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Macro Market Insights

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Short Canada

Post-election, the bears are coming out of hibernation. It's in stark contrast from the story being told during the third quarter. As the rest of the world cut interest rates to adapt to a slowing global economy, the Bank of Canada was able to stand pat. In the discussion, points were raised about their ability to do so as interest rates were at an already accommodative level. Moreover, as the Canadian central bank's policy rate has typically closely followed the US Federal Reserve, the resounding question was if they won't cut rates now, then when? To some, it seemed clear they were just buying time.

Consensus forecasts are for the Bank of Canada to lower interest rates in the beginning of next year. In terms of a softening Canadian economy, recent data could certainly support this action, but also to the contrary, third quarter GDP data from Statistics Canada justifies this Goldilocks's economy (not too hot, not too cold).

There were two standout areas of concern as Canadian exports have edged lower over the past year, apart from the anomalous double-digit print in the second quarter. Household consumption growth is minimal and business investment had been lackluster, but it too saw a revival in the most recent three-month thanks to a revitalized residential housing market. What we're witnessing is mixed economic data with a downward bias.

Canadian employment data is also flashing signs of caution. Into the election, the strong results of Statistics Canada's Labour Force Survey were refuted by notable Bay Street economists. The issues raised were over both job quality and concentration in the public sector. The time-lagging Survey of Employment, Payroll, and Hours highlights a diverging trend in the oft volatile Labour Force Survey, which tends to steal headlines. In the latter survey, job losses were reported in retail and construction in September. It takes us full circle to what was the standout areas in the Canadian economy that now may be nearing an inflection point.

It raises the question to whether the burst of hiring and spending from Canadian businesses is sustainable in a lackluster economy. As we suggested in past newsletters, Canadian businesses will be hard pressed to escape the global headwinds of deglobalization from trade tensions and geopolitical unrest.

This was reinforced by notable comments this week from the CEO of Quebec's Pension fund, Michael Sabia. Sabia, who will be stepping down in February following a decade of near double digit returns under his leadership, suggests a fragmented global economy with different regions of influence. Also notable from Sabia's tenure was increasing the funds allocation to international markets, which is another key takeaway.

To what extent the prognostications of a fragmented global economy come true, the notion of a slowdown in Canada is coming to fruition. Since the inversion of Canadian and US government bond yields mid-Summer, investors have been on recession watch. Absent of a market shock, highly levered Canadian households will see continued moderation of consumer led growth. Calling or predicting the next downturn is its own challenge, but momentum is clearly slowing.