July 29, 2016

TD Economics

Data Release: Wildfires drag GDP lower in May

- Real GDP fell 0.6% (m/m) in May, with oil and gas production tumbling as a result of the Alberta wildfires. This marked the largest monthly decline since March 2009. Excluding this temporary oil and gas setback, monthly GDP fell by 0.1% according to Statistics Canada.
- The impacts of the wildfires were most evident in oil and gas extraction (-8.9% m/m), as well as petroleum manufacturing (-15.4%). Petroleum manufacturing was disrupted as the wildfires reduced the supply of raw inputs.
- Weakness within manufacturing (-2.4%) was not isolated to the petroleum industry, as production fell in both non-durable goods manufacturing (-2.8%) and durable goods manufacturing (-2.1% m/m). Output of transportation equipment (-3.4%) was affected in part by supply interruptions among motor vehicle and part manufacturers (-5.5%).
- It was a more positive story in the service side of the economy, with output up 0.3% in its eighth consecutive monthly expansion. Both wholesale and retail trade saw healthy gains in May, up 1.0% and 0.4% respectively. Finance and insurance was up a healthy 0.6%, while the real estate sector saw a more modest gain of about 0.1% after last month's strong performance (April: +0.5%).

Key Implications

- The May GDP report had little in the way of surprises, with what would otherwise have been a somewhat disappointing month dragged further into contractionary territory by the Alberta wildfires. Despite an expected recovery in output in June, the wildfire impacts result in second quarter GDP growth that is currently tracking -1.5%. A healthy rebound in growth is expected for the third quarter as the return to normality continues through the summer.
- When we look through the wildfire-generated volatility, the picture that emerges is of an economy that, following a strong December and January, has been just trudging along. Average growth through the middle of the year looks to be effectively in line with (or slightly below) the economy's underlying potential, meaning that none of the economic slack that developed through 2015 is currently being absorbed. While this is not the worst outcome, it does point to an economy that is largely treading water as the adjustment to lower commodity prices continues.
- From the Bank of Canada's perspective, recent developments have been more or less in line with the expectations communicated in their July 2016 Monetary Policy Report. As such, there is little impetus at present for the Bank of Canada to change its policy interest rate from its current level of 0.50%. That said, much will depend on the evolution of exports over the coming months. The Bank of Canada has repeatedly stressed that it sees a return to healthy export growth after the retrenchment that marked the start of this year; exports are expected to contribute roughly half of the growth forecast for 2017. However, the external environment has been less supportive of exports, as shown by the weak business investment in today's U.S. GDP report – a key driver of Canadian export gains. Should export growth fail to match their expectations, a re-evaluation of their growth outlook (and its implications for the policy rate) will likely be in order.

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