BC STATS

Ministry of Finance and Corporate Relations

BRITISH COLUMBIA 2000 Marking The Millennium

Contact: Data Services
Tel: (250) 387-0325
Release: December 29, 1999
Issue: 99-12

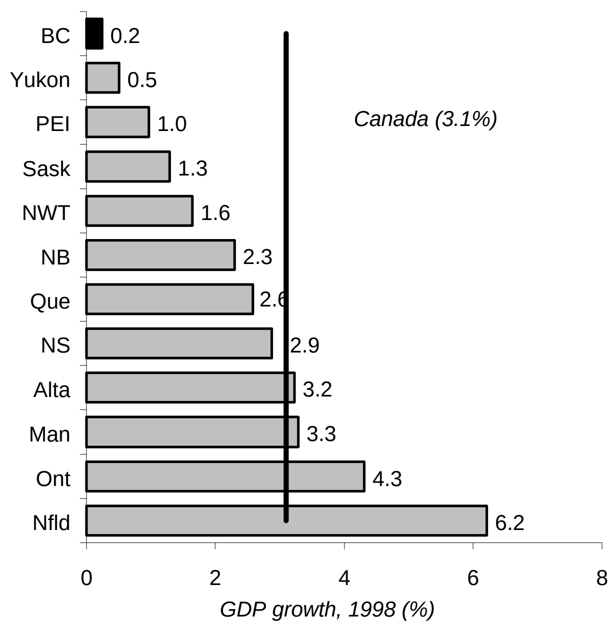
Business Indicators ◆ December 1999

BC's economic performance in the 1990s

BC's economy stalled, but did not shrink, in 1998

Data recently released by Statistics Canada suggests that BC's economy stalled in 1998, with real[1] gross domestic product (GDP) remaining virtually unchanged (+0.2%) from the previous year. The lack of economic growth came as no surprise, as most economists believed that BC was in a recession. Forecasters had predicted declines of as much as one percent for 1998. The fact that the economy actually expanded marginally was better news than had been anticipated.

For the first time since the early 1980s, the province trailed behind every other region of Canada in 1998

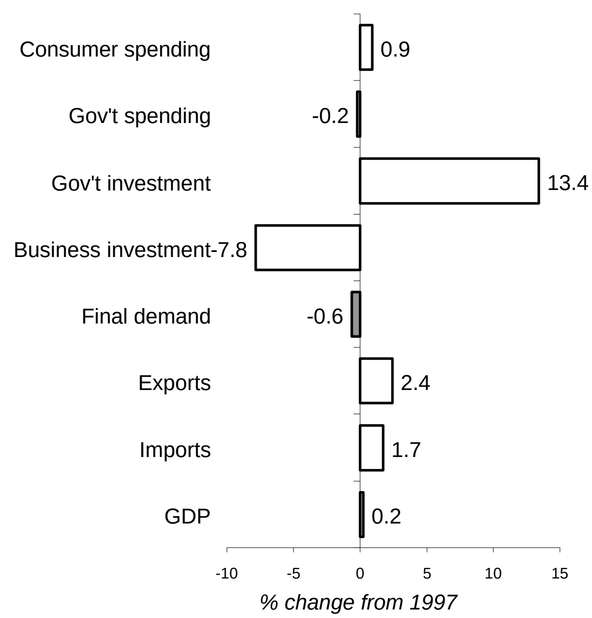


Despite the better-than-expected performance, the province slipped to last place among the Canadian regions for the first time since the early 1980s. Canada's economy grew 3.1% in 1998, led by a 6.2% expansion in Newfoundland, which is beginning to reap the benefits of Hibernia offshore oil production. Ontario's strong manufacturing sector fuelled its economic expansion (+4.3%) in 1998. Manitoba (+3.3%) and Alberta (+3.2%) were the only other regions to experience above-average growth in 1998.

Weak domestic demand, particularly in the business sector, was the main reason for the lack of growth

British Columbia's anaemic economic performance in 1998 was largely attributable to a decline in business sector investment. Overall, business spending on structures and equipment was down

Business investment fell, offsetting increases in consumer spending and government investment



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[1] All of the figures quoted in this article are in constant (1992) dollars, which means that they have been adjusted to remove the effects of inflation (i.e., they are expressed in 1992 prices).

7.8%, marking the third time in the last four years that it has fallen. Saskatchewan (-7.9%), Yukon (-1.1%) and Newfoundland (-0.5%) were the only other regions where businesses cut back on their investment spending during 1998. However, most parts of the country saw investment increase significantly less in 1998 than it had in the previous year. Nationally, business spending on structures and equipment rose only 3.4% after growing 16.9% in 1997.

In BC, the residential sector, which has struggled during the last few years, shrank 10.3%, while spending on non-residential structures fell even more (-12.4%). At the same time, purchases of machinery and equipment dropped to 1.0% below the 1997 level.

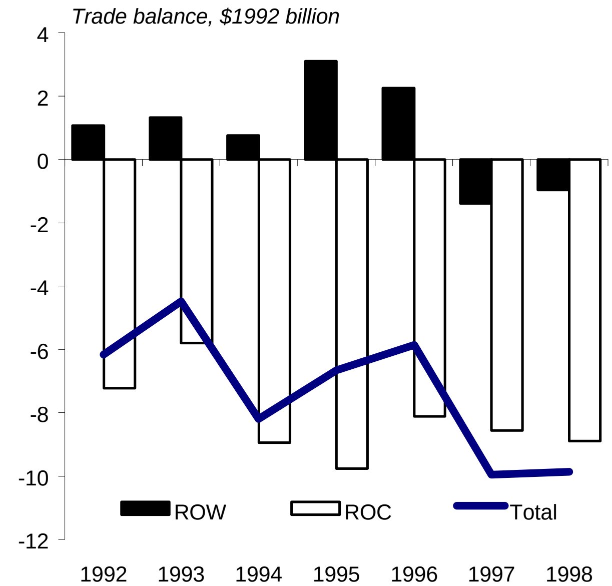
Offsetting the decline in business investment was a 0.9% increase in consumer purchases of goods and services. This was considerably weaker than the 4.2% gain seen in 1997, and represented the smallest rise in consumer spending since the beginning of the decade. Consumer expenditures on services were up 1.5% and spending on non-durable (+0.6%) and semi-durable (+0.3%) goods also increased. However, purchases of consumer durables, a key indicator of consumer confidence, fell 0.9% in 1998.

Investment by the government sector provided a boost to the economy. Total spending on structures and equipment was up 13.4%, as federal, provincial and local government investment in structures (+13.6%) and machinery and equipment (+12.8%) increased substantially. However, governments kept a tighter rein on wages, salaries and other operating costs, which fell 0.2%.

An improvement in the trade deficit helped offset the decline in final demand

The decline in business investment was strong enough to offset the increased spending by the personal and government sectors. Final domestic demand decreased 0.6% in 1998, indicating that BC's weak economic performance in 1998 was due to factors within, rather than outside, the province. The marginal increase (+0.2%) in GDP occurred because BC's trade deficit with other countries (ROW) and other provinces (ROC) improved slightly (from -$10.0 billion to -$9.9 billion) in 1998. This, together with a $264 million increase in the value of inventories held by businesses, brought GDP growth up to 0.2% for the year.

The province's overall trade deficit improved slightly in 1998, but remains much larger than in the past



The modest improvement in BC's trade deficit came as imports of goods and services increased less (+1.7%) than the province's total exports (+2.4%). BC's trade deficit with the rest of Canada worsened slightly in 1998 (from -$8.6 billion to -$8.9 billion), but this was offset by an improvement (from -$1.4 billion to -$1.0 billion) in the international trade deficit.

Historically, an overall trade surplus (goods and services) with other countries has partly counterbalanced BC's deficit with the rest of Canada. But in the last two years the province has imported more goods from other countries than it has exported to them. A surplus in foreign trade in services has not been large enough to compensate for the deficit on the goods side.

The province benefits from its location as the Pacific gateway to Canada

The low value of the Canadian dollar, together with a booming US economy, may have boosted the volume of exports from BC during 1998. Despite the dampening effect of the Asian crisis on foreign demand for BC products, the province's total international exports were up 2.0% in 1998. The value of goods shipped to other countries rose 1.4%, while service exports increased at more than double (+3.7%) that rate.

British Columbia's location as the Pacific gateway to Canada has cushioned the province from some of the effects of the collapse in Asian markets. Vancouver's port is the busiest in Canada, shipping goods produced in BC and other parts of Canada to international destinations, and serving as the point of entry for many commodities coming into the country from the Far East and the western seaboard of the United States.

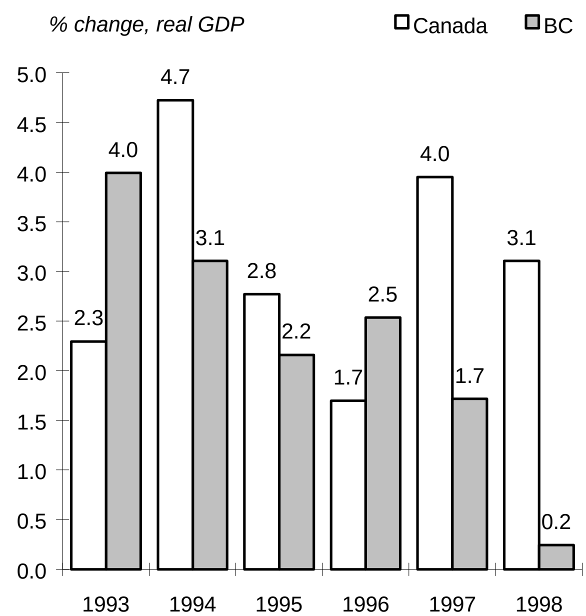
BC firms provide transportation, wholesaling and other services to foreign purchasers of Canadian products, and to foreign producers of goods entering Canada via BC. This trade in services also occurs with other provinces. For example, when prairie grain is shipped from BC ports, the economic activity associated with bringing the grain from the BC/Alberta border to the point at which it leaves the country is attributed to BC because it takes place within the province's boundaries. In the same way, BC businesses benefit when other provinces import goods that enter Canada via the west coast. This means that, to a certain extent, the province is able to ride on the coat tails of increased economic activity in the rest of Canada.

Service exports, especially transportation, wholesaling and financial services, are BC's most important inter-provincial exports. After forest products, they are the province's most important source of international export revenues. In 1998, international and inter-provincial service exports contributed $14.0 billion to BC's GDP, equivalent to more than half the value ($25.7 billion) of all goods exported to other countries and provinces. A 3.3% increase in service exports was one of the main reasons for the improvement in BC's trade deficit last year. However, both international (+1.4%) and inter-provincial (+4.3%) exports of goods also expanded in 1998.

BC's economic situation during the 1990s has been quite different from that in the rest of the country

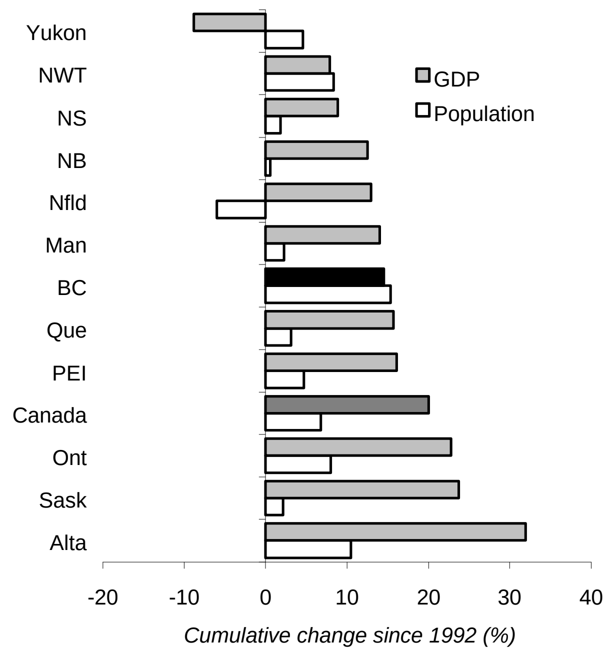
BC's economy has not performed well during most of the 1990s. GDP growth has been below the Canadian average in all but two years since 1993, and compared to Ontario and Alberta (the other "have" provinces), British Columbia's record has been somewhat dismal. During the period since 1992, Alberta's economy has expanded by nearly a third (32%), while Ontario's has grown 23%. Saskatchewan (24%) has also outperformed the Canadian average (20%). In BC, the economy has grown only 15% during this period, a rate comparable to that seen in most parts of Atlantic Canada.

Economic growth in BC has been below the Canadian average during most of the 1990s



The slow GDP growth has occurred despite the fact that the population has been expanding at a fast clip. In fact, until 1998, British Columbia had the fastest-growing population in the country. Its population increased 15% between 1992 and 1998–more than double the national average (+7%), and nearly fifty percent more than in second-place Alberta, where the population has increased by 11% since 1992.

BC's population has grown more rapidly than its economy since 1992



BC is unique among the provinces in that the size of its economy has not grown as much as its population since the beginning of the decade. Only the territories have seen a similar phenomenon. In the rest of the country, economic growth has been well in excess of population gains.

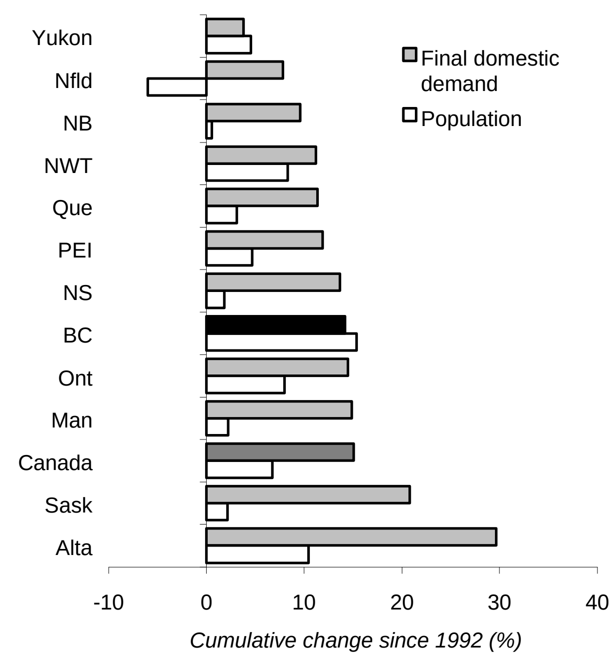
This suggests that the influx of people into the province since 1992 has not stimulated economic growth to the extent that might have been expected. Population growth is often viewed as a driving factor in GDP gains, but this does not seem to be the case in BC. The new arrivals in the province have not boosted the demand for goods and services to the same extent that they have in other parts of the country. Or have they?

One way to answer this question is to look at what's happened to final domestic demand–total spending on goods and services by residents of the province. This includes consumer purchases of goods and services produced in the region or imported from other provinces and countries. Also included is investment in structures and equipment, plus current expenditures made by federal, provincial and local governments.

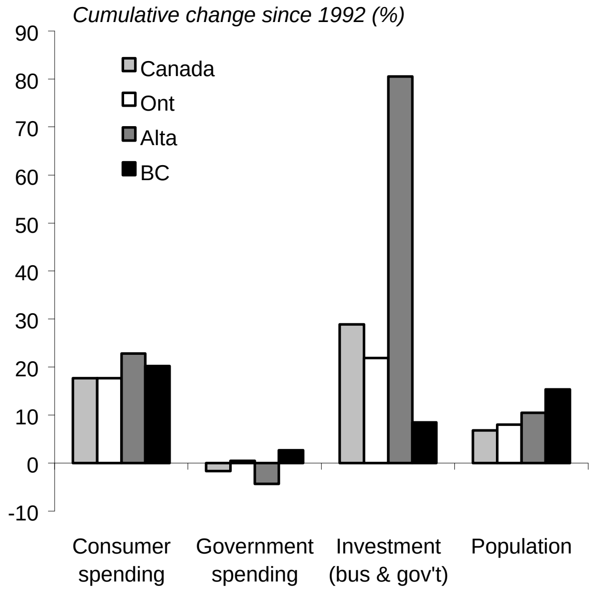
Like GDP, final domestic demand has not increased as much as the population, an experience that is contrary to that in every other part of the country. However, the cumulative growth in the demand for goods and services in BC (+14% since 1992) is only marginally less than the Canadian average of 15%. This suggests two conclusions: first, that BC's lower-than average GDP growth is largely due to its external trade; and second, that while the influx of people into the province has undoubtedly boosted the demand for goods and services in the province, the effect has been weaker than in the rest of the country. The question then becomes, what is the source of this weakness?

Looking at the components of final demand, some interesting trends emerge. First, we see that personal expenditures in the province have increased commensurately with population growth. Since 1992, consumer spending in the province has

Final domestic demand in the province has also failed to keep pace with population growth



Consumer spending has increased faster than the population, but investment growth in BC has been weak



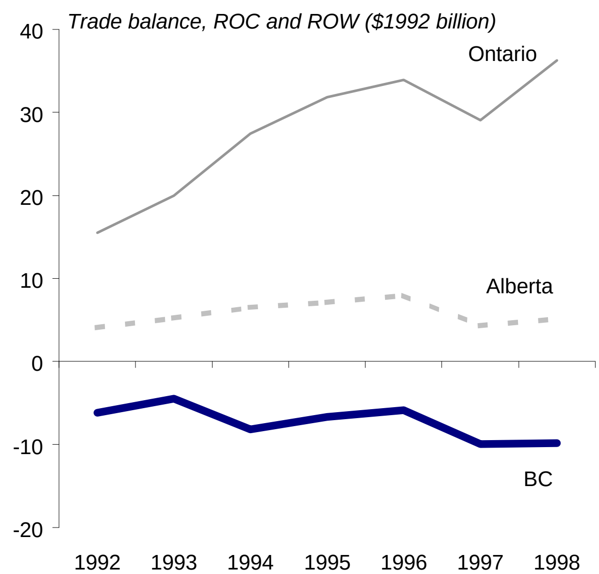
risen more (+20%) than anywhere else in Canada except Alberta (+23%). The average increase for all of Canada was 18% over this period. At the same time, federal, provincial and local government spending on goods and services (+3%) has increased in BC but has decreased (-2%) at the national level.

It is in the area of investment that BC has fallen behind the rest of Canada. Investment growth (+8%) in the province has been weaker than in any other region except Yukon, where it has declined 17% since 1992. Nationally, business and government spending on fixed capital has risen 29% since 1992. Alberta (+81%) and Ontario (+22%) have seen significant increases in spending on plant and equipment during the 1990s. This has contributed to the strength of the economies of Canada's two other "have" provinces.

A combination of factors has been responsible for BC's weak investment growth during the 1990s. Probably the most important is the collapse of the housing market. Despite an influx of people from other provinces and from the rest of the world, the value of residential construction in the province remains below 1992 levels. This suggests that, while in-migration has boosted the demand for goods and services in BC, it hasn't generated a similar stimulus in the housing market. The weakness in the residential construction sector is reflected in the fact that the cost of new housing in the province has been declining steadily since 1994.

BC has also seen below-average increases in business investment in structures (+18%, compared to 32% nationally) and machinery (+36%, compared to 67%). Government spending on structures (+2%, compared to a 15% decline at the national level) and equipment (+45%, compared to +40%) has risen more than in other parts of the country, but this has only partly mitigated the effect of lower spending by the business sector.

BC is the only "have" province that has consistently had an overall trade deficit

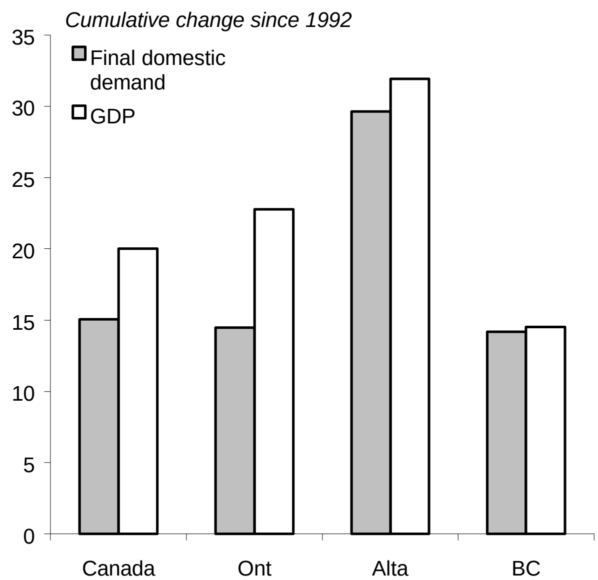


Slower than average growth in final demand is only part of the explanation for BC's poor showing compared to Alberta and Ontario. Both of these provinces export more goods and services to other countries and provinces than they import from them. They are the only regions that have overall trade surpluses. Alberta's surplus is mainly due to trade–mostly in energy products–with other countries. Ontario sells more goods and services to other provinces, and to other countries, than it buys from them. It has had an international trade surplus in every year since 1993. The reverse is true in BC–and in the rest of Canada–where the value of imports exceeds total exports.

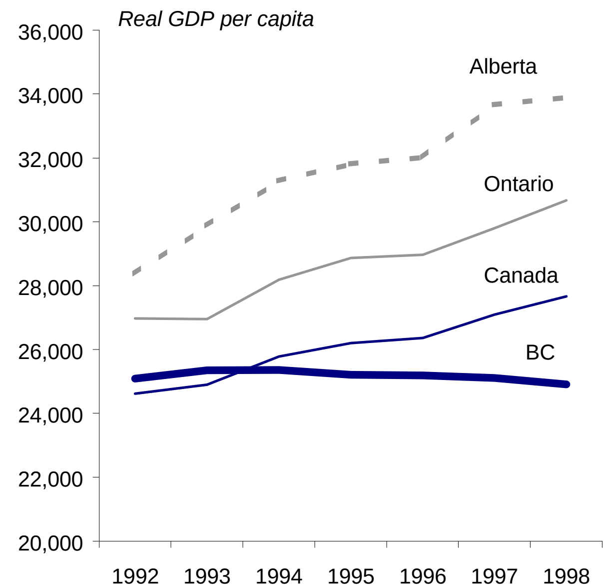
During the 1990s, Ontario's large surplus has grown quite significantly (from $15.5 billion in 1992 to $36.2 billion in 1998). Alberta has seen some ups and downs, but its trade surplus was $5.1 billion in 1998, just over a billion dollars more than in 1992 ($4.1 billion).

At the same time, British Columbia's trade deficit has worsened, going from -$6.1 billion to -$9.9 billion. This reflects, in part, the demand made by a growing population for goods and services produced outside the province. In other words, purchases of goods and services produced outside the province do not necessarily foster GDP growth.

Inventory changes and the external sector provide more of a boost to the economies of Ontario and Alberta than they do to BC's



On a per capita basis, GDP in the province has declined since 1992



Taken together, the cumulative effects of below-average growth in final demand (largely due to weak business investment), and a trade deficit that has increased by 60% since 1992 have dampened BC's overall GDP growth. These factors, plus a rapidly growing population, have contributed greatly to the decline in per capita GDP during the 1990s.

A turnaround in business investment could help British Columbia's economy regain some of the ground that it has lost, thereby boosting per capita GDP. However, the province will remain vulnerable to the vagaries of external markets for products such as lumber unless it is able to develop a more diversified manufacturing base, or to further exploit its potential to supply specialized services to other countries and to the rest of Canada.