


# Finance Committee Submission, Canadian Real Estate Market and Home Ownership

January 30, 2017

Presented by
Stuart Levings, President & CEO, Genworth Canada

Good evening

Genworth Canada is this country's largest private sector mortgage insurer, with about 30% market share and CMHC's largest competitor.

The insurance we provide reimburses lenders for their losses when homebuyers default.

Mortgage insurance is mandatory for homebuyers who put less than 20 percent down. Thus, we primarily serve first time buyers.

With insurers taking default risk, lenders are able to offer first time buyers competitive interest rates, and have confidence to do so across Canada, throughout economic cycles.

We're housing risk aggregators with specialized expertise. We're well capitalized, tightly regulated and deeply experienced to properly manage mortgage related risks.

Regarding the topic of mortgage rule changes, I will speak to two key points:

1. The Government has made numerous changes in the insured mortgage segment over the past couple of years, some with impacts yet to be felt. To avoid a potential "tipping" point, it's critical that we take a pause and assess the cumulative impact prior to considering any additional changes, including the current risk sharing proposal.

2. The changes to date have largely targeted aspiring first-time buyers, making it harder for them to gain a foothold in the housing market today. Homeownership and the opportunity to build equity through the "forced savings" mechanism of a mortgage payment is an important cornerstone of the financial plan for many young families. We believe they aren't the problem and that further targeting of this segment is not the best solution.

Insured first-time buyers are the most tightly regulated, rigorously underwritten borrowers in the market today.

These buyers reside in all regions across Canada, range in age from 25 to 40[1] and they typically demonstrate stable employment with average household incomes of $80 to $100K[1]. They buy homes they can afford, often below market averages, especially in Toronto and Vancouver. Their credit scores reflect fiscally prudent, responsible borrowers, averaging 752[2] last year.[3]

[1] Company sources, Q3'16 YTD, transactional new insurance written, purchase only
[2] Company sources, Q3'16 YTD, transactional new insurance written
[3] https://www.thestar.com/business/personal_finance/spending_saving/2013/01/21/my-credit-score-is-788--what-does-it-mean.html As reported in the Toronto Star, Equifax classifies credit scores as: 350-559 Poor; 560 to 659 Fair; 660 to 724, Good; 725 to759 Very Good; and 760 and above, Excellent.

# Strong portfolio quality – credit score

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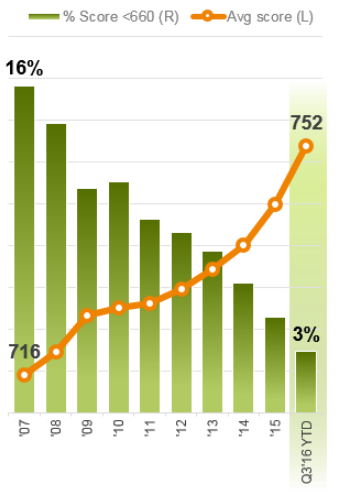
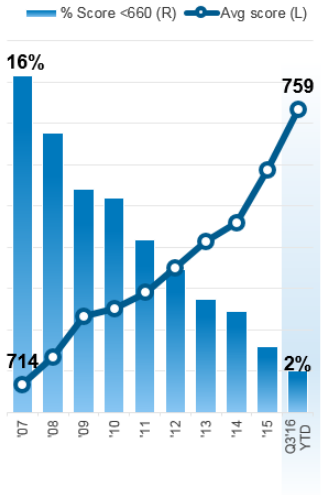
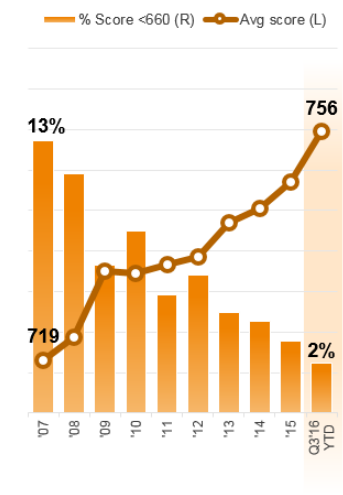
## Canada




## Greater Toronto Area




## Greater Vancouver Area




**PORTFOLIO QUALITY SIGNIFICANTLY IMPROVED COMPARED TO '07/08**

Note: Company sources for transactional new insurance written.

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# Conservative first-time homebuyer profile

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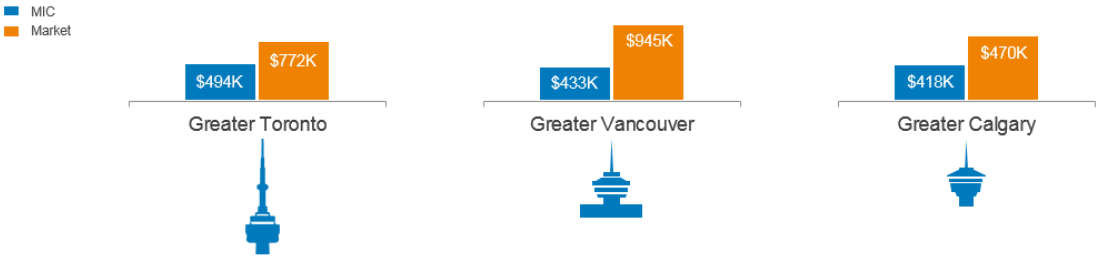
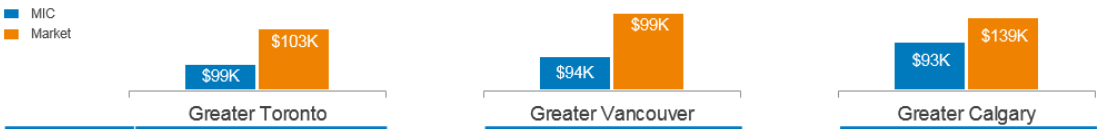
## Residential average prices well below market....




## ....with similar household median incomes




| MIC | Greater Toronto | Greater Vancouver | Greater Calgary |
|---|---|---|---|
| Avg GDSR | 29% | 27% | 27% |
| Avg TDSR | 36% | 36% | 36% |
| % Multiple Borrowers | 68% | 70% | 71% |
| % Condos | 25% | 35% | 9% |
| % Fixed Rate | 92% | 91% | 94% |

Data sources: CREA, TREB, Genworth (NIW purchase only); all data for Q4'16 except household median incomes (Q3'16); market income calculated using Statistics Canada national income and regional populations

Genworth MI Canada Inc.

Canada's mortgage finance system is a proven model. The rest of the world views our mortgage insurance structure as a best practice and key contributor to our mortgage finance stability.

During the Global Financial Crisis US delinquencies rose above 5%. By contrast, Genworth Canada's worst vintage year to date is 2007, which peaked in '09 at 0.95%.

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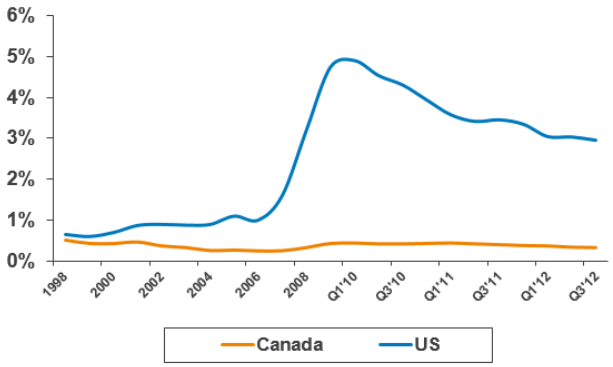
## Canada's MI industry is stable

The strength of the Canadian mortgage market

- Prime borrowers
- Strong credit culture
- Mortgage interest not tax deductible
- Borrower recourse
- Mandatory MI for high LTV (80%)
- No delegated underwriting

**Mortgage Delinquencies in Canada vs. U.S. (1994 – Q3 2012)**




Source: Canadian Bankers' Association; Mortgage Bankers' Association

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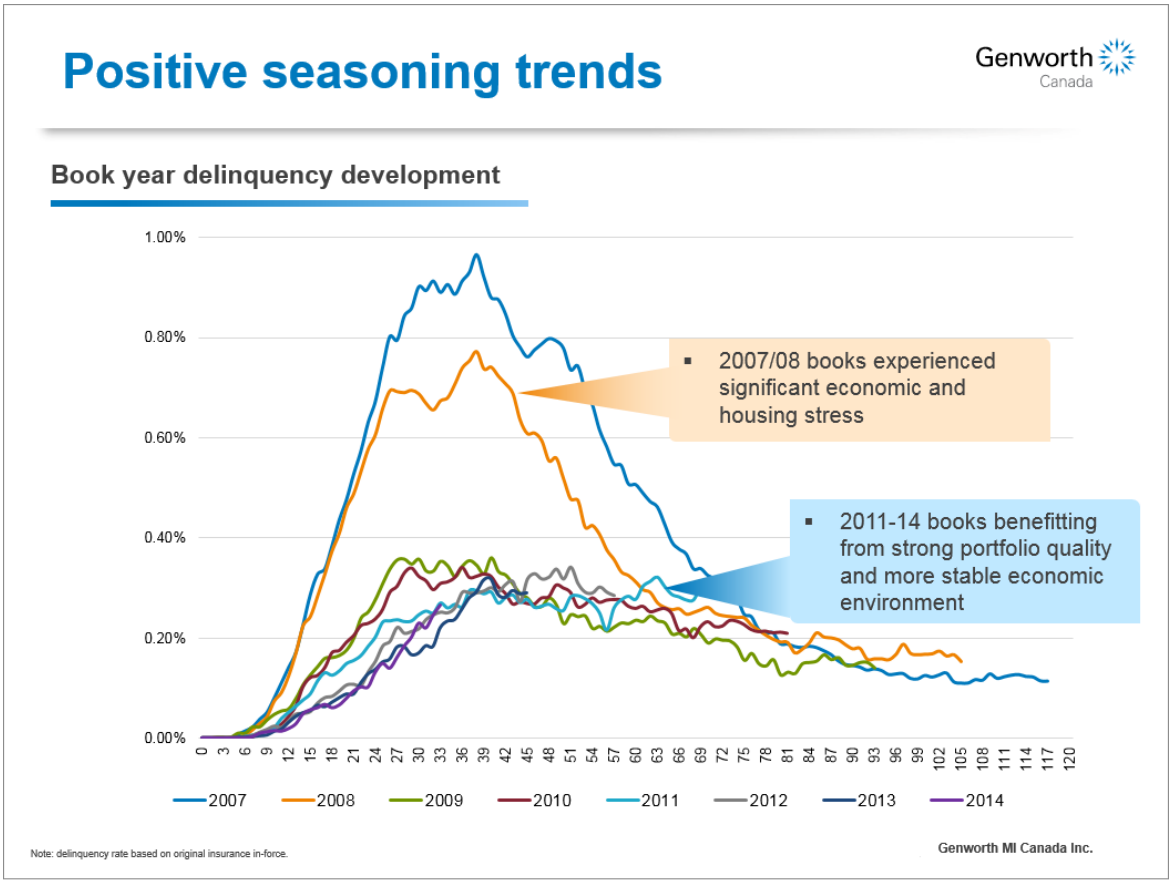


Our submission highlights nearly two dozen federal interventions since 2008, primarily targeting the insured market and first time buyers. While many of these changes have contributed to the overall strength of our mortgage finance system, some may have gone too far.

| | SPONSOR | MEASURE | DATE |
|---|---|---|---|
| Mortgage Insurer Changes | Dept of Finance | Mortgage Insurance Rules Change Round 1: Maximum Amortization 35 yrs on high ratio ; Minimum down payment 5%; Min credit score; loan documentation standards | October, 2008 |
| | Dept of Finance | Mortgage Insurance Rules Change Round 2: Buyers must qualify at 5 yr fixed; refi cap at 90% LTV; 20% down needed for MI backed non-owner occupied speculative homes | April, 2010 |
| | Dept of Finance | Mortgage Insurance Rule Change Round 3: Max Am 30 yrs on high ratio; refi cap at 85% LTV; MI withdrawal from HELOC market | March/April, 2011 |
| | Dept of Finance | Mortgage Insurance Rules Change Round 4: Max Am 25 yrs on high ratio; refi cap at 80% LTV; GDS capped at 39% & TDS 44%; $1M cap on high LTV insured loans | July, 2012 |
| | Dept of Finance | Mortgage Insurance Rules Change Round 5: Increase min down on homes over $500K (10% on portion above $500K | Implemented, February 2016 |
| | Dept of Finance | Mortgage Insurance Rules Change Round 6: Eligibility rules for high ratio products now applicable to low ratio (disqualifying refinances), all insured mortgages must qualify at Bank of Canada rate AND announcements of Foreign Buyer tax measures/ launch of Risk Sharing consultation | Implemented Oct/Nov, 2016 |

**See appendix A for more extensive list of changes*

The most recent changes last October, for example, are significant, the impacts of which have yet to be fully observed. I can't stress enough; it's going to take time before we know their total cumulative effect on the market.

We believe implementing any more changes could tip the market too far, creating the kinds of housing challenges these measures seek to prevent – hurting new buyers, existing homeowners, and the broader economy in the process.

Let me address the last two changes specifically.

In December 2015, the Government increased minimum down payments on homes selling over $500,000. While targeting the strong Toronto and Vancouver markets, these changes had an impact on other markets too.

- Calgary in particular, was hit quite hard, with approximately 12% of insured buyers affected by the change. As you know, this market was already under pressure and didn't need any additional cooling.

- In fact, only 13% cent of the Toronto/Vancouver buyers were making down payments small enough to be impacted, despite the much higher average house prices in these regions.

Given how little the first time buyer participates in these two cities, it's not surprising that despite these, and other changes to date, significant home price appreciation in Toronto and Vancouver continued. National solutions are perhaps ill-suited to address local market challenges. Recently Vancouver's market has started to slow, however it appears to be driven by a local solution to a local challenge, specifically foreign buyers.

Last October brought more changes, including an interest rate stress test for insured buyers. While we support the concept of a stress test, we believe the target rate was set too high.[4]

Let me be clear: This was a significant change. Under this new test, approximately one third of the first time buyers we approved in 2016 would now be offside.[5]

These buyers face stark choices: buy a less expensive home, perhaps a condo or further from work; ask their parents for more money, delay their purchase to save for a larger down payment; or consider a bundled loan from a private lender.

It's this option that should concern us most: pushing first time buyers into the private lending space, a segment that continues to grow as mortgage insurance rules tighten. This segment represents a higher cost option with limited transparency and regulatory oversight.

To conclude…

In 2010, the insured mortgage market represented approximately 40% of annual originations.[5] With the cumulative changes, it's expected to drop to around 20% this year.[5]

Home prices and related mortgage debt are growing the fastest in segments of the market not accessible to first time buyers. Yet even though they're not driving the problem, they're the ones absorbing all the consequences, making it even harder for them to access responsible home ownership.

The big question we need to ask is: What's the cumulative impact of all these changes: for home prices, demand, first time buyers, and the growing unregulated sector?

So What Should the Government Do?

- Take a pause – study the impact of all the changes made to date before considering any more.
- Modify the stress test to better reflect future rate expectations.
- Given the number of potentially damaging consequences, do not proceed with a risk sharing model.
- Finally – continue to work closely with other levels of Government to study and address individual housing markets at the regional level.

Thanks

[4] The new stress test forces all insured borrowers to qualify at the 5 year posted Bank Rate, an average of the posted rates of Canada's five largest lenders. The rate currently sits at 4.64% while the prevailing market rate is closer to 2.50%. The Posted Rate is primarily used to assess penalties for buyers who break their mortgage contracts. Genworth proposes that a new benchmark be found that is better aligned with Bank of Canada rate forecasts.

[5] Company estimate

APPENDIX A

| SPONSOR | MEASURE | DATE |
|---|---|---|
| Dept of Finance | Mortgage Insurance Rules Change Round 1: Maximum Amortization 35 yrs on high ratio ; Minimum down payment 5%; Min credit score; loan documentation standards | Implemented October, 2008 http://www.fin.gc.ca/n08/08-051-eng.asp |
| Dept of Finance | Mortgage Insurance Rules Change Round 2: Buyers must qualify at 5 yr fixed; refi cap at 90% LTV; 20% down needed for MI backed non-owner occupied speculative homes | Implemented April, 2010 http://www.fin.gc.ca/n10/10-011-eng.asp |
| Dept of Finance | Mortgage Insurance Rule Change Round 3: Max Am 30 yrs on high ratio; refi cap at 85% LTV; MI withdrawal from HELOC market | Implemented March/April, 2011 http://www.fin.gc.ca/n11/11-003-eng.asp |
| Dept of Finance | Mortgage Insurance Rules Change Round 4: Max Am 25 yrs on high ratio; refi cap at 80% LTV; GDS capped at 39% & TDS 44%; $1M cap on high LTV insured loans | July, 2012 http://www.fin.gc.ca/n12/12-070-eng.asp |
| Dept of Finance | Protection of Residential Mortgages or Hypothecary Insurance Act – (Legislates private insurer Guarantee Agreements with Government) | Implemented, January 2013 http://laws-lois.justice.gc.ca/eng/acts/P-25.7/FullText.html |
| Dept of Finance | CMHC – New powers for the Finance Minister | Announced, Budget 2012 http://www.fin.gc.ca/n12/data/12-050_1-eng.asp |
| Dept of Finance | CMHC – Now Subject to OSFI oversight | Announced, Budget 2012 http://www.fin.gc.ca/n12/data/12-050_1-eng.asp |
| Dept of Finance | CMHC – Governance Reform | Announced, Budget 2012 http://www.fin.gc.ca/n12/data/12-050_1-eng.asp |
| Dept of Finance | Covered Bond Framework | Announced, Budget 2012 http://www.budget.gc.ca/2012/rd-dc/brief-bref-2012-eng.pdf |
| OSFI | B20 Residential Mortgage Underwriting Practices and Procedures | Implemented, Q1 2013 http://www.osfi-bsif.gc.ca/Eng/fi-if/rg-ro/gdn-ort/gl-ld/Pages/B20_let.aspx |

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|---|---|---|
| OSFI | B21 Residential Mortgage Insurance Underwriting Practices and Procedures | Implemented June 30, 2015/Sep 2015 http://www.osfi-bsif.gc.ca/Eng/fi-if/rg-ro/gdn-ort/gl-ld/Pages/b21_let.aspx |
| Dept of Finance | CMHC to pay risk fee to Government of Canada of 3.25% of premiums written and 10 basis points on new portfolio insurance written | Implemented January, 2014 https://www.cmhc-schl.gc.ca/en/corp/about/core/upload/2013_Q3_QFR_Publication_English_Final.pdf (page 9) |
| OSFI | Own Risk and Solvency Assessment (for federally regulated insurers) | Implemented January, 2014 http://www.osfi-bsif.gc.ca/Eng/fi-if/rg-ro/gdn-ort/gl-ld/Pages/a4e19_let.aspx |
| CMHC | CMHC retreats from Second Home and Self-employed Without 3rd Party Income Validation products | Implemented May, 2014 https://www.cmhc-schl.gc.ca/en/hoficlincl/moloin/moloin_014.cfm |
| CMHC | CMHC caps new guarantees under its securitization programs | Announced August , 2013 http://globalnews.ca/news/763918/cmhc-limits-guarantees-for-mortgage-lenders/ |
| Dept of Finance | Amend NHA/PRMHIA Regulations – Amending the Eligible Mortgage Loans Regulations – Purpose Test (Prohibits use of taxpayer backed insured mortgages as collateral in securitization vehicles that are not sponsored by CMHC | May 2015 http://www.gazette.gc.ca/rp-pr/p1/2015/2015-06-06/pdf/g1-14923.pdf |
| CMHC | CMHC announces premium increases | Implemented June , 2015 https://www.cmhc-schl.gc.ca/en/corp/nero/nere/2015/2015-04-02-1605.cfm |
| CMHC | CMHC announces increases to guarantee fees for both NHA MBS/CMB | Implemented July 2016 https://www.cmhc-schl.gc.ca/en/corp/nero/nere/2015/2015-12-11-0900.cfm |
| Dept of Finance | Mortgage Insurance Rules Change Round 5: Increase min down on homes over $500K (10% on portion above $500K | Implemented, February 2016 http://www.fin.gc.ca/n15/15-088-eng.asp |

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|---|---|---|
| Dept of Finance | Mortgage Insurance Rules Change Round 6: Eligibility rules for high ratio products now applicable to low ratio (disqualifying refinances), all insured mortgages must qualify at Bank of Canada rate AND announcements of Foreign Buyer tax measures/ launch of Risk Sharing consultation | Implemented Oct/Nov, 2016 http://www.fin.gc.ca/n16/16-117-eng.asp |
| Department of Finance | CMHC Securitization Programs - Substitutions Regulations via PRMHIA/NHA | Registered May 15, 2015 http://www.gazette.gc.ca/rp-pr/p2/2015/2015-06-03/pdf/g2-14911.pdf |
| OSFI | New Capital Model for Mortgage Insurers – Increasing capital on certain mortgages, increasing target Minimum Capital | Implemented January, 2017 http://www.osfi-bsif.gc.ca/Eng/fi-if/rg-ro/gdn-ort/adv-prv/Pages/cptins_gias.aspx |
| CMHC | Premium Hike | To be Implemented March, 2017 https://www.cmhc-schl.gc.ca/en/corp/nero/nere/2017/2017-01-17-0830.cfm |
| Select Provincial Measures, since 2008 | • Numerous provinces have amended conduct codes for Realtors and Mortgage Brokers<br>• Numerous provinces have amended Condominium Acts (including Reserve rules)<br>• Various jurisdictions have amended Land Transfer Tax rebates for first time buyers<br>• BC moved in 2016 to tax foreign buyers http://www.bnn.ca/b-c-introduces-15-real-estate-tax-targeting-foreign-homebuyers-1.532374 | |