RBC Economics | Current Analysis

Squeeze Play: Higher wages alone won't solve Canada's labour shortage problem

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The Insights:

- Worker shortages will continue to challenge Canada's post-pandemic labour market as the baby-boom generation continues to move into retirement age. Roughly 23% of the working age population is expected to be 65 years or older by 2024.
- Shortages won't be limited to the industrial sector. Shifts in labour markets during the pandemic mean there won't be enough unemployed workers to fill gaps in other industries, particularly hospitality.
- The labour squeeze will push wages higher—but other benefits, like flexible work arrangements, will also be critical as firms seek to retain or hire employees.
- More immigration can help replenish vacancies. And businesses are increasingly looking at ways to boost existing employees' productivity through investments in machinery and technology.

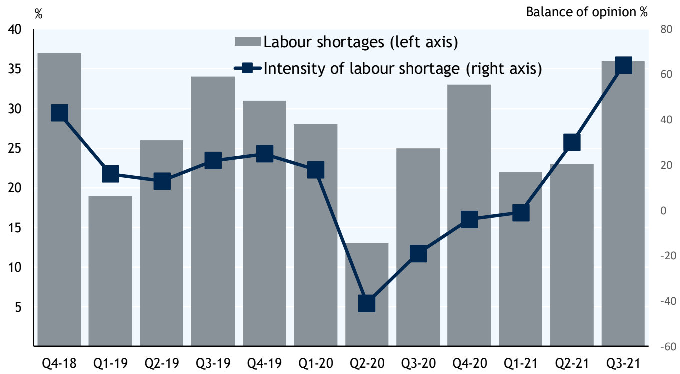
The Context:

Labour shortages, already a pressing issue for Canadian businesses before the pandemic, are poised to get worse. It increasingly looks like there will not be enough workers to satisfy current needs. This is evident both in the industrial sector, where skilled trades are in short supply and in the travel and hospitality industries, where the current employment shortfall compared to pre-pandemic levels is the largest. An aging population will continue to boost retirements and lower the share of the population participating in labour markets—removing roughly 600,000 workers from the available labour market pool over the next three years .

Our Analysis:

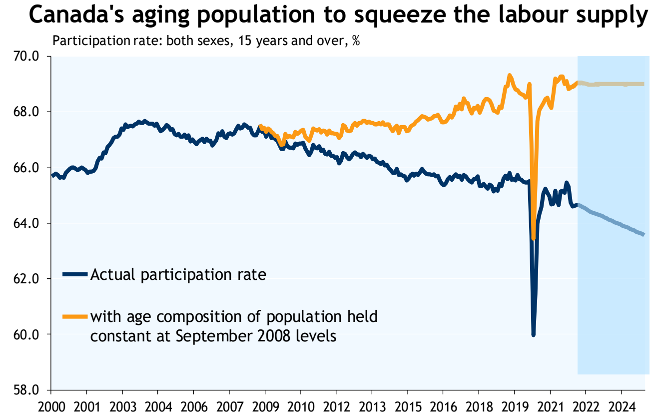
There are currently more than 870,000 vacant jobs in Canada, and over one third of businesses are grappling with labour shortages. That's not a new problem—nor is it easy to solve. Businesses were already reporting acute labour shortages in some sectors prior to the pandemic. Since 2008/09, an aging workforce has subtracted one

Canadian labour shortages getting more severe



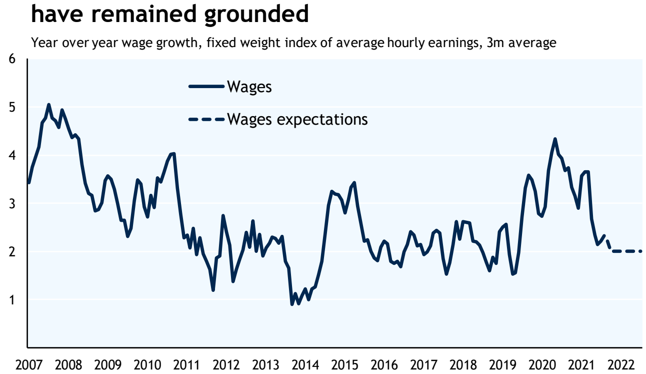
Source: RBC Economics, BoC Business Outlook Survey

Canada's aging population to squeeze the labour supply



Source: Statistics Canada, RBC Economics

Despite labour squeeze, workers' wage expectations have remained grounded



Source: RBC Economics, Statistics Canada, BoC Consumer Expectations Survey

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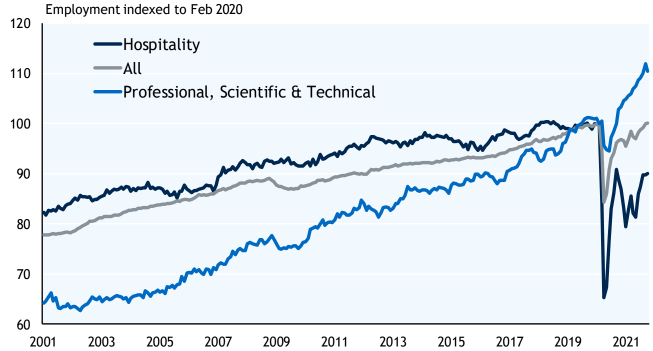
million workers from the economy. And longer-run demographic forces will continue to weigh on labour force participation as waves of baby boomers reach typical retirement age. In all, 23% of the working age population will be above the age of 64 by 2024, up from 20.5% in 2019 and 15% two decades ago.

The pandemic has only amplified this challenge. It likely delayed some retirements, making the future wave of exits from the labour force even larger. It also boosted asset prices, providing more financial security for some households considering retirement.

We expect labour shortages to become even more extensive in the year ahead. Job growth has been very strong in some sectors, including professional and financial services, which have added 245,000 jobs compared to February 2020 levels. It's been very weak in others, particularly the hardest-hit travel and hospitality sectors. Overall, employment in 'high-contact' services sectors remained 278,000 below pre-pandemic levels in October. And current demand for workers in these businesses was just over 200,000 in August. Meantime, there were less than 150,000 available unemployed workers more than 'normal' remaining in the labour pool, leaving a gap. As a result, there are probably not enough unemployed workers to either meet current demand or to bring employment in the sector back to pre-pandemic levels .

COVID-19 accelerated a worker shift into professional jobs

Employment indexed to Feb 2020

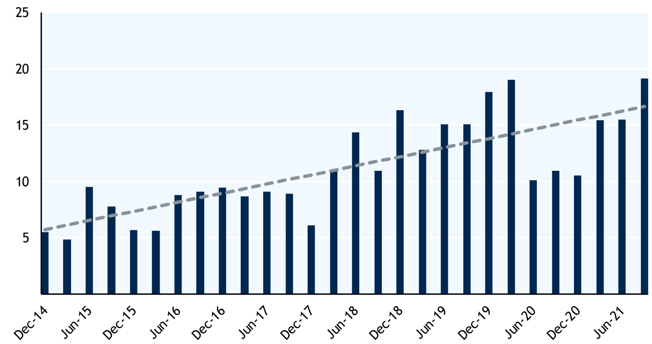


Source: RBC Economics, Statistics Canada

Much of this can be attributed to job switching: half of unemployed accommodation and food services workers that found employment in the last 12 months did so in other industries according to Statistics Canada.

Many workers feel more confident about switching jobs

Probability of leaving job voluntarily in the next 12 months



Source: RBC Economics , BoC Consumer Expectations Survey

With businesses still struggling to hire, we expect remaining unemployed workers to find their way into paid employment. But with too few workers to satisfy demand, pressure on wages will increase. Against that backdrop, it's not surprising that Canadians are feeling more confident about their employment prospects. In a recent Bank of Canada survey, more workers signaled a willingness to quit their current jobs. That's a positive sign from an employee's perspective, but a challenge for businesses trying to both retain workers and hire more.

The Road Ahead:

Higher wages aren't the only thing workers are seeking in their post-pandemic careers. Though shortages have put them in a strong bargaining position, workers' wages expectations haven't changed much. They are however, increasingly looking for more "suitable hours", according to BoC surveys. Those contending with child and elder care are seeking greater autonomy in work scheduling. And indeed, the most resilient industries through the pandemic have been in professional, scientific, and technical fields where working from home is easier. So while higher wages will be part of the equation, firms looking to hire from within a limited talent pool will also need to place emphasis, where possible, on more holistic employment offerings.

Higher planned immigration rates will also help, as will business plans for more investments in machinery, as well as in digitalization, that could boost productivity of existing workers. But those investments take time to bear fruit. In the meantime, it looks likely that labour shortages will continue to intensify, putting a cap on the productive potential of the economy, slowing growth and keeping upward pressure on costs.