PRE-BUDGET ANALYSIS

Five issues to watch for in the 2026 federal budget

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Some 19 months into its mandate and with a new budgetary cycle in place, on November 5th, Prime Minister Mark Carney's majority government will table its second budget. This budget comes at a time of heightened uncertainty and volatility caused by an escalating trade conflict, growing geo-political tensions, rising inflation, AI bubble concerns and now interest rate hikes. In addition, the Carney government will now have to deal with a separatist government in Quebec, reassure Albertans about the value of staying in the federation and genuinely engage Canada's Indigenous communities in a meaningful and constructive dialogue. The challenge facing the Prime Minister and his government is immense, but it also presents a unique opportunity to set a path for future economic prosperity and to become a global leader.

By most accounts, the Carney government has embraced the enormous challenge, calling it a generational challenge, and has set out an ambitious agenda as evidenced by its Mandate Letter and the 2025 Federal Budget. A laser focussed approach on economic issues has earned the government the support of senior business and other influential leaders. While many have applauded the Carney government for thinking big and differently, the optimism is somewhat guarded as questions remain about the government's capacity to execute as well as the implications of a rapidly changing and deteriorating global environment.

As government budgets go, second budgets are typically an opportunity for new or returning, governments to fine-tune its priorities and overall strategy (pivot where necessary), recalibrate its fiscal plan to reflect changing economic forecasts, spending pressures and consider new revenue options; and start shifting towards execution.

Governments also want to demonstrate some immediate changes (the so-called 100-day commitment pledges) as well as showing progress on bigger initiatives. While the Carney government is barely at the mid-point of its mandate, it is a bit too early to fully assess its performance on the major commitments but examining whether it is headed in the right direction is of value.

Against the backdrop of the 2025 Federal Budget, 2026 Spring Economic Update and key developments that have occurred since then, here are five key issues to watch for.

1 Facing strong economic headwinds while building the strongest economy in G7

Given Canada's poor economic record over the past couple of decades marked by sluggish economic growth, declining private sector investment and low productivity, one of the top priorities of the Carney government has been to build the strongest economy in the G7. The government has noted that Canada starts from a position of strength and needs to better leverage its world-class talent, abundant natural resources, comprehensive free-trade agreements and stable environment including the rule of law.

Table 1 · Economic growth forecasts 2025 to 2027 for G7 countries

Country & Institution	2025	2026	2027
United States			
IMF (October 2026)	2.3	2.3	2.3
OECD (September 2026)	2.1	2.2	2.1
Germany			
IMF	0.2	1.3	1.1
OECD	0.3	1.1	1.1
France			
IMF	0.9	0.4	0.7
OECD	0.9	0.4	0.7
United Kingdom			
IMF	1.2	1.3	1.2
OECD	1.3	1.1	1.0
Japan			
IMF	1.2	0.7	0.7
OECD	1.2	0.8	0.7
Italy			
IMF	0.5	0.8	0.6
OECD	0.5	0.9	0.6
Canada			
IMF	**1.9**	**1.1**	**1.7**
OECD	**1.9**	**0.9**	**1.3**

Sources: IMF, World Economic Outlook, October 2026 and OECD Economic Outlook, September 2026.

In the 2026 Spring Economic Update, the government highlighted that Canada is projected to have the second fastest-growing G7 economy behind the United States.

Since that update, the trade conflict with the U.S. has escalated including the imposition of additional punitive tariffs, and geo-political tensions have worsened with the Iran war creating bottlenecks in the Strait of Hormuz impacting the supply of key commodities like energy and fertilizers giving rise to inflation and higher interest rates. Based on the latest IMF and OECD economic growth forecasts (Table 1), Canada's real GDP growth for 2026 has dropped from 1.5% to about 1%. While overall global economic growth has been downgraded, Canada has now slipped to having the 4th fastest growing economy in 2026 within the G7.



The more concerning trend is Canada's medium term economic growth especially over the next five years. According to several economic forecasts (Table 2), while Canada's economic growth is expected to bounce back in 2027 and beyond, it is projected to grow at a rate of less than 2% suggesting that it will continue to under-perform and will unlikely meet the government's ambitious goal.

Canada's economy has proven to be resilient in recent years having avoided a recession. What remains unclear is whether the government's investment-led strategy will fill the gap in economic growth or if the government will need to take further actions in hopes of achieving the desired goal of being the strongest economy in the G7.

Table 2 · Comparison of Canada's real GDP growth projections (%) – 2026 to 2029–31

Institution	2026	2027	2028	2029-31
Parliamentary Budget Office	0.9	1.5	1.7	1.8
Finance Canada (2026 Spring Economic Update)	1.1	1.9	1.9	-
Bank of Canada (July 2026 Monetary Policy Report)	0.7	1.8	1.8	-
IMF (October 2026 World Economic Outlook)	1.1	1.7	1.7	1.7
OECD (September 2026 Economic Outlook)	0.9	1.3	-	-
RBC Economics	1.0	1.6	-	-
C.D. Howe	0.6	0.8	1.3	1.8

Sources: Parliamentary Budget Office, Economic Forecast Outlook, October 2026, RBC Economic, Monthly Forecast Update, October 2026 and C.D. Howe.

2 Will investors make a big bet on Canada and can Canada deliver?

At the core of Carney's economic strategy, is the commitment to catalyze $1T in investment to build nation-building infrastructure and resource development projects.

To that end, the government has introduced Bill 39, *Building Canada Strong Act* and created the Major Projects Office (MPO).

In addition, the government established the Canada Strong Fund (Canada's Sovereign Wealth Fund) and held its first Investment Summit in Toronto in September 2026. Following the Summit, the government announced that it had secured nearly $500B in new investment commitments to Canada.

While early indications are that the government is having some success in attracting investment from institutional and private investors, maintaining this momentum will be critical given the competitive global investment environment.

The federal government has reported that some 18 projects have been referred to the MPO across several sectors including mining and critical minerals, energy and transportation infrastructure. The big challenge for the government will be the effectiveness of the expedited review process and managing the different interests including having meaningful engagement with Indigenous communities. If these delicate relationships are not managed properly, it could derail the whole initiative. As several observers have noted, the execution risk is high.

Finally, large scale projects like infrastructure and resource development projects that are being contemplated by the federal government are complex and often tend to be over-budget and subject to delay. As the Parliamentary Budget Office (PBO) highlighted, the Trans Mountain Pipeline project ended up costing $34B, more than six times the initial private sector estimate. Moreover, a recent study indicated that Canada is among the most expensive jurisdictions within OECD countries to build new transit projects. The federal government will need to put into place appropriate mechanisms and guardrails to avoid such cost overruns and reputational risk.

3 From unprecedented trade agreements to sustainable trade diversification

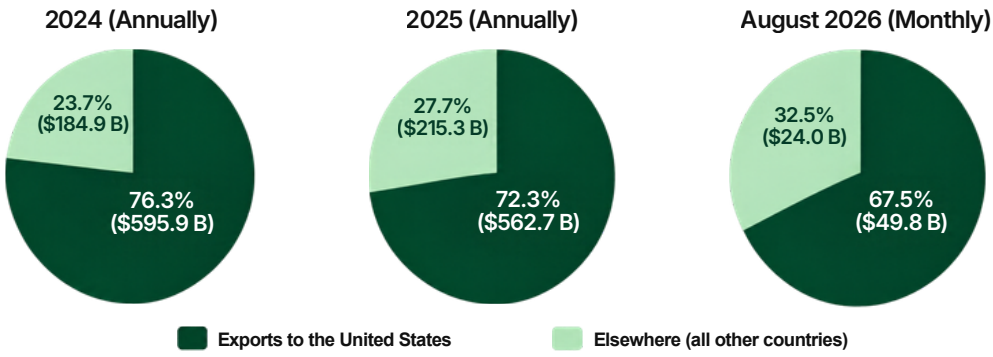
Even before the start of the second term of the Trump administration, Canada had the most free-trade agreements in the world. It was also the only country with comprehensive free-trade agreements with all of the G7 countries. Following the imposition of the illegal and unjustified tariffs by the U.S., Prime Minister Carney has doubled down on building stronger trade relationships with like-minded partners and has signed more than 20 new deals including most recently the enhanced alliance with the European Union. While having such trade agreements and access to global markets is important, the real value is derived from leveraging them.

In Budget 2025, the government set out a goal of doubling non-U.S. exports by an additional $300B by 2035, proposing to end the over-reliance on U.S. trade and shifting from "trade dependency to trade resilience". Recent data suggests that the shift to increased non-U.S. trade has started with some 32.5% of Canadian exports in August 2026 going to non-U.S. markets compared to 23.7% in 2024 (Figure 1).

Given Canada's long trade history with the U.S. including the highly regarded Canada-U.S.-Mexico Free-Trade Agreement and its geographical proximity, diversifying to other export markets has proven to be challenging for most Canadian businesses with the exception of a few large corporations. In particular, Canada's small and medium-sized enterprises have struggled to find new customers in other parts of the world making them even more vulnerable during the recent trade tension with the U.S. To address some of the challenges, the federal government has launched various programs within the Business Development Bank of Canada and the Export Development Corporation to assist SMEs with the transition. Some have argued that these programs are insufficient, and with the Finance Minister dropping hints in recent days, we will have to wait and see what additional measures the government will introduce to support SMEs to weather the impact of the punishing tariffs and to seek out new markets.

Figure 1 · Canadian merchandise exports by destination, 2024–2026

Share of total exports



Source: Statistics Canada, Tables 12-10-0171-01 and 12-10-0176-01.

Other trade matters to watch for in Budget 2026 will be the federal government's assessment and positioning on what progress has been made on eliminating interprovincial trade barriers. After some intense attention several months ago and some bold commitments, the issue seems to have disappeared from the radar of political leaders. Given that removing interprovincial trade barriers has an estimated benefit of up to $200B, representing some 4 per cent of our GDP, the federal government should be inclined to continue to encourage provinces and territories to eliminate these unnecessary regulatory barriers.

Despite the recent news that U.S. and Canadian trade representatives are now back at the negotiating table working towards a new deal, the federal government will want to re-emphasize the imperative of trade diversification.

4 Making prudent investments without compromising fiscal sustainability

In recent weeks and months, we have seen governments around the world under pressure to address an impending fiscal crisis. This has added to the volatility in the global markets and led to unrest in the streets of major international cities. Relative to its G7 peers, Canada's fiscal position is considerably better as it has one of the lowest net debt-to-GDP ratios in the G7. However, this single indicator does not fully capture the scope of the challenge facing the federal government.

Since taking office, the Carney government has introduced numerous major programs and initiatives with substantial costs. While it can be argued that these investments are necessary and justified in light of the trade conflict with the United States, the growing risk to Canada's sovereignty and the need to fast track critical infrastructure and resource development projects to boost Canada's economic growth and productivity, the question remains how will Canada finance all the new priority spending?

Table 3 · Comparison of PBO fiscal outlook (October 2026) with Finance Canada 2026 spring economic update (April 2026)

	2025–26	2026–27	2027–28	2028–29	2029–30	2030–31
Revenues ($B)	$511.1	$538.7	$554.0	$570.9	$587.9	$610.1
Expenses ($B)	$578.7	$602.0	$624.2	$635.0	$655.9	$677.9
Budgetary Balance – Deficit ($B)						
– PBO	($67.6)	($63.3)	($70.2)	($64.2)	($67.9)	($67.8)
– SEU	($66.9)	($65.3)	($63.1)	($57.7)	($56.2)	($53.2)
Public Debt Charges ($B)	$53.6	$59.3	$65.0	$71.1	$76.6	$83.0
Federal Debt ($B)	$1,334.3	$1,397.6	$1,467.7	$1,531.9	$1,599.8	$1,667.6
Federal Debt as a % of GDP	41.1	40.8	41.4	41.9	42.4	42.6

Source: Parliamentary Budget Office, Economic and Fiscal Outlook, October 2026.

In Budget 2025, the federal government committed to undertake a Comprehensive Expenditure Review aimed at reducing duplication and inefficiencies, and generating savings of $60B over the next five years. Some have argued that the government didn't go far enough in its restraint plan and should have pursued a rigorous Program Review exercise like the one implemented by former Federal Finance Minister, Paul Martin, in 1995. In the absence of further spending reductions and new revenue sources, the government will have to largely rely on debt-financing to fund the new initiatives, and this can have significant implications. According to PBO, the federal government's deficit will be between $63B and $70B annually over the next 5 years, and the debt-servicing costs (public debt charges) will be the fastest growing spending program increasing from $59.3B in 2026-2027 to $83B in 2030-31, which represents a 40% increase (see Table 3).

Furthermore, the PBO points out that the federal government will not meet one of its two fiscal anchors announced in Budget 2025, namely maintaining a declining debt-to-GDP ratio. The significance of this fiscal anchor is highlighted by the IMF, which has noted that it would, "strengthen discipline, transparency and credibility preserving fiscal space for high-return investment".

5 Growing calls for comprehensive tax reform

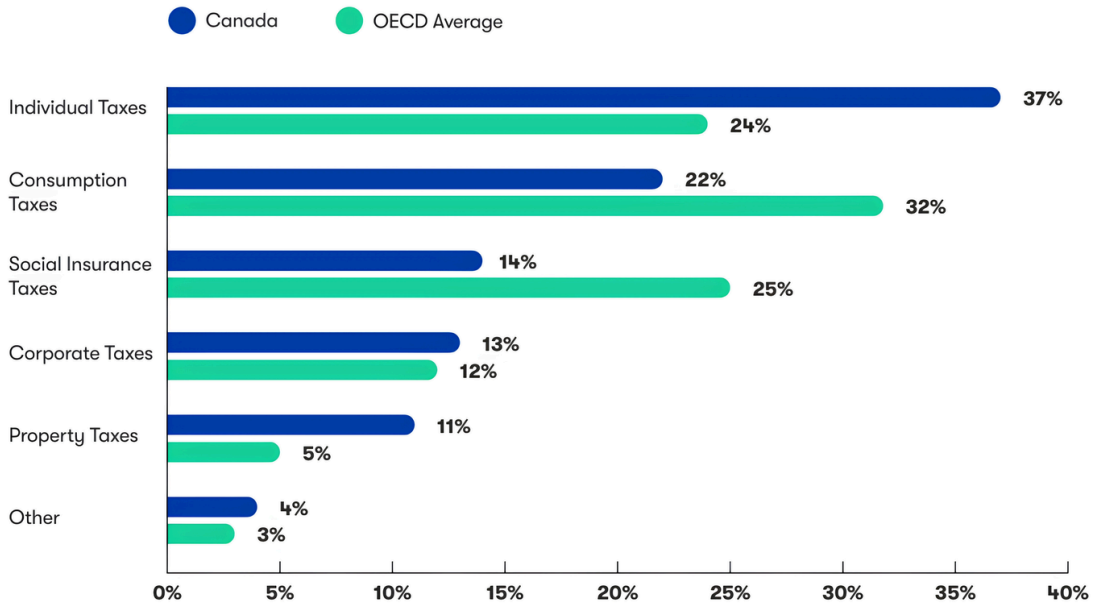
Among Prime Minister Carney's first set of decisions after being elected in April 2025 were the cancellation of the proposed capital gains exemption changes and the consumer carbon tax. In Budget 2025, the government announced the Productivity Super Deduction and subsequently expanded it, creating the Productivity Mega Deduction which was announced at the inaugural Investment Summit in Toronto in September 2025.

An important thing to watch for in the Budget 2026 will be whether the federal government reports on the progress it has made on the Comprehensive Expenditure Review and the targeted savings and whether it is contemplating any new revenue sources. While all of these tax measures have been widely endorsed by the business community, there is growing pressure on the government to overhaul Canada's dated tax system rather than introducing what has been described as "half-measures and piecemeal reforms" that don't optimize economic growth.

Several prominent organizations including the CPA, KPMG, major banks and the C.D. Howe Institute as well as the House of Commons Standing Committee on Finance have called on the government to establish a panel or commission to conduct a comprehensive review of Canada's tax system. It has been six decades since the tax system was comprehensively reviewed by the Royal Commission on Taxation in 1962, led by Kenneth Carter (commonly referred to as the Carter Commission). Arguably, much has changed since then, including the structure of our economy.



Figure 2 · Sources of all government revenue in Canada and the OECD average, 2022

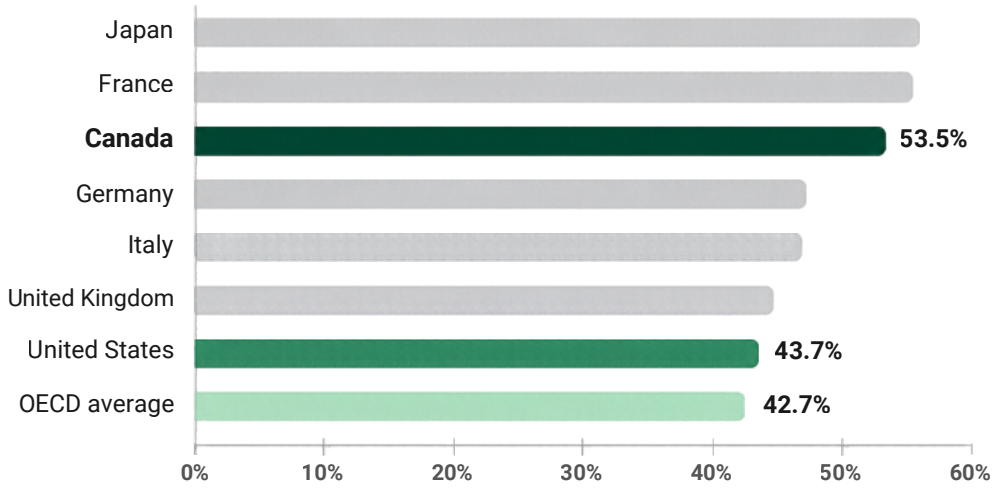


Source: Tax Reform for Growth in Canada Report, October 2025. Page 18. Chartered Professional Accountants of Ontario © 2025, CPA Canada. All rights reserved.

Proponents of tax reform point out that various aspects of personal income tax, corporate income taxes, capital gains taxes and tax credits need to be changed to create a more competitive economy that attracts critical capital and talent. One particular issue that is gaining increasing attention is the need to rebalance the tax mix in line with other OECD countries by shifting more of the burden to consumption taxes rather than income taxes. As Figure 2 illustrates, Canada disproportionately relies on individual taxes, rather than consumption taxes, compared to the OECD average. Furthermore, Canada has one of the highest top combined marginal income tax rates among OECD countries, approximately 10% higher than the United States and the OECD. This significant gap adversely impacts Canada's ability to recruit and retain top talent (see Figure 3).

According to one study, a doubling of the GST to 10% could generate enough income to reduce personal income taxes by 25%. While the federal government is unlikely to move that far, this does demonstrate the enormous value of the GST consumption tax. It is worth noting that although consumption taxes (like raising the GST and provincial sales taxes) can be regressive, in that everyone regardless of income pays the same rate, the impact on lower-income individuals and families can be mitigated through targeted GST tax credits.

Figure 3 · Top combined marginal income tax rates in G7 countries and OECD average, 2024



Source: OECD Data Explorer, 2024.

Final Comment

Budget 2026 is unlikely to have many surprises given that the federal government has already rolled out several new major initiatives since the Budget 2025 and 2026 Spring Economic Update. In recent days, Finance Minister, Francois-Philippe Champagne has disclosed that the budget will be entitled "Masters of Our Destiny – Maîtres Chez Nous" and will build on the government's focus on investment and productivity with targeted initiatives for small and medium-sized businesses. The government will likely profile its affordability measures with some possible enhancements and lay out its new immigration plan. As is usually the case, the government's projected budgetary deficits and debt will receive lots of attention and will likely be closer to the estimates presented in the PBO's October 2026 Economic and Fiscal Outlook.

What remains to be seen is whether the federal government broadens its Comprehensive Expenditure Review to generate a higher quantum of savings that can be reallocated to new priorities, and if the government heeds to the calls of various organizations and the recommendations of the House of Commons Standing Committee on Finance to undertake a comprehensive review of the tax system.

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