Growing labour shortages, higher wages a pressing concern for Canadian businesses

By David Parkinson, Rachelle Younglai and Greg Keenan
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In Calgary, Dany Babakhanian is seeing the tide turn. Last month, he paid his first bonuses in three years at his sign-making company, IDENT. He's hiring again, and looking at giving his staff raises for the first time since the oil market collapsed in 2014.

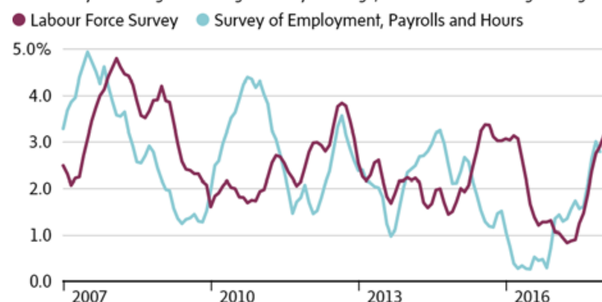
In Toronto, Shahin Alizadeh, president of Downtown Auto Group, is scrambling to find enough mechanics for his car dealerships. Pay for support staff has jumped roughly 25 per cent in the past couple of years.

In Vancouver, Betty Lou Pacey's optical-fibre lighting-equipment company, BL Lighting, is struggling to fill even entry-level positions, despite increasing the wages she's offering. Job postings can go weeks without a qualified applicant surfacing.

"It's a constant problem," she says. "Even for basic skills, you just can't find anyone."

Despite regional economic differences, a common theme has begun to emerge across the country. After years in the wilderness, wages for Canadian workers have finally begun to pick up. A boom in hiring in the past year or so, a symptom of the broad-based economic growth that has taken hold across a wide range of sectors and regions, has depleted supplies of workers and left many employers needing to step up their game to fill vacancies, especially in more specialized and skilled positions. Toss in recent minimum-wage increases in Ontario and Alberta, and the result has been evidence of the beginnings of building wage inflation in this country – the final ingredient that economists have long awaited in the long, on-again-off-again recovery from the Great Recession and subsequent oil shock.

Statistics Canada's monthly labour-force survey showed that average hourly wages grew 3.3 per cent year over year in January, the strongest growth yet in the steady rise in the pace of wages that began last summer.



THE GLOBE AND MAIL, SOURCE: STATSCAN / LFS DATA UNADJUSTED; SEPH DATA ADJUSTED AND INCLUDES OVERTIME PAY

While other measures suggest the LFS may be overstating the wage acceleration, there is nevertheless no question that wages have picked up over the past several months, as the country's unemployment rate sank to 10-year lows and the minimum-wage increases came into effect. Statscan's monthly payroll survey, released Friday, pegs growth of average weekly earnings on company payrolls at 2.3 per cent year over year, while a new broad-based composite measure introduced by the Bank of Canada to gauge wage inflation puts year-over-year growth at 2.2 per cent – in both cases, about double the pace of last spring.

It's still pretty tame, by historical standards; the country's average hourly wage was growing by more than 4 per cent annually prior to the 2008-09 global financial crisis and recession. Still, after years where the biggest concern was a disturbing absence of wage growth in the post-crisis economic cycle, the prospect of higher wages in the months to

come has quickly re-entered the equation for policy makers, economists and businesses.

For the country's employers, the question of how to attract and retain skilled staff in the country's increasingly tight and competitive hiring environment – and what it's going to cost them, in terms of more generous wages – has moved from a non-issue a couple of years ago to a pressing concern today.

"It's becoming increasingly part of the conversation," says Shane DeCoste, who runs the Express Employment Professionals staffing-agency office in Halifax.

Recovering momentum

One of the most interesting aspects of this burgeoning wage inflation is not that it's happening, but that it took so long. In Canada and much of the world's advanced economies, wages have been one component of the economy that failed to launch as economies have clawed their way back to normal following the Great Recession. Indeed, many economists began to question whether historical links between declining unemployment and rising wages – commonly referred to in economics circles as the Phillips Curve – had become broken in the aftermath of the global financial crisis.

Some experts have theorized that demographics have shifted the labour and wage landscape in advanced economies, as growing numbers of the huge baby-boomer generation cross over into retirement age. In Canada, the highest-paid and most productive age segment in the labour force, the so-called prime-age workers (age 25-54), has shrunk to about 65 per cent of the country's employed workers, down from 70 per cent a decade ago and 75 per cent two decades ago. About 21 per cent of the country's workers are older than 55, more than double their share of two decades ago.

Others wondered if globalization wasn't the key factor, as jobs in some sectors, most notably manufacturing, have gravitated to lower-wage producers overseas, and wage competition among trading partners generally has heated up. Another theory is that technology may be a culprit, as automation reduces the necessity and value of human labour. Yet another is that the declines in unionization over the past couple of decades have eroded workers' bargaining power.

But while all these factors are certainly at play, economist Philip Cross, a senior fellow at the Macdonald-Laurier Institute, an Ottawa-based think tank, argues that the underlying economic principle of the Phillips Curve – that shrinking labour supply relative to demand will push up wages – has merely been delayed, one of the many after-effects of one of the most severe and disruptive financial and economic shocks in history.

He also notes that, after the Great Recession, Canada actually had a relatively normal-looking recovery in wage growth; as recently as 2014, the pace was running close to 3 per cent. But that was derailed by the crash in oil prices in late 2014, which bludgeoned employment in key energy-producing regions and in businesses supporting the industry, and gutted business spending. The country's economy suffered a considerable setback – and the wage story was dragged down with it.

"I don't think the relationship is dead; I think we've shown … that a strong economy can still generate higher wage pressures. It's just been very hard to generate a consistently strong economy in the aftermath of the financial crisis," he says. "Just as we were getting going, we were hit by the oil crisis."

What has put Canada back on the wage-growth track has been an employment boom over the past year and a half, fuelled by a broad-based economic expansion, that has substantially re-shaped the labour landscape. The country went on an unprecedented tear of 17 consecutive months of job growth from July, 2016 to December, 2017, during which employment

swelled by 600,000 jobs – equal to the growth in the prior four years combined. The surge has quickly sopped up much of the available supply of labour. The Bank of Canada's labour market indicator, a composite of a variety of statistical gauges of labour-market health, fell to a post-recession low in the fourth quarter – indicating that market conditions are the tightest they have been in nearly a decade.

The central bank believes there is still some labour market slack, or more people available to work. The bank points to a still-elevated rate of long-term unemployment (those out of work more than a year) and a relatively low youth participation rate as evidence that there might be more available labour out there than the low unemployment rate suggests. This helps explain why wage growth is still modest by historical standards.

In a paper published by the bank last month, staff economic analysts also suggest that there is a lagging effect of labour slack on wage growth; even when the slack tightens, it takes up to a year for wages to catch up. But it's coming.

"Since the labour slack is currently being absorbed, this drag should disappear in coming quarters," the paper says.

'It's just a struggle'

Employers are already feeling the pressure, especially in regions and sectors of the economy where growth has been strong, and in industries (such at technology) where there is heavy competition for workers with highly specialized skill sets. The Bank of Canada's most recent quarterly Business Outlook Survey showed that concerns about labour shortages are at their highest in a decade. In many pockets of the economy, the race is on to secure workers and the pickings are much slimmer than they were a year or two ago – and, increasingly, costlier.

"Hiring is really hard … It's just a struggle," says Gregory Levey, co-founder of Figure 1, an app that allows the medical community to share images of tricky cases. Figure 1 is based in Toronto, which has become a popular destination for tech companies of all sizes – and a competitive place for landing tech talent. "I spend a lot of my time on hiring."

The company has raised salaries, on average, by about 10 per cent a year for the past five years, but it's still an uphill battle to find enough talent for his 50-person operation. Figure 1 recently opened a small New York office, because it couldn't find people in Canada with enough experience.

"The technical talent is hard to come by," says Bryan de Lottinville, president of Benevity Inc., a provider of corporate-philanthropy technology and services with a fast-growing staff of more than 400 in its Calgary, Toronto and Victoria offices. "The inventory of experienced software and technical people is a challenge in Canada."

Andrew Zakharia, who runs a boutique accounting firm called AZ Accounting, set up a social fund and has given his long-time employees raises eight times in the span of two years. "I am trying to do as much as I can to keep my staff because I am obviously concerned if they leave … It is hard to find those people," he said.

A nationwide shortage of technicians to fix vehicles is driving up costs for auto dealers such as Mr. Alizadeh's, pressing them to spend more time and resources developing people in-house. But even people further down the skill scale, such as receptionists, sales clerks and car jockeys, are commanding substantially more money to retain.

"We used to pay a receptionist, let's say, $14 an hour," says Mr. Alizadeh, whose dealership group operates 10 locations in central Toronto. "That seemed normal three years ago. Today, they're at $17 or $18."

In Ontario, the provincial government's minimum-wage increase and other labour-law

reforms that took effect in the new year have added to employers' labour cost burden. But for many businesses, the thinning supply of available workers has forced wages above the newly mandated $14-an-hour minimum anyway.

"Most manufacturers have recognized for the past year and a half or so that to get talent to show up for work, they have to pay more than the minimum wage," says Bruce Hein, who operates the Express Employment Professionals offices in Sarnia and Brantford.

"There's such high demand for good people, and a shortage of supply of good people," he says. "Most of our clients are crying for people to just show up every day."

Western signs of success

Part of Canada's wage growth story is about Alberta's boom, bust, and recovery.

When oil prices were soaring, wages were increasing at a torrid pace. In January, 2011, average weekly earnings expanded by 7 per cent year over year. But after oil prices collapsed, many businesses such as Mr. Babakhanian's had to slash jobs to survive the downturn. Other employers also gave their staff pay cuts and required them to take unpaid vacation.

This contributed to nearly two years of declining year-over-year wages from employers – the province's worst performance on record. The slump in Alberta and energy-sector wages weighed on the country as a whole and played a significant role in the stagnation of wage growth.

Mr. Babakhanian watched his company's revenue sink for about 26 consecutive months. He could not give his staff raises when he had lost half his revenue.

It was only in April of last year when IDENT's revenues stopped falling. Mr. Babakhanian remembers thinking: "We didn't slide last month. It seemed like we hit the bottom and we can start building the business around what the new normal looks like."

Around the same time, wages across Alberta started increasing again, as the province's oil-stained economic slump showed evidence of finally turning the corner.

Mr. Babakhanian's energy-sector clients started ordering more signs. He had to hire two new employees. And this January, for the first time since the oil crash, Mr. Babakhanian gave his employees a small bonus.

"I just gave everyone a small bonus saying thanks for sticking with me for the last two years. It has been a grind. We made a little, little profit and I want to share it with you guys," he said.

Mr. Babakhanian says it is too soon to tell whether he can give his employees pay raises this year. He said he could not afford to pay more now. He is still selling his products at the discounted rate.

Sharlene Massie, who runs About Staffing, an Alberta employment agency, says businesses are now offering contract positions rather than the hourly temp work that was common during the downturn. However, "No one has gone way up in pay," she says. "Calgary is starting to see some [wage] growth, but it hasn't yet manifested itself in the craziness that occurred a few years ago. We're not seeing anything like that in the bounce-back," Benevity's Mr. de Lottinville says. "But it is generally more positive."

Still, Alberta's wage turnaround has helped pace Canada's upturn in wage growth in recent months, as hiring and wages in the province begin to recover lost ground.

"The fact that Alberta is no longer in negative territory is having an effect, [and] recent growth from Ontario and Quebec has also driven wages up," says Andrew Fields, labour analyst with Statscan.

Searching for signs

Even though Canada's economic growth is expected to moderate this year and next, experts believe that wage growth should continue to build, as the economy continues to expand and soak up the available pool of labour.

Not that the pace of wage growth yet suggests any sort of rapid escalation in the Bank of Canada's slow reversal of its ultralow rate policy. The central bank's concern would be if wage gains began to get passed along to consumers and significantly accelerated Canada's inflation rate – a threat that still looks relatively tame at the current wage-growth trend that appears to be only slightly ahead of the central bank's 2-per-cent consumer inflation target.

"It's not the level of wage increases that you would start raising interest rates," Mr. Cross says. "That's barely keeping up with inflation, so you're not seeing the squeeze on profit margins. When you start getting in the 3-per-cent range … that's getting into the danger zone."

He characterizes the rate increases the central bank has put in place in the past year as more a case of unwinding the extremely low and stimulative rates put in place to combat the past economic crises, rather than a typical rate tightening spurred by mounting wage inflation.

Frances Donald, senior economist at Manulife Asset Management, argues that global competitive realities and online-shopping technologies will restrict businesses' ability to pass their rising wage costs on to consumers, and as a result may limit the impact on overall inflation compared with what we might have typically seen in past cycles.

"We are in a different inflation paradigm than we were even 10 years ago," she says. "There is now global competition for goods. So historically, if you could only buy a book in a small-town bookstore, you had no choice but to accept the higher cost." Now with e-commerce, she says, it is easy to find the lowest price.

Still, the rapid upturn in wage growth over the past several months has put wages on the Bank of Canada's radar as a consideration in setting interest rates this year, even if the overall size of the wage gains still looks relatively manageable.

"What they are looking for are signs of an overheated economy, and part of an overheating economy is the speed of the adjustment, not just the level of the adjustment," Ms. Donald says.

Craig Riddell, a professor at the University of British Columbia's Vancouver School of Economics, says the global resource boom that began around the turn of this century was the key driver of Canadian wage growth up until the oil shock, especially for middle and lower-end earners – and the reason why Canadian wages were able to withstand the recession and financial crisis better than others. With that boom now over, Canadian wage growth could have a hard time returning to the kind of levels seen before the financial crisis and the oil shock.

"The forces that contributed to it are now gone," he says.

'I don't have an answer'

Still, it's clear that the pressures of increasingly scarce labour in Canada is going to continue to press businesses to respond with more attractive wages.

"Some have done it willingly … some are midway through the convincing stage. But it's a common theme," says Mr. DeCoste of Express Employment in Halifax.

For some, that will mean looking for places to save costs to offset the increased wage hit. For others, it will mean passing their higher labour costs along to customers, by raising prices.

"We've had to increase the costs of our labour. Ultimately, we have to pass those increases along," says Chris Cooke, president of Huron Web Printing and Graphics, a commercial printer in Wyoming, Ont., a small town a little east of Sarnia. "You can't just suck it up."

But higher wages are only part of the solution – and, in some places, not providing much of a solution at all. Ms. Pacey, of BL Lighting in Vancouver, figures she has raised entry-level clerical wages by about 20 per cent over the past two years – and still can't find people with even the most basic qualifications. Meanwhile, she's thinking of cancelling paid lunch breaks to defray her rising labour costs.

"This lament is being heard throughout all employers. Every employer is just crying for employees," she says. "I don't have an answer. I really don't."

The tight labour market is already pushing more employers to spend more resources on developing and training their existing staff, and give them more opportunity for internal advancement.

"If they're support level, we try encourage them to sign up for apprenticeship in the service department. If they're a receptionist, we encourage them to aim for an administration position within the company," says Mr. Alizadeh of Downtown Auto Group. "You have to give them some level of excitement about the next phase."

Businesses are also getting more creative on non-monetary attractions to draw and retain staff. For example, at Figure 1, Mr. Levey gives his employees yoga classes, occasional catered lunches and one eye-catching perk: Unlimited paid vacation. (In practice, he says, people police themselves to something reasonable – about three weeks, on average.)

"Wages, by themselves, are just table stakes," Mr. de Lottinville of Benevity says. "Anybody who is not embracing a broader strategy to attract, retain and engage their people is really making a big mistake. You can't buy your way to making employees happy any more – if you ever could."