

Bank of Canada
Monetary Policy Framework Renewal
Conference Discussion
– Housing

Amy Hongfei Sun
Queen's University

October 16, 2025

Summary

- ▶ As part of the policy framework renewal, the Bank conducted a comprehensive and thorough study on monetary policy and housing in the Canadian context, supported by staff's original work with empirical and quantitative analyses.
- ▶ Addressing the new issues around housing that emerged in the high inflation episode since the pandemic
- ▶ This discussion: summary + comments (areas to dig deeper)

Key Questions Visited

- ▶ Which measures of prices for housing services should be included in the Bank of Canada's inflation target?
 - ▶ Rising MIC creates a communication challenge for the Bank.
- ▶ How does monetary policy affect housing market imbalances?
 - ▶ Gap between housing demand and supply has increased dramatically. Higher house price growth \Rightarrow high rent inflation.
- ▶ What are the implications of housing market dynamics on the conduct of monetary policy?
 - ▶ How and whether monetary policy should respond to housing market dynamics are more important questions now in Canada, given persistent imbalances between housing supply and demand, and persistently elevated shelter inflation.

Comments

- ▶ The Bank staff's work has generated a rich set of insightful findings and policy takeaways.
- ▶ There may be more to explore in terms of how to treat the MIC in capturing shelter inflation in the CPI basket.

Shelter Inflation - MIC

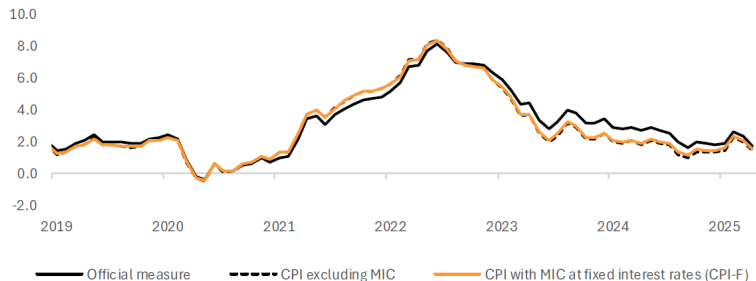
► Citing from the *Housing Overview Note*:

Another option with the ability to help avoid some of the past communications issues with MIC would be to apply a constant interest rate in MIC calculations (Chart 2). This would avoid the perception of “chasing our tail” by targeting our own policy rate. But such a shift could raise communication or trust issues with the public by ‘moving the goal post’ of what the Bank targets. It would also make mortgage costs reflect only volumes, not financing prices—reducing credibility by downplaying the actual pressures households face.

.....

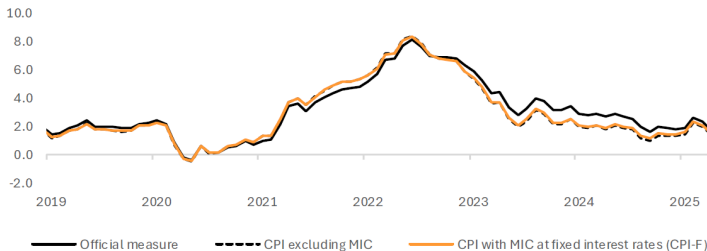
- Asking Statistics Canada to publish a CPI series using a constant interest rate (CPI-F), to help with communications during future episodes when MIC skews the official measure.

Chart 2: MIC kept total CPI inflation elevated for longer
(y/y percentage change, %)



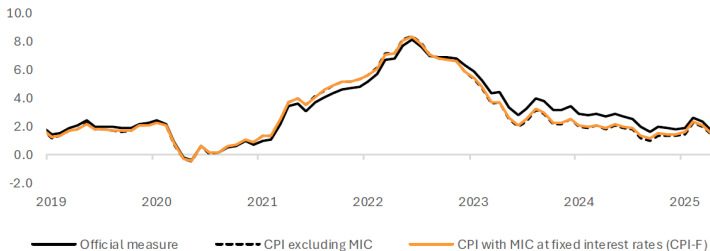
- ▶ The separation of CPI and CPI_F during 2023-2025 ($CPI_F - CPI < 0$) creates communication issues for the Bank.

Chart 2: MIC kept total CPI inflation elevated for longer (y/y percentage change, %)



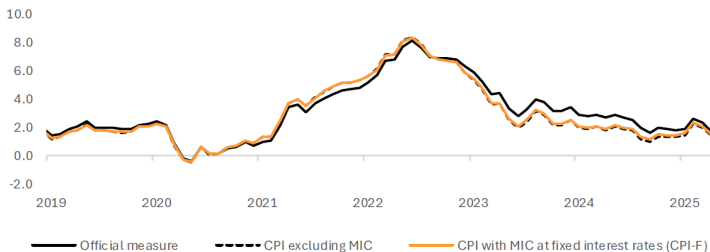
- ▶ Comparing the official CPI and CPI_F can provide important clues about housing and mortgage market dynamics.

Chart 2: MIC kept total CPI inflation elevated for longer (y/y percentage change, %)



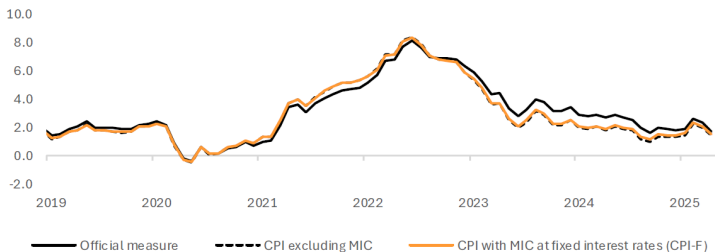
- ▶ The separation of CPI and CPI_F ($CPI_F - CPI > 0$) around 2021-2022 seems to hint at the upcoming separation ($CPI_F - CPI < 0$) during 2023-2025.
- ▶ The separation could be driven by a change in the market composition of mortgage contracts.

Chart 2: MIC kept total CPI inflation elevated for longer
(y/y percentage change, %)



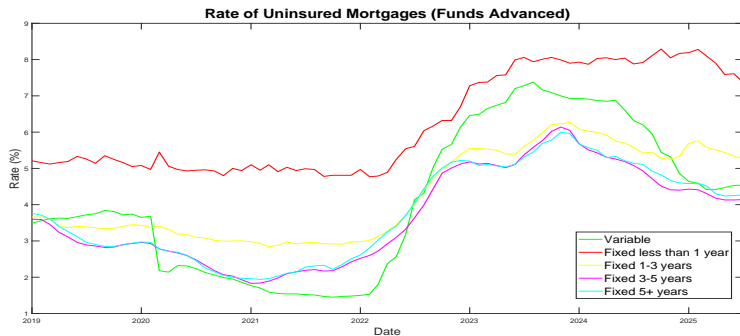
- ▶ Choice between variable-rate and fixed-rate mortgages:
high house price growth + wide rate gap ($r_f - r_v$)
⇒ dramatic rise in the share of variable-rate mortgages

Chart 2: MIC kept total CPI inflation elevated for longer
(y/y percentage change, %)



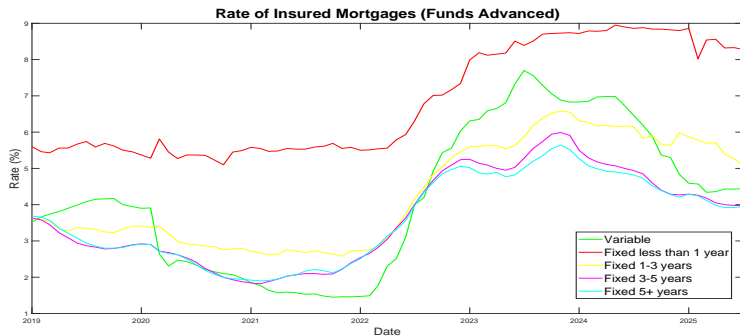
- ▶ Elevated share of variable-rate mortgages drives a wedge between CPI_F and CPI : $CPI_F - CPI > 0$ in a low-rate environment and $CPI_F - CPI < 0$ in a high-rate episode.

Mortgage Rates - Uninsured New Loans



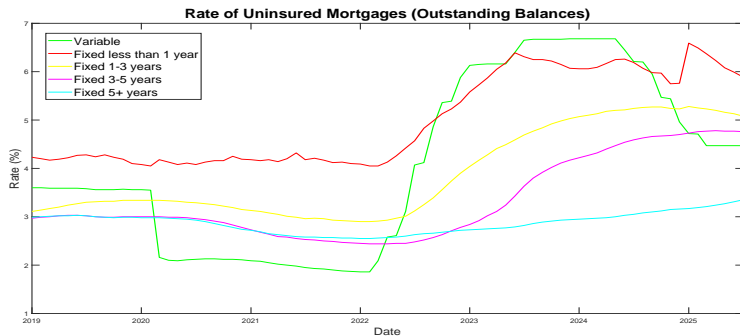
Source: Statistics Canada. Table 10-10-0006-01 Funds advanced, outstanding balances, and interest rates for new and existing lending, Bank of Canada

Mortgage Rates - Insured New Loans



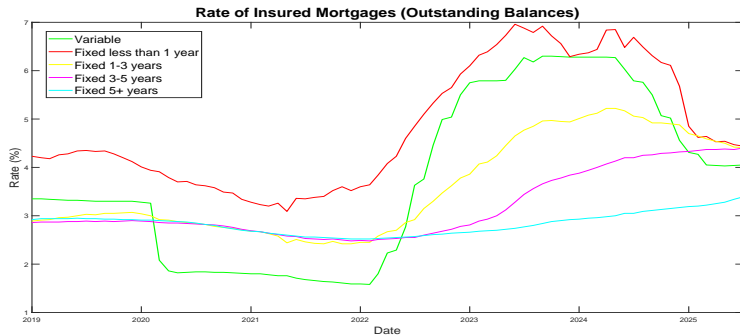
Source: Statistics Canada. Table 10-10-0006-01 Funds advanced, outstanding balances, and interest rates for new and existing lending, Bank of Canada

Mortgage Rates - Uninsured New & Existing Loans



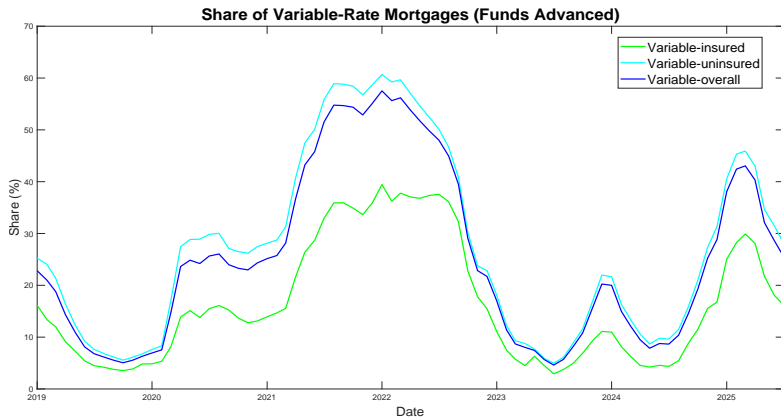
Source: Statistics Canada. Table 10-10-0006-01 Funds advanced, outstanding balances, and interest rates for new and existing lending, Bank of Canada

Mortgage Rates - Insured New & Existing Loans



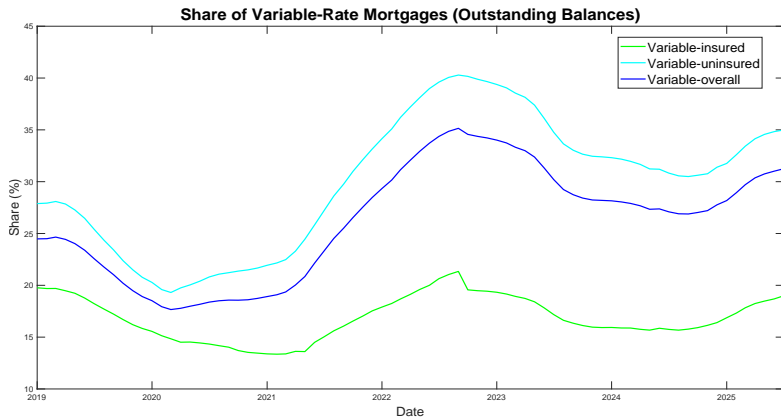
Source: Statistics Canada. Table 10-10-0006-01 Funds advanced, outstanding balances, and interest rates for new and existing lending, Bank of Canada

Share of Variable-Rate Mortgages - New Loans



Source: Statistics Canada. Table 10-10-0006-01 Funds advanced, outstanding balances, and interest rates for new and existing lending, Bank of Canada

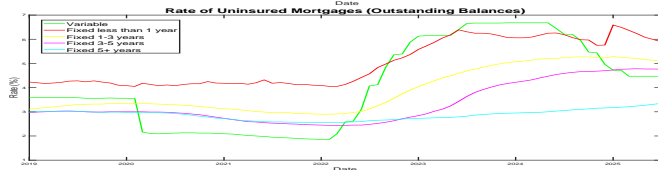
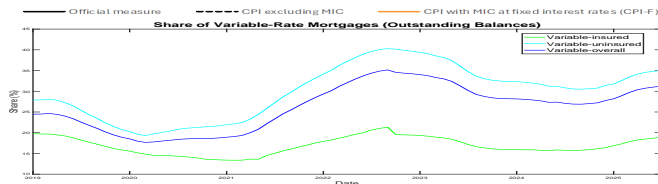
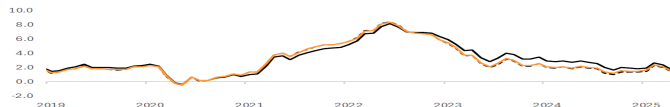
Share of Variable-Rate Mortgages - New & Existing Loans



Source: Statistics Canada. Table 10-10-0006-01 Funds advanced, outstanding balances, and interest rates for new and existing lending, Bank of Canada

Communication to the Public

Chart 2: MIC kept total CPI inflation elevated for longer (y/y percentage change, %)



Housing and Financial Stability Concerns

- ▶ High price growth + low interest rates
⇒ growing share of variable-rate mortgages (and highly-leveraged indebted homeowners)

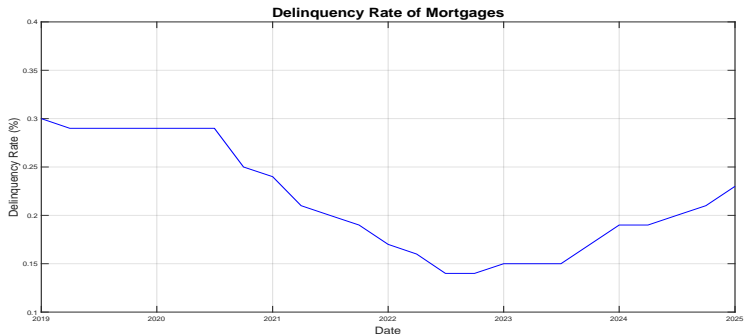
Housing and Financial Stability Concerns

- ▶ High price growth + low interest rates
⇒ growing share of variable-rate mortgages (and highly-leveraged indebted homeowners)
- ▶ Sensitivity to interest rate changes

Housing and Financial Stability Concerns

- ▶ High price growth + low interest rates
⇒ growing share of variable-rate mortgages (and highly-leveraged indebted homeowners)
- ▶ Sensitivity to interest rate changes
- ▶ A turn to the higher-rate episode accumulates risk of mortgage default.

Mortgage Delinquency Rate



Source: Canada Mortgage and Housing Corporation

- ▶ What does "the amount of mortgage default" look like?

Implications for Monetary Policy?

- ▶ Sustained separation of CPI_F and CPI is an alarming signal that calls for policy to address sharply rising variable-rate share

Implications for Monetary Policy?

- ▶ Sustained separation of CPI_F and CPI is an alarming signal that calls for policy to address sharply rising variable-rate share
- ▶ Incorporate mortgage variety, endogenous contract choices, and mortgage default into structural models (e.g., NK-EE)

Implications for Monetary Policy?

- ▶ Sustained separation of CPI_F and CPI is an alarming signal that calls for policy to address sharply rising variable-rate share
- ▶ Incorporate mortgage variety, endogenous contract choices, and mortgage default into structural models (e.g., NK-EE)
- ▶ Explore an MIC-gap-augmented Taylor rule :

$$i_t = \pi_t + r_t^* + a_\pi (\pi_t - \pi_t^* + a_m (\pi_{f,t} - \pi_t)) + a_y (y_t - y_t^*)$$

Implications for Monetary Policy?

- ▶ Sustained separation of CPI_F and CPI is an alarming signal that calls for policy to address sharply rising variable-rate share
- ▶ Incorporate mortgage variety, endogenous contract choices, and mortgage default into structural models (e.g., NK-EE)
- ▶ Explore an MIC-gap-augmented Taylor rule :

$$i_t = \pi_t + r_t^* + a_\pi (\pi_t - \pi_t^* + a_m (\pi_{f,t} - \pi_t)) + a_y (y_t - y_t^*)$$

- ▶ By varying a_m , evaluate its performance on mitigating a positive separation and preventing a sustained negative separation.

Takeaways

1. Use the separation of CPI and CPI_F and the movements in the variable-rate mortgage share to help with communication to the public
2. Explore policy measures to mitigate a *positive* separation so as to prevent a sustained *negative* separation, which is likely to be associated with a higher risk of mortgage default