

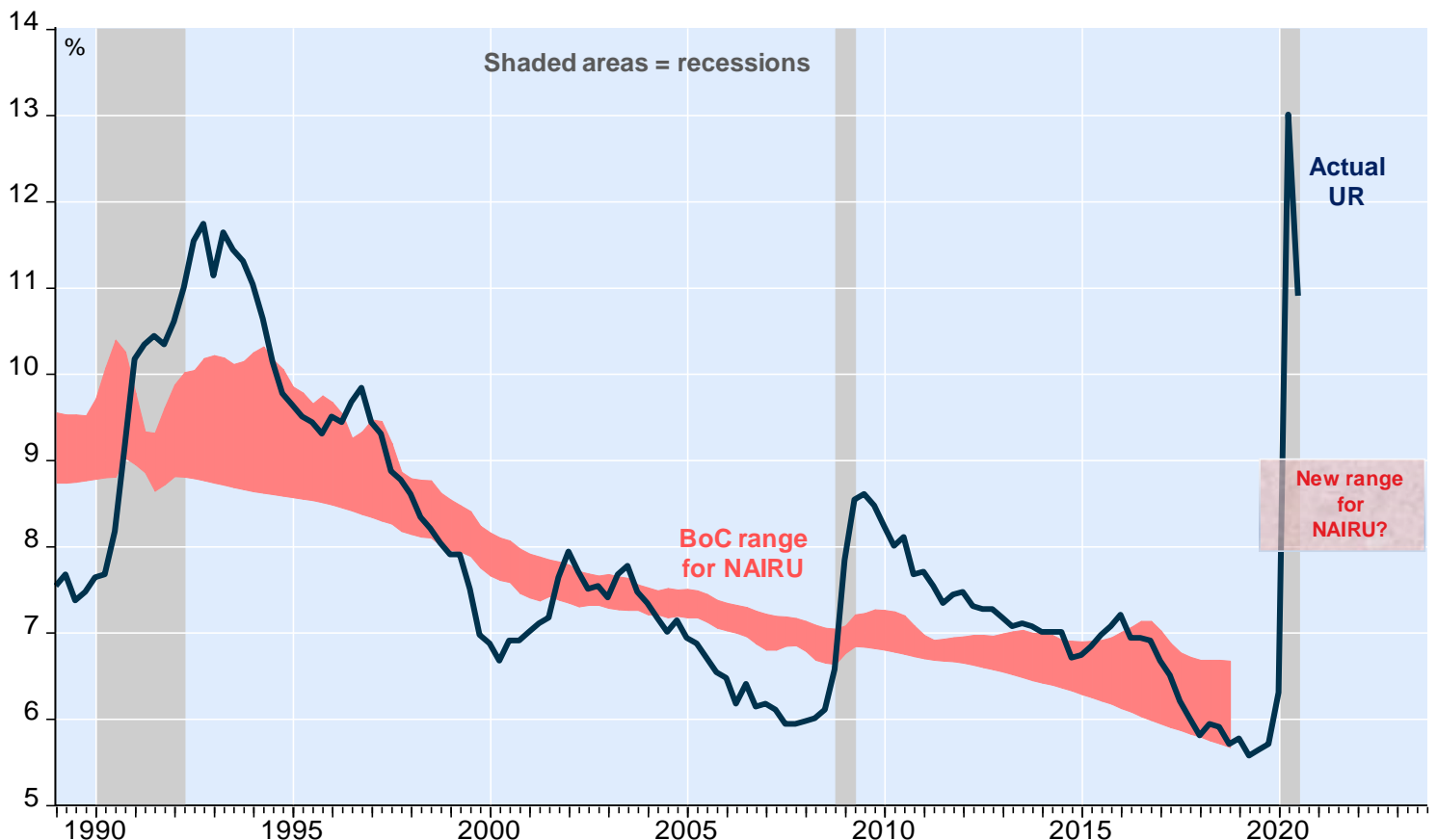
Canada Watch

By Stéfane Marion

This is a big week for central banks as they begin to publicly discuss their role in a post-pandemic environment that will most likely be characterized by unemployment rates that remain well above their pre-recession lows for an extended period. Here at NBF we assume a Canadian jobless rate that will average 8% in 2021. Most pundits would associate this level with an economic backdrop characterized by a large negative output gap and deflationary pressures. That is not our forecast. Recall that trend unemployment (NAIRU) tends to increase during recessions and we expect the rise to be particularly acute this time around. Unless an effective vaccine against the coronavirus is soon deployed, we believe that the new range for NAIRU could be as high as 8%-9%. Keep in mind that the industries hardest hit by the pandemic (retail trade, air transportation, food & accommodation and arts & entertainment) account for about a fifth of total employment. Some permanent destruction of capacity appears to be inevitable in these sectors, a situation Ottawa addressed last week by "temporarily" easing the qualification rules for employment insurance (EI) for all workers in every industry: work 120 hours and get at least 26 weeks of benefits. Labour market hysteresis risks becoming a medium-term fixture of the Canadian economy where a jobless rate of 8-9% is the new norm. If you think we are too pessimistic, we would refer you to the Bank of Canada's recently [published](#) range of estimates for the trend unemployment rate going back to the late 1980s. As today's Hot Chart shows, the NAIRU was in the 9-to-10% range through the late 1980s and the first half of the 1990s. That was until Ottawa made sweeping changes to the system in 1996 aimed at ensuring that workers develop significant attachment to the labour force before collecting EI benefits.

Canada: Back to the early 1990s for NAIRU?

Range for NAIRU vs. actual unemployment rate



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