ECONOMICS | RESEARCH

CURRENT ANALYSIS

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Atlantic Canada: An economy in renewal

In the past year, Atlantic Canada has emerged as one the regions in Canada putting up the strongest resistance to the downturn. While the recession likely did cause the region's economy to contract in 2009 (confirmation will come only when official annual provincial GDP numbers are released next spring), the effect on available indicators has been relatively muted, especially compared with hard-hit provinces such Ontario, Alberta and British Columbia. Since the peak (at the national level) in October of last year, job losses in Atlantic Canada have been less severe than in the rest of the country (see Chart 1). Provincial unemployment rates have risen less rapidly than the national average (see Chart 2) – the rate in New Brunswick even declined modestly. Retail sales, although shrinking a little, have held up comparatively much better than those in the rest of the country (see Chart 3). And, spending on residential construction in the region has remained above water until very recently amid sharp drops elsewhere in the country (see Chart 4) and the high-profile collapse south of the border.

This resilience to the deepest downturn in the global economy since the Great Depression is doing much to shed Atlantic Canada's old image as being plagued by depleting natural resources and chronic unemployment that was chasing young people away. The transformation of the region's economy during the past decade or so has been significant and a renewed sense of dynamism and confidence now prevails.

The main trigger of all this transformation has been the development of major energy and mining projects, but others factors have also contributed. Since the first barrel of oil produced at the Hibernia field off the shore of Newfoundland in 1997, the oil and gas industry has grown into a key economic engine in the region. Megaprojects such as Hibernia, Terra Nova, White Rose, Sable Island, Deep Panuke and, soon, Hebron have injected several billion dollars into the region's economy and have spawned a host of supporting businesses from engineering firms to equipment manufacturers to transportation service companies. Additionally, the development of a world-class nickel deposit in Labrador has further broadened the industrial base.

While these projects have generated tremendous economic activity during their construction stages, they are now generating increased incomes in their production stages, including in the form of government royalties. In fact, for Newfoundland & Labrador, offshore and mining royalties have soared since early this decade to account for as much as 45% of total provincial own-source revenues last fiscal year (see Chart 5) – although they are projected to drop to 32% this fiscal year due to lower average prices and production rates. This surge in royalties has

CHART 1

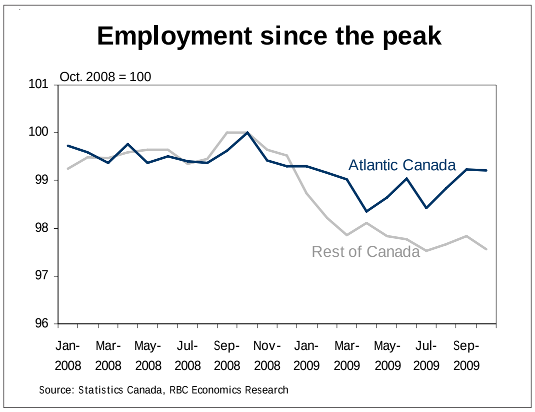

CHART 2

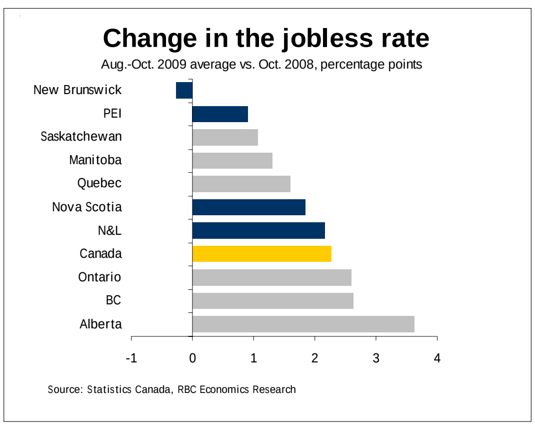

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CHART 3

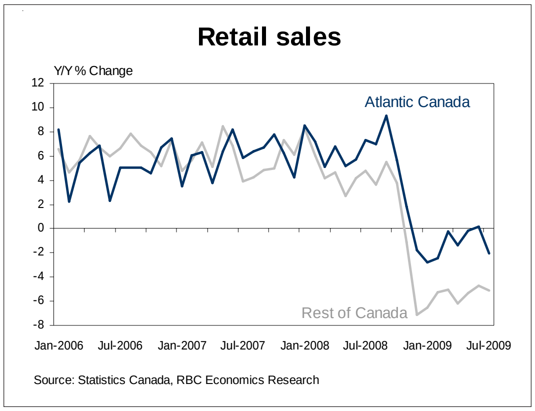


CHART 4

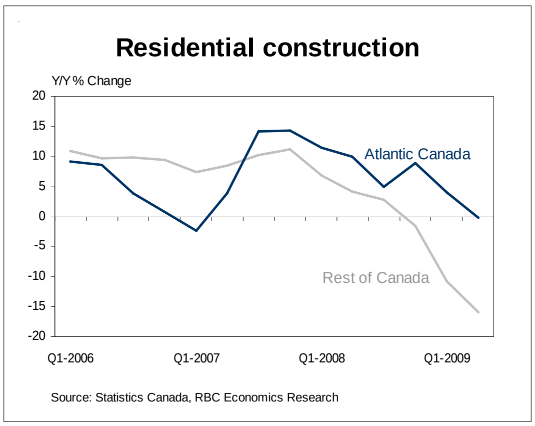
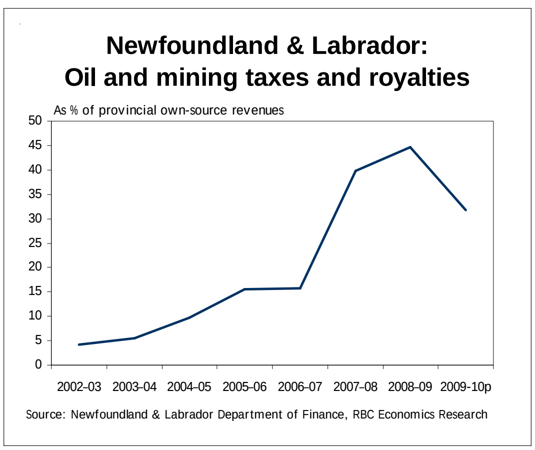


CHART 5



significantly contributed to Newfoundland & Labrador ditching its longstanding "have-not" province label as it came off federal equalization in 2008.

The benefits from the boom in energy and mining have flowed not only to Newfoundland & Labrador and Nova Scotia – where most of the biggest projects reside – but also, at least indirectly, to New Brunswick and Prince Edward Island. While not a significant producer of crude oil or natural gas, New Brunswick has bulked up in the energy area with the recent addition of Canada's first-ever liquid natural gas regassification terminal, which complements the province's major oil refining capacity.

In Prince Edward Island, traditional sectors such as agri-food and tourism are increasingly being supplemented by growing high-tech industries like aerospace, information technology, new media and bioscience, all of which are the objects of concerted efforts by the provincial government to establish new sources of economic growth. Aerospace is a particularly bright spot, even at a time of upheaval in this industry globally, as exports have grown by almost 10% year-to-date in 2009 after an impressive 68% increase in 2008. This industry now ranks as the number-two export category in the province (behind potato products, a long-time success story in the province).

Fastest population growth since the early 1990s

One of the clearest manifestations of renewed optimism in the Atlantic region has been the reversal of earlier net migration outflows to other provinces (see Chart 6). Through most of recent decades, Atlantic Canada suffered net population losses to other parts of the country – often young, skilled and educated individuals – seen at the time as a sign of discouragement. Since the middle of 2007, however, the relatively brighter economic prospects in the region have not only worked to retain people in the region but also to attract other Canadians in greater numbers. In some cases, this increase in provincial in-migration reflects the return home of individuals who had left previously to go to formerly booming places such as Alberta or Ontario, but where the job markets have since soured. However, it also likely represents Canadians born outside the region attracted by Atlantic Canada's improved economic opportunities and, of course, the region's well-known quality of life.

With the number of foreign immigrants trending higher in the region since about 2003 on a net basis, Atlantic Canada is now seeing its strongest overall migration flows in decades (see Chart 7). Very importantly, this translates into the fastest population growth since the early 1990s. Atlantic Canada's population growth rate might be still be small by national standards (running at 0.3% year-over-year in the third quarter of this year compared to about 1.2% for Canada as a whole), but it is a vast improvement from absolute declines through most of the 1995-2007 period.

The implications of growing net in-migration and population should not be understated. Favourable demographics are a significant economic driver, which pushes up demand for everything from housing to consumer services (think hair cuts, health care) to goods and to various infrastructures (roads, public transit, etc.) and expands the labour force. In turn, this supports investment – in new housing, new sewage systems, new roads, new shopping malls, etc. and creates new jobs. Going from a situation of net decline in population to one of net population growth, if maintained, represents a meaningful improvement in the long-term economic fundamentals for the region.

Add to this continued investment in major projects in the energy (Hebron, White Rose expansion) and metal processing facilities (Long Harbour) in the coming years and the Atlantic region should maintain its forward momentum in the years ahead. Statistics Canada's survey of private and public investment intentions conducted in early-summer showed a 24% increase in capital spending plans in Newfoundland & Labrador in 2009, in stark contrast to a 10% decline nationally.

Certainly, in the short-term, economic prospects remain fairly bright. We forecast real GDP growth for the Atlantic provinces (2.4% altogether) close to the national average of 2.6% next year. Considering that the decline in activity this year will be more modest in the region than in the rest of Canada (-1.3% compared to -2.6%, respectively) and that Atlantic Canada has outperformed the national average in both 2007 and 2008, this expected performance in 2010 is noteworthy

Challenges ahead

While economic fundamentals have improved, the region will continue to face challenges. Above all, strong reliance on megaproject construction begs the issue of follow-up acts. Atlantic Canada has been successful at attracting major projects in the past many years, but new projects are constantly needed to pick up any slack from completed work. Also, industrial diversification into energy is welcome but is no panacea. The ups and downs of global energy markets imply a large degree of volatility. Finally, provinces such as Prince Edward Island still rely disproportionately on mature, seasonal industries (e.g., agriculture, fisheries, tourism), which tend to restrain growth prospects. Efforts to diversify into faster-growing sectors will need to be ongoing to ensure that the economic renewal process progresses further in the years ahead.

CHART 6

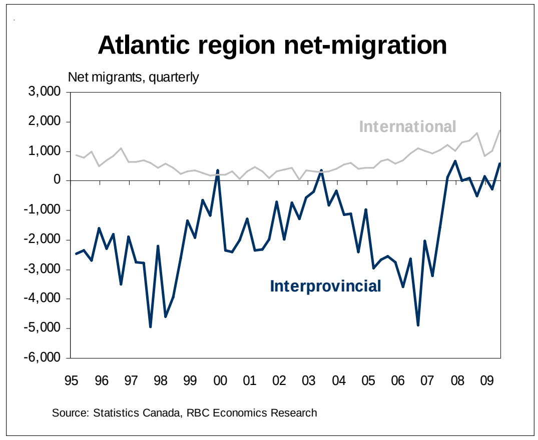


CHART 7