

Economic double-header: Canadian productivity problems + tariffs in focus



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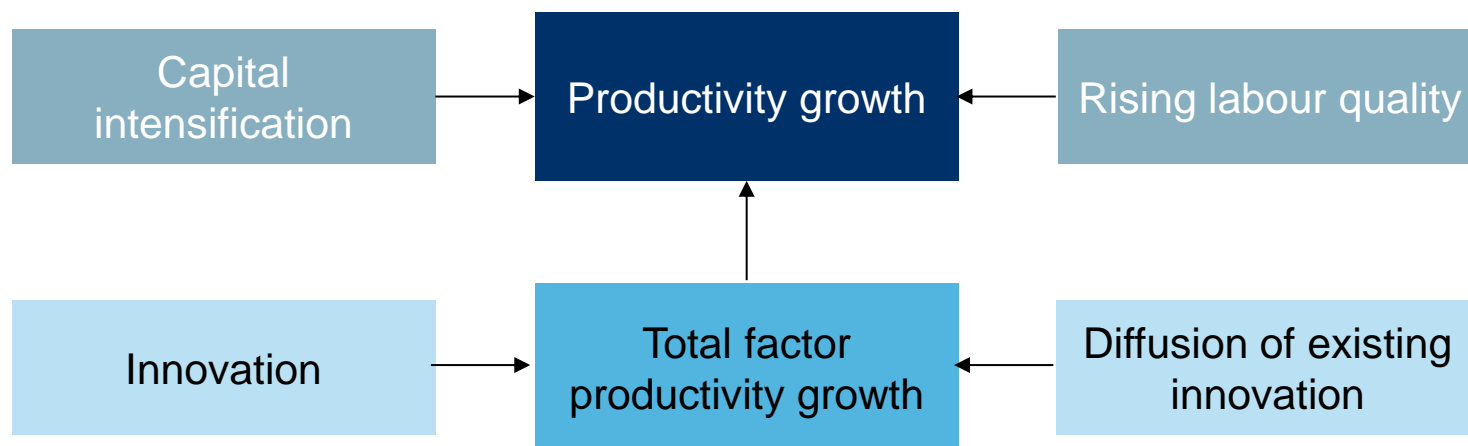
Canadian productivity:

What is wrong and what can be done

Defining productivity

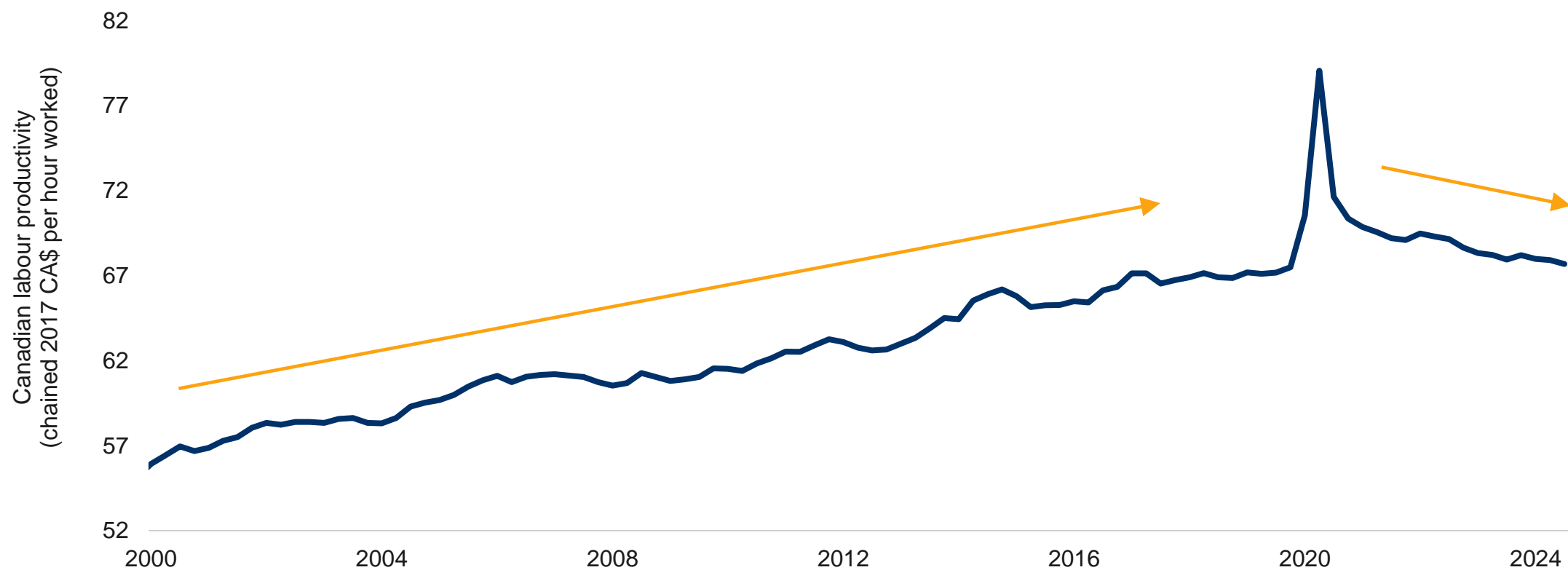
$$\text{Labour productivity} = \text{Economic output} / \text{hours worked}$$

Want to get as much as possible out of each unit of human effort



Acute recent productivity problem in Canada

Canadian productivity has been declining



Note: As of Q3 2024. There is no assurance that any of the trends depicted or described herein will continue.

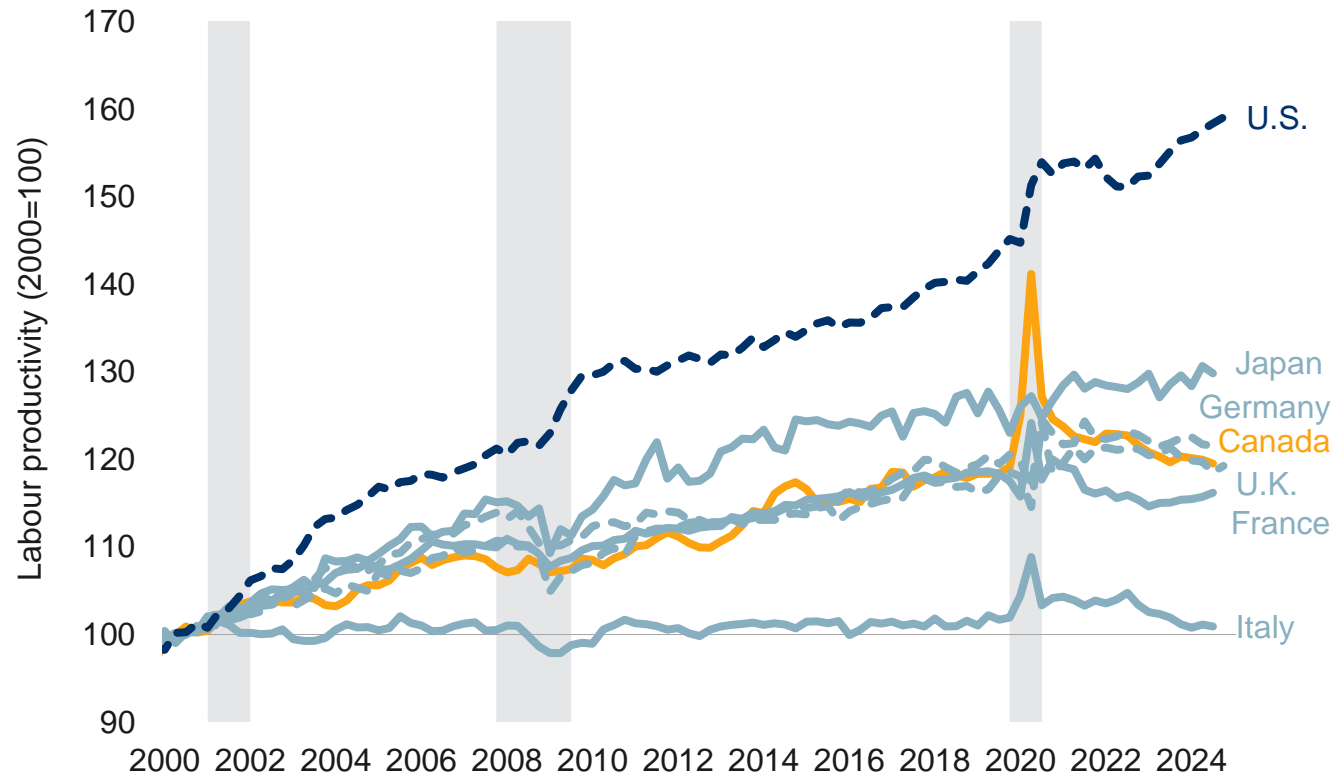
Source: Statistics Canada, Haver Analytics, Macrobond, RBC Global Asset Management (RBC GAM)

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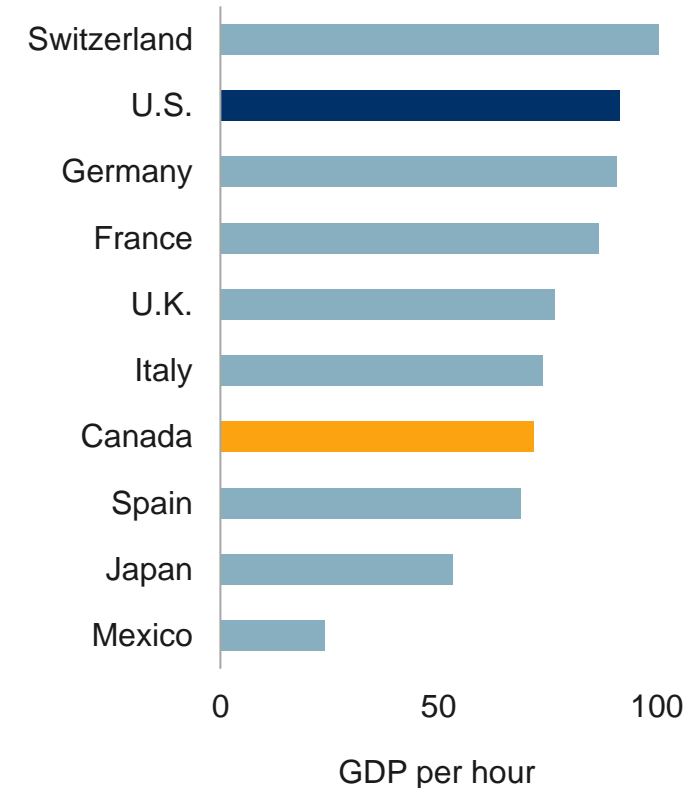
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Canadian productivity doesn't look quite as bad versus non-U.S. peers

U.S. outpaces other G7 countries in productivity gains



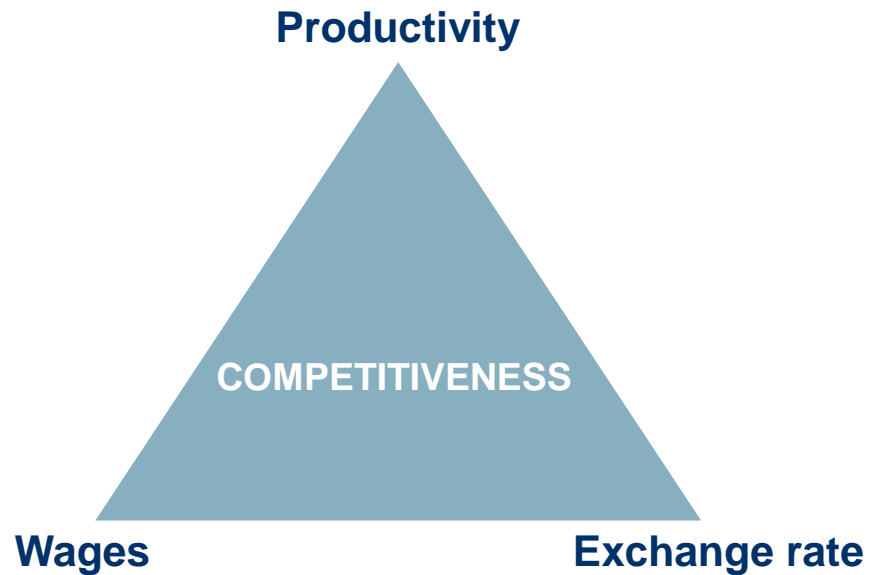
Productivity level



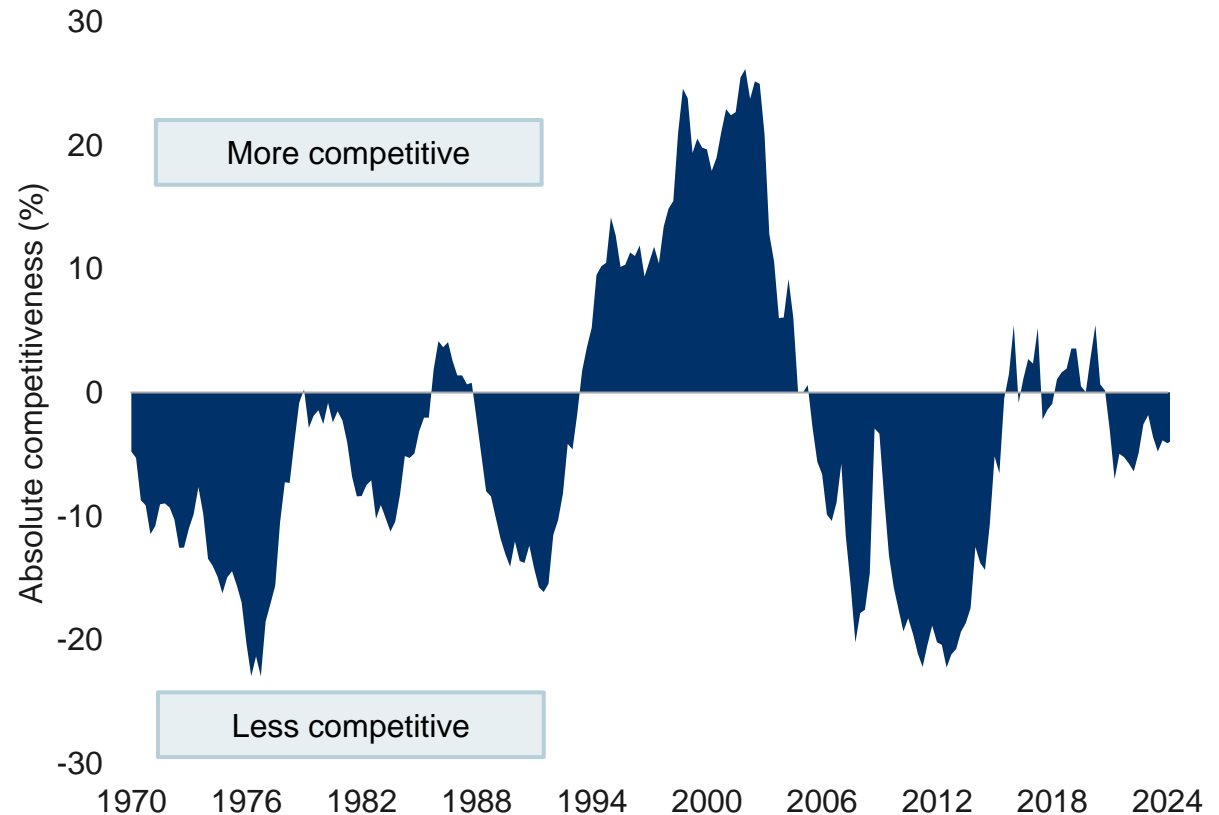
LHS: Note: As of Q4 2024 for U.K. and U.S., Q3 2024 for all other countries. Productivity measured as total economy/business sector/non-agricultural industry real output (in local currency) per hour of all persons. Shaded area represents U.S. recession. Source: Haver Analytics, Macrobond, RBC GAM

RHS: Note: As of 2022. GDP in current prices at PPP exchange rate US\$. Source: OECD, Macrobond, RBC GAM

Low wages and a weak exchange rate keep Canada reasonably competitive



Canada's competitiveness versus the world



LHS: Source: RBC GAM as at February 17, 2025.

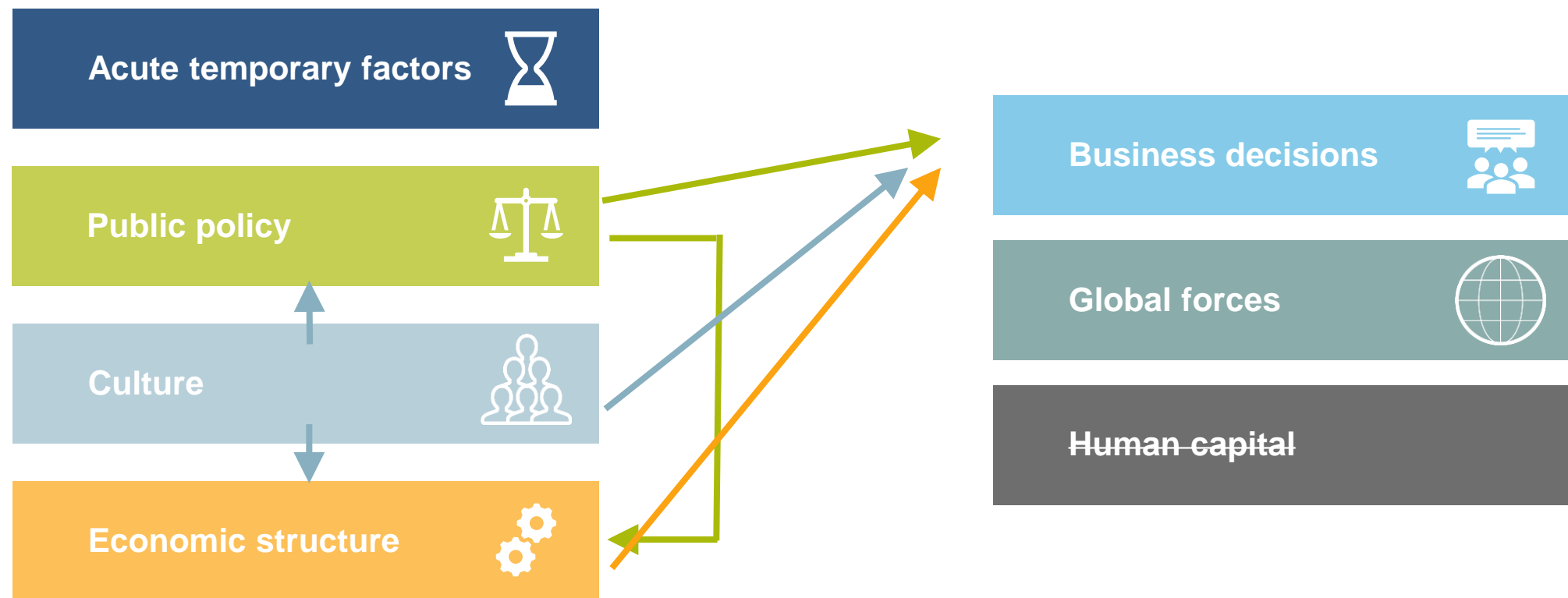
RHS: Note: OECD projections for 2024. Absolute competitiveness calculated as currency-adjusted unit labour cost ratio between Canada and its trading partners, vs. the average relationship from 1981 to 2011. Source: OECD Economic Outlook, Dec 2024, Macrobond, RBC GAM

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Productivity shortfall: Root causes

Roots of poor Canadian productivity



Source: RBC GAM as at February 12, 2025.

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Acute temporary factors

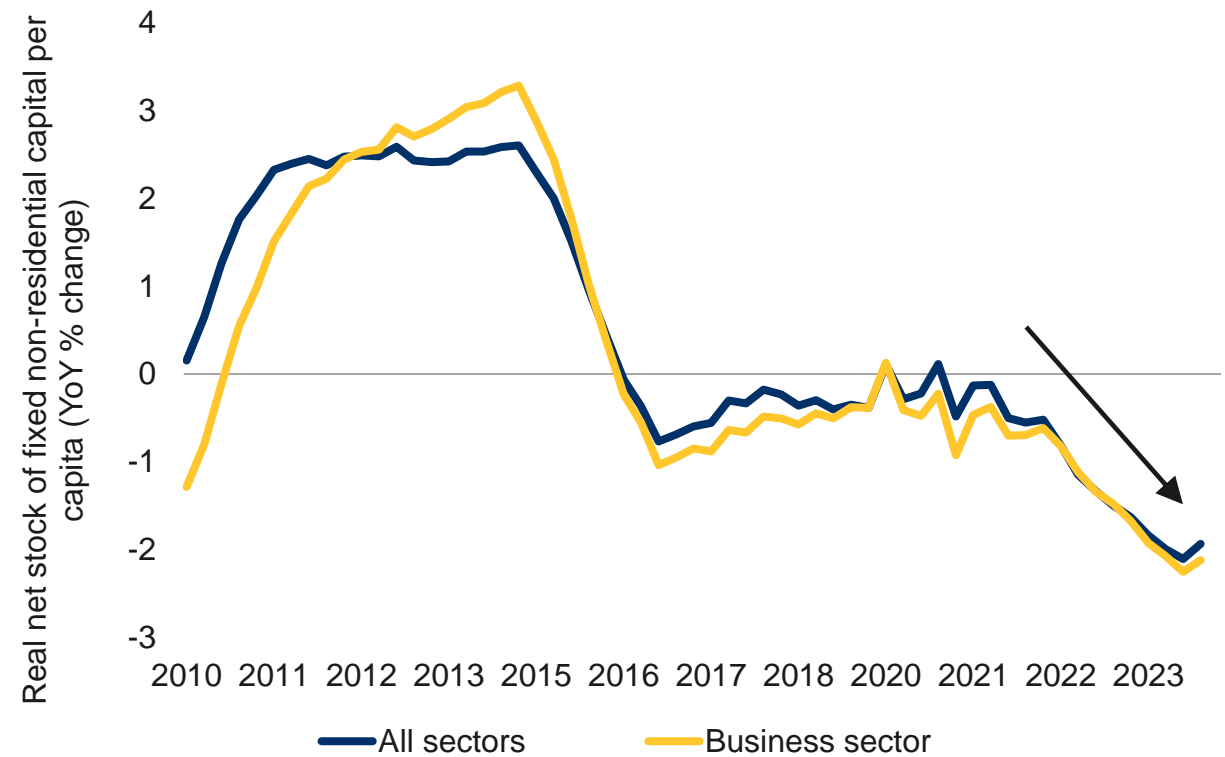
Canadian immigration surge

Lingering pandemic distortions

Rate shock

High uncertainty

Canadian capital stock per capita has been shrinking



LHS: Source: RBC GAM as at February 11, 2025.

RHS: As of Q3 2024. Statistics Canada, Macrobond, RBC GAM. There is no assurance that any of the trends depicted or described herein will continue.

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Economic structure

Challenging geography and climate

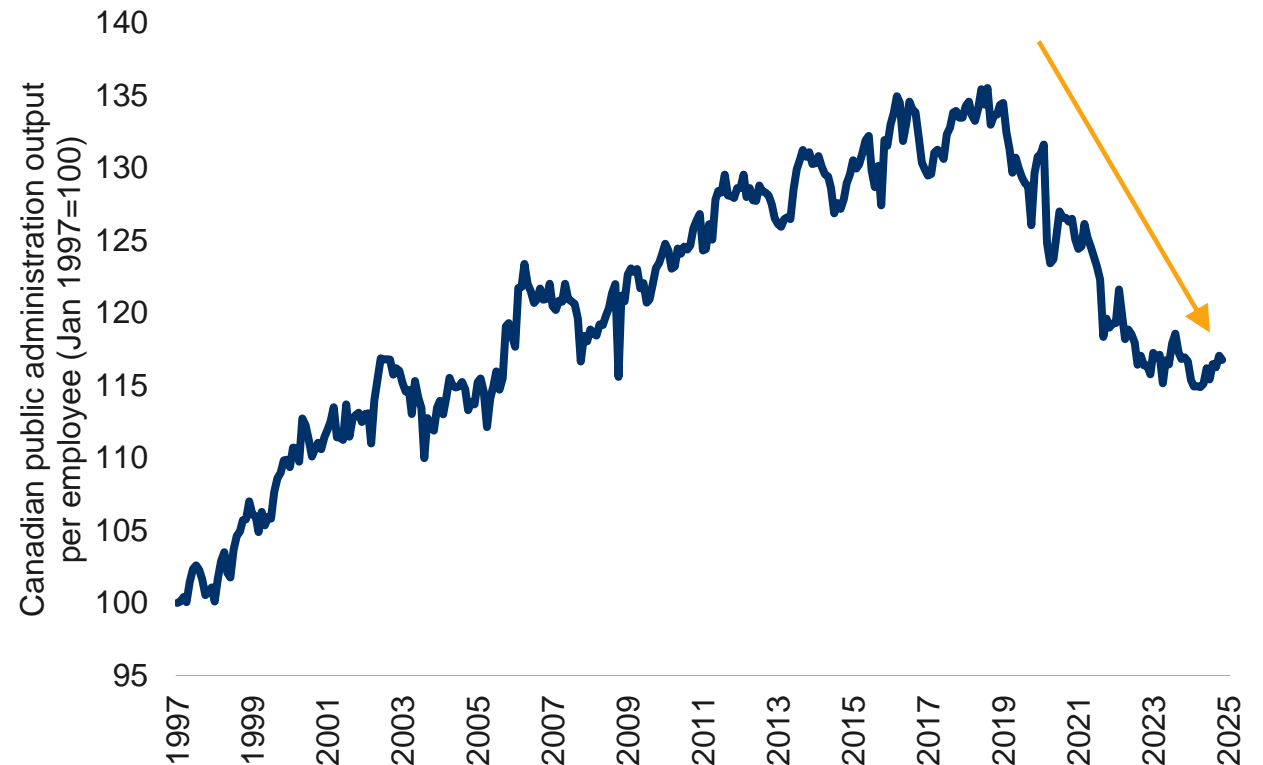
Low population density

Lack of scale

Canadian sector tilts

- Government
- Housing
- Oil and gas
- Supply management
- Large semi-oligopolistic service sectors
- Seasonal industries

Canadian public administration productivity dropped



LHS: Source: RBC GAM as at February 13, 2025.

RHS: Note: As of Nov 2024. There is no assurance that any of the trends depicted or described herein will continue. Source: Statistics Canada, Macrobond, RBC GAM

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Global forces

Global dampeners

- Global productivity trough for last 15 years
- Hard to match waves of 20th century tech

Global boosters

- Internet revolution still playing out
- AI may be next major technology
- Emerging markets (EM) nations like China now at tech frontier

Conclusion

- Scope for global productivity revival
- But expect slower growth than prior century

U.S. productivity waves



Source: RBC GAM as at February 20, 2025.

RHS: Note: As of 2024. Data prior to 1948 is consumption per capita growth; 1948 and later is growth of standard output per hour. Source: R. Shiller, Haver Analytics, RBC GAM

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Canadian public policy

Taxation

Regulatory

Size of government

Immigration

Rank	Personal income tax rate	Corporate income tax rate	Tax revenue as a % GDP	Government R&D support % GDP
Best ↑ ↓ Worst	MEX 35.0	SUI 19.7	MEX 17.7	GBR 0.48
	SUI 41.5	ESP 25.0	USA 25.2	FRA 0.42
	USA 43.7	GBR 25.0	SUI 27.1	USA 0.26
	ESP 45.0	USA 25.8	JPN 34.4	CAN 0.25
	GBR 45.0	FRA 25.8	CAN 34.8	ESP 0.22
	ITA 47.2	CAN 26.2	GBR 35.3	JPN 0.14
	DEU 47.5	ITA 27.8	ESP 37.3	ITA 0.11
	CAN 53.5	JPN 29.7	DEU 38.1	DEU 0.07
	FRA 55.4	DEU 29.9	ITA 42.8	SUI 0.03
	JPN 55.9	MEX 30.0	FRA 43.8	MEX 0.02

Need policies that are more competitive than U.S., not merely as competitive

LHS: Source: RBC GAM as at February 17, 2025.

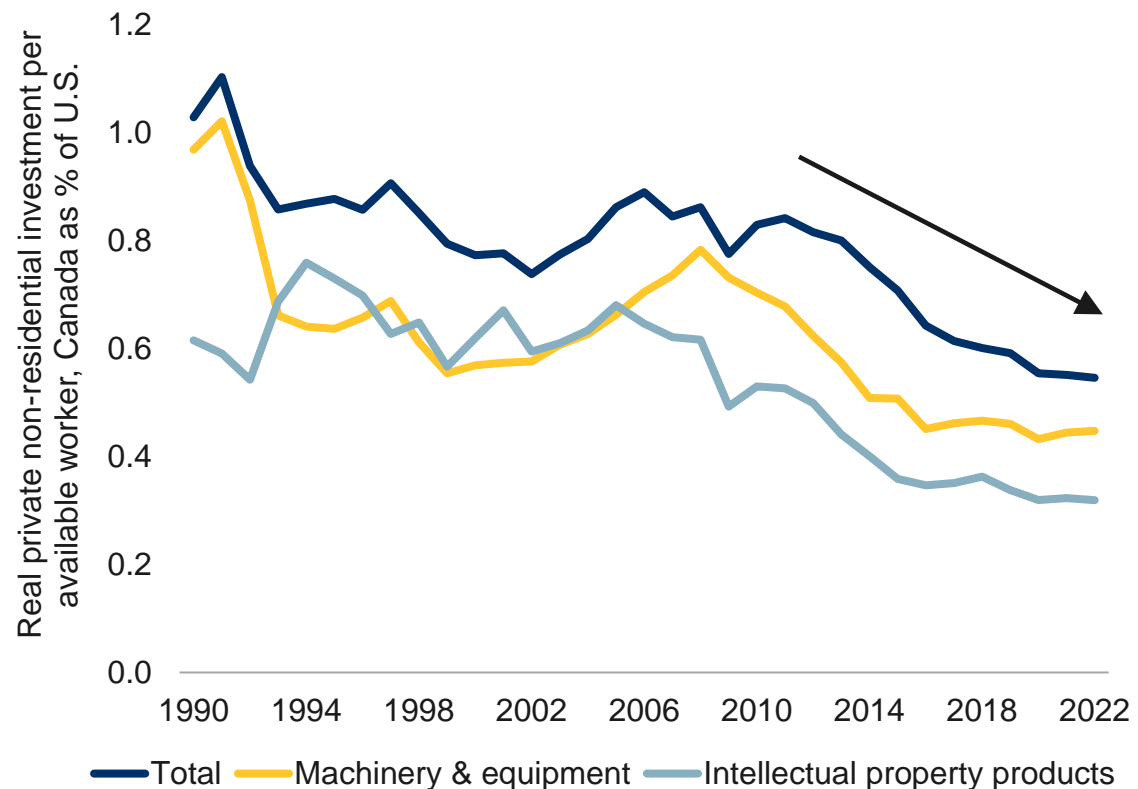
RHS: Note: As of 2022 for Personal Income Tax, 2023 for Corporate Income Tax and Tax Revenue, and 2021 for Government R&D Support. Government R&D Support defined as direct government funding and government tax support for business R&D. Source: OECD, Macrobond, RBC GAM

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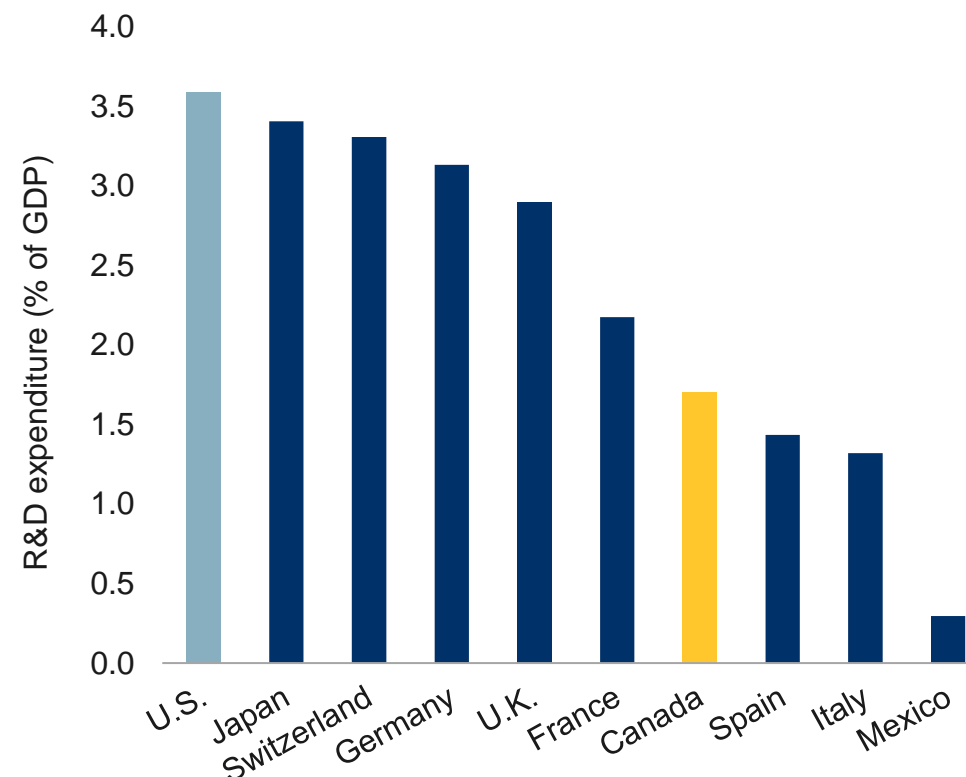


Business decisions

Business investment in Canada has fallen behind the U.S.



Expenditure on R&D by country



LHS: Note: As of 2023. U.S. real private investment converted to Canadian dollars using purchasing power parity-based exchange rates. Source: C.D. Howe Institute, Haver Analytics, RBC GAM

RHS: Note: Based on latest data available, ranging from 2021 to 2023. Source: OECD, Macrobond, RBC GAM

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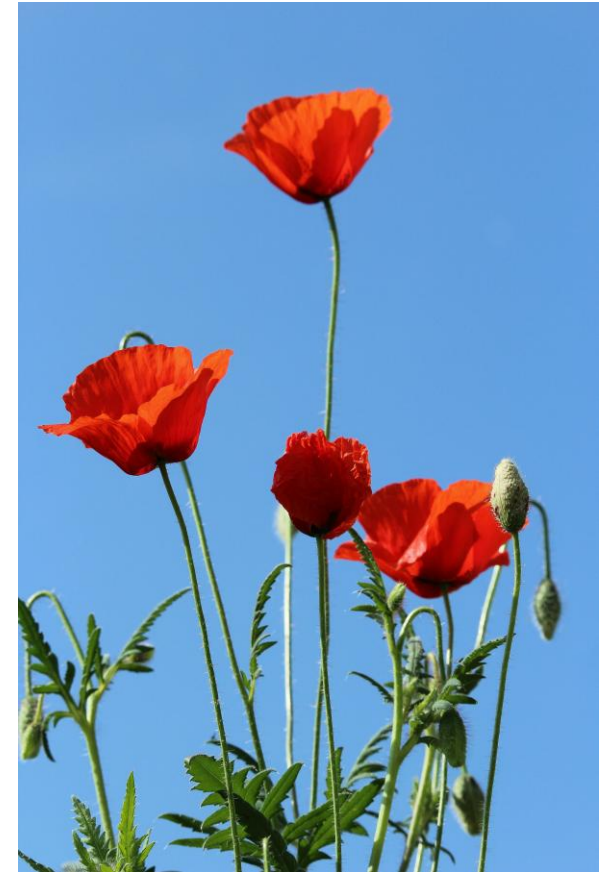
Canadian culture

Risk-averse culture

Complacency

Antagonism toward success

Tall poppy syndrome



Source: RBC GAM as at February 12, 2025.
RHS: Source: pexels.com

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Canadian productivity conclusions

Importance

Paramount

Challenge

Big, multi-faceted problem

Opportunity

Plenty of areas for improvement

Catalysts

- Recent economic underperformance
- End of massive immigration
- Tariff threat
- Canadian election
- New technologies

Outlook



- Room for faster productivity growth
- Probably happens gradually
- Aspire to boost Canadian productivity growth from +1.0%/yr to +1.5%/yr
- Aspire for prosperity to rise 50% faster!
- Aspire for Canadians to become 16% more prosperous than otherwise within a generation

Markets



- Stronger Canadian dollar
- Higher earnings / faster equity gains
- Slightly higher interest rates

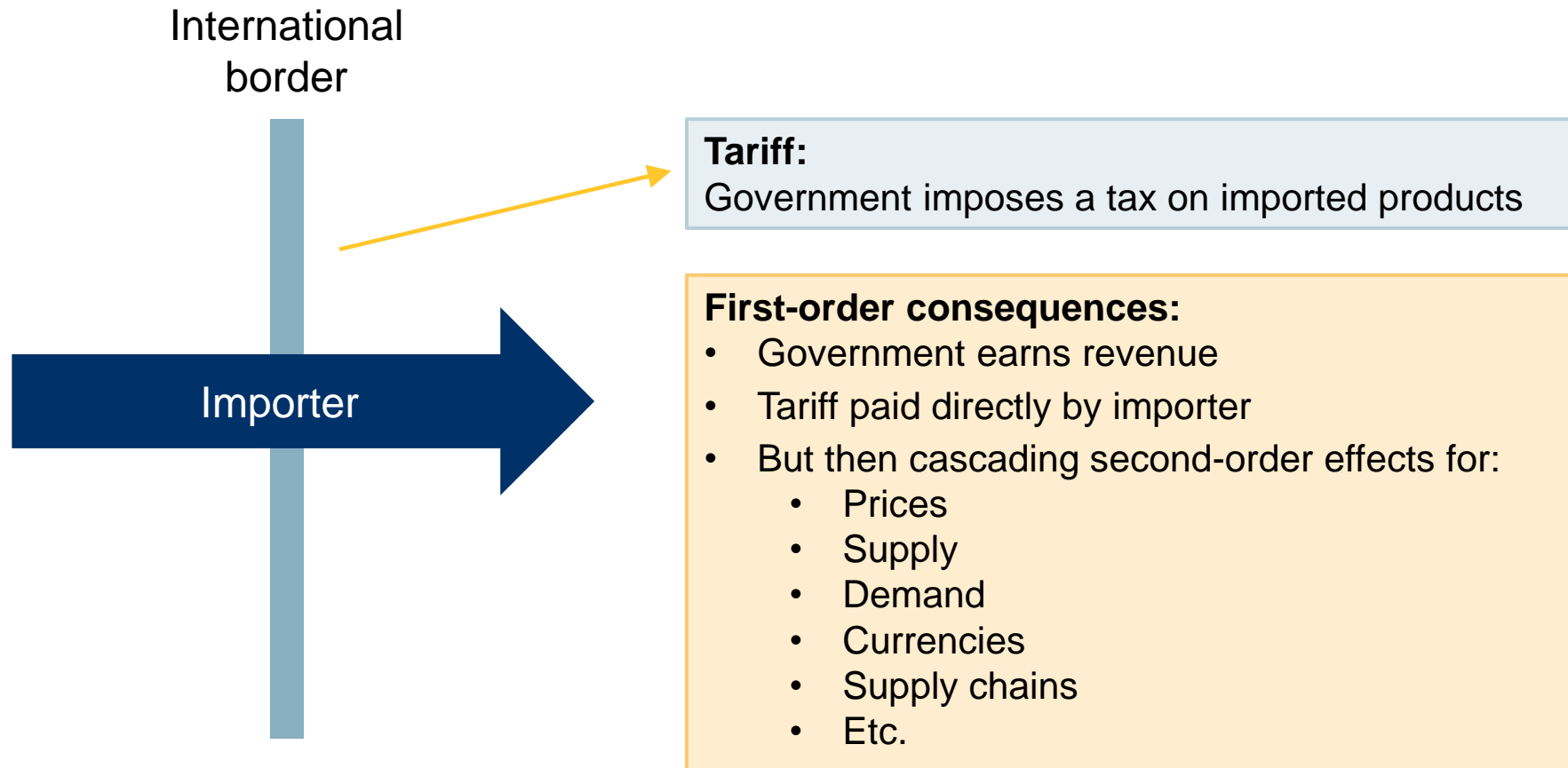
Source: RBC GAM as at February 17, 2025.

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Tariffs in focus:

Outlook, response and impact

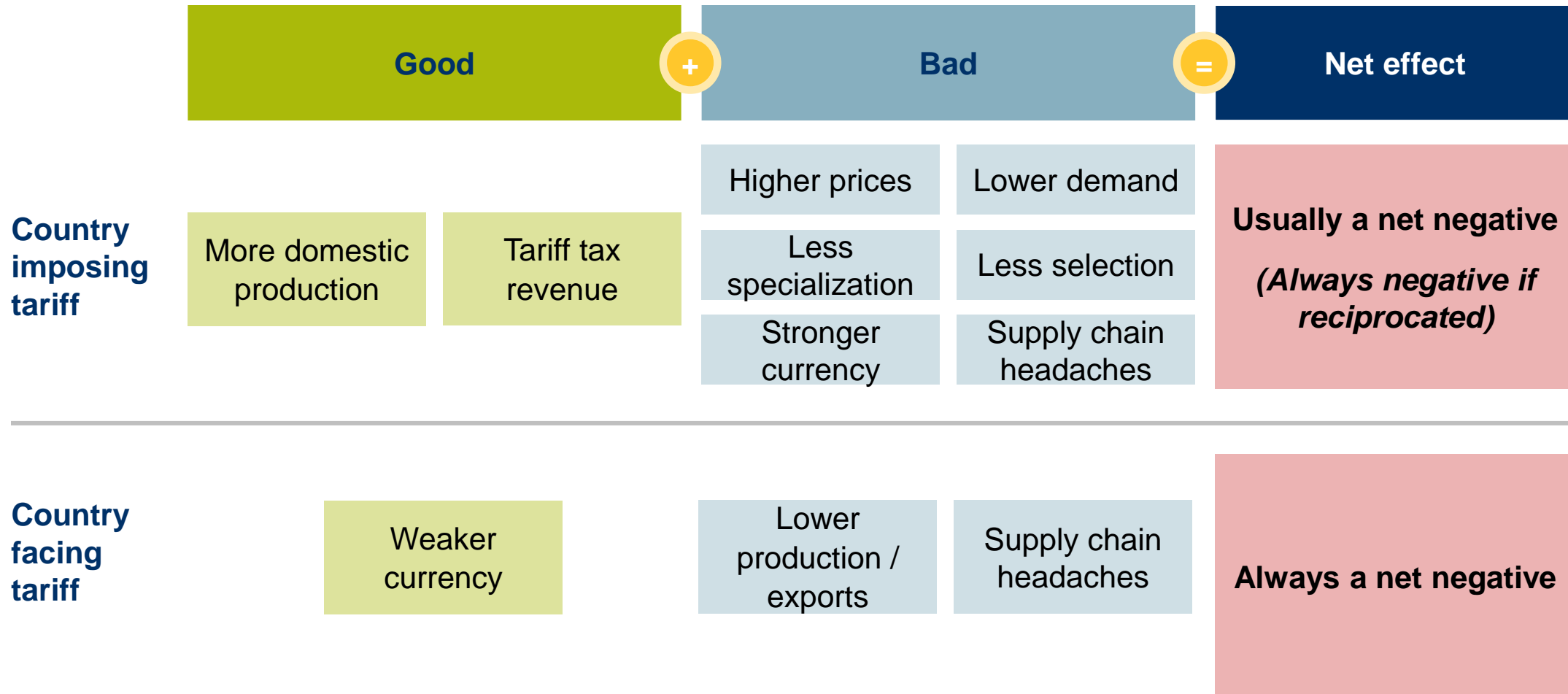
What is a tariff?



Source: RBC GAM as at February 17, 2025.

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Economic damage from tariffs is not back-of-the-envelope math



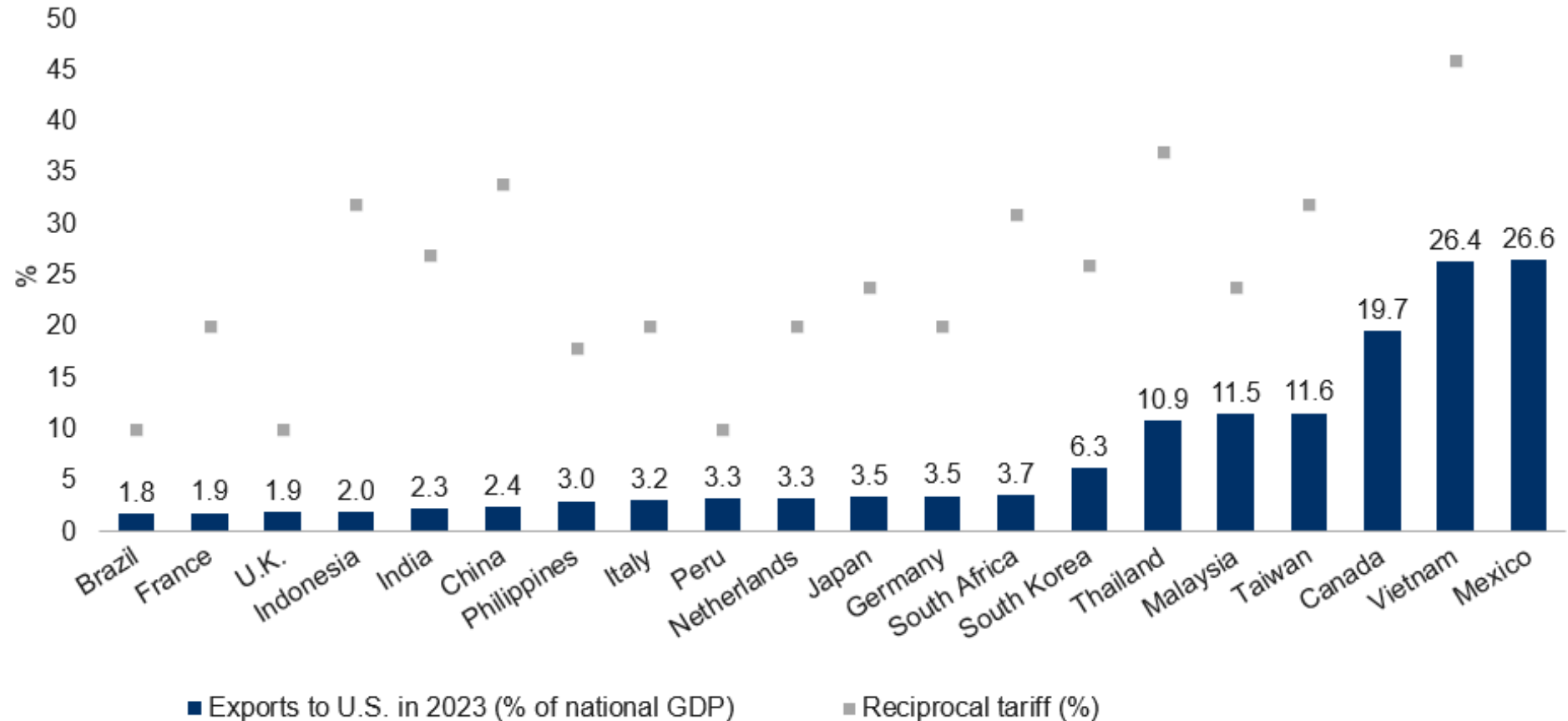
Source: RBC GAM as at February 17, 2025.

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Whose economy is most exposed to U.S. tariffs?

1) Countries with big exposure to U.S. demand; 2) Countries with big reciprocal tariffs

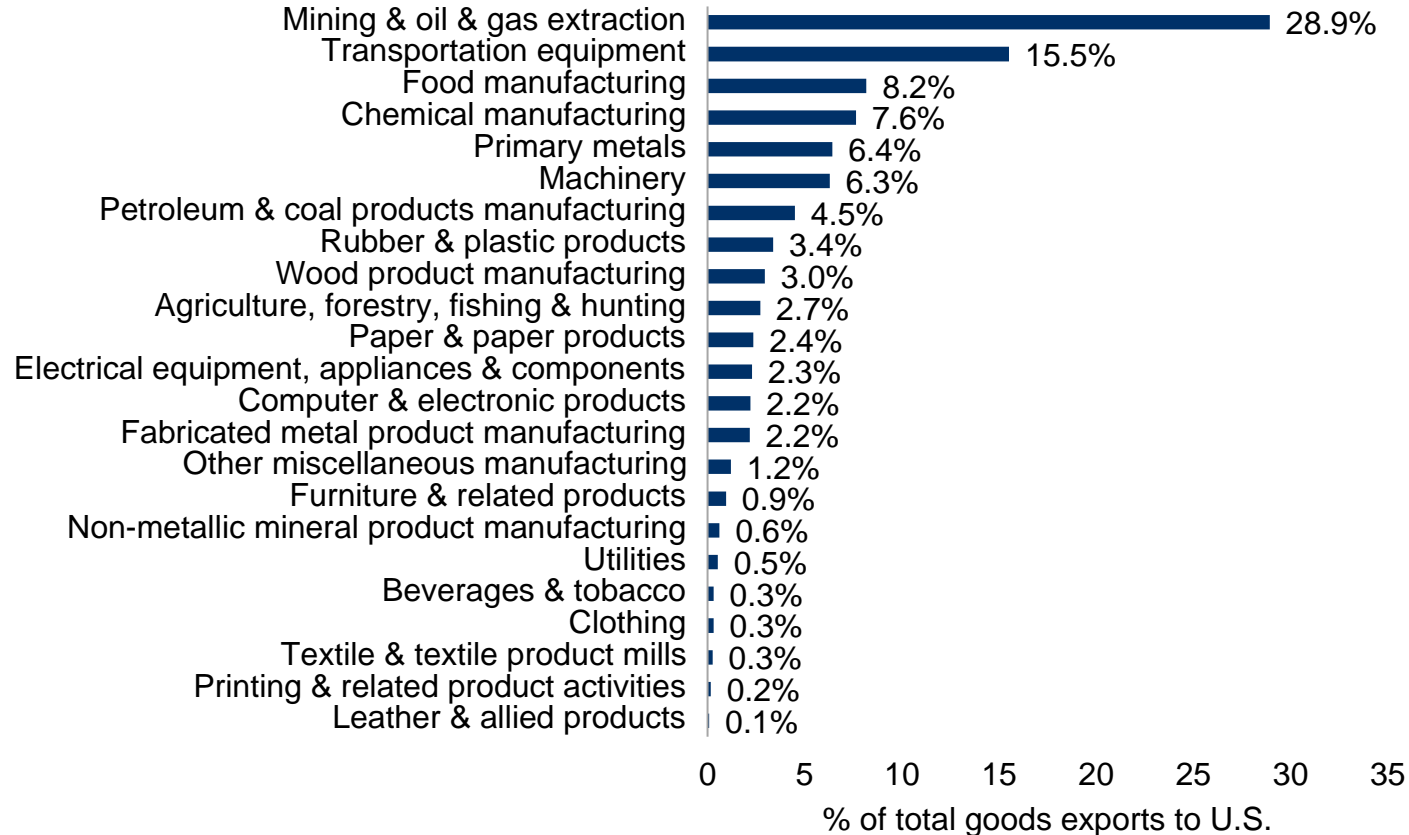
Exports to U.S. are significant for some countries



Note: Reciprocal tariffs announced by the Trump administration on April 2, 2025. Source: IMF, The White House, Macrobond, RBC GAM

Canada-U.S. trade factors

Canadian goods exports to U.S. by industry



> Canada is second-largest exporter to US, after Mexico and ahead of China

> Canada is the #1 importer of U.S. products

> Overall U.S. trade deficit with Canada is just US\$45 billion, not the US\$200 billion that has been cited

> Canada is a net importer of manufactured goods from U.S.

> Canada is a net importer of services from the U.S.

> Without Canadian energy exports to the U.S., the trade surplus flips to deficit

LHS: Note: Share of goods exports based on 12-month total as of Dec 2024. Source: Government of Canada, Department of Innovation, Science & Economic Development, Macrobond, RBC GAM
 RHS: Source: RBC GAM as at January 29, 2025.

Tariff proposals and implementation

Large, problematic tariffs are constantly evolving

U.S. tariff proposal	Implementation	Commentary
Canada and Mexico tariffs (25%)	Implemented On March 4	Implemented, then mostly lifted on Mar 6 Could yet be revived at a later date
China tariff (up to 145%)	Implemented On Feb 4, Mar 4, Apr 2, Apr 9	China has retaliated; US tariff rate was as high as 145% 90-day reduction to 30% announced in early May
Steel and aluminum tariffs (25% → 50%)	Implemented On Mar 12, Increased Jun 4	Affect Canada the most “Only” lasted 14 months in first Trump term
Reciprocal tariffs	Executive order Implemented Apr 5/9	Big tariffs on a range of countries – Implementation delayed 90 days But Canada and Mexico have initially avoided further tariffs
Auto sector tariff (25%)	Implemented On Apr 3	Auto tariffs implemented, including on Canada and Mexico
Sector-specific tariffs	Mentioned often Awaiting details	Copper, pharma, chips, forestry?
Other tariffs	Mentioned	Threat of 50% tariff on European Union

Note: As at 05/28/2025. Colour coding conveys degree of risk from each type of tariff, defined as the interplay of likelihood and impact. Source: RBC GAM

Major tariff-related economic forces

United States

Force	Impact	Description
Tariffs	Substantial negative	Higher prices, lower demand, less specialization, less selection
Uncertainty	Upfront negative	Freezes capital expenditure and hiring
U.S. products boycotted	Small supplemental negative	Lower demand for U.S. products
Long-term reputational damage	Small enduring negative	Enduring loss of trust in U.S. policy / as reliable partner
On-shoring encouraged	Small long-term positive	U.S. manufacturing base slightly bolstered?
Monetary stimulus	Lagged positive	Output loss dominates increase in prices
Fiscal stimulus	Positive?	Some measure of fiscal support?

Canada

Force	Impact	Description
Tariffs	Negative force of uncertain magnitude	Higher prices, lower demand, less specialization, less selection
Uncertainty	Upfront negative	Freezes cap ex and hiring
Canadian boycott of U.S. products	Small supplemental negative	Canadians may simply buy fewer products
On-shoring toward U.S.	Small long-term negative	Canadian manufacturing base slightly diminished?
Monetary stimulus	Lagged positive	Output loss dominates increase in prices
Fiscal stimulus	Positive	Unemployment and industry support

Base-case macro assumption for Trump presidency

Trump policy expectations – tariffs tilt economy toward more negative interpretation

Policy	Short-term economy	Inflation (+ is higher)
Overall effect	—	+ +
➔ Tariffs	— — —	+ + +
Immigration	— —	neutral
Regulations	+ +	neutral
Taxes	+ +	+
Animal spirits	+	+
Gov't spending	—	—

Note: As at April 3, 2025. Source: RBC GAM
+/- indicate positive/negative impact on variable at top of column.

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Fracturing international order

- > Transition from hegemonic to multi-polar era
- > De-globalization
- > Spheres of influence form

Implications:

- Protectionism: tariffs, nationalism
- Prior international norms undermined
- National borders more malleable?
- Slower growth / higher inflation
- Trend to persist for extended period



Source: RBC GAM as at February 12, 2025

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