

# The Canadian Housing Market: Will it continue to perform?

Monday May 25, 2015

Eric Lascelles  
Chief Economist  
RBC Global Asset Management Inc.



RBC Global  
Asset Management

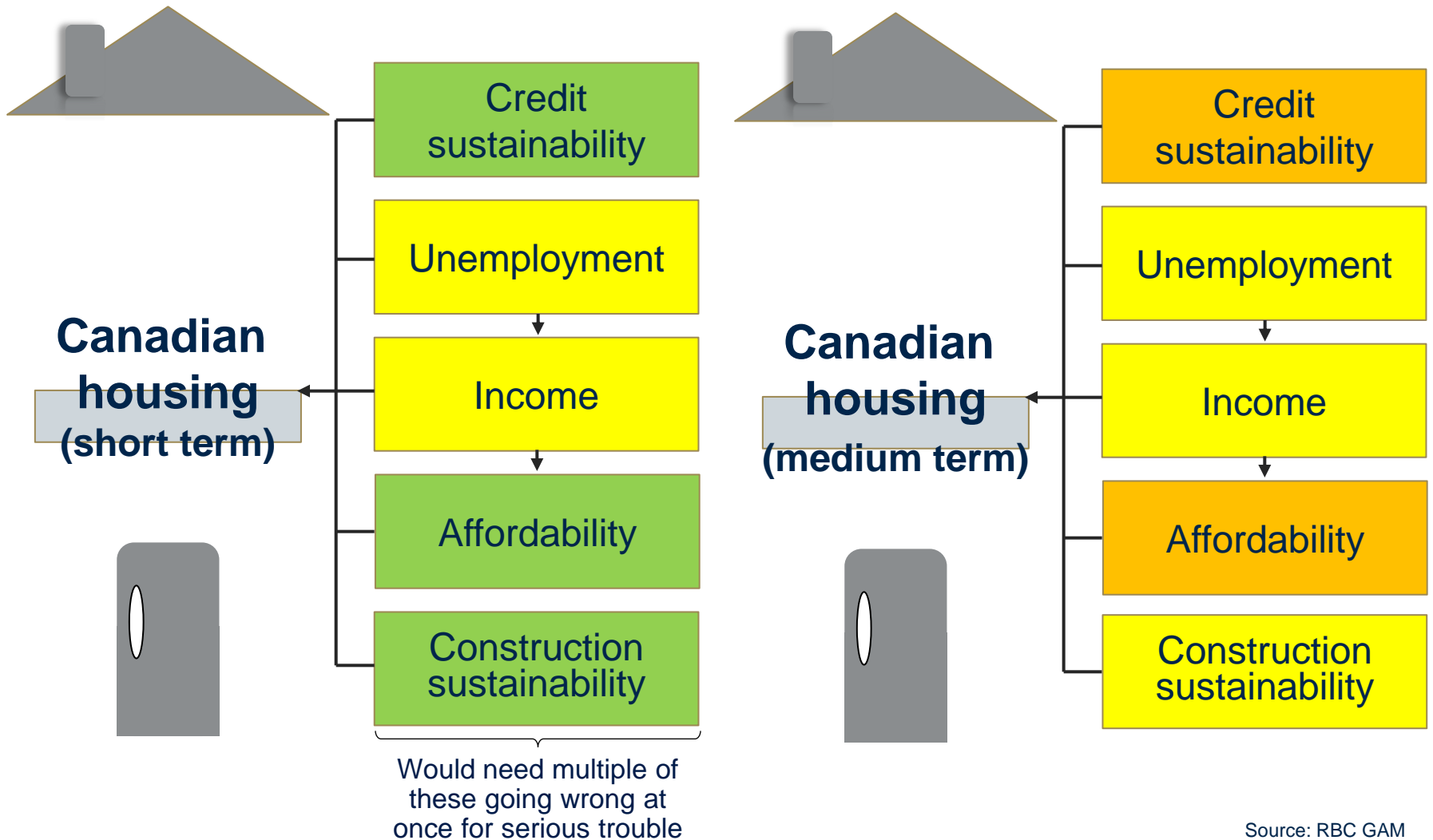


# Canadian Housing Outlook

May 2015

Presented by:  
Eric Lascelles, Chief Economist

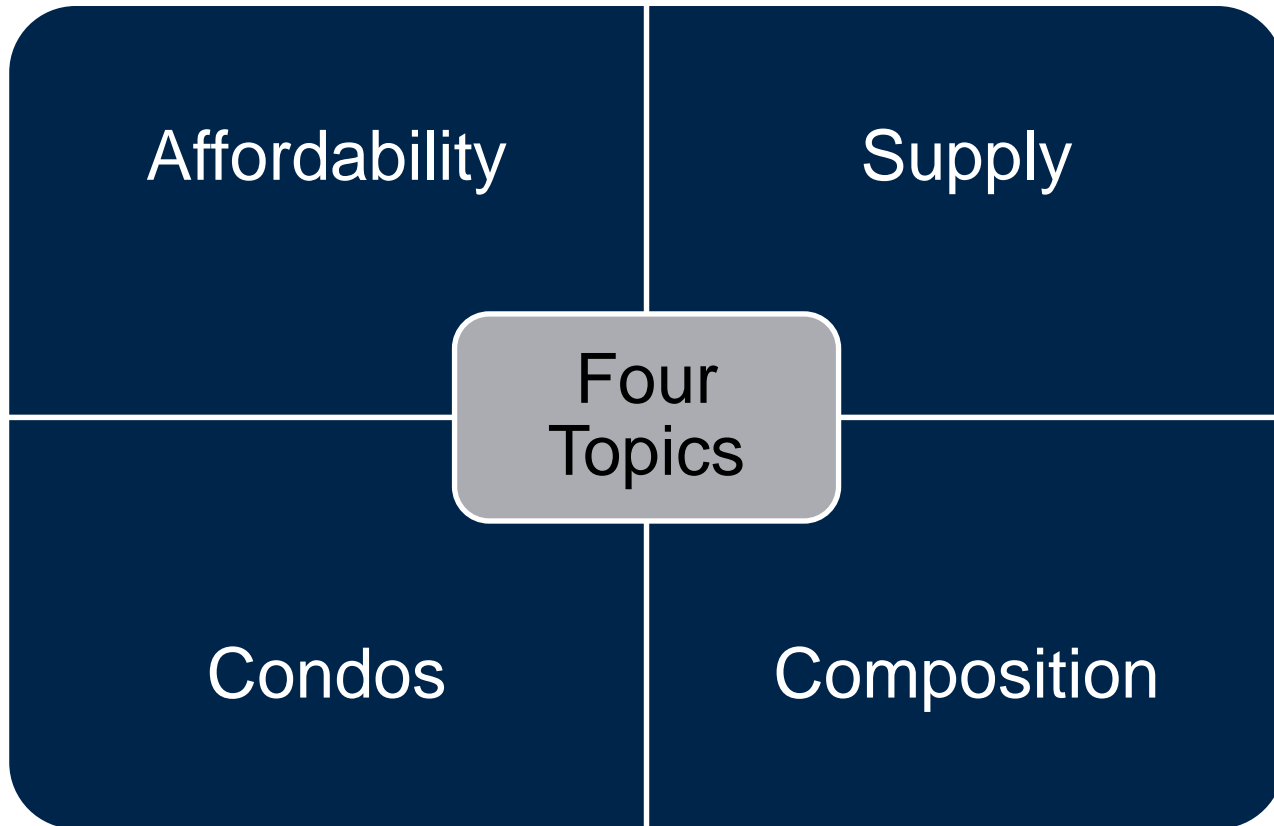
# Canadian Housing Overview



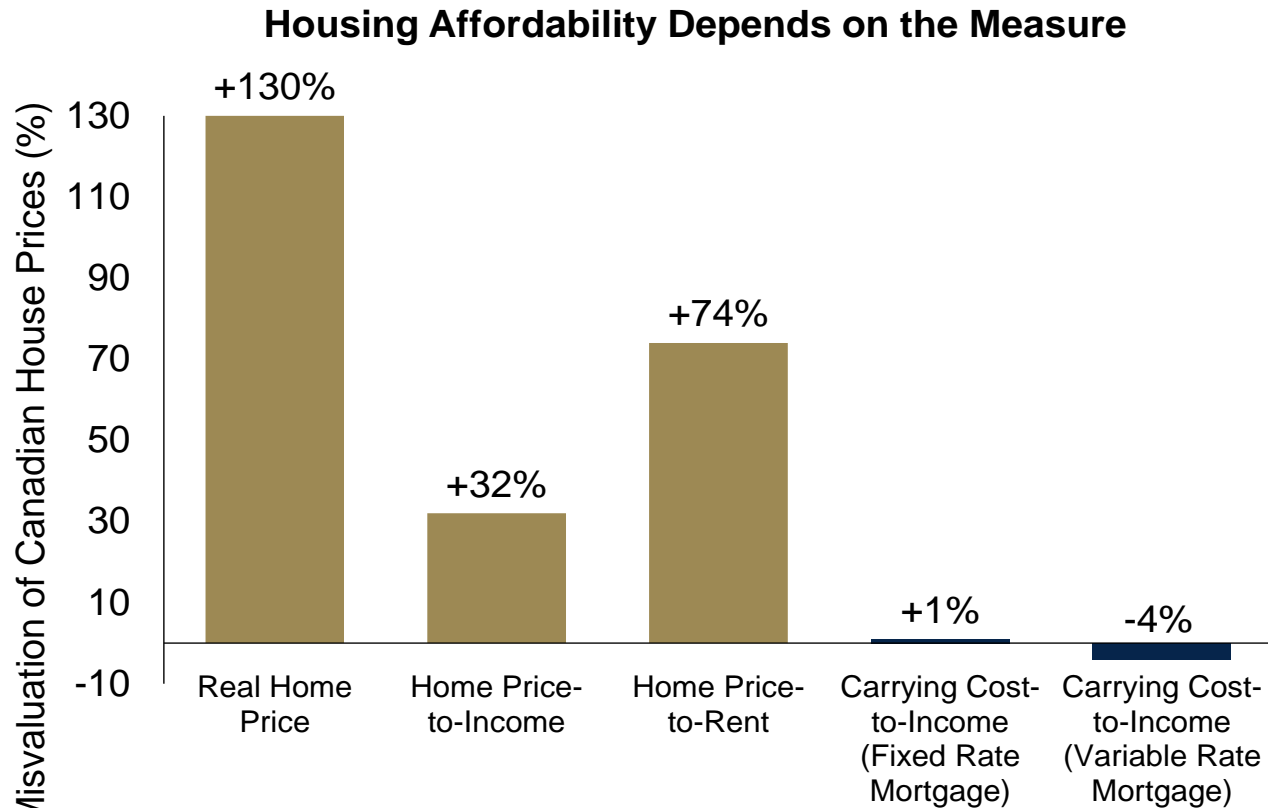
Source: RBC GAM

# Four Quick Canadian Housing Themes

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# Housing Affordability Measures Disagree Vehemently

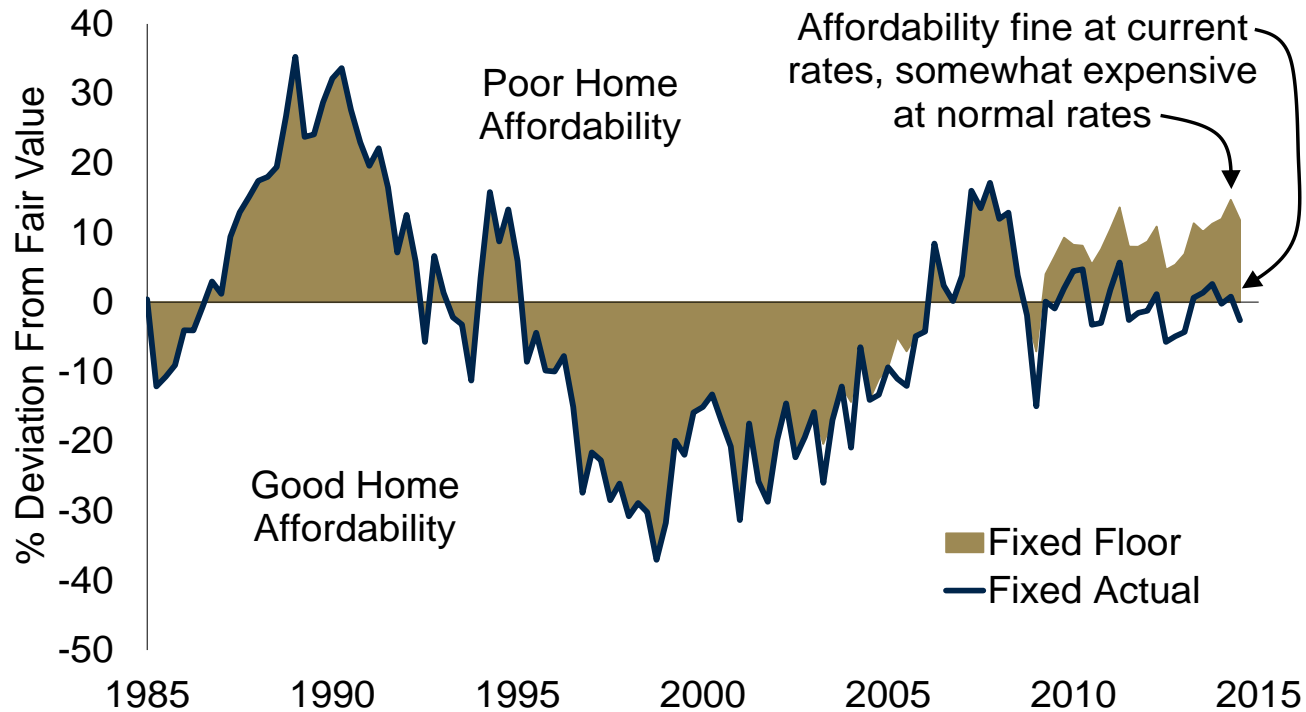


Note: Real home price is % change from 1980 level; price-to-income and price-to-rent versus average since 1975; carrying cost versus average since 1980.

Source: The Economist, Haver Analytics, RBC GAM

# By Best Measure, Affordability OK Now, Gets Worse Later

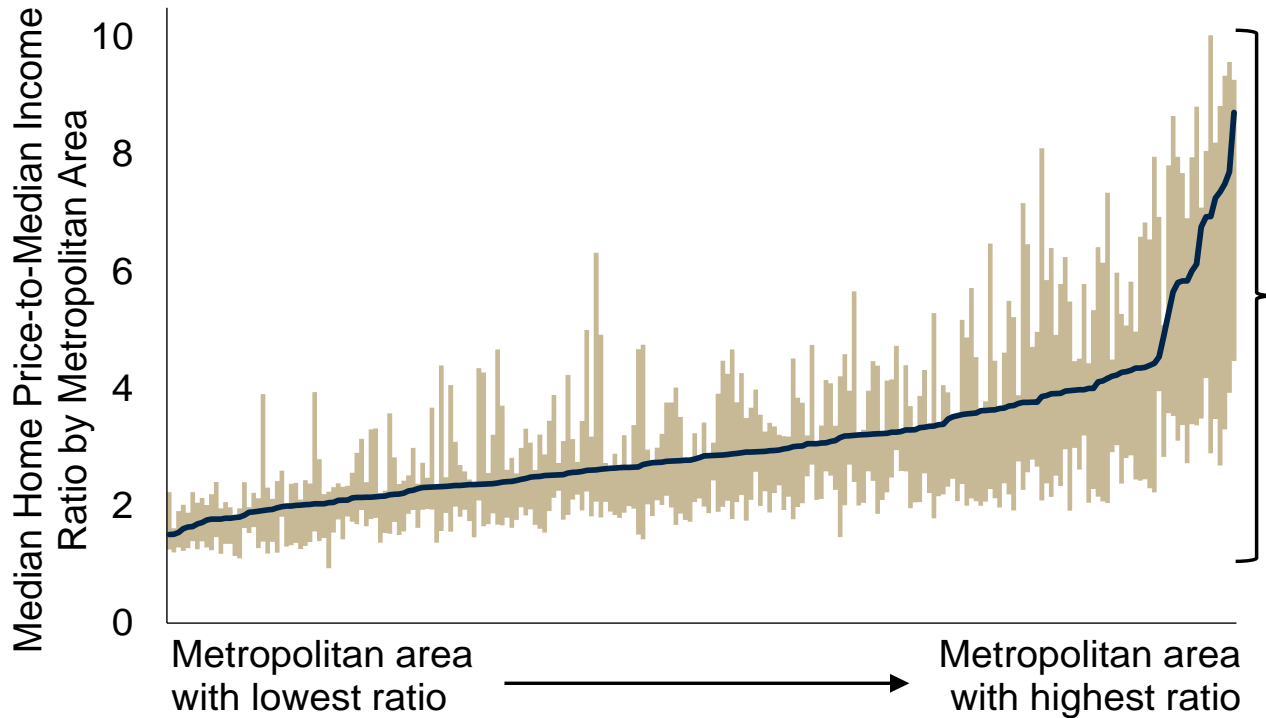
## Canadian Affordability Will Fall When Rates Normalize



Note: Fixed Floor imposes a minimum "normal" mortgage rate on the affordability calculations, and so reveals how affordability would look at normal mortgage rates.  
Source: CREA, Statistics Canada, Haver Analytics, RBC GAM

# “Normal” Affordability Differs Radically By Market

## "Normal" Housing Affordability Varies Enormously

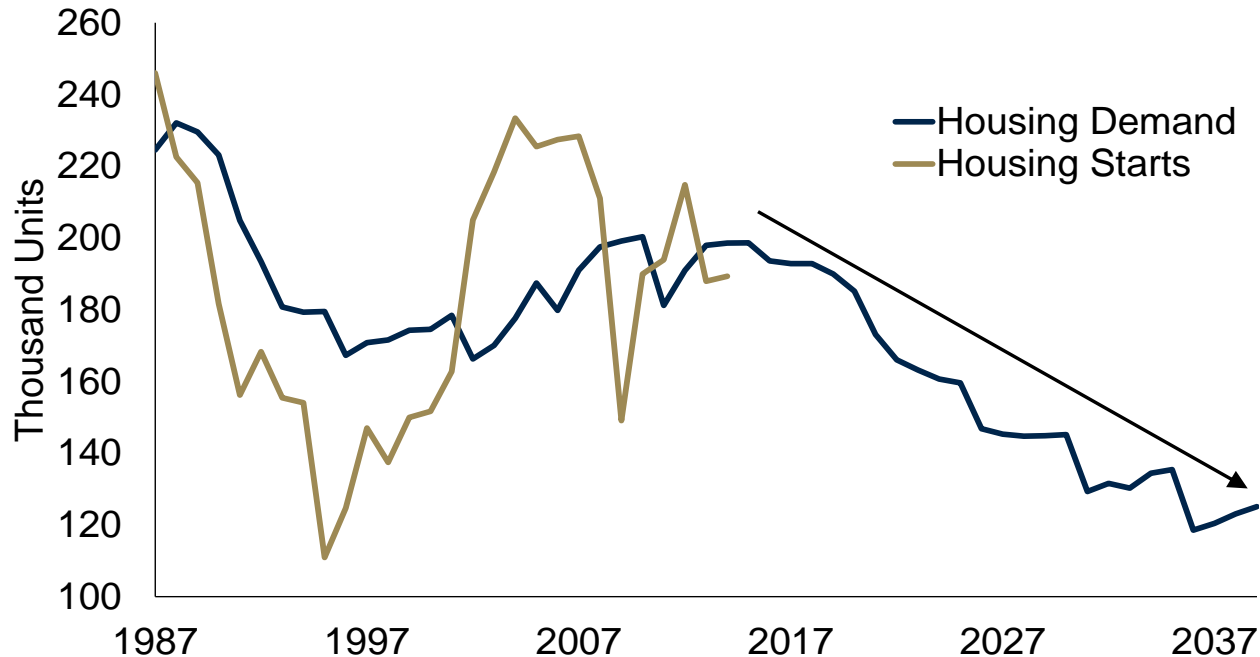


Note: Based on latest data available. Shaded area represents the range of historical median home price-to-median income ratios of 228 metropolitan areas sampled.

Source: NAHB, Haver Analytics, RBC GAM

# Construction In Line With Millennial Boom

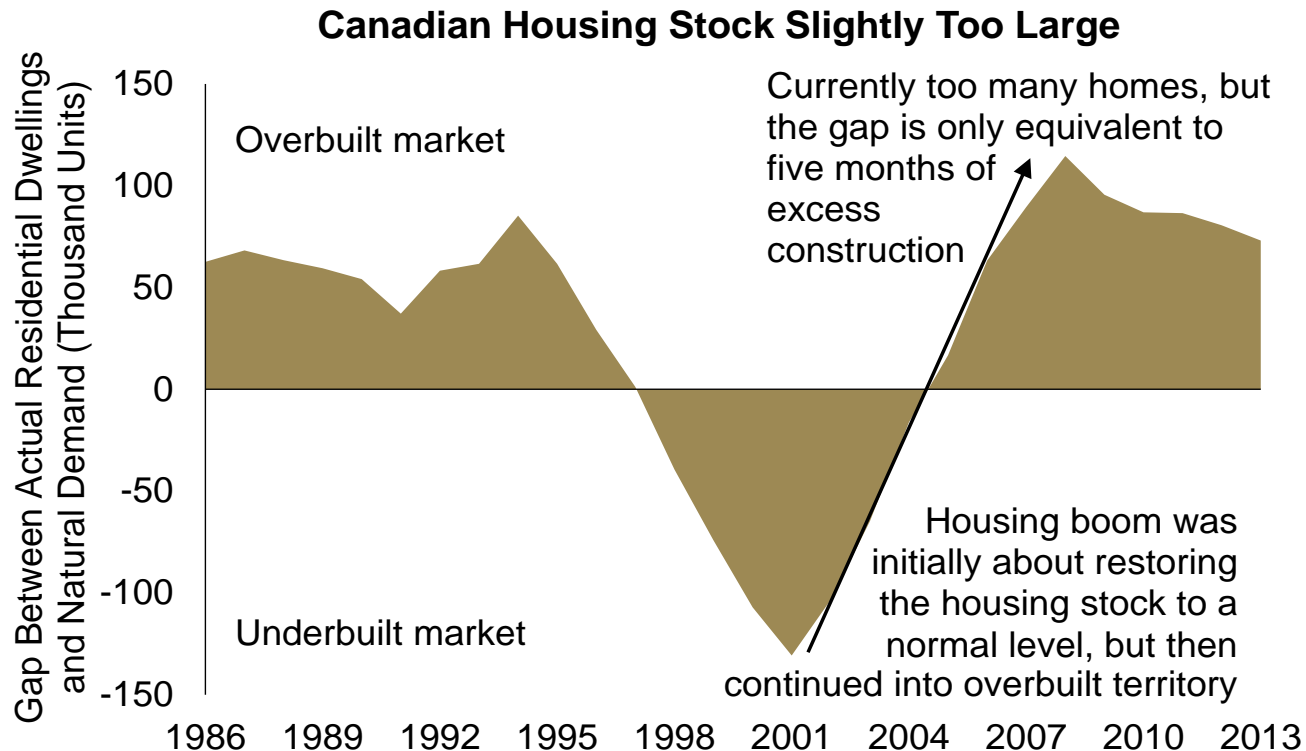
## Canadian Construction to Fall with Lower Demand



Note: Housing starts-equivalent measure of demand calculated using UN population forecasts, historically normal age-based population-to-household ratios, a 1.03 multiplier from housing completions to housing starts, a 1.12 multiplier from housing completions to increases in the housing stock (due presumably to the conversion of some properties into multi-unit apartments after completion), a 1.055 multiplier to reflect the existence of seasonal properties and a 0.015% annual teardown rate on the existing housing stock.  
Source: CMHC, Statistics Canada, UN, Haver Analytics, RBC GAM



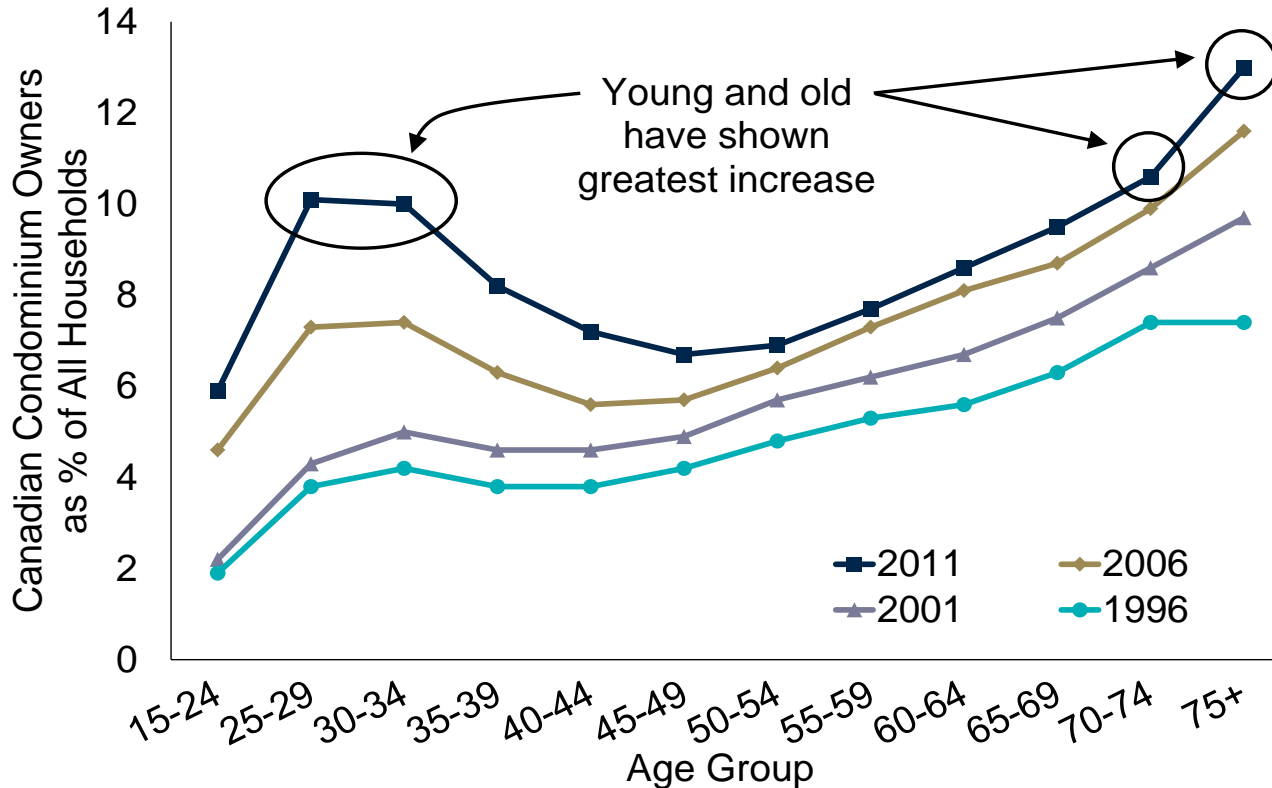
# Housing Stock Is Slightly Overbuilt, But Not Severely



Note: Natural demand calculated using UN population forecasts and historically normal age-based population-to-household ratios. Actual housing stock calculated using reported figures through 2000, then estimated via the rate at which new homes are completed (with a 1.12 multiplier from housing completions to increases in the housing stock due presumably to the conversion of some properties into multi-unit apartments), a 1.055 multiplier between the number of households and number of dwellings to reflect seasonal properties and a 0.015% annual teardown rate on the existing housing stock. Source: CMHC, Statistics Canada, UN, Haver Analytics, RBC GAM

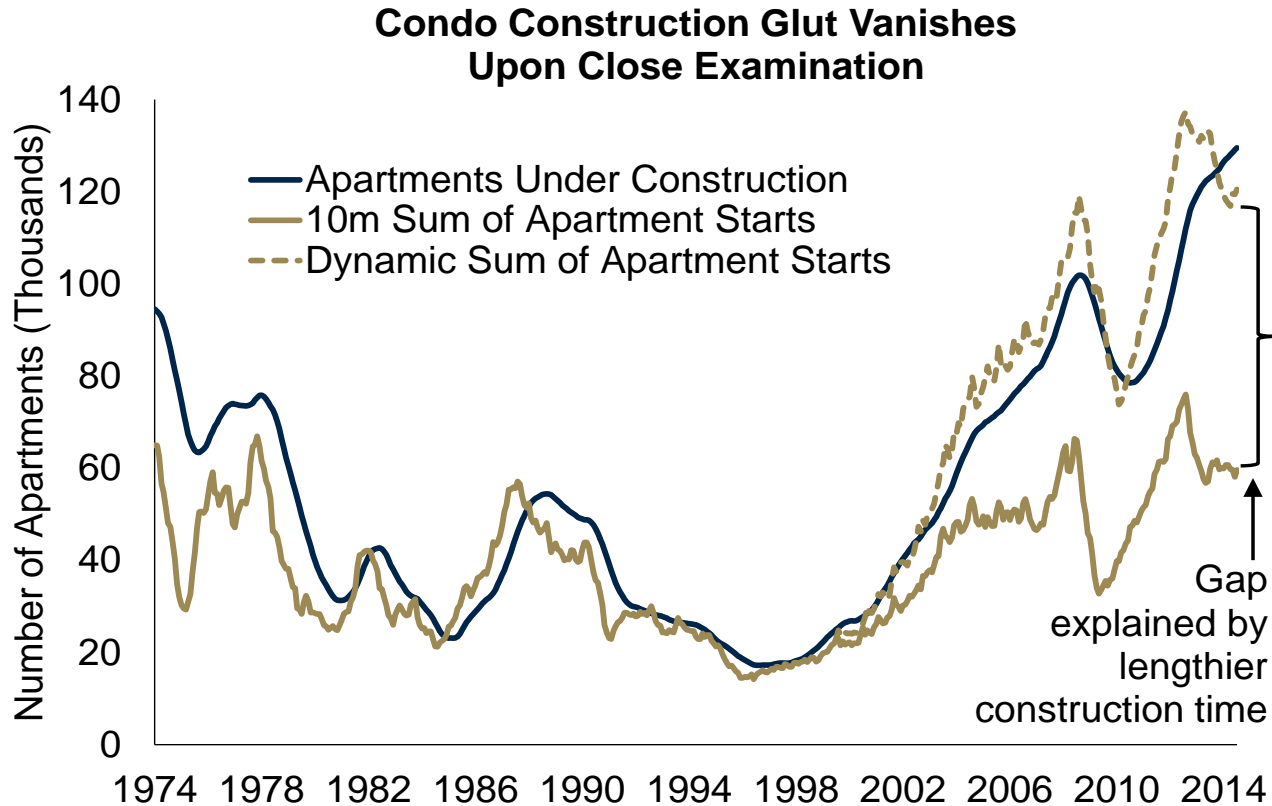
# Support for Condo Demand: Demographics, Preferences, Relative Affordability

Condo Appetite Rising Over Time



Source: Canadian Housing Observer 2013, CMHC, RBC GAM

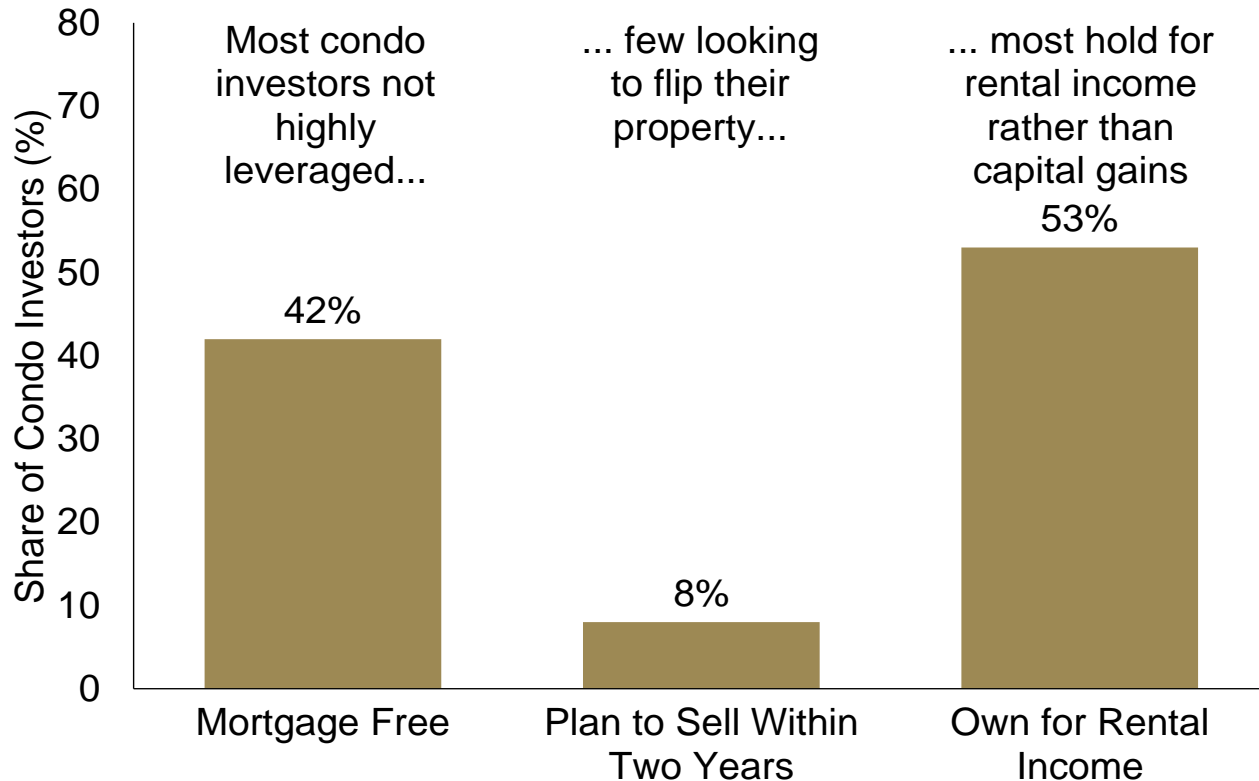
# Condo Construction Now Takes More Time = More Cranes



Note: Dynamic Sum of Apartment Starts scales the average construction time steadily upward from 10 months to 20 months between 2000 and 2009, then holds constant at 20 months thereafter. Source: Haver Analytics, RBC GAM

# Investors Have Healthy Attitudes; Fill Hole in Rental Market

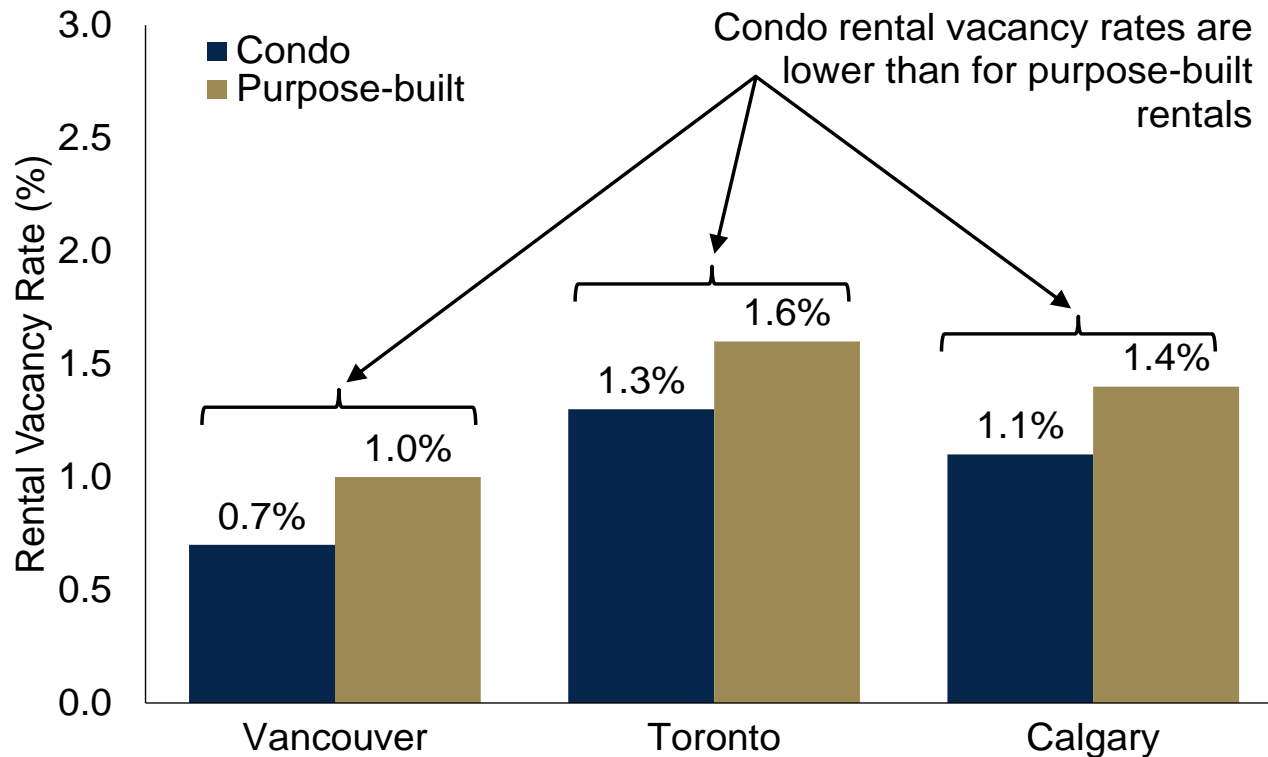
## Condo Investors Are Level-headed Bunch



Note: Based on survey conducted in 2013. Source: CMHC, RBC GAM

# Condo Rental Market Looks Healthy

## Rental Vacancy Rates Are Low



Note: As of October 2014. Source: CMHC, RBC GAM

# Canadian Credit Compositional Concerns

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- **Aggregate household debt burden not especially pressing**
- **Major Canadian lenders/insurers seem fine**
  - Can absorb Alberta weakness
  - OK (though not happy) if confronted by a more serious housing downturn
  - CMHC stress tests pass with flying colours
- **But what about compositional issues beneath the surface?**
- **Most players behave rationally**
  - Poor take less debt than rich
  - Old take less debt than young
- **Still, there are potential problems**
  - **Alberta** indebtedness is highest of provinces
  - Some **smaller markets** have too much condo inventory
  - **Seniors** experiencing faster debt growth
  - A non-trivial cohort of **stretched Canadians** will suffer materially when rates rise
  - **Small banks**: one-third of uninsured mortgage growth is sub-prime
  - **Non banks**: generate almost one-quarter of insured mortgage growth, 3-5x usual



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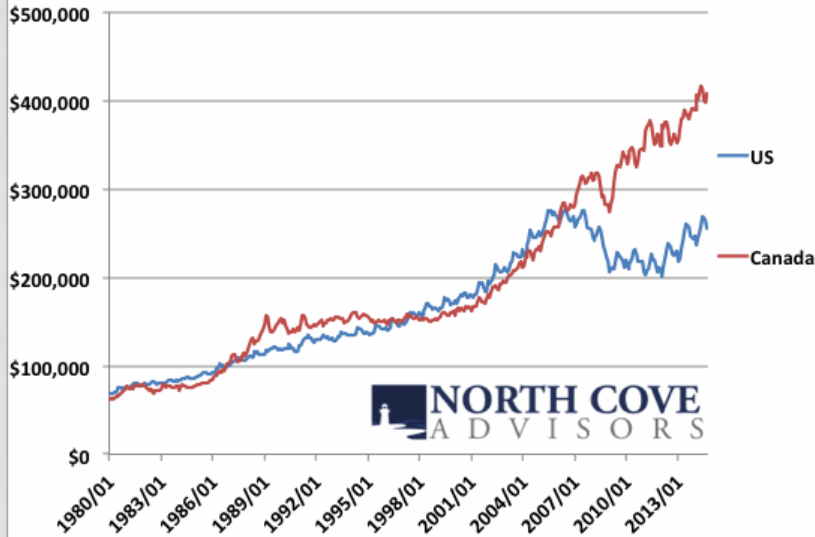
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Ben Rabidoux  
President  
North Cove Advisors



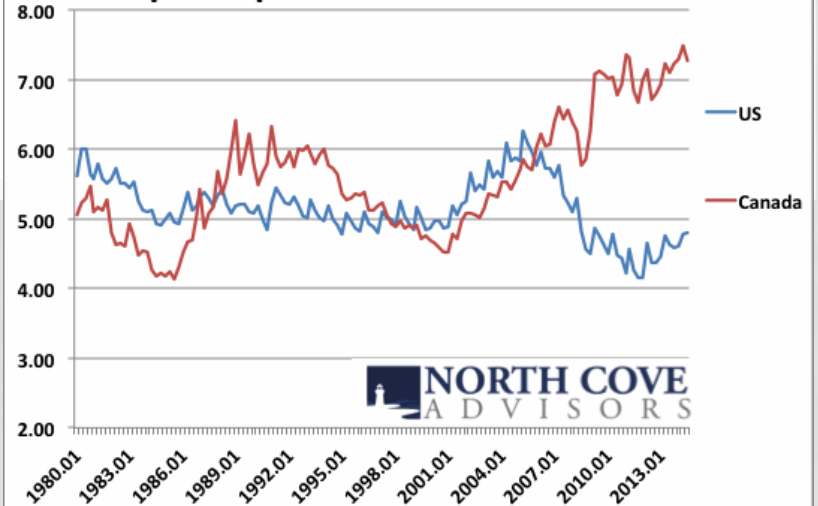
### Average house prices in local currency



Sources: NRA, CREA Last reading: Sept 2014



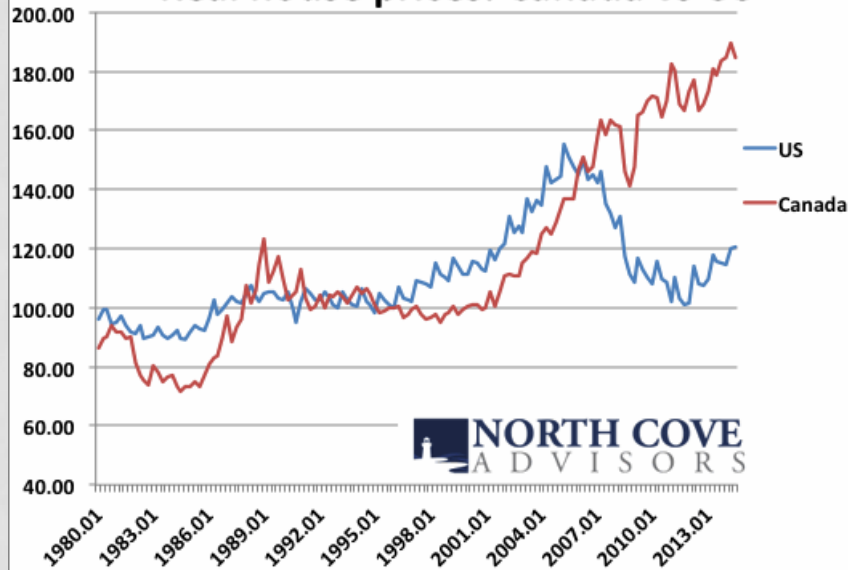
### Average house prices as a multiple of per capita GDP: Canada vs US



Sources: BEA, NRA, CREA, Stats Canada Last reading: Q3 2014



### Real house prices: Canada vs US



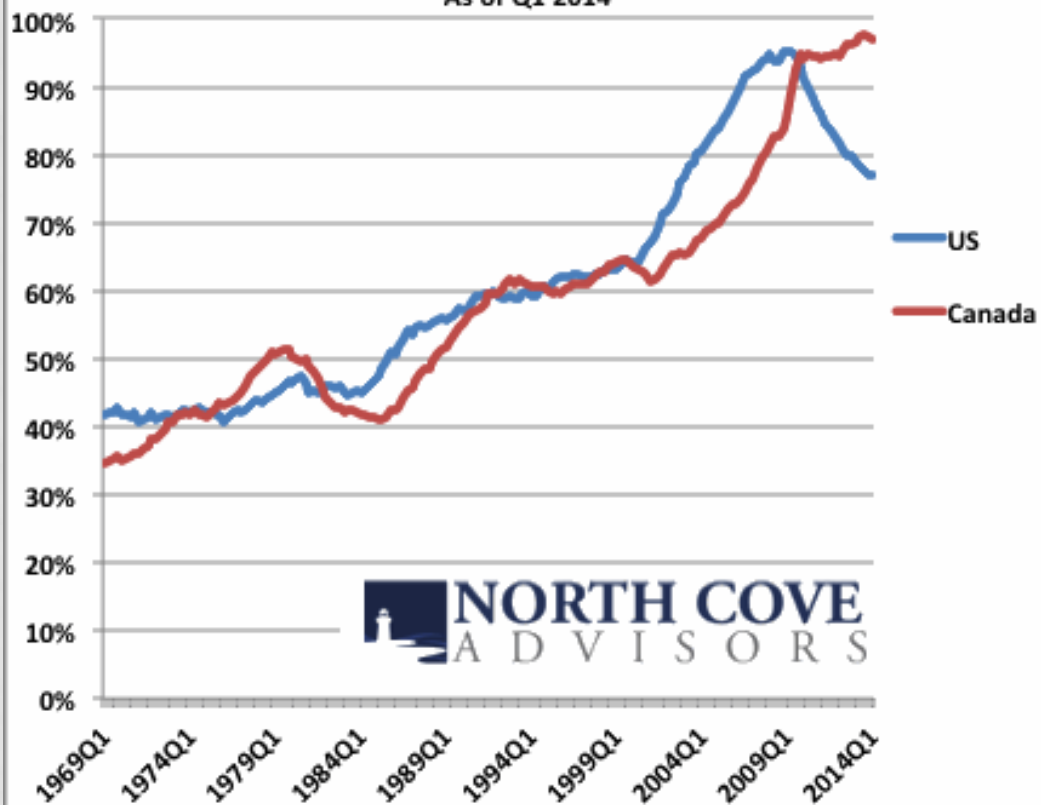
Q1 1996 = 100

Sources: BEA, NRA, CREA, Stats Canada Last reading: Q3 2014



## Household and non profit sector debt to GDP

As of Q1 2014



 **NORTH COVE**  
ADVISORS

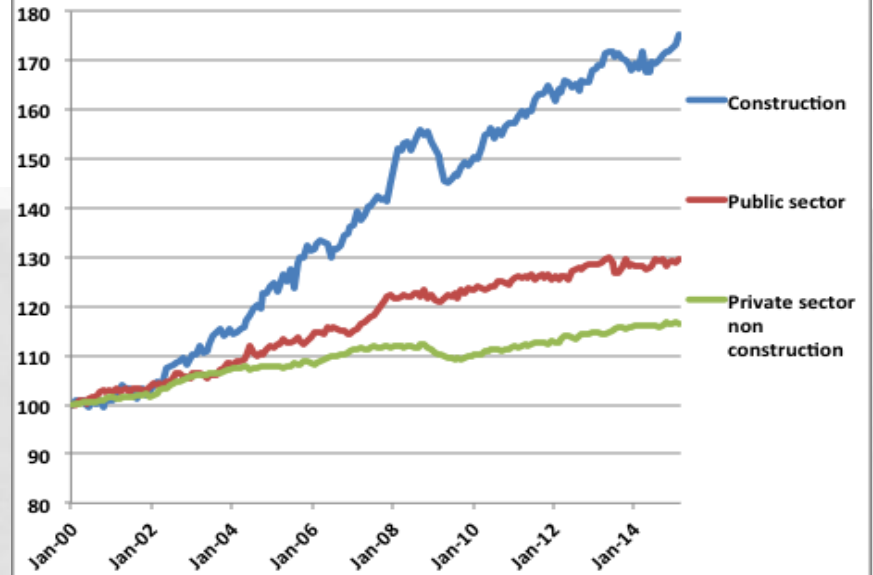
### Percent of labour force employed in construction



Last reading as of Feb 2015  
Sources: Stats Canada, BLS

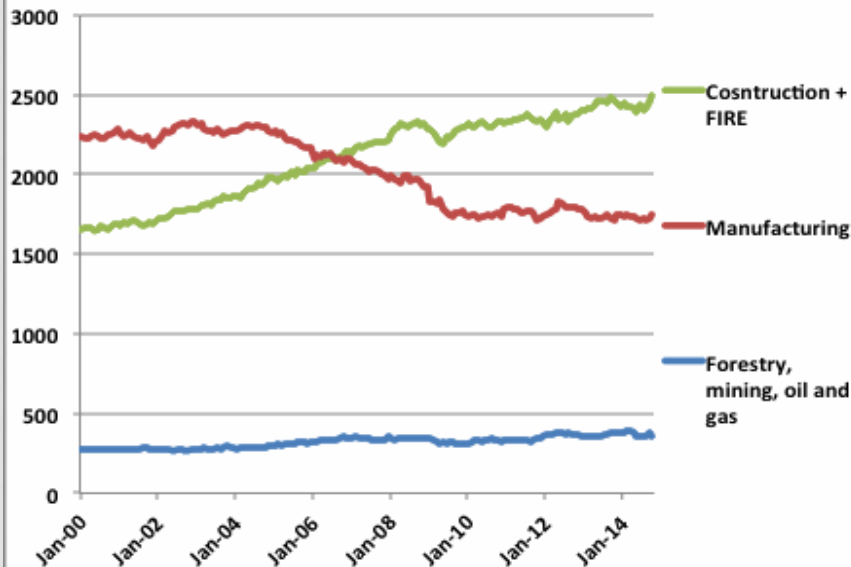
### Employment growth in Canada

January 2000=100



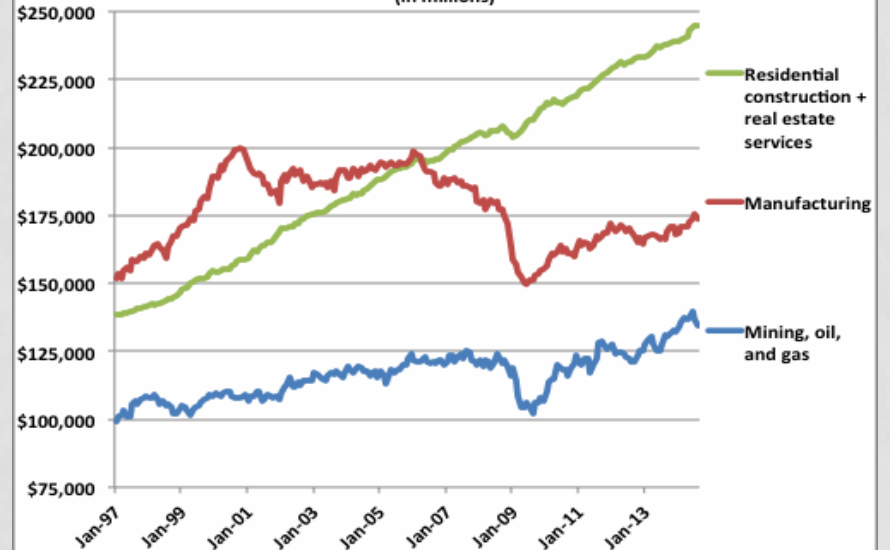
### Employment by industry

(in 000s)



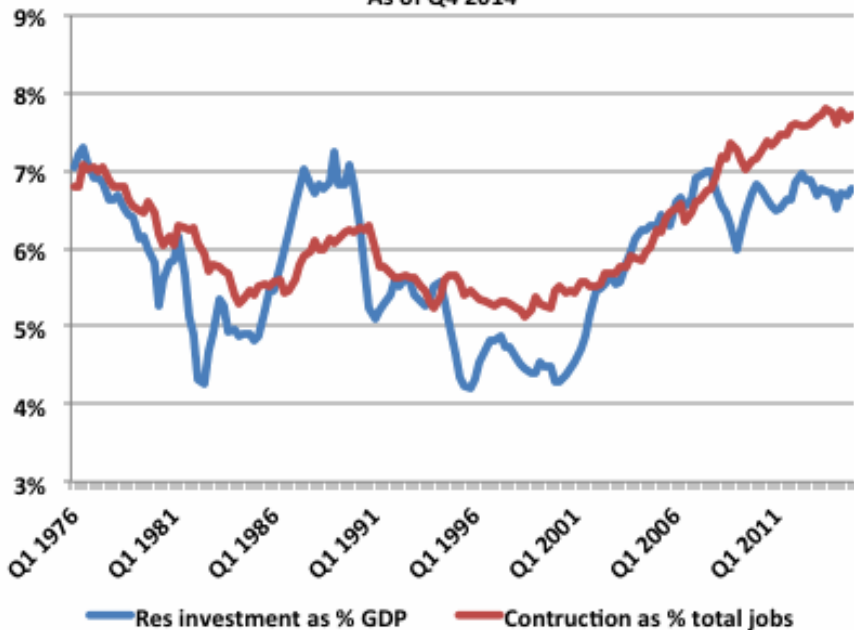
### Canadian GDP by industry

(in millions)

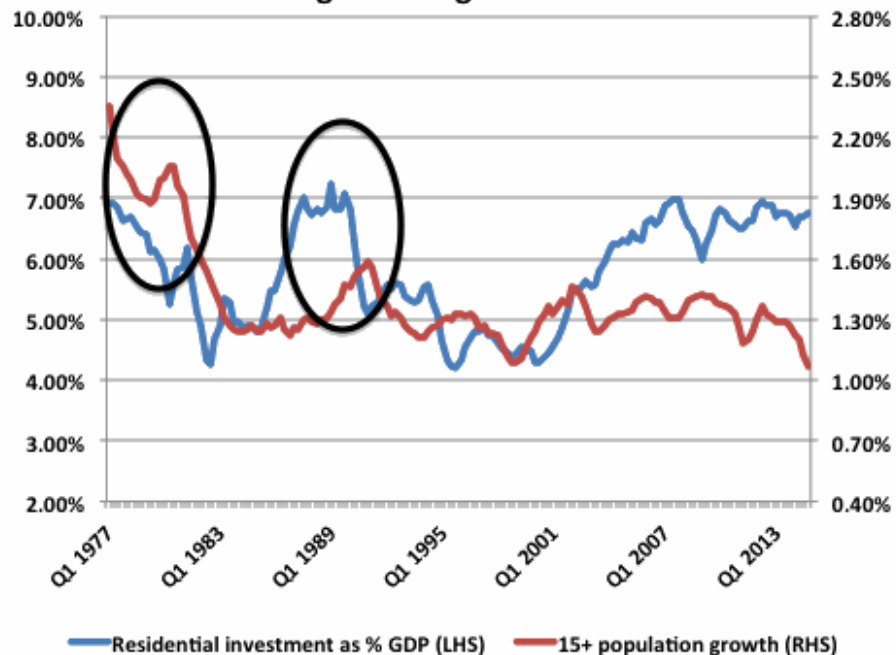


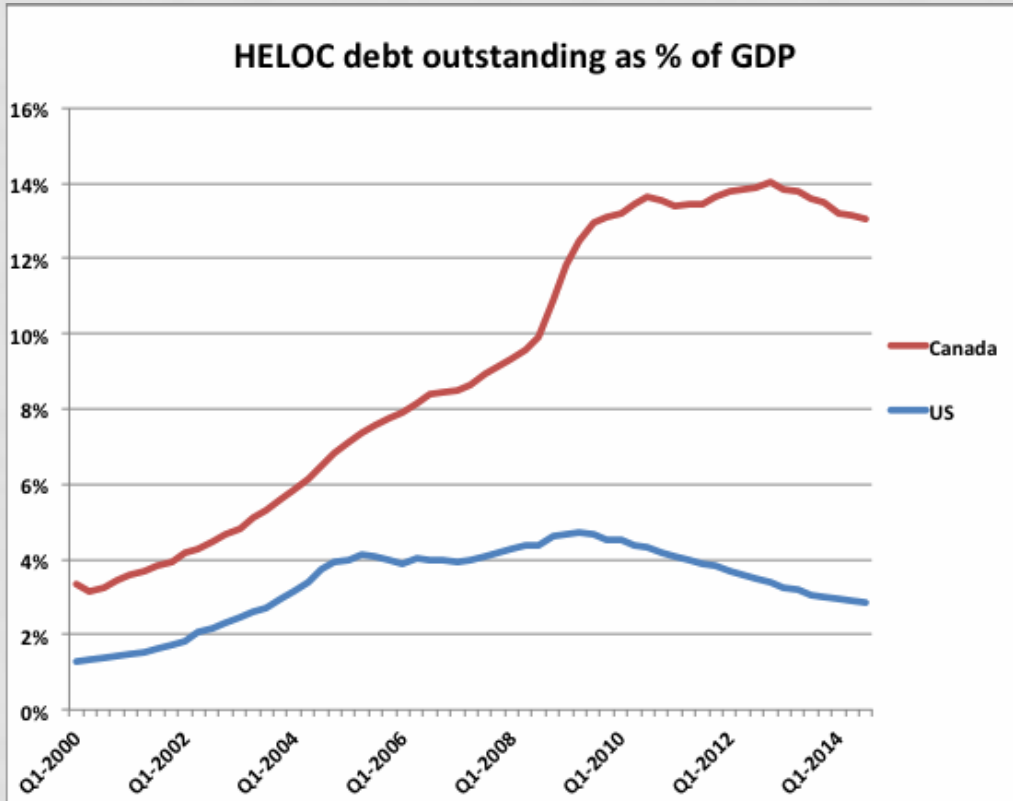
### Residential investment vs construction employment

As of Q4 2014



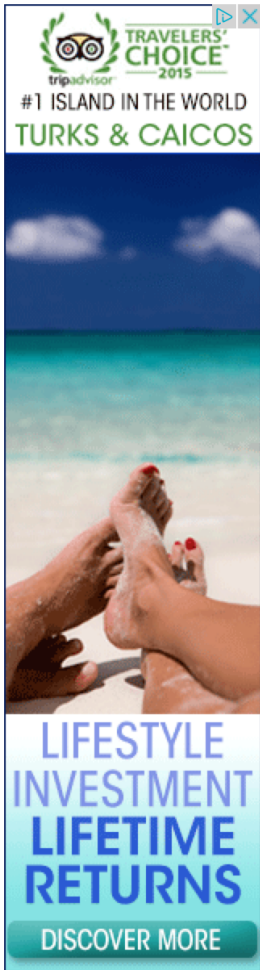
### Residential investment vs population growth: Something's missing this time around





Home equity withdrawal in 2014 estimated at \$63B by CAAMP.

- Cdn mortgage underwriting better than US at peak but consensus is still offside regarding conservative nature of underwriting.
  - 109% LTV loans still possible for first time buyers
  - 100% LTV, cash back mortgages, “flex down”, 35 yr ams on uninsured mortgages.
- Structure of non-prime mortgages is of particular concern.
  - 1-2 yr terms on nearly all Alt-A loans, including non prime books at publicly traded Alt lenders.
  - 1 year, interest only terms for private mortgages
    - “Private lenders are our biggest competitors” –Martin Reid, President of HCG in BNN interview, May 7, 2015.
    - NIM compression in non-prime books at major Alt lenders confirms trend.



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Oshawa / Durham Region



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**2nd and 3rd mortgage (up to 90% LTV)**

Hi, No matter what is the reason why you need a 2nd or 3rd mortgage, I have access to private money. - Poor credit - High loan to value - Fast disbursement and closing - Flexible terms All deals are...

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**\*I Don't Care About Your Bad Credit! Private 2nd Mortgage To 90%**

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Deal Directly with the Decision Makers, and avoid Hassles. You will be dealt Professionally and with Courtesy, same way , as we will like to be Treated Ourselves. There is NO UPFRONT FEE, NO...

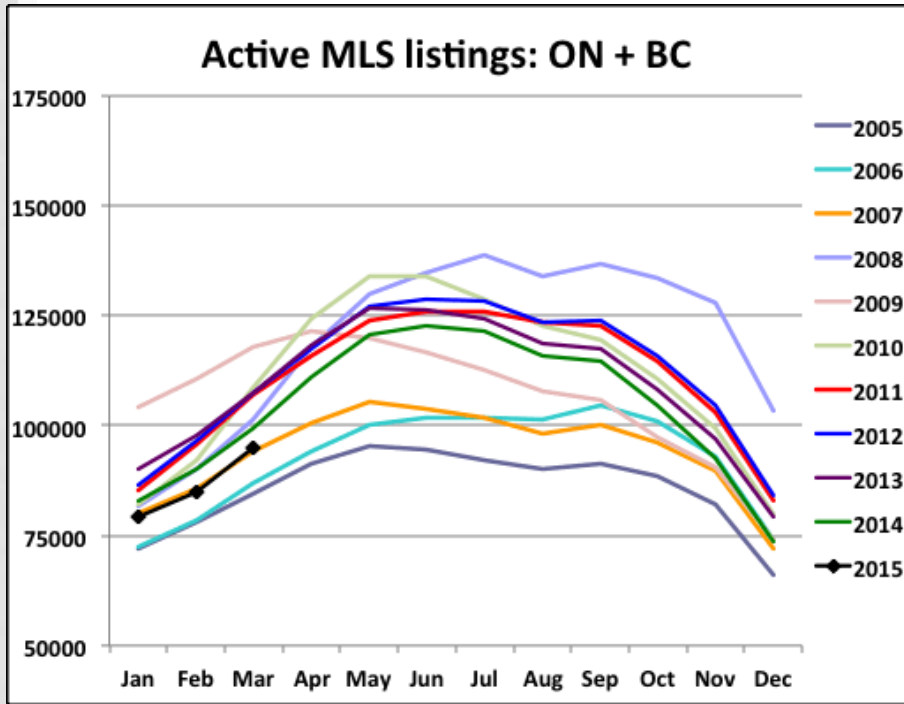
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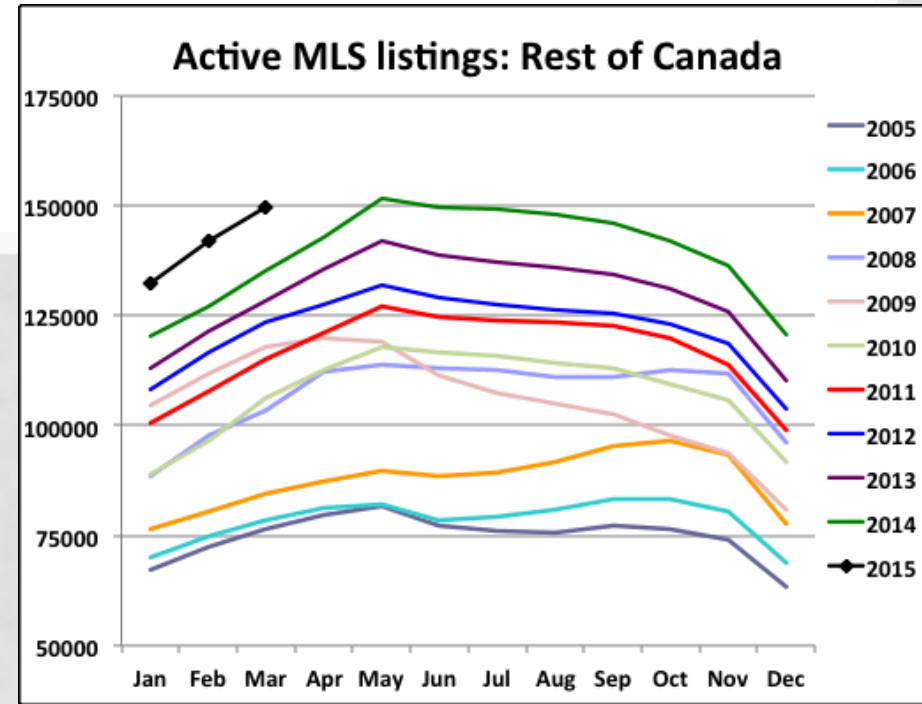
**HAVE YOU BEEN TURN DOWN**

HAVE ACCESS TO MANY PRIVATE LENDERS SECOND MORTGAGES UP TO 95 % LTV CONSTRUCTION FINANCING, MODULAR HOMES,WATERFRONT LOTS,RURAL AREAS (WELL/SEPTIC) SELF-EMPLOYED GREATER THAN 3 MONTHS CONSUMER...

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Mississauga / Peel Region



MOI = 3.5, decade avg of 4.3



MOI = 8.1, 20 yr high





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# The Canadian Housing Market: Will it continue to perform?

Monday May 25, 2015

Craig Sweeney  
Chief Risk Officer  
Genworth Financial Canada



**Genworth MI Canada**

**Canadian Housing Market**

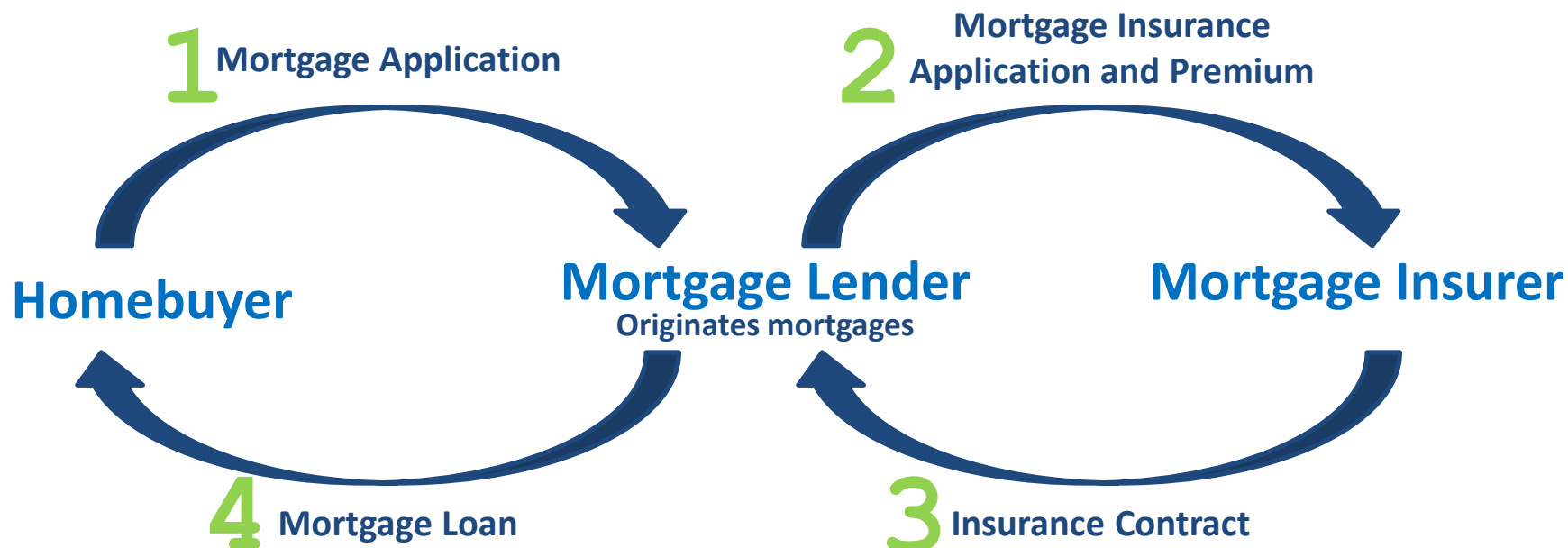
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JUNE 2015



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To supplement its financial statements, the Company uses select non-IFRS financial measures. Non-IFRS financial measures include net operating income, interest and dividend income (net of investment expenses), operating earnings per common share (basic), operating earnings per common share (diluted), shareholders’ equity excluding accumulated other comprehensive income (“AOCI”), operating return on equity and underwriting ratios such as loss ratio, expense ratio and combined ratio. The Company believes that these non-IFRS financial measures provide meaningful supplemental information regarding its performance and may be useful to investors because they allow for greater transparency with respect to key metrics used by management in its financial and operational decision making. Non-IFRS measures do not have standardized meanings and are unlikely to be comparable to any similar measures presented by other companies. These measures are defined in the Company’s glossary, which is posted on the Company’s website at <http://investor.genworthmicanada.ca>. A reconciliation from non-IFRS financial measures to the most readily comparable measures calculated in accordance with IFRS, where applicable can be found in the Company’s most recent management’s discussion and analysis, which is posted on the Company’s website and is also available at [www.sedar.com](http://www.sedar.com).



- Mandatory for less than 20% down payment
- Covers 100% of loan, secured by property
- Upfront borrower paid premium
- Lender receives protection against loss from mortgage default

Government Policy Actions Reduce Risk

**Macroprudential Actions**

- ✓ Purchase LTV Reduced From 100% to 95%
- ✓ Refinance LTV Reduced From 95% to 80%
- ✓ Investment Properties Reduced From 95% to 80%
- ✓ Max Amortization Reduced From 40 to 25 Years
- ✓ All Borrowers Must Qualify at 5-year Fixed Rate
- ✓ Max Debt Service Ratio's Lowered
- ✓ Minimum FICO 600 Required For MI

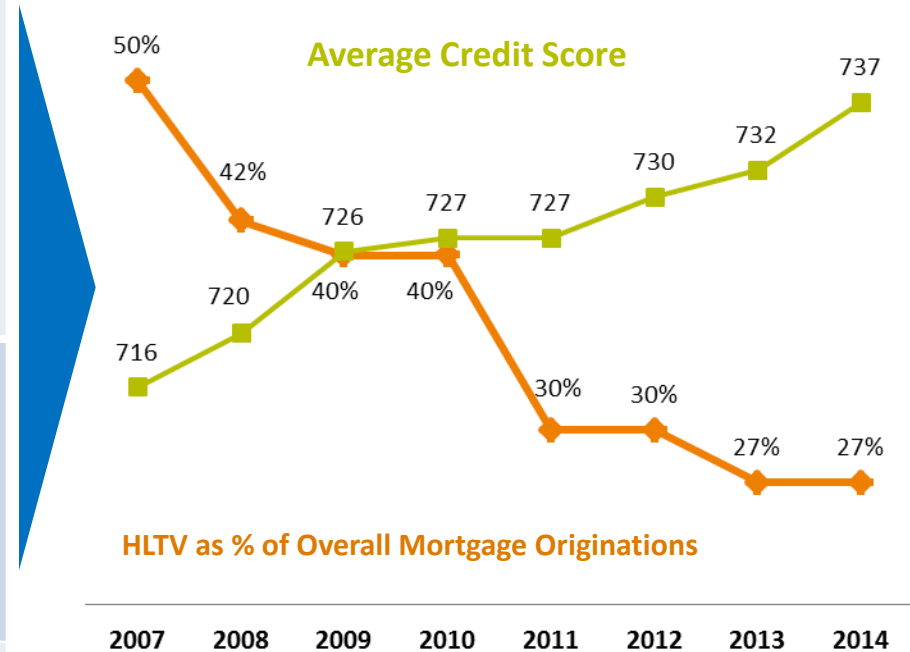
**Microprudential Actions**

- ✓ Increased Regulatory Oversight of Private MIs through PRMHIA
- ✓ OSFI Assumes Oversight Of CMHC
- ✓ New Limits Planned on Gov't Backed MI For low-LTV Mortgages
- ✓ B20 & B21 Policy Guidelines On Mortgage Lending

**Monetary Policy**

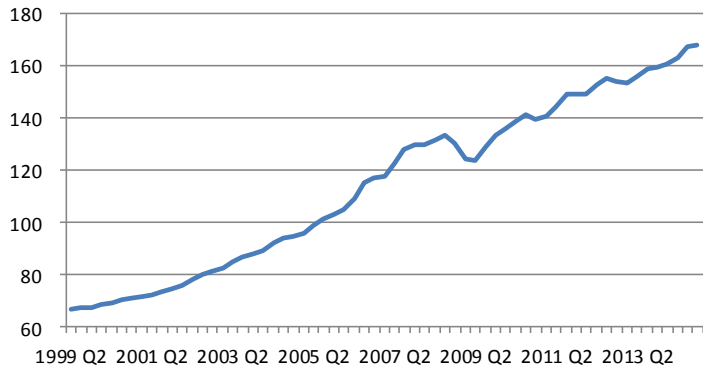
- ✓ Very Accommodative
- ✓ Interest Rates Remain Low To Support Economic Recovery

Quality Of New Business Continues To Improve

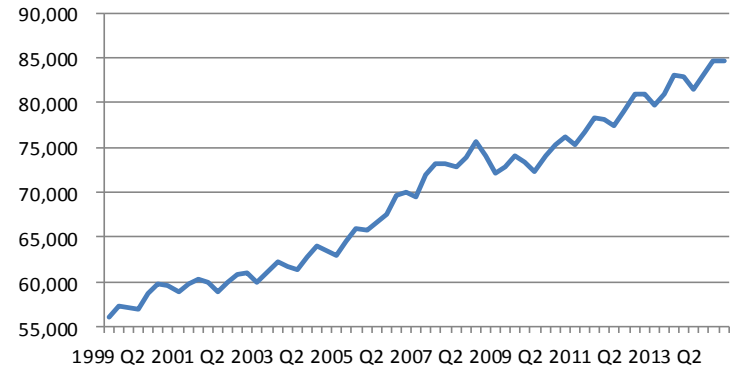


Source: Genworth data, as at December 31, 2014

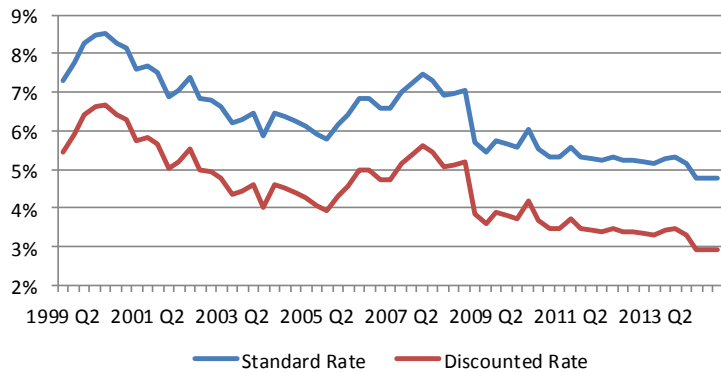
Canada HPI - Teranet



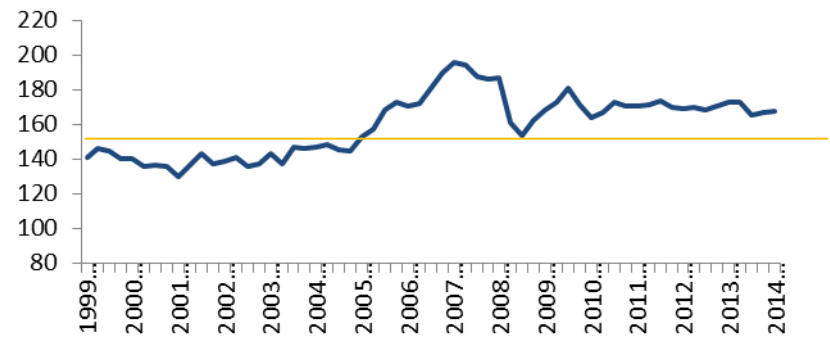
Canada Median Household Income



Canada 5-Yr. Fixed Mortgage Rates



Canada - Income & Interest Rate Adjusted HPI



Source: Genworth data, Teranet, Stats Canada

Region	Average Home Price			Average Income	Average Gross Debt Servicing
	Genworth	Market	% Variance	Genworth	Genworth
Vancouver	\$486K	\$847K	-43%	\$115K	28%
Toronto	\$447K	\$589K	-24%	\$108K	29%
Calgary	\$421K	\$445K	-5%	\$113K	27%
Rest of Canada	\$297K	\$334K	-11%	94K	24%
Canada	\$326K	\$424K	-23%	\$97K	25%

Note: Q1'15 data; Genworth averages for purchase deals only, market averages from CREA; market rest of Canada calculated by using CREA cities weighted average s

**GENWORTH'S AVERAGE HOME PRICE ~23% LOWER THAN MARKET AVERAGE**

## ASSESSMENT OF CURRENT HOUSING RISK

● Stable  
● Monitoring

Region	Risk Level	2015 NIW*	Avg. Credit Score**	Issues / Trends
Vancouver	●	7%	744	<ul style="list-style-type: none"> <li>Income gains and population growth supporting housing</li> <li>Smaller but better quality high LTV market since 2012</li> </ul>
Calgary	●	8%	741	<ul style="list-style-type: none"> <li>Lower oil prices to impact demand in 2015</li> <li>Risk of housing correction currently low</li> </ul>
Toronto	●	19%	741	<ul style="list-style-type: none"> <li>Modestly overvalued, primarily in single family segment</li> <li>Housing starts and household formation balanced</li> </ul>
Montreal	●	5%	744	<ul style="list-style-type: none"> <li>Modest oversupply putting downward pressure on condo prices</li> <li>Strong credit score profile in 2014 &amp; 2015 YTD</li> </ul>

\* New Insurance Written

\*\* YTD. As at March 31,2015



Market Dynamics	2015 vs. 2007
Underwriting standards	<ul style="list-style-type: none"><li>▪ Better underwriting quality in recent years</li><li>▪ Higher risk products eliminated prior to 2011</li></ul>
Portfolio quality	<ul style="list-style-type: none"><li>▪ Stronger borrower profile – average credit score up 21 points in Alberta since 2007</li></ul>
Government policy actions 2009-15	<ul style="list-style-type: none"><li>▪ Increased oversight enhancing safety and soundness housing market (PRHMIA, B20, B21)</li></ul>
Housing market	<ul style="list-style-type: none"><li>▪ Risk of a major housing correction low due to reasonable current valuations</li></ul>

- ✓ Positive economic and regulatory environment
- ✓ Portfolio quality continues to be strong
- ✓ First time buyers purchasing within financial means
- ✓ Housing risk limited to isolated pockets

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