Advanced Mortgage Investment Corporation's President and CEO was featured in a recent article in the Ottawa Business Journal.

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REAL ESTATE

Homebuyers banking on alternative lenders

Federal government's tougher stress test rules for mortgages implemented in 2018 pushing more and more borrowers away from the Big Six banks and toward private lenders and credit unions, industry experts say

BY DAVID SALI
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Michael Hapke has a perfect vantage point from which to witness a dramatic shift in the way Canadians are borrowing money to buy homes.

A founding partner of Ottawa-based Advanced Mortgage Investment Corp., Hapke has been a private mortgage lender for 15 years. He says tougher stress test rules implemented last year for home buyers who don't need mortgage insurance are pushing more and more Canadians to look to alternative lenders that aren't obliged to follow the Office of the Superintendent of Financial Institutions' tighter lending requirements.

"If you build a wall, you'll figure out how to go over it, under it or around it," Hapke says.

Hapke's company is one of hundreds of private mortgage lenders across Canada that don't take deposits and are not under the purview of the OSFI. Some of them, like his firm, are mortgage investment corporations – or MICs, as they're commonly referred to – that pool money from investors and are sometimes run as publicly traded firms. Other types of "alternative lenders" include credit unions, which are provincially rather than federally regulated, and other private lenders that typically charge much higher rates of interest than traditional banks – some as high as double-digits for second mortgages.

Hapke says there's no question the new stress test rules enacted in January 2018 have led to a spike in business for alternative lenders.

"The majority of MICs would tell you, we're busier than we've ever been," he says. "I could be busier than I've ever been, but just because we see (new business) doesn't mean I want to do it. We are very selective. But there's definitely more business going to alternative or private sources than in the past."

Recent statistics on the number of Canadians borrowing from alternative lenders prove him right.

According to the Bank of Canada, alternative lenders have seen their share of the mortgage market double since 2015, with institutions outside the "Big Six" banks now holding about eight per cent of all Canadian mortgages.

The new OFSI guidelines, known as B20, were designed to reduce the number of riskier mortgage loans as home prices skyrocketed in markets such as Toronto and Vancouver and households began racking up more and more debt in order to get into the market.

In order to obtain a loan from a federally regulated lender, homebuyers now must prove they can service their uninsured mortgage at a qualifying rate of the greater of the contractual mortgage rate plus two percentage points or the five-year benchmark rate published by the Bank of Canada. An existing stress test already requires those with insured mortgages to qualify at the Bank of Canada benchmark five-year mortgage rate.

With rejection rates from traditional lenders rising, Hapke says an increasing number of clients who would have qualified for bank mortgages in the past are now turning to firms like his.

"We turn down more, but all of the good stuff that all of the rule changes have left behind is where we really step in and earn our keep, so to speak," he explains. "These mortgage rule changes have made it more difficult, and what we're seeing on the private lending side is the quality of business that is coming over to us is second to none. It's fantastic."

> **"These mortgage rule changes have made it more difficult (for potential buyers), and what we're seeing on the private lending side is the quality of business that is coming over to us is second to none.**
>
> – Michael Hapke, founding partner of Ottawa's Advanced Mortgage Investment Corp.

For example, Hapke says many of his clients are people who've split from their spouses but still don't have a formal separation agreement in place.

"If there's not a separation agreement, (the banks) are not touching it. I'll still do that deal," he says. "I don't need a separation agreement to see that the person's got a perfectly good repayment history, the person can afford the payments and there's good equity in the property. That's a deal I'm happy to do."

Self-employed business owners are also finding it tougher to qualify for mortgages under the new rules because the big banks tend to scrutinize the numbers on their T4 slips without taking into account the equity in their companies, says Ottawa mortgage broker Steve Cochrane.

"There are two sides of the coin: You can either claim more income, pay more tax and get a lower (mortgage) interest rate or claim less income, pay less tax and have a higher interest rate (through a private lender)," he says.

"It pretty much always comes out in the wash anyway."

Hapke also says he's seeing more customers who are partnering with friends or getting help with a downpayment from the "bank of Mom and Dad" in order to jump into the market.

Ottawa mortgage broker Chris Allard says he's noticed a similar trend, with a "significant" uptick in the number of files crossing his desk from people who've been gifted funds for a down payment as well as applications co-signed by a friend or relative.

"If there's an option at all for parents or family members to gift funds or to co-sign, they will take that option before choosing to pay a higher mortgage interest rate," he says.

'COMPLETE OVERKILL'

The new rules have effectively cost potential homebuyers 20 per cent of their borrowing power, Allard says, estimating that that many buyers who would have qualified for a $400,000 mortgage two years ago might only qualify for a $320,000 loan today.

"That is a pretty significant difference for a lot of people," he says. "That is why you're seeing so many gifted down payments or co-signers or alternative mortgages."

Hapke and many local brokers say they're no fans of the stricter stress test, arguing measures originally designed to cool overheated markets in two particular cities – Toronto and Vancouver – have wound up hurting homebuyers from coast to coast.

"Instead of just punishing the two bad kids in the class, they're holding everybody back from recess," Hapke says, a sentiment echoed by Cochrane.

"It's complete overkill, certainly for Ottawa," he says. "Now a place like Calgary is struggling. The markets that were already having a hard time are having a really hard time now."

Still, broker Dan Faubert says potential homebuyers shouldn't be scared off by the prospect of turning to alternative lenders if they can't qualify for a mortgage from a traditional bank. For people with good credit and a steady income, MICs, credit unions and other private lending institutions are often a viable option.

"Just because your bank says no, doesn't mean you can't borrow money today," Faubert says.

Allard says many alternative lenders today offer rates only "marginally higher" than the big banks, but if a half-point difference is a red flag, then he suggests potential buyers think long and hard about whether jumping into the market is a prudent move.

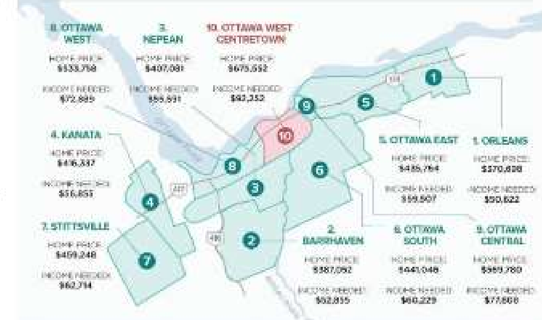
"If that is the dealbreaker of buying a home or not, sometimes we have to ask ourselves, 'Is buying a home (the) right (decision) at this time if $100 is going to be the difference between me being comfortable with the payments or not?'"

Cochrane, too, says it's important for those considering the alternative lending market to do their homework.

"Work with somebody who's honest and transparent and will provide you with options," he counsels. "The landscape is constantly changing. Every day there's something new."

Income Required to Afford a Home in Each Ottawa Neighbourhood

Based on 2018 sold home prices from the Ottawa Real Estate Board, and assuming a 20% down payment and a mortgage rate of 3.35%, Zoocasa calculated the minimum household income required to buy an average home. Here are the most and least affordable Ottawa neighbourhoods.



OTTAWA NEIGHBOURHOODS RANKED (MOST TO LEAST AFFORDABLE)	AVERAGE HOME PRICE 2018	INCOME REQUIRED TO AFFORD AVERAGE HOME	MEDIAN HOUSEHOLD INCOME BEFORE TAX	DIFFERENCE BETWEEN ACTUAL AND REQUIRED INCOME
1. ORLEANS	$370,698	$50,622	$85,981	+$35,359
2. BARRHAVEN	$387,092	$52,855	$85,981	+$33,126
3. NEPEAN	$407,081	$55,591	$85,981	+$30,390
4. KANATA	$416,337	$56,855	$85,981	+$29,126
5. OTTAWA EAST	$435,764	$59,507	$85,981	+$26,474
6. OTTAWA SOUTH	$441,046	$60,229	$85,981	+$25,752
7. STITTSVILLE	$459,248	$62,714	$85,981	+$23,267
8. OTTAWA WEST	$533,758	$72,889	$85,981	+$13,092
9. OTTAWA CENTRAL	$569,780	$77,808	$85,981	+$8,173
10. OTTAWA WEST CENTRETOWN	$675,552	$92,252	$85,981	-$6,271

Methodology

Zoocasa.com is a real estate website and brokerage that provides advanced online search tools and data to empower Canadians to buy or sell their homes faster, easier and more successfully. Home buyers can browse real estate listings on the website or the free iOS app.

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