BMO Blue Book

October 2017

BMO 200 Financial Group

We're here to help.™

Canada

ECONOMICS

Robert Kavcic,
Senior Economist

Sunny Skies

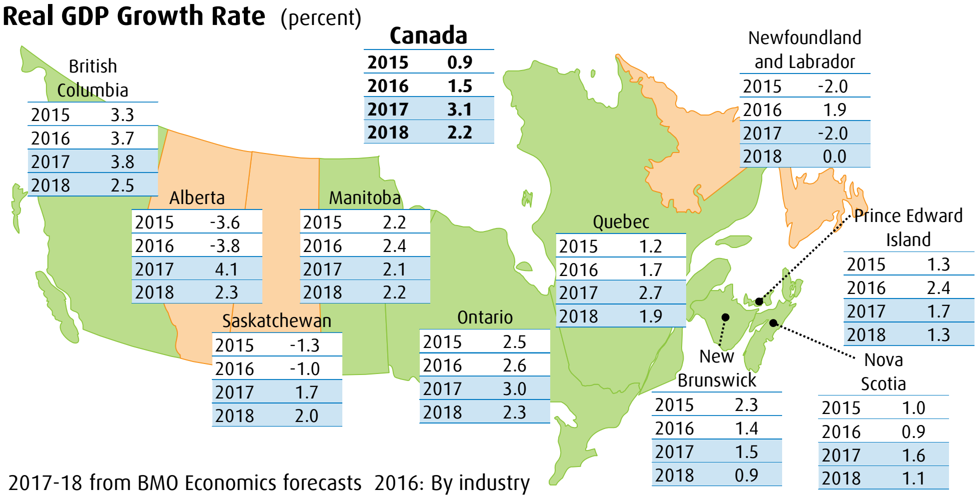
Canada's economy is on pace to match the best annual growth performance since the financial crisis, with real GDP likely to expand 3.1% this year, up from 1.5% in 2016. Consumer spending remains solid, while the worst of the capital spending retrenchment in energy is behind us and fiscal stimulus will add support. That said, peak growth is likely past, with the economy expected to moderate to a 2.2% pace in 2018 as most provinces see growth step down. The big story at the regional level is a narrowing gap between the best and worst performers, as the recession fades in oil-producing provinces, while British Columbia and Central Canada should moderate after a few years of blistering growth.

British Columbia is expected to post a fourth consecutive year with growth in excess of 3% in 2017, as demographic and consumer spending trends are strong, while housing activity has picked up again. **Ontario** is expected to expand 3.0%, with sturdy U.S. demand and improved population growth helping, even as housing moderates in the wake of recent policy changes. Indeed, external economic conditions in Canada's largest province are about as good as they can possibly get right now. **Quebec** should accelerate for a second consecutive year, with growth expected at 2.7%, as the labour market in the province continues to perform well—the jobless rate recently hit a record low of 5.8%, and is now trending consistently below the national average.

Alberta's economy has returned to growth, and could potentially lead the country this year at 4.1%. But, part of the GDP strength reflects a bounce-back from a negative wildfire impact last year. Underlying growth is likely to settle into the 2%-to-2.5% range by 2018, consistent with neutral oil prices and a much softer environment than enjoyed over the past 15 years. **Saskatchewan** is expected to return to modest 1.7% growth this year, while **Newfoundland & Labrador** GDP will get dragged down by a number of major capital spending projects reaching

Provincial GDP

Real GDP Growth Rate (percent)



2017-18 from BMO Economics forecasts 2016: By industry completion. **Manitoba** maintains a very consistent growth trend of just above 2%.

Momentum has improved somewhat across most of Atlantic Canada, with **New Brunswick** expected to see 1.5% growth this year, still subdued as fiscal restraint weighs. More favourable fiscal backdrops in **Nova Scotia** and **Prince Edward Island** should allow growth in those provinces to clock in closer to 2%, but longer-term demographic headwinds continue to weigh on the region, even as population growth, consumer spending and residential construction see a near-term boost.

COMMERCIAL BANKING

Andrew Irvine,
Head of Canadian Commercial Banking, BMO Bank of Montreal

Across Canada, we see fantastic opportunities for BMO's business banking customers. With the economy showing good strength, the optimism we see from them is encouraging. Even in areas where the economic situation is a challenge, firms are doing what it takes to succeed.

When I look across the country, one area of particular excitement lies in the growth of innovation. Whether it's the creation of information technology superclusters in major centres, to focused modernization and efficiencies in traditional sectors such as agriculture and the fishery, innovation is transforming the outlook for businesses from coast to coast.

We strongly encourage the continuation of this trend. Innovation will position our companies well, whether it's for competing in global markets or maintaining economic viability during a downturn. With interest rates set to rise but still historically low, now may well be an excellent time to invest in innovative efficiencies for many firms.

Throughout the provinces, we see signs of success or progress for our business customers. B.C. is enjoying the strength of its economy, while Western Canada is beginning to recover from the downturn in energy prices. Ontario continues to benefit from a strong service sector and the vibrancy of new entrepreneurs. Quebec's economy is showing exciting strength, and firms are taking advantage.

Atlantic Canada has challenges, especially in export industries—such as forestry and the fishery—as a result of a relatively higher dollar. But firms are modernizing where they can and showing great resilience.

The ongoing NAFTA renegotiations do represent an area of concern for businesses, such as exporters with a focus on the United States, manufacturers in North America-wide supply chains and supply-managed agriculture producers. Along with our business customers, we look forward to the certainty that a final agreement will bring. We will provide assistance to all of them in the event the trade landscape changes significantly.

BMO is here to help our customers. Small and medium-sized businesses are a fundamental component for Canada's economic architecture; we encourage them to come see us to ensure they have the right strategy for the times. As always, we have a full array of services to help businesses become and stay successful, and we have a highly-skilled team of commercial bankers situated in communities across Canada. Our bankers stand ready to advise business owners on strategic spending and investment decisions that will help them boost productivity and expand into new markets, both at home and abroad.

British Columbia

ECONOMICS

Robert Kavcic,
Senior Economist

Economic growth in British Columbia is **on pace for a very strong 3.8% print** this year, which would mark the fourth straight year above the 3% mark. The labour market and consumer spending trends are driving growth, while housing activity has picked up again.

The **Vancouver housing market** has shaken off prior cooling measures (i.e., 15% tax on non-resident buyers), and continues to post sales and price gains. Benchmark prices were up 10.9% y/y as of September, and even prices in the higher-end detached market are above pre-tax levels. Housing starts are running near the strongest level of the past 30 years, with strength in the multi-unit segment.

The **labour market** is strong, with employment growth leading all provinces, and the jobless rate nearing a decade low below 5%. That is drawing in increased **migration** from other Canadian provinces, adding to a steady stream of international inflows for more than 50,000 in total in the 12 months through June.

Non-energy **mining investment** has downshifted notably, and continues a multi-year period of retrenchment. Development in the LNG sector remains in flux with Petronas officially cancelling its planned Pacific Northwest LNG project.

The Province of British Columbia's new government released an **updated fiscal plan**, including higher top personal income, corporate and carbon tax rates, offset partly by lower Medical Service Plan premiums. The Province is now projecting a $246 million surplus this fiscal year, down from the $2.7 billion in FY16/17.

COMMERCIAL BANKING

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

The B.C. economy continues to outpace provincial peers and reflects the optimism our customers have in local markets. BMO's Business Banking customers continue to invest and grow their businesses with availability of capital and investment return considered strong throughout the province.

Emerging momentum in provincial knowledge based industries is evident and represents both business opportunity and a further diversification play for our economy, aided in part by a competitive Canadian dollar which is having a broad based effect on many BC based businesses.

Agriculture, as always, continues to play a leading role in British Columbia's economy. While caution remains a theme in the industry, the sector remains strong as it benefits from stable fuel costs and the low dollar. We continue to watch North American NAFTA discussions with interest, including the treatment of supply managed operations.

The continuing trend of strong economic growth by our Aboriginal clients throughout the province with investments in a wide variety of infrastructure, partnerships and diversification provide further support to our economy with growth potential continuing to create local jobs and improve the quality of life in Aboriginal communities. Aboriginal communities continue to represent an ever increasing important sector as they strategically deploy capital that supports economic independence.

One burgeoning area of growth is our provincial health care industry. With a demographic shift flowing from an aging population, combined with net migration, we believe this industry sector is poised for growth. Opportunities exist in both private and government funded seniors care facilities, combined with contributions from the non-profit sector. We expect to see additional health care segments supporting growth through pharmacies, medical imaging and professional services. These health care professionals require investment with the establishment of practices, the acquisition of equipment and the purchase of premises; this activity will lead to significant growth in the industry in the coming years.

Tourism will continue to 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.

The BC wildfires from earlier in the year have had a material impact on businesses connected to natural resources and tourism. BMO has proactively engaged affected customers to ensure we meet the increased banking needs and are providing the appropriate long term solutions.

Alberta

ECONOMICS

Robert Kavcic,
Senior Economist

Alberta's economy has returned to growth, and could potentially lead the country this year at 4.1%. But, part of the GDP strength reflects a bounce-back from a negative wildfire impact last year. Underlying growth is likely to settle into the 2.0%-to-2.5% range by 2018, consistent with neutral oil prices and a much softer environment than enjoyed over the past 15 years.

The **energy sector** directly accounts for roughly 26% of Alberta GDP, 6% of employment and almost two-thirds of private non-housing capital spending. Our forecast for relatively stable oil prices around current levels suggests ongoing maintenance of existing projects, but not a lot of new capital investment.

The **housing market** is stabilizing after a prolonged correction that saw benchmark prices in Calgary fall 6% from peak levels. Housing starts have found a footing, though well down from pre-shock levels. **Commercial real estate**, however, remains awash in supply with vacancy rates topping 27% in Calgary's downtown office segment, and cap rates are rising accordingly.

The **labour market** has stabilized, though employment remains below 2015 levels and the jobless rate is lingering around the 8% level—that is above the national average for the first time in 27 years. The province is seeing net **interprovincial outflows** as relative economic prospects have improved in other regions.

The **Province of Alberta is projecting a $10.5 billion deficit** for FY17/18 (3.2% of GDP). That is slightly narrower than the $10.8 billion shortfall in FY16/17—that was the largest on record, and near the early-90s nadir as a share of GDP.

COMMERCIAL BANKING

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

Given the ongoing concerns with the price of oil, it's no surprise that our customers remain cautious. We won't be seeing robust activity levels until we see stability—and then growth—in energy prices.

That said, it's important to note that oil and gas companies have done a significant amount of work over the past two years to cut their basic cost structures so that they can extract for lower prices. That effort has included the increased use of technology and automation—for instance, the advent of self-driving vehicles. As a result, the heydays of heady employment numbers are likely not to return, as the number of actual employees needed—even with strong prices—will be lower. Nevertheless, this situation will still lead to stability and growth, which will certainly be an improvement over the previous several years. The worst is definitely behind us.

Signs of stability have emerged in other parts of the economy as well. In housing, for instance, prices did go down but didn't drop precipitously. As well, BMO's mortgage business didn't have a particularly large number of borrowers underwater—it just wasn't a serious problem. This represents a confirmation that the bottom of the cycle in Alberta wasn't a complete collapse—people did feel difficulties, but they were able to keep their houses.

Compared to two years ago, we are also beginning to see more of a buzz and the emergence of cautious confidence in in the commercial sector, which is much like a canary in the coalmine for the economy. Companies are borrowing to invest in their operations and are slowly hiring more staff, and we are seeing improvements in their balance sheets.

In the always-important agriculture sector, we've seen a good year. The summer was spectacular, if a bit dry. We can expect a good harvest at reasonable prices. We're also starting to see agriculture producers move toward more value-added activities, such as expanded dairy operations and more food processing. All of this represents good news for the overall economy.

In short, we are optimistic about a steady return to moderate growth. Given the past few years, this represents positive news for all concerned.

Saskatchewan

ECONOMICS

Robert Kavcic,
Senior Economist

Saskatchewan's economy remains subdued, as the effect of the oil price downturn lingers. Real GDP is expected to advance a moderate 1.7% this year, underperforming the national average, but that will mark a turnaround after two consecutive years of negative growth.

The **oil sector** has been retrenching, with the Province expecting relatively stable production over the near term. **Potash** production is rising at a steady clip but prices are depressed and capital investment in new capacity is now declining. **Crop production** was challenged by dry weather this year, with wheat output expected to be down roughly 30% from last year.

The **labour market** remains challenged, with employment little-changed from four years ago. That has lifted the jobless rate above 6% for the first time since the late-1990s. **Population growth** remains elevated at 1.3% y/y, but has softened over the past three years—the province is again losing migrants to other regions.

For the **housing market**, the slowdown in employment and population growth comes at a time when a glut of new supply from the prior boom is still getting absorbed.

The **Province of Saskatchewan is projecting a $685 million deficit** on a summary basis for FY17/18, or a chunky 0.8% of GDP, unchanged from the budget plan. But, the Province chipped away at half of its contingency reserve, which now sits at $135 million. The still-heavy dose of capital spending, combined with the budget shortfall, will drive a significant $2.7 billion **borrowing requirement** this fiscal year.

COMMERCIAL BANKING

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

Michael Beal,
Vice President, Business Banking, Regina and SW Saskatchewan, BMO Bank of Montreal

Marcia Lemon,
Vice President, Business Banking, Northern Saskatchewan, BMO Bank of Montreal

After several soft years, business in Saskatchewan is starting to see some positive momentum.

In the always-important agricultural sector, we've seen a fairly stable year for most producers. While the weather created very dry growing conditions in some locations, crop yields have met projections nonetheless. In fact, leftover moisture from several wet years benefited pockets of farmers in areas around the province—with some producers yielding above-average production.

Meanwhile, land prices continue to rise. This trend is not as dramatic as we've seen in the past, but values continue to trend upwards.

Farmers are also showing a desire to diversify; quinoa, soybeans, corn and hemp are being included in crop rotations. We see this as the start of a possible trend which aligns with the growth in knowledge-based industries related to agriculture; this has the potential to benefit production in the coming years.

On the manufacturing side—which is often dependent on agriculture—we are starting to see businesses looking to invest in opportunities outside of both the province and Canada. After a pullback of export activity, several manufacturers of farm equipment are looking to reengage exporting activities inter-provincially, in addition to the U.S. and parts of Europe. The high dollar may be a hindrance, but the trend is encouraging.

In the southern part of the province, the oil & gas industry has recently started to come back with renewed activity. Companies are advertising and looking to hire qualified workers in the area. Businesses either directly involved in oil & gas or providing related services are feeling cautiously optimistic.

Businesses are also seeing renewed growth in Regina and Saskatoon. Homebuilders are now reporting that there is a pickup in starts after a few years of lower demand. We're also seeing renewed interest in franchise start-ups, primarily in services such as restaurants.

One issue affecting our customers has been the question of how to manage their finances in an environment of potential rising interest rates. We encourage them to come in and speak to us to devise an effective strategy. This doesn't necessarily mean locking in right away—it means having a plan, making informed decisions and taking advantage of rates which are still historically low.

Manitoba

ECONOMICS

Robert Kavcic,
Senior Economist

Manitoba continues to grow at a steady pace, with real GDP expected to rise 2.1% this year, down somewhat from 2016. Manitoba is benefiting from low energy-sector exposure, a diverse manufacturing base and a sturdy service sector.

Agriculture output faced tougher conditions through 2017, even as it was spared the worst of the drought. Wheat production is tracking 14% lower this year, while canola is modestly lower as well. **Manufacturing** has had a solid run since 2010, and should continue to benefit from the lagged impact of a weaker Canadian dollar and still-solid U.S. demand. While the early cyclical rebound faded after the oil shock, momentum has improved in recent quarters. The transportation sector has been especially strong.

Labour market momentum is improving, with employment up 1.2% y/y in Q2. It's very likely that the stagnation from 2014 through 2016 was more a function of the deep decline in Alberta's job market. The jobless has also begun to fall sharply, now sitting at 4.9% after reaching a twenty-year high of 6.5% at one point last year.

Housing market activity should remain stable, with sales and price growth both modest, supported by solid population growth and favourable affordability.

The **Province of Manitoba is projecting an $840 million summary budget deficit** in FY17/18, slightly larger than the $764 million reported for FY16/17. That weighs in at 1.2% of GDP, the largest shortfall outside of Alberta and Newfoundland & Labrador this fiscal year.

COMMERCIAL BANKING

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

Manitoba's businesses continue to benefit from the steady economic environment that has characterized the province for many years. We simply don't see the kind of discussions that other jurisdictions experience about boom and bust.

That said, we see many signs of great news. From the perspective of business activity among our customers, we haven't seen such growth since 1967. The last four-to-five years have seen a change in confidence, leading to investments in projects—particularly in Winnipeg.

We have also seen a number of our customers—particularly on the manufacturing/automotive side—starting to invest in beachheads in the United States. They recognize this process will be slow and difficult, but it's encouraging to see Manitoba businesses put their toes in the water in this way.

At the same time, our customers in commercial building feel a certain level of uncertainty. For instance, the higher dollar is putting new pressure on businesses that rely on exports. The issue is not a major one as of the moment, but businesses are keeping an eye on the situation.

Meanwhile, companies that tend to focus on projects related to infrastructure and hospitals are watching for the support they might get from the various levels of government; currently, such support is uncertain. As well, developers based in Winnipeg are preparing for the impact of a municipal levy for the first time.

Irrespective of how the various levels of government choose to proceed on these matters, our business customers are looking for certainty. If this can be achieved quickly, Manitoba businesses will be able to proceed with their activities with confidence.

Outside Winnipeg, the agricultural sector's situation is best described as mixed. Some customers are going well, while others—particularly in the southeast where there has been some flooding during the year—are experiencing more troubles. As a whole, the performance of the agricultural sector this year has been below average.

We've also observed that farmers are in a wait-and-see mode with making more investments to their own operations. This, in turn, has had an impact on the verticals that feed the industry, such as companies that supply farm equipment. With farms holding back somewhat, the income for these supporting companies has softened.

The good news remains Manitoba's economic stability; by and large, our customers are feeling reasonably positive for the months and years ahead.

Ontario

ECONOMICS

Robert Kavcic,
Senior Economist

Ontario's economy remains one of Canada's growth leaders, expected to post 3.0% growth this year, the fastest pace since 2010. The acceleration that began in 2014 is noteworthy, and reverses a decade of prior underperformance. Real GDP is expected to moderate to 2.3% by 2018, still an above-potential pace for Ontario.

Export volumes have risen strongly this cycle, but have recently seen momentum ebb. Longer-term issues remain for the sector, as relatively high labour costs continue to pose challenges versus Mexico and the Southern U.S. And, Ontario is one of the provinces most exposed to **NAFTA**. While **manufacturing** output rebounded strongly earlier in the recovery, growth has softened in the past two years as firms have filled up production capacity, but have been shy to deploy new capital.

The **housing market** is enduring a correction in the wake of provincial policy measures (April 2017) that included a 15% tax on non-resident buyers. While benchmark prices continue to dip, especially for detached homes (down roughly 10% through September), indications suggest the market is gradually balancing. Underlying supply-demand conditions remain very favourable.

The **labour market** is strong, with employment growth among the strongest in Canada—most has been concentrated in the Greater Toronto Area. The jobless rate is now trending below the national rate for the first time since 2006, and the province is drawing in a record 175,000 migrants/year from outside Canada and other provinces.

The **Province of Ontario is projecting a balanced budget in FY17/18**, ending a nine-year run of red ink. That follows a small $1 billion shortfall in FY16/17.

Eastern Ontario

COMMERCIAL BANKING

Victor Pellegrino,
Senior Vice President,
Eastern Ontario Division,
BMO Bank of Montreal

Eastern Ontario is open for business.

Throughout the region, we see positive sentiment and growing confidence from our commercial customers, along with a general improvement in employment. There has been a clear change for the better in their outlook; a year ago, we noted more cautious optimism—but that has been cast aside. We are seeing more activity and more requests for lending.

In Ottawa, we are seeing a renaissance to coincide with Canada 150. The new Confederation Line is nearly complete—five years between approval and operation is a remarkable achievement. With the line entering service next year, we expect to see new businesses popping up along its route.

This momentum can be seen in other areas as well. For instance, we are seeing the development of major condominium complexes of up to 50 stories. As well, the relocation of the Department of National Defence to the old Nortel building in Kanata will lead, over the course of two years, to the relocation of 10,000 people—this represents an opportunity for housing development and business investment in the western part of Ottawa.

We are also seeing an uptick in activity in key centres throughout the rest of Eastern Ontario, including Durham, Peterborough and Kingston. In the far west of the area, the expansion of Highway 407 is leading to new business demand along that corridor. As well, the cheaper affordability index of Durham compared to Toronto is bringing new residents and new business.

Across Eastern Ontario, agriculture remains a strong part of the economy. Our customers in the sector are contemplating growth and expansion—something we encourage with interest rates still on the low side. Recent hesitation and prudence has diminished.

That said, the ongoing NAFTA negotiations have implications for a wide variety of businesses, particularly in agriculture and exports. Those customers feel a certain degree of nervousness given the position of the U.S. negotiators; they are looking forward to the certainty that a final agreement will bring.

Regardless, positive sentiment is great to see in Eastern Ontario. We look forward to strong business activity in the months ahead.

Southwestern Ontario

COMMERCIAL BANKING

Julie Barker-Merz,
Senior Vice President,
Southwestern Ontario Division,
BMO Bank of Montreal

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

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

The diverse economy of Southwestern Ontario provides a mixed picture, with a number of different considerations affecting our business banking customers.

In several centres across the region, including Kitchener-Waterloo and London, the technology sector continues to show impressive strength. We are also starting to hear more about the use of advanced manufacturing practices and artificial intelligence expanding to other industries.

As all these elements come together, the results in the coming years will bear watching, particularly with a proposed advanced manufacturing supercluster—running from the Greater Toronto Area to Kitchener-Waterloo-Cambridge—being supported by local boards of trade. Optimism in this space is significant, with exceptional possibilities for businesses in the region.

Firms that support infrastructure development have a bright future, with several major projects—such as the new Gordie Howe International Bridge in Windsor—currently under construction.

Among manufacturers, any customers with a connection to the United States are closely looking at the NAFTA renegotiations. Several companies in this sector have integrated supply chains—particularly in the auto sector—which might be affected by changes to trade rules. But the sector in general is showing good performance; the companies that stayed in business during and after the recession are doing well and looking to expand through acquisition or grow with new equipment. With borrowing costs still reasonably low but interest rate hikes on the horizons, now may be a good time for such firms to proceed.

On the construction side, residential builders are benefiting from the growing number of people moving into the region—from Toronto, for instance—to take advantage of lower housing and cost of living prices. Our developer customers are active and busy throughout Southwestern Ontario—particularly in the major centres—as a result. This activity includes new condominiums in London and Kitchener-Waterloo-Cambridge, bringing excellent work opportunities.

In agriculture, the wet spring caused some stress at the beginning of the growing season. The good news is, in the end, the problems from weather ended up simply pushing crops back by a couple of weeks instead. That said, a number of BMO's agriculture customers are contemplating the implications on their operations of climate trends.

The greenhouse segment in Essex and Kent counties has been expanding significantly in recent years, although some producers in centres like Leamington are experiencing challenges related to the price of hydro and access to natural gas.

The Greater Toronto Area

COMMERCIAL BANKING

Steve Murphy,
Senior Vice President,
GTA,
BMO Bank of Montreal

The excitement and strength that the Greater Toronto Area's economy has shown over the past few years continues—its impact on national and provincial growth remains impressive.

We continue to see a lot of start-up activity on the part of new Canadians. These newcomers often have a very entrepreneurial outlook and see the self-employment as the best way of making a new start in a new home. We see this growth throughout the region, but in the western suburbs in particular. These new arrivals open businesses in a wide variety of industries, which in turn serves to further diversify the regional economy.

The City of Toronto's traditional strengths in services continue. Growth in that sector is leading to more major new building activity, with office towers in the south part of the downtown core rising and filling. Toronto continues to hold the role as Canada's foremost business hub, with all the ancillary services that go along with it.

The building of transportation infrastructure to support the GTA's ongoing growth continues; the TTC's new subway extension into Vaughan will open in December 2017, while the construction of the Eglinton Crosstown remains on schedule for completion in 2021. Construction firms working on transit expansion will benefit for several more years at least, with possible new opportunities on the horizon—particularly if a proposed "Union Station West" near Pearson International Airport is built.

Manufacturing continues to show strength, although the higher Canadian dollar and uncertainty related to NAFTA negotiations provide uncertainty for firms with a major export component.

One area of particular interest is the technology sector, where more start-up firms appear on a regular basis. With incubators like the DMZ at Ryerson University providing the impetus and support for new entrepreneurs in the technology space, we can see a bright future for technology firms. The region's reputation as an international hub for technology—the largest in Canada and third largest in North America—continues to grow, and will only increase with the arrival of more entrepreneurs.

One area that bears watching is residential construction. The GTA continues to attract people and businesses from across Canada and around the world, but new mortgage borrowing rules and the potential for higher interest rates in the coming months and years may reduce the demand for new homes. Construction firms will watch coming trends with interest.

Quebec

ECONOMICS

Robert Kavcic,
Senior Economist

Quebec is posting one of the best economic performances, both in absolute and relative terms, in 15 years. Real GDP is on pace to grow 2.7% this year, up from 1.7% in 2016 and a 1.3% average in the four years prior to that. Growth should moderate to 1.9% next year, but remain strong by recent standards.

Export momentum has faded in recent quarters alongside a stronger loonie, but **business investment** has started to improve after a multi-year lull. Confidence is being helped by a stable political backdrop and improved government finances.

The **labour market** performance has been impressive, with Quebec posting some of the best job growth in Canada and the jobless rate falling below the national average for the first time outside the financial crisis—it hit a record low 5.8% in July. Demographic headwinds continue to weigh on Quebec's economy, but population growth has picked up in recent quarters, though it remains well below Ontario and Western Canada.

The **Montreal housing market** is seeing momentum improve after a multi-year period of stagnation. Benchmark prices have clearly broken out to the upside, and are now running at 4.7% y/y pace—that's the best in six years.

The **Province of Quebec's fiscal situation has improved dramatically**, with a $2.5 billion surplus pegged for FY17/18 before transfers to the Generations Fund. With an election looming in 2018, further moves to lower the tax burden are likely.

COMMERCIAL BANKING

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

Quebec businesses, along with the economy, have turned the corner—improvement is everywhere, with customers feeling very positive.

We do still see some caution among business owners, however. When we look at real dollar investments, such as for new equipment to improve productivity, we are seeing a bit of a lag. There's a sense that these firms do have ideas and plans, but are hesitating on execution. Given the slower economy over the past few years and the uncertainty over the NAFTA negotiations, this restraint is understandable.

But all signs point to growth in sectors throughout Quebec. With interest rates still reasonably low, prices still good and opportunities growing, now is a good time to proceed.

In the major cities of Montreal and Quebec City, we're seeing a buzz with renewed strength in both employment and growth. The recent increases in infrastructure spending represent a significant part of that—we're seeing construction everywhere, and many firms are set to benefit both now and in the coming years.

As we noted last year, Montreal continues to see more strength in the area of information technology. Diversification of economic growth in major centres represents a strong opportunity for Quebec, and we are encouraged to see this trend continue.

We also note the entrance of more start-ups into the marketplace, benefiting from the support of government organizations like Startup Canada. In Quebec, there's never been a better time to start a business—and BMO is here to help.

In the health care sector, businesses are set for strong growth. The expansion of medical-related professional services that we observed last year—particularly in Montreal given the new McGill University Health Centre—continues. We can expect to see even more growth in this important segment in the coming months.

In agriculture, we're seeing a lot of strong growth among producers. Business owners remain optimistic—even in the face of possible difficulties flowing from the NAFTA negotiations. Dairy farmers, in particular, do not appear to be concerned. Whether that confidence is warranted remains to be seen, but the positive sentiment is fantastic to see.

On the resource side, we continue to wait to see how Plan Nord will move forward. The potential for this major project remains impressive and has the potential to benefit a significant number of businesses.

In short, excitement is building for Quebec businesses; we look forward to see what they will achieve in the coming year.

New Brunswick

ECONOMICS

Robert Kavcic,
Senior Economist

Economic growth has picked up in New Brunswick, but remains relatively subdued. Real GDP is expected to expand 1.5% this year, up slightly from 1.4% in 2016. Growth is then expected to cool to below 1% next year as demographic headwinds weigh on potential growth.

Capital spending has retrenched recently as some major projects have wound down in the forestry and refining sectors. Challenges also persist in the potash sector. **Forestry exports**, however, are getting a boost from the U.S. housing expansion, though a trade dispute over softwood lumber remains a shadow.

Labour market trends remain weak, with employment unchanged from where it stood four years ago, and private-sector employment is at the same level it was 12 years ago. Interestingly, the unemployment rate plunged to just 6.5% in July (a record low), but that came alongside a big decline in the labour force. The jobless rate has since begun to move higher again.

Demographics remain a major challenge, as the province continues to see net outward migration and an aging population left behind. However, population growth has turned positive in recent quarters after four years of outright decline, spurred by a jump in international immigration.

The **Province of New Brunswick remains in a challenging fiscal position**, with the budget deficit tracking $156 million this fiscal year, and net debt on the rise.

COMMERCIAL BANKING

Justin Scully,
Regional Vice President,
Commercial Banking,
Atlantic Provinces Division,
BMO Bank of Montreal

New Brunswick's businesses continue to deal with softer growth compared to the rest of the country. Several sectors provide solid opportunities for success, but new challenges will be on the minds of our Business Banking customers.

Exports represent a key opportunity for the province's business banking customers, in a wide variety of sectors. The possibilities coming from the newly-announced Atlantic Trade Strategy, an initiative of all the Atlantic provinces and the federal government with the goal of doubling the number exporters in the region by 2025, have the potential to be a significant boon to the private sector.

This initiative will benefit from New Brunswick's strength as a hub for transportation, with several major transport firms having corporate headquarters in the Province.

On the agriculture side, we continue to see transfers of ownership to the next generation of farmers. Success here will be dependent on farms' abilities to harness new technology to improve efficiency in their operations. Interest rates remain historically low but will likely be on the rise in the coming months; agriculture producers may want to consider making investments now to take advantage and ensure their ability to compete in global markets.

The ever-important forestry sector continues to see opportunity with stronger growth across Canada and, in particular, the United States. But uncertainty stemming from the NAFTA negotiations, along with the Trump Administration's 20 per cent softwood lumber duties, may hold companies in this sector back. Firms will be keeping a close eye on the situation as they consider their next investment plans.

One area of significant disappointment is the recent cancellation of the Energy East project, which would have brought Western Canadian oil to New Brunswick for refining and export. The private sector in the province had been looking at the opportunities that the project would have provided; they must now retrench and contemplate ways of expanding their businesses in a more moderate way.

New Brunswick's fiscal challenges remain on the mind of business owners; they continue to deal with the impact of the recent increase of the provincial corporate tax rate along with ongoing efforts to limit deficits. The last budget featured no new taxes or spending cuts; with the next election drawing near, the fiscal outlook will likely be a major issue.

Nova Scotia

ECONOMICS

Robert Kavcic,
Senior Economist

Economic growth looks to improve in Nova Scotia this year, with real GDP expected to grow 1.6%, up from a 0.9% pace in 2016. While still sluggish from a national perspective, that would be tops in Atlantic Canada, and mark the best pace in seven years.

The Halifax Shipyard is now busy with the $25 billion contract to build combat ships for the Royal Canadian Navy (through 2030) well underway. Other major **capital projects** such as the Nova Centre and Maritime Link are also supporting growth.

Residential construction activity has also picked up, with the number of units under construction in Halifax at the highest level in 40 years (there are 3,500 condo units currently under construction). This is partly in response to **firmer population growth** through two channels: a reversal of outflow previously headed to Alberta, and a big jump in international immigration.

The **labour market** continues to underwhelm, with employment trending modestly lower as sagging private-sector payrolls offset gains in the public sector. The jobless rate is bouncing around in the 8.0%-to-9.0% range, and remains favourable versus its Atlantic Canada peers.

The **Province of Nova Scotia is projecting a $21.3 million surplus** in FY17/18 (0.1% of GDP), after some adjustments related to federal transfers. Net debt also continues on a gradually-downward track, leaving Nova Scotia to stand out as a relative positive on the provincial credit landscape.

COMMERCIAL BANKING

Justin Scully,
Regional Vice President,
Commercial Banking,
Atlantic Provinces Division,
BMO Bank of Montreal

The outlook for Nova Scotia businesses continues to improve, with positive economic growth and a wide range of opportunities available to the province's businesses.

The benefits of the $25 billion project to build vessels for the Royal Canadian Navy at the Irving Shipyard in Halifax continue to support local businesses. While the building of the facilities has been completed, the actual construction of the ships themselves is well underway. Firms involved in that activity can expect to have major work for years to come, with the corresponding support for growth and jobs.

Other major construction projects in Halifax continue as well, supporting development firms in the city. The replacement for the Victoria General Hospital represents an investment of $500 million—a major opportunity for local construction firms. Other smaller projects are allowing for more jobs and growth, and the benefits of completed projects coming on stream—such as the Nova Centre—are just now starting to be felt. BMO is proud to be part of the Nova Centre, moving its Halifax operations into the new BMO Tower at that development.

The energy sector is benefiting from a slow but steady rise of oil prices, but the continued low prices for natural gas are beginning to diminish the opportunities for that resource. With ExxonMobil looking to wrap up production for its Sable natural gas project in 2019 and Encana starting to contemplate the decommissioning of its Deep Panuke project, offshore exploration efforts are now almost entirely focused on oil. But companies in this sector still have the benefit of local skilled labour—both on the energy and construction sides—given the return of Nova Scotians from Western Canada over the past several years.

The fishery continues to be an important part of Nova Scotia's economy. Global demand for local products is providing significant benefits for local fishers and processors, although the recent rise in the Canadian dollar could provide a drag on exports. But the industry as a whole is looking strong, with many of our customers benefiting.

Nova Scotia's long term business prosperity still requires ongoing effort, to capitalize on positive growth. The province continues to concentrate on attracting new immigrants to reverse the decline and aging of its population; ongoing success in this effort will support economic expansion for years to come.

Prince Edward Island

ECONOMICS

Robert Kavcic,
Senior Economist

The **PEI economy continues to grow at a solid pace**, with real GDP growth expected to soften to 1.7% this year after a 2.4% jump in 2016. Sturdy U.S. economic growth and a population boost should continue to offset public-sector restraint.

Exports are rising at a solid clip, led by gains in electronics and electrical equipment, as well as past gains in aerospace and transportation equipment. U.S. demand is expected to remain firm but the recent run in the Canadian dollar could take some momentum out of **tourism** activity.

Public-sector restraint is likely to remain a drag on growth in the year ahead. After peaking last fiscal year, **public-sector capital spending** is expected to fall gradually over the next four years—transportation infrastructure spending in particular will be cut sharply this fiscal year.

Population growth is holding at a very strong 1.7% y/y pace. International immigration has accelerated recently, but net interprovincial migration remains a modest drag. **Employment** growth remains strong in the private sector, while the jobless rate has fallen sharply, to below 9% at one point this summer.

The **Province of Prince Edward Island is projecting a $0.6 million surplus** in FY17/18 (effectively balanced as a share of GDP), a meaningful improvement from the $17.9 million deficit estimated for FY16/17.

COMMERCIAL BANKING

Justin Scully,
Regional Vice President,
Commercial Banking,
Atlantic Provinces Division,
BMO Bank of Montreal

With solid growth and a return to surplus in the provincial government's books, the story for Prince Edward Island's businesses looks positive. Sectors across the province are seeing good news.

As ever, the fishery represents a major component of PEI's economy. Catches are good and global demand—especially from the Asian market—continues to buoy the industry on both the fisher and processor sides. Exports are being held back somewhat by a higher Canadian dollar, but the overall situation remains strong.

Tourism continues to be a major source of income for the province. Visitors from across North America and around the world come to PEI for the impressive golf courses, fantastic beaches and vibrant towns. In particular, American tourists have been a major component of the tourism trade. Again, the somewhat stronger dollar represents a new challenge, but visitors from other parts of Canada help to alleviate any difficulties. Tourism businesses continue to see positive growth.

Agriculture also maintains its importance to the provincial economy, and the situation for PEI farmers remains solid. Developments in recent years that have reinforced the strength of the industry, including consolidation and modernization, have been good for the sector. Innovation is fundamental to the success of farms given global competition; we encourage our agriculture customers to take advantage of lower interest rates to make the necessary investments, especially given the likelihood of higher borrowing costs in the next year.

It is also impossible to ignore the ongoing benefits of economic diversification in PEI. Despite the province being known best for its more traditional economic drivers, more and more knowledge-based industries and high-tech firms are growing and succeeding. Companies focusing on aerospace, chemicals and information technology are calling PEI home and taking on the world. Strong economic growth in other global markets, particularly the United States, is helping these companies succeed. The higher dollar may hold them back somewhat, but their place in the PEI economy is stable and assured.

Newfoundland & Labrador

ECONOMICS

Robert Kavcic,
Senior Economist

Newfoundland & Labrador continues to struggle amid lower oil prices and fading near-term production and investment. Real GDP is expected to contract 2.0% this year, the weakest performance in Canada, before stabilizing next year.

The **oil sector** makes up roughly 22% of provincial GDP and more than 7% of employment—both just slightly smaller than in Alberta. As a result, incomes have been hit hard in the province. Production continues to fade after peaking in 2007, at least until the pipeline is filled with new output, such as Hebron later this year.

Employment continues to fall, recently hitting the lowest level in almost a decade. That has left the unemployment rate at the highest level in the country, around 15%. **Retail sales** and **home prices** have weakened as a result.

The **Province of Newfoundland and Labrador has largely dealt with a serious fiscal challenge**, leaning on a stiff and broad-based dose of tax measures (in Budget 2016) rising to nearly $1 billion per year. That included a 2 percentage point increase in the HST, across-the-board personal income tax hikes and a 1 ppt increase in the corporate tax rate. But, the province entered this period with relatively favourable tax rates, so these moves for the most part bring it back toward the provincial median. The budget deficit is currently tracking at a still-wide $778 million for FY17/18 (2.5% of GDP), but the improvement (and lower borrowing requirement) has been enough to **stabilize the Province's credit rating**.

COMMERCIAL BANKING

Justin Scully,
Regional Vice President,
Commercial Banking,
Atlantic Provinces Division,
BMO Bank of Montreal

While the recent situation for businesses in Newfoundland & Labrador has been a challenge because of lower oil & gas prices and government cutbacks, we see the current economic environment as starting to stabilize.

Much in the same way that we observed last year, we see firms that form the oil and gas supply chain holding back on investing in their own businesses until the situation stabilizes. A conservative approach to taking new opportunities clearly makes sense under the circumstances; all players are hoping that new investment prospects and renewed provincial growth will return once world energy prices stabilize.

At the very least, existing oil fields can still maintain production; even with lower prices, these operations are relatively low cost and remain viable. Also, we are expecting to see the first production from Hebron by the end of this year, which will help counteract weakness elsewhere. Plus, the $3.2 billion West White Rose project will begin construction very soon.

One very good piece of news comes from the bidding for offshore drilling—despite the collapse in energy prices, the most recent three bids led to over $2.5 billion in committed spending. This is a very good sign for the long-term viability of the industry and has shown continued interest from both larger, traditional firms and new entrants.

On the mining side, project spending has softened—representing a further challenge for the provincial economy. One major project—the underground nickel mine at Voisey's Bay in northern Labrador—may be able to support the industry in the meantime; this new activity will hopefully start next year.

The challenges at the Muskrat Falls hydro-electric project continue, with uncertainty still affecting businesses that might benefit. Cost overruns, and an expectation that the project won't generate electricity until 2020 at the earliest, remain issues. Local businesses look forward to clarity on the project, which could still provide significant economic benefits once complete.

In the fishery, recent drops in exports and reductions in the crab and shrimp quotas have caused difficulty. Fishers and producers hope to benefit from the Atlantic Fisheries Fund, which is designed to help drive innovation in the sector. If this initiative is successful, renewed businesses in the fishery will be well-positioned to compete in global markets in the long term.

Provincial Economic Summary

	BC	Alberta	Sask.	Manitoba	Ontario	Quebec	NB	NS	PEI	NL	Canada
Real GDP Growth (chain-weighted : year/year % change)											
2016 [1]	3.7	-3.8	-1.0	2.4	2.6	1.7	1.4	0.9	2.4	1.9	1.5
2017 f	3.8	4.1	1.7	2.1	3.0	2.7	1.5	1.6	1.7	-2.0	3.1
2018 f	2.5	2.3	2.0	2.2	2.3	1.9	0.9	1.1	1.3	0.0	2.2
Employment Growth (year/year % change)											
2016	3.1	-1.6	-0.9	-0.5	1.1	0.9	-0.1	-0.4	-2.3	-1.4	0.7
2017 f	3.7	0.9	0.1	1.7	1.6	2.0	0.2	0.6	2.9	-4.1	1.7
2018 f	1.7	1.2	0.2	1.1	1.6	1.2	0.0	0.0	0.2	-2.0	1.3
Unemployment Rate (percent)											
2016	6.0	8.1	6.4	6.2	6.6	7.0	9.6	8.4	10.8	13.5	7.0
2017 f	5.2	8.0	6.3	5.4	6.0	6.1	7.9	8.4	9.8	14.8	6.4
2018 f	5.5	7.4	6.2	5.2	5.5	5.8	7.3	8.4	9.4	15.4	6.0
Housing Starts (thousands)											
2016	42.1	24.6	4.9	5.3	75.3	38.6	1.9	3.7	0.6	1.5	198.4
2017 f	41.0	29.7	5.1	7.3	82.2	42.1	1.7	4.2	0.8	1.3	215.9
2018 f	37.0	29.0	4.8	6.0	71.5	39.5	1.7	4.0	0.6	1.3	195.3
Consumer Prices (year/year % change)											
2016	1.9	1.1	2.2	1.3	1.8	0.7	2.2	1.2	1.2	2.7	1.4
2017 f	1.9	1.3	1.4	1.7	1.6	1.3	2.3	1.3	2.0	2.6	1.5
2018 f	2.1	1.8	1.9	2.0	2.0	1.8	1.8	1.9	1.7	2.0	1.9

[1] 2016 provincial GDP by industry f = forecast