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VIEWPOINT

Observations and Insights

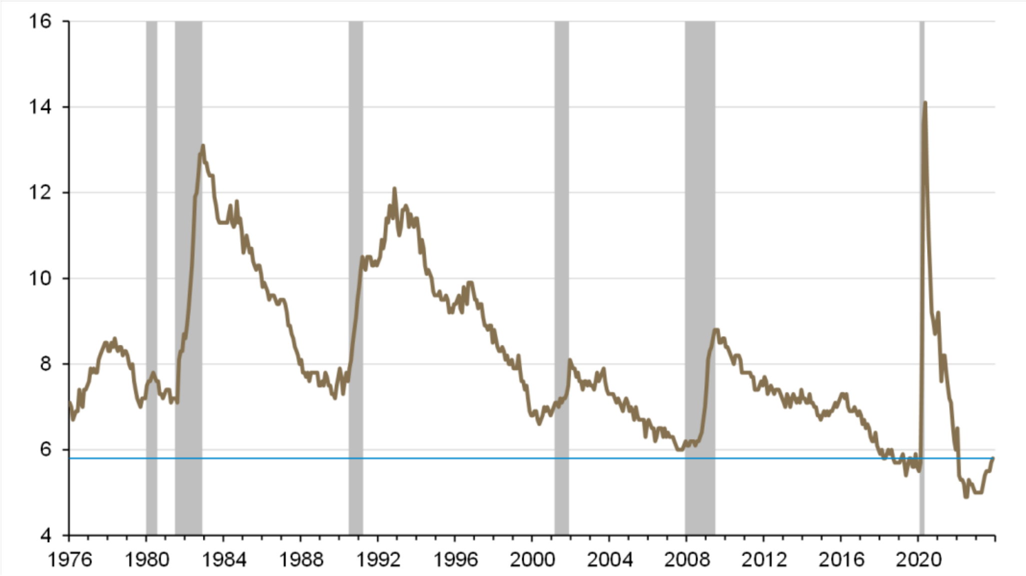
Canadian employment data -- unemployment rate increase more about surging labour supply than waning demand

In July of last year, the Canadian unemployment rate was sitting at an all-time low of just 4.9% (data since 1976), and that, combined with other indications of "excess demand" within the domestic economy, prompted the Bank of Canada to accelerate their pace of rate hikes (they raised the overnight rate target by 100bps to 2.50% on July 13, 2022[1]).

Fast forward 16 months and the policy interest rate has doubled (another 250bps worth of hikes to 5.0%) while the unemployment rate has coincidentally increased to its highest level since January 2022 at 5.8% in November.

For sure, the unemployment rate started at a historically low level and remains notably below "normal" levels (the average in non-recessionary periods since 1976 is 7.5%), but previously, when the unemployment rate has increased by this magnitude over a 16-month time span, it has been a fairly clear indicator of recessionary conditions. Not a positive indicator for the year ahead.

Unemployment rate, Canada
(percent)



Shaded regions represent periods of US recession; source: Guardian Capital based on data from Statistics Canada to November 2023

With that said, however, historically the rise in the unemployment rate has come as the result of a shift of Canadians from the ranks of the employed to the unemployed (i.e., people lost their jobs) — in previous periods where the unemployment rate has increased by 0.9 percentage points or more

[1] Bank of Canada, Bank of Canada increases policy interest rate by 100 basis points, continues quantitative tightening, July 13, 2022, https://www.bankofcanada.ca/2022/07/fad-press-release-2022-07-13/

over a 16-month span **(excluding the outlier pandemic shock)**, the average change in total employment is **-106,300** (i.e., overall employment has declined).

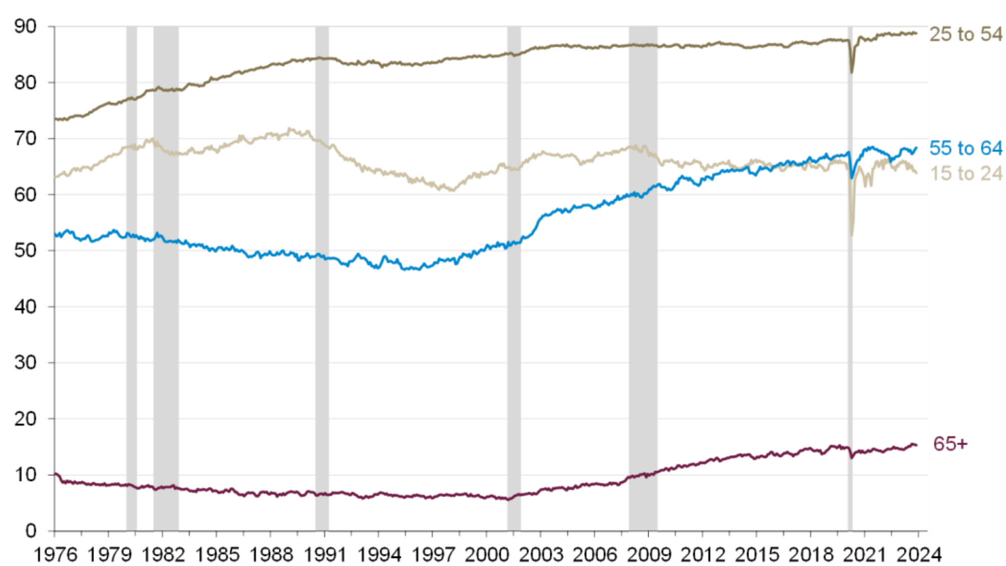
In stark contrast, the Canadian economy has added 581,400 jobs on net over the last 16 months (including the stronger-than-expected 24,900 increase in November reported today[2], which was concentrated in full-time and private sector jobs).

How can the unemployment rate rise when employment is increasing robustly (that's an average of 36,000 per month since July 2022, which is roughly double the typical pace of job gain over the pre-pandemic decade), you may ask?

The answer is the number of people looking for jobs has been growing even faster than the number of people actually finding jobs — the supply of workers in Canada has boomed with the labour force (the sum of those classified as employed and unemployed) expanding by a record 810,400 over the last 16-months.

Part of this reflects the continued recovery of labour force participation from pandemic lows — the overall participation rate (share of the population that is either employed or looking for work) is back within an arm's reach of pre-COVID levels, while the rates for those aged 25 to 54 and 55 to 64 are sitting at or near all-time highs (same goes for the 65+ crowd, while the youngest cohort has been trending lower; the greater share of the population among the low-participation 65+ crowd should be taking the overall rate lower anyway).

Labour force participation rate by age cohort, Canada
(percent)



Shaded regions represent periods of US recession; source: Guardian Capital based on data from Statistics Canada to November 2023

[2] Statistics Canada, The Daily, Labour Force Survey, November 2023, https://www150.statcan.gc.ca/n1/daily-quotidien/231201/dq231201a-eng.htm?HPA=1, December 1, 2024

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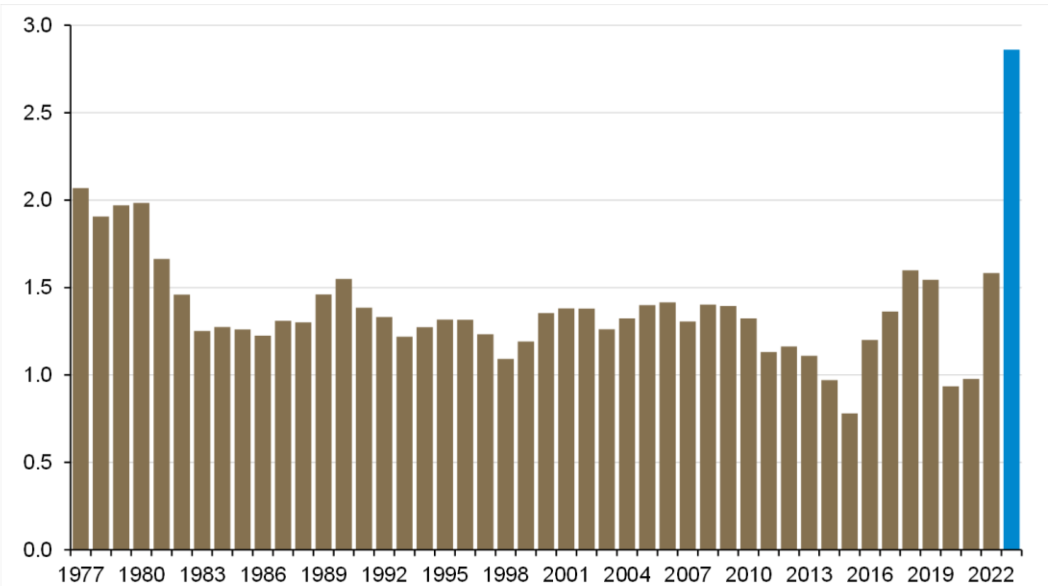
A bigger factor, however, is that the overall population of working-aged people in Canada has surged over the last year against a resumption of immigration flows — the number of people in Canada aged 15 or older has increased by 871,000 this calendar year-to-November, which is a record both in absolute terms and relative to the size of the Canadian population (+2.9% which is more than double the average of the previous 46 years).

Population aged 15+, Canada
(year-to-November percent change)



Source: Guardian Capital based on data from Statistics Canada to November 2023

The sheer volume of added people to the workforce has been a driving factor of the rise in unemployment — labour demand remains pretty solid, but it has not been able to keep up with the increase in the supply of workers. And while job vacancies remain elevated[3], today's *Labour Force Survey*[2] released from Statistics Canada noted that "*immigrants who had arrived in the previous five years faced challenges finding work related to their post-secondary credentials or work experience acquired abroad*" — this is a long-standing issue that needs to be addressed by various levels of government and licensing bodies so as to better integrate skilled workers into the Canadian economy.

This is all well and good, but why does this matter? Well, mainly because it suggests that the rising unemployment rate is not giving off the same blaringly negative signal that we have seen in previous cycles and, therefore, does not warrant the same type of policy response.

That the supply constraints in the Canadian job market are easing not through job loss is a very welcome development for policymakers. It eases pressures (and the latest *Business Outlook*

[3] Statistics Canada, The Daily, Job vacancies second quarter 2023, Job vacancies decrease for the fourth consecutive quarter, https://www150.statcan.gc.ca/n1/daily-quotidien/230919/dq230919b-eng.htm, September 19, 2023

Survey[4] from the Bank of Canada indicated that businesses were seeing fewer and less intense labour shortages), which, in turn, mitigates "cost-push" inflationary impulses and helps with the central bank's inflation focus, but is not resulting in widespread economic hardship that comes with job loss (which would carry negative implications for spending and investment).

Signs of moderating economic growth momentum, a downward trajectory in underlying inflation rates and indications of less tightness in labour markets all support the idea that the Bank of Canada is likely done with its tightening cycle (i.e., policy rates are not likely to increase further) — but the indications that activity is not collapsing, and that the unemployment rate increases are more a function of abnormally strong labour supply than falling demand, likely mean that the Bank of Canada will not be as proactive in unwinding its policy tightening as markets are currently assuming (the overnight index swaps given better-than-even odds of a rate cut in March and 100bps worth of cuts are fully priced over the next year).

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[4] Bank of Canada, Business Outlook Survey—Third Quarter of 2023, Results of the third-quarter 2023 survey, Vol. 20.3, https://www.bankofcanada.ca/2023/10/business-outlook-survey-third-quarter-of-2023/, October 16, 2023

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