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CANADA HAS A RETIREMENT CRISIS. **VS.** CANADA DOES NOT HAVE A RETIREMENT CRISIS.

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“Be it resolved that there is a retirement crisis in Canada.”

RETIREMENT SAVING IN CANADA: A SLOW AND STEADY CRISIS ON THE HORIZON

PSD IN CONVERSATION WITH DAVID FOOT

Is there a retirement crisis in Canada?
You need to look at it from two sides. The human resources side, [that is,] in terms of the number of bodies in the workforce. But we have another crisis unfolding as a result of these ridiculously low interest rates, meaning that pension investments are not nearly sufficient [for people to] live on in retirement. There is some interaction between those two parts of the retirement crisis.

Some argue our real retirement income targets are lower than most of us think - not 70%, but 50% income replacement.
I would agree with that perception, but even getting enough returns on your investment for 50% income replacement could be a challenge in this ridiculous low-interest rate environment.

Do Canadians have a solid fourth pillar of retirement to lean on – savings, real estate, and other assets?
I’m not quite as optimistic, although I do agree that everyone talks about all the debts they have, but not their assets. You have to live somewhere, so although your home is a financial asset, it’s difficult to draw income from it if you’re living in it. It’s not impossible, but a reverse mortgage is very expensive. For some of the other sources of income, people are reluctant to use them. There’s a big inheritance motive – people want to be able to leave money to their children and their grandchildren. They would rather be in poverty themselves than use them. You’ve got to have public policies that enable people to use those assets in effective ways.

So is it a crisis? We know the first baby boomers born in 1947 reached the retirement age of 65 in 2012. So we know that on average, for the entire economy, the boomers will gradually start to trickle out of the workforce over the next 20 years. Over the second and third decades of the new millennium, the boomers gradually exit the workforce. Some of them may work a couple of extra years. I’m on record in favour of policies that encourage phased retirement, to let people step back, creating opportunities for twenty-somethings, while at the same time allowing them to continue working. For the public sector, retirement is a little earlier than 65 – the average age of retirement in the economy is 62, while for the public sector it is a little earlier. So that retirement trickle has already been underway for three or four years in the public sector. It never ceases to amaze me that our media and some government people think all of the boomers are about to retire all at once.

How does Canada’s retirement trend compare to other developed countries?
These other countries don’t have a baby boom like Canada. In Europe, each country has different demographics, but in general, the baby boom didn’t start until the mid-50s because of the post-war reconstruction. In Europe, even though the countries are older – they have a bigger percentage in the senior ages – their baby boom is actually younger and much smaller. In the US, they have a similar baby boom, which probably started a year before ours, but they have had a much higher fertility rate in the last 30 years, so they have a lot more young people coming into the workforce than we do here in Canada.

Is there a role for public policy to try and influence fertility?
Increasing fertility is probably a non-starter. Monetary incentives – baby bonuses – don’t work. However, if you provide good quality universal child care, you’ll see a better turn around with fertility rates. Unless you introduce a national, good quality, universal child care system in Canada, you’re not going to see a good turnaround. On the other end, you can encourage things like phased retirement – working half the time for half the salary, perhaps to age 70. Half the salary of a 60 year old could pay the full salary of a 25 year old. You can keep the knowledge in the workplace, get workplace renewal, and put an incredible team together, because young people are the champions of the latest technology and the older person has the experience and the knowledge. But it does pose a real policy challenge. Let’s say I work Tuesday, Wednesday, and Thursday at 60% salary, and I don’t work Monday or Friday. On the days that I’m working, I want to be able to continue to build pension credits. On the days I’m not working, I want to be able to withdraw. Our pension systems aren’t set up for that sort of thing. But it’s not difficult to do; that’s why we have computers. Certain individual companies can do it, but we need a much more flexible pension system to allow you to contribute and withdraw in the same year. The federal government is moving in that direction, but we’re still not there yet.

Ontario's Finance Minister has stated that if Ottawa doesn't enhance the CPP, Ontario will introduce its own provincial fund. Is that wise?

One of the points of a supplementary pension is to provide something that is portable, and that means portable across the country. I would argue that a provincial government setting up its own system wouldn't be optimal. Is it better to have something than nothing? Probably, and in particular, we need an opportunity for people to accumulate pension benefits on a basis that they choose. Think of all the consultants to the government. These are people running their own companies, often very small companies, and it's not easy for them to set up a pension fund. If they do, the management expense ratio is two or three percent, whereas we know in the Canada Pension Fund, you can get expert advice, and the benefits of pooling and risk sharing, with a much lower management expense ratio.

There are lots of people in Canada that don't have access to a corporate pension fund, who have run their own companies both in the public and private sectors, that will pay very high expense ratios under the current arrangements. We need a pension fund where you can contribute whenever you've got money. The cash flow for consultants is very lumpy, and when you get paid out on a contract, why shouldn't you be able to take $10,000 out of the contract and put it in the pension fund?

We need a pension fund, I would argue, that is universally available to everyone, that is not mandatory, that builds a pool of resources that allows you to access expertise, and that is separate from the Canada Pension Fund, because otherwise you're getting something that is too big to fail. If you get some bad decisions, you want a second pension plan to set up in competition to the CPP in some sense, so that you don't have all of your eggs in one basket.

The maximum annual benefit for the CPP is $12,000, and the average annual benefit last year was $7,000. Is this adequate?

Remember, that's on top of other government programs like OAS and so on. It's not the only source of income in retirement. It depends on the individual lifestyle – some people are very frugal and some people are not.

Some point to the Netherlands for its robust pension system. Should Canada?

Whenever I've travelled outside Canada, everyone points to Canada as the global brand, and the reason is we established the Canada Pension Plan back in the mid-60s, we established RRSPs in the 70s, we rejigged the Canada Pension Plan to invest globally in the 90s, and we've established these retirement savings options in the 2000s. That's four public policy events, and other countries in the world haven't even had one of them. In fact, whenever I travel, people refer to Canada as the gold standard regarding pension planning, not necessarily regarding the level of pensions.

And these events came about as a result of strong leadership?

Certainly the establishment of the CPP in the mid-60s came from long-term policy thinking. That used to be very apparent in the public sector, where the politicians brought the short-term to the table and the public servants brought the long-term to the table. The Deputy Minister was the one that negotiated the meeting of the ways, and that gave us public healthcare and public pension.

The latest change to policy was moving OAS and GIS eligibility from 65 to 67 starting in 2023 – a wise move?

Life expectancy has been going up two years a decade. Think about that – that means if you're 60 today, your life expectancy has gone up 12 years over your lifetime. In some sense, we should index age of retirement to life expectancy. Then it wouldn't have to be a political decision, it would just happen automatically once every five years when the latest data on life expectancy comes out. The age of retirement would just move a little bit. So it's probably a wise move, but I don't like it being in the political arena, it should be indexed to life expectancy.

Canada has done a good job of tackling the formerly high rates of poverty among seniors. Is that progress in jeopardy?

I see it in jeopardy. The reason is we're getting rid of defined benefit pension plans, and one of the reasons that we've been able to reduce the senior poverty rate – from over 20% to around 10% - is that these people can count on a stable income flow in retirement. The move from defined benefit to defined contribution takes that away. It also gives an opportunity for people in the financial sector to take real advantage of individuals trying to manage their own finances. The move to defined contribution is an indicator that we'll see an increase in the senior poverty rate.

What's the solution?

Go back to defined benefit and make sure that all part-time workers have pensions. All of these part-time people working in the service sector don't have pensions. When you're in your 20s you don't think you need it, you don't think you're ever going to get old, but it has implications down the road. We're jeopardizing Canada's future the way we're running our workforce today, with defined contribution pension plans or no pension plans at all.

"The whole decision-making apparatus in North America, particularly in the last decade, has become much more short-term in its focus, and that's not unique to the public sector. It's a disaster in terms of incorporating demographic information into decision making. Someone needs to take a leadership role – someone who's not tied in to the short-term."

Do Canadian governments adequately incorporate demographics into our public policy analysis?
I've said that demographics explains two-thirds of everything. In some instances, it explains significantly more than that – a good example would be school enrollments. In other cases, it could be significantly less than two-thirds – something like mental health issues might be one of those examples. We used to do a reasonably okay job, but we've fallen behind. What's happened is we've incented civil servants to think short-term, not long-term, by giving them annual bonuses. To incorporate private sector behaviour into the public sector is a disaster, because the private sector is very short-term in its focus. The impacts of demographics are medium and long-term.

Short election cycles contribute to the short-term thinking.
If you have three or four years in office, and it takes a couple years to get established and another year to get reelected, people are only thinking one or two years at a time. In the private sector, they really only think one year at a time and that's why we haven't seen any long-term investment in Canada in the private sector, even though we keep cutting corporate taxes and telling everyone they'll use that money to invest. They won't – they'll use that money to pay themselves bigger bonuses because they're only thinking short-term.

The whole decision-making apparatus in North America, particularly in the last decade, has become much more short-term in its focus, and that's not unique to the public sector. It's a disaster in terms of incorporating demographic information into decision making. Someone needs to take a leadership role – someone who's not tied in to the short-term. I'll give you one example of someone who was thinking longer term – Paul Martin when he was Finance Minister and he redesigned the Canada Pension Plan. He set it up as a global sovereign fund that could invest outside Canada. That was a leadership decision as far as that policy was concerned.

Demographics should be a major factor in all policy decisions, but it almost never is. About the only thing it's ever used in is pension policy, and that's because the actuaries actually insist on putting demographics there. More recently, it's been invoked in health policy planning, but in almost everything else it's not. Like in transportation planning; why would you expand public transportation in aging populations – they don't take public transit, at least not the current type of public transportation. You need to rethink things. A 75 year old is not going to stand on the street and wait for a bus at six at night. The other example is bailing out the auto-industry – no demographic analysis figured into that. As you get older you own fewer cars. An ageing population doesn't have the same automobile capacity, and you want more safety – you're not going to buy a dinky car.

A demographic filter should be used in public policy decision making, even if it ends up being overridden by short-term political needs. We've been overrun with the short-term in both the public and private sectors in Canada. Demographics is, if anything, being less utilized today than it was years ago.

DAVID K. FOOT is co-author of the best-selling books Boom Bust & Echo: How to Profit from the Coming Demographic Shift, and Boom Bust & Echo: Profiting from the Demographic Shift in the 21st Century. Following his undergraduate degree in Australia and his doctorate in economics from Harvard University, Professor Foot's research involved projections of the Canadian economy. He is a recipient of one of the national 3M Awards for Teaching Excellence and is a two-time winner of the University of Toronto undergraduate teaching award.