

Economist sees signs strong rebound taking root

By Alia McMullen, Financial Post May 11, 2009

Just when it appeared the tide of popular opinion had turned against the chance of a resolute rebound, some economists have begun to return to the belief Canada is headed for a strong recovery buoyed by the need to replenish the massive drawdown in inventories.

As the pace of recession slows and the financial crisis eases, economists have begun to spread before them an assortment of letters — from V to L, W to U — in an effort to piece together the shape of the inevitable recovery.

The length of the recession in the United States has already all-but-ruled out the short and sharp dip and recovery of the V-shaped recession, and many economists have begun to lean toward the U-shaped theory — a protracted recession, in this case caused by the financial crisis and large debt overhang, followed by strong growth. This theory has largely flowed through to expectations for Canada.

But not all are convinced the array of letters, which also include the L-shaped recession indicative of years of stagnant growth and the W-shaped scenario of a double dip recession, will adequately represent this recovery, particularly in Canada's case. Some have put forth modified scenarios such as 'the hook' or 'the spoon' to depict a recovery that falls somewhere between a U and an L.

Then there's the possibility that Canada, boosted by improved investor sentiment, commodity prices and the likely need to rebuild inventories when demand returns, will recover much faster than expected.

Stéfane Marion, the chief economist and strategist at National Bank Financial Group said last week's surprise rise in Canadian employment was the latest in a line of "green shoots" that suggested an increasing possibility that growth could return to Canada as soon as the second quarter of this year.

"To the same extent that we were all surprised at the speed of which everything imploded in the fourth and first quarters, it is in the realm of possibility that you can have a more potent rebound as soon as the second quarter because of the credit markets that are normalizing," he said.

While Mr. Marion said he would watch one more month of economic data carefully before changing his official projection of an annualized drop of 0.9% in the second quarter, he said there was a good chance Canada's recession would be shorter than that of the United States. This could result in Canada experiencing a small v-shaped scenario, where the recovery is sharp, but less so than the traditional bounce backs of previous downturns.

In the U.S., the recession appears to be forming a U shape on the charts, particularly in light of the White House's upgraded outlook for growth, which reflects a strong return to growth. The White House said Monday

it now expects the U.S. economy to expand by an annualized 3.5% in the fourth quarter of this year, a figure which is almost double the median expectation of U.S. economists. It said this pace of growth would continue throughout 2010.

Mark Chandler, a strategist at RBC Capital Markets, said the seeds of recovery could receive an additional boost from the rally in equity markets, which is now in its 10th week, because higher stock prices would likely help repair household worth.

“Rather than thinking of the economy driving equities, let’s think about what happens if equities in and of themselves manage to hold on to these gains or extend it, then that goes some way to repairing the psyche of consumers,” he said.