Scotiabank

GLOBAL ECONOMICS

INSIGHTS & VIEWS

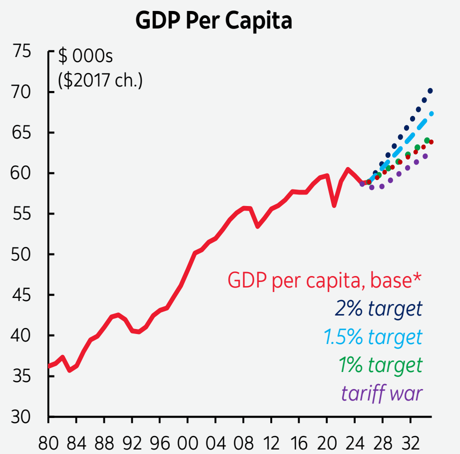
February 27, 2025

Contributors

Jean-François Perrault
SVP & Chief Economist
Scotiabank Economics
416.866.4214
jean-francois.perrault@scotiabank.com

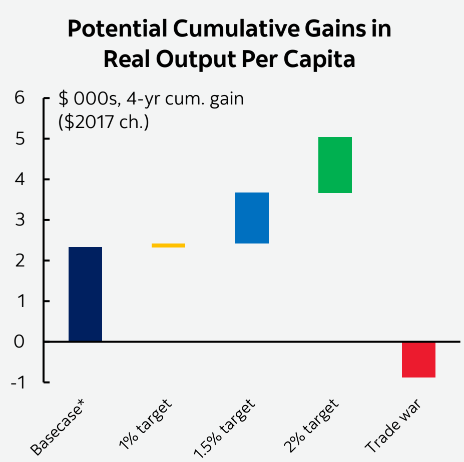
Rebekah Young
VP & Head of Inclusion and Resilience Economics
Scotiabank Economics
416.862.3876
rebekah.young@scotiabank.com

Chart 1



Sources: Scotiabank Economics, Statistics Canada.
*See Footnote 1 for assumptions.

Chart 2



Sources: Scotiabank Economics.
*See Footnote 1 for assumptions.

Owning the Podium in Canada's Federal Elections

CANADA'S NEXT LEADER SHOULD MAKE AN EXPLICIT PLEDGE TO IMPROVE LIVING STANDARDS

- **Canadians could face a federal election within weeks. Aspiring leaders will be challenged to present a compelling—and unified—long-term vision for the country, even as the immediate threat of a trade war looms.**
- **Crafting a vision is often the easy part. Ahead of polls, leaders often make sweeping promises to improve Canadians' lives. However, execution frequently falls short, and too often these promises fail to translate into meaningful and broad-based improvements in living standards.**
- **Canadians should demand better results from their governments. The federal election presents an opportunity to introduce a formal accountability mechanism to hold leaders to task. An explicit economic target tied to national welfare could instill greater discipline in policymaking, force trade-offs, and, importantly, provide clear and timely signals when the government is off track.**
- **We propose that leaders commit to raising real GDP per capita growth by 2% annually on a sustained basis. While far from perfect, GDP per capita is measurable, timely, and easily grasped by Canadians. Stronger gains ultimately support higher real incomes for households. This level of ambition would equate to a compounding annual gain of ~$1,200 per person or almost $5,000 over a 4-year mandate (charts 1 & 2).**
- **The scale of effort required to reach a 2% per capita GDP growth target would be staggering. Earlier investments in the country's human capital would need to be matched with similarly audacious capital investments. It would also require extraordinary coordination across all policy levers, leaving little margin for distraction.**
- **Annual capital investment would have to be about ~15% higher (or an incremental ~$60 bn) to be consistent with such a target. At present, annual increases barely keep pace with depreciation let alone population growth. Even then, deep structural reforms would be needed to unlock accompanying total factor productivity gains to make the math work.**
- **The sheer scale of the challenge should spur political leaders to chart a course that at least approaches the level of ambition Canadians expect.**
- **But the potential fiscal investments and the political capital required should not be underestimated. The price to the public purse could run in percentage—not decimal—points of GDP if Canada wants to front-run uncertainty in the near term and make a downpayment on transforming the economy in the long run through well-crafted policies that incent greater private sector investment.**
- **Aspiring leaders must be upfront with Canadians if they are to gain a license to execute against such an agenda. And they must also establish strong frameworks for transparency and accountability, ensuring demonstrable progress toward their commitments if they are to maintain that license.**

HEADING TO THE POLLS

Canadians will soon head to the polls, with Parliament prorogued until March 24th as the governing Liberal Party prepares to elect a new leader on March 9th. Opposition parties have signaled they will push for a non-confidence vote as soon as Parliament resumes, potentially triggering an early election. However, the incoming Prime Minister could seek to delay the vote to pass urgent legislation with cross-party support—especially if tensions with the U.S. escalate. Regardless, an election is inevitable with the likeliest scenario this Spring and, latest by law, October.

The race is shaping up to be competitive. Recent polls indicate a significant narrowing between the Conservative Party leader and the Liberal frontrunner. While concrete policy platforms will only emerge once the election writ is issued, early messaging suggests leaders are seeking to distinguish themselves across the usual policy fronts. Potentially diverging policy directions could carry sectoral implications, both within and across industries. Yet, shifting U.S. policy developments could ultimately overshadow any domestic agenda, regardless of which party ultimately takes power.

FEET TO THE FIRE

Canadians should demand better results from their governments. The upcoming federal election presents an opportunity to strengthen government accountability for decisions that shape the country's future. While elections already serve as a check on poor governance—allowing voters to replace ineffective leaders—a more structured accountability mechanism could better align political promises with public expectations. Election platforms are often filled with ambitious proposals to improve the country's trajectory. Sometimes they succeed; other times, they fall short. The fundamental issue with platforms is their lack of a binding commitment mechanism: the more promises a party makes, the easier it becomes to claim success, even when policies as a whole fail to deliver meaningful economic benefits.

We propose that the next Prime Minister commit to an explicit economic target—one directly geared to the standard of living—as hopefuls make their pitches to Canadians. A reasonable option could be GDP per capita growth. Higher productivity and output per worker drive sustainable, non-inflationary wage increases and ultimately improve household incomes over time. The next government could set an explicit target for GDP per capita growth, committing to a specific annual increase or a cumulative goal over its mandate. While not a perfect metric—given recent distortions from rapid population growth—it remains one of the most transparent, timely, and easily understood indicators of economic progress.

Such a commitment could add discipline to party platforms, serving as a macroeconomic filter for policy proposals. It would push parties to structure their platforms around a tangible objective, backed by a clear framework for measuring progress, evaluating trade-offs, and managing risks. If government policies fail to meet the target, policymakers would be compelled to reassess their approach and implement necessary adjustments to deliver promised economic gains.

This level of accountability is standard in other sectors. Publicly traded companies routinely provide earnings guidance, outlining how they plan to achieve profit targets. If they fail to meet expectations, share prices drop, executives are held accountable, compensation shrinks, and management adjusts strategies accordingly. Within the public sphere, the Bank of Canada's inflation-targeting mandate provides a similarly explicit and measurable tool for accountability. The Governor must explain his decisions eight times a year and constantly course-correct when data deviate from expectation.

Political ownership is key. Countless think tanks, growth councils, and international organizations have called for similarly ambitious economic goals, but no government has fully owned such a transparent, high-stakes target that allows for meaningful evaluation. A well-defined GDP per capita goal would require governments to explain any shortfalls and outline corrective actions, ensuring greater public scrutiny by Canadians. This type of commitment may well be a bridge too far for leaders and shocks can throw governments off path, but the overriding principle stands: political platforms, and subsequent policy actions should they win, should be squarely focused on delivering tangible economic benefits to Canadians.

Critics may argue that good governance is about more than economic growth—it involves enforcing laws, delivering public services, protecting rights, and ensuring national security. However, Canada's declining productivity threatens all these responsibilities. If leaders are serious about safeguarding the country's long-term prosperity, they must chart a clear economic path—starting at the top—with mechanisms to hold elected officials to task.

FEARLESS BUT FOCUSED

A per capita GDP target should be bold yet achievable. There is no magic number, but history can inform the possible ranges. During the economic boom of the 1980s, per capita GDP grew at an average annual rate of 2.5%, driven in part by trade liberalisation. This slowed slightly to 2.2% through the 1990s and early 2000s, as the internet age took off up until the onset of the Global Financial Crisis (GFC). The post-GFC recovery saw annual growth of about 1.5% until 2015, after which it tapered to just 0.7% in the years heading in to the pandemic, as resource-sector investments declined and population growth gained steam. Since COVID-19, the average has remained flat, masking annual declines of around -1.5% in the two most recent years, as explosive population growth overwhelmed the numerator.

Setting a 2% per capita GDP growth target would be ambitious. While a short-term rebound is expected as population growth stabilizes and newcomers integrate, medium-term projections suggest growth in this metric would likely settle somewhere around 0.9% over the medium term based on assumptions in our latest economic **outlook**. Achieving sustained 2% growth would only bring Canada back to its pre-pandemic trajectory (2010–2019) by the end of the decade. A 1.5% target—aligned with the post-GFC growth rate from 2010 to 2014—may be more realistic but might fall short of voter expectations.

The economic dividends of a 2% growth target could be significant. Output per capita in 2024 is estimated at $58,700 (2017 dollars). Growth at 2% would translate into an annual and compounding gain of $1,200 in real terms—for a net ~$700 above a base case—per head.[1] Over a four-year mandate, it could translate into an extra $5,000 per person—or $2,600 above the baseline—propelling that metric to $65,000 in inflation-adjusted terms by 2029. It would leave Canada's $2.4 tn economy almost 5% higher over that period relative to business as usual.

A 2% target may not only be ambitious but essential in the event of a prolonged and serious trade war. A severe trade conflict—including 25% tariffs and partial retaliation—could drive per capita output flat to negative over the next two years before recovering at a modest medium-term speed limit of 0.9%, albeit from a lower baseline, leaving **output** about 3.7% lower. An ambitious growth agenda would be crucial to ensuring real income per capita gains stay in the black over the horizon.

STRONGER INVESTMENTS, STRONGER RESULTS

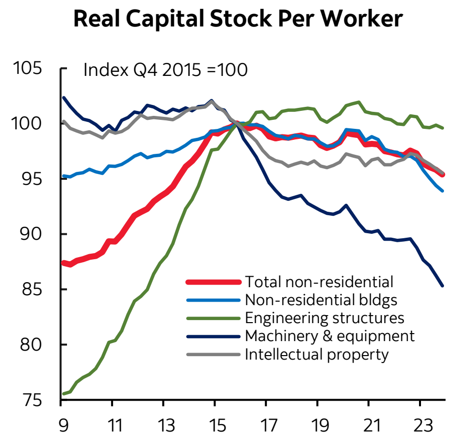
Canada's abysmal productivity performance has been exhaustively documented. While the crisis was declared last year, the trend decline accelerated a decade ago as resource investment pulled back, compounding a longer list of structural challenges. Key factors include burdensome regulations, weak external competitiveness, an outdated tax system, internal trade barriers, and a generally low risk tolerance to cite a few headwinds.

Greater capital investment holds an important key to meaningfully unlocking stronger productivity performance and hence prosperity in Canada. Fundamentally, output per capita is a function of the capital-to-labour ratio and the productivity of those inputs. (A more complete picture would also factor in equilibrium unemployment and participation rates.) Canada has made significant investments in human capital in recent years, from immigration policies to childcare programs, but these efforts have not been matched by equally ambitious capital investments. As a result, capital stock per worker has eroded steadily over the past decade (chart 3).

The scale of investment required to achieve a 2% per capita GDP growth target is massive. As an illustration, increasing the capital stock per worker by 2% annually—a pace consistent with the boom starting in the early 2000s—would require growing the economy's non-residential capital stock from an estimated $2.7 tn today (in 2017 dollars) to $3.0 tn within a four-year mandate (charts 4 & 5). That gap may seem manageable at first glance given real annual non-residential investment has oscillated around $330 bn over the past decade. However, much of this investment simply offsets depreciation, which has averaged $305 bn per year over this period.

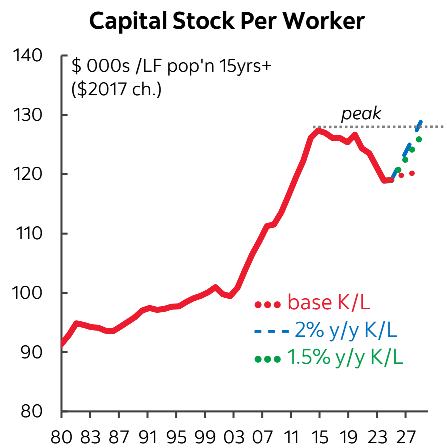
[1] The base case uses assumptions from Scotiabank Economics' February 10th **outlook** while the tariff scenario is based on Scotiabank Economics' November 28th **estimates** (25% tariffs with half-retaliation). For the capital deepening scenarios, the base case is simplistically based on annual stock growth of 1.1% consistent with the pre-pandemic trend, while a historic depreciation rate (12.3%) is used.

Chart 3



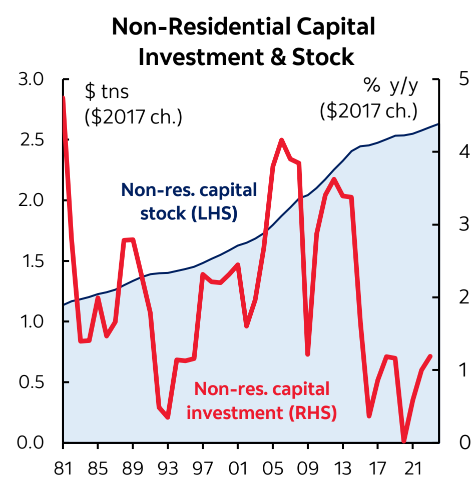
Sources: Scotiabank Economics, Statistics Canada. *(2020 data adjusted to remove pandemic distortions.)*

Chart 4



Sources: Scotiabank Economics, Statistics Canada.
**See Footnote 1 for assumptions.*

Chart 5



Sources: Scotiabank Economics, Statistics Canada.

Annual capital investment would have to be some 15% higher (or average annual growth of an additional ~$60 bn) to be consistent with that pace of capital deepening (chart 6). Over a four-year mandate, incremental investment needs would amount to $250 bn. Even then, reaching 2% real GDP per capita growth would be difficult, given the country's capital share of output sits around 35%. Achieving such results would be contingent on the right conditions for a vigorous response in multifactor productivity (MFP). (A Cobb-Douglas production function dictates that if the growth rates for GDP per capita, population, and capital deepening are fixed, then the necessary MFP growth rate is the residual.) That math alone suggests MFP performance in the order of 1.3% annually, which is likely only possible with accompanying massive structural adjustments on top of this illustrative ramp-up in investment (chart 7).

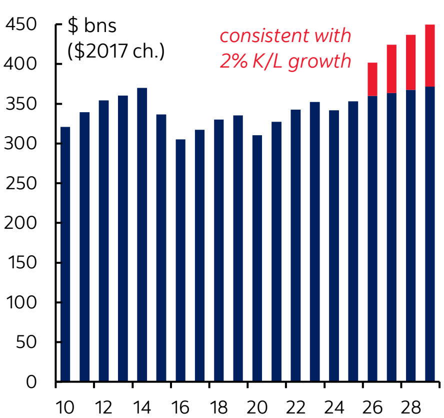
FROM SHOVELS TO SHAREWARE

A productivity-centric agenda would double-down on the sectors that could deliver the biggest gains. Extractive and utility sectors alone hold half of the country's private sector capital stock while transportation & warehousing and manufacturing bring that share to three-quarters. (Governments hold a quarter of *all* stock, public and private [chart 8].) These are also—for the most part—the sectors with highest productivity levels (chart 9).

But the evolution of Canada's capital stock has varied considerably across these outsized performers (chart 10). Investment in transportation & warehousing has surged since the turn of the century at one end of the spectrum, while manufacturing has been hallowed-out at the other end. Strong capital accumulation in the extractive sector has given way to a sharp pullback since 2015, while investment in utilities has stalled over the past decade despite clear need. (We've plotted the construction sector even though it reflects only 2% of private capital stock given it holds a critical key to greater housing supply.)

Chart 6

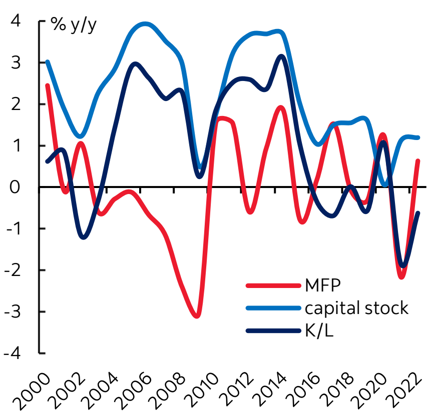
Non-Residential Capital Investment



Sources: Scotiabank Economics, Statistics Canada.
See Footnote 1 for assumptions.

Chart 7

Productivity Growth By Component

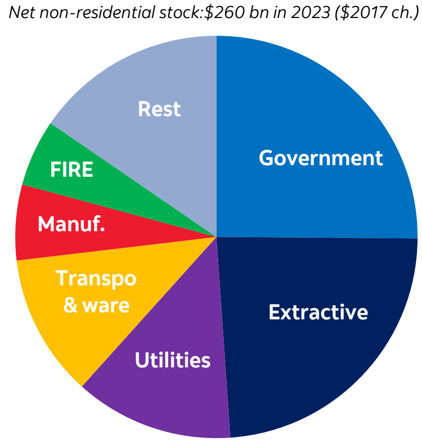


Sources: Scotiabank Economics, Statistics Canada.

Chart 8

Capital Stock by Industry

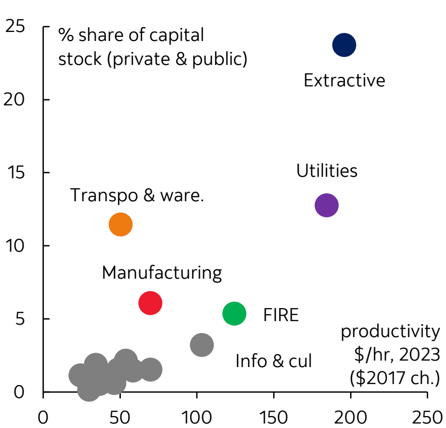
Net non-residential stock:$260 bn in 2023 ($2017 ch.)



Sources: Scotiabank Economics, Statistics Canada.

Chart 9

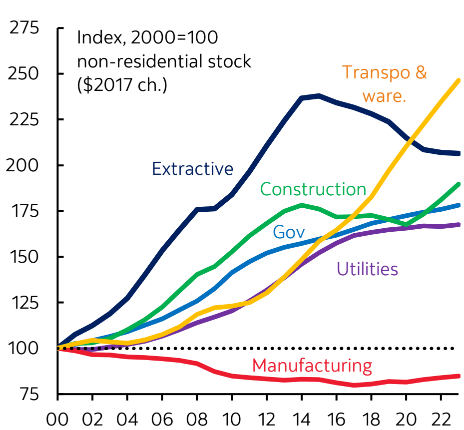
Productivity By Sector



Sources: Scotiabank Economics, Statistics Canada.

Chart 10

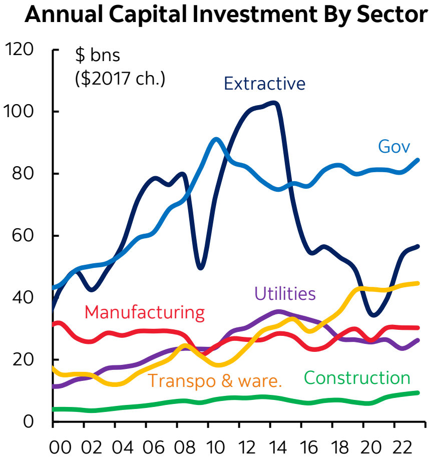
Evolution of Capital Stock



Sources: Scotiabank Economics, Statistics Canada.

Chart 11

Annual Capital Investment By Sector



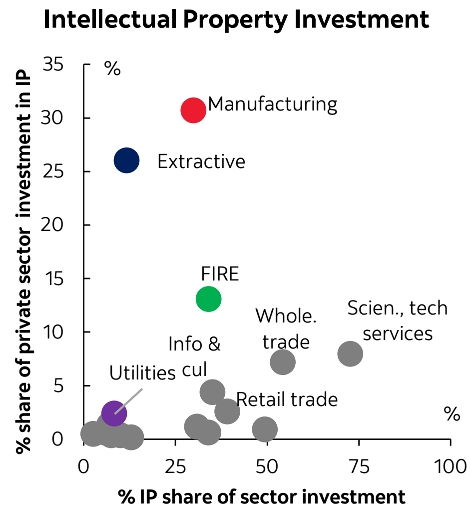
Sources: Scotiabank Economics, Statistics Canada.

February 27, 2025

A path back to prosperity would require large-scale infrastructure investments to ease bottlenecks that limit resource development: port, rail and road capacity, and pipelines to cite a few. Massive investments are also needed in the power generation space, as shortages of electrical capacity will be a meaningful constraint to growth going forward, as recognized by Hydro Québec, for instance (electricity generation has been trending down since the pandemic!). Just raising investment levels to prior peaks in the extractive sector and utilities alone would amount to an incremental $50 bn, while returning government investment to its 2010 peak would bring that tally to almost $70 bn (chart 11).

There has been a lot of lip-service to shifting to an innovation economy, but the bulk of Canada's IP assets still sit within these traditional industries (chart 12). This doesn't negate the critical need to bet on more leaders in the new age economy (and modernising the laggards), but it points to a 'place to start' if Canada wants to make clear inroads on improving productivity and prosperity.

Chart 12

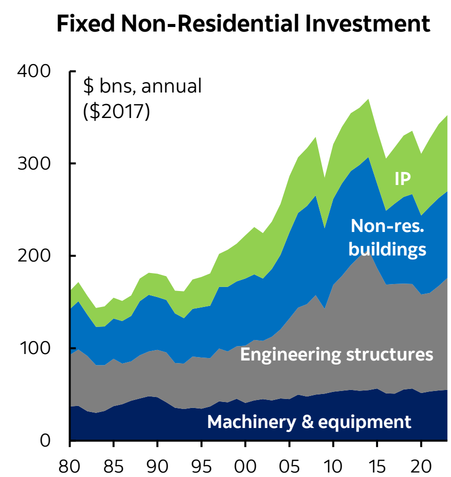


Sources: Scotiabank Economics, Statistics Canada.

CATALYSING ACTION

Unlocking private investment on this scale would likely require substantial public sector incentives. Dismantling non-financial barriers could tip the scale for greater private investment absent public outlays, but abysmal progress to-date is not promising. The government would very likely need to leverage its balance sheet—whether through programs, partnerships or privatization—to incent a stronger private response. For point of reference (and glossing over a huge degree of complexity), the Canada Infrastructure Bank aims to crowd in three dollars of private and institutional investment for each public dollar. Recent industrial subsidy programs had ratios below 1:1. Such ranges could easily put the public investment share of earlier gaps between 0.5–2.5% of GDP annually depending on the nature of the investment and prevailing economic conditions—and of course the efficacy of the tools deployed.

Chart 13



Sources: Scotiabank Economics, Statistics Canada.

There is no single policy fix for Canada's investment shortfall. Past efforts—including investment tax incentives, R&D credits, and capital cost allowances—have had limited macroeconomic impact. Expanding or accelerating these measures could help, but the government may need to take on even more fiscal risk in the short-run to kick start an investment revival. The simple realities are that measures to increase investment take time to bear fruit, if they are successful.

The other reality is that the current uncertainty faced by Canadians in relation to President Trump's economic agenda are paralytic to capital deployment. Finding ways to overcome this uncertainty in the short-run and to make a downpayment on the capital needed to transform our economy in light of an unstable economic relationship with the United States requires unconventional thinking. One approach could be to deeply discount the cost of capital for firms on a temporary basis. Full expensing may be required, particularly in the United States acts on President Trump's desire for this, but that does nothing to overcome uncertainty if those measures are permanent. A firm could always claim that expense at any point in the future when investments are made. A simple, time-limited matching grant that offsets upfront costs for companies, including start-ups, of sufficient scale to have a measurable impact could be a powerful incentive to overcome uncertainty in the short-run. A 25% matching grant focused on machinery, equipment, and intellectual property, for instance, could carry an annual price tag of $60–70 billion, depending on uptake (chart 13). In this way, firms would have, say, 24 months, to take advantage of a historical reduction in the cost of capital. Investments taken beyond that time-frame would revert to normal operating procedures.

Investment-inducing policies could be tweaked and tailored any number of ways, but our back-of-envelope illustrations speak to the scale around which to anchor ambition investment goals—and the expectations that come with them. We are talking potentially percentage—not decimal—points of GDP, when it comes to potential public investment needs.

SWEAT NOW, SHINE LATER

It is not clear what precisely drives under-investment in Canada, and even less clear what to do about it. However, it is evident that low business investment is a shared responsibility between the business community and government. Both must collaborate to scale up investment in Canada, leveraging public finance while enabling the private sector to invest in the most productive areas. This effort must be meaningful in scale, especially as ongoing tariff threats risk further destabilizing Canada's economic trajectory.

The flip side of the coin, Canada needs more investable projects and a stronger investment climate. A predictable and efficient regulatory landscape would help, but the country must also continue the dialogue on potentially narrowing public infrastructure investments gaps with greater (and voluntary) long-term private participation. Additionally, Canada needs a greater appetite for risk, a higher tolerance for (some) failure, and a robust regulatory framework that adjudicates the appropriate balance.

Several reinforcing structural adjustments should be central to any growth agenda—and to all party platforms. It is a now-or-never moment for dismantling internal trade (and non-trade) barriers within Canada. A comprehensive, pro-growth tax review is imperative for any leader serious about economic progress. This should be coupled with a comprehensive transfer review given their central role in redistribution across households, regions, and orders of government. Government must right-size its footprint to crowd in, rather than stifle private sector investment. Moreover, all levels of government should commit to a single-taxpayer doctrine, recognizing that Canada's highly decentralized governance structure is failing to deliver results and hold elected leaders accountable.

The wish-list is much longer and all the more urgent today. It is critical Canada's next leader own the end-goal of protecting Canada's prosperity and chart a credible path to that end. It is Canadians best insurance however policies unfold south of the border.