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GLOBAL ECONOMICS

SCOTIA FLASH

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Contributors

Derek Holt
VP & Head of Capital Markets Economics
Scotiabank Economics
416.863.7707
derek.holt@scotiabank.com

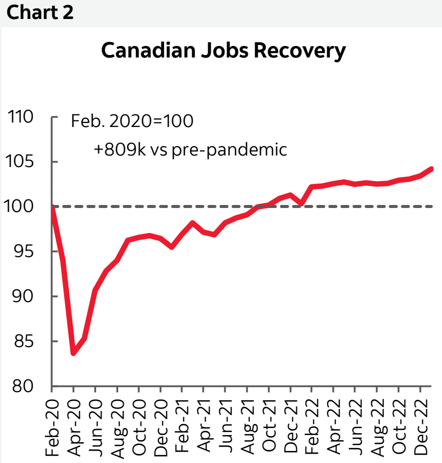
Chart 1

Canadian Jobs Break Down

Province	m/m
Ontario	+62.8k
Quebec	+47.4k
Alberta	+20.7k
Nova Scotia	+9.4k
British Columbia	+7.7k
Saskatchewan	+4.5k
Manitoba	+0.8k
Prince Edward Island	-0.4k
New Brunswick	-0.6k
Newfoundland & Labrador	-2.3k
Employment Type	**m/m**
Full Time	+121.1k
Part Time	+28.9k
Public Sector	+31.5k
Private Sector	+114.7k
Self Employed	+3.7k

Sources: Scotiabank Economics, Statistics Canada.

Chart 2



Sources: Scotiabank Economics, Statistics Canada.

Canadian Jobs Defy the BoC's Pause

- **Job growth blew away estimates again**
- **Robust details backed up the strong gain**
- **Hours worked point to strong GDP**
- **Wage growth stumbled again, adding to debate**
- **Further BoC hikes possible on domestic, external drivers…**
- **…with future cuts overplayed**
- **Eight plausible reasons for why job growth is so strong despite higher rates**

Canadian jobs, m/m 000s SA / UR (%), January:
Actual: 150.0 / 5.0
Scotia: 15.0 / 4.9
Consensus: 15.0 / 5.0
Prior: 69.2 / 5.0

Apparently, pandemics are ultimately good for jobs. Who knew?!

Another smashing employment report added 150k more jobs to the economy which takes the tally to date up by 809k jobs compared to what existed before the pandemic. See charts 1 and 2. The labour force has expanded by 685k over this same period.

Canada's sovereign yield curve immediately cheapened across the board relative to Treasuries and the Canadian dollar stepped over the yen to become the day's new class leader with a post-jobs appreciation of two-thirds of a cent to the USD.

In case anyone is tempted to dismiss the jobs number as noise, recall that the 95% confidence interval is about +/-57k. It would be highly improbable for this to have been a fake reading especially given a string of such readings.

BOC—APRIL IN PLAY

I wish the BoC would just stop giving forward guidance. Stop. Please. You're no good at it. Your models can't forecast inflation. Here's another illustration of how the BoC should be taking steps one at a time, being more circumspect and taking in new information during unique times as it arrives on a meeting-by-meeting basis. There is greater risk to falling behind developments amid regime shift and not tightening enough to ensure that inflationary forces have been countered than there is in overtightening by not waiting for the full lagging effects of adjustments to date. The BoC may be faced with yet another credibility challenge via its 'conditional' pause that mainstreet heard as 'done.'

Instead, the labour market continues to tighten and the details support robust GDP growth such that the balance of risks facing inflation remain skewed higher than the BoC's forecasts. Wage-price and output gap pressures will be expanded upon below.

March is out of the question for the BoC but if we keep getting data that is even remotely like this then don't rule out a return with another hike as soon as April with a fresh set of forecasts. Markets are now pricing a very decent chance at this and it fans my marketing narrative that the BoC may well not be done and shouldn't view itself as being done. I'm also deeply skeptical that the BoC would cut this year and think markets are too aggressively pricing cuts next year.

Macklem did, however, express this as a "conditional pause" and the condition keeps getting blown away by jobs and growth. There is a lot more data to consider into the next MPR meeting but the other consideration is that the Fed is leaving the BoC in the dust especially after this morning's upward US revisions to core CPI in November and

December and a strong UofM sentiment reading including higher 1-year inflation expectations. I can see the Fed's terminal rate at 5.5–6% in which case the BoC fans import prices via CAD if they go to sleep which further unmoors inflation expectations.

ROBUST DETAILS

The underlying details were robustly supportive of the headline gain.

Almost all of the gain was in full-time positions that were up by 121k with part-time jobs up 29k

Most of the gain was in private sector payrolls (+115k) as self-employed positions were roughly flat and public sector payroll positions were up by 31.5k.

Goods sectors added 25k jobs as construction jobs were up by 16k, manufacturing added 7k and resources were flat (+1k) with agriculture down 4k. Chart 3 breaks down job growth by sector last month.

Most of the gain was in services that were up 125k. Within services the breadth of the gain was decent.

59k jobs were added in wholesale/retail sectors with another 40k in health care/social and 18k more education sector jobs. The public sector jobs were not in administration (-3.8k) and skewed toward health/education.

By province, Ontario registered 63k more jobs with Quebec up 47k, Alberta up 21k and BC posted a modest 8k gain.

Businesses are still finding workers. The labour force expanded by 153k to keep the unemployment rate flat at 5%.

Still, the participation rate went up by 0.7 ppts to 65.7% which is the highest since last May. The peak was 66.3% in April 2019. There is no evidence of mass retirement and quitters north of the border.

Youth jobs were up only 7k. The overall employment gain was spread among men 25+ at +75k and 25+ women at +68k with older workers also gaining at +43k for 55+ led by men at 25k and women at 17k.

WAGES THE FLY IN THE OINTMENT

Wages stumbled again. Average hourly wages of permanent employees fell -0.1% m/m SA after 0% m/m change in December. This has to be carefully monitored along a highly volatile trend (chart 4).

The debate around this will be a) whether wage growth is truly cooling based on the first two soft months in quite a while and whether that's just a return to prior soft patches along a strong trend, or b) as the job market keeps getting tighter and tighter will wages accelerate again? And bear in mind poor productivity growth as the other part of it.

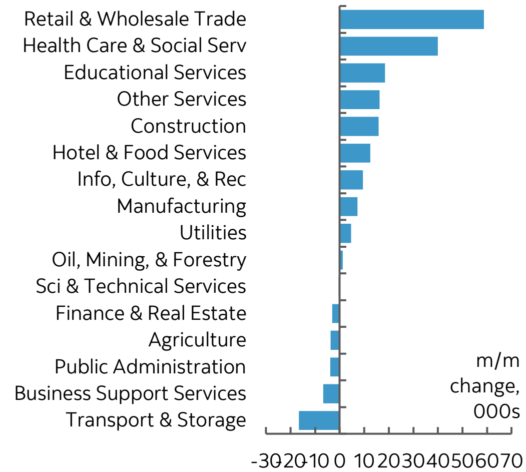
STRONG GDP SIGNALS KEEP PUSHING EXCESS DEMAND

There is, however, something that could offset the recent soft patch in wage growth from an inflation standpoint. Hours worked point to ripping GDP growth that continues to slant inflation risk higher rather than lower.

Hours worked were up 0.8% m/m SA in January which is a strong signal for monthly GDP given that GDP is an identity defined as hours worked times labour productivity.

Chart 3

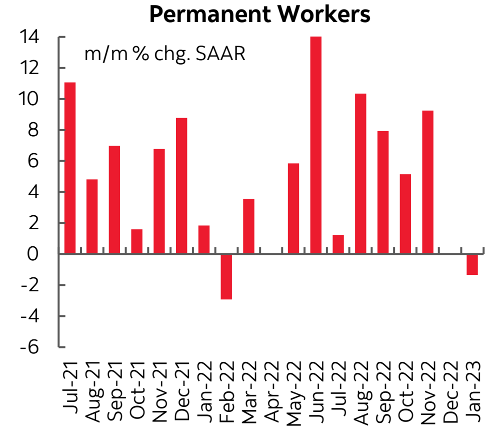
January Changes in Canadian Employment Levels by Sector



Sources: Scotiabank Economics, Statistics Canada.

Chart 4

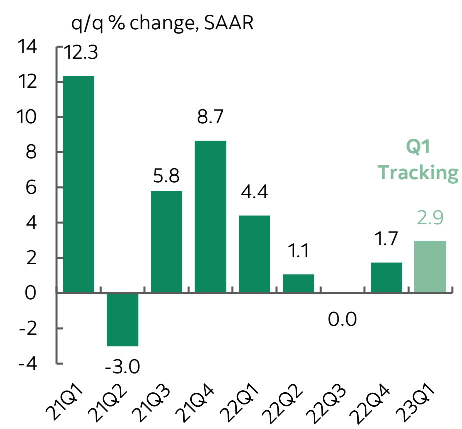
Average Hourly Wages of Permanent Workers



Sources: Scotiabank Economics, Statistics Canada

Chart 5

Total Hours Worked



Sources: Scotiabank Economics, Statistics Canada.

Hours are tracking a gain of +2.9% q/q in Q1 based on the Q4 hand-off and the start of Q1 assuming February and March are flat in order to focus the math on what we know so far (chart 5). That also suggests solid Q1 GDP growth.

If that holds, then the BoC is potentially getting surprised higher again given they had forecast Q1 GDP growth at just 0.5% q/q SAAR in the January MPR.

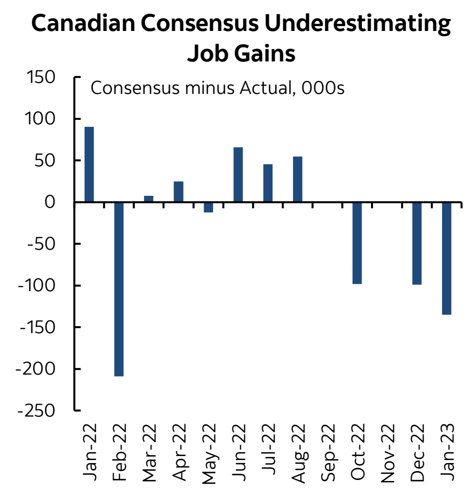
This means that Canada is still not taking steps to create any slack by growing at a rate below potential growth. It's the opposite amid tentative signs Canada's economy continues to grow at (Q4) or above (Q1) potential and hence further into excess aggregate demand.

That, in turn, means that the lagging effects continue to skew toward upside risks to core inflation that are not over yet.

WHY IS THIS HAPPENING?

As chart 6 demonstrates, consensus has some explaining to do. In fact, the consensus bias has drastically underestimated recent job growth in the US and Canada. In the US, consensus has underestimated job growth in twelve of the past thirteen months. In Canada, consensus has underestimated job growth to the tune of 332k jobs since October using the initially reported actual job growth estimates and by 274k compared to currently revised job growth estimates. Market-based borrowing costs have been rising for about a year-and-a-half and yet job growth remains very robust despite such long lags.

Chart 6

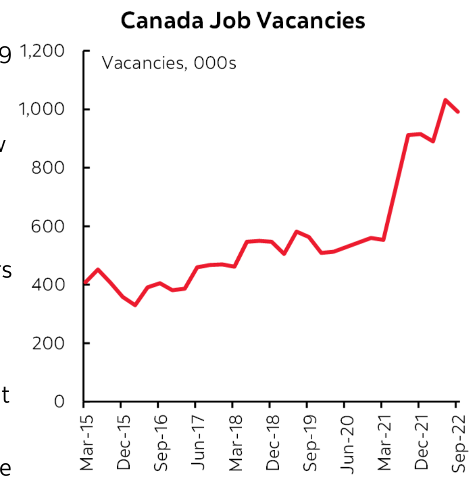


Sources: Scotiabank Economics, Bloomberg.

Why? I'm not entirely sure but beyond simply pointing the finger toward excessive gloom, here is a list of re-hashed plausible explanations for why job growth is accelerating despite higher borrowing costs that began in the Fall of 2021 (market, versus administered policy rate).

1. Supply chains are improving, offering the ability to produce more. It's extremely unusual to have improving supply chains into a tightening environment which is among many differences in our times compared to the human tendency to look for past parallels.
2. To meet higher production, adding variable costs may be preferred over fixed costs in terms of sourcing inputs to produce more amid all of the uncertainty. It's easier to adjust VCs than getting stuck with fixed depreciation and interest charges.
3. Productivity is weaker than in 2019 in absolute terms. Employers may feel they need to hire more workers to produce an hour's worth of output than they would have had to hire in 2019 to do the same. In short, hire more folks to make up for some of the slackers!
4. There are still massive job vacancies in sectors that couldn't hire anyone in the past and now can. I don't buy Macklem's line about falling vacancies as the decline is a rounding error with still nearly 1 million job openings in Canada.
5. I'm really not sure about the effects of immigration. It's not showing up in 'traditional' sectors (prof/sci/tech or trades or self-employed) as much as elsewhere. Plus there tend to be integration lags.
6. There is probably ongoing labour hording. Companies that release talent in this environment can just simply wave buh-bye as they go to the competition and permanently handicap organizations. I'm of the strong belief that companies need to be super careful that excessive restructuring winds up harming their revenues and competitiveness in this environment.

Chart 7



Sources: Scotiabank Economics, Statistics Canada.

7. And of course there are the fundamental supports via the terms of trade, excellent corporate balance sheet fundamentals, manageable inventories that if anything need to go higher on an I:S ratio basis, and fiscal supports. Plus I'm still of the belief that there is way too much negativity toward the household sector in Canada.
8. Another explanation I've been using is the economic necessity angle. In other words, we have more people being drawn into the workforce and going back to work if they have that as an option in their households and given pressures on finances. They are filling vacancies out of necessity which eases the shock to finances. In other cases, higher wages may be driving a pull factor even though that stumbled a bit that last couple of months.