Scotiabank

GLOBAL ECONOMICS

INSIGHTS & VIEWS

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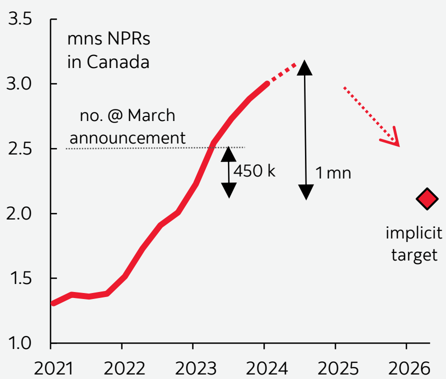
Chart 1

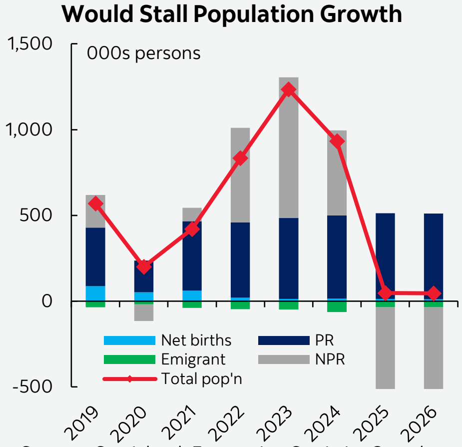
Non-Permanent Residents in Canada Yet to Peak



Sources: Scotiabank Economics, Statistics Canada, IRCC.

Chart 2

Meeting the NPR Target Would Stall Population Growth



Sources: Scotiabank Economics, Statistics Canada.

Closed for Business? Confusion Reigns

CANADA NEEDS CREDIBLE IMMIGRATION ANCHORS

- **Canada's federal immigration minister is set to announce annual immigration targets on November 1st. The rolling 3-year plan could signal softer permanent resident (PR) targets ahead, but most attention will focus on first-time targets for temporary residents.**
- **Expect hard-to-interpret numbers as *gross* new issuance targets will necessarily embed an army of assumptions that will make it guess-work arriving at implications for top-line population growth, let alone its composition.**
- **Since the last annual plan, the federal government has announced a series of well-intentioned changes to stem unsustainable population growth including caps on student visas, changes to temporary foreign worker programs, and an overarching attrition target for non-permanent residents (NPR) in the country (i.e., to 5% of the total population by 2026). But the suite of measures don't yet add up.**
- **Population growth is decelerating modestly—and to be fair some policies are only just taking effect—but the government is now *further* away from its NPR target than when it was set last March (chart 1). And the runway is that much shorter.**
- **The 5% NPR attrition target is no longer reasonably achievable. It would effectively translate into annual *net* NPR outflows in the order of half-a-million over the next two years. Current PR targets would offset this, but the net effect could completely stall population growth (chart 2).**
- **It could also translate into contraction of Canada's labour force in the order of 1% over the next two years—and almost 20% of NPRs currently in the labour force—with a potentially commensurate impact on output levels absent a productivity response. Dealing with a sudden drop in the number of workers could pose a substantial challenge to businesses.**
- **With about 40% of Canada's temporary workforce participating in highly productive parts of the economy, it is not evident there would be an immediate productivity offset. Too many distortions and too much decentralization under current gatekeeping policies give little confidence that labour force attrition would be achieved in an orderly fashion with long-term welfare (i.e., productivity) front and centre.**
- **Scotiabank Economics earlier estimated that the productivity-neutral rate of population growth likely sits in the order of 350 k (or 0.85%) annually absent an immigration system with a greater focus on potential, coupled with a substantial ramp-up in business investment. The risk now is over-correcting on the numbers and underwhelming on potential.**
- **In reality, without robust systems to incent or even track outflows, there is a material risk that aggressive adherence to the target would put further pressure on asylum claims, exacerbate already-stretched adjudication systems, and inevitably drive up undocumented persons in the country.**
- **The government has weaved a complicated web. Policymakers must now not only address its backward-looking bind, but also double-down on the forward-looking objective of improving Canadians' welfare over time. Addressing the former, but not the latter risks going from bad to worse.**

THE BEST LAID PLANS

Canada's federal immigration minister will table annual immigration targets on November 1st. This rolling three-year plan has traditionally set out planned permanent resident admissions including notional numbers across categories of admission. Last year's outlook scaled the headline number to 485 k for 2024, then leveled off at 500 k in 2025 and 2026. Economic immigrants would comprise 58% of the target, families nearing 24%, and humanitarian streams the balance (18%) in 2024 (chart 3). There was to be a modest rotation towards a greater economic share over the horizon (to 60% by 2026).

The immigration landscape has changed markedly since those plans were tabled. Explosive population growth—notably among non-permanent categories—left the government on its back foot. Population growth hit 3.2% last year with planned PR admissions at 472 k vastly overshadowed by a net 821 k coming into the country on temporary visas. This massive population shock blew through the country's economic and infrastructure speed limits. This has been well-documented elsewhere including by Scotiabank Economics.

The federal government is now rapidly back-peddling to rein in those numbers to more sustainable levels. An overarching attrition target was set last March with the aim of reducing the number of non-permanent residents (NPRs) in the country to 5% of the population by 2026. To this end, a series of measures have been announced including caps on international students, changes to post-graduate work permits, and tightened rules for hiring temporary foreign workers. Further measures were to follow pending negotiations with provinces.

The immigration minister also indicated that transitions to permanency would play a stronger role in NPR stock attrition. Last year about 39% of the PR target was met via this route, while momentum in 2024 is closer to 45%.

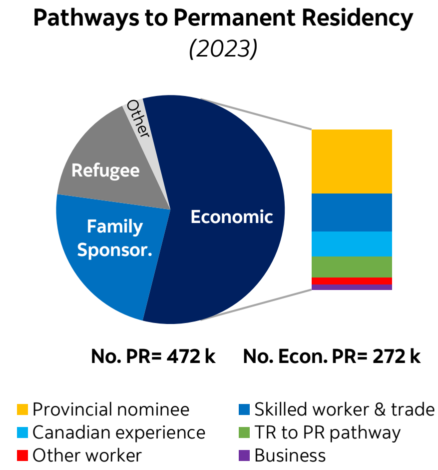
MOVING GOAL POSTS

The attrition target was broadly reasonable—if not regrettably necessary—when it was tabled last March. The number of NPRs in the country then stood at 2.5 mn or 6.3% of the population with the target expected to bring it down to around 2.1 mn by 2026. This implied annual attrition in the order of 150 k over three years. Transitions to permanency would have effectively zeroed net flows actually leaving the country. Coupled with current PR targets, total population growth would have materially slowed to somewhere in the order of 0.85% annually. This would have reflected a sharp deceleration relative to recent years, but lesser so relative to historic rates and would have unfolded into a slowing economy and softening labour markets.

Recent data show the country is now even further from that target. At last count, there were just over 3 mn non-permanent residents in the country or 7.3% of the total population. This trajectory has yet to peak. The pace of growth has been decelerating as NPR flows are modestly abating (chart 4), but no where near the pace consistent with the attrition target. Granted, some stop-gap measures had not taken effect yet at last count (through July), but more timely Labour Force Survey (LFS) data show growth of the working-age population running at an annualized pace of 4 % sa in September.

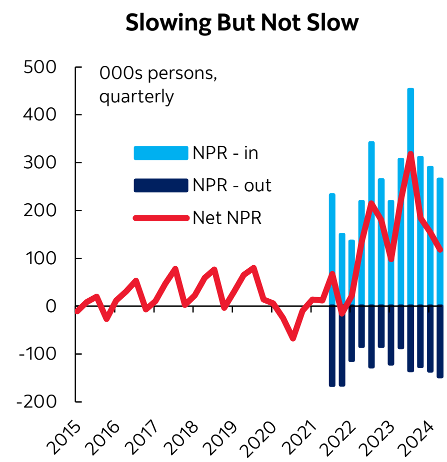
Adhering to the original NPR target would stop population growth in its tracks. The simple math suggests that the NPR population would likely need to decline by 1 mn over two years. Assuming PR targets are maintained (i.e., 1 mn over the next two years), this would effectively flatline net population growth. Whether a substantial share of current NPRs within the country are transitioned to PR status or NPRs are forced out *en masse* with new PR arrivals taking their stead, the net change in headcount approaches zero either way (chart 2, again).

Chart 3



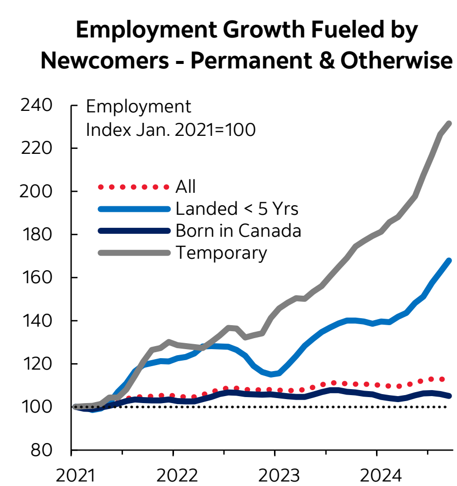
Sources: Scotiabank Economics, IRCC.

Chart 4



Sources: Scotiabank Economics, Statistics Canada.

Chart 5



Sources: Scotiabank Economics, Statistics Canada.

Hitting the target now would be a clear over-correction. Scotiabank Economics has earlier estimated the productivity-neutral rate of population growth at around 350 k or 0.85% annual growth given the economy's capital intensity, labour composition, and trend business investment (among other factors). To be clear, capital deepening is sorely needed, but the growth-friendly and socially-responsible route is through heightened business investment (and possibly labour reallocation), but not labour attrition.

LABOUR PAINS

The economic impacts could be particularly pronounced through labour supply channels. Just under half of the 3 mn NPRs (1.4 mn) currently in the country hold a work-only permit, while another third of the 1 mn international students hold dual study-work permits according to IRCC data. Backing temporary workers out of LFS data provides a more conservative estimate of 1.1 mn temporary workers currently employed in Canada (and 1.2 mn in the labour force). Over a quarter of the 2.3 mn jobs added in Canada since 2021 have been filled by temporary residents—and almost half including those landing less than five years ago (chart 5).

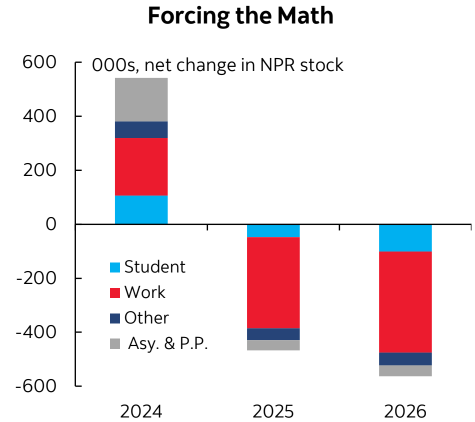
Current policies infer not just stalled labour force growth but a contraction. Student caps would carry some of the load, but the bulk would likely come from work streams. Our very rough guesstimate—admittedly making many sweeping assumptions[1]—suggest the impact on the labour force could be a contraction in the order of 200 k over the next two years (charts 6 & 7). This would represent about 1% of the entire labour force and almost 20% of temporary labour supply.

This could drive a commensurate contraction in output, according to René Lalonde's macro model, *absent a productivity response*. With annual employment growth of around 1.2% broadly consistent with stable inflation, such a sudden contraction in labour supply would lower the non-inflationary speed limit of the Canadian economy at least in the near term. It is a reasonable assumption that temporary residents' consumption footprint is disproportionately lower than its economic impact through labour supply channels, suggesting on balance upside risk to inflationary pressures.

The contraction in the labour force could represent a major challenge for businesses that currently employ workers that would be impacted by new policies. If businesses scramble to replace unplanned attrition, they would be competing over a smaller pool of resources. In the first instance, this would be disruptive to operations as up to 200k employees would need to be replaced. It would also likely lead to higher wages. Absent a productivity boost, this could prove inflationary. At the unlikely extreme—i.e., full replacement with those leaving the country—this would drive the unemployment rate a full percentage below the current status quo. There would be an uptick in employer-to-employer transitions, further underpinning inflationary dynamics through wage pressures and business inefficiencies. Keep in mind, current vacancies sit at around 570 k while unemployment among those born in Canada is still relatively tight by historic standards (chart 8). On a more positive note, greater labour scarcity could compel businesses to look to use technology to adapt to a smaller workforce. This would be most welcome, while still posing macro challenges in the interim.

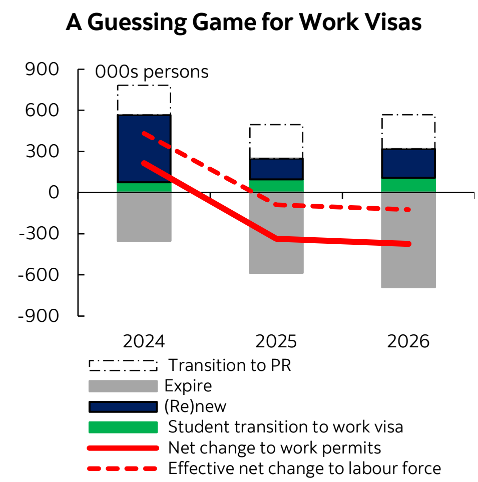
[1] A wide range of assumptions render these estimates tenuous at best. IRCC reports on visa issuance, while Statistics Canada has only recently started reporting NPR flows on a net and gross basis with low visibility on methodology. There is no publicly-available data on visa expirations or departures. Our estimates make the following assumptions: a median work and student visa duration of 2 years; 20% of students transition to work visas; a slight 15% pick-up in the recent pace of NPR-to-PR transitions; an attrition of "other" (family) NPRs consistent with the pace of attrition of principal applicant work visas; asylum, refugee and protected persons peaks at 450 k this year and decline by 25% over the horizon as the growth in claims is only partially offset by transitions to PR or departures against substantial backlogs in the processing systems.

Chart 6



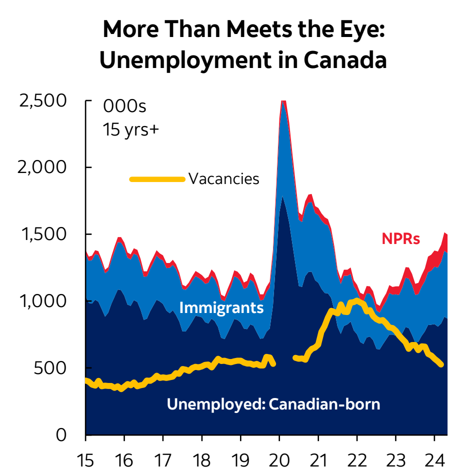
Sources: Scotiabank Economics, IRCC, StatsCan. *See publication footnote for assumptions.*

Chart 7



Sources: Scotiabank Economics, IRCC, StatsCan.

Chart 8



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PIÑATA POLICIES

There should *in theory* be some productivity offset in response to a labour shock, but it would not be immediate, nor is it a given with the risk of a blunt approach to attrition. Contrary to common discourse, a material share of temporary residents work in highly productive positions. According to Canada's TEER accounting (i.e., the classification of occupations according to training, education, experience and responsibilities), over 40% of temporary residents worked in high-competency sectors (TEER 0–2) at census time. The share is closer to 60% including medium-skill or TEER 3 (chart 9). The federal High Skilled PR stream, for example, comprises TEERs 0–3, while longitudinal data show principal applicants under this stream substantially out-perform peers with median wages 50% higher than the all-Canadian figure five years after landing (unfortunately, IRCC data on IMP work permits categorizes 90% of positions as 'other').

It is not yet evident that aggressive policies targeting labour force attrition would put a premium on potential or productivity. Changes to the Temporary Foreign Worker Program—while of outsized significance to a couple of sectors—would likely have a relatively small impact on headline numbers: the program accounts for only about 20% of work permits, while sectoral carve-outs likely protect in the order of 50% of permit holders (chart 10). Meanwhile, only a fraction of eventual permanent residents are measured against the points-based Comprehensive Ranking System (CRS) that does a *reasonable* job of predicting potential, with concessions to provinces further diluting its utility.

HEAD IN THE SAND

Perhaps the biggest risk is one of unintended consequences. IRCC staffing has increased by 60% since the onset of the pandemic, and—despite processing 7.3 mn applications last year—backlogs are still **pervasive** among temporary visas. Appeals filed with the Immigration & Refugee Board are **elevated** (mostly through sponsorship channels), while the Federal Court's **backlog** of pending immigration cases has tripled since the onset of the pandemic and now comprise three-quarters of all cases pending before the judiciary.

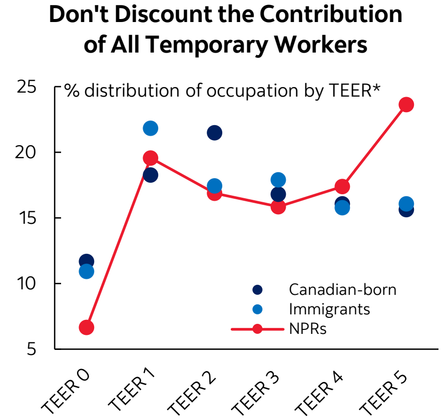
Asylum claims are now growing exponentially against these already-stretched adjudication systems (chart 11). The federal government does not have a robust system to incent or even track actual departures from the country with the immigration minister putting undocumented persons around 600 k earlier this year. Whatever the actual number, it could very likely climb higher ahead.

WHEN THE FACTS CHANGE

The government must choose the least-bad path ahead. It must balance the need to right-size the share of temporary residents in the country against long-term labour market needs—particularly those positions and people that have the potential to punch above their weight. It will be weighing accountability for mismanaged expectations of those already in the country against the moral hazard of driving those numbers even higher. Policymakers must both address its backward-looking bind, while also doubling-down on the forward-looking objective of improving Canadians' welfare over time. Addressing the former, but not the latter risks going from bad to worse.

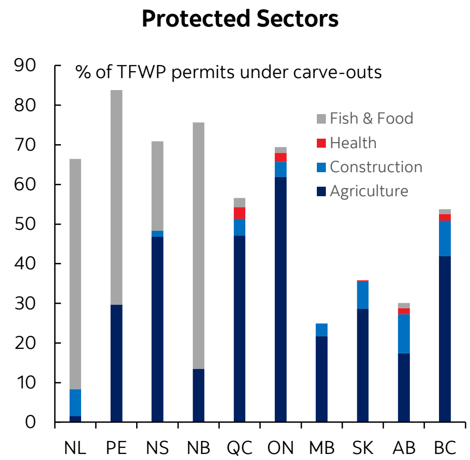
The most immediate dilemma is likely a political one. They've set an anchor that is no longer economically nor societally realistic. The November 1st announcements may not explicitly show their cards, but let's hope the numbers paint a more balanced picture. We will be looking for numbers that imply population growth in the order of 350 k annually or just shy of 1% over the horizon. That suggests hitting the attrition target beyond the horizon of the forthcoming immigration plan—and well-beyond this government's mandate.

Chart 9



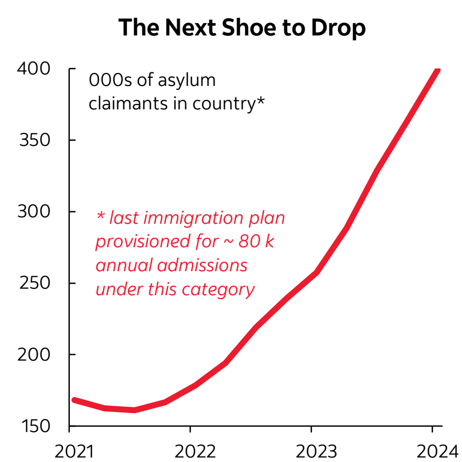
Sources: Scotiabank Economics, Statistics Canada (Census 2021). **Training, education, experience & responsibility where 0 is highest.*

Chart 10



Sources: Scotiabank Economics, IRCC.

Chart 11



Sources: Scotiabank Economics, Statistics Canada.

We hope—but don't expect—greater signals that the sum-of-the-parts will bolster the productivity imperative. As we have argued before, this would merit a ceiling for net inflows irrespective of stream—and hence population predictability—but with permanency granted on potential (in economic streams) while putting a premium on procedural transparency to re-anchor expectations. A coherent and complementary plan to inspire greater business investment would be wishful thinking for November 1st.