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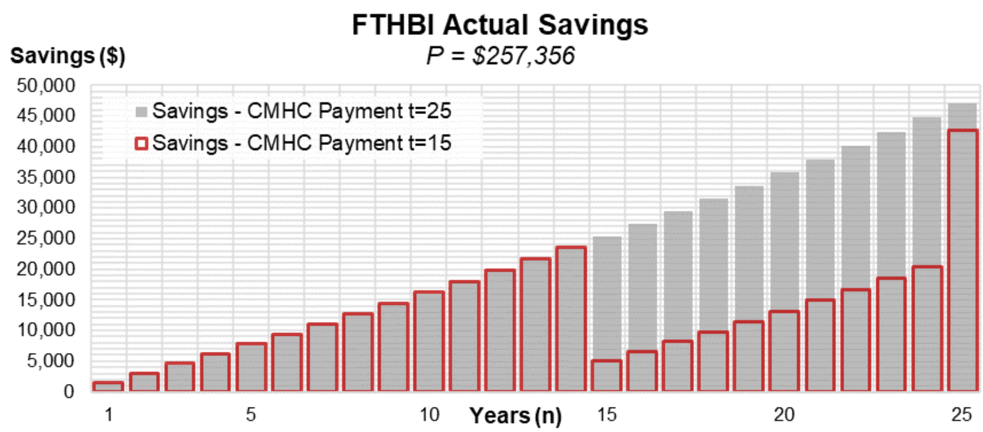
Subject: FTHBI: Liberal on promises, not details

Comments: By now, most of our audience has likely heard of the proposed First-Time Home Buyers Incentive (FTHBI); the government's Shared Equity Mortgage (SEM) program aimed at reducing mortgage payments for first-time home buyers by adding to their down payment. In principle, SEMs allow investors to help finance a home purchase for rights in the asset's future value. Although the receiving party pays no interest, they share a percentage of the home's appreciation at the time of sale/repayment, plus return the initial investment.

Critics of the budget measure were quick to point out the program's $505,000 purchase price cap (based on a 5 percent down payment) is a snub to pricier markets. However, with an estimated Atlantic Canada CMA house value of $257,356*, many Atlantic households could be eligible. At that price, the government's equity stake could reduce mortgage interest by upwards of $121/month, or $47,160 over 25 years** – but the Canadian Housing & Mortgage Corporation (CMHC) will want its money back, eventually. The only way to maximize the savings is to sell your home before or when repayment is due. To illustrate, the below graphic demonstrates that a household repaying CMHC earlier (e.g. year 15) will have lower total savings/return than if repaid at the year of sale (e.g. year 25).



Generally, owners would have to independently save on average 11 percent more if they repaid CMHC prior to a home sale to achieve the same total savings; or, they would have to accept the equivalent percent loss in total future savings.

It is difficult to predict how popular the FTHBI will be. As they say: "the devil is in the details," but the detail will not come until early fall. If it is truly an SEM – meaning CMHC will take an appreciation cut – participation may be slight. If it is comparable to an interest-free loan, there could be better uptake. Based on the median Canadian home value, the three-year, $1.25 billion program budget translates into a capacity to aid up to 20,500 households annually. At the end of the day, each eligible household should be able to save more thanks to the program; however, there are greater benefits for starter homes (i.e. shorter tenure) that take complete advantage of compound interest. Although the program has potential, optimism should be paired with caution before we receive the government's fall update.

* based on Halifax, Moncton, Charlottetown, and St. John's prices

** assumes monthly savings deposits of $121 compounded at a 2 percent annual growth rate (matching target inflation); mortgage payments assume 25-year amortization, 3.5 percent rate, 5 percent down payment, and includes CMHC mortgage insurance.