Environmental Scan

Quebec

2019–2021 HORIZON

This document summarizes the factors that influenced the 2019–2021 economic scenario prepared by the Labour Market Analysis Directorate – Service Canada, Quebec Region, in January 2019. Although indicators have evolved since that date, the change does not affect the findings in this scan.

ECONOMIC CONTEXT

We have seen a two-speed global economy since mid-2018. On the one hand, trade conflicts are threatening global growth and causing enormous uncertainty—in fact, the World Trade Organization (WTO) observed a slowdown in trade growth the close of 2018. The WTO also downgraded its 2019 growth forecast, given that the number of orders continues to decrease, and airfreight, automobile production and sales, agricultural products and electronic components were on the decline at the end of 2018. On the other hand, a number of countries are reporting strong economic growth. This robust economic performance has somewhat defied expectations as international trade continues to shrink.

The US economy grew at a fast clip in 2018, buoyed by personal and corporate tax cuts. However, manufacturers had to contend with the US trade policy, including tighter market conditions, higher industrial prices, deferred investments and delays in implementing ongoing projects owing to the scarcity of some materials, especially steel products. The situation was compounded by inflation and a sharp decline in tourism.

US-China tensions may also pose risks to global trade. The prices of products targeted by both China and the US have collapsed. The US domestic market is stretched by tariff-related inflation. Exporters are seeking alternative markets for their products, often at reduced prices, which raises concerns about dumping. Businesses are seeking compensation for lost earnings, adding to the cost of the trade war. This situation is an economic drag on all global economies.

Emerging economies generally rely on international trade to fuel their growth. In the early days of the millennium, the BRIICS countries – Brazil, Russia, India, Indonesia, China and South Africa – demonstrated the highest potential for growth. Today's weaker growth prospects in these countries have cast doubt on their ability to meet their debt obligations. Brazil is laden with debts from the *World Cup* (FIFA) and the *Olympic* Games, while dealing with political crises; Russia is still facing international sanctions that impede its growth; India and Indonesia still have a strong potential for growth, but their complex management systems and limited monetary reserves are leading to deferred structural investments; China is dealing with trade tensions that constrain its development; and South Africa is on the brink of recession. The *International Monetary Fund* (IMF) anticipates that the growth outlook in emerging countries will face pressure from debt and protectionist measures by 2020. As if on cue, Turkey is in the grip of a political and trade war with the US; Argentina is facing a difficult economic environment and has been forced to seek further assistance from the FMI and an emergency line of credit; and Venezuela has been experiencing a severe economic crisis since oil prices began to slide. And the list goes on.

Storm clouds are gathering over Europe. The situation in PIIGS countries – Portugal, Ireland, Italy, Greece and Spain – has improved since the sovereign debt crisis, but their economies are not at peak performance. Greece's economy is no longer in a state of financial crisis, but the labour market is still facing difficult challenges with a very high unemployment rate. The employment rate in the 20–64 age group paints another gloomy picture for the country: 58% of the workforce is employed, compared to 80% in Germany. The employment rate in the European Union is slightly above 72%, compared to 78% in Quebec. The Italian economy is facing pressure from the protectionist rhetoric propagated by the coalition government and a budget that has come under criticism for the size of its deficit. The Governor of the Bank of England has warned the British government that a no-deal Brexit from the European Union would very likely have a damaging impact – significant negative sectorial impacts have been projected even with a "harmonious" exit. The accumulation of economic challenges and debts/deficits in the European Union has led economists to forecast that the situation is as precarious as the one that led to the last recession, and many of them are apprehensive that 2019 will see turbulence.

Recently, Lynn Patterson, Deputy Governor of the *Bank of Canada*, closed her remarks at the *Hamilton Chamber of Commerce* with the following words: "It now appears the economy will be weaker in the first quarter of 2019 than we had projected in January. However, we still expect Canadian economic growth to pick up later in the year, supported by ongoing strength in employment and rising wages. We will have more to say in April, when we will have a new economic projection, as well as our annual updated estimates for economic potential and the neutral interest rate." All we can say is that the global environment is rather troubling.

In Canada, the United States-Mexico-Canada Agreement (USMCA) has dispersed some heavy clouds threatening the business environment. However, the renegotiation of the American Free Trade Agreement (NAFTA) has not been settled, as the US continues to maintain tariffs on steel, aluminum, softwood lumber, paper, PET resin, solar panels and pipes for pipelines. Let's be honest: a continuation of the current US trade policy is still a concern for the business community, especially in the fields impacted by the tariffs. However, the medium- and long-term outlook is looking up. The agreement still needs to be ratified by all three governments, and Mexico and Canada have called for the US tariffs to be removed before it is signed.

Consolidated Forecasts of the Main Banking Institutions in Canada

	GDP			Employment			Unemployment		
	2018	**2019**	**2020**	**2018**	**2019**	**2020**	**2018**	**2019**	**2020**
	2.4%	1.8%	1.4%	1.0%	0.7%	0.5%	5.5%	5.4%	5.3%
	2.1%	2.1%	1.7%	1.2%	1.0%	0.8%	5.9%	5.8%	5.8%
	2.9%	2.5%	1.8%	1.6%	1.3%	1.0%	3.9%	3.7%	3.8%

Source: LMAD, October 30, 2018 consolidation

The growth in private investments may improve over the next few years, perhaps as early as 2020, even though such decisions take time to materialize – and this will depend on the global trade environment, which could undermine these gains before then. Another risk to growth is that inflation and an increase in policy rates have pushed up prices and the cost of borrowing. Households may see an erosion in their discretionary spending if this trend is not offset by rising wages, while businesses may face higher costs as their earnings dwindle.

On a more positive note, the Office of the Auditor General of Quebec noted rigour in the process of establishing budgetary forecasts of the ministère des Finances and the surpluses identified, while the Parliamentary Budget Officer in Ottawa highlighted the sound management of Quebec's finances. Quebec's domestic demand has grown over the last 12 consecutive quarters. While it is still below its optimal level, gross fixed capital formation grew in 2018, construction is in a good position and there was growth in exports, tariff barriers notwithstanding. As such, indicators point to continued good results.

THE LABOUR MARKET

Following a year of robust job creation, 2018 returned to the slower growth we were accustomed to during the post-recession years. Full-time employment rebounded significantly, but this growth was largely eroded by the decline in part-time positions. In 2017, there had been significant gains in both types of employment, leading to strong growth overall.

The unemployment rate in Quebec continued to fall in 2018 to reach 5.5% – the rate had declined shortly after the recession but stabilized at around 7.7% between 2012 and 2015. The unemployment rate continued to fall thereafter, but a significant improvement to this indicator only came with the strong performance of labour markets in 2017. The employment rate barely grew in 2018 to 61.0%, which may well be close to the peak it is expected to reach before the anticipated decline over the next years. The participation rate dropped in 2018, bringing it back to the 2016 level. We believe that this indicator peaked in 2017 and that the participation rate will also most likely fall over the coming years.

Labour Market Indicators

Province of Québec	2016	2017	2018	Variation 2016-2017		Variation 2017-2018	
				Number	%	Number	%
Population 15+ (In Thousands)	6,887.9	6,931.9	6,985.9	44.0	0.6%	54.0	0.8%
Labour Force (In Thousands)	4,448.3	4,495.7	4,509.5	47.4	1.1%	13.8	0.3%
Employment (In Thousands)	4,133.1	4,223.3	4,262.2	90.2	2.2%	38.9	0.9%
Full-Time (In Thousands)	3,344.0	3,409.4	3,470.7	65.4	2.0%	61.3	1.8%
Part-Time (In Thousands)	789.1	813.8	791.5	24.7	3.1%	-22.3	-2.7%
Unemployment (In Thousands)	315.2	272.5	247.3	-42.7	-13.5%	-25.2	-9.2%
Unemployment Rate	7.1%	6.1%	5.5%	-1.0		-0.6	
Participation Rate	64.6%	64.9%	64.6%	0.3		-0.3	
Employment Rate	60.0%	60.9%	61.0%	0.9		0.1	

Source: Statistics Canada, Table 14-10-0090-01 Labour Force Characteristics

Quebec has a good growth potential, but it needs to be achieved. Without getting into fear-mongering rhetoric, a number of labour markets are facing pressure owing to unmet labour needs. Businesses fear that they may not be able to find and retain the necessary workforce for their day-to-day operations. The issue is even more complex in a growing market.

Since 2009, the growth in Canada's labour force has slowed down and the participation rate has dropped. In Quebec, the drop started in 2003, but it has been limited in scope. The participation rate for the 40-44 age group peaked in 2018, with close to 92% of them employed or looking for employment. The figure stood at 76% for 55–59 year-olds, 52% for 60–64 year-olds and 11% for the 65 and over age group. This drop reflects retirements.

A look at the 20-64 age group, which represents the largest workforce in Quebec, shows that the situation is getting worse: this population has been declining since 2017. Moreover, youth aged 15–24, particularly young men, have been less active in the labour force for the past few years. In this context, hiring challenges may worsen. Finally, there may be long distances between the place of residence of those who are willing to work and available jobs, and a mismatch between the skills and experience sought and individuals' interests and education. As a result, regions have both unemployed people and unmet labour needs.

The above situation may be supportive of greater automation. However, this would require significant investments, but Quebec's industrial structure has a big gap – the base is dominated by numerous small businesses, which do not always have the resources, while the top includes some large businesses, which carry a lot of weight in the economy, are major prime contractors. In this structure, the middle layer is too small to serve as a bridge between the two poles. The irony though is that businesses that turn to automation need specialized personnel, but such workers are harder to find than the production jobs that need to be filled.

The issue of labour shortages in Quebec regions came up repeatedly in 2018. It was also stressed that the situation has persisted in some areas for many years and that due to demographic changes (aging population, migration of young people, falling birthrates), this does not bode well for the future.

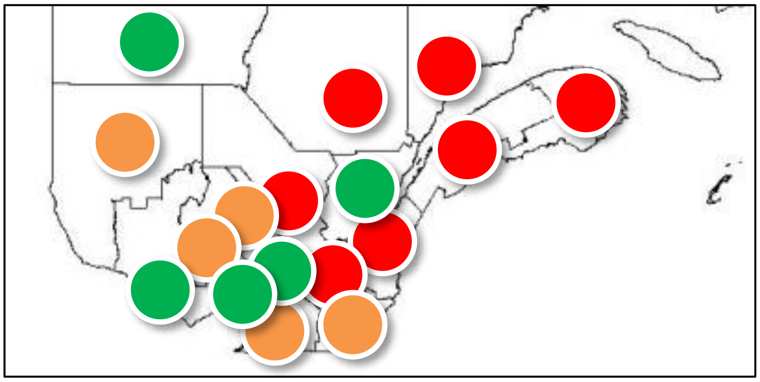
The *Institut de la statistique du Québec* uses the Labour Replacement Index (LRI) as well as other tools to illustrate the impact of the demographic trend on the Quebec labour market. The LRI illustrates the relationship between the number of young people from age 20 to 29 likely to enter the labour market and the potential number of retirees among people from age 55 to 64. The index only factors in the number of young people who may be available, but not their education level, interests or qualifications.

In 1987, the index for Quebec was 200, meaning that there were 200 young people age 20 to 29 for every group of 100 people age 55 to 64. In 2009, the index fell below the level of 100 young people for every 100 people approaching retirement. In 2017, the index dropped to 85, but it could drop to 79 by 2022.

The LRI shows that the majority of regions are already grappling with low labour replacement potential or on track to face significant challenges. Demographic forecasts indicate that the situation is not expected to improve. It is worth noting that these scenarios have already factored in migration, which currently accounts for approximately 70% of population gains in Quebec.

Recruitment challenges affect a cross-section of specialized and non-specialized positions in the goods-producing and service sectors. As illustrated on the map below, the challenges are more striking as one moves away from metropolitan areas with a larger and diversified pool of workers.

Labour Replacement Index in Quebec Regions
Averages for the 2018–2022 period



Labour Replacement Possible, Barring Exceptions	
Nord-du-Québec	151
Montréal	122
Laval	89
Capitale-Nationale	84
Province of Québec	**83**
Outaouais	80

Increasingly Difficult Labour Replacement	
Montérégie	76
Estrie	76
Lanaudière	73
Abitibi-Témiscamingue	72
Laurentides	70

Low Poential for Labour Replacement	
Côte-Nord	68
Centre-du-Québec	68
Chaudière-Appalaches	67
Mauricie	62
Saguenay–Lac-Saint-Jean	61
Bas-Saint-Laurent	55
Gaspésie–Les-Îles	45

EMPLOYMENT OUTLOOK IN QUEBEC – 2019–2021 HORIZON

We anticipate that growth will occur throughout the forecast period. However, the global economic slowdown, particularly in Europe and emerging economies, the global trade environment, which is engulfed in protectionist measures, and the pressure facing the Quebec labour markets, have tempered the expected growth.

Overall employment will grow over the next three years, but the gains will be lower than those achieved since 2015. Annual growth will be weak and there will be a slight drop each year, at an average annual growth rate of 0.7%.

Growth Scenario by Activity Sector

Province of Québec	2016-2018 Average		2019-2021
	Level In Thousands	Share of Total Employment	Average Annual Growth
All Industries	**4,206.2**	**100%**	**0.7%**
Goods-Producing Sector	853.4	20%	0.3%
Services Sector	3,352.8	80%	0.8%

Sources: 2016–2018 Employment – Statistics Canada, Table 14-10-0090-01, Labour Force Characteristics
Growth 2019–2021 – Service Canada, Quebec Region, Scenario of the Labour Market Analysis Directorate, January 11, 2019

Risks in Quebec During The Forecast Horizon

Short-term – 2019	
Risks with Positive Impacts	**Risks with Negative Impacts**
▪ USMCA dispels most uncertainties; private investment once again becomes a potential for growth ▪ Confidence level high	▪ USMCA subject to review in six years; invest or wait? ▪ US tariffs on lumber, aluminum, steel, paper, etc. still in force
▪ Public investments hit record highs over the next 10 years	▪ Public debt continues to grow and may weigh very heavily on budgets within five years
▪ Quebec's strong economic performance boosts labour markets	▪ Growth undermined by labour market recruitment challenges
▪ Governments take action to provide stimulus programs for individuals and businesses, thereby boosting spending ▪ Strong economic performance results in higher wages	▪ Higher interest rates increase cost of borrowing and measures are not significant enough to stimulate consumption ▪ Wages do not rise fast enough to offset growing needs
▪ Exports, including products under US tariffs, continue to grow	▪ Tighter conditions in Europe and emerging economies reduce potential; trade conflicts exact a high toll

Medium-term – 2020–2021	
Risks with Positive Impacts	**Risks with Negative Impacts**
▪ First year to see potential substantial gains in private investments	▪ US trade barriers and weakening European markets continue to undermine Quebec's export potential
▪ Governments introduce measures to promote procurement of machinery and computer equipment to enhance business competitiveness	▪ Quebec would enjoy two-fold benefits from these measures if procurement done in the province; however, this equipment is often imported
▪ GDP growth continues	▪ Consumption no longer a significant contributor; investments take time to materialize; exports are compromised
▪ Canada ratifies the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP); potential to diversify exports	▪ Slow pace of implementing Agreement and distance to markets lower potential for the province

Note: *In preparing this document, the authors have taken care to provide clients with labour market information that was timely and accurate at the time of publication. Since labour market conditions are dynamic, some of the information presented here may have changed since this document was published. Users are encouraged to also refer to other sources for additional information on the local economy and labour market. Information contained in this document does not necessarily reflect official policies of Employment and Social Development Canada.*

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