

Productivity Mega Deduction = Mega Growth?

TD Economics / TD Securities · 2026-09-16 · English original

Francis Fong, Managing Director & Senior Economist

- Prime Minister Carney announced an expanded immediate expensing framework aimed at kickstarting major projects and capital spending in Canada at the Investment Summit. The policy expands on the existing Productivity Super Deduction announced in Budget 2025. It allows firms to deduct 100% of the depreciation of capital assets in the first year of operation on a broader set of equipment classes. This lowers the tax burden in the current year by reducing taxable income.
- The previous Super deduction covered a narrower set of equipment classes amounting to 15% of capital assets, according to the Department of Finance. The Mega deduction expands the policy to more equipment classes, covering approximately 65% of assets and hews closely to Carney's Major Projects initiatives. These new classes include fibre-optic cable, mining property, oil and gas pipelines, software, research and development, computer equipment, aircraft and vehicles, patents, rail track, bridges, and roads – all priority areas when it comes to AI, defense, critical minerals, and energy.
- The deduction is also now permanent, which is significant. In effect, firms will now see a permanent reduction in the hurdle rate for capital initiatives large and small, with the focus clearly on ensuring the incentive is there for domestic and foreign capital to locate in Canada and get projects off the ground.
- The initiative is projected to cost \$36 billion over five years. This builds on the previous \$1.5 billion price tag for the Super Deduction over 5 years, and a smattering of accelerated capital cost allowance policies in the last several years.

Key Implications

- There are several questions worth exploring: 1) How does this and any other of Carney's announcements work in tandem? 2) How does it compare with the U.S.? 3) Will it work at getting shovels in the ground on major projects? 4) What will the impact be on the economy and deficit?
- Deducting depreciation is just one variable in the investment calculus. It sits alongside federal and provincial statutory tax rates, other deductions, tax credits, sales and property taxes, capital and labour inputs, financing mechanisms, and other measures. In a way, immediate expensing is meaningful, but not game changing in isolation.
- But it carries more influence when layered with the many other policies that are 'derisking' capital spends within the private sector. These include: \$8.2 billion in direct investments committed by the federal government to capital projects, along with hundreds of billions more announced but not yet committed. The government is also speeding up environmental and impact assessments, and recently announced advancing tax rulings for major projects to create tax certainty.
- Canada is competing for capital internationally, so it behooves the government to also consider how its tax framework compares to the United States. According to Finance, the immediate expensing framework puts Canada's marginal effective tax rate (METR) on new investment at 6.4% — a massive 10.5 percentage points below the U.S.

- However, the analysis is more complex than implied by this figure alone. Both countries are pulling on similar, but differing levers. First, when it comes to the highly observable statutory corporate tax rate, the playing field is fairly leveled between countries. The U.S. applied two rounds of changes to close the gap in the combined federal-state statutory corporate tax rates vs the combined Canadian federal-provincial rates via the Tax Cuts and Jobs Act, and the One Big Beautiful Bill Act. Moreover, the U.S. 100% immediate expensing framework (which Canada is mirroring) is still considered more generous given slightly looser eligibility requirements.
- Still, a lower METR for Canada matters. Immediate expensing in the U.S. only applies to a firm's federal tax liability unless the state matches the policy, of which only about half have done so. Moreover, Finance has largely referred to harmonized sales taxes in Canada as the primary reason for the favourable gap alongside the previous accelerated capital cost allowance regime on structures. These initially were the reasons for the two countries to have similar METRs before these policy announcements this week, which now adds the expanded immediate expensing in Canada.
- All said, there is a lot for investors and companies to digest rather than a straight-up statement of the figures. The biggest draw for investors is likely that the entire basket of Canadian policies is clearly trending in the right direction, removing some barriers from projects that often require significant risk, time and capex.
- The magnitude of the near-term economic benefits of the package is uncertain. The backgrounder accompanying the release purports that the initiative could generate additional economic activity of between 1.4 and 3 times the annual federal cost, corresponding to an average "economic output" of \$22 billion.
- The potential lift to real GDP growth could be anywhere between 0.3% and 0.8% during the uptake period.
- That's quite the range and will depend on (1) the overall uptake on the policy, and (2) the composition of the industries that will use the tax deduction.
- From our lens, we would pencil in the impact in the lower-to-mid range of the estimate with the expectation that the benefits would likely start to flow in mid-to-late 2027.
- The expansion of the deduction is expected to add another \$7.2 billion to the \$63 billion-dollar deficit for fiscal 27/28. The government has emphasized that new spending will be focused on investment and, according to the PM's speech, the operating budget is expected to be balanced next year. Given the ongoing surge in bond yields, the cost of deficit spending has steadily increased. Financial markets expect greater discipline from governments in ensuring that every new dollar spent carries a higher rate of return than in the past. We now eagerly await the full breakdown of all the government's plans in this fall's budget.

Source: <https://economics.td.com/ca-productivity-mega-deduction>