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Recovery declining dramatically: economist

The Canadian economy had a great run immediately following the recession, but analysts warn that the stark reality of a slow, painful recovery — like the one gripping the United States — is beginning to sink in.

Growth forecasts are being scaled back on the emergence of weaker economic indicators — highlighted yesterday by a report on the surprise drop in July retail sales. This is on top of soft consumer price statistics that suggest core inflation is slowing, and a bleak wholesale trade report.

These factors prompted IHS Global Insight to warn Canadian growth could slow at a more dramatic pace than that of the U.S. economy. The firm now estimates annualized growth in Canada of less than 1% for this quarter — a big comedown for an economy that advanced 5.8% in the first three months of 2010, followed by a 2% gain in the April-to-June period.

“When you look at relative momentum, Canada is declining even faster than the United States,” said Brian Bethune, the firm’s chief Canadian economist.

Warnings of a much slower economy may come at a bad time for the Conservative government, which is aggressively pushing its handling of the economy as a big selling point should an election be called in the coming months.

Mr. Bethune said consumer spending that surged in February and March is running out of steam, as is activity in the housing market. Moreover, he said, labour market momentum is waning. In comparison, some key recent U.S. indicators — notably the ISM gauge, non-farm payrolls and retail sales — were stronger than anticipated.

Meanwhile, expectations mount the Bank of Canada will not raise rates at its meeting next month, and may be on the sidelines for a while, just like its U.S. counterpart, the Federal Reserve.

“The list of reasons for the Bank of Canada to pause is seemingly lengthening by the day,” Douglas Porter, deputy chief economist at BMO Capital Markets, said after the release of retail data, which showed sales at malls slipped 0.1% month-over-month in July — marking the fourth straight monthly decline.

Besides a rate decision, the central bank is set to release its latest quarterly outlook, which was already “too optimistic,” Mr. Bethune said, before this week’s spate of poor data. The central bank originally projected 3% annualized growth for Canada in the second quarter, only to come in at 2%. And the 2.8% advance it envisaged in the third quarter is looking a little too robust given how some economists are speculating the economy may have shrunk in July.

CIBC World Markets offered a preview of what's ahead for the Bank of Canada forecast when CIBC economists slashed its outlook for growth in Canada and the United States, warning investors to be prepared for the "great disappointment" of a dismal recovery that will stretch through 2011.

"The great recession that shattered global growth in 2008-2009 is now water under the bridge, but the great disappointment of a subpar global recovery will be with us for a good while longer," CIBC chief economist Avery Shenfeld said in a report.

CIBC cut its outlook for 2011 growth to 1.9% from 2.5%, while scaling back its U.S. target to a "paltry" 1.8% from 1.9%. Starting for the July-September period, annualized quarterly growth will not surpass 2% until mid-2011.

The U.S. economy, Canada's largest trading partner, will continue to be weak, as fiscal stimulus is removed and consumers continue to pay down debt. In addition, housing prices may fall further, CIBC warned, as a flood of foreclosed homes hit the market.

In Canada, Ottawa and the provinces will also undertake budget-cutting measures in 2011, which will hamper job creation, especially in construction. "And it's unlikely that the new jobs created in 2011 would be of the same high quality — limiting the upside potential in personal income," CIBC said.

Canadian retail data, released yesterday, suggest consumers may be keeping more of their income in their pockets. One factor could be that households are coming to grips with their record-high debt levels.

The retail data "suggests that Canadian consumers are beginning to adopt the same behaviours as their American counterparts concerning discretionary consumption," said Marie-Claude Guillotte, an economist at Laurentian Bank Securities. "It may be that Canadian consumers are also feeling a need to put their financial affairs in order — a goal that necessarily entails cutting spending."