

THE ECONOMY IN BRIEF

DEPARTMENT OF FINANCE

DECEMBER 1999

KEY MESSAGES

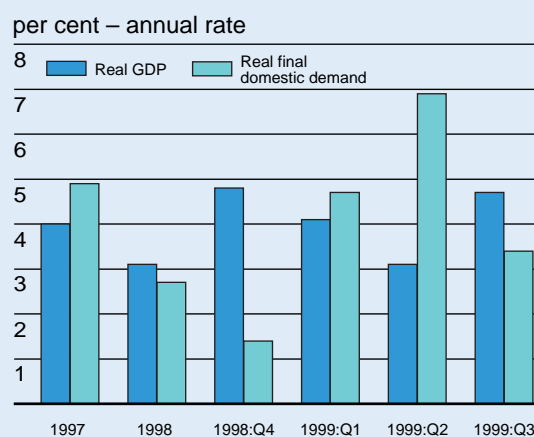
- In the third quarter of 1999, real gross domestic product (GDP) grew sharply, rising 4.7% following a gain of 3.1% in the second quarter. This brought output to 4.2% above its level a year earlier.
- Demand growth in the quarter was balanced. Much stronger foreign demand boosted real exports by 15.0%, contributing to increased Canadian production. Private and public domestic demand for goods and services, housing and investment also continued to grow, although at a slower pace than in the second quarter.
- While rising imports did satisfy part of the increased demand, the nominal trade surplus rose significantly despite a modest decline in the terms of trade (export prices rose less than import prices). The current account improved sharply, going from a deficit of about \$7 billion in the second quarter to a surplus of about \$2.6 billion in the third quarter, its best level and first surplus since 1996. As a share of nominal GDP, the current account surplus was 0.3%, significantly better than the average deficit of 1.8% in 1998.
- Canadian labour productivity (output per employed person) registered an impressive gain of 3.2% in the third quarter, as employment rose 1.5%.
- With a further gain of about 60,000 jobs in the month, November employment stood at over 310,000 above the level at the end of 1998, with full-time jobs accounting for more than the total net gain. More than 340,000 net new jobs were created in the 12 months since November 1998. The unemployment rate in November 1999 was 6.9%, the lowest rate since August 1981.

SUMMARY¹

In the third quarter of 1999, the Canadian economy continued its solid performance. The sharp gain in output in the quarter came from both increased foreign and domestic demand. Very strong export growth boosted the growth rate of Canadian production above that of the previous quarter. Final domestic demand (spending by Canadian consumers, business and government on goods, services, housing and plant and equipment) also continued to rise (Chart 1). Meanwhile, cost and inflation pressures remained relatively subdued.

¹ Unless otherwise noted, data and per cent changes are quoted at annual rates. The cut-off date for data is December 3, 1999.

Chart 1
Growth in real GDP and
real final domestic demand



Consumers continue to buy

Real consumer expenditure increased 4.8% in the third quarter following gains of over 4% in the previous two quarters. Spending rose much more sharply than in the second quarter on all major categories of durables. Purchases of automotive products rebounded strongly from a decline in the second quarter. Growth in services remained significant but was only about half the pace in the previous quarter.

Personal income grew 3.8% in the third quarter, a slightly faster pace than in the second quarter. Labour income, which also registered a growth rate similar to that in the previous quarter, increased as a result of gains in both employment and the average wage per worker.

Main economic indicators

(per cent change at annual rates unless otherwise indicated)

	1997	1998	1999:Q1	1999:Q2	1999:Q3	Most recent
Real gross domestic product	4.0	3.1	4.1	3.1	4.7	-
GDP excluding inventories	3.2	3.6	5.8	-0.3	7.1	-
Final domestic demand	4.9	2.7	4.7	6.9	3.4	-
Government expenditure	-1.0	2.0	0.1	3.0	1.1	-
Consumer expenditure	4.2	2.8	4.4	4.3	4.8	-
Residential investment	12.6	-1.9	17.3	14.0	2.5	-
Business fixed investment	18.8	5.7	9.8	23.9	1.7	-
Non-residential construction	14.0	0.1	8.0	3.2	8.5	-
Machinery and equipment	22.2	9.5	10.9	37.0	-1.8	-
Business inventory change ¹	0.7	-0.4	-1.6	3.4	-2.2	-
Trade balance ¹	-1.7	1.0	1.7	-5.8	3.7	-
Exports	8.5	8.2	10.1	1.4	15.0	-
Imports	14.6	5.8	6.1	18.8	5.5	-
Current account balance						
(nominal \$ billion)	-14.3	-16.4	-6.1	-7.0	2.6	-
(percentage of GDP)	-1.6	-1.8	-0.7	-0.7	0.3	-
Real personal disposable income	1.3	2.4	2.0	1.5	2.5	-
Profits before taxes	8.5	-6.0	25.6	18.4	49.6	-
Costs and Prices (% , y/y)						
GDP price deflator	0.8	-0.6	0.3	0.8	2.3	-
Consumer price index	1.6	0.9	0.8	1.6	2.2	2.3 99-Oct
CPI - excluding food and energy	1.6	1.3	1.0	1.5	1.6	1.6 99-Oct
Unit labour costs	1.8	0.9	-0.2	-0.4	0.3	
Wage settlements (total)	1.4	1.7	1.5	2.4	2.3	3.0 99-Sep
Labour market						
Unemployment rate (%)	9.2	8.3	7.8	8.0	7.6	6.9 99-Nov
Employment growth	1.9	2.8	3.7	-0.2	1.5	5.0 99-Nov
Financial markets (average)						
Exchange rates (cents U.S.)	72.24	67.48	66.17	67.90	67.30	67.49 2-Dec-99
Prime interest rate (%)	4.96	6.60	6.75	6.33	6.25	6.50 2-Dec-99

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.

With personal taxes rising at a slower pace than in the previous quarter, and slower than personal income, real personal disposable income growth jumped to 2.5%. But with strong growth in nominal personal spending outpacing that in nominal disposable income, the personal savings rate fell to 0.3% from 0.9% in the second quarter.

Investment activity rises more moderately

Business investment in plant and equipment increased 1.7% in the third quarter, a much slower pace than in the previous quarter. Investment in non-residential construction grew noticeably more than in the second quarter, with similar gains in both building and engineering structures. However, machinery and equipment investment actually slipped slightly after rising 37.0% in the previous quarter. The sharp slowdown was due to fewer aircraft purchases and a levelling off in computer investment, perhaps the result of firms having already largely dealt with potential Y2K problems.

Residential investment growth also slowed from its pace in the previous two quarters. While total housing starts were similar in the second and third quarters, a shift from multiple units to single homes, which create more activity per average unit, boosted new construction activity in the third quarter. Transfer costs also registered a smaller gain than in the second quarter, but renovations declined, largely offsetting the gains in the other two components.

Exports surge

Much stronger foreign demand for Canadian products contributed to a sharp jump of 15.0% in real exports in the third quarter. One factor behind this was strong growth in real GDP in the United States in the third quarter. This boosted U.S. imports from Canada, especially of automotive products. Canadian exports of computers and telecommunications equipment also

rose sharply. In contrast, total real imports by Canadians rose a more modest 5.5% in the third quarter, reflecting slowdowns in business investment and imports of machinery and equipment.

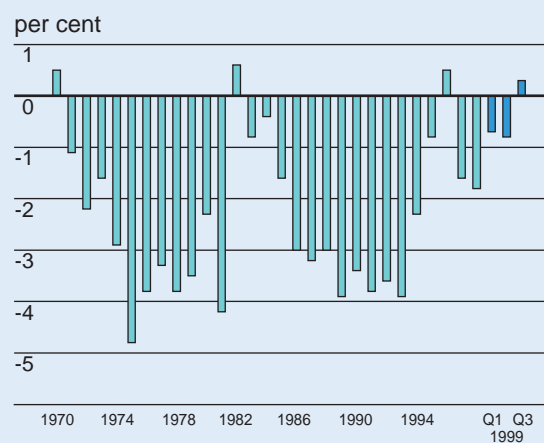
Inventory accumulation smaller

Businesses increased their inventories by \$2.9 billion in the third quarter following a much larger accumulation of \$7.7 billion in the second quarter. With stronger demand boosting sales, the economy-wide inventory-to-sales ratio dropped to its lowest recorded level.

Current account moves to a surplus

An improvement in the real merchandise trade balance dominated a small deterioration in the terms of trade, yielding a much greater nominal merchandise trade surplus than in the second quarter. This produced an improvement in the current account, which moved from a deficit of \$7 billion to a surplus of \$2.6 billion, or 0.3% of nominal GDP (Chart 2). Over the past 30 years, the current account has generally been in deficit.

Chart 2
Current account
as a percentage of nominal GDP



Inflation subdued while profits soar

Underlying price and cost pressures remained subdued in the third quarter. The implicit and chain price indices for GDP were both somewhat over 2% above their year earlier levels. Consumer prices accelerated to 2.6% in September on a year-over-year basis, owing in part to the temporary impact of higher energy prices. They then eased back to 2.3% in October.

Labour productivity, measured as output per employed person, rose noticeably again in the third quarter. Labour costs per unit of output rose only slightly from their second quarter level and were modestly above their level of a year earlier.

Pre-tax corporate profits surged another 49.6%, the fourth consecutive double-digit increase. The gains in the quarter were widespread among industries, with notable advances in petroleum and gas, transportation, telecommunications, motor vehicles and banks. Profits rose to 10.6% of nominal GDP and to a level 25.9% above that of a year earlier.

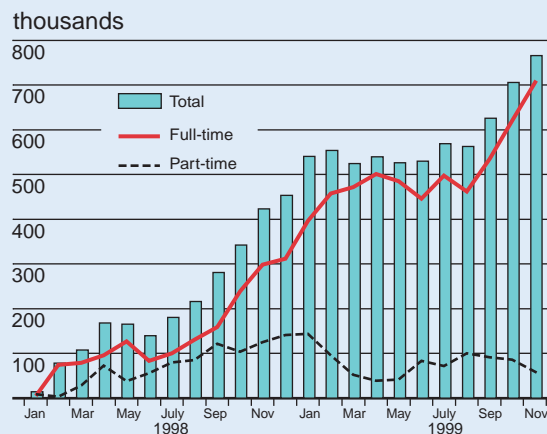
Lowest unemployment rate in 18 years

Third quarter employment increased 1.5% after declining slightly in the second quarter. Employment surged by another 60,000 jobs in November for a three-month gain of over 200,000 jobs (Chart 3). This brought the level to over 310,000 above that at the end of 1998. Full-time jobs have accounted for more than the total net gain. The unemployment rate in November was 6.9%, the lowest rate since August 1981.

The Canadian dollar experiences modest gains

After trading around 65 cents U.S. in the last quarter of 1998, the Canadian dollar strengthened along with world commodity

Chart 3
Cumulative employment growth since December 1997



prices. It peaked near 69 cents U.S. in early May before losing ground to trade near 67 cents U.S. It has since rebounded somewhat and on December 2 closed at 67.49 cents U.S.

Since May, Canadian market interest rates have risen along with those in the United States. Most recently, the U.S. Federal Reserve raised the target for the federal funds rate from 5.25% to 5.50% on November 16, its third round of monetary tightening in 1999. These moves were aimed at staving off inflationary pressures that might arise from a tight U.S. labour market, continued strong U.S. domestic demand and firming foreign economies.

The Bank of Canada matched the November increase by the Federal Reserve. However, interest rates in Canada have generally remained below those in the United States, especially short-term rates.

