WEEKLY COMMENTARY

Provincial GDP Numbers Show Rate Hikes' Early Impacts, Highlight New Weak Points

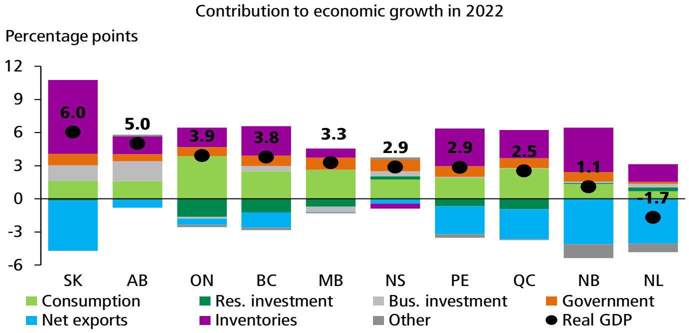
By Marc Desormeaux, Principal Economist

Earlier this week, the 2022 GDP numbers released for Canada's provinces showed broad-based headline output gains. But in an environment of big historical revisions and lingering questions about how the past year's super-fast monetary tightening cycle will impact debt-saddled households, we spotted several troubling details.

Spiking business inventories drove much of the expansion experienced across the country last year (graph 1). At the national level, that effect has since receded significantly. Moreover, while household consumption rose across the provinces in 2022, it was undoubtedly helped by rebounds from 2021 COVID lockdowns. It also pushed imports much higher to more than offset strong export growth in several jurisdictions. And excluding the three westernmost provinces, non-residential business investment fell. However, we expect the major project activity that supported capital outlays in Saskatchewan, Alberta and BC to ease over the next two years. That said, major project activity in those regions will be less sensitive to borrowing costs than investment activity elsewhere in the country.

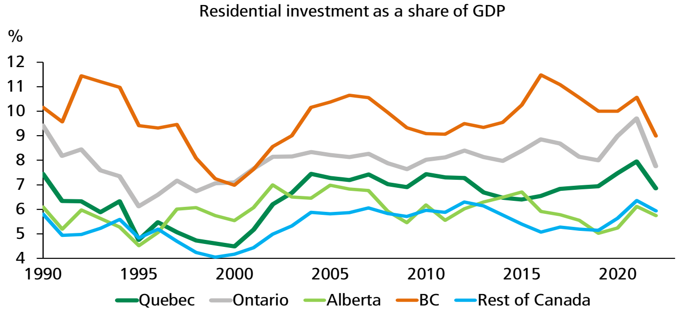
We already knew how much of a drag housing posed at the national level last year as interest rates rose sharply, but the breadth of weakness and depth in some regions was striking. Seven provinces experienced residential investment declines, a count exceeded only during severe recessions in the past. In all three of the large oil-consuming provinces (Ontario, Quebec and BC), residential investment fell by more than at any point since the 1990s. In fact, in both Ontario and BC—the two most housing-oriented provincial economies—growth would have been over 5% were it not for the drag from residential investment. Remarkably, following 2021's heights, residential capital outlays' share of output in 2022 was below the average of the decade before the pandemic everywhere but the Maritimes (graph 2).

GRAPH 1
Broad-Based Headline Growth Masks Weakness in Parts of Canada's Provincial Economies



Sources: Statistics Canada and Desjardins Economic Studies

GRAPH 2
Housing Stepped Back After Huge Contributions to Growth in Prior Years



Sources: Statistics Canada and Desjardins Economic Studies

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Going forward, we expect local housing market conditions to continue to dictate relative regional economic performance. Statistics Canada noted that residential investment declines were most pronounced in Ontario and BC, where home sales were initially hardest hit and are now falling again. And we think there's less chance that purchasing activity rebounds in these areas in the coming months the way it did after the Bank of Canada first implied it was done hiking rates. Combined with accumulated affordability erosion since that time, the higher-for-longer narrative that has taken hold in bond markets could keep mortgage rates high until interest rates are eventually cut next year. By contrast, four months after the central bank hiked again, home purchasing activity is still going strong in the oil-producing regions, helped by exceptionally strong population growth and relative affordability.

The 2022 data also revealed some risks that weren't present in early GDP estimates for Canada's two largest provinces. In Ontario—as most elsewhere—elevated levels of savings accrued by some households during the pandemic appear to have shielded consumers against the effects of higher interest rates and inflation. But Statistics Canada's official 3.2% household saving rate for 2022 was less than half the 7.3% that had been estimated by the province. That means a smaller financial cushion against adverse economic shocks than previously assumed in one of the regions most sensitive to high interest rates. More broadly, it's more likely that persistently high borrowing costs prompt consumers to pull back spending in Ontario and BC than in Alberta and Saskatchewan, where savings are higher.

Provincial GDP data are lagged, but nonetheless provide critical takeaways for growth in 2023 and beyond. For one thing, the recent drag from the housing market and signs of potentially greater financial stress in highly indebted regions reinforce our view that the oil-producing provinces are best positioned to weather the coming storm. That would be a change from the five years before the pandemic, when slow recovery from the 2014–15 crude price correction held back the expansion in our commodity-producing regions. Maybe more importantly, just as affordability significantly affected provincial economic prospects in 2022, it looks likely to continue to do so in the years to come.

What to Watch For

By Randall Bartlett, Senior Director of Canadian Economics, Tiago Figueiredo, Associate – Macro Strategy, Marc Desormeaux, Principal Economist, Marc-Antoine Dumont, Economist, and Francis Généreux, Principal Economist

UNITED STATES

TUESDAY November 14 - 8:30

October	**m/m**
Consensus	0.1%
Desjardins	0.0%
September	**0.4%**

Consumer price index (October) – After three months at or under 0.2%, the month-over-month change in the consumer price index (CPI) spiked to 0.6% in August and 0.4% in September, partly due to a rise in energy and gasoline prices. However, the trend reversed in October, with pump prices declining 6.8%. As such, energy's contribution to the monthly all items index is expected to be clearly negative. We also think food prices increased 0.2%, which is a bit less than the 0.3% we saw in September. Less food and energy, we expect another 0.3% gain in line with August and September's prints. Added to food cost increases, this gain should offset the negative impact of energy prices, with the month-over-month change in the all items index expected to come in at 0.0%. Year-over-year, the all items index should fall from 3.7% to 3.2%, while core inflation is likely to remain flat at 4.1%.

WEDNESDAY November 15 - 8:30

October	**m/m**
Consensus	-0.3%
Desjardins	0.0%
September	**0.7%**

Retail sales (October) – Retail sales rose quite strongly for the third consecutive month, with September's 0.7% gain following 0.9% and 0.6% increases in August and July, respectively. This was a major contributor to higher consumer spending and real GDP in the third quarter. Look for the fourth quarter to have started on a more modest note. Auto sales fell in October based on new motor vehicle sales data released in early November. Sharply lower pump prices are also likely to have dragged down gasoline station receipts. The situation is more mixed for the other categories. Preliminary card transaction data suggests that sales of certain durable goods declined but food services and online shopping rose further. All in all, we expect total retail sales to be flat at 0.0%, and sales excluding motor vehicles and gasoline to gain 0.5%.

THURSDAY November 16 - 9:15

October	**m/m**
Consensus	-0.3%
Desjardins	-0.1%
September	**0.3%**

Industrial production (October) – Industrial production rose 0.3% in September, primarily on the back of a 0.4% gain for manufacturing. This was especially surprising given that it occurred during the autoworkers' strike. Although this labour dispute is now over, it still probably had a negative impact on manufacturing in October. We expect to see a 0.2% decline in manufacturing, no change in mining and a slight rise in energy production. Overall, we think industrial production will drop by 0.1%.

FRIDAY November 17 - 8:30

October	**ann. rate**
Consensus	1,350,000
Desjardins	1,375,000
September	**1,358,000**

Housing starts (October) – Housing starts were up 7.0% in September, reflecting a return to a more normal level after August's 12.5% slump. We're expecting another—albeit more modest—increase for October. The 6,700 jobs added in residential construction last month was the strongest print since May 2022. Building permits also remain well above housing starts, which could provide a boost to the latter. Rising mortgage rates are clearly expected to cause further pain in the housing market, but it could take a bit longer for construction to take a meaningful hit.

CANADA

WEDNESDAY November 15 - 8:30

September	**m/m**
Consensus	n/a
Desjardins	-0.1%
August	**0.7%**

Manufacturing sales (September) – Following two consecutive months of growth, Canadian manufacturing sales are expected to have edged down 0.1% in September. This was likely the result of volumes, as price growth probably mirrored the increase in the Industrial Product Price Index. Exports of motor vehicle engines and parts fell in September as did car and truck production, pointing to lower manufacturing sales in the automotive sector. According to Statistics Canada, factory sales were also down in the primary metals, chemical and transportation equipment sectors during the month.

WEDNESDAY November 15 - 9:00	
October	**m/m**
Consensus	n/a
Desjardins	-2.0%
September	**-1.9%**

Existing home sales (October) – We expect Canadian Real Estate Association data due out Wednesday to show that national-level home sales fell by 2% in October. As always, however, city-level results will be much more useful and interesting. Preliminary information from local real estate boards suggests that homebuyers in most large centres are feeling the pinch of higher borrowing costs. According to these data, even the Calgary and Edmonton markets—so far relatively unaffected by the second round of interest rate hikes that began in June—are cooling. Meanwhile, high-priced Vancouver and Toronto—whose sales activity has taken big steps back in the last four months—may have moved past their peak rates of decline. Again, though, we should be just as interested in what happens to listings. More big increases would further imply that many current homeowners are struggling to cover higher mortgage interest costs. Still, tighter supply in some areas could help sustain upward pressure on prices even if sales decline.

THURSDAY November 16 - 8:15	
October	**ann. rate**
Consensus	n/a
Desjardins	250,000
September	**270,500**

Housing starts (October) – Will this be the month new housing construction finally slows? We think it just might be. We expect the October 2023 housing starts data—set for release on Thursday—to report a drop to 250k units across Canada. We reiterate that other than the record-high population growth currently underway across much of the country, there aren't many indicators that suggest conditions supportive of homebuilding. Interest rates and building material costs are at decades-high levels. Sentiment in the homebuilding sector is very weak, and the construction industry continues to grapple with labour shortages. Ontario and BC are the regions to watch, as their resilient homebuilding has propped up national-level starts for several months now. Building permits and construction industry employment are trending lower in Ontario but rebounded strongly in BC in the latest data.

OVERSEAS

TUESDAY November 14 - 18:50	
Q3 2023	**q/q**
Consensus	-0.1%
Q2 2023	**1.2%**

Japan: Real GDP (third quarter) – At first glance, the Japanese economy had a very good second quarter with real GDP up a non-annualized 1.2%. But this headline number conceals some weaknesses, including declines in real consumption and investment. Will these pullbacks become more acute in the third quarter? Over the summer we saw housing starts and industrial production contract, but retail sales improve—albeit more modestly in real terms. Japanese PMIs have also fallen in recent months. As such, Japanese real GDP growth is unlikely to be as stellar as spring's surprise print, and we may even see a contraction.

TUESDAY November 14 - 21:00
October

China: Industrial production and retail sales (October) – Although global economic activity is slowing and Chinese exports have been declining year-over-year since May, industrial production has held up fairly well, rising 4.5% in both August and September. That said, consumption of goods in advanced economies is likely to continue to moderate and eventually become a headwind for the Chinese manufacturing sector. In the short term, gains in industrial production and retail sales may cool in October, reflecting the unexpected decline in PMIs and more entrenched weakness in the Chinese economy. October's data will also provide further insight into the path for economic growth in the fourth quarter.

Economic Indicators

Week of November 13 to 17, 2023

Day	Time	Indicator	Period	Consensus	Desjardins	Previous reading
UNITED STATES						
MONDAY 13	---	---				
TUESDAY 14	8:30	Consumer price index				
		Total (m/m)	Oct.	0.1%	0.0%	0.4%
		Excluding food and energy (m/m)	Oct.	0.3%	0.3%	0.3%
		Total (y/y)	Oct.	3.3%	3.2%	3.7%
		Excluding food and energy (y/y)	Oct.	4.1%	4.1%	4.1%
WEDNESDAY 15	8:30	Producer price index				
		Total (m/m)	Oct.	0.1%	-0.3%	0.5%
		Excluding food and energy (m/m)	Oct.	0.3%	0.2%	0.3%
	8:30	Empire State Manufacturing Index	Nov.	-2.6	-7.5	-4.6
	8:30	Retail sales				
		Total (m/m)	Oct.	-0.3%	0.0%	0.7%
		Excluding automobiles (m/m)	Oct.	-0.2%	0.2%	0.6%
	10:00	Business inventories (m/m)	Sept.	0.4%	0.4%	0.4%
THURSDAY 16	8:30	Initial unemployment claims	Nov. 6–10	225,000	220,000	217,000
	8:30	Philadelphia Fed index	Nov.	-11.0	-7.5	-9.0
	8:30	Export prices (m/m)	Oct.	-0.6%	0.0%	0.7%
	8:30	Import prices (m/m)	Oct.	-0.3%	-0.2%	0.1%
	9:15	Industrial production (m/m)	Oct.	-0.3%	-0.1%	0.3%
	9:15	Production capacity utilization rate	Oct.	79.5%	79.5%	79.7%
	10:00	NAHB housing market index	Nov.	40	n/a	40
	16:00	Net foreign securities purchases (US$B)	Sept.	n/a	n/a	63.5
FRIDAY 17	8:30	Housing starts (ann. rate)	Oct.	1,350,000	1,375,000	1,358,000
	8:30	Building permits (ann. rate)	Oct.	1,453,000	1,450,000	1,471,000
CANADA						
MONDAY 13	---	Markets closed (Remembrance Day)				
TUESDAY 14	---	---				
WEDNESDAY 15	8:30	Manufacturing sales (m/m)	Sept.	n/a	-0.1%	0.7%
	8:30	Wholesale sales (m/m)	Sept.	n/a	0.0%	4.2%
	9:00	Existing home sales (m/m)	Oct.	n/a	-2.0%	-1.9%
THURSDAY 16	8:15	Housing starts (ann. rate)	Oct.	n/a	250,000	270,500
FRIDAY 17	8:30	Industrial product price index (m/m)	Oct.	n/a	0.0%	0.4%
	8:30	Raw materials price index (m/m)	Oct.	n/a	-2.4%	3.5%
	8:30	International securities transactions ($B)	Sept.	n/a	n/a	-8.47

Note: Each week, Desjardins Economic Studies takes part in the Bloomberg survey for Canada and the United States. Approximately 15 economists are consulted for the Canadian survey and a hundred or so for the United States. The abbreviations m/m, q/q and y/y correspond to month-over-month, quarter-over-quarter and year-over-year change respectively. Following the quarter, the abbreviations f, s and t correspond to first estimate, second estimate and third estimate respectively. Times shown are Eastern Standard Time (GMT - 5 hours). Desjardins Economic Studies forecast.

Economic Indicators

Week of November 13 to 17, 2023

Country	Time	Indicator	Period	Consensus m/m (q/q)	Consensus y/y	Previous reading m/m (q/q)	Previous reading y/y
OVERSEAS							
SUNDAY 12							
Japan	18:50	Producer price index	Oct.	0.0%	0.9%	-0.3%	2.0%
MONDAY 13							
Germany	---	Current account (€B)	Sept.	n/a		16.6	
TUESDAY 14							
Eurozone	5:00	Net change in employment – preliminary	Q3	n/a	n/a	0.2%	1.3%
Eurozone	5:00	Real GDP – preliminary	Q3	-0.1%	0.1%	-0.1%	0.1%
Germany	5:00	ZEW Current Conditions Survey	Nov.	-76.9		-79.9	
Germany	5:00	ZEW Expectations Survey	Nov.	5.0		-1.1	
Japan	18:50	Real GDP – preliminary	Q3	-0.1%		1.2%	
China	21:00	Industrial production	Oct.		4.5%		4.5%
China	21:00	Retail sales	Oct.		7.0%		5.5%
Japan	23:30	Industrial production – final	Sept.	n/a	n/a	0.2%	-4.6%
WEDNESDAY 15							
France	1:30	ILO unemployment rate	Q3	7.3%		7.2%	
United Kingdom	2:00	Consumer price index	Oct.	0.1%	4.7%	0.5%	6.7%
United Kingdom	2:00	Producer price index	Oct.	0.1%	-1.0%	0.4%	-0.1%
France	2:45	Consumer price index – final	Oct.	0.1%	4.0%	0.1%	4.0%
Eurozone	5:00	Trade balance (€B)	Sept.	n/a		11.9	
Eurozone	5:00	Industrial production	Sept.	-0.9%	-6.3%	0.6%	-5.1%
Japan	18:50	Trade balance (¥B)	Oct.	-712.1		-434.1	
Japan	23:30	Tertiary Industry Activity Index	Sept.	-0.1%		-0.1%	
THURSDAY 16							
Italy	4:00	Trade balance (€M)	Sept.	n/a		2,070	
FRIDAY 17							
United Kingdom	2:00	Retail sales	Oct.	0.3%	-1.5%	-0.9%	-1.0%
Eurozone	4:00	Current account (€B)	Sept.	n/a		27.7	
Italy	4:30	Current account (€M)	Sept.	n/a		2,840	
Eurozone	5:00	Consumer price index – final	Oct.	0.1%	2.9%	0.1%	4.3%

NOTE: Unlike release times for US and Canadian economic data, release times for overseas economic data are approximate. Publication dates are provided for information only. The abbreviations m/m, q/q and y/y correspond to month-over-month, quarter-over-quarter and year-over-year change respectively. Times shown are Eastern Standard Time (GMT - 5 hours).