OBSERVATION

TD Economics

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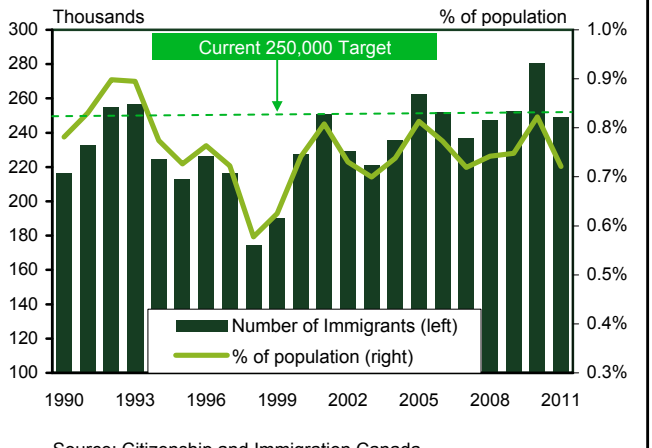
ESTIMATING CANADA'S FUTURE IMMIGRATION NEEDS

Highlights

- The federal government recently launched public consultations asking the question, "What is the appropriate level of immigration for Canada?"
- We approached this question from a purely mathematical perspective by projecting labour force growth rates under various immigration assumptions
- If a goal of the system is to maintain gains in the labour force at roughly their historical trend rate, then our analysis suggests that the annual immigration target would need to be raised from its current 250,000 level to at least 350,000 after 2016 in order to offset the impact of the aging population.
- While this estimate does provide some food for thought, there are many other considerations that need to be taken in deciding an optimal immigration target. First, this is a very narrow perspective and meeting labour market needs is just one of many goals of the immigration system. Balancing all of those goals would likely yield a different estimate.
- Moreover, the more pressing concern is the poor economic outcomes of newcomers to Canada. Much effort has been made by the federal and provincial governments to improve this situation, and until these reforms bear fruit, it is likely counterproductive to raise the current 250,000 target.

The federal government recently launched public consultations asking the key question, "What is the appropriate level of immigration for Canada?" While simple at first glance, this is an exceedingly difficult question to answer. Immigration has many different goals and each goal will augur for a different level. Put simply, there is no magic number. Traditionally, Canada has accepted around 0.8% of its population in new permanent residents each year (chart 1). However, we are now at an inflection point. The baby boomer generation is starting to retire, and this will have a material impact on Canadian businesses if they cannot find the skilled labour they need to continue growing in the future. To some degree, we can ease this demographic transition through immigration. But, if there is going to be more focus on immigration, then Canada needs a more robust process for deciding on what future immigration levels should be.

CHART 1: IMMIGRATION TO CANADA



Source: Citizenship and Immigration Canada

In this report, we approach this question from a purely mathematical perspective by estimating what rate Canada's labour force would grow at under various levels of immigration. This exercise is not meant to provide hard recommendations for immigration targets, but rather a few reference points with which to anchor the policy debate. This is because looking at this issue entirely through the lens of aggregate labour force growth is a very narrow perspective, and balancing all of the goals of the immigration

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system would likely yield a different estimate. In addition, the more important aspect of this debate is how to improve the economic outcomes of the immigrants that are already here and whom face significant labour market hurdles. On this front, much effort has been made recently by both the federal and provincial governments and an assessment of their success should precede any discussion of changing the current immigration target.

Why is labour force growth important?

The two key factors that determine growth in an economy over the longer haul are labour productivity and a growing labour pool. While it can be argued that productivity is the more important determinant of economic prosperity, Canada's economy has benefitted from solid gains in the labour force. Over the past two decades, real GDP per capita, productivity and the labour force have all been increasing at around 1.25% per year.

As such, barring a substantial productivity boom, a growing labour pool will be needed to sustain gains in living standards, especially in the next couple of decades. The baby boomer generation now accounts for roughly 40% of our current labour force and many will move into retirement in the coming years. This heralds a period in which labour force growth could potentially turn negative in the absence of immigration, simultaneously putting severe financial strain on government spending programs such as Old Age Security and on healthcare, while also constraining government tax revenues due to slower trend economic growth. As such, additional working-age individuals will also be needed in order to bolster government revenues.

In table 1, we estimate varying levels of labour force growth and the immigration that would be required to achieve them. If a goal were to maintain labour force growth of between 1-1.25%, then our calculations suggest that annual immigration levels could be maintained around 250,000 over the next few years. However, as the demographic pressures bite, the annual requirement would rise above 350,000 over the medium term in order to take up the slack due to the aging population.

How did we come up with these numbers?

To arrive at these figures, we projected what the Canadian population would look like 10 years from now in the absence of any immigration (permanent or temporary). Assumptions were made on labour force participation rates by age cohort. By taking the difference between the projected labour force levels and the "targeted" growth rates yields the number of immigrant workers that would be required annually in order to achieve the targets. The immigration numbers were grossed up to account for those that accompany immigrant workers that typically are not part of the labour force, such as young children. According to the 2006 census, roughly 53.7% of all immigrants that arrived between 2001 and 2006 were part of the labour force. For the Canadian-born population, the comparable figure is 54%.

TABLE 1: VARYING IMMIGRATION TARGETS AND IMPLIED LABOUR FORCE GROWTH RATES

Annual Immigration Levels	Implied Labour Force Growth Rates (Annual Average % Chg.)	
	2012-2016	2017-2021
150,000	0.6-0.8	0.1-0.5
200,000	0.8-1.0	0.3-0.6
250,000	0.9-1.1	0.5-0.8
300,000	1.1-1.3	0.6-0.9
350,000	1.3-1.5	0.8-1.1
400,000	1.4-1.6	0.9-1.2
450,000	1.8-2.0	1.2-1.5

Source: TD Economics

This implies that our forecast assumes no change in the composition of immigrants. However, there have been numerous calls to increase the share of economic class immigrants to upwards of 70% from its current level of around 60%, which TD Economics would support. This would lower the required number of immigrants modestly to due to the economic class having a higher participation rate than the other classes.

Given the large number of assumptions necessary (Table 2), we developed several projection scenarios in order to develop a range of immigration requirements all of which are anchored by a constant labour force growth target. As one can imagine, the number of immigrants required is not constant over time. In fact, our assessment indicates that Canada can maintain its current 250,000 immigration target until 2016 and still sustain a pace of labour force growth consistent with recent history. Older workers are increasingly delaying retirement and the largest portion of the baby boomer generation remains firmly attached to the labour force. However, beyond 2016, that portion of the baby boomer generation (currently in their late 40's and early 50's) will begin to push beyond the age of 55 where labour force participation rates begin to fall dramatically. At this point, labour force growth grinds to a halt and higher levels of immigration are likely necessary to sustain a modest pace

of labour force growth. If we were to maintain the current 250,000 target, average labour force growth would slow to around 0.75% per year.

Concluding Thoughts

We must stress again that while this analysis provides some food for thought, deciding on an optimal immigration target would need to be based on a more rigorous framework that takes several considerations into account. One in particular is the relatively elevated unemployment rate in Canada currently, although we would expect this rate to fall over time under our base-case economic scenario. A more pressing concern is the poor economic outcomes of recent immigrants to Canada. Despite being more educated than their non-immigrant counterparts, many face tremendous hurdles in joining the labour market, relating to language barriers and credential recognition issues. As a result, each new cohort of immigrants arriving in Canada falls increasingly further from the Canadian-born counterparts (see TD Economics report "Knocking Down the Barriers"). If Canada were able to more effectively and efficiently integrate its newcomers, then required number of immigrants would notionally be reduced given a higher productivity level among the immigrant labour pool.

Much effort has been made by the federal and provincial governments to try to improve these outcomes. Recent announcements include introducing a minimum language standard for federal skilled workers, a skilled tradesperson stream for federal skilled workers, and a method of pre-assessing credentials before the immigrant arrives. Until these reforms bear fruit, it is likely counterproductive to raise the current 250,000 target. In fact, one could even go so far as to make the argument for a lower near-term immigration target given these issues. We are, however, not strongly in favour of this due to the difficulty of projecting immigration requirements, the multi-year nature of immigration and settlement, and the potential reputational impact on Canada. In addition, we are optimistic that recent policy developments will improve the situation for newcomers to Canada, which should help to address some of these issues.

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TABLE 2: ASSUMPTIONS REQUIRED TO ESTIMATE IMMIGRATION LEVELS TO CANADA
Population Forecast by Age Cohort
Immigration Rates
Permanent immigration set to 0
Temporary immigration (temporary foreign workers, students, refugee claimants) set to 0
Death rates (2 scenarios)
1) Set to 2011 level
2) Projected by age cohort using hodrick-prescott filters
Emigration rates
Set to average over last 10 years distributed by age cohort
Labour Force Forecast
Generated using population forecast combined with labour force participation rate projections by age cohort
Participation Rates (3 scenarios)
Participation rates for those under the age of 55 were projected using hodrick-prescott filters for all 3 scenarios
Three projection scenarios for participation rates for those over the age of 55
1) Rise by average change since 2000
2) Rise by half of average change since 2000
3) Rise 10% faster than average change since 2000
Immigration Levels Estimation
Required number of immigrants workers derived from 1% labour force growth forecast less labour force projections detailed above
Total number of immigrants required calculated by dividing number of immigrant workers needed by share of immigrants ages 15 and over and by the participation rate of immigrants
Children of immigrants who arrive through the forecast horizon are added to the labour force as they reach working age.