

Bank of Canada chops rate, but fixed mortgages don't budge

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Many Canadians may have been hoping that Tuesday's big cut in the Bank of Canada's key lending rate would lead to lower fixed mortgage rates, but it hasn't.

The central bank chopped its overnight lending rate by half a percentage point to 3.5 per cent. Financial institutions then matched that cut by lowering their prime lending rates by a half percentage point to 5.25 per cent.

That automatically pushed down the rates for variable mortgages, lines of credit, and other floating-rate loans that are tied to the prime. But not the rates for fixed mortgages — the most common kind of mortgage.

A day after the big Bank of Canada move, fixed mortgage rates remain just where they were before the central bank acted.

In fact, since early December last year, the central bank has chopped its key lending rate by a full percentage point and it has signalled that further rate cuts are "likely."

Yet the posted rate for the popular five-year fixed mortgage has dipped by less than two-tenths of a percentage point in the same time frame.

Analysts point out that the central bank's overnight lending rate is, as the name suggests, a very short-term lending benchmark. Long-term fixed mortgage rates tend to be more influenced by moves in the bond market, which has become a more difficult borrowing environment lately.

Analysts say the global credit crunch — triggered by the U.S. subprime mortgage crisis — has made it more expensive for Canadian banks to access funds.

Spreads increasing

"What essentially is happening is the banks are increasing the spread between what they charge you for a mortgage and what they may pay for money," said Tsur Somerville of the Sauder School of Business in Vancouver.

"They're essentially compensating themselves for higher risk in real estate," he told CBC News.

That one-percentage-point discount on the posted rate that mortgage borrowers were automatically offered is also becoming more difficult to get.

"All the different ways that you used to be able to get a discount — those seem to be drying up," Somerville said. "So when I talk to people, what they're saying is those discounts are hard to get right now."

The tighter lending environment is also being felt in the U.S. mortgage market.

A study released Wednesday by TD Economics showed that American homeowners were not getting much of a break from the big slashing in the federal funds rate by the U.S. Federal Reserve.

The Fed has chopped its key lending rate by 2.25 percentage points in the past six months, but fixed mortgage rates have hardly moved at all.

The most recent Primary Mortgage Market Survey Report from Freddie Mac — also known as the Federal Home Loan Mortgage Corporation — showed 30-year fixed-rate mortgage rates are virtually unchanged from late August.

Rates on jumbo mortgages — those over \$417,000 US — have fallen by just one-fifth of a percentage point since August, as financial institutions grow more risk averse.

TD economist Beata Caranci said the recently approved \$168 billion US economic stimulus package will give the U.S. economy a lift in the second half of the year.

"However, once this short-lived impact dissipates, the U.S. economy could relapse in early 2009 if American households are unable to derive greater benefits from the longer-term influence of past Fed rate cuts," she said.