BMO Blue Book

Winter 2021

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BMO Blue Book — Winter 2021

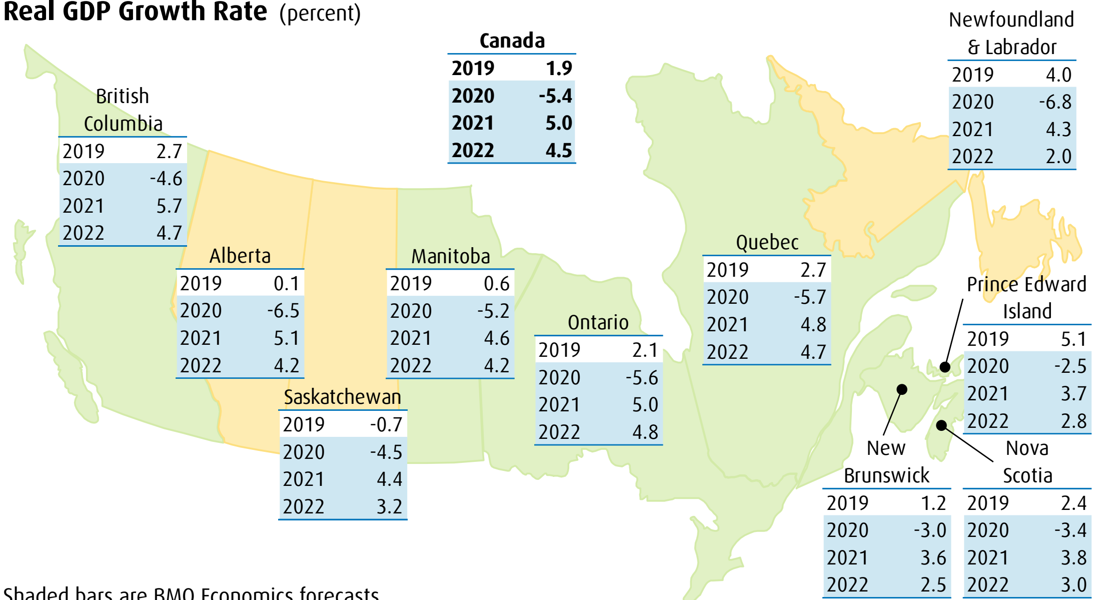
To Immunity and Beyond

Douglas Porter, CFA,
Chief Economist

The Canadian economic recovery ran into a hurdle at the turn of the year, with a number of large jurisdictions imposing second-wave lockdown measures related to the COVID-19 pandemic. The economy is expected to rebound a solid 5.0% this year, but the real gains will come after a first-quarter lull passes, with monetary and fiscal stimulus still extremely supportive, and a wave of pent-up demand likely coming. This year's growth will offset the 5.4% decline seen in 2020, leaving output roughly at pre-COVID levels by the end this year.

Provincial GDP

Real GDP Growth Rate (percent)



Region	2019	2020	2021	2022
Canada	**1.9**	**-5.4**	**5.0**	**4.5**
British Columbia	2.7	-4.6	5.7	4.7
Alberta	0.1	-6.5	5.1	4.2
Saskatchewan	-0.7	-4.5	4.4	3.2
Manitoba	0.6	-5.2	4.6	4.2
Ontario	2.1	-5.6	5.0	4.8
Quebec	2.7	-5.7	4.8	4.7
New Brunswick	1.2	-3.0	3.6	2.5
Nova Scotia	2.4	-3.4	3.8	3.0
Prince Edward Island	5.1	-2.5	3.7	2.8
Newfoundland & Labrador	4.0	-6.8	4.3	2.0

Shaded bars are BMO Economics forecasts

All Canadian provinces were hit by the pandemic, forcing some degree of economic disruption and digging fiscal holes of various depths. That said, Manitoba, Ontario and Quebec were facing more stringent **second-wave containment measures** as 2021 began, and those have been reflected in recent economic data. Indeed, those provinces, as of January, maintained the deepest employment shortfalls versus pre-pandemic levels at more than 5% each, even as some sectors (such as finance and professional services) have long fully recovered--recent declines in accommodation & food and retail have been significant. On the flip side, provinces that have avoided stringent restrictions have seen activity in a number of areas perform well through the turn of the year. British Columbia, for example, is seeing housing, manufacturing, retail

sales and small businesses sentiment all above pre-COVID levels, while jobless rates in Atlantic Canada have largely recovered.

British Columbia is expected to lead the country in real GDP growth this year, with a 5.7% rebound estimated. This firm recovery comes in part because the province has not had to implement tough measures to start the year.

Alberta has begun to ease various measures, and a better-than-expected oil price backdrop is encouraging. Real GDP is expected to rebound 5.1%, while business confidence has improved more than anywhere else in Canada in recent months. **Saskatchewan** and **Newfoundland & Labrador** should also benefit from an improved energy-price environment, with growth rates in the 4.5% range.

Manitoba is traditionally the most stable economy on the provincial landscape, with a diverse industry base providing a cushion. But, challenging COVID case trends force more aggressive containment measures, and the province has underperformed. Still, the economy should grow 4.6% this year despite a slower start.

Ontario's economy entered the pandemic with the strongest growth trends in more than 15 years. But, with the largest urban centre, the province has struggled more than most with the shape of its COVID curve, longer first-wave lockdowns, and now second-wave restrictions in most regions. Torrid housing and consumer spending performances should cushion the blow, even as impacted Main Street businesses continue to struggle and limit the rebound to 5.0%. As vaccination becomes more widespread later in the year, look for Ontario to lead the recovery.

Similarly, **Quebec** was enjoying multi-decade highs for economic growth before the pandemic, but has struggled heavily with COVID cases. That prompted aggressive lockdowns through the spring (a full shutdown of the construction sector, for example), and the first move into second-wave measures in the fall, which have persisted into February. As a result, Quebec will likely underperform with 4.8% growth this year, but the province should come back stronger in the second half of the year.

Finally, **Atlantic Canada** fared very well on the COVID front on a relative basis, but much of the regional economy is nevertheless impacted. The 'Atlantic Bubble' has been a success from a health care perspective, but has hurt activity in a number of sectors (think travel & tourism) that depend on flows from other regions. Longer term, a population boom had spurred above-potential economic growth in the region pre-pandemic, and it remains to be seen when those flows will return.

Christine Cooper,
Co-head,
Canadian Commercial Banking

Nadim Hirji,
Co-head,
Canadian Commercial Banking

Business Environment National Overview

Consumers and businesses—from smaller and scaling organizations to large corporations—have faced one of the most challenging times in recent history. The early stage of the pandemic was characterized by uncertainty. As it continued, we saw organizations grow increasingly resilient as they pivoted their business models to adapt to the changes that stood before them. We have an on the ground view of what the recovery looks like across the largest sectors of the Canadian economy.

While our clients recognize that challenges still exist, we see an underlying optimism for 2021. A couple provinces have faced extended restrictions related to the pandemic, which have put some additional pressure on businesses operating there. But the vaccine and eventual inoculation of the population should carry this optimism along for the year ahead. Also propping up sentiment is the expectation and hope of additional fiscal stimulus, pent-up demand for services, and a recovering global economy.

As we look across specific sectors, businesses operating in the agriculture and agribusiness industry are well positioned for 2021. Strong global demand for protein, grains and oilseeds is extremely positive. Producers looking for opportunity to increase processing capacity have provided strong investment in the sector. We saw supply chains pivoting to divert supplies to retail channels early on in the pandemic, and the back-end work that has already been established will carry forward well.

Technology and innovation is one of the shining stars in Canada, and few sectors have grown faster than Information and Communications Technologies; there has never been a better time for this sector to carry the torch and light the way to economic recovery in Canada. Amid the pandemic, there has been an accelerated shift to digital which is positioning this sector well both for the remainder of this year and beyond. COVID has also shifted financing to certain areas based on business and consumer needs. Life science and biotech firms have received more financing, and there has been healthy growth in areas like education technology and cybersecurity.

For real estate, 2020 brought with it one of the strongest market rebounds in history. Government relief measures and deferral programs were invaluable to commercial mortgage clients—it created a trickle-down effect of relief. While downtown office spaces continue to be challenged, some corporate landlords are using the time as an opportunity to re-invest in office towers. There is every expectation that Canadians will once again fill those towers—at least for a few days each week. As we look to the remainder of this year, we see stability in housing and commercial real estate markets.

We view our commitment to stand with our customers in both prosperous as well as challenging times as a competitive differentiator and as an obligation of our partnerships. Throughout the pandemic, we have introduced relief measures and facilitated access to government relief programs to help our clients bridge the gap to recovery. Our teams have also had thousands of conversations with clients to support their individual needs. And we have hosted many thought leadership forums which we hope have helped to add value during these challenging times. We operate as partners and, as the bank for business, we always stand behind our clients to find opportunities to help them on the way back up and facilitate their long-term growth.

Robert Kavcic,
Senior Economist

Provincial Economies

All Canadian provinces were hit by the pandemic, forcing some degree of economic disruption and creating fiscal holes of various depths. That said, the recovery is well underway across the country with all provinces set to post strong growth numbers in 2021. While fundamental factors such as demographics, resource prices, fiscal capacity and various industry trends will eventually reassert themselves, the outlook remains dominated by COVID and the race for vaccination.

British Columbia

The B.C. economy is expected to grow 5.7% this year, well ahead of the 5.0% rate estimated for all of Canada. That also follows a more mild 4.6% decline in 2020.

Quite simply, the province has not faced the same per-capita COVID case burden as the other large provinces, and containment measures have been much less severe. Still, there was no escaping the downturn in 2020.

The unemployment rate is expected to remain below the national average, at 6.8% for all of 2021, versus 8.0% for Canada.

Housing market activity rebounded strongly through the second half of 2020, with sales in Vancouver up 53% y/y in January. Price growth continues to accelerate, and residential construction activity is relatively steady.

The Province projected a $13.6 billion deficit in its latest fiscal update, or 4.9% of GDP, which is slightly deeper than the provincial average. Net debt should remain among the lowest in Canada at just over 22% of GDP, but the now majority NDP government has begun to hint at bigger spending priorities.

Alberta

The Alberta economy is expected to rebound 5.1% this year, slightly firmer than the 5.0% growth expected nationally. Relatively strict restrictions have begun to ease as COVID case counts have fallen sharply in recent weeks.

The rebound in oil prices have provided some relief, with WTI trading above $60 early in the year. But, President Biden's scrapping of a key KXL pipeline expansion permit highlights longer-term capacity constraints facing the sector. That said, depending on how export demand evolves (potentially flatter than previous assumptions), expansions of Line 3 and TransMountain could add 800k bpd of capacity by late-2022.

The unemployment rate finished 2020 at 11.1%, down from a 15.5% high earlier in the year. It is expected to average 9.3% for all of 2021, versus 8.0% for Canada.

After a multi-year period of weakness, housing markets in Calgary and Edmonton have strengthened, as seen across much of the country. Home prices in Calgary are still about 9% below the 2015 peak, but they are up modestly from a year ago. The commercial real estate backdrop remains tough, with high vacancy rates in the downtown office market.

The Province is expecting a $24.2 billion deficit in FY20/21, which weighs in at a heavy 8.1% of GDP. And, net debt has jumped above 22% of GDP, conceding its position as the lowest debt-to-GDP ratio in Canada.

Saskatchewan

The Saskatchewan economy is expected to grow 4.4% this year, somewhat flatter than the national average, but keeping in mind that the province was less impacted in 2020. Indeed, Saskatchewan was among provinces with the lightest COVID-related lockdown measures, which tempered the downturn somewhat. The resource sector remains challenged after a multi-year lull, but firmness in oil prices is encouraging, as well as a broader recovery in resource prices globally.

The unemployment rate sat at 7.2% in January, and is expected to stay below the national average in 2021, thanks to the better starting point. Still, the relatively muted backdrop aside from the pandemic will offer less momentum by 2020, and the province will continue to lose population to other provinces.

The Province is expecting a $2.0 billion deficit in FY20/21, which is a moderate 2.7% of GDP when compared to its peers. Net debt is on track to finish the year at the lowest share of GDP (19.4%) in Canada.

Manitoba

The Manitoba economy is expected to rebound 4.6% this year, trailing the national increase, reflecting a tough environment. Keep in mind that Manitoba typically handles downturns much better than the rest of Canada, but some of the most aggressive COVID-related measures have worked against that tradition. At one point, the province was dealing with the largest per-capita case count, and measures were implemented targeting retail, restaurants, bars, clubs and casinos.

The unemployment rate sits at 8.0% after topping 11% in April and May. But, after a second wave of steep declines since October, service-sector employment remains more than 6% below pre-COVID levels.

The Province of Manitoba is expecting a $2.0 billion deficit in FY20/21, or a relatively modest 2.7% of GDP. Net debt is expected to rise above 36% of GDP, still comfortably below Ontario and Quebec.

Ontario

Ontario's economy contracted an estimated 5.6% in 2020, similar to the 5.4% decline estimated nationally. The economy is expected to rebound 5.0% in 2021 (in-line with Canada), after a tough start gives way to a more powerful recovery later in the year.

The province's COVID case count has been running lower than the national average in per capita terms, but broad-based and lingering restrictions have affected the provincial economy, particularly in Toronto and surrounding areas.

The unemployment rate finished 2020 at 9.6%, down from a 13.5% high earlier in the year, before jumping above 10% amid January lockdowns. It is expected to average 8.5% for all of 2021, versus 8.0% for Canada. While sectors hard-hit by the pandemic (travel, accommodation & food, entertainment and various services) continue to

struggle, others such as finance and professional services have rebounded strongly, although still leaning heavily on remote work.

Housing markets across Ontario are exceptionally strong, especially outside the GTA. Existing home sales rose 8.3% for all of 2020, which is a feat considering the challenges in the spring. By the second half of the year, sales were pushing record levels, with January's tally the highest on record after seasonal adjustment. The strength reflects record-low mortgage rates, a swift job recovery in higher-paying industries, and a sudden shift in preferences toward larger homes outside the core. In the commercial real estate sector, downtown office vacancy rates have jumped to 7.2%, according to CBRE, from around 3% a year ago. This segment will remain challenged, and face a longer-term adjustment as post-COVID work practices change.

The Province of Ontario is estimating a $38.5 bln deficit for FY20/21 (4.5% of GDP), which is on the deeper end of the provincial spectrum. That said, this likely marks the worst point for the fiscal balance.

Quebec

The Quebec economy is expected to rebound 4.8% this year, slightly slower than the rate expected for all of Canada. The province continues to battle COVID-19 cases, and dragged some of the more significant containment measures into the new year. These include shutdowns to restaurants, cinemas, many forms of retail and schools. Quebec entered the pandemic in a position of strength, and the fundamentals still argue for outperformance after the pandemic—but it will take a while to get there.

After falling sharply to 7.2% by November, the unemployment rate has backed up to 8.8% amid a second wave of containment measures. Since the fall, employment in accommodation & food services and trade has fallen by more than 120k positions, though jobs in finance and professional services are at-or-near record highs.

The housing market is extremely strong, with sales and prices in Montreal still surging. Montreal's benchmark price was up almost 20% y/y in January. This partly reflects the impact of record-low mortgage rates and increased demand for larger homes, consistent with other major cities.

The Province of Quebec is expecting a $12.4 billion deficit in FY20/21, which is on the lower end of the spectrum at 2.8% of GDP. Keep in mind that Quebec was running sizable surpluses before the pandemic, so the deterioration is still significant. Net debt will top 43% of GDP, still below Ontario.

New Brunswick

The New Brunswick economy is expected to grow 3.6% in 2021, much milder than the rebound expected nationally. Keep in mind that the estimated contraction in 2020 was also much milder than most other regions. More recently, COVID-related measures have been much milder than in the larger provinces, helping avoid the worst of the second wave.

The unemployment rate has dipped below 9%, below the national average, for now, as some larger provinces are grappling with stricter containment measures. Employment in impacted industries, such as trade and accommodation & food, have

fully recovered their 2020 declines, leaving service-sector employment above pre-COVID levels.

While the province has seen a recent boost in population, demographic flows will be a medium-term issue post-COVID, potentially dampening a previous support.

The Province of New Brunswick is projecting the smallest deficit in Canada this year at $183 million or just 0.5% of GDP. Net debt will edge up to just over 38% of GDP. Given the heavy fiscal burden absorbed by the Federal government, the impact in the smaller Atlantic provinces has been more mild.

Nova Scotia

The Nova Scotia economy is expected to grow 3.8% this year, reversing a significant portion of the 3.4% decline estimated for 2020. Atlantic Canada more broadly has been relatively sheltered from COVID cases and associated lockdowns.

Still, various modest measures that have been implemented have chipped economic activity, and travel flows have been restrained, weighing on tourism activity. The outlook for the 2021 season is also still in limbo with vaccinations slow to roll out.

The unemployment rate effectively unwound all of the COVID shock, sitting at 8.3% as of January. Employment has recovered almost all of the decline since February 2020, while labour force participation is almost all the way back.

Resale housing market activity is extremely strong, with sales rebounding to record levels amid pent-up demand and shifting preferences toward locations outside urban cores. Residential construction has held steady, with little impact from the pandemic.

The Province of Nova Scotia is expecting a $778 million deficit in FY20/21, or 1.8% of GDP—that's modest compared to its peers. Net debt will rise to 38.2% of GDP, but the Province has made solid fiscal progress in recent years.

Prince Edward Island

The PEI economy is expected to grow 3.7% this year in a strong recovery from a COVID-plagued 2020. Keep in mind that the province was enjoying a significant boom before the virus broke out, leading the country in economic growth in 2019.

While COVID-related lockdowns have still weighed heavily, the pandemic curve has been much flatter given the small and closed-in nature of the province. Re-opening was quicker than most other provinces through last year, with a limited second wave.

The unemployment rate has reversed all the increase seen since the pandemic began, sitting at 7.9% in January. That partly reflects lower demographic inflows and a lower labour force participation rate.

Tourism and seasonal visitors during the summer months are major drivers of local economic activity, and both of those sources will be challenged again this year given a slow vaccine rollout in Canada. Additionally, an influx of international immigrants has boosted housing demand in recent years, but that looks to be at risk in the near term until immigration returns more strongly.

The FY20/21 deficit is pegged at $178 million, or a moderate 2.4% of GDP. Net debt is tracking below 35% of GDP, the lowest east of Saskatchewan.

Newfoundland & Labrador

The Newfoundland & Labrador economy is expected to grow 4.3% this year, after a deep 6.8% decline in 2020.

The province was already in a challenged position pre-COVID, but pandemic disruptions and the decline in oil prices exacerbated the headwinds. That said, a strong rebound in oil prices is encouraging for near-term prospects and income. Despite being relatively sheltered and having a flat COVID curve, the province saw more small business shut-downs than most early in the pandemic.

The unemployment rate jumped to almost 18% (highest in Canada) at one point last year, but has now settled in below 13%, which is more normal for the province, as jobs have fully recovered.

The Province of Newfoundland & Labrador is estimating a $1.8 billion deficit in FY20/21, or 6.0% of GDP. That is running smaller than initially expected, but will still lift the net debt-to-GDP ratio above 53%, the highest in Canada by a wide margin.

Provincial Economic Summary

	BC	AB	SK	MB	ON	QC	NB	NS	PE	NL	Canada
Real GDP Growth (chain-weighted : year/year change)											
2020	-4.6	-6.5	-4.5	-5.2	-5.6	-5.7	-3.0	-3.4	-2.5	-6.8	-5.4
2021	5.7	5.1	4.4	4.6	5.0	4.8	3.6	3.8	3.7	4.3	5.0
2022	4.7	4.2	3.2	4.2	4.8	4.7	2.5	3.0	2.8	2.0	4.5
Employment Growth (year/year % change)											
2020	-6.5	-6.5	-4.6	-3.7	-4.7	-4.8	-2.6	-4.7	-3.2	-5.9	-5.1
2021	5.6	4.2	1.6	2.2	4.7	4.3	2.9	4.6	1.8	5.8	4.2
2022	2.8	3.8	1.5	1.8	4.4	3.3	1.5	1.4	0.7	0.2	3.5
Unemployment Rate (percent)											
2020	9.0	11.6	8.4	8.1	9.6	8.9	10.1	9.8	10.7	14.2	9.6
2021	6.8	9.3	7.3	7.5	8.5	7.0	9.4	7.8	9.9	12.2	8.0
2022	5.8	7.5	7.0	6.7	6.5	5.9	8.7	7.2	9.5	12.0	6.5
Housing Starts (thousands)											
2020	38.0	24.2	3.1	7.3	81.2	54.7	3.7	4.9	1.0	0.8	219
2021	37.0	28.0	2.8	7.5	80.0	55.0	3.5	4.5	1.3	0.7	220
2022	37.0	30.0	3.0	6.7	75.0	50.0	2.9	3.8	1.3	0.6	210
Consumer Prices (year/year % change)											
2020	0.8	1.1	0.2	0.5	0.6	0.8	0.2	0.3	0.0	0.2	0.7
2021	2.0	1.7	1.6	1.7	2.1	2.0	1.5	1.2	1.4	1.2	2.0
2022	2.2	1.8	1.7	1.7	2.2	2.0	1.8	1.7	1.9	1.6	2.1

Shaded bars are BMO Economics forecasts

Andre Salvi,
Senior Vice President and Head, Technology & Innovation Banking Group

Devon Dayton,
Managing Director and Head, Technology & Innovation Banking Group

Technology and Innovation

The COVID-19 pandemic has led to a massive acceleration in the shift to digitization; as a result, the technology and innovation sector has benefited significantly over the past year.

So many participants in the economy have adopted e-commerce platforms at a greater speed; while disruptive, the pandemic has been a catalyst for new digital adoption. Software based tech companies, in particular, have benefited from this. As well, many biotech and life science firms have received more financing as part of the effort to fight the virus.

We were impressed by the speed with which companies in the technology sector adapted to the new normal. The pandemic has acted as an accelerant for companies, such as in education—particularly remote learning—and cybersecurity (given the surge in e-commerce and working from home).

They were also able, in a time of global uncertainty, to pivot and change on delivery and staffing models. They are making particularly good use of new possibilities for the courting of employees—with the work-from-home model, there's a broader geographic pool of candidates available to them.

Within the industry overall, we saw a slight but understandable blip in March and April, in some subsectors, but business models proved to be quite resilient and by summer, many valuations returned to previous levels or even surpassed them. Overall access to capital, both debt and equity, continues to remain very strong, and industry players are bullish about 2021 as a result.

Across the country, we've been watching our technology ecosystems closely—particularly those in Toronto, Waterloo, Montreal and Vancouver, and Canadian businesses, both established and emerging, continue to access global markets.

Lynda Taylor,
Senior Vice President and Head, Agriculture and Agribusiness

Janine Sekulic,
National Director, Agriculture and Agribusiness

Agriculture and Business

2020 will be remembered for many reasons, not the least of which is the strength and resiliency of Canada's agri-food sector. It was not without challenges. At the onset of the pandemic, for the first time in decades and much to their disbelief, Canadians saw empty grocery store shelves and stockpiling of basic non-perishables. Widespread economic shutdowns that sent people home indefinitely meant diverting supplies destined for restaurant and foodservice establishments to retail channels. Supply chains pivoted, changing packaging and product mixes to meet the demands of a market that literally changed overnight.

The market livestock sector was dramatically impacted by COVID-19. Fed cattle and market hog prices declined in April and May with uncertainty around processing capacity as plants closed to deal with coronavirus infections among workers. At the same time, retail meat prices soared on fears of shortages, which fortunately did not materialize. Retail prices moderated through the fall and winter when supply was no longer a concern. Fed cattle prices have recovered somewhat from the lows but remain pressured by big beef supplies in the system. Hog producers continue to struggle with thin to negative

margins. It has been a challenging time but global demand for protein is cause for optimism in these sectors in the longer term.

Grain and oilseed prices were a completely different story. After starting out the year lacklustre, the impacts of the La Nina weather pattern combined with surging demand from importing countries has driven crop prices to values not seen since 2014. The strength in these markets is expected to continue at least into mid-2021. The downside of high grain prices, however, is added pressure on livestock producers' margins due to high feed costs.

Dairy and poultry producers were negatively impacted by supply chain logistics early in the pandemic, but marketing boards were able to adjust quota allocations to accommodate shifts in demand for certain types of products. There continue to be challenges, but for the most part right across the country these industries stabilized within weeks of the initial COVID-19 outbreaks and have been relatively steady since.

Weather being ever the story in this industry, the potato crop ranged from best ever on the west side of the country where conditions were good, to disastrous in Atlantic Canada where it was terribly dry. The dry conditions that had gripped the southern Prairies finally relented for the most part. Cool, wet weather that produced excellent forage crops on BC's lower mainland was detrimental to blueberry production. Greenhouse operators across the country enjoyed a strong year, as people eating at home drove strong demand for fresh produce.

Despite the challenges, Canadian agriculture remains a bright spot in what has been a relatively dark global economic outlook overall. Strong global demand for protein, grains and oilseeds is extremely positive. Increasing attention on the opportunities to increase processing capacity and add value to our commodities here at home is leading to strong investment in the sector. While the optimism is cautious, we believe there are many reasons to be excited about agriculture, and we starting out 2021 eager as ever to continue supporting our customers through unprecedented times.

Real Estate Finance

Michael Beg,
Senior Vice President and Head,
Real Estate Finance

Karla McCarthy,
Head, Income Property Finance

The Canadian real estate sector experienced one of its most surprising years ever in 2020. With the COVID-19 pandemic significantly affecting the broader economy, the expectation was for real estate to have major challenges with income property commercial mortgage payment defaults and a housing market correction. Instead, we saw one of the strongest market rebounds in history, a veritable z-shaped recovery where the markets are—by and large—stronger than what was seen pre-COVID.

To be sure, a number of our clients needed assistance to get through the worst of the downturn. We provided relief such as commercial mortgage deferrals, which helped clients manage cash flow and allowed them to be more flexible with their tenants.

As well, relief measures implemented by the government helped to prop up the real estate side, and we expect this to continue until the vaccines roll out. These government support measures have brought tangible results. At the height of the pandemic driven downturn, we offered mortgage deferrals to under a fifth of our commercial mortgage clients. Given that real estate represents a major segment of

the wider economy—around 20 per cent of GDP—the success of the deferral programs, along with the various government supports, cannot be underestimated.

Across the country, we have seen a modest shift away from major cities and centrally located offices. As a result, there have been changes in rents and buying patterns. That said, the commercial real estate market has been particularly strong across the country, and notably in Montreal and Toronto. It's been an average year in the Atlantic region and B.C., but housing market trends in all locations are strengthening in recent months. Alberta had a very weak market during the worst of the pandemic but has solid stable trends and the outlook for the coming year is positive.

In downtown spaces, some corporate landlords are using the opportunity to reconfigure presently high vacancy retail spaces; they remain confident that people will be back in office towers eventually and are taking advantage of the current situation. Some studies have predicted that over 95% of employees will return to office spaces, but the lingering question is the number of days per week which will impact office demand and adjacent retail foot traffic.

As we move into 2021, we expect to see a continuing albeit declining ebb and flow in lockdowns across the country. To the extent lockdowns push out longer than expected, it will put additional pressure on businesses; this inevitably works its way up the chain, with some tenants still struggling to pay rent meaning corporate landlords having trouble paying mortgages. However, the situation has tended to be more stable in recent months in the wake of vaccination news and the vaccine rollout.

Pandemic-related risks remain. A slower rollout of vaccines will affect the entire economy's ability to rebound; the hope is that any slow starts will be corrected once vaccinations are rolled out to the general public. While growth should level off given weaker employment, low rates and anticipated net immigration will bode well for stable housing and commercial real estate markets.

Sanjay Arora,
Managing Director and Regional Vice President, Business Property Finance

Seniors Housing

Seniors housing represents a vital, growing sector in the Canadian economy, with a great deal of potential in the coming years.

Over the next two decades, the 75+ year segment of the Canadian population is expected to grow over 110 per cent, compared to growth of just under 20 per cent for the whole population. As well, Statistics Canada's most recent data has shown that the life expectancy of people aged 65 and over is increasing. With waitlists growing and government-funded construction and investment, the opportunities in the sector are impressive.

We're seeing a significant amount of activity among our clients in the sector. Among the key trends, larger players are choosing to divest smaller properties in secondary markets; at the same time, they are building for scale in larger urban centres. Operators are also leaving existing business lines to move towards either long-term care or retirement.

These trends have led to significant M&A activity over the last five years. While we've seen a dip over the last year given the pandemic, we expect that this trend will resume once the situation returns to something closer to normal.

Of note regarding the pandemic, the sector has fared well overall. Our clients in the space did see lower occupancy levels resulting from lockdowns and deferrals of residents moving in. But they continued to pay their loans and we supported them, where they requested additional covenant relief. COVID-19 has understandably increased the cost structure of the sector in the near term. We've noted that the larger, well capitalized firms have been better able to manage that cost pressure. That said, we expect costs to normalize and be fully passed along to residents within 24 months.

On the long-term care front, provincial governments have stayed committed to the sector by giving operators full occupancy protection and reimbursement for all cost associated with prevention, containment, screening, and testing from wave one of the pandemic and additional funding to help manage the second wave of COVID-19.

The consensus from operators is an expectation for a reversion to the mean once vaccines roll out. They expect a significant uptick in occupancy, given that there are a number of seniors either holding a room or making inquiries but choosing to wait for vaccination and the ability to have their loved ones visit regularly. For those in a senior's residence, most homes expect their residents to be fully vaccinated by the end of February 2021. Occupancies in the sector have fallen on average by 10-15% in 2020, but we expect this to stabilize later this year and trend higher by the end of the year.

In the short-to-medium term, we are expecting the pandemic's fallout to lead to increased regulation and higher operating costs related to personal protective equipment and labour. We also anticipate an acceleration of the consolidation trend, given the capacity of larger firms to support what will be inherently higher costs associated with construction related to safer designs, technological improvements, and testing for residents and visitors alike. We also expect to see the construction of more gated communities, with more robust on-site amenities. In the long term, the increase in the senior population over the next 10-20 years will result in a corresponding growth in demand (which is needs based) which will continue to provide underpinnings for the sector as a whole.

Hospitality

Stephen Vermette, Managing Director and Regional Vice President, Business Property Finance

Among all the sectors in the Canadian economy, hospitality stands out for the significant challenges caused by the COVID-19 pandemic.

After many years of relatively consistent growth, 2020 delivered record declines in operating performance, financial losses and erosion of value across the industry in virtually all markets. To present one dramatic example: according to Cushman Wakefield, accommodation has seen drops in revenue available per room from 50 to 75 per cent across the top 10 major markets in Canada.

As we look ahead to 2021, continued travel restrictions, travel bans and evolving quarantine requirements will continue to hold back the industry's ability to recover;

depending on the specific subsegment, we expect issues to persist from two to up to four years.

Property sales have suffered as well. Transactions have reached lows not seen since the financial crisis. The majority of transactions have been as a result of converting hotel properties to market rentals, or affordable housing.

With limited transaction activity, Canada's largest players and those with significant liquidity and capital have been best positioned to take advantage. They have started to look at the situation to determine their ability to grow and expand once the pandemic subsides and the economy moves back to something resembling normalcy.

Meanwhile, there will be players in the market who were subject to high leverage before the pandemic hit; they have seen their equity erode or disappear entirely. These firms will clearly struggle to survive a protracted recovery without government liquidity support.

On the positive side, there have been examples of markets which benefited from staycation activities over the summer—in particular, the interior of B.C. and Vancouver Island. In relative terms, limited service properties have recovered better than full service, luxury, urban properties which were more dependent on international/ business travel and conference activity. With travel still limited, we expect these properties to be the slowest to recover.

We do see some optimism among our clients, corresponding to the delivery of vaccines. The hope is that as more people are vaccinated, the sooner that domestic and international travel patterns can start to return to normal. In general, the expectation for improved inter-provincial travel is late 2021. The hope is that pent-up demand will help drive the recovery faster; its strength will hinge on the success of the vaccine rollout.

Paul DeMarchi,
Managing Director,
Transportation Finance

Transportation

The COVID-19 pandemic has brought to the forefront the vital role that freight transportation plays in the success of the Canadian economy. The critical role of the sector in keeping people supplied in the worst days of the crisis will always be remembered.

Unsurprisingly, the industry as a whole has had a fantastic tail wind over the last six months. Freight demand is up, with understandable spikes for consumer goods and foodstuffs. Meanwhile, freight rates have risen as not enough trucks are available to move product—a problem exacerbated by COVID-19 with a reduction in drivers.

With more goods to be moved combined with some capacity constraints, the economics for trucking companies have all trended very positive; carriers are well positioned, and our clients in the space are feeling very bullish for the upcoming year. Trucking tends to be on the front end of recoveries or downturns, so this outlook is encouraging.

It's also important to note that a number of our client firms have fleets that cross the Canada/U.S. border. The business is robust stateside, and with the certainty that a new trade agreement brings, that is good news for companies here.

But we need to keep in mind the unknowns of operating in the latest stage of the pandemic; the vaccine will no doubt alter the business with changes to demand and driver capacity. Insurance will also continue to be a difficult variable for profitability; we expect to see a persistent escalation in insurance costs over the next couple of years.

Meanwhile, we're also seeing the likelihood of more consolidation; medium-sized firms are likely to be acquired, leading to larger, more robust and stable operators going forward.

Another factor benefiting larger firms is a major regulatory change coming in the summer of this year on how drivers log their hours. Traditionally, this has been done manually; going forward, this process will move to electronic devices. The bigger firms are already doing this, which provides them with an inherent advantage.

But in the end, all the fundamentals are there for a decent runway as the economy stabilizes and re-opens. The transportation industry is well-positioned, and we look forward to a solid year ahead.

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