

Economics

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Canadian GDP (Jan & Feb adv): Defying gravity

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GDP (period/period % chg)	22:Q3 ¹	22:Q4 ¹	Nov	Dec	Jan	Jan Y/Y
GDP (at basic prices)	2.3	0.8	0.1	-0.1	0.5	2.2
• Goods-producing	3.0	-2.9	0.2	-0.7	0.4	2.0
• Services-producing	2.0	2.2	0.1	0.1	0.6	2.3
• Business	1.9	-0.1	0.1	-0.2	0.6	1.9
• Non-business	3.9	4.7	0.4	0.3	0.3	3.5

Source: Statistics Canada

- The Canadian economy continued to defy the gravitational pull of higher interest rates at the start of 2023, with monthly GDP data suggesting that the economy is on track for almost 3% annualized growth during Q1. That's a far cry from where consensus forecasts sat at the start of the year, and the numerous calls that a recession was imminent. However, barring a surge in restaurant sales during January, it appears that much of the growth we are seeing is being driven by the unwinding of previous supply disruptions, which is also helping to calm inflation. As such, the strength the economy to start 2023 shouldn't be particularly concerning for the Bank of Canada.
- The 0.5% gain in January GDP was a tick above the 0.4% expected by the consensus and a couple of ticks higher than the 0.3% advance estimate. Mining, oil & gas and transportation & warehousing saw big increases, although these reflected rebounds after unplanned maintenance and weather disrupted activity in the prior month. Accommodation & food services surged by 4%, although that could partly reflect difficulties in seasonally adjusting these data following the winter lockdowns of prior years. However, while part of January's strength reflected some sectors rebounding from December declines, growth was also encouragingly broad based across industries with 17 of 20 seeing increases. February's advance estimate surprisingly pointed to a 0.3% gain, despite some industry data recently suggesting a potential pullback. Mining, oil & gas and manufacturing were cited as drivers of that increase.
- The easing of previous supply constraints appears to be playing a role in driving growth during Q1. Manufacturing was a driver of growth in January and was cited as seeing a further advance in February, while wholesaling also saw its highest level of activity since last May in the January data. Strong growth in transportation & warehousing during the first month of the year wasn't driven by air transportation, where activity was flat and still well below pre-pandemic levels, but rather by a surge in rail transportation following weather delays in the prior month. The easing of previous supply disruptions can explain why we are seeing strong growth at the same time that we are also seeing inflation easing a little quicker than the Bank of Canada had previously anticipated.
- The stronger than expected growth we are seeing so far in 2023 should also be considered in the context of a surging population. With latest monthly data from the labour force survey suggesting that the Canadian working age population rose at a 2.1% annualized pace in the three months to February, GDP growth of just under 3% in Q1 wouldn't look overly strong in per capita terms, particularly following two quarterly declines in GDP per capita during the second half of last year.

¹ Annualized.

Implications & actions

Re: Economic forecast — The strong growth in January, plus surprise further advance in February, leaves GDP tracking almost 3% for Q1 as a whole, which is clearly well above the 0.5% expected by the Bank of Canada within its January MPR. However, the fact that inflation has also eased a little quicker than they previously thought suggests that much of the growth we are seeing is related to the unwinding of previous supply constraints, and as such the apparent strength in the economy to start 2023 may not be too concerning for policymakers. We still expect the impact of past interest rate hikes to show up in slower growth during the remainder of the year.

Re: Markets — Despite the upside surprise in today's data, bond yields and the Canadian dollar saw very little movement following the release, likely because investors know that the bar for the Bank of Canada to raise interest rates again is set very high amid the uncertain global backdrop.

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