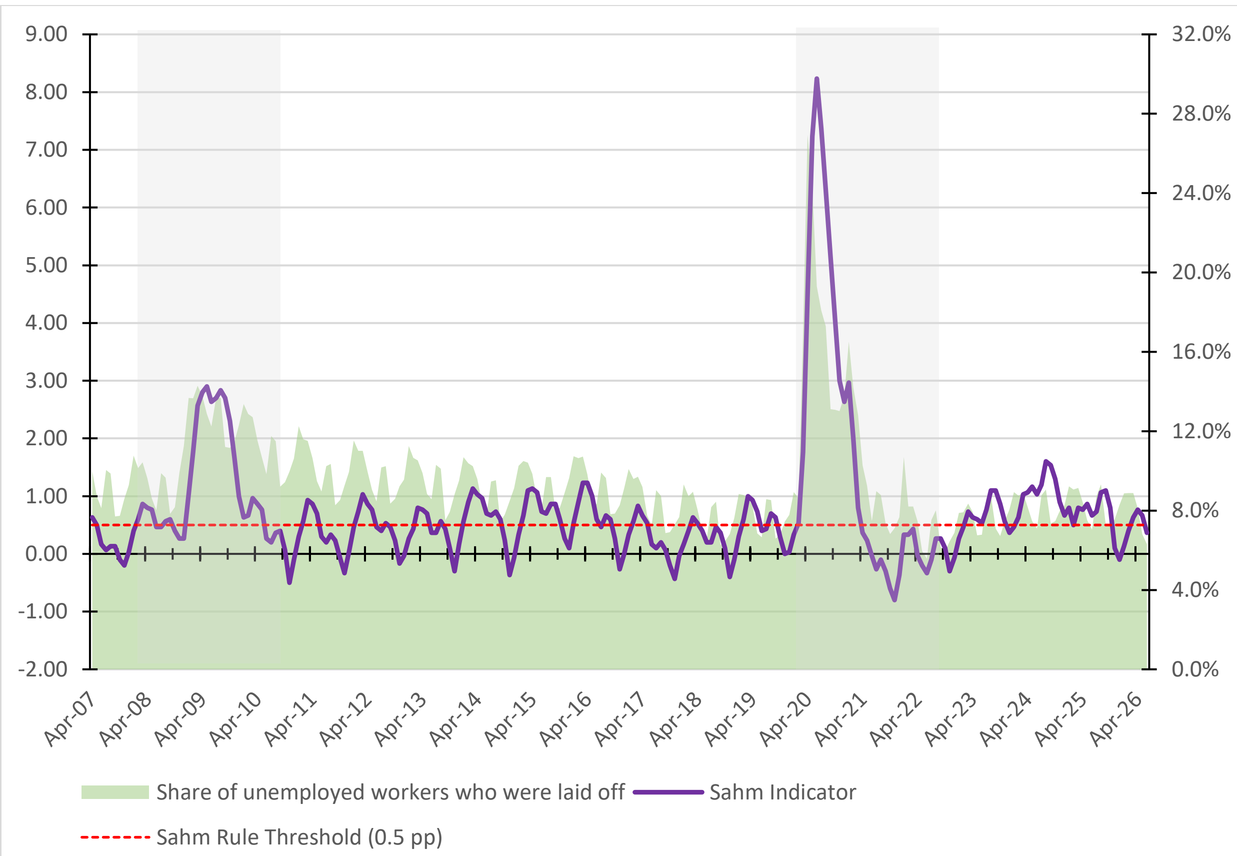
The Sahm Signal in Canada

The Sahm Rule, developed by U.S. economist Claudia Sahm, is designed to identify the early stages of recession by watching how quickly unemployment rises. The logic is that when the three-month average unemployment rate rises sharply from its recent low, the labour market has usually weakened enough to signal that the broader economy is in trouble. In the United States, the rule has a strong historical record. Given the number of recent news articles about rising unemployment in Canada, I thought a Sahm-style indicator for Canada was worth a closer look.

A Sahm-style measure for Canada shows that the unemployment rate has risen materially from its post-pandemic low. The signal first became more concerning in 2023, strengthened through 2024, and remained elevated into 2025 and early 2026. On its own, that would suggest a labour market moving towards recessionary territory. The indicator peaked at about 1.6 percentage points in August 2024, *well above the usual 0.5 percentage point threshold associated with rising recession risk in the US*. By June 2026, however, it came down to about 0.4 percentage points.
But the Canadian story is more complicated than the headline signal suggests.

The key distinction is between unemployment caused by layoffs and unemployment caused by weak labour absorption. In a classic downturn, unemployment rises because firms cut workers. Layoffs surge, job losses spread, and households feel the shock quickly. That is what the data showed during the Great Recession (2008-09) and, in much more extreme form, during the first months of COVID-19 (2020).

Sahm-Style Indicator and Laid-off Workers as a Share of the Unemployed, Canada
April 2007 to June 2026



Source: Statistics Canada, Table 14-10-0017-01 & TDP EIU

In May 2009, Canada's Sahm-style indicator reached roughly 2.9 percentage points. At the same time, laid-off workers accounted for about 12.9% of the unemployed. In June 2020, the indicator exploded to 8.2%, while the laid-off share rose to nearly 19.3%. Those were unmistakable labour-market shocks, driven by direct job losses.

Canada's Sahm-style indicator has again moved into warning territory, but the share of unemployed workers who report being laid off has not risen in the same way. In August 2024, when the indicator reached its recent peak, laid-off workers represented only about 9.1% of the unemployed. In June 2026, that share was around 6.3%.

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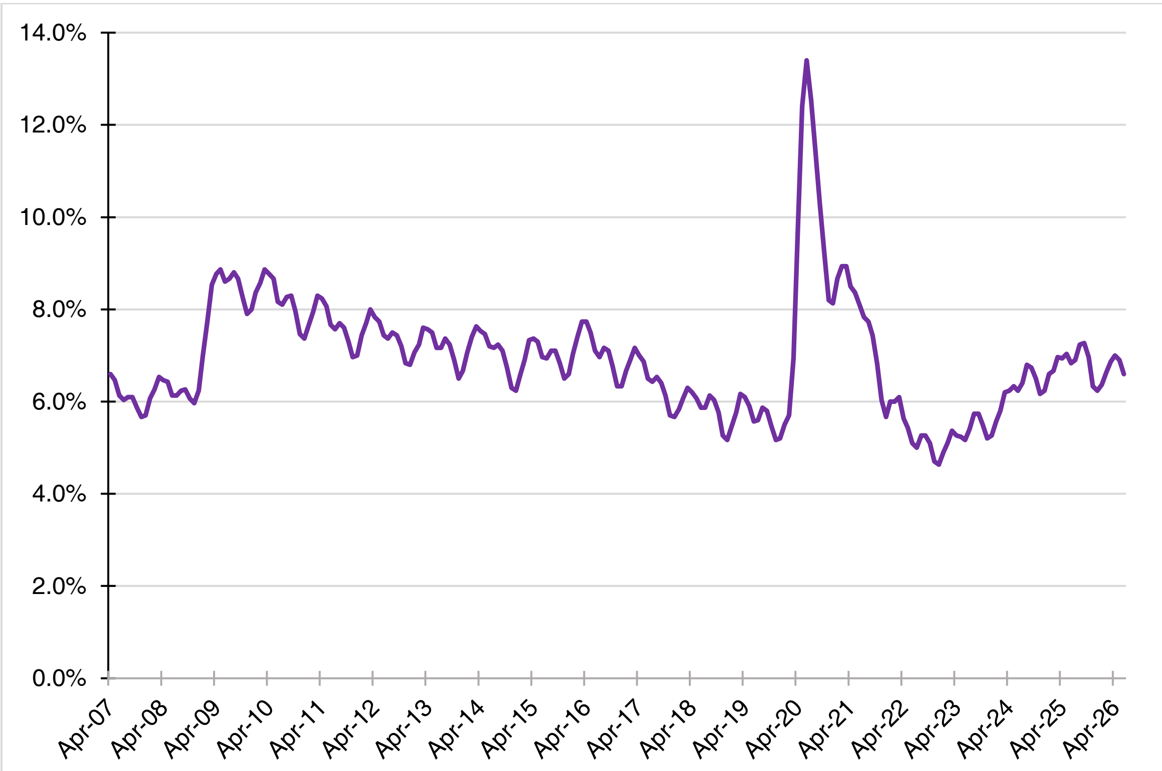
Canada's unemployment rate has risen because job creation has struggled to keep pace with the number of people available for work. The employment rate has weakened, participation has softened, and the economy appears to be absorbing workers less effectively than it did during the immediate post-pandemic recovery. This is not a mass-layoff recession story; it is a hiring, absorption, and labour-market slack story.

The next few months may reinforce that point. July and August often bring more students and recent graduates into the labour force, many looking for summer or early-career work at the same time. If hiring does not keep pace, the unemployment rate could move higher even without a major increase in layoffs.

Unemployment Rate, Three-month Moving Average, Canada
April 2007 to June 2026



Source: Statistics Canada, Table 14-10-0017-01 & TDP EIU

A layoff-driven downturn points to collapsing demand and firms actively shedding labour. An absorption-driven slowdown can be quieter but still damaging. New entrants struggle to find work. Recent graduates face fewer openings. Newcomers encounter a softer hiring environment. Workers who lose jobs may take longer to find employment. The unemployment rate rises not because everyone is being fired, but because fewer people are being pulled into employment quickly enough.

This makes the Canadian Sahm-style indicator useful for assessing labour-market conditions, but not as a clear indicator of an impending recession. The absence of a large layoff spike is reassuring, but the sustained rise in unemployment is still worrying. A labour market does not need a wave of layoffs to weaken; it can also weaken through a slower and more painful loss of momentum.