

Newfoundland & Labrador: Recovery on the Horizon

Canada's economy crawled out of recession in the fall, with strong domestic demand met largely by foreign producers. Real GDP grew 0.4% annualized in Q3, tempered by a 36% surge in imports. Domestic demand was solid, with personal consumption up 3% and machinery investment advancing for the first time in six quarters. As well, despite the strong currency, exports rose the most in five years in response to an upswing in global demand. Employment has turned modestly higher, suggesting the unemployment rate will peak around 8½%, a full three percentage points below the previous recession high and virtually in line with the three-decade mean. Hiring intentions are firming, according to the Business Outlook Survey. Meantime, **Newfoundland & Labrador is also on the path to recovery** after the province's recent economic strength deteriorated alongside the decline in oil prices and subsequent falloff in output. Real GDP likely contracted 4.9% in 2009 before rebounding 3% in 2010.

Offshore oil output is now in secular decline, and fell in 2009, while a strike at the Voisey's Bay nickel mine will also hurt output. In 2010, offshore output will continue to trail off, but the mining sector should bounce back, providing some support. Also offering support will be an aggressive government infrastructure spending program. At more than 3% of GDP, the Province's stimulus program is among the strongest in Canada in FY2009/10.

Other underlying economic trends remain mixed in the province. Retail sales, for example, were actually up year-over-year through October, the only province able to stake that claim. However, the

labour market has deteriorated, with the unemployment rate staying over 15% for the past seven months and employment down about 5% from peak levels.

One reason for the higher unemployment rate has been a pickup in labour force growth. The province has seen net in-migration of more than 2,300 people in the latest four quarters (through 2009Q2), the biggest annual gain on record. A slowdown in Alberta has no doubt reversed the migration flows seen during that province's boom, and as Western Canada begins to recover, Newfoundland & Labrador should again start to see out-migration.

The Province of Newfoundland and Labrador is forecasting a \$443 mln deficit for FY09/10, a steep shift from a fourth consecutive surplus of \$2.4 bln in FY08/09. Importantly, the deficit is improved from a budget estimate of \$750 mln thanks to rebounding oil prices. The deficit is projected to drop to only \$141 mln in FY10/11 before returning to surplus by FY11/12.

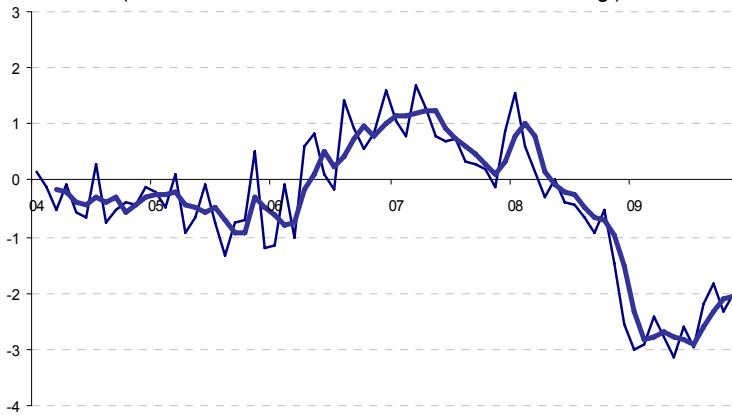
Revenue is expected to decrease 11.3% to \$6.2 bln in FY09/10, reflecting a decline in oil royalties (the combination of lower prices and lower production), though not as much as initially expected. The province is now

Newfoundland & Labrador *Economic Outlook*

	2008	2009f	2010f
Real GDP (% chng)	-0.1	-4.9	3.0
Employment (% chng)	1.4	-2.4	0.5
Unemployment Rate (%)	13.3	15.5	16.0
Housing Starts (000s)	3.2	3.2	3.5
CPI (% chng)	2.9	0.2	1.3

Source: Statistics Canada, BMO Capital Markets

Provincial Economic Momentum Index
(Newfoundland & Labrador. Dark line = 3-mo avg.)





assuming oil prices of \$71.80, up from the budget forecast of just \$50.

After cutting personal income tax rates in the prior two fiscal years (to give the province the lowest personal tax rate in Atlantic Canada), this year's modest tax changes focussed on low-income earners and small businesses. Program spending is projected to grow 14.4% to \$5.9 bln

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