

Section 1

Review of the Economic Situation in 2000 and Outlook

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Review of the Economic Situation in 2000 and Outlook

This section presents the highlights of the economic situation in Québec in 2000 as well as the economic outlook used to prepare the Budget Plan.

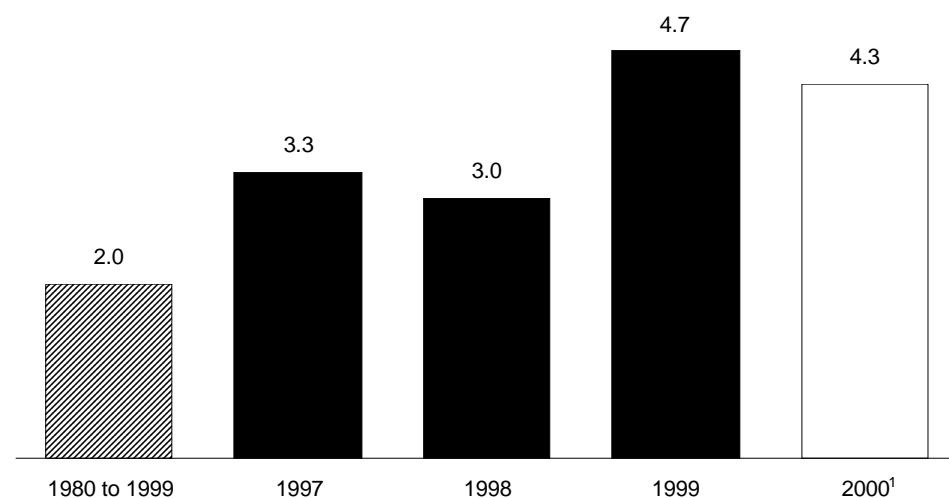
The economic situation in 2000

Fourth consecutive year of robust economic growth

Thanks to strong domestic and foreign demand, the Québec economy followed the same trend as in recent years, growing by 4.3% in 2000, twice the average rate observed between 1980 and 1999. Following the excellent performance in 1999, when real GDP reached 4.7%, in 2000 Québec posted its second strongest economic growth in 12 years.

GRAPH 1.1

CHANGE IN QUÉBEC REAL GDP (annual percentage change)



1 Preliminary result.

Sources: Institut de la statistique du Québec, Conference Board of Canada and ministère des Finances du Québec.

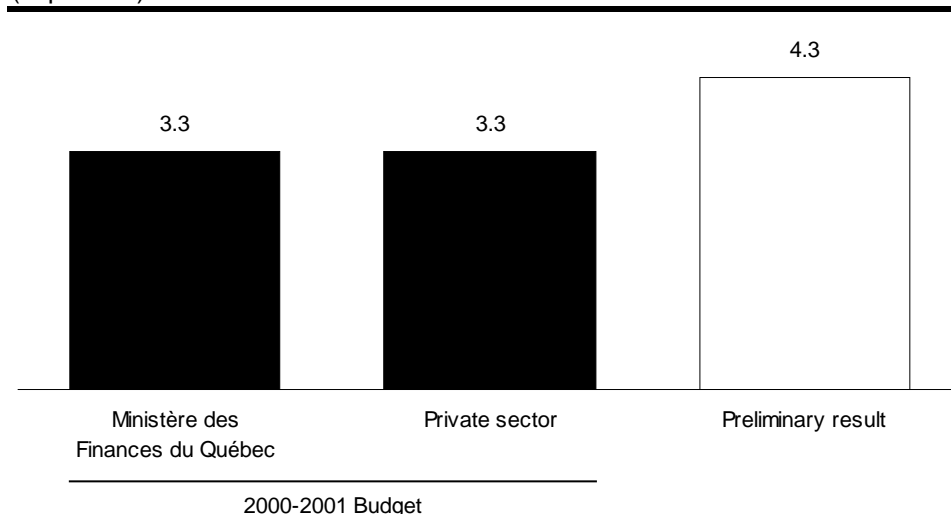
Domestic demand was up 5.0% last year due to a marked 15.7% increase in business non-residential investment. This is the strongest upswing in domestic demand in 15 years. Foreign demand also contributed significantly to Québec's economic growth, with international exports of goods rising by 12.2%. However, the net contribution of the foreign sector to real GDP growth was attenuated by the sharp increase in imports (11.1%).

The economic performance in 2000 was better than projected by most private forecasters a year ago.

The rise in real GDP outpaced the forecasts used to prepare the 2000-2001 Budget Plan by approximately one percentage point, creating 10 000 more jobs than expected. This outcome is attributable to the stronger-than-anticipated U.S. economy and the exceptional increase in investments.

GRAPH 1.2

GROWTH IN QUÉBEC REAL GDP IN 2000 (in percent)



Sources: Institut de la statistique du Québec and ministère des Finances du Québec.

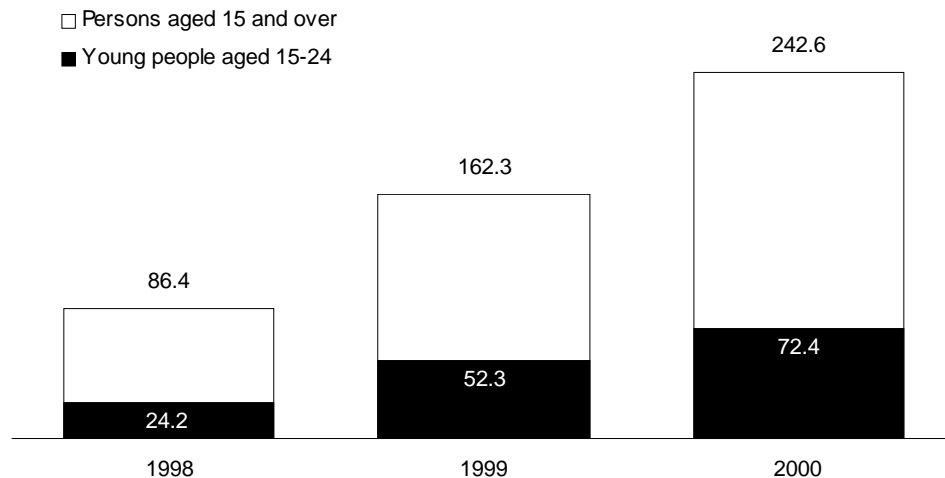
Positive spin-offs for the labour market

The robust growth in Québec's economy in recent years led to a substantial improvement in labour market conditions. On an annual basis, over 80 000 new jobs were created in Québec last year. This is the strongest performance recorded since the late 1980s, after that observed in 1998. Some 243 000 jobs have been created since 1997, nearly all full-time positions (232 000). Such strong job creation over a three-year period had not been seen since the mid-1980s.

For the third year in a row, job creation largely benefited young people, who obtained one quarter of all new jobs created in Québec even though they account for only 16% of the working-age population. In the past three years, nearly 30% of all new jobs have gone to young people aged 15-24.

GRAPH 1.3

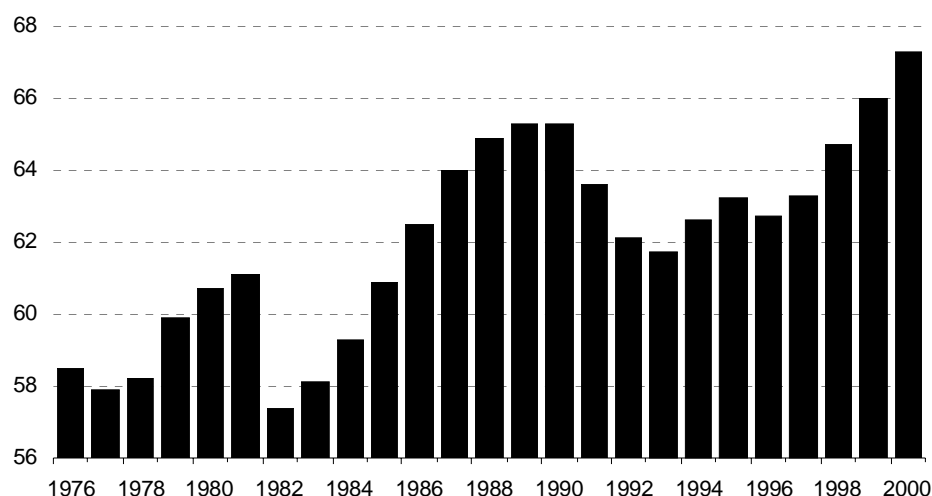
NUMBER OF JOBS CREATED SINCE 1997
(in thousands)



Source: Statistics Canada.

The employment rate for persons aged 15-64, i.e. the proportion of persons in this age group who are gainfully employed, climbed considerably in 2000. Already at a peak in 1999, the employment rate for the 15-64 age group gained another 1.3 percentage points to reach 67.3% in 2000.

GRAPH 1.4

EMPLOYMENT RATE FOR PERSONS AGED 15-64
 (in percent)


Source: Statistics Canada.

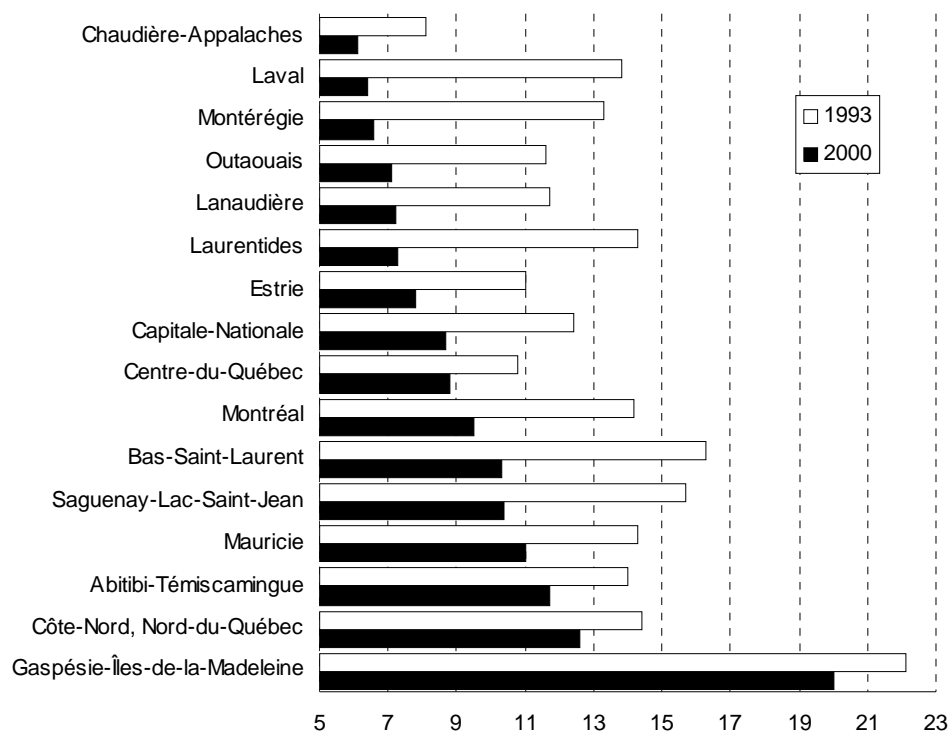
Furthermore, despite the increase in the labour force participation rate from 62.8% in 1999 to 63.2% in 2000, the unemployment rate fell to its lowest level in 25 years, averaging 8.4% in 2000. It has dropped by five percentage points since its cyclical peak in 1993.

Compared with 1999, the unemployment rate declined in nearly all of Québec's administrative regions in 2000. The largest decreases were recorded in the regions of Laval (-1.8% to 6.4%), Côte-Nord and Nord-du-Québec (-1.8% to 12.6%), Lanaudière (-1.7% to 7.2%), Abitibi-Témiscamingue (-1.7% to 11.7%) and Montérégie (-1.6% to 6.6%).

These decreases continue the trend observed since 1993. In fact, the unemployment rate has fallen significantly in all of the regions over this period.

GRAPH 1.5

UNEMPLOYMENT RATE IN QUÉBEC BY ADMINISTRATIVE REGION (in percent)

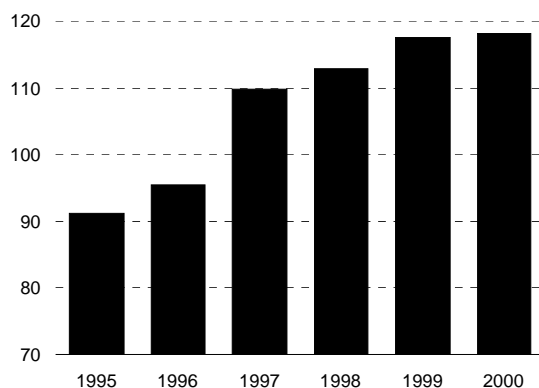


Source: Statistics Canada.

Strong domestic demand

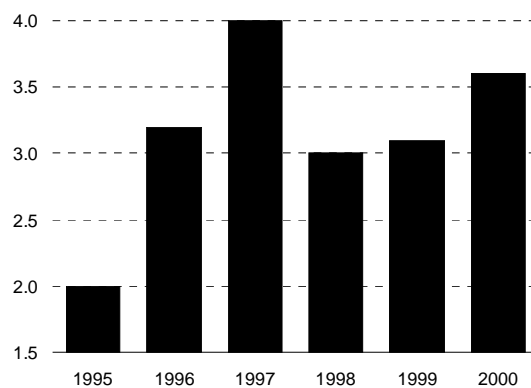
The continued improvement of labour market conditions coupled with the personal income tax reductions sustained the high level of household confidence in Québec, which posted its highest annual rate in 12 years. This confidence resulted in a 3.6% jump in real consumer spending by Québec households in 2000, the largest annual increase since 1988, except for 1997 (4.0%).

GRAPH 1.6

CONSUMER CONFIDENCE INDEX
(1991 = 100)

Source: Conference Board of Canada.

GRAPH 1.7

REAL CONSUMER SPENDING
(percentage change)

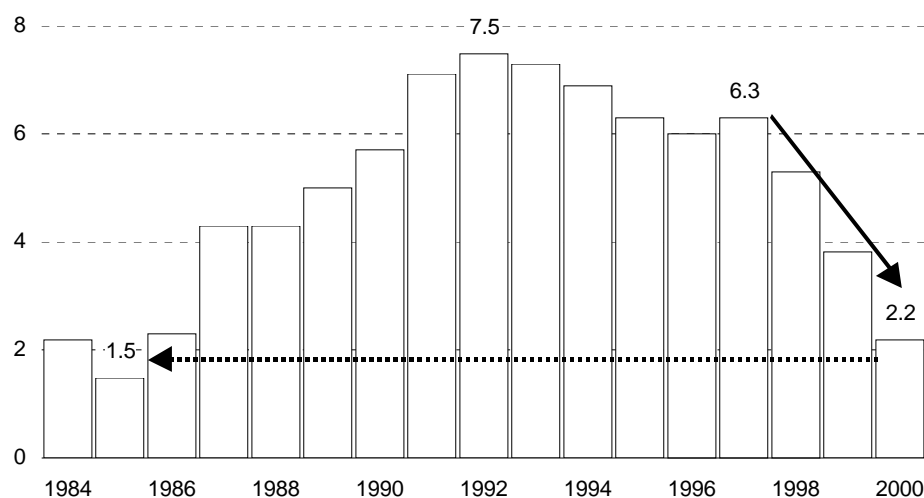
Sources: Institut de la statistique du Québec and ministère des Finances du Québec.

While household consumer spending rose substantially in 2000, residential investment was sluggish, posting only 2.0% real growth due to a decline in new housing construction. The drop in housing starts from 25 700 units in 1999 to 24 700 in 2000 translated into a 5.7% decline in investment in new construction. On the other hand, real estate commissions were up 7.9% and spending on renovations, 6.9%.

The decline in housing starts in 2000 masks a major improvement in new-housing market conditions. Following a long period of market imbalance, balance was finally restored to the rental-housing sector. Montréal, for example, boasts a vacancy rate of only 1.5%, one fifth the 1993 rate of 7.7%. The vacancy rate has also declined for Québec as a whole, dropping from 3.8% in 1999 to 2.2% in 2000, the lowest level since 1985 (1.5%). Had it not been for resolving the imbalance, housing starts in Québec would have been higher in 2000.

GRAPH 1.8

RENTAL HOUSING VACANCY RATE IN QUÉBEC (in percent)



Sources: Canada Mortgage and Housing Corporation and ministère des Finances du Québec.

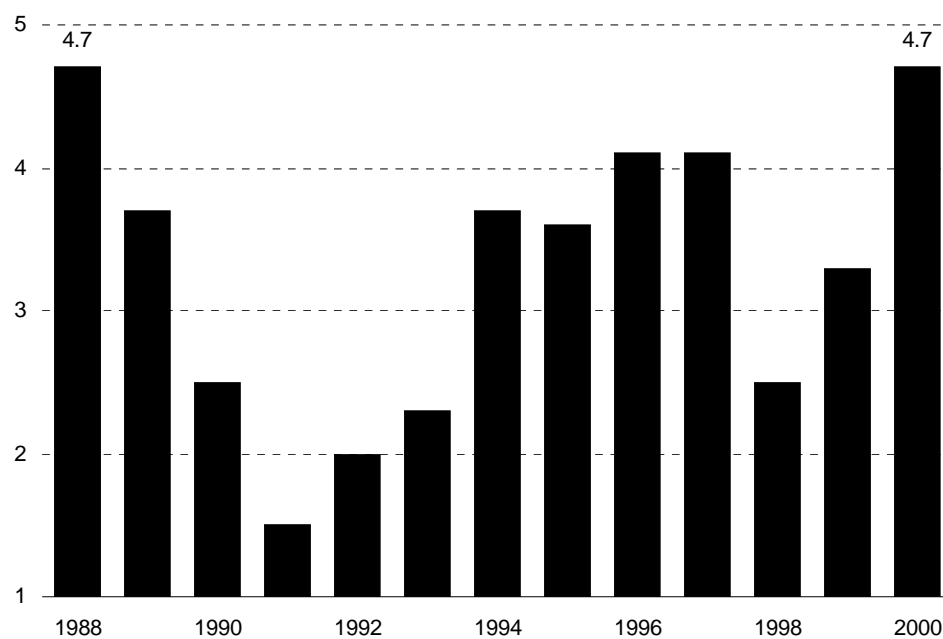
Enterprises also benefited from the favourable economic setting. Increased demand and higher profits encouraged Québec enterprises to expand and modernize their production facilities in 2000. As a result, business non-residential investment rose by 15.7% in real terms, the strongest growth observed since 1987. Purchases of machinery and equipment posted the most substantial gains, at nearly 20%.

Expanding world economy

In 2000, the Québec economy continued to benefit from an external environment that was favourable to trade. According to the International Monetary Fund (IMF), the world economy grew at a rate of 4.7% in 2000, the strongest annual growth in 12 years. The vitality of the world economy is attributable to the rapid economic recovery in several Asian countries and the exceptionally robust economy in the United States.

GRAPH 1.9

WORLD REAL GDP GROWTH (in percent)



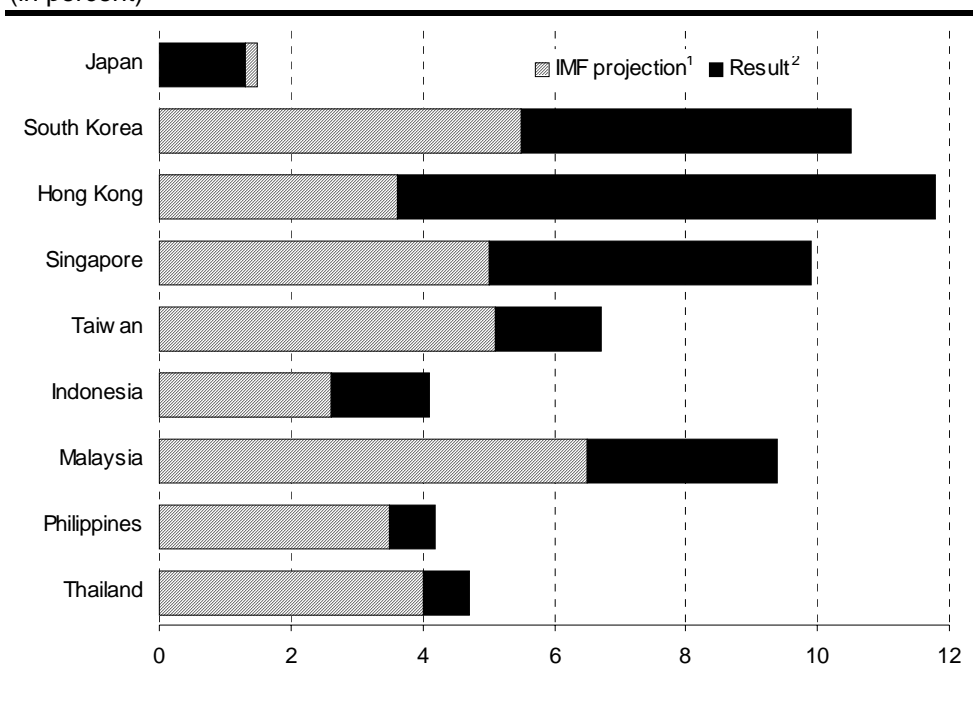
Source: International Monetary Fund, October 2000.

Sustained economic expansion in Asia

Economic growth in emerging Asian countries was better than expected last year, owing primarily to two factors:

- a more dynamic foreign demand stimulated exports to Europe and the United States; and
- the rise in oil prices was beneficial for producing countries (Indonesia, Malaysia, Singapore).

GRAPH 1.10

GROWTH IN REAL GDP IN 2000 – VARIOUS ASIAN COUNTRIES
 (in percent)


1 International Monetary Fund projection in October 1999.

2 Result for the first three quarters of 2000.

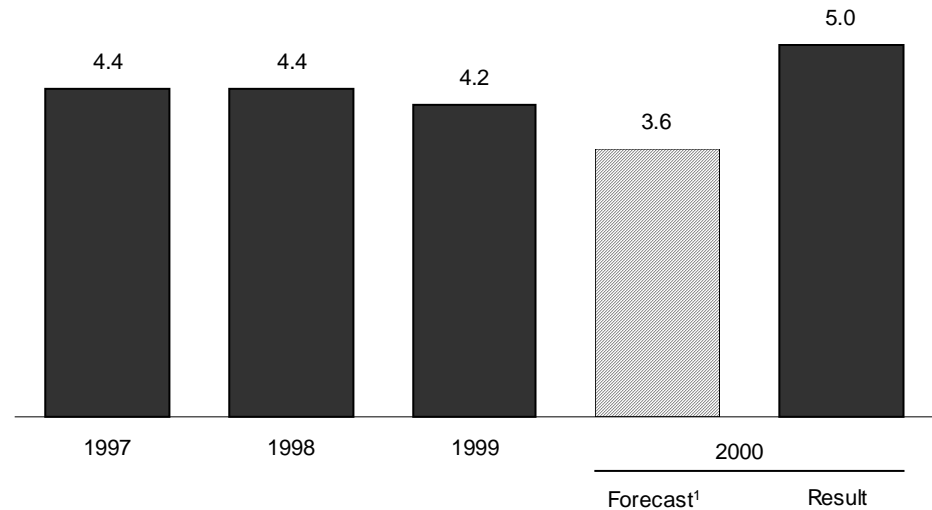
Sources: International Monetary Fund and Datastream.

In Japan, on the other hand, the economic situation remained fragile. Low private consumption and major structural problems caused by the high public debt, restructuring by businesses and an aging population continued to cripple the country's economy. As a result, the unemployment rate remained relatively high in 2000, at 4.7%.

Another outstanding year for the U.S. economy

Marking the tenth year of expansion, economic activity grew by 5.0% in the United States in 2000, nearly one and a half percentage points higher than projected by American forecasters a year ago. For the fourth consecutive year, the United States saw its economy expand by over 4%.

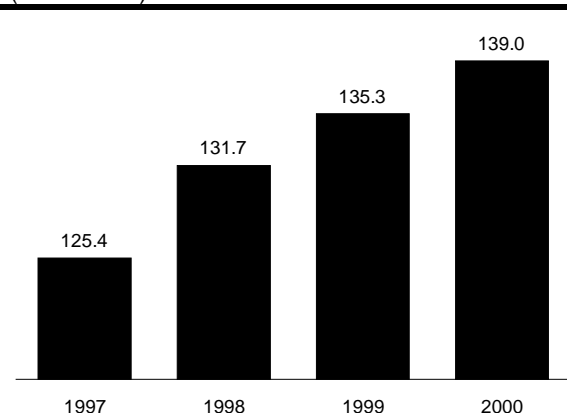
GRAPH 1.11

REAL GDP GROWTH – UNITED STATES
(in percent)

1 At the time of the 2000-2001 Budget.
Source: Standard & Poor's *DRI*.

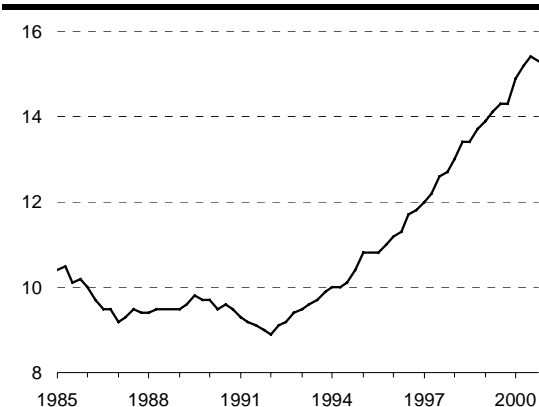
This economic growth was led by the steady climb in consumer spending, which was up 5.3% in 2000 due to the continued high level of confidence among American consumers. The unemployment rate reached 3.9% in September and October of last year, the lowest level since January 1970 (3.9%). Thanks to this full-employment economy, enterprises continued to invest heavily, especially in new technologies.

GRAPH 1.12

CONSUMER CONFIDENCE INDEX – UNITED STATES
 (1985 = 100)


Source: Standard & Poor's DRI.

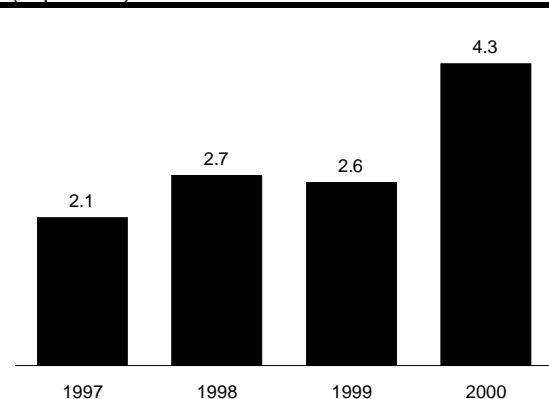
GRAPH 1.13

INVESTMENT RATIO – UNITED STATES
 (as a percentage of the GDP)


Source: Standard & Poor's DRI.

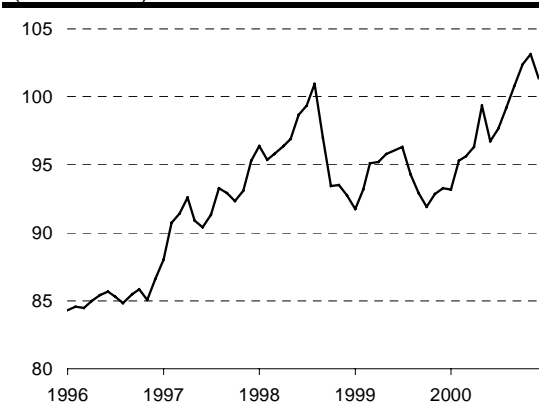
Due to significant gains in productivity and the strong American dollar, inflationary pressures remained under control in the United States. Growth in the consumer price index (CPI) for commodities other than food and energy rose slightly, from 2.1% in 1999 to 2.4% in 2000. The overall inflation rate climbed even more, to 3.4%, owing to the sharp increase in oil prices (57%).

GRAPH 1.14

GROWTH IN LABOUR PRODUCTIVITY – UNITED STATES
 (in percent)


Source: Standard & Poor's DRI.

GRAPH 1.15

TRADE-WEIGHTED EXCHANGE VALUE INDEX OF THE US DOLLAR¹
 (1973 = 100)


1 Relative to the currency of 7 of the United States' main trading partners.

Source: Standard & Poor's DRI.

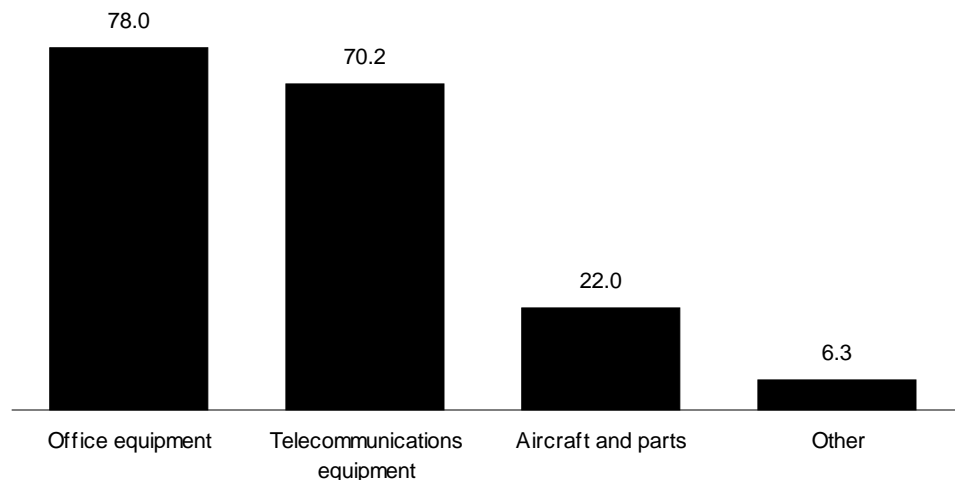
Strong growth in Québec's international exports of goods

Benefiting from growing world demand and a weak Canadian dollar, international exports of goods posted another year of solid growth. The volume of exports was up by 12.2% in 2000, the highest increase since 1994.

This sharp rise is primarily attributable to the successful showing of Québec high-tech products on international markets. In 2000, exports of office, telecommunications and transportation equipment accounted for over two thirds of the increase in Québec's international exports.

GRAPH 1.16

GROWTH IN QUÉBEC'S INTERNATIONAL EXPORTS OF GOODS¹ IN 2000 (in percent)



¹ Data on customs basis.

Source: Institut de la statistique du Québec.

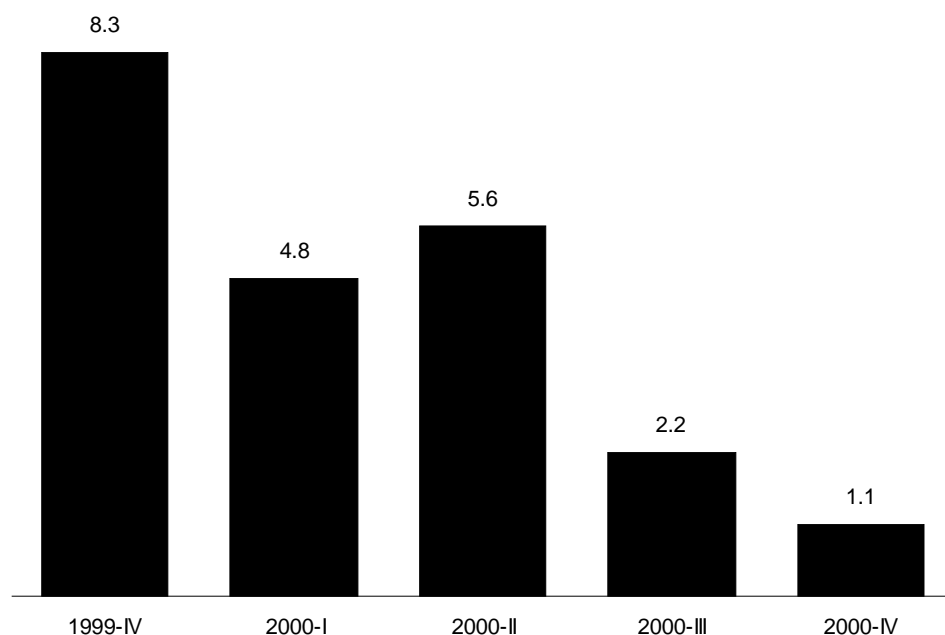
Economic outlook for Québec in 2001

Slowdown in economic growth in the United States

Despite 5.0% annual growth in 2000, the U.S. economy slowed down considerably in the second half of the year owing to the tightening of monetary conditions, the rise in energy costs, the downturn in stock markets and the decline in automobile sales. Whereas the annualized growth rates were 4.8% and 5.6% in the first and second quarters of 2000, respectively, U.S. real GDP rose by only 2.2% in the third quarter and by 1.1% in the fourth quarter.

GRAPH 1.17

ECONOMIC GROWTH – UNITED STATES (annualized rate in percent)



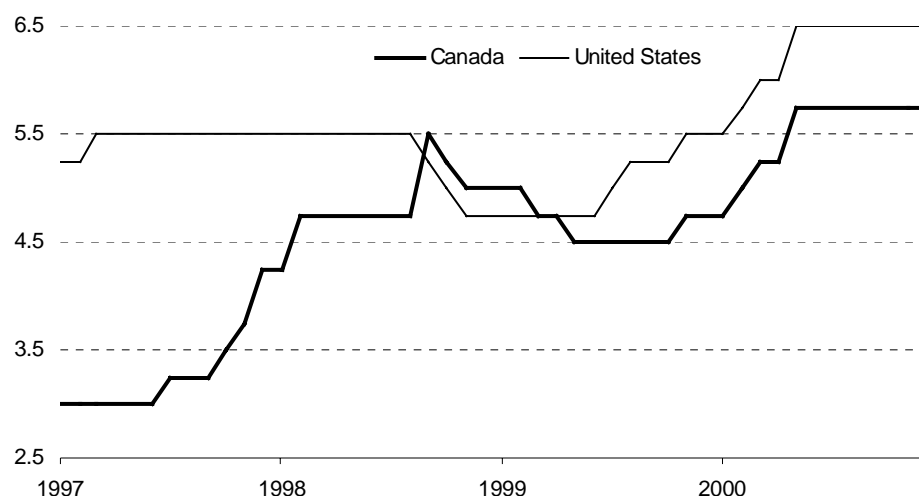
Source: Standard & Poor's *DRI*.

To prevent an acceleration of inflation, U.S. monetary authorities continued to hike interest rates in 2000, a trend begun in 1999. The leading rate rose from 4.75% in June 1999 to 6.50% in June 2000. With the value of the Canadian dollar relative to the American dollar remaining at an all-time low, the Bank of Canada followed the United States' lead in all rate hikes by the U.S. Federal Reserve last year.

GRAPH 1.18

OVERNIGHT INTEREST RATE

(in percent)



Sources: Standard & Poor's *DRI* and Bank of Canada.

Monetary tightening, higher energy prices and stock market correction resulted in a slowdown in the main engine of the U.S. economy in recent years: domestic demand. This slowdown will continue in 2001. Consequently, private forecasters project 2.7% growth in domestic demand this year, half the rate recorded in 2000. The slowdown in domestic demand will cause real GDP to grow by only around 2% this year, three percentage points less than last year.

Monetary easing

The marked slowdown in the U.S. economy prompted the Federal Reserve Board to reorient its monetary policy. After six consecutive increases in the federal funds rate, the U.S. Federal Reserve took the world by surprise on January 3, 2001, when it announced, between two regular meetings, that the leading rate would be cut by 50 basis points. At the end of January, the U.S. central bank announced a further 50-point cut. On March 20, the Federal Reserve cut its leading rate by another 50 basis points.

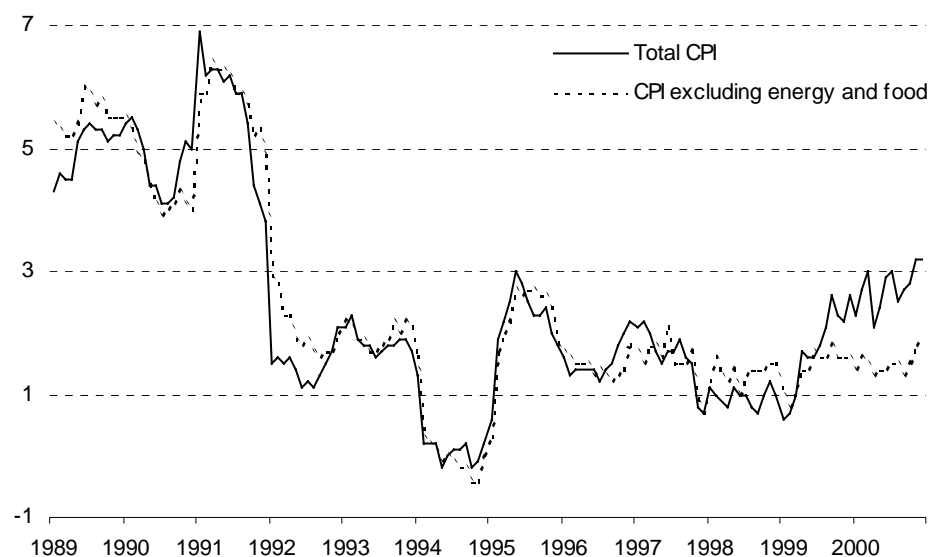
In Canada, monetary easing should be more tempered given the dynamic domestic demand, which will be stimulated by an expansionary fiscal and budgetary policy.

Decline in inflation

Growth in the consumer price index (CPI) for commodities other than food and energy remained below the midpoint of the Bank of Canada target band (1% to 3%) throughout 2000. Between December 1999 and December 2000, the price of energy nevertheless rose by 13.6% and the price of food, by 3.2%, resulting in a 3.2% increase in the overall price index during the year.

GRAPH 1.19

CONSUMER PRICE INDEX - CANADA (annual percentage change)



Source: Statistics Canada.

The oil price rose substantially last year, reaching an average of US\$28.40 per barrel, its highest level since the mid-1980s. Experts project a decline in price in 2001. OPEC countries appear to be in a position to agree and to adjust their production so that the oil price remains around its current level of US\$25 per barrel.

The slowdown in North American economies and maintenance of world oil prices below 2000 levels should mean a decline in inflation in 2001 and a return to the midpoint of the Bank of Canada target band.

More subdued slowdown in Canada and Québec

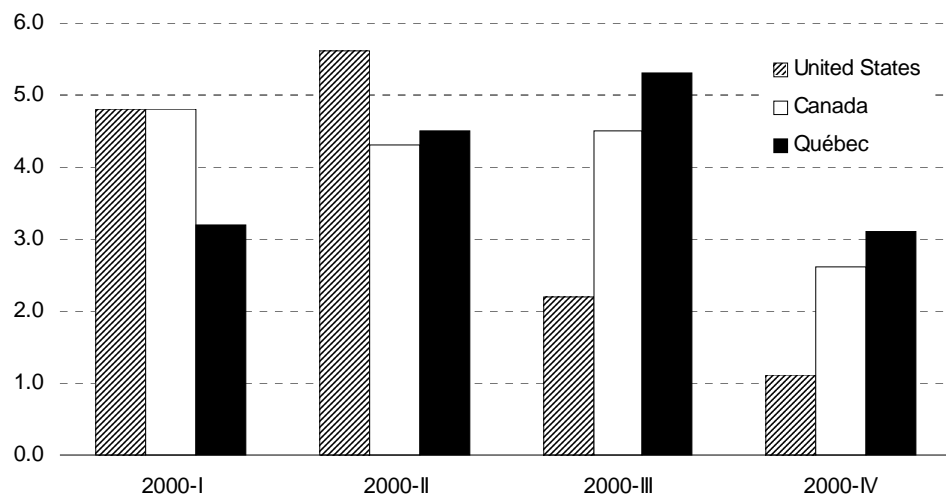
The slowdown in economic growth should be more subdued in Canada and Québec than in the United States.

First, the signs of a downturn are not as clear as in the United States:

- real GDP growth in the second half of the year did not slow down as much as it did in the United States; and

GRAPH 1.20

REAL GDP – QUÉBEC, CANADA AND THE UNITED STATES (annualized change in percent)



Sources: Standard & Poor's *DRI*, Statistics Canada, Institut de la statistique du Québec and ministère des Finances du Québec.

- sustained job creation in Québec resulted in 41 000 new jobs between October 2000 and February 2001.

Second, the Canadian and Québec governments implemented expansionary fiscal and budgetary policies before the United States. The plan put forward by the Bush administration will not be adopted until later in 2001 and its impact may not be felt until 2002.

Third, household confidence remained high in Canada and Québec, despite falling slightly in the last quarter. The decline in consumer confidence was much sharper south of the border.

Finally, the automobile sector makes only a modest contribution to the Québec economy; therefore, the decline should primarily affect Ontario.

However, given the significant economic integration with the United States, the Canadian and Québec economies cannot avoid being affected by the economic slowdown in the United States.

Overall, real GDP should grow by 2.9% this year in Canada and by 2.7% in Québec. This will be sufficient for continued improvement in labour market conditions. Thanks to the creation of 50 000 jobs per year, Québec's unemployment rate is projected to fall from 8.4% in 2000 to below 8% by 2002.

Slower growth in exports

In 2001, Québec's international exports will feel the effects of the economic slowdown south of the border. After jumping 12.2% in 2000, growth in international exports of goods should be more subdued this year, rising by around 5.0%.

Despite the slowing down, exports are expected to grow faster than real GDP again this year. The share of international exports in GDP should therefore continue to increase.

Robust domestic demand

Once again this year, the Québec economy will be supported by fiscal and budgetary policies favourable to growth.

Thanks to major reductions in income tax and the projected decline in energy prices, households should see their purchasing power increase significantly. Real consumer spending is projected to grow by 3.5% this year (4.7% in current dollars) and by 2.6% in 2002 (4.1% in current dollars).

Market conditions in the residential sector have improved immensely in the past few years. Due to the drop in the vacancy rate, which is at its lowest level in 15 years, and the small number of unsold housing units, housing starts should reach 27 000 units this year.

However, according to the most recent Statistics Canada investment intentions survey, non-residential investment should decline by 1.4% in Québec in 2001 owing to the completion of two major investment projects: the Alcan project in Alma and the Magnola project in Asbestos. Excluding these two projects, non-residential investment should reach around 3.5% this year. And while investments in the manufacturing sector are expected to drop, they should still amount to \$5.2 billion this year, double the level in 1993 (\$2.6 billion), the low point of investments for the decade.

The Statistics Canada survey shows, among other things, that robust upswings should be recorded in the following sectors: transportation and storage (17.1%), real estate and rental services (16.9%), public services (16.3%) and communications (14.7%).

TABLE 1.1

ECONOMIC OUTLOOK
(percentage change)

	2000	2001	2002
OUTPUT			
— Real gross domestic product	4.3	2.7	2.6
— Gross domestic product	6.9	4.0	4.0
COMPONENTS OF EXPENDITURE			
— Consumption	5.1	4.7	4.1
— Housing starts ('000)	24.7	27.2	27.6
— Non-residential investment	6.1 ¹	-1.4 ¹	1.1
— International exports of goods ²	12.2	5.0	6.4
COMPONENTS OF INCOME AND PRICES			
— Wages and salaries	6.7	3.6	3.5
— Personal income	5.6	3.4	3.6
— Corporate profits	17.7	8.1	7.4
— Consumer prices	2.4	1.4	1.7
LABOUR MARKET			
— Labour force	1.4	1.1	1.2
— Employment	2.4	1.5	1.5
— in thousands	80	50	52
— Unemployment rate (%)	8.4	8.0	7.8
INTEREST RATES – CANADA (%)			
— 3-month Treasury bills	5.5	5.0	5.1
— 10-year Canada bonds	5.9	5.3	5.5

1 Statistics Canada, Private and public investment.

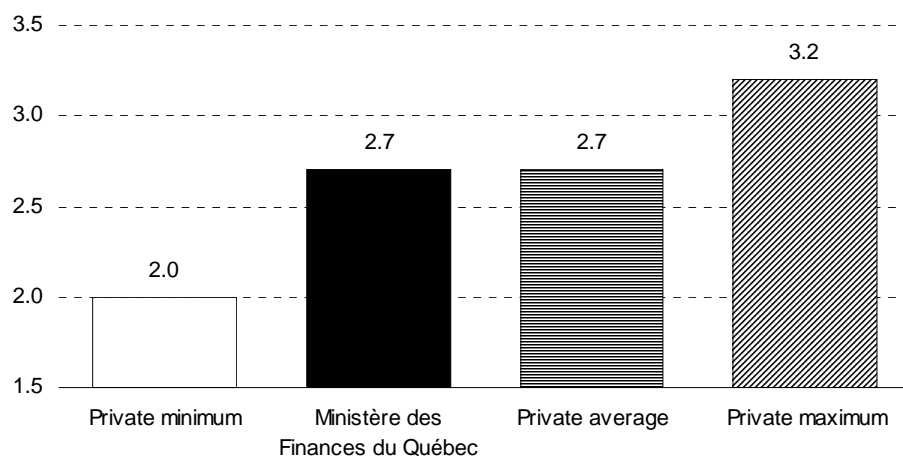
2 Constant 1992 dollars based on economic accounts.

Comparison with private-sector forecasts

Private-sector forecasters are divided on the rate of Québec's economic growth this year owing to the uncertainty over the magnitude of the economic slowdown in the United States and the factors liable to attenuate its impacts on Québec. While some anticipate as much as 3.2% growth in 2001, others predict more subdued growth, as low as 2.0%. On average, private-sector forecasts predict real GDP will grow by 2.7% in Québec, the same rate that was used to prepare this Budget.

GRAPH 1.21

ECONOMIC GROWTH IN QUÉBEC - 2001 COMPARISON WITH PRIVATE-SECTOR FORECASTS (in percent)



Source: According to a ministère des Finances du Québec survey.