



2026.06.10

Q: When is good news bad news?

A: When unexpectedly *good* short-term economic growth is potentially *bad* for long term economic growth, because it increases the risk of higher inflation and higher interest rates (both of which are headwinds to every economy).

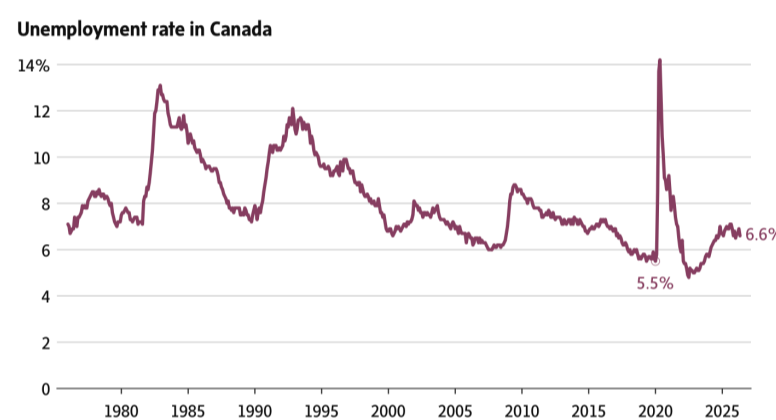
Markets sold off sharply on Friday on news that the Canadian economy roared back in May with a strong month of job creation. The labour market added 87,800 jobs in May, Statistics Canada said on Friday, easily outpacing analyst expectations of 10,000 positions added. In turn the unemployment rate fell to 6.6 per cent from 6.9 per cent in April.

Overall it appears that Canada has shaken off economic stagnation that has characterized its economy this year as it faces trade and geopolitical risks.

Short term the Bank of Canada is widely expected to take the jobs report in stride and keep its key rate at 2.25 per cent on Wednesday for a fifth consecutive hold. The central bank is being tugged in one direction by conflict in the Middle East, which is pushing up prices for gasoline and other goods, and domestic weakness that is sapping demand.

The Canadian economy finds itself in a rough patch. Gross domestic product has dropped for two consecutive quarters, sparking debate in political circles about whether the country is falling into a recession, though economists on Bay Street say recession talk is premature. Of late, there have been tentative signs of an economic pick-up. The preliminary estimate for April GDP shows a big rebound in activity.

Friday's jobs report showed that employment gains were spread across the goods and services sectors and entirely driven by full-time work, which rose by 154,000 positions. Construction set the pace with 27,000 jobs added, offsetting its previous month's loss of almost 16,000. Additional gains were seen in the information, culture and recreation sectors as well as transportation.



THE GLOBE AND MAIL, SOURCE: STATISTICS CANADA

While the central bank isn't anticipated to make any changes in the near term, investors expect the BoC to hike rates by a quarter-point by the end of the year, based on pricing in the swaps market. This puts investors at odds with most economists on Bay Street, who think the domestic economic outlook is too frail because of ongoing trade uncertainty to justify higher interest rates.

The Canada story remains the same: the economy is hanging in there despite the headwinds from trade and now energy prices. Just when it appears that Canada is crumbling amid a string of negative data points, things reverse. We've seen this story a few times in the past year. The economy isn't booming, but it isn't falling apart, either.

Stay tuned!

Thanks for reading!

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Source: Dimensional

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