B.C. Economic Briefing

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Highlights:

- Retail sales decline for third straight month
- Have home sales hit bottom?
- Resource sectors curtail manufacturing sales
- Consumer prices rise 2.9 per cent from a year ago

Soft retail sales signal slower consumer demand

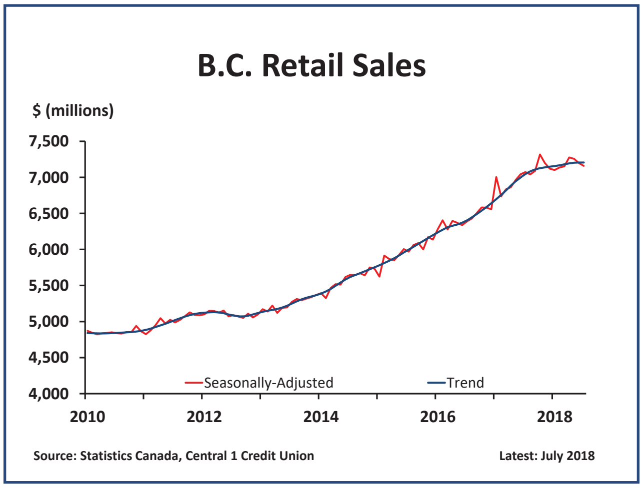
Retail spending softened for a third straight month in B.C. as declines in motor vehicles and parts, and gasoline station sales dragged headline sales lower. Total provincial sales reached a seasonally-adjusted $7.16 billion, down 0.5 per cent from June. Year-over-year sales growth decelerated to 1.2 per cent from 2.2 per cent. The Vancouver Census Metropolitan Area led the pullback, with sales down 1.6 per cent from June, and down 2.2 per cent year-over-year.

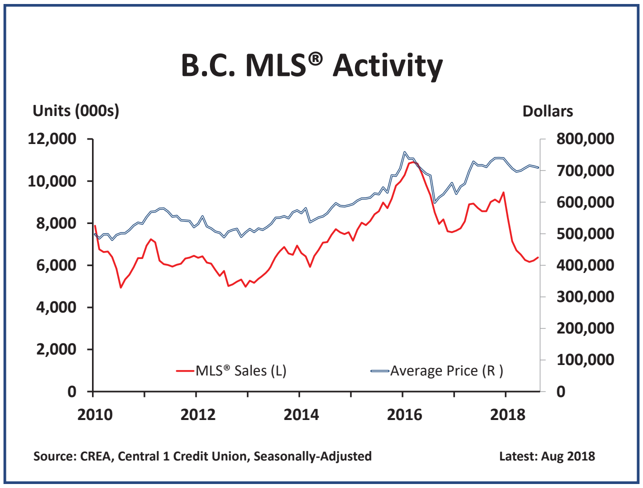
B.C. was one of only two provinces, alongside Manitoba, to report a monthly sales decline. In comparison, national sales rose 0.3 per cent from June, with a year-over-year gain of 3.7 per cent.

July's slump largely reflected lower motor vehicle sales which we estimate fell ten per cent on a month-to-month basis (seasonally-adjusted). Sales in this sector were down five per cent year-over-year. Gasoline sales decelerated from an eight per cent year-over-year pace to a three per cent pace. Housing-related sales of furniture, and furnishing and building materials accelerated.

The recent slide adds to a soft range-bound trend since late 2017. That said, this has largely aligned with fluctuations in motor vehicle sales and gasoline station sales/prices. The former reflects a turn from the cycle high reached late last year. Sales remain elevated, but higher interest rates, slowing in the economy and housing market, and lower replacement demand have been factors. Excluding these volatile retail components, retail spending has continued to rise, albeit at a slowing pace.

Year-to-date, retail sales were up 3.8 per cent through July, and the deceleration in the trend is consistent with a slowdown of growth in B.C.'s economy. While





the economy remains solid with low unemployment rates and strong wage growth, labour availability has been a constraint to consumer demand. Further contributing to a slower retail profile are near peak tourism flows and subdued housing market activity.

Home sales turn higher but price momentum waning

B.C.'s resale housing market looks to have finally turned the corner, following the shock of federal B-20 mortgage stress test measures and drag from higher interest rates. While sales remain and down more than 25 per cent on a year-over-year basis, MLS® sales rose two per cent from July to 6,370 units. With a second straight gain, the negative contribution of the resale market to economic growth has ended, stabilizing ancillary sectors including related financial and professional services.

A scan of MLS® sales shows sales gains across the majority of real estate board areas in August.

The Greater Vancouver board area posted a 2.9 per cent increase, while Victoria sales rose 2.7 per cent. Elsewhere on Vancouver Island, sales surged 9.8 per cent from July. Offsetting gains were declines of eight per cent in the South Okanagan, and nearly 11 per cent in Chilliwack. That said, the provincial sales pace is feeble, tracking at a pace last seen in 2014. Among regions, post-B-20 home sales have slumped the hardest in the higher priced regions of the Lower Mainland and Victoria.

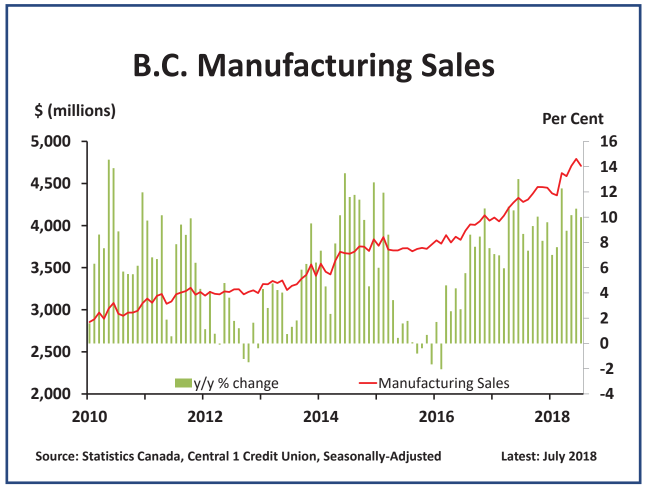
Resale inventory continued to creep higher. Provincial active listings have surged 30 per cent since the beginning of the year, but the monthly pace of growth withered to a modest 0.9 per cent. Despite the relatively strong surge, inventory levels remain near historical lows. Moreover, new listings are not out of the ordinary, suggesting a sluggish sales environment has kept prospective sellers on the sidelines as they wait out market softness. Sales-to-listing ratios point to balanced market conditions in the Lower Mainland and central and southern interior markets, while sellers' markets persist on Vancouver Island and in Kamloops.

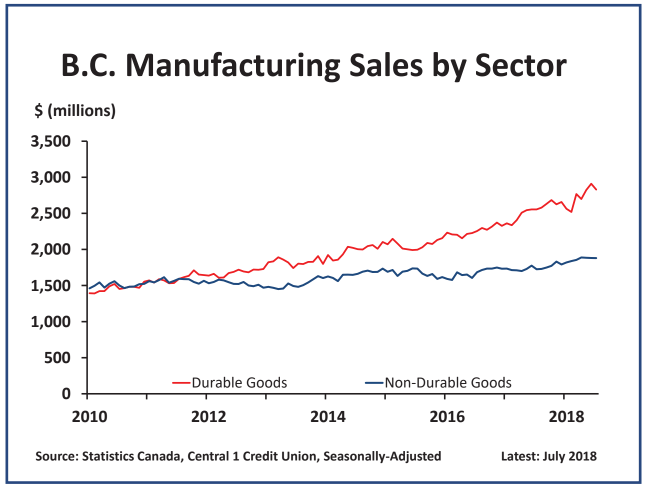
Nevertheless, momentum matters and sales weakness is eroding prices in various markets. The provincial MLS® average price declined 0.5 per cent from July to $709,727 and was virtually unchanged from same-month 2017. That said, the steep decline in sales is leading to an erosion in sale prices in the Lower Mainland real estate board areas, and a flatter environment in Victoria, according the benchmark price indices. This is based on a low volume environment, meaning only those more motivated to sell are setting the price trend. Lower Mainland benchmark values are expected to ease another five to seven percent, led by a decline in detached home prices. Other markets around the province are expected to see modest price growth, reflecting the solid economy. Mortgage stress test measures are less of a barrier due to lower price levels. Rising interest rates will be a headwind.

While the resale market is no longer a direct drag on growth, the sluggish environment will slow future economic activity. Slower sell-through of pre-sales will curtail housing starts, detracting from the contribution of construction to economic growth.

Resources products weigh on July manufacturing, upward trend remains strong

Manufacturing sales backtracked in July following two months of gains, but remained firmly ahead of year-ago levels. July dollar-volume factory sales reached a seasonally-adjusted $4.71 billion, down 1.7





per cent from June. Main contributors to the pull-back are forestry product shipments, which fell 2.6 per cent or $30 million from June to $1.15 billion, and a 15 per cent ($53 million) decline in primary metals manufacturing. These sectors accounted for almost all of the net decline. A decline in forestry product and lumber prices partly reflected a period of high but eroding price levels, as U.S. inventories firmed and demand temporarily softened. U.S. tariffs on aluminum may be biting into Canadian manufacturing and affecting B.C. production. While these two sectors were a drag, sectors with significantly higher sales relative to June were: chemical manufacturing (up 10.2 per cent), machinery (up 5.1 per cent), and food products (up 1.9 per cent).

Despite July's slip, the manufacturing trend remains positive. Unadjusted sales volume rose 11.8 per cent on a year-over-year basis, up from ten per cent the previous month. Year-to-date sales growth reached a robust 9.7 per cent, with activity trending higher since early 2016. Growth has been particularly strong for wood and paper products, with elevated prices contributing to the former, while machinery and electronics production have also strengthened. Strong U.S. economic growth, increased demand from China and other emerging markets have underpinned export demand, lifting provincial manufacturer fortunes. A current risk to the manufacturing cycle is the trade war between China and the U.S., which could temper global growth and negatively impact trade and demand. That said, Canada could receive a boost if China's import demand repositions away from the U.S. Meanwhile, the relative uncertainty of the Canada – U.S. trade relations could also dampen future manufacturing activity if auto tariffs are imposed and tariff wars intensify.

Inflation remains elevated in August despite climbdown

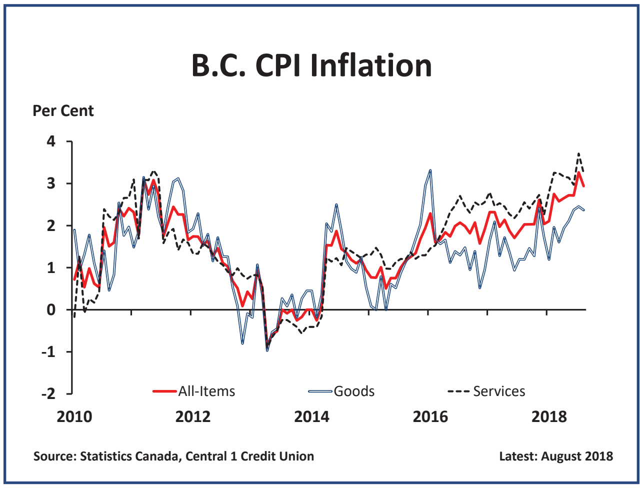
B.C. consumer price inflation fell back in August to a 2.9 per cent year-over-year pace, down from 3.3 per cent in July. This was above the national pace of 2.8 per cent.

A decline in gasoline prices from July, which lowered year-over-year growth from 23 per cent to 14 per cent in the product segment, contributed to the dip. That said, gasoline is still putting upward pressure on headline inflation relative to other goods.

Excluding energy costs, inflation was a modest 2.5 per cent. Food prices were up 1.9 per cent from a year ago, although food prices at restaurants (up 3.9 per cent), reflect rising wage pressures and operational costs. Scant inflation in retail food costs and clothing and footwear, both up 0.9 per cent, likely reflect strong retail competition both from brick and mortar and for the latter, online, which is holding prices down for consumers.

The shelter index rose 2.8 per cent, which declined from a 3.3 per cent pace in July, which seems to reflect a softening of home values. Rental accommodations rose at 1.9 per cent pace, although this seems low, particularly in light of persistently low vacancy rates, and a rent growth allowance of up to 4.5 per cent this year, which does not apply to turnover suites.

Broadly, the price of goods (up 2.4 per cent) has trailed services (up 3.2 per cent). Retail competition is holding the latter at bay, while a tight labour market, with unemployment near five per cent of the labour force, high job vacancy rates, and rising operational costs is likely driving service prices up.



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