Ontario Construction Secretariat

EYE ON ICI NEWSLETTER

OCTOBER 2014

The 2014 OCS Annual General Meeting at the Westin Ottawa Hotel, Ottawa, Ontario

EVENT RECAP: OCS 2014 ANNUAL GENERAL MEETING

On September 29th – 30th the OCS hosted its 22nd Annual General Meeting (AGM) in Ottawa, Ontario. As always, the event provided an opportunity for industry stakeholders to come together and hear updates on the activities of the OCS.

A networking reception kicked things off on day one giving OCS stakeholders the opportunity to meet with Ontario MPs and MPPs. Peter Braid, MP and Parliamentary Secretary for Infrastructure and Communities, spoke about the New Building Canada Plan, the federal government's 10-year, $53 billion infrastructure plan, of which $11 billion will flow to Ontario. Ottawa MPP and former Minister of Labour Yasir Naqvi spoke about the important role of collaboration between the industry and government in executing value-added construction projects. Finally, MPP and Attorney-General Madeline Meilleur shared steps that the government is taking to address the underground economy in construction.

(L to R) OCS Chief Executive Officer Sean Strickland, MPP Yasir Naqvi (center), and MP Peter Braid

On day two, Chief Executive Officer, Sean Strickland, provided delegates with an overview of key OCS achievements from the past year. He also spoke about the new OCS Strategic Plan and the proposed 2015 work plan and budget. OCS will continue to undertake value-added research and focus on strategic objectives related to 'Enhancing Labour Relations', 'Positive Perceptions of Unionized Construction' and 'Progressive Public Policy'. Delegates heard presentations on key OCS research projects including findings from our union/non-union safety study with the Institute for Work and Health, an analysis of market performance and insight from an Ipsos Reid survey of public perceptions of Ontario's construction industry. We were also pleased to hear from Ottawa Public Health as they shared information about their Construction Industry Smoking Cessation Program.

Continued on Page 2

INSIDE THIS ISSUE

Continued from Page 1

OCS AGM 2014 ANNUAL GENERAL MEETING SEPTEMBER 29-30, 2014 RECAP

OCS CEO Sean Strickland addresses delegates

OCS CEO Sean Strickland and MPP and Attorney-General Madeline Meilleur

Attendees at the 2014 AGM networking reception

MP Peter Braid

A presentation by Ottawa Public Health on their Construction Industry Smoking Cessation Program

"Investing in infrastructure is truly an investment in our future, and the OCS is an important part of this future. As you know, the Government of Canada recently launched the New Building Canada Plan, the largest and longest federal infrastructure plan in Canadian history. Through this plan, we are delivering $53-billion over the next decade for provincial and municipal infrastructure."

~ Peter Braid, MP & Parliamentary Secretary for Infrastructure & Communities

OCS President Joe Keyes addresses EBAs and OCS Board of Directors at the 2014 OCS Annual General Meeting in Ottawa, Ontario

CURRENT ANALYSIS AND NEAR TERM OUTLOOK:
TRENDS IN INVESTMENT AND BUILDING PERMITS

Total ICI Investment

Seasonally adjusted, constant dollar ICI investment advanced 1.7% (q/q) to $4.1 billion in the second quarter of 2014, building on the modest gain made in the first quarter. The first and second quarter increases in investment were driven entirely by the commercial market. Despite back-to-back quarterly advances, the level of investment in the first half of 2014 was slightly lower than in 2013 averages (see **Figure 1**). For context, the $8.2 billion investment achieve in the first half of 2014 is between its 3 and 5 year average.

Industrial Market

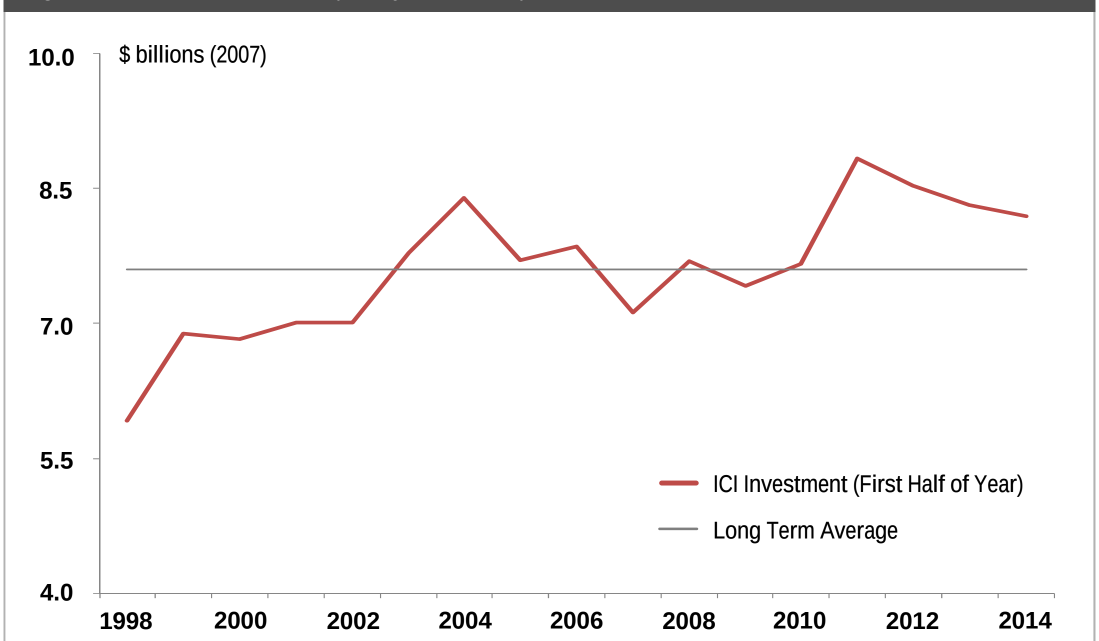
Current Trends

In our July issue of *Eye on ICI*, we noted that the first quarter decline in industrial investment may have been attributed to extreme weather conditions. However, second quarter data does not support that hypothesis as we did not witness a 'bounce-back' in industrial investment with the arrival of nicer weather. Industrial investment dropped 1.3% (q/q) in the second quarter to $488 million, leaving it 6% below its year-ago level. Year-to-date industrial investment for the first half of 2014 came in at $980 million, above both its 3 and 5 year averages, yet 5% below what was achieved in 2013.

On a quarter-over-quarter basis, only four Census Metropolitan Areas (CMAs) managed to post gains, with growth led by Kitchener-Waterloo-Cambridge (KWC). However, investment in KWC was a miniscule $15 million in the second quarter. There were similar stories in both London and Ottawa, where investment increased on a quarter-over-quarter basis, though the actual level of investment was fairly low level. Only the Toronto CMA managed a fairly healthy investment level in the second quarter. On the flip side, the largest negative contributions to quarterly growth belonged to Brantford, Guelph and Hamilton.

Continued on Page 4

Figure 1: *Total ICI Investment: January through June of each year*



Source: Statistics Canada, OCS calculations

"Despite back-to-back quarterly advances, the level of investment in the first half of 2014 was slightly lower than in 2013 averages"

Continued from Page 3

When comparing the first half of 2014 to the same period in 2013, only 6 out of 15 CMAs reported increased industrial investment. There was solid growth in Toronto and very strong growth in both Windsor and Kingston. Meanwhile, the largest negative contributors to the drop in first half investment were KWC (thanks to a rock bottom first quarter) and Oshawa (unwinding from 2 solid years).

Outlook

Building permit data – which is a leading indicator of investment – is pointing to lower investment over the next few quarters as intentions dipped 7% over the first half of 2014 (compared to the same period in 2013). However, conditions are favourable for a pickup in investment over the medium term with a strengthening U.S. economy, increasing manufacturing capacity utilization indicating more strain on current resources, and big transit and energy projects on the books. Indeed, merchandise exports, which correlate strongly with industrial investment, jumped 6% in the second quarter.

Commercial Market

Current Trends

In the second quarter, commercial investment advanced a sturdy 3.9% (q/q) to $2.6 billion and was 8% higher than its year-ago level. Over the first half the year, commercial investment totalled $5.1 billion – a new record.

The Ottawa CMA was the largest contributor to the strength in the commercial market in the first half of the year, as the region enjoyed $400 million worth of investment in the second quarter, lifted by the Landsdowne Live development. As has been the story for some time, Toronto was also a very large contributor for well documented reasons including an office market boom. Meanwhile, St. Catharines-Niagara had its healthiest first half for commercial investment since 2003.

On the flip side, first half declines were registered in 8 out of 15 CMAs, with the largest declines belonging to London, Windsor, Brantford and Kingston. Investment values were lower in Hamilton and KWC as well.

Outlook

The commercial market will likely continue to fire on all cylinders over the near term, with commercial building intentions jumping 20% over January-June (versus the same period in 2013). While permits are signalling continued near-term strength, there are some tentative signs that the market may run out of juice, at least over the medium term. In Toronto, the epicentre of commercial investment boom, office vacancy rates have been trending higher and commercial permits as a share of GDP are at their highest level since 1989 (though nowhere near those bubble levels). All of this is to say that what goes up, must come down, eventually.

Institutional Market

Current Trends

Institutional investment dropped 2% over April-June versus the first quarter, marking the 10th straight quarterly decline – an unprecedented run. At a little over $1.0 billion, the level of investment was 15% lower than its year-ago level. Over Jan-June, institutional investment was valued at $2.1 billion – a level that would be considered normal 13 years ago but is probably unsustainable for 2014.

Only 6 out of 15 CMAs managed an increase in the first half of the year versus the same period in 2013. The one standout CMA is Kingston, which saw a 250% increase over 2013 thanks to a record second quarter fuelled by the Providence Care Hospital project. Meanwhile, the biggest first half decliners included Ottawa, London, Windsor and Toronto.

Outlook

Building permits are very strong predictors of upcoming investment and fortunately they increased 8% in the first half of 2014. It appears that the stars may be aligning for an upturn in institutional investment in the near future.

Continued on Page 5

Continued from Page 4

An important reason for this tentative optimism stems from the fact that the level of investment is currently so low. As mentioned, current investment levels are plumbing depths not seen since 2001, when Ontario's population was 12% lower than it is now. As such, further significant deterioration would be inconsistent with fundamentals. Additionally, even though we are in an environment of fiscal austerity, the recently passed provincial budget actually had *increases* in spending for institutional structures earmarked for this fiscal year. Put it all together and the retrenchment in institutional investment may end sooner rather than later.

Bottom Line

Total ICI investment increased for the 2nd straight quarter over April-June, though the entire increase was accounted for by the commercial market which continues to be strong thanks to Ottawa and Toronto. Industrial investment has trended lower so far in 2014 though remains at a respectable level. Going forward, a strengthening U.S. economy, increasing manufacturing capacity utilization and big transit and energy projects may limit the downside to industrial investment. Meanwhile, institutional investment continues to drag though increasing permits hints that its decline may finally be petering out.

Table 1: *Ontario ICI Building Investment, Second Quarter Summary Table*

Sector	April-June Value	versus first quarter of 2014	versus second quarter of 2013	first half of 2014 versus first half of 2013	Comments
Industrial	$488 million	1.3% lower	5% lower	4.5% lower	Q2 level still decent
Commercial	$2.6 billion	3.9% higher	8% higher	6% higher	Strong Q2 growth
Institutional	$1.0 billion	2.0% lower	15% lower	16% lower	10 straight quarters of decline
Total ICI	$4.1 billion	1.7% higher	flat	1.6% lower	Decent first half level

ONTARIO REGIONAL PERMITS UPDATE

NORTHERN ONTARIO

A solid second quarter propelled first half **industrial** permit values 26% higher than their Jan-June 2013 level. Northeastern Ontario (which counts Sudbury as its largest city) comprised 93% of permit issuance in the first half of 2014. Some of the largest industrial projects currently underway in the north include the Vale AER plant and the Lower Mattagami Hydroelectric Dam, though neither would be picked up fully by the permit data.

$87 million worth of **commercial** permits were issued over Jan-June 2014, slightly lower than in 2013 though still a respectable level. Smaller commercial alterations and renovations accounted for a large chunk of commercial work. Over the long-term, average growth in commercial permit values has been strong in Northern Ontario.

Modest second quarter permit issuance, particularly in Northwestern Ontario, sent the value of **institutional** permits lower in the first half of 2014 (compared to the same period in 2013). In fact, first half issuance was at its lowest level since 2009, despite notable permit activity by Laurentian University in Sudbury.

Permit Values - January to June - 2014

Sector	Value (in 000s)	% Change
Industrial	$50,277	▲ 18.0%
Commercial	$87,182	▼ -13.8%
Institutional	$86,771	▼ -30.8%
Total ICI	$224,230	▼ -16.7%

Source: StatsCan

EASTERN ONTARIO

A mere $48 million worth of **industrial** permits were issued over the first half of 2014, the lowest amount since 2008. Permit values fell in Kingston-Pembroke and were sharply lower in Ottawa. Amongst the largest industrial projects in Eastern Ontario includes the Ottawa Confederation Line. Industry stakeholders are also gearing up for work on the upcoming Napanee Generating Station.

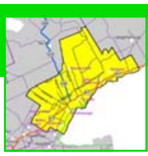
A solid $443 million worth of **commercial** permits were issued in the first half of 2014, with gains observed in both Ottawa and Kingston-Pembroke, with the latter lifted by a large retail addition. The Ottawa commercial market continues to go strong, with the Landsdowne Live project providing a boost to the region.

A record $461 million worth of **institutional** permits were issued in Eastern Ontario in the first half of the year. Just over half of the value of building intentions was accounted for by the Providence Care Hospital in Kingston. Construction on the new hospital began in May of this year. Issuance was also strong in Ottawa in the first half of the year.

Permit Values - January to June - 2014

Sector	Value (in 000s)	% Change
Industrial	$48,937	▼ -56.5%
Commercial	$443,153	▲ 36.0%
Institutional	$461,312	▲ 188.4%
Total ICI	$953,402	▲ 59.4%

Source: StatsCan



GTA ONTARIO

A paltry $295 million worth of **industrial** permits were issued in the Greater Toronto Area during the first half of 2014. Other industrial market indicators paint a healthier picture with industrial investment up 18% year-over-year in the second quarter and the availability rate in the GTA very low (meaning that there is continued incentive to build). With transit sector work and massive power sector projects on the horizon, one can't be too bearish on the industrial market.

The GTA's **commercial** sector just keeps powering along, with nearly $2 billion worth of permits issued over Jan-June 2014, far and away a new record level. Commercial construction has been strongly upward trending since the end of the recession, powered by an office building cycle in the downtown core.

Institutional permits were a modest $370 million in the first half of 2014, extending the downward trend and pointing to subdued institutional construction going forward. Though projects like the Humber River Regional Hospital and the new Oakville Hospital are winding down, new large-scale hospital projects in Vaughan, Milton and downtown Toronto promise to take up some of the slack.

Permit Values - January to June - 2014

Sector	Value (in 000s)	% Change
Industrial	$295,075	▼ -19.8%
Commercial	$1,962,134	▲ 43.4%
Institutional	$370,732	▼ -37.4%
Total ICI	$2,627,941	▲ 12.9%

Source: StatsCan

CENTRAL ONTARIO

Permit Values - January to June - 2014

Sector	Value (in 000s)	% Change
Industrial	$283,614	▲ 11.8%
Commercial	$450,000	▼ -24.0%
Institutional	$402,348	▲ 8.5%
Total ICI	$1,135,962	▼ -6.6%

Source: StatsCan

A strong second quarter powered **industrial** permits higher in the first half of 2014. Kitchener-Waterloo-Barrie (KWB) made the largest contribution to growth, a positive sign after back-to-back years of extremely depressed permit values. Issuance was also strong in Muskoka-Kawarthas. Building intentions took at step back in Hamilton-Niagara from very strong levels in 2012 and 2013.

A slow second quarter for **commercial** permit issuance dropped its first half value to a relatively modest $450 million. The primary culprit was the Hamilton-Niagara region which is unwinding from a record 2014, despite permitting for Tim Hortons Field. Permit values were also lower in KWB while Muskoka-Kawarthas saw a modest increase.

A massive second quarter propelled **institutional** permit values higher over the first half of the year. KWB was by far the largest contributor to the increase in building intentions, thanks to a permit issued for the new Cambridge Memorial Hospital, on which construction started in September. Permits were higher in Muskoka-Kawarthas as well. Conversely, building intentions dropped significantly in Hamilton-Niagara despite a relatively large permit issued for work at McMaster University in Hamilton.

SOUTHWESTERN ONTARIO

Permit Values - January to June - 2014

Sector	Value (in 000s)	% Change
Industrial	$249,432	▲ 11.2%
Commercial	$188,437	▼ -11.3%
Institutional	$144,453	▲ 28.7%
Total ICI	$582,322	▲ 6.1%

Source: StatsCan

Industrial permit values advanced 12% in the first half of 2014 (compared to the same period in 2013). The increase was completely accounted for by Stratford-Bruce where intentions were valued at over $100 million, pointing to solid construction going forward. In contrast, permit values were lower in Windsor-Sarnia and particularly London, where building intentions are unwinding from a huge 2013. Longer-term prospects are perhaps better for the region with a sharply improving U.S. economy.

Falling **commercial** building intentions in London sent values for the region lower over the first half of the year. Conversely, permit values were higher (though still not very high) in Windsor-Sarnia, driven by a slew of smaller commercial projects in Windsor. Permits reached their highest level since 2010 in Stratford-Bruce and, in fact, this sub-region has had the highest long-term average growth of the three.

Over the first half of the year, **institutional** building intentions were valued at a very low $144 million, signalling modest institutional construction going forward. However, they were still higher than their miniscule 2013 level. The primary driver of growth was London, though permits were also higher in Windsor-Sarnia. Meanwhile, permits dropped but were at a reasonable level in Stratford-Bruce.

TOP CONSTRUCTION PROJECTS STARTED - APRIL TO JUNE 2014

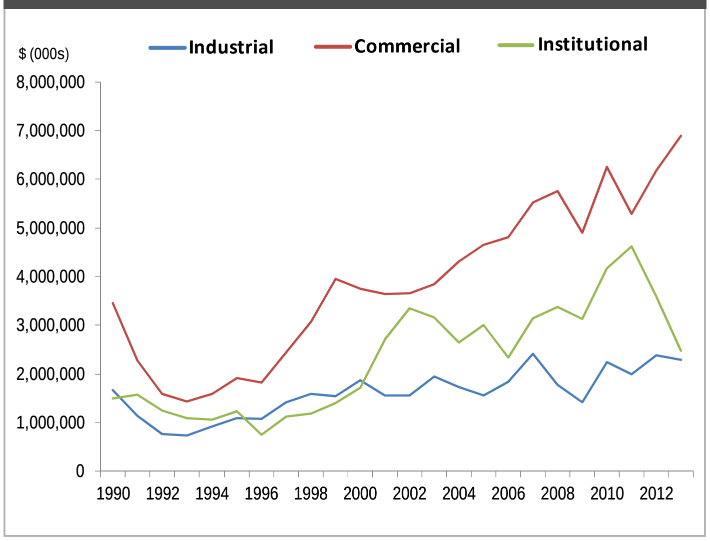
PROJECT	CITY	VALUE
Hanlan Feedermain, Contract 3, North Section	Mississauga	$234M
Bio-based Production Plant	Sarnia	$180M
Viva Bus Operators, Phase One	Richmond Hill	$105M
Mid Halton Waste Water Treatment Plant	Oakville	$101M
Holland River Bridge and 2nd Concession	East Gwillimbury	$93M
Duffin Creek Water Pollution Control Plant, Stages 1 & 2	Pickering	$76M
Mississauga Bus Rapid Transit, Segment 3	Mississauga	$63M
Hyatt Andraz Hotel	Ottawa	$55M
QEW, Burlington Bay Skyway Northbound Lane	Burlington	$44M

Source: Reed Construction Data, Industrial Info Resources

THE SHIFTING INDUSTRIAL LANDSCAPE

It's no secret to construction stakeholders that the province's industrial construction market has been in a funk. Indeed, permits for industrial construction have shown the least growth of all three ICI markets. Nominal (i.e. not adjusted for inflation) permits were only 38% higher in 2013 than their level in 1990. This substandard growth pales in comparison to both the commercial sector and the institutional market, even with the latter's deep retrenchment in the past few years.

Figure 1: *Industrial Permits Lag both Commercial and Institutional Permit Issuance*



Source: Statistics Canada

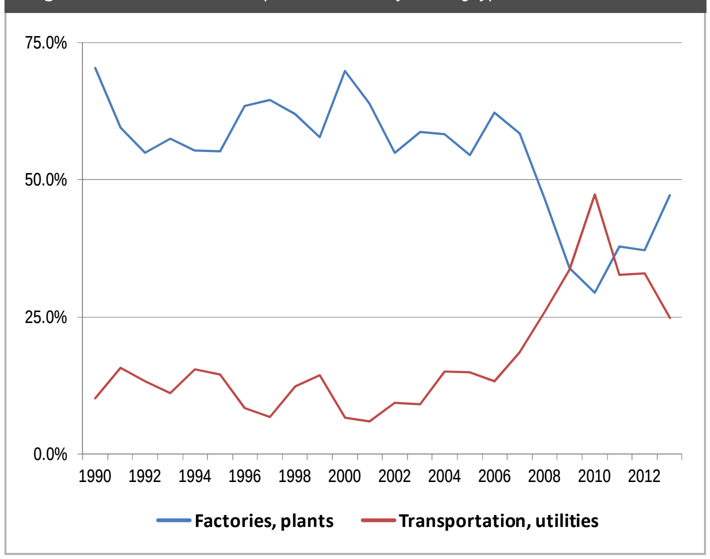
Probably the biggest reason for the lacklustre performance of the province's industrial building market has been the struggles of its manufacturing sector. In the mid 1970s, nearly 1 in 4 jobs were in manufacturing. Today, that figure is 1 in 10. The deterioration of manufacturing has caused changes in the type of industrial structures that have been built. In this article, we'll use building permit data to get a sense of how the industrial landscape has been modified. Of course, not all work that is commonly considered industrial is permitted for. Nevertheless, examining the building permit data can help illuminate some interesting trends.

Trends in Industrial Building Types

Statistics Canada tracks building permit information for a variety of industrial building types. The main categories are factories and plants, mining and agricultural buildings, transportation and utilities buildings, and minor new construction and improvements. Historically, factories and plants have accounted for the largest share of permits, representing 55% percent of the market from 1990-2013.

However, when we look across time, a very revealing trend emerges. In the 1980s, factories accounted for three-quarters of industrial permits issued. Fast forward to 2010 and that figure collapsed to 30%. Challenges in Ontario's manufacturing sector have led to a reduced demand for the construction of new facilities. In fact, building intentions for factory building intentions were 8% *lower* in 2013 than they were in 1990 (and this is not accounting for the value-boosting effects of inflation).

Figure 2: *Share of industrial permits issued, by building type*



Source: Statistics Canada, OCS Calculations

At the same time, other industrial sector building types have picked up the slack. The most prominent of which has been construction of transportation and utilities buildings. Since 2006, building intentions for transportation and utilities buildings have increased dramatically and on average represented approximately one-third of the market. Over the long-term, growth in building intentions for transportation and utilities buildings has out-paced growth in factories. **As illustrated in Figure 1, there has been a shift in the type of industrial structures being built in Ontario over the past decade. The construction of factories and plants dropped dramatically while transportation and utilities buildings saw a surge in growth.**

It is premature to assess whether this is a structural shift or merely a temporary blip. The construction of transportation and utilities buildings is not highly related to movements in the overall economy. This provides an obvious advantage as realized during the latest recession when building intentions for factories tumbled 66% while permits for transportation and utilities buildings advanced 5%. Over the past few years, government funding of transportation and utilities infrastructure has played a significant role in creating construction opportunities for new bus terminals, transit, railway stations, sewage treatment plants and water filtration facilities. Construction of these structures is dependent on government spending plans, which don't necessarily vary in tandem with economic growth and are probably less sensitive to foreign competition, especially relative to manufacturers.

Crystal Ball Gazing

A high Canadian dollar combined with intense competition from low cost producers means that manufacturers in the province will continue to be challenged for the foreseeable future. This suggests dollars flowing to factories and plants in the form of new investment could be relatively subdued, at least when compared to historical standards. Luckily, with big transportation projects planned for the province, like the next round of Metrolinx's *Big Move* initiative, and the continued need to invest in water/wastewater facilities, the transportation and utilities sector could continue to take up the slack.

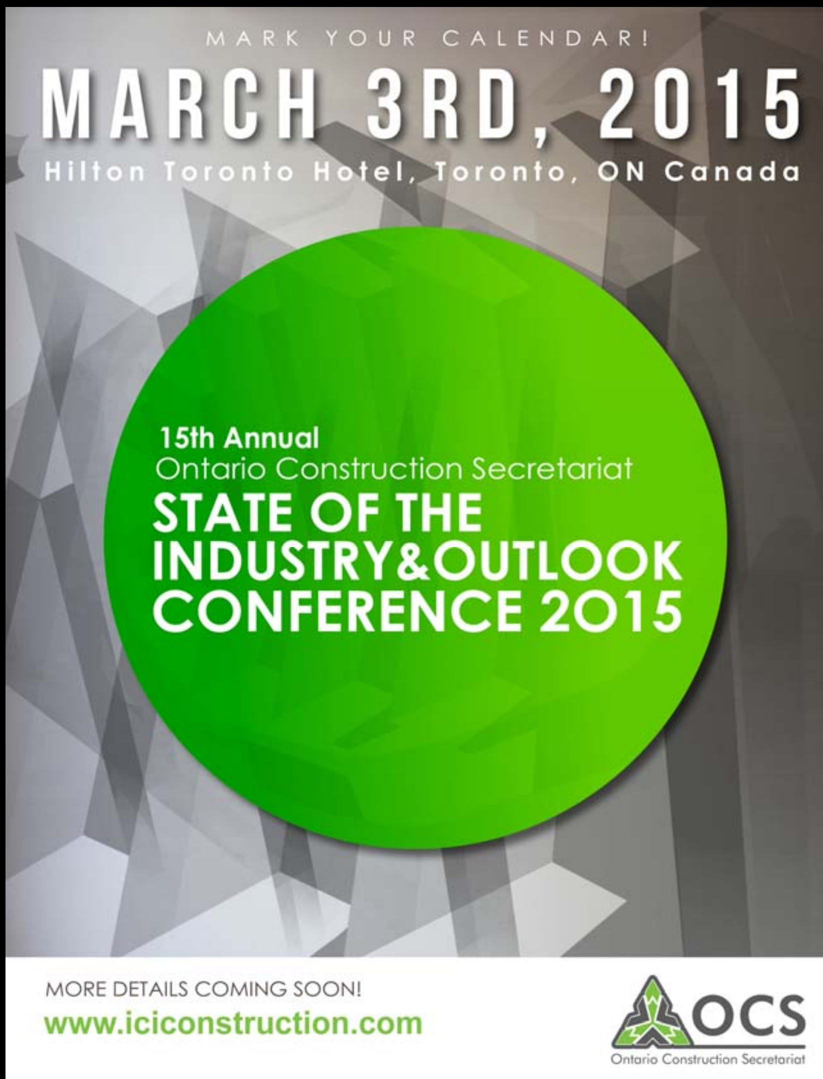
Concluding Remarks

Construction of industrial buildings has been relatively subdued over the past number of years. This is primarily due to the challenges faced by the provinces' manufacturing sector. Those challenges have led to a declining share of building investment in factories and plants within the industrial market. Thankfully, projects in the transportation and utilities sector – which are less dependent on economic growth and are less sensitive to foreign competition – have taken up the slack. Going forward, it seems reasonable to think that this trend will continue, given on-going challenges faced by manufacturers, a government committed to flowing dollars into transportation, and the need to continue to invest in infrastructure, like water/wastewater facilities.

UPCOMING EVENTS

FOR MORE INFORMATION AND OTHER UPCOMING CONFERENCES & INDUSTY EVENTS: **www.iciconstruction.com**

MARK THESE IMPORTANT DATES IN YOUR CALENDAR FOR 2014 - 2015



FOR INFORMATION ON THIS EVENT OR OTHERS:
Email: info@iciconstruction.com
www.iciconstruction.com

2014/2015 OCS EVENT CALENDAR

NOV 13-14 2014 LABOUR RELATIONS SYMPOSIUM
Sheraton Toronto Airport Hotel
Toronto, Ontario

MAR 3 2015 STATE OF THE INDUSTRY & OUTLOOK CONFERENCE
Hilton Toronto Hotel
Toronto, Ontario

FOR MORE INFO ON THESE EVENTS EMAIL US AT: INFO@ICICONSTRUCTION.COM

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