

# A growth regimes perspective on Canada's transition to private debt-led growth since the Global Financial Crisis

Theodore Klassen

Frontiers in Growth Regimes Research: Theoretical Perspectives &  
Country Cases  
IPE Berlin Online Workshop  
October 7, 2022

# Motivation

## Pre-GFC

- Frequent celebration of the “exceptionalism” of Canada’s policy regime
- Inflation-targeting; labour market flexibilization policies; hegemonic norm of balanced budgets; and, especially, free trade agreements with the US (1988) and with the US and Mexico (1994).

## Post-GFC

- “Household debt exceeded 170 percent of disposable income in 2019, one of the highest levels among G20 countries” (IMF 2021).
- “Debt-to-assets and debt service-to-income ratios for non-financial corporates at end 2019 were the highest among the G7” (IMF 2021).

# Approaches to Canadian political economy

## **Dependency or 'staples' theory**

- Focus on foreign ownership (Levitt 1970; Clement 1977).
- Or the role of primary commodity 'staples' exports (Watkins 1963; Stanford 2008, 2019).

## **Marxism**

- Conceptual frame on accumulation (McCormack/Workman 2015).
- Linked to the state (Panitch 1977; Albo/Jenson 1997).
- Corporate power (Carroll 1986).
- Internationalization of Canadian capital (Klassen 2009, 2014).

## **Capital as Power**

- Investigation of the differential accumulation of dominant capital (Brennan 2013, 2014).

# Background: 'Staples' U-turn



Figure 4.1 Composition of Canadian exports

Source: Stanford (2019).

# Background: Patterns of trade

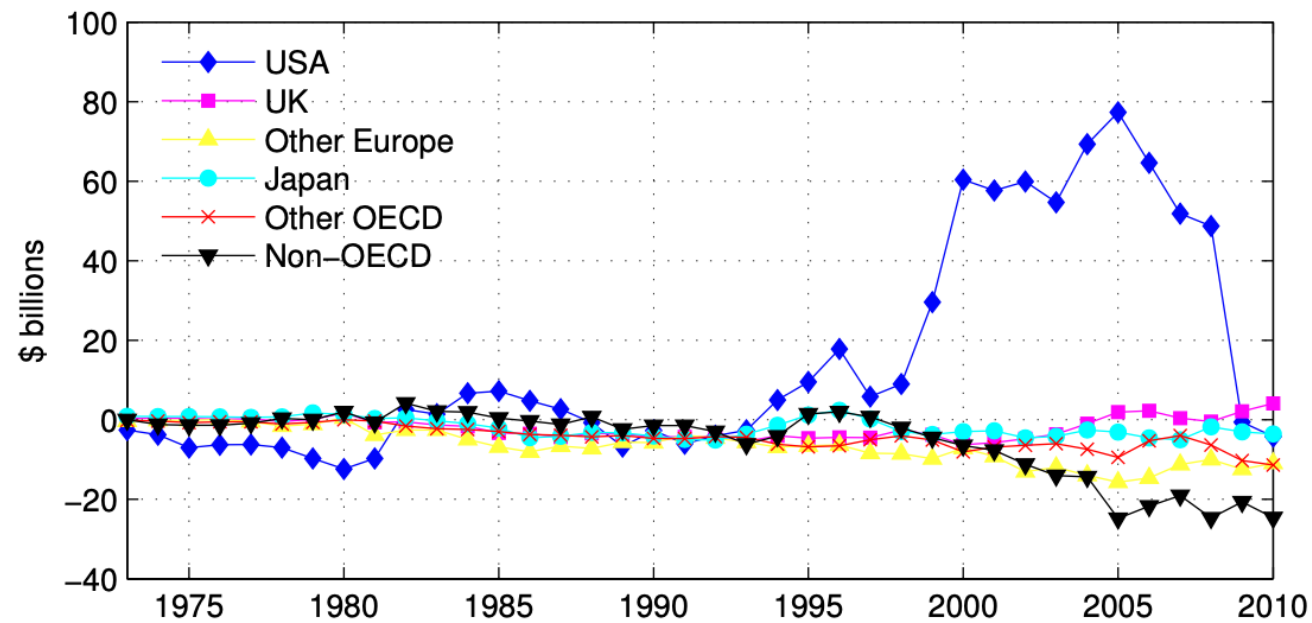


FIGURE 4. Canada's Trade Balance by Region, 1970-2010<sup>14</sup>

# Post-Keynesian macro: a demand-centred approach

## **Growth regimes**

- Typology derived from patterns of sectoral financial balances and growth contributions by component of GDP (e.g. Dodig et al. 2016; Dünhaupt/Hein 2019).
- Analytical focus on the sources and financing of demand.

## **Macroeconomic policy regime**

- Assessment of the demand effects of each lever of macroeconomic policy (monetary, fiscal, and incomes policy) as well as of open economy conditions (e.g. Hein/Martschin 2021).
- Derived from the optimal post-Keynesian policy mix to support a stable domestic demand-led regime.

# Typology of growth regimes

Export-led mercantilist	Weakly export-led	Domestic demand-led	Debt-led private demand boom
<ul style="list-style-type: none"> <li>• Positive financial balances of the private sector, and the private household sector;</li> <li>• negative financial balances of the external sector;</li> <li>• positive balance of goods and services;</li> <li>• positive growth contributions of net exports.</li> </ul>	<p>Either</p> <ul style="list-style-type: none"> <li>• positive financial balances of the private sector,</li> <li>• negative financial balances of the external sector,</li> <li>• positive balance of goods and services;</li> <li>• negative growth contributions of net exports.</li> </ul> <p>Or</p> <ul style="list-style-type: none"> <li>• negative but improving financial balances of domestic sectors;</li> <li>• positive but declining financial balances of external sector;</li> <li>• negative but improving net exports;</li> <li>• positive growth contributions of net exports.</li> </ul>	<ul style="list-style-type: none"> <li>• Positive financial balances of the private household sector and positive or balanced financial balances of the private sector as a whole;</li> <li>• balanced or positive financial balances of the external sector;</li> <li>• growth is almost exclusively driven by domestic demand;</li> <li>• around zero growth contribution of net exports.</li> </ul>	<ul style="list-style-type: none"> <li>• Negative or close to balance financial balances of the private sector;</li> <li>• positive financial balances of the external sector;</li> <li>• significant growth contributions of domestic demand, and private demand in particular;</li> <li>• negative growth contributions of net exports.</li> </ul>

Source: Dünhaupt/Hein (2019, 458).

# Results

**Table 1: Indicators for Canada's demand and growth regime, averages per trade cycle**

	1983-1991	1992-2000	2001-2009	2010-2020
Financial balances of the external sector, per cent of nominal GDP	2.23	1.09	-0.94	3.54
Financial balances of the public sector, per cent of nominal GDP	-6.85	-3.32	0.25	-2.15
Financial balances of the private sectors, per cent of nominal GDP	4.62	2.16	0.64	-1.52
— Financial balances of households, per cent of nominal GDP	3.97	1.12	-3.29	-2.80
— Financial balances of corporations, per cent of nominal GDP	0.64	1.04	3.93	1.28
Real GDP growth, per cent	2.70	3.43	1.74	1.57
Growth contribution of domestic demand, percentage points	3.05	2.73	2.70	1.57
— Growth contribution of households and NPISH, percentage points	1.61	1.71	1.69	0.99
— Growth contribution of general governments, percentage points	0.53	0.07	0.50	0.28
— Growth contribution of gross fixed capital formation and investment in inventories, percentage points	0.91	0.95	0.51	0.30
Growth contribution of the balance of goods and services, percentage points	-0.37	0.68	-0.94	0.00
— Growth contribution of exports, percentage points	1.50	3.16	-0.39	0.71
— Growth contribution of imports, percentage points	1.87	2.49	0.54	0.71
Net exports of goods and services as a share of nominal GDP, per cent	1.29	2.46	3.23	-1.79
Regime	DDL	'Rising' WEL	'Falling' WEL	DLPD

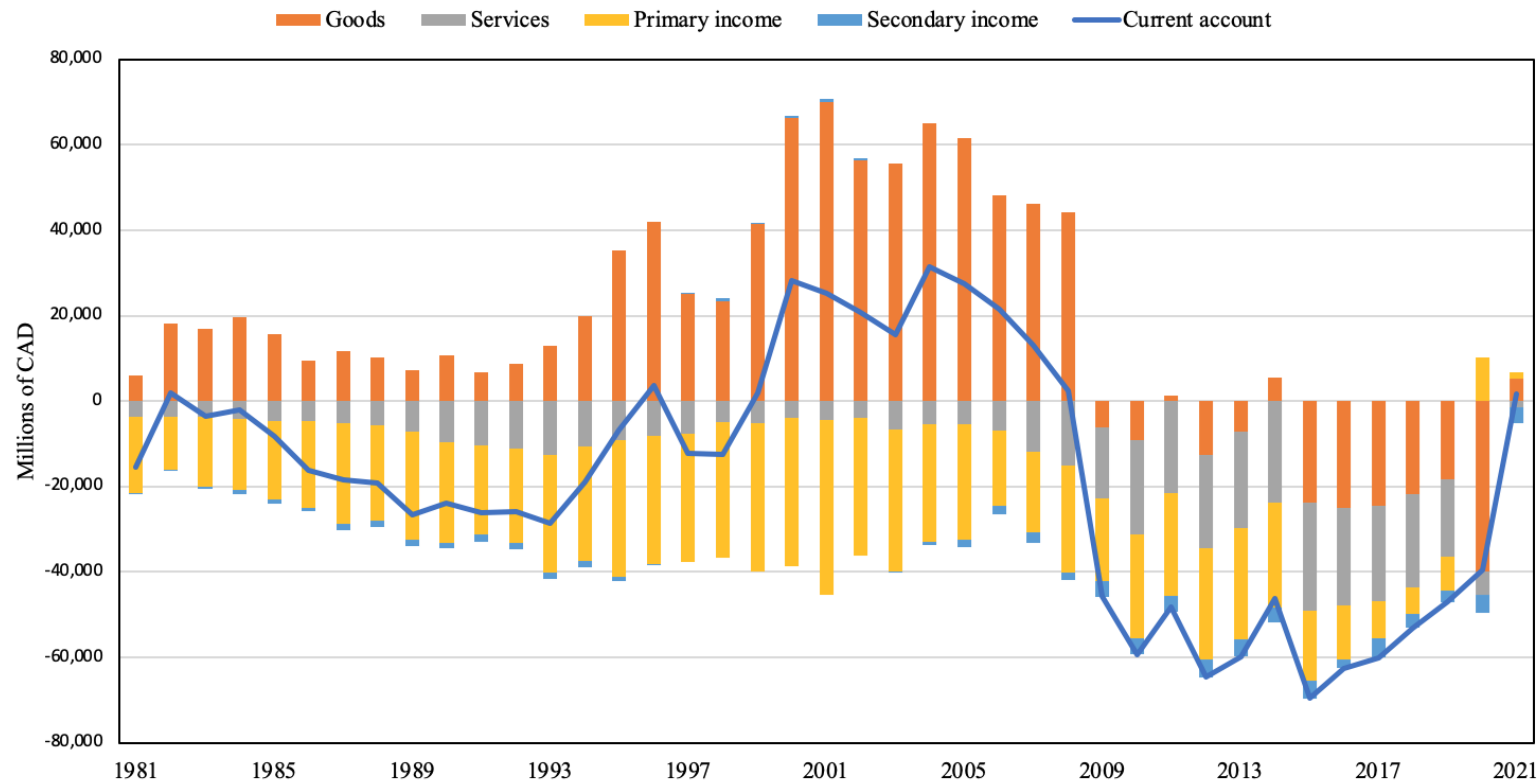
**Source:** Statistics Canada (2021a; 2022d; 2022e; 2022f; 2022g; 2022h), author's calculations and representation.

**Notes:** *DDL*, domestic demand-led; *DLPD*, debt-led private demand boom; *WEL*, weakly export-led; *NPISH*, non-profit institutions serving households.



# Current account

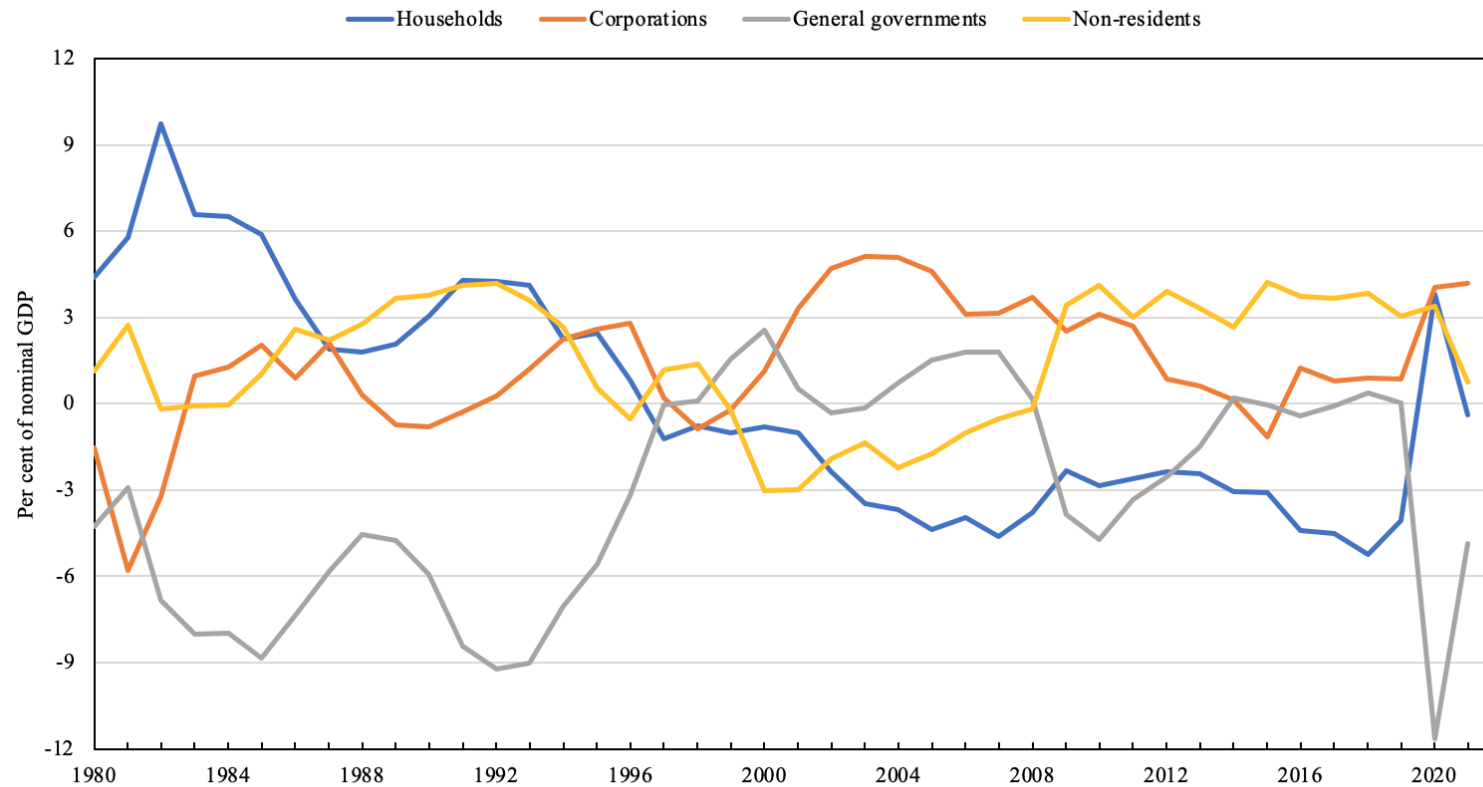
**Figure 1: Current account**



Source: Statistics Canada table (2022c), author's representation.

# Sectoral financial balances

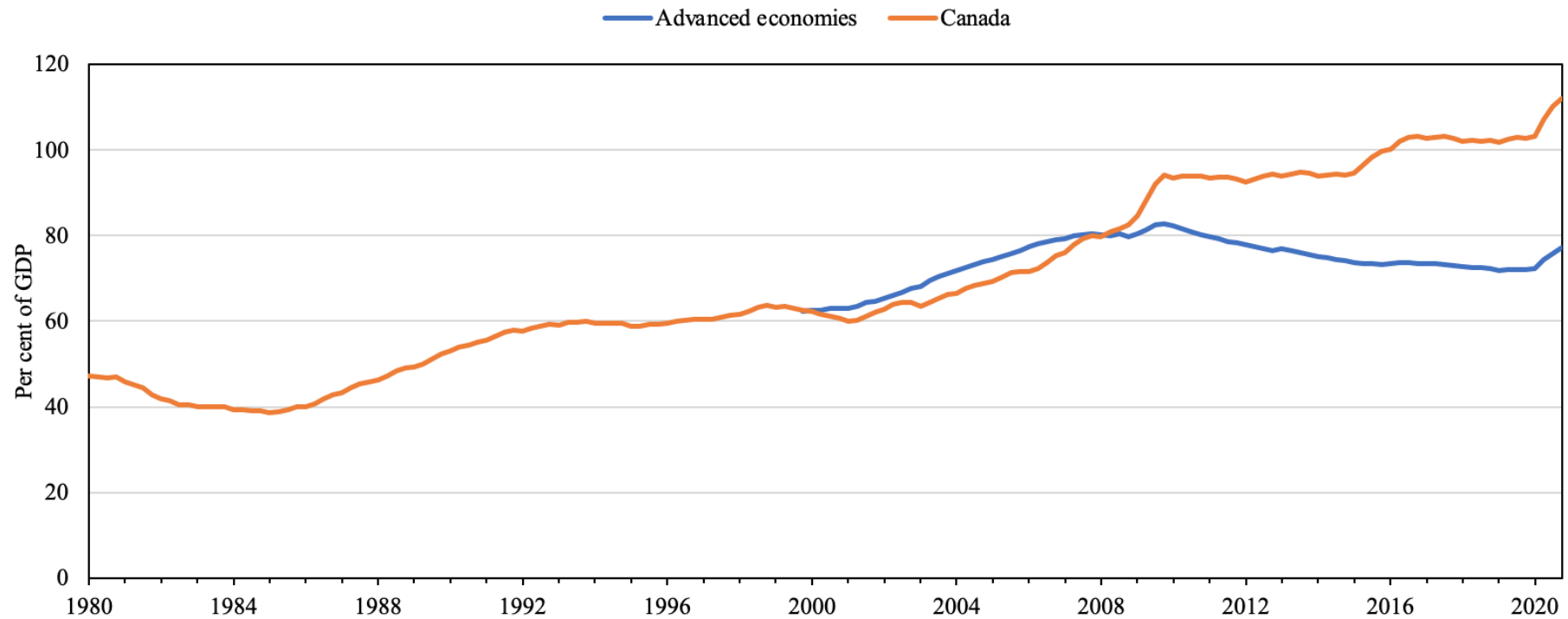
**Figure 2: Sectoral financial balances**



Source: Statistics Canada (2022d; 2022e; 2022f; 2022g; 2022h), author's calculations and representation.

# Household debt ratios

**Figure 3: Household sector debt-to-GDP ratios**



**Source:** BIS (2021), author's representation.

**Note:** The figure displays credit to households and NPISHs from all sectors at market value.

# Macroeconomic policy regime

## Monetary policy

- Should target a slightly positive real long-term interest rate that is equal or less than real GDP growth to foster investment and support demand; role also for financial regulation and stability.
- **Indicator:** real long-term interest rate-real GDP growth differential.

## Incomes policy

- Should support nominal stabilization by linking unit labour cost growth to the target rate of inflation.
- **Indicators:** ULC growth rate and Bank of Canada inflation target; adjusted wage share.

## Fiscal policy

- Should act counter-cyclically to stabilize demand at non-inflationary full employment; role also for redistribution and public investment.
- **Indicators:** movement of general government structural balance and the output gap.

# Results

**Table 2: Canadian macroeconomic policy regime indicators, average annual values**

	1983-1991	1992-2000	2001-2009	2010-2020
<b>Monetary policy</b>				
Short-term real interest rate, per cent	5.53	3.75	1.02	-0.52
Long-term real interest rate, per cent	5.71	5.30	2.35	0.31
Long-term real interest rate minus real GDP growth, percentage points	3.01	1.86	0.61	-1.27
<b>Labour market policy</b>				
Nominal unit labour costs, annual growth, per cent	3.43	1.29	2.29	1.71
Inflation rate (CPI), per cent	4.67	1.59	2.04	1.65
Adjusted wage share, per cent	58.02	57.76	55.11	55.59
Change in adjusted wage share from previous business cycle	-1.38	-0.27	-2.64	0.48
<b>Fiscal policy</b>				
General government structural balance as percentage of potential GDP, annual change, percentage points	-0.25	0.99	-0.38	-0.55
Output gap as percentage of potential GDP, annual change, percentage points	0.23	0.42	-0.61	-0.01
Number of years with pro-cyclical fiscal policy (co: contractionary, ex: expansionary)	4 (1 co, 3 ex)	3 (2 co, 1 ex)	3 (1 co, 2 ex)	6 (4 co, 2 ex)
General government gross fixed capital formation, per cent of GDP (chained 2012 dollars)	3.19	3.17	3.65	3.91
<b>Open economy</b>				
Change in real effective exchange rate, vis-à-vis 27 countries, per cent	0.72	-3.11	1.90	-0.90
OECD economic complexity index	n.a.	1.09*	0.98	0.94
Real exports of goods and services, per cent of GDP	20.89	31.37	33.68	31.25
Real imports of goods and services, per cent of GDP	16.97	24.46	28.49	31.78

Source: See Appendix.

Note: \* = data unavailable for years prior to 1998.

# Results

**Table 3: Macroeconomic policy regime assessment**

	1983-1991	1992-2000	2001-2009	2010-2020
Monetary policy stance	–	–	–	+
Wage and incomes policy stance	–	–	+/–	+
Fiscal policy stance	+	+	+	–/+
Open economy conditions	–	+	–	+
Demand and growth regime	DDL	‘Rising’ WEL	‘Falling’ WEL	DLPD

**Notes:** Inspired by a similar table in Hein and Martschin (2021, 515); *DLPD* = debt-led private demand; *DDL* = domestic demand-led; *WEL* = weakly export-led ; + : expansionary stance, – : contractionary stance, 0: neutral stance.

*Monetary policy:*

- + : negative real long-term interest rate-real GDP growth differential
- : positive real long-term interest rate-real GDP growth differential

*Wage policy:*

- + : nominal unit labour cost growth close to Bank of Canada inflation target and rising labour income share
- : nominal unit labour cost growth far away from Bank of Canada inflation target (after 1991) and falling labour income share
- + / – : nominal unit labour cost close to Bank of Canada inflation target (after 1991) and falling labour income share

*Fiscal policy:*

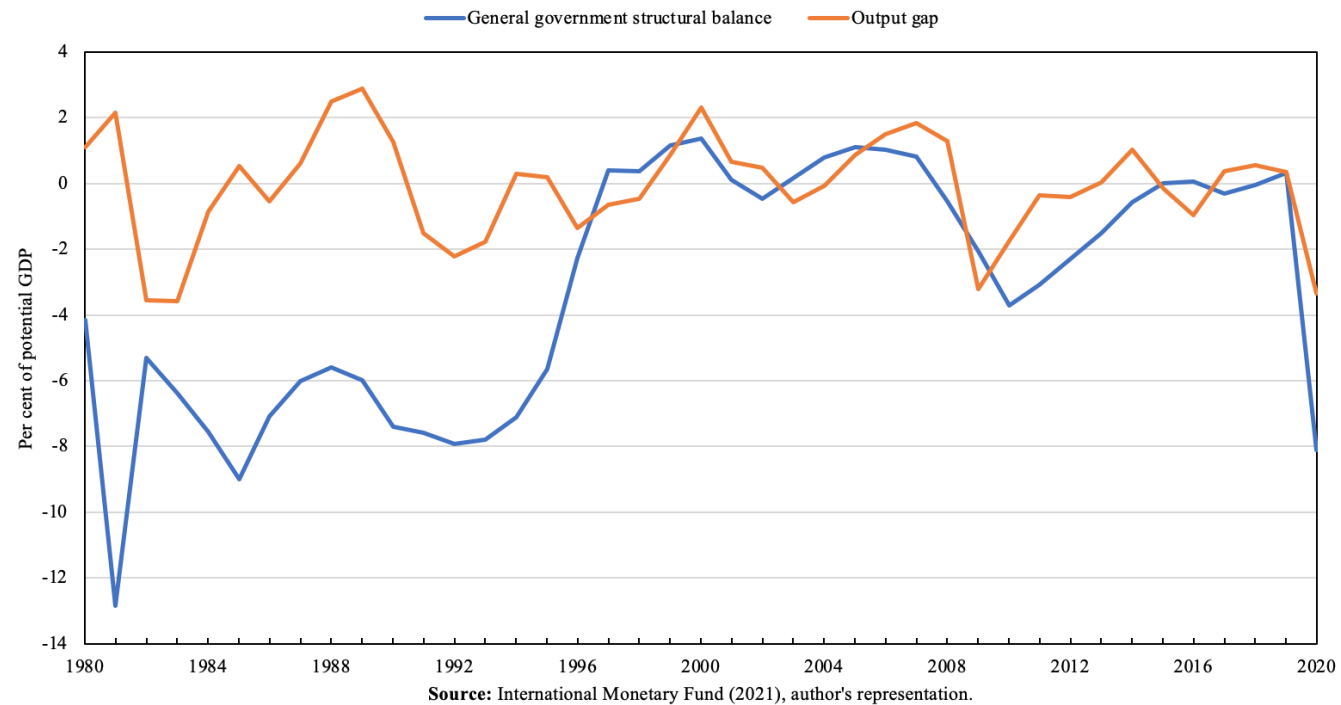
- + : counter-cyclical in many years, high public investment to GDP ratio
- / + : pro-cyclical in many years, high public investment to GDP ratio

*Open economy conditions:*

- + : real depreciation
- : real appreciation

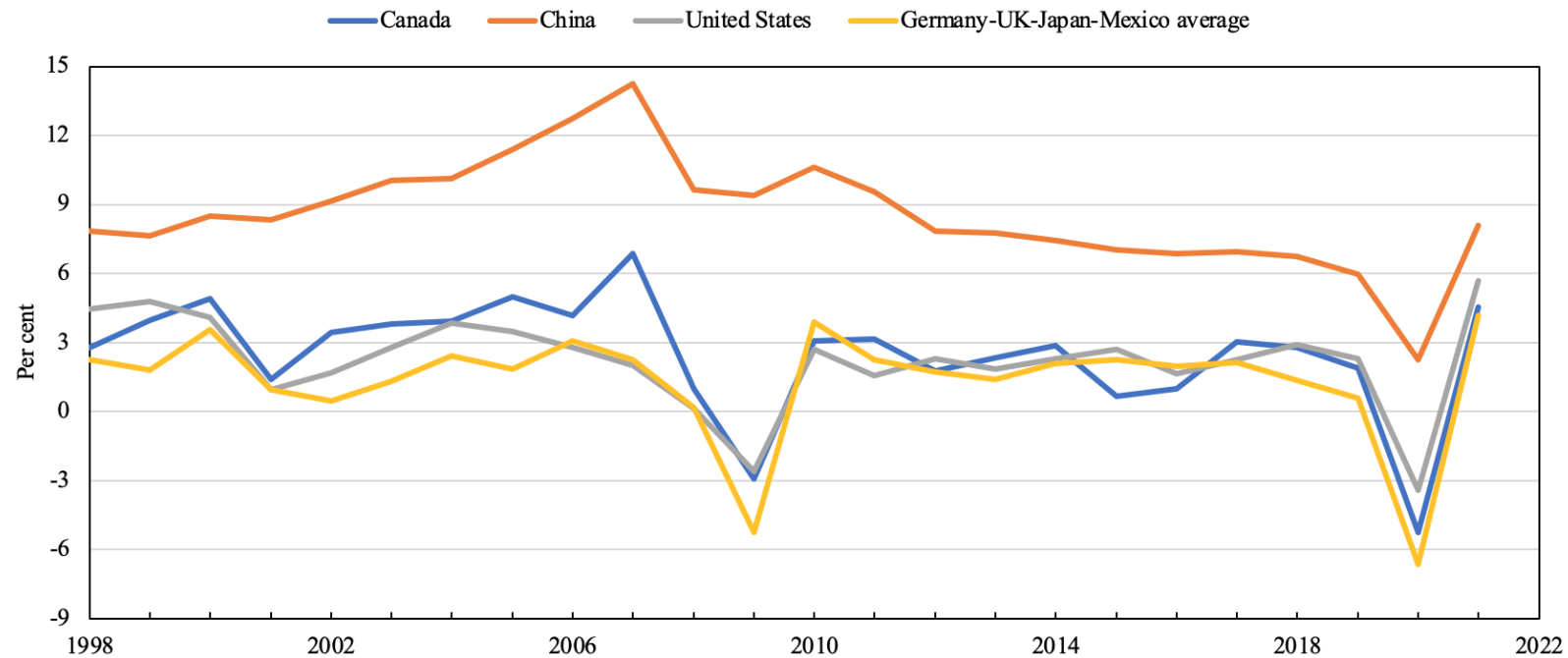
# Fiscal policy stance

**Figure 4: General government structural balance and the output gap**



# Comparative growth rates

**Figure 5: GDP growth vis-à-vis major trading partners**



Source: World Bank (2022), author's calculations and representation.

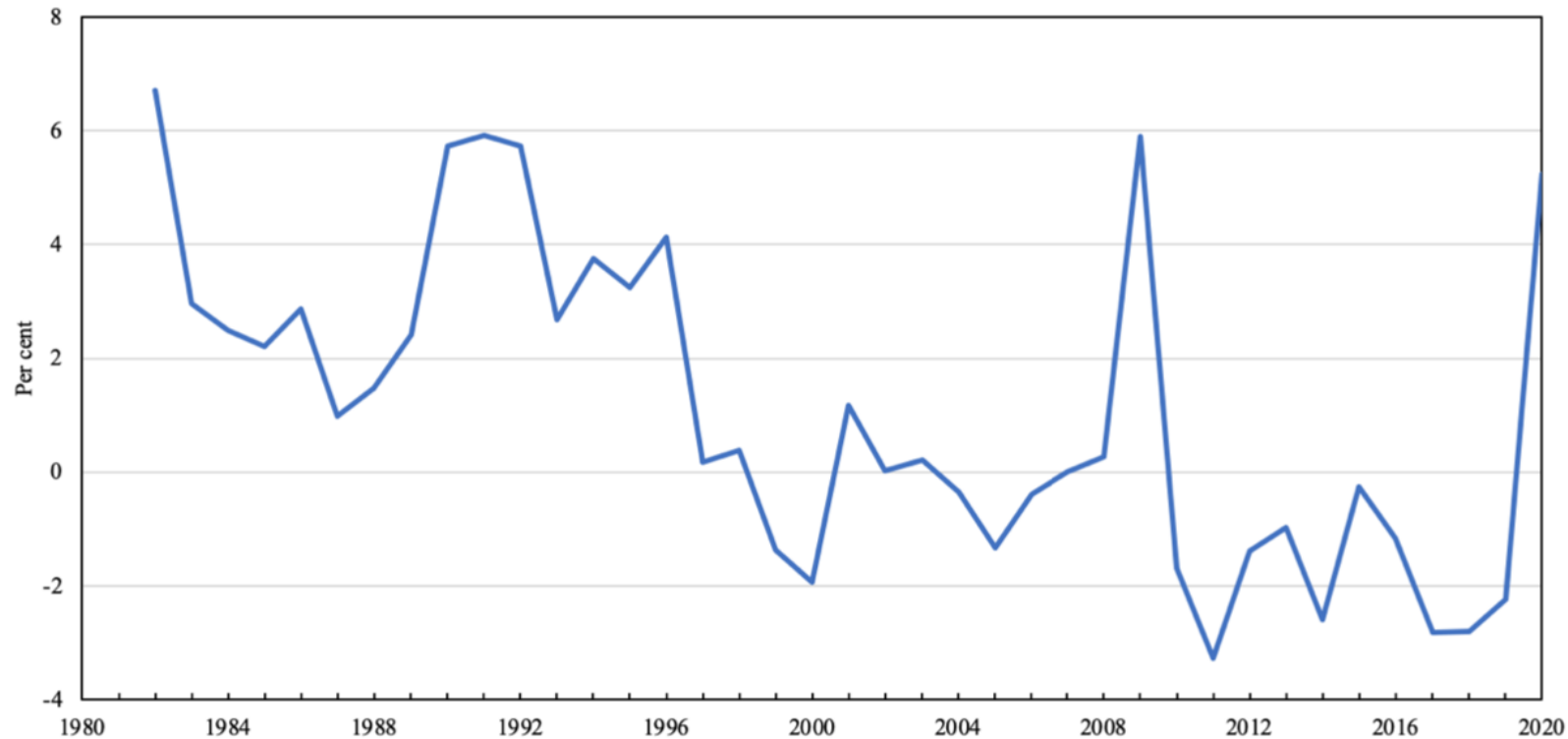


# Summary and conclusions

- This research deployed the tools of post-Keynesian macro to provide a new contribution to Canadian political economy.
- The findings demonstrate a series of growth regime shifts: a DDL regime from 1983-1991; a 'rising' WEL regime from 1992-2000; a 'falling' WEL regime from 2001-2009; and a DLDP regime from 2010-2020.
- The macroeconomic policy regime analysis shows that open economy conditions played a key role in these shifts of growth regimes via successive cycles of currency appreciation (decreasing price competitiveness) and currency depreciation (increasing price competitiveness). At the same time, the structural transformation of the Canadian economy via the secular decline of the economic complexity index makes Canadian exports increasingly dependent on commodity price booms.
- Fiscal policy has seen a return of public sector deficits but has failed to support the deleveraging of households.
- Reliance on expansionary monetary policy has directly encouraged the accumulation of private debt.

# Appendix 1: Monetary policy stance

Figure 8: Real long-term interest rate minus real GDP growth

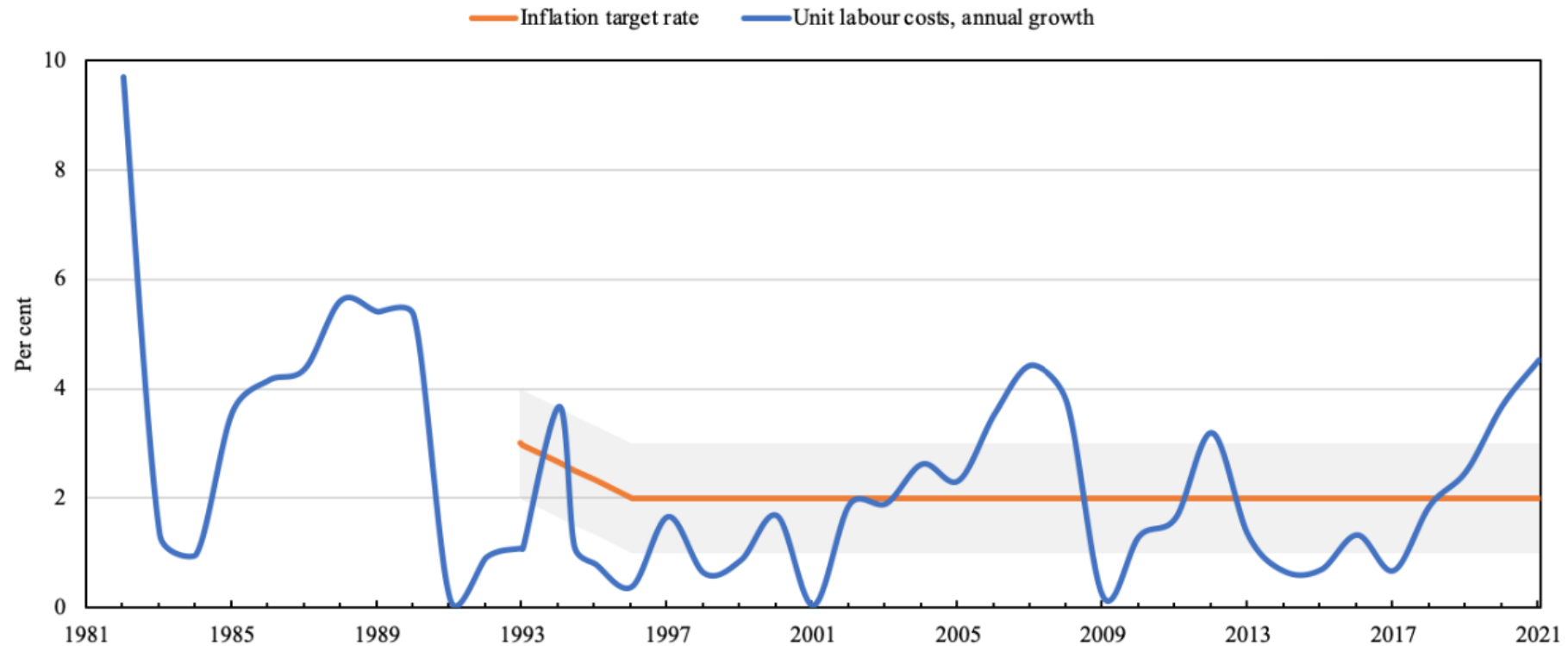


**Source:** Organization for Economic Cooperation and Development (2022a) and Statistics Canada (2021a; 2022b), author's calculations and representation.

**Note:** The real long-term interest rate is calculated by subtracting the rate of CPI growth from the nominal long-term interest rate.

# Appendix 2: Incomes policy stance

**Figure 9: Nominal unit labour costs and the Bank of Canada inflation target**



**Source:** Statistics Canada (2022i) and Bank of Canada (1991), author's presentation.

**Note:** The inflation target range is plus or minus one per cent of the target rate.