BMO Blue Book

May 2015

BMO Financial Group

We're here to help.™

Canada

ECONOMICS

Douglas Porter, CFA,
Chief Economist &
Managing Director

Changing of the Guard

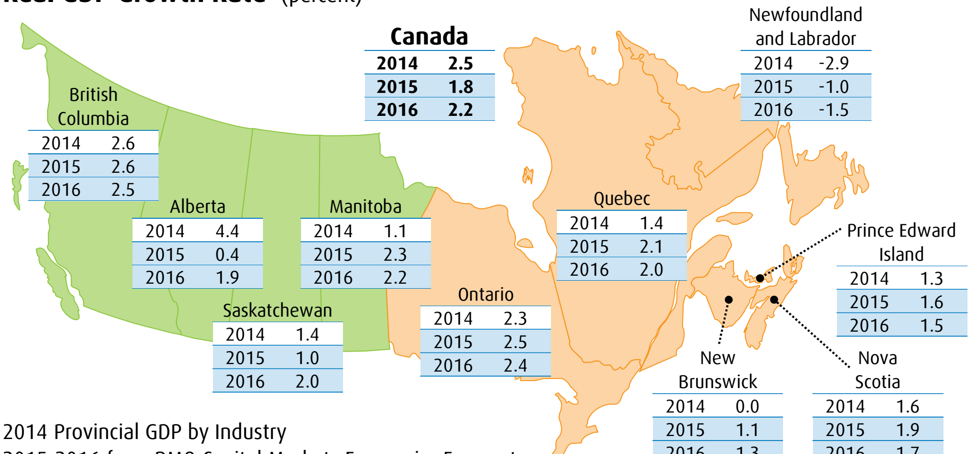
The Canadian economy is grappling with the big drop in oil prices, and the net impact will be a downshift in overall growth in 2015. Real GDP is likely to expand at a 1.8% clip, down from a 2.5% pace in 2014, as lower oil prices carve roughly half a percentage point from growth. But the more dramatic impact will be how the regional landscape is shaken up this year, as previously high-flying oil-producing provinces plunge to the bottom of the growth leaderboard, while some past persistent laggards move toward the top.

After several years of stark outperformance, economic growth in **Alberta** is expected to slow to just 0.4% this year, effectively placing the province in recession. The slide in oil prices has taken a chunk out of capital spending budgets, even as oil production continues to grow—the bulk of oilsands capital is invested up front. This has tipped the housing market into a correction and weakened the employment backdrop, which in turn will stem the inflow of migrants from other areas of the country. **Saskatchewan's** energy sector will also feel the impact, and growth is expected at 1.0% this year, although conditions for potash and agriculture are more favourable. **Newfoundland & Labrador** is likely to see GDP contract 1.0% this year as fiscal restraint remains heavy and oil production fades until more output is brought online later in the decade.

There are, however, some winners. **British Columbia** is projected to lead the pack this year, with real GDP growth expected at 2.6%. The province's resource base is much more diverse (natural gas, base metals, forestry and little direct exposure to oil), while exports and manufacturing should benefit from the powerful combination of sturdy U.S. demand and a weaker Canadian dollar. Central Canada also stands to benefit in that environment, along with lower input costs through the manufacturing supply chain. Importantly, the weakness in oil prices is largely due to a supply shock, not sluggish external demand, especially in Canada's largest trading partner. In fact, when considering the benefit of lower oil prices, strong

Provincial GDP

Real GDP Growth Rate (percent)



2014 Provincial GDP by Industry
2015-2016 from BMO Capital Markets Economics Forecasts

U.S. demand and a weaker loonie, 2015 may be nearly as good as it gets in Central Canada. As a result, real GDP growth in **Ontario** is expected at 2.5%, which would top the national average for the first time in 13 years. Growth in **Quebec** is expected to pick up to 2.1%, supported as well by an element of political stability that has been lacking in the province for some time, but still burdened by fiscal restraint on both the expenditure and taxation fronts (at least for one more year). **Manitoba's** diverse economy should grow 2.3%. One reason that these manufacturing-heavy provinces will struggle to churn out more than 2.5% growth, despite all of the tailwinds, is that the sector does not carry the weight it did in the past, especially after significant capacity was destroyed during the Great Recession. Ontario's auto sector, for example, is effectively running at full capacity, and new investment is increasingly getting directed toward the Southern U.S. and Mexico.

Finally, Atlantic Canada will remain subdued, in part due to demographic challenges and fiscal restraint. But, growth in most of the region is expected to improve from the sluggish pace of recent years, and slower activity in Alberta could cool the exodus of younger workers. **Nova Scotia** is poised to lead the region at 1.9% this year, as work begins on the federal shipbuilding contract. **New Brunswick** faces a stagnant population, but a weaker loonie should boost exports and tourism, and in **PEI** as well—look for growth of 1.1% and 1.6%, respectively.

Budget Season Wrap Up

Much of what Ottawa giveth in tax cuts this year, the provinces will taketh away. Indeed, with all but PEI's budget in hand as we go to print, net tax/fee increases for FY15/16 total nearly $3 billion. British Columbia is the odd province out, while Quebec's total includes measures in the fall fiscal update. Alberta saw personal income tax rates lifted on incomes above $100,000 in addition to a new health levy and a host of user fee increases—a looming election as we go to print will determine the fate of these measures. Most of Atlantic Canada is also pushing through tax hikes, especially in Newfoundland & Labrador where the budget has been challenged by lower oil royalties. Ontario, however, announced only a minor net tax increase, leaning instead on asset sales now, and cap-and-trade revenues later (the latter is not built into the fiscal plan). All told, **while Ottawa's package of tax cuts/benefit increases will come in at just over $5 billion in FY15/16, it looks like the Provinces will take back a bit more than half of it**. Meantime, government spending in most regions will decline on a real per-capita basis.

Revenue-raising measures and spending restraint will leave the combined deficit pegged at $13.6 billion versus the $12.6 billion now estimated for FY14/15, or a relatively modest 0.7% of GDP. Beneath the steady overall bottom line, there are notable changes below the surface. Alberta's budget balance will see the largest deterioration (more than $5 billion) this year amid a slide in oil revenues, while British Columbia will see its surplus shrink. On the flip side, Ontario and Quebec are looking at much-improved bottom lines, with each expecting a balance about $2.5 billion better than in FY14/15—a surplus in Quebec (before Generations Fund transfers) and a less-wide deficit in Ontario. Atlantic Canada remains challenged by a sluggish economy and weakening demographics. New Brunswick's deficit will widen this year to among the deepest in Canada as a share of GDP, while Nova Scotia continues to see gradual improvement in its budget metrics, leaving it in arguably the most favourable position in Atlantic Canada. Overall, 6 of 10 provinces are expecting an improvement in their FY15/16 bottom lines.

British Columbia

ECONOMICS

Robert Kavcic,
Senior Economist

Economic growth remains sturdy in British Columbia, and the province is expected to lead the pack in 2015. Real GDP is expected to expand 2.6% this year, in-line with the pace recorded in 2014, and leading the country for the first time in a decade. While the housing market continues to strengthen, particularly in Vancouver, firm U.S. demand and a weak Canadian dollar should offset the slowdown in China and uncertainty in the mining sector.

The **housing market** continues to strengthen as mortgage rates plumb new lows. Sales across the province hit the best level in more than 5 years in March—early-year demand was helped by mild weather, but underlying strength looks real. That has helped pull the months' supply of homes available for sale down to the lowest since early-2010—just below 6 now versus more than 10 at the end of 2012. In Vancouver, prices are rising again, up 6.4% y/y alongside torrid gains in the detached market. Housing starts remain remarkably stable in the province, running at a 28,000 unit pace in 2014, little changed from levels recorded in each of the prior 4 years. That said, Vancouver still faces an elevated number of completed but unoccupied units on the market (mostly condos), but that continues to trend down. As a result, new residential construction activity will likely remain relatively stable as current supply is absorbed.

While the province has little direct exposure to oil, **non-energy mining investment** has downshifted, with non-gas capital spending down sharply for a second straight year in 2014 amid a lower commodity price backdrop. While the **LNG** tax framework was revamped to create a more competitive backdrop, development remains highly uncertain given lower oil prices and industry consolidation—any economic benefits are still years away. Non-energy **exports** are growing at a solid clip, with forestry benefiting from a weaker currency and solid U.S. housing starts (the province now exports roughly equal amounts to the U.S. and Asia). B.C.'s **labour market** performance remains disappointing, with employment up just 0.5% y/y in Q1, largely because of weakness in the public sector and construction. However, the unemployment rate is a relatively-low 5.8%, and interprovincial migration has turned positive.

The Province of British Columbia is projecting a modest **$284 million surplus** for FY15/16 (0.1% of GDP), smaller than the $879 million now estimated for FY14/15. Contingencies and allowances of $600 million leave plenty of wiggle room for the Province to hit this target. Modest surpluses extend over the three-year fiscal plan and, importantly for B.C., net debt continues to grind down as a share of GDP, dipping below 16% by FY17/18. In fact, FY15/16 net debt is now pegged fully $1.3 billion lower than expected at this time last year, a positive development that has been recognized by Moody's (removing the negative credit-rating outlook). This year's budget offered few major new policy initiatives.

COMMERCIAL BANKING

Mike Bonner,
Senior Vice President,
British Columbia and
Yukon Division,
BMO Bank of Montreal

Sean Armstrong,
Regional Vice President,
Commerical Banking,
B.C, Vancouver Island
and Yukon,
BMO Bank of Montreal

Dean Kirkham,
Regional Vice President,
Commercial Banking,
Greater Vancouver,
BMO Bank of Montreal

The business momentum in Vancouver continues to be strong with our commercial clients investing back into their business and going into new markets. Our customer's confidence seems to be returning to prerecession levels. The confidence stems from the improving US housing market which has bolstered our forestry industry, the lower Canadian dollar making our exports more competitive, a low interest rate environment and the continuation of significant foreign investment into Vancouver and other parts of BC. Our clients are expanding.

Demand from the new Canadian investors immigrant market - primarily China - continues to grow. The demand for commercial real estate remains stable, while demand for agricultural properties continues to grow as these buyers look to export value-added agricultural products to China.

A trend to watch and support has been the recent M&A activity. Over the past few years we have seen consolidation from a number of our clients with deep balance sheets expanding via acquisition; we anticipate this trend will continue. As an example, in healthcare, we are seeing larger customers looking to capitalize on the efficiencies of a group by acquiring single practices that are transitioning into retirement.

Looking at our rural markets, across the board we are seeing positive indicators for some strong years ahead in Agriculture. We had a fantastic winter which brought the bears out of hibernation early and put our crops about 2-3 weeks ahead of last year. Throughout the sector, production remains strong and growth still evident.

The Dairy industry has experienced lower feed costs, steady milk prices, and additional allocations of quota of up to 10% as well as sleeve days. Continuing the trend, the organic and specialty milk markets are growing and becoming more efficient and profitable.

Our Aboriginal clients continue to show strong economic growth throughout the province with investments in infrastructure projects, for profit businesses and partnering with other businesses and industries contributing to the overall health of this sector. We see significant growth potential here.

The low dollar is expected to have a positive impact on tourism throughout the region and we would anticipate seeing more US visitors and Canadians visiting.

The technology sector continues to show strong growth in a number of markets throughout the province. We see this industry continuing as a strong economic driver and one where we want to continue to build the knowledge, capabilities and relationships to support its future growth.

Alberta

ECONOMICS

Robert Kavcic,
Senior Economist

The slide in oil prices will have a major negative impact on Alberta's economy this year, with real GDP growth expected at just 0.4%, effectively placing the province in recession. That would be down from steady 4%-plus growth over the prior five years, a period in which the province stood head and shoulders above the rest of the country. By 2016, growth should improve again to 1.9%, assuming WTI oil prices push back up above $65.

The **energy sector** directly accounts for roughly 25% of Alberta GDP, 7% of employment and almost two-thirds or private non-housing capital spending. As a result, the drop in prices will likely cut roughly 3 ppts from provincial growth this year, largely through the capital spending channel as major producers have slashed their budgets. Oilsands production, however, is expected to hold up much better given that much of the cost of long-life projects is sunk up front. Indeed, total oil production continued to run at an 11% y/y pace as of Q4, led by bitumen.

Employment has held up well through Q1, up 2.2% y/y and still among the strongest in Canada. While resource-sector employment has slid by more than 17,000 (9.4%) since peaking in September, the losses have been more than offset by gains in the service sector. That said, the jobless rate has moved up to 5.5% as of March, the highest level since mid-2011, and after vying for the lowest rate in the country in recent years, it is now bettered by Saskatchewan, Manitoba and, possibly soon, British Columbia. As a result, look for **interprovincial migration** flows to Alberta to slow considerably this year—there were a net 33,000 inward migrants in 2014, which added nearly a full percentage point to population growth. This will continue to weigh on Alberta's **housing market**, which is in the grips of a correction. In Calgary, for example, existing home sales are 40% below mid-2014 levels, while new listings have surged—the dramatic shift in market balance has begun to drag down prices.

The Province of Alberta is projecting a **$5.0 billion deficit** for FY15/16 as resource revenues have plunged. The shortfall weighs in at a still-manageable 1.5% of GDP, but that marks the deepest budget hole for the Province in 22 years. In order to cushion the blow, the Province is raising $1.5 billion in new revenues through a variety of tax increases, cutting nominal spending by $323 million and drawing down the Contingency Account. The deficit remains large at $3.0 billion in FY16/17 before returning to a small surplus in FY17/18 as WTI oil prices are expected to rebound to around $75. The Province will continue to borrow aggressively (by Alberta's standards) for capital purposes, pulling the balance sheet into a net debt position by FY16/17. Among the **tax measures** announced was a change to the personal income tax structure away from a 10% flat rate (beginning in the 2016 tax year, the tax rate on incomes above $100k will gradually rise to 11.5% by 2018); and a health care contribution at incomes above $50k. As we go to print, voters are about to decide the fate of a four-decade PC dynasty.

COMMERCIAL BANKING

Susan Brown,
Senior Vice President,
Alberta & NWT Division,
BMO Bank of Montreal

Lynda Taylor,
Regional Vice President,
Commercial Banking,
Northern Alberta,
BMO Bank of Montreal

Mike Darling,
Regional Vice President,
Commercial Banking,
Southern Alberta,
BMO Bank of Montreal

Alberta businesses have long benefited from resilience and a can-do attitude. The province will benefit from that outlook now more than ever.

Clearly, the oil and gas story dominates the picture for businesses in Alberta. At the moment, firms seem to be holding their own—but we are all waiting for the other shoe to drop.

We won't have a real sense of how the industry has been affected until spring breakup has concluded, when heavy trucks can start traversing the province's roads. At that point, we will see how many service contracts are renewed, or not. That will give us a sense of the impact of the oil price drop on the industry in Alberta.

There will always be production in Alberta, but new projects are being put on hold. This slowdown has inevitably led to a reduction in jobs, especially for contract workers from other provinces. As a result, the impact on Alberta residents may be somewhat muted.

We need to remember that the oil and gas industry in Alberta has been through difficulties of this sort before. Well-run firms are concentrating on productivity. It's not their first rodeo—after several years of high oil prices, many have amassed significant war chests, and now they're selling equipment and hunkering down until conditions change. Firms have long been philosophical about the cyclical nature of the sector; they know that higher prices will return eventually.

Other industries continue to roll along. The agriculture sector will benefit from lower fuel input costs; assuming a good growing season, we expect our customers to have a good year. Livestock, in particular, should continue to do well with beef prices higher than they have been in a long time.

Tourism will benefit from the lower Canadian dollar, with more visitors coming in from the United States and more Canadians choosing to travel within the country. We also continue to see reasonable growth in the service sector.

We know that the resilience of Alberta is being put to the test; we have every confidence that the province's businesses will continue showing their strength and resourcefulness.

Saskatchewan

ECONOMICS

Robert Kavcic,
Senior Economist

Saskatchewan's economy is being tripped up by the slide in oil prices, with real GDP expected to remain subdued at 1.0% in 2015. While that is only modestly weaker than last year's 1.4% pace, 2014 was depressed by a steep drop in crop production after a bumper year in 2013. Smoothing out the prior five years saw Saskatchewan's economy grow at a blistering 3.9% clip, so this year's expected performance would mark a meaningful downshift in growth.

The **oil sector** is expected to retrench this year amid a much weaker price environment, with the Province expecting a 4% drop in oil production in 2015. Note that oil & gas directly accounts for roughly 15% of Saskatchewan's GDP—well below Alberta, but still a significant weight. Other resource sectors are expected to buffer the weakness in oil, including an expected 8% increase in **potash** production, while **farm-sector** growth is expected to normalize after steep production declines in 2014 (post-2013 bumper crop)—Statistics Canada estimates wheat and canola production were down 27% and 20%, respectively, last year.

The **labour market** performance has weakened in recent months, with employment growth slowing to 0.4% y/y in Q1 alongside a drop in private-sector jobs—recent weakness has been in manufacturing, resources and construction. **Population growth** remains historically high at 1.5% y/y, but those inflows are facing a higher unemployment rate—the jobless rate is still relatively low at just under 5%, but that's up from just 3.4% as recently as November. **Housing** demand has also weakened, with existing home sales sliding more than 12% y/y in Q1. This is proving to be bad timing given already-elevated supply in Regina and Saskatoon—there are a record number of completed but unoccupied units overhanging these two cities. In the resale market, the months' supply of homes for sale has shot up to more than 9, the highest in at least a decade. As a result, prices are correcting with Regina's benchmark price down more than 6% since its late-2013 high.

The Province of Saskatchewan is projecting a **$106.8 million surplus** on a summary basis for FY15/16, or a small 0.1% of GDP. That's up from $40.5 million now expected in FY14/15, as higher tax receipts and potash revenues offset a drop in oil revenues. The latter surplus is tracking smaller than expected at midyear ($70.9 million) as revenues have been clipped. The Province is also projecting modest surpluses through the 4-year forecast horizon, averaging just under $140 million per year. While operating spending will be well-contained this coming fiscal year, capital expenditures are getting a healthy boost—that doesn't impact the operating balance, but will add significantly to the Province's (comparatively favourable) debt load. Some policy measures were also taken in this budget to boost revenues, most notably a change to **profit taxes in the potash-sector**—capital spending for project maintenance and new expansion will now be deducted over a longer period of time, boosting near-term revenues for the Province.

COMMERCIAL BANKING

John MacAulay,
Senior Vice President,
Prairies and
Central Canada,
BMO Bank of Montreal

Pam Spady,
Regional Vice President,
Prairies and Central
Canada Division,
BMO Bank of Montreal

The recent drop in the price of oil and gas is leading to a new level of caution among Saskatchewan businesses. The full degree of the impact will be more easily measured as we move into the summer months. We know the other shoe will drop; it's just a matter of when.

Last year, the industry moved from strength to strength, with places like the Bakken, Lloydminster and Maple Creek benefitting the most. Now, we have to expect companies there to start dialing back. Those which have set funds aside to cope with the price drop will clearly fare the best.

We're actually keeping an eye on our commercial customers on a week-by-week basis to see how they are faring. That said, we have not seen a significant amount of weakening; we're hopeful that most of our customers will be able to weather the downturn and emerge from this period of lower prices in a healthy state.

Other industries that have been supported by the oil and gas boom are now anticipating slowdowns as well. As an example, we have noted a softening in our mortgage growth in the southern part of the province, such as in Regina and Estevan. We can assume this is partly a function of fewer people entering the province, which has corresponding effects to construction and retail sales.

Cities such as Regina and Saskatoon still have a number of projects on the go, however; construction for transportation, universities, hospitals and schools continues, with related support for trades and engineering companies. A shortage of labour may cause difficulties, however, if the influx of skilled labour continues to slow.

In agriculture, which remains the largest part of our commercial portfolio in the province, we expect that lower energy prices and the weaker Canadian dollar will help support Saskatchewan farmers. Last year, the slowdown in grain shipping caused some difficulty but we still saw a number of our customers remain stable; as well, farm equipment dealers did not see a significant drop in purchases. If we get a positive growing season with the weather, we are hopeful this resilient sector will have a strong year.

Manitoba

ECONOMICS

Robert Kavcic,
Senior Economist

Manitoba's sturdy and diverse economy is expected to improve this year, with real GDP growth pegged at 2.3%, up from a 1.1% pace in 2014. Note that last year's performance was weighed down a big drop in crop production after a bumper year in 2013. With little direct exposure to oil and a diverse manufacturing sector, that would leave growth ahead of the national average for the third time in four years.

Output in the **agriculture** sector has swung wildly in recent years, with production of wheat (-35%) and canola (-26%) expected to be down sharply in 2014 after a bumper crop in the prior year. Meantime, while **oil production** has risen fourfold since the start of the 2000s, the sector directly makes up a very modest 2.5% of real GDP in the province.

Manufacturing output has had a solid run since 2010, and is expected to benefit in the year ahead from the combination of a weaker Canadian dollar and still-strong U.S. demand. Shipments weakened somewhat around the turn of the year (possibly weather related), but underlying trends are still positive—in particular, transit-sector orders are rolling in from various municipalities (public transit) and U.S. cities with improved fiscal backdrops. And, despite some turn-of-the-year weakness, non-energy exports are holding near cycle highs.

The **labour market** has also improved, in contrast to its nearest neighbours to the west. Employment growth led the country in March at a very strong 3.1% y/y clip, the best pace the province has seen in 13 years amid broad-based hiring (note that these estimates from the Labour Force Survey may be exaggerating growth, as the payrolls survey is showing much more subdued trends). Still, at 5.4% in March, the jobless rate is now second lowest in the country.

Population growth remains at historically-strong levels, holding at 1.3% y/y in 2015Q1. That continues to support **housing** demand, which has held steady despite steep declines in both Alberta and Saskatchewan in recent months. Housing starts, however, have rolled over after hitting the highest level since the late-1980s in 2013.

The Province of Manitoba is projecting a **$422 million budget deficit in FY15/16**, a still-manageable 0.6% of GDP, but little improvement over the $424 million shortfall expected for FY14/15. The budget will now return to surplus a year later than previously expected, in FY19/20, pushing its timeline a year behind Ontario. And, cumulative deficits over the 2014-to-2018 period are now running a hefty $1.1 billion larger than expected a year ago. As a result, net debt is tracking on a higher path, and is expected to near 31% of GDP this fiscal year. With an election looming next spring, this budget comes with sturdy spending growth, and only modest net new tax increases.

COMMERCIAL BANKING

John MacAulay,
Senior Vice President,
Prairies and
Central Canada,
BMO Bank of Montreal

Ron Collins,
Vice President,
Commercial Banking,
BMO Bank of Montreal

Manitoba businesses continue to benefit from the strong diversity of the provincial economy. With the lower dollar and stronger U.S. economy, we expect those benefits to keep the provincial economy in a solid position.

The recently released strong job creation numbers for Winnipeg and the province as a whole bear out what we've been seeing among our customers. Several are having record years, and they're taking the income they are receiving to invest in new machinery—ensuring continued improvement their long-term productivity.

We also continue to see more economic growth and investment by the province's First Nations. Reserves are engaged in major infrastructure projects, which create local jobs and improve the quality of life in Aboriginal communities.

On the construction side, customers working in the mining sector and on hydro development are very busy. In resources, the fall in commodity prices is causing some difficulty but the province is not negatively affected as much as other provinces more closely tied to the sector.

Manufacturing is benefiting from U.S. growth; trade in the province is typically north-south, so the renewed momentum in the U.S. economy provides nothing but good news for firms in this sector.

The increase in trade has also been particularly beneficial for the transportation industry, especially trucking. Those companies have definitely picked up momentum with more activity, more sales, higher profits and investments in fleet expansion. The synergy with the uptick in manufacturing has a clear benefit for trucking; we're no longer seeing empty trucks head down to the U.S. after dropping of their American-sourced hauls.

Winnipeg is also a good transportation hub for the entire country; this has been of particular benefit for food service companies who send their products to the rest of Canada. We're also noting corresponding benefits for the cold storage industry in the city.

Agriculture remains solid in Manitoba. We have seen a bit of a slowdown in land values and equipment purchases, but customers in the sector are comfortable with that; they accept the cyclical nature their business.

Taken together, the news we are hearing from our customers is positive and optimism is high. We look forward to the year ahead to see just how strong business performance will be.

Ontario

ECONOMICS

Robert Kavcic,
Senior Economist

Ontario's economy is poised to outperform in 2015, with growth expected to top the national average for the first time in 13 years. Real GDP will likely expand 2.5% this year versus 1.8% nationally, helped by firm U.S. demand, the lagged impact of a weaker currency, low oil prices and a solid housing market. Indeed, if not for a stiff dose of fiscal restraint, it might be as good as it gets in Ontario this year.

The combination of stronger U.S. demand, a weaker loonie and lower oil prices plays right into the hands of **exports and manufacturing**, an area of the economy that has lagged so far this cycle. Exports were up strong 13% y/y in the latest three months, led by autos and machinery & equipment. However, longer-term issues remain, as relatively high labour costs continue to pose challenges for the auto sector versus Mexico and the Southern U.S. High electricity rates are another challenge, with average prices paid by large consumers in the Toronto area well above those in competing cities such as Montreal, Winnipeg, Chicago and Detroit.

The **housing market** continues to perform well around much of the province, led by strong conditions in Toronto, where resale prices are pushing record levels. Housing starts are settling in at, or slightly below, levels required to satisfy demographic demand, though the condo market could be tested as the near-record 56,000 units recently under construction are now reaching completion. The detached market, however, remains starved for supply and is well-supported by demographic fundamentals. Ontario's **labour market** remains disappointing, with employment up a modest 0.6% y/y in Q1. But, job growth in smaller cities around the Greater Toronto Area has been encouraging—this includes the likes of Barrie, Hamilton and Guelph. Improved transit to these areas is also a long-run positive. The jobless rate sat at 6.9% in March, a tick above the national average—we suspect it will soon dip below the Canadian rate for the first time in nine years.

The Province of Ontario is projecting an **$8.5 billion deficit** in FY15/16, or 1.1% of GDP, versus $10.9 billion now expected for FY14/15. That still leaves the province near the high end of the provincial deficit table, but it reverses two straight years of widening shortfalls. The Province continues to target FY17/18 for a balanced budget, and cumulative deficits between FY14/15 and FY17/18 are now $2.5 billion lower than projected a year ago, including a $1.6 billion positive revision to FY14/15. This year's budget built in tight program spending assumptions through 2018—flat nominal spending growth, or declines of 2.5%-to-3% per year in real per-capita terms. While the deficit is tracking lower this fiscal year, net debt will continue to rise as a share of GDP, reaching a record 39.8%, though that is slightly lower than previously expected. Asset sales of $5.7 billion over 10 years were the centrepiece of this year's budget, and all eyes are now on Moody's and S&P to see if they will act on their negative rating outlooks.

Eastern Ontario

COMMERCIAL BANKING

Sandra Henderson,
Senior Vice President,
Eastern Ontario Division,
BMO Bank of Montreal

Victor Pellegrino,
Regional Vice President,
Commercial Banking,
Eastern Ontario Division,
BMO Bank of Montreal

Throughout Eastern Ontario, we are seeing good momentum across the businesses we support.

In agriculture—where BMO still has leading market share among the major banks, we see a number of customers maintaining the trend of consolidation in the past couple of years. A number of farms are looking to grow their businesses through acquisition, and the low interest rate environment is helping them do it.

The higher U.S. dollar may cause some difficulties, however, although the impact depends on the particular crop. Also, the full effects haven't been felt since much of the change in value happened over the winter; with farms starting to buy feed and other materials, we should start to be able to gauge the impact of the high U.S. dollar shortly. The fall in commodity prices are also a concern, but again with the season just starting any impacts are just anecdotal at this stage.

On the manufacturing side, many traditional manufacturers have left or closed following the impact of the recession. However, we're starting to see a comeback in niche, specialized fields—particularly in knowledge-based industries. Ottawa remains a hub for such companies, and we're starting to see a revival in that space from the depths of 2000. This is good news for the National Capital Region, with such firms looking to court a high-skilled labour force. Ottawa may also benefit from this being an election year, with government layoffs highly unlikely.

Meanwhile, larger plants throughout the region, such as for Ontario Hydro and General Motors, remain stable (aside from the previously-announced relocation of Camaro production). While there's no robust growth, we aren't seeing signs of a slowdown either.

Commercial construction is seeing some growth, particularly in Ottawa. The city has an underdeveloped condominium market and has been playing catchup compared to the rest of the country. The momentum is slowing a bit of late, and new home prices are settling as a result. We are also curious to see if the recent transit infrastructure efforts in Ottawa will lead to ancillary benefits. We haven't seen them yet, but we look forward to that changing once the Confederation Line opens.

Western Ontario

COMMERCIAL BANKING

Curtis Scragg,
Senior Vice President,
Southwestern Ontario Division,
BMO Bank of Montreal

Rick Jaques,
Regional Vice President,
Commercial Banking,
Southwestern Ontario,
BMO Bank of Montreal

David Blyth,
Regional Vice President,
Commercial Banking,
Southwestern Ontario,
BMO Bank of Montreal

Southwestern Ontario businesses are beginning to feel more optimism the further we get from the recession. The benefits of U.S. growth, cheaper fuel and low interest rates are starting to become apparent.

That said, there appears to be somewhat of a lag in the change of environment. We expect to see our commercial customers' financial statements continue to improve, but the real benefits should be seen over the next 12 to 18 months.

As many observers have noted, manufacturing in the region was hit hard during the recession and when the dollar was high. We expect that those companies that closed or relocated to lower-cost jurisdictions like China or Mexico will not be coming back. But among those who stayed, benefits of the friendlier environment will continue to support their bottom lines.

Among those companies, the increase in business activity is corresponding with a need to make capital expenditures to modernize processes or acquire additional equipment; the low interest rate environment will continue to support those actions. That said, these firms remain cautious; while new equipment may be adding to capacity, they are waiting before making significantly larger investments in new jobs.

As well, with the period of lower interest rates getting longer, some companies are choosing to wait to take advantage of the situation; they don't feel any pressure to act now. While we understand the need for caution, we don't expect this period of low rates to last too much longer and we encourage our customers to take advantage to support productivity improvements.

Another benefit for manufacturing is strong growth in the transportation sector, particularly in trucking. With lower fuel costs and more U.S. demand for Canadian products, we can expect to see continued improvement in this area.

Meanwhile, knowledge-based industries in the Kitchener-Waterloo-Cambridge areas are showing strength once again. BMO has been excited to see the launch of a number of startups in this space, led by young and dynamic CEOs.

Agriculture, as always, continues to play a leading role in Southwestern Ontario's economy and remains the largest sector in our commercial lending book. Here too, we are seeing caution, mainly as a result of lower commodity prices. But the sector remains strong, as it benefits from lower fuel costs and the low dollar.

The Greater Toronto Area

COMMERCIAL BANKING

Andrew Auerbach,
Senior Vice President,
GTA,
BMO Bank of Montreal

Doug Palmer,
Regional Vice President,
Commercial Banking,
GTA Central,
BMO Bank of Montreal

Sheri Griffiths,
Regional Vice President,
Commerical Banking,
GTA North,
BMO Bank of Montreal

The Greater Toronto Area remains one of the most vibrant places to do business in all of Canada. As the largest centre in the country, businesses here will always benefit from a strong labour pool—people continue to come here and the local economy benefits. The proximity to large companies and key educational institutions ensures that Toronto's businesses will remain strong and competitive.

At the same time, these factors contribute to a robust housing market and good construction activity on both the residential and non-residential sides.

Major projects, such as the Pan Am Games, transit expansion like the Eglinton Crosstown and the extension of the subway, continue to provide construction firms and workers with jobs and opportunity. The focus in the recent provincial budget on infrastructure spending should lead to more of the same, which will almost certainly offset any issues created by reduced government spending in other areas.

On the manufacturing side, the benefits of the weaker Canadian dollar, the emerging strength of the U.S. economy and lower energy prices are beginning to become apparent. While those manufacturers that had had to close or chose to move during the recession are almost certainly not coming back, the ones that remain will benefit from these factors.

We are also seeing the emergence of a good number of niche manufacturers who are capitalizing on new market opportunities. These manufacturers concentrate on providing high value-add. As an example, we are seeing food processors who are focusing on providing products that suit the shift in consumer preferences for locally grown foods.

In services, the city continues to do well in financial series and knowledge-based industries. Growth can be seen both with existing firms and in business formation.

The GTA will remain one of the most important business hubs in the country, and the future continues to look bright.

Quebec

ECONOMICS

Robert Kavcic,
Senior Economist

Quebec's economy is poised to pick up on the back of a stronger U.S. economy and improved business confidence. Real GDP will likely grow 2.1% this year, up from a 1.4% clip in 2014. Looking ahead, growth should hold at 2.0% in 2016 as net exports benefit from stronger sales to the U.S. and the impact of past weakness in the Canadian dollar. The political and fiscal landscape has also stabilized, which should support business confidence and investment.

Exports and business investment have been a drag on growth, but momentum appears to be turning positive. Net export volumes improved for a second straight year in 2014, and the value of exports was up a strong 18% y/y in the latest three months, led by aerospace, machinery and electrical equipment. Meantime, business investment was weak through the second half of 2014 amid ongoing declines in nonresidential construction, but the outlook is better with the political backdrop now stable and government finances much improved.

The **housing market** remains subdued, including that in Montreal where home sales over the latest twelve months were near the lowest in twelve years. Across the province, there is more than a year worth of resale supply on the market, and average prices are little-changed over the past two years. With the soft demand backdrop, housing starts have settled in near 12-year lows (even lower than during the recession in 2008/09). The **labour market** performance has also been weak, but is showing tentative signs of improved momentum. Employment was up 0.6% y/y in Q1, and the jobless rate sat at 7.5% in March, down from above 8% last summer.

The Province of Quebec is projecting a **balanced budget** in FY15/16, ending a run of six straight years in the red. Before transfers to the Generations Fund (for debt reduction), the surplus comes in at $1.6 billion, also the first positive balance since 2008. Notably, net debt is now poised to edge down as a share of GDP after topping 50% in FY14/15, and is expected to fall to 44.5% by FY18/19. After a meaningful dose of combined restraint in last year's budget and fall fiscal update (tax-related measures totaling nearly $1 billion, plus other measures such as a hiring freeze and higher daycare fees), this year's budget keeps a lid on spending growth, but serves up some tax relief.

While the relief is minimal this fiscal year, it will gradually rise to more than $1 billion by FY2019/20. Measures include a gradual elimination of the health contribution tax starting in 2017, a reduction in corporate tax rates from 11.9% to 11.5% by 2020 and lower small business taxes. Additional, more elaborate, changes to the tax system are also likely coming in the year ahead. These tax relief measures aimed further down the road are a clever signal to markets and businesses that Quebec's **financial momentum** is turning for the better.

COMMERCIAL BANKING

Mario Rigante,
Senior Vice President,
Quebec Division,
BMO Bank of Montreal

Quebec businesses are beginning to benefit from the rebound in the central Canadian economy. With the dollar lower as well, we're seeing more firms engaged in projects to expand their businesses and reach.

To be sure, caution remains; many of our commercial customers were affected negatively by the recession and they are reticent to do too much. But optimism is clearly emerging.

Transportation is one area where we are seeing a strong resurgence, thanks to lower fuel costs and more goods to send to the U.S. The benefits are being seen in the trucking industry in particular, but also with companies who are involved in transportation logistics such as ports. Growth in transport can be seen as a leading indicator; typically, stronger company performance in these areas translates into benefits for ancillary businesses. We are on the lookout to see those benefits emerge in the coming months.

The improving strength of the U.S. economy will support a number of our manufacturing customers as they receive new and larger orders. We've seen customers in plastics, electrical components and pharmaceuticals benefit from this renewed U.S. growth, and we expect to see other companies benefit as well.

With the return of the Liberals to government last year, the Plan Nord economic development strategy to develop natural resources in northern Quebec has been re-instituted. As the project continues to develop, we hope to see a number of companies benefit. In particular, we expect Montreal to see growth in the necessary ancillary services to support Plan Nord, such as consulting and professional services.

The health sector also has the potential for strong growth, particularly with the construction of two new super-hospitals in Montreal. We can expect to see specialized clinics and health services moving close to those facilities, which is good news for both real estate and professional services.

New Brunswick

ECONOMICS

Robert Kavcic,
Senior Economist

Economic growth remains weak in New Brunswick, and while the province will continue to lag most of the pack, momentum should improve somewhat in the year ahead. Real GDP is expected to grow 1.1% this year after effectively no growth over the prior four years. Exports should get a boost from a weaker loonie, but the fiscal environment is among the most challenging in Canada.

After providing a strong buffer during the recession, a retrenchment in **capital spending** in both the public and private sectors was a key reason for soft growth in recent years. However, StatsCan's survey of public and private investment intentions pointed to a modest 2.1% increase in 2014—not great, but a marked improvement from the double-digit declines seen in each of the prior two years. This year's provincial budget pegged capital spending at $597 million, up 8% from FY14/15, though none reflects new projects until FY16/17. Transportation infrastructure, which absorbs the bulk of the ongoing capital budget, will see a 5.7% boost.

Challenges remain in the manufacturing sector, though the potash sector has improved. **Potash output** is poised to rise as the Piccadilly mine is set to commence production eight years after being announced, while the global price backdrop has stabilized after a tough few years. **Forestry exports** should also get a boost from the U.S. housing recovery, with housing starts south of the border now consistently topping the 1 million annualized mark. That said, non-energy exports were well below year-ago levels in the three months through February. Overall **labour market** trends remain weak, with employment down 0.9% y/y in Q1. In fact, employment has been grinding steadily lower over the past six years. At the same time, the unemployment rate continues to drift higher, sitting at 10.1% in March, among the highest in Canada. Demographics remain a major concern, as the province continues to see net outward migration and an ageing population left behind.

The Province of New Brunswick is projecting a **$477 million deficit** in FY15/16, or a meaty 1.4% of GDP, in the first budget under the recently-elected majority Liberal government. The shortfall is wider than the $255 million expected for FY14/15, but the prior-year figure was flattered by some one-time transfers from Ottawa, while the current year now builds in a $150 million contingency reserve meant to absorb downside revenue surprises. Eliminating these two special factors would leave the deficit roughly steady on a year-over-year basis. Looking ahead, the Province has not outlined a medium-term fiscal plan (the election campaign pegged FY17/18 for a balanced budget), and the Strategic Program Review, which will be ongoing through the year, will likely lead to a tough budget in FY16/17. This year's document keeps a grip on spending, while introducing a few lower-tier revenue measures—a bigger move, such as an HST increase, is potentially still on the table for next year.

COMMERCIAL BANKING

Carolyn Booth,
Senior Vice President,
Atlantic Provinces Division,
BMO Bank of Montreal

Leigh Winchester,
Regional Vice President,
New Brunswick West Market,
Atlantic Provinces Division,
BMO Bank of Montreal

Positive news for New Brunswick companies is beginning to emerge, with several good stories to tell.

As usual, forestry leads the way as the key sector for the province. With the low Canadian dollar, the stronger U.S. economy and a corresponding demand for more home construction south of the border, the forestry industry is likely to see a marked improvement. New Brunswick has long been a large net exporter of wood products and construction materials to the U.S., so prospects for these companies are bright.

These benefits also spill over to small manufacturing, which in New Brunswick often has a relationship with the forestry sector. The positives for makers of windows and doors, for instance, are similar to those seen for the sector as a whole.

The opening of a new potash mine in Sussex Region, combined with existing production and rising global demand, should bring significant income into the province in the years ahead—again benefiting from the low Canadian dollar.

Agriculture continues to benefit from efforts by local farms to modernize their operations. The dairy industry, where technology and automation have led to reduced costs and business expansion, leads the way and provides a positive example for producers across New Brunswick. The fishery is also looking positive, with the lower dollar and increased foreign demand—particularly from Asia—keeping prospects high.

We also note the ongoing discussions across Canada regarding the proposed Energy East pipeline. While discussions on this exciting opportunity are expected to continue for some time, the province's political and business leaders will no doubt do their utmost to sell the rest of the country on this idea.

We do note the growth of knowledge-based industries to the province, which are attracting much-needed foreign investment to the region. As well, New Brunswick may benefit from the pending federal election if it receives a share of government funds for infrastructure projects; these have the potential to create jobs in the interim.

There is no single silver bullet that will solve New Brunswick's traditional challenges of muted growth, and aging population and outward migration. But the signs are good with renewed optimism in several sectors and the prospect of more New Brunswickers returning to the province from Western Canada because of the drop in oil and gas prices. We look forward to the possibility of several positive years for New Brunswick companies.

Nova Scotia

ECONOMICS

Robert Kavcic,
Senior Economist

Economic momentum should improve in Nova Scotia this year, with real GDP expected to grow 1.9%, up from a 1.6% pace in 2014. That would be tops in Atlantic Canada, and leave growth above the national average for the first time since the recession. Stronger U.S. demand and the massive shipbuilding contract will support growth in the near term, but longer-term challenges remain.

Irving Shipbuilding's $25 billion contract to build combat ships for the Royal Canadian Navy through 2030 will provide support with production expected to begin later this year. **Exports** also stand to improve further in the year ahead, after production from the Deep Panuke natural gas project boosted shipments early in 2014. Non-energy exports are holding above year-ago levels, with auto parts up nearly 10% y/y in the latest three months. Additionally, **offshore exploration** activity is picking up, with BP/Shell set to spend roughly $2 billion in the coming years.

There are downsides in the province as well, and the **demographic drain** is among the largest. Nova Scotia's population has faded since peaking in mid-2011, though growth has again turned modestly positive recently. One factor is a turnaround in interprovincial migration flows, largely to Alberta, alongside the slide in oil prices—we suspect outward migration could cease altogether in 2015. Longer term, however, demographics will be a persistent headwind pulling trend economic growth down to just above 1%. The **labour market** continues to underperform, with employment little changed from a year-ago in Q1. The unemployment rate has held relatively steady at around 9%, but that largely reflects a steep decline in the participation rate in recent years. For the most part, this reflects an ageing Nova Scotia population, as the prime-age part rate has recovered smartly in the past year. With challenging demographics, the **housing market**, particularly in Halifax, remains soft. In the latest 12 months, existing home sales in the city hit the lowest in 16 years.

The Province of Nova Scotia is projecting a **$97.6 million deficit** in FY15/16 (a modest 0.2% of GDP), down from the $102 million shortfall now expected for FY14/15. The Province is targeting a small surplus by FY16/17, one year earlier than previously estimated, and a year ahead of the timelines in Ontario and (presumably) New Brunswick. If this target is met, net debt will continue to gradually fall as a share of GDP after peaking at 37.7% FY13/14—it is pegged at 36.3% in FY15/16. This year's budget came with a dose of spending restraint and only a few new revenue measures (netting out to just a $16 million increase for FY15/16). But, more meaningful taxation reform could be coming in the year ahead. The recently-published Nova Scotia Tax and Regulatory Review (November, 2014) made 22 recommendations for tax changes and 20 for regulation. The main message was that consumption taxes should increase (including a broadening of the tax base), while income taxes should be simplified and reduced.

COMMERCIAL BANKING

Carolyn Booth,
Senior Vice President,
Atlantic Provinces Division,
BMO Bank of Montreal

The business outlook in Nova Scotia is full of green sprouts with economic growth forecasted at levels that the province has not experienced in recent times. Our commercial customers feel that the tide is turning in their favour.

Irving Shipbuilding has made progress on the $25 billion contract to supply Canada's next generation of warships. With contracts in place and facility upgrades nearly done, the start of construction of the first vessels is imminent.

The housing market can still be classified as a buyer's market as demand remains soft. The resale market is performing slightly better than new home construction sales. Despite softness in the market, prices have shown modest growth. These trends are expected to persist and home builders are proceeding cautiously.

Construction firms are generally in a solid position. Construction of the Nova Centre, the largest integrated development project in the province's history, has been a particular boon for local firms.

The fall in the price of oil and gas represents both opportunity and challenge. Reduced demand for labour in Western Canada has led many Nova Scotians to return home. This has provided relief to a labour market which has long experienced a shortage of skilled workers. Conversely, many Nova Scotians earn their living in Western Canada and some of these families are likely to be affected.

Despite lower energy prices, both BP and Shell have indicated that they intend to continue with their multi-billion dollar explorations of Nova Scotia's offshore. Companies throughout the energy supply chain have the opportunity to make strategic investments, so they will be well positioned to capitalize when energy prices trend upwards.

With respect to agriculture, we are beginning to see success among commercial customers in niche industries. One example would be Nova Scotia wineries which, with emerging reputations for excellent quality product, are well positioned to benefit from a strong U.S. economy.

The outlook for the fishery in 2015 is outstanding. Nova Scotia lobster exports should yield significant economic benefits as both harvesters and processors are poised to benefit from increased demand from the US, Europe and Asia.

Again, the low dollar, strong economic growth in the United States and proximity to the American North East should benefit the province's manufacturing sector.

Companies that invest in equipment upgrades and process improvements will set themselves for longer-term success; with Nova Scotia's economic prospects as strong as has been seen in many years, now is the perfect time for businesses to make strategic investments.

Prince Edward Island

ECONOMICS

Robert Kavcic,
Senior Economist

The **PEI economy continues to grow at a moderate pace**, with real GDP expected to accelerate slightly to 1.6% this year from a 1.3% pace in 2014. Firmer U.S. economic growth and a weaker Canadian dollar will help offset ongoing public-sector restraint and more normal agricultural output this year.

Exports are expanding at a strong clip, up 11% y/y in the three months through September, led by gains in machinery and electrical equipment, as well as a healthy level of farm, fish and food product shipments. With U.S. demand expected to remain firm and the Canadian dollar weaker, trade and tourism could be a positive for the province in 2015. This follows a year in which visitor traffic was down roughly 14% y/y in 2014, despite the 150-year anniversary celebrations of the Charlottetown Conference, which set the stage for Confederation.

Public-sector restraint is likely to remain a drag on growth in the year ahead. On the capital spending side, StatsCan's survey showed public-sector capex down a steep 25% in 2014, but the decline should level off this year with the Province's capital budget roughly flat year-over-year. On the operating spending side, the Province is maintaining a tight grip on spending growth.

Meantime, **population growth**, while regaining some momentum in recent quarters, has slowed significantly from the torrid pace (by PEI's standards) seen earlier in the recovery. International immigration has cooled, while net interprovincial migration remains a major drag, with roughly 1,000 people leaving per year currently. Still, despite the slowdown, population growth (0.7% y/y in Q1) is running well ahead of its Atlantic Canada peers, which are in outright decline.

The **labour market** remains challenged, with employment flat-lining over the past two years. Public-sector employment declines were the culprit through 2013 and early 2014, but private-sector employment has taken a nasty spill more recently. As a result, the unemployment rate has turned higher, sitting at 11.0% in March, the second highest in Canada.

The Province of Prince Edward Island has yet to table a FY15/16 budget given a May 4th provincial **election**—results are pending as we go to print. The most recent FY14/15 fiscal update (released in March) pegged the deficit at $34.7 million, a $5 million improvement over the budget plan. Net debt is also on track to fall for a second straight year as a share of GDP in FY14/15, sitting at 36.1%.

COMMERCIAL BANKING

Carolyn Booth,
Senior Vice President,
Atlantic Provinces Division,
BMO Bank of Montreal

Prince Edward Island continues to reap the benefits of the modernization of its economy, with benefits that will support growth for years to come. Recent growth has been positive to the point that the provincial government is expecting to run a surplus in the coming year—always a good sign.

For a small province, Prince Edward Island features a very diversified manufacturing sector—much more so than the rest of Atlantic Canada. When we look at the businesses that have had major recent success, we look to aerospace, pharmaceuticals, biosciences and chemicals. All of these niche opportunities will benefit from the growing strength of the U.S. economy and the lower Canadian dollar.

Of course, Prince Edward Island will always be known for the fishery, tourism and agriculture—all of which stand to gain in the current economic conditions. In the fishery, for example, those companies that made an effort to improve their productivity in more challenging years are reaping the rewards. The low dollar, combined with increased demand from both a resurgent United States and countries in Europe, will help boost income for local producers. More demand from Asia will also help this trend, and our customers are looking forward to more success.

Companies in the tourism industry are anticipating a banner year. Prince Edward Island has long been a top tourist destination, but the low dollar will make a trip to the province even more attractive—for foreign tourists and Canadians alike.

On the agriculture side, a number of our customers are benefiting from the same sorts of investment we described for the fishery. For those who have made the effort, technological innovation continues to reduce costs and increase yields. Again, with the benefit of the low dollar and strong U.S. economy, the outlook is very bright for Prince Edward Island farmers.

The positive news remains tempered with relatively high unemployment, but the bright outlook represents an opportunity for companies in the province to continue the good momentum. The consolidation of Prince Edward Island's traditional strengths, along with continued diversification, will undoubtedly lead to greater economic success.

Newfoundland & Labrador


ECONOMICS
Robert Kavcic,
Senior Economist

Newfoundland & Labrador is struggling amid the slide in oil prices and fading near-term production. Real GDP is expected to contract 1.0% this year—the weakest performance in Canada—and fall a further 1.5% in 2016 as oil production declines. Longer term prospects are more encouraging, however, based on our forecast for WTI oil returning toward $70 by the end of 2016, which should support continued development of the offshore sector.

Newfoundland & Labrador's **oil sector** makes up roughly 22% of provincial GDP and more than 7% of employment—both shares are just slightly smaller than in Alberta. As a result, the slide in oil prices is expected to hit incomes hard in province. Production also continues to drift down after peaking in 2007, at least until the pipeline is filled with new output, such as Hebron in late-2017. Also, an extension of White Rose is in the engineering and design phase (oil production also expected to increase in late-2017) and a major discovery by Statoil in the Flemish Pass Basin could hold 300-to-600 million barrels of light oil. In the meantime, oil production slipped 5.7% y/y in 2014.

Other underlying economic trends in the province have been weakening. **Employment** fell for a second straight year in 2014, and was down a steep 2.3% y/y in Q1. That left the unemployment rate at the highest level in the country at 13.3% in March. Public-sector job cuts have been the major culprit, with employment down 18% from its early-2013 high—education, health care and public administration have all fallen significantly. With the sluggish labour market and confidence plagued by lower oil prices, **retail sales** momentum had faded (sales slowed to 1.5% y/y in the latest three months, versus a rate of more than 4% y/y before oil prices plunged), while average home prices are now down from a year ago.

The Province of Newfoundland and Labrador is projecting a **$1.1 billion deficit** (a hefty 3.3% of GDP) in FY15/16 as the slide in oil prices has taken a major chunk out of royalty revenues. The FY14/15 shortfall is now pegged at $924 million, or $386 million deeper than estimated a year ago. Looking ahead, the province is projecting deficits out to FY19/20, when the budget returns to balance alongside a steady increase in Brent crude prices to $90 by 2020, from $62 this fiscal year. While program spending will rise this year, the Province is taking some measures to raise revenues, including a 2 ppt increase in the HST and higher tax rates on personal incomes above $125,000. Total net revenue measures will amount to $122 million in FY15/16 (almost 0.4% of GDP), rising to $225 annually in later years. The Province will tap capital markets again this year, borrowing $2 billion in FY15/16. As a result, net debt is expected to rise $1.3 billion to $11.5 billion by the end of FY15/16, or 35% of GDP—that is still well down from about 70% in the late 1990s, but up nearly 10 ppts in just three years.

COMMERCIAL BANKING

Carolyn Booth,
Senior Vice President,
Atlantic Provinces Division,
BMO Bank of Montreal

Jim Fallon,
Regional Vice President,
Eastern Newfoundland
& Labrador,
Atlantic Provinces Division,
BMO Bank of Montreal

The best news coming from our Newfoundland & Labrador customers is in the fisheries sector. We're seeing a good number of companies doing well, and the lower Canadian dollar is clearly helping with exports to the United States and elsewhere. Shellfish (mainly shrimp and crab) have recorded a strong year. With no significant changes in quotas forecast for 2015 and prices remaining at 2014 levels, we expect another positive year.

The province is still being negatively affected by the combined impact of low oil prices and falling commodity prices—particularly iron ore. As an example of the effects, last year we anticipated that the $1.3 billion Alderon Kami Iron Ore project in Western Labrador might proceed; with lower commodity prices the benefits of this and other mining projects become less clear. Even with lower prices, nickel production in Voisey's Bay and processing in Long Harbour continues to support the local economy in those parts of the province.

The direct impact on employment levels at the three producing oil fields is expected to be minimal. Hibernia, White Rose and Terra Nova produce at a low marginal cost and remain viable. The development of the Hebron Gravity base structure and the Muskrat Falls Hydro project continue. It remains to be seen the impact continued low oil prices will have on future exploration and development.

It's clear that the provincial deficit, which relies heavily on royalties from oil and commodities, will rise significantly. The near and medium term effects for the provinces workforce—given that a third of the working population works for the government in some fashion—could be significant. This may lead to a drop in consumer spending and a continued decline in housing starts.

One interesting element of the fall in oil and gas prices will be the effects on Newfoundland & Labrador workers who have been travelling to Alberta. With so many of them bringing wealth back to the province over the past few years, any layoffs may cause problems in rural communities. On the other hand, their return may help alleviate the current local shortage of skilled labour for ongoing mega projects like Hebron and Muskrat Falls. We will have to see how this nets out before we get a real understanding of the wider impact on commercial customers and the wider economy.

Understandably, people and businesses in Newfoundland & Labrador are showing a great deal of caution—at least in comparison to the previous five years. It remains to be seen if the oil and commodity price drop has long-lasting effects.

Provincial Economic Summary

	BC	Alberta	Sask.	Manitoba	Ontario	Quebec	NB	NS	PEI	NL	Canada
Real GDP Growth (chain-weighted : year/year % change)											
2014 [1]	2.6	4.4	1.4	1.1	2.3	1.4	0.0	1.6	1.3	-2.9	2.5
2015 f	2.6	0.4	1.0	2.3	2.5	2.1	1.1	1.9	1.6	-1.0	1.8
2016 f	2.5	1.9	2.0	2.2	2.4	2.0	1.3	1.7	1.5	-1.5	2.2
Employment Growth (year/year % change)											
2014	0.6	2.2	1.0	0.1	0.8	-0.1	-0.2	-1.1	-0.4	-1.9	0.6
2015 f	0.7	0.6	-0.7	1.7	0.6	1.1	0.1	0.2	0.2	-1.4	0.6
2016 f	1.3	0.3	0.3	0.9	1.2	1.1	0.2	0.5	0.3	-0.4	1.0
Unemployment Rate (percent)											
2014	6.1	4.7	3.8	5.4	7.2	7.8	9.9	8.9	10.5	12.0	6.9
2015 f	5.8	5.7	4.9	5.6	6.8	7.4	10.2	8.8	10.4	12.8	6.8
2016 f	5.5	5.8	5.0	5.3	6.5	7.1	10.1	8.7	10.2	13.3	6.6
Housing Starts (thousands)											
2014	28.3	40.5	8.2	6.2	58.3	38.9	2.3	3.1	0.5	2.2	188.6
2015 f	29.0	37.0	6.1	5.8	57.5	34.3	2.0	3.0	0.5	2.0	177.6
2016 f	28.4	32.0	6.5	5.7	59.0	40.0	2.3	3.7	0.5	2.2	180.3
Consumer Prices (year/year % change)											
2014	1.0	2.6	2.4	1.8	2.3	1.4	1.5	1.7	1.6	1.9	1.9
2015 f	1.4	1.0	1.3	1.5	1.4	1.2	1.1	1.0	0.7	0.8	1.3
2016 f	2.2	2.0	2.0	2.3	2.2	2.0	1.9	2.3	1.7	1.9	2.1

[1] 2014 provincial GDP by industry   f = forecast