Scotiabank

GLOBAL ECONOMICS

PROVINCIAL PULSE

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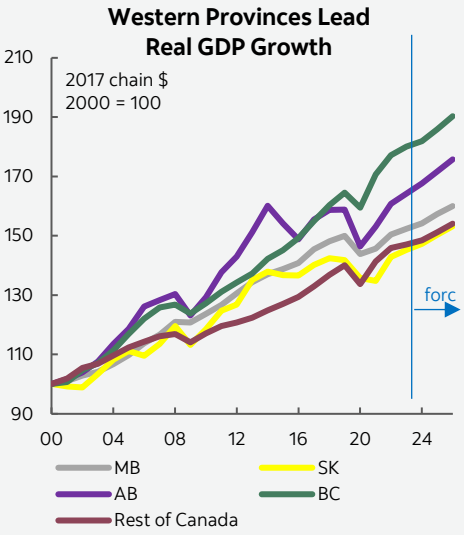
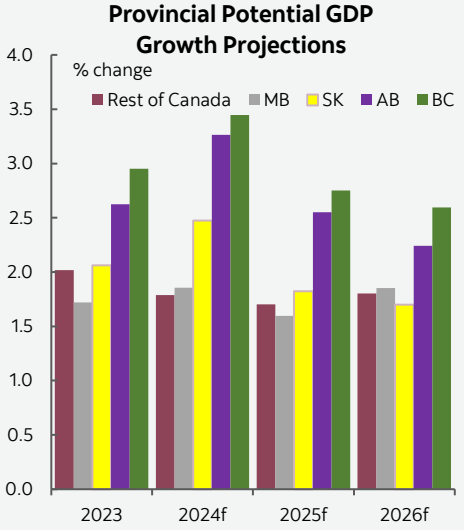
Chart 1



Sources: Scotiabank Economics, Statistics Canada.

Chart 2



Sources: Scotiabank Economics, Statistics Canada.

The Western Advantage: Will the Western Provinces Continue to Outperform?

HIGHLIGHTS

- **Western provinces, led by British Columbia (BC) and Alberta have demonstrated historically impressive growth, propelled by strong structural advantages. Potential GDP forecasts suggest sustained outperformance in the west relative to the national average in the next two years.**
- **The Prairie provinces benefit from rapid growth in labour supply amidst nationwide challenges of weak capital investment and declining productivity, driven by demographic factors and immigration. With participation rates expected to decline nationally amidst the retirement wave, the Prairie provinces should maintain higher labour participation due to their younger population. Immigration, particularly through robust intake from the Provincial Nominee Program (PNP), supports stable population gains and enhances labour market outcomes in the Prairie provinces.**
- **Over the past two decades, the western provinces have seen strong growth alongside notable gains in labour productivity driven by substantial investments, particularly in the oil and gas sector during the early 2010s. However, since 2019, a broad-based decline in labour productivity has tempered the potential growth outlook, with varying trajectories to recovery anticipated across provinces.**
- **BC has notably boosted its economic potential with robust labour productivity improvements driven by increased capital investments in natural gas, utilities and manufacturing sectors, enhancing production capacities.**
- **Despite reduced capital investments, the Prairie provinces have maintained growth in total factor productivity (TFP), particularly in the agriculture and energy sectors. Future digitization and scaling efforts are expected to further enhance TFP in agriculture, supporting continued labour productivity growth in the Prairies.**
- **Efforts to reduce emissions require significant capital investments to sustain production gains, potentially drag TFP growth in western provinces. Innovation and efficiency will be crucial to enhancing labour productivity as western provinces face similar productivity challenges as the rest of Canada. Transition and diversification efforts in sectors with high productivity gains offer opportunities for growth while continuing to innovate in natural resources.**
- **The oil and gas sector remains pivotal to Alberta's economic growth, with carbon intensity improvements and methane abatement crucial for meeting emission reduction targets and sustaining sector growth. Resource advantages support western outperformance but may start running their courses past 2026. Meanwhile, failing to meet emission caps by 2030 could lead to costly production curtailments.**

WESTERN CANADA: WHERE GROWTH ROAMS FREE

The western provinces have outperformed their peers over the past two decades (chart 1). Amidst the ongoing slowdown, the Prairie provinces stand out as growth leaders. Despite BC facing disproportionate effects from the monetary policy tightening, its economy has remained resilient, reflecting strong fundamentals.

Structural factors should increasingly determine growth ranking as cyclical factors subside. Potential GDP projections based on a standard Cobb-Douglas production function, which breaks down potential growth into productivity, labour and capital, suggest that western provinces, especially British Columbia (BC) and Alberta, enjoy structural advantages and should continue to outperform over the next two years (chart 2). We expect BC to top the ranking of potential growth over our forecast horizon, closely followed by Alberta. Saskatchewan holds an advantage over the national average, although to a lesser extent. Manitoba's growth profile should remain middle-of-the-pack, closely following that of the national average.

AN UNEQUIVOCAL LABOUR ADVANTAGE IN CANADA'S HEARTLAND

The rapid growth of the labour supply gives the Prairie provinces an edge over their peers in a broader Canadian environment of weak capital investment and declining labour productivity. The rapid replenishment of labour supply comes not only from population growth—demographic factors, particularly population aging and migration, are playing an important role in shaping the labour market. Over the past decade, participation rates have declined by 2–4 ppts. As baby boomers retire, participation rates are expected to keep falling across Canada, though the Prairie provinces should retain an advantage due to a favourable age structure. Our model suggests that a younger population in the Prairie provinces support participation rates 1–4 ppts higher than the national average (chart 3).

Immigrants continue to enhance labour market advantages in the Prairie provinces. Immigrants settled in the Prairie provinces, especially the more established ones that landed over 5 years ago, historically have better employment outcomes than those elsewhere in Canada. Immigrant participation in the Prairies has steadily risen to over 70%, compared to under 65% in Ontario and BC (chart 4). Unemployment rates for landed immigrants have remained stable at around 5.5% in Saskatchewan and Manitoba, while other provinces have seen rates exceed 8% during recessions (chart 5).

Employment outcomes partly reflect provincial selection biases in immigration. Manitoba and Saskatchewan ramped up the use of their Provincial Nominee Programs (PNP) to meet labour market needs, receiving 60–80% of their immigrants through PNP, well above 10% seen in Ontario. This program ensures stable population growth, particularly from economic immigrants. Although Manitoba and Saskatchewan are not favoured domestic destinations, they are poised to continue growing their population through immigration (chart 6).

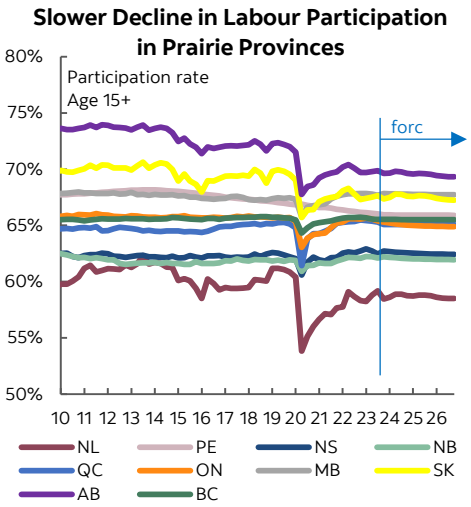
Overall, labour advantages are expected to give the Prairie provinces a combined 0.8 ppts edge in potential annual growth over the rest of the country for the next two years.

BEATING THE PRODUCTIVITY SLUMP

The Western provinces' strong performance coincided with notable improvement in labour productivity. The progress was largely driven by investments—capital stock grew sharply in the Prairies, partly attributable to the substantial investments in the early 2010s in the oil and gas sector. Since 2019, however, a broad-based decline in labour productivity has dampened potential growth. While productivity is expected to eventually recover, the provinces face uneven paths to recovery.

While the rest of the country experienced declining productivity, BC emerged as a standout with robust labour productivity boosting its potential growth. The province witnessed broad-based increases in capital investments, notably becoming the only one to see per capita growth in capital stock. This has enhanced BC's production capacity across

Chart 3



Sources: Scotiabank Economics, Statistics Canada.

Chart 4

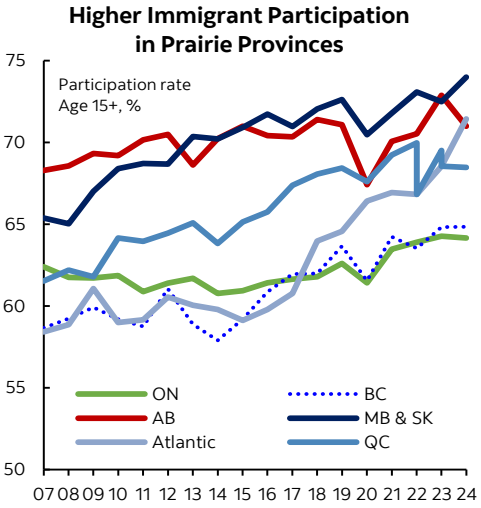


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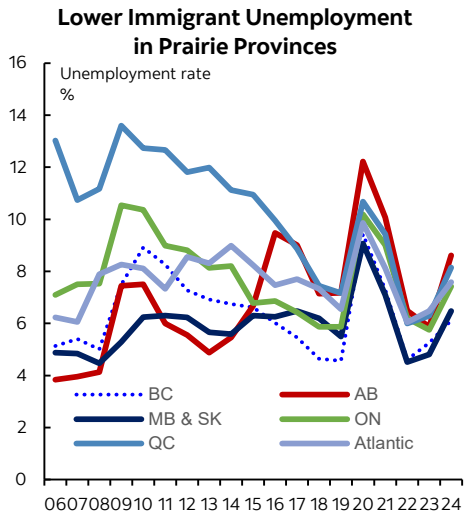
Chart 5



Sources: Scotiabank Economics, Statistics Canada.

various sectors. Further bolstering its economic growth, BC is currently advancing 11 major projects over $5 bn in natural gas and utilities—including LNG export facilities and the Site C dam—and in the manufacturing sector, especially in petrochemicals.

Recent trends suggest that while the Prairie provinces experience a sharp contraction in capital investments, they offset this with growth in total factor productivity (TFP) (chart 7). TFP measures production efficiency with a given amount of input (labour and capital). The agriculture sectors and energy sectors achieved higher production even with declining capital investment. In Manitoba and Saskatchewan, the agriculture industry has led improvements in efficiency through consolidation and automation. Future digitization and scaling are expected to further benefit this sector's TFP, surpassing other sectors, and boosting labour productivity growth in the Prairies.

Capital intensity in Alberta decreased significantly in the years leading up to the pandemic, driven by reduced investment in the oil and gas sector following the oil price shock. Despite lower investments, production efficiency improved particularly in the oil sands, with production levels reaching new highs in 2023. With reasonably high crude prices and growing demand for Canadian oil due to new egress capacity, continued growth in capital expenditure is expected to drive operational expansion and further increases in production in the near term. Current projections indicate that as capital expenditure increases steadily, production efficiency should stabilize at significantly higher levels than in the early 2010s (chart 8). Efforts to reduce emissions necessitate significant capital investments in the sector to sustain production gains, potentially weighing on TFP growth in the energy sector going forward. Hence, innovation and efficiency will be crucial to sustain and enhance labour productivity in Alberta.

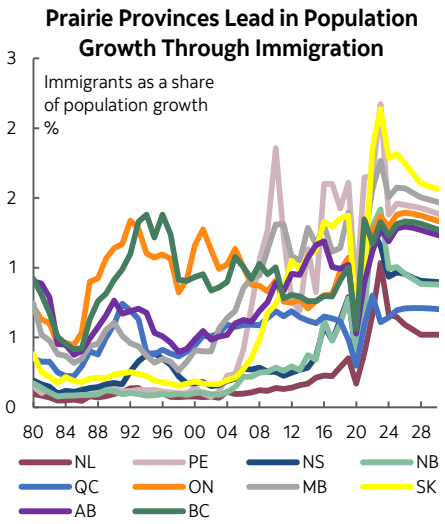
Overall, growth in TFP is projected to add an average of 0.5 ppts to national growth annually in the 2020s, as estimated by the Bank of Canada, lower than its historical average. Undoubtedly, the western provinces face the same productivity challenges as the rest of the country. The upcoming years present an opportunity to address these issues through transition and diversification efforts that will foster growth in sectors with high productivity potentials, while continuing to innovate in the natural resource sector.

COMMODITY DEMAND REMAINS CRUCIAL TO GROWTH PATH FORWARD

The opening of the Trans Mountain pipeline extension (TMX) has transformed the market outlook for heavy oil. Scotiabank GBM forecasts that the WCS-WTI price differential will narrow from 15.24 USD/bbl to 13.25 USD/bbl by 2026 due to increased egress capacity. This 2 USD difference will benefit profitability for heavy oil producers and could gradually lift Alberta's GDP by roughly 0.5 ppts.

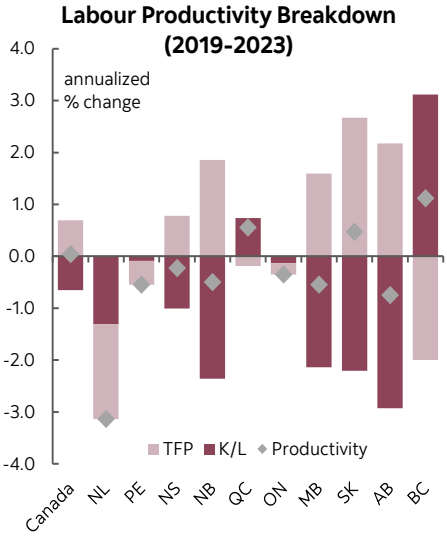
Climate policies have a significant impact on oil producers, but their effects are expected to be contained in the near term. According to our baseline scenario, production is set to increase due to supportive prices and a narrower spread. Scotiabank GBM anticipates relatively high energy prices over the next two years, with WTI prices projected to be in the range of $70–75 USD/bbl. The bright outlook hinges on the effective reduction of emissions, allowing producers to capitalize on robust prices. Under the federal government's oil and gas emissions cap, the sector needs to reduce GHG emissions by 20–30% below 2019 levels, as modeled by the Canadian Climate Institute. Most of this reduction is expected to come from decreasing GHG intensity rather than cutting production. Emission intensity will need to continue declining at the same rate as the past two decades, about 5% per year (chart 9). Therefore, continued production expansion depends on investments in efficiency improvements and emission abatement technologies. Alternatively, if emission intensity does not improve further, production would need to decrease by 3.5% annually to meet the 2030 targets (scenario 3, chart 10).

Chart 6



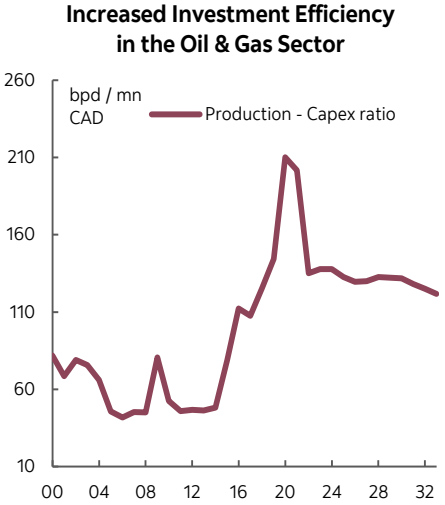
Sources: Scotiabank Economics, Statistics Canada.

Chart 7



Sources: Scotiabank Economics, Statistics Canada.

Chart 8



Sources: Scotiabank Economics, Statistics Canada, Alberta Energy Regulator.

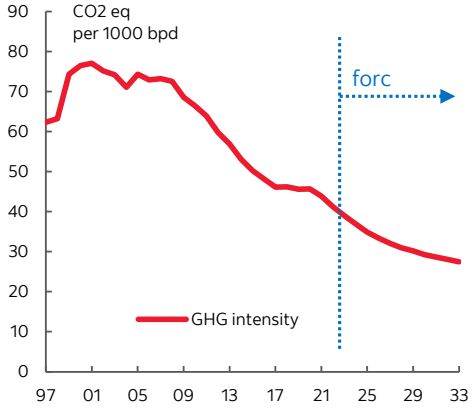
If significant improvements in carbon intensity are achieved, the oil and gas sector is poised to drive Alberta's growth and expand its share of real output in our baseline scenario. A recent Deloitte report (here) confirms that the 2030 emissions goal is attainable through efficiency improvements, methane abatement, and Carbon Capture and Storage (CCS) projects. Ongoing efficiency improvements are bearing fruit in the oil and gas sector and should continue to contribute to emission reductions. However, the primary uncertainty lies in methane abatement—a crucial element for meeting the emissions cap. BC and Alberta have set targets to reduce methane emissions by at least 75% from 2012 levels by 2030. According to a study by the Conference Board of Canada (here), while this reduction is feasible with existing technologies, failing to meet these targets could reduce Alberta's real GDP by 3.8–6.8 ppts by 2030 compared to baseline projections. Additionally, CCS/CCUS (Carbon Capture, Utilization and Storage) adoption will play a complementary role by 2030, though high costs may impact the speed and extent of growth in this sector, as noted by Scotiabank Economics (here).

The economic costs could be material if emission reduction efforts fall short of expectations. Achieving emission intensity reductions will require substantial investments, but the alternative—achieving reductions through production cuts—would result in significant economic costs. Meanwhile, the costs of inaction significantly outweigh the costs of acting, which further threatens economic growth potential. The Canadian Climate Institute estimated that by 2025, the previous 10 years of climate change will have shaved $25 bn off of national GDP relative to a stable-climate scenario, roughly half of the annual projected growth in national GDP in 2025. Western provinces are disproportionally affected by costly climate events. The Insurance Bureau of Canada reported that western Canada experienced over $240 per capita in damage for severe weather events in 2023, three times the amount experienced by the rest of the country.

Compared to domestic climate policies, international demand for fossil fuels has a more pronounced impact on the resource sector. According to the International Energy Agency (IEA), global demand for fossil fuels—coal, oil and natural gas—is expected to peak before 2030 under current policies. Currently, oil price forecasts remain range-bound for the next two years at relatively high levels, supported by production cuts implemented by OPEC+. This near-term stability in oil prices bodes well for Alberta and Saskatchewan since it reduces growth volatility from oil's boom and bust cycles.

Chart 9

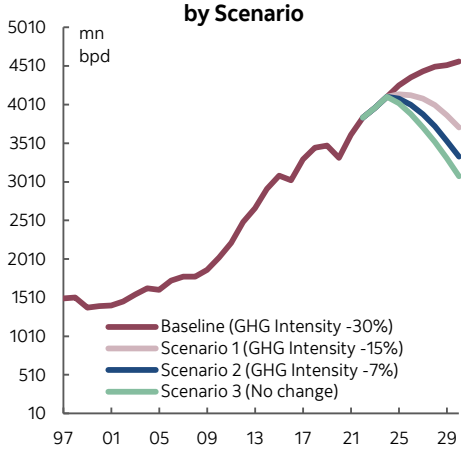
GHG Emission Intensity Needs to Decline to Achieve Production Growth in Alberta



Sources: Scotiabank Economics, Statistics Canada, Alberta Energy Regulator.

Chart 10

Alberta Oil Projection Forecast by Scenario



Sources: Scotiabank Economics, Alberta Energy Regulator.

The Provinces

(annual % change except where noted)

Real GDP	CA	NL	PE	NS	NB	QC	ON	MB	SK	AB	BC
2010–19	2.2	1.1	2.1	1.2	0.7	1.9	2.3	2.2	2.3	2.6	2.9
2021	5.3	1.0	8.4	5.9	5.3	6.7	5.4	1.3	-0.7	4.6	7.1
2022	3.8	-1.7	2.9	2.9	1.1	2.5	3.9	3.3	6.0	5.0	3.8
2023e	1.2	-2.5	2.2	1.3	1.3	0.0	1.2	1.3	1.6	2.2	1.6
2024f	1.2	1.8	2.0	1.3	1.1	0.7	1.1	1.2	1.4	2.1	1.1
2025f	2.0	2.6	2.2	1.6	1.4	1.7	2.0	2.0	2.1	2.4	2.2
Nominal GDP											
2010–19	4.0	3.7	4.2	3.0	2.8	3.8	4.1	3.9	3.5	3.7	4.5
2021	13.4	18.5	14.9	10.0	10.9	11.6	9.8	9.2	13.9	24.9	15.8
2022	11.8	6.8	9.3	7.1	7.4	8.4	9.2	8.6	29.1	22.0	11.0
2023e	2.8	-3.7	5.1	4.3	4.0	3.7	4.3	4.1	-1.2	-2.3	4.6
2024f	4.4	5.7	5.0	4.0	4.0	3.6	3.9	3.8	6.0	6.4	4.2
2025f	3.9	3.5	4.6	3.5	3.5	3.8	4.0	3.9	3.8	3.6	4.2
Employment											
2010–19	1.3	0.6	1.5	0.3	0.0	1.2	1.4	1.0	0.9	1.3	2.0
2021	5.0	3.4	4.0	5.6	3.1	4.3	5.2	3.7	2.6	5.4	6.2
2022	4.0	4.4	5.4	3.6	2.8	3.0	4.6	3.2	3.5	5.2	3.2
2023	2.4	1.8	5.7	2.6	3.5	2.3	2.4	2.5	1.8	3.6	1.6
2024f	1.8	2.4	4.3	2.7	2.4	0.8	1.3	1.9	1.9	2.9	2.1
2025f	1.1	0.8	2.4	1.4	1.4	0.9	1.2	1.2	1.3	1.8	1.3
Unemployment Rate (%)											
2010–19	6.9	13.3	10.6	8.7	9.4	7.1	7.0	5.6	5.3	6.2	6.2
2021	7.5	13.1	9.8	8.6	9.2	6.1	8.1	6.5	6.6	8.6	6.6
2022	5.3	11.3	7.6	6.5	7.2	4.3	5.6	4.6	4.7	5.8	4.6
2023	5.4	10.0	7.3	6.3	6.6	4.5	5.7	4.8	4.8	5.9	5.2
2024f	6.3	10.3	7.9	7.2	7.6	5.2	6.8	5.4	5.5	6.5	5.8
2025f	6.6	10.8	8.6	7.7	8.0	5.5	7.1	5.8	5.9	7.0	6.1
Total CPI, annual average											
2010-19	1.6	2.0	1.6	1.7	1.8	1.5	1.9	1.8	1.8	1.7	1.6
2021	3.4	3.7	5.1	4.1	3.8	3.8	3.5	3.2	2.6	3.2	2.8
2022	6.8	6.4	8.9	7.5	7.3	6.7	6.8	7.9	6.6	6.5	6.9
2023	3.9	3.3	2.9	4.0	3.5	4.5	3.8	3.6	3.9	3.3	4.0
2024f	2.6	2.5	2.3	2.7	2.4	2.9	2.6	1.6	1.8	2.8	2.6
2025f	2.2	2.0	2.1	2.1	2.1	2.3	2.2	2.1	2.2	2.3	2.1
Housing Starts (units, 000s)											
2010–19	201	2.2	0.8	4.2	2.7	44	70	6.6	6.0	31	34
2021	271	1.0	1.3	6.0	3.8	68	100	8.0	4.2	32	48
2022	262	2.7	1.2	5.2	3.7	41	87	3.5	2.6	41	24
2023	240	1.0	1.1	7.2	4.5	39	89	7.1	4.6	36	50
2024f	248	1.7	1.1	7.4	4.6	47	85	7.3	4.5	39	50
2025f	257	2.1	1.1	6.5	4.2	53	89	7.9	5.7	39	48
Motor Vehicle Sales (units, 000s)											
2010–19	1,816	33	7	52	42	441	738	56	54	239	199
2021	1,663	29	8	45	38	413	667	50	43	197	203
2022	1,523	25	7	39	35	372	642	46	42	184	182
2023	1,684	27	8	42	38	412	720	50	45	210	205
2024f	1,755	28	8	45	38	415	720	51	45	204	201
2025f	1,799	29	8	46	39	425	738	52	46	209	206
Budget Balances, (CAD mn)											
2020	-327,729	-1,492	-6	-342	409	-7,539	-16,404	-2,124	-1,127	-16,962	-5,507
2021	-90,200	-272	84	339	769	-772	2,025	-704	-1,468	3,915	1,265
2022	-35,322	784	-66	116	1,013	-6,150	-5,863	-378	1,581	11,641	704
2023e	-40,003	-433	-86	40	247	-6,302	-3,000	-1,997	-483	5,234	-5,914
2024f	-39,800	-152	-85	-467	41	-10,998	-9,800	-796	-273	367	-7,911

* NL budget balance in 2019 is net of one-time revenue boost via *Atlantic Accord* .

Sources: Scotiabank Economics, Statistics Canada, CMHC, Budget documents; Quebec budget balance figures are after Generations Fund and before Stabilization Reserve transfers.