

Economic Spotlight

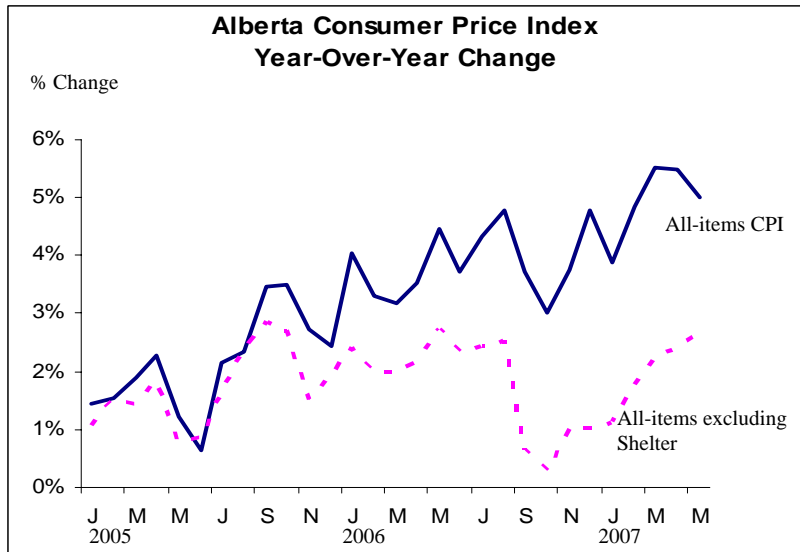
ALBERTA'S CONSUMER PRICE INDEX (CPI)

Summary

Alberta's all-items CPI inflation rate has averaged 4.9% so far in 2007, up a full percentage point from its average of 3.9% in 2006 (and 2.1% in 2005). The sharp rise in shelter costs continues to drive inflation in Alberta, though other inflation pressures are beginning to emerge. Interestingly, the 2006 increase in new house prices was almost double the increase in the residential construction cost index.

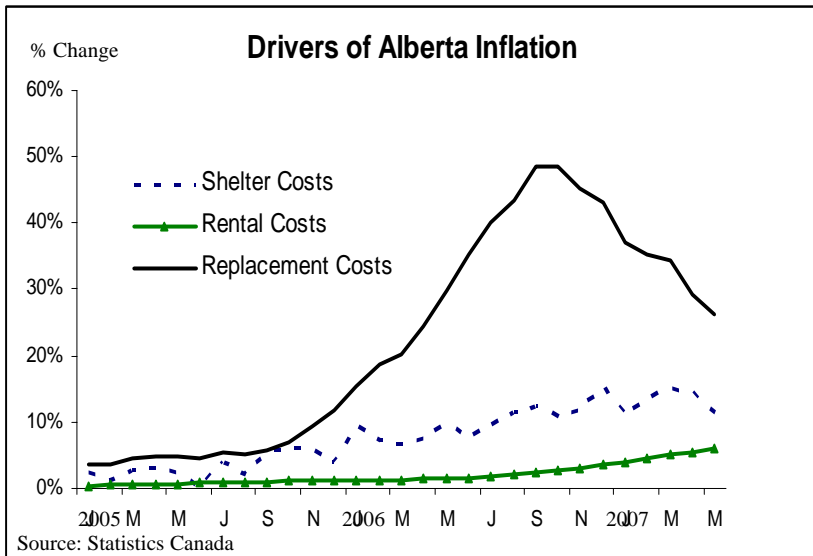
Alberta All-items CPI

Alberta's all-items CPI inflation rate was at 5% in May, half a percentage point below the April and March rate of 5.5%. The effect of a surge in consumer prices in May of last year was the main reason for the decline in inflation. An 18% decline in natural gas prices also contributed to the reduction. Shelter costs contributed 2.3 percentage points to the increase in Alberta's CPI in May.



Source: Statistics Canada

The sharp rise in Alberta's inflation is being driven by the rising cost of shelter, in particular, homeowners' replacement costs and rental costs. Excluding shelter, which has a weight of about 28% in the overall index, the year-to-date increase in Alberta's CPI is 2.0%.



Source: Statistics Canada

Shelter

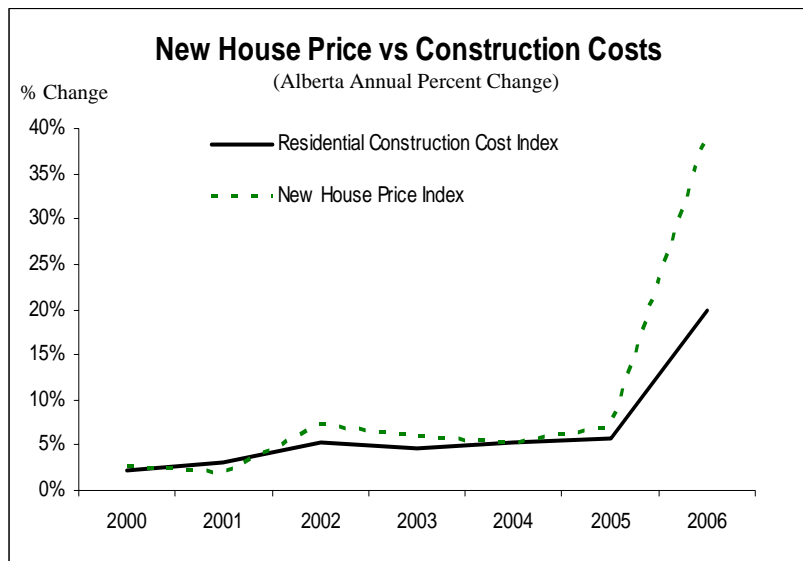
Overall shelter costs, which include rental and owned accommodations, increased by 11.5% between May 2006 and May 2007, the smallest increase since the beginning of 2007. Although the CPI index for rental accommodation was up 5.9% in May, the bulk of the increase was due to the index for owned accommodation, which was up 16.8%. Water, fuel and electricity prices were down 0.4%, as an 18% decline in natural gas prices outweighed a 13% increase in electricity prices.

The owner accommodation cost index has five categories: mortgage interest costs, homeowners' replacement costs, property taxes, insurance premiums and maintenance and repair. Most of the increase came from homeowners' replacement cost, which rose by 26.3% between May 2006 and May 2007, its slowest year-over-year increase since April 2006. Homeowners' insurance premiums also rose by 26.3% over the same period, as insurance costs are strongly influenced by home replacement costs. The property tax index was up 3.6% in May, while repairs and maintenance were up 0.1%.

The home-owner's replacement cost index is measured by the house-only component of new house prices. Fuelled by record inter-provincial migration and rising wages and personal incomes in the past three years, strong demand for residential construction has caused a spike in home prices in Alberta. The new house price index (house-only) surged 39.6% in 2006, compared to 10.2% for Canada as a whole. In the first four months of 2007, Alberta new house prices averaged almost a 32% increase, one of only two provinces to register double-digit increases in new house prices. Saskatchewan new house prices are up 18% so far this year. Although the pace of growth in Alberta's new house price index has moderated from its peak of 53.5% in August, the year-over-year increase remains high.

So far in 2007, the new house price index is increasing at a faster rate in Edmonton (35%) than in Calgary (29%). Increases in land prices are out-pacing increases in house building costs, with the land price index surging 55% in Edmonton and 46% in Calgary.

In general, the new home price index tends to follow trends in the residential construction cost index. However, the link broke in 2006 when gains in new house prices (39.6%) exceeded the increase in residential construction costs (19.8%). It appears that recent increases in new house prices are not entirely due to rising costs for materials, energy and labour, but rather strong demand for Alberta housing is putting upward pressure on prices.



Source: Statistics Canada

Other Sectors

Food

Alberta food prices were up 4.9% in May 2007 from May 2006, compared to a 3.5% increase for Canada as a whole. Increases were led by double digit gains in prices for fresh fruits (13.7%) and vegetables (10.8%), but prices were also up for bakery and other cereal products (6.4%), meat (5.7%) and dairy products (4.1%). In 2006, food prices were up 2.9% in Alberta and 2.4% nationally. The International Monetary Fund estimates world food prices increased 10% in 2006, driven by corn, wheat and soybean oil prices.

One of the main drivers for the escalation in food prices has been the increased demand for ethanol blended fuel production, particularly in the United States using corn. After nearly doubling in the past couple of years, prices for corn have contributed to widespread price increases in alternative grains and oilseeds, animal feed products, as well as many of the food products available to consumers.

Canadian raw material prices have surged for wheat (28%), barley (36%), corn (40%), oilseeds (34%) and canola (42%) in the first five months of 2007. This follows modest gains in 2006 and in most cases price declines in the previous two years.

Consumer liquidity in Asian countries, combined with droughts in Australia and New Zealand as well as lower subsidies in the European Union are contributing to an increased international demand for fresh products (including dairy products), tighter worldwide supplies and higher prices.

Alberta **Energy** prices as a whole were up 2.1% in May. A large decline in natural gas prices (-18.1%) brought down the overall sub-index, as prices for electricity (13.2%) and gasoline (6.3%) were up strongly. Prices for water utilities were also up 10.2% in May.

Conclusion

Alberta's CPI inflation rate is likely to remain elevated this year as year-over year increases in house prices remain high. Food and energy prices are also likely to maintain upward pressure on overall prices. Overall inflation is expected to temporarily increase in July when the impact of the 2006 GST tax cut disappears.