Canada: Mortgage Credit Growth Firms While Consumer Debt Softens

- **Total household credit growth appears to have found its bottom in mid-2018, with trend growth in residential mortgage borrowing leading a pick-up in overall credit expansion through January 2019 in the Bank of Canada's latest data release.**
- **Progressive revisions in the Bank of Canada's consumer credit data over recent months imply that consumer lending growth has slowed markedly. These revisions appear to undermine speculation that tighter mortgage lending standards have begun pushing households to substitute alternative means of financing to sustain their current spending or other major debt burdens.**
- **The outstanding stock of home equity lines of credit (HELOCs) has risen at a strong pace since 2016, though survey data does not imply that withdrawals of home-equity have been used toward the repayment of other types of debt.**

TOTAL HOUSEHOLD CREDIT GROWTH PICKING UP

Total household credit grew 3.4% m/m SAAR, 3.2% 3-mma seasonalised, and 3.1% y/y in January. Although year-on-year growth continues to decelerate from a recent high of 5.8% y/y in May 2017, the 3-month trend bottomed in August 2018 at a post-2012 low and January marks five months of gains (chart 1).

The share of household credit—consumer and mortgage—held at banks has remained relatively unchanged during the last year, and in fact over the past two decades, at around 80% of the total outstanding despite concerns that borrowers may be turning to less-regulated nonbank lenders following the implementation of more stringent home mortgage rules in January 2018 (chart 2).

RESIDENTIAL MORTGAGE CREDIT GROWTH FIRMING

Residential mortgage credit growth broke a 19-month series of slow-downs in year-on-year terms in January to tick up from 3.1% y/y in December to 3.2% y/y. Lending growth began accelerating, however, in Q3-2018 and has now recorded seven consecutive months of month-on-month higher growth, with the three-month trend sitting at 3.9%, its highest rate since March 2018 (chart 3).

Residential mortgage credit, which accounts for over 70% of the stock of lending outstanding to households (chart 4), has since 2013 contributed about an 80% share of total household credit growth (chart 5). Chartered banks currently account for about 80% of residential mortgage credit growth, up from a recent low of 52% in Q3-2018—well below its post financial crisis of around 75%—as nonbanks' share of mortgage lending growth has shrunk over the past six months (chart 6).

The ongoing slowing in mortgage credit growth in year-on-year terms is likely being driven by the tightening in federal mortgage lending rules implemented in January 2018; provincial measures, particularly in Ontario and BC, that have been introduced since 2017 to dampen housing demand and enhance the sustainability of debt burdens (table 1); and supply shortfalls that

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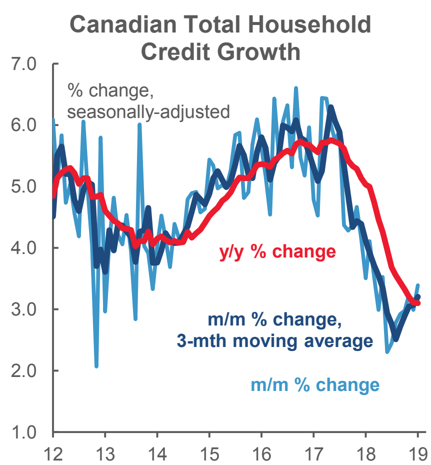
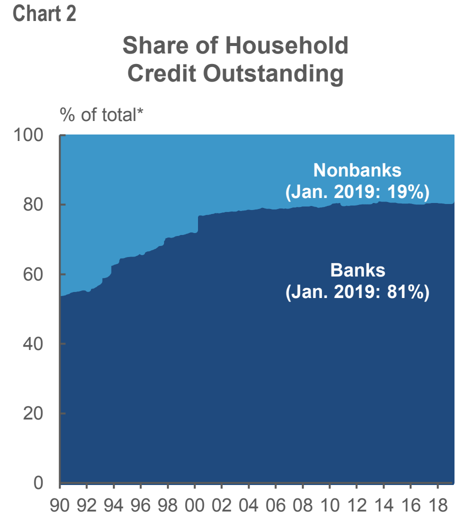
Chart 1



Sources: Scotiabank Economics, Bank of Canada.

Chart 2



Sources: Scotiabank Economics, Bank of Canada
*excludes off-balance sheet securitisation and interpolates change in accounting standards in 2011 related to National Housing Act mortgage backed securities (NHA MBS). Step change in 2000 is due to a change in the BoC's data source for NHA MBSs: "Prior to January 2000, NHA mortgage-backed securities data were obtained from the program trustee, Computershare Trust Company of Canada. Since January 2000, data have been obtained from Canada Mortgage and Housing Corporation."

continue to make affordability challenging despite tight labour markets, low unemployment, and moderate real wage gains (chart 7).

It's unlikely, however, that the five interest-rate increases from the Bank of Canada since mid-2017 have meaningfully dented growth in mortgage lending: the Bank's real policy rate remains slightly negative (chart 8) and five-year mortgage rates are nearly unchanged from five years ago (chart 9).

CONSUMER CREDIT GROWTH: WHEN A SPIKE BECOMES A TROUGH

Household consumer credit, which includes home-equity lines of credit (HELOCs), accounts for only about a third of outstanding household lending (chart 4, again). The Bank of Canada's January data currently show that growth in consumer credit has been on a sustained downturn in month-on-month, 3-mma, and year-on-year terms since October 2018 (chart 10). A wind-down of off-balance sheet consumer-credit securitisation has led the retreat (chart 11).

Up until October, the Bank of Canada's consumer credit data showed a marked spike in growth between June and October 2018 (chart 12, historical series) that implied, amongst other possibilities, that the federal government's B20 rules could be pushing borrowing demand from the mortgage sector to consumer loans to make up shortfalls in home financing. **Progressive revisions to the BoC's credit data since then, however, show significantly softer consumer credit growth in the May-October period and a sustained deceleration from October onward to the present (chart 12, again).**

Such revisions aren't unprecedented—household credit data is typically volatile and subject to change—but it's notable that even with this large revision, total household credit growth does not appear to have been materially affected by the change; the revisions merely shifted certain banks' assets from consumer credit to mortgage credit.

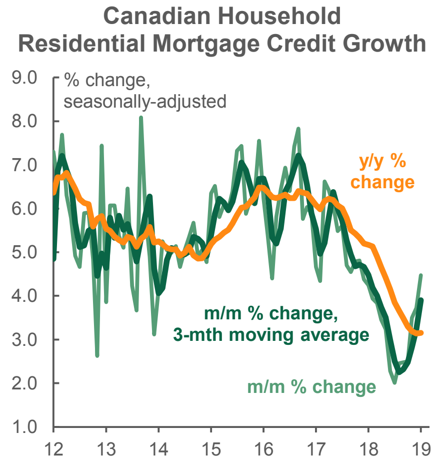
STRONG EXPANSION IN HELOC CREDIT, BUT RISKS APPEAR BALANCED

HELOC balances have significantly expanded in recent months, outpacing the growth in non-HELOC credit (chart 13) as reflected in OSFI data to December from chartered banks. As of December 2018, HELOCs accounted for 47.3% of consumer credit booked with Canadian banks, compared to a recent-low of 44.8% in May 2016 (chart 14). However, only about 15% of households have a HELOC (chart 15).

The rise in HELOC borrowing may be explained, amongst other possibilities, by the increase in the value of residential assets held by households and the lower rate of interest offered on most HELOC products. Borrowers may also be borrowing against their homes to repay principal or simply to capitalise interest due on other types of debt, thereby enabling excessive borrowing.

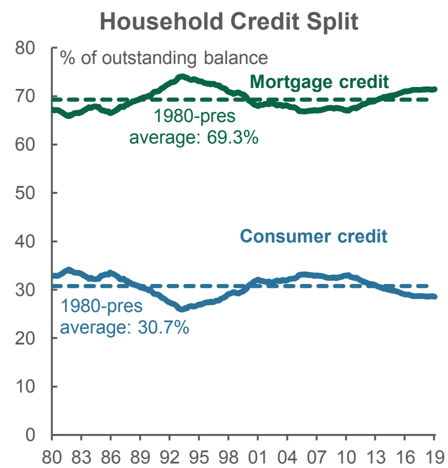
We don't view the recent rise in HELOC borrowing as particularly concerning. Survey data show that Canadians have not taken equity out of their homes to repay or consolidate other debt to a greater extent than previously was the case. According to a survey carried out by Mortgage Professionals Canada in November 2018, close to a quarter of equity taken out of homes—roughly half in the form of HELOC borrowing and the other half via mortgage principal increases—in the twelve months to November 2018 was put toward debt consolidation and repayment. This share has only increased slightly since 2017 and is still well below the 28% share it commanded in 2016 (chart 16). Roughly the same share of home-equity withdrawal has been put toward renovations and home repair that should, in principle, increase property values.

Chart 3



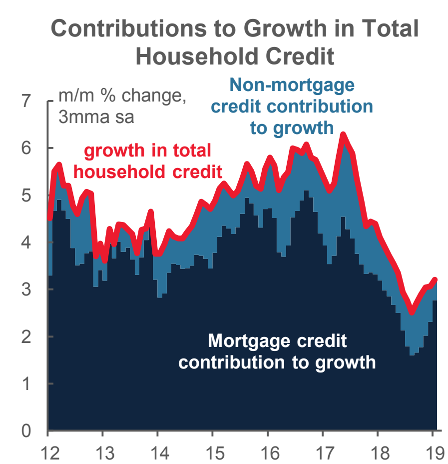
Sources: Scotiabank Economics, Bank of Canada.

Chart 4



Sources: Scotiabank Economics, Bank of Canada.

Chart 5



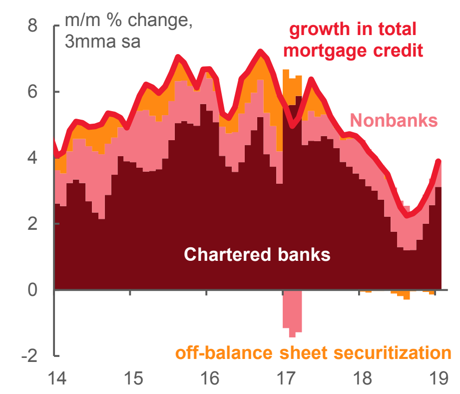
Sources: Scotiabank Economics, Bank of Canada.

Table 1: Recent Housing Policy Developments in Canada

2019	2018	2017	2016
British Columbia: Increase in speculation tax on foreign and domestic home owners who do not pay income tax in BC from 0.5% of a property's assessed value to 2%; additional school tax levied on portion of a property's value that exceeds CAD 3 mn.	**Ontario:** Elimination of rent control on new rental units first occupied on or before November 1, 2018 **British Columbia:** Extension of the Property Transfer Tax on non-resident buyers. Investment of more than CAD 1.6 bn through FY2021 toward the goal of building 114,000 affordable housing units in the next 10 years. **Canada:** OSFI imposes more stringent stress tests for uninsured mortgages, including a minimum qualifying rate at the greater of the five-year fixed posted rate or the contractual rate plus 200 bps, effective January 1, 2018	**Ontario:** 16 measures aimed to slow rate of house price appreciation Key aspects include: - 15% non-resident speculation tax - Expanded rent control to all private rental units in Ontario - Vacant home tax - CAD 125 mn five-year program to encourage construction of new rental apartment buildings	**Canada:** Qualifying stress rate for all new mortgage insurance must be the greater of the contract mortgage rate or the Bank of Canada's conventional five-year fixed posted rate Low-ratio mortgage insurance eligibility requirements updated for lenders wishing to use portfolio insurance: - Maximum amortization 25 years - CAD 1 mn maximum purchase price - Minimum credit score of 600 - Property must be owner occupied Elimination of primary residence tax exemption for foreign buyers Minimum down payment on insured mortgages on homes valued CAD 0.5–1 mn increased from 5% to 10% **British Columbia:** 15% land transfer tax on non-resident purchases in Metro Vancouver introduced

Chart 6

Contributions to Growth in Total Household Mortgage Credit



Sources: Scotiabank Economics, Bank of Canada.

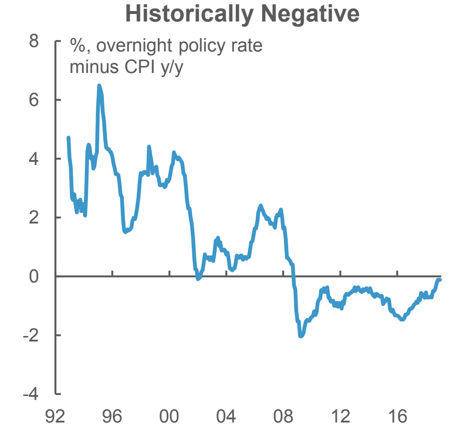
Chart 7

Canadian Housing Affordability Index

Sources: Scotiabank Economics, Bank of Canada.

Chart 8

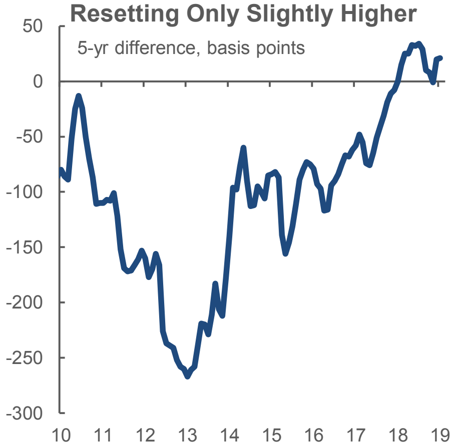
BoC's Real Policy Rate Still Historically Negative



Sources: Scotiabank Economics, Bank of Canada, Statistics Canada.

Chart 9

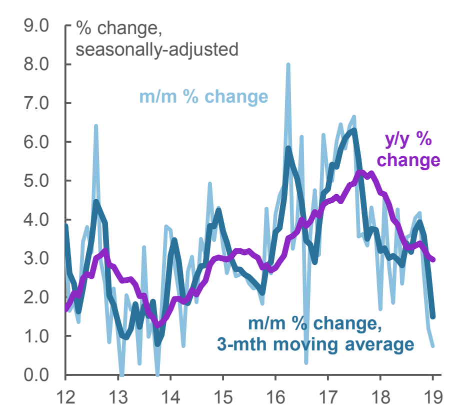
5-yr Mortgage Rates Resetting Only Slightly Higher



Sources: Scotiabank Economics, CMHC.

Chart 10

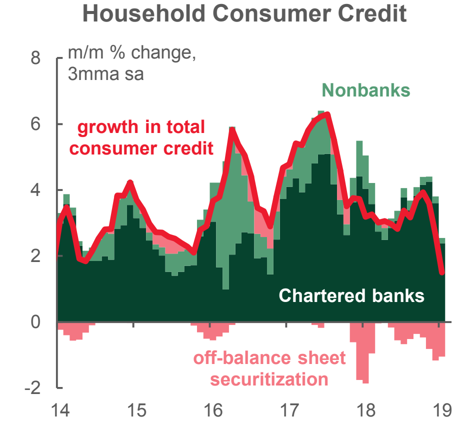
Canadian Household Consumer Credit Growth



Sources: Scotiabank Economics, Bank of Canada.

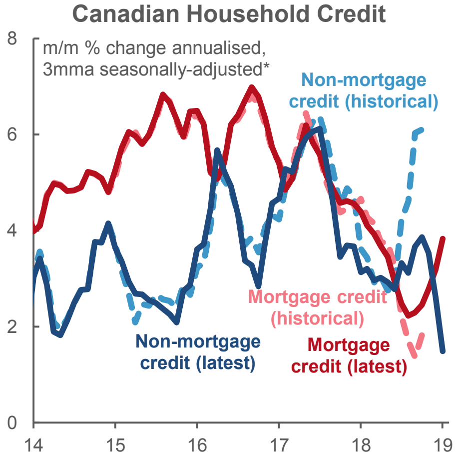
Chart 11

Contributions to Growth in Total Household Consumer Credit



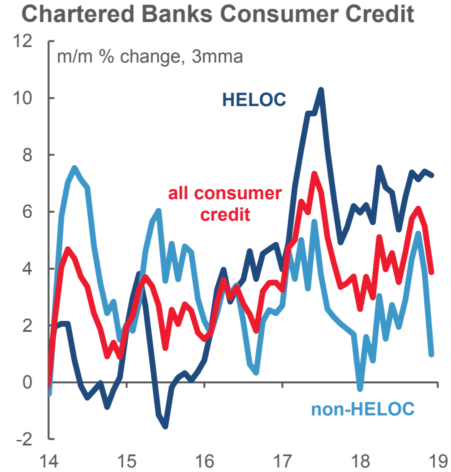
Sources: Scotiabank Economics, Bank of Canada.

Chart 12



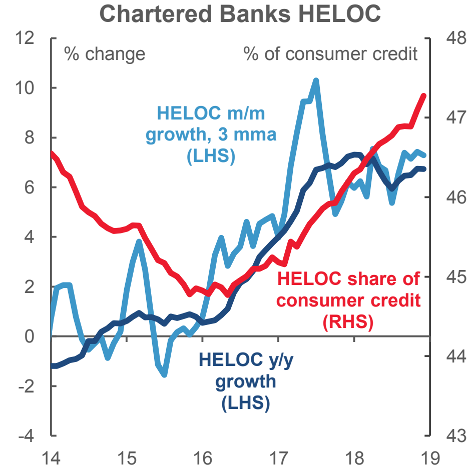
Sources: Scotiabank Economics, Bank of Canada.
*historical series are BoC data to October 2018.

Chart 13



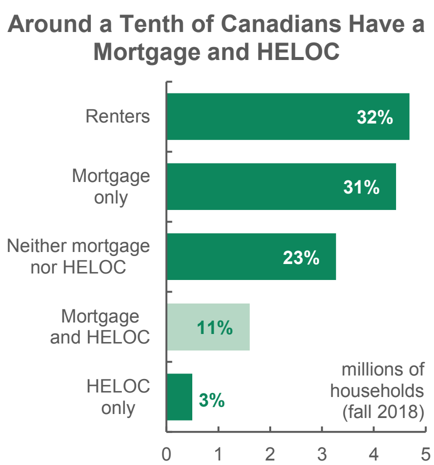
Sources: Scotiabank Economics, OSFI.

Chart 14



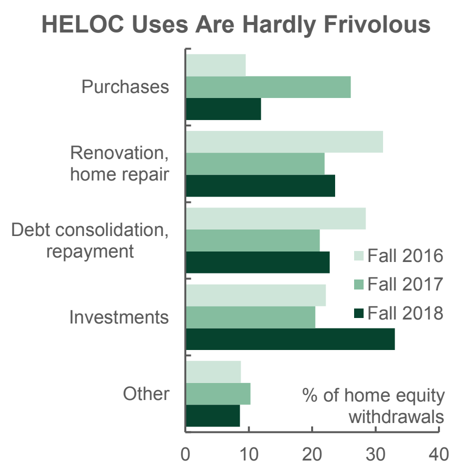
Sources: Scotiabank Economics, OSFI.

Chart 15



Sources: Scotiabank Economics, Mortgage Professionals Canada.

Chart 16



Sources: Scotiabank Economics, Mortgage Professionals Canada.