# WEEKLY COMMENTARY

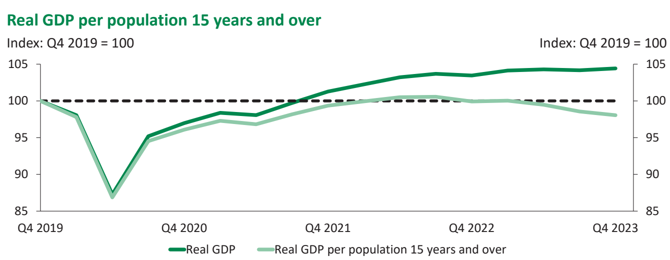
# Will the Upcoming Federal Budget Unlock Productivity Gains?

## By Randall Bartlett, Senior Director of Canadian Economics

Well, it's official. The federal government will publish its 2024 budget on April 16. And given how much notice we have, the budget's contents will no doubt be leaked in dribs and drabs over the coming weeks. As such, we thought it a good opportunity to take stock of the state of the Canadian economy and where it may go from here.

Just over a week ago, Statistics Canada released real GDP for the fourth quarter of 2023. As we pointed out, while the headline came in hotter than expected, the details left us feeling cold. Even more concerning was the weakness in real GDP per capita, which fell for the third consecutive quarter to 2.5% below its recent Q3 2022 peak (graph 1). A persistent drop in this economic indicator typically only takes place during recessions. Much of this weakness can be chalked up to surging population growth, which shows no sign of slowing down.

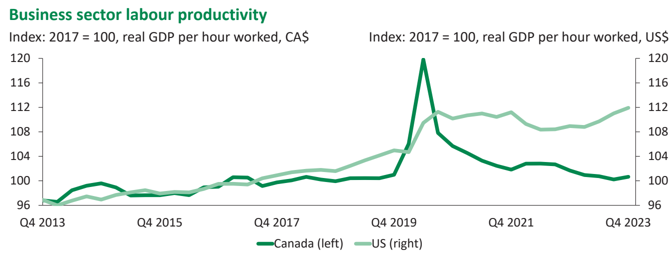
### Graph 1
**Real GDP per Capita Fell Further below the Pre-COVID Level in Q4**




Statistics Canada and Desjardins Economic Studies

The erosion of Canadian living standards is also a reflection of Canada's lacklustre productivity growth. Data released this week showed a minuscule advance in output per hour worked in the final quarter of 2023, but the trend is not the country's friend (graph 2). While productivity may have stopped its five-quarter slide in Q4, it remains below its pre-COVID peak. And the end-of-year uptick may only be a brief reprieve. Contrast this with the US, which has maintained much of its COVID-era productivity gains and has seen growth pick up over the past year.

### Graph 2
**Canada's Labour Productivity Has Been Lagging behind the US's**




Bureau of Economic Analysis, Statistics Canada and Desjardins Economic Studies

The big question for policymakers going into the 2024 federal budget should be: how do we emulate American productivity gains to raise living standards in the Great White North? Some have attributed our productivity penury entirely to immigration, but our problems long precede the recent spike in newcomers to Canada. Our research shows that productivity growth has been in the dumps since 2014, when oil prices took a dive and capital investment in the energy sector slowed to a crawl. No sectors have stepped up to take the baton, leaving productivity to stagnate and living standards to languish.

So why aren't businesses investing? Much like consumers, they are currently facing high interest rates and input costs. And many companies that survived the pandemic emerged highly indebted. The spike in business insolvencies in January 2024—the

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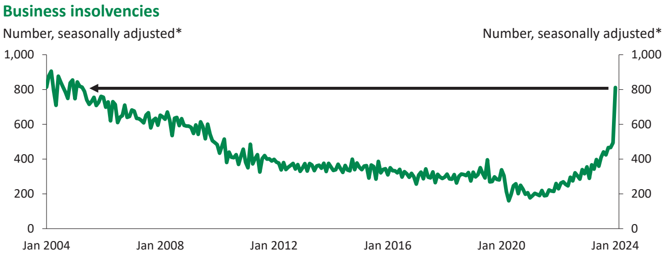
same month as the Canada Emergency Business Account loan repayment deadline—is a clear illustration of these struggles (graph 3). Insufficient domestic demand is also increasingly cited as limiting sales and production growth. And the outlook remains uncertain, with most consumers surveyed telling the Bank of Canada they expect a recession in the next 12 months.

**Graph 3**
**Business Insolvencies Are Higher than during the GFC**




*Seasonally adjusted by Desjardins Economic Studies; GFC: Global Financial Crisis
Innovation, Science and Economic Development Canada and Desjardins Economic Studies

Many of these same survey respondents are also of the view that inflation is being primarily driven by high government spending. This leaves the federal government in a tough spot in the run-up to Budget 2024. It doesn't want to make the Bank of Canada's job harder by opening the taps to even more deficit-financed spending, particularly with inflation slowing and rate cuts on the horizon. At the same time, the federal government is being called upon to address the affordability crisis, increase military spending, expand its nascent pharmacare program … the list goes on. While many of these initiatives may be well-intended, they are likely to do little in the near term to spur renewed business investment and innovation. As such, the federal government would be wise to look south of the border or further afield for inspiration. Otherwise, Budget 2024 risks missing a crucial opportunity to boost Canadian productivity, economic growth and living standards.

# What to Watch For

By Randall Bartlett, Senior Director of Canadian Economics, Tiago Figueiredo, Associate – Macro Strategy, Marc Desormeaux, Principal Economist, Marc-Antoine Dumont, Senior Economist, and Francis Généreux, Principal Economist

## UNITED STATES

TUESDAY March 12 - 8:30

| February | m/m |
|---|---|
| Consensus | 0.4% |
| Desjardins | 0.5% |
| **January** | **0.3%** |

**Consumer price index (February) –** Price growth disappointed in January. The core consumer price index, which strips out food and energy, posted a surprise 0.4% monthly increase. It'll be interesting to see if February brought a more modest gain. Meanwhile higher gasoline prices will certainly have nudged up headline CPI, as prices at the pump were up 4.9% between January and February. However, we think food prices increased less than the 0.4% we saw in January. Core inflation probably ticked down from 0.4% to 0.3% in February. We're anticipating further weakness in used cars and trucks, and goods inflation likely also remained sluggish. Services inflation was particularly strong in January, especially in terms of shelter costs, which were pushed up by methodological quirks. We expect this month's print to be a little weaker. The all items index probably rose 0.5% in February—its biggest jump since August—and from 3.1% to 3.2% year-over-year. Core inflation likely slowed from 3.9% to 3.7%.

THURSDAY March 14 - 8:30

| February | m/m |
|---|---|
| Consensus | 0.7% |
| Desjardins | 0.7% |
| **January** | **-0.8%** |

**Retail sales (February) –** Consumer spending cooled in January. Total retail sales fell 0.8%, the biggest drop since March 2023. However, this underperformance appears to be partly due to much worse weather in January than in December. A milder February bodes well. We're already seeing some positive signs with new motor vehicle sales up almost 6% last month. We also expect gasoline stations to have provided some lift, as pump prices have started to rise again. Preliminary card transaction data for other retail categories is mixed for February and failed to reliably capture January's weakness. Overall, we expect total retail sales to have grown by 0.7%, with sales excluding motor vehicles and gasoline ticking up by 0.3%.

FRIDAY March 15 - 8:30

| February | m/m |
|---|---|
| Consensus | 0.0% |
| Desjardins | 0.3% |
| **January** | **-0.1%** |

**Industrial production (February) –** Once again, the weather was a major factor in January. Industrial production dropped 0.5%, while the mining sector sank 2.3%. However, much colder weather than in December drove up demand for heating, causing energy production to surge by 6%. Most of these impacts are expected to have reversed in February. Milder weather likely brought energy production down and gave the mining sector a boost. February's rebound in manufacturing hours worked, especially in the auto industry, suggests manufacturing output could bounce back strong with a 0.6% monthly gain. Overall, we expect a 0.3% uptick in industrial production.

FRIDAY March 15 - 10:00

| March | Index |
|---|---|
| Consensus | 77.0 |
| Desjardins | 74.5 |
| **February** | **76.9** |

**University of Michigan consumer sentiment index (March, preliminary) –** After two months of strong gains in December and January, the University of Michigan consumer sentiment index fell back in February, primarily due to respondents who provided their information at the end of the month. At 79.6, the preliminary version suggested another gain, but the final reading was revised sharply lower, to 76.9. Aside from the first month of the pandemic, this was the largest downward revision since September 2008, and could suggest further headwinds for March. A lower Conference Board index in February along with higher gasoline prices, March's drop in the TIPP index and weaker stock market performance could all drag the University of Michigan index down further this month.

## CANADA

THURSDAY March 14 - 8:30

| January | m/m |
|---|---|
| Consensus | 0.3% |
| Desjardins | 0.4% |
| **December** | **-0.7%** |

**Manufacturing sales (January) –** Manufacturing sales are expected to have rebounded in January, likely rising by 0.4%, in line with the flash estimate from Statistics Canada. Importantly, the seasonally adjusted Industrial Product Price Index—which is highly correlated with the manufacturing sales price index—dropped by 0.9% in the month. This suggests the already-positive print to start the year could be much larger when expressed in volume terms, helping to provide solid support to January real GDP.

| FRIDAY March 15 - 8:15 | |
|---|---|
| **February** | **m/m** |
| Consensus | 215,000 |
| Desjardins | 220,000 |
| **January** | **224,000** |

**Housing starts (February) –** We expect next Friday's release to show that Canadian housing starts edged lower to 220k (saar) in February 2024. As we've highlighted multiple times before, the fundamentals—from still-high interest rates and borrowing costs to dismal homebuilder confidence to the unavailability of labour—are not supportive of new residential construction. In recent months, building permits have been trending lower. Moreover, homebuilding activity in Ontario and BC now looks to be moderating.

## OVERSEAS

| WEDNESDAY March 13 - 3:00 | |
|---|---|
| **January** | **m/m** |
| Consensus | 0.2% |
| **December** | **-0.1%** |

**United Kingdom: Monthly GDP (January) –** The UK economy had a shaky end to 2023, with real GDP declining 0.1% month-over-month in December and 0.3% on a quarterly basis, pushing the country into a technical recession. However, 2024 likely started on a brighter note. PMIs improved in the first two months of the year, and retail sales surged in January. As a result, monthly GDP probably rose.

# Economic Indicators

## Week of March 11 to 15, 2024

| Day | Time | Indicator | Period | Consensus | Desjardins | Previous reading |
|---|---|---|---|---|---|---|
| **UNITED STATES** | | | | | | |
| MONDAY 11 | --- | --- | | | | |
| TUESDAY 12 | 8:30 | Consumer price index | | | | |
| | | Total (m/m) | Feb. | 0.4% | 0.5% | 0.3% |
| | | Excluding food and energy (m/m) | Feb. | 0.3% | 0.3% | 0.4% |
| | | Total (y/y) | Feb. | 3.1% | 3.2% | 3.1% |
| | | Excluding food and energy (y/y) | Feb. | 3.7% | 3.7% | 3.9% |
| | 14:00 | Federal budget (US$B) | Feb. | n/a | n/a | -21.9 |
| WEDNESDAY 13 | --- | --- | | | | |
| THURSDAY 14 | 8:30 | Initial unemployment claims | March 4–8 | n/a | 218,000 | 217,000 |
| | 8:30 | Producer price index | | | | |
| | | Total (m/m) | Feb. | 0.3% | 0.5% | 0.3% |
| | | Excluding food and energy (m/m) | Feb. | 0.2% | 0.4% | 0.5% |
| | 8:30 | Retail sales | | | | |
| | | Total (m/m) | Feb. | 0.7% | 0.7% | -0.8% |
| | | Excluding automobiles (m/m) | Feb. | 0.5% | 0.4% | -0.6% |
| | 10:00 | Business inventories (m/m) | Jan. | 0.3% | 0.0% | 0.4% |
| FRIDAY 15 | 8:30 | Empire State Manufacturing Index | March | -7.0 | -2.5 | -2.4 |
| | 8:30 | Import prices (m/m) | Feb. | 0.2% | 1.0% | 0.8% |
| | 8:30 | Export prices (m/m) | Feb. | 0.1% | 1.0% | 0.8% |
| | 9:15 | Industrial production (m/m) | Feb. | 0.0% | 0.3% | -0.1% |
| | 9:15 | Production capacity utilization rate | Feb. | 78.4% | 78.6% | 78.5% |
| | 10:00 | University of Michigan consumer sentiment index – preliminary | March | 77.0 | 74.5 | 76.9 |
| **CANADA** | | | | | | |
| MONDAY 11 | --- | --- | | | | |
| TUESDAY 12 | --- | 2024 Quebec budget | | | | |
| WEDNESDAY 13 | 8:30 | National balance sheet | Q4 | | | |
| THURSDAY 14 | 8:30 | Manufacturing sales (m/m) | Jan. | 0.3% | 0.4% | -0.7% |
| FRIDAY 15 | 8:15 | Housing starts (ann. rate) | Feb. | 215,000 | 220,000 | 223,600 |
| | 8:30 | International securities transactions ($B) | Jan. | n/a | n/a | 10.44 |
| | 8:30 | Wholesale trade (m/m) | Jan. | n/a | -0.6% | 0.3% |

Note: Each week, Desjardins Economic Studies takes part in the Bloomberg survey for Canada and the United States. Approximately 15 economists are consulted for the Canadian survey and a hundred or so for the United States. The abbreviations m/m, q/q and y/y correspond to month-over-month, quarter-over-quarter and year-over-year change respectively. Following the quarter, the abbreviations f, s and t correspond to first estimate, second estimate and third estimate respectively. Times shown are Eastern Daylight Time (GMT - 4 hours). Desjardins Economic Studies forecast.

# Economic Indicators

## Week of March 11 to 15, 2024

| Country | Time | Indicator | Period | Consensus m/m (q/q) | Consensus y/y | Previous reading m/m (q/q) | Previous reading y/y |
|---|---|---|---|---|---|---|---|
| **OVERSEAS** | | | | | | | |
| **SUNDAY 10** | | | | | | | |
| Japan | 19:50 | Real GDP – final | Q4 | 0.3% | | -0.1% | |
| **MONDAY 11** | | | | | | | |
| Japan | 19:50 | Producer price index | Feb. | 0.1% | 0.6% | 0.0% | 0.2% |
| **TUESDAY 12** | | | | | | | |
| Germany | 3:00 | Consumer price index – final | Feb. | 0.4% | 2.5% | 0.4% | 2.5% |
| United Kingdom | 3:00 | ILO unemployment rate | Jan. | 3.8% | | 3.8% | |
| **WEDNESDAY 13** | | | | | | | |
| United Kingdom | 3:00 | Monthly GDP | Jan. | 0.2% | | -0.1% | |
| United Kingdom | 3:00 | Trade balance (£M) | Jan. | -3,100 | | -2,603 | |
| United Kingdom | 3:00 | Construction | Jan. | 0.0% | -0.5% | -0.5% | -3.2% |
| United Kingdom | 3:00 | Index of services | Jan. | 0.2% | | -0.1% | |
| United Kingdom | 3:00 | Industrial production | Jan. | 0.0% | 0.7% | 0.6% | 0.6% |
| Eurozone | 6:00 | Industrial production | Jan. | -1.5% | -3.0% | 2.6% | 1.2% |
| **THURSDAY 14** | | | | | | | |
| Germany | --- | Current account (€B) | Jan. | n/a | | 31.4 | |
| **FRIDAY 15** | | | | | | | |
| Japan | 0:00 | Tertiary Industry Activity Index | Jan. | 0.1% | | 0.7% | |
| France | 3:45 | Consumer price index – final | Feb. | 0.8% | 2.9% | 0.8% | 2.9% |
| Italy | 6:00 | Retail sales | Jan. | n/a | n/a | -0.1% | 0.3% |
| Italy | 7:00 | Trade balance (€M) | Jan. | n/a | | 5,614 | |

Note: Unlike release times for US and Canadian economic data, release times for overseas economic data are approximate. Publication dates are provided for information only. The abbreviations m/m, q/q and y/y correspond to month-over-month, quarter-over-quarter and year-over-year change respectively. Times shown are Eastern Daylight Time (GMT - 4 hours).