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JLR PUBLICATION

2020 Mortgage Market Report

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HIGHLIGHTS:

- Nearly 280,000 mortgages were published in 2020, up 14% from 2019.
- After several years of increasing market share, small players lost ground to the big banks and Desjardins Group for a second straight year.
- Desjardins continued to dominate the market in 2020, granting 40.6% of the mortgages for property purchases.
- After several years of decline, CIBC's market share rebounded in 2020. However, in spite of a 1.1 percentage point increase, the bank's market share remained lower than in 2016 and 2017.

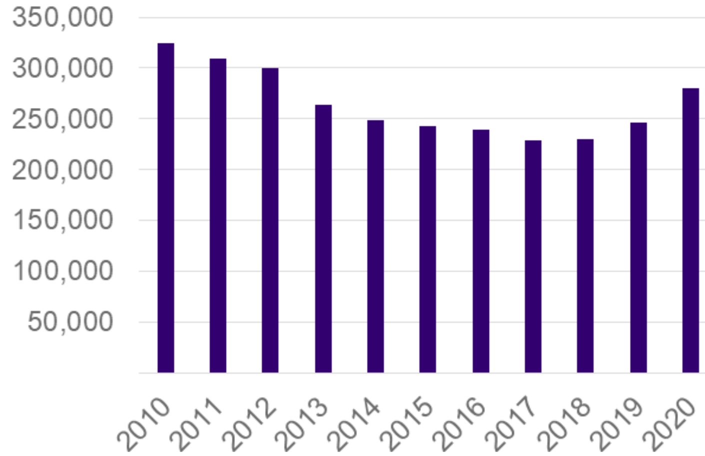
The real estate market was surprisingly strong in 2020, which translated into a robust mortgage market. In this context, the majority of financial institutions saw a rise in their mortgage customer base. Of course, some did better than others.

An analysis of the mortgages published in the Quebec Land Register and compiled by JLR, an Equifax Company, revealed several market trends. In this analysis, we accounted for all mortgages, including those issued for residential properties and for other types of purchases. However, since about 90% of mortgages issued are for residential properties, this sector has a powerful influence on market developments.

1. CHANGES IN THE NOTARIZED MORTGAGE MARKET

Less frequently published renewals in the Land Registry combined with a modest sales growth has led to a reduction in the number of published mortgages over the past several years. Over the past two years, however, the highly active real estate market and rise in renewals and refinancing have led to a surge in the number of publications. In 2020, the number of new mortgages recorded jumped by 15% over last year, to reach nearly 280,000 deeds.

Graphic 1 : Change in the Number of Mortgages Published in the Land Register

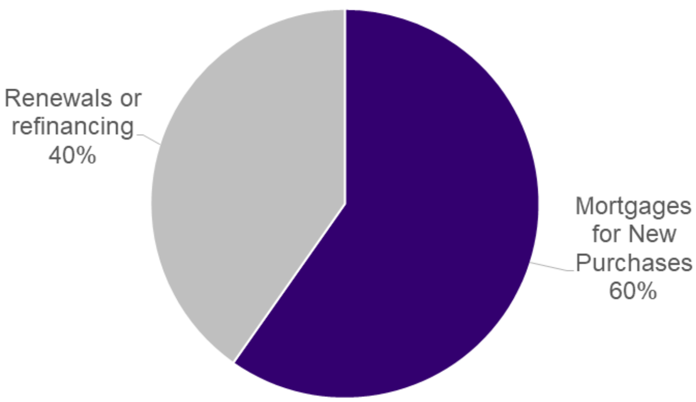


Mortgages published in the Quebec Land Register can be divided into two categories: those issued for property purchases and those granted for renewals or refinancing.

The growing popularity of collateral mortgages has led to a reduction in the number of refinancing loans requiring a deed to be published over the last decade, since they allow loans to be renewed without the need for a notary. However, despite the existence of collateral mortgages, a new deed is always published if the owner borrows more than the amount guaranteed under the loan, changes financial institution or adds a second mortgage.

In 2020, a new trend was observed and the publication of mortgage renewals and refinancing loans increased by 11% to reach a total of nearly 113,000 deeds. This rebound is perhaps attributable to some homeowners moving up their mortgage renewals, looking to take advantage of interest rate cuts and a rise in refinancing loans for renovations. The number of second-tier loans does not appear to have influenced the growth in the volume of deeds.

Graphic 2: Distribution of Mortgages by Type

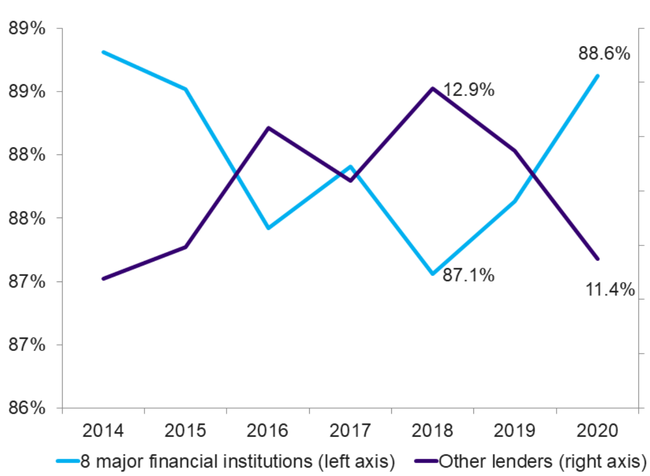


The remainder of this report will focus exclusively on mortgages issued to acquire new properties, since the inclusion of collateral mortgages limits the number of renewals and refinancing deeds published in the Quebec Land Register, which skews the interpretation.

2. CHANGE IN MORTGAGE MARKET SHARE

A few players dominated the Quebec mortgage market. The seven major Canadian banks[1] and Desjardins Group issued 88.6% of the mortgages granted for a new purchase in 2020.

Graphic 3: Change in Mortgage Market Share



Over the past year, the "other lenders" than the eight major institutions saw their market share decline by 1 percentage point. This fall contrasts with the increases observed before 2016. Several phenomenons are behind this reversal in the trend.

Since the early 2000s, regulatory changes and technological advances have led to greater competition in the mortgage market. In fact, the arrival of mortgage financing companies such as First National, Paradigm Quest and MCAP increased the market share of small lenders. However, these new companies have now been around for a while and their market share has been stagnating for about 2 years.

Legislative tightening in recent years may in part explain the setback in the growth of these types of creditors. For instance, according to Coletti, Gosselin and MacDonald (2016)[2], mortgage financing companies were more exposed than traditional lenders' to clients who could not meet the standards introduced in the fall of 2016.

In the end, mortgage finance companies granted about 6% of new loans in Quebec in 2020, a similar proportion than that of the previous year. In short, the stagnating market share of these creditors may, in part, explain the stagnation in small lenders' market share, but cannot account for the decline. The withdrawal of some players from the market seems to be a more likely explanation.

Indeed, the closure of the residential mortgage department at Industrial Alliance in late 2019 most certainly reduced the market share of "other lenders". In 2018, the company had a 0.8% market share, while in 2020 it issued only a few dozen mortgages for non-residential property purchases. As a result, the new loans that Industrial Alliance is no longer issuing are being redistributed among the various players, including the eight major institutions, resulting in a loss of market share for the "other lenders" category.

1. The Bank of Montreal, Toronto-Dominium Bank, National Bank, Laurentian Bank, Scotiabank, CIBC and Royal Bank. For the purpose of historical comparison, we kept Laurentian Bank in the top eight institutions, despite its current market share falling below 1%..
2. Coletti, D. Gosselin, M-A. and MacDonald, C. (2016). "The Rise of Mortgage Finance Companies in Canada: Benefits and Vulnerabilities," Financial System Review, Bank of Canada, pp. 45-61.

Following its withdrawal from the market, Industrial Alliance sold its mortgage portfolio to National Bank, but this transfer was not included in the statistics for this report as these are not mortgages issued for new purchases. Over 4,000 properties were subject to a deed of mortgage assignment between the two institutions. There may have been more transfers, but no mortgage assignments were yet published. This not only increased the number of National Bank mortgages on file (not included in the market shares herein), but may also bolster the institution's mortgages for home purchases in the coming years. Indeed, some of these new clients may move in the future and choose to seek financing from National Bank to avoid prepayment penalties.

La Capitale also left the residential mortgage market following its association with the SSQ. In 2018, the institution held 0.3% of the mortgage market share. This player's departure has had an impact, albeit more limited than that of Industrial Alliance, on reducing the market share of "other lenders". La Capitale sold its mortgage portfolio of 6,376 loans to Desjardins in early 2020[3]. For the time being, however, La Capitale remains the registered holder in the Land Register in most cases and the various loans will gradually get transferred.

Finally, a portion of the market shares decline for "other lenders" may be attributable to low interest rates and the strength of the real estate market. In the current environment, online lenders can have more trouble distinguishing themselves with more attractive interest rate offers than the large banks. In addition, the quick turnaround on the resale market may be limiting time for buyers to shop around for mortgages.

3. MORTGAGE MARKET SHARES (MORTGAGES ISSUED FOR PROPERTY PURCHASES ONLY)

3.1 PROVINCE OF QUEBEC

The Desjardins Group continued to lead the mortgage market with 40.6% of all mortgages issued for new purchases in 2020, a similar figure to that in the previous year. However, this result conceals a more complex picture. The rise in transactions outside of the Montréal Census Metropolitan Area (CMA) should have benefitted the Desjardins Cooperative, whose numbers in the regions are better than in Montréal. In fact, if Desjardins had held equivalent market shares in each region than that of 2019, it would have secured nearly 2,000 additional mortgages in 2020. This would have increased its market share in all of Quebec by about 1 percentage point. In short, the Group has lost ground in several regions, but the significant rebound in property purchases outside of Montréal, where it performs very well, allowed the institution to maintain its overall provincial market share.

The increased attractiveness of properties outside of Montréal this year skewed the interpretation of several market share statistics, as the popularity of lenders varies greatly from region to region.

In 2020, lenders that are more popular in Montréal than in the regions, like the Bank of Montreal, Scotiabank, Royal Bank, Toronto-Dominion Bank and CIBC, were disadvantaged in the calculation of provincial market shares. In spite of this, the market share for the Bank of Montreal and CIBC increased by 0.4 and 1.1 percentage points respectively thanks to an improvement in all Quebec CMAs and outside of them. In the case of CIBC, this represented a significant jump in its market share following two difficult years. However, the proportion of mortgages issued by CIBC remained lower than in 2016 and 2017. In 2018 and 2019, the bank hit the brakes as the quality of its loans and exposure on the Canadian market were raising concerns. However, in September 2019, the president of CIBC admitted that the bank had gone too far and would adjust course to win back customers[4]. Its 2020 results were therefore consistent with this plan.

3. *Desjardins fait l'acquisition du portefeuille de prêts hypothécaires de La Capitale,* January 21, 2020, https://blogues.desjardins.com/communiques-de-presse/2020/01/transfert-hypotheque.php

4. Doug Alexander, CIBC May Have Gone Too Far in Mortgage Retreat, CEO Dodig Says, Bloomberg, September 4, 2019, https://www.bloomberg.com/news/articles/2019-09-04/cibc-may-have-gone-too-far-in-mortgage-retreat-ceo-dodig-says (consulted on February 22, 20201) 0).

For three years now, Laurentian Bank has remained a marginal lender with a market share under 1%. According to a La Presse article from March 3, 2021, Laurentian Bank is looking to turn things around and grow its residential mortgages file. Among other things, it intends to improve its approval process[5]. The institution may therefore capture some market share from its competitors in 2021 or 2022. However, Laurentian Bank has a long climb ahead before it can regain the market share it held in the early 2010s.

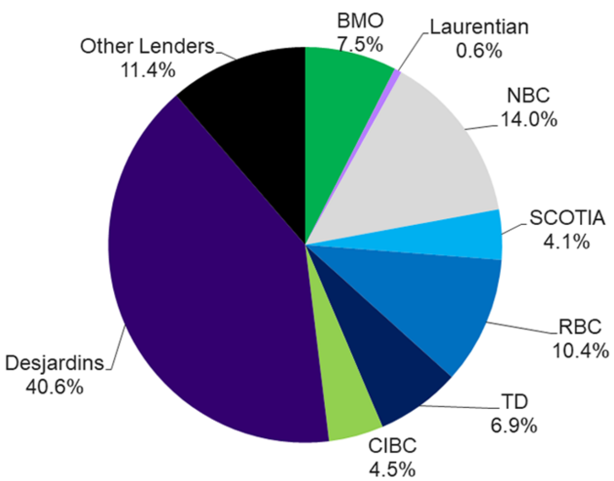
As for National Bank, its market shares varied less from region to region and were therefore less influenced by the change in geographical distribution of its transactions. The institution continued to be the second-largest lender in 2020, improving its market share by 0.5 percentage points. This was the third consecutive year that its market share increased.

With strong growth in property sales and prices, the total value of loans granted has increased for most institutions, although some lost a portion of their market share.

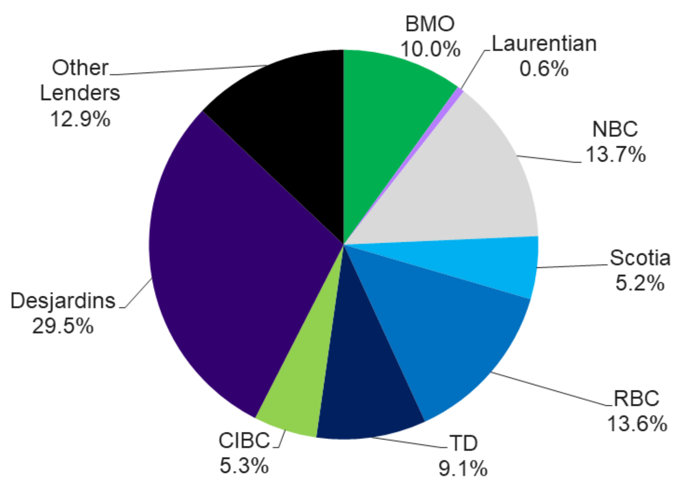
3.2 REGIONAL RESULTS

Just fewer than 78,000 mortgages issued for property purchases were published in 2020 for properties located in the Montréal Census Metropolitan Area (CMA). The number has increased but, as mentioned earlier, the proportion relative to the rest of Quebec has decreased. However, this is not expected to continue in 2021 as supply is now limited across Quebec, not just in Montréal. Desjardins had the largest number of new mortgages published in the Montréal CMA with a 29.5% market share; however, this is the market in which the Cooperative performs least well. In comparison, it issued over 50% of mortgages in the Saguenay–Lac-Saint-Jean and Trois-Rivières CMAs and outside of Quebec's 6 CMAs.

Graphic 4: Mortgage Market Shares - Province of Quebec



Graphic 5: Mortgage Market Shares - Montreal CMA



Market shares are calculated based on numbers of mortgages. The results would be somewhat different if the amount of mortgages was considered instead. For example, Desjardins, which is far more dominant in the regions where property values are lower on average, would have a smaller market share.

With its proximity to Ontario, the Gatineau market differed from the other sectors in terms of its mortgage offering breakdown. In that CMA, Royal Bank, TD Bank and Scotiabank held positions #2–4 on the list of leading lenders. National Bank, the second-largest lender in the province, fell to fifth place among mortgage creditors in the Gatineau region.

5. Julien Arsenault, *La Banque Laurentienne veut redresser la barre,* La Presse, March 3, 2021, https://www.lapresse.ca/affaires/entreprises/2021-03-03/prets-hypothecaires/laurentian-bank-wants-straighten-la-barre.php (consulted on March 23, 2021)

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4. TRENDS
4.1 BAD DEBTS

Due to the pandemic and its devastating effects on employment in 2020, many expected a significant rise in bad debts (for mortgages). Instead, the various support measures, but especially the possibility for many households to defer their mortgage payments for six months, reduced the number of bad debts. Despite growing somewhat since payment deferrals were discontinued, the number of prior notices and repossessions has remained very low.

2021 may bring a slow rise in bad debts, but recent price increases are reducing the number of short-term recoveries. In fact, within this highly robust housing market, households are able to resell their properties fairly easily and thereby avoid handing over their keys to creditors in the case of financial problems. In this context, potential financial losses for lenders are likely to be limited in 2021. The number of bad debts this year will be higher than in 2020, when an all-time low was recorded, but they are expected to remain well below the ten-year average. In the longer term, rapid price increases, if they deviate from fundamentals, will put the market at risk of correction and an ensuing growth in bad debts.

4.2 REGULATION

In mid-2020, the CMHC tightened its mortgage insurance underwriting rules by no longer accepting non-traditional sources of down payment that increase debt, and by increasing its requirements for amortization ratios and minimum credit score. However, lenders were able to turn to other insurers for their riskier customers, which reduced the impact of these changes.

For 2021, in early April the OSFI announced the possibility of increasing the interest rate used to qualify uninsured loans. If the institution goes ahead with this plan, uninsured loans will have to pass the stress test using the higher interest rate between the one of the loan+2% and 5.25%. The latter currently sits at 4.79%. This could, in part, protect financial institutions and households against potential rate hikes.

In its latest budget, the federal government proposed imposing a 1% tax on foreign-owned real estate considered vacant or underutilized beginning in 2022. The impact of this measure on the housing market is expected to be minor and will not curb the housing boom, especially outside the major centres.

Should increases continue and speculation set in, further announcements may be forthcoming this year since, for now, the above-mentioned measures are unlikely to significantly reduce price increases.

4.3 INTEREST RATES AND MARKET FORECAST

As a result of the pandemic, variable and fixed interest rates have fallen sharply. According to Ratehub, the best offer for a fixed 5-year interest rate declined from 2.44% in late February 2020 to 1.38% in December 2020. Lower rates, combined with a high savings rate and the increased importance of housing, have boosted sales, along with the number of new mortgages. In this context, prices have risen rapidly; allowing financial institutions to increase the amounts loaned to acquire property.

Interest rates rebounded in March 2021 as the economic outlook improved. According to Ratehub, the best offer in the country for a 5-year fixed-rate mortgage was 1.68% at the end of March. This rate remains historically low, but an upswing this year will limit price increases in 2021 rather than driving them as it did in 2020.

In its April 21, 2021 statement, the Bank of Canada (BoC) announced that it will maintain its policy rate at the current level, but adjust its quantitative easing program. This will entail adjusting the weekly target in Canadian government bond purchases from $4 billion to $3 billion. As such, the BoC will begin gradually adjusting its support for the economy by reducing its bond purchases. Against this backdrop, medium and long-term interest rates are expected to remain low, but still rise slightly from their current level over the course of the year.

The institution will soon make a decision on its regulatory framework for the next five years. Currently, the BoC's priority is to keep inflation low and stabilize it between 1% and 3%. A change in its target, by incorporating an employment component for instance, could change its policies slightly and thereby affect interest rates. That said, notwithstanding possible changes to the Bank of Canada's targets, mortgage interest rates are expected to rise slowly in 2021as the economic situation improves and the BoC reduces its support.

In short, the interest rate component is not expected to translate into higher prices and more sales in 2021; in fact, the effect will be the opposite. However, housing will remain a priority for households during the pandemic and bolster demand, while limited supply is expected to reduce opportunities to purchase. Under these conditions, sales growth will be limited, but prices could continue to grow as long as supply remains low.

Ultimately, growth in the number of mortgages will be limited by a dwindling supply of residential properties. In the first half of the year, the number of new mortgages will remain high compared to last year. However, in the second half of the year, the number of new mortgages will likely decrease compared to 2020 given the exceptional catch-up effect observed last year. The total value of loans, on the other hand, could increase significantly as the gains in property prices have been significant and several factors continue to drive increases throughout 2021.

CONCLUSION

The mortgage market was disrupted by the pandemic in 2020. In the end, however, it was a prolific year in terms of lenders' portfolio growth, due to the strength of the real estate market.

In 2021, the risk for lenders and new buyers could increase as property values continue to rise quickly, especially if interest rates rise faster than expected. As a result, the likelihood of a correction could increase and change the strategic positioning of lenders.

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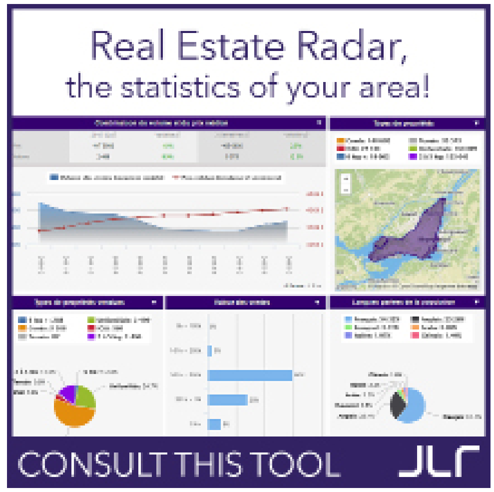

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