



Weekly economic Briefing

volume 12 . number 37 . September 15, 2006

Industrial goods lead export growth

Exports of B.C.-origin industrial goods and materials totalled \$574 million in July, the second-highest monthly total ever after June's record high. B.C.'s industrial goods and materials exports include mostly copper and molybdenum ores and concentrates, unwrought aluminum and zinc, as well as various non-metallic minerals used in construction and manufacturing. Manufacturers and miners export these goods mostly to the United States, Asia and Europe.

Robust global economic growth, led by several Asian countries, underlies the strong world-wide demand for industrial materials. High oil prices together with strong monetary and fiscal conditions are the main factors behind the strong U.S./Canadian dollar exchange rate, which amplifies the value of Canadian exports. The outlook is for these trends to continue.

The value of all B.C.-origin exports totalled \$2.8 billion in July, down \$319 million (-10.3%) from June. Most of the drop was in energy and forest products, although machinery, equipment and industrial goods also declined from June. Monthly swings in export values of this magnitude are normal.

In the first seven months of 2006, B.C.-origin exports totalled \$19.8 billion, up \$845 million (4.5%) from the same period last year. Year-to-date exports of industrial goods and materials are up \$513 million (17.4%), energy exports are up \$173 million (4.7%) on the strength of coal and natural gas shipments, and machinery and equipment exports, including a small volume of automobile parts, are up \$123 million (4.8%).

International Exports of B.C.- Origin Goods



Source: Statistics Canada.

Meanwhile, forest product exports totalled \$7.7 billion year-to-date, down \$36 million (0.5%) year-over-year. Slower housing construction in the U.S. since late 2005 and the strong Canadian dollar are dampening output prices for B.C.'s lumber and panel manufacturers.

Credit Union Central forecasts that B.C.'s exports of goods and services, both international and interprovincial, will rise by about 3% per year through 2007, with the value of international exports of B.C.-origin goods alone growing more strongly than that. Meanwhile, imports of goods and services are forecast to rise twice as fast, widening B.C.'s overall trade deficit from \$5 billion in 2005 to \$11.4 billion in 2007.

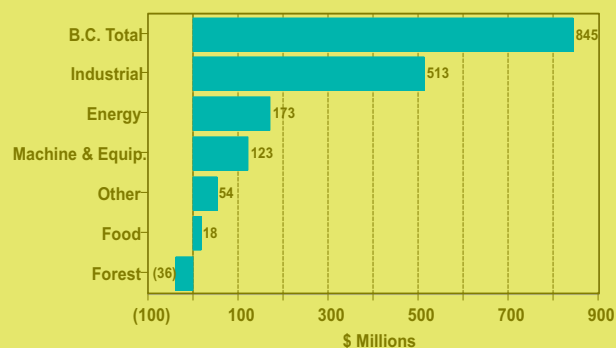
B.C. housing starts trending lower

Housing starts in urban B.C. centres declined in August, continuing a general downward trend that began a few months earlier. While monthly ups and downs regularly occur, the trend since February is clearly downward. Does this mean that housing construction is past its peak and the overall housing market has also seen its high for this cycle? Tough questions, but the answer is "probably not", based on expectations of future demand drivers.

The monthly housing starts figures bounce around mainly due to the lumpy or bulky nature of multi-unit projects, and in August a drop in multi-unit starts pulled down total housing starts. Seasonally adjusted housing starts fell to 2,340 units in August from 3,051 in July, marking the lowest level since April 2005. Multi-unit starts dropped to 1,344 units from 2,000 in July and single-detached units edged lower to 996 units from 1,051.

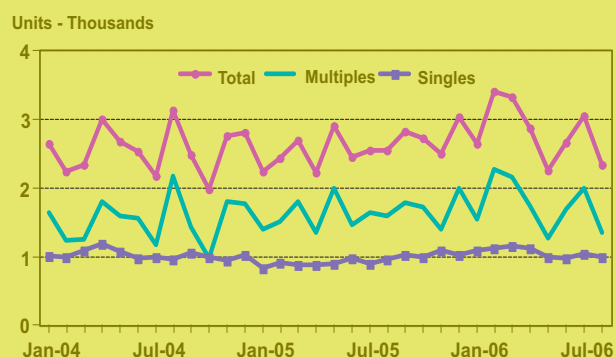
Year-to-date housing starts are 12% higher in urban B.C., with singles starts up 16% and multi-unit starts up 10%. These figures do not reveal monthly trend changes since last February. Housing starts are trending lower across both dwelling types, although somewhat steeper in singles starts, even though the decline from the multi-unit starts highs of last February and March appears greater.

**Year-to-Date International Goods Exports
Jan-Jul 2006 less Jan-Jul 2005 (B.C.-Origin)**



Source: Statistics Canada.

**Housing Starts by Dwelling Type,
Seasonally Adjusted, Urban B.C., Monthly**



Source: CMHC, CUCBC.

Latest: August

The recent decline in housing starts is probably related to the downturn in housing sales that began in August 2005. A time lag between changes in sales and changes in housing starts is normal, though variable. Builders are less inclined to make more investments if sales are sliding lower and sales prospects are uncertain or dim. As sales go, so go housing starts. The historical relationship between the monthly MLS residential unit sales trend and the monthly housing starts trend is quite clear, at least at major cycle turning points, but less so for intervening movements.

With the sales trending downward since last August and housing starts since March, does this signify a market top? That depends on the future course of sales and on what drives sales. The increase in mortgage rates that prompted the decline in unit sales is over. Rates have dipped slightly lower in the past four weeks and the Bank of Canada is on hold for the next few months at least. This will have a positive impact on sales.

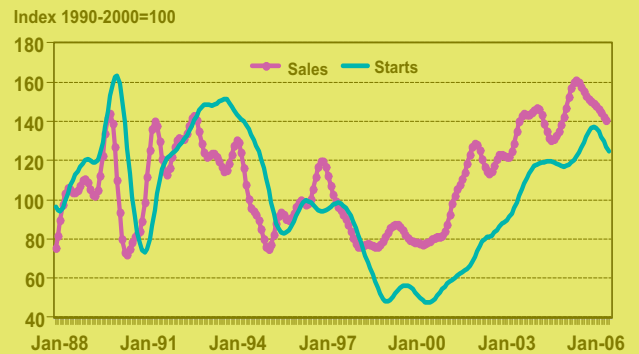
Energy prices have come down and that leaves more income for other spending, and perhaps more importantly, it boosts consumer confidence. It also bolsters economic prospects and activity since more income is available for non-energy spending. The much-debated U.S. economic slowdown or looming recession hinges a fair bit on high energy prices, though it is largely driven by fears of a housing collapse. Stronger U.S. economic growth is positive for B.C.'s economy.

B.C.'s economic prospects remain vary favourable, though a U.S. recession would have a substantial negative impact on the provincial economy and would ripple through to the housing market. This forecast does not foresee a U.S. recession, which, by the way, would result in lower interest rates and a re-stimulated housing market.

With B.C.'s future economic growth pegged at above 4% next year and just below 4% in 2008, the housing market is not likely to continue declining. Migration to the province is rising, though from a low level, and at the margin contributes to housing sales demand. Overall, the key housing sales drivers of interest rates, income growth, and migration appear to support future housing unit sales.

The main negative demand factor is the high level of housing prices and the affordability squeeze on low-equity and first-time buyers. This is a worsening situation and is not expected to improve until prices or mortgage rates decline. An affordability squeeze affects unit sales and the market over a long period and does not cause a substantial market downturn in a few months.

Housing Sales and Housing Starts Trends, B.C.



Source: CREA, CMHC, CUCBC.

Latest: August

Looking ahead, the likely end to B.C.'s housing cycle will be a gradual or moderate decline, barring a large, sudden, negative geopolitical development that crashes global financial markets. The timing of a cycle end is always uncertain, but sometime in the next one to three years is a reasonable starting point. Normally functioning markets always find their oversupply point and housing is no different. The scenario foreseen for B.C. is a soft landing with no, or only modest, declines in prices. Unit sales and housing starts undergo larger swings than prices.

This forecast sees housing sales beginning to trend higher in the fourth quarter and into 2007. B.C. housing starts are forecast at 38,400 units this year and 39,100 units next year. Recent sales and housing starts activity likely does not signal the end of this up-cycle.