$1.41 trillion in debt – and counting (June 2010)

A number like $1.41 trillion is hard for most Canadians to grasp, and many Canadians would be surprised to find that that figure represents the total debt of Canadian households as measured in the month of December 2009.

In each of the last three years (the spring of 2007, the winter of 2008 and December 2009), the Certified General Accountants Association of Canada has carried out a consumer survey and analyzed the results with respect to the amount and character of debt held by Canadians, and their perceptions of that debt. While each of those three years represented very different economic times, ranging from the economic good times of 2007 to the early part of the "Great Recession" in 2008 and the recovery which began emerging in 2009, the results from each year all share one feature – the increasing use of debt by Canadian household to meet living costs. And, while the trend of an increasing debt load is a concern in and of itself, that concern is heightened by the fact that the interest cost of carrying that debt is likely to increase in the next few months.

In addition to the increasing level of debt (which reached a record debt-to-income ratio of 144.4% at the end of 2009, up from 107% at the beginning of 2005), the CGA report identified a number of aspects of the character of that debt, which gives rise to concern. The following issues were identified in the Executive Summary to the 2010 report:

- The increase in household debt over the last couple of years has not been spread equally across all types of debt. Specifically, while during 2008-09 the growth rate of mortgages and other types of credit secured by an underlying asset slowed, the pace of expansion of consumer credit (represented for the most part by unsecured lines of credit and credit cards) accelerated over the same period. The growth in unsecured lending has been such that the overall share of debt represented by revolving credit (again, personal lines of credit and credit cards) within total consumer credit increased from 21.1% in 1989 to 77.7% in 2009. Borrowing through personal lines of credit, in particular, increased 25 fold over that time period.

- Also of concern is the fact that much of that unsecured debt, on which the interest rate charged is almost always a variable rather than a fixed rate, was taken on during a period of extremely low interest rates. In fact, the study notes that the exposure of Canadian households to rising interest rates has increased generally with an overall increase in the level of variable rate debt. The proportion of household debt with a variable rate increased from 14% in 1997 to 25% in 2007, and that proportion is even greater when mortgages are included in the calculation. In 2009, just over one quarter (27%) of mortgages had variable-rate terms, while another 6% had a combination of variable and fixed rates. The study's authors concluded that, should the mortgage interest rate go up by two percentage points, middle income and mid-to-high income Canadian households could be required to cut about 10% of their spending on other day-to-day expenses.

- While Canadian families may, in the near future, be facing a need to cut back in other areas in order to meet increases in debt repayment obligations, it's clear that many Canadians just don't have much room to maneuver. The survey showed that, even with access to credit cards and lines of credit, one-quarter of Canadians would not be able to handle an unforeseen expenditure of $5,000, and one-tenth of Canadians would have trouble meeting an unanticipated expense of just $500.

- Given the foregoing, it's perhaps not surprising that savings have not been a priority for Canadians during the last couple of years. One-third of Canadians who had not yet retired indicated that they had not committed any resources to any type of regular savings, including retirement savings. By comparison, in 2007, one-quarter of Canadians reported that they had no regular savings plan. As well, the fact that savings for any purpose can now be accumulated on a tax-free basis through a tax-free savings account or TFSA, doesn't seem to have made a difference. Of the approximately two-thirds of Canadians who are familiar with TFSAs, more than half did not make use of them (although in a previous year's survey, nearly two-thirds thought that they would.)

The CGA's executive summary of the results of the 2009 survey and analysis characterized the trends revealed by those results as "worrisome". Just how worrisome those trends are will likely become apparent once interest rates start to rise later this year.

The full CGA report, entitled "Where is the Money Now: The State of Canadian Household Debt as Conditions for Economic Recovery Emerge" can be found on the Association's Web site at http://my.texterity.com/cgaresearchreports/debt2010#pg1.