

What's the real issue in the debt debate?

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Is there a debate about public debt in Canada—and if there is, why should anyone care about it?

Ten years ago, the context for discussion of public debt in Canada was an economy in which federal and provincial governments were still running substantial deficits, despite the fact that public debt had recently risen rapidly to fractions of GDP that had not been seen in half a century. In addition, with high unemployment and a recent growth experience that contrasted very unfavourably with the USA, Canadians had ample reason for dissatisfaction with their real economic outcomes. Debate on the issue of public deficits and debts was therefore fierce, with frequent expressions of a sense of crisis, many adverse comparisons with other nations and a broad awareness of the importance of the government debt issue for Canadian society.

In contrast, in 2002-03, the federal government, like most provinces, was running a financial surplus, and economic growth was strong. The debt/GDP¹ ratio was, as a consequence, dropping like a stone. Canadians were adjusting to the prevalence of newspaper stories about the superior job creation record of the Canadian labour market, as growth in the U.S. slipped below that in Canada. With dramatic speed, both federal and state governments in the U.S. had shifted from large surpluses to large structural deficits. In broader international comparisons, Canada's low and falling debt/GDP ratio compared favourably with other OECD countries, and Canada was the only G-7 country to have a budgetary surplus in 2002 and to project another surplus for 2003.

With so much good news about, it was perhaps not surprising that the debt/deficit issue slipped off the media agenda and ranked relatively low in polling estimates of the policy concerns of Canadians. So why should there be a debate? What exactly *is* the problem?

One problem is that we do not have a clear objective for the ultimate level of the debt/GDP ratio and there is little evidence of agreement on how far Canadians want it to decline. Certainly there is little consensus among professional economists about the appropriate level of the public debt or the size and nature of its social costs and benefits. A second problem, which interacts with the first, is that it remains unclear exactly why “we” should care or why “we” might have a common opinion. “Efficiency” arguments do not produce a clear guide and “equity” arguments depend crucially on personal values, **which are bound to differ**. In the

¹In 2001-02 the federal debt/GDP ratio was 46.5 per cent, down nearly 20 percentage points from its peak in 1995-96. On a total government sector basis, between 1995 and 2002 Canada's debt/GDP ratio was reduced by 26.8 percentage points, the largest decline in the G7. (See Budget 2003, Ch.8)

controversy over the implications of the public debt, there has been a tendency to interpret the debt issue in terms of intergenerational equity, but I will argue that such an emphasis is fundamentally misplaced. In practice, the debate on deficits and debts has had the subtext of continuing disagreements over the size of government and the appropriate degree of redistribution by the state. Until this is recognized explicitly, we are unlikely to make much progress.

What is the optimal size of the debt?

As Don Drummond's calculations in this volume illustrate, the current policy settings of the federal government imply a continuing and rapid decline in the debt/GDP ratio. Although the recent string of surpluses has brought a useful reduction in debt principal, the main action is in the denominator, not the numerator of the debt/GDP ratio [the total stock of nominal debt is only declining slightly, but nominal GDP is currently rising at about six per cent annually.]² The question Drummond poses is: "How low should we go? What is the optimal level of the debt/GDP ratio?" He sees this as a challenge to the Canadian economics profession—surely economics should have something useful to say about the "fiscal anchor" of government and when one should stop the process of debt reduction.

In an informal poll at the final session of the conference, participants were asked to specify their own estimate of the optimal long-run debt/GDP ratio of all levels of government and the appropriate time frame for Canada to get there. At the time, the combined debt/GDP ratio of federal and provincial governments was slightly over 70 per cent, and all respondents³ thought some reduction was desirable. None of the 20 respondents was willing to suggest an optimal ratio less than 20 per cent or greater than 50 per cent. However, the two most frequently specified ranges (by 30 per cent of respondents in each case) were right at the edges of this band—20 to 25 per cent and 46 to 50 per cent. Although other responses were spread in between, and the average response was almost exactly in the middle of the range (35.7 per cent), that average clearly masks a significant divergence of opinion.

To some readers, the 20 per cent to 50 per cent range may seem like quite a dispersion of expert opinion. In fact, it represents a considerable compression of the range of published estimates cited by Scarth in his paper in this volume. These range from +60 per cent to -300 per cent.⁴ His own preference is for a debt ratio in the 20 to 25 per cent range, largely because that would correspond to the approximate levels of the mid-1970s. However, Scarth does not make strong claims for this particular ratio and he emphasizes that departures from the optimal debt ratio do not appear to have large efficiency costs. Furthermore, he regards deviations from the optimal range, both over the business cycle and for longer periods, as desirable, and he argues

²Third quarter 2002 over third quarter 2001—see CANSIM II—variable V498918

³ My own view is that there are large costs (both economic and political) when public finances become highly vulnerable to variations in interest rates – so my preference is for continued decline in the debt/GDP ratio. I do not have strong opinions about the target Debt/GDP ratio, but something like 40% (federal plus provincial) seems reasonable.

⁴Note that an optimal debt ratio of -300 per cent (i.e. a net asset position for government of three times GDP) means that the state would own much, if not all, of the nation's capital stock.

for a policy of “letting the debt ratio rise when we face major events that are expected to lower living standards”.

As a “fiscal anchor” for government budgets, this may seem to many people to be somewhat elastic—and the low cost of divergences from the optimum ratio that Scarth notes may prompt some readers to conclude that it does not matter much. However, Scarth does also get at the issues that sit behind the debate on government debt. He recognizes that debt may finance government spending on productive capital, so that estimates of the efficiency impacts of such debt depend heavily on one’s own opinions about the relative productivity of government or private sector investment expenditure. As well, Scarth argues that the chosen target for the debt ratio “must be based primarily on its consistency with our equity objectives” and he distinguishes between the distributional implications of tax cuts or spending increases as alternatives to debt reduction. As he notes, “liquidity-constrained (i.e., poorer) households may do better if the tax cut use for the fiscal dividend is rejected.” In this, he comes close to recognizing that disagreements over the appropriate role, size and income distributional impact of government have been the subtext for the debate on deficits and debts in Canada.

In an accounting sense, it is the *difference* between government revenue and expenditure, and not the *level* of either, which affects the deficit and the debt. In principle, one could solve “the debt problem” either at high levels of public expenditure accompanied by high taxes or at low levels of expenditure and taxation. In principle, the level of public expenditure is also analytically distinct from the redistributive impact of that expenditure: **the same level of expenditure can give rise to many different patterns of redistribution, while a given redistribution can be achieved at many different levels of expenditure.** In practice, however, in Canada the issue of debts and deficits has become intertwined with broader, and more ideological, debates about the appropriate role and size of government. In practice, expenditure cuts have been crucial in producing the recent surpluses of Canadian governments, and tax cuts have followed—so deficit elimination, debt repayment and a reduction of distributional equity and the role of government in Canadian society have coincided.

Inter-generational equity is a misleading focus

Of course, any mention of the term “equity” presupposes some conception of “equity among whom.” In the papers presented at this conference, the primary focus was on “inter-generational equity”—and with the exception of Scarth’s paper, generations were thought of in terms of a “representative agent,” so issues of “intra-generational equity” (i.e., equity between the rich and the poor of any given generation) were almost entirely ignored.

I would argue that this emphasis is profoundly misplaced. Over time it is the real assets of a nation’s residents that will determine their aggregate productive potential and consequently the economic well-being of different generations. But *government debt is a financial instrument*. Financial instruments are inherently an asset to some people (in this case, the holders of government bonds) but a liability to others (in this case, taxpayers). Hence, like any other financial instrument, bonds serve to redistribute income (i.e., potential consumption) among the Canadians who are alive at any given point in time. If more bonds are in existence at some future time, more of that period’s potential consumption will be transferred from taxpayers to

bondholders—which means that *intra*-generational distribution, and the equity implications of that redistribution, are central to the debt debate.

If one uses the term “generation” to mean “the set of all Canadians alive at any time” the issue of the “intra-generational distribution of income” is the distribution of income among the different persons who are alive at a particular time, while the issue of the “inter-generational distribution of income” is the distribution of aggregate income among people who are alive at different times. Since no generation can compel the labour supply of another generation living at a different time, no generation can directly determine the aggregate income of future generations. But each generation *can* determine the potential income of future generations by leaving an aggregate bequest of productive resources. In this sense, the crucial issue in the “inter-generational distribution of income” is the time path of the aggregate stock of productive resources, which one should interpret broadly to include human, environmental and social capital, as well as physical capital in machinery, equipment and structures.⁵ At any point in time, Canadian society has a particular potential aggregate income, as implied by Canada’s aggregate stocks of capital and labour. The intra-generational distribution of that aggregate income is determined by the distribution of labour incomes, by public policy decisions on transfer payments and tax burdens, and by the set of legal claims to property income (including bonds).

In this view, financial claims have the two-fold character of being an asset to their holder and a liability to their issuer. Domestically held government debt is an asset to the bondholder and a liability to the taxpayer—both of whom are living Canadian members of the same “generation.” It follows that we cannot get very far in understanding the debt problem if we assume there is only one type of agent, because taxpayers and bondholders are then the same “representative agent.” As Dahlby notes in his paper, if there is a single representative agent, “everyone holds the same amount of the public debt and everyone in the economy would be better off if the government repudiated the public debt.” In a representative agent model with only one type of agent, everyone owns debt, and everyone owes the taxes that pay the same debt. As a consequence, the public debt creates a “deadweight loss”⁶ for everyone since everyone’s labour supply decisions are distorted by the taxation necessary to pay the debt. However, nobody gets a net benefit since everyone is both a taxpayer and a bondholder. In this sort of economy,

⁵There is a substantial literature on the importance of human and social capital for long-term economic growth (see, for example, Helliwell, 2001). Public expenditure on education, training and health care clearly adds to the human capital stock, and in practice such spending dominates the program expenditure of governments. However, national income accounting conventions only count public sector investment in fixed capital and infrastructure as part of “capital formation.” Hence, although Scarth is correct in his comment that “government spends a very small proportion of its funds on *what the national accounts refer to as investment goods* (italics added),” it is the omission of human capital from the national accounts that explains this.

Throughout the conference, there was continual slippage back and forth between the System of National Accounts conception that government spending (G) is government’s consumptive use of resources (which does *not* include transfers between individuals) and the Public Accounts measures of public spending (which do include transfers).

⁶“Deadweight loss” is a measure of the inefficiencies in a market system created by taxation—i.e., the loss of consumer and producer surplus implied by the “wedge” that taxes impose between the prices that buyers pay and the revenue that sellers receive, in either product or labour markets. Theoretically, deadweight loss increases strongly as the tax rate rises, but there are substantial disagreements about how large it is, in practice.

there is a pure Pareto improvement from debt repudiation—everybody benefits—and therefore no reason not to do it⁷.

Hence, government debt only comes into existence and poses an issue for society because of the heterogeneity of types of agents. The collective decision to issue public debt would make no sense if all individuals were to buy the same amount of it, since they might as well just pay that amount as taxes. Heterogeneity in initial wealth and/or time preference is needed if we are to explain why some people initially make the individual choice to buy bonds (and abstain from consumption) while others do not, **preferring instead to consume more in the initial period and defer their tax burden to the future. However, given that there is a heterogeneity of wealth and time preferences, one of the social benefits of a market for public debt is that individuals are able to reallocate their potential consumption over time without risk of default**⁸.

In order to finance a given level of government expenditure over time, governments have to decide, at the margin, whether to tax or borrow in the current period. Borrowing now means a greater government debt, which implies higher future tax rates than would otherwise have been the case, which means more intra-generational redistribution (from taxpayers to bond holders) among the people who will be alive at different times in the future. If higher future tax rates imply distortions in future labour supply or savings behaviour that reduce future output, this deadweight loss will be a cost in the aggregate output of future generations that should be counted as “inter-generational redistribution of income.”⁹ Of course, taxing now would also imply deadweight loss so the correct measure of the impact of debt financing on intergenerational distribution is the difference in the present value of the deadweight loss between taxing now and taxing later. The issue of “equity” in inter generational distribution then depends, like the aggregate savings decision that determines the capital stock, on what one thinks the “fair” time path of aggregate consumption should be—and there is a large and profound literature on this point.

Intra-generational redistribution is the key issue

⁷In a representative agent model, there is also no reason for the public debt to be issued in the first place. In Dahlby’s model, it is just assumed that the economy starts with a government debt.

⁸ As the Bolder and Lee-Sing paper argues, in financial markets “Market participants generally view a liquid and active government securities market as the essential foundation of an efficient domestic debt market.” Hence, they argue that “debt management practice provides a public good to the Canadian public.” Of course, this argument that efficient financial markets depend on the sufficiently large availability of a risk free debt instrument in a variety of terms is only an argument for a positive gross level of public debt. The net level of debt could be zero (or even negative) if government owned a sufficiently large stock of assets to offset its gross debt. Government ownership of the capital stock has not been much in fashion recently, indeed the recent trend to privatization runs the other way.

⁹Hence, Bev Dahlby’s model is asking the intergenerational question in the right way, by looking at the impact of higher debt/income ratios (D/Y) on the time path of aggregate income (e.g. because increased debt/GDP will reduce capital accumulation or distort labour supply). In the real world, management of the debt incurs a real resource cost, which should be added to the future deadweight loss of debt financing. Surprisingly, nobody mentioned the administrative costs of debt management at this conference.

Up to this point, the term generation has been used to mean “those Canadians alive at a given time.” This usage is consistent with the discussion of national output, consumption and debt in many of the papers in this volume—e.g., those by Dahlby and Johnson. It is not the definition used by Boadway, however, who refers to a generation as “all those born at time t .” Whichever definition is used, it is still true that a bond is an asset to its holder and a liability to its payer. But if we use “generation” in Boadway’s sense of “birth cohort,” then some of each birth cohort will own bonds¹⁰, while others will not. This inequality between people of the same age who have financial wealth and those who do not is an important determinant of “intra-generational distribution.”

If all birth cohorts had the same proportion of bondholders and distribution of income and bond wealth, then there would be no net payments of bond interest between birth cohorts. The issue of “inter-generational distribution” (in Boadway’s sense of “generation”) that is posed by the government debt therefore depends on the extent to which birth cohorts differ in the proportion of bondholders and in their distributions of income and wealth. However, bondholders rather disappear from Boadway’s paper. When he says (see page 6) “the essential feature of long-term debt financing is that it is essentially an inter-generational transfer” (see p. 6) he does not mention that some members of *every* birth cohort will be receiving the payments that taxpayers are making.

If distribution between birth cohorts is the issue, then one must recognize that cohorts are linked within the family, both by inheritance and by *inter vivos* transfers. Within family lines, some families will pass bond portfolios to their descendants, while others will pass on only tax liabilities. Greater debt financing does imply a greater inter-generational (i.e., between birth cohorts) transfer of this type of financial instrument *within families*, (i.e., more assets for those who inherit bonds, larger future tax liabilities for those who do not), but the empirical issue is whether or not other transfers are unaffected. Although the Barro hypothesis of equal offsetting changes in other intra-family transfers is extreme, it is also extreme to argue that families don’t regard government bonds and other assets as being any sort of substitute for one another in their bequest decisions. To the extent that families treat government debt as equivalent to other assets, the *form* of intergenerational transfers within families will be affected by greater issuance of public debt, but not the level.

Debt reduction and the size of government

To this point, it could be argued that we have implicitly seen the public debt as being the result of a sequential decision process, in which the first decision to be made is the optimal level of public expenditure and the second decision is how much of that spending to finance by current taxation and how much to finance by future taxation (i.e., public debt). In this view, the level of spending and the financing decision are not logically linked. However, although this viewpoint is analytically appealing, **and has been the favoured assumption in this volume**, it is

¹⁰If we are thinking in terms of the lifetime well-being of the individuals who belong to the same birth cohort, then one would have to count both the bonds they now hold and the present value of any bonds they might expect to acquire later by inheritance.

rather dissonant with the actual debate on public debt in Canada, which has had the size of government as a consistent subtext.

If debt financing and the level of public spending are linked, then in calculating the aggregate intergenerational impact of greater debt, one should include the impact of the associated government spending on future productive resources. Does public spending crowd out productive private sector investment? Does public spending increase future productive resources, or does it all go to current consumption (evidence that “governments have spent beyond their means” as Robson puts it)?¹¹ It is at this stage that the debt debate begins to merge with the broader and more ideological public debate on the appropriate size and role of government.

Both Boadway and Robson advocate “generational accounting” without any real mention of the implications of its **crucial** assumption that all government expenditure should be allocated *at cost* to particular birth cohorts. To take a concrete example, if governments spend more on the maintenance or creation of physical infrastructure such as roads or bridges, or on human capital via spending on health, education or retraining, such expenditures add to the deficit and thereby increase the tax liabilities of future generations. Will the public capital stock and private human capital resulting from these expenditures also add to the incomes of future generations? In generational accounting the answer is assumed to be “no.” All government expenditure is assumed to be consumption: the rate of return on all public sector projects is implicitly set to zero

This assumption that the public sector produces no value-added is really quite fundamental to “generational accounting.” If public sector expenditures on things like education are presumed to be unproductive, their dollar values can be allocated, as “consumption,” to individuals in particular birth cohorts, and the dollar value of benefits to individuals is equal to the dollar value of costs to government. Individuals are, in this scenario, presumed to be indifferent between receiving a public service (e.g., an education) or a tax cut or a cash transfer of equal cost—so the net total of transfers and services received minus taxes paid can be calculated for each cohort. (The calculation is of course crucially contingent on the assumptions made about sharing within families and about the future incomes and taxes paid by each cohort.) The value of total expenditure will then correspond to the discounted dollar value of the taxation required to pay for such expenditures. In the accounting identity stressed by generational accountants, the “tax payments of the unborn” is the residual that balances the tax and expenditure sides of government accounts. However, if expenditures on services such as education yield greater dollar benefits to recipient individuals than their dollar cost to government (i.e., if the rate of return on human capital is positive), **this fundamental accounting identity of “generational accounts” becomes meaningless.**

¹¹Public spending on physical capital, such as roads, is captured in the national balance sheet but arguably most public spending, especially on education and health, assists in the production of human capital, which is individually owned and not counted in the System of National Accounts. Whether or not government spending actually crowds out private investment clearly depends on whether the economy is presumed to be closed or open to capital imports at the going international rate of interest and whether it is at or below full employment.

Even granted the assumption that all public spending is unproductive, generational accounts are entirely dependent on the allocation of expenditure to cohorts—which is extremely sensitive to how transfers of resources within households are modelled. For example, are education or health services received by children benefits to them personally or to the head of the household to which they belong? Generational accountants usually assume there is zero shifting between generations either of tax burdens or transfer benefits. It may well be that burdens and benefits are not fully shifted, but this assumption that there is *no* linkage between generations, except through the public debt, is clearly extreme.

As Kotlikoff and Summers (1981) demonstrated long ago, in 1974 at best some 19 per cent of total U.S. wealth was the result of life-cycle savings. The remainder of the U.S. capital stock was transferred within families as intergenerational bequests—and since then wealth inequality has increased considerably. The “generational accounts” perspective can only be rescued if it is argued that actual intergenerational transfers are all unintentional, arising only because of the uncertainty of lifetimes and the non-availability of annuities.¹²

In considering equity between different generations, we are focussing attention on a particular type of *group* equity. When there much greater variation within groups than there is between groups, as there is, it might be considered misleading to organize one’s data so as to suppress consideration of most of the inequality among individuals, and concentrate on the between-group differences that, empirically, constitute a relatively small component of aggregate inequality. Differences among individuals within birth cohorts are much larger in magnitude than differences between cohorts in average income. In fact, in the 1990s in Canada, as in other countries, over 95 per cent of aggregate income inequality (as measured by the Theil index) can be ascribed to inequality among people of the same birth cohorts, and less than five per cent to between-cohort differences in average equivalent money income (see Osberg, 2003:127).

The costs of deficit reduction

As Boadway has pointed out elsewhere, much of what government actually does is redistributive—either in direct transfer payments or as “quasi-private services” such as education, health or welfare services. As he says, “these quasi-private services fulfil an important equity role in the economy; indeed they constitute perhaps the main instruments of redistribution available to governments” (Boadway 1993:28). However, as Kneebone and Chung’s chapter in the current volume notes, it was the expenditure cuts between 1993 and 1997 that produced an increase of 3.8 per cent in the federal government’s primary balance, and set the stage for the dramatic declines in the debt/GDP ratio we have seen since then.¹³

¹²This implies that the failure of capital markets to supply the option of annuities is truly colossal and that the elderly who die leaving the multi-million dollar estates that in fact comprise much of the capital stock must have had highly exaggerated ideas of their potential life span, and/or future spending. As well, it implies that inheritance taxation, even at a confiscatory rate, would have no impact on savings or labour supply behaviour, since all bequests are assumed to be unintentional.

¹³„ Kneebone and Chung estimate the relative role of structural and cyclical expenditures on debt accumulation but their Hodrick-Prescott filter methodology for estimating potential output is basically a moving average of actual output (in this case, with an unusual and arbitrary “smoothing constant”), which essentially assumes that the makers

In several recent federal budgets, it has been noted that “federal government spending, as percentage of GDP, is at its lowest level in 50 years” (2001) and that “The program spending to GDP ratio has declined significantly, from about 16 per cent in 1993-94 to about 11 per cent in 2000-01. This decline was largely attributable to the expenditure reduction initiatives announced in the 1995 budget aimed at eliminating the deficit (2003).” Although a one time increase in health care transfers to the provinces increases the ratio in 2002-03, the growth rate of federal expenditures is projected to be less than that of GDP, implying that federal government expenditure will continue to shrink as a percentage of Canada’s economy. A small and forever declining role for the federal government in Canadian economic and social life means that the cuts in federal expenditures in the 1990s represent a permanent change in the size of the public sector, not a temporary belt-tightening. Although during the 1990s Canadians were encouraged to think of expenditure restraint in terms of the necessary sacrifices needed to solve a deficit problem, now that the deficit has been eliminated there is no intention to gradually restore expenditure to its historic share of GDP.

It should not be thought that reducing the size of the federal government has been a small achievement. Total federal program spending fluctuated between 15 and 16.2 per cent of GDP from 1959/60 to 1989/90 but is forecast to be just 11.8 per cent in 2004/2005. From 1951 to 1994, total federal spending was only once below 14 per cent of GDP.¹⁴ In 1948/49 total federal program spending (including transfers to the provinces) was 10.3 per cent of GDP and in 1949/50 it was 11.5 per cent.¹⁵ Since the Second World War, **these are the only** two years in which federal spending was below its current level. Since 1940-47 was dominated by the war effort, when federal expenditure was a much higher fraction of aggregate national output, one really has to go back to the 1930s to find a similar span of time in which federal government expenditure has been a comparable share of aggregate Canadian GDP.

As the federal budget of 2003 noted (Annex 4, page 6) when one adds together all the different levels of government, the picture is, if anything, magnified: “The rapid turnaround in Canada’s financial position, as a percentage of GDP, is attributable in large part to a sharp reduction in program spending, that is, all expenditures less gross debt charges. Between 1992 and 2002, Canada’s total government program spending as a share of GDP was reduced by 9.1 percentage points, a far greater reduction than in any other G7 country. As a result, Canada’s program spending relative to GDP is now below the G7 average whereas in 1992 it was well

of macro policy can make no lasting errors There is actually a lot of uncertainty about the level of “potential output” (even the Bank of Canada now presents the confidence bands surrounding its point estimates of potential output), so one needs to beware of “false precision”. However, the more fundamental objection is that Kneebone and Chung are engaged in an accounting exercise, which ignores the impacts of interest rates on GDP growth, and the consequent impact of growth on tax revenues and program expenditures. For a simulation of the time path of the debt/GDP ratio which does take into account the general equilibrium effects of monetary policy in the 1988-93 period, see McCracken (1998), who concludes that the monetary policy regime change of 1988 was responsible for essentially all of the debt accumulation of the early 1990s.

¹⁴In 1965-66, at 13.7 per cent of GDP.

¹⁵All figures from Osberg (2001) updated from Chapter 8, *Budget Plan*, Budget 2003

above the G7 average. In fact, in 2002 Canada's program spending, as a percentage of GDP, was lower than in all other G7 countries except the U.S.A."

It is clear that the debt crisis of the 1990s has been the occasion for a truly profound shift in the size of Canada's public sector—one that has been at least partially locked in by the tax cuts of the 2001 and subsequent budgets. One will look in vain for polling evidence¹⁶ that this long-term change is what most Canadians wanted—but it is what they have got, along with a reduction in the tax burden, particularly of upper income groups.

Cuts of this magnitude mean that the "social wage" of public services for all citizens has fallen, but the pain of this is least keenly felt by those who have high market incomes with which to purchase private substitutes. When, for example, the public education system is starved of resources, affluent parents can afford to pay for private alternatives to public primary and secondary schools and they can also afford the increasing tuition charges of post secondary education. The decline in quality of public education is, as a consequence, experienced primarily by those who cannot afford alternatives. Meanwhile, any disincentive effect of higher post-secondary tuition fees increases the relative scarcity of university graduates, and the private returns to post-secondary education of those who can afford to go. Debt reduction has been funded in part by decreased spending on education, which does have an intergenerational impact- but it differs qualitatively among family lines. The combination of a relatively better private education for the children of the affluent, greater scarcity value for their educational credentials and lower income tax rates on those higher earnings means greater individual incomes—but factory schooling for the masses, plus greater financial barriers to post-secondary education mean the less affluent have less chance of accessibility, and a greater private debt burden if they do persist in education.

Hence, in my view, the real issue in the debt debate is the implication for equity—within generations—of how we chosen to deal with debt. The public policy choices on taxation and expenditure that will shape the evolution of the debt will certainly affect "intergenerational equity," in the sense of equality of opportunity, as well as "intra-generational equity," in the sense of equality of outcomes, but it is misleading in the extreme to portray the debt issue as a conflict between generations.

¹⁶See Osberg (2001) for a detailed discussion and www.ekos.com for more recent updates.

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