The Longest Decade: Introduction and Overview

Keith Banting
Andrew Sharpe
France St-Hilaire

The 1990s was a long decade in Canada. It was a period of transitions and turbulence, of seismic shifts in the Canadian economy and dramatic changes in many longstanding public programs. It was also a decade in which Canadians' attitudes toward their economic future and their expectations of government seemed to evolve in new and uncharted directions.

The 1990s were years of economic contrasts. The decade began with a deep, prolonged recession marked by the highest average rate of unemployment since the 1930s, yet it ended with the return of strong economic growth. Underneath the valleys and peaks of a particularly intense economic cycle, however, the basic structure of the Canadian economy was being reshaped in powerful ways by forces felt around the world, such as trade liberalization, globalization and technological change. Many of these structural trends had roots in earlier years or decades, but their full impact became clear in the 1990s, and Canadians had to embrace new ways of thinking about their economic and social future.

The 1990s also saw major changes in public policy. Most importantly, the basic strategy guiding macroeconomic policy shifted dramatically. Monetary authorities adopted price stability as their primary objective, producing restrictive inflation targets and high interest rates compared to many other countries. Fiscal policy was also tightened sharply, as federal and provincial governments moved aggressively to eliminate longstanding deficits, mainly through deep cuts to public expenditures. In the case of the federal government, its program expenditures as a proportion of GDP fell to levels not seen since the late 1940s. In addition, important components of social policy were restructured. Although the origins of many these changes can be traced to earlier years, the pace of change accelerated over the 1990s, reshaping a range of social programs inherited from the post-war generation, especially those with direct implications for the labour market such as unemployment insurance, social assistance and child benefit programs. The Canadian social policy infrastructure at the end of the decade was markedly different from that of 1990.

As with all eras of rapid and often wrenching change, economic transitions and policy changes produced considerable turmoil in the lives of many Canadians. Indeed, for policy analysts the decade of the 1990s represents a laboratory for assessing the consequences of economic and policy changes for the structure of Canadian society. Admittedly, the changes of the 1990s and their attendant impacts are still working their way through our economic and social systems, and in a real sense the story of the 1990s is still being written. Nevertheless, a new decade and a new century provide a good vantage point from which to look back and attempt an initial assessment of one of the longest decades in recent Canadian history. This book is devoted to the task of analysing the impact of economic performance on patterns of social well-being in Canada during the 1990s.

THE TOOLS OF ANALYSIS: CONCEPTS AND LINKAGES

Before plunging into all of the controversial debates about the record of the 1990s, it is important that we establish as much clarity as possible concerning the core concepts at the heart of the study and the linkages between them.

The term "economic performance" poses the fewest difficulties. As used in this volume, the term is defined relatively narrowly as trends in key macroeconomic variables such as output growth, productivity, employment, unemployment and inflation. Economic performance can be measured in absolute terms or, more appropriately but with much greater difficulty, relative to potential. For example, an absolute slowdown in the long-term rate of economic growth that reflects slower population growth, and therefore lower potential growth in the labour force, does not really represent a deterioration of economic performance as such. However, a slowdown in actual output growth relative to potential labour-force and output growth does. Operationalizing the idea of potential growth can be complex, because gauging trend productivity growth is notoriously tricky. But the basic concepts are clear.

Good economic performance is thus defined as a situation in which output, employment and productivity grow at their potential and the unemployment rate and the rate of inflation are low. Poor economic performance is defined as a situation in which output, employment and productivity growth are below potential and unemployment and inflation are unacceptably high.

In contrast with the relative clarity of the meaning of economic performance, "social progress" is a much broader idea. Social progress can be manifested by improvements in a wide range of measures, including the incomes of families and individuals, the sense of economic security enjoyed by workers, the levels of poverty and social exclusion, the extent of inequality in life chances, the vibrancy of cultural life, the integrity of distinctive communities, the strength of social cohesion and the sustainability of our environmental heritage. Such a complex and multi-faceted phenomenon is best thought of as an overarching societal goal rather than as an analytical concept, and contributors to this volume tend to focus on specific dimensions of our collective social experience.

Any assessment of social progress is also hindered by the fact that it must move beyond aggregate measures. Overall indicators of the average level of social well-being always mask variations in the experiences of different individual and groups, and this is especially important during periods of historic transition. Economic and social change on a major scale always produces winners and losers, groups who benefit from the new order and groups whose economic and social prospects are eroded by the same forces. The history of wars, it is often observed, is written by the winning side. The history of social progress needs to be more balanced.

As well as being complex, "social progress" is inevitably a contested idea, because different people have very different conceptions of what constitutes the "good" society. Even if members of a society agree on whether specific indicators tap dimensions of social progress, they will differ on the relative importance to be attached to the various indicators and hence on whether social progress, in the aggregate, is advancing or not. For certain indicators, there may even be disagreement about which direction of change represents social progress, reflecting the ideological or world view of the observer. For example, some may see a rising proportion of students in private schools as a negative indicator because they believe such a trend threatens the development of an inclusive society. Others may view this as a positive development because it means that individuals have more choice in educational options for their children. In the end, therefore, it is unlikely that we will find consensus on a common measure of social progress or well-being. Exploring the relationships between economic performance and social progress remains a compelling task, but the judgements rendered in this volume are best seen as contributions to an open and pluralistic debate on this critical dimension of Canada's future.

Not surprisingly, perhaps, the linkages between these two phenomena — economic performance and social progress — are many and varied. In some cases, the links are direct and immediate; changes in the average income of Canadians and the level of unemployment are tightly tied to the performance of the economy and productivity trends in particular. In other cases, the links are more indirect and conditioned by other factors. For example, there is a significant lag between the performance of the "official" economy, as measured by such indicators as GDP growth and average income, and Canadians' own sense of economic security, as measured by opinion polls. Moreover, some commentators have wondered whether the link between economic growth and particular components of social well-being, like poverty for example, may have weakened over time such that the return of economic growth late in the decade did not lead to a sharp decline in poverty rates. In yet other areas, the link between changes in economic performance and certain dimensions of social progress may be especially weak. For example, there may be little or no link between economic performance and indicators of social cohesion or social capital such as membership in associations and groups. Cultural or social factors are likely to exercise much greater influence in shaping such aspects of our collective social experiences. Finally, the link between economic performance and social progress may also be negative. For example, economic growth may have a deleterious effect on certain environmental indicators such as greenhouse gas emissions or quality of life indicators such as the time spent commuting.

The role of public policy highlights the importance of the indirect linkages between economic performance and social lives of citizens. In part, the impact of economic performance on social well-being flows through public policy. To take the most obvious example, poor economic performance in the 1990s reduced government revenues and increased deficits, significantly contributing to the pressure on governments to take dramatic action on fiscal policy. The major cuts in unemployment benefits and to a lesser extent in social assistance triggered by these pressures had a palpable impact on the lives of many Canadians. Yet no simple economic determinism drove the reaction of governments. As the chapters in this volume make clear, governments were faced with a variety of options, and, inevitably, fundamentally political judgements had to be made about how to proceed. Similarly, an analysis of the evolution of social programs makes clear that a wide range of social, demographic and political factors also came into play in redefining social Canada. The performance of the economy is a powerful factor conditioning public policies, but the impact is indirect and mediated by political and social pressures.

Tracing the linkages between the economy and social well-being is also a challenge because it is *long-term* economic performance that is likely to have the most pervasive impact. The short-to-medium-term economic record, such as that of the 1990s, can have many important consequences, as we will see in greater detail in a moment. But the most significant consequences of the performance of the economy take generations to unfold. One need not adopt the extreme caution of the Chinese leader who opined that it was still too early to assess the impact of the French Revolution on the course of human history. But the consequences of economic trends do need to be measured in generations as well as decades. Modern research on the importance of early childhood development, for example, suggests that changes in the cultural richness of the family and community environment in which young children are nurtured can have long-term effects on their development as adults. The full consequences of the economic turbulence of the 1990s will therefore continue to work their way through our social and economic systems for a long time. In addition, long-term economic trends are critical because they shape and change social norms and public expectations of the future. The sustained economic growth of the post-war decades certainly contributed to the underlying optimism of the era and people's faith in the capacity of governments to act as instruments of collective choice and social progress. The more troubled economic record of the last decades of the 20th century undoubtedly played a key role in eroding that confidence.

Finally, in comparison with the short- and long-term links running from economic performance to social progress, the links running from social well-being to economic performance are less obvious and not as well documented. Nevertheless, these links are likely to be important for many economic variables. To take the most obvious example, in a knowledge-based economy, social and cultural factors that influence the desire and capacity of families to invest in their children's education and development have potentially powerful long-term consequences for productivity growth and the vibrancy of a society's economic future; changes in family structures and other social patterns that influence the capacity of families and communities to make such investments do matter. Similarly, many analysts have argued that the strength of social networks and levels of social and political trust represent a form of social capital with important implications for economic activity. For these and other reasons, there appears to be some evidence that greater social equality can boost long-term productivity and growth. In particular, inequality can have negative implications for the accumulation of human capital. Those at or near the bottom of the income distribution in an unequal society may have much more financial difficulty providing opportunities for post-secondary education for their children than a comparable group in a more equal society.[1]

The links between economic performance and social progress are thus multiple and complex, and tracking the relationships in a comprehensive way is a challenging analytical task. Nevertheless, it is possible to make at least provisional judgements about the core dynamics at work. What follows is a broad assessment of these patterns as manifested in the economic and social record of the 1990s.

ECONOMIC PERFORMANCE AND SOCIAL PROGRESS IN THE 1990s: THE BROAD PATTERNS

There is wide agreement that Canada's economic performance in the 1990s was, on average, poor, particularly relative to earlier decades. Growth in total output, employment and output per capita were considerably slower than in earlier periods. This slowdown reflected a gap between actual and potential performance, but not a drop in potential. The tragedy of the decade was the unemployment rate, which reached levels unseen in half a century. The only key economic variable that produced positive results (as traditionally defined) was inflation, which was very low. As noted at the outset, economic performance varied greatly within the decade. The economy went into a deep and protracted recession, with declining or weak output and employment growth along with rising or high unemployment, in the seven-year period from the 1989 cyclical peak to 1996. This was followed by robust output and employment growth and falling unemployment in the four-year period from 1996 to 2000. However, measures of the average performance of the economy are influenced more by the first period than by the second. Overall, the 1990s were a tough decade for Canada.

Following a trend started in the 1980s, the policy climate in Canada in the 1990s became more market-oriented and less reliant on state intervention, a development common to most if not all OECD countries. Macroeconomic policy was dominated by the themes of price stability and deficit elimination. The quest for liberalization drove policy developments in the trade and investment area, predominately the Free Trade Agreement (FTA) in 1989 and the North American Free Trade Agreement (NAFTA) in 1994. As noted earlier, program spending as a share of GDP was drastically cut in the mid-1990s and continued to fall in the late 1990s even though surpluses emerged. Labour market policy saw a shift in emphasis from passive or income-support policies (Unemployment/ Employment Insurance and welfare) toward more active policies fostering the integration of the jobless into the workforce. The trend away from universality in income security programs accelerated in the 1990s as income transfers were increasingly targeted to the poor and middle-income groups. Governments continued the privatization and deregulation trend started in the 1980s. Unlike the case for earlier decades, it is difficult to point to any major program initiatives by federal or provincial governments (partial exceptions may be child benefits, the Millennium Fund and spending increases in programs for Aboriginals).

What, then, of social progress? The aggregate measures tell one story. The average incomes of Canadians, however measured, eroded during the 1990s. For example, real personal disposable income per capita peaked in 1989, declined steadily through the first half of the decade and had not yet fully recovered by the year 2000 (Sharpe 2001). The decade also saw a growing gap in the standard of living between Canada and the United States, where productivity growth was considerably stronger throughout much of the decade. Aggregate measures of economic security capture another dimension of what was a tough decade for Canadians. As we shall see, the overall level of economic security enjoyed by Canadians declined during the 1990s, driven by increases in the risk of unemployment, the risk of financial insecurity due to illness and the risk of single-parent poverty.

Income inequality also increased in Canada in the 1990s. Turbulence and change in the economy contributed to greater polarization in labour-market outcomes. Based on trends in the Gini coefficient, a common measure of income distribution, inequality of market income for economic families (of two or more) rose 10.4 percent from 1989 to 1998, the most recent year for which data are available (Statistics Canada 2000). Moreover, the traditional role of the State in offsetting growing inequalities in market income diminished as the decade proceeded. Overall, the Gini coefficient for after-tax income rose somewhat less than that for market income (7.9 percent). In the first half of the decade, the tax and transfer system (particularly the latter) did work to offset the rise of market income inequality and keep after-tax income inequality relatively stable. But after 1995 this offsetting effect was weakened as cuts to social programs (the 1995 reductions in social assistance benefits in Ontario and the 1996 reform to Employment Insurance stand out as the most important) significantly weakened parts of the social safety net.

These economic and social policy trends inevitably had implications for poverty in terms of incidence, depth and persistence. There is no official measure of poverty in Canada. However, Statistics Canada does produce estimates of the proportion of the population living below what it calls low-income cut-offs (LICOs), and a number of non-governmental organizations refer to these estimates as the poverty rates. By this measure, the incidence of poverty rose in the 1990s. The proportion of Canadian economic families living below Statistics Canada's LICOs increased from 7.7 percent in 1989 to a peak of 10.2 percent in 1993, and had fallen to only 9.1 percent by 1998, the most recent year for which data are available (Statistics Canada 2000). Moreover, the average income gap, defined as the gap between the LICO and the average income of a family living below the LICO, rose 12.0 percent, from \$5,928 to \$6,638 (\$1998), between 1989 and 1998.

Probing beneath these aggregate trends reveals a more complex pattern of winners and losers in the 1990s. Some groups did very well in the decade while others did quite poorly. As a general rule, persons with post-secondary education, older workers, women and workers in industries with expanding exports benefited from the changes in the economic environment, while the poorly educated, younger workers, men and workers in industries with expanding imports suffered real setbacks. Although these divergent outcomes in part reflect the relative degree of preparedness of these groups to adapt to the turbulent changes that beset the 1990s, the causes of some of these labour market trends are not yet fully understood.

Overall, the 1990s was a tough decade in social as well as economic terms. Canada seemed to be headed toward a more unequal society. However, some observers argue that the overall level of inequality in Canada is not the main concern as long as Canadians maintain a strong commitment to equality of opportunity. Historically, Canada has been characterized by a relatively high degree of intergenerational mobility, ranking alongside the most mobile countries such as Sweden and Finland. This pattern of increased intergenerational mobility over past decades was undoubtedly underpinned to a significant degree by the dramatic postwar expansion of educational systems, especially post-secondary education, and the strong public financing that drove that expansion. We still do not know the extent to which the policy changes of the 1990s, which increasingly shifted the costs of post-secondary education from public to private shoulders, changed that pattern and began to reduce the life chances of children from less affluent families. However, the early warning signs are not encouraging (Bouchard and Zao 2000). These signals simply reinforce the conclusion that the legacy of the adjustments and turbulence of Canada's longest decade will continue to unfold for years to come, and that the interim report contained in the pages of this volume will need to be updated on a continuing basis.

DETAILED VIEWS: THE CHAPTERS IN THIS VOLUME

The chapters in this volume, written by leading experts in the field, provide more detailed views of specific dimensions of the economic and social developments of the 1990s. The chapters are organized into four sections dealing with basic concepts, the public view of economic and social trends, changes in key public policies, and the outcomes in terms of the economic, social and environmental record of the 1990s. This section provides a brief summary of each chapter.

Concepts, Measurement and Linkages

The first chapter in this section, by Lars Osberg of Dalhousie University, discusses the concept of social progress and reviews a number of measures of social progress. The second chapter, by John Helliwell of the University of British Columbia, examines the linkages between social capital and the economy and well-being.

Lars Osberg was given the daunting task of examining the conceptual issues involved in defining and measuring social progress as well as reviewing the indicators currently available. As the author points out in his introduction, while much was made of the fact that Canada yet again earned first place in the United Nations' Human Development Index last year, other indices have produced less stellar results. He cites, for example, our 31st-place ranking based on the Weighted Index of Social Progress (WISP). Osberg's point is that there exists a wide range of similar indices, and each is based on a different set of criteria reflecting its own underlying choice and ranking of goals and priorities. Thus to agree on a measure of social progress presumes some prior conception of "good" outcomes and some way of knowing whether society is progressing overall in that direction.

Modern pluralist societies, however, have no common benchmark for defining the "good" society. Therefore, Osberg argues, social progress in a liberal society must be measured in the "enabling" sense that a society progresses when it enables more of its citizens to achieve the kind of life they personally value. Moreover, he insists on the need to draw a distinction between *needs* and *wants* and to think of progress in terms of "first meeting needs and then satisfying wants." His central argument is that if individuals are to choose freely what they want, their basic human rights need to be met. Canadian society has already committed itself to a definition of such rights in signing and ratifying a series of international covenants such as the United Nations Universal Declaration of Human Rights (1948) and the International Covenant on Economic, Social and Cultural Rights (1966). One measure of social progress in Canada would therefore be the percentage of Canadians who actually now enjoy these basic human rights. Using the right to housing as an example, Osberg also emphasises the fact that human rights covenants explicitly recognize the interdependence of social, economic, legal and political rights. The chapter goes on to discuss some of the empirical difficulties involved in constructing a measure of the attainment of social and economic rights, and it reviews several quantitative indices of social progress through the prism of human rights. The author concludes by highlighting the problems associated with data based on aggregate measures (e.g., population means or totals), which cannot reveal the particular circumstances of minorities. He also warns of the dangers of excessive complexity in data processing, which can at times obscure the link to human rights.

In the second chapter in this section, John Helliwell provides an up-to-date and comprehensive survey of the literature on the impact of social capital on both the economy and well-being. He begins by defining social capital as the networks and norms that facilitate cooperative activities within groups (bonding social capital) and between groups (bridging social capital). Researchers have found that high levels of interpersonal trust make many aspects of life more enjoyable and more productive by reducing the costs of dealing with risk and uncertainty. He points out that the direct linkages running from social capital to well-being are better documented than indirect linkages running from social capital to better economic performance and then to greater well-being. He also notes that it is important to disentangle what social capital is from what it does. Trust and the effectiveness of institutions may be better thought of as consequences of social capital than as part of social capital narrowly defined.

Helliwell surveys a number of studies that show that social capital actually saves lives. The denser the social network to which one belongs, the better the health outcomes, with the causation running from the former to the latter. Education levels have been found to be the most consistent factor in explaining differences in connectedness and trust, which, according to Helliwell, is a powerful result that broadens the total returns to investment in education. The author also surveys the literature on subjective well-being, pointing out that unemployment lowers subjective well-being by more than the usual measure of economic cost and certainly more than inflation. This implies that estimates of the trade-off between inflation and unemployment should attach substantially more weight to unemployment than that implied by the "misery index" which treats as equivalent a one-percentage point increase in the rate of inflation and a one-percentage point increase in the unemployment rate.[2]

A key issue in the debate on well-being is whether it is absolute or relative values for income, education and social capital that influence happiness or well-being. According to Helliwell, the literature concludes that the happiness effect of higher income is based on relative rather than absolute income. In contrast, it is absolute levels of education and social capital that influence well-being. He argues that one interpretation of these results is that education and social capital have positive externalities while income has negative externalities. That is to say, the overall population gains from contact with the more educated and civic-minded. In contrast, when others have higher income it exposes the inferiority of one's own income and reduces subjective well-being.

Public Views of Economic Performance and Social Progress

The second section of the volume turns to the public's view of the experience of the 1990s. Frank Graves, of Ekos Research Associates, examines the relationship between what he describes as the "official economy," as portrayed by conventional measures of economic performance, and public perceptions of the state of the economy. He also considers the public's understanding of the relationship between economic and social well-being, and the linkages between the public's perception of economic performance and their attitudes toward the redistributive role of the State and its broader role as an instrument of social progress. The analysis in this chapter is based on data from quantitative surveys and evidence from qualitative focus groups conducted over the past decade.

One of Graves' main arguments is that although there is a strong relationship between the perceived and official economy, the relationship is lagged and imperfect. As the author points out, this was particularly the case in the mid-1990s when the economy was perceived not only as considerably more turbulent than it was, but also as failing to recover at a time when the official data on economic growth indicated a turnaround. While public perceptions are highly segmented on the basis of region and socio-economic status, Graves also provides a number of other explanations for the imperfect nature of the relationship. For instance, he finds that people's perceptions about the state of the Canadian economy are very much based on their personal experience, which does not necessarily correspond with macroeconomic indicators. In addition, the experience of the mid-1990s clearly shows that once feelings of economic insecurity and anxiety toward the future take hold, they are more difficult to reverse than feelings of confidence. Indeed, it was only after a sustained period of strong performance in the Canadian economy and solid evidence of improvement in the state of public finances that indices of public insecurity and confidence levels moved in the expected direction.

By the end of the decade, not only had Canadians finally caught up with the data, but they had also changed their outlook on the economy. In particular, Graves detects a significant shift in attitudes on the part of Canadians toward globalization, technology and trade liberalization, and greater acceptance of the changes these forces entail. Yet at the same time they are increasingly concerned by what they perceive as rising poverty levels and growing inequality.

According to the author, Canadians understand and explicitly rank social and economic well-being considerations. Most people see "social well-being," which they equate with the notion of overall quality of life, as the ultimate goal. Graves also reports a growing tendency to explicitly link economic and social well-being and a desire to find ways to reconcile the two. Based on these observations, it is not surprising to find that public expectations and attitudes toward the role of government have also undergone important adjustments. Graves argues that economic performance clearly influences attitudes toward redistribution but that the linkage is different at the individual and aggregate/macro levels. At the individual level, those with high incomes will tend to place less emphasis on redistribution. At the collective level, however, Canadians have shown rising support for "conditional government activism" to address issues of social well-being as the economy has strengthened and perceptions of "needs" in specific policy areas such as health care have emerged. Looking at public opinion trends on the role of government and its priorities, Graves foresees the emergence of what he calls a new "humanomic" approach that is "redefining the relationship between economic and social policy as components of an overall plan to increase opportunity and reduce economic risk."

Public Policy, Economic Performance and Social Progress

The next set of chapters explores the impact of changes in public policy on economic performance and social well-being during the 1990s. The editors identified three policy areas as particularly important in shaping social progress in the 1990s: macroeconomic policy, trade policy and social policy. We invited individuals who were either players in these policy decisions or were persons deeply engaged in the attendant public debate to contribute chapters to this section. Four chapters examine the broad patterns of macroeconomic policy, while two others are devoted to trade policy and social policy, with particular reference to income security.

Macroeconomic policy. Monetary and fiscal policy were at the heart of the public policy debate in this country in the 1990s. Indeed, policy decisions in these areas affecting the state of the economy and the allocation of government resources had a profound impact on all aspects of Canadian society and provoked intense controversy. The four chapters on this general topic, two on monetary policy and two on fiscal policy, provide quite different perspectives from authors who are veterans of macroeconomic policy debates. Two are contributed by senior economic policy-makers and two by well-known critics of macroeconomic policy.

In the first chapter on monetary policy, Paul Jenkins and Brian O'Reilly of the Bank of Canada survey monetary policy developments in the 1990s, focusing on links between monetary policy and the economic well-being of Canadians. In the second, Pierre Fortin of the Université du Québec à Montréal provides a critique of the conduct of Canadian monetary policy in the 1990s, a critique that he developed throughout the decade. In the first chapter on fiscal policy, Don Drummond, who was until recently a senior official in the federal Department of Finance with responsibility for budget coordination, gives his perspective on fiscal developments in the 1990s. This is followed by a chapter by Jim Stanford of the Canadian Auto Workers (CAW), who has a different take on this topic.

Macroeconomic trends and policy developments in the 1990s are well known and the basic facts are not in dispute. In the late 1980s, under the leadership of John Crow, the Bank of Canada adopted price stability as its primary objective. This policy was formalized in February 1991 with the announcement of a Bank of Canada-Department of Finance agreement on inflation targets. With the tightening of labour markets in the late 1980s and early 1990s, a restrictive monetary policy was adopted to dampen incipient inflationary pressures. Short-term interest rates surged and at one point were 4 percentage points above comparable rates in the United States. Inflation was duly subdued, but economic growth slumped and failed to revive. From 1989 to 1993, real GDP growth averaged 0.4 percent per year; it was by far the weakest four-year period of economic growth since the Great Depression.

The stagnant economy and high interest rates had very negative effects on government fiscal balances. Governments eventually reacted to their burgeoning deficits by cutting program spending and to a lesser degree raising taxes. According to OECD measures, Canada pursued the most restrictive fiscal policies among all OECD countries in the mid-1990s. This action in turn reduced growth and the economy continued to perform well below potential. Finally, starting in 1997 the worst of the government cuts had been absorbed, interest rates declined and the American economy went into high gear. Canada now entered a period of rapid growth that reversed much of the decline experienced in the first half of the decade. The unemployment rate fell dramatically, the gap between actual and potential growth was reduced if not eliminated, and budget surpluses emerged.

The key issues in the debate on macroeconomic policy are the following:

- To what degree was the recession of the early 1990s exclusively due to monetary policy as opposed to other factors such as restructuring of the economy?
- Did the federal government overreact to the fiscal situation and pursue an unnecessarily harsh fiscal policy to the detriment of the economic well-being of Canadians?
- To what degree was the economic boom starting in 1997 a direct result of the monetary and fiscal policies pursued in the first half of the decade, with low inflation and falling deficits essential preconditions to interest rate reductions, and enhanced business and consumer confidence?

The four chapters in the section offer different answers to these questions. In reference to the first question, the Bank of Canada economists do admit that tight monetary policy in the early 1990s hurt growth in the short term, but they argue that such action was necessary to ratchet down entrenched inflationary expectations. Moreover, they argue that stagnation in the early part of the decade was not simply the result of monetary policy, but also reflected a weak US economy and structural problems in the Canadian economy. Pierre Fortin offers a very different view. While not denying that the US economic slowdown in the early 1990s reduced growth in Canada, he lays the blame for the inferior economic performance of the Canadian economy relative to the US economy squarely on the Bank of Canada, and dismisses structural explanations of the recession as lacking an empirical basis.

In response to the second question, Don Drummond makes the case that, given the context at the time, the fiscal policy implemented in the mid-1990s was justified. With large deficits, there was little room for the Bank of Canada to reduce interest rates to stimulate the economy and generate revenues. It was imperative that the deficit be eliminated. Tax rates were already high, so the government had no choice but to cut program spending. Drummond recognizes that the cuts caused hardship for some Canadians, but feels that the suffering was relatively limited and temporary in nature. Jim Stanford agrees with Drummond that measures were needed to eliminate the deficit, but he argues that the federal government's spending cuts were larger than necessary and caused real pain in many areas of Canadian life. He shows that a strategy in which program spending is frozen in nominal terms, but not cut, would have produced more growth and employment and still yielded almost the same deficit by 1999 (although with slightly higher debt levels) as the program-cutting path actually followed.

Probably the most controversial of the three questions is the third one. The Bank of Canada makes the case that although establishing a low-inflation environment generated short-term pain in the early 1990s, it is now paying off with long-term gain. According to the Bank, price stability has enhanced economic well-being. Low inflation has reduced inflation uncertainty, a boon to investment. Don Drummond argues that the elimination of the deficit has reduced risk premiums and allowed the Bank of Canada to bring interest rates down.

Both Fortin and Stanford give less credit to monetary and fiscal policies adopted in the first half of the decade for the economic renaissance of the second half. They note that over the decade economic growth was very weak and that four good years cannot offset the negative effect of six poor years. Both authors agree that the conduct of monetary policy has become more conducive to growth in recent years and point to the willingness of the Bank of Canada to allow the dollar to fall as a positive development. But they both argue that the virtues of price stability have been oversold and that a less rigid approach to monetary policy, such as the strategy practised so successfully by Alan Greenspan, would be more productive.

Trade policy. Daniel Schwanen of the Institute for Research on Public Policy addresses the impact of the major trade liberalization efforts undertaken by Canada and its trading partners beginning with the Canada-US Free Trade Agreement in 1989. The author focuses in particular on the question of whether liberalized trade could have been a factor behind the emergence of greater inequalities in Canada in the 1990s. He begins by reviewing some theoretical links between trade and inequality, and notes that trade can affect the relative position of unskilled workers not only through "factor price equalization" — for example, competition of unskilled Canadian workers with lower-paid workers in other countries — but also because trade fosters scale and innovation.

These last two phenomena, in turn, tend to favour skilled over less-skilled workers.

The author divides Canadian manufacturing industries into five groups according to their sensitivity to trade liberalization in the 1990s and to the direction taken by exports and imports following the opening of trade. He finds that workers in export-oriented manufacturing industries did markedly better than others during the period in terms of employment and earnings, while workers in industries characterized by high levels of imports, who were less educated and already earning less on average before the FTA, did poorly. Schwanen notes that trade liberalization is more likely to have affected services indirectly than directly, through the inputs that services provide to manufacturing. Accordingly, he divides service industries into those that are highly sensitive to two-way trade and those that are not. He finds that employees in trade-sensitive service industries, who were already earning higher wages and were more highly educated than the Canadian average, experienced a greater rise in their employment and earnings relative to workers in other service industries. At the same time, workers in the least trade-sensitive service industries (many in the public sector) who were also highly educated, and who comprised a high proportion of youth, experienced relatively poor outcomes.

Schwanen concludes from this exercise that more open trade may have contributed to inequalities in Canada by favouring certain groups already doing relatively well while being detrimental to many less-skilled and lesser-paid groups. Furthermore, he notes that liberalized trade may help explain the fact that increases in inequality have also been observed *within* groups of workers with equivalent education and experience. This is because groups of industries employing workers with similar characteristics nevertheless performed differently, depending on their exposure to trade liberalization.

Social policy. Perhaps one of the most highly charged public debate in this country over the past decade has been that concerning the dismantling of the "universalist" model of the "welfare state" adopted in the post-war years. In his chapter, Ken Battle of the Caledon Institute of Social Policy is critical of the ongoing public discourse on this issue, which he considers lacking in both substance and subtlety. He argues that this has led to a polarization of views and produced persistent mythologies, which have insulated governments from effective criticism and inhibited an open and informed public debate on the present and future course of social policy. As one of the country's leading experts on social policy, Battle is well placed to provide a comprehensive analysis of the major developments in income security policy in Canada since the mid-1980s. He documents the changes in approaches and instruments, identifies the forces propelling these changes, and assesses the outcomes relative to the broad principles and objectives of social policy.

The first section of the chapter charts the trends in major income security expenditures since 1980. On the whole, income security expenditures in the 1990s show a relatively small downward trend in both absolute and relative terms, although provincial spending fell more sharply (13.2 percent in real terms between 1993-94 and 1998-99) than federal spending (3.8 percent over the same period). But underlying this modest trend are important differences in individual programs. While income support programs for politically favoured groups such as the elderly continued to grow, unemployment insurance and social assistance expenditures moved up and down erratically as a result of both economic turmoil and changes in benefits and eligibility requirements imposed by cash-strapped governments.

According to Battle, the pressures to reform Canada's social programs stem from a variety of profound changes that extend well beyond the economic realm. He argues that the shift away from a universalist model of the welfare state is not a 1990s phenomenon, but one that can be traced back to the late 1970s and is still under way. Battle goes on to describe how social, demographic, political and ideological forces, often interacting with economic factors, are setting the course in the ongoing transformation of Canadian social policy. In his view, the series of changes and reforms implemented in the policies and programs related to income security over the last two decades reflect the emergence of a new conceptual framework which he describes as the "post-welfare state" model. This new model, as he defines it, retains the fundamental objectives of social policy but seeks new approaches and mechanisms related to financial sustainability, efficiency and effectiveness in order to adapt the old model to the changing economic, social and political realities of the new century.

Battle also makes clear that, while economic concerns have always been an aspect of social policy, they are "front and centre" in the post-welfare state. He identifies several key characteristics of this new approach to social policy, emphasising: (1) the replacement of universal social programs and needs-tested income security programs with broad-based and progressive income-testing, (2) a greater concern for the work-disincentive effects of social programs such as the effects of clawback provisions for social benefits and the welfare wall, (3) a greater integration of social programs and the tax system, (4) efforts to find a balance between "passive" and "active" social programs such as training or various preventive measures, and (5) attempts to measure the outcomes of social policy and provide greater accountability.

The chapter goes on to describe the major changes to social benefits and the extent of program coverage. The limits that were imposed, both directly through tightened eligibility requirements (e.g., Employment Insurance and social assistance) and indirectly through the partial de-indexation of various benefits (e.g., earnings supplements, the Child Tax Benefit) and tax credits (e.g., the GST and other refundable tax credits), have considerably reduced the size of the qualifying population relative to what it would have been.

However, Battle places the most emphasis on the changes to several income security programs that could be considered universal in the sense of not imposing income-based qualifying conditions and which over years have been reformed in that direction (e.g., Old Age Security and child benefits). He considers the displacement of demogrants (available to all) and needs-tested benefits by income-tested benefits delivered through the income tax system to be the most important advance in contemporary Canadian social policy. In addressing some of the criticisms of this approach, he argues that the large majority of families with children and seniors still receive benefits and that the changes have resulted in greater vertical equity overall. Battle also stresses the importance of the National Child Benefit in removing children from social assistance caseloads, which he considers "a major step forward in the essential task of dismantling social assistance and replacing it with more effective programs."

Battle describes the general process of reform and developments in social policy in the last two decades as one of "relentless incrementalism" where cumulative, purposeful and patterned change has produced a substantial shift in the structure of the Canadian income security system. He argues that this shift has occurred partly by stealth but also because Canadians had come to accept the need to deal with the chronic problems of public finances and were receptive to the criticisms directed at major social programs. The author concludes that in the end the emerging post-welfare state will better serve Canada's evolving social, economic and political needs. In particular, he sees little cause for continuing nostalgia over the fading universalist welfare state, which in his estimation never worked all that well.

The Outcomes: Canada's Economic, Social and Environmental Record

The final section of the volume turns more directly to the economic, social and environmental outcomes of the 1990s in Canada. The first chapter examines trends over the decade in various components of economic well-being. The second chapter provides a comprehensive overview of distributional changes during that period and the third chapter looks at long-term trends in intergenerational mobility. The final chapter analyses the relationship between economic growth and environmental degradation.

Lars Osberg of Dalhousie University and Andrew Sharpe of the Centre for the Study of Living Standards provide an overview of trends in a number of dimensions of economic well-being (consumption flows, stocks of wealth, income equality and economic security). They assess these trends through the lens of the Index of Economic Well-Being, a new composite measure developed by the Centre for the Study of Living Standards. In modern democracies, the authors point out, national systems of social and economic statistics have become a crucial part of the informational feedback loop of public policy. Through measures of social and economic outcomes, statistical agencies provide decision-makers and voters with the information that often defines the success or failure of public policies. The motivation for the development of the Index is the belief that current measures — such as trends in per capita income — may not necessarily be a good guide to popular perceptions of trends in economic well-being.

The main findings of the article are that after registering increases in the 1970s and 1980s, the Index declined in absolute terms in the 1990s. This development was largely driven by the fall in the economic security component of the Index. Two of the four subcomponents of economic security experienced significant declines. The risk from unemployment increased dramatically, reflecting the falling employment rate and, more importantly, the decline in the share of the unemployed covered by Unemployment Insurance (renamed Employment Insurance in 1996). The risk to financial security from illness, as proxied by the proportion of disposable income devoted to medical expenses, rose considerably, in part due to delisting of a number of medical services and higher drug prices. A decline in the equality component of the Index also contributed to the overall decline. In contrast, both the consumption and wealth stocks components increased, although at a slower pace than in earlier periods.

The time path of the Index was not one of continuous decline over the decade. Rather, the Index fell steadily from 1989 throughout the first half of the 1990s, hitting a trough in 1996. Since then, the Index has been on an upward trend.

Osberg and Sharpe point out that the determinants of the nearly 20 variables that make up the Index are complex. Certain variables have been strongly influenced by poor economic performance in Canada in the 1990s, some have been moderately influenced and, finally, some are largely independent of current economic performance in Canada (but not necessarily economic performance in other countries), because they are driven by either longer-run social trends or discretionary policy choices. But, overall, the authors conclude that there has been a direct link between the deterioration of economic performance in this country in the 1990s and the overall state of economic well-being.

The following chapter examines trends in earnings and income inequality in Canada. Andrew Heisz of Statistics Canada, Andrew Jackson of the Canadian Council on Social Development and Garnett Picot of Statistics Canada provide a comprehensive analysis of the distributional changes that have occurred in the 1990s as well as useful comparative perspectives in terms of both trends over time and the situation here relative to that in the United States. This exercise is all the more important given the significant changes and developments that have taken place in the labour market and the economy at large over the last decade. Indeed, there has been growing concern over the repercussions of these changes on Canadian society and the perception of increased polarization and a growing gap between the haves and the have-nots.

The story is a complex one that depends on which definition of income is used and whether the focus is on individuals or families. And, as this chapter shows, it also requires a thorough examination of the shifts beneath aggregate trends. In other words, the real story is to a great extent buried in the subtext. The authors focus on four aspects of distribution outcomes: (1) earnings and income inequality, (2) the relative earnings of the young and old and the more and less educated, (3) the changing relative position of men and women, and (4) changes in low-income trends in Canada during the 1990s.

Looking at long-term aggregate trends, the data indicate that earnings inequality, which had risen significantly in Canada between the 1970s and the 1980s, increased only modestly during the 1990s. Earnings inequality among men increased to a lesser extent in the 1990s than it had in the two previous decades, and even improved slightly between 1997 and 1998, while the changes among women were more muted. When earnings are aggregated at the family level, however, inequality is seen as continuing to rise in the 1990s. According to the authors, the difference between individual and family earnings is directly related to changes in marriage and family formation patterns and, in particular, the growing numbers of single-parent families and an increasing tendency for high earners to marry high earners and low earners to marry low earners.

The measure of inequality in family disposable income is of particular relevance to policy-makers as it reflects the distribution of total monetary income from all sources, including pensions, social transfers and investment income, and also takes into account personal income taxes. Interestingly, there appears to have been little change in this measure of inequality over the past 30 years. According to the authors, the earnings losses among low-income families throughout this period (and especially in the 1980s) were largely offset by increases in social transfer payments. Although data for recent years do suggest that some increase in disposable income inequality may have taken place, it is not yet clear whether this is related to cutbacks in some social programs in the 1990s or to changes in data collection methods over this period.

Of course, the apparent stability in some of the aggregate measures of inequality over the last decade masks important shifts and offsetting changes in the relative wages of various groups as well as within groups. For instance, the authors point to a widening earnings gap between younger and older male workers in the 1980s and 1990s, mainly as a result of the fall in the real earnings of young male workers (under 35). As the chapter suggests, the causes of this deterioration remain somewhat of a puzzle and even raise questions about the skill-biased technological change hypothesis and the resulting demand for skilled labour as a primary driving force behind the recent changes in the labour market outcomes of Canadian workers. For instance, there appears to have been no significant change in relative wages or employment rates among more highly educated workers as a whole in Canada throughout the 1980s and up to the mid-1990s. In fact, the situation was more one of deteriorating outcomes for the least educated. The latest data from the Labour Force Survey, however, do indicate that the earnings of young university-educated workers have increased in recent years, both in real terms and relative to the less educated.

The real success story in Heisz, Jackson and Picot's account of distributional outcomes over the past two decades is the dramatic improvement in the labour market position of women relative to men. As the authors report, women have experienced gains on almost all fronts, including significant increases in educational attainment, labour-force participation and employment rates, and a narrowing of the male-female wage gap as women's earnings rose more rapidly than men's in the first half of the 1990s. In both the likelihood of being employed and the likelihood of being unemployed, women's outcomes have improved considerably while those of men have deteriorated.

This chapter also provides an overview of low-income trends. The figures show that the low-income rate, which essentially mirrored cyclical changes in unemployment throughout the 1980s and at least up to 1994, continued to rise to a peak in 1996 (four years after the end of the recession) despite improving labour markets, and had not recovered by 1998. According to the authors, the increase in the low-income rate over the 1988-98 period can be attributed almost entirely to declines in employment earnings among families. Moreover, as they point out, social transfers did not offset these earnings declines as they had in the 1980s. The low-income gap (defined as the difference between Statistics Canada's low-income cut-off and the average income of low-income individuals and families), which had fallen steadily and significantly following the recession in the early 1980s, increased sharply after 1989 and continued to widen into the recovery through to

1998. According to the authors, the widening gap stemmed from both lower social benefits and employment earnings received by low-income families.

The issue of child poverty has been a dominant theme of the social policy debate in Canada for well over a decade. During the 1990s, however, the concern over this problem has shifted from simply a desire to reduce the incidence of child poverty to a broader awareness of its potential long-term consequences not only for the children currently affected, but for subsequent generations as well. These broader concerns have emerged as a result of the rapidly growing body of theory and evidence on the potential role of the "environment" in all of its complexity, including family structure, socio-economic status, neighbourhood and community, in predicting adult outcomes. These various factors can have a determining influence on early childhood development and subsequent readiness to learn, as well as on education and labour market outcomes later in life. One of the central issues in this debate is the nature of the relationship between family characteristics, in particular family income, and the long-term outcomes of children. As Miles Corak of Statistics Canada argues in the introduction to his chapter, an understanding of the extent of intergenerational mobility and the mechanisms that bring it about is of great importance for policy-makers. It has implications for education, health care, immigration policy and early childhood investment.

Corak's chapter provides an overview of the state of knowledge in this area and, most importantly, reveals the complexity of the factors at play and the gaps in our understanding of the underlying causes and effects. According to the author, Canadian society is characterized by a relatively high degree of intergenerational mobility — high enough to suggest that "being raised by a low-income parent does not pre-ordain children to a low-income adulthood." Indeed, Canada ranks among the most mobile advanced economies along with Sweden and Finland and has a degree of intergenerational mobility two to three times that of the United States. In general, international comparisons indicate that countries with a high degree of intergenerational mobility tend to have low rates of income inequality and child poverty. Canada differs in this regard, in that the incidence of child poverty reported is more akin to that of the least mobile countries such as the United States and the United Kingdom (although the use of an absolute as opposed to relative measure of poverty does improve our ranking). A further important point highlighted by Corak is that the pattern of intergenerational mobility varies across the income distribution. The degree of mobility, which is high at the lower end of the income distribution, declines to a moderate level further up the lower half of the distribution and then rises again over the upper half before reaching almost complete immobility at the very top.

Corak finds that, except for those families who are very well off and able to transfer wealth to their children, the primary way in which families might influence the future economic status of their children is indirectly through financial and non-financial investments in their overall capacity to succeed in the labour market. He notes that various models of human capital investment might help explain the patterns of intergenerational mobility observed, pointing to the potential link between the financial capacity of parents and access to higher education and the more subtle correlation between parent and child education levels, which bring other factors into play such as parental expectations and non-monetary investments. On the first issue, Corak finds little direct evidence on whether or not Canadian youths are being denied access to post-secondary education due to financial constraints, although it is evident that the pattern of increased intergenerational mobility in Canada over the past decades does coincide with the significant expansion of post-secondary education and public financial support. As for the quality of the environment in which young children are raised, and its impact on their development and long-term outcomes, Corak stresses that there is very little solid evidence about how this process plays out and in particular to what extent it is related to family income. As a result, he concludes, it is difficult to gauge the effectiveness of government policy based on long-term productivity arguments, and it may be that the best argument for initiatives aimed at child poverty and other related programs is the actual benefits provided to the children involved.

Finally, in the last chapter of the volume Kathleen Day and Quentin Grafton of the University of Ottawa explore the relationship between the economy and the environment. One perspective sees economic growth leading to environmental degradation by imposing stresses on limited natural resources and ecosystems and by increasing emissions of pollutants. A second perspective argues that the opposite relationship holds. Economic growth, once a certain level is achieved, leads to a cleaner environment, as higher incomes shift societal preferences toward better environmental quality and at the same time provide the resources necessary to achieve this goal. In addition, it is argued that economic growth is increasingly service-based, "decoupling" pollution from economic activity.

The authors examine the relationship between economic growth and environmental degradation in Canada. They point out that Canada faces a number of environmental challenges, including climate and atmospheric change, species loss, degradation of ecosystems and depletion of renewable natural resources, and that these challenges are driven by human activity in terms of consumption patterns, production processes and waste disposal. Day and Grafton use an econometric model to relate per capita income to 10 measures of environmental degradation in Canada over the past several decades. They find that economic growth has not itself reduced environmental degradation, as the second approach outlined above suggests. The implication of their findings is that economic growth does not necessarily resolve environmental problems. This does not mean that further economic growth is irreconcilable with the sustainability of the environment, but it does mean that public policy, at both the national and international level, must play a key role in balancing the needs of the environment with those of the economy.

CONCLUSIONS

The relationship between economic performance and social progress in Canada in the 1990s is complex and multi-faceted, as demonstrated by the chapters in this volume. Nevertheless, one message does stand out. The poor economic performance of the 1990s, as evidenced by high unemployment rates and slow growth in real income, had a major impact on many indicators of social well-being. While economic growth by no means buys advances in all areas of social progress, it is critical in a number of important areas such as poverty, economic security and consumption. There is little doubt that the longest decade would have felt considerably shorter had economic performance been better.

As stated earlier, the relationship between economic performance and certain measures of social progress may vary over time. Some observers have noted that economic growth and falling unemployment in the second half of the 1990s do not appear to have significantly reduced the poverty rate and have expressed concern that poverty reduction may have become "decoupled" from economic growth. Unfortunately, data on low-income trends are currently available only to 1998 so we do not yet know the impact of recent strong growth on poverty. Therefore, it is too early to make a judgement on the decoupling issue. A further possibility, which should also be investigated, is that previous cuts to social programs may have offset the effect economic growth might have had on the earnings of low-income families in the late 1990s. As we have seen, Canada's social policy infrastructure has undergone considerable change over the last decade, and in many ways the real test of the new regime will be how it performs through the next economic downturn.

Clearly, the impact of the poor economic performance and the key policy decisions of the 1990s is still being felt, and the repercussions are likely to continue to unfold for some time into the future. From this perspective, judgements on the effects of the 1990s must be considered interim ones. Indeed, the long-term consequences may be more important than those in the short term. Future contributors to the *Review of Economic Performance and Social Progress* will be invited to explore these issues.

NOTES

1 See Fortin, Sharpe and St-Hilaire (forthcoming) for a collection of papers exploring various dimensions of the linkages between economic growth and inequality. The papers are drawn from the IRPP-CSLS conference on this topic held in January 2001 in Ottawa. The conference papers are posted at www.csls.ca and www.irpp.org

2 The index simply adds the rate of unemployment to the rate of inflation thus treating them as equivalent.

REFERENCES

Bouchard, B., and J. Zao. 2000. "University Education: Recent Trends in Participation, Accessibility and Returns." *Education Quarterly Review* 6(4):24-32.

Fortin, P., A. Sharpe and F. St-Hilaire. Forthcoming. *The Linkages Between Economic Growth and Inequality.* Special issue of *Canadian Public Policy*.

Sharpe, A. 2001. "Determinants of Trends in Living Standards in Canada and the United States, 1989-2000." *International Productivity Monitor* 2:3-10.

Statistics Canada. 2000, June. *Income in Canada, 1998*. Catalogue #75-202-XPE. Ottawa: Statistics Canada.