



Date: September 9, 2010

Canada Not in Danger of US-Style Housing Bust

ARTICLE REVIEW: Jim MacGee, August 31, 2010, "Not Here? Housing Market Policy and the Risk of a Housing Bust", CD Howe Institute.

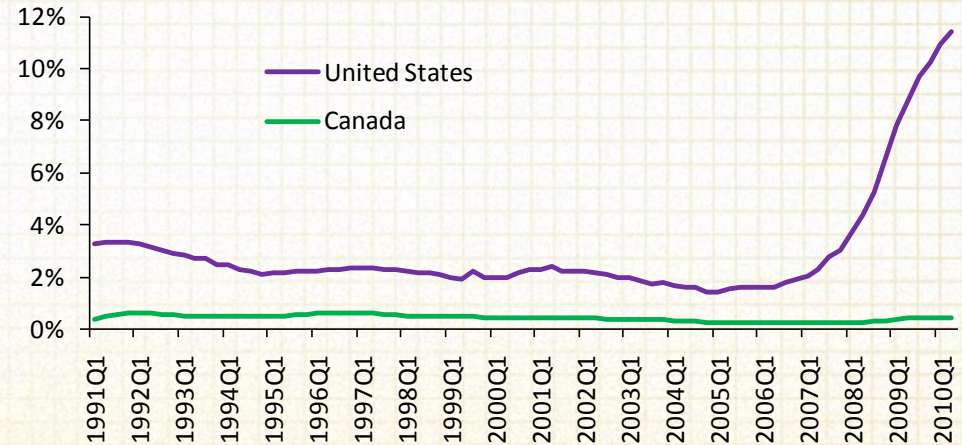
Link to Briefing: http://www.cdhowe.org/pdf/ebrief_105.pdf

The CD Howe Institute recently released a study written by Professor Jim MacGee (University of Western Ontario), which poses the question of whether or not the Canadian housing market could experience a US-style bust, including a steep drop-off in the average selling price.

MacGee argues that mortgage underwriting standards evolved much differently in the US and Canada leading up to the economic downturn in both countries. As early as 2003, US sub-prime borrowers (i.e. those with troubled credit histories) were gaining access to more exotic mortgage products that included the option for interest only payments and negative amortization. Riskier borrowers and borrowing terms prompted mortgage defaults and declining average selling prices *in advance* of the economic downturn in the US. In Canada, in contrast, defaults rose only in conjunction with the economic downturn and remained much lower than in the US (see Chart 1). The lower default rate in Canada, bolstered by the comparatively low percentage of riskier "exotic" mortgage types in this country, helped support home prices and also supports the view that Canada's Federal Government-guaranteed mortgage insurance program is not exposed to the same risk as government sponsored and private insurance programs in the US.

Home price growth in the GTA has been supported by a sustained period of affordability, as evidenced by TREB's Affordability Indicator (see Chart 2). Even with the strong price increases experienced over the better part of the last year, the average combined mortgage, property tax and utility payment as a percentage of average gross household income remains in line with the accepted mortgage lending standard, which requires a gross debt service ratio (GDS) of 32 per cent or less.

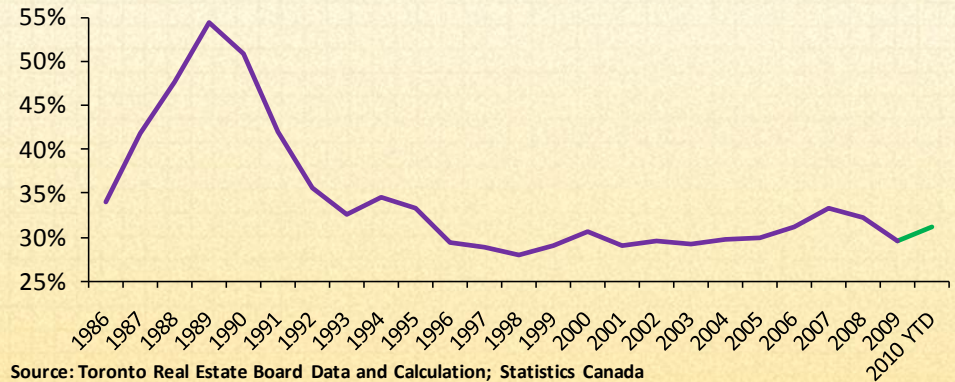
Chart 1: Residential Mortgage Delinquency Rates Canada and United States



Source: US Federal Reserve Board; Canadian Bankers Association

Chart 2: TREB Affordability Indicator

Share of Average Household Income Used for Mortgage Principal and Interest, Property Taxes and Utilities on the Averaged Priced GTA Resale Home*



Source: Toronto Real Estate Board Data and Calculation; Statistics Canada

*Assumptions: The average YTD selling price as of August 2010; 20 per cent down payment; the average five year fixed rate mortgage rate; 25 year amortization; estimated average property taxes, utility costs and household income.

Written By:

Jason Mercer

TREB Senior Manager of Market Analysis.

j Mercer@trebnet.com

