



## TD Economics

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### Release: Department of Finance tightens CMHC rules

- For the second time in twelve months, the Department of Finance tightened rules on residential mortgages to help slow the pace of household debt accumulation. Changes include shortening the amortization period to 30 years (which had already been shortened from 40 to 35 years in 2008), withdrawing CMHC insurance of home equity lines of credit (HELOC), and a reduction in the maximum refinance percentage from 90% loan-to-value to 85%. Changes to the amortization period and the refinancing ratio will take effect March 18 and the HELOC change will take effect April 18, 2011.

### Key Implications

- The amortization change may alter the quarterly profile of housing market activity as some sales are pulled forward by households to pre-empt it. But the impact is not expected to be large, nor does it lead us to alter our annual forecast. Existing home sales were already forecast to weaken by about 8% compared to 2010, and prices to slip by a modest 1%. On aggregate, our calculations suggest that 20K sales (annually) may be impacted by the amortization change, with the average price likely to weaken a further percentage point. However, while the last few months of data represented upside risk to our December forecast, today's measures put our forecast back on track.
- The other two changes are more likely to impact consumer durables and housing-related spending. For instance, household usage of HELOCs is mostly directed towards renovations, vehicle purchases, and debt consolidation. Yet, on that front as well, the impact is not expected to be large. Our macroeconomic forecasts already embedded a significant slowdown in household debt accumulation and consumer durable spending. The withdrawal of HELOC insurance may cause some substitution toward more traditional mortgages, but very few financial institutions insure their HELOC portfolios. As such, the change is unlikely to register significantly on the aggregate lending scale. Moreover, less than a fifth of refinancing deals are high loan-to-value (LTV >80%), and lowering the LTV threshold to 85% likely impacts less than a tenth of refi loans through lower amounts and/or alternative vehicles. All said, aside from some distortion on the timing of some heavily credit-dependent activities, the policy changes do not alter our forecasts.
- In terms of monetary policy, this helps take some pressure off the Bank of Canada (BoC). With all the talk about the non-sustainable pace of household debt accumulation, there was speculation about whether or not the BoC would consider hiking interest rates for reasons not directly related to its inflation-targeting mandate. Such speculation can be put to rest for the time being, and we can go back to focusing on the inflation outlook.

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