The Turner Report

When you knock on as many doors as I am these days, you sure get an earful from people about what's on their minds. It's 100% mortgage rates 100% of the time.

Seems homeowners have become quite rattled at the fact the Bank of Canada has upped its key lending rate twice in the last nine weeks, boosting the prime rate by a half point, and adding as much to the cost of variable rate mortgages, home equity loans and lines of credit. Since almost half of us are now opting for these VRMs, every time the cost of money goes up, so does your mortgage payment. So the question on all lips is simple: Should I lock in now? That answer in a moment.

First, why are rates rising? Good question. The big answer is that the central bank sees inflationary trends in the economy, and it is using interest rates to try and cool them off. Rising energy costs are inflationary. Rising government sending is inflationary. Rising levels of consumer debt is inflationary. So, by raising the cost of borrowing, the central bank is attempting to dampen the urge to gorge out on cheap money.

Secondly, rates have been artificially low ever since the American central bank (the Fed, as it is known) crashed them following 9/11 to ward off a post-terrorist attack recession. As a result, we found ourselves with 4% mortgages - the cheapest money in 40 years. That played a big role in fuelling the five-year-long real estate boom now hitting the top of its cycle, and contributed to creating the biggest pile of mortgage debt in Canadian history.

So, how long will rates rise, and how high will they go? This answer is more difficult, since the Bank of Canada would like to keep hiking rates as long as it can - until the economy falters as a result, or until higher rates push the value of the dollar too high. A soaring loonie, of course, makes our exports more expensive, which costs us in both lost sales and lost manufacturing jobs.

The safe bet is that the cost of money will continue to edge higher for about a year, which will mean four to six more increases of a quarter point each. This, by the way, is far less drastic a move than in the States, where the Fed has hiked interest rates a dozen times over the past two years. So, our prime rate of 4.75% today could be at around 6% by Christmas of next year.

This may not sound like a lot, but if you took out a below-prime, variable rate mortgage a few months ago at 4%, when the prime was 4.25%, then seeing it hike to 5.75% means you'll be paying more every month. On a $300,000 mortgage, that actually translates into $3,564 more a year - no small amount of extra after-tax income.

Compounding the anxiety for homeowners is the rising cost of everything - gasoline, home heating oil, electricity, property taxes and natural gas. Together, it's all taking a toll, especially on people who bought new houses in the last year or two with relatively small downpayments and honking big mortgages. There are, believe it, a lot of those people in Halton these days, where new subdivisions have been rising out of farmers' fields faster than crops ever did.

Okay - back to the first question - does all this mean it is now time to lock in that variable rate mortgage, and convert it to a loan with a rate that's fixed for the next three or five years? Nope, it does not.

Rates will continue to rise, yes, but at relatively slow pace. Converting to a fixed rate now will increase your borrowing cost more, and sooner, than necessary. Better that you stick with the VRM for at least six months because your payments will be lower, saving you some much-needed winter cash to pay for all those rising, evil utility bills. Come the crocuses, then it will be time to seriously consider getting fixed. Well, you know what I mean.

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