Industry Update

Canada Truck Transportation

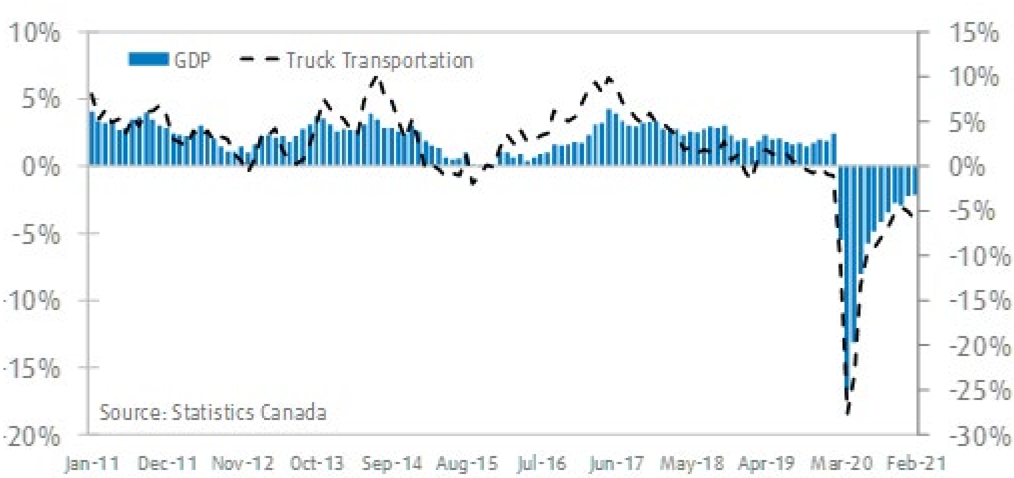
Key Developments

- **Transport Minister** Omar Alghabra is recommending that local jurisdictions follow a year-long progressive enforcement period for ELDs, offering penalty relief and "education and awareness" to carriers facing a June 12th deadline for the ELD mandate itself.
- Owing to differences in the availability of Covid vaccines, North Dakota is offering vaccines to Canadian truck drivers and other essential workers who cross the U.S. border from Manitoba and Saskatchewan. The **Ontario Trucking Association (OTA)** has called on officials to seek a similar arrangement with the state of Michigan.
- The **Alberta Motor Transport Association (AMTA)** announced a pilot program allowing semi-trucks fitted with close-proximity platooning technology that reduces drag and increases fuel efficiency.
- An Ontario MPP has introduced a motion to address **rising insurance costs** faced by owner-operators. The motion calls for the provincial government to review underwriting rules, risk classifications, driver training standards, fees, and requirements for fleets to provide drivers a letter of experience used by insurers when determining premiums.
- Be sure to check out the latest perspectives from BMO economists on the Canadian macro outlook (page 6).

Industry Fundamentals

With the emergence of a third wave of the pandemic and universal vaccine availability not expected until September, the macro recovery has been put on hold temporarily. That said, gradually improving vaccine availability coupled with recent mitigation measures appear to be working as the pace of new Covid cases has receded from a peak in April. On another positive note, the red-hot housing market, combined with the sustained uptrend in natural resource prices, offers a couple of much-needed pandemic-resistant freight tailwinds. Meanwhile, the remainder of the economy waits for easing restrictions before resuming the macro recovery, hopefully during the 2nd half of the year.

Canada Monthly GDP Y/Y Growth (Seasonally Adjusted)



Canadian real GDP rose 0.4% in February, just shy of the initial flash estimate, but in line with our estimate. Notably, the initial flash estimate for March points to a substantial 0.9% gain. The gain in February was led by robust retail activity (+4.5%) as various regions re-opened. Construction has also been on a tear led by the torrid housing market, with activity now up from a year ago in this highly cyclical sector. Nonetheless, overall GDP in February was still down 2.2% from the pre-pandemic peak it reached precisely a year earlier.

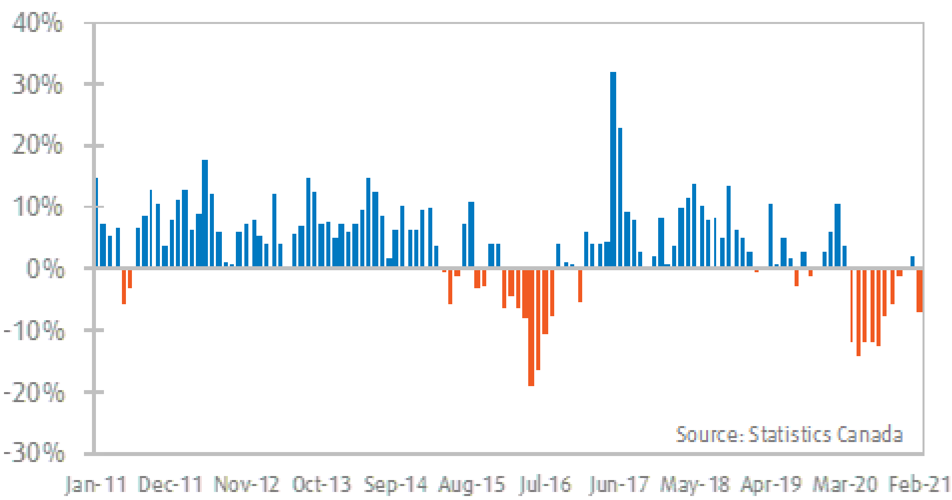
Similarly, while well off the bottom, **truck transportation** sector activity remains more than 6% below where it was a year earlier.

Trucking Business Influencers

Canada Weekly Diesel Fuel Retail Price (Cents/Liter)

Retail Diesel fuel prices across Canada have been on a steady uptrend and are now at a level last seen before the pandemic's onset. As of early May, the average weekly Diesel price of 125 cents/liter was up 16 cents (+15.0%) since the beginning of the year and up more than 40% since the bottom last year. That said, the current BMO outlook suggests that crude prices are nearing a peak and are likely to drift slowly lower as OPEC+ gradually lifts capacity constraints and new supply creeps into the market.

Canada Crude Oil Production Y/Y % Change



After reaching peak output in December and despite generally rising oil prices, **crude oil production** across Canada saw typical seasonal declines during both January and February. Further, data from Baker Hughes reflects recent shutdowns due to scheduled maintenance resulting in the number of active oil rigs declining from about 100 in February to only 22 at the beginning of May. As a result, forthcoming production data is likely to remain subdued throughout the spring.

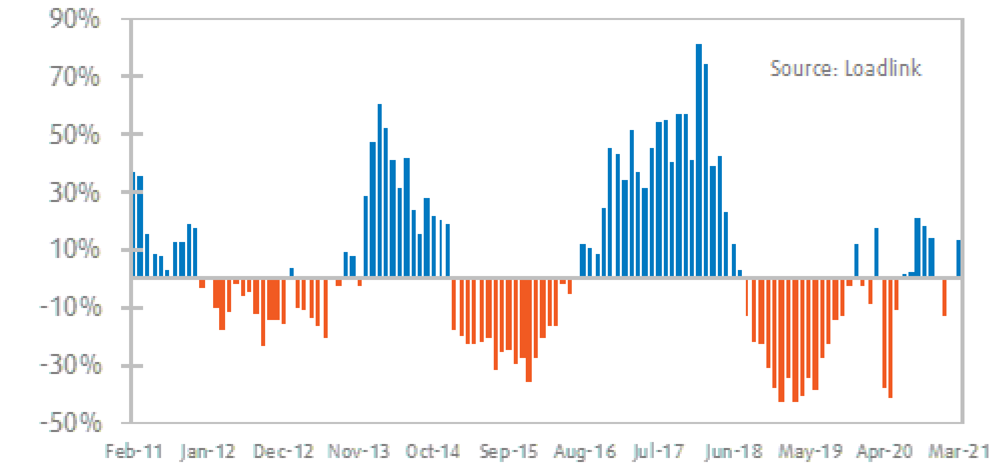
Longer-term, the big questions for crude oil production will be how the demand curve evolves, coupled with climate change policies and the trend towards fossil fuel divestments.

Interest Rates: 3 & 5 Year Interest Rate Swap Pricing

Interest rate swaps are derivative instruments commonly used by financial institutions to mitigate interest rate risk on a loan portfolio. The pricing of interest rate swaps (swap rates) mirror expectations of the future direction of interest rates. That said, the widening spread between the 3-year and 5-year has begun to reflect a bias toward higher rates further into the future as a typical response to a resumption of economic growth and likewise the possibility of increasing inflationary pressures.

Freight Indicators

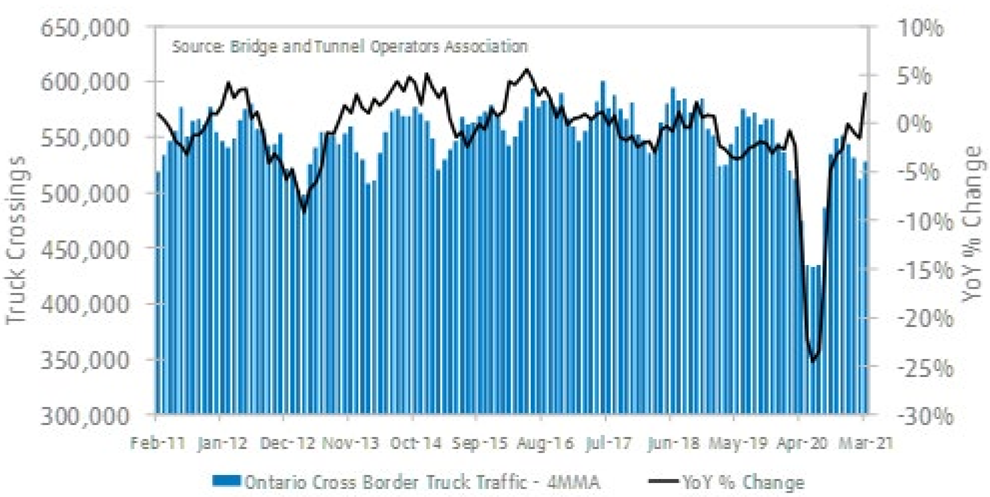
Canadian Truckload Spot Freight Volume Index Y/Y % Change



Despite an uptrend in Covid cases during March and April and a tightening of social restrictions, strong seasonal tailwinds helped boost spot freight volumes at the outset of 2021. As a result, truckload spot freight volume during March increased 33% from February and 13% over the previous year.

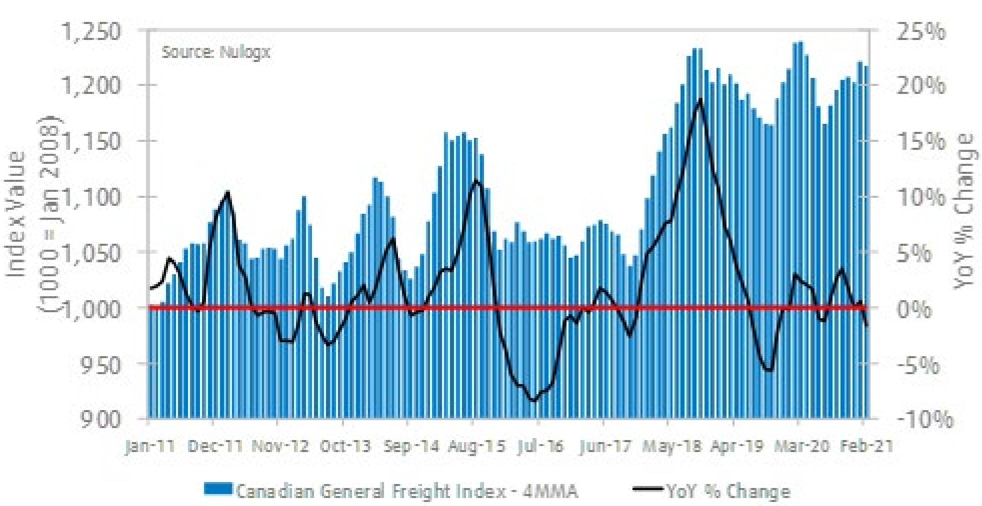
For the entire first quarter, **truckload spot freight volume** increased 14% compared to the fourth quarter of 2020 but only 1% compared to the year-ago first quarter. Given the strong recovery in freight since the middle of last year and despite a growing number of trucks in the market, spot market capacity continued to tighten in early 2021. The truck-to-load ratio of 2.27 during March contracted 13% from February and was 4% lower than a year earlier.

Ontario Cross Border Truck Traffic



Despite a third Covid wave and increased social restrictions across the country, **truck border crossings** have recovered to near-normal levels. Further, while the latest reading of the four-month moving average of crossings showed an uptick, the most recent surge in crossings during March was masked by weaker trends during the prior three months. In fact, following a nine-month low number of crossings during February, crossings during March rebounded to reach a 2 ½ year monthly high.

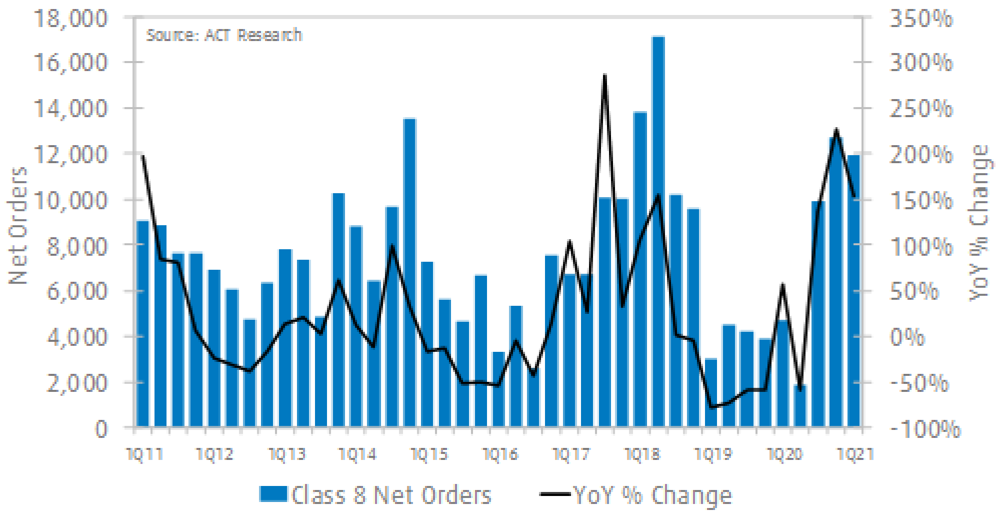
Canadian General Freight Pricing Index



An index representing the **total cost** (fuel surcharges + base rates) of over-the-road freight transportation for Canadian shippers has been at historically elevated levels since the beginning of 2018. Over much of that timespan, tight capacity has put significant upward pressure on base freight rates, which has more than offset downward pressure on fuel surcharges. That said, there has been a reversal in that trend since late last year as base rates have recently begun to level off while fuel surcharges have started to move higher. Nonetheless, the overall price level remained elevated through February, with the four-month moving average down less than 2% from an all-time high a year earlier and up nearly 5% from a more recent low last Summer.

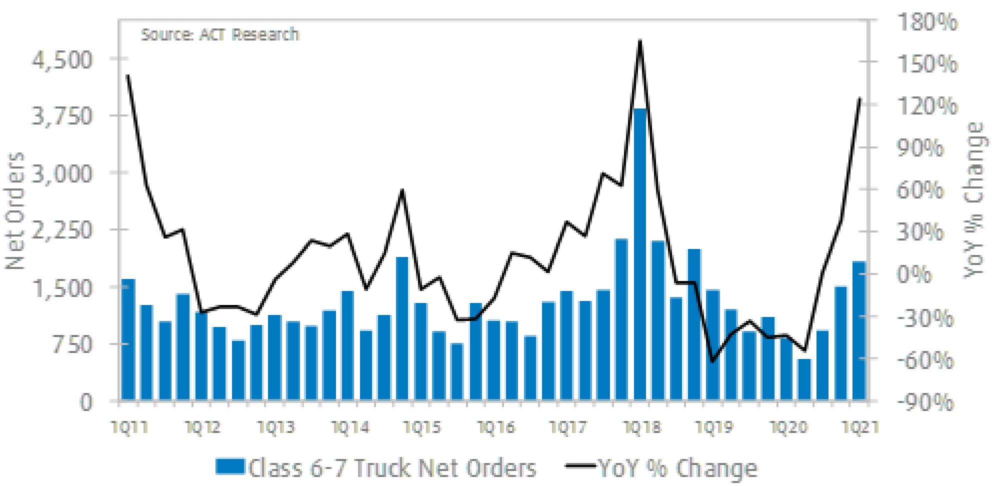
Truck Orders

Canada Class 8 Net Orders



Net new Class 8 orders during the 1st quarter of 2021 saw a typical albeit modest seasonal downtick. That said, orders were the 2nd most for any 1st quarter and the 5th most for any quarter over the past decade. What's more, the quarter finished with robust momentum as orders during March were the 4th highest total for any month since July 2018.

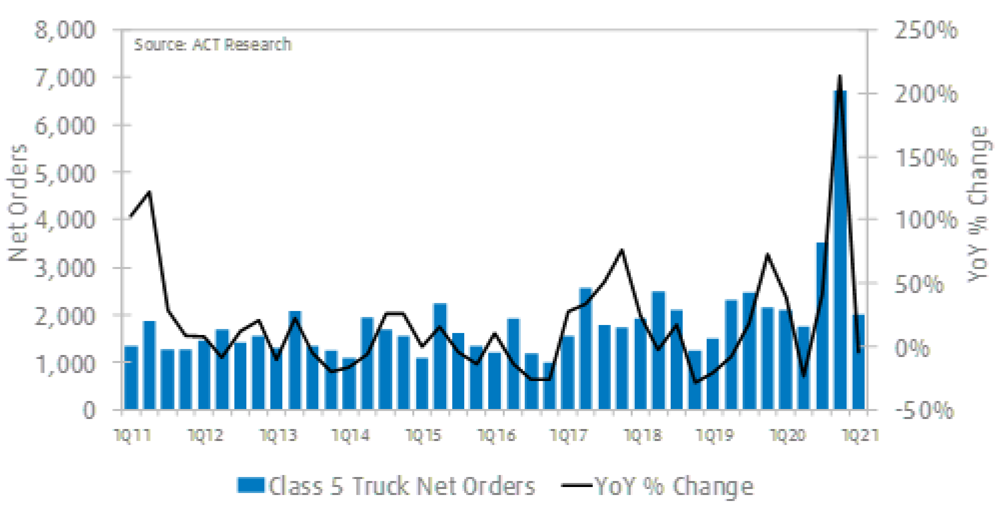
Canada Class 6-7 Truck Net Orders



Class 6-7 Truck Net Orders during the 1st quarter of 2021 continued to rebound from last year's lows. During the 1st quarter, class 6-7 net orders were up 22% from the 4th quarter and up 124% compared to the weak year-earlier 1st quarter.

That said, the upper end of the medium-duty segment continues to face longer-term headwinds, particularly in end-markets such as energy production. Additionally, the ongoing buildout of regional distribution centers and a trend toward shorter hauls favors smaller trucks featuring more fuel-efficient engines.

Canada Class 5 Truck Net Orders

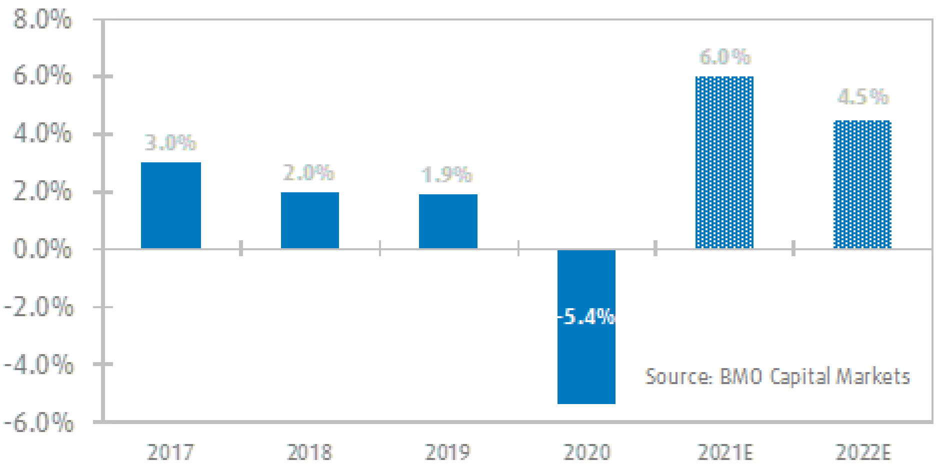


Despite a significant decline from the record 4th quarter, demand for **Class 5 trucks** continues to be firm with the usual support of diverse end-markets, consistency in vocational sectors, and a pandemic fueled tailwind for e-commerce and last-mile delivery.

Although 1st quarter orders declined 70% from the 4th quarter and 4% from the year-ago quarter, the intake was the 2nd best for any 1st quarter in more than a decade.

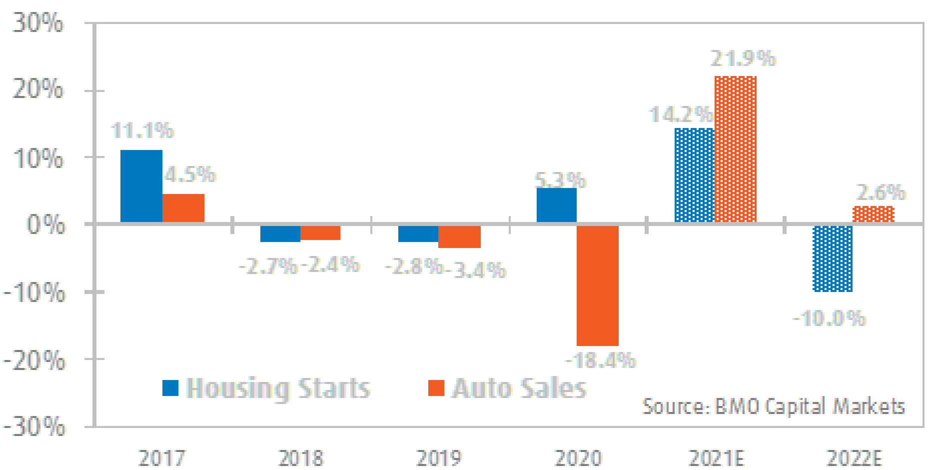
Macroeconomic Indicators

Canada Annual GDP Estimated Y/Y % Change



Despite the expansion of pandemic-related restrictions across the country, **Real GDP** looks to re-accelerate during the 2nd half of the year and still grow 6.0% for all of 2021. Underpinning the recovery will be expanding vaccinations, fiscal stimulus, strong demand for housing, a broad-based rebound in commodity prices, supportive financial conditions, pent-up demand for services, elevated household savings, and a recovering U.S. and global economy.

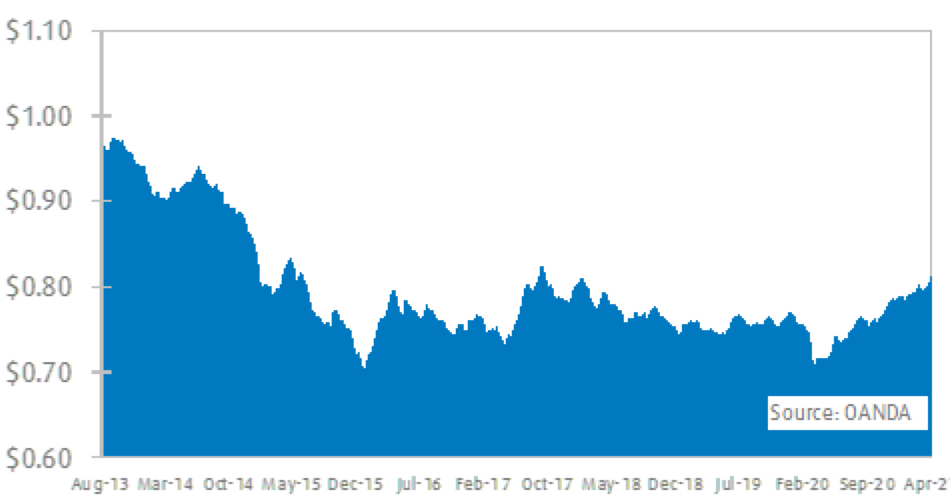
Canadian Annual Housing Starts and Auto Sales Estimated Y/Y % Change



Canadian housing starts jumped 21.6% to 335,200 annualized units in March. The gain was better than expected and marks the most active single month in modern history (or at least since the data began in 1990), aided by loosening restrictions and warmer weather. Both single- and multi-unit starts increased in the month. All told, starts were up 22% to an annualized rate of 296,174 in the first quarter of the year, with the six-month moving average jumping to 273,664 annualized units.

Despite challenges in the supply chain, pent-up demand and well-capitalized consumers are likely to support a strong rebound in the **auto sector** that could see unit sales return to 2019 levels.

U.S. Dollar per 1 Canadian Dollar



The Canadian dollar is the best-performing major currency so far this year, despite the U.S. dollar's firming trend through the first three months. Rising commodity prices (to record highs for Canada's non-energy prices), an improving balance of payments situation (best since 2008), along with the Bank of Canada's less dovish shift in guidance and QE have all supported the currency.

BMO economists expect the Canadian dollar's strengthening momentum to continue, particularly with the U.S. dollar likely back on a weakening trend, averaging C$1.20 (above US$0.83) by the end of this year and C$1.175 (above US$0.851) by the end of 2022.

"Voice of the BMO Economics Team"

With the pandemic yet to be fully resolved, we thought it would be helpful to share some refreshed thoughts from the BMO Economics Team on the near-term outlook for the Canadian economy. For more: https://economics.bmo.com/en/

North American Outlook: Separate Ways, For Now – Sal Guatieri, BMO Senior Economist

After showing surprising resilience to the second wave of the virus and new restrictions in the winter, Canada's economic growth is set to stall in the second quarter in response to aggressive new constraints to arrest a third wave of cases. Thankfully, the hearty rebound at the turn of the year has taken real GDP to within 1.3% of pre-pandemic levels, with the remainder expected to be sopped up by year-end. Based on Statistics Canada's strong flash estimate for March GDP (0.9% m/m), we have upped our Q1 growth call to 6.5% annualized. That's actually a little better than the U.S. rate, despite stricter restrictions in Canada and massive stimulus payments in the U.S., a testament to the economy's ability to partly adapt to the pandemic.

The same forces pushing the U.S. economy faster—massive fiscal stimulus, pent-up demand, hefty household savings—are set to drive Canadian GDP skyward in the second half of the year. The recent federal budget announced another $101 billion of new spending over three years, half of which will hit this year, amounting to 2% of GDP. Meantime, the housing boom south of the border (despite rivaling that of the 2006 bubble) is mild compared with Canada, where benchmark home prices rocketed 20% y/y in March and many rural areas are seeing gains of over 30% (and don't even talk about cottage country). Record sales have easily soaked up record listings. How much longer the buying frenzy will (or can) last is anyone's guess. Policy proposals to date (including, a tax on vacant property held by nonresidents and a higher qualifying rate on uninsured mortgages) will have only a modest impact. Eventually, eroding affordability should start clamping down on demand. We do not expect a pullback in house prices, but this assumes the market will cool to more sustainable rates soon; otherwise a correction would be inevitable. Barring a housing downturn or more pandemic trouble, Canada's GDP is expected to grow 6.0% in 2021 and 4.5% in 2022, a healthy rebound from last year's 5.4% contraction.

A fierce rally in commodity prices is also helping the economy, likely turning the Q1 current account into surplus for the first time since 2008. While oil prices appear to have steadied near pre-virus levels and close to long-term norms in real terms, that's not the case for most of the other key resources that Canada sells abroad. The Bank of Canada's ex-energy commodity price index has shot up nearly 30% in the past six months to all-time highs. This, along with a recent hawkish turn by the central bank, has pumped the Canadian dollar to more than three-year highs above 81 cents US (below C$1.23). The loonie is the top-performing currency this year (not counting the crypto kind). Resource prices are expected to ease moderately as more supply comes online and as consumer spending is diverted toward the service sector. Still, prices should remain supportive, and with the BoC likely to raise rates before the Fed, the loonie looks to have found a higher flight path. We see it cruising to 83.3 cents at year-end and to 85.1 cents (C$1.175) by late 2022.

The Bank of Canada recently announced it would start reducing the pace of government bond purchases to $3 billion per week from $4 billion. This wasn't a surprise, but attributing the taper solely to a sharply upgraded economic outlook was (as opposed to concern that the Bank already owns more than 40% of federal supply). The Bank now believes the economy's slack could be absorbed in the second half of 2022 rather than in 2023. Accordingly, we pulled forward the timing of rate liftoff by several months to early 2023. Like the Fed, the Bank is willing to tolerate some upward drift in inflation, as its 1%-to-3% target range affords some flexibility. We see the Bank's three core measures of inflation, currently averaging a tick below 2%, trending modestly higher next year. But, as in the U.S., the risks appear to be all on the upside.

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