AUTORITÉ DES MARCHÉS FINANCIERS

Economic and Financial Review

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Office of the Chief Economist

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Highlights

- In 2024, global economic growth remained steady at around 3%, but the major economies headed down divergent paths.
- In the United States, the economy proved especially resilient, while the economies of Canada and the euro area posted more moderate growth. In Québec, the economy started to grow again owing largely to consumer spending.
- Inflation cooled from the highs reached in recent years and, by mid-year, the major central banks began loosening monetary policy while keeping it restrictive.
- The economy and markets remained relatively insensitive to geopolitical tensions, but the imposition of sweeping tariffs by the new U.S. administration could begin to significantly impact the global economy as early as the first months of 2025.
- Stock markets delivered solid returns in 2024, continuing on the upward track they have been travelled since the 2022 correction.
- On the bond markets, short-term yields decreased owing to monetary policy easing, while long-term yields increased overall, causing yield curves to steepen.
- A number of issues will be on the radar in 2025, including the impact of Donald Trump's return to the White House, changing inflation and monetary policy, household and corporate debt, developments in the residential and commercial real estate markets, financial market valuations, and artificial intelligence.

	Real GDP			**Inflation**			**Unemployment Rate**		
% change	2023	2024e	2025f	2023	2024e	2025f	2023	2024e	2025f
United States	2.9	2.7	2.1	4.1	2.9	2.5	3.6	4.0	4.3
Euro area	0.4	0.8	1.0	5.5	2.4	2.0	6.6	6.4	6.4
Canada	1.5	1.3	1.8	3.9	2.4	2.0	5.4	6.3	6.7
Québec	0.2	1.3	1.6	4.5	2.3	1.8	4.5	5.4	5.7

e: estimate, f: forecast

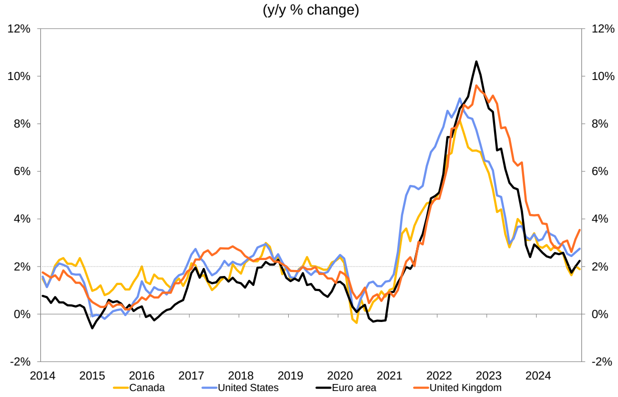
Sources: Bloomberg and AMF

Economy

World

In 2024, global economic growth remained steady at around 3%, but major economies headed down divergent paths. While the U.S. economy proved especially resilient, Canada and the euro area experienced more moderate growth. Inflation cooled from the highs reached in recent years, and major central banks began loosening monetary policy. The economy and markets remained relatively insensitive to geopolitical tensions, including the wars in Ukraine and the Middle East, but the U.S. election may begin to significantly impact the global economy as early as the first months of 2025.

Consumer Price Index – World
(y/y % change)

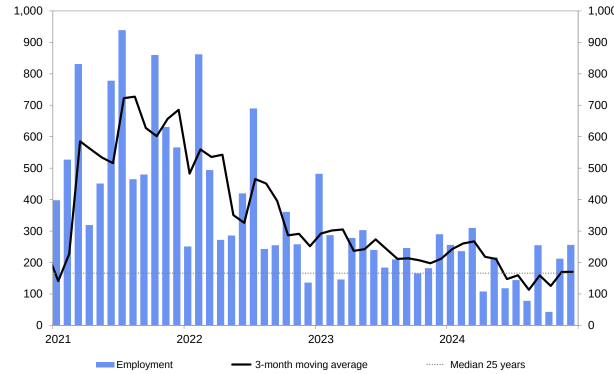


Sources: Eurostat, OECD and AMF

In 2024, the United States posted solid economic growth owing largely to sustained household spending. U.S. GDP growth reached 3.1% in the third quarter of 2024, after growing 3% in Q2, and the latest indicators point to growth remaining at that level through Q4. All in all, the outlook continues to be excellent for 2025, with expected GDP growth of 2% to 3%.

The labour market slowed somewhat but remains relatively robust. Despite some fluctuations, job creation remained firm over the year, with an average of 186,000 jobs being created every month. The slight rise in the unemployment rate over the past two years, from a low of 3.4% to 4.1% in December, enabled the labour market to move from a shortage situation to a market that is more balanced, though still at full employment. Nevertheless, this development helped ease wage pressures.

Employment – United States
(m/m % change, in thousands)



Sources: U.S. Bureau of Labor Statistics and AMF

Inflation fluctuated around 3% throughout the year, above the Federal Reserve's 2% target. The strength of the U.S. economy and persistent inflation caused the Fed to hold off on reducing its rates until September. The rate was lowered 100 basis points in the last four months of the year, to a range of 4.25% to 4.50%.

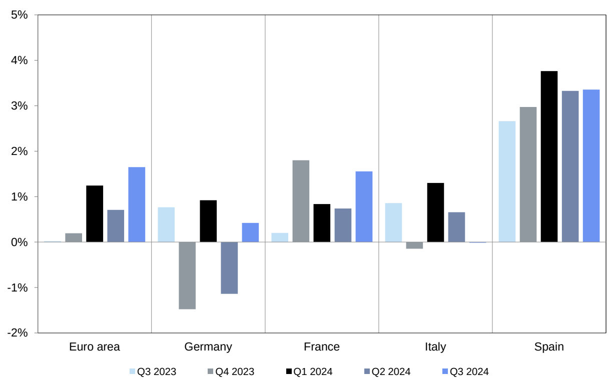
However, the return of Donald Trump to the White House in 2025 has muddied the waters. His threat of sweeping tariffs, including 25% tariffs on Canada and Mexico, could, if acted upon, reshape global trade and the global economy. The tariffs could hit the U.S. economy as hard as the economies of its main trading partners, pushing up inflation and dragging down GDP growth.

In the euro area, where the economic recovery is still tentative, the situation is quite different. The 0.8% rise in GDP in Q2 was followed by GDP growth of 1.5% in Q3. Germany, Europe's manufacturing powerhouse, has been stagnating for more than two years. Germany's GDP contracted 0.2% in 2024 after shrinking 0.3% in 2023.

In addition, the 20 member countries of the euro area are still facing challenges. The composite purchasing managers' index (PMI) ended 2024 at 49.6, under the 50 level separating growth from contraction. The services sector posted modest growth, while manufacturing contracted throughout the year.

With economic activity deteriorating and inflation, which closed the year at 2.4%, relatively under control, the European Central Bank started to lower its rates at the end of the spring. The deposit rate (its key policy rate) fell from 4% in June to 3% in December.

Real GDP – Euro Area
(q/q annualized % change)



Sources: Eurostat and AMF

China, which ended its ultra strict zero-COVID policy two years ago, is still in the midst of a slower-than-expected economic recovery. The country continues to grapple with persistent weakness in the residential real estate sector, fragile domestic demand, deflation risks, trade tensions with the West and demographic decline. GDP growth continued to slow throughout the year, from 5.3% in Q1 to 4.6% in Q3.

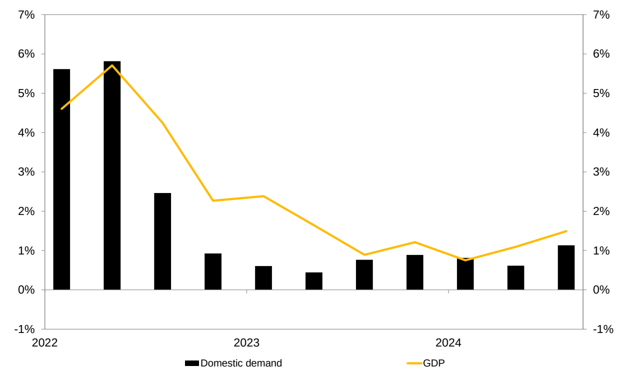
Throughout 2024, the Chinese government took a number of steps to stimulate the economy, including lowering interest rates and reducing financial institutions' reserve ratios, but these measures have yet to yield tangible results. Faced with likely increases in U.S.-imposed tariffs, the Chinese economy may take a further hit in 2025.

Canada

Hindered by tight financial conditions, Canada experienced only very modest growth in 2024. The economy was dragged down by residential investment, business investment and net exports, but supported by public spending and household consumption.

The pace of growth in domestic demand would have been relatively modest had it not been for strong public spending. As shown in the following graph, private domestic demand grew only marginally, at barely 1%.

Domestic demand and GDP – Canada
(y/y % change)

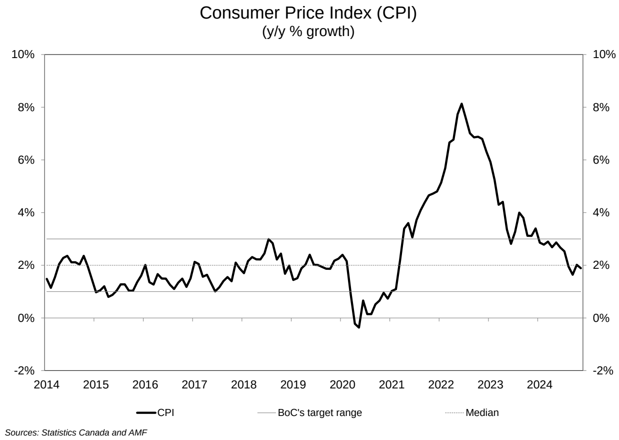


Sources: Statistics Canada and AMF

High interest rates and the cooling labour market put a damper on consumer spending, which was nonetheless buoyed by outsized population growth not seen since the 1950s. However, signs of improvement appeared near the end of the year. Conversely, private investment is still struggling to recover, while residential construction continues to experience the delayed effects of recent years' interest rate hikes.

The pace of job creation in the labour market was clearly insufficient to keep up with labour force growth, resulting in a higher unemployment rate. From a low of 4.8% in 2022, the unemployment rate climbed as high as 6.8% in 2024, ending the year at 6.7%.

The economic slowdown of the past two years has generated sufficient excess capacity to create an environment conducive to an easing of inflationary pressures. As measured by the Consumer Price Index (CPI), inflation is now close to 2% as compared to its peak of over 8% in 2022.



The slowdown in inflation is largely due to lower energy prices, although price growth for other CPI components also continues to slow. For example, food inflation, which has received extensive media coverage in recent years, has also fallen back. The price of food was up 2.7% at the end of 2024, far from the peak of 10.5% reached in 2022.

Reassured by declining underlying inflationary pressures and the slowing pace of economic growth, the Bank of Canada started a cycle of monetary policy easing, cutting its key policy rate from 5% to 3.25% in 2024. Despite successive interest rate cuts, monetary policy remains restrictive and further rate decreases are anticipated for 2025.

In 2025, GDP is expected to grow more quickly in the wake of monetary policy easing but only very slightly, with it struggling to achieve overall growth of 2% for the year.

This modest improvement in the economy will be largely driven by the pick-up in business investment and residential construction, the latter bolstered by monetary easing and the resulting loosening of borrowing conditions.

The effects of recent years' interest rate hikes will, however, continue to be felt in 2025. There are still a significant number of households that will have to renew their mortgages at higher interest rates than previously obtained, which means they will have less income available for other purposes.

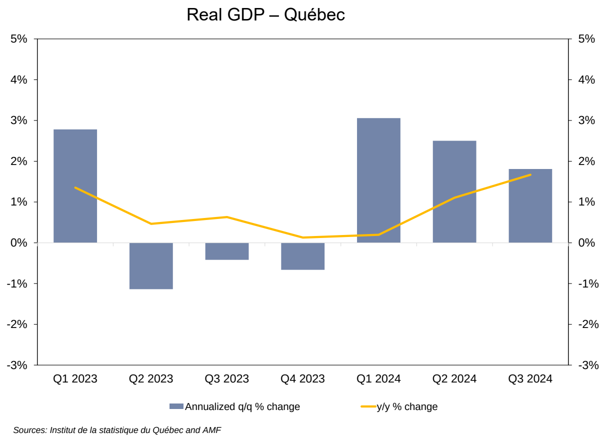
Last fall, the federal government announced a two-month federal sales tax holiday on certain goods. This tax break will have a minimal, one-time impact on GDP growth in the first quarter of 2025.

The anticipated economic upswing will be reflected in stronger job creation, leading the unemployment rate to first stabilize and then decline. With a slow but steady recovery, inflation is expected to hover around 2%.

The outlook for the Canadian economy, however, is clouded by the significant risk of potential impacts from the protectionist policies adopted by the U.S. government. Because of the close ties between the countries, the effects of the new U.S. administration's tariff, immigration and corporate tax policies could hit Canada hard and fast. Some investment projects could end up delayed, or even cancelled, simply because of the reigning climate of uncertainty, undermining the strength of the current recovery.

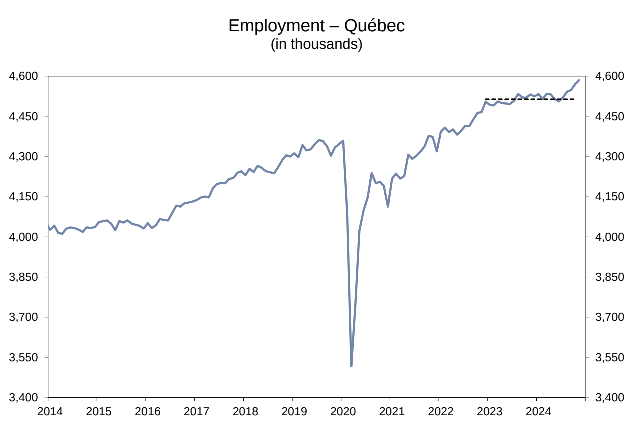
Québec

The Québec economy returned to growth in 2024 after a difficult 2023 marked by interest rate hikes, labour disputes and various major natural disasters. While GDP grew a mere 0.6% in 2023, preliminary estimates are that it will have doubled to nearly 1.2% in 2024.



Despite a sluggish labour market and increased unemployment, consumer spending in Québec remained relatively firm in 2024. Outsized population growth, driven by strong immigration, was a major factor. The succession of interest rate cuts underway will bolster household confidence and spending this year.

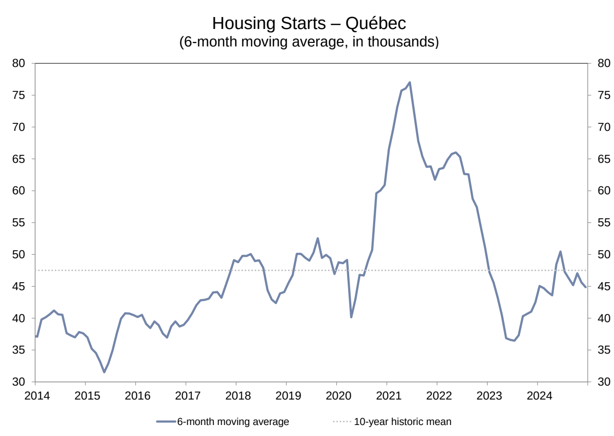
Employment stalled in 2023 and 2024, and the unemployment rate rose during that time, from a low of 4% to a high of 5.9% last fall. This weakness in the labour market also helped alleviate labour shortage challenges, at least for a while. The job vacancy rate, which reached a peak of 6.4% in 2022 and 5% in 2023, continued on its downward trend over the past year and now stands at 3.2%. This job vacancy rate is similar to the average observed prior to the pandemic. The employment recovery begun in the final months of 2024 will continue this year, in tandem with the upswing in the economy.



Business investment, which has been affected by restrictive borrowing conditions, will benefit from a slightly more favourable environment. Looser credit conditions and increased business leader confidence should stimulate capital spending.

Major projects taking place in the mining and battery industries and supporting the transition to a carbon neutral economy will play a key role in the recovery. At the same time, the large-scale investments planned by Hydro-Québec, primarily to increase production capacity and modernize its system, will significantly lift investment growth in Québec in the coming years.

After hitting an eight-year low in 2023, residential construction showed some encouraging signs of recovery in 2024. Housing starts increased, and this trend is expected to continue in 2025, sustained by interest rate cuts and a strengthening labour market.



Residential property sales are also seeing a sizeable rebound, despite a continuing decline in housing affordability and record-high home prices.

Buoyed by a solid and resilient U.S. economy, Québec exports recorded relatively strong growth, to the benefit, in particular, of strategic sectors such as aerospace and transportation equipment, which posted significantly higher international sales.

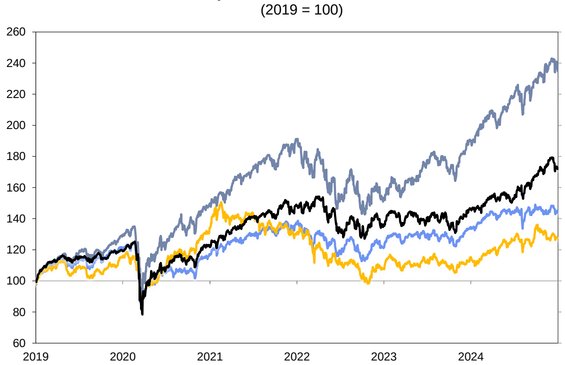
It is still too early to assess the effects of any economic policies the U.S. administration might adopt. However, higher tariffs would have considerable repercussions on the Québec economy owing to the size of its exports, which account for around 47% of the province's GDP, and its dependence on the U.S. market, which accounts for nearly 75% of Québec's international exports.

Financial markets

Stock markets delivered solid returns in 2024, continuing on the upward track they have travelled since the correction of 2022. The MSCI All Country World Index posted an impressive 18.4% gain in 2024, after returning 19.5% in 2023.

Stock markets, particularly in the United States, have been buoyed by the highly resilient global economy since 2023, despite monetary tightening on a scale virtually unprecedented in recent history. The expectation of a recession has been gradually set aside to make room for a scenario of a soft landing, moderation of inflationary pressures and normalization of interest rates.

Major Stock Market Indexes
(2019 = 100)



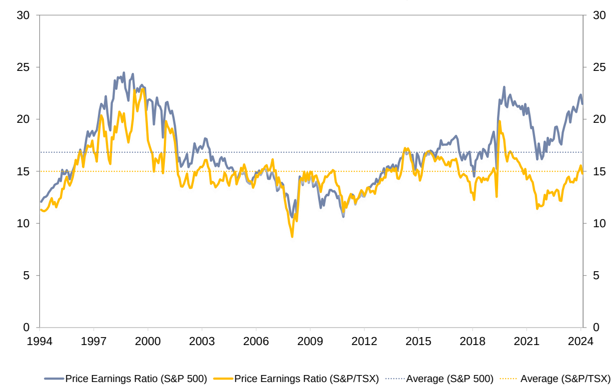
¹ Europe, Australasia and Far East ² Emerging markets
Sources: LSEG and AMF

Once again, U.S. stock market indexes led the field. The S&P 500 continued to dominate its peers with a 23.3% gain in 2024, fuelled by the strong performance of the tech giants and heightened investor interest in artificial intelligence. In addition, the technology-heavy NASDAQ returned 28.6% over the year.

There was also strong growth in the S&P 500 Consumer Discretionary and Financials, with returns of 29% and 28%, respectively, bolstered by the robust U.S. economy. Following the November 5 U.S. election, stock market indexes continued to rise, with volatility increasing slightly late in the year.

The tremendous growth in the U.S. indexes is largely due to higher valuation levels, while earnings growth is positive but well below index returns. The S&P 500 is currently trading at around 22 times forward earnings, well above its historical average.

Forward 12-month Price Earnings Ratio



Sources: LSEG and AMF

Certain elements of the incoming U.S. administration's economic program, including the promised of tax cuts and the deregulation of certain industries, could be good for the corporate earnings. However, the possible imposition by the new U.S. administration of sweeping tariffs could be very disruptive to global trade and lead to heightened financial market volatility.

In Canada, the S&P/TSX managed to generate a return of 18% in 2024, following a much more modest rise of 8% in 2023. Financials and Energy, the two largest sectors of the index, which, together, account for around half of its capitalization, posted excellent returns of 25% and 18%, respectively. Despite a marked slowdown in the Canadian economy and rising interest rates, Canadian households and businesses remained on relatively sound financial footing.

Elsewhere in the world, developed market indexes outside of North America delivered lower but nonetheless satisfactory returns. The

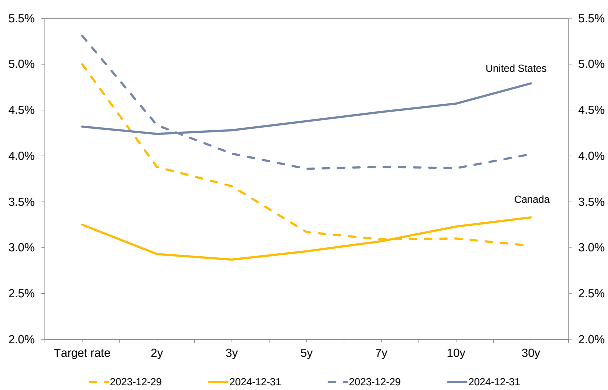
MSCI EAFE rose 8.4% for the year in an environment where a number of major economies, particularly in Europe, are stagnating. Emerging markets, including the Chinese stock indexes, also performed well after significant declines in 2023.

On the bond markets, short-term yields decreased as a result of monetary policy easing, while long-term yields increased overall, causing yield curves to steepen. The rise in long-term yields, particularly in the United States, was due to the strong economy and persistent inflationary pressures.

The spread between Canadian and U.S. bond yields widened, reflecting the relative weakness of the Canadian economy and the more accommodative stance of the Bank of Canada in 2024. For 2025, markets have priced in only a slight, very gradual easing of monetary policy, both in Canada and the United States.

Yield spreads on corporate bonds have narrowed, potentially reflecting improved economic conditions.

Yield Curves – United States and Canada



Sources: LSEG and AMF

The divergence in yields between Canada and the United States has contributed to the Canadian dollar's substantial decline in value since the start of the year. With the uncertainty surrounding the imposition of tariffs by the new U.S. administration, the Canadian dollar fell below the US$0.70 threshold for the first time since 2020.

Lastly, interest in the cryptoasset sector has increased significantly owing, in particular, to the SEC's approval of exchange-traded funds that hold Bitcoin directly. This growing enthusiasm for the sector was sparked by the election in the United States of the new administration, which is expected to take a more lenient regulatory approach to the sector. Bitcoin has surpassed US$100,000, up approximately 135% from the beginning of 2024, while the aggregate valuation of cryptoassets has reached US$ 3,700 billion.

Market Performance

Stock Markets		Level	% change				Last 12 months	
		2024-12-31	1 month	3 months	6 months	1 year	Min.	Max.
MSCI All Country World Index		1,029	-1.70	1.02	5.55	18.40	857	1,061
MSCI EAFE[1]		1,510	0.35	-0.91	-0.66	8.41	1,382	1,561
MSCI Emerging Markets		68,031	1.04	-4.56	0.89	10.54	58,553	72,731
S&P 500		5,882	-2.50	2.07	7.71	23.31	4,689	6,090
S&P/TSX		24,728	-3.59	3.03	13.04	17.99	20,585	25,692
Morningstar National Bank Québec Index		491	-2.84	3.51	12.45	19.91	403	509

Bond Markets		Level					Last 12 months	
		2024-12-31	-1 month	-3 months	-6 months	-1 year	Min.	Max.
Québec	10-year	4.02	4.02	4.02	4.02	3.72	3.72	4.16
Canada	10-year	3.23	3.08	2.96	3.50	3.11	2.87	3.87
United States	10-year	4.57	4.17	3.78	4.40	3.88	3.62	4.71
Canada	BBB - 10-year Gov. spread	1.35	1.43	1.58	1.65	1.69	1.27	1.74
United States	BBB - 10-year Gov. spread	1.04	1.09	1.24	1.27	1.34	1.01	1.39

[1]Europe, Australasia and Far East

Sources: Bloomberg and AMF

Issues that will be on the radar in 2025

Geopolitical tensions

Uncertainty and unpredictability appear to be on the rise in the global geopolitical environment, with protracted conflicts (Ukraine, Middle East) having unforeseen consequences, such as regime change in Syria; Donald Trump's return to the White House auguring a period of hard-power foreign policy; and persistent tensions between the West and Russia, China, Iran and North Korea. Heightened polarization and foreign interference are undermining the health of several democracies (e.g., France, Germany, South Korea) and leading to the election of anti-establishment parties that want to tear everything down and start over. The resulting coalition governments and political cohabitations are weakening governance in many nations.

U.S. politics

Donald Trump's return to the White House could shake up the world order, both politically and economically, and is already stirring up tensions with traditional allies and adversaries of the United States. The incoming U.S. president is using economic and military threats to put pressure on, and obtain concessions from, countries such as Canada, Mexico, China, Panama and Denmark/Greenland. The principles guiding him on foreign policy could lead to major changes in support to Ukraine, transatlantic relations, multilateral cooperation and the fight against climate change. His economic and trade policies, including the use of tariffs, deregulation, tighter restrictions on immigration, and expansionary fiscal and budgetary policies, may end up undermining both the U.S. and global economies.

Residential real estate

The residential real estate market continued its recovery last year, with home sales gradually strengthening. Housing prices rose during the year and even reached new highs. The supply of homes for sale remains insufficient, and homes have become increasingly less affordable. All the same, the monetary easing that is underway is expected to benefit potential new buyers and provide some relief to households that have mortgages coming up for renewal. Affordability issues will, however, persist.

Commercial real estate

Commercial real estate, particularly the office building sector, continues to face multiple challenges. Office building vacancy rates remain high in Canada's major cities, reflecting the ongoing prevalence of hybrid work arrangements in a number of fields. Construction levels in the office building sector have fallen significantly, which should eventually contribute to achieving a better balance between supply and demand for offices, but this rebalancing could take a long time. The Canadian financial sector's exposure to the office building sector is, however, still relatively limited.

Household debt

Canadian household debt fell in 2024 owing to slowing growth in credit and more sustained growth in disposable income. However, the household debt ratio in Canada remains very high, at around 175% of disposable income. In Québec, households are in a relatively better financial position than elsewhere in Canada, on both the debt and savings sides. Nevertheless, recent years' interest rate increases have ratcheted up debt servicing costs. A high debt level makes the Canadian economy more sensitive to changes in interest rates and any adverse economic conditions that may develop. The most indebted households are particularly vulnerable. The expected economic recovery and interest rate decreases should help curb this risk in 2025, but the threat of tariffs on Canadian exports to the United States could jeopardize the anticipated economic and job recovery.

Corporate debt

Canadian corporate debt remained fairly stable over the past year. However, relatively high interest rates and a weak economy had a negative impact on the financial health of some companies. The number of corporate insolvencies in Canada rose considerably in 2024, particularly in construction, transportation and storage, and accommodation and food services. Recent and expected rate cuts, together with stabilizing economic conditions, should allow companies to consolidate their financial position. Nevertheless, some companies may have to continue to refinance their debt at higher rates, and several risks continue to loom over the health of the global economy and the business environment.

Financial market valuations

The main stock market indexes rose sharply over the past year owing, in part, to the strong performance of the global economy, particularly in the United States, which enabled companies to deliver significant earnings growth. Stock markets were also buoyed by investor enthusiasm for the technology sector. However, the rise in U.S. stock market indexes largely reflects a significant increase in valuation ratios, with the S&P 500 currently trading at around 22 times forward earnings, well above the historical average. Should economic conditions deteriorate, stock market indexes could decline and corporate bond spreads could widen.

Labour shortage

The labour shortage situation appears to have reversed itself in 2024. The number of job vacancies fell and the job vacancy rate returned to pre-pandemic levels. The number of companies claiming to be constrained by an insufficient number of workers also fell from its peak. In 2025, however, the economic recovery, slowing population growth related to measures to limit immigration and the still-high number of retirements could result in a resurgence in labour market tensions. It is very possible that this improvement is due only to current economic conditions and that the structural challenges caused by an aging population will quickly resurface.

Climate change

The year 2024 was the warmest on record, with global temperatures rising more than 1.5°C above pre-industrial levels for the first time. Insurable losses from weather events in Canada reached new highs. The insurability of climate change risks will therefore have to be monitored in the context of high premium inflation. Moreover, the new U.S. administration may hinder international cooperation to fight climate change and protect the environment. Washington State may, nonetheless, soon join the California-Québec carbon market. Implementation of the new Canadian Sustainability Disclosure Standards will also need to be monitored in 2025.

Sustainable finance

Although consumers have access to a growing range of “green”, “ESG” (environmental, social and governance) and “sustainable” label financial products, the investment criteria for this new asset category have yet to be standardized. The implementation in 2025 of a green and transition finance taxonomy in Canada will need to be monitored. With the Republicans back in power in the United States, the regulatory framework for sustainable finance could become more fragmented internationally. Large-scale investments will be needed in clean technology and renewable energy to bolster the energy transition and address climate change-related issues.

Artificial intelligence

Artificial intelligence (AI) is helping transform the financial sector by improving effectiveness and innovation. Anticipated advances include integrating AI into self-directed brokerage and using it to enhance fraud detection and optimize trading strategies. AI-based risk management could also strengthen market stability and resilience. Despite these benefits, AI presents significant risks, including algorithmic anomalies, which could undermine confidence and fairness, resulting in compliance challenges, and employment displacement, disrupting traditional roles. In 2025, the regulatory framework is expected to be strengthened and new legislation implemented (particularly, the European Artificial Intelligence Act) to support innovation while protecting financial consumers.

Digital assets and decentralized finance

Despite their high volatility and the current divergence in the way different jurisdictions regulate them, cryptoassets are playing an ever-growing role in the global financial system. Bitcoin and Ethereum, in particular, are increasingly being incorporated into traditional financial products, such as derivatives and exchange-traded funds, strengthening their interconnection with traditional markets. Their popularity, combined with the outlook of regulatory easing in the United States, could heighten operational risk and the leverage effect, increasing the potential for crises and bankruptcies like those observed in 2022.