

Good news: growth in the number of businesses is accelerating in Canada

As the Bank of Canada has frequently pointed out, there is a close link between new business creation, real GDP growth and non-residential investment. According to Statistics Canada, growth in the number of private firms has recently accelerated in this country, after wavering in recent years. This confirms our forecast of more robust economic growth in 2016, and an eventual increase in non-residential investment outside the energy sector.

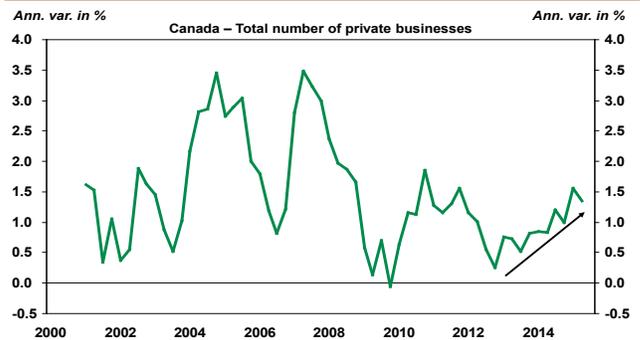
Change in the number of businesses has garnered special attention from the Bank of Canada (BoC) in the past few years. Governor Stephen Poloz has referred to it on several occasions, in particular in a speech he gave on May 19 in Charlottetown. He mentioned that “new firms are the prime creators of new jobs in the economy.” Also according to Stephen Poloz, “recessions are painful and require adjustments. Companies, and sometimes entire industries, shut down, often never to return. But after the destruction, new ones are born that help drive the next wave of growth.” Furthermore, “while part of the increase in business investment will be companies adding to their own capacity, another part will be the creation of new companies.”

In short, the BoC perceives a close link between change in the number of firms, the economic growth cycle and growth in non-residential investment. In light of the difficulties that the Canadian economy has recently experienced, and the decline in non-residential investment, it is therefore appropriate to analyze the recent trend in the number of businesses in the country. Lately, Statistics Canada has been providing quarterly data on the subject.

THE NUMBER OF BUSINESSES IS STILL ON THE RISE

As may be seen in graph 1, the annual change in the number of businesses declined rapidly after the great recession of 2008–2009. A rally was seen starting in 2010, but it ran out of steam fairly quickly because another slowdown was recorded at the beginning of 2012. We must keep in mind that global economic conditions remained uncertain throughout that period, greatly influencing business confidence. This

Graph 1 – Growth in the number of businesses has accelerated since the end of 2012



Sources: Statistics Canada and Desjardins, Economic Studies

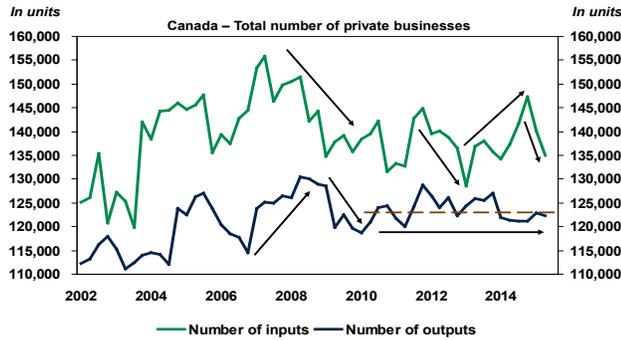
mainly resulted in less creation of new businesses (input¹) in 2012, while the number of business closures (output²) held fairly steady (graph 2 on page 2).

Annual growth in the number of businesses started to accelerate again from the beginning of 2013 onwards, reaching 1.6% in the first quarter of 2015. The upturn in U.S. demand and the lower value of the Canadian dollar were certainly positive factors in that new momentum. However, growth in the number of firms waned somewhat

¹ Inputs are businesses that had no employees in the previous year and that had employees for the first time in the designated quarter of the current year.

² Outputs are businesses that had no employees in the subsequent year and that had employees for the last time in the designated quarter of the current year.

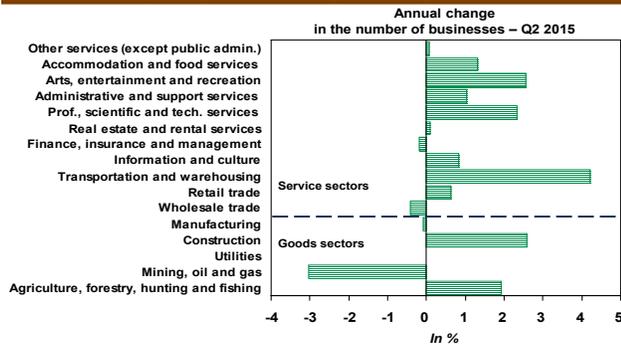
Graph 2 – The recent swings in the total number of businesses come mainly from inputs



Sources: Statistics Canada and Desjardins, Economic Studies

in the spring of 2015, when new business creation slowed once again. Lower energy prices and the technical recession that followed were obviously key factors in that slowdown. Thus, the mining, oil and gas sector posted the worst annual change in the number of businesses in the second quarter of 2015, with a pullback of 3.0% (graph 3). Manufacturing and wholesale trade, which suffered some contagion effects following the decline in non-residential investment in the energy sector, also exhibited a downturn in the number of businesses.

Graph 3 – The number of businesses is in decline especially in the mining, oil and gas sector



Sources: Statistics Canada and Desjardins, Economic Studies

But in most of the other sectors of the Canadian economy, the numbers are quite positive. For example, annual growth in the number of businesses is fairly high in transportation and warehousing, construction, arts and recreation, professional, technical and scientific services, agriculture, forestry, hunting and fishing and accommodation and food services.

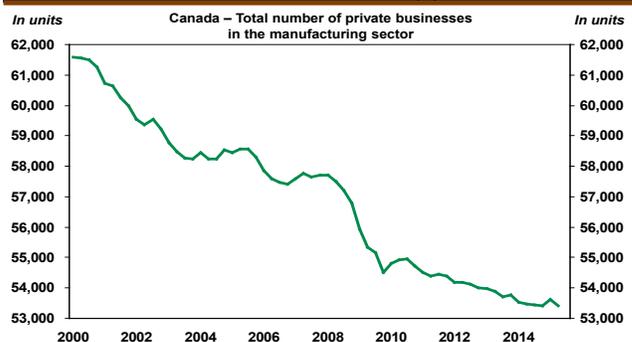
HEADING TOWARDS MORE ROBUST GROWTH?

As oil prices stabilize, the negative effects observed in the energy sector and related industries should soon begin to fade. In such conditions, it is reasonable to believe that growth in the number of businesses will continue its upward trend in the coming quarters.

This means that economic growth should accelerate in the quarters that lie ahead. Our scenario calls for real GDP growth of 2.1% in Canada in 2016, after a gain of just 1.1% in 2015. Furthermore, non-residential investment could eventually benefit from the increase in the number of businesses in the non-energy sectors.

In conclusion, we would point out that the data on the number of businesses shed some very interesting light on the manufacturing sector and the transformations that are currently underway in the Canadian economy. The number of businesses in the manufacturing industry has been in decline since data were first collected on the subject (graph 4), bearing witness to its shrinking weight in Canada’s overall output. However, this is a phenomenon that is fairly widespread throughout most industrialized countries, and that was exacerbated by the effects of the great recession of 2008–2009 and by the loonie being close to parity. We are forced to note that most of those businesses seem to have disappeared for good, and that they will not be replaced by new manufacturing firms. Conversely, many service sectors have enjoyed net business creation in recent years—evidence of the shifts that are currently in progress within the Canadian economy.

Graph 4 – The number of businesses in the manufacturing sector has been in decline for many years



Sources: Statistics Canada and Desjardins, Economic Studies

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