



The Economic and Fiscal Challenges of Population Ageing

Finance Canada

Prepared for the Conference on New Approaches to Social Policy

Policy Research Initiative

Ottawa, December 13, 2004

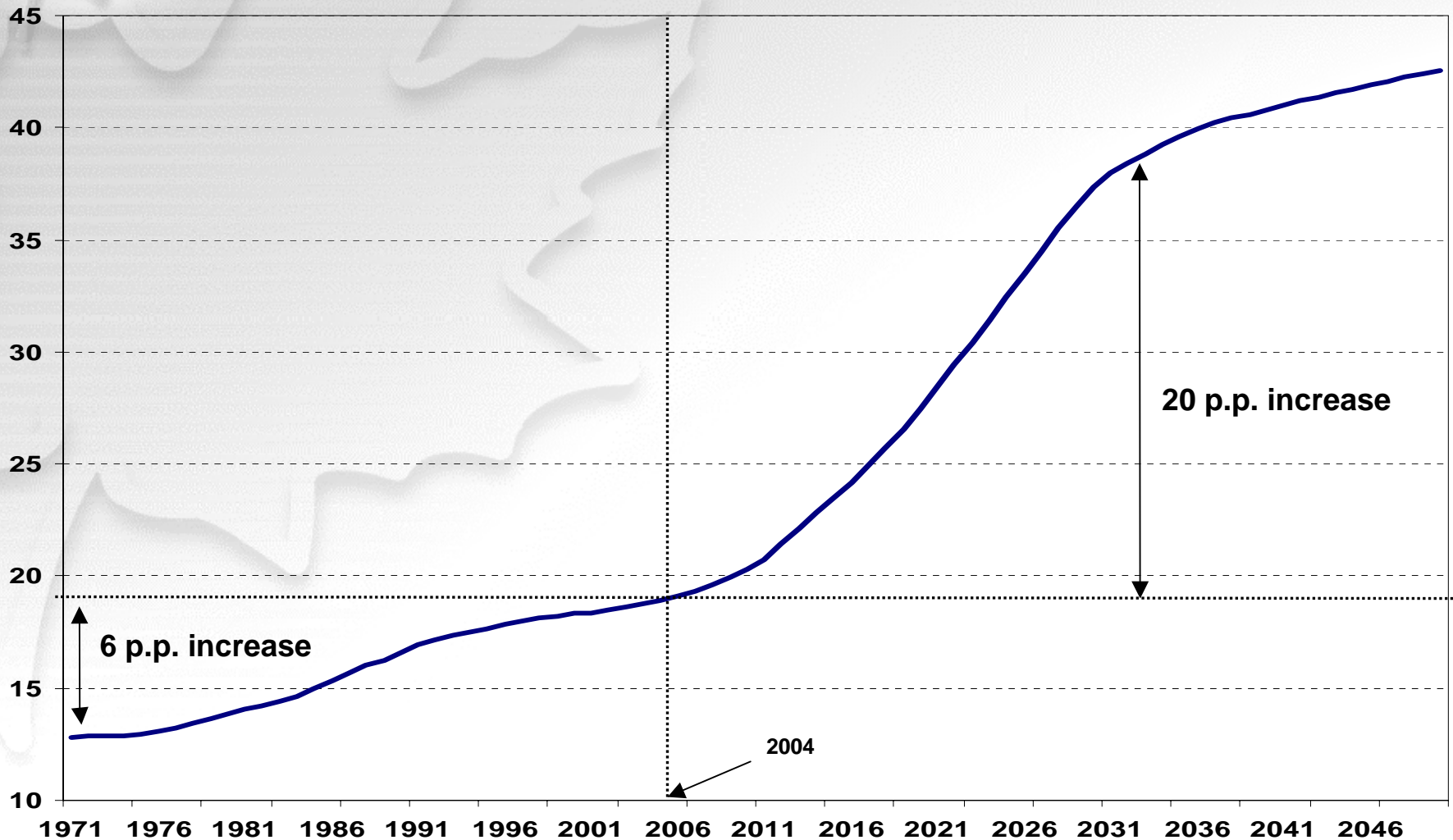
Outline

- Demographics of Ageing
- Economic Implications
- Fiscal Implications
- Public Policy Implications

Demographics of Ageing

Old-age dependency ratio expected to more than double

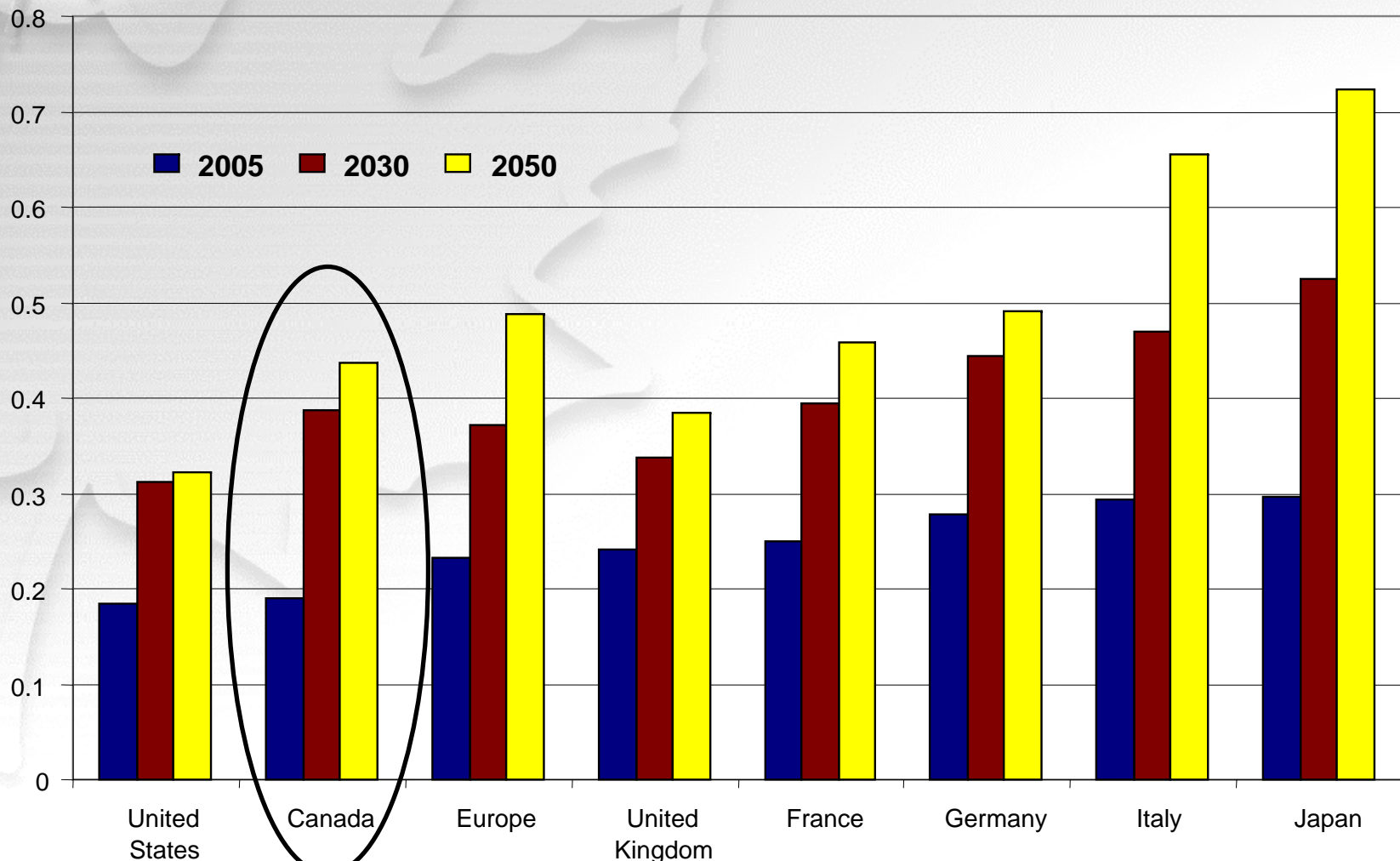
Old-age Dependency Ratio: Ratio of Persons Aged 65+ to Persons Aged 15-64



Demographics of Ageing

Population ageing will be a challenge for all G-7 countries...

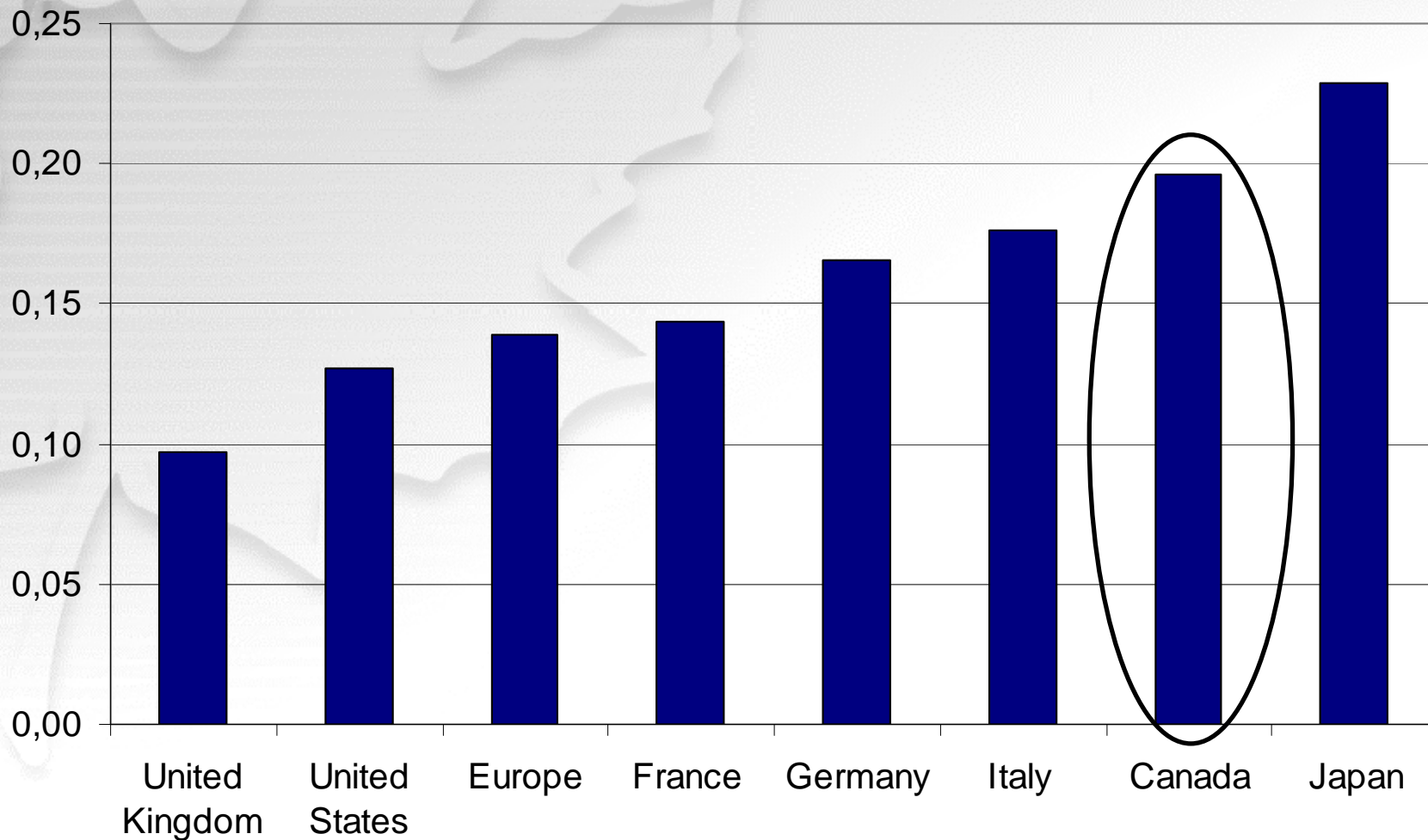
Old-age Dependency Ratios (65+ to 15-64), 2005, 2030 and 2050



Demographics of Ageing

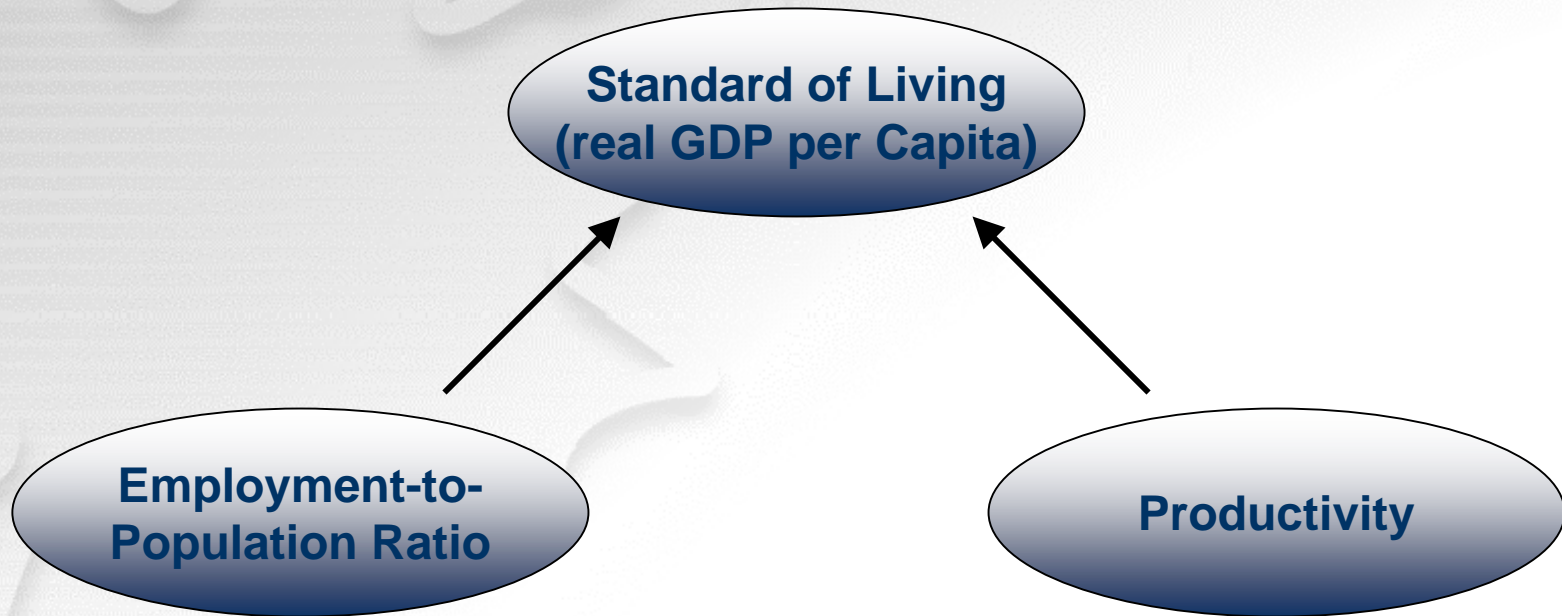
... but more so in Canada over the next 25 years

Changes in Old-age Dependency Ratios (65+ to 15-64), 2005 to 2030



Economic Implications

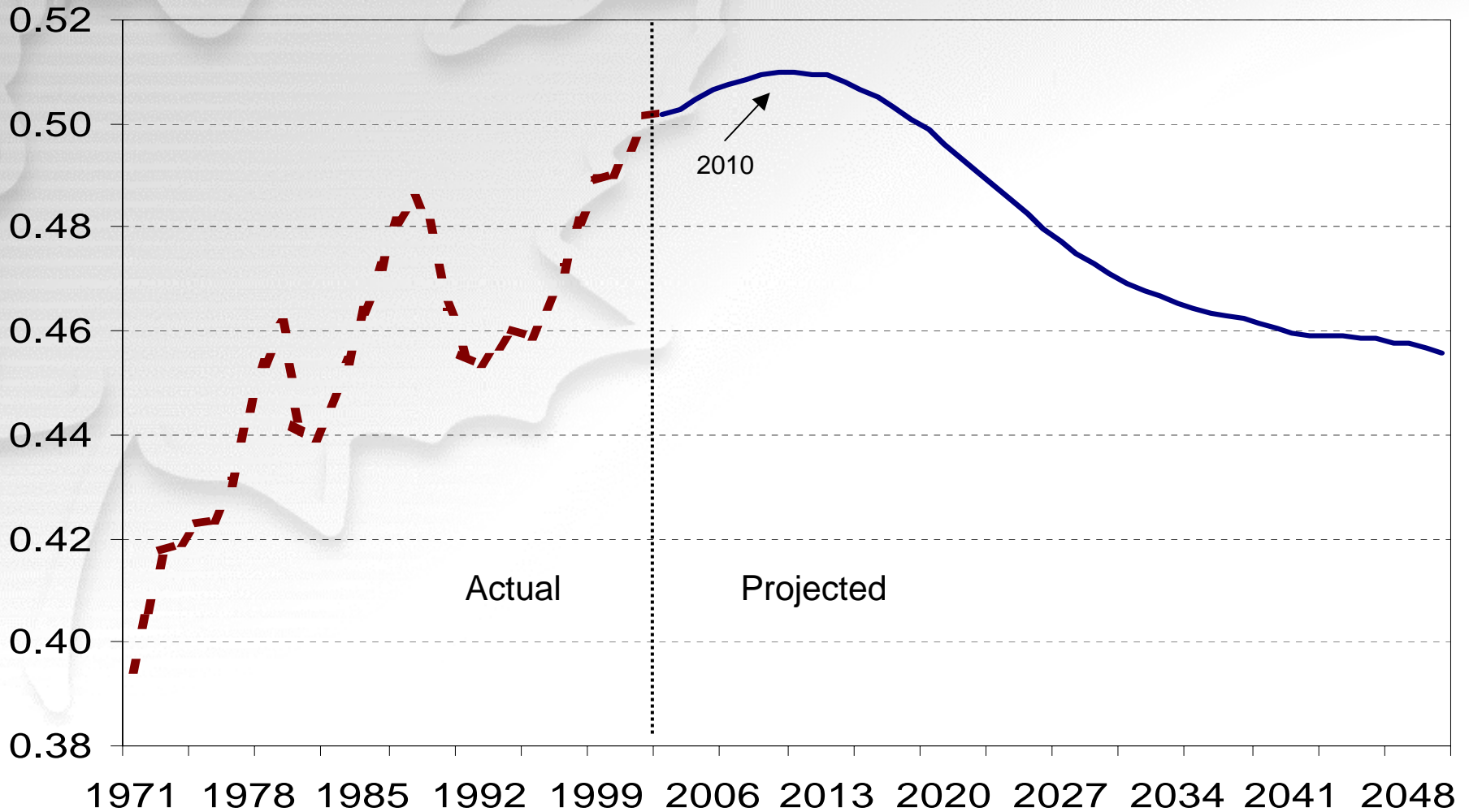
Sources of growth in living standards



Economic Implications

The employed share of the population to start declining around 2010...

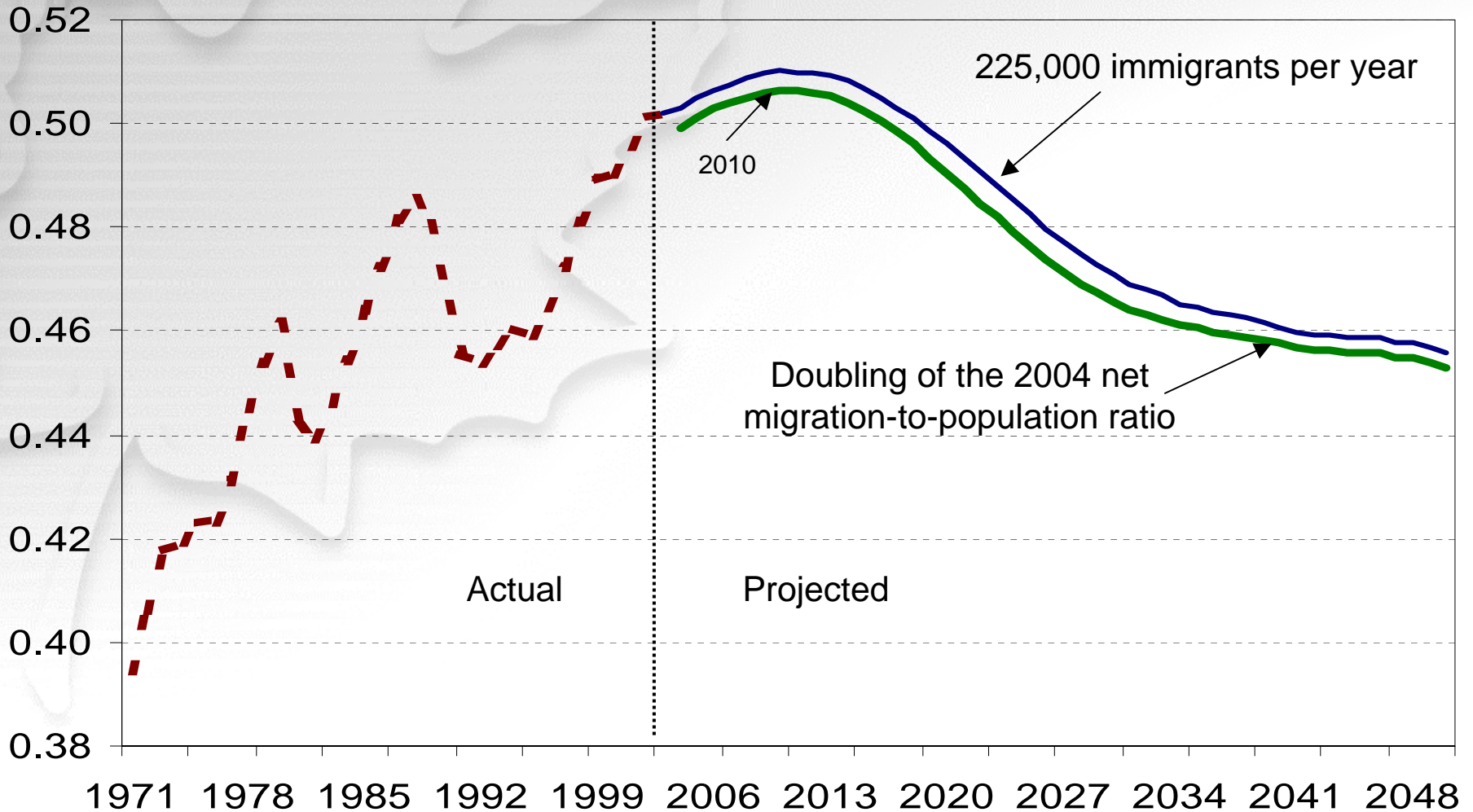
Employment-to-total Population Ratio, Canada



Economic Implications

... regardless of immigration level

Employment-to-total Population Ratio, Canada



Economic Implications

Impact of ageing on productivity...

Direct effect of ageing

- Are older workers less productive than prime age workers?

Indirect impact of ageing

- Is the composition of demand in an older society skewed toward service industries that are less innovative?

Capital deepening

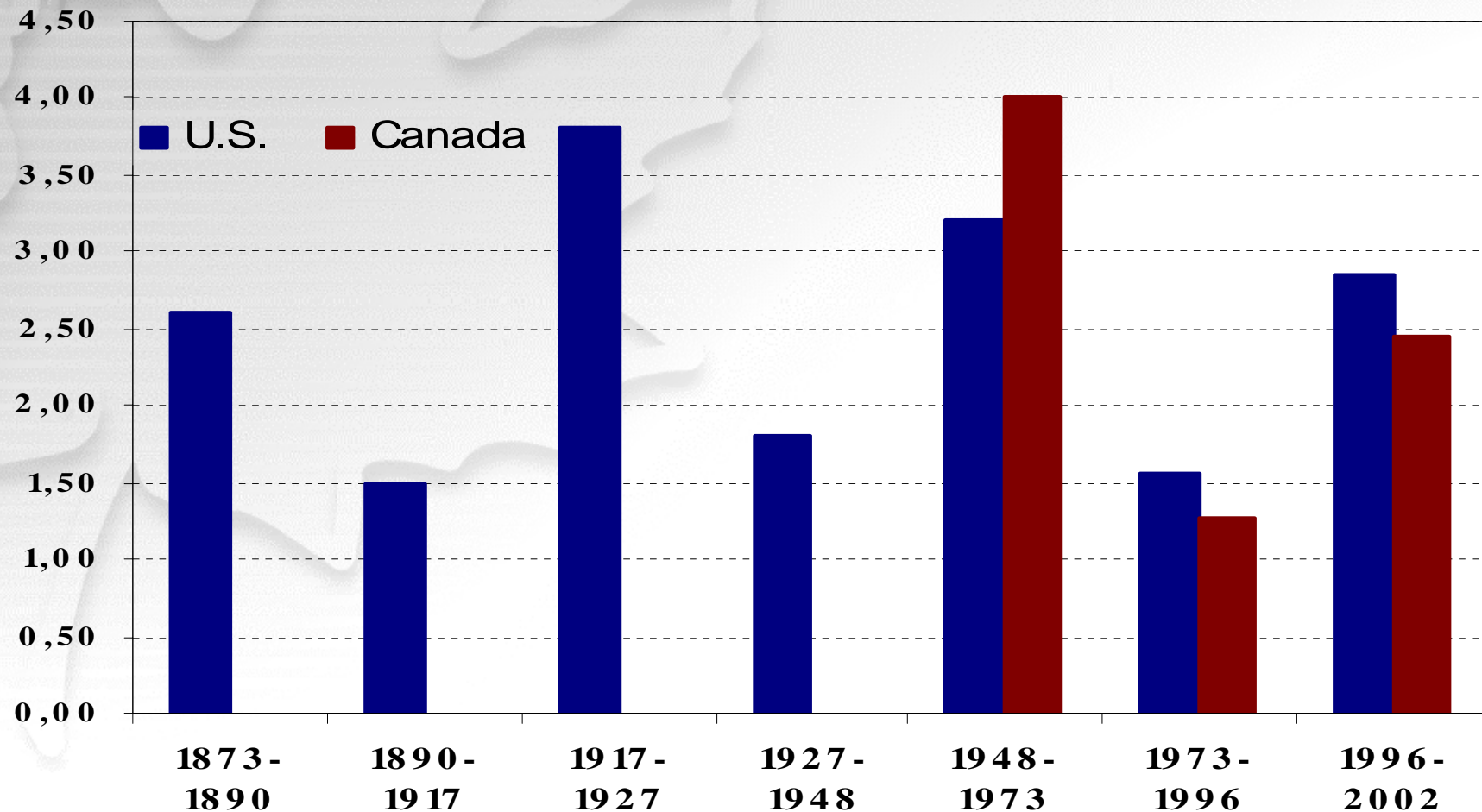
- Likely lower real interest rates and higher real wages would translate into both physical and human capital deepening, thus boosting labour productivity growth.
- But this will depend to some extent on the path of public savings and on the future tax level and mix.

... is uncertain

Economic Implications

How long will the recent productivity growth upsurge last?

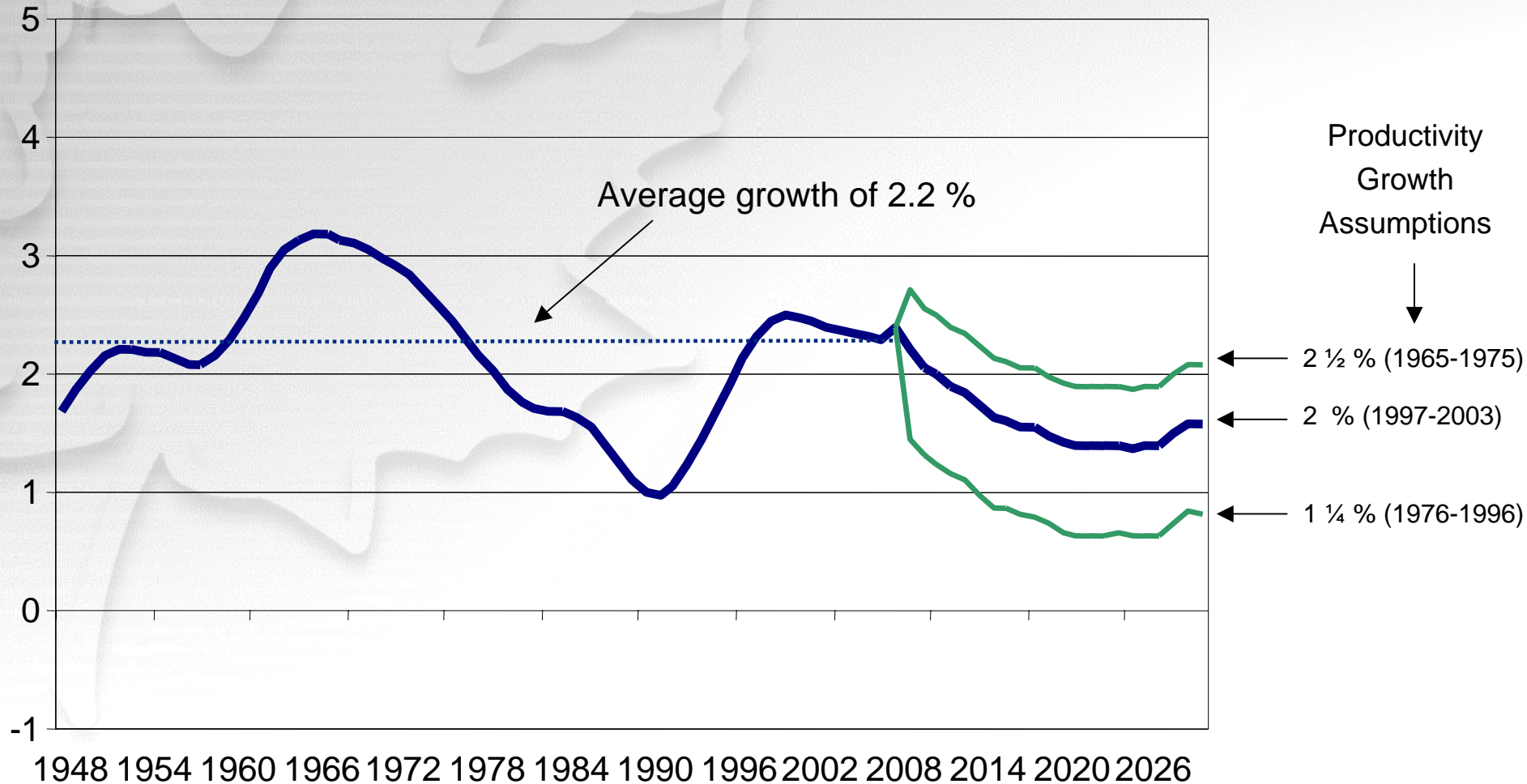
U.S. and Canadian Labour Productivity Growth (Business Sector), 1873-2002



Economic Implications

Growth in living standards will depend increasingly on productivity growth

Trend Real GDP Per Capita Growth



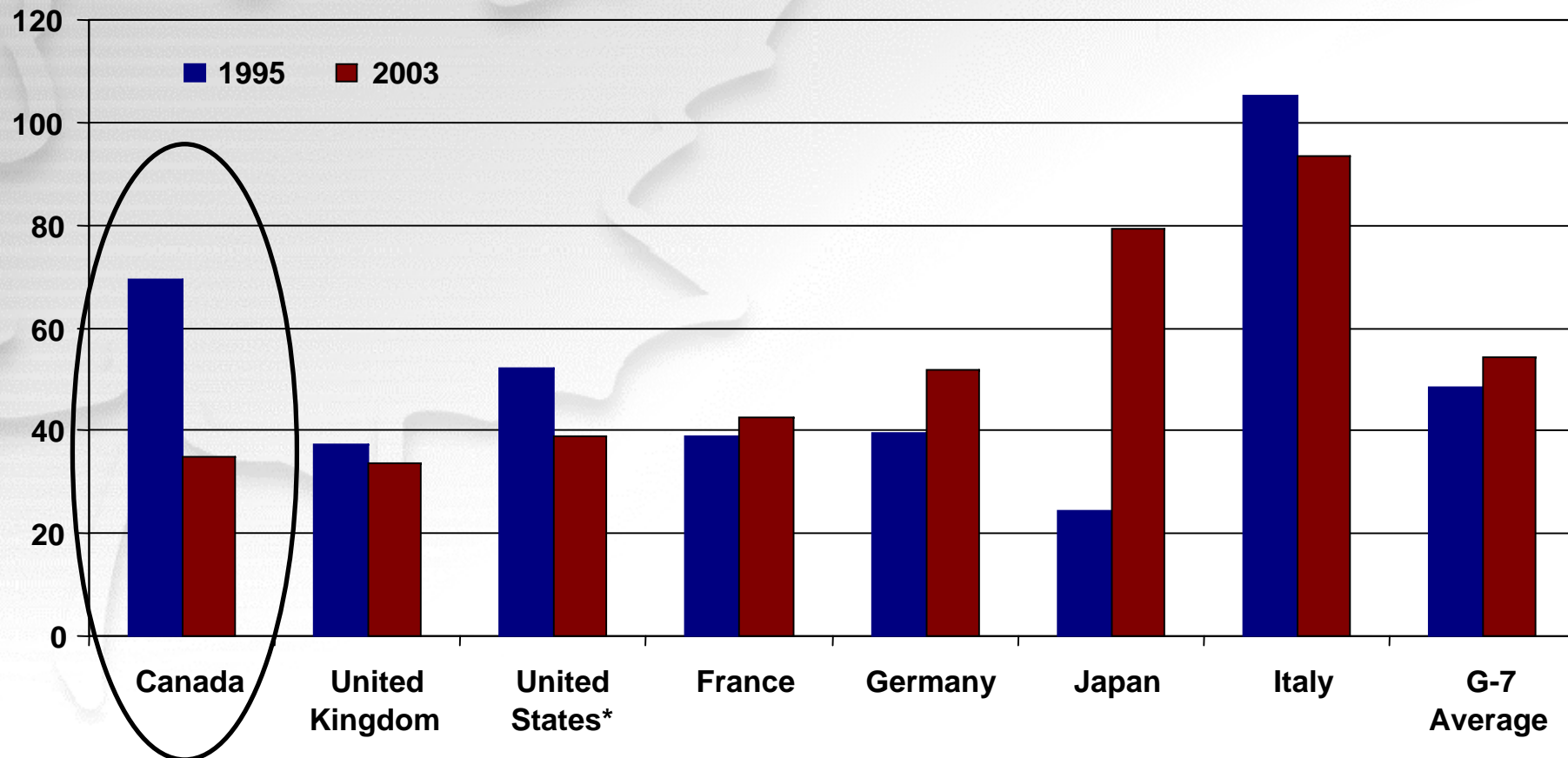
Note: Trend real GDP per capita growth is calculated using a Hodrick-Prescott Filter

Fiscal Implications

Canada's fiscal progress has been impressive

Total Government Net Financial Liabilities in G-7 Countries

per cent of GDP, national accounts basis



* Adjusted to exclude certain government employee pension liabilities in order to be more comparable with other countries' debt measures.

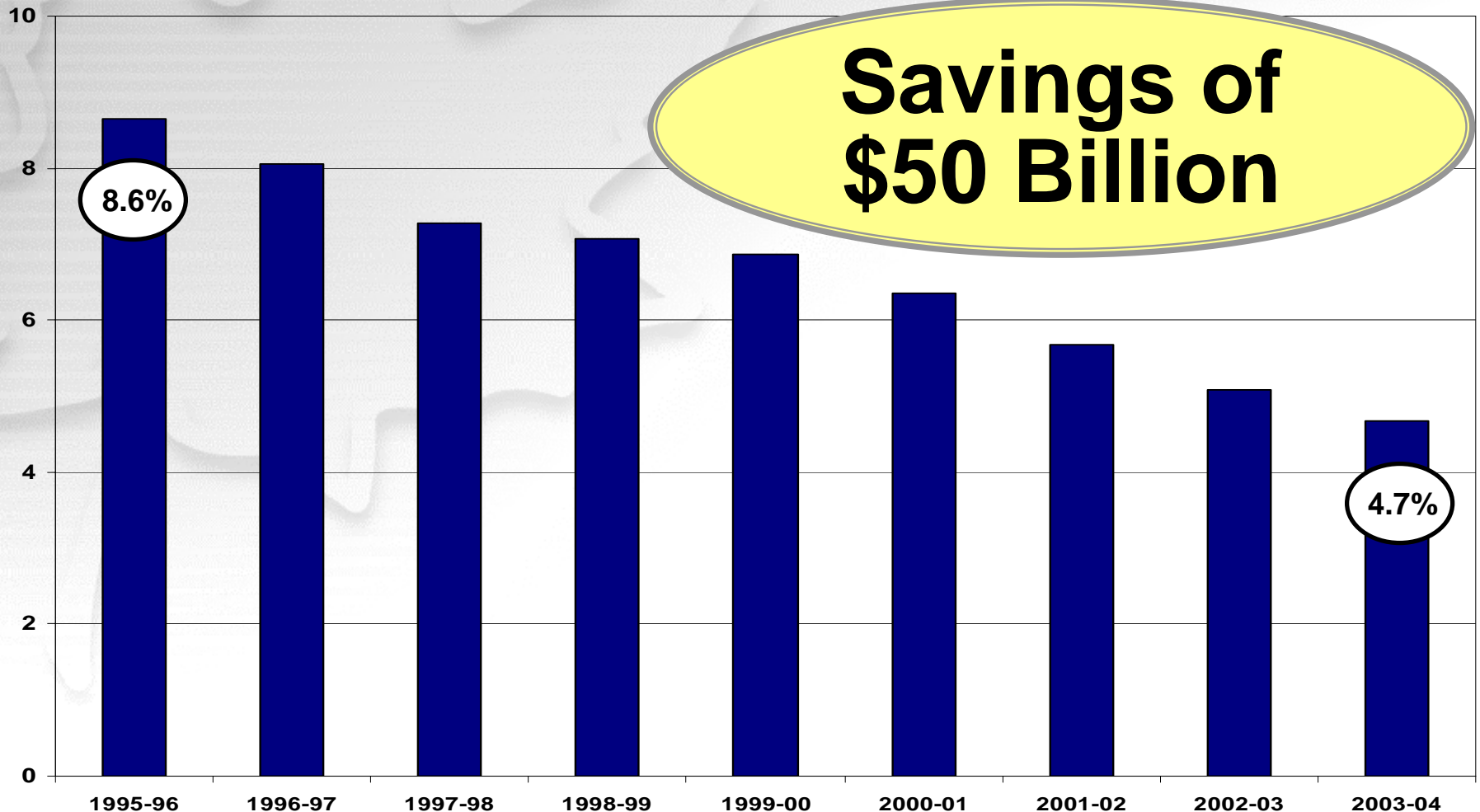
Sources: *OECD Economic Outlook No.75* (June 2004); Department of Finance calculations.

Fiscal Implications

Reducing the debt frees up resources for new priorities and helps prepare for ageing

Total Government Debt Charges

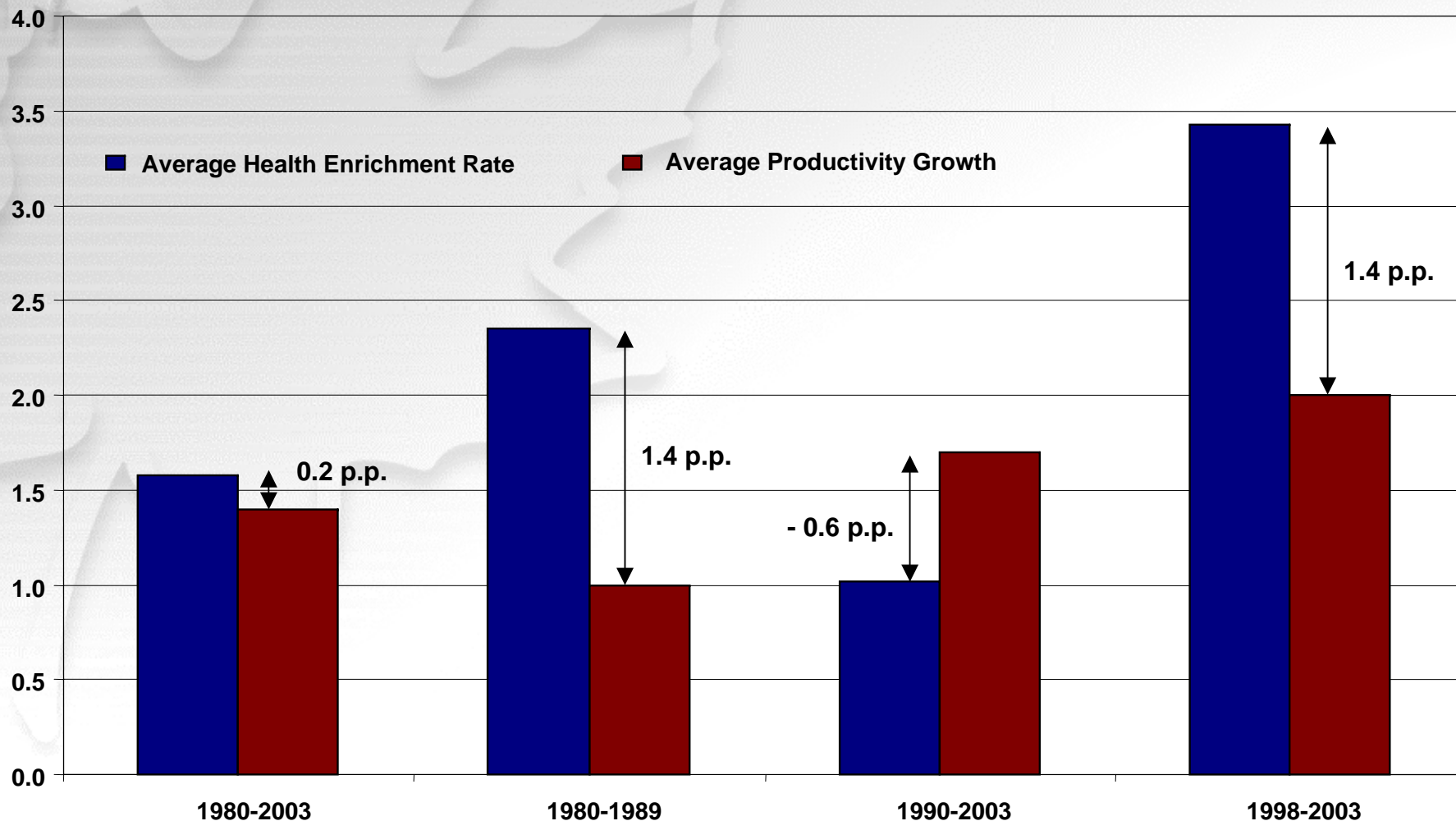
per cent of GDP, public accounts basis



Fiscal Implications

Main fiscal challenge will be aligning health enrichment to productivity growth

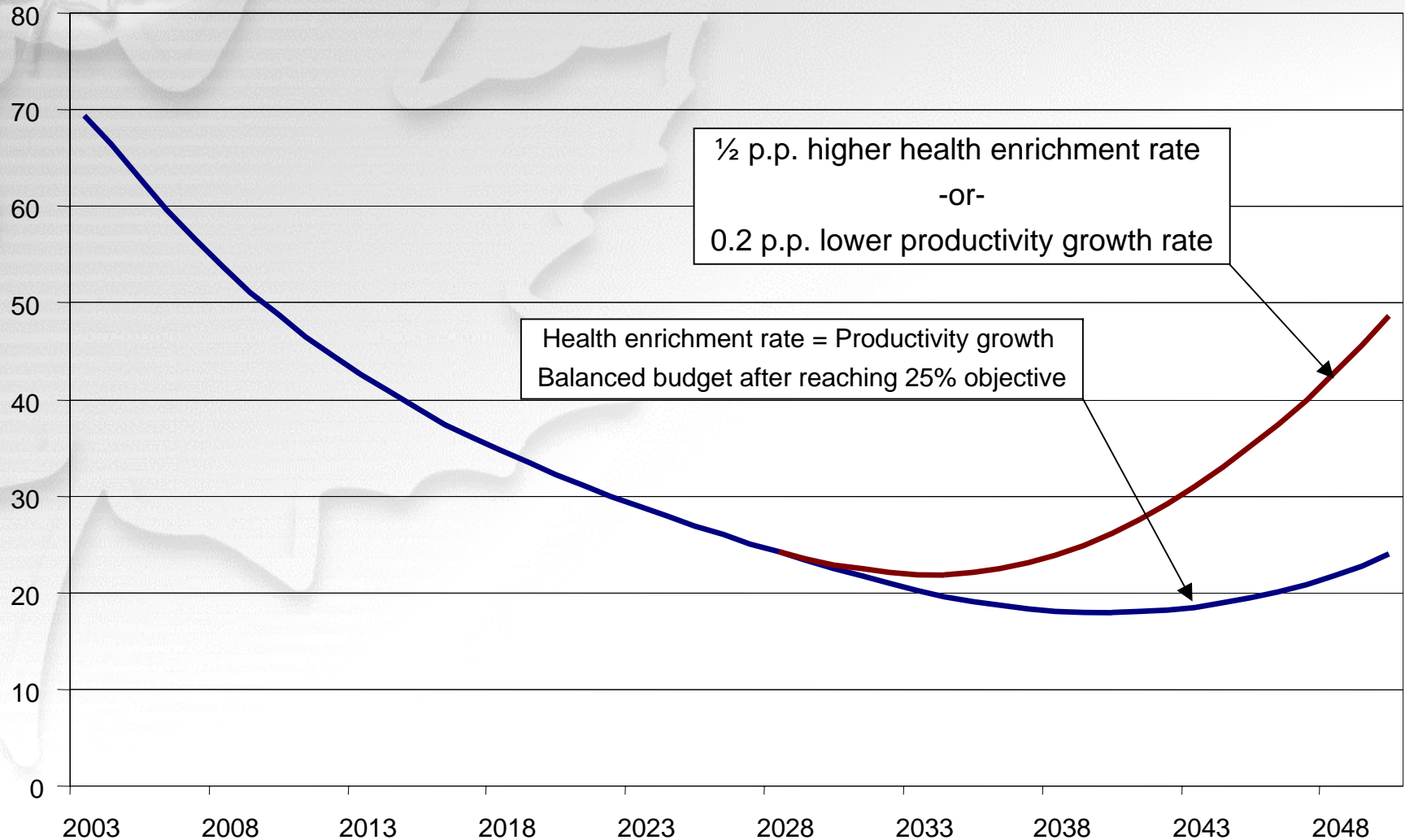
Average Health Enrichment and Productivity Growth Rates, 1980-2003



Fiscal Implications

The long-term fiscal outlook will be heavily influenced by the evolution of health care spending and productivity growth

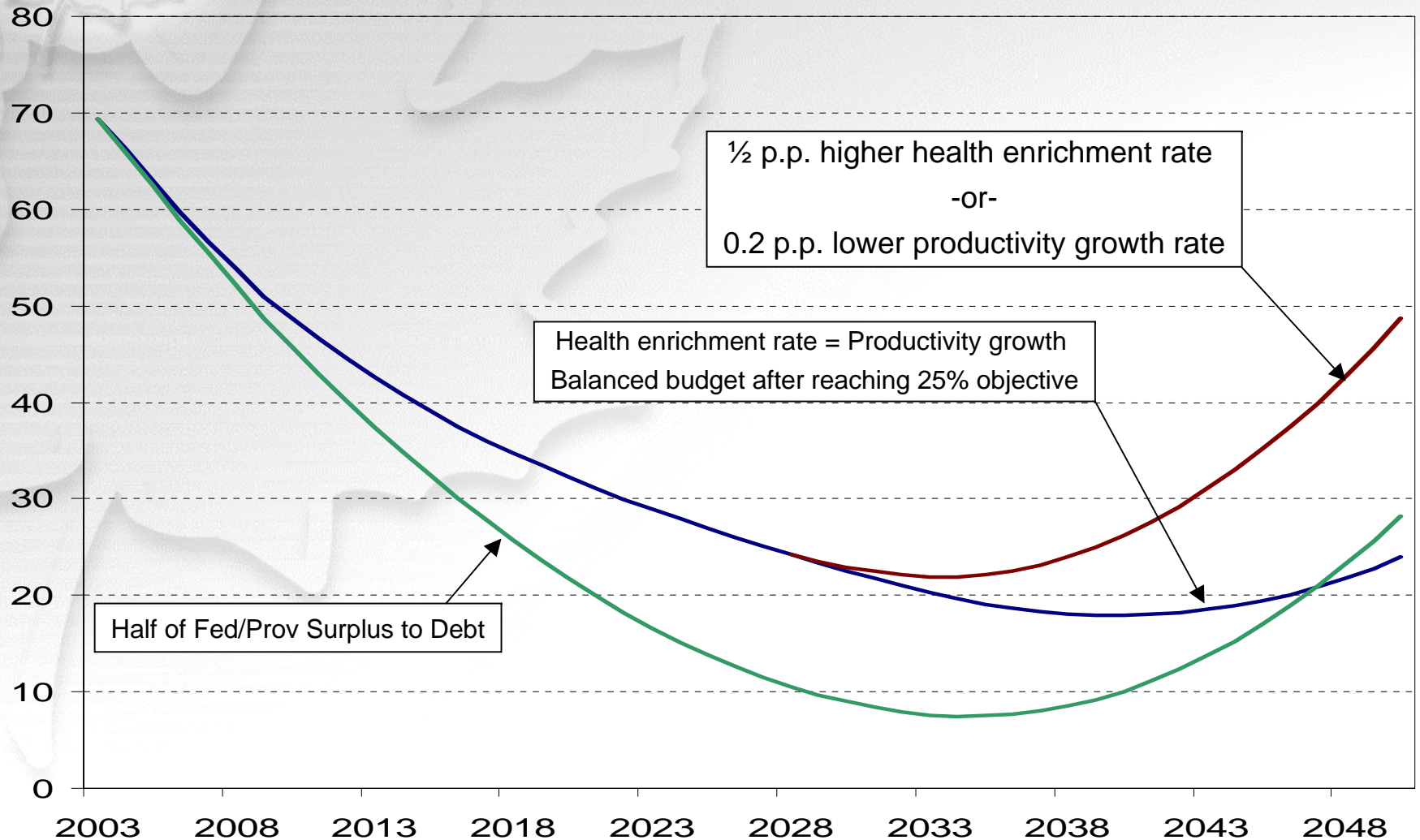
Combined Federal & Provincial Debt-to-GDP Ratios



Fiscal Implications

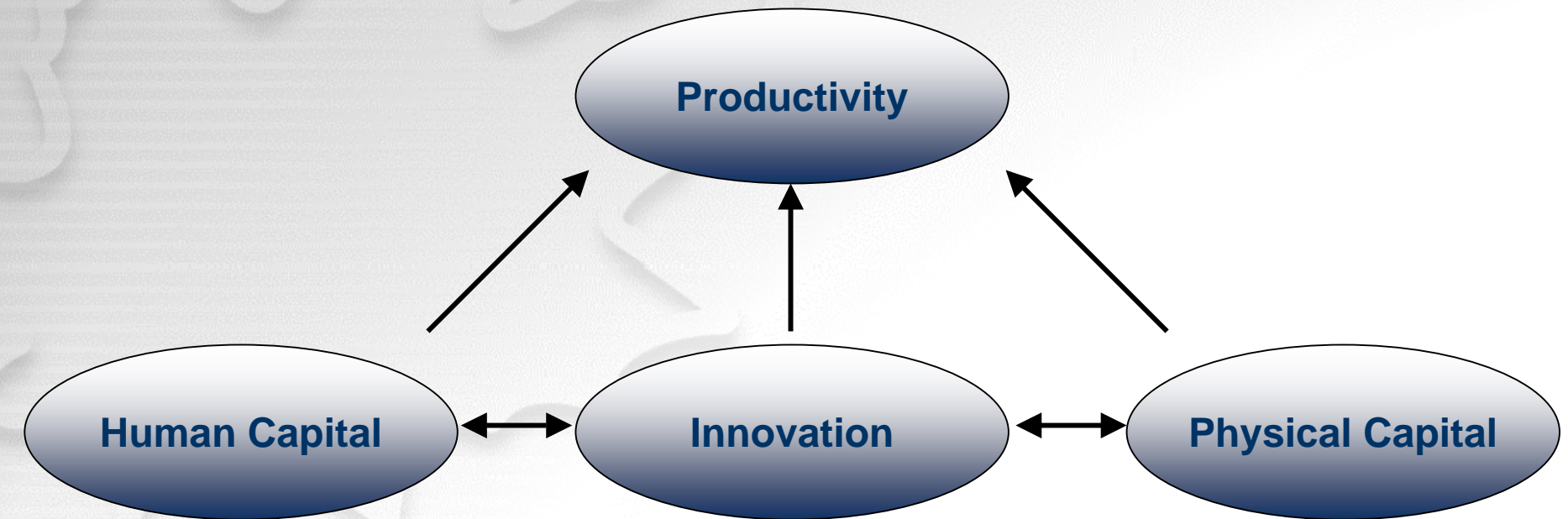
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Combined Federal & Provincial Debt-to-GDP Ratios



Public Policy Implications

With an ageing population, productivity growth is the key; thus we must focus on its drivers



Public Policy Implications

Policy instruments to improve productivity

Macroeconomic Policies

- Low inflation
- Prudent fiscal planning and balanced budgets
- Declining Debt-to-GDP ratio

Microeconomic Policies

- Support for learning
- Encourage research and development
- A competitive tax structure
- Efficient financial markets
- Trade liberalization and attracting foreign investment
- Efficient design of social policies
- Public infrastructure

Public Policy Implications

Key Messages

- Canada will experience rapid ageing over the next 50 years.
- Therefore, future improvement in living standards will depend on productivity growth.
- Recent strategy has been to reduce the debt and provide a productivity-enhancing environment.
- To meet the challenge of ageing, this approach needs to be preserved.
- And health care costs need to be contained.



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