Economic Trends

This month's Economic Trends comes from the [2020-21 Mid-year Fiscal Update and Economic Statement], released on November 24, 2020.

Overview

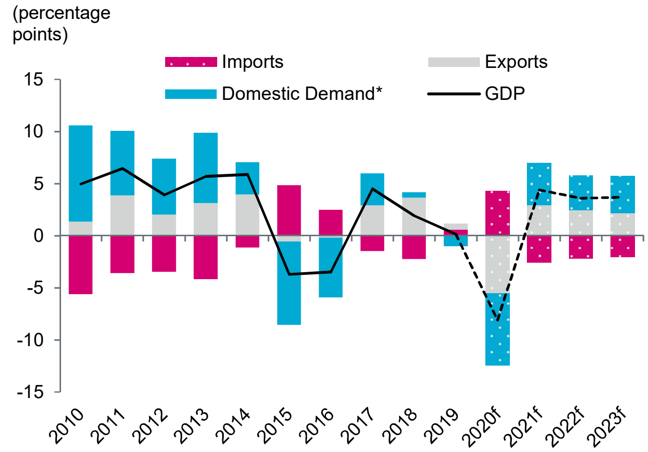
The Alberta economy is slowly coming out from the depths of the downturn caused by the dual shock of the COVID-19 pandemic and collapse in oil prices. The Alberta Activity Index, an indicator of provincial economic activity, has bounced back nearly 6 per cent since hitting a trough in May. The recovery has been led by households, and indicators like retail spending and housing have rebounded more strongly than anticipated. Business activity continues to lag behind, but there have been some bright spots. The agriculture sector is benefitting from strong crop conditions overall, and the forestry sector is seeing higher lumber prices. There has been support for natural gas producers with higher prices and investment in pipeline capacity. Even so, overall economic activity in the province remains well below February's level.

Recent indicators also suggest that momentum in the economy is slowing. Investment remains weak in the province, and the resurgence in COVID-19 cases in Alberta, Canada and around the world poses a headwind to the recovery. Nonetheless, continued government income support programs and increased public infrastructure spending will remain supportive of growth in the near term. Given the sharp contraction in the second quarter and the slowing pace of recovery, real gross domestic product (GDP) is expected to decline 8.1 per cent this year, the largest annual contraction in modern history.

The province is expected to see a partial rebound in real GDP next year (Chart 1), led by a strong bounce back in oil production and consumer spending. However, elevated concerns about the virus are expected to limit gains in some parts of the economy, particularly those impacted by social distancing and other public health measures. In addition, muted global oil prices will temper prospects in the energy sector, while elevated uncertainty will keep non-energy investment subdued. Real GDP is forecast to grow 4.4 per cent in 2021.

CHART 1: EXPORTS TO LEAD ECONOMIC RECOVERY

Contribution to Change in Alberta Real GDP by Expenditure



Sources: Statistics Canada, Haver Analytics and Alberta Treasury Board and Finance; f-forecast

* Includes total household, business, and government spending

Over the medium term, real GDP growth is forecast to moderate to around 3.7 per cent. As the economy moves closer to full recovery, growth will be increasingly driven by investment. Measures to support business investment, such as the acceleration of the Job Creation Tax Cut, are helping to set the foundation for growth as pandemic-related uncertainty abates. At the same time, a pick-up in population growth and a strengthening labour market will further lift consumer spending and housing activity.

The COVID-19 crisis is the latest in a series of challenges that Alberta's economy has faced in recent years, dating back to the 2014 oil price crash and 2015-16 recession. The result has been a prolonged period of weakness in the economy. Real GDP is not expected to return to pre-COVID levels, or even 2014 levels, until 2023. The recovery in the labour market will lag behind real GDP. While employment is expected to fully recover by 2022, the unemployment rate will remain elevated throughout the forecast period. Even as the economic recovery begins to take shape, real GDP per capita, a measure of standard of living, will remain below pre-COVID levels.

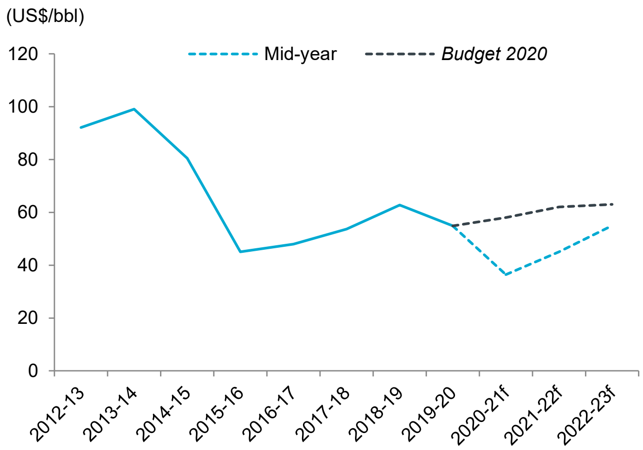
Business Sector

Moderate gains in oil prices

The recovery in global oil prices stalled heading into fall amid a resurgence in COVID-19 infections around the world, which intensified concerns about demand and the global economic recovery. Abundant supply, amid weak demand and high inventories, is expected to keep a lid on prices in the short term. WTI is forecast to average US$36.40/bbl in 2020-21. WTI is expected to improve slowly to US$45.00/bbl in 2021-22 and US$54.90/bbl by 2022-23 with the gradual rebalancing in the global oil market. (Chart 2).

CHART 2: LOWER TRAJECTORY FOR OIL PRICES

West Texas Intermediate



Source: Alberta Treasury Board and Finance, f-forecast

Oil production drives exports

A gradual ramp-up in oil production is expected to spearhead growth in real GDP. Oil production has bounced back after dropping over 800,000 barrels per day (bpd) between December 2019 and May 2020. Building on improving demand in the second half of this year, oil production is anticipated to nearly fully rebound in 2021. It is forecast to expand by an average of nearly 222,000 bpd (or 7 per cent) to reach 3.5 million bpd in 2021. Overall, total oil production in the province is forecast to climb to nearly 3.8 million bpd by 2023. It will remain a key driver of exports, accounting for roughly half of the annual growth in real overall exports over the forecast period.

Narrow differentials support prices

The differential between WTI and Western Canadian Select (WCS) has remained in a tight range since the spring, as voluntary production shut-ins have significantly eased transportation bottlenecks in the province. Export pipeline capacity is set to improve from targeted debottlenecking and the start-up of the Sturgeon Refinery and Gibson/USD's diluent recovery unit, which are expected to free up some space on the pipeline system. With export capacity anticipated to meet growing oil production, the light-heavy differential will continue to reflect pipeline transportation costs. It is expected to widen slightly from an average of US$11/barrel in 2020-21 to around US$14/bbl in the following two years. This, along with the modest improvement in WTI, will help lift WCS prices to above US$40/bbl by 2022-23.

Exports to rise

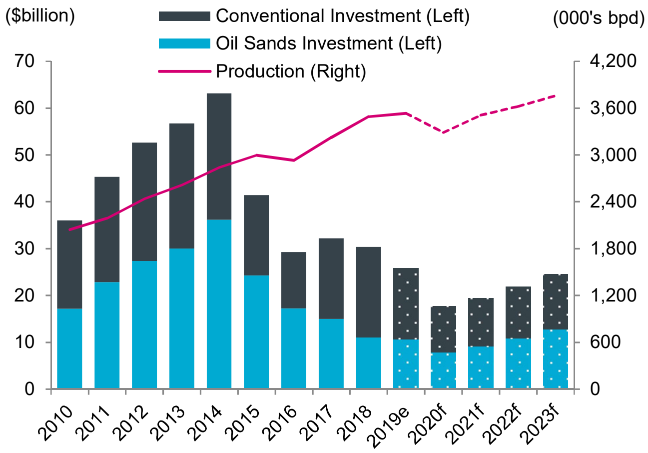
Exports have improved alongside an upturn in global activity, although slowing economic momentum in the U.S. and globally is keeping a lid on the recovery. Exports of refined petroleum products have bounced back strongly, forestry exports are nearing record highs due to strong prices and a rebound in residential construction activity. The food manufacturing sector has also held up well during the pandemic. However, other exports, such as chemicals and machinery and equipment, continue to struggle. Meanwhile, service exports are expected to be slower to pick up amid ongoing travel restrictions and sluggish recovery in business-related services. As global economic activity improves and COVID-19 impacts dissipate, non-energy exports are expected to pick up and increasingly contribute to growth in overall exports. These will help lift growth in real overall exports to around 4 per cent in 2022 and 2023.

Oil sands leads energy investment

After pulling back in 2020, investment in oil and gas extraction is expected to turn positive next year on improving demand and prices. Oil and gas investment is forecast to increase by nearly $1.7 billion, or 9.3 per cent, in 2021 after plunging more than an estimated 30 per cent this year. Growth is forecasted to accelerate in 2022 and 2023, averaging about $2.6 billion (or 12 per cent) per year. The growth in investment will be led by the non-conventional sector, with increasing spending on both sustaining capital and strategic initiatives aimed at reducing GHG emissions and improving future returns. Growth in conventional investment is forecast to be more modest and supported by growing natural gas activity. While oil and gas investment is expected to pick up, it is not expected to return to 2019 level throughout the forecast period as producers are expected to maintain capital discipline and gradually increase production (Chart 3).

CHART 3: OIL AND GAS INVESTMENT WILL REMAIN BELOW 2019 LEVELS

Alberta Nominal Oil and Gas Investment and Crude Oil Production



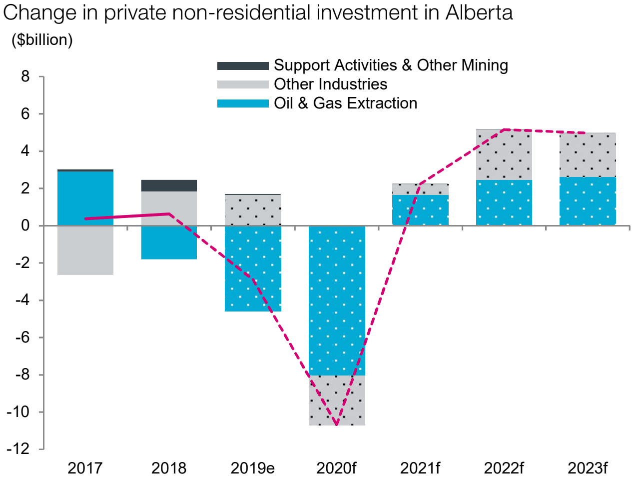
Sources: Statistics Canada, Alberta Treasury Board and Finance; e-estimate, f-forecast

Non-energy investment to pick up

Investment intentions outside the energy sector have pulled back significantly. Many companies have either delayed or cancelled expansion plans amid weaker profits and heightened economic uncertainty. Business investment outside oil and gas extraction is forecast to fall about 9 per cent this year after growing over the last two years. The weakness is being partially offset by a ramp-up in provincial infrastructure spending. Economic support measures, including the provincial government's investment in the KXL project, are also helping to support private sector investment in the near term (see page 15). Non-energy investment is expected to stabilize next year before accelerating over the medium term as pandemic-related uncertainty dissipates (Chart 4).

CHART 4: NON-ENERGY INVESTMENT TO ACCELERATE OVER THE MEDIUM TERM

Change in private non-residential investment in Alberta



Sources: Statistics Canada, Haver Analytics, Alberta Treasury Board and Finance; e-estimate, f-forecast

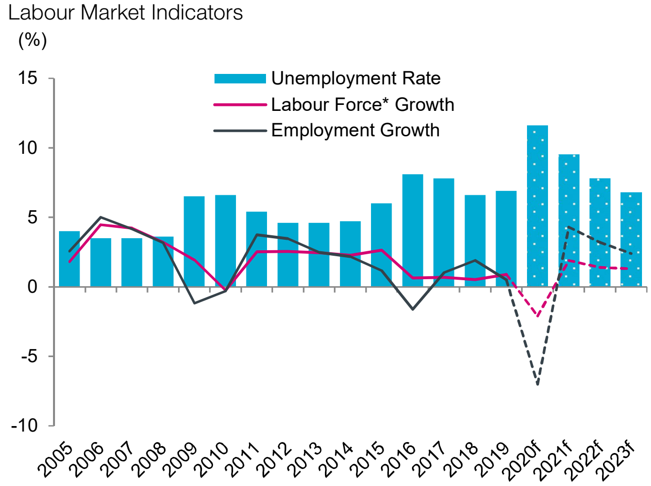
Household Sector

Protracted jobs recovery

Alberta's labour market continues to make headway, but it still has a long way to go. With the strong gains since May, employment has now recovered more than 258,000 (or 72 per cent) of the 360,900 jobs lost between February and April. Despite the improvement, employment remains more than 100,000 below February's level. Employment is forecast to contract 7 per cent in 2020. While the labour market is expected to gradually strengthen over the medium term, the road to recovery will be slow and uneven. Employment is forecast to see a partial rebound of 4.3 per cent in 2021 before growing at an average of 2.8 per cent in the following two years (Chart 5). Employment is not forecast to surpass the 2019 level until 2022.

CHART 5: UNEMPLOYMENT RATE TO EASE GRADUALLY

Labour Market Indicators



Sources: Statistics Canada, Haver Analytics and Alberta Treasury Board and Finance; e-estimate, f-forecast

* The number of people working or looking for work.

Unemployment to slowly decline

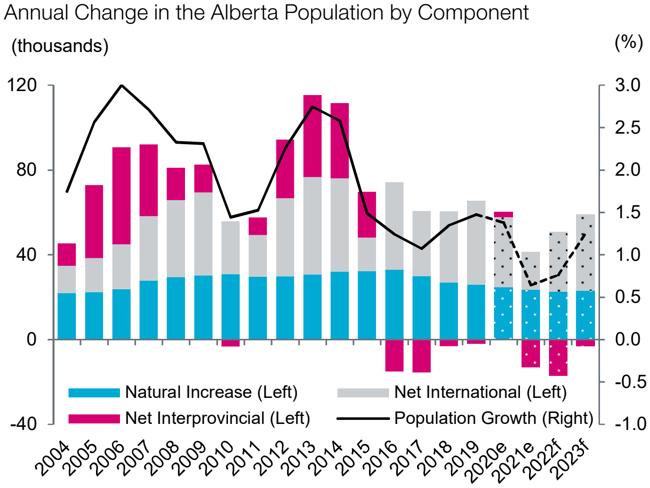
Despite the labour market improvement, unemployment in the province remains high and is expected to decline slowly. Job gains have struggled to keep pace with the increase in the number of people looking for work since the economy reopened and the unemployment rate is forecast average 11.6 per cent this year. Given the uneven recovery across industries and segments of the population, the unemployment rate is expected to decline slowly. A slower pace of labour force expansion arising from weaker migration and an aging population will help the labour market gradually rebalance over the medium term. However, given the depth of the contraction and prolonged recovery in employment, the unemployment rate is not expected to move closer to the 2019 level until 2023, when it averages 6.8 per cent.

Population growth to slow

Alberta's population growth is set to slow in the near term. International travel restrictions will continue to weigh heavily on immigration, while relatively weaker economic conditions in the province will lead to net outflows of interprovincial migrants. These factors will keep annual population growth below 1 per cent in the next two census years. Population growth is forecast to rise to 1.3 per cent in 2023 as travel restrictions are lifted and international migration is expected to return to pre-COVID levels and interprovincial outflows are expected to continue but moderate (Chart 6).

CHART 6: POPULATION GROWTH TO PICK UP AFTER NEAR-TERM SLOWDOWN

Annual Change in the Alberta Population by Component



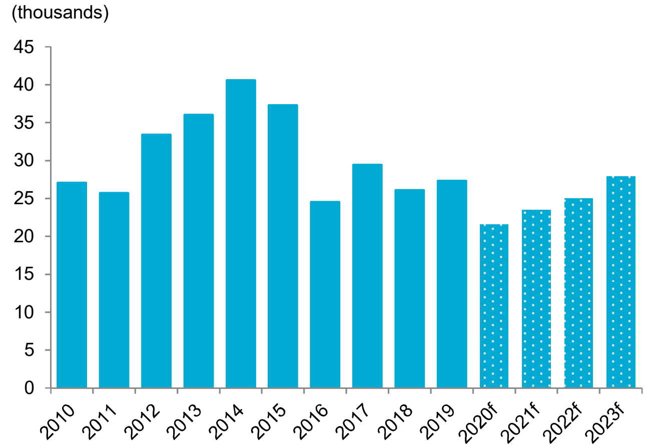
Sources: Statistics Canada, Haver Analytics and Alberta Treasury Board and Finance; e-estimate, f-forecast

Housing market resilient

The housing market has held up relatively well compared with other sectors of the economy. It has benefitted from historically low mortgage rates, pent-up demand and improving consumer confidence. Government income supports, along with mortgage and other loan payment deferrals, have also buffered the housing market from the worst impact of the pandemic. With the Bank of Canada expected to keep interest rates unchanged through 2023, low mortgage rates will continue to support housing demand in the coming years. However, slower population growth, along with the protracted recovery in the labour market, are likely to keep a lid on growth. As a result, housing starts are expected to pick up slightly to 23,500 units next year before gradually increasing to nearly 28,000 by 2023 (Chart 7).

CHART 7: HOUSING STARTS TO RISE BUT REMAIN BELOW BUDGET EXPECTATIONS

Alberta Housing Starts



Sources: Canada Mortgage and Housing Corporation, Haver Analytics and Alberta Treasury Board and Finance; f-forecast

Services a drag on spending

The recovery in consumer spending has outpaced other parts of the economy, as government income support programs have blunted the impact of the pandemic on household incomes. Retail sales have now surpassed February levels. However, spending in some discretionary categories, such motor vehicle sales and clothing, has remained lacklustre and spending on services – which account for nearly 60 per cent of overall consumer spending – remains weak, reflecting pandemic-related impact on travel, restaurants, and entertainment. Lingering concerns over the virus and prolonged recovery in the labour market will likely restrain growth in real consumer spending next year. After declining by more than 6 per cent this year, it is forecast to partially rebound by 5.6 per cent in 2021. It is expected to improve further in 2022 and 2023 as population growth picks up and the labour market improves.

Risks to Outlook

The uncertainty surrounding the pandemic creates a number of risks to the Alberta economy and provincial government revenues. For example, a severe and prolonged second wave of infections leading to a broad-based shut down of economies around the world would derail the recovery in global demand and prolong the rebalancing in global oil markets. On the upside, a stronger than expected recovery in the global economy would pave the way for a faster rebalancing in the global oil market.

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