November 8, 2019

Why The Latest Canadian Jobs Report Is More Dovish For The BoC

- Job growth stalled…
- ….especially removing election effects, but there was no GM strike effect
- On its own, a small job loss shouldn't terribly fuss the Bank of Canada…
- ...as a soft patch against a torrid trend pace of job growth
- But the rub lies in the fact that wage growth is losing momentum…
- ...as month-ago SA wages point to the year-ago rate crashing back down
- Also, hours worked suggest the economy stalled in 2019Q3 & Q4…
- ...which stalls progress in closing spare capacity…
- …as a risk to the durability of meeting its inflation target
- Overall, cooling wages and GDP would merit concern beyond headline jobs

Canada, net change in employment SA (mm 000s) / UR (%), October:
Actual: -1.8 / 5.5
Scotia: 15 / 5.5
Consensus: 15 / 5.5
Prior: 53.7 / 5.5

The broad picture provided in this report is slightly more dovish by way of implications to the Bank of Canada. I would flag evidence of waning wage growth despite the year-ago rate's signals as the main reason (see below). Also, hours worked bode poorly for GDP growth (see below). Distant to these observations is the fact that jobs were weaker than the headline number suggests, but on that, one shouldn't over react to just a single report. An election effect was a more modest driver of the headline that masked underlying weakness, while the GM strike did not carry any effect whatsoever.

Public administration jobs were up 20k and some fraction of that, maybe all, would have been election oriented. Chart 1 shows the change in public administration in months containing past elections. It all depends upon when the election occurred in relation to the reference week. This year's election was just after the election week and so only advance polls may have influenced hiring.

My assumption explained in the Global Week Ahead had been that there would be a more muted election effect of +15k than past elections and also underlying flatness in employment ex-public administration. The underlying ex-public component was weaker than that assumption but the election component was in the ballpark. Strip out all of the public admin component and **underlying job growth ex-election was down as much as 22k.** That's the weakest jobs number since July, but hardly the end of the world after a torrid pace of gains over the prior two months.

Is wage inflation coming to an end? Yes LFS average hourly wages showed an up-tick to 4.4% y/y growth, but continued base effects from prior momentum are driving much of this. A three month moving average of the m/m SA % change is down to 0.5% now. The peak by that measure was 9.2% and that was back in

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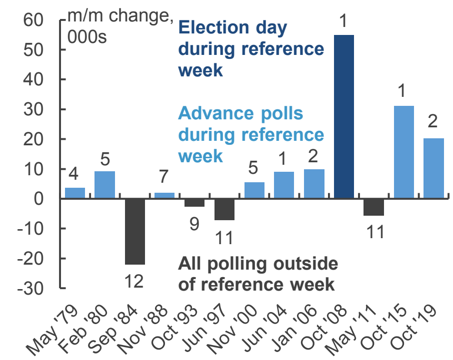
Changes in Public Admin Employment During Federal Election Month



Note: Labels above bars are the rank within that year from largest gain decending to largest loss.
Sources: Scotiabank Economics, StatsCan.

Canadian Wage Growth

Sources: Scotiabank Economics, Statistics

July. Chart 2 shows this point in that the three month moving average of the month-ago wage growth rate in seasonally adjusted terms has been pushing lower and by nature of the math leads the year-ago rate. It is important to look at evidence at the margin versus relying on the year-ago wage growth rate that takes an eternity for the momentum to turn as new data rolls in. What this says is that if the month-ago trend momentum continues to be cool, then year-ago wage growth should come right back down into 2020.

I don't think the BoC would be fooled by the year-ago rate. Quoting it now risks facing an embarrassing flip into 2020 if wage growth turns out to be unsustainable. This measure is also not in sync with other wage measures and the BoC doesn't even really pay attention to this metric anyway. It gets a trivial weighting in wage common, their preferred wage composite that pulls on four sources. The correlation in direction, however, combined with evidence of a turn at the margin in LFS wages may suggest that the same holds true for wage common. ie: their preferred measure may also cool into 2020.

Hours worked are tracking very softly in a GDP impact sense. After a 3.4% q/q annualized surge in Q2, hours worked were flat (+0.2% SAAR) in Q3 and up only 0.6% so far in Q4 at the same seasonally adjusted and annualized rate rate (SAAR). That leans toward potential downside risk to the BoC's 1.3% GDP growth forecast for each of Q3 and Q4. That's because GDP is an identity that takes hours worked times labour productivity. **We'd need strong productivity numbers observed through activity readings in order to leverage up soft hours worked and drive GDP growth to be stronger than what is being guided by hours worked.** We figure this leveraging effect is likely to be soft.

As for monthly GDP, hours worked were up only 0.1% m/m after a 0.3% drop in Sept and a 0.7% rise in August that followed a 0.7% drop in July.

By sector, **goods employment fell by 41k.** That was because construction was down 21k, manufacturing fell 23k, and each of utilities, ag and natural resources were all flat.

There was no GM auto strike distortion to the manufacturing jobs drop in case one is wondering. There are two reasons for this; one is conceptual and related to survey design; the other is factual and related to where the manufacturing loss occurred.

- Conceptually, Canada's Labour Force Survey does not treat strikes the same way as the nonfarm payrolls report in the US. Therefore this gives reason to ignore the strike effect before even turning to the data. LFS relies on the respondent's perceived employment status. If the individual thinks they will go back to work after the strike and is just temporarily sidelined, they will count as employed. It is not like nonfarm payrolls in the US that remove striking workers from the headline job change.
- Factually, the job losses in Ontario's manufacturing sector were not in autos and also not in auto-oriented areas like Windsor/ Sarnia. StatsCan guided that the manufacturing jobs lost in Ontario were in food, rubber/plastics, and medical equipment but there was no decline in autos.

Services employment was up 39k but strip out 20k for public administration. Finance/insurance heaped on 18k but all other sectors were flat except for 'other' services that fell 18k. So overall, **services hiring only pushed higher because of finance/insurance and an election effect that should come right back out of the next batch of numbers.**

Payroll jobs were up 26k because public sector hiring was up 29k but **private sector payrolls fell for the second straight month** after a 94k surge in August.

Self-employed jobs unwound the prior month's 42k jump and fell 28k.

Full-time jobs fell by 16k but after a 70k gain in September and 94k in total over the months of August and September. **Part-time jobs were up 14k** which reversed the 16k drop the prior month. These figures are also distorted by election effects.

The age breakdown is another quality dent. youths 15-24 got about 6k more jobs but both men and women over 25 lost jobs.

By province, Quebec's 9,500 drop may not sit well after a glowing Fall statement that lauded economic strengths, but the province is still up by 111k jobs on a year-ago basis. Ditto for Ontario that lost 16k jobs last month. In fact, only BC (+15k) and Alberta (+8k) registered notable gains.

On the BoC, I think they would need more than one shaky jobs report after the pair of torrid gains and the trend since mid -2016 to ring alarms. This jobs tally is incrementally more cautious, but we need more data and more clarity on various forms of global event risk. **That said, returning to the opening comments, the concern is what the report's underlying components indicate by way of the likelihood that wage growth comes right back down in year-ago terms into 2020 while GDP growth rests upon weak foundations in hours worked as an important indicator of output gains.**