



2013 HR-NHQ 027637

**MEMORANDUM TO THE DEPUTY MINISTER OF EMPLOYMENT AND
SOCIAL DEVELOPMENT**

WHAT WE KNOW ABOUT THE MIDDLE CLASS IN CANADA

OCT 15 2013

(FOR INFORMATION)

SUMMARY

Please find attached a presentation summarizing research findings on the income, spending and wealth patterns of Canada's middle class over 1993-2007, based on internal research conducted over the past three years (Annex A).

Findings point to a middle class that isn't growing in the labour market, is increasingly indebted although it has a relatively modest standard of living, and are less likely to move to higher income (i.e., the middle class is no springboard to higher incomes).

A briefing session can be organised should you wish.

BACKGROUND

In this research, middle-income Canadians are those whose after-tax family income adjusted for family size falls between 75% and 150% of the overall adjusted median income. This definition is used by researchers in Canada and the United States to study this segment of the population. It is also the definition preferred by the International Labour Organisation.

The deck has been presented at a Medium Term Planning event.

CURRENT STATUS

SPR is currently updating the analysis with more recent data (2008-2011) in order to assess the impact of the latest recession.

ATIA ✓

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Attachment: 1



Human Resources and
Skills Development Canada

Ressources humaines et
Développement des compétences Canada

Canada

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ANNEX A

What we Know About the Middle Class in Canada

September 27, 2013

Objectives of the research and data sources

▪ Objectives

- To summarize research findings on the income, spending patterns and wealth of middle-income Canadians; and
- To compare their situation to that of Canadians in lower and higher income brackets.

▪ Data Sources

- **Income:** cross-sectional and longitudinal data from the master files of Statistics Canada's Survey of Labour and Income Dynamics.
 - Cross-sectional results: 1993, 1996, 1999, 2002, 2005 and 2007.
 - Longitudinal results: panel one (1993-98), panel two (1996-2001), panel three (1999-2004), and panel four (2002-2007).
- **Wealth:** cross-sectional data from the master files of Statistics Canada's Survey of Financial Security (SFS 1999 and 2005) and Canadian Financial Capability Survey (CFCS 2009).
- **Spending:** cross-sectional data from the master files of Statistics Canada's Survey of Household Spending (SHS 1999, 2005 and 2009)

Why care about middle-income Canadians?

- According to Easterly (2001): *“A higher share of income for the middle class and lower ethnic divisions (i.e. a ‘middle-class consensus’) are empirically associated with higher income and higher growth. These associations are robust to a number of alternative controls. A middle class consensus is also associated with more education, better health, better infrastructure, better economic policies, less political instability, less civil war and ethnic minorities at risk, more social ‘modernization’ and more democracy.”*

- In the U.S., Stiglitz, a Nobel laureate in economics, argues that inequality is holding back the economic recovery for four reasons, three of which have to do with the middle class:
 - First, the middle class is too weak to support consumer spending that has historically driven economic growth.

 - Second, the hollowing out of the middle class means that they are unable to invest in their future, by educating themselves and their children and by starting or improving businesses.

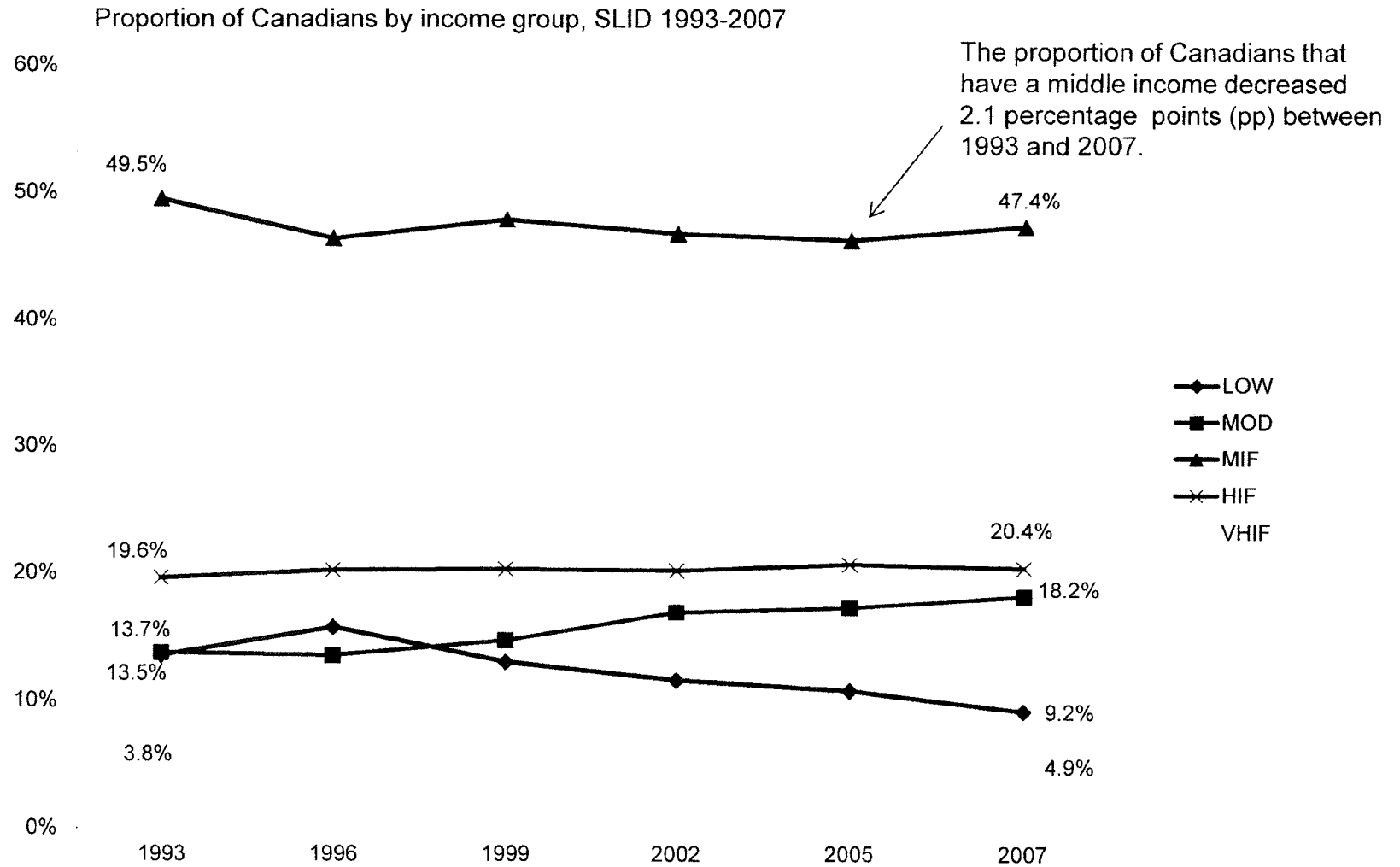
 - Finally, the weakness of the middle class is holding back tax receipts, which means that the government cannot make the vital investments in infrastructure, education, research and health that are crucial for restoring long-term economic strength.

- In Canada, political parties are making the middle class a central piece of their agendas.

Definitions

- **Low Income (LOW)**
 - After-tax economic family income is below the relevant after-tax low-income cut-off (LICO) in the reference year.
- **Modest Income (MOD)**
 - After-tax economic family income is above the relevant after-tax low-income cut-off (LICO) but below 75% of the overall adjusted median income in the reference year.
- **Middle Income (MIF)**
 - **Adjusted after-tax economic family income is between 75% and 150% of the overall adjusted median income in the reference year.**
- **High Income (HIF)**
 - Adjusted after-tax economic family income is higher than 150% but at most 250% of the overall adjusted median income in the reference year.
- **Very-High Income (VHIF)**
 - Adjusted after-tax economic family income is higher than 250% of the overall adjusted median income in the reference year.

There is a slight hollowing out of the middle class in Canada

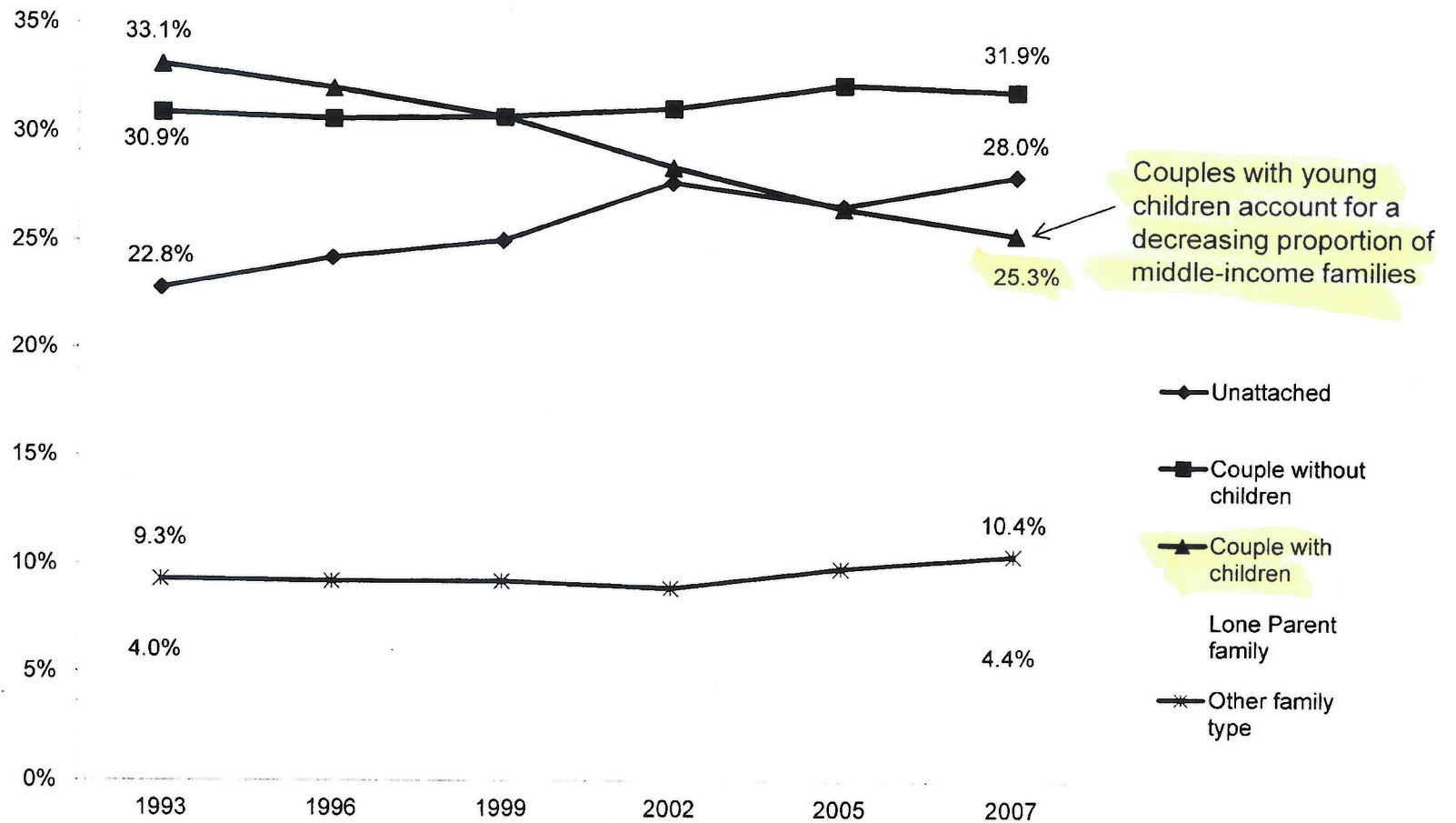




What is the face of the middle class?

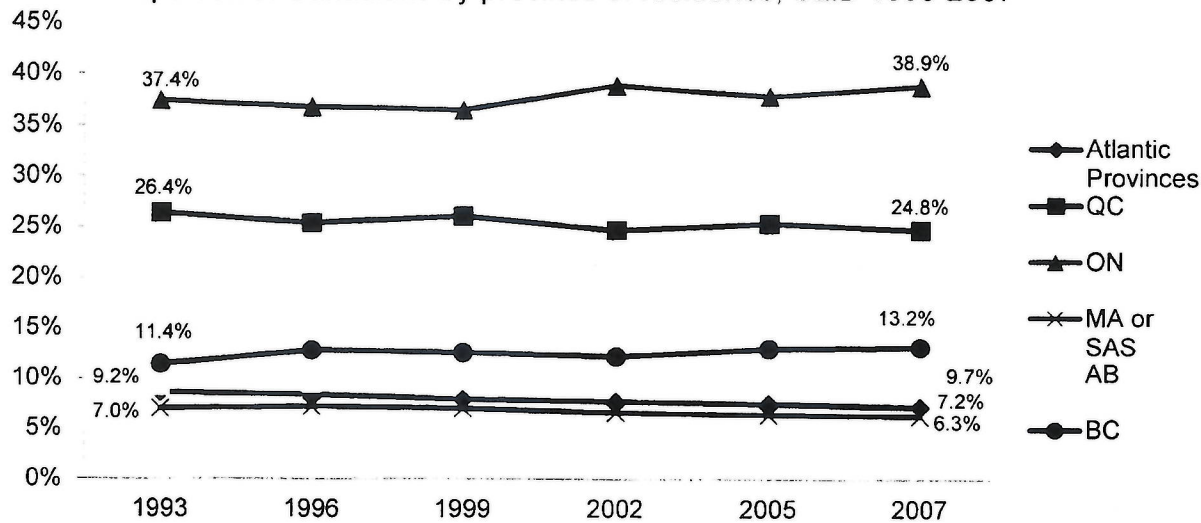
The '2 parents- 2 kids' stereotype is not representative of the middle class anymore

Proportion of middle-income families by family type, SLID 1993-2007



The majority of middle-income Canadians live in Ontario or Quebec

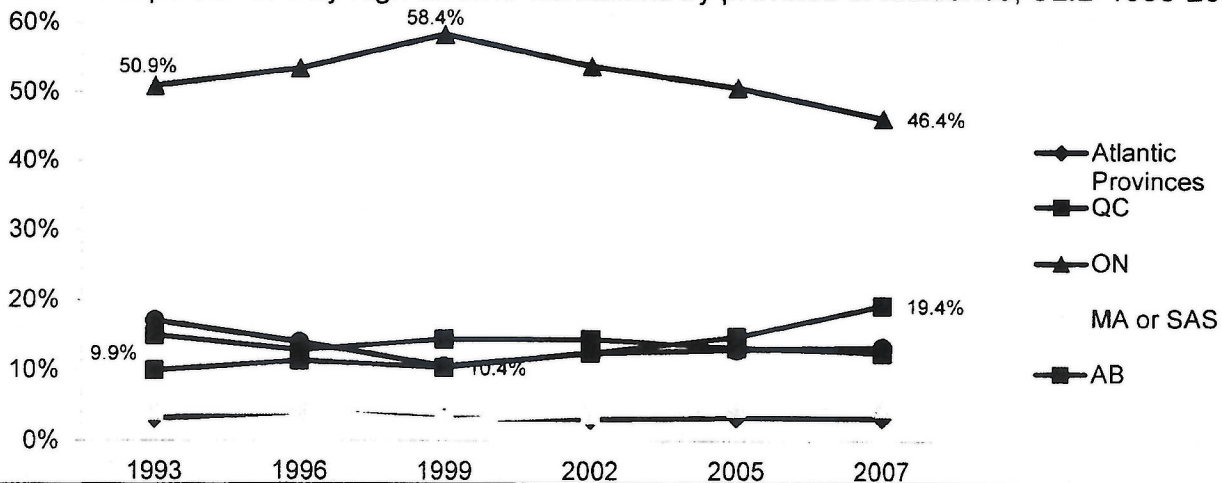
Proportion of Canadians by province of residence, SLID 1993-2007



Most middle-income Canadians live in Ontario or Quebec (63% in 2007).

- This has not changed much over the past 15 years.

Proportion of very-high income Canadians by province of residence, SLID 1993-2007

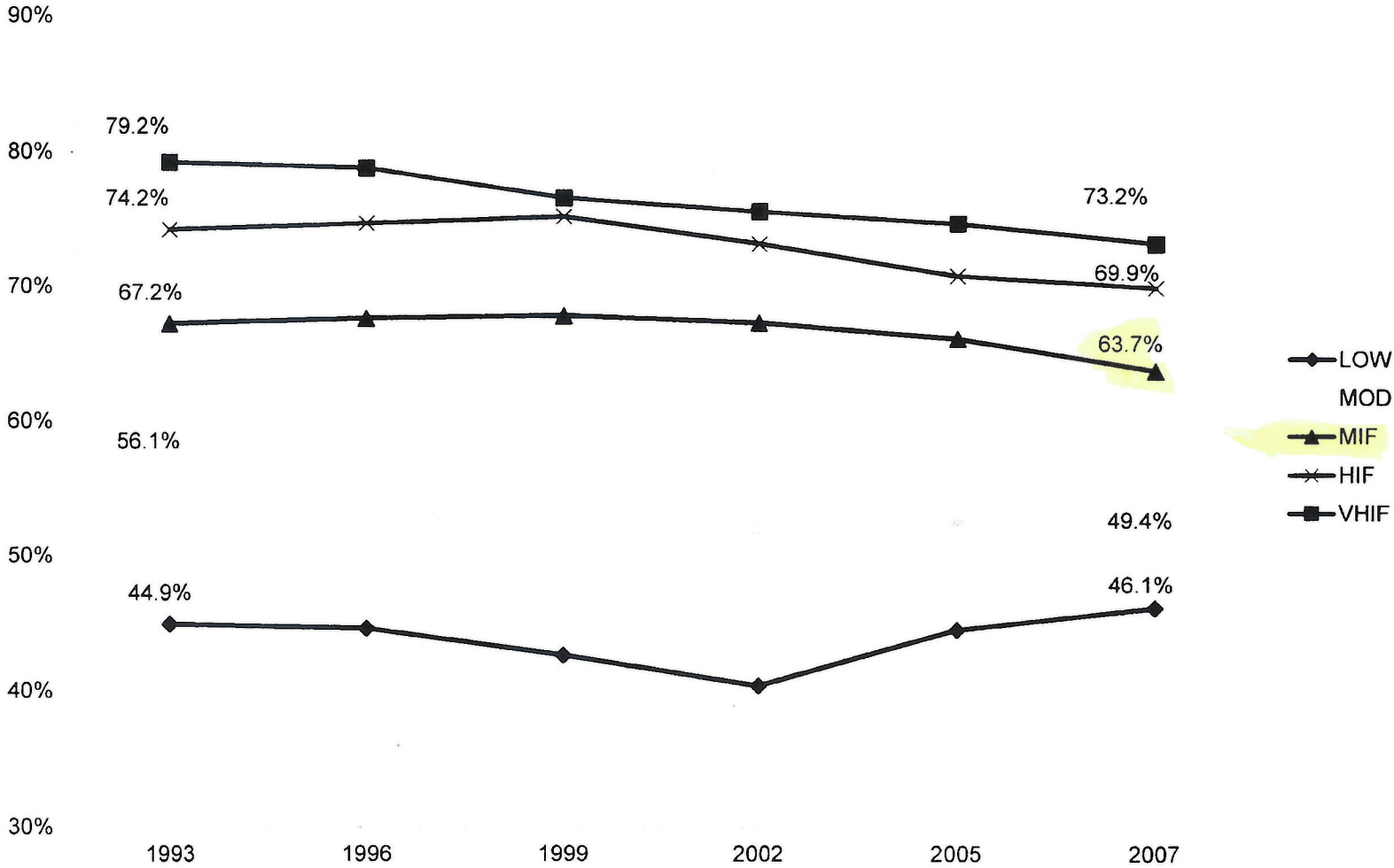


Most very-high income Canadians live in Ontario, but they are increasingly likely to be found in Alberta, i.e. **money is moving out West**

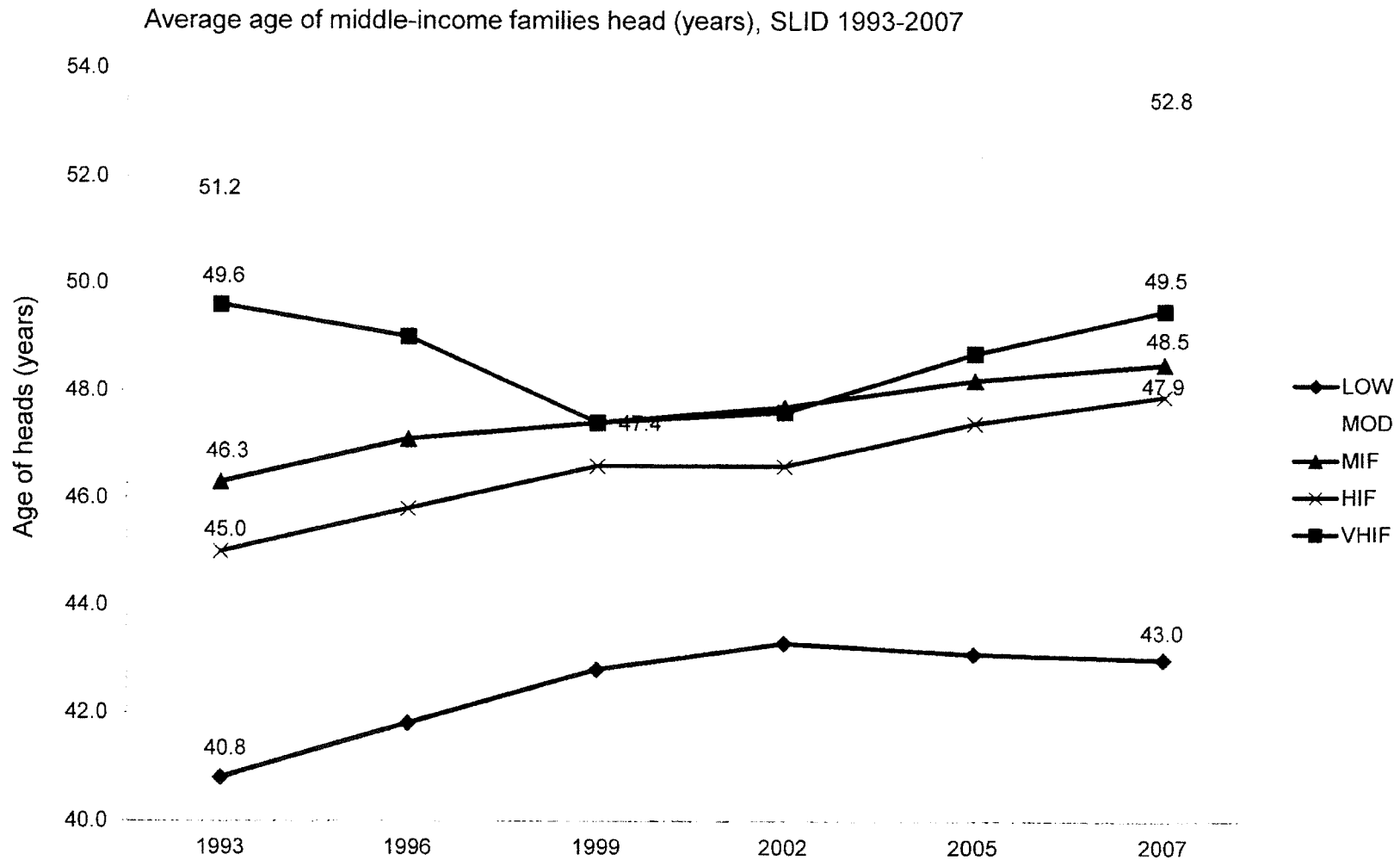
- Between 1999 and 2007, the proportion that lived in Ontario decreased 12 pp while the proportion that lived in Alberta increased 9 pp.

Most middle and higher-income families are headed by a man, but decreasingly so

Proportion of families whose main income earner is a man, SLID 1993-2007

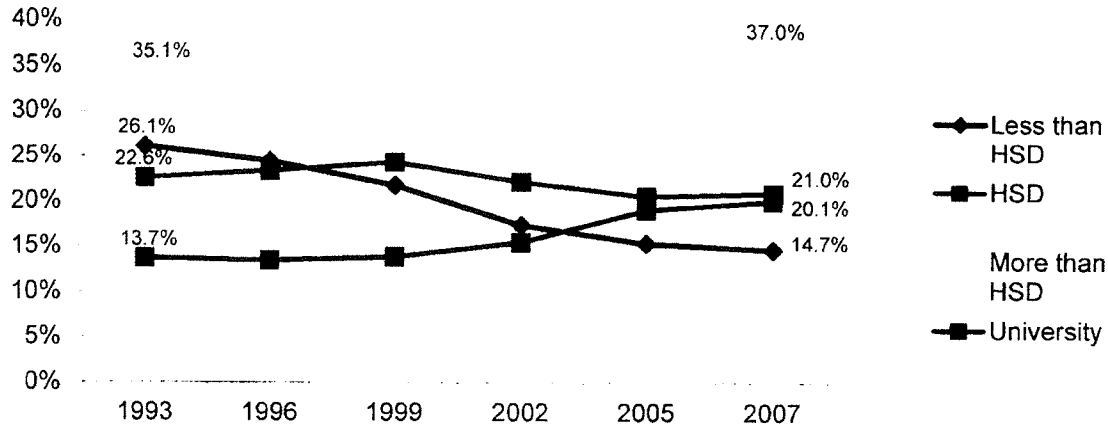


Heads of middle-income families are getting older...



...and more educated

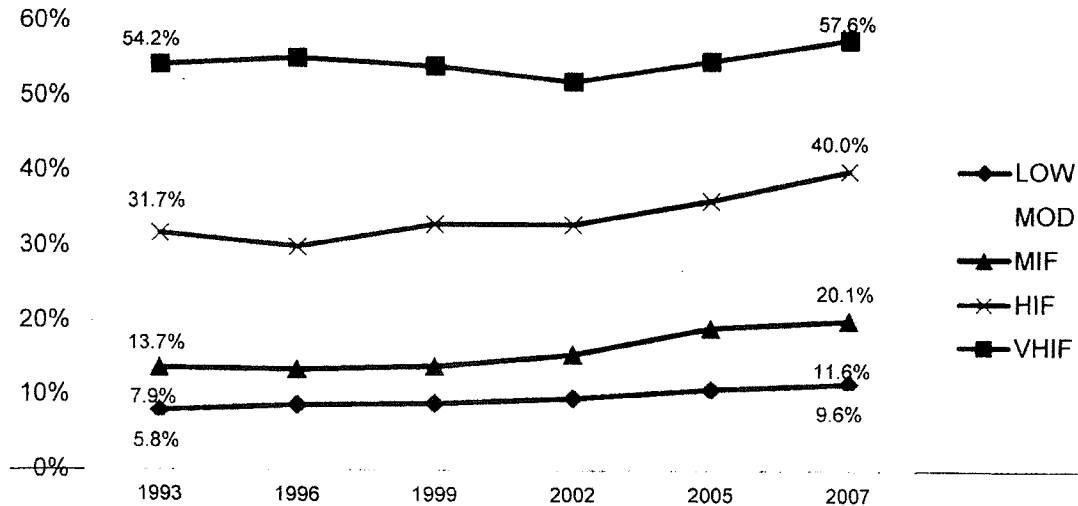
Proportion of family heads by education level, middle-income families, SLID 1993-2007



Heads of middle-income families are increasingly educated.

- In 1993, 26% had not completed high school. By 2007, this proportion had dropped below 15%.
- The proportion who held a university diploma increased 6.4 pp over this time period.

Proportion of families whose head hold a university diploma, by income group, SLID 1993-2007



Nevertheless, heads of higher-income families are significantly more educated.

- Over 1993-2007, the proportions of heads who held a university diploma always were 20 to 40 pp higher in high/very-high income families than in middle-income families.



How did the income of the middle class evolve over time?

The market does not reward middle-income families so well...

Year-over-year change in the earnings and after-tax income of economic families, SLID 1993-2007

	Year over year change in average economic family earnings * 1993-2007 (sample limited to families with positive earnings)	Year over year change in average economic family after-tax income* 1993-2007
LOW	0.5%	-1.5%
MOD	1.3%	1.8%
MIF	1.7%	3.6%
HIF	3.3%	4.3%
VHIF	6.3%	6.2%

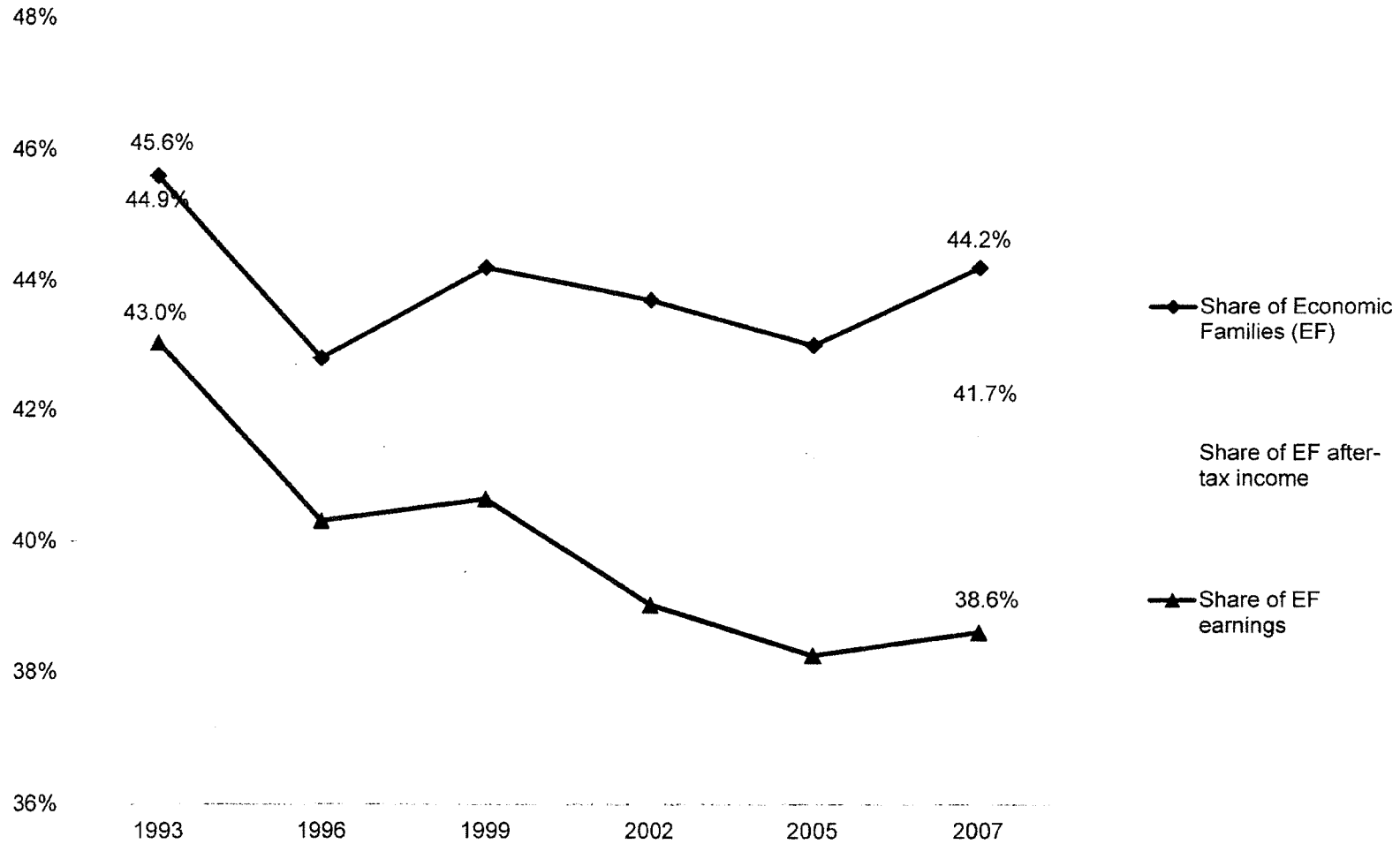
Between 1993 and 2007, middle-income families experienced a much better progression in income than earnings.

- They saw their earnings rise, on average, by 1.7% per year while their after-tax income increased at a rate of 3.6% per year.

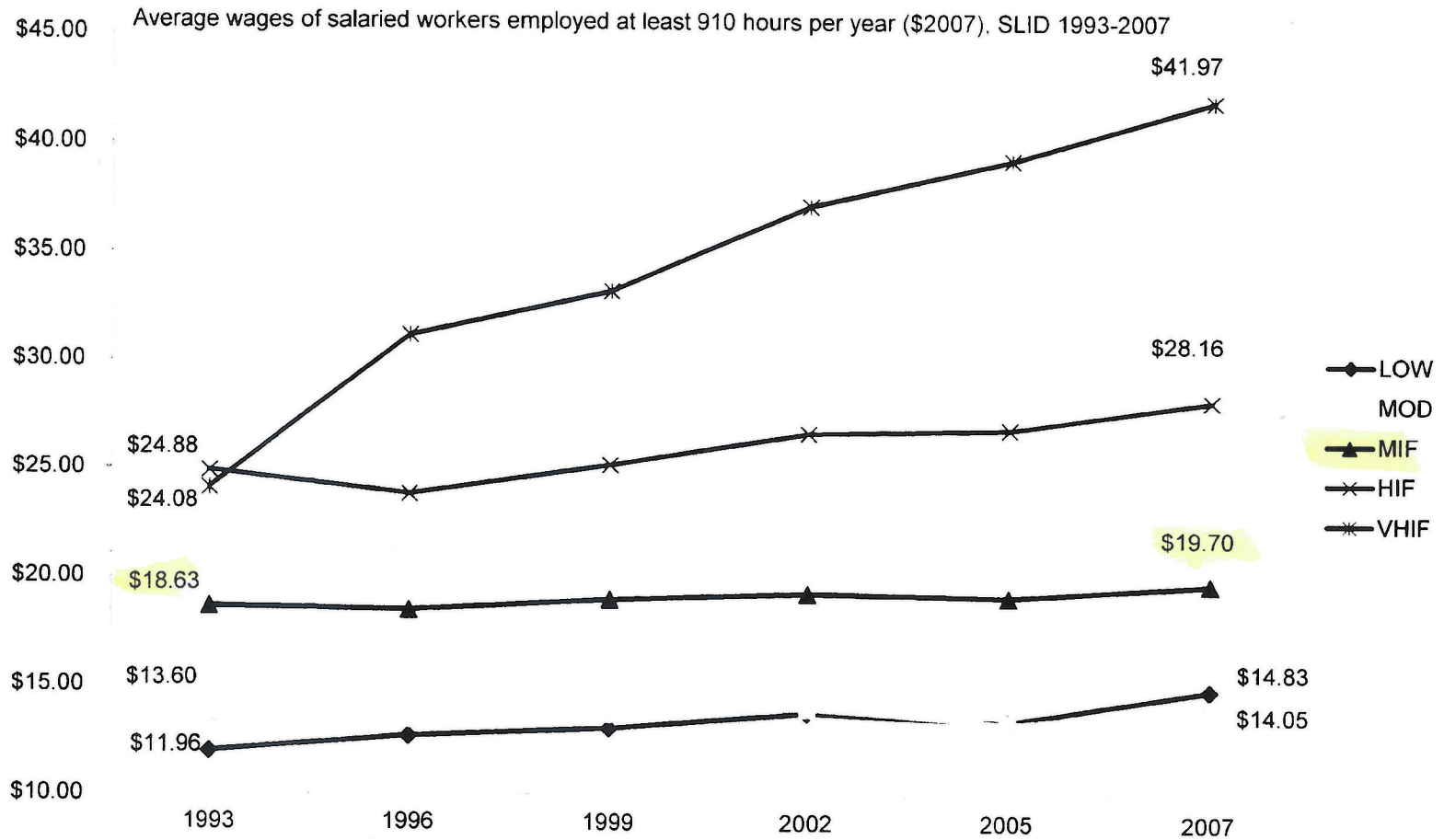
*All numbers used to calculate year-over-year changes were adjusted to reflect their value in constant 2007 dollars, using the Consumer Price Index (CPI).

...as a result, they get an increasingly smaller share of the earnings pie

Middle-income families' share of economic families, total earnings and after-tax income, SLID 1993-2007



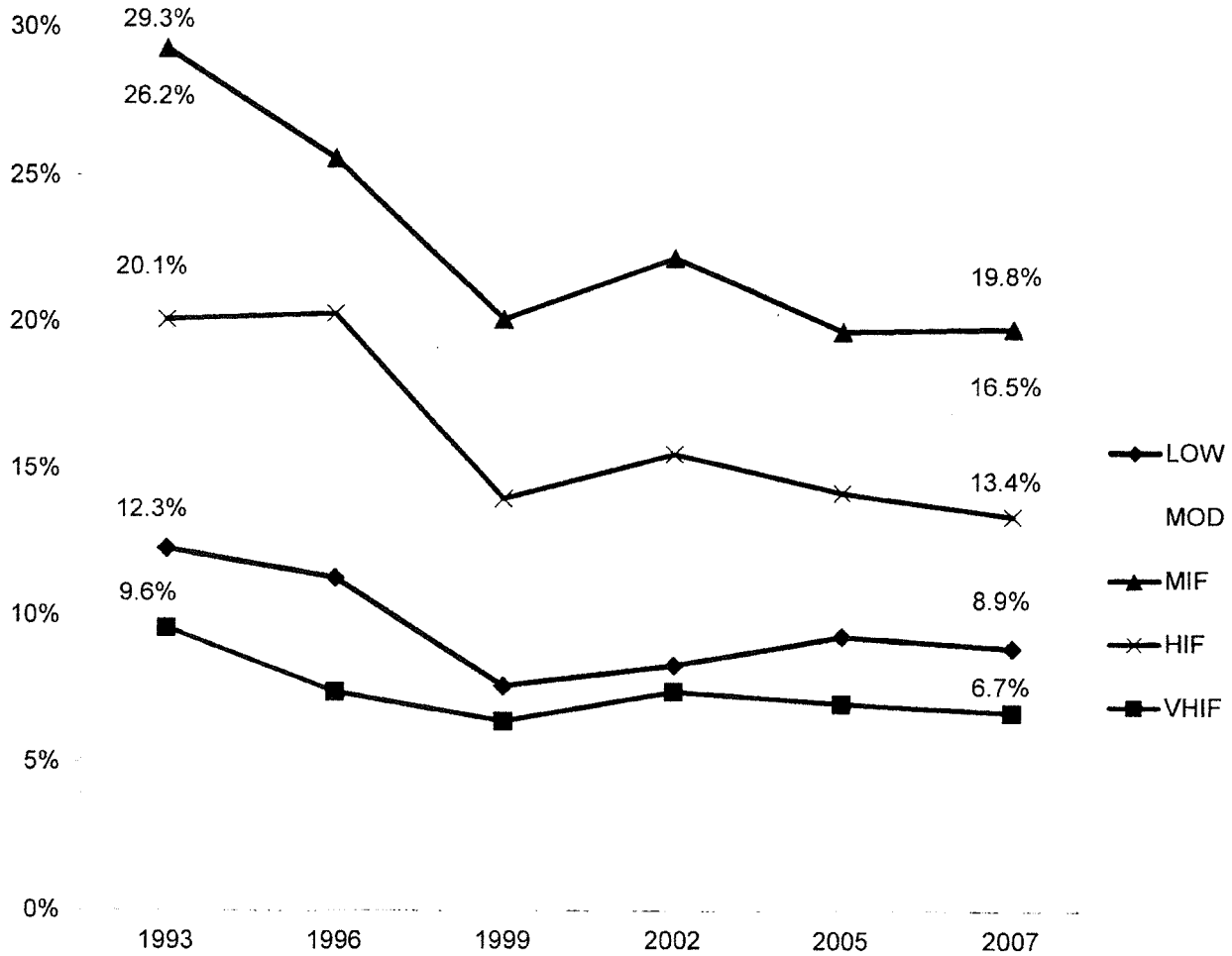
The wages of middle-income workers have stagnated...



Note: Family income is used to determine which income group individuals fall into. This graph present wage data for the individuals in those families.

...and they get lesser government support for work transitions

Proportion of economic families whose members received any EI benefits, by income group, SLID 1993-2007



	Average EI benefits received (\$2007), SLID	
	1993	2007
MOD	\$8,200	\$6,800
MIF	\$8,200	\$6,900
HIF	\$7,500	\$6,700

Middle-income Canadians are no more likely to move up than down the income ladder

Income mobility of middle-income Canadians , SLID 1993-2007

	Average number of years spent in various income groups by Canadians who started a panel in the middle class over:			
	1993-1998	1996-2001	1999-2004	2002-2007
LOW	0.27	0.21	0.16	0.18
MOD	0.41	0.46	0.51	0.50
MIF	4.55	4.62	4.56	4.54
HIF	0.73	0.66	0.71	0.72
VHIF	0.04	0.05	0.06	0.06

Canadians who were a member of the middle class at the beginning of a panel spent on average:

- Four and a half years out of six in middle income (close to 80% of the period);
- About eight months in low or modest incomes; and
- About as much time in high or very high incomes (nine months).

Logistic regressions indicate that the overall probability of joining higher-income brackets for middle-income Canadians is low (at 3.7%), confirming what descriptive statistics had indicated.

However, some factors increase the likelihood of moving up the income ladder. The most important are:

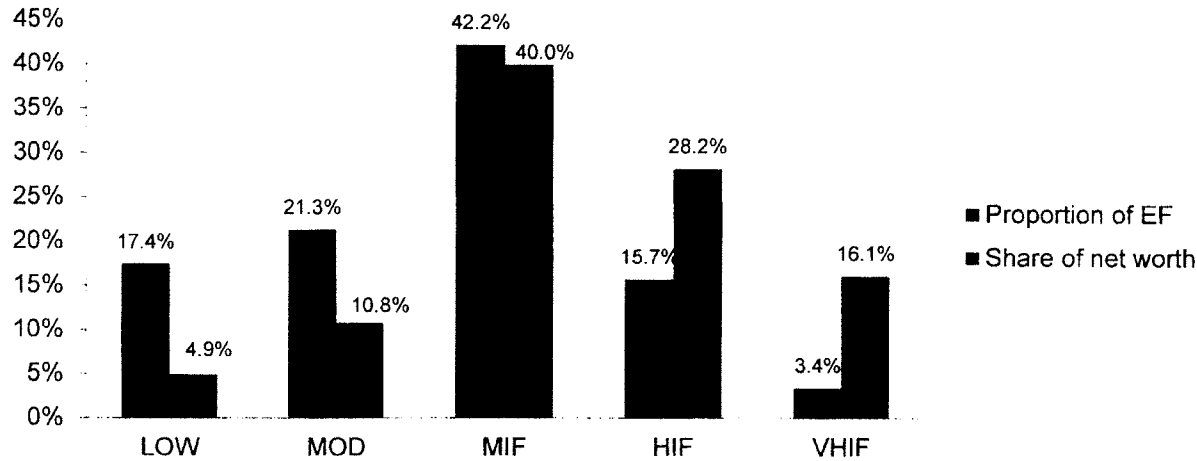
- Experiencing a reduction in family size (7.5 pp);
- Benefitting from an increase in the earnings of other family members (5.2 pp); and
- Holding a university diploma (5.3 pp).



What happened to middle class' wealth?

Wealth is not distributed equally among the middle class...

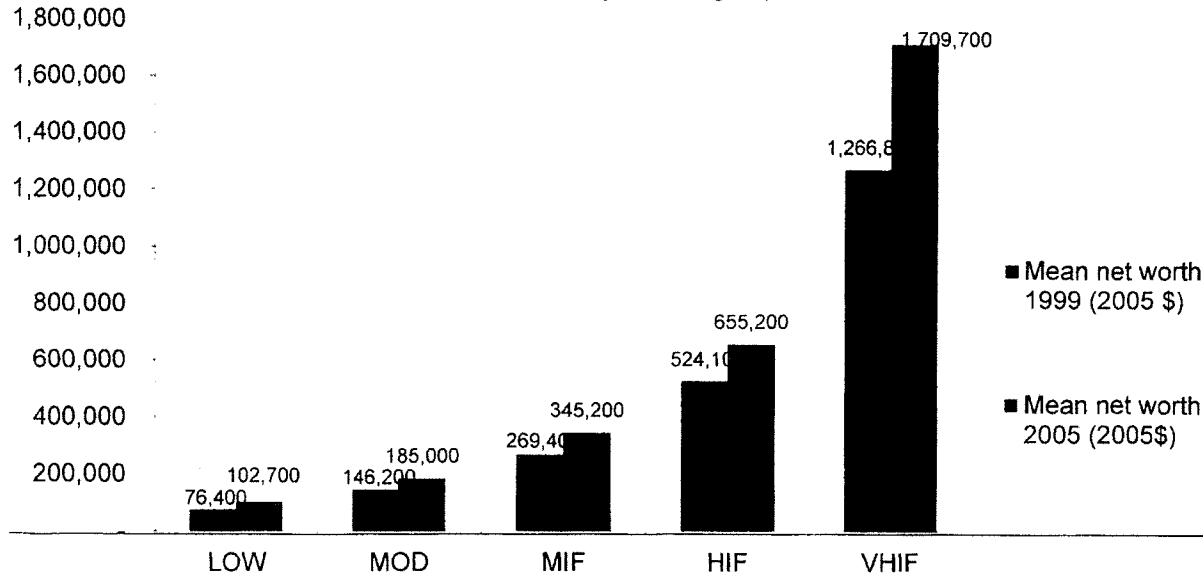
Proportion of economic families and total net worth held by income group, SFS 2005



Distribution of net worth among middle-income families, SFS 2005

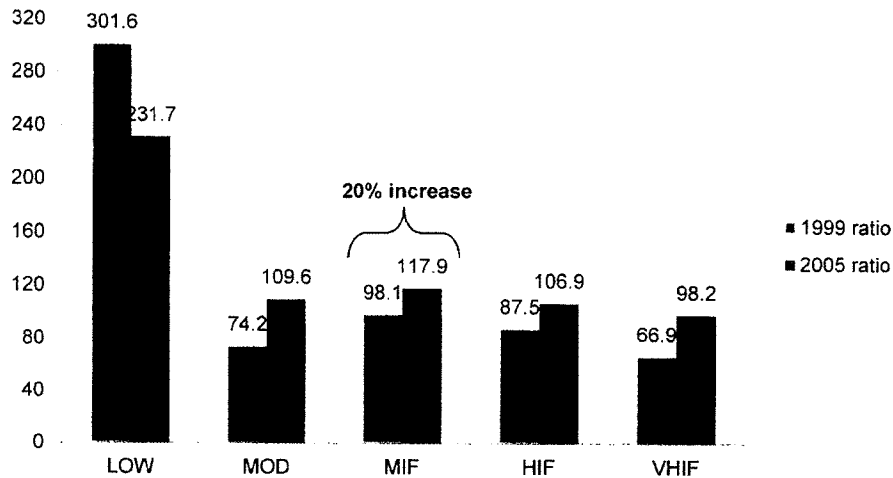
	Proportion of MIF with:
Zero or negative wealth	4.4%
\$1-\$4,999	2.3%
\$5,000-\$14,999	4.7%
\$15,000-\$29,999	4.9%
\$30,000-\$49,999	4.6%
\$50,000-\$74,999	7.0%
\$75,000-\$99,999	4.5%
\$100,000-\$149,999	8.7%
\$150,000-\$249,999	13.6%
\$250,000 or more	45.4%
Mean net worth	\$345,200
Median net worth	\$208,700

Mean net worth of economic families, by income group, SFS 1999, 2005



...and middle-income families are increasingly vulnerable to financial shocks

Ratio of household debt to economic family disposable income, SFS



Between 1999 and 2005, the debt-to-income ratio of middle-income families increased 20% (from 98.1% to 117.9%), i.e. they spent more of their income on debt payments and, therefore, were more likely to be financially strained.

There are no current detailed data on wealth. However, at the national level, the debt-to-income ratio has increased steadily over the past few years and stood at 163% in 2013, a rate close to the one observed in the U.S. before the 2007-2008 housing crash.

Composition of the asset and debt portfolios of middle-income families, SFS

ASSETS	1999	2005	DEBTS	1999	2005
Private pension	29.8%	31.0%	Mortgages	79.2%	75.0%
Non-pension	9.5%	9.5%	Line of credit	4.6%	8.5%
Non-fin. assets	53.9%	52.5%	Credit card and installment debt	3.0%	3.7%
• Main residence	35.7%	37.7%	Student loans	2.8%	2.1%
Equity in business	6.8%	7.0%	Vehicle loans	6.8%	6.7%
			Other debts	3.5%	3.9%

The largest asset of middle-income families is their main residence and increasingly so.

- In 2005, close to 40% of the assets of the middle class sat in their house.

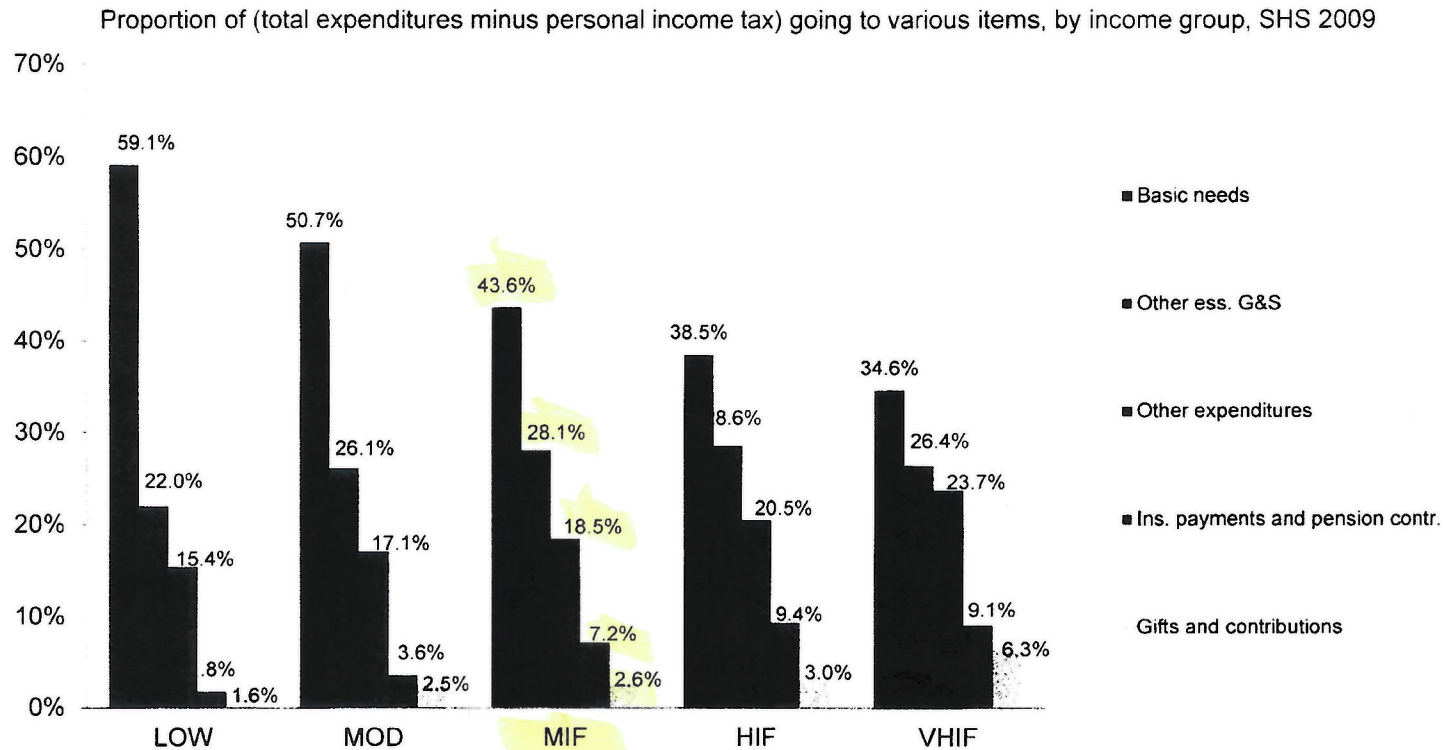
Mortgages are their largest debt, but lines of credit and credit cards are gaining importance.

- In 1999, these types of credit accounted for less than 8% of the middle class debt. By 2005, they accounted for over 12%.



What about middle class' spending?

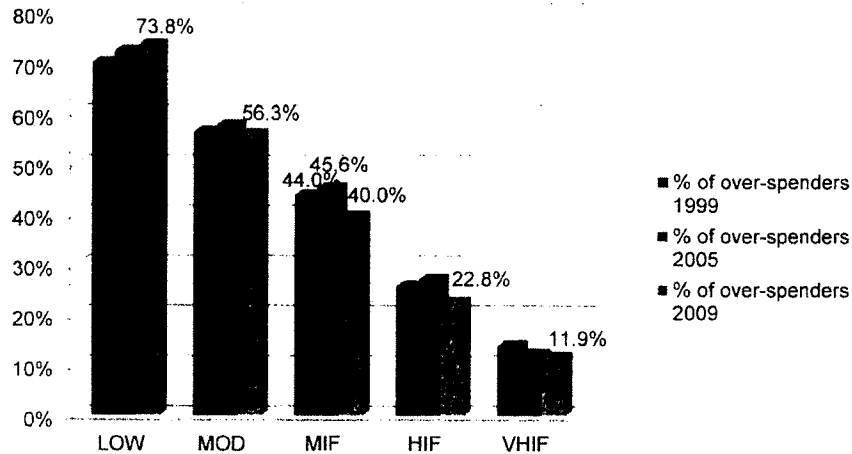
Basic needs account for a large proportion of middle class' spending...



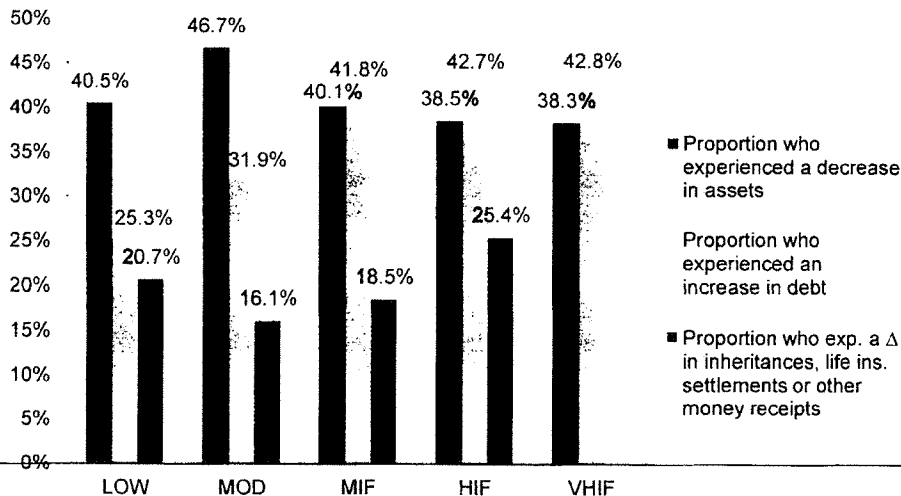
In 2009, basic needs (i.e. food, shelter and clothing) accounted for a large proportion of middle-income families' expenditures (after tax). This proportion slightly decreased over time (from 45.1% in 1999 to 43.6% in 2009). Meanwhile, the proportion going to other essential goods and services (such as communications, transportation, etc.) slightly increased (from 25.7% in 1999 to 28.1% in 2009), while the proportion going to other expenditures (such as recreation, reading material, etc.) was almost stable (at around 19%). The proportion going to gifts and contributions was small and did not vary much.

...and many in the middle mortgage their future to sustain their current consumption

Proportion of economic families who spend more than they earn, SHS



Proportion of over-spenders who experienced a decrease in assets, an increase in debt, or received money gifts, SHS 2009



In 2009, 40% of middle-income families spent more than they earned.

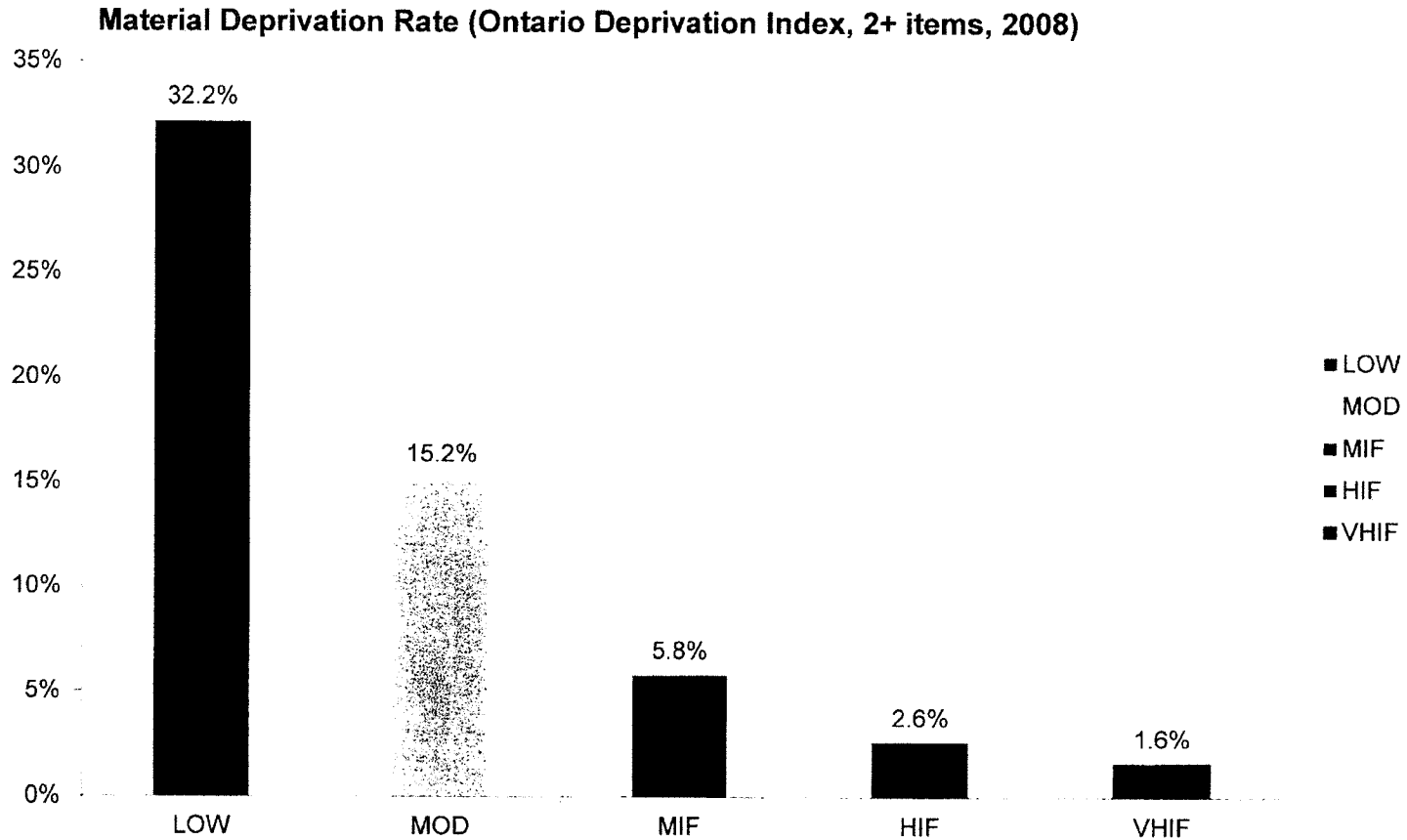
- On average, they spent 25% more than their adjusted after-tax income (\$37,100).
- Although the proportion of over-spenders was lower in 2009 than ten years ago, amounts over-spent increased 16% (from \$7,800 to \$9,100, in adjusted \$2009).

Over-spenders are more likely than others to be young, educated and to work full time.

Over-spending comes at a cost. In 2009, to finance their extra consumption:

- 40% of middle-income over-spenders sold assets; the average drop was \$10,700.
- 42% increased their debt load, on average by \$10,100.
- 19% got gifts, life insurance settlements, etc. The mean amount received was \$7,600.

A relatively small proportion of middle-income households experience material deprivation



Main Findings

- Over 1993-2007, there has been a slight hollowing out of the middle class, and the face of the middle class has changed considerably.
 - Couples without young children and unattached individuals now account for most middle-income families.
 - Heads of middle-income families are older and significantly more educated.
- Although middle-income families experienced a good progression in after-tax income, the same cannot be said of their earnings. In particular, the wages of middle-income workers stagnated. Furthermore, over the medium term, middle-income Canadians are unlikely to move to higher income brackets i.e. *the 'Canadian dream' is a myth more than a reality.*
- Although the middle class holds a relatively fair share of the 'wealth pie', higher-income families have far greater nest eggs. Furthermore, wealth is not divided equally among middle-income families, with those headed by younger individuals being at a disadvantage. Owning a house makes a big difference for middle and lower-income families.
- A large proportion of middle-income families' spending goes to basic needs, and many in the middle spend more than they earn, mortgaging their future to sustain their current consumption.
- In Ontario, a relatively small proportion of middle-income households experience material deprivation.