



Weekly economic Briefing

volume 12 . number 45 . November 10, 2006

Higher economic growth in B.C.

Newly released data from Statistics Canada on provincial economic activity show a stronger B.C. economy during 2002 to 2005 than previously estimated. Top-line real GDP growth is higher for each year.

The largest revision affected 2004, with real GDP growth rising 0.6 percentage points to 4.6% from 4.0% previously. Growth in 2005 is revised up by 0.2 points to 3.7% from 3.5%. Most of the 2004 and 2005 revisions were centred in the trade accounts, with slightly higher exports and noticeably lower imports creating an improvement in the net trade balance.

Large upward revisions to labour income in 2004 and 2005 pushed up personal disposable income by similar amounts. Labour income in 2004 is 1.8% or \$1.39 billion higher than previously estimated, while the 2005 figure is 2.0% or \$1.65 billion higher. Personal disposable income is up 1.4% or \$1.30 billion and 1.8% or \$1.74 billion in 2004 and 2005, respectively. Corporate profits before tax were revised slightly downward in both years.

There were minor revisions to the GDP industry accounts. The all-industries figure changed negligibly. The most notable revision occurred in the manufacturing sector, which was revised downward by about \$900 million (1997 chained dollars) or 0.6% in each of 2004 and 2005. Upward revisions of \$300 million or 0.5% in the information/cultural industries provided some offset in each of those years.

One piece of data that potentially portends some weakness in 2006 is the substantially higher level of inventories in 2005 than initially estimated. The new inventory figure for 2005 is \$1,737 million (chained 1997 dollars) compared to \$1,053 million in the first estimate. If inventories are too high relative to sales, either producers will cut back on production or distributors will cut back on purchases.

B.C. Real GDP Growth Estimates



Source: Statistics Canada.

These new data on B.C.'s economic performance from 2002 through 2005 substantiates and reinforces its strong growth phase. A particular positive is the considerable upward revision to labour income, which helps explain the strong growth in consumer spending. Overall, the higher growth figures will tend to lift 2006 and 2007 forecasts, since there is more upward momentum to be incorporated into models and expectations than before.

Non-residential building permits dip temporarily

Non-residential building activity is a growing force in B.C.'s construction industry. Permits issued for commercial, industrial, and institutional-government buildings have grown at a 9.4% pace through to September, following a 55% surge in 2005.

In September, non-residential building permits fell 29% from August to \$226.2 million seasonally adjusted. Industrial permits countered the trend, with an 11% gain from August to \$43.3 million seasonally adjusted.

September's provincial decline can be traced to the Vancouver metropolitan area, where non-residential permits fell 45% to \$145.3 million seasonally adjusted in September from \$266.3 million in August. However, industrial permits climbed 58% to \$30.2 million.

Large monthly swings in non-residential permits are common, owing to the large nature of buildings such as hotels, offices, hospitals, factories and stores, which seasonal adjustment cannot smooth out.

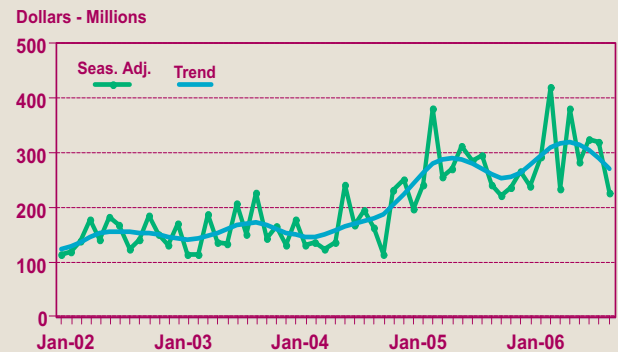
Higher construction costs are inflating building permit values, so this year's 9.4% gain probably means little or no rise when adjusted for inflation. The year-over-year increase in non-residential building construction was 9.5% in the second quarter of 2006.

Nonetheless, the underlying trend will remain upward since there are many building projects on the horizon. Olympic venue construction is still in the early stages. The industrial market in the Lower Mainland is tight and more investment is expected. Also, the office market is tightening, as is the retail market. The total value of non-residential permits is forecast at \$3.6 billion during 2006, rising to \$4.2 billion in 2007.

Modest rise in October housing starts

A modest increase in October seasonally adjusted housing starts in urban B.C. did not reverse the short-term trend decline of the past eight months. Seasonally adjusted total housing starts came in at 2,681 units in October compared to 2,405 in September. Both single-detached and multi-unit seasonally adjusted starts rose in October, with the larger gain seen in multi-units.

B.C. Non-residential Building Permits, Seasonally Adjusted, Monthly



Source: Statistics Canada.

Latest: September

Year-to-date housing starts are up 6% in urban B.C. The Vancouver metropolitan area is even with last year, but Victoria is up 36%, Abbotsford is up 33%, and the remaining urban centres are up 9%.

It is unclear whether the trend decline will continue, and thus make last February the high point in housing construction. A significant resurgence in starts during the next three to six months would turn up the trend and potentially set a new high. But with unit sales on a trend decline for the past year, a reversal there is necessary before a turnaround can occur in housing starts. Sales data for October were stronger than in September, and November appears to be holding up, according to anecdotal information. There is a fair possibility that sales, and ultimately starts, could turn upward.

Our housing starts forecast for 2006 is revised downward to 37,000 units, with a slight drop-off in 2007 to 36,600 units. Most of the moderate supply adjustment is expected in the Vancouver metro area, since sales there have dropped more than in other regions and high land costs are squeezing builders' profit margins. Housing starts in lower-cost markets are expected to rise in 2007.

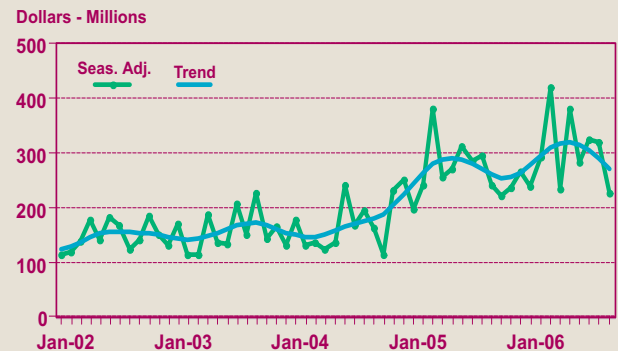
Merchandise exports little changed

Seasonally adjusted merchandise exports from B.C. edged up to \$2.758 billion in September from \$2.698 billion in August, just below the average of the prior eight months. For the year so far, goods exports are barely higher than in the same period of 2005, rising by 1.3% to \$25.4 billion. Last year as a whole saw a 10.2% gain.

Many cross-currents exist, with prices and volume rising in some export sectors but falling in others. Forestry product exports are declining due to lower lumber and panel board prices, a result of lower U.S. housing starts. Seasonally adjusted forestry exports declined to \$1.036 billion in September, the lowest level this year. Energy product exports, mainly coal and natural gas, are also lower this year, mostly reflecting the large drop in natural gas prices this year. Coal prices are off this year by a small amount, although B.C.'s coal production is down by 20%.

Industrial goods exports are rising, as are machinery and equipment exports and consumer goods exports. Industrial goods, which for B.C. are mainly metal ores and concentrates, are up 15% to \$4.425 billion so far this year, largely boosted by higher prices for copper, molybdenum, and zinc. Machinery and equipment exports are up 4% to \$3.132 billion this year and are a longer-term growth story as well. Consumer goods exports are a small segment in B.C., made up of apparel and footwear exports and various miscellaneous goods. These exports are up almost 6% this year, but their longer-term trend ranges from flat to down.

B.C. Non-residential Building Permits, Seasonally Adjusted, Monthly



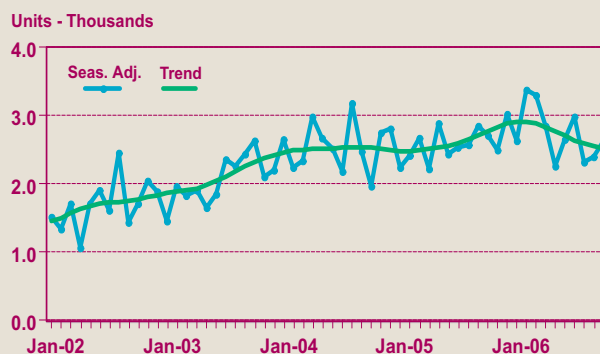
Source: Statistics Canada.

Latest: September

The outlook for B.C. merchandise exports is mixed and generally weak, due to the forest products outlook. U.S. housing starts are seen declining further before stabilizing and rising from a deeper low, sometime around mid-year 2007. Since forest products account for almost 40% of B.C.'s total dollar exports, this will have major influence on the total. The outlook for metals and energy is brighter, as these products enjoy a favourable demand environment. The remaining 25% of goods exports, largely machinery and equipment, look to grow at a moderate pace.

Merchandise exports from B.C. could increase slightly this year but a small decline could also occur – it is a close call. A total dollar value of about \$34 billion in 2006 is a reasonable estimate, while the outlook for 2007 is for a small 2% gain, but that could easily turn into 2% decline. B.C.'s export dependence on the U.S. and its relatively narrow product base currently limit its upside potential. On top of that, the high U.S.-Canada exchange rate doesn't help.

Housing Starts, Urban B.C., Seasonally Adjusted, Monthly



Source: Statistics Canada.

Latest: October