Better Dwelling – May 25, 2023

Canadian Mortgage Delinquencies Begin To Climb, A Lot More Are Brewing

MAY 25, 2023

Canadian real estate might be seeing higher prices, but more buyers can't pay their bills. Equifax data reveals the mortgage delinquency rate climbed in Q1 2023. Households are also increasingly falling behind on payments, a sign that further mortgage delinquencies are in the pipeline. This is occurring as lenders scramble to extend the length of repayments for overleveraged borrowers, hoping to avoid defaults and the downward pressure on prices it can create.

Canadian Mortgage Delinquency Rate & What It Means

First off, let's talk delinquencies, which are greatly misunderstood. Canada's mortgage delinquency rate is the share of total mortgages past due by at least 90 days in Canada. After 90 days, this is the point at which a lender can take action if the borrower doesn't pursue a remedy like reinstating (paying the past due), or redeeming (paying it off in full). Most people think a low rate is a sign of consumer health, but it's actually a sign of market liquidity.

If a borrower knows they won't be able to catch up on payments, they're likely to sell. In a busy market, it's a fast process where the home can be sold before a lender takes action. Slow markets take longer to sell, increasing the odds of delinquency before the property can be liquidated.

Low delinquency rates are more indicative of bubbles than strong consumer health. Not being able to pay your bills in a bull market means you might end up with a profit, and forced sales don't show up as a stat—no one defaulted.

Canada's Mortgage Delinquency Rate Is Climbing

Mortgage delinquencies are climbing across the country. The delinquency rate hit 0.15% in Q1 2023, up 1 basis point (bp) from the previous quarter. Not particularly high, but the highest level since Q2 2022 and the first increase since 2018. However, back then the rate was double the current level. It's not a panic-inducing change, but a sign the normalization that we've been hearing about might arrive soon.

A large share of these are problematic late delinquencies. Roughly 18% of the delinquent accounts are 150 days past due (DPD), and are considered written off with no chance of being saved. Another 63% of those delinquent accounts are between 120 and 149 DPD, approaching the write off point. The remaining 19% of delinquent accounts are between 90 and 119 DPD, in fresh delinquency territory. The longer the account remains past due, the more likely the borrower is to default.

A Further Increase To Canadian Mortgage Delinquencies Is Coming

Early delinquencies indicate we might see mortgage delinquency normalization soon. Accounts 30 to 59 DPD climbed 1 basis point over the past year, hitting 0.18% of mortgages in Q1 2023. Accounts between 60 and 89 DPD also saw annual growth of 0.64 basis points, the largest increase since at least 2019.

Most of the accounts in arrears will be remedied by paying the past due, lender negotiations, or the home will be sold. However, every delinquency starts as "just a little past due," and is considered a warning.

Mortgage delinquencies have been unusually low, and normalization has been widely expected. Over the past few years, it became almost impossible to default with a highly liquid market and lenders granting exceptions like payment holidays. As these programs ended, most experts called a return to healthier levels.

More recently, Canada's Big Six banks have extended amortizations beyond 30 years for nearly 1 in 4 mortgages. The extended length helps over-leveraged borrowers with smaller payments over a longer period, with the regulator believing it can prevent delinquencies and prevent downward pressure on home prices.

It's easy to have a low delinquency rate if you never have to pay off your mortgage. Though that makes the number defaulting even more disturbing—if lenders are pulling out all the stops to prevent defaults and the rate is still climbing, structural problems are likely brewing. That's how a small failure turns into a big one that "no one saw coming."