BMO Blue Book

May 2013

BMO

BMO Bank of Montreal
BMO Capital Markets

Canada

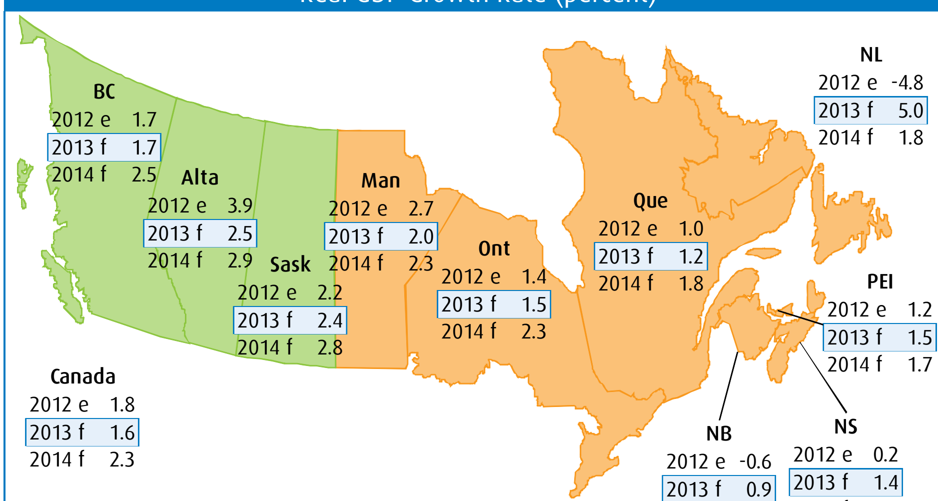
ECONOMICS
Douglas Porter, CFA,
Chief Economist &
Managing Director

Striking the Right Balance

The Canadian economy continues to grow at a modest pace, as a slowing housing market, sluggish consumer spending and a moderate dose of fiscal restraint weigh on activity. Economic performance continues to vary by region, with Western Canada still outperforming the rest of Canada, albeit by a narrower gap than seen in recent years. On the fiscal front, the FY13/14 budgets are now in hand, with half of the provinces pushing back the timing of their return to balance. Provincial governments have walked a fine line between continuing to trim deficits, while not digging in too deeply in a soft growth environment.

While certainly not without challenges, the resource sector continues to fuel above-average growth in Western Canada. Alberta's economy is expected to expand 2.5% this year, well above the 1.6% national rate, but a clear downshift from average growth of more than 4% over the prior two years. Growth has been tempered by a lack of pipeline capacity (and still-uncertain development prospects) and, in turn, a deep discount for Canadian heavy oil prices relative to WTI, which has narrowed recently. British Columbia, with its softening housing market, is expected to hold steady at 1.7% this year, while Saskatchewan and Manitoba expand in the low-2% range, narrowing the gap between the West and the rest of Canada by about half from 2012.

PROVINCIAL GDP
Real GDP Growth Rate (percent)



Source: [2013-14] BMO Capital Markets Forecasts

Central Canada continues to face familiar challenges, including fiscal restraint and an elevated Canadian dollar. As a result, Ontario's economy will likely remain sluggish at a 1.5% pace this year, while Quebec's should pick up to a still-soft 1.2%—recall that Quebec's 2012 performance was marred by political/policy uncertainty, student protests and labour disruptions. The good news is that the U.S. economy is poised to return to sustained 3%-plus growth during the second half of the year, which should bolster growth as we move into 2014.

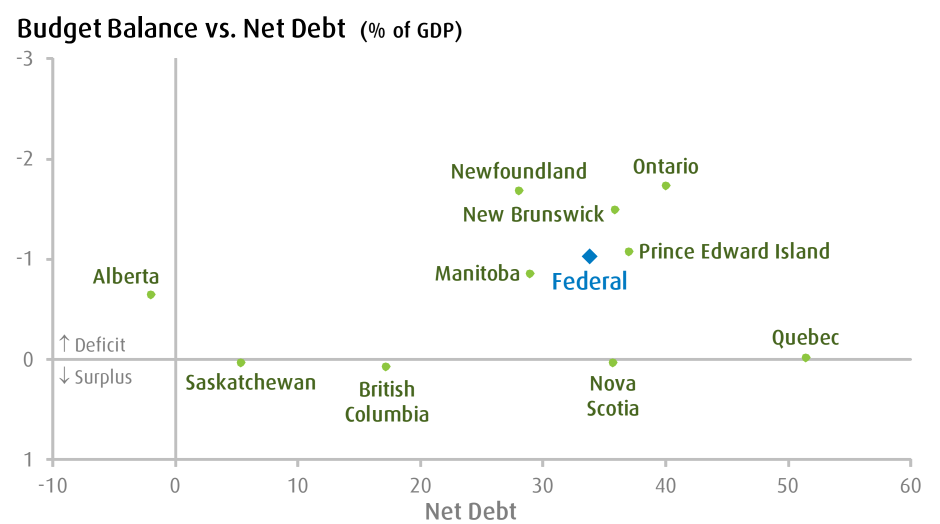
Atlantic Canada's outlook is mixed, depending on the degree of fiscal restraint hitting each province and the timing of major capital spending projects. New Brunswick, for example, will see about $168 million in net tax hikes this fiscal year (0.5% of GDP) in order to set the budget on track for balance, pinning growth below 1%. On the flip side, Newfoundland & Labrador will likely see real GDP jump 5% as offshore oil production rebounds and construction of the massive Hebron project ramps up.

The 2013 provincial budget season is now complete, and overall, the provinces have tiptoed down the path of fiscal restraint. The majority put through some combination of net revenue-raising measures to keep deficits in check, including higher corporate tax rates (B.C. and New Brunswick) or cancelled reductions (Saskatchewan); higher personal income taxes, particularly at the upper end (B.C., Quebec, and New Brunswick); and a sales tax increase in Manitoba. The net fiscal impact is mild at just over $1 billion for FY13/14 (less than 0.1% of GDP), with harder hits of around 0.5% of GDP in Manitoba and New Brunswick. Combined, revenue growth is still pegged at a modest 3.1% in FY13/14, reflecting the soft economic backdrop.

Meantime, total program spending growth across the provinces is 1.9%—that's down from 2.2% last year and a modest contraction in real per-capita terms. While not overly austere, we can't expect provincial government spending to add to growth this year.

The end result of moderate revenue-raising measures and tempered spending increases is that fully half of Canada's 10 provinces have pushed back the timing in which deficits will be eliminated—Alberta, Manitoba, New Brunswick, PEI and Newfoundland & Labrador. That said, deficits will still weigh in at less than 2% of GDP across the board this fiscal year, and less than 1% of GDP in the majority of provinces. The overriding theme this budget season might well be that the provinces are managing to strike a fine balance; whether by design or coincidence, the provinces have found a reasonable trade-off between austerity and stimulus.

PROVINCIAL FISCAL LANDSCAPE
(FY13/14, as of latest update)



COMMERCIAL BANKING

Steve Murphy,
Senior Vice President,
Commercial Banking

BMO's commercial customers across Canada are maintaining their cautious approach to the economy. But even in a period of more restrained growth there are causes for optimism in many locations and sectors.

The resource sector in Western Canada continues to lead the way, leading to population increases in Saskatchewan and major new work projects in Alberta. The ancillary benefits are significant, with increasing demand for all sorts of small companies—from manufacturers to skilled trades.

The agriculture sector has seen a great deal of success across the country, from dairy and poultry farmers in B.C., to expanding farms in the Prairies, to steady yields in central and eastern Canada. While world prices may start to fall, last year's success has generally put our farmers on a strong footing.

Companies in manufacturing, depending on their markets, are showing good signs of stability. By and large, those that cut costs and focused on productivity during the downturn are coming good. The auto sector in Ontario has stabilized, firms that support resource development in the West continue to get business, and niche manufacturers are finding new markets. Plus, manufacturers in Nova Scotia and across Atlantic Canada continue to gear up for decades of work related to the contract for Halifax Shipyard to build vessels for the Canadian Navy.

Still, caution is the order of the day given current growth prospects and the ongoing high Canadian dollar. But the potential is still there. The U.S. economy is starting to show real signs of strength, which in turn benefits companies that focus on exports. While caution can be understandable, the success of those companies that have invested in their operations should act as an example of what is possible. With the dollar still high and interest rates still low, the tools are in place for companies to make the investments that will improve their productivity—an investment that can provide impressive returns for years to come.

To help companies achieve such goals, BMO is open for business. We have a full array of services to help businesses become and stay successful, and we have a highly-skilled team of commercial bankers situated in communities across Canada. Our bankers stand ready to advise business owners on strategic spending and investment decisions that will help them boost productivity and expand into new markets, both at home and abroad. Our bankers are also armed with limits to make almost every lending decision locally.

British Columbia

ECONOMICS

Robert Kavcic,
Senior Economist

Economic growth remains muted in British Columbia, with real GDP likely to hold steady at 1.7% this year—that would mark the slowest pace since the downturn in 2009. Among the headwinds are a slowing domestic housing market and softer Asian export demand, though a resurgent U.S. housing market plus firmer momentum in China will likely support exports later in the year.

British Columbia's housing market is fully in correction mode, particularly in Vancouver and Victoria where buyers now have control of the market. Sales volumes across the province were down 19% y/y in the first quarter, and were running at just 70% of the 10-year average for that period of the year. With little snap back expected in the housing market, construction activity is expected to soften through 2014.

The external environment did not help much in 2012, with China's economy slowing and the U.S. embattled with fiscal uncertainty—exports fell 4.1% last year. Looking ahead, a strengthening housing market should lift U.S. economic growth, supporting exports, while growth in China looks to have bottomed. Note that British Columbia's forestry exports were up 11% y/y in February—about 40% of forestry-related exports go to the U.S., down from 65% a decade ago.

COMMERCIAL BANKING

Dean Kirkham,
Vice President, Commercial Banking, Greater Vancouver District

The current climate among businesses in B.C. is one of caution. With growth sluggish, a lull in Chinese demand and uncertainty regarding the political environment, we are seeing more businesses choosing to sit on the fence.

Among major commercial sectors, our agricultural clients represent a stand-out industry—particularly in the supply-managed areas of poultry, dairy and eggs. We are, however, beginning to hear concerns about the long-term future of supply management, with objections being raised by other countries during ongoing trade talks. The hope is that any changes that may result are still some time away.

On the natural resources side, we're seeing positive signs in the forestry industry. With U.S. housing starts trending up, we are hearing from our clients that they are securing more demand from south of the border and elsewhere. While the strong dollar is still a challenge with this export-intensive industry, the signs are good.

Among major commercial sectors, real estate has represented an ongoing concern throughout the province. Among our clients, home builders are seeing their work slow down. While all the evidence suggests the housing market is due for a soft landing, some won't be convinced until they see it.

For commercial owner-operators, the situation is different—there is still a good amount of real estate demand. We are seeing continued commercial space growth in virtually every market.

China continues to have a significant impact on the B.C. economy, both through trade and immigration. For instance, the recent uncertainty regarding Chinese growth and demand has contributed to the sluggish growth we are seeing here. We've also noted a lull in both Chinese immigration to B.C. and the amount of money coming in from that country. This may well be contributing to the softening of the real estate market, particularly in Vancouver. Still, the pace of demand remains reasonable, despite the notable slowing.

Alberta

ECONOMICS

Robert Kavcic,
Senior Economist

Economic momentum has softened in Alberta alongside tempered enthusiasm in the energy sector. After growing 3.9% in 2012, Alberta's economy is expected to expand a more modest 2.5% this year, sluggish by the standard set over the past decade. The main trigger for softer activity has been the wide differential received by Canadian producers of heavy oil relative to WTI prices. The differential topped $40/bbl at one point in late 2012, as higher oilsands output and surging U.S. Bakken production have filled limited pipeline capacity. The good news is that the discount has narrowed substantially so far in 2013, thanks to seasonal demand for bitumen, completed refinery maintenance and more pipeline capacity linking Cushing and the Gulf Coast. Despite the challenge, oil production in the province was still up a solid 16% y/y in 2012Q4.

Employment growth has cooled to just 1.7% y/y in March, down from a 2.6% pace for all of 2012. Resource-sector employment has slumped 10% since its record high in early 2012, while construction and trade have also softened. The labour market, however, remains tight with the jobless rate at 4.8% (2nd lowest in Canada) and average weekly earnings rising 6.1% y/y in 2013Q1. With in-migration strong, incomes rising and excess supply from the pre-recession boom worked down, the local housing market is outperforming much of the rest of Canada.

COMMERCIAL BANKING

Mike Darling,
District Vice President,
Commercial Banking,
Southern Alberta

Lynda Taylor,
District Vice President,
Commercial Banking,
Northern Alberta and
Northwest Territories

The recurring theme in Alberta remains a real sense of optimism, both for the major cities of Calgary and Edmonton and the province as a whole.

It comes as no surprise, given the demand for liquid gas, that the economy in Northwestern Alberta is being fuelled by expansion and growth in the oil and gas services sector and also the oil and gas construction industry. In particular, construction companies in the Northwest are bidding on new work emanating from major liquid gas players. Meanwhile, the continuing population influx into Fort McMurray and the Northeast has created demand for additional services and amenities.

In both Calgary and Edmonton, business is also largely centred on servicing the oil patch. Our clients there are expressing cautious optimism for 2013 with the hold on pipeline construction decisions hanging over the industry. But one client with specialized conventional drilling equipment noted that 2012 was his best year ever and even this year is looking good.

In the Calgary area, infrastructure and housing activity are robust. Home builders are especially upbeat given the continuing low interest rates and the low unemployment rate. Calgary's housing is close to fair value. Currently, price growth is picking up in Calgary and we see increases in the future to fall in line with incomes that are growing at a steady clip.

Of particular note are the prospects for Alberta's First Nations; Alberta is full of opportunities for First Nations with numerous Bands ready to enter into creative economic development opportunities. We're hearing more about green energy projects such as wind farms in Alberta. BMO has provided many innovative solutions to First Nations over the years, and we were proud to hear one Band Administrator said that BMO's approach to on on-reserve lending is helping them achieve their goals for their community.

Saskatchewan

ECONOMICS

Robert Kavcic,
Senior Economist

Saskatchewan remains among the top economic performers in Canada, although growth has softened somewhat. Real GDP is expected to grow 2.4% this year, up slightly from a 2.2% pace in 2012, with strong resource-sector activity helping to maintain above-average growth.

Oil production is now running at about 170,000 bpd, spurred on by activity in the Bakken, just south of Regina. While potash producers have scaled back output alongside weaker demand in China and India, the long-term prospects in the sector remain encouraging. BHP Billiton's $14 billion Jansen mine 140 km east of Saskatoon, while pushed back from the 2015 target date, is expected to produce 8 million tonnes per year.

Construction activity is also a major growth driver, as homebuilders keep pace with a surging population. Nonresidential activity is also firm after at least a decade of underinvestment in infrastructure—the combined value of nonresidential permits in the two cities was $836 million in the 12 months through January, near the highest on record. Employment growth remains solid in the province, rising 4.4% y/y in 2013Q1, the fastest pace in Canada and pulling the jobless rate below 4%, the lowest in over four years (and the lowest in Canada).

COMMERCIAL BANKING

John MacAulay,
Senior Vice President,
Prairies and Central Canada

With Saskatchewan continuing to be one of Canada's strongest economies, we are seeing all kinds of positive news among our commercial clients.

Taking the lead is agriculture, which represents 70% of our commercial business in the province. Farms are expanding in size, and the price of farmland continues to increase. However, there remains significant amount of demand for land. While it's not a free-for-all, farmers are having no difficulty selling.

With crops, the unusually late spring could have an impact. At a minimum, seeding will take place later than usual. Producers have the opportunity to plan for this—the larger ones may choose to lease extra equipment to seed 24 hours a day instead of 16.

In natural resources, mining is still strong and generating lots of employment. While the rescheduling of some BHP Billiton projects may flatten growth somewhat, we have yet to see a significant detriment to the industry. Meanwhile, the oil & gas industry continues to move along well near Lloydminster and Maple Creek, and in the Bakken. With so many projects ongoing, skilled labour remains a challenge.

In the cities, Saskatoon and Regina continue to be buoyed by increasing population numbers. Both cities are experiencing significant in-migration, with Saskatoon currently the fastest growing city in Canada. Residential real estate is consequently very strong, as is the demand for skilled trades, security, storage and restaurants.

Infrastructure spending continues as well, with corresponding benefits to independent contractors. Of particular note is Regina's new Global Transportation Hub, which will be accessible by rail, airport and road. Approximately 5,000 trucks go down the road to this hub every day, and we are expecting further impressive growth as more companies move their operations there.

Manitoba

ECONOMICS

Robert Kavcic,
Senior Economist

Manitoba's diverse economy continues to grow at a steady pace. Real GDP is expected to downshift to a 2.0% rate this year from 2.7% in 2012, though that would remain above the national average. Stability remains one of Manitoba's key economic strengths.

Energy and mining continue to see solid momentum in the province. While still a small share of the overall economy, the minerals sector has risen to nearly 7% of total output, with oil production ramping up to almost 18 million barrels in 2012 from about 8 million just five years ago. Manufacturing, however, remains the key driver and activity is sturdy thanks in part to the aerospace sector. Aging fleets in North America and rebounding passenger traffic are boosting demand—transportation equipment shipments were near a record high in the twelve months through February. Meantime, the agriculture sector enjoyed a rebound in production in 2012 after excessive moisture plagued crops the prior two years.

Job growth has been sturdy over the past year, with employment up 1.8% y/y in 2013Q1, led by the private sector. Resource-sector job growth is strong, but construction employment has been the star, surging nearly 20% y/y in the first quarter to record levels.

COMMERCIAL BANKING

John MacAulay,
Senior Vice President,
Prairies and Central Canada

Manitoba benefits from a very diverse economy. The province is typically steady—it seemingly never suffers a significant recession or benefits from a strong boom. This provides a stable environment in which our clients can do business and succeed.

We're seeing a very upbeat story in agriculture. Last year was very good, with lots of expansion, land acquisitions and rising property values. A number of our clients have taken the opportunity to invest in their equipment and processes with new technology. Productivity has improved following these investments, and our farms have the opportunity to compete globally as a result.

Manitoba's economic diversity applies to its manufacturing sector as well, with a number of different manufacturers with wide-ranging activities in plastics, metals and original equipment. Most of these successful manufacturers have a specialization niche. For instance, we have one client who developed a product that reduces concrete corrosion—a useful by-product of dealing with the harsh weather in Manitoba. But with infrastructure work happening across the continent, they've successfully expanded their sales base and developed new markets in both Canada and the U.S.

The U.S. downturn led to some softness, but there's been a solid increase in east-west trade with other provinces—particularly to support resource growth in Alberta and Saskatchewan. We had one client in wood products who never considered other parts of Canada as a potential market before because of ongoing strength in the U.S. But with the 2008 downturn, they invested in machinery, diversified their products, and tapped markets to the east and west.

Construction has been strong as well, particularly in Winnipeg. With plant expansions and building upgrades to support manufacturing, non-residential construction has a positive outlook.

Ontario

ECONOMICS

Robert Kavcic,
Senior Economist

Economic growth remains sluggish in Ontario with a cooling housing market, elevated loonie and fiscal restraint weighing on growth. Real GDP is expected to expand a modest 1.5% in 2013, with momentum picking up later in the year once growth south of the border begins to run at a 3%-plus clip.

The housing market continues to cool, and the stricter mortgage rules introduced last July have had a clear negative impact on sales. Existing home sales in Toronto slid 16% y/y in Q1, and price growth has cooled notably. Condo prices could face continued downward pressure as a wave of completions hit the resale market in 2013. Note that there are currently nearly seven condo units under construction in the GTA for every single detached home, and the amount of unsold inventory is the highest in at least a decade.

Manufacturing is not without challenges such as a Canadian dollar near par and relatively high labour costs. Perhaps the best news for the sector is the firming U.S. economic recovery and better consumer spending trends. Ontario’s labour market performance was mixed in 2012, with job growth of just 0.8%, but momentum encouragingly picked up later in the year alongside gains in the service sector.

COMMERCIAL BANKING

Susan Brown,
Senior Vice President, Ontario Provincial Division

Caution remains the prevailing sentiment among Ontario businesses. Levels of optimism vary depending on the region; while we do see pockets of strength throughout the province, businesses located where the recession hit harder, such as the southwest, are more wary.

Manufacturing will always be a major component to the Ontario economy. In the consumer auto sector, increased sales have led to stability, with tooling and parts companies that survived the slowdown now seeing stronger profits. In fact, this is a wider trend among manufacturers in general—those that cut costs and focused on productivity are doing much better. Pressure from the high Canadian dollar is a continuing concern, reinforcing the importance for firms to improve their productivity. We still encourage manufacturers to take advantage of low interest rates to invest in their businesses, and expect that positive environment to continue.

One unique emerging trend we are noting is company owners who could not sell during the downturn because of a lack of demand, are now moving to take advantage of increased valuations to exit their businesses. As a result, we have seen a number of opportunities in the succession financing space; pent-up demand is building and owners are now selling with the economy showing more stability.

The agricultural sector continues to be strong. Despite some pockets of drought in 2012, by and large yields were good and farm valuations are steady. Demand for quota remains high, meaning quota prices are continuing to move up. Meanwhile, consolidation in the sector and high demand are leading to record land prices.

Of particular note is the significant amount of spending by educational institutions. Universities are continuing to expand with demand for post-secondary programs on the rise. As examples, major construction programs are taking place in Waterloo, London, Windsor and Kingston—injecting strength to the non-residential construction sector and helping real estate in those centres.

Greater Toronto Area

COMMERCIAL BANKING

Mike Bonner,
Vice President, Commercial Banking, GTA Division

Growth in the GTA appears to be back in many of the important sectors that drive our customers' actions & success in the region.

GTA manufacturers have seen an increase in support from government policymakers. One of our manufacturing clients noted that the federal government has set aside key funding to support manufacturing efficiencies and new technologies—which will make Canadian manufacturers more competitive and allow them to grow their businesses and increase jobs.

There remains a sense of caution in the GTA market. Clients are optimistic, but wary of a fragile economic recovery going forward. Businesses have chosen to invest in opportunities that diversify their market share, whether that is new business ventures or adding and expanding to their existing clientele. This expansion, both horizontally and vertically, has driven modest growth across the Greater Toronto Area.

Many customers have observed growth in the construction sector which has benefited the GTA business environment. A long-time BMO client told us recently that there has been more construction in Toronto in the past year than any other market in Canada; he certainly has a positive outlook for the GTA market.

The construction sector has also been supported by a number of large-scale developments such as the Metrolinx Rail Expansion and Pan Am Games' facilities. These projects, in conjunction with others underway across the GTA, indicate growth in this sector that can be expected to continue at least until these multi-year projects are completed.

Overall, we understand the ebb & flow of the marketplace that we are in, and it is positive to see that many of our customers have confidence in the future. They are turning to BMO to help them strive to what they wish to achieve in 2013 and prepare them for what 2014 has to offer.

Quebec

ECONOMICS

Robert Kavcic,
Senior Economist

Economic growth continues to lag in Quebec amid fiscal restraint and a challenging business environment. Real GDP expanded just 1.0% in 2012, among the weakest performers in Canada, with economic headwinds compounded by student protests and a labour dispute with Rio Tinto Alcan workers. Growth should pick up to 1.2% this year as these temporary factors fade and fiscal restraint becomes less arduous, but the province will continue to underperform.

Fiscal restraint remains in focus, but the burden won't be overly severe in the year ahead. Program spending is forecast to grow 1.9% this fiscal year and 2.5% in FY14/15, modest contractions in real per-capita terms. Long-term capital spending targets were also cut by about $1.5 billion per year, but will continue to grow on a year-over-year basis. Employment remains volatile in Quebec, up a strong 2.6% y/y in 2013Q1. Net public-sector employment was down 1.8% y/y, but the private sector more than picked up the slack, up 4.1% y/y. Businesses were hesitant to hire against an uncertain political backdrop through much of 2012. Trade headwinds such as a strong Canadian dollar are also weighing on activity, but should improve as the expansion strengthens south of the border.

COMMERCIAL BANKING

Mario Rigante,
Vice President, Commercial Banking, Montreal District

Among BMO commercial clients in Quebec, there remains a base of cautious optimism. The positives are still obvious: Quebec has everything a company needs to succeed—a large, well-educated workforce, excellent real estate, plus strong domestic and international markets.

Meanwhile, businesses do understand the need to invest in their operations to improve productivity. However, they are choosing to be very selective and cost-conscious with their projects, investments and equipment purchases. There is certainly more attention being paid to the bottom line than we've seen in the past.

We do see investments being made by liquid-rich companies, but they are choosing to proceed based only on proven formulas. This represents an increase in risk aversion and a decrease in investment on potential—they are willing to pay, but they want to make sure their investments will provide proven earnings and proven growth.

However, the continued accessibility of capital has given some of our clients the opportunity to make the leap. We have one client—a seafood business on the north shore—that needed to refinance and recapitalize in order to re-inject funds into his cash flow. We worked to link him with asset-based lending partners who were willing to take on more risk, and the business got the ready access to capital—at a good price—that they needed.

Beyond that, companies are using accessibility of capital to make other investments, such as purchasing their own real estate.

On the non-residential construction side, there may have been a reduction in stimulus from governments but a number of high-profile projects are still ongoing—whether it's infrastructure in the cities like the Olympic Park or Techno-Park in Montreal, or resource extraction in the north. Capital is still being invested that will create the opportunities for those companies that gravitate toward such projects.

New Brunswick

ECONOMICS

Robert Kavcic,
Senior Economist

Economic growth remains very sluggish in New Brunswick as investment activity has cooled amid a period of fiscal restraint. Real GDP is expected to grow just 0.9% this year, underperforming the national average after declining in 2012, but should pick up again in 2014.

A downturn in capital spending in both the public and private sectors is a key reason for the soft near-term growth outlook. Overall capital spending intentions point to a 5.4% decline in 2013, with public-sector investment falling a steep 13.5% as the Province further ratchets down its capital spending program. In the private sector, some major project completions will temper growth, including the Point Lepreau nuclear plant refurbishment and Potash Corp's Sussex mine. Stronger U.S. growth, particularly in the housing sector, should help drive firmer exports into 2014—the forestry sector should benefit from the turnaround in the U.S. market.

Labour market trends reflect the soft economic backdrop, with employment unchanged from year-ago levels in the first quarter. Encouragingly, Nova Scotia's massive shipbuilding contract should see some benefits spill over into the province—J.D. Irving said it will be looking for 6,500 new employees in the coming years, with about 2,700 of those in New Brunswick.

COMMERCIAL BANKING

Allison Hakomaki,
District Vice President, New Brunswick & PEI

In the last two years, our customers have been focusing on their bottom lines and finding efficiencies to drive cost out of the business.

Those who are investing in technology are seeking cost savings, further production efficiencies and more capacity. A good example would be trucking companies that are equipping their trucks with satellite tracking, speed regulators and wind skirts to ensure their vehicles run with the utmost efficiency.

On the agricultural side, dairy customers are also finding efficiencies through technology despite challenges with rising feed costs. Technology is helping reduce input costs from feed to labour, allowing owners to increase the size of their operations.

Meanwhile, the potato industry of the Saint John River Valley is evolving into fewer, larger farms. The larger farms have increased contract volumes, and have replaced table potatoes with commodities like corn, soybeans and canola.

In Saint John, talk is turning to the ever-important energy sector. The idea of a west-east pipeline is certainly something that could excite everyone in the province; however, some companies aren't waiting for that. Now that Point Lepreau's refurbishment is complete, along with the second potash mine in Sussex, companies must look beyond their borders for opportunities. Our customers are capitalizing on the mining and energy activity in Newfoundland and Labrador to find new business, and they are also exploring the possibilities of exporting manufactured product to Alberta's energy sector.

On the lumber side, we are also seeing some renewed strength thanks to a rebound in the U.S. housing market. We are already noting a steady increase in the price of lumber in the past six to eight months, although they are still below the prices of a few years ago.

Nova Scotia

ECONOMICS

Robert Kavcic,
Senior Economist

Economic growth in Nova Scotia is poised to pick up over the medium term, but the near-term outlook remains subdued. Real GDP will likely grow 1.4% this year, up from just 0.2% in 2012, with growth prospects firming in the coming years as shipbuilding activity gets underway. It's not clear how much impact will be felt this year (perhaps we're still a year or two away), but capital spending intentions in the manufacturing sector are pointing to a near-20% increase in 2013. While clearly positive for the Nova Scotia economy over the medium term, the massive project is not without challenges. Among these is the availability of skilled labour, some of which continues to migrate to labour markets in Western Canada—the net outflow of 4,300 people in 2012 was the largest in more than 50 years.

While shipbuilding activity might not have an immediate positive impact in 2013, exports should see a rebound. The Deep Panuke natural gas project is expected to begin producing later in the year, and output at Sable should rebound after downtime in 2012. Auto-related exporters will also benefit from strong U.S. auto sales, which were almost back to pre-recession levels (+7.8% y/y) in the first quarter. The labour market remains sluggish, with little net new job growth in the past four years. Employment was down 1.1% y/y in the first quarter as the public sector shed more than 7% in the past year amid ongoing fiscal restraint.

COMMERCIAL BANKING

Carolyn Booth,
Senior Vice President,
Atlantic Provinces Division

The big story for businesses in Nova Scotia remains the massive, $25 billion, 30-year contract to build Canadian military vessels at the Halifax Shipyard. While the real impact won't be fully in place until 2014/2015, we are already seeing activity start to ramp up.

The contract will require companies to engage in a number of activities to support the project, including assembly, hauling and storage. Such a project cannot help but be positive, even if there remains the challenge of finding skilled labour with so many Nova Scotians working out west.

But there is an increasing understanding that the economic benefits from these projects are finite. While companies will make efforts to derive as much benefit out of them as possible, Nova Scotians need to consider a new question—how do we attract new, permanent employers to the province?

The province needs to have the benefit of firms that provide long-term, sustainable employment opportunities. These are the companies that can give Nova Scotians the opportunity to stay home and develop their skills. As well, the people who work at these firms will have the opportunity to learn skills that—hopefully—they can spin-off into new entrepreneurial ventures.

Some of those firms have already arrived. Research in Motion is here, and the provincial government has given them financial incentives to ensure they keep their 400 jobs in Nova Scotia. As well, IBM is on its way to establishing the company's only global delivery centre in Canada, with the Province as its main client. Along with several hedge-fund firms, these are the companies that can provide Nova Scotia with the long-term, sustainable employment opportunities that the major projects—as important as they are to the economy—typically don't provide.

Prince Edward Island

ECONOMICS

Robert Kavcic,
Senior Economist

The PEI economy continues to grow at a moderate pace, with real GDP expected to expand 1.5% this year after 1.2% growth in 2012. Firmer public-sector capital spending will help offset a slowdown in population growth, while exports are poised to improve.

Public-sector capital spending is expected to rebound after sliding 26% in 2012—PEI's latest five-year capital plan calls for a net $60.3 million in FY13/14. Notably, capital spending in the public administration sector is expected to jump 35% this year after fiscal restraint led to cutbacks last year. Private-sector investment growth, however, should remain subdued.

Meantime, population growth has slowed notably in the past year amid more normal immigration trends and ongoing out-migration to other provinces—the most since the late-1960s last year. Population growth was barely positive in the first quarter after expanding as quickly as 1.8% y/y early in 2011, and the slowdown should temper consumer spending and housing activity. Job growth remains solid in the province at 3.6% y/y in the first quarter, driven by gains in both the private and public sector. Private-sector gains have been largely in the trade, recreation and accommodation & food sectors—partly tourism related and partly the result of strong recent population growth, though the latter is now fading. The unemployment rate, however, has drifted up above 12%, and is just a few ticks below Newfoundland & Labrador as the highest in Canada.

COMMERCIAL BANKING

Allison Hakomaki,
District Vice President,
New Brunswick & PEI

Our clients in PEI are looking for a steady year ahead—they are not inclined to expand their businesses, but they do not want to step back either.

The agriculture sector—always an important component to the provincial economy—had a very strong year in 2012, but this strength had a great deal to do with a spike in prices. Most of our agri clients expect prices to slip from these heights, so they will be looking to a large and high-quality yield to compensate.

The fishery has had difficulties in the last several years because of the high dollar, a sluggish U.S. economy and lower demand and consumption in Japan. But 2012 saw some positive momentum, particularly with a lobster catch that was 10% above the previous year. With signs of an ongoing uptick in economic strength south of the border, export markets for the fishery—particularly high-end products like lobster and crab—may be set for improvement.

Tourism in the province is innately connected to the U.S. economy, so this industry is another that is hopeful of an upswing given renewed U.S. economic growth. Meanwhile, cutbacks from the federal and provincial governments may dial back consumer spending. But PEI continues to make a real effort to diversify its economy, with the aerospace industry and bioscience leading the way.

For residential construction, a number of small multi-unit projects are continuing; however, a high vacancy rate suggests a lack of new builds in the year ahead. Non-residential construction is stronger, with ongoing work on new retail space and a major convention centre in Charlottetown.

Newfoundland & Labrador

ECONOMICS

Robert Kavcic,
Senior Economist

Newfoundland & Labrador's economy is poised to bounce back after temporary factors tripped up growth last year. Maintenance shutdowns in the offshore oil sector sliced real GDP by 4.8% in 2012, but higher output, plus ramped up investment in the sector, should lift growth to 5% this year, the fastest in Canada.

Construction and capital investment activity have been key economic drivers in the province in recent years, and growth is expected to remain solid this year, with StatCan's survey pointing to a 9.7% increase. Investment in the oil & gas sector is expected to surge 83% as construction of the Hebron project ramps up (production won't begin until late 2017).

Other underlying economic trends in the province are solid. The jobless rate sits near a record low, though still high versus other provinces at 12.3%, helped by 3.0% y/y job growth. Average weekly earnings growth is also strong, up a heated 4.4% y/y in January, supporting personal incomes and consumer spending. Indeed, Newfoundland & Labrador retailers have enjoyed some of the strongest growth in Canada over the past year (+5.9%), trailing only Saskatchewan and Alberta.

COMMERCIAL BANKING

Jim Fallon,
District Vice President,
Newfoundland & Labrador

The recurring theme for Newfoundland & Labrador is consistent strength. Our customers are feeling positive, and major projects that have the long-term potential to drive economic growth are either moving along or coming closer to fruition. That said, there are no new confirmed projects on the horizon, and the mood of our customers, while good, has plateaued. There is still optimism in offshore oil and gas industry for possible expansion of existing projects as well as deep water exploration.

Projects like Muskrat Falls and Hebron, for instance, are now in progress and ramping up—not proposals for the future. That is leading to actual contracts for work, particularly on the non-residential construction side where there's often more work to be done than what have the capacity to do. We have one customer in St. John's who deals mainly with commercial construction—he tells us he was thinking of cutting back but can't, because he's benefiting so much from the ramping up of major projects.

This situation, while positive, still brings us to the ongoing difficulty of labour shortages—a challenge that affects a number of the firms that want to take advantage of the number of available projects.

The fishery, meanwhile, is benefiting somewhat from recovering U.S. markets. As long as demand for product remains high, the industry—which has been troubled in the past—will remain viable.

We've also had a great deal of success working with Aboriginal governments and supporting significant development in Labrador. In both eastern and western Labrador there's optimism that more projects are coming.

As an example, construction of a new town centre is underway in Goose Bay. That's a town that had suffered a downturn after the loss of all the foreign militaries that operated out of the air force base, but now things have never been better there. With such ongoing projects, the future is definitely bright in Labrador.

Provincial Economic Summary

	BC	Alberta	Sask.	Manitoba	Ontario	Quebec	NB	NS	PEI	NL	Canada
Real GDP Growth (chain-weighted : year/year % change)											
2012	1.7	3.9	2.2	2.7	1.4	1.0	-0.6	0.2	1.2	-4.8	1.8
2013 f	1.7	2.5	2.4	2.0	1.5	1.2	0.9	1.4	1.5	5.0	1.6
2014 f	2.5	2.9	2.8	2.3	2.3	1.8	1.6	1.9	1.7	1.8	2.3
Employment Growth (y/y % chng)											
2012	1.6	2.6	2.2	0.9	0.8	0.8	-0.2	0.6	1.0	2.1	1.2
2013 f	0.3	1.6	2.2	1.5	1.2	1.4	0.2	0.0	2.2	1.8	1.2
2014 f	1.5	1.5	1.2	0.9	1.4	1.2	0.5	1.1	0.2	0.3	1.3
Unemployment Rate (percent)											
2012	6.8	4.6	4.7	5.3	7.9	7.8	10.3	9.0	11.4	12.5	7.3
2013 f	6.5	4.6	4.4	5.0	7.5	7.5	10.5	9.2	11.7	11.8	7.0
2014 f	6.3	4.4	4.2	5.0	7.1	7.2	10.1	8.8	11.4	11.6	6.7
Housing Starts (thousands)											
2012	27.5	33.3	10.0	7.4	77.0	47.1	3.3	4.5	0.9	4.0	215.0
2013 f	21.4	32.0	8.0	6.6	55.5	40.0	2.7	4.8	0.8	3.4	174.5
2014 f	20.5	31.0	7.5	6.0	53.5	40.0	2.7	4.8	0.8	3.3	170.0
Consumer Prices (year/year % change)											
2012	1.1	1.1	1.6	1.6	1.4	2.1	1.7	1.9	2.0	2.1	1.5
2013 f	0.5	1.3	1.5	1.4	1.3	1.5	1.3	1.5	1.3	1.7	1.3
2014 f	1.7	2.0	2.1	1.8	1.8	1.8	1.5	1.7	1.5	2.0	1.8

f = forecast