



# Weekly economic Briefing

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## B.C. job growth stalls

The number of people employed in British Columbia dropped by 2,900 in October, after adjusting for seasonal effects. Employment growth has been stalled since September, after rising strongly from January to August. Adjusted for irregular influences, the trend level of employment increased by 6,600 workers last month, a 0.3% increase from September.

The provincial unemployment rate in October was 8.3% of the labour force on a seasonally adjusted basis, up from 8.1% in September. The unemployment rate rose because the labour force grew by 11,700 (seasonally adjusted), while employment decreased slightly. After adjusting for irregular influences, the trend rate of unemployment was 8.1%, down from 8.2% in September. B.C.'s unemployment rate is on an improving, downward trend, although it has increased slightly over the past two months as employment growth stalled.

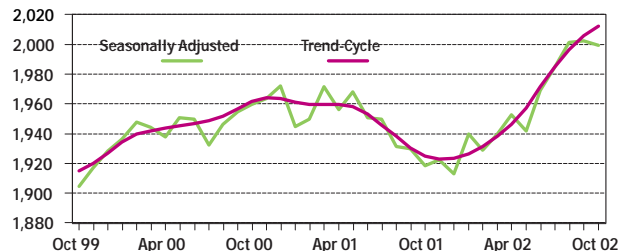
October's job losses were seen in the Mainland-Southwest region (-5,400), North Coast-Nechako (-1,600), Kootenay (-1,500) and Northeast (-700). Regions showing modest increases in employment were Vancouver Island (+1,100), Thompson-Okanagan (+700) and the Cariboo (+600).

Job losses in October occurred mainly in professional, scientific and technical services (-7,800), educational services (-5,000) and information, culture and recreation (-2,500). Employment gains were seen mainly in health care and social assistance (+5,800), the small and varied service industries (+5,100), construction (+5,000) and finance, insurance, real estate and leasing (+4,500).

### Employment growth stalls

#### B.C. Employment

Employed Persons (1,000's)

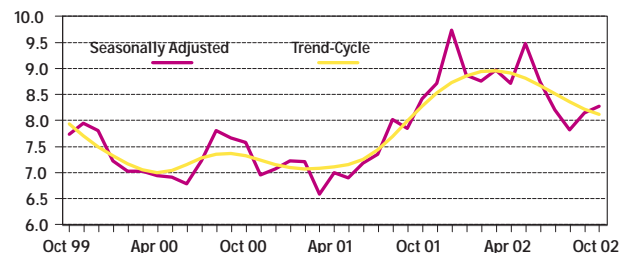


Source: Statistics Canada and CUCBC Economics.

### Unemployment rate edges up

#### B.C. Unemployment Rate

Percent of Labour Force



Source: Statistics Canada and CUCBC Economics.

Full-time employees bore the brunt of October's job losses (-18,300), while part-time employment increased (+15,400). The losses were split among private-sector workers (-6,800) and public-sector workers (-4,600). Employment gains in October were entirely among the self-employed (+8,500).

CUCBC Economics is forecasting that annual average employment in B.C. will increase by 1.2% this year and another 1.3% in 2003. The province-wide unemployment rate is forecast to average 8.6% this year and 8.2% in 2003.

## Non-residential building permits up

Higher building permits for commercial structures raised the total value of non-residential permits in B.C. to \$150 million in September from \$126 million in August. The trend in non-residential building intentions is toward slow growth, as increases in commercial and industrial construction are being largely offset by decreases in institutional and government building.

The trend rate of growth in non-residential building permits in September was 0.6% (+\$756,000) per month, after adjusting for seasonal and irregular influences. Commercial building permits increased at a trend rate of 1% (+\$940,000) per month, while the rate for industrial building permits rose to 2.8% (+\$480,000) per month. In contrast, government and institutional building permits fell at a trend rate of 2.5% (-\$750,000) per month. Trends in commercial building permits are toward more office, warehouse and restaurant construction and away from trade, service and hotel construction.

While non-residential building permits have dropped substantially in 2002 compared to 2001, CUCBC Economics is forecasting an increase of \$115 million (+6.8%) next year. Forecasts are for commercial building permits to rise \$100 million (+9.5%) in 2003 and for industrial permits to grow by \$20 million (+8.7%). Government building permits are forecast to fall by \$5 million (-1.2%) in 2003 after dropping \$327 million (-45%) in 2002. This year's drop in government building can be traced to B.C. government cuts in capital spending.

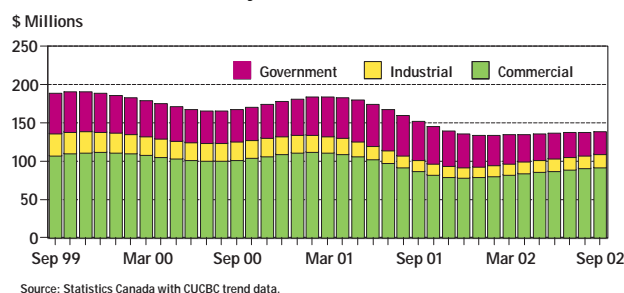
## Housing starts keep rising

Housing starts in urban areas of B.C. with populations of 10,000 or more totalled 1,916 units in October, a gain of 25% from 1,529 units in October 2001. Year-to-date housing starts in urban B.C. amounted to 16,769 units to the end of October, up 26.4% from 13,270 units in the same period of 2001. Year-to-date housing starts consist of 8,260 single-detached units, up 50%, and 8,509 multi-family units, up 9.5%. Every urban area in B.C. has recorded higher year-to-date housing starts compared with last year.

In metropolitan Vancouver, October's housing

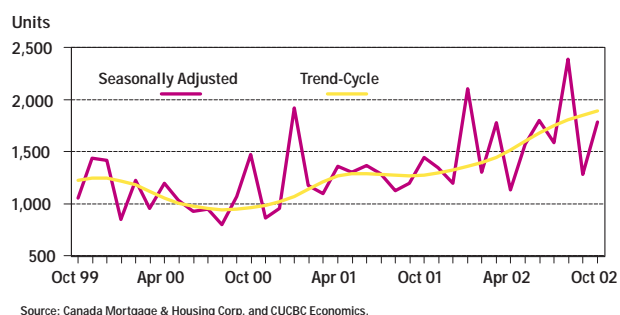
## Commercial and industrial building up

### Non-Residential Building Permits British Columbia, Monthly



## Housing starts continue to rise

### Housing Starts: B.C. Urban Areas



starts totalled 919 units, up 17% from October 2001. Year-to-date starts in metro Vancouver amount to 10,772 units, up 15% from the same period in 2001. Multi-family units are up 2% to 6,567 units, year-to-date, while single-detached starts are up 43% to 4,205 units. Housing starts are higher in every municipality in the metro area, year-to-date, except for Vancouver City, Port Coquitlam, North Vancouver City, West Vancouver and Pitt Meadows.

Housing and related consumer spending continue to be the largest contributor to economic growth in B.C. Low interest rates, immigration and property price inflation are some of the factors driving strong growth in housing sales and construction. CUCBC Economics is forecasting total housing starts, including those in non-urban areas, of 22,500 units this year and 25,400 units in 2003, up from 17,234 units in 2001.

## Revisions show B.C. economy dipped into recession

The latest Provincial Economic Accounts released by Statistics Canada show that B.C.'s economy dipped into a small recession last year, despite previous calculations of modest growth for the year. Revised Gross Domestic Product (GDP) estimates put inflation-adjusted or real growth at -0.2% in 2001, instead of the 0.9% gain originally estimated. A large deterioration in the province's exports accounts for the drop, since domestic demand, which excludes the trade sector, grew at a real rate of 3.8%, up from 3.6% in 2000.

On this occasion, Statistics Canada's took its revisions all the way back to 1981, because it is introducing a new price deflator. While there was little change in most years, some exceptions stand out. The Expo year of 1986 was downgraded to 0.2% from 1.5%, while 1992 was increased to 2.6% from 2.1%, and 1993 rose to 4.5% from 4.1%.

For the 1981 to 2001 period, average annual real GDP growth was poorer than previously estimated, at 2.3% versus 2.5%. Looked at another way, real GDP grew 55.4% from 1981 to 2001, instead of the 63.4% in the previous estimates. Total real GDP was revised downward in 13 of those years.

## Fed move surprises

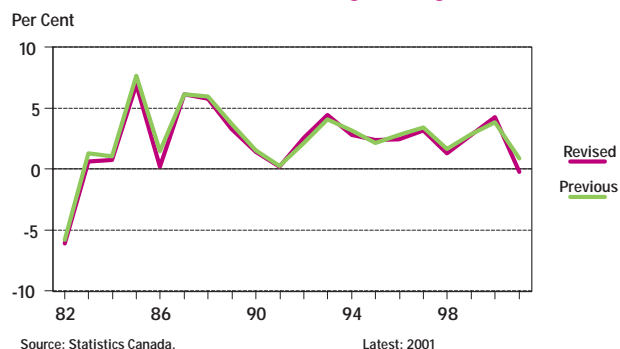
A 'soft spot' in economic growth and a low inflation rate prompted the U.S. Federal Reserve to aggressively cut its key lending rate by 50 basis points (bps), exceeding the expectations of most pundits. The Fed's surprising move is a statement that the economy is weaker than generally thought and a recession was imminent without the cut.

### *So how weak is the economy and does it justify the cut?*

Job growth, the single most important current indicator, was down 5,000 in October – a minuscule amount in a base of over 130 million – and September was down 13,000, but revised upward from the initially estimated 43,000 drop, and August was increased to 107,000. Manufacturing was down in August and September and the lower Institute of Supply Management (ISM) manufacturing index for October very likely means another decline, which would mark three consecutive months. The ISM index for the services sector – about 75% of the total economy – pointed to expansion in October, but at a slower pace.

## First recession in 20 years

### B.C. Real GDP, Annual Percentage Change



Source: Statistics Canada.

Latest: 2001

Consumer confidence fell sharply in October, raising fears that the underpinning of this economic recovery is about to falter, and this was likely the most influential indicator for the Fed. Auto sales during October fell to their lowest level since April 1998. The Fed cited heightened geopolitical risks as contributing to greater uncertainty, which is inhibiting spending, production, and employment. An economic growth soft spot is certainly present, but is it sufficient to warrant using almost 30% of your ammo? That's what 50 basis points amounts to for the Fed, with its key rate now just 1.25%.

Stock prices, a frequent mover of consumer expectations and a component of the Leading Economic Index (which declined in the two months ending September), had their best October performance in years. Could this foretell better times ahead? The MBAA index of mortgage applications rose in the latest week, as mortgage rates turned downward and remained at near historical highs, indicating there is still some oomph left in consumer spending. Investment spending on IT equipment and software was up for the third consecutive quarter and economy-wide GDP growth came in at 3.1% in the third quarter. But this was obviously not enough for the Fed.

Lower rates will certainly help keep the housing sector contributing to economic growth, but this will have less effect on auto sales since manufacturers' incentives were already quite generous. Business investment spending is a function not only of the cost of capital but also of profitability, which requires less excess capacity among other things, and this latest cut will not do much to ignite investment spending in the near term.

This move was more about perceptions and expectations than anything else. The Fed felt it had to make a statement that it was concerned and serious about avoiding deflation and a recession. Deflation is the worst situation for a central bank – and an economy – because real interest rates are high even when the nominal interest rate is zero, and high real interest rates discourage spending. Deflation also works to discourage spending because it then becomes rational to wait for lower prices before spending. Deflation puts a central bank on the sidelines. Had the same conditions existed, but with an inflation rate further away from zero, say 2% or more, the Fed might not have cut, since the economic data were not that bad.

Why save your ammo and not take action when there is at least some risk of recession and deflation? Rate cuts can always be retracted, and now it is possible that Fed tightening will begin sooner. An oft-quoted Fed report on Japan's monetary policy performance concluded that the Bank of Japan did not act soon enough and hence contributed to the current deflation and recession. The Fed did not want to repeat that mistake.

More cuts cannot be ruled out if the economy does not shift to firmer growth. The Fed has clearly shown that it is prepared to use more of its scarce and dwindling ammo (only 125 basis points are left to cut). The Fed's neutral bias or balanced risk assessment of near-term growth almost certainly eliminates a cut at its December 5 meeting, but thereafter it is an open matter, although this Fed watcher expects no further cuts.

The Bank of Canada now finds itself under some pressure to either follow the Fed or to manage expectations about not cutting rates at its next meeting, on December 3. Depending on data that comes out between now and then, the Bank will have to make a critical decision. There is every indication that job growth will slow but still hover around 2%, and that's not enough reason to cut rates.