic, meaning that the average Canadian is somewhat poorer now. The same trend can also be seen in consumer spending, where individual spending is much weaker than aggregated spending.

This situation points to sluggish economic activity and a likely further slowdown in growth, especially in the first half of 2024. Moreover, it indicates that a recession, as defined by two consecutive quarters of GDP contraction, is also very likely in the coming quarters. With this in mind, we expected the economy for growth a modest 0.3% in 2024.

Inflation to continue to moderate

Inflation moderated throughout 2023, starting at 5.9% and reaching 3.1% in October. Similarly, the average of the BoC's core measures also eased from 5.2% to 3.6%. While the BoC welcomes slower inflation, the central bank is not yet ready to declare victory in its fight against inflation, as price momentum remains high and inflationary pressures remain broad.

Wage growth is also too high for the BoC's comfort, at around 5% y-o-y. The central bank worries that, in an environment where businesses are making more frequent and bigger price adjustments, higher wages will likely be passed on to consumers more rapidly, eroding their purchasing power and prompting workers to ask for wage increases; it's this inflationary cycle that the BoC is concerned about. While it may not necessarily lead to higher inflation, it could make inflation stickier and more difficult to return to target.

Slowing growth and a rise in the unemployment rate will lead to some slack in the economy. This will ease the wage and inflationary pressures. In addition, global factors such as the continued reduction in supply chain disruptions and lower global food and energy prices will continue to hold back inflation. However, shelter costs are likely to remain elevated and continue to be the main

contributor to inflation, as housing shortages continue to support robust rent increases and higher interest rates continue to filter into higher mortgage interest payments.

We estimate that headline inflation will stabilize around 3% until the Spring of 2024 before gradually declining to reach around 2% around the summer and staying close to this level for the rest of the year. Core inflation is expected to be slower to return to the 2% target. We estimate it will stay above 2.5% until the Summer of 2024 and end the year slightly above the BoC's target at 2.4%.

The evolution of energy prices and the Canadian dollar will affect how quickly inflation decelerates in 2024 or how sticky it could become. As mentioned earlier, there is a risk that oil prices could once again surge due to geopolitical events. As we have shown (see *The current energy shock is more inflationary and stickier than the 1970s oil shocks*), the sharp increase in energy prices in 2022 was much more inflationary than in previous periods and has been an important source of persistence in inflation through higher transportation costs. The Canadian dollar has been relatively weak in 2023, mainly due to a strong USD. With CAD expected to appreciate in 2024, mainly due to a depreciation in the USD, the stronger currency will likely dampen import prices and accelerate the moderation in inflation.

Some monetary easing is expected around mid-year

While the BoC continued to warn that further rate hikes could be necessary at their latest monetary policy decision, Governor Macklem has recently stated that monetary policy is likely sufficiently restrictive to return inflation to its target, suggesting that the central bank base case is that interest rates will remain unchanged for some time. This is in line with our view, and the attention now turns to when the first-rate cut will occur to bring monetary policy to a more neutral territory. However, the BoC will likely be patient and need a strong confirmation that inflation will be sustainably close to its 2% target before reducing its policy rate.

The combined effects of reduced inflationary pressures, slower growth, a rise in the unemployment rate and slack within the economy create the desired conditions for the BoC to cut interest rates in the second quarter of 2024. In our view, the central bank is aiming for inflation, both headline and core, to be below 3% and the momentum in core measures, defined as the three-month annualized price change, to reach under 2.5%.

Once the BoC begins to lower its policy rate, the next question will be the pace of cuts and the anticipated terminal rate. The pace of the rate cuts is likely to be moderate, with about 100bp of cuts before the end of 2024 to a level of 4%, unless the country enters a hard-landing scenario.

Looking further ahead, as we have shown (see *What happened to the recession? The role of the policy stance and demographic*), we believe that the neutral rate in Canada, the level of interest rates that is neither restrictive nor accommodative, is likely around 3.5%. This is above the current BoC estimate of 2-3%, but Governor Macklem has recently conceded that the neutral rate is likely higher than their estimate. With this in mind, we expect some modest cuts in early 2025 to bring interest rates to 3.5%.

We also expect the BoC to continue reducing the size of its holdings of Government of Canada bonds by not reinvesting the proceeds from maturing bonds, removing about $56bn of liquidity in 2024 and $44bn in 2025. By the end of 2025, the BoC balance sheet would still be about twice as large as its pre-pandemic size.

The risks to monetary policy are twofold: more persistent inflation would delay the timing of the first rate cut, while a hard landing would likely accelerate rate cuts and could necessitate interest rates to fall below the neutral rate, depending on the severity of the downturn.

Households remain under financial strains

Consumers will continue to be under financial pressure in 2024. While wage growth has moved above inflation in recent months, contributing to the improvement in purchasing power, many will see the impact of rate hikes in the form of both higher borrowing costs and debt-service ratio. We estimate that about a quarter of outstanding fixed-rate mortgages will be renewed this year at rates well above their previous rates (see *Will it be a hard landing or a soft landing? The labour market will decide*).

As a result of the impact of a higher proportion of income going towards debt repayment and continued underperformance in purchasing power, consumers will need to reduce their discretionary spending. In addition, slower growth will lead to weaker hiring and a gradual rise in the unemployment rate. This will lead to a further decline in consumer spending, especially as consumer confidence remains weak and reduces households' desire to spend.

The sharp increase in interest rates and debt payments will cause many households to struggle with their finances. Already, insolvencies in Canada are increasing rapidly and are above their pre-pandemic levels in many provinces.

The sharp increase in interest rates and debt payments will cause many households to struggle with their finances. Already, insolvencies in Canada are increasing rapidly and are above their pre-pandemic levels in many provinces. So far, most of the increase is from proposals - this refers to a renegotiation of terms, meaning that borrowers and lenders modify the parameters of loans to ensure the borrower can make their payments. To date, bankruptcies remain historically low because households' income remains high, allowing lenders and borrowers some flexibility to address tensions.

Housing to weaken further

The housing market peaked in early 2022 as interest rates started to increase. After a temporary pickup in early 2023, activity and prices are once again declining and are expected to continue to weaken in 2024. Affordability is at or close to its lowest in decades in many markets, with higher interest rates exacerbating the effect of high prices.

As we have shown in the past (see *House prices will have to decline further to restore affordability, except in the Prairies*), record low interest rates were maintaining affordability in many markets. While the decline in demand for housing is pushing prices lower, a widespread lack of supply, both in terms of new builds and listings, has so far prevented a sharp correction in prices.

Hard of soft-landing?

With this in mind, we believe a soft or hard landing in Canada will depend on how the labour market reacts to slower economic activity. Weaker activity, leading to hiring underperformance and a gradual increase in the unemployment rate, would mean a soft landing. However, if a receding economy leads to layoffs and a jump in the unemployment rate, the result may be a hard landing (see *Will it be a hard landing or a soft landing? The labour market will decide*).

A loss of employment may lead to a hard landing because households are particularly vulnerable to shocks given their high levels of indebtedness and rising insolvencies, the latter of which suggests that households are already struggling. While higher interest rates will continue to have a significant impact on household finances in the near future, we argue that an income shock due to job losses would have a much more significant negative impact on the economic outlook, as borrowers will no longer be able to restructure their borrowing; this would force borrowers to sell assets or default on their obligations. Such a scenario could have important negative spillovers to the rest of the economy as house prices drop and lenders reduce credit availability to protect their balance sheets from further losses and defaults.

While the labour market appears resilient for now, it tends to be a lagging indicator of the economic cycle and is usually at its best on the eve of a downturn. Similarly, although the intense labour shortages over the past two years may delay layoffs, it may not prevent them entirely. Nevertheless, our base case remains that the Canadian economy will experience a soft landing in 2024, but we remain vigilant for any indications that the situation may deteriorate.

Outlook for Alberta

The completion of the TransMountain and Coastal GasLink pipelines is anticipated to narrow price spreads and boost volumes, contributing positively to growth in 2024.

Throughout 2023, economic activity in Alberta was relatively strong compared to its counterparts, growing by 5.0%; this was only second to Saskatchewan, which grew by 6.0%. We expect Alberta's outperformance relative to other provinces to continue in 2024, regardless of whether it experiences a hard or soft landing. In the case of a hard landing, while growth is expected to be better, it is not clear whether Alberta would be able to escape a recession.

Business investment and the oil and gas sector remain a bright spot

Although the positive terms of trade from the oil and gas sector has been smaller in recent years despite record high revenues (*Where's the boom? How the impact of oil on Alberta may have permanently weakened*), the energy sector remained a solid tailwind for the economy in 2023. Investment in the industry remains an important support to growth. Moreover, high revenues contribute to elevated royalties on non-renewable resources and a robust fiscal situation in the province.

The expected completion and activation of the TransMountain oil pipeline and the Coastal GasLink pipeline will allow more products to reach markets. This will lead to a narrowing in price spreads between local and international prices and higher sales volumes, leading to higher revenues. The increase in volume and prices will be a positive for growth in 2024.

A continued rise in investment by the oil and gas sector will further support growth, with investment likely to increase by about 10% in 2024, but the level remains well-below the peak reached in 2014. Despite higher interest rates, we also expect to see solid business investment in other sectors of the economy, specifically manufacturing, petrochemicals, and technology.

Labour market to ease

Similar to the rest of the country, we expect Alberta's labour market to underperform in 2024, with the unemployment rate increasing to reach 7.0%. This is mainly due to hiring being too weak to absorb the influx of newcomers into the labour market. However, we cannot exclude the possibility of witnessing more layoffs, especially if the rest of the country were to experience a hard landing.

Strong demography key to Alberta's growth outperformance

Population growth of 4.5% in 2023 was a significant source of growth in the province and will likely continue in 2024. Alberta's population growth is expected to remain the fastest among its counterparts in 2024, with the province benefitting from an influx of international migrants and newcomers from other provinces in search of affordability. In addition, we estimate that about 80% of new migrants are establishing themselves in Calgary and Edmonton. This growth contributes to place strains on housing, especially in Calgary, and other public services such as health care, education, roads, and so forth.

Alberta's resilient consumer spending faces headwinds with wage challenges, rising interest rates, and record-high household insolvencies, while the housing market defies odds, fueled by population growth and affordability.

However, a strong demography hides underlying weaknesses within the economy. For example, while retail sales in the province are one of the fastest growing, once adjusted for population, the increase in consumer spending is much more subdued.

Consumers facing headwinds

As mentioned earlier, consumer spending in Alberta remained robust in 2023 and this trend is likely to continue in 2024, supported by solid population growth. However, spending per person is much weaker and remains almost 5% below its peak in 2014, adjusted for inflation.

Continued underperformance in wage growth in the province relative to the rest of the country (see The Alberta Advantage is melting away and Where's the boom? And the rise and fall of the Alberta Advantage), has meant that households in Alberta have seen a more significant loss in purchasing power than in other provinces, with wages in Alberta converging quickly to the national average. While structural factors explain this convergence, there are signs that wage underperformance could be coming to an end; in 2024, we believe wage and income per worker are likely to increase at the same pace in Alberta as in the rest of the country.

Households are also feeling the impact of higher interest rates. Albertans are the third most indebted in the country, with a debt-to-income of 180%, with Ontario and BC being the most indebted at 206% and 219%, respectively. However, with a slightly higher proportion of non-mortgage debt, likely at fixed rates, and smaller mortgages, Albertans are less sensitive to interest rates.

Interestingly, we note some compelling differences between the most indebted provinces. While Ontario and BC's purchasing power has outperformed Alberta's since 2019, retail sales volume per person in these two provinces significantly underperforms Alberta's. This suggests that the impact of interest rates on household finances and the angst it creates is a more significant deterrent to household spending than the change in purchasing power.

A major concern looking ahead is that household insolvencies have reached their highest level on record in recent months. While most of these are proposals (renegotiation of terms), similar to the national level, there are concerns that we could see a further rise in insolvencies in coming months, resulting in a surge in bankruptcies if the labour market deteriorates.

Housing market to remain robust

The continued increase in population and relatively more affordable in Alberta housing has meant that housing activity in the province remains higher than its pre-pandemic level despite the negative impact of higher interest rates. Inventories remain low, especially in Calgary, and are supporting prices. Similarly, rental prices have surged over the past year in many markets, with Calgary in the lead.

Housing investment has improved recently, with a sharp rise in housing starts, but remains low. Labour shortages, elevated construction costs, and higher interest rates have negatively impacted residential construction. However, recent data suggests that developers are responding to low inventories and rising prices in the housing sector and that residential investment will improve in 2024.

Risks to the outlook

In a complex economic landscape, Canada braces for potential scenarios – from global resilience boosting exports to recession risks, geopolitical shocks impacting commodity prices, and the delicate balance between household resilience and the threat of a housing market correction.

- The US and global economy could prove to be more resilient. This would support Canadian exports, leading to better growth. This could support inflation, especially if global commodity prices increase, potentially meaning that the BoC would need to keep rates unchanged for longer than predicted in our base case.
- The US economy could slow more than expected and enter a recession. This scenario would have a negative impact on Canadian growth. However, as US growth slows and the Federal Reserve cuts rates, we could expect some spillover to Canadian rates, with lower long-term interest rates and potentially some easing by the BoC.
- Oil and other commodity prices could increase sharply due to a geopolitical crisis. This would lead to higher inflation. As a result of the rise in inflationary pressures, the BoC may be unable to cut its policy rate to respond to the weaker economy and could even require rate hikes if the impact proves persistent.
- The slowdown in economic activity in Canada leads to a rise in layoffs. As mentioned earlier, the decline in income could lead to a sharp increase in insolvencies, especially bankruptcies. The resulting losses could lead to a credit crunch, with financial institutions reducing their lending to protect their balance sheets. Moreover, the forced selling of homes and the lack of availability of mortgages could lead to a sharp correction in the housing market. The BoC would likely react by cutting interest rates relatively aggressively. However, the extent of cuts may depend on the outlook for inflation.
- Canadian households could be more resilient than expected to the financial strains of higher debt payments. We would point to continued pent-up demand in some areas and the substantial savings that many households have accumulated both during and since the pandemic as a possible source of this resilience.
- Inflation proves to be more persistent than expected. As mentioned earlier, high wages could feed into higher prices, preventing the anticipated moderation in inflation. Similarly, high input costs may contribute to inflation. While we do not think it would lead to a rate hike, such a situation would delay any rate cuts in 2024.
- Alberta is not immune to these shocks. Higher energy prices would be a positive for the province, while lower energy prices would be a negative. Layoffs in Alberta due to slower economic activity, while less likely than in the rest of the country, would pose a severe challenge to its heavily indebted households and could lead to much weaker growth in 2024.

Forecast details – Canada

	2023				2024				2022	2023	2024	2025
%	1Q23	2Q23	3Q23	4Q23	1Q24	2Q24	3Q24	4Q24				
Nominal GDP	-0.2	3.1	6.4	2.0	2.2	2.9	3.5	3.9	11.8	2.4	3.1	4.2
Real GDP	**2.5**	**1.4**	**-1.1**	**-0.2**	**0.0**	**0.7**	**1.3**	**1.7**	**3.8**	**1.0**	**0.3**	**1.9**
Personal consumption	5.3	-0.1	0.1	-0.5	-0.5	0.5	0.9	1.5	5.1	2.0	0.1	1.7
Non residential fixed invest	4.2	13.9	-10.1	2.0	2.0	2.0	4.5	4.5	4.0	1.3	1.6	5.3
Residential fixed invest	-12.6	-4.2	8.3	-2.0	1.0	1.0	1.0	1.0	-12.1	-10.0	1.0	1.9
Government expenditures	2.1	1.6	6.4	1.0	1.0	1.0	1.0	1.0	3.4	2.3	1.7	1.0
Exports	12.1	5.1	-5.1	1.3	1.6	2.1	2.7	3.1	3.2	4.6	1.2	3.0
Imports	4.0	4.4	-0.6	1.9	2.3	2.5	2.5	2.7	7.6	1.1	2.1	2.7
Contributions to GDP:												
Domestic final sales	2.6	1.2	-0.3	0.0	0.3	0.8	1.3	1.6	3.1	0.8	0.6	1.3
Inventories	-2.7	-0.1	-0.8	0.0	0.0	0.0	0.0	0.0	2.1	-0.9	0.0	0.6
Net trade	2.5	0.2	0.0	-0.2	-0.2	-0.1	0.0	0.1	-1.4	1.1	-0.3	0.0
Unemployment rate	5.0	5.2	5.5	5.8	6.3	6.8	7.0	7.0	5.3	5.4	6.8	6.4
Employment, 000	**231**	**80**	**76**	**95**	**33**	**23**	**90**	**150**	**750**	**480**	**262**	**639**
Personal income (y-o-y)	5.2	6.0	6.6	6.8	6.2	4.6	4.1	4.1	8.8	6.1	4.7	5.3
Disposable income (y-o-y)	5.2	5.0	5.0	4.5	4.4	4.7	4.6	3.5	5.5	4.9	4.3	4.7
Net corps. operating surplus (y-o-y	-12.7	-26.6	-22.4	-16.2	-4.9	2.7	0.6	4.3	14.7	-19.7	0.6	8.0
Current Account balance	-6.8	-7.3	-3.2	-5.8	-5.2	-5.6	-5.5	-5.5	-2.6	-5.8	-5.5	-5.5
% of GDP	-1.0	-1.0	-0.4	-0.8	-0.7	-0.8	-0.7	-0.7	-0.4	-0.8	-0.7	-0.7
Consumer prices	5.1	3.5	3.7	3.0	3.0	2.4	1.7	2.0	6.8	3.8	2.3	1.8
Core C PI	**4.9**	**4.1**	**3.9**	**3.4**	**3.1**	**2.8**	**2.4**	**2.4**	**5.0**	**4.1**	**2.7**	**2.1**
Housing starts (000)	223.1	248.9	259.1	266.1	267.7	270.0	272.1	274.3	263.3	249.3	271.0	288.7
Housing sales (y-o-y)	-37.4	-4.6	8.7	7.8	8.5	-6.0	-3.5	-1.0	-25.6	-6.4	-0.5	1.9
House price index (y-o-y)	-14.7	-8.6	0.0	4.2	3.6	-1.3	-0.5	0.5	12.5	-5.3	0.5	3.2
Overnight target rate	4.50	4.75	5.00	5.00	5.00	4.75	4.25	4.00	4.25	5.00	4.00	3.50
BoC 's assets ($bn)	382.3	357.5	323.6	318.3	308.1	276.5	266.5	262.4	410.7	318.3	262.4	218.2
3-month T-Bill	**4.34**	**4.90**	**5.07**	**5.00**	**4.90**	**4.65**	**4.15**	**3.90**	**4.23**	**5.00**	**3.90**	**3.50**
2-year government bond	3.74	4.58	4.87	4.22	4.03	3.84	3.69	3.59	4.06	4.22	3.59	3.50
5-year government bond	3.05	3.61	4.33	3.50	3.40	3.30	3.30	3.30	3.37	3.50	3.30	3.70
10-year government bond	2.90	3.26	4.03	3.40	3.40	3.40	3.40	3.50	3.30	3.40	3.50	3.80
USD/CAD	1.35	1.32	1.35	1.37	1.35	1.34	1.31	1.29	1.35	1.37	1.29	1.27
WTI (USD)	77.2	71.8	85.4	78.0	80.0	80.0	80.0	80.0	93.7	78.1	80.0	80.0
WCS (USD)	59.5	58.7	67.4	60.0	62.0	65.0	68.0	68.0	72.2	61.4	65.8	70.0
WTI-WCS	17.7	13.1	18.0	18.0	18.0	15.0	12.0	12.0	21.4	16.7	14.3	10.0
WCS (USD)	83.0	92.0	68.0	53.7	62.0	64.0	64.0	66.0	54.9	74.2	64.0	64.5
WTI-WCS	11.7	16.4	21.3	28.8	17.0	15.0	13.0	11.0	13.3	19.5	14.0	10.5

Source: Statistics Canada, Bank of Canada, Bloomberg, Alberta Central

Forecast details – Alberta

	2020	2021	2022	2023	2024	2025
Nominal GDP	-14.4	24.9	22.0	-5.1	5.5	2.8
Real GDP	**-7.8**	**4.6**	**5.0**	**2.4**	**1.8**	**2.2**
Personal consumption	-6.5	4.6	3.4	2.2	0.5	2.0
Non residential fixed invest	-20.6	12.9	11.6	7.4	5.0	5.0
Residential fixed invest	-3.9	22.1	-1.3	2.0	3.5	5.5
Government expenditures	-0.5	-0.6	3.1	1.0	0.8	0.8
Exports	-4.7	3.4	4.6	2.5	2.0	3.3
Imports	-8.7	8.4	7.0	3.3	3.0	4.0
Unemployment rate	**11.5**	**8.5**	**5.8**	**5.8**	**6.8**	**6.3**
Employment, 000	-162.0	117.0	116.6	84.5	77.3	122.1
Personal income (y-o-y)	2.1	3.7	6.5	0.5	3.7	2.8
Disposable income (y-o-y)	4.2	1.9	6.1	1.0	3.1	2.6
Net corps. operating surplus (y-o-y	-51.4	233.2	66.1	-5.5	12.6	9.7
Consumer prices	**1.1**	**3.2**	**6.5**	**3.4**	**2.6**	**1.8**
Core C PI	1.2	1.3	4.7	3.5	2.6	2.1
Housing starts (000)	24.2	31.9	36.4	36.3	45.4	50.5
Housing sales (y-o-y)	3.8	64.9	-1.3	-2.5	3.4	6.1
House price index (y-o-y)	1.1	9.3	4.8	1.2	2.3	1.1
Population growth (y-o-y)	1.3	0.6	1.7	3.6	3.4	2.5
Oil prices (WTI, $)	38.6	68.2	93.7	78.1	80.0	80.0
Oil price spread (WTI-WC S)	10.8	14.0	21.4	16.7	14.3	10.0
Overnight target rate	0.25	0.25	4.25	5.00	4.00	3.50
3-month T-Bill	0.06	0.16	4.23	5.00	3.90	3.50
2-year government bond	0.20	0.95	4.06	4.22	3.59	3.50
5-year government bond	0.41	1.30	3.37	3.50	3.30	3.70
10-year government bond	0.67	1.42	3.30	3.40	3.50	3.80
USD/CAD	1.27	1.27	1.35	1.37	1.29	1.27

Source: Statistics Canada, Bank of Canada, Bloomberg, Alberta Central

Charles St–Arnaud
Chief Economist
charles.starnaud@albertacentral.com

If you're interested in receiving the Economic Outlook and/or regular economic updates, please email:
communications@albertacentral.com

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