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Canadian Federal Election 2015:
Post-Election Economic Landscape

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Election Results: As of writing, the latest results are:

- Liberals 184 seats (39.5% vote) vs 34 seats (18.9% vote) in 2011
- Conservatives 99 seats (31.9%)
- NDP 44 seats (19.7%)
- Bloc Quebecois 10 seats (4.7%)
- Green 1 seat (3.5%)

The resulting Liberal majority was a surprise as the late-campaign polls pointed to a minority. Initial market reaction was muted though, as the risks were tilted toward a more decisive Liberal win. The ruling Conservatives fared worse than the polls suggested and will cede power after almost 10 years at the helm (since January 2006).

With a majority government in place, there is much more clarity on the outlook for policy and certainty that the next election will be at least four years away. The Conservatives are now the official opposition, and won't be able to keep the Liberals from implementing their full platform (Stephen Harper resigned as party leader). Meantime, the NDP lost a significant number of seats, and will likely move to regroup over the coming years.

Market response: Despite the surprise majority result, financial market reaction has been muted so far. The Canadian dollar strengthened 0.1% from yesterday's close to around 76.9 cents ($1.30/US$). However, note that the U.S. dollar itself is broadly weaker overnight and that oil prices are little changed, suggesting the election had little impact on the loonie. Indeed, the Canadian dollar is in the middle of the pack versus the greenback from yesterday's North American close.

In a similar vein, bond yields have nudged up, with 10-year GoCs rising 4 bps to 1.49% and 2s are up 2 bps to 0.54%. But, again, this has largely mirrored the move in Treasury yields, with some slight underperformance in the 10-year space perhaps giving a nod to the increased issuance likely over the next few years.

The Liberal victory does carry some potential implications for various TSX sectors. (Please see the appendix on the outline of the proposed Liberal platform.) Moreover, because the Liberal platform was well advertised and the risk of a majority outcome incorporated, we are unlikely to see big shifts in the days ahead. Still, some broad takeaways or at least areas of focus would be: Infrastructure-related companies (big additional outlays planned), oil & gas (phase out few remaining subsidies, cap-and-trade system), pipelines (supports Keystone and potentially Energy East, but not Northern Gateway), financial services (roll back the TFSA limits, increase allowable frequency of RRSP withdrawals) and telecom (less fractious relations).

Table 1
Summary of Votes and Seats

Federal Election — Canada

	2015		2011	
Political Party	**Votes**	**Seats**	Votes	Seats
Liberals	**39.5**	**184**	18.9	34
Conservatives	**31.9**	**99**	39.6	166
NDP	**19.7**	**44**	30.6	103
Bloc Québécois	**4.7**	**10**	6.0	4
Other	**4.2**	**1**	4.9	1
		338		308

Source: Elections Canada

Economic Implications: By far the most important thrust of the Liberal platform for the medium-term outlook is the proposal to boost the budget deficit to up to $10 billion annually over the next two fiscal years (and then a third deficit of nearly $6 billion in year three, before returning to balance in year four). Note that the fiscal boost is even a bit bigger than $10 billion (or 0.5% of GDP), since finances are assumed to have started in a small surplus over the next two years. For instance, the Liberal plan looks for a budget deficit of $9.5 billion in FY2017/18, but was assuming a starting point of a $2.2 billion surplus, for a net swing of $11.7 billion (close to 0.6% of GDP).

The net measures are roughly evenly split between $5 billion of additional infrastructure spending (itself split between public transit, social and green project) and a wide variety of measures including an enhanced child benefit, spending on the environment, veterans, culture, indigenous peoples, health care and jobs training. Note that new revenue measures (i.e. tax hikes) will almost exactly offset any tax relief measures in the Liberal platform, indicating that any net new fiscal stimulus will almost entirely fall on the spending side of the ledger. The overall thrust of the tax measures is redistribution. From an investor perspective, the concern could be whether the government could in fact begin to rein in the deficit three to four years down the line. After all, it's easy to start spending, but it's much tougher to unwind that spending.

The net fiscal boost—and we can all debate the appropriateness of running deficits—will give at least a short-term lift to economic growth, with most of the impact landing in 2016. We do not believe that there is a significant multiplier effect to fiscal policy in Canada, given the openness of the economy and relatively high taxation rates. At best, the stimulus would lift GDP growth by a bit more than 0.5% next year, so we would be leaning toward annual growth of closer to 2½% in 2016 (versus our current call of just over 2%, and just 1.2% this year), **assuming the proposed measures are fully implemented in the next budget.** However, when/if the spending is reversed it will act as a modest drag on GDP growth.

A firmer underlying GDP growth rate, even if it does prove temporary, would at the margin reduce the chances of further Bank of Canada rate cuts, and indeed could even bring the first rate hike somewhat closer. While we are keeping our rate call unchanged for now (the Bank to stay on hold over the next year, and finally starting to raise rates in early 2017), that may change if the Liberal proposals are soon put in place and, in fact, start boosting growth. In turn, stimulative fiscal policy is generally a short-term positive for a currency (through the channel of leading to a tighter monetary policy than would otherwise be the case). However, we would remain cautious on the Canadian dollar over the near-term due to the following three factors:

1. We remain fundamentally bullish on the U.S. dollar, given the ongoing outperformance of the U.S. economy, and we continue to look for the Fed to begin hiking rates (still possibly by year-end) well ahead of other central banks.
2. Oil prices remain volatile, with no clear direction yet and remain vulnerable to a renewed slide.
3. While stimulative fiscal policy is generally currency-supportive, the nature of the proposed policy is less market-friendly (all spending, slide back into deficit, higher personal taxes).

Beyond the deficit boost and any currency impact, some other important key implications from the Liberal platform include:

- Enhancements to the Canada Pension Plan (CPP) likely means that the proposed new Ontario Retirement Pension Plan (ORPP) will be officially put on ice. Ontario Premier Wynne has already clearly indicated this direction.
- The Trans-Pacific Partnership deal may be in question with Liberal support lukewarm at best.
- Income splitting for families (but not pensioners) will be ended.
- The TFSA limit will be rolled back from $10,000 annually to $5,500.
- The middle income tax cut (reduced from 22% to 20.5% for earnings between $45,000 and $89,000) will be almost exactly offset by the increase in tax rates for those earning above $200,000 (a new upper rate of 33% from 29%).

Big Picture View of Liberal Platform

The Liberal Party ran its campaign on the following platform planks:

Area	Policy
Personal Taxation	Cancel income splitting (not for pensioners)
	Cut personal income tax rate (20.5% from 22%) for incomes between $45k and $89k
	Raise personal income tax rate (33% from 29%) for incomes above $200,000
	Reverse TFSA limit increase
Corporate Taxation	Lower small business rate from 11% to 9%
Families	Replace Universal Child Care Benefit with income-tested tax-free benefit (no benefits if household income > $150k)
	More flexible maternity payments (EI)
Housing	Increase frequency of allowable RRSP withdrawals
Environment	Supports cap-and-trade system, and working with provinces
	Phase out subsidies for fossil fuel
	Subsidies/tax breaks for clean energy
Infrastructure	Additional infrastructure spending of $60 bln over 10 years (roughly $120 bln total)
Gov't Finance	Deficits near $10 bln/yr over next 2 years; nearly $6 bln in FY18/19; balanced budget in FY19/20
Energy/Pipelines	Oppose Northern Gateway, support Keystone XL, unclear on Energy East
Trade	Supports trade deals in principle; TPP subject to consultation
Other	Bring OAS age back to 65 from 67
	Increase CPP contributions/benefits
	EI premiums cut to $1.65 by 2017