

Canadian economic overview



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Canadian economy

Regional divisions in the Canadian economy remained intact throughout 2007. The west continued to benefit from high energy and commodity prices while the east struggled with the compounding effect of the Canadian dollar's steady rise on the energy intensive manufacturing base. Similar to 2006, domestic demand, not export growth, supported the country's economic performance. The gap between west and east is expected to narrow in 2008 as the country as a whole faces a weaker overall outlook on the basis of meager international trade prospects.

The Canadian dollar reached parity for the first time since 1976. It also recorded an unprecedented high of \$1.10 against the US dollar in November 2007 before receding back down to just around the parity mark at the end of the year. This remarkable ride saw a 24% increase in the value of the Canadian currency during 2007. The question remains, how long will this wild ride continue? The rise in currency has benefited consumers. However, it has put many manufacturers at a disadvantage against those in the US. Canadian manufacturers are also feeling a pinch from a slowdown in US economic growth, softened demand for

Canadian products and competition from lower cost offshore markets.

Citing the ongoing problems in the credit markets and the decelerating US economy as downside risks to Canada's growth prospects, in December 2007 the Bank of Canada cut its target overnight lending rate by 25 basis points, to 4.25%. It is likely that further rate cuts will be forthcoming in 2008.

Canada's unemployment rate hit a new 33-year low of 5.8% in October 2007 and finished the year at 5.9%. Employment increased by 2.2% or 370,000 jobs in 2007, marking the fifteenth year of consecutive employment increases. This growth far exceeded that of the US which recorded 0.2% employment growth for the same period. The only sector since 2002 to experience employment decline has been the manufacturing sector. It has lost almost 350,000 jobs in the past five years. Hourly wages continue to feel upward pressure as a result of tight labour market conditions, particularly in the western provinces.

Corporate profits rose throughout 2007 to a record high of \$67 billion in the third quarter. Conditions are conducive for continued business investment with the stronger dollar giving businesses increased purchasing power, reducing the costs of imported machinery and resulting in increased investment in capital equipment and machinery.

While there are clear signs of a correction in the US housing market, the Canadian market appears to be on much better footing. The Canadian housing market has boomed in recent years with high start levels, strong resale activity and price gains in most markets. What is generally lacking in Canada is the speculation and excess development that has been evident in many US markets. However, the potential for a cooling in the housing market and dampening of house values cannot be ruled out.

Low mortgage rates and strong employment and income growth continue to support the high level of housing starts recorded in Canada. Housing starts in 2007 remained on pace with 2006 at 227,500. Housing starts will trend lower in 2008 but still reach 214,000 units, marking the seventh consecutive year of over 200,000 units recorded. Resale activity hit a record 521,100 units in 2007 and prices continued to feel upward pressure, particularly in the western provinces. Resale activity will cool in 2008, but still reach over 500,000 units sold.

All told, the Canadian economy will not be immune to slowing economic conditions in 2008 despite the strength of its commodity market. With a moderating world economic forecast for the short term, it is anticipated that raw material prices will also see a decline in 2008. The bright spot remains the strong consumer fundamentals, with retail sales up 5.4% over last year. An additional 1% decline in the GST in January 2008 should also have beneficial effects on consumer spending. The strength of Canada's fiscal situation is also a key characteristic that will help the country cope with any impending slowdown.

British Columbia

British Columbia (BC) continues to enjoy a construction boom and robust consumer confidence with solid employment gains and strong housing activity. The Canadian dollar and US housing slowdown are a drag on the forestry sector. However, the rest of the economy is healthy, growing by roughly 3.3% in 2007 and forecast to grow by about the same in 2008.

Competition for labour is strong amongst the western provinces because of the volume of large-scale projects underway. Total construction output growth registered an impressive 8.9% in 2007. It is expected to moderate to 4.8% in 2008. Job creation remains strong in BC with more than 72,000 new jobs created and an unemployment rate of 4.2% at the end of 2007. Employment growth and consumer confidence continued to fuel

retail sales in the province, up 7% from 2006. Housing starts rose 3.8% in 2007, coming in at roughly 37,800 units. Housing demand is expected to cool in 2008 yet remain healthy.

Alberta

Alberta was surpassed temporarily by Newfoundland and Labrador for the economic growth leader in 2007. Nevertheless, Alberta is forecast to be back in the lead for 2008. Development and investment in the oil sands, and spin-off investment throughout the province, are driving much of the growth. The economy expanded by roughly 4.8% in 2007 and is expected to expand by 4.7% in 2008.

Labour continues to be a problem for Alberta given the sheer volume of construction projects on the go, and competition from other western provinces for both skilled and unskilled labour. Alberta boasts the lowest unemployment rate in the country at 3.2%, with 82,000 new jobs created in 2007. The extreme labour shortage has employers attempting to recruit prospective employees from across the country, which in turn is impacting labour markets in other provinces.

The construction sector is booming in Alberta. Construction output growth increased by 2.1% in 2007. With over \$169 billion in announced, planned, under construction or recently completed projects related to the oil and gas industry and strong non-residential construction in both Calgary and Edmonton, increasing construction costs are becoming a concern and could put a damper on future capital projects.

The housing market in Alberta remains solid, fuelled by strong employment and population growth. Rapid price growth has resulted in housing starts decreasing 2.5% in 2007, coming in at roughly 47,750 units. Starts will decrease an additional 12% in 2008. For the first time in 14 years, Edmonton surpassed Calgary in housing start activity. The resale market remains strong, however, price pressures are evident.

Saskatchewan

Saskatchewan experienced a boom in 2007 led by a strong mining sector and a rebound in potash production. The economy expanded by 3.7% in 2007, the strongest growth it has seen in 10 years, and is projected to expand by 3.3% in 2008.

Both non-residential and residential investments are boosting construction activity in Saskatchewan. Non-residential construction output increased by 4.6% in 2007 and is expected to grow by 4.3% in 2008. Residential investment remained strong in 2007, with 6,000 new units representing a 61% increase over the previous year. The resale market is also strong with a 33% increase in sales for 2007. As a result, price growth is strong, with prices increasing 29% over 2006.

Similar to BC, Saskatchewan is competing with Alberta for labour. Saskatchewan has a 4% unemployment rate with 1,600 jobs created in 2007. This is one of the lowest unemployment rates recorded in the province in the last 25 years.

Saskatchewan is experiencing consecutive quarters of positive in-migration for the first time in 23 years, which is boosting the demand for housing as well as retail activity. Retail sales were up 12.1% over the previous year, the fastest growth of all the provinces.

Manitoba

Manitoba recorded solid economic expansion in 2007, fuelled by strength in the mining and utilities industries. The economy expanded by 3.4% and is forecast to grow by 3% in 2008.

Large-scale investment projects are boosting Manitoba's economic outlook. Overall, the construction sector grew by 8.9% in 2007. Housing starts hit a 20-year high of 5,750 units in 2007, an increase of 14.4% over the previous year. Activity will cool off slightly in 2008 with 5,600 units expected.

Manitoba recorded a 4.2% unemployment rate with approximately 11,000 new jobs created in 2007. Solid employment also supported retail sales growth. Retail sales increased 8.1% for the year.

Ontario

The Ontario economy continues to be impacted by the appreciation of the Canadian dollar, softened US demand and higher commodity prices. Export growth remains limited and it is expected that this trend will continue throughout 2008. The saving grace is domestic demand, which helped the economy expand by 1.8% in 2007. The economy is expected to post a more balanced performance in 2008 of 2.3%.

Ontario's employment's growth registered a meagre 1.4% in 2007 with notable job losses in the manufacturing sector. The unemployment rate at the end of 2007 was 6.5%, with over 88,000 new jobs created. Retail sales increased 4.5% year over year in 2007.

Housing starts declined 7.8% to an estimated 67,700 units and are expected to increase slightly in 2008 to 68,175 units. Housing starts remain above historical averages in the province, bolstered by strong immigration levels. The resale market is also strong with a record 214,000 sales in 2007. Prices are running ahead of inflation with a 6.2% increase in 2007.

Non-residential investment increased by 3.5% in 2007. However, it is forecast to decrease by 1.3% in 2008 as work on several projects begins to wind down.

Québec

The Québec economy is facing similar challenges in its manufacturing and export sectors as seen in Ontario. Overall, the economy expanded by 1.9% in 2007 and is expected to improve by 2.5% in 2008. The domestic economy provided some relief to the overall economic picture as decent wage growth and fiscal relief bolstered after-tax income and consumer spending.

The labour market continued to improve with service sector job growth offsetting losses to the manufacturing sector. At the end of 2007 the unemployment rate in the province was a record low 7%, with roughly 92,000 jobs created overall.

The housing market proved resilient with starts increasing 9.4% in 2007 to 52,400 units. Starts are expected to moderate in 2008 to 48,410 units. The resale market is also well sustained by the economic conditions in the province.

The non-residential construction industry remains active due to publicly funded capital projects and several mine expansions. It is expected that over the next five years the provincial government will invest \$30 billion in public transportation, roads, schools and hospitals. Hydro Québec has several major construction projects underway, including plans to spend \$1 billion to improve the province's connection to the Ontario Hydro grid.

New Brunswick

Supported by solid non-residential investment, New Brunswick's economy expanded by 2.4% in 2007. Projects, such as the \$1.4 billion Point Lepreau nuclear plant and the \$750 million Canaport LNG project, continue to provide economic benefit and strengthen New Brunswick's position as an energy hub for Atlantic Canada. The strong Canadian dollar and soft demand from the US will continue to have an impact on the manufacturing sector. As such, the projected economic growth for 2008 is 2%.

The jobless rate reached a low of 7.8% in 2007 with over 12,000 new jobs created. The employment picture for 2008 is forecast to be similar with the unemployment rate remaining in the 7.6% range.

Housing starts remained flat in 2007 at 4,025 new units. It is anticipated that housing starts will decrease 7.4% in 2008 to 3,725 units. Retail sales increased by 6.8% this past year.

Nova Scotia

Supported by the services sector, the economy grew by 2.3% in 2007. It is expected to record a similar performance in 2008. The manufacturing, forestry and utility industries continue to struggle with weak market conditions. The energy sector, however, remains a bright spot. A lack of major new construction projects resulted in contraction in the energy sector in 2007 but a pick up is expected in 2008 with the construction of a \$4.5 billion liquefied natural gas terminal.

With the creation of 6,600 new jobs, employment grew 1.5% in 2007. After hitting a 30-year low in 2006, the unemployment rate at the end of 2007 increased slightly to 7.7%. Consumers remain upbeat and continue to spend with retail sales up 5.4% over last year.

Housing starts declined 4% in 2007, with roughly 4,700 total new units. Housing starts are expected to decline again in 2008 to roughly 4,525 units.

Prince Edward Island

Like many of the provinces, decreasing manufacturing shipments and faltering trade are a drag on the economy of Prince Edward Island. The economy expanded by 2.2% in 2007. Supported by the services sector, the same level of growth is projected for 2008. Tourism continues to weather the strength of the Canadian dollar with increased hotel occupancy levels in 2007. The same is forecast for 2008.

While the unemployment rate reached a 29-year low in the fall of 2007, employment growth was flat year over year at 0.7%. Consumer confidence remains on solid footing, with retail sales up 10.3% over the previous year.

Several mega-projects are coming to a close that will see investment spending and construction output begin to slow. Housing starts are on a declining trend, down 7.8% in 2007 to 680 units. It is expected that starts will decline further in 2008.

Newfoundland and Labrador

Rebounding offshore mining output placed Newfoundland and Labrador temporarily in the top spot for economic growth in 2007, with the economy expanding by a robust 5.7%. However, with no large-scale construction projects expected over the next few years, economic growth will remain muted over the medium term.

At 12.4%, the province continues to have the highest unemployment rate in the country. Unemployment levels are expected to remain high over the near term. Despite high unemployment, retail sales remained solid, up 9.3% over 2006.

The domestic economy of the province remains healthy. Housing starts increased 4.1% in 2007 with roughly 2,325 new units. Flat employment and continued out-migration point to a further easing of housing starts in 2008.

