Canada's economy rebounded strongly in Q2 as domestic demand strengthened

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The Bottom Line:

Canada’s economy rebounded in the second quarter, with real GDP increasing 3.3% annualized, following a small upward revision to Q1 growth from a small 0.1% decline to a small (but positive) 0.3% increase.

The quarterly and monthly GDP data are volatile and the pace of growth in Q2 is unlikely to be repeated to the same extent in the quarters ahead — the early estimate of July output was “essentially unchanged” from June levels.

But the data is consistent with an economic backdrop that has been gradually improving, particularly when measured on a per-person basis with Canada’s population edging lower.

Some of the improvements reflected a reversal of temporary weakness earlier in the year. Net trade contributed substantially to growth as exports outpaced imports, led in part by a recovery in auto production and shipments following winter disruptions.

Still, the Q2 rebound extended beyond trade. Household spending strengthened despite higher fuel costs, business investment increased alongside stronger equipment imports, and residential investment recovered as home resales and housing starts improved. Final domestic demand overall (spending by Canadian businesses, consumers, and governments) rose 3.9% annualized after edging lower (-0.1%) in Q2.

Growth is expected to moderate from Q2’s strong pace but remain positive over the remainder of 2026. The latest 50% U.S. tariffs add downside risk, although we expect the effects will be concentrated heavily in specific exposed sectors/products with limited aggregate economic growth implications.

More than 80% of Canadian exports continue to enter the U.S. duty-free under CUSMA, helping preserve the broader growth backdrop. But producers of plastics, electrical machinery, furniture and wood products face potentially severe disruptions, with the regional effects concentrated in Quebec, British Columbia and Ontario. Canada’s counter-tariffs and support measures will help shape how widely those effects spread.

Overall, the Q2 report confirms that the economy entered this latest period of trade disruption from a stronger starting point.

Our base case remains for a gradual cyclical recovery, but national growth figures will mask much more difficult adjustments for affected industries, communities and workers. We continue to expect the Bank of Canada to keep interest rates unchanged through the remainder of 2026.

The details:

Real GDP increased 3.3% annualized in Q2, following the upwardly revised 0.3% gain in Q1 (previously reported as -0.1%). That marked a meaningful rebound after a weak winter, and revised data showed the Canadian economy did not shrink for two consecutive quarters. With population growth continuing to decline, per-capita GDP growth increased again in the second quarter.

Final domestic demand increased 3.9% annualized, reflecting gains in household consumption, machinery & equipment, and residential investment.

Household consumption rose 3.3% annualized, with spending on goods increasing 2.6% and services spending rising 3.9%. Gains were led by the services category.

Elevated energy costs continued to weigh on household purchasing power but the household saving rate (the shared of household disposable incomes not spent on current consumption) edged up to 3.7% from 3.3% in Q1. Disposable incomes were boosted in part by a one-time GST/HST credit payment as part of the new Canada Groceries and Essentials Benefit.

Business fixed investment jumped 9.5%, supported by a 22% jump in spending on machinery & equipment that built on the 11.5% growth in Q1, as well as a rebound in residential investment following declines in the prior two quarters.

Export growth increased 15.1%, led by a recovery in motor vehicles following winter production disruptions, while imports rose only 1%. Net trade added 4.4 ppts to annualized GDP growth but the auto-related boost is unlikely to be repeated to the same extent in subsequent quarters.

The main offset to gains elsewhere came from a 4.9 percentage point subtraction from GDP from a rundown in business inventories, along with a pullback in government capital spending.

Industry-based GDP rose 0.3% in June, led by services-producing industries (+0.4%), while weakness in goods-producing industries (-0.1%) partially offset the increase – the monthly GDP data (calculated separately from the quarterly expenditure addup) posted a 3.6% annualized increase in Q2 following a 0.6% Q1 increase.

Statistics Canada’s advance estimate indicated GDP was unchanged in July, suggesting economic activity likely moderated at the beginning of Q3. Gains in real estate, rental and leasing, and professional, scientific and technical services were offset by declines in retail trade and manufacturing.

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Source: https://www.rbc.com/en/economics/canadian-analysis/data-flashes/canadas-economy-rebounded-strongly-in-q2-as-domestic-demand-strengthened/