ECONOMIC RESEARCH AND STRATEGY

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Canadian January Labour Market Report – Good Quantity, Deteriorating Quality, Poor Diffusion

The Canadian labour market began the year 2024 with another mixed bag Labour Force Survey (LFS). A good quantity of jobs added, hiding concerning concentration. And quality was poor.

Total employment rose at the brisk pace of 37K in January relative to December, the best monthly performance since the solid, broad-based hiring wave of last summer. However, full-time positions dipped modestly for a second consecutive month, revealing involuntary part-time employment in this stagnant economic environment. Job vacancies are moderately lower than 6-12 months ago, mostly resulting from fewer companies intending to hire. The January LFS report exposes this soft spot: private sector employment edged up mildly for a second consecutive month in January (+7K) to reach a level only 34K above June of last year. This is clearly insufficient considering the 21.6M labour force. Meanwhile, the long streak of solid hiring in the public sector continues with the addition of 48K jobs in January, marking the best monthly performance since the Spring of 2022.

Another "mixed bag" dynamic in January relates to the employment and unemployment rates, although the longer-term trend unambiguously points to deteriorating conditions. The employment rate has been consistently falling during the last year as job creation cannot keep up with sizzling population growth. The employment rate reached its lowest level in January (61.6%) since the economy was in recovery mode in 2021 after the worst of the pandemic. Unemployment rose modestly from a trough of 5% in the Spring of 2023 to 5.8% in December. It suddenly, and surprisingly, tracked back in January to 5.7%. Growth in the labour force is still positive but has faltered significantly during the last two months, a growing concern as Canadians may actively be looking into fewer job opportunities given the lasting economic stagnation. Since there are fewer job postings and opportunities, we forecast unemployment to move up in the coming months, reaching a peak of 6.5% by mid-year.

In addition, the healthy 37K net increase in total employment comes from only 6 industries (out of 16) registering gains. This concentration, or poor diffusion, contrasts with the Winter of 2023 when workers were added in most sectors. After fewer holiday seasonal jobs contributed to a soft 2023 year-end, the trade sector added 31K workers in January relative to the previous month. The two other private industries that registered gains in January were: 1-finance, insurance and real estate services; 2-transportation and warehousing. A modest pullback in employment was recorded in all goods-related sectors, including the construction and manufacturing sectors. Losses were unfortunately heavier in accommodation & food as well as in information, culture and recreation sectors.

Market watchers and central bankers have repeatedly stated that wage growth is running too hot. This situation has unsurprisingly not changed in January: LFS average hourly earnings year-over-year growth reached 5.3%. Average hourly earnings from the payroll-based SEPH report, a more reliable wage measure less volatile than the LFS and consistent with what governments collect in terms of taxation revenues, has been running on a year-over-year basis closer to 3.5%-4% lately. To explain this rapid wage inflation in Canada, we can infer valuable research from the Federal Reserve of Cleveland. It shows solid wage growth mostly reflects the pass-through effects of high inflation rather than low unemployment. In fact, in the deliberations of the January policy meeting, BoC officials expressed a similar view and added a crucial twist: "*Members viewed past wage growth as largely reflecting catch-up with the cost of living, and that wage growth was not a problem for inflation if coupled with productivity growth"*. There is the rub. Canada is well known to have a poor track record in terms of productivity gains for several reasons, the latest one being slower AI adoption relative to the U.S. As a result, we see a growing risk that Canadian CPI inflation will moderate very slowly in the months and quarters ahead. The BoC may not be able to start reducing its policy rate next June as we initially projected two months ago.

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