THE ECONOMY IN BRIEF

DEPARTMENT OF FINANCE JUNE 2000

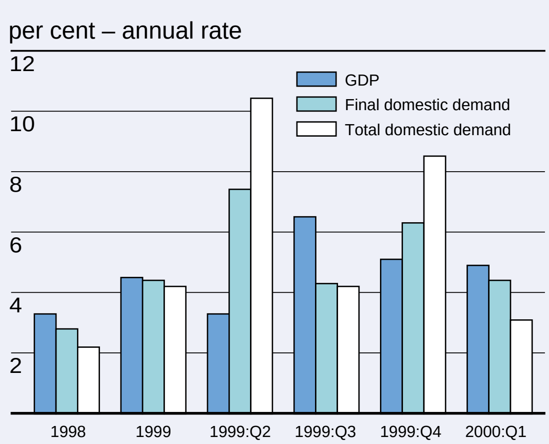
KEY MESSAGES

- In the first quarter of 2000, real gross domestic product (GDP) grew a robust 4.9% following even stronger gains of 6.5% and 5.1% in the third and fourth quarters of 1999. This brought output to 4.9% above its level a year earlier. At the same time, the first quarter of the new millennium saw nominal GDP surpass the trillion dollar mark for the first time.
- Growth in both foreign and domestic demand contributed to increased output. Total domestic demand grew less rapidly than in the fourth quarter. However, real exports jumped 13.9%, boosting Canadian production.
- The nominal trade surplus increased significantly as both the real trade balance and the terms of trade improved (export prices rose while import prices fell). The current account moved from a deficit of about $1 billion in the fourth quarter to a surplus of over $19 billion, or 1.9% of nominal GDP, in the first quarter. This is the highest current account surplus ever both in dollar terms and as a share of nominal GDP. This continued a trend begun several quarters earlier, as the average deficit stood at 1.8% of nominal GDP in 1998 and 0.4% in 1999.
- The strong pace of job creation has continued into 2000. A gain of 115,000 net new jobs from January to April on top of the 427,000 created during 1999 brought net job creation to over 542,000 since the end of 1998. Full-time jobs accounted for more than the total net gain. The unemployment rate in April 2000 remained at 6.8% for the fifth consecutive month, the lowest rate since April 1976.

SUMMARY[1]

In the first quarter of 2000, the Canadian economy continued its solid growth, with both increased foreign and domestic demand. Export growth jumped while imports satisfied a smaller part of growing domestic demand than in the fourth quarter, providing a boost to Canadian production. Total domestic demand (spending by Canadian consumers, business and government on goods, services, housing and plant and equipment plus inventory accumulation) growth continued but at a slower pace than in the fourth quarter (Chart 1), restraining growth to a rate similar to that in the fourth quarter. Meanwhile, cost and inflation pressures remained subdued.

Chart 1
Growth in real GDP and real domestic demand



Final domestic demand is spending by Canadians on goods, services, housing and plant and equipment. Total domestic demand is final domestic demand plus inventory accumulation.

[1] Unless otherwise noted, data and per cent changes are quoted at annual rates and the cut-off date for data is May 31, 2000.

Main economic indicators
(per cent change at annual rates unless otherwise indicated)

	1998	1999	1999:Q2	1999:Q3	1999:Q4	2000:Q1	Most recent	
Real gross domestic product	3.3	4.5	3.3	6.5	5.1	4.9	–	
GDP excluding inventories	3.9	4.7	0.6	6.6	3.0	6.2	–	
Final domestic demand	2.8	4.4	7.4	4.3	6.3	4.4	–	
Government expenditure	1.6	2.8	3.8	3.3	3.8	1.5	–	
Consumer expenditure	2.9	3.5	4.7	4.6	3.7	3.4	–	
Residential investment	-2.0	6.6	11.7	4.8	12.1	9.8	–	
Business fixed investment	6.1	10.5	25.3	4.8	20.5	11.2	–	
Non-residential construction	1.7	2.0	0.0	2.5	8.6	12.5	–	
Machinery and equipment	9.0	15.6	41.9	6.0	27.2	10.5	–	
Business inventory change[1]	-0.5	-0.2	2.7	-0.1	2.0	-1.1	–	
Trade balance[1]	1.1	0.4	-5.5	2.5	-3.6	2.5	–	
Exports	8.9	10.0	0.4	12.9	10.7	13.9	–	
Imports	6.1	9.4	16.7	6.5	22.1	7.9	–	
Current account balance								
(nominal $ billion)	-16.3	-3.4	-7.2	1.7	-1.3	19.4	–	
(percentage of GDP)	-1.8	-0.4	-0.8	0.2	-0.1	1.9	–	
Real personal disposable income	2.8	2.7	4.0	1.9	3.4	4.5	–	
Profits before taxes	-5.6	23.7	23.6	59.8	27.0	31.5	–	
Costs and prices (%, y/y)								
GDP price deflator	-0.6	1.6	1.0	2.5	3.1	3.3	–	
Consumer price index	0.9	1.7	1.6	2.2	2.4	2.7	2.1	Apr-2000
CPI – excluding food and energy	1.3	1.5	1.5	1.6	1.6	1.5	1.3	Apr-2000
Unit labour costs	1.4	0.5	0.4	0.5	0.8	1.6	1.9	Mar-2000
Wage settlements (total)	1.7	2.2	2.4	2.3	2.9	2.3	2.5	Mar-2000
Labour market								
Unemployment rate (%)	8.3	7.6	7.8	7.6	7.0	6.8	6.8	Apr-2000
Employment growth	2.7	2.8	2.5	2.2	3.5	3.8	0.4	Apr-2000
Financial markets (average)								
Exchange rate (cents U.S.)	67.48	67.32	67.90	67.30	67.90	68.80	67.05	01-Jun-2000
Prime interest rate (%)	6.60	6.44	6.33	6.25	6.42	6.75	7.50	01-Jun-2000

[1] Annualized change expressed as a percentage of GDP in the previous period.

Sources: Statistics Canada, the Bank of Canada and Human Resources Development Canada.

Canadians still buying

Real consumer expenditure increased a solid 3.4% in the first quarter, modestly off the pace of the previous quarter. The pace of growth for spending on durables, such as furniture and appliances, increased relative to the previous quarter, but the pace of growth for spending on non-durables and services slowed. The slowdown for non-durables in part reflected a return to more normal spending on food, which had spiked in December due to Y2K concerns and millennium celebrations.

The 5.8% gain in personal income was faster than in the fourth quarter. Labour income registered its strongest quarterly growth rate since the late 1980s. Employment gains were similar to those in the fourth quarter while hours worked increased more sharply.

With personal income taxes rising only modestly faster than in the previous quarter, real personal disposable income growth rose to 4.5%. On a per capita basis, real personal disposable income grew 4.1%, continuing a positive trend. And with disposable income outgrowing consumer spending, the personal savings rate rose to 3.4% from an upwardly revised 3.2% in the fourth quarter. Changes in Statistics Canada's treatment of public service pension plans, as well as historical revisions to income and outlays, raised the savings rate by between one and three percentage points since 1961.

Investment activity continues to grow

Business investment in plant and equipment increased a robust 11.2% in the first quarter. However, this was slower than the pace in the previous quarter. Machinery and equipment investment grew 10.5% after a much sharper gain in the previous quarter. Non-residential construction growth, at 12.5%, increased faster than in the fourth quarter, with significant gains in engineering projects, as higher energy prices boosted oil patch activity.

Residential investment growth was strong in the first quarter but slower than in the fourth. Renovations posted a second consecutive solid gain of nearly 20% while transfer costs rebounded sharply from a decline in the previous quarter, as sales of existing houses jumped. However, growth in new construction activity slowed sharply despite a modest increase in housing starts.

Inventories rise more modestly

Businesses raised their inventories by $6.6 billion in the first quarter following a larger accumulation of $9.2 billion in the fourth. With stronger demand boosting sales more than the increase in inventories, the economy-wide inventory-to-sales ratio dropped to its lowest recorded level.

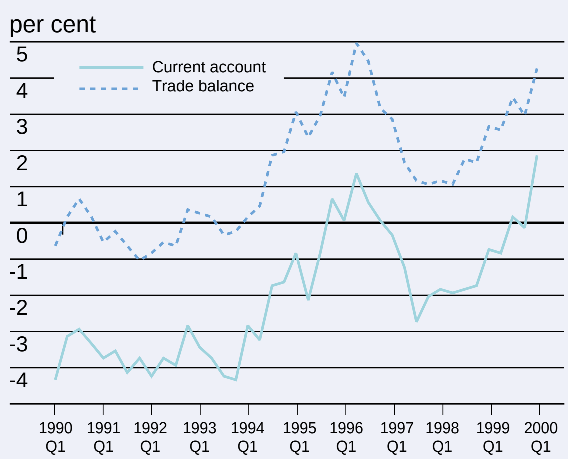
Surge in exports boosts production

Increased foreign demand for Canadian products raised real exports 13.9% in the first quarter. A dominant factor behind rising exports has been solid external demand arising from strong growth in the United States economy and the ongoing recovery in nations affected by the financial crisis of 1997-1998. Meanwhile, total real imports by Canadians rose a more moderate 7.9% in the first quarter, reflecting the more modest gains in consumer spending and business investment in machinery and equipment and inventories than in the previous quarter.

Record current account surplus

The gain in the real trade balance plus an improvement in the terms of trade resulted in a much larger nominal trade surplus than in the fourth quarter. This, along with improvements in the investment income deficit (including net retained earnings) and net transfers, moved the current account from a deficit of about $1 billion in the fourth quarter to a record surplus of over $19 billion, or 1.9% of nominal GDP, in the first quarter (Chart 2). This continued the improvement in the current account, which registered a much smaller deficit in 1999 than in 1997 and 1998.

Chart 2
Current account as a percentage of nominal GDP



Inflation rises temporarily while profits jump again

The implicit and chain price indices for GDP both advanced about 4% in the first quarter, as higher export prices sharply raised these indices to levels over 3% higher than a year earlier. However, consumer price inflation remains moderate. After rising to 3.0% in March on a year-over-year basis, largely due to the temporary impact of higher energy prices, CPI inflation eased to 2.1% in April as energy prices retreated. Moreover, underlying CPI inflation, which excludes food and energy prices, posted only a modest year-over-year increase of 1.3% in April.

Labour productivity, measured as output per employed person, rose slightly slower in the first quarter than in the fourth. Labour costs per unit of output rose from their fourth quarter level and were 1.6% above their level of a year earlier.

Pre-tax corporate profits surged 31.5%, the sixth consecutive double-digit increase. Profits rose to 12.0% of nominal GDP and to a level 34.8% above that of a year earlier.

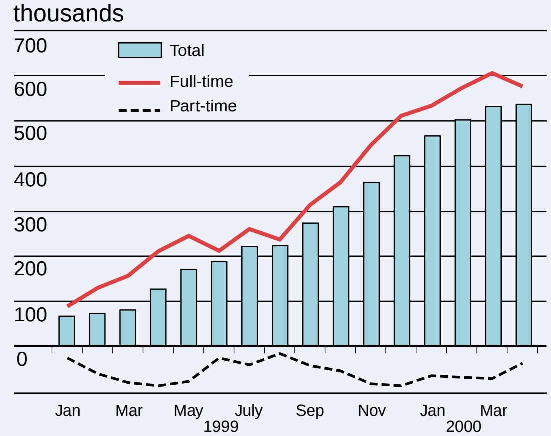
Unemployment rate remains at 24-year low

First quarter employment increased 3.8%, adding to the over 427,000 net new jobs created during 1999. Even with the modest employment gain in April, the number of net new jobs created in the six months since October 1999 stood at 229,000 (Chart 3). This raised the total increase to over 542,000 jobs since the end of 1998. And despite a drop in April, full-time jobs have exceeded the total net gain as part-time employment fell over that period. The unemployment rate in April 2000 remained at 6.8%, the lowest rate since April 1976.

The Canadian dollar gives back some gains

After dropping to an all-time low close of 63.31 cents U.S. in late August 1998, the Canadian dollar rebounded along with world

Chart 3
Cumulative employment growth since December 1998



commodity prices. It rose above 69 cents U.S. on several occasions, most recently in early March. It has since lost some ground to trade below 67 cents U.S. On June 1, it closed at 67.05 cents U.S.

Canadian market interest rates have risen along with those in the United States. Most recently, on May 16, the U.S. Federal Reserve tightened monetary conditions for the sixth time since mid-June 1999, raising the target for the Federal Funds Rate from 6.00% to 6.50%, bringing the total increase to 175 basis points. The Bank of Canada matched the May increase by the Federal Reserve, as it had in February 2000 and November 1999.

However, interest rates in Canada generally have remained below those in the United States, especially short-term rates. The differential between Canadian and U.S. 3-month Treasury bill yields widened from under 40 basis points in mid-November 1999 to over 90 basis points at the beginning of March. More recently, short-term rates in the two countries have converged, with the Canadian yield only 7 basis points below that of the U.S. on June 1.

The main source of data used in this publication is Statistics Canada. Subscription inquiries should be directed to the Distribution Centre at (613) 995-2855. For other inquiries about this publication, contact Mostafa Askari at (613) 992-3055.
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