

The loon laid an egg.

Canadian GDP (Apr) 0.0%

There is going to be some disappointment associated with Canada's economic performance in April with the economy very nearly taking a step back. Actual GDP declined by about CAD400mn or -0.03%. The -0.0%/m/m was back of the market median of expectations looking for 0.2%/m/m and a little worse than our own slightly more pessimistic forecast looking for 0.1%/m/m (0.08% if we really want to be specific).

Underneath the headline disappointment, the story played out largely as expected with most categories exhibiting either incremental gains or incremental declines.

The movers, for the goods producing categories included a -0.7%/m/m drop in activity for the utilities sector which is largely weather related. Unseasonable mild temperatures have reduced the need for late season heating. The pay back comes in May with unseasonably warm temperatures. Manufacturing also slipped, dropping -0.3%/m/m although this is a moderation from five months of back to back gains of 1.0%/m/m or greater.

Service sector industries saw a couple of categories swing around. Retail trade fell by -1.7% but this was already well telegraphed given the rather significant decline in the retail sales report. So too did the arts, entertainment and recreation category plunge by -1.8% as the bloom of the Olympic rose finally faded.

Canada entered into the first quarter of 2010 like a lion, but exited like a lamb with April GDP bearing witness to a significant slow down in economic momentum. Average monthly growth for the last six months has been running at around 0.5%/m/m.

In part, we are seeing some strength drained off with the wrapping up of the Olympic experience that was seen to have boosted spending. As well, and particular to the consumer in April was the calendar effect associated with an early Easter in March which ended up cannibalizing April consumption. So too did we see some settling out from the binge on new autos in February. In that, much of the down side of the report can be explained in terms of factor that are more transitory than trend.

For those tasked with pricing the future cost of money in the here and now, today's report will complicate the pricing of the BoC. From a forecast standpoint, we continue to hold to our expectations that the BoC will hike rates by 25bps at its July 20 meeting, bringing the O/N rate target to 0.75%.

One month's data does not a trend make. Rather the past six months reflect a trend of particular strength that seemed destined to experience some degree of future moderation. Is this an inflection point? If ones experience were limited to the news stream it would certainly dovetail with that expectation. Yet from a more fundamental standpoint it is too early to tell whether or not this is a stand alone number.

However, against the back drop of deflationary fears, uncertainty associated with the ebb and flow of events in the European periphery, and concern over global economic growth and efforts to cool an overheated Chinese economy, in this environment, the gravitas attached to today's number set is likely exaggerated. Which is to say, in spite of an admiral economic performance over the last six months, with the economy performing well ahead of plan, the market tendency will to throw the report at the feet of the BoC and believe that it trips them up.

Still, it is important to recognize that for Canada, while it is no island unto itself, the main economic attachment point remains the US economy not Europe nor China for that matter. So too while the uncertainty associated with European sovereign credit risk has translated into equity market volatility, it has done little to upset inter bank lending in North American. Yes inter bank lending rates are higher (CDOR minus T-Bills), but nowhere near approaching the conditions that prevailed at the time of the financial crisis in 2008.

Instead, the issues as they pertain to Canada remain I) an economy that has performed well ahead of plan and II) a consumer that has been encouraged to binge on credit given historically low rates for money. Indeed, the BoC is unlikely responding to fears for inflation when it is raising rates so much as a need to discourage the consumer consumption of credit by raising the cost of funds.

Disclosure appendix

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