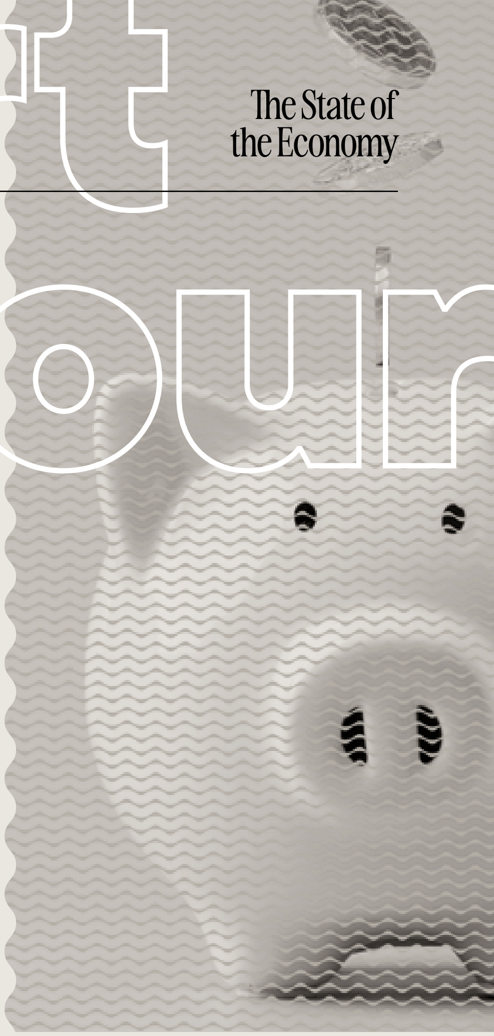
Part Four



Why stagflation is still possible and why this matters to hoteliers

FROM OMNIGENCE ASSET MANAGEMENT

While financing trends underscore the resilience of Canada's hotel sector, sustaining this momentum requires addressing broader structural pressures.

Rising inflation, energy costs, and demographic shifts are compounding operational challenges, particularly as stagflation risks heighten economic uncertainty. These forces tie back to earlier discussions on strategic investments, as hoteliers must balance immediate financial opportunities with long-term resilience. The next section explores how the industry can navigate these pressures through targeted strategies in efficiency, workforce planning, and sustainability to secure future growth.

As Canada's economy faces the forces of rising inflation and sluggish growth, and the threat of tariffs on Canadian goods by the U.S., Canada may enter a period of stagflation. A report from Omnigence Asset Management, "Is Canadian Growth Dead? Preparing for Stagflation and the Socio-Economic Barbell," provides an analysis of the economic pressures that could shape the next three decades. These include housing shortages, increasing energy costs, a declining middle class, and stagnating real GDP per capita. Canadian hoteliers, already dealing with evolving consumer behaviour, must now adapt to this new economic landscape.

Pressures on hospitality operations

The report highlights how Canada's housing supply deficit—estimated at more than 3 million units—has created ripple effects across the economy. For the hotel industry, this shortage impacts workforce housing, particularly in urban and remote regions where staff accommodations are critical. Combined with Canada's population growth rate, which is among the highest in the developed world at over 2.7 per cent annually, this exacerbates demand pressures without sufficient infrastructure to support it.

Energy costs have also risen dramatically, nearly tripling as a share of GDP compared to historical averages. These higher expenses directly affect hotel operations, from utilities to transportation. Omnigence notes that energy prices now consume 8 per cent of GDP, compared to a long-term average of 4 per cent—a stark reminder of how external costs can disrupt profitability.

Changing consumer spending

One of the most significant trends identified in the report is the erosion of the middle class, a phenomenon Omnigence calls the "socio-economic barbell." Between 1971 and 2021, the share of adults in middle-income households dropped from 61 per cent to 50 per cent. At the same time, the proportion of lower- and upper-income households has increased. This restructuring is reshaping consumer habits, with implications for hotels:

- Budget-conscious travellers are likely to seek out affordable options, from economy hotels to extended-stay properties. These preferences align with reduced discretionary spending, driven by higher costs of living and limited wage growth.
- High-income travellers, on the other hand, may sustain demand for boutique and luxury accommodations, which could buffer parts of the industry from broader economic pressures.

The report also notes the long-term weakening of the Canadian dollar relative to the U.S. dollar, could make Canada a more attractive destination for international visitors. This dynamic creates an opportunity for hotels to increase their focus on marketing to foreign tourists.

Adapting hotel strategies

Omnigence underscores the need for operational resilience to address the pressures of stagflation. For hoteliers, this means adopting targeted strategies to manage costs and capture emerging opportunities:

- **Energy efficiency:** Investing in energy-efficient technologies, such as smart HVAC systems and renewable energy sources, can reduce costs in a time of persistently high energy prices. These initiatives also align with guest preferences for sustainability.

- **Workforce investments:** High housing costs and labour shortages make it critical to provide competitive wages and, where possible, housing assistance for employees. Retention efforts can mitigate the costs associated with the constant turnover in a tight labour market.
- **Digital transformation:** Tools like AI-based pricing systems, automated check-ins, and enhanced data analytics can streamline operations and enhance guest experiences, allowing hoteliers to do more with fewer resources.

Long-term considerations

Canada's economic fundamentals suggest a prolonged adjustment period. Real GDP per capita, which has stagnated since 2013, is projected to remain unchanged until the 2050s, according to Omnigence's modelling. During this time, inflation is expected to remain above historical averages, further straining middle-income earners and small businesses.

The report also flags demographic trends, particularly Canada's aging population, as a critical driver of economic change. By 2050, the dependency ratio—defined as the number of people of working age for every retiree—will drop to 2.2, down from 4.4 in 2010. This shift will increase demand for tailored services, such as accessible accommodations and wellness tourism, providing new opportunities for hotels to innovate.

Insights from Omnigence

Omnigence's analysis indicates that stagflation is not merely a theoretical risk for Canada but a tangible reality. The report suggests that businesses, including hotels, need to focus on inflation-resistant investments and strategies aligned with long-term demographic and economic trends.

ABOUT OMNIGENCE

Omnigence Asset Management specializes in macroeconomic analysis and investment strategies for complex economic environments. The report "Is Canadian Growth Dead? Preparing for Stagflation and the Socio-Economic Barbell" was authored by Omnigence directors shown above left to right: Barclay Laughland, data scientist Keenan Viney, Matt Barr and Stephen Johnston.