

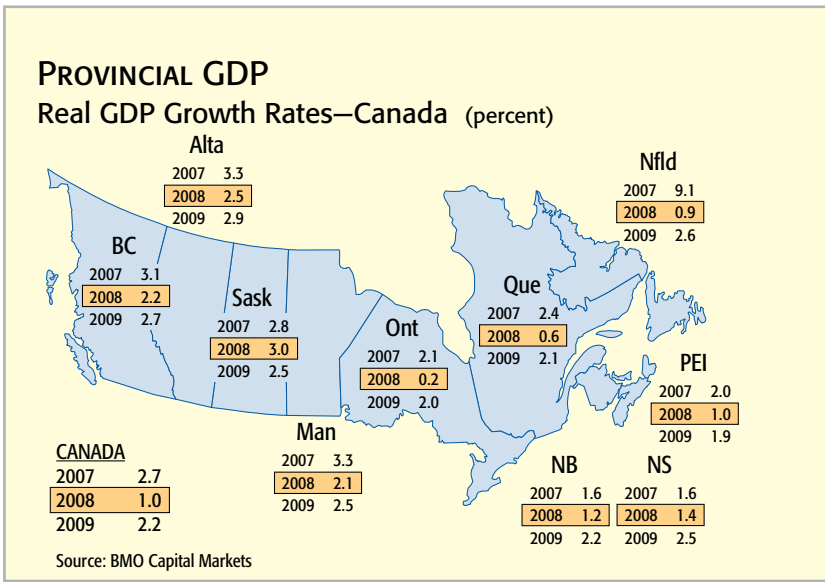


Regional Disparity Continues

Summer 2008
 Robert Kavcic
 Economic Analyst

1-800-613-0205
 www.bmonesbittburns.com
 /economics

 The disparity in Canadian regional economic performance continues unabated, with surging commodity prices supporting growth in the West, and the strong C\$ and slowing U.S. economy depressing manufacturing-heavy Central Canada. While most provinces will lose momentum this year, record oil prices and the U.S. downturn will hit Central Canada particularly hard, keeping this regional disparity intact.



The resource-rich provinces were the clear-cut GDP growth leaders again in 2007. Newfoundland & Labrador led the country with a 9.1% surge, thanks to strong offshore oil output and a rebound in production at the Voisey's Bay nickel following strike activity in 2006. Western Canada also rode commodity prices to another year of above-average real GDP growth, with the four provinces west of Ontario averaging 3.1%, helped by a favourable mix of energy and mining output and exploration and construction activity. Meantime, economic growth in Central Canada and the Maritimes was below the national rate in 2007 as rising fuel costs, a strong C\$ and slowing U.S. economy dragged on manufacturing.

This regional disparity continues, though more the result of a pronounced slowdown in Central Canada than accelerating growth in the West. The bulk of the weakness is in manufacturing and export-heavy Ontario and Quebec, where GDP growth will likely dip below 1% for the first time since the 1990s. On average, western provinces are expected to grow 1.6 ppts faster than in the East, up from 1.2 ppts last year (volatile Newfoundland & Labrador is excluded).

Population: 32,934,166	Party in Power: Conservatives	Legislative Seats: Conservatives 127	Minority Government Since: January 2006
Area: 9,984,670 km²	Prime Minister: Rt. Hon. Stephen Harper	Liberals 96	
GDP/Capita: \$46,628	Finance Minister: Hon. Jim Flaherty	Bloc Quebecois 48	
National Capital: Ottawa		New Democrats 30	
		Independent 4	
		Vacant 3	



This gap should narrow in 2009 when the U.S. economy—and Central Canada—recovers.

One trend that has started to reverse is the flow of migrants. Net interprovincial migration to Alberta hit a record 58,200 people in 2006, with many leaving Atlantic Canada in search of high-paying jobs. However, late-2007 saw a sharp reversal in this pattern, with Alberta recording its biggest quarterly outflow since 1988 and Atlantic Canada experiencing in-migration and accelerating population growth. With a number of construction projects on tap, Atlantic Canada could be at risk of facing its own skilled labour shortage, making for some interesting competition for workers between the West and East.

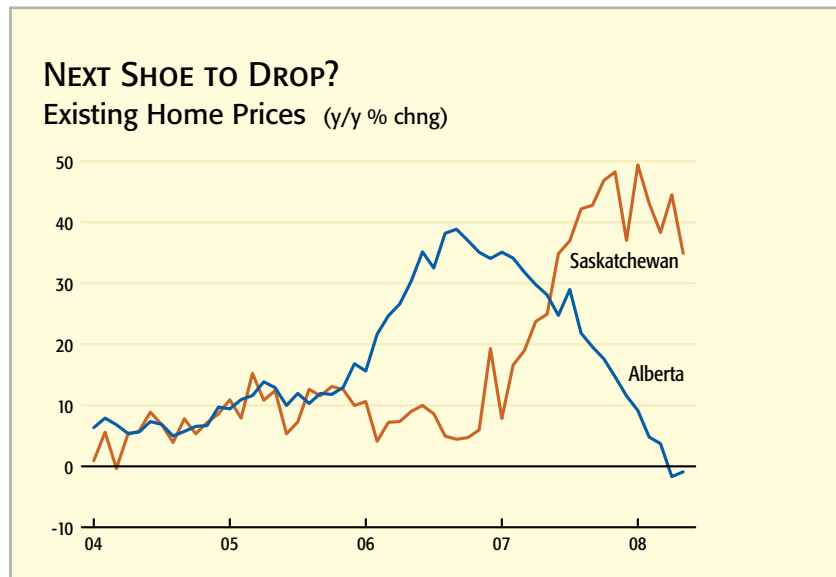
Western Housing Boom: Balancing Act

Canadian housing market activity has cooled sharply so far in 2008, confirming that the multi-year housing boom has indeed fizzled, particularly in the formerly white-hot West. National existing home sales were down 13% y/y through May. The breadth of the declines is eye-catching, with 9 of 10 provinces seeing sales below year-ago levels through May—Newfoundland & Labrador is the exception—and 19 of 20

major markets down in May. The most pronounced declines have been in Alberta and B.C., with Saskatchewan also starting to lose momentum.

While sales are falling, new listings continue to rise, led by a whopping 58% jump in Regina—the country’s latest hot-spot. But with sales in the city down an almost equally-whopping 28% y/y, Saskatchewan’s white-hot housing market is quickly balancing out, and downward price pressures like the ones we’ve seen in Alberta in the past year are likely to take hold in the coming months. Prices in Calgary and Edmonton are now down 2.4% y/y and 4.8% y/y respectively, joining layoff-ridden Windsor as the only three cities with prices in the red.

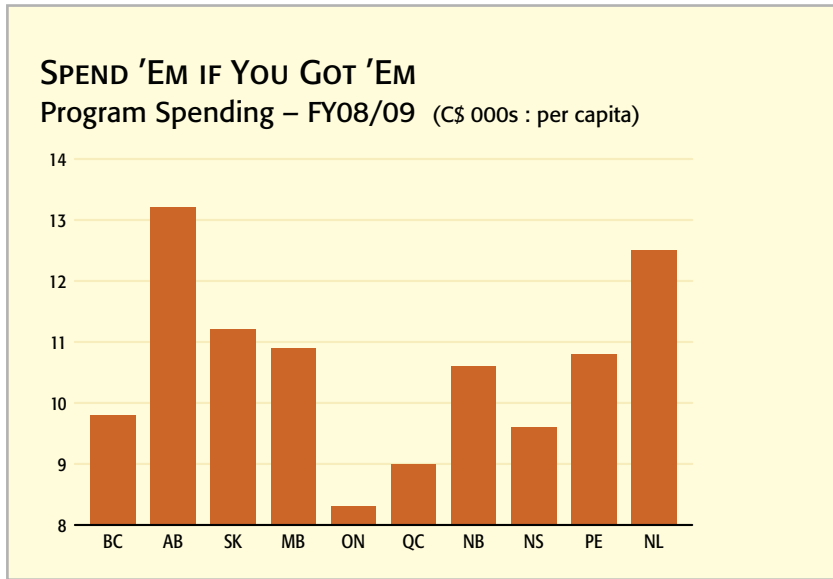
Canada’s western-led housing boom looks to be over, and the days of 40%-plus price appreciation in Alberta are behind us, and soon to be behind us in Saskatchewan as well. However, thanks to still-solid job growth, strong underlying economic fundamentals and more conservative lending (i.e.: no explosion in subprime mortgages), a balancing period is likely rather than a U.S.-style collapse.





Commodity Boom Lines (some) Provincial Coffers

The regional disparity is also evident on the fiscal front. Overall, the Canadian provinces continue to see black ink, with all but PEI expecting balanced budgets or surpluses for both FY07/08 and FY08/09. The combined provincial surplus is pegged at just under \$3 billion this year—excluding \$750 million allowances in B.C. and Ontario—down from nearly \$9 billion last year, largely due to smaller figures in B.C. and Alberta



With rising resource revenues, Western Canada and Newfoundland & Labrador were afforded the most wiggle room this budget season, and could see further upside to their estimates given oil and natural gas price assumptions that are comfortably below current levels—we’ve inserted a commodity sensitivity comment in each of the relevant provincial pages. Indeed, these provinces were able to make bolder moves, particularly on the program spending front, where average growth is pegged at a robust 6.3% this year—Newfoundland & Labrador tops the charts at 12.9%. Alberta is the biggest spender on per-capita basis, doling out more than \$13,000 per person, while Ontario and Quebec lag well behind. The Central and Maritime provinces took a cautious approach amid an uncertain economic outlook, opting for modest targeted spending and a sprinkling of tax relief for the manufacturing sector.

The provinces remain active borrowers despite their budget surpluses. Total provincial borrowing is pegged at \$51.2 bln for FY08/09, primarily made up of re-financings, and includes borrowing on behalf of government enterprises, public pensions and for capital investment programs. About 30% of combined funding has been completed by mid-June.



British Columbia

Population: **4,373,827**
 Percent of Canada: **13.3**
 Rank by Population: **3rd**
 Area: **944,735 km²**
 GDP/Capita: **\$42,596**

Provincial Capital: **Victoria**
 Party in Power: **Liberals**
 Premier: **Hon. Gordon Campbell**

Finance Minister: **Hon. Carole Taylor**
 Legislative Seats: **Liberals 46**
New Democrats 33

Next Election: **May 2009**

Economic growth in B.C. will slow to 2.2% this year after 3.1% growth in 2007, as headwinds in forestry work against a sturdy consumer and booming resource sector. A rebound is expected in 2009 as the U.S. economy recovers.



Mining and domestic demand to buffer struggling forestry sector.

\$50 mln surplus amid revenue-neutral carbon tax.

The B.C. forestry sector continues to fight a losing battle with the strong loonie and U.S. housing recession. About 60% of B.C.'s exports go to the U.S, of which about a quarter are lumber, shingles, plywood and other wood products. Adding to the misery are billions of mountain pine beetles eating their way through B.C. forests, which are now expected to kill 80% of the province's pine, according to the Business Council of B.C.

The mining and energy sectors, however, are prospering as surging prices and Alberta's royalty hike are boosting exploration activity in the province. In May, B.C.'s Crown land auction for oil & gas fetched \$441 million, the biggest monthly sale on record. So far in 2008, B.C. land sales have totalled \$824 million, twice the amount generated by Alberta and easily on pace to set an annual record.

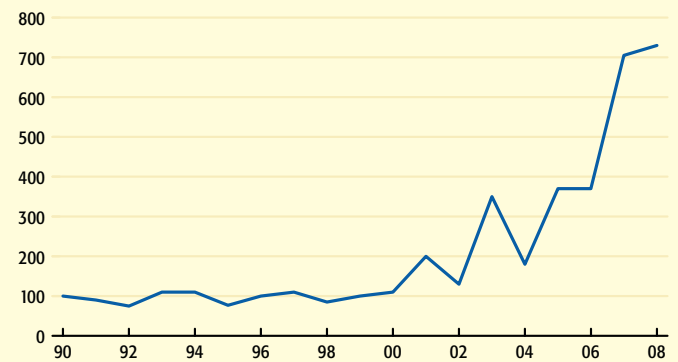
Strong construction activity ahead of the 2010 Olympics will also continue to offset weakness in forestry, while residential construction remains strong and consumer activity sturdy—retail sales were up 4.4% y/y in Q1. The labour market is also tight with 3% y/y job growth and the unemployment rate near a record low.

The Province of British Columbia is forecasting its fifth consecutive year in the black, with a "green" budget. Following a \$2.0 bln surplus in FY07/08, a modest \$50 mln surplus is projected for FY08/09, with a 2.3% decline in total revenue outpaced by 1.1% growth in spending. The projected surplus rises to \$150 mln in the subsequent two out years, each incorporating more than \$1 bln in allowances and spending contingencies. The highlight of the budget was a set of measures designed to reduce B.C.'s greenhouse gas emissions by one-third by 2020, which includes a revenue-neutral carbon tax, and more than \$1 bln in funding for a broad range of climate change incentives. The carbon tax will be credited back to low-income households, with all remaining revenue returned via lower personal and corporate tax rates. Borrowing requirements are projected to be \$5.2 bln in FY08/09, with 22% completed by mid-June.

Commodity note: The province is assuming \$5.65 natural gas in FY08/09, with every dollar adding \$275 million.

BRITISH COLUMBIA: PUMPED UP LAND PRICES

Land Leased for Oil and Gas Exploration (C\$/acre : avg.)



Source: B.C. Ministry of Energy, Wall Street Journal



Alberta

Population: **3,460,125**
 Percent of Canada: **10.5**
 Rank by Population: **4th**
 Area: **661,848 km²**
 GDP/Capita: **\$75,761**
 Provincial Capital: **Edmonton**

Party in Power: **Progressive Conservatives**
 Premier-Designate: **Hon. Ed Stelmach**
 Finance Minister: **Hon. Iris Evans**

Legislative Seats:
PC 72
Liberals 9
New Democrats 2

Majority Government Since: **March 3, 2008**

Royalties and slowing housing market to cool growth.

Surplus projected to narrow to \$1.6 billion.

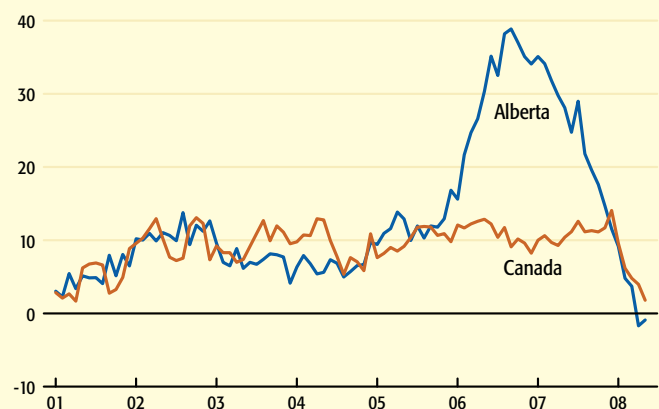
While Alberta was unseated as the growth leader last year, and should slow to 2.6% this year, the province remains one of the engines driving Canada's economy, and above-average growth is expected through 2009.

There are a number of factors contributing to slower growth in the province, even with oil prices probing record levels. The formerly white-hot housing market has cooled fast, with existing home prices down 0.9% y/y in May, the first annual decline since 1996. Sales are down sharply, new listings are rising fast and the province is experiencing net out-migration for the first time in over a decade—the days of 40% y/y home price appreciation are indeed now a thing of the past. As a result, residential construction activity is also stalling with housing starts averaging 43,300 annualized units in the latest 12 months, down 13% from the prior year. Commercial construction, however, is supported by the \$1 billion Encana building in downtown Calgary to be completed by 2011. Meantime, the royalty hike has cast some uncertainty over the oil & gas sector, with evidence suggesting a spillover in activity to B.C. and Saskatchewan, both in terms of drilling and exploration activity and migration flows.

However, there is still life in Boomtown. Domestic demand remains strong with job and wage growth keeping consumer activity firm. The province still boasts the fastest rate of employment growth at 3.3% y/y, while the jobless rate remains near a multi-decade low. A bust scenario is still a long-shot in the province, but the Western-Canada commodity boom is no longer just an Alberta story.

The Province of Alberta is projecting a 15th consecutive budget surplus in FY08/09, with an earlier-than-promised elimination of the health care premium and aggressive spending. The surplus is projected to be \$1.6 billion, down from \$4.0 billion in FY07/08. The Province expects surpluses of \$362 million and \$199 million in FY09/10 and FY10/11 respectively, as spend-

ALBERTA: HOUSING LEADER TO LAGGARD
 Existing Home Prices (y/y % chng)





ing growth moderates and revenue dips alongside gradually lower commodity prices. Total revenue is projected to grow 2.2% to \$38.6 billion in FY08/09 thanks to higher resource revenue, while total spending is expected to grow a hefty 9.7%, with health care getting almost 40% of the allocation. Alberta plans to borrow \$1.7 billion in FY08/09, which it will subsequently lend to other provincial corporations. Alberta Capital Finance Authority plans to borrow \$800 million, while ATB Financial plans to raise \$600 million.

Commodity note: Alberta is assuming \$78 oil and \$6.75 natural gas in FY08/09, with per-dollar sensitivities of \$130 million and \$1.14 billion respectively.



Population: **995,640**
 Percent of Canada: **3.0**
 Rank by Population: **6th**
 Area: **651,036 km²**
 GDP/Capita: **\$46,283**

Provincial Capital: **Regina**
 Party in Power: **Saskatchewan Party**
 Premier: **Hon. Brad Wall**

Finance Minister: **Hon. Rod Gantefoer**
 Legislative Seats: **Saskatchewan Party 38**
 New Democrats 19
 Vacant 1

Election to Be Held by: **November 2012**

Saskatchewan to remain Canada's hottest economy.

Commodity-fuelled surpluses pegged as temporary.

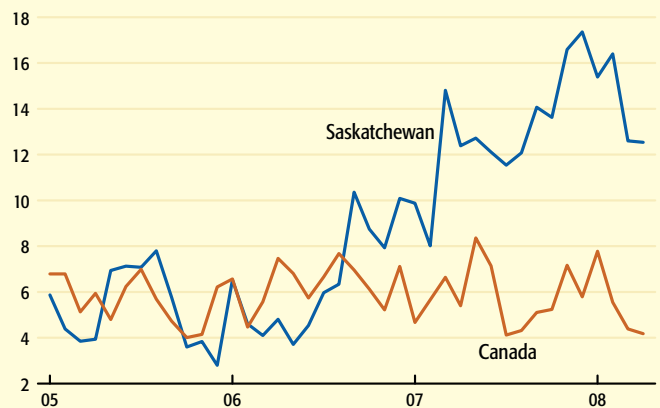
Saskatchewan's momentum should continue this year, with real GDP growth likely accelerating to 3%, before losing some steam in 2009. Saskatchewan boasts Canada's hottest economy, with nominal GDP ballooning 11.4% last year, and the province leading in retail sales growth and housing market performance.

The commodity/agriculture boom is in full gear in Saskatchewan, with exploration activity and crop receipts surging. Crown land sales through May already surpassed the government's estimate for the year, reflecting robust exploration activity in the wake of Alberta's royalty hike and surging commodity prices. Meantime, crop receipts rose 66% y/y in Q1, the fastest pace in over a decade. The boom is driving investment in the province, with projects like the \$1.8 billion PotashCorp mine expansion pegging capital spending intentions at 18% y/y in 2008.

With the province netting more than 10,000 interprovincial migrants in the latest 4 quarters, and population growth the highest since the 1970s, the housing market continues to surge. Average home prices were up 43% y/y in Q1 and housing starts were 36% above year-ago levels. While this torrid pace has begun to moderate, the housing market will continue to support growth in the province.

SASKATCHEWAN: SHOPPING SPREE

Retail Sales (y/y % chng)





Meantime, with strong population growth and rising wages—average weekly earnings rose 5% y/y in Q1—consumer activity is the strongest in the country. Retail sales rose a league-leading 13% in 2007, with the momentum holding firm. The housing boom is clearly at work, with surging sales in segments like home improvement, furniture and building supplies.

The Province of Saskatchewan is projecting its 15th consecutive year of black ink for FY08/09, and is taking measures to help handle its new-found economic boom. The surplus in the GRF is estimated at \$250 million after a \$10 million transfer to the new Growth and Financial Security Fund, down from \$347 million last year. The province expects to draw on the GFSF in each of the subsequent three years as it returns to pre-transfer deficits. Spending on infrastructure is a priority to keep election promises and manage growth. Revenue is expected to inch down 0.3% to \$9.37 billion in FY08/09, owing to lower federal transfers, while program spending is slated to rise 4.9% to meet the demands of the economic expansion. Total borrowing requirements are expected to be \$911 million in FY08/09, with 44% completed by mid-June.

Commodity note: Saskatchewan is forecasting \$82 oil and \$335 potash in FY08/09, with per-dollar sensitivities of \$19.1 million and \$3.7 million respectively.



Manitoba

Population: **1,185,216**
 Percent of Canada: **3.6**
 Rank by Population: **5th**
 Area: **647,797 km²**
 GDP/Capita: **\$39,022**

Provincial Capital: **Winnipeg**
 Party in Power: **New Democrats**
 Premier: **Hon. Gary Doer**

Finance Minister: **Hon. Greg Selinger**
 Legislative Seats: **New Democrats 36**
PC 19
Liberals 2

Next Election: **May 2011**

Capital spending to offset manufacturing headwinds.

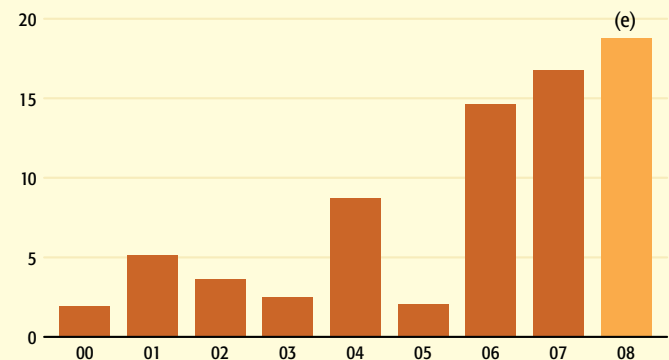
Cautious budget calls for \$96 mln surplus.

Manitoba posted another year of solid 3.3% real GDP growth in 2007, as construction activity and a sturdy manufacturing sector buoyed the province's economy. While the strong C\$ and U.S. slowdown are weighing on growth this year, the diversity of the manufacturing sector, mining activity and aggressive capital spending will all help moderate the slowdown in Manitoba to 2.1%.

Construction activity was the main pillar of strength in 2007, and that is continuing on both the residential and non-residential sides this year. Major infrastructure projects like the Red River Floodway, Winnipeg Airport and highways are expected to continue into 2009, keeping a key economic support in place this year. Meantime, resurgent population growth—currently

MANITOBA: CAPITAL SPENDING BOOM

Capital Expenditures (y/y % chng)



(e) = estimate



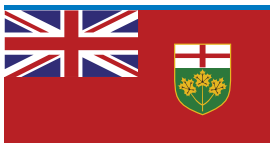
the highest since the mid-1980s—and strong job creation are boosting the province’s housing market. Existing home prices were up 13% y/y in May, paced only by red-hot Saskatchewan, and Newfoundland and Labrador.

While Canadian manufacturing continues to grapple unsuccessfully with the strong dollar, high energy prices and sputtering U.S. growth, Manitoba’s diverse manufacturing sector is putting up a formidable fight. Led by components related to the new Boeing 787, the aerospace sector remains hot. While Canadian manufacturing shipments were down 5% y/y in the first quarter, aerospace shipments were up more than 7% y/y.

Finally, with many commodity prices probing record levels, oil & gas exploration should remain strong and mining output firm. Additionally, the bright outlook in agriculture will also help to offset some of the overall softness in manufacturing.

Manitoba’s FY08/09 budget took a cautious approach against an uncertain economic backdrop, offering some modest tax relief, help for the manufacturing sector and a mix of spending measures. The province is projecting a \$96 million summary budget surplus for FY08/09, down from an estimated \$329 million for FY07/08. Longer term, the province is committed to keeping the bottom line in the black, with surpluses projected out to FY2011/12. Total revenues are projected to rise 1.3% to \$12.3 billion in FY08/09, led by a 6.8% jump in Federal transfer revenues, while spending will rise 3.3% to \$12.2 billion, led by health care and education. The province’s 10-year infrastructure program also remains in force.

Total borrowing requirements are expected to be \$2.8 billion in FY08/09, with \$1.4 billion of refinancing.



Ontario

Population: **12,790,237**
 Percent of Canada: **38.8**
 Rank by Population: **1st**
 Area: **1,076,395 km²**
 GDP/Capita: **\$45,432**

Provincial Capital: **Toronto**
 Party in Power: **Liberals**
 Premier: **Hon. Dalton McGuinty**

Finance Minister: **Hon. Dwight Duncan**
 Legislative Seats:
Liberals **71**
PC **26**
New Democrats **10**

Next Election: **October 2011**

Manufacturing troubles to pull growth below 1%.

Budget remains balanced after reserve cushion.

The Ontario economy is struggling against the backdrop of a strong Canadian dollar, high energy costs, and a U.S. downturn. While real GDP growth was a moderate 2.1% in 2007, the sputtering manufacturing sector will likely drag down growth to 0.2% this year before rebounding in 2009.

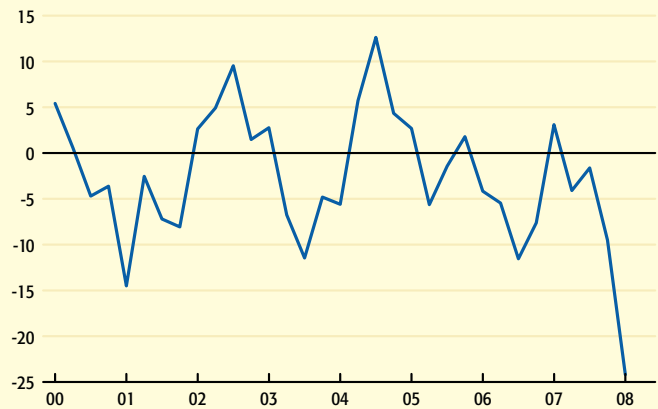
Weakness in manufacturing, particularly in the auto sector, continues to weigh heavily on the province. Not only are there cyclical headwinds—commodity prices and the U.S. economy—but also a structural shift in manufacturing to more cost-effective emerging markets. The auto sector continues to face a barrage of layoffs—5,000 in the last two years—and new investment is diminishing with the Canadian dollar at parity and UAW concessions in the U.S. reducing Ontario’s cost advantage. In a sign of the times, GM will no longer employ anyone directly in Windsor when its transmission plant closes in 2010.



The service sector is picking up much of the slack in manufacturing, keeping the Ontario economy above water. While manufacturing employment is down 5% y/y through May, service-sector jobs are up 3.3% y/y on strong public-sector hiring, helping to support consumer spending. Meantime, while Ontario's economy is traditionally the most closely tied to the U.S., the rising importance of the service sector has helped reduce that dependence, and should buffer this downturn.

ONTARIO: AUTO SECTOR TAILSPIN

Mfg. Sales – Transportation Equipment (y/y % chng)



Commercial office properties are still sprouting—Toronto Life Square and Ritz Carlton for example—but the residential housing market is cooling. Existing home sales are down 10% y/y through May, while price growth continues to plod along in the low-single digits. This softness is expected to continue for the remainder of 2008.

The Province of Ontario is trading carefully against the backdrop of slowing economic growth, with the FY08/09 budget providing modest additional relief for manufacturers and a focus on infrastructure, education and health care. The Province expects to post another balanced budget in FY08/09 after a \$750 million reserve allowance—though that assumes 1.1% economic growth—with more of the same projected through FY2010/11. Revenue is expected to inch up 0.4% to \$96.8 billion this year, as slower economic growth dampens personal and corporate income tax revenues, while program spending is slated to rise 0.3%, led by health care and education.

Ontario's borrowing requirements are expected to be \$24.3 billion in FY08/09, with 22% completed by mid-June.



Population: **7,695,104**
 Percent of Canada: **23.4**
 Rank by Population: **2nd**
 Area: **1,543,056 km²**
 GDP/Capita: **\$38,284**

Provincial Capital:
Quebec City
 Party in Power:
Liberals

Premier:
Hon. Jean Charest
 Finance Minister:
Hon. Monique Jerome-Forget

Legislative Seats:
Liberals 48
Action Democratique 41
Parti Quebecois 36
 Minority Government Since:
March 2007

The Quebec economy grew at a healthy 2.4% clip in 2007, boosted by strong domestic activity. However, momentum is fading this year as the surging loonie and U.S. housing recession chip away at manufacturing, with real GDP growth likely to slow to 0.6% before rebounding in 2009.



Manufacturing headwinds blowing strong.

Balanced budget through FY2009/10.

Consumer activity in the province is firm, with retail sales up a healthy 5.6% y/y in the first quarter. While the labour market was resilient with the unemployment rate dipping below 7% for the first time, cracks are starting to show. Last year, an impressive 92,000 new jobs were created in the province, but nearly all of it was in the service sector, which has slowed sharply in recent months. As a result, the unemployment rate has ticked up 0.7 ppts from its January low.

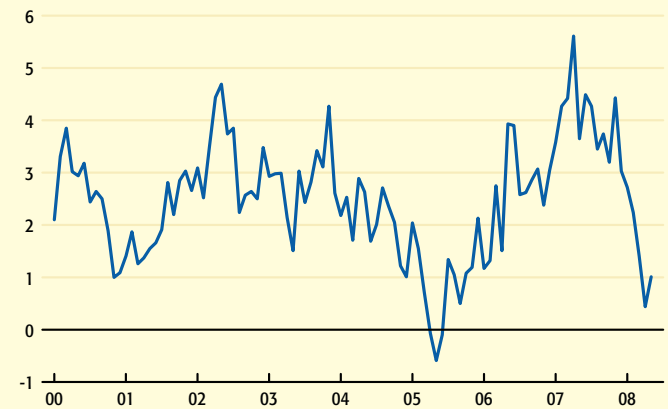
If the service-sector buffer wears off, Quebec labour markets could continue to slacken.

On the bright side, investment activity will continue to support economic activity this year. While housing starts should trail off after a sturdy 2007, government-funded non-residential projects will pick up the slack. In the pipeline in the coming years are the McGill Health Centre, Ste-Justine Hospital, and various highway upgrades. Meantime, the commodity boom looks to be finding its way to Quebec. Investment in the mining sector is expected to rise 45% this year, while natural gas exploration is gaining steam as interest in the Utica shale region grows. These factors should serve to keep Quebec's economy above water in this challenging period.

Quebec's FY08/09 budget was heavy on fiscal discipline and light on headline-grabbing tax or spending measures. The Province managed to keep the books balanced last fiscal year and looks for a similar performance in FY08/09, and again next year. This assumes 1.5% real GDP growth in 2008, twice our call. Revenue growth will slow to just 0.1% this fiscal year alongside softer economic activity, while program spending is slated to rise at a stronger 4.2% pace on health and education outlays. That combination will cut the pre-transfer consolidated balance from a \$1.1 billion surplus in FY07/08 to a \$628 million deficit this fiscal year.

Borrowing requirements are expected to be \$11.1 billion in FY08/09, with 44% completed by mid-June.

QUEBEC: SERVICES WITHOUT A SMILE
Service-Sector Employment (y/y % chng)



New Brunswick

Population: **749,525**
Percent of Canada: **2.3**
Rank by Population: **8th**
Area: **72,908 km²**
GDP/Capita: **\$34,964**

Provincial Capital: **Fredericton**
Party in Power: **Liberals**
Premier: **Hon. Shawn Graham**

Finance Minister: **Hon. Victor Boudreau**
Legislative Seats: **Liberals 39**
PC 27

Next Election: **September 2010**

New Brunswick posted below-average 1.6% real GDP growth in 2007, as the negative impacts of the surging C\$ and slowing U.S. economy offset an upbeat mining sector. The



Capital projects brightening long-term outlook.

Tax-system review to recommend changes in the fall.

story should remain the same this year, with growth slowing to 1.2% as U.S. export demand softens further.

The province faces the harsh reality of being the country's most export-dependent province, so the strong loonie and slowing U.S. demand will continue to weigh heavily, with the forestry industry hit particularly hard.

However, major capital projects like the \$1.4 billion Point Lep-

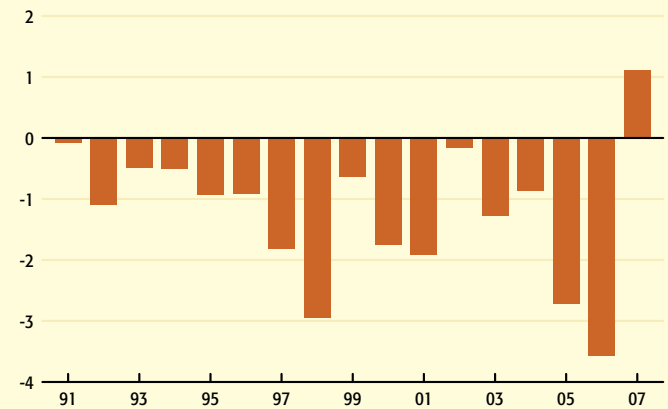
reau nuclear plant upgrade and the \$1.7 billion Potash mine facility continue to fuel non-residential construction activity. Longer term, more stimulus can be expected from the \$7 billion Eider Rock refinery project by Irving Oil.

With all of this construction activity, a lack of skilled labour may be a brewing issue in Atlantic Canada—New Brunswick's unemployment rate is hovering near a record low. Indeed, many of the Atlantic provinces are actively recruiting trades people who left for Western Canada to come back home. There has been some success, with New Brunswick experiencing net in-migration for the first time in 17 years last year. That said, the outlook in Atlantic Canada should improve when the U.S. economy turns the corner, provided the region can attract the necessary skilled labour.

The Province of New Brunswick is projecting a fifth consecutive year of black ink in FY08/09, with the surplus pegged at \$19 million, up from \$18 million in FY07/08. Operating revenues will rise 2.7% to \$7.1 billion in FY08/09, with own-source revenue rising a modest 0.3%. Meantime, total spending is also projected to rise 2.7% to \$7.1 billion, with across-the-board increases in education, health care and social development. New Brunswick plans to borrow \$1.9 billion in FY08/09, with 34% completed by mid-June.

The province is also undergoing a comprehensive review of its tax system with a recent paper outlining a number of options including a flat personal income tax, a reduction in the corporate income tax rate, a B.C.-like carbon tax and an increase in the HST as an offset. A committee has been chosen to review these options, and will present its recommendations in fall 2008 before a "fiscally-neutral" five-year plan is unveiled (presumably, certain tax cuts will be offset by other tax hikes and spending cuts).

NEW BRUNSWICK: HOME FOR A CHANGE
Net Interprovincial Migration (000s)





Nova Scotia

Population: **934,344**
 Percent of Canada: **2.8**
 Rank by Population: **7th**
 Area: **55,284 km²**
 GDP/Capita: **\$35,762**

Provincial Capital: **Halifax**
 Party in Power: **Progressive Conservatives**
 Premier: **Hon. Rodney MacDonald**

Finance Minister: **Hon. Michael Baker**
 Legislative Seats: **PC 21**
New Democrats 20
Liberals 9
Independent 1

Minority Government Since: **June 2006**

Cloudy picture in the manufacturing sector.

Tax cuts propping up consumer spending.

As in much of Atlantic Canada, Nova Scotia's economy is being supported by robust construction spending while facing stiff manufacturing headwinds. As a result, growth likely slipped modestly to 1.4% this year, but should rebound in 2009.

Non-residential construction continues to march ahead, and EnCana's \$700 million Deep Panuke offshore natural gas project should provide an added boost when it begins later this year, with the full impact felt in 2009. Production from the offshore project is expected to commence in 2010. The residential side, while less robust, should contribute modestly to growth this year.

Meantime, while the manufacturing environment is poor, the sector will be buffered by contracts like the one to maintain Canadian military helicopters—manufacturing shipments were up a solid 7.4% y/y in the first quarter. Combined with sturdy spending in the wake of personal income tax breaks, Nova Scotia should stay above water this year, setting the stage for a pick-up in growth in 2009.

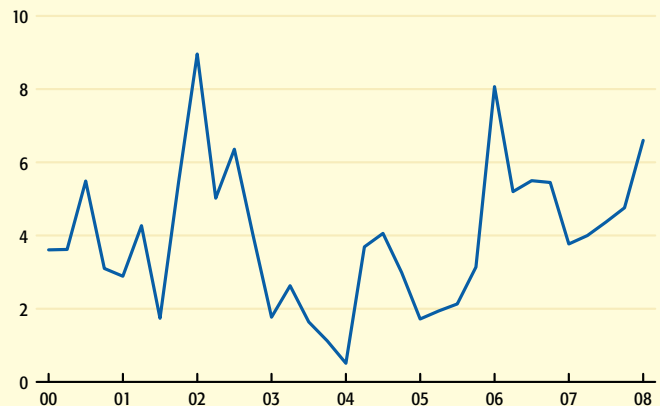
The Province of Nova Scotia is expecting its seventh consecutive year in the black with a projected surplus of \$190 million in FY08/09, up from \$158 million in the prior year. The cautious budget provides a smattering of new tax relief measures and modest spending growth, reflecting concern over the economic outlook—a theme seen throughout most of Central and Eastern Canada.

Revenue is expected to rise 2.3% to \$8.1 billion in FY08/09, with a small offering of new tax cuts amounting to \$24.4 million, while previously announced tax cuts will proceed as planned. Meantime, program spending is expected to rise a modest 3.6% to \$7.4 billion in FY08/09.

Borrowing requirements are expected to be \$915 million in FY08/09, with 9% completed by mid-June.

NOVA SCOTIA: TAX CUTS LIFT CONSUMER SPENDING

Retail Sales (y/y % chng)





Prince Edward Island

Population: **138,563**
 Percent of Canada: **0.4**
 Rank by Population: **10th**
 Area: **5,660 km²**
 GDP/Capita: **\$32,775**

Provincial Capital: **Charlottetown**
 Party in Power: **Liberals**
 Premier: **Hon. Robert Ghiz**

Finance Minister: **Hon. Wes Sheridan**
 Legislative Seats:
Liberals 24
Conservatives 3

Next Election: **May 2011**

C\$ weighing and tax stimulus wearing off.

\$34.9 mln deficit this year—only province in the red.

Economic growth in PEI should slow to 1% this year as consumer activity gives back some of its strength and the U.S. downturn continues.

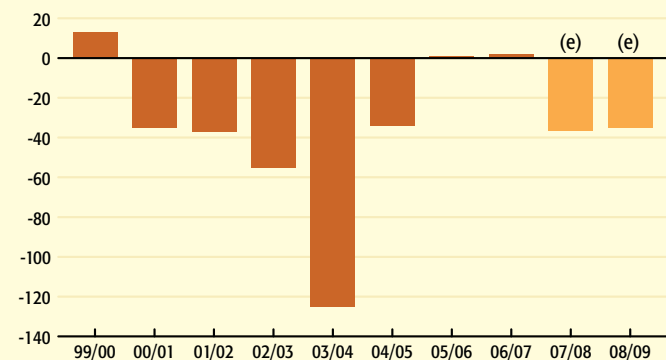
Housing starts remain soft, and consumer activity has lost the momentum from personal income tax cuts. Retail sales rose a below-average 5.3% y/y in the first quarter, down from a high of 9.3% y/y in the third quarter of 2007. Wholesale trade is also down sharply while manufacturing shipments are soft amid the strong dollar and weak U.S. demand.

This year, the strong loonie should also put a damper on tourism activity, as Canadians increasingly head south—if anywhere at all given rising fuel costs—and the C\$ purchasing power of U.S. travelers has fallen sharply.

The Province of Prince Edward Island is projecting a second consecutive budget deficit in FY08/09, making it the only Canadian province to dip its pen in red ink this year. The deficit is expected to come in at \$34.9 million, a slight improvement over \$36.6 million in FY07/08. Total revenue is projected to grow 6.8% to \$1.35 billion in FY08/09, led by strong growth in both own-source (6.2%) and federal transfer (7.8%) revenues, while total expenditure is projected to grow 6.4% in FY08/09, to \$1.39 billion.

Borrowing requirements are expected to be \$161 million in FY08/09, with 38% completed by mid-June.

PEI: BACK IN THE RED
 Budget Balance (C\$ mlns)



(e) = estimate



Newfoundland & Labrador

Population: **507,298**
 Percent of Canada: **1.5**
 Rank by Population: **9th**
 Area: **405,720 km²**
 GDP/Capita: **\$49,374**

Provincial Capital: **St. John's**
 Party in Power: **Progressive Conservatives**
 Premier: **Hon. Danny Williams**

Finance Minister: **Hon. Thomas Marshall**
 Legislative Seats:
PC 44
Liberals 3
New Democrats 1

Next Election: **October 2011**

Newfoundland & Labrador led the country in economic growth in 2007, with real GDP rising a



Offshore oil output to fall this year, but underlying trends solid.

Energy prices fuel record surplus in FY07/08.

torrid 9.1% amid a rebound in offshore drilling and mining activity. This year, that boost will wear off and pull growth down to a below-average 0.9%, but the underlying trends still look good.

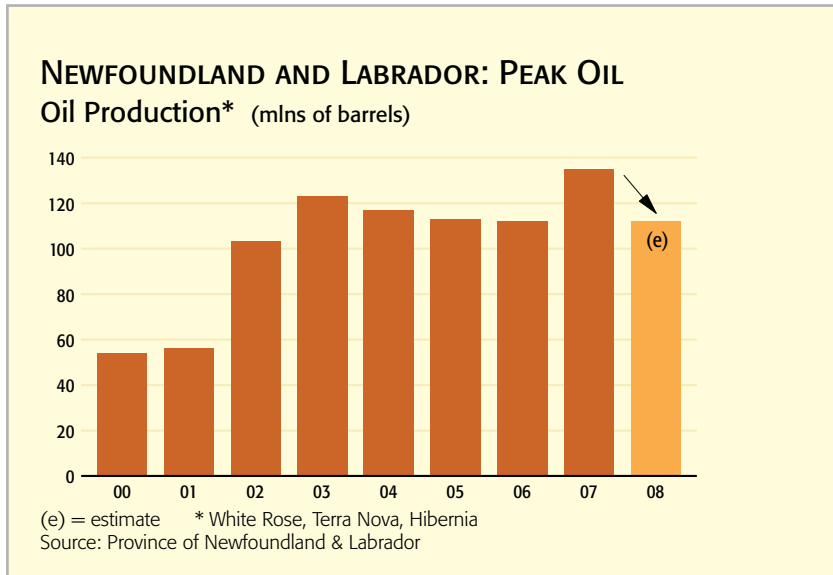
Output at the province's three major offshore oil projects rebounded sharply in 2007, with Terra Nova providing most of the punch, while output at the Voisey's Bay nickel mine returned to normal after strikes plagued much of 2006. However, offshore oil production is expected to decline 17% this year, weighing heavily on the headline GDP number. Longer term, the province's royalty deal on the Hebron oilfield project is expected to generate revenues of \$16 bln over its 25-year life, and employ about 1,000 people when construction begins in 2010.

While headline GDP growth will stall this year, the underlying economic trends remain rosy. The commodity boom has lined the province's coffers, allowing income tax cuts to add an additional boost to consumer spending—retail sales were up 9% y/y in Q1, outpaced only by Saskatchewan. Meantime, a reversal in migration flows has sprung population growth back into positive territory after three years of outright declines, while the housing market now trails only Saskatchewan in price momentum, with average prices up 21% y/y in May.

But the upbeat mood is not without some warnings. A multi-year exodus of migrants has drained the skilled labour pool, and the province is now working hard to bring people back. A lack of skilled labour could be a serious constraint on the province, preventing it from fully capitalizing on the current commodity boom.

The Province of Newfoundland and Labrador revised up its FY07/08 surplus estimate to a record \$1.4 billion from its prior estimate of \$882 million, driven by higher-than-expected revenue as energy prices surged. For FY08/09, the province expects the surplus to shrink to \$544 million amid further tax cuts and aggressive spending, and fall further to \$236 million by FY10/11. Revenue is expected to decline 3.7% to \$6.4 billion in FY08/09. After cutting personal income tax rates last year, another 1% will be shaved off each tax bracket effective July 1st, 2008. Meantime, spending is expected to surge 11% to \$6.0 billion, giving Newfoundland & Labrador the distinction of fastest projected spending growth in Canada. The province expects no net new borrowing in FY08/09.

Commodity note: The province is assuming \$87 oil in FY08/09, offering upside at current prices.



PROVINCIAL ECONOMIC SUMMARY

	BC	Alberta	Sask.	Man.	Ontario	Quebec	NB	NS	PEI	NL	Canada
Real GDP Growth (chain-weighted : y/y % chng)											
2007	3.1	3.3	2.8	3.3	2.1	2.4	1.6	1.6	2.0	9.1	2.7
2008 f	2.2	2.5	3.0	2.1	0.2	0.6	1.2	1.4	1.0	0.9	1.0
2009 f	2.7	2.9	2.5	2.5	2.0	2.1	2.2	2.5	1.9	2.6	2.2
Employment Growth (y/y % chng)											
2007	3.2	4.7	2.1	1.6	1.5	2.3	2.1	1.3	1.2	0.7	2.3
2008 f	2.6	3.0	1.5	1.7	1.2	1.3	1.2	0.4	1.6	2.7	1.6
2009 f	2.0	2.1	1.3	1.3	0.7	0.7	1.5	0.6	0.4	1.8	1.1
Unemployment Rate (%)											
2007	4.2	3.5	4.2	4.4	6.4	7.2	7.6	8.1	10.3	13.6	6.0
2008 f	4.3	3.4	4.3	4.2	6.6	7.5	8.6	8.2	10.8	12.6	6.2
2009 f	4.3	3.6	4.1	4.3	6.8	7.8	8.6	8.4	11.2	11.9	6.3
Housing Starts (000s)											
2007	39.2	48.1	5.9	5.8	68.0	48.5	4.1	4.7	0.7	2.6	227.6
2008 f	37.0	39.5	6.1	5.8	65.9	44.0	3.8	4.4	0.6	2.8	209.8
2009 f	36.0	40.0	5.5	4.6	62.0	41.5	3.4	3.3	0.6	3.2	200.0
Consumer Prices (y/y % chng)											
2007	1.8	4.9	2.9	2.1	1.8	1.7	1.9	1.9	1.8	1.6	2.1
2008 f	2.4	3.9	3.5	2.3	2.0	2.1	1.9	2.8	2.5	2.8	2.4
2009 f	2.2	2.8	2.9	2.1	2.0	2.0	2.1	2.4	2.3	2.5	2.2

PROVINCIAL ECONOMIC INDICATORS

(3-mnth m.a. : y/y % chng)

Retail Sales

Feb 08	5.3	5.4	16.4	11.8	6.0	6.0	5.4	5.3	5.6	9.3	6.4
Mar 08	4.1	3.8	14.8	11.3	6.0	5.8	5.6	6.5	5.4	9.5	5.9
Apr 08	3.2	2.5	13.8	9.5	4.6	4.8	4.9	5.8	5.0	7.9	4.7

Manufacturing Shipments

Feb 08	-7.6	-0.6	11.1	0.8	-8.0	-1.7	20.8	8.4	-5.9	18.0	-3.9
Mar 08	-8.6	-3.1	8.8	-3.9	-10.2	-3.6	22.8	8.1	-1.9	15.6	-6.0
Apr 08	-8.6	-2.6	11.4	-4.8	-9.0	-3.5	33.7	10.4	-1.7	13.0	-5.1

Exports

Feb 08	-11.5	20.5	27.8	2.3	-15.2	-7.9	10.8	5.6	-10.0	0.3	-5.4
Mar 08	-12.6	23.5	37.4	2.3	-15.0	-6.9	16.1	2.0	1.1	-1.5	-2.1
Apr 08	-11.3	30.6	42.8	-1.9	-13.2	-1.7	23.9	-2.2	1.4	6.2	-0.7

Employment Growth

Mar 08	2.4	3.3	0.9	1.7	1.8	2.1	2.1	0.4	0.8	2.3	2.0
Apr 08	2.7	3.1	1.3	2.1	2.0	1.5	1.8	0.3	1.0	1.9	2.1
May 08	2.8	3.2	1.4	2.1	2.1	1.1	1.2	0.7	1.7	2.3	2.0

PROVINCIAL FISCAL SUMMARY

FY08/09 (as of June 19, 2008)

	Budget Balance (\$ mlns)	% of GDP	Gross Financing Requirements** (\$ blns)	S&P	Moody's	DBRS
British Columbia	50	0.0	5.2	AAA	Aaa	AA (high)
Alberta	1,568	0.6	1.7	AAA	Aaa	AAA
Saskatchewan	250	0.5	0.9	AA	Aa1	AA (low)
Manitoba	96	0.2	2.8	AA	Aa1	A (high)
Ontario	0	0.0	24.3	AA	Aa1	AA
Quebec	0	0.0	11.1	A+*	Aa2	A (high)
New Brunswick	19	0.1	2.2	AA-	Aa1	A (high)
Nova Scotia	190	0.5	1.9	A+*	Aa2	A
PEI	(35)	(0.7)	0.9	A*	Aa2	A (low)
Nfld & Labrador	544	2.1	0.2	A	Aa2	A (low)
Total Provincial	2,682	0.2	51.2			

Source: Provinces and BMO Capital Markets () = deficit

* positive outlook ** includes provincial crown corporations

HISTORY OF CANADIAN FISCAL BALANCES

(\$ mlns)

	97/98	98/99	99/00	00/01	01/02	02/03	03/04	04/05	05/06	06/07	07/08e	08/09f
BC	(167)	(1,003)	148	1,503	(1,184)	(2,737)	(1,191)	2,696	3,090	4,056	1,970	50
Alberta	2,659	1,094	2,791	6,571	1,081	2,133	4,136	5,175	8,551	8,510	4,031	1,568
Saskatchewan	35	28	83	58	1	1	1	383	400	293	347	250
Manitoba	76	31	11	40	63	4	(577)	562	394	430	329	96
Ontario	(3,966)	(2,002)	668	1,902	375	117	(5,483)	(1,555)	298	2,269	600	0
Quebec	(2,157)	126	7	427	22	(728)	(358)	(664)	37	109	0	0
NB	(1)	(204)	(30)	43	79	1	(173)	242	235	237	18	19
NS	(442)	(261)	(797)	147	113	28	38	170	228	182	158	190
PEI	(7)	28	13	(35)	(37)	(55)	(125)	(34)	1	2	(37)	(35)
NL	133	(187)	(269)	(350)	(468)	(644)	(914)	(489)	77	154	1,377	544
Provinces	(3,837)	(2,349)	2,625	10,306	45	(1,881)	(4,646)	6,486	13,311	16,242	8,793	2,682
Federal	2,959	5,779	14,258	19,891	8,048	6,621	9,145	1,463	13,218	13,800	10,200	2,300
Total	(878)	3,430	16,883	30,197	8,093	4,740	4,500	7,949	26,529	30,042	18,993	4,982

HISTORY OF CANADIAN FISCAL BALANCES

(% of GDP)

	97/98	98/99	99/00	00/01	01/02	02/03	03/04	04/05	05/06	06/07	07/08e	08/09f
BC	(0.1)	(0.9)	0.1	1.1	(0.9)	(2.0)	(0.8)	1.7	1.8	2.3	1.1	0.0
Alberta	2.5	1.0	2.4	4.5	0.7	1.4	2.4	2.7	3.9	3.5	1.5	0.6
Saskatchewan	0.1	0.1	0.3	0.2	0.0	0.0	0.0	1.0	0.9	0.7	0.8	0.5
Manitoba	0.3	0.1	0.0	0.1	0.2	0.0	(1.5)	1.4	0.9	1.0	0.7	0.2
Ontario	(1.1)	(0.5)	0.2	0.4	0.1	0.0	(1.1)	(0.3)	0.1	0.4	0.1	0.0
Quebec	(1.1)	0.1	0.0	0.2	0.0	(0.3)	(0.1)	(0.3)	0.0	0.0	0.0	0.0
NB	(0.0)	(1.2)	(0.2)	0.2	0.4	0.0	(0.8)	1.0	1.0	0.9	0.1	0.1
NS	(2.2)	(1.2)	(3.5)	0.6	0.4	0.1	0.1	0.6	0.7	0.6	0.5	0.5
PEI	(0.3)	0.9	0.4	(1.0)	(1.1)	(1.5)	(3.3)	(0.8)	0.0	0.0	(0.8)	(0.7)
NL	1.3	(1.7)	(2.2)	(2.5)	(3.3)	(3.9)	(5.0)	(2.5)	0.4	0.7	5.5	2.1
Provinces	(0.4)	(0.3)	0.3	1.0	0.0	(0.2)	(0.4)	0.5	1.0	1.1	0.6	0.2
Federal	0.3	0.6	1.5	1.8	0.7	0.6	0.8	0.1	1.0	1.0	0.7	0.1
Total	(0.1)	0.4	1.7	2.8	0.7	0.4	0.4	0.6	1.9	2.1	1.2	0.3

The information, opinions, estimates, projections and other materials contained herein are provided as of the date hereof and are subject to change without notice. Some of the information, opinions, estimates, projections and other materials contained herein have been obtained from numerous sources and Bank of Montreal ("BMO") and its affiliates make every effort to ensure that the contents thereof have been compiled or derived from sources believed to be reliable and to contain information and opinions which are accurate and complete. However, neither BMO nor its affiliates have independently verified or make any representation or warranty, express or implied, in respect thereof, take no responsibility for any errors and omissions which may be contained herein or accept any liability whatsoever for any loss arising from any use of or reliance on the information, opinions, estimates, projections and other materials contained herein whether relied upon by the recipient or user or any other third party (including, without limitation, any customer of the recipient or user). Information may be available to BMO and/or its affiliates that is not reflected herein. The information, opinions, estimates, projections and other materials contained herein are not to be construed as an offer to sell, a solicitation for or an offer to buy, any products or services referenced herein (including, without limitation, any commodities, securities or other financial instruments), nor shall such information, opinions, estimates, projections and other materials be considered as investment advice or as a recommendation to enter into any transaction. Additional information is available by contacting BMO or its relevant affiliate directly. BMO and/or its affiliates may make a market or deal as principal in the products (including, without limitation, any commodities, securities or other financial instruments) referenced herein. BMO, its affiliates, and/or their respective shareholders, directors, officers and/or employees may from time to time have long or short positions in any such products (including, without limitation, commodities, securities or other financial instruments). BMO Nesbitt Burns Inc. and/or BMO Capital Markets Corp., subsidiaries of BMO, may act as financial advisor and/or underwriter for certain of the corporations mentioned herein and may receive remuneration for same. "BMO Capital Markets" is a trade name used by the Bank of Montreal Investment Banking Group, which includes the wholesale/institutional arms of Bank of Montreal, BMO Nesbitt Burns Inc., BMO Nesbitt Burns Ltée/Ltd., BMO Capital Markets Corp. and Harris N.A., and BMO Capital Markets Limited.

TO U.S. RESIDENTS: BMO Capital Markets Corp. and/or BMO Nesbitt Burns Securities Ltd., affiliates of BMO NB, furnish this report to U.S. residents and accept responsibility for the contents herein, except to the extent that it refers to securities of Bank of Montreal. Any U.S. person wishing to effect transactions in any security discussed herein should do so through BMO Capital Markets Corp. and/or BMO Nesbitt Burns Securities Ltd.

TO U.K. RESIDENTS:

The contents hereof are not directed at investors located in the U.K., other than persons described in Part VI of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001.

™ - "BMO (M-bar roundel symbol) Capital Markets" is a trade-mark of Bank of Montreal, used under licence.

© Copyright Bank of Montreal