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ANNUAL REPORT
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FARM CREDIT CANADA

Economic environment

Global economic trends shape the business environment of Canadian agriculture and agri-food. Geopolitical tensions, trade disruptions and softer commodity prices contributed to a slowing in global gross domestic product (GDP) in 2019 compared to 2018. Through the first three months of 2020, the continued spread of the COVID-19 virus has resulted in swift responses by government and central banks across the globe.

Domestically, broad-based economic growth in 2019 supported Canada's unemployment rate near 40-year lows. In 2019, the economy grew at a slower pace than 2018 as global trade uncertainty held back business investment and exports. Elevated household debt continued to weigh on consumer spending. Despite these challenges domestically and in export markets, the overall economic climate remained favourable for the entire Canadian agri-food supply chain in 2019. Increased domestic concern over the rise of COVID-19 across Canada led to swift action by the federal and provincial governments to slow the spread, however the pandemic still resulted in increased unemployment and slowing domestic GDP in 2020. While the Canadian agri-food supply chain continues to function well overall, there have been shifts in consumer behaviours and increased costs.

Demand for agriculture commodities and food remains strong

The global economy grew at an estimated pace of 2.9% in 2019. Growth in emerging markets continued to outpace economic expansion of advanced economies. This has significant implications for the global demand for food and agricultural commodities, which has remained strong. Higher incomes in emerging market economies have raised the demand for animal-based proteins and processed food products as consumers allocate their additional income to food spending. Stronger disposable income in advanced economies has supported demand for restaurant meals and prepared foods. Widespread social distancing and self-isolation has resulted in a sudden shift in consumer behaviours in 2020. As a result, more people are working from home and shifting food consumption away from restaurants.

The U.S.-China trade tension has altered trade flows in agriculture and agri-food markets, leading to overall lower commodity prices for Canadian producers in 2019. Canada-China trade relations are also facing difficulties, with China restricting market access for a few Canadian agricultural products.

The United States remains Canada's largest export market, accounting for about 30% of our agriculture exports and more than 70% of our food and beverage manufacturing exports. Strong economic growth in the U.S. pushed the unemployment rate down to 3.6% in 2019, nearly a 50-year low, supporting increased demand for value-added foods. The Federal Reserve lowered its key interest rate three times in 2019 to 1.75% as lower global growth, trade uncertainty and geopolitical tensions created headwinds for the U.S. economy. To help support the U.S. economy from the impacts of COVID-19, the Federal Reserve lowered its key interest rates twice in early 2020 to 0.25%. Strong economic performance continued to support a strong U.S. currency, negatively impacting U.S. competitiveness in international markets and resulting in continued weakness in U.S. farm income in 2019. The strong U.S. dollar continued to give Canadian agriculture and agri-food exports a competitive advantage relative to U.S. products.

Trade agreements create future opportunities

Canada, Mexico and the United States completed negotiations to update the North American Free-Trade Agreement and the deal was ratified by all three countries. The resulting Canada-U.S.-Mexico Agreement (CUSMA) will maintain market access for the Canadian agribusiness, agriculture and agri-food supply chain. CUSMA will also expand access to foreign products in the Canadian dairy and poultry markets.

Canadian dollar supports farm income

The Canadian economy grew at an estimated annual rate of 1.6% in 2019, operating near capacity as the unemployment rate ended 2019 at 5.6%, the lowest rate in 40 years. With the economy operating near capacity, the Bank of Canada left its key interest rate unchanged throughout the majority of 2019, supporting historically low borrowing costs and encouraging producers and agribusiness and agri-food operators to leverage growth opportunities and make investments. On March 4, 2020, the Bank of Canada lowered its rate of 1.75% by 50 basis points to 1.25% due to the global impacts of the COVID-19 virus. In response to those impacts as well as a sharp drop in the price of oil, the Bank of Canada cut its overnight rate target on March 16 by another half a percentage point to 0.75%. On March 27, the Bank of Canada lowered its rate 50 basis points for a third time to 0.25%. The central bank indicated the unscheduled rate decision was due to the pandemic and its impact on the economy, adding that lower oil prices, even since the scheduled rate decision in early March, would continue to weigh on the economy. It is anticipated that the first quarter of 2020 will be weaker than expected and the Bank of Canada will closely monitor economic and financial conditions and adjust monetary policy accordingly.

Weaker Canadian oil prices and global trade uncertainty supported a Canadian dollar slightly above US$0.75 in 2019, which remained favourable to support Canadian exports. Lower oil prices and increased market uncertainty caused the Canadian dollar to decline to around US$0.72 in March 2020. Overall, Canadian agriculture benefits from a low dollar as it supports farm revenues by lifting prices paid to Canadian producers and making Canadian products competitive in the world market. Although some input prices such as machinery and equipment have been driven higher, the weaker Canadian dollar supported profit margins for Canadian crop, livestock and food-processing sectors.

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