

Canada's Economy Outperformed 'Flash' Estimates — Again!

- The economy shrank materially less than early guidance
- Growth is broadly tracking the BoC's revised April forecast...
- ...but vaccinations are occurring a lot faster than they assumed
- StatsCan's 'flash' guidance has a persistent negative bias
- Markets ignored the release with an eye on Q3

CDN GDP, m/m %, SA, April with May flash:

Actual: -0.3

Scotia: -0.8

Consensus: -0.8

Prior: 1.3% (revised up from +1.1)

May 'flash': -0.3

That's it? That's your best punch, third wave?? Hmph. While the human toll and the strain on health systems and some sectors are pronounced and real, the impact of the third wave on the broad economy is so far looking rather slight as the economy transitions toward rebounding over in a two-dose kind of summer.

April GDP fell by considerably less than the preliminary 'flash' guidance from Statistics Canada. On June 1st, the agency said April GDP was tracking a decline of 0.8% m/m and today they revised that to -0.3% for a notable half point upward revision. Less is not always more it seems as CAD couldn't have cared less about the backward looking estimates.

The flash guidance is appreciated, but not terribly accurate even with all of the internal data that the agency has at its disposal and that we don't. As chart 1 demonstrates, **actual GDP growth as we presently understand it net of all revisions to date has exceeded preliminary flash guidance in 10 out of the 14 months** that it has been provided during the pandemic and with only one notable overshoot back in April of last year. Despite internal data advantages, StatsCan keeps surprising itself and it might be helpful to hear an explanation for a fairly persistent positive bias to the surprises. One might expect some mean reversion that cancels out the overshoots and undershoots and not exceeding advance estimates 70–80% of the time.

With that rather large caveat, May's 'flash' guidance is for another 0.3% m/m decline which probably means the economy was flat or may have even posted growth. If not for the positive upward revision to April's estimated growth, then May would have posted positive GDP growth. Also note that March GDP growth was revised up to 1.3% m/m from 1.1%.

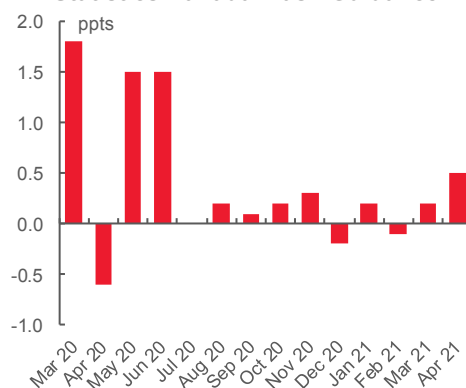
Monthly Canadian GDP is tracking 1.5% below Feb 2020 up to May of this year (chart 2). It's likely that Q3 will see GDP return to the pre-pandemic level. With less supply side expansion, we're on track to see spare capacity shut into early 2022.

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Chart 1

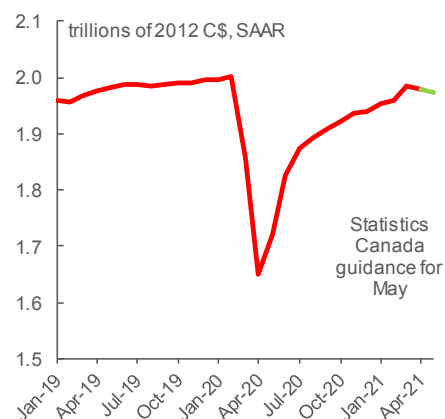
Spread Between Actual Real GDP and Statistics Canada Flash Guidance



Sources: Scotiabank Economics, Statistics Canada.

Chart 2

Canadian Industry GDP



Sources: Scotiabank Economics, Statistics Canada.

So what kind of growth is Canada tracking? How does that compare to the Bank of Canada's projection?

One approach is to use today's monthly production-based GDP figures that indicate Q2 growth tracking 1.9% q/q annualized (chart 3). That assumes flat GDP in June only to focus upon the effects of what we know so far and without imposing artificial judgement toward June GDP when we don't have any actual data for the month. If June shows preliminary evidence of positive reopening effects, then this estimate could push higher.

The more common approach to tracking growth is to use expenditure-based quarterly figures. Scotia's Nikita Perevalov runs a 'nowcast' model that tracks this concept and he gets 3.5% for Q2. That would be in line with the BoC's Q2 forecast from the April MPR which is based on this expenditure-based GDP concept. Q2 tracking will obviously be further informed as June data rolls in with potential revisions to prior months. Between now and the July 14th BoC communications, however, there won't be much added information other than next Friday's jobs that I estimate at +175k for June.

Recall that two of the main differences between the two ways of tracking GDP growth that are both derived from the fact that quarterly GDP considers *how* higher output was achieved whereas monthly GDP does not. The 'how' part is informed by factors like inventory and import swings. Our tracking suggests that inventories fell at a slower pace in Q2 than in Q1 which in a GDP accounting sense means a positive contribution to Q2 GDP growth. Our tracking also leans toward a decline in imports which means less of a leakage effect from the economy during Q2 which means imports add a positive contribution to Q2 GDP growth.

In any event, the BoC is unlikely to care much whatsoever about Q2. It's water under the bridge and they generally knew at the time of publishing the April MPR forecasts that the economy was going into third wave lockdowns that were expected to begin easing in May which they did (and much more so over June into July).

Further, the April MPR had assumed that vaccinations would lead to herd immunity 'later in the year' after the US achieved this milestone around mid-2021. Canada might be at a 75% double dose level of herd immunity as soon as Macklem's press conference on July 14th. If not, then it's likely this milestone will be hit shortly thereafter.

As for what drove April GDP, chart 4 shows that it was dragged lower by sectors you would expect to have suffered the most during the restrictions. Statistics Canada does not break down their preliminary guidance for May, but loosely indicated that weakness was focused upon retail trade, construction and real estate rental/leasing while finance and insurance and wholesale picked up.

Chart 5 shows cumulative GDP changes by sector since the start of the pandemic.

Chart 3

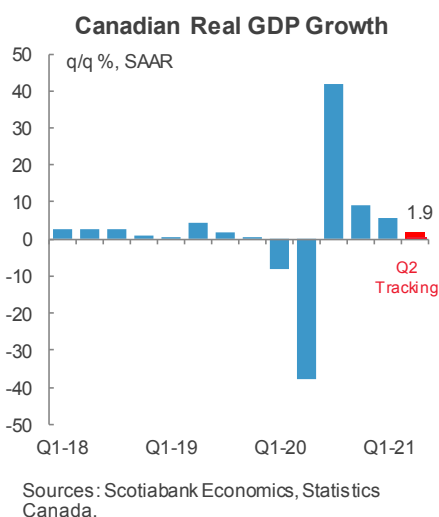
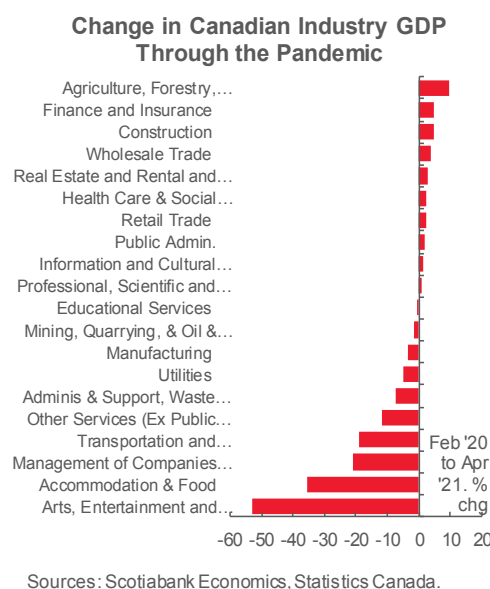


Chart 4



Chart 5



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