ECONOMIC and FINANCIAL REVIEW

Direction principale
des affaires internationales
et de la vigie stratégique

October 15, 2018

AUTORITÉ DES MARCHÉS FINANCIERS

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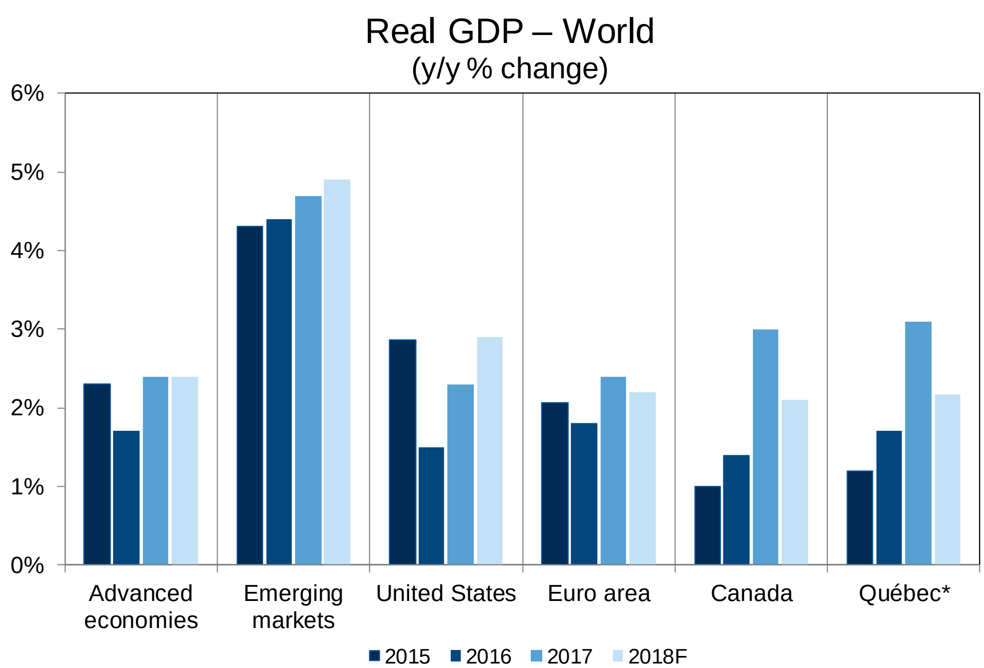
HIGHLIGHTS

- After peaking in 2017, global economic growth has been more subdued and less synchronized since the start of the year. Trade tensions are beginning to affect confidence and investment.
- The U.S. economy is operating at full capacity, and recent indicators suggest that it still has momentum. The Federal Reserve tightened its monetary policy again in September.
- The Canadian economy regained strength in the second quarter owing mainly to exports and consumption. The labour market has slowed since the beginning of the year, but the economy is still close to full employment.
- In Québec, growth has declined since last year, but nonetheless reached a respectable level of 2.5% in the second quarter. The unemployment rate continues to be near its lowest point in 40 years, while the number of job vacancies continues to rise.
- U.S. stock markets have continued to soar to record highs, largely unaffected by trade tensions. Stock exchanges elsewhere in the world have registered more mixed results. Oil prices are up due to concerns about supply from oil producing countries.
- In Québec, the mining sector is entering a transition phase after seeing mining product prices fluctuate for the past few years. The number of Québec listed mining companies has decreased, but their market capitalization is on the rise again.

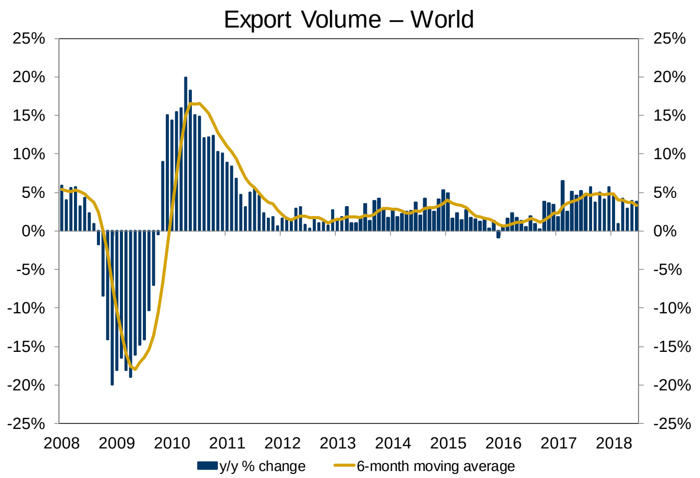


*For 2018, average of forecasts by major Canadian financial institutions
Sources: International Monetary Fund, Institut de la statistique du Québec and AMF

ECONOMIC CONTEXT

WORLD

After peaking in 2017, global economic growth has been more subdued and less synchronized since the start of the year. Global trade has slowed, as has global industrial production. The OECD has also lowered its projections for many advanced economies and emerging markets, citing the impact of trade tensions on confidence and investment.



Sources: CPB Netherlands Bureau for Economic Policy Analysis and AMF

The relative health of most advanced and emerging economies has nonetheless prompted some central banks to put away their extraordinary stimulus packages and, in certain cases, begin raising key policy rates. Despite this tightening, however, monetary policies are still highly accommodative.

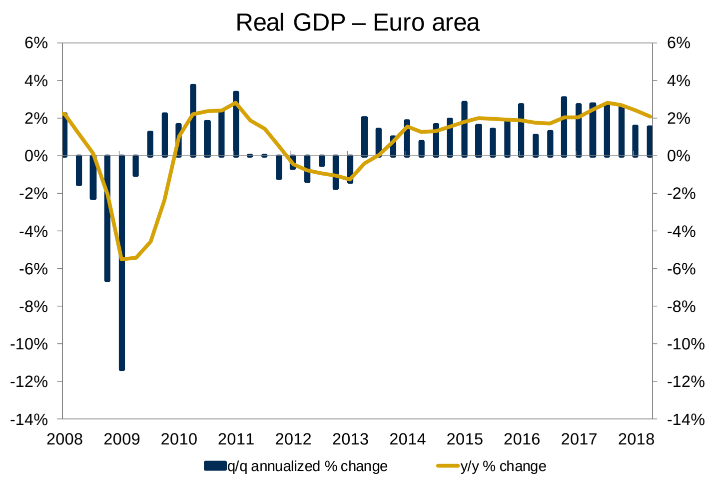
In the United States, the U.S. administration has continued to turn up the pressure on its trading partners with further tariffs and new threats. In the third quarter, the United States imposed tariffs on US$250 billion worth of Chinese imports, leading China to retaliate with tariffs on $110 billion of U.S. imports. Washington is still threatening to impose tariffs on all Chinese imports if Beijing does not change its trade practices, which Washington considers to be unfair.

This one-upmanship could disrupt trade, supply chains and global investment as businesses look for ways to circumvent the tariffs. Ultimately, the tariffs will take a bite out of producers' and retailers' profits or be passed on to consumers. More than 40% of Chinese exports are produced by foreign companies, many of which are American. This means that the tariffs will end up having a direct or indirect impact on U.S. businesses and households.

The United States and Canada managed to ink a last-minute deal on a renegotiated NAFTA in September after a bilateral agreement had been reached between Washington and Mexico during the summer. The new deal, which must still be approved, will tighten the rules of origin for the auto sector and will now cover financial services and e-commerce. The U.S. tariffs on steel and aluminum will, however, remain in effect.

In the meantime, the U.S. economy continues to operate at full throttle. The Fed raised its rates again in September, with further tightening to follow by the end of the year and next year.

In the euro area, the economy saw more restrained growth in the first half of 2018 compared to last year. Purchasing managers indexes are down, reflecting lower business confidence in the economic outlook. The European Union, which was also targeted by the U.S. administration, made some concessions to ease trade tensions with the United States.



Sources: Eurostat and AMF

The European Central Bank has left its rates unchanged and plans to keep them there until at least the summer of 2019. However, its asset purchases were reduced from €30 billion to €15 billion per month in October, and the quantitative easing program will wrap up by the end of the year.

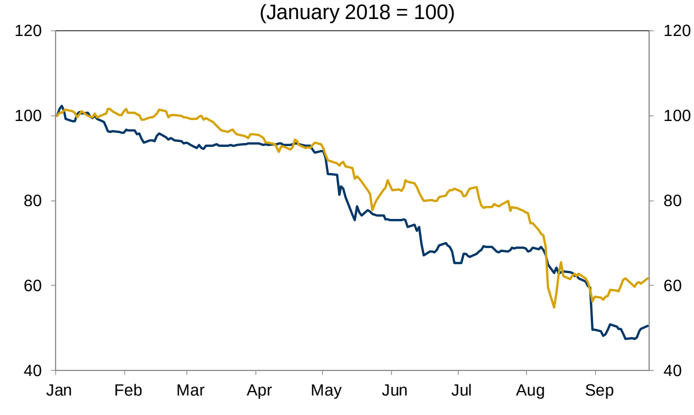
Brexit negotiations have stalled after the plan proposed by the British was rejected. European authorities gave Theresa May an ultimatum to reach an agreement no later than this fall. The IMF is predicting a recession in Great Britain if the country exits the European Union without an agreement. Meanwhile, the British economy is holding firm, and the Bank of England has continued to gradually tighten its monetary policy, increasing its key policy rate in August.

Despite solid growth rates, the situation remains difficult in many emerging economies, which have seen their currencies and stock markets plummet. Higher interest rates in the United States, a surging greenback and steeper oil prices have made some of those countries more vulnerable.

This is particularly true of Turkey and Argentina, both of which are grappling with huge external deficits and high foreign debt, much of it denominated in U.S. dollars. In Turkey, the central bank hiked its key policy rate to 24% to prop up the falling lira, rein in skyrocketing inflation and stem the flight of capital. Argentina asked the IMF to speed up payments under the IMF's lending program, which was increased to US$57 billion.

In contrast, China has relaxed monetary conditions through various measures in response to the economic slowdown and U.S. protectionism.

Argentine peso and Turkish lira against US dollar (January 2018 = 100)



Sources: WM Reuters and AMF

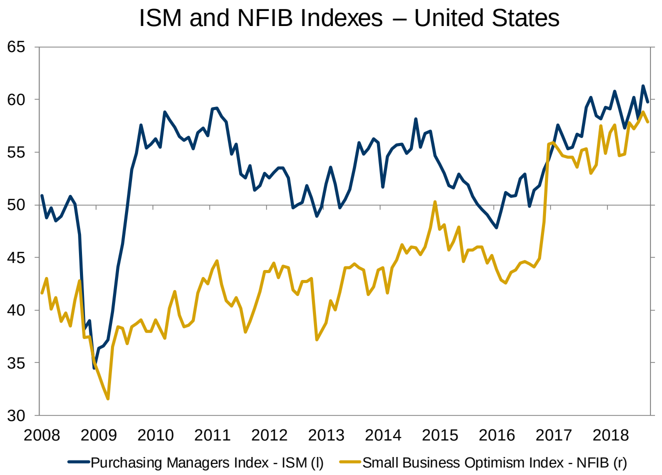
U.S. stock markets have continued to soar to record highs, largely unaffected by global trade tensions. Elsewhere, stock exchanges have registered more mixed results.

Oil prices rose during the third quarter, a trend that seems to be holding up. OPEC and Russia have refused to step up production, while the decline in Venezuela's output, and the U.S. sanctions against Iran are raising fears of a drop in supply on the global markets.

UNITED STATES

The U.S. economy is operating at full capacity, with recent indicators suggesting continued momentum despite escalating trade tensions and tighter financial conditions.

The ISM Purchasing Managers Index stood at 59.8 in September, after peaking in August at 61.3, its best performance in the past 14 years. Such levels reflect particularly high confidence in the U.S. economic outlook. The NFIB Small Business Optimism Index also peaked.



Sources: Institute for Supply Management, National Federation of Independent Business and AMF

GDP posted solid growth of 4.2% in the second quarter, buoyed by accelerated consumer spending, higher private investment and a substantial resurgence in exports. The outlook for the end of the year remains very good, with the U.S. economy maintaining its momentum.

Consumer spending was up 3.8% in the second quarter. A strong labour market, high household confidence and significant growth in household net worth will continue to bolster consumption and make it the main driver of economic activity in the months ahead.

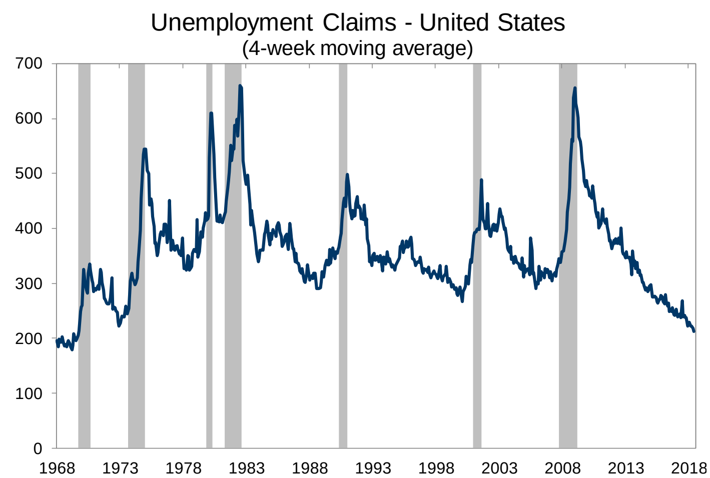
The same can be said of private investment. The achievement of full production capacity means that businesses will have to maintain the pace of capital spending.

The increase in exports in the second quarter could, however, prove fleeting and be the result of a surge in shipments abroad ahead of retaliatory trade actions on U.S. products. The contribution of net exports to economic growth may therefore have been short-lived.

In such a favourable context, the lull in the residential real estate market comes as a surprise. Housing starts have been retreating for the past few months, and home sales have been falling.

The continuing rise in house prices and increasing interest rates may have made potential buyers more skittish. Yet, the National Association of Home Builders reports strong demand for housing. The slowdown may therefore be due, in part, to an unusually low inventory of homes for sale.

The labour market remains strong and tight. Employment continues to post solid gains; the unemployment rate remains at a historic low; and the number of job vacancies is still growing. The main beneficiaries of this combination are workers. Wages, for example, have been steadily rising for close to a year now. Unemployment claims have just reached their lowest level since 1969.



Sources: U.S. Department of Labor and AMF

The Fed has raised its key policy rate again, increasing it to a range of 2 to 2.25%.

The economy is firing on all cylinders, and all the ingredients are there to fuel inflationary pressures, namely rising oil prices and higher wages, production costs and customs tariffs.

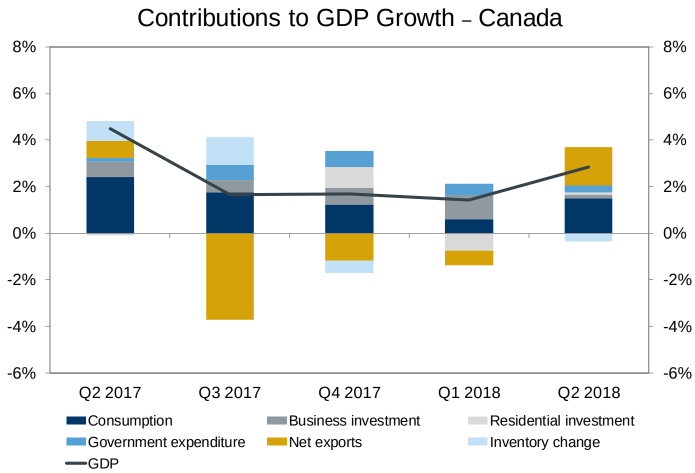
Economic indicators point toward continued solid economic growth in the second half of the year. However, the current pace is unsustainable and is largely attributable to the stimulating, but one-off effects of U.S. fiscal policy.

The Fed is therefore faced with a dilemma. Raising rates too quickly could choke off the current expansion. Conversely, raising them too slowly could stoke inflation and would lead to more drastic monetary tightening down the road. For now, the Fed Chair does not perceive any risk of overheating and is advocating continued gradual rate increases.

The U.S. economy is expected to gradually slow going into 2018–2019 as the Fed forges ahead with its campaign of gradual monetary tightening and as the effects of the tax cuts that took effect this year fade. Full resource utilization could, however, revive inflationary pressures, which would speed up monetary tightening.

CANADA

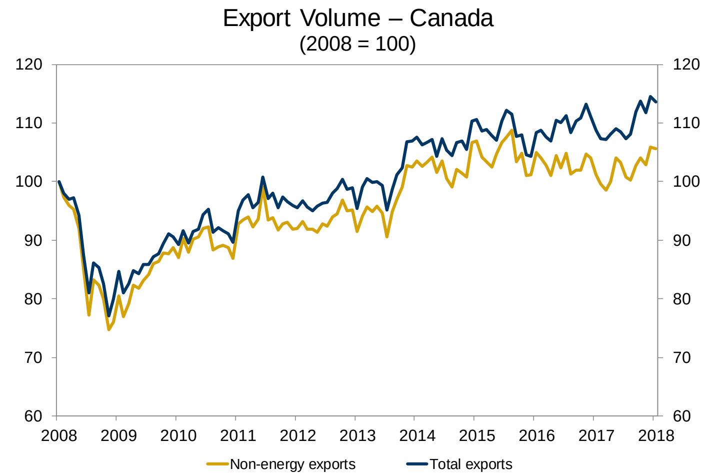
The Canadian economy rebounded in the second quarter owing mainly to exports and consumption. GDP rose 2.9% after registering more modest growth of 1.4% in the first quarter.



Sources: Statistics Canada and AMF

Foreign trade contributed to economic growth for the first time in a year. In the second quarter, exports jumped 12.3% on an annualized basis.

While up slightly in recent quarters, non-energy exports have been essentially stagnant since 2015. In fact, despite its weak currency, Canada is facing competitiveness issues in comparison with the United States, particularly in terms of productivity and labour costs.



Sources: Statistics Canada and AMF

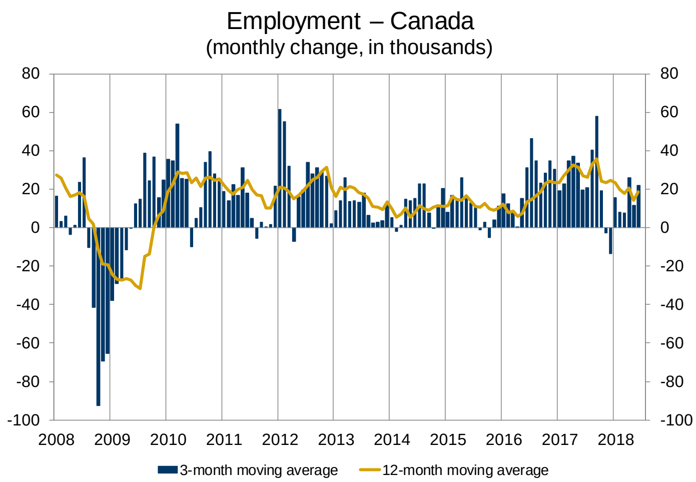
At least the last-minute NAFTA deal lifted the cloud of uncertainty that had been hanging over Canada–U.S. trade relations for the past several months. Canada had to give up limited access to its dairy, poultry and egg market; however, it was able to preserve the dispute resolution mechanism and is expected to be spared from potential U.S. tariffs on the auto industry. With roughly three quarters of Canadian exports landing in the United States, potential trade barriers would have a major impact on Canada's economy.

Business investment has slowed sharply, rising just 1.9% on an annualized basis, the smallest increase in the past six quarters. In a context of full resource utilization, this slowdown seems to be more the result of a pause than a trend reversal. Some businesses may have put off investments pending the outcome of trade negotiations with the United States.

Household consumption rebounded after cooling somewhat in recent quarters. Growth in consumption rose to 2.6% after increasing by 1.0% in the first quarter. Canadian households continue to be among the most indebted in the world. The ratio of household debt to disposable income is nearly 170%, suggesting that rising rates and debt service payments will eventually dampen consumption growth.

After experiencing robust growth in 2017, the labour market has pulled back considerably since the start of 2018. Since the beginning of the year, 48,700 jobs have been added, compared to 253,600 during the same period last year.

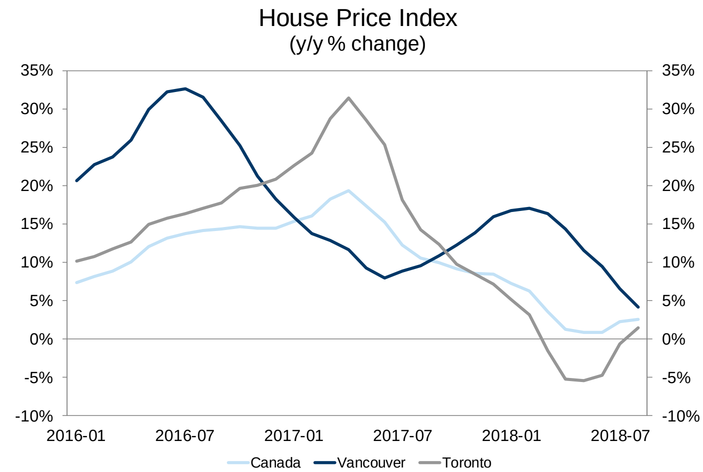
Despite this pullback, the labour market is still close to full employment, and recruitment problems are surfacing in various sectors and regions. The unemployment rate was 5.9% in September, close to its historic low.



Sources: Statistics Canada and AMF

The residential real estate market continues to wade through an adjustment period following the implementation of various macroprudential measures and an increase in interest rates. Housing starts have been on a slight downtrend since the beginning of the year but remain above 200,000 units.

There continue to be significant differences among the various areas of Canada. In the Toronto area, the market seems to be stabilizing. Sales are up and prices have begun to rise again. In Vancouver, however, sales are down significantly, and home prices are not rising as quickly following the introduction of macroprudential measures by the province in February, which built on federal measures that took effect in January.



Sources: The Canadian Real Estate Association and AMF

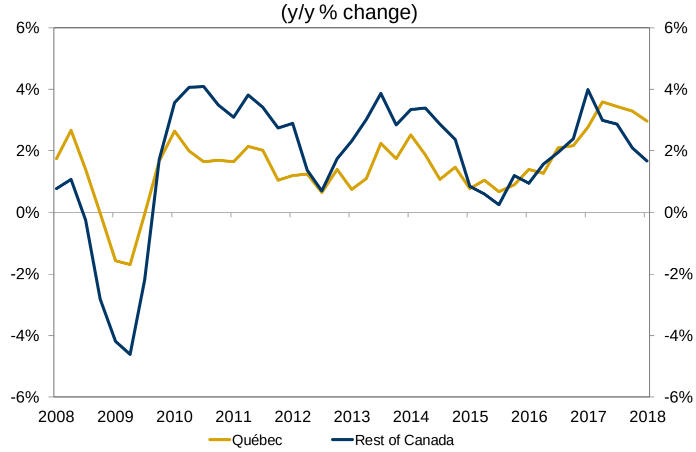
Inflationary pressures have been slow to emerge in the past year despite solid economic growth, but the trend of the past months is clearly an upward one. Total inflation reached 2.8% in August, near the top of the Bank of Canada's target range. However, part of the increase in inflation seems to be a one-time spike. As a result, the central bank left its key policy rate unchanged in September.

Full resource utilization and emerging inflationary pressures unquestionably argue in favour of monetary tightening. However, the Bank of Canada could once again exercise caution because of the risks related to real estate and high household debt.

QUÉBEC

Québec's economy has slowed since last year but has nonetheless kept up a respectably solid cruising speed. Gross domestic product posted annualized growth of 2.5% in the second quarter. On an annual basis, GDP rose 3% and again exceeded Canada's economic performance, despite the recovery underway in Alberta, in particular.

Real GDP– Québec and Rest of Canada
(y/y % change)

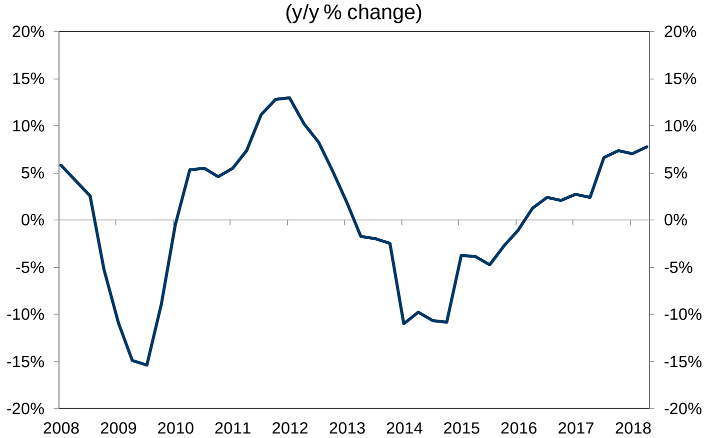


Sources: Institut de la statistique du Québec, Statistics Canada and AMF

Growth is now driven a little less by consumer spending and more by other components of aggregate demand, namely private investment, government expenditures and net exports. Indeed, growth in consumption has slowed over the past few quarters, in tandem with employment.

Private investment has continued its recovery, spurred by the relatively robust global economy, domestic demand and full resource utilization within the Québec economy.

Business Investment – Québec
(y/y % change)

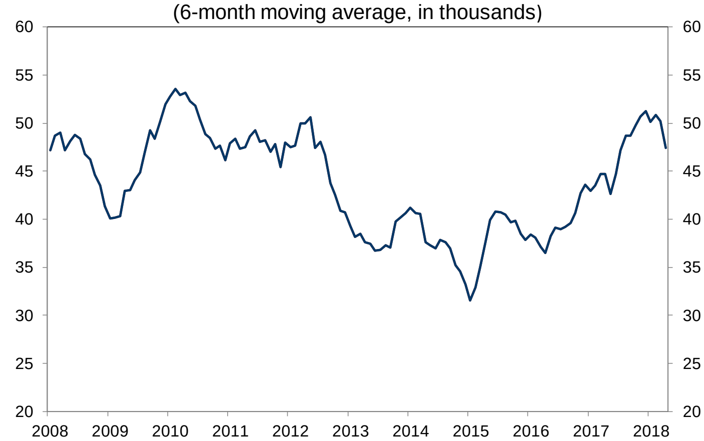


Sources: Institut de la statistique du Québec and AMF

The real estate market has remained robust. Home sales have continued to show strength, especially in the condo segment, while, at just above 2%, price increases have been moderate across the province.

In contrast to sales, housing starts have dipped after a year of exceptional growth. The numbers are still fairly high, however, averaging more than 47,000 units over the past six months.

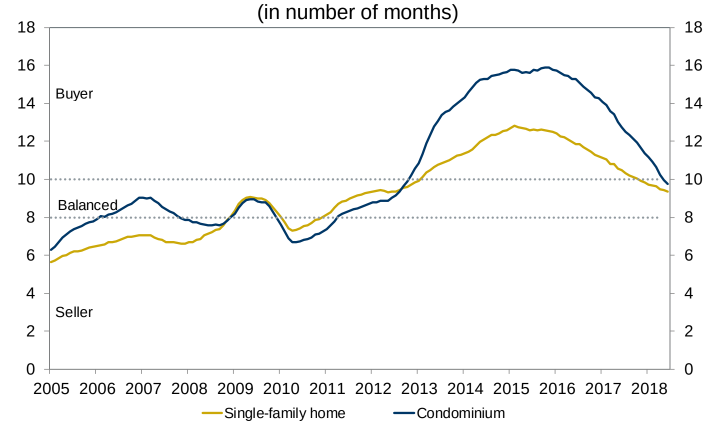
Housing Starts – Québec
(6-month moving average, in thousands)



Sources: Canada Mortgage and Housing Corporation and AMF

The Québec residential real estate market is therefore not experiencing the same excesses as in Ontario and British Columbia. Moreover, the ratio of unsold properties to sales level suggests better balance across the market.

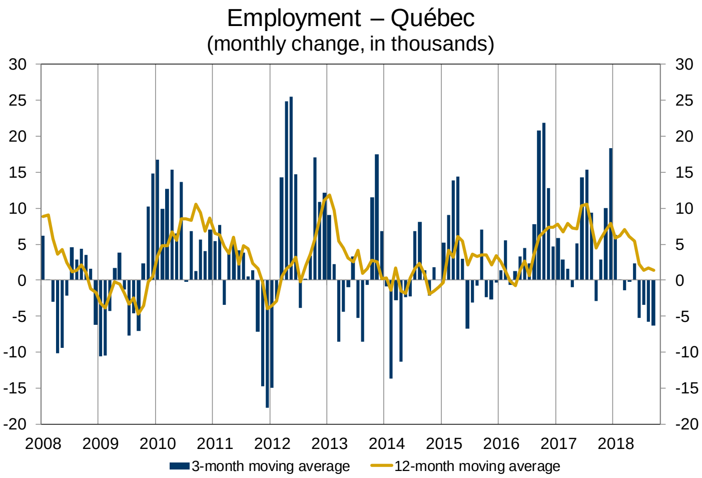
Ratio of Inventory of Unsold Properties
to Sales Level – Québec
(in number of months)



Sources: FCIQ Centris and AMF

The labour market has been faltering for several months now. Employment has declined several times in recent months after an exceptional performance in 2017.

More than 38,900 jobs have been shed since the beginning of the year, in contrast with the situation in 2017. At this same time last year, 39,100 jobs had been added.



Sources: Institut de la statistique du Québec and AMF

The unemployment rate has, nevertheless, barely budged and is now at 5.3%. It is therefore still close to its lowest point in 40 years, and its low sensitivity to employment fluctuations partly reflects the pressures of an aging population and the current labour shortage.

The number of job vacancies also continued to grow. More than 100,000 positions found no takers. This situation reflects not only the tight labour market, but also the mismatch between the skills sought by employers and those offered by workers.

The low unemployment rate has also caused wage rates to grow faster. For the first time since 2011, wages and salaries increased 4%.

Québec's economy is currently operating at full capacity, and its GDP performance since the start of 2018 is still better than the rest of Canada's. The fact that an agreement was reached in the NAFTA renegotiations also bodes well for Québec, whose economy depends heavily on foreign trade, particularly with the United States. However, the growth seen in the first half of the year should gradually become a little more restrained.

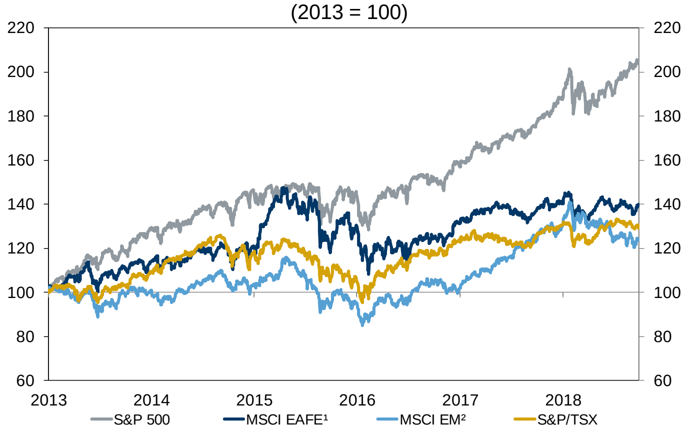
FINANCIAL MARKETS

STOCK MARKETS

Most of the world's major stock market indexes posted negative or anemic performances in the third quarter, as they have since the start of the year. The exception is the United States, where the S&P 500 recorded a return of 7.2% over the quarter, 9.0% from the start of the year and 15.7% over 12 months.

Some of the factors influencing investor sentiment over the quarter were fears of escalating trade tensions, the woes of some emerging markets and the slowdown in economic and trade growth.

Major Stock Market Indexes
(2013 = 100)

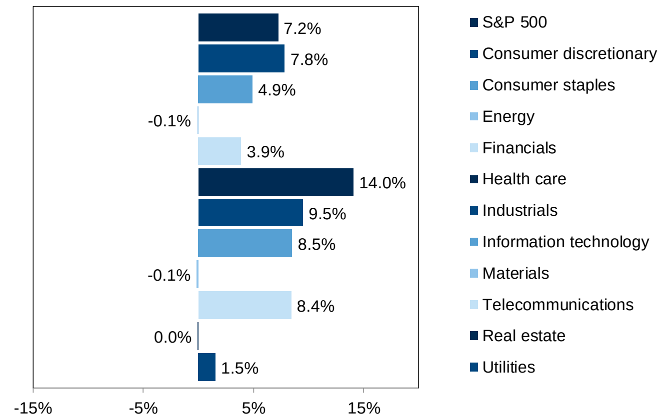


¹ Europe, Australasia and Far East ² Emerging Markets
Sources: Datastream and AMF

In the United States, the stock markets have benefited from a very favourable economic climate. The U.S. economy continues to fire on all cylinders and corporate earnings are enjoying strong growth, supporting by, among other things, lower taxes and still-favourable financial conditions.

Most sectors of the S&P 500 posted significant increases during the quarter. The information technology sector, in particular, continued to act as a driving force.

Performance of the Main S&P 500 Subindexes
(2018 Q3, q/q % change)



Sources: Datastream and AMF

Major changes to the industry classification system used for the S&P and MSCI indexes[1] will complicate matters somewhat in the fourth quarter. As of October 1, a new communications sector will replace telecommunications and will now include some companies that were previously in the information technology sector, like Facebook and Alphabet, or in the consumer discretionary sector, like Netflix.

In Europe, the stock market indexes have performed poorly since the beginning of the year. The changes in the European markets are due to a slowdown in European economic growth and, were the United Kingdom to abruptly exit the European Union without a prior agreement, the increasing likelihood of a hard Brexit. The European markets have also been affected by political changes in Italy and greater exposure to struggling emerging markets.

Since the beginning of the year, there has been a significant swing in investor sentiment against emerging markets, many of which have seen their currencies slide considerably, their access to credit reduced and their stock markets tumble.

Turkey, in particular, is dealing with a major crisis of confidence. Like many emerging markets, Turkey has benefited in recent years from significant capital inflows

[1] Global Industry Classification Standard Structure (GICS)

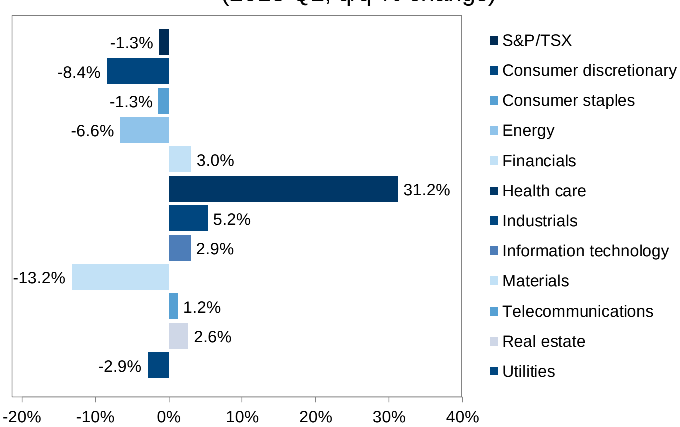
from foreign investors in search of returns, a movement that has now reversed direction. Argentina is also facing a major financial crisis and has had to turn to the IMF in order to avoid a disaster.

In both cases, a large current account deficit and a high level of foreign-currency-denominated (mainly U.S. dollar) debt have made the economy especially vulnerable to rising interest rates and a stronger U.S. dollar.

Investor confidence in emerging markets is not being helped by signs of an economic slowdown in China and that country's strained trade and diplomatic relations with the United States.

Some investors have been worried that this situation could spread to all emerging economies, but the risk of this happening appears to be under control for the time being. Most emerging markets are in a relatively good position to contend with higher interest rates and a rising U.S. dollar, particularly since their foreign-currency-denominated debt is lower than in Argentina and Turkey. Many emerging economies also have considerable foreign exchange reserves and large trade surpluses.

Performance of the Main S&P/TSX Subindexes
(2018 Q2, q/q % change)



Sources: Bloomberg and AMF

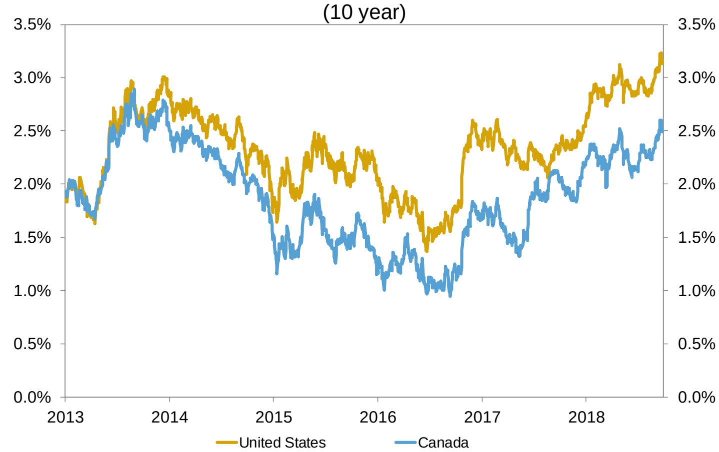
In Canada, the S&P/TSX posted a negative performance of around 1% both in the third quarter and since the start of the year. The energy sector, in particular, fell 6.6% during the quarter. Although global oil prices increased, the Western Canadian Select discount widened substantially, reflecting the persistent market access issues facing Alberta oil. The materials sector, weighed down by lower gold prices, saw an even more significant decline of 13.2%. In contrast, the industrials sector returned 5.2% in the third quarter, while the health sector posted a return of 31.2%, driven by cannabis companies.

Lastly, the overall performance of TSX-listed companies headquartered in Québec was similar to that of the composite index. The Morningstar National Bank Québec Index returned negative 1.3%, dragged down by the materials sector.

Bond markets

The bond market, pulled by opposing forces, did not move in a clear direction in the third quarter. On the one hand, an increased aversion to risk favoured government bonds, particularly U.S. government bonds, dragging down long rates. On the other hand, solid economic growth and monetary tightening in the United States continued to push rates higher.

Yield on Government Securities
(10 year)



Sources: Datastream and AMF

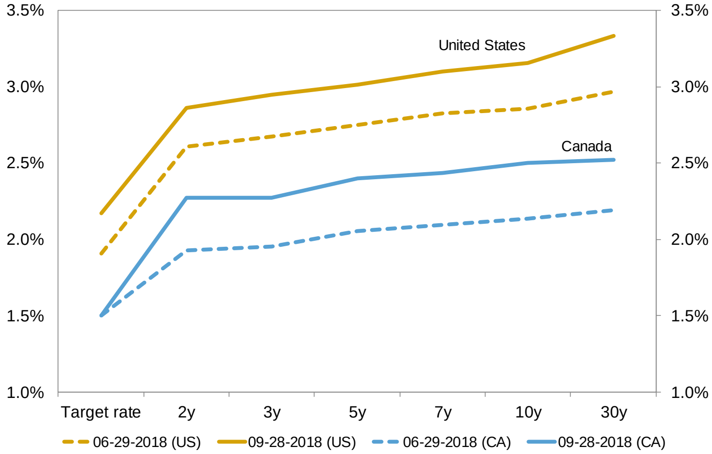
Ultimately, U.S. 10-year yields ended the third quarter at just above 3%, up slightly from the beginning of the quarter but at essentially the same level as in May. Interest rates continued to rise in October.

U.S. short yields have been increasing for several quarters with the successive rounds of monetary tightening by the Fed. Further monetary tightening is likely: Fed policymakers' median forecast shows an additional 25-basis-point increase by the end of 2018 and three increases of the same size in 2019.

The key policy rate will therefore gradually near the neutral rate of approximately 3%, according to many estimates. From there, any further monetary tightening will move monetary policy into restrictive territory.

Elsewhere in the world, the major central banks in advanced economies continue to adopt highly expansionary monetary policies, but the winds are gradually shifting. The European Central Bank will wind up its quantitative easing program by the end of the year but does not plan to increase its key policy rate before the summer of 2019.

Yield Curves – United States and Canada



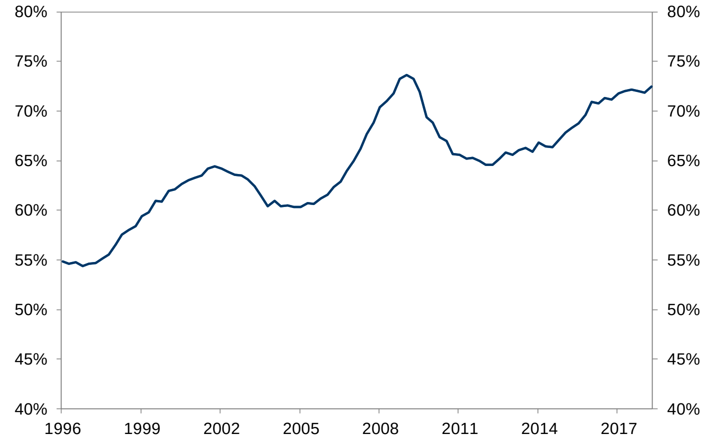
Sources: Datastream and AMF

In Canada, bond yields edged up across the curve in the last quarter in response to the strong performance of the Canadian economy. Nonetheless, Canadian yields remain below U.S. yields.

The Bank of Canada is expected to continue to gradually tighten its monetary policy, but at a slower pace than the Fed. The Canadian economy is likely more sensitive to rate increases because of high household debt and continuing imbalances in the residential real estate market.

As for corporate bonds, spreads with government bonds remained fairly stable during the third quarter in Canada and the United States. Yield spreads are historically very low, suggesting, among other things, that investors are not particularly concerned about corporate financial positions.

Corporate Debt to GDP Ratio – United States



Sources: Federal Reserve and AMF

Corporate debt levels nonetheless appear to be relatively high from a historical perspective. Low interest rates since the Great Recession and strong investor demand for corporate bonds have prompted many corporations to favour debt financing over equity financing. The normalization of interest rates will inevitably result in higher debt servicing costs and, to some extent, a relative deterioration in the balance sheets of some corporations.

Market Performance

Stock Markets

		Level	% change							Last 12 months	
		2018-09-28	1 month	3 months	6 months	9 months	1 year	3 years[2]	5 years[2]	Min.	Max.
MSCI All Country World Index		610	0.3	4.2	6.3	3.8	9.0	11.1	8.3	560	622
MSCI EAFE[1]		1,152	1.2	1.8	4.1	-1.0	2.3	6.4	5.0	1,085	1,207
MSCI Emerging Markets		57,943	-1.4	-1.0	-5.2	-4.8	0.3	9.6	4.8	56,288	65,823
S&P 500		2,914	0.4	7.2	10.3	9.0	15.7	14.9	11.6	2,519	2,931
S&P/TSX		16,073	-1.2	-1.3	4.6	-0.8	2.8	6.5	4.7	15,035	16,567
Morningstar National Bank Québec Index		289	-1.4	-1.3	5.1	0.3	6.8	9.1	12.2	270	299

Bond Markets

		Level								Last 12 months	
		2018-09-28	-1 month	-3 months	-6 months	-9 months	-1 year	-3 years	-5 years	Min.	Max.
Québec	10-year	3.0	2.8	2.8	2.7	2.6	2.8	2.5	3.6	2.4	3.1
Ontario	10-year	3.0	2.9	2.8	2.7	2.6	2.7	2.4	3.6	2.4	3.1
Canada	10-year	2.4	2.2	2.2	2.1	2.0	2.1	1.4	2.5	1.8	2.5
United States	10-year	3.1	2.9	2.9	2.7	2.4	2.3	2.0	2.6	2.3	3.1
United Kingdom	10-year	1.6	1.4	1.3	1.3	1.2	1.4	1.8	2.7	1.1	1.6
Germany	10-year	0.5	0.3	0.3	0.5	0.4	0.5	0.6	1.8	0.3	0.8
	AA Corp. (10-year)	3.3	3.2	3.1	3.0	3.1	3.3	2.9	3.5	2.8	3.4
Canada	BBB Corp. (10-year)	4.0	3.8	3.8	3.8	3.8	4.0	3.8	4.4	3.6	4.1
	BBB - 10-year Gov. spread	1.6	1.6	1.6	1.8	1.7	1.9	2.4	1.8	1.6	1.9
	AA Corp. (10-year)	3.8	3.6	3.7	3.6	3.1	3.1	3.1	3.4	3.0	3.9
United States	BBB Corp. (10-year)	4.5	4.4	4.5	4.2	3.7	3.7	4.1	4.4	3.6	4.6
	BBB - 10-year Gov. spread	1.5	1.5	1.6	1.5	1.3	1.4	2.1	1.8	1.2	1.7

[1]Europe, Australasia and Far East [2]Annualized returns

Sources: Datastream, Bloomberg and AMF

SPECIAL FEATURE

SPOTLIGHT ON THE QUÉBEC MINING SECTOR

Global trends in the mining sector

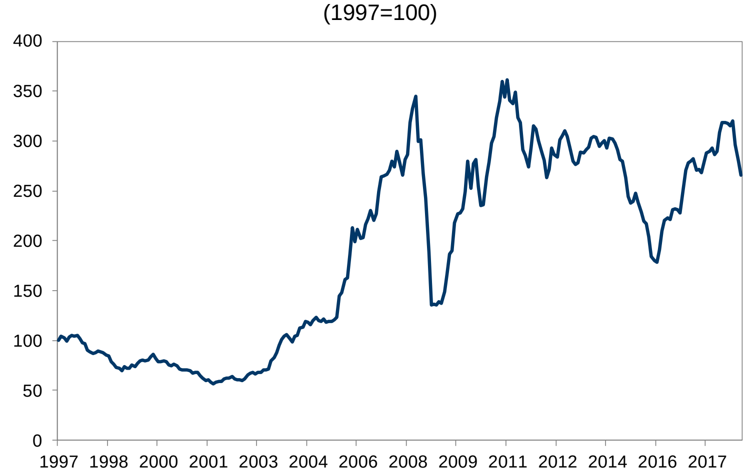
Mining product prices have seesawed for the past 20 years, mirroring the ups and downs in the global economy. In the first decade of the 2000s, the mining sector experienced strong expansion, driven by growing demand from emerging economies due, in particular, to accelerated development in China. Higher prices and demand spurred mining company investment.

After the 2008 financial crisis, mining product prices rebounded, reaching a record high in 2011. Prices then experienced a long period of decline, dropping 50% in five years. This decrease was partly the result of a slowdown in global demand, especially from China as it transitioned from an investment- and export-based economy to an economy based on domestic consumption and services.

Global economic growth regained momentum in 2016, once again fuelling demand for metals and other minerals. Mining companies around the world have shown cautious optimism about the sector's recovery by moderately increasing their investments.

To date, metal prices have recovered roughly 70% of their value since the peak in 2011, but this recovery is not distributed evenly across the various products. The prices of some mining products, including copper, gold and those related to new technologies, such as lithium and graphite, have risen more significantly.

Commodity Price Index - Metals
(1997=100)



Sources: Commodity Research Bureau and AMF

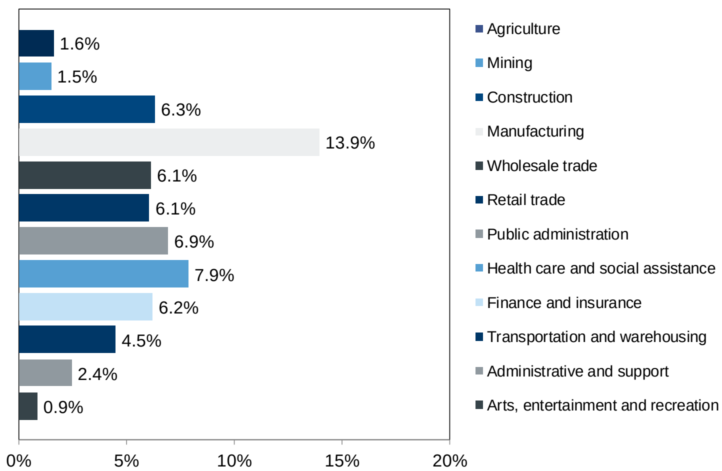
Québec, a major producer

Québec ranks second in Canada behind Ontario in terms of mining production value, and its production is also the most diversified. Québec production totalled $8.9 billion in 2017, or approximately 20% of the Canadian total.

Many juniors (mining companies that are generally not yet at the production stage) and some larger Canadian and foreign mining companies have operations in Québec. They produce mainly ferrous metals, precious metals (gold and silver), base metals (nickel, copper and zinc) and diamonds. Québec also has significant potential for minerals used in the manufacture of technological products, including lithium, graphite and rare earths.

In 2017, the mining sector accounted for 1.5% of Québec's GDP and employed close to 18,000 workers, representing 0.5% of all Québec employment.

Share of the Major Sectors in Québec's GDP

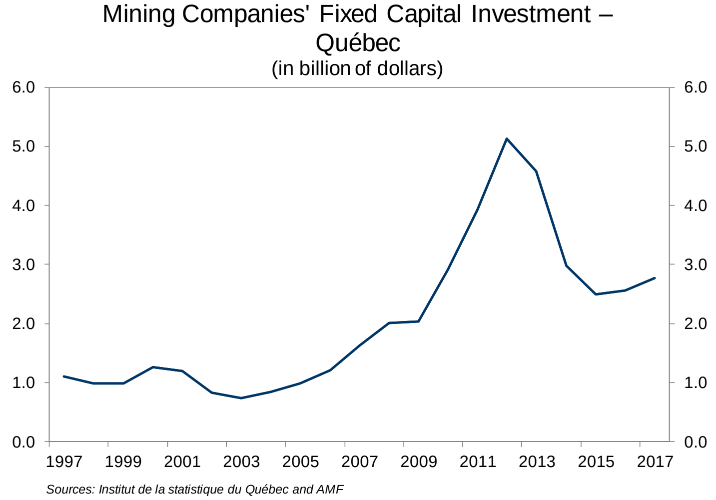


Sources: Institut de la statistique du Québec and AMF

Rebound in investment

After the slump in mining product prices from 2011 to 2015, investment in the mining sector fell sharply. Juniors, in particular, began to downsize their operations in order to reduce their debt and operating costs. This period also saw many mergers and acquisitions.

With global demand on the rise, investment spending is beginning to pick up again. Investment in Québec grew 8% in 2017 to total $2.77 billion. Substantially all such investment (97%) is shared among three regions of Québec: Nord-du-Québec, Abitibi-Témiscamingue and Côte-Nord. According to estimates prepared by the Institut de la statistique du Québec, the situation has continued to improve in 2018.



Diversified production

The ore extracted in Québec comes from some 30 active mines. Metal products account for most of Québec's mining production, representing 84% of total production for a value of $7.5 billion in 2017. Gold and iron ore each account for about 40% of extracted ores, while for base metals—particularly copper, zinc and nickel—the figure is close to 20%.

Production of non-metal products, meanwhile, reached $1.5 billion in 2017. Three quarters of production comes from construction materials (cement, dimension stone, sand and gravel) and the remainder from various minerals, including diamonds, graphite and mica. Québec's first diamond mine opened in 2016.

Approximately 30 mining projects under development were also identified in 2017. More than 40% of mining projects were for minerals used in the manufacture of technological products, such as lithium, graphite and rare earths. The other projects focused mainly on metals, particularly gold.

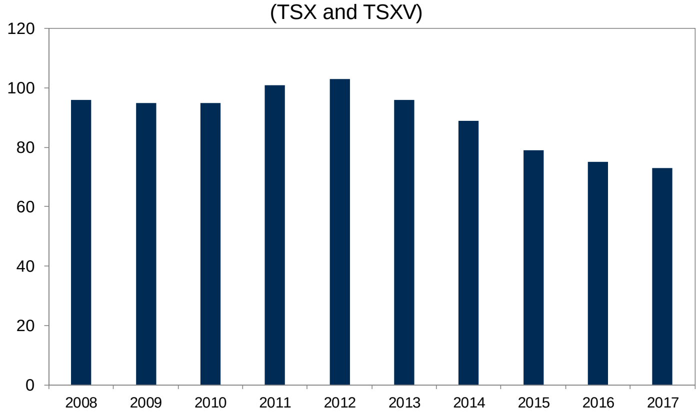
Fewer mining companies listed on the TSX and TSXV

The number of companies listed on the Toronto Stock Exchange (TSX) and the TSX Venture Exchange (TSXV) has been on the decline for many years. The mining sector is no exception. In fact, the decrease in this sector has been even sharper, owing to the fall in mining product prices in recent years and a wave of mergers and acquisitions.

While the drop is significant, the mining sector still accounts for half of the companies listed on the TSX and TSXV in Canada. In 2017, out of the 2,436 companies listed on the two exchanges, 1,211were mining companies.

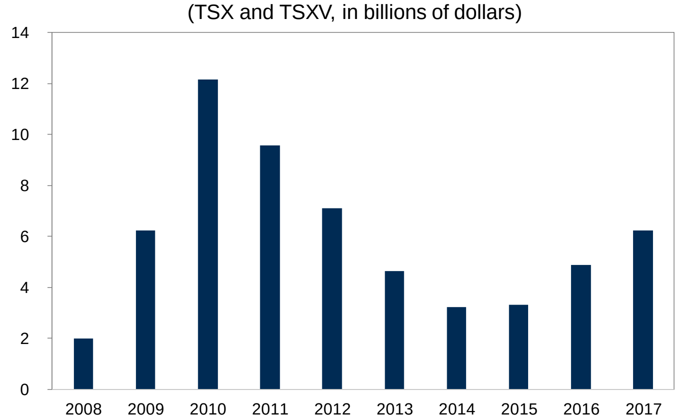
Out of 189 Québec listed companies, 73 are mining companies: 7 on the TSX and 66 on the TSXV. Therefore, despite its low weight in the economy as a whole, Québec's mining sector accounts for more than one third of all issuers, making it the largest sector in terms of number of listed companies.

Number of Listed Companies in the Mining Sector – Québec
(TSX and TSXV)



Sources : TMX Group and AMF

Market Capitalization of Listed Companies in the Mining Sector – Québec
(TSX and TSXV, in billions of dollars)



Sources: TMX Group and AMF

The number of listed mining companies has shrunk by about 30% in five years in Québec, similar to Canada as a whole. However, although the number of Québec mining companies has fallen since 2012, their market capitalization has rebounded, reaching $6 billion by the end of 2017. Moreover, mining companies raise capital on the exempt market, particularly from qualified investors.

The Québec mining sector also enjoys support from multiple financial backers, such as institutional investors, tax-advantaged funds and private equity funds. In addition, the flow-through financing program, enhanced by the Québec government, provides investors with an additional tax deduction and advantageous treatment of capital gains on the disposal of securities. This financial support from the Québec government and institutional investors has no equivalent in the rest of Canada.

Challenges facing the sector

The past ten years have been one of extremes for the mining sector. Mining product prices experienced record expansion, but also hit a very pronounced low. Mining production and investment are now on the rise and are expected to continue their upward trajectory.

However, mining companies are now facing new challenges. They must adapt to new environmental rules and concern themselves with the social acceptability of new mining projects. They must also contend with land access issues, build new infrastructure and find skilled labour.

New technologies will enable mining companies to address the shortage of skilled labour by automating certain jobs: using drones, for example, for exploration or using driverless vehicles for extraction and transportation. However, investments will need to be significant, since mining companies have under-invested in research and development for at least a decade.[2] Instead of investing in innovation, they have chosen to priortize investments providing a short-term return, cleanse their balance sheets and reduce costs.

Lastly, Québec companies will also have to deal with U.S. protectionism. Trade tensions with the United States, fuelled by tariffs on steel and aluminum and the difficulties in reaching an agreement on NAFTA, have recently made mining companies more hesitant about investing without guaranteed access to the U.S. market.

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[2] Deloitte, *Tracking the trends 2018 – The top 10 issues shaping mining in the year ahead*

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NOTE