Canada: Insolvencies Fall in August Following July's Spike

- **The total number of Canadian insolvencies came down in August by 8.3% m/m sa after July's spike to levels last seen in 2009 following the outbreak of the global financial crisis**
- **Consumer insolvency volumes declined from the previous month by 7.3% m/m sa, but year-on-year growth of the three month average remained expansionary at 9.6% y/y 3mma, falling only slightly below July's figures which were comparable to those in 2009.**
- **Total business insolvencies dropped markedly in August, falling well below one standard deviation from the average—decreasing by 36.2% m/m sa from the prior month**

TOTAL INSOLVENCIES RE-ENTER THRESHOLD

The total number of Canadian insolvencies came down in August after July's spike to levels last seen in 2009 following the outbreak of the global financial crisis (GFC). Overall, total insolvencies declined by 8.3% in month-on-month seasonally adjusted (m/m sa) terms following a 15.2% uptick in July. August's numbers come as a relief after July's increase took the total number of monthly insolvencies to nearly two standard deviations above the average since the beginning of 2010 (chart 1). Consumer insolvencies accounted for around 98% of all Canadian insolvencies in August, and drove the contraction this month with a 7.3% m/m sa decline. The number of business insolvencies declined markedly in August with a 36.3% m/m sa drop, pushing below one standard deviation of the monthly average since 2010 (chart 2).

August's reduction in insolvencies re-entered the upper-edge of one standard deviation above the historical average, providing a touch of regularity after July's figures broke through the boundaries on the backdrop of high debt levels in Canada. However, these higher recent numbers appear less worrisome when adjusted for developments in the Canadian economy over the last decade. When scaling consumer insolvencies credit outstanding, or the total pool of Canadian enterprises—both of which have grown progressively over the last decade, Canadian insolvency figures in recent months do not appear abnormal.

CONSUMER INSOLVENCIES DECLINE

Consumer insolvency volumes perceptibly fell relative to numbers in the prior month, driven by consumer proposals in number, as well as a fall—albeit smaller in volume—in bankruptcies this month. Consumer insolvencies overall posted a 7.3% decline from the prior month in seasonally-adjusted terms. However, last month marked the largest surge since the beginning of 2013.

Trend growth in consumer insolvencies continued to accelerate in August following two years of gradual rate increases from the Bank of Canada (chart 3). Market rates have been on an overall declining trajectory over the course of 2019, relieving some pressure on households (chart 4). The three-

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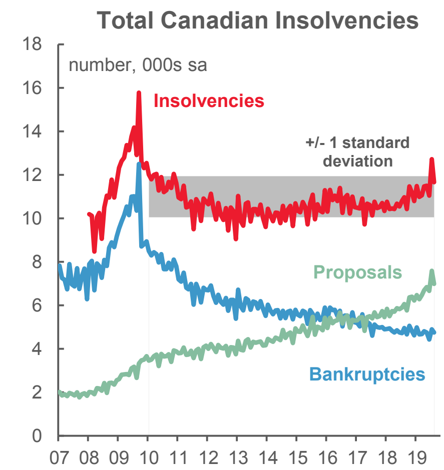
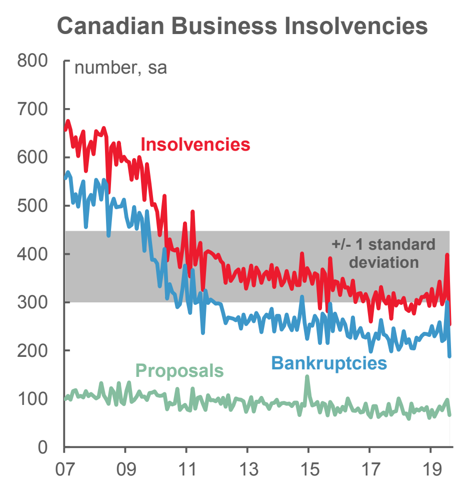
Chart 1



Sources: Scotiabank Economics, OSB.

Chart 2



Sources: Scotiabank Economics, OSB.

month-moving average trend of consumer insolvencies continued on an upward path, posting a comparatively large increase of 9.6% year-on-year, coming off its largest increase in the same terms since the end of 2009 at 10.0% in July.

The volume of consumer proposals had already been on an upward trajectory pre-dating what the trend-growth implies as a result of earlier policy change. The volume of consumer proposals began to spike in exactly September of 2009 (chart 5), when the Bankruptcy and Insolvency Act (BIA) was introduced. The Act changed the specifications of consumer proposals, increasing the threshold for liabilities from $75,000 to $250,000, allowing consumers to restructure their debt repayment instead of defaulting entirely on their loans.

Consumer bankruptcies have been on a rather consistent decline since 2009 as a result of the BIA, contrasting the path of proposals. Bankruptcies declined by 2.3% m/m sa in August, continuing along an overall decade-long declining trajectory since the debt-restructuring plan was introduced with the intention of relieving lenders from larger losses.

Rising levels of consumer insolvencies appear subdued when taking into account the growth of overall consumer credit. With debt levels on the rise and the Canadian debt-service ratio at an all-time high, the rising insolvency rates can appear especially worrying. However, total consumer insolvencies when scaled to total household credit have actually been rather resilient and have returned to their plateau after July's temporary spike (chart 6).

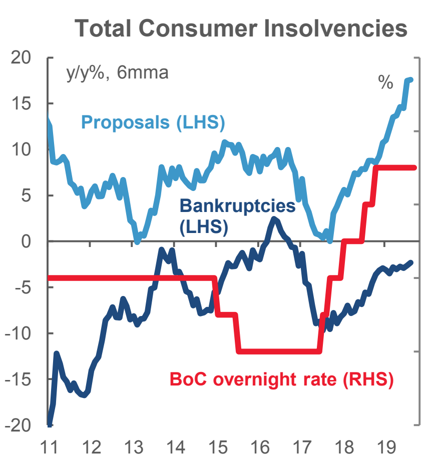
Currently, the majority of household credit is centralized in mortgage credit which makes up almost three-quarters of all household credit, in line with the long-term average. Despite rising mortgage credit levels, there has been a rather persistent decline in percentage of mortgage arrears since 2010. This trend of lower mortgage arrears is vividly contrasting the increase in the consumer proposal rate over the same period (chart 7)—suggesting that Canadians are paying their mortgages. Consumer credit, though constituting a smaller proportion of all household credit, has also continued to remain rather stable in recent years, also opposing the rise in the consumer proposal rate.

Breaking down insolvencies by province, Ontario and Quebec almost-at-par lead the country in volume of total insolvencies (chart 8). Ontario is currently leading the country in proposal growth rates as well as volume while Quebec houses a higher number of bankruptcies. Despite Alberta's relatively heightened growth rate of insolvencies in comparison to the remainder of the country, the volume of total insolvencies only makes up around one-tenth of the nation's total.

BUSINESS INSOLVENCIES FALL BELOW AVERAGE

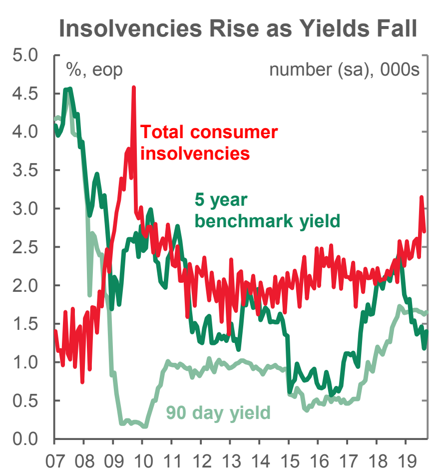
Total business insolvencies dropped markedly in August, falling well below one standard deviation from the average. In terms of volumes, business insolvencies only make up around 2% of all Canadian insolvencies. Overall, the number of business insolvencies appears slow-to-react to rising interest rates, showing resilience. Despite higher numbers of business insolvencies in earlier months, when looking at 12-month volumes side by side over the last 5 years, the change is not as significant as growth-rates imply (chart 9).

Chart 3



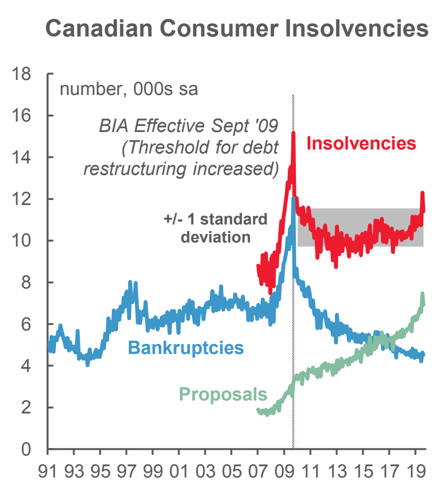
Sources: Scotiabank Economics, OSB, Bank of Canada.

Chart 4



Sources: Scotiabank Economics, OSB, Bank of Canada.

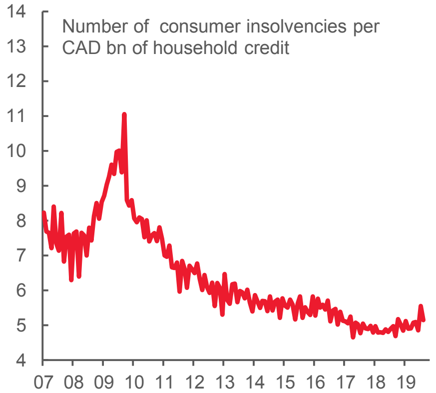
Chart 5



Sources: Scotiabank Economics, OSB.

Chart 6

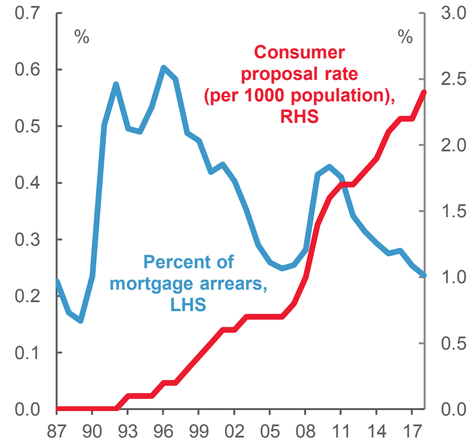
Consumer Insolvencies Trend Downward in Relation to Household Credit Growth



Sources: Scotiabank Economics, BoC, OSB.

Chart 7

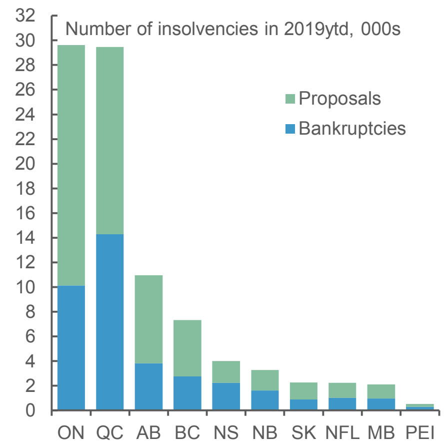
Mortgage Loans are Sound



Sources: Scotiabank Economics, CBA, ISED.

Chart 8

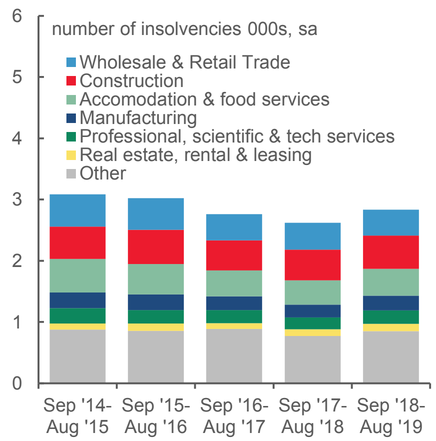
Consumer Insolvencies By Province



Sources: Scotiabank Economics, ISED.

Chart 9

Business Insolvencies Still in Line



Sources: Scotiabank Economics, ISED.