

Demographic shock: An update It remains a problem for the next fifteen years!

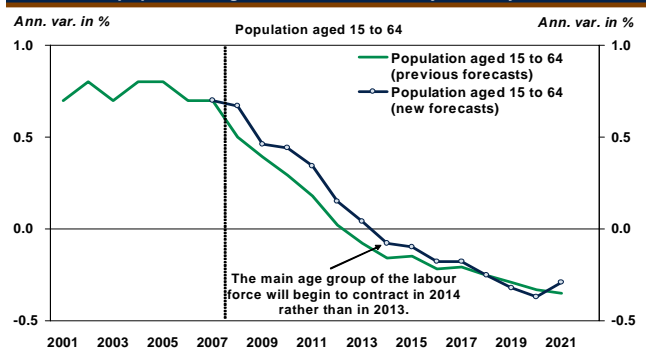
We tackled Québec's demography problem in two recent issues of the *Economic Viewpoint*¹. These studies are in part based on demographic outlooks provided by the Institut de la statistique du Québec (ISQ) and Statistics Canada. The ISQ has recently updated its projections, which are more optimistic over a very long horizon. According to the body's new projections, Québec's population will not decline before 2056; previous forecasts called for a demographic decline in around 2031. Due to an increase in the birth rate, Québec's natural increase will remain positive until 2029; subsequently, immigration will be entirely responsible for population growth. The phenomenon of aging will still be very much with us. Of the 1.6 million additional inhabitants that Québec should have in 2056 compared with 2006, 1.5 million will be 65 or older.

Some may think that the new data change the conclusions of our previous studies. Upon verification, however, we see very few changes, especially for the next fifteen years.

Moreover, the change had been partially anticipated (see the remark on page 5 of the May 28, 2009 *Economic Viewpoint*) and our studies focused on a nearer timeframe. Comparing the ISQ's new forecasts with its previous ones show that, in fact, much of the changes primarily affect very long-term data, post 2030. In the nearer term, the picture is almost identical. For example, the beginning of the decline of the population aged 15 to 64, which is highly representative of labour force evolution, is put off by just one year, from 2013 to 2014 (graph 1).

¹ *Economic Viewpoint* "Québec economy: The adverse effects of demographic shock are looming – It is important to act now to soften the impact on the labour market," dated August 13, 2008; *Economic Viewpoint* "Impact of the demographic shock on Québec's economy – Slowdown in GDP growth will have far-reaching consequences," dated May 28, 2009.

Graph 1 – According to the ISQ's new outlook, the decline in the population aged 15 to 64 will come just one year later



Sources: Statistics Canada, Institut de la statistique du Québec and Desjardins, Economic Studies

THE DIE IS CAST!

The first study, published August 13, 2008, described the magnitude of the demographic shock and its consequences for Québec's labour force. It also focused on the fact that the shock would begin very shortly and could not be avoided over the near or medium term. For example, Québec would have to welcome about 300,000 immigrants a year to stabilize the population aged 15 to 64, a figure which corresponds to the total number of immigrants who come to Canada every year. Even if the birth rate suddenly shot up to 2.1, the minimum rate needed to replace the population, this would not turn the trend around quickly. The impacts of a pro-natalist policy can only be seen over the very long term. However, measures that are designed to increase the portion of the population aged 15 and up that is entering the job market can have a much more immediate and meaningful impact on the size of the labour force.

Unless its labour force increases, Québec is vulnerable to serious consequences, addressed in greater detail in the

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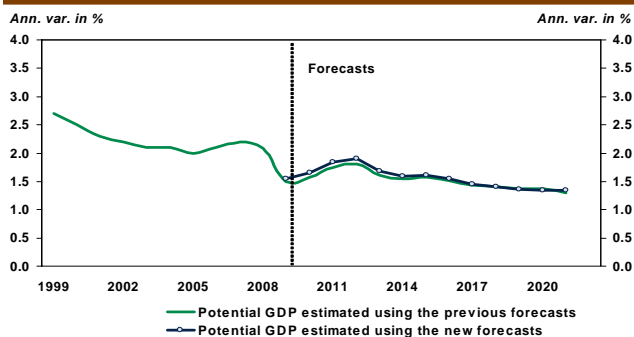
NOTE TO READERS: The letters **k**, **M** and **B** are used in texts and tables to refer to thousands, millions and billions respectively.

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second study, released last May 28. According to previous forecast for the evolution of the labour force, growth of potential GDP (the economy's long-term average growth rate) would drop substantially by 2021.

The estimates of potential GDP were revised following the ISQ's recent update to its demographic data. However, the initial calculations were based on labour force projections published by Statistics Canada, which have not yet been revised. Given that the ISQ does not publish a labour force outlook, potential GDP growth has been re-estimated according to our own forecasts, adjusted based on the new data on the population aged 15 to 64. In the end, our new potential GDP estimates are very similar to our initial estimates. The biggest gaps occur before 2014 but they are still relatively small (graph 2).

Graph 2 – Our estimates for the Québec economy's potential growth are almost unchanged

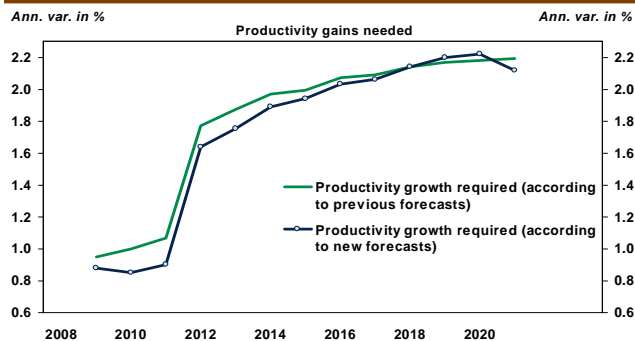


*Estimation based on a constant returns to scale production function, the available and forecast quantities of labour and capital, and on constant growth in technological developments.
Sources: Statistics Canada, Institut de la statistique du Québec and Desjardins, Economic Studies

To limit the decline in its growth potential, Québec could look to an increase in productivity gains. However, increasing productivity means producing more with the same amount of resources, which is not easy to do. In the last few years, Québec has posted an average labour productivity increase of about 1.0% a year. According to our new forecasts, the productivity gains that would be needed to keep potential GDP growth at 2% until 2021 are still sizeable (graph 3). They would have to more than double. Unless a decline in economic growth can be prevented, government income growth could be quite limited at a time when spending will increase due to the population aging that is still expected.

Note, however, that less of an effort would be required in terms of productivity gains if more people entered or remained in the labour force. Moreover, investment, which translates into an increase in the amount of productive capital, is another factor that could contribute to potential economic growth.

Graph 3 – Substantial productivity gains will still be needed to keep potential growth close to 2%



Sources: Statistics Canada, Institut de la Statistique du Québec and Desjardins, Economic Studies

OUR CONCLUSIONS STILL STAND!

Thus, despite Québec's improved demographic outlook over the longer range, the problems and challenges to tackle within the next 15 years remain. The conclusions set out in our recent studies still hold up; we encourage you to consult them.

True, the situation may not be as difficult as we could have feared over the very long range, although nothing guarantees that the population will not shrink, sooner or later. In any event, we must not entertain any illusions. The proportion of people aged over 65 will be much greater than it is today and pressure on the public finances will remain heavy. The slight leeway provided by the change to the demographic projections should not be used as an excuse to avoid making the decisions that must still be made today. Moreover, the higher birth rate now being recorded means that, in the short term, we will have to care for and educate more children than we had previously expected. As a result, this will certainly put extra pressure on balancing the public finances for several years, until these young people enter the labour force and contribute to the public coffers.