Economics

IN FOCUS

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What's *really* happening in Canada's labour market?

by **Andrew Grantham** andrew.grantham@cibc.com

Job growth appears to be accelerating again and the unemployment rate has barely increased since trade uncertainties flared up earlier this year. It seems too good to be true. Unfortunately, that's probably because it is. There's ample reason to question whether employment growth has really been as strong as suggested by the widely followed Labour Force Survey (LFS), while the rise in unemployment may actually be largely unrelated to the struggles of the manufacturing and other trade-sensitive sectors.

If the Canadian labour market is weaker than advertised, this slack should eventually place downward pressure on core measures of inflation and bring a couple more interest rate cuts from the Bank of Canada later this year.

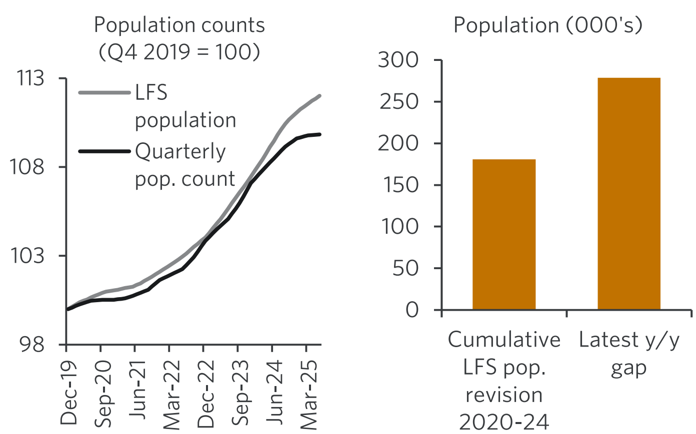
Population problems

A key reason for continued strength in the LFS employment count could be the fact that the base population in that survey has slowed less than that seen within the quarterly population data. While population data in the LFS can and will differ at times because it only counts working age persons, it can also be prone to future revision particularly during times when accelerations/decelerations are being driven by non-permanent residents (NPR's).

In fact, earlier this year, a rebasing of the LFS resulted in upwards revisions to population and employment counts between 2020 and 2024. That was a period of time when NPR'S were generally rising as a share of the population and the LFS population count had lagged the quarterly figures.

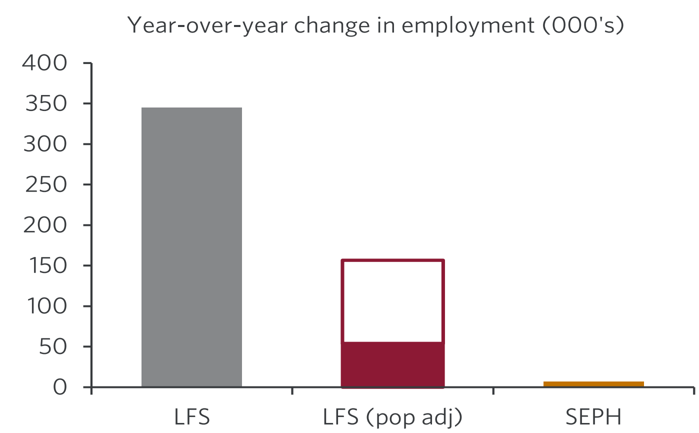
Today the opposite is true, with the quarterly population count decelerating sharply largely because of the impact of NPR's. In this situation the LFS population figures (and by extension employment growth) may end up being revised downwards at some point in the future. How much? Judging by the gap that has opened up recently between the LFS and quarterly population figures (Chart 1, left), the revision could be significant. In fact, the gap that has opened up in just one year is larger than the cumulative upward revision seen between 2020 and 2024 mentioned previously (Chart 1, right).

Chart 1: LFS population has diverged from quarterly count (L); a future revision could be large (R)



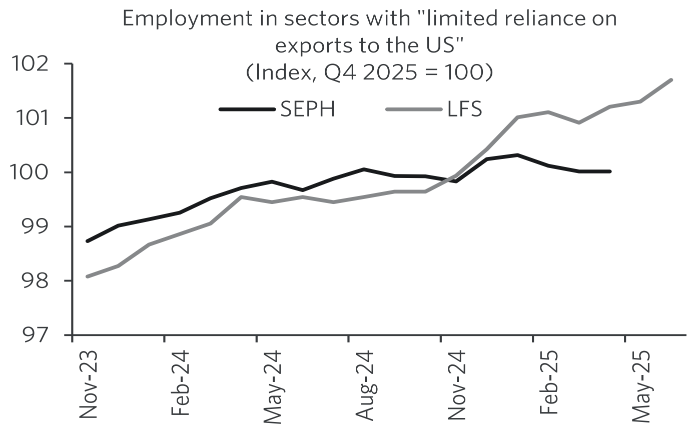
Source: Statistics Canada, CIBC

Chart 2: LFS employment growth may look a lot weaker if population growth were slower



Source: Statistics Canada, CIBC

Chart 3: Employment has been weaker in the SEPH survey, even in trade insensitive sectors



Source: Statistics Canada, CIBC

If the year-over-year growth rate in population within the Labour Force survey matched the recent quarterly data, and assuming the employment-population ratio is correct, then job growth over the past year could be cut down to a fraction of what is currently reported (Chart 2).

The complication though is that, as we have written about in the past, the quarterly count could actually be understating population growth due to it overestimating the number of NPRs leaving the country, and undercounting asylum seekers and "others". However, even after accounting for this impact, we suspect that actual population growth, and by extension employment, has been weaker than advertised by the LFS (Chart 2 again). These population-adjusted figures would also be closer to the stall shown in the payrolls survey of employment (SEPH) over the past year.

This is important because the Bank of Canada has recently used the strength in LFS employment, and in particular continued job growth in sectors less sensitive to trade uncertainties, to justify its pause in interest rates. However, if these data are being inflated by an inaccurate population count, and if the SEPH data are potentially painting a truer picture, then the employment trend even within these sectors could be much weaker than believed (Chart 3).

More than one explanation

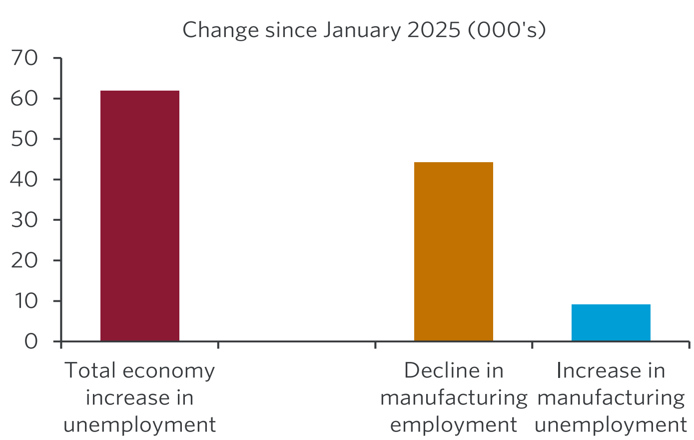
Of course, even if the population and employment counts are overstated, this doesn't bring into question the validity of the unemployment rate which, at 6.9% now, hasn't risen much relative to where it stood prior to trade uncertainties escalating.

What we can question though is just what has been causing the unemployment rate to move higher. It is very easy to assume that trade uncertainties, resulting in job losses within the manufacturing sector, have driven the entire increase. After all, the rise in the number of persons employed has broadly matched the decline in manufacturing employment since January (Chart 4).

However, alternative data series within the same LFS report suggest that this may not be the complete story. While manufacturing employment has fallen by 45K since January, unemployment data by sector suggests only a 9K increase. In other words, only 20% of the decline in manufacturing employment appears to have been reflected in the unemployment rate. Some may have retired, temporarily left the labour force to wait out trade uncertainty, or have found work in other sectors.

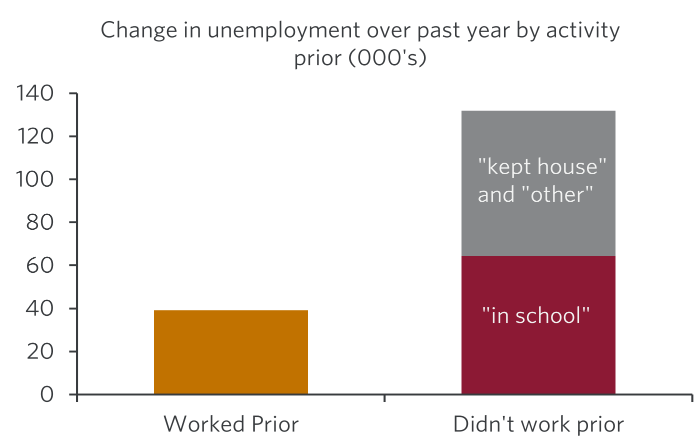
This tallies with aggregate data suggesting that it hasn't been "job losers" driving the unemployment rate higher over the past year, but rather the continued difficulties finding work of people entering or re-entering the labour market. This represents the continued and well documented struggles of students. However, increasingly it also represents people re-entering the workforce having previously "kept house" (Statistics Canada's definition not mine) or "other" reasons (Chart 5).

Chart 4: Manufacturing's woes have driven only a fraction of the rise in unemployment



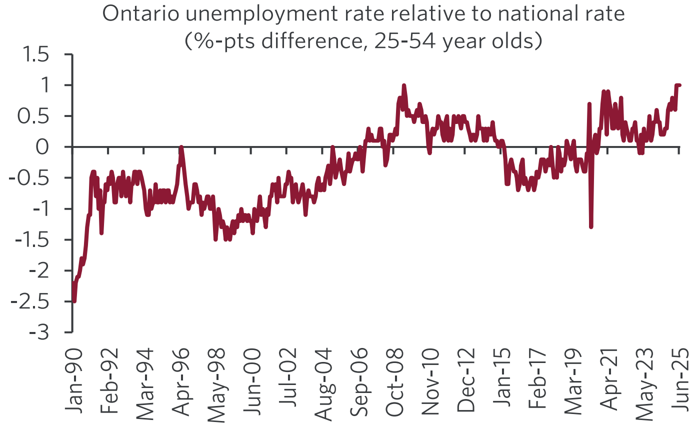
Source: Statistics Canada, CIBC

Chart 5: Increase in unemployment driven by lack of job options for new and returning workers



Source: Statistics Canada, CIBC

Chart 6: Ontario's unemployment rate near historic high above national average

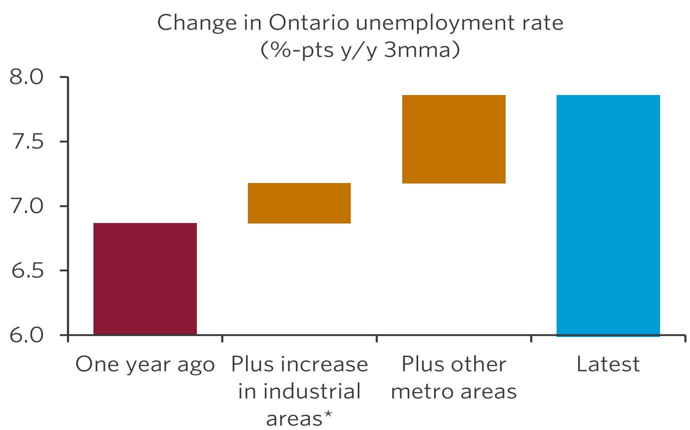


Source: Statistics Canada, CIBC

The provincial breakdown is also used as evidence that tariffs have been the main driver of the rise in unemployment since the start of the year. After all, Ontario has seen the biggest increase, and this was expected due to its large dependence on exports to the US. The current unemployment rate for prime-aged workers in Ontario is now 1% above the national average (Chart 6) — a divergence only seen once before during the 2008/09 financial crisis (when Ontario's finance sector was also struggling, and not just its manufacturing base).

However, much like the national figures shown above, Ontario's unemployment rate increase has been mainly a reflection of new entrants been unable to find work, rather than job losses in the manufacturing sector. While city level data show large increases in unemployment rates in trade-sensitive areas such as Oshawa and Windsor, these more industrial areas of Ontario have actually accounted for only a fraction of the province-wide rise in unemployment rate (Chart 7). The Greater Toronto Area (GTA), with its diverse economy, has contributed about half of the increase.

Chart 7: Rise in Ontario unemployment not just a reflection of increased joblessness in industrial areas



*Oshawa, Windsor, Guelph, Barrie, Kitchener-Cambridge-Waterloo, Brantford, Barrie.

Source: Statistics Canada, CIBC

What's really happening

The notion that Canada's labour market is in good health, aside from understandable weakness in trade sensitive areas such as manufacturing, is too simplistic and likely incorrect. Actual employment growth over the past year may have been much slower than advertised by the LFS, including in sectors that should be less sensitive to trade uncertainties. Meanwhile, the modest rise in unemployment rate appears to reflect the continued struggles of new or re-entrants to find work, rather than actual job losses confined to areas such as manufacturing.

A weaker than advertised labour market should, over time, place downward pressure on core measures of inflation and allow the Bank of Canada to cut interest rates again before the end of the year.

Contacts:

Avery Shenfeld
avery.shenfeld@cibc.com

Benjamin Tal
benjamin.tal@cibc.com

Andrew Grantham
andrew.grantham@cibc.com

Ali Jaffery
ali.jaffery@cibc.com

Katherine Judge
katherine.judge@cibc.com

CIBC Capital Markets
PO Box 500
161 Bay Street, Brookfield Place
Toronto, Canada, M5J 2S8
Bloomberg @ CIBC

economics.cibccm.com