Trends in the Canadian mortgage market: Before and during COVID-19

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Mortgage borrowing reached record highs in 2020, with households adding nearly $108 billion in mortgage debt, compared with less than two-thirds of that amount in 2019 and just under $46 billion in 2018. Despite the economic upheaval caused by the pandemic, expected credit losses on mortgage loans remained slight, accounting for 0.1% of mortgage debt as a share of total household mortgage debt in the third quarter.

A new study explores how the housing mortgage market has evolved since the start of the millennium, with a focus on the recent surge in lending during the pandemic.

New mortgage lending hits record high during the pandemic, spurred by originations and renewals

The amount of new mortgage lending by chartered banks reached record levels in 2020, driven in part by historically low borrowing costs and resilient demand for housing. This lending, which represents the origination of new mortgages for the purchase of properties and the refinancing and renewals of existing mortgages, surpassed $42 billion on a seasonally adjusted basis for the first time ever in March.

As interest rates fell to historic lows in March, mortgage renewals rose sharply, pushing the total value of mortgage renewals up 13.3% on a seasonally adjusted quarterly basis. As many financial institutions allow borrowers to renew several months before their end of term, renewals may have been spurred not only by those with terms ending in the quarter, but also by those with terms expiring in the future who may have taken advantage of early renewal options.

Household borrowers react to interest rate environment and shift term preferences

Mortgage lending data from chartered banks show that Canadians were most likely to choose five-year fixed-rate mortgages during the pandemic, with this loan type accounting for almost half (49%) of the total outstanding balance of existing mortgages by late 2020, up 7.0 percentage points from early 2019.

As interest rates fell in March 2020, the demand for variable-rate mortgages spiked, while longer-term rates were slower to adjust. As longer-term rates began to mirror the decline in variable rates, growth in demand for five-year, fixed-rate mortgages accelerated into the summer.

Chartered banks provide the bulk of mortgage financing and deferrals

Historically, non-bank lending institutions have held about one-quarter of the total household residential mortgage market's outstanding debt. As the lockdown took effect in March 2020, the growth in household mortgage debt provided by non-banks slowed, with chartered banks providing the bulk of the funds.

As the employment rate fell and businesses closed in mid-March, many Canadians found themselves out of work or working fewer hours. To support borrowers and reduce the risk of near-term mortgage defaults, the Office of the Superintendent of Financial Institutions (OSFI) announced a special capital treatment for federally regulated deposit-taking institutions granting payment deferrals to borrowers.

This gave many lenders leeway to provide relief without the need to reclassify loans with payment deferrals as non-performing. As of November 30, 2020, chartered banks had provided mortgage payment deferrals to over 797,900 Canadians.

Non-bank lenders, while not subject to the guidelines outlined by the OSFI, also provided payment deferrals to a further 100,372 Canadians—mainly for uninsured mortgages—during the second quarter.

Debt service ratio falls as households defer mortgage payments

The household debt service ratio is a measure of total obligated payments of principal and interest as a proportion of household disposable income. This measure does not include any deferred principal payments, which resulted in a lower debt service ratio than if borrowers had been obligated to pay.

The size of these deferrals as a proportion of total obligated payments of mortgage principal grew from less than 1% in the first quarter to a high of over 18% in the second quarter. By the third quarter, the proportion had fallen considerably, as the special capital treatment provided by OSFI on new approvals came to end on October 1, 2020.

Expected credit losses grow, but represent a small proportion of overall mortgage debt

As part of their risk management planning, financial institutions estimate the proportion of their loan portfolios that may enter default each quarter. These expected credit losses (ECL) are based on actuarial assumptions that attempt to anticipate the default rates on loans and subsequently the amount of impaired loans that may need to be written off in a given quarter.

While ECL on mortgage loans had been rising slowly from 2017 to the end of 2019, as the pandemic hit, banks' ECL increased sharply. However, these expected credit losses as a proportion of total household debt remained slight, accounting for 0.1% in the third quarter.

The study "Trends in the Canadian mortgage market: Before and during COVID-19" is now available as part of the series *Analysis in Brief* (**11-621-M**).

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