The Long-Term Growth Challenge: So Many Questions, So Few Easy Answers

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The Canadian economy faces serious growth headwinds over the next few decades, and policymakers across the country should be thinking hard about how growth can be improved. Many policy options will hopefully be considered, but finance ministers will soon find that there are no quick fixes. Economic growth is a complex process.

The broadest measure of average income is per capita GDP, which is simply the overall national income divided by the number of people. Over long periods of time, this measure grows for two reasons—improvements in labour productivity and increases in the labour-force participation rate.

Since 1970, per capita GDP in Canada has increased at an average rate of 1.3% per year—enough to double average income in roughly two generations. Higher productivity accounted for 0.9% of this; the remaining 0.4% comes from greater labour-force participation. The rising labour-force participation has, in turn, been driven by two factors: more women entering the labour force and the economic coming-of-age of the baby-boom generation.

What is projected to occur over the next quarter century? Productivity growth has slowed dramatically in recent years, and if trends continue it will rise by only about 0.4% annually. The aging of the baby boomers will lead to a significant decline in the labour-force participation rate, from about 67% today to about 61% by 2040. This aging will actually *subtract* from annual income growth by about 0.3%. So the overall projection for per capita GDP between now and 2040 is an annual growth rate of a measly 0.1%—barely noticeable for the average family, even after a few *decades* of compounding.

These are precisely the growth headwinds that led the federal finance minister, Bill Morneau, to create his Advisory Council on Economic Growth (on which I sit). The fourteen members of the Council, headed by McKinsey's Dominic Barton, will meet several times over the next year to develop a strategy for improving Canada's growth rate.

There is nothing easy about the Council's task. While governments across the world have long been interested in developing policies to enhance economic growth, one of the only universal lessons is that there is no easy solution. But there are lots of possibilities worth examining.

More capital investment would likely lead to higher growth, but can this best be encouraged through corporate-tax cuts, more generous investment tax credits, or with policies to enhance household saving? Or perhaps we need to relax the current restrictions on foreign direct investment in order to take advantage of savings from the rest of the world?

Better infrastructure might be an important part of the solution, but which infrastructure matters most? Is it bridges and highways that facilitate greater cross-border trade, airports that encourage two-way flows for business and tourism, public transit in urban centers, or electricity grids that allow for trade across provinces?

A more highly skilled labour force would likely increase our growth rate, but what is the best way to improve skills? Would better primary and secondary education do the trick, or would our scarce resources be better spent on universities and technical schools? Or maybe it's not about spending more public dollars, but instead about redesigning our system to produce graduates with different kinds of skills.

Maybe financial markets lie at the heart of our growth challenges, with too few venture capitalists and commercial bankers too conservative in their risk assessments and lending practices. If so, what is the right policy response, especially since we already have crown corporations making loans to the private sector? And should governments even be in the business of providing venture capital?

There is plenty of evidence that an important source of growth is greater competition; there currently isn't much in some of our industries, including banking, telecommunications, and airlines. Reforming regulations, reducing tariffs, and removing ownership restrictions could unleash the competitive forces that drive innovation and long-run improvements in average income.

Mr. Morneau knows that few things could be more important to Canadians' prosperity than improvements in our long-run growth rate. His Advisory Council will be asking questions and reviewing evidence that has been discussed many times; this is well-trodden ground. Hopefully the members' fresh look and outside perspective will lead to new and promising ideas.

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