2015 FORECAST

BY JIM BARNES

OIL PRICES AND THE SPUTTERING WORLD ECONOMY RAISE RED FLAGS

Back in the spring, many industry leaders felt 2015 might be another banner year. Before the recent decline in the price of oil, Tim Talbott, president and CEO of Bird Construction Inc. in Mississauga, Ont., expected levels of business in the industry to increase slightly in 2015. “Now, it’s wait-and-see,” he says.

Michael Atkinson, president of the Canadian Construction Association based in Ottawa, says the association had been predicting the construction investment in Canada in 2014 to come in at around $293 billion. “That would have been a two to two-and-a-half per cent increase over the previous year,” he says. However, many forecasters in the industry have been revising their predictions lately. When assessing an outlook, take the date the outlook data was gathered into consideration, suggests Atkinson.

A potential slowdown is no news to Clive Thurston, president of the Ontario General Contractors Association. For his association’s members, “This is the worst year we've seen in a long time,” he says, referring primarily to projects worth less than $100 million. “I think next year is going to be a very, very tough year.”

“We are hearing that the emphasis in infrastructure will shift from the vertical to the horizontal—transportation, transportation, transportation. We're going to see sewer and water mains and roads getting the attention they need,” says Thurston.

“Resource commodities and infrastructure renewal have helped drive the recent market,” says Tim Smith, executive vice president, Buildings/ICI, EllisDon Construction in Mississauga, Ont. “Over the past two years, we were seeing investment in aging assets. There are a lot of products that are getting upgraded and revived.”

CURRENT EVENTS

A lot seems to have changed in the Canadian construction market in the second half of 2014.

One game-changer was a drop of roughly 20 per cent in the price of oil from the June 2014 peak. That drop was somewhat mitigated by a corresponding drop in the value of the Canadian dollar. The ultimate effect is unclear, and natural gas prices also are under pressure.

"We're expecting the West to remain hot in 2015, but the impact of the decline in the price of oil remains to be seen. It will be early to mid next year before we see any impact from that," says Talbott.

“Oil prices are forecast to decline until 2016 and increase thereafter,” according to the *Preliminary Investment Trends Report* from BuildForce Canada, published in September. Buildforce (formerly known as the Construction Sector Council) studies labour market data in the Canadian construction industry as a whole. Its research currently covers the period 2015 to 2024.

The report calls for oil to recover and exceed its previous peak price of about US$100 per barrel by 2019. Natural gas, however, is not expected to return to its peak due to competing supplies from shale gas deposits.

Canada’s dollar has dropped in value against the U.S. dollar significantly this year; currently it’s worth about US$0.88. That came as a relief to many in industry, since it enhances exports and led to a revival in manufacturing and new jobs. Exports were up 16 per cent in July over the previous year and saw strength in autos, aerospace, consumer products, machinery and equipment and other categories.

Statistics Canada reported that the industrial capacity utilization rate rose to 82.7 per cent in the second quarter, the fourth consecutive quarterly increase and the highest rate since mid-2007. The manufacturing sector tracked this number closely, with an 82 per cent rate. As capacity utilization rates grow, so will interest in new industrial construction.

While many other developed nations →

struggle with economic inertia, the U.S., Canada's primary market, remains healthy. Growth should be about 2.8 per cent in 2014 and average 2.9 per cent per year over the medium term, according to BuildForce.

The result has been job growth and an increase in consumer confidence. Canada added 43,000 jobs in October, pushing the jobless rate down to 6.5 per cent, its lowest level in six years. Employment rose markedly in Ontario, Manitoba, Nova Scotia and Prince Edward Island.

Another driver of construction demand is immigration. "The Canadian government just increased our immigration levels again," notes Atkinson. "We have well over a quarter of a million new Canadians every year. What are those people going to need? More infrastructure, more housing."

TWO STATES OF MIND

"This country is a tale of two different economies and two different states of mind. The West is generally positive, led by Alberta. In the East, Ontario is steady, but competitive from our perspective," says Talbott.

Published in May, the Atlantic Provinces Economic Council's (APEC's) *2014 Major Projects Inventory* identifies a record $122 billion worth of investment in 439 major projects in various stages of development across Atlantic Canada—up seven per cent over last year's report.

The Inventory calls for major project investment in Atlantic Canada to remain near record levels in 2015. However, beyond 2015 the level of activity is less rosy. "Our forecast beyond 2015 sees declining investment in Atlantic Canada as large projects such as Hebron and Muskrat Falls wind down," says Patrick Brannon, APEC's director, Major Projects. "The big question is whether proposed LNG export projects, the Energy East pipeline or new offshore or mining projects will be developed to keep investment strong later in the decade."

Newfoundland and Labrador: In TD Economics' *Provincial Economic Forecast*, published in October, summaries are provided of economic activity in each province. The report notes that following a surge in 2013, real GDP gains in Newfoundland and Labrador should be smaller in 2015 (2.2 per cent) and 2016 (1.8 per cent). Weaker

oil production and decreased capital investment are cited as causes. APEC lists 120 projects worth $49 billion, a nine per cent decline over last year. That is mainly due to completion of nearly $9 billion of investment activity last year.

Nova Scotia: Real GDP growth in Nova Scotia is forecast to average 2.5 per cent over the 2015-16 period, likely the best performance among the Atlantic provinces, notes TD Economics. According to APEC, 183 projects worth $55 billion will be underway in Nova Scotia. That's a 36 per cent increase over last year, largely due to H-Energy's proposed $3-4 billion LNG facility and an update in the value for the Pieridae Energy LNG project.

New Brunswick: APEC has identified 92 projects totalling $16.9 billion, down 11 per cent from last year. Part of the decline is the removal from the inventory of a proposed second nuclear power plant. Real GDP is forecast to rise by one per cent in 2014, before gaining a step in 2015-16 and averaging growth of just under two per cent, according to TD Economics.

Prince Edward Island: APEC lists 44 projects worth $2.1 billion in the Inventory, a 10 per cent increase over 2013. Federal infrastructure programs are largely behind the increase. TD Economics notes real GDP growth in Prince Edward Island is forecast to run at around 1.5 per cent over the forecast period, continuing the recent period of steady, modest gains.

CORE ECONOMIES

Quebec: Quebec's economy struggled during the first half of 2014, with real GDP up only 1.4 per cent, year over year, says TD Economics. The pace of expansion should strengthen to 2.3 per cent next year.

According to BuildForce, nonresidential construction investment will slow in 2014 and 2015, but is expected to resume growth in 2016 as new mining and pipeline projects launch.

Ontario: Growth is forecast to average a healthy 2.7 per cent in 2015 and 2.3 per cent in 2016, says TD Economics. Driving the change are the weaker loonie and growing exports, especially in manufacturing. BuildForce foresees investment in major resource development, electric utilities and transit system projects. Investment in these projects will grow until →

2017 and stabilize after that. Industrial building construction is also expected to increase. Stronger growth in commercial building construction over the outlook period should offset fluctuations in institutional building, researchers say.

Manitoba: can expect a sharp rise in manufacturing sales and output into 2015, thanks to the US recovery and a weak Canadian dollar, says TD Economics. Economic growth is forecast at 2.5 per cent in 2015 and 2.1 per cent in 2016. Non-residential construction will be driven primarily by projects in the mining and utilities sectors, says BuildForce.

Saskatchewan: According to TD Economics, economic activity is forecast to bounce back in 2015 (+2.5 per cent) before returning to around two per cent in 2016. BuildForce notes major mining and pipeline projects should drive investment in engineering and industrial construction. Demand is projected to rise over the near term, peak in 2017, and then slow down as major projects are finished.

Alberta: Calling for growth in GDP of 3.3 per cent in 2015, TD Economics expects Alberta's economy to outperform the rest of Canada for the next few years. "The recent pullback in crude oil prices will weigh on incomes and take some steam out of the economy going forward. We expect prices to stabilize in early 2015." Oil sands, pipeline, storage and electric power construction projects will keep Alberta's construction activity well above historical levels, says BuildForce. Maintenance work and sustaining capital projects will add to this activity.

British Columbia: Real GDP gains in British Columbia are forecast to increase to about 2.6 per cent on average over the 2015-16 period, says TD Economics. Upcoming LNG projects will fuel non-residential construction in 2016. Buildforce also spotlights LNG: "Industrial, LNG terminals, pipelines, utilities and mining projects are expected to ramp up over the medium term," says the report. "By 2017, construction investment is projected to set a new record."

The Canadian construction outlook continues to be very positive, despite some bumps in the road. In terms of public infrastructure, Atkinson notes it is no longer a question of "do we do it" but "when and how can we ensure that they get in place fast enough to help our economy?"

Generally speaking, the sector continues to generate a lot of new business. "Ask any contractor across Canada about their greatest need. It will be skilled tradespeople and skilled, experienced management people. For the foreseeable future, it is still a robust market," says Smith. ☐

Jim Barnes is a contributing editor to On-Site.

Residential keeps on ticking

Housing starts in Canada show ongoing health, despite increases in household debt ratios and the potential for higher interest rates. "We have had strong levels of activity recently, and we think that is going to continue," says Bob Dugan, chief economist, Canada Mortgage and Housing Corporation, Ottawa.

The fundamentals remain strong, he says. Mortgage rates will remain low, the job market is strengthening and net immigration to Canada's major urban centres remains high.

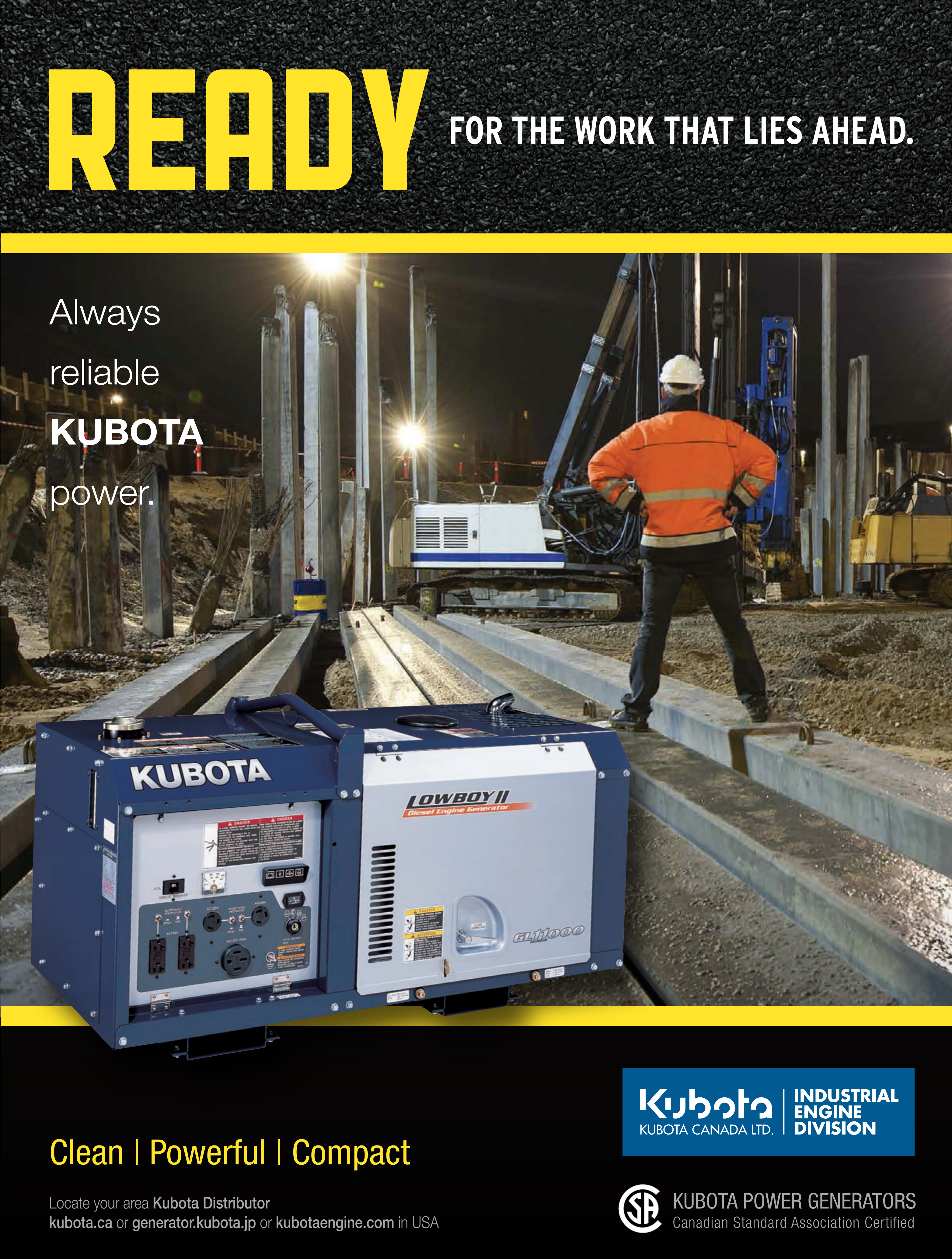
However, acting as a drag on growth are rapid increases in home prices in the large urban centres, demographic changes including a decrease in the size of the 25-34 year old segment (typical first-time buyers) and pending mortgage rate increases (possibly at the end of 2015). At present, Dugan notes there are above-average inventories of completed, unsold units in the market.

CMHC's most recent Housing Market Outlook was released in the fourth quarter of 2014. On an annual basis, it calls for housing starts to range between 172,800 and 204,000 units in 2015 and 168,000 units and 205,800 units in 2016.

Single-detached starts are expected to range between 70,400 and 83,600 units in 2015 and 67,000 and 83,000 units in 2016, a decline from 2013. Total multi-unit starts over the 2014 to 2016 period are expected to remain comparable to levels observed in 2013.

A significant downside risk would be a shock to the global economy that causes substantial unemployment in Canada. Since many Canadians have relatively high ratios of debt to income and a large proportion of their net worth in real estate, they may be trying to liquidate housing in a soft market to pay their bills.

"If the financial crisis taught us anything, it's the importance of liquidity," says Dugan.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