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Daily Economic Update

March 15, 2018

Canadian households' high debt levels will shape the 2018 outlook

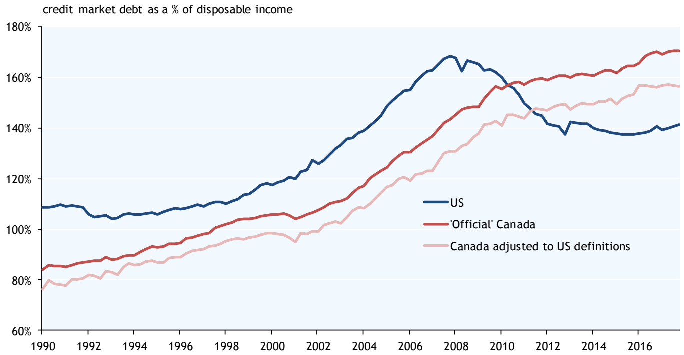
In broad strokes, 2017 painted a familiar picture of household finances: rising asset values, more borrowing and fairly steady debt payments relative to consumers' incomes. 2018 should be more interesting. For one, it looks like debt growth is turning a corner. As the Bank of Canada pointed out last week, household credit growth has slowed in recent months. With interest rates expected to rise further and housing regulations tightening at the federal and provincial level, the peak in debt growth could very well be behind us. That should be viewed as a positive development by the BoC, though progress on reducing the 'key vulnerability' of elevated household debt will likely be very slow.

While more moderate debt growth is a welcome development, policymakers will want to be sure they aren't hitting the brakes too hard. We got the slightest taste of what rising interest rates mean for household debt service costs in Q4/17 and think a trend of gradually rising interest payments will become entrenched this year. Households shelling out a bit more to cover debt costs—and less attractive interest rates for big ticket purchases—will be a headwind for consumer spending this year. How highly indebted consumers react to rising borrowing costs remains a key uncertainty facing the BoC and one that will likely keep them cautious in raising rates.

Highlights:

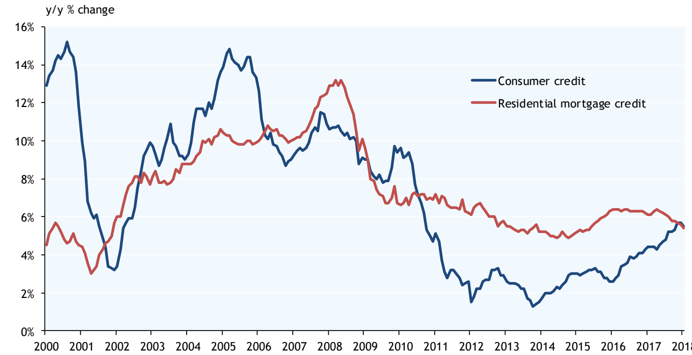
- Aggregate household balance sheets improved in Q4/17 with net worth rising 2.1%.
- Household assets rose by 1.9% quarter-over-quarter thanks to strong equity market performance. Nonfinancial assets continued to rise at a more moderate pace as home prices came off the boil.
- Credit market debt rose 1.1% as both mortgage and non-mortgage debt increased at a similar pace.
- Credit market debt-to-assets and debt-to-net worth ratios retraced the previous quarter's increases, edging down to 16.3% and 19.6%, respectively. Both are just slightly above longer run averages.
- The household debt-to-disposable income ratio was little changed at 170.4%. The previous quarter's reading was revised down to 170.5% though that was still a record high.
- A previous release showed the household debt service ratio was little changed at 13.8% though the interest portion of payments rose by 0.1 percentage point of disposable income.

Canada and US debt-to-income ratios



Source: Statistics Canada, Federal Reserve, Burea of Economic Analysis, RBC Economics Research

Canadian household credit growth



Source: Statistics Canada, Federal Reserve, Burea of Economic Analysis, RBC Economics Research

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