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PROVINCIAL OVERVIEW:

Present estimates by the Conference Board of Canada place B.C. real GDP growth at 1.9% for 1987. This is a decline from last year but healthier growth is expected in 1988, at 2.8%. Personal disposable income is expected to rise; real consumer expenditure should remain at current levels; and inflation could rise slightly. One continuing trouble spot is the level of unemployment which is expected to settle at 13.3% this year and to dip only slightly in 1988.

As is consistent with a persistent disparity, 1987 national real growth is stronger than that for B.C. - the same will hold for 1988 as national GDP rises to 3.0% from its present 2.5%. The difference between the provincial and national growth derives from the slump in B.C.'s mining and moderating growth in tourism this year while the eastern economy has been boosted by the auto industry and housing starts. If national growth slows beyond 1988 as expected, the difference between B.C. and central Canada will lessen correspondingly.

In early 1987, lower oil prices, falling wage rates and high unemployment had a particularly direct affect on the B.C. economy because of our trade dependence. World commodity prices, elevated supply and demand competition for goods and services, and the health of the U.S. economy all have a direct impact on the cost of living in B.C. and on the value of commodities produced within the province. These forces have conspired to the disadvantage of B.C. over recent years. However, there is some firming of international commodity prices and this bodes well for the future. In regard to the U.S. economy, the current downturn in housing, production, and business starts, will have a negative impact on B.C. in the future.

SECTORAL:

The modest growth in B.C. in 1987 is mainly due to high unemployment levels, continued low capital investment and a slow down in the goods producing industries, for example: fall in demand for coal, copper, lead, zinc and other industrial materials. On the positive side, the forestry industry is currently enjoying a boom (especially in regard to pulp and newsprint), the service sector is performing better than expected and some growth is anticipated for most sectors of B.C.'s mining and oil and gas industries in 1988.

SUB- REGIONS:

Northwestern B.C. is experiencing increased interest in regional economic development as seen by new interest in oil and gas exploration, increased investment in the wood industry and the impact of port investment at Prince Rupert. These developments will help accelerate growth in the region, a welcome prospect after the severe and lingering recession.

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SECTORAL TRENDS AND INDUSTRY ISSUESForestry

The recent boom in the forestry industry has created, for the first time since the recession, an excess of cash flows over capital expenditures. Ross HayRoe of the Papertree Letter indicates that companies will now be more cautious in planning expenditures than they were prior to the 1981/82 recession. Future spending priorities may emphasize modernization and other improvements rather than acquisitions of firms.

While the forest industry is recognizing the importance of value added, older mills are still necessarily geared to volume. MacMillan Bloedel is taking the lead among majors, by selectively moving away from volume processing towards value-added. It appears this focus will require wholly modernized, new or restructured plants since value added and volume production are widely incompatible within the same mill.

The restructuring approach begun in the early 1980's in plywood is being adopted elsewhere in the wood products industry. Recently, employees of Evan's Products of Golden, B.C. agreed to buy the company from its U.S. parent. The trend

of employee ownership is on the rise as workers attempt to turn troubled companies into profit making ventures.

Repap Enterprises of Montreal (who operate a pulp mill in Prince Rupert) appear to have developed a new sulphur free pulping process. Energy savings enable lower capitalization and thus the potential for the restructuring of the industry to smaller, lower capacity mini mills. The process works but the resulting paper is darker and weaker.

Tourism

Tourism consultant L.J. D'Amore and Associates has recently indicated that the trend in tourism in the U.S. is moving towards experience and adventure, not just destination travel. Given the highly competitive destination resort market, a potential market niche for Whistler, as an example, could be to promote adventure travel packages coupled with the resort community atmosphere.

The pressure on airlines to increase the number of overseas flights coming into Canada and the potential length of stay allowed for cruise passengers may prove to be a significant boost to the B.C. industry.

Current travel packages don't allow the extension of stay beyond that of the scheduled cruise length.

The B.C. cruise ship industry is currently enjoying an upturn as more companies, such as Sea Ventures of Miami, choose Vancouver as a home port for the 1988 Alaska Cruise season. However, proposed amendments to the Jones Act (which requires that all foreign ships, after leaving an American port, proceed to a foreign berth before re-entering the U.S.), could reduce foreign cruise business for the city of Vancouver.

A DRIE study is being conducted by Coopers Lybrand on a long term tourism strategy for Vancouver and its hinterland. The focus is on the development of an approach to exploit Vancouver's role as a gateway. This may guide future tourism programming in B.C. and is timely in respect to the national park development of South Moresby Island.

Marine Industries

Because of the dwindling U.S. gas supplies and a lack of exploration south of the border, there may be a turnaround for the currently depressed oil and gas industry in Canada. This

SECTORAL TRENDS AND INDUSTRY ISSUES (cont'd)

potential demand increase, along with announced royalty and tax relief, could boost exploration and development activity in B.C.

Chevron plans to explore for oil and gas north of Vancouver Island now that the moratorium has been lifted. The company is taking a leading role by resuming exploration in frontier areas. If results are positive, this could mean new impetus for a B.C. based supply industry, in particular, ship repair and the transportation sector. The immediate economic impact will be modest however. Environmentalists remain concerned.

The soon to be removed container clause (which allows Vancouver long shoremens to repack containers) could become a major force in boosting the competitiveness of the Port of Vancouver. Industrial Inquiry Commissioner Joe Weiler has indicated that removal of the clause should provide long run impetus for increased investment in the port, more effective marketing and enhanced cooperation. Employment levels should not be affected, as a work guarantee and a joint training and productivity fund will be set up.

Advanced Materials

The pace and volume of research on superconductors worldwide, indicates that the technology is offering commercial promise. B.C. is participating through its resident R&D expertise. This is demonstrated by the recent NSERC research grants awarded to U.B.C. and McMaster. The present study on the potential for advanced manufacturing in ceramics, which has been jointly funded by DRIE and the Provincial Government under the IDA, may offer the basis for further investment.

Small Business

Capital financing for B.C. small businesses may improve with the introduction in February of the new B.C. Securities Act and the implementation of major deregulatory changes at the end of June 1987. These changes, aimed at allowing banks, insurance companies and credit unions, as well as non-residents to directly enter the B.C. securities market, are expected to increase competition among financial institutions, and to create overall a better response to meeting the financing needs of junior companies.

Additionally, venture

capital needs may be more easily met through changes in the provincial Business Venture Capital Act which allows access to smaller projects while increasing the maximum level of financing.

Services

The federal/provincial Asia Pacific Centre Memorandum of Understanding (MOU) on Trade, Commerce and Travel promises to highlight the service sector in B.C. as an important contributor to regional economic development. The private sector Advisory Committee established under the MOU has set up task forces to examine expansion of financial, legal and other business services, the enhancement of transportation infrastructure, the export of professional and technical expertise and the improved coordination of international tourism marketing. The MOU calls for \$6 million in expenditures over 3 years. This agreement is clear recognition of B.C. as the gateway to the Pacific Rim; it will provide new impetus for service industry growth over the long-term.

SPECIAL FEATURE: Federal Tax Reform and the Manufacturing & Service Sectors

The June tax reform proposals will bring manufacturing companies' tax rates more in line with the average Canadian corporation.

The service sector has fared well so far, but must wait for the new sales tax system to really assess the impact. Some of the more significant effects on the manufacturing and service industries are described below.

The most significant impact on the manufacturing sector is the sharp limitation in the way they can write-off equipment and machinery. MacMillan Bloedel has indicated that its capital-cost allowance will fall by more than \$40M a year, increasing its taxable income by that amount. Another new rule, which would take effect in 1990, will permit MacMillan Bloedel and others to depreciate equipment only once it is in use. But because pulp mills often take 2-3 years to build, the assets will be in the ground long before the company can take a write-off. The tax changes are expected to reduce company cash flows and the overall level of capital expenditures. Manufacturers will retain their deduction for research and development costs. This will serve as an incentive to continue to conduct research and

development.

Burns Fry Limited has expressed the view that the B.C. forest industry has no reason for complaint with the tax reform proposals. B.C. companies will remain competitive with their US counterparts in terms of tax rates and depreciation schedules because they have kept the advantage of not having a minimum tax which exists in the U.S. The cash advantage allows B.C. companies to pay down debt or to catch-up on capital spending.

Mining retains most of its preferential tax treatment and is helped by the general cutting of corporation tax rates. But, it will end up paying more taxes overall. Mining companies will no longer be able to use earned depletion, which allows mines to generate tax deductions that exceed amounts actually spent for certain exploration and resource development. For this reason, experts are saying that the mining industry is one of the losers in tax reform. The Globe & Mail states that the only positive feature is that mining companies can still deduct all capital expenses for new mines before paying any taxes. They can continue to take a resource allowance which generally

exceeds provincial royalties. In addition, they can still attract outside investment using flow-through shares, which pass on tax incentives directly to shareholders. Mining companies will also be able to continue to benefit from the deduction for research and development, when they develop new extraction techniques. The general impact could be the careful planning of future projects which will be of a lasting viable nature.

Firms within the services, high-tech, retail and wholesale trade industries and other companies with low levels of capital investment, will be better off from the proposed cut in corporate tax rates. On the high-tech side, Wood Gundy states that this sector should continue as before to attract government support as a designated core industry to B.C.'s future industrial base.

Overall, experts feel that the first phase of tax reform is analogous to the calm before the storm. The second phase is intended to replace perceived inadequacies of the federal sales tax system. It is expected to have far reaching implications for British Columbia.

CALENDAR OF SELECTED EVENTS

- Meetings to discuss the provincial government's proposed changes to its forestry stumpage system will occur:
 - Williams Lake - July 20, 1987
 - Prince George - July 22-23, 1987
 - Smithers - July 24-25, 1987
 - Kamloops - July 27-28, 1987
 - Nelson - July 29-30, 1987
 - Vancouver - July 29-31, 1987
- Free Trade: August 6, 1987 - White House must submit a process report to Congress. October 3, 1987 - President must inform Congress of intention to enter a free trade agreement. Congress has 90 days to consider.
- Federal Tax Reform: The deadline for written submissions to the Commons Finance Committee on tax reform is August 18, 1987. Public Hearings are scheduled to begin August 31, 1987 with the committee arriving in Vancouver September 21, 1987.
- The 17 year old Vancouver Ports container clause may be abolished as early as September 1, 1987 or as late as September 30, 1987.
- The B.C. Ministry of Economic Development and Douglas College are sponsoring a one day seminar on "Ways to Encourage Economic Development at the Community Level" in the Fall of 1987.
(Call 387-0279)
- On four successive Tuesdays in October 1987, U.B.C. will hold seminars on topics of Community Economic Development.
(Call 222-2181)
- The Ministry of Economic Development and the University of Victoria are sponsoring a four (4) day seminar on "Promoting Import Replacement in a Resource Based Economy", October 27, 1987 to October 29, 1987.
(Call 387-0279);
- The 17th Annual Economic Outlook Conference will be held on November 18, 1987 at the Four Seasons Hotel in Vancouver.

This quarterly bulletin is prepared by Strategic Planning Division,
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