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BC 2007 ECONOMIC FORECAST: ANOTHER YEAR OF SOLID GROWTH

In the wake of the strongest multi-year expansion since the late 1980s, economic growth in BC is likely to moderate somewhat in 2007 but stay comfortably above its long-term average. This modest downshift is due predominantly to a weakening US housing market and a subdued overall export performance. The good news is that domestic demand in the province is buoyant. Non-residential construction stands out as a driving force in the current upswing. In addition, optimistic and wealthier BC consumers should continue to spend freely. For 2007, the Business Council expects the BC economy to grow by 3.4% on an after-inflation basis, down from 4.3% last year. A similar performance is likely in 2008.

In contrast to the previous two years, when almost all sectors and regions of the economy were in good shape, this year will see a few more soft spots. BC's forest sector is already feeling the effects of the downturn in the US housing market. Weak natural gas prices over much of 2006 herald an easing in exploration and development in the northeast in 2007. But this shifting landscape will go largely unnoticed in the increasingly diversified and services-

BC Near-Term Economic Outlook (annual per cent change unless otherwise indicated)			
	2006	2007	2008
Real GDP	4.3e	3.4	3.5
Employment	3.0a	2.0	1.8
Unemployment rate (%)	4.7a	4.4	4.3
Housing starts (000 units)	36.2e	32.0	30.0
Retail sales	7.2e	6.5	6.0
BC CPI	1.7a	2.1	2.1
e - estimate a - actual Sources: Statistics Canada, BC Stats and Business Council for estimates and forecasts.			

oriented Lower Mainland region. Greater Vancouver's expanding gateway role, coupled with high levels of activity in industries like advanced technology, film and television, and non-residential construction, will keep the region on a solid growth track. Additional sources of strength in the Lower Mainland include spin-off benefits from the booming mining sector and stepped up preparation for the 2010 Olympics.

External Outlook

On the whole, the external economic setting is still quite positive from BC's perspective. Although global growth will not match last year's impressive gain of almost 5%, global output should continue to grow at a healthy clip - likely in the range of 3.5-4.0%. Against a backdrop of near 10% growth in China and a robust expansion throughout most of the rest of Asia, commodity markets should remain relatively strong. However, some softening in prices is likely for certain resource products.



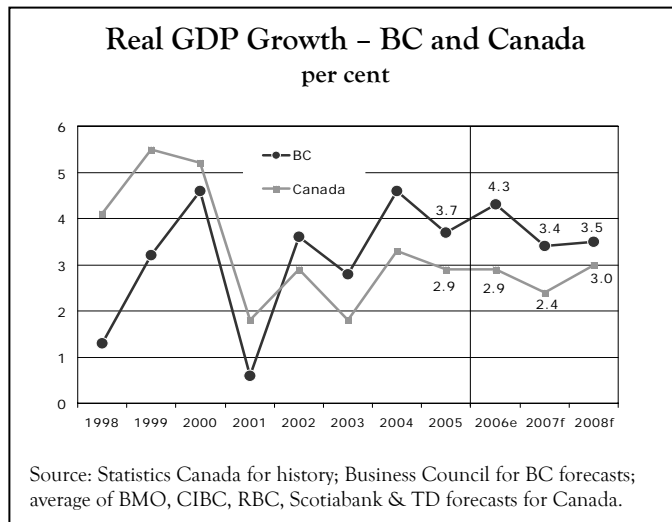
As the destination for almost two-thirds of the province’s international exports, developments in the US carry heavy weight in assessing BC’s economic prospects. After slowing in the third quarter of 2006, the American economy has lately shown signs of strengthening. Opinions are mixed on the outlook for 2007, with some economists predicting a significant slowdown stemming largely from falling housing prices and the collateral impact on consumer spending. But recent, generally positive data have prompted a number of economists to upgrade their forecasts.

Even if the broader US economy moves to a stronger growth footing, conditions in the US housing market will stay soft in the next 12-18 months. Some indicators suggest the US housing market may have turned the corner, but high inventories of new homes mean any gain in new home construction will be minimal at best. Over the course of a typical economic cycle, US housing starts tend to drop by about 50% from their peak before they begin to recover. Currently, US home building activity is off by just 25% since starts peaked in early 2006.

In Canada, the near-term outlook points to modest growth in the vicinity of 2.2-2.5% this year, down from 2.7% in 2006. As 2006 came to a close, the consensus view was that the Bank of Canada would likely trim interest rates sometime in the first half of 2007, to counter the effects of a slowing economy. But with the release of the Bank of Canada’s latest Monetary Policy Report, expectations have shifted and many forecasters now see little likelihood that the Bank will adjust its trend setting rate in 2007. The central Bank believes the Canadian economy ended 2006 at or just above capacity. Feeble productivity growth means there has been a slower than expected increase in economic capacity, which suggests that Canada is already operating at or very near its non-inflationary “speed limit.” In this setting, the Bank will not want to provide monetary stimulus by cutting interest rates. Signs that the US economy is perking up faster than most forecasters had anticipated will be welcomed by Canada’s export sector and further lessen the pressure for lower interest rates this year.

After reaching a peak of almost 91 cents per US dollar last year, the Loonie has depreciated in the past six months, slipping below 85 cents US by late January. As a result, most forecasters have revised down their exchange rate expectations. With the

prices of many Canadian commodity exports, including oil, easing, further depreciation vis-à-vis the US greenback is possible. As well, uncertainty about the minority federal government’s longevity is a wild card that could make investors jittery and put additional downward pressure on the Canadian dollar.





BC Economy

From roadwork to bridges and highways, high rise towers, new business parks, warehouses, resort developments, and retail malls, evidence of the current construction boom is visible all across the province. Official figures confirm this. The value of non-residential building permits surged nearly 30% in 2006, following a 55% jump in 2005. There are now a total of 783 large projects proposed or under construction in BC. This is up from 650 a year ago and 476 in 2005. The value of these projects is estimated at \$111 billion. Although some of these projects may never be built and others will face delays, the evidence points to a high level of construction activity through 2008.

The other key factor shaping BC's still-upbeat near-term outlook is significant growth in personal incomes and consumer expenditures. A long stretch of above average job growth accompanied by rising wages is translating into tangible income gains. On top of this, home owners have benefitted from rising real estate prices. In 2004 and 2005, real personal expenditures on consumer goods and services (a more comprehensive measure than retail sales, which does not capture consumer spending on services) rose 4.3% and 4.4% respectively. All indications are that BC consumers will continue to open their wallets in the coming year.

The job market should also remain healthy, following back to back years of impressive job creation in 2005 and 2006. However, with BC's unemployment rate near a 30-year low heading into 2007, labour shortages will become more common and many employers will have a tough time filling vacant positions. Low unemployment and tight labour market conditions will dampen job growth, pushing it back down towards its long-term average of around 2% by the second half of this year.

Government fiscal stimulus is another positive for the domestic economy. The province is on course to post a surplus of at least \$2 billion when the books are closed on 2006-07. Already it has announced an \$885 million boost in health spending for the coming fiscal year. When the budget is tabled on February 20, it would not be surprising to see spending increases in other areas and, possibly, a modicum of targeted tax relief.

Driven by increased immigration and a modest pick up in interprovincial migration, stronger population growth is another factor supporting the domestic economy. Within Canada, BC and Alberta stand out as the only two provinces recording net inflows of interprovincial migrants.

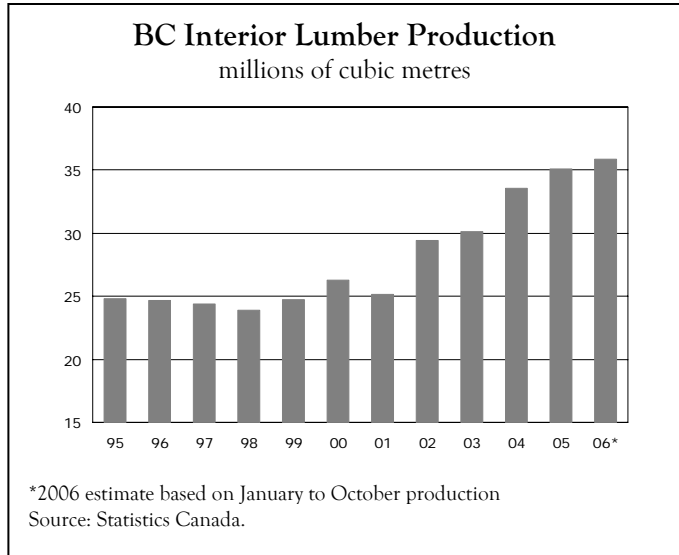
BC Industry Outlook

Over the past couple of years, nearly all industries benefited from the strong global economy and the economic rebound in BC. While prospects for most BC industries are still bright, there are clouds on the horizon for some. In general, the recent retreat in the Canadian dollar is a positive development for export oriented industries, but it also coincides with softer commodity markets and a slumping US housing sector.



Forestry and Related – Cloudy

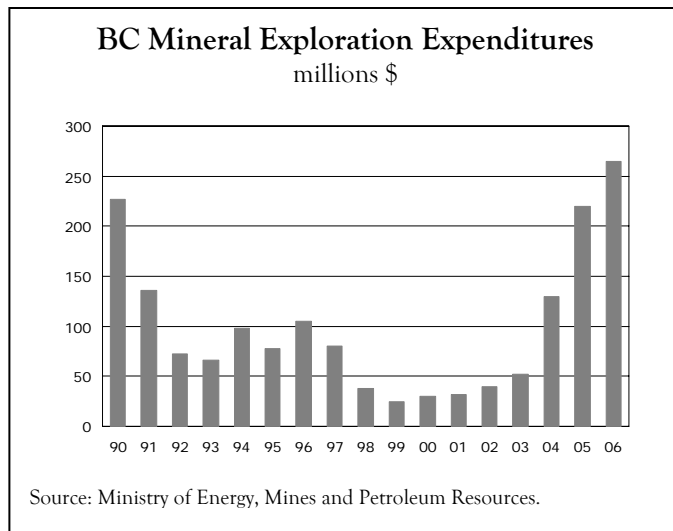
The plunge in US housing starts is taking a toll on BC's lumber producers. Lumber prices recently fell to their lowest point since mid-2003. Prices have recovered somewhat, moving up to around US\$270 per thousand board feet by early February, but at this level profit margins are thin or non-existent for many BC producers. Under the new Canada-US Softwood Lumber Agreement, the full 15% export charge applies on BC softwood shipments to the US as long as lumber prices are below \$US350 per thousand cubic feet.



Total lumber production in the interior is still high and will persist at elevated levels because of beetle kill wood. The need to cut dead/dying timber stands while they still have some value is creating a huge surplus of logs, which is keeping lumber producers operating at or near capacity. The integrated forestry companies (those producing both wood products and pulp) are benefitting from strong pulp prices.

Oil and Gas – Bright with (temporary) scattered clouds

The boom in the natural gas industry concentrated in northeast BC is showing some signs of cooling. Faced with weaker prices, major producers are all scaling back investment plans for 2007. The number of wells drilled in 2006 was down slightly from the previous year. The price of natural gas has drifted below the US\$7.00 range. Inventories have built up thanks to warmer than usual weather. Many analysts believe inventories will stay high until the summer, perhaps putting additional downward pressure on prices. Over the medium- and longer-term the industry should be a bright spot for BC, given the positive outlook for North American demand. But it will not be a driver of economic growth this year.



Mining and Coal – Sunny and warm

Metals and mineral prices remain high and are helping to fuel the ongoing expansion of BC's mining industry. Although the outlook is more mixed, copper and zinc prices are expected to remain at elevated levels.¹ Metal-

¹ Scotiabank, "Global Outlook", January 2007.



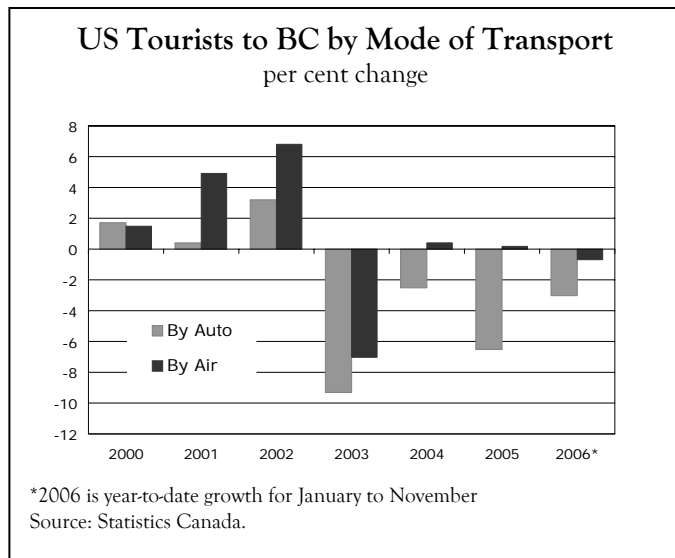
lurgical coal prices are also at historical highs. Strong global demand and the development of a more competitive policy environment for the industry in BC have paved the way for a dramatic increase in exploration and development activity in the sector. Mineral exploration expenditures have soared over the past three years and hit a record \$265 million in 2006 and may post further gains this year. China is a relevant factor here. Its sustained economic boom has been helping to keep global mineral prices high. In addition, BC benefits directly from selling to China. Metallic minerals (grouped together as copper, nickel, lead, and zinc ore mining) are BC's second largest export category shipped to China.

In the context of BC's economic outlook, mining is important because it is a high-value added industry. One medium-size mine generates almost as much revenue annually as BC's entire cruise ship industry. Three new mines opened in BC last year. There are currently 617 exploration projects underway in the province, and 25 major mining projects proposed or under environmental assessment. Opening even a few additional mines would provide a significant lift to the provincial economy.

Tourism - Cloudy with sunny periods

Considering that much of the decline in US cross border traffic is correlated with the ascent of the Canadian dollar, its recent decline vis-à-vis the US greenback should provide some relief to BC's struggling tourism industry in 2007. Border and related security concerns continue to overshadow the sector and are negatively impacting the important American tourism market.

As of January 23rd this year everyone flying into the United States is required to have a passport, including returning US citizens. While the impact of this measure is not likely to be as dramatic as many fear, it is another factor working to deter international travel. Over the past few years, the decline in US travellers to BC was concentrated almost entirely in the short-stay market segment. While air travel has been relatively stable, it also has not grown. The greatest concern relating to the new passport requirement is the effect on the convention business. In the short-term at least, more US event organizers may opt to choose American cities for future meetings and conventions.



Fortunately, other segments of BC's tourism market (some overseas markets and Canadian visitors) have performed better. This has helped push BC occupancy rates moderately higher and contributed to relatively healthy gains in accommodation room revenues.



High Tech and Knowledge-based Industries - Bright

The outlook is for a robust expansion in the high tech sector. BC's gaming and software cluster is especially vibrant. Biotech research also continues to gather momentum. The province's dynamic ICT sector is well positioned to take advantage of the rapid changes in the industry and is expected to be a growth leader in the coming years.

Commercial Transportation - Bright

Two-way trade between North America and the Asia-Pacific continues to expand. Last year the number of twenty-foot equivalent containers shipped through the Port of Vancouver jumped 25% and overall tonnage was up 4%. The railway and trucking industries are also benefiting from BC's strong economy and continued growth in trade between North America and Asia.

Film and Television - Mainly sunny

Despite the fact the Canadian dollar is sharply higher than a few years back, conditions in the film and television industry are still quite buoyant. Following a steep drop in 2004, production spending in BC rebounded in 2005 and the available data suggest that 2006 was another good year.

Non-residential Construction - Spectacular sunshine

As outlined above, this sector is booming. In fact, not having enough skilled workers to complete projects on time is the single biggest risk for the industry. A shortage of workers and higher materials costs have already resulted in the cancellation of a few residential projects. Activity in the industry looks likely to remain at or near-record levels for the balance of the decade.

Housing and Residential Construction - Bright with a few light clouds

BC's housing market is going through an adjustment phase, owing mainly to deteriorating affordability stemming from higher prices. In the face of easing sales activity, new home construction is trending down. For 2007 the total number of starts is expected to be off slightly from 2005 and 2006 levels. Residential construction has been an important economic driver for BC since 2002. The expected small drop in housing starts in 2007 comes after several years of very strong growth.

Summary

The BC economy is expected to continue growing at an above average pace in 2007 and 2008, with real GDP advancing by roughly 3.5%. Overall consumer spending, retail sales, and business investment should all enjoy another year of solid growth. The main area of weakness will be exports. Job creation in the province will slow, due mainly to a lack of available new workers. The slight downshift in BC's economic expansion will go undetected by most people thanks to robust domestic demand and a healthy job market. Tight labour market conditions will keep wages and salaries on a rising trend and lend support to consumer spending.