2010 Calgary Economic Outlook

A Charlie Brown Economy

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Highlights

- Calgary will experience a Charlie Brown economy in 2010; an economy that experiences variable performance with ups and downs, similar to the pattern on his shirt. This is a result of Calgary's economy being dependent upon the state of the U.S. economy and energy markets.

- The U.S. economy is far from out of recession and onto any sustained path to recovery. It is expected to continue to face variable performance during 2010, impacting the demand for Calgary based goods and services.

- Oil prices should remain in a range sufficient to enable Calgary-based producers to earn returns and maintain moderate levels of investment.

- An explosion of supply in North American natural gas has changed the dynamics of this sector. With low prices and a lower cost environment in the U.S. and B.C., Alberta faces serious short and long-term challenges to its natural gas industry, and is likely to result in further business fallout in Calgary over 2010.

- Calgary's economy has been negatively impacted by the recession in terms of employment losses, skyrocketing employment insurance benefit claims, rising bankruptcies and mortgage arrears, slower real estate markets and a pullback in construction.

- Calgary's economy will recover, but 2010 won't be the year of sustained recovery. Calgary's economic performance in 2010 should be one of variable performance, reflecting the volatility in the U.S. economy and natural gas market. Specifically:

    - Calgary is forecast to see population growth in 2010 of 16,000 to 18,000 people, representing growth of between 1.5 to 1.7 per cent over 2009.

    - Calgary is estimated to see an employment loss of -1.6 per cent in 2009, followed by modest growth in 2010 forecast at between 0.7 and 1.0 per cent.

    - The unemployment rate is expected to hit 8 per cent by end of 2009, achieving an estimated 6.5 per cent for 2009, and is forecast to continue to rise through the first half of 2010, averaging a forecasted 7.4 to 7.7 per cent for 2010 overall.

- Inflation is not expected to be much of a concern through the balance of 2009, coming in at an estimated 0.4 per cent, and is forecast to be between 0.8 and 1.1 per cent in 2010.

- While showing some resiliency in the mid part of 2009, Calgary will only see an estimated 4,800 housing starts in 2009, followed by a forecasted 5,000 to 6,000 units, primarily single-family, in 2010.

- The office market has been impacted by the recession as a result of low deal flow, changing market conditions and new inventory added. The industrial segment apperas to be holding up better and is in a more steady state than office. In the office segment, with the amount of available existing product, and the amount of new product under construction, it is not expected that there will be any announcements of new projects throughout 2010.

- Building permit values were saved in 2009 by robust investment in the institutional real estate sector, and are estimated to reach a total value of $2.65 billion in 2009. However with no new commercial projects, limited residential and a reduction in institutional spending, building permit values are forecast to decline from 2009 to between $2 and $2.25 billion in 2010.

- Real GDP is expected to contract in 2009 at an estimated annual rate of -2.5 per cent, reflecting local and global recessionary conditions. Calgary should continue to face economic challenges and variable performance in 2010. The flow of government stimulus dollars will continue into 2010 and should also be supported by moderate oil sector expenditure and modest consumer expenditure growth, generating a minimal elevation of economic activity over 2009. Calgary real GDP growth is forecast between 0.8 and 1.2 per cent for 2010.

- Looking beyond 2010, more appropriate metrics for determining the end of recession are needed. Failure to do so can perpetuate volatility in markets and expectations, may remove stimuli too early and may not address the systemic problems that brought the economy into recession in the first place.

- Alberta and Calgary are at a time of great opportunity. The recession has reinforced the reality of our reliance on energy prices. Efforts should be taken by government and business to work at achieving Calgary's goal of becoming THE global centre for ALL things energy. Addressing the state of the natural gas sector, by ensuring we create new markets and applications for domestic supply, as well as creating the infrastructure and environment to enable Alberta to capture its market share, will be critical to preserving our prosperity and economic vitality and well-being.

Introduction

What a year! Financial market collapse. Bankruptcies. The Great Recession. And now, recovery. Are we really there yet?

Calgary Economic Development has prepared this 2010 Calgary Economic Outlook as a means of helping to decipher how the local economy is forecast to perform in 2010 amidst uncertainty over the shape and timing of recovery. This Outlook is meant to aid the community in its business planning, budgeting and organizational forecasting. It gives a snapshot of local indicators and discusses their directions in 2010. The report also touches on more strategic issues for 2010 and beyond.

Our aim is to provide increased information on local economic performance to support the community in its continued success and prosperity through every stage of economic cycle.

A Charlie Brown Economy

Calgary will experience a Charlie Brown economy in 2010. Charlie Brown is a boy easy to like and admire. His heart is always in the right place, he tries hard, he is thoughtful of others and wants to succeed. However, despite his best efforts, Charlie Brown doesn't always connect with the football. In this regard, he is representative of the Calgary economy for 2010.

Calgary, despite best efforts, is still essentially an oil and gas economy, reliant upon the state of energy markets. So, ultimately, as energy prices rise and fall, so does the economic activity in Calgary. We try hard to find new economic activities to strengthen, such as technology or creative industries. We work to put strategic infrastructure in place to make Calgary a more attractive place to work and live, such as airport enhancements and public transit. We are the volunteer capital of Canada.

However, we can't escape a global recession. When oil and gas prices fall and capital dries up, the economy is affected as companies cut spending and jobs. All across the value chain the impacts are felt. Cuts to oil sands capital expenditure result in the loss of work and jobs for engineers, lawyers, accountants, financiers, manufacturers, and transporters. When wages are lost or cut, housing markets are affected and retail spending is curtailed.

Charlie Brown is also another strong representation of Calgary's economy for 2010 for another reason. His great shirt. The pattern on the bottom of his trademark yellow shirt represents the shape of Calgary's economic activity for the next 12, and possibly more, months.

Source: *Charles Monroe Schulz*

No, Calgary's economy won't perform or recover as a V, or a U. It will be a Charlie Brown shirt economy and recovery. No one knows the exact number of peaks and troughs we will experience before we see truly sustained recovery, but the overall representation is accurate; that Calgary is likely to experience numerous bumps along the way to sustained recovery. Why? For two reasons: first, the Calgary economy is heavily tied to the U.S. economy, with approximately 87 per cent of Alberta's international exports bound for the U.S.; and second, the Calgary economy is still heavily tied to the energy markets. Both are likely to experience fluctuations and volatility over 2010. And as the ocean rolls, how can we expect a ship afloat to not roll with the waves?

Now this is not to say that things aren't heading in the right direction. Things in the big picture globally, and nationally, are looking far better than they were in late 2008 and early 2009. Many economic indicators are showing signs of bottom, or in some cases, even recovery. But before we get to sustained recovery, we will likely experience more volatility along the way. Think of what one reads in the newspaper across any given week. One day a positive economic result is announced - markets rally and spirits rise. The following day another economic result is announced, yet it performs below expectations and markets stumble. What is one to think about the true nature of the recovery? We wonder if it is truly upon us with such volatility and variability in performance. Such is the nature of Charlie Brown's shirt.

State of the U.S. Economy

There is much talk about recovery in the U.S. But the word sustained never seems to enter the conversation. There are promising signs, most definitely; housing markets appear to be strengthening, manufacturers appear to be getting their equipment fired back up, and stock markets have rallied over the past 6 months. But it just seems too good to be true. It just seems difficult to believe that we got it all right the first time.

Over the long-term, the U.S. economic recovery stage has been set with appropriate fiscal and monetary responses meant to address the greatest recession in decades. But that doesn't mean that a sustained recovery is actually underway. It may be, but we will only know when we look back at historical results. With so much variable economic performance, is the U.S. really there? There were just too many things wrong with financial and capital markets in the U.S. to expect the U.S. economy can be through this recession, and on track for a sustained and consistent path of growth in under 12 months.

The U.S. economy is still very fragile and unstable, despite some positive activity amongst a select range of economic indicators. The U.S. could slip back into recession in the short-term on its path to sustained recovery. And as Alberta's largest trading partner, this economic instability can affect demand for Alberta goods and services, and therefore our local economic performance. This is a result of a number of factors but primarily the state of labour markets, private spending and real estate markets.

Consider recent results. On September 25, data released showed that U.S. new orders of durable goods fell in August by a seasonally adjusted 2.4 per cent, after having posted a gain of 4.8 per cent in July. On September 29, the Conference Board in the U.S. released its consumer confidence index results, that point to erosion in consumer confidence, down to 53.1in September from 54.5 in August.

On September 30, positive news emerged with U.S. second quarter GDP contracting by only 0.7 per cent, below 1.0 per cent expectations. However the next day, a key manufacturing benchmark, the ISM Purchasing Manager's Index, dropped to 52.6 in September from 52.9 in August. ISM New order and production indices declined as well, 4.1 and 6.2 per cent respectively over the same period. These results may serve to continue fuelling speculation that the manufacturing and production activity in the U.S. is not sustainable but a reflection of the rebuilding of inventories.

The National Association of Realtors reported that sales of existing homes dropped 2.7 per cent in August, breaking a four month growth pattern. New home sales in the U.S. dropped from strong monthly growth of 7.8 and 6.5 per cent respectively for June and July to a meagre 0.7 per cent in August, much lower than anticipated.

On October 1 it was released that U.S. auto sales dropped 23 per cent in September 2009 from September 2008, and 41 per cent from August, demonstrating that the surge in car sales in prior months was truly just the "Cash for Clunkers" program and not a reflection of a sustained rebound in new car demand. But it was October 2, when U.S. unemployment rose by 263,000 and the unemployment rate increased to 9.8 per cent that truly confirmed that a sustained rebound is far from guaranteed.

All this to demonstrate one thing; the road ahead for Alberta's largest trading partner is by no means on solid and consistent footing for recovery.

U.S. labour markets still show signs of growing weakness, as the unemployment rate now sits at 9.8 per cent as of September, the highest in nearly 3 decades. With challenged labour markets come implications for retail spending and the stability of housing markets.

With rising unemployment, many Americans aren't willing to open the wallet quite yet. The U.S. consumer is in a rebuilding mode. Household net worth has fallen by US$13.8 trillion since second quarter 2007. Generally, U.S. consumers have heard the call to increase their savings, with the U.S. Bureau of Economic Analysis reporting that the personal savings rate has reached five per cent as of Q2 2009, well above the sub two per cent rate seen for much of the past 3 years.

Overall, personal expenditure should be much slower for years to come. Simply for the fact that the traditional vehicles used to finance consumption expenditures – lines of credit, equity loans, credit card debt – are not as readily available as years past. But they are also saving more, recognizing past mistakes.

One can't forget that that U.S. economy is ultimately being propped up by government programs and funds; an unsustainable approach. With programs such as TARP and Cash for Clunkers, the government has stepped in to spend when the private sector stepped out. Sustained recovery will be reflective of a time when government removes stimuli and it is replaced by private demand, spending and investment. That time does not appear to be upon us quite yet.

Perhaps the most concerning aspect of the U.S. economy is the state of its real estate markets. Despite the fact that the Case-Shiller 20 city housing price index has now shown three months of increase according to July 2009 data not seasonally adjusted, after dropping steadily since July 2006, it is still down approximately 14 per cent year over year.

While nationwide pricing appears to be solidifying, there are potential storm clouds brewing. In the residential market, consider that:

- It is estimated that 24 per cent of U.S. mortgages are in negative equity, with that figure rising to 60 per cent in Las Vegas;
- Housing inventory is still an estimated 9 to 10 months worth of supply;
- Economists feel that some markets in the U.S. still have 5 to 10 per cent more loss of housing value to go;
- It is estimated that there are 2.8 million active interest-only mortgages in the U.S., worth a total value of $908 billion.

Combine unsteady economic performance, rising unemployment, abundant supply, delayed foreclosures, negative equity and interest-only mortgages resetting in the near term, and the picture for the U.S. residential real estate market looks to be one of moving toward another brick wall. There is still great potential for further fallout across the economy.

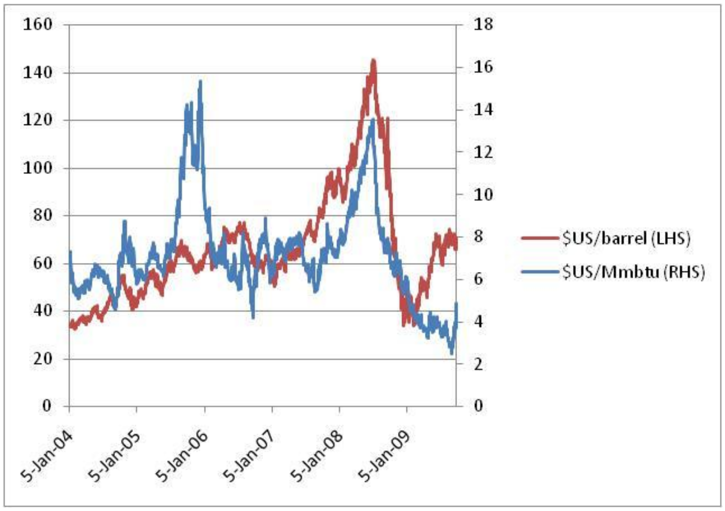
From the commercial real estate perspective, the shoe is only starting to drop. Vacancies are rising across the country, but the true cloud on the horizon is the state of commercial real estate finance. According to Real Estate Economics in New York, there are US$1.3 trillion in commercial mortgages being held by U.S. banks, and US$536 billion in development and construction loans. As capital markets have not fully recovered, and many U.S. banks are still on unsteady ground, should any magnitude of these projects experience delays in pre-sales, leasing, revenue shortfalls or an inability to complete a project, the potential for continued bank losses is extraordinary.

U.S. environmental policy doesn't necessarily directly impact the orders for goods or services in Calgary quite yet, but current policy directions in the U.S. at the federal level, and at certain state levels like California, have significant implications for the long-term vitality of Alberta's energy sector. Depending on the ultimate policy directions in the U.S., the Alberta energy sector, headquartered in Calgary, faces a different landscape from its biggest customer which could create volatility in employment, investment and operations for some time to come.

Ultimately, the talk of recovery in the U.S. appears to be more of a case of bad news not as bad as expected, but not necessarily much sustained and steady good news quite yet.

State of Energy Markets

If there is one difficult thing to predict, it is energy markets. But one thing is certain; they are far from stable. The past year has seen oil range from a high of U.S.$147 per barrel of WTI down to the mid U.S.$30's per barrel and back up to U.S.$70.41 as of October 5 close. Natural gas has also fluctuated but not to the degree that oil has, ranging from a high of U.S.$13 per MMBtu, down to record lows of below U.S.$3.



Source: GLJ Energy Publications

Over the past 4 months, oil has been showing some greater stability around the mid-U.S.$65-75 range, while the state of natural gas has many in industry and government concerned for the long-term future of Alberta. The prices of these commodities in 2010 will dictate much of Calgary and Alberta's economic performance.

Oil

The oil side of the energy market looks to be the more promising for Calgary and Alberta. After a strong decline in prices, oil's position around the U.S.$70 range is boding well for Alberta producers. According to producers, prices at this level are enabling conventional producers to generate good returns, and WTI/heavy spreads are at levels making existing oil sands operations profitable. Part of the basis for this is the reduction in costs in Alberta, which have come down since the peak in 2007/2008. If prices and cost structures hold steady in this range, the oil side of Calgary's energy sector should be steady.

However, 2010 will not likely represent any return to surging oil demand growth or oil sands investment. North America's oil consumption has been on a decline for a number of years, and even with recovery in the U.S., their demand growth for oil is not expected to drive market dynamics that would see strong price growth. Asia and other developing economies will be the source of demand growth, particularly China. The state of oil markets in 2010 will be influenced by the rate of demand growth within China, as well as inventory levels and refining capacity.

From the oil sands perspective, the Oil Sands Developers Group estimates that with the recession a combined $50 Billion was eliminated from capital and operating expenditure amongst oil sands companies. While prices are at levels that may make some oil sands projects economically viable, it appears that two forces are at play: the industry has learned from the past; and, capital availability will limit the number of new projects going ahead.

Too many projects went ahead at once during the 2006 - 2008 period, driving costs well into the stratosphere. This impacted long-term returns, as well as productivity. The reduction of expenditures in 2009 capital budgets has forced many firms to re-evaluate their projects. Many have chosen to hold off, while some are taking advantage of lower costs and more labour availability. Imperial Oil's Kearl Project and Royal Dutch Shell's expansion of its Athabasca Oil Sands Project are two examples of projects going ahead. Many others are still on the sidelines, not wanting to move quite yet and create cost escalation again.

Perhaps a larger factor is the availability of capital. The global recession brought about a severe tightening of capital. While markets are flowing better now than in late 2008, accessibility to the magnitude of capital required for oil sands projects is not as great as in 2006 or 2007. Lack of capital will definitely be a constraint on new projects.

The reduction in oil sands expenditure is indicative of much of the picture globally; large reductions in investment have brought global production growth down significantly. One of the potential implications of this underinvestment is believed to be a supply shortage that could manifest as early as fourth quarter 2010. This would see prices potentially spiking over U.S.$100, creating significant inflationary headwind for a recovering global economy.

For the shorter-term outlook, most analysts expect oil to be in the U.S.$60-90 range throughout 2010, which will be adequate pricing to keep conventional and unconventional oil activity in Calgary and Alberta humming along at a manageable pace.

Natural Gas

The natural gas game has changed materially in North America. Plain and simple. The explosion of supply as a result of available unconventional sources has changed the dynamic that has driven so much of Alberta's prosperity for years.

The U.S. is experiencing strong production in 2009, with inventories well above historical levels, estimated at 500 bcf over the 5 year maximum inventory level. With limited export activity and huge growth in domestic supply in the U.S., imported gas from Alberta may be crowded out by domestic product, negatively impacting Alberta, and largely Calgary, based companies. Add to this record low prices over the summer of 2009.

Another obstacle facing Alberta is the cost differential to production in the U.S. Higher labour costs, drilling costs, seasonality, distance to market and regulatory costs create a lower cost structure in the U.S. The Canadian Society for Unconventional Gas indicates that break-even gas prices (U.S.$) for major North American unconventional projects are:

- Fayetteville: $4.10
- Barnett 1: $4.42
- NE BC Shale (assumed same cost as Alberta shale): $6.80

With the NYMEX near-month at U.S.$4.98 as of October 5 closing, and the highest future contract over 2010 priced at U.S.$7.10 (December), it is clear to see that Alberta's unconventional gas market faces great challenges.

Even if gas prices were to climb to levels that would make projects economically viable in Alberta, the key question is whether Alberta would capture its share of the market. The cost structure and environment, distance to market, rig availability, and competition from B.C. create uncertainty. It is not a certainty that with higher prices Alberta would capture its market share of production.

Analyst expectations of prices for 2010 vary greatly, but the general range appears to be U.S.$4-8 per MMBtu. Ultimately, it is shaping up to be a potentially slow 2010 for Alberta based natural gas activity whether through pricing, or Alberta not capturing its market share.

This new world for natural gas forces many decisions. Alberta business and government need to work to find new markets and new applications for our domestic natural gas. Working to create export opportunities should be evaluated. Expansion of use into power generation and transportation will be two key ways to generate more domestic demand as well as work towards achieving greenhouse gas reductions. Lower cost structures need to be considered if companies are to make returns in a $7 gas environment. And the regulatory and royalty structure needs to ensure that Alberta is competitive and captures it share of North American activity while also delivering prosperity for Albertans. Alot to bite off, but these decisions and changes are critical to ensuring longer-term economic vitality and well-being in Calgary and Alberta.

Implications for Alberta and Calgary

The state of the U.S. economy and energy markets sets the stage for variable performance in Alberta and Calgary; a Charlie Brown economy. So much is beyond our control in the short-term. But, as will be discussed later, the outcome in the long-term is very dependent upon the path that we choose.

The full implications for Calgary's economy in 2010 are wide ranging across a variety of economic indicators more fully discussed below. However, the Charlie Brown pattern of volatility has already emerged in Canada, Alberta and Calgary. Recent performance in a suggested "recovery" provides some evidence that while things look generally better than during the depths of the recession, there are still uncertain times ahead for Calgary.

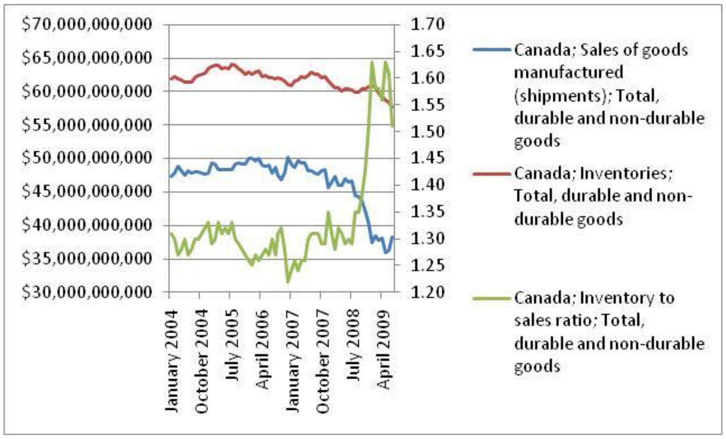
Canadian Performance

The picture starts at the Canadian level, where the economic picture is far from certain in terms of sustained recovery. September 30 saw the release of July GDP figures, which after a 0.1 per cent increase in June were flat in July, much below expectations. Relevant to Alberta and Calgary, the output of the mining, oil and gas sector dropped 1.5 per cent in July, the ninth consecutive month of decline.

On the positive side of the ledger, the August Canadian Index of Leading Economic Indicators increased by the largest amount since April 2002, up 1.1 per cent over July. This index, according to Statistics Canada, is an accurate predictor of economic activity and gains in the index of this magnitude are only seen in the early stages of recovery.

From a sales and manufacturing perspective, real sales of durable and non-durable goods are down nearly 18 per cent year over year as of July in constant 2002 dollars, and down 20 per cent from levels five years ago.

The Canadian inventory to sales ratio, while having shown some rebound in June is still 17 per cent over the 5 year trend line, showing that while inventories have dropped, sales have dropped even more.



Source: Statistics Canada

Canada's industrial capacity utilization rate, while on a downward trend pre-recession, took a considerable nosedive during the past year, now sitting at 67.4 per cent as of second quarter 2009. A bottom perhaps, but no sign of sustained recovery. The good news about low utilization is that it will keep Canada's output gap at a sufficient level as to keep inflation at bay. If there is no roaring demand for product, there is little pressure to push prices up.

Alberta Performance

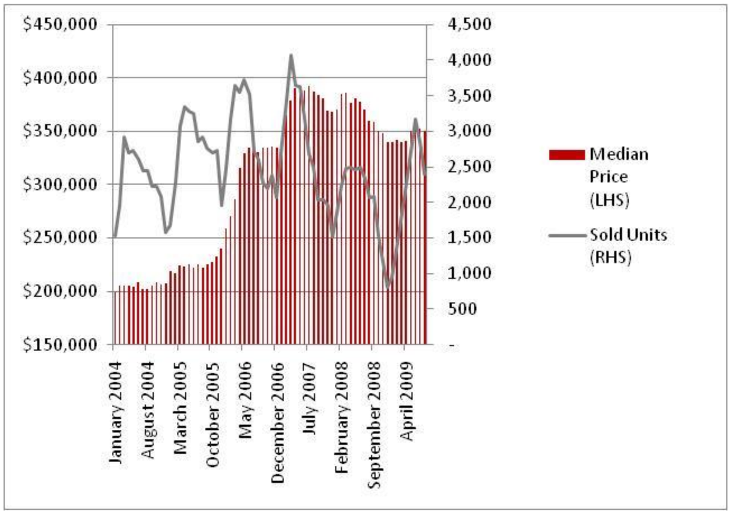
The former engine of Canada's economic growth, Alberta is now performing as the brake on recovery. Despite some increases in June and July of 2009, Alberta international exports remain 40 per cent lower than 2008 year-to-date, and below 2006 levels. Exports to the U.S. are down sharply from 2008 at 39.8 per cent, while exports to China, Alberta's second largest trading partner, are down 33.4 per cent. Mining and energy exports, which comprise approximately 65 to 70 per cent of Alberta exports, are down 44.6 per cent as of June 2009 over 2008. Manufacturing shipments continue their free-fall in Alberta, down 22.7 per cent year-to-date as of July, more than the national figure of down 20.5 per cent. Finally, while they have shown some signs of upward movement in May, June and July, Alberta retail sales and new vehicle sales are nothing to write home about in terms of a turnaround or recovery, as they are still down 9.7 (January to June) and 26.2 (January to July) per cent respectively to the same period 2008.

As economic conditions continue to shown signs of an unstable recovery, a number of lagging indicators show that the fallout from job losses continue to mount in Calgary. Employment insurance beneficiaries have surged in Calgary by 319 per cent as of July year-over-year. Bankruptcies in Calgary continue to rise, 71.3 per cent higher in Q2 2009 than same time 2008. This is led solely by consumer bankruptcies as businesses appear to be holding their own for now. Mortgages in arrears for Alberta have grown 132 per cent as of July 2009 over 2008, a slowing rate from previous months but still growing steadily overall and as a proportion of total mortgages.

Perhaps the most concerning implication of the Charlie Brown economy is the business fallouts that may emerge with slow or variable levels of activity in the natural gas sector. Potential outcomes of a slow winter include bankruptcies and M+A activity in oil field services, as well as lay-offs if natural gas activity remains low in Alberta. And if the price of natural gas remains at current levels, expect the Provincial Government to be facing difficult decisions as to spending in the 2010/2011 budget. Lower government spending could impact everything from income support, infrastructure spending, recreation and health care.

Calgary Real Estate Markets

On the residential real estate side of the equation, single family residential building permit values are essentially flat as of August compared to 2008, however apartment condo permit values are down 95 per cent from 2008. The Calgary Real Estate Board indicates that as of August, Calgary's MLS housing activity has picked up some steam over the summer but is showing signs of slowing. Total MLS sales jumped solidly in May, as did median prices, peaking in June at 3,170 units and $360,000 respectively, and have retreated to lower levels as of August. Overall, Calgary housing prices have held up strongly during the recession, and were in fact in retreat as of their peak in July 2007. Median price sits now only 2.6 per cent below September 2008 price level.



Source: Calgary Real Estate Board

While there was strong activity during the summer of 2009 that brought the market back into better balance, heading into the traditionally slow winter season it is unlikely that Calgary's resale housing market will continue to show steady growth, as much of the summer activity was likely a result of a sweet spot of pent up demand, government incentives and low mortgage rates.

On the non-residential side, thank goodness Charlie Brown for spending on institutional development, for if it were not for the surge of construction projects in Calgary associated with institutions such as University of Calgary, SAIT Polytechnic, Mount Royal University, Alberta Health Services and the Calgary International Airport, there wouldn't be much to keep the construction sector busy. New activity in the commercial and industrial segments has all but vanished compared to levels of previous years, down 95 per cent in industrial value year-to-date as of August and down 72 per cent same period for commercial values.

The state of Calgary's commercial real estate is much like that of the U.S. - it is truly feeling the impact of the recession. Calgary's office vacancy rate as of the third quarter is estimated at 13.1 per cent according to CBRE, up from 4.7 per cent same time in 2008. With more job losses expected, and potential for more M+A or bankruptcy activity this winter as a result of slow natural gas activity, vacancy rates are likely to rise further. This may set up the potential for financial difficulties for smaller owners that are highly leveraged.

Industrial real estate segment activity remains steady but tepid, as slower manufacturing and distribution activity keeps demand for space in check. Vacancy rates on the industrial side have held up relatively well but have risen to 4.7 per cent according to CBRE, and the once feverish demand for land and space is a much slower market.

Community Impact

Finally, the implications of challenging economic times locally are the impact to Calgarians and the agencies that serve their needs. The United Way in its Resiliency Report found that with rising unemployment, more Calgarians are finding it difficult to cope financially, mentally and emotionally with the result being that social service agencies are seeing triple digit increases in demand. With strained budgets due to reduced government or donation revenue, many agencies are finding it a challenge to keep up with demand, with the end result being Calgarians going with their needs unmet or without resources. It is critical that during these kinds of economic times that government, agencies and the community overall work collectively to aid Calgarians in need.

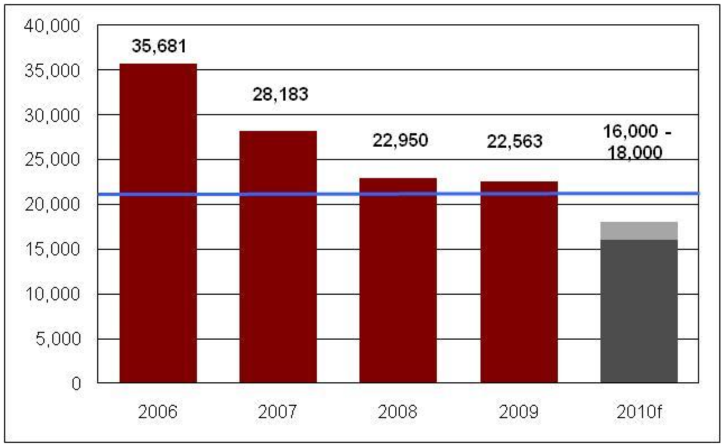
Calgary 2010 Economic Outlook – Key Indicators

Population Growth

Calgary saw a net population increase of 22,563 from April 2008 to April 2009 according to The City of Calgary Civic Census. This represents an annual growth rate over 2008 of 2.16 per cent.

While 2009 may have seen some still very healthy growth, slower economic conditions in Alberta are expected to act as a deterrent to attracting new Calgarians in 2010. Add to the fact that Calgary's housing prices have held up relatively well during the recession and that from pure house price alone, Calgary is now the second most expensive jurisdiction in Canada behind Vancouver, and fewer people will be able to make the move and enter the Calgary housing market. While Calgary's unemployment rate should remain one of the lower among major centres in Canada, the volatility of a Charlie Brown economy in Calgary should serve to erode the overall attractiveness of Calgary as an employment market.

For 2010 in Calgary, natural addition is forecast to be between 9,000 and 10,000, with net migration at between 7,000 and 8,000, resulting in total population growth of between 16,000 and 18,000 persons. This represents annual population growth of between 1.5 and 1.7 per cent over 2009.



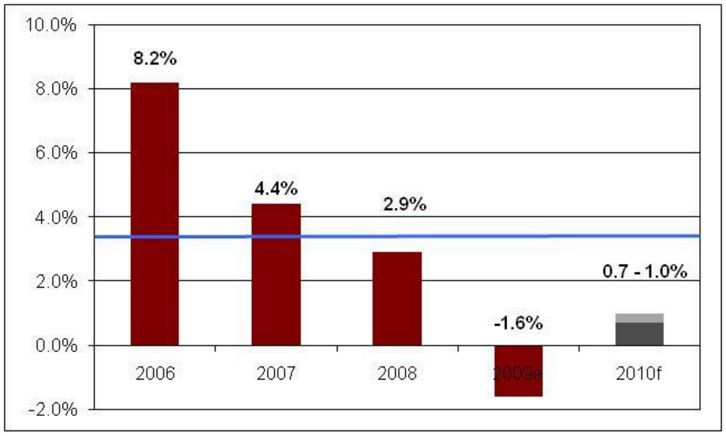
Source: Calgary Civic Census, CED

Employment Growth

2009 saw Calgary's labour market reverse years of nation-leading employment growth. In the first half of the year, job losses mounted, however June started three months of job gains. All these job gains have been in part-time jobs, with continued losses in the full-time segment. A substantial increase in the labour force, as more people join the search for work to deal with income needs, has pushed the unemployment rate in the Calgary region to 7.0 per cent as of August. All sectors have been affected; however the energy, construction and manufacturing sectors have taken the brunt of the total employment losses in Calgary, now sitting at 17,700 since September of 2008, not adjusted for seasonality.

We have not seen the end of job losses in the Calgary region as of August. Further job losses are expected in 2009 and into the first quarter of 2010, particularly in the natural gas and service sides of the energy sector. If new investments are not made on the oil side of the sector, work in engineering and other professional services for the energy sector may also be impacted as well. If orders do not pick up in 2010, or the Canadian dollar remains at elevated levels, employment in the manufacturing sector may fall even further than current levels. Finally, with a slower year predicted for real estate development across all forms, construction employment is not expected to make any rebounds from current levels and may be fortunate to avoid any further losses.

Further job losses to be experienced in Calgary for the balance of 2009 should result in an estimated employment decline for 2009 of 1.6 per cent, ultimately with fewer people employed in 2009 than were in 2008. By second quarter 2010, most firms should have experienced the extent of layoffs and found a bottom to employment losses. As 2010 progresses some firms may determine conditions are ripe for growth in key areas for the long-term, or want to hedge bets by hiring more part-time workers, and will move Calgary's employment growth in 2010 to a forecasted 0.7 to 1.0 per cent.



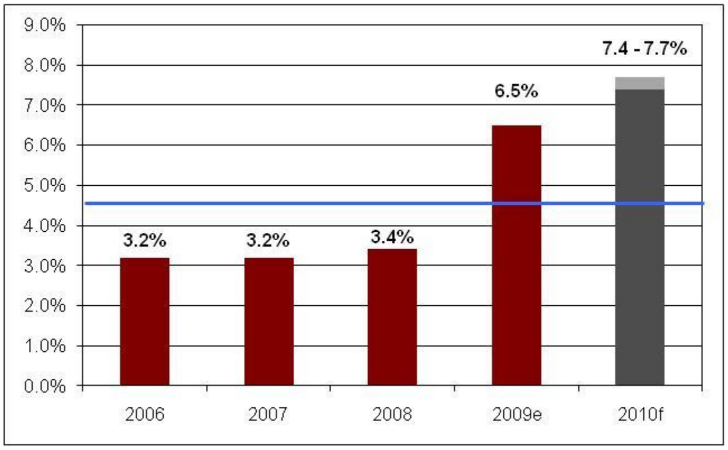
Source: Statistics Canada, CED

Unemployment Rate

Calgary has seen a dramatic rise in the unemployment rate during 2009. Coming off an annual unemployment rate of 3.4 per cent in 2008, in the past 9 months, Calgary's unemployment rate has more than doubled, resting at 7.0 per cent as of August.

Continued slow activity in the natural gas sector is expected to exact further employment impacts in the Calgary region, pushing the unemployment rate to 8 per cent by end of 2009. Throughout the winter, with limited work in the natural gas side, the unemployment rate is expected to rise slightly above 8 per cent before it begins its move back down to approximately 7.4 per cent by end of 2010.

The unemployment rate is estimated to be 6.5 per cent annual average for 2009, and is forecast between 7.4 and 7.7 per cent annual average for 2010.

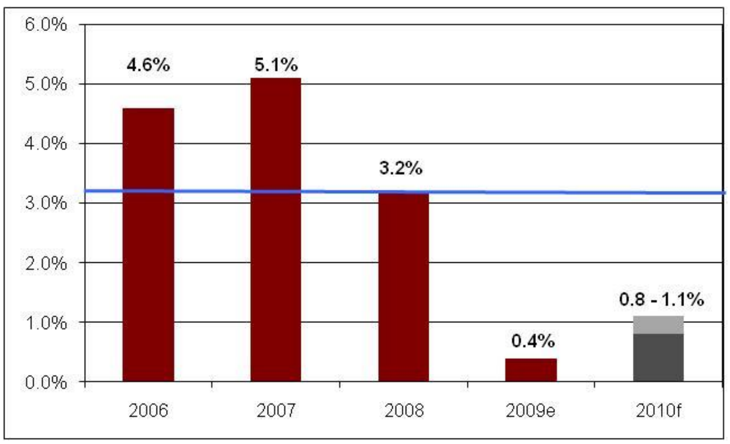


Source: Statistics Canada, CED

Inflation

As predicted in the updated 2009 forecast, inflation has not been a factor in 2009, primarily as a result of high gasoline prices during the summer of 2008, pushing the summer month inflation rates in 2009 into disinflationary territory. Expect the negative sign to disappear by October's figures and back into very modest inflation territory. Calgary's overall inflation for 2009 is estimated at 0.4 per cent.

The reverse of 2009 is expected to happen in 2010, as early 2010 inflation will reflect low gasoline prices that were experienced when oil dropped into the U.S.$30 and U.S.$40 per barrel range. Expect inflation to rise in early 2010 but then drop again to more modest levels. Consumer spending is not expected to rise dramatically in 2010, and the low capacity utilization is expected to keep prices at bay. Therefore, Calgary's inflation is forecast between 0.8 and 1.1 per cent for 2010.



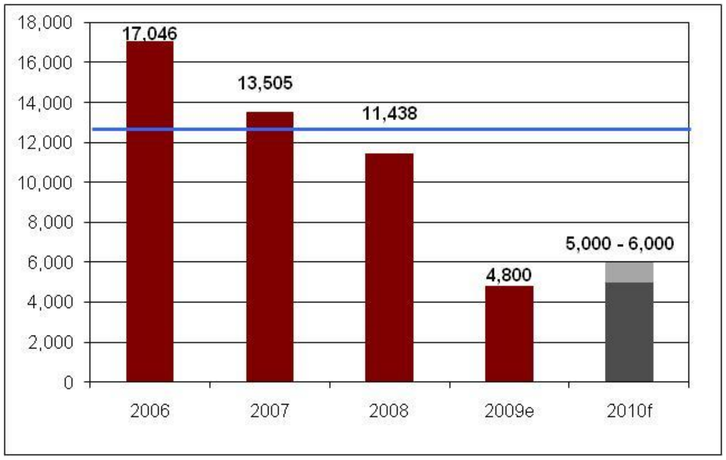
Source: Statistics Canada, CED

Residential Real Estate – Housing Starts

Calgary experienced a rebound in housing during the spring and summer of 2009, but it is not likely to translate into a continued upward trajectory of residential real estate activity into 2010. The rally was a likely result of lower prices, pent up demand, low mortgage rates and government incentives. With the exception of low mortgage rates, the other conditions are largely exhausted or soon to expire. With further job losses, or concern of employment or wage losses, the housing market is unlikely to grow at any rate above economic growth throughout 2010. The uncertainty and volatility inherent in the Charlie Brown shirt pattern will play out in the housing market as well because of these factors.

Having said that, there will likely be continued interest from first time home buyers taking advantage of low mortgage rates. Therefore new housing starts and MLS sales of product under $500,000 should remain strongest of all segments. Single-family product should comprise the bulk of housing starts as the condo segment remains heavily over-supplied in Calgary.

With a tempering of demand from peak spring and summer levels going into winter, 2009 housing starts are estimated at 4,800, and forecast between 5,000 and 6,000 units for 2010.



Source: Statistics Canada, CMHC,CED

Commercial Real Estate

Nothing like a recession to change the dynamics of a real estate market overnight. If it hadn't been for the recession, one probably wouldn't be talking about double digit vacancy in the Calgary office market. But we are.

With third quarter overall office vacancy estimated at 13.1 per cent by CBRE, and continued job losses anticipated, the vacancy rate is expected to rise to the end of 2009 and continue to rise in 2010, as further job losses are experienced and new supply is added to inventory. With rental rates declining steadily, it is definitely a tenant's market. With such abundant supply of both head and sub-lease space available, there is ultimately no pressure for new space above and beyond what is already in the pipeline. Therefore expect no announcements of new office product for many years to come.

The downtown office market has taken the hardest hit in terms of magnitude of change in vacancy and rental rates. With approximately 4.6 million sf of space to come on stream within the next few years, overall vacancy rates in the high-teens are a common refrain in the forecasting reports by major brokerage houses. While offering tenants plenty of choice, high vacancy rates can challenge building owners from a financial perspective.

The beltline and suburban markets are not immune to the recession and the space decisions being made by Calgary users. Vacancies across both submarkets have risen and now sit at 12.09 and 11.54 per cent respectively according to Colliers International. In the beltline, over 500,000 sf of space is expected to come on stream in 2010 pushing the vacancy rate higher, and rental rates even lower. 2010 is expected to be the peak year for pressure on vacancy rates and rents. Similarly on the suburban side, vacancies and rents are responding to slower market conditions. 2009 should see a large increase in inventory, as over 1.6 million sf are added, with more modest increases around 250,000 sf for the next three years.

2009 has brought the industrial real estate sector to a slowdown, with the lowest level of new inventory introduction in the past 10 years. However, the industrial segment has held up better than office. Absorption, while low compared to the past ten years, has remained positive. Vacancy now stands at 4.7 per cent as of third quarter according to CBRE. Few large transactions have occurred in 2009, in line with a slower market, pushing rental rates lower and cap rates higher. With limited new supply to come on stream in 2010, expectations are that vacancy rates will trend downward again in 2010 should demand return. However, the manufacturing sector is facing a significant headwind and may not be a large source of space demand. The transportation sector has been affected by the recession, with less cargo movement due to lower consumer expenditures and manufacturing activity, therefore demand for distribution and warehouse space has been softened.

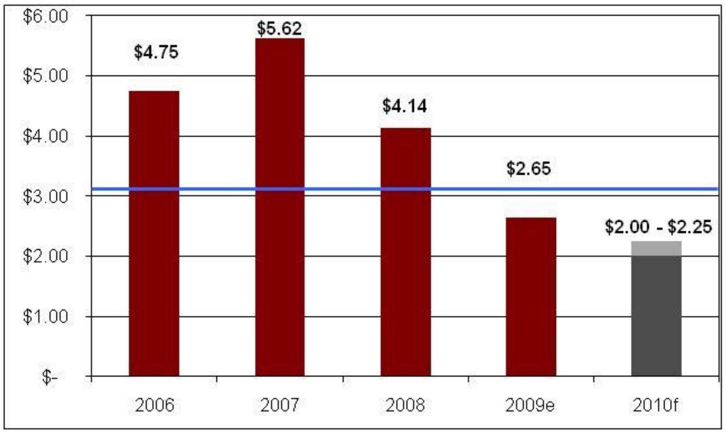
Additionally, with the opening of the north ring road, less expensive property in areas surrounding Calgary to the north and east may take market share from more expensive serviced land within the city boundaries. All in all, the industrial segment is poised for a steady but slow year in 2010 as space demand remains at low levels compared to historic performance.

Building Permit Values

Calgary's issuance of building permits in 2009 definitely reflected a year when the private sector pulled away and the institutions stepped in. Pent up demand, government incentives and low mortgage rates however resulted in consistent issuance of single family residential permit values despite a recession.

The picture for 2010 is shaping up to be less rosy for building permit values than 2009 is expected to be. The state of office and industrial markets suggests that there should be very little permit value issued for new product, with some improvement permits being issued as firms choose to stay put and improve rather than move. On the residential side, an anticipated release of pent up demand is expected to keep new single family permit values in low territory compared to historic performance and the condo market at negligible levels. Finally, after a surge in government and institutional permit values in 2009, they are expected to taper off as stimulus dollars are reduced and City of Calgary capital budget dollars taper off in 2010 as per the 2009-2011 budget.

Building permit values for 2009 are estimated at $2.65 Billion, and are forecasted between $2.0 and $2.25 Billion for 2010.



Source: City of Calgary, CED

Real GDP Growth

Calgary's economy was the strongest performing urban economy in Canada for essentially a decade. But a global recession, and reliance upon energy markets and one trading partner has brought Calgary's economic performance down significantly.

With the state of economic activity around the world, Calgary will experience a recession for 2009. It is simply inevitable. Even with three quarters of strong economic activity in 2008, including a period of U.S.$147 oil, Calgary only produced 0.4 per cent real GDP growth. With depressed oil prices for much of the first half of 2009, and depressed natural gas prices for much of the entire year, combined with job losses, reduced private sector spending and investment, the stage is set for a true recession in 2009. Real GDP is estimated at -2.5 per cent in 2009.

For 2010, economic activity is not expected to charge ahead like a bull. Remember, it will be a Charlie Brown economy. It is going to experience much volatility and variability reflecting fluctuations in the U.S. economy and oil and gas activity. Considering the major components of real GDP - consumer expenditure, business investment, government expenditure, and net exports - there doesn't appear to be any one area that would push strong overall economic growth.

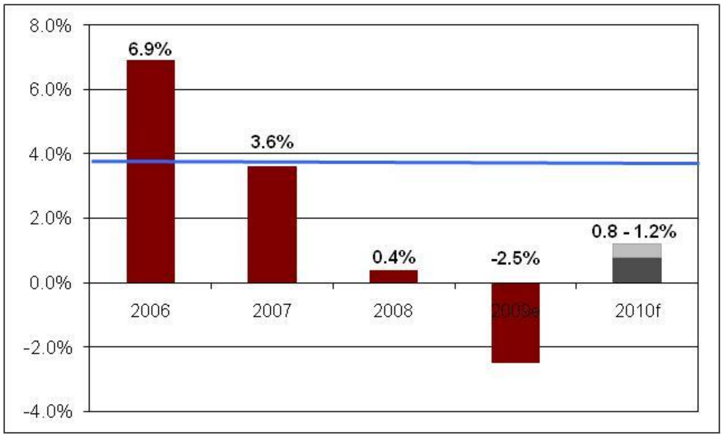
Unsteady performance in the U.S. should create variable activity for manufacturers and exporters. Oil prices should remain strong enough to encourage continued business investment in that side of the sector, however no where near levels experienced pre-recession. Much of this hinges on Asia, specifically China, which currently appears to be back on track for solid oil demand growth.

Natural gas prices are expected to be quite volatile throughout 2010, and even if they do increase to the U.S.$6-7 range, the question is whether Alberta can competitively capture more of the drilling activity to spur a return to business investment in the natural gas business. Growth in U.S. inventories and domestic production suggests that there may be a reduction to Alberta exports of natural gas to the U.S. This would see a reduction of natural gas export values in Alberta, which as of 2008 comprised approximately 30 per cent of total. Overall the picture suggests limited business expenditure and investment in natural gas, and potentially even a decline depending on prices. Natural gas is truly the wild card for Alberta and Calgary, but the outlook is weighted to the downside all things being equal.

Real estate, as discussed above, is not expected to contribute heavily to economic activity given the forecasted slowdown in new building permit activity across all segments of industry. Continued government stimulus is expected to fuel some institutional development, and the single-family residential segment is expected to at least maintain 2009 levels. But overall, real estate is not expected to be a growth segment of the economy in 2010.

With declining revenues and soon-to-be-expiring stimulus dollars, all three levels of government are expected to trim their spending. Finally, the consumer is expected to grow spending from 2009 levels, however they are expected to be cautious, still minimizing big ticket expenditures until economic conditions show greater certainty of recovery and stability.

The Calgary economy is expected to move up and down, largely with energy prices and seasonality, as periods of time throughout the year may show improvement, and some may show decline; a Charlie Brown shirt pattern of economic activity. Overall, Calgary real GDP growth in 2010 is forecast between 0.8 and 1.2 per cent.



Source: Conference Board of Canada, CED

Looking to 2010 and Beyond

There is great risk in believing that this economic recession is done and gone, for that may create complacency. We risk going back to our former ways. Some people have been more greatly impacted than others - mostly those that have lost jobs - but, in Calgary, for 93 per cent of the labour force, very little has changed in the grand scheme of things. Humans learn from mistakes by adapting behaviour. If we assume all is well there is a risk that we will not have learned our lesson well enough.

It is interesting to reflect that we will never claim that we are in recession until there is irrefutable proof of at least two consistent quarters of negative performance. Yet, before we are actually even out of recession we proclaim we are out of recession. Human nature. Cautious on the negative; optimistic on the positive. Again, this approach sets us up for greater challenges ahead, if we don't truly reflect on the impacts, and adapt behaviour accordingly.

More meaningful and sustained recovery is ingrained in a greater and more robust scorecard than currently being watched by the majority of the developed world. We celebrate with one day's worth of positive data, only to sink the following day on negative performance of some other data.

Recovery is going to happen. When exactly, no one knows. Balance sheet recessions, like the one we are in, have proven historically to be longer and slower to recover. It might take another 6, 12 or 18 months before we can truly say that the worst might be behind us. And when it does, it likely will be a slow, steady recovery that will look incredibly modest. In the long-term however, more modest growth rates might become the new norm, and ultimately be what we need to keep us honest.

As individuals, companies and governments, let's set realistic benchmarks that determine recovery and indicate whether we have set forth on a genuine path. This might look something like multiple quarters of stability or growth in key indicators; reductions in the demands on our social infrastructure and agencies; resolution to balance sheet related matters among financial institutions; governments not needing to flow billions of dollars to, or take ownership positions in, ailing companies; and a demonstration of the private sector to get back into spending and investing their own money replacing government stimuli.

In light of these types of measures, it would appear that we are some time away from sustained recovery globally and locally. When it will happen is anyone's guess, therefore we should be prepared for, and ready to address, continued recessionary conditions in all their shapes and forms and the associated impacts at the organizational and community level.

By adjusting our measures for evaluation of recovery, we set the stage for more significant assessment of what got us here in the first place, and the things needed to ensure they don't happen again. For we have excellent memories in the short-term, but in the long-term we forget everything.

There is one final aspect of Charlie Brown that we all admire; his ambition to kick the football. He dreams about it, he plans for it, he prepares for it. His focus is squarely on that football.

In Calgary and Alberta, we need to truly reflect on our football. Our plan, and our ambition.

The recession provides ample evidence of one fact - that Calgary and Alberta are still heavily dependent upon the price of oil and gas. There are lots of other factors at play, but boiled down to its essence, our prosperity depends on the state of two prices. That's it. Two prices. This may be simplistic, but it illustrates an important fact. We aren't there yet in terms of a more diversified economy.

An opportunity has been handed to us. One that has shone the spotlight on a fact that we didn't want to believe was still true. The fundamental changes in North American natural gas supply have only added to the imperative that is this opportunity. That opportunity is to become THE global energy centre for ALL things energy.

The Calgary Economic Development Strategy 2008-2018 puts in place this ambitious goal. It builds upon our strength in energy. And evolves that strength across ALL things energy, renewable and non-renewable, and across all elements of the value chain - from education, to research, finance, value-add, transportation, to end user. Calgary should be THE place in the world where anything energy-related has to be.

We need to strategize and execute how Calgary and Alberta will kick our football. We need to work to ensure economic vitality and well-being for decades to come by becoming THE global energy leader. Achieving this goal would be tantamount to not only kicking our football, but kicking it clear through the uprights.

The natural gas situation in Alberta is an illustration of the importance of assessment and evolution of one of our most crucial economic drivers. The supply landscape has fundamentally changed for natural gas in North America, with significant consequences for Alberta. As a large employer and source of government revenue, much is at stake if the sector doesn't evolve and adapt.

What does evolution in natural gas look like? It is greater focus within industry on being lower cost producers. It is finding new markets for our product - potential LNG exports to Asia where demand is high. It is finding new applications for the product - power generation and transportation fuel.

Evolution also looks like ensuring the right infrastructure is in place to support these new markets and applications. And that the right investments are made to support industry and infrastructure growth and development. It also means that we have a competitive environment to ensure that we get our share of production activity.

How we address and evolve the natural gas side of energy over the coming years will be an important part of achieving our global energy centre goal. But it doesn't stop there. We need to look at energy overall. And all elements that create and move energy. We need to move on our goal of becoming THE global centre for ALL things energy.

Our time is upon us, now let's get out there and kick that football Charlie Brown!

Risks to the Outlook

Upside

- Higher than expected oil and natural gas prices
- Faster and more stable recovery in the U.S.
- Consistent government expenditure
- Lower Canadian dollar
- Greater level of business investment and spending

Downside

- Sustained high Canadian dollar
- Low oil and gas prices
- Stringent and rapid environmental regulation in the U.S. on energy products
- Heavily reduced government spending
- Poor economic performance in the U.S.
- Weaker than expected consumer spending

Sources

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Canadian Bankers Association

Canadian Society for Unconventional Gas

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The City of Calgary

TD Economics

U.S. Bureau of Economic Analysis

U.S. Department of Labor

Zillow.com

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