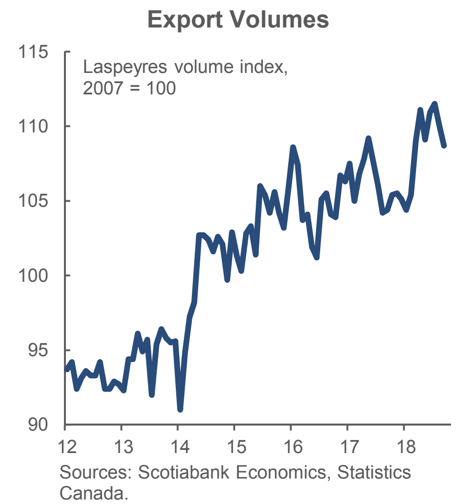
Look To The Trends In Canadian Trade

CONTACTS

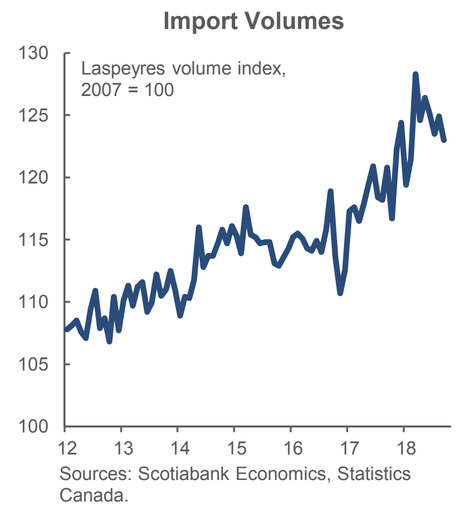
Derek Holt, VP & Head of Capital Markets Economics
416.863.7707
Scotiabank Economics
derek.holt@scotiabank.com

Canada, International Merchandise Trade balance (CAD billions), September:
Actual: -0.42
Scotia: 0.20
Consensus: 0.20
Prior: -0.55 (Revised from: +0.53)

- While the trade balance swung back into deficit and the prior month's surplus was revised away, I still don't think the trade figures will overly fuss the BoC. The core arguments that a) export gains in Q2 were unsustainable at the same clip into Q3 and b) that distortions derived from the energy and aircraft sectors are fouling up the near-term interpretations remain valid. Look through much of the third quarter's trade figures in favour of broad trends here.
- As a supporting point, note that export volumes were up 16.3% q/q SAAR in Q2 including today's revisions. They fell by only 1% q/q SAAR in Q3 and therefore retained most of the upside. The third quarter ended softly as export volumes fell 1.2% m/m and import volumes fell by 1.5% m/m. That requires sizeable gains in Q4 to offset the negative hand-off from the end of the third quarter. The magnitude of the jump in Q2 may continue to weigh upon H2 trade figures.
- Second, the export figures are distorted by transitory effects from Syncrude's shutdown. This will bounce back and the 2.3% m/m jump in energy exports in September was encouraging. There were also distortions on the energy imports side as they fell by 11.5% while maintenance work was being conducted at Canadian refineries.
- Third, import volumes were up 7.7% in Q2 and then fell by 4.9% in Q3. Much but not all of the surge has been unwound. Witness the trends in export and import volumes in the charts below.
- The BoC will look to the trend over time. Nobody looks at the spot figures that are based upon incomplete surveys and heavily subject to revision.
- In fact, even aside from their volatility, these figures change nothing about the argument that an economy at capacity with inflation on target and the real policy rate slightly negative should be moving toward a neutral policy rate. The December versus January timing of the next rate hike is likely more conditioned upon a) a broader suite of data, b) prospects for targeted fiscal stimulus on November 21st, c) prospects for a Canada-US steel/aluminum tariff agreement, d) NAFTA/USMCA implementation risks and d) ongoing Fed hikes and external policy developments. Volatile monthly trade figures don't much factor into that equation.
- Why did the trade surplus in September get swept away? Here's StatsCan's explanation:
    - "Owing to a large upward revision to imports for the August reference month, the trade balance originally reported as a $526 million trade surplus last month is now showing a $551 million deficit. Most of this revision was due to the import of three high value ships, which were reported after the publication of August data. Although late documentation of high-value transactions is common for trade data, the aggregate value these ships represent is infrequently received in late transactions."



Sources: Scotiabank Economics, Statistics Canada.



Sources: Scotiabank Economics, Statistics Canada.

- By export category, five of eleven sectors saw declines in September. The weakest categories were metal and non-metallic minerals (-8% m/m), consumer goods (-3.9%), and electronic equipment (-4.8%), industrial machinery and parts (-1.6%).
- By import category, the 0.4% m/m drop was backed by mostly driven by an 11.5% m/m decline in energy products and a 28% m/m decline in aircraft and other non-autos transportation equipment/parts.
- Note that imports of machinery and equipment have been rather strong this year. They surged by 18.5% q/q SAAR in Q2 over Q1 and then grew by another 16.8% in Q3 over Q2. The small decline at the end of Q3 puts early tracking of Q4 at -2.3% with two months of more data to go, but some moderation following such strong gains in imported capital equipment wouldn't surprise.