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Economics Group

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Consumer Spending Lifted Canadian GDP Yet Again in Q4

Canadian GDP grew at an annualized rate of 2.6 percent in Q4-2016, which was better than consensus expectations. Consumer spending and trade did most of the heavy lifting. The Bank of Canada stayed on hold.

Streaks Not Likely to go on Forever

Canadian consumer spending expanded at an annualized rate of 2.6 percent in the final quarter of 2016. This extends a truly remarkable streak of uninterrupted quarterly growth in consumer spending that dates back to the second quarter of 2009.

The untrammeled expansion has not come without cost. The run-up in housing prices in Canada along with the 7+ years of uninterrupted expansion in consumer spending has burdened household finances. The consumer debt-to-GDP ratio in Canada now stands at 96.2 percent, up from just 74.9 percent in Q2-2008. The state of consumer balance sheets in Canada has deteriorated to a point where we find ourselves questioning the sustainability of consumer spending continuing to act as a driver of economic growth as it so reliably has done since Canada emerged from recession more than seven years ago.

While we are on the topic of streaks, business investment fell again in the fourth quarter, this time at an annualized rate of 6.0 percent. The latest quarterly drop extends the number of declines in this category to nine straight. It does not take much detective work to identify a connection between the time that oil prices peaked in mid-2014 and when business investment first began to decline in the fourth quarter of that year.

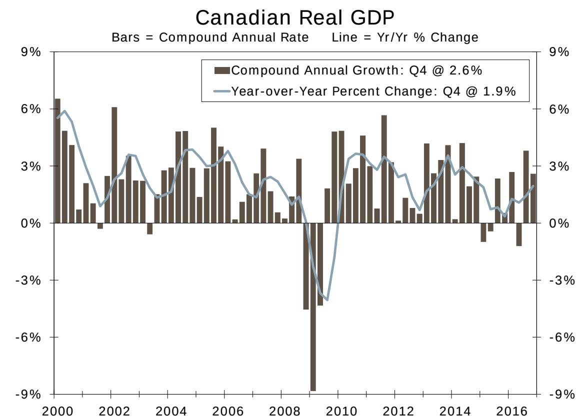
In the official release from Statistics Canada, the text noted that business investment in structures got a boost in the prior quarter (the third quarter) from the Hebron offshore oil project. Following that one-time boost, it is not surprising to see the steepest declines in this sub-category.

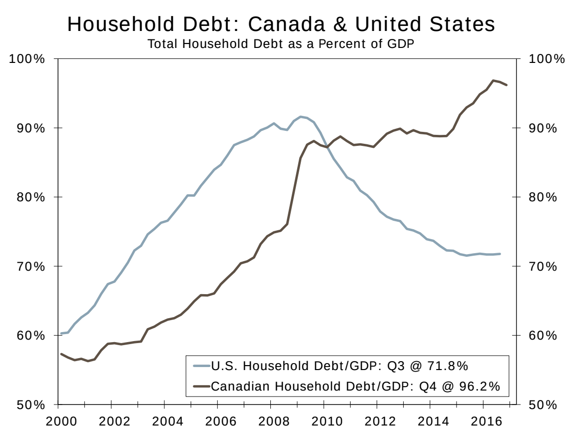
Just as we are skeptical about consumer spending continuing its streak, in our view there is good reason to suspect that after more than two years of scaling back, businesses now have a very low base of spending upon which we could see some improvement in business spending in 2017. The case for improving activity in the business sector is corroborated by trend improvement in the Ivey PMI and the fact that the Markit PMI in February rose to its highest level since 2014.

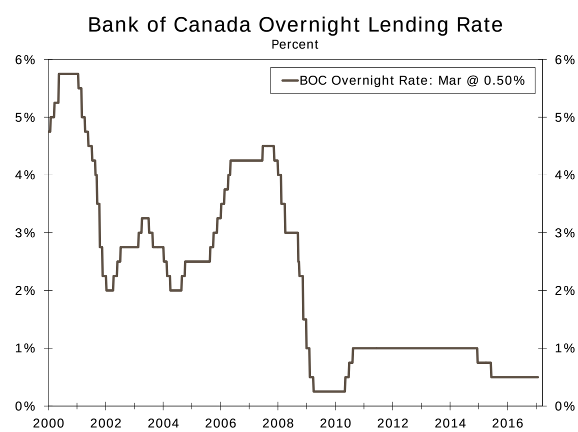
On the trade side, imports posted a steep decline and exports increased modestly resulting in a boost from net exports.

Implications for the Bank of Canada

In Ottawa yesterday, the Bank of Canada (BoC) maintained its overnight rate target at 0.50 percent. In its accompanying note, the BoC identified fact that CPI inflation had risen to 2.1 percent in January and correctly anticipated that fourth quarter growth might exceed consensus expectations. It also said the inflation surge was likely transitory and that growth would remain under pressure. On that basis, we suspect the BoC will remain on hold for the foreseeable future.







Source: IHS Global Insight, U.S. Federal Reserve and Wells Fargo Securities

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