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Productivity Gains in Canada Are Not Flowing to the Middle Class

Press Release – Ottawa, November 14, 2016

The Centre for the Study of Living Standards (CSLS) today released two reports on the distribution of the gains from productivity growth, one for Canada and one for OECD countries.

Canadian labour is more productive than ever before, but there is a pervasive sense among Canadians that the living standards of the 'middle class' have been stagnating. Over the 1976-2014 period, labour productivity in Canada grew by 1.1 per cent per year while median real hourly earnings grew by only 0.1 per cent per year.

As noted by CSLS Executive Director Andrew Sharpe, "this disconnect between rising labour productivity and stagnant earnings for the median worker likely explains the prevailing sense of middle class malaise."

This gap between labour productivity and median real hourly earnings growth can be largely explained by two factors. Rising earnings inequality, as proxied by faster growth in average wages than median wages, accounted for one half of the gap, and the declining share of labour in national income accounted for 30 per cent.

The increased income generated by labour productivity growth has not flowed to the median worker in the form of higher earnings, but rather has gone to other workers and owners of capital. The fastest real wage growth has occurred at the top and at the bottom of the earnings distribution. As observed by CSLS Chair Don Drummond, the story is a 'hollowing out of the middle' rather than 'the super-rich taking all the gains.'

The most plausible explanations for both the 'hollowing out of the middle' of the earnings distribution and the decline of labour's share of income are globalization, technological change, and institutional change.

Canada was far from alone in experiencing a significant gap between growth in productivity and median wages. Indeed, of the 11 countries for which CSLS was able to obtain comparable data for the period 1986 to 2013, Canada's gap was close to the middle with four countries having a larger gap (the United States being the worst), three having a smaller gap and three, being Spain, Norway and Ireland, experiencing faster growth in median earnings than productivity.

Over the period studied, U.S. labour productivity grew at an impressive annual pace of 1.6 per cent but real median wages barely budged. The failure of the spoils from productivity to flow to the middle class likely explains much of the angst expressed by U.S. voters during the course of the recent election. The experience should serve as a warning to governments in other countries.

The CSLS studies demonstrate that productivity growth has been beneficial to Canadian workers. Efforts should be re-doubled to improve Canada's lackluster productivity record. But the studies also show that bolstering productivity growth is not a sufficient condition for raising the economic well-being of the middle class. A multi-faceted approach will be required. Policy changes affecting income distribution can play a role. More fundamental policy change will also be needed, including identifying good job opportunities for those in the shrinking middle class and support for adapting to the ever-changing skill requirements. As noted by CSLS Chair Don Drummond, "for the sake of middle-class Canadians, we cannot repeat the past."

The reports are posted at http://www.csls.ca/reports/csls2016-15.pdf and http://www.csls.ca/reports/csls2016-16.pdf

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The Centre for the Study of Living Standards (CSLS) is a national, independent, Ottawa-based not-for-profit research organization. Its primary objective is to contribute to a better understanding of trends and determinants of productivity, living standards, and economic well-being in Canada through research.