

Study
December 2020

Manufacturing industry outlook

How changes in the economy are affecting
Canada's manufacturing sector



Industry at a glance

90,850
businesses, including 93%
with 100 employees or less



1.7 million people
employed

11.2%
of Canada's economy



68% of Canadian
merchandise
exports

Why it matters

The manufacturing sector is a pillar of the Canadian economy and a major contributor to the country's trade performance, with 68% of goods exports tied to the sector. From food and medicine to fabricated metal and cars, it would be hard to find a Canadian business that's not connected to the sector.

Companies that embrace advanced manufacturing technology, including automation and 3D printing, will be better positioned to be competitive in the years ahead. Supply chain disruptions, shortages and slow growth in manufacturing have a trickle-down effect on all Canadians.

Report highlights

Canada's manufacturing sector is diverse, representing 21 industry groups. Some sub-sectors have been hit harder by the COVID-19 pandemic than others. Recovery will be uneven. Overall, manufacturing is not expected to return to pre-crisis levels until mid-2022.

9.3%

decline expected in Canadian manufacturing output in 2020, almost twice the expected 5.7% decline of the overall economy.



Exports of manufactured goods took a hit due to global and North American supply chain disruptions.



Labour productivity is down, due to lockdowns, social distancing and enhanced protocols for cleaning within facilities.



Pharmaceuticals and food manufacturing are leading the sector's recovery, with a spike in consumer demand domestically and internationally.



Aerospace manufacturing will take the longest to recover due to a slow rebound in global air travel.

The U.S.: A key trading partner

Canada's manufacturing sector is highly dependent on exports, especially to the United States. Economic performance in the U.S. is a key driver of the sector.

68%

of Canada's merchandise exports in 2019 were tied to the manufacturing sector, representing \$354 billion.

More than

80%

of merchandise exports are shipped to the U.S.



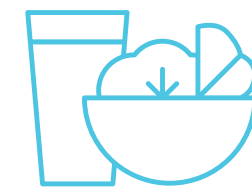
Top five manufacturing sub-sectors

Canadian manufacturers are diverse, encompassing everything from craft beer and textiles to chemicals and airplane components. Sub-sectors have been affected differently by the economic downturn, and recovery will be similarly varied. The following five sub-sectors represent 55% of total manufacturing output in 2019.



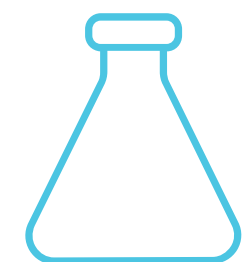
Transportation equipment manufacturing

Autos will get a short-term boost from order backlogs to the end of 2020. Aerospace will be constrained by sluggish global air travel until 2024.



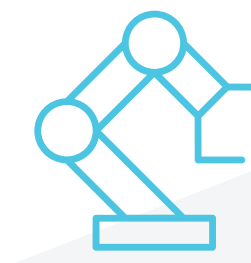
Food manufacturing

A surge in consumer demand, followed by a longer-term push for national self-sufficiency and domestic production, will spur a fast recovery.



Chemical manufacturing

Diverse sales and international trade will support recovery. Pharmaceuticals experienced heightened demand throughout the pandemic, which is expected to continue.



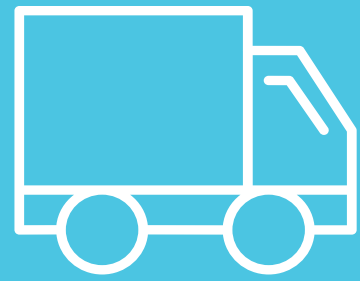
Machinery manufacturing

Firms have postponed some capital investments, triggering a decline in machinery purchases. As companies slowly reinvest, there will be a gradual return to pre-crisis levels by 2022.



Fabricated metal product manufacturing

A strong non-residential construction industry, steady increases in steel prices and favourable export conditions put the industry in a competitive position.



Transportation equipment manufacturing

Planes, trains and automobiles, along with recreational vehicles, boats and farm vehicles, are included in this sector. Auto and aerospace manufacturing are its two largest industries.

Auto manufacturing

Canada's auto industry was in decline when the pandemic shutdown hit. The termination of car models and the continued relocation of production outside of Canada have hurt the industry.

74.6%

decline in new car sales in April, 2020 over the same month in 2019.

28%

decline anticipated for the industry overall in 2020.

Closure of factories and physical distancing requirements have triggered a production lag.

A two-phase recovery

①

A rapid, short-term rebound

- **Order backlogs and pent-up demand** due to purchases put on hold during the lockdown will give the auto industry a bump in the second half of 2020.
- **Historically low lending rates and aversion to public transit** are expected to continue into 2021, giving new car sales a boost.
- **By mid-2022**, the initial rebound will lift production close to pre-pandemic levels.

②

Slower growth starting in mid-2022

- **Scheduled production cuts and relocation of auto production outside of Canada** will continue to limit growth.
- **Replacement parts market will grow** as new vehicle sales plateau and the fleet ages.
- **Fall 2023**—Full recovery to pre-COVID levels expected.

Aerospace manufacturing

The aerospace industry has been hit hard by the pandemic. Fear of virus exposure, border closures, restrictions on international travel and uncertainty about travel regulations have brought demand from airlines to a near halt.

18.4%

contraction of the industry in the first six months of 2020.

8.4%

decline expected for 2020 overall.

65%

drop in Canadian demand for air travel expected in 2020, which in turn will slow capital investments by airlines.

A slow recovery to 2024 for aerospace

Passenger air traffic

isn't expected to return to pre-pandemic levels until 2026. Travel regulations and weak traveller sentiment will constrain demand for new aircraft.

Economic growth

Growth in both developed and emerging markets is expected to drive global trade and consumer spending, which will encourage people return to air travel.

1.1% growth forecast for aerospace manufacturing in 2021 and 5.4% in 2022.

Fuel prices

Recovering fuel prices and aging aircraft fleets will boost demand for new, fuel-efficient planes in the long run.





Food manufacturing

Food producers are expected to fare better than most industries in the sector. Distribution disruptions, labour shortages, reduced demand from restaurants and new social distancing measures all hindered the industry in the early spring of 2020. At the same time, consumer demand shifted to grocery purchases and eat-at-home products. Overall, the industry declined 5.2% to mid-2020 but had already recovered to pre-pandemic levels by the fall of 2020.

Consumers shift to eat-at-home products

Low demand from restaurants and the hospitality sector continues as operator capacity is hindered by social distancing measures, the absence of large events and reduced tourism. Consumers will continue to spend more in supermarkets in the near-term, which will support demand for food manufacturers.

78.9%

spike in grocery spending in March, 2020 over the previous year triggered a shift in focus for the industry.

Healthier foods

A shift to healthier foods and organic products—Canada's food processors can remain competitive by quickly adapting to consumer preferences.

18%

higher grocery spending in October, 2020 over the same month in 2019.



Chemical manufacturing

Chemicals are used in the production of a variety of industrial and consumer products. Chemical manufacturers benefit from diverse sales and broad involvement in international markets. Highly advanced processing and reliance on machines have helped to buffer the industry from the costs of pandemic-related social distancing and cleaning requirements. Different parts of the industry are expected to rebound at varying paces, depending on the markets they serve.

Base chemicals manufacturing industry

Performance in other sectors will determine how quickly this sub-industry rebounds.

14.5%

decline is forecast for the industry overall in 2020.

2023

chemical manufacturing is expected to return to pre-crisis levels.

Transportation sector

Demand from the transportation sector, including automakers is expected to be slow, dampening the need for chemical inputs.

A boost from construction

Non-residential construction activity is expected to give base chemicals a boost, although slower performance in residential markets will slightly temper demand.

Pharmaceuticals industry

19.1%

growth in industry output in the five years ending in 2020.

Disruptions

Global supply chain disruptions during the pandemic have been a challenge for Canadian drug companies, especially imports of raw materials from China and India. This has triggered supply bottlenecks as companies scramble to find alternative suppliers and distributors.

Growing demand

10.4 million Canadians will be over 65 by 2036, representing a quarter of the population. This age group requires more medical care and pharmaceuticals.

A resilient sector

Robust demand for drugs has persisted through the crisis.

5% growth forecast for 2020.

2.8% average annual growth for the following five years.

Better access

Easier access to prescription drugs and accelerated research is anticipated with the adoption of new technologies like telemedicine, virtual clinical trials and artificial intelligence.



Machinery manufacturing

Machinery manufacturers are heavily dependent on the performance of the Canadian and global economies. Capital investments in new equipment and machinery have taken a hit during the pandemic, with the current global slowdown in manufacturing. It's expected new purchases of machinery will be delayed as firms try to reduce debt. Overall, this sub-sector is expected to recover more slowly than the broader manufacturing sector.

13.6%

contraction in output is forecast for the machinery manufacturing sub-sector in 2020.

34.6%

fewer small and medium-sized Canadian businesses indicated they would make capital investments in machinery and equipment in April, 2020, compared with the same month in 2019. This is a result of the uncertainty due to the pandemic.

Productivity

Firms are looking to enhance productivity through automation. Labour productivity has declined this year as companies cope with social distancing protocols associated with the pandemic. This is an opportunity to encourage companies to invest.

47%

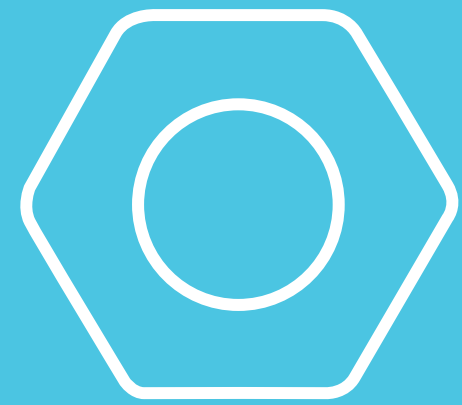
of small and medium-sized Canadian businesses intend to purchase new machinery and equipment in the following 12-month period.

21%

of companies are expected to invest more in machinery than in the past.

2022

A return to pre-crisis levels is expected for this sub-sector by the beginning of 2022.



Fabricated metal manufacturing

Metal producers are feeling the slowdown in transportation manufacturing and the construction industry. An over-supply of steel from China and a global decline in demand has driven down prices for Canadian fabricated metal, most of which is steel based. On the up side, the low Canadian dollar is a boon for Canadian exports to the United States. New infrastructure investments will encourage domestic demand over the long term.

12.9%

forecasted decline in Canadian fabricated metal output in 2020.

Severe contraction in transportation and construction hampered domestic demand for metal production during the pandemic.

Oversupply of steel and dampened global demand have reduced market prices for Canadian steel products, but prices are expected to stabilize over five years.

Recovery in non-residential construction is expected to boost demand for fabricated metal in 2021.

Infrastructure investment through the federal government's *Investing in Canada Plan* will increase demand.

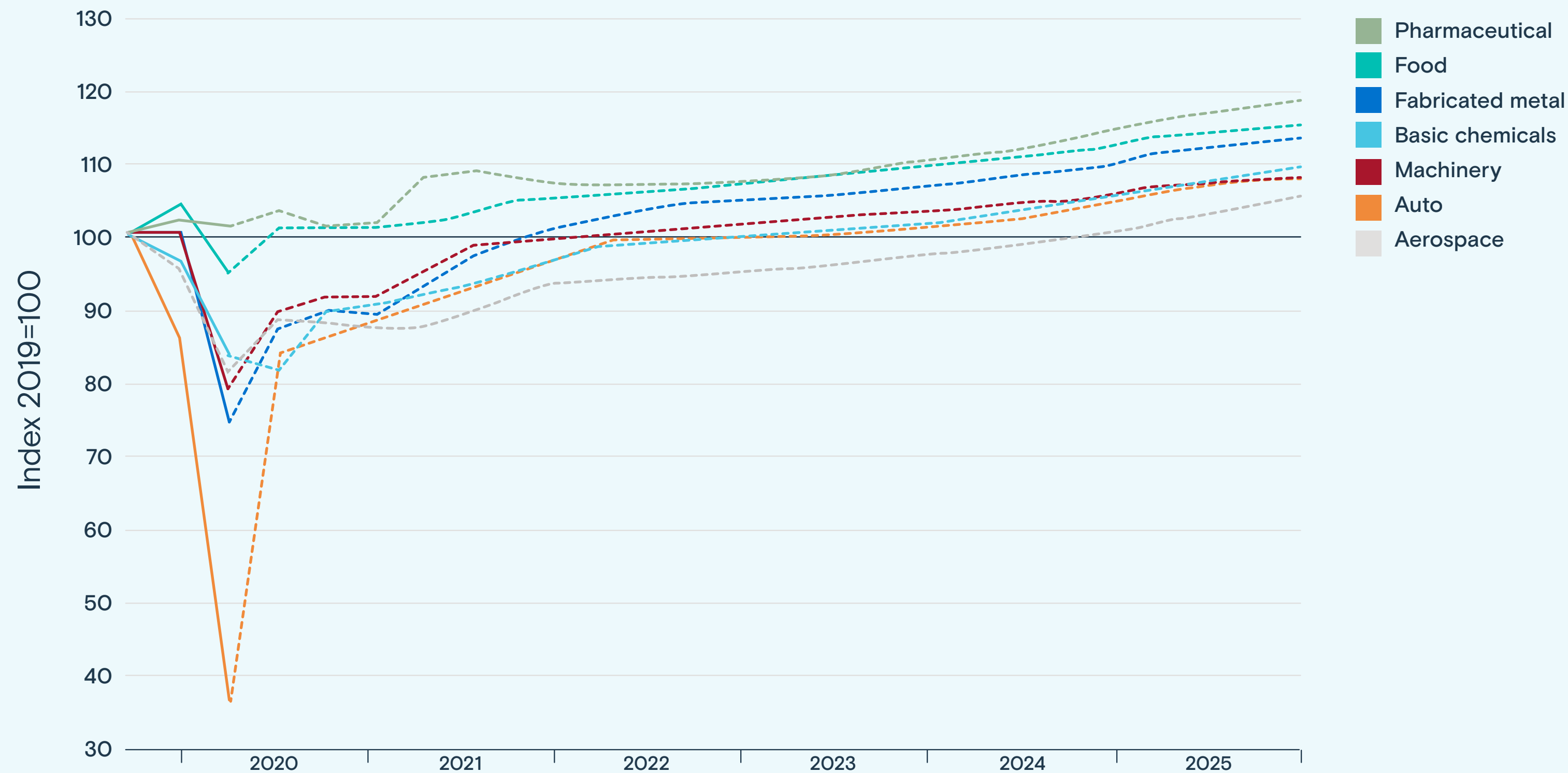
Export growth is a bright spot for metal manufacturers. The U.S. boasts a strong construction sector. Depreciation of the Canadian dollar makes Canadian steel more competitive south of the border.

Fall 2021

The fabricated metal industry is expected to return to pre-crisis levels as steel prices stabilize, exports grow and non-residential construction returns to normal levels.

Manufacturing sub-sectors in Canada

Quarterly, seasonally adjusted at annualized rate, Index 2019=100



Recovery will be uneven

Disruptions in global supply chains will continue to affect Canada's manufacturing sector for a few years. Sub-sectors will feel the impact in varying ways. Aerospace and auto manufacturing will take the longest to recover. Pharmaceuticals and food manufacturing have already bounced back to pre-crisis levels.

How to position your manufacturing business for the recovery



Trends in the manufacturing sector

Embracing new trends could help manufacturers recover from the pandemic recession. Supply chain disruptions, new technologies, customization and rising customer expectations offer both challenges and opportunities.

Supply chain disruptions

Challenge

Supply chain disruptions require organizations to quickly pivot to alternative suppliers, adapt to rapidly changing consumer demands and invest in nimbler logistics.

Opportunity

Reassess your sourcing strategies, supply chain agility and paths to market. Diversify suppliers to adapt quickly to market trends. Consider focusing on local suppliers and markets.

Technology adoption

Challenge

Canadian firms lag global competitors in Industry 4.0 adoption, including robotics, Internet of things, cloud networking, data analytics and artificial intelligence.

Opportunity

Create an integrated, long-term plan to pursue improved technology usage in your business to enhance productivity, quality, decision-making and profitability.

Customization

Challenge

Consumers increasingly want customized goods on demand and expect manufacturers to quickly respond with high quality products.

Opportunity

Collaborate with clients on customized designs. Enlist suppliers in helping you to improve your agility. Digital platforms and 3D printing hubs can boost capacity and help you reach new customers.

Direct-to-consumer sales

Challenge

Lockdowns and a shift to remote work have accelerated digital adoption and contributed to new consumer behaviours, including buying goods directly from manufacturers.

Opportunity

Move sales and marketing online so you can be adaptive; take advantage of new online platforms; and sell your products directly to consumers.



How manufacturers can stay ahead in a downturn

Innovate

Use downtime to develop new ways of doing things. Create new designs and distribution methods. Invest in technology to boost productivity and put your business ahead of the competition.

Get online and embrace technology

Expand your e-commerce capability to position your business as a direct-to-consumer choice. Use technology to create seamless, connected production and fulfillment infrastructure.

Add value

Be strategic about partnerships to create higher value products. Consider vertical integration by adding a service component to your product to optimize your position in the value chain.

Invest in people

Evaluate employee skills to discover untapped talent and boost innovation and engagement. Recognize employee productivity, engagement and versatility.

Methodology

BDC produced its forecasts using the Global Economic Model from Oxford Economics. It uses an error correction methodology, where multiple time series estimate the speed a dependent variable returns to its equilibrium after an exogenous shock. This large-scale macroeconomic model has the advantage of being comprehensive as it includes thousands of macroeconomic variables.

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