Economics | Forecast / Outlook Reports

Economic Analysis of Ontario

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Economics

HIGHLIGHTS

- Economy will continue to rebound in 2021 and intensify for remainder of forecast.
- Real GDP to climb four per cent in 2021, 4.4 per cent in 2022 and 2.9 per cent by 2023.
- Strong hiring growth will pull down the average unemployment rate to eight per cent in 2021, with a continued slide over next two years.
- A stronger economy, open borders, and increased immigration quotas will lift population growth over next three years.
- Risks to recovery remain elevated and highly dependent on consumer and business sentiment.

INTRODUCTION

The economic shock caused by the pandemic hit Ontario very hard causing a severe short recession that surpassed the economic fallout of the previous two recessions. Medical science focused efforts on creating and distributing effective COVID-19 vaccines at a pace unseen prior to the pandemic. On average, vaccine development takes well over a decade to be approved. The current vaccines being rolled out were developed using new technologies and were approved in less than 12 months. These vaccines are key to unlocking the economy post 2020 and returning Ontario to a new normal, starting in the second half of 2021 and for the next few years. The services sector, especially those subsectors heavily dependent on leisure and tourism will take the longest to recover.

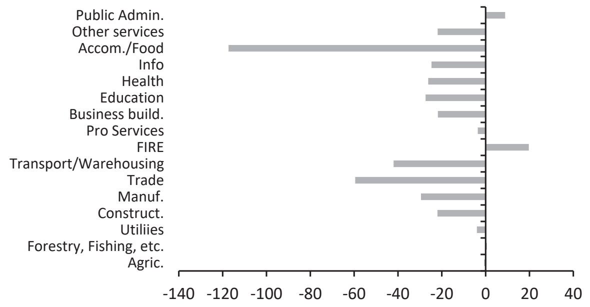
In 2021, real GDP will jump by four per cent and annual average employment growth will increase by 4.2 per cent, contributing to an unemployment rate that will slide down to eight per cent.

Labour Market

With COVID-19 only starting at the end of the first quarter, the COVID-19 pandemic was quite disruptive to Ontario's economy over the next nine months due to increased public health measures and rolling lockdowns aimed to reduce the viral spread. The average

Nearly all job losses in 2020 occurred in services sector

Net jobs lost/gained 2020 vs 2019, '000s



Source: Statistics Canada, Central 1 Credit Union

unemployment rate in Ontario swelled to 9.6 per cent in 2020 from 5.6 per cent in 2019. This was due to heavy losses in full-time work largely in the private sector and in client-facing services linked to leisure and tourism due to households tightening their belts.

Although the pandemic-created recession was short, the economic impacts were considerable. The number of discouraged workers, those not actively in the labour force looking for work, jumped 6.1 per cent in 2020 and the total job losses were over 50 per cent deeper than the two previous recessions during the early 1990s and 2008-09.

Housing and Retail

While other sectors of the economy faced significant headwinds in 2020, the resale homes market defied the odds. Since the economy reopened in May, the market was fueled by low interest rates enticing people to make home purchases sooner than planned, and compelling remote workers to leave the largest urban areas for more space and increased relative affordability. Anecdotal evidence suggests some buyers were moving to smaller markets such as Windsor, London, or Northern Ontario.

Average home price increased an eye popping 17.1 per cent in 2020. According to the Canadian Real Estate Association's (CREA) constant quality housing price indexes (HPIs), for the seven real estate boards surveyed in Ontario, the average jump in HPI in 2020 was 13.1 per cent with a low of 10.2 per cent (Oakville-Milton) and a high of 18.4 per cent (Ottawa).

Retail Sales

Retail sales have struggled in 2020, particularly retail businesses that thrive on constant client-facing exposure and/or linked to tourism. The start and stop nature of the economy due to public health restrictions, which were raised, then lifted and ramped up again in the autumn have eaten away at any potential growth in sales. Over the first eleven months of 2020, retail sales in Ontario remained 3.8 per cent behind 2019 volumes. Despite innovations like curbside pickups or e-commerce, it has not been enough to offset losses.

Manufacturing and Exports

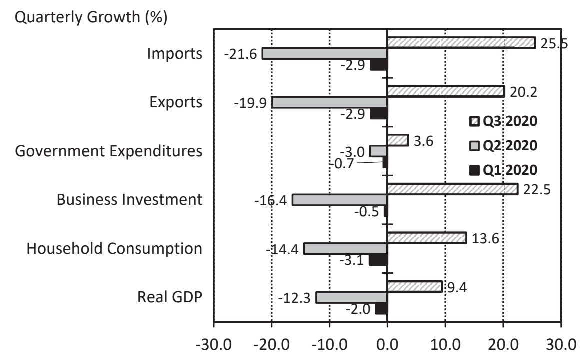
Year-to-date, manufacturing sales still lag 2019 sales by 12.7 per cent. Substantial economic uncertainty continues to constrain business investments and consumer demand. Inventories are rising. Year-to-date, durable (down 16.6 per cent) and non-durable goods (down 6.3 per cent) are substantially lagging 2019 total sales. Significant drag caused by transportation equipment manufacturing, down 25.1 per cent year-to-date, more than offset other areas reporting growth such as food manufacturing.

Following the economic reopening in May, exports grew significantly in May and June, averaging month-over-month growth of just over 31 per cent. Exports have waned since then, averaging monthly growth of 2.4 per cent with November posting the weakest pandemic era monthly growth of 0.5 per cent. While trade with the rest of the world increased, trade with Ontario's largest trading partner, the U.S., faltered leading to weaker growth since June. Over the first eleven months of 2020, export volumes lagged 2019 by 11.3 per cent. Weaker transportation equipment exports, especially aerospace and new cars, weighed in the sector. The emergence of e-trade continued to support consumer good exports in 2020 as businesses pivoted to new sales method to maintain revenue streams.

Health and social services

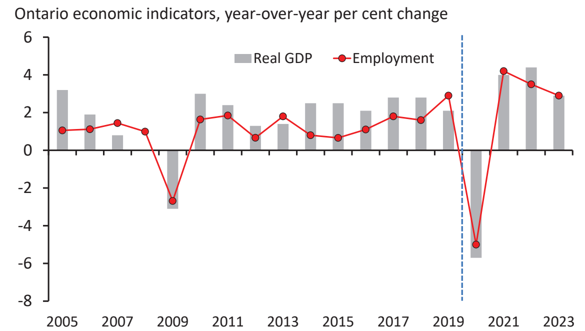
In 2020, this sector laid off 3.4 per cent of its workers. This was the steepest fall in employment for the sector in almost 30 years. The increased need for health care workers such as personal support workers and nurses in palliative care, long-term care homes and hospitals and mental health care professionals modestly offset job losses in other areas such as dental offices and family doctor clinics. Many of these services moved to online or telephone due to increased public health restrictions and lockdowns throughout the year.

Ontario's economy gradually recovering



Source: Ontario Finance, Central 1 CU Latest: Third quarter 2020
Note: Real seasonally adjusted GDP at 2012 prices presented

Pandemic recession acute but short-lived



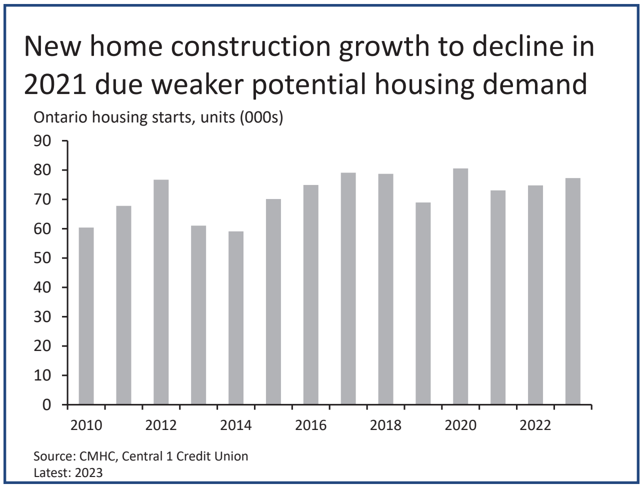
Source: Statistics Canada, Ontario Finance Ministry , Central 1 Credit Union
Latest: 2023

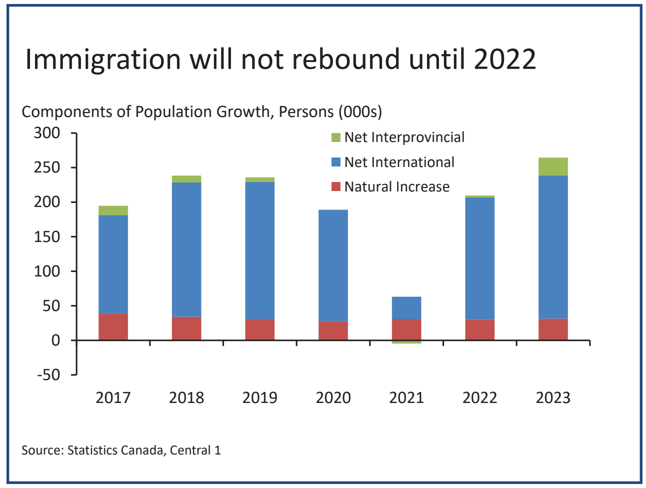
Education

In 2020, hiring in this sector fell by 4.6 per cent, according to the Labour Force Survey. While primary and secondary schools increased hiring to lower the teacher-to-student-ratios and provide more online options, post-secondary institutions faced difficulties due to weaker enrollment, particularly from international students, leading to job losses. Excluding community colleges and private primary and secondary schools, international students in 2018-19 made up 15.5 per cent of total enrollment (73,106 international students out of 470,304 total students) and was growing steadily since 2012-13 when international enrollment accounted for 9.2 per cent of total enrollment.

Construction

The new home construction segment in 2020 was unscathed. It would have been a record year if not for the public health restrictions affecting supply chains and lack of sufficient skilled trades slowing down the sector in March and April and again in November and December during the second wave of the virus. New





housing starts in Ontario increased 16.3 per cent, outperforming the post-2009 recession's trend. Much of the growth in new home construction came from high-density vertical living units. Condo apartments accounted for 54.3 per cent of all starts with most of the growth in the province's largest urban markets: Toronto, Ottawa-Gatineau, London, and Kitchener-Cambridge-Waterloo. Prior to the pandemic investors were expecting strong housing demand largely from permanent and non-permanent immigration and tourism which led to increased new home sales several periods prior to 2020, many of those units finally broke ground in 2020.Building intentions went in divergent directions in 2020. Residential building permit volumes increased by 14.2 per cent, supported by strong new housing demand and renovation spending non-residential building permits declined 6.5 per cent on much weaker industrial and institutional investment. Commercial space spending held up and was supported by large projects such as the Python project spearheaded by Amazon in Ottawa-Gatineau and growth in "pop-up" businesses as individuals pivoted during the pandemic.

Hospitality and food services

Since our last forecast, the conditions for the hospitality and food services sector have become more dire. Increased health restrictions continued to put a greater number of businesses at risk of permanent closure. The Canadian Federation of Independent Business has recently estimated the current ramp up in public health restrictions could cause the closure of between 71,000 and 222,000, or between seven and 21 per cent of all businesses, depending on how the situation evolves[1]. A large portion of those closures would occur in Ontario where only 37 per cent of small and medium enterprises are fully open.

1 https://globalnews.ca/news/7590374/small-businesses-closure-canada-covid-19/

With border restrictions in place, non-resident visits to Ontario fell 86.0 per cent compared to the same period in 2019. Airlines continue to cut staff, future investments and routes. Fewer non-resident visits have also affected industries complementary to travel such as hotels. Year-to-date data from January to September, showed hotel occupancy in Ontario was 35.5 per cent, nearly half of what it was during the same period in 2019.

Population

Since 1991, Ontario's population has increased by an average of nearly 150,000. With the pandemic closing the border to non-essential travel and in some cases, like the Atlantic provinces and Quebec that have restricted interprovincial movements, Ontario's population grew by a paltry-by-comparison 95,239. This is a steep fall of 35.8 per cent from the long-term average. As expected, much of the decline from immigration and non-permanent residents and to a much lesser extent interprovincial

THE OUTLOOK

Even with increased public health measures and a province-wide lockdown in late December 2020, economic growth over the summer and early autumn will provide a strong basis for growth in 2021. The increased vaccine supply and efficient roll out will support business and consumer confidence, leading to robust economic activity particularly in the spring and summer. Real GDP is forecast to increase four per cent in 2021. Consumers will gradually come out of public health measure-induced hibernation to spend. This along with increased interprovincial and global trade, and attractive interest rates for business investment will all support GDP growth. Real GDP growth is forecast to grow at 4.4 per cent in 2022 and by 2.9 per cent by 2023, slightly stronger than pre-pandemic activity.

Goods producing-sector growth (up 4.9 per cent) in 2021 will outstrip service-sector growth (up 3.8 per cent). The services sector will face some potential long-term scarring from business closures and gradually returning customers before coming closer in line to the latter part of the forecast with goods-sector growth.

Increased global trade will benefit the goods-sector, particularly commodities and manufacturing in 2021. The mining sector is forecast to grow by 6.5 per cent in 2021 and manufacturing sales are expected to climb 6.7 per cent. Areas of manufacturing that will benefit from increased global trade will include food, beverage, and tobacco/cannabis manufacturing, textile, clothing, and leather products manufacturing, wood products and furniture manufacturing, machinery manufacturing, and transportation equipment.

Building intentions will be strong in 2021 for non-residential construction (up 5.6 per cent) as businesses ramp up investments in areas such as industrial (up 28.4 per cent) and commercial projects (up 11 per cent). Inflation adjusted residential building intentions will move up more modestly (up 1.6 per cent) largely on renovation spending and other residential construction. While the resale homes market is expected to remain very tight in 2021 supported by attractive interest rates, new home housing starts are forecast to decline by 9.3 per cent to 73,100 units in 2021, putting a lid on residential construction intentions. Weaker than trend population growth and substantial economic uncertainty in 2020 tamped down new home construction in 2021 and for the remainder of the forecast horizon as new housing demand is a lagging indicator.

The services-sector is forecast to be a mixed bag with some areas thriving in 2021 while other sectors will take longer to reach pre-pandemic activity due to significant difficulties and scarring faced in 2020. Many of these sectors are client-facing services and unable to pivot online and generally related to travel and leisure such as accommodation and food services, arts, entertainment, and recreation, health care and social services, education, and retail trade.

During 2020, a key determinant of which services sectors would be relatively unscathed, and which would falter was the ability to effectively pivot online. This theme will persist for most of 2021 until the economy opens in the second half. Services such as finance, insurance, and real estate will benefit from strong resale housing demand and an ability to show homes online and close deals electronically. Professional, scientific, and technical services will continue to support clients online and add to their businesses as business investment gradually rebounds.

The population in 2021 will increase quite modestly (up 0.4 per cent), well below the long-term trend. Persistent barriers to movements of people, from abroad and from within Canada, will keep population growth modest. Not until the travel and tourism industry begins to recover and worldwide vaccinations reach an adequate level will population growth move beyond a trickle. By 2022, population is forecast to grow by 1.4 per cent and by 1.8 per cent by 2023. Growth over these two years will be driven largely by permanent and non-permanent immigration once world travel opens.

In late 2020, the federal government committed to allow about 1.2 million immigrants over the next few years to make up for the shortfall in immigration caused by the pandemic. With a strongly rebounding economy, Ontario will welcome most of those new residents, typically upwards of 50 to 60 per cent per annum.

Exports are forecast to grow by 5.6 per cent in 2021 and grow at six per cent in 2022 and four per cent in 2023. Pre-pandemic real export volumes will be reached by 2022 and comfortably surpassed by 2023. Strong interprovincial and global demand for goods and services, after nearly two years of plants sitting largely underused, will drive exports.

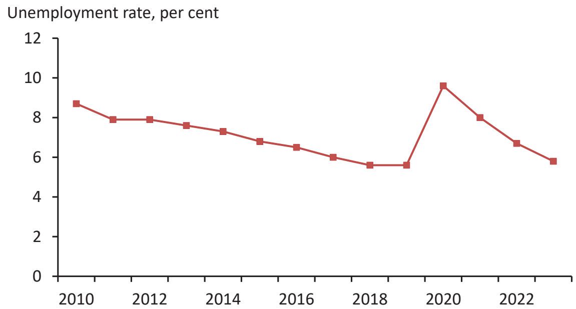
Ontario Labour Market

Ontario's unemployment rate is forecast to start sliding down in 2021 to eight per cent, a sizeable drop from the nearly 10 per cent unemployment rate in 2020 due to robust hiring (up 4.2 per cent). As the economy continues to open further and areas that faced significant impacts in 2020 such as household consumption, business investment and expenditures on machinery and equipment will rebound and intensify the need for labour.

Strong hiring growth in 2021 will entice many potential workers off the sidelines and into the labour force. The participation rate is forecast to swell to 64.8 per cent in 2021 up from 63.5 per cent in 2020. The labour force is forecast to increase 2.5 per cent on stronger immigration flows and laid off and idle workers re-entering the labour market.

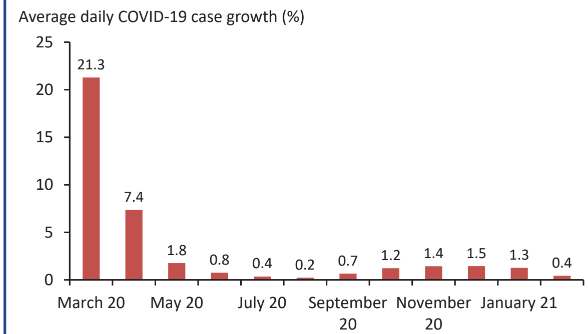
Employment growth for the remainder of the forecast is expected to remain robust and above trend, averaging 3.2 per cent per annum in 2022 and 2023, lifted

Strong post-pandemic hiring growth will gradually bring down the unemployment rate



Source: Statistics Canada, Central 1
Latest: 2023

COVID-19 daily case growth is slowing down but risks remain elevated



Source: Ontario Public Health, Central 1
Latest: Year-to-date February 2021

by a growing economy with greater expenditure and a drawing down of savings accumulated during the pandemic. With stronger hiring growth compared to growth in the labour force, the unemployment rates are forecast to continue sliding, averaging 6.7 per cent in 2022 before finally reaching nearly pre-pandemic level by 2023 at 5.8 per cent.

The unemployment rate is not expected to reach pre-pandemic levels until likely mid-decade as hard-hit areas in services will need at least a couple of years to rebuild from the pandemic even with supportive consumer demand and expenditures. For example, sectors in tourism will need to pivot to new and likely permanent procedures and rules which will slow down travel demand for a few years. The same could be said of arts, entertainment, and recreation as concerts and sporting events will gradually return to normal with new procedures (i.e., vaccine passports/certificates).

Active COVID-19 cases and positivity rate trending down in Ontario but risks remain high.

The latest public health restrictions and the province-wide lockdown have helped tamp down the spread of the virus considerably while vaccine deployment is ongoing.

Further declines in case counts move the province into a situation where some economic restrictions may be relaxed, while vaccines provide more support for medium-term economic growth as a growing proportion of the population is inoculated. At the same time, there remain clear negative risks to the outlook.

The challenging second wave and arrival of new virus variants requires vigilance against increased spread of the virus and accelerated vaccine deployment. However, Canada is at a disadvantage given the lack of domestic vaccine production and a push by Europe and the U.S. to inoculate its population first. This could delay the economic recovery and push back efforts to re-open tourism and the hardest hit sectors.

Muted household expenditures

A real risk to the recovery is consumers tightening their belts post-health crisis to shave down debt loads. The pandemic has profoundly affected household balance sheets and changed consumer preferences. It is very possible that once the pandemic is under control and the economy opens many consumers will not return to old habits quickly. A recent report suggests that many Canadians may actively repair finances and repay debt by controlling spending[2]. It is not a foregone conclusion that households will tap into their sizeable pandemic savings for discretionary spending once the economy is fully open. Canadian households hold above average debt loads compared to many other countries and labour market uncertainty could remain high post-health crisis and erode consumer confidence. If the economy can rebound quickly and long-term scarring is kept to a minimum, this risk can be largely mitigated.

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2 https://www.bloomberg.com/news/articles/2021-01-12/canadian-households-focus-on-repairing-finances-not-spending

Ontario Forecast Table

Provincial Forecast	2017	2018	2019	2020	2021	2022	2023
GDP at market prices	4.3	4.1	3.8	-5	5.2	6.5	5.3
Real GDP, expenditure-based	2.8	2.8	2.1	-5.7	4	4.4	2.9
Household consumption	4.2	2.9	1.9	-5.9	4	4.8	3.4
Government expenditure	1.8	4	1.4	-1.2	0.6	0.4	1.1
Government capital formation	7.9	6.1	0.8	-2.1	0.8	5.2	-0.3
Business capital formation	2.5	4.4	-1.1	-4.6	5.2	7.8	4.9
Residential structures	0.8	-3.6	0.5	1	1.6	2.5	5.3
Machinery and equipment	6.4	6.5	-0.6	-17.3	5.9	17.7	-0.6
Non-residential structures	0.4	19.8	-4.3	-5.4	10.1	6.7	8.2
Final domestic demand	3.5	3.4	1.2	-4.5	3.3	4.2	3
Exports	0.5	1.1	2.1	-10.8	5.6	6	4
Imports	3.1	2.3	0.6	-10.2	5.5	5.5	3.2
Net exports, $2012 bil.	-4.4	-9.2	-3.5	-5.4	-5.2	-3.8	-1
Employment	1.8	1.6	2.9	-5	4.2	3.5	2.9
Unemployment rate (%)	6	5.6	5.6	9.6	8	6.7	5.8
Personal income	4.2	4.6	4.3	6.8	-5.8	4.2	4.5
Disposable income	4.6	4.6	4.2	13.4	-8.9	3.3	3.2
Compensation of employees	4.6	6.1	4.6	-2.7	4	5.3	5.4
Net operating surplus: Corporations	1.6	0.6	0	-14.5	-2.4	19.6	6.7
CPI	1.7	2.4	1.9	0.6	1.7	1.8	2.1
Retail sales	7.7	4.5	2.3	-3.7	5.8	8	5.4
Housing starts, 000s	79.1	78.7	69	80.6	73.1	74.8	77.3
Population Growth (%)	1.4	1.7	1.6	1.3	0.4	1.4	1.8
Key External Forecasts							
U.S. Real GDP	2.4	2.9	2.3	-3.5	4.8	4	2.3
Canada Real GDP	3.4	2.1	1.6	-5.5	4.3	4.8	3
European Union Real GDP	2.7	1.9	1.3	-6.8	4.8	3.9	2.2
China Real GDP	6	6.9	6.1	1.3	8.2	5.5	4.9
Japan Real GDP	2.2	0.3	0.8	-5.5	3	1.7	0.9
Canada 3-month t-bill, %	0.71	1.4	1.66	0.5	0.3	0.3	0.5
Canada GoC long-term Bond, %	2.18	2.33	1.73	1	1.1	1.3	1.8
U.S.-Canada Exchange Rate, cents/dollar	77.05	77.16	75.37	74.6	77	77	77.06
Crude Oil WTI USD$ per barrel	50.88	64.94	56.98	38.5	51	53	56
Henry Hub Natural Gas Price, US$ per mmbtu	2.99	3.17	2.57	2.01	2.9	3	3

Source: Statistics Canada, CMHC, Central 1 CU.

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