Trend Chart

Greater Metropolitan Region

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Business and environement: Leading instead of being led

Exclusive partner

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Canada

Chambre de commerce du Montréal métropolitain

Board of Trade of Metropolitan Montreal

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Editorial

Business and the environment: Leading instead of being led

By Isabelle Hudon, president and CEO of the Board of Trade of Metropolitan Montreal

This fall, the environment has taken centre stage in Montreal in a variety of forms. First, there was Katrina and the sudden surge in oil prices, which have since eased. Then, Montreal hosted the U.N. conference on climate change. Finally, by making cleanliness a major election issue, the mayoral campaign in Montreal reminded us that we are not indifferent to the quality of our immediate environment. Wal-Mart as well did its part to keep the environment in the news by adopting an environmental policy with regards to its suppliers.

Yet, although the environment was a hot topic in fall 2005, it begs the question: was this just a "seasonal" phenomenon, a mere passing fancy?

This is a tempting conclusion now that the price of gas has fallen back to below $1 a litre, but one that couldn't be more wrong. Environmental issues – and moreover, public and consumer awareness of the issues – are here to stay. In fact, the price of gas at the time of writing is not considered a return to the norm but rather a fleeting, exceptional situation.

The same holds true for business environmental stewardship: our expectations in this regard are also here to stay and will only increase. As such, this is an excellent opportunity for business to be on the cutting edge of the "green shift."

The first good reason to embark on this path is competitiveness. Whether firms go green out of necessity or because they recognize a growing demand for environmentally-friendly goods and services, companies that invest today in improving their environmental performance are also investing in their future competitiveness. There is nothing new in this. It is simply an age-old, widely used business strategy: anticipate and capitalize on change.

Another reason is the need to partner with the private sector in our efforts to protect and enhance the environment. It's no secret that many environmentally-related decisions carry major economic repercussions. Still, that does not mean that economic and environmental interests must always clash. Therefore, although some effort and sacrifices are required to achieve environmental objectives, active involvement in the decision making will allow the private sector to better share its concerns and avoid serious economic ramifications. In short, businesses should be acting now rather than waiting for future measures and requirements that may affect them.

Saying that companies must show some environmental initiative does not imply that they are totally passive. Often, quite the opposite is true. However, many of these initiatives remain unknown to the public as the information is kept within the company and its employees. Companies would do well to communicate their projects to the public and to set examples to follow.

That said, it is also true that whenever a company advertises its environmental initiatives, it is often dismissed as a public relations ploy. But in truth, the motivation hardly matters so long as the actions are real. In fact, at a time when consumers are placing increasing value on the environmental performance of the companies they patronize, environmental and economic interests can indeed be reconciled.

Companies must therefore walk the talk, in other words, they must do what they say they are going to do. More importantly, they must go beyond merely informing the public of their initiatives and tooting their own horn, for instance, by participating in environmental forums. A good example of how this is done can be found in the City of Montreal's sustainable development plan. While everyone who signs the plan makes a commitment to take action, this initiative also allows the stakeholders to share inspirational experiences and broadens the scope of the action taken.

Ultimately, this type of approach places the company in the driver's seat, allowing it to lead instead of being led. ■

Trends and overview

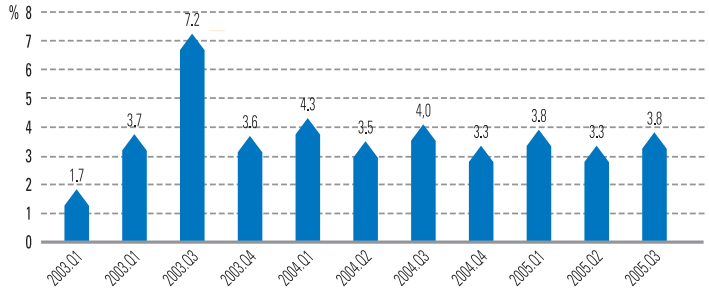
United States

Greenspan stays the course despite hurricanes

One can hardly discuss the American economy without mentioning Hurricanes Katrina and Rita, which pummelled the Southeastern United States at the end of the summer. We have yet to grasp the full impact of these natural catastrophes, but they will no doubt cloud the economic picture.

While the labour market fared well in July (+277,000) and August (+211,000), **job creation** made an about turn after Katrina, losing 35,000 jobs for the first time since April 2003. According to preliminary analyses, Katrina and Rita wiped out more than 500,000 positions. The automobile industry is not helping the situation, with GM announcing an impending cut of 25,000 positions and Ford planning to follow suit in 2006. Still, the unemployment rate, which was 5% in July, managed to slip to 4.9% in August – a level not seen since 9/11. Although it inched up to 5.1% in September, such a figure indicates that the economy is running at near full capacity.

In fact, the **gross domestic product (GDP)** grew at an annual rate of 3.8% in the third quarter, up five basis points. Some economists have revised this figure downward to 3% for the fourth quarter because of the hurricanes. However, the reconstruction efforts and projected housing growth should see the economy expand to an impressive 3.6% in 2006.



Quarter-tu-Quarter Growth in Real GDP

Source: U.S. Department of Commerce, Bureau of Economic Analysis

While attesting to a strong economy, these indicators also raise the spectre of **inflation**, which the hurricanes only exacerbated. Compared to the corresponding year-earlier periods, the Consumer Price Index (CPI) stood at 3.5% in July, and 3.6% the next month. Not surprisingly, it jumped to 4.7% in September, fuelled by the price of crude, which hovered at $70 per barrel.

The Federal Reserve responded to the inflationary pressures by tightening monetary policy, raising its **overnight rate** both on September 20 and then again on November 1. Thus, after twelve successive increases, the rate now stands at 4%. In his decision, Fed chairman Alan Greenspan stated that he would rather see a slight economic slowdown than unbridled inflation and considers the consequences of the hurricanes to be temporary.

The labour market was not alone to feel the fallout of the hurricanes in September. **Consumer confidence** also suffered as gas prices and interest rates rose as attested by the University of Michigan's Consumer Sentiment Index, which plunged from 89.1% to 76.9%. Moreover, **industrial production** declined 1.4% in September as oil production and refining capacity was partially paralyzed in the Gulf of Mexico.

Where the effect of Katrina and Rita may be longer lasting is the U.S. budget and current account. It is estimated that the clean-up cost for Katrina will add $200 billion to the current **budget deficit**, thereby surpassing the record $668.1 billion set in 2004. As for the **trade balance**, the monthly balances are still in the red, and July (-$58 billion) and August (-$59 billion) are no exception. As a result of the higher value of energy imports, the total annual losses to date are $404.3 billion. ■

Trends and overview

Canada

The great economic divide

Following the trend set in the first three months of the year, **productivity** remained unchanged in the second quarter of 2005. GDP growth in Q2 (0.8%) combined with an increase in the number of hours worked, thus erasing any productivity gains.

Moving into the third quarter, **GDP** was 0.2% in July and 0.5% in August, fuelled in large part by the goods producing industries, which saw the value of their output rise in July (+0.3%) and August (+1%). However, overall, the services industry was the shining star, and more specifically, the retail and wholesale trades.

Consumption therefore continues to drive economic growth, with **retail** sales registering increases month after month. August broke the streak, slipping 0.3% due to a downturn in the automobile sector (-0.4%), which accounts for about a third of total retail sales. **Wholesale** sales fell $228 million in July only to rebound nicely the following month, setting a new record of $39.9 billion (+0.7%).

Like the wholesale and retail trades, the industrial sector also helped lift GDP in July and August as manufacturers operated at almost full capacity. In fact, according to Statistics Canada, the **industrial capacity utilization rate** was 86.7% in the second quarter, its highest level in five years, a noteworthy performance given the fragility of the manufacturing industry.

What all this means is that the economy is running at full capacity, which in turn means growth. However, this comes with the attendant risk of the economy overheating and sparking **inflation**, which already reared its head in the third quarter, especially in September when the CPI jumped 3.4% due to surging gas prices.

This could soon spread to salaries. **Earnings** already increased in August (+4.2%) in such growth industries as mining extraction (+5.1%), retail (+3.9%) and construction (+3.8%). Given the very high participation rate, these increases should become more widespread as employers try to hold onto their employees.

In fact, earnings rose 4.1% in the **manufacturing sector**. The Bank of Canada's quarterly survey in the fall shows that manufacturers are optimistic about the future despite having to contend with a loonie that is now even stronger as a result of rising commodity prices and that makes their products that much less competitive. They must also deal with more expensive input and transportation costs.

Of all the provinces, Quebec and Ontario depend the most on manufacturing for revenues and consequently are not faring as well as their westerly neighbours, who are reaping the benefits of the petrodollar. The economic boom in the West, and particularly the oil-sands boom in Alberta, contrasts sharply with the rest of the country and is creating a real **economic divide**, as exemplified by the $400 cheques the Alberta government will be sending its residents for Christmas. ■

Trends and overview

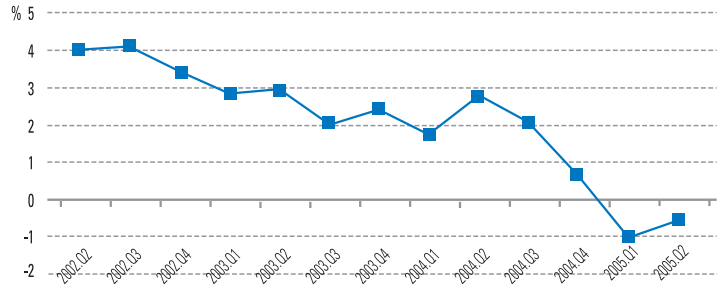
Quebec

Consumption sustains the economy

After rising 1% in July year-over-year and dropping 16% in August, **housing starts** ended the third quarter down slightly. The value of residential **building permits** evolved in tandem, rising 16.5% – the best performance since November 2004 – but tumbling 22.7% the following month, most likely due to the fact that new homes were selling at a slower pace.

The labour market created 24,400 **jobs** in the third quarter. However, this news is not as good as it appears because at the same time, 15,100 full-time jobs were replaced by 39,500 part-time positions, and since the latter are considered less stable, future consumption could be affected.

Wages rose 0.8% in the second quarter, lifting **personal disposable income** after taxes and other transfers by 0.9% – the highest increase in one year.



Savings Rate of Quebec Households

Source: Institut de la statistique du Québec

More disposable income means more consumption. For the moment, this aspect of the economy is already faring well. Mega construction or expansion projects are regularly being announced, the most recent one involving a $100 million power centre in Candiac. As well, many new retailers are setting up shop in Quebec or multiplying their points of sale, including, for example, the U.S. chain Best Buy.

Moreover, the picture is still rosy for **retailers**, which set a new record in June and then again in July with annual sales of $84.7 billion. But the wind changed direction in August, causing sales to dip slightly (-1%). For their part, **wholesalers** set a record in June ($91.4 billion) but slipped in July (-0.1%) and again in August (-0.8%).

Retailers and wholesalers certainly played a role in Quebec's gross domestic product (GDP) growth, which was zero in May but advanced 0.5% the following month, mostly on the strength of the trades. July, for its part, owes its performance to the manufacturing sector, which helped lift **GDP** by 0.6% thanks to an increase in output (+1.9%).

However, the most recent data on merchandise trade in Quebec is rather sobering. Manufacturers are grappling with two issues: surging gas prices, which besides shrinking their profit margins – especially those of carriers –, are bolstering an already strong dollar, making their products less attractive to our main trading partner, the U.S. Finally, the Quebec **trade balance** has been in the red since February and dipped further in August to -$1.7 billion. ■

Our economic conditions

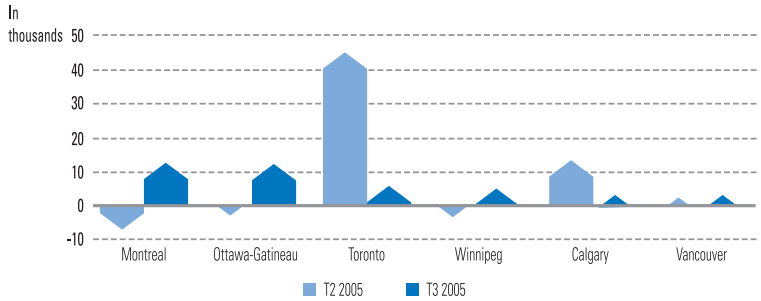
Labour market

Manufacturing undermines job creation

Job creation in **Montreal** once again finished the quarter in the red, losing 6,900 jobs, a poor performance compared to the same period last year (+6,200). Although July was positive with the addition of 18,800 positions, August (-1,900), and especially September (-23,900) cast a pall. During this time, the unemployment rate, which had dropped two basis points in July to 8.1%, rose for two months in a row, to 9.0%.

The manufacturing and professional, scientific and technical services sectors were the hardest hit. However, gains in public administration and educational services somewhat offset the decline.

In the rest of the country, the job situation remained unchanged in Vancouver while Toronto created an enviable 30,600 positions.



Job Creation 2005 – Canadian Cities

Source: Conference Board of Canada

Thanks to gains in July (+15,300) and August (+16,900), **Quebec** was able to finish the third quarter with 24,400 new jobs. While more encouraging than the previous quarter (-7,400), this performance is still well below the 34,800 jobs created in the same period last year.

Dragged down in part by sluggish manufacturing in Montreal, the manufacturing sector in the province took a major hit this quarter, eliminating 26,700 jobs and thus accounting for 70% of the job losses during this period. Most of the other sectors posted gains, led by educational services (+21,700) and construction (+18,200). Quite surprisingly, retail did not shine (+400) despite strong retail and wholesale activity.

The unemployment rate in the province jumped four basis points in July, to 8.4%, where it remained for the next two months. Analysts are not overly concerned since at the same time, the participation rate was around 65.7%.

In **Canada**, Quebec recorded noteworthy gains (+24,400), while its closest rivals, British Columbia (+8,300) and Ontario (+7,800), lagged behind. Although Alberta may have only posted minimal gains, it still boasts a low unemployment rate.

Overall, the national picture is positive but somewhat disappointing, with only 31,100 new jobs created. Most of these gains took place in August (+27,500), while July and September did very little to improve the picture. On the bright side, 52,200 jobs were full-time while 21,100 part-time positions disappeared. This bodes well for future consumption growth, one of the main engines of the economy.

Hammered by the loonie's strength, the manufacturing sector unfortunately stood out for its poor performance (-42,200) in Ontario and Quebec. However, these losses were offset by gains in transportation and warehousing (+22,600), healthcare and social assistance (+21,300), and educational services (+20,800).

For its part, the unemployment rate hardly budged, inching up one basis point in July, to 6.8%, but dropping by the same amount in September, thus returning to a 30-year low. ■

Our economic conditions

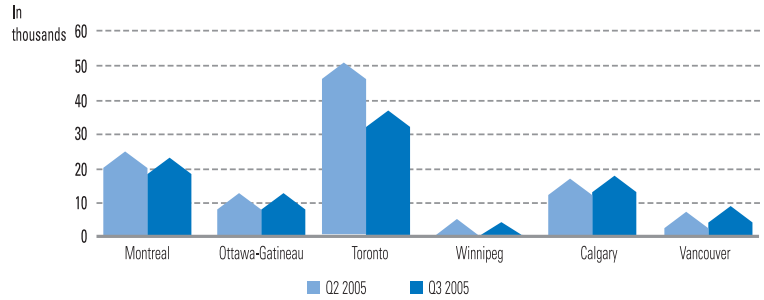
Housing market

Surprise jump in September

Housing starts in the **Montreal** census metropolitan area (CMA) rose in the third quarter of 2005 compared to the same period last year. July (+15%) and September (+28%) were behind the increase from 6,340 to 6,703 units (+5.7%). In fact, forecasts that the real estate boom was losing steam were proven wrong in September.

The rental and condo markets were largely behind this performance, closing the quarter up 14.3% and 30.6% respectively. Although the condo market appears to be doing well, Canada Mortgage and Housing Corporation (CMHC) cautions that this market is reaching a state of equilibrium and will slow in 2006 more than the other segments. As for detached, semi-detached and row houses, construction dropped over the same quarter last year.

The growth in the housing market was led by the South Shore, with Longueuil leading the way. Thanks to increases recorded each month, the South Shore finished the quarter up 25.6%, from 1,171 units to 4,170 units. Montreal also recorded gains (+9.6%), although to a lesser extent. These good results offset the losses on the North Shore (-6.3%) which was dragged down by a particularly sluggish August.



Housing Starts – Canadian Cities

Source: Conference Board of Canada

Unfortunately, **Quebec** overall cannot boast such positive results, with housing starts barely changing in the third quarter over the same period last year (-0.5%, down from 10,501 units to 10,452 units). The province's performance in August (-16%) and September (+13%), which was largely fuelled by activity in Montreal, was virtually cancelled out.

Housing starts in Sherbrooke nearly doubled in September, lifting the quarterly total by 10.7%. Thus, Sherbrooke, Trois-Rivières (+23.1%) and Montreal are the only centres with 100,000 residents and more to record growth in the third quarter of 2005.

During the quarter, multiples – which include detached and row houses, rental units and condos – stole the show with an 11.2% jump in construction. In contrast, single starts took a big tumble (-15.7%).

The residential housing market in **Canada** was disappointing in the third quarter. In seasonally-adjusted data (SAD), housing starts decreased 4.5% from 241,300 units in June to 230,500 in September. CMHC analysts do not seem unduly concerned, believing that the outlook is still favourable as a result of low mortgage rates and a healthy labour market.

Multiples in urban centres (-5%) and detached homes (-2%) were behind the decrease.

While different regions of Canada recorded notable gains, Ontario did not fare too well, recording a 32.3% drop in the third quarter. In fact, it is the province's relative weight that pushed national housing growth into the red. ■

Our economic conditions

Financial market

Inflation rate

Canadians generally paid more in the third quarter for the goods and services that make up the inflation-measuring Consumer Price Index (CPI). Thus, consumers paid 2% more in July, (over the same month in 2004), and then 2.6% more the next month. And September was even worse, with prices climbing another 3.4%, a level unseen since March 2003.

Not surprisingly, gas prices are behind the CPI's increase in the third quarter. Prices at the pump spiked 12.3% in July and another 20.1% in August, but the biggest surge came in September with Hurricane Katrina (+34.7%). Other factors that boosted inflation were homeowners' replacement costs (i.e., expenses that offset home depreciation) and restaurant meals.

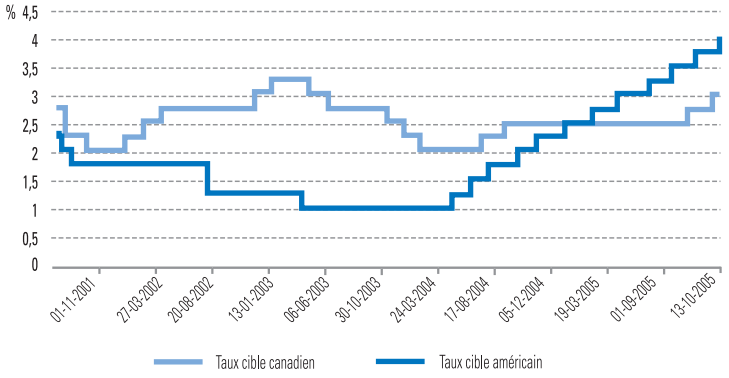
The relative stability of the Bank of Canada's Core CPI means that inflation was predominantly fuelled by rising gas prices and has not yet spread to the prices of other goods and services. In fact, this index, which includes the eight most volatile components,[1] dipped one basis point in July to 1.4%. It then rose to 1.7% in August, where it remained in September.

Interest rates

Seeing inflation rise, the Bank of Canada decided to intervene after a nearly full year pause in monetary tightening. The Bank is taking into account global energy prices and the fact that the economy is running at almost full capacity.

As such, to minimize the risk of inflation surpassing the mid-point of the Bank's inflation control target range – set at 2% –, the central bank raised interest rates by a quarter point to 2.75%. In its press release, the Bank stated that based on its preliminary analysis of Katrina's impact, the U.S. economy should slow slightly, and in Canada, consumer prices are expected to jump in the near term.

The Bank thus opened the door to future rate increases, which was confirmed on October 18 when the overnight rate rose once again, to 3%. Moreover, two days later, the Bank stated in its *Monetary Policy Report* that it was projecting GDP growth of 2.8% in 2005 and 2.9% in 2006. However, these projections raise the spectre of the economy overheating and an upward inflationary spiral.



Taux directeur canadien et américain

Sources : Banque du Canada et Réserve Fédérales

1. Fruits, vegetables, gasoline, fuel oil, mortgage interest, intercity transportation and tobacco products.

Our economic conditions

Exchange rate

In this report, the Bank of Canada also discussed currency rates, adding that the Canadian dollar has strengthened against the world's major currencies, particularly the greenback. To quote, "This recent strength appears to be underpinned by fundamental factors, including high prices for crude oil and natural gas and Canada's generally solid economic performance."

In fact, the catastrophe created by Hurricane Katrina — and to a lesser extent Rita — paralyzed part of the oil production and refining capacity in the Gulf of Mexico. As a result of jeopardized supply and pressure on demand, the price of crude exploded, and since Canada is a net exporter, this was good news for the loonie.

At the same time, the Canadian dollar was buoyed by a solid performance by economic indicators such as job creation, trade surplus and industrial capacity utilization, all of which attest to a vibrant domestic economy.

Thus, since early 2003 when its value began to climb against the greenback, the loonie has shot up more than 35%. More recently, our currency set several records in early fall, the latest on September 30 when it reached $0.8615, its highest level in 13 years.

While some analysts believe our currency is over-valued, the loonie's upward trend may nonetheless persist, mainly because Canada's tightened monetary conditions will attract investors in search of higher interest rates, which at the moment are not available in Europe or Japan, where monetary policies are relaxed.

Stock markets

Although crude oil set new records, trading at more than US$70 a barrel in September, other commodity prices have been climbing as well. The price of gold, for example, jumped nearly 6% in the third quarter, trading at about $465 an ounce. During the same period, the market price of natural gas soared more than 77%.

Strong demand for natural resources and their rising value on the stock market turned out to be good news for the S&P/TSX benchmark index, which rose above 11,000 in September, mostly on the strength of oil and gold stocks. However, October saw a reversal, with the index falling several times as the energy sector cooled off.

Conversely, the increase in the price of some natural resources exerted strong pressure on manufacturers. Those who have not passed on the increases for fear of losing their competitiveness must certainly be feeling the pinch on the bottom line by now. ■

Our economic conditions

Foreign Trade

Canadian and Quebec trade performance at opposite ends of the spectrum

At $6.1 billion, Quebec merchandise exports hardly budged in June. However, July marked the beginning of a downward trend (-5%) that continued into August (-4%). Thus, in the seventh month of the year, 18 of Quebec's 25 main product groups lost ground, with telecom equipment leading the way (-$51 million). In August, they were dragged down by aircraft sales, which took a nose-dive (-60.2%). As for the destination of our goods, the value of U.S.-bound exports slipped throughout the summer, from $5 billion in May to $4.5 billion in August (-10%).

For their part, Quebec imports rose $191 million in June only to embark on a rollercoaster ride in the months that followed: down 11.3% in July and then up to an unprecedented high of $7.2 billion in August (+21.1%). It bears mentioning that in July, although crude oil imports increased (+22.3%), nearly all the other product categories declined. The situation took a turn for the better in August thanks to rising imports of aircraft and aircraft engines (+$571 million) and petroleum and coal products (+$139 million). The downturn in July is explained by a decrease in imports from the U.S. (-$607 million) which, however, was more than offset in August (+$657 million). But this time the limelight was shared with China, whose imports also rose (+$85 million).

Quebec's trade balance continued its downward spiral in June (-$673 million) and July (-$216 million). August was particularly harsh, with a $1.7 billion deficit as a result of a major increase in imports and slight decrease in exports.

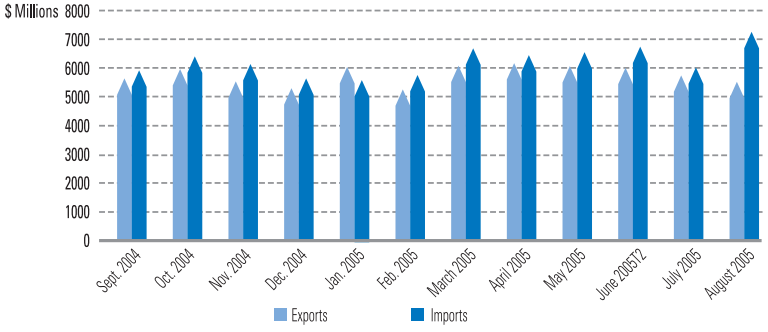
Canada

In comparison, the Canadian picture couldn't be more different, with exports continuing to rise, recording their sixth consecutive gain in August and even setting an annual record in June when the country shipped $37.2 billion in goods (up $674 million). The increases in July (+$180 million) and August (+$561 million) were somewhat more modest, fuelled by soaring energy prices. In fact, energy exports climbed $1.4 billion (+22.9%) between May and August.

As for destination, the growth was towards the U.S.: from May to August, the value of U.S.-bound merchandise increased $985 million (+3.3%).

Imports also increased but to a lesser extent, rising $154 million in June and $164 million the following month to $32.4 billion. However, August saw a dip of $115 million. Over these three months, imports of industrial goods fell $139 million, which was offset by an increase in automotive products (+$228 million). Imports are beginning to show signs of diversification in terms of origin as the largest increase (+$259 million) came from goods shipped from countries other than the U.S., European Union, OECD and Japan.

In the previous edition of the *Trend Chart* (October 2005), we stated that while positive, the Canadian trade balance has been eroding for the past 12 months. The latest figures contradict this statement and attest to a complete reversal. Indeed, the trade balance is growing once again, rising 28% from May to $5.5 billion in August. ■



Foreign Mechandise Trade in Quebec

Source: Institut de la statistique du Québec

Are rising energy prices a fact of life?

The recent increases in energy prices across North America have had a profound impact on the Quebec and Montreal economies which, because of their heating needs and types of production, are highly dependent on energy resources. Subjected to strong fluctuations dictated by global market forces for which there are few levers of influence, the price of gas at the pump has, after peaking at nearly $1.40 a litre, however, recently dropped below the $1 level.

Besides the negative impact they have on the economy and business competitiveness, rising energy costs have an effect on less obvious elements, notably, those pertaining to the transportation and use of electrical resources.

The volatility of gas prices...

We could see it coming: high fuel prices hit transport companies especially hard, which in turn has an indirect impact on business competitiveness, particularly that of companies that export their goods over long distances.

However, this undeniable fact creates an unusual situation in that it makes market proximity a more important competitive advantage. According to a recent study conducted by the CIBC, on average, a 1% increase in fuel prices leads to a 0.4% increase in total freight rates.[2] Therefore, because of the shipping costs of some manufacturing products, it could become more profitable to keep their production near the markets where they are sold. According to the study's author, we may also see less production transferred to Asia, where low wages make manufacturing costs generally more competitive. Depending on how high oil prices rise, it will be interesting to observe this new phenomenon in the coming months and to assess its impact across the metropolitan region.

Rising fuel prices do not only affect the transportation of goods but people as well. In this regard, a study carried out in 2004 by the Board of Trade of Metropolitan Montreal on the economic spin-offs of public transit in Greater Montreal showed that households that use public transportation spent less money on travel. In fact, in 2003 alone, Montreal households saved $570 million in travel expenses by using public transit.[3]

In the Board of Trade's opinion, the savings have the two-fold advantage of providing families with more disposable income to spend on shopping, cultural outings and recreation, and making an additional contribution to the local economy since the extra money ends up being spent here, unlike for fuel and car part purchases, where it ultimately leaves Quebec. In fact, the local economy is hardly dependent on the automobile and oil industries. Thus, with the recent hikes in gas prices, public transit could now save Quebec households in the vicinity of $700 million per year.

It is also interesting to compare gas price increases at the pump in the last decades in constant 2003 dollars. For example, a litre of gas cost $0.985 in 1982 and $0.763 in 2003.[4] The main reason for this large spread is that gas prices in North America have not increased in tandem with the Consumer Price Index (CPI). Some believe that this increase is merely an inevitable price adjustment that businesses and individuals were going to have to pay, while others subscribe to the view that Quebec must diversify its energy if the province is to achieve its full economic potential and sound economic growth.

2. Soaring Oil Prices Will Make The World Rounder (http://research.cibcwm.com/economic_public/download/occ_55.pdf)
3. Public transit: a powerful economic engine for the Metropolitan Montreal region. (http://www.ccmm.qc.ca/documents/memoires/2004_2005/CCMM_TransportCommun_etude.pdf)
4. Ministère des Ressources naturelles et Faune (http://www.mrn.gouv.qc.ca/energie/energie/energie-portrait-prix.jsp)

The stability of Quebec's energy sources

In Quebec, oil represents 37% of all the forms of energy consumed, just behind electricity at 38%. On a national scale, this proportion rises to 40% while electricity, at 25%, is much lower than in Quebec.[5] Insofar as the price of electricity is considerably lower in Quebec than elsewhere in North America (Chart 1), companies and citizens alike benefit from an asset that has become a real competitive advantage.

Indeed, Quebec depends heavily on hydroelectric resources, an inexpensive, renewable and accessible source of energy that provides the province with considerable revenues. In fact, the export of surplus electricity to neighbouring provinces and to the Northeastern United States is quite lucrative, adding $1.7 billion to government coffers in four years alone.[5] To place this figure in perspective, this amount is equal to the cost of upgrading the existing infrastuctures of the Montral metro.

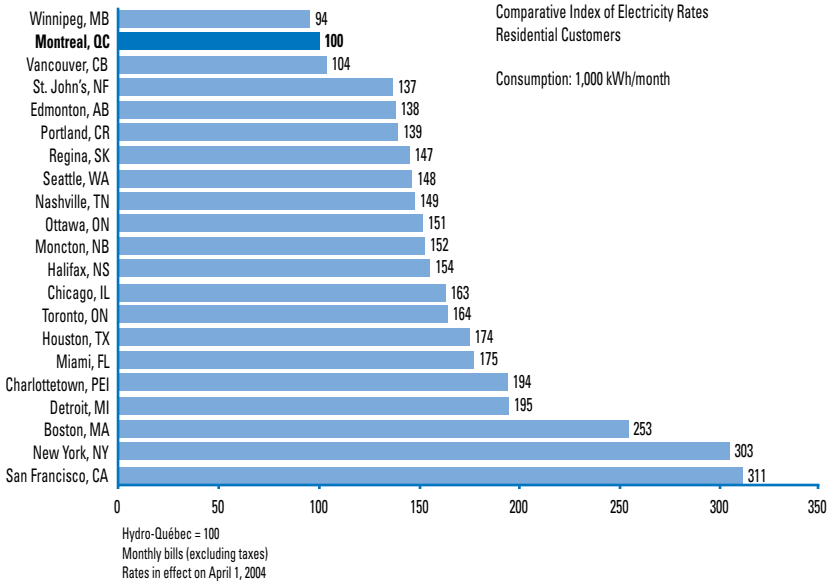
As the Board of Trade highlighted in a brief submitted last March to the parliamentary commission on the Quebec energy sector, it is in the government's interest to keep electricity prices stable, predictable and in line with the cost of living. Moreover, in order to ensure the province's economic development, it would do well to boost electricity generating capacity by adding hydroelectric and wind power stations and implementing energy-efficient measures in order to meet demand and increase revenues from the export of surplus electricity.

Diversifying energy sources and maximizing the use of electrical resources provide a competitive advantage that Quebec must leverage, especially in this context of rising gas prices. In fact, Quebec, with its hydroelectric reservoirs, is one of the few places in the world where energy, in the form of water, can be stored and used to produce electricity at will, i.e., when it can be sold at a high price on foreign markets. Selling electricity during a heat wave is such a time when demand and the price of electricity in the U.S. is high while local demand is relatively low.

Moreover, although Quebec and Montreal have little control over fluctuations in fuel prices, the exact opposite is true when it comes to electrical energy, a resource with still largely untapped potential. And given that this resource is a renewable form of energy and that multiple initiatives are underway around the world to reduce greenhouse gases, Quebec clearly enjoys a strong competitive edge in the energy field.

Quebec has several sources of energy, including electricity, which are produced locally, are renewable and allow for stable prices and supply to citizens and business. As a result of its abundant electrical resources, Quebec is therefore somewhat less vulnerable to fuel price fluctuations since these fluctuations affect a small part of its total energy consumption. Consequently, it only makes sense to invest in this comparative advantage, which responsibly exploited, will benefit both Montreal and Quebec as a whole. ■

Chart 1



5. *L'énergie au Québec*, ministère des Ressources naturelles et Faune, 2004.

A glance at Montreal

Winning strategies for reconciling environmental performance with corporate financial performance

By Paul Lanoie, PhD, Professor at HEC Montréal and member of the Groupe d'études et de recherche sur le management et l'écologie (GERME)

How to convince business leaders to improve their company's environmental performance?

There's always coercion: laws, bylaws and green taxes. However, with this approach, environmental stewardship is perceived by managers as just another of the many burdens or constraints with which they must contend. And although efforts are made, they are often half-hearted and under duress.

Why not take a different approach? Talking money rather than preaching may be the right way to reach business leaders. From this perspective, we propose two strategies to enable companies to reconcile environmental and financial performance.

Product differentiation

Companies can design products that are kinder to the environment and highlight their features in such a way that consumers will be willing to pay more. In this way, rather than losing, the company stands to gain.

Examples of this approach can be found in a wide variety of areas. For instance, despite their generally higher prices, organic food stores such as Aliments MERCI are becoming increasingly popular in Montreal. In France, Ecofamille specializes in organic products for the family, including such items as washable diapers and baby clothes made of organic cotton (no fertilizers or chemical pesticides). In the U.S., a chemical products firm called Ciba set itself apart 25 years ago with the introduction of dyes (e.g., Cibacron LS) that adhere better to fabric. Rinsing and wastewater treatment is made easier with this dye, generating savings for manufacturers. Despite its higher cost, this product has been a success. Finally, a number of carmakers – such as Toyota with its Prius – offer hybrid cars (conventional and electric combined) that cut gas costs by 30% to 50%. Although they cost substantially more than a conventional vehicle (about 50% more), sales are up across the board, and the government of Quebec is even thinking of subsidizing this type of vehicle purchase.

What does it take to successfully implement such a strategy? First, it is important to focus on goods for which consumers are willing to pay; in other words, you stand a better chance with luxury items than staples. The Prius is proof in this regard. Moreover, you must be able to provide credible information that attests to the environmental benefits of the product (e.g., official fuel consumption tests). Finally, this strategy stands a better chance of success if there are barriers to imitation as in the case of Ciba, which patented its dyes.

Focus on cost reduction

The second strategy, **identifying opportunities to improve the environment while reducing costs**, is probably the most promising. In effect, although improving the environment is generally perceived as a cost, in many cases it can be an opportunity to use resources more efficiently and trim expenses. Harvard's professor, Michael Porter has drawn attention to this approach, which departs from conventional wisdom. His reasoning is that "pollution is a manifestation of economic waste and involves unnecessary or incomplete utilization of resources, or resources not used to generate their highest value." Proponents of industrial ecology, who hold that one company's waste can be another's input, share the same view.

Examples abound here as well. Each year, American medical device producer Baxter, which has a subsidiary in Quebec, calculates its return on investment as a result of pollution control. Thus, it has determined that energy consumption and waste management improvements made between 1994 and 2000 saved the company $53 million in 2001, or 10% of profits. The new trend of building "eco-friendly" buildings meets the same imperatives. For example, Ford recently built the world's greenest assembly plant in Detroit. Among other things, it boasts the largest "living roof" on the planet (covered in grass). This roof saves the carmaker some $35 million a year by reducing storm-water runoff. This process also extends the life of the roof, which is no longer exposed to the hot rays of the sun, reducing the heat that penetrates the building, and by extension, air conditioning costs. In Montreal, buildings like La Tohu and the new Pavilion at École Polytechnique also prove that it is indeed possible to build in a less polluting way and cut costs at the same time.

Not only can better environmental performance lead to lower energy and material costs, it can also reduce capital expenses. Indeed, a growing number of studies show that the financial markets tend to punish firms that are not environmentally responsible by reducing their stock value. An environmentally lax company will therefore have a harder time gaining access to the capital market. For example, in a well-known study, Klassen and McLaughlin examined the impact on the stock market of 140 positive announcements related to environmental management (e.g., environmental achievement awards) and 22 crisis announcements (e.g., legal action, oil spills). In this sample, firms associated with a favourable announcement saw their market value increase 0.82% on average while those with a negative announcement saw it drop an average of 1.5%.

Others go one step further by maintaining that not only can it reduce energy, material and capital costs, improved environmental performance can also decrease labour costs. As such, companies that make environmental stewardship a priority will have an easier time attracting and retaining quality employees. While quite plausible, this assumption has yet to be proven empirically.

Conclusion

In short, the way to encourage business leaders to support the environmental cause is to speak their language and show them that what initially looks like a burden can in fact become an opportunity. When you stop and think about it, this strategy only makes sense. In our daily lives, there are many things we can do to both prevent and reduce air pollution: taking a bicycle or public transportation to work, turning off the lights when leaving the room, wrapping gifts in reusable bags, among others. After all, improving resource management on a daily basis is the first step towards sustainable development. ■

Guest columnist

The art of coexistence: A *sine qua non* for Montreal's evolution

By Benoit Labonté, mayor of the Ville-Marie Borough and member of the Executive Committee responsible for the Downtown core, Culture and Heritage

Strolling through the neighbourhoods of central Montreal, known as the *Ville Marie* borough, you can't help but be struck by the area's diversity, in every sense of the word. Walking east to west on St. Catherine Street from *Joe-Montferrand* Park to the old *Forum*, visitors quickly become immersed in a rich blend of different ethnicities.

The trek takes you through or near nine historically, sociologically and economically distinct neighbourhoods: *Sainte-Marie*, *Saint-Jacques*, the *Village*, the *Latin Quarter*, the *Faubourg Saint-Laurent*, the business district, *Golden Square Mile* and *Shaugnessy Village*. Bordering the route are *Chinatown* and *Old Montreal*, the city's historic centre and most visited neighbourhood in Canada. But more importantly, every day along this route, hundreds of thousands of workers, business leaders, merchants, consumers, artists, creators, street entertainers, leaders and volunteers of community organizations, members of ethno-cultural communities, university professors and students, tourists and others rub shoulders. You would also be struck by their sheer number – seventy-five thousand in the Ville-Marie borough alone – because, unlike most North American cities of this size, Montreal has a vibrant, inhabited downtown, comprised of an eclectic mix of people. In a manner of speaking, all these citizens make up the social capital of the Ville-Marie borough.

This profusion of activity and the diversity of the people who live, work, study and pass through these neighbourhoods, as well as of those who come for a visit or just to have fun and immerse themselves in a different culture, gives Montreal an important advantage over other cities in the world. It also attests to the fact that Montreal is an exceptionally fertile breeding ground of creativity that favours its economic, social and cultural development, and by extension, the development of the entire region. However, in order to hold onto this invaluable strategic advantage, we must work actively to cultivate social cohesion – or the art of *coexistence* – which is the only way to ensure that Montreal's growing reputation as an inclusive, egalitarian society is not just a theoretical view. Still, while it brings collective wealth, diversity can also be a source of tension and conflicts when it comes to coexistence.

These conflicts may be inevitable but this does not mean that we should stand idly by and allow the balance of power to decide the outcome, because the strong would, more often than not, prevail over the weak and the unfortunate

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result would be a homogeneous society. Since the future of the metropolitan region — its *new urbanity* if you will — depends on its diversity, we have an obligation to channel it positively and transform it into a lever for development, progress and the qualitative growth of the community.

While it is first up to citizens to do their part in this regard by demonstrating the open mindedness that is so essential to living in an urban society, it is ultimately the responsibility of the elected officials to coalesce the many elements that characterize this coexistence by acting as *unifying agents*. To do so, they must fully exercise their moral and institutional leadership by stimulating the emergence of *citizen and institutional synergies* and creating interfaces and innovative mechanisms to prevent, reduce or settle conflicts before they turn into crises and before the "survival of the fittest" law settles the issue, often inappropriately.

Many solutions can be explored in this regard, be it through public dialogues, the creation of citizen and youth advisory councils or twinning programs similar to those found between cities that match up two community organizations, associations, schools or businesses that work in the same sector but in vastly different environments. All these measures would further the art of living together and facilitate coexistence.

Such coexistence "management" initiatives rest on two premises:

1) Montrealers are open, inclusive and equality conscious; and
2) coexistence conflicts all too often stem from mutual ignorance.

These various types of proposed exchanges and synergies would ultimately allow us to build bridges between the different worlds that inhabit central Montreal's neighbourhoods, bridges that would bring social harmony and improve the quality of life in Montreal for years to come.

Only by living together more harmoniously can we hope to achieve greater social cohesion and enhance one of Montreal's greatest assets: its social, economic and cultural diversity. ■


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Canada Economic Development report

Causes and outlook of rising petroleum prices

After starting the year at around US$44 per barrel, the price for the West Texas Intermediate peaked at US$70.85 at the end of August, only to retreat lately at around US$60. Although hurricane Katrina, which effects are temporary, caused the price of oil to rise a few dollars, and thus broke the US$70 mark, the causes of the present situation lie much deeper. First, following the high prices of the oil shock of the early 80s, the oil companies invested massively in the upstream sector of exploration and production. This extra supply resulted in prices of around US$10 per barrel when demand fell following the early 90s recession. They subsequently cut their investments in exploration and production and laid off a sizeable part of their workforce.

We are thus today lacking the capacity to immediately increase production and the oil companies have a tough time recruiting qualified workers (only 1,500 are currently enrolled in petroleum engineering, a decrease of 85% since 1982)[6]. Second, there is a lack of refining capacity to meet demand. It has been over 20 years since the last refinery was built in the United States. The countless number of authorizations necessary to build one as well as public opposition are strong deterrents. This problem is compounded by the fact that we find and pump less light and sweet crude oil. The heavy and sour crudes found in Alberta, Venezuela and Kazakhstan require more processing than the lighter and sweeter ones. Unfortunately, there are few refineries capable of processing those crudes, which results in higher refining margin and higher prices.

The harmful effects of higher oil and gas prices will be widely but not uniformly felt around the province. The Canadian Department of Finance estimates that, for the province of Quebec, a 20 % increase in the price of oil could translate in a 0,8 % loss of production in the first year and 1,4 % after two years[7]. Consumers, in particular those living in areas where public transportation is deficient and who consequently depend on a car for their transportation needs, are expected to spend less on other goods and services.

With winter coming, the price increase of natural gas and heavy fuel should significantly inflate the heating bill. The world's biggest retailing giants are also worried about the approaching Christmas season, usually the most profitable period of the year, since falling consumer spending could hit their revenue. Although the general industry has improved its energy efficiency by 14 % from 1990 to 2002[8], for the firms, their burden will be proportionate to their use of petroleum inputs (energy and petroleum materials).

The transportation industry will be one of the first to be considerably hit. The industries using great amounts of hydrocarbons (plastic manufacturing, for example) should follow. The construction sector, especially large scale non-residential projects that require numerous pieces of energy-hungry heavy equipment over a long period, will be hit. With time, these effects will spread to the whole economy. Tourism and leisures, going from hotels to restaurants to performing arts, will suffer as a result. Also, compared to closer located competitors, industries based far from their main markets will be disadvantaged. It is thus feared that the most remote regions will experience more difficulties.

The alternative energy producers should gain from increasing oil prices. Ethanol and other biofuels production could be stimulated. Diversity in sources of energy, as well as financial hedging through derivatives or long term supply contracts, will help attenuate the volatility of energy prices. Energy efficiency will increasingly become a competitive factor. ■

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