Canadian Construction Association
Best Practices Services

ICIC Construction Sector Quarterly Insights

Q3 2022

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Overview for Third Quarter 2022

Highlights:

- **Sentiment for Industrial, Commercial, Institutional and Civil (ICIC) Construction remains positive in North America**

- **Two critical issues currently inhibiting the industry's growth: the unprecedented post COVID-19 workforce shortages and the rapid growth in the prices of construction materials**

The macroeconomic changes that are important for the industry to continue monitoring over the second half of the year are:

Rising interest rates: Expected interest rate hikes by the Bank of Canada (October 26 and December 7) and the Federal Reserve of the United States (November 2 and December 13).

Geopolitical escalations: The ongoing conflict in Ukraine and new sanctions on Russia.

Changes in global oil production: Future announcements in oil production by OPEC+.

This report was prepared by the Canadian Construction Association (CCA) to provide an overview of the current economic health of the industry and implications for member businesses.

Workforce shortages and rising cost of materials hindering industry growth

Over the last two years, the construction industry has experienced growth in part due to the large financial supports made by governments in response to the COVID-19 pandemic. However, the momentum driving the construction sector has softened as of late as changes in the macroeconomic environment start to weigh on investments and take a toll on global expectations of economic activity. As central banks fight rampant inflation around the world and as the Bank of Canada tries to lower inflation growth back to its 2 per cent target, rising interest rates are gradually slowing down economic growth. Industries sensitive to interest rate changes, such as construction, are feeling these changes faster than others.

Firms consulted for the **Business Outlook Survey** by the Bank of Canada felt the economy is falling back to normal levels following the fast economic recovery from the pandemic.

That said, sentiment for non-residential construction remains positive in North America. The non-residential sector continues to stay strong despite inflation and labour challenges thanks to the support of fiscal initiatives used to offset the shocks caused by the COVID-19 pandemic and private investments made in the sector.

Although investments remain strong, the construction businesses surveyed raised two critical issues currently inhibiting the industry's growth: the unprecedented post COVID-19 workforce shortages and the rapid growth in the prices of construction materials.

Q2 Industry Performance Overview

Non-residential construction sector

Canada's economy grew by 1 per cent during the second quarter of the year. Growth in all industries, except for the transportation and accommodation sectors, has peaked or slightly declined as businesses began to experience a slowdown through the first half of 2022 as the economy returned to normal levels.

Construction (residential and ICIC) contributed $152 billion to the GDP in Q1 and Q2, or 7.45 per cent of the total GDP [Chart 1] . However, the construction sector across Canada was one of the six industries whose growth decreased during Q2, contracting by -0.56 per cent. The slowdown in the sector was mainly driven by declines in residential construction. Non-residential building construction contracted by -1 per cent during Q2 2022. Engineering and other construction activities (heavy and civil construction) helped offset the decline, as these services posted a growth of 2.17 per cent during the same period [Chart 2].

Investment

Sentiment in non-residential construction remained positive in Canada. Construction investments have continued an upward trend since October 2021. Investment in non-residential construction rose 5 per cent in Q2 2022, above the pre-pandemic high seen in Q1 2020, reaching $5.34 billion in July [Chart 3]. The governmental as well as industrial and institutional sectors drove the increases as they grew 21.6 and 5.1 per cent, respectively. The commercial component contracted 1.62 per cent over the same period.

The total value of building permits for non-residential building construction, a health indicator of building construction, declined by 5 per cent in Q2, yet they continue above their pre-pandemic trend. The decline comes after a record-high value of permits in Q1, where the permits for two large hospitals were issued. Building permits in the following three sectors, industrial, commercial, institutional and governmental construction, are 27 per cent, 5 per cent and 9 per cent higher than their pre-pandemic high of Q4 2019 [Chart 4].

Employment

Labour force levels in construction (residential and ICIC) remain above pre-pandemic levels. The labour force slightly increased (0.22%) during Q2 2022, adding 5,900 workers across Canada. Employment in construction (residential and ICIC) also slightly increased (0.44 per cent) during the same quarter, with an additional 6,600 jobs, and employing 1.52 million Canadians [Chart 5]. This is the third consecutive quarter where the number of workers employed is larger than the number of workers added to the workforce. Preliminary numbers for Q3 show a contraction of the labour force while employment saw slight gains. Under this preliminary scenario, approximately 96 per cent of the workforce is employed, leaving only four per cent, or 69,800 workers, to cover current vacancies in construction.

Vacancies in construction remain elevated, as shown by the latest data available for July, with 81,565 vacant positions. Construction holds 8.5 per cent of all vacancies across all industries. The construction sector continues to have a higher-than-average job vacancy rate compared to other economic sectors [Chart 6]. With such a high employment rate, the industry continues to face intense competition to find and attract workers with the relevant skills from other sectors.

Material inflation

Supply chain pressures have slowly eased during the first two quarters this year. The **Freightos Baltic index**, measuring the average cost of transporting goods using shipping containers, has slowly decreased as global supply chain health improves [Chart 7]. Looking forward, a weaker global economy and sluggish consumer demand may help ease supply chains further. Yet it will take some time until the shocks caused by the pandemic in the domestic supply chain are relieved.

The Industrial Product Price Index, which measures the average changes of all products used in the industry, increased by 5.25 per cent during Q2 2022, a slowdown of 1 percent compared to the previous quarter. The price of construction components stagnated during Q2, with some exceptions [Chart 8]. Easing prices of construction materials, such as lumber products (-9%) and cement (-10%), are helping cool down the inflation of non-residential construction materials. The metal and energy commodities, two important groups for non-residential construction, may play an important role in the industry during Q3 and Q4.

The group of primary ferreous metals that includes steel and iron products used in non-residential building construction, increased by 5 per cent during Q2. However, during July and August, steel and iron prices stagnated or slightly declined, partly due to the low domestic demand in the Chinese construction market [Chart 9]. Prices for hot-rolled iron (-15%), iron and steel pipes (-15%), unwrought aluminum (-3%), and copper (-11%) have all declined during Q2. Prices may rebound as China introduced a stimulus package for the year's second half to give steel and iron prices some upward momentum.

The price for energy and petroleum products, a group including motor and diesel gasoline, increased on a quarterly basis by 31 per cent. Prices for all components in this group have increased during Q2 due to the market volatility derived from current geopolitical events [Chart 10]. However, prices have eased during July and August. Notably, motor gasoline prices decreased by 10 per cent in August. Volatility in the group of energy products will remain as the world seeks to absorb the disruptions in the global energy markets.

Changes in labour and material costs for construction can be seen in the **Building Construction Price Index** (BCPI), an index that captures the price changes to construct a range of buildings. The index reveals an increase of almost 20 per cent in the cost of non-residential building construction over the last two years [Chart 11]. A similar increase in the price of constructing a building occurred over nine years, from Q2 2011 to Q1 2020.

What's ahead for the industry

Global economic growth projections for Q3 and Q4 were reduced as central banks continue to tighten monetary policy moving into 2023. Meanwhile, workforce shortages and inflation issues may persist, further slowing national economic growth. Businesses shared these expectations of future market conditions on the Canadian Survey on Business Conditions for Q3, a survey by Statistics Canada.

Respondents in the construction industry (residential and ICIC) cited inflation (72%), the rising cost of inputs (62.2%) and recruitment and retention of skilled employees (51%) to be an obstacle to growth through the next quarter. Although future economic growth may have softened, nearly three-quarters of businesses surveyed, including those in construction, remain very optimistic about their future outlook over the next 12 months.

The macroeconomic changes that are important for the industry to continue monitoring over the second half of the year are:

- **Rising interest rates:** Expected interest rate hikes by the Bank of Canada (October 26 and December 7) and the Federal Reserve of the United States (November 2 and December 13).

- **Geopolitical escalations:** The ongoing conflict in Ukraine and new sanctions on Russia.

- **Changes in global oil production:** Future announcements in oil production by OPEC+.

For more information on this report or the work CCA is currently focused on to address these issues, please email CCA Assistant Manager of Economics and Policy Development, Mario Baker (**mbaker@cca-acc.com**).

Quarterly insights summary data

Chart 1: Contribution of the Industry

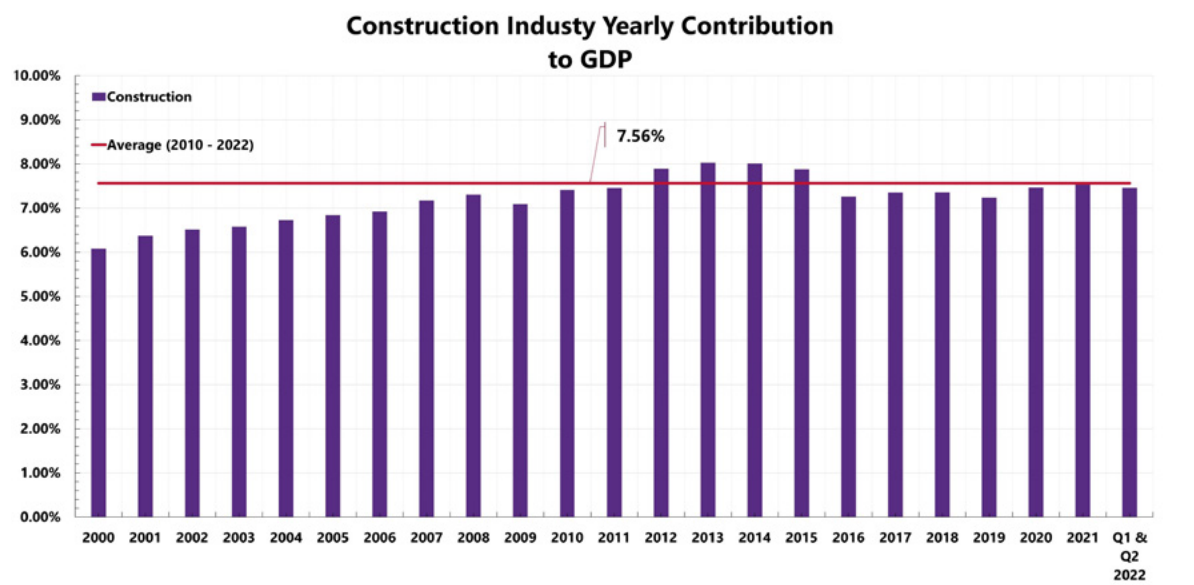


Chart 2: Growth of the Industry

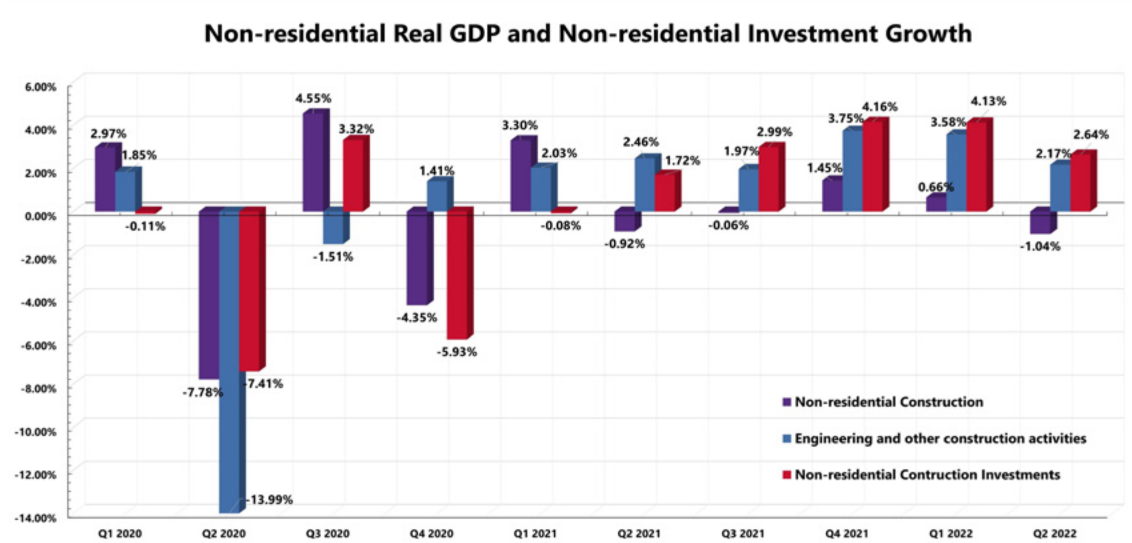


Chart 3: Investments in Non-residential Construction

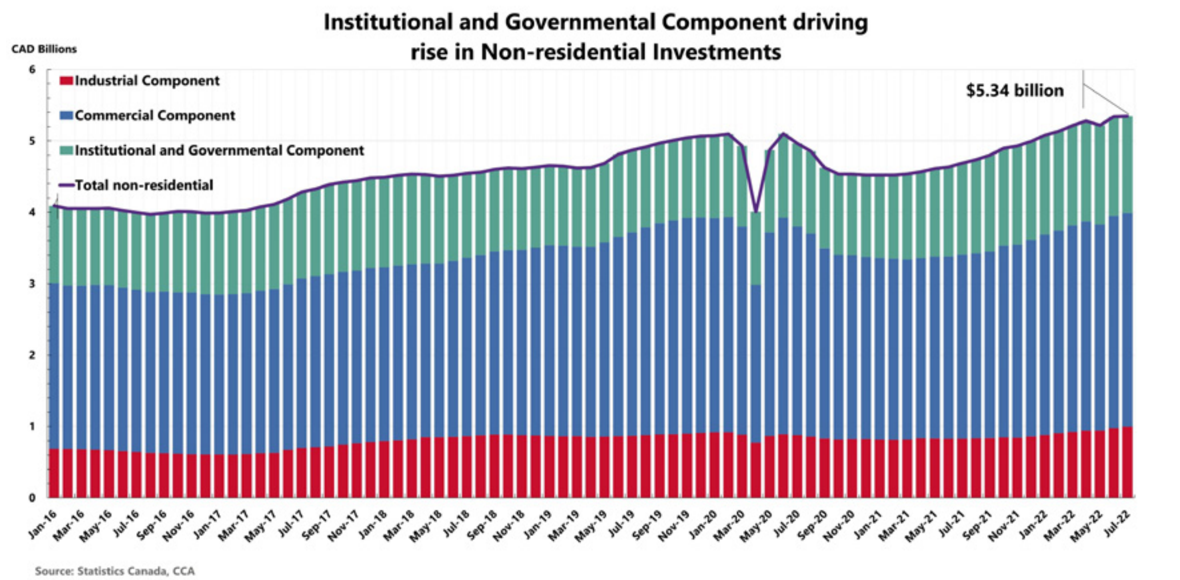


Chart 4: Building Permits

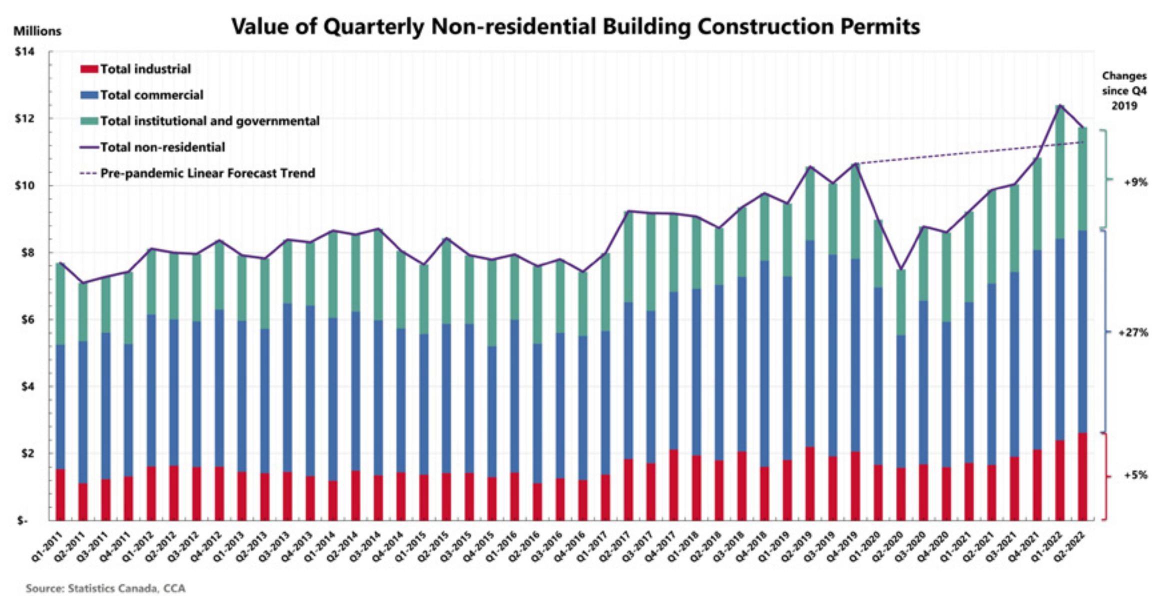


Chart 5: Workforce

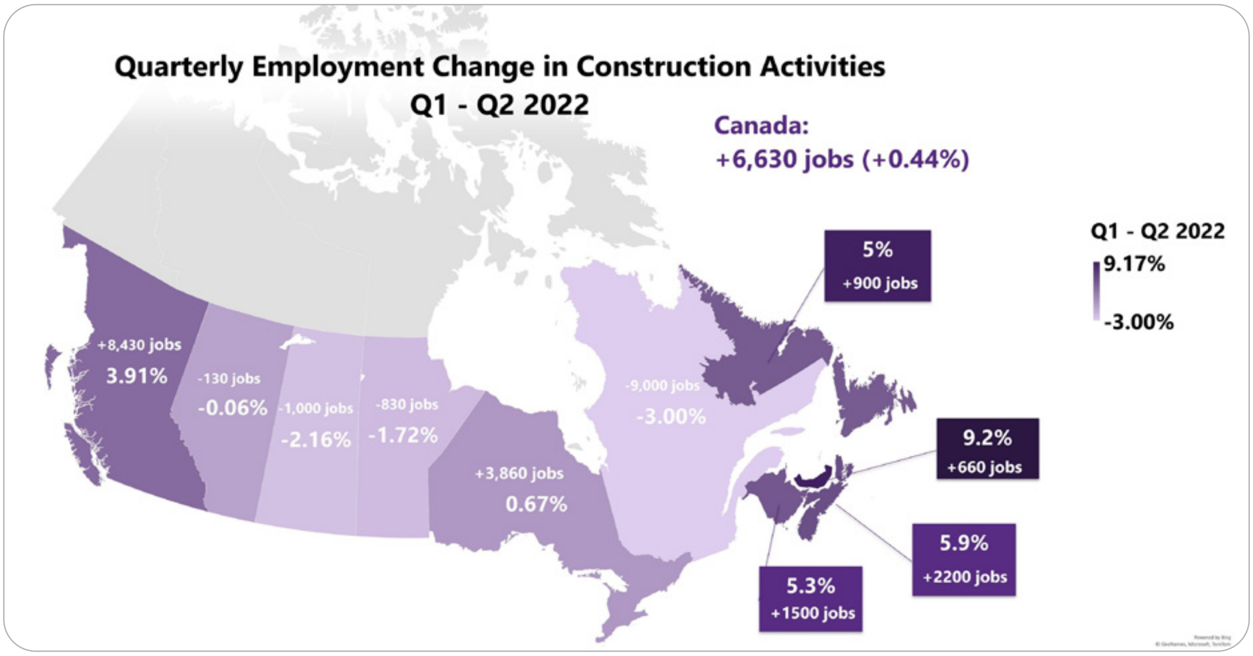
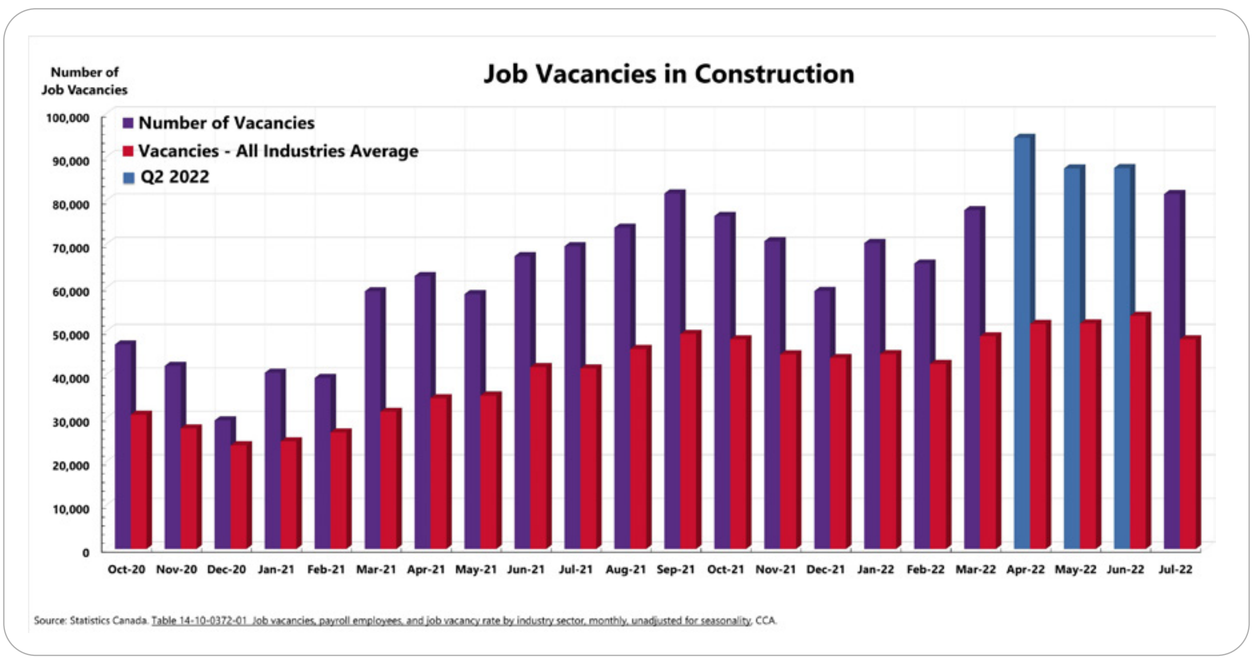


Chart 6: High Construction Investments = More Jobs Created



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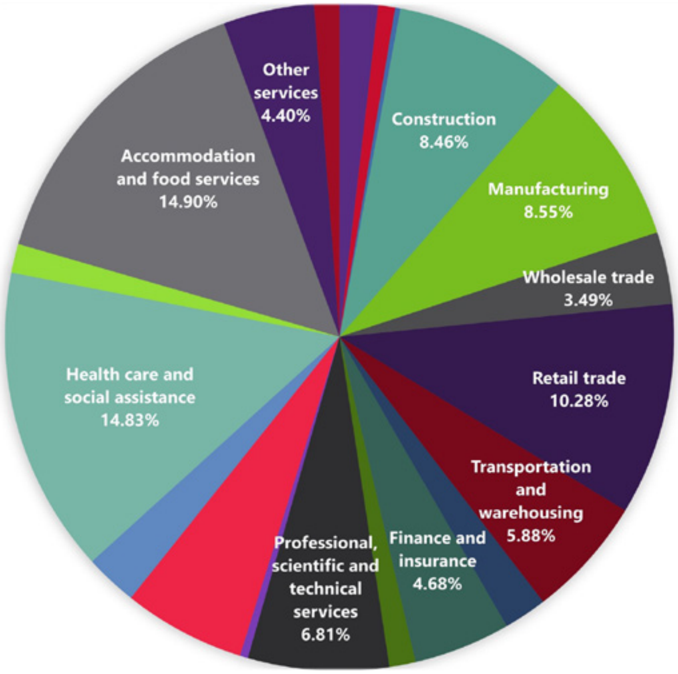

Chart 7: Supply Chains / Container Bottlenecks

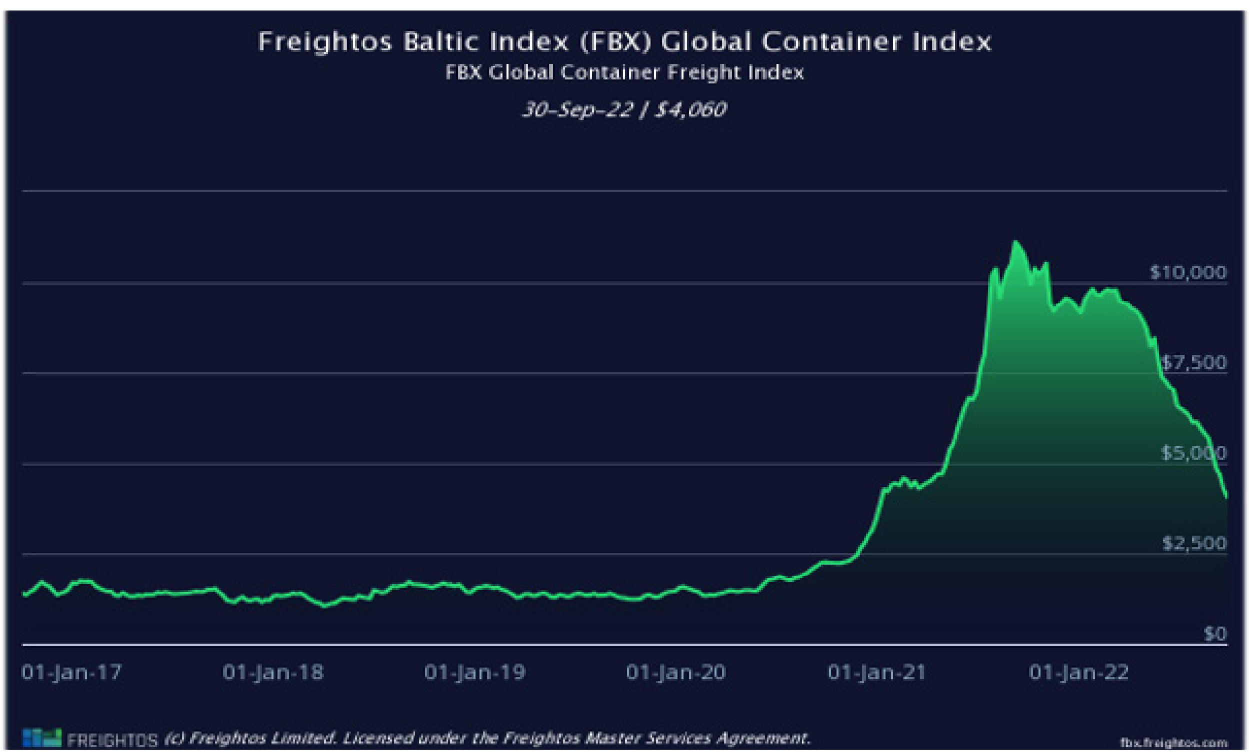

Chart 8: Inflation of Construction Materials

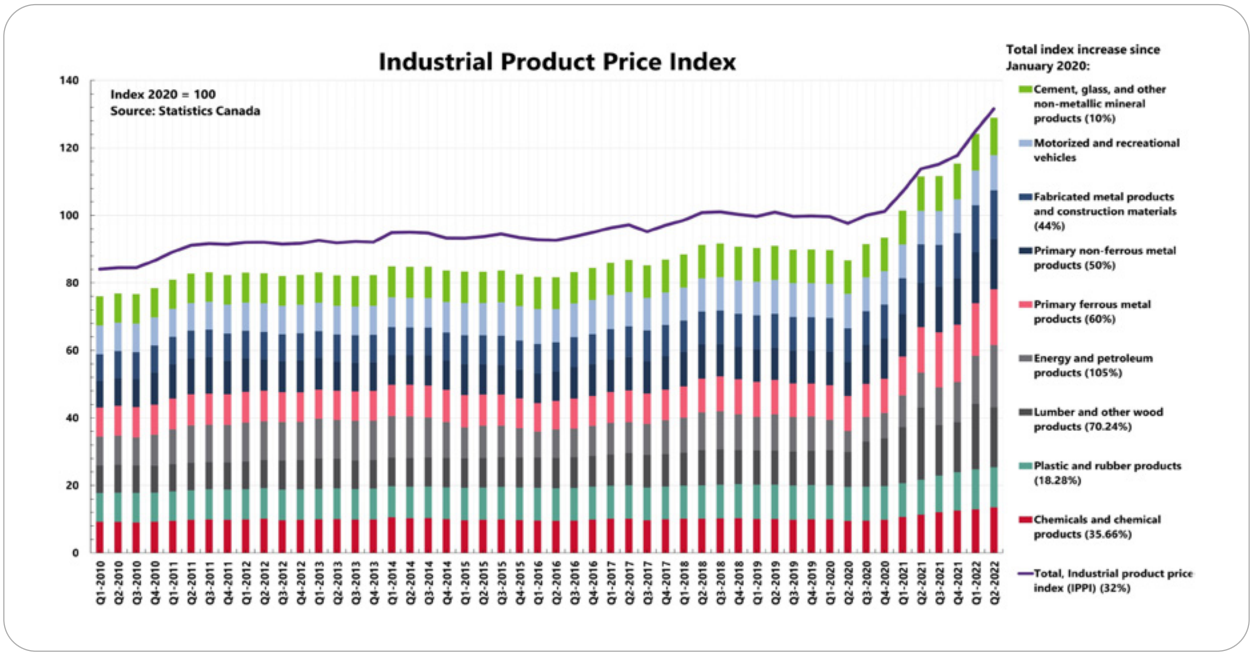

Chart 9: Inflation - Metal Products

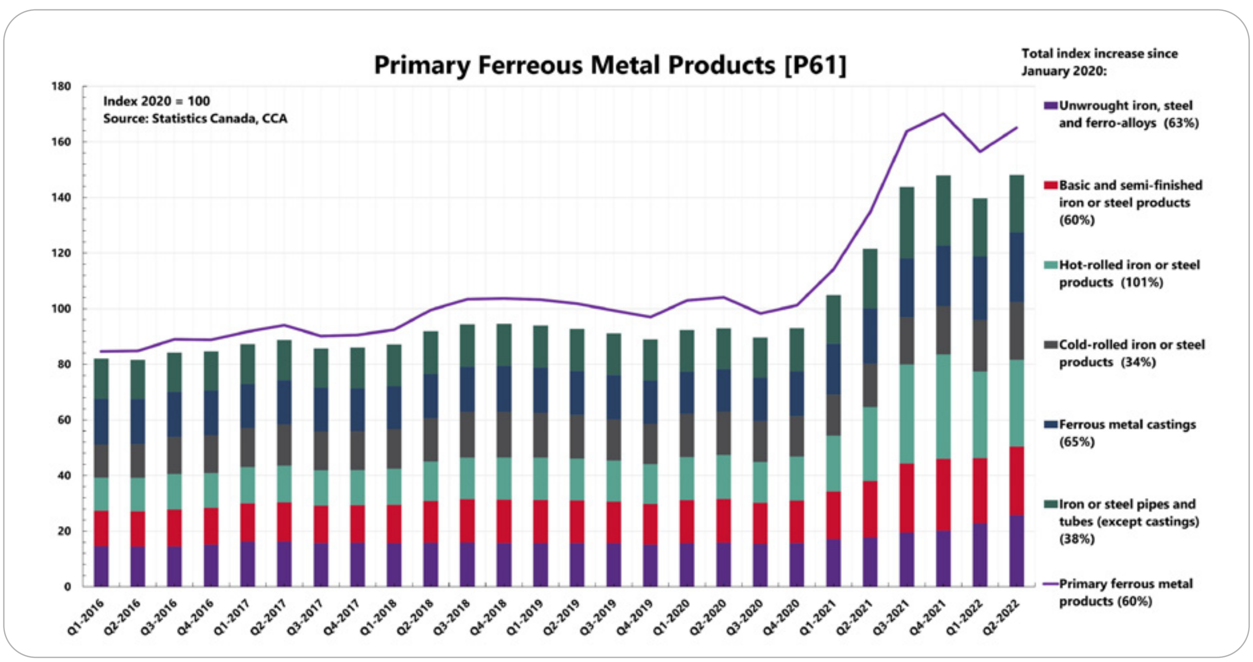

Chart 10: Inflation - Energy and Petroleum Products

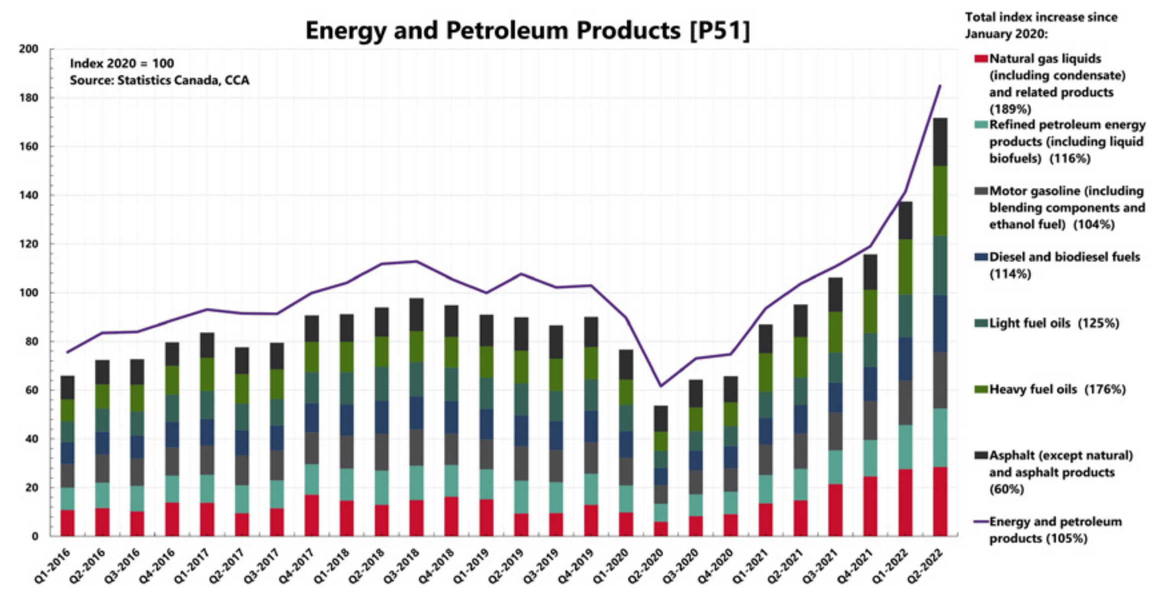

Chart 11: Building Construction Inflation