

# MONTHLY ECONOMIC INDICATORS

## September 1998

### HIGHLIGHTS

-  **Solid job gains in July and August offset losses in the previous two months.**
-  **The unemployment rate falls to 8.3% in August, the lowest rate in eight years.**
-  **Output edges down in June, the third decline in as many months.**
-  **Exports are flat, but the trade surplus rises due to falling imports.**
-  **The dollar reaches a new low, prompting the Bank of Canada to raise interest rates.**
-  **North American stock markets fall sharply in August, dragged down by instability in Asia and Russia.**

### Key Monthly Economic Indicators

		% Change		
		since month	last year	
Real GDP (\$92 B)	707.5	-0.1	2.5	June
Goods	235.1	-0.4	2.0	June
Services	472.4	0.0	2.8	June
Composite Index	207.7	0.3	5.4	July
Employment (000's)	14,306	0.2	1.3	Aug
Full-time	11,627	0.4	2.9	Aug
Part-time	2,680	-0.2	-1.4	Aug
Unemployment* (%)	8.3	8.4	9.0	Aug
Youth*	14.5	15.3	16.6	Aug
Adult*	7.2	7.1	7.6	Aug
CPI inflation*	1.0	1.0	1.7	July
Retail Sales (\$M)	20,430	-1.7	4.0	June
Housing Starts (000's)	123.1	-6.5	-6.7	July
Trade Balance* (\$B)	1,541	1,328	2,483	June
Exports	26,041	0.1	5.7	June
Imports	24,500	-0.8	-0.8	June
M&E	8,396	3.4	17.7	June
3-mth Corp. paper* (%)	5.82	5.19	3.63	Sept 4
Long bond yield* (%)	5.61	5.57	6.38	Sept 4
Canadian dollar* (US¢)	65.54	66.18	72.06	Sept 4

\*Data in levels only – % change not reported.

**This issue's Special Report:  
Rising Skill Intensity in Canada: Evidence and Explanations**

The "Monthly Economic Indicators" (MEI) provides a variety of economic analysis and data in a convenient format. The MEI does not interpret or evaluate government policies, and every attempt is made to present factual information in an informed and balanced manner consistent with generally accepted economic principles. It is available to all employees of Industry Canada in either hard or electronic copy, or can be accessed via the Internet at [http://strategis.ic.gc.ca/sc\\_ecnmy/mera/engdoc/03.html](http://strategis.ic.gc.ca/sc_ecnmy/mera/engdoc/03.html).



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This report uses data available as of September 4, 1998. It has been prepared by Joseph Macaluso, Stéfane Marion and Shane Williamson of the Micro-Economic Analysis Directorate. The special report in this issue was written by Wulong Gu, with assistance from Caroline Farmer. All information is taken from public sources, primarily Statistics Canada, the Bank of Canada and the Canada Mortgage and Housing Corporation. Please address comments to Shane Williamson at 613-954-3494 or through the Internet at [williamson.shane@ic.gc.ca](mailto:williamson.shane@ic.gc.ca).



### *The economy slows sharply in the second quarter...*

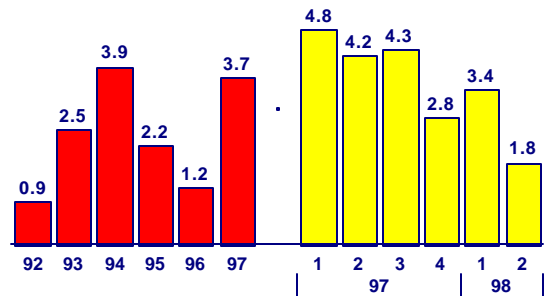
- Real GDP increased by 1.8% (annual rate) in the second quarter of 1998, the slowest quarterly growth rate in two years.
- The slowdown was widely anticipated, with construction strikes in Ontario and plant closures in the auto sector (related to a major GM strike in the U.S.) both acting as a drag on the economy. The trade sector did not contribute to growth, with an investment-related rise in imports outpacing export growth.
- Inventory accumulation slowed sharply in the second quarter, holding back overall production gains. The slowdown was most evident in Wholesale and Retail Trade.
- Still, some segments of the economy displayed surprising strength. In particular, domestic demand was very strong, buoyed by a substantial rise in consumer spending (despite lower disposable income) and a sharp rebound in M&E investment.

### *...making the outlook for last half of the year uncertain*

- Canada's near-term outlook is clouded by economic developments both at home and abroad. The second-quarter surge in consumer spending was financed through personal savings and increased borrowing, which may not be sustainable unless income picks up.
- Overseas, the economic and political instability that originated in Asia but has now spread to other emerging markets (including Russia) has taken its toll on Canadian financial markets.
- The falling Canadian dollar prompted an increase of one full percentage point in the trend-setting Bank Rate, which induced corresponding increases in rates for consumer and business loans.
- This increase, plus recent volatility in stock markets, could weaken consumer confidence in the latter half of the year. Business profits are also down, hit hard by lower commodity prices and weak demand in overseas markets.

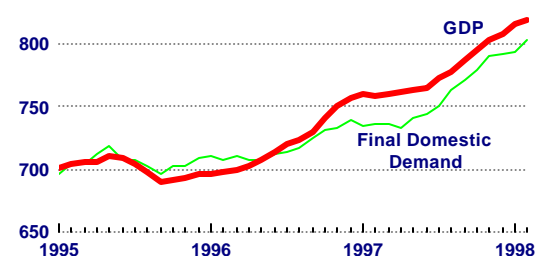
### Growth in Real Gross Domestic Product

% change, SAAR



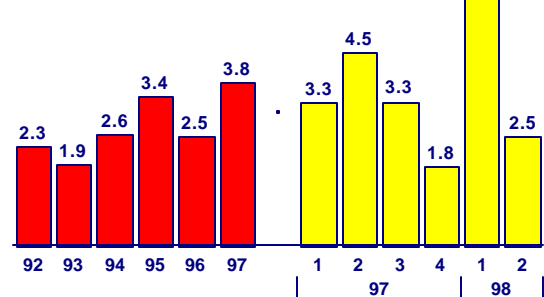
### GDP and Final Domestic Demand

\$ Billions

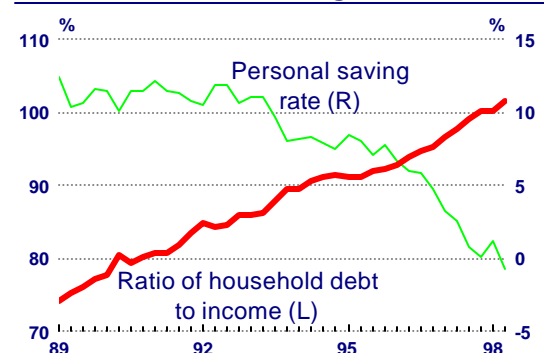


### Growth in Labour Income

% change, SAAR



### Personal Debt and Saving Rate





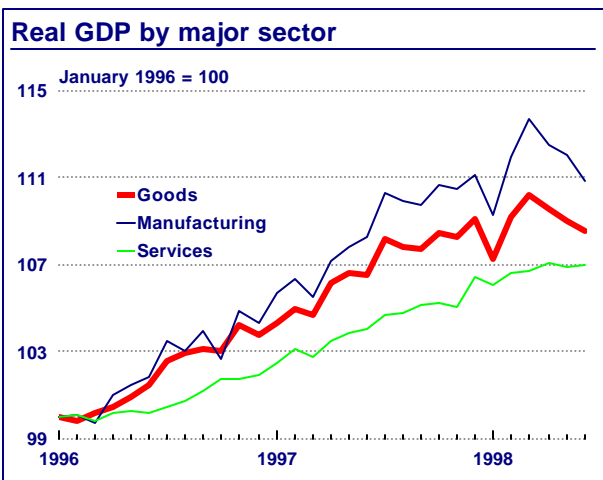
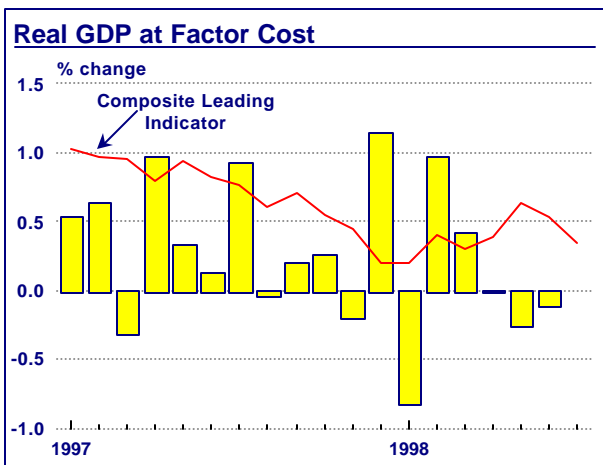
## Real GDP by Industry

### Output is down slightly in June...

- Real GDP edged down 0.1% in June, marking the first time since the beginning of 1991 that the economy failed to grow for three consecutive months. Economic activity nevertheless expanded in the second quarter, albeit at a slower pace than in the previous quarter.

### ...as labour disputes cut into Goods production

- Losses in the Goods-producing industries accounted for the decline in total output in June. Manufacturing output registered the largest of three consecutive monthly declines, as striking GM workers in the U.S. idled production at the company's Canadian operations. Excluding autos, production in Manufacturing was flat in June.
- Elsewhere in the Goods-producing industries, strikes in some key housing trades in Ontario contributed to the fourth straight decline in Construction activity. Mining posted a sharp rebound, however, boosted by increased production of oil and gas.
- In the Service sector, output has levelled-off in the past two months. Widespread losses in Retail and Wholesale Trade (the latter affected by auto-plant closures) were offset by increased activity in Finance and Business Services.



### Real GDP at Factor Cost (1992 dollars)

#### June 1998

	level	monthly change	% Change since last month	year
<b>Total Economy</b>	<b>707,487</b>	<b>-790</b>	<b>-0.1</b>	<b>2.5</b>
<b>Business sector</b>	<b>581,710</b>	<b>-597</b>	<b>-0.1</b>	<b>3.1</b>
<b>Goods</b>	<b>235,055</b>	<b>-884</b>	<b>-0.4</b>	<b>2.0</b>
Agriculture	11,999	-72	-0.6	-2.8
Fishing & Trapping	900	-43	-4.6	-3.7
Logging & Forestry	3,672	-38	-1.0	-12.5
Mining*	28,907	263	0.9	5.5
Manufacturing	124,662	-1,361	-1.1	2.4
Construction	40,261	-137	-0.3	3.4
Other Utilities	24,654	504	2.1	-1.1
<b>Services</b>	<b>472,432</b>	<b>94</b>	<b>0.0</b>	<b>2.8</b>
Transport & Storage	29,862	81	0.3	1.1
Communications	26,276	146	0.6	5.9
Wholesale Trade	42,419	-197	-0.5	6.3
Retail Trade	42,016	-734	-1.7	4.1
Finance & Insurance	36,727	478	1.3	2.2
Real Estate & Ins. Agent	75,865	85	0.1	1.9
Business services	41,943	427	1.0	8.7
Government services	40,277	-74	-0.2	-0.6
Education	40,538	10	0.0	-0.1
Health & Social Services	48,862	-67	-0.1	1.0
Accommodation & Food	18,999	-34	-0.2	2.9
Other	28,648	-27	-0.1	1.8

\*Includes Quarrying and Crude Petroleum & Natural Gas



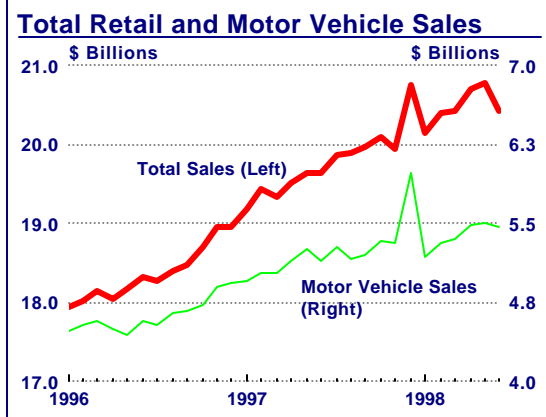
## Consumer Spending and Attitudes

### Surging consumer spending in the second quarter...

- Following a pause early in 1998, consumer spending surged 5.5% (annual rate) in the second quarter, growing at its fastest pace in 1½ years.
- Roughly half of this increase was due to higher sales of new motor vehicles. Generous incentive programs have generated considerable volatility in auto sales since December. Excluding motor vehicles, personal consumption has increased roughly 3.5% (annual rate) in each of the first two quarters of the year.
- The second-quarter rise in consumer spending was financed by lower personal savings – the saving rate turned negative – and increased borrowing. Disposable income edged down in the second quarter, after increasing in the two previous periods.

### ...may not be sustained into the last half of the year

- Buoyant consumer spending is unlikely to be sustained without a solid pick-up in disposable income. Indeed, June's broad-based decline in retail sales suggests a lack of momentum going into the third quarter.
- Consumer confidence remains relatively high, but could be shaken by the recent turmoil in financial markets and generally-weaker labour markets.



### Retail Sales and Consumer Credit

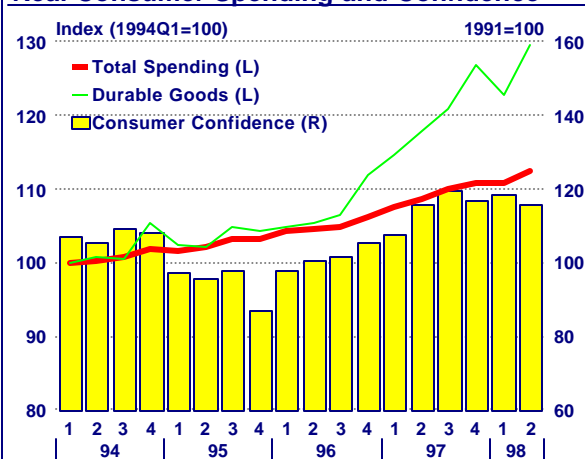
	June 1998	% Change	
		vs. last month	vs. last year
<b>Total Retail Sales</b>	20,430	-1.7	4.0
Food	4,837	-0.1	4.0
Drug Stores	1,088	-1.6	8.9
Clothing	1,128	-3.7	2.3
Furniture	1,040	0.3	6.9
Automotive	7,903	-1.6	3.6
General Merch. Stores	2,250	-4.8	2.9
All other Stores	2,184	-2.4	4.1
Total ex. motor vehicles	14,968	-2.0	3.2
<b>Consumer Credit</b>	152,184	0.5	10.1

### Real Consumer Spending and Household Finances

	\$ Millions, SAAR (unless otherwise noted)			
	1996	1997	1998 Q1	1998 Q2
<b>Real Consumption (92\$)</b>	451,682	470,177	477,388	483,856
% change	2.4	4.1	0.6	5.5
Durable Goods	54,465	61,020	62,400	65,880
% change	3.7	12.0	-12.4	24.2
Semi-Durable Goods	42,816	44,606	46,596	46,584
% change	0.6	4.2	12.7	-0.1
Non-Durable Goods	116,773	117,922	117,732	118,668
% change	2.1	1.0	0.4	3.2
Services	237,628	246,629	250,660	252,724
% change	2.5	3.8	2.2	3.3
<b>Disposable Income</b>	518,167	523,010	531,632	524,576
% change	1.4	0.9	5.5	-0.2
<b>Saving Rate (%)</b>	5.8	1.7	1.2	-0.7
<b>Debt-to-Income Ratio (%)</b>	94.2	98.4	100.1	101.5
<b>Consumer Attitudes*</b>	101.2	115.0	118.4	115.8

\*Conference Board of Canada

### Real Consumer Spending and Confidence





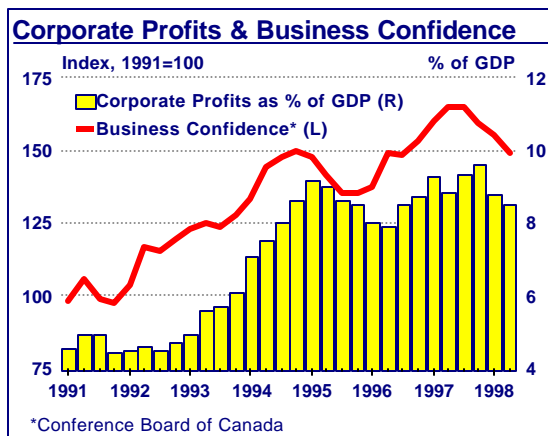
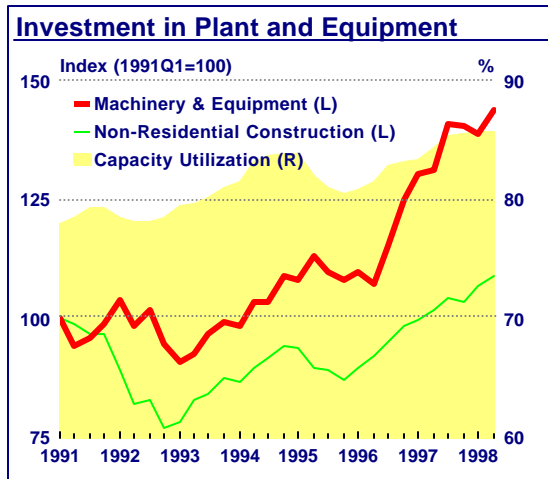
## Business Investment in Plant and Equipment

### Investment rebounds in the second quarter...

- Business investment in Machinery & Equipment (M&E) rose sharply in the second quarter, rebounding from declines in the previous two periods. Increased purchases of Industrial Machinery, Computers and Motor Vehicles led the second-quarter advance.
- Non-residential Construction slowed somewhat in the second quarter, but nonetheless posted a strong result. The slowdown was concentrated within the engineering component, particularly oil and gas drilling.
- These investment figures are broadly consistent with Statistics Canada's recent survey of private and public investment intentions. Spending on plant and equipment is expected to increase 6.6% overall in 1998.

### ...despite lower business confidence

- Business confidence declined for the fourth straight period in the second quarter. The drop stemmed mainly from heightened concern over firms' financial positions related to renewed economic instability in Asia and falling commodity prices.
- Business profits have fallen in the past two quarters, hit hard by low commodity prices and weak foreign demand. Given little prospect for a quick turnaround, investment plans may eventually be scaled down.



### Business Investment and Corporate Finances

\$ Millions, SAAR (unless otherwise noted)

	1996	1997	1997 Q3	1997 Q4	1998 Q1	1998 Q2
<b>BUSINESS INVESTMENT</b>						
<b>Machinery &amp; Equipment</b>	44,310	52,586	54,568	54,396	53,752	55,612
<i>(1992Q1) % change</i>	4.2	18.7	32.3	-1.3	-4.7	14.6
<b>Non-residential Construction</b>	33,581	36,637	37,332	37,036	38,284	38,956
<i>(1992Q1) % change</i>	4.3	9.1	10.7	-3.1	14.2	7.2
<b>Capacity Utilization (% Non-farm goods)</b>	82.1	84.6	85.4	85.5	85.7	85.6
Capacity Utilization (Mfg. sector)	82.5	84.9	85.8	85.8	86.2	86.2
<b>CORPORATE FINANCES &amp; ATTITUDES</b>						
<b>Corporate Operating Profits</b>	96,067	110,682	112,732	116,020	107,816	102,852
<i>(1992Q1) % change</i>	-1.1	15.2	21.3	12.2	-25.4	-17.2
Profits - Non-financial industries	71,871	82,218	82,656	84,760	79,676	73,896
<i>% change</i>	-6.7	14.4	4.0	10.6	-21.9	-26.0
Profits - Financial industries	24,194	28,462	30,072	31,260	28,140	28,956
<i>% change</i>	20.5	17.6	91.1	16.8	-34.3	12.1
<b>Business Credit</b>	570,653	620,412	627,130	646,767	660,392	674,568
<i>% change</i>	5.0	8.7	10.9	13.1	8.7	8.9
<b>Index of Business Confidence*</b>	147.0	162.3	164.9	159.2	155.0	148.9

\*Conference Board of Canada



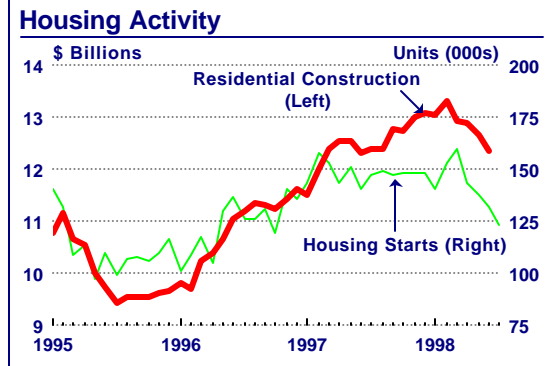
## Housing

### Spending on housing is down in the second quarter...

- Spending on Residential Construction declined in the second quarter, marking the third time in the past four quarters that activity in this sector has fallen.
- Though real estate commissions on sales of existing homes were up, new construction fell sharply. In addition to a general softening in housing demand, strike activity in some key trades has contributed to the weak results.

### ...but activity could rebound in coming months

- Housing starts registered their fifth consecutive monthly decline in July as labour disruptions continued to slow construction in Ontario, which normally accounts for more than a third of total housing starts. With most disputes now settled, starts could pick-up in coming months.
- The total value of residential building permits fell 3.4% in July, the third decline in four months. This weakness may be attributed partly to an increase in the number of newly-completed but unsold dwelling units.
- Sales of existing homes edged down in July. However, the recent increase in mortgage rates may prompt a short-term rise in activity as prospective buyers with pre-approved mortgages at lower rates opt to purchase now.



### Monthly Housing Indicators

	levels	Change since	
		last month	last year
<b>Residential Construction</b> (1)	12,344	-2.4%	0.1%
<small>(\$92M, factor cost basis)</small>			
<b>Building Permits, \$M</b> (2)	1,377	-3.4%	-1.0%
<b>Sales of Existing Homes</b> (2)			
<small>(# of units, unadjusted data)</small>			
<b>Housing Starts, # of units</b> (3)	123,100	-8,600	-24,600
Newfoundland	600	-100	-300
Prince Edward Island	300	-100	-100
Nova Scotia	1,800	-200	-1,100
New Brunswick	2,500	700	800
Quebec	14,300	-2,700	-5,800
Ontario	38,900	-7,200	-10,600
Manitoba	2,000	-400	-100
Saskatchewan	2,500	500	200
Alberta	20,700	1,900	3,800
British Columbia	18,800	-200	-6,500

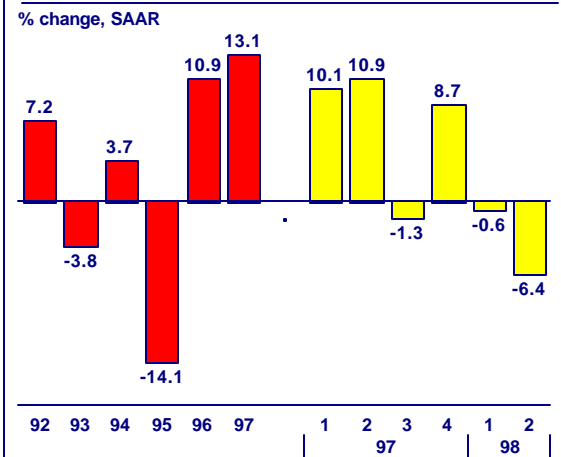
1 - June data; 2 - July data; 3 - July data.

Sources: Statistics Canada, Canada Mortgage and Housing Corporation, Canadian Real Estate Association

### Real Investment in Residential Structures

\$92 Millions, SAAR (unless otherwise noted)	1996	1997	1998 Q1	1998 Q2
<b>Residential Construction</b>	38,056	43,038	43,880	43,164
% change	10.8	13.1	-0.4	-6.4
Construction by Business sector	37,928	42,912	43,732	43,020
% change	10.9	13.1	-0.6	-6.4
New Housing	18,536	21,967	23,028	21,744
% change	8.5	18.5	2.3	-20.5
Alterations & Improvements	12,126	13,471	14,176	14,140
% change	7.4	11.1	9.9	-1.0
Ownership & Transfer Costs	7,394	7,600	7,188	6,676
% change	23.6	2.8	-25.6	41.4

### Growth in Real Residential Construction





## Trade and Competitiveness

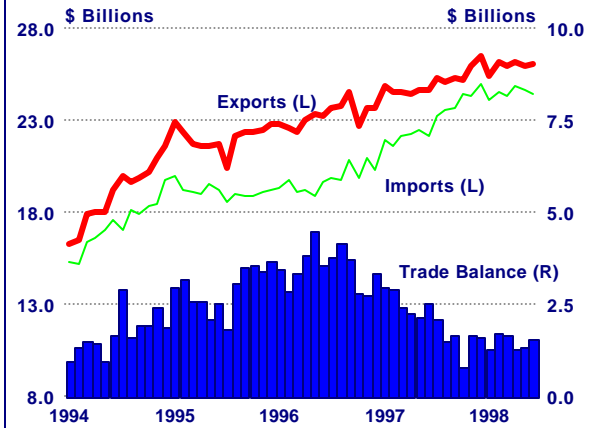
### Slightly higher exports...

- Merchandise exports edged up 0.1% in June. Plant closures and transportation problems led to a sharp reduction in exports of Automotive Products. However, these losses were offset by higher exports of Industrial Goods, M&E and Energy Products.
- Exports have not risen appreciably so far in 1998, mainly because of lower shipments to Japan and other Asian economies. For example, exports to Japan were down 27% in the first half of the year compared to the same period a year ago.

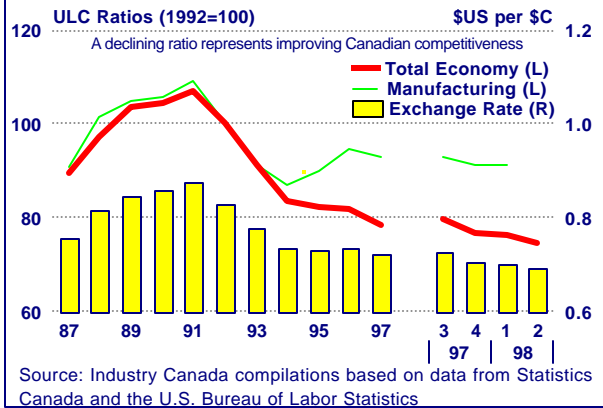
### ...and falling imports lead to a higher trade surplus in June

- Imports were down 0.8% in June, the second straight monthly decline. Lower imports of Automotive Products, again due to strike-related plant closures, were the main factor in this drop.
- The combination of slightly-higher exports and lower imports raised Canada's merchandise trade surplus to \$1.5 billion in June, up from \$1.3 billion in May.
- The fall in the dollar has led to a considerable improvement in Canada's competitive position against the U.S. On a common currency basis, Canadian unit labour costs fell 7.7% relative to those in the U.S. in the second quarter (annual rate).

### Merchandise Trade Flows and Balance



### Canada-U.S. Unit Labour Cost Ratios



### Merchandise Trade

June 1998	Levels (\$ millions)		Year-to-date (\$ millions)		Change (\$M)	% Change	
	1998 May	1998 June	1997 Jan-Jun	1998 Jan-Jun		May to June 1998	May to June 1998
<b>Exports</b>	<b>26,023</b>	<b>26,041</b>	<b>147,704</b>	<b>155,794</b>	<b>18</b>	<b>0.1</b>	<b>5.7</b>
to United States	21,581	21,410	118,469	128,637	-171	-0.8	7.5
<b>Imports</b>	<b>24,695</b>	<b>24,500</b>	<b>132,606</b>	<b>147,063</b>	<b>-195</b>	<b>-0.8</b>	<b>10.6</b>
from United States	19,017	18,550	100,712	112,590	-467	-2.5	9.0
<b>Trade Balance</b>	<b>1,328</b>	<b>1,541</b>	<b>15,098</b>	<b>8,731</b>	<b>213</b>		
with United States	2,564	2,860	17,757	16,047	296		
<b>Exports by Commodity</b>							
Agriculture/Fishing Products	2,100	2,053	11,923	12,474	-47	-2.2	1.5
Energy Products	1,979	2,022	13,634	11,670	43	2.2	-9.5
Forestry Products	2,865	2,878	17,610	17,412	13	0.5	-3.1
Industrial Goods & Materials	4,814	5,188	27,247	29,021	374	7.8	14.3
Machinery & Equipment	6,428	6,488	32,768	37,904	60	0.9	17.1
Automotive Products	5,934	5,497	34,369	36,104	-437	-7.4	-1.6
Other Consumer Goods	1,017	1,053	5,086	5,929	36	3.5	22.1
<b>Imports by Commodity</b>							
Agriculture/Fishing Products	1,427	1,457	7,532	8,424	30	2.1	16.2
Energy Products	739	856	5,344	4,688	117	15.8	5.2
Forestry Products	214	212	1,159	1,225	-2	-0.9	10.3
Industrial Goods & Materials	4,953	4,884	26,144	29,382	-69	-1.4	12.1
Machinery & Equipment	8,123	8,396	43,279	48,903	273	3.4	17.7
Automotive Products	5,418	4,866	28,772	32,024	-552	-10.2	-2.9
Other Consumer Goods	2,827	2,848	14,131	16,431	21	0.7	20.1



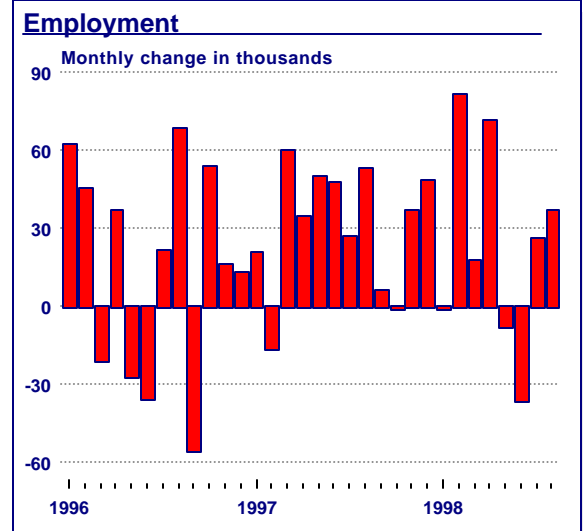
# LABOUR MARKET TRENDS



## Employment and Unemployment

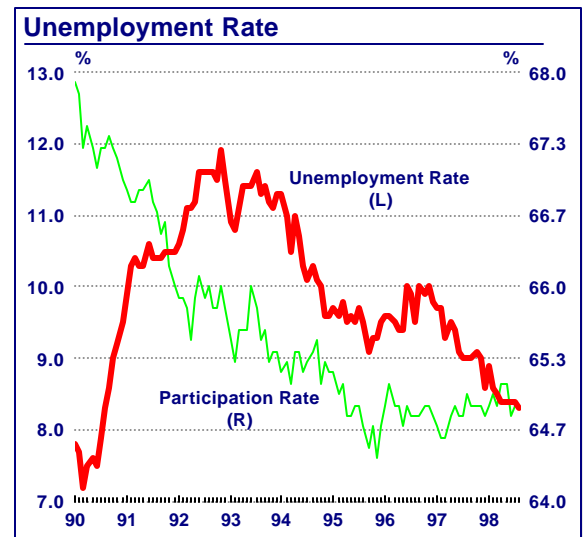
### Employment is up 37,000 in August...

- Following an increase of 27,000 in July, employment rose 37,000 in August. Job gains over the past two months have more than offset losses in May and June.
- The August gain was due entirely to an increase in the number of full-time positions, as part-time employment was down on the month.
- Youth employment once again accounted for a large share of the overall advance. Net job gains for youth in July and August have totalled 47,000, the best back-to-back performance in more than nine years.



### ...lowering the unemployment rate to 8.3%

- August job gains lowered the national unemployment rate by 0.1 percentage points to 8.3% – the lowest rate in eight years. The decline would have been greater if not for an increase in the number of people seeking work.
- The unemployment rate for youth fell 0.8 percentage points to 14.5% in August, and is now down two full points since the beginning of the year. The adult unemployment rate edged up slightly to 7.2% on the month.



### Labour Force Trends

(in thousands)	Levels			Change since			% Change since	
	1997 August	1998 July	1998 August	last month	last year	year-to-date	last month	last year
<b>Employment</b>	14,023.3	14,269.6	14,306.4	36.8	283.1	191.6	0.3	2.0
<b>Full-time</b>	11,304.2	11,585.0	11,626.7	41.7	322.5	125.1	0.4	2.9
<b>Part-time</b>	2,719.1	2,684.6	2,679.7	-4.9	-39.4	66.5	-0.2	-1.4
<b>Youth 15-24</b>	2,043.1	2,076.8	2,098.5	21.7	55.4	59.3	1.0	2.7
<b>Adult 25+</b>	11,980.1	12,192.8	12,207.9	15.1	227.8	132.3	0.1	1.9
<b>Self-employed</b>	2,540.1	2,499.7	2,555.4	55.7	15.3	79.4	2.2	0.6
<b>Unemployment</b>	1,386.8	1,310.5	1,298.7	-11.8	-88.1	-22.6	-0.9	-6.4
<b>Unemployment Rate</b>	9.0	8.4	8.3	-0.1	-0.7	-0.3		
<b>Youth 15-24</b>	16.6	15.3	14.5	-0.8	-2.1	-1.3		
<b>Adult 25+</b>	7.6	7.1	7.2	0.1	-0.4	0.0		
<b>Labour Force</b>	15,410.1	15,580.0	15,605.0	25.0	194.9	168.9	0.2	1.3
<b>Participation Rate</b>	65.0	64.9	64.9	0.0	-0.1	0.1		
<b>Employment Rate</b>	59.1	59.4	59.5	0.1	0.4	0.3		



## Industry Overview

### Retail Trade and Business Services post big job gains in August, but employment in Manufacturing falls

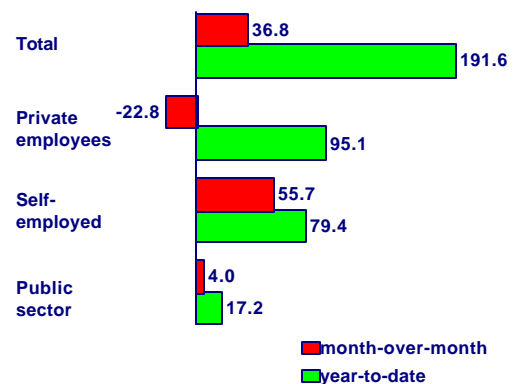
- Employment in Retail Trade and Business & Personal Services both advanced 20,000 in August, contributing to an overall gain of 46,000 in the Services-producing industries. Public Administration and Finance industries both posted declines on the month.
- Employment in the Goods-producing sector edged down 9,000 in August. There were 23,000 fewer jobs in Manufacturing, despite the return to work of those affected by the GM strike in the U.S.
- Elsewhere in the Goods sector, solid back-to-back increases propelled employment in Construction to a four-year high in August. Job gains in Agriculture could be related to the early harvest of some crops.

### Self-employment rises sharply for the second straight month

- The number of self-employed workers rose 56,000 in August, building on an increase of 22,000 the previous month.
- In contrast, the number of paid employees in the private sector fell 23,000 in August.

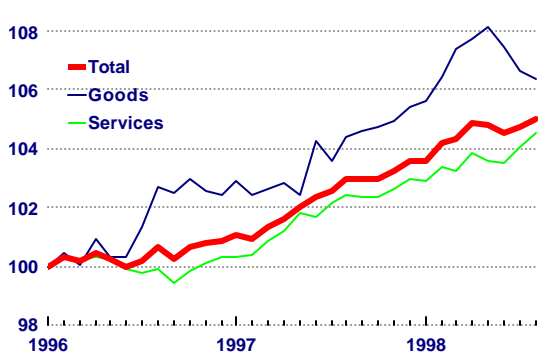
### Employment growth by worker category

August 1998 (thousands)



### Employment by major sector

January 1996 = 100



### Industrial Employment Trends

(in thousands)	Levels			Change since			% Change since	
	1997 August	1998 July	1998 August	last month	last year	year-to-date	last month	last year
<b>Total</b>	14,023.3	14,269.6	14,306.4	36.8	283.1	191.6	0.3	2.0
<b>Goods-producing</b>	3,791.5	3,872.7	3,863.6	-9.1	72.1	34.4	-0.2	1.9
Agriculture	421.1	430.3	446.1	15.8	25.0	31.3	3.7	5.9
Mining & Oil Wells	170.9	173.8	171.8	-2.0	0.9	-9.4	-1.2	0.5
Other Primary	119.1	117.9	107.3	-10.6	-11.8	-4.2	-9.0	-9.9
Utilities	140.9	131.9	129.5	-2.4	-11.4	-13.0	-1.8	-8.1
Manufacturing	2,191.5	2,264.8	2,242.2	-22.6	50.7	11.6	-1.0	2.3
Construction	747.9	754.0	766.7	12.7	18.8	18.2	1.7	2.5
<b>Service-producing</b>	10,231.8	10,396.9	10,442.8	45.9	211.0	157.2	0.4	2.1
TSCO*	910.3	908.0	911.2	3.2	0.9	-11.5	0.4	0.1
Wholesale Trade	657.8	679.9	686.2	6.3	28.4	19.2	0.9	4.3
Retail Trade	1,737.8	1,748.1	1,768.3	20.2	30.5	43.1	1.2	1.8
FIRE*	795.5	776.8	770.9	-5.9	-24.6	-35.6	-0.8	-3.1
Education	961.9	961.8	977.8	16.0	15.9	10.4	1.7	1.7
Health/Social Serv.	1,427.8	1,472.7	1,472.4	-0.3	44.6	22.6	-0.0	3.1
Bus. & Personal Serv.	2,947.5	3,037.4	3,056.9	19.5	109.4	91.8	0.6	3.7
Public Administration	793.2	812.2	799.0	-13.2	5.8	17.2	-1.6	0.7

\*TSCO: Transportation, storage and communication; FIRE: Finance, Insurance and Real Estate



## Provincial Overview

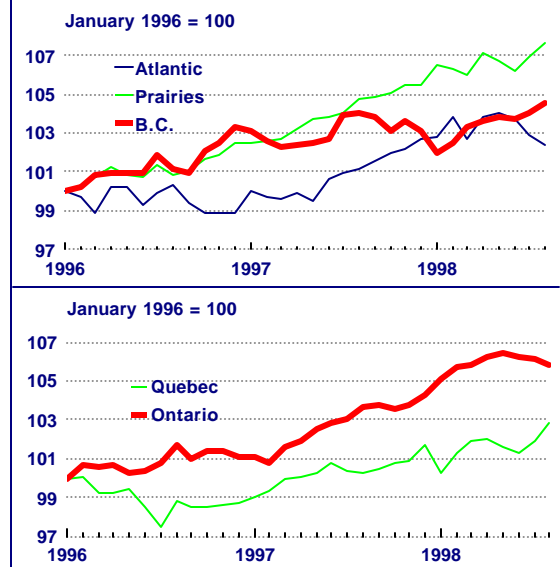
### Employment rises in 7 of 10 provinces, led by Quebec and Alberta...

- Employment was up 31,000 in Quebec in August, bringing total gains over the past two months to 49,000. This performance is in sharp contrast to the rather weak labour market conditions that prevailed in this province in the first half of 1998.
- Alberta posted another large gain, despite slowing activity in the oil patch.
- Ontario suffered its second straight decline (-18,000) due to job losses in Manufacturing. Given strength earlier in the year, however, employment is still up significantly on a year-to-date basis.
- In Newfoundland, job losses over the past two months have nearly offset gains in the first half of the year.

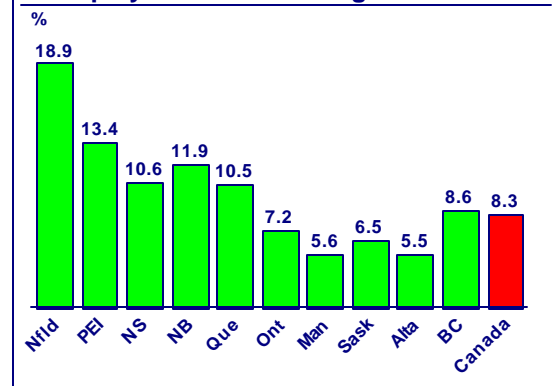
### ...but unemployment rates increase sharply in Newfoundland and Prince Edward Island

- Back-to-back job losses in Newfoundland led to sharp increases in its unemployment rate in both July and August. As of August, the unemployment was 18.9%, compared to 16.6% in June. In Prince Edward Island, the unemployment rate was also up sharply in August.
- Employment growth in both Quebec and British Columbia led to significantly-lower unemployment rates in these provinces.

### Regional employment patterns

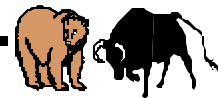


### Unemployment Rates -- August 1998



### Provincial Employment and Unemployment Trends

	Employment (thousands)						Unemployment rate (%)		
	Levels	Change since last month		Change since last year		Levels	Change since		
	1998 August	(000's)	%	(000's)	%		last month	last year	
Canada	14,306.4	36.8	0.3	283.1	2.0	8.3	-0.1	-0.7	
Newfoundland	190.4	-7.0	-3.5	-3.3	-1.7	18.9	1.4	0.7	
P.E.I.	60.7	-1.7	-2.7	-0.4	-0.7	13.4	1.0	-0.7	
Nova Scotia	402.1	0.8	0.2	9.7	2.5	10.6	0.0	-1.0	
New Brunswick	321.2	2.8	0.9	5.2	1.6	11.9	0.7	-0.4	
Quebec	3,340.8	30.5	0.9	83.3	2.6	10.5	-0.4	-1.0	
Ontario	5,572.5	-17.5	-0.3	110.1	2.0	7.2	0.0	-1.0	
Manitoba	549.6	2.5	0.5	11.2	2.1	5.6	0.3	-0.6	
Saskatchewan	478.0	2.0	0.4	0.5	0.1	6.5	0.5	0.8	
Alberta	1,527.3	14.1	0.9	57.1	3.9	5.5	0.1	-0.3	
B.C.	1,863.8	10.3	0.6	9.9	0.5	8.6	-0.5	0.0	



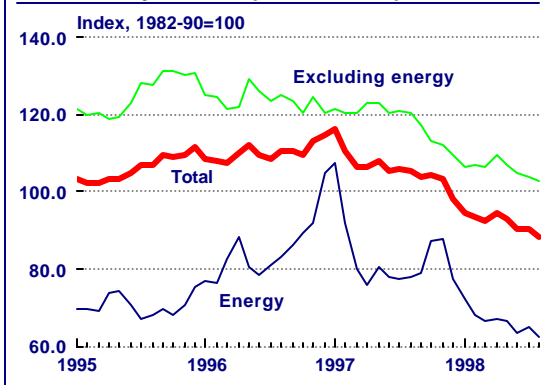
### Inflation holds steady at 1.0% in July...

- The annual rate of CPI inflation was 1.0% in July, the same as in June. "Core" inflation, which excludes indirect taxes and the volatile food and energy components, was also 1.0% in July, the bottom end of the official 1-3% target band established jointly by the Bank of Canada and the Department of Finance.
- Compared to last year, the largest price hikes in July were for university tuition, tobacco products, travel tours, telephone services and natural gas. These increases were partly offset by lower costs for gasoline, mortgage interest charges and computers.
- Underlying inflationary pressures remain subdued. Commodity prices are down sharply compared to last year and producer prices remain well-behaved.

### ...with the lowest rates in P.E.I. and Newfoundland

- In July, the overall price level was down 1.0% on a year-over-year basis in Prince Edward Island, the only province to record an overall price decline on the year. Sharply-lower shelter costs in this province can be traced to declining house prices and home insurance costs. Inflation is also quite low in Newfoundland (+0.1%).
- Saskatchewan and Alberta had the highest inflation rates in July (1.5%).

### Commodity Prices (\$U.S. basis)



### Consumer Prices

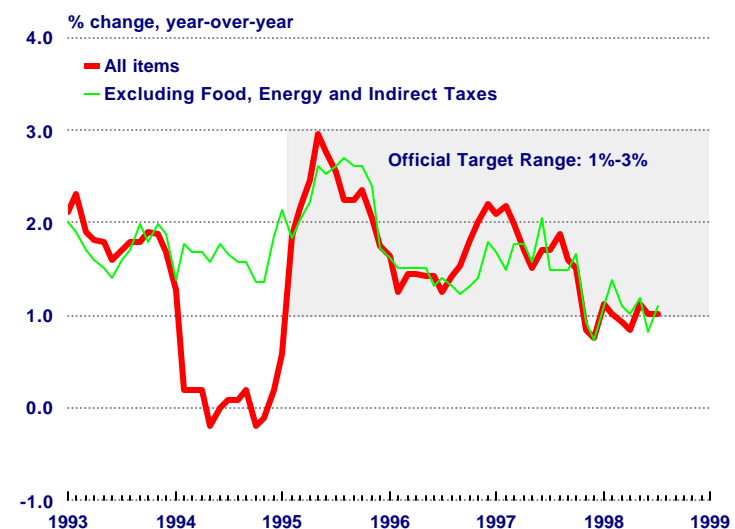
July 1998

	Index (1992=100)	% Change	
		since month	last year
<b>All items CPI</b>	108.8	0.0	1.0
Food	109.9	-0.3	1.4
Shelter	103.6	0.1	0.3
Household operations	108.0	0.0	1.5
Clothing & Footwear	102.6	-0.6	1.1
Transportation	120.4	-0.2	-0.4
Health & Personal Care	108.4	0.2	2.2
Recreation, Educ. & Reading	119.4	0.8	2.3
Alcohol & Tobacco	92.8	0.2	4.2
<b>CPI excl. Food &amp; Energy</b>	109.0	0.2	1.3
Energy	104.2	-0.9	-3.1

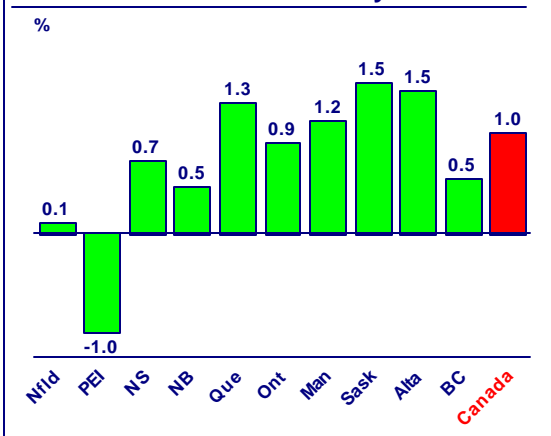
### Commodity Prices (August)

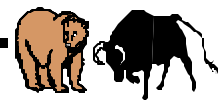
Index, 1982-90=100	88.6	-2.0	-16.1
Excluding Energy	102.6	-1.2	-14.9
Energy	62.5	-4.1	-19.7

### Consumer Price Index



### Provincial CPI Inflation -- July 1998



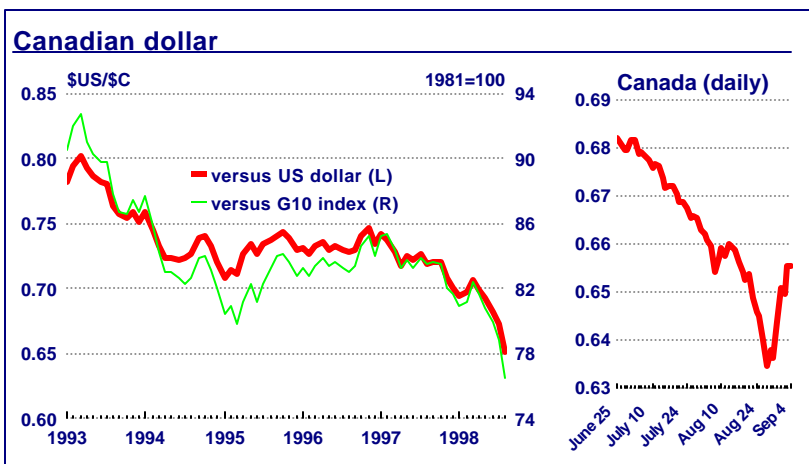


### The Canadian dollar and stock markets fall sharply in August..

- The Canadian dollar encountered intense selling pressures through most of July and August, closing at a new all-time low of US63.31¢ on August 27 – down nearly eight full cents from its recent peak in March. The dollar's weakness has been attributed to economic and political instability in the Asia Pacific region and more recently Russia, which has prompted a flight of international capital to the "safe haven" U.S. dollar. This turmoil has also resulted in sharply-lower prices for commodities, further undermining the dollar given the widely-held view that our currency is closely linked to commodities.
- Global market turmoil, falling commodity prices and lower corporate profits also triggered substantial declines in Canadian stock prices. The TSE 300 index fell 20% in August, its biggest monthly loss since October 1987. While the U.S. market has fared better than its Canadian counterpart, U.S. share prices are also down sharply from previous highs.

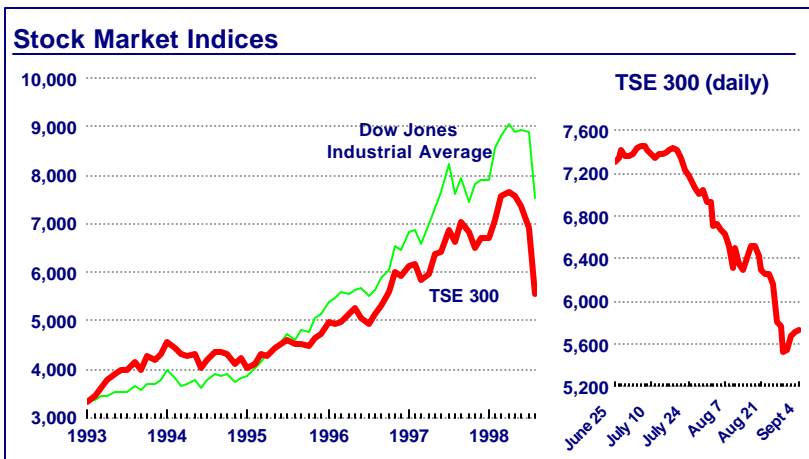
### ...but recover some of these losses early in September

- A modest rebound in commodity prices and hopes of an interest rate cut in the U.S. lent support to both the Canadian dollar and stock markets early in September. By September 4, the Canadian dollar had partly recovered to US65.54¢ and share prices had recouped some of their previous losses.



### The Canadian Dollar

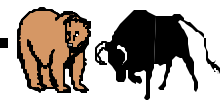
(close)	\$US vs. \$Cdn	index vs. G-10 (81=100)	DM vs. \$Cdn	yen vs. \$Cdn
1996	0.7296	84.00	1.139	83.64
1997	0.6991	81.62	1.247	90.87
1998 Mar	0.7043	82.35	1.290	91.11
Apr	0.6988	81.63	1.268	92.21
May	0.6863	80.83	1.228	93.37
June	0.6813	79.96	1.223	95.71
July	0.6614	78.82	1.207	94.69
Aug	0.6361	76.50	1.164	94.15
Sept. 4	0.6554			



### Key Stock Market Indexes

	August Close	% change from	
		last month	last year
<b>TSE 300</b>	<b>5,531</b>	<b>-20.2</b>	<b>-16.4</b>
Oil & Gas	4,398	-21.2	-38.5
Metals & Minerals	2,500	-22.5	-49.2
Utilities	6,399	-15.9	18.2
Paper & Forest	3,181	-22.2	-37.7
Merchandising	4,962	-19.9	-15.0
Financial	6,768	-28.1	-4.2
Services	4,229	-21.6	-48.4
Price-Earnings Ratio*	23.3	-6.3	1.0
<b>S&amp;P 500</b>	<b>957</b>	<b>-14.6</b>	<b>6.4</b>
<b>Dow Jones</b>	<b>7,539</b>	<b>-15.1</b>	<b>-1.1</b>

\*columns 2 & 3 reflect change in levels

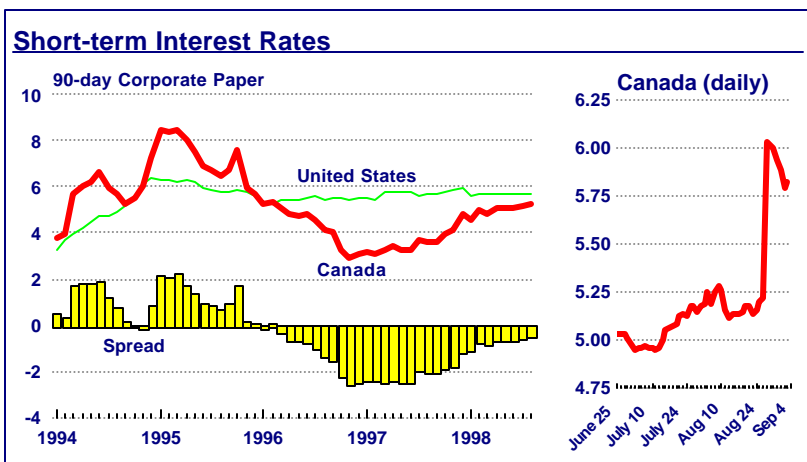


### *The Bank of Canada raises interest rates to defend the dollar...*

- In a bid to bolster confidence in the Canadian dollar, the Bank of Canada raised its trend-setting Bank Rate to 6.0% on August 27, an increase of one full percentage point.
- The Bank's aggressive move prompted corresponding increases in consumer and business lending rates. The prime rate jumped up one full percentage point to 7.5%, its first increase in eight months. Mortgage rates were also up across the board, ranging from a hike of 70 points in the one-year rate to a 40-point rise in the five-year rate.
- The uncertain outlook for the Canadian dollar has reduced the attractiveness of Canadian dollar-denominated assets. Thus, even though the underlying fundamentals of low inflation and improved government finances remain in place, bond yields in Canada rose sharply toward the end of August.

### *...pushing Canadian rates above U.S. rates across all maturities*

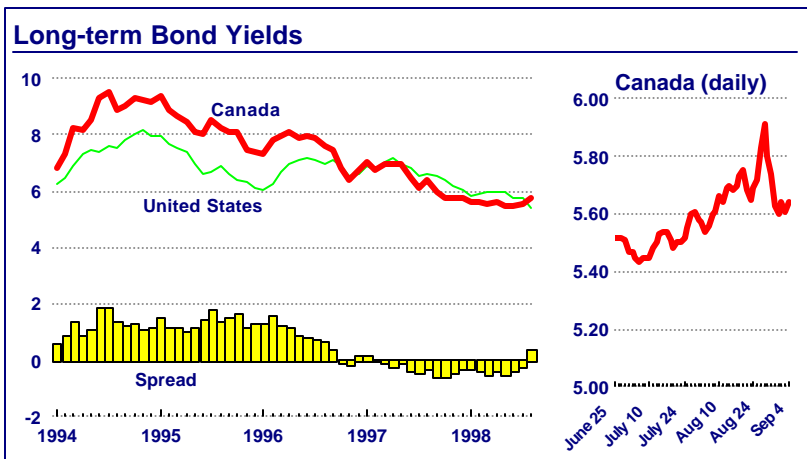
- Short-term and long-term rates in the U.S. have held steady in recent months – in fact, bond yields have actually fallen slightly in response to an influx of foreign capital. As a result, the Canadian yield curve now lies above that of the U.S. across all maturities – a reversal from previous months when Canada's yield curve was below that of the U.S.



#### Key Money Market Rates

(end of period)	90-day Corporate Paper	spread against U.S.	Long Bond Yield	spread against U.S.
1996	3.13	-2.42	7.09	0.51
1997	4.80	-1.17	5.95	0.03
1998 Mar	4.84	-0.80	5.70	-0.23
Apr	5.04	-0.63	5.76	-0.31
May	5.04	-0.61	5.61	-0.22
June	5.06	-0.60	5.52	-0.13
July	5.14	-0.53	5.61	-0.15
Aug	5.22	-0.44	5.83	0.41
Sept. 2	5.88	0.30	5.60	0.26

A positive spread indicates that Canadian rates are above their U.S. counterparts.



#### Key Lending Rates

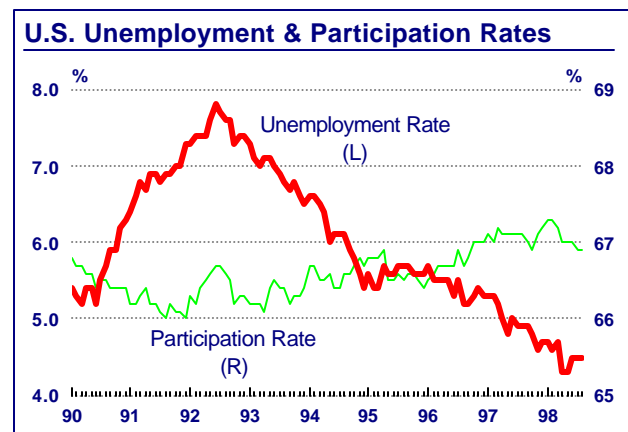
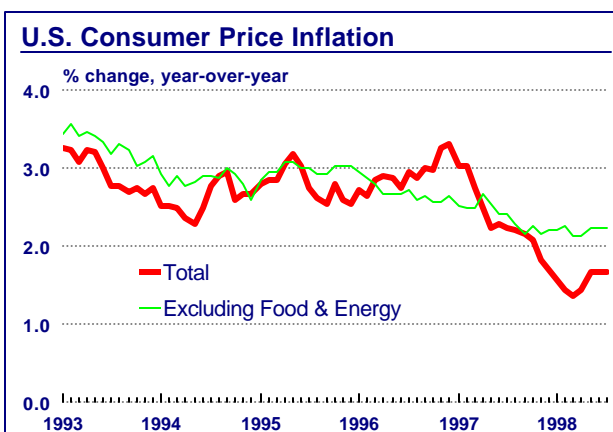
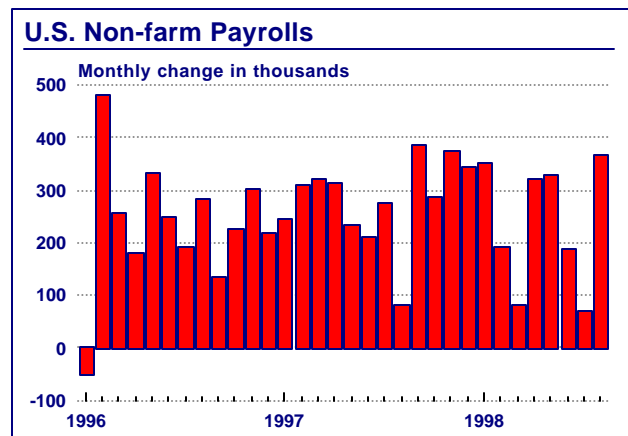
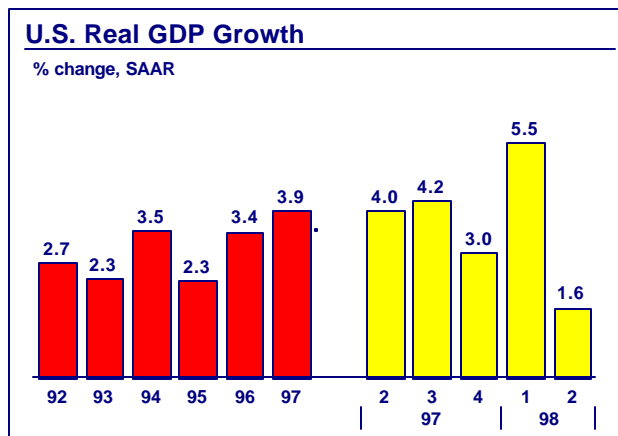
(end of period)	Bank Rate	Prime Lending Rate	Mortgage Rate 1 year	Mortgage Rate 5 year
1996	3.25	4.75	5.20	6.95
1997	4.50	6.00	6.65	7.05
1998 Mar	5.00	6.50	6.40	6.85
Apr	5.00	6.50	6.55	6.95
Ma	5.00	6.50	6.55	6.95
June	5.00	6.50	6.55	6.95
July	5.00	6.50	6.55	6.95
Aug	6.00	6.50	7.45	7.55
Sept. 2	6.00	7.50	7.45	7.55



## U.S. Economic Trends

### Highlights...

- Preliminary estimates show that the U.S. economy expanded at an annual pace of 1.6% in the second quarter, down markedly from 5.5% in the first quarter. Final domestic demand remained the main engine of growth in the second quarter, buoyed by robust consumer spending and strong increases in M&E investment and residential building. Output growth was moderated by lower exports and a sharp downturn in inventory investment.
- Non-farm payroll employment increased 365,000 in August, following a gain of just 68,000 in July. The August rebound reflects the return of workers affected by auto-related strikes and plant shutdowns in July. The unemployment rate held steady at 4.5% for the third straight month.
- Despite sustained growth over the past year, inflation remains subdued. The GDP deflator was up 1.0% from its year-ago level in the second quarter, a 30-year low. In July, the annual rate of CPI inflation was 1.7%, the same as in May and June. Core inflation excluding the volatile food and energy components was 2.2%, the rate around which it has hovered for almost a year.
- The Federal Reserve is expected to leave interest rates unchanged at the upcoming Federal Open Market Committee (FOMC) meeting on September 29. However, given slower growth and low inflation, plus increased uncertainty regarding the effect on the U.S. economy of the Asian/Russian crises and the drop in equity prices, a growing number of analysts believe that the next move on the part of the Federal Reserve will be to lower interest rates.





**Rising Skill Intensity in Canada: Evidence and Explanations**

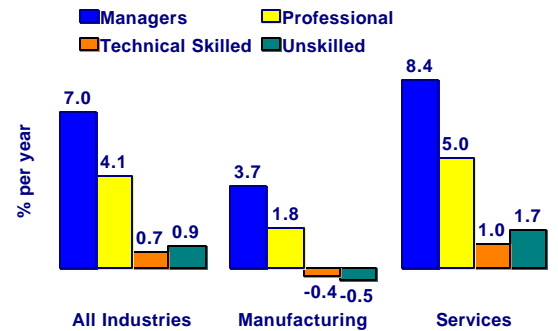
**Total hours worked has grown faster for skilled workers than for unskilled workers...**

- Over the 1981-94 period, total hours worked by skilled workers grew 2.9% per year in the non-primary business sector.
- Among skilled workers, managers were the fastest growing occupation in terms of hours worked, with an average annual increase of 7.0%.
- By comparison, total hours worked for unskilled workers rose only 0.9% per year.

**...and skill intensity has been rising in almost all Canadian industries**

- The skill requirements of Canadian industries – as defined by the share of skilled workers in total hours worked – increased from 35.5% in 1981 to 41.4% in 1994.
- Skill intensity tends to be higher in the Service sector than in Manufacturing. In 1994, managers, professional and technical skilled accounted for roughly 44% of total labour input in Services, compared to about 34% in Manufacturing industries.
- Although skill upgrading over the 1981-94 period was pervasive across Canadian industry, the increase was greater in the Service sector. The share of skilled workers was up 5.5 percentage points in Services, compared to an increase of 4.7 percentage points in Manufacturing.

**Growth in Hours Worked by Skill Level\*: 1981-94**



\* Skill classification based on the National Occupational Classification (1993). Skilled workers include managers, professionals, and technical skilled workers.

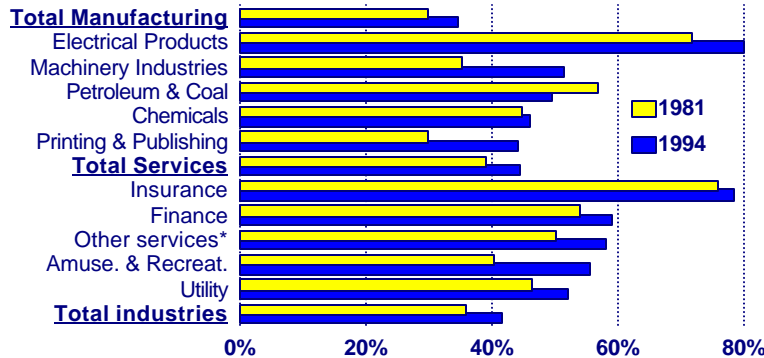
Source: Compilations based on Statistics Canada data.

**Skill Composition for the Non-Primary Business Sector: 1981-94\***

	Skilled Workers:				Unskilled Workers:
	Total	Mgrs.	Profess	Tech.	
1981	35.5	6.0	7.1	22.4	64.5
1986	39.7	10.9	7.6	21.2	60.3
1987	39.6	10.7	7.8	21.1	60.4
1988	39.7	10.9	7.8	21.1	60.3
1989	40.1	11.0	8.1	21.0	60.0
1990	40.0	10.8	7.8	21.4	60.0
1993	41.5	11.6	9.4	20.4	58.6
1994	41.4	12.0	9.7	19.7	58.6

\*Data gaps are due to the unavailability of surveys.

**Skill Intensity\*: 1981-1994**



\* Skill intensity is defined as the share of skilled workers (managers, professional and technical skilled) in total hours worked. Other services include services to business.  
Source: Compilations based on Statistics Canada data.



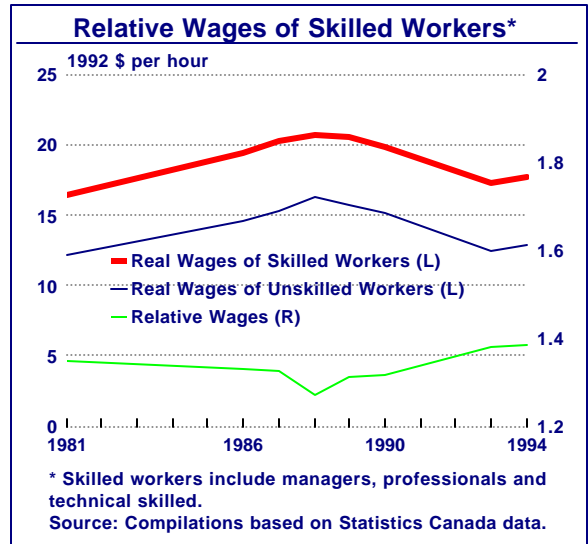


***The wage premium for skilled workers was roughly the same in 1994 as in 1981...***

- In 1981, managers, professionals and technical skilled workers earned 35% more on average than did unskilled workers.
- Real wage rates for both skilled and unskilled workers increased over the 1981-1988 period. However, since wages for unskilled workers rose at a faster pace than did those for skilled workers, the gap between skilled and unskilled wages narrowed to 27% by 1988.
- After peaking in 1988, wages for both skilled and unskilled workers fell in real terms until a modest recovery in 1994. By 1994, the wage premium for skilled workers was 38%, slightly higher than that prevailing in 1981.

***...suggesting that the supply of skills is keeping pace with demand***

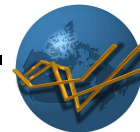
- In a simple labour demand and supply framework, the skill premium will remain unchanged if the supply of skills keeps pace with the rising demand for skills.
- Indeed, the overall skill level of the Canadian labour force has increased significantly. Between 1981 and 1994, members of the labour force with post-secondary degrees or higher more than doubled in number, while those with high school degrees or less declined dramatically.



**Real Wage Rates (1992 dollars per hour): 1981-94\***

	Skilled Workers:				Unskilled Workers:
	Total	Mgrs.	Profess	Tech.	
1981	16.38	19.78	18.64	14.75	12.14
1986	19.48	20.22	21.33	18.41	14.66
1987	20.31	21.28	22.52	19.01	15.31
1988	20.66	21.18	22.67	19.65	16.26
1989	20.58	21.13	22.61	19.51	15.69
1990	19.91	20.38	21.74	19.00	15.14
1993	17.27	18.74	18.84	15.71	12.51
1994	17.78	19.42	19.32	16.04	12.86

\*Data gaps are due to the unavailability of surveys.



# Rising Skill Intensity in Canada: Evidence and Explanations

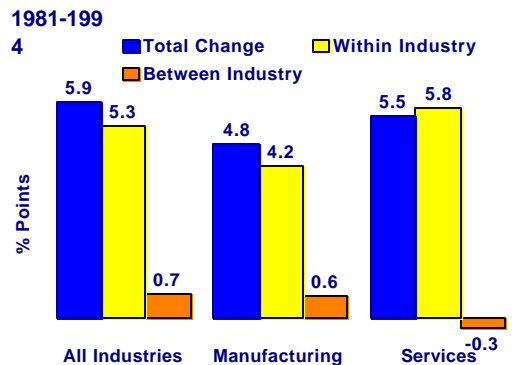
## Two major explanations have been put forward for skill upgrading: skill-biased technical change and globalization

- A number of economists argue that technological changes made possible by the explosion of computing power tend to be biased in favour of skilled workers. This explanation would apply across all industries.
- An alternative explanation points to globalization, especially increased trade with less-developed countries. This should cause a shift in production between industries, *i.e.*, from less skill-intensive to more skill-intensive sectors.

## Skilled-biased technical change appears to be the most important factor in Canada

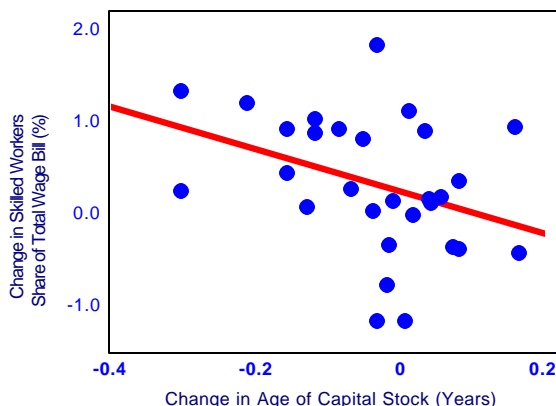
- The increase in skill intensity at the aggregate level since the early 1980s can be explained almost entirely by changing skill intensity *within* each industry rather than shifts in production from less skill-intensive to more skill-intensive industries. This is consistent with the view that skill-biased technical change is the major factor explaining skill upgrading.
- In addition, skill intensity is found to be positively correlated with a number of measures of technical change, such as changes in the R&D stock, patent stock and the age of capital stock across industries. This also suggests that most of the skill upgrading in Canada can be explained by technical changes.

### Decomposing Changes in Skill Intensity



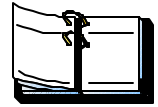
\* Skill intensity is defined as the share in total employment of managers, professionals and technical skilled workers.

### Correlation between Age of the Capital Stock and Share of Skilled Workers in the Total Wage Bill: 1981-94



\* Skilled workers include managers, professionals and technical skilled workers.

## COMING UP



### Key Future Data Releases and Planned Events

#### CANADA

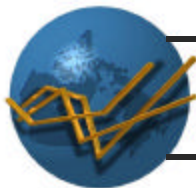
International Trade -- July .....	September 17
Consumer Price Index -- August .....	September 18
GDP at factor cost -- July .....	September 30
Labour Force Survey -- September .....	October 9
Economic and Fiscal Update (Dept. of Finance) .....	October
Business Conditions Survey .....	November 2
Financial Statistics for Enterprises, 3rd Quarter, 1998 .....	November 20
National Economic & Financial Accounts, 3rd Quarter, 1998 .....	November 30
Balance of International Payments, 3rd Quarter, 1998 .....	November 30
Monetary Policy Report (Bank of Canada) .....	November

#### UNITED STATES

Consumer Price Index -- August .....	September 17
International Trade -- July .....	September 17
GDP -- 2nd Quarter 1998, final .....	September 24
Federal Open Market Committee meeting .....	September 29
Employment Situation -- September .....	October 6
Federal Open Market Committee meeting .....	November 17

Note: the September MEI uses data available as of September 4, 1998

The Special Report scheduled for the October MEI is entitled  
"Intrafirm Trade of Foreign Subsidiaries in Canada"



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***Micro Economic Policy Analysis***  
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