THE ECONOMY IN BRIEF

DEPARTMENT OF FINANCE — MARCH 2000

KEY MESSAGES

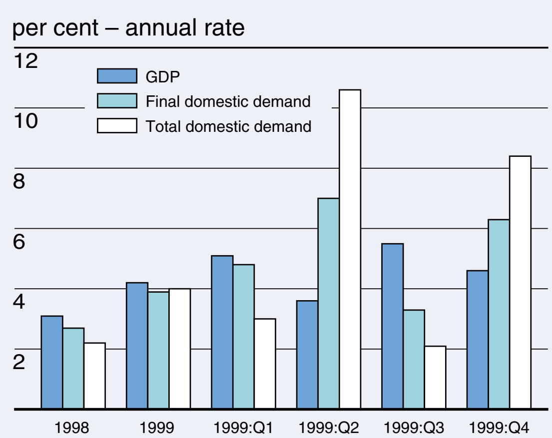
- In the fourth quarter of 1999, real gross domestic product (GDP) grew sharply, rising 4.6% following an even larger gain of 5.5% in the third quarter. This brought output to 4.7% above its level a year earlier. For 1999 as a whole, the increase in real GDP was 4.2%.
- Demand growth in the quarter was strong and balanced. Both domestic and foreign demand rose robustly, boosting Canadian production. Total domestic demand growth strengthened to 8.4%, with particularly sharp increases in machinery and equipment and inventory investment. Real export growth moderated to a still strong 7.4%. That plus stronger import growth to satisfy the increased demand, especially in categories with a high import content such as machinery and equipment and inventory investment, led to a drop in net exports, detracting from output growth in the fourth quarter.
- The nominal trade surplus decreased noticeably despite a gain in the terms of trade (import prices fell). The current account deteriorated from a surplus of about $2 billion in the third quarter to a deficit of about $5 billion, or 0.5% of nominal GDP, in the fourth. However, this is still a marked improvement relative to the average deficit of 1.8% of nominal GDP in 1998, with the current account deficit for 1999 as a whole standing at $4.3 billion, about one quarter its 1998 level.
- With over 427,000 net new jobs created during 1999, a further gain of about 44,000 in January 2000 brought net job creation to over 471,000 since the end of 1998. Full-time jobs accounted for more than the total net gain. The unemployment rate in January 2000 remained at 6.8%, the lowest rate dating back to April 1976.

SUMMARY[1]

In the fourth quarter of 1999, the Canadian economy continued its robust performance, with both increased domestic and foreign demand. Total domestic demand (spending by Canadian consumers, business and government on goods, services, housing and plant and equipment plus inventory accumulation) growth was stronger than in the third quarter (Chart 1). But export growth slowed and with imports satisfying a larger part of the growing domestic demand than in the third quarter, overall growth was below that in the third quarter. Meanwhile, cost and inflation pressures remained subdued.

[1] Unless otherwise noted, data and per cent changes are quoted at annual rates. The cut-off date for data is February 28, 2000.

Chart 1
Growth in real GDP and real domestic demand



Final domestic demand is spending by Canadians on goods, services, housing and plant and equipment. Total domestic demand is final domestic demand plus inventory accumulation.

Department of Finance Canada — Ministère des Finances Canada

Canada

Main economic indicators
(per cent change at annual rates unless otherwise indicated)

	1998	1999	1999:Q2	1999:Q3	1999Q:4	Most recent	
Real gross domestic product	3.1	4.2	3.6	5.5	4.6	–	
GDP excluding inventories	3.6	4.1	0.3	6.8	2.5	–	
Final domestic demand	2.7	3.9	7.0	3.3	6.3	–	
Government expenditure	2.0	1.8	2.1	2.3	3.6	–	
Consumer expenditure	2.8	3.2	4.8	3.9	3.8	–	
Residential investment	-1.9	6.5	15.8	3.9	8.1	–	
Business fixed investment	5.7	10.4	23.1	2.0	21.9	–	
Non-residential construction	0.1	2.8	3.3	3.6	9.3	–	
Machinery and equipment	9.5	14.9	35.6	1.2	29.1	–	
Business inventory change[1]	-0.4	0.1	3.3	-1.2	2.0	–	
Trade balance[1]	1.0	0.2	-5.8	3.3	-4.5	–	
Exports	8.2	9.7	1.2	15.0	7.4	–	
Imports	5.8	9.7	18.6	6.5	21.2	–	
Current account balance							
(nominal $ billion)	-16.4	-4.3	-8.0	2.1	-5.0	–	
(percentage of GDP)	-1.8	-0.5	-0.9	0.2	-0.5	–	
Real personal disposable income	2.4	2.3	3.4	2.3	4.0	–	
Profits before taxes	-6.0	25.2	28.4	58.4	35.1	–	
Costs and prices (%, y/y)							
GDP price deflator	-0.6	1.7	0.9	2.5	3.1	–	
Consumer price index	0.9	1.7	1.6	2.2	2.4	2.3	2000-Jan
CPI – excluding food and energy	1.3	1.5	1.5	1.6	1.6	1.4	2000-Jan
Unit labour costs	0.9	0.3	-0.2	0.5	1.0		
Wage settlements (total)	1.7	2.2	2.4	2.3	2.9	2.3	99-Dec
Labour market							
Unemployment rate (%)	8.3	7.6	7.8	7.6	7.0	6.8	2000-Jan
Employment growth	2.7	2.8	2.5	2.2	3.5	3.7	2000-Jan
Financial markets (average)							
Exchange rate (cents U.S.)	67.48	67.32	67.90	67.30	67.90	68.91	28-Feb-2000
Prime interest rate (%)	6.60	6.44	6.33	6.25	6.42	6.75	28-Feb-2000

[1] Annualized change expressed as a percentage of GDP in the previous period.
Sources: Statistics Canada, the Bank of Canada and Human Resources Development Canada.

Canadians go shopping

Real consumer expenditure increased a solid 3.8% in the fourth quarter, only slightly off the pace of the previous two quarters. The gain in spending on durables, such as automotive products and furniture and appliances, moderated from its very strong pace but growth in spending on services doubled its pace of the previous quarter.

Personal income grew 4.8% in the fourth quarter, about the same pace as in the third. Labour income growth picked up modestly as growth in employment was much stronger than in the third quarter.

With personal income taxes rising at a slower pace than in the previous quarter and marginally slower than personal income, real personal disposable income growth jumped to 4.0%.But with continued strong growth in consumer spending, the personal savings rate remained unchanged at 1.1%.

Investment activity rockets

Business investment in plant and equipment soared 21.9% in the fourth quarter, a much stronger pace than in the previous quarter. Investment in machinery and equipment and non-residential construction both grew significantly faster than in the third quarter. Machinery and equipment investment jumped nearly 30% after a very modest rise in the previous quarter, with virtually all major categories registering significant gains. Non-residential construction rose about 9%, with a strong gain in engineering projects being moderated by a drop in building construction.

Residential investment growth also more than doubled its pace in the previous quarter. Increased housing starts boosted new construction activity while renovations also registered a substantial gain following a decline in the third quarter. These more than offset a sharp decline in transfer costs, as sales of existing houses fell in the fourth quarter.

Inventory investment jumps

Businesses raised their inventories by $9.1 billion in the fourth quarter following an accumulation of $4.9 billion in the third quarter. With stronger demand boosting sales relatively more than the increase in inventories, the economy-wide inventory-to-sales ratio nonetheless dropped to its lowest recorded level.

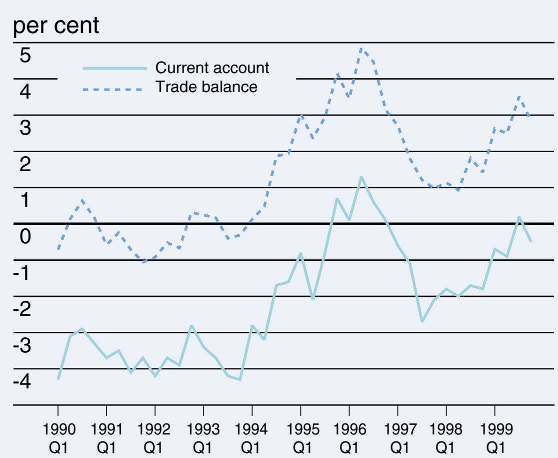
Exports up but imports up more

Increased foreign demand for Canadian products contributed to a gain of 7.4% in real exports in the fourth quarter. A major factor behind rising exports has been strong growth in the United States economy and the ongoing recovery in countries affected by the financial crisis of 1997-1998. Meanwhile, total real imports by Canadians rose 21.2% in the fourth quarter, reflecting the jumps in consumer spending on goods and business investment in machinery and equipment and inventories.

Current account deficit smaller in 1999

A deterioration in the real merchandise trade balance dominated an improvement in the terms of trade, yielding a smaller nominal merchandise trade surplus than in the third quarter. This resulted in the current account moving from a surplus of $2.1 billion to a deficit of $5.0 billion, or 0.5% of nominal GDP (Chart 2). Nonetheless, this is a considerably smaller deficit than those seen in 1997 and 1998. Indeed, the current account deficit for 1999 as a whole was only about one quarter that of 1998.

Chart 2
Current account as a percentage of nominal GDP



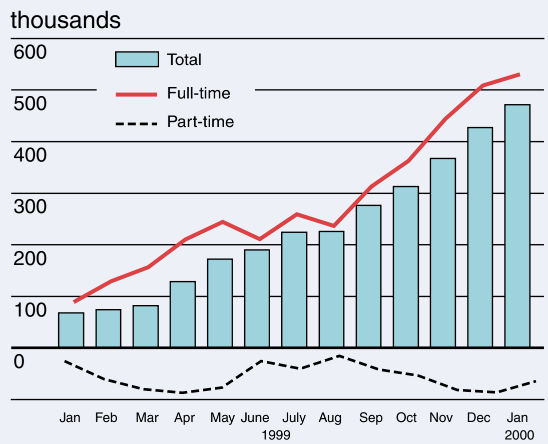
Inflation subdued while profits jump again

Underlying price and cost pressures remained subdued in the fourth quarter. The implicit and chain price indices for GDP both advanced somewhat more than 3% over the last four quarters. Consumer price inflation ticked up to 2.6% in September on a year-over-year basis and again in December, owing in part to the temporary impact of higher energy prices. CPI inflation eased back to 2.3% in January.

Labour productivity, measured as output per employed person, rose again in the fourth quarter, although at a slower pace than in the third. Labour costs per unit of output rose modestly from their third quarter level and were 1.0% above their level of a year earlier.

Pre-tax corporate profits surged another 35.1%, the fifth consecutive double-digit increase. The gains in the quarter were widespread among industries, with both financial and non-financial corporations showing solid gains. Profits rose to 11.8% of nominal GDP and to a level 38.7% above that of a year earlier.

Chart 3
Cumulative employment growth since December 1998



Lowest unemployment rate in 24 years

Fourth quarter employment increased 3.5%, with over 427,000 net new jobs created during 1999. A further 44,000 net new jobs were created in January 2000 for a six-month gain of nearly 250,000 jobs (Chart 3). This raised the total increase to over 471,000 jobs since the end of 1998. Full-time jobs grew even faster, exceeding the total net gain as part-time employment fell. The unemployment rate in January 2000 remained at 6.8%, the lowest rate since April 1976.

The Canadian dollar maintains gains

After trading around 65 cents U.S. in the last quarter of 1998, the Canadian dollar strengthened along with world commodity prices. It peaked near 69 cents U.S. in early May before losing ground to trade near 67 cents U.S. It has since rebounded to near 69 cents U.S. On February 28, it closed at 68.91 cents U.S.

Since May, Canadian market interest rates have risen along with those in the United States. Most recently, on February 26 the U.S. Federal Reserve raised the target for the Federal Funds Rate from 5.50% to 5.75%, its fourth round of monetary tightening since mid-June 1999. These moves were aimed at staving off inflationary pressures that might arise from a tight U.S. labour market, continued strong U.S. domestic demand and firming foreign economies.

The Bank of Canada matched the February increase by the Federal Reserve, as it had in November 1999. However, interest rates in Canada have generally remained below those in the United States, especially short-term rates. The differential between Canadian and U.S. 3-month Treasury bill yields widened from under 40 basis points in mid-November 1999 to over 80 basis points on February 28, 2000.

The main source of data used in this publication is Statistics Canada. Subscription inquiries should be directed to the Distribution Centre at (613) 995-2855. For other inquiries about this publication, contact Mostafa Askari at (613) 992-3055.
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