Canada's economic growth slows in fourth quarter, making rate hike unlikely

By Andy Blatchford
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Canada closed out 2018 with its weakest quarterly economic performance in two and a half years – and experts say signs of the growth slowdown is likely to spread into the early months of 2019 and possibly beyond.

Economic growth over the final three months of 2018 ground down to an annualized pace of just 0.4 per cent, Statistics Canada said Friday as it released its latest data on real gross domestic product.

The surprisingly feeble pace was Canada's slowest since the middle of 2016 and it came in lower than the two per cent growth in the previous quarter.

Through all of last year, the economy expanded 1.8 per cent, compared with the three per cent growth in 2017, the report said.

"I think we're seeing confirmation of a trend in terms of economic deceleration, but we're seeing it come through much more quickly," TD Bank senior economist Brian DePratto said in an interview.

DePratto and other analysts predicted Friday that more soft numbers are on the way because Alberta's oil production cuts at the start of the year will only be felt in the next quarterly data release.

"All this suggests, at our early read, we could have another quarter of effectively treading water – very, very little growth," he said.

The reading Friday was unexpectedly low – economists had expected growth at an annualized pace of 1.2 per cent for the final quarter of 2018, according to Thomson Reuters Eikon.

Statistics Canada said the late-2018 slowdown was mostly due to a 2.7 per cent contraction, on a quarter-over-quarter basis, in investment spending. Overall exports saw a slight decline and household spending slowed for a second straight quarter.

The agency also released downward revisions for the first half of 2018 that dropped the second-quarter reading to 2.6 per cent, from 2.9 per cent, and lowered the first-quarter number to 1.3 per cent, from 1.7 per cent.

"The 'R' word will be on minds as Canada's economy barely skirted the start of a recession in (the fourth quarter)," CIBC chief economist Avery Shenfeld wrote in a research note to clients.

"If not for a huge employment gain in January we'd be worried about an outright recession, but at this point, its best described as a stalled engine."

DePratto said stripping out the numbers around trade and inventories – both of which he argued aren't necessarily pure indicators of the health of the economy – shows Canada has now had a year of growth deceleration and a second quarter of contraction.

"You've got to go back to early 2015 to see the last time you had that back-to-back contraction," he said.

"That's not exactly an encouraging parallel."

The Bank of Canada has been widely expected to leave its benchmark interest rate unchanged at its policy announcement next week.

Following the report Friday, there were doubts whether central bank governor Stephen Poloz will increase the rate again this year – or whether his next move will even be a hike.

"Accordingly, the Bank of Canada also looks to stay very quiet for very long-they will need

compelling evidence that growth is returning to an above-trend pace before even considering rate hikes, and that won't likely be the case until late this year, at the earliest," BMO chief economist Douglas Porter wrote in a research report.

The Statistics Canada report said the country's terms of trade – a comparison of the prices of exports versus the prices of imports – saw its biggest drop since early 2009. It fell 3.6 per cent in the fourth quarter, which was mostly due to a 34.3 per cent decline in crude exports.

The agency said lower export prices led to a one per cent decline in real gross national income, which represents the real purchasing power of income earned. It was the steepest drop since the first quarter of 2015.

On Friday, for the first time, the impacts of cannabis legalization were reflected in Statistics Canada's real GDP report. Canada legalized recreational pot in October.

Household spending on marijuana, at an annual rate, totalled $5.9 billion in the fourth quarter – with illegal pot accounting for $4.7 billion of the total and legal weed representing $1.2 billion.

"Cannabis accounted for 0.5 per cent of total household spending," the report said of the quarterly numbers. "And non-medical cannabis accounted for 11.2 per cent of spending on alcohol, tobacco and cannabis."

The weaker GDP growth for all of 2018 reflected a slowdown in most categories, including weaker results for household consumption, business investment and housing investment, which contracted 2.3 per cent. The agency said the drop in housing investment coincided with rising interest rates and stricter mortgage rules came into force.

In December, economic growth contracted 0.1 per cent for the second consecutive month and the third decline in four months.

Statistics Canada accidentally posted numbers from Friday's GDP report on its website at least 10 minutes before its official release time of 8:30 a.m. EST. Markets can trade on economic data, therefore the agency is tasked with ensuring everyone has access to new information at the same time.

Statistics Canada said it's looking into the cause of the unexpected early release, which is called a "technical issue."