Labour Economic Monitor

May 2009

Introduction: Springtime in Alberta

It's springtime in Alberta, and signs of the new season are everywhere. Birds are flocking back, the ice is out of the river, and down at the Legislature, the government has unveiled *Budget 2009, Building on Our Strength*. Like most Alberta budgets, this one is as much about show business as it is about provincial finances.

The good news is that the government hasn't reacted to the recession by defaulting back to Ralph Klein-style budget cuts. Overall program spending will be down by $668 million, with health-care expenditures projected to fall by just $27 million. While these reductions look modest enough, given an overall budget of about $36 billion, their effects will be magnified by inflation and population growth. If the province's population rises by 1.7% while inflation rises by the same amount (which is what the budget assumes), the government would have to increase spending by about 2.9% just to keep services at the same level. So in real, per capita terms we're looking at spending cuts, although they're relatively modest.

The real kicker will come next year. According to the budget speech delivered by Finance Minister Iris Evans (who, by all accounts, is one of the more intelligent and hard-working members of Cabinet), the government will be looking to cut $2 billion next year unless the province's "fiscal situation improves beyond our forecast." That, unfortunately, is the government's economic vision in a nutshell: it's either an oil boom or spending cuts.

Not surprisingly, health care will be a major target when it comes time to implement these cuts. Health Minister Ron Liepert has taken to muttering darkly in the Legislature about the costs of Medicare:

> *"Mr. Speaker, if our publicly funded health care system isn't sustainable in the future, we won't have one…"*

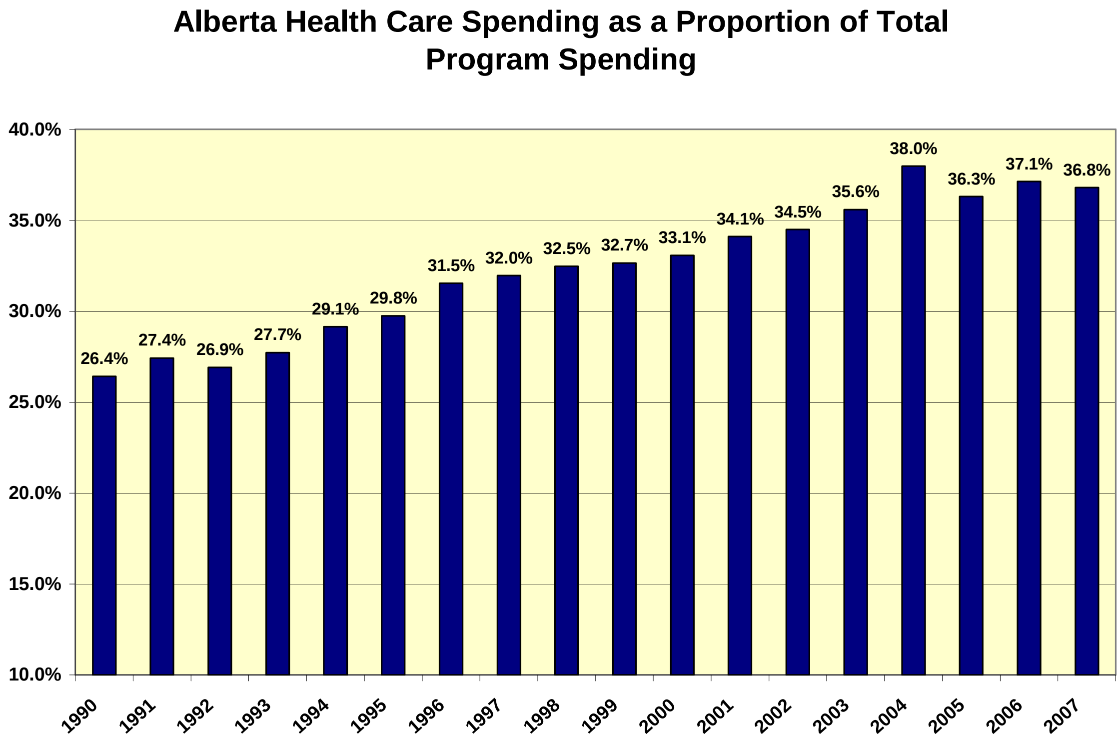
and,

> *"Unless we get a handle on expenditures, we won't have a publicly funded health care system."*

Of course, the Honourable Mr. Liepert is also on record as basing his vision for the future of health care on the Mazankowski Report. In other words: more privatization, and more cuts to services. The Mazankowski Report, which provided the blueprint for Alberta's vision of the "Third Way" in health care, was supposed to have gone on to its just reward (oblivion) when Ralph Klein pronounced the Third Way dead. It appears, however, that like the bad guy in the horror movies, it can always come back for a sequel.

We've heard this kind of talk before: Ralph Klein used to go on endlessly about how health-care costs were "skyrocketing out of control," and how we had to cut health care to save Medicare. Evidence to support this argument always relied on a bit of creative accounting. A favorite tactic is to point out that health care is consuming an ever larger portion of the provincial government. The logic seems to be that if we let it go unchecked, sooner or later every penny the government gets in revenue will go to health care, leaving nothing left to pay for education, social services, or subsidies for horse racing.

It's true that health-care spending has grown as a percentage of total budget program spending.

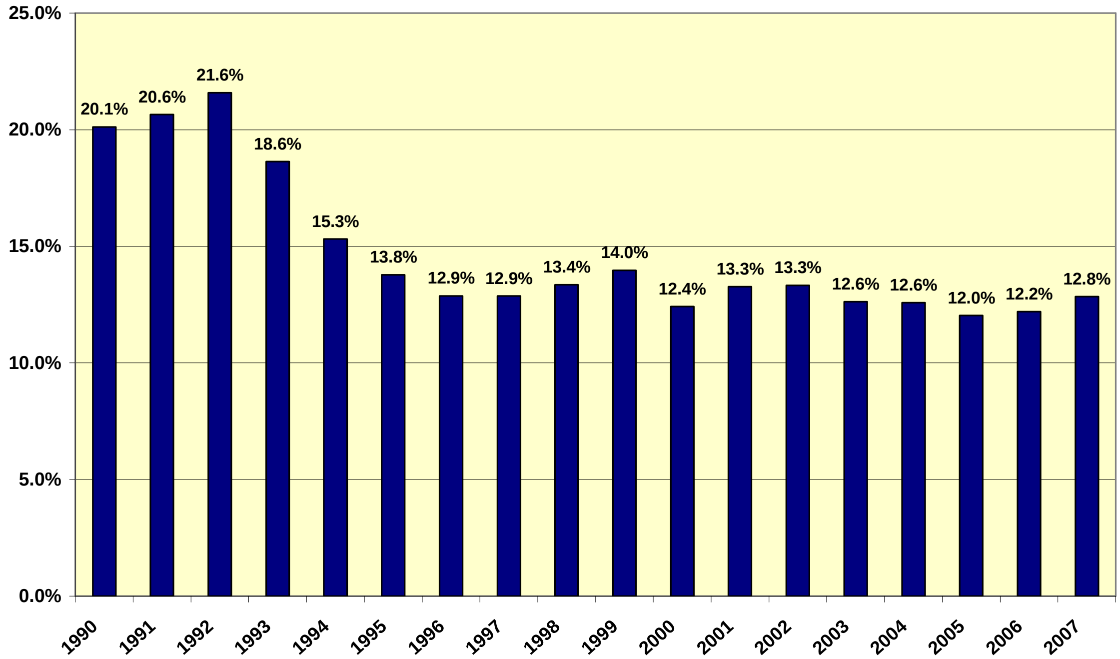


What the above chart doesn't tell us is what the budget for total program spending was doing at the same time. The question is: was health-care spending growing as a percentage of total budget spending because health care costs were "skyrocketing," or because the total budget for government program spending was stagnant or declining?

One way to evaluate total budget spending is to measure it as a percentage of the province's real Gross Domestic Product. GDP is the total value of goods and services produced in the province in a given year. By comparing budget program spending to GDP, we're figuring out how much of the total wealth we produce is spent on by the provincial government on providing services to Albertans.

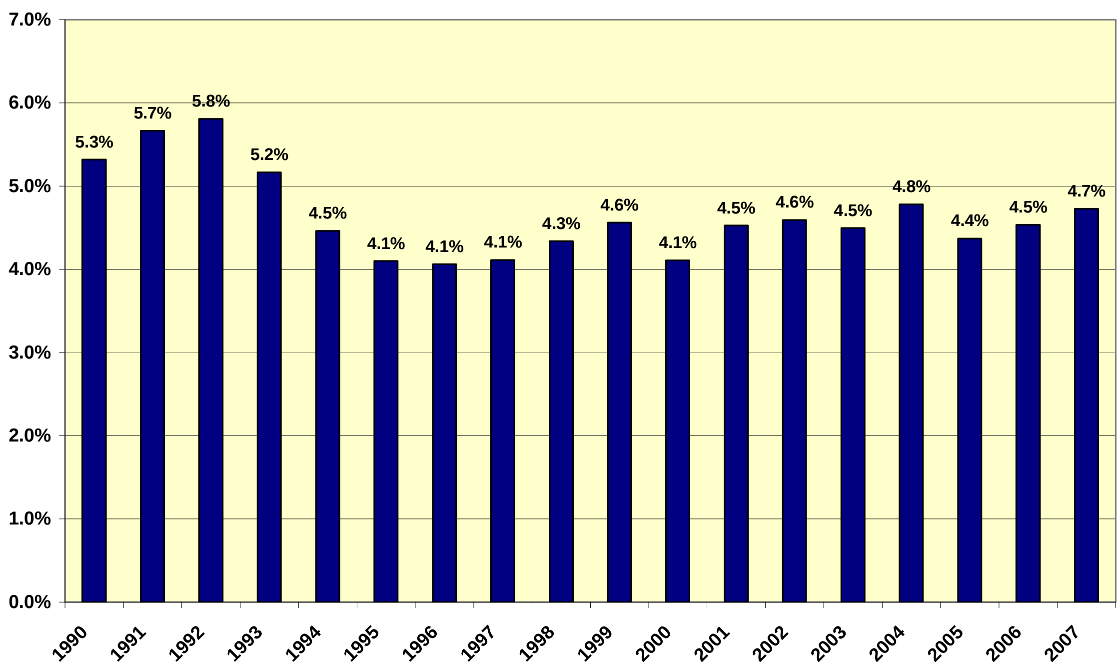
When we make this comparison, the result is striking: total provincial government program spending as a proportion of GDP dropped radically during the early years of the Klein cuts and never really came back. If the days of the radical spending cuts ended in the late 1990s, it's because there was nothing more to cut and for all the talk about "reinvesting" in Alberta, those funding levels have never been fully restored.

Alberta Gov't Program Spending as % of Real GDP



So if we turn our attention back to health care and ask, "How much of the wealth created in the province do we spend on health care programs?" the answer looks like this:

Alberta Health Care Program Spending as a % of GDP



So much for the “skyrockets!”

This is not to argue that we don’t have to work at controlling health-care costs. There are other ways of measuring government spending, and in future editions of *Labour Economic Monitor* we may take a look at some of them. We also have to look at how different kinds of health-care costs vary over time, and what drives these costs.

For example, capital costs for health care – the cost of building new facilities may be affected by a number of different cost drivers. When the Getty government decided in the 1980s that every Tory MLA should have at least one shiny new hospital in his or her riding, that decision drove up costs, arguably without really improving service very much. When Ralph Klein decided to reduce beds available and closed hospitals around the province (not to mention blowing one of them up!), he created a health-care infrastructure deficit that had to be addressed later, thus guaranteeing that costs would rise in the future. Finally, when the “reinvestment” designed to eliminate that infrastructure deficit happened in the middle of a construction boom that drove up costs all across the province, it pretty much guaranteed that the costs in question would rise very dramatically.

The real point of the argument is this: governments in general, and conservative governments in particular, always try to spin these kind of statistics and sacrifice clarity and accuracy to their own political agendas. That’s why we should never accept these kinds of arguments about government spending at face value. Rather, we have to ask what the numbers really mean and what’s the story behind them.

Global Recession Update

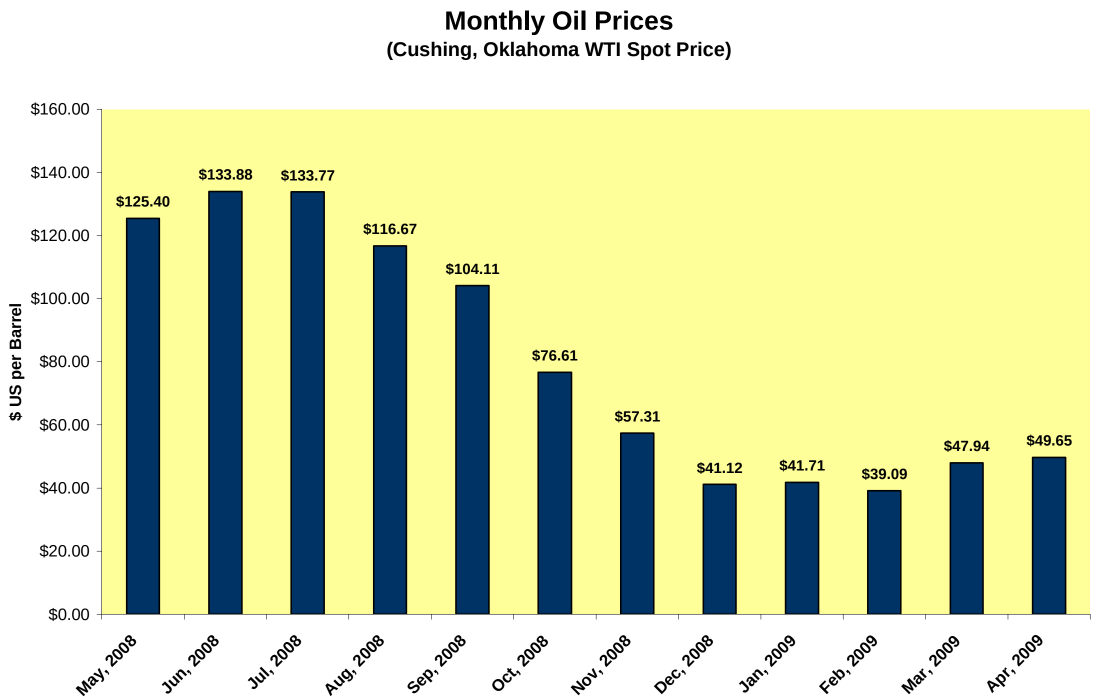
On the world economy front, the good news is that stock markets appear to be rising again. Of course, this could well be a “dead cat bounce” (a bit of stock traders’ humour used to describe a temporary uptick in markets, and based on the cynical observation that “even a dead cat will bounce once, if you drop it from high enough”).

The bad news is that even if this market rebound does prove more durable, it won’t have much of an impact on the “real economy” – where jobs are created, and goods and services are produced. The latest figures from the International Monetary Fund have downgraded growth projections for the coming year even further. Last fall, the IMF was projecting the global economy to grow by about 3% this year, but the current forecast is for a world-wide contraction of 1.3%.

Meanwhile, world leaders continue to stumble around like a flock of sheep on drugs. At the G20 meeting in London a few weeks back, the assembled leaders promised to give $1.1 trillion to struggling economies around the world. The largest three pledges were for $100 billion each from the U.S., the European Union, and Japan. So far, Japan is the only one of these to actually produce the cash. If this kind of shilly-shallying is what we can expect from the leaders of the world economy, it could be a long recession.

Energy Prices

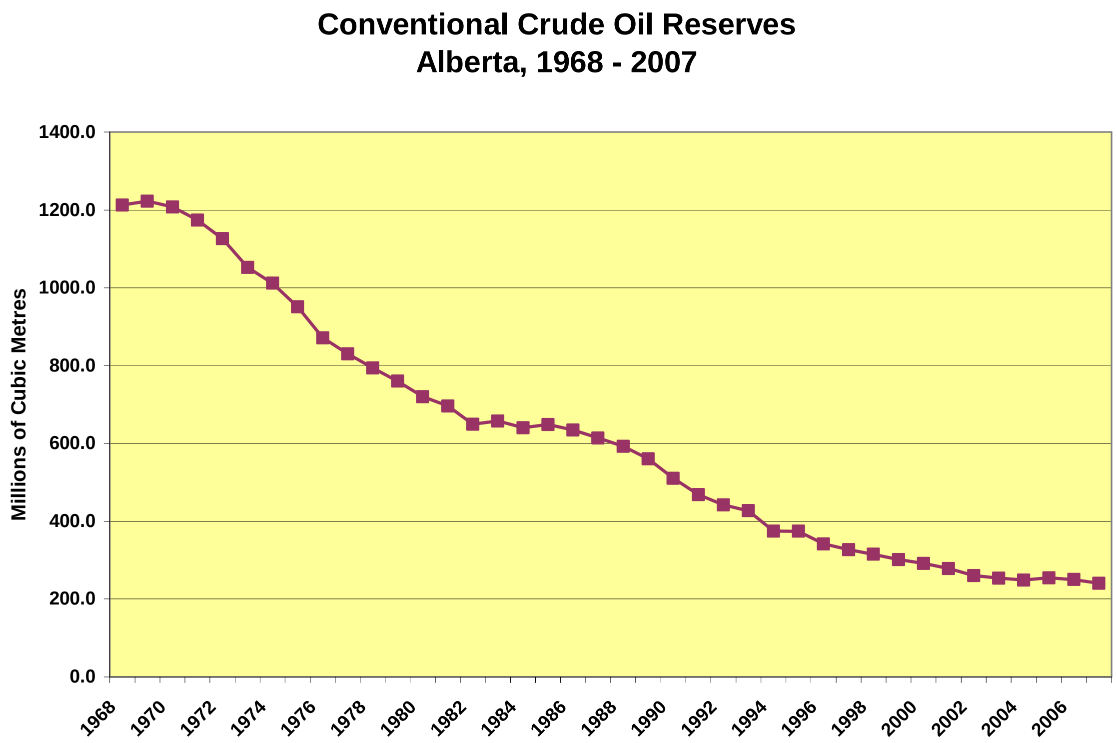
Energy markets are also a case of "sort of good news, bad news, and more bad news." On the one hand, the price of conventional crude oil rebounded slightly in April, after sinking to below $40 per barrel in February. As this is being written, prices on the spot market have risen above $50/Bbl.



The first bad news is that this modest recovery is unlikely to do much for the provincial economy. This seems odd, given that by historical standards current oil prices aren't that low. Even after the stunning drop of the last half year, the price of West Texas Intermediate crude is still at about the level it was in late 2004, and the provincial economy was doing very well at that point.

The oil price spike of the last two years wasn't entirely the result of normal market forces. It's true that it reflected a world-wide economic boom, and that the prices of most raw materials were rising. In the case of oil, however, the supply is both restricted by the efforts of the OPEC cartel and then subject to further manipulation by the giant oil companies. Finally, market speculators drove the price of futures contracts well above any kind of rational level.

So if current prices are reasonably good, why shouldn't we expect the Alberta economy to rebound quickly? The short answer is that modest improvements in the price of conventional crude oil won't help our economy because we don't have much of it left.

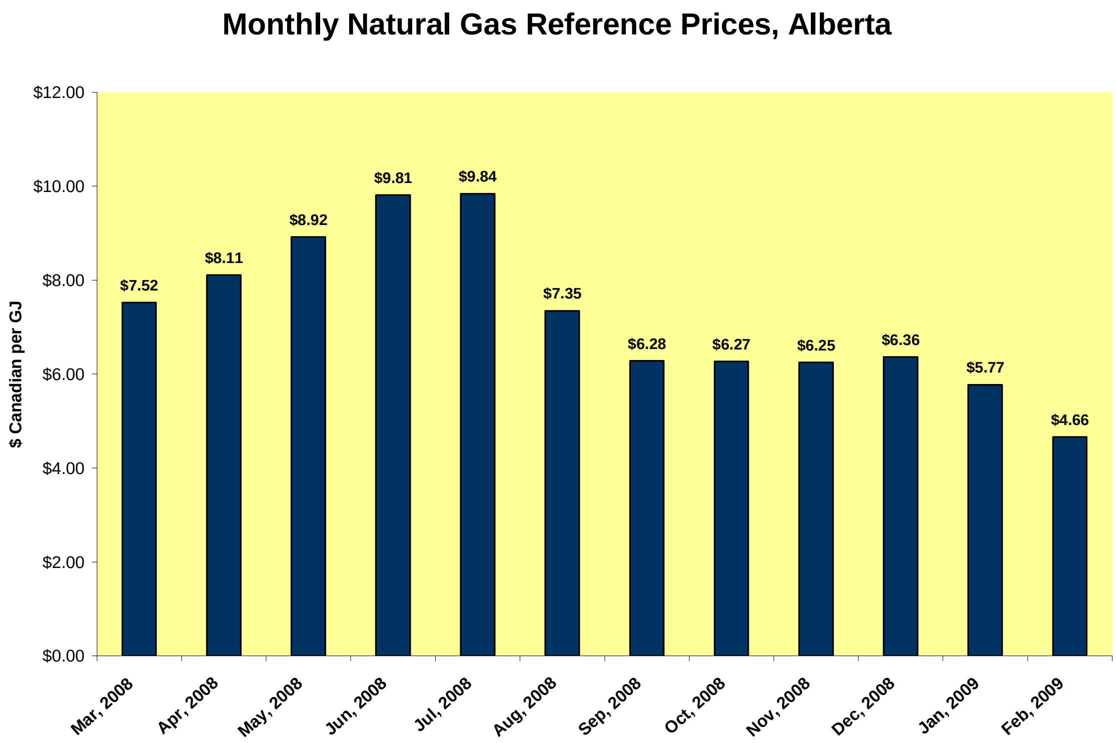


For the past forty-odd years, successive governments have sold off Alberta's oil resources at a fraction of its true worth, charging royalties that were a joke by international standards. Now the end of our reserves of conventional oil is in sight and we have nothing to show for it, except for the pitiful remnant of the Heritage Fund.

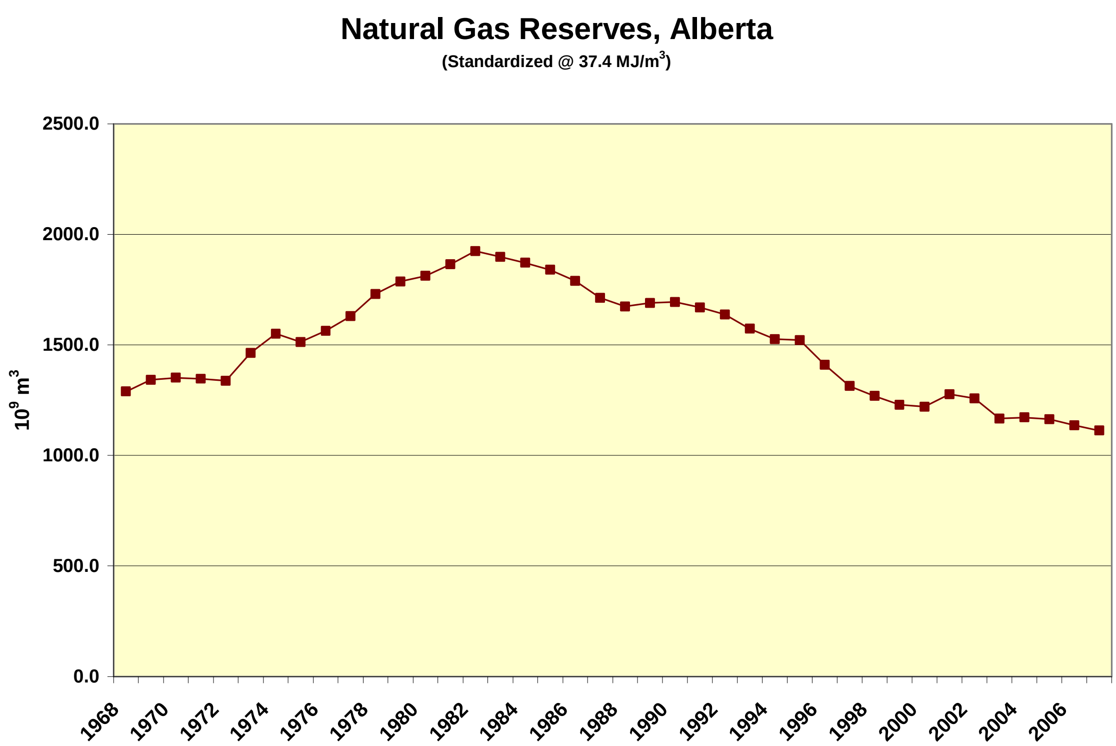
At the same time, governments used what royalty revenues they did take in to substitute for tax dollars in order to support the "Alberta Advantage." As a result, the revenue system that supports the government has been hollowed out and the province's ability to raise tax revenues sufficient to pay for needed public services has withered.

This explains why the Stelmach government in 2005 and 2006 was passing out oil-sands licences as though they were free merchandise samples at a sales convention. They know that time is running out for the conventional oil and gas industry, and they're desperate to get a new revenue stream in place before the bottom falls completely.

The last bit of bad news is that natural gas prices have tanked and show little sign of recovering in the near future. The February price was just $4.66 per Gigajoule. The budget assumes that this price will rise to an average of $5.50/GJ over the coming fiscal year but that even if this happens, revenue from gas royalties will fall by almost 40% this year. Estimates for royalties through 2011-2012 are that these revenues will rise only slightly, even if gas prices rise to $6.50/GJ.



In part, these dismal predictions reflect the fact that major natural gas discoveries in the U.S. will hold prices down. That, however, is only part of the story.

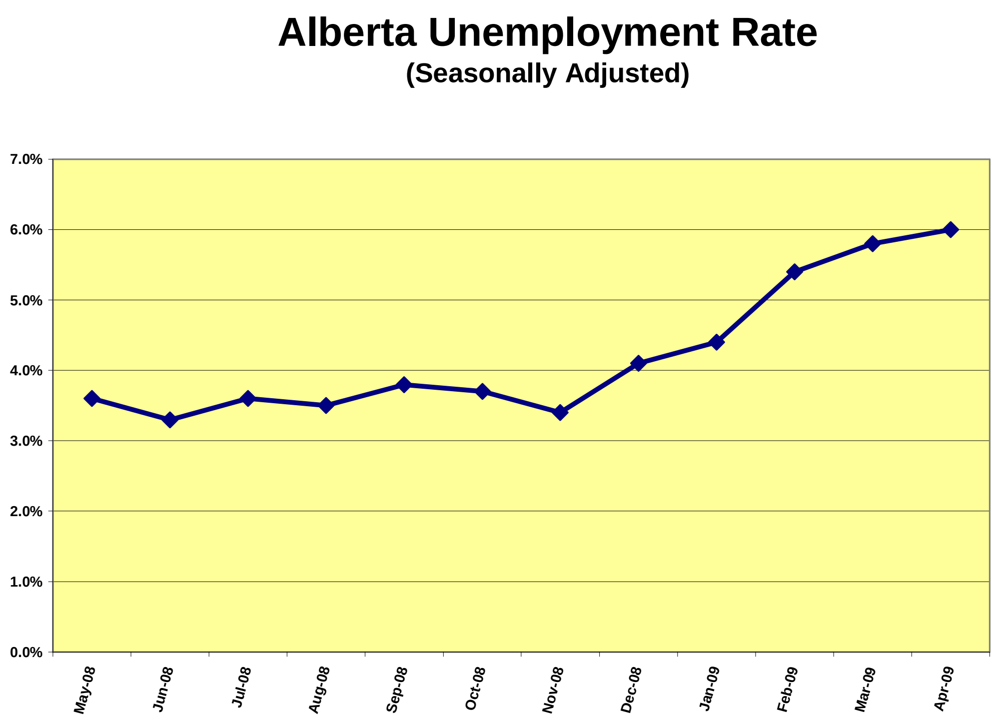


The government is also coming to recognize that Alberta's reserves of natural gas are dwindling, and that this means that our days as a major exporter are numbered. The province's gas reserves peaked in 1982 and any undiscovered gas remaining is probably contained in relatively small pockets of gas that are deeper and therefore more expensive. No amount of subsidizing the conventional energy industry through royalty cuts will alter these realities.

Unemployment

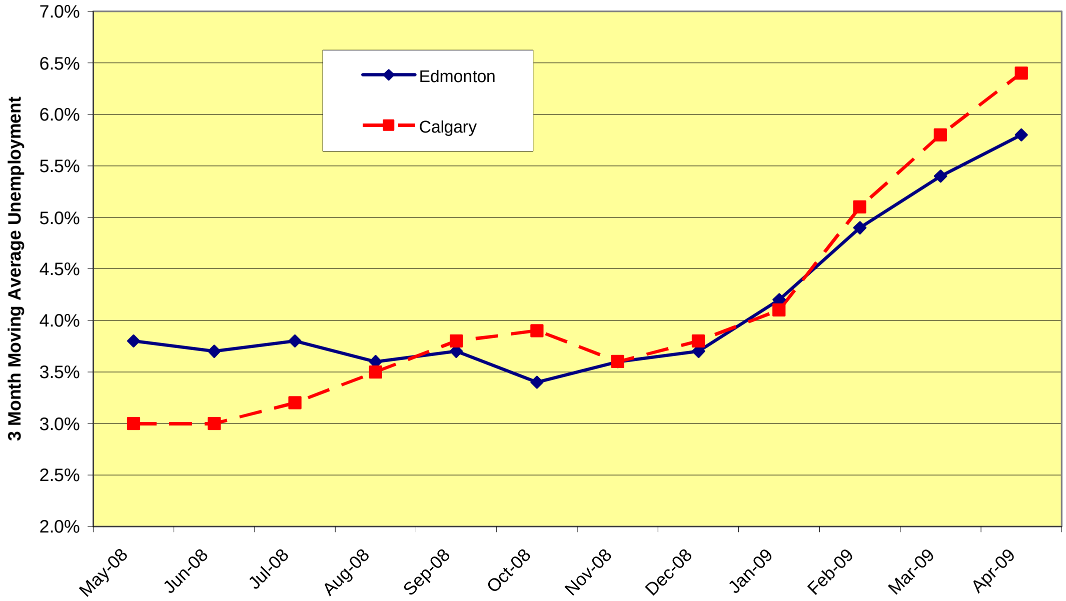
Unemployment rates in Alberta took off in December and have been rising ever since. April's seasonally adjusted rate for the province was 6.0%, as compared to a national rate of 8.0%. As usual, these numbers conceal a much worse reality, as thousands of full-time jobs are replaced by part-time work.

Over the last twelve months, the number of Albertans in full-time positions has fallen by 56,500 (a drop of 3.3%), while part-time jobs have increased by 42,200 (a whopping 13.4% increase).



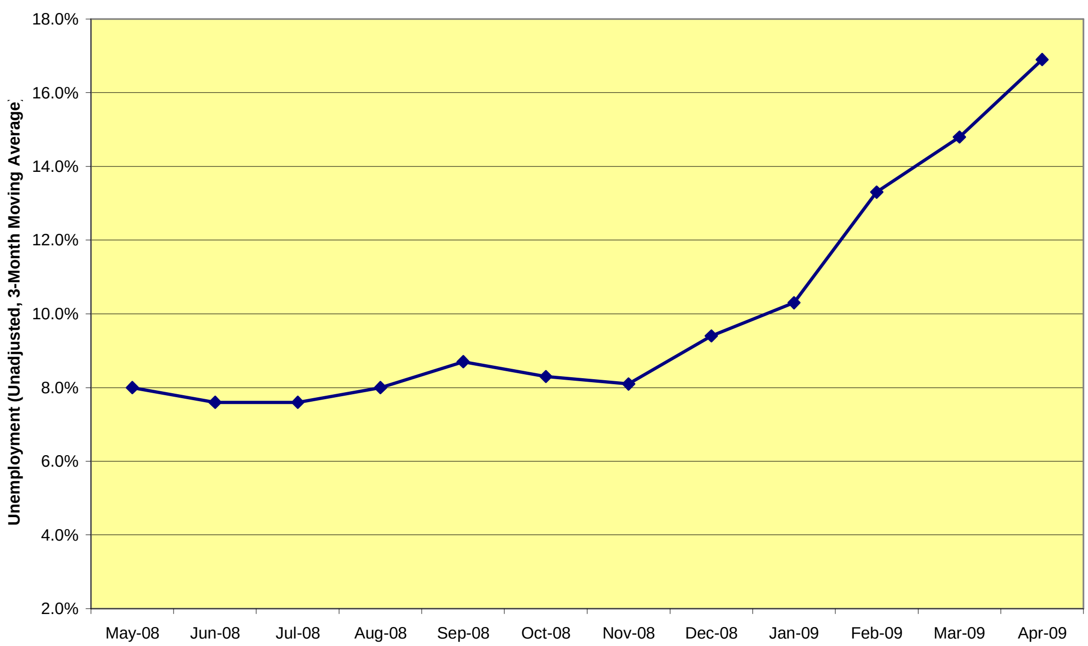
All regions in the province show rising joblessness, with Calgary's unemployment rate more than double what it was a year ago. In general, rates area higher in northern Alberta, while in the south, the unemployment rate in the Lethbridge/Medicine Hat has risen only slightly – from 4.4% in April 2008 to 5.3% in April, 2009.

Regional Unemployment Rates, Edmonton and Calgary



As always, though, the really shocking figures are those for Alberta's aboriginal people.

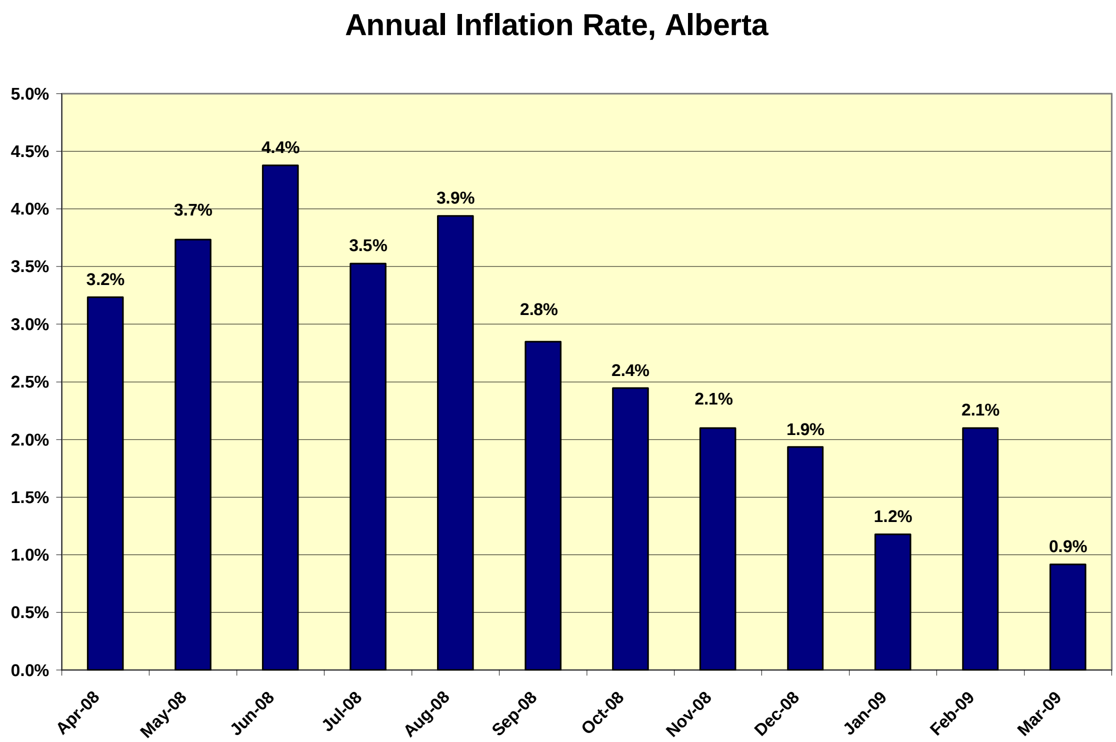
Alberta Unemployment: Aboriginal People (Off-Reserve)



The April joblessness rate for aboriginal people living off-reserve was 16.9%, more than double the rate of the previous year. This is persuasive evidence of the structural racism embedded in the Alberta labour market – aboriginals are almost always the last hired in good economic times and the first fired when recession hits.

Inflation

The rate of inflation continues to slow in Alberta, with downward pressure on the consumer price index stemming from falling natural gas prices. In March, the year-over-year inflation rate in Alberta was just 0.9%. The national rate was slightly higher, at 1.2%.

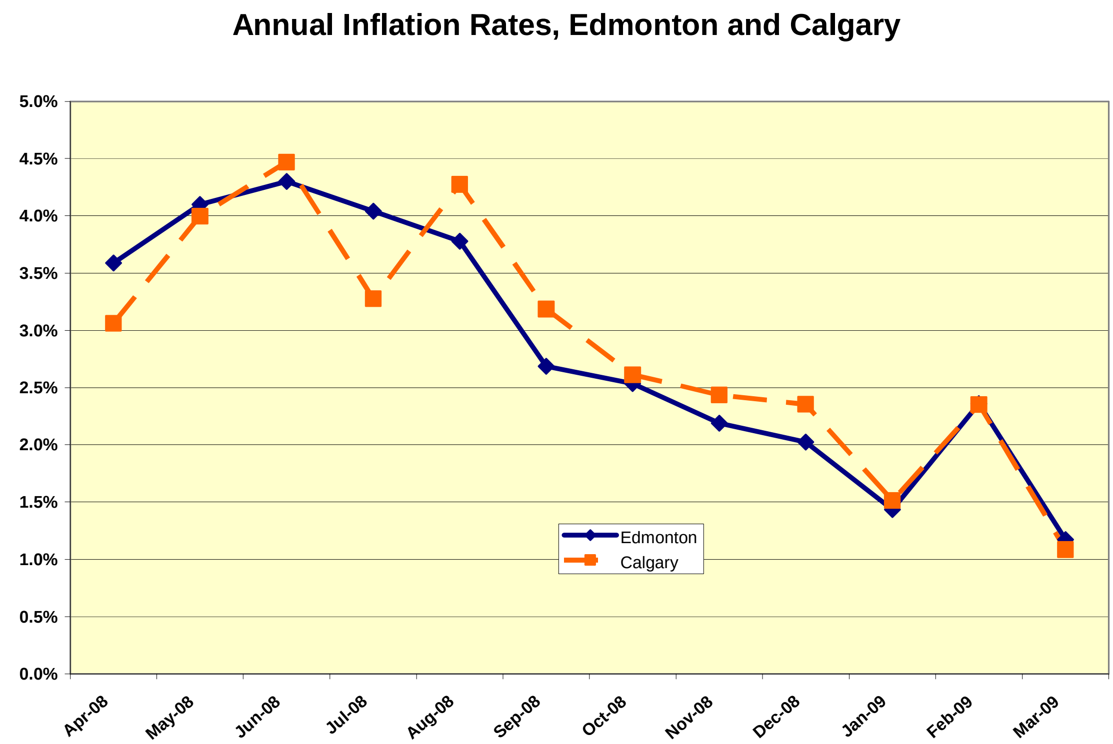


What inflation remains in the economy is driven by rising food prices. This is unfortunate since we can choose to put off buying a new car or appliance, but we can't really postpone food purchases.

As we've discussed in previous issues of the *Labour Economic Monitor*, the Bank of Canada bases its interest rate policies on so-called "core inflation" – the Consumer Price Index with volatile items such as food and fuels removed. The Bank's core index (for all of Canada) in March was 2.0% higher than a year ago, suggesting that despite the severe recession, some inflationary pressures remain.

The higher core rate of inflation is a bit of a concern because while recessions obviously tend to drive prices down, the huge amount of money being poured into bailing out banks could result in very serious inflationary pressures down the road. High rates of inflation could then cause the various central banks to raise interest rates, thus choking off potential economic recovery. Faced with the triple-threat of hyper-inflation (if the various stimulus packages go too far), deflation (if they don't go far enough) and stagflation (if we get the worst of both worlds), it's hard to picture a strong upturn in the North American economy any time soon.

As we'd expect, inflation in Edmonton and Calgary is tracking province-wide trends quite closely. The March rate of inflation was 1.2% in Edmonton and 1.1% in Calgary.



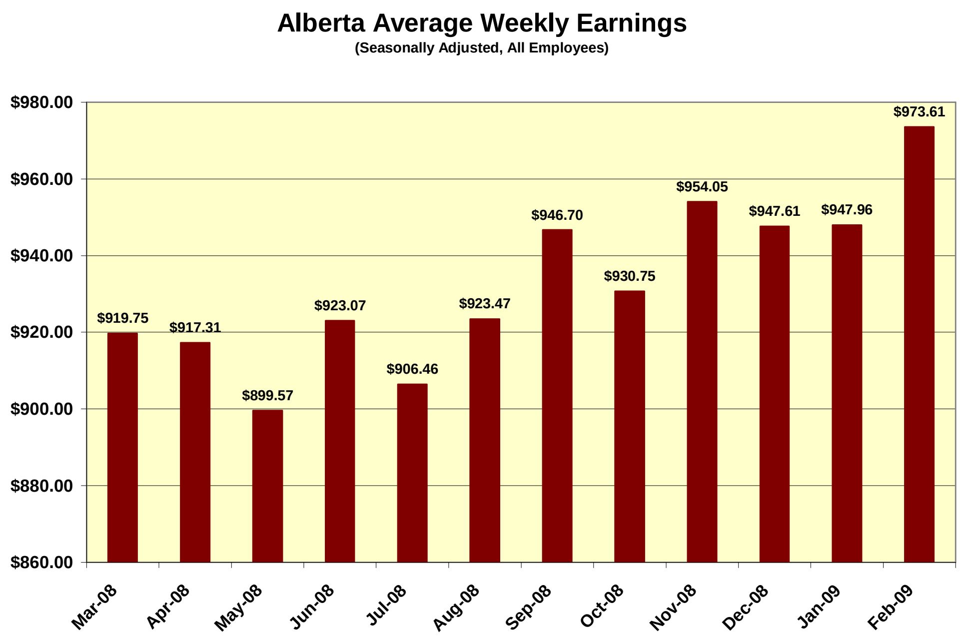
Wages

Those readers who pay close attention to the wage figures published in the *LEM* (and we know that includes almost all of you) will notice that both the weekly and the hourly wage numbers appearing in this issue don't jibe with those from the last edition. For example: the last issue we said that average weekly earnings for June of 2008 were $871.51, while in this issue they are reported as $923.07. This difference, of over $50 per week, is obviously significant, and requires some explanation.

The same is true for the average hourly wage numbers. In the last issue of *LEM*, we reported the June 2008 average hourly wage in the province as $20.92/hr, while the current edition the figure for the same month is $22.15/hr, over a dollar an hour more. These differences require an explanation.

The wage data presented in *LEM* come from the Statistics Canada *Cansim* database, which in turn is based on something called the *Survey of Employment, Payrolls and Hours* (SEPH). In March of this year, StatsCan announced that they were changing the statistical models used to calculate average wage and earnings figures. The nature of these changes is too complicated to report here, but the result was to show higher wage growth than the previous model. This created some interesting problems for unions or other groups that had negotiated pay increases based on changes in the Alberta Average Weekly Wage, and those problems are still be worked out.

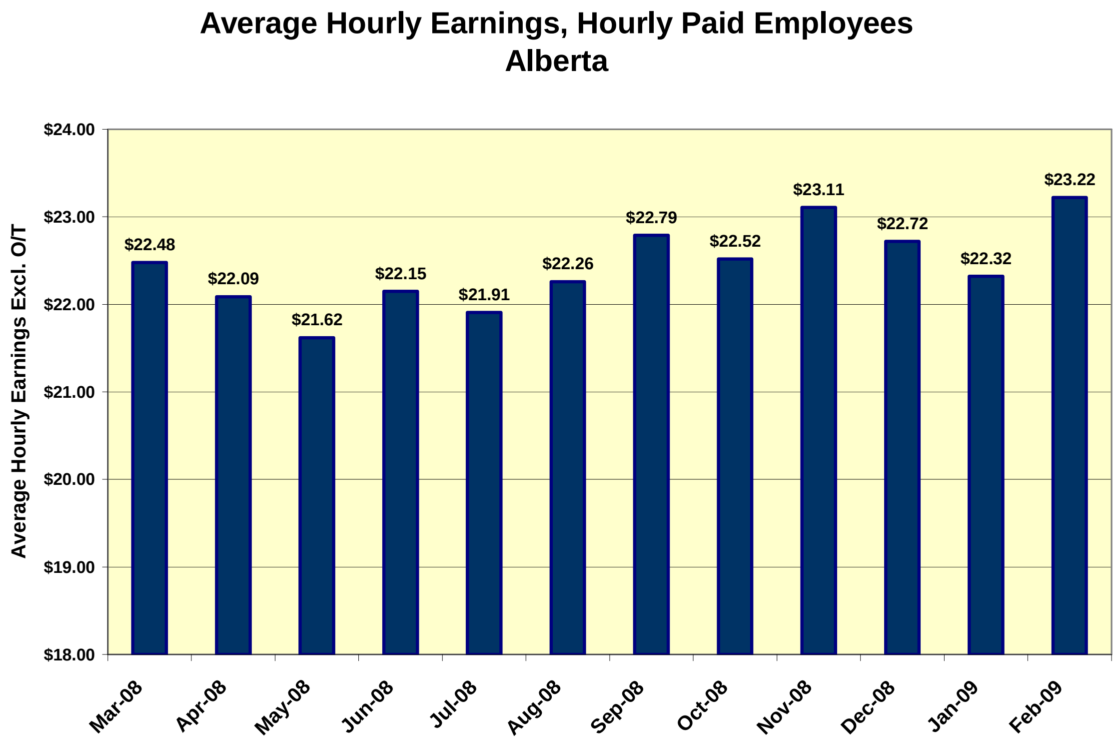
For our purposes, however, all we need to know is that the figures published in the *LEM* are based on the most accurate data available from Statistics Canada at any given time.



The latest figures show healthy growth in weekly earnings, with the average for the last twelve months a full 6.0% higher than over the same period one year earlier. Given that inflation is about 1% (see above), this means that Albertans are making big gains in real wages, even as the recession begins to bite. This is not what we would normally expect, but there are a couple of things that may help to explain it:

1. Wages are a “lagging indicator” – it takes time for changes in the supply of and demand for labour to be reflected in wage levels. In addition, many unionized workers will be working under collective agreements negotiated at the height of the boom. This is one of the advantages on belonging to a union – your employer can’t knock down your wages the minute the economy takes a downward turn (as recently happened to workers employed in the province’s largely non-union drilling industry). By the same token, unionized wages will sometimes recover more slowly when the economy picks up, as agreements negotiated in the middle of a slump continue to apply.

2. Wage information from StatsCan always lags several months behind and therefore may not yet have picked up the latest trends in wages in the labour market. The wage figures quoted above, for example, only go up to February of this year. Unemployment in Alberta didn't really start to take off until December of '08, so the twelve-month average numbers quoted above only include two months where the labour market was starting to turn downward.



Hourly wages show a tend similar to the weekly figures quoted above, with the twelve-month average about 6.2% higher than in the same period a year earlier.

Wage Settlements

What with the length of time it takes to negotiate a collective agreement and the sometimes even longer period it takes to report the settlement to the government, it's not surprising that only a handful of settlements have been reported so far in 2009.

Year	*# CAs*	*# E'ees*	*Rate*
2006	209	41,632	**3.5%**
2007	244	99,197	**5.2%**
2008	173	97,085	**4.5%**
2009	24	2,288	**1.8%**

Public-sector settlements are averaging 2.7% so far this year, with private sector rates climbing by 1.2%. In fact, neither of these trends is meaningful since they reflect only a relative handful of agreements signed and just 2,300 employees in total.

For more detailed information on sectoral settlement rates, contact *Labour Economic Monitor* at the AFL, or check out the Alberta Employment ant Immigration data at:

http://www.employment.alberta.ca/3240.html

Conclusion

The recession is just beginning to bite in Alberta, and how long it will last depends on factors in the global market far beyond the control of anyone in this province. Even if, for example, oil prices begin to rise again, that won't necessarily mean the provincial economy will pick up noticeably. As noted earlier in this issue, the conventional oil industry in the province is well past its prime, leaving the Stelmach government with nothing but the large oil-sands megaprojects to shore up any economic recovery. Unfortunately most of these projects have been put on hold or abandoned, and it will take more than a modest rise in crude prices to get them restarted.

With the global banking system still in lockdown, large-scale credit is still incredibly difficult (and expensive) to obtain. Oil-sands extraction facilities and upgraders are very capital-intensive projects and require a high level of debt financing. We're unlikely to see much of an increase in this sector until credit markets loosen up, and it's hard to say when that will happen.

There is one good piece of news, however. With the public backlash against the massive (and massive is probably an understatement) multi-trillion-dollar bailout of the banking system, many of the "masters of the universe" have been forced to forego their million-dollar bonuses. This, in turn, has led to a serious decline in the markets for polo ponies and private jet aircraft.

Fortunately, merchant bankers and investment dealers are a resourceful bunch. Forced to do without bonuses, these financial wizards are falling back on – raises!? The Manchester Guardian reports that:

> *"Bankers and financiers in the City of London are scooping bumper pay rises to compensate for losing multi-million-dollar bonuses in a development that could trigger fresh "reward for failure" rows. UBS, which last year received a Swiss government bailout, is paying London staff increases of between 15% and 20%."*

Makes you feel warm all over, doesn't it?