

The financial situation of Quebec households The picture differs widely with borrower age

Household debt loads have shot up in the last 15 years in Quebec.¹ The value of assets has also grown steeply, with the result that the debt/asset ratio has not fluctuated much, a sign that, overall, borrowers remain in relatively good financial shape. Beyond the broad picture, are households in some age brackets in shakier financial position than they were? Has the position worsened more for young people, or older households? For those under 35, debt levels have skyrocketed, going up more steeply than their assets. Their situation is not necessarily alarming, but greater vigilance is required, as about 20% are in the financial discomfort zone. Even the debt of households over 65 has gone up. Many more are resorting to debt than were 15 years ago. One thing is certain, debt profiles and asset accumulation differ widely depending on the age group.

¹ Economic Viewpoint "Update: Quebec households' financial situation - Debt and asset value have both increased over the last 15 years," May 9, 2016. <https://www.desjardins.com/ressources/pdf/pv160509e.pdf?resVer=1462554278000>

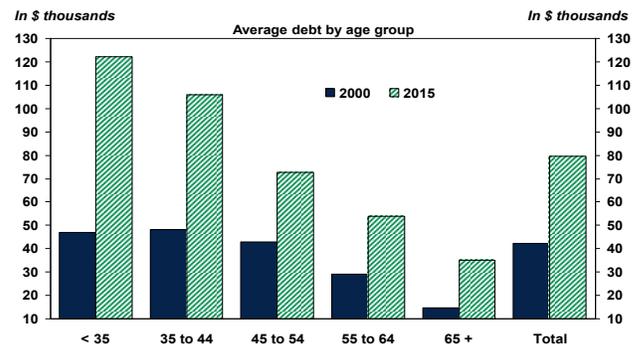
DEBT IS RISING FOR EVERYONE

According to the data compiled from the Ipsos Reid survey for Quebec, debt² for all households averaged around \$40,000 in 2000, then slowly climbed to nearly \$80,000 in 2015. Debt has increased in all age categories, but has risen more steeply among young people (graph 1). For households under age 35, borrowing was around \$50,000 on average 15 years ago, and had risen to nearly \$125,000 last year. Two key factors explain the strong growth. One is that skyrocketing home prices have inflated the value of mortgage loans, particularly for first-time buyers. The second is that low interest rates and the flexible terms on loan insurance in the 2000s have made it possible for many young households to buy homes. Fifteen years ago, the average debt was similar for those under 35 and those aged 35 to 44. That is no longer the case. Young households now have higher debt loads due to the strong shift toward ownership.

Those under 35 usually have the lowest income at the time their debt is peaking. Debt declines with repayments and incomes go up over time, so that the debt load usually

² Household debt breaks down into residential mortgages, various types of personal loans, lines of credit, credit cards and car loans (including leasing).

Graph 1 – Change in indebted households' average debt in Québec

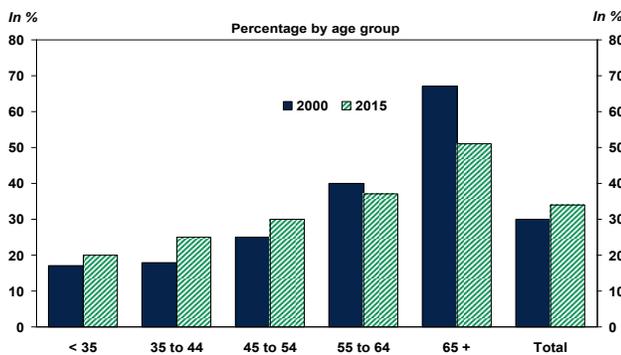


Sources: Ipsos Reid and Desjardins, Economic Studies

drops with age. Average debt is around \$100,000 for 35- to 44-year-olds, then slides to around \$70,000 for those aged 45 to 54. For households aged 65 and older, average debt is the lowest of all the groups, at around \$35,000.

This age group also has the largest share of households with no debt at all (box 1). Half of households 65 and up do not borrow (graph 2). The proportion is much smaller than it was 15 years ago, when close to 70% of this group had no debt to pay off. Some households in this age group, which took advantage of the low interest rates of the last few years to buy a more expensive home or even purchase a secondary residence, have thereby extended their payment periods. They may not necessarily have the income to pay off their loans in full. The fact remains that a growing proportion of households 65 and older have accumulated debt in the last 15 years.

Graph 2 – Indebted households' proportion in Quebec

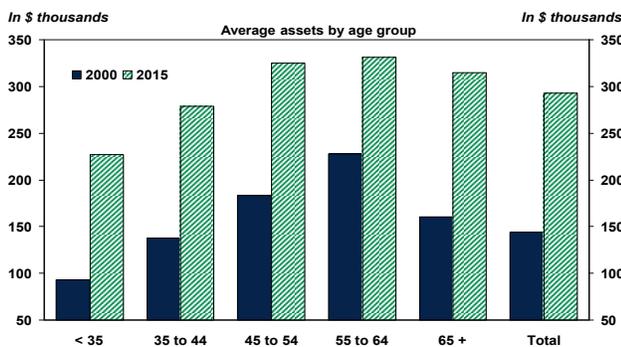


Sources: Ipsos Reid and Desjardins, Economic Studies

ASSETS HAVE ALSO CLIMBED, REGARDLESS OF AGE

The fact that debt has risen in all age groups is not enough to determine whether their relative financial vulnerability has increased over the last 15 years. If the debt load has risen with a concomitant increase in the value of assets³ in each group, their respective financial standing has not

Graph 3 – Change in indebted households' average



Sources: Ipsos Reid and Desjardins, Economic Studies

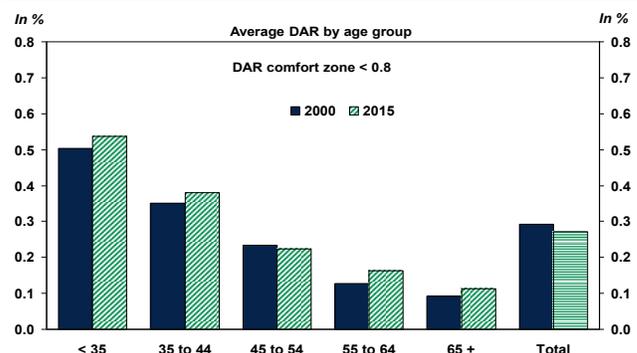
³ Assets include both financial and non-financial assets, such as homes, cars, furniture and personal property. Financial assets³ can be held as chequing and savings accounts, as well as by investment type (bonds and other guaranteed investments, mutual funds and equity).

BOX 1 : SOME HOUSEHOLDS AVOID DEBT

While the spectre of debt looms over many households, others have nothing to worry about. According to the Canadian Financial Monitor survey, about one third of Quebec households have no debt. This group includes households with no credit products, and households that use credit products but systematically pay off their monthly balances (this essentially applies to those with credit cards or personal credit lines). In principle, households that have no loans or that borrow in a very disciplined way are not vulnerable. In general, these are people who are at a later stage in their lives. Half of households over 65 have no debt, while close to 40% of the 55 to 64 group are in this situation. At this point, many homeowners have already paid off their mortgages, wrapping up the borrowing period. Conversely, young debt-free households usually rent, or are still living at home. Only 20% of households under 35 do not borrow, with the result that 80% have loans to pay off. At this stage in life, incomes are usually less than expenses, and buying property, along with various goods such as furniture, helps boost financing. Although a proportion of Quebec households is debt free, particularly older households, the average value of loans presented in this Economic Viewpoint concerns those that are carrying debt.

necessarily worsened. In the case of young people under age 35, their assets were worth an average of about \$95,000 in 2000, and are now above \$225,000 (graph 3). The change in the asset level has not been as steep as that in the debt level, so that the debt-to-asset ratio has increased slightly, as with most other age groups (graph 4). Households under 35 are still more vulnerable than the others: their incomes are relatively low at a time when their debts generally exceed their assets. This is consistent with the first phases of the financial life cycle.

Graph 4 – The debt-to-asset ratio (DAR) of indebted households



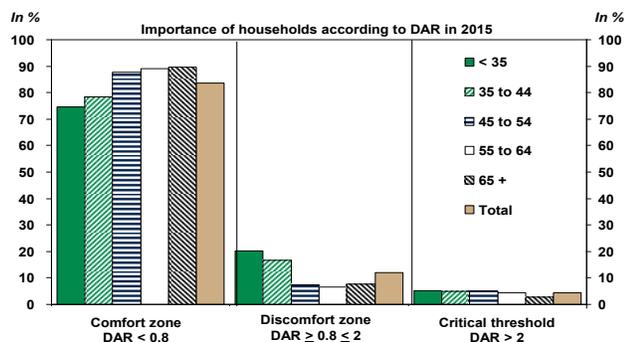
Sources: Ipsos Reid and Desjardins, Economic Studies

The biggest accumulation of assets comes in the group aged 65 and older. In 2015, in that group, financial and non-financial assets totalled \$315,000, almost double the level 15 years before. Of course, these households are well along in their life cycle (box 2), a situation usually characterized by a substantial accumulation of assets and low debt loads. Unsurprisingly, seniors are in a much stronger financial situation than other age groups.

Although debt has risen since 2000, the average debt-to-asset ratio of all age groups is well below the 0.8 or 80% threshold that Statistics Canada labels as high. The indicator, which measures the degree to which households assets can cover debt, can also be associated with a discomfort zone ($DAR \geq 0.8$ and ≤ 2), and an insolvency threshold ($DAR > 2$). According to the statistics on insolvency, consumers who declare bankruptcy or make a proposal to creditors to settle their debts usually have twice as much debt as assets. However, households in this situation are not all struggling financially.

Beyond the general average debt-to-asset ratio trend, it is its distribution of households by three risk zones that helps better pinpoint the proportion of households that may not be able to meet their financial obligations (graph 5). Nearly 85% of all indebted households had sufficient assets to cover their loans in 2015 ($DAR < 0.8$). The percentage is 90% for the 65 and older age group. Conversely, only 75% of young households are in the financial comfort zone. More households under 35 can therefore be found in the discomfort zone ($DAR \geq 0.8$ and ≤ 2), about 20%. In most other age groups, that figure is under 10%. Lastly, about 5% of households are in the critical zone ($DAR > 2$), regardless of the age group.

Graph 5 – Distribution of indebted households by age group according to debt-to-asset ratio (DAR)

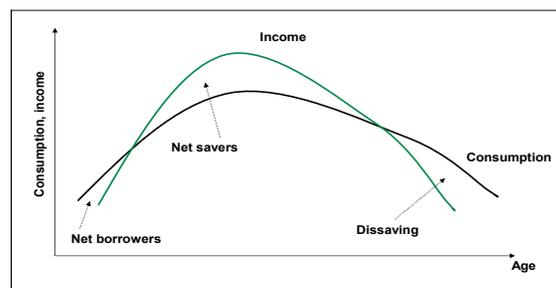


Sources: Ipsos Reid and Desjardins, Economic Studies

BOX 2 : LIFE CYCLE AFFECTS THE FINANCIAL PICTURE

Households' financial profiles, i.e. the picture for savings, borrowing and consumption, varies enormously based on age (graph 6). Young households usually turn to loans to build wealth, as their expenses generally exceed their incomes. In relation to assets, the debt load is usually heavier for households under age 35 than it is for other age groups. At this stage in life, mortgage loans are relatively high and, often, education loans are still on young households' balance sheets. Over time, individual income rises and exceeds expenses, making it easier for them to save. People of a certain age consume less, but their incomes drop substantially as their capital is gradually depleted. Life cycle therefore influences households' financial situations, which is also reflected in the various indicators presented in this Economic Viewpoint. We can therefore expect young households to be characterized by some financial shakiness, which decreases with age, in step with the various stages of life. However, regardless of the age group, a proportion of households is likely to experience financial difficulties.

Graph 6 – Life cycle of households' financial situation



Sources: Organisation for Economic Co-operation and Development and Desjardins, Economic Studies



CONCLUSION

In short, the financial situation of households that are carrying debt varies with the age group. Those under age 35 do, of course, have a more fragile financial picture, given that their debt-to-asset ratio is higher than other households. About 75% of people under age 35 are in a comfortable financial position, compared with 85% for all households. As a result, the weight of households likely to fail to meet their financial commitments declines as of age 35. Overall, there is less concern over the financial situation of older households. More vigilance is required for young people, as the risk of financial difficulties is clearly greater. These findings for Quebec match Statistics Canada's for Canada as a whole, and the OECD's findings for the major industrialized countries.

The bigger debt load a household has, the more vulnerable it is to events that could affect the value of its assets (box 3). A sudden, ongoing drop in the value of assets, such as a plunge in home prices or sharp stock market correction, could erode the financial situation of some households.

BOX 3: RISKS THREATEN SOME HOUSEHOLDS

Households with high debt loads generally have a more trouble-free financial picture: higher income or substantial savings that lessen the spectre of excess debt. This is a broad picture, however, and some households are still at risk of defaulting on payment in the event of an economic shock. An economic contraction that would shake up the job market and residential real estate market is a threat. Other situations, such as a serious illness or job loss that could affect the income of the affected household, could lead to a deterioration in the personal financial situation.

A sudden rise in interest rates could also trigger financial problems by making the debt load heavier. A recent *Economic Viewpoint*⁴ assessed the impact of an increase in the cost of borrowing on vulnerable households. This risk has since dissipated, at least for the immediate future. The gloomier global economic outlooks will prompt central banks to maintain low key interest rates, which will keep medium- and long-term rates low.

⁴ Economic Viewpoint "Simulation results: How vulnerable are Quebecers to an interest rate increase?", June 2, 2016. <https://www.desjardins.com/ressources/pdf/pv160602e.pdf?resVer=1464875179000>

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