Old School Thinking Not the Answer to Economic Growth

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The economic slump that the Western world is in will last for a generation unless and until serious changes are made. While we have been through this scenario before, this time it's different. The economy is not expanding – it's flatlining – and the conventional solutions are doing little more than placing us in survival mode.

Economic strain brings challenges, but it also provides opportunities for meaningful reform that takes into account the economic realities we are faced with today. As a specialist in economic growth theory, I have found the upheavals over the past half century to be especially compelling. Even more intriguing is where this has left us in recent years.

Since the end of the Second World War, we have experienced several major recessions in the developed world ("Economic Growth since WWII" n.d.). Throughout those times, government policy was reasonably effective in doing what had to be done to get the wheels turning. Lowering interest rates spurred consumption of big-ticket items. The combination of lower taxes and higher spending helped return us to full employment. The idea was that if you just gave the system a slight nudge, things would pretty much take care of themselves.

To put it bluntly, that model doesn't work now, and is broken beyond being fixable. Public policy has placed us in a low-economic growth box that will go on for an extended period that will be impossible to sustain.

This has profound implications for all industries; however, it is particularly acute for healthcare. From 1998 to 2008, annual spending increases averaged about 7.5%. In 2011, it was estimated to be closer to 4% (Canadian Institute for Health Information 2011). Is this because there's less of a need to spend? Of course not. It's all about ability. When the economy is stagnant, it becomes a zero-sum game – if you want to spend a dollar on healthcare, it must be at the expense of something else.

In order to understand why we are engaging in a very different discussion than at any other time in economic history, we need to look at the factors that brought us here. Let's start with some factors that weren't in play in the past recessionary rounds:

- A bloated public sector. The latest labour force survey from Statistics Canada (2012) indicated that for every single public sector employee, there were 3.1 private sector employees. Ten years ago, that ratio was 4.3:1. There is valuable work done in the public sector; however, for the most part, it doesn't generate wealth. It's much more about the distribution of it.
- An aging population. Canadians aged 65 years and older now account for approximately 15% of the population. Even 10 years ago, they represented only 12.6%. And demographics aren't working in our favour: Statistics Canada projects that by 2051, one quarter of us will be 65 years or older (Human Resources and Skills Development Canada 2012). Older people both work fewer hours and require more healthcare – in the United States, 5% of the population account for half of healthcare spending (Agency for Healthcare Research and Quality 2006)!

So what can be done? From a big-picture perspective, the only long-term solution is to adopt a pro–economic growth agenda. While some might argue this is happening today, what we are working with in reality is a pro-security agenda that is rife with bailouts and mending already broken – and unfixable – models.

The auto industry is a wonderful case in point. The political process opted to bail out the sector without recognizing the fact that the model is broken. It would have been far more productive to have allowed the companies to declare bankruptcy and reorganize, so that wages could be commensurate with the value of the process. The irony hit when GM closed a plant because it was unsustainable, proving that the public policy was badly thought through.

The education system is equally hampered by outdated processes and systems, and it is seeing productivity drop by as much as 50% or more. For example, a full-time teaching position in the community college system in the 1970s required at least 19 hours of in-class time per week. Now this is down to 12. Clearly there are some efficiency issues that need to be addressed.

The question is this: how do we create value for the economy? There are options that could turn the public sector into a competitive, lean entity; these options may seem radical, but actually make perfect sense. For example, what if jobs such as teaching were put out for tender, and decisions were made based on who would be the most competitive candidate?

Tradespersons happily do this every day, and their value is measured by their performance.

Inequities in the tax system are an equally compelling thorn in the side of progress. If you inherit money, you receive it tax free. Then you can put it in the stock market, and only half of the gains are taxed. However, if a nurse works overtime, every single dollar is taxed. How in the world does that create value for work done?

Value is also an issue when it comes to benefits such as welfare and unemployment insurance. It would be much more productive to take a page from the insurance system, where premiums escalate with risk (e.g., for smokers). The same approach could be used to determine eligibility and compensation.

I recognize the fact that these approaches go against the grain of public policy as we know it. There is no question, however, that the economic stagnation we are witnessing today is largely because that policy is moving in the wrong direction. We are tying ourselves into an ever-tighter "slow-growth knot," and citizens are becoming hapless victims.

It is clear – the numbers don't lie – that tweaking the system in small increments is not addressing the important structural issues that are consigning us to an era of slow growth. It will take a paradigm shift to get us back to the days of 3% real economic growth. HQ

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