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ECONOMICS
B.C. Weekly Briefing

This week's indicators of B.C. economic activity are mixed, reflecting the uneven and overall modest growth widely expected to prevail during this economic rebound. International visitors and retail sales increased in November, while manufacturing sales declined. Consumer price inflation remained negligible in December.

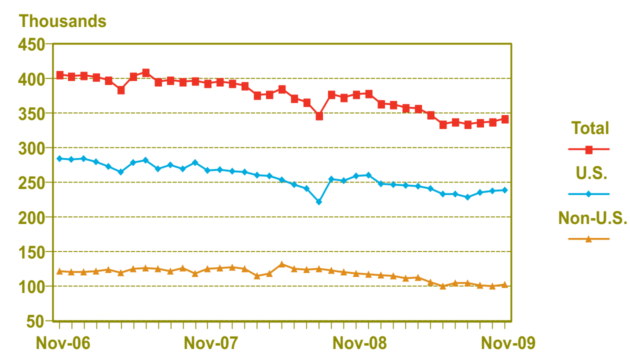
International non-resident traveller entries to B.C. edged up in November, marking the third straight month over month rise. Gains were broad-based, as more visitors arrived from both the U.S. and elsewhere. The recent upward trend has been led by U.S. visitors and stands in contrast to the downward trend that has prevailed since early 2003.

Total entries in November increased by 4,793 travellers (1.4%), month-over-month, seasonally adjusted, according to the latest estimates from Statistics Canada. U.S. visitors rose by 1,981 persons (0.8%), while visitors from other countries increased by 2,812 persons (2.8%). In the 11 months through November, total entries dropped by 335,334 persons (7.9%) compared to the same period a year earlier. Year-to-November visitors from the U.S. fell 149,709 (5.2%) year-over-year, while visitors from other countries dropped 185,625 (13.4%).

International tourism will likely continue to struggle for some time yet, although the 2010 Winter Olympics will provide a massive temporary boost in the Greater Vancouver and Squamish-Lillooet regions. The global economic recovery will lift business travel in the coming years, but discretionary travel spending is likely to remain weak for some time due to high and rising household and government debt.

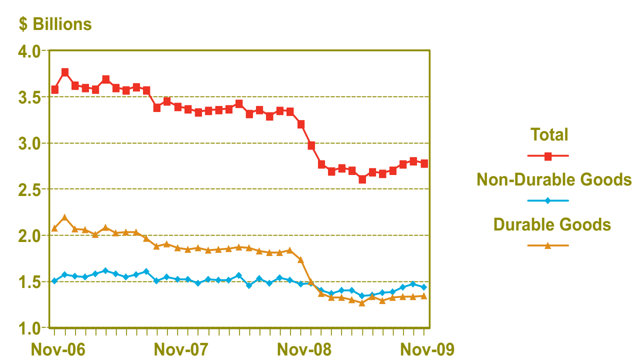
Manufacturing sales in B.C. are slowly coming back from their hard-hit recession-low of eight months ago, despite a slight dip in November. According to the latest estimates from Statistics Canada, sales fell $23 million (0.8%) from October to November, seasonally adjusted.

International Non-Resident Traveler Entries
British Columbia, Seasonally Adjusted, Monthly



Source: Statistics Canada.

Manufacturing Shipments
British Columbia, Monthly, Seasonally Adjusted



Source: Statistics Canada.

The decline was entirely among non-durable goods, which fell 2.1%, while durable goods increased 0.5%.

Wood products are by far the largest component of durable goods manufacturing in B.C., although mineral products are also a substantial component. Food and paper products are the dominant components of B.C.'s non-durable goods manufacturing.

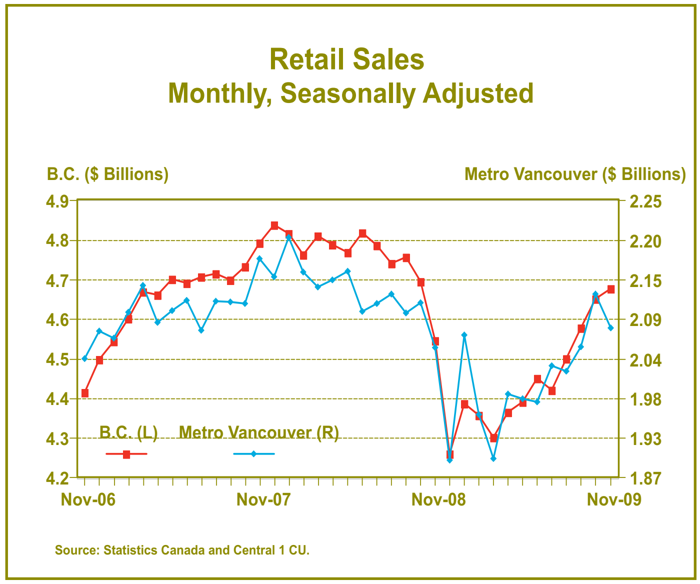
In the first 11 months of 2009, B.C.'s manufacturers sold $30.1 billion worth of goods, down $6.8 billion (18.4%) from the same period a year earlier. The decline was led by durable goods, which fell $5.6 billion (27.7%), while non-durable goods declined $1.2 billion (7%).

B.C.'s manufacturing industries, notably forestry, mining, oil and gas, are weighed down by the high dollar and various structural issues. Nonetheless, a cyclical upturn linked to the U.S. and global economic recovery will play out and lift their exports. Central 1 Credit Union forecasts this sector's gross domestic product (GDP) will edge up 1.3% in 2010, not including price changes, following an estimated 15.9% contraction in 2009. Growth is forecast at 4.5% in 2011 and 4% in 2012.

The forest industry's real GDP, including wood products manufacturing, pulp and paper manufacturing, and logging and support activities, fell to a record low in 2009 but will rebound with higher U.S. housing starts in the next five years. The U.S. housing market will remain severely stressed in 2010, resulting in housing starts rising to about 0.75 million units from 0.55 million units in 2009. While this would be a 35% jump, the level is about one-half of a normal year, which is roughly estimated at 1.5 million units. By 2014, industry GDP will be about 20% below its 2006 high.

In addition to excess production capacity in wood products manufacturing, the pine beetle infestation will have a major negative impact on this sector. Those logs are drier and more costly to transform into dimensional lumber, which is typically a lower grade. Attempts to quickly harvest infested timber are being hampered by low export demand, the high dollar, the Softwood Lumber Agreement and few alternative uses other than wood pellets or power co-generation. Over time, the pine beetle structural issue reduces the supply of harvestable timber, causing supply constraints for producers.

B.C.'s mining sector is poised for growth after 2010 with the rebound in copper, gold, and coal prices and demand in the Asian economy. A handful of major new projects are expected to begin construction and in some cases start production before 2014. Project risk is always high since any number of factors can derail the plans, but the geological potential is there and new projects can become viable under the right market conditions and with the proper infrastructure in place, such as the Northwest energy transmission line. Mining GDP fell into a deep valley in 2009 and is forecast to return to an average level by 2014.



Oil and gas mining will also undergo a cyclical revival, though of a lesser magnitude than forestry and mining. The major new development in the natural gas industry is the surge in shale gas production, due to hydraulic fracturing along with horizontal drilling. Shale gas has been produced for decades in North America but modern techniques have significantly increased its scale and commercial viability. This unconventional supply has altered the natural gas market, reducing prices and price expectations. In northeastern B.C., the Horn River and Montney areas are keenly sought out by exploration and development companies. Oil and gas real GDP is forecast to expand by 18% between 2009 and 2014, reaching new highs each year.

Retail sales in B.C. increased in November, continuing the upward trend that began in April 2009, according to the latest estimates from Statistics Canada. Sales grew by a moderate 0.6% month-over-month, seasonally adjusted. Consumer spending is in the early stages of what is likely to be a long, slow rebound from the sharp recessionary declines at the end of 2008. In the first 11 months of 2009, retail sales in B.C. totalled $48.3 billion, down $3.3 billion (6.3%) from the same period a year earlier.

Central 1 Credit Union forecasts consumer spending in B.C. will increase over the next several years, but at a below-average rate of growth. High and rising household and government debt levels, lower employment and lower household net worth will dampen consumer spending growth for at least a couple of years. Consumer spending did not increase in 2009, which was a rare occurrence for B.C. and the worst performance since the 1982 contraction.

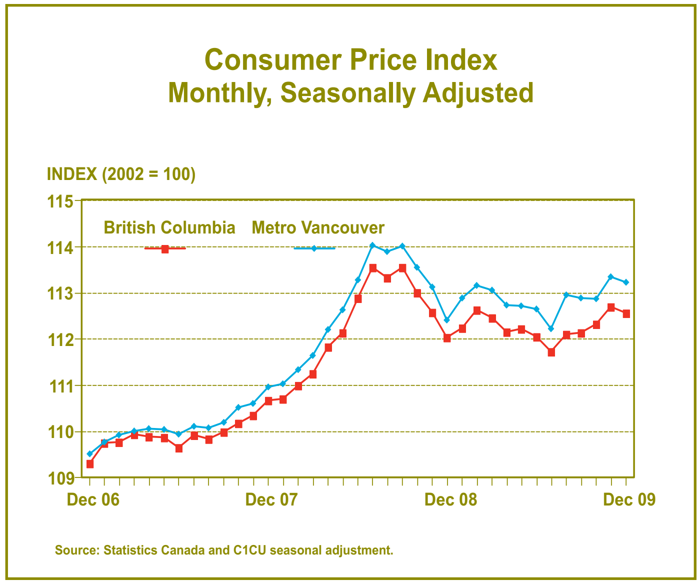
Retail sales will close 2009 about 6% lower year-over-year, as will spending on consumer durables in the economic accounts. Only consumer non-durables and services saw increased spending in 2009. Retail sales are forecast to rise 4.3% in 2010 and 5% in 2011.

Looking ahead, consumer spending changes include higher overall growth and a shift to durable and semi-durable goods. Some of this shift represents pent-up demand from the recession and the previous couple of years, while another component is new growth from an expanding population and income base. A prime example of pent-up demand is housing-related purchases.

A significant event for consumers in 2010 is the implementation of the Harmonized Sales Tax (HST) effective July 1. This will increase the sales taxes paid by consumers and potentially reduce demand due to higher final prices and lower disposable income. Because businesses are able to write-off their HST costs, with small exceptions, lower prices for some goods and services are possible, but this depends on the firm's financial situation, industry market conditions, and competition.

The impact of the HST on consumer spending is subject to many estimation errors and it is difficult to exactly separate its impact from the influence of other factors. Our forecast model, which attempts to control for other factors, projects consumer spending to be 1% to 2% higher by 2014 under the no-HST scenario, with durable goods spending at the upper end of the range. No doubt, other models would yield a different result but this estimate is a reasonable discussion point.

Consumer prices in B.C. edged down in December compared to November, even though the recent trend has been upward. The all-items Consumer Price Index (CPI) decreased 13 basis points from November, seasonally



adjusted (A basis point is one one-hundredth of one per cent). December's CPI is up 45 basis points, or less than one half of one per cent, from a year earlier.

The latest monthly decrease was spread widely over consumer products and led by lower prices for clothing, food, furnishings and gasoline. The latest 12-month increase was also broadly based and led by higher prices for gasoline, seafood, non-alcoholic beverages, property taxes, personal-care products and reading materials.

Neither inflation nor deflation is of particular concern over the near-term. The latest recession has left considerable unused production capacity, while monetary policy can readily become less expansive if price inflation accelerates unexpectedly. Central 1 Credit Union forecasts that B.C.'s CPI inflation rate will average 1.5% in 2010, up from no change in 2009 but still below the long-term average.

David Hobden, Economist
dhobden@central1.com
604 737 5063

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