Are millions of home owners now taking over 30 years to pay off their mortgage? Not exactly

ROBERT MCLISTER
SPECIAL TO THE GLOBE AND MAIL
PUBLISHED MAY 5, 2023

The narrative that some Canadians need to take more than 30 years to pay off their mortgages is alarming, but needs analyzing.

MARCUS OLENIUK/THE GLOBE AND MAIL

Nearly a third of homeowners will need more than 30 years to pay off their mortgages, according to a recent news report that blamed higher interest rates for these extended amortizations.

This week's lowest fixed and variable mortgage rates in Canada

Many people reading that would think Canadians will suddenly require years more time to pay off their mortgages than banks typically allow. It's the sort of narrative that gets people all riled up for no good reason.

What (I think) the writer really means

The fact is, 30 years is the longest amount of time you can amortize – spread out the payments on – a prime mortgage. And prime mortgages – which are available to creditworthy borrowers – account for over four out of five residential mortgages in this country.

Roughly one-third of borrowers have a floating-rate mortgage and about 30 per cent of bank borrowers have seen their amortizations extend beyond 30 years. That's because variable-rate payments are fixed, and those borrowers temporarily pay less principal and more interest as rates rise. That, in turn, can extend their theoretical amortization periods well beyond 30 or 40 years in some cases.

(Floating-rate mortgages with payments that move with prime rate are technically called "adjustable-rate mortgages.")

Sign up for the Carrick on Money Newsletter

Protect your money with Rob Carrick's proven personal finance advice on saving and investing.

REGISTER TO SIGN UP

But the keywords here are "temporary" and "theoretical."

CALCULATOR: See how rising interest rates will affect the cost of your mortgage

The majority of these folks are forced by their lender to get back on track with their initial scheduled amortization once they renew. That means they have to increase their payments in most cases to make up for the principal they didn't pay down when rates were soaring. This catch-up on principal payments ensures that an

original 25-year amortized mortgage actually is paid down in 25 years, rather than over a longer period.

The other point worth noting is that interest rates don't go up forever. They're cyclical. Once inflation heads back toward the Bank of Canada's 2-per-cent target, prime rate will drift back down. At that point, everyone with a fixed-payment variable mortgage will start paying more principal and less interest, thus reducing their theoretical amortizations.

Finally, there's the matter of prepayments. Past research from Mortgage Professionals Canada indicates that the average Canadian pays off a mortgage in less than 20 years. That's largely because roughly one-third of borrowers make mortgage extra payments in any given year.

Once you look past the attention-grabbing headlines and take a closer look at the details, it's simply not accurate to say that one-third of mortgagors will take more than 30 years to pay down their original mortgage.

The real problem with amortizations

The biggest beef with amortizations in this country is that regular folks are forced to resort to longer and longer amortizations to afford a home. They pay interest to lenders for too much of their working lives, money that could be saved or better spent elsewhere.

Average amortizations have been steadily increasing since the pandemic started. The Bank of Canada reports that 46.5 per cent of new mortgages have an amortization over 25 years, up a whopping 14 percentage points in just a few years thanks to rising rates and home prices. Albeit, it's still less than the 46.8 per cent peak in 2016.

This is a problem – not with amortizations themselves, or with banks, but with ungodly housing costs in this country. That's a problem primarily caused by the imbalance between immigration and housing construction, which is beyond the scope of this column.

CMHC forecasts 32-per-cent drop in new home construction due to inflation, labour shortages

In his book, *The Next Age of Uncertainty*, former Bank of Canada governor Stephen Poloz speaks to this problem and, among other solutions, supports 50-year amortizations where appropriate. The idea is that long amortizations give many more Canadians a chance to get on the housing ladder, build retirement savings through principal payments and enjoy tax-free capital appreciation on their primary residence.

"What's the difference between rent and interest?" Mr. Poloz told MortgageLogic.news in a recent Zoom interview. "Instead of paying rent for 50 years and then retiring, you just pay interest to a bank for 50 years."

Of course, home values could ultimately rise if long amortizations increased demand and let buyers pay higher purchase prices. But ideally, the government would offset this effect by matching immigration to housing supply – thus slowing appreciation to more reasonable and sustainable longer-term rates.

Insured borrowers still get the best deals

The gap between default-insured and uninsured mortgage rates just keeps getting wider, at least for the terms people want most.

Take two-year fixed-rate and variable-rate mortgages, for example. They're a hot commodity because more people want shorter commitments – given they think rates are coming down by next year.

The spread between insured and uninsured mortgages grew five basis points this week on two-year fixed and variable-rate mortgages. (A basis point is one-hundredth of a percentage point.)

On an insured two-year, for example, you can now get rates as low as 4.99 per cent from a national lender. If that same mortgage is uninsured, you'll pay 5.44 per cent

and up, given the extra theoretical risk to the lender.

This divergence reflects higher funding costs and more bank control of uninsured mortgage pricing, a trend that keeps worsening as potential recession causes a greater implied risk to lenders.

It's unlikely this problem will correct itself any time soon, at least until there's a more liquid source of uninsured funding in this country.

That aside, it was another fairly quiet week for mortgage rates, as the bond market awaits more signs of falling inflation.

Lowest nationally available mortgage rates

TERM	UNINSURED	PROVIDER	INSURED	PROVIDER
1-year fixed	5.74	Ratehub	5.54	QuestMortgage
2-year fixed	5.44	HSBC	4.99	Nesto
3-year fixed	5.14	First National	4.64	Nesto
4-year fixed	5.04	First National	4.44	QuestMortgage
5-year fixed	4.79	HSBC	4.29	Ratehub
10-year fixed	5.74	HSBC	5.04	Nesto
Variable	5.90	HSBC	5.45	Nesto
5-year hybrid	5.35	HSBC	6.06	Scotia eHOME
HELOC	6.70	HSBC	N/A	N/A

* Home equity line of credit.

SOURCE: ROBERT MCLISTER; DATA AS OF MAY 4.

Rates are as of May 4, 2023, from providers that advertise rates online and lend in at least nine provinces. Insured rates apply to those buying with less than a 20 per cent down payment, or those switching a pre-existing insured mortgage to a new lender. Uninsured rates apply to refinances and purchases over $1-million and may include applicable lender rate premiums. For providers whose rates vary by province, their highest rate is shown.

Robert McLister is an interest rate analyst, mortgage strategist and editor of MortgageLogic.news. You can follow him on Twitter at @RobMcLister.

Do some quick calculations, learn, or read more on the topic

Calculators

MORTGAGE CALCULATOR

More on the topic

Ontario woman, 39, moved 3,400 kilometres to northern B.C. for a government job and bought two houses: ‘It was a huge move’

This week’s lowest fixed and variable mortgage rates in Canada