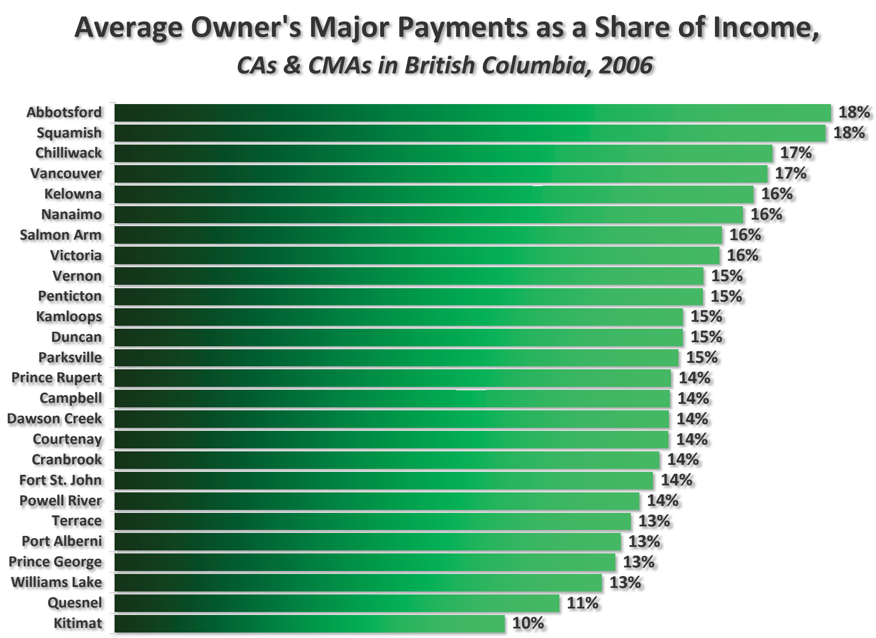
In the Eye of the Beholder:

Housing Affordability in British Columbia

Part 2: Measuring Occupancy Affordability for Owners



URBAN FUTURES
Strategic Research to Manage Change

In the Eye of the Beholder:

Housing Affordability in British Columbia

Part 2: Measuring Occupancy Affordability for Owners

By Ryan Berlin & Andrew Ramlo

Background to a presentation by David Baxter
to the Canadian Home Builders' Association
on November 1, 2010

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I Introduction

This report is the second in a series of Urban Futures publications titled *In the Eye of the Beholder: Housing Affordability in British Columbia*. The series is concerned with the evaluation of existing measures and definitions of housing affordability from the perspective of specific groups of market participants. As a general framework, the series is concerned with the big picture, looking at commonly-cited measures of housing affordability and what they do—and do not—tell us about housing affordability in BC.

The first report, *Evaluating Current Measures of Occupancy Affordability for Tenants*, examined existing measures of tenant occupancy affordability, demonstrating why commonly-cited tabulations of occupancy affordability for tenants reveal little about the causes, nature, and scope of affordability problems that renters have in British Columbia.

This second report focuses on issues of occupancy affordability for owners, which relates to owner-occupied households' ability to make their mortgage payments and pay their property taxes, utilities (water, electricity, oil, gas, coal, wood or other fuels), fees for municipal services,[1] and, if applicable, condominium fees. Although this report builds on the previous work and begins with a review of what current measures of occupancy affordability for owners tell us about housing affordability, an examination of current market indicators of potential affordability problems is made for homeowners in British Columbia, and an outlook for what the near-term future holds with respect to occupancy affordability for owners is provided.

II Survey Measures of Occupancy Affordability for Owners

Historically, there has been little focus on housing affordability issues as they pertain to homeowners when compared to the focus on tenants and their ability to become homeowners. That being said, there was enough focus on one particular dimension of owners' affordability—older homeowners on fixed incomes and their ability (or lack thereof) to pay their property taxes—that it resulted in the introduction of the British Columbia Property Tax Deferment program. This program permits people aged 55 and older (and those with disabilities) to defer property tax payments, with the amount of unpaid taxes together with accumulated interest (at a preferential rate) being registered as a lien against the property and paid at the time the property is sold.

Beyond this specific situation, however, discussions of homeowners' occupancy affordability have not received much attention. This may be explained, in part, by the past three decades being characterized by generally falling interest rates (from a peak of over 20 percent in 1981 to historic lows through 2010) that, all other things equal, have worked to ease the burden of mortgage payments.

This all changed with the onset of the sub-prime mortgage crisis in the United States. Spurred by high levels of mortgage default and foreclosure, discussions of owners not being able to keep up with mortgage payments, owners being "underwater" as the value of their homes fell below the outstanding balances on their mortgages, and banks foreclosing on a large number of properties still dominates discussions of the residential housing market in the United States today. It is therefore not only relevant, but critical, to consider owners' ability to continue to afford their mortgage payments today and in the coming years here in British Columbia.

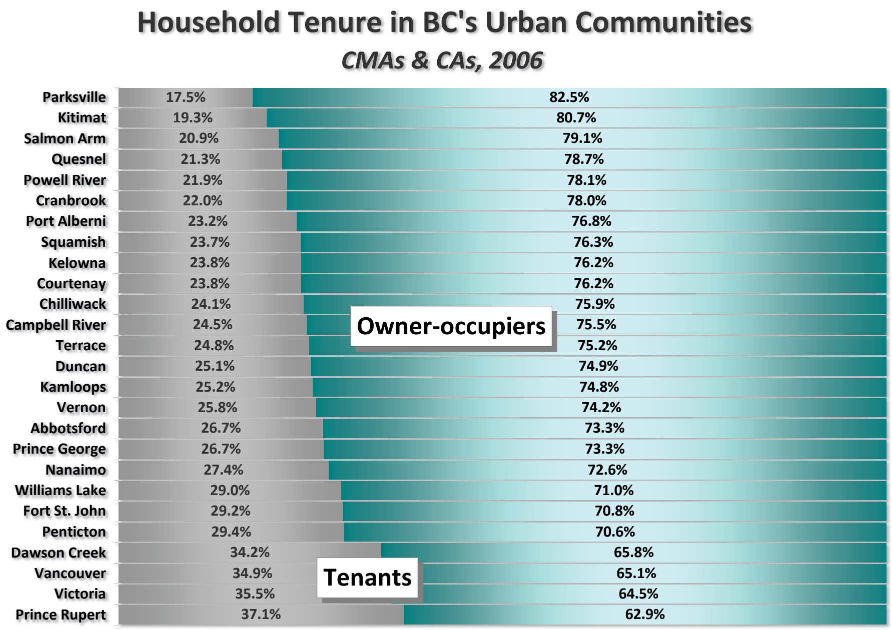
In this context it is essential to be clear that when discussing housing affordability for homeowners it is not housing prices but *occupancy costs*—mortgage payments, property taxes, condominium fees, and utilities—that must be considered. While of deep interest to households who are already owners, those

1 Combined, these elements—mortgage payments, property taxes, utilities, and fees for municipal services—are defined as "owners' major payments.

looking to enter the market, and the media, housing prices alone are not relevant to the ability of existing owners to continue to own their homes; once a household owns their home, and so long as they can continue meet their monthly housing costs within a reasonable share of household budgets, they are able to afford their housing.

1. A Census-based Calculation of Affordability

Figure 1



It is interesting to note that of all dimensions of housing affordability, issues of owners' affordability pertains to the largest number of households in British Columbia, as owner-occupiers accounted for 70 percent of all households in the province in 2006 (the date of the most recent Census enumeration). The share of owner-occupied housing ranged between 63 percent in the Prince Rupert Census Agglomeration (CA) to 83 percent in the Parksville CA (Figure 1). In the Vancouver Census Metropolitan Area (CMA), 65 percent of all households were owner-occupied, similar to the 64 percent for the Victoria CMA.

In order to assess the degree to which housing is affordable for these households, it is necessary to measure the ease with which these households are able to make the payments necessary to remain owner-occupiers. In this vein, Statistics Canada publishes a Census-based calculation of housing affordability for owner-occupiers. Unfortunately, the way in which Statistics Canada tabulates this calculation renders it of little use in measuring the extent or incidence of owner-occupiers' housing affordability problems. The reason that this Census-based measure does not provide a valid description of the affordability situation for owner-occupiers is that the data are not collected in a way that ensures households reconcile their total expenditures (including housing costs) with their income.

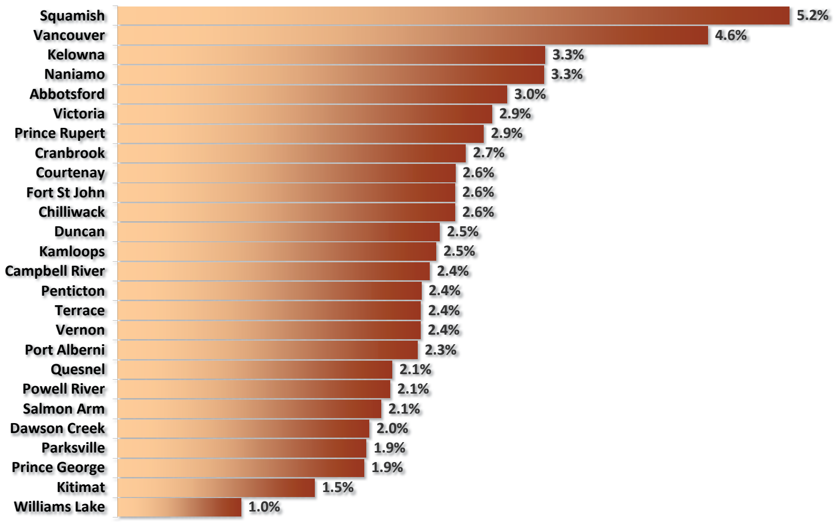
Rather, Statistics Canada's affordability measure is created by combining information from two separate questions in the Census questionnaire, one concerned with households' previous-year (2005) income and another concerned with households' current-year (2006) spending on "owner's major payments". The result is what is called a "derived variable" and, in many instances, may not be what it is purported to represent—that is, the percentage of a household's income that is spent on shelter costs. Instead, it represents a ratio calculated between one year's housing costs to another year's income—specifically, 2006 housing costs and 2005 income. Only if incomes did not change from year-to-year (which they do) would it make sense to use a ratio of income from one year to housing costs from another year.

As an example of the challenges created by deriving variables from different parts of the Census questionnaire, the Statistics Canada affordability calculation indicates that there are many owner-occupier households in British Columbia who spend 100 percent (and more in some instances) of their household income on major housing payments. As Figure 2 shows, the percentage of households spending more than their income on housing ranges from a high of five percent in the Squamish CA to a low of one percent in the Williams Lake CA.

Figure 2

Percentage of Owner-Occupiers Spending 100% or more of their Income on Owner's Major Payments in British Columbia

CMAs & CAs, 2006



The reality is that this is impossible: households cannot spend more than, or all of, their income on shelter as they would not have any money to spend on food, transportation, entertainment or any other typical household expenditure.

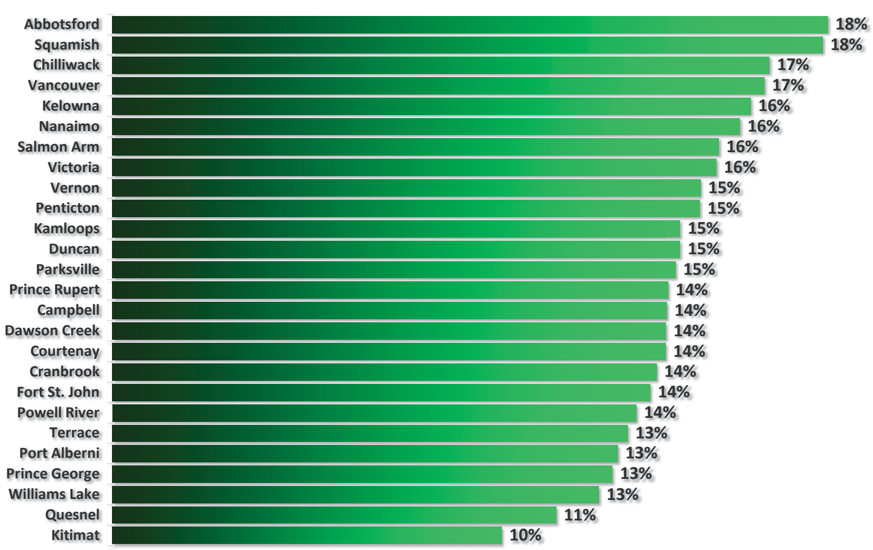
Unfortunately, this problem cannot be solved by excluding from consideration those households whose housing cost -to-income ratio is 100 percent or more, as this would still not account for the other households who are purported to be spending 99 percent or 98 percent (and so on) of their income on housing. There is no threshold that can be established to deal with those households who should be included or excluded, as the problem is not caused by including or excluding, but rather by using income from one year and housing costs from another to derive an index.

The impossible situations represented by the Statistics Canada affordability index are the result of households whose prior year incomes were lower than their current year incomes out of which they were paying for housing. Ironically, households who may have experienced a decline in income between 2005 and 2006 (such as someone recently unemployed) would be shown to be spending a smaller percentage of their incomes on housing than they actually were; a statistic that would not characterize the true affordability situation for that particular household. The flaw associated with matching housing costs from one year with incomes from another year means that Statistics Canada's Census-based calculations on owner-occupied housing affordability do not assist in identifying the specific nature, causes, or extent of affordability problems for owner-occupiers in British Columbia's communities.

Figure 3

Average Owner's Major Payments as a Share of Income,

CAs & CMAs in British Columbia, 2006



While of little assistance in measuring the extent of affordability problems or in identifying the owner-occupied households experiencing them, the aggregate data on average 2005 incomes and owners' 2006 major payments do give some indication of the *average* share of household income devoted to major housing payments. The ratios range from 18 percent of 2005 income spent on major housing payments in 2006 in the Abbotsford CMA and Squamish CA, to a low of ten percent in the Kitimat CA (Figure 3). With a province-wide average of 16 percent, owner-occupied households in BC spend, on average, less than the generally-accepted rule of thumb for affordability—that a household should spend no more than 30 percent of its gross income on housing—and thus these data indicate that there is not a systemic owner-occupancy affordability problem in BC. Beyond this, however, Statistics Canada's Census-based tabulations of 2005 income and 2006 spending on housing tell us little about the extent of affordability problems in BC's communities or about the owners who may be experiencing such problems.

2. The Survey of Household Spending

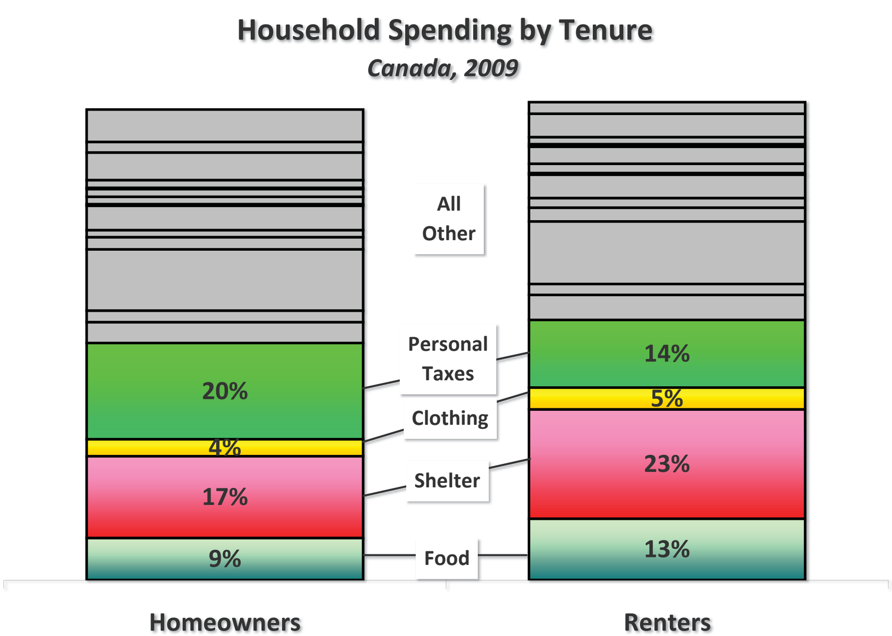
In addition to the difficulties posed by combining 2005 income and 2006 owners' major payments, another shortfall of the Census-based calculation of housing affordability is that it does not involve directly asking households, of current total household expenditures, how much is spent on housing (and other living expenses).

Statistics Canada does ask these questions (in a sense) in another survey—the Survey of Household Spending (SHS)—in which respondents provide details on income, changes in assets and savings, and current household expenditures. The SHS is carried out annually by Statistics Canada, collecting information from a sample of Canadian households about their spending on a wide range of items from food, clothing, and transportation, to rent, mortgage payments, and other household operations. The virtue of this particular method of data collection is that housing based expenditures are considered alongside all other expenditures and household income in that same year.

While tabulations of these survey data include spending details by household tenure (for tenant households and for owner-occupied households) and by income group, the results are not published for urban regions within Canada, and hence the data can only be used to indicate general levels of spending on housing relative to incomes Canada-wide.

The most recent (2009) data from the SHS show that, on average, owner-occupiers spend 17 percent of their household income on shelter, which is generally consistent with the province-wide average of 16 percent according to the most recent Census. One of the reasons for the SHS average being higher than the Census average is that the SHS category of spending on "shelter" includes more expenditure items than does the Census-defined "owner's major payments" category. These data indicate that owners can, on average, afford housing; however, neither the data from the SHS nor any other published data indicate the degree to which some owners are experiencing affordability problems.

Figure 4



These data confirm what the adjusted Census affordability ratios for owners (and for tenants, as demonstrated in the first report in this series) show: that overall, owner-occupied households do not suffer from widespread, acute affordability problems, as on average they are spending substantially less than 30 percent of their income on shelter. That being said, to the extent that it is recognized that certain segments of the population have specific affordability concerns, it is important to note that there are no existing data that can be used to measure the extent or incidence of these affordability problems for homeowners in British Columbia.

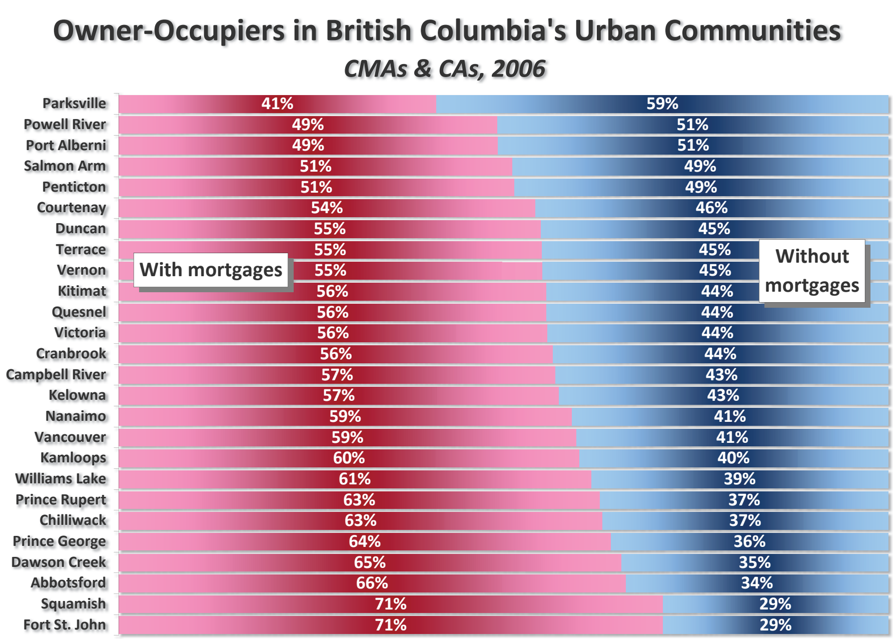
3. Owner-occupied Households and Mortgages

The single largest liability on an owner-occupied household's balance sheet is typically its mortgage. As such, discussions about the ability of households to afford to remain in their homes are overwhelming concerned with their ability to make mortgage payments. The deep and recent recession in the United States was precipitated by the inability of a large number of households to meet their mortgage payments; in other words, the post-2008 period in the United States has been characterized by a dramatic and widespread owner-occupier affordability problem. With this as the backdrop, this section considers whether this might be a concern in British Columbia in the coming years by examining the most recent Census-based owners' major payments data and the degree to which they may, or may not, indicate potential affordability issues in the years to come.

It may be a surprise to some that owners spend a relatively small proportion of their (previous year) income on (current year) major housing payments—in the range of ten to 18 percent in BC—when compared to the proportion spent by tenants (in the range of 15 to 26 percent[2]). One of the primary reasons for the relatively low share of income going to major housing payments for owner-occupiers is that the data include households both with, and without, mortgages. As the cost of accommodation for homeowners declines significantly once the mortgage is paid off (all else being equal), it is important to separate these two groups of owner-occupiers—those with a mortgage and those without—in the analysis of, and in discussions of, housing affordability.[3]

In British Columbia, 42 percent of owner-occupier households have no mortgage on their home. This varies widely with in the province, from a low of 29 percent in the Squamish and Fort St. John CAs to a high of 59 percent in the Parksville CA (Figure 5). Within this range, the communities where there is the greatest exposure to mortgage risk for owner-occupiers would be, all other things equal, Squamish and Fort St John where 71 percent of the households have mortgages, Abbotsford (66 percent), Dawson Creek (65 percent), and Prince George (64 percent). Less exposure exists in communities such as Parksville (where 59 percent of homeowners have no mortgage), Powell River (51 percent), Port Alberni (51 percent), Salmon Arm (49 percent), and Penticton. (49 percent).

Figure 5

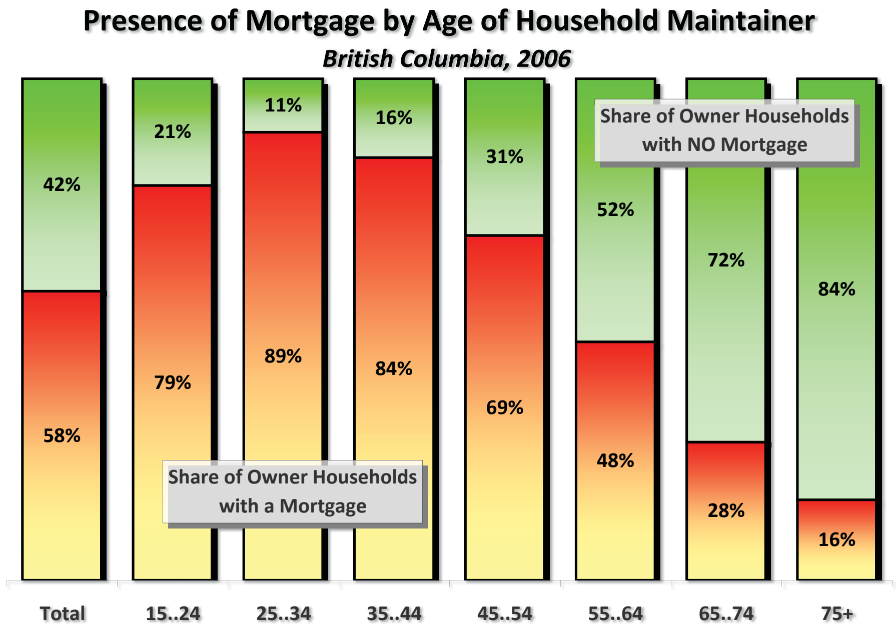


As there is a strong relationship between age and the propensity to have a mortgage, the mortgage vulnerability

2 *In the Eye of the Beholder: Evaluating Current Measures of Occupancy Affordability for Tenants*, Urban Futures, 2010.

3 This is not to say that households without mortgages are completely free of any affordability concerns, just that it is important to consider those with mortgages and those without mortgages separately, as the nature of any affordability concerns that do exist for each type of household would likely be quite different.

Figure 6

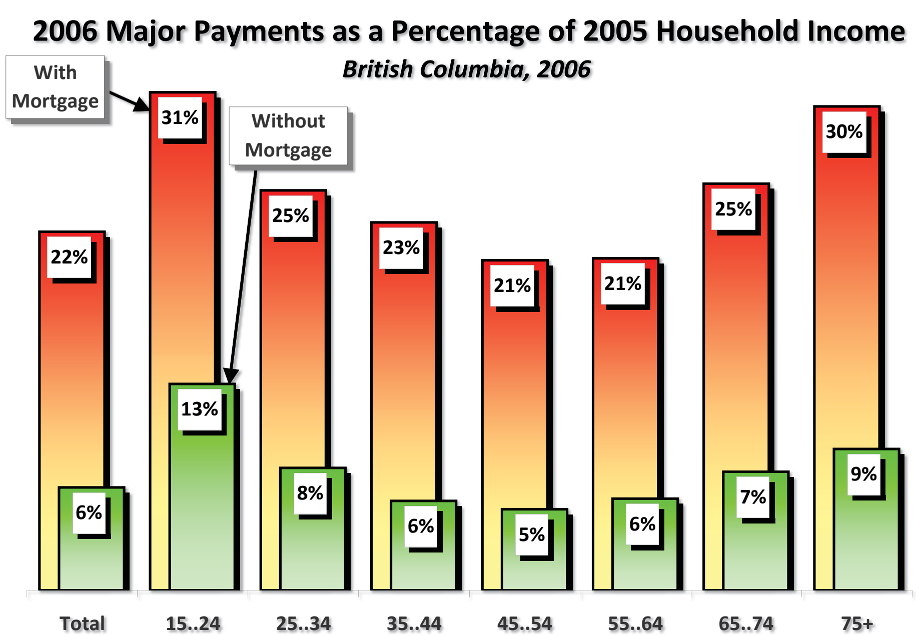


of these communities is in part reflective of their underlying demography. As would be expected, the lifecycle pattern of mortgage indebtedness shows that young households who are just starting out as owner-occupiers have relatively high levels of mortgage debt: for example, the 2006 Census indicated that 89 percent of owner-occupiers in the 25 to 34 age group in the Vancouver CMA had mortgages (Figure 6). As the household ages and pays down—and eventually pays off—the mortgage, the mortgage presence incidence rate falls, with only 16 percent of those in the 75-plus age group having mortgage debt.

In again considering the communities listed above, it is not surprising then that the six with the highest proportion of owner-occupied households without a mortgage (Parksville, Powell River, Port Alberni, Salmon Arm, Penticton, and Courtenay) all ranked in the top seven communities in BC in terms of the share of their populations aged 50-plus. Conversely, the five communities with the highest proportion of owner-occupied households with a mortgage (Fort St John, Squamish, Abbotsford, Dawson Creek, and Prince George) had six of the seven highest percentages of population aged 25 to 49.

The other issue that must be considered as part of this discussion is the share of income going to owners' major payments for households with, and without, a mortgage. While in British Columbia as a whole owners' major payments in 2006 accounted for an average of 16 percent of households' 2005 income or all owned households, the share for households without mortgages was only seven percent versus 22 percent for those with mortgages (Figure 7). Thus, in separating households with a mortgage from those without, the Census data show that as a share of income the housing payments made by owner-occupied households with mortgages is in a comparable range to that of tenants.

Figure 7



When considered on an age specific basis there are two groups that stand out in Figure 7. Both the youngest cohort (15 to 24) and the oldest (75-plus) have current-year housing costs to prior-year income ratios that are at or above the generally-acceptable rule of thumb level (30 percent) for the share of household income going to housing costs. In the 15 to 24 age group (where there are very few owner-occupier households) the ratio of 2006 owners' major payments to 2005 income of 31 percent is the highest among all age groups. As this age group sees significant changes in household income from one year to the next, the high ratio is likely attributable to the fact that the income used in the calculation is from 2005 and the payments from 2006. That said, although the highest of all age groups, major payments as a share of income for this age group are only marginally above the 30 percent housing affordability benchmark. A similar situation is seen for the most senior age group where major housing payments represent 30 percent of household income for those still paying off their mortgage.

While the data in Figure 7 may raise some affordability-related questions for these two age groups, what the data also show is the strength of paying off the mortgage: the overwhelming majority of older households (84 percent of the owner-occupiers in the 75-plus age group, Figure 6) benefit from being a homeowner without a mortgage, with major housing costs representing under ten percent of prior-year income. Any housing affordability challenges that these mortgage-free households face will relate more to their ability to pay for their utilities charges, municipal fees, condominium fees, and property taxes. In the specific case of the seniors population and those with disabilities, the province's Property Tax Deferment Program can provide assistance should it be needed.

4. Summary of Current Affordability Measures

The Census-based tabulations of income and housing costs that are commonly used to assess the affordability situation for owner-occupiers tend to distort affordability issues, as they rely on ratios of previous-year income and current-year owners' major payments and do not directly ask respondents to detail their particular basket of expenditures relative to their reported household income. The Survey of Household Spending, on the other hand, may provide a more appropriate evaluation of affordability, as it relies on household income and spending data from the same year and requires that the sum of all spending (and saving) be reconciled with total household income. Unfortunately, the SHS is not published for individual communities, and thus is only able to provide a summary of the broader affordability situation in the province.

Given these limitations, it is important to re-iterate that while both surveys show that housing affordability problems for owner-occupiers are not currently widespread throughout the province as a whole—with the majority of households spending less than the benchmark 30 percent of their income on housing—neither provide much assistance in identifying the extent of the affordability problems that do exist or the individuals who are experiencing them.

III Recent Evidence on Ownership Affordability Concerns

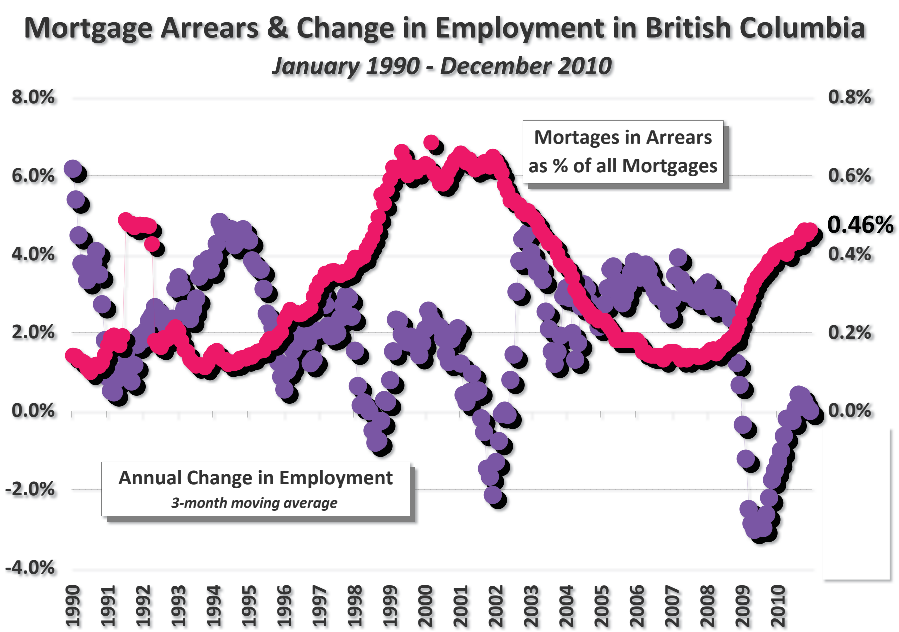
As evidenced by the continued growth in foreclosures south of the border contrasted against the continued price increases in Canada, housing affordability situations have certainly changed since 2006. By the end of 2010, mortgage delinquency rates in the United States were, for prime loans, in the range of 5.2 percent (fixed) and 13.3 percent (variable), while for sub-prime loans they were in the range of 23.8 percent (fixed) and 29.8 percent (variable). These rates compare to delinquency rates of 2.6 percent for prime loans and 13.3 percent for sub-prime loans in 2006.[4] Housing starts last year (2010) were at an all-time low of 586,900 (compared to 1,800,900 in 2006),[5] and the number of vacant residential units has risen to 9.1 million (compared to 7.6 million 2006).[6]

4 *National Delinquency Survey*, Mortgage Brokers Association of America, Q4 2010 and Q4 2006. Note that the delinquency rate includes loans that are at least one payment past due but does not include loans in the process of foreclosure.
5 New Privately Owned Housing Units Started, 1959-2010, US Census Bureau.
6 2011 *Population Survey/Housing Vacancy Survey*, US Census Bureau.

In Canada as a whole, while the data show that the overall level of affordability for owner-occupiers has remained generally at its 2006 level—with owner-occupied households spending 17 percent of their income on housing—residential sales data show that average prices in Canada increased by 11 percent between 2006 and 2010, and in BC by 29 percent. Given the substantial price increases provincially, there is some concern that British Columbia could see the number of households with affordability problems increase in the coming years as lending rates begin to rise. While there are many opinions about this issue, it is instructive to explore the available data on mortgage arrears in BC in order to understand both how they have changed over the recent past and how increasing lending rates may impact them in the coming years.

Mortgage arrears information is published monthly by the Canadian Bankers Association. This information tabulates, for each province, the total number of mortgages held by the seven major national banking institutions, the number of these mortgages for which the payments are three months or more in arrears, and this number as a percentage of the total number of mortgages held by these institutions (the arrears rate). From one perspective, the data for British Columbia (shown in Figure 8) indicate a dramatic change—a tripling—in the mortgage arrears rate over the past three years: in December of 2010, 0.46 percent of the mortgages in British Columbia held by major Canadian banks were in arrears (4.6 of every 1,000 mortgages), three times the 0.14 percent rate that prevailed during 2006 and 2007. Clearly, these data show that affordability (as it pertains to homeowners) deteriorated over this period.

Figure 8



While the arrears *rate* has changed significantly, it is important to put this in context: the 0.46 percent of mortgages three months or more in arrears represents only 2,772 mortgages out of a total of 596,750 in British Columbia. This alone is hardly evidence of a widespread affordability problem, particularly in comparison to the 8.6 percent rate of serious delinquency[7] that currently prevails in the United States (86 mortgages out of every 1,000).

Unlike the record-setting arrears rates observed in the United States, the current arrears rate in British Columbia of 0.46 percent sits below the 0.5 to 0.6 percent arrears rate that prevailed from 1998 to 2003. Given the roller-coaster pattern exhibited by the arrears rate over time, it is hard to determine what a normal level of arrears would be; however, with the average arrears rate in BC over the past two decades being 0.36 percent, the current level could be considered slightly high, albeit by a small margin. A similar situation is seen nationally, with the arrears rate at the end of 2010 at 0.44 percent, up above a low point of 0.24 percent seen in 2006, but only slightly above its long-run historical average of 0.42 percent.

If we look to the roots of the recent increase in the arrears rate, we find that the pattern of change is more in keeping with cycles of economic activity observed within the province and not by the forces that caused widespread market failure in the United States. In BC, the increase in the arrears rate between 2009 and

7 The *serious delinquency* rate is defined as the percentage of loans that are 90 days or more past due or in the process of foreclosure.

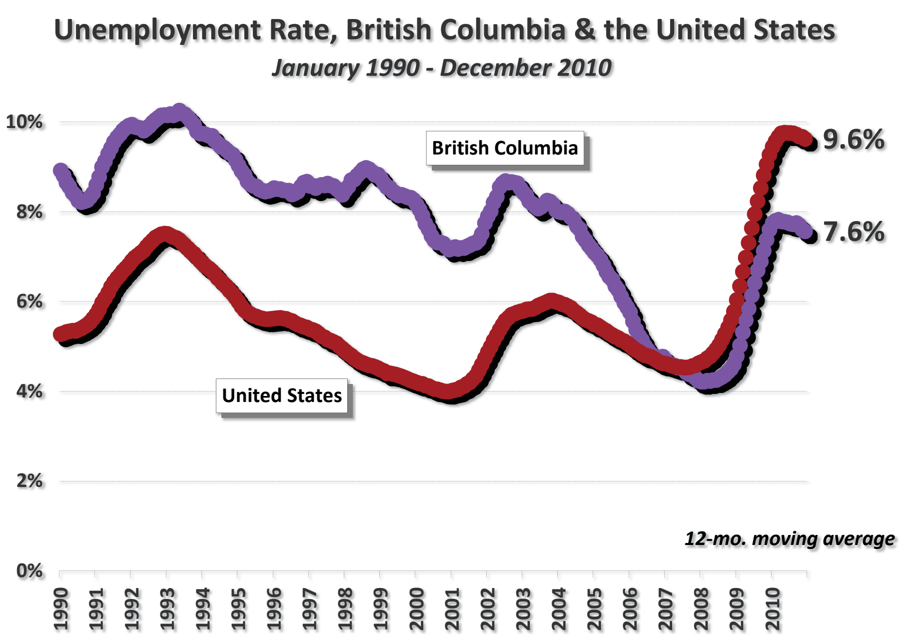
2010 matched the largest loss of employment that the province experienced at any point over the past two decades: by May of 2009, there were three percent fewer jobs in the province than there were a year earlier. While job losses had ceased by the end of 2010, at that point in time there were 13,000 fewer jobs in the province than there were only 12 months earlier, and 40,000 fewer than there were two years before.

The previous peak in arrears rates, in the 0.6 percent range between 1999 to 2003, was also associated with two periods of employment losses, one in 1999 and one in 2002. Conversely, the low arrears rate period of 2005 to 2008 corresponds with a period where employment growth was in the range of three percent annually. Looking back a decade earlier (1993 to 1996), the same low 0.14 percent arrears rate corresponded to annual employment growth in the four percent range.

Thus, BC's current mortgage arrears rate appears to be responding to broader changes in the economy. As employment growth resumes, arrears rate is expected to follow past trends, which is to plateau as employment again begins to grow, followed by a decline through the next stage in the economic cycle.

It is useful to compare not only BC's and the United States' mortgage arrears situations, but also their relative economic situations, which shows how normal the contemporary context is in this province and how dramatically unusual it is in the United States. Historically, British Columbia has experienced a significantly higher unemployment rate than the United States, averaging 8.7 percent between 1990 and 2004, compared to an average of 5.6 percent in the United States (Figure 9). Overall during this period, the unemployment rate in the province was 3.1 percentage points (55 percent) higher than the US average. Over the subsequent five years, BC's unemployment rate fell from eight percent at the beginning of 2004 to a record low of 4.2 percent in early 2009; the unemployment rate in the United States also declined over this period, although not by nearly as much, falling from six percent to 4.5 percent. Since 2008, in an unprecedented scenario, unemployment rates in British Columbia were lower than in the United States.

Figure 9



The increase in unemployment rates triggered by, and contributing to, the recent recession has also been unprecedented, with the unemployment rate in the United States more than doubling, from 4.5 percent to 9.6 percent—the highest employment rate since the 1983 recession and almost twice its average level over the 1990 to 2004 period. In contrast, while the unemployment rate in British Columbia increased from 4.2 percent to 7.6 percent, in doing so it essentially returned to its normal long-run level (in the neighbourhood of eight percent). Given the historical spread between unemployment rates in BC and in the US, what the United States is currently experiencing is the equivalent of an unemployment rate of 15 percent in British Columbia. Thus, just as the mortgage arrears rate, default rates, and the unemployment rate are all at unusually high levels in the United States, they are not currently at such levels in British Columbia.

IV The Future of Occupancy Affordability for Owners

While the mortgage arrears data show that the affordability picture in British Columbia has deteriorated since the 2006 Census (as the number of mortgages in arrears and the arrears rate have both grown) they also show that the arrears rate still currently falls well below historical peaks. While this may reassure some, others are concerned about the situation that may arise in the coming months and years as interest rates inevitably increase from their historical lows.

The primary focus of this latter concern is the prevalence of variable-rate and short-term, fixed-rate mortgages. These mortgage terms means that although borrowers have the opportunity to realize the benefits of falling interest rates (which they have generally done since the 1990s), they also have the obligation to incur the costs of rising rates. As there is no apparent reason to see further declines in interest rates, the future concern is clearly with the affordability consequences of rising lending rates.

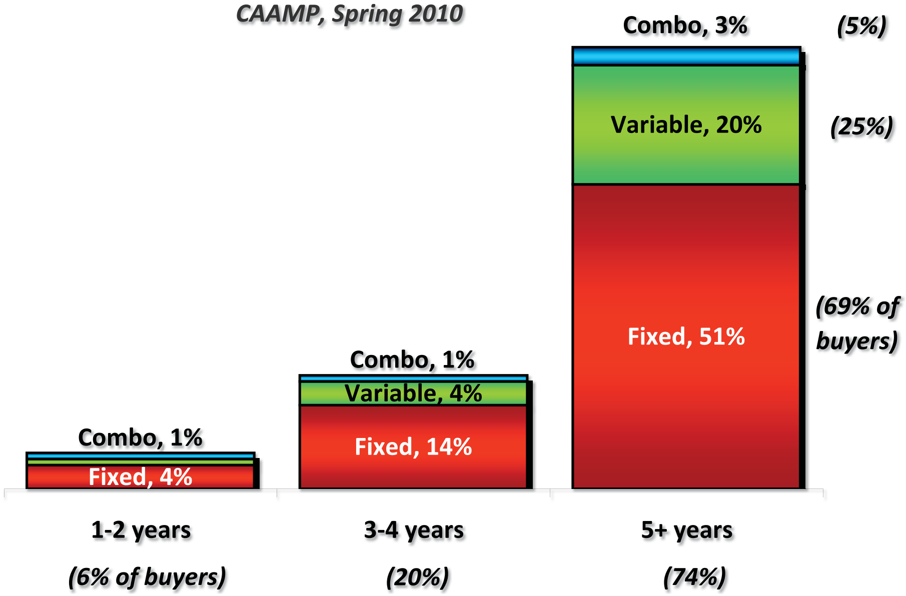
Two relevant issues need to be addressed here: the proportion of mortgages with variable and shorter-term contracts; and the rate at which interest rates are expected to increase.

While a significant number of householders do opt for shorter-term variable-rate contracts, they do not represent the majority of households. For example, data published by the Canadian Association of Accredited Mortgage Professionals (CAAMP) show that almost three-quarters of buyers choose contract terms of five or more years (with 94 percent choosing three or more years), 51 percent choose fixed mortgage interest rates and five-year terms, and 14 percent choose fixed rates and 3 to 5 year contractual terms (Figure 10). Only a very small percentage of first-time buyers—six percent—choose contract terms of under three years, and only one-quarter of those choose variable interest rates. Borrowers are aware of the risks of short-term and variable-rate mortgages, and appear to be realistic in their assessment of how to position themselves with respect to these risks.

Figure 10

Mortgage Financing Arrangements, Canada

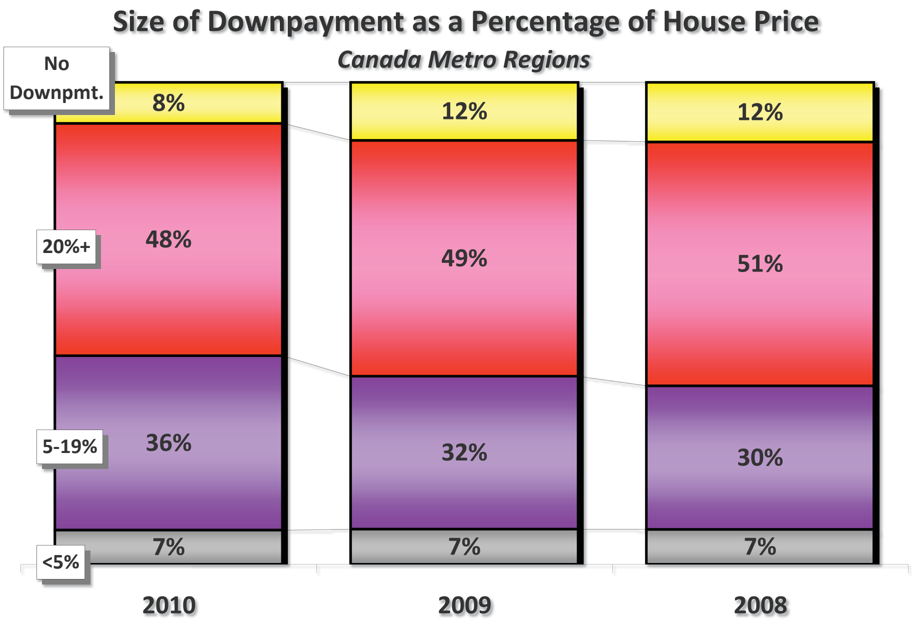
CAAMP, Spring 2010



While these mortgage financing data are not available specifically for British Columbia, there is no evidence that purchasers in this province are substantially less prudent (if at all) than those in the rest of Canada. As an example, one need only to consider the mortgage arrears rate in BC, which is only marginally above the national rate (0.46 percent versus 0.42 percent).

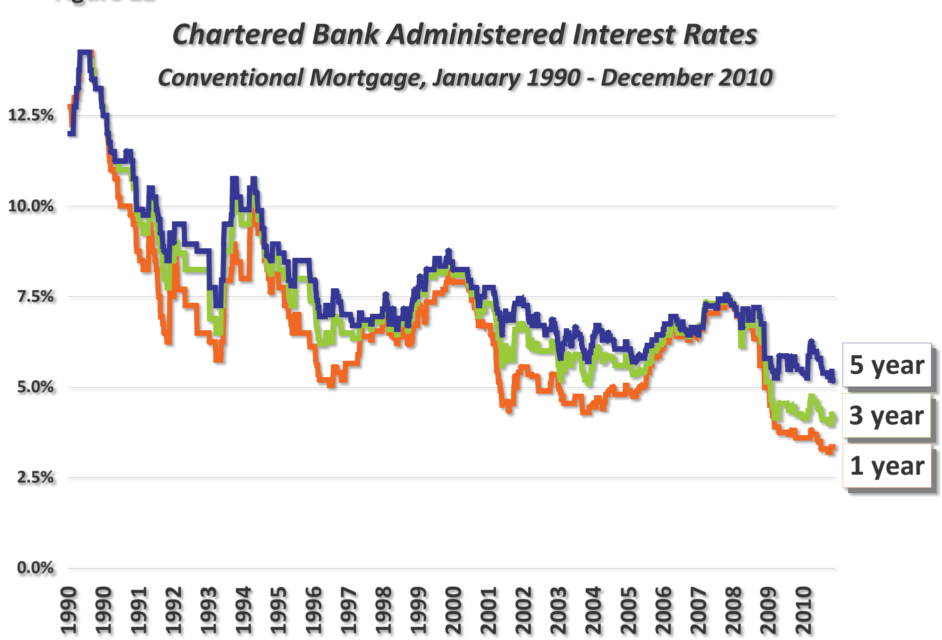
In the context of considering the short-term future of housing affordability, an additional consideration is the magnitude of household debt-servicing and the size of down payment. While many sub-prime mortgages in the United States required little or no down payment—a circumstance that became dire from an affordability perspective as housing values fell below outstanding mortgage balances for many households—the situation is much different in Canada. Canada Mortgage and Housing Corporation (CMHC) survey data show that of all home purchases between 2008 and 2010 only seven percent were

Figure 11



CMHC: home purchasers in Halifax, Montreal, Toronto, Calgary and Vancouver only; excludes did not know & no

Figure 12



associated with a down payment of five percent or less (Figure 11). Furthermore, between 48 percent and 51 percent of all purchasers indicated that their down payment was 20 percent or more. Even in Canada's most expensive housing market (the Vancouver CMA) the CMHC survey data indicated that only two percent of all recent purchases were associated with less than five percent down.

Finally, while interest rates will clearly increase in the future, the range of factors that will contribute to the timing and pace of their change are wide and varied. Therefore, and as a starting point, it is instructive to consider how rates have changed historically. As the data in Figure 12 show, during the low interest rate environment that has prevailed over the past decade and a half, rates for conventional mortgages generally took two or more years to increase by one percentage point (in the case of five-year rates), gradually marching their way upward rather than sprinting forward.

Thus, barring some extreme set of circumstances—such as rapid general price inflation—there does not appear to be grounds for concern about a sudden and sharp increase in interest rates. This is reinforced when considering the recent appreciation of the Canadian dollar against its US counterpart. All other things equal, any increases in interest rates in Canada would lead to further upward pressure being placed on the Canada/US dollar exchange rate, which in turn would have a detrimental effect on a wide range of domestic exports, from cars built in Ontario's manufacturing heartland to logs harvested from BC forests.

As such, in considering both the current housing affordability context for BC and Canada, and the factors that could impact affordability-related issues in the coming months and years—including trends in mortgage lending rates, mortgage financing arrangements, and down payments—the existing data do not reveal the existence (or emergence) of a US-style affordability crisis in the this province.

V Conclusions

There exists a wide range of measures and indicators of owners' occupancy affordability—that much we do know. What we do not know much about, however, are the origins, nature, and extent of the affordability problems experienced by certain owner-occupied households in British Columbia. No single number—be it an average, a median, or any other point measure—can adequately represent the diverse range of issues associated with housing affordability for all owners.

The most commonly-used data in discussions of housing affordability in British Columbia are from the most recent (2006) Census. While housing affordability is typically measured by considering the percentage of a household's income that is spent on major housing costs, the data from the Census, unfortunately, are of only limited use in this respect. This is because this "derived" variable is generated by way of asking respondents to the Census to indicate their *2005* income on one part of the questionnaire and their *2006* housing costs on another. While these issues makes measuring affordability problematic through the Census, the data do show that, on average, owner-occupied households in British Columbia spend between ten and 18 percent of their income on housing. This is significantly below the generally-accepted threshold for affordable housing of 30 percent of income going to housing costs.

A less widely-cited survey, the Survey of Household Spending (SHS), represents a refinement over the Census-tabulations of affordability in that current-year expenditures, on everything from housing to clothes to pet supplies, are reconciled with current-year income. This eliminates the impossible situation of a household reporting that it spends 100 percent or more of its income on housing, as certain tabulations from the Census appear to show. While not as comprehensive as the Census in terms of its sample size or geographic coverage, the most recent (2009) data show that on average in Canada owner-occupied households spend 17 percent of household income on shelter costs—well below the 30 percent threshold for affordability.

While they are not necessarily ideal sources of data for the purposes of measuring housing affordability, both the Census and the SHS show that on average, in BC and in Canada, owner-occupied households spend considerably less than 30 percent of their income on housing. In other words, these data do not reveal systemic and widespread owner-occupier affordability problems. As we do know that affordability challenges exist for some households, it is unfortunate that neither survey reveals much detail about the nature or extent of the problems being experienced by those households.

There is also much discussion about the affordability of housing for owner-occupiers in British Columbia in the coming years. While recent data on mortgage delinquencies show BC's arrears rate increasing significantly over the past few years, it is important to put the current arrears rate in context: at 0.46 percent, it is only marginally above its long-run provincial average, and falls significantly below the equivalent 8.6 percent seen in the United States. Moreover, the increase in BC's arrears rate coincides with a unique set of economic circumstances that saw the province's unemployment double over a two-year period. In the coming years however, as BC's economy recovers from the recession and resumes along its long-run growth trend, it is expected that both the unemployment rate and the mortgage arrears rate will steadily decline from levels seen today.

For many, the current low interest rate environment presents affordability concerns for homeowners insofar as rates can be expected to rise in the coming years. While this may be true, history has shown that when rates do rise they do not do so rapidly. Furthermore, while unpredictable short-term increases in mortgage interest rates would especially impact those owner-occupiers with shorter-term variable-rate mortgage contracts, the majority of homeowners choose five-year fixed-rate contracts, thereby mitigating some of the effects of potentially rising rates.

Given this body of evidence, there is no empirical basis on which to say that BC currently suffers from widespread owner-occupied housing affordability problems, nor are there signs of impending doom on the horizon.

All of this being said, it must be recognized that while these measures show that housing is affordable for the average homeowner in this province, it is not affordable for all. To the extent that we want to identify who these households are and what the origins and nature of their affordability concerns are in an effort to help them, we need better data.

More specifically, and as stated in our previous report on housing affordability (*In the Eye of the Beholder: Evaluating Current Measures of Occupancy Affordability for Tenants*), in order to specifically address the issue of housing affordability for owner-occupiers, homeowner expenditure data for all items (including shelter) would need to be tabulated for specific regions or housing market areas. Within such as tabulation, and with a view to informing the analysis of owner-occupied housing affordability, one would want to know the percentage of, or how many, homeowner households there are in each income quintile (or decile) for each housing cost-to-income quintile (or decile). Data of this nature would address the core of the housing affordability issue, by cutting through averages and medians, by excluding higher-income earning owners who choose to spend more of their income on their home, by focusing the analysis on specific housing markets and, most importantly, by identifying those with affordability concerns.