TABLE 16.7

Book value long-term debt/equity ratios for selected industries in Canada, 2008

Industry	Ratio
All industries	0.835
Non-financial	0.877
Agriculture, forestry, fishing, and hunting	1.273
Oil and gas extraction and support activities	0.617
Mining and quarrying (except oil and gas)	0.469
Utilities	0.965
Construction	1.254
Manufacturing	0.604
Wholesale trade	0.709
Retail trade	1.053
Transportation and warehousing	1.439
Information and cultural industries	1.193
Real estate and rental and leasing	1.838
Professional, scientific, and technical services	0.483
Administrative and support, waste management, and remediation services	1.393
Educational, healthcare, and social assistance services	0.628
Arts, entertainment and recreation	2.166
Accommodation and food services	2.172
Repair, maintenance, and personal services	0.816
Finance and insurance	0.721

Source: Statistics Canada "Quarterly financial statistics for enterprises," Catalogue 61-008-x, Fourth Quarter, 2008, March 2009.

industry is in distress, the average leverage is likely too high. For example, in 2008, the average debt/equity ratio of 4.938 agriculture and forestry was probably too high.

The leverage ratios in Table 16.7 are considerably higher than they were in the 1960s. Most of the increase in Canada came in the 1970s and early 1980s—periods of low interest rates and economic growth particularly in Western Canada. Significant corporate tax rates encouraged corporations to use debt financing. Table 16.7 shows that the construction industry had one of the highest uses of leverage in 2008 and this industry accounts for a major portion of the leverage increase for Canadian companies over the last 40 years. In the U.S., the increase in leverage was similar but occurred in the leveraged buyout period of the 1980s.[8]

Concept Questions

1. Do Canadian corporations rely heavily on debt financing? What about U.S. corporations?
2. What regularities do we observe in capital structures?

16.10 LONG-TERM FINANCING UNDER FINANCIAL DISTRESS AND BANKRUPTCY

One of the consequences of using debt is the possibility of financial distress, which can be defined in several ways:

1. *Business failure.* Although this term usually refers to a situation where a business has terminated with a loss to creditors, even an all-equity firm can fail.[9]

[8] Our discussion of trends in leverage draws on M. Zyblock, "Corporate Financial Leverage: A Canada–U.S. Comparison, 1961–1996," *Statistics Canada*, Paper no. 111, December 1997 and P.M. Shum, "Taxes and Corporate Debt Policy in Canada: An Empirical Investigation," *Canadian Journal of Economics* 29, August 1996.

[9] Dun & Bradstreet Canada Ltd. compiles failure statistics in "The Canadian Business Failure Record."