

Canada: Consumer Insolvencies Trending Upward

- Canada's monthly new insolvencies have trended upward since the beginning of 2019, led by increases in consumer proposals. In October, the total number of new consumer and business cases hit the highest level since September 2009.
- Scaled by working-age population and total consumer credit outstanding, the rise in consumer insolvencies looks less striking, but recent developments are nevertheless directionally clear: insolvencies are rising.
- Mortgage and credit card arrears, however, remain flat. This could imply that the increase in consumer proposals may be an ongoing artefact of the 2009 reforms to the *Bankruptcy and Insolvency Act (BIA)* and/or a by-product of refinancing to take advantage of low interest rates rather than mounting debt distress, but it's not clear from the data.
- The monthly number of new business insolvencies remains low by historical comparison.

TOTAL INSOLVENCIES KEEP RISING

Canada's monthly incidence of new consumer and business insolvency cases in October hit the highest level that has been recorded since September 2009. Proposals, mainly from consumers, led the increase, as they have since 2016–17 (chart 1). In seasonally adjusted terms, insolvencies rose by 2.3% m/m sa in October, which represented a bit of a slowdown from the 5.2% pickup we saw in September. This pulled year-on-year trend growth down to 13.0% y/y following an 18.4% rise in September. Despite the slight deceleration in the growth of new insolvencies, the raw monthly volume of new cases moved to about three standard deviations above the January 2010-onward average (chart 1, again).

While total monthly insolvencies are clearly trending upward, data are sending mixed signals about the state of Canadian household finances. As this report outlines, consumer proposals haven't popped as much when scaled by adult population or by the stock of outstanding consumer credit. It's also notable that the proportion of mortgage and credit-card debt in arrears hasn't risen. And on a regional basis, there is only a partial match between provinces with the most stretched household balance sheets and the highest rates of insolvencies. The remainder of the report looks into these developments in more detail.

CONSUMER PROPOSALS REACH TEN-YEAR HIGH

Almost all of the action in Canadian insolvencies is on the consumer side, where new cases hit their highest monthly number in October since June 2009, some three standard deviations above the 2010–present average (chart 2). October saw a seasonally-adjusted increase of 2.3% m/m after a 5.2% gain in September. The year-on-year trend growth rate decelerated to 13.4% y/y from 19.3% in September.

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Chart 1

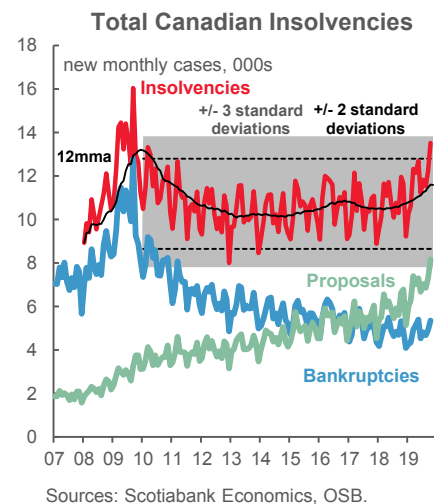
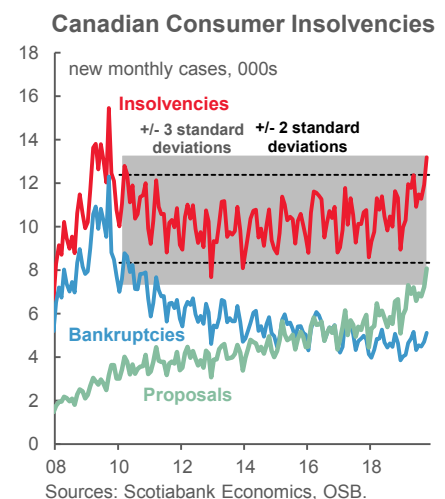


Chart 2



Since the advent of the 2009 reforms to the *Bankruptcy and Insolvency Act (BIA)* that changed the threshold under which proposals can be sought, Canadians have broadly tended to substitute proposals in many cases where they otherwise would have sought bankruptcy protection. Proposals allow debtors to maintain control of their assets, but they require agreement by a weighted vote of creditors and they impose a potentially persistent impact on a debtor’s credit rating. As a result, entering into a proposal is a non-trivial undertaking. The recent rise in proposals may reflect an attempt by some marginal borrowers to benefit from low rates and get ahead of future problems by seeking a pre-emptive treatment of their liabilities—despite the costs of an insolvency process. But this likely represents only a small share of the recent surge in proposals since low rates also imply that the bar for creditors to agree to proposals is higher.

The recent rise in consumer insolvencies looks a bit less marked when it’s scaled against Canada’s adult population (chart 3) and the stock of consumer credit outstanding (chart 4)—but the rise is still notable. In October, new consumer insolvencies as a share of Canada’s population over 15 years of age moved to a level last seen in November 2010, which is two standard deviations above its 2010-onward average (chart 3, again). That said, the ratio is still relatively low compared with those that have prevailed in countries experiencing financial distress. In terms of the total stock of household credit outstanding, the rise in consumer insolvencies is less remarkable (chart 4, again), and takes us back only to levels last seen in March 2017.

Chart 3

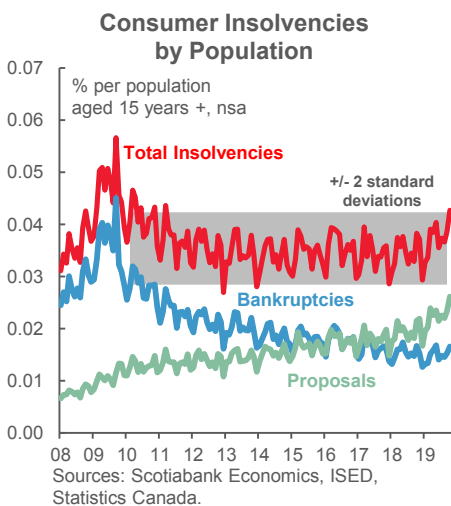


Chart 4

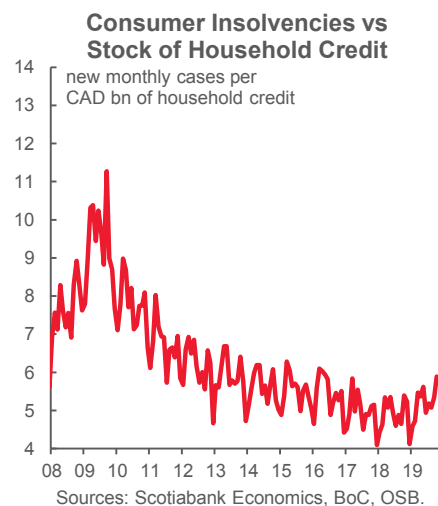


Chart 5

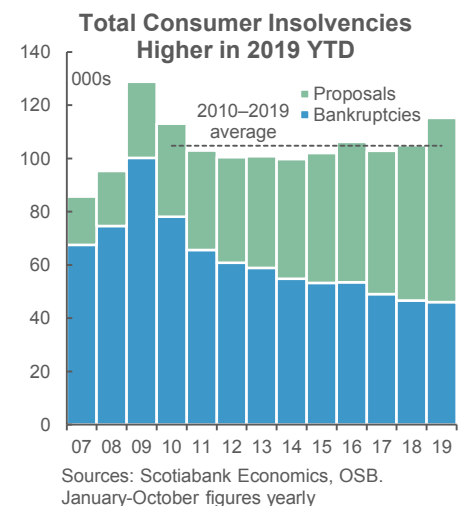


Chart 6

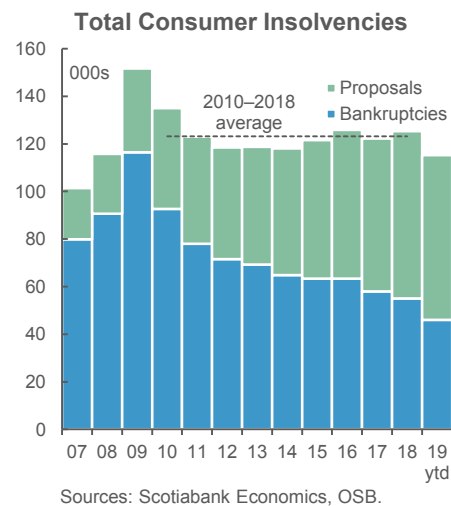


Chart 7

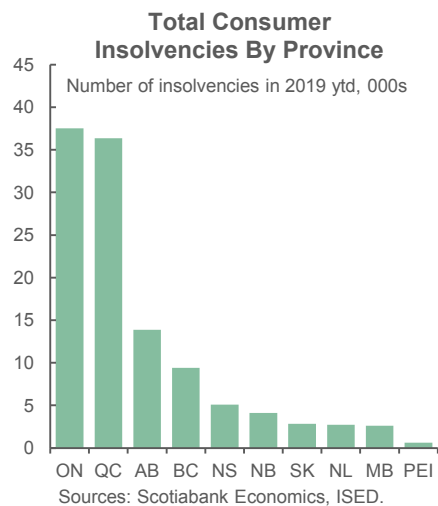
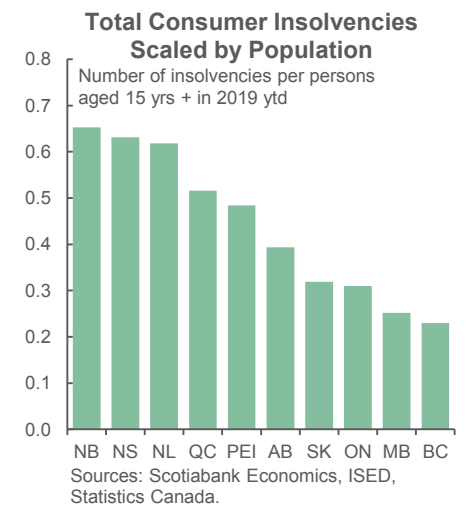


Chart 8



Overall, consumer insolvencies through the course of the year have shown a notable increase in comparison to recent year-to-date numbers. Comparing year-to-date volumes over the last decade, this year has brought in the highest number of consumer insolvencies since 2009 (chart 5). If seasonal patterns hold, 2019 would be on track to record the highest number of insolvencies since 2010 (chart 6).

Ontario and Quebec continued to lead the provinces in October in terms of total new consumer insolvencies (chart 7), owing to the size of their populations and economies, but the Atlantic provinces again come to the fore when consumer insolvencies are scaled by their populations over 15 years of age (chart 8). Liability-asset ratios are highest in Alberta, Newfoundland & Labrador, and New Brunswick (chart 9), which implies that debt concerns likely to remain most pronounced in these areas, but the overlap between provinces with stretched balance sheets and high insolvency-population ratios is mixed.

A SMALL CONUNDRUM: CONSUMER DEBT, ARREARS, & INSOLVENCIES

It's not obvious that rising debt distress is driving the recent increase in consumer insolvencies. Commentators reflexively point to Canadian households' near-record average ratio of debt to personal disposable income (chart 10) to explain rising consumer insolvencies, but this comparison of debt stocks to annual income flows isn't a good measure of debt distress, particularly when Canadians' average liability-asset ratios remain moderate (chart 10, again). Mortgage and credit-card arrears would normally be expected to rise ahead of an increase in insolvencies—and they haven't notably (chart 11) outside of a few provinces (chart 12). Moreover, with strong hiring and wage growth in 2019 (chart 13) amidst lower market interest rates, Canadians should have marginally more breathing room to meet their debt obligations. It could be that the recent increase in insolvencies is a lagged effect of the Bank of Canada's policy rate increases during 2017 and 2018 that hit marginal borrowers who stretched to buy expensive homes ahead of the tightening in rules under the B-20 guidelines, but this isn't clear in the data. Similarly, it seems unlikely that more than a small share of new consumer insolvencies reflect debtors who are making pre-emptive proposals to profit from low rates.

BUSINESS INSOLVENCIES STILL LOW

Business insolvencies remained low in October and stayed under the 2010–present average (chart 14). Business insolvencies continue to account for just over 2% of total Canadian insolvencies and haven't been noticeably affected by recent increases in the Bank of Canada's policy rate (chart 15). Similarly, the share of insolvencies across sectors has remained stable (chart 16). Scaled by the total number of Canadian enterprises, business insolvencies are at historic lows (chart 17).

Chart 9

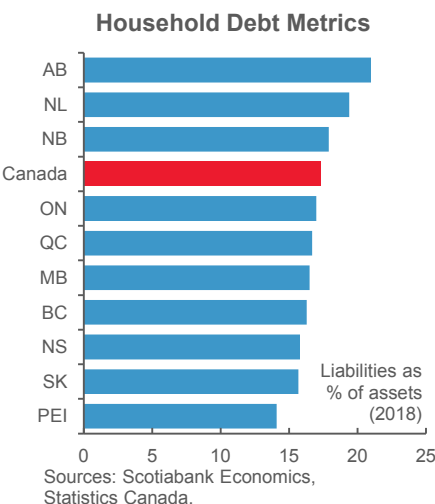


Chart 10

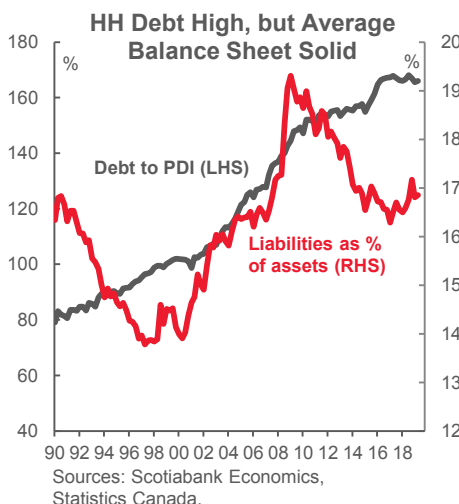


Chart 11

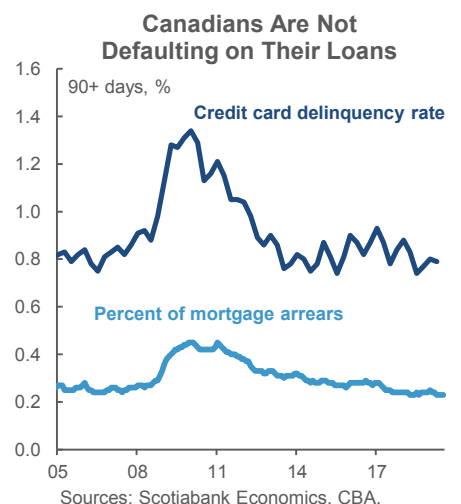


Chart 12

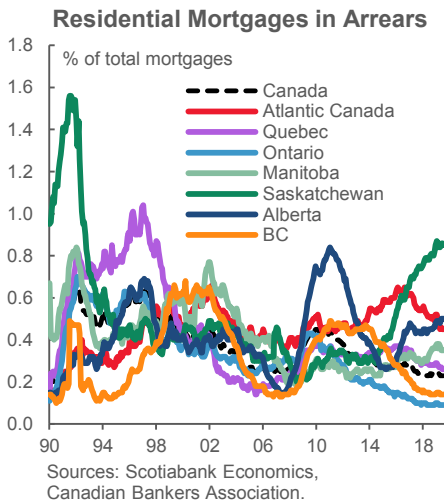


Chart 13

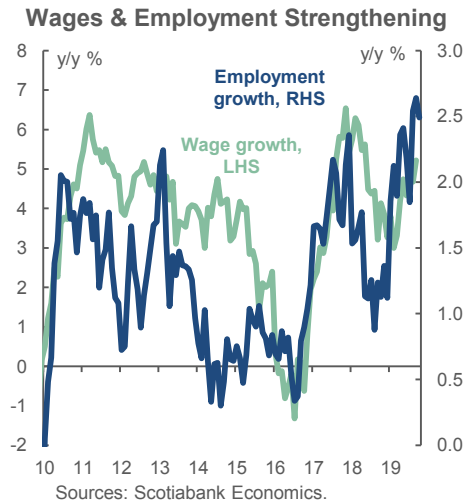


Chart 14

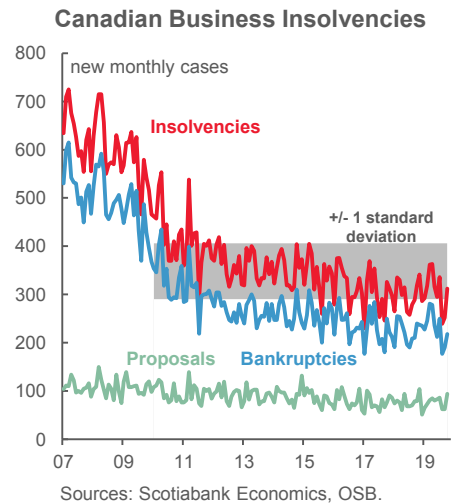


Chart 15

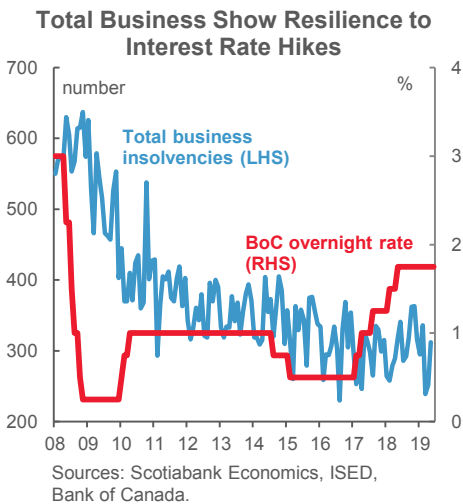


Chart 16

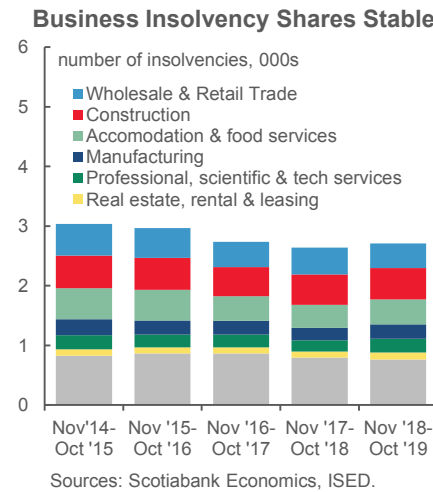
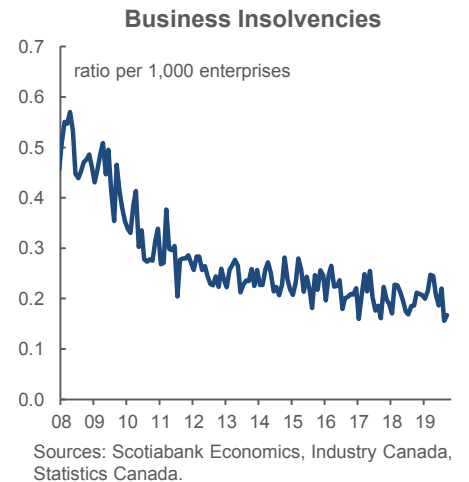


Chart 17



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