Growing Signs of a Canadian Recession Tell Investors to Boost Their Exposure to Defensive Stocks

Description

Despite the Bank of Canada's optimism regarding the outlook for Canada's economy, the data continues to point to a far darker outlook. Recent economic data from Statistics Canada showed that Canada's GDP for April 2015 had contracted for the fourth straight month, with signs that the economy can only get worse.

Now what?

The sharp collapse in oil prices has shaken Canada's economy as the energy industry slashes investments and savagely cuts costs in order to shore up their balance sheets and preserve cash flow in a harsh operating environment.

Initially, it was thought that only the oil patch would bear the majority of the brunt of this economic shock, with the Bank of Canada expecting a lower loonie to drive an uptick in manufacturing activity and exports, but this hasn't occurred. Not only did first-quarter 2015 GDP contract by 0.6%, but April 2015 GDP shrunk by 10 basis points, leaving Canada on track for a second consecutive quarter of negative growth, which is technically a recession.

There are a range of reasons for this.

Key among them is the significant focus that federal and provincial governments placed on boosting investments in the patch during the boom years, which boosted the energy industry's share of GDP to over 6%. Alberta became the third-largest province by contribution to GDP, making it a contributor to national economic growth.

As a result, the oil shock has caused up to $59 billion in oil projects to be cancelled, put on hold, or placed under review. It has also triggered savage cost cutting by energy companies, with many slashing outsourced services and head counts, all of which will have a tremendous impact on the broader economy.

This is causing business and consumer confidence to wane and, along with declining wage growth, is causing spending to fall as households batten down the hatches for tougher times ahead. Now the greatest fear is that this may spread to Canada's financial system, with households coming under greater financial pressure because of near-record debt and declining real wages.

This has made a number of Canada's domestically focused banks vulnerable. **Canadian Western Bank** (TSX:CWB) is shaping up to be among the hardest hit. Whereas the Big Five have to yet to experience any real impact on their balance sheets, Canadian Western had its impaired commercial loans more than triple in value year over year by the end of the second-quarter 2015.

So what?

There is certainly no guarantee that Canada will slip into recession, but there are worrying signs that one is not far off. This makes it imperative for investors to be mindful of weather-proofing their portfolios, and the best way to do so is with defensive stocks.

Some of the best defensive industries include utilities and infrastructure with companies like **Canadian Utilities Ltd.** (TSX:CU) and **Brookfield Infrastructure Partners L.P.** (TSX:BIP.UN)(NYSE:BIP), which provide products and services with virtually unchanging demand. They also operate in monopolistic and highly regulated industries with wide economic moats that help to protect their competitive advantage and long-term earnings growth. This allows them to pay sustainable, steadily growing dividends juicy yields of 3% and 5%, respectively, rewarding investors for their patience as they wait for the economy to improve.

CATEGORY

1. Dividend Stocks
2. Investing

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2. TSX:BIP.UN (Brookfield Infrastructure Partners L.P.)
3. TSX:CU (Canadian Utilities Limited)

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Author
mattdsmith