



International tourist traffic rebuilding

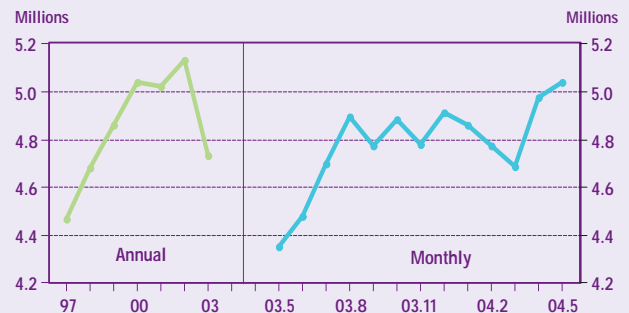
Tourist traffic from other countries is slowly rebuilding after the shock-induced plunge in 2003. Total tourist entries to B.C. climbed to 420,200 persons seasonally adjusted in May, up over 1% from April and the highest level since January 2003. A return to more normal conditions, along with improved global economic growth, has seen the return of tourists to B.C. At the depth of the SARS, Gulf WAR II, and BSE situations last year, tourist entries plummeted to 362,700 persons. For the year as a whole, tourist visitor fell almost 8%.

A stronger rebound is coming from Overseas tourists than from U.S. tourists. Overseas tourist traffic is up over 20% from last year's low while U.S. traffic is up about 2%. Part of the reason is that Overseas traffic dropped by considerably more than U.S. traffic and is a position to make up more ground. However, other reasons such as exchange rate movements and possibly security concerns are also at play. Overseas tourist levels are now higher than before 2003 while U.S. traffic has not fully recovered to pre-2003 levels.

Tourism is quite exposed to exchange rate movements and the U.S.-Canada exchange appreciation since early 2002 is likely having some impact. Compared to the near 20% appreciation against the U.S. dollar, the

International tourist traffic slowly rising

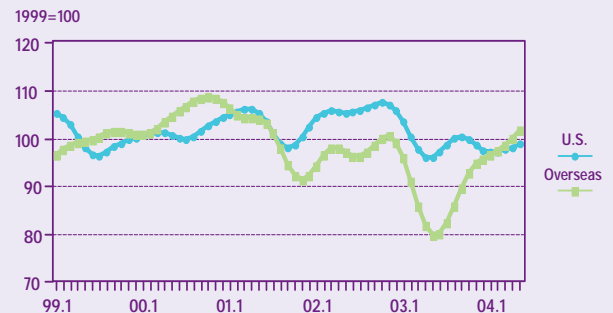
International Tourists to B.C.



Source: Statistics Canada, CUCBC. Monthly data - seasonally adjusted at annual rate.

Larger rebound in non-U.S. tourist traffic

International Tourist Entries to B.C.



Source: Statistics Canada, CUCBC. Note: Based on trend-cycle data. Latest: May 2004

Canadian dollar has depreciated about 10% against the Euro and is roughly unchanged against the Japanese Yen. A stronger U.S. economy provides some offset to the unfavourable currency move.

Based on current trends, total tourist entries to B.C. will post about a 5% to 7% gain this year but will not exceed 2002's high mark. That will probably have to wait until next year.

U.S. housing starts drop

Residential construction activity in the U.S. dropped sharply in June increasing the probability that the high for this cycle has been set. Seasonally adjusted housing starts fell to 1.8 million units annualized down from 1.97 million in May and from the high of 2.067 million in December 2003. Single-family construction dropped the most. June's result conforms to other indicators pointing to moderation in single-family housing activity as mortgage rates have increased in the past three months.

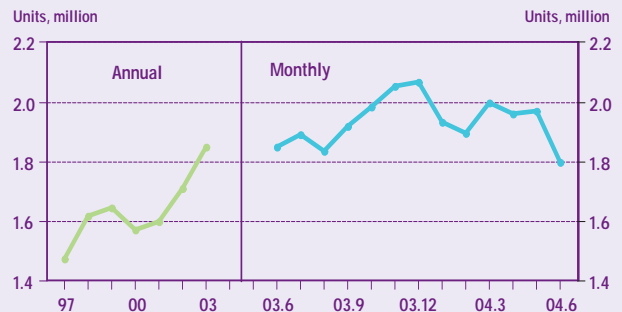
With mortgage rates expected to move up some more in the coming months, demand will slow and builders will curtail production to minimize unwanted inventory. Longer term rates, such as the 10 year government bond yield, are forecast to increase another 50 to 75 basis points bringing it to about 5.25% or 5.50% by the end of 2005. It was at less than 4% earlier this year. Stronger job and income growth in the U.S. provides some offset to higher mortgage rates but higher rates will override that offset this time since pent-up demand is fairly low after a multi-year housing expansion.

Forecasts of 2005 U.S. housing starts are universally lower than 2004's expected level of 1.86 million units according to the consensus forecast. Not one of the more than three dozen forecasters canvassed sees 2005 housing starts higher than in 2004. The consensus forecast average is 1.7 million units for 2005.

Fewer U.S. housing starts have negative implications for B.C.'s lumber industry with likely lower export volumes and lower prices. The expected 10% decline in housing starts is not large by historical standards but it is sufficient to change the demand-supply balance in lumber and other housing input markets. The dollar value of B.C. lumber exports to the U.S. is up almost 30% so far this year, and should the consensus forecast materialize, exports will decline in tandem.

U.S. housing starts past peak?

U.S. Housing Starts



Source: U.S. Dept. of Commerce. Monthly data - seasonally adjusted at annual rate.