



As Good As It Gets

Alberta Economic Profile and Forecast

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WESTERN CANADA'S ECONOMY

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1. Overview

Spurred by high energy prices, rapid population growth, and surging employment, Alberta's economy is basking in the best of times in the spring of 2006. Economically, this is truly *as good as it gets*. Almost every sector of the economy is operating at or near full capacity.

Provincial government spending—up 8.3% in 2006/07—will add fuel to the economic fire, as will the coming tax reductions for businesses and the federal government's proposed reduction of the GST by 1 percentage point.

Despite Alberta's current economic strength, policy-makers still face significant economic challenges. Most of the trouble spots relate to the fever pitch of activity in the province:

- general labour shortages are causing opportunities to be lost, increasing payroll expenses for businesses, and exacerbating high school drop-out rates;
- in the construction sector, skilled labour and material shortages are lengthening construction time and adding to project costs;
- forestry and agriculture continue to feel the pressure of low commodity prices and high input costs;
- the provincial government has demonstrated a disappointing lack of vision by not articulating a long-term strategy for managing non-renewable natural resource revenue; and
- the provincial economy remains highly dependent upon volatile energy prices; the services and manufacturing sectors are doing very well, but in most cases they rely, directly or indirectly, on energy sector activity.

Momentum is on the side of continued growth in the province. Even if energy prices ease somewhat, the steady inflow of workers into the province and the abundance of employment opportunities will keep the economic ball rolling. **The Canada West Foundation is forecasting real GDP growth of 5.2% for 2006 and 4.7% for 2007.**

Figure 1:
Summary of Real GDP Growth Forecasts for Alberta
Annual % Growth

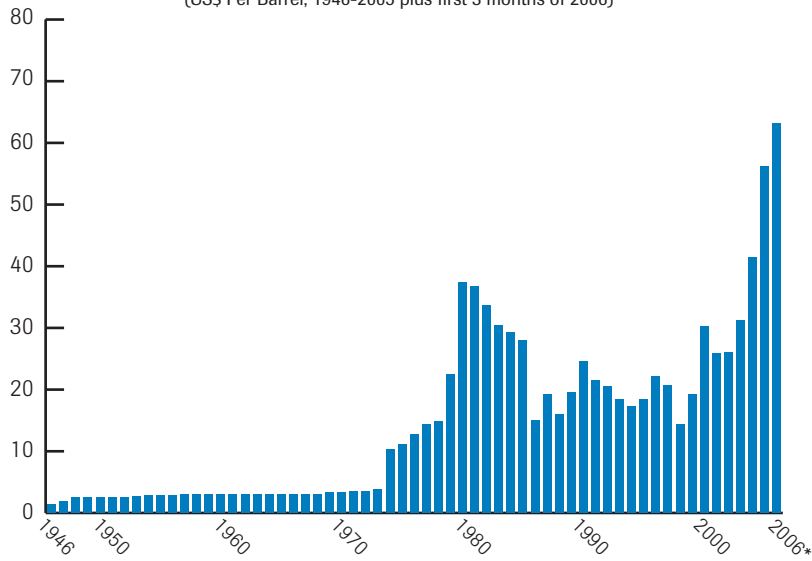
	2005	2006	2007
Alberta Budget (March 2006)	4.3%	4.8%	3.5%
BMO Economics (March 2006)	4.2%	5.2%	4.5%
RBC Financial (March 2006)	4.6%	5.2%	4.0%
TD Economics (February 2006)	4.4%	4.5%	3.4%
Scotiabank Economics (March 2006)	4.6%	4.8%	4.0%
CIBC World Markets (February 2006)	5.0%	7.0%	6.0%
Canada West Foundation (April 2006)	4.8%	5.2%	4.7%

2. Oil and Gas

The surging energy sector is clearly responsible for much of Alberta's rapid economic growth. The Petroleum Services Association of Canada estimates a record 20,000 wells will be drilled in Alberta in 2006. Crude oil prices have remained in the range of US\$60-\$68/barrel for much of the past year, leading to record drilling and oil sands investment. Natural gas prices have dipped due to warm weather in the winter, but also remain very robust.

In the oil sands, billions of dollars worth of mining projects, upgraders, refineries, and in situ projects are underway, with many more at the planning or proposal stages. According to Statistics Canada, investment in non-conventional oil extraction in Canada is expected to rise 10.6% in 2006 to \$10.8 billion. Investments in Alberta's oil sands will account for the vast majority of this total.

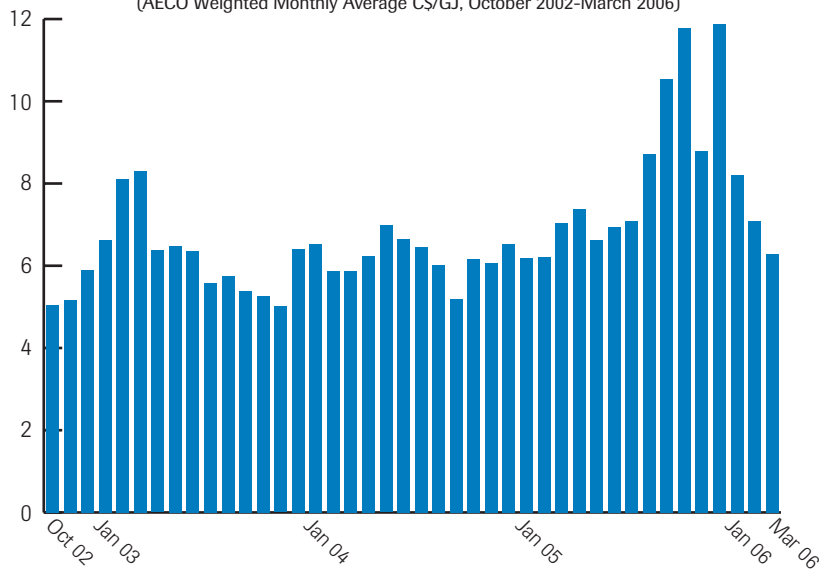
Figure 2:
Annual Average Price of West Texas Intermediate Crude
 (US\$ Per Barrel, 1946-2005 plus first 3 months of 2006)



*First 3 months only
 Source: www.economagic.com

Figure 3:
Natural Gas Prices

(AECO Weighted Monthly Average C\$/GJ, October 2002-March 2006)



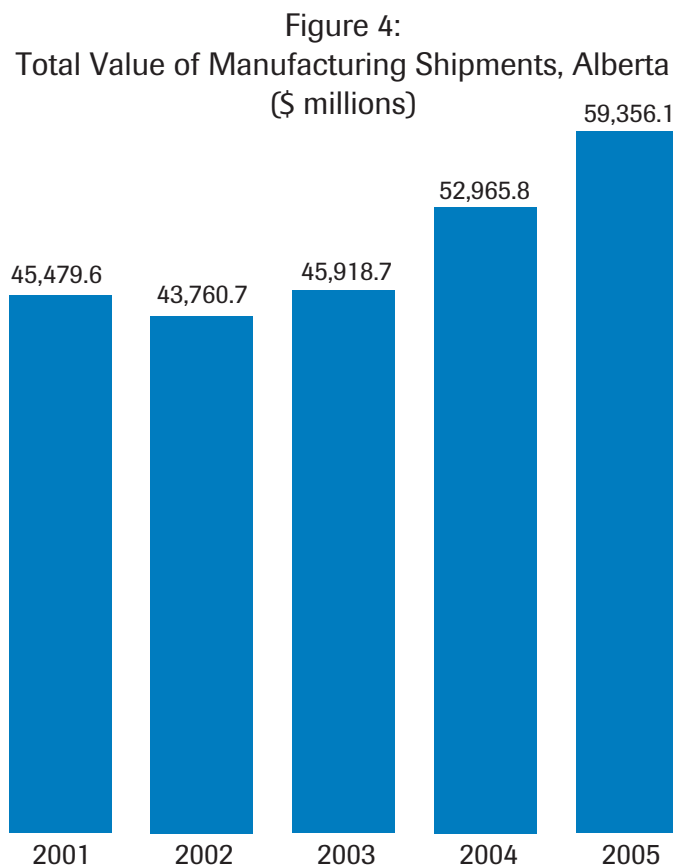
Source: www.ngx.com

3. Manufacturing

Manufacturing activity in Alberta continues to rise dramatically with a 12% increase in 2005. This compares to a national increase of 3% over the same period. The expansion in Alberta has happened despite the high Canadian dollar.

While the dramatic rise in manufacturing activity in Alberta may suggest growing economic diversity in the province, this argument is less compelling when the statistics are analyzed by sector. Over 40% of the value of manufacturing shipments is in three categories, all of which are related to the energy sector: refined petroleum products, chemical production, and plastics. Other manufacturing categories such as machinery and fabricated metals are also heavily dependent upon activity in the energy sector. Alberta's economy is still very dependent upon oil and gas.

Food manufacturing accounted for \$8.7 billion in activity in 2005, down about 4.6% from the previous year (see Figure 5). Some of this decline can be attributed to the re-opening of the US border to live cattle exports in 2005, which has resulted in less live cattle slaughtering and packing in Alberta compared to a very busy year in 2004.



Source: Statistics Canada, CANSIM Table 304-0015

Figure 5:
Value of Food & Beverage, Refined Petroleum,
and Chemicals Manufacturing in Alberta (\$ millions)

	Food & Beverage	Refined Petroleum	Chemicals
2000	8,313.2	8,195.4	7,595.8
2001	8,421.1	7,523.5	8,242.5
2002	8,275.0	7,495.8	7,855.6
2003	7,976.4	8,257.4	8,284.8
2004	9,087.3	10,017.9	9,645.3
2005	8,686.1	12,757.2	10,489.3

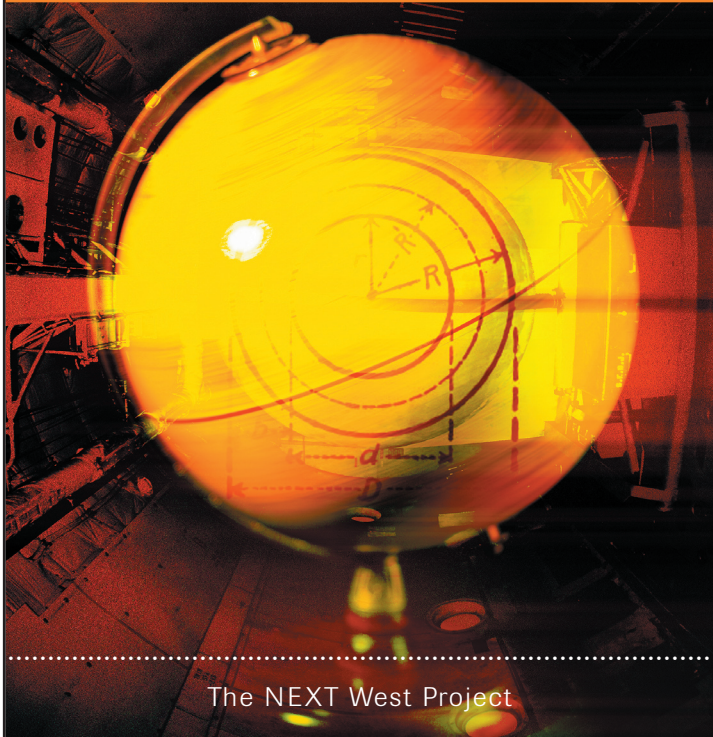
Source: Statistics Canada, CANSIM Table 304-0015

Looking forward to the rest of 2006 and 2007, manufacturing should continue to expand, albeit at a more moderate pace than that set over the previous two years. Drilling activity and increased bitumen flow from the oil sands will boost refined petroleum product manufacturing. The trend line for chemical and plastics production, however, is less certain. Securing a sufficient supply of ethane feedstock is a key challenge. (Ethane is extracted from natural gas and is the base input in the production of ethylene. Ethylene is used to make plastics.)

SHAPING OUR FUTURE

The Transformation of Western Canada's Economy

Calgary, April 28, 2006




The NEXT West Project

Featuring a keynote presentation by bestselling author Dr. David Foot, the **Shaping Our Future Conference** will gather experts from business, government, economics, and industry associations to explore a long-term public policy strategy for western Canada's economy. Three main questions will be posed:

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- 2** What do we want the economy of western Canada to look like in 2026?
- 3** What policies can we put in place now to help create the economy we envision for 2026?

A conference report will be released in the fall of 2006.



4. Tourism

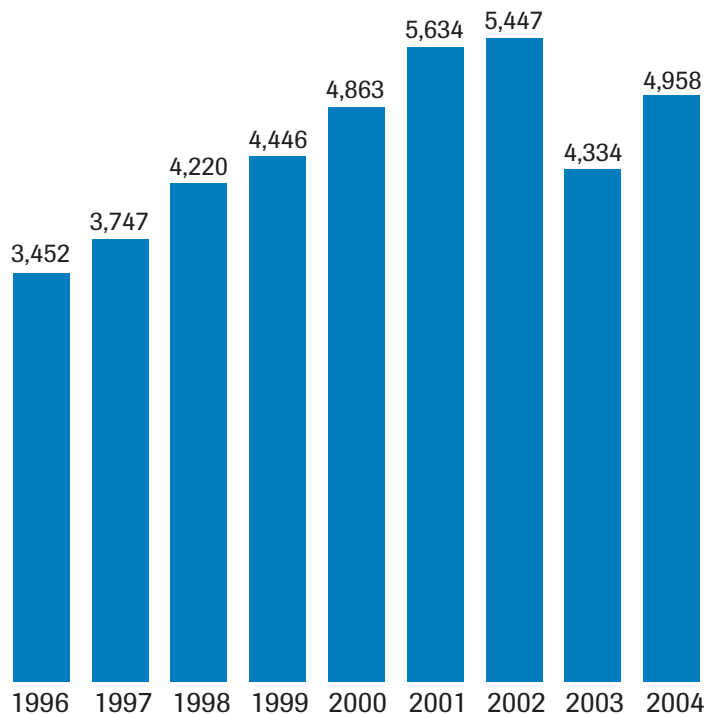
Tourism in Alberta is a \$5 billion industry that employs more than 103,000 people. Tourism operators in Alberta were dealt a series of blows in the early part of the century (9/11, SARS, and forest fires). The hit was particularly hard in 2003 when receipts fell some 20%.

However, statistics on travel and spending indicate that tourism in Alberta may be making a modest recovery. Occupancy rates in hotels were up in 2005 from 2004 (an increase of 3.8 percentage points in Edmonton to 66.1%, and 4.3 percentage points in Calgary to 69.8%). Total visits from the US fell in 2005 by 8.6% due, in large part, to higher fuel prices. However, other international visitors increased by 6.8%. Restaurant receipts rose in 2005 by 7.8% to just over \$4 billion (although not all of these receipts can be attributed to tourists).

The 2006 provincial budget announced a 15% increase in funding for tourism marketing and development. This means an increase of more than \$6 million, bringing total funding to \$48 million. Travel Alberta will spend \$41 million to promote tourism in the province and Alberta Economic Development will spend \$7 million in assisting communities to identify tourism development opportunities.

As a result of these initiatives, forecasts for tourism receipts are positive. Barring future geopolitical crises, major jumps in fuel prices, or SARS-like pandemics, it is expected that tourism receipts in 2006 could surpass the record \$5.4 billion mark set in 2002.

Figure 6:
Total Tourism Receipts, Alberta
(\$ millions)



Source: Statistics Canada Canadian Travel Survey and International Travel Survey and Alberta Economic Development

5. International Exports

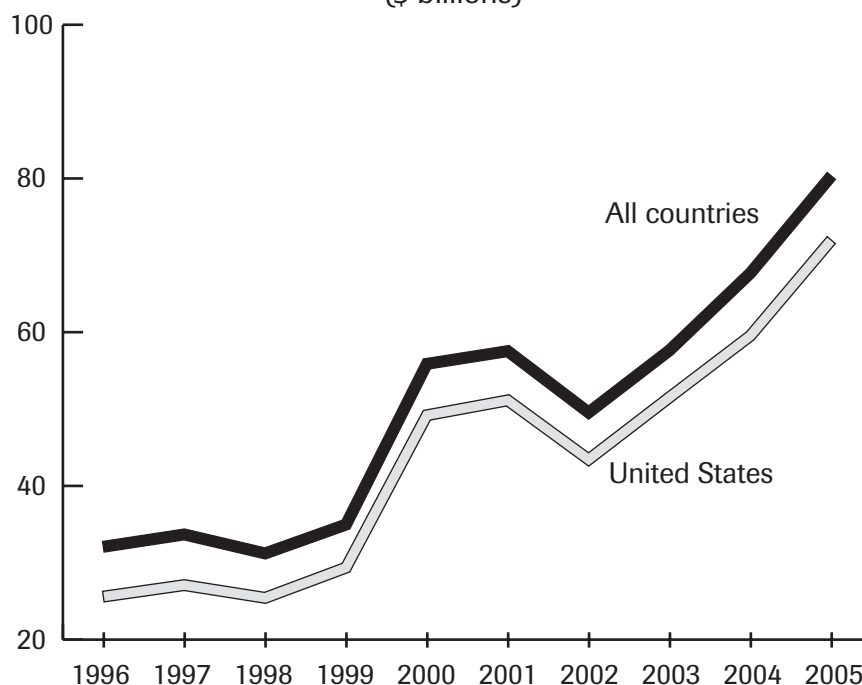
Alberta's international exports reached a record high of \$80.3 billion in 2005, an increase of 18.7% over 2004. The majority of the increase is due to higher oil and natural gas prices. However, a notable rise of 6.5% occurred in the exports of manufactured goods. This compares to only a 1% increase for Canada's overall manufacturing exports over the same period. Unlike the increase in energy commodities, the increased value of manufactured exports was driven by higher volumes, not price.

Exports of manufactured items from Alberta are dominated by chemicals, refined petroleum products, and machinery. Exports of oil and gas field machinery and mining equipment saw an increase of 60% in 2005. Most of this machinery is exported to the US (60%); other major customers include Russia, Iran, Algeria, UAE, Australia, and Sudan.

The double-digit percentage increases in the value of exports from Alberta since 2002 are even more remarkable given the appreciation of the Canadian dollar over the same time period.

Alberta's reliance on the US as an export market has grown steadily over the past decade. In 1996, just under 80% of Alberta's exports were destined for the US; in 2005, this dependence reached nearly 90%.

Figure 7:
International Merchandise Exports From Alberta
(\$ billions)



Source: Industry Canada Trade Data Online

6. Hi-Tech

Alberta's hi-tech sector is a broad category of economic activity that includes electronics and microelectronics, nanotechnology, software development, telecommunications, biotechnology, ag-biotech, and health and medical sciences research.

An important sub-sector of Alberta's hi-tech sector is *Information and Communication Technologies* [ICT], which includes computer equipment and services, software, navigational and medical instruments, semiconductors, and telecommunication equipment and services. ICT in Alberta involves numerous large multinational companies with significant manufacturing operations in the province. According to Alberta Economic Development, there were approximately 7,000 ICT companies operating in Alberta in 2002 generating an estimated \$10 billion in revenues and \$2.5 billion in exports. Employment in ICT totaled 54,500.

Recent concern has been voiced that hi-tech companies in Alberta do not receive sufficient government support. A survey of 128 hi-tech firms in Alberta (conducted by Ernst & Young LLP) suggested that 49% are considering relocating to other provinces that offer more generous tax credits for research and other incentives that help hi-tech companies generate capital. Alberta companies indicate that one of their largest challenges is securing financing from equity markets or governments.

The Alberta government's position has been to shy away from direct tax credits or any other form of assistance that targets specific sectors. However, the government does offer support to hi-tech and bio-tech firms through programs such as Venture Alberta, The Alberta-California Venture Channel, and the Alberta Heritage Foundation for Medical Research Technology Commercialization Program.

The health sciences and biotech sector is another area of hi-tech activity in the province. Some of the leading companies based in Alberta include:

Biomira Inc., a biotechnology company applying its leading technology in immunotherapy and organic chemistry for the development of cancer therapeutics.

Isotechnika Inc., which focuses on novel immunosuppressive therapeutics that are safer than currently available treatments.

Madentec Ltd., which has developed unique software and electronics products that allow persons with physical disabilities to gain productivity and independence.

Micralyne Inc., a developer and manufacturer of BioMEMS and microfluidic components (e.g., innovative silicon chips for drug delivery).

Oncolytics Biotech Inc., which is working towards the use of a viral anti-cancer agent.

priMED Medical Inc., focused on the business of designing, manufacturing, and marketing of wound care and infection and prevention medical supplies.

SemBioSys Genetics Inc., which is working on the development, commercialization, and production of protein-based pharmaceutical and non-pharmaceutical products based on its plant genetic engineering skills and proprietary oilbody-oleosin technology platform known as the Stratosome Biologics System.

Tenet Medical Engineering Inc., a company that designs and develops patient positioning products for surgery and rehabilitation.

Source: Alberta Economic Development, www.alberta-canada.com/biotech/companies.cfm

7. Forestry

Soaring prices for energy, skilled labour, and transportation, coupled with the high value of the Canadian dollar and softer revenues, have painted a gloomy picture for Alberta's forestry sector. Responsible for about \$5.3 billion in total manufactured goods in the province, forestry is a major contributor to the economy.

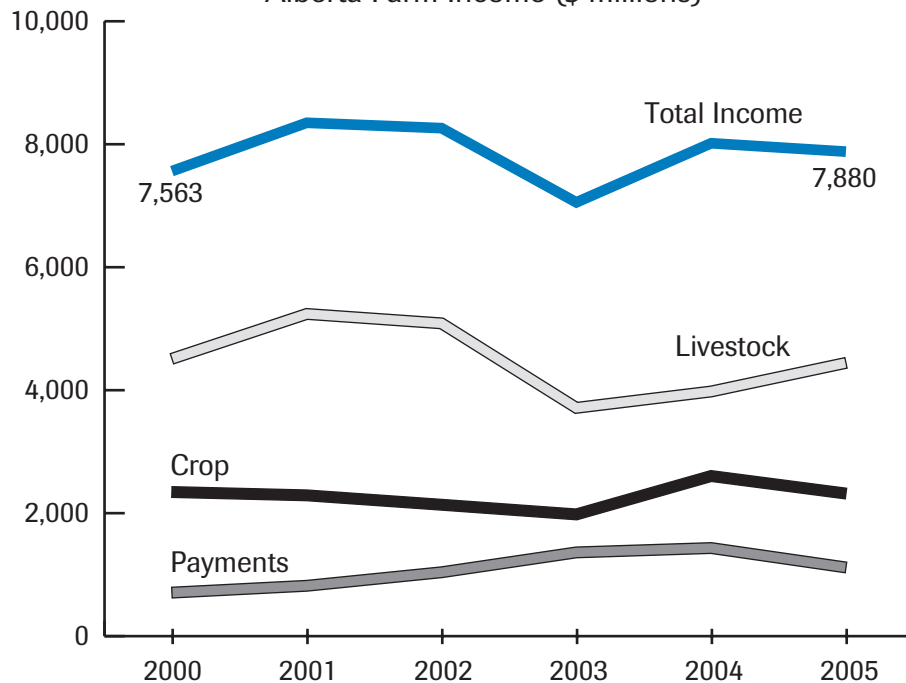
As the Alberta Forest Products Association argues, forestry has been going through some tough times: "The province has lost four lumber sawmills in the past two years: Atlas Lumber in Blairmore; Canfor's lumber mill in Hines Creek; Weyerhaeuser's lumber mill in Grande Cache and Seehta Forest Products' Red Earth lumber mill. Secondary manufacturers are also facing increasing pressures, many to the verge of closing, as was seen with the recent announcement by Sawn Wood Products in Drayton Valley to close its doors. Alberta's pulp mills are also facing significant cost pressures and are struggling to stay competitive in the current global market. The recent announcement at West Fraser's Hinton pulp mill, including decommissioning one pulp line and eliminating 100 permanent jobs, is a direct consequence of the competitiveness pressures felt by the industry." (Alberta Forest Products Association News Release, April 4, 2006.)

The outlook for 2006 is not much better. The expectation of higher interest rates in the US—and the resulting higher mortgage costs—are likely to dampen the American housing market. The Canadian dollar is also expected to remain strong, and there is little optimism that the ongoing softwood lumber trade dispute between Canada and the US will be resolved any time soon.

8. Agriculture

Alberta farmers received marginally less income in 2005 due primarily to lower crop income and fewer direct payments from insurance and government assistance programs (see Figure 8). However, livestock receipts grew by nearly half a billion dollars to \$4.4 billion—an increase of 12% over 2004. This reflects the resumption of trade in live cattle with the US and gradually strengthening cattle prices.

Figure 8:
Alberta Farm Income (\$ millions)



Source: Statistics Canada CANSIM Table 002-0002

Farm income is not likely to increase significantly in 2006. Prices for wheat, barley and canola are forecast to remain flat this year; livestock prices are expected to remain flat or fall. Crop growing conditions will be dictated by spring and summer moisture levels. According to an Agriculture and Agri-Food Canada forecast issued March 1, 2006, much of Alberta's crop producing areas are expected to receive below normal moisture for the spring period, especially in areas north of Edmonton and in the southern part of the province. Temperatures are also expected to be cool. (Source: www.agr.gc.ca/pfra/drought/spring2006_e.htm)

Figure 9:
Agricultural Prices and Price Forecast

	Wheat (\$US/tonne)	Barley (\$US/tonne)	Canola (\$US/tonne)	Cattle (US cents/lb)	Hogs (US cents/lb)
2000	147.08	145.33	185.25	70.3	61.1
2001	151.53	144.90	211.31	72.9	61.3
2002	176.07	159.31	253.45	68.7	48.1
2003	177.49	178.80	271.75	83.1	55.9
2004	186.49	155.19	283.48	84.3	70.1
2005	197.62	153.26	237.49	87.5	68.5
2006 (f)	198.76	156.59	238.75	86.4	60.8

Source: TD Economics, TD Commodity Price Report, March 15, 2006

9. Construction and Capital Investment

Private and public sector investment—both in terms of construction activity and investment in machinery and equipment—is expected to increase by 9.5% in 2006 to just over \$66 billion. Investments in the oil sands alone are expected to total nearly \$10 billion. Building permits for both residential and non-residential projects are already showing strong increases over the very high levels of activity posted in 2005. During the first two months of 2006, the value of building permits issued increased by 38%. Residential housing projects, which account for 70% of the value of building permits issued, are up 54% over the same two-month period in 2005.

Figure 10:
Alberta Private and Public Investment, and Investment Intentions for 2006
(\$ millions)

	Construction	Machinery & Equipment	Total	annual % change
2004 (actual)	33,991.7	16,816.0	50,807.7	--
2005 (estimate)	42,161.7	18,155.2	60,316.9	18.7
2006 (intentions)	47,879.9	18,143.7	66,023.6	9.5

Source: Statistics Canada, Private and Public Investment, The Daily, Feb. 23, 2006

Figure 11:
Value of Building Permits, Alberta
(seasonally adjusted, \$ millions)

	Jan-Feb 2005	Jan-Feb 2006	% change
Total	1,442.6	1,990.8	38.0
Residential	909.7	1,400.7	54.0
Non-Residential	532.9	590.1	10.7
Calgary	497.2	744.1	49.6
Edmonton	407.2	547.2	34.4

Source: Statistics Canada, The Daily, April 6, 2006

Figure 12:
Total Housing Starts, Alberta

2005 (actual)	40,847
2006 (forecast)	39,500
2007 (forecast)	37,500

Source: CMHC Housing Market Outlook, First Quarter 2006

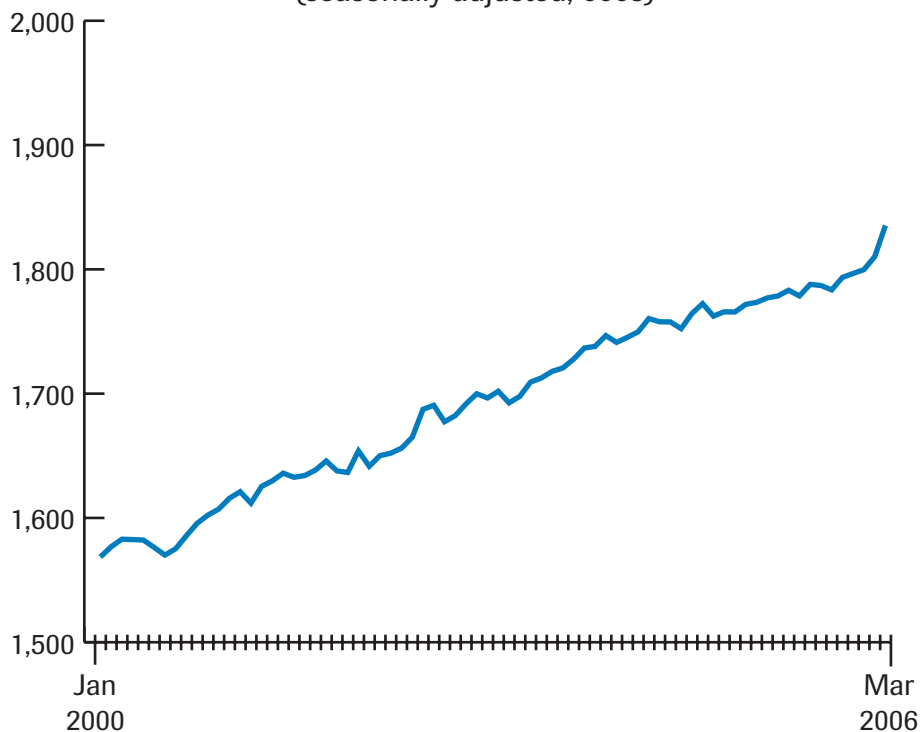
Alberta housing starts totaled 40,847 in 2005, their highest level since 1978. Housing starts in the province are forecast to remain very strong throughout 2006 and 2007, prompted by a very vibrant job market and the continued in-flow of workers from other parts of Canada. The combination of a strong job market and population growth will keep total housing starts strong at an estimated 39,500 units in 2006 and 37,500 units in 2007. With mortgage rates rising only moderately, the largest factor holding back gains in housing starts will be labour and material shortages.

10. Labour Market

Employment in Alberta edged up in March 2006 by 6,600 (seasonally adjusted), bringing gains in the past year to 65,000 (+3.7%). Over the last 12 months, employment gains were concentrated in the construction sector, professional, scientific and technical services, public administration, and natural resources. The unemployment rate in March 2006 was 3.4%, the lowest in the country.

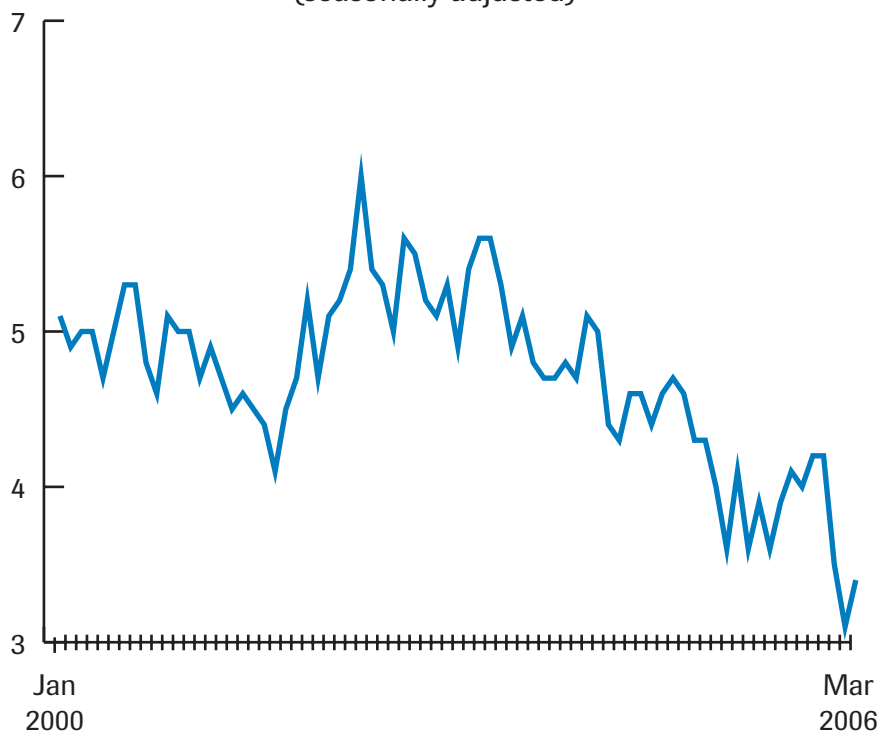
Regionally, the strongest gains in employment came in the Athabasca-Grande Prairie-Peace River area with an increase of 8.1%. This is not surprising given the heated economic activity surrounding oil sands project construction and operation.

Figure 13:
Employment in Alberta, January 2000-March 2006
 (seasonally adjusted, 000s)



Source: Statistics Canada CANSIM Table 282-0087

Figure 14:
Unemployment Rate in Alberta, January 2000-March 2006
(seasonally adjusted)



Source: Statistics Canada CANSIM Table 282-0087

A shortage of labour in Alberta is the most pressing economic problem at the moment. Even with the large in-flow of population into the province (see section 11 below), employers are still finding it very difficult to find workers. While the situation in 2004 could have been described as a shortage of *skilled* workers, the situation in the spring of 2006 is characterized by a *general* shortage of labour—both skilled and unskilled.

Figure 15:
Top 10 Job Vacancies in Alberta, 2005

Occupational Group	Estimated Job Vacancy Rate*	Average Annual Salary (\$)
Professional Occupations in the Physical Sciences	17.7	79,130
Structural Metal and Platework Fabricators and Fitters	13.2	44,806
Oil and Gas Drilling, Servicing and Related Labourers	9.7	46,990
Food Service Supervisors	9.4	16,311
Glaziers (i.e., window making and installing)	8.8	33,889
Cooks	8.6	19,305
Maitres d'hotel and Hosts/Hostesses	8.3	9,115
Cashiers	7.8	18,761
Automotive Service Technicians	7.8	48,687
Other Medical Technologists and Technicians	7.7	61,047

*The job vacancy rate is the total number of job vacancies unfilled for 4 months or longer divided by the sum of all job vacancies and the number employed.

Source: Alberta Human Resources and Employment, 2005 Annual Alberta Labour Market Review, March 3, 2006

Figure 16:
Increases in Hourly Wages, Alberta
February 2005 to February 2006

	% change
ALL OCCUPATIONS, workers 15 years and over	6.1
Management occupations	7.9
Business, finance and administrative occupations	4.4
Natural and applied sciences and related occupations	4.9
Health occupations	4.4
Occupations in social science, education, gov't service and religion	-0.3
Occupations in art, culture, recreation and sport	5.0
Sales and service occupations	6.9
Trades, transport and equipment operators and related occupations	4.3
Occupations unique to primary industry	17.3
Occupations unique to processing, manufacturing and utilities	6.7

Source: Statistics Canada, CANSIM Tables 282-0069 and 282-0073

This labour shortage is having some direct negative impact on the provincial economy. Some estimates suggest that because of the present tightness, the growth in provincial GDP will be shaved by as much as 1 percentage point. Anecdotal stories about how shops and companies are turning away business opportunities simply because there is not enough labour.

According to Alberta Human Resources and Employment, job vacancies are most acute in professional occupations in the physical sciences (which includes metallurgists, soil scientists, and physical science occupations). But the shortages are also very pronounced across a wide

swath of the Alberta economy in occupations ranging from the oil patch to the food and hospitality sector. They are also spread across a wide range of pay scales.

As a predictable result of the shortage of workers in Alberta, wages have been rising. Overall, hourly wages in the province have risen by 6.1% (February 2006 over February 2005). This compares to a national wage increase of 3.3% over the same time frame. The strongest wage gains have come in occupations unique to primary industry, reflecting once again the very active oil and gas sector.

11. Interprovincial Migration and Population Growth

Alberta's population reached 3,306,359 on April 1, 2006—an annual increase of 2.48%. This was the fastest rate among all of the provinces, and 2.5 times the rate of growth posted nationally (0.98%).

Much of this population growth is attributed to positive net interprovincial migration. During 2005, Alberta saw a net increase of 41,700 people from other provinces. This was the ninth consecutive year for which Alberta has posted the largest gain in interprovincial migration in Canada.

In the fourth quarter of 2005 alone, the province saw 24,997 interprovincial migrants (17,059 net gain). Most of these new-comers arrived from Ontario (6,625), BC (6,553) and Saskatchewan (3,593).

Net international migration in 2005 was far less at 14,377. The provincial government is taking some important steps to address the shortage of skilled labour. In October 2005, Economic Development Minister Clint Dunford announced a plan to increase annual international immigration to the province to 24,000 to help deal with the labour crunch. The province also wants to improve the processing time for foreign-credential recognition and offer more training to address skill gaps and enhance language training.

12. Public Finance

On March 22, 2006, the provincial government brought down its budget for the 2006/07 fiscal year. Alberta's unique situation of having no outstanding provincial debt and massive royalties from non-renewable resources has put the government in a very comfortable and enviable position.

Total provincial program expenditure is forecast to rise by 8.3% to just over \$28.4 billion (excluding unforeseen spending on disaster relief, forest fires, prosperity cheques, new infrastructure projects, and other ad hoc uses of surplus revenue).

New base operating spending will go largely to the following areas:

- Advanced Education (+16%)
- Education (+ 5.1%)
- Health and Wellness (+7.5%)
- Seniors and Community Supports (+9%)

Total revenue is forecast at \$32.4 billion—about \$2.1 billion less than 2005 because of conservative natural resource revenue assumptions. Taxes are coming down by a small amount. The basic, spousal and eligible dependant tax credit is being raised to \$14,899 (up \$376 from 2005), saving Albertans an estimated \$77 million. Health care insurance premium subsidy thresholds are being raised by \$5,000. The general corporate income tax rate will be reduced from 11.5% to 10%. Finally, school property tax mill rates are being reduced by 7%.

The forecast surplus of \$4.1 billion will be allocated to savings (including \$1.9 billion to the Heritage Fund, the new Alberta Cancer Prevention Legacy Fund and the Medical Research Endowment Fund), capital investment (\$813 million), the Sustainability Fund (\$325 million), and contingency allowances (\$300 million).

There has been considerable concern raised in the province about the scope of spending increases announced in the budget. While the debt-free status of the province and high energy prices are keeping the province in the black, there are some fears expressed that the government has lost control of its spending. University of Alberta economist Paul Boothe has argued that, if program spending continues to increase at this same rate—and energy prices are stable or somewhat lower—the province will be in a deficit situation in 3-5 years.

13. Conclusion

Energy prices and the activity surrounding oil, gas and oil sands projects will continue to push Alberta's economy ahead in 2006 and 2007. Notwithstanding the notorious volatility of energy prices, there is a general consensus that prices are not likely to collapse to their pre-2000 levels any time soon.

Heavy migration to the province will provide much of the impetus for strong housing starts, retail sales, and demand for personal and business services. High levels of provincial government spending—the highest of all provinces on a per capita basis—will add to overall demand.

Given this heated economic scenario, it is surprising that general inflation in Alberta has yet to emerge. While annual wage inflation (+7.0% on hourly wages) has certainly boosted consumer spending (+16.7 annually), annual inflation, as measured by the Consumer Price Index, was up only 3.3% in February. While this is higher than the national average (+2.2%), it is still relatively low.

Labour shortages will continue to be the most serious impediment to economic growth in 2006. Positive international and interprovincial migration to the province will help meet employers' needs, as will increased investment by the government in post-secondary training and skills development. However, labour shortages will act as a natural braking mechanism on the economy, preventing run-away economic growth that could be difficult to contain. It is questionable if real GDP growth of 7-10% is desirable given the probabilities of over-strained infrastructure, inflation, severe housing shortages, and environmental degradation.

The Canada West Foundation is forecasting real GDP growth of 5.2% for 2006 and 4.7% for 2007. 

About the Canada West Foundation

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A dynamic and prosperous West in a strong Canada.

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In 1970, the One Prairie Province Conference was held in Lethbridge, Alberta. Sponsored by the University of Lethbridge and the Lethbridge Herald, the conference received considerable attention from concerned citizens and community leaders. The consensus at the time was that research on the West (including BC and the Canadian North) should be expanded by a new organization. To fill this need, the Canada West Foundation was created under letters patent on December 31, 1970. Since that time, the Canada West Foundation has established itself as one of Canada's premier research institutes. Non-partisan, accessible research and active citizen engagement are hallmarks of the Foundation's past, present and future endeavours. These efforts are rooted in the belief that a strong West makes for a strong Canada.

More information can be found at www.cwf.ca.



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