Marris Miller

Environment for Retirement

Generational Shifts, Productivity and Growth: *The Big Picture*

The Pension Papers™

Environment for Retirement

Executive Summary

As we move more deeply into an aging society in the Western world, we have come to realize that the social and economic context of aging affects how we live, how much we choose to save and what we can expect from our pensions.

Few Canadians are financially ready for retirement. But this is only a small part of the problem: companies may not be ready either. Demographic movements could have an impact on corporate and investment-based pension fund performance because generation shifts may affect new contributions, productivity and growth.

In this paper, we look at how our aging society will have an effect on how we plan for our futures, whether or not we have a secure pension in place and discuss why corporations and organizations must create an ethical way to introduce their employees to financial management.

The information in this publication should not be relied upon as consulting advice. We encourage you to contact us directly with any specific questions.
© 2019 Marris + Miller. All rights reserved.

Canada's population is aging, like other Western countries around the world. The last census in Canada, which took place in 2016, showed that there were 5.9 million people aged 65 and older in the country, which is the largest increase in that age group over prior demographic findings in almost a century.[1] By 2025, one in five Canadians will be 65 or older.

This is because, as the world population increases, the rate of births is decreasing – especially in developed countries like Canada and in Europe. From an economic perspective, this means a rapidly aging population that could have a detrimental impact on future generations. To secure our financial future, we need to take a fresh look at the workforce evolution that bring the new pension designs to light to help businesses succeed.

Despite the fact that there is an assumption that pension plans assure the elderly of a secure future, this is not necessarily the case.

As of today, the fertility rate is 1.60, which means we are not replacing ourselves.[2] What contributes to the 0.88% population growth are migrants who, hopefully, are well-educated and prepared to enter the labour force.

We need to look at how our aging society will have an effect on how we plan for our futures, whether or not we have a secure pension in place. Demographic movements could have an impact on pension fund performance because generation shifts may affect new contributions, productivity and growth.

Economically, company pension plans are defined as any corporate savings plan that employees contribute to through their payroll, which can include matching plans, defined benefits, or RSP investment strategies which act as a benefit due to corporate co-investment. This separates corporate plans from Canada and Quebec Pension Plans (CPP/QPP), which are federally-mandated investments to which every worker in Canada must contribute, as well as two other programs called Old Age Security and (for those with no other resources) the Guaranteed Income Supplement.

Despite the federal mandate, however, few Canadians are financially ready for retirement.

A recent report from a CIBC poll suggests that 32 per cent of Canadians between 45 and 64 have nothing saved for retirement, and 53 per cent of Canadians say they don't actually know if they are saving enough at all.[3] Out of those who have been saving, only 10 per cent of them have a plan in place.

---

[1] Russell, A. (2017). Is Canada's health-care system ready for our rapidly greying population? *Global News,* 5 May. Retrieved from https://globalnews.ca/news/3429041/healthcare-stats-canada-2016-census/.
[2] https://www.worldometers.info/world-population/canada-population/
[3] Lovett-Reid, P. (2019). 32% of Canadians are nearing retirement without any savings: Poll. *BNN Bloomberg*, 8 February. Retrieved from https://www.bnnbloomberg.ca/32-of-canadians-are-nearing-retirement-without-any-savings-poll-1.991680

This is despite the fact that, as CIBC estimates, the average Canadian needs at least $756,000 to plan for our now-normal 30 years of retirement, and this is a very conservative estimate when we think about how inflation has affected growth indicators in recent years. The CIBC poll discovered that most people have saved only around $184,000 by the time that they retire. And we're not alone: Americans have an even worse savings rate in place, with the median amount of post-job savings only hitting US$5,000.

So, why is this the case? Why do we in the Western world, with all of the resources we have at our fingertips, fail to plan ahead when we know that we're so far from our goals? How are we lacking in this area and what can we do to change things?

The social and economic context of aging

The social and economic context of aging affects how we live, how much we choose to save and what we can expect from our pensions.

How many members of the working-age population are needed to support those over age 65?

More than we think.

The way that CPP/QPP was set up originally was as an investment in our future, rather than an investment in a fund: current workers are meant to provide the tax dollars needed to fund retired workers. For every individual who needs to retire, therefore, there needs to be 2.3 people contributing to Canada pensions at the current replacement rate. As we age as a society, and more people are retiring, that number has been on the increase.

As a large proportion of Canadian society ages, we as a nation will face many challenges in an effort to provide support for our elderly population that will complicate our ability to rely on CPP/QPP. In addition to psychological, mental and physical disabilities which increase economic and social costs, the frail elderly population are also vulnerable and lack economic support and therefore are unable to successfully mitigate the financial demands of old age. This means that the cost of being elderly may be going up for our social services: the more that we age as a society, the more that we need to pay for health care and other costs.

The predicament we're in is, however, a result of changing social norms around aging.

As a result of capitalism and neoliberalism, aging has come to be understood in terms of biological science's attention to innate and virtually immutable processes, in which the utility of the human being slows and then comes to an end.[4] When a person once was a thriving member of society, they become perceived as limited and useless due to the fact that they are no longer able to contribute to their own and others' financial health. Not only can the elderly not work, but more funds will be

[4] Powell, J. & Hendricks, J. (2009). The sociological construction of ageing: Lessons for the rising. *International Journal of Sociology and Social Policy, 29*, 84-94.

needed to pay for health care due to the fact that older patients' illnesses and recovery cycles are likely to be much more complex than younger patients', and government benefits for seniors are likely to exceed the ability of the younger generations to pay for these services.

What this means is that when a society holds, as one of its primary values, a focus on economic production and efficiency, the elderly are likely to suffer.

Ageism refers to the cultural, political, and socio-economic discrimination of people on the basis of age, but a recent article from CNN suggests that it is not something that is only imposed upon people, but that ageism can become internalized.[5] As people age, when they believe that they will become infirm, there is a greater chance that they will. As noted in the article, at a recent meeting of the National Academies of Sciences' Forum on Aging, Disability and Independence, it was found that if those who are aging are able to believe in their own ability to be well, they would live an average of 7.5 years longer than those who did not. The article suggests that the elderly need to combat their own biases against what it means to move through this part of the human development cycle so that they can have a happier and healthier time as an older person.

The reality is, though, that when the elderly are affected by poverty, they won't necessarily be able to achieve this goal.

With the current set-up of CPP/QPP, the average elderly person will receive just over $13,000 per year in benefits. It is thought by many that the federal government's Plan cannot sustain itself. With fewer younger people contributing to the fund, the amount of subsidies available to the elderly in their retirement decreases.

Not only are they not able to lean on federal pensions, but our social world has changed in a significant way so that fewer elderly people are living with their younger relatives as they age.

It's gotten to the point that we're looking at how to integrate long term care into our community and health care planning. In 2002, the Romanow Report suggested that the current health care system, as it stood, could not support the Canadian public for an undefined period of time.[6] As noted by Romanow, with a rising average age, there would be more seniors in the country than ever before, placing a burden on the health care system because of their natural frailty and an equal burden on the taxpayers of Canada to fund their care. There was, according to Romanow, a need for a new infrastructure that would align with the health care demands of this population and with the needs of a country with an increased number of immigrants to make up for the population deficit. The changes that he recommended included expanding long term care facilities across the board. Ontario is

[5] Graham, J. (2017). How to beat the stereotypes around aging. *CNN*, 14 November. Retrieved from http://www.cnn.com/2017/11/14/health/beat-aging-stereotypes-partner/index.html.
[6] Romanow, R. (2002). *Building on Values, the Future of Healthcare in Canada*. Ottawa: Government of Canada.

lready doing this: they are creating budgets for long term care so that the elderly will have a place to live, given the fact that there are so many constraints on their incomes in the present day.[7]

What does this mean for the average person edging towards retirement? What is the role of business, the government and individuals in preparing for a new workforce? Will pensions still be able to add value to business through attracting and retaining employees?

This changing social context is why so many people rely so heavily on investments in order to survive.

In Table 1, below, we can see how this has played out in the public sphere. The amount of RRSPs collected by Canadians in real dollars has increased in a massive way over the last 25 years. And these are not corporate pension plans; these are the funds of Canadians being put aside in order to manage their own futures.

Table 1
Pension savings combined: RRSPs collected per year (adjusted for inflation)

	1993	2003	2016
	$ thousands	$ thousands	$ thousands
Total accumulated RRSP assets	6,974,700	13,382,221	40,394,515

Source: Statistics Canada, Catalogue no. 74-507-XCB.

Even with this increase, however, Canadians, as we discussed at the beginning of this paper, are not putting aside enough. In 2016, according to Statistics Canada, only 23 per cent of people were putting money towards RRSPs, at a median rate of $3,000 per year.[8]
In Canada, non-governmental pension plans account for almost 16 times the wealth of CPP/QPP.

Financially, therefore, it could be assumed that people are relying on corporate pension funds.

But are they?

The reality faced by workers

In today's corporate climate, a pension paid out after decades of work with the same firm is no longer guaranteed. The ways in which pensions are both designed and doled out are changing significantly.

As Statistics Canada reports, "Canadian firms have responded to growing competition within industries and from abroad by reducing their wage offers for new employees, by offering temporary

[7] Ontario Ministry of Health and Long Term Care (OMHLTC). (2016). *Health Links.* Retrieved from http://www.health.gov.on.ca.
[8] Statistics Canada. (2016). Table 11-10-0044-01 Selected characteristics of tax filers with Registered Retirement Savings Plan (RRSP) contributions

jobs to a growing proportion of them and by offering less often pension plans that guarantee defined benefits at the time of retirement."[9] Not only are fewer companies offering pension plans to their employees, but they are redefining the work relationship as temporary or part-time so that, in the case that health care benefits are offered, workers are not able to access them.

This means that the pension burden on the public sector, and on individuals themselves, may increase over time.

The answer for many companies and individuals are retirement funds offered through banks and investment corporations, like RSPs. RSPs are made up of mutual funds - an amalgamation of high- to medium-risk stocks – combined with the safety net of government bonds. What does this mean for workers? That instead of a standard employment contract plus government pension providing security in retirement, families from every walk of life now have to rely on the growth and sustainability of corporate investment to take care of them at the end of their lives. In the US alone, investment in retirement mutual funds has increased 460% in the last 10 years.

In Canada, numbers aren't as high as in the US, but they have experienced a 58% higher rate of growth in net investment compared to CPP/QPP in the last ten years. Because of the downturn in population growth in Canada, CPP/QPP itself is invested in corporations: 56.6% of the CPP reserve fund is invested in publicly-traded stocks, and 12.7% is invested in governmental corporate developments like real estate.

At the same time, many companies are aiming to make the process easier by situating pensions in stock options or company equity programs rather than in true pensions. It is estimated that approximately twenty percent of the U.S. labor force (22 million employees) participate in over 400,000 workplace profit-sharing plans and that the number of profit-sharing pension plans has increased by 19,000 per year since 1970.[10] Nonetheless, despite the fact that more conservative mutual fund-based pension strategies require substantially higher contribution rates for workers, therefore limiting their investment options outside of their companies, equity-based strategies are much more risky over the long term for workers themselves.

Let's take a look at a case study that may help to clarify this situation, and to illustrate some of the challenges of changing economic influences including shifts in demographics and illustrate why pension management is a key component of a company's human resource policies.

Attempting to merge several disparate collective pension agreements into a single long-term contract left Telus workers without a definitive contract for over four years while the details were hammered out between management and Telecommunications Worker union representatives. In

---

[9] Morissette, R. & Johnson, A. (2005). *Are Good Jobs Disappearing in Canada?* Business and Labour Market Analysis Division, Statistics Canada.

[10] Bebchuk, L.A. & Fried, J.M. (2014). *Pay without Performance: The Unfulfilled Promise of Executive Compensation*. UC Berkeley: Boalt Hall.

2005, 13,500 Telus workers in British Columbia and Alberta began job action to protest pension management standards in the merger between Telus and BCTel, but were not able to return to work until October 23 of that year. In the interim, Telus not only engaged more than 5000 management employees in front-line work replacing union staff, but 50 per cent of union staff in Alberta crossed the picket lines. This ended up costing the company a significant amount of money as processes were shifted over a number of years to accommodate union action. Part of the reason for this dichotomy of response was that employees in BC retained their existing BCTel pensions, which overlapped BCTel's acquisition by Telus; these workers were unwilling to negotiate the same deal as Alberta workers. The challenge was enormous: both the company and the union had to mitigate and merge the Telus and BCTel pensions contracts, along with employee and management expectations, in order to create a new comprehensive deal. This case study shows that the result of concerns over the viability of pensions can actually derail company operations if not managed correctly.

This example is a simple one, but what it illustrates is that there is a fundamental disconnect between the way that companies think and the impact on workers.

The bigger picture: Global trends for retirement

There are many global externalities that may have an effect on the development and management of funds. Because more and more corporations are putting the onus on their employees to participate in choosing and managing the mutual funds that now make up the majority of their pensions, this must be taken into account on an ethical level. As pension researchers Mitchell and Utkus have written, "underlying this global movement spurring participant choice is an implicit assumption about behaviour: that the employee-citizen to whom the responsibility of choice has been handed is a well-informed economic agent who acts rationally to maximize his self-interest."[11]

But this idealized situation is not necessarily a reflection of reality. Global changes towards neoliberalism do not reflect the real way that people make decisions.

Most individuals make decisions based on emotions rather than on rational thought, which means that the retirement options being offered right now are not necessarily the panacea they are thought to be. As Mitchell and Utkus explain, overconfidence in their own financial planning abilities means that many people believe they can live well on relatively small asset pools during retirement, yet after leaving work, they then find they run out of money, sometimes within a few months of retirement. If human decision-making regarding financial planning is flawed, then less risky investment choices may be more ethical components of a well-developed pension program.

A broad Pension Research Council study also points out that the difference is linked to the fact that some types of market organization are more cost-effective than others, in terms of converting

[11] Mitchell, O. & Utkus, S. (2013). *Lessons from Behavioral Finance for Retirement Plan Design*. PRC WP 2013-6. Philadelphia PA: Pension Research Council, University of Pennsylvania.

retirement saving into retirement assets and therefore there are significant challenges that may go unnoticed.[12]

The end result for workers

Today's corporations are taking on more than just the role of inventor, or manufacturer, or employer: they are subsuming yesterday's government and by providing retirement support for most Canadians, even yesterday's family. In doing so, government and corporate interests seem to intersect positively when it comes to providing retirement security for Canadians because the risks of investment are absorbed by corporations and not tax revenue.

But the reality is that this may not be the case. Workers may be more at risk than ever before.

The reality of poverty in Canada today is that much of it is hidden. We live in a country known for its prosperity and social support systems, so there is a great deal of assumption about the level of poverty in Canada; most people believe that it is much lower than it actually is. The difficulty in this is that, when there is such a widespread assumption that people have access to assistance and are not comparatively poor, many people, and even communities, become invisible and their basic needs are not met. There are pockets of endemic poverty in many areas of the country, and among certain sociodemographic groups, that are left unchecked by society, policy makers and leaders.

In fact, Canada has one of the highest poverty rates in the world among countries in the developed world. The reality is, however, that one in six Canadians fall under the poverty line, which is a much higher level than expected and most of this risk is linked to the challenges faced by the elderly poor who do not have the savings they need to retire securely.[13]

Existing policies are related to the form of Canada's welfare state because they are a legacy that was created at the very start of our nation, rather than reflecting our current reality. The welfare state was designed to serve what was known as the deserving poor, namely people who are too old or young to work, the disabled and infirm. At the same time, the way in which poverty has been measured has changed over time, and at present there is contention as to what level of income represents poverty and so many people end up slipping through the cracks.

Without a good income at retirement, the elderly may be subject to food and housing insecurity and barriers to social support systems, both those created through policies and those that arise naturally in a community, such as friendships, partnerships and collegial support systems. What this means is that these individuals may face not only endemic economic barriers, but also barriers to their personal security and health over the long term.

---

[12] Bateman, H. & Mitchell, O. (2002). *New Evidence on Pension Plan Design and Administrative Expenses.* PRC WP 2002-10. Philadelphia PA: Pension Research Council, University of Pennsylvania.
[13] Raphael, D. (2011). *Poverty in Canada: Implications for Health and Quality of Life*. 2nd Edition. Toronto: Canadian Scholars' Press.

This is going to cost Canada more, if these fundamental barriers to retirement success are not addressed.

And, perhaps unexpectedly, it's also going to create risk for corporations.

Pension plans must be created in consideration of both immediate and potential future externalities such as government regulations, macroeconomic shifts, as well as local and international accounting practices. Companies looking to create a viable pension plan need to develop the means to integrate new knowledge and external shifts over time so that the pension is not negatively affected over the long term. This means that pension managers need to not only understand the development of the company's own finances, but also the ways in which external factors can have an effect on the sustainability of the pension plan.

What does this mean for the design, management and outlook of after-work pay? First, when we evaluate the sustainability of the pension fund, we've made certain assumptions on growth, namely that pension payments consist of 30% from contribution and 70% from investment returns. We need to be clear of what we expect to get from future returns and consider whether conventional assumptions are sustainable. Second, if we need superior productivity to generate economic output and inspire growth, we need to inspire people to be at their best in terms of productivity so that their financial future is secure.

Companies are a part of our communities and poverty will affect their long term sustainability. If we drive both workers and consumers to the lowest common denominator of pension choices, it's going to make an impact on taxation, on regulation and on employee morale.

Do we need population growth to sustain economic growth, and can our resources, as they presently stand, support the kind of growth we're used to? Today, it looks like that ultimate limit is set by our natural resources and the sustainability of our environment, but what we've seen here is a call to action when it comes to our people.

To this end, corporations and organizations must create an ethical way to introduce their employees to financial management. Because employees may be unaware of their rights and because they have been proven to be overconfident, the company must complete due diligence in ensuring that pension choices are understood by employees.

Pension management, rather than the possibility of a high return, must be in the forefront of a company's consideration.