

# Canada: June trade - wider deficit (-C\$1.1bn) on weaker volumes.

The worst of all possible outcomes.

**The Canadian trade data for the month of June provides us with the first real whiff of how June GDP may be shaping up. And that first whiff is a tad pungent with the trade deficit widening out from an upwardly revised May deficit of -CAD0.7bn to June's -CAD1.1bn. The market median had been looking for a trade deficit of -CAD0.3bn while our own forecast had penciled in a slight trade surplus of CAD0.2bn.**

Our own focus on the trade data invariably moves clear of the headline surplus/deficit where the bulk of the market interest lies, towards the real story - both figuratively and actually - as it pertains to trade volumes. Unfortunately little relief from the headline found in the underlying story. Our tendency is to be rather tolerant of a widening in the trade deficit so long as it is a function of expanding export and import volumes. The idea being that for a small open economy like Canada's, an active border is indicative of an active economy. Alas, for June, it was the worst of possible outcomes. A widening trade deficit coming on the back of both declining import and export dollar sales and volumes.

June's deficit was a function of the retreat in exports -2.5% m/m outpacing the decline in imports -1.2%. In terms of real activity, export volumes fell by -1.3% m/m while import volumes were unchanged.

To be fair, the picture on trade is not entirely a washout. Indeed a little perspective is needed to set June's trade data into the right context. For that, we have to look back on May's report where we find particularly strong growth in trade volumes - specifically export volumes jumped by 2.8% m/m (although revised down from the originally reported increase of 3.9%) while imports rose by an impressive 4.5% m/m. In effect, June's sloth like activity helps to smooth out some of May's frenetic activity. On that basis, it is perhaps more valuable to aggregate the two reports together. In terms of dollar receipts May exports were up 4.1% m/m only to have fallen by -2.5% in June. In keeping with this theme, May's imports were up 6.9%, only to be partially offset by June's -1.2% m/m decline in dollar receipts.

In terms of export damage, energy (-5.5%), industrial goods (-7.2%) and automotive (-4.6%) were all hard hit. Two out of three. For our forecast looking for a minor surplus of C\$200mn we had banked on declines in both the industrial goods and automotive categories but were looking for a nice boost to come out of energy. Higher temperatures in the North East were expected to have boosted the natural gas story, offsetting the weakness in the crude oil story (prices for crude were considerably lower). The average price paid per imported barrel of oil into the US declined by 5.8% m/m. Unfortunately natural gas exports were largely flat while crude petroleum exports plunged (-4.9% m/m). In each of the past four months, crude petroleum exports have declined on average -4.25% m/m. And higher crude import volumes into the US (on a barrel basis, crude petroleum imports into the US were up 11.4%) didn't help to insulate Canadian energy exports as both prices and volumes weakened.

The hit to auto sector exports is largely a seasonal effect. In May, passenger automobile exports surged by 30% as manufacturers pushed product out the door ahead of the summer shutdowns. On that basis, we are not overly concerned by the softness in the auto category.

Exports in the industrial goods category were hard hit by a -42.7% m/m decline in the export of nickel ores and a -51.0% decline in crude non-metallic minerals which immediately brings to mind the China story. Although Statcan points out that the bulk of the decline in exports outside of the 1.0% m/m drop in shipments into the US was a function of weaker demand out of EU countries. Particularly in the precious metals category.

On the upside, lumber exports have proven particularly strong (up on average 4.5% m/m in each of the past three months) although its hard to get bulled up on the US housing market which suggests efforts to market into other areas of the globe may be paying off. Overall forestry products were up 1.4% in June. So too have exports of industrial machinery shown considerable strength over the past three months, rising 7.8% m/m in the current report. Aerospace and transportation equipment outside of autos saw strong growth as well as a good month for the export of office equipment and electronics pandering to the business investment story. Overall, machinery and equipment exports rose 3.7% m/m

In terms of imports, one bright spot worth noting is the rise in the import of machinery and equipment which rose by 0.5% m/m in June, having previously jumped 7.0% m/m in May. Again, this panders to the business investment story. For Canada to continue down the road to economic recovery, there is a necessary need to see demand roll away from a reliance upon consumer and government demand and on over to business investment and trade. In one sense not a complimentary set of circumstances. As we note, rising business investment tends to show up in higher imports of capital equipment. Still, in that imports of machinery and equipment continue to build upon May's elevated levels is encouraging, suggesting that Canadian businesses are beginning to move off the sidelines of the economic recovery and beginning to participate more directly.

Energy product imports dropped by a whopping -19.3% m/m which appears to have corresponded with the completed filling and coming on line of the first phase of a major pipeline into the US. It is often the cast that domestic production of heavy crude is blended with lighter grades of imported oil in order to facilitate its movement through pipelines.

While June's trade report is a disappointment, so too aggravated by downward revisions to May's strength, there is enough left in the May story that when blended with June and some seasonal effects, helps to make today's numbers a little more digestible.

# Disclosure appendix

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