Economy ‘firing on all cylinders’ as Canada sees best growth in six months

By David Parkinson
January 31, 2018 – *The Globe and Mail*

Canada’s economy posted its fastest growth in six months in November, as a surge in manufacturing led a broad-based rebound from October’s disappointing economic stall.

Statistics Canada reported that real gross domestic product rose 0.4 per cent month over month. That’s the biggest one-month increase since May, and a welcome improvement from October’s flat reading.

The gain matched economists’ consensus estimate, as earlier economic data, particularly in manufacturing and exports, had signalled a solid recovery from October’s weakness. Manufacturing output gained 1.8 per cent month over month, a three-year high, largely reflecting a rebound in the automotive sector, as two major auto plants returned from October shutdowns. Motor-vehicle manufacturing soared more than 14 per cent in the month, while auto parts were up nearly 9 per cent.

But November’s upturn wasn’t a one-sector story; 17 of 20 industries posted gains in the month, indicative of widespread strength. The goods-producing side of the economy surged 0.8 per cent, while service-producing sectors rose 0.3 per cent – for both, the strongest growth in months.

Economists said that after a relatively tepid third quarter (annualized growth of 1.7 per cent, less than half the pace of the first half of the year) and October’s weak start to the fourth quarter, the November figures are an encouraging sign that Canada’s broad-based economic recovery is on track.

“The Canadian economy fired on all cylinders in November: Production resumptions led the way, but nearly all major sectors reported gains on the month, an encouraging sign,” Toronto-Dominion Bank senior economist Brian DePratto said in a research note. “As shown by this month’s breadth of growth, the underlying trend for the Canadian economy remains a positive one.”

Other strong performers in the month included retail and wholesale trade, up 0.6 per cent and 0.5 per cent, respectively. The mining and oil-and-gas extraction segment also rose 0.5 per cent, recovering from a slump in October, partially reflecting the return of oil-sands production following maintenance downtime.

With some of the early indicators suggesting that December was also a reasonably solid month for the Canadian economy, economists now believe growth in the fourth quarter will probably come in at about 2 per cent annualized when the quarterly data are released about a month from now. That pace would undershoot the Bank of Canada’s most recent estimate of 2.5 per cent, released two weeks ago.

However, it’s also faster than the central bank believes the economy’s capacity is growing. Given that the Bank of Canada already believes the economy is running very close to its full production capacity, the fourth-quarter growth looks sufficient to further tighten an already tight economy – the justification behind the central bank’s interest-rate hike in mid-January.

“This report won’t change much from a policy perspective for the Bank [of Canada], which remains in cautious tightening mode,” said Bank of Montreal economist Benjamin Reitzes in a research note.

Still, some economists are concerned that the economy could be destined for more modest growth in the first half of 2018. In particular, higher interest rates and tighter mortgage regulations could slow the housing and consumer sectors, which have been major drivers of Canada's economic recovery.

"The early evidence points to a big drop off in [home] sales in January, reflecting that tightening of mortgage rules and the sharp increases in both variable and fixed mortgage rates," said Paul Ashworth, chief North American economist for London-based Capital Economics.

Economists are also concerned about how the uncertainty surrounding the future of the North American free-trade agreement, as well as the recent U.S. corporate tax cuts, might affect Canadian business investment – which was another key source of the economy's strength in 2017.

"To sustain further meaningful growth, we're going to need to see investment in export capacity – something we're not convinced is coming in the near term, given the increased attractiveness of the U.S. in light of recent tax cuts, and serious concerns on the trade front regarding NAFTA," said Canadian Imperial Bank of Commerce economist Nick Exarhos in a research report.