Intelligence MEMOS

From: Andy Charles

To: Bill Morneau, Minister of Finance

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Re: **HOUSING PRICES IN THE GTA AND MORTGAGE LENDING**

The trajectory of home price increases in the GTA has been an obsession over the past 18 months. Everybody has a theory. What or who is responsible for driving prices upwards? Foreign buyers? Low interest rates? Pure speculation? And today's quarterly sales forecast from the Canadian Real Estate Association will only feed the conversation.

While it is difficult to pinpoint a single direct cause or rationale for the surge of house prices in the GTA, it is important from a public policy perspective to understand what factors are contributing to the price escalation and what factors are not.

Let's start with not:

1. The First Time Home Buyer

Recent changes to mortgage insurance eligibility have made Toronto less accessible than ever for the first-time home buyer. High ratio mortgages now make up less than one in five mortgages Canada wide, and significantly less in Toronto. Insured mortgages have a $1 million purchase price maximum.

To associate the recent price surge in the GTA with the purchasing activities of the insured first-time home buyer is a fallacy, as the vast majority of transactions are being completed by borrowers with no mortgage insurance.

2. Loose Mortgage Lending Standards and Risky Borrowers

The Department of Finance has repeatedly made traditional mortgage lending safer by limiting high-ratio eligibility several times in the past decade.

Additionally, the credit quality of borrowers is high; average credit scores for Canada Guaranty's new high-ratio originations are in the high 760's. This is 40 to 60 points higher than average credit scores before the financial crisis.

3. The structure of the Canadian mortgage insurance framework and Canada's mortgage market dynamics.

The introduction of risk sharing between mortgage insurers and lenders would have minimal, if any, impact on the housing market in the GTA. Risk sharing is much more likely to contribute to a reduction in mortgage lending in remote and economically challenged areas of the country.

So what are the contributing factors to our rising prices? A major problem is supply.

To date, there has been a fundamental disconnect between Canada's very successful immigration policy and the creation of housing supply and infrastructure in the GTA and Greater Golden Horseshoe (GGH) area overall.

It is essential that going forward, policymakers carefully study how immigration, population growth, combined with a low interest rate environment and strong job growth are contributing to current and future housing demand in the GTA and GGH. How this healthy demand is interacting with future additions to the housing supply and public infrastructure in the GTA will help dictate the path of housing prices and the affordability of living in the GTA for future generations.

The time and effort of policymakers should be spent on areas that are leading to demand and supply imbalances, which tend to be more focused regional housing markets like the GTA. Policies directed more Canada wide are likely to lead to structural and potentially disruptive changes in what is a balanced and well-functioning Canadian mortgage market.

While we are now seeing softening in GTA house prices since the Ontario government fair housing announcement in April, the underlying demand fundamentals suggest prices will continue to increase in the longer term if essential housing supply and infrastructure issues are not adequately addressed.

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