Alberta's Economic Update

and how to strike a balance between the economy and the environment in Canada

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Outline

- **About The Conference Board of Canada** and Our Work
- **Macroeconomic Roundup**
  Global, United States (U.S.), and Canada's economic outlooks
- **Alberta's Economic Outlook**
  Labour markets / consumers, investment, and trade.
- **An Energy Perspective on Sustainability**

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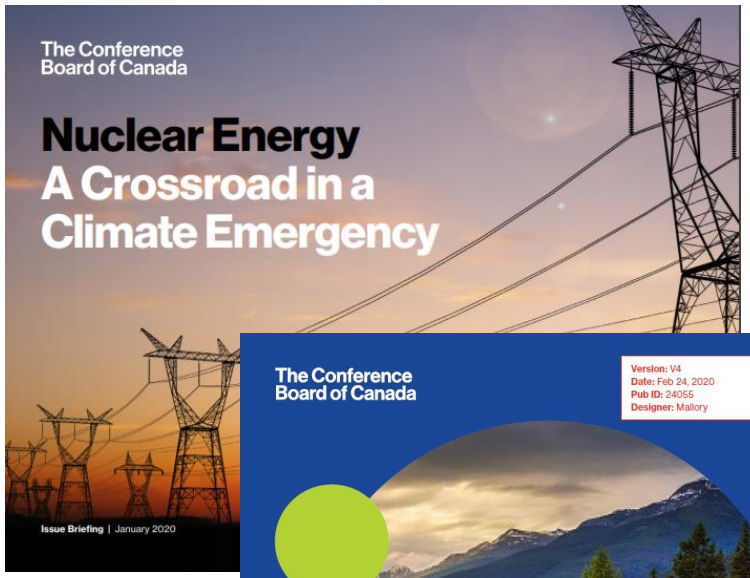
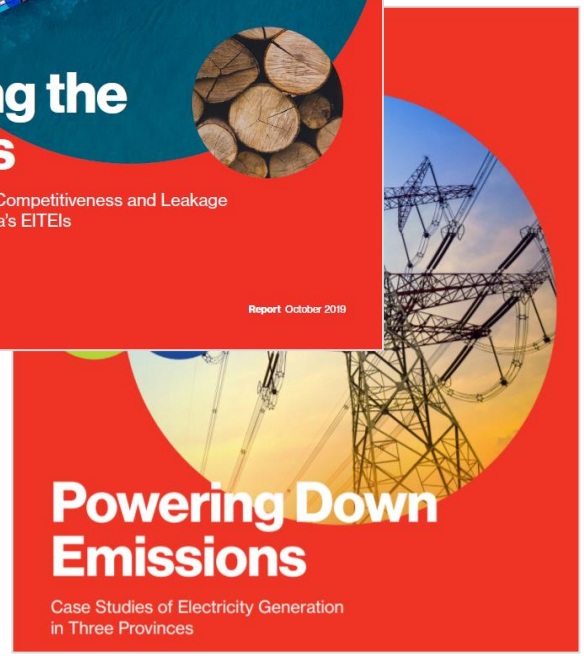
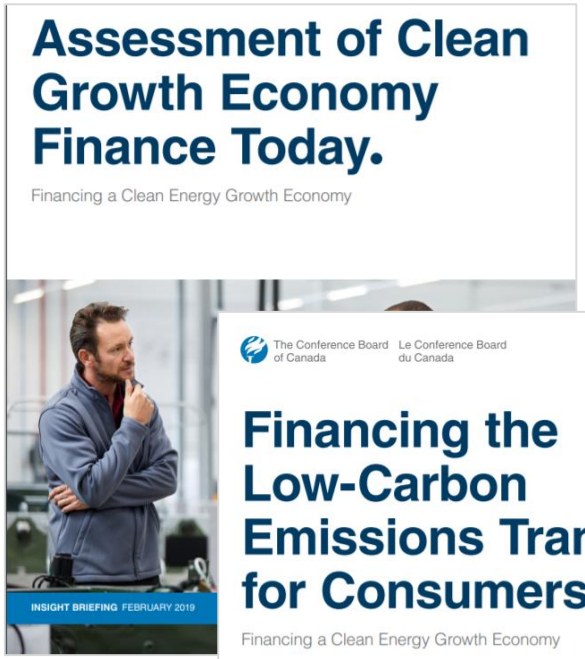
Our operating principles: evidence-based, systems-driven, and practical approach to research; inclusive engagement, and; independent / objective and non-partisan thought leadership.

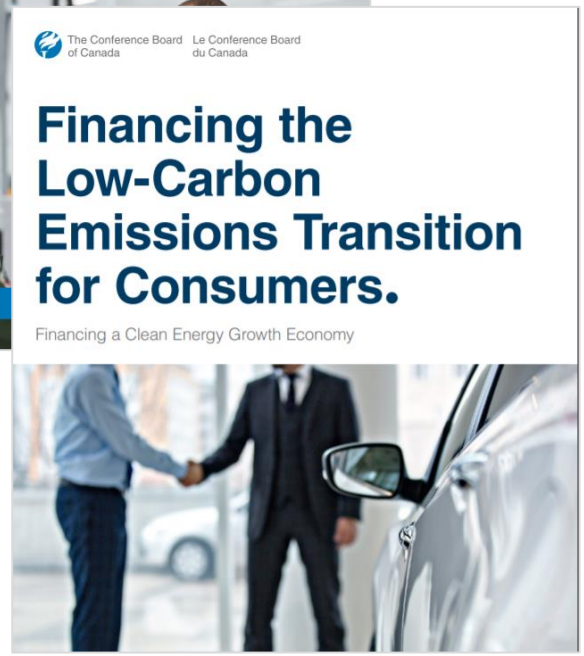
Our funders: some of Canada's largest energy companies and financial institutions.

A sample of our recent work at CEGE









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Macroeconomic Roundup

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Key Takeaways

- **Global economic growth** is currently at its slowest since the global financial crisis. Concerns about trade conflicts (e.g., US-China, Brexit, etc.) have eased – but have already taken a toll on global business investment, industrial output, and trade flows. Growth is expected to pickup in 2020-21, but various known and unexpected risks (e.g., COVID-19) will likely change that.
- **U.S. economy** is on a slowdown trajectory but far off from a recession. Impact of trade wars is less severe that in other areas of the world and so far impacting mainly businesses, not consumers. Phase I deal with China is good news – but far off from a complete and viable solution to trade disputes.
- **Canadian economy** is performing OK. Households are supporting growth. Business investment and export growth outside the energy sector are needed. We might see an uptick in federal spending. Economy is being impacted by weak global growth and recent events pose downside risks to the outlook.

Global macroeconomic environment

A slowdown is evident. A rebound is anticipated – but downside risks abound.

Global gross domestic product (GDP) growth in 2019: 2.9 per cent

- Slowest pace of growth registered since the 2008-09 financial crisis
- Significant broad-based slowdown in growth relative to 2018 (3.6 per cent)
- Key factors: trade barriers, social unrest, geopolitical tensions

IMF's global GDP forecast for 2020-21: 3.3 – 3.4 per cent

- Growth stabilization / rebound driven by recovery in emerging economies ▲
- Advanced and major economies continue on a slowdown trajectory ▼
- Trade tensions easing – but various downside risks remain (e.g., social unrest). IMF projection was also completed prior to COVID-19 outbreak !

All figures from latest version of the International Monetary Fund's (IMF) World Economic Outlook (WEO)

COVID-19 Outbreak

Global economy faces a broad range of direct and indirect (i.e., supply-chain) impacts:

- **Direct impact** on China's economy through **production shutdowns** and **pause in consumer spending**
- **Weaker transportation fuel demand** (incl. gasoline, diesel, jet fuel) has lowered oil prices
- **Global tourism spending** will take a hit
- **Foreign affiliate sales** affected. **Chinese imports** will also suffer
- Impact on **global supply chain** will be noticeable (Apple, Nissan, Hyundai)
- If outbreak is not contained (as expected) **fear factor could exacerbate** slowdown

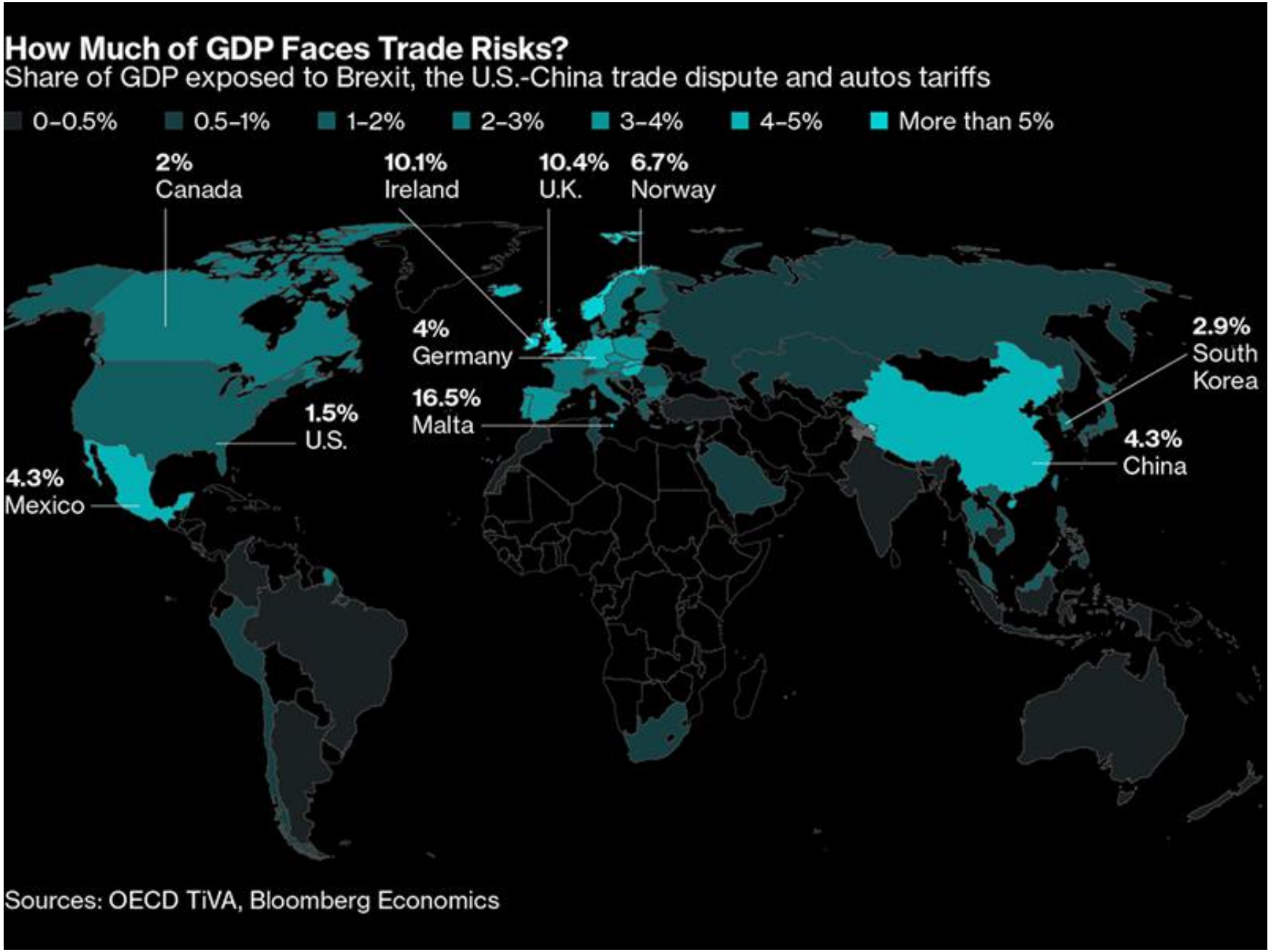
Trade wars' impact on the global economy

1) **Trade wars= policy uncertainty ▲**
   business confidence **▼ → business investment ▼**
2) **Tariffs= input costs ▲ + supply-chain disruptions ▲**
   manufacturing output **▼ → trade ▼**

(1) + (2) = Business investment ▼ + trade ▼ = global output ▼ commodity prices ▼ and global GDP ▼

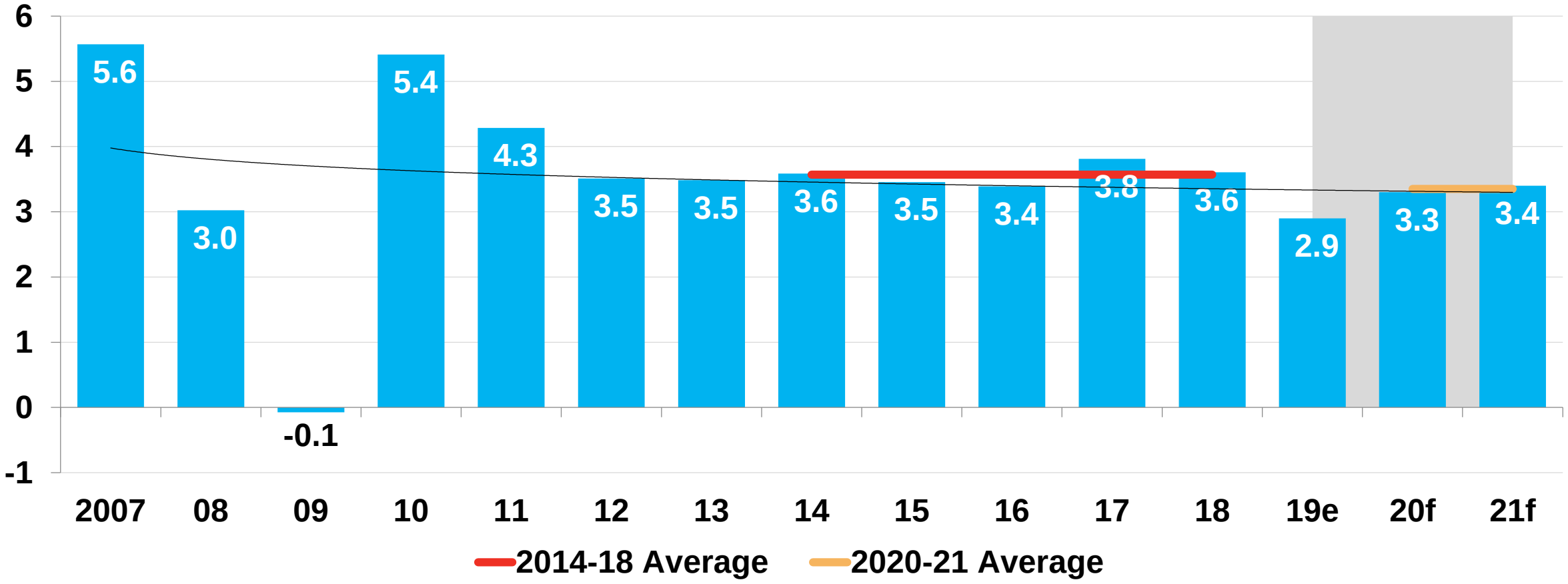
To date, impacts appear to be **concentrated on businesses**, not on consumers – i.e., on intermediate inputs, not on final goods.

Impacts **are widespread –** due to global integration of supply-chains and because of multiple trade disputes taking place.


How Much of GDP Faces Trade Risks?
Share of GDP exposed to Brexit, the U.S.-China trade dispute and autos tariffs
0–0.5%
0.5–1%
1–2%
2–3%
3–4%
4–5%
More than 5%
2%
Canada
10.1%
Ireland
10.4%
U.K.
6.7%
Norway
4%
Germany
16.5%
Malta
1.5%
U.S.
4.3%
Mexico
2.9%
South Korea
4.3%
China
Sources: OECD TiVA, Bloomberg Economics

After 2019's slowdown, global economic growth may recover to the 3.3 per cent mark – that is below recent historical performance, but consistent with a long-term deceleration trend

year-over-year (y/y) change in global economic growth, per cent



e= estimate; f=forecast

Sources: The Conference Board of Canada; IMF

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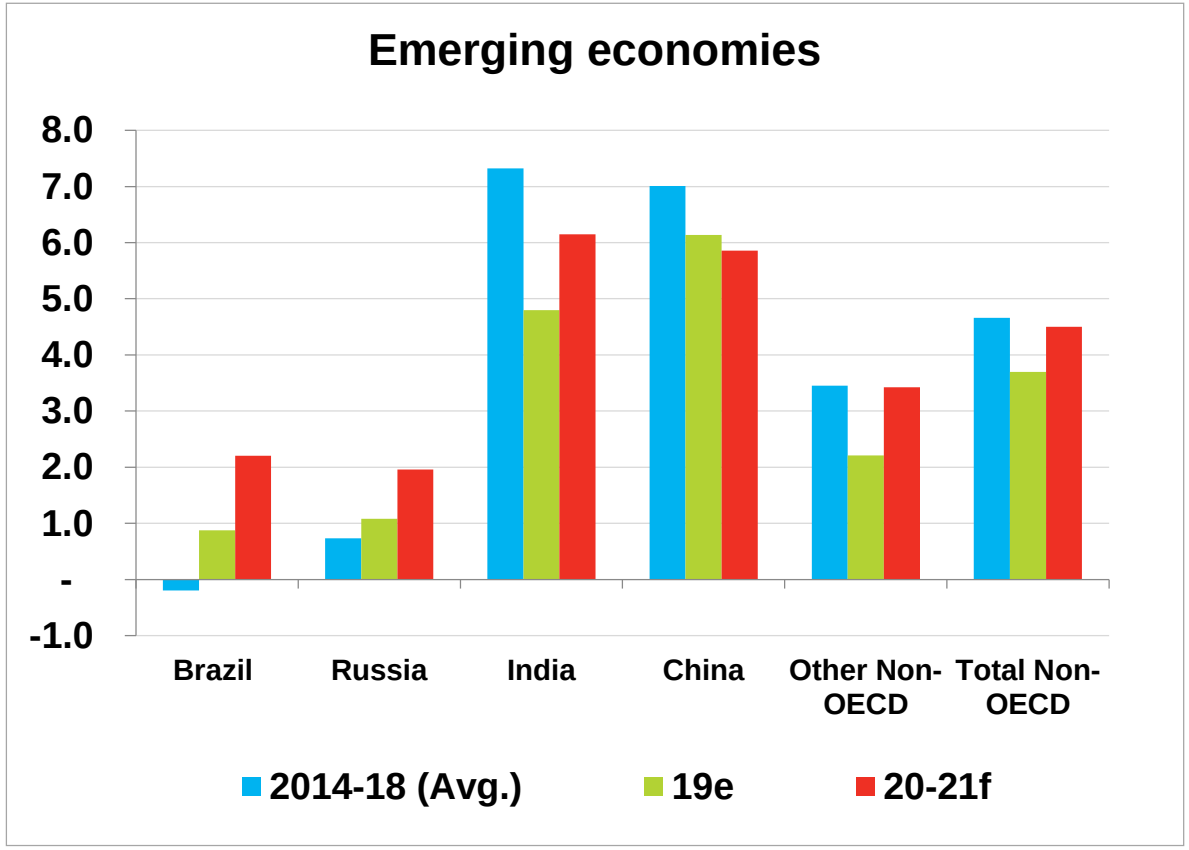
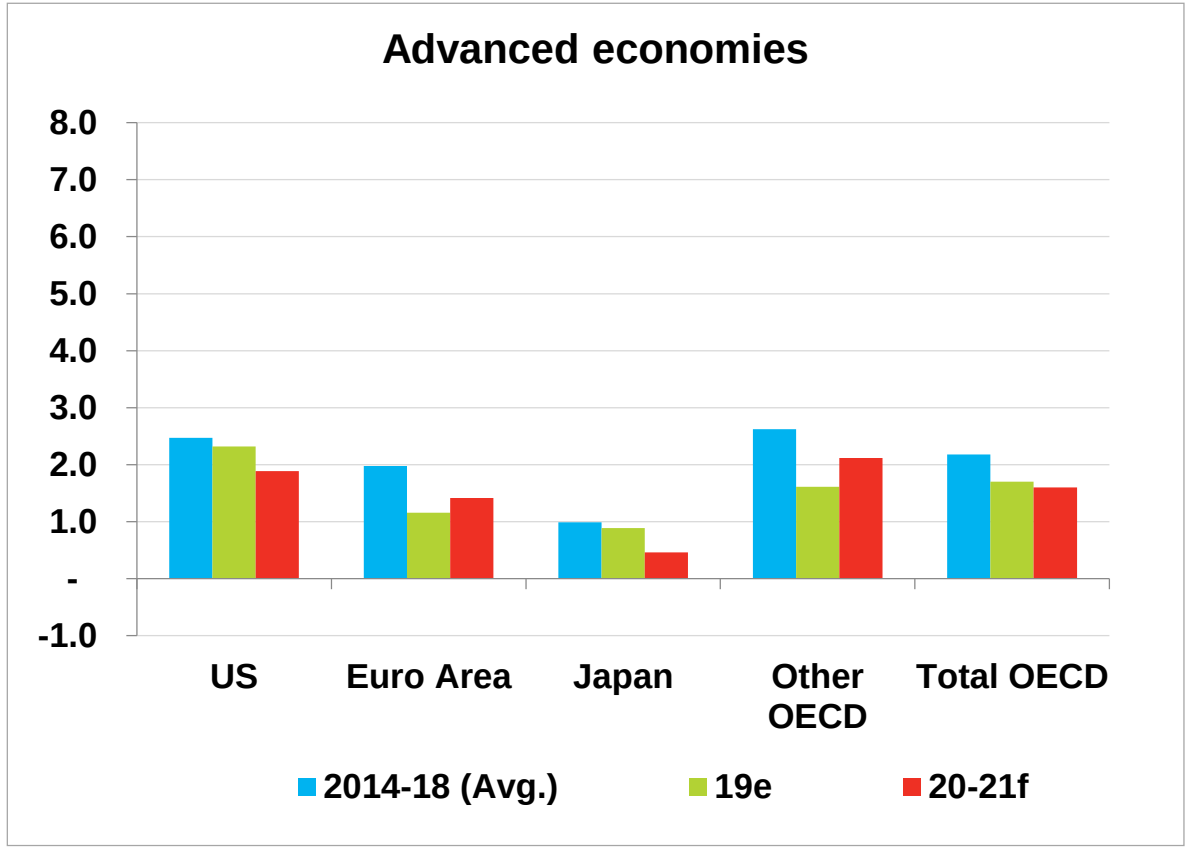
Emerging economies drive global growth rebound, while advanced economies continue on slowdown trajectory – differences are apparent within groups

y/y change in economic growth by region, per cent





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Sources: The Conference Board of Canada; IMF

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U.S. Economy

Growth slowdown trend is evident since mid-2018 – expected to bottom-out by late 2020

2019 GDP growth: 2.3 per cent

- Slowest growth pace since 2016 and well below that of 2018 (2.9 pc) – still, 10th straight year of economic expansion (2nd longest in recent U.S. history)
- Driven by growth deceleration in business investment (significant) and consumer spending (gradual)

2020-21 GDP growth: <2 per cent

- Continued slowdown from consumer spending and growing trade deficits
- Tempered by expected pickup in business and government investment

Trade War Averted, but Tariffs Remain

- **Phase I of the U.S.-China trade deal provides relief – but much remains unsolved. It is a deal for things not to get worse**

- The deal halves tariff rates on $120 billion worth of goods, **but most of the higher duties which affect another $360 billion of Chinese goods and more than $100 billion worth of countervailing tariffs on U.S. exports remain**

- China commits to boost U.S. imports of manufactured products, services, agriculture, and energy from 2017 levels by $200 billion over two years. **This requires a doubling of these U.S. exports to China**

- Some **concessions** from China to enforce theft of IP, especially in pharmaceuticals. **Sticking points** around Chinese subsidies for SOEs and cyber security remain

Impact of Trade Wars on the U.S. Economy

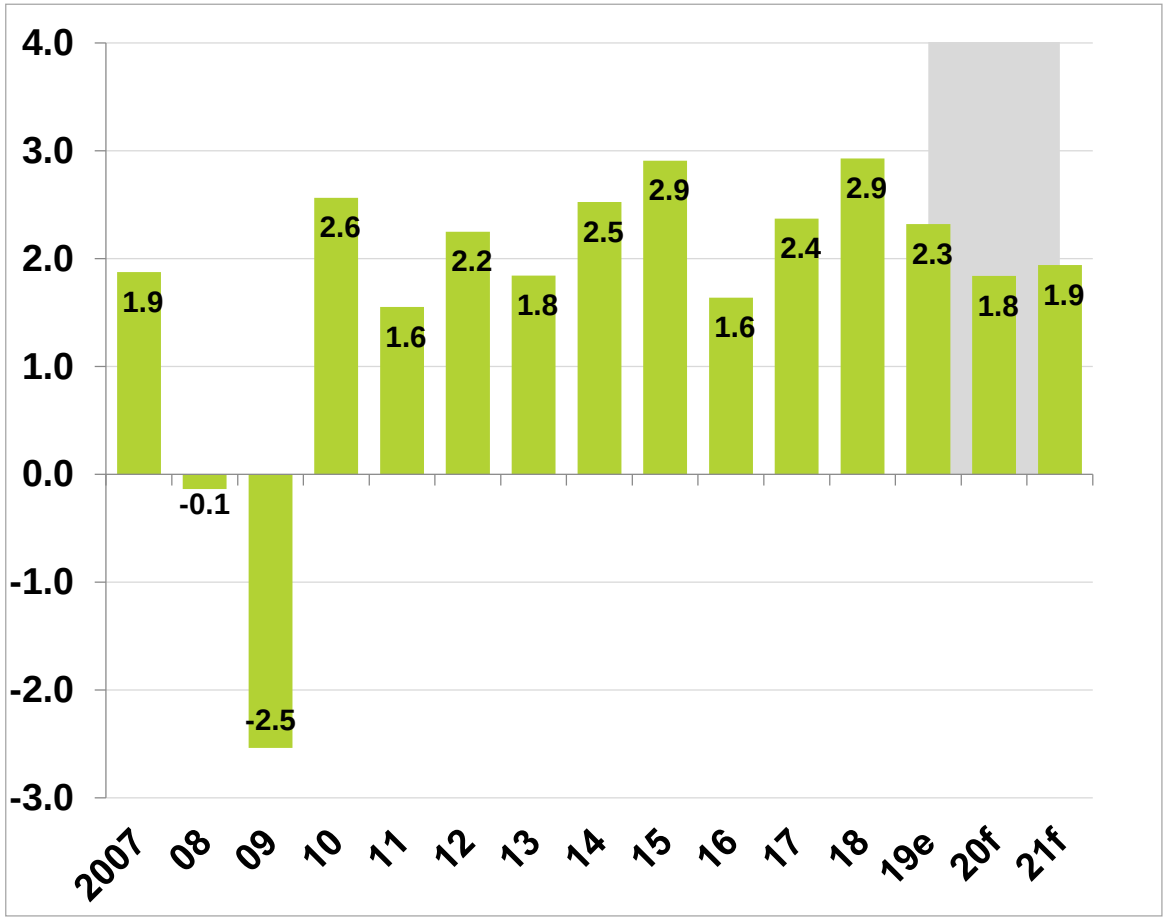
Limited impact to date relative to other regions of the world – since trade is not a significant component of U.S. GDP
(e.g., exports/GDP: 13 per cent in U.S.; 32 pc in CAD; 62 pc in AB)

Estimated long-term impact on U.S. economy (depending on escalation): -0.2 to -0.7 per cent **on GDP growth;** 200k-500k **job losses**, and; U.S. $100-$200 billion in **government revenues**.
(Based on Bloomberg and The Tax Foundation)

Stateside, **higher costs of imported goods mainly borne by businesses**. **Retaliatory tariffs** have hit **American farmers** and **U.S. companies operating in China**.

U.S. GDP continues on a slowdown trajectory but unlikely to go into recession – as some predict

y/y change on U.S. real GDP, per cent



e= estimate; f=forecast

Sources: The Conference Board of Canada; U.S. Bureau of Economic Analysis (BEA)

Consumers: 2/3rds of U.S. final demand

- Healthy labour markets support spending. But, a slowdown in hiring + a plateauing of wages + increased savings rate = spending slowdown

Business investment: 17 pc of U.S. final demand

- Residential: supported by low mortgage rates and high demand
- Non-residential: negatively impacted by uncertainty, but supported by low interest rates

International trade: trade deficits persist and are actually growing (net imports: U.S.$1 trillion)

Government spending: ramping up despite U.S.$1 trillion-level deficits

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Canada's Economic Outlook
Five key takeaways

LABOUR MARKET IS PERFORMING VERY WELL

INCOME GROWTH IS BOOSTING CONSUMER SPENDING

CANADA IS IMPORTING WEAKER GROWTH

BUSINESS INVESTMENT REMAINS WEAK

CAN GOVERNMENT BOOST GROWTH?

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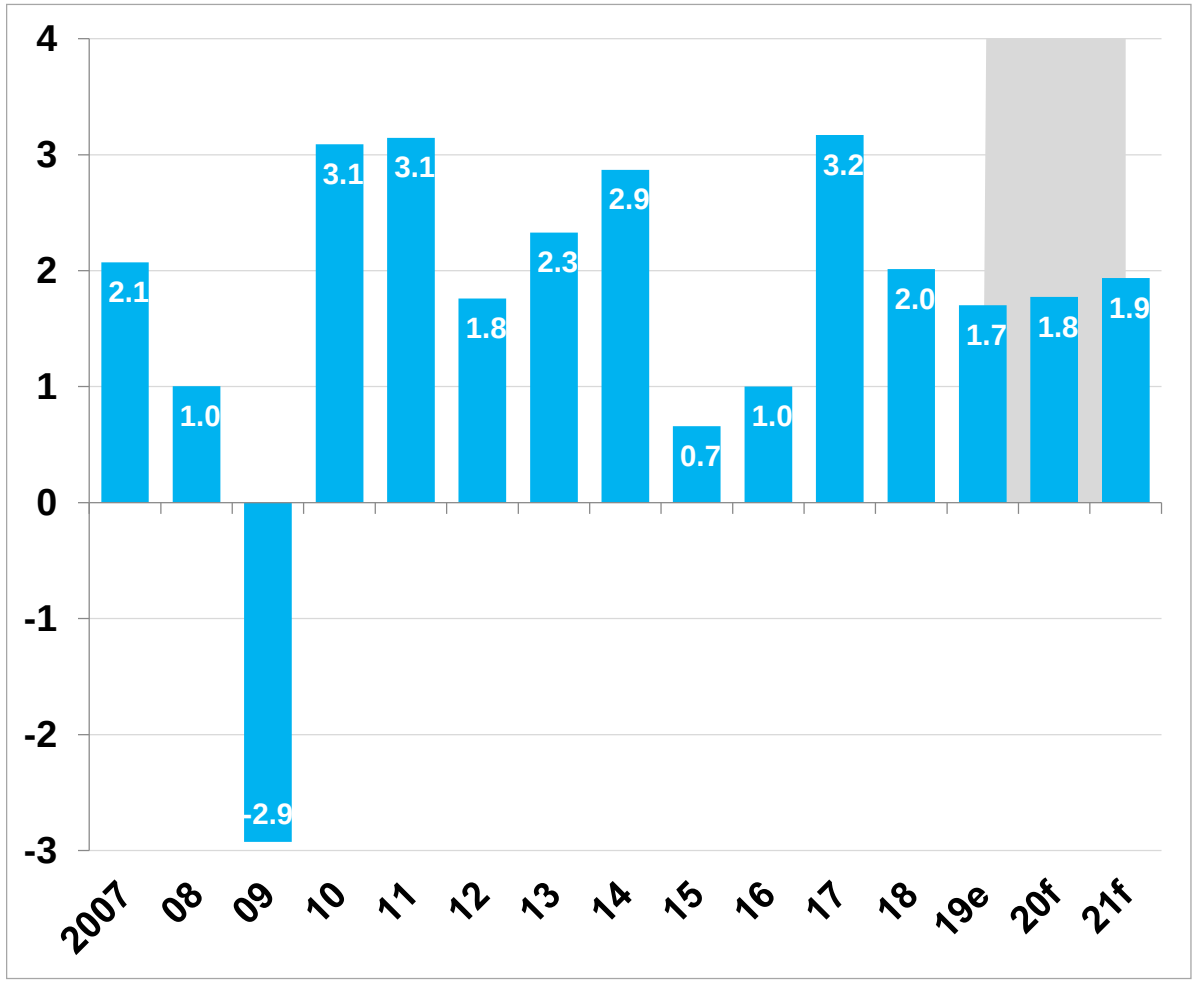
Canada's economic performance: 2018's slowdown continued into 2019, small rebound expected in 2020-21

y/y change in real GDP, per cent



e= estimate; f=forecast

Sources: The Conference Board of Canada; Statistics Canada

Consumer spending

- Growth slowed down in 2019, but expected to pickup slightly in 2020-21: supported by strong labour markets, wage gains, low interest rates, and moderate inflation.

Business investment: No growth in 2019. Fifth-straight year of lackluster growth / decline.

- Residential: picking up again – population and employment growth + low mortgage rates.
- Non-residential: Other sectors are not picking up slack from energy sector. Some rebound in energy

Net Trade: small positive contribution to GDP growth

- Good news: CUSMA / Bad news: global uncertainty + weak U.S. growth
- Net trade vol. growth: mainly from energy products

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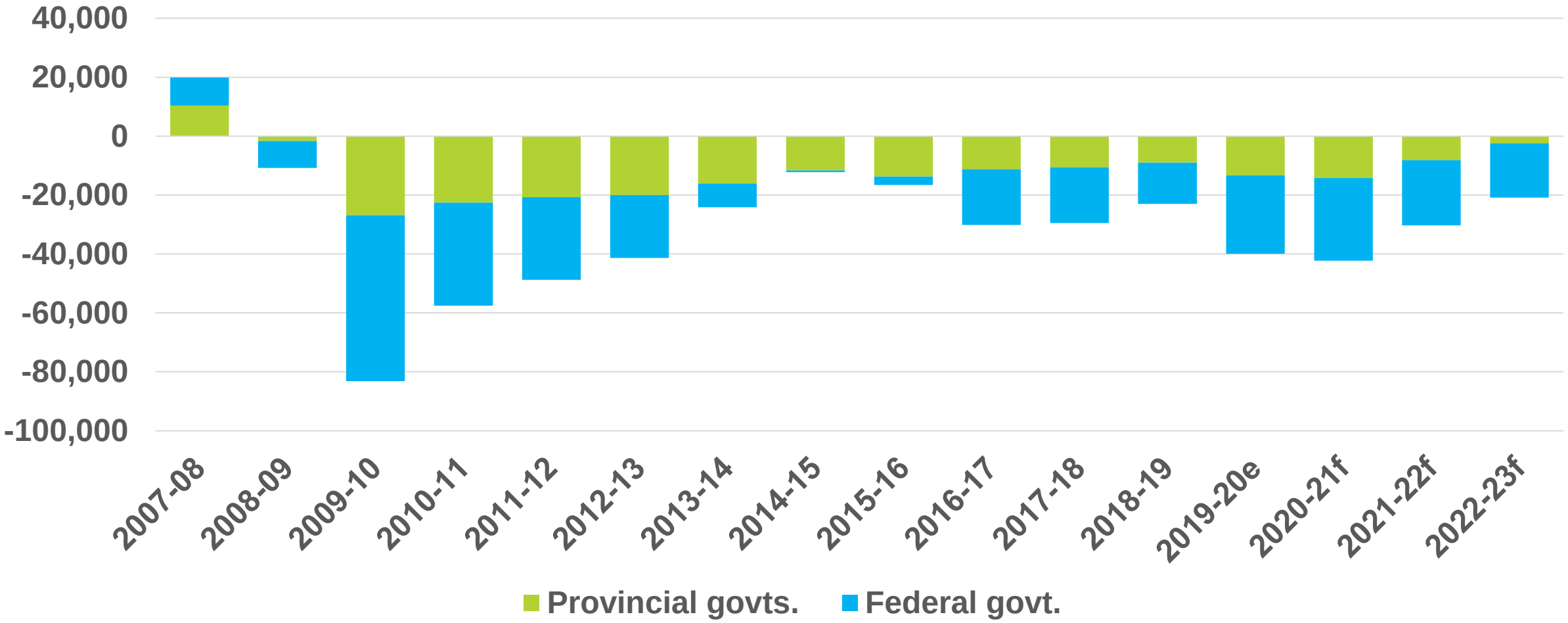
Can Government Boost Growth?

federal and provincial deficit billions of current $



e= estimate; f=forecast

Sources: The Conference Board of Canada; Provincial Governments, Statistics Canada

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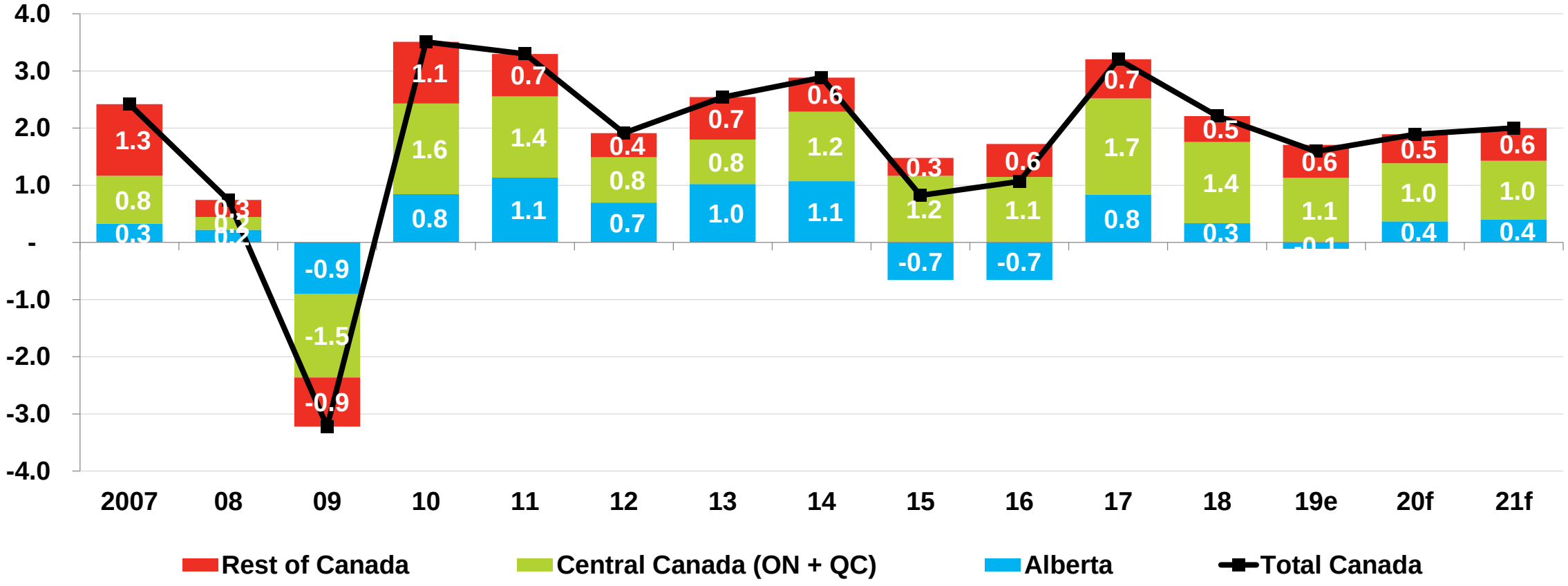
Performance of regions across the country impact Canada's economic growth

Contribution to Canada's GDP annual change, by region, percentage points



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The bottom line on Canada's economy

- Canada's economy continues to be propped up by household spending
- Tight labour market will be a challenge for employers and tax competitiveness (relative to the U.S.) is not favourable
- Stronger business investment and non-resource exports will be needed to sustain growth into next year
- Geopolitical risks remain high; U.S.—China trade continues to add downside risk. Length of Coronavirus impact is a big unknown. Rail blockades add to uncertainty and downside risks to the outlook.

Potential impact of COVID-19 and rail blockades on Canada's economy

COVID-19

- **Direct hit on tourism:** China accounts for 7 per cent of tourism spending in Canada (BC, PEI, and others)
- **Direct hit on exports to China:** e.g., fresh lobster in Atlantic Canada
- **Indirect hit via lower commodity prices** (e.g., oil, iron, copper, lumber) and **disrupted supply-chains**

Rail blockades

- Immediate: disruption of **supply-chains** and **delivery of final goods** across Canada and North America.
- Long-term: **impact on business investment decisions** – particularly on infrastructure and natural resource extraction projects

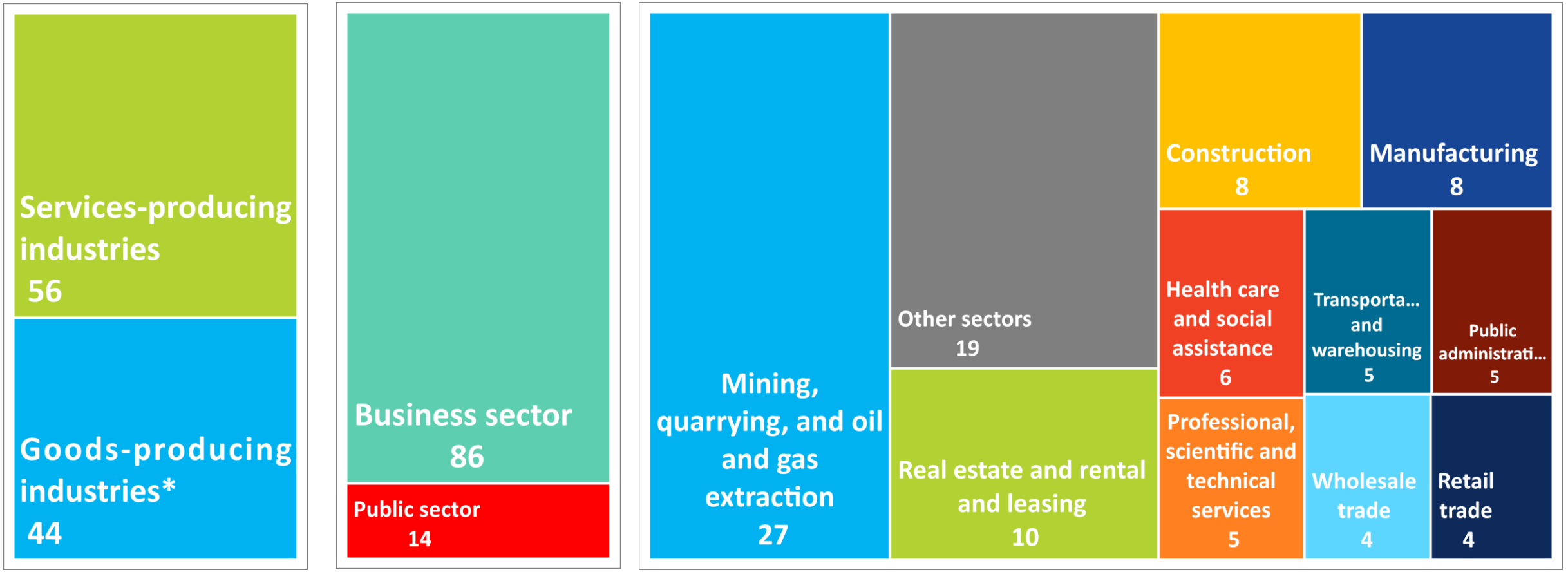
Alberta's Economic Outlook

Key Takeaways

- **Alberta's economy contracted in 2019**. Business and government investment were the main drag factors. Export growth is decelerating – in part due to impact of government policies.
- **A structural change in global oil markets is having a long-lasting impact on Alberta's economy**. Not until 2020 are we expected to get back to the level of economic activity recorded in 2014 (i.e., previous peak). Growth will be slower going forward, expectations need to be revised.
- **Province is transitioning** from investment-driven to export-driven growth. Consumer spending is steady. Investment remains the main "swing factor".
- **Improving economic prospects are dependent** on higher commodity prices and the completion of incremental pipeline projects.

Alberta's Economic Structure: A goods-driven economy, with a small public sector and large dependence on resource extraction and construction

Alberta's gross domestic product (GDP) by industry type (left), ownership model (middle), and by major sub-sector (right), per cent of total for 2018



**includes agriculture, mining (incl. oil and gas), utilities, construction, and manufacturing industries.*

Source: The Conference Board of Canada; Statistics Canada

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Alberta's Economy – small contraction registered in 2019

GDP growth in 2019: -0.2 per cent

- **Growth contracted** in two non-consecutive quarters: *recession?*
- **Business investment contracted for fifth-straight year** and it is still over 40 per cent below 2014's peak levels
  - **Significant decline in drilling / oil field services (-33 pc y/y) and construction (-6 pc y/y) sectors:** impact of low commodity prices and curtailment (market access).
- **Government investment** also declined (by about **-10 pc y/y**).
- **Export growth decelerated –** impact of curtailment on production.
- **Consumer spending** slowed down significantly, but still growing.

Bounce-back Anticipated for 2020-21

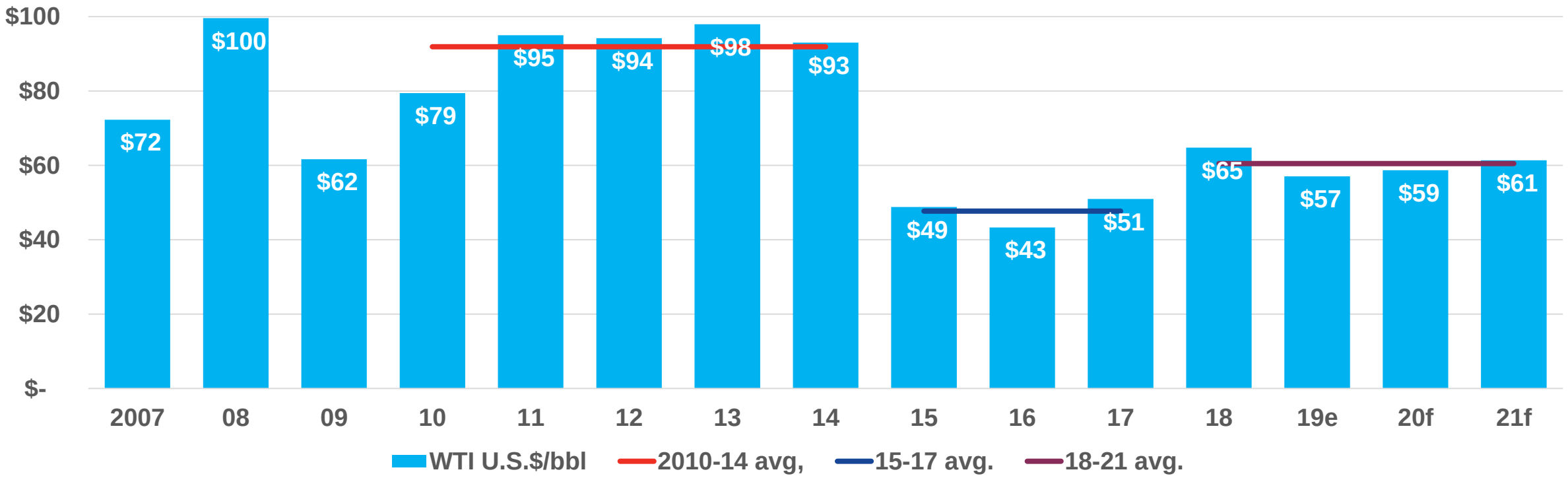
but growth will remain low by historical standards (i.e., *the new normal*), while various downside risks remain

GDP growth 2020-21: 2.2 – 2.3 per cent

- **Acceleration in consumer spending** anticipated
- **Govt. spending declining –** constrained by budget restraint
- **Rebound on business investment anticipated** – mainly non-residential (structures, IP [R&D], and machinery & equipment)
- **Export growth continues – but deceleration is clear:** O&G output growth decelerates after years of low prices, underinvestment in capacity, and market access constraints. *Net trade: single largest economic growth factor in 2020-21.*

A structural shift has taken place in global oil markets in the past decade. West Texas Intermediate (WTI) to remain at around the U.S.$50-60/bbl range in 2020-21

WTI price, U.S.$/bbl



2020-21 WTI forecast will be revised downward due to impact of COVID-19 on fuel demand and global economy

Source: The Conference Board of Canada; Statistics Canada; U.S. Energy Information Administration (EIA)

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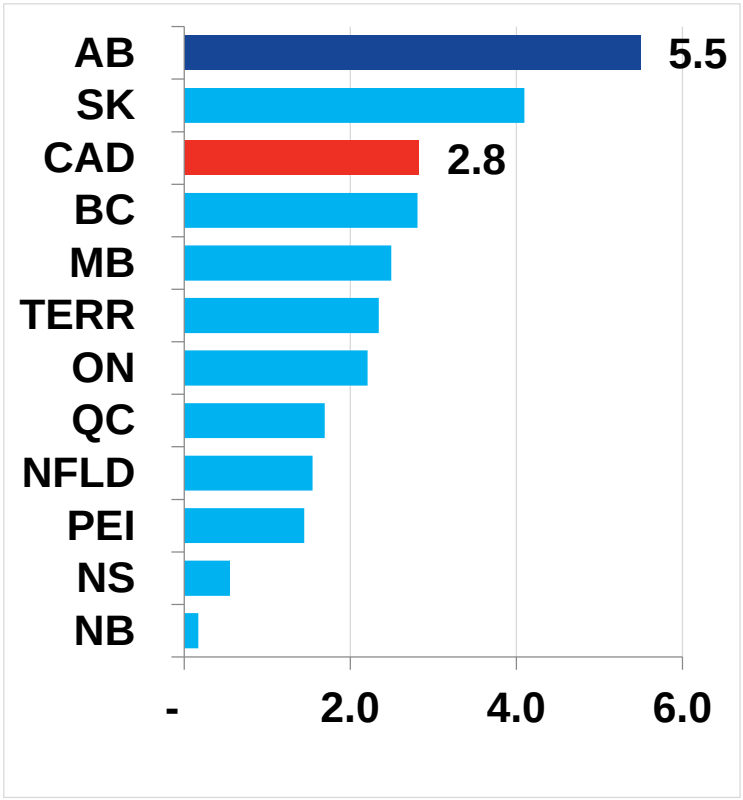
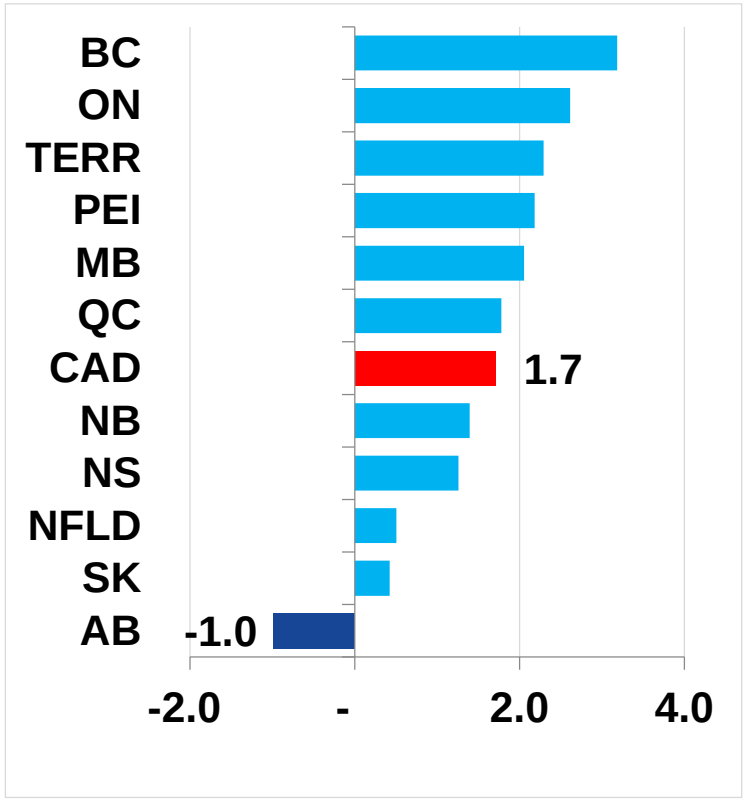
Changes in commodity prices impact the fortunes of Canada and its regions – Alberta is a clear example

average annual real GDP change, by region, per cent

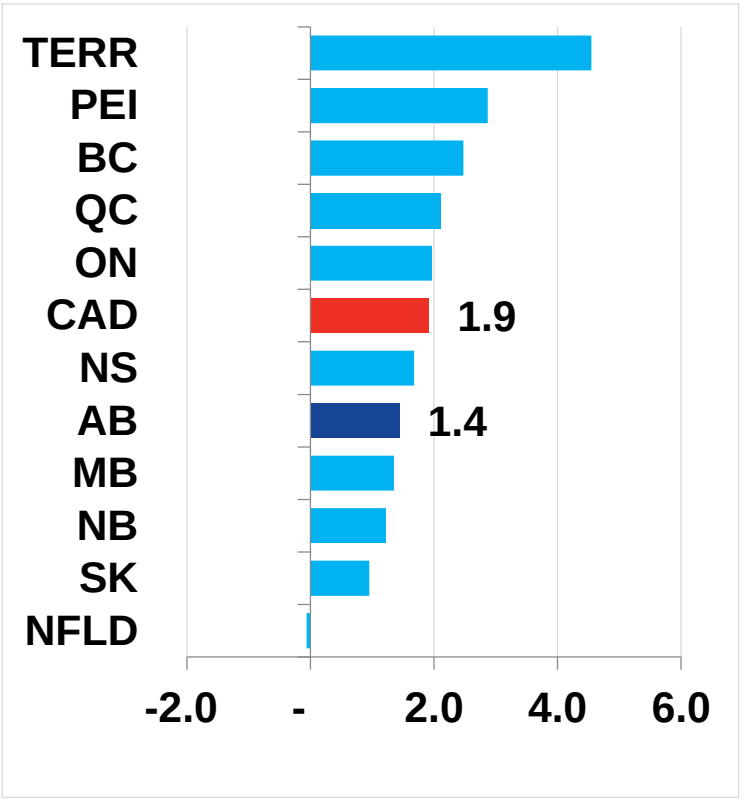
2010-14 (WTI @ U.S.$92/bbl)



2015-17 (WTI @ U.S.$48/bbl)



2018-21f (WTI @ U.S.$60/bbl)



Source: The Conference Board of Canada; Statistics Canada

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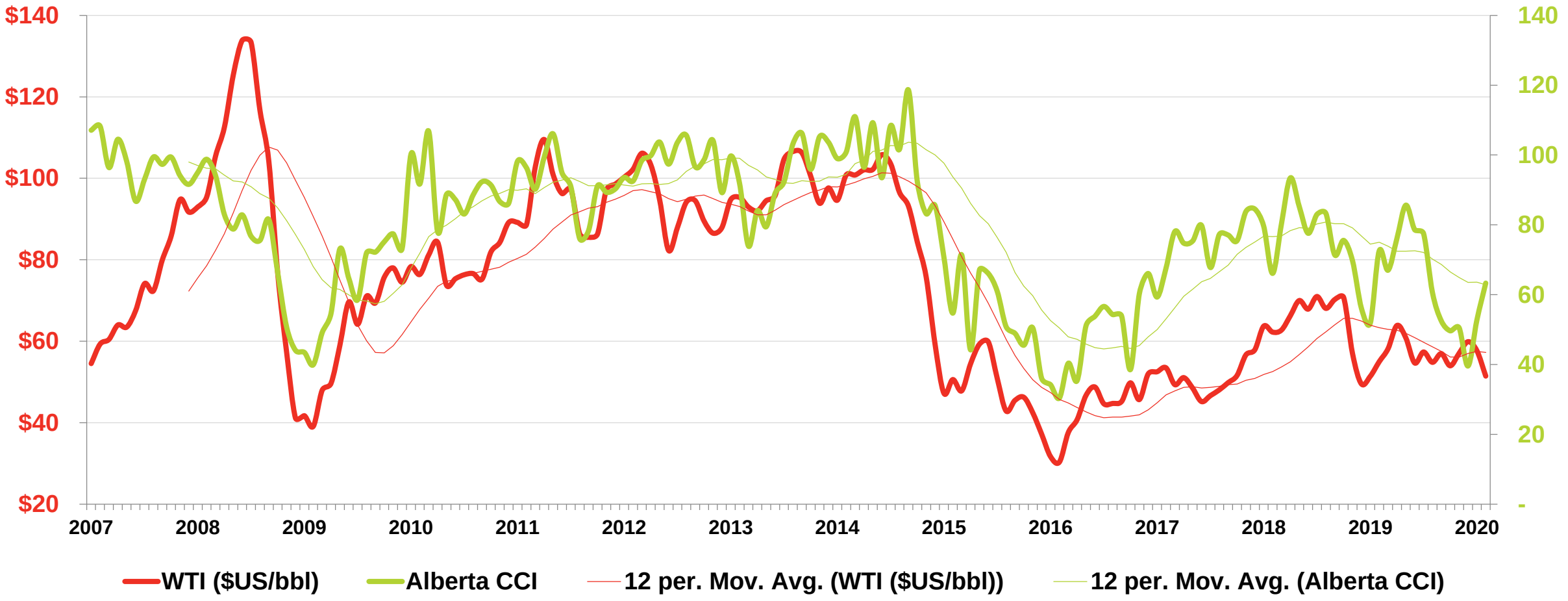
Alberta consumers keep a watchful eye on crude oil prices – sentiment follows along

Alberta consumer confidence index, right, 2014 = 100, and; West Texas Intermediate crude oil prices, left U.S.$/bbl



Source: The Conference Board of Canada; Statistics Canada

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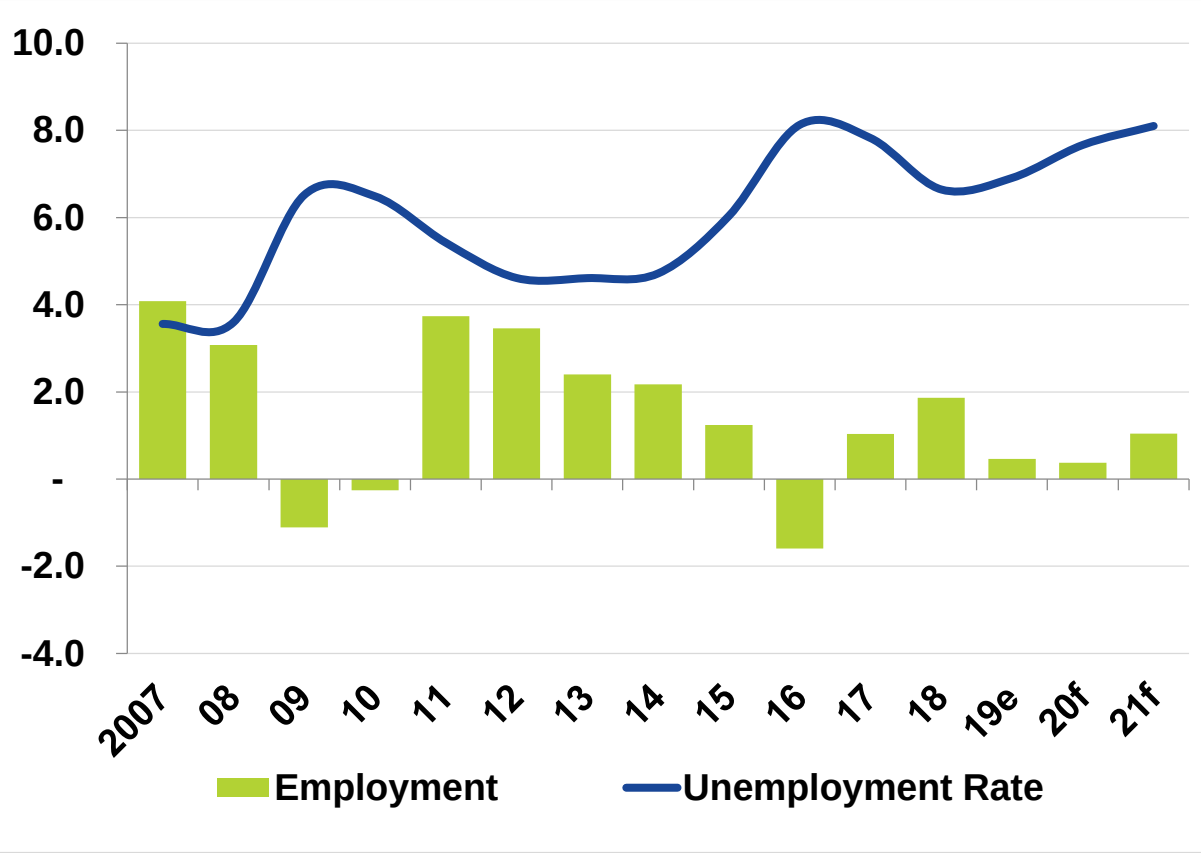
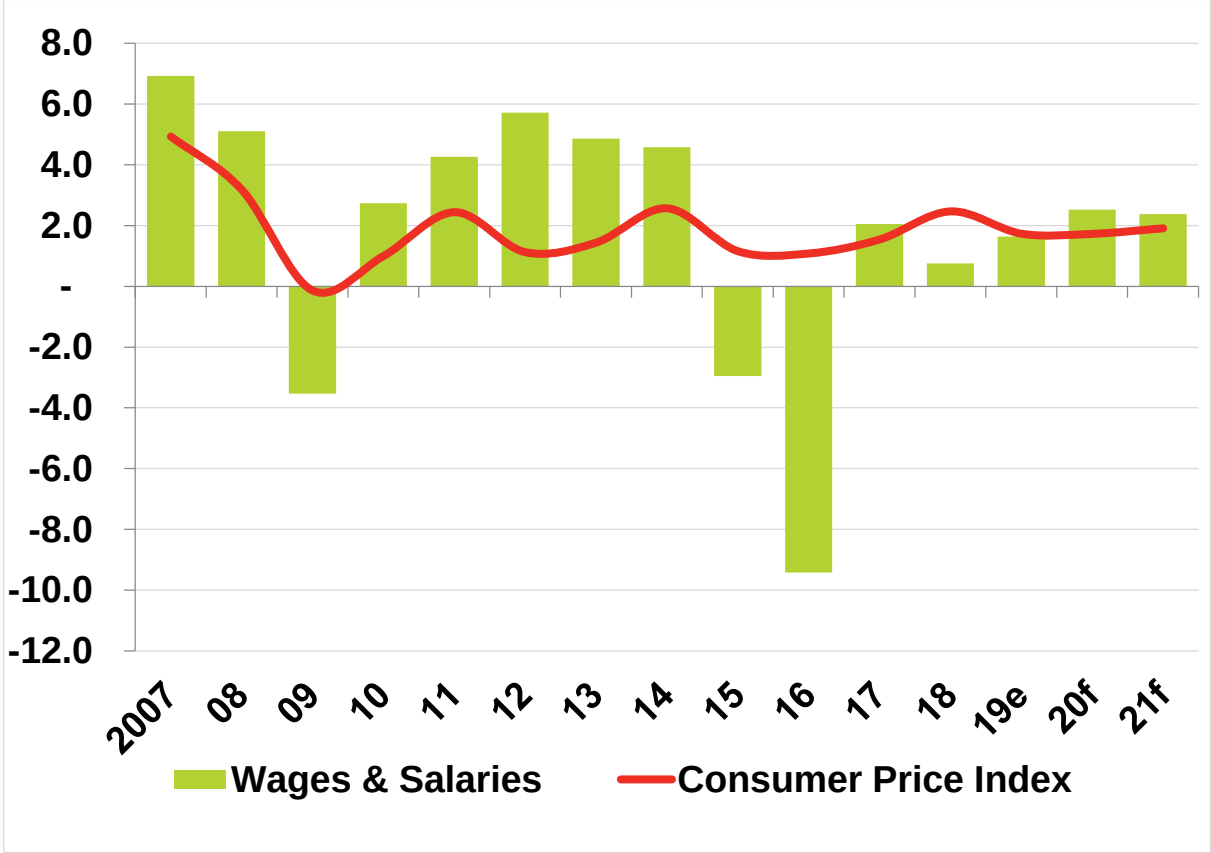
Employment levels picking up, but unemployment rate remains elevated. Wages increasing at a faster pace than inflation boosting household incomes and supporting increased consumer spending

y/y in labour market indicators, per cent





Source: The Conference Board of Canada; Statistics Canada

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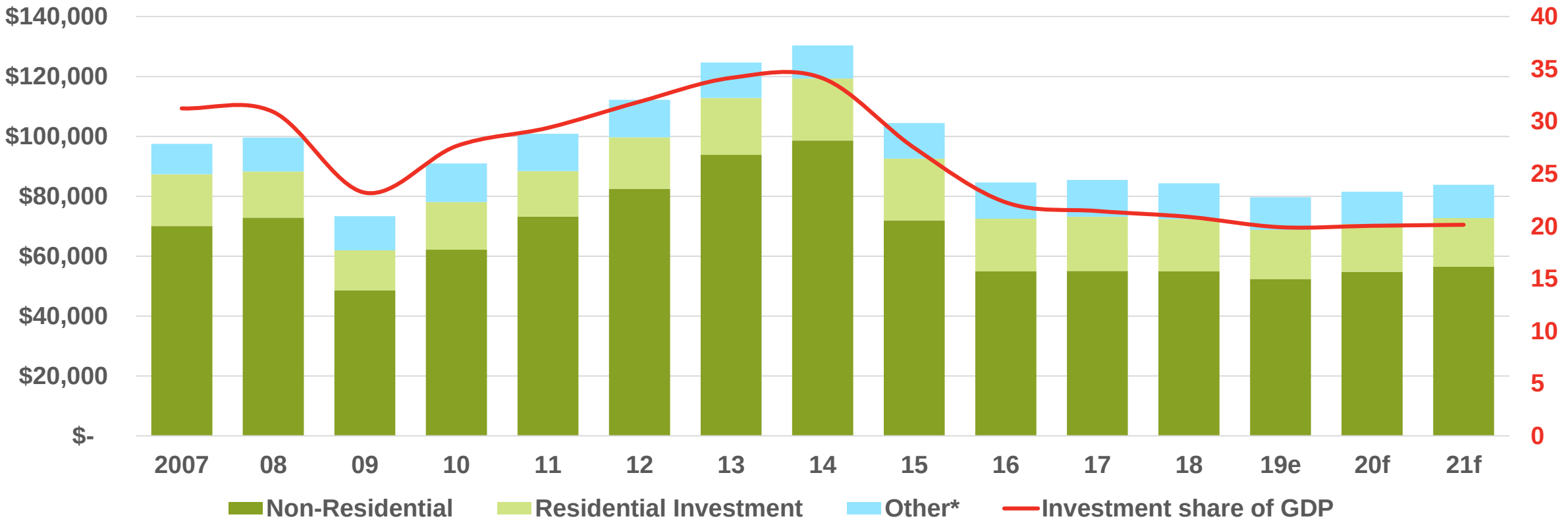
After five years of contraction, investments will finally turn the corner starting in 2020. Levels to remain 40 per cent below 2014's highs.

Total investment levels by category, billions of $2012, left, and; investments' share of provincial economy, per cent of total, right



Other includes government and non-profits investments

Source: The Conference Board of Canada; Statistics Canada

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Alberta's energy products dominate the province's exports

share of province's total merchandise exports' value by product in 2018, per cent

Source: The Conference Board of Canada; Alberta Finance

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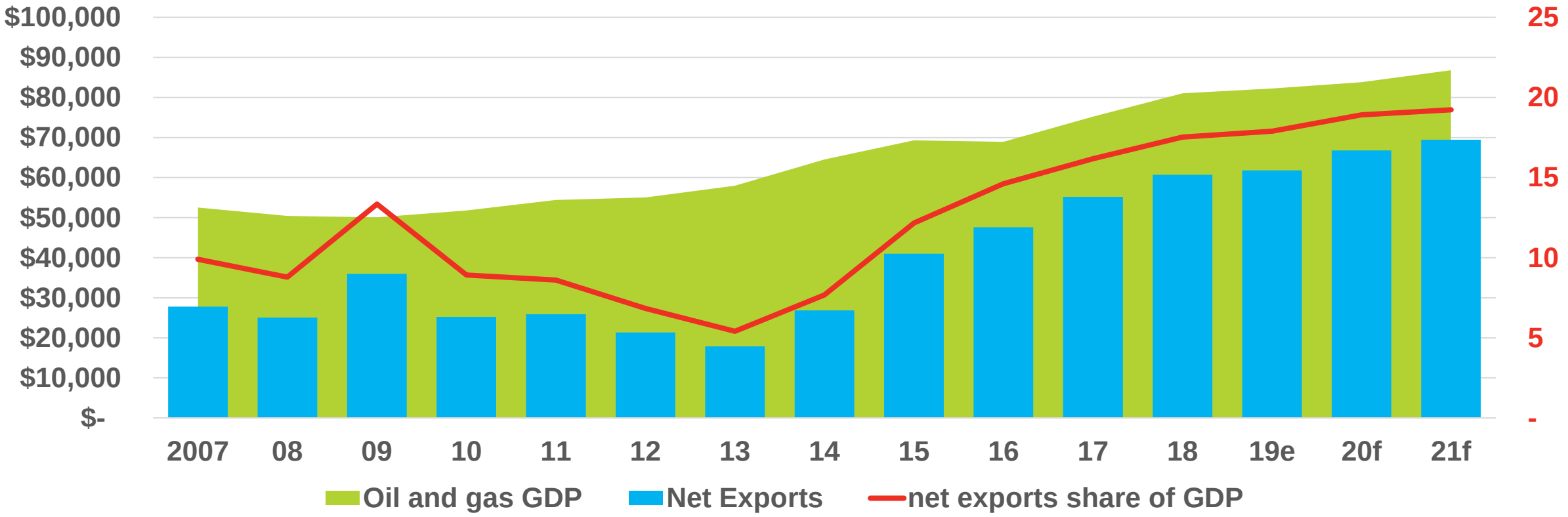
Province's net exports continue to go up with oil and gas production levels. Exports are a key growth driver for Alberta's economy – but growth is slowing down

Alberta's oil and gas industry output and net exports, billions of $2012, left, and; net exports share of provincial GDP, per cent, right



Source: The Conference Board of Canada; Statistics Canada

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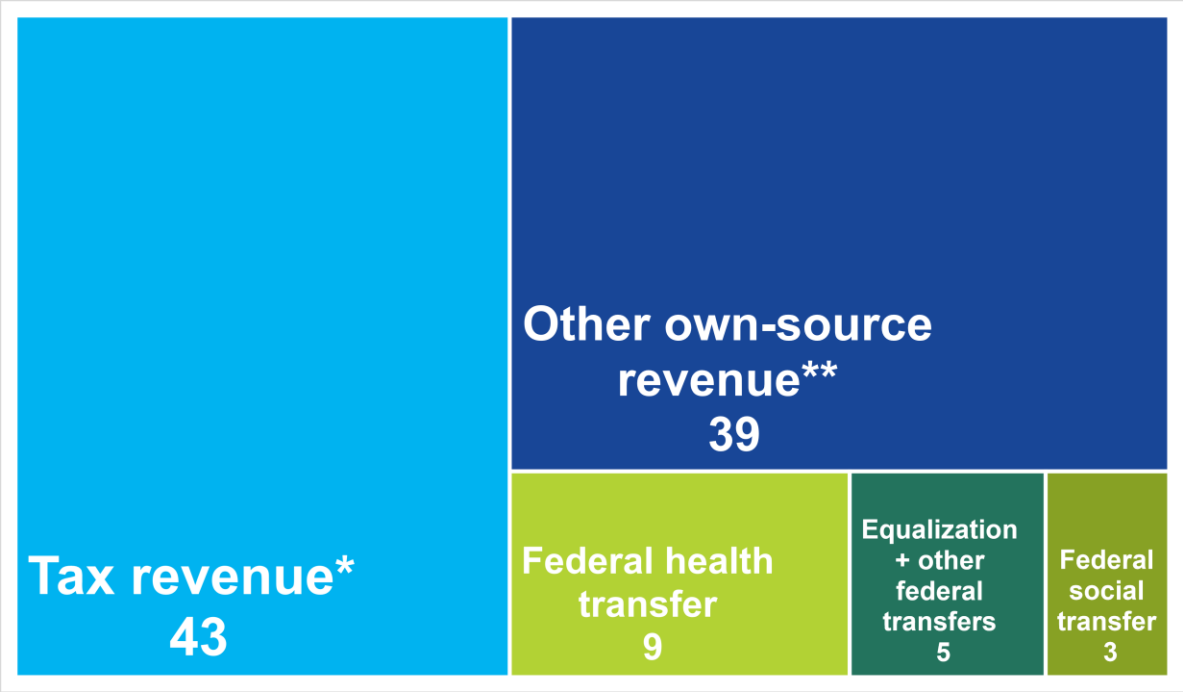
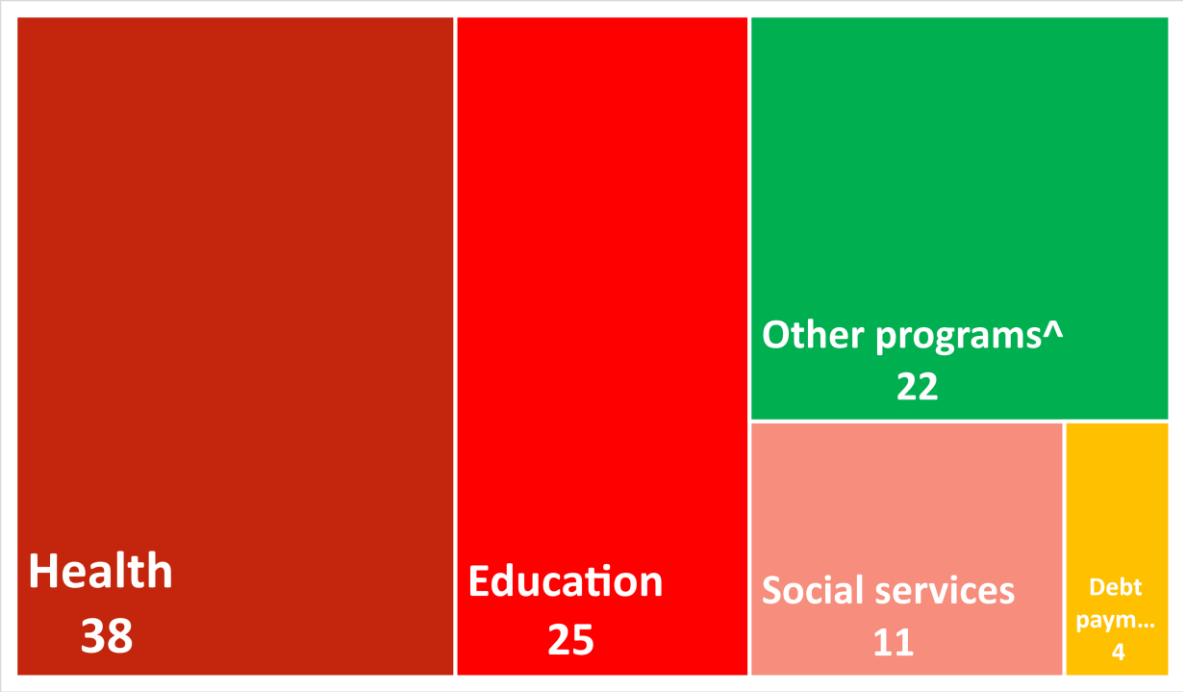
Government Finances – Revenues and Spending

provincial government revenues by source (left) and expenditures by category (right) for fiscal year (FY) 2019-20, per cent of total





Total revenues: $51 billion

- ~80 per cent of revenues are self-generated.
- Large reliance on natural resources revenues (13 pc of rev.), less reliance on federal transfers.

Total spending: $59 billion

- Health, education, and social services combined account for three-quarters of spending.
- Less than 5 per cent of spending on debt charges.

**includes income and sales taxes **includes royalties, income from crown corporations, and others. ^includes transfers to municipal governments.*
Source: The Conference Board of Canada; Provincial governments

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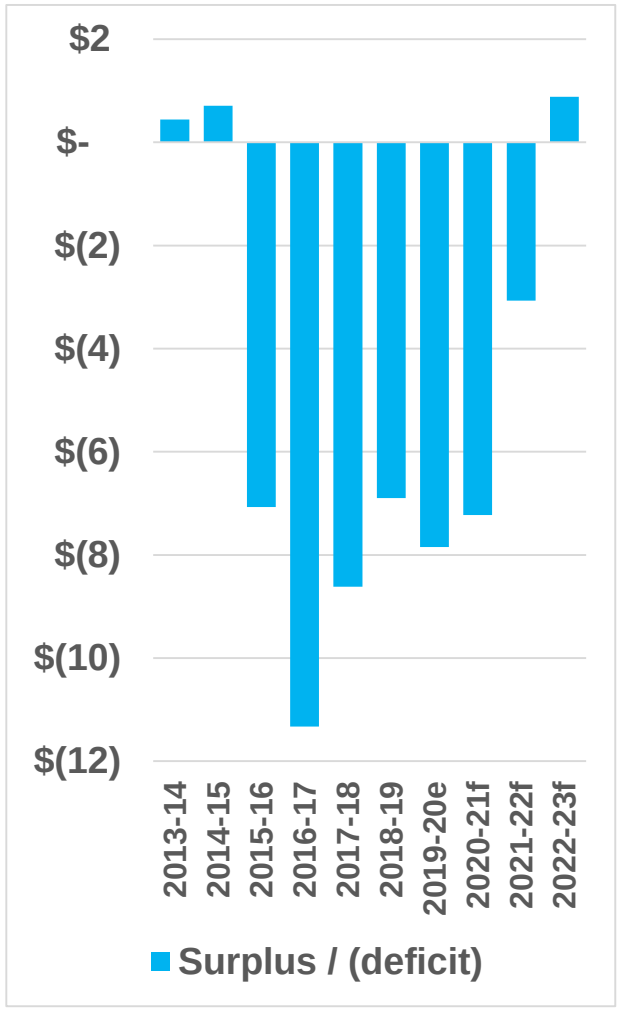
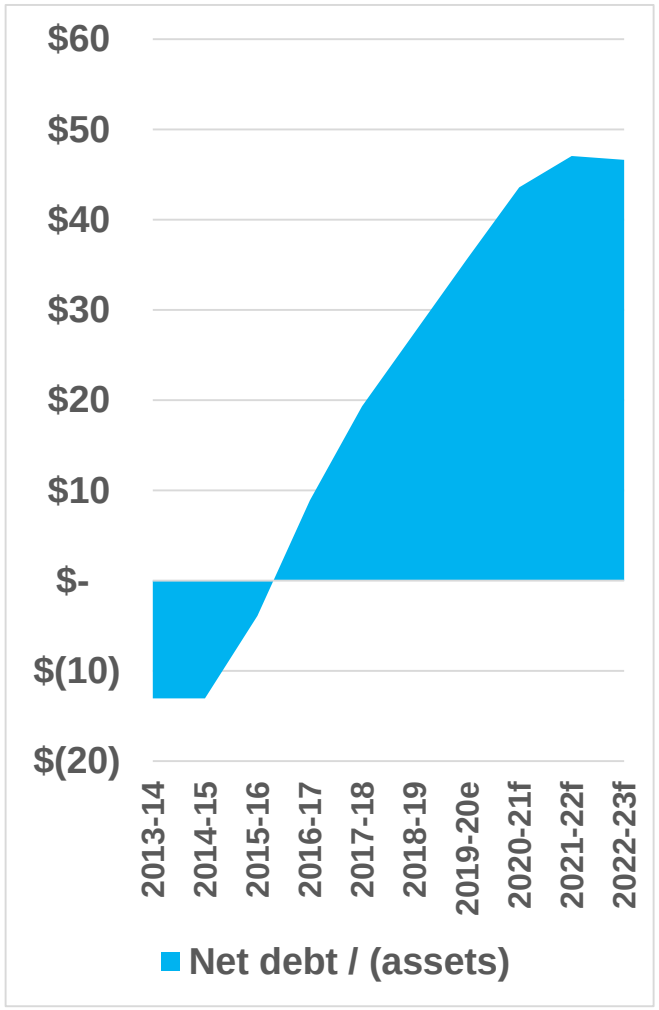
Alberta Provincial Government Fiscal Indicators

ongoing and shrinking deficits + growing but manageable debt levels

provincial government's budget surplus (deficit), left, and; net debt (assets), right, billions of $





- **Deficits have been common** in the province since the global financial crisis. **Current deficit** is equivalent to **13 per cent of government expenditures**
- **Per-capita program spending (i.e., health, education, other)** in AB is **third highest across Canada** and 6 pc above prov. avg.
- **Debt charges / revenues** are **the lowest across Canada** (at 4 per cent), **but rising**
- **Net debt / GDP ratio** of 10 per cent is **the lowest across Canada, but also growing.**

Latest budget was released last week.
Plan to **balance budget by 2022-23** through: **$2.5b of deep-cuts in program spending**, and **an optimistic $7b+ boost in revenues** (taxes, royalties, and transfers).

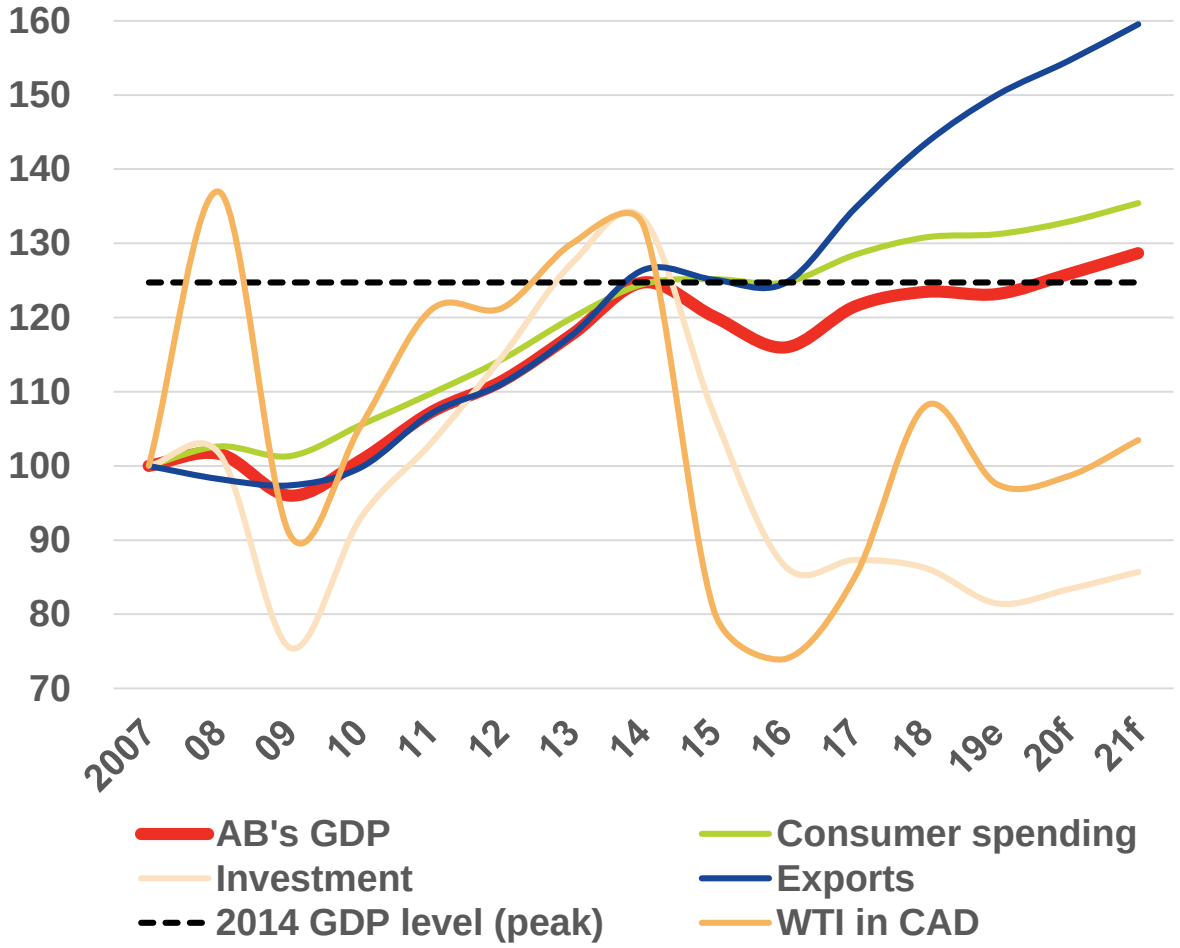
e= estimate; f= forecast

Source: The Conference Board of Canada; Provincial governments

The Conference Board of Canada

Where are we on the economic cycle and what is driving growth in the province?

Trends on indicators of provincial economic activity, 2007 = 100



Source: The Conference Board of Canada; Statistics Canada

PARADIGM SHIFT ON STRUCTURAL DRIVERS OF GROWTH: FROM INVESTMENT TO EXPORTS

2007-09: GDP up and down with global financial crisis

2010-14: Broad-based expansion with investment fueling rapid growth

2015-16: Broad-based contraction, rapid investment pullback drags economy into persistent recession

- Investment followed prices between 2007 and 2016. Overreliance on investment created boom and bust cycles with commodity price fluctuations.
- Investment levels failed to go up with prices after 2016, and are currently at levels not seen since the global financial crisis.

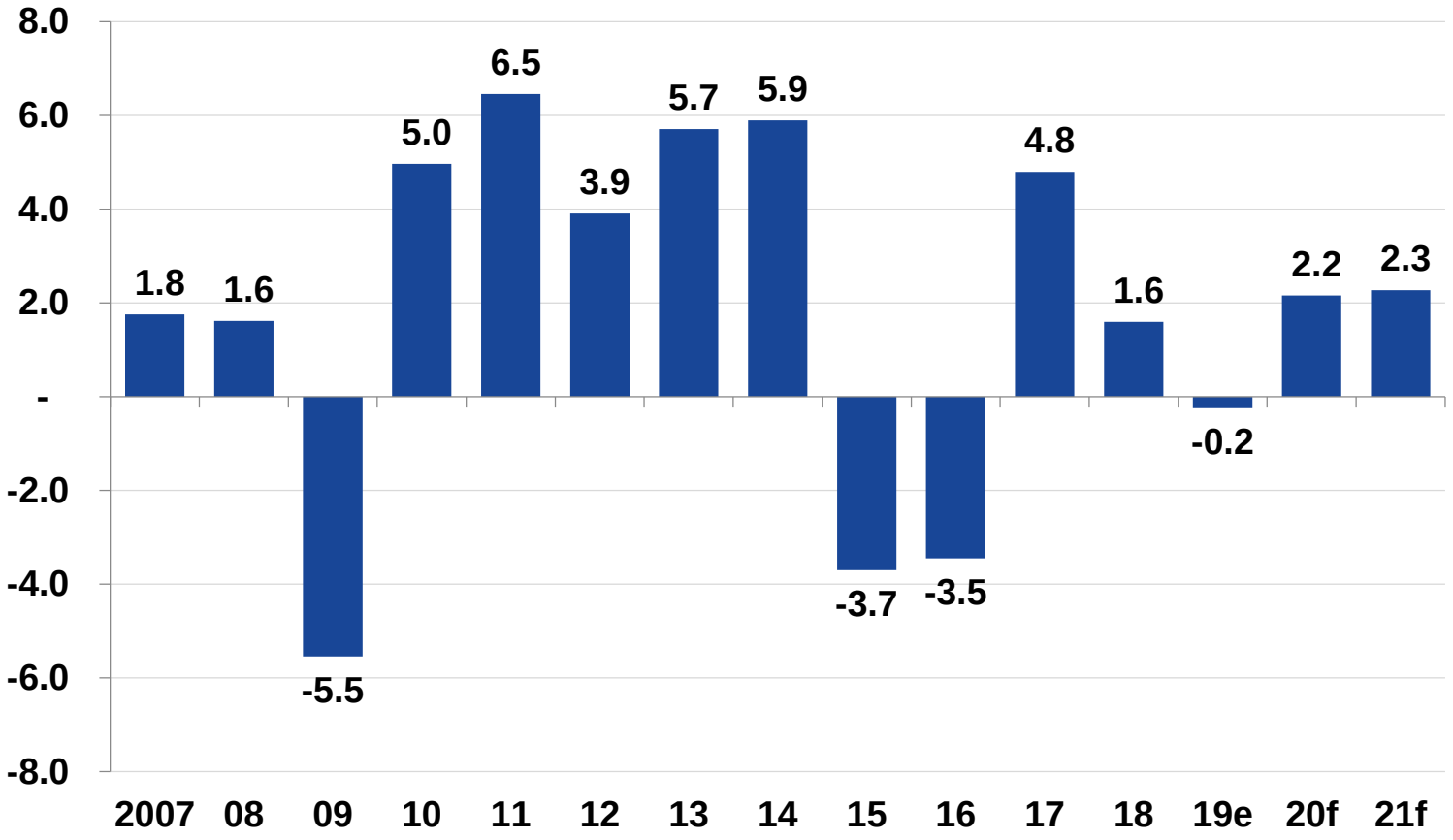
2017-21: recovery period, with consumer spending and exports driving growth (5-6 yrs. to recover econ loses)

- **Importance of healthy labor markets, consumer confidence, and access to export infrastructure**

The Conference Board of Canada

After a lackluster year in 2019, a recovery is in the cards for Alberta, but some downside risks are evident

y/y real GDP growth, per cent



Main outlook risks

- **Improvements in global economy and rising oil prices are needed (i.e., resolution of trade wars).**
- **Completion of pipelines to allow for expansion of oil and gas production and exports is also assumed to take place.**

The Conference Board of Canada

An Energy Perspective on Sustainability

(i.e., balancing the economy and the environment – and other important areas)

Key Takeaways

- **Global action on climate change will require a complete overhaul of the energy-system** (i.e., all energy-related activities from production to end-use). This will have an impact on trade-exposed and energy-dependent jurisdictions like Canada and Alberta.
- **This transition should be considered a strategic opportunity** to transform to a sustainable economic model that protects the environment, creates wealth, and enhances the standard of living of Canadians.
- **But to get to that model we need to understand our current situation, define where we want to go, and chart a path forward.** We suggest the use of a sustainability framework with a focus on energy to chart this transformation – one that will take place over the long-term and will achieve a balance between the economy, the environment, and society.

Climate Change

- Global atmospheric concentration of human-caused greenhouse gas (GHG) emissions is increasing. These emissions are the main driver of global warming and climate change. (IPCC, 2018)
  - **In Canada, warming is happening at twice the global rate. The effects of warming – including extreme weather, precipitation, flooding, ocean acidification, and permafrost thaw – are projected to intensity.(ECCC, 2019)**
- Global warming and climate change will have disruptive impacts across all aspects of life – not only on the natural environment, but also on people, the built environment (i.e., infrastructure), and the economy. (IMF, 2019; McKinsey, 2020, and; WEF, 2020)

GHG Emissions and The Future of Energy

- Through the UNFCCC's 2015 Paris Agreement, 175 parties agreed to hold increases in global temperatures below 2°C above pre-industrial levels – to limit climate change's impacts.
  - **As a signatory to the agreement, Canada has committed to reduce its GHG emissions levels to 30 per cent below 2005's levels by 2030. The federal government has proposed reaching a "net zero" emissions target by 2050.**
- Energy-related GHG emissions (incl. combustion + fugitives) account for ¾ of total emissions. Fossil fuels account for 80 per cent of all energy used. (C2ES, 2019; IEA, 2020, and WRI, 2020).
  - **In Canada, the corresponding shares are 80 per cent and 75 per cent, respectively. (ECCC, 2019, and; Statistics Canada, 2020)**

GHG Emissions and The Future of Energy

- Reducing GHG emissions globally, and in Canada, will require an overhaul of the entire energy-system (i.e., all activities from energy production to end-use)
- International Energy Agency (IEA) global projections: (IEA, 2019)
  - **a scenario that reaches the goals of the Paris Agreement only requires a 20 per cent increase in cumulative (2019-40) energy-system investments relative to a business-as-usual scenario**. What changes dramatically is the composition of the investment – i.e., move away from fossil fuels to more renewables, energy efficiency, electrification of end-uses, etc.
  - This scenario doesn't require lower economic or population growth.
  - **Technology and costs are not an issue, coordinated implementation of the right policies and changes needed to drive this change are the main constrain. We found similar results when doing a recent energy-economy-GHGs modelling exercise for Natural Resources Canada.**

This global transition to a low-carbon future will have an impact on trade-dependent countries like Canada and energy-producing regions like Alberta. This should be viewed strategically as an opportunity, not a threat.

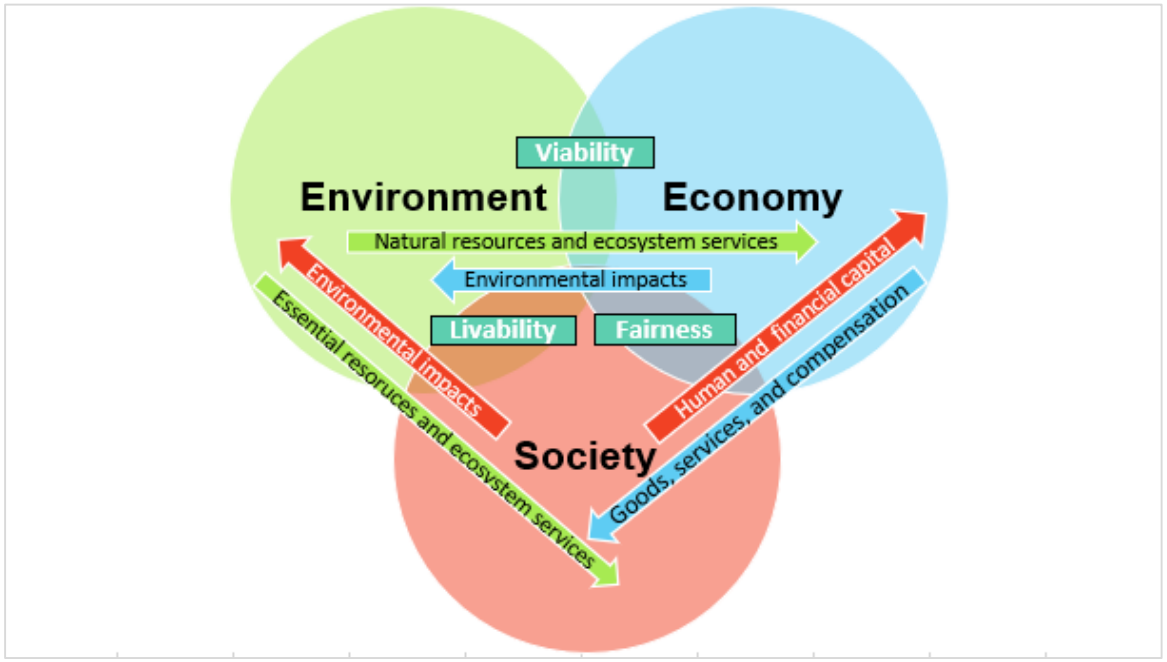
How Can We Capitalize on This Opportunity?

Move Canada and Alberta towards a sustainable economic model that balances the environment, the economy, and society

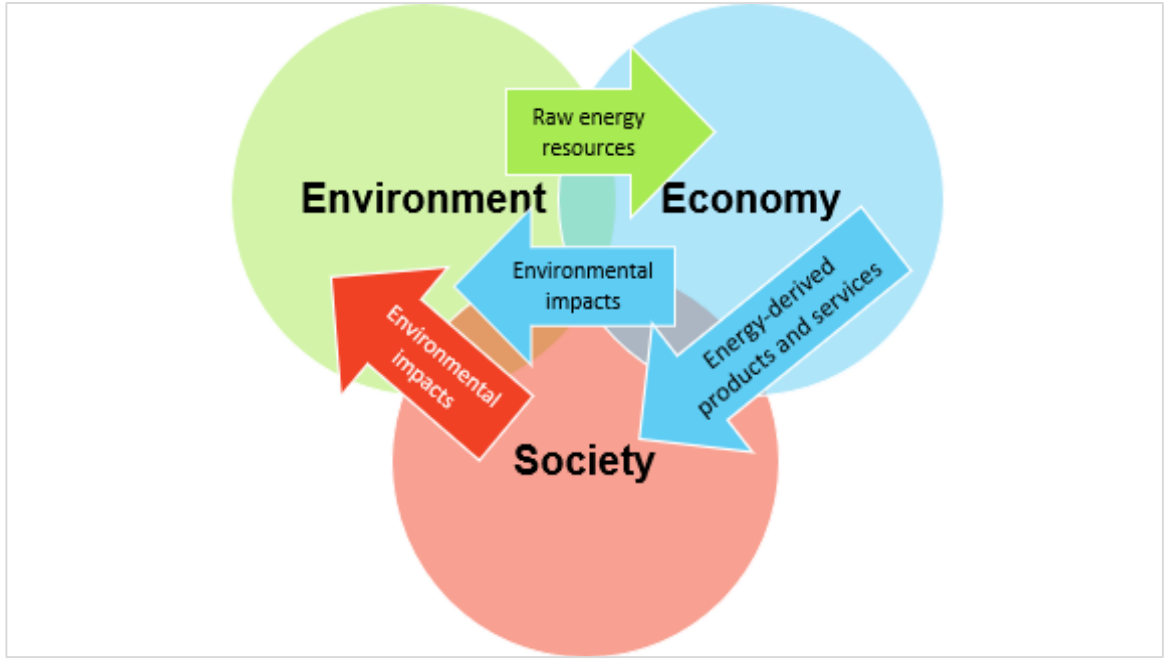
We call this ***a clean energy growth economy*****:** one that sustains the natural environment, creates economic wealth, and enhances the standard of living of Canadians.

The analytical framework can be understood as an **energy-system perspective on sustainability.** We **focus on energy, given its ubiquity and importance to climate change and sustainability issues.**

"Traditional" Sustainability Framework



Energy-System Lens on Sustainability



Source: The Conference Board of Canada; European Commission

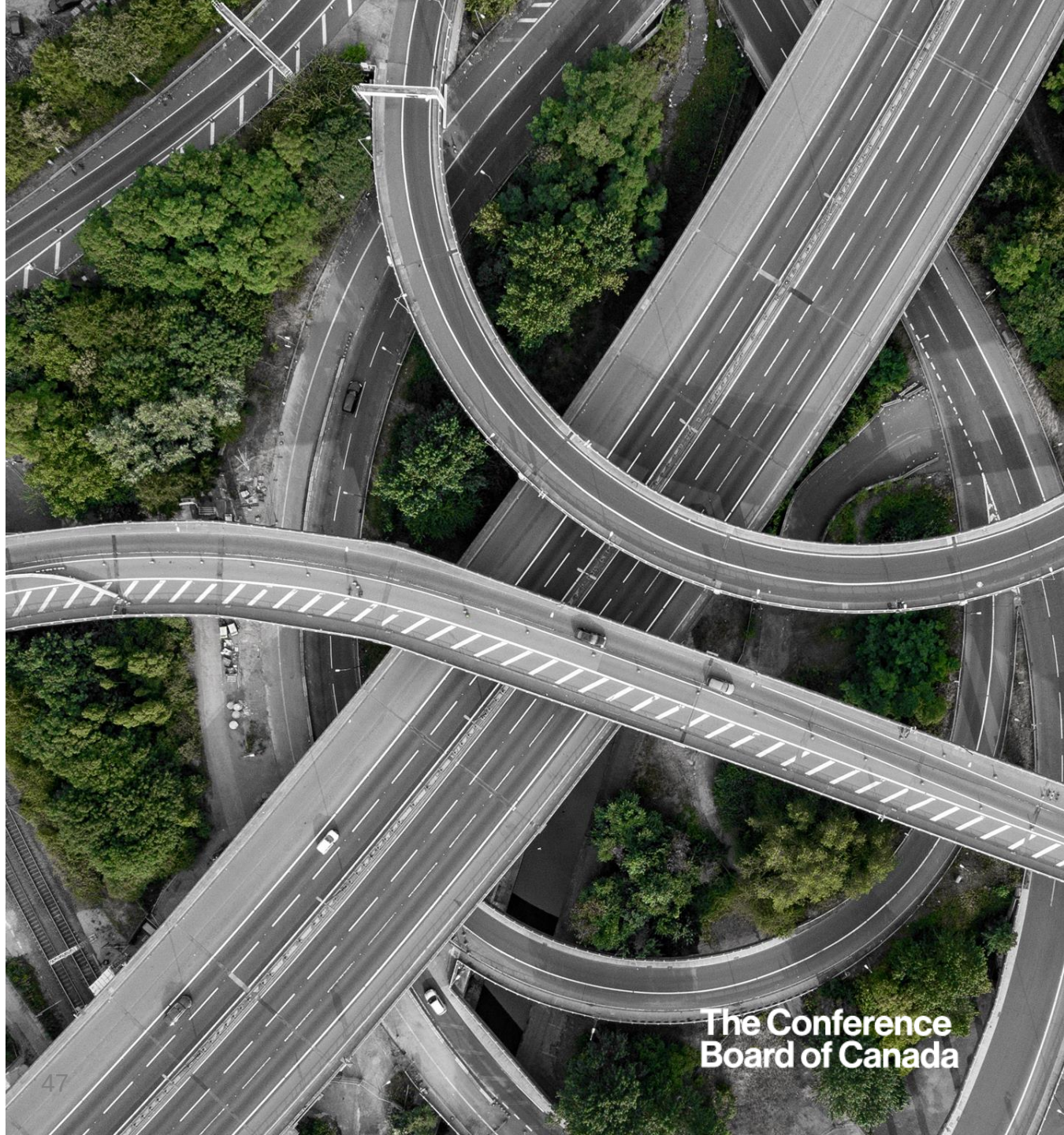
The Conference Board of Canada

Canada's transition to a clean energy growth economy – so many questions!

- **What does it look like? (i.e., how do we define it, measure it, etc.)**
- With a well-defined framework and via data-driven indicators

- **How do we track progress in moving forward?**
- Looking at the past, understanding recent trends, driving forces, and potential future targets for indicators

- **How do we move from aspiration to implementation?**
- By proposing clear actions to get us to our destination



We Can Also Ask People Across the Country

We did this across seven locations in Canada in November 2019.

Discussions focused on the **region-specific opportunities and challenges of achieving theme-specific strategic goals** that represent success in the transition, including:

- ***Economy****: maximizing Canada's potential and global competitiveness*
- ***Environment****: reducing human-induced environmental impacts and using resources sustainably*
- ***Society:*** *ensuring Canadians' standard of living continues to improve*

We engaged with close to 100 business, government, and civil-society leaders at these "townhall" events

What We Heard

One example: *Cross-jurisdictional cooperation and consistency on policy and regulation (economy / challenge)*

What is the issue?

Lack of coordination across levels of government, regions, and departments hampers the transition. Cross-jurisdictional disagreements and inconsistency lead to complexity and uncertainty. This discourages investment and innovation, hurting economic opportunities and the cost-effectiveness of environmental protection – such as GHG emissions reduction efforts.

What is a good example?

In the Prairie provinces, multiple and inconsistent regulations and policies at the provincial vs. federal levels make investment decisions for infrastructure and technology in the natural resources sector very difficult to make. This limits the positive economic, environmental, and social impacts of such investments.

What We Heard

One example: *Cross-jurisdictional cooperation and consistency on policy and regulation (economy / challenge)*

How can we "evidence" the issue with actual data?

- Business investment levels in Canada follow businesses' stated investment intentions very closely (based on The Conference Board's Index of Business Confidence survey). Business investment has performed very poorly in the last few years. **"Government policies" has become the top response for negative factors impacting investment decisions.**
- An index of **"economic uncertainty" is currently at an all-time high in Canada**, **corresponding with a negative view on government policies.**
- **Natural resource sector investment levels have decoupled from their traditional linkages to commodity prices in Canada** – but not in the U.S. (our largest customer and competitor in the sector). **Regulatory complexity and uncertainty are a likely cause for this disconnect**.

What's The Road Ahead?

We will **continue to work on evidence-based research and inclusive dialogue** to create **a roadmap of key actions for a clean energy growth economy transition in Canada**.

- All our work is available free of charge on our website

The framework presented here – i.e., an energy perspective on sustainability – provides a means to understand, discuss, and act on **key long-term pressing issues** such as climate change; the needed energy transition; **balancing the economy and the environment**, and; the future of Canada and Alberta.

The economic outlook is always relevant, but it is becoming increasingly important to employ an approach that accounts for the impacts of government policies, business decisions, and consumer choices not only on the economy, but also on the environment and society.

The Conference Board of Canada