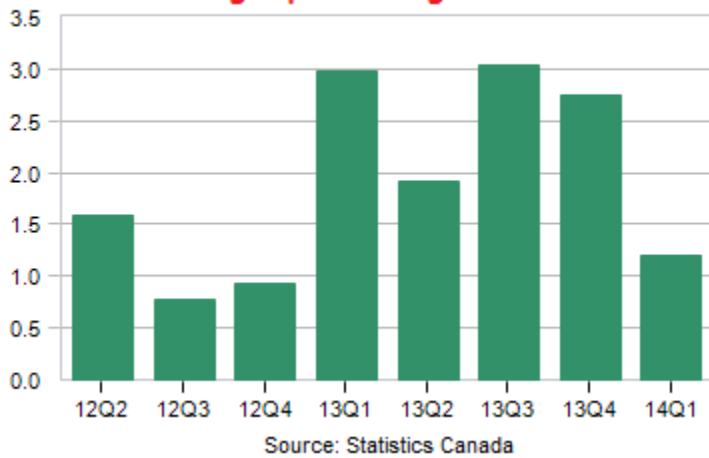


Canada's Economic Outlook

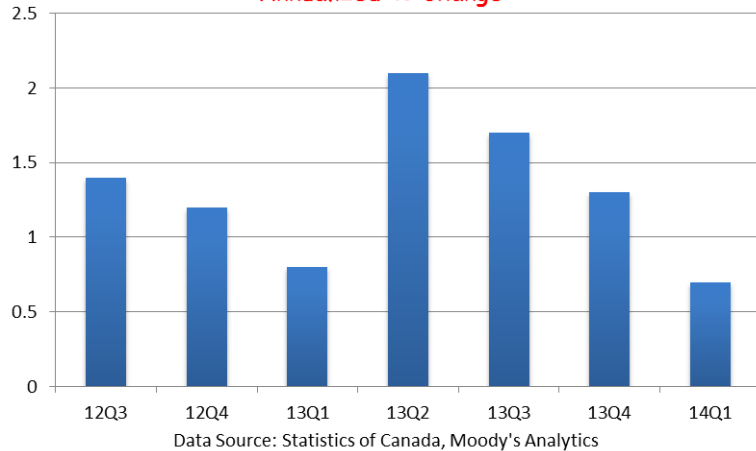
Canada Real GDP
% change quarter ago annualized



Canada's first quarter economic growth rate fell to its slowest pace since late 2012. The main culprit for the slowdown is a temporary reduction in domestic demand as a result of bad winter weather across North America. Despite the first-quarter slump, Canada's economy has been demonstrating a solid recovery. The economy is expected to pick-up in the second quarter and through the rest of the year.

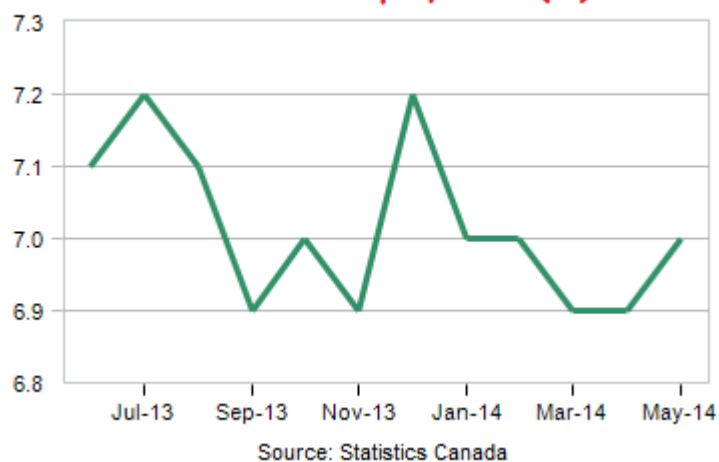
Improving economic conditions in the U.S. are expected to be a major driver for Canada's economic rebound. Canada's economic performance tends to lag that of the U.S. by about a quarter and, given the recent economic performance in U.S., growth in Canada is expected to pick up over the second half of the year. The economy should return to potential GDP by next year.

Canada Household Consumption
Annualized % Change



Canada's recent slowdown is largely due to sluggish household consumption. Household consumption grew at its slowest pace in a year in the first quarter. The slowdown is a temporary result of the harsh winter weather, which caused consumers to retrench. Notwithstanding the recent drop, Canada's household consumption has been growing at a solid rate. Consumer confidence measures indicate that consumers are more optimistic than they have been in three years. As a result, spending is expected to pick up through the rest of the year.

Canada Unemployment (%)



Canada's unemployment rate recently increased slightly to 7%. The recent uptick is the result of both an increase in cyclical and structural unemployment levels. Due to an increase in energy and commodity prices, labor demand for Canada's commodity exports industry has increased, while the supply of skilled labor in the industry has failed to keep up. At the same time, demand for labor in the nation's weakening industries, such as trade and manufacturing, is shifting to more high-tech positions. The mismatch of skills and demand has led to an increase in the number of structurally unemployed workers in Canada.

Meanwhile, the recent decline in Canada's economic growth and production has resulted in an increase in cyclical unemployment. Canada's cyclical unemployment is expected to decline over the coming months as the economy picks up. The economy should return to full employment by next year.

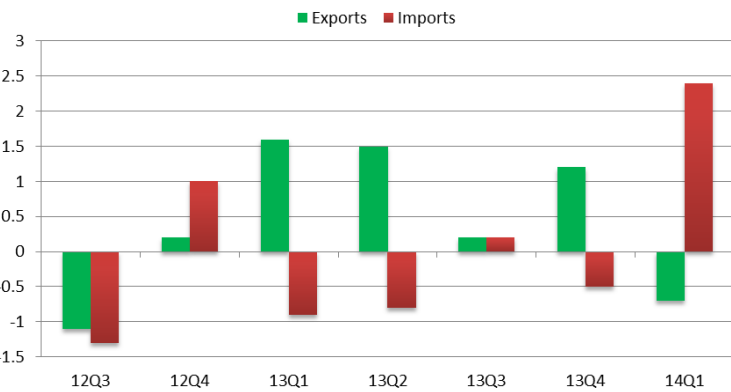
Canada Exchange Rate (C\$:US\$)



Source: The Economist Intelligence Unit.

The Canadian loonie has significantly depreciated against the dollar over the past year. This is mainly because the value of the dollar has increased as a result of the Federal Reserve reducing its quantitative easing. The Bank of Canada has maintained its monetary policy stance and kept its target for the overnight rate at 1% since September 2010. Since the Federal Reserve will continue to slow down its monetary easing over the rest of the year, the loonie is expected to continue to drop in value against the U.S. dollar in the coming months.

Canada Trade Annualized % Change

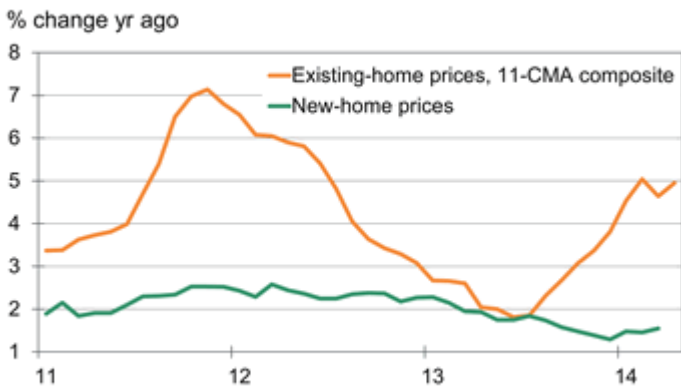


Data Source: Statistics of Canada, Moody's Analytics

Canada's exports have recently declined as a result of harsh winter weather in North America. Exports to the U.S., Canada's principal trading partner, dropped due to the decreased demand during the bad weather. In particular, demand for Canada's manufactured exports has dropped due to a stalling housing market in the U.S. and pent up consumer and business demand following the harsh winter weather. Exports are expected to rebound in the second quarter and through the rest of the year as demand from the U.S. picks up.

On the other hand, Canada's imports have seen strong gains. Imports have reached a record high due to a spike in consumer goods. This is mainly the result of improving economic conditions in Canada and strong consumer confidence levels. This trend is expected to continue in the near term as Canada's economic recovery builds momentum.

Canada Home Prices

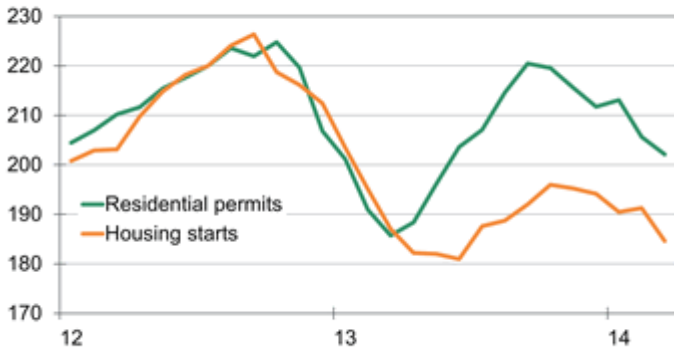


Sources: Statistics Canada, Teranet-National Bank, Moody's Analytics

Canadian home prices have been steadily rising since around mid-2013 and there is worry about a burst in a housing bubble. Home prices have reached their highest value on record, with the average home selling for over six times Canada's median family income. Thankfully, however, low interest rates in Canada have helped maintain a reasonable level of housing affordability.

Canada Housing Starts and Permits

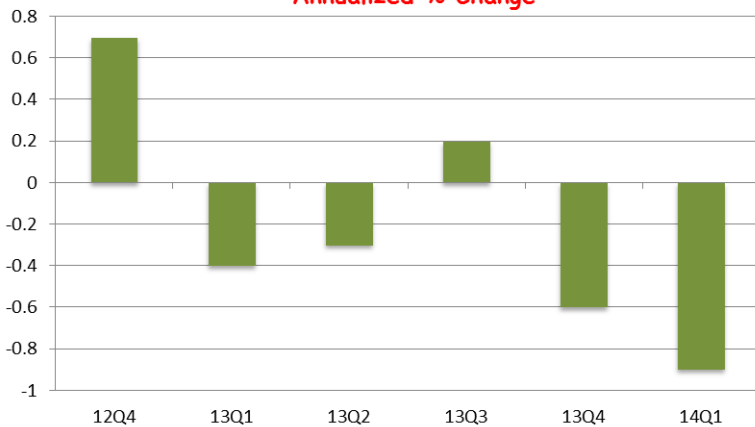
Construction units, 6-mo MA, ths SAAR



Sources: Statistics Canada, CMHC, Moody's Analytics

While house prices have been on an upward trend, home sales and housing starts have been on a downward trend since about mid-2013. This signals that Canada's housing market is cooling. As a result, house prices are expected to follow suit and slowly decrease in the near term. Overall, it looks like the housing market should be able to manage a soft landing.

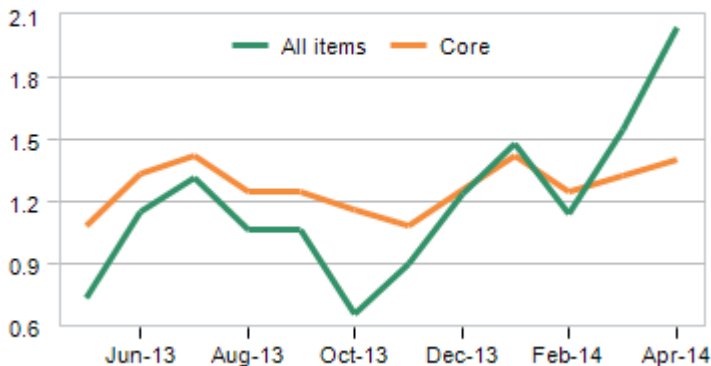
Canada Investment Annualized % Change



Data Source: Statistics of Canada, Moody's Analytics

Unfortunately, Canada's level of investment is on a downward trend and has demonstrated weakness since the beginning of 2013. The recent drop is largely due to a decrease in residential investment. Given the decrease in sales and housing starts, residential investment has been hit. This trend is expected to continue in the near term as Canada's housing market continues to cool.

Canada Consumer Price Index % change year ago



Sources: Statistics Canada, CMHC, Moody's Analytics

Both headline and core inflation rates have recently increased in Canada. This is welcomed news, as prices have remained suppressed for over a year. The main reason for the bounce in prices is higher energy prices. However, the recent depreciation of the loonie is also helping by increasing imported inflation. Further, given that foreign goods are relatively more expensive as a result of the depreciation of the loonie, import growth in Canada is expected to decline. This should help to reduce competition among Canadian businesses and boost overall prices. As prices steadily rise, it is expected that the Bank of Canada will slowly begin tightening its monetary policy stance.

Overall, notwithstanding the soft growth in the first quarter due to the unusual winter weather, Canada's economy is demonstrating a solid recovery. Growth is expected to rebound in the second quarter as a result of the better weather. Improving economic conditions in the U.S. will also help boost Canada's economic growth further. The economy is expected to return to potential GDP by next year.