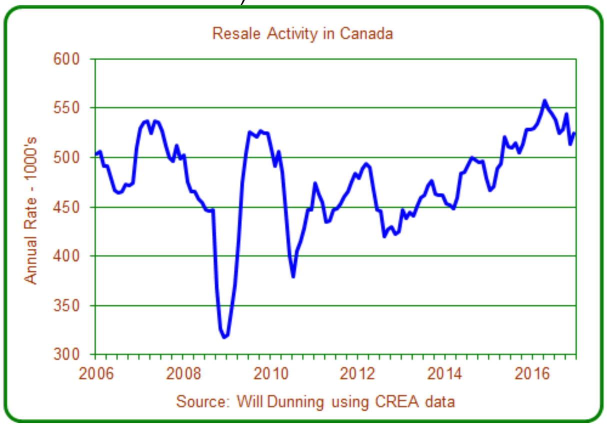
# Housing Market Digest – Canada

January 2017

## *Resale Market*

The Canadian Real Estate Association reported that resale activity was up slightly in December, to an annualized sales rate of 525,100. The rise compared to November was almost entirely in Alberta and Saskatchewan, and reflects improving confidence in the wake of stronger pricing for oil and natural gas. The drop from the peak seen last spring is due to the foreign buyers' tax in BC. (As I commented last month, there is a significant risk that the tax, by damaging expectations about the future housing market, could cause a regional economic recession).



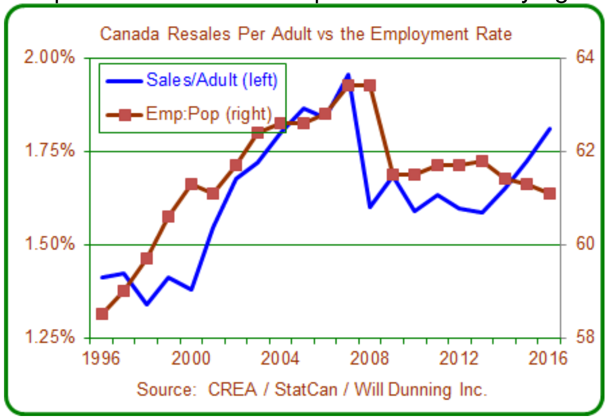

As commented last month, It is much too soon to draw any conclusions about effects from the revised mortgage insurance "stress test":

- Recent increases in mortgage interest rates may be causing a rush into the market, to take advantage of pre-approvals.
- Moreover, pre-approvals dated before the stress test policy took effect are still in play, allowing some buyers to escape the test.
- Weather remains unusually mild in Ontario and Quebec, which may be encouraging buyers and sellers to act sooner than usual.

For the year as a whole, a new record was set, at 536,188 sales. This was 3.6% higher than the prior record (set in 2007).

We should expect sales to rise over time, as the population is growing, as is the inventory of homes on the ground that can potentially be sold. Therefore, another way to look at the sales data is in comparison to the size of the adult population. The next chart does that, using annual data. This approach indicates that sales are still slightly below the pre-recession level.

Furthermore, the chart compares the sales rate to the employment-to-population ratio. There is a reasonably close fit between the two lines, which confirms that the job situation is a strong determinant of resale housing activity. Yet, starting during 2015 and increasingly in 2016, sales were stronger than we might expect on the basis of the employment situation. This reflects the importance of record low interest rates: very good affordability has provided additional impetus to home buying.

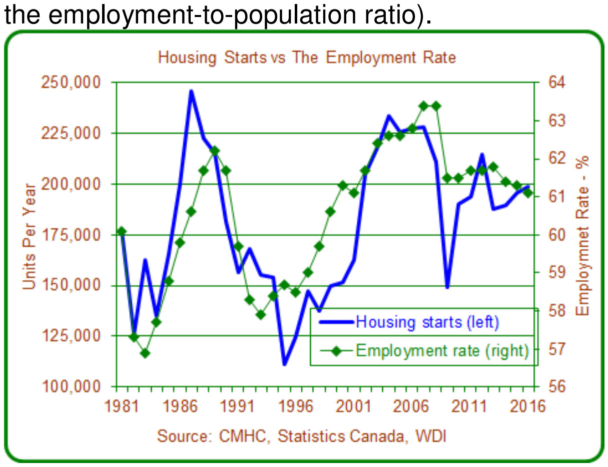



CREA's House Price Index shows a year-over-year increase of 14.2%. The data is showing a turning point (as the YoY increase is down from a peak of 14.7% in August). This can be attributed to the Vancouver situation. Elsewhere price trends are showing little change.

Fewer listings are flowing into the market, and the imbalance between supply and demand has worsened. For the year, the national sales-to-new listings ratio averaged 62.3% (about 10 points above the "balanced market" level).

## *Housing Starts*

Final housing starts data for 2016 haven't yet been released by CMHC, but it appears that the total might be about 3,000 more than the 2015 figure of 195,535. Housing starts continue to map quite well against the employment situation (as measured by the employment-to-population ratio).



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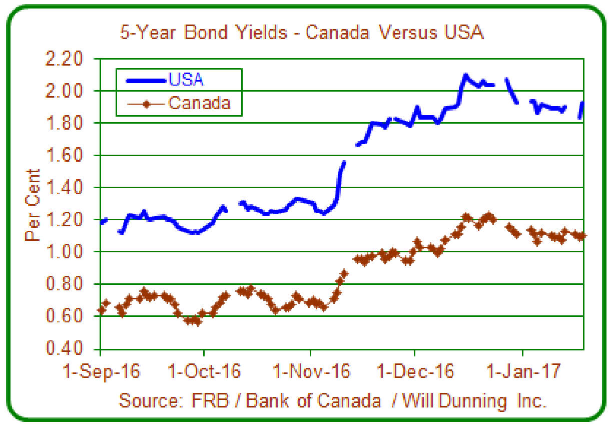
## *Employment Trends*

Data from Statistics Canada's Labour Force Survey indicates that employment rose by 214,100 during 2016. The growth rate of 1.2% was slightly better than the population growth rate of 1.0%, and resulted in a small rise in the employment-to-population ratio. The monthly data suggest that growth was better in the second half of the year (at an annualized rate of 1.9%) than during the first half (0.5%) and leaves an impression that the economy is gaining momentum. But, there is some evidence of distortions in the data, and it is more likely that there was relatively consistent growth during the year. Similarly, the "true" employment rate was probably quite flat during the year.

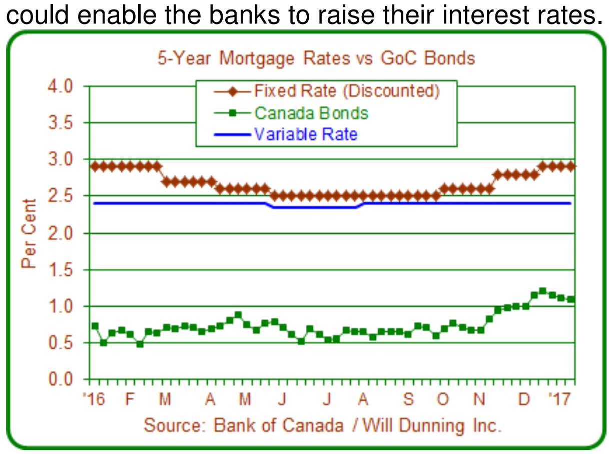
Canada and the US data both saw little change during the year in their employment rates. For the US, this represents deterioration, as it interrupted an improving trend. For Canada, 2016 brought an end to a falling trend. The employment rate in Canada had started to fall at the start of 2013 – I see this as partly due to the mortgage insurance change that took effect in July 2012. So, I wonder if the new mortgage insurance stress test (at the posted five-year rate) will negatively affect our employment situation later this year.


## *Interest Rates*

In the wake of the US presidential election, bond yields rose rapidly in the US (three-quarters of a point for 5-year bonds) and slightly less in Canada (a half point). Yields have subsequently retreated. These recent (and future) moves have more to do with political uncertainty than with economic prospects, which makes the outlook for rates highly uncertain. That said, neither Canada nor the US can tolerate large and sustained rises in interest costs and therefore I would be surprised if, six months from now, bond yields and interest rates in Canada are higher than at present.




Mortgage interest rates partially followed the initial rise in bond yields. Now, with yields down slightly, the spread between the 5-year Canada bond versus my opinion-estimate of a typical 5-year fixed mortgage rate is 1.7 points. This is equal to the average for the past decade. From that perspective, there is at present no need for mortgage interest rates to change. But, regulatory changes could cause the spread to increase. Firstly, the need for lenders to hold more capital reserves would raise their funding costs. Secondly, the regulations are squeezing non-deposit-taking lenders. A reduction in competition could enable the banks to raise their interest rates.




Some of the banks have raised their posted rates (one of them is at 4.84%). But the Bank of Canada has not yet changed its estimate of the typical posted rate, which is still 4.64%.

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*Completed by Will Dunning, Chief Economist, Mortgage Professionals Canada*