

Temporary, the factory weakness should be

Manufacturing sales for October:

Latest: -0.4% (actual), +1.0% (expected)

Previous: +0.4% (revised downward from +0.5%)

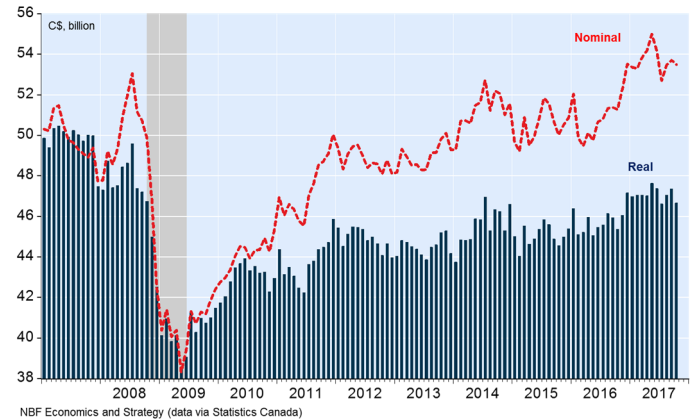
FACTS: Manufacturing shipments fell 0.4% month on month in October following two consecutive positive prints. October sales were significantly weaker than consensus expectations. Sales expanded in 13 of the 21 broad industries surveyed including petroleum/coal products (+2.2%), wood products (+3.4%), and fabricated metal products (+2.6%). However, this was not enough to offset a significant drop recorded in the transportation category (-5.0%) as slumping sales of motor vehicles dwarfed gains in aerospace. Shipments of food products (-0.3%), machinery (-1.4%) and chemical manufacturing (-1.1%) also weakened. Nationally, total manufacturing shipments improved in only 4 of the 10 Canadian provinces, with Alberta increasing 4.2%. Ontario (-2.2%), on the other hand, registered a third decline in sales in the last four months. Quebec (-0.4%) saw its first decline in 4 months. In the country as a whole total factory sales dropped 1.5% on a monthly basis if the effect of price changes are removed (top chart). Meanwhile, real inventories grew 0.7%, leading the real inventory-to-sales ratio to rise from 1.39 in September to 1.42 in October.

OPINION: While October factory shipments came in significantly below expectations, the details of the report lead us to believe that there is a positive side to the story. To begin, most of the decline registered in the month was due to a drawback in the auto sector. The decline was likely due to strikes at GM plants in Ontario during the month. This statement is reinforced by a large monthly downswing (-2.2%) in the latter province which represents 45% of the nation's manufacturing sales. Excluding transportation, sales actually grew by 0.7% in the month. We expect factory sales to pick back up following this transitory weakness. The divergence between U.S. industrial production of motor vehicles with its Canadian counterpart hints at a rebound on this side of the border (middle chart). Even then, real shipments are on track to fall during the quarter after a flat Q3. Assuming no change in November and December, inventories should have progressed 3.0% in the quarter, more than the 1.3% rise registered in Q3 (bottom chart). All in all, temporary weakness in factory sales likely restrained October GDP growth although there will be some offset from inventory accumulation.

Kyle Dahms

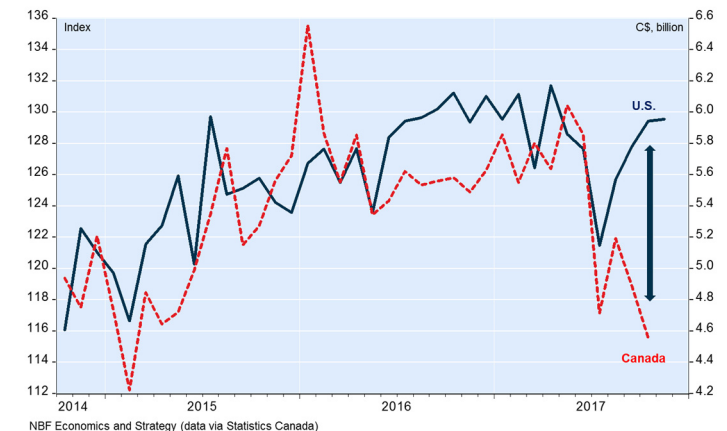
Canada: Manufacturing sales unexpectedly drop in October

Nominal vs. real factory sales. Last observation: October 2017



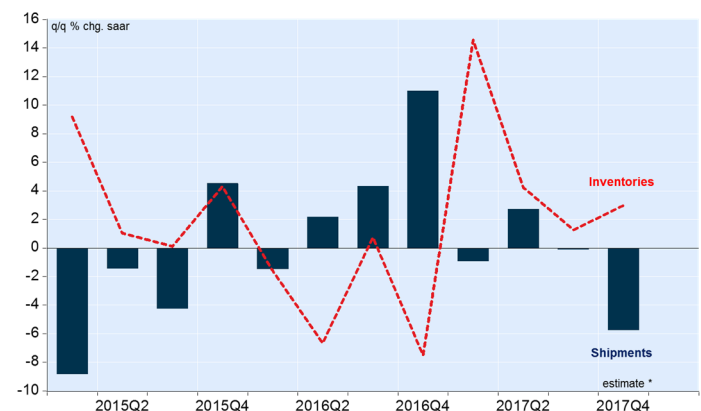
Canada: Divergence with U.S. production hints at upcoming rebound

Industrial production of motor vehicles and parts (US) and shipments of motor vehicles (Canada)



Canada: Factory output growth likely softened in Q4

Real manufacturing shipments and inventories



*Assuming no change in November and December

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