

February 29, 2024

Canada: Weakening in the private sector continues in the fourth quarter

By Matthieu Arseneau

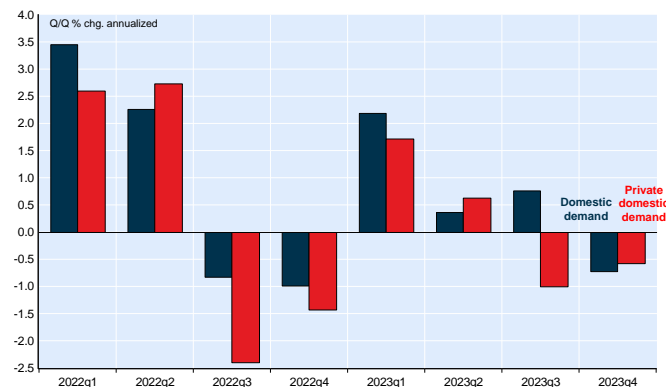
While growth was slightly stronger than expected, this does not mean that the Canadian economy is experiencing good times. The quarter was saved by the contribution of international trade, which benefited from a surge in exports. Domestic demand declined for the first time in four quarters, while the government was unable to come to the rescue this quarter. The negative impact of monetary policy becomes clearer when we look at private domestic demand, which contracted for the second quarter in a row and has fallen four times in six quarters, the period coinciding with the tightening of monetary policy (chart). Business investment fell sharply for the second consecutive quarter, as spending for both structure and machinery & equipment were again postponed. This illustrates that corporations are very cautious in the current context, which has allowed profits to recover, although they remain well below their peak in 2022. Efforts to restore profitability were also reflected in employee compensation, which rose at the slowest pace in more than three years in Q4. Consumers, for their part, continue to feel the financial squeeze in a high-interest-rate environment, with consumption rising just 1.0% in the quarter. Underwhelming economic performance is particularly telling when viewed against the current exceptional demographic backdrop. GDP per capita has fallen sharply since monetary tightening began, by 3.2% - a decline of a magnitude only seen in recession (right chart). What lies ahead is unlikely to be more enviable, as we estimate that 30% of the impact of previous rate hikes on consumption remains to be seen, given the lag in monetary policy transmission. In light of this morning's report, we continue to see a buildup of excess supply in the economy over the coming months, with a larger negative output gap. Under these circumstances, we still expect monetary easing to start in June.

HIGHLIGHTS:

- Statistics Canada released its GDP estimate for Q4 2023. The economy expanded at an annualized rate of 1.0%, slightly higher than consensus estimate calling for a 0.8% increase. The previous quarter's result, meanwhile, was revised up from -1.1% to -0.5%.
- Domestic demand was down in Q4 (-0.7%), as non-residential structures (-11.6%), investment in machinery & equipment (-5.7%), residential investments (-1.7%) and government consumption (-1.9%) posted pullbacks while household final consumption rose modestly (+1.0%). On the other hand, government investments posted a strong gain (+3.2%). Trade had a strong positive impact on GDP, with exports (+5.6%) bouncing back while imports retreated (-1.7%). Inventory investment was lower compared to Q3 resulting in a negative contribution of 0.5% to GDP.
- Nominal GDP grew a robust 6.6% on an annualized basis following a 6.5% increase in the third quarter of 2023. Also in nominal terms, disposable income jumped an annualized 5.3% following a 9.1% increase in Q3. Consumption, meanwhile, rose 4.7% annualized. As a result, the savings rate declined from 6.3% to 6.2%, remaining above its pre-pandemic level (2.8%).
- Industry data showed that output was flat in December, below consensus estimate calling for 0.2%. Goods were down 0.2% while services were flat. Statistics Canada also released an advance estimate for January showing an increase of 0.4% with the conclusion of the strikes in Quebec in December.
- See charts on next page for more details.

Canada: Private domestic demand contracted again in Q4

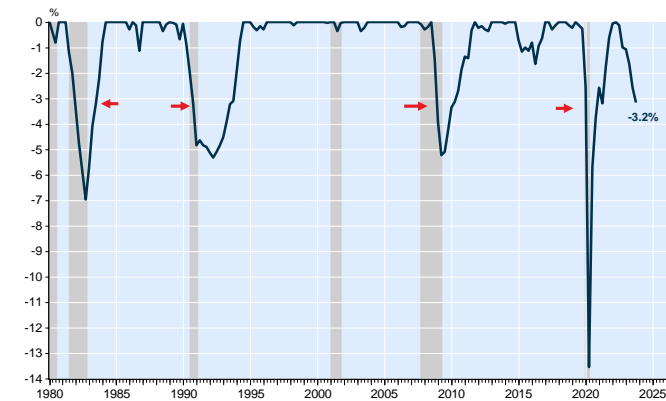
Final domestic demand and private final domestic demand



NBF Economics and Strategy (data via Statistics Canada)

GDP per capita has fallen sharply since monetary tightening began

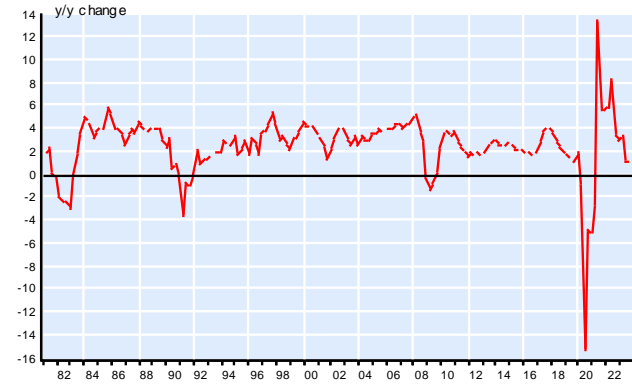
Change since peak in GDP per capita



NBF Economics and Strategy (data via Statistics Canada)

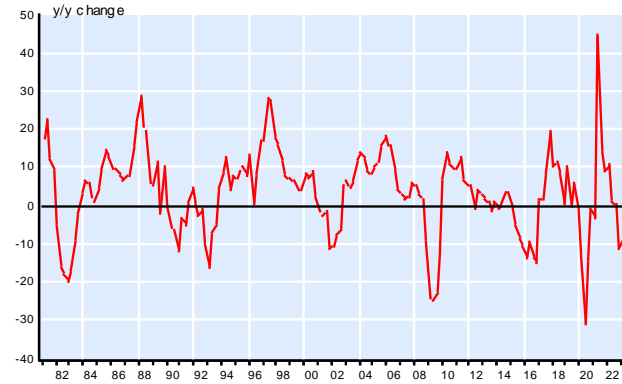
Consumption

Real consumer expenditures



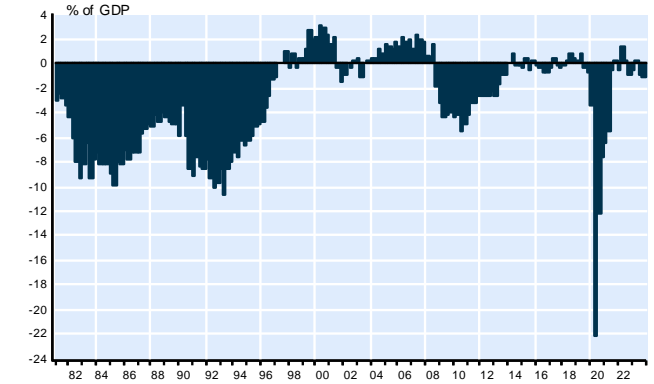
Business Investment

Real investment in machinery and equipment



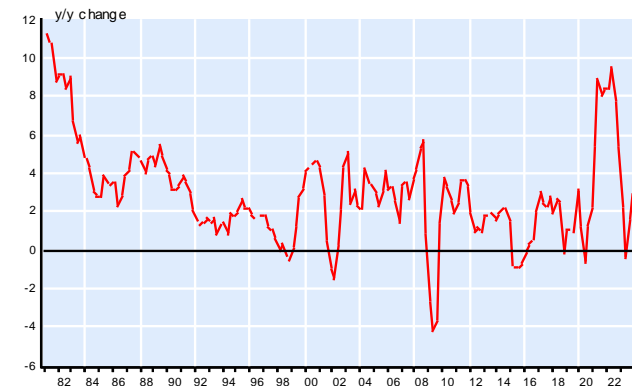
Government

Net lending as a share of GDP



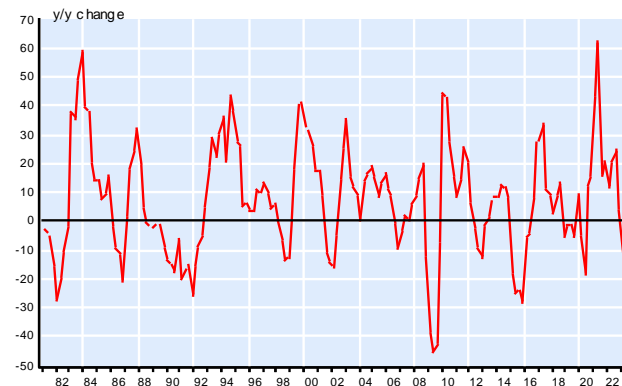
Inflation

GDP deflator (chain-weighted)



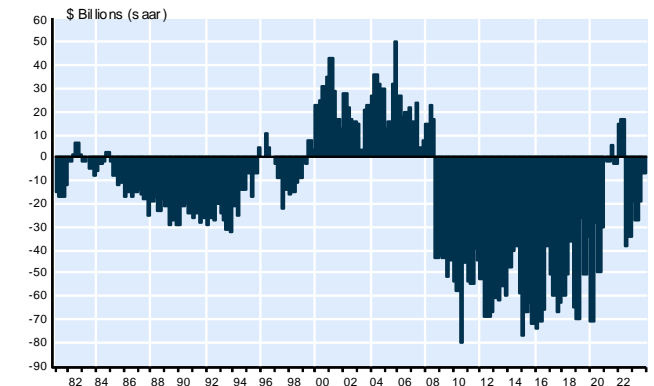
Profits

Corporate profits before tax



Current account

Balance on the current account



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