

Canada: February's trade surplus widens CAD600mn

A humble report with big implications for Canada.

Virtuous. The Canadian trade surplus in February at CAD1.4bn is well ahead of the market median at CAD0.6bn and our own forecast at CAD0.2bn. Setting aside the whoop associated with running a decent surplus, there is a more important mix of virtuous factors held below the headline. To be certain, the upside surprise rise in the trade surplus was a nice treat. Even better, the rise in the trade surplus came on the back of rising volumes for both the import (+1.0%/m/m) and export (1.4%/m/m) categories.

More still. Both the breadth, 6 of 7 categories saw gains, and the geographic dispersion were impressive. Exports to the EU grew by 5%/m/m, OECD 8.3%/m/m, the US 2.0% and all others 5.3%/m/m. And coming on the back of severe winter storms in the US northeast which was believed to have crimped activity, is all the better.

Why is this so important? For Canada to embark upon a sustained and balanced economic recovery, these are the kind of reports that we need to see. While the consumer, supported by a bed feathered in rate driven liquidity, has long carried the economic football for Canada through thick and thin, sustainable economic recovery necessitates that they be able to hand off the ball to both rising business demand and a recovery in external demand. On both points we are seeing movement and improvement.

Yesterday's Bank of Canada business outlook survey reflected renewed interest in business investment. From the report, "the balance of opinion on investment in machinery and equipment moved further into positive territory, pointing to an increase in investment spending over the next 12 months. Rather than just repairing or replacing existing equipment, firms are increasingly focusing investment spending on expansion--often into new markets or product lines--or on improving efficiency." In concert with this, it is noted that machinery and equipment imports were up 3.3%/m/m in February which will pander to the recapitalization story.

Complimenting what ostensibly looks like a nice potential pick up in business investment, external demand which makes up ~35% of the economy, the very external demand which was dashed on the rocks of global economic recession and financial conflagration, external demand which plunged on a volume basis by 30% between January 2007 and the low struck in May of 2009, is in the process of staging a recovery. February's report caps off a nice string of gains begun in June of 2009. From June 2009 to present, export volumes are up 14% although still 21% off the high watermark set in December of 2006. None-the-less, this is a strong report that dovetails very nicely with the theme of sustainable economic recovery for Canada given the breadth of the gains. And not only from just an export standpoint but so too did we see import volumes also advance, suggesting growing cross border activity. An active border, an active economy.

Underneath the headlines, of the 6 export categories posting gains, the auto sector (5.0%/m/m) and industrial goods (7.2%/m/m) saw particularly strong gains. The auto sector of course being one of the hardest hit areas of the economy would understandably be one area to benefit most from the onset of economic recovery. From an export standpoint, by luck of the draw, Canadian auto manufacturers happen to be producing some of North America's best selling model lines which undoubtedly contributes positively to the export picture (exports of passenger vehicle and chassis were up 9.4%/m/m).

Domestic press has been replete with stories of jobs growth in the auto sector as a number of the domestic assembly plants seek to bring back on line idled capacity as a means of meeting demand.

Embracing global economic recovery.

The rapid acceleration in industrial goods and machinery exports (+7.2% m/m) is arguably reflective of the overall global economic recovery. Looking at this category which includes materials, a couple of sectors were behind the surge, notably a 83.1% m/m rise in copper exports (a key economic barometer) coupled with a 265% m/m rise in nickel ores. Aerospace exports also jumped a surprising 8.2% m/m. Surprising given that the durable goods and factory orders and shipment data out of the US suggested that the aerospace sector continued to sag in February. So too did Canada's beleaguered forestry sector show signs of export life with most categories seeing growth. In that both lumber and wood products each jumped more than 7% perhaps speaks to an improved outlook for the new build sector in the US.

Growth in energy exports was sluggish at 0.8% m/m. As much as Canada is thought of as an oil story, that in reality is only half of the story. While crude petroleum exports were up 6.1% m/m, natural gas exports were down -7.6% m/m. On a dollar basis, natural gas exports are down 45% since April of 2008. By contrast, crude is down -10% over the same period. Imports of energy dropped by -14.2% m/m. Shutdowns and maintenance to blame. Tis the season when refineries begin to go off-line as they switch over from heating distillates on to high grade gasolines in front of the summer driving season.

The importance of the recovery in external demand that is highlighted by this report to the Canadian economic recovery story cannot be underestimated. In that we are seeing trade volumes on the rise at the rate they have been very encouraging. Of course the caveat lector (reader beware) is the return to near dollar parity in March and US dollar/CAD parity in April. While the currency has been run up the pole and hung as one of the primary culprits behind the plunge in external demand, we would put forward that a growing global economic pie is more important to Canada's external demand picture than the valuation of the Canadian currency. Under conditions of a shrinking economic pie, there is going to be no growth in demand volume at any price, regardless of how the currency is priced. To be certain, a strong currency will challenge exporters and impact profitability. However, we would suggest that the fact that the global economy is once again growing and with it demand expanding, although the Canadian dollar has hit parity with the US dollar, it need not suggest that export volumes retreat in both March and April. Soon enough we will know. And with that information, we will be in a better position to weight the economic and monetary impact of dollar parity.

Disclosure appendix

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