

Canada: The economy hit where it hurts

By Matthieu Arseneau, Daren King, Ethan Currie

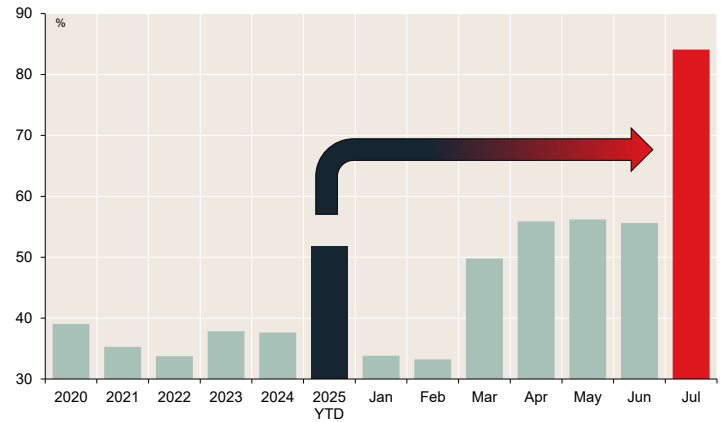
Summary

- Although Canada has been relatively spared by Washington for the time being, based on the tariff rate collected compared to other trading partners, the impact should not be underestimated. These tariffs apply to exports that represent a larger portion of GDP compared to other countries, and some sectors are facing prohibitive customs duties.
- But even more worrisome, the entire Canadian economy is weighed down by uncertainty, with business leaders fearing new measures from the US administration, or even an undesirable outcome to the negotiations to revise the free trade agreement. GDP contracted in the second quarter, with exports and investment falling sharply. The paralysis of businesses is also reflected in the labor market, which continues to deteriorate.
- This economic slowdown has convinced the Bank of Canada that inflation risks are now much lower than they were a few months ago, especially since the government has significantly reduced retaliatory tariffs. The BoC therefore resumed lowering interest rates in September and may do so again in October to give the faltering economy some breathing room. Subsequently, the Bank of Canada will have to adapt its actions to developments in the trade situation, but also to the federal budget in November, which could also stimulate the Canadian economy.
- Against a backdrop of weak population growth, we forecast GDP growth of just 1.2% for 2025 and 2026. This forecast factors in economic weakness that is expected to persist until the end of the year, as well as a potential upturn next year, provided that trade tensions with the United States de-escalate.

Summer is coming to an end and there is complete silence regarding the talks between the Canadian and American governments on the future of their trade relations. Despite this, economic news continues to be dominated by this conflict. Let's try to shed some light on the tariffs imposed by Washington at the time of writing. First, there are tariffs of 10% on energy and potash and 35% (25% before August) on other goods, due to alleged border security issues. Canada also has to contend with the 25% duty on vehicles and auto parts. Added to this are the 50% duties on steel and aluminum, as well as the new 50% duty on copper products imposed on all trading partners. While these multiple duties officially imposed on Canada may seem significant, the reality is less worrying. In fact, the USMCA limits the scope of certain tariffs, particularly those related to security and automobiles. In July, nearly 85% of goods imported by the United States complied with this agreement.

Canada: USMCA registrations soar to record high

Share of U.S. goods imports from Canada registered under USMCA as a share of total, by year / 2025 month

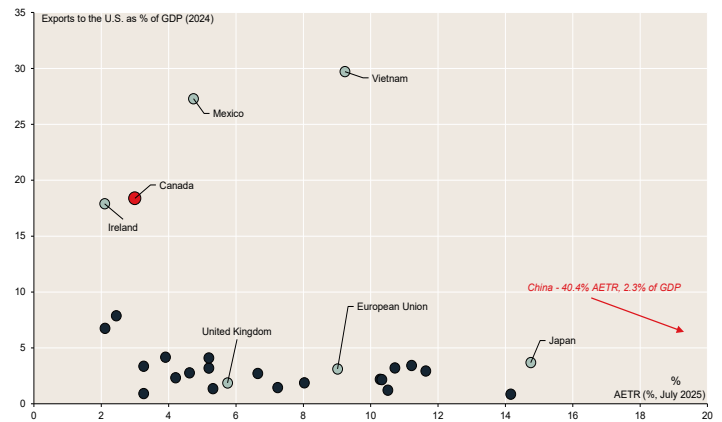


NBC Economics and Strategy (data via U.S. Census Bureau) | Note: 2020 data begins in July

According to our estimates, based on the announced tariffs, the effective rate will not exceed 5% at term, which is well below the 19% imposed on average by Washington on its trading partners. But for now, U.S. customs authorities are unable to collect this amount, probably due to a temporary decline in imports subject to tariffs or administrative delays in their application. The tariffs collected represent only 10.0% of imports, and less than 3.0% for Canada, one of the countries least affected so far. So how is it that the situation is damaging to the Canadian economy? It should be remembered that, even though the effective rate is relatively low, it applies to Canadian exports representing 18% of GDP, one of the highest proportions among the United States' trading partners.

Canada: Minimal tariffs but on a significant portion of the economy

Duties collected / customs import value, by trading partner (July 2025) and exports to the U.S. as a % of GDP



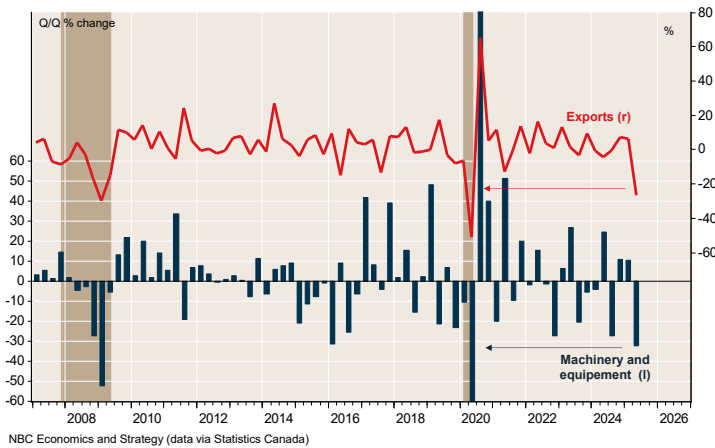
NBC Economics and Strategy (data via Bloomberg)



Certain sectors, such as steel, aluminum, and automotive, are facing prohibitive tariffs, but the economic impact of which extends far beyond these sectors alone. The entire Canadian economy is weighed down by uncertainty, with business leaders fearing new measures from the US administration and even an undesirable outcome to the negotiations to revise the free trade agreement. The Canadian economy recorded its sharpest contraction since the pandemic in the second quarter, with an annualized decline of 1.6%. Not only did exports fall by 27% on an annualized basis, but uncertainty is such that companies have sharply reduced their investment in machinery and equipment, which fell by 33% on an annualized basis, the fourth worst quarterly performance on record.

Canada: Exports and investment severely affected by the trade conflict

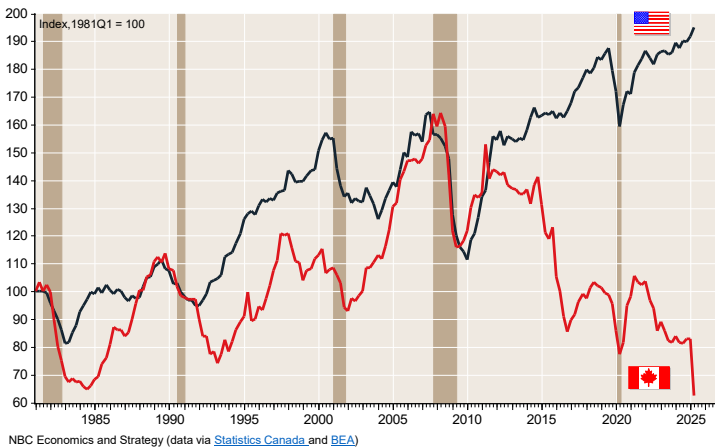
Exports and investment in machinery and equipment (real terms)



Focusing on real investment in industrial machinery and equipment, the decline is even more dramatic, reaching its lowest level since 1981. This decline is all the more worrying as the weakness in investment contrasts with that of the United States and has been Canada's Achilles heel for several years. It has contributed to weak productivity and stagnant living standards since 2015. In recent months, we have expressed our concern about the deindustrialization of the country ([here](#), [here](#), and [here](#)). There is no doubt that Washington's protectionist measures are hitting Canada where it already hurts, as the industrial sector has been battered by excessive regulation and a chronic lack of ambition on the part of successive governments to promote the transformation of our resources. Not so long ago, in 2000, the United Nations ranked Canada 5th in the world for industrial competitiveness. Since then, it has been relegated to 20th place.

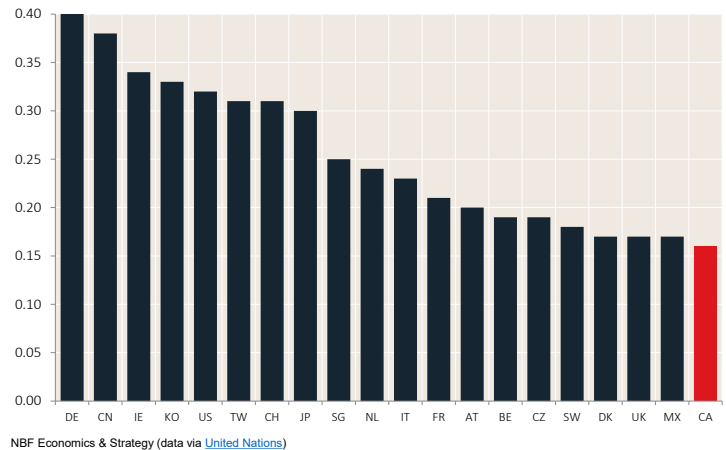
Canada: The implosion of industrial capacity

Investment in industrial machinery and equipment (volumes)



Canada: Once a top 5, now just top 20

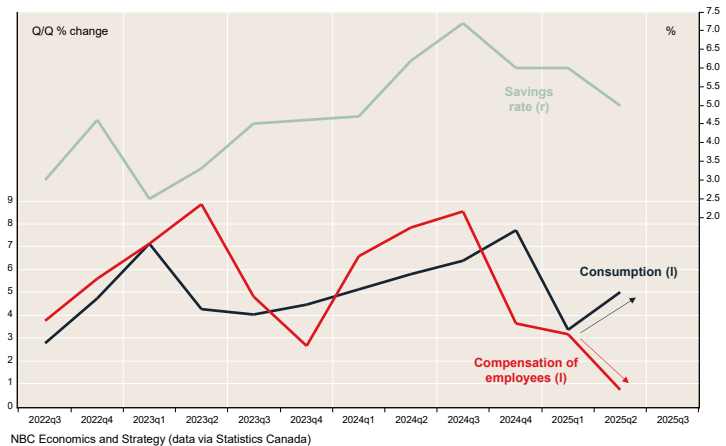
Competitive Industrial Performance Index (CIP): Global ranking as of 2023 for 152 countries



Second-quarter economic performance would have been even worse without the strong performance of consumption, which rose 4.5% on an annualized basis. However, the sustainability of this strength is questionable, as it occurred despite weak growth in employee compensation, which led them to reduce their savings rate for the third consecutive quarter.

Canada: Strong consumption despite weak compensation

Consumption, compensation and savings rate (nominal terms)

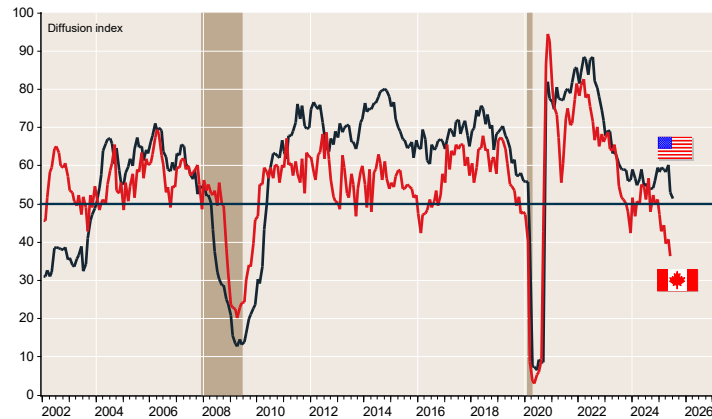


Indeed, the paralysis of businesses is having an impact not only on investment but also on the labor market, which continues to deteriorate. Job losses are not limited to sectors sensitive to trade with the United States. Of the 250 industries in the private sector, only 36% have seen employment rise in the last six months, which is typical only during a recession.



Canada: Labour market weakness is widespread among private sector

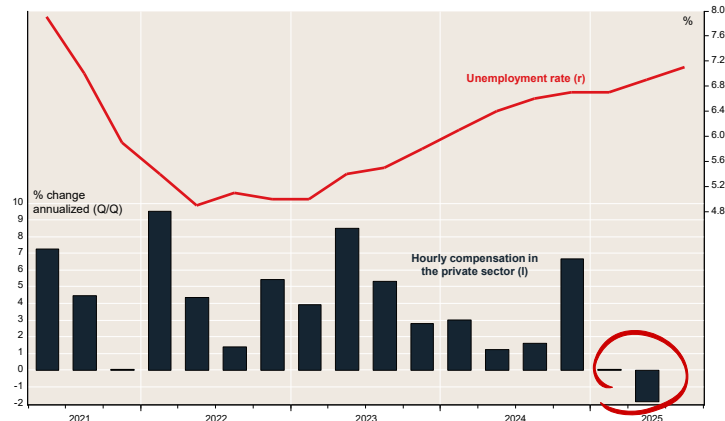
% of sectors showing an increase in jobs over the last 6 months, Canada (250 sectors) and U.S. (251 sectors)



The labor market deteriorated significantly in August, with the unemployment rate now reaching 7.1%, its highest level since August 2021. This increase could have been even greater had it not been for the decline in the labor force participation rate, which limited the damage for the time being. Given the significant increase in the unemployment rate since last February (6.6%), it is not surprising to see a rapid decline in wage pressures in the private sector.

Canada: Wage pressures are fading fast

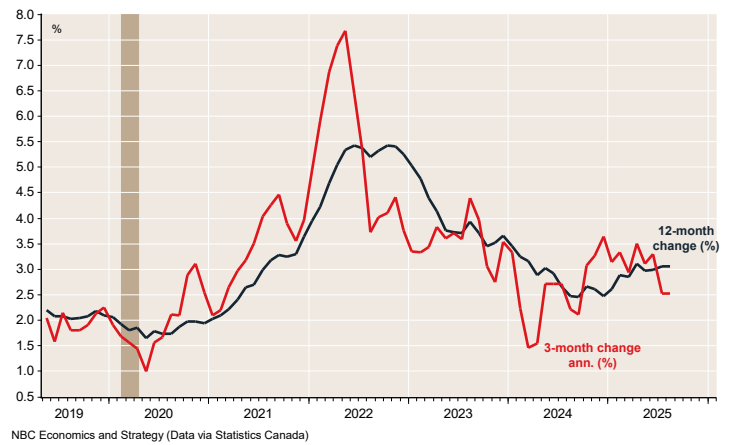
Unemployment rate and hourly compensation in the business sector (productivity account)



This cooling of the economy has convinced the Bank of Canada that inflation risks are now much lower than they were a few months ago, especially since the government has significantly reduced retaliatory tariffs. Core inflation has also slowed recently. The BoC therefore resumed lowering interest rates in September and could do the same in October to give a little breathing room to a faltering economy. This should help ensure that the rebound in residential activity is sustainable and limit the impact of interest payments for many mortgage holders. The Bank of Canada will then have to adapt its actions in line with developments in the trade situation, but also with the federal budget in November, which could also stimulate the Canadian economy. Against a backdrop of weak population growth, we forecast GDP growth of just 1.2% for 2025 and 2026. This forecast factors in economic weakness that is expected to persist until the end of the year, as well as a potential upturn next year, provided that trade tensions with the United States de-escalate.

Canada: Underlying inflation has moderated

Average of Trim-CPI and Median-CPI





Canada economic forecast

(Annual % change)*						Q4/Q4		
	2022	2023	2024	2025	2026	2024	2025	2026
Gross domestic product (2012 \$)	4.2	1.5	1.6	1.2	1.2	2.3	0.4	1.8
Consumption	5.5	1.8	2.4	2.7	1.5	3.5	1.8	1.4
Residential construction	(10.6)	(8.5)	(0.6)	0.7	0.0	1.6	(2.5)	1.2
Business investment	6.4	1.0	(2.4)	(1.5)	1.3	1.3	(2.2)	3.1
Government expenditures	2.6	2.6	4.3	2.6	2.3	5.3	1.8	2.4
Exports	4.2	5.0	0.6	(2.5)	0.1	0.2	(4.3)	1.6
Imports	7.5	0.3	0.7	0.6	1.4	0.1	0.5	1.9
Change in inventories (millions \$)	51,121	25,497	14,284	16,277	16,648
Domestic demand	3.3	1.1	2.1	2.1	1.6	3.6	1.1	1.8
Real disposable income	(0.3)	1.6	4.6	2.1	1.2	4.8	0.9	1.3
Employment	4.1	3.0	1.9	1.3	0.3	1.6	0.6	0.6
Unemployment rate	5.3	5.4	6.4	7.0	7.1	6.7	7.3	7.0
Inflation	6.8	3.9	2.4	2.0	2.1	1.9	2.0	2.2
Before-tax profits	17.9	(14.8)	(3.1)	3.1	1.5	(3.0)	(2.1)	4.2
Current account (bil. \$)	(8.7)	(18.4)	(13.0)	(35.0)	(20.0)

* or as noted

Financial Forecast**

	Current					2024	2025	2026
	9/18/25	Q4 2025	Q1 2026	Q2 2026	Q3 2026			
Overnight rate	2.50	2.25	2.25	2.25	2.25	3.25	2.25	2.50
Prime rate	4.50	4.25	4.25	4.25	4.25	5.25	4.25	4.50
3 month T-Bills	2.43	2.25	2.25	2.25	2.40	3.15	2.25	2.65
Treasury yield curve								
2-Year	2.48	2.40	2.35	2.45	2.60	2.94	2.40	2.65
5-Year	2.74	2.70	2.65	2.80	2.85	2.97	2.70	2.90
10-Year	3.19	3.15	3.15	3.20	3.25	3.24	3.15	3.30
30-Year	3.62	3.60	3.55	3.60	3.65	3.34	3.60	3.65
CAD per USD	1.38	1.37	1.36	1.33	1.32	1.44	1.37	1.30
Oil price (WTI), U.S.\$	64	60	62	63	65	72	60	66

** end of period

Quarterly pattern Canada

	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025	Q1 2026	Q2 2026
	actual	actual	actual	forecast	forecast	forecast	forecast	forecast
Real GDP growth (q/q % chg. saar)	2.4	2.1	2.0	(1.6)	0.5	0.8	1.4	1.8
CPI (y/y % chg.)	2.0	1.9	2.3	1.8	1.9	2.0	1.8	2.2
CPI ex. food and energy (y/y % chg.)	2.5	2.1	2.5	2.6	2.5	2.6	2.3	2.1
Unemployment rate (%)	6.6	6.7	6.6	6.9	7.1	7.3	7.3	7.2

National Bank of Canada



Provincial economic forecast

	2022	2023	2024e	2025f	2026f	2022	2023	2024e	2025f	2026f
	Real GDP (% growth)					Nominal GDP (% growth)				
Newfoundland & Labrador	-1.9	-2.6	2.4	1.4	1.3	6.5	-5.5	3.2	0.8	2.1
Prince Edward Island	4.4	2.2	3.6	1.8	1.1	10.4	4.9	5.8	4.0	3.3
Nova Scotia	3.5	2.0	2.7	1.3	1.1	7.4	8.0	5.0	3.4	3.0
New Brunswick	2.0	1.6	1.8	1.0	0.9	10.4	3.2	4.4	3.7	3.0
Quebec	3.4	0.6	1.3	0.9	1.0	8.7	5.0	5.4	3.6	2.9
Ontario	4.1	1.7	1.4	1.0	1.0	9.4	5.4	5.3	3.5	3.1
Manitoba	4.2	1.7	1.1	1.2	1.1	10.8	4.5	3.3	4.3	2.6
Saskatchewan	7.2	2.3	3.4	1.9	1.8	30.4	-4.8	5.3	4.3	2.1
Alberta	6.0	2.3	2.7	1.8	1.8	24.4	-4.3	5.1	3.1	2.4
British Columbia	4.0	2.4	1.2	1.2	1.3	10.8	3.6	4.0	3.9	3.0
Canada	4.2	1.5	1.6	1.2	1.2	12.4	2.9	4.7	3.5	2.9
	Employment (% growth)					Unemployment rate (%)				
Newfoundland & Labrador	4.0	1.7	2.7	0.0	0.2	11.1	9.8	10.0	10.2	10.3
Prince Edward Island	5.0	6.2	3.6	1.0	0.8	7.7	7.3	7.8	8.1	7.6
Nova Scotia	3.5	2.7	3.1	0.8	0.7	6.6	6.4	6.5	6.5	6.6
New Brunswick	2.9	3.4	2.8	1.0	0.6	7.2	6.6	7.1	7.4	7.5
Quebec	3.1	2.9	0.9	1.6	0.3	4.3	4.4	5.4	6.0	6.1
Ontario	4.8	3.1	1.7	0.9	0.2	5.6	5.6	7.0	7.7	8.0
Manitoba	3.6	2.7	2.6	1.5	0.4	4.5	4.9	5.5	5.9	6.0
Saskatchewan	3.5	1.6	2.6	2.4	0.6	4.6	4.7	5.5	5.1	5.4
Alberta	4.9	3.7	2.9	2.0	0.7	5.8	5.9	7.1	7.6	7.8
British Columbia	3.4	2.6	2.4	1.1	0.3	4.6	5.2	5.6	6.3	6.4
Canada	4.1	3.0	1.9	1.3	0.3	5.3	5.4	6.4	7.0	7.1
	Housing starts (000)					Consumer Price Index (% growth)				
Newfoundland & Labrador	1.5	1.0	1.7	1.5	0.8	6.4	3.3	1.8	1.4	1.9
Prince Edward Island	1.0	0.9	1.2	1.6	0.7	8.9	2.9	1.9	1.5	1.7
Nova Scotia	5.6	7.1	7.4	10.2	7.8	7.5	4.0	2.3	1.8	2.1
New Brunswick	4.6	4.7	6.2	6.6	6.0	7.3	3.5	2.2	1.6	2.0
Quebec	58.5	39.9	48.8	59.6	56.5	6.7	4.5	2.3	2.1	1.6
Ontario	96.0	90.0	74.5	62.5	65.0	6.8	3.8	2.4	2.0	2.2
Manitoba	8.1	7.1	7.2	6.8	7.0	7.9	3.6	1.0	2.4	2.0
Saskatchewan	4.2	4.6	4.3	6.0	5.8	6.6	3.9	1.4	2.1	2.1
Alberta	36.4	35.9	47.8	58.0	55.5	6.5	3.3	2.9	1.9	2.0
British Columbia	46.7	50.6	45.8	45.0	42.0	6.9	4.0	2.6	2.2	2.0
Canada	262.7	241.8	245.1	257.8	247.1	6.8	3.9	2.4	2.0	2.1

e: estimate

f: forecast

Historical data from Statistics Canada and CMHC, National Bank of Canada's forecast.



Economics and Strategy

Subscribe to our publications:

NBC.EconomicsStrategy@nbc.ca

To contact us:

514-879-2529

Stéfane Marion

Chief Economist and Strategist

stefane.marion@nbc.ca

Matthieu Arseneau

Deputy Chief Economist

matthieu.arseneau@nbc.ca

Jocelyn Paquet

Senior Economist

jocelyn.paquet@nbc.ca

Kyle Dahms

Senior Economist

kyle.dahms@nbc.ca

Alexandra Ducharme

Senior Economist

alexandra.ducharme@nbc.ca

Daren King, CFA

Senior Economist

daren.king@nbc.ca

Warren Lovely

Chief Rates and Public Sector Strategist

warren.lovely@nbc.ca

Taylor Schleich

Rates Strategist

taylor.schleich@nbc.ca

Ethan Currie

Senior Associate Analyst

ethan.currie@nbc.ca

Angelo Katsoras

Geopolitical Analyst

angelo.katsoras@nbc.ca

Nathalie Girard

Senior Coordinator

n.girard@nbc.ca

Giuseppe Saltarelli

Desktop Publisher

giuseppe.saltarelli@nbc.ca

General: This Report was prepared by National Bank Financial, Inc. (NBF), (a Canadian investment dealer, member of CIRO), an indirect wholly owned subsidiary of National Bank of Canada. National Bank of Canada is a public company listed on the Toronto Stock Exchange.

The particulars contained herein were obtained from sources which we believe to be reliable but are not guaranteed by us and may be incomplete and may be subject to change without notice. The information is current as of the date of this document. Neither the author nor NBF assumes any obligation to update the information or advise on further developments relating to the topics or securities discussed. The opinions expressed are based upon the author(s) analysis and interpretation of these particulars and are not to be construed as a solicitation or offer to buy or sell the securities mentioned herein, and nothing in this Report constitutes a representation that any investment strategy or recommendation contained herein is suitable or appropriate to a recipient's individual circumstances. In all cases, investors should conduct their own investigation and analysis of such information before taking or omitting to take any action in relation to securities or markets that are analyzed in this Report. The Report alone is not intended to form the basis for an investment decision, or to replace any due diligence or analytical work required by you in making an investment decision.

This Report is for distribution only under such circumstances as may be permitted by applicable law. This Report is not directed at you if NBF or any affiliate distributing this Report is prohibited or restricted by any legislation or regulation in any jurisdiction from making it available to you. You should satisfy yourself before reading it that NBF is permitted to provide this Report to you under relevant legislation and regulations.

National Bank of Canada Financial Markets is a trade name used by National Bank Financial and National Bank of Canada Financial Inc.

Canadian Residents: NBF or its affiliates may engage in any trading strategies described herein for their own account or on a discretionary basis on behalf of certain clients and as market conditions change, may amend or change investment strategy including full and complete divestment. The trading interests of NBF and its affiliates may also be contrary to any opinions expressed in this Report.

NBF or its affiliates often act as financial advisor, agent or underwriter for certain issuers mentioned herein and may receive remuneration for its services. As well NBF and its affiliates and/or their officers, directors, representatives, associates, may have a position in the securities mentioned herein and may make purchases and/or sales of these securities from time to time in the open market or otherwise. NBF and its affiliates may make a market in securities mentioned in this Report. This Report may not be independent of the proprietary interests of NBF and its affiliates.

This Report is not considered a research product under Canadian law and regulation, and consequently is not governed by Canadian rules applicable to the publication and distribution of research Reports, including relevant restrictions or disclosures required to be included in research Reports.

UK Residents: This Report is a marketing document. This Report has not been prepared in accordance with EU legal requirements designed to promote the independence of investment research and it is not subject to any prohibition on dealing ahead of the dissemination of investment research. In respect of the distribution of this Report to UK residents, NBF has approved the contents (including, where necessary, for the purposes of Section 21(1) of the Financial Services and Markets Act 2000). This Report is for information purposes only and does not constitute a personal recommendation, or investment, legal or tax advice. NBF and/or its parent and/or any companies within or affiliates of the National Bank of Canada group and/or any of their directors, officers and employees may have or may have had interests or long or short positions in, and may at any time make purchases and/or sales as principal or agent, or may act or may have acted as market maker in the relevant investments or related investments discussed in this Report, or may act or have acted as investment and/or commercial banker with respect hereto. The value of investments, and the income derived from them, can go down as well as up and you may not get back the amount invested. Past performance is not a guide to future performance. If an investment is denominated in a foreign currency, rates of exchange may have an adverse effect on the value of the investment. Investments which are illiquid may be difficult to sell or realise; it may also be difficult to obtain reliable information about their value or the extent of the risks to which they are exposed. Certain transactions, including those involving futures, swaps, and other derivatives, give rise to substantial risk and are not suitable for all investors. The investments contained in this Report are not available to retail customers and this Report is not for distribution to retail clients (within the meaning of the rules of the Financial Conduct Authority). Persons who are retail clients should not act or rely upon the information in this Report. This Report does not constitute or form part of any offer for sale or subscription of or solicitation of any offer to buy or subscribe for the securities described herein nor shall it or any part of it form the basis of or be relied on in connection with any contract or commitment whatsoever.

This information is only for distribution to Eligible Counterparties and Professional Clients in the United Kingdom within the meaning of the rules of the Financial Conduct Authority. NBF is authorised and regulated by the Financial Conduct Authority and has its registered office at 70 St. Mary Axe, London, EC3A 8BE.

NBF is not authorised by the Prudential Regulation Authority and the Financial Conduct Authority to accept deposits in the United Kingdom.

EU Residents: With respect to the distribution of this report in the member states of the European Union ("EU") and the European Economic Area ("EEA") by NBC Paris, the contents of this report are for information purposes only and do not constitute investment advice, investment research, financial analysis or other forms of general recommendation relating to transactions in financial instruments within the meaning of Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 ("MiFID 2"). This report is intended only for professional investors and eligible counterparties within the meaning of MiFID 2 and its contents have not been reviewed or approved by any EU/EEA authority. NBC Paris is an investment firm authorised by the French Prudential Control and Resolution Authority ("ACPR") to provide investment services in France and has passported its investment services throughout the EU/EEA under the freedom to provide services and has its registered office at 8 avenue Percier, 75008 Paris, France. "NBC Financial Markets, a subsidiary of National Bank of Canada" is a trade name used by NBC Paris S.A.

NBF is not authorised to provide investment services in the EU/EEA.

U.S. Residents: With respect to the distribution of this report in the United States of America, National Bank of Canada Financial Inc. ("NBCFI") which is regulated by the Financial Industry Regulatory Authority (FINRA) and a member of the Securities Investor Protection Corporation (SIPC), an affiliate of NBF, accepts responsibility for its contents, subject to any terms set out above. To make further inquiry related to this report, or to effect any transaction, United States residents should contact their NBCFI registered representative.

This report is not a research report and is intended for Major U.S. Institutional Investors only. This report is not subject to U.S. independence and disclosure standards applicable to research reports.

HK Residents: With respect to the distribution of this report in Hong Kong by NBC Financial Markets Asia Limited ("NBCFMA") which is licensed by the Securities and Futures Commission ("SFC") to conduct Type 1 (dealing in securities) and Type 3 (leveraged foreign exchange trading) regulated activities, the contents of this report are solely for informational purposes. It has not been approved by, reviewed by, verified by or filed with any regulator in Hong Kong. Nothing herein is a recommendation, advice, offer or solicitation to buy or sell a product or service, nor an official confirmation of any transaction. None of the products issuers, NBCFMA or its affiliates or other persons or entities named herein are obliged to notify you of changes to any information and none of the foregoing assume any loss suffered by you in reliance of such information.

The content of this report may contain information about investment products which are not authorized by SFC for offering to the public in Hong Kong and such information will only be available to, those persons who are Professional Investors (as defined in the Securities and Futures Ordinance of Hong Kong ("SFO")). If you are in any doubt as to your status you should consult a financial adviser or contact us. This material is not meant to be marketing materials and is not intended for public distribution. Please note that neither this material nor the product referred to is authorized for sale by SFC. Please refer to product prospectus for full details.

There may be conflicts of interest relating to NBCFMA or its affiliates' businesses. These activities and interests include potential multiple advisory, transactional and financial and other interests in securities and instruments that may be purchased or sold by NBCFMA or its affiliates, or in other investment vehicles which are managed by NBCFMA or its affiliates that may purchase or sell such securities and instruments.

No other entity within the National Bank of Canada group, including National Bank of Canada and National Bank Financial Inc, is licensed or registered with the SFC. Accordingly, such entities and their employees are not permitted and do not intend to: (i) carry on a business in any regulated activity in Hong Kong; (ii) hold themselves out as carrying on a business in any regulated activity in Hong Kong; or (iii) actively market their services to the Hong Kong public.

Copyright: This Report may not be reproduced in whole or in part, or further distributed or published or referred to in any manner whatsoever, nor may the information, opinions or conclusions contained in it be referred to without in each case the prior express written consent of NBF.