



ALBERTA ECONOMIC OUTLOOK

November 2017

ATB Financial's Alberta Economic Outlook

Winter 2017

Economics and Research, ATB Financial

Released four times a year, ATB Financial's *Alberta Economic Outlook* summarizes the province's current economic landscape to give us an idea of what the future may hold for our economy. The *Alberta Economic Outlook* aims to provide Albertans with commentary that is clear and meaningful.

Overview

Coming out of two years of deep recession, Alberta's economy is now gaining momentum as 2017 draws to a close.

Global growth in Europe, the US and Asia has given a boost to energy prices, which have also been helped by some supply constraint and political events in the Middle East. Crude oil prices, as measured by the West Texas Intermediate (WTI) benchmark, have hovered close to the \$US 50 per barrel mark for most of the year, but in November they've risen above \$US 55--the highest in two years. That's helped stabilize Alberta's oil industry.

Agri-foods and beverages, tourism and retail sales are showing steady growth and are adding to the province's comeback this year. Construction activity is still slowing, though, particularly in non-residential projects.

Real GDP growth is expected to approach four per cent in 2017, which is likely to be the highest among the Canadian provinces. Growth will moderate to close to Two-and-a-half per cent over the next two years.

Key results:

- Alberta has emerged from two years of recession with growth of around four per cent in 2017, likely the strongest in Canada.
- Retail and housing sector performance have improved
- Oil prices have steadied and begun to inch higher (currently around \$US 55 per barrel).
- Alberta's energy sector will grow this year, particularly in conventional drilling.
- Tourism, agriculture and agri-food will continue to show steady growth
- Net out-migration to other provinces will likely taper off but still continue.
- Alberta is expected to see a stubbornly high unemployment rate in 2017 and 2018.

	2016	2017	2018	2019
Real GDP growth (annual % change)	-3.7	3.9	2.7	2.2
Consumer price index (annual % change)	1.1	1.6	2.3	1.9
Unemployment rate (%)	8.1	8.0	7.3	7.2
Employment (annual % change)	-1.6	2.0	1.2	2.3
Housing starts (000s)	24.6	28.9	28.4	27.1

Oil and gas

At the beginning of November, the price of West Texas Intermediate broke the \$US 55 threshold for the first time in over two years. Draws on crude inventories and a general rebalancing of supply and demand fundamentals are lifting prices. Not surprisingly, markets continue to be fixated on OPEC's next move. Much of the tightening in oil supply has been driven by OPEC's decision since January to cut 1.8 million barrels of crude from the market and those cuts may or may not continue. Saudi Arabia and Russia have suggested they are willing to extend the cuts to the end of next year, but markets will have to wait to see if a formal commitment is made.

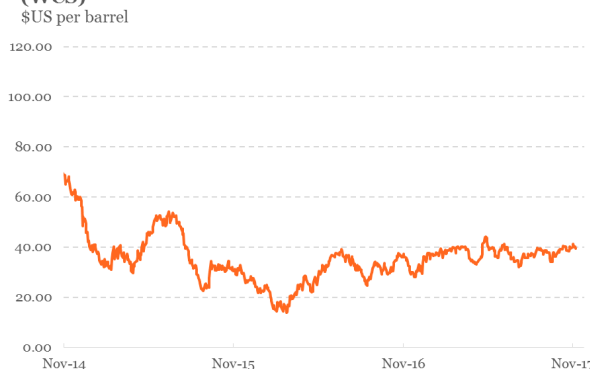
Throughout the summer, there were continued concerns that rising US shale output would disrupt stability in crude markets and keep oil's price pinned lower. However, stronger than expected demand kept supply at bay and prices stable. Prices since ATB Financial's previous *Alberta Economic Outlook* have increased slightly and have averaged just over \$US 49 per barrel. As we head into 2018, our economics team has revised its projection for the price of oil in 2017. We now anticipate that oil prices will average around \$US 50 per barrel (WTI) this year and move marginally higher next year.

Alberta oil production has ramped up this year despite the fact that oil prices have hovered below the \$US 50 per barrel (WTI) range for the majority of 2017. Additionally, new projects related to non-conventional extraction (i.e., oilsands) are underway and have helped boost output. As such, large investments in new oilsands projects are unlikely to materialize in the

Daily crude oil price, West Texas Intermediate (WTI)



Daily crude oil price, Western Canadian Select (WCS)



short-term with oil prices near \$US 50 a barrel.

As we head into 2018, changes within the oil and gas industry are beginning to take effect. There will be a greater focus going forward on short-term, nimble projects rather than large-scale, long-term projects.

The Canadian benchmark for natural gas (AECO spot price) started 2017 on a brighter note but quickly declined through the summer. Lately, AECO's spot price hasn't shown much improvement. Throughout the summer, the price hovered between \$1.00 and \$2.00/MMBtu. As of November, the price of the Alberta benchmark was averaging above \$2.00/MMBtu.

Weak natural gas prices over the course of this year are the result of lacklustre demand. Specifically, demand for heating and cooling has been low due to higher inventories and weather conditions. Weather models predict higher than average temperatures for parts of Canada and the US this winter, and with a higher inventory build, it's likely that natural gas will not see material price gains for quite some time. We anticipate natural gas prices to average slightly below \$2.00/mmBTU (AECO) this year. The North American benchmark, Henry Hub is expected to average \$US 3.00/MMBtu in 2017.

Daily natural gas price, AECO
\$US per MMBtu



Daily natural gas price, Henry Hub
\$US per MMBtu



Labour Market

As numerous job reports have shown this year, the path toward recovery for Alberta's labour market hasn't been a straight line. After several promising months during the first half of 2017, the province's job picture kicked off the second half of 2017 with less optimism. However, since the summer months, the province's labour market has gained some traction.

In October, Alberta racked up a gain of 12,000

Change in employment, Alberta
Thousands, seasonally adjusted

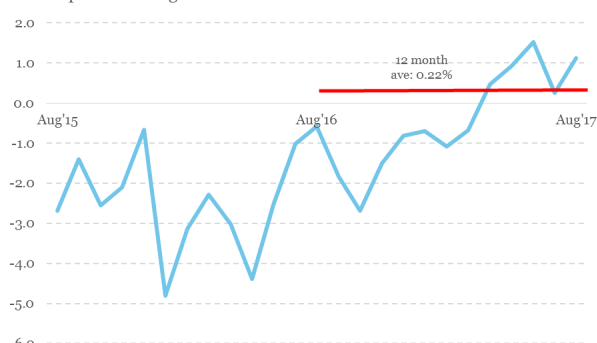


new jobs—all of them full-time. That follows big losses in July and September and only a small gain in August. October’s employment gains were one of the largest the province has seen in the post-recession period. Overall, job growth seems to be moving in the right direction, albeit unevenly.

Compared to a year ago, the sectors responsible for the strongest job gains were transportation and logistics (+8,300), manufacturing (+7,800) and finance, insurance, real estate and rental and leasing (+5,600). The commercial construction slowdown in Alberta’s large cities and towns caused job losses in construction (-4,700) and accommodation and food (-4,200).

Average weekly earnings, Alberta

Annual per cent change



Source: Statistics Canada, CANSIM Table 281-0063

Both business confidence and overall economic conditions have improved since the beginning of the year, but plenty of employers still remain hesitant to add workers to the payroll. However, the 12-month trend does show an improved job market in Alberta. Net employment is up by 0.75 per cent. We are projecting Alberta’s unemployment rate will average 8.0 per cent this year, a marginal improvement from last year’s average of 8.1 per cent.

After falling for much of the year, wages have begun to creep higher. This has helped support housing and retail in the province. In August, average weekly earnings of employees grew about one per cent over the month to \$1,134. This figure is adjusted for seasonality and includes overtime pay, but excludes taxes.

In August, there were several job categories that registered increases in pay. Surprisingly, the most significant gains were made in the mining, quarrying and oil and gas category. Weekly wages for workers in this group grew by 5.4 per cent to \$2,320 per week. Statistics Canada notes that net employment in this higher-paying sector increased by 8,100 (8.3 per cent) in the 12 months leading up to August and has contributed to overall provincial earnings growth. Wages in this category are up close to four per cent, year-over-year. Other noteworthy pay gains were made in finance and insurance (4.3 per cent) and real estate (3.5 per cent).

Despite overall wage growth in August, not all industries saw improvements. For the second month in a row, take-home pay of administrative and support, waste management and remediation services workers fell the most (-8.5 per cent). Other significant pay declines were recorded in forestry and logging (-6.1 per cent) as well as utilities (-3.5 per cent).

The fact that both employment and wages in our energy sector are up significantly from last year is good news for Alberta’s labour market and for the recovery in general. Improving wages in the coming years will continue to support the province’s retail sector as well as housing and other forms of residential investment.

Agriculture and forestry

At the end of last year, cattle ranchers in the province had to deal with potential bouts of bovine tuberculosis. Reduced herd sizes and higher demand for beef improved the price of cattle slightly at the beginning of the year. Cattle prices continued to gain momentum in the summer months, but have since fallen. As of September, the price of cattle was \$125.83 per hundredweight. Compared to last year, this is an improvement of about one per cent. Despite the marginal improvement over the course of 2017, cattle prices are well short of their highs reached back in 2015 (approximately \$190 per hundredweight).

Like cattle, hog prices have followed a similar path. September's pricing shows that the price of hogs per hundredweight was \$64.03. That's about 1.5 per cent less than the same month during last year. It's expected that both hog and cattle prices should remain in these ranges for the rest of 2017.

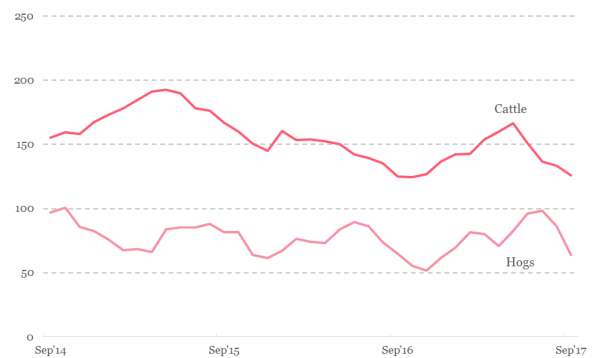
It's not just livestock prices that are having a bit of trouble, canola has also struggled lately.

Compared to the time of the last *Outlook* (July 2017), canola crusher (the main input to canola oil) has fallen about six per cent. However, compared to last year, crusher prices are still about 5.9 per cent higher than last year's average price.

Unlike livestock and canola, wheat prices have improved significantly from last year. Drought conditions in parts of the US have helped boost prices. As of September, prices were up about 15 per cent. If current prices for wheat continue their trend and the weather cooperates, grain farmers could continue to see decent returns this year and next.

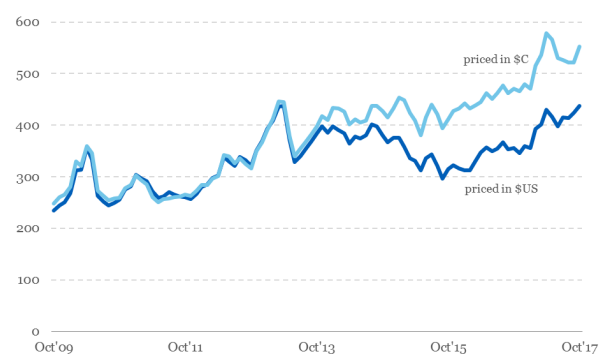
Despite the expiry of the Canada US Softwood Lumber Agreement and the US-imposed steep tariffs on Canadian lumber imports, Alberta's forestry sector is performing better than expected. As of October, the average benchmark price for North American framing lumber has remained strong. That month, the average price was \$US 438 per thousand board feet (the price is calculated by Random Lengths, an American industry group, and is based on the average of 15 key framing lumber prices). October's price was up 3.3 per cent from September and prices are now up 23 per cent since the beginning of the year. When calculated in Canadian dollars, the

Livestock prices, Alberta
Dollars per hundredweight



Source: Statistics Canada, CANSIM Table 002-0043

North American lumber prices*
Dollars per thousand board feet



Source: Random Lengths
*composite price is a weighted average of 15 key framing lumber prices

benchmark lumber price is actually around \$560 dollars per thousand board feet. While this price appears lucrative, part of this increase is due to diminished supply from this summer’s forest fires in British Columbia.

While pricing remains attractive for forestry producers, there’s no denying that Canada’s forestry sector is experiencing tension and strife. Since April, domestic producers have had to deal with steep tariffs on their lumber imports and a new trade agreement in softwood lumber is not expected anytime soon. This puts Alberta exporters at a disadvantage to US producers. The tariffs and uncertainty surrounding a new softwood arrangement—and Canada-US trade relations in general—are expected to slow the province’s forestry industry for the remainder of this year and in subsequent years.

Construction and real estate

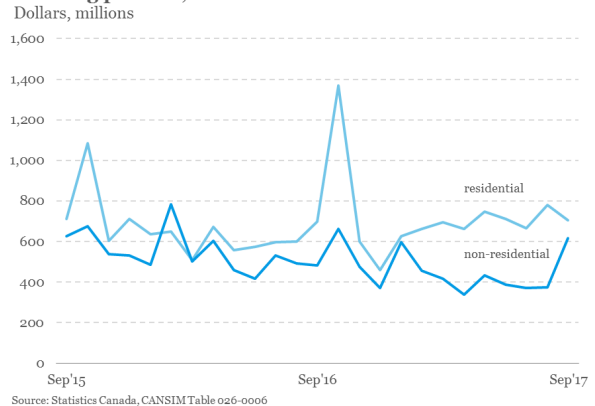
Building activity in Alberta has slowed since the furious pace set during 2010 to 2014. However, despite Alberta’s economic contraction over the last couple of years, overall construction activity has been remarkably stable.

In September, building permits issued by Alberta’s towns and cities totalled \$1.3 billion, an increase of about 15 per cent from August. Compared to the same time last year, total building permits in Alberta are up by 12 per cent.

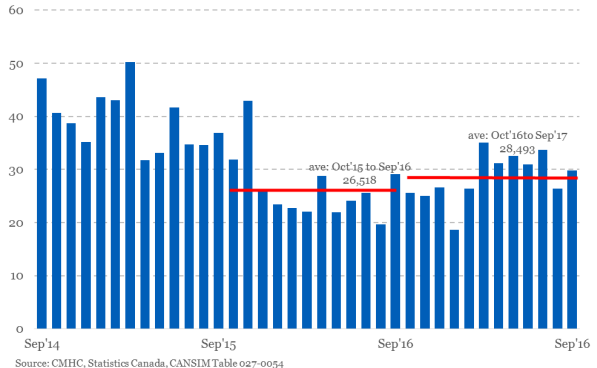
The residential sector as a whole reached \$704 million in September. Despite the fact that building permits fell nearly 10 per cent from August, permits are up from the same month last year and are up on the year as a whole. What’s more is that September’s total was nearly \$10 million above this year’s residential permit average, suggesting that Alberta’s residential sector is solid.

What was most surprising in September was that non-residential construction intentions grew the most and reached the highest total of 2017. Non-residential projects saw \$617 million of permits issued in September, nearly double August’s total. Permits for both industrial and governmental and institutional buildings helped advance non-residential activity. This category grew two-fold from August to September because of a high-value permit for a new hospital in the province.

Building permits, Alberta



Housing starts, Alberta
Thousands, seasonally adjusted annualized rate



Permits for commercial projects (such as office towers and business malls) experienced losses over the course of the month (-11.3 per cent) and are still down significantly from where they were at this time last year (-21.2 per cent). Looking ahead, commercial activity is expected to remain quiet. Both Calgary and Edmonton have a significant amount of commercial and residential real estate coming online in their downtowns over the next couple of years. As a result, future activity, particularly in the non-residential space, will be muted over the short- and medium-term. As we head into 2018, building activity as a whole may begin to recede.

In October, home builders started construction on 29,403 homes in the province, including multi-family units. The figure is adjusted for seasonality and is expressed as an annualized rate (that is, the number of units that would be built in one year if the pace in June continued for 12 months).

Given Alberta's economic state, housing starts throughout the year have been a pleasant surprise. The pace of building has barely slowed throughout the year. Both prices and rates are helping drive consumers' appetite to get into home ownership.

Throughout the recession, house prices across Alberta (both new and existing) barely moved. Now that the recession is over, buyers who were on the sidelines may be itching to jump into the market because they are more certain prices are not going to fall any further.

The Bank of Canada raised borrowing costs in July and September. Canada's better-than-expected economic performance suggests that mortgage rates could continue to rise by the middle of next year, which could prompt more buyers to get into the market sooner rather than later.

That may leave home builders feeling cautious and could slow housing starts in the next couple of years. Alberta may have emerged out of recession in 2017, but the expansion remains gradual. If too much new home inventory goes on the market in advance of buyers, prices could tip lower. A slight moderation in housing starts is expected next year.

Home prices in Edmonton have begun to show a bit of momentum over the second half of the year. In October, the average price of a single-detached home was \$431,654. That was 1.4 per cent higher than the same month last year. The median sale price in October was \$390,000, down 0.74 per cent from October of 2016.

In Calgary, the average price of a house in October was \$475,720, a little more than a three per cent increase from last year. The median price in October also advanced +1.2 per cent to \$415,000.

Wholesale, retail and manufacturing

Over the course of eight months, Alberta's wholesale trade has shown consistency. Even though sales fell between July and August, activity is up about nine per cent.

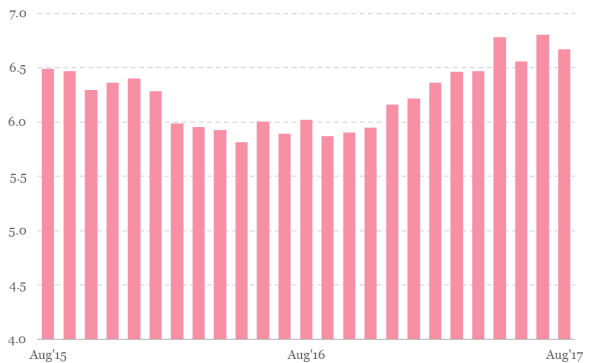
In August, sales to businesses, institutions and government reached \$6.7 billion. Since last year, sales in all but one subsector are up significantly. Farm products (+39.5 per cent), building materials and supplies (+26.4 per cent), and motor vehicle and parts (+15.6 per cent) have shown the greatest progress. The only wholesale category to register a decline from last year in September was the personal and household goods category (-6.2 per cent).

After retail sales reached an all-time record high in October of 2014, Alberta consumers started to buckle under the weight of plunging oil prices and falling confidence. But as the recession's grip eased up, shoppers returned to the malls, big box stores and car dealerships. Although August's wholesale total was reduced from July, total activity as a whole is up almost to where it was last year.

In August, total sales did slip to \$6.74 billion (adjusted for seasonality), but that was after sales hit an all-time record high in June (\$6.8 billion). Despite the small pullback over July and August, total sales in the province remain solidly above the levels hit during the recession. Over the last complete 12 months, sales are 5.3 per cent higher compared to the previous 12-month period.

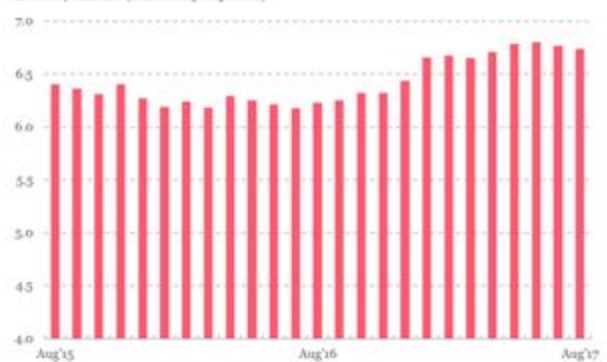
Durable goods such as vehicles have shown particular promise. The latest data on vehicle sales show that 22,257 new cars and trucks rolled off the dealership lots in August. Sales are up nearly 20 per cent year-over-year, a number that's been relatively consistent this year. On one hand, this sales growth may be prompted by pent-up consumer demand—that is, at a certain

Wholesale trade, Alberta
Dollars, billions (seasonally adjusted)



Source: Statistics Canada, CANSIM Table 081-

Retail sales, Alberta
Dollars, billions (seasonally adjusted)



Source: Statistics Canada, CANSIM Table 080-0020

Manufacturing shipments, Alberta
Dollars, billions (seasonally adjusted)



Source: Statistics Canada, CANSIM Table 304-0015

point many consumer items simply need to be replaced, even if shoppers aren't in the mood to spend. On the other hand, the growth may be due to cheaper financing options.

As a whole, retail sales are expected to push higher than last year, but this impressive growth isn't expected to last. Slower retail activity in the coming years will be due to Alberta's relatively slow economic recovery, but also because of higher mounting consumer debt levels and rising borrowing costs. Specifically, the durable and semi-durable good categories may be hit hardest.

Alberta's manufacturing sector has performed well recently, too. Sales from Alberta factory floors reached \$5.8 billion in September. While that month's total was one per cent less than August, September's sales number was enough to bring shipments up 10 per cent from where they were a year ago.

Notable increases occurred within petroleum and coal products (+4.0 per cent), electrical equipment, appliance and component manufacturing (+5.7 per cent), as well as paper manufacturing (+6.0 per cent).

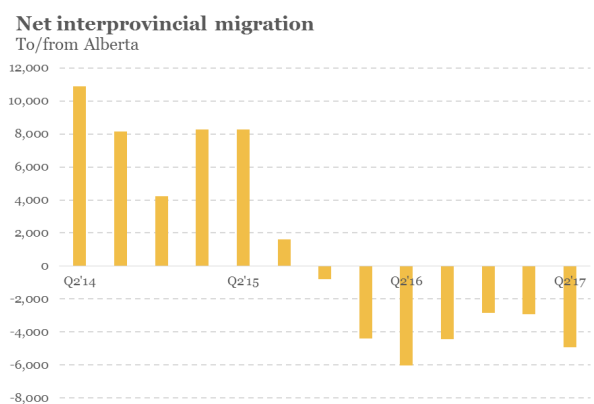
After slowing significantly in 2016, sales from most energy-related industries (machinery, primary metal, fabricated metal, etc.) are well above from where they were at the same time last year. The growth in these industries is vital to Alberta's energy sector. Their performance for far this year is a sign that shows Alberta's energy sector is gaining a bit of strength after a rough couple of years.

Almost all of the manufacturing industries are above where they were a year ago. The most optimism remains in food and beverage processing, though both have experienced some setbacks recently. In general, as economic conditions improve in Alberta and the province's energy sector continues to progress, manufacturing will continue to help with Alberta's economic recovery.

Population

For seven consecutive quarters, Alberta has seen a net outflow of interprovincial migrants. Most recently, the province experienced a net loss of 4,914 residents between April and June. Alberta's weak economy and struggling labour market explain the net outflow.

In 2017, it's expected that Alberta will continue to suffer a net outflow of interprovincial migrants. Last year, the province lost about 17,700 people to other provinces. ATB's economics team anticipates moderate improvement on this front in 2017 with the net



interprovincial loss coming in around 8,000 people. In 2018, we project a net inflow of people coming to Alberta from other provinces.

Political instability and economic challenges in other parts of the world will continue to support the flow of international migrants to Alberta. Recent announcements from the federal government suggest an increase in the number of international migrants in the coming years. High immigration numbers bode well for retail and housing, two sectors in the province that are expected to slow in the coming years.

Not only will international migration help offset the interprovincial losses, but natural population increases (births minus deaths) will also add to Alberta's population base. Due to its relatively young population, Alberta has the lowest provincial death rate and one of the highest birth rates. As a result, it has the highest rate of natural increase among the provinces and this helps keep the population growing even when interprovincial migration is negative.

Conclusion

The recession of 2015-16 is firmly behind us. Alberta's economy is posting a comeback—albeit a gradual and uneven one.

The energy sector has stabilized and is enjoying some modest growth in business investment, especially in conventional drilling. But the advances are coming on the heels of two years of massive contractions. It takes less capital investment today to see 10 or 20 per cent growth than it did prior to the downturn. Nonetheless, these improvements have been critical to Alberta's turn-around in 2017. The energy sector is the backbone of the economy, even if it is not a growth engine in the same way it was between 2010 and 2014.

Other sectors have also contributed to growth this year, including food and beverage processing, retail and wholesale trade and business and personal services (i.e., tourism and IT sectors). Construction activity is set to slow in the wake of massive commercial building project starts and completions over the last few years.

The most significant challenge remaining for Albertans will be the job market. Despite posting real GDP growth of close to four per cent this year—likely the strongest in Canada—Alberta is still suffering unemployment of nearly eight per cent. The economic growth spurt this year will feel counter-intuitive for thousands of jobless Albertans. They may even doubt the legitimacy of the economic data. In late 2017, the economy does not “feel” strong.

Alberta's economy is evolving, but not necessarily returning to what it looked like prior to the downturn. New industries are gradually emerging. Yet it may take a while longer before job growth pushes unemployment rates back to four or five per cent.

ATB Financial's economics team is forecasting growth of 3.9 per cent in 2017, to be followed by growth of 2.7 and 2.2 per cent in the following two years respectively.