

BUDGET PAPER A: BACKGROUND NOTES ON THE ECONOMY

Highlights

- Estimates of economic growth for Prince Edward Island, as measured by constant dollar Gross Domestic Product, suggest that the Province expanded by 1.8 per cent in 1998, which compares to a national rate of growth of 3 per cent. The rate of growth of GDP for Prince Edward Island in 1997 is recorded as 1.2 per cent by Statistics Canada whereas forecasters had expected a modest decline that year, in view of the loss of construction work upon completion of the Confederation Bridge. Thus overall the Prince Edward Island economy has been expanding, but at a rate of growth less than the national rate.
- The leading growth sectors in the Provincial economy in 1998 were tourism, retail sales and manufacturing. By contrast, the sector that experienced some economic difficulty was agriculture. Decreased agricultural production was largely the result of a reduced potato harvest, coupled with a sharp fall in cash receipts from hog sales which caused significant financial problems for hog producers.
- Total employment on Prince Edward Island increased from 60,500 in 1997 to 60,900 in 1998. Growth of employment on the Island in 1998 was very limited as the numbers employed in goods production fell from 17,400 in 1997 to 17,100. The services sectors provided employment for 43,700 Islanders in 1998, an increase of 600 from the previous year. The unemployment rate did decline during the year, from 14.9 per cent in 1997 to 13.9 per cent in 1998. However Statistics Canada estimates that the population of Prince Edward Island in 1998, at 136,400 was below the level of 136,800 attained in 1997, as a result of interprovincial migration.
- Growth of personal income on Prince Edward Island in 1998 was very modest, at an estimated 1.6 per cent, largely due to a 2.8 per cent reduction in the value of Employment Insurance Benefits, which counteracted the positive impact of gains to earned incomes. As a percent of the Canadian average, personal income per person Prince Edward Island slipped from 81.7 per cent in 1997 to an estimated 80 per cent in 1998. In 1999 income growth is expected to rise to 2.1 per cent.
- Islanders benefited from a significant reduction in consumer prices in 1998 as the All Items Consumer Price Index fell by 0.5 per cent. The main cause of this decline was a sharp drop in energy costs which decreased overall by 11 per cent. The CPI for non Energy items increased by 1.3 per cent.

Detailed Review

National Economy

- The Canadian economy performed well in 1998 despite earlier fears of a potential economic set back from the financial and economic problems that beset the Far East. Statistics Canada estimates that GDP in constant dollars increased by 3 per cent in 1998, which can compare to 3.9 per cent in the USA and the 3.8 per cent Canadian growth that was recorded in 1997. It might be noted that the 3 per cent growth for Canada matches the Prudent Planning assumptions that were incorporated into the 1998 Federal Budget. Chart One shows the annual percentage change in GDP in constant dollars since 1990.

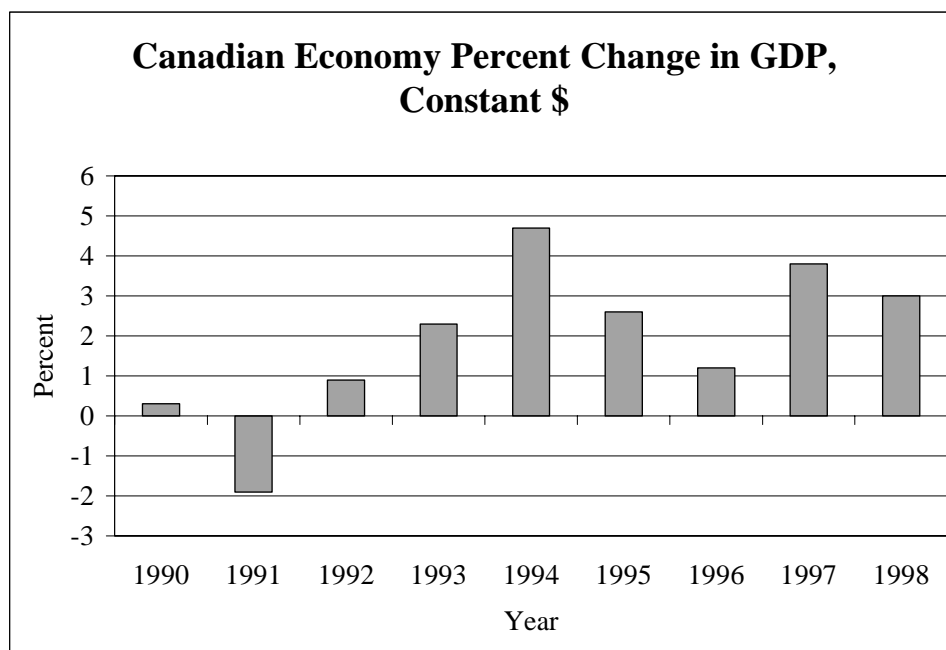


Chart One. Source: Statistics Canada, Systems of National Accounts.

- Throughout 1998 the Canadian dollar has been weak by comparison to the US dollar, averaging \$US 0.674. Interest rates have been low and inflation very modest. The 90 day Treasury Bill Rate in 1998 averaged 4.75 per cent and the rate of increase in the Canadian Consumer Price Index was only 1 percent.
- The Canadian economy was again led by rising international exports, particularly to the USA. The value of exports of goods and services from Canada rose 8.1% in 1998 in constant dollars. There were also strong growth of Personal expenditures on durable goods
- Employment increased by 389,000 in 1998, an increase of 2.8 per cent. This brought the unemployment rate down to 8.3 per cent, the lowest since 1990.

- The Bank of Canada reports weak international demand coupled with excess supplies of metals, oil, lumber, pulp and agricultural products resulted in a sharp reduction of commodity prices. The reduction of international demand and the fall in commodity prices was primarily responsible for the weakening of the Canadian dollar and narrowing trade surplus during 1998.
- Most economic forecasters consider that the Canadian economy will continue to expand in 1999, on the strength of further growth in the USA. The Federal Budget is based on an anticipated Canadian GDP growth of 1.8 per cent in constant dollars, using prudent growth assumptions, or 2.5 per cent in nominal dollars.
- The emerging national economic outlook therefore is one of continuing but slowing growth at low rates of inflation. The expectation is that the economic problems of the Asian economies are largely on the mend.

Provincial Economy

- The value of Prince Edward Island's GDP at Market prices for 1998 is estimated to have been \$3,016 million. In constant dollars this represents a 1.8 per cent increase over 1997. Employment averaged 60,900 per month in 1998, an increase of only 0.7 per cent and the unemployment rate was 13.9 per cent, which can compare to 14.9 per cent in 1997.
- The economic outlook for 1999 suggests that the economy will continue to expand at a similar pace of approximately 1.8 per cent in constant dollars. In light of recent experience there is the likelihood that increased employment will produce a further modest decline in the unemployment rate.
- The economic outlook is consistent with a return to population growth following the decline that occurred between 1997 and 1998. It is expected that this will approximate the present annual rate of natural increase of some 450 persons.
- Consumer spending was bolstered by another strong year for tourism and retail sales were up by 4.5 per cent. Residential construction improved as housing starts were up by 11.5 per cent, following the poor performance of 1997.

- Personal Income valued an estimated \$2,616 million in 1998. Total incomes on Prince Edward Island increased by only 1.6 per cent that year, though this was coupled with a 0.5 per cent decline in consumer prices. Total wages and salaries paid to Islanders comprise 53 per cent of total income and increased by 3.1 per cent. Growth of personal incomes in recent years has been seriously effected by the changes to the EI program. This can be seen in Chart Two.

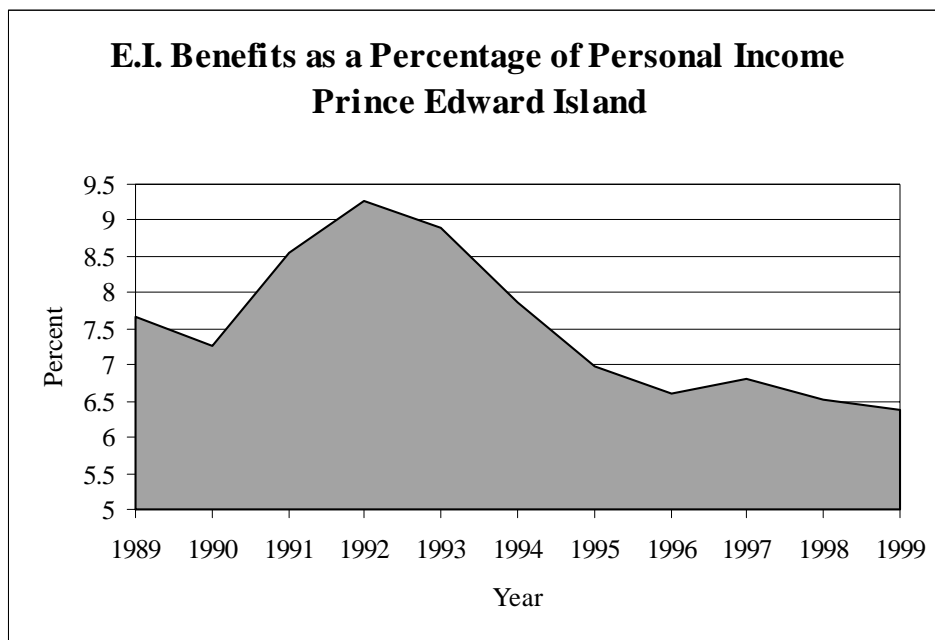


Chart Two. Source: Statistics Canada, 1999 Estimated

Sector Detail

Agriculture

GDP for agriculture was down in 1998 by an estimated 7.2 per cent. Whereas the hog sector received considerable public attention in light of the collapse in hog prices, the main factor causing the decline in agricultural production was a fall of 17.4 per cent in the size of the potato harvest from 1997. The volume of hogs produced actually increased by 3 per cent, though the revenue from hog sales fell from \$29.4 million to \$21.2 million, given the large drop in hog prices. With respect to potatoes, which form 55 per cent of the value of all receipts from farming on Prince Edward Island, improved prices raised the value of receipts to an all time record of \$168.8 million in 1998. The following table itemizes the value of Farm Cash Receipts on Prince Edward Island in recent years. A return to better prices for hogs and continuing expansion of potato production in 1999 is expected to raise the GDP for agriculture substantially.

Table 1. Farm Cash Receipts, PEI \$ Millions

	Potatoes	Beef	Hogs	Dairy	Other	Total
1993	98.0	32.9	21.5	38.9	47.5	238.8
1994	163.7	27.3	22.3	41.0	53.0	307.3
1995	149.8	28.4	24.8	43.3	65.7	312.0
1996	137.5	27.4	30.6	45.8	48.9	290.2
1997	128.1	29.6	29.4	47.1	40.6	274.8
1998	168.8	27.8	21.2	48.3	42.1	308.3

Source: Statistics Canada Agricultural Division

Fishing and Forestry

The value of fish landings for 1998 is estimated to be \$120.6 million. This represents an increase of 6.1 per cent over 1997. Lobster landings were up by 6.2 per cent in volume and the value of the lobster catch reached \$80.6 million. Lobster landings form 67 per cent of fish landings. Mussel harvesting, at \$15.1 million is the second most important component of the Prince Edward Island fishery. A continuation of past trends is expected in 1999.

Prince Edward Island's forests and woodcutters harvested approximately 579.7 thousand cubic meters of wood in 1998. Estimated receipts for delivered forestry products increased 3.3 per cent totalling \$ 282 million. Steady growth has occurred in the saw log industry, growing 3.4% over 1997 and by 45.5% since 1994. Pulp wood production has declined since 1995 as fewer acres are converted from forest to other purposes. Approximately 100 thousand cubic meters of fuel wood was harvested, down approximately 13 per cent from 1997. Declines in energy prices since the shock of 1991 is partly responsible for a 61 per cent decline in fire wood production since 1991.

Manufacturing

Manufacturing was a leading growth sector for Prince Edward Island in 1998 with an estimated constant dollar increase of 5 per cent. Manufacturing shipments valued \$921.9 million in 1998. The largest contributors to manufacturing growth in 1998 were Chemicals, Transportation Equipment and the Wood Industries. The largest component of Prince Edward Island's manufacturing is Food Industries, representing some two thirds of all Island manufacturing. That sector comprises potato processing plants, dairies, bakeries, the feed industry and fish processors. In total the Food Industry group experienced no growth in 1998 following the major expansion that occurred in 1997.

In 1999 the Food Industries component is expected to return to expansion as the AgraWest plant is fully operational and increased potato production is expected.

Tourism

Enterprise PEI indicates in their report *Economic Impact: Tourism 98* that 1.24 million pleasure travellers came to Prince Edward Island May 14 to October 31 1998. This represents an increase of 4.2 per cent in numbers by comparison to this period in 1997. The total value of tourist expenditures on Prince Edward Island in that period is estimated to be \$274.4 million, which is an increase of 11.6 per cent over the previous year. The recent trends in tourist visitation on Prince Edward Island are identified in the Chart Three. It is evident that the scale of tourist activity on Prince Edward Island has increased very significantly since the opening of the Confederation Bridge on June 1, 1997.

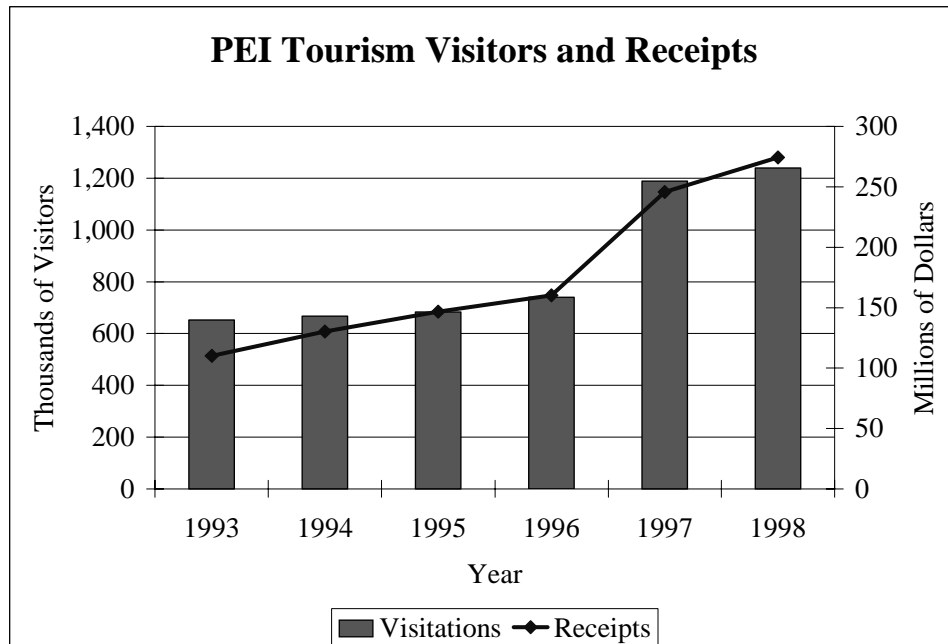


Chart Three. Source: Department of Fisheries and Tourism

The provincial Department of Fisheries and Tourism expects further growth in tourism in 1999 and anticipate expenditures by tourists to increase by 5 per cent in the coming tourism season.

Construction

Year over year comparisons of construction activity between 1997 and 1998 are unfortunately distorted by the completion work associated with the Confederation Bridge in early 1997. Statistics Canada indicates that non residential capital construction expenditures fell from \$218.7 million to \$137.7 million in this period. However, of that decline, \$69 million was associated with the

Confederation Bridge.

Housing Starts on Prince Edward Island were up by 11.5 per cent in 1998, largely as a consequence of a 60.6 per cent improvement in the fourth quarter statistics.

The value of non residential building permits increased by 18 per cent in 1998. A series of construction projects were underway during the year, including the Brudenell Golf Course, the AgraWest potato dehydration plant in Souris, shopping mall developments as well as numerous tourist facility improvements.

The yearly figures for total construction expenditures for 1998 indicate a decline of 19.8 percent when compared with 1997. Employment in the construction sector in 1998 was down from the 4,400 recorded in 1997 to 4,100.

Looking forward to 1999, Statistics Canada's Investment Intentions indicate that \$273.1 million of construction are expected. This is indicative of a modest increase from 1998.

Transportation and Utilities

Electricity consumption increased by 2.6 per cent in 1998. The consumer price of electricity fell by 2.9 per cent during the year and this was one aspect of the significant fall in energy costs on Prince Edward Island. The pattern of change in energy prices during the past decade is shown in Chart Four.

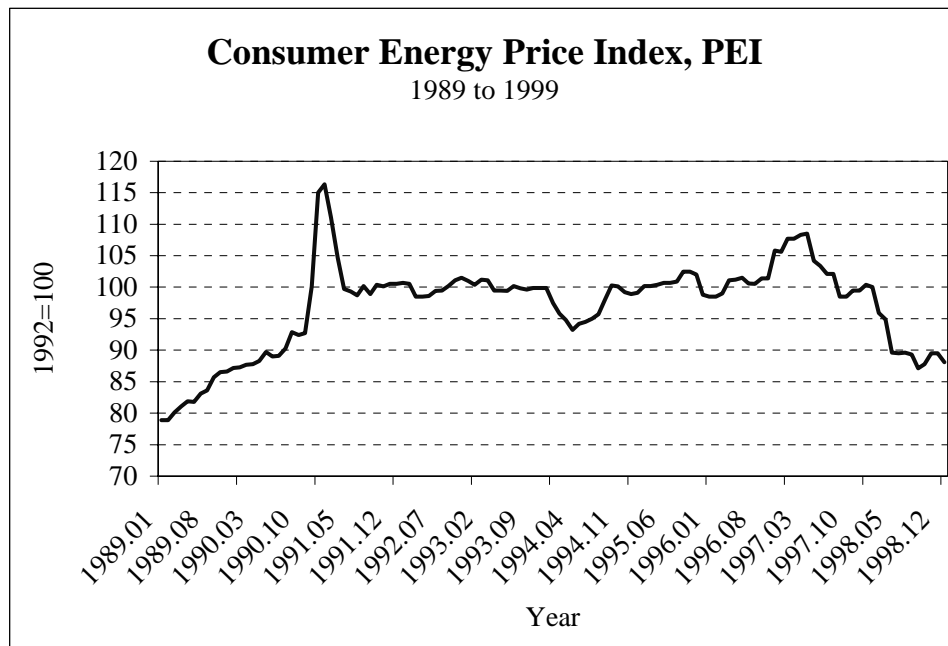


Chart Four. Source: Statistics Canada

GDP of the transportation sector was up significantly in 1998, the first full year of operation of the Confederation Bridge. Further expansion in the volume of truck and passenger traffic on the Bridge is anticipated in 1999.

Services Sectors

The largest private sector employer on Prince Edward Island is the Retail/Wholesale sector, with employment of 9,700 in 1998. In 1998 retail sales reached a record level of \$1,040.7 million which represented an increase of 4.5 per cent from 1997. New motor vehicle sales were down by 3.4 per cent in 1998 in terms of numbers of units. The value of sales was up slightly, at 0.4 per cent, led by commercial purchases, but the value of passenger car purchases was down by 2.3 per cent. The major area of stimulus in the retail sector was clothing and footwear, resulting in part from the Government decision to eliminate footwear and clothing from sales tax in November 1997.

Education and Health Care together provide employment for some 11,400 Islanders. The Health Care sector is a strongly expanding sector whereas the education sector faces a slow decline in the school age population. The number of persons 0-14 years of age declined from 29,300 in 1996 to 28,448 in 1998. By contrast the population 65+ increased from 17,500 to 17,700 over this period. Employment in public administration on Prince Edward Island is recorded as 5,400 and has been in decline since 1996, though in 1998 increased provincial employment compensated for loss of federal employment. Statistics Canada data indicate that municipal employment was up sharply in 1998.

Summary

The provincial economy expanded modestly in 1998, though employment growth was slight. The unemployment rate declined by comparison with 1997 but at 13.9 per cent remained significantly higher than the national average. The impact of the Confederation Bridge is significant, particularly for increased tourism. Agriculture enjoyed rising prices for potatoes but the collapse in hog prices caused serious difficulties in that sector. An improved picture for agriculture is expected in 1999.

Looking forward to 1999 the economy is expected to continue to expand, though at a pace somewhat less than the national average. A number of new projects are planned or are underway, including new retail stores, golf courses and tourist facilities.

**SUMMARY STATISTICS
PRINCE EDWARD ISLAND ECONOMY**

	1992	1993	1994	1995	1996	1997	1998
Population on 1 July (in '000)	130.9	132.3	133.7	134.8	136.2	136.9	136.5
Personal Income per capita (\$)	17,595	18,218	18,209	18,793	19,036	18,781	19,178 ¹
As % of Canadian Personal Income	81.5	83.8	83.2	83.6	83.8	81.7	80.0 ¹
Employment	54.1	54.4	56.1	58.7	60.1	60.5	60.9
Unemployment rate (%)	17.9	18.1	17.2	14.7	14.5	14.9	13.9
<i>Unemployment Rate - Canada</i>	<i>11.3</i>	<i>11.2</i>	<i>10.4</i>	<i>9.5</i>	<i>9.7</i>	<i>9.2</i>	<i>8.3</i>
CPI - annual change P.E.I. (%)	0.7	2.0	-0.2	1.6	1.9	1.3	-0.5
<i>CPI - annual change (%) Canada</i>	<i>1.5</i>	<i>1.8</i>	<i>0.2</i>	<i>2.1</i>	<i>1.6</i>	<i>1.6</i>	<i>1.0</i>
Retail trade (\$ million)	796.0	839.9	857.1	893.9	926.5	996.2	1,040.7
New Motor Vehicle Sales (units)	4,217	4,449	4,764	4,223	4,120	4,717	4,556
Farm Cash Receipts (\$ million)	227.0	238.8	307.3	312.0	290.2	274.8	308.3
Potato Receipts (\$million)	72.8	98.0	163.7	149.8	137.6	128.0	168.8
Lobster Landings (\$ million)	57.8	50.7	64.2	78.4	61.7	73.2	80.6
Lobster Landings (lbs - million)	19.5	19.4	18.6	19.3	18.0	17.8	18.9
Housing Starts (units)	644	645	669	422	554	470	524
Investment (\$ million)	390.4	411.6	483.1	518.8	493.6	490.3	448.7
Manufacturing Shipments (\$ million)	501.4	510.8	540.0	704.2	747.5	877.0	921.9
Tourist expenditures (\$ million)	57.5	110.0	127.8	141.4	150.8	245.9	274.4
GDP at market prices (\$ million)	2,336	2,469	2,542	2,709	2,865	2,943	3,016 ¹

Note 1: estimated value

Sources: Statistics Canada, CMHC, Provincial Department of Fisheries and Tourism, Enterprise P.E.I.