Canadian Debt Is Spinning Out of Control

Description

The Big Banks in Canada want the federal government to go easy and not amass massive budget deficits because its debt might spin out of control. Economists suggest focusing more on productivity-enhancing measures than buoying consumer demand.

Finance Minister Chrystia Freeland met with the bankers to discuss the economic outlook and potential policy steps. Prime Minister Justin Trudeau plans new spending to drive economic recovery and fill in gaps in social safety nets exposed by COVID-19.

Big lenders' concerns

Bank of Montreal Chief Economist Doug Porter is concerned about launching all kinds of spending. The peak of expenditures should be over following the recovery in the last three to four months. For Royce Mendes, an economist at the **Canadian Imperial Bank of Commerce**, the government can't test the limit and allow the debt-to-GDP ratio to go up.

According to **Bank of Nova Scotia** economists Jean-François Perrault and Rebekah Young, the debt ratio could soar to 65% but would not affect its image. Canada is one of the least indebted governments in the G7 group. It would add another half-trillion-dollar to the deficit over the next three years.

However, the BNS report emphasizes the need for a firm commitment to bring down the debt burden gradually to ease concerns about the fiscal path. Legislation forcing the government to lower its debt ratio should be introduced.

Royal Bank of Canada Chief Economist Craig Wright wants to hear from the government its guidance on how to move the debt-to-GDP ratio lower. It should eventually return to balance.

Invest but don't leverage

Does the borrow-to-invest strategy make sense today because interest rates are low, while stocks are cheap? It's not advisable for regular investors since the market is hyper volatile. Similarly, leverage is only for experienced traders.

Only invest if you have free money to spare. If the goal is to earn extra cash or build an emergency fund, the **National Bank of Canada** (TSX:NA) can be your income facilitator. The sixth-largest bank in Canada is a dividend all-star as it has increased dividends for ten straight calendar years.

The bank stock pays a 4.01% dividend and maintains a payout ratio of less than 50%. A $25,000 position will produce $1,002.50 in passive income. It has climbed 84.15% from its COVID-low in March and is trading at $69.57 per share or a mere 1.07% year-to-date loss.

Despite its limited exposure outside of Canada, National Bank is growing its investment banking activities and doing well overall relative to larger industry peers. The profits are near pre-coronavirus levels. Also, the conservative increase in loan loss provision is a healthy sign.

In Q3 of the fiscal year 2020 (quarter ended July 31, 2020), the bank reported a $602 million net income, which is a 0.99% slide from the same period in 2019. The wealth management and financial markets business segment turned in strong performances during the quarter.

Low-debt advantage

Government borrowings were necessary to stabilize the economy. However, it will raise the debt-to-GDP ratio to 49% in 2020-21 from 31 % in 2019-20. Notwithstanding the jump, the country can still maintain its low-debt advantage. Last, consultations with market participants will continue to assess the capacity for long-term debts.

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