Central 1™

B.C. Economic Briefing

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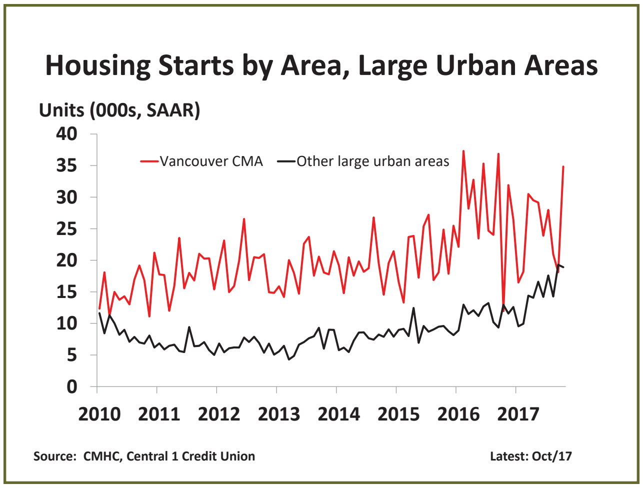
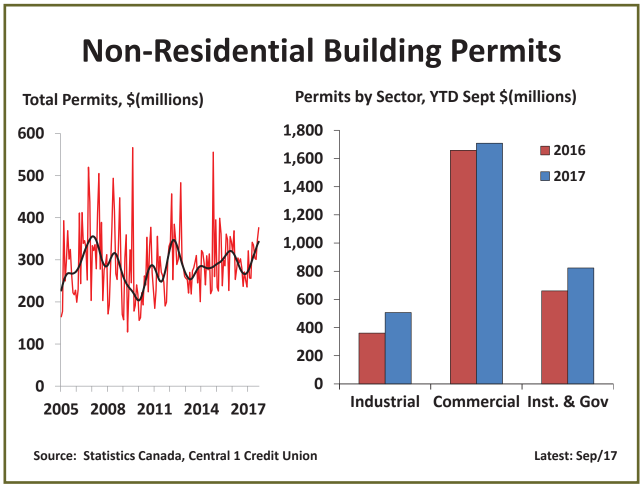
HIGHLIGHTS:

- Housing starts unsustainable and volatile
- B.C. businesses among the most confident in the country
- Non-residential construction permits on the rise
- B.C. leads the nation in economic growth, according to new Statistics Canada report





October housing starts surge on Metro Vancouver multi-family construction

A flurry of activity in the Vancouver census metropolitan area (CMA) fueled a surge in provincial housing starts in October after a softening observed over the last two months. Urban- B.C. housing starts soared to the highest level since 1990 at a seasonally-adjusted annualized rate (saar) of 53,750 units, up from a 37,400 unit pace in September.

Starts in the Vancouver CMA nearly doubled from September to 34,850 units (saar) –driving most of the provincial gain – while starts jumped 30 per cent in Victoria to 9,334 units (saar), adding to a prior month surge. Kelowna starts declined by more than half, with fewer starts also observed in Abbotsford-Mission.

Without a doubt, October's gain is unsustainable. Monthly housing starts are volatile given the infrequency and scale of large multi-family apartment projects which can have a substantial impact on any given month. In particular, multifamily starts in the Vancouver CMA accounted for almost all of October's gain, which will retrace. Nonetheless, underlying construction remains high as strong economic growth, in-migration, low interest rates, a tight rental market and exceptionally low inventory have propelled new home construction. Financing requirements mean the vast majority of these units are presold, either by the end-user or for investment/speculative purposes.

The burst in starts – and relatively weaker starts in same-month 2016 – lifted year-to-date urban-area activity above year-ago levels by two per cent, compared to a five per cent shortfall in September. Multi-family starts are tracking slightly ahead of last year's record-high performance, reflecting strong demand for relatively affordable product in large urban areas, investor demand and, potentially, downsizing by older age cohorts. In some areas, like Kelowna, construction of rental product has been a key driver.

Urban B.C. Year-to-Date Housing Starts - October 2017				
	2016	2017	unit change	% change
Abbotsford-Mission CMA	1,050	1,502	452	43.0
Kelowna CMA	1,736	3,083	1347	77.6
Vancouver CMA	23,109	20,924	-2185	-9.5
Victoria CMA	2,519	3,477	958	38.0
Chillwack CA	605	765	160	26.4
Courtenay CA	259	238	-21	-8.1
Kamloops CA	507	389	-118	-23.3
Nanaimo CA	737	833	96	13.0
Prince George CA	282	237	-45	-16.0
Vernon CA	286	252	-34	-11.9
Total Urban Starts	32,667	33,366	699	2.1
Single-Family	8,696	8,585	-111	-1.3
Multi-Family	23,971	24,781	810	3.4

Source: CMHC

Rising housing starts have been most pronounced in Kelowna (+ 77 per cent), Abbotsford-Mission (+43 per cent), and Victoria (+38 per cent) over the first 10 months. Vancouver CMA starts are still 10 per cent lower despite October's surge, but compares to a record performance a year ago. Starts in smaller urban areas have been mixed with gains in Chilliwack and Nanaimo and declines in most other areas.

Barring a sharp retrenchment, annual 2017 starts, inclusive of rural areas, will come in within five per cent of 2016 levels and will likely surpass 40,000 units – for just the fourth time since 1990. The province is amidst a robust building cycle reminiscent of the mid-2000s when adjusted for population.

That said, the trend should ease in 2018. A record number of units are under construction, with many slated for completion in the coming year, which should lift housing inventory. Meanwhile, rising mortgage rates and tighter mortgage policies curtail household demand. That said, provincial and federal governments are expected to lift housing-related investments, which will provide an offsetting boost.

Small business confidence steady in B.C.

Optimism among small business in B.C. jumped in October according to the latest CFIB Business Barometer reading, following a three month slide. The index rose two points to 61.9, on a scale of 0 to 100. A value above 50 means on balance, the number businesses expecting stronger performance over the next year outnumber those expecting a weaker performance. While still significantly lower than mid-year levels, B.C. businesses are among the most confident in the country, which aligns with B.C.'s strong economic environment observed over the past year. Some of the third quarter slide may have reflected a natural leveling of sentiment following a positive period of activity.

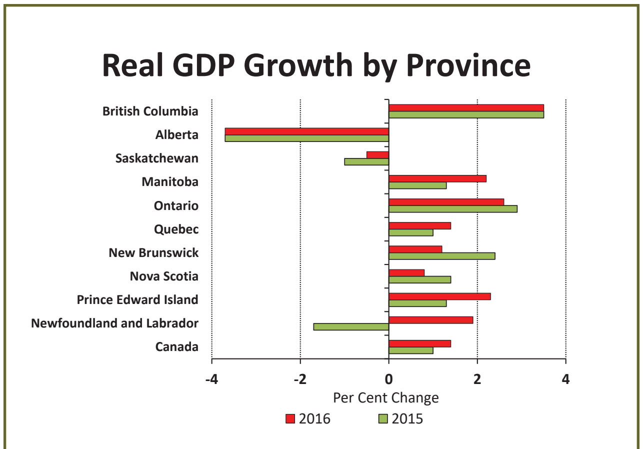
Rising trend for non-residential construction

Non-residential building intentions continued to firm in September with B.C. permits up 8.4 per cent to $376.2 million (seasonally-adjusted), adding to a 15 per cent increase in August. Following a lacklustre pace for much of 2017, permit activity has been on the rise and has lifted year-to-date growth to 13 per cent (+$359.6 million), with a 40 per cent increase in industrial permits and a 24 per cent increase in government-related activity. Commercial permits are flat.

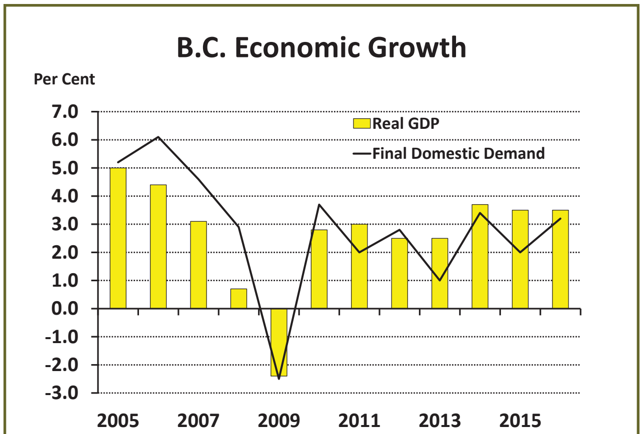
Through the first three quarters, private-sector permit growth has been led by factories and plants, which doubled (+$125.7 million), and warehouse permits, which rose 38 per cent ($82.7 million). Government-led permitting has been led by investments in schools, with permits up 60 per cent (+$182.2 million). While sector permits are sporadic, gains reflect solid business confidence, a growing economy and rising exports. E-commerce is also driving demand for warehousing, while public policy is driving education-related investment.

Household demand and residential investment drive 2016 GDP growth

This week saw the release of Statistics Canada's provincial gross domestic product (GDP) estimates based on economic expenditure and income accounts. Aligning with industry estimates published earlier in the year, B.C. led the nation in economic growth with a 3.5 per cent expan-



Source: Statistics Canada, Central 1 Credit Union



Source: Statistics Canada, Central 1 Credit Union Latest: 2016

sion of GDP in 2016, compared to a national expansion of 1.4 per cent. This marked the third straight year that economic growth exceeded three per cent in B.C. The second strongest growth performance in 2016 was observed in Ontario at 2.6 per cent, while Alberta trailed the nation with a 3.7 per cent contraction.

For the most part, B.C.'s growth performance aligned with Central 1 estimates. Economic growth was driven by strong household spending and government uplift, while business investment and exports lagged. Consumer spending, which makes up more than three quarters of GDP, remained a primary source of growth, expanding three per cent – albeit down from a 3.4 per cent expansion in 2015. A strong labour market, population expansion and housing demand were driving factors of consumer demand, specifically for durable goods expenditures (including vehicles and appliances) which rose 7.3 per cent and semi-durable goods (3.8 per cent). Spending on services rose 2.7 per cent.

Growth in residential investment came in as expected, as a near-record year of housing starts, a high number of transactions and renovation spending contributed to a 15 per cent increase. Government spending also contributed to growth with current expenditures rising a modest 2.5 per cent, while investment rose 5.6 per cent after a pullback in 2015. The latter reflects spending infrastructure spending on roads and other major projects.

In contrast, business investment was a drag and likely reflected weakness in the commodities sector, global trade uncertainty and less spending on office, commercial and hotel space relative to previous years. Non-residential investment in structures added to a 2015 slump, with a16 per cent drop in 2016. Machinery and equipment investment rose 7.4 per cent, in part reflecting reinvestment in depreciating assets. Investment in intellectual property, which also includes mining exploration, fell 10.4 per cent.

Exports came in weaker than anticipated, slowing to 1.9 per cent from 2.8 per cent in 2015, owing mostly to a slowdown in international shipments of both goods and services. In contrast, exports to other provinces rebounded from 0.7 per cent to 2.2 per cent but were still lacklustre, potentially reflecting the impact of weakness in the energy patch. Real imports rose one per cent despite strength in consumer demand, as a weaker Canadian dollar curtailed international imports, while higher vehicle demand may have benefitted Ontario. British Columbia's imports from other provinces rose 4.7 per cent.

While real output in the economy was robust in 2016, nominal GDP growth came in well below expectations at 4.8 per cent, compared to our expectation of 5.8 per cent, reflecting weak growth in wages, consumer prices and lower than anticipated exports. Income growth in 2016 largely went to corporate profits which rose 9.8 per cent, while employee compensation rose by a modest 3.8 per cent – which points to gains driven by hiring rather than wages.

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