Economic Trends

While the province continues to recover from the recession, the pace of growth has started to moderate. Job gains have stalled after making significant headway in the first half of the year, but retail sales and residential construction continue to improve. Activity in conventional oil and gas remains solid; however, lower oil prices and production outages earlier in the spring are weighing on the value of goods exports and manufacturing shipments. This month's InFocus looks at Alberta's interprovincial trade flows using the latest available data from 2013.

Key Indicators

Seasonally adjusted unless otherwise indicated.

Indicator	Latest Month	Value	Change year-over-year (y/y)
Alberta Activity Index (y/y growth)	July	+6.3%	+16.3p.p.
Employment (thousands)	August	2,287	+1.5%
Unemployment Rate	August	8.1%	-0.4p.p.
CPI Inflation (unadjusted)	August	1.1%	+0.4 p.p.
Retail Sales	July	$6.8 B	+9.5%
Housing Starts (annualized)	August	26,154	+32.9%
Rigs Drilling (unadjusted)	September	127	+59.8%
Manufacturing Shipments	July	$5.8 B	+9.7%
Exports (unadjusted)	July	$7.6 B	+23.8%

Source: Alberta Treasury Board and Finance, Statistics Canada, CAODC, CMHC. p.p.= percentage points.

Household Sector

Population growth moderating

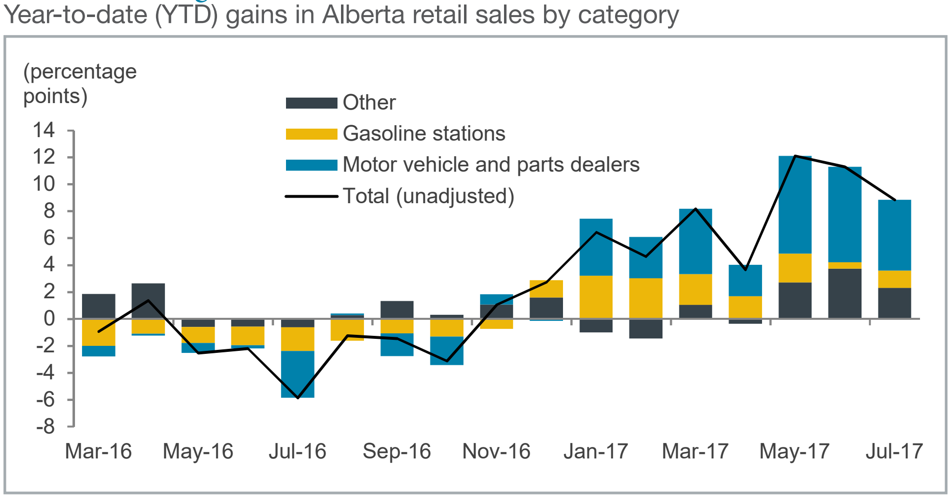
Alberta's population growth slowed again in the second quarter to dip below the national average. Alberta's population stood at 4,286,134 as of July 1, 2017, an increase of 13,736 people (+0.32%) from the previous quarter. While natural increase and international migration remained strong, continued net outflows of interprovincial migrants weighed on population growth. These continued outflows were largely due to fewer people coming into the province rather than people leaving the province compared to recent years. On a year-over-year basis, Alberta's population grew by 1.17%, the slowest year-over-year growth for the second quarter since 1988. Alberta's population growth has been slowing since 2013.

Employment takes a breather

After a solid first half of the year, employment gains stalled in the summer. Alberta added a modest 2,300 jobs in August following a sharp pullback in July. With the economy recovering, a growing number of full-time positions and hours have drawn more Albertans back into the labour force, which resulted in a surge in the province's participation rate in August. This, combined with the slower pace of job gains, has put upward pressure on the unemployment rate. It went up 0.7 percentage points to 8.1% in August.

Chart 1: Broad gains in retail sales

Year-to-date (YTD) gains in Alberta retail sales by category



Source: Statistics Canada

Strong consumer spending

Albertans continue to spend amid the economic recovery. The improvement in retail sales has been led by sales at motor vehicle and parts dealers and in particular, new trucks sales (+16.6% year-to-date or YTD). Although truck sales receded in July from a high set in the previous month, other categories are now contributing to growth (Chart 1). With nearly all categories gaining ground, retail sales are up 8.0% YTD and are above pre-recession peak.

Single-detached boosts starts

Single-detached housing starts are driving the recovery in Alberta's residential construction. Single-detached starts continue to improve from 2016 levels (+50.5% year-over-year or y/y) and are up nearly 35% YTD. Meanwhile,

Alberta Government

September 2017
Treasury Board and Finance
Economics and Revenue Forecasting

the number of single-family homes under construction has increased since November 2016 to hit a twenty one-month high in August. On the other hand, multi-unit starts pulled back to a seven-month low after surging earlier in the year, weighed down by elevated inventories of completed and unabsorbed apartment units. As a result, overall housing starts cooled in August after five months of robust activity, but are still up 36% from last year.

Business Sector

Solid activity in conventional oil and gas

Activity in Alberta's conventional oil and gas sector remains robust, despite the slower pace of rigs drilling. Drilling activity usually picks up in June following spring break-up, but the seasonal upturn this year has not been very strong, likely weighed down by lower oil prices over the summer and rig efficiency gains. Despite the slower pace, average rigs drilling has nearly doubled year-to-date. Similarly, the total number of metres drilled for oil and gas has more than doubled compared to last year, led by a significant increase in metres drilled for conventional oil. As a result, the average number of metres drilled per well held close to its ten-year high for the month of July. The use of more efficient technology led to a significant increase in metres drilled per well during the two-year downturn. Land sales in Alberta's conventional sector have also risen sharply this year, with sales in the first nine months of this year surpassing total annual sales in 2016 and 2015.

Exports and manufacturing shipments slide

Exports and manufacturing shipments retreated in June and July after a solid run over the past year. The value of goods exports fell by nearly 14% over the two months (Chart 2). Energy exports contributed to most of the decline, largely pulled down by lower energy prices and fire-related outages at Syncrude's upgrader facility which started in mid-March. Non-energy exports also slipped, led by a pronounced decline in agricultural and forestry products which both retreated from the multi-year highs seen earlier in the spring. Similarly, manufacturing sales of petroleum and coal products took a hit from lower oil prices, although shipments of other major categories such as chemicals and food manufacturing products also slid. Despite the setback, business output in the province continues to far exceed recessionary levels.

Construction sector lagging

Continued weakness in private non-residential investment is dampening the recovery in Alberta's construction sector. Non-residential building construction investment has fallen steadily since peaking in the first quarter of 2015. Commercial construction is responsible for most of the weakness, with investment in the second quarter of 2017 falling to a six-year low. There was no offset from governmental and institutional building, which slipped in the second quarter for the first time since 2014 after hitting a six-year high. Although there's been some improvement in industrial construction so far this year, building permits, a leading indicator of construction activity, suggest that both industrial and commercial spending will remain subdued for the remainder of this year. Declines in the non-residential sector have been somewhat countered by an improvement in residential investment, which was up over 5% y/y.

Chart 2: The value of business output steps back in recent months

Total value of goods exports and manufacturing shipments

Source: Statistics Canada

Outside Alberta

Canada to lead growth in major economies

With stronger-than-expected growth in the first half of the year, Canada is on track to be the fastest growing major economy in 2017. Canadian real GDP growth accelerated to an average annualized pace of about 3% in the first two quarters of the year, driven by a surge in energy exports, robust consumer spending and continued improvement in business investment. In contrast, the US and EU grew more modestly at 2.1 and 2.3%, respectively. The Organization of Economic Cooperation and Development is now projecting the Canadian economy to grow by 3.2% while the US and EU are forecast to grow by 2.1% in 2017.

BoC embarks on rate hike cycle

In light of increased momentum in the Canadian economy, the Bank of Canada (BoC) began tightening its monetary policy in the summer after nearly seven years of no rate hikes. The BoC raised interest rates twice in the last three months, reversing the emergency rate cuts it implemented in 2014 and 2015 following the oil price collapse. This brought the overnight target rate to 1.0%. Meanwhile, the US Federal Reserve has taken a pause after three rate increases since December 2016 but announced the gradual reduction of its $4.5 trillion balance sheet starting in October.

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Alberta's Interprovincial Trade Flows

Interprovincial trade flows account for a large percentage of Alberta's external trade and form an integral part of the Alberta economy. Interprovincial trade tends to get less attention than international trade, in part, because of a lack of data. Detailed statistics on interprovincial trade are published with a four-year lag, with 2013 being the most recent. This inFocus attempts to shine some light on this important aspect of Alberta's economy using the most recent data for 2013.

Interprovincial trade in perspective

Alberta's interprovincial trade of goods and services (exports plus imports) with the rest of Canada was about $145 billion in 2013. Interprovincial trade was 24% smaller than international trade and accounted for 38% of Alberta's exports and 47% of imports. When it comes to services, however, interprovincial trade dominates, representing almost 80% of Alberta's trade in services. Alberta has the second largest interprovincial trade volume in the country after Ontario.

Size and distance drive trade

Size and distance largely determine the volume of trade between Alberta and other provinces. Alberta's top three trading partners are Ontario, the largest economy, and the neighbouring provinces of Saskatchewan and BC. Ontario accounts for 40% of Canada's population and nominal GDP making it the largest market in the country and Alberta's largest interprovincial trading partner. Alberta's exports to Ontario in 2013 totaled $28 billion and imports totaled $34 billion (Chart 1).

Quebec is the second most populace province in Canada and about five times bigger than Saskatchewan in terms of GDP. However, proximity outweighs market size as Alberta's bilateral trade with Saskatchewan in 2013 was about 16% more than with Quebec. Similarly, despite Ontario having a larger economy, BC exports more to Alberta.

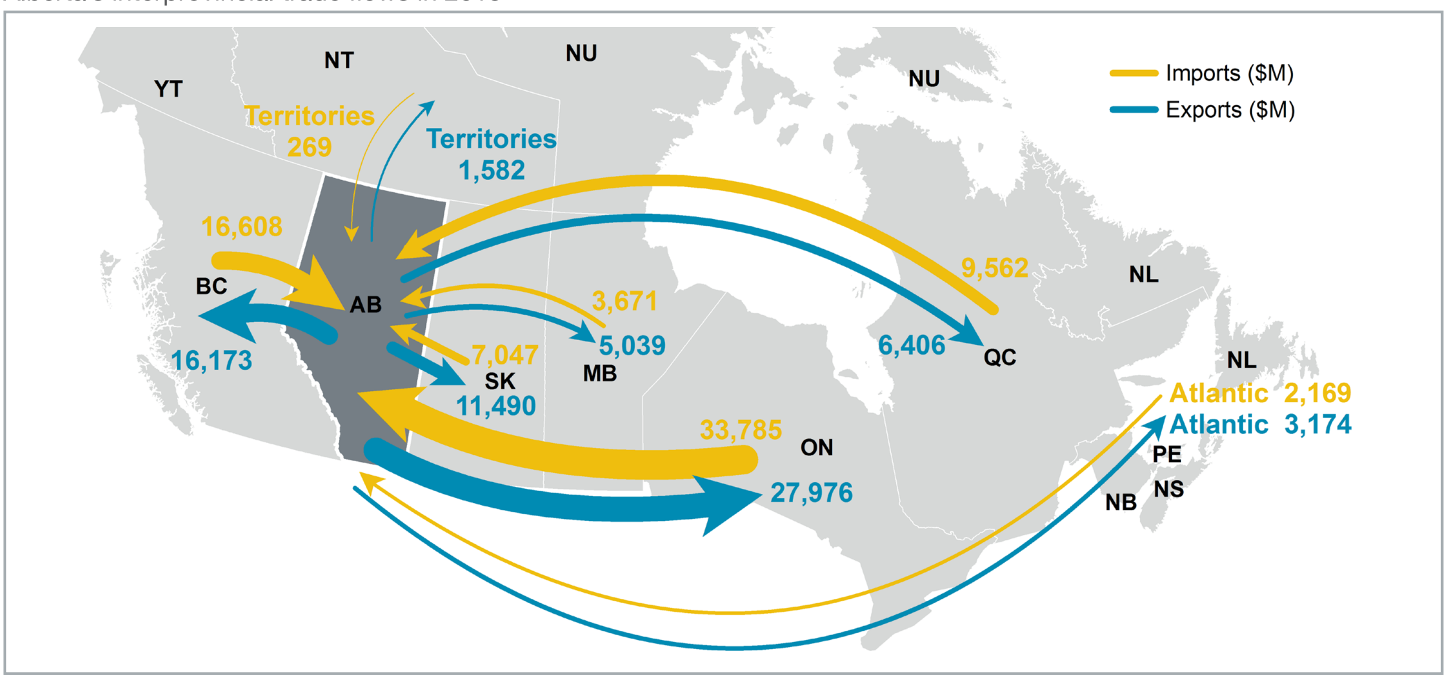
Oil and gas supply chains

Supply linkages between Alberta and other provinces are a major determinant of the composition of Alberta's interprovincial trade. This is especially true for the oil and gas industry where exports of mineral fuels (crude and synthetic oil), refined petroleum products, and mineral support services (example drilling) accounted for 39% of Alberta's interprovincial exports.

The main oil and gas producing region in BC is in the northeast and most easily accessible from Alberta. As such, BC relies heavily on the Alberta oil and gas industry to develop these resources. Around two-thirds of the oil and gas support services consumed in BC were

Chart 1: Trade flows influenced by size and distance

Alberta's interprovincial trade flows in 2013



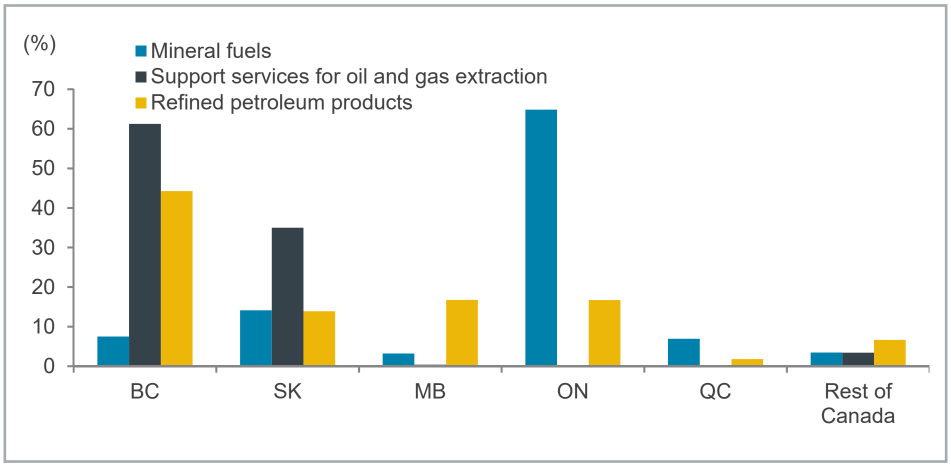
Source: Statistics Canada

imported from Alberta. Once these wells are drilled and pumping, oil and natural gas flows from northern BC into the gathering system in Alberta and onto other markets. While Saskatchewan is much less reliant on Alberta, about one-third of the oil and gas support services and refined products consumed in Saskatchewan were imported from Alberta.

Alberta is host to the largest refining capacity in the country. Manitoba, Saskatchewan, and BC were the recipients of three quarters of Alberta's interprovincial exports of refined petroleum products. The largest share of Alberta's refined products is consumed in BC as demand far outstrips BC's limited refining capacity. Ontario has sufficient refining capabilities to supply the domestic market, but lacks domestic sources of crude oil. As such, nearly 65% of Alberta's interprovincial exports of mineral fuels, were exported to the Ontario market (Chart 2). In return, Alberta was the recipient of $1.5 billion of Ontario's primary metals, such as iron and steel. These metals are used in Alberta's manufacturing sector and go into the construction of buildings and oil and gas facilities.

Chart 2: Refining capacity determines energy exports

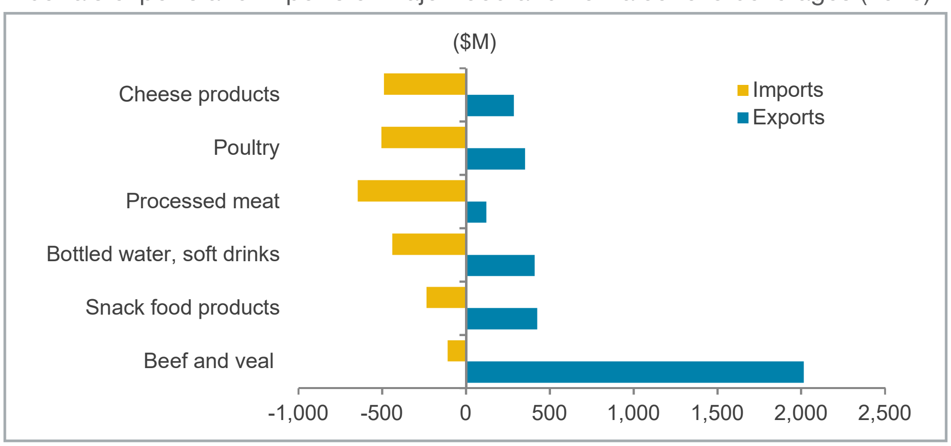
Share of Alberta's interprovincial energy exports by destination



Source: Statistics Canada

Chart 3: Comparitive advantage in food products

Alberta's exports and imports of major food and non-alcoholic beverages (2013)



Source: Statistics Canada

Food, finance and comparative advantage

Comparative advantage is an important determinant of the composition of interprovincial trade. For example, food and non-alcoholic beverages are Alberta's top goods import and one of its top exports. The province enjoys a comparative advantage in exporting frozen beef and veal to other provinces while importing poultry, cheese and processed meat. Over 80% of all frozen beef and veal products traded within Canada originates from Alberta. Alberta receives 60% of its food imports from Quebec and Ontario.

Another example of the impact of specialization is in the trade of financial services, where the financial hubs in Toronto and Montreal give Ontario and Quebec a comparative advantage. Alberta imported over $10 billion worth of banking and financial services in 2013, the bulk coming from Ontario and to a lesser extent Quebec. Alberta is most dependent on interprovincial trade for insurance. Just over 40% of the insurance services consumed domestically are imported from other provinces. Despite being a net importer for almost all types of finance and insurance services, Alberta was the largest interprovincial exporter of portfolio management services in 2013.

Conclusion

As the fourth most populous province in Confederation and the third largest economy, Alberta plays a unique role in interprovincial trade flows. Alberta has the second largest internal trade volumes of any province and is the leading supplier of beef and energy products for the country. With recent pacts, such as the Canadian Free Trade Agreement (CFTA), new trade opportunities are likely to open up between Alberta and the other provinces.

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