Housing Market Digest

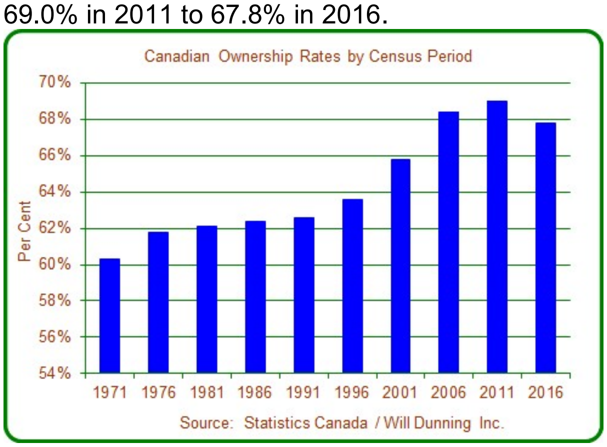
Greater Toronto Area, May 2021

Canadians are unnecessarily being prevented from making housing choices that are in their own best interests. The higher policy interest rate from OSFI will worsen that over-reach.

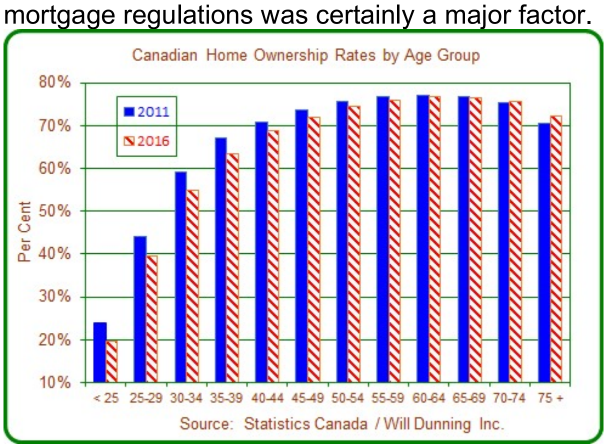
"Short-Term Pain for Long-Term Dire Straits"

During the past decade, there has been a series of policy changes that have made it more difficult to obtain mortgages. The changes were partly motivated by a desire to cool housing markets across Canada. Those policies have varied in their effects. In combination they have caused home buying to be much less than it would have been.

After a generation of social progress, in which the ownership rate rose in Canada, the rate fell, from 69.0% in 2011 to 67.8% in 2016.



For the age groups under 40, ownership rates fell sharply, by 4 percentage points during that period of 5 years. If the ownership rates had stayed at the 2011 levels, there would have been 200,000 more Canadian home owners in 2016 than was found. There were multiple factors that caused the ownership rate to fall, but the tightening of mortgage regulations was certainly a major factor.



Since 2016, the mortgage stress tests have been added, and have been a further impediment, which very likely caused the ownership rate to fall further during 2016 to 2020. Covid-19 might have caused the ownership rate to rise during the past year. Housing data from the 2021 Census will be released in Sept. 2022.

Demand-suppressing policies have also reduced sales of new homes, contributing to housing shortages in Canada. I'm currently working on a research project that estimates "demographic requirements" (the amounts of housing needed as a result of our growing population) in comparison to actual housing production. The draft estimates indicate that during 2006 to 2020, production of "low-density" housing (singles and semis) in large cities was about 500,000 less than required (in the March edition of this report, I commented that the shortfall in the Toronto CMA was 130,000 for low-density housing).

The shortage of housing is a major factor in surging housing prices across Canada. The increased policy rate from OSFI (an increase to 5.25% from 4.79%) will further suppress demand, which will also further constrain future supplies. This policy will worsen the long-term dire straits.

The interest rate used in the stress tests is far above any scenarios for mortgage interest rates. Therefore, the policies are no longer about managing risk. They are actively suppressing an important sector of the Canadian economy, to the detriment of our collective well-being.

Three weeks ago, I wrote a letter to the Minister of Finance, recommending a test rate of 3.76%, which is the maximum monthly average actual rate seen in Canada since 2013. That letter is now the first item on the Recent Reports page of: https://www.wdunning.com/

What Should Be Done?

There are no easy solutions. Further worsening the already-dreadful stress tests is the wrong direction. Instead, allow rates to normalize. A 1.25% yield for 5-year Government of Canada bonds would result in mortgage rates in the area of 2.5-2.75%. A half point rise in the Bank of Canada Overnight rate would also be appropriate.

Moreover…

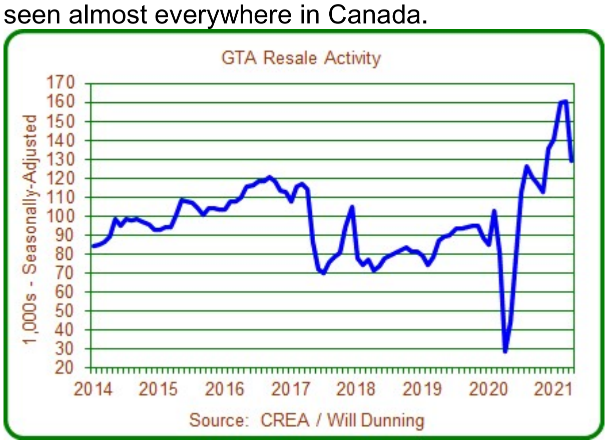
Within OSFI's policy guideline B20 there is a requirement that mortgages that are transferred to federally-regulated lenders must be stress tested. At present, most renewing mortgages were initiated five years ago, qualified at actual interest rates well below 3%. In order to be transferred they must be tested at 4.79% (and soon probably at 5.25%). This policy creates a risk for renewers that they could be captured and exploited by their current lenders. This is bad policy, harmful to Canadians. We don't have data to know to what extent this capture is happening, but it is a risk.

Sponsor(s)?

As mentioned above, I'm working on a research project that compares demographic housing requirements to actual production for 2006 to 2020, for each of the major cities across Canada. I don't have a client for this project. I'm willing to do it *pro bono*. If any of you might be interested in sponsoring this project, we can explore that.

Resale Markets

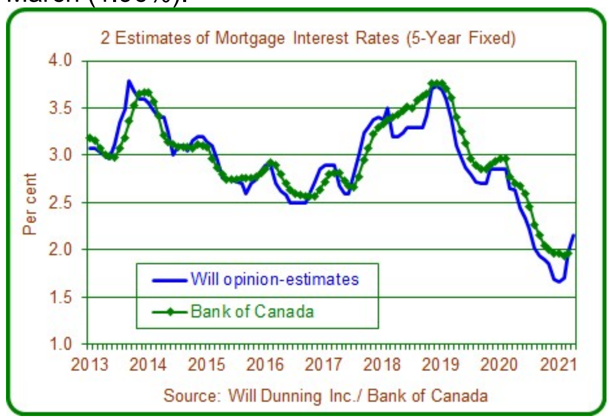
Rising interest rates during February and March added to the urgency to buy, to take advantage of time-limited rate guarantees. As that effect has waned, sales slowed in April, although the rate of 129,000 is still well above the long-term average (which I estimate as 105,000, on a population-adjusted basis). But, from 2018 (the start for the OSFI test) to the present, total resales in the GTA have been 9% below the population-adjusted averages. It's likely that the province-wide shutdown contributed to the slower sales in April, but on the other hand, similar reductions were seen almost everywhere in Canada.



Interest Rates

For many years, I have built a dataset of opinion-estimates of typical mortgage interest rates advertised by major lenders. This is unofficial data, but I'm ok with that.

There is an alternative dataset, which is contracted interest rates for "funds advanced", surveyed by the Bank of Canada. That data can be found here (and you can download a .csv): https://www.bankofcanada.ca/rates/banking-and-financial-statistics/interest-rates-for-new-and-existing-lending-by-chartered-banks/?page_moved=1#download
This chart compares the datasets. The numbers are similar most of the time. I continue to use my unofficial data, because mine has a longer history (the BoC data starts in 2013) and my data is weekly and more-timely: it includes part of this May (2.2%), the most recent BoC data is from March (1.96%).



Other News

I have provided consulting services to Mortgage Professionals Canada since 2005. I've had a huge amount of fun working on the interesting projects that they requested, and I am very grateful to them for their interest and support. I have decided that it's time to move on. I'm looking for opportunities to provide research and advice to new clients.

This is the band ("Grouplove") that I really want to see:

https://www.youtube.com/watch?v=lfAYNKu3IRY

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