# Special Report

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November 26, 2018


# End of an Era for Canada's Auto Industry?


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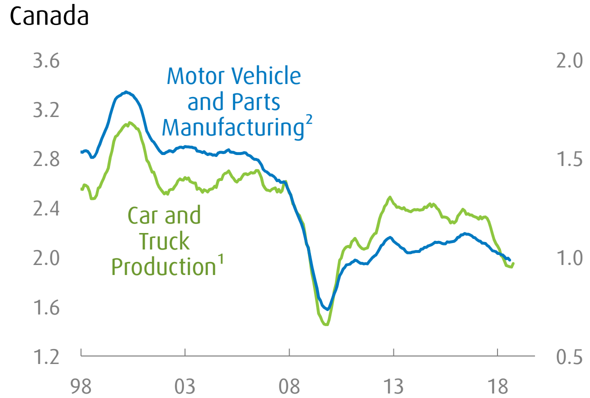
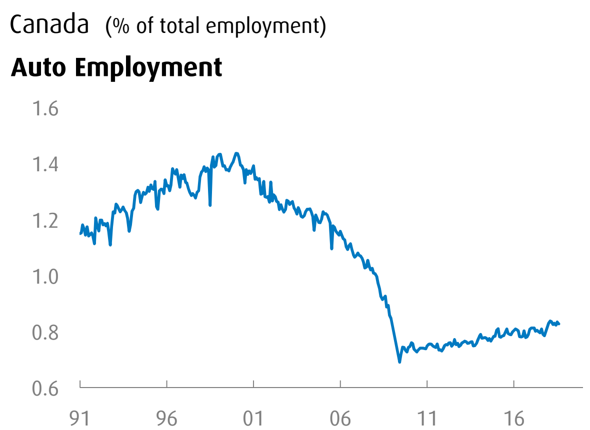
- The news that GM's venerable plant in Oshawa will be *"unallocated in 2019",* along with four other North American plants, will dig into Canadian growth over the next year. In this Special Report, we look at the various potential implications of this important development, for financial markets, the regional outlook and the sector.
- As background, the motor vehicle and parts industry directly accounts for just a shade under 1% of overall Canadian GDP (and about 2.3% of Ontario GDP). This is well below the recent peak of over 1.8% in 1999, as the sector has been declining in relative terms amid tough competition from Mexico and a falling market share for North American vehicles *(Chart 1)*. Production has similarly dropped from a peak above 3 million vehicles per year in 1999 to less than 2 million in the past 12 months.
- Gauging the economic impact of a shutdown at Oshawa is complicated by the fact that: a) some management jobs will also be lost; and, b) the plant also acted as a "finishing" facility for some truck production. We estimate at first blush that today's measures would cut Canadian GDP by 0.1%-to-0.2% over a full year.
- Similar to autos' portion of GDP, the share of total employment has fallen sharply since 2000. While conditions have stabilized for the most part since 2009, the share is just over half of the peak seen about two decades ago *(Chart 2)*. Indeed, most of the damage was done from 2000 to 2009.
- According to Statistics Canada's industry employment survey (SEPH), the sector employs almost 140,000 people, meaning the nearly 3,000 GM cuts directly account for a bit over 2% of the tally. However, that's just 0.02% of total employment.
- The income hit looks to be a bit more impactful, as the job losses consist of solid middle-income and some upper-income earners. We estimate the income losses will be around $300 million annually. After accounting for the multiplier effect (historically, some have suggested an almost 7 times multiplier from auto sector jobs, but we're assuming something closer to 4 times), the cut to GDP could thus be in our estimated range above.

Chart 1
**Auto Sector: Gearing Down**




[1] (lhs : mlns of units : 12-mo m.s.) [2] (rhs : % of real GDP : 12-mo m.a.)
Sources: BMO Economics, Haver Analytics

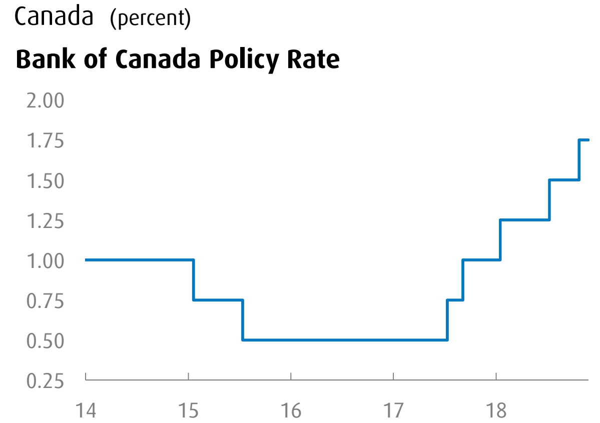
Chart 2
**Employment Perspective**




Sources: BMO Economics, Haver Analytics

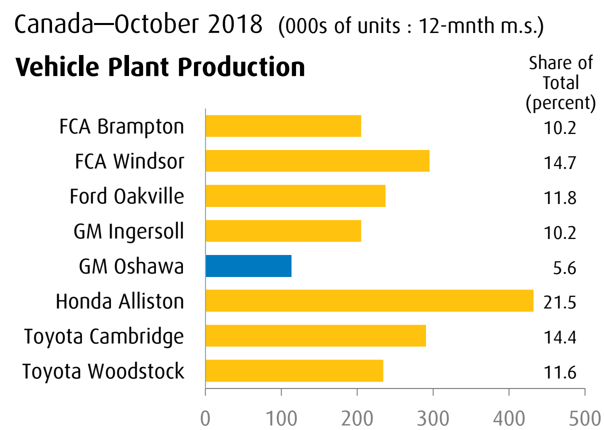
- Over the past month, Bank of Canada rate-hike odds have consistently fallen as the drop in oil prices and broader risk aversion take a toll. The GM announcement adds further fuel to speculation that the BoC could pause for longer.
- While the closure hits close to home for Governor Poloz, the impact on GDP and employment isn't likely enough, by itself, to change the trajectory for policy *(Chart 3)*. Indeed, the weakness in oil prices will likely be the larger concern, along with their longstanding concerns around household debt.
- Meantime, the BoC believes that the output gap is closed and labour markets are very tight, according to the Business Outlook Survey. Assuming oil prices stabilize and the broader backdrop doesn't deteriorate further, a January hike remains our base case. However, it's a much closer call than even two weeks ago, and—as previously mentioned—depends on at least a partial recovery in WCS oil prices.
- The announcement is a tough pill to swallow given the Oshawa plant's symbolic status and longstanding ties to the local community. However, the plant's position in the pantheon of Canadian assemblies has long since been surpassed by its competitors. In fact, the Oshawa plant produced the fewest units in Canada over the past year among the nation's eight assembly plants, and that's including the final finishing and painting of mostly assembled pickups from the U.S. *(Chart 4)*. Curiously, out of all of the announced closures, the Oshawa plant is the only one with flex capabilities (that is, the ability to manufacture both cars and trucks on the same line), something that would have seemed ideal were a manufacturer to shift its strategy towards light trucks and electrified vehicles.
- While Canadian auto production has been on a long-term decline, the trend has not applied across the board to all plants and manufacturers. GM's Canadian production has declined 59% since its peak in 2004 and is down over 45% from its post-recession high in 2012. For context, that amounts to a staggering 570,000 units displaced since 2004 and a hefty 290,000 unit decline since 2012. The trend has been much more stable and, in some cases, positive for other manufacturers in the context of the current cycle.

Chart 3
**BoC Likely Unfazed**



Sources: BMO Economics, Haver Analytics

Chart 4
**Canada's Output by Facility**



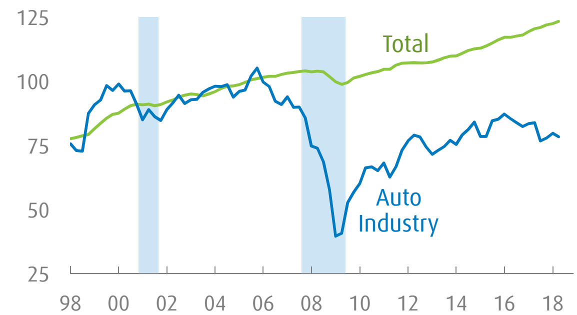
Source: BMO Economics

- From a regional perspective, the impact will fall squarely on Ontario, as the auto sector plays a significant role in the province's economy. Directly, auto and parts manufacturing accounts for 2.3% of GDP, but accounting for various indirect effects (think transportation, housing, local retailers, etc.) could bump the real-world impact to 5%-to-10% of the provincial economy.
- That said, the auto sector has been gradually pulling less of the Ontario economy over time, and the GM Oshawa plant is itself an illustration of that. Since peaking in 2005, real output in the sector has contracted by roughly 22%, recovering only about half of the financial crisis declines. That has pulled the sector's weight down from a high of 4.2% at its peak in 1999. In other words, the sector accounts for only about half the weight it did less than 20 years ago *(Chart 5)*. Still, we judge the full-year growth impact from the shutdown could be in the 0.3-to-0.5 ppt range for the province.
- From an employment perspective, the coming job losses shouldn't move the needle on the provincial jobless rate, especially since some current workers may now choose to leave the workforce (though we don't want to downplay the significance in the Oshawa community itself).
- While the impact on the Ontario economy will likely be contained overall, the longer-term symbolism of this move is significant. That is, Ontario continues to gradually shift away from basic manufacturing, toward higher value added production/research (true even within the auto industry itself) and into professional services, a trend that began to unfold at the start of the 2000s, and then accelerated through the financial crisis.
- Meantime, today's news is yet another illustration of the importance of policy geared toward business competitiveness—from all levels of government.

Chart 5
**Autos & Ontario: Smaller Share**

Ontario (2005 = 100)

**Real Production**




Shading marks periods of U.S. recession
Sources: BMO Economics, Haver Analytics