



# TD Economics

## Special Report

April 27, 2006

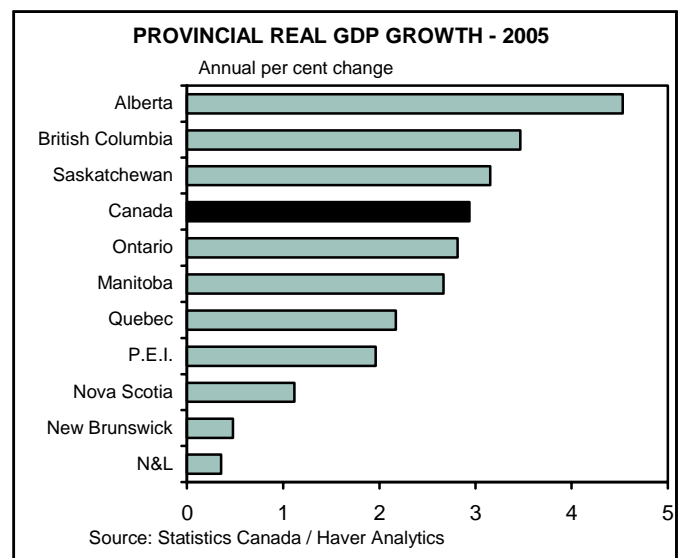
### LIVING STANDARDS GROW FASTER IN THE WEST IN 2005

The annual provincial economic accounts were released on Wednesday by Statistics Canada, confirming that the Western provinces remained on top of the leaderboard for a third consecutive year in 2005, while Central Canada experienced moderate gains and Atlantic Canada trailed at the bottom of the pack.

#### Western economies in the fast lane in 2005

Real GDP growth figures – which captures growth in production and strips away the distortionary impact of general price increases – revealed that energy-rich Alberta posted the strongest economic performance in 2005, growing at 4.5 per cent. Alberta's neighbours, British Columbia and Saskatchewan, ranked in second and third place, respectively, with solid gains above the 3-per-cent mark. Economic growth elsewhere in the country was below the national average of 2.9 per cent. Ontario's real GDP expanded at a respectable pace of 2.8 per cent, despite having its key manufacturing sector hit by sky-high energy prices and a strong loonie. Meanwhile, Quebec posted more modest, but still respectable growth of 2.2 per cent. The Atlantic region struggled the most in 2005 with real output advancing at a mere 0.8 per cent. Notably, Newfoundland & Labrador's economy edged up 0.4 per cent due to temporary production problems in oil fields.

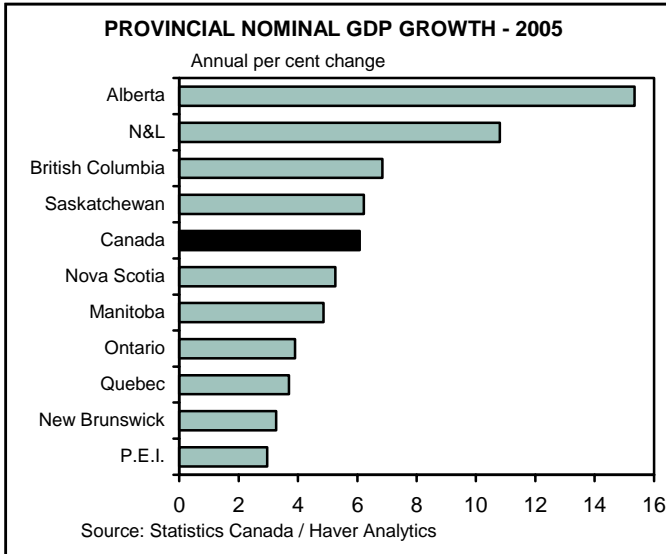
While it is conventional to look at inflation-adjusted GDP, this measure alone does not capture the full extent of the West's outperformance. This is because real GDP removes the positive impact of last year's run-up in commodity prices on corporate profits, wages and governments revenues. So, it is worthwhile to look at nominal GDP, which is a measure of overall income. Following double-digit increases in 2003 in 2004, Alberta's nominal GDP soared by 15.3 per cent in 2005, representing three to four



times the growth seen in most of Central and Atlantic Canada (see chart on next page). Nominal GDP in the other energy-entoured provinces of Newfoundland & Labrador, Saskatchewan and British Columbia advanced at a pace of 6.0 per cent or more. In Central Canada, nominal GDP rose by a modest pace of 3.7 per cent and 3.9 per cent in Quebec and Ontario, respectively.

#### Wide divergence in standards of living in 2005

However, there is more to the story than just growth. The fact that regional economies expanded at different speeds raises the question of how the provinces stacked up in terms economic well-being. To address this matter, we present three measures of standards of living in the accompanying tables: Income per person (Nominal GDP per capita); after-inflation output per person (real GDP per capita); and after-tax, after-inflation personal income (real personal disposable income per capita).



First, income per person reveals a clear-cut disparity from coast to coast. As shown on the adjacent chart, each Albertan had on average \$66,397 in 2005 – 156 per cent of the Canadian average of \$42,464 – an increase of 13.5 per cent from a year earlier. Ontarians ranked second at \$42,993 with a gain of 2.8 per cent from last year. Saskatchewan’s nominal GDP per person (\$42,743) was a notch higher than for Canada as a whole. Residents living in all other seven provinces had an income below the national average. Notably, P.E.I.’s reading of \$30,015 was half that in Alberta. The bottom line is that Albertans were better off in 2005, both in terms of the level and the rate of growth in income.

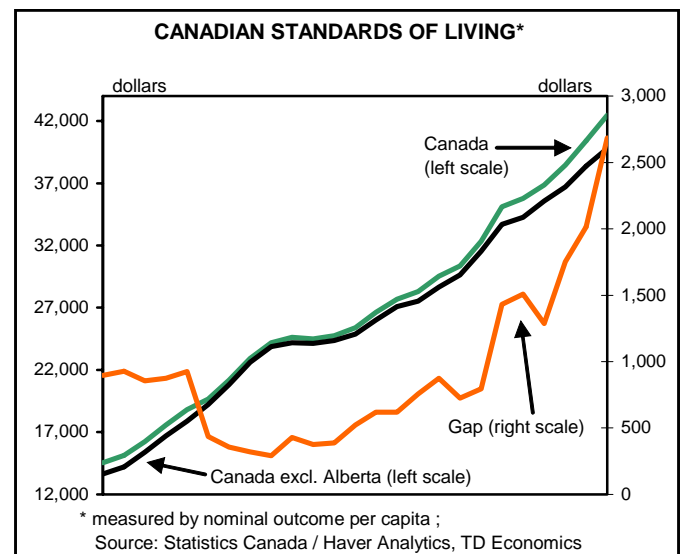
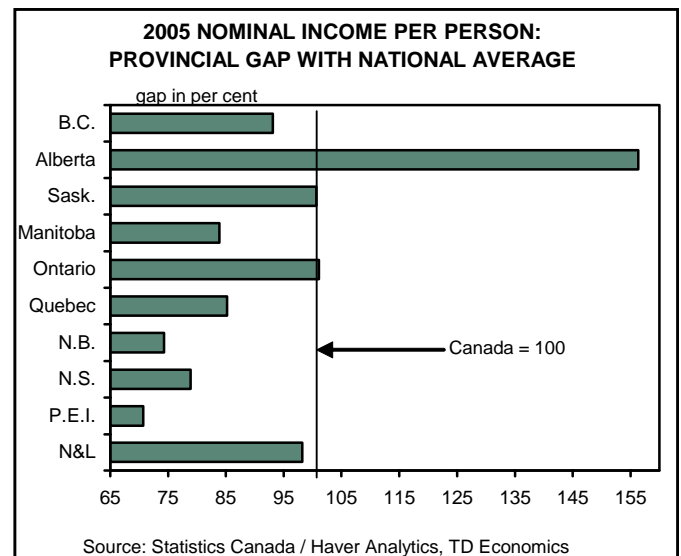
**Some provinces are catching up**

It is more interesting to put the 2005 figures in a historical context and find out which provinces are catching up over the long haul and which ones are not. The first key observation is that income per capita in 6 out of the 10 provinces has moved towards the national average since 1985 on an income per capita basis (see table). Another finding is that provinces do not catch up at the same speed or at the same time. For example, the average income of Canadians living in Nova Scotia, New Brunswick and Prince Edward Island increased faster than the national average during the 1980s. In contrast, income per person in Newfoundland & Labrador improved mostly since 2000, thanks in part to a booming oil sector. Saskatchewan is the only province that saw income per capita move up above the national average in the last 20 years. Relative to Canada, Ontario’s advantage in income per person was thinner in 2005 than in 1985.

In contrast to these six jurisdictions, residents living in the four other provinces have not seen income move towards the Canadian average in the last two decades. The gap has remained the same in Quebec and widened in Manitoba. Income per person in British Columbia is well below Canada’s average today after being well above in the early 1980s. Lastly, Alberta stretched its lead meaningfully in the last 10 years.

**Strong income growth in Alberta pulls up Canada**

One reason sometimes cited to explain the slow catch-up in some provinces is that they cannot keep up the pace with the energy-rich and low-tax jurisdiction of Alberta. For example, Albertans saw their income increasing fast, from 122 to 156 per cent above the national average between 1995 and 2005 alone. This blockbuster improve-



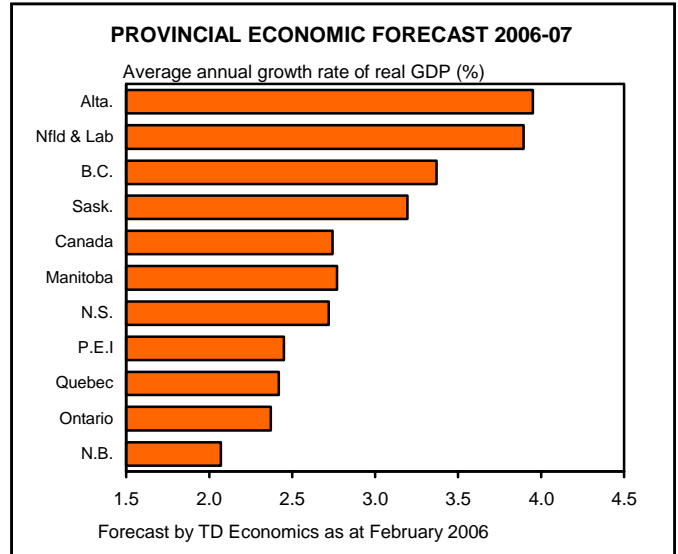
ment pushed up Canada's income per person. By stripping away Alberta, the average income of Canadians is much lower. In 2005, the average income per capita in Canada was \$42,464, but stood at \$39,780 for Canada excluding Alberta, a difference of \$2,685 (see chart on previous page). All provinces have narrowed the gap in income per person relative to Canada – excluding Alberta – during the 1995-2005 period.

Admittedly, the run-up in commodity prices is also part of the story behind recent gains in income per person. Inflation-adjusted output per capita – which keeps the general price level constant – reveals two main points: First, the same 6 provinces are catching up to the national average. Second, the provincial disparity on a real GDP per person basis is not as sizeable. For example, Alberta's inflation-adjusted output per person is at 122 per cent of the Canadian average in 2005, compared to 156 per cent for income per person.

**After inflation, after-tax income more homogenous**

GDP per capita is the most commonly used measure to capture economic well-being, but has some caveats. For energy-based provinces like Newfoundland & Labrador and Alberta, sky-high energy prices may provide a kick to corporate profits or provincial coffers, but may also fail to improve the economic well-being of residents to the same extent. To see how Canadians really benefit from a growing economy, it is worthwhile to look at inflation-adjusted, after-tax income available per person.

In a nutshell, this measure reveals good news for Canadians. Real after-tax income per resident was closer to

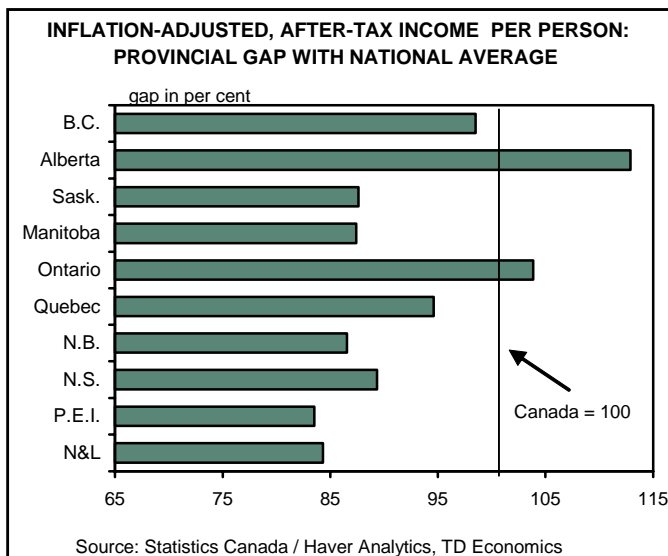


the national average in 2005 than on a real output per capita basis in all provinces except Saskatchewan, where the real after-tax income per person gap with Canada was 88 per cent in 2005 compared to 96 per cent for real output per capita (see table). And, even if Albertans' lead on a real after-tax income basis is smaller than on a real GDP basis, the gap with Canada was larger than ever in 2005 (113 per cent).

**The bottom line**

No matter how we slice it, the level of economic well-being of Canadians varies from coast to coast. Factors that could explain such disparities include economic structure, productivity gains, tax burden, labour market performances, and fiscal policies (such as the Equalization Program). On that front, the Expert Panel on Equalization, established a year ago to review the equalization formula, is expected to submit its recommendations to the federal government this spring. Meanwhile, economic growth will continue to influence the future course of standards of living. As noted in our *Provincial Economic Update* report, the gap in regional growth performances is expected to remain largely intact in 2006 and then narrow in 2007, as commodity prices – which have given the west the edge since 2003 – retreat to some extent.

*Sébastien Lavoie, Economist*  
416-944-5730



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PROVINCIAL REAL GROSS DOMESTIC PRODUCT (GDP)					
Annual average per cent change					
	2002	2003	2004	2005	81-05
<b>CANADA</b>	3.1	2.0	2.9	2.9	2.8
<b>N. &amp; L.</b>	16.4	6.2	-1.4	0.4	2.6
<b>P.E.I.</b>	5.8	1.5	1.8	2.0	2.6
<b>N.S.</b>	4.2	0.9	1.4	1.1	2.4
<b>N.B.</b>	4.4	1.7	2.0	0.5	2.5
<b>Quebec</b>	2.7	2.1	2.3	2.2	2.1
<b>Ontario</b>	3.2	1.6	2.7	2.8	3.0
<b>Manitoba</b>	1.9	1.8	2.3	2.7	2.0
<b>Sask.</b>	-0.2	3.8	3.4	3.2	2.1
<b>Alberta</b>	2.5	3.1	4.3	4.5	3.1
<b>B.C.</b>	3.5	2.7	4.0	3.5	2.5

Source: Statistics Canada / Haver Analytics

PROVINCIAL NOMINAL GROSS DOMESTIC PRODUCT (GDP)					
Annual average per cent change					
	2002	2003	2004	2005	81-05
<b>CANADA</b>	4.2	5.4	6.1	6.1	5.7
<b>N. &amp; L.</b>	16.4	10.2	7.2	10.8	6.1
<b>P.E.I.</b>	8.3	3.5	4.6	3.0	5.8
<b>N.S.</b>	4.5	6.0	4.1	5.3	5.9
<b>N.B.</b>	2.3	4.9	3.6	3.3	5.6
<b>Quebec</b>	4.5	4.3	5.0	3.7	5.3
<b>Ontario</b>	5.4	3.2	4.9	3.9	6.1
<b>Manitoba</b>	4.2	2.9	6.0	4.9	4.8
<b>Sask.</b>	3.6	6.0	9.9	6.2	4.5
<b>Alberta</b>	-0.3	13.5	9.3	15.3	6.0
<b>B.C.</b>	3.5	5.6	7.7	6.8	5.7

Source: Statistics Canada / Haver Analytics

PROVINCIAL STANDARDS OF LIVING (\$ dollars)												
	NOMINAL GDP PER CAPITA				REAL GDP PER CAPITA (cst \$1997)				REAL PDI PER CAPITA (cst \$1992)			
	1985	1995	2000	2005	1985	1995	2000	2005	1985	1995	2000	2005
<b>CANADA</b>	18,816	27,695	35,124	42,464	25,725	28,482	33,294	35,909	16,690	17,039	18,379	18,947
<b>N. &amp; L.</b>	11,481	18,752	26,313	41,707	15,433	19,211	23,289	29,637	10,777	13,674	14,586	15,976
<b>P.E.I.</b>	11,322	19,807	24,674	30,015	16,235	20,149	22,805	24,863	12,658	14,856	15,876	15,823
<b>N.S.</b>	14,008	20,785	26,390	33,529	19,466	20,908	24,584	27,241	14,229	15,372	16,431	16,934
<b>N.B.</b>	12,958	21,813	26,761	31,548	18,255	22,016	25,238	27,878	13,030	15,080	16,218	16,396
<b>Quebec</b>	16,123	24,575	30,588	36,201	22,838	25,053	29,296	31,547	15,149	16,019	17,106	17,929
<b>Ontario</b>	20,374	30,126	37,803	42,933	29,183	31,111	36,803	38,592	18,470	18,357	19,922	19,678
<b>Manitoba</b>	17,137	23,912	29,705	35,634	23,671	24,676	28,649	30,655	16,467	15,686	16,329	16,562
<b>Sask.</b>	17,501	26,074	33,537	42,743	21,669	26,907	30,983	34,416	14,888	14,604	15,451	16,599
<b>Alberta</b>	27,828	33,711	48,315	66,397	30,777	35,994	40,428	43,676	18,093	17,467	19,268	21,390
<b>B.C.</b>	18,019	28,060	32,532	39,556	27,329	28,731	30,999	33,909	16,755	17,006	17,910	18,663

Source: Statistics Canada / Haver Analytics

STANDARDS OF LIVING - DIFFERENCE FROM CANADIAN AVERAGE (in per cent)												
	NOMINAL GDP PER CAPITA				REAL GDP PER CAPITA				REAL PDI PER CAPITA			
	1985	1995	2000	2005	1985	1995	2000	2005	1985	1995	2000	2005
<b>CANADA</b>	100	100	100	100	100	100	100	100	100	100	100	100
<b>N. &amp; L.</b>	61	68	75	98	60	67	70	83	65	80	79	84
<b>P.E.I.</b>	60	72	70	71	63	71	68	69	76	87	86	84
<b>N.S.</b>	74	75	75	79	76	73	74	76	85	90	89	89
<b>N.B.</b>	69	79	76	74	71	77	76	78	78	89	88	87
<b>Quebec</b>	86	89	87	85	89	88	88	88	91	94	93	95
<b>Ontario</b>	108	109	108	101	113	109	111	107	111	108	108	104
<b>Manitoba</b>	91	86	85	84	92	87	86	85	99	92	89	87
<b>Sask.</b>	93	94	95	101	84	94	93	96	89	86	84	88
<b>Alberta</b>	148	122	138	156	120	126	121	122	108	103	105	113
<b>B.C.</b>	96	101	93	93	106	101	93	94	100	100	97	99

Source: Statistics Canada / Haver Analytics