ECONOMIC VIEWPOINT

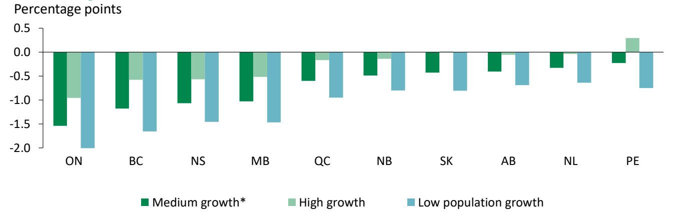
Ottawa's Temporary Migrant Cut Could Dramatically Change the Provinces' Fiscal Destinies

By Marc Desormeaux, Principal Economist

Highlights

- Statistics Canada's latest demographic projections could significantly alter the outlook for economic growth and government budgets across the provinces.
- Ottawa's plan to dramatically cut the non-permanent resident (NPR) population suggests we could soon see Canadian headcount gains fall to a rate previously seen only during the worst of the pandemic when borders were closed. That's a stunning result following the skyrocketing population growth of 2022–24.
- The NPR cut could significantly weigh down GDP and tax revenues in all provinces, with the biggest drags likely to come in Ontario and BC (graph 1). By contrast, Alberta's smaller reliance on NPRs leaves it less vulnerable to the proposed federal policy.
- Theoretically, spending cuts could outstrip the forecast revenue losses and limit the impact on provincial budget balances, but the reality for fiscal policymakers is far more complicated.
- All of this makes fiscal planning exceptionally challenging for provincial governments at this juncture. We hope that the coming months will bring more policy clarity.

Graph 1
New Projections Still Suggest Ontario and BC Will Suffer the Most from the Temporary Resident Cut



* Uses M1 scenario
Statistics Canada, provincial budget documents and Desjardins Economic Studies

Introduction

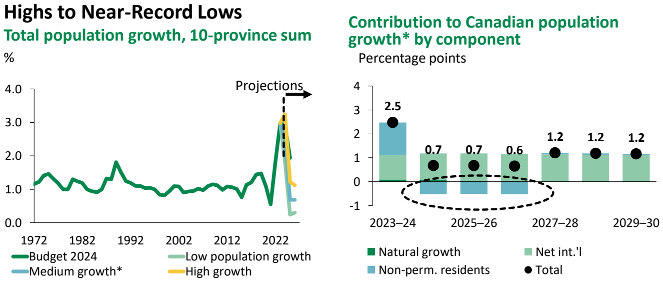
[Ottawa's decision to cut the number of Canada's non-permanent residents](#) to 5% of the total population over the next three years (from 6.2% in 2023) is a significant policy change with huge economic implications. But there is a great deal of uncertainty about the impact. [Continued rapid growth of temporary worker and international student admissions](#) suggests the first reductions may not come until late 2024 or even later, making it more difficult to meet the plan's already-ambitious targets. How provincial governments respond and how the Feds will handle the transition from temporary to permanent workers also make it unclear just how much our population could grow in the next few years.

[Statistics Canada's latest demographic projections](#) have provided some of the clarity that was missing. And in this note, we analyze what they could mean for economic growth and government budgets across the provinces. The new numbers appear to confirm Desjardins Economics' long-held view. The NPR cut will significantly weigh down GDP and tax revenues in all provinces, with the biggest drags likely to come in Ontario and BC. Against that backdrop, the key question heading into fall fiscal update season is how provincial governments could adjust their spending plans to meet their fiscal management objectives.

The Temporary Migration Cut Should Drive Much Weaker Population Growth

By far the biggest takeaway from the new national demographic projections is the extent to which negative net NPR admissions will weigh down population growth. Following historic net inflows in 2023–24, Statistics Canada now foresees record outflows exceeding 210k in each of 2024–25, 2025–26 and 2026–27 in its medium-growth scenarios[1] (with a smaller but still-near-record drag in a more optimistic scenario). That represents a massive shift from the demographic projections on which provincial governments based their latest fiscal plans. Most provinces assumed headcount gains would moderate over the next two years but remain high by historical standards. By contrast, if the new medium-growth population forecasts come to fruition, Canadian headcount gains in the next two years would fall to a rate previously seen only during the peak of the pandemic (graph 2).

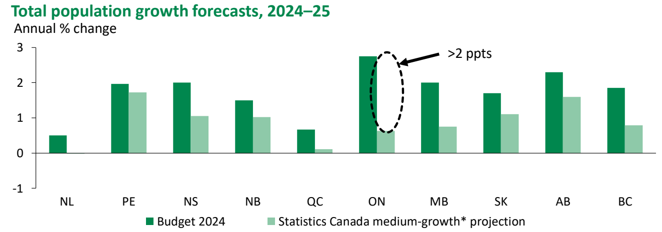
Graph 2
The Temporary Migrant Cut Could Bring Population Growth from Record Highs to Near-Record Lows



* Uses Statistics Canada's M1 scenario
Statistics Canada, provincial budget documents and Desjardins Economic Studies

The data suggest Canada's largest province is the most vulnerable to the effects of potentially much slower population growth (graph 3). Rather than the nearly 3% headcount advance penciled in for 2024–25 in its March 2024 budget, Ontario would see gains of just 0.6% in that period under the new Statistics Canada scenario. That's roughly equal to the pace seen in 2020–21, when pandemic lockdowns hammered immigrant admissions. That said, while the gap between growth rates under the Statistics Canada scenario and provincial government forecasts is greatest in Ontario, all

Graph 3
Population Growth Is Expected to Weaken across the Provinces, but Especially in Ontario

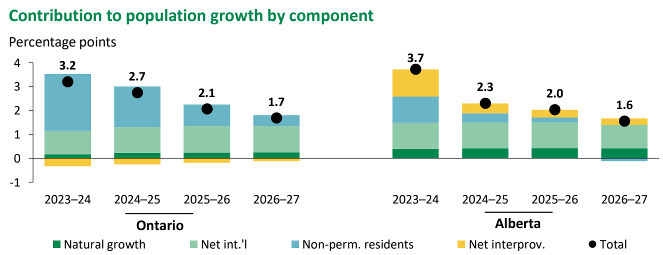


* Uses M1 scenario
Statistics Canada, provincial budget documents and Desjardins Economic Studies

provinces would be impacted. The new projections suggest most provinces would experience weakness not seen in decades. That's a stunning result following the skyrocketing population growth of 2022–24.

As we've argued repeatedly, a province's economic vulnerability is directly related to its reliance on NPRs for population growth. While not every provincial government publishes detailed demographic projections by component, comparing Ontario's and Alberta's most recent forecasts illustrates this point. The summer 2023 projections that underpinned Ontario's 2024 budget assumed that net NPR admissions approaching 300k over the next year would account for over 60% of population growth (graph 4). Statistics Canada's medium-growth scenario for Ontario baked in net outflows of nearly 100k per year for the next three years. By contrast, Alberta's 2024 budget expected NPRs to make up less than 20% of provincial headcount gains in 2024–25. Wild Rose Country's expectations for more balanced population growth leave it less exposed to Ottawa's planned NPR cuts.

Graph 4
The Population Growth Forecasts in Ontario Budget 2024 Rely Heavily on Temporary Migration



Ontario Ministry of Finance, Alberta Treasury Board and Finance and Desjardins Economic Studies

[1] For our base case projection in this report, we use the M1 medium-growth scenario, which is the most commonly employed among analysts. More details on the scenarios can be found here.

GDP and Revenues Should Come in Weaker Than Expected

To assess the economic and fiscal impacts of weaker population growth, we used the fiscal sensitivities published in the 2024 provincial budgets and an analytical framework that links economic activity to the trend level of sustainable long-run output. To account for changes in projected headcount gains, we altered the pool of available labour in each province per the differences between the rates of demographic growth assumed by Statistics Canada and those forecast by the provincial governments. We also adjusted the unemployment and labour force participation rates for each province based on historical trends and immigration status. Factors such as commodity prices and interest rates impact provincial growth trajectories as well, but we did not change them in response to changes in population growth. (See our latest Economic and Financial Outlook for forecasts of these indicators.)

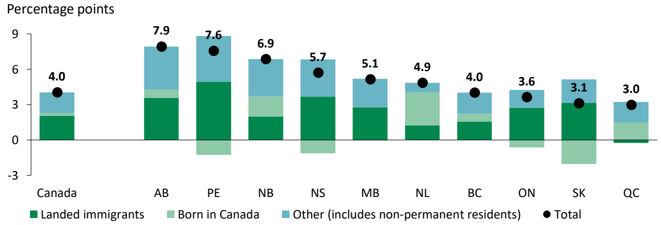
As we would expect, the forecast reductions in output and tax revenues are greatest for the provinces that would see the biggest population growth slowdowns. That means under the medium-growth scenario, Ontario would lead the way with a roughly 1.5 percentage point hit to economic growth (graph 1 on page 1) and more than $1.5B in lost tax revenues in the year ahead. BC would also experience a larger-than-average drag, while the oil-producing provincial economies would prove relatively resilient.

But the longer-run economic effects could potentially be even larger given the role NPRs have played in addressing labour shortages. Our work shows that since the job vacancy rate peaked, immigrants and temporary workers have accounted for nearly all of Canada's job creation. Without an abundance of Canadian-born workers waiting on the sidelines to fill positions left vacant as NPR levels fall, the policy could challenge businesses' ability to meet demand—particularly in sectors like accommodation and food services and retail trade—even if population growth slows. That's true in nearly every province (graph 5).

Graph 5
Newcomers Have Helped Fill Job Vacancies across the Country

Contribution to employment growth by immigration status since June 2022*

Percentage points



* Peak national job vacancy rate
Statistics Canada and Desjardins Economic Studies

The Government Spending Response Is Less Clear

Of course, much weaker population growth also has implications for the spending side of provincial government ledgers. Decades-high headcount gains have prompted provinces—which are responsible for delivering key health and educational services—to invest heavily in new programs and infrastructure. Absent those headcount gains, if governments focused on deficit reduction find themselves bringing in weaker-than-expected tax revenues, some provinces could reasonably be expected to spend less than projected in their 2024 budgets.

What happens to provincial spending plans is anyone's guess at this point, so we simply offer an illustrative scenario here. Government plans will ultimately become clear only in the months ahead as we get more information on how population growth is impacting economic conditions and the political environment. For our part, we assume that population growth tracks the Statistics Canada medium-growth trajectory in fiscal year 2024–25 (FY2025) and that each provincial government maintains the rate of per-person program expenditure forecast for that year in Budget 2024. Such a scenario implies keeping the aggregate quality of public services in line with the most recent government plans. That said, keeping per capita spending consistent with prior targets might prove challenging following a big reduction in NPRs, who are more likely to be of working age and have less significant health care needs.

Under our illustrative scenario, the provinces could collectively reduce planned program spending by about $6.7B in FY2025. For the four largest provinces, aggregate spending reductions of about $6B in the scenario compare to estimated total revenue losses of less than $3B.

While these spending cuts could theoretically outstrip the forecast revenue losses and limit the impact on provincial budget balances, the reality for fiscal policymakers is far more complicated. For one thing, the timing of economic activity (and by extension tax revenue collection) is not the same as it is for delivery of government programs and infrastructure. Sensible plans to adjust spending in response to Ottawa's NPR cut would require much more information about the implementation of a policy about which we have very few details. What's more, spending cuts could have meaningful effects on government sectors like health and education, which as we noted above will also have to grapple with potentially dramatic reductions in the pool of labour they need to provide quality service. These sectors will have to deal with rapid population aging and a wave of retirements in the years ahead as well. Keep in mind too that current government expenditure targets were already restrained as of the end of the 2024 budget season.

Final Thoughts

If demographics are destiny, Canada's fate has become a whole lot fuzzier. Statistics Canada's newest population projections suggest significant revenue and economic hits to all provincial governments, consistent with what we've been saying for some time now. Also in line with previous Desjardins Economics research on the topic, downside risk is particularly acute for provinces whose demographic growth is more reliant on temporary migration. With provincial fall fiscal updates just a few months away, the big question now is how government spending will respond.

Ultimately, at this juncture Ottawa's temporary migration policy presents significant downside risk for provincial coffers, but leaves the provinces with few options to mitigate that risk. That's a major constraint to put on provincial governments. Meaningful hits to tax revenue could come as soon as this fiscal year, and in our federation, provinces are responsible for administering the health and education systems. We hope that the coming months will bring more policy clarity.