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Beyond the STAPLES ECONOMY

By Marc Lee

BC'S ECONOMIC HISTORY IS A classic case of what Canadian economic historian Harold Innis termed a "staples economy"—an economic development model driven by the extraction and export of unprocessed or semi-processed raw materials. Many issues facing the BC economy are rooted in our staples past.

BC's economy has been stagnating for two decades, a period that transcends the tenure of any particular government. There are two negative trends underlying BC's economic stagnation: a slowdown in private and public investment relative to GDP; and a shift in BC's net export performance from a trade surplus to a trade deficit. Both of these factors are connected to BC's resource economy. Exporting natural resources has certainly been a successful strategy historically for BC, but international competition and changing technology make this less effective than it used to be. The provincial government has a role to play in leading a made-in-BC economic strategy that addresses these longer-term structural issues.

A Long View of the BC Economy

BC is a small, resource-dependent economy heavily reliant on the export of basic commodities. While it is true that BC now has a more diversified economy than in the past, this largely reflects the vitality of Greater Vancouver. Many observers have correctly noted that BC has "two economies": the populous and diversified Lower Mainland area (plus the provincial capital of Victoria), and the rest of the province, where resource industries still rule, and changes in export markets and commodity price swings have a great bearing on the fortunes of workers and communities.

While many remember the 1990s as a weak decade in terms of economic performance, this actually reaches back to the 1980s, when there were only three good years of growth out of ten. In contrast, the 1960s and 1970s saw some bad years, but these were well outnumbered by the good.

Figure 1 (see page 2) shows BC's real GDP per capita—the total size of the BC's economic output per person, after accounting for population growth and inflation—over the past 40 years in the form of an index (1961=100). The bulk of growth in real GDP per capita occurred in the first two decades. For the twenty-year period from 1961 to 1981, BC's real GDP per capita increased a total of 78%. But from 1981 to 2001, the total increase was a mere 7%.

This 20-year story of slowdown in the BC economy transcends the tenure of any particular government. It points to structural features of the economy that go much deeper than alleged government mismanagement. Socred governments, NDP governments and now a Liberal government have all presided over this period of relative stagnation in GDP growth.

The Investment Slowdown

The level of investment is a principal driver of economic growth and productivity. The upper line in Figure 2 (see page 2) shows two components of private sector investment: investment in machinery and equipment; and investment in non-residential structures; both as a percentage of GDP.

Beginning in the early 1980s and continuing through the 1990s, there is a general decline in business investment as a share of GDP. By the 1990s, this amounts to a difference of around four percentage points of GDP compared to the 1960s and 1970s. Like trends in GDP growth, the investment slowdown is not just a 1990s story.

Nor has the public sector picked up the slack (the lower line in Figure 2). Although public sector investment is much smaller in magnitude than private sector investment, it has also been on a four-decade declining trend when expressed as a percentage of GDP. This has compounded the decline in private sector investment somewhat, although the

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overall investment slowdown has much more to do with the private sector.

The investment decline translates into a productivity performance that is somewhat lagging other provinces. BC produced about $35 of income for every hour worked in 2001, slightly behind the Canadian average. Ontario creates about $2 more income per hour worked than BC, while Alberta (the highest in Canada) creates about $4 more income per hour than BC. This is a reversal from the early 1980s, when BC was Canada's productivity leader.

Interestingly, when we account for the shares of particular industries in the overall economy, BC's productivity gap vis-à-vis Ontario is mostly accounted for by the different industrial mix. In "like" industries, productivity levels are very similar, but Ontario's economy is characterized more by high-value manufacturing, and less by natural resources, relative to BC's.

Alberta, of course, demonstrates that it is possible to have a prosperous resource economy. Indeed, Alberta is even more resource dependent than BC. But its situation is unique, shaped by substantial oil and gas exports to the US. While BC does produce some oil and gas, our international exports are dominated by wood, pulp and paper products, which together accounted for almost half of our $30.8 billion of exports in 2001. BC will never have the same oil and gas endowment as Alberta. Comparisons to Alberta often presume that BC could replicate Alberta's economic performance by lowering taxes, but low taxes are the consequence of a boom in oil and gas exports that reap windfall revenues for government—not their source.

BC's Trade Deficit

The BC economy as a whole is less reliant on resources as a share of GDP than in the past, but when it comes to

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Figure 1: Index of BC Real GDP Per Capita, 1961-2001 (1961=100)

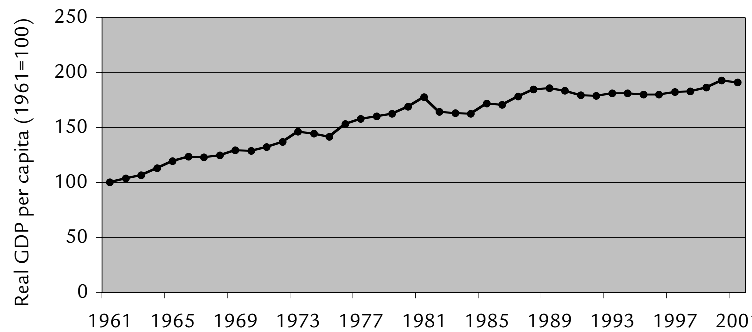


Figure 2: Public and Private Investment as a Share of GDP, 1961-2001

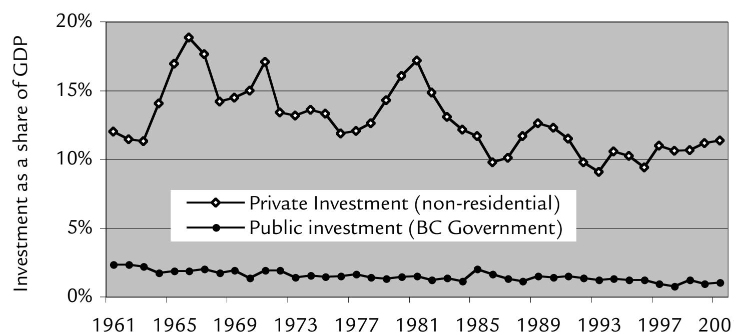
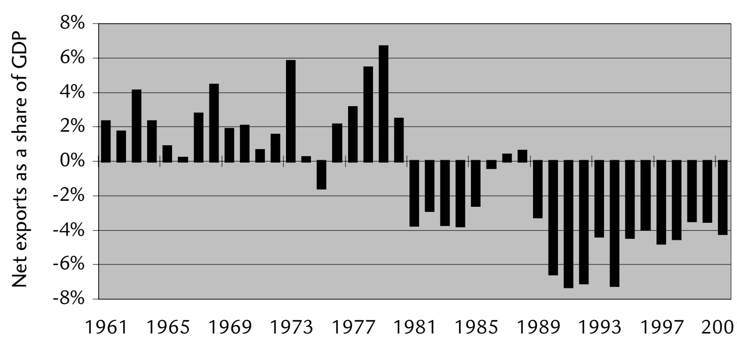


Figure 3: BC Net Exports (International and Interprovincial) as % of GDP, 1961-2001



Source for Figures 1–3: CCPA calculations based on BC Stats, BC Economic Accounts

BC Exports Raw Logs, Jobs and Revenue

By Dale Marshall

Raw log exports are going to leave BC in higher volumes over the next three years. That's because the BC government, in February 2001, passed an Order-in-Council authorizing an additional 2.7 million cubic metres of raw log exports. The increased exports are to come from the battered North Coast, an area already reeling from declines in its salmon fishery and forestry sector.

And yet, the issue of raw log exports is a no-brainer. If we're going to allow our public forests to be cut, then let's make sure that we get substantial economic gains in return. These gains go beyond profits for forest companies or revenues for the provincial government and include what is, for the majority of people, most important: jobs. Creating as many good jobs as possible from our limited forestry resources means processing BC's timber here in BC.

This is the simple logic behind a *Forest Act* regulation that restricts the export of unprocessed timber from public land. It is good public policy. It does, however, allow raw log exports under certain conditions, the two most important being that it would be "uneconomic" to process the logs in BC, or that the logs were surplus to the milling capacity of the province.

Unfortunately, these loopholes have been used to increase the volume of raw logs leaving the province. From 1997 to 2001, exports have increased more than tenfold. Though exports from private land are partly responsible for the increase, raw logs are leaving our public forests in greater volumes than ever before. Almost 1.2 million cubic metres of raw logs were exported from public forests in 2001.

If BC were to do nothing more than run these logs through sawmills and pulp mills, the province would have 800 more jobs in its forestry sector, bringing $54 million in wages and benefits to forest-dependent communities every year. Many more jobs could be created if we moved up the value chain and created the same level of employment (per cubic metre of wood) as the US, Scandinavia, or even Eastern Canada.

Instead, even fewer jobs will be created from forestry in BC. The Order-in-Council will allow increased raw log exports of about 900,000 cubic meters annually. This represents the loss of a further 700 full-time jobs—all in exchange for a mere $2.7 million in stumpage paid to the government in lieu of employment. Added to lost jobs from existing raw log exports, as many as 1,500 jobs are being sacrificed.

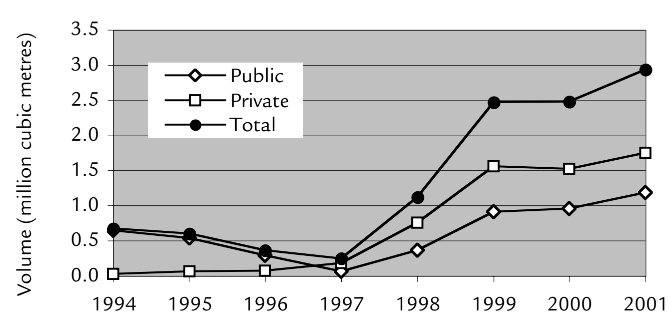
Incredibly, the provincial government's official reason for the increased log exports is a lack of milling capacity in the province. All evidence, and common sense, points to a different conclusion: that BC has milling *overcapacity*. In fact, just three months before the Order-in-Council, forestry analyst Peter Pearse delivered his commissioned report to the government. Its conclusion: eight to sixteen mills would have to close in the foreseeable future because there wasn't enough wood to sustain them. Over the last two years, Weyerhaeuser, Western Pulp, and Doman, among others, have complained about inadequate fibre supply and temporarily closed mills.

Not surprisingly, the government's decision has brought criticism and action from the people of the province. A coalition of forestry unions and environmental groups have hired Sierra Legal Defense Fund to fight the Order-in Council in court.

It didn't have to be this way. Forest Minister Mike de Jong has defended the government's action, saying it was necessary in order to keep jobs for loggers. But real government help for forest industry workers would consist of incentives for forest companies to move up the value chain instead of down. The Minister's short-term "solution" has not been matched by a long-term strategy to do that. It should also be diversifying forest tenures to include communities and First Nations, who are often more willing than transnational corporations to operate in an environmentally sensitive way and make the most of a renewable, but finite, resource.

Dale Marshall is Resource Policy Analyst for the BC office of the Canadian Centre for Policy Alternatives and author of a recent policy brief, Down the Value Chain: The Politics and Economics of Raw Log Exports*, available at www.policyalternatives.ca.*

Raw Log Exports in BC (1994-2001)



Source: BC Ministry of Forest, 1995-2002.

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exports, resources are still dominant. Adding together all resource sectors—forestry, agriculture, fish products, minerals and energy—some 77.8% of BC exports are from natural resources. Fortunately, BC has made some gains. In 1992, the share of exports from natural resources was 86.4%. And within the sub-categories of resource products, value-added exports have gained ground. For instance, value-added wood products now comprise 3.1% of total exports, up from 1.8% in 1992. While it is notable that BC has diversified its export base and is adding more value to its exports in certain areas, commodity exports still comprise the lion's share of exports.

Where this becomes particularly problematic is when BC's overall trade position is considered—both international and interprovincial. Figure 3 shows that through the 1960s and 1970s BC had a consistent trade surplus (exports in excess of imports) averaging 2.4% of GDP. This began to reverse in the 1980s. From 1981 to 2001, BC had a trade deficit averaging 3.8% of its GDP, a large and troubling turnaround.

The biggest factor behind the trade deficit is a steady increase in imports from other countries relative to GDP, while BC's exports to other countries have remained relatively steady at around 30% of GDP. BC still maintains a small surplus on *international* trade, but this is more than offset by a large deficit on *interprovincial* trade.

The roots of the problem go back to the composition of BC trade: we are still a staples economy that tends to export raw materials and commodities, while importing manufactured goods and capital equipment. And BC's resource exports now command a lower price on international markets. Whereas Ontario has weaned itself from natural resources in favour of manufactured goods, BC continues to follow a development strategy more common to the Third World than the First.

While trade and the resource sector will continue to be important for the province, we must increase the value created from BC's resource harvest, we must accelerate diversification, and we must seek to produce more at home of what we currently import. The role of the provincial government should be to facilitate this structural change, while protecting and helping communities through the transition.

Towards a Made-in-BC Economic Strategy

The government's strategy—tax and spending cuts, privatization and deregulation, and the Olympics—is more of a leap of faith than a compelling plan for BC's future. In spite of all the rhetoric about "making BC open for business" there is no evidence that such strategies actually work—that they deliver the type of investment desired, or that they are worth the inevitable trade-offs in social and environmental protections.

BC needs to be much more creative in developing an investment strategy, and must seek a made-in-BC approach, not some off-the-shelf, one-size-fits-all imported one. It must address the growing gap between the "hinterland" and the Lower Mainland, and must seek to further diversify the BC economy. This means getting beyond the resource mindset that permeates the province's business culture. And it has to be a multifaceted strategy that moves BC up the value chain and promotes investment.

A number of key areas should form the basis of a made-in BC strategy:

- We need to use the tax system creatively—designing carrots and sticks that encourage investment, production and employment, and that meet other social and environmental objectives—not give blank cheques via tax cuts to corporations.
- A public investment bank should be created to provide seed funding for new and innovative economic areas, where private sector financing is less likely to be forthcoming. Such a bank could also focus on innovative investments in the resource sector and alternative energy.
- We need a bold and comprehensive strategy for the resource sector based on adopting new environmentally-friendly technologies and moving up the value chain, thereby providing resource-dependent communities with both economic stability and environmental sustainability.
- Public investments and infrastructure development based on fundamental and existing needs should be prioritized. The emphasis should be on long-term care facilities, public transit, social housing and child care facilities—not Olympic circuses.

Economic growth is important but it has to be sustainable and equitable. BC is still a wealthy province, and is starting from a privileged position. But there is much work that desperately needs doing. Government cannot just sit on the sidelines; it must lead an economic strategy that is active and deliberate.

Marc Lee is the CCPA–BC's Economist, and Editor of BC Commentary. This piece is an excerpted version of material presented in the CCPA's 2003 BC Solutions Budget*, available at www.policyalternatives.ca.*

BC Commentary is produced by the BC Office of the Canadian Centre for Policy Alternatives. Editor: Marc Lee; Layout: Shannon Daub
1400–207 West Hastings Street • Vancouver • BC • V6B 1H7 • Tel: (604) 801-5121 • Fax: (604) 801-5122 • info@bcpolicyalternatives.org

www.policyalternatives.ca