

SEVERAL FACTORS POINT TO STRONGER GROWTH OUTLOOK FOR BC

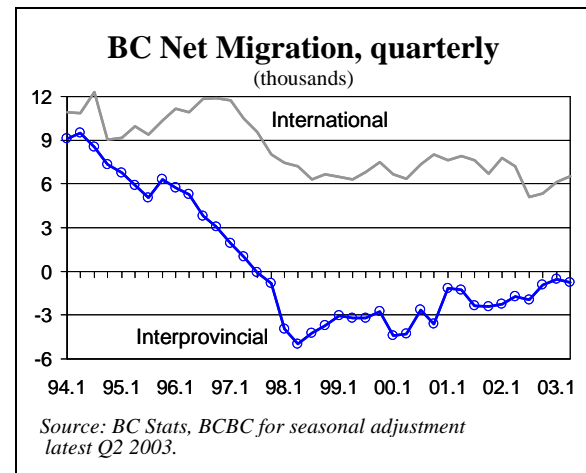
Now that the US economy is shifting to a firmer growth footing and the negative shocks that battered the province are fading, the outlook for the BC economy has brightened. Supporting a stronger growth scenario is the fact that there has also been a broader improvement in the global economy (notably Asia), which is translating into more buoyant commodity markets. This change in the external environment is welcome because lacklustre US and global growth has kept a lid on BC's export activity over the past couple of years and been a key reason for the province's generally weak growth performance.

The improvement in the export sector should begin to show up in the final quarter of 2003 and carry into 2004. In turn, this should gradually feed back into an increased level of domestic economic activity as firms expand their payrolls. The current consensus forecast is for real GDP growth in BC to accelerate to almost 3% in 2004, or nearly double the current projection for 2003.¹

While this is a substantial turnaround, a number of ongoing structural issues and emerging concerns will work to dampen economic activity over the near term.

Reasons for Optimism

The best news is the **outlook for the US economy**. There is mounting evidence that a firmer recovery is now taking hold south of the border. The historically low interest rate environment, a falling US dollar and solid gains in the equity markets have produced



very supportive monetary and financial conditions while tax cuts and rising defence spending are providing a significant fiscal boost. There are even signs that businesses are taking advantage of new, more generous depreciation provisions in the US, which together with low borrowing costs may finally spur an increase in investment spending. American exporters are also being helped by the weaker US dollar and the pick up in global economic conditions.

Although the US job market remains soft, a few preliminary indications suggest that employment may be slowly turning up.

The broader improvement in the global economic outlook is evident in **rising commodity prices**. In particular, copper, gold and several other base metals have posted gains in recent months; newsprint and pulp prices have moved into an up-cycle; and, although they have lately backed off, lumber prices at US\$290 per thousand board feet are well above the US\$220 range seen earlier this year.

¹ The consensus forecast is based on the average of published forecasts from Canadian financial institutions.

The **natural gas industry is booming** in BC and long term prospects for this sector are excellent as Alberta's production is beginning to slide and North American demand is expected to continue to grow. This means higher BC exports, more jobs in the Northeast and a substantial boost to provincial government revenue.

Another plus for BC is that interest rates are expected to remain relatively low over 2004, which will continue to support a **robust housing sector**. A high and rising level of re-sales as well as increasing home construction activity have provided important support to the domestic economy in recent years.

After a marked slowing this year, motor vehicle sales and retail sales have surged, hinting at a revival in consumer confidence and a return to **stronger growth in consumer spending**.

It should also be noted that BC's job market has been reasonably healthy, particularly given the various economic difficulties the province has experienced. BC has recorded **moderate job growth** (+25,000) since the beginning of the year. Admittedly, in the past few months the gains have been concentrated in the part time category, but looking ahead there is reason to believe that stronger economic growth will see some part time jobs converted into full-time positions.

Interprovincial migration continues to improve and will soon be contributing to population growth. Although there are still more people moving to other provinces than coming to BC from the rest of Canada, the net outflow has declined steadily over the past couple of years and is poised to turn positive in the next couple of quarters.

Concerns and Mitigating Factors

There are also a few reasons for caution. The biggest reason is the **rapidly appreciating Canadian dollar**. The loonie has climbed by an unprecedented 20% relative to the US dollar since last December, and most analysts are forecasting further upside. The stronger dollar makes it more difficult for BC exporters to compete in the US marketplace and also squeezes profits for companies selling in US dollars but paying wages and other operating costs in Canadian denominated dollars. Unfortunately, the stronger currency is a clear negative for economic growth in BC, with estimates suggesting that a one cent increase in the Canadian dollar costs the forest industry alone \$100 million dollars annually.

Adding to these difficulties, **the softwood lumber dispute** continues to exact a toll on BC forest companies. At this point a resolution of this trade dispute does not appear imminent.

The **tourism industry will struggle to regain lost ground** in 2004. This is not so much a concern as it is a mitigating factor. The outlook for the sector has improved (after a poor 2002-03), but it will take time for the industry to fully recover and this process will be slowed by the rising dollar.

Finally, there is some lingering doubt about the **sustainability of the US recovery**. If current monetary stimulus in the US does not have traction and the fiscal stimulus fades without triggering a recovery in business investment, overall economic growth could subside in the second half of 2004. Such a scenario would quickly impact BC's fragile export sector.

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