

September 1, 2023

## Canadian GDP growth edged lower in Q2

- Canadian GDP surprised on the downside by edging slightly lower (-0.2% at an annualized rate) in Q2. The early estimate a month ago was for a 1% increase.
- On a monthly basis, weakness was concentrated in a 0.2% drop in output in June. The early estimate of July GDP was "essentially unchanged" from that June level, leaving activity early in Q3 down ~-0.4% in Q3 (close to our own tracking for a -0.5% GDP decline that quarter)
- Consumer spending edged up in Q2 (+0.2%) but that was the smallest rise since pandemic lockdowns in Q2-2021. Residential investment continued to decline with a bounce-back in the home resale market offset by a drop in new building activity.
- Business investment rose, in part on a surge in (imported) aircraft purchases. Net trade subtracted half a percentage point from GDP growth with a larger tick higher in imports than exports.
- The small decline in Q2 GDP isn't entirely a surprise - earlier advance GDP estimates have been revision-prone in the past and there have been signs that headwinds to economic growth from higher interest rates have been building under the surface. But the data is now tracking well-below the 1.5% per-quarter annualized growth rates the BoC has been assuming for the middle quarters of this year.
- Part of the Q2 weakness is tied to 'temporary' factors like the federal workers strike in April, but labour market data has also been looking softer with the unemployment rate up half a percent over the last three months. And consumer delinquency rates have been edging higher.
- **Bottom line:** The GDP data should reinforce expectations that the BoC will move back to the sidelines and forego another interest hike next week. The BoC won't put too much emphasis on one piece of data, and inflation is still 'stickier' at above-target rates than they would like. But evidence is building that the lagged impact of earlier rate hikes are beginning to work more significantly to cool GDP growth and labour markets, and that should mean inflation pressures will continue to gradually slow.

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Policymakers will want to leave the door open to re-starting hikes again down the road if necessary. But if the unemployment rate continues to drift higher, as we expect, a re-start won't be necessary.

| <b>Canadian GDP Growth</b>         |                           |                |                |                |
|------------------------------------|---------------------------|----------------|----------------|----------------|
|                                    | <i>Q/Q annualized %</i>   |                |                |                |
|                                    | <u>2022/Q3</u>            | <u>2022/Q4</u> | <u>2023/Q1</u> | <u>2023/Q2</u> |
| Consumer spending                  | 0.3                       | 1.1            | 4.7            | 0.2            |
| Goods                              | -3.9                      | 2.4            | 4.9            | 0.6            |
| Services                           | 3.9                       | 0.0            | 4.7            | -0.1           |
| Government                         | 4.7                       | 2.3            | -3.7           | 2.5            |
| Res Investment                     | -18.4                     | -9.9           | -19.1          | -8.2           |
| Business investment                | 1.0                       | -5.1           | 5.7            | 10.3           |
| Net trade (ppt cont, annualized)   | 4.5                       | 5.4            | 3.1            | -0.5           |
| Inventories (ppt cont, annualized) | -1.4                      | -5.7           | -1.5           | -0.8           |
| <b>Canada GDP</b>                  | <b>2.3</b>                | <b>-0.1</b>    | <b>2.6</b>     | <b>-0.2</b>    |
|                                    | <i>Q/Q percent change</i> |                |                |                |
| <b>Household disposable income</b> | 0.5                       | 2.5            | -0.6           | 2.6            |
| <b>Saving rate</b>                 | 4.7                       | 5.8            | 3.7            | 5.1            |

\*Source: Statistics Canada, RBC Economics