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CANADA

Household debt hits a new peak

Canadian households continued to take on debt in Q4 2014. The ratio of their credit market debt to disposable income rose to 163.26%, a level not seen since 1990 when the statistic was first compiled. The problem remains the same, which is debt growth (especially mortgage debt) that is faster than income growth.

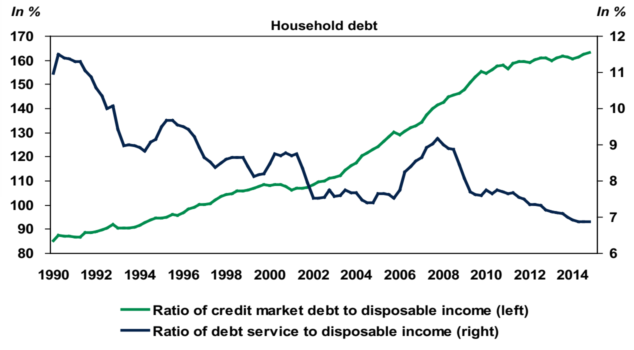
For now, the situation is not alarming, as debt service (interest payments made on loans) remains at a historic low. This observation is a little paradoxical given that the size of the debt is at a peak, but it is due to the very low interest rates. According to our estimates, the average interest rate on all household loans is falling steadily, going to 4.33% in Q4 2014, its lowest point since 1990. Given that the Bank of Canada ordered a key interest rate cut in January, everything suggests the downtrend will persist for a while, simultaneously favouring further increases in household debt loads.

The main concern with the debt load is that interest rates will slowly go up at some point, a situation that could lead to a fairly rapid rise by Canadians' financial obligations.

That being said, the financial picture of households is less bleak when we look at it through other lenses. For example, owner's equity as a percentage of real estate is not only close to its historic average, it is also much higher than the equivalent metric in the United States.

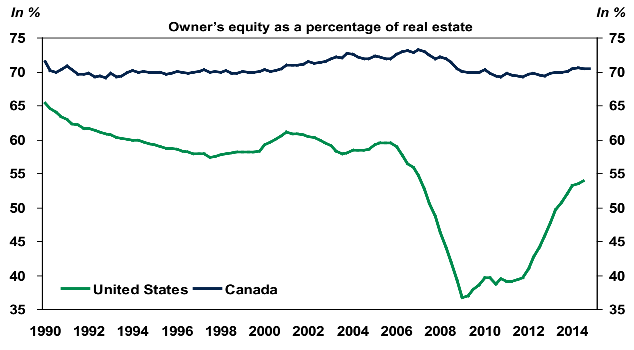
Implications: It will eventually take an interest rate increase to deal with the financial stability problem created by household debt. However, the increase will have to be very gradual to minimize its impact on households' financial obligations. This kind of adjustment is unlikely in short term, given the negative impacts the slide by oil prices will have on Canada's economy. Moreover, the possibility of another key interest rate cut cannot be completely ruled out. It will likely be 2016 before we see interest rates start to rise.

Low interest rates reduce the debt service ratio



Sources: Statistics Canada and Desjardins, Economic Studies

Canadians have more equity in their properties



Sources: Statistics Canada, Federal Reserve Board and Desjardins, Economic Studies

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