

Winter is coming

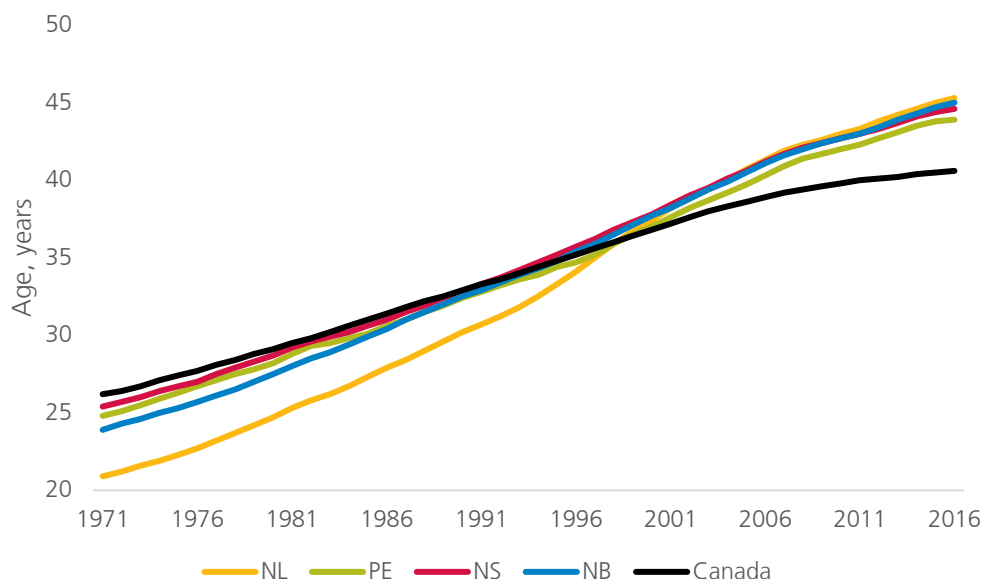
Why Atlantic Canada's aging population should scare governments (and the people who pay for them)

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It is no secret that Atlantic Canada's population is getting older. To be sure, an aging population isn't unique to Atlantic Canada. The massive population cohort of baby boomers (born between 1946 and 1964) and subsequent decline in family sizes and fertility rates have left many industrialized countries grappling to understand and prepare for what will happen as baby boomers retire from the work force and require greater levels of care. What makes this demographic shift so critical for the Atlantic region is that the aging population is hitting it before the rest of Canada. Over the past four decades the median age in the region has gone from being significantly younger than the national average to significantly older than the country as a whole (see figure 1). The shift will also, with the exception the recent projections for Prince Edward Island, mean outright decline in population over the next 20 years (see figure 2).

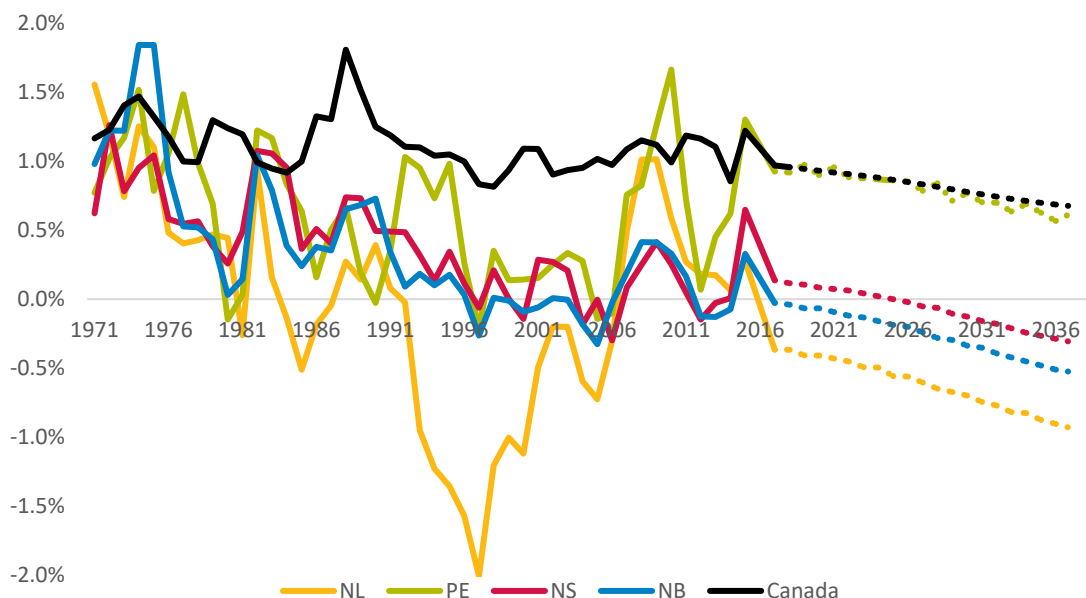
Figure 1:

Median age 1971-2016, national and Atlantic provinces



Source: Statistics Canada. Table 051-0001

Figure 2:

Annual population change 1971-2038, by province

Source: Statistics Canada. Table 051-0001 & Table 052-0005, medium-growth projections (1991/92- 2010/11 trend)

The curious case of PEI

How could one province in the region be bucking the population trends being experienced in the rest of the region?

The population numbers for PEI largely stem from a massive influx of immigrants beginning during the mid-2000s related to the province's Provincial Nominee Program and its "Immigrant Partner" stream which had investment requirements that were significantly lower than other provinces and did not require applicants to have active participation in a business.

While immigration levels have remained stronger than has historically been the case even after that program was effectively shut down, only time will tell if PEI will be able to attract and retain newcomers at the scale necessary to achieve population forecasts.

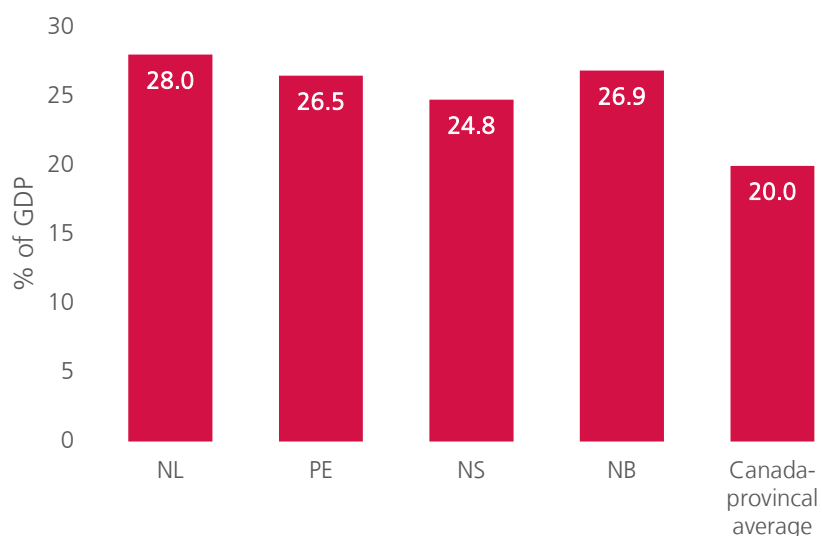
"Grey" Spending

Aesop's fable *The Ant and the Grasshopper* praises the virtue of working hard and saving for the winter season. Similar to the grasshopper, given the choice between long-term planning and dealing with immediate threats, politicians almost inevitably chose to act on the threats facing them right now rather than preparing for harsher times ahead. Unfortunately, dealing with the interests of the present has not put us on a rosy path for the future.

Given the demographic reality facing Atlantic Canada, it should be no surprise that small businesses are concerned about the sustainability of the public purse. As it exists right now, all four Atlantic provinces have expenditures that are higher than other provincial counterparts as a percentage of GDP (see figure 3).

Figure 3:

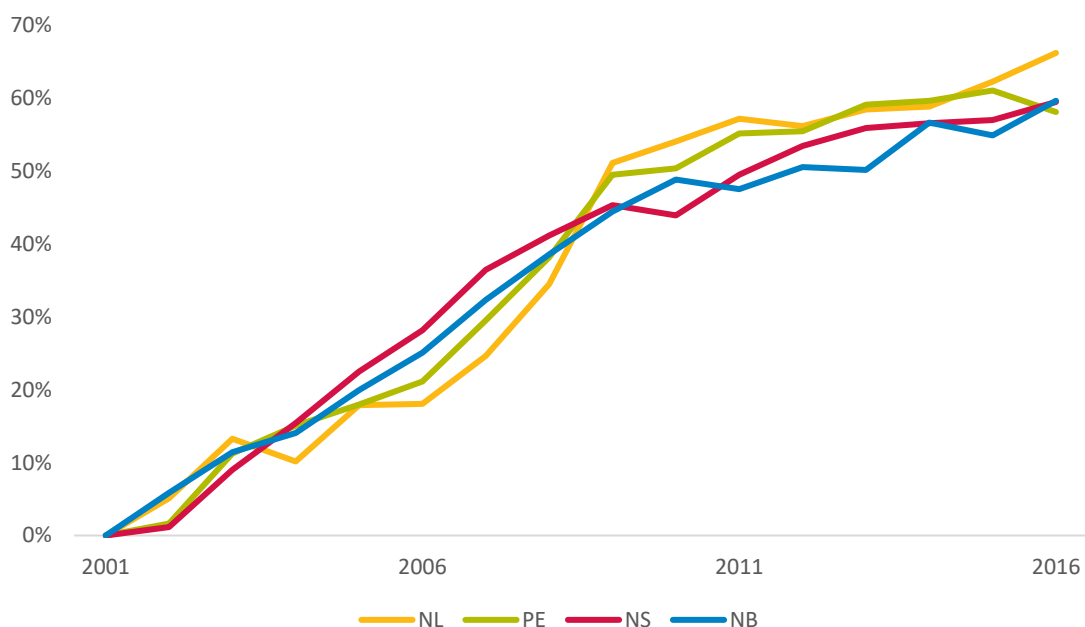
Provincial government expenditures, 2016-2017 (% of GDP)



Source: Provincial government budget documents

In addition to having high levels of spending, Atlantic governments also struggle to restrain spending growth. Inflation is often used as a benchmark for judging how well a government is controlling its spending. Allowing for inflation essentially means government is maintaining its existing programs but not creating new or more expensive ones without prioritizing within its existing spending envelope. While inflation hovers around 2 per cent annually, all four Atlantic provinces have averaged annual spending growth since 2001 that is double that rate, ranging from 3.9 per cent in PEI to 4.4 per cent in Newfoundland and Labrador. Cumulatively, this has led to substantial growth in government expenditures (see figure 4).

Figure 4:

Cumulative growth in total expenditures, by province

Source: Provincial Public Accounts, 2001-2015; Provincial Budgets 2016

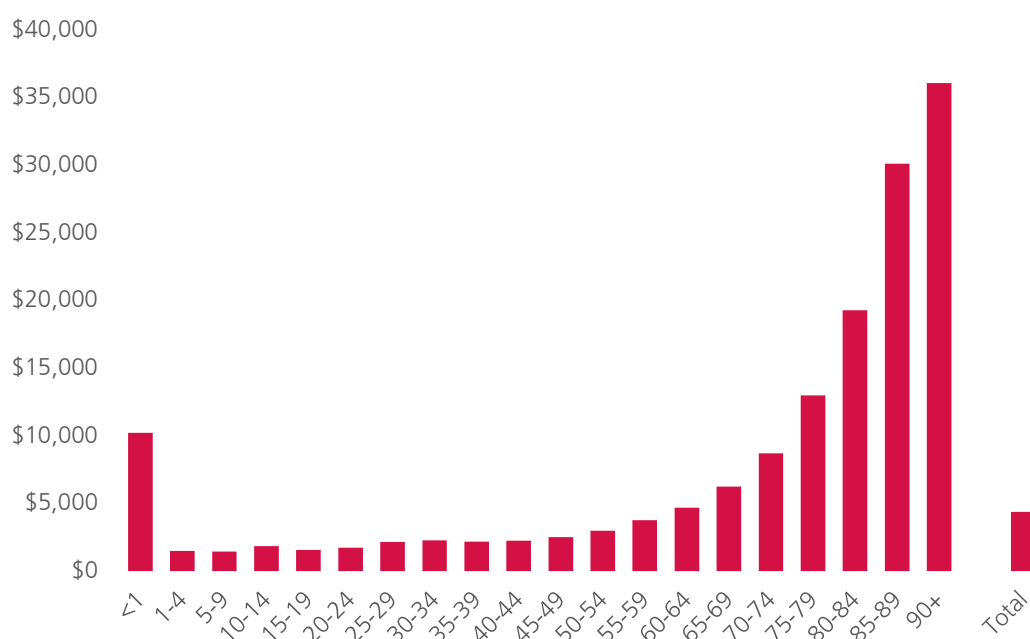
While there are always calls for new spending and programs, it is important for governments to keep in mind that even in the absence of new expenditures there will be considerable pressure coming to key existing government programs. Health care, seniors housing, long-term care and home care as well as other social programs that support seniors are likely to see increased demands.

Health care is probably the most obvious and well-studied area that will be impacted by aging since cost and consumption tend to increase near end-of-life (see figure 5).¹ With a senior population, demand for care can reasonably be expected to increase. Recent reports from the C.D. Howe Institute estimate the increased health care cost associated with the aging population would total \$245 billion for the Atlantic region (\$65B for NL, \$13B for PEI, \$89B for NS, and \$78B for NB)² over the next 50 years.

¹ [Canadian Institute for Health Information, National Health Expenditure Trends, 1975-2016](#). 2016.

² C.D. Howe Institute, [Managing the Cost of Healthcare for an Aging Population for NL, PEI, NS, and NB](#). 2015.

Figure 5:

Total Health Care Expenditures per capita by age group, 2014 Atlantic average

Source: Canadian Institute for Health Information, National Health Expenditure Trends, 1975-2016

Health care spending already represents the single largest spending area for provincial governments in the region representing a range of 35 to 40 per cent of total expenditures. It is also an area where governments face higher rates of inflation than the rest of their portfolios. The Canadian Institute for Health Information notes that provincial public spending on health has increased on average 7.4 per cent a year.³ This is largely due to increased physician spending, higher hospital costs, and higher prescription drug costs.

“Grey” Revenue

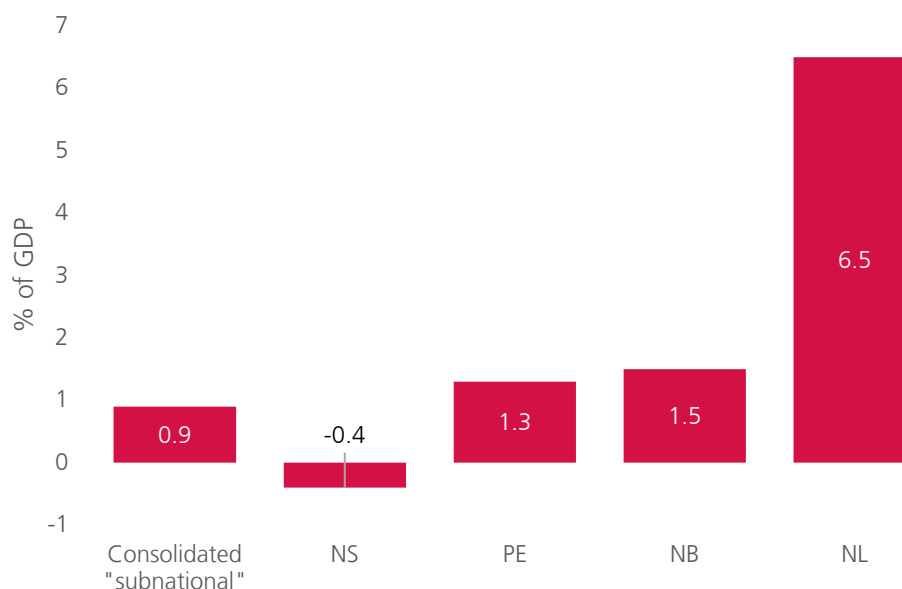
Even with better constraint on expenditures, balanced budgets will remain a challenge for Atlantic governments because many forecast that the aging population will mean slower revenue growth. Nominal Gross Domestic Product (GDP) is the broadest single measure of a jurisdiction’s tax base. Where governments have done longer-term forecasting, the impact of an aging tax base is a key factor in determining future fiscal health, inevitably pointing to low revenue growth. For instance, the federal Parliamentary Budget Office (PBO) released its *Fiscal Sustainability Report* in October 2017. In this analysis, the PBO makes predictions for each province in terms of the sustainability of its current fiscal position. With the exception of Nova Scotia, it predicts that all other Atlantic provinces have an unsustainable fiscal situation with “fiscal gaps” (the difference between projected revenues and expenditures) that range from 1.3 per cent of GDP in Prince Edward Island to 6.5% of GDP in Newfoundland and Labrador (see figure 6). In each case, the PBO projections assume spending to increase in line with nominal GDP and has adjusted for demographic change. Should governments increase spending beyond nominal GDP growth, their fiscal situation

³ [Canadian Institute for Health Information, Health Care Cost Drivers: The Facts](#). 2011.

would become less sustainable. Likewise, should governments restrain spending growth below the change in nominal GDP, then their sustainability would improve.⁴

Figure 6:

Parliamentary Budget Office “fiscal gap” projections



Source: PBO, 2017

Internationally, many countries that produce long-term budgetary forecasts are predicting the same trends. In the United States, the Congressional Budget Office’s (CBO) current 30-year forecast shows considerable spending pressure due to age-related demands (notably their Social Security and Medicare programs) and debt-servicing costs. As a means of illustrating the magnitude of the future budgetary shortfall, the CBO provides examples of the size of spending cuts or revenue measures that would be needed to maintain debt-to-GDP ratios.⁵

In Australia, intergenerational reports have been produced every five years since 2002 as a requirement under their Charter for Budget Honesty. These reports forecast the impact changing demographics will have on government programs and fiscal position over the proceeding 40 years. Long-term targets for improvement have been set and progress is tracked and reported. The result has been gradual improvement in the sustainability of public finances and greater accountability for the long-term impacts of policy decisions.⁶

In Atlantic Canada, provincial governments fall well short of such long-term analysis and planning with most provincial budgets including only basic projections for a few additional fiscal years. In Newfoundland and Labrador, this gap was recently noted by the Auditor

⁴ Office of the [Parliamentary Budget Officer, Fiscal Sustainability Report](#), 2017.

⁵ [Congressional Budget Office, Congress of the United States. The 2017 Long-Term Budget Outlook](#), 2017.

⁶ [Department of Treasury, Commonwealth of Australia. 2015 Intergenerational Report](#), 2015

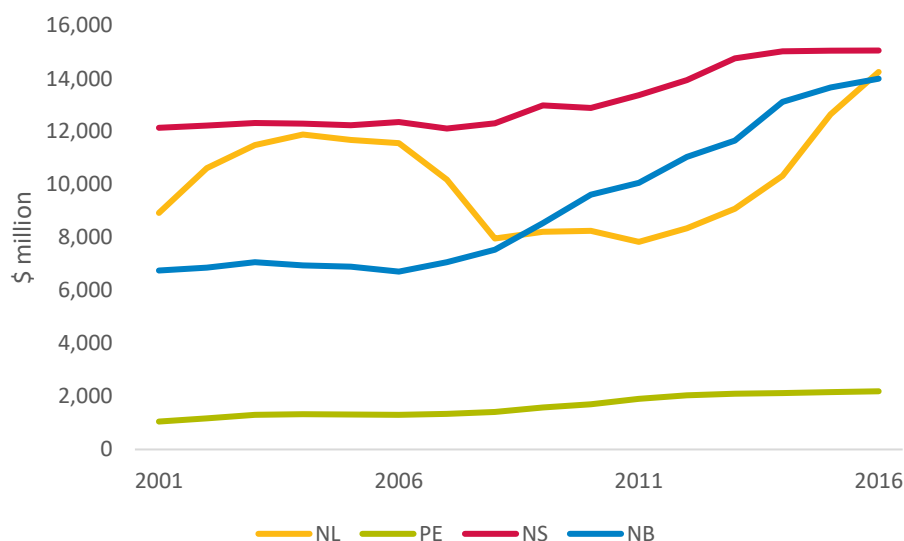
General in his 2017 Annual Report⁷ which contained an entire section noting gaps in government's preparedness for the demographic shift hitting that province.

Additional fiscal considerations

Beyond understanding the impact of age-related spending demands and “greying” revenues, the future of interest rates and bond ratings must be considered. Since the 2008 global recession, governments have benefitted from low interest rates. This has meant they have been able to increase their borrowing substantially (see figure 7) while limiting the impact on their annual budgets. With interest rates beginning to climb, this reality is slowly coming to an end and the impact will be felt by governments when they borrow or refinance existing loans. Unsustainable spending will also lead bond raters to downgrade government bond ratings meaning higher borrowing costs and a bigger bite from annual budgets.

Figure 7:

Net debt (\$ million), by province



Source: Provincial Public Accounts, 2001-2015; Provincial Budgets, 2016.

Fiscal recommendations:

1. **Each provincial government should “age-test” their programs and services** so that they understand the long-term cost implications and can make better long-term decisions. While there are few examples where this is done, the provinces can look at Australia’s intergenerational reports or the U.S. Congressional Budget Office’s forecasts as models to follow. Provincial analysis should include an examination of the impact rising interest rates will have on their overall fiscal health.
2. **Go back to the drawing board.** Many government programs are renewed with little evaluation and grow more and more expensive every year. If governments are to put

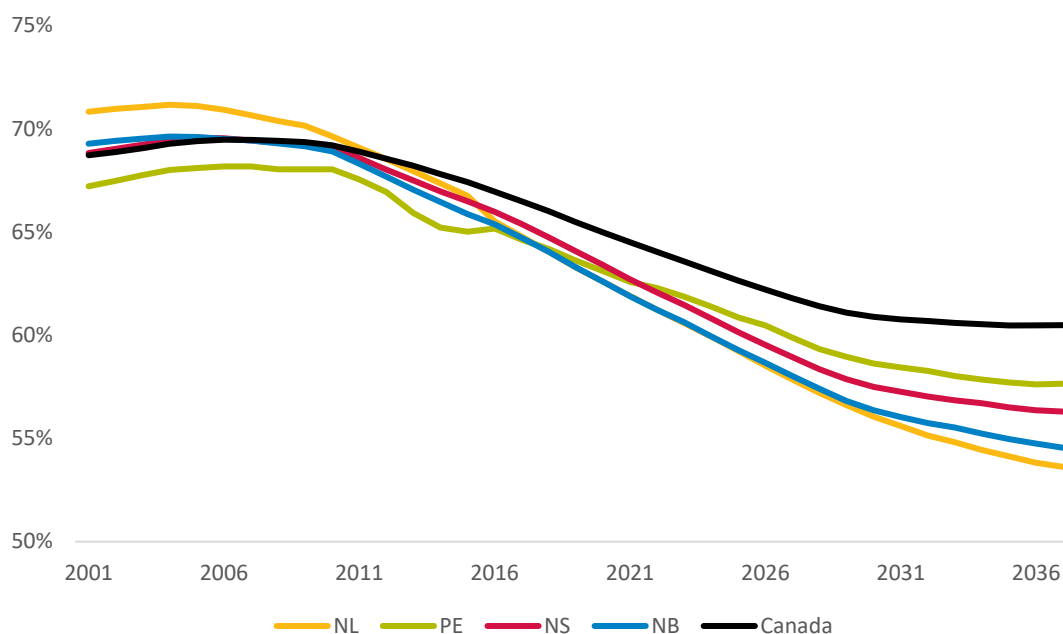
⁷ [Auditor General of Newfoundland and Labrador, Report to the House of Assembly on Performance Audits of Departments and Crown Agencies](#), June 2017

- themselves on a more sustainable spending path, all areas of government should be open to increased scrutiny to ensure that tax dollars are being used in the most effective ways.
3. **Restrain overall growth in spending.** Given that there will be increased demand in a number of program areas, it is of the utmost importance that governments focus on overall spending restraint. Enforcing restraint can be difficult in four-year election cycles, therefore, government should look to implement fiscal responsibility legislation that focuses on spending controls rather than just balanced budgets.
 4. **Work together.** Provinces do not have to act in a vacuum. Poor economies of scale in smaller provinces are often cited as a reason for high levels of government spending. Working together in certain areas can increase efficiencies and achieve overall savings. Such cooperation already exists in a number of areas. For instance, in health care, provinces frequently make use of specializations that exist in other provinces where it does not make economic sense to provide that care in each individual province or where staffing vacancies would otherwise mean that services are not available.
 5. **Resist the temptation to raise taxes.** Tax increases choke the ability of businesses to grow and consumers to purchase goods and services. The net effect rarely works in government's favour. On the other hand, small businesses reinvest any tax savings into their operations that result in greater productivity and economic returns.

Growth beyond population

Given the impacts of an aging population on government finances, economic growth will be critical. A key challenge in achieving economic growth will be the fact that the aging population also mean the aging of the Atlantic region's workforce. Traditionally, the working-aged population is considered to be those aged between 15 and 64 years. With more and more Atlantic residents entering retirement age (65 years and plus), there will be fewer and fewer potential workers (see figure 8).

Figure 8:

Working-aged residents (15-64 years) as % of total population

Source: Statistics Canada, Table 052-0005, medium-growth projections (1991/92- 2010/11 trend)

If there are not a sufficient number of workers to replace those who are retiring, it will be a significant challenge to maintain, let alone grow, the current economic output. Richard Saillant, former director of the Donald J. Savoie Institute at the Université de Moncton, projects that, when all factors are considered, real GDP growth over the next 20 years will range from retraction in Newfoundland and Labrador of -0.3% to growth of less than one per cent in Prince Edward Island.⁸ The 2017 Fiscal Sustainability Report from the PBO makes slightly more optimistic projections⁹ (see table 1), however, both predict rates of growth that are significantly less than what the provinces have seen over the past 15 years.

Table 1:

Real GDP growth, average & projections

	Average real GDP growth 2001-2015	Saillant "medium growth" real GDP projections 2013-2038	PBO real GDP projections 2017-2022	PBO real GDP projections 2023-2091
Newfoundland and Labrador	2.2%	-0.3%	-0.1%	0.2%
Prince Edward Island	2.1%	0.9%	1.7%	1.6%
Nova Scotia	1.3%	0.2%	0.9%	0.5%
New Brunswick	1.3%	0.3%	0.7%	0.4%

Source: Statistics Canada, Table 384-0038, Saillant (2016), PBO (2017)

To their credit, all four Atlantic provinces have developed population strategies aimed at increasing immigration and repatriating former residents. Such programs have yielded

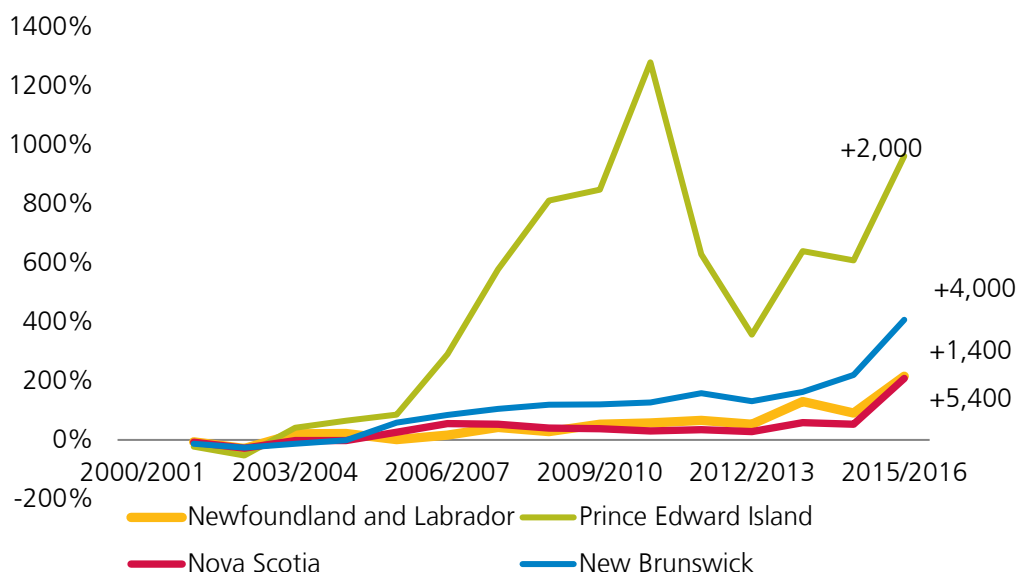
⁸ Richard Saillant, *A Tale of Two Countries*, 2016.

⁹ PBO, 2017.

some successes (see figure 9), notably, PEI has seen a substantial increase in international immigration as was discussed earlier.

Figure 9:

Annual international immigration, by province



Source: Statistics Canada. Table 051-0011

Increased immigration is a laudable and important goal, but it is one small piece of the puzzle. More people coming to our provinces in most cases will not be enough to completely offset population decline unless there is dramatic improvement to retention of newcomers and our existing population. It is also important to remember that our economic challenges will not simply be from declining numbers of people in our region but more so a decline in the number of productive workers, therefore, increasing the population alone is no magic bullet and there should be an understanding of the costs associated with retention efforts and skills training.

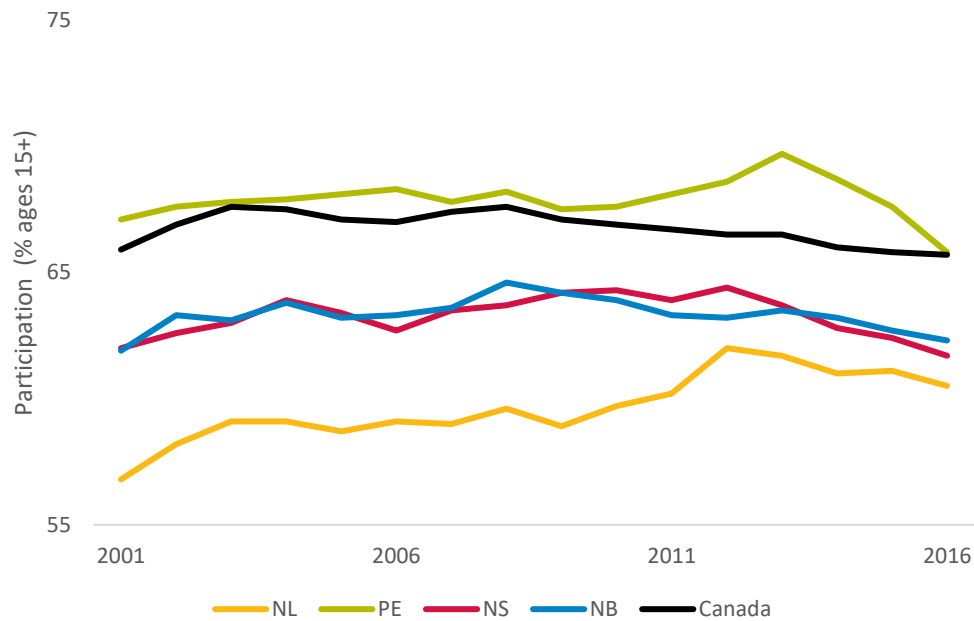
Labour force participation

With a decline in the working-aged population it is important, as much as is possible, we focus on better engaging people in the work force. This includes residents of all ages, abilities, and backgrounds. We know from small business owners, many are already responding to hiring challenges by looking at under-skilled or less experienced workers and providing them with on-the-job training and mentoring.

There are variations among provinces on participation rates, however the Atlantic region lags the national average (see figure 10). While it is reasonable to assume participation rates may naturally improve among the working-aged population due to the market demand to replace retiring workers, it is also incumbent upon government to ensure programs are not creating undue barriers to employment, ensure education and training programs provide appropriate skills, and create strategies aimed at increasing participation.

Figure 10:

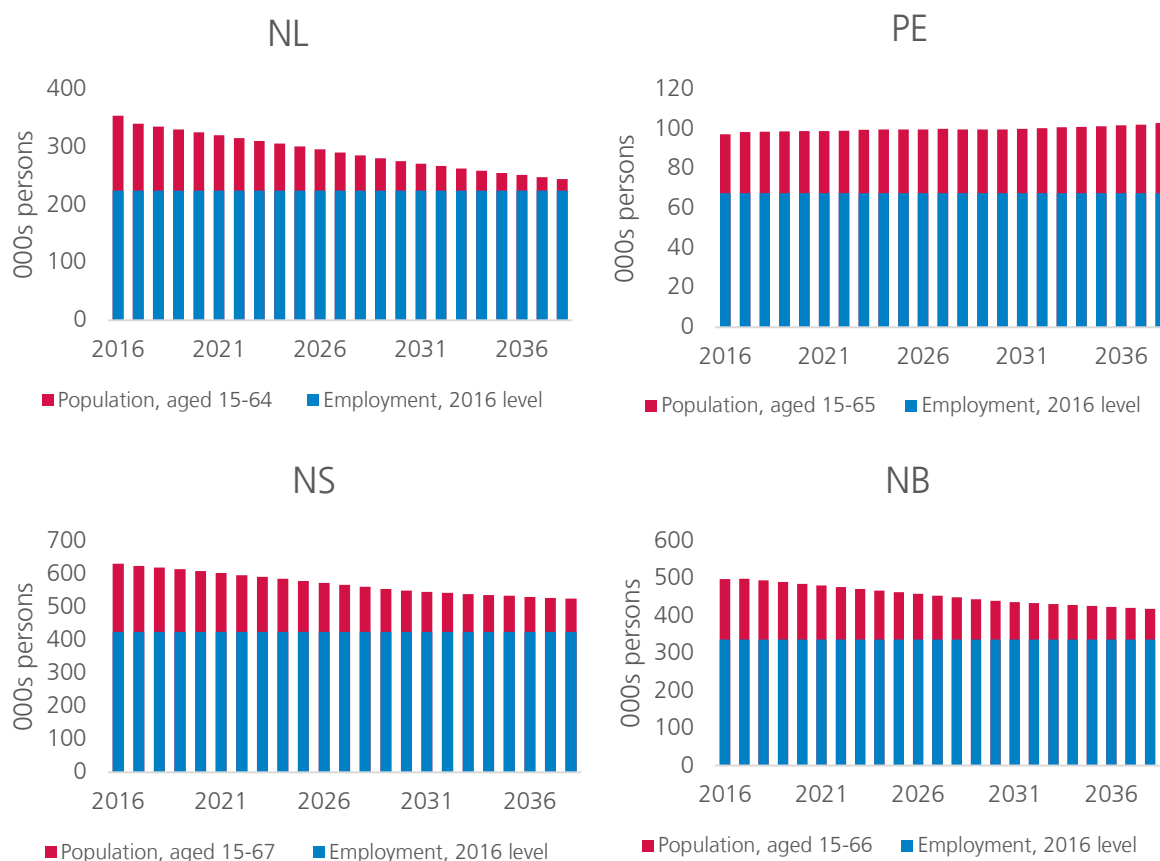
Labour force participation rates, by province



Source: Statistics Canada, Table 282-0002

If we are to maintain the current number of jobs in our region, provinces with declining populations would need to have a significantly greater portion of their work-aged population engaged in the workforce (see figure 11).

Figure 11:

Work-aged population (15-64) versus 2016 employment, by province

Source: Statistics Canada, Tables 282-0002 and 052-0005, medium-growth projections (1991/92- 2010/11 trend)

Looking at the current labour force there are groups of individuals that are under-represented, notably ethnic minorities, newcomers, and those with disabilities. Any programs and services designed to assist individuals who are not fully engaged in the work force should ensure that such programs are effectively reducing barriers to labour attachment and are ensuring that any skills training provided is a good match for available jobs.¹⁰

In addition, involvement of senior populations in the work force should not be overlooked even if that involvement is post-retirement, part-time, seasonal, or in a different industry. With people living longer, healthier and more active lives, many are capable of working beyond conventional retirement age and doing so, even if in a limited capacity, can help improve the incomes of seniors, ensure retirement savings last longer, and promote social integration.

Productivity

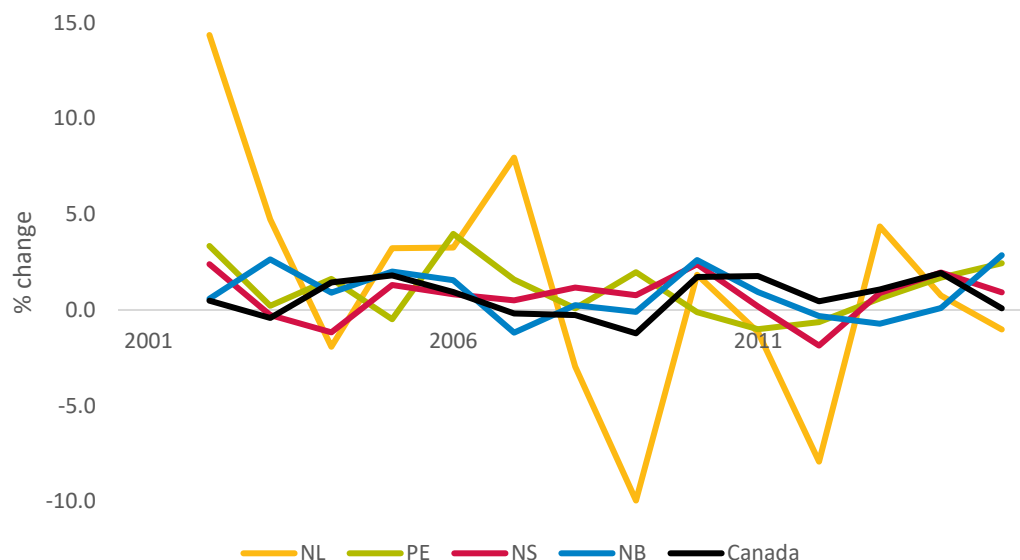
With population challenges, prospects for economic growth in the Atlantic region will be limited without a concerted effort to increase productivity: the amount of economic output produced per worker. While Newfoundland and Labrador has experienced years of

¹⁰ [CFIB. Small business, big investment: Improving training for tomorrow's workforce. 2015.](#)

considerable growth and others of significant decline corresponding to the impact of natural resources prices on their GDP, the rest of the region has had relatively low and steady productivity growth (see figure 12).

Figure 12:

Annual productivity growth, by province



Source: Statistics Canada, Tables 384-0038 and 282-0002

There are many reasons for this, including; access to capital, lower economies of scale, and a larger-than-average public sector. Because much of the region has not had to cope with chronic labour shortages, productivity has not been a top priority for governments or many businesses. With fewer workers, we must support efforts to improve productivity through training, innovation, and investments and government policies should be designed to support those efforts rather than hinder them.

It is important to note that “innovation” and productivity improvement from the perspective of small businesses may not fit into government definitions of innovation. When it comes to government programs and priorities, the innovation agenda is largely focused on high-tech start-ups or strategic clusters. For small businesses, innovation is happening in all industries and often takes the form of new or improved products and services or creating new or improved internal processes. For them, barriers to innovation include struggling to find qualified labour, government red tape, and the costs involved.¹¹ If government is to help support small businesses be innovative and boost their productivity, and thereby economic growth, it is important that it focus on addressing those key barriers rather than limiting their definition of innovation. Governments can likewise be innovative in the ways they design and deliver and aim to improve their own productivity.

¹¹ [CFIB, Beyond the Big Idea](#), October 2016.

Economic development recommendations:

1. **Continue with population strategies that focus on increased immigration, including improved retention.** As much as is possible, focus should be placed on attracting immigrants with skills that are in demand by small businesses, including lower skilled workers and support services should focus on work force attachment.
2. **Improving participation in the labour force is key.** It is unlikely that immigration alone will lead to a complete replacement of existing workers. Engaging more residents in the work force than has historically been the case will further help to offset the impact of retiring workers.
3. **Atlantic Canada needs a heavy emphasis on productivity improvement.** This can come from improved labour productivity (i.e. skills and training), capital and technology investments, or making better use of both labour and capital. Industrial profiles can also have a significant impact on productivity with higher-valued exports leading to higher GDP returns.

Since governments tend to have a poor track record for picking winners and losers in the economy, measures to improve productivity should focus on creating an overall environment for success. Better than grants and programs, tax relief provides an efficient means of ensuring businesses have the means to invest in their own operations. Further to tax relief, governments can help to improve the productivity in small businesses by streamlining their regulatory environments.

What about the federal government...

The role the federal government can or should play in the fiscal sustainability of our provincial governments is a matter of considerable debate. Rather than wading into such a debate, our recommendations are focused on areas that are within the control of the provincial governments. To the extent that the federal government can support these recommendations and goals, they should at least not work counter to them. The Atlantic Growth Strategy is one avenue for the federal and provincial governments to work together.

Conclusion

The population challenges that are facing Atlantic Canada are real and are already beginning to be felt by businesses and governments in the region as baby boomers begin to age out of the work force. This aging of the population will have significant impact on both government finances and the region's economic development.

While population strategies are certainly a wise course of action for provincial governments, it is unlikely that immigration or even better retention alone will offset the impact of retiring workers. It is important that both government and businesses look to improved participation of residents in the work force and improved productivity if Atlantic Canada is to thrive in an environment where labour is scarce and demands for expensive government programs are growing.

Appendix A: Provincial Profiles

New Brunswick

Population & Participation

New Brunswick currently has the second oldest population in the region.

	Current Population	Population 2038	% change
Total	756.3 thousand	716.6 thousand	- 5.2%
Working-aged (15-64)	494.4 thousand	390.9 thousand	-20.9%
Median Age	45	49.8	10.7%

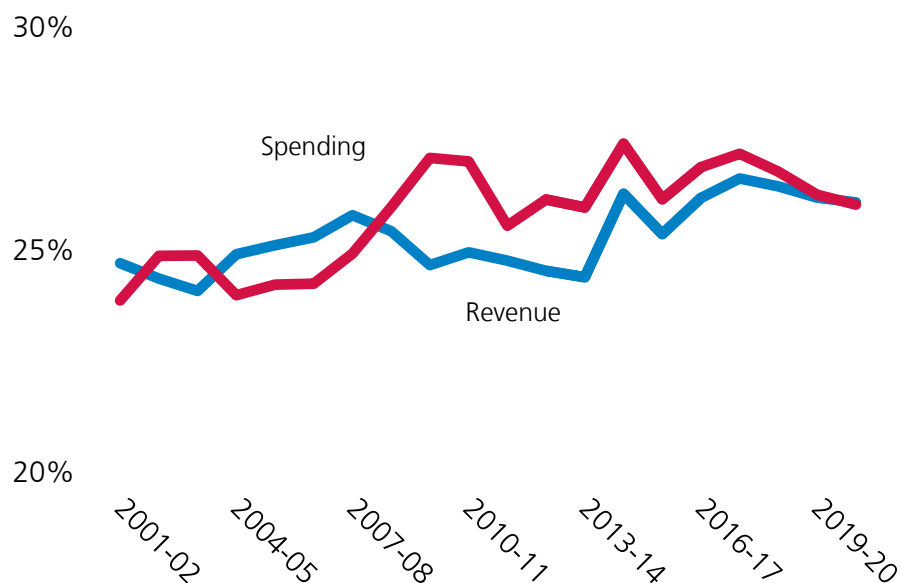
The highest participation rate experienced in New Brunswick (2001-2016) was 65 per cent in 2008.

Economic growth

	Average, 2001-2015	Saillant's "medium growth" projections 2013- 2038	PBO real GDP growth projections 2017-2022	PBO real GDP growth projections 2023-2091
Real GDP, annual growth	1.3%	0.3%	0.7%	0.4%
Productivity, annual growth	0.9%	0.6%	1.2%	1.0%

Fiscal situation

In its most recent budget, the New Brunswick government posted a \$192 million deficit. It appears to be on track to reach its balanced budget target by 2020-2021 though it will be a challenge to maintain balanced budgets over the long-term given spending patterns.



Nova Scotia

Population & Participation

	Current Population	Population 2038	% change
Total	949.5 thousand	933.9 thousand	- 1.6%
Working-aged (15-64)	631.3 thousand	525.8 thousand	-16.7%
Median Age	44.6	49.6	11.2%

The highest participation rate experienced in Nova Scotia (2001-2016) was 64 per cent in 2010.

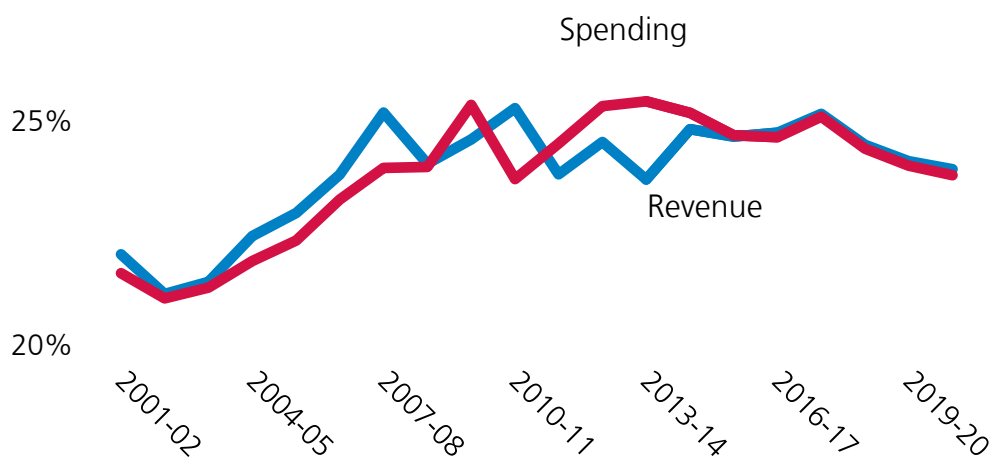
Economic growth

	Average, 2001-2015	Saillant's "medium growth" projections 2013-2038	PBO real GDP growth projections 2017-2022	PBO real GDP growth projections 2023-2091
Real GDP, annual growth	1.3%	0.2%	0.9%	0.5%
Productivity, annual growth	0.8%	0.5%	1.3%	1.0%

Fiscal situation

Nova Scotia is starting with a stronger position than many other provinces. Government was able to table balanced budgets in 2016-17 and 2017-18 and has been proactive in managing its labour costs. That's not to say that it does not also face significant challenges.

30%



Prince Edward Island

Population & Participation

Prince Edward Island currently has the youngest population in the region and the total population is expected to grow. Such growth depends upon significantly stronger immigration and retention than has historically been the case.

	Population 2016	Population 2038	% change
Total	148.6 thousand	178.3 thousand	18.1%
Working-aged (15-64)	97.2 thousand	102.8 thousand	-16.7%
Median Age	43.9	49.6	11.2%

The highest participation rate experienced in Prince Edward Island (2001-2016) was 70 per cent in 2013.

Economic growth

	Average, 2001-2015	Saillant's "medium growth" projections 2013-2038	PBO real GDP growth projections 2017-2022	PBO real GDP growth projections 2023-2091
Real GDP, annual growth	2.1%	0.9%	1.7%	1.6%
Productivity, annual growth	1.2%	0.3%	0.7%	0.4%

Fiscal situation

In many cases, Prince Edward Island is doing better than its regional counterparts when it comes to economic growth and population. This has enabled the province to balance its 2017-18 budget. While this is good news, it does not mean the province is immune to the challenges of an aging population.



Newfoundland and Labrador

Population & Participation

Newfoundland and Labrador has gone from having the youngest population in 1971 to the oldest in 2016.

	Current Population	Population 2038	% change
Total	530.1 thousand	455.6 thousand	- 14.1%
Working-aged (15-64)	353.9 thousand	244.3 thousand	-31.0%
Median Age	45.3	53.3	17.7%

The highest participation rate experienced in Newfoundland and Labrador (2001-2016) was 62 per cent in 2012.

Economic growth

Natural resource royalties have made Newfoundland and Labrador somewhat of an outlier in the Atlantic region over the past decade and have fed significant growth to the province's GDP.

	Average, 2001-2015	Saillant's "medium growth" projections 2013- 2038	PBO real GDP growth projections 2017-2022	PBO real GDP growth projections 2023-2091
Real GDP, annual growth	2.2%	-0.3%	-0.1%	0.2%
Productivity, annual growth	1.1%	0.9%	1.2%	1.0%

Fiscal situation

While there were strong revenues when oil prices were high, low oil prices on the world market have led to significant deficits and substantial tax hikes in the 2016-17 budget. This unpredictability highlights the need to ensure spending will be sustainable even when royalties are not flowing. While government states that it is on track to balance the budget by 2022, Finance Minister Tom Osborne is clear that spending challenges remain.

