Economics | Current Economic Trends

Ontario Economic Briefing

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central 1 Economics

Highlights

- Residential and commercial building permits down significantly in April
- Large decline in multi-family residential projects pulls down overall residential investments as single-detached home projects remain flat
- 58.7 per cent of businesses feel it is much harder to find workers now than a year ago
- Gains were reported in both services-producing and goods-producing industries in March, with expansion in 14 of 20 industrial sectors
- Toronto resale market continues to tumble with no bottom in sight yet

A 20 per cent jump in non-residential investments assures overall building permit volumes rose 2.5 per cent in April

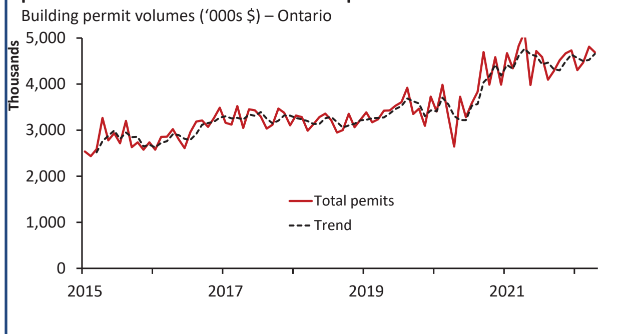
Edgard Navarrete, Regional Economist

Total building permit volumes fell by 2.5 per cent m/m in April 2022 after posting a very strong 7.7 per cent m/m rate of growth in March.

Provincially, the fall in future building intentions came from a strong contraction to residential building permits, down 11.7 per cent m/m owing to a strong contraction to multi-family units (down 21.7 per cent m/m) while single-detached homes remained relatively flat (up 0.3 per cent m/m). Currently, increased input costs, slowing housing demand and skilled labour shortages are all pushing residential investments down.

While investments in residential fell in April, non-residential investments jumped by 20 per cent m/m on the back of strong growth in industrial investments (up 48.8 per cent m/m) and institutional investments (up 78.6 per cent m/m) easily outstripping the fall in commercial investments (down 7.9 per cent m/m). Typically, commercial investments in Ontario account for the majority of non-residential investments, nearly half, so the jump in industrial and institutional volumes

Significant slow down in residential investments pulls Ontario's total building permit volume down in April



Source: Statistics Canada, Central 1 latest: Apr/22

is even more surprising. Commercial investments may potentially be headed towards a down trend as increased borrowing costs, weakened consumer demand and the persistence of hybrid work all are all real risks. Commercial investors must be more prudent about location and scope of projects until the turbulence in the economy subsides.

Year-to-date, total building permits are down 3.7 per cent as residential investments still lag last year by 8.7 per cent, even as non-residential investments are up 9.2 per cent. Non-residential investments are up due to a large relative boost to industrial projects which lead last year's pace by 75.6 per cent.

In Ontario's census metro areas, total building permits are down 6.9 per cent m/m in April due to a large residential investment contraction (down 16.8 per cent m/m) partially offset by a 19.6 per cent m/m jump in non-residential projects.

Total building permit volumes fell in 7 of the 16 metro areas of Ontario with the following areas posting significant m/m contractions in April:

- Barrie down 68.3 per cent
- Guelph down 39 per cent
- London down 24.2 per cent
- Toronto down 13.1 per cent
- Ottawa-Gatineau down 12.1 per cent

Ontario businesses are resilient but continue to face many headwinds

Edgard Navarrete, Regional Economist

Statistics Canada released Canadian Survey of Business Conditions data for the second quarter of 2022. As expected, many of the headwinds faced by businesses in Ontario are issues that are well documented during, at least, the last six months.

According to the latest results, most businesses expect the conditions to remain the same (78.7 per cent), slightly higher than the national average (76.7 per cent) and despite all the uncertainty over the last two and a half years of pandemic and inflationary shocks, Ontario businesses prove resilient. Over the next three months Ontario businesses are most worried about skilled labour shortages and recruiting talent, rising input and transportation costs.

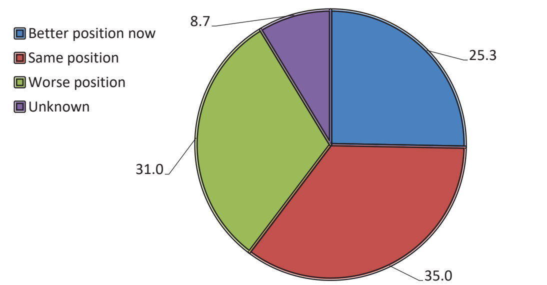
Of the businesses surveyed, 58.4 per cent feel that it is currently harder to find talent than a year ago. As expected, the need is even more acute for very technical services such as professional, scientific and technical services (62.7 per cent), healthcare and social assistance (79.7 per cent), and for client-facing services such as accommodation and food services (73.1 per cent), arts, entertainment and recreation (62.2 per cent). Fewer immigrants than usual, increased retirements during the pandemic and people leaving industries to move to other provinces or retraining in new areas are all affecting the supply pool for businesses. This aligns with low unemployment rates and increased job vacancies.

Firms are responding with management working more hours (50.4 per cent of firms) and having existing staff work more hours (41.9 per cent).

Inflationary pressures are affecting the supply of labour and more and more workers are demanding higher wages to close the gap with the cost of living. Businesses understand this, and over half (53 per cent) know that inflation will be a central issue of wage discussions with employees over the next year. The issue again becomes more acute for client-facing services such as accommodation and food services (84.2 per cent), arts, entertainment and recreation (68.7 per cent), administrative and support, waste management and remediation services (67.4 per cent), and healthcare and social assistance (55.1 per cent). Many of these areas pay at or slightly above the minimum hourly wage and with cost of living going up, many are leaving these sectors for more lucrative areas.

60.3 per cent of Ontario businesses at least in the same position if not better than 2019

Current business conditions compared to same time in 2019, per cent of respondents



Source: Statistics Canada, Central 1 Latest: Q2 2022

Manufacturing is an area that has a very acute case of wage inflation (80.8 per cent) with many owners feeling that inflation will be a greater issue when discussing wages over the next year. Many jobs in manufacturing are highly skilled, and considering labour shortages, current employees have substantial negotiating power.

Supply chain issues are a major concern for business owners in Ontario and it is affecting production. Many businesses surveyed feel that sourcing inputs domestically (43.6 per cent), and abroad (36.7 per cent) will be an issue over the next year and this will influence maintaining inventory levels over the next year (31.0 per cent of respondents). The war in Europe has exacerbated energy costs for everyone, including businesses. A sizeable number of Ontario businesses (39.3 per cent) feel that energy prices will continue to climb and 54.3 per cent of businesses surveyed believe these costs will be passed onto consumers via higher prices for goods and services.

To combat some of these increased costs, businesses may need to take on more debt although according to the survey, fewer than half of the businesses (43.6 per cent) are able to do so. The pandemic dwindled contingency funds significantly and many businesses already have significant debt on the books. Taking on new debt, therefore, becomes more difficult, particularly as borrowing costs are now climbing during a monetary tightening phase aimed at controlling inflation.

Finally, despite all the challenges, Ontario businesses have proven to be resilient. Of those surveyed, over 60 per cent feel that business today is about the same as or better than 2019 (35.0 per cent and 25.3 per cent respectively). The rate for client-facing businesses who are equal or better falls off by seven per cent on average in areas like accommodation and food services, retail trade, and arts, entertainment and recreation.

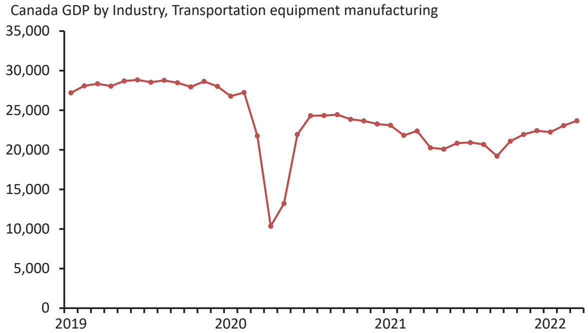
Canadian GDP growth kept climbing in March, led by continuous recovery in client-facing industries

Ivy Ruan, Economics Research Associate

In March, Canadian real gross domestic product (GDP) at seasonally adjusted at annual rate (SAAR) was up 0.7 per cent from last month, with gains in both services-producing sectors (0.6 per cent) and goods-producing sectors (0.9 per cent). Having COVID-related restrictions largely lifted across provinces, preliminary April estimates point to continuous growth, but at a lower rate of 0.2 per cent due to market volatility from inflation, rate hikes and geopolitical conflicts. Changes in consumer spending behaviors amid higher prices may also add negative pressure to the Canadian economy.

Motor vehicle and motor vehicle parts reported steady growth in March

Canada GDP by Industry, Transportation equipment manufacturing



Source: Statistics Canada, Central 1 Latest: Mar-22

While provincial GDP is unavailable, Ontario likely contributed significantly to the national gains in client-facing industries in March as its capacity limits in all indoor public setting were lifted. Growth in hard-hit client-facing services sectors will help recoup losses incurred during the last Omicron-led wave. The accommodation/food services sector expanded 10.9 per cent in March and transportation and warehousing rose 3.2 per cent, largely thanks to increases in air transportation (57.2 per cent) and public transit ridership (3.0 per cent) from rising travel demand. As a popular travel destination and transit centre, Ontario is expected to see steady gains in related sectors during the coming months.

Ontario is relatively more exposed to the manufacturing sector. On a national level, manufacturing sector surpassed the pre-pandemic level with gains on both durable (1.2 per cent) and non-durable (0.5 per cent) goods manufactured in March. Transportation equipment manufacturing, a key contributor to Ontario's provincial economy, reported national increases in motor vehicle (8.8 per cent) and motor vehicle parts (6.7 per cent) and represented a key segment of the national growth in durable goods manufactured.

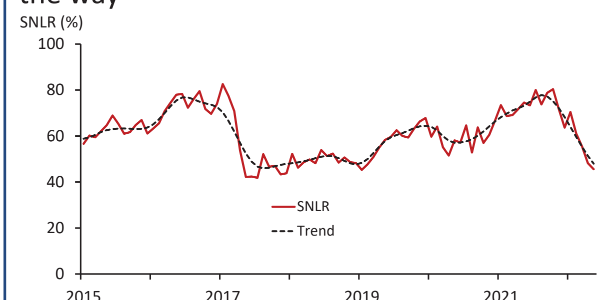
Home sales fell an additional 8.1 per cent in May, market continues to rebalance

Edgard Navarrete, Regional Economist

Toronto's resale market is now on a down trend with three consecutive months of data showing weaker activity. Sales fell a further 8.1 per cent m/m in May while new listings fell an additional 2.8 per cent m/m. Compared to a year ago, sales are down 37.5 per cent, due in part to base year effects, while new listings are still up 2.3 per cent from a year ago; but again that is likely reflective of base year effects as the market was very tight a year ago and buyers dealt with the ongoing lack of supply.

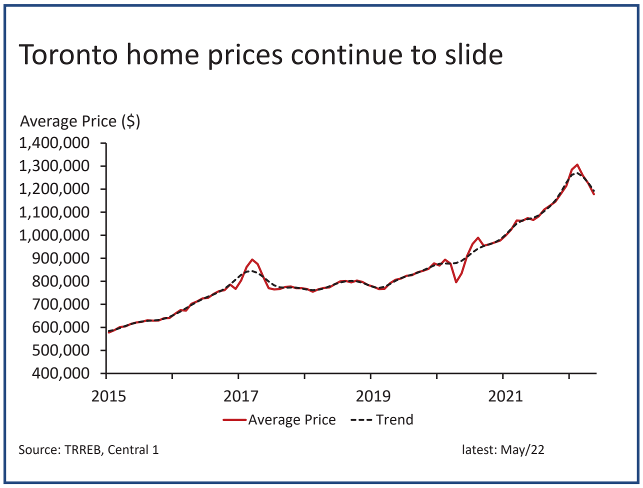
With another month of weaker sales, the monthly tally (6,507 seasonally adjusted units) is now lower than at the same time in 2019. The increased costs of borrowing have really affected buyers psychologically and the ongoing inflationary pressures are also not helping consumer budgets leading to many opting to forgo a purchase. Moreover, with the market in flux, many potential buyers are worried about purchasing a unit and not being able to obtain financing as home valuations in some segments are declining and any significant difference between market value at time of purchase and when the financial institution appraises the unit will have to be made up by the buyer. Some anecdotal evidence points to some buyers now experiencing buyer's remorse and looking to back out of deals; it is not a huge trend but something that is presently creeping up slowly.

Tighter monetary policy has really cooled Toronto's housing market with more hikes on the way



Source: TRREB, Central 1 latest: May/22

Interestingly, during this downturn, the average days on the market remain low with May's average days on market for a unit at 12 days, in line with a year ago when the average days on market was 11 days. Whereas the average days on market was low a year ago due to units being snapped up very quickly after intense bidding wars, the current trend may see sellers backing off quickly if they don't get a quick sale.



With sales falling at a faster clip than new listings, the market continues to rebalance and the SNLR continued to slide down in May coming in at 45.5 per cent from 48.2 per cent in April. Tighter monetary policy has been able to cool the market quickly and bring it back down to a balanced market. With less euphoria in the market, price gains are also moderating as buyers have more negotiating power. The average price for a Toronto home in May fell an additional 3.8 per cent adding to the drop values over the previous two months. Now the average home price stands at $1,177,856. Even with the ongoing cooling, current home valuations remained 31.8 per cent above what they were prior to the pandemic in February 2020.

Over the first five months of 2022, sales and new listings are down 30.4 per cent and 8.7 per cent respectively. The average home price continues to hold up and is still 18.9 per cent ahead of last year's pace.

The Toronto Region Real Estate Board (TRREB) releases a constant quality housing price index (HPI) each month. According to the latest estimates, the overall HPI fell 3.7 per cent in May, the steepest m/m decline since July 2017 when policy intervention last cooled the market. May's single-detached homes saw a stronger pull back in HPI values than higher density housing including townhomes and condo apartments. With affordability top of mind for buyers still actively looking for a home and price levels for single-detached homes still unattainable for many, high-density housing has become more popular.

The Bank of Canada has signaled from its most recent policy rate decision meeting that they are ready to move beyond the neutral policy rate band of two to three per cent if needed to cool persistent inflation. Increased policy rate hikes will continue to affect buyer psyches and keep more buyers away from the market until the market settles.

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