



Household Debt Bubble Could Crash the TSX Index

Description

It's been a solid few weeks for the **S&P/TSX Composite Index**, which clocked a 1.37% gain last week and got off to a positive start on Monday. However, in the long run, the forecast is not as rosy as recent results suggest. While energy and minerals are currently driving many TSX constituents higher, there are broader macro trends that threaten to erase the gains.

One of the big concerns at the moment is household debt. As you may have heard, there's a personal debt bubble in the works, a rise in household borrowing that's pushing Canadian families to dangerously high levels of leverage. The problem is so severe that banks are raising their provisions for credit losses, while hedge funds are betting against Canada's biggest financial institutions.

It's not just banks that could suffer under the collapse of a debt bubble, either. As you'll see in a minute, one major sector could lose out even more. But to understand the broader economic implications of a debt crisis, we need to start by looking at the nation's biggest financial institutions.

Banks could be hit hard

As the main providers of credit in the economy, banks are naturally impacted by consumer credit problems. If individuals feel their debt is becoming too much to bear, they may default or even declare bankruptcy—as a result, banks miss out on revenue.

Consider **Canadian Imperial Bank of Commerce** ([TSX:CM](#))([NYSE:CM](#)) for example. While the bank does have a [growing U.S. business](#), the vast majority of its income comes from domestic operations. As a consequence, any rise in defaults and/or bankruptcies would hit the bank hard.

Although mortgage loans are somewhat safer than unsecured loans, there's still a huge portion of CIBC's book of business that is totally vulnerable to defaults—and the bank's management is aware of it, as we'll see in a minute.

Consumer spending could take a hit

It would be a huge mistake to assume that only banks would be negatively impacted by a household debt collapse. Business-to-consumer (B2C) industries of all types would be hit too. Consumers depend on credit to finance purchases—particularly large purchases like cars.

If there's a rise in defaults and delinquencies, consumer credit scores will suffer and people will be able to borrow less money. As a consequence, consumers will start to look at ways of trimming their spending—we'd expect retailers of all types to lose out in this scenario.

Are we already seeing the effects?

So far, I've spoken of the household debt bubble collapse as something that's going to happen in the future. But in truth, it may already be in progress.

To return to CIBC for a moment: in its most recent nine-month period, the company had \$593 million in [provisions for credit losses](#) (PCLs), up from \$365 million a in the nine-month period a year before. Such a big increase in PCLs shows that the bank believes defaults are an increasing risk and is responding accordingly.

On the bright side, the bank reported that increasing PCLs in personal banking were offset by lower credit risks in "Corporate and Other." This would suggest that CIBC itself may not be devastated by the household debt problem, although its acknowledgement of rising consumer credit risks could be bad news for retailers.

CATEGORY

1. Bank Stocks
2. Dividend Stocks
3. Investing

TICKERS GLOBAL

1. NYSE:CM (Canadian Imperial Bank of Commerce)
2. TSX:CM (Canadian Imperial Bank of Commerce)

PARTNER-FEEDS

1. Msn
2. Newscred
3. Sharewise
4. Yahoo CA

Category

1. Bank Stocks
2. Dividend Stocks

3. Investing

Date

2025/09/08

Date Created

2019/06/25

Author

andrewbutton

default watermark

default watermark