Economic News

New Stimulus Measures Will Boost Growth but Will Come at a Cost

November 25, 2024

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Highlights

On November 21, the federal government announced that it would be removing the Goods and Services Tax (GST) on qualifying goods for two months starting December 14 (totalling $1.6B) and give Canadians who earned $150,000 or less in 2023 a tax-free rebate of $250 in early Q2 2025 (totalling $4.7B).

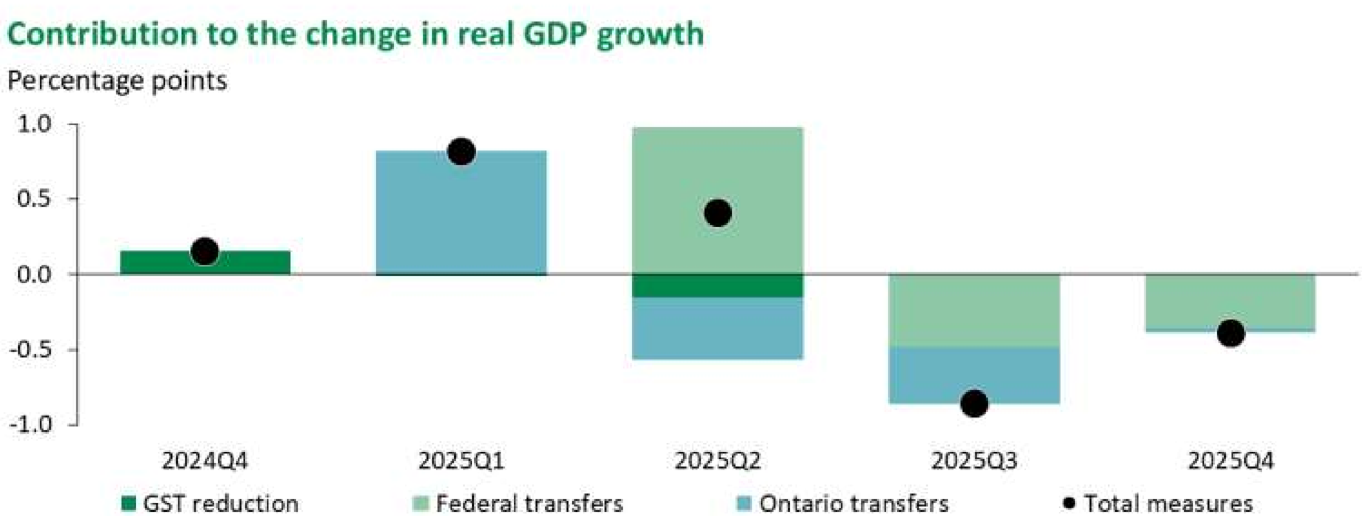
We've determined that these measures, when combined with a similar transfer in Ontario in Q1 2025 (totalling $3.0B), will likely boost real GDP growth by 0.2 percentage points (ppts) in 2025. However, inflation should be less than 0.1 ppts higher next year as a result. And while we think the Bank of Canada will look through this temporary increase in price growth, it will certainty not make the central bank's job any easier.

Implications

The recent federal announcement of $6.3B in new spending this year and next will be welcomed by many Canadian households struggling with the high cost of goods, services and borrowing. But what these measures mean for the economy will differ substantially due to their timing and nature.

Starting with the most immediate measure—the removal of the GST on qualifying goods for two months starting December 14—this should show up disproportionately in the holiday season. During the qualifying period, we assume that as much as half of the $1.6B in tax relief could go out the door in the last few weeks of 2024, with another roughly 30% in January and 20% in February of 2025. While much of this will be spent, a portion will also be saved given all households benefit from the GST vacation regardless of income, and most consumption and saving takes place at the top end of the income distribution. Accounting for these considerations, we've determined that annualized real GDP growth could be 0.3 percentage points (ppts) higher in Q4 2024 because of this measure than in our [November 2024 Economic and Financial Outlook (EFO)](#) (graph 1). In Q1 2025, growth should look a lot like it did in our baseline, and then weaken in Q2 as consumption returns to a more normal pace. Notably, the economic impact of the measure will be felt disproportionately by those provinces with a Harmonized Sales Tax (HST), including Ontario, Newfoundland and Labrador, Nova Scotia, New Brunswick and Prince Edward Island. In Quebec, Finance Minister Eric Girard indicated that the Quebec Sales Tax would not be reduced, unless Ottawa compensated for it.

Graph 1
New Stimulus Will Boost Growth Now but Will Quickly Fade Away



Government of Canada, Government of Ontario, Statistics Canada and Desjardins Economic Studies

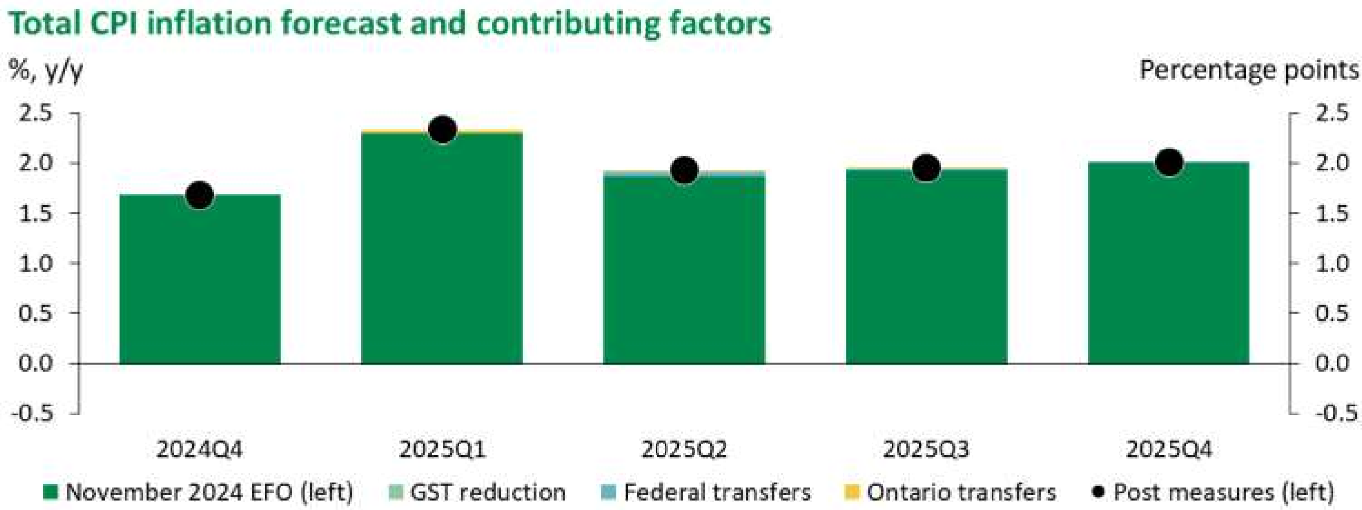
In the case of Ontario, the partial GST holiday in Q1 2025 pales in comparison to the boost consumers will get from the provincial government. It plans to send $200 to every eligible man, woman and child in Ontario early in the new year, with a total cost of about $3B. Given the untargeted nature of this transfer, a portion of it is also likely to be saved. At the national level, this could translate into 0.8 ppts in additional annualized real GDP growth in Q1 2025 relative to our November baseline, but subtract 0.4 ppts in each of the subsequent two quarters as the short-term boost to growth fades (graph 1).

Not to be upstaged, the federal government plans to send out its own tax-free $250 rebate in Q2 2025 to all Canadians who worked in 2023 and had individual net income up to $150,000. Given this measure is more targeted than the two discussed already, t uplift to consumption is likely to be larger on a dollar-for-dollar basis as less will be saved. The recently updated fiscal multipliers from the Parliamentary Budget Officer provide a reasonable guide in this regard. Nationally, this could translate into a boost 1.0 ppts to annualized real GDP growth in Q2 2025 but subtract 0.4 ppts in each of the subsequent two quarters (graph 1).

Putting this all together, real consumption and GDP growth could be much higher in the final quarter of 2024 and the first half of 2025 than projected in our November 2024 EFO. For 2025, annual real GDP growth could be lifted by roughly 0.2 ppts relative to our baseline. Inflation will be higher too, albeit by less than 0.1 ppts, tempered by the mechanical offset from the lower consumption tax (graph 2). With more money chasing a similar amount of goods and services, companies will be able to pass some of their still-high costs on to consumers. The effects could also be more insidious, such as retailers offering less generous Boxing Day discounts. That will offset some of the impact on growth by making the planned fiscal largesse not go as far as it might otherwise. Ontario is likely to bear the brunt of higher inflation among Canadian provinces because of planned spending measures. While we're not currently baking any change in the policy rate path into our outlook as the central bank will likely look through the impact of these temporary measures, they certainly don't help make the case for rates to fall faster.

Graph 2

Inflation Will Be Higher But Not Enough to Concern the Bank of Canada



EFO: Economic and Financial Outlook

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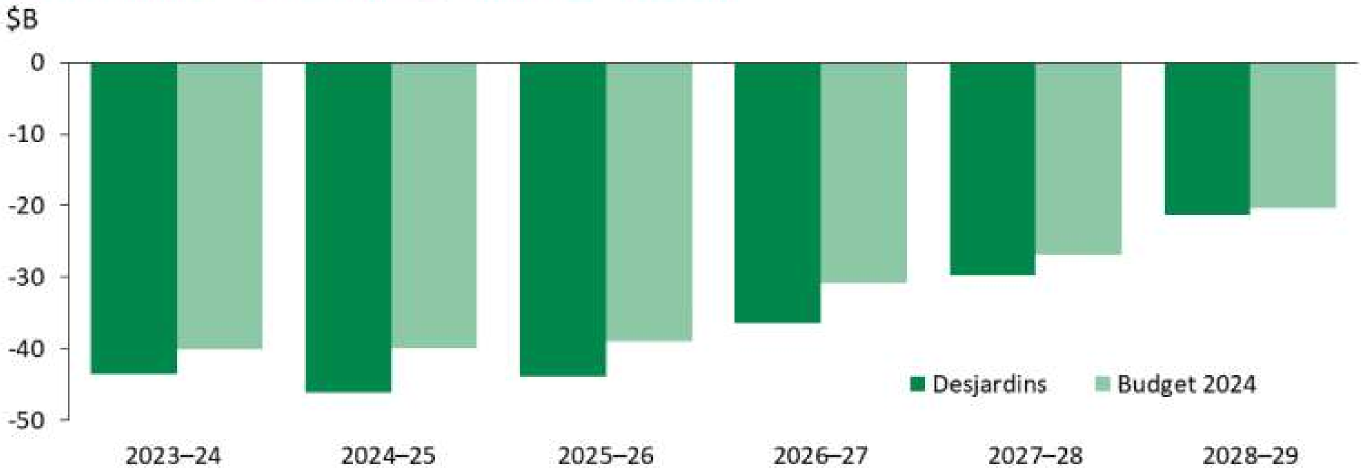
With growth and inflation impacts in hand, the $6.3B question is: what does it mean for the federal government's fiscal forecast? The Government of Canada was already in a challenging financial position. We suspect that the federal government ran a larger deficit last year than they planned, as does the Parliamentary Budget Officer. With this weaker starting point, slower economic growth on reduced population gains and the uncertainty related to the incoming Trump administration stateside, pointed to larger deficits ahead for each year of the outlook. Add to this the new measures announced last week, and it will be extremely difficult for the federal government to stick to its fiscal anchors. Indeed, the federal fiscal outlook looks increasingly adrift (graph 3). There are also adverse fiscal implications for those provinces that participate in the HST, although there are measures in place to mitigate some of that budgetary risk, transferring some or all of it to the federal government.

Graph 3
New Measures Will Lead to Larger Federal Deficits than in Budget 2024

Government of Canada budget balance forecasts



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The economic soundness of these measures is questionable. While many Canadians are struggling financially, these new measures lack the targeted approach of previous initiatives. Earlier similar measures, such as the grocery rebate in 2023, which was means-tested and distributed to recipients of the GST tax credit, or the Canada Child Benefit top-up of 2020, were to reach those most in need. A more focused approach, directing funds to Canadians with a higher propensity to spend would have generated a larger boost, and would have genuinely supported struggling households. Moreover, addressing business competitiveness challenges via investment incentives would be much more constructive for the longer-term outlook than these sugar-rush, yet costly solutions.