Post-Election Economic Landscape

A Publication of BMO Capital Markets Economic Research • Douglas Porter, CFA, Chief Economist, BMO Financial Group

As You Were, Canada

ECONOMIC RESEARCH
economics.bmo.com

Douglas Porter, CFA, Chief Economist
douglas.porter@bmo.com

Robert Kavcic, Senior Economist
robert.kavcic@bmo.com

The incumbent **Liberal government has secured another minority mandate** in Canada's 44th federal election. While the final seat count might still drift around in the coming days as mail-in ballots are counted, the ultimate result is set. At last check, the Liberals were on track (leading or elected) to take 158 seats, almost right in line with the 155 seats held by the party at dissolution (and the 157 won in the 2019 election), leaving them shy of the 170 needed for a majority. So, as for the past two years, they will need to lean on support from another party *(Table 1)*.

The Conservatives are looking at 119 seats (down from 121 in 2019); the Bloc Québécois took 34 (32 in 2019); the NDP holds 25 (24 in 2019); while the Green Party comes away with 2 seats (3 in 2019). Note that the Conservatives should again win the popular vote, with 34.0% support at this point, versus 32.2% for the Liberals. The key takeaway here is that **Canada's political landscape looks remarkably similar after this election to the way it did before**—almost as if Canadians spelled out "we don't want an election now" with their votes.

Table 1
Summary of Votes and Seats
2021 Canadian Federal Election

	2021*		2019	
Political Party	**Votes** (%)	**Seats**	**Votes** (%)	**Seats**
Liberals	32.2	**158**	33.1	**157**
Conservatives	34.0	**119**	34.4	**121**
Bloc Québécois	7.7	**34**	7.7	**32**
NDP	17.7	**25**	15.9	**24**
Green	2.3	**2**	6.5	**3**
PPC	5.1	**0**	1.6	**0**
Other	0.9	**0**	0.8	**0**

Sources: BMO Economics, Elections Canada * as of Sep. 21st, 8:00 am

As usual in a minority situation, there will be plenty of horse-trading ahead of next year's budget, although the Liberals' 2021 document largely set the course for the coming years. The first real sense we will get on that front will be the government's Throne Speech, when it sets out its priorities, and will be treated as a confidence issue.

With another minority mandate in store, we can glean some insights from the campaign proposals of two of the major parties. While any party can theoretically support the Liberals, **the NDP is the likely first choice to step up and deal**, as we have seen pre-election, and because many issues in the two parties' platforms overlap. For example, both parties will look to extend some pandemic-era programs (e.g., wage and rent subsidies); both have clearly prioritized taxing the upper end of the income spectrum and corporations; both are in favour of subsidized child care; agreement should easily be found on housing-related policy; and, neither has any inclination to balance the budget.

For **a more detailed list of major pledges, see the Table on page 5**.

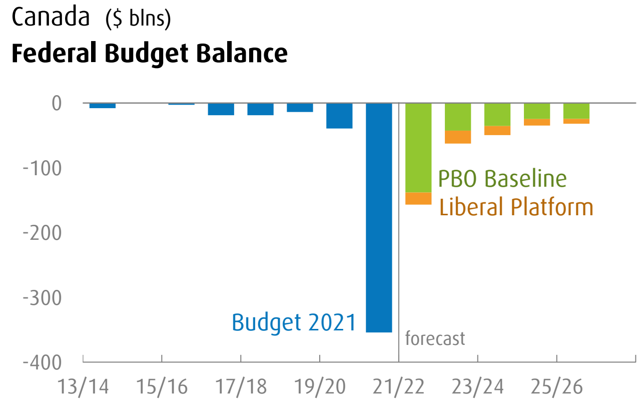
Here are a few of the key implications for the economy, some sectors, and financial markets:

Fiscal Policy

Fiscal policy will likely remain loose under a minority Liberal government. In fact, **the new deficit path will likely look decidedly similar to that laid out in Budget 2021** but, because of better underlying economic and revenue performance, it will also come with increased spending. The Liberal platform laid out a net $12.6 billion in new measures for FY21/22 (roughly 0.5% of GDP), rising to $13.8 billion in FY22/23, before fading gradually to $6.4 billion by FY25/26.

All told, the Budget 2021 deficit projected by the Liberals for FY21/22 sat at $154.7 billion. After the PBO adjusted that baseline to a $138.2 billion shortfall ahead of the election, newly-announced priorities in the Liberal platform pull the deficit back up to $156.9 billion (including a $6 billion contingency). In both the 2021 budget and Liberal platform, the deficit by FY25/26 sat just above $30 billion.

Chart 1
Deficit Path Well Defined



Sources: BMO Economics, PBO, party platforms FY20/21 = estimate

Longer term, **balanced budgets are not a priority**, and a stable debt-to-GDP ratio (after taking a big step up during the pandemic) seems to be the fiscal anchor. Note that, in the Liberal platform, after hitting 51.2% this fiscal year, the ratio falls gradually to 49.2% by FY25/26. As we noted many times pre-pandemic when a 30% debt-to-GDP ratio was the de facto fiscal anchor, it is an anchor that is destined to break during challenging times.

Taxes

The Liberal platform included roughly $4 billion of net tax increases/revenue collection measures by FY22/23, rising to $8 billion by FY25/26. The biggest-ticket items are proposed taxes on large financial institutions, at around $2.5 billion per year. At the same time, expanding the CRA's revenue-collecting ability adds a net $4.6 billion by the latter year of the plan.

Smaller-ticket items in the Liberal plan, such as a minimum tax on higher-income earners and a flipping tax (on homes) carry lower dollar amounts, but are important to signal the party's priorities. In that light, the NDP are openly pushing for taxes on higher-income earners, corporations and an increase in the capital gains inclusion rate. It appears that these are areas that the Liberals potentially may be willing to go in order to garner support. In fact, it's notable that tax changes are an area where the Liberals and NDP see plenty of overlap, and **one could argue that the risk of tax increases is higher in this minority mandate that it was in the last**.

Housing

A Liberal/NDP mandate could see **continued involvement in the housing market**, with an eye on affordability. Non-resident buyers are the first likely target, with the

Budget 2021 vacancy tax taking effect in 2022. That could be supplemented by an outright ban (Liberal platform) and/or transactions tax (NDP platform).

Various other measures to 'improve affordability' are also likely in play. We tend to be skeptical on this front given that such measures usually just increase demand and get capitalized into prices. For example, the Liberals have promised tax-free savings accounts for first-time home buyers, while the NDP seeks to bring back 30-year amortizations for insured mortgages. Additionally, the Liberals have pledged to open the market to more price transparency, as well as implementing a short-term flipping tax.

Longer term, supply is a focus of all parties, but we've been down this road many times. The reality is that Canadian housing starts have averaged nearly 270k annualized units over the past twelve months, or a third more than in the decade leading up to the pandemic. While the federal government can certainly push for affordable housing units, ultimately the pace of new development falls to provincial and municipal jurisdictions, and the economics of owning such properties (especially on the rental side).

Overall Economic Growth

This **election result will not prompt any changes to our growth outlook** for Canada. While the backfilling of fiscal upside with more spending, as per the Liberal platform, means marginally more stimulus for longer, it won't prompt a forecast change given much larger issues at play for the economy, like the Delta variant and supply-side constraints. Interestingly, all major parties ran with promises to boost employment, but most of them push on the demand curve. With more than 700,000 job vacancies as of 2021Q2, it's the supply side that needs the push. We are currently expecting growth to come in at 5.0% this year, before fading next year to a still-strong 4.5%.

Interest Rates and the Canadian Dollar

With no change in the growth outlook expected, and budget deficits likely sticking to the already-telegraphed course, there's little in this election result to alter the interest rate outlook. For the **Bank of Canada**, the broader economic backdrop, completeness of the labour market recovery and percolating inflation pressure remain the biggest factors. At this point, we judge the Bank will continue to taper asset purchases this year, and the stage should be set for rate hikes in the second half of 2022.

For **longer-term yields**, there's little to change the fundamental fiscal picture in Canada, which was already deteriorating before the pandemic. If anything, a Liberal/NDP policy program for a few more years could delay the pace of post-COVID fiscal consolidation, although the market has likely already adapted to that reality. In the meantime, borrowing requirements will continue to fall from last year's pandemic high, and Ottawa's debt-servicing burden remains historically low relative to revenues.

The **Canadian dollar** faded slightly during the course of the election campaign, but the external backdrop was a much bigger factor than the status-quo election result. That is, a generally softening growth forecast and cooler global risk appetite have moved the currency, while oil prices have held relatively steady. We continue to see modest upside for the currency over the next year, as the economic recovery progresses and the Bank of Canada lifts interest rates somewhat ahead of the Federal Reserve. Suffice it to say that, with so many major global cross currents right now, this stable election result is well down the list of factors impacting the loonie.

Equities

Economic growth, interest rates, oil prices and broader market sentiment are still much bigger factors for stocks, but there are a few areas to note. The Liberals promised to raise corporate income taxes on **banks and insurance companies** who earn more than $1 billion per year, and introduce a second temporary levy on these companies. The combined cost is estimated at roughly $2.5 billion per year through FY25/26. It's more than likely that the NDP would support such measures, if not petition for a broader increase in corporate tax rates.

Some **REITs** could also be in focus, with the Liberals pledging to further tax corporate owners of residential property that *"are amassing increasingly large portfolios of Canadian rental housing"*. Details on this front remain vague for now.

A Liberal/NDP government is also a net negative for the **energy sector** versus a Conservative win. But on this front, it is largely status quo, with the Liberals targeting a 40%-to-45% reduction in greenhouse gas emissions (versus 2005 levels) by 2030. The NDP will push harder on this front (50% reduction), while both will look to eliminate subsidies to the oil & gas sector.

Bottom Line

The most significant development from an economic perspective during the election campaign was the broad tilt to increased fiscal spending proposed by almost all major parties. While the specific details need to be ironed out in a minority government, there are clear areas of overlap between the Liberal proposals and the NDP, their most likely dance partner. The extra spending does not move the needle on our growth forecasts, but it does suggest that the pressure will remain firm on the inflation front —that's because the constraint on the economy is on the supply side, and not the demand front.

Table 2
Federal Election 2021: Major Economic Issues

Liberals	NDP	Conservatives
Businesses		
Extend the recovery hiring program to March 31, 2022	Continue existing small business wage and rent subsidies	Paying up to 50% of salary for net new hires for six months after CEWS ends
Extend the wage and rent subsidies to Sept 25, 2021; phase-out began in July	Long-term hiring bonus to pay the employer portion of EI and CPP for new or rehired staff	Loans of up to $200k for SMEs in hospitality, retail, and tourism; up to 25% forgiven
Temporary wage and rent support of up to 75% for tourism industry		
Taxes		
3% digital services tax to start in 2022	Increase the capital gains inclusion rate to 75%	5% investment tax credit for capital investments made in 2022 and 2023
Luxury goods tax	Raise the top marginal tax rate 2 ppts to 35%	25% tax credit on investments up to $100k in small businesses over the next two years
Raise taxes on banks and insurance companies that earn more than $1 bln/year	1% wealth tax for >$10 mln in wealth	15% tax credit for vacation expenses of up to $1k/Canadian for trips in Canada in 2022
Minimum 15% tax on people who qualify for top marginal tax bracket	Raise corporate income tax rate 3 ppts	Sales tax and 3% digital services tax on companies that don't pay tax in Canada
	Taxes on multinational internet companies	1-month GST exemption and dine-in rebate
	Temporary 15% tax on excess profits by large corporations who received the wage subsidy during the pandemic	
Fiscal		
FY22/23 deficit $62.7 bln (PBO)	$48 bln of net new spending over the next 5 yrs; no plan to balance budget	FY22/23 deficit $57.3 bln (PBO)
No plan to balance the budget		Balanced budget still a long-term priority
Health Care		
Funding for virtual care; strengthen federal powers under the Canada Health Act	National pharmacare starting in 2022	Boost annual growth rate of the Canada Health Transfer to at least 6%
Domestic vaccine production in Quebec; free vaccine boosters	Universal dental care	Prioritize COVID booster shots and accelerate homegrown production of vaccines and PPE
	Establish a crown corporation responsible for domestic production of vaccines	
Environment		
Reduce corporate income tax by 50% for manufacture of zero-emission technologies	Reduce emissions by at least 50% from 2005 levels by 2030; maintain carbon tax	Personal Low Carbon Savings Account and a Small Business Low Carbon Savings Account
Reduce emissions to 40%-45% below 2005 levels by 2030	Goal of 100% non-emitting electricity by 2040	Remove the carbon tax backstop system; cap carbon tax at $50/tonne
Interest-free loans for home retrofits	Retrofit all buildings by 2050	Reduce emissions to 30% of 2005 levels by 2030
Transition away from fossil fuel industry with increased emissions caps; end subsidies	End subsidies to oil & gas sector	
Child Care		
Cut child care fees by 50% by the end of 2022	Universal $10/day child care	Create refundable child care tax credit; cover up to 75% of child care costs (income tested)
Universal $10/day child care within five years	Expanded access to EI for parents	Expand Canada Child Benefit and EI benefit
Expanded Canada Caregiver Credit		
Housing		
1% annual vacancy tax on non-resident owners	Build 500k+ units of affordable housing in the next ten years; half within five years	Encourage 1 million homes in the next 3 years
Eliminate blind bidding; open price transparency	20% tax on non-resident foreign buyers	Ban on homebuying by non-residents with a review in two years
Flipping tax on sales within 12-months	Double Home Buyers Tax Credit to $1,500	Encourage 7-to-10-year mortgages
Tax on large residential REITs; assess downpayment requirements for investment property	Re-introduce 30-year terms to CMHC-insured mortgages for first-time homebuyers	Amend the mortgage stress test to improve access for non-permanent employees
Tax-free First Home Savings Account		
Other		
Expanded EI and worker benefit	Targeted student debt forgiveness up to $20k; double Canada Student Grants	Double the Canada Workers Benefit up to a maximum of $2.8k/person or $5k/family
Double Canada Student Grant for two years	Cap cell phone and internet prices	Connect all Canadians to high-speed internet by 2025
Federal minimum wage of $15/hr	Expand sickness benefits from 15 to 50 weeks	
Permanently eliminate interest on Canada Student Loans	Guaranteed basic income	
	Federal minimum wage starting at $15/hr	

Sources: BMO Economics, Federal Budget, party statements

= potential policy overlap

General Disclosures

"BMO Capital Markets" is a trade name used by the BMO Investment Banking Group, which includes the wholesale arm of Bank of Montreal and its subsidiaries BMO Nesbitt Burns Inc., BMO Capital Markets Limited in the U.K., Bank of Montreal Europe Plc in Ireland and BMO Capital Markets Corp. in the U.S. BMO Nesbitt Burns Inc., BMO Capital Markets Limited, Bank of Montreal Europe Plc and BMO Capital Markets Corp are affiliates. BMO does not represent that this document may be lawfully distributed, or that any financial products may be lawfully offered or dealt with, in compliance with any regulatory requirements in other jurisdictions, or pursuant to an exemption available thereunder. This document is directed only at entities or persons in jurisdictions or countries where access to and use of the information is not contrary to local laws or regulations. Their contents have not been reviewed by any regulatory authority. Bank of Montreal or its subsidiaries ("BMO Financial Group") has lending arrangements with, or provide other remunerated services to, many issuers covered by BMO Capital Markets. The opinions, estimates and projections contained in this report are those of BMO Capital Markets as of the date of this report and are subject to change without notice. BMO Capital Markets endeavours to ensure that the contents have been compiled or derived from sources that we believe are reliable and contain information and opinions that are accurate and complete. However, BMO Capital Markets makes no representation or warranty, express or implied, in respect thereof, takes no responsibility for any errors and omissions contained herein and accepts no liability whatsoever for any loss arising from any use of, or reliance on, this report or its contents. Information may be available to BMO Capital Markets or its affiliates that is not reflected in this report. The information in this report is not intended to be used as the primary basis of investment decisions, and because of individual client objectives, should not be construed as advice designed to meet the particular investment needs of any investor. This document is not to be construed as an offer to sell, a solicitation for or an offer to buy, any products or services referenced herein (including, without limitation, any commodities, securities or other financial instruments), nor shall such Information be considered as investment advice or as a recommendation to enter into any transaction. Each investor should consider obtaining independent advice before making any financial decisions. This document is provided for general information only and does not take into account any investor's particular needs, financial status or investment objectives. BMO Capital Markets or its affiliates will buy from or sell to customers the securities of issuers mentioned in this report on a principal basis. BMO Capital Markets or its affiliates, officers, directors or employees have a long or short position in many of the securities discussed herein, related securities or in options, futures or other derivative instruments based thereon. The reader should assume that BMO Capital Markets or its affiliates may have a conflict of interest and should not rely solely on this report in evaluating whether or not to buy or sell securities of issuers discussed herein.

Dissemination of Economic Publications

Our publications are disseminated via email and may also be available via our web site https://economics.bmo.com. Please contact your BMO Financial Group Representative for more information.

Additional Matters

This report is directed only at entities or persons in jurisdictions or countries where access to and use of the information is not contrary to local laws or regulations. Its contents have not been reviewed by any regulatory authority. BMO Capital Markets does not represent that this report may be lawfully distributed or that any financial products may be lawfully offered or dealt with, in compliance with regulatory requirements in other jurisdictions, or pursuant to an exemption available thereunder.

To Australian residents: BMO Capital Markets Limited is exempt from the requirement to hold an Australian financial services licence under the Corporations Act and is regulated by the UK Financial Conduct Authority under UK laws, which differ from Australian laws. This document is only intended for wholesale clients (as defined in the Corporations Act 2001) and Eligible Counterparties or Professional Clients (as defined in Annex II to MiFID II).

To Canadian Residents: BMO Nesbitt Burns Inc. furnishes this report to Canadian residents and accepts responsibility for the contents herein subject to the terms set out above. Any Canadian person wishing to effect transactions in any of the securities included in this report should do so through BMO Nesbitt Burns Inc.

To U.K./E.U. Residents: In the UK, Bank of Montreal London Branch is authorised and regulated by the Prudential Regulation Authority and the Financial Conduct Authority ("FCA") and BMO Capital Markets Limited is authorised and regulated by the FCA. The contents hereof are intended solely for clients which satisfy the criteria for classification as either a "professional client" or an "eligible counterparty", each as defined in Directive 2014/65/EU ("MiFID II"). Any U.K. person wishing to effect transactions in any security discussed herein should do so through Bank of Montreal, London Branch or BMO Capital Markets Limited; any person in the E.U. wishing to effect transactions in any security discussed herein should do so through BMO Capital Markets Limited. In the UK this document is published by BMO Capital Markets Limited which is authorised and regulated by the Financial Conduct Authority. The contents hereof are intended solely for the use of, and may only be issued or passed on to, (I) persons who have professional experience in matters relating to investments falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the "Order") or (II) high net worth entities falling within Article 49(2)(a) to (d) of the Order (all such persons together referred to as "relevant persons"). The contents hereof are not intended for the use of and may not be issued or passed on to retail clients.In an E.U. Member State this document is issued and distributed by Bank of Montreal Europe plc which is authorised and regulated in Ireland and operates in the E.U. on a passported basis. This document is only intended for Eligible Counterparties or Professional Clients, as defined in Annex II to "Markets in Financial Instruments Directive" 2014/65/EU ("MiFID II").

To Hong Kong Residents: This document is issued and distributed in Hong Kong by Bank of Montreal ("BMO"). BMO is an authorized institution under the Banking Ordinance (Chapter 155 of the Laws of Hong Kong) and a registered institution with the Securities and Futures Commission (CE No. AAK809) under the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong). This material has not been reviewed or approved by any regulatory authority in Hong Kong. Accordingly the material must not be issued, circulated or distributed in Hong Kong other than (1) except for "structured products" as defined in the Securities and Futures Ordinance, in circumstances which do not constitute it as a "Prospectus" as defined in the Companies Ordinance or which do not constitute an offer to the public within the meaning of that Ordinance, or (2) to Professional investors as defined in the Securities and Futures Ordinance and the Securities and Futures (Professional Investor) Rules made thereunder. Unless permitted by the securities laws of Hong Kong, no person may issue in Hong Kong, or have in its possession for issue in Hong Kong this material or any other advertisement, invitation or document relating to the products other than to a professional investor as defined the Securities and Futures Ordinance and the Securities and Futures (Professional Investor) Rules.

To Korean Residents: This material is not provided to make a recommendation for specific Korean residents to enter into a contract for trading financial investment instruments, for investment advising, for discretionary investment, or for a trust, nor does it constitute advertisement of any financial business or financial investment instruments towards Korean residents. The material is not provided as advice on the value of financial investment instruments or any investment decision for specific Korean residents. The provision of the material does not constitute engaging in the foreign exchange business or foreign exchange brokerage business regulated under the Foreign Exchange Transactions Act of Korea.

To PRC Residents: This material does not constitute an offer to sell or the solicitation of an offer to buy any financial products in the People's Republic of China (excluding Hong Kong, Macau and Taiwan, the "PRC"). BMO and its affiliates do not represent that this material may be lawfully distributed, or that any financial products may be lawfully offered, in compliance with any applicable registration or other requirements in the PRC, or pursuant to an exemption available thereunder, or assume any responsibility for facilitating any such distribution or offering. This material may not be distributed or published in the PRC, except under circumstances that will result in compliance with any applicable laws and regulations.

Singapore Residents: This document has not been registered as a prospectus with the Monetary Authority of Singapore and the material does not constitute an offer or sale, solicitation or invitation for subscription or purchase of any shares or financial products in Singapore. Accordingly, BMO and its affiliates do not represent that this document and any other materials produced in connection therewith may lawfully be circulated or distributed, whether directly or indirectly, to persons in Singapore. This document and the material do not and are not intended to constitute the provision of financial advisory services, whether directly or indirectly, to persons in Singapore. This document and any information contained in this report shall not be disclosed to any other person. If you are not an accredited investor, please disregard this report. BMO Singapore Branch does not accept legal responsibility for the contents of the report. In Asia, Bank of Montreal is licensed to conduct banking and financial services in Hong Kong and Singapore. Certain products and services referred to in this document are designed specifically for certain categories of investors in a number of different countries and regions. Such products and services would only be offered to these investors in those countries and regions in accordance with applicable laws and regulations. The Information is directed only at persons in jurisdictions where access to and use of such information is lawful.

To Thai Residents: The contents hereof are intended solely for the use of persons qualified as Institutional Investors according to Notification of the Securities and Exchange Commission No. GorKor. 11/2547 Re: Characteristics of Advice which are not deemed as Conducting Derivatives Advisory Services dated 23 January 2004 (as amended). BMO and its affiliates do not represent that the material may be lawfully distributed, or that any financial products may be lawfully offered, in compliance with any regulatory requirements in Thailand, or pursuant to an exemption available under any applicable laws and regulations.

To U.S. Residents: BMO Capital Markets Corp. furnishes this report to U.S. residents and accepts responsibility for the contents herein, except to the extent that it refers to securities of Bank of Montreal.

These documents are provided to you on the express understanding that they must be held in complete confidence and not republished, retransmitted, distributed, disclosed, or otherwise made available, in whole or in part, directly or indirectly, in hard or soft copy, through any means, to any person, except with the prior written consent of BMO Capital Markets.

ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST

BMO Financial Group (NYSE, TSX: BMO) is an integrated financial services provider offering a range of retail banking, wealth management, and investment and corporate banking products. BMO serves Canadian retail clients through BMO Bank of Montreal and BMO Nesbitt Burns. In the United States, personal and commercial banking clients are served by BMO Harris Bank N.A., (Member FDIC). Investment and corporate banking services are provided in Canada and the US through BMO Capital Markets.

BMO Capital Markets is a trade name used by BMO Financial Group for the wholesale banking businesses of Bank of Montreal, BMO Harris Bank N.A. (member FDIC), Bank of Montreal Europe p.l.c, and Bank of Montreal (China) Co. Ltd, the institutional broker dealer business of BMO Capital Markets Corp. (Member FINRA and SIPC) and the agency broker dealer business of Clearpool Execution Services, LLC (Member FINRA and SIPC) in the U.S., and the institutional broker dealer businesses of BMO Nesbitt Burns Inc. (Member Investment Industry Regulatory Organization of Canada and Member Canadian Investor Protection Fund) in Canada and Asia, Bank of Montreal Europe p.l.c. (authorised and regulated by the Central Bank of Ireland) in Europe and BMO Capital Markets Limited (authorised and regulated by the Financial Conduct Authority) in the UK and Australia.

A member of BMO Financial Group