

I. Executive Summary

This is the Twenty-First Actuarial Report since the inception of the Canada Pension Plan (CPP) in 1966. It presents the financial status of the Plan as at 31 December 2003. The previous triennial report is the Eighteenth Actuarial Report as at 31 December 2000, which was tabled in the House of Commons on 10 December 2001.

The Canada Pension Plan was subject to a series of amendments since the Eighteenth Actuarial Report pursuant to the adoption of Bill C-3 and Part 4 of Bill C-30. The effects of these amendments were covered in the Nineteenth and Twentieth Actuarial Reports, which were tabled 17 June 2002 and 20 April 2004, respectively, in the House of Commons. Part 4 of Bill C-30 received Royal Assent on 14 May 2004. According to the legislation, the coming into force of CPP amendments requires the formal approval of at least two-thirds of the provinces representing two-thirds of the population. This is in process and should be completed in due course. The effects of Bill C-3 and Part 4 of Bill C-30 are included in the financial projections of this report.

A. Purpose of the Report

This report has been prepared in compliance with the timing and information requirements of the *Canada Pension Plan*. Section 113.1 of the Act provides that the Minister of Finance and ministers of the Crown of the provinces shall review the state of the CPP once every three years, and may consequently make recommendations to change the benefits or contribution rates, or both. Section 113.1 identifies the factors they consider in their review, including information to be provided by the Chief Actuary.

Another important purpose of the report is to inform contributors and beneficiaries of the current and projected financial status of the Plan. It provides information to evaluate its financial sustainability over a long period, assuming the Act remains unchanged. Such information should facilitate a better understanding of the financial status of the Plan and the factors that influence costs, contributing to an informed public discussion of issues related to it.

B. Scope of the Report

Section II presents the general methodology used in preparing the actuarial estimates included in this report, which are based on the key “best-estimate” assumptions described in Section III. Section IV includes the projections of the income, expenditures and assets of the Plan over the next 75 years. Section V summarizes the financial results under alternative younger and older population scenarios. The impact of financial markets volatility on the financial status of the Plan is also examined.

Section VI presents a general conclusion about the financial status of the Plan, while Section VII consists of the actuarial opinion. The various appendices provide for supplemental information on the provisions of the Plan, the description of the data, the assumptions and methods employed, the sensitivity analysis and the long-term financial sustainability of the Plan. The reconciliation of the results with those presented in the Eighteenth Report and the financial results under the steady-state contribution rate are also shown.

C. Main Findings

The results of the actuarial projections of the financial status of the Canada Pension Plan presented in this Twenty-First Report are generally consistent with the trends revealed in the previous triennial actuarial report.

- Demographic changes will have a major impact on the ratio of workers to retirees; the ratio of the number of people aged 20 to 64 to those aged 65 and over is expected to fall from about 4.9 in 2004 to 2.3 in 2050.
- The pay-as-you-go rate is expected to increase steadily from 8.3% in 2004 to 11.3% by 2050, mainly driven by the retirement of the baby boom generation.
- The steady-state contribution rate, which is the lowest rate sufficient to sustain the Plan without further increase, is 9.8% of contributory earnings. This rate is the same as presented in the previous triennial actuarial report and 0.1% lower than the legislated 9.9% contribution rate.
- With the 9.9% legislated contribution rate, the assets are expected to increase significantly over the next 17 years, with the ratio of assets to the following year's expenditures growing from 3.1 in 2004 to 5.6 by 2021.
- Total assets are expected to grow from \$68 billion at the end of 2003 to \$147 billion by the end of 2010.
- During the period 2004 to 2021, contributions are more than sufficient to cover the expenditures. Thereafter a proportion of the investment earnings is required to make up the difference between contributions and expenditures. In 2050, the proportion of investment earnings is 29%.
- Investment earnings, which represent 14% of revenues (i.e. contributions and investment earnings) in 2004, will represent 27% thereof in 2020. In 2050, investment earnings represent 32% of revenues. This clearly illustrates the importance of the investment earnings as a source of revenues to the Plan.

D. General Conclusions

The results contained in this report confirm that the legislated contribution rate of 9.9% in 2004 and thereafter is sufficient to pay for future expenditures and to accumulate assets worth \$147 billion (i.e. 4.4 times the annual expenditures) in 2010. In 2050, the assets are projected to be \$1,554 billion or 6.3 times the annual expenditures.

The steady-state contribution rate determined under this report is 9.8%. Better than anticipated economic experience, especially regarding labour force participation and employment data, over the period 2001 to 2003, combined with the amendments since the last report have put downward pressure on the steady-state contribution rate. On the other hand, a more pessimistic demographic outlook, due to the continuing downward trend in fertility rates and increases in longevity, combined with lower expectations with respect to inflation and rates of return on investments have put upward pressure on the steady-state contribution rate. These factors tend to counterbalance each other, leaving the steady-state rate unchanged at 9.8%.

To measure the sensitivity of the long-term projected financial position of the Plan to changes in the future economic and demographic outlook, two demographically based scenarios that portray a generally younger and older population were developed. The younger and older population scenarios produced steady-state contribution rates of 9.3% and 10.3%, respectively.

Under the 9.9% legislated contribution rate, the assets are projected to grow rapidly over the next 17 years as contribution revenues are expected to exceed the expenditures over that period. Assets will continue to grow until the end of the projection period, but at a slower pace, and the ratio of assets to the following year's expenditures (asset/expenditure ratio) is expected to reach a level of 6.3 by 2050. These are indicators that the Plan is sustainable over the long term, as it is projected that there will be more cash inflows than outflows over the entire projection period. The pool of assets generated over the projection period provides the Plan with the capacity, through investment earnings, to absorb a wide range of unforeseen economic or demographic fluctuations, which otherwise would have to be reflected in the legislated contribution rate. Thus, despite the projected substantial increase in benefits paid as a result of an aging population, the Plan is expected to be able to meet its obligations throughout the projection period.