How Canadians Are Faring in the Recession

The seemingly constant flow of bad economic news — job losses, stock market downturns, business closures, and personal and corporate bankruptcies — since the second quarter of 2008 can't leave anyone in doubt that Canadians in all provinces, all economic sectors, and all age groups have been hit hard by the current recession. For the most part, most of that economic news has focused on industries or provinces as a whole, but a recent Statistics Canada study provides insight into how the recession is affecting Canadians at an individual and family level.

The StatsCan report, which is available on the Agency's Web site at http://www.statcan.gc.ca/daily-quotidien/090316/dq090316a-eng.htm, looked at changes in the net worth of Canadian households for the fourth quarter of 2008 (October to December inclusive). Not surprisingly, that net worth declined by an average of 4.4%, lowering average household net worth from $179,300 in the second quarter of 2008 to $165,300 in the fourth quarter. The fourth-quarter decline followed a similar result for the third quarter of 2008, and StatsCan noted that the 4.4% drop was the largest quarterly drop recorded since 1990.

The drop in household net worth was driven more by a decline in the value of household assets (down by 3.2% in the fourth quarter) than by any increase in household debt. Notwithstanding this, Canadians continue to borrow, with the credit market debt of households increasing by 1.7% during the fourth quarter. Not surprisingly, in a quarter where the Canadian stock market dropped by 24%, most of the decline in household asset value was driven by losses attributable to financial assets.

Debt-to-income ratio measures the amount of current after-tax income required to eliminate one's debt, and the debt-to-income ratio of Canadians, which has risen by more than 50% since the 1990s, continued to do so as of the end of 2008. However, while Canadians continued to take on more debt relative to their income, the actual cost of servicing that debt (relative to income) has declined over the past five years with the decline in interest rates. Specifically, the debt service ratio, which stood at a high of 10% in the early 1990s, dropped to a low of 6.5% in 2004 and stood, as of the end of 2008, at 7.9%. The StatsCan report suggests that one of the reasons that Canadians were willing to let their debt grow so dramatically was that there was an equally dramatic decline in the cost of servicing that debt over most of the past two decades. In other words, while the debt held by Canadian households continued to grow each year, their overall cost of borrowing did not, perhaps obscuring to some degree the extent to which households were leveraged.

The final measure considered by StatsCan in its analysis was the ratio of debt to net worth for Canadian households. While that ratio has remained relatively stable over the past two decades (ranging from 22% in 1990 to 19% in 2000), it hit a high of 25% as of the end of 2008. While the relative stability of this measure suggests that asset growth has largely kept pace with the growth in liabilities taken on by households, the recent increase to 25% reflects the decline experienced during 2008 in average household net worth.

As the financial pundits continue to remind everyone, stock markets have always bounced back, the value of real estate invariably increases over the long term, and recessions always come to an end, eventually. What remains to be seen is whether the lessons learned from the current economic crisis, particularly in relation to the consumption and debt-acquisition patterns that contributed to it, will be remembered after the crisis is over.