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Chair

Mr. James Rajotte

Standing Committee on Finance

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● (1605)

[*English*]

The Chair (Mr. James Rajotte (Edmonton—Leduc, CPC)): I call this meeting to order.

This is meeting number 71 of the Standing Committee on Finance. Orders of the day are pursuant to Standing Order 108(2), a study of the impact of low oil prices on the Canadian economy.

I want to thank our witnesses for being with us here this afternoon in Ottawa. I want to apologize for the delay caused by the vote, and I understand that we may have another vote, but we very much appreciate your being here with us.

We have, first of all, from the University of Ottawa, Monsieur Jean-Thomas Bernard. We have Mr. Philip Cross, from the C.D. Howe Institute. From Memorial University of Newfoundland, we have Professor Wade Locke. From the C.D. Howe Institute as well, we have Mr. Steven Ambler. From RBC Financial Group, we have the senior vice-president and chief economist, Mr. Craig Wright. Welcome.

I understand Mr. Randall Bartlett, from TD Bank Financial Group, had to leave for a personal emergency, so we hope everything is okay there.

You each have five minutes. If you could shorten that at all, it would be very much appreciated.

[*Translation*]

Professor Bernard, you have the floor.

Professor Jean-Thomas Bernard (Visiting Professor, Economics, University of Ottawa, As an Individual): Thank you.

I will just make a few brief comments.

I would like to remind you what we mean by "Dutch disease". It means that the increase in the development of one or more natural resources causes the exchange rate to go up, which leads to a relative decline in the manufacturing sector. That is the standard definition.

One of my colleagues has studied the phenomenon very closely. He tried to measure the impact on the Canadian economy for the growth period in the 2000s. His study shows that about 42% of the impact on the manufacturing sector of the increase in the exchange rate is the result of an increase in the prices of raw materials.

There are debates on the mechanism causing this negative impact on the manufacturing sector, but in general, the emphasis is on the increase in the domestic prices of services in Canada compared to what is happening elsewhere, an increase that has a negative impact on the entire manufacturing sector.

I would like to mention two other points that are not often mentioned in this debate.

Professor James Hamilton noticed a negative relationship between rising oil prices and economic activity around the world. That is one more effect on Canadian manufacturers. If the increase in oil prices has a negative impact on economic activity worldwide, there is clearly a negative impact on the Canadian manufacturing sector, regardless of all the other effects that may occur.

We must also remember that Canada is a large country and that transportation costs are relatively more significant for the Canadian economy than for the other economies of industrialized countries. Therefore, an increase in oil prices affects the transportation sector, which causes additional challenges for Canadian manufacturers.

The last point has to do with an ongoing debate among economists regarding the effect of this relative decline in the manufacturing sector or the effect on the overall productivity of the Canadian economy as a whole. I would simply like to say that this issue has not been resolved, although we often hear comments about this relationship.

● (1610)

The Chair: Thank you for your presentation.

[*English*]

Mr. Philip Cross (Research Fellow, C.D. Howe Institute, As an Individual): Thanks for inviting me, and in particular for sitting me next to my thesis supervisor at Queen's. I'll be expecting a grade at the end of my presentation.

Voices: Oh, oh!

Mr. Philip Cross: If I get a hook in the middle, you'll know what's up.

I submitted a written version of my presentation in French and English, so I won't go through it in the interest of brevity. A couple of the main points I wanted to bring to your attention were, first of all, that this industry is cyclical. We've had sharp drops before in 1986, 1998, and 2009. The one I wanted to bring to your attention was in 1998. It stands out because that was when conventional oil production peaked in this country and we began the long-term shift to reliance on the oil sands for our oil.

The importance of that is that it shows that even at a time of weak prices other variables can be very important in determining the course of this industry, such as technological change or a change in tax policy. Alberta changed its oil royalties in 1998, which helped kick that industry off. Public attention tends to be fixated on price, and that's not the only thing that's going on here in the longer term.

The other thing I'll bring to your attention is that recessions in the resource sector generally, and especially in the oil industry, are quite different than recessions that we're used to. I was head of business cycle analysis. I studied recessions for Statistics Canada. I declared, you know, when the recessions began, when they ended. I spent a lot of time studying these things. Typically a recession in the auto industry and the housing industry is a very sharp cutback in output and employment. That's not what you get in the resource sector.

What happens in the resource sector? I circulated a graph of what happened in the manufacturing industry versus what happened in the oil industry over the last couple of decades. You can see that when oil output falls it's by very small amounts, 1% to 2%. The recessions in this industry are felt more in prices and profits than output and employment.

The whole dynamics of these recessions are quite different. You'll get a responsive output in the longer term as investment dries up, but you won't get the sharp drops in output that you would in auto assembly or housing. I'll remind people that recessions in the resource sector are different than in a lot of other industries.

The Chair: Thank you very much, Mr. Cross.

I have Mr. Locke next, so we'll jump to Mr. Locke.

● (1615)

Professor Wade Locke (Professor, Memorial University of Newfoundland, As an Individual): Thank you.

In the interests of brevity as well, I'll just deal with a couple of slides. There's a full slide presentation there for you.

I would point out that the oil and gas industry has been extremely important to Newfoundland and Labrador. We have produced about 1.5 billion barrels of oil since the industry started in 1997. This had a value of $110 billion. We have collected in the range of $18 to $19 billion in royalties, and we have had investment of $34 billion to $35 billion in development and ongoing operations.

We have about 4% or so of our workforce working directly in Newfoundland, and another 4% to 5% of our workforce working in Alberta in the oil sands. The immediate impact of the fall in the price of oil will be through people being laid off and projects being delayed in Alberta. That will have a dramatic and notable impact on our particular economy. The next impact will be through the treasury. We have now gone into a significant deficit, which will have to be dealt with, as a result of relatively lower oil prices. We had oil prices in the range of $105 for the last four years, and suddenly $105 is not a good number to be using. We're going through a substantial change in expenditures and taxes.

Hibernia is the second-biggest producing field in Canada's history. It is behind the Pembina, but a substantial amount of oil comes out of eastern Canada. I would point out that the impacts on Canada will come through a number of ways. One is through equalization, which won't be felt yet, as a result of the falling revenues from lower oil prices to Alberta, Newfoundland, Saskatchewan, and British Columbia. You will see this in two years' time, in terms of lower equalization for places like Ontario.

It is interesting when you look at the forecast. We're expecting by the end of this year to start to return to balance. All of this disruption in the oil and gas sector you should bear in mind is because of a 1% to 2% oversupply, and this caused prices to fall by 60%. It is hard to understand.

There is a lot of uncertainty in terms of the forecast for supply as well. A lot of this is being driven by shale oil production. We're looking at 100 million barrels a day of increased production, from the current levels of 93 million to 94 million barrels, by 2020. It's not at all clear where that oil is going to come from. A large chunk was expected to come from Iraq and Libya, and not all of it is coming from shale.

The other thing I would point out is that a lot of the efficiencies that people talk about for shale have already been achieved. They have been drilling in the sweet spots, or spots that are 10 times more productive than the margins. It is not at all clear that they can continue to produce to this level. In fact, the most recent numbers coming out of the drilling report from the EIA a couple of days ago indicate that in April we're expecting falls in production in shale in three of the four major shale projects. This assumes no growth in demand, as well, in Europe or Japan or any of those places. It wouldn't take much of a change in any of those places to translate into a huge increase in prices.

Right now, we have a short-term issue; the question is how long it will last. The long-term issue is that there's not enough supply in shale or in the alternative sources at current prices for this to happen. If prices were to stay at $60, we'd have problems in Newfoundland in terms of the offshore as well.

I'll leave it there. Thank you.

The Chair: Okay. Thank you very much for your presentation.

We'll go to Mr. Ambler, please.

Professor Steven Ambler (David Dodge Chair in Monetary Policy, C.D. Howe Institute): Thank you for inviting me.

My comments will be based on the written submission that I sent in, which was basically the Verbatim published by the C.D. Howe Institute on March 2. Copies may have been circulated in advance. If not, the document is available on the C.D. Howe website.

Once again, in the interests of brevity, I'll skip over a lot of stuff.

This is based on our meeting before the January rate announcement by the Bank of Canada and also on the basis of a compilation of written submissions by the members of the monetary policy council at the C.D. Howe. Our consensus was that the overall impact of the recent drop in oil prices is negative.

There were differing degrees of pessimism among the members of the monetary policy council. There was a consensus, however, that most of the negative impacts are going to have an immediate effect on the Canadian economy, whereas the positive impacts are more uncertain and are in general subject to longer lags.

I note in passing, and with interest, that the Bank of Canada's own assessment of the impact of lower oil prices is quite negative, whereas in the last Federal Open Market Committee minutes, their assessment for the impact on the U.S. economy is actually, on balance, positive. Now, I know there are many structural differences between the two economies, but if you look at the importance of the petroleum sector in the two economies, in Canada it's 3%, which gives you a negative overall impact, whereas in the U.S., it's about 1% of GDP. So where it comes out as a wash, maybe, is sort of halfway in between at 2%.

The reason it's complicated is due to the complicated input-output linkages between the petroleum sector, on the one hand, and the other sectors of the economy, such as manufacturing and transportation and other sectors, and we go a through a list of possible negative and positive impacts.

I'll skip to the possible positive ones, which come mostly through the real exchange rate depreciation that accompanied the decrease in oil prices recently and was actually boosted to the tune of about an extra two to two and a half cents on the dollar by the rate decrease by the Bank of Canada in January. One could expect an increase in demand for exports, some incentives by manufacturing and other industries to increase productive capacity, and a shift in final demand by consumers from imports to domestic production.

In terms of the policy implications that follow from this, one strong message that I'd like to convey—it's more of a personal opinion than the consensus view of the council—is that one should never reason from a price change. That's a sort of basic introductory economics message.

To analyze the medium- or longer-term impacts of the price change on things like Canadian exports, it's crucial to know to what extent the decrease in oil prices is a supply-side effect, with increasing supply coming on stream from preceding investments—the so-called shale gas and fracking revolution—or whether the decrease in price reflects projected weaker growth of the world economy. Of course, depending on where you come down on that issue, and it's uncertain—the literature is actually divided on the subject—that leads to either a much more optimistic or pessimistic point of view for the future of things like Canadian exports.

One thing that I think we recommended in terms of policy as the bottom line is that the Bank of Canada should be quite explicit in its own assessment of the reasons for the recent drop in oil prices. Some members of the council I think feared that the rate cut was the result of a pessimistic assessment of prospects for world economic growth, and this could actually have a spillover effect in terms of negatively affecting inflation expectations for the Canadian economy.

My own view as well is to exercise caution, and in terms of monetary policy, to think long and hard because my own view is that the biggest monetary policy mistakes in the last 45 years, not only in Canada but in the world as a whole, have been essentially inappropriate responses to oil price shocks.

● (1620)

This includes the great inflation of the seventies—and it's a bit of a minority opinion—and even the fact that the Fed in 2008, as nominal income in the U.S. was dropping rapidly, kept interest rates fairly high because of a fear of inflation at a time that commodity prices and petroleum prices were increasing.

The Chair: Thank you very much for your presentation.

We'll now hear from Mr. Wright, please.

Mr. Craig Wright (Senior Vice-President and Chief Economist, RBC Financial Group): Thank you, Mr. Chair, and committee members. I appreciate the opportunity to be here and I look forward to the Q and A session.

To pick up after Steve's comments, there is a wide range of estimates in terms of the impact. I think it's somewhere between a small negative to a bigger negative, the more bearish view seems to come from the Bank of Canada. Our view is that it's a small negative, which I think is closer in line with the Department of Finance estimates federally.

When we look at the feed-through effects, there are three things we look at. What's the cause? As Steve suggested, it's different if it's from the supply side than from the demand side. We think much of what we're seeing is the excess supply, and price is corrected. On the demand side, if it were a demand shock then you'd get the follow-through with weakness in demand for all our exports, and not just energy, and it spreads across and it's more negative. Then there is also the depth and the duration.

Often what you find is that the best cure for low oil prices is low oil prices because the markets respond. What you see is that the demand picks up. Many countries produce oil, but all countries use the output of oil. We also see the supply cutbacks, and we've seen some data on the rig counts that suggest it's already taking place. That sets the stage for recovery in oil prices. We think that will take place as we move through the second half of this year and into next year. That's the economics of oil prices. Of course the politics of oil prices is dramatically different and that's what is keeping uncertainty high.

When we look at the impact on the economy we look at the real impact and the nominal impact. On the real side, it will be a negative for energy investment. That will be the negatives that we hear from Newfoundland and Labrador, from Alberta, and to a lesser degree from Saskatchewan.

There are offsets. What we think is that it acts as a significant tax cut for consumers, particularly in the U.S. The U.S. consumers will spend that money and that's going to lift exports for Canada. It's also positive for Canadians. We also see more money available that doesn't go in the gas tank. It goes to spending on other goods.

It's also consistent with the weakness in the Canadian dollar. There is a great deal we don't know about what drives the Canadian dollar, but over a long period of time you do see a fairly tight relationship to oil prices and to commodity prices more generally in the Canadian dollar, so a more competitive currency. That view of those offsets suggests we'll see better news on the export side, a little firmer consumer spending, and non-energy investment should pick up as we move forward.

The nominal side is where the big impact comes from, and that's the price of what Canada produces. The price of what we produce is getting weaker, so we do see nominal GDP get softer. That translates into weaker corporate profits and weaker government revenues. The potential spillover to the economy from that depends in part on what corporations do in terms of job cutbacks or what governments do when the revenue line looks a bit weaker. Are there significant tax hikes or significant spending cutbacks? I think that's the risk, going forward.

If you look at least at the provincial level, most of the provinces that have been hit are fiscally more sound than what we see in other provinces. I think the federal numbers are safe in terms of surpluses as we move forward.

The risk, as suggested earlier, is that the negatives are known in near term, and that the offsets are less certain and appear in the medium term. That's keeping uncertainty relatively high.

● (1625)

The Chair: Thank you very much for your presentation.

We'll go to Mr. Cullen, for a five-minute round.

Mr. Nathan Cullen (Skeena—Bulkley Valley, NDP): Thank you, Chair. Thank you to our witnesses. I find this incredibly engaging, trying to understand what the indicators are showing us.

I want to clear something up first, and it was a bit of a C.D. Howe fight that I think we had going on here, or “debate” is what I meant to say.

In your report, Mr. Ambler, I think you talked about this and I want to compare it to what Mr. Cross said about the time it takes for the impact to be felt on natural resource industries.

Mr. Cross, broadly speaking you said that the natural resource sector doesn't react to a price change like this in the most immediate and quick turnaround.

But in your report, Mr. Ambler, there was a consensus that:

> In other words, the negative impact may be faster than traditional models would predict because companies are quickly adjusting their capital plans.

I don't know if there is a contradiction, but just in your testimony today, Mr. Cross, you talked about there being a slower tendency within the natural resource sector to come off of certain investments.

Mr. Ambler, the consensus out of the economists you spoke to talked about this particular uniqueness of the sector, being able to ratchet back much quicker, and feeling those negative impacts faster.

Am I reading what you said right, Mr. Cross, or am I getting it wrong?

Mr. Philip Cross: First of all, let's clarify the situation here. Steve is here in the position of speaking officially for the C.D. Howe Institute; I am speaking as an individual. I happen to be a research fellow at C.D. Howe, but I did not coordinate my response, as you may have noticed. I don't think it's actually in contradiction.

What I am saying is that you don't see the cutbacks. When there was a recession in the housing and auto industries in 2008-09, housing starts fell 35%, and auto assemblies fell 35%. Oil output is not going to fall 35% this time around.

Mr. Nathan Cullen: There is too much momentum in the system.

Mr. Philip Cross: It's not so much that there is too much momentum, as that oil is so capital-intensive. Once you turn on an oil sands plant, you never turn it off, except under the most extreme circumstance.

● (1630)

Mr. Nathan Cullen: You do cancel future—

Mr. Philip Cross: What you will see is, immediately, a cutback in investment. In 2008-09 we saw both auto output and investment by the auto industry fall precipitously. This time around in the oil industry, you will see little or no change in output, but you will see a big drop in investment. The investment will lead to lower output in the future, but you won't get that output response right now.

The Chair: Colleagues, the bells are ringing. Can I assume consent to continue for the time being?

Some hon. members: Agreed.

Mr. Nathan Cullen: Thank you, Chair. Thank you for that, Mr. Cross.

This debate going on about whether this is a supply-side or demand-side reaction seems.... We are dealing with economics so we are not seeking consensus, but the best appreciation and understanding of this one issue would be fundamental in then determining what actions the federal government may take in a budget.

Is there any correlation between understanding what the cause of this price drop is, and being confirmed in that position, and the type of budget you would suggest being drawn up, or are those two things unrelated?

If it's the supply side, does that change the scope and nature of any budget initiatives or economic initiatives the government may have? If it's the opposite, does it change it as well?

Mr. Craig Wright: I had mentioned the supply imbalance rather than demand.

I think if we look back through 2014, we see supply running ahead of demand. It wasn't a huge gap, as was suggested earlier, but we saw prices sort of drift lower, and that made sense. As I suggest, that would sow the seeds for an eventual recovery in oil prices. If you look at some of the surveys and inputs into the budget forecasting process, whether provincially or federally, the baseline forecast was a recovery.

Then what we saw—or didn't see, more correctly—was that, on November 27, things were softening up. The OPEC meeting was November 27. OPEC does what OPEC usually does, and I think that was the working assumption everybody had. However, they didn't, because of the concerns or the conspiracy theories, or whatever was driving it. That's why I think the outlook for oil is even more uncertain than typical, because it is not necessarily just about the economics; it's about the politics.

Mr. Nathan Cullen: Someone in our last panel said this is the biggest reaction to a non-event, which was the Saudis talking about an extra 300,000 or 400,000 barrels a day. The markets responded, and we've seen this. The political nature of this is important, because it affects the economics and the economic output.

If economics was left to its own devices, if the market was left to do what it would do, the commonly used expression “the solution to low oil prices is oil” would be true. Does adding in the geopolitics to this—the Saudis, the Russians, etc.—not create the potential at least for a longer-term experience of these $50-a-barrel prices? Is that a reasonable assumption to make, mixing those two things together?

Mr. Craig Wright: Yes.

Prof. Steven Ambler: Indeed.

There are a couple of people on the council who have speculated about the fact that there are some countries, notably Russia and Iran, to the extent that it's not subject to sanctions, that basically have fixed requirements to meet in terms of income from royalties. The speculation is that countries like Russia and Iran might actually have a downward-sloping supply curve for oil. This is politics, right? As the price goes down, they have to pump out more of the stuff to meet their revenue requirements.

Mr. Nathan Cullen: Keeping oil prices lower still, or at the same rate.

Prof. Steven Ambler: Exactly. This certainly adds to the uncertainty.

Mr. Nathan Cullen: Thank you.

The Chair: Thank you, Mr. Cullen.

We'll go to Mr. Saxton.

Mr. Andrew Saxton (North Vancouver, CPC): Thank you, Mr. Chair.

Thanks to our witnesses for being here today.

I'll be splitting my time with Ms. Bateman.

My first question is for Steven Ambler of the C.D. Howe Institute.

Mr. Ambler, is this oil price drop peculiar? Is it different from price drops in the past, or is it following the characteristics of previous price drops?

Prof. Steven Ambler: I think there are structural differences. I mean, it has dropped more quickly and farther than previous oil price drops.

Craig brought up OPEC. The share of OPEC's production in total world oil output has actually fallen quite a lot. Even if the Saudis wanted to clamp back on their production to drive oil prices back up, OPEC doesn't have as much of an influence on world oil prices anymore.

I think there are differences.

● (1635)

Mr. Andrew Saxton: Thank you.

Craig, I have a question for you as well.

What impact do you think this oil price correction is going to have on Canada's GDP this year?

Mr. Craig Wright: We have a small negative impact in terms of real GDP. As I suggested, the negatives are clear and they'll show up soon, and that's why most people have had a soft first half of the year. The positives, in terms of exports growth and investment outside of the energy patch, will show up with a bit of a lag. We think a good part of that will show up in the manufacturing sector. If you look at the rebalancing across provinces, people are taking Alberta and Newfoundland and Labrador lower, and lifting Ontario, reflecting that pickup in manufacturing given the U.S. economy and the more competitive Canadian dollar.

We have a small negative hit for real GDP and a bigger nominal hit for the dollar value of what we produce.

Mr. Andrew Saxton: Finally, what is your prediction on oil prices three years from now?

Mr. Craig Wright: We have them moving higher.

On an annual average basis for this year, we had $53 a barrel, and then next year we have $77 a barrel. We think that in that soft first half of the year we could even drift lower from where we are today, just sub-$50, and then a recovery as we move through the second half of this year and into next year. In the long run, we're still of the view that the cruising speed for oil prices is higher.

In the old days, we used to think $25 a barrel. OPEC targeted $22 to $28. Now we think, given the divergent growth around the global economy and higher costs of capital, labour, smaller finds, and the like, it's probably something higher, maybe in the $70 to $80 range for the long run.

Mr. Andrew Saxton: Thank you very much.

Ms. Joyce Bateman (Winnipeg South Centre, CPC): That's wonderful.

Thank you all for being here, and please accept our sincere apologies for the compression of time.

Mr. Cross, you spoke about the cyclical nature of the industry and referenced other times that there have been incredible fluctuations, but then you made the comment that price isn't the only thing going on in the longer term. I'm wondering if you could expand on that for me, sir.

Mr. Philip Cross: Sure.

I think it is quite revealing. Going back to the old phrase “never waste a good crisis”, this industry didn't waste the crisis in 1998. Even as oil prices were falling, I think down to $10 a barrel during that period, the industry undertook its remarkable shift from conventional to non-conventional production. That was because they switched technologies. They were using the old bucket wheels at the time to extract oil from the oil sands, and somebody hit on the idea of scraping this off and putting it in big trucks and delivering it directly to the upgraders. At the same time it was made more profitable by changes to Alberta's royalty regime that were adopted in 1998.

We do tend to fixate on prices. It's not just that. There are other technological changes going on in this industry. Over half of all oil production in Canada now is coming from the oil sands, but within the oil sands, soon over half of oil sands production will be in situ with the steam-assisted gravity drainage. Every time there's a picture of the oil sands now in the papers, you always see the monster trucks and everything, and soon we're going to have to update those pictures. It's going to be a quite different industry—much less visible in the future.

Ms. Joyce Bateman: Craig, perhaps you could speak to this positive upside as well.

Mr. Craig Wright: Briefly, if you look at the 1998-99 episode, we saw a much sharper price decline. Peak to trough, oil prices fell 70%. *The Economist* had that sub-$10 oil on the cover. This time around we've peak-to-trough fallen just over 50%, so it's less dramatic.

In the 2008-09 period, there was the financial crisis, so credit was tough. There was the uncertainty with global recession, depression, deflation—all these big ugly stories out there—and notwithstanding all of that, you did see Alberta oil production in that period rise.

To the earlier comments that we've seen a switchover, there's never a good time for a shock like this, but we are seeing more of a play from the non-conventional than from the conventional. These are 40-year to 50-year production phases, and in that period, they would be accustomed to some ups and downs. We're a little more insulated now relative to where we were only a short time ago.

● (1640)

The Chair: Okay. Thank you.

We'll go to Mr. Brison, please.

Hon. Scott Brison (Kings—Hants, Lib.): Mr. Locke, a lot of Atlantic Canadians work in the oil industry, in the oil sands, and as such are paying provincial income taxes in our provinces as well as paying their mortgages and car payments, and the rest of it. That's a significant part of our economy. Have you done some analysis as to how big a part of our economy that is, and how vulnerable provincial governments and our economies are to layoffs in this sector? For instance, Suncor has announced 1,000 job losses. Have you done some consideration as to the impact of that revenue and that economic benefit as a result of those people working in the oil industry?

Prof. Wade Locke: We are in the process of doing specifically that now for Newfoundland. In terms of people working in Alberta, about 25,000 Atlantic Canadians is the most recent number from Stats Canada, so it's a substantial number. It's the fly in, fly out people who would be adversely affected, and it will have a dramatic impact in rural parts of your province and rural parts of our province, specifically Cape Breton and on the west coast and south coast of Newfoundland.

Hon. Scott Brison: Sure, people are on the planes with me every Monday morning on early morning flights connecting through Ottawa on their way out west.

Mr. Cross, you said that a positive outcome could be that the Alberta government could be going through a fundamental reassessment of its overall fiscal strategy. The Alberta government is introducing a budget on March 26. You didn't mention the federal government. It appears they're going through a bit of a re-evaluation of their fiscal strategy as well. I'm just curious as to why you wouldn't mention the federal government, which is actually delaying a budget as a result of falling oil prices.

Mr. Philip Cross: I didn't mention them because I didn't think the issues were as large for the federal government as the Alberta government. On the idea, for example, of Alberta potentially adopting a sales tax or making better use of its heritage fund, the situation would seem to call for a much more...I don't want to use the word “dramatic”, but a much more fundamental response from the Alberta government. I don't think there's the implication in this that the federal government needs to fundamentally re-evaluate its strategies. Not that much money is implicated here for the federal government.

I'll just get back to your previous question about the interprovincial aspect; that's something that has bedevilled StatsCan. How many people working in Alberta fly out from Newfoundland? We really have no way of measuring that. It's something we discuss internally a great deal. If in the survey week, you're in Alberta, and we catch you there, and you answer the survey, well, you're down as Alberta. If we capture you in Newfoundland, in your off-week, we just ask, “Do you have a full-time job?” If you say yes, then you're going to show up as employed in Newfoundland. It creates real problems for statistics, and statistics aren't as nice and cut and dried as a lot of people think. It's a messy business out there.

Hon. Scott Brison: It would be helpful to have that information to understand the relative vulnerability of various provinces, and Revenue Canada ought to be able to give us some idea in terms of where people are actually filing their taxes.

Mr. Philip Cross: I think that's more likely to be your better source of that, because they're going to ask where you earned this money. That's going to be reported by the employer and that's going to be different in the province of residence.

Hon. Scott Brison: You've said that, in fact, there's not as large a reason for the federal government to re-evaluate its fiscal plan. Any idea why they're delaying a budget, in that case?

Mr. Philip Cross: Coming from Statistics Canada, I've been very far removed from the policy process over the years, and I feel very comfortable and happy with that.

Hon. Scott Brison: In terms of the impact of the drop in WTI on GDP, and then on government revenue, recognizing it's not a linear formula, there's been some analysis that a dollar drop in WTI would lead to about a billion-dollar drop in GDP, depending on where it is in the curve. But certainly for each dollar, there would be a drop commensurately in terms of federal government revenue.

The federal economic update in the fall was based on $81-a-barrel oil. What do you think the impact is going to be on federal revenue, based on current levels?

● (1645)

The Chair: And who is that to...?

Hon. Scott Brison: It's to Craig.

Mr. Craig Wright: I think the sign is correct. As I said, nominal GDP feels the effect, and there is a range of estimates again for nominal, so in the prebudget meeting with the minister we'll have all our latest forecasts out there. For nominal GDP, last year it grew by just under 4.5% and this year we have it just under 2%, so we're looking at a two percentage point hit to nominal GDP, which will translate into roughly a similar magnitude.

The federal government has the fiscal sensitivity tables, as you're well aware, and you can work through the fiscal sensitivity for a 1% drop in nominal GDP. So we're at 2% relative to where we were a short while ago and I think that's probably the way to go about it. Then you can work that through the math and the fiscal numbers.

Our own view is that given the starting point, we have nine months of the data for the fiscal year just ending this March, and it's about $11 billion ahead of what it was for the same period last year, so there is a cushion built in there, plus there is also the adjustment for risk, which is exactly for these sorts of surprises.

The Chair: Okay, thank you.

Colleagues, we have about 14 minutes until votes. I'm going to recommend that as long as one opposition member stays I will stay in the chair and keep the meeting going. If members want to come back after the vote, they can. I'm not going to hold members here, but frankly, this discussion is interesting. As long as we're somewhat paired we can stay, but I'm not holding members. We have three opposition members. We have a number of Conservatives. As long as one opposition stays, I will stay and I will let the rest of you pair as you see fit, or not.

We will go to Mr. Van Kesteren, for your round, please.

Mr. Dave Van Kesteren (Chatham-Kent—Essex, CPC): Thank you, Chair.

I have to tell you that I have been looking forward to this, to get the economists here, and the one thing that strikes me more than anything else is the relative calm that you have. I think most Canadians in general are a little bit nervous about these oil prices. These are uncharted waters. They are not necessarily uncharted. We've seen this, but it's comforting, I suppose, to some degree to feel that from you because it's something that I was a little bit nervous about, I must say.

I have a few questions that maybe you could clarify for me. I'm wondering where more of a negative effect would be felt. Would it be felt more in the shale gas production in the U.S. or in the oil sands and the offshore? Which area would have more of a negative effect?

I throw that out to anybody.

Mr. Cross, you look like you want to answer.

Mr. Philip Cross: I'll jump in. The oil sands have 30-year to 40-year production. You and I could start a business for shale oil. For $1.5 million to $2 million, we have our little fracking operation going. That money can be turned off pretty quickly. With oil sands, you're talking about billions of dollars committed and the investments are all made up front. That's why I say that once you've made the investment you have no incentive to turn it off. You've already incurred all the costs and you need the revenue to pay it back.

I would think that because of the lower upfront capital cost, the shale is going to be more vulnerable than the oil sands.

Mr. Dave Van Kesteren: The other thing I find rather surprising is the lack of consensus as to what exactly is going on. I'm certainly not an economist, but I dug into this as much as possible and I really can't say that I've hit on anything that would answer why this is happening.

I suppose one of the questions I would ask is if it were a reaction to the Saudi attempt to drop shale production—you sort of answered, but I want a clearer answer—isn't it something that they could easily correct just by shutting the taps just a little? It seems like there isn't a whole lot of fluctuation that's causing the price drop. Isn't it something they could correct rather quickly?

The Chair: Is this for Mr. Cross?

Mr. Dave Van Kesteren: It's for anyone.

Mr. Philip Cross: Craig would like to say something.

Mr. Craig Wright: I'll just follow up on Mr. Cross' comments on the shale plays. It is relatively less capital intensive, but once you get it going you have to keep it running, and it's a higher-cost play so that break-even price is higher for shale than for others. With shale gas, a lot of the capital raised comes from credit markets. So it's not just a price correction, there has also been some tightening in credit because they tend to go to the high-yield market. They're getting hit both by the soft price, below their break-even price, but also by the fact that the capital market, the access to credit, has tightened up, which isn't the case across the rest of the globe.

● (1650)

Mr. Dave Van Kesteren: Isn't it something that, if there is manipulation in the market...?

I think, Mr. Locke, you were—

Prof. Wade Locke: I was just going to say, to answer your initial question, that it depends on how long you think the price change is going to be for. If you think it's a short-term phenomenon, then the reaction will be somewhat different from what it would be if you think it's going to be a longer-term phenomenon. If you think the price is going to be $50 to $60 for a long period of time, that will change the reaction for many things.

It is true that shale can start or stop more quickly. In fact, what has happened is that the shale plays have drilled their wells and have not completed them, because two-thirds of their cost is in completion. If you believe prices are going to go up, you may as well wait six months, spend one-third, and.... What some people don't understand about shale is that half of your shale production occurs in the first three years, so if you believe prices are going to go up and half of your production is done in three years, you may as well wait for the price to go up.

But it comes down to how you react to price falls. It depends on whether you believe it to be a short-term, a medium-term or a longer-term phenomenon. If it's a longer-term phenomenon, many of the projects that might go forward—not currently operating but that might go forward in the future—won't go forward.

Mr. Dave Van Kesteren: Okay. I have one minute left, and this question is the one I really wanted to ask more than anything else.

That's the one side of the equation. The other side of the equation is that real production is dropping, that GDP is dropping worldwide. Do we have the real numbers for the production happening in China?

The other part I want to ask is: how much are the numbers we're getting out of the U.S. something we can really bank on as well? Do we know the actual numbers in China? Do we know the actual numbers in the U.S.? Is this just the result, possibly—and Mr. Ambler, you look as though you want to jump in on this one—of a real drop in production in the world?

The Chair: Make just some brief remarks on this.

Mr. Cross.

Mr. Philip Cross: I'll take a stab at it, being a statistician. Statisticians love these industries in which you have a small number of producers. Basically, it's an oligopoly. The dream industry for StatsCan is the auto industry. Survey six industries and you have a census.

These are large firms. I think the data is extremely good. Wherever you go, the industry collects very good data on this. It's a small number of people that you have to survey. I think there is extremely good data in North America and indeed around the world on this. It's one of the best industries in the world, right up there with autos.

Mr. Dave Van Kesteren: Okay, thank you.

The Chair: Thank you very much.

We'll go to Mr. Cullen.

I think, Mr. Cullen, that you and I will just swap five-minute rounds.

Mr. Nathan Cullen: That sounds good. It sounds great.

I want to turn to manufacturing for a moment. We've spent a fair amount of time on the oil side of things, but part of what this committee is attempting to do in, as you can see, an incredibly constricted manner is to get a snapshot sense of where the Canadian economy is and what the federal government response should be, because that is where, as policymakers, we are.

I very much take the advice given about the mistakes, in the U.S. example and some other examples, of overreacting. However, turning to manufacturing for a moment, I want to get your sense of where you see the state of affairs to be.

Allow me to put two things in context first. One is that we have lost a significant number of manufacturing jobs in Canada over the last six, seven, or eight years—400,000 according to StatsCan, I believe. That's the number that we use. The scenario of a low, 80¢ loonie and a 4%-plus growth in the U.S. market typically and traditionally has meant a quick response on the Canadian manufacturing side; our products are cheaper and there is an American consumer looking to buy.

Two factors concern me about this. Have we hit a structural impasse on the manufacturing side? We saw production increase last year but did not see a great deal of uptake on employment. Second, the Canadian consumer seems to be perhaps getting double-hit in this particular scenario, in which any imports are more expensive to buy and consumer debt load in Canada is incredibly high, historically high—is that right, Mr. Cross?

Mr. Philip Cross: Totally.

Mr. Nathan Cullen: Okay. So we have a very high debt load being borne by Canadian consumers. What are Canadian manufacturers, Canadian value-added companies looking at right now? Is the net impact of this particular scenario—low energy prices, low oil prices, and a lower loonie—good for Canadian manufacturing? When are we going to see the hiring come back of the 400,000 who have since been laid off? “Are we going to?”, I suppose, is a fairer question.

● (1655)

Mr. Craig Wright: Maybe I can start.

We did a report on the outlook for the manufacturing sector in light of the decline in oil prices and we took on board some of the considerations, that it is more the structural change that made the manufacturing industry different, insomuch as it is not positioned to recover through this period.

What we found is that the auto sector—15% of the Canadian economy—is running up against capacity limits. If you look at capacity limits as being pre-crisis levels, the auto sector is already back there. But they could always lengthen shifts and run a bit longer, and then, if that doesn't work, they invest, which is—

Mr. Nathan Cullen: Do they have room still?

Mr. Craig Wright: Yes.

Mr. Nathan Cullen: We've seen some recent auto investments, but before they start hiring in thousands of workers....

Mr. Craig Wright: Yes. The other side is that there is also 85% of manufacturing that is not the auto sector, and that's the area where en masse I think 15 of the 16 industries we look at are running below pre-crisis levels in terms of capacity utilization. In terms of when such utilization levels show up, I would argue that we've already seen some evidence of that. We saw it through last year, with manufacturing shipments up just over 5.5% after being flat in the previous year.

Then manufacturing relative to size of GDP, to speak to your comment on the restructuring, has continued to move lower, from about 16% of the economy to around 11% from 2002 to today. One thing that took place through that period, besides the global recession that we had, was the trend appreciation of the Canadian dollar. Now, as we move forward, a stronger U.S. is the bigger story. The volume matters more than the price, but the currency is moving in the right direction as well. I think that's why we'll see a bounce in manufacturing as we go forward. It has already begun.

Mr. Nathan Cullen: But your outlook is not to see a bounce back to, say, 2006 levels.

Mr. Craig Wright: No.

Mr. Nathan Cullen: You're not imagining the 400,000 jobs coming back—

Mr. Craig Wright: No, I think there's a cyclical story and a structural story.

Mr. Nathan Cullen: I see.

Mr. Craig Wright: We have a cyclical bounce and a secular decline for manufacturing.

Mr. Nathan Cullen: A cyclical bounce...

Mr. Craig Wright: And a secular decline.

Mr. Nathan Cullen: Okay.

Prof. Steven Ambler: As well, there has been a secular decline in the share of manufacturing and total output, but there is a big distinction between the share of output and employment. This is, I think, true across all industrialized economies. It is just a fact of life that manufacturing is enjoying productivity increases, so you can produce the same amount of stuff with fewer people. Whether or not manufacturing output comes back, it's certainly the case that employment is not going to come back. The case is the same for Canada as for the U.S., as for the U.K.—overall.

The Chair: Monsieur Bernard.

Prof. Jean-Thomas Bernard: I wanted to mention that the pulp and paper industry in Canada, which used to be a huge industry, is still decreasing. It will not bounce back in the near future, because there is a structural shift towards other ways to transmit information.

Now, there has been a huge revival of the manufacturing sector in the U.S., but I don't expect this to happen, at least not to the same extent, in Canada, because the revival in the U.S. is basically due to the fact that they have access to really cheap gas through shale gas. This has created a huge revival for the chemical industry. I don't expect something like this will go on in Canada.

The Chair: Mr. Cross.

Mr. Philip Cross: One other thing is that I wouldn't expect as strong a response now as before 2008, because one way manufacturing survived and adapted to the high dollar over the last decade was that they oriented away from U.S. export markets and towards supplying energy industries out west. That demand is not going to be as strong, obviously. We still have a great deal of exposure to U.S. exports, but not as much as before. So the bounce back that you're going to get in manufacturing won't be as strong as in the nineties, for example.

Mr. Nathan Cullen: My very crude understanding of this has traditionally been that what is good for the resource sector, especially the oil sector—being able to sell oil at a higher loonie and having strong global production—when it offsets, when prices for energy drop and when the loonie also drops, it is rebalanced out within the Canadian economy, historically. I emphasize the crude aspect of my analysis.

Yet when you talk to me about the structural changes—the secular decline—plus the fact that a great deal of manufacturing in Canada was also wedded to the resource sector, if those investments come off and there is a structural decline within manufacturing, that rebalancing in the economy.... It's not as if you lose jobs in the oil patch and then pick them back up in Ontario and Quebec, as maybe you would have 20 or 25 years ago.

● (1700)

Mr. Philip Cross: I really resist the idea that resources and manufacturing are in opposition to each other in this country.

Mr. Nathan Cullen: It's not that they're in opposition, but that the factors in play for both of them sometimes have opposite effects. A higher loonie has an effect on the resource sector—

Mr. Philip Cross: Remember too that our manufacturing sector has changed over the last decade quite significantly. Clothing is gone. The forestry-based industries—lumber, pulp and paper—are not coming back to anywhere near the level they used to be. There have been structural shifts.

What has replaced them is.... More than half of manufacturing now is resource-based—the big petroleum refiners, the chemicals, the primary metals—or the capital goods. There has been quite a shift in the manufacturing industry, so that much more it moves in line with the resource sector.

Mr. Nathan Cullen: They go together.

Mr. Philip Cross: Or important parts of it move in line.

Of course, there's still a very important auto industry, and industries that benefit from the lower dollar and the pick-up in the U. S. economy. It's just not as big a part of our manufacturing industry as it used to be.

The Chair: I want to follow up on a question Mr. Cullen raised.

Are any of you concerned that the manufacturers did not take advantage of the higher dollar to update their machinery and equipment at a time when they should have been doing that? They may now have the benefits of the lower dollar in terms of exports, but obviously, in terms of buying machinery and equipment from the U.S., it's more expensive.

Mr. Craig Wright: Last week I believe, Statistics Canada released the latest numbers for labour productivity in Canada, and over the last five years, Canadian productivity is actually above the U.S. productivity numbers. That's with one year of zero.

In 2014, labour productivity was up 2.5%. We've been looking for, and hoping for, that rebound in productivity for some time. There's a lot we don't know about what drives productivity, but generally what you find is both an absolute and a relative rise in investment. The absolute but also the relative size of the economy is usually a good precursor for a pick-up in productivity.

When you look at the post-crisis-period investment, growth in Canada is right up there next to the U.S. within the G-7. So I think we did undertake a fairly sizable investment over the period, which is perhaps finally starting to show some dividends in terms of productivity. With the currency, that labour cost number is a competitive challenge. It's still a challenge, but it is less than it was only a short while ago.

Mr. Philip Cross: I agree with that, and would add that I think your perception is based on what happened before 2008. There was a reluctance to invest because a lot of industries were basically going out of business, in clothing, paper, and so on. Then, of course, there was the big recession in 2008-09. Nobody was going to invest in Canadian manufacturing in the middle of that chaos. But since 2009, investment has increased every year in manufacturing. It's almost back to its pre-recession level. It's related to the restructuring that's been going on in the industry and the fact that the growth has been in resources and in the capital goods industries.

But I entirely agree that there's been a lack of appreciation of how much restructuring manufacturing has gone through, and the fact that productivity is doing well compared to American manufacturing. We need to update our narrative on this.

The Chair: I appreciate that.

The second issue I wanted to raise, Mr. Ambler, is in the C. D. Howe report. It says:

> One Council member recommended that the Bank clarify whether it attributes the recent fall in oil prices to supply effects or to demand effects.

If you look on pages 7 and 8 of the information Mr. Locke has presented to the committee, and if you look at the increase in production in the United States in particular, it seems to me, on the face of it, it's supply effects. It's not demand effects.

Would anyone like to comment on that, or does anyone believe it's demand effects rather than supply effects that have caused the dramatic price drop?

● (1705)

Prof. Steven Ambler: I think it's a bit of both.

My understanding is that there's been a huge, unplanned accumulation of unsold petroleum. You hear at least anecdotal stories of ships being hired and then basically sailing around waiting for stocks to deplete. I think there is something happening on the demand side, as well.

Yes, there is a fracking revolution, the shale gas revolution, so there's been a shift in the supply curve to the right. But I think growth in demand due to weaker growth overall in the world economy has played a part as well.

The Chair: Okay.

Does anyone else want to comment on that?

Prof. Wade Locke: Clearly, the supply-side impacts have been bigger than anybody anticipated. Demand has been growing, just not as quickly as people originally thought. Most of the effects are demand driven. As for people using tankers for storage, those cases have been going down.

Right now, as I said in my presentation, if you look at the most recent drilling report that came out two days ago from the EIA, we will start to see a fall in production come April. The expectation is that the productivity people talked about for shale can't keep up with the fall in the rigs. The expectation is that, while inventories are building up in the States and elsewhere, they're expected to start to come down.

The Chair: Very good.

Prof. Jean-Thomas Bernard: The period of 2010 to 2014 has been very unusual in the oil industry in the sense that we had very high prices—about $105 per barrel, sometimes a bit more at $110 and sometimes a bit less—in terms of historical periods. We have to go back to the oil shock of 1979 before we hit that same level.

This was very high and not only high, but stable. Somehow people in the industry and the government came to the view that the prices were high and would continue to be high and also stable. This is not the reality of the oil price when you look at it over a longer period.

We are getting back to the usual way of the industry. This unstable high price boosted supplies to levels that were not met by demand. That's why the price collapsed.

The Chair: I'll just pop in one last question.

Mr. Wright, I think you said the best thing for low oil prices is low oil prices. I sort of posed the question yesterday.... I think you've heard some of the comments today that if the Saudis and OPEC simply adjusted some of their behaviour that this would be the biggest thing that could impact the price in the short term.

Yesterday one of the witnesses said the Saudis don't have the policy levers that they used to because of the changed dynamic and the changed makeup in terms of who our global producers are today. Would you agree with that statement or is there any disagreement with that?

Mr. Craig Wright: I think when you look at the why the Saudis didn't do what they typically do last November, there are a number of a different theories for it. My thinking is that it's in light of the U. S. shale build up that we've seen. Obviously the U.S. isn't oil independent, but they're relying on less oil and their imports are continuing to drop relative to overall consumption.

The Saudis are more sensitive to losing market share elsewhere like in China and onwards. I think they are trying to drive out, even within the OPEC group, some of the higher-cost producers. Their break-even price in Saudi Arabia is somewhere close to $10 a barrel, but their fiscal break-even price is a lot higher because they do have a fairly sizeable spend on the social front in Saudi Arabia. They're living off the earlier surpluses and there's a limit to how long that can take place. I think it's mostly a market share game, and even Saudi Arabia has a limit on how far they can run with that.

The Chair: Okay. I appreciate that.

I'll go back to Mr. Cullen.

Mr. Nathan Cullen: Thank you.

I enjoyed this committee, this is....

The Chair: Yes, it is. I think we're going to run it like this from now on.

Mr. Nathan Cullen: Yes, we may have a few more votes.

We do appreciate this. There were a number of us who thought to have this type of expertise at the panel and then be popping in and out of votes and not using your insights was going to be a shame, so thankfully all of this is being recorded and we're bringing it in.

I want to pull a little further back in terms of job growth expectations for this year. We saw what some have called relatively anemic growth last year in 2014 at 0.7% or 0.8%. Combine that with, as CIBC pointed out recently, a generational downturn in job quality in Canada.

I'm going to assume this $50 barrel and 80¢ loonie for current circumstances, and we can all look for a climb depending on what the Russians may or may not do. Given this current circumstance what are your expectations for the Canadian economy going through the rest of this year in terms of potential job growth with this as one of the factors? Does this improve job growth perspectives across the economy or diminish the expectations that you had for this year?

Anyone have some insights on that?

● (1710)

Mr. Craig Wright: As to our employment outlook, this year we have a slight acceleration as you mentioned. There was lacklustre growth last year on a monthly basis and it was about 10,000 jobs on average each and every month. We had a pretty strong January and we'll get the February numbers this Friday, but we see it moving.... We have growth at 2.4% this year, so to us that suggests somewhere between 15,000 to 20,000—

Mr. Nathan Cullen: Is that 2.4% readjusted?

Mr. Craig Wright: That is our current growth forecast.

Mr. Nathan Cullen: Is that adjusted downwards?

Mr. Craig Wright: We do quarterly forecasts and our next round comes out tomorrow. It's a full macro with global, U.S., Canada, and then provincial numbers. We only do provincial on a quarterly basis. From December in our last quarterly forecast to tomorrow's forecast, our growth forecast comes down from 2.7% to 2.4%.

That is a bit above trend. Unless we get this productivity on a sustained basis, our speed limit's in and around 2%. As long as the growth in the economy is a bit stronger than the speed limit, we'll see the unemployment rate continue to drift lower. We think trend growth, if the economy is at 2.5%, is around 15,000 a month.

Mr. Nathan Cullen: You mentioned the strong January, but does your forecast concern itself with what kinds of jobs are being created? We saw a net loss of full-time employment, a net gain of some 50,000-odd part-time and—

Mr. Craig Wright: You could look at it every which way. I tend to look at it on a year-over-year basis. Then you could look at it over a post-crisis period. What we found is that just over 80% of the job gains over a post-crisis period or over the most recent year have been full time rather than part time. They also tended to be more private sector than public sector.

Self-employment's also been up. I think that's probably a demographic challenge. As we go forward we're going to see more people staying engaged in the labour market longer, and that suggests to us that self-employment may not be a bad thing at all. To me, any job's a good job.

Mr. Nathan Cullen: Sure. But traditionally part-time employment and self-employment were considered, broadly speaking, as more precarious. No? Not from the bank's perspective?

Mr. Craig Wright: I don't share that view.

Mr. Philip Cross: I'll jump in on this one.

I wrote what you could call a high-spirited op-ed in the *Financial Post* yesterday on the CIBC jobs report. First of all, part-time and self-employment peaked 20 years ago. It's been a declining share of employment over time. So the idea that jobs are shifting into this precarious labour force, no, it doesn't work. This index is not something Statistics Canada would ever produce. Conceptually it's a very weak index.

Mr. Nathan Cullen: Those are fighting words, Mr. Cross.

Mr. Philip Cross: And I'm pulling my words now compared to the op-ed. I would bring your attention to that op-ed.

Mr. Nathan Cullen: I will. I think the finance minister called it a sham economic picture.

Mr. Philip Cross: One of the problems in our society is the growth of pseudo-knowledge and sham data. I think that's what I called it.

Mr. Nathan Cullen: You were quoted yesterday in the House, were you not?

Mr. Philip Cross: I don't keep track of the House.

Mr. Nathan Cullen: I think you were, by the finance minister himself.

The Chair: It's a great line of questioning.

Mr. Nathan Cullen: Are you enjoying this?

Mr. Philip Cross: When you think about it, adult unemployment in this country is below 6%.

Mr. Nathan Cullen: Is that the real unemployment number?

Mr. Philip Cross: The adult unemployment number.

Mr. Nathan Cullen: Is that the actual number of unemployed adults or is it...? Does it include people who have given up looking for work, people who are long-term unemployed?

Mr. Philip Cross: No.

Mr. Nathan Cullen: Okay.

Mr. Philip Cross: But it's at an historically low level. You could argue about that level.

I think the number I cited was that almost all of the growth in the last four years has been in jobs over $20 and especially over $30 an hour. I look at data like that and I just think, how can you tell me job quality is the worst ever? Not just low, but the worst ever, worse than 1982, worse than in 2008. At Statistics Canada if somebody had put something like that in front of me I would say, you have to be kidding.

I would encourage you to find better measures than that particular index.

● (1715)

Mr. Nathan Cullen: CIBC's feelings are eternally hurt now. They're never going to produce another estimate again.

I want to go to Mr. Locke. You talked earlier in your testimony about a 1% to 2% oversupply across a 60% price drop. Is that accurate? I'm trying to think of another commodity that's that sensitive.

Prof. Wade Locke: That's what happened here. We're talking about one to two million barrels a day, based upon a 93 to 94 billion barrels a day production, and the price dropped by 60%.

Mr. Nathan Cullen: But to drop another 1% or 2% wouldn't cause a further 60% drop because it's not in combination with...or would it? I'm trying to think of other commodity prices, other natural resource products that would drop.

Prof. Wade Locke: That drop is not consistent with the elasticity of demand.

Mr. Nathan Cullen: Okay.

Prof. Wade Locke: These were all coming through demand effects. Demand elasticity is in a range of 0.1, so we would expect to clear a 2% oversupply. A 20% drop in price will clear that because it's all coming through demand. So if there are any supply effects, you would need that big of an increase. So it is peculiar—

Mr. Nathan Cullen: It's peculiar. There must be something else going on.

Prof. Wade Locke: There must be something else going on.

Mr. Nathan Cullen: I want to get back to this. The chair mentioned this as well. This is to you and Mr. Wright. I don't pretend any expertise in the oil market whatsoever.

The Saudis seem to pretend at action yet didn't necessarily take a great deal of action, according to one of our witnesses yesterday who is in the energy business. I forget the quote exactly, but it was something to the effect of this having been effectively the biggest non-action maybe in the history of the oil market, where the Saudis at OPEC say one thing, and the market then responds.

I want to get back to whether it's a glut or a demand-side problem, because if the future bets right now are still consistently looking at $50, there can't simply be this 1% to 2% production oversupply alone. Can there? That seems a remarkable loss in value of a globally traded product simply because there's an extra 1% or 2% kicking around the market. This seems to be people hedging as well, suggesting that this might be in part at least a mix of the demand-side concerns from the market as well. Am I wrong? Am I reading what I'm hearing...?

Mr. Craig Wright: I think, as Steve said earlier, it's both demand and supply. I would argue it's early. If you look at oil prices through 2014, we had some downside demands, surprises. The U.S. printed a negative growth in the first quarter. It was weather-related and it has since snapped back, but it was a negative surprise. China was shifting growth down to more sustainable growth. The eurozone was continuing to struggle. So that opened up this gap between supply and demand. Energy prices started the year north of $100 and drifted down to about $75 a barrel back in November. Then everything changed post-November 27, and that's when, I think, the politics of oil kicked in. Then there's speculation and a lot of other non-economic issues that pushed it lower, and it'll take some clear line of sight before we get a bounce-back.

The Chair: Thank you, Mr. Cullen.

I'm going to chime in here as well. First of all, does anyone want to make a brief comment on the impact on Canada's housing market, impacts we can see?

Mr. Craig Wright: Everybody's obviously watching. I think we've seen the early round of impact, if you look at the December, January, and February numbers out of Alberta. There, I think, it was a confidence story. The shock has been quite dramatic and confidence has been rattled by it, given all the other shocks we've been putting up with. Now the next thing to watch is the employment side, and I think that's the key for the housing market. When you look at the housing market, invariably it's tied to the employment market, and if we're right, and jobs continue to grow, the unemployment continues to drift below its 20-year average. That suggests to us the adjustment in the housing market won't be dramatic and we think the bigger risk going forward, albeit more next year and the year after, is a rate increase rather than this shock.

The Chair: Thank you.

Mr. Cross, in your statement in terms of Canada's dependence on oil, you said that our overall dependence on oil should not be exaggerated. Oil extraction accounts for about 3% of Canada's GDP, while adding investment by the industry lifts the total share of oil-related activity to 6%, compared with 11.7% for manufacturing output and investment and 6.8% for housing.

I think I'm certainly reading that you're advising governments not to overreact, in part, and saying, take a realistic assessment in terms of the size of the industry and the impact it's having. You do, I think, point out that there's obviously a different impact in provinces like mine, like Alberta, from a fiscal point of view.

I wanted to open it up to anyone. Obviously we're moving toward a federal budget here in the spring. Is there any advice you have related to the size of the oil sector, and then how the government should be reacting in its upcoming budget?

I'll start with you, Mr. Cross.

● (1720)

Mr. Philip Cross: I think I was basically just responding to this attitude that because of the dramatic growth of oil sands output in this industry generally over the last decade, that somehow we've become a petrostate. I'd very much agree. I remember back in the fall, Jack Mintz was asked if the Canadian dollar was a petrocurrency. I thought he gave a very good response. He said that if it is, it isn't a very good one. If we're a petrostate, we're not a very good one.

We're not. Yes, petroleum grew rapidly and the resource sector generally grew. What people don't remember is how much that industry shrank during the 1990s. To me, a lot of this growth of resources was simply getting back to the kind of balanced economy between resources and manufacturing that traditionally has underpinned prosperity in Canada. I thought it was dangerous to become overly reliant on a low dollar and manufacturing for growth, and I think that was borne out by, first, the ICT bust in 2000, and then the ongoing troubles in textiles and forestry-based manufacturing.

I think we've seen an appropriate rebalancing away from manufacturing and back to resources. I don't think we're overly dependent on resources. Manufacturing is still a much bigger industry than the resource sector. I think people should keep that in mind. We're not Alberta, which does have an outside dependence on the resource sector.

The Chair: Thank you.

Any advice going forward, Mr. Locke?

Prof. Wade Locke: Sure. I would advise you and industry not to let short-term issues dictate long-term plans. The question you need to make a decision on is, how long the lower prices will prevail and what their impacts will be. If this is a one- to two- to three-year problem, then we shouldn't be cutting expenditure. We shouldn't be doing anything dramatic. We should try to deal with the situation, to get through this as best we can.

I think the one piece of advice is, don't let short-term problems dictate long-term strategies.

The Chair: Thank you.

Mr. Wright on this.

Mr. Craig Wright: I think it's a similar view, to stay the course and don't get distracted. I think I would prefer the focus remaining on improving Canada's speed limit, that 2% speed limit for Canada in its labour force growth and productivity. I think that's the way of growing the economic pie, which we're all after.

That means tax relief, tax reform, regulatory relief, and keeping the focus on how to improve productivity, with a particular focus on small and medium-sized enterprises in Canada, as 99.8% of our firms are made up of under 500 employees. Helping them grow will help productivity grow, which is what we're all after.

The Chair: Thank you.

I have about 10 seconds, Mr. Cross, if you want to add something.

Mr. Philip Cross: I would just throw it in that along with 1998 being instructive, 1986 was also instructive. In 1986 prices fell so rapidly they wanted to shut down the Hibernia project. The government had to bail out. That proved to be a very far-sighted decision.

It just goes back to “don't panic”.

The Chair: Thank you.

We could probably do one more NDP round and one more Conservative round.

Monsieur Dionne Labelle.

[*Translation*]

Mr. Pierre Dionne Labelle (Rivière-du-Nord, NDP): I had to step out for a moment, so good afternoon once again, gentlemen.

I have carefully read the document from the C.D. Howe Institute. In terms of monetary policy, you are very critical about the drop in the Bank of Canada index. I especially noticed in your document that your monetary policy council has 12 economists and they do not agree with each other.

The document does in fact show that you don't agree on what the impact of a drop in oil prices will be on the provinces. Do the provinces have to raise their taxes or rack up deficits? Your council is discussing that. There are no consistent views in terms of inflation expectations. According to your document, there is no consensus on the scope of the positive effects on the economy. You also don't agree on the effect of the decline on the stability of the Canadian economy.

When we insisted that the study bring together experts, we were hoping to find out where we were heading, but we seem to get a different answer from one economist to another.

I say this with sympathy, but the fact remains that it is difficult for us to see where we are heading if the price remains at $50 for four or five years.

● (1725)

Dr. Steven Ambler: I think we all agree here around the table that there is a lot of uncertainty about the positive effects. Each individual has their own way of weighing the uncertainties, but I think there is still a consensus that the overall impact on the Canadian economy is negative. That being said, the opinions do actually diverge in terms of the magnitude of the negative impact. Finally, we agree that the positive effects are more in the medium and long term and that their scope is also more uncertain.

Mr. Pierre Dionne Labelle: Do you agree that the falling price of oil will boost the global economy in general?

Dr. Steven Ambler: Yes, it is certain that, for a country or a group of countries that does not produce oil, the impact is positive. In that sense, I think Canada is lucky that the U.S. is its main partner. That is where it seems the strongest real growth will be in the next two or three years.

Some countries or groups of countries that do not produce oil, such as Japan, China and the eurozone, are unfortunately lagging behind, but for other reasons.

Mr. Pierre Dionne Labelle: Yes.

Dr. Steven Ambler: The falling oil prices are definitely helping them, but they are facing a whole host of other structural problems, unfortunately.

Mr. Pierre Dionne Labelle: Yes, I agree with you.

I don't remember who among you said—and I really like this comment—that we are overestimating the impact of the oil sector on the Canadian economy as a whole. We talked about the GDP percentage earlier. The Bank of Canada says that it is 6%. It certainly represents 14% of our exports, but overall, Canada remains relatively balanced economically.

Have I understood your viewpoint correctly?

Mr. Philip Cross: Yes, I think I said that.

Mr. Pierre Dionne Labelle: Yes.

Mr. Philip Cross: Let me just reiterate that, even with the increasing growth, partly in response to the decline in the development of resources, the idea is that we are more dependent than before on resources, especially in the oil sector. That is relatively small compared to the manufacturing and housing sectors, for example.

Mr. Pierre Dionne Labelle: ...all the strengths of the economy.

Mr. Philip Cross: The government has 23%, for example.

Mr. Pierre Dionne Labelle: The Bank of Canada says that there will be a slowing of growth, but not a reversal. We will be heading toward growth, but more slowly.

Mr. Philip Cross: Yes. According to the Bank of Canada's best estimate, by the end of the year, the growth of the oil industry will be reduced by 0.3%, which would not have been the case if there was no decline in the sector.

Mr. Pierre Dionne Labelle: Thank you.

The Chair: Thank you, sir.

Mr. Saxton, go ahead.

[*English*]

Mr. Andrew Saxton: Thank you, Mr. Chair.

I have a question for Craig Wright. Craig, what impact do you see this lower oil price having on consumers? I know that in my riding of North Vancouver, consumers have been saving $20 to $25 every time they fill up their tanks. Mind you, that has narrowed in the last few weeks, because the price has actually gone up quite a bit. I think we are at about $1.25 right now. Are we seeing this extra disposable income go into other parts of the economy?

● (1730)

Mr. Craig Wright: When we looked at the impact of oil, I mentioned some of the offsets. In particular, we looked at the gas savings, if you will, for the U.S. Our numbers calculate net savings for the U.S. consumer of about $150 billion. Doing the same math here, we don't get quite the same pass-through from the decline in oil prices to a decline in gas prices. As you suggested, they tend to go down more slowly than they go up, but we have seen what we think works out to about $11 billion equivalent tax cut for the Canadian consumers. That's going to help.

I think earlier there was discussion about the debt-to-income ratio. We do have consumer spending slowing down. The effective tax cut from lower gas bills will cushion the slowdown, but we do have consumer spending moving more in line with income growth rather than getting the extra kick from debt accumulation. The debt-to-income ratio is a concern, and we'll get more data out tomorrow, which suggests we'll have another record-high debt-to-income ratio. Consumers will slow down growth more in line with income, but the help from the lower gas prices will cushion the slowdown.

Mr. Andrew Saxton: Okay, thank you.

My next question is for Mr. Locke. Mr. Locke, you mentioned the impact that the lower oil prices are having on the economy of Newfoundland and also the government budget being the main recipient of the royalties. What more can the federal government do in this regard, or have we done enough? Is it more of a provincial issue at this stage?

Prof. Wade Locke: It's more of a provincial issue. I don't think there is anything we can do as nation about the issue. What I would hope is that the people in the industry take a longer-term perspective on what's really happening. They are reacting to the short-term price changes as if they are a long-term phenomenon, and there is a lot of uncertainty around issues. If you look at the underlying factors that determine supply estimates, they will give you a lot of pause for concern. When you look at that, there is a lot of uncertainty, a lot of volatility. People are reacting because of the uncertainty and the risk, trying to get through this the best way they can using whatever discretion they have. It will have long-term consequences for us, both as a society and as a province.

Mr. Andrew Saxton: Have there been significant layoffs in Newfoundland, and if so, have the employees being laid off been told to be ready to be rehired in the near future? What sort of state is that in?

Prof. Wade Locke: There certainly have been people not recalled to Alberta jobs. There has not been a lot of reduction from existing operations within Newfoundland. There has been a delay in one of the projects for a year, the White Rose extension. Right now there aren't a lot of fundamental changes in the province itself. The concern would be that if people delay investing in new projects—and there are lots of new projects—it will have long-term implications for the province and for the country as a whole.

Mr. Andrew Saxton: Okay, thank you very much.

Mr. Cross, can you tell me where you see the Canadian economy going this year? What sort of growth rates are you predicting?

Mr. Philip Cross: I'm almost tempted to hand this off to Craig.

I'm happy to say—

Mr. Andrew Saxton: I'm trying to spread my questions around.

Mr. Philip Cross: Coming from Statistics Canada, I have very few reflexes about forecasting and policy-making.

My general impression.... I produce a leading indicator that has declined 0.2% in the last month. Basically, it's all because of the commodity price component. If you exclude that, it's up 0.3%. I agree with the general idea that the costs are going to be front-loaded from this. We'll have a weak first quarter, and then we'll see the positive impacts on household spending and especially U.S. growth. Overall, I'd be quite optimistic, just because of the U.S. economy. It's been stuck at 1.5% to 2% for years now, and the consensus seems to be that it's finally going to break out above 3%. The employment data in the U.S. has been quite good, so I think that will pull us along.

Mr. Andrew Saxton: So you do not expect a severe economic downturn as a result of the oil.

Mr. Philip Cross: No. I saw a poll in the paper that the majority of Canadians think that the economy is declining and you sit there and go, people read too much into the stock market and the dollar. There are a lot of headlines surrounding this. It's a big price effect, it's a big story, but the idea that this is going to pull down our whole economy exaggerates the importance of this sector in our economy.

Mr. Andrew Saxton: Thank you, Mr. Chair.

The Chair: Thank you, Mr. Saxton.

I want to thank, on behalf of all the committee, the witnesses who appeared today. For your responses to our questions, thank you so much. If there's anything further you wish us to consider please do submit that to the clerk. We will ensure all members get it. Thank you for your patience with respect to the two votes.

Colleagues, if I could just have the subcommittee members stay behind, we will adjourn this meeting and come back with that one. Thank you.

The meeting is adjourned.