

# Economic Trends

September 2021

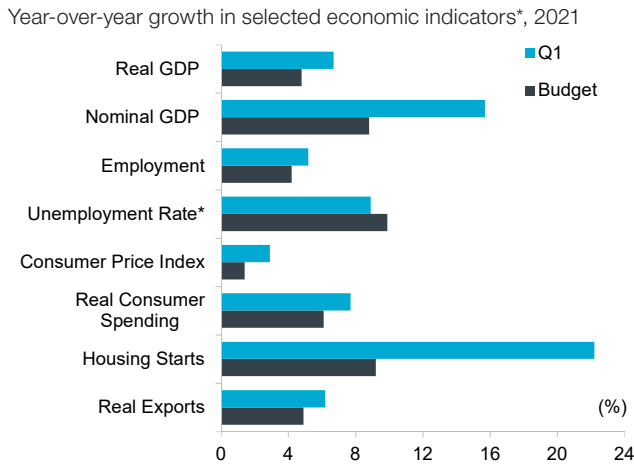
This month's Economic Trends is taken from the [Economic Update](#) of the 2021-22 first quarter fiscal update and economic statement, released on August 31, 2021.

## Overview

Recovery in the Alberta economy in the first half of the year surpassed [Budget](#) expectations. The Alberta Activity Index, a measure of provincial economic activity, rose nearly 9% through May. All components rebounded, led by the household sector, which includes consumer spending and housing activity. Significant progress on vaccinations, along with declines in COVID-19 infections and hospitalizations, led to the reopening of the Alberta economy in the summer. This sets the stage for a broader recovery in the second half of the year. However, with the spread of more contagious variants, the pandemic continues to pose risks to the outlook.

After last year's historic estimated contraction of 8.2%, Alberta's real gross domestic product (GDP) is now forecast to rebound 6.7% in 2021. This is up significantly from the [Budget](#) forecast of 4.8% (Chart 1). Growth is forecast to moderate to 4.3% in 2022. With the stronger outlook, real GDP is now anticipated to return to 2014 levels next year.

### CHART 1: OUTLOOK IMPROVES DRAMATICALLY SINCE BUDGET 2021



Source: Alberta Treasury Board and Finance; \*Unemployment rate is forecast level

Even so, sectors of the economy are expected to recover at different paces. This will result in an uneven employment recovery and gradual decline in the unemployment rate.

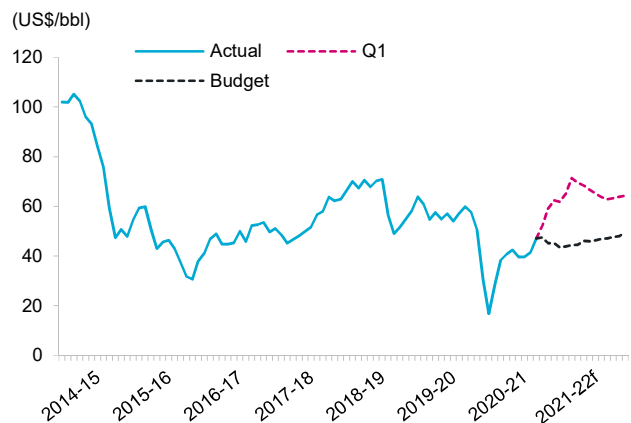
With higher oil prices, incomes are expected to rebound more strongly than real output. Nominal GDP, a broad measure of income, is forecast to grow 15.7% and return to 2019 levels this year.

## Stronger oil prices

The recovery in oil prices has been much stronger than expected. The improvement in global petroleum demand has outstripped supply, underpinned by a solid pickup in the global economy and ongoing output restraint by OPEC+. This has fueled a strong rally in oil prices. West Texas Intermediate (WTI) has risen more than 40% since the beginning of January and has now surpassed pre-pandemic levels. Demand-related risks due to COVID, however, remain high. Prices have softened recently as the rapid spread of the Delta variant is raising concerns about the global recovery. WTI is forecast to average US\$65.50/bbl in 2021-22, US\$19/bbl higher than [Budget](#) (Chart 2).

### CHART 2: SIGNIFICANT IMPROVEMENT IN OIL PRICES

West Texas Intermediate



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



Meanwhile, the differential between WTI and Western Canadian Select (WCS) is expected to remain in line with pipeline transportation costs in the near term, averaging US\$13/bbl in 2021-22. The U.S. portion of Enbridge's Line 3 replacement is nearing completion, which will bolster pipeline takeaway capacity this year. This will help lift the WCS price to around US\$52/bbl in 2021-22, the highest annual average since the 2015-16 downturn. The uplift in oil prices will be tempered by a higher Canadian dollar, which is now forecast at 79.1 US¢/Cdn\$ in 2021-22, 1.7 cents higher than *Budget*.

## Business output ramps up

Business output has staged a remarkable recovery so far this year. Manufacturing shipments and international goods exports have risen more than 25% year-to-date and now exceed pre-pandemic levels (Chart 3). While energy products have led the gains, the value of non-energy exports remains at a record high, buoyed by food manufacturing, chemical and forestry products. The latter has benefitted from strong lumber prices and residential construction activity. One category that continues to lag behind is machinery manufacturing, which has been weighed down by the slow recovery in U.S. drilling activity.

**CHART 3: BUSINESS OUTPUT SURGING**

Alberta's merchandise exports and manufacturing shipments



Sources: The Bank of Canada and Haver Analytics

With the strong rebound in output, real exports are forecast to increase more than 6% in 2021. However, ongoing travel restrictions and pandemic-related concerns will limit the growth in service exports this year. As service exports pick up, overall exports are forecast to rise almost 5% in 2022.

## Incomes bounce back

Household and corporate incomes in the province are expected to continue to see a swift recovery. Corporate earnings are rising on the back of stronger-than-expected commodity prices and a rebound in economic activity. While federal government income supports to individuals have eased from last year's exceptionally high levels, they remain elevated. This, along with an improving labour market, will continue to support household incomes. Nominal GDP, a broad measure of income, is forecast to grow 15.7% in 2021, compared to 8.8% growth forecasted at *Budget*. It is forecast to return to 2019 levels this year. The strong rebound in incomes will translate to better-than-expected provincial government revenues this fiscal year.

## Cautious optimism in energy sector

There is more optimism in Alberta's oil and gas sector. The rebound in prices and production has boosted cash flows and strengthened financial positions among producers. Drilling activity is picking up after a slow start to the year, with rig counts exceeding 2019 levels in June and July. Oil sands production has also risen more than 8% in the first half of the year amid a quick rebound in bitumen output.

With the ramp up in activity, the composition of investment growth is expected to shift to the conventional oil and gas sector. Meanwhile, growing bitumen production is expected to lift sustaining capital in the non-conventional sector. However, oil sands producers are anticipated to maintain capital discipline as they focus on debt repayment and returns to investors.

After plunging an estimated 37% last year, oil and gas investment is forecast to grow 22% to reach nearly \$20 billion this year. This improvement is expected to continue in 2022.

## Non-energy investment rising

Investment outside oil and gas is anticipated to see a solid recovery this year. Industrial investment is getting a lift from expansions in petrochemical manufacturing, transportation, renewable energy and agricultural infrastructure. Commercial investment has also turned a corner amid higher investment in trade and services, as well as warehousing. The latter is benefitting from a shift towards e-commerce. Non-energy investment is forecast to grow at about 5% per year in 2021 and 2022, and will return to 2019 levels this year.

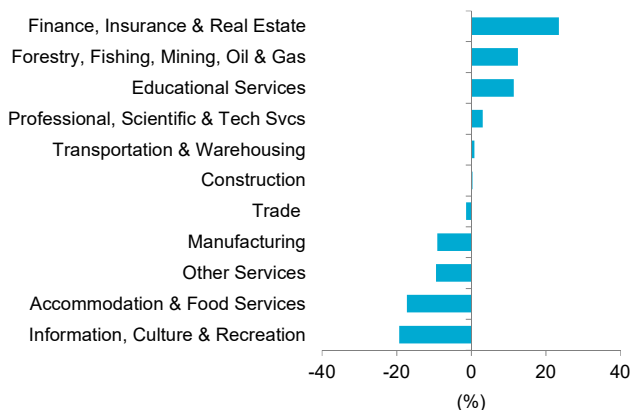
## Labour market recovering

Alberta's labour market continues to strengthen. The province has added more than 70,000 jobs since the start of the year and gained back nearly 90% of the jobs lost during the pandemic. Despite the double blow of COVID-19 and the oil price crash last year, Alberta's employment recovery is in line with Ontario and ahead of other resource-based provinces. The unemployment rate has also fallen to 8.5%, the lowest since the pandemic started.

A complete recovery, however, will take more time. Employment in some industries continues to lag behind, especially in tourism-related and other services, including personal services (Chart 4). Linger concerns over the virus and other factors also appear to be weighing on the recovery in the labour force participation, particularly among youth and women aged 35-39 years old. This is likely contributing to hiring challenges faced by some sectors as the economy reopens and activity bounces back. Employment is now forecast to grow 5.2% and the unemployment rate to average 8.9% this year, better than *Budget* expectations. This improvement is expected to carry into next year, when the pandemic subsides further and the recovery in the services sector gains more traction.

### CHART 4: SOME HARD HIT INDUSTRIES CONTINUE TO LAG BEHIND

Percentage change in employment since pre-COVID (February 2020) levels



Source: Alberta Treasury Board and Finance

Average weekly earnings (AWE) are normalizing as the labour market improves. Last year, significant job losses in the lower-paying services sector lifted AWE to elevated levels. As these compositional effects from the pandemic dissipate, AWE are forecast to fall 1% this year before growing again in 2022.

## Cost pressures picking up

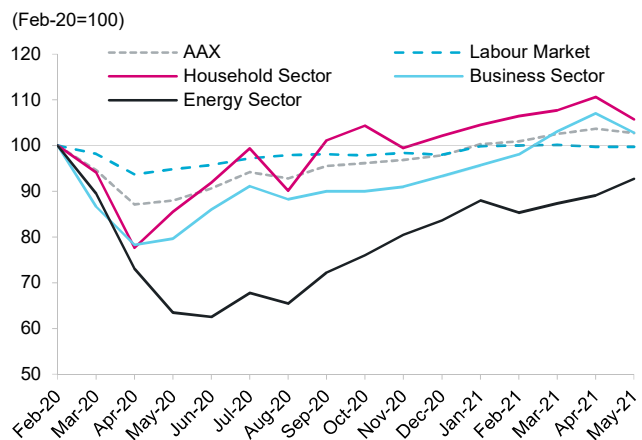
Both businesses and consumers are facing higher costs. Construction costs accelerated the most in the residential sector, where they were up nearly 21% through June. Strong demand, along with supply constraints, pushed lumber prices to record highs in the second quarter before pulling back recently. Non-residential building construction costs were also up 2.6% over the same period. Prices for motor vehicles and imported appliances are rising amid supply chain bottlenecks caused by global chip shortages and constrained shipping capacity. Gasoline prices have also jumped from last year's depressed levels, while food prices have picked up since the start of the year. Consumer inflation is now expected to accelerate to 2.9% this year, 1.5 percentage points higher than at *Budget*. As the impact of these temporary factors fades, inflation is expected to moderate to 2.4% in 2022.

## Households drive growth

The household sector, which includes consumer spending and residential construction activity, has been a significant driver of Alberta's economic rebound (Chart 5). Housing starts averaged over 31,000 units through July, underpinned by low mortgage rates and a rebound in consumer confidence. Housing starts are now forecast to average over 29,000 in 2021, up from 26,000 at *Budget*. They are forecast to rise to nearly 30,000 units next year.

### CHART 5: HOUSEHOLD SECTOR LEADING THE RECOVERY

Alberta Activity Index major components indexed to February 2020 levels



Source: Alberta Treasury Board and Finance

Despite rising COVID-19 infections and tighter public health measures in the first quarter of the year, consumer spending has stayed strong. Retail spending has reached a record high and was up 8% between December 2020 and June 2021. The strength in the housing market has buoyed sales in housing-related categories such as building materials, furniture and appliances. Sales at gasoline stations have also risen on the back of higher prices. With the economy reopening, consumer spending is expected to see a more broad-based recovery. Spending on restaurants, accommodation and other travel-related services is anticipated to pick up from strong pent-up demand and accumulated household savings. After contracting an estimated 8.2% last year, real consumer spending is forecast to grow 7.7% in 2021 and 5.2% in 2022.

## Risks to Outlook

Risks to the outlook have become more balanced since *Budget* with broader vaccination rates and an improvement in oil prices. However, the rapid spread of the Delta variant could dampen the global recovery and lead to a sharper pullback in commodity prices and demand, including oil. A stronger-than-expected increase in OPEC+ or U.S. production could also weigh on oil prices. At the same time, a resurgence in COVID-19 infections in Alberta could also derail the recovery in the second half of the year. On the upside, containment of the Delta variant and a strengthening global recovery could lead to sustained higher oil prices and exports.

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