



**AUGUST 8, 2016**

OUR ECONOMIC PROSPECTS IN A  
SLOW GROWTH WORLD

PRESENTED TO

THE PROBUS CLUB OF NORTH SHORE VANCOUVER

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## WHAT DO BUSINESS LEADERS THINK OF ECONOMISTS?

**Any company that has  
an economist on staff certainly  
has one employee too many”**

**Warren Buffett**

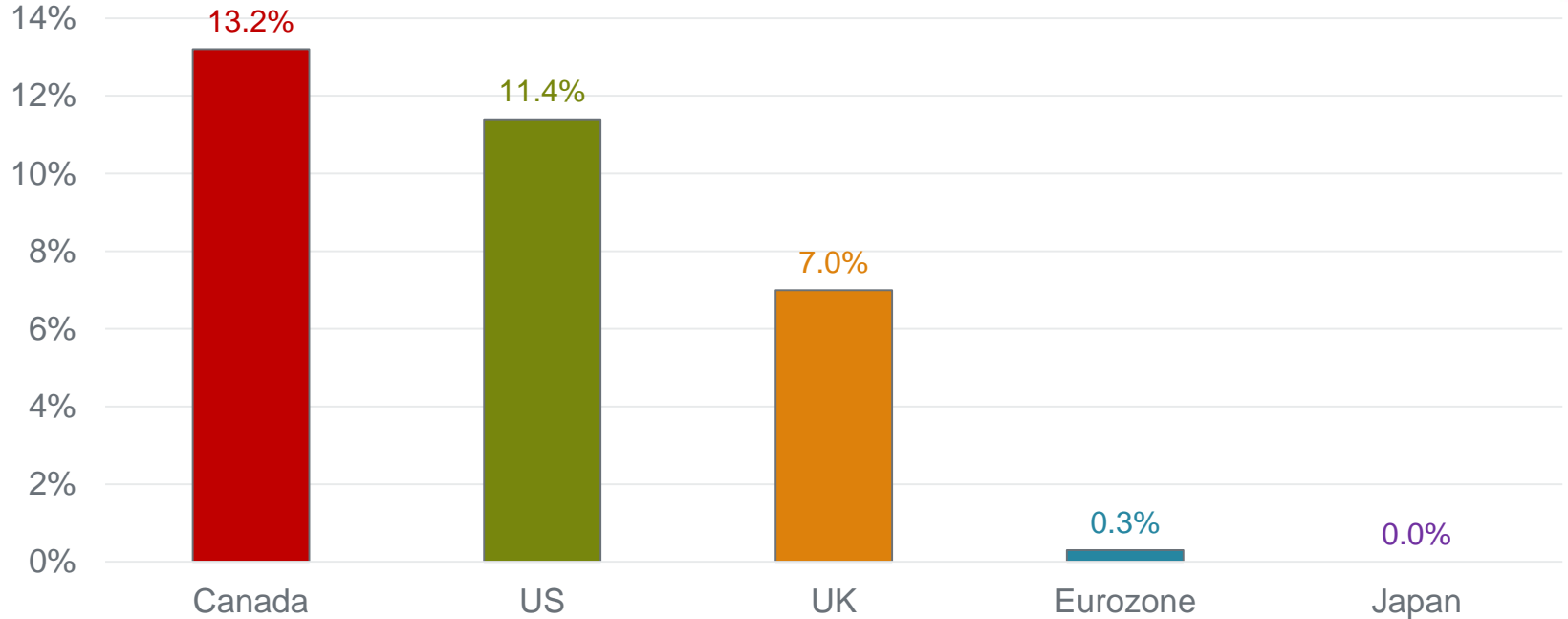
## 2016: A TOUGH FIRST SEVEN MONTHS OF THE YEAR!

- Global economic forecasts are revised down... *again*
- Five central banks have set 'negative' policy rates (ECB, Japan, Denmark, Sweden and Switzerland)
- Bond yields hover near all-time lows in many advanced economies...with more than US\$10 trillion in sovereign debt trading at negative nominal yields!
- The UK votes to leave the EU
- China's equity market struggles, capital outflows accelerate, debt continues to mount, and doubts persist whether the country can avoid a 'hard landing'
- Choppy economic data spark concern about the durability of the already lengthy American economic expansion
- Donald Trump secures the Republican Party nomination for President, promising radical changes to US trade, foreign and immigration policies if he wins

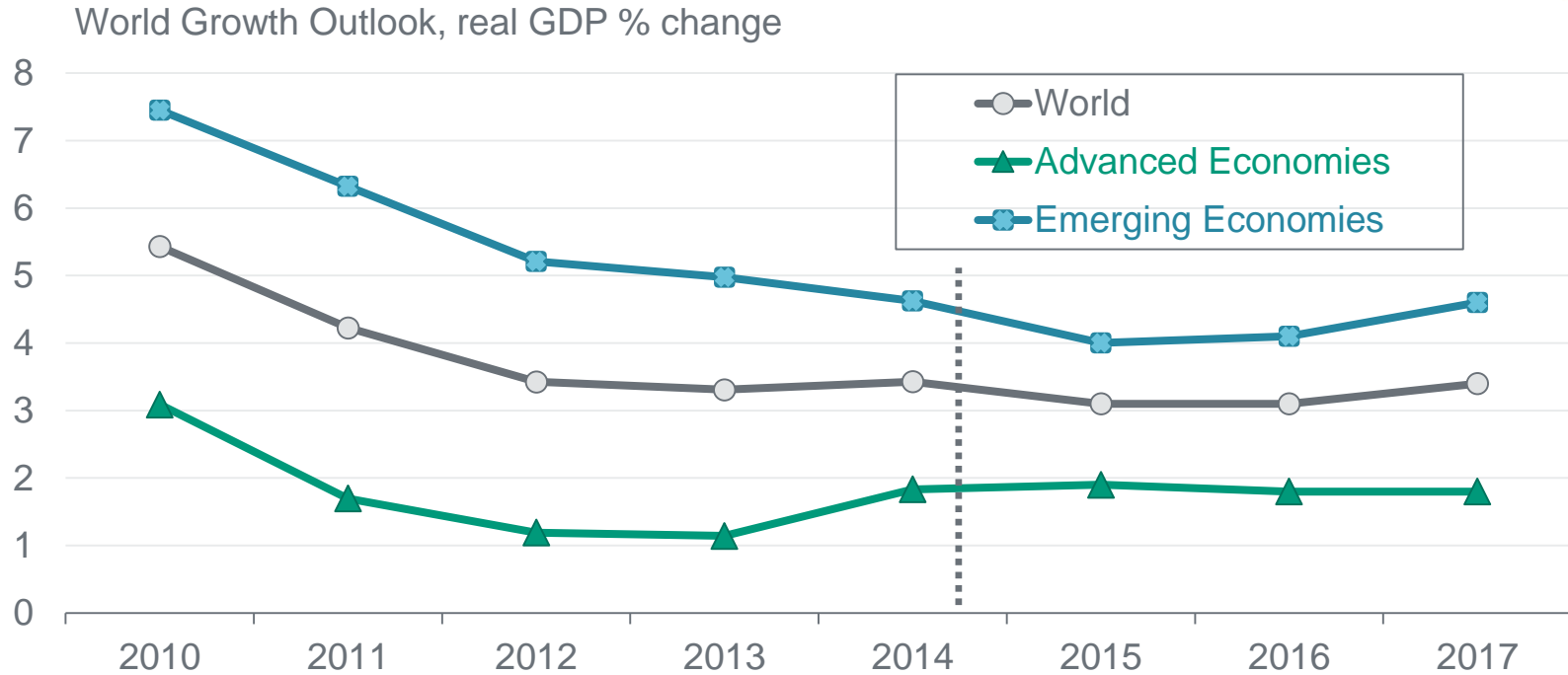
# BREXIT IN A SNAPSHOT...



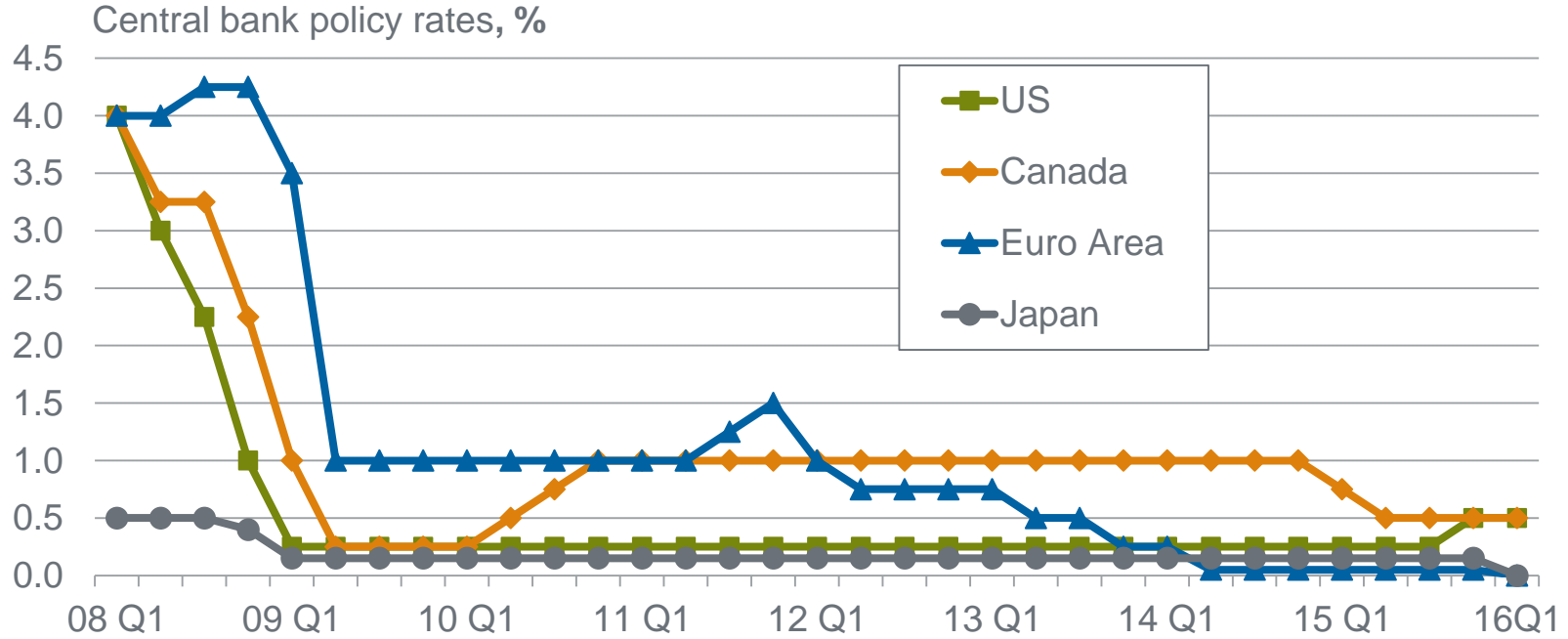
## CUMULATIVE CHANGE IN REAL GDP (ECONOMIC OUTPUT), 2016Q1 VS 2008Q1, SELECTED ADVANCED ECONOMIES



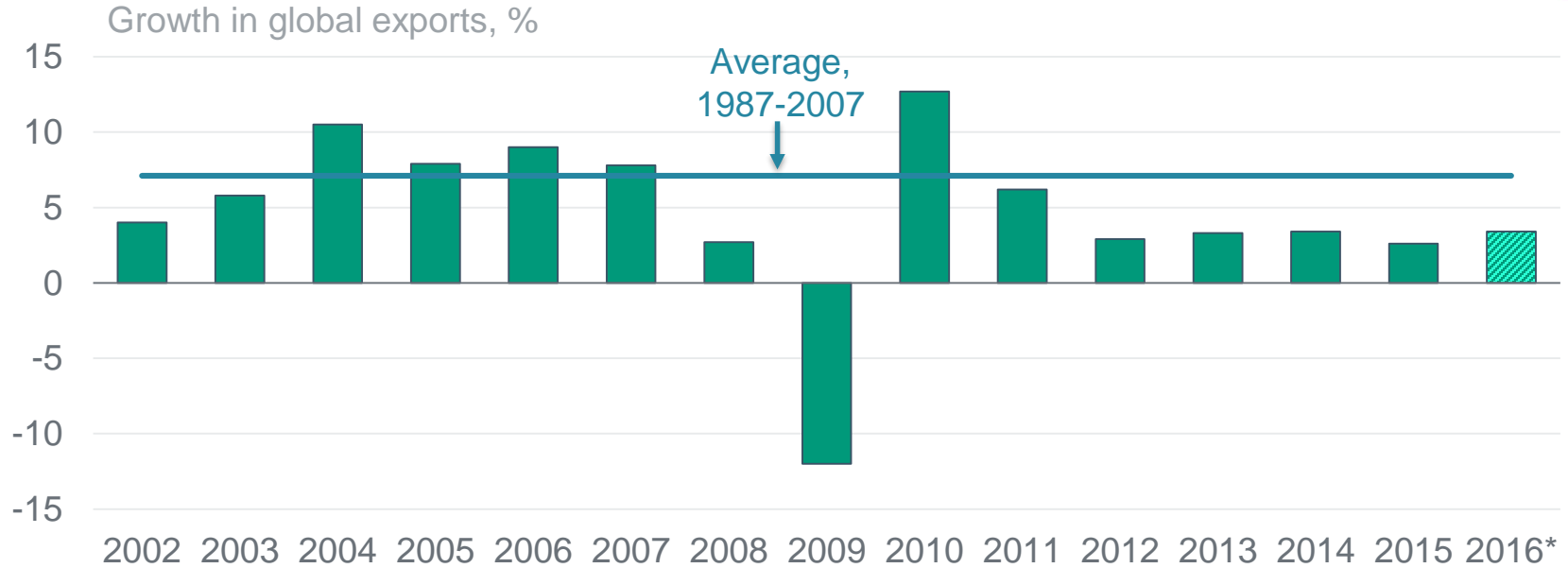
## GLOBAL ECONOMY LOST MOMENTUM POST-2010



## SEVEN PLUS YEARS OF RECORD LOW CENTRAL BANK INTEREST RATES

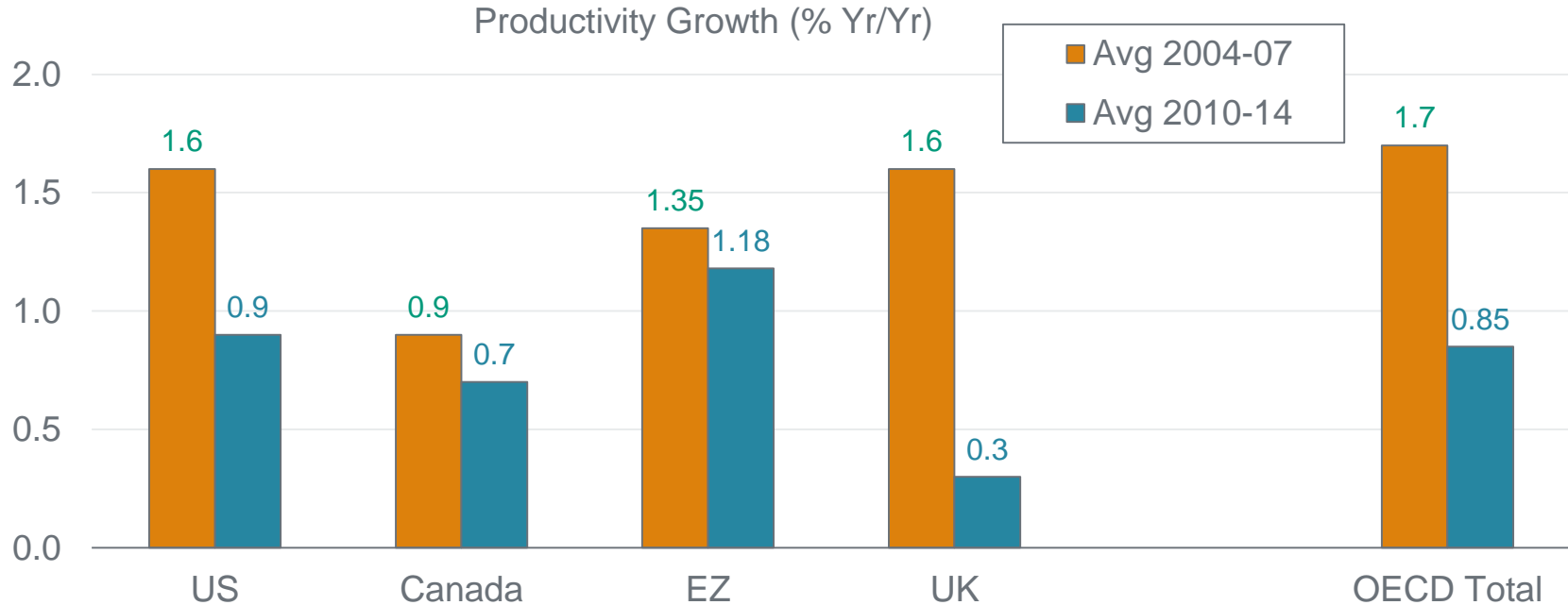


## FALTERING GAINS IN INTERNATIONAL TRADE

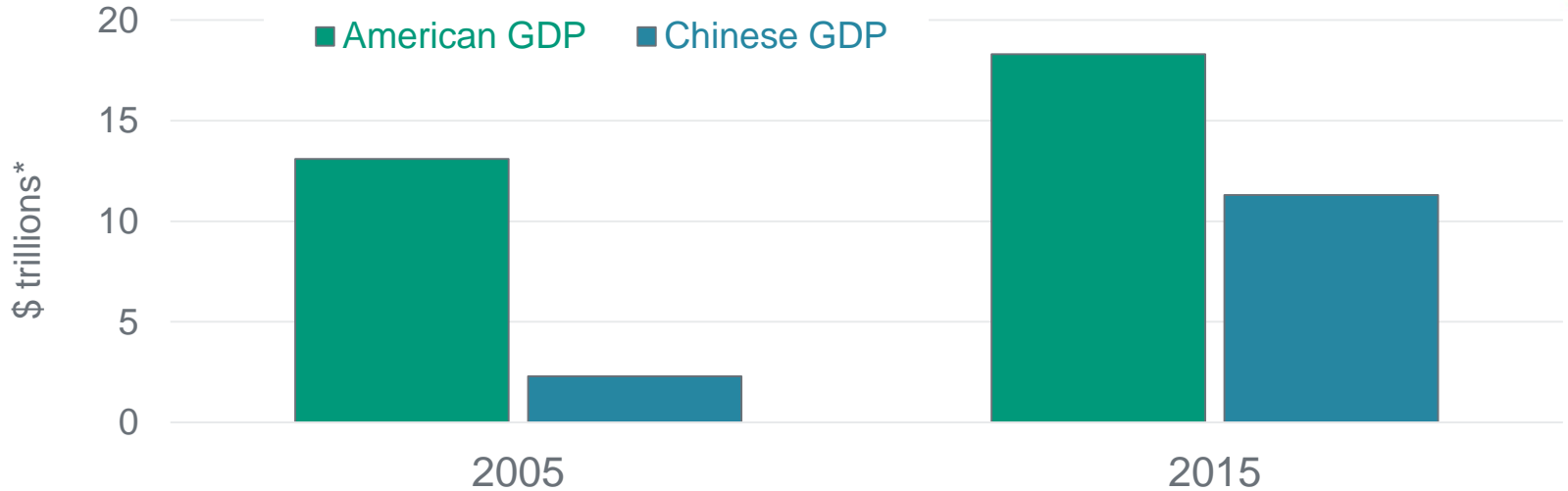




## A SURPRISING PRODUCTIVITY SLOWDOWN ACROSS THE OECD



## CHARTING THE IMPACT OF CHINA'S ECONOMIC RISE



- While its economy has cooled, the extra global spending attributed to China in 2015 was ~2.5 times greater than in 2005, when its economy grew ~12% versus ~6.5% today

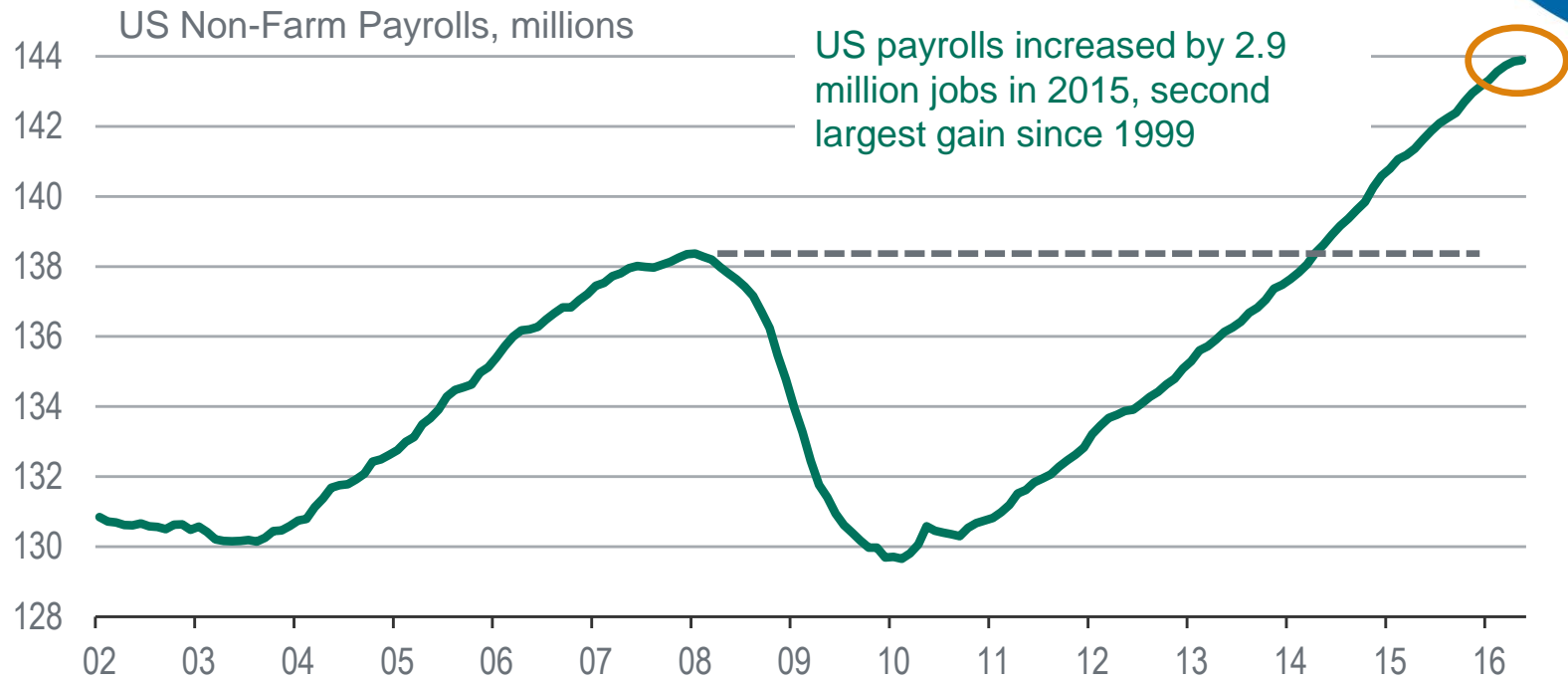
## CHINA'S NEW FIVE YEAR PLAN

- Outlines the shift to a slower economic growth track – revised target of 6.5% per year, enough to double per capita GDP between 2010 and 2020
- Bolster the service sector and lift household consumption as % of GDP over time
- One child policy is eliminated
- Restrictions on the rights of migrants to access social services and permanently settle in cities will be relaxed, gradually
- The government intends to expand pension and healthcare coverage – with the goal of reducing incentives for household savings (circa 30%, vs 6-7% in most OECD countries)
- A continued, step-by-step effort to integrate China into the global financial system...and make the yuan a more widely used currency
- China has developed a strong political focus on advancing economic integration with the rest of Asia (Silk Road Strategy, Asian Infrastructure Bank, etc.)

## AMERICA'S MODEST ECONOMIC EXPANSION CHUGS ALONG

- Real GDP grew 2.4% in 2015, the same as 2014
- But growth eased to just 1.2% (annualized) in the first half of 2016, reflecting the strong US dollar, soft global economy and plunging investment in the oil and gas sector
- However...
  - 73 consecutive months of positive employment gains
  - consumption is trending higher
  - housing starts are slowly climbing, should reach ~1.2 million this year
  - lower energy prices are a (net) economic plus for the US...in the medium-term
  - fiscal drag is diminishing as state/local government budget positions improve
- Recent forecasts suggest the US economy will grow by ~1.7-2.1% (after-inflation) in 2016/17
- Interest rate hikes by the Federal Reserve will be slow to come...if they come...in the next 2 years

## US EMPLOYMENT SURGES



# HOUSING STARTS CONTINUE TO GRIND HIGHER



## GROWTH IN US HOUSEHOLDS: HISTORY AND OUTLOOK

(AVERAGE ANNUAL INCREASE IN NUMBER OF HOUSEHOLDS, OVER THE PERIOD SHOWN)

### History

|           |           |
|-----------|-----------|
| 2004-2007 | 1,216,859 |
| 2007-2010 | 802,066   |
| 2010-2013 | 965,918   |

### Forecasts for 2015-2025

|                 |           |
|-----------------|-----------|
| Low estimate    | 1,160,000 |
| Middle estimate | 1,240,000 |
| High estimate   | 1,320,000 |

## AMERICA'S HUGE ECONOMY MATTERS!

- Estimated US\$18 trillion of GDP this year, equal to almost one quarter of global output (at market exchange rates)
- Consider the size of these US metro areas, in terms of annual output/GDP, relative to the national economies listed adjacent to them:

Metro New York > Australia

LA/Long Beach/Anaheim > Netherlands

Metro Chicago > Nigeria

Greater Houston > Taiwan

Dallas-Fort Worth > Norway

Washington/Arlington > Austria

San Francisco/Oakland > Ireland

Boston/Cambridge > Colombia

Greater Atlanta > Malaysia

Seattle/Tacoma/Bellevue > Singapore

Miami/Fort Lauderdale > Israel

Greater Detroit > Greece

Metro Minneapolis > Portugal

Denver/Aurora > Vietnam

Portland/Vancouver WA > Hungary



## FACTORS SHAPING CANADA'S ECONOMIC PERFORMANCE IN 2016-17

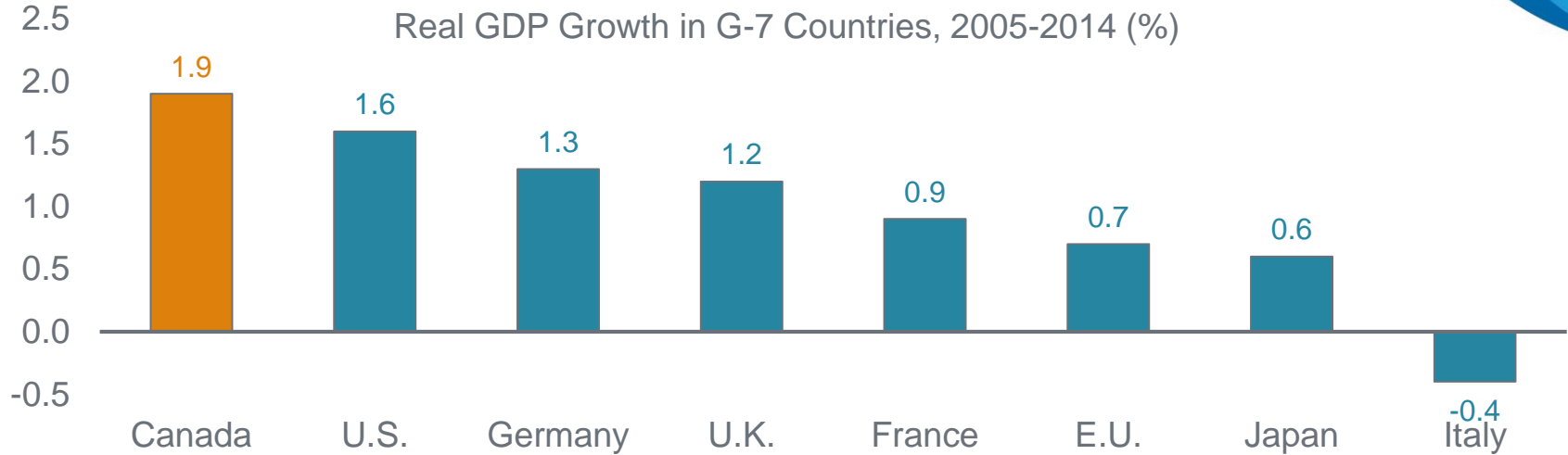
### Negative impact

- Largely tapped out and increasingly indebted consumers – pointing to weaker growth in consumer spending going forward
- Anticipated slowdown in housing-related investment
- Weak/declining business capital spending
- Still sluggish commodity markets (natural resources = 50% of Canada's merchandise exports)

### Positive impact

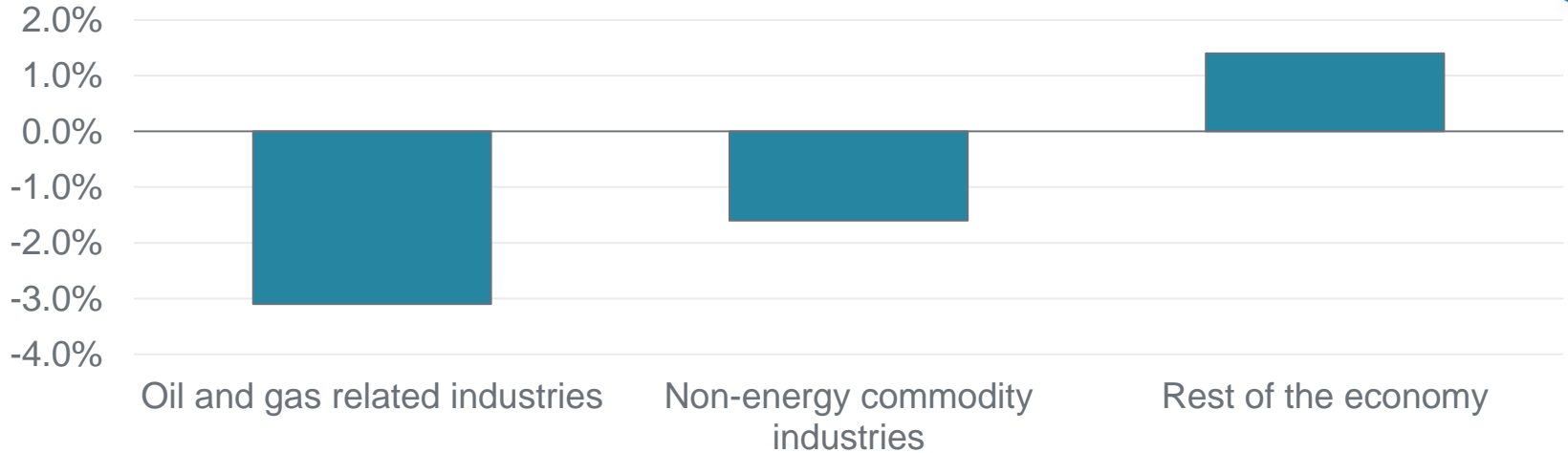
- Federal government budget deficit will provide some near-term support to aggregate demand
- Moderate US economic expansion
- (Some) gains in non-energy exports
- Continued low interest rates and low Canadian dollar

## CANADA LED THE G-7 IN ECONOMIC GROWTH TO 2014



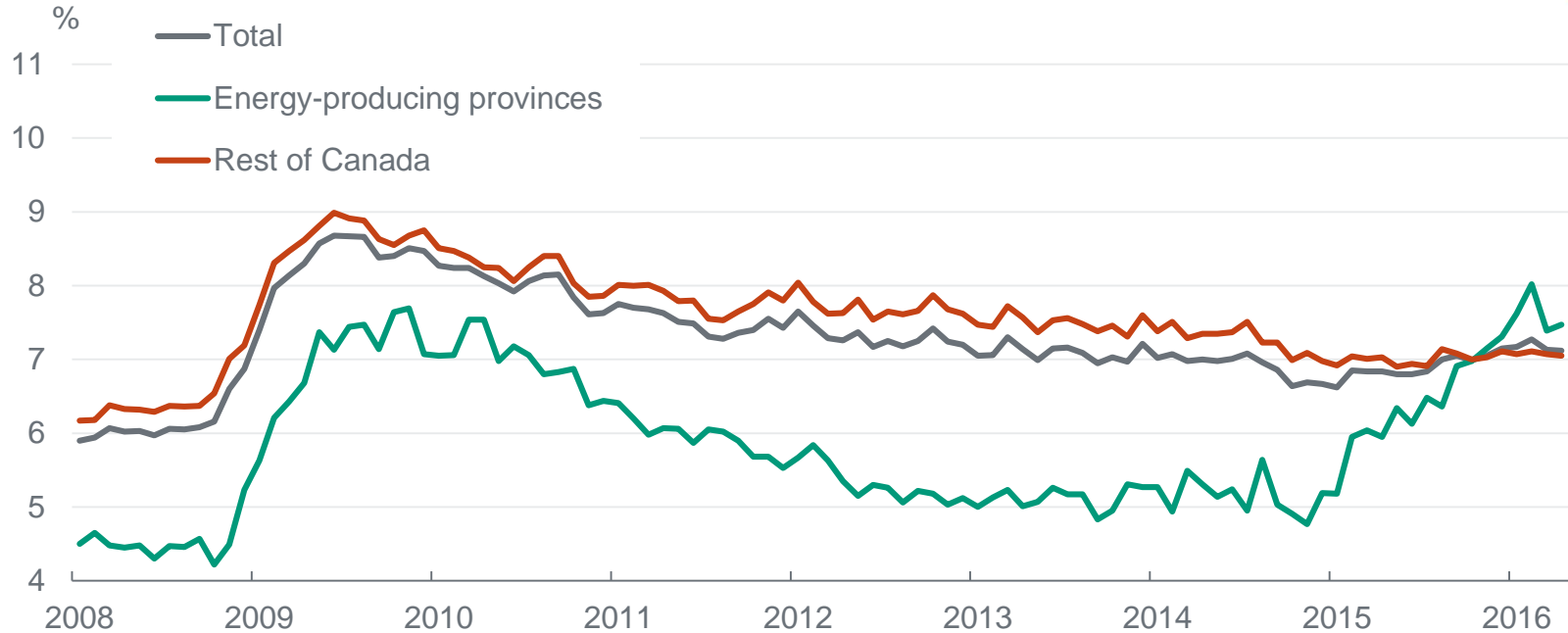
- Data from the OECD place Canada at the top of the G-7 in overall economic growth in the decade ending in 2014

## ...BUT OUR ECONOMY HIT THE SKIDS IN 2015 (Y/Y % CHANGE IN REAL GDP FROM 2014)



- Resource-related industries, representing ~20% of Canadian GDP, have accounted for most of the recent weakness in the Canadian economy

## CANADIAN ECONOMIC ROTATION – UNEMPLOYMENT RATES BY BROAD REGION<sup>1</sup>



## TOP GLOBAL OIL PRODUCERS

| Top Producers <sup>1</sup> | Crude Oil (mmbpd) |                   |
|----------------------------|-------------------|-------------------|
|                            | 2014              | 1993-2013 Average |
| <b>US</b>                  | <b>11.7</b>       | <b>8.1</b>        |
| Russia                     | 10.4              | 8.2               |
| Saudi Arabia               | 9.7               | 7.8               |
| <b>Canada</b>              | <b>4.3</b>        | <b>3.0</b>        |
| China                      | 4.1               | 3.5               |
| Iraq                       | 3.3               | 1.8               |
| Iran                       | 2.8               | 3.3               |
| UAE                        | 2.8               | 2.1               |
| Kuwait                     | 2.8               | 2.1               |
| Mexico                     | 2.8               | 3.3               |

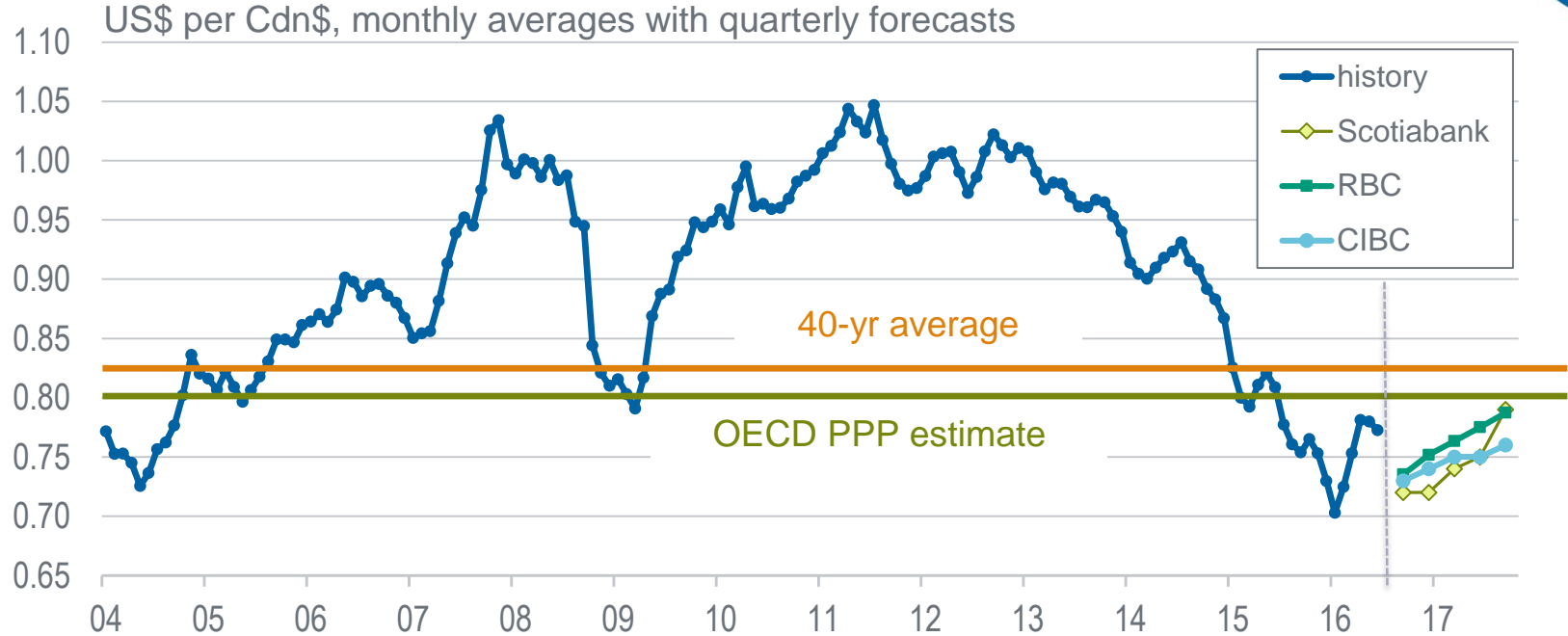
<sup>1</sup> includes products

Source: International Energy Agency.

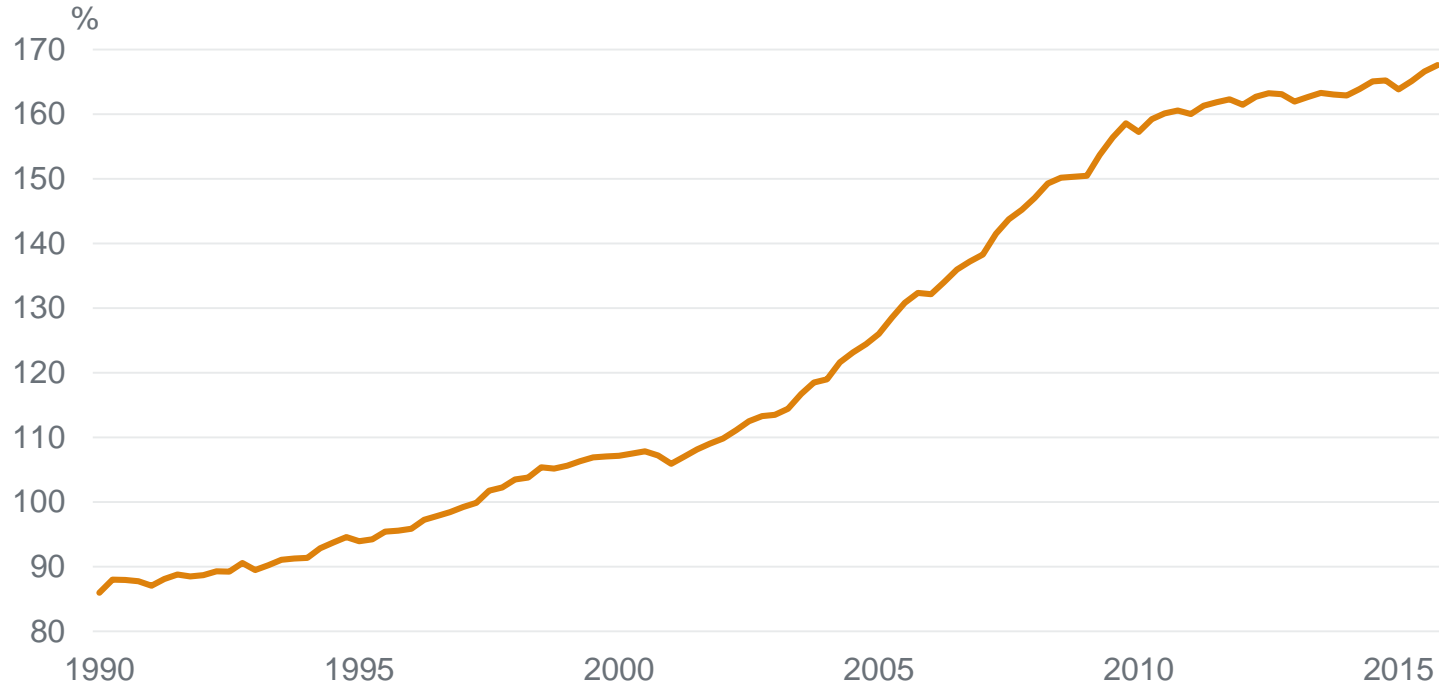
## ENERGY'S PLACE IN CANADA'S EXPORT MIX\*



## A BUMPY RIDE FOR THE CANADIAN DOLLAR

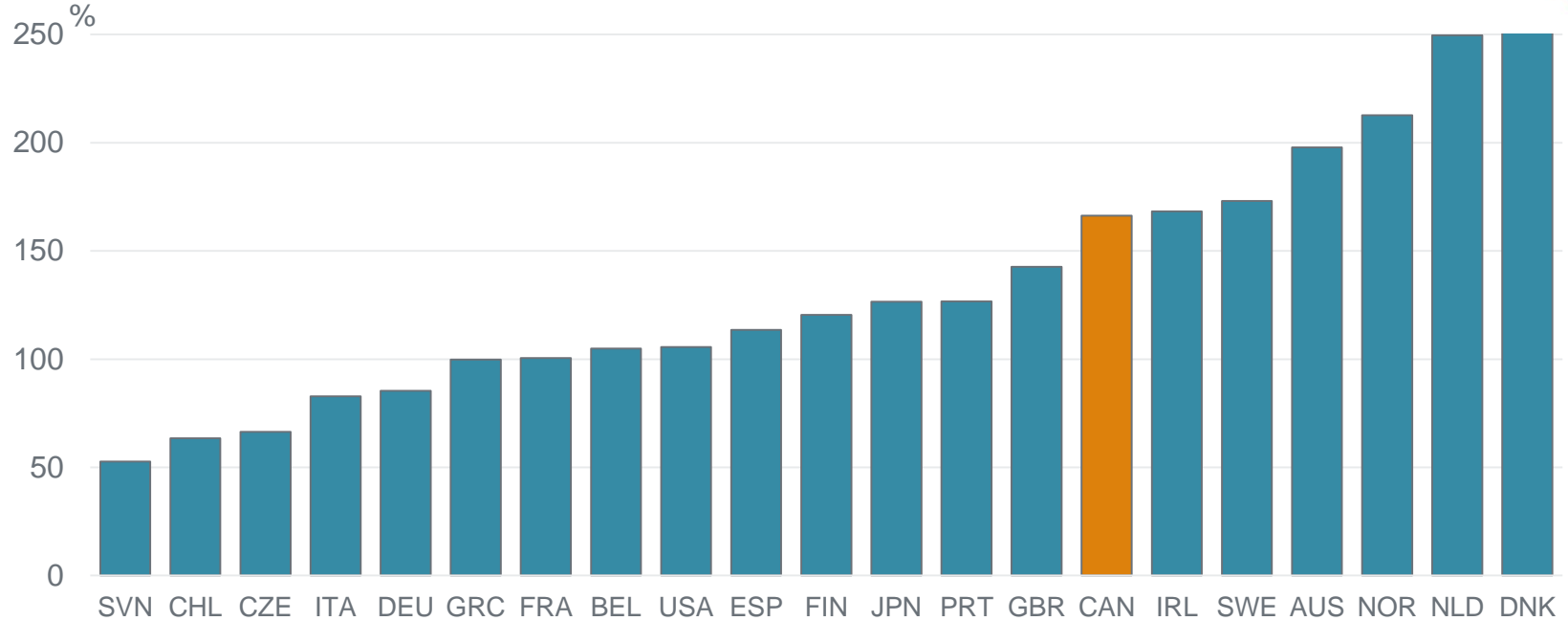


## CANADIAN HOUSEHOLD DEBT TO DISPOSABLE INCOME





## HOUSEHOLD INDEBTEDNESS RATIO, CANADA VS OTHER OECD COUNTRIES, Q4 2015<sup>1</sup>



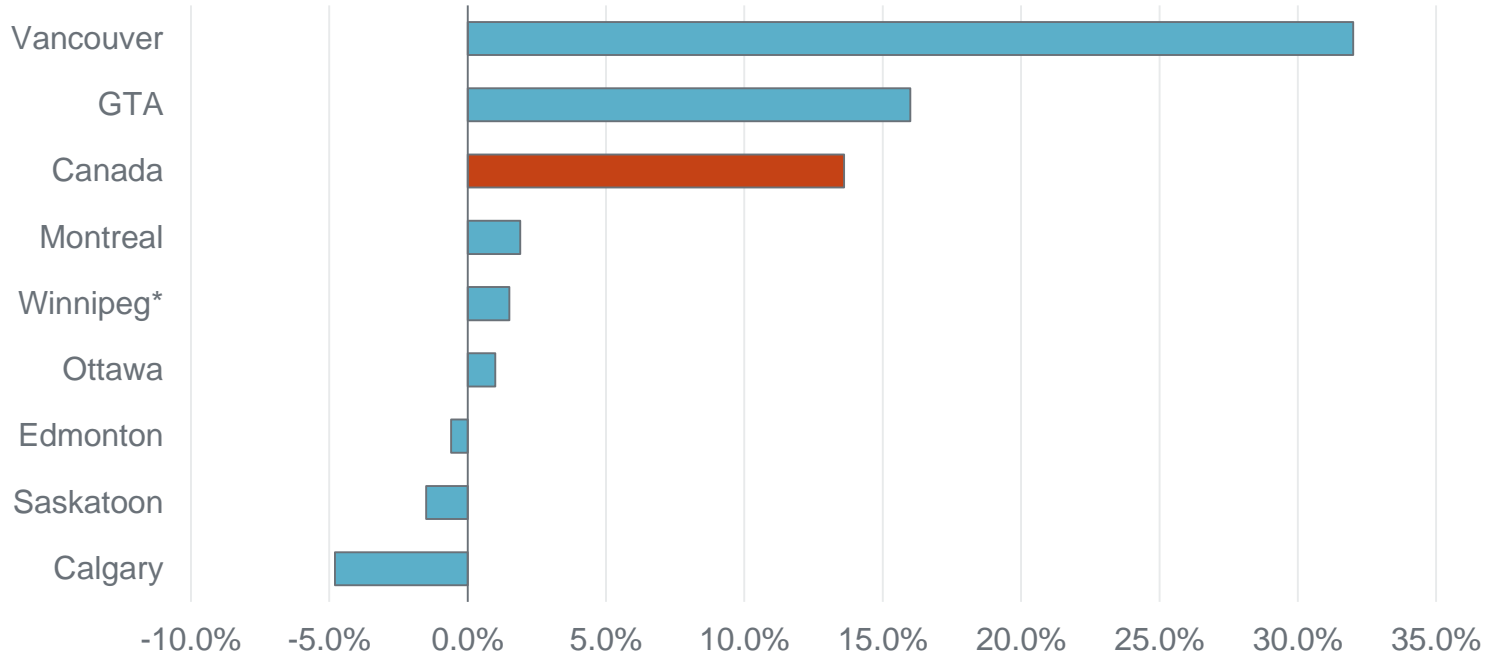
## CANADIAN HOUSEHOLD FINANCES: DEBT UP VS INCOME... BUT NET WORTH ALSO UP AND HOMEOWNERS' EQUITY STABLE

| Indicator                                 | Q1 2005 | Q1 2010 | Q1 2013 | Q1 2016 |
|---|---------|---------|---------|---------|
| Debt-to-disposable income                 | 126     | 157     | 162     | 167     |
| Net worth as a % of disposable income     | 644     | 686     | 755     | 823     |
| Debt to total assets (%)                  | 16.4    | 18.6    | 17.6    | 16.9    |
| Financial assets to non-financial assets  | 112     | 104     | 108     | 111     |
| Owner's equity as % of real estate assets | 74.8    | 73.0    | 73.5    | 73.7    |
| Real estate as % disposable income        | 299     | 355     | 386     | 412     |

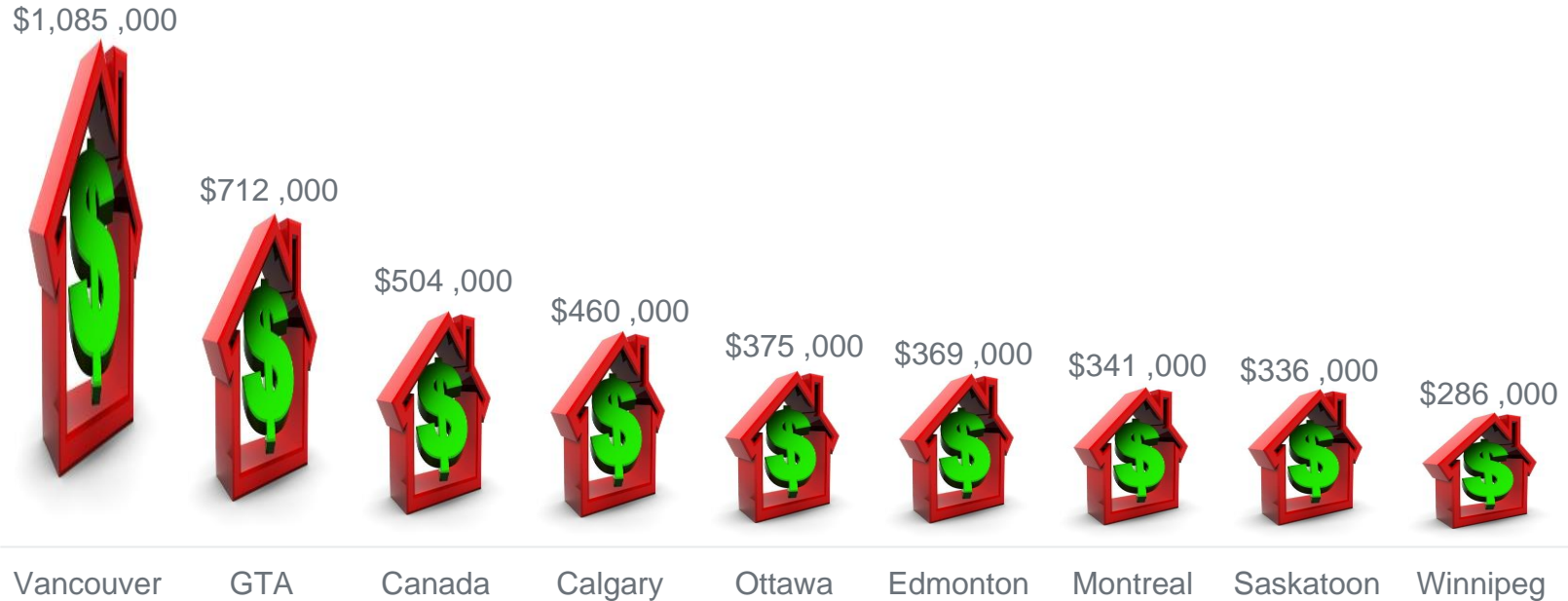
## COMMENTS ON HOUSING SECTOR IN CANADA

- Since 2005, house prices have risen 90% in nominal terms
  - adjusted for inflation, prices have roughly doubled in the last 25 years
- Residential investment has been running above 7% of GDP, vs. long-term average of 5.8%
- Significant regional variation in housing metrics – investment, price trends, sales activity
- More higher-risk mortgages, but no replication of the US sub-prime disaster
- Looking ahead, forecasters expect a slowdown in homebuilding...and modest declines in prices in some parts of the country.
- Credible estimates suggest the ‘national’ housing market is over-valued by 15-25%
- Note that the population ages 25-40 is growing in several metro areas, providing some ongoing support to housing demand
- Foreign money has been playing a significant role in housing markets in Metro Vancouver and the GTA, much less so in other regions

## CANADIAN HOUSING MARKETS...MARCHING TO DIFFERENT DRUMMERS (12-MONTH CHANGE IN EXISTING HOME PRICES, TO JUNE 2016)



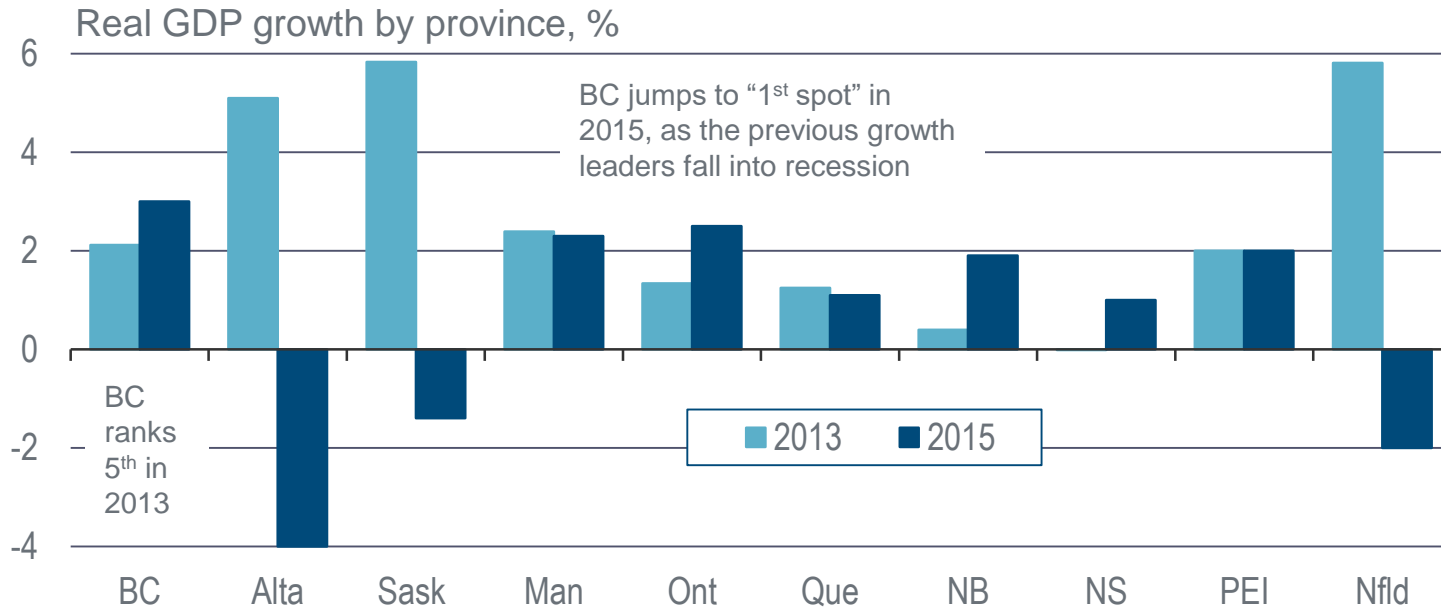
## CANADIAN HOUSING MARKETS...MARCHING TO DIFFERENT DRUMMERS (AVERAGE EXISTING HOME PRICES, MAY 2016)



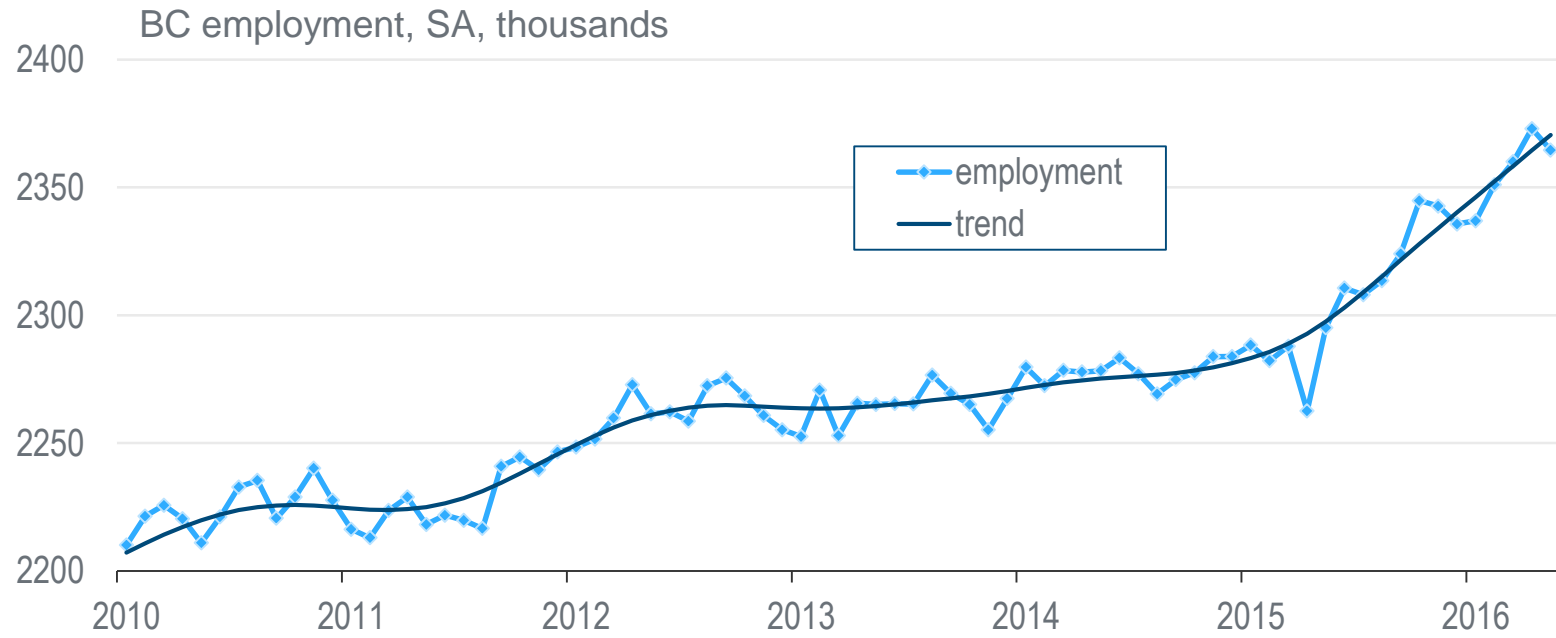
## AN UPDATED ECONOMIC FORECAST FOR CANADA

|                               | 2015       | 2016       | 2017       |
|-------------------------------|------------|------------|------------|
| Real GDP Growth (%)           | 1.1        | 1.2        | 2.0        |
| Nominal GDP Growth (%)        | 0.5        | 1.7        | 4.2        |
| Real business investment (%)  | -10.6      | -8.6       | 1.2        |
| Unemployment rate (%)         | 6.9        | 7.0        | 6.9        |
| 3-month T-bill rate (%), Q4   | 0.45       | 0.53       | 0.76       |
| 10-yr gov't bond rate (%), Q4 | 1.52       | 1.12       | 1.41       |
| Canada/US dollar, Q4          | 74.9 cents | 76.1 cents | 78.3 cents |

## BC'S RELATIVE ECONOMIC POSITION DEPENDS ON HOW OTHER PROVINCES PERFORM

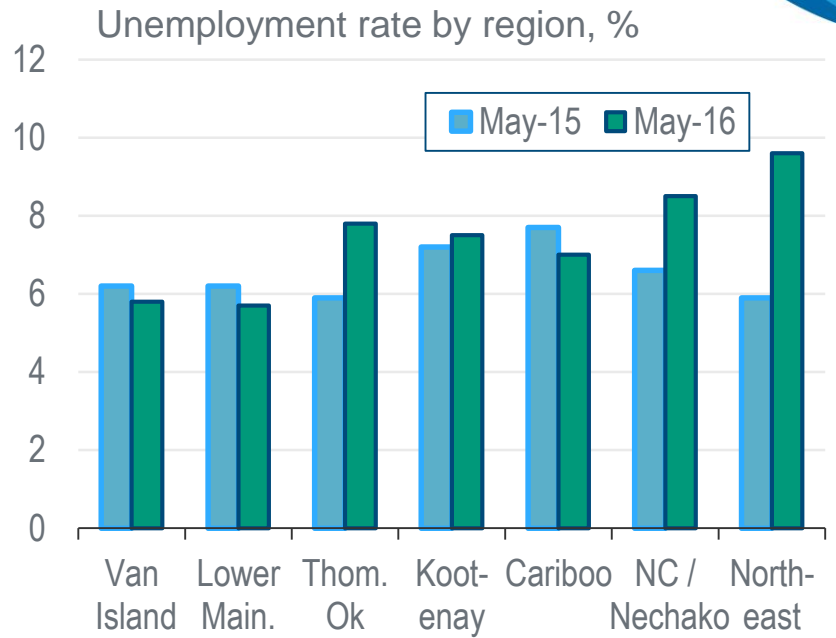
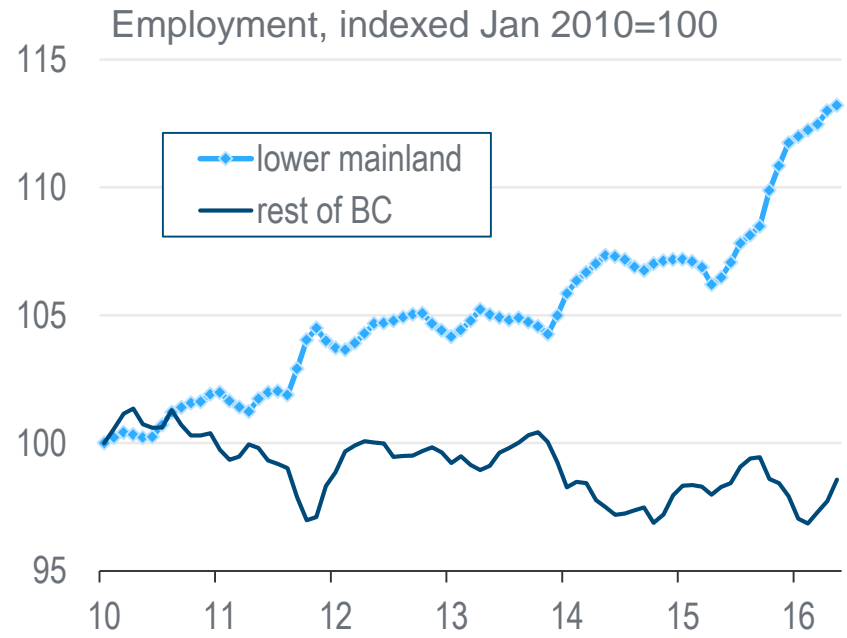


## THE BC JOB MARKET HAS DEFINITELY PICKED UP





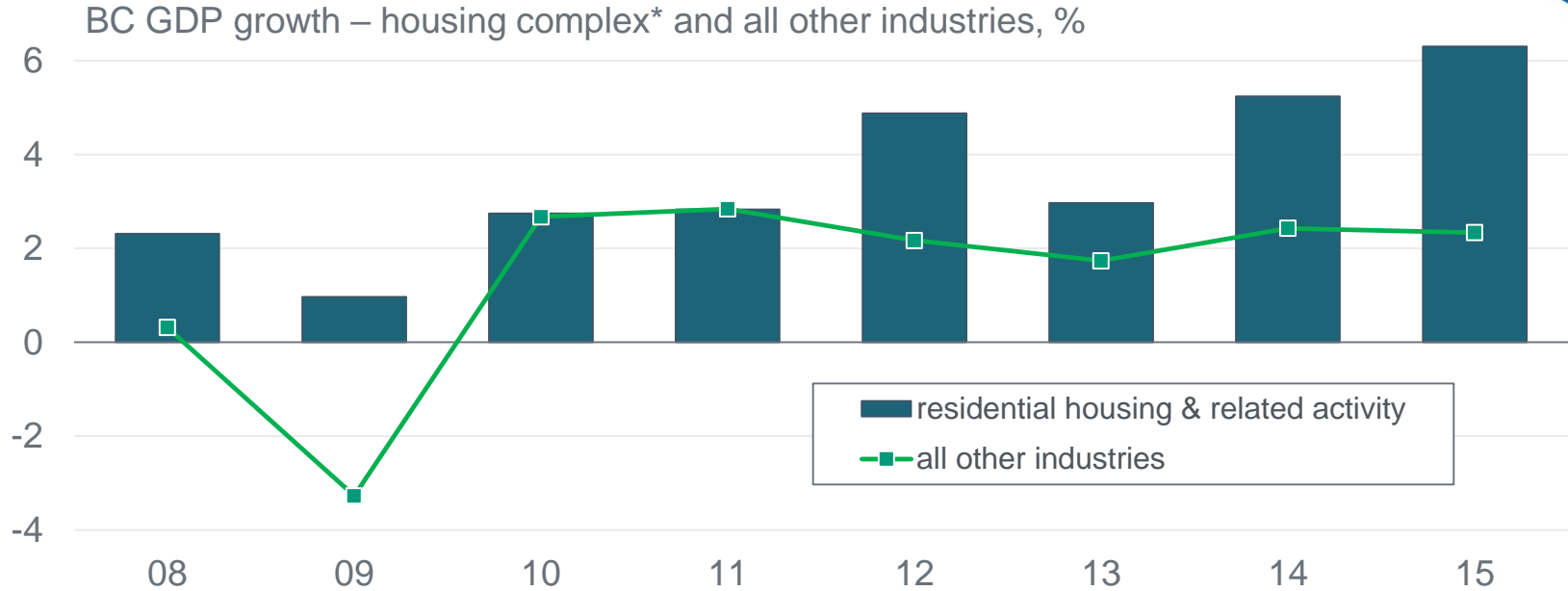
## BUT...ALL JOB GROWTH HAS BEEN CONCENTRATED IN THE LOWER MAINLAND



## US NOW DRIVING BC EXPORT GAINS



## HOUSING IS PROVIDING A BIG ECONOMIC LIFT FOR BC



\* Includes residential construction, offices of real estate agents and related, and imputed rent.

Source: Source: Statistics Canada, CANSIM table 384-0038, data released November 10, 2015..  
BC Ministry of Finance, Budget and Fiscal Plan for forecasts

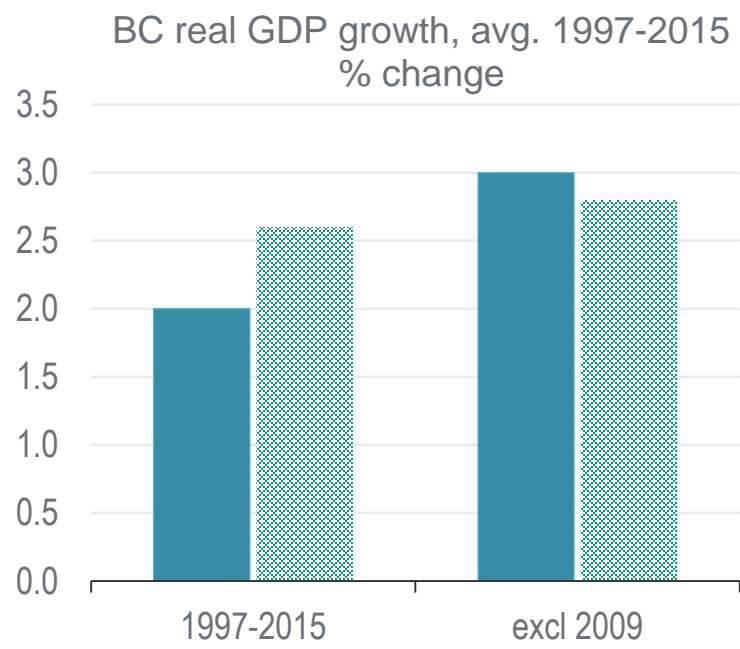
## BC'S MAIN TRADED INDUSTRIES – VALUE OF EXPORTS 2015

|   |                       |
|---|-----------------------|
| <u>Forestry</u>                               |                       |
| Wood products                                 | \$8.5 billion         |
| Pulp and paper                                | \$4.4 billion         |
| <b>Total forestry</b>                         | <b>\$12.9 billion</b> |
| <b><i>Forestry as % of total exports*</i></b> | <b>36%</b>            |
| <u>Others</u>                                 |                       |
| Metallic minerals                             | \$4.4 billion         |
| Machinery and equipment                       | \$4.8 billion         |
| Coal  | \$3.1 billion         |

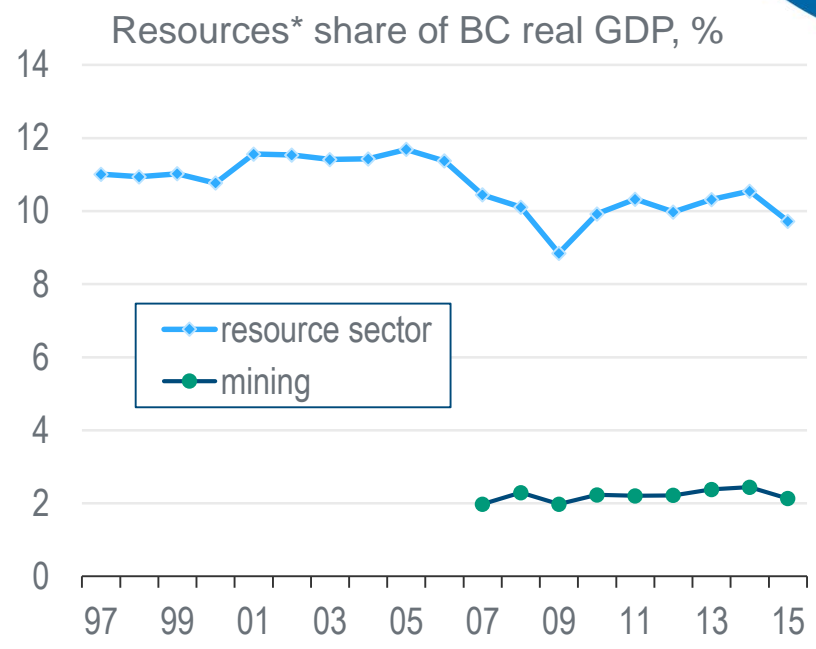
|                                |                       |
|--------------------------------|-----------------------|
| <u>Others (cont'd)</u>         |                       |
| Natural gas                    | \$1.4 billion         |
| Agrifood products              | \$2.7 billion         |
| Fabricated metals              | \$1.1 billion         |
| Fish products                  | \$1.1 billion         |
| Chemical products              | \$1.1 billion         |
| Plastics                       | \$426 million         |
| Apparel etc.                   | \$124 million         |
| <b>Total BC goods exports:</b> | <b>\$35.8 billion</b> |

BC also has service industry clusters that engage in international trade, of which the most important are tourism (~\$4 billion of exports), transportation, communications (incl. software), education, engineering, and technical/scientific/environmental services

## RESOURCES STILL IMPORTANT



■ resource sector\*    ■ rest of economy



Source: Statistics Canada

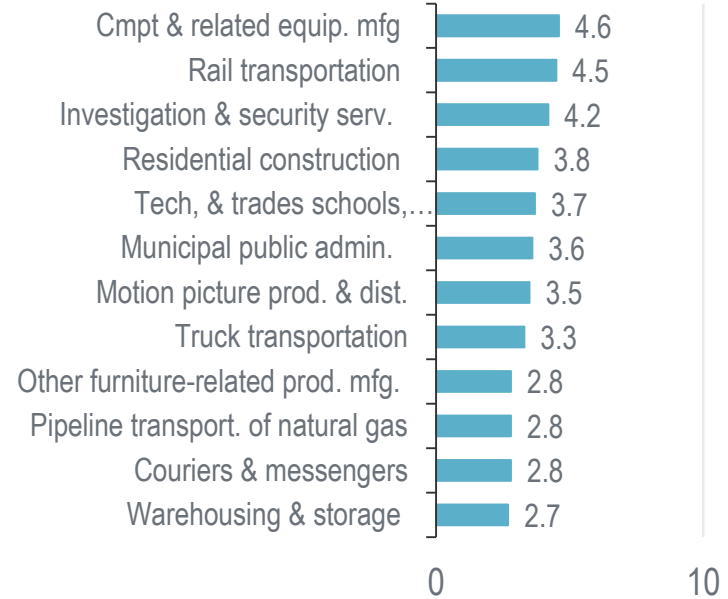
\* includes forestry, mining, oil and gas and related support activities and processing.

## LEADING GROWTH INDUSTRIES COME FROM A MIX OF SECTORS

BC top growth industries 1997-14  
average annual % change



BC top growth industries 1997-14  
average annual % change



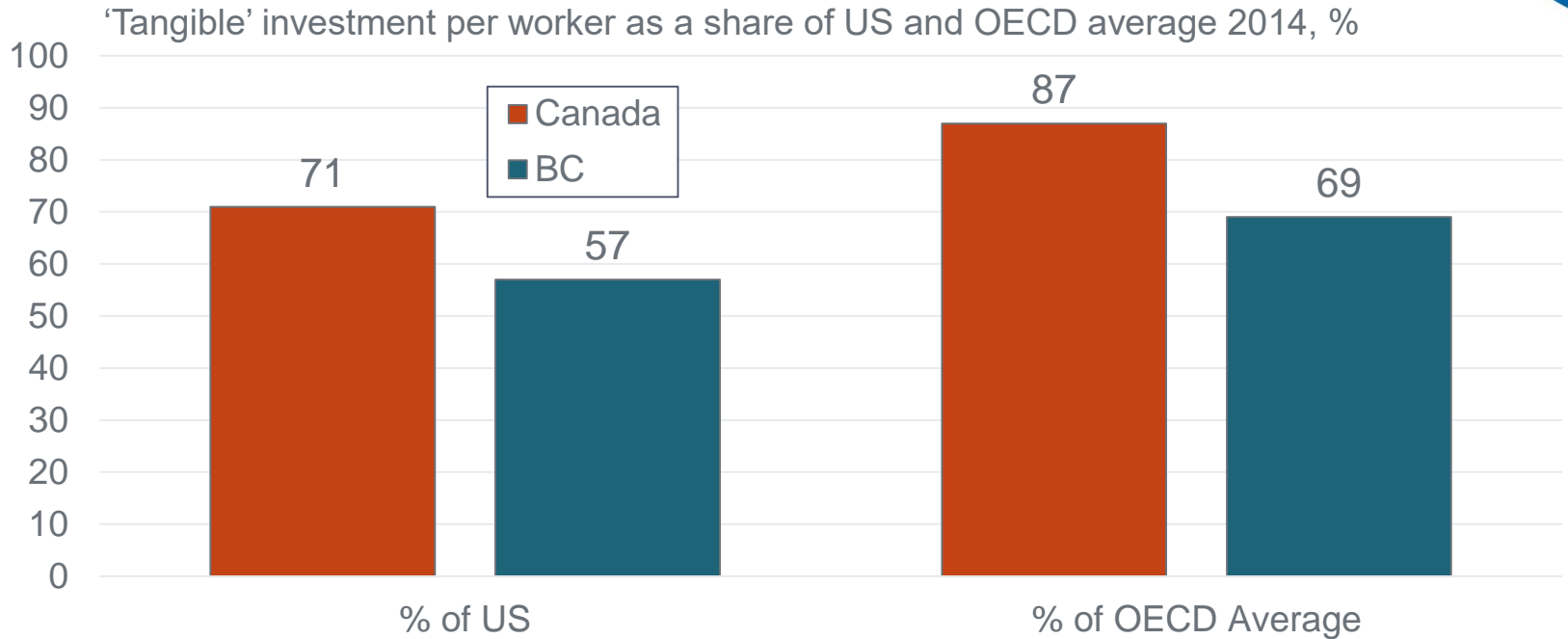
Source: Statistics Canada.

## BC ECONOMIC OUTLOOK

(ANNUAL % CHANGE UNLESS OTHERWISE INDICATED)

|                            | 2014 | 2015e | 2016f | 2017f |
|----------------------------|------|-------|-------|-------|
| Real GDP                   | 3.2  | 3.0   | 2.7   | 2.6   |
| Employment                 | 0.6  | 1.2   | 3.0   | 1.5   |
| Unemployment rate (%)      | 6.1  | 6.2   | 6.1   | 5.9   |
| Housing starts (000 units) | 28.4 | 31.4  | 39.0  | 38.0  |
| Retail sales               | 5.5  | 6.5   | 6.5   | 5.5   |
| BC CPI                     | 1.2  | 1.1   | 1.6   | 1.6   |

## BC LAGS IN CAPITAL INVESTMENT





## RECAP

- Today's choppy and risk-prone global economic environment, featuring unusually low inflation, near-zero policy interest rates, and weak business investment, looks set to persist
- Amid lower commodity prices and a financially stretched household sector, Canada is struggling to find a new growth platform that is less energy- and resource-driven
- BC is outpacing Canada in GDP and job growth, reflecting a rising population, strength outside of the resource sector, and frothy housing markets
  - BC's relative outperformance should continue over 2016-17
  - LNG could still produce an 'upside surprise' in 2017-18
- Looking further ahead, BC, like Canada as a whole, faces challenges stemming from the expected fall-off in the economy's growth potential, declining competitiveness in key traded goods industries, housing affordability issues in urban areas, and widening regional disparities in demographic and economic performance