

Report of Economic Climate

2004, A year of recovery for the Canadian economy

Gilles Soucy
Chief Economist

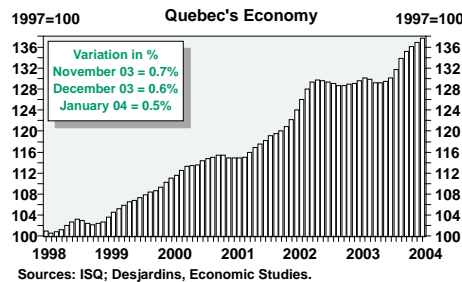
Economically speaking, 2003 was a year of disappointment for Canada and Québec. Without being disastrous, the growth of gross domestic product (real GDP) increased by only 1.7%, well below the 3.0% that we predicted one year ago. More importantly, for the first time since 1998, the Canadian economy has been surpassed by the US economy, which posted a growth rate of 3.1%.

Obviously, there were a number of calamities that struck our economy last year and curbed growth: SARS, Mad Cow disease, a hurricane in the Maritimes, forest fires in Western Canada and the huge blackout in Ontario. These unfortunate incidents came on top of the early part of the year which was fraught with uncertainty concerning the outcome of the Saddam/Bush conflict.

That was not all, however, as the loonie's flight added to difficulties like a ball on a chain. The contraction of our foreign trade accounted for a great deal; conversely, the current account surplus, in real terms, sank from \$56,212 million in 2002 to \$31,369 million in 2003. Of course, the weak US economy from the summer of 2002 to the spring of 2003 contributed as well, but the gains made by our currency against its US counterpart also played a pivotal role. Final domestic demand, i.e., the domestic economy, was not to blame since it posted growth of 3.6%, in 2003, beating its performance of 2.9% in 2002.

Continued on page 2...

DESJARDINS LEADING INDEX



Overview

Personal Bankruptcy: Challenges for individuals and society as a whole

Mathieu D'Anjou
Economist

Personal bankruptcy plays an essential role in a market economy by giving a second chance to consumers in financial difficulty. It would be unproductive to keep overwhelmed citizens indebted for the rest of their lives without any hope of recovering from it, thereby losing their incentive to work. It is much more efficient to give them a fresh start. However, it must not be forgotten that bankruptcies create losers. General creditors receive only a small fraction of what they are owed when there is a bankruptcy (2.1% in 2003 in Québec). If bankruptcies increase, the moneylenders will compensate their losses by increasing the interest rates they set on their loans. This increase in the cost of credit would penalize all borrowers.

Not only does it cause important economic consequences, but bankruptcy also involves a moral issue. In fact, the way in which we decide to treat people

Continued on page 7...

Financial Industries

2003, a remarkable year for the Desjardins Group

Danny Bélanger, Economist
Mario Couture, Senior Economic Advisor

In many respects, 2003 was a remarkable year for the Desjardins Group. This was particularly evident in such sectors as savings, financing offers, life and health, and property and casualty insurance protection as well as asset administration and management.

Regarding savings, we should mention that the upturn in the stock markets in 2003 seriously boosted savings products such as mutual funds and securities. These products, which gradually regained investor trust, bolstered the rise in financial wealth of Québec households.

As for financing activities, the demand in individual and business loan applications in Québec gained some ground in 2003. Household spending on durable goods, the growth in the construction sector combined with the new record set in the resale of existing homes and the recovery of business investments all had a hand in this trend.

Finally, the life and health, and property and casualty insurance sector also flourished in Québec in 2003. The administration and management of assets also benefited from the upturn in stock market indices.

Continued on page 9...

Report on Economic Climate

HIGHLIGHTS

United States

- ✘ In terms of growth, the US economy is reporting almost irreproachable performance that sets itself clearly apart from the other major industrialized nations, including Canada. Real GDP growth leapt by an annualized 6.1% in the second half of 2003.
- ✘ Job creation is still not achieving the expected results. The US economy began to generate jobs as late as September 2003, but average monthly job creation has been limited to 60,600 positions since then. Only 21,000 jobs were created in February.
- ✘ Nonetheless, we are predicting robust growth of real GDP at 4.4% in 2004 and 3.7% in 2005.

Canada

- ✘ The Canadian economy rebounded in the fourth quarter of 2003, an increase of 3.8% of real GDP, at an annualized rate.
- ✘ However, the thrust of this increase is attributable to a surge in inventories. Final domestic demand was greatly disappointing, rising by merely 1.2%, annualized.
- ✘ On another note, exports seem to finally be reacting to the vigorous economic growth in the United States, with an annualized growth of 13.5%. We are predicting 2.8% progression of real GDP for 2004, compared to 1.7% in 2003.

Québec

- ✘ Québec's economy experienced the same circumstances as those affecting Canada as a whole in 2003. However, the sustained rise in the Desjardins Leading Index since the summer of 2003 has market watchers anticipating better days for 2004.
- ✘ Residential and non-residential investment is poised to become the driving force of the economy in 2004. Québec companies' investment intentions are higher than in the rest of Canada, whereas housing starts experienced an excellent year's beginning, despite the cold snap.

A LOOK AHEAD

- ✘ Québec's Economic Accounts will be released on March 26.
- ✘ Two other things to watch for are the upcoming budgets of Canada and Québec, due to their potential impact on the economy and on the financial markets.

- Continued from page 1

All told, the situation is looking up for 2004. First, the year 2003 ended on a positive note: exports, in real terms, jumped by 13.5%, at an annualized rate, in the fourth quarter. That is a sign that our exports are apparently reacting to a US economy that has been going flat out since mid-2003, and that will keep to a brisk pace throughout 2004.

The Bank of Canada, having lowered its key lending rates four times since July 15, 2003, to thwart the adverse effect of the loonie's rise on the economy. The bank rate that had been cut to 3.5% was chopped further to 2.5% last March 2nd. In so doing, the Bank sought to attenuate the negative impact of the dollar's gains on foreign trade by stimulating domestic demand; this was a bid to bring economic growth as quickly as possible to its full potential. The idea was also to encourage the inflation rate to rise, which recently collapsed toward the mid-point of 2.0%. As the Bank's governor, David Dodge, said lately in Montréal, the central bank is seeking to ease the economy's adjustment to a higher dollar.

In addition, we have observed that the cut in key lending rates by the Bank of Canada has had the effect of slowing the loonie's flight. Indeed, the narrowing of the gap between Canadian and US short-term rates, kicked off by lower key lending rates, has curbed the inflow of foreign capital in Canada. In turn, this has offset the pressure pushing our dollar skyward. After having soared as high as US78¢ early in the year, the loonie recently fell back close to US75¢, and occasionally lower, at times. However, the downturn is not solely attributable to the central bank's cut in key lending rates, but also to the movements in the foreign exchange market on a global scale, particularly, the rally of the US dollar.

Therefore, what we must remember is that the cut in key lending rates has two broad effects: (1) stimulating economic activity; and (2) curbing the increase of the dollar. That is one card the Bank of Canada might play again during the spring if economic growth were to turn out to be below potential or if the loonie soared so high as to hinder the economic recovery expected in 2004.

According to our most recent forecasts, real GDP growth will rise to 2.8% in 2004, then dip to 3.6% in 2005, due, in particular, to highly accommodating monetary conditions and the vigorous expansion in the United States. Domestic demand will be driven by a dramatic jump in business investments that should double in size in an effort to adjust to the new high level of the dollar and in a bid to profit from the strong hike in raw material prices on the global markets. Our detailed forecasts for Canada and Québec will be released in the upcoming issue of this newsletter, toward April 20. ■

March 5, 2004

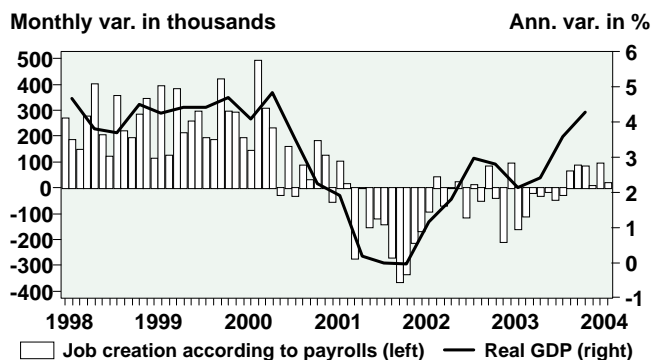
The US Economic Climate...

By Francis Généreux, Economist

Solid growth but low employment

Economic growth is still a factor in the United States. Real GDP was revised slightly upward for the last quarter of 2003, with growth now ringing in at 4.1%. In addition, the indices measuring manufacturing and non-manufacturing activity as well as the leading indicator are reporting signs that the next few quarters should deliver sound economic growth. Despite this, the labour market continues to be disappointing: only 21,000 positions were created in February while the forecast was for some 130,000 net hirings. If employment had progressed at the same speed as in recent economic recoveries, there would currently be 8,034,000 more jobs in the United States. We are still of the opinion that the job situation will soon be on the road to recovery. The ISM indices, regional manufacturing indices, weekly jobless claims, the number of announced layoffs, the demand for workers from temporary service agencies and the activity among retailers all indicate that robust job expansion should be just around the corner for our neighbours to the south.

UNITED STATES: ECONOMIC GROWTH AND JOB CREATION

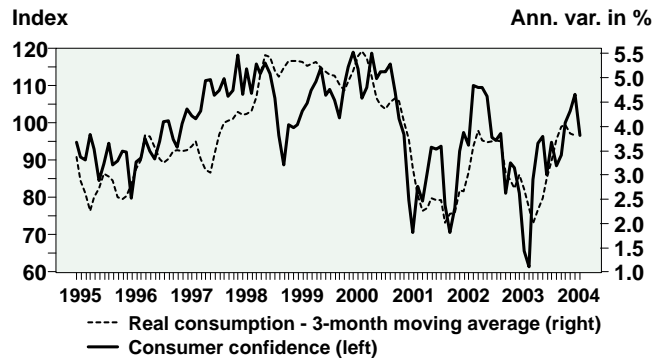


Sources: Bureau of Economic Analysis; Bureau of Labor Statistics; Desjardins, Economic Studies.

Dwindling consumer confidence?

Statistics on consumer confidence fell short of expectations in February. The indices of the University of Michigan and the Conference Board have declined by more than 9% since January. Over the short term, consumers' morale is linked to the employment trend, financial markets and the geopolitical context. January's figures might have been boosted due to the capture of Saddam Hussein on December 15, but the recently observed drop in the confidence indices is just too steep to be construed as a resumption of normal activity. Sluggish job creation no doubt also contributed to the drop in confidence, despite the solid performance of the stock market. However, the current confidence level is still in keeping with sound growth levels – but not outstanding – household consumption. Since the financial situation of households seems to be in good shape as Alan Greenspan commented recently, the job situation ought to pick up over the months ahead, and the optimism of households should eventually bounce back.

UNITED STATES: THE RECENT DROP IN CONFIDENCE WILL HAVE LITTLE IMPACT ON SPENDING

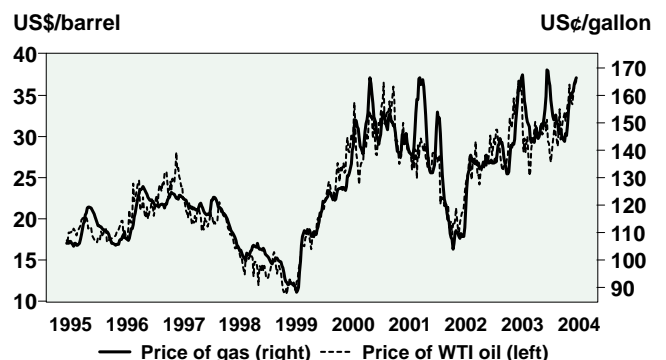


Sources: Bureau of Economic Analysis; Conference Board; Desjardins, Economic Studies.

Does the higher price of oil have an impact on consumption?

Among the factors that could spark worry among American households, the rising cost of energy, especially gas, is starting to be of some concern. The price of a barrel of oil lately came close to US\$36, and even US\$37. The price of gas at the pump reacted to the hike, and has soared by 14.5% since the beginning of the year. For the time being, the economic impact of the "energy tax" seems to be negligible, as long as consumption and retail sales are faring well. The tax cuts decreed in 2003 continue to boost households' disposable income and are able to offset the additional amounts allotted to energy products. But, if the price of oil keeps rising, it could end up having a noticeable effect on economic growth and gobble up some US\$60 billion, or close to 0.7%, of the annualized consumption of households.

UNITED STATES: OIL AND GAS PRICES



Sources: US Department of Energy; Datastream; Desjardins, Economic Studies.

The Canadian Economic Climate...

By Joëlle Noreau, Economist

Canada: Surprising fourth-quarter results

Real GDP grew by 3.8% (at an annualized rate) in the fourth quarter of 2003: this was the strongest growth rate of GDP recorded since the second quarter of 2002. Although on the surface these results seem to be good news, they do not hold up well to scrutiny. Most of the growth hinges on the increase in inventories and housing investment which are due to level off in 2004. What is more, domestic demand was anemic: it rose by a mere 1.2%, a direct consequence of the slower mode of households who kept their spending at the same level as in the third quarter. Real GDP will have spurred to 1.7% in 2003, a long shot below its American counterpart (3.1%). The year 2004 got under way with the following perspectives: a predicted rise in both exports and imports and an upturn in business investments. Simultaneously, we forecast that the flurry of housing activity will be maintained, with renovation making up for the slight fall-off in housing starts. The governments - like households - will continue to spend with moderation. Real GDP ought to register annual growth in the neighbourhood of 2.8% in 2004.

CANADA: REAL GDP AT MARKET PRICE

Annualized growth rate in %

	2003				Variation 2002 to 2003
	I	II	III	IV	
GDP	2.5	-1.0	1.3	3.8	1.7
Consumption	3.2	3.5	4.6	0.1	3.3
Res. construction	2.9	1.2	18.6	10.0	7.5
Bus. investment	9.5	2.3	15.0	2.1	3.5
Gov't spending	4.3	5.0	1.2	1.0	3.4
Final dom. demand:	4.1	3.5	5.8	1.2	3.6
Exports	-5.6	-3.1	-1.7	13.5	-2.1
Imports	3.8	5.4	-4.0	17.8	4.0

Var. of inventories

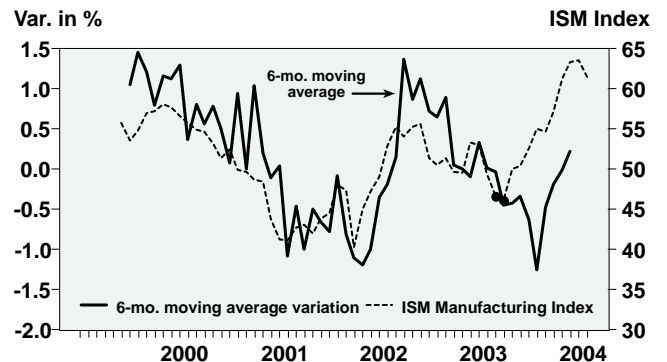
(in 1997 C\$ billions) 19,350 15,602 2,902 10,998 12,213

Sources: Statistics Canada; Desjardins, Economic Studies.

Will the manufacturing sector benefit from the upturn in the United States?

During the 1990s, in the favour of free trade (FTA and NAFTA) and the depreciation of the Canadian dollar, Canadian manufacturers' shipments progressed in sync with those of US industry. The strength of the Canadian dollar, the attenuating impact of NAFTA, the collapse of the information technology and communications sector, as well as fiercer competition from emerging nations are, to a certain extent, having the effect of loosening the tightly woven ties with American industries. Real Canadian manufacturers' shipments (1997\$) inched up by a paltry 0.4% in 2003. The dominant sector is transportation. The question is whether the slowdown observed in the automotive sector, in late 2003, will linger in 2004. In addition, the aeronautic sector is expected to gradually expand by late 2004. The primary processing of metals will be favoured by a boosted

CANADIAN MANUFACTURING SHIPMENTS & ISM INDEX: A TURNAROUND IN NEAR FUTURE?



Sources: ISM; Statistics Canada; Desjardins, Economic Studies.

world demand for industrial metals. However, certain sectors will experience difficulties that override the appreciation of the Canadian currency (i.e., pulp and paper, textiles, clothing, lumber). In all, the volume of manufacturers' shipments from Canada could expand to a spread ranging from 2.5% to 4% in real terms in 2004.

The Canadian dollar on a see-saw trend

After spectacular growth in 2003, the Canadian dollar has now embraced a waltz of hesitation since the outset of 2004. The rally of the US dollar against the major currencies and cuts in the key lending rates effected by the Bank of Canada in January and March resulted in the gap's narrowing between short-term US rates, and have taken pressure off the loonie. The monthly average value of our currency declined in February to US75.25¢, whereas it had reached US77.16¢ in January 2004. The decline cannot be taken for granted: the jolts in the currency are not over yet, since its movement is closely tied to the conduct of the US dollar on the international currency market. Furthermore, our central bank could intervene with another cut in the key lending rates over the spring, especially if the loonie were to rise again toward the US78 to 80-¢ spread. ■

CANADA: TREND OF CANADIAN DOLLAR



Sources: Statistics Canada; Bank of Canada.

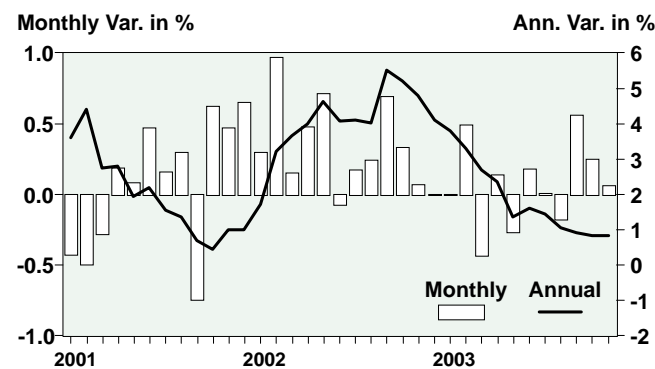
The Québec Economic Climate...

By Mathieu D'Anjou, Economist

More vigour at the end of 2003 for the Québec economy

Monthly GDP by industry in Québec recorded a third consecutive increase in November 2003. Growth in economic activity remains moderate but, due to a favourable base effect, the Québec economy should register annualized quarterly growth of approximately 3% in the last quarter of 2003. The boost in the Desjardins Leading Index (DLI) in the second half of 2003 was a hint that this acceleration in the economy would occur. The recent trend of the DLI remains positive and also points to strong growth in the Québec economy for the first half of 2004. However, risks remain and the recovery still needs to gain some speed, particularly in business and foreign trade, before we can conclude that the 2003 slowdown is definitely behind us.

QUÉBEC: 1997\$ GDP BY INDUSTRY

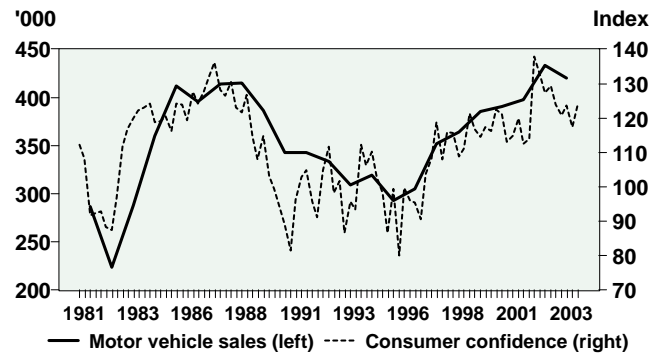


Source: Institut de la statistique du Québec.

Motor vehicle sales running out of steam at the end of the year

New motor vehicle sales dropped by 22% in Québec in December 2003 compared to the same month in 2002. The annual downturn for the fourth quarter was 15%. In spite of this disappointing year end, consumers purchased over 420,000 new vehicles in 2003, the second best year in the history of Québec. Sales only fell by 3.1% compared to their historic peak of 2002. The drop was twice as great for Canada, where motor vehicle purchases decreased by 6.2% in 2003. The excellent results of the last two years go hand in hand with the high confidence of Québec households. Very attractive incentives offered to buyers also contributed to the car craze. Motor vehicle sales should remain historically high this year.

QUÉBEC: MOTOR VEHICLE SALES

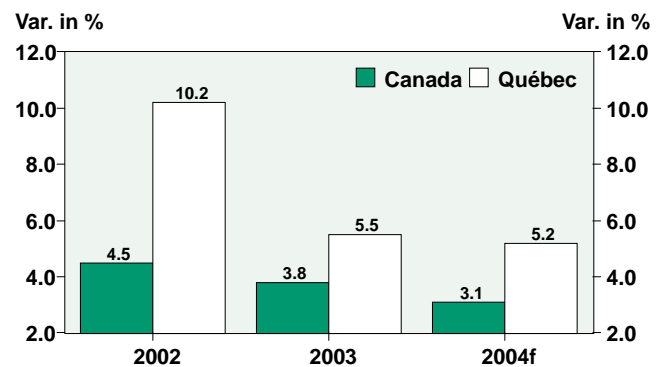


Sources: Statistics Canada; Conference Board.

Investment to grow in 2004

According to the Statistics Canada survey, the nominal value of investments should increase by 5.2% this year in Québec, a growth similar to that registered in 2003. These prospects include all investments, residential or not, private and public. Private investment should grow somewhat faster than public agency investment, contrary to the last four years where increase in public investment clearly dominated. After three years of spectacular growth, the increase in housing investment will slow to 6.7%. Investment in the manufacturing sector should experience a strong upswing (+16%). However, the hike will be almost exclusively attributable to the primary metal industry which is dominated by aluminum smelters. The postponement and the reassessment of certain projects (e.g., the Alcoa aluminum smelter in Baie-Comeau, the Gaspésia paper-making plant) could lead to somewhat weaker investment than forecast in the Statistics Canada survey. The rise in investment will slow to 3.1% in Canada. At first glance, the investment growth forecast may seem disappointing. However, nominal forecasts do not take into account the fact that the price of several

GROWTH IN INVESTMENT WILL REMAIN STRONGER IN QUÉBEC



Source: Statistics Canada.

The Québec Economic Climate

By Mathieu D'Anjou, Economist

investment goods experienced a significant decrease following the marked rise of the loonie in 2003. We can therefore expect that investments will significantly contribute, in real terms, to Canada and Québec's economic growth in 2004.

Inflation rate growing faster than earnings in 2003

The average weekly earnings of Québec workers grew by 1.9% in 2003 to reach \$656.76. This increase is superior to the 1.2% increase in Canada, but Canadian workers maintain higher weekly earnings of \$689.49. The growth in wages has not resulted in real enrichment for workers because the General Price Index, which is used to measure inflation, rose by 2.5% in Québec. Substantial rise in energy prices and cigarette tax hikes magnified the inflation rate in 2003. Price hikes are

QUÉBEC: RATE OF INFLATION AND WAGES



Source: Statistics Canada.



Desjardins
Economic Studies

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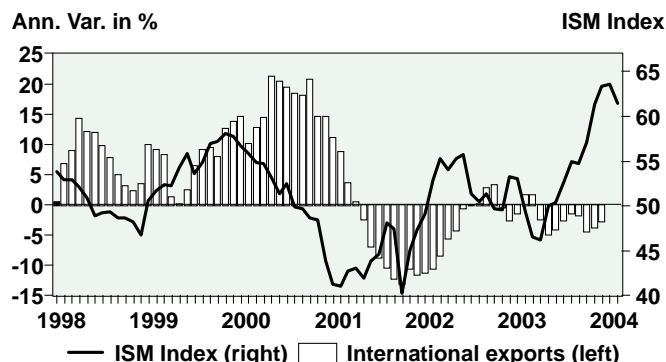
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QUÉBEC: EXPORTS COULD SEE RESUMPTION IN GROWTH



Sources: ISQ; Datastream.

expected to slow this year. Workers should therefore obtain a real increase in their purchasing power in 2004, especially since the high inflation rate of 2003 will surely weigh in wage negotiations.

Will Québec exports finally emerge from their state of lethargy?

The ISM Manufacturing Index in the United States continued growing to reach 63.6% in January 2004, a peak since December 1983, before dropping slightly in February. The US manufacturing industry therefore seems to be running at full speed. After a time, this usually results in a boost of Québec international exports. This would be welcome, as our foreign trade experienced another difficult year in 2003. The value of shipping outside Canada, in real terms, dwindled by 1.7%, a third consecutive annual drop, while our imports surged by 6.7%. This evolution, which is in part explained by the sharp appreciation of the Canadian dollar, practically erased our commercial surplus abroad. Québec's international trade surplus therefore dropped from \$5.6 billion in 2002 to only \$565 million in 2003. Fortunately, the worse seems to be behind us and our international exports increased in three of the last four months of 2003. This trend should become more marked this year, although the strength of the loonie will curb and somewhat delay the effects of the vigorous economic activity of the United States on our foreign trade. ■

Overview...

- Continued from page 1

who are bankrupt is necessarily incidental to the way we consider them as unlucky people whom we have to help or as those who are guilty whom we have to punish or, in the least, retrain. We can appreciate these different philosophies when we compare American laws that place the emphasis on a second chance and economic efficiency, and with European laws that are much more severe toward people who are bankrupt and that further protect the creditors.

This is a topic of current interest since the importance of household debt and the slight increase in bankruptcies in 2003 have many concerned that there will be a noticeable increase this year.

The Long History of Personal Bankruptcies in Canada

The first Canadian laws on personal bankruptcies date back at least 1843. However, there were very few people who were bankrupt up until the 1950s. Consumer credit was still rare during that time. Personal bankruptcies skyrocketed in the 1970s with an average annual increase of 23% in Canada during the whole decade. It progressed rapidly during the 1980s and 1990s at approximately 8% per annum.

In Québec, the number of personal bankruptcies went from less than 3,000 in 1976 to a peak of nearly 27,000 in 1997! The rising trend has stopped since, and the number of bankruptcies declined during four of the last six years. Despite a slight increase of 4% in 2003, the rate of personal bankruptcies in Québec remains down by 16% in relation to the peak of 1997.

Personal bankruptcies are slightly more frequent in Québec than in the rest of Canada.

The Canadian trend is quite similar to that of Québec; however, the decline in bankruptcies has been less apparent since 1997.

Personal bankruptcies are slightly more frequent in Québec than in the rest of Canada. There were three bankruptcies for every 1,000 inhabitants in Québec in 2003 compared to only 2.7 throughout the rest of Canada. Bankruptcies are much more common in the United States (5.3 for every 1000 inhabitants in 2002). Before the increase in the 1970s, there were only six bankruptcies for every 100,000 inhabitants in Canada.

When faced with this increase of personal bankruptcies, it became obvious that the rules relative to bankruptcies needed to be amended in order to simplify and render the process less expensive. Therefore, since 1992, there have been major changes made to the Bankruptcy and Insolvency Act (BIA). The ceiling of garnishable assets which permits access to the summary administration procedure was greatly increased and is now at \$10,000. This quick and inexpensive procedure is now used in more than 90% of personal bankruptcy cases.

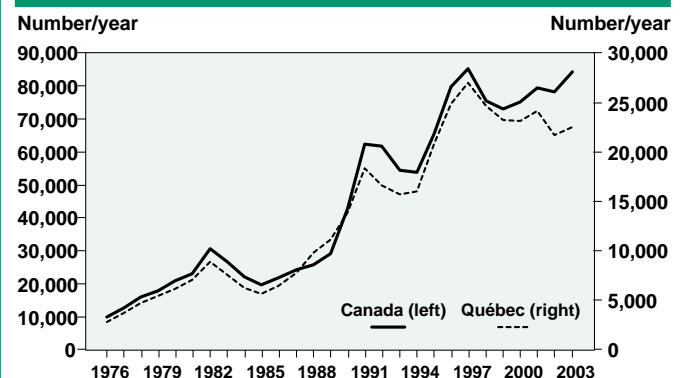
Since the changes in 1992, the BIA now also offers a new option to consumers who earn sufficient revenue. Instead of declaring bankruptcy, they can file a Consumer Proposal.

This provision allows the borrower to renegotiate a new arrangement with his/her creditors in order to extend the reimbursement period and/or reduce the amount of debt, thereby avoiding bankruptcy and preserving property that is protected by law as long as the terms of the proposal are respected. This provision is also advantageous to general creditors who can recuperate a slightly larger part of what is owed to them. The provision, having been unpopular when introduced, is now used in almost 15% of insolvency cases. It must be mentioned that since 1997, simple bankruptcy is less attractive, a consumer earning supplementary income, in other words more than what is needed to cover the basic needs of the family unit, can be refused discharge from bankruptcy after the normal period of nine months and is made to continue to reimburse a part of the debt.

Options for a Consumer in Financial Distress

1. *Renegotiate with the creditors.*
2. *Consolidation loan from a financial institution; hence, having only one creditor. It usually provides a lower interest rate and monthly payment.*
3. *Voluntary deposit: The consumer deposits the garnished part of his/her salary at the local courthouse that in turn uses it to repay the creditors. The consumer obtains a partial protection, its salary and moveable assets cannot be seized.*
4. *Consumer proposal: Renegotiation with creditors under the BIA. The consumer agrees to pay a monthly amount during a period that cannot exceed 60 months. If the creditors accept, all assets are protected and the affected debts are eliminated by the date of maturity.*
5. *Bankruptcy: A last-resort solution that consists of handing over all assets that can be garnished to a trustee who in turn uses them to reimburse creditors. In the case of a first bankruptcy, the person who is bankrupt will usually be discharged after nine months of all debts, save some exceptions such as student loans and payments due for support payments.*

SURGE IN PERSONAL BANKRUPTCIES



Source: Statistics Canada.

Overview

Who Becomes Bankrupt?

Two empirical analyses¹ were recently made in order to identify the characteristics of bankrupt Canadians. One of the goals of this study was to see if those who were bankrupt were really poor or unlucky consumers beyond their resources. In fact, many worry that bankruptcy could be used in an abusive manner by individuals who are financially better off or by irresponsible consumers.

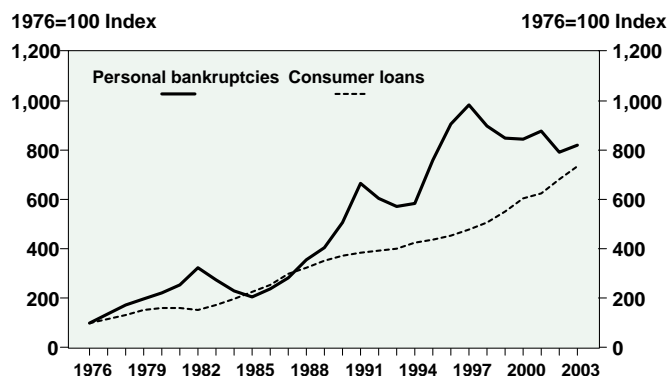
Generally, people who are bankrupt seem to live in a very difficult financial situation. Their median income is much below average, a large portion of them are unemployed, their debts are very high compared to their income and they possess very few assets. The main causes of bankruptcies are loss of employment, business failure and excessive debt.

What Factors Favour an Increase in Bankruptcies?

While it is interesting to study the individual characteristics of consumers who declare bankruptcy, it is much more useful for economists and financial institutions to study the broad economic variables that influence the total number of personal bankruptcies.

The level of debt and burden of the debt is certainly an important determinant of the number of personal bankruptcies. There cannot be bankruptcies without debt and it is not a coincidence if the increase in personal bankruptcies coincides with a sharp increase in consumer credit. Quebecers continued to rack up personal debts in 2003, consumer credit jumped 7.4%. The ratio of consumer credit to disposable income soared, from 18% in 1976 to 27% in 2003. This would indicate that the capacity to pay of Québec households did not increase as quickly as their loans. If we add mortgages, the rate of indebtedness reaches 87%. Even though this level is worrisome, it is still lower than the rate of Canadian and American indebtedness, which exceeds 100% of disposable income. Once the wealth of households is considered, the situation becomes less worrisome. In fact, Canadian household liabilities represented 18.5% of household assets in 2002, a level 1.2% higher than the average of the last 30 years.

QUÉBEC: GROWTH IN LOANS AND BANKRUPTCIES



Source: Statistics Canada.

QUÉBEC: BURDEN OF LOANS



Source: Desjardins, Economic Studies.

It is not one's indebtedness but the necessary payments that can push households over the brink into bankruptcy. The burden of borrowing is directly related to interest rates. For example, the monthly cost of a \$200,000, 25-year mortgage increases by \$375, almost 30%, when the mortgage rate rises from 6% to 9%. A quick hike in mortgage rates and consumer loan rates is often followed by a substantial increase in the number of bankruptcies. Due to low interest rates, particularly for mortgages, the burden of debt with respect to disposable income bottomed out in 2003 despite record debts.

The number of bankruptcies is also influenced by economic conditions since these affect consumers' capability to pay. In particular, job losses are often accompanied by a boom in personal bankruptcies. It is therefore useful to aptly examine economic conditions when we want to predict the trend in bankruptcies.

2004-2005 Perspectives

Personal bankruptcies should increase slightly this year in Québec. Québec households are vulnerable, given their heightened debt load. As well, the consequences of the economic slowdown in 2003 will continue to be felt. Meanwhile, the improvement in business conditions and the expected upward trend in job creation in 2004 will temper the rise in bankruptcies. The movement in interest rates will be a determining factor since an increase would directly translate into an increased burden of consumer debt. Happily, rates should remain very accommodating this year. However, interest rates cannot always remain so low and are expected to rise by the end of 2004 or in 2005 when the Canadian economy recovery becomes firmly established. If spending and saving habits do not change, a higher increase in bankruptcies could therefore become a concern by next year. ■

1. Schwartz 1999 and Ramsay 1999

Financial Industries...

- Continued from page 1

Personal savings: Notable growth in 2003

After experiencing a somewhat difficult period in 2002 from a financial perspective, Quebecers regained a certain level of prosperity in 2003. In fact, along with the great majority of investors around the world, Quebecers took advantage of the impressive rally in most stock markets. In Canada, the surge in stock market activity resulted in a vigorous 24.3% increase in the S&P/TSX Index on the Toronto stock exchange, compared to the 14.0% drop observed the year before.

Financial assets held by individuals in Québec increased by 8.9% (\$24.9 billion) in 2003, to settle at \$305.5 billion last December 31, whereas the assets had been stagnant one year earlier. This remarkable growth stems in large part from the strong increase in some investments, such as mutual funds and securities, to name but two. These savings products, which were heavily shaken by the stock market debacle in 2002, gradually regained investor confidence over the last year.

Mutual funds and securities were single-handedly responsible for nearly 78.0% of the increase in Québec households' financial wealth in 2003. They rose by 11.8% (\$19.4 billion), for a total of \$183.7 billion last December 31, compared to the 3.9% (\$6.6 billion) decline registered in 2002. We should mention that as recently as 1993, these savings products constituted only 28.2% of individual investment portfolios, while today, the proportion is twice as great. The search for more substantial returns to offset the low returns offered on more conventional products such as deposits (e.g. chequing accounts, regular GICs, etc.) is obviously related to the increased need for financial asset diversification which characterized the previous decade.

Faced with this new context, the Desjardins Group therefore has adapted the savings products it offered in order to more effectively meet the changing needs of its members and clients. On December 31, 2003, the in-force business of deposits, mutual funds, securities and of its Capital régional et coopératif Desjardins has accumulated over the years reached \$72.8 billion, up 11.5% (\$7.5 billion) in the last year, compared to the 5.8% (\$3.4 billion) rise observed in 2002. Thanks to a wide range of very competitive savings products, the Desjardins Group carved out a very enviable place for itself in the highly competitive Québec market; its market share was assessed at nearly 24.0% last year.

Thanks to a wide range of highly competitive savings products, the Desjardins Group has carved out an attractive position in Québec.

Individual and business loans in high demand

In spite of the serious downturn in the Québec economy in 2003, especially due to the drop in exports and the exceptional rally in the Canadian dollar, individual and business loan applications remained brisk. In fact, household's enthusiastic spending trend, the booming housing market and rising business investments helped maintain domestic demand on an even keel all while creating a most favourable economic climate for financial institutions.

Individual and business outstanding loans for all financial institutions in Québec rose by nearly 8.0% (\$14.4 billion) in 2003, to reach a volume of \$196.8 billion last December 31, compared to the 6.9% (\$11.8 billion) growth registered in 2002. As for the Desjardins Group, it was able to take advantage of this proliferation of business opportunities in several sectors. Its loan portfolio (excluding institutional credit) grew by 9.0% (\$5.2 billion), to amount to \$63.0 billion on December 31, 2003, compared to the 7.6% (\$4.1 billion) rise observed the year before. This loan volume corresponds to a market share of approximately 32.0% in the province of Québec, putting the Desjardins Group a long way ahead of its closest rivals.

The residential mortgage credit sector in Québec was in great demand in 2003. In fact, the housing market literally blasted through this period. Housing starts jumped by 18.5%, reaching 50,289 units, while the resale of existing homes set a new record of 71,880 transactions. On the other hand, this frenetic activity led to a large (15.8%) increase in the average sale price of homes.

The Desjardins Group is very involved in the financing of housing activity in Québec. The context was therefore quite favourable for business development in this sector in 2003. The Desjardins Group's residential mortgage loan portfolio amounted to \$35.7 billion last December 31, a 9.6% (\$3.2 billion) hike over last year, compared to the 8.4% (\$2.5 billion) increase observed in 2002. Due to these excellent results, the Desjardins Group increased its market penetration rate to nearly 38.0% in 2003.

Finally, the Desjardins Group's growth in consumer loans also improved in 2003, rising from 7.4% (\$772 million) in 2002 to 9.7% (\$1.0 billion) last year. What is more, its loan portfolio grew by 7.6% (\$805 million) in the commercial and industrial credit sector, reaching a total of \$11.4 billion last December 31, compared to the 3.3% (\$341 million) increase registered one year earlier.

Financial Industries...

PERSONAL SAVINGS ACTIVITIES

As at December 31, in M\$	2003			1998			1993		
	Chartered Banks	Desjardins Group	Total market ¹	Chartered Banks	Desjardins Group	Total market ¹	Chartered Banks	Desjardins Group	Total market ¹
ON-BALANCE SHEET PERSONAL SAVINGS²									
	56,502	53,064	121,833	45,473	42,416	102,374	47,310	38,489	106,447
• Market share (%)	46.4	43.6	100.0	44.4	41.4	100.0	44.4	36.2	100.0
OFF-BALANCE SHEET PERSONAL SAVINGS*, INCLUDING:									
	126,195	19,711	183,686	78,752	8,342	123,170	26,533	1,532	41,720
• Market share (%)	68.7	10.7	100.0	63.9	6.8	100.0	63.6	3.7	100.0
MUTUAL FUNDS ³									
	18,384	5,779	79,906	11,734	4,072	56,054	4,316	869	16,236
• Market share (%)	23.0	7.2	100.0	20.9	7.3	100.0	26.6	5.4	100.0
RETAIL BROKERAGE ⁴									
	107,811	13,552	128,217	67,018	4,270	85,886	22,217	663	30,787
• Market share (%)	84.1	10.6	100.0	78.0	5.0	100.0	72.2	2.2	100.0
SOCIAL INVESTMENT FUNDS									
IN VENTURE CAPITAL ⁵									
	0	380	5,312	0	0	2,809	0	0	829
• Market share (%)	0.0	7.2	100.0	0.0	0.0	100.0	0.0	0.0	100.0
ON- AND OFF-BALANCE SHEET PERSONAL SAVINGS*, INCLUDING:⁶									
	182,697	72,775	305,519	124,225	50,758	225,544	73,843	40,021	148,167
• Market share (%)	59.8	23.8	100.0	55.1	22.5	100.0	49.8	27.0	100.0
RRSPs ⁷									
	46,386	23,133	100,607	32,487	16,856	74,617	19,453	11,596	44,358
• Market share (%)	46.1	23.0	100.0	43.5	22.6	100.0	43.9	26.1	100.0

* : Double-counting taken into account by subtracting, from the total market, mutual funds sold through securities brokerage firms. Here are the amounts subtracted: \$29,749 million in 2003, \$21,579 million in 1998 and \$6,132 million in 1993.

FINANCING ACTIVITIES

As at December 31, in M\$	2003			1998			1993		
	Chartered Banks	Desjardins Group	Total market ⁸	Chartered Banks	Desjardins Group	Total market ⁸	Chartered Banks	Desjardins Group	Total market ⁸
CONSUMPTION									
	22,901	11,676	43,479	15,693	9,344	30,007	12,994	7,018	23,690
• Market share (%)	52.7	26.9	100.0	52.3	31.1	100.0	54.9	29.6	100.0
HOME MORTGAGES									
	48,854	35,659	94,692	36,007	27,838	74,888	26,328	25,257	64,200
• Market share(%)	51.6	37.7	100.0	48.1	37.2	100.0	41.0	39.3	100.0
COMMERCIAL & INDUSTRIAL									
	24,948	11,367	48,283	24,985	9,875	45,925	22,722	9,090	44,869
• Market share (%)	51.7	23.5	100.0	54.4	21.5	100.0	50.6	20.3	100.0
FARM									
	3,932	4,307	10,299	2,463	2,586	6,354	1,388	1,760	4,029
• Market share (%)	38.2	41.8	100.0	38.8	40.7	100.0	34.5	43.7	100.0
TOTAL									
	100,635	63,009	196,753	79,148	49,643	157,174	63,432	43,125	136,788
• Market share (%)	51.1	32.0	100.0	50.4	31.6	100.0	46.4	31.5	100.0

Financial Industries...

INSURANCE ACTIVITIES (premiums underwritten⁹)

LIFE AND HEALTH INSURANCE	2002		2001	
	M\$	%	M\$	%
Main companies				
Desjardins Group	1,314	16.1	1,171	16.3
Sunlife of Canada	1,109	13.6	500	6.9
Industrial Alliance	839	10.3	732	10.2
SSQ Life	672	8.2	568	7.9
Great West	657	8.1	648	9.0
Standard Life	641	7.9	333	4.6
Manulife	481	5.9	344	4.8
Maritime Life	391	4.8	321	4.5
Canada Life	340	4.2	309	4.3
La Capitale Assurances MFQ	260	3.2	236	3.3
Subtotal	6,704	82.2	5,162	71.7
Banks	229	2.8	208	2.9
TOTAL	8,159	100.0	7,200	100.0

PROPERTY AND CASUALTY INSURANCE	2002		2001	
	M\$	%	M\$	%
Main companies				
ING Canada	993	16.0	779	14.4
Desjardins Group	728	11.7	649	12.0
AXA Canada	555	8.9	512	9.5
Aviva Canada	431	6.9	413	7.6
Promutual Group	364	5.9	324	6.0
Groupe Co-operators	250	4.0	220	4.1
La Capitale	244	3.9	213	3.9
AIG	212	3.4	133	2.5
Lloyd's	199	3.2	201	3.7
Fairfax	184	3.0	141	2.6
Subtotal	4,160	66.9	3,585	66.2
Banks	112	1.8	119	2.2
TOTAL	6,214	100.0	5,417	100.0

Notes and sources
M\$ Millions of dollars

1. The total market includes other financial institutions not affiliated with the banks or the Desjardins Group, i.e. trust companies, life and health insurance companies, mortgage loan corporations, mutual fund promoters and independent brokers.
2. Including the savings of individuals transferable by cheque, non-transferable by cheque, term savings (including stock-market linked savings), government savings products, individual registered and non-registered annuities, and group RRSPs/RRIFs from life insurance companies.
3. Market results include all the mutual funds listed by the ISQ and the segregated funds estimated using data from CLHIA and Morningstar Canada.
4. The market results are estimated and include all the assets in safekeeping on behalf of individuals at securities brokerage firms, including the amounts they have invested in mutual funds.
5. This category encompasses the assets of the Fonds de solidarité de la FTQ, FondAction CSN, and Capital régional et coopératif Desjardins.
6. With the exception of banks and the Desjardins Group, the total excludes the mutual funds sold by securities brokerage firms.
7. The results of the banks and of the market are estimated and include conventional and self-administered RRSPs/LIRAs.
8. The total includes, in addition to the institutions set out in Note 1, financial corporations, chain stores, the Caisse de dépôt et placement, the CMHC, the SHQ, the Business Development Bank of Canada, Investissement Québec, Farm Credit Canada and La Financière agricole du Québec.
9. Direct underwritten premiums.

Sources: Bank of Canada, Statistics Canada, Institut de la statistique du Québec (ISQ), the Superintendent of Financial Institutions, the Inspector General of Financial Institutions, Investment Funds Institute of Canada, Morningstar Canada, Canada Mortgage and Housing Corporation, Journal Les Affaires, Investor Economics Inc., Canadian Life and Health Insurance Association and the Fédération des caisses Desjardins du Québec.

Life and Health Insurance: Dominated by a Handful of Heavyweights

The direct premiums collected by life and health insurance companies amounted to nearly \$8.2 billion in 2002, a 13.3% jump over 2001 when they had risen to \$7.2 billion (+8.2%). It is difficult to flesh out a portrait for the year 2003, as the final data will be published only during the summer of 2004. However, to judge by the trend set in Canada, the Québec industry will likely record bolstered growth in the neighbourhood of 14.0%, or approximately \$9.3 billion.

In 2002, the stellar expansion of premiums underwritten for annuities (+48.7%) was considerably favoured by savers turning toward products that offered both guaranteed capital and an assured rate of return. This brisk expansion proved to be to the detriment of segregated funds, which had been given a rough ride in years past. In 2003, despite the improvement in the stock markets, the net sales of segregated funds registered \$1 billion, down from 2002 (\$1.3 billion), and a far cry from the level reached in 2000: \$5.6 billion¹.

Competition among insurers remains fierce, especially in the group insurance sector. In 2002 in Québec, there were 131 companies specialized in life and health insurance, and five others which had business in property and casualty insurance as well. Of those firms, which shared some \$8 billion in insurance premiums and annuities that year, there were a handful of heavyweights and a host of small companies.

The concentration of just a few firms is manifest in the fact that the ten largest life and health insurance companies collected as much as 82.2% of the premiums in terms of life and health insurance as well as annuities. Among the heavyweights, the Desjardins Group, through its subsidiary Desjardins Financial Security, still topped first place, with a relative market share of 16.1% and a volume of premiums of \$1.3 billion. SunLife and Great West² followed, with respective market shares of 13.6% and 12.2%. Finally, the tandem Maritime Life and Manulife Financial were to corner 10.7%, if the merger went through as scheduled.

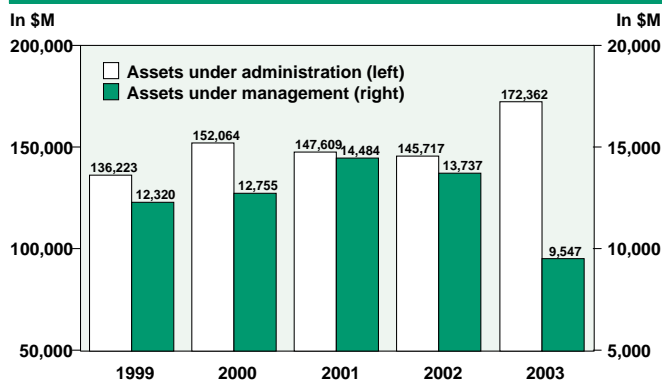
Financial Industries

Property and casualty insurance: Sustained growth

Property and casualty insurance also reported outstanding results for 2002. The premiums underwritten by firms in the field amounted to \$6.2 billion, a gain of \$14.7% over 2001 (+10.6%). For 2003, the Canada-wide trend leads us to believe that the Québec market will also profit from this upturn. The amount of premiums collected has apparently jumped by close to 11.0%, reaching \$6.9 billion. The economic slowdown, fuelled to a great extent by dwindling exports, does not appear to have dampened Québec household confidence.

As an illustration, a remarkable upswing was observed in the Québec housing market in 2003. The resale housing market reached a new peak of 71,880 transactions, whereas housing starts soared to 50,289 units, a level not seen since 1988 (58,062 units). In another sector, the new automobile sales were down slightly over last year, settling at 420,185 cars sold;

ASSETS ADMINISTERED AND MANAGED BY DESJARDINS GROUP



Source: Desjardins, Economic Studies.

this is the second highest peak witnessed in Québec. It does not come as a surprise, therefore, that property and casualty insurers had a flurry of activity as well in 2003, especially since close to 60% of the premiums collected had to do with motor vehicles on the one hand (40%), and housing on the other (20%).

Let us close in stating that the concentration of this sector is not as great as that of the life and health insurance sector. Comparing the two, the ten largest insurance companies collected approximately 67% of the premiums paid in 2002. At that time, the Desjardins Group, through its Québec subsidiaries Desjardins General Insurance and The Personal General Insurance, came in second, cornering a market share of 11.7%. It was outclassed by the European giant, ING (16.0%).

Administration and management of assets: A sigh of relief

The stock market recovery of 2003 (i.e. S&P/TSX closed up by 24.3%), was met with a sigh of relief by firms active in the industry of asset administration and management. In Canada, for instance, according to a study conducted by Mercer, pension funds enjoyed their best returns in 2003 since 1997. In the case of mutual funds and securities brokerage, assets grew by 12% and 17%, respectively³.

The presence of the Desjardins Group in these fields of activities is assured through its subsidiaries, Desjardins Specialized Financial Services Management, Desjardins Securities, and Desjardins Asset management. The assets it administered and managed for others soared by 18.3%, to reach \$172.4 billion at December 31, 2003, as contrasted by a 1.3% drop in 2002. ■

1. Source: Investor Economics Inc.

2. Including Canada Life

3. Sources: The Investment Funds Institute of Canada (IFIC) and Investor Economics Inc.

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