ECONOMIC CLIMATE
for BARGAINING

September 2007 **Vol. 4, No. 3**

Frontline Summary

Economic weaknesses coming home to roost discusses how the housing-related slowdown in the U.S. economy and related developments here might affect our economy. This section also includes a consensus forecast of major economic indicators for Canada and the provinces.

Housing bubbles and busts. House prices in Canada, as in the United States, have increased at more than three times the rate of inflation during the past decade, creating an additional $500 billion plus of household wealth, at least on paper. With rising interest rates, we may soon be in for a decline in house prices. Real estate "busts" have much deeper and longer effects on the economy than stock market busts.

"Building Canada": dismantling the public sector? focuses on the set of 2007 federal budget policies to promote and subsidize public-private partnerships (P3s), illustrates public sector capital investment by sector and briefly summarizes the state of P3 projects in different provinces.

Employment growth strong, but becoming lopsided. Canada has had a period of remarkably strong employment growth and record low unemployment rates. The strong labour market is not only providing many new jobs, but has helped to provide workers with long-overdue real wage raises. But private sector job growth is looking increasingly lop-sided: much of the growth in new jobs has come from sectors such as construction and trade, which could suffer considerable job loss in a downturn. Fortunately, there has been decent job growth in the public sector, which will continue to strengthen the economy and our communities.

Equality on hold. After six years of rising wages and a slowly but gradually narrowing gender wage gap, women's pay equality in the labour market seems to be on hold again. Progress to reduce the gender gap would benefit not just women, but the whole economy.

Rising mortgage rates lifting inflation. Inflation is rising because of three factors: higher food prices, housing price increases and the booming Alberta economy. It's not just higher house prices that are increasing the cost of home ownership: now rising mortgage rates are pushing up the cost of living. This section also summarizes regional inflation trends and expectations.

Wage increases deliver more real gains. Union members have continued to achieve decent gains in average wage settlements this year, building on wage increases from the past few years. Further decent wage gains are expected next year.

Next Issue: December 2007

Please contact Toby Sanger (**tsanger@cupe.ca** or 613-237-1590 ext. 241) if you wish to propose corrections, suggestions, contributions or if you have any questions.

ECONOMIC CLIMATE *for* BARGAINING

Economic weaknesses coming home to roost

The United States economy is now well into orange alert territory. After years of unsustainable growth based on inflated house prices, borrowed money, tax cuts and increasing inequalities, the unravelling is under way.

Housing starts and the construction industry have slowed and house prices are dropping with repercussions being felt in financial markets. Some are forecasting a drop in U.S. house prices of 14% over this year and next.

Home prices are of broader significance because, in a time of slow wage and salary growth, their rising asset values have been used to support ongoing household consumption and investments, which has kept the economy growing through the "wealth effect".

Erasing some of this wealth could have severe effects on the entire economy. The combined impact would cut from 3% to 7% off the U.S. economy, according to some estimates.[1] These figures are backed up by international experience: a 2003 International Monetary Fund study showed that real GDP growth dropped by an average of 8% after a real estate bust[2].

Some decline is inevitable: the question is how rapidly events will unwind. The U.S. government and the Federal Reserve face the delicate task of letting overblown asset values gradually deflate without bursting or collapsing the bubble. But things can easily get out of hand, as events in August showed.

Canada's immediate economic problems don't seem nearly as severe. In the past few years, we've had strong economic growth, historically low unemployment, record corporate profits and fiscal surpluses all around. But we are far from immune from impacts south of the border or from our own economic failings.

Our forest industry has already suffered badly from the U.S. construction slowdown and a mass of other plagues.

The repercussions of lost jobs and lost incomes are being felt in many smaller communities across Canada as property tax revenues fall and services are cut.

Canada's auto industry is now taking another direct hit. General Motors recently announced a layoff of 1,200 workers at its Oshawa truck plant because of declining demand for trucks in the slumping U.S. construction industry. The loss of these higher-paid jobs will multiply through the economy, affecting jobs and incomes for suppliers, retailers and local communities.

In the past few years a total of 23,000 jobs have been lost in the Canadian auto industry and over 250,000 in the entire manufacturing industry. While many of these laid-off workers have found other work, the new jobs pay an average of 25% less and tend to be even less secure.

Canada and other countries suffered from the mini-sub-prime meltdown in the U.S. mortgage industry, with the collapse of a number of investment funds and potentially high losses for some banks and pension plans. The impacts have just begun to run their course, but they have already led to higher interest and mortgage rates and tighter credit controls, which add up to slower growth on the horizon. A looming concern is how higher interest rates and declining house prices will ultimately affect the U.S., global and Canadian economies.

The strong growth of many developing and emerging country economies should make the global economy less vulnerable to a downturn in the United States. Still, the American economy still accounts for well over 20% of global GDP and Canada's closer ties, with over 80% of our exports still going to the U.S., make us more vulnerable.

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1 *Midsummer Meltdown*, Dean Baker, Center for Economic and Policy Research, August 2007.
2 IMF, *World Economic Outlook*, April 2003.

The Canadian economy has grown at a strong pace so far this year as a result of continued strong growth in the Alberta oil and gas industry and high rates of consumer spending. But our economic fortunes remain unbalanced. Runaway growth in the oil sands has created a lot of jobs, incomes and profits, but it is also generating inflationary pressures. This will slow down the rest of the economy as the Bank of Canada raises interest rates in reaction.

Income shares and investments are also out of balance. Corporate profits have claimed an increasing share of our national income, but they have invested smaller shares of this back into the Canadian economy. Two-thirds of this year's increase in capital investment is expected to come just from the public sector. Fortunately, the latest economic reports show a rebound in both labour income and business investment: hopefully these can be maintained.

Housing starts in Canada have declined by about 6% so far this year, but prices continue to climb. These will inevitably cool off this year and next as higher interest rates have an impact. House prices could very well decline in some markets, especially if mortgage interest rates continue to rise. Canada doesn't have a U.S.-style problem with sub-prime mortgages, but many households and the broader economy would be hurt by general house price declines.

Economic forecasts at this time in the cycle need to be interpreted with considerable caution. It is rare for private or government economists to publicly forecast a downturn or substantial slowdowns in the economy, but they do occur with some regularity.

The good news is that Canada's federal and provincial governments all have substantial surpluses. They need to use these to encourage balanced economic growth by taking action to help our ailing industries and by increasing investments in public services and infrastructure – and not by squandering them on ineffective tax cuts.

Canadian Economic Outlook			
Annual growth rates unless indicated	**2006**	**2007**	**2008**
Growth in the Economy			
Real GDP	2.8%	2.5%	2.5%
- Consumer Spending	4.2%	3.7%	2.9%
- Business Investment	9.9%	5.0%	7.6%
- Government Spending	3.9%	2.7%	3.1%
Labour Market			
Employment growth	2.0%	2.1%	1.1%
Unemployment rate	6.3%	6.1%	6.3%
Productivity growth	0.8%	0.5%	1.6%
Inflation - Consumer Price Index	2.0%	2.4%	2.2%
Corporate Profits before tax	5.0%	5.2%	2.3%
Real Personal Disposable Income	4.9%	3.8%	2.7%
Personal Savings Rate	1.8%	2.3%	2.5%
Housing Starts (000s)	228	214	192
Interest Rates and Exchange Rate			
Short term 3 Month T-Bill	4.02%	4.28%	4.78%
Long term 10 Year Bond	4.21%	4.50%	5.05%
Exchange rate US$/C$	$ 88.2	$ 92.6	$ 95
Consensus average based on latest forecasts from different Canadian forecasters as of Sept 8, 2007.			

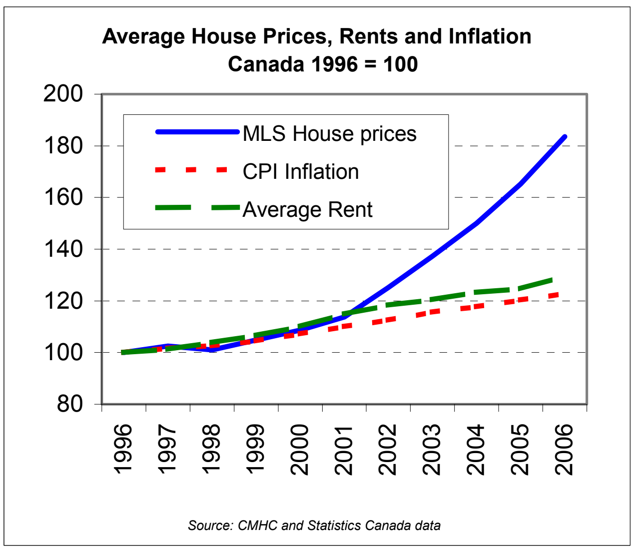
Provincial Outlook								
% annual growth unless where noted					**Unemployment**			
	Real GDP		**Employment**		**Rate**		**Inflation**	
	2007	**2008**	**2007**	**2008**	**2007**	**2008**	**2007**	**2008**
Newfoundland & Labrador	6.5	1.0	1.3	0.6	13.5	13.2	2.0	1.7
Prince Edward Island	1.9	2.0	1.4	0.7	10.5	10.5	1.6	2.0
Nova Scotia	2.3	2.4	1.4	0.8	7.9	7.9	1.8	1.9
New Brunswick	2.3	2.4	1.2	1.0	7.8	7.7	1.7	1.7
Quebec	1.9	2.6	1.8	1.0	7.5	7.5	2.2	2.1
Ontario	1.8	2.5	1.3	1.0	6.6	6.7	2.1	2.2
Manitoba	2.9	3.0	1.3	1.0	4.5	4.8	2.4	2.6
Saskatchewan	3.9	3.1	2.8	1.1	4.0	4.2	3.1	2.9
Alberta	4.4	3.7	4.3	2.2	3.6	3.9	5.3	4.0
British Columbia	3.2	3.4	2.9	1.9	4.4	4.5	2.3	2.9
Based on consensus forecasts from four different forecasters, as of Sept 8, 2007.								

Housing Bubbles and Busts

House prices in Canada and many other countries in the world have increased at high rates during the past decade, aided partly by low interest rates.

The average selling price of a house in Canada increased by 83.7% in the past decade, far higher than the increase in the *Consumer Price Index* measure of inflation and increases in rents.

This rise in house values above inflation created approximately $640 billion of extra wealth in Canadian residential real estate during the past decade. If adjustment is made for an increase in the quality of homes or for renovations, the extra wealth still amounts to approximately $500 billion, which is equivalent to more than a third of Canada's total economic output.



But now interest and mortgage rates are rising and the Bank of Canada and commercial banks are expected to continue to increase interest and mortgage rates.

Just as low interest and mortgage rates help to boost home prices, sustained increases in interest rates lead to house price declines.

These price changes can develop into booms and busts through speculation and if households and other investors are highly leveraged or have little ability to deal with changes in costs.

These can have significant impacts on the broader economy in a number of different ways: through economic activity in the construction industry; through the "wealth effect" when people borrow against their homes; impacts on financial assets and on interest rates; and multiplier effects on the broader economy.

Real estate and stock market booms and busts can also affect each other and occur at similar times. For a number of reasons, the economic impacts of real estate busts are much greater than stock market busts. In a study about real estate and stock market busts published by the International Monetary Fund in 2003[3], it found that the average real estate bust involved:

- Average price declines of about 30 percent over four years.
- A loss of economic output of about 8%. This was twice the 4% loss associated with stock market busts. Real GDP didn't fall by this amount from one year to the next, but it was this much lower overall than it would otherwise have been during the period.
- Large impacts on household consumption and investment as a result of a real estate bust.

These issues could be of concern for CUPE members in a number of different ways: impact on their own household finances, impact on jobs and communities, and effects on financial markets and pensions.

Whether Canada is headed for a real estate bust depends on what happens in the United States, the health of the rest of our economy and what the Bank of Canada and Canada's commercial banks do.

In previous housing market busts in Canada, commercial banks and other retail lenders directly held a larger portion of mortgages themselves. In recent years, these lenders have "securitized" these assets by selling them off to other investors, including investment funds and pension funds. This means that the impacts of a real estate bust, should it occur, would be different.

The effects of asset price bubbles – such as real estate and stock market booms and busts – have not been integrated in the models that the Bank of Canada uses. But two recent discussion papers published by their staff give an indication of how it could react[4].

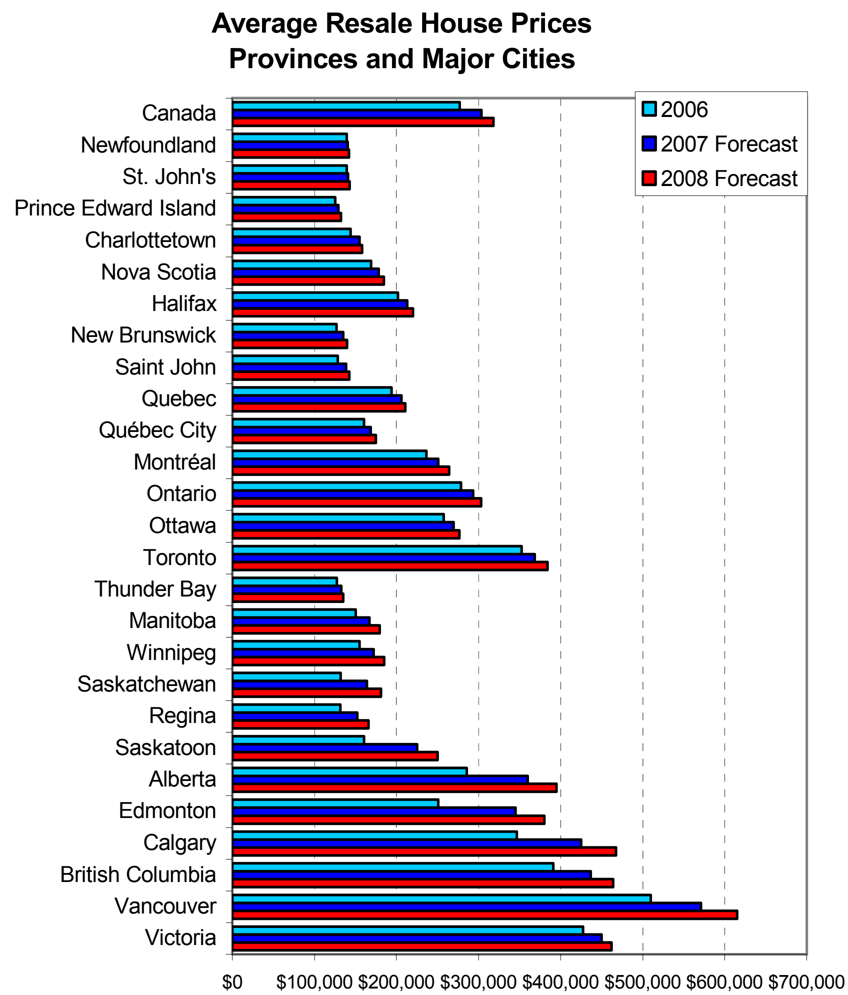
[3] IMF, *World Economic Outlook*, "When Bubbles Burst", April 2003. http://www.imf.org/external/pubs/ft/weo/2003/01/pdf/chapter2.pdf

[4] Jack Selody and Carolyn Wilkins, 2007. *Asset-price Misalignments and Monetary Policy: How Flexible Should Inflation-Targeting Regimes Be?* Bank of Canada Discussion Paper 2007-6, July 2007; Meenakshi Basant Roi and Rhys R. Mendes, 2007. *Should Central Banks Adjust Their Target Horizons in Response to House-Price Bubbles?,* Bank of Canada Discussion Paper 2007-4, May 2007. http://www.bankofcanada.ca/en/res/dp/dp(y)_2007.html

They concluded that during an asset price bubble, the Bank shouldn't change the level of its overall inflation target but that it should be flexible in the length of its target horizon. In other words, it could let inflation deviate from this target rate for a longer period. This suggests that the Bank of Canada will not act aggressively to raise interest rates if inflation continues to increase above 2% if there is a possibility that this could contribute to a housing price bust.

Before he became the most powerful central banker in the world as chair of the U.S. Federal Reserve Board, Ben Bernanke also studied the issue of stock market bubbles[5]. He concluded that central banks with inflation targets should stick to their targets during these types of bubbles.

We may soon see how well these economic theories translate into practice and reality.



Source: CMHC Housing Market Outlook 2007Q3

[5] Ben Bernanke and Mark Gertler, 2001. *Should Central Banks Respond to Movements in Asset Prices?* American Economic Review, Vol. 91, No. 2. May 2001.

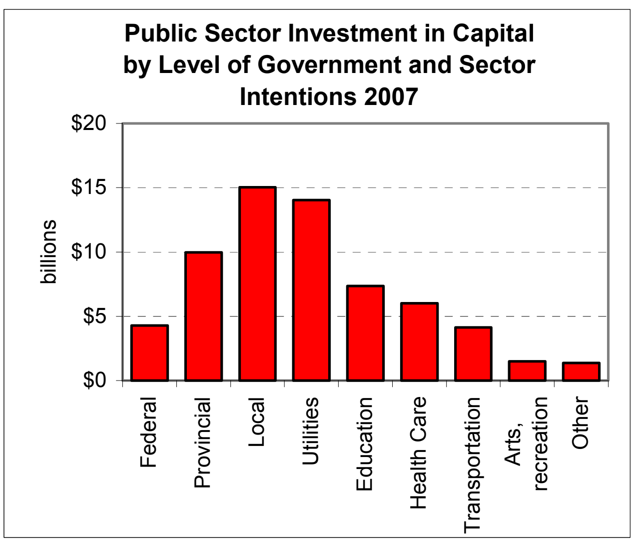
"Building Canada": dismantling the public sector?

The Harper government took major steps in the 2007 federal budget to advance its privatization and P3 agenda.

These steps include:

- Consolidating federal infrastructure funding into the **Building Canada Fund** ($8.8b/ 7 yrs)
- Forcing proponents of large infrastructure projects using these federal funds to **fully consider P3s**
- Creation of a **Federal P3 office***,* designed to execute federal P3s and oversee assessment of P3s for projects seeking federal funding
- A $1.25 billion **Fund for P3 projects,** providing a subsidy of up to 25% for "innovative P3 projects"
- Sale/leaseback of federal properties.

The central objective of these measures, as outlined in the budget document, was not to provide better value for public spending, which is only mentioned peripherally. Instead, the overarching objective is to make Canada "a leader in public-private partnerships" and to develop a private market for Canadian P3s on par with those in Australia and the United Kingdom.



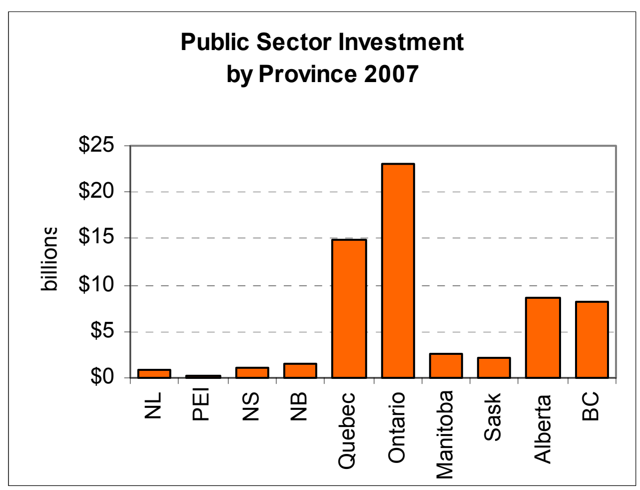
These measures responded directly to demands from business lobby groups and large banks for the federal government to create a national market for P3s. In reports issued in 2004 and 2006, the TD Bank lamented the lack of public expertise in P3s and the small and fragmented size of the P3 market in Canada.

It called for the federal government to become a champion for P3s, by funding P3s at the provincial and municipal levels, by undertaking them itself and by developing a consistent pan-national set of practices and procedures.

This is exactly what the Harper government delivered in the 2007 Budget. The federal government is a relatively small and declining player when it comes to infrastructure investments. Its total investments of $4.3 billion will only amount to 6.7% of the estimated total $64 billion that the broader public sector will put into capital investments in 2007. Local governments, provinces, utilities, hospitals, and schools, colleges and universities in the public sector all invest considerably more than the federal government in capital construction and equipment.

Provincial governments in British Columbia, Ontario and Quebec have proceeded the farthest with P3s. Each of these governments has created provincial agencies responsible for promoting, facilitating, executing, managing and assessing P3s.

Partnerships BC has 17 active projects in the fields of transportation, health care, water treatment, and recreation. *Infrastructure Ontario* has 40 active projects, with a large majority in health care and others in justice, transportation and IT. *L'Agence des partenariats public-privé du Québec* has 8 active projects in transportation, health care, arts, and justice. New Brunswick also has operational and proposed P3s in transportation. Alberta has P3s in transportation, health care and proposals for P3 schools. These are by no means all of the projects in operation or proposed: local and First Nations governments also have a number of active P3 projects. The Ontario government is also pushing strongly for a large role for P3s in energy and water investments.



All of the provincial P3 agencies perform some sort of value for money assessment for the different projects, but the published reports are brief, cursory and lacking in objectivity, written from the point of view of a proponent. None of Canada's P3 agencies have released significant details on the procedures that they use to make comparisons or conduct value for money reports. Some involve third party "fairness commissioners" to review the process, but these are often P3 consultants with close ties to the industry.

With this lack of transparency, accountability and objectivity about the process and projects details, it is difficult to get a clear understanding of the ultimate costs to the public of this form of privatization.

Virtually all the published reports on projects show that the base costs of P3 projects are considerably more – often hundreds of millions more – than traditional public delivery. Projects are almost always rationalized by the P3 agencies by arguing that the projects transfer substantial risk to the private sector or by using inflated discount rates or other dubious accounting methods. But the risks to the public sector are generally highly exaggerated and transfer of risks to the private sector is never complete.

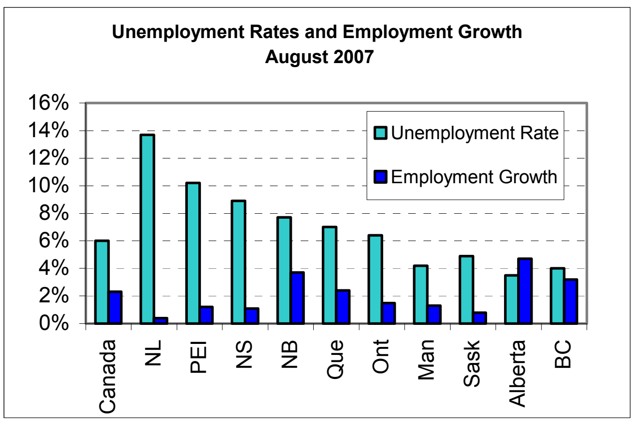
Employment growth strong, but becoming lopsided

Canada's national labour market continues to show great strength. The unemployment rate in August was at a 33-year low of 6% nationally and was down from a year ago in every province except Nova Scotia. Over 380,000 jobs have been created in the past 12 months, more than 70% of them full-time.

The strong labour market is giving workers increased bargaining power: average hourly wages for all workers increased by 4% in the past 12 months. Increases were even higher for workers in primary industry, trades and transport occupations.

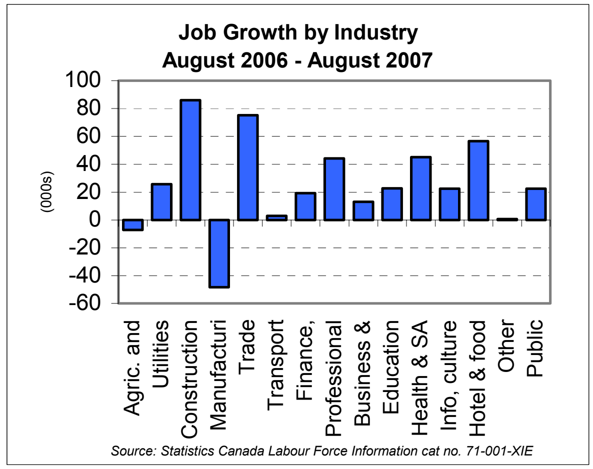
These wage gains are welcomed and long overdue after years of declining real wages.

At the same time the private sector labour market is becoming increasing lop-sided. Over 260,000 jobs – almost 70% of the total job growth over the past year – has come from just four sectors: construction, trade, professional services and accommodation and food.



These industries together with manufacturing show some of the greatest variation in employment during economic cycles. A slowdown in the economy would lead to considerable job loss in these sectors.

Fortunately, there has been decent growth in public sector employment, particularly in local government and health services, which will continue to provide strength to our communities and the broader economy.



In the main public service sectors:

- *Health care and social assistance* employment increased by 45,000 jobs, or 2.5%, during the past 12 months. This continues its strong annual growth rate of 3% a year during the past five years. A reported 29,000 of the new jobs in the sector were created in Ontario with another 19,000 added in Alberta. There was an estimated loss of 7,000 of these jobs in B.C.
- *Education services* have added an estimated 22,000 jobs, growing by 2% during the past 12 months. In this sector, Ontario has added a reported 33,000 jobs, with a reported loss of 16,100 for Quebec and of 12,400 for British Columbia in this sector. (The monthly figures need to be interpreted with some degree of caution, especially during the summer months for this sector.)
- Employment in *public administration* has increased by an estimated 22,300 (+2.7%) in the past 12 months, according to the Labour Force Survey, with half of the additional jobs in B.C. Another 7,000 each were added in both Ontario and Quebec, with a reported 4,300 jobs in this sector lost in Nova Scotia.

The public sector employment survey, which directly surveys governments, shows an increase of 28,000 in public sector employment from the 2nd quarter of 2006 to the 2nd quarter of 2007, reflecting a more modest increase of 0.9%.

Within the public sector, employment in local government and local government enterprises has grown at the fastest rate, adding more than 10,000 new jobs and growing at a rate of 2.4% during this period.

Public sector employment in health and social services increased by an estimated 16,700 during this period, at an annual rate of 2.1%, with most of the new jobs added in Ontario and Quebec. Public sector employment in universities and colleges increased by an estimated 1,500 positions and at a rate of 0.5%. Provincial government employment increased at a rate of only 1%, adding 4,500 jobs, while employment in the federal government declined by an estimated 3% during this period.

Average hourly wages by occupation	August-06	August-07
All occupations	$ 19.58	$ 20.36
Management	$ 31.45	$ 32.14
Business, finance and administrative	$ 18.81	$ 19.48
Natural and applied sciences	$ 27.90	$ 28.77
Health	$ 22.88	$ 24.50
Social sciences, education, government and religion	$ 25.40	$ 26.21
Art, culture, recreation and sport	$ 18.99	$ 19.94
Sales and service	$ 13.05	$ 13.64
Trades, transport and equipment operators	$ 19.32	$ 20.36
Primary industry occupations	$ 15.01	$ 16.41
Manufacturing, processing and utilities	$ 17.19	$ 17.65

These wage levels are based on information obtained through the Labour Force Survey and can represent changes in survey coverage, the share of full-time and part-time work in addition to changes in wage levels.

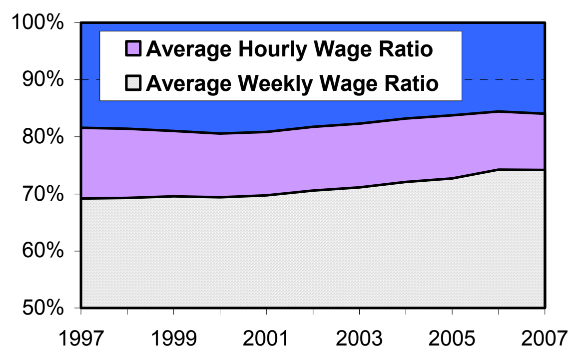
Equality on hold?

After six years of rising wages and a slowly but gradually narrowing gender wage gap, women's pay equality in the labour market seems to be on hold again.

In the past six years, average wages paid to women increased at a faster rate than men, gradually narrowing the pay gap. Average *hourly* wages paid to women increased from a ratio of 80.6% in 2000 to 84.5% in 2006.

Because women are much more likely than men to work in part-time jobs with fewer hours, the gender gap in *weekly* wages is higher. This also narrowed in the past six years as more women were able to get full-time jobs.

Ratio of Female to Male Wages
Canada 1997 to 2007



Source: Statistics Canada Labour Force Survey

However, during the past year women's wages have increased at a slower rate than men, increasing the hourly wage gap and putting equality on hold again.

Part of this is because the boom in resource and construction industries has provided larger pay gains and special trades adjustments to trades, equipment and primary industry occupations, which are very much dominated by men. It also reflects a broader set of policies that don't provide support for reducing gender and other social inequalities in society: privatization, tax cuts, constraints to social spending, cancellation of the national child care program, and cuts to programs for women, Aboriginal Canadians and other equity groups.

Increasing overall inequalities in society magnify and reflect gender inequalities. Over 60% of low paid workers are women and one in five working women are paid less than $10/hour.

While women in some professional occupations make almost as much as men, the gender wage gap is much greater in lower paid occupations and especially where there is a low rate of unionization. Canada's gender wage gap is now larger than all other OECD countries, with the exception of Korea, Japan, Germany and Switzerland.

Greater instability in work and lower pay results in reduced income security. Changes to the unemployment insurance program that increased qualifying hours and reduced benefits especially hurt women. Only 32% of all unemployed women now receive EI benefits, compared to 40% of men.

Lower paid and less stable work also translates into less retirement security. For many years women have been much less likely than men to be covered by a workplace pension. The gap is still large, especially for older women and for women in lower and middle-income families. The positive news is that women are increasingly contributing to their own pension plans and younger women are as likely as men to be covered by a workplace pension. Much of this is probably due to the higher proportion of women in the public sector and increasing rates of unionization among women.

Lack of support and incentives for women in the workforce has also had negative overall economic consequences. As even Goldman Sachs Bank recently argued, closing the gender employment gap, with the help of policies such as subsidized child care, would have huge positive economic consequences and could play a key role in addressing the twin problems of an aging workforce and pension sustainability[6].

[6] Kevin Daly. *Gender Inequality, Growth and Global Ageing.* Goldman Sachs Global Economics Paper No.154. April 2007.

Rising mortgage rates lifting inflation

Consumer price inflation has risen during the past year and further increases should be expected over the coming year. These price hikes are increasing the cost of living for Canadians and particularly lower-income Canadians.

Virtually all the inflationary pressures in Canada have come from just three sources: food price increases, housing price increases and the booming Alberta economy. Outside these areas, there is no sign that persistent and broad-based inflationary pressures have developed – and therefore no reason for the Bank of Canada to use the blunt instrument of higher interest rates to cool down the economy.

Consumer price inflation, which averaged 1.8% in the first quarter of this year, increased to an average rate of 2.2% from April to July. The national average is 2% for the year so far, but will no doubt exceed this during the rest of the year. Inflation has been rising despite the higher Canadian dollar and last year's cut in GST, both of which should have helped reduce prices.

Price increases for food and shelter alone were responsible for 63% of the rise in inflation during the past year. In other words, without price increases in these areas, the CPI would have only increased by 0.7% from July 2006 to July 2007. Lower and middle-income families spend much more of their income in these areas, which means they have faced a higher rate of inflation than the average.

In past years, the main factor pushing up the cost of housing was escalating house prices. Rising house prices continue to be a major factor in Canada, but now the main influence pushing up housing costs is higher mortgage interest rates. Mortgage rates have increased by at least 75 to 100 basis points for all terms from the start of this year (100 basis points equals one percentage point). For someone with a $200,000 mortgage, this increase in rates would add $1,100 to $1,400 to their annual mortgage payments.

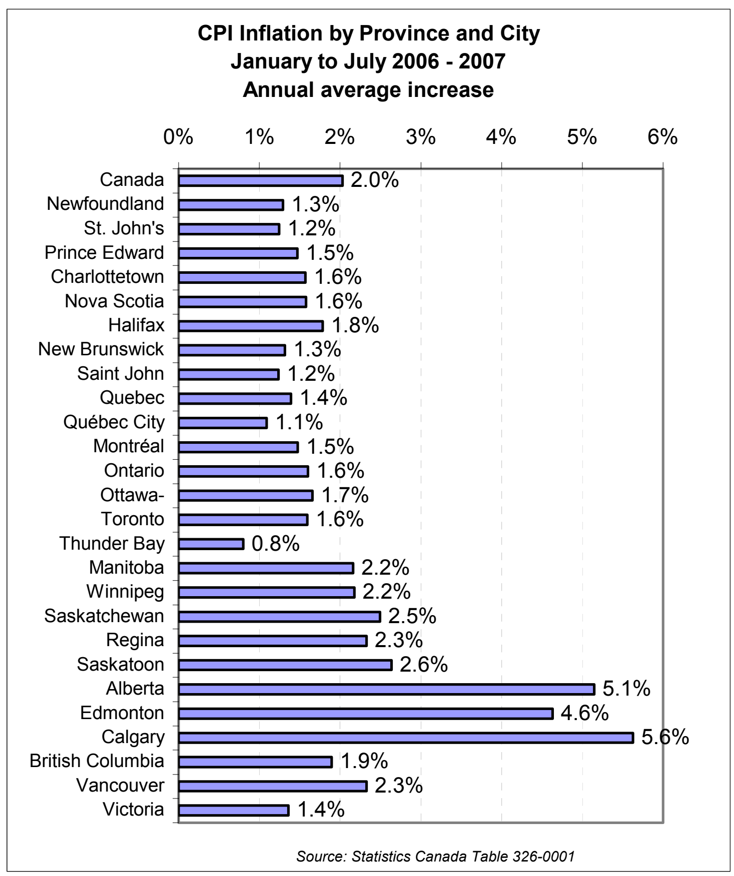
Further mortgage rate hikes appear to be coming. When the Bank of Canada raised its key lending rate in July, it strongly suggested that more rate increases should be expected. Recent forecasts issued by Canada's major banks predict that interest rates will rise by an additional 50 to 100 basis points over the next year.

As a result of the sub-prime market cooldown in August, the Bank of Canada kept its interest rate unchanged at its September announcement date, but it didn't do this to provide relief to Canadians households. Commercial banks and lenders have already raised rates and tightened up credit for consumers on their own without prodding by the central bank.

Higher prices are also spreading through the food basket. Past months have seen a large increase in the cost of grains and particularly of corn. Regulations for ethanol content in fuels and subsidies for biofuels have been a major factor driving up food prices. Higher prices for corn and other grains, a big part of animal feed, are now also showing up in higher prices for meat and dairy products on the grocery shelf.

Regional inflation trends

Price increases in Alberta continue to far outstrip those in the rest of Canada, with an average increase of 5.1% so far this year. Saskatchewan has run a distant second with a 2.5% increase to date. Manitoba's average price increase of 2.2% puts it in 3rd place.



All other provinces have experienced average CPI inflation of less than 2% so far this year. Price increases in the rest of Canada outside Alberta have averaged only 1.6%.

Inflation Outlook

Major banks and other economic forecasters have all hiked their predictions for inflation for this year.

The national rate of consumer price inflation is expected to average about 2.4% in 2007. Next year is also expected to see inflation at about 2.2% or more - unless there is a housing market meltdown which would both lead to a drop in house prices and interest rates.

Resale house prices increased by an average of 11% across Canada in 2006. The Canada Mortgage and Housing Corporation is forecasting an average price increase of 9.6% this year, followed by an average increase of about 4.9% in 2008. Actual and forecasted house prices for provinces and major cities are presented on page 6.

Inflation in Alberta is expected to average 5.3% in 2007, followed by Saskatchewan with an increase of 3.1%, Manitoba with 2.4%, and BC with an increase of 2.3%. Inflation rates in 2008 are expected to moderate in Alberta and Saskatchewan, but to increase in both BC and Manitoba. Inflation rates are expected to average 2.2% or less in other provinces for both these years.

Inflation forecasts for all provinces are presented in the Provincial Outlook Table, on page 4.

Wage increases deliver more real gains

Union members achieved decent gains in average wage settlements by the mid-point of this year, building on wage increases from the past few years.

Base wage increases for major agreements have averaged 3% this year, compared to 2.5% in 2006 and 2.3% in 2005. Public sector workers achieved slightly higher gains, with wage increases averaging 3.1% for the first half of the year compared to 3% for the private sector.

These agreements have provided workers with average wage increases slightly higher than the national rate of consumer price inflation, which has increased at a rate of 2%.

But averages can be deceiving: there has been a lot of variation in the rate of inflation across Canada and in wage gains achieved in different regions and sectors of the economy.

Workers in Alberta and Saskatchewan continued to lead other provinces in wage increases. Wage gains averaged 4.4% for Alberta agreements reached in the 2nd quarter of the year, bringing their increase this year to 4.1%. These increases are below the province's running 5.1% inflation rate, but may be closer to the average increase in inflation for the length of the contract.

Workers in Saskatchewan have also achieved solid wage increases at the bargaining table. Their gains averaged 4.1% to the mid-point of the year. This is consistent with many public sector gains in the province and is above Saskatchewan's average rate of inflation for the year of 2.5%. However, inflation has started to accelerate in Saskatchewan in recent months, driven up by rising house prices.

Average wage gains in Newfoundland and Labrador have continued to be relatively low, averaging only 0.7% this year but this only reflected a couple of contracts, including one with an annual wage reduction of 0.7% for employees of Fisheries Products International.

In all other provinces, settlements achieved in the first half of this year averaged between 2.5% and 3.5%.

Workers in public administration and utilities achieved the highest average increases of the major industry sectors, with average wage gains of 3.6%. Wage increases in education, health and social services agreements have averaged 3.1% and those in information and culture 3.4%.

Wage increases for workers in the hard-hit manufacturing industry have only averaged 1.7%, while those in entertainment and hospitality gained 2.6% and workers in transportation an average of 2.7%.

Private Sector Compensation Surveys

Three private sector salary surveys that have been released so far this year are projecting similar trends in pay increases for 2008. Surveys by Mercer, Morneau-Sobeco, and Hewitt Associates forecast the following:

By Region

- Average salary increases of about 3.8% across Canada
- Highest increases in Calgary (4.2% to 5.2%)
- Rest of Alberta averaging increases of 4% or more
- Vancouver and B.C. with average increases of 3.7% to 3.9%
- Increases averaging 3.3% to 3.7% in the rest of Canada

By Sector:

- Highest increases in oil and gas, with 5.2% to 6.3% increases
- Higher than average increases in utilities and government
- Vast majority of other sectors expecting increases between 3% and 4%
- Increases averaging about 3% in auto, forest and paper, printing and hospitality

Unionized workers are expected to gain increases averaging 3.1% in 2008, following average increases of 3.2% in 2007, while salaries for executives are expected to rise by 4% in 2008.

Employers are showing greater interest in using flexible work arrangements and workplace benefits, including spelling out total compensation packages, to attract employees. Top benefit issues for employers continue to be health care costs and disability management, even though health care cost increases have trended lower because of less downloading of costs from public plans and fewer releases of new "break-through" drugs.

During the first half of 2007, pension funded ratios reached their highest level in about five years, according to analysis by Watson Wyatt. Still, an increasing number of employers report that that they have or are planning to close their defined benefit plans to new employees.

A number of pension plans invested considerably in securities that could suffer significant losses as a result of a downturn in the U.S. housing market.

Average Wage Settlements Major Collective Bargaining by Year					
	2004	**2005**	**2006**	**2007Q1**	**2007Q2**
All	1.8	2.3	2.5	3.1	3.0
Public Sector	1.4	2.2	2.6	3.3	3.0
Private Sector	2.2	2.4	2.1	2.6	3.1
CPI Inflation:	*1.8*	*2.2*	*2.0*	*1.8*	*2.2*

Average Wage Settlements by Province												
	NL	**PEI**	**NS**	**NB**	**QC**	**ON**	**MB**	**SK**	**AB**	**BC**	**Multi Prov**	**Federal**
2004	1.0	2.4	4.7	4.1	2.6	3.0	2.6	1.0	3.1	-1.6	2.7	1.6
2005	2.1	2.5	3.2	3.0	1.6	2.7	2.9	1.9	3.0	0.5	4.1	2.6
2006	1.7	2.7	3.1	2.9	1.8	2.5	2.6	2.1	3.4	2.4	3.5	2.3
2007Q1	-	2.9	1.8	3.0	2.9	2.9	2.7	4.0	3.5	2.3	6.6	2.8
2007Q2	0.7	2.8	3.7	2.0	3.2	2.9	3.0	4.2	4.4	2.9	--	2.7

Average Wage Settlements by Industry				
Industry	**2005**	**2006**	**2007Q1**	**2007Q2**
Primary	2.3	2.7	3.2	3.2
Utilities	2.6	2.3	3.1	4.0
Construction	2.5	3.5	2.9	3.2
Manufacturing	2.4	2.0	0.7	2.1
Wholesale and Retail	1.9	1.1	1.4	3.1
Transportation	2.9	2.1	3.2	2.6
Information & Culture	2.4	2.5	1.6	3.8
Finance & Professional Services	2.3	2.5	2.0	3.9
Education, Health, Social Services	2.1	2.5	3.1	3.0
Entertain and Hospitality	1.9	2.9	2.6	--
Public Administration	2.4	2.8	4.0	3.1

Source: Human Resources and Skills Development Canada, Major Wage Settlements, [latest information as of August 24, 2007] http://www.hrsdc.gc.ca/en/lp/wid/adj/01wage_adj.shtml

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September 13, 2007