Market View
Economics and Strategy

NATIONAL BANK OF CANADA
CAPITAL MARKETS

March 5, 2026 – (Vol. X, No. 28)

# The other 'G' in GDP

By Ethan Currie, Taylor Schleich & Warren Lovely

There are many ways to dissect the quarterly national accounts in the most normal of times, but considering the economic volatility in 2025, these data offer up even more at this juncture. With annual figures now available, we already explored Canada-U.S. growth differentials (**here**). This *Market View* looks at another important 'G' within the GDP report—we're talking about the government sector, of course! Read on for an overview of how public expenditures are driving economic growth in Canada, where this spending is concentrated (hint: military capacity), and what it suggests for the fiscal and rates outlook.

**Chart 1-4:** Canadian government expenditures have decisively outpaced broader economic growth over the past decade. More recently, sluggish private sector investment has been partially offset by a growing public footprint. While private investment has been flat-to-negative in the past three years, public sector fixed capital has expanded at a healthy CAGR of 3.5% over that period (compared to 1.7% for overall GDP).

Canada has lagged U.S. growth (and productivity) in years since the pandemic, while the government share of GDP in the two countries have moved in opposite directions. Indeed, government expenditure growth is the only area where Canada holds a relative edge when compared to the U.S. GDP picture, where growth in other components are much more impressive south of the border.

**Chart 5-6:** Thankfully, the share of Canadian 'G' allocated to fixed capital (as opposed to consumption) is growing. While not at record highs yet, this is reflective of prior infrastructure commitments, and shows early promise of the recently unveiled **Canada Defence Industrial Strategy**.

These plans were quantified in Budget 2025, which revealed a change in trajectory away from program spending and towards capital-intensive projects. We explored Budget 2025 in more detail **here**.

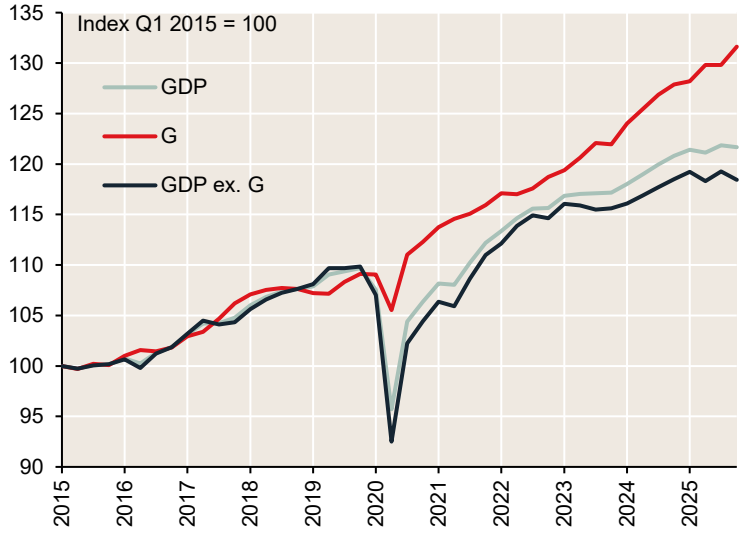
**Chart 7-10:** Zooming in, government investment in the defence sector is making strides never seen before. Ambitious NATO spending targets (one of which achieved in 2025) suggest that growth here will continue, which lends itself well to the prospect of productivity enhancement. Historically, as Canada's military spending declined, the country's manufacturing footprint and labour-productivity growth weakened in tandem. Over time, higher defence expenditures could help re-energize Canada's manufacturing base, which has steadily lost global relevance.

**Chart 11-14:** This government impulse won't come without a fiscal price tag, however. While investment is picking up at the federal level, this is true for every stage of government, and it remains that the bulk of capital spending takes place at the provincial level. With operational spending pressures / deficits also evident, net borrowing requirements are set to increase and debt burdens are pointed higher as a result.

Expansionary policy, like in the U.S., is set to keep the sovereign yield curve at relatively steeper levels. A net debt edge provided by an **actuarially sound public pension sector**, combined with the investment-intensive nature of Canada's fiscal outlook is reflected in a more modest duration premium relative to other developed bond markets. Indeed, the GoC longer-end has also fared relatively better in recent episodes of fiscal anxiety-driven yield surges.

**Chart 1: 'G' has propped up GDP in Canada since COVID**

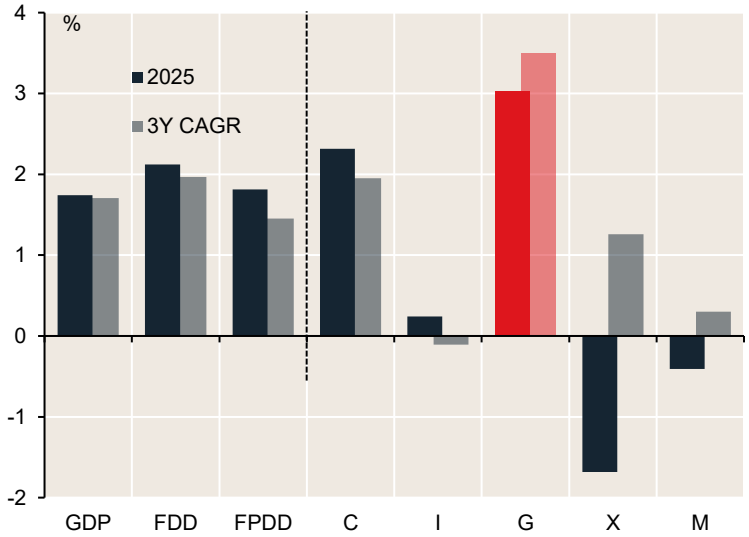
*Canadian GDP, gov't expenditure (G), and GDP ex. G, indexed to 2015*




*Source: NBC, StatCan | Note: Chain-weighted prices*

**Chart 2: More recently, 'G' has been the clear growth driver**

*Real GDP growth, by component*

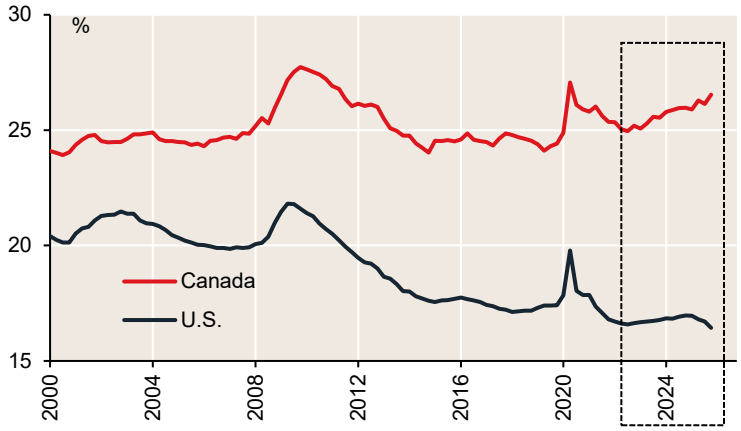



*Source: NBC, StatCan*

Note: In some cases, we combine GDP components (i.e., 'G' / government as the combination of government consumption and fixed capital formation). Chain-weighted data when combined are not additive but discrepancies are small (+/- a few tenths of a %-pt). FDD = Final domestic demand, FPDD = Final private domestic demand (FDD-G).

**Chart 3: Relatively, 'G' contribution on the rise in Canada**

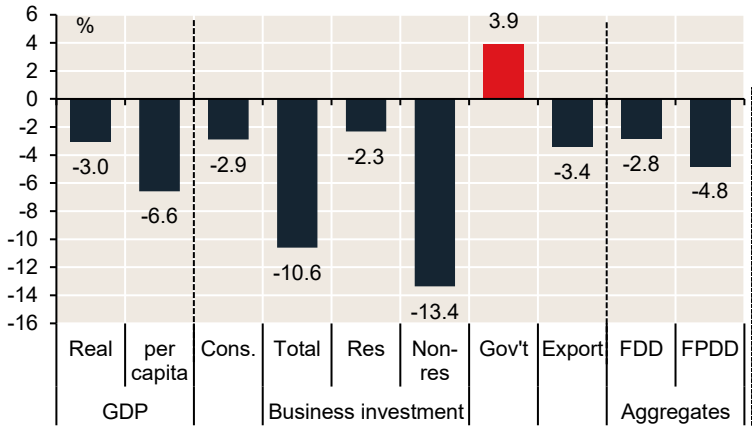
*Government expenditure as a share of GDP, since 2000: Canada & U.S.*




*Source: NBC, StatCan, Bloomberg*

**Chart 4: Without 'G', CA-US growth differentials even worse**

*Cumulative GDP growth diff since 2022, by component: Canada less U.S.*

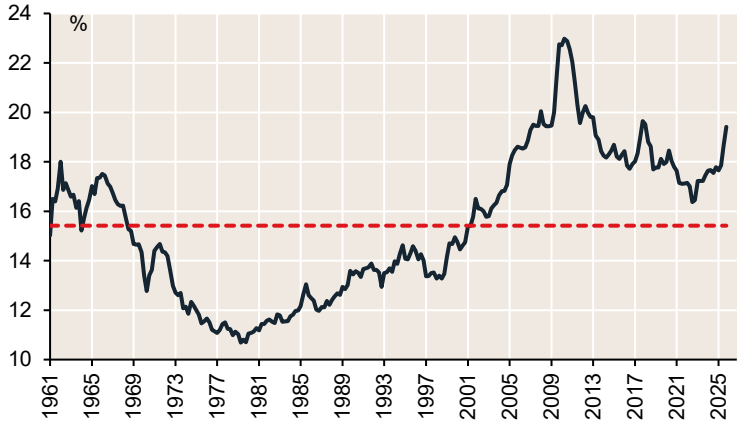



*Source: NBC, BEA, StatCan, Bloomberg*

Government contributions (consumption + investment) have propped up Canadian economic growth over the last half decade. These expenditures as a share of GDP are increasingly larger in Canada than they are in the U.S. In fact, if it weren't for the government sector, cumulative growth in every component of GDP would fall short relative to the U.S. over the past three years.

**Chart 5: Increased 'G' stemming more from investment…**

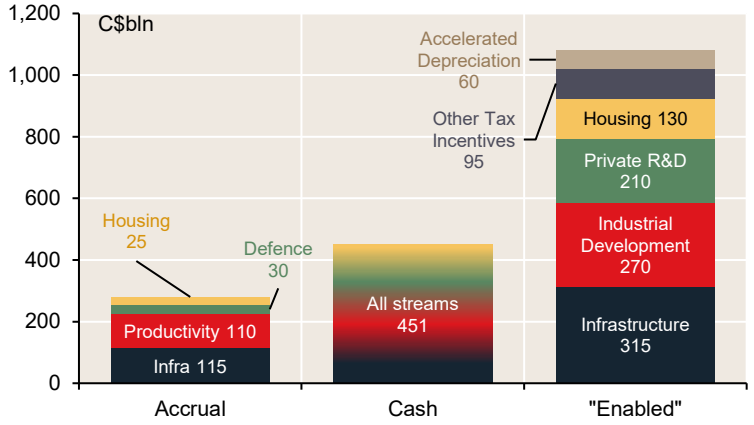
*Canadian gov't investment as a share of total gov't expenditure, since 1961*




*Source: NBC, StatCan | Note: Red line denotes full data series average*

**Chart 6: … showing early promise of renewed Budget focus**

*GoC accrual- and cash-based investment spending & total 'enabled' investment*

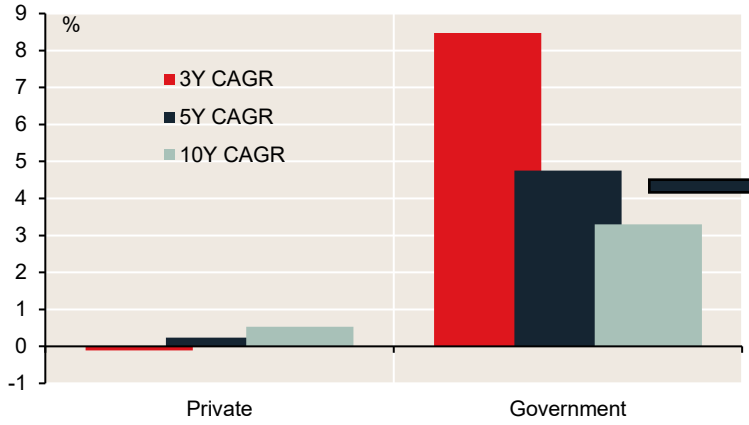



*Source: NBC, GoC*

The ratio of government investment to consumption is the highest it's been in nearly a decade and now decisively higher than its long-term average. It's still early, but that's material evidence of a 'spend less to invest more' agenda—where program spending growth is set to hit the brakes (from an 8.1% CAGR in the past 10Y, down to 0.5% to 2029-30), and capital spending will keep pace.

**Chart 7: Private investment flat, as 'G' steps in…**

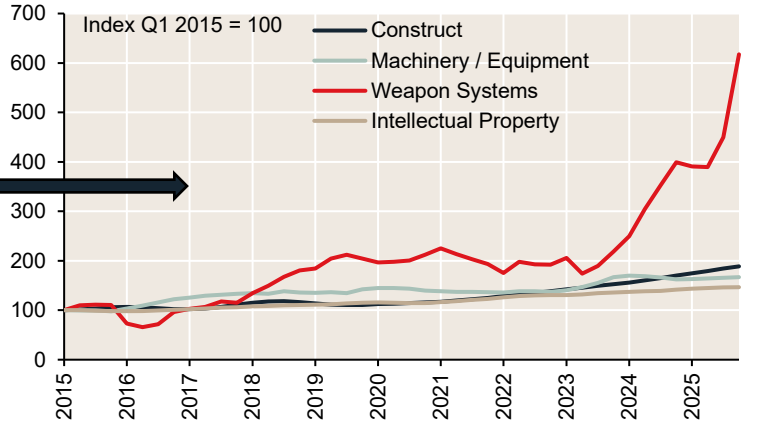
*Real fixed capital formation growth: Private vs public*




*Source: NBC, StatCan*

**Chart 8: … with military-related spending leading the way**

*Government investment by major component (nominal, 4Q MA), indexed to 2015*

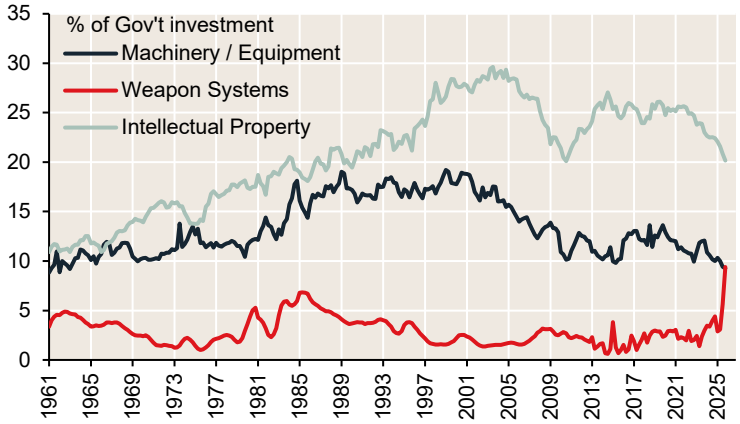



*Source: NBC, StatCan*

No, Chart 7 isn't missing a bar—in the last three years, private investment is flat-to-unchanged. Government investment has expanded at a healthy clip more recently, however, and that's been driven by a massive surge in capital allocated to weapon systems. With another NATO target (3.5% core spending) in sight, there's no question this subcomponent will remain in focus.

**Chart 9: Defence expenditures naturally a smaller 'G' driver**

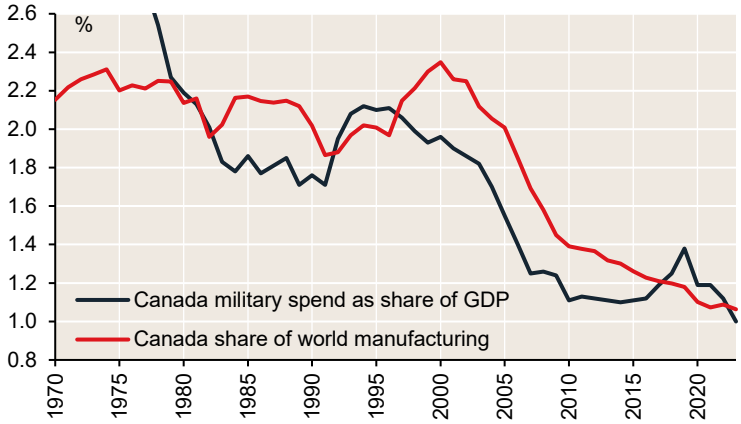
*Share of government investment by major component, since 1961*




*Source: NBC, StatCan | Note: Last major subsection (construction) not included in visual; Nominal figures are used*

**Chart 10: Where defence dollars go, industry will follow**

*Canada military expenditure (% of GDP) vs manufacturing share (% of world)*

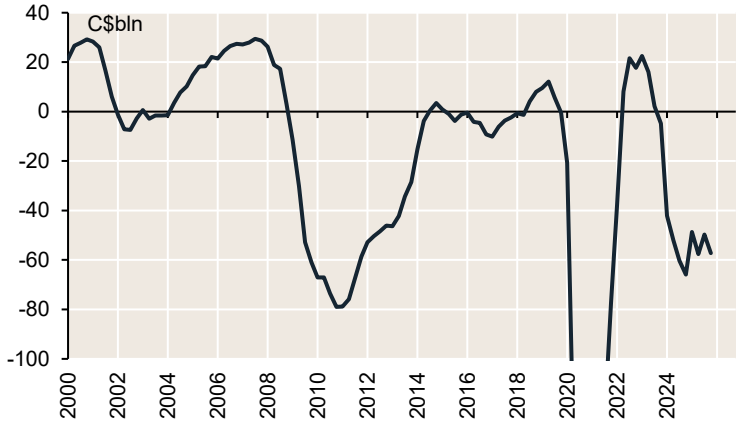



*Source: NBC, SIPRI, UN Trade & Development | Note: Share of world sector value-added*

Investment in weapons systems makes up a smaller % of overall gov't investment. For the first time ever though, it isn't the smallest subcomponent, as investment here made its largest contribution to total investment on record in Q4. Ottawa's defence budget (as % of GDP) is set to be the largest in 70 years—promising for a sector that has key productivity implications.

**Chart 11: Intensified 'G' footprint not without a fiscal cost**

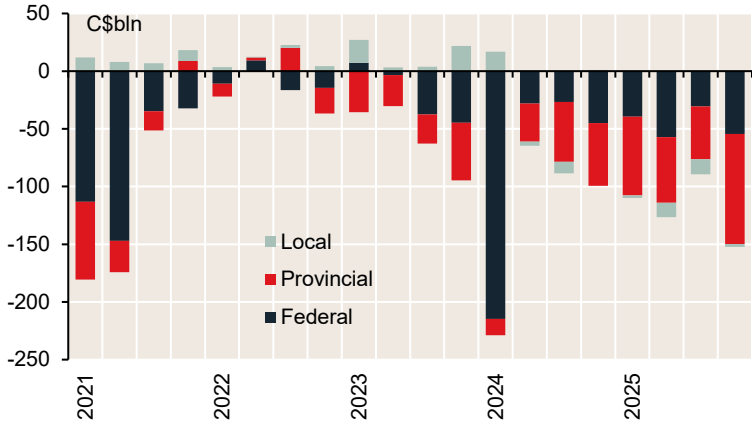
*Canadian general government net lending (borrowing), since 2000 (4Q MA)*




*Source: NBC, StatCan*

**Chart 12: Bulk of borrowing need stemming from provinces**

*Net lending (borrowing) by level of government, quarterly since 2021*

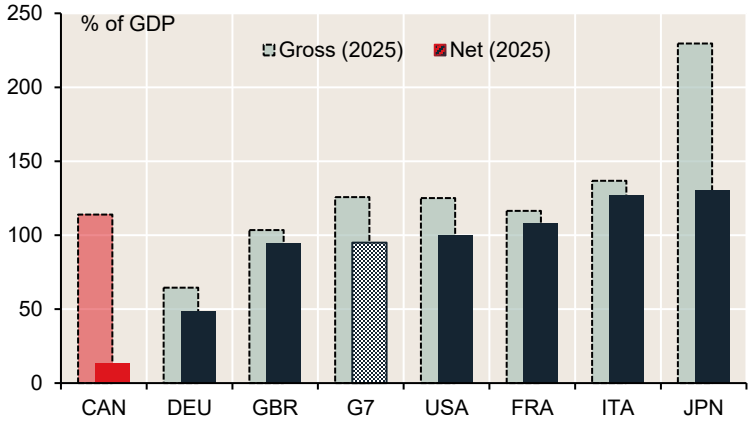



*Source: NBC, StatCan*

Of course, this government investment intensity is not without cost. Deficits, at every level of government, are higher than pre-pandemic levels and debt accumulation is set to continue. The national net borrowing burden is shared, and increasingly represented by the provincial level—where 2026 budgets are already pointing towards sustained shortfalls amidst a challenging economic backdrop.

**Chart 13: Fiscal edge will be helpful for ambitious targets…**

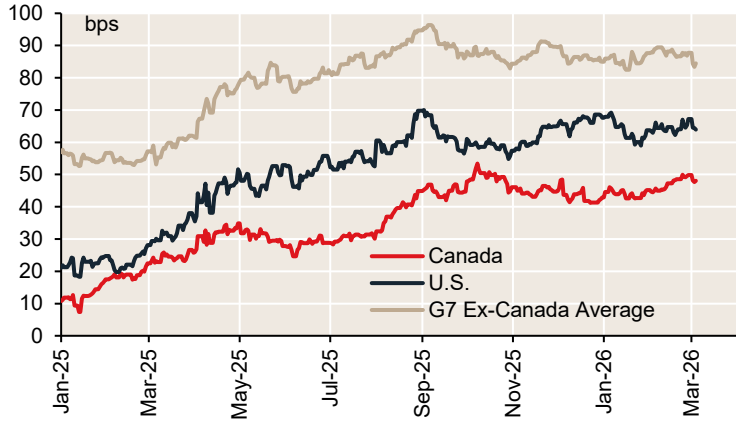
*General government gross & net debt-to-GDP ratios of G7 nations: 2025*




*Source: NBC, IMF, Bloomberg*

**Chart 14: … and bond markets tend to agree for now**

*10s30s yield curve: Canada, U.S., and G7 ex-Canada since 2025*




*Source: NBC, Bloomberg | Note: G7 Ex-Canada is simple average*

Though net borrowing requirements are structurally larger than pre-COVID, investment-driven deficits will be more well received than consumption-driven shortfalls. Canada's relative net debt edge should also ease **fiscal expansion anxieties**. Bond investors already concede this, as Canada has the flattest yield curve in the G7, and GoC 30s have fared particularly well in long-end shocks.

## Economics and Strategy

**Subscribe to our publications:**
**NBC.EconomicsStrategy@nbc.ca**

**To contact us:**
514-879-2529

**Stéfane Marion**
Chief Economist and Strategist
*stefane.marion@nbc.ca*

**Matthieu Arseneau**
Deputy Chief Economist
*matthieu.arseneau@nbc.ca*

**Jocelyn Paquet**
Senior Economist
*jocelyn.paquet@nbc.ca*

**Kyle Dahms**
Senior Economist
*kyle.dahms@nbc.ca*

**Alexandra Ducharme**
Senior Economist
*alexandra.ducharme@nbc.ca*

**Daren King, CFA**
Senior Economist
*daren.king@nbc.ca*

**Warren Lovely**
Chief Rates and Public Sector Strategist
*warren.lovely@nbc.ca*

**Taylor Schleich**
Rates Strategist
*taylor.Schleich@nbc.ca*

**Ethan Currie**
Strategist
*ethan.currie@nbc.ca*

**Angelo Katsoras**
Geopolitical Analyst
*angelo.katsoras@nbc.ca*

**Nathalie Girard**
Senior Coordinator
*n.girard@nbc.ca*

**Giuseppe Saltarelli**
Desktop Publisher
*giuseppe.saltarelli@nbc.ca*


**General:** This Report was prepared by National Bank Financial, Inc. (NBF), (a Canadian investment dealer, member of CIRO), an indirect wholly owned subsidiary of National Bank of Canada. National Bank of Canada is a public company listed on the Toronto Stock Exchange.

The particulars contained herein were obtained from sources which we believe to be reliable but are not guaranteed by us and may be incomplete and may be subject to change without notice. The information is current as of the date of this document. Neither the author nor NBF assumes any obligation to update the information or advise on further developments relating to the topics or securities discussed. The opinions expressed are based upon the author(s) analysis and interpretation of these particulars and are not to be construed as a solicitation or offer to buy or sell the securities mentioned herein, and nothing in this Report constitutes a representation that any investment strategy or recommendation contained herein is suitable or appropriate to a recipient's individual circumstances. In all cases, investors should conduct their own investigation and analysis of such information before taking or omitting to take any action in relation to securities or markets that are analyzed in this Report. The Report alone is not intended to form the basis for an investment decision, or to replace any due diligence or analytical work required by you in making an investment decision.

This Report is for distribution only under such circumstances as may be permitted by applicable law. This Report is not directed at you if NBF or any affiliate distributing this Report is prohibited or restricted by any legislation or regulation in any jurisdiction from making it available to you. You should satisfy yourself before reading it that NBF is permitted to provide this Report to you under relevant legislation and regulations.

National Bank of Canada Financial Markets is a trade name used by National Bank Financial and National Bank of Canada Financial Inc.

**Canadian Residents:** NBF or its affiliates may engage in any trading strategies described herein for their own account or on a discretionary basis on behalf of certain clients and as market conditions change, may amend or change investment strategy including full and complete divestment. The trading interests of NBF and its affiliates may also be contrary to any opinions expressed in this Report.

NBF or its affiliates often act as financial advisor, agent or underwriter for certain issuers mentioned herein and may receive remuneration for its services. As well NBF and its affiliates and/or their officers, directors, representatives, associates, may have a position in the securities mentioned herein and may make purchases and/or sales of these securities from time to time in the open market or otherwise. NBF and its affiliates may make a market in securities mentioned in this Report. This Report may not be independent of the proprietary interests of NBF and its affiliates.

This Report is not considered a research product under Canadian law and regulation, and consequently is not governed by Canadian rules applicable to the publication and distribution of research Reports, including relevant restrictions or disclosures required to be included in research Reports.

**UK Residents:** This Report is a marketing document. This Report has not been prepared in accordance with EU legal requirements designed to promote the independence of investment research and it is not subject to any prohibition on dealing ahead of the dissemination of investment research. In respect of the distribution of this Report to UK residents, NBF has approved the contents (including, where necessary, for the purposes of Section 21(1) of the Financial Services and Markets Act 2000). This Report is for information purposes only and does not constitute a personal recommendation, or investment, legal or tax advice. NBF and/or its parent and/or any companies within or affiliates of the National Bank of Canada group and/or any of their directors, officers and employees may have or may have had interests or long or short positions in, and may at any time make purchases and/or sales as principal or agent, or may act or may have acted as market maker in the relevant investments or related investments discussed in this Report, or may act or have acted as investment and/or commercial banker with respect hereto. The value of investments, and the income derived from them, can go down as well as up and you may not get back the amount invested. Past performance is not a guide to future performance. If an investment is denominated in a foreign currency, rates of exchange may have an adverse effect on the value of the investment. Investments which are illiquid may be difficult to sell or realise; it may also be difficult to obtain reliable information about their value or the extent of the risks to which they are exposed. Certain transactions, including those involving futures, swaps, and other derivatives, give rise to substantial risk and are not suitable for all investors. The investments contained in this Report are not available to retail customers and this Report is not for distribution to retail clients (within the meaning of the rules of the Financial Conduct Authority). Persons who are retail clients should not act or rely upon the information in this Report. This Report does not constitute or form part of any offer for sale or subscription of or solicitation of any offer to buy or subscribe for the securities described herein nor shall it or any part of it form the basis of or be relied on in connection with any contract or commitment whatsoever.

This information is only for distribution to Eligible Counterparties and Professional Clients in the United Kingdom within the meaning of the rules of the Financial Conduct Authority. NBF is authorised and regulated by the Financial Conduct Authority and has its registered office at 70 St. Mary Axe, London, EC3A 8BE.

NBF is not authorised by the Prudential Regulation Authority and the Financial Conduct Authority to accept deposits in the United Kingdom.

**EU Residents:** With respect to the distribution of this report in the member states of the European Union ("EU") and the European Economic Area ("EEA") by NBC Paris, the contents of this report are for information purposes only and do not constitute investment advice, investment research, financial analysis or other forms of general recommendation relating to transactions in financial instruments within the meaning of Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 ("MiFID 2"). This report is intended only for professional investors and eligible counterparties within the meaning of MiFID 2 and its contents have not been reviewed or approved by any EU/EEA authority. NBC Paris is an investment firm authorised by the French Prudential Control and Resolution Authority __ ("ACPR") to provide investment services in France and has passported its investment services throughout the EU/EEA under the freedom to provide services and has its registered office at 8 avenue Percier, 75008 Paris, France. "NBC Financial Markets, a subsidiary of National Bank of Canada" is a trade name used by NBC Paris S.A.

NBF is not authorised to provide investment services in the EU/EEA.

**U.S. Residents:** With respect to the distribution of this report in the United States of America, National Bank of Canada Financial Inc. ("NBCFI") which is regulated by the Financial Industry Regulatory Authority (FINRA) and a member of the Securities Investor Protection Corporation (SIPC), an affiliate of NBF, accepts responsibility for its contents, subject to any terms set out above. To make further inquiry related to this report, or to effect any transaction, United States residents should contact their NBCFI registered representative.

This report is not a research report and is intended for Major U.S. Institutional Investors only. This report is not subject to U.S. independence and disclosure standards applicable to research reports.

**HK Residents:** With respect to the distribution of this report in Hong Kong by NBC Financial Markets Asia Limited ("NBCFMA") which is licensed by the Securities and Futures Commission ("SFC") to conduct Type 1 (dealing in securities) and Type 3 (leveraged foreign exchange trading) regulated activities, the contents of this report are solely for informational purposes. It has not been approved by, reviewed by, verified by or filed with any regulator in Hong Kong. Nothing herein is a recommendation, advice, offer or solicitation to buy or sell a product or service, nor an official confirmation of any transaction. None of the products issuers, NBCFMA or its affiliates or other persons or entities named herein are obliged to notify you of changes to any information and none of the foregoing assume any loss suffered by you in reliance of such information.

The content of this report may contain information about investment products which are not authorized by SFC for offering to the public in Hong Kong and such information will only be available to, those persons who are Professional Investors (as defined in the Securities and Futures Ordinance of Hong Kong ("SFO")). If you are in any doubt as to your status you should consult a financial adviser or contact us. This material is not meant to be marketing materials and is not intended for public distribution. Please note that neither this material nor the product referred to is authorized for sale by SFC. Please refer to product prospectus for full details.

There may be conflicts of interest relating to NBCFMA or its affiliates' businesses. These activities and interests include potential multiple advisory, transactional and financial and other interests in securities and instruments that may be purchased or sold by NBCFMA or its affiliates, or in other investment vehicles which are managed by NBCFMA or its affiliates that may purchase or sell such securities and instruments.

No other entity within the National Bank of Canada group, including National Bank of Canada and National Bank Financial Inc, is licensed or registered with the SFC. Accordingly, such entities and their employees are not permitted and do not intend to: (i) carry on a business in any regulated activity in Hong Kong; (ii) hold themselves out as carrying on a business in any regulated activity in Hong Kong; or (iii) actively market their services to the Hong Kong public.

**Copyright:** This Report may not be reproduced in whole or in part, or further distributed or published or referred to in any manner whatsoever, nor may the information, opinions or conclusions contained in it be referred to without in each case the prior express written consent of NBF.