Still Awaiting Canada's Non-Energy Export Revival

The much-anticipated rotation in Canadian growth toward a stronger trajectory in non-energy exports remains elusive. Even with a solid July rebound, non-energy export volumes are sitting almost 5% below the level at the start of the year. Reduced auto shipments and a drawdown of U.S. inventories appear partly to blame, but the slowdown has been more broadly based. With indebted households limited in their ability to drive notably stronger spending gains, moving beyond the economy's current sluggish growth trend relies critically on a stronger export performance.

Several factors are contributing to the slow and uneven trend in Canadian exports. The persistent softness in global and U.S. industrial activity, and business investment in particular, are largely responsible. In turn they are restraining demand for industrial materials and equipment, key Canadian export sectors accounting for roughly a third of non-energy shipments. The traditional strong relationship between Canadian exports and U.S. domestic demand remains intact, with the 2.7% average annual growth rate in Canadian non-energy export volumes over the latest four quarters in line with the 2.2% average annual increase in U.S. domestic demand (chart 1).

Charts 3-12 display the 10 major subcategories of Canadian non-energy merchandise exports alongside their respective U.S. demand benchmarks. Shipment volumes in most broad sectors are largely tracking relevant U.S. demand metrics, with the notable exception of the aerospace industry, where the new CSeries aircraft has been slow to launch.

Domestic competitiveness issues, reinforced by persistently weak productivity growth and relatively high unit labour costs, remain a hurdle to a faster export recovery. The improvement in Canada's cost competitiveness stemming from the roughly 15% decline in the value of the Canadian dollar vis-à-vis the U.S. dollar over the past two years has occurred against the backdrop of a broad strengthening in the greenback. Canada's effective exchange rate measured against the currencies of our major trading partners excluding the United States is little changed over this period.

Canada's share of U.S. non-energy goods imports has recently shown signs of stabilizing after declining steadily over the past decade and a half (chart 2). This includes several sectors assumed to be more sensitive to exchange rate movements, including consumer products and transportation equipment. However, there have been numerous false starts in the past.

Capacity constraints also are likely holding back export activity. A number of domestic manufacturing industries are operating at or above historical capacity utilization rates, including food products, wood & paper products, plastics & rubber products, furniture products and transportation equipment. Global economic uncertainty, weak domestic earnings growth and the rising cost of imported machinery suggest businesses may remain reluctant to commit new capacity-generating investments, dampening future export potential.

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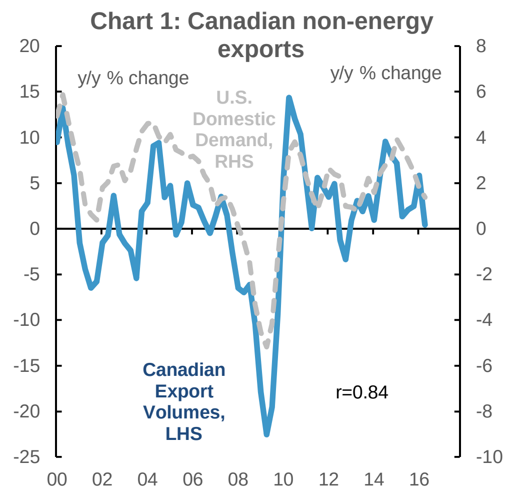
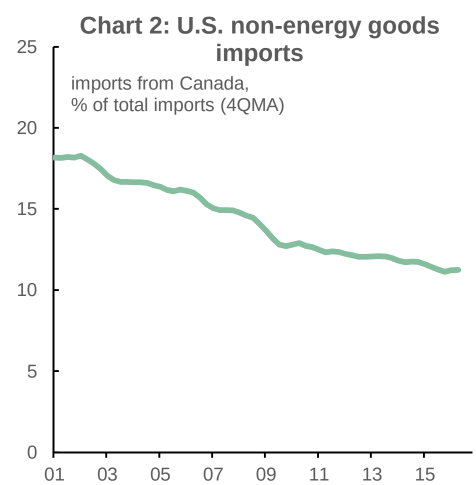
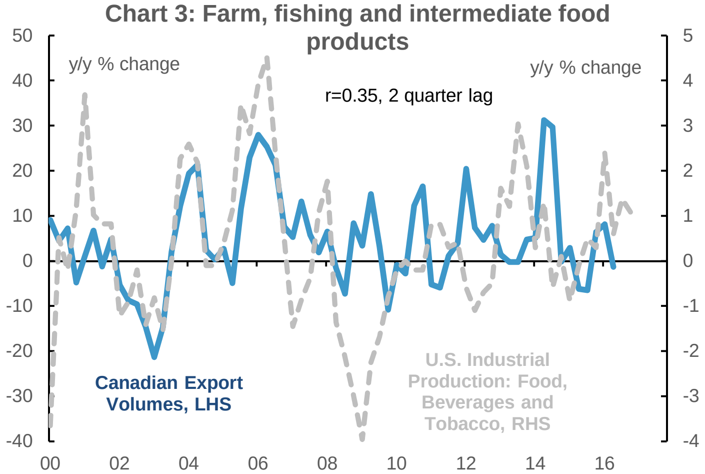


Source: Statistics Canada, U.S. BEA, Scotiabank Economics.



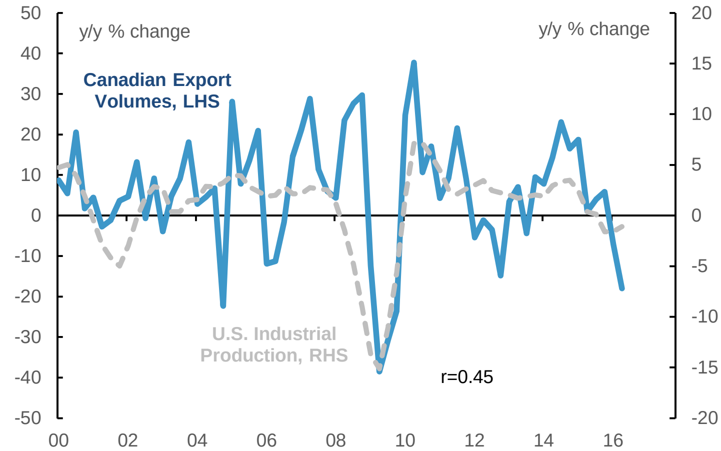
Source: U.S. Census Bureau, Scotiabank Economics.

Chart 3: Farm, fishing and intermediate food products



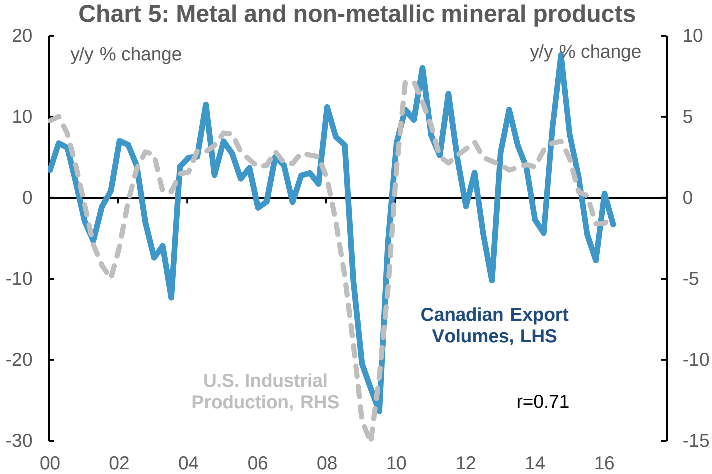
Source: Statistics Canada, U.S. Federal Reserve, Scotiabank Economics.

Chart 4: Metal ores and non-metallic minerals



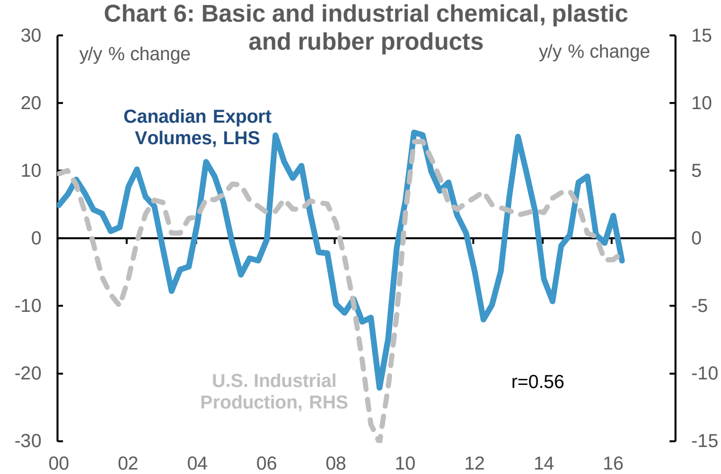
Source: Statistics Canada, U.S. Federal Reserve, Scotiabank Economics.

Chart 5: Metal and non-metallic mineral products



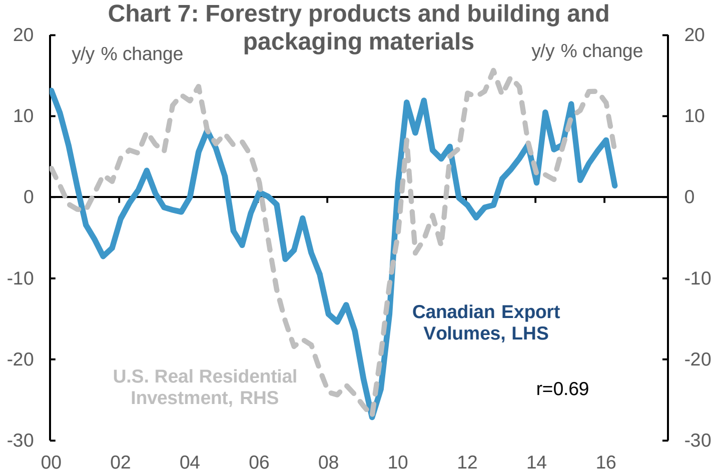
Source: Statistics Canada, U.S. Federal Reserve, Scotiabank Economics.

Chart 6: Basic and industrial chemical, plastic and rubber products



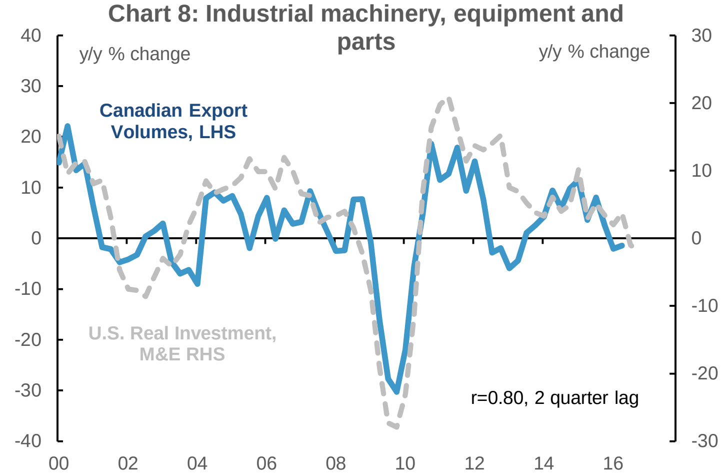
Source: Statistics Canada, U.S. Federal Reserve, Scotiabank Economics.

Chart 7: Forestry products and building and packaging materials

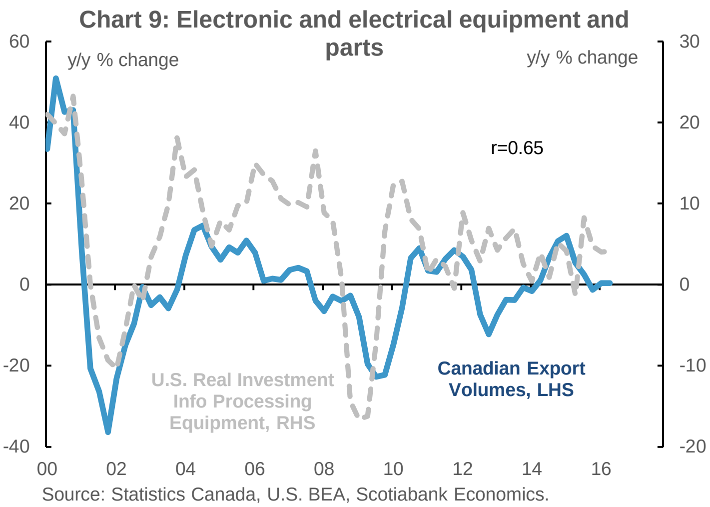


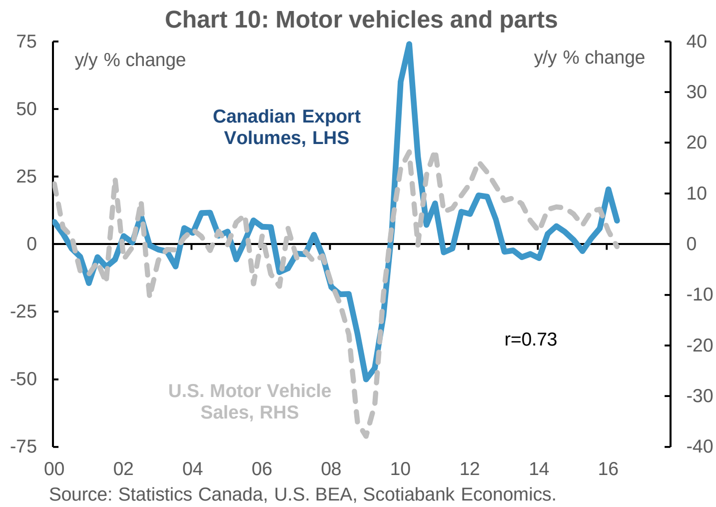
Source: Statistics Canada, BEA, Scotiabank Economics.

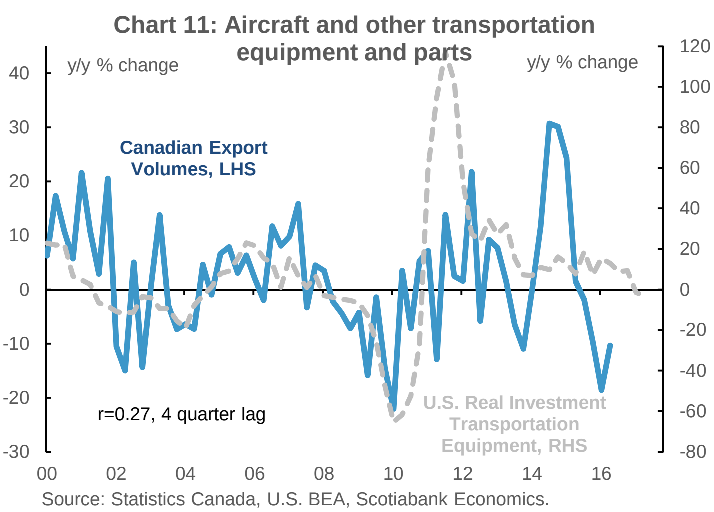
Chart 8: Industrial machinery, equipment and parts

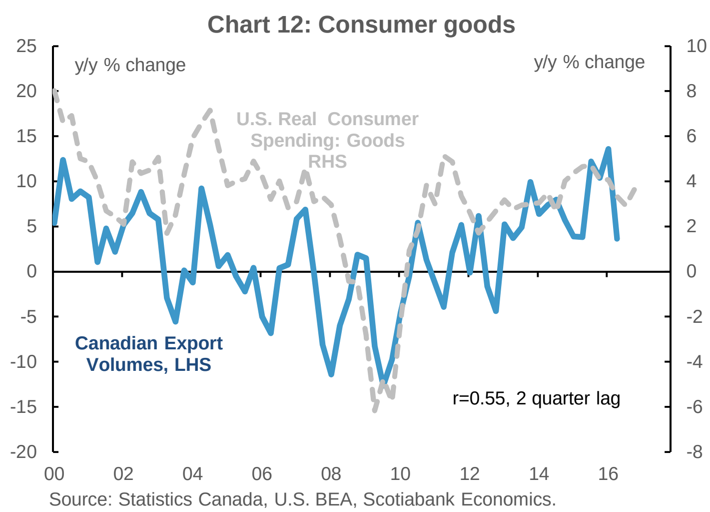


Source: Statistics Canada, U.S. BEA, Scotiabank Economics.









Canadian Export Volumes, year-to-date % change

Motor vehicles and parts	13.1
Consumer goods	5.8
Forestry products and building and packaging materials	4.7
Total non-energy goods exports	***2.1***
Farm, fishing and intermediate food products	1.8
Electronic and electrical equipment and parts	0.7
Basic and industrial chemical, plastic and rubber products	0.6
Industrial machinery, equipment and parts	-2.2
Metal and non-metallic mineral products	-2.6
Metal ores and non-metallic minerals	-11.9
Aircraft and other transportation equipment and parts	-14.9

Source: Statistics Canada, Scotiabank Economics

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