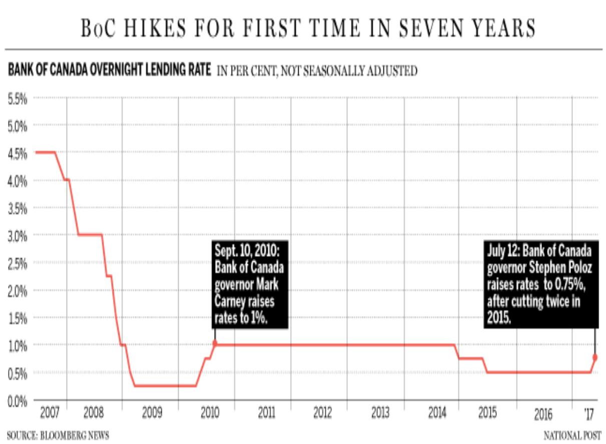
Consumers feel pinch as banks pass on full BoC hike, but not all the cuts

By Garry Marr
July 13, 2017 – *Financial Post*

The country's major banks are passing on the full weight of a 0.25-per-cent increase from the Bank of Canada, despite the fact that, on the way down, consumers only received a portion of the central bank's discounts.

Vince Gaetano, a principal at mortgage broker monstermortgage.ca, questioned whether Canada's major banks were gouging consumers with the move, which affects about a quarter of Canadians with a mortgage tied to prime.

"It's quite simply greed," said Gaetano. "There is always a focus on profits and getting more money out of the pockets of Canadians. The last Bank of Canada decrease of 0.25 per cent only garnered a benefit of 0.15 per cent to Canadian borrowers. This happened the last two rate decreases."



Royal Bank of Canada was the first out of the gate with an increase, raising its prime lending rate from 2.7 per cent to 2.95 per cent. The other major banks followed with increases throughout the day.

"After careful consideration of a range of factors, we are increasing our prime lending rate in line with the Bank of Canada overnight rate by 25 basis points to 2.95 per cent, effective July 13," RBC said in an email to the Financial Post. "The Bank of Canada Rate is one reference point that we use to set our prime rate and is not the sole driver of the bank's funding costs. In a persistently low rate environment, funding costs have steadily increased over the past few years."

Traditionally, the prime lending rate at most major banks has tracked the Bank of Canada's overnight lending, but there have been points where it has diverged. In 2015, over the course of two rate cuts, the major banks decided not to match the full cut twice — the 0.2-per-cent spread has not been recovered since.

Back in 2008, when the late Jim Flaherty was finance minister, the Bank of Canada cut the prime lending rate by 50 basis points, only to see the banks agree to pass on half the rate cut. After Ottawa agreed to provide more liquidity in the mortgage sector, the major banks agreed to further cuts to their prime rate.

Finance Minister Bill Morneau wasn't stepping in to the debate Wednesday. "As Minister of Finance, I do not comment on the Bank's independent decision," he said, in an emailed statement.

The move by the banks hit consumers with mortgages tied to prime, starting Thursday. On a $400,000 mortgage with a 25-year amortization, monthly interest costs just rose $50 based on the 25-point increase, said James Laird, co-founder of ratehub.ca.

"I don't know if I know the truth," said Laird, about whether banks needed to pass on the full increase based on funding costs.

"I'm not surprised. Was I surprised when some of the savings were not entirely passed along (in 2015)? I wasn't. If you asked me yesterday if the (central) bank moved up 25 basis points, would the banks follow suit, and I would say absolutely. They focus on their bottom line and (the) best move for bottom line is for them all to move up in unison by 25 basis points."

He said Toronto-Dominion Bank's response to the rate hike would be interesting. About a year ago, the bank moved prime to 2.85 per cent for variable rates and home equity lines of credit. Other customers were paying 2.7 per cent. Late Wednesday, TD moved its mortgage prime rate to 3.1 per cent.

Variable rate products are subject to a prime rate set by the bank and the vulnerability of consumers to financial institutions raising that rate could influence behaviour, Laird said. "All those people in variable rate mortgages, nothing happened (in terms of a central bank rate move) and TD changed their rates," he said.

In a statement, TD said "adjusting our rates is not a decision we take lightly. We look at a number of factors when determining rates including the competitive landscape, the cost of lending, managing risk and the Bank of Canada's overnight rate."

Laird said it's still clear variable rate products save consumers money compared to a fixed rate about 90 per cent of the time.

Another factor is most Canadian consumers with a variable rate mortgage have negotiated a discount off of prime that is on average close to 60 basis point for a five-year term, according to ratespy.com. Those consumers, while their prime rate might be 2.95 per cent as of Thursday, would still be paying their mortgages based on 2.35 per cent after the discount.