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Atrocious, Anomalous, and So Much More

The best comment between the statuses of either the US or the Canadian economy comes from a Bank of Montreal Economist, Jenifer Lee. In referring to US economic growth in the first quarter she writes “the good news is its history.” The statement is as much applicable to Canada as well, as Stephen Poloz’s crystal ball should receive some credit for its foresight of an “atrocious first quarter” for growth. The US economy for the last 18 months has been the bellwether for global GDP growth, and since the energy sector began to tank in Canada around Q4 2014, The US relation to Canada has become even more important.

The numbers were a struggle as Canadian and US GDP growth in Q1 contracted at 6/10th and 7/10th of a per cent respectively, and although forecasted to be bad, the actual reported GDP arrived well below expectations. For Canada, it was the overbearing 30 per cent decline of the mining, oil and gas sectors. And although this blow comes very much as anticipated, awaiting the revival of the manufacturing sector is something that will not be realized in the short term. For Canadian growth to pick up absent of a revival in the energy sector, the health of the United States economy will ultimately be the be the decider for the overall economic health of this country.

US economic growth arguably sites more reason for caution. The two important factors of port strikes in Los Angeles and cold weather in the east were no doubt factors that weighed heavily on economic activity in January through March. And even though recent indicators have signalled a bit of a tide change for the better, devastating news this week of flood disasters in the US’s fourth largest city, Houston, will surely be yet another curve ball for the economy this year. It repeats the question, and whether it is inspired or not by an over focus from financial media, of when the US Fed will be able to raise interest rates.

Sound analysis on this topic suggests that the Fed raising rates is somewhat of a misnomer. The Fed does not want to jeopardize economic activity because of a restrictive rate environment. Instead a rise in rates will simply be an adjustment to current economic conditions. As good and likely as that sounds though, a very interesting interview from St. Louis Fed President James Bullard this week offered a contrary point of view. An insider to the Federal Open Market Committee, Bullard’s take was that the Fed must remain reactive and very sensitive to adjustments in the economy. According to Bullard, (and I summarize) the beauty of being data dependant is the Fed can literally take in all up to date information and decide on a moment’s notice when to raise rates. There is no telltale sign that says they should do it in June, July, or even September.

And this is where the market forces decide. We have the US dollar resuming yet another bull run. As we close the week, even with oil finishing up nearly 5 per cent, currencies and precious metals sit quietly against a market convinced action from the Federal Reserve is the most important aspect of financial markets entering the summer. This is in tune with a forecast that both the US and for that reason the Canadian economy will pick up too. Entering the summer months, this will advance the talk of a Fed rate hike; and as result, the rest of the dependent globe can follow.

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