

# **Budget Address**

**2009 - 2010**

***NORTHWEST TERRITORIES***

**BUDGET PAPERS**

**A ♦ Economic Review**

**February 5, 2009**

## **ECONOMIC REVIEW 2009 – 2010**

### **Outlook**

In 2009 the size of the Northwest Territories (NWT) economy, as measured by its real<sup>1</sup> gross domestic product (GDP), is forecast to decline by 1.3 per cent from 2008. The decline reflects the global economic slowdown that began to develop in the United States towards the end of 2007 and then spread throughout the international economy during 2008. Diamond mining, the NWT's largest business sector, has been affected by a number of factors. Costs have increased as production has shifted towards the more expensive underground extraction process and diamond prices have weakened.

The NWT economic outlook over the medium-term is uncertain. Without approval of new projects, and based on the known status of existing projects, the NWT's GDP is expected to decline annually until 2012.

The United States entered its recession near the end of 2007. The U.S. currently accounts for almost one-half of the world market for polished diamonds so weakening American demand places downward pressure on diamond prices. Emerging economies including Russia, India and China, important growth markets for diamonds, were unable to compensate as they also began to weaken in 2008.

All major Canadian banks and other major private sector forecasters predict that the Canadian economy will weaken during 2009.

Construction of the Snap Lake diamond mine was completed in 2007 and no new capital investments of similar size are being undertaken in 2009. The credit squeeze of 2008 is expected to continue into 2009. The resulting scarcity of available capital and the high cost when it is available, may impact the timing of construction projects currently in the planning stage.

Employment of NWT residents is expected to increase modestly from 22,000 in 2008 to 22,100 in 2009. Average weekly earnings are forecast to increase by 1.1 per cent in 2009.

Consumer price inflation in Yellowknife (NWT-wide figures are not available) is expected to moderate. Consumer prices increased by 4.0 per cent in 2008 over 2007; in 2009 they are expected to rise by 2.4 per cent.

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<sup>1</sup> Measured in chained 2002 dollars

### ***Northwest Territories Economic Outlook***

Indicator	2006	2007	2008e	2009f
Gross Domestic Product, chained 2002 \$ millions	3,711	4,138	3,601	3,554
% change	5.1	11.5	(13.0)	(1.3)
Total Investments, chained 2002 \$ millions	1,690	1,827	1,520	1,424
% change	18.0	8.1	(16.8)	(6.3)
Consumer Expenditures, chained 2002 \$ millions	1,157	1,202	1,228	1,245
% change	2.8	3.9	2.2	1.4
Government Expenditures, chained 2002 \$ millions	1,120	1,154	1,147	1,127
% change	(1.8)	3.0	(0.6)	(1.8)
Exports, chained 2002 \$ millions	2,571	2,974	2,611	2,589
% change	2.2	15.7	(12.2)	(0.5)
Imports, chained 2002 \$ millions	2,859	3,015	2,907	2,843
% change	5.6	5.5	(3.8)	(2.2)
Employment, number of persons	22,800	22,600	22,000	22,100
% change	0.4	(0.9)	(2.7)	0.5
Average Weekly Earnings, dollars	973	1,005	1,046	1,058
% change	1.3	3.2	4.1	1.1
CPI All-Items (Yellowknife, 2001 = 100)	107.7	110.8	115.3	118.1
% change	1.4	2.9	4.0	2.4

Source: Statistics Canada and the NWT Bureau of Statistics

(e) estimate

(f) forecast

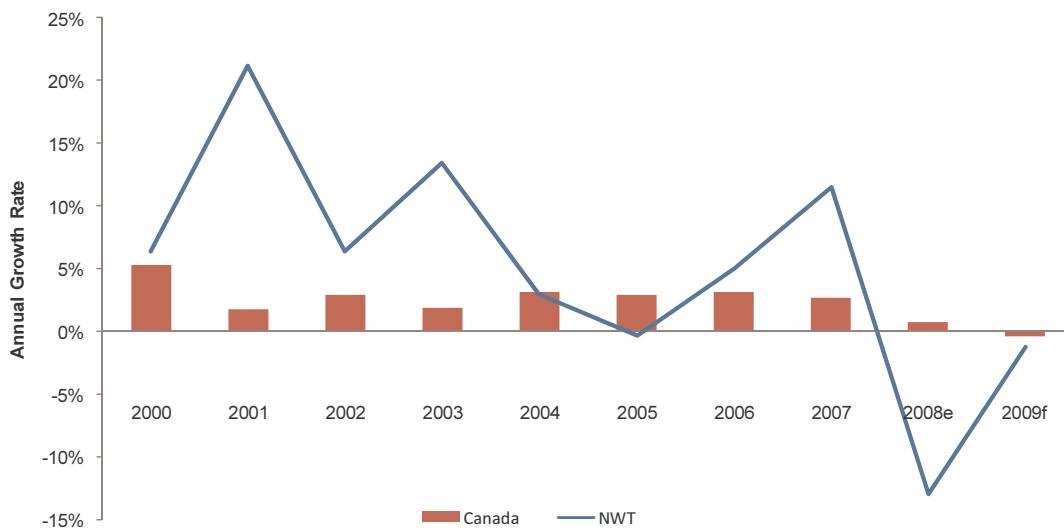
## 2008 Economic Performance

The NWT economy is estimated to have shrunk 13.0 per cent in 2008 compared to 0.7 per cent for Canada. Reduced economic activity in 2008 was directly related to the completion of the Snap Lake diamond mine. This project raised construction activity to historically high levels in 2007. Completion of the mine in 2007, without new investment of a comparable size, led directly to the reduced level of GDP in 2008.

In 2007 the NWT's GDP per capita was almost \$110,000, the highest in Canada and more than double the Canadian average of \$46,500. GDP, however, includes incomes paid to all factors involved in the production process, which are labour and capital. Because the NWT has a capital-intensive resource-exporting economy, a smaller portion of the NWT GDP is earned as wages, salaries and supplementary income than the Canadian average: 36.2 per cent in 2007 compared to 52.0 per cent nationally.

Mining, principally diamond production, has been the main economic driver of the territorial economy since 1999. In 2007 the mining industry grew by 31.6 per cent, well above the industry's average annual rate of growth between 1999 and 2006 of 23.2 per cent. During 2008, the NWT's third diamond mine at Snap Lake was officially opened.

### *Annual Growth Rate in Real GDP, chained (2002) dollars*

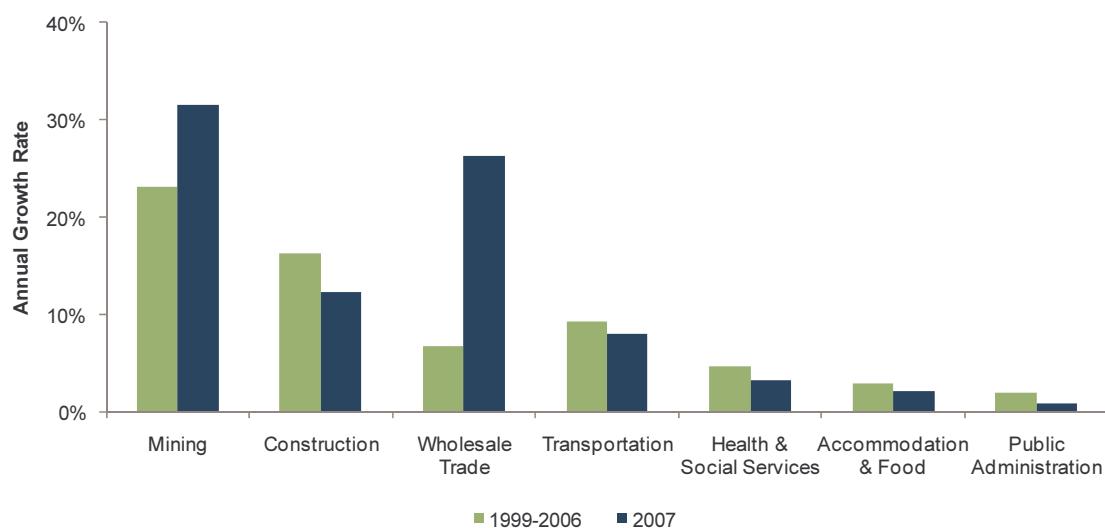


Source: Statistics Canada, NWT Bureau of Statistics and NWT Finance  
e = estimate  
f = forecast

Other important growth sectors include wholesale trade and construction. Wholesale trade had a very strong performance during 2007, increasing 26.3 per cent over 2006 and significantly bettering the 1999 to 2006 average annual growth rate of 6.7 per cent. Construction also recorded strong growth of 12.3 per cent during 2007, although this was slightly down from the average annual pace of 16.2 per cent during the previous seven-year period. Completion of the Snap Lake mine during this period contributed to the slower rate of growth.

The health and social services sector grew 3.1 per cent in 2007, slowing from an average annual growth rate of 4.6 per cent over the previous seven years since Division. Public administration (federal, territorial and local governments) increased by 0.8 per cent in 2007 over 2006.

#### ***Annual Growth Rates of Selected NWT Industries, chained (2002) dollars***



Source: Statistics Canada

The NWT's economy is integrated with the global and national economies. 2008 was a tumultuous year for many economies. The American sub-prime mortgage crisis revealed weaknesses in the global financial system. The resulting financial crisis and ensuing global credit freeze contributed to the consumer-led economic recession in the United States and other major economies. The International Monetary Fund forecasts that developed countries will experience a recession during 2009 while emerging economies are forecast to grow, but at much reduced rates.

As a consequence of the developing global slowdown, commodity prices peaked in mid-2008 then dropped precipitously. The Toronto Dominion Commodity Price Index (TDCI) shows how commodity prices rose until July 2008 then dropped dramatically. By November the index had lost half of its value, reflecting the lower global economic outlook as well as tighter credit conditions and efforts to reduce debt-to-equity ratios. Price volatility raised levels of risk and uncertainty for investors, contributing to the economic slowdown.

By the first week of 2009, the price of oil had fallen 70 per cent from its July 2008 high. Similarly, the price of natural gas had fallen by 57 per cent. Gold was trading 11 per cent below its March 2008 high, but still slightly above its average weekly price for the year.

### ***TD Commodity Price Index, 1997=100***

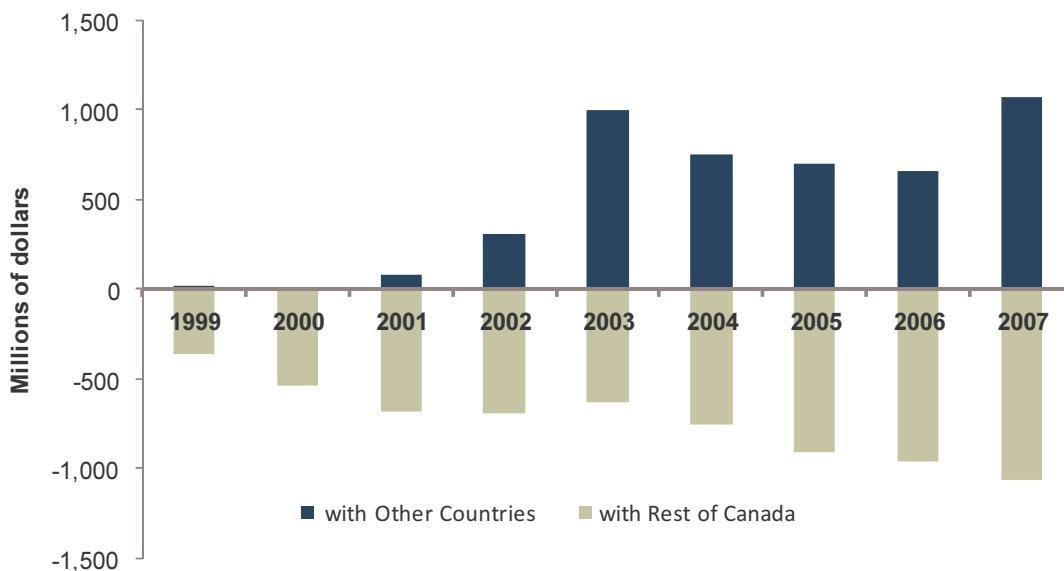


Source: TD Bank Financial Group

### ***Trade***

The NWT economy depends on trade with other countries and the rest of Canada. The NWT's trade surplus with other countries grew markedly during the first part of the decade, primarily driven by diamond exports. In 2007 the NWT trade surplus with other countries grew by 62.2 per cent over the 2006 level. The NWT has a trade deficit with the rest of Canada since most goods, including machinery and construction materials, are imported from southern Canada. Since Division, the trade deficit with the rest of Canada has grown, but at a slower rate than the trade surplus with other countries has increased. In 2007 the trade deficit with the rest of Canada increased by 10.3 per cent over 2006.

### NWT Balance of Trade, chained (2002) dollars



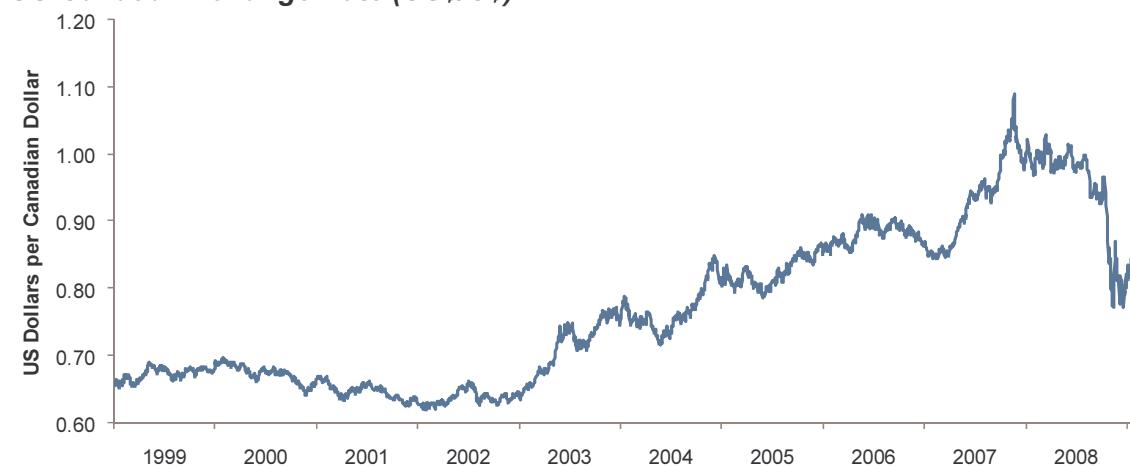
Source: Statistics Canada

### Exchange Rate

The NWT's international trade surplus is important to the health of the economy. A strengthening Canadian dollar means that NWT businesses get paid less in Canadian dollars after the currency conversion although it does mean that capital equipment imported to Canada will be less expensive. When the Canadian dollar declines, the effects are the reverse: NWT businesses will get paid more for their products after the currency conversion while imports will cost more.

The Canadian dollar spent the first half of 2008 roughly at par with the American dollar. In July the Canadian dollar began to fall against the American dollar, settling into the low 80 cent US range by the end of the year.

### US-Canada Exchange Rate (US\$/C\$)

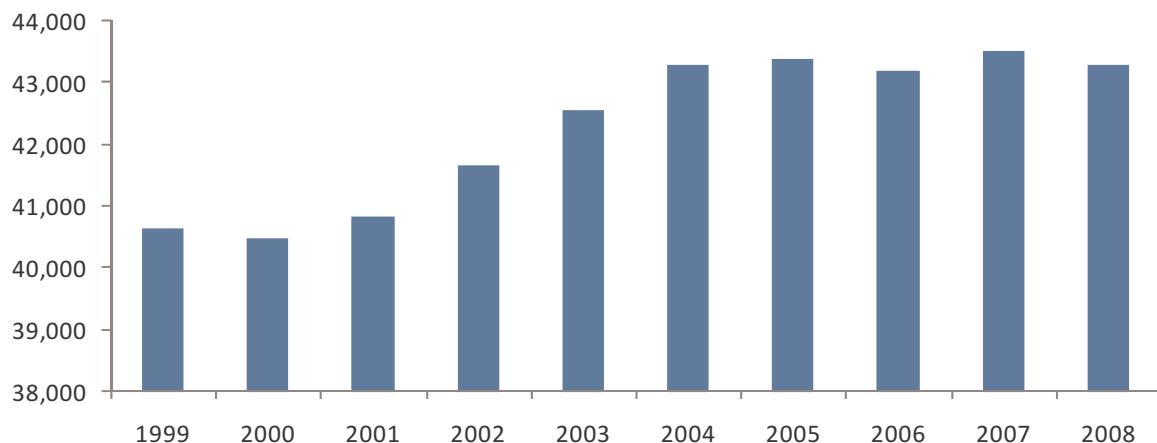


Source: Bank of Canada

### ***Population***

The NWT population was estimated to be 43,151 on October 1, 2008, an increase of 6.5 per cent since 1999 but a decrease of 152 persons from the beginning of 2008. The decrease in 2008 was largely due to net out-migration to the rest of Canada. During the first nine months of 2008, 1,954 people moved to the NWT from elsewhere in Canada, while 2,744 left the NWT, a net loss of 790 residents. Net migration into the NWT from outside Canada was positive, resulting in an additional 109 people.

#### ***NWT Population, as of July 1***



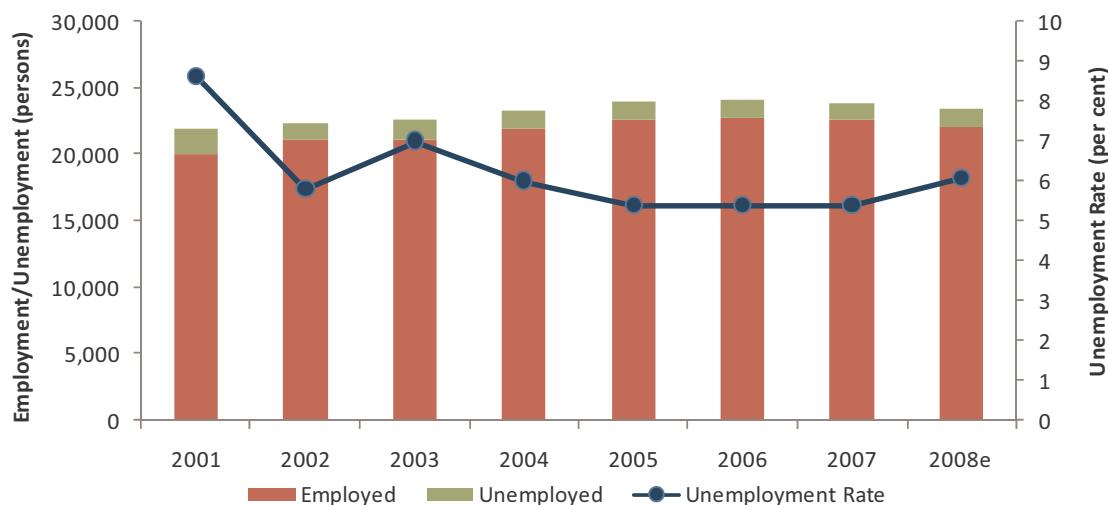
Source: Statistics Canada

### ***Labour***

During 2008, NWT employment declined by 2.4 per cent compared to 2007. Employment averaged 22,100 persons. This represents a labour force (population 15 years of age or older) participation rate of 75.1 per cent, down from 77.9 per cent in 2007.

The NWT's unemployment rate rose to 6.1 per cent in 2008, an increase from 5.7 per cent in 2007, but slightly below the seven-year average of 6.4 per cent.

### Labour Force, Employment and Unemployment



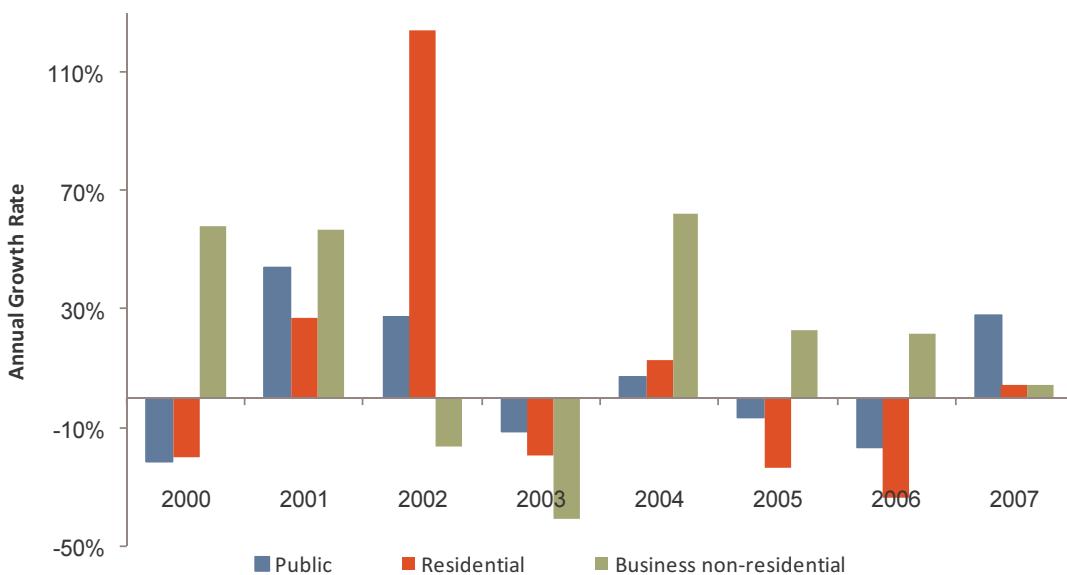
Source: Statistics Canada and NWT Bureau of Statistics

e= estimate

### Investment

Total investment, measured in 2002 dollars, reached \$1.8 billion in 2007, the highest level since Division. This was an increase of \$111 million over 2006, and 50.6 per cent above the 1999 to 2006 average. Business and non-residential investment of \$1.6 billion accounted for almost 90 per cent of total investment in 2007. Investment by governments of \$159 million in 2007, up from \$124 million the previous year, accounted for 8.8 per cent of investment, and residential investment for the remainder. Given completion of the Snap Lake diamond mine during 2007, and the absence of major new investment announcements by the private sector, private sector investment is estimated to decline significantly in 2008 and is forecast to decline in 2009.

### Investment by Source, Annual Growth Rate



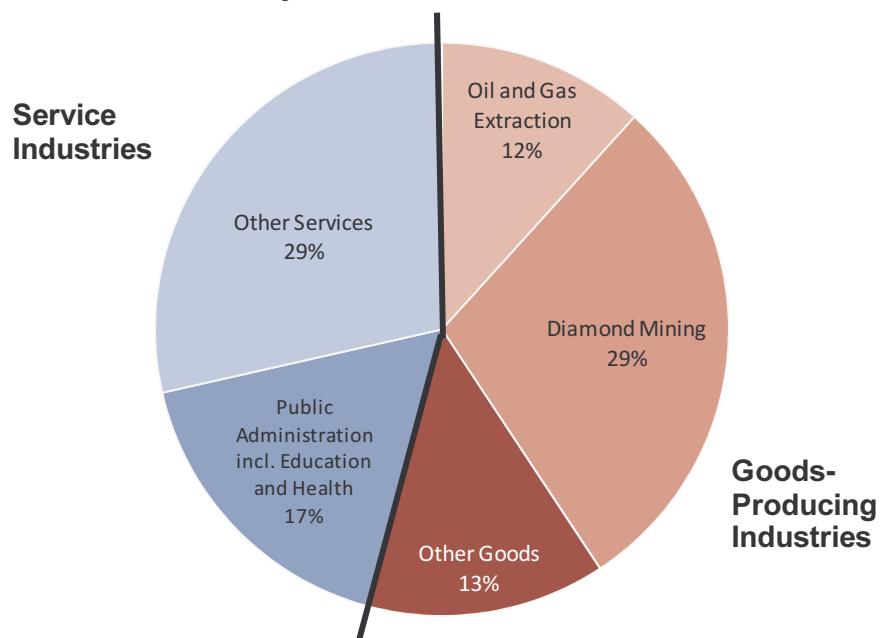
Source: Statistics Canada

## Economic Structure

Goods-producing industries accounted for 54.2 per cent of the NWT economy in 2005 compared to 33.4 per cent nationally. Within the goods-producing sector, the diamond mining industry was responsible for 53.5 per cent of the total value of the sector output. The oil and natural gas extraction industry accounted for 21.6 per cent of the value and the construction industry accounted for most of the balance.

Service industries accounted for 45.8 per cent of the NWT economy compared to 66.6 per cent nationally. The service sector includes a wide range of industries such as wholesalers, banks, real estate, and hotels. The broad public sector is also included in the service sector: schools, hospitals, police and fire services as well as government departments.

### *Structure of the NWT Economy, 2005*



Source: Statistics Canada

## Goods-Producing Industries

Goods-producing industries include diamond mining, oil and gas extraction, fisheries, fur, utilities, construction and manufacturing.

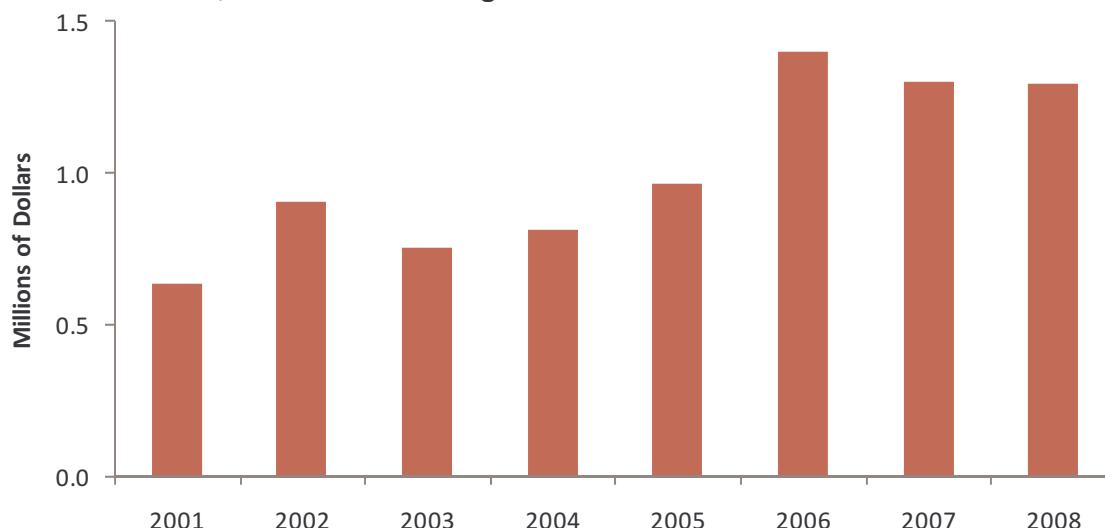
### **Renewable Resources**

Agriculture, forestry, fishing and hunting accounted for less than one half of one per cent of the NWT's 2005 GDP. However, the fur harvest and the fisheries have an important presence in the history of Northerners and a continuing role in their present lives.

### *Fur Harvest*

Trapping remains an important source of cash for many people in the NWT, especially in the smaller communities, and allows for a connection with the land that is not possible with most other occupations. In the fiscal year ending June 30, 2008, the value of fur sales was \$1.3 million, down marginally from 2007.

### ***Value of Fur Sales, Fiscal Year Ending June 30***



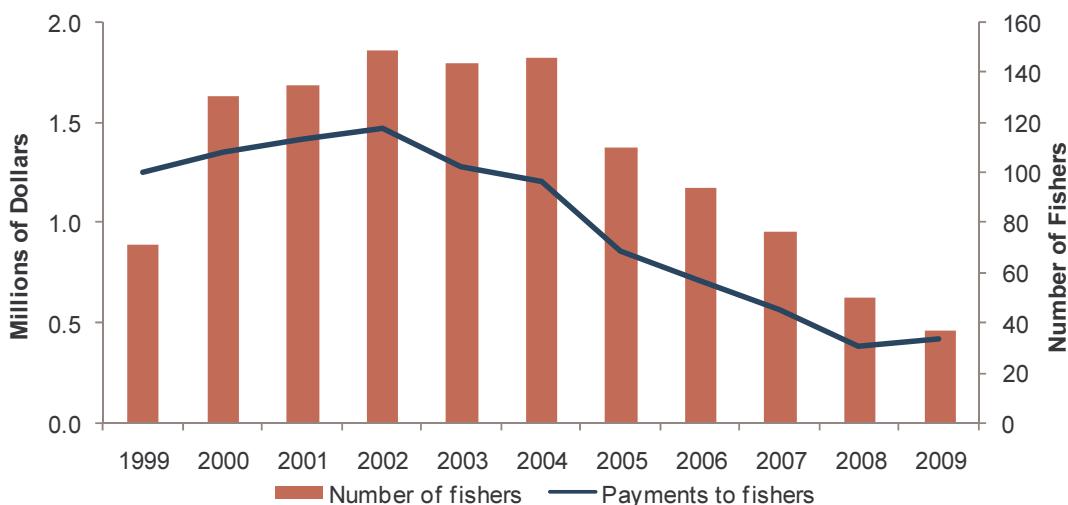
Source: NWT Industry, Tourism and Investment

### ***Commercial Fishery***

The NWT's commercial fishery is a small but valued part of the territory's economy. Data are provided for fish marketed through the Freshwater Fish Marketing Corporation (FFMC) – a self-sustaining federal Crown corporation which functions as the buyer, processor and marketer of freshwater fish that is sold interprovincially and internationally from Alberta, Saskatchewan, Manitoba, the NWT and part of north-western Ontario. The data illustrate that the NWT's commercial fishery marketed through the FFMC has declined since the early part of the decade.

The FFMC reports that initial payments to NWT fishers – on a delivery-point, net-of-freight basis – increased modestly during the fiscal year ending April 30, 2009, reversing the steady decline since 2002. (Note: the export fishery is only active during the summer months; therefore reported NWT results for the fiscal year ending in 2009 are complete because all deliveries and reporting is finalized in the summer months of calendar 2008.)

### ***NWT Export Fishery: Sales and Number of Fishers, Fiscal Year Ending April 30***



Source: Freshwater Fish Marketing Corporation

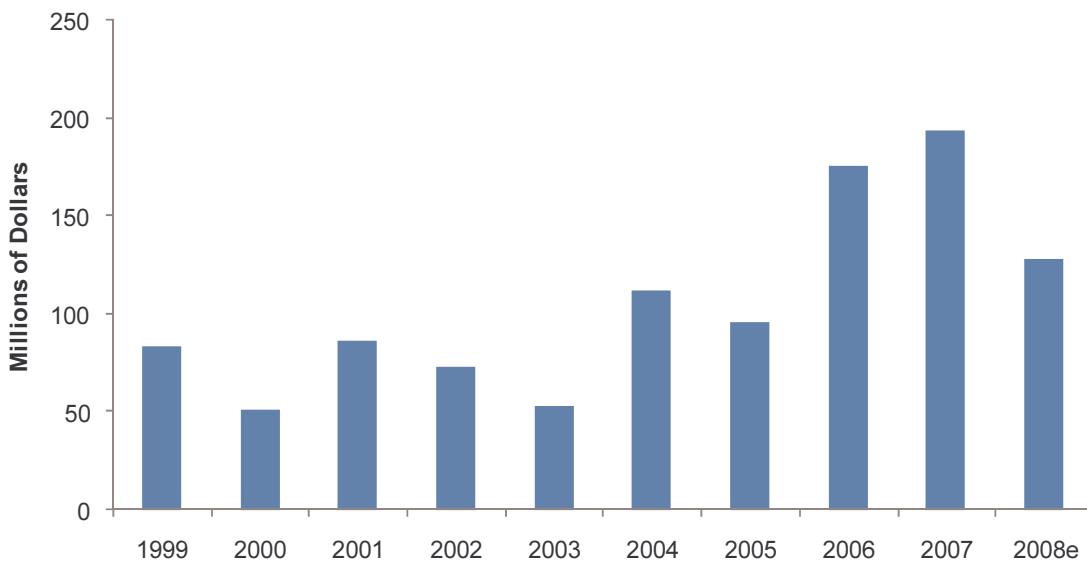
## ***Exploration***

Exploration expenditures include field work, overhead costs, engineering, economic and pre-production feasibility studies, and environment and land access costs. Exploration expenses in 2008 are estimated to be \$128.7 million, down about 34 per cent from 2007, but above the post-Division average of \$108.0 million per year.

During 2008, exploration activity in the NWT focused on diamonds, which accounted for 67.4 per cent of total expenditures. Precious metals were responsible for 14.4 per cent of exploration expenditures, with base metals accounting for 8.2 per cent. Uranium and other metals accounted for most of the balance.

Two proposed mines are currently undergoing environmental assessment, the Tyhee Development Corporation Yellowknife Gold Project and the Canadian Zinc Prairie Creek Mine. The De Beers Canada – Mountain Province joint venture Gahcho Kué diamond mine has completed bulk drilling and is now focused on completion of updated geology and resource models. It is also undertaking a feasibility study that is expected to impact the final design of the project. De Beers has deferred its environmental impact statement pending the results of the feasibility study. There is one additional mineral exploration project undergoing environmental assessment and six exploration projects are waiting for federal Ministerial decision. One oil and gas project is beginning environmental assessment and two projects are waiting for federal Ministerial decision.

### ***NWT Exploration Expenditures***

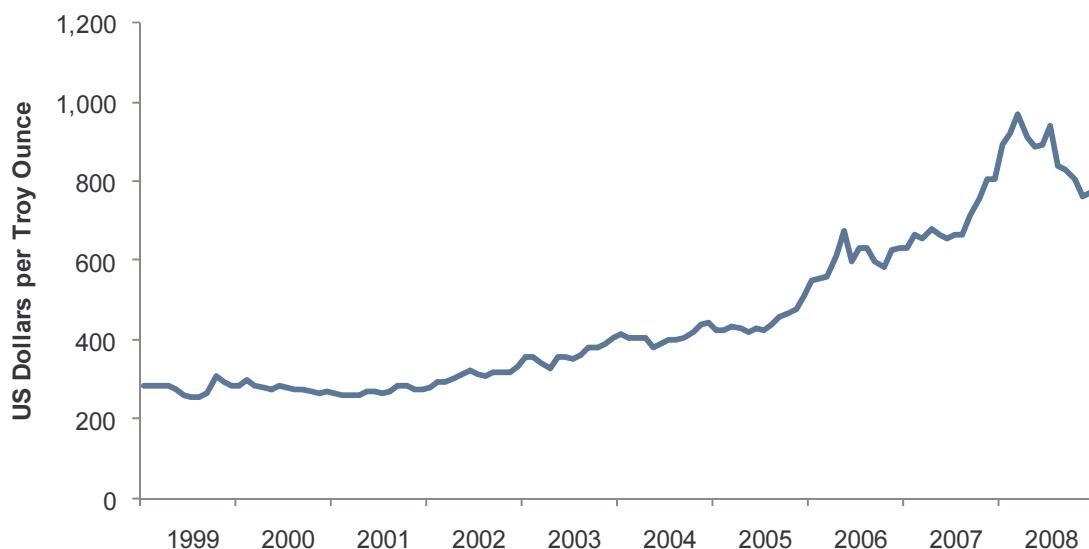


Source: Natural Resources Canada  
e = estimate

## ***Precious Metals***

Precious metals include gold and silver. After many decades of gold mining in the NWT, the territory's two remaining gold mines shut down and there has been no gold production since 2004. However, increases in the price of gold and other precious metals have increased exploration activity.

### Price of Gold



Source: kitco.com

### Diamond Mining

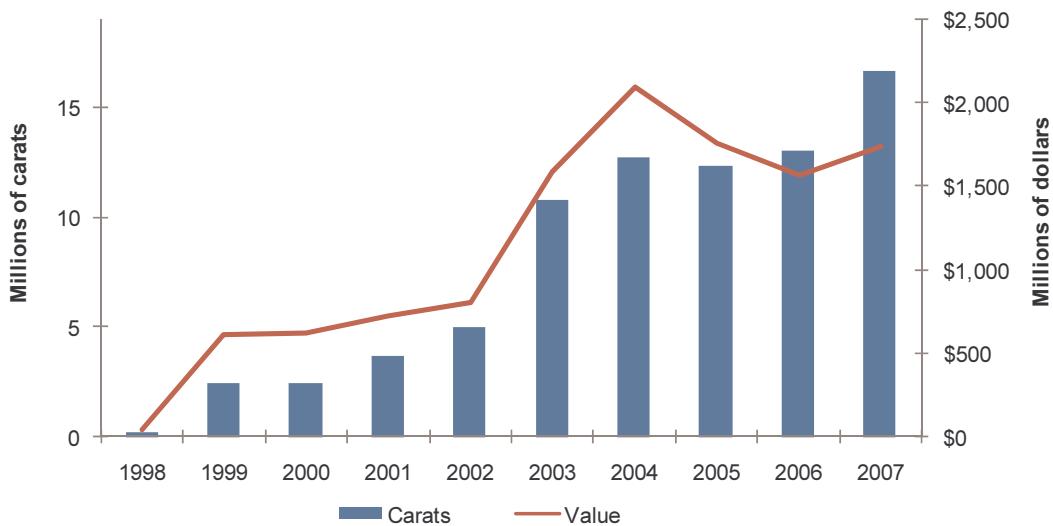
The main economic driver of the NWT economy has been the diamond industry. The Ekati Mine was Canada's first diamond mine when it opened in 1998. Two additional mines have since opened: Diavik in 2003 and Snap Lake in 2008. The environmental assessment process for a potential fourth mine, Gahcho Kué, has been postponed.

Diamond shipments increased during 2007, measured in both volumes and value. The volume of shipments increased 28 per cent to 16.6 million carats. Shipment value increased 11.4 per cent, from \$1.57 billion in 2006 to \$1.75 billion in 2007.

In 2007 Canada remained the third-largest diamond producer by value, behind Botswana and Russia. However, the NWT is no longer the only Canadian jurisdiction with producing diamond mines. During 2008 the Victor Mine began production in Ontario.

Diamond prices are set in the international market, reflecting structured bidding activity and the specific quality attributes of a given diamond – its colour, clarity, cut and carat (weight). At the beginning of 2008, diamond prices were expected to increase modestly over the year. By the end of 2008, the global recession was beginning to have an impact on the world's diamond industry and diamond prices are expected to weaken. In response, Canadian diamond production is expected to decline.

### NWT Diamond Shipments: Weight and Value



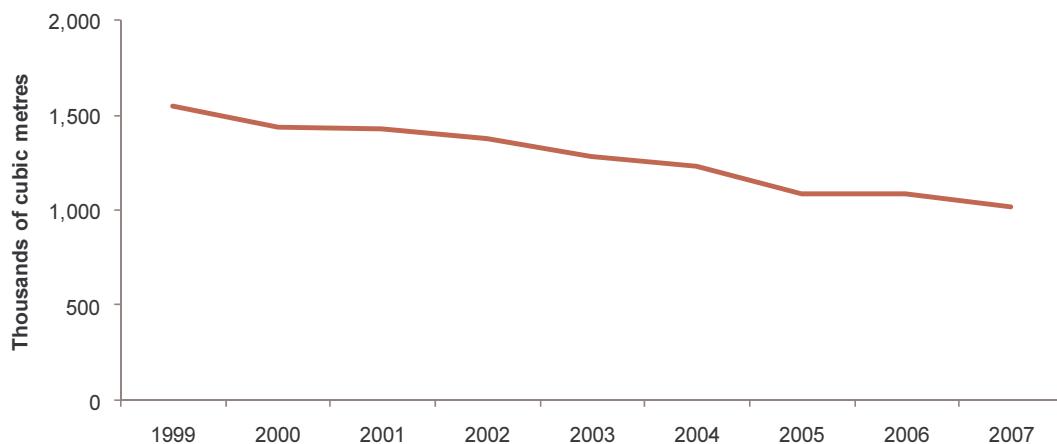
Source: Natural Resources Canada

### The Oil and Gas Sector

Expenditures on oil and gas activities in the NWT in recent years have been sustained at high levels. Expenditures include costs of exploration and development drilling, well completion and abandonment, and geophysical and geological programs. Exploratory drilling levels were sustained in the Mackenzie Delta and in the central Mackenzie Valley.

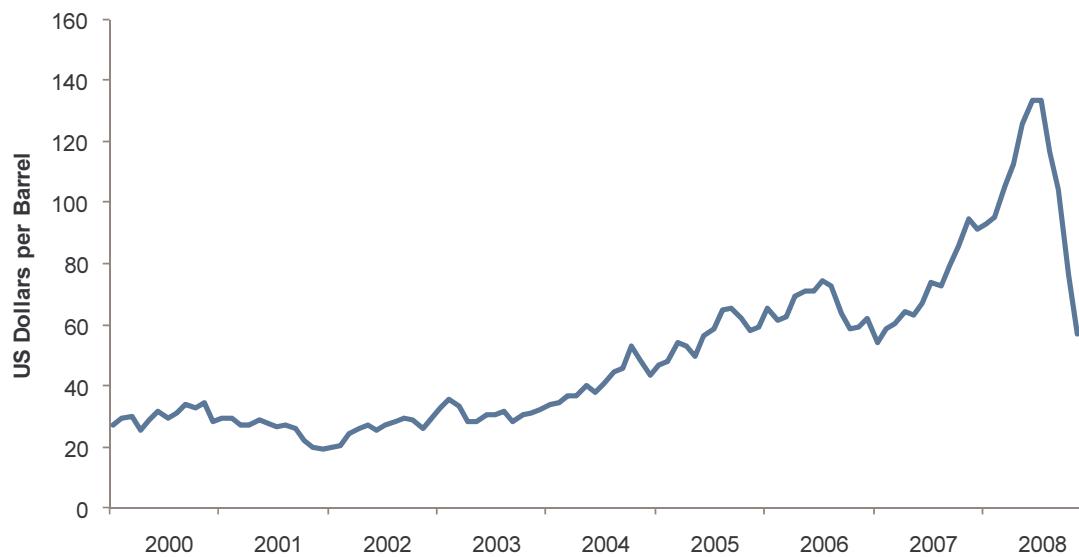
Oil and natural gas production in the NWT has been gradually decreasing due to the depletion of reserves. Growth in production requires new discoveries and new field developments to replace depleted wells. If the Mackenzie Gas Project goes ahead, substantial oil and gas exploration and production is likely to take place in the Mackenzie Delta and Beaufort Sea areas, and could make the NWT a major exporter of energy.

### NWT Crude Oil Production



Source: NWT Bureau of Statistics

### Price of Oil: West Texas Intermediate

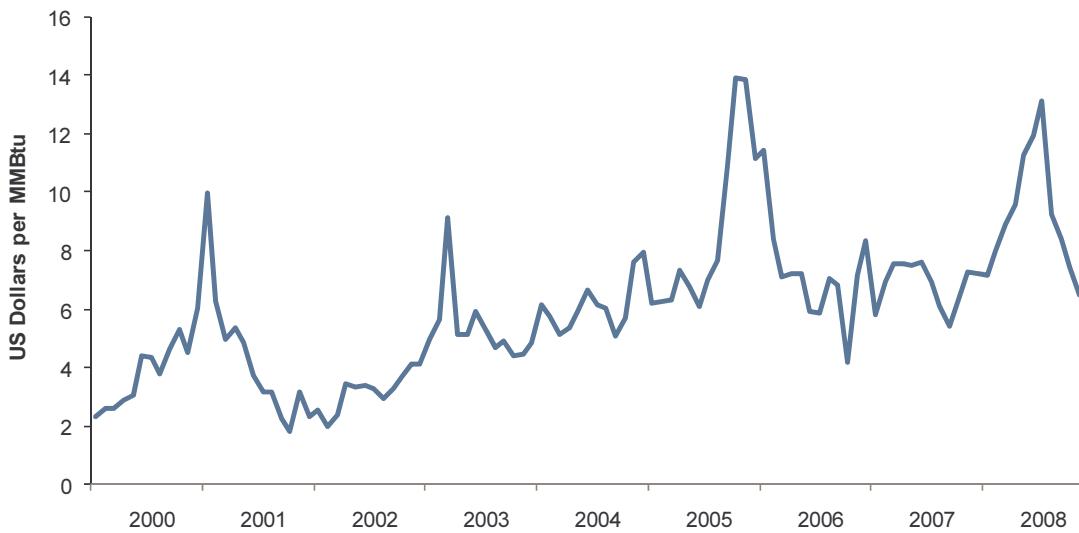


Source: Sproule Associates Limited

Crude oil prices were volatile during 2008. Oil prices peaked at US\$146 per barrel on July 14 before dropping to less than US\$40 per barrel by the beginning of 2009.

Natural gas prices have also exhibited volatility.

### Price of Natural Gas: Henry Hub NYMEX



Source: Sproule Associates Limited

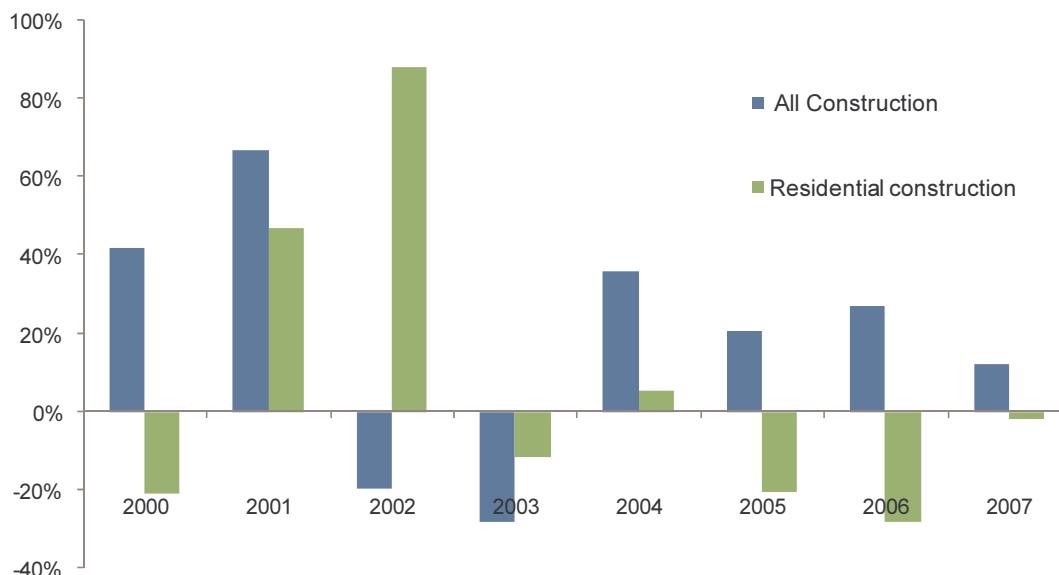
## Construction

The construction industry includes residential construction, non-residential construction, and engineering services. In 2005 construction accounted for 18.5 per cent of NWT GDP. Engineering services include those construction expenditures associated with the development of the diamond mines and investments in the oil and gas industry. Engineering services accounted for an average 87 per cent of the value of construction between 1999 and 2005. Residential and non-residential construction accounted for the remainder.

In 2007, the contribution of all construction activities to the NWT's GDP increased 12.3 per cent over 2006. This was below the average annual growth rate of 19.7 per cent over the eight year period from 1999 to 2007.

The value of residential construction declined slightly for the third year in a row.

### ***Annual Change in the Contribution of NWT Construction Activity to GDP***



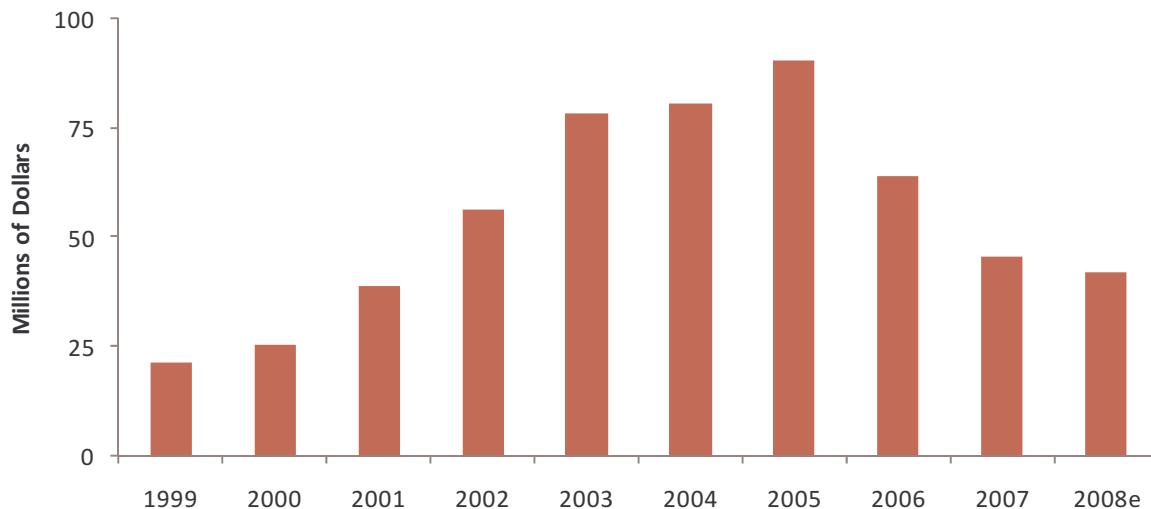
Source: Statistics Canada

## Manufacturing

The NWT's manufacturing sector includes a variety of businesses such as food processors, cement and concrete producers, wood products processors and diamond processors. The NWT manufacturing and trade benefited from strong economic growth prior to 2005 primarily because of the growth in the diamond industry. Much of the NWT's manufacturing shipments consist of cut and polished diamonds. As the number of rough diamonds available for processing in the NWT increased between 1999 and 2005, the NWT's manufacturing shipments also increased.

Since peaking in 2005, manufacturing shipments declined 18.4 per cent in 2006 and 37.7 per cent in 2007. During the first nine months of 2008, manufacturing shipments fell 7.9 per cent below the same period in 2007.

### ***NWT Manufacturing Shipments, All Industries***



Source: Statistics Canada

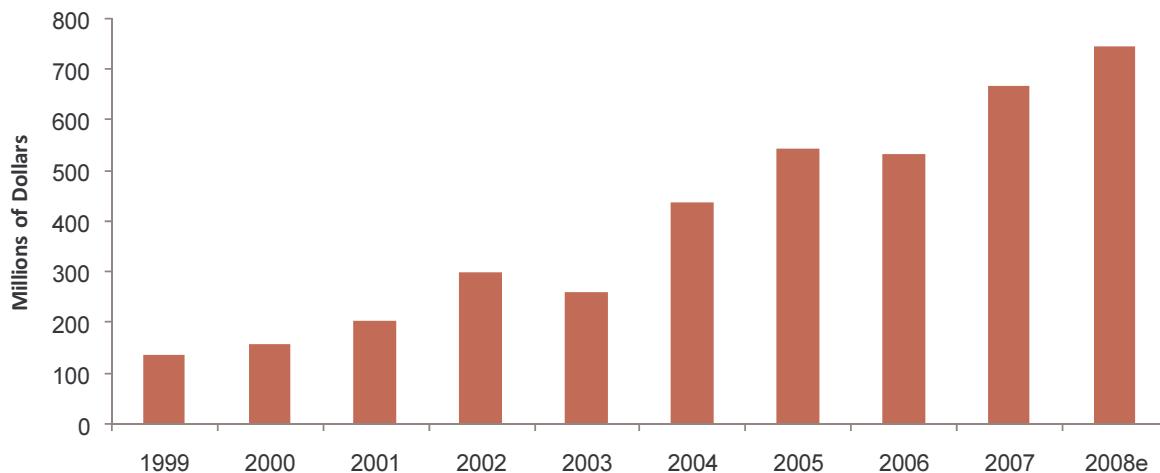
e = estimate

## **Services**

Some service industries are directly related to goods-producing industries, for example transportation and wholesale trade. Other service industries, such as education and health services, support the resident population. Some services attract non-residents to the NWT, earning outside income for territorial residents. The most obvious example is tourism. Only selected service industries are included in the following discussion.

### ***Wholesale trade***

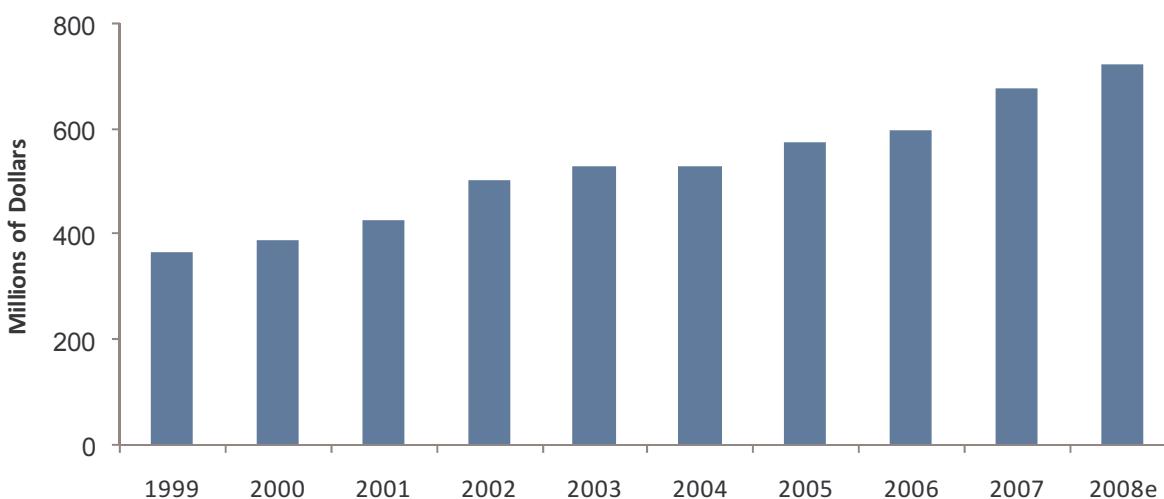
Wholesalers handle the distribution of large quantities of merchandise to retailers, businesses and institutional customers, including the supply of equipment and capital goods. Therefore, the sector is strongly influenced by capital investment and business activity. During the first eight months of 2008, wholesale trade increased by 11.6 per cent over the same period in 2007. If this trend continues for the rest of 2008, wholesale trade will reach \$745 million; more than double the average annual level since Division.

***NWT Wholesale Trade***

Source: Statistics Canada  
e = estimate

***Retail trade***

Retail trade focuses on the final consumer and includes gasoline stations, grocery stores and sporting goods stores as well as the full range of consumer services. Retail trade in the NWT has grown every year since 1999. During the first nine months of 2008, retail sales in the NWT increased by 7.2 per cent over the same period in 2007. This is slightly below the average annual rate of growth since 1999 of 8.0 per cent.

***NWT Value of Retail Trade***

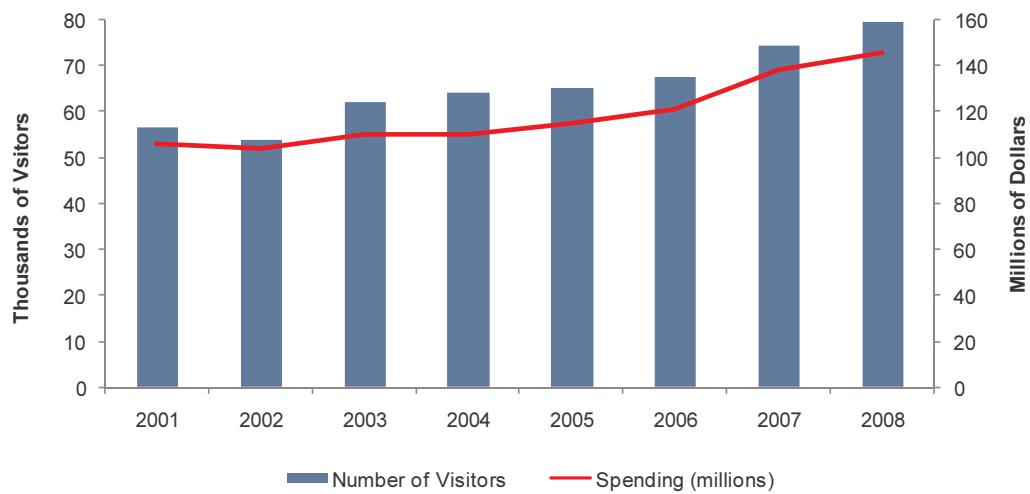
Source: Statistics Canada  
e = estimate

## ***Tourism***

Tourism is an important part of the NWT's economy, with large untapped potential, including niche categories such as cultural tourism, diamond-based tourism and the international tourist market. There are four components to the NWT's tourist trade: eco-tourism, hunting and fishing lodges, leisure travel and business travel.

The number of total visitors increased 2.2 per cent from 74,400 in 2007 to 76,000 in 2008. From 2001 to 2007 the annual rate of growth averaged 4.7 per cent. Total spending by visitors increased 5.3 per cent from 2007 to 2008, reaching almost \$146 million in 2008.

### ***Visits and Expenditures, Fiscal Year Ending March 31***



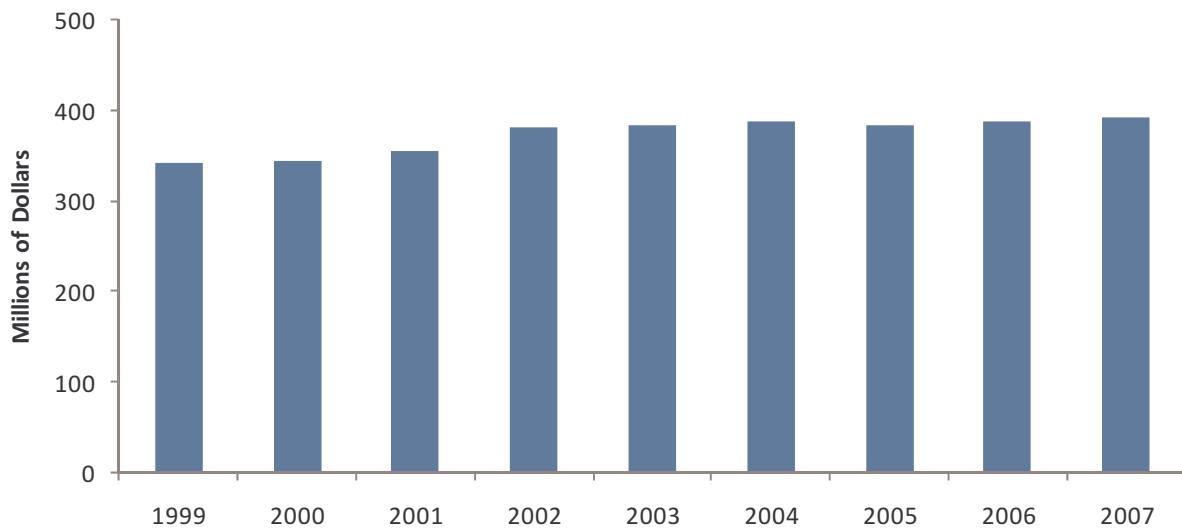
Source: NWT Industry, Trade and Investment

## ***Public Administration***

Public administrative services focus on the NWT resident population. Services include: the courts, policing and correction services, fire protection, defence and public program administration. It includes all levels of government in the NWT: federal, territorial, local, and Aboriginal.

Public administration is measured in terms of its contribution to NWT GDP. This avoids double-counting government expenditures, a particular problem when money is paid from one level of government and spent by another level of government.

Public sector expenditure was stable between 1999 and 2006, growing at an average rate of 1.8 per cent. In 2007, growth slowed to 0.8 per cent relative to 2006.

***Public Sector Expenditures, chained (2002) dollars***

Source: Statistics Canada