Canadian economy’s resilience faded in H2/19
Recent data suggest the Canadian economy’s surprising resilience through much of 2019 began to fade late in the year. GDP fell 0.1% in October (the first decline since February), extending a streak of sub-trend gains with the economy having expanded a paltry 0.1% (non-annualized) since June. Goods production remained soft in October—posting its third decline in four months—while growth in the services sector stalled. Weakness in the latter was narrowly based and doesn’t look like the start of a trend. The goods sector is another story. Labour disruptions south of the border impacted Canada’s auto sector in October, and while we could see some rebound in the subsequent two months, the closure of GM’s Oshawa plant at the end of 2019 represents a permanent hit to motor vehicle production. A strike by rail workers in November disrupted trade and will have weighed on economic output in the month. All told, it looks like Canadian GDP growth slipped below 1% in Q4/19. To the extent that some of that slowdown reflects transitory factors, we expect activity will pick up modestly early this year. But we still anticipate sub-trend growth in the first half of 2020.

Labour market losing its lustre
After an ugly November employment report, Canada’s December jobs numbers caused a sigh of relief. The overall headcount retraced a good portion of the previous month’s decline, and more importantly, the unemployment rate fell back to 5.6%—just 0.2 percentage points above May’s 45-year low. If we’re being picky, wage growth slowed somewhat in December but a 3.6% year-over-year increase is still strong given inflation and productivity trends. While closing 2019 on a positive note, it’s still the case that Canada’s previously impressive labour market lost some momentum late in the year. That suggests that the economy’s shift to sub-trend growth in H2/19 can’t be solely blamed on transitory factors.

Ottawa has a bit less fiscal room than we thought
With a federal election in October, we had to wait until December for the now-minority Liberal government’s fall fiscal update. Its main policy change delivered on a key campaign pledge to reduce income taxes for nearly 20 million Canadians. Phased in over four years, the measure will lower a single individual’s tax bill by nearly $300 per year. With a federal election in October, Ottawa has a bit less fiscal room than we thought—owing to reducing debt as a share of GDP (now projected to edge up to 31% this year) the Liberals will have to prioritize some of their election promises. So while we continue to expect federal fiscal policy will be stimulative in 2020-21 (beyond the very modest boost from tax cuts that took effect in January), it might be less supportive than previously thought.

Governor Poloz doesn’t tip the BoC’s hand
In remarks early this year, BoC Governor Poloz was a bit more dovish than in December but still didn’t stray far from a balanced tone. While noting some improvement in global trade tensions “on the surface,” he said it remains to be seen whether investment and trade will improve with US trade policy remaining unpredictable. On the domestic economy, he mentioned a number of transitory factors that have weighed on growth recently but still described recent data as “mixed.” The BoC doesn’t appear to be in any rush to ease monetary policy (having held rates steady last year while others cut) and markets are pricing less than 50/50 odds of a move this year. But with growth numbers having disappointed recently—and as noted above, not entirely due to transitory factors—we continue to think the door is open to a rate cut by the middle of the year.

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