

# **BUDGET PAPER A:**

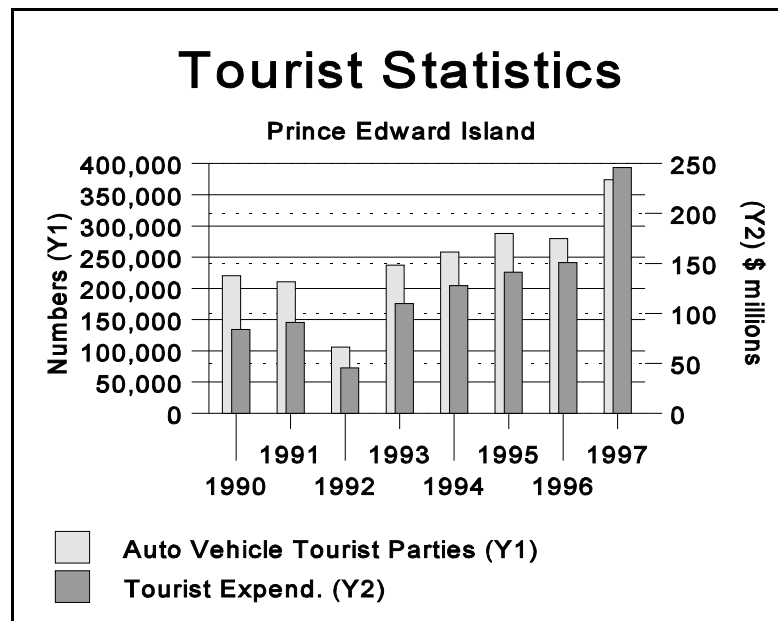
## **BACKGROUND NOTES ON THE ECONOMY**

---

- The fiscal pressures that affect the Prince Edward Island Budget arise from specific fiscal issues that pertain to the province, local economic circumstances, as well as the broader economic and financial environment that impact on all aspects of the national and provincial economy. The purpose of this note is to provide information on the economic and financial environment in the Budget period.
- The prevailing economic situation in Canada in 1997 and 1998 is closely related to the relatively favourable economic situation in the USA. The current economic environment in North America at the present is characterized by a strong US Dollar, low inflation, low unemployment and sustained economic expansion. The latest estimates of Gross Domestic Product by the US Department of Commerce indicate that in 1997 the US economy expanded by 3.8%, in constant dollars. This follows growth of 2% in 1995 and 2.8% in 1996. Private forecasts indicate that the US economy is expected to continue to expand in 1998 and 1999, by 2.5% and 2.3% respectively.
- Interest rates increased somewhat during 1997 but are at low levels relative to recent economic history. The low Canadian interest rates relative to those in the US placed the Canadian Dollar under continuing pressure, relative to the US Dollar, and this was accentuated in late 1997 and early 1998 when the Canadian Dollar fell below 70 cents US. The low value of the dollar has improved Canadian competitiveness and Canadian exports performed well in 1997, up by 8.6% over 1996 in constant dollars.
- According to Statistics Canada, the growth of the Canadian economy matched the US expansion of 3.8% in 1997, and this represented a significant improvement over the 1.2% gain posted for 1996 and 2.2% increase in 1995. Inflation in Canada remained at very low levels, with the CPI increasing by only 1.6% in 1997. The level of Canadian unemployment rate declined slightly in 1997, to 9.2% from 9.7% in 1996. The number of Canadians employed increased by 1.9% in 1997. The recent federal budget indicated that federal finances were in balance and are projected to remain balanced in the coming years.
- Economic projections by private sector forecasters indicate that the Canadian economy will continue to expand in the coming years, in the order of 3% in both 1998 and 1999. Inflation is expected to remain low at about 1.6%. Short term interest rates are also expected to continue to be low, with the 3 month Federal Treasury Bill Rate having averaged 3.2% in 1997, and anticipated to stay at its current level of 4.6% in 1998.
- In terms of future risks associated with the national economy the volatility of the economies in the Asian region is the most apparent, in view of the open global economy. However the spillover impacts of these recent economic reversals on the North American economy,

through trade and capital linkages, are estimated to be slight. For Canada the primary resource sectors, such as base metals and lumber are most affected.

- For Prince Edward Island, the most significant economic event of 1997 was the completion and opening of the Confederation Bridge on June 1st. The positive economic impacts of this event have been very considerable. The total number of tourist parties visiting the Island in 1997 in total was up by 30% over 1996. Expenditures by tourists in 1997 are estimated at

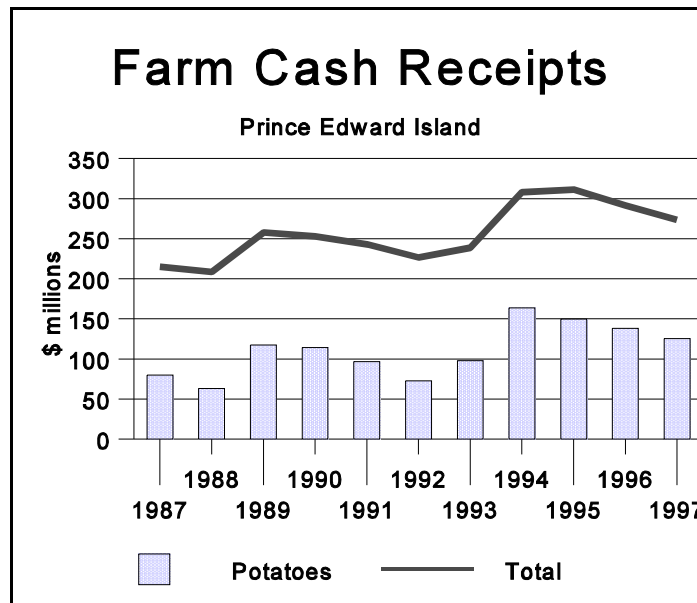


\$245.9 million, an increase of 63% from 1996.

- The Conference Board of Canada had predicted a modest economic downturn for PEI in 1997 as the construction activity associated with the Bridge wound down and the Marine Atlantic ferries ceased to operate. Their latest estimates indicate that on balance the positive economic impacts outweighed the negative and they now estimate that GDP expanded by 0.7% in constant dollars in 1997.
- The average monthly level of employment in 1997 on the Island reached 60,500 according to Statistics Canada, up by 400 from 1996. The unemployment rate increased from 14.5% to 14.9% as the local labour force increased by 700.
- The local inflation rate remained extremely low in 1997, with the PEI Consumer Price Index averaging an increase of only 1.3%.
- Evidence of the renewed confidence in the PEI economy was found in a sharp escalation in

motor vehicle sales and retail sales generally. The number of new motor vehicles sold in 1997 was up by 14.5% over 1996. The value of retail trade on PEI in 1997 is estimated by Statistics Canada to have reached \$1,023.5 million. This represents an all time record and an increase of 8% over 1996. Despite this strong local market, the financial difficulties facing Eatons nationally spilled over into the Province when the company announced closure of its downtown Charlottetown store early in 1998.

- Income growth on Prince Edward Island in 1997 was affected by the changes to the Unemployment Insurance Program, now named the Employment Insurance Program, which went into effect during the year. The 1997 statistics on Employment Insurance Income indicate that for PEI there was a small increase in total benefits received following the significant drop that occurred since 1993. The total number of EI weeks paid on PEI increased from 625,490 in 1996 to 628,660 in 1997. Benefits paid under Part I and II of the program increased from \$167.2 million to \$175.2 million. These amounts can compare with the \$215.6 million paid under the UI program to Islanders in 1993.
- The farm sector on PEI was negatively affected by weak potato prices and a delayed harvest. Consequently the value of potato sales in 1997 fell to \$125.3 million, from \$138.0 million in 1996. Livestock sales increased significantly in 1997 but overall farm cash receipts measured only \$273.3 million, compared to \$291.4 million in 1996 and \$311.3 million in 1995.



- Preliminary statistics on fishing indicate that PEI enjoyed a solid year with the lobster harvest valuing \$73.1 million, compared to \$61.7 million in 1996. The value of all fish harvested in 1997 is recorded as \$111.9 million.

- Capital investment on PEI was clearly impacted by the completion of the Confederation Bridge. The total value of private and capital expenditures in 1997 was \$489.9 million according to Statistics Canada, which compares with \$493.6 million in 1996 and \$518.8 million in 1995. The number of Housing Starts were also down in 1997, numbering 470, compared to 554 the previous year.
- 1998 represents the first full year in which the overall impact of the Bridge can be measured. The Conference Board of Canada projects that the Island economy will expand by some 1.5% this year in constant dollars.
- Increased competition from improved transportation creates both opportunities and challenges. The Government moved to improve competitiveness in the provincial retail sector by exempting clothing and footwear from sales tax from November 24, 1997 to September 26, 1998, as a pilot effort, to encourage off Islanders to travel to the Island to shop.
- Government operations at all levels are a significant part of the PEI economy. The 1998 Federal Budget incorporates continuing restraint in spending both on direct federal operations as well as transfers to the provinces. Reductions in federal transfers to the Province are discussed in Budget Paper B. Thus there is little potential for economic stimulus from increased expenditures by either level of government. Recently Revenue Canada announced plans to reduce GST processing activity at the Summerside processing facility, coupled with a move to income tax processing, and increased reliance on seasonal help. Government current expenditures in Canada have declined from 23.6% of Gross Domestic Product in 1992 to 20.4% in 1997.

**Summary Statistics**  
**Prince Edward Island Economy**

	1992	1993	1994	1995	1996	1997
Population	131,357	132,832	134,191	135,297	136,634	137,147
Personal Income per Capita ( \$ )	17,258	17,880	17,733	18,353	18,708	n.a.
As a % of Canadian Personal Income	79.2%	81.7%	80.4%	81.5%	82.5%	n.a.
Employment	54,100	54,400	56,100	58,700	60,100	60,500
Unemployment Rate	17.9%	18.1%	17.2%	14.7%	14.5%	14.9%
<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>
CPI - Charlottetown, Summerside	0.8%	1.9%	-0.2%	1.6%	1.8%	1.2%
<i>CPI - 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>
Retail Trade ( \$ m )	798.4	845.9	867.6	910.2	948.0	1,023.5
New Motor Vehicle Sales (units)	4,217	4,449	4,764	4,223	4,120	4,717
Farm Cash Receipts ( \$ m )	226.9	238.5	308.1	311.3	291.4	273.3
Potato Receipts ( \$ m )	72.8	98.0	163.7	149.6	138.0	125.3
Lobster Landings ( \$ m )	57.8	50.7	64.2	78.4	61.7	73.1
Lobster Landings ( lbs - million )	19.5	19.4	18.6	19.3	18.0	17.8
Housing Starts	644	645	699	422	554	470
Investment ( \$ m )	390.4	411.6	483.1	518.8	493.6	489.9
Manufacturing Shipments ( \$ m )	501.4	510.8	540.0	704.2	747.5	881.4
GDP at Market Prices ( \$ m )	2,184	2,325	2,381	2,506	2,648	2,699 <sup>e</sup>

e - Prince Edward Island Provincial Treasury estimate

n.a. - not available