

Consumer Mortgage Choices In a Changing Market



Prepared for:

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By:

Will Dunning

CIMBL Chief Economist

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Introduction and Summary

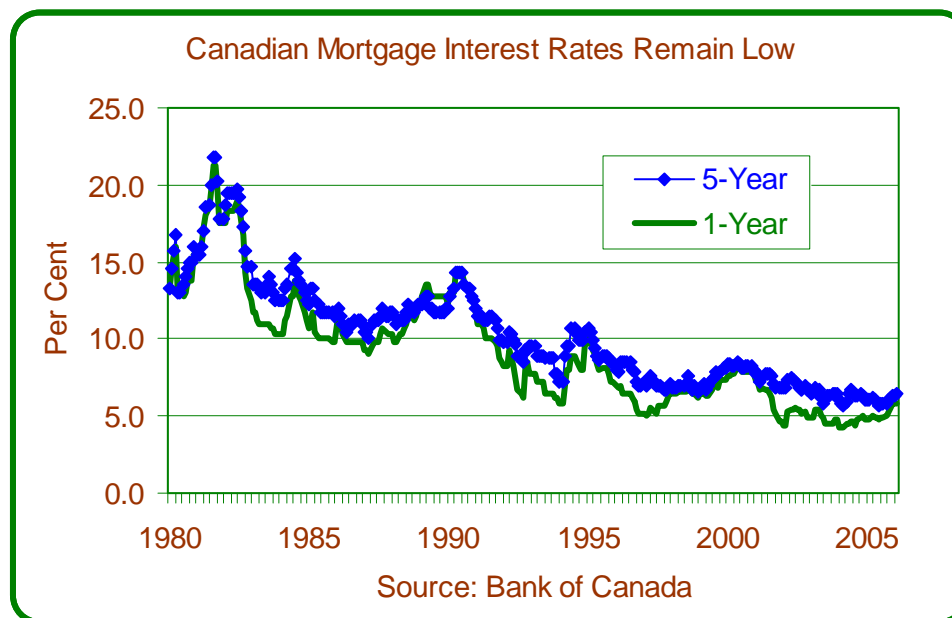
Background

This research project was conducted for the Canadian Institute of Mortgage Brokers and Lenders (“CIMBL”) by Will Dunning, Chief Economist of CIMBL.

During the past decade Canadian mortgage borrowers have benefited from reductions in mortgage rates. As shown in the chart below, in recent years the rates for one year and five year mortgages have been at the lowest levels in a generation. However, interest rates have risen from those lows during the past half year.

- As of late March 2006, the rate for one year mortgages is 1.5 percentage points above the record lows seen in early 2004.
- The rate for five year mortgages has increased by three-quarters of a percentage point from the lows seen in the summer of 2005.
- Despite these increases, mortgage interest rates remain very low.
- Furthermore, in the competitive mortgage marketplace, actual rates are typically 1.00 to 1.35 percentage points below the advertised rates that are shown in the chart. At the time of writing typical rates after negotiated discounts might be 4.9% for a one year term and 5.1% for a five year term. For variable rate mortgages, a 4.75% rate would be typical.

It isn't clear whether the recent increases in rates represent a turning point in the interest rate cycle – which would be followed by additional increases - or whether this is a short-term fluctuation.



In a time of change and uncertainty about interest rates, CIMBL and the mortgage professionals that it represents are interested in exploring the impacts on Canadian mortgage consumers and the choices that they make:

- Will their mortgage renewal behaviour be changed, in selection of terms (length of time before their next renewal) or types of mortgages (fixed rate, variable rate, or combination mortgages)?
- To what extent will mortgage holders renew early – before their scheduled renewal dates?
- What are the impacts of rising rates on the household finances of mortgage holders?
- What are consumers' expectations about future directions in mortgage rates?

Data for this research study was collected by Pollara, a national public opinion and market research company, via a 14-question telephone survey with 1,015 residential mortgage holders across the country. A sample of 1,015 Canadians ensures an accuracy of $\pm 3.1\%$, nineteen times out of twenty. The survey was conducted during February 2006.

Summary

Types of Mortgages

Fixed rate mortgages remain the most popular type of mortgage in Canada, accounting for 67% of the total. Among the two other categories, variable rate mortgages account for 22% of the total. A relatively new type of combination mortgage, in which some of the mortgage is based on a fixed rate and some is based on variable rates, accounts for 11% of mortgages.

Choices of mortgage types change over time.

- Among those who have renewed their mortgages recently, there has been some shifting away from fixed rate mortgages, to variable rate and combination mortgages.
- When mortgage holders were asked what type of mortgage they expect to choose when they renew their mortgages, among those who expressed an opinion, fixed rate mortgages were mentioned by 56% (lower than the current share of 67%). 19% said they would choose a variable rate mortgage (down slightly from the current share of 22%). It appears that the share will rise for combination mortgages, as these were mentioned by 24% (substantially above the current share of 11%).

Mortgage Renewal Activity

During the past six months close to one fifth of mortgage holders (18%) have renewed their mortgages. About 10% of borrowers renewed on schedule and about 7% renewed before the scheduled date.

Mortgage Rates

For the mortgages currently held by Canadians, the average mortgage interest rate is 4.9%, which is quite similar to the rates that are currently available for new and renewed mortgages. However, of course, individual circumstances vary:

- Estimates developed in this study suggest that if rates remain at current levels, 62% would face increased interest rates at their next renewal, 35% would have decreases, and 3% would have no change in their interest rate.
- For those scheduled to renew in the next 12 months 50% would have increased interest rates, 47% would have decreases, and 3% would have no change.
- For those expecting to renew early, 54% would have increased rates, 44% would have reductions, and 2% would have no change.

Impacts of Recent Changes in Mortgage Rates

About one-quarter of mortgage holders say that recent increases in mortgage rates have negatively affected their standard of living. On the other hand, almost 20% say recent changes in rates have positively affected their standard of living – although rates have increased recently, they are lower than they were a few years ago and many mortgage borrowers are saving money when they renew. Overall, the impact of recent changes in rates is negative.

The negative impacts are greatest for holders of variable rate mortgages, while the effects are more mixed for those with fixed rate and combination mortgages.

Consumers' Expectations About Future Changes in Mortgage Rates;

Most mortgage holders (66%) expect that mortgage rates will increase in the near future. Very few of them (3%) think that rates will decrease. About one-quarter (26%) expect rates to stay the same. Just 6% have no opinion on this question.

Impact of Rising Rates on Mortgage Shopping

About one-third of mortgage holders say that they would look for more mortgage quotes if mortgage rates rise.

Future Mortgage Renewals

About 15% of mortgages are scheduled for renewal during the coming year. This appears to be a stable proportion, as the fall 2005 CIMBL report found that 15% of mortgages had a renewal on schedule during the prior year.

As well, about 15% of mortgage holders think they will renew before their scheduled renewal date. Early renewal is most common for people who are close to their scheduled renewal date, and decide to renew a few months early. Among those whose renewal date is a year or more distant, about one-tenth think they will renew early.

Expected Mortgage Terms at Next Renewal

Overall, about one-tenth of the consumers expect to choose a term of less than one year. Long terms (5 or more years) are no more popular, as only 11% expect to choose a term of 5 years or longer. Most consumers prefer mid-length terms ranging from 2 years to less than 5 years.

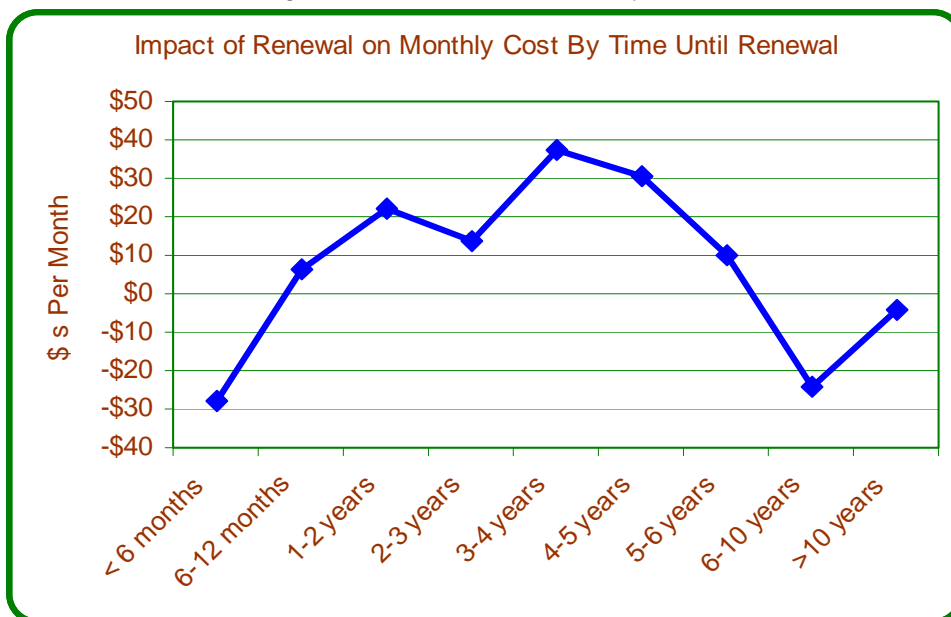
People who will renew during the next two years are much more likely to select a short term for their next mortgages, including 9% who would select a term of less than 6 months and 12% who would select a term of 6 to 12 months. Long term mortgages are even less popular with this group, as just 6% would choose a mortgage with a term of 5 years or longer.

Potential Increases in Consumers' Monthly Mortgage Payments

It is estimated that at current interest rates, mortgage renewals would cause monthly interest payments to rise by a small amount - about \$21.50 on average, once all mortgage renewals have occurred. For Canada's 4.6 million home owners with mortgages, the total cost, once all have renewed, would be about \$1.17 billion per year.

The impacts vary over time:

- For those who renew during the next six months, the average impact is a reduction of \$28 per month. This occurs because the average interest rate after renewal will be lower than before renewal.
- For those renewing during the next six to twelve months, small increases are expected - an average of about \$6 per month.
- For those renewing during the next 1 to 6 years, average costs will rise.
- The small number of mortgage holders that have 6 or more years remaining in their terms will on average see reductions after they renew.



Potential Impacts of Rate Increases on Consumers

Consumers vary in their ability to absorb rising interest rates. The survey asked the mortgage holders to identify the thresholds at which increased mortgage payments would have a significant impact on their overall standard of living. The responses showed that the impacts begin with relatively small rises in costs: a \$50 increase in monthly cost would have a significant impact for 10% of mortgage holders, and a further 11% would be affected by a rise of \$50 to \$100.

Combining the responses on thresholds with the changes in monthly costs that have been estimated here, about 9% of mortgage borrowers will face cost increases at or above their thresholds for “a significant impact” on their standard of living. 91% would see no increase in the monthly cost, or an increase that is below their threshold.

Potential Impacts of Further Increases in Mortgage Rates

If mortgage interest rates rise by a further one-half of a percentage point, total interest costs, after all mortgage holders have renewed their mortgages, would increase by \$3.9 billion per year, versus the \$1.17 billion increase that is expected at current rates. For 18% of mortgage holders, the cost increases would cross their threshold for a “significant impact” on their overall standard of living.

An increase of one percentage point from current rates would bring the increase to \$6.7 billion. Close to one-third (29%) of mortgage holders would cross their thresholds for a “significant impact”, but the majority (71%) would not cross their thresholds.

About CIMBL

CIMBL is the national organization representing Canada's mortgage industry. With over 8,200 mortgage professionals, its membership is drawn from every province and from all industry sectors. This diversified membership enables CIMBL to bring together key players with the aim of enhancing professionalism.

Established in 1994, CIMBL has taken a leadership role in Canada's mortgage lending industry and has set the standard for best practices in the industry.

CIMBL's other primary role is that of consumer advocate. On an ongoing basis CIMBL aims to educate and inform the public about the mortgage industry. Through its extensive membership database, CIMBL provides consumers with access to a cross-country network of the industry's most respected and ethical professionals.

About the Author

Will Dunning is an economist (BA, MA), and has specialized in the analysis and forecasting of housing markets for the past 24 years. In addition to being Chief Economist for CIMBL he operates an economic analysis consulting firm, Will Dunning Inc.

About Pollara

Pollara is the largest Canadian-owned public opinion and marketing research firm, providing a full range of research services to leading global, national and local companies as well as public and non-profit sector organizations. Pollara is particularly distinguished for its financial services practice, providing quantitative and qualitative research and counsel on customer value/satisfaction, new product development, advertising testing and tracking, branding, consumer demand and pricing models and public affairs/public policy.

Current Situation

This section looks at current characteristics of residential mortgages in Canada, using data from a consumer survey that was conducted during February 2006. It begins with data on the ages of mortgage holders and then examines:

- The sizes (remaining principal balances) of mortgages.
- The types of mortgages chosen by consumers.
- Actual interest rates on the mortgages currently held.
- The extent to which mortgages have been renewed recently, and the choices that have been made.
- The impacts of recent increases in mortgage rates on consumers' financial situations.

Ages of Mortgage Holders

Most mortgage holders (over 80% of the total) are in the age groups from 25 to 54; just 3% are aged 18 to 24, or 65 years and over; and 12% are aged 55 to 64.

<i>Age Group</i>	<i>% of All Mortgage Holders</i>	<i>Average Remaining Principal</i>
18-24	3%	\$108,404
25-34	21%	\$138,983
35-44	35%	\$123,239
45-54	25%	\$95,384
55-64	12%	\$111,355
65 +	3%	\$81,750
Total	100%	\$116,821

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.

Remaining Mortgage Principals

The survey found that on average the remaining mortgage principal is about \$116,800, as is shown in the table above. Looking at age groups, the highest remaining principals are for people in the 25-34 and 35-44 brackets, and lower for the older age groups.

Types of Mortgages

Mortgages have been grouped into three types:

- Fixed rate (where the rate is fixed for the entire term of the mortgage).

- Variable rate (where the rate is adjusted periodically based on changes for other “benchmark” interest rates).
- Combination mortgages (where a fixed rate applies to some of the mortgage amount and a variable rate applies to the remainder).

As is shown in the following table, fixed rate mortgages are most common, accounting for two out of three current mortgages. Variable rate mortgages are a substantial minority, at 21% (22% if “don’t know” and “refused” responses are excluded from the calculation). Combination mortgages are a relatively new option and account for one-tenth of mortgages.

<i>Type of Mortgage</i>	<i>% of All Mortgages</i>	<i>% Excluding Don't Know / Refused</i>
Fixed Rate	65%	67%
Variable Rate	21%	22%
Combination	10%	11%
Don't Know / Refused	4%	
Total	100%	100%

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.

The following table looks at mortgage types by age group. It indicates that younger age groups are more likely than older groups to have a combination mortgage. The younger half of the age distribution (up to 44 years) is less likely to have a fixed rate mortgage than is the upper half (45 years and older). Variable rate mortgages are most common for the oldest age group shown (65 years and older). It was shown earlier that there are relatively few mortgage holders in this age group and therefore the number of Canadians aged 65 and older who have variable rate mortgages is limited.

<i>Age Group</i>	<i>Fixed Rate</i>	<i>Variable Rate</i>	<i>Combination</i>	<i>Don't Know / Refused</i>	<i>Grand Total</i>
18-24	59%	10%	23%	9%	100%
25-34	62%	24%	11%	3%	100%
35-44	63%	21%	12%	3%	100%
45-54	70%	17%	7%	6%	100%
55-64	70%	22%	8%	0%	100%
65 or over	50%	39%	5%	5%	100%
Total	65%	21%	10%	4%	100%

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.

As shown in the next table, across the regions of Canada, about two-thirds of mortgages have fixed rates, with the exception of Alberta: in Alberta there is more use of variable rate and combination mortgages than in the other regions.

<i>Region</i>	<i>Fixed Rate</i>	<i>Variable Rate</i>	<i>Combination</i>	<i>Don't Know / Refused</i>	<i>Grand Total</i>
Atlantic	64%	20%	14%	1%	100%
Quebec	68%	17%	11%	4%	100%
Ontario	66%	24%	8%	2%	100%
Manitoba & Saskatchewan	69%	15%	14%	1%	100%
Alberta	52%	26%	14%	8%	100%
British Columbia	65%	22%	7%	6%	100%
Total	65%	21%	10%	4%	100%

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.

Mortgage Interest Rates

The average mortgage interest rate, as of the survey date in February 2006 is below 5%, at an average of 4.86%.

- As shown in the following table, rates are lower for variable rate mortgages: at an average of 4.4% those rates are not appreciably different than the 4.5% rate that might have been negotiated at the time of the survey (or the 4.75% rate that is typical at present). This is not surprising, since the rates are adjusted in accordance with market rates.
- For fixed rate mortgages and combination mortgages, the current rates of mortgage holders average 5.0%. This is in line with the rates that might be negotiated today: as was note in the Introduction section, typical negotiated rates at present are 4.9% to 4.95% for one year terms and 5.1% for five year terms. It is a coincidence that the actual rates on existing mortgages, which were negotiated in the past, should be roughly equal to the rates that might be negotiated today. As is explored below, this has important implications for future mortgage renewals.

<i>Type of Mortgage</i>	<i>Average Interest Rate</i>
Fixed Rate	5.0%
Variable Rate	4.4%
Combination	5.0%
All Mortgages	4.9%

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc

The next table looks at the distribution of actual rates reported by Canadian mortgage holders. An interesting finding is that one in five (21%) mortgage holders reported that they didn't know their mortgage rate.

In the right hand column of the table those who didn't know their mortgage rate are excluded from the calculation. It shows that about one in ten mortgages (11%) have

rates below 4% (including 3% that have rates below 3.0%, 2% that have rates from 3.0% to 3.49%, and 6% have rates from 3.5% to 3.99%.

Most mortgages (69%) have rates in the range 4.0% to 5.49%. 20% of mortgages have rates of 5.5% or higher.

<i>Mortgage Rate</i>	<i>% of Total</i>	<i>Excluding Don't Know / Refused</i>
Less than 3.00%	2%	3%
3.00% - 3.49%	2%	2%
3.50% - 3.99%	5%	6%
4.00% - 4.49%	15%	19%
4.50% - 4.99%	23%	29%
5.00% - 5.49%	16%	21%
5.50% - 5.99%	5%	6%
6.00% - 6.49%	5%	6%
6.50% - 6.99%	2%	3%
7.00% higher	3%	4%
Don't Know	21%	
Refused	2%	
Total	100%	100%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.		

Recent Renewal Activity

During the past six months close to one-fifth of mortgage holders (18%) have renewed their mortgages. This includes 10% who renewed on schedule (at the end of the mortgage term) and 7% who renewed before the term was completed.

Renewed	Renewed on Schedule	10%
	Renewed Early	7%
	Don't Know/Refused	< 1%
Did Not Renew		82%
Don't Know/Refused		< 1%
Total		100%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.		

Looking at just those mortgage holders who have renewed in the past six months, 42% renewed early and 58% renewed on schedule. In CIMBL's earlier report on "*The State of the Residential Mortgage Market in Canada*" (October 2005), there was an identical

finding: among those who had renewed during the previous year, 42% had renewed early and 58% had renewed on schedule. Thus, it appears that recent increases in mortgage rates have not led to more early renewals.

In terms of mortgage types - fixed rate, variable rate, and combination mortgages – there has been some shifting. The next table shows that among mortgage holders who have renewed during the past year, there has been some movement away from fixed rate mortgages (from 71% before renewal to 65% after renewal). The largest increase was in the variable rate category (from 19% before renewal to 24% after renewal). Combination mortgages are a recent innovation and are gaining popularity. Among these renewers, just 5% had combination mortgages before renewal but the share for this type increased to 8% after renewal.

<i>Type of Mortgage</i>	<i>Type Before Renewal</i>	<i>Type After Renewal</i>
Fixed	71%	65%
Variable	19%	24%
Combination of fixed and variable	5%	8%
Don't know/refused	0%	3%
Total	100%	100%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.		

The table above looks at overall changes. But, a closer examination of changes made by individuals shows that there was even more switching. The next table shows that:

- Among mortgage holders who had a fixed rate mortgage before their renewal, about three-quarters (74%) continued to use a fixed rate mortgage after the renewal. About one-fifth (19%) of those who had fixed rate mortgages switched to variable rates and 6% switched to combination mortgages.
- Among those who previously had a variable rate mortgage, only one-third (34%) chose to remain on a variable rate. Most switched to different types of mortgages. This included 56% who switched to fixed rate mortgages and 2% who switched to combination mortgages.
- Among those who previously had a combination mortgage, most (62%) continued with that type, and over one-third switched to different types. This includes 20% who switched to fixed rates and 18% who switched to variable rates.

<i>Type Before Renewal</i>	<i>Type After Renewal</i>				
	Fixed	Variable	Combination of fixed and variable	Don't know/refused	Total
Fixed	74%	19%	6%	1%	100%
Variable	56%	34%	2%	8%	100%
Combination of fixed and variable	20%	18%	62%	0%	100%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.					

Impacts of Recent Changes in Mortgage Interest Rates

The survey asked the mortgage holders to what extent recent changes in mortgage rates had an impact on their overall standard of living. Responses were recorded in a 10-point scale, where “1” means a very negative impact and “10” means a very positive impact. In the following table, the responses have been grouped into:

- “Strongly negative” (scores of 1 or 2),
- “Somewhat negative” (scores of 3 or 4),
- “Neutral” (scores of 5 or 6),
- “Somewhat positive” (scores of 7 or 8), and
- “Strongly positive” (scores of 9 or 10).

Slightly over one-quarter (27%) of the mortgage holders rated the impact as either strongly negative or somewhat negative. On the other hand, 17% rated the impact as positive (either somewhat positive or strongly positive) – not all consumers have experienced negative impacts:

- Some borrowers who have renewed recently have seen their rates fall, because even though rates have increased recently, the five year mortgage rate is still lower than it was a few years ago.
- Some borrowers who previously had long-term fixed rate mortgages may have shortened their terms or switched to variable rate mortgages, which would result in lower costs.

The last line in the table shows that the “balance of opinion” (positive responses minus negative responses) is -10%: overall, these mortgage consumers rate the impacts as negative.

<i>Impact</i>	<i>% of Total</i>
Strongly Negative	15%
Somewhat Negative	12%
Neutral	42%
Somewhat Positive	13%
Strongly Positive	5%
Don't Know/Refused	13%
Total	100%
Balance of Opinion	-10%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.	

The next table looks at the responses in more detail. It is reasonable to expect that the impact from rising mortgage rates will be more negative for borrowers with variable rate mortgages than the other types. To test this, the next table looks at the balance of

opinion by type of mortgage, separating borrowers who have renewed and those who haven't. There are some surprising results.

- Not surprisingly, among those who have not renewed, the balance of opinion is significantly more negative for those with variable rate mortgages (-22%, more than double the scores for fixed and combination mortgages).
- Among those who have renewed and have a fixed rate mortgage, the balance of opinion is negative.
- The most surprising result is that among those who have renewed, who have variable rate and combination mortgages, the balance of opinion is essentially "nil". This may indicate that in the course of negotiating their new mortgage, many of these borrowers achieved some savings. For example, they might have switched from a fixed rate mortgage that had a higher interest rate.
- Also surprising is that for borrowers with fixed rate mortgages, those who have not renewed have essentially the same balance of opinion as those who have renewed. Explanations include that among those who haven't yet renewed, many may be anticipating that they will be negatively impacted when they renew in future.

<i>Type of Mortgage</i>	<i>Not Renewed</i>	<i>Renewed</i>
Fixed Rate	-8%	-9%
Variable Rate	-22%	-1%
Combination	-9%	1%
Don't Know / Refused	-6%	10%
Total	-11%	-6%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.		

Looking Ahead

This section provides survey results on future mortgage activities, and considers the potential impacts of recent increases in mortgage interest rates on consumers. Among the topics covered are:

- What are consumers' expectations about future mortgage rates?
- Will higher rates affect their shopping behaviour?
- How many mortgage renewals will be occurring in future?
- How many consumers expect to renew their mortgages before the scheduled renewal dates?
- What choices do consumers expect to make?

Consumers' Expectations About Future Changes in Mortgage Rates;

Two-thirds of mortgage holders (66%) expect that mortgage rates will increase in the near future, while just a very small minority (3%) thinks that rates will decrease. About one-quarter (26%) expect rates to stay the same.

<i>Response</i>	<i>% Responding</i>
Increase	66%
Decrease	3%
Stay the Same	26%
Don't Know	6%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc	

Impact of Rising Rates on Mortgage Shopping

The mortgage consumers were asked to speculate: compared to the last time you arranged a mortgage "if mortgage rates rise, are you going to be looking for more quotes, fewer quotes, or about the same number of quotes when you shop around for your next mortgage?" Slightly more than one-half said they would look for about the same number of quotes. A significant minority (35%) thought they would look for more quotes.

<i>Response</i>	<i>% Responding</i>
About the Same Number of Quotes	54%
More Quotes	35%
Fewer Quotes	3%
Don't Know / Refused	8%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.	

Anticipated Mortgage Renewals

Mortgage holders were asked when their mortgage would be up for renewal. The table below summarizes the responses, showing the percentage responses for each time period. The first column of numbers shows the percentages including responses of “don’t know” and “refused”. The second column shows the percentages excluding those responses. It shows that:

- 9% of the mortgages are scheduled for renewal during the next six months. This is very similar to the 10% that actually had a scheduled renewal in the previous six months.
- A further 6% are scheduled for renewal during the next 6 to 12 months. Combining the renewals during the next six months with those that are scheduled for 6 to 12 months, 15% are scheduled to be renewed during the coming year. In the fall 2005 survey it was found that the same percentage (15%) of mortgages had a scheduled renewal during the previous year.
- This combination of findings indicates that the percentage of mortgages that have scheduled renewals during the coming year will be very similar to recent experience.
- An additional 14% of mortgages are scheduled to be renewed during the next one to two years. In total, therefore, 29% of mortgages are scheduled for renewal during the coming two years.
- 70% of mortgages have 2 or more years before their scheduled renewals.
- Only 6% of mortgages have 5 or more years before their scheduled renewal.
- 1% will not be renewed.

<i>Time to Renewal</i>	<i>% of Total</i>	<i>% Excluding “Don’t Know / Refused”</i>
Less than 6 months	8%	9%
6 to 12 months	6%	6%
1 to less than 2 years	13%	14%
2 to less than 3 years	17%	18%
3 to less than 4 years	20%	21%
4 to less than 5 years	23%	24%
5 to less than 6 years	1%	1%
6 to less than 10 years	3%	4%
More than 10 years	1%	1%
Will not be renewing	1%	1%
Don’t Know / Refused	6%	
Total	100%	100%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.		

Anticipated Early Renewals

Most mortgage holders (73%) expect that they will wait until their scheduled renewal date. However, a substantial proportion of mortgage holders (15%) think they will renew their mortgage before their scheduled renewal date.

<i>Response</i>	<i>Per Cent</i>
No	73%
Yes	15%
Don't Know	12%
Total	100%

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.

As is shown in the next table, among mortgage holders whose scheduled renewal is in the near future, a high percentage expects to renew early; among those whose scheduled renewal is within the next six months, almost one half expect to renew earlier than scheduled; for those whose renewal is within 6 to 12 months, almost one-third expect to renew early. For those whose renewals are more distant, about one-tenth expect to renew early. This pattern makes sense: people whose mortgages will be renewed in the near future are interested in locking in current rates; for the others, because of uncertainty about rates further into the future they are prepared to wait and see.

<i>Remaining Term</i>	<i>No</i>	<i>Yes</i>	<i>Don't Know</i>	<i>Total</i>
Less than 6 Months	43%	45%	12%	100%
6 to 12 Months	61%	29%	10%	100%
1 to Less than 2 Years	81%	10%	10%	100%
2 to Less than 3 Years	75%	9%	15%	100%
3 to Less than 4 Years	76%	12%	12%	100%
4 to Less than 5 Years	81%	11%	8%	100%
5 or More Years	76%	9%	15%	100%
Don't Know / Refused	68%	13%	19%	100%
Total	73%	15%	12%	100%

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.

Expected Consumer Choices at Renewal

The mortgage consumers were asked about their expected choices for their next mortgage term, including the length of the term and the type of mortgage.

As shown in the next chart, only one-tenth of the consumers, in total, expect to choose a term of less than one year. This includes 4% who expected to choose a term of less than 6 months and a further 6% who expect to choose a term of 6 to 12 months. A further 8% would choose a term of 1 year to less than 2 years. Long terms (5 or more years) are no more popular, as only 11% expect to choose a term of 5 years or longer (this includes 4% who selected a term of 5 to less than 6 years; 5% selecting a term of 6 to less than 10 years; and 3% who selected 10 or more years). Most consumers prefer mid-length terms ranging from 2 years to less than 5 years.

Looking in more detail, there is a different pattern. Those with renewal dates within the next two years are much more likely to select a short term for their next mortgage, including 9% who would select a term of less than 6 months and 12% who would select a term of 6 to 12 months. Long term mortgages are even less popular with this group, as just 6% would choose a mortgage with a term of 5 years or longer.

A high percentage of mortgage consumers are unsure what term they will select, as 21% replied that they didn't know what term they will select and 1% declined to answer this question. Interestingly, those for whom the renewal is closest in time were no more likely to have made up their minds.

<i>Expected Term Selection</i>	<i>Time Remaining Until Scheduled Renewal</i>			
	<i>Less than 2 years</i>	<i>2 years to less than 4 years</i>	<i>4 or more years</i>	<i>Total</i>
Less than 6 months	9%	3%	1%	4%
6 to 12 months	12%	4%	4%	6%
1 to less than 2 years	17%	5%	3%	8%
2 to less than 3 years	8%	10%	4%	7%
3 to less than 4 years	8%	7%	6%	7%
4 to less than 5 years	19%	40%	46%	35%
5 to less than 6 years	4%	3%	4%	4%
6 to less than 10 years	1%	5%	8%	5%
More than 10 years	1%	1%	6%	3%
Don't know / Refused	21%	22%	18%	22%
Total	100%	100%	100%	100%

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.

The next chart summarizes the responses on the types of mortgages that consumers expect to select at their next renewal.

- In the first column it shows the expected choices, including responses of “don't know” and “refused”.
- The second column shows the percentages for each of the three mortgage types excluding the “don't know” and “refused” responses. It indicates that over one-half of mortgage consumers would choose fixed rate mortgages at their next renewal.
- The last column shows the percentage shares at present: the 56% future share for fixed rate mortgages would be a substantial reduction compared to the current actual share of 67%. Variable rate mortgages will essentially maintain their share, at about 20%. Based on these current expectations of consumers, the share for combination mortgages would more than double, to about one-quarter.

<i>Type of Mortgage</i>	<i>Expected Future Choice</i>		<i>% of Current Mortgages</i>
	<i>% of Responses</i>	<i>% Excluding Don't Know / Refused</i>	
Fixed	42%	56%	67%
Variable	14%	19%	22%
Combination	18%	24%	11%
Don't know	24%		
Refused	1%		
Total	100%	100%	100%

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.

Mortgage Interest Rates of Current Mortgages

It was shown earlier than the current average mortgage interest rate is 4.9%. Looking more closely:

- For consumers with scheduled renewals during the next six months, the current average mortgage rate is 5.3%. This is higher than the rates that are currently available: for fixed rate mortgages current rates, after negotiated discounts, range from 4.95% to 5.1%; for variable rate mortgages, rates are typically 4.75%. Therefore, many of those mortgage holders with pending renewals will save money after their next renewal (assuming that rates stay at or close to current levels).
- For those with scheduled renewals during the next 6 to 12 months, the average current mortgage rate is similar to the rates that they can expect to negotiate. Therefore, this group will see little change in its payments (however, within the group there will be variations - some will see payments rise and others will see them fall).
- The same applies for those whose mortgages are scheduled for renewal in the following year: if mortgage rates stay at current levels, on average there will be little change in mortgage payments.

<i>Time to Renewal</i>	<i>Average Interest Rate</i>
Less than 6 months	5.3%
6 to 12 months	4.9%
1 to less than 2 years	4.9%
2 to less than 3 years	4.7%
3 to less than 4 years	4.8%
4 to less than 5 years	4.8%
5 to less than 6 years	4.7%
6 to less than 10 years	5.4%
More than 10 years	4.6%
Will not be renewing	4.4%
Don't Know / Refused	4.9%
Total	4.9%

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.

Another view of the data looks at the current actual mortgage rates for rates for those who expect to renew their mortgage early versus those who expect to wait until their scheduled renewal date. For those who expect to renew early, the average current interest rate (4.9%) is virtually the same as for mortgage holders who do not expect to renew early or who don't know (both at 4.8%).

Table 20	
Average Mortgage Interest Rates	
By Expectation of Early Renewal	
<i>Expectation</i>	<i>Average Interest Rate</i>
Expect to renew early	4.9%
Do not expect to renew early	4.8%
Don't know	4.8%
Total	4.9%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.	

It was noted earlier that one out of five mortgage holders responded that they don't know their current mortgage rate. This relatively high rate persists across the different characteristics that were explored above:

- It might be thought that those who are closer to renewal would be more likely to know their rate. That was not the case, as those who will be renewing soon are no more likely to know their interest rate.
- For each of the three mortgage types (fixed, variable rate, and combination) the percentages that don't know their rate are virtually identical.
- Among those who expect to renew their mortgages before the scheduled renewal dates, the percentage who don't know their current interest rate is the same as for people who don't plan to renew early.

Impacts of Changing Interest Rates

The consumers' responses to the survey have been used to estimate future changes in their mortgage costs. The methodology for this analysis is described in the Appendix.

Expected Changes in Mortgage Interest Rates After Renewal

The following table summarizes the anticipated changes in mortgage rates after the mortgage renewals. It indicates that, based on current interest rates and the consumers' expected choices, about 60% of them will have higher mortgage interest rates after their next renewal. Slightly over one-third would have lower rates after the renewal, and a small percentage would see no change in their rates.

	<i>Interest Rate After Renewal is ...</i>			<i>Total</i>
	<i>Increased</i>	<i>Decreased</i>	<i>Unchanged</i>	
% of Mortgage Holders	62%	35%	3%	100%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.				

The next table looks at the results in more detail, showing the extent of increases and decreases by the scheduled renewal dates. Those with the earliest renewals (within 12 months), have the lowest incidence of increased interest rates, 50%, versus the average of 62%. For longer periods until renewal, there are increasing percentages that will see higher rates after renewal.

<i>Time Until Renewal</i>	<i>Interest Rate After Renewal is ...</i>			<i>Total</i>
	<i>Increased</i>	<i>Decreased</i>	<i>Unchanged</i>	
Up to 12 Months	50%	47%	4%	100%
1 to less than 2 years	56%	41%	3%	100%
2 to less than 4 years	60%	36%	4%	100%
4 or more years	70%	28%	2%	100%
Total Mortgage Holders	62%	35%	3%	100%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.				

Another view of the data looks at mortgage holders who expect to renew early compared to those who don't. As can be seen in the next table, mortgage holders who expect to renew early are less likely to see a rise in their monthly interest payments (54%) compared to those who don't expect to renew early (63%) and those who don't know if they will renew early (66%).

<i>Expectation of Early Renewal</i>	<i>Interest Rate After Renewal is ...</i>			<i>Total</i>
	<i>Increased</i>	<i>Decreased</i>	<i>Unchanged</i>	
Expect to Renew Early	54%	44%	2%	100%
Do Not Expect	63%	33%	3%	100%
Don't Know	66%	33%	1%	100%
All Mortgage Holders	62%	35%	3%	100%

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.

Impacts on Monthly Interest Costs

Based on the anticipated changes in mortgage interest rates at renewal, the impact on monthly interest payments has been calculated for each of the mortgage holders. The following table summarizes the results.

After the next mortgage renewal, the monthly interest cost increases by an average of \$22 per month.

Impacts vary, depending on renewal dates. For the earliest renewals (those scheduled to occur within the next six months), monthly interest payments are reduced by an average of \$28. For those with scheduled renewal dates during the next six to twelve months, the average interest cost increases slightly, by \$6 per month. In general, the farther in the future the renewal date is, the greater is the impact on monthly payments. However, for those whose renewal is 6 or more years in the future, the average monthly cost is expected to fall, after renewal.

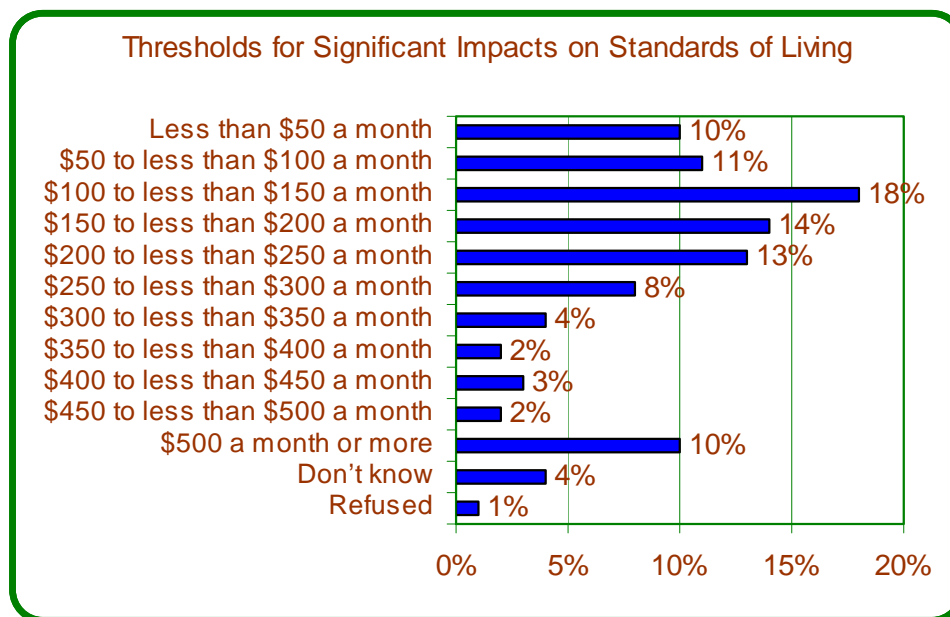
<i>Time to Scheduled Renewal</i>	<i>Average Change</i>
Less than 6 months	-\$28
6 to 12 months	\$6
1 to less than 2 years	\$22
2 to less than 3 years	\$14
3 to less than 4 years	\$38
4 to less than 5 years	\$31
5 to less than 6 years	\$10
6 to less than 10 years	-\$24
More than 10 years	-\$4
Don't know	\$71
Grand Total	\$22

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.

Interest rates for five-year mortgages have increased by about three-quarters of a point since last summer, and rates for shorter terms have increased even more. For a

borrower with an average-sized mortgage (\$116,800), an increase of three-quarters of a point would cost about \$73 per month in additional interest. With the average impact at just \$22 per month, clearly most borrowers will not be affected to that extent. As has been discussed, about 60% of the mortgage holders are expected to face increased payments at their next renewal. On average, their increase is about \$69 dollars per month. For those with reduced payments at their next renewal (over one-third) the average reduction is about \$67.

The survey asked mortgage holders to identify thresholds, the amounts by which their current mortgage payment per month would have to increase before having “a significant impact” on their overall standard of living. The following chart summarizes the responses. It shows that there are negative impacts at all levels. About one-fifth of mortgage holders would be significantly affected if their monthly payment increased by \$100 per month and more than one-half would be significantly affected if their payment increased by \$200.



Estimated Increases in Monthly Payments Versus Thresholds

This section combines the estimates of changes in monthly interest payments with the thresholds reported by the mortgage holders. The results are summarized in the next table. It shows that for 9% of mortgage borrowers, the estimated increases in their monthly payments are above their thresholds for “significant impacts” on their standard of living¹. For the vast majority (91%), the increases in the monthly interest payments are below the thresholds that they identified. The percentages vary slightly depending on the amounts of time that remain before the scheduled renewals.

¹ The thresholds are expressed as ranges rather than exact numbers. For example, in the first range of “less than \$50 per month”, the consumer’s actual threshold could be anywhere from \$0 to \$50. In calculating how many consumers might have increase above their thresholds, the lower boundaries were used.

<i>Time to Scheduled Renewal</i>	<i>Above Threshold</i>	<i>Not Above Threshold</i>	<i>Total</i>
< 12 months	7%	93%	100%
1 to less than 2 years	8%	92%	100%
2 to less than 4 years	10%	90%	100%
4 or more years	8%	92%	100%
Total	9%	91%	100%
Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.			

The Aggregated Impact

The preceding analysis has developed estimates that can be used to estimate the total change in mortgage interest payments in Canada that might occur as current mortgage holders renew their mortgages.

At present there are about 8.2 million to 8.25 million home owners in Canada. Of these about 4.6 million have mortgages on their homes.

The table on the next page provides the calculations:

- It starts by showing, for each of the time periods for future renewals, the percentage of mortgages that will be renewed.
- Multiplying those percentages times the 4.6 million, it estimates how many mortgages will be renewed during each period.
- The average impacts (increases or decreases in monthly mortgage interest costs, per dwelling) have previously been calculated.
- The average impact is multiplied by the number of dwelling units that are involved, to calculate the aggregated impact (in millions of dollars).
- In the second last column, the totals are combined, to show the total impact in millions of dollars per month.
- Finally, the monthly total figures are converted to annual amounts.

This analysis indicates that, in the short-term, the total amount of mortgage interest that is paid each month will fall. This will occur because on average the renewals will be at lower interest rates than prior to renewal. A year in the future, however, the interest rates on renewal will be higher than the pre-renewal rates, so that the total amounts of interest paid will start to rise. By the time all mortgages are renewed (98.7% of current mortgages are expected to be renewed) the total amount of interest paid per year will be \$1.17 billion higher than at present. Spread across 4.54 million home owners who will renew mortgages, this amounts to an average of \$258 per household per year, or \$21.53 per month².

² These calculations make a simplifying assumption that when the home owners renew their mortgages the remaining mortgage balance will be the same as at present. To the extent that they have reduced the amounts outstanding, the rise in the costs will be reduced as well.

<i>Time to Scheduled Renewal</i>	<i>% Renewing</i>	<i># Renewing</i>	<i>Average Impact \$ Per Month Per Dwelling</i>	<i>Aggregate Impact/Month (\$ Millions)</i>	<i>Cumulative Impact/Month (\$ Millions)</i>	<i>Cumulative Impact/Year (\$ Millions)</i>
Less than 6 months	8.5%	391,283	-\$27.84	-\$11	-\$11	-\$131
6 to 12 months	5.9%	270,959	\$6.33	\$2	-\$9	-\$110
1 to less than 2 years	12.8%	588,583	\$22.09	\$13	\$4	\$46
2 to less than 3 years	17.3%	797,077	\$13.68	\$11	\$15	\$177
3 to less than 4 years	20.0%	918,051	\$37.58	\$34	\$49	\$591
4 to less than 5 years	23.0%	1,057,925	\$30.74	\$33	\$82	\$981
5 to less than 6 years	0.9%	39,135	\$9.94	\$0	\$82	\$986
6 to less than 10 years	3.3%	152,239	-\$24.00	-\$4	\$78	\$942
More than 10 years	1.1%	48,306	-\$4.47	-\$0	\$78	\$939
Don't know when will renew	6.0%	274,678	\$70.80	\$19	\$98	\$1,173
Will not be renewing	1.3%	61,763	\$0.00	0		
Total	100.0%	4,600,000		\$98	\$98	\$1,173

Source: Pollara survey for CIMBL, February 2006; analysis by Will Dunning Inc.

Potential Impacts of Additional Increases in Mortgage Rates

As always, there is uncertainty about future changes in interest rates. This section assesses the impacts of future increases in mortgages rates, testing first the impact of a one-half percentage point increase and then a one percentage point rise.

In the event that mortgage rates are one-half point higher than at present:

- The average increase in interest costs on renewal would be \$72 per month, versus the \$22 increase that is estimated at current rates.
- Once all renewals have occurred, the total increase in interest costs would amount to \$3.9 billion per year, versus the currently-estimated increase of \$1.17 billion.
- For 18% of mortgage holders the increase in monthly costs would take them across their threshold for “a significant impact” on their overall standard of living (it was estimated earlier that at current rates 9% would cross their threshold at the next renewal).

- The impact would be minor for those who renew during the first year, amounting to a total of \$194 million. Within this group, 19% would cross their threshold for a “significant impact”.

In the second scenario, in which mortgages interest rates are a full one percentage point above current levels:

- The average increase in interest costs on renewal would be \$123 per month, versus the \$22 increase that is estimated at current rates.
- Once all renewals have occurred, the total increase in interest costs would amount to \$6.7 billion per year, versus the currently-estimated increase of \$1.17 billion.
- For 29% of mortgage holders the increase in monthly costs would take them across their threshold for “a significant impact” on their overall standard of living (it was estimated earlier that at current rates 9% would cross their threshold at the next renewal).
- For those renewing in the first year, the total impact would be \$498 million per year. Within this group, 19% would cross their threshold for a “significant impact”.

Appendix – Methodology for Analysis of Impacts of Changing Interest Rates

The methodology is summarized as follows.

The mortgage rate that each consumer will have after their next renewal was estimated, based on their reported expectations about:

- The term they will select for the next mortgage.
- The type of mortgage they will select.
- And, assuming that the rate is at the current level of 4.75% for all variable rate mortgages.
- For fixed rate and combination mortgages the rates were assumed as follows
 - 4.95% for mortgage terms up to 2 years.
 - 5.00% for terms of 2 years to less than 4 years.
 - 5.05% for terms of 4 years to less than 5 years.
 - 5.10% for terms of 5 years to less than 6 years.
 - 5.30% for terms of 6 years to less than 10 years.
 - 5.50% for terms of 10 years and over.

For each of the consumers, the future rate was compared to the current actual rate, to calculate the amount of change in the interest rate at renewal. These changes in the rates were applied to their reported remaining mortgage balances to calculate the changes in the amounts of interest that each consumer would pay each month. (This approach ignores any changes that they might make in the amount of principal they repay each month.)

Then, these estimates were combined with the data on when the renewals would occur, in order to calculate the aggregate impacts for the future periods.

Those estimated increases in monthly payments were compared to the amounts that consumers say their payments could increase before there was a significant impact on their overall standard of living.

As can be seen in this discussion, responses from several questions were combined to complete these calculations. A “don’t know” response on any of the questions would make it impossible to calculate the impacts for a consumer, which reduced the size of the effective sample. Compared to the total sample of 1,015, the sample used for these calculations was reduced by 57%, to 438.