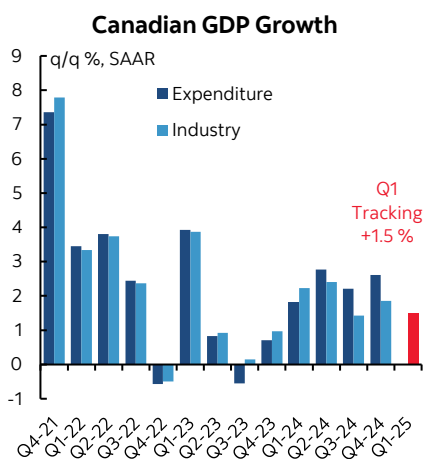


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Chart 1



Sources: Scotiabank Economics, Statistics Canada.

Small Comforts — The N.A. Economy Was Ok Before Trump's Tariff Wars

- Canada's economy ended an as-expected Q1 on a softening note...
- ...ahead of deepening downside risks driven by erratic US policy
- The US economy was stronger than GDP indicated for Q1...
- ...given solid growth net of wild tariff-driven import and inventories swings
- US core inflation was hot in Q1 but ended on a soft note ahead of tariffs
- N.A. GDP growth will quickly begin to weaken due to US government policies

Canadian GDP, m/m % SA, February:

Actual: -0.2

Scotia: -0.1

Consensus: 0.0

Prior: 0.4

March 'flash' guidance: +0.1

Canada's economy posted mild growth in Q1 alongside volatile monthly GDP figures that broadly met expectations. The focus is all forward-looking in terms of the risks and so I'll keep this relatively brief. There were small reactions in markets.

GDP fell -0.2% m/m in February which was weaker than consensus (0.0) and slightly weaker than my estimate (-0.1). My simple regression model was estimating -0.3%.

The preliminary 'flash' estimate for March GDP was +0.1% m/m which was also in line with my expectations but that was admittedly based on little information and subject to revision.

It all nets out to tracking Q1 GDP at 1.5% q/q SAAR which was in line with expectations that I wrote about in my weekly (chart 1). Ok, not great.

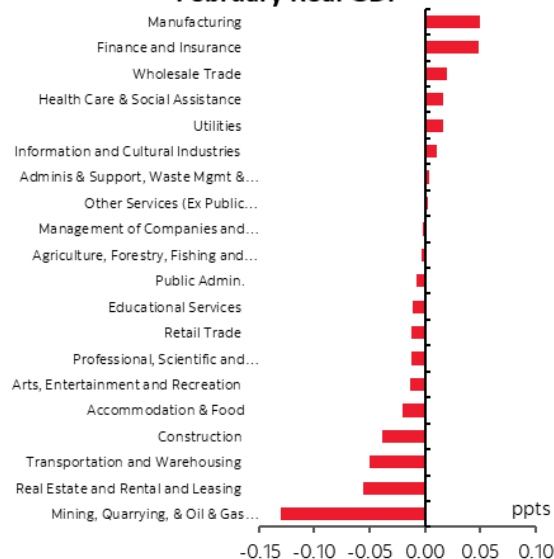
Chart 2 shows the weighted contributions to February GDP growth by sector. Growth was driven by manufacturing likely on front-running, finance and insurance, and with tiny contributions from a few others. The big drag on growth came from mining/oil/gas followed by smaller drags from other sectors.

As for March, recall that we don't get details, just the preliminary estimate of 0.1% with the verbal guidance as follows:

"Increases in mining, quarrying, and oil and gas extraction, retail trade and transportation and warehousing were partially offset by decreases in manufacturing and wholesale trade."

Chart 2

Weighted Contributions from Sectors to February Real GDP



Sources: Scotiabank Economics, Statistics Canada.

If we land around 1.5% for Q1 then that's in the spit zone for potential GDP which means Canada neither added to nor subtracted from a small amount of slack (ie: negative output gap). That gap hasn't worked so well in terms of explaining persistent underlying core inflation pressures that are dominated by other factors.

In any event, Q1 was probably the peak for Canadian GDP growth this year. Our forecast has less than 1% q/q annualized growth in every remaining quarter of 2025 and there is likely more downside than upside risk to that thanks to Trump's damaging policies against the US and global economies.

US Q1 GDP, q/q SAAR, %, Q1:

Actual: -0.3

Scotia: -1.1

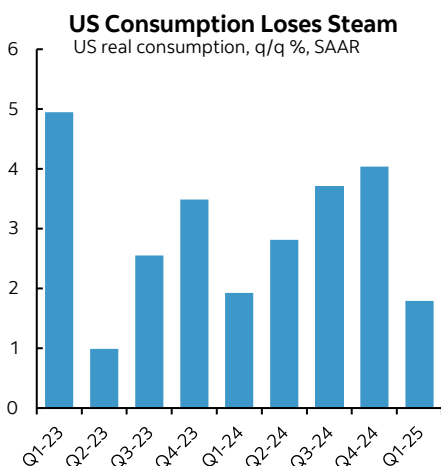
Consensus: -0.2

Prior: 2.4

Sometimes GDP isn't the greatest gauge of an economy's strength. This is one of those times as I'll explain.

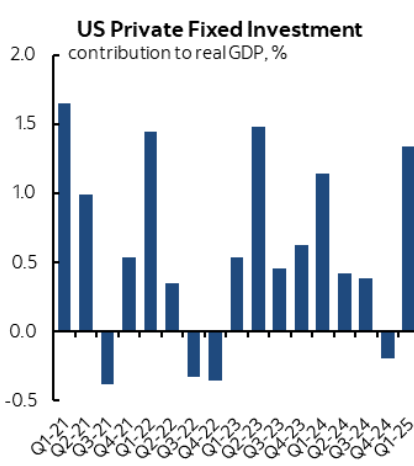
First, on the surface, it looks like the economy was weak as it contracted by -0.3% q/q at a seasonally adjusted and annualized rate (SAAR). That looks like consensus was right, but that's misleading since the median estimate masked the enormous range of estimates that were fairly evenly spread out from about -1% to +1%.

Chart 4



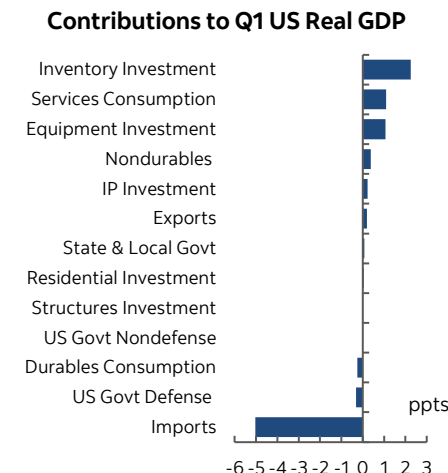
Sources: Scotiabank Economics, BEA.

Chart 5



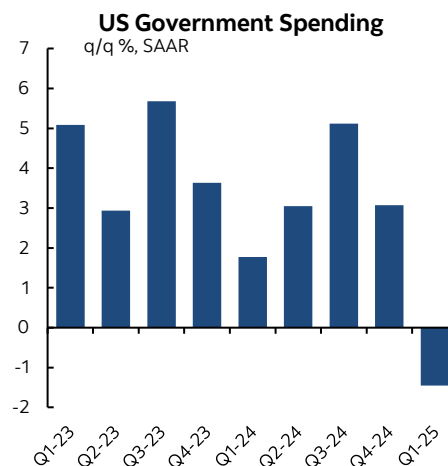
Sources: Scotiabank Economics, BEA.

Chart 3



Sources: Scotiabank Economics, BEA.

Chart 6



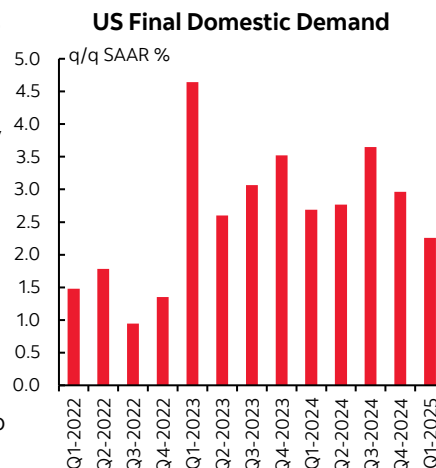
Sources: Scotiabank Economics, BEA.

US GDP was stronger than the headline appeared. That's revealed by chart 3 that breaks down the weighted contributions to GDP growth by component. Imports dragged a whopping 5 ppts off of the q/q SAAR headline growth estimate and that was due to tariff front running. Some of that showed up in inventory stocking as inventories contributed 2.25 ppts to Q1 US GDP growth. Simply put, US businesses ramped up imports and orders to give them some time to adjust to tariffs by having pre-tariff inventory on hand to meet demand.

Across other components, consumption slowed to 1.8% q/q SAAR (chart 4) and added 1.2% to GDP growth in weighted terms. Exports only added 0.2% in weighted contribution terms. Fixed Investment (ie: ex-inventories) added 1.3 ppts mostly through nonresidential investment and in turn mostly due to a 1.06 contribution from equipment purchases (chart 5). Government spending was a drag (chart 6).

Key, however, is final domestic demand. This measure for the US takes out trade and inventories to focus more directly upon the domestic economy. FDD grew by 2.3% q/q SAAR (chart 7). That continues a slowing pattern of late, but it's still respectable.

Chart 7



Sources: Scotiabank Economics, BLS.

Unfortunately, US growth is likely to begin cratering in short order. Our forecast expects sub 1% q/q SAAR GDP growth in each of the next five quarters with the economy fully stalling out toward the end of the year. If GDP rebounds next quarter then it's likely due to net swings in import and inventory contributions to growth as tariff front-running effects dissipate and give way to emptying store shelves. The trend outlook for the US economy is bleak imo.

The bigger surprise here was that core PCE inflation ripped, landing at 3.5% q/q SAAR which was higher than expectations that were in the low 3% range (chart 8). That was mainly because February core PCE was revised up from 0.37% m/m SA to 0.5%. March core PCE inflation came in a tick softer than consensus as shown in the monthly figures (chart 9).

The US Q1 Employment Cost Index was up 0.9% which was on the screws (chart 10).

Did US consumption growth peak in March (chart 11)? It might be strong again in April given indicators like industry guidance for a surge in auto sales this month on tariff front-running. Consumption is also buoyed by income gains (chart 12). The issue going forward is to what extent consumption weakens given a combination of a) falling confidence, b) potential job losses, and c) the dissipation of tariff front-running effects. We expect a sharp weakening for consumer spending over the course of 2025.

Chart 8

US Core PCE Inflation

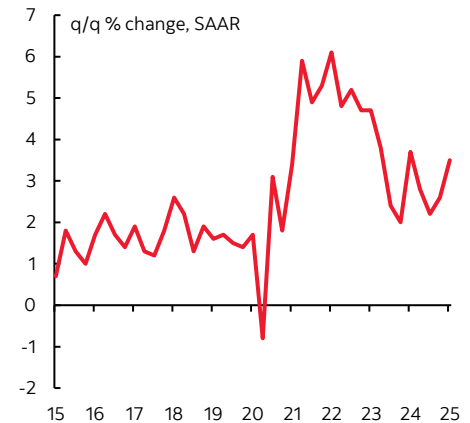


Chart 9

US Core PCE Inflation

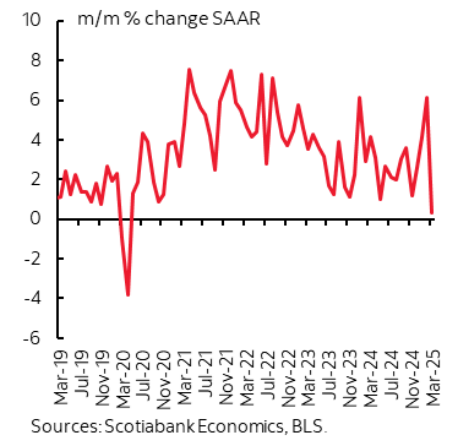


Chart 10

US Employment Costs

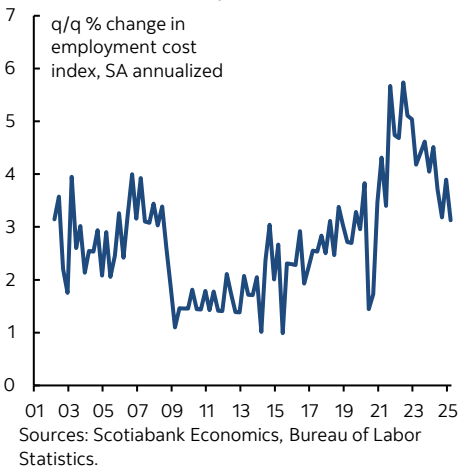


Chart 11

US Real Personal Consumption

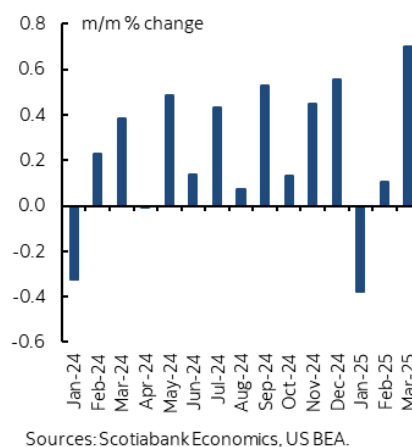
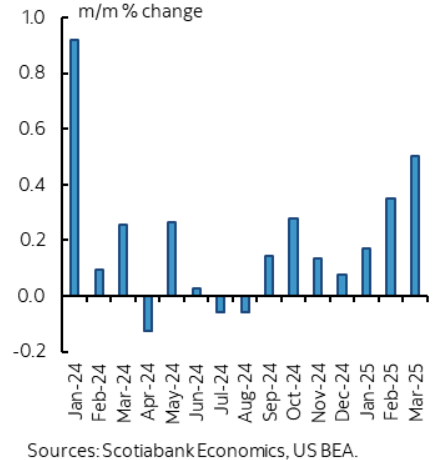


Chart 12

US Real Disposable Income



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