Scotiabank

GLOBAL ECONOMICS

SCOTIA FLASH

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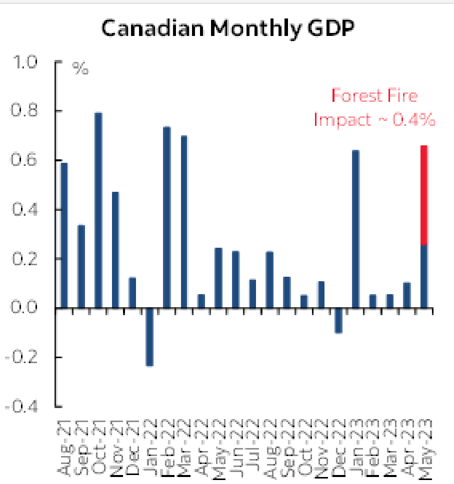
## Contributors

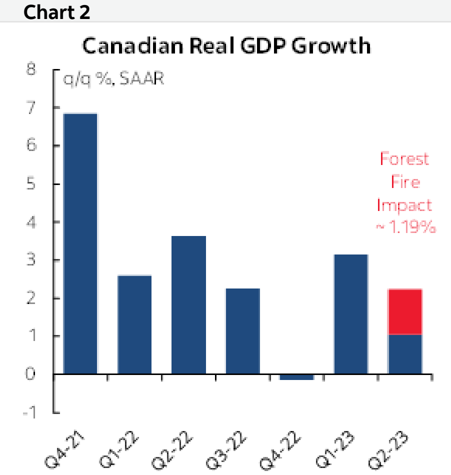

**Derek Holt**
VP & Head of Capital Markets Economics
Scotiabank Economics
416.863.7707
derek.holt@scotiabank.com


Chart 1




Sources: Scotiabank Economics, Statistics Canada.

Chart 2




Sources: Scotiabank Economics, Statistics Canada.

# Canada's Economy is Stronger Under the Hood

- **Canada's economy grew solidly in May, gave back some of it in June...**
- **...as wildfires took a toll...**
- **...such that underlying Q2 growth would have been double what occurred...**
- **...keeping the BoC focused on stronger underlying details with an ongoing hike bias**

**Canadian GDP m/m % May, SA:**
Actual: 0.3
Scotia: 0.4
Consensus: 0.3
Prior: 0.1
June guidance: -0.2

Canada's economy is considerably stronger than the latest GDP figures suggest. If not for the effects of various distortions, the economy may have been tracking double the growth rate in Q2 compared to the official statistics. That would preserve growth at a rate above potential GDP growth and continue to push the economy into excess demand conditions.

What are the Bank of Canada implications? It's challenging to control for serial shocks that are hitting the Canadian economy dating back to late last year and more recently including the Federal civil servants strike in April, wildfires over the past couple of months and then other disruptions such as the BC port strike. The BoC's job is to seek to control for these effects and craft monetary policy accordingly. In my view, such an exercise would be inclined to emphasize underlying resilience in the economy and to maintain a bias toward further tightening that will be informed by data.

In short, it would be pretty silly of the central bank to drop its hike bias because of transitory shocks like strikes and forest fires!

May GDP landed at 0.3% m/m and a tick beneath Statistics Canada's initial 'flash' reading for the month. Preliminary guidance for June indicates a contraction of -0.2% m/m.

May would have been even stronger it not for the effects of wildfires. They had a particularly disruptive effect upon the mining, oil and gas sector as multiple projects were impacted. That sector's output fell by 2.9% for the biggest drop since December when pipeline disruptions south of the border impacted the sector's output. In weighted terms, the hit to this sector knocked about 0.2 ppts off of m/m GDP growth.

Statcan had this to say about the effects:

> "Following four months of growth, the oil and gas extraction subsector fell 3.6% in May, as all components contributed to the decline. Oil and gas extraction (except oil sands) dropped 6.6% as a result of the forest fires in Alberta. The fires primarily impacted installations in the western parts of the province, from Edmonton to the Rocky Mountains' Foothills in the Clearwater, Montney and Duvernay formations. These played a crucial role in the industry's largest monthly contraction since April 2020, resulting in a steep drop in both natural gas extraction and crude oil. Oil sands extraction decreased 1.6% in May 2023, as maintenance at a number of facilities in Alberta throughout the month contributed to lower production."

There were also very likely indirect effects from the wildfires that are much harder to estimate. Travel and tourism could be one such candidate.

Running with a very rough estimate of what May GDP might have looked like in the absence of wildfires could very reasonably reveal a true underlying growth estimate of 0.5–0.6% and maybe higher. That would make for the hottest gain since at least January (chart 1).

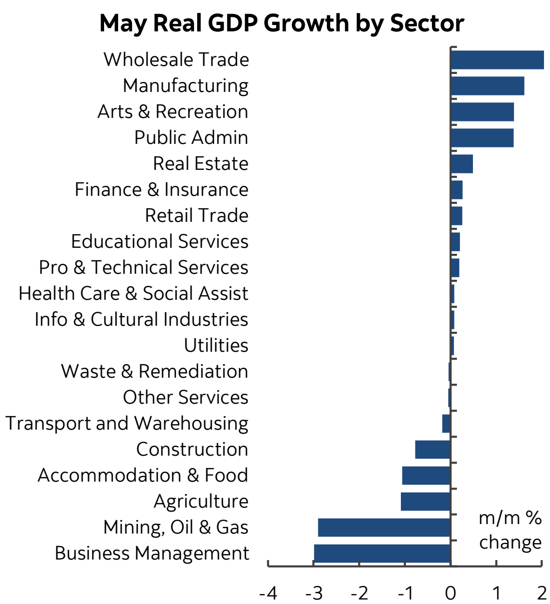
Furthermore, I don't trust Statcan's June GDP estimate of -0.2% m/m. Their energy surveys are lagging and not reliable at this stage and so any future impact of stabilizing output is likely to be underestimated.

Controlling for these effects has me thinking that Q2 GDP growth would instead be 2%+ q/q SAAR, or double the 1% tracking using the official figures (chart 2).

So, for what it's worth, charts 3 and 4 provide the breakdown of May GDP by sector and in terms of weighted contributions to overall GDP growth.

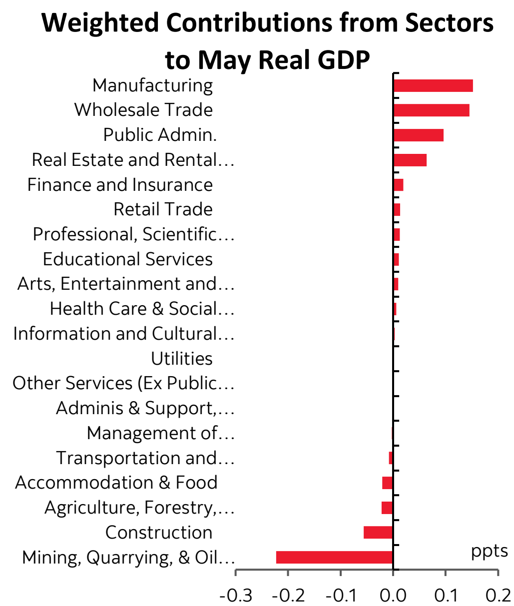
What's causing underlying resilient growth? I know what's not causing it as opposed to all of the consensus hype. In the Global Week Ahead that will be published later today, I will write about how it is a total myth that GDP and employment gains are being driven by a surge of immigration to Canada over 2022–23. The available facts do not support such a conclusion that too many are deriving from what is a spurious correlation between population growth and GDP growth over this period.

**Chart 3**



Sources: Scotiabank Economics, Statistics Canada.

**Chart 4**



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