

BUDGET ANALYSIS

Federal Spring Economic Update 2026

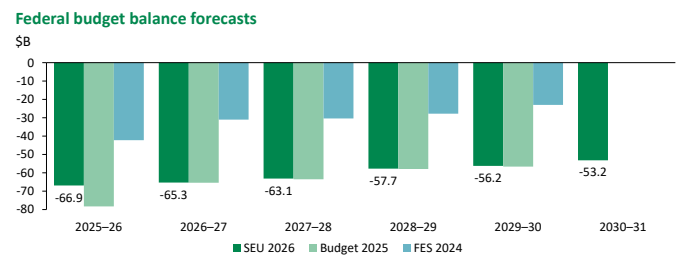
Don't Start Popping the Champagne Yet

By Jimmy Jean, Vice-President, Chief Economist and Strategist, and Randall Bartlett, Deputy Chief Economist

HIGHLIGHTS

- ▶ As was widely telegraphed prior to the Spring Economic Update (SEU) 2026, the federal government's fiscal performance wasn't as bad as previously predicted. The 2025–26 fiscal year (FY26) deficit was still a substantial \$66.9B, but came in lower than the \$78.3B projected in Budget 2025 (graph 1).
- ▶ But don't start popping the champagne yet. A big part of the near-term improvement in the deficit was a better-than-expected economic performance, which is beyond the federal government's control. It is also something that may not be repeated.
- ▶ Despite this improved starting point and economic outlook, the deficit forecast going forward is essentially unchanged from Budget 2025. That's partly because last year's savings also stemmed from lapsed spending—money that didn't get out the door—as opposed to prudent fiscal management. New measures were announced which filled that newfound fiscal room as well.
- ▶ On the spending side, many of the big measures were announced well in advance of the SEU 2026. Key measures since Budget 2025 include the Canada Groceries and Essentials Benefit (\$11.8B over six years); supporting workers in the skilled trades (\$6.0B); \$4.1B for empowering and healthy Indigenous communities; \$2.0B for supporting Ukraine; \$1.7B to work with the provinces and territories to improve the housing supply; additional measures to support workers (\$1.3B); increasing student grants and loans (\$1.1B); and \$1.0B for environmental protection and conservation.
- ▶ Turning to revenues, the most substantive of these measures is the temporary suspension of the federal fuel excise tax (\$2.4B in FY27). This is followed closely by the revamped tax credit for electric vehicle purchases, at \$2.3B over six years. Otherwise, the tax breaks were few and far between.
- ▶ One of the major benefits of the upwardly revised nominal GDP outlook is that it reduced the size of future deficits as a share of GDP even if those deficits were largely unchanged from Budget 2025. The projected path for the federal debt-to-GDP ratio is also meaningfully lower, despite the path of the federal debt not changing all that much. This will help to keep Canada in a better fiscal position than many of its advanced economy peers, supporting a strong credit rating and comparatively lower debt services cost.

Graph 1
A Smaller Deficit Last Year Isn't Expected to Persist Into Future Years



SEU: Spring Economic Update; FES: Fall Economic Statement
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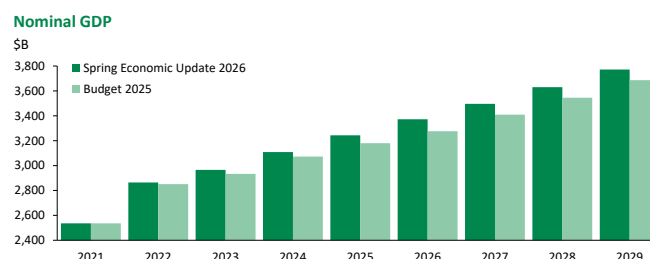
As was widely telegraphed prior to the SEU 2026, the federal government’s fiscal performance wasn’t as bad as previously predicted. While last year’s deficit was still a substantial \$66.9B (table 1), it was lower than in Budget 2025. But don’t start popping the champagne yet. Despite a better starting point and economic outlook, the federal deficit and debt forecast going forward is essentially unchanged from Budget 2025. That’s because newfound fiscal room from higher revenues and lapsed expenditures was largely filled by new spending measures and modest tax relief. However, the higher level of nominal GDP over the outlook helped to bring down the deficit and debt-to-GDP ratios, improving the sustainability of federal finances and likely the views of rating agencies and investors as well.

Unexpected Help from the Economy

Sometimes good news comes from where it’s least expected. This was the case with the Canadian economy following the publication of [Budget 2025](#). With the release of Q3 2025 data at the end of November 2025, the level of Canada’s nominal GDP—the broadest measure of the taxbase—was revised up by 1.2% in 2024. Real and nominal GDP growth in 2025 also came in better than expected (table 2 on page 2). Together, this boosted the starting point for an improved economic outlook overall. The level of nominal GDP is now expected to be 2.3% higher in 2029 than projected in Budget 2025 (graph 2).

There are a few important implications of this economic tailwind for federal finances. The first is a higher revenue outlook than forecast in Budget 2025. Second, a better economic outlook

Graph 2
The Outlook for Nominal GDP Has Improved Since Budget 2025



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than previously expected means spending on programs linked to the economy, like Employment Insurance, could be lower than previously projected. Consequently, smaller deficits mean less debt accumulation and lower-than-planned public debt charges, creating a more virtuous (or less vicious) fiscal spiral. The other benefit is improved deficit and debt levels as a share of nominal GDP, just because of nominal GDP now being higher over the fiscal forecast.

As Goes the Economy, So Go Revenues

That better-than-expected economic activity boosts revenues is a tale as old as time. According to what we can tell from the information provided by the federal government in the SEU 2026, it looks like the economic tailwind boosted revenues by a total of as much as \$35.9B in the five fiscal years starting in FY26

TABLE 1
Summary of transactions

IN \$B (EXCEPT IF INDICATED)	ACTUAL	PROJECTIONS					
	2024–2025	2025–2026	2026–2027	2027–2028	2028–2029	2029–2030	2030–2031
Budgetary revenues	511.0	511.5	529.6	546.8	565.9	589.8	613.7
<i>Growth (%)</i>	11.2	0.1	3.5	3.2	3.5	4.2	4.1
Program spending	-489.9	-512.8	-536.1	-543.9	-555.9	-575.4	-591.6
<i>Growth (%)</i>	5.0	4.7	4.5	1.5	2.2	3.5	2.8
Debt charges	-53.4	-54.0	-58.7	-65.7	-71.6	-75.7	-80.9
<i>Growth (%)</i>	13.0	1.1	8.7	11.9	9.0	5.7	6.9
Net actuarial losses	-4.0	-11.6	-0.1	-0.4	3.9	5.2	5.6
Budgetary balance	-36.3	-66.9	-65.3	-63.1	-57.7	-56.2	-53.2
Federal debt ¹	1,266.5	1,333.9	1,399.3	1,462.4	1,520.1	1,576.3	1,629.4
<i>Growth (%)</i>	2.5	5.3	4.9	4.5	3.9	3.7	3.4
Budgetary revenues (% of GDP)	16.4	15.8	15.7	15.6	15.6	15.6	15.7
Program spending (% of GDP)	-15.8	-15.8	-15.9	-15.6	-15.3	-15.3	-15.1
Public debt charges (% of GDP)	-1.7	-1.8	-1.7	-1.9	-2.0	-2.0	-2.1
Budgetary balance (% of GDP)	-1.2	-2.1	-1.9	-1.8	-1.6	-1.5	-1.4
Federal debt (% of GDP)	40.7	41.1	41.5	41.8	41.9	41.8	41.6

¹ Debt representing the accumulated deficits including other comprehensive income.
Department of Finance Canada and Desjardins Economic Studies

TABLE 2
Economic and Financial Forecasts

AVERAGE ANNUAL GROWTH IN % (EXCEPT IF INDICATED)	2025		2026f			2027f		
	Actual	Budget 2025	SEU 2026	Budget 2025	Desj. Group	SEU 2026	Budget 2025	Desj. Group
Real GDP	1.7	1.1	1.1	1.2	1.4	1.9	2.0	2.1
GDP deflator	2.6	2.4	2.8	1.8	3.2	1.8	2.0	2.3
Nominal GDP	4.3	3.5	4.0	3.0	4.6	3.7	4.1	4.4
Treasury bills—3-month	2.6	2.6	2.2	2.3	2.3	2.5	2.5	2.7
Federal bonds—10-year	3.2	3.3	3.4	3.4	3.4	3.6	3.5	3.3
Unemployment rate	6.8	7.0	6.5	6.8	6.7	6.2	6.4	6.6
Exchange rate (US\$/C\$)	72.0	72.2	73.7	75.1	73.0	75.4	76.4	76.0
Real GDP—United States	2.1	1.6	2.4	1.6	2.2	2.0	2.0	2.0

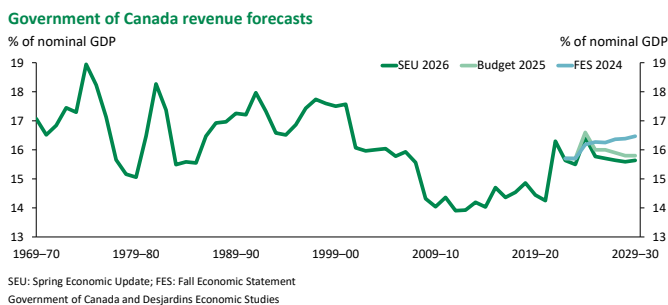
f: forecasts

NOTE: Data may not add to totals due to rounding.

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relative to Budget 2025. Even with this improvement, overall revenues are projected to fall further as a share of GDP, albeit still remaining elevated compared to pre-COVID levels (graph 3).

Graph 3
Planned Revenues Keep Falling as a Share of GDP



But the increase in revenues is not ultimately as large as the improved economic outlook would suggest. That's because the federal government has also announced relatively modest tax cuts since Budget 2025. One measure that has received a lot of attention recently was the cut to the 10-cent federal excise tax on gasoline from mid-April 2026 until Labour Day. The federal government has estimated that it will cost about \$2.4B in FY27. This is followed closely by the revamped tax credit for electric vehicle purchases, at \$2.3B over six years. Otherwise, the tax breaks were few and far between in the SEU 2026.

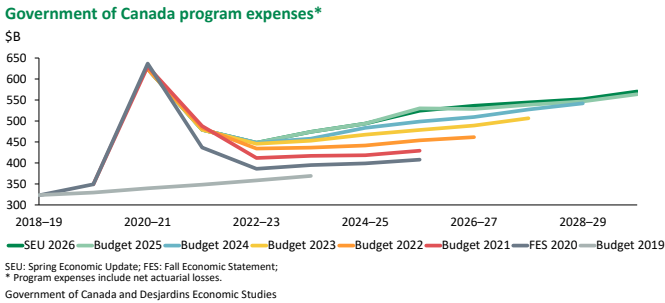
Spending Is Lower but for the Wrong Reasons

While the improved economic performance and resulting better revenues helped to bring down the federal deficit last year, the biggest contribution came from lower planned spending. And it unfortunately appears to have been primarily for the wrong reasons. Despite big spending plans for FY26, the federal government doesn't seem to have been able to get the money out the door fast enough. In "fiscal speak", these are called lapses. Lapses were common in the decade prior to 2025, and speak to possible risk around policy execution as opposed to prudent fiscal management.

Not that the federal government wasn't able to get some money out the door. Key measures since Budget 2025 include the Canada Groceries and Essentials Benefit (\$11.8B over six years); supporting workers in the skilled trades (\$6.0B); \$4.1B for empowering and healthy Indigenous communities; \$2.0B for supporting Ukraine; \$1.7B to work with the provinces and territories to improve the housing supply; additional measures to support workers (\$1.3B); increasing student grants and loans (\$1.1B); and \$1.0B for environmental protection and conservation. As a result, the outlook for program spending (including actuarial losses) remains essentially unchanged from Budget 2025 (graph 4 on page 3).

Given the upward revisions to nominal GDP, we were surprised to see no mention of higher defence spending in FY26. The estimates in our [SEU preview](#) suggested FY26 defence spending would need to be about \$1.2B higher than in Budget 2025 to end the last fiscal year at 2% of GDP. And this amount would

Graph 4
Despite Near-Term Savings, the Spending Outlook Remains Elevated



increase over time along with nominal GDP. However, the Government of Canada claims to have met its self-imposed 2% of GDP defence spending target by the end of FY26, on the way to 3.5% of GDP by 2035 (plus 1.5% of GDP in defence-related spending).

But we would be remiss not to highlight the savings the federal government has introduced. In addition to the workforce reduction laid out in Budget 2025 and subsequently acted on, the federal government recently launched the Federal Contracts Review to evaluate its use of existing contracts. Further, the federal government has maintained the informal separation of capital and operating expenses, and continues to show an operating budget surplus starting in FY29. We are skeptical of the value of this accounting framework in the absence of oversight by an agent of Parliament, such as the Auditor General or Parliamentary Budget Officer (PBO).

Canada’s First Sovereign Wealth Fund is a Work in Progress

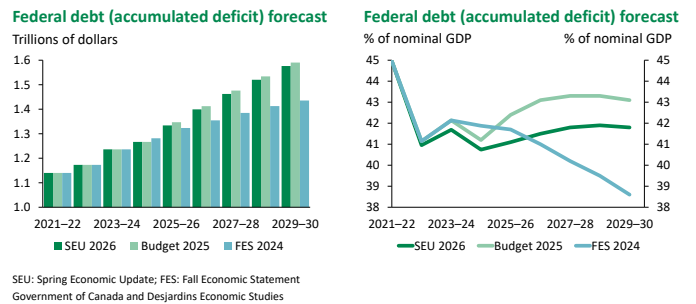
The day prior to publishing the SEU 2026, the federal government launched Canada’s first Sovereign Wealth Fund—the Canada Strong Fund (CSF). While details were scant in the [original press release](#), hopes that the SEU 2026 would put more meat on the bone were dashed. Importantly, there was no explicit accounting for how and when the CSF’s \$25B seed capital will be raised.

Ultimately, while more public dollars dedicated toward catalyzing private infrastructure investment is welcome, the proposed CSF draws a lot of parallels with previously announced investment vehicles, like the Canada Infrastructure Bank and Canada Growth Fund. Whether or not the CSF will be truly transformative will come down to execution—a place where past funds have come up short. Only time will tell if these goals are reached. (See [our note](#) on the recent successes and shortcomings of federal infrastructure investment.)

Debt Metrics Improve Thanks to Smaller Deficits and Higher GDP

While a bit of a mixed bag of a fiscal update, the SEU 2026 met expectations in that it showed a lower path for the federal debt-to-GDP ratio than in Budget 2025 (graph 5). Most of this was the result of a higher level of nominal GDP pulling down the ratio—a bit of good luck that in no way reflects actions taken by the Government of Canada. But as was discussed previously, there is also some good news on the top-line federal debt outlook, having come in modestly below earlier projections. This has opened up some additional fiscal room since the Budget 2025, when the [Office of the PBO](#) assessed federal finances as being on the brink of becoming unsustainable.

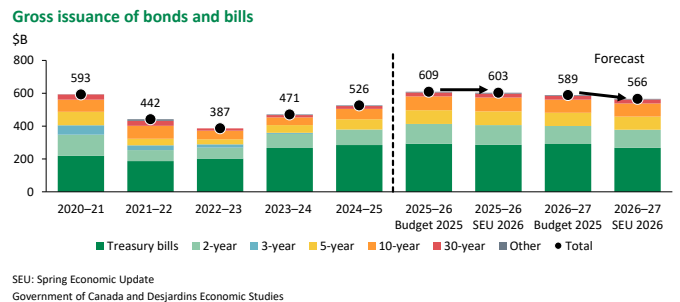
Graph 5
Federal Debt Outlook Largely Improved Due to Higher Nominal GDP



Debt Management Strategy Broadly Unchanged

For FY27, the Debt Management Strategy (DMS) outlined a gross domestic debt issuance program of \$566B, down from the \$589B forecast in the Budget 2025 (graph 6). Treasury bills absorbed the entirety of the decline in issuance, with the bond issuance program maintained at \$298B. The bucket distribution was also unchanged from the budget, with 35% of the issuance allocated in maturities of 10 years or more. Similarly, benchmark

Graph 6
Planned Debt Issuance Has Come Down from Budget 2025



target size ranges and the pattern of auctions were kept consistent with the 2025 budget. There weren't any further changes either to the CMB program, after it was raised to \$80B (from \$60B) in Budget 2025.

Conclusion

At a time of mounting global fiscal strain, an update showing improved deficit and debt metrics deserves recognition. But gains driven by nominal GDP effects and spending lapses fall well short of the "sound fiscal management" touted by Mark Carney.

Risks remain skewed to the downside. Recent developments continue to point to capital erosion in Canada's manufacturing sector, which is at odds with the government's ambitious, but still largely aspirational industrial agenda. The statement offers little in the way of new or enhanced support for affected sectors in the near term.

The sovereign wealth fund proposal also lacks critical detail. Questions around its financing structure and retail investor access remain unanswered, reinforcing the sense that this is a concept in development rather than a deployable tool now. That is underwhelming given the idea's lack of novelty, and the absence of clear evidence that it would meaningfully improve capital formation or avoid duplicating existing vehicles.

Support for skilled trades stands out as a relative bright spot. Chronic labour shortages in construction have long sat uneasily alongside a policy narrative centred on accelerating physical investment. A softer labour market may now help rebalance that gap by drawing more workers into the trades.

Overall, the update reads as incremental. There may be a significant number of stand-alone announcements between now and the fall Budget 2026 given an unstable economic environment that demands greater urgency and policy agility.