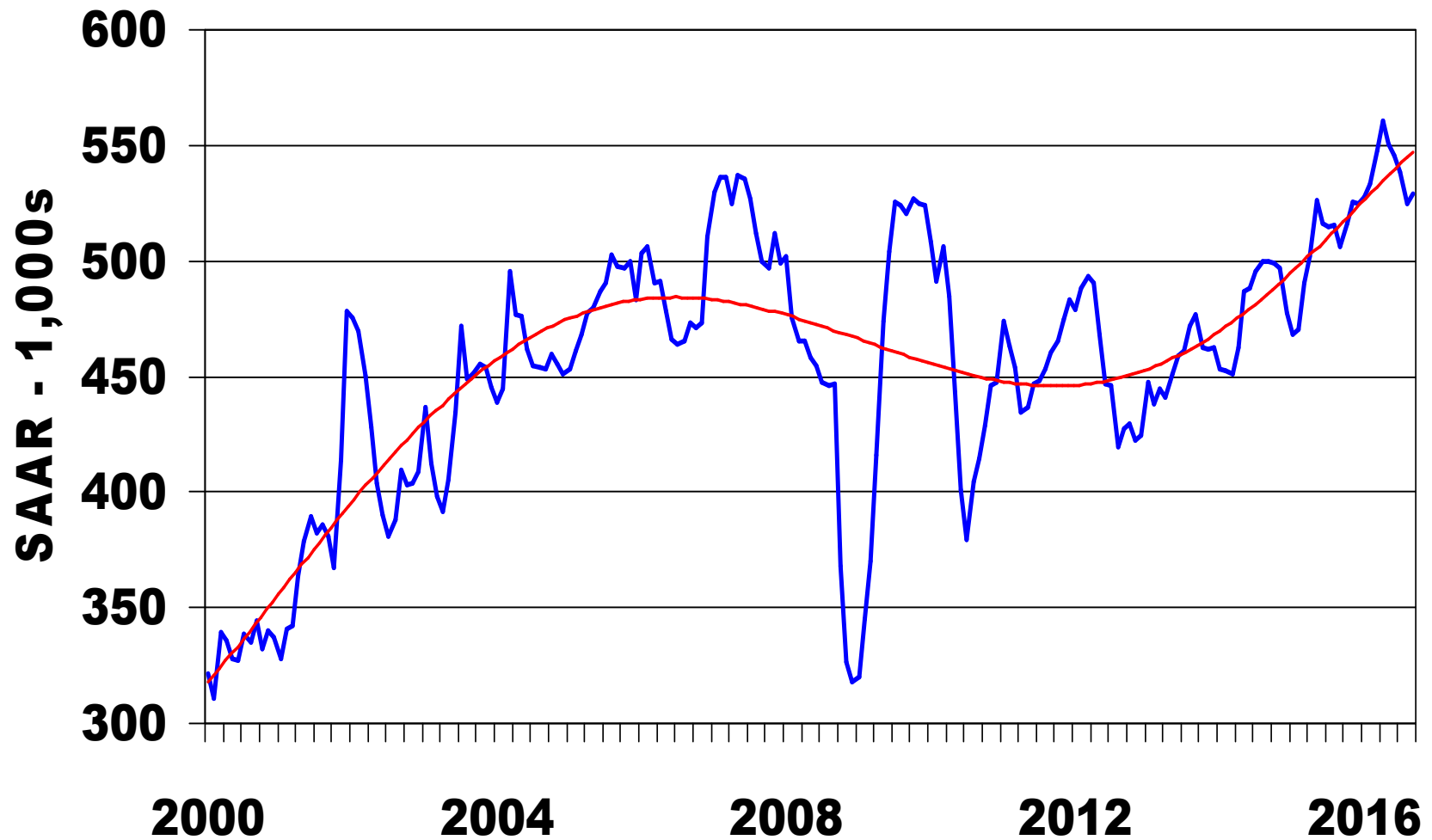


# Housing Market Overview

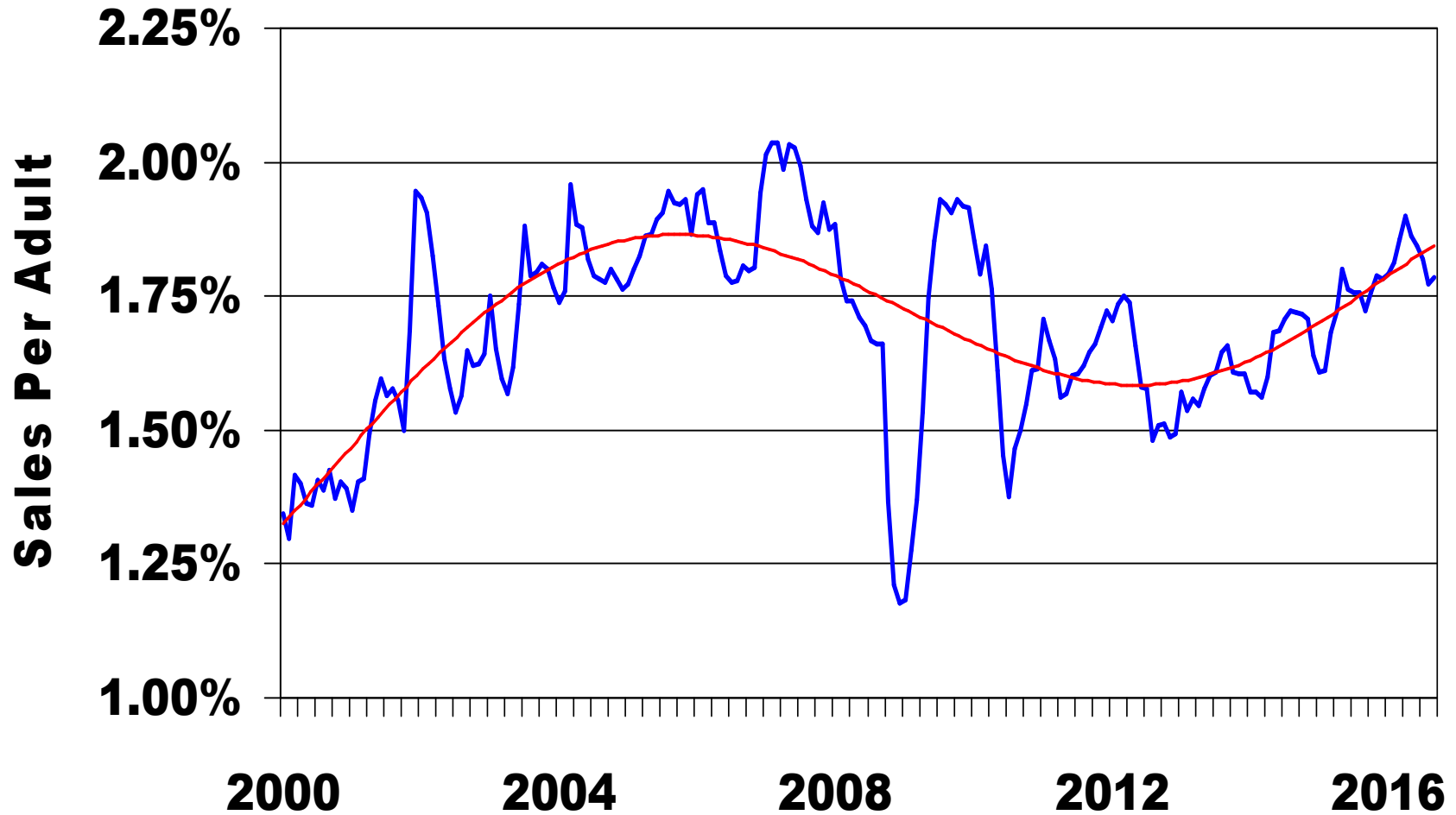
Will Dunning  
November 5, 2016

# Very Strong Resale Activity in Canada



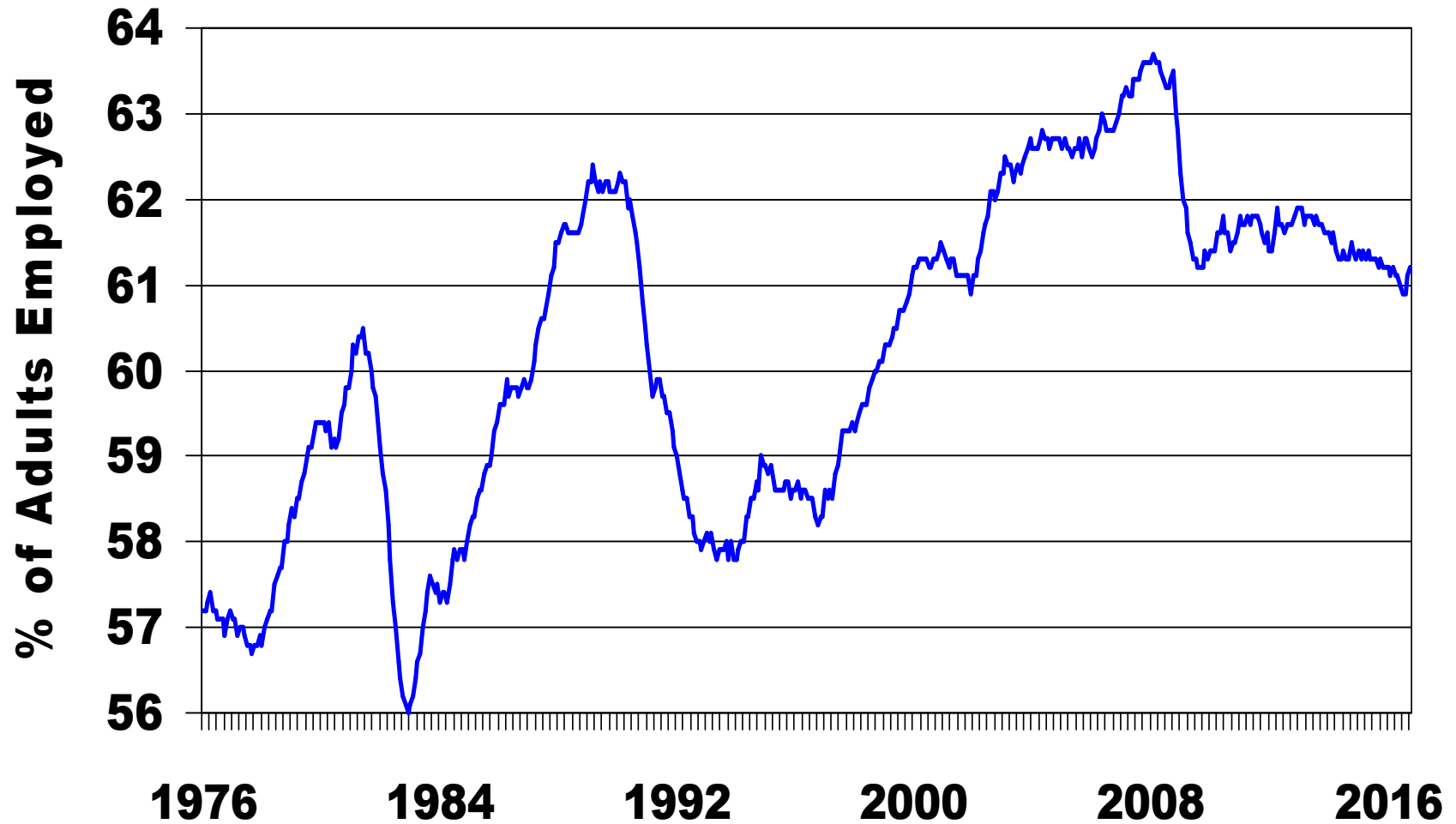
Source: CREA / Will Dunning

# Per Capita Sales: Approach Pre-Recession Level



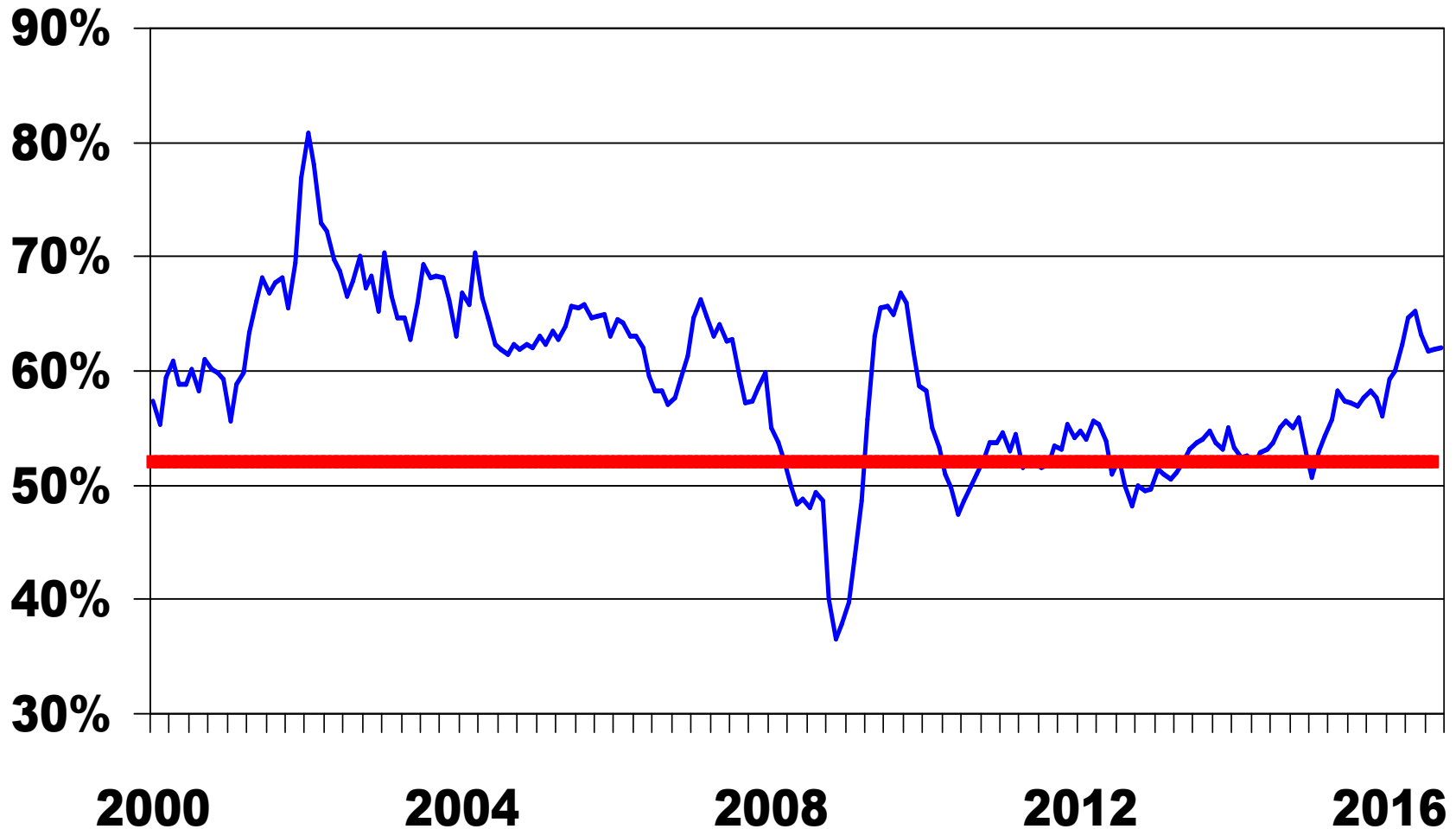
Source: CREA / StatsCan / Will Dunning

# Employment Conditions Moderately Favourable



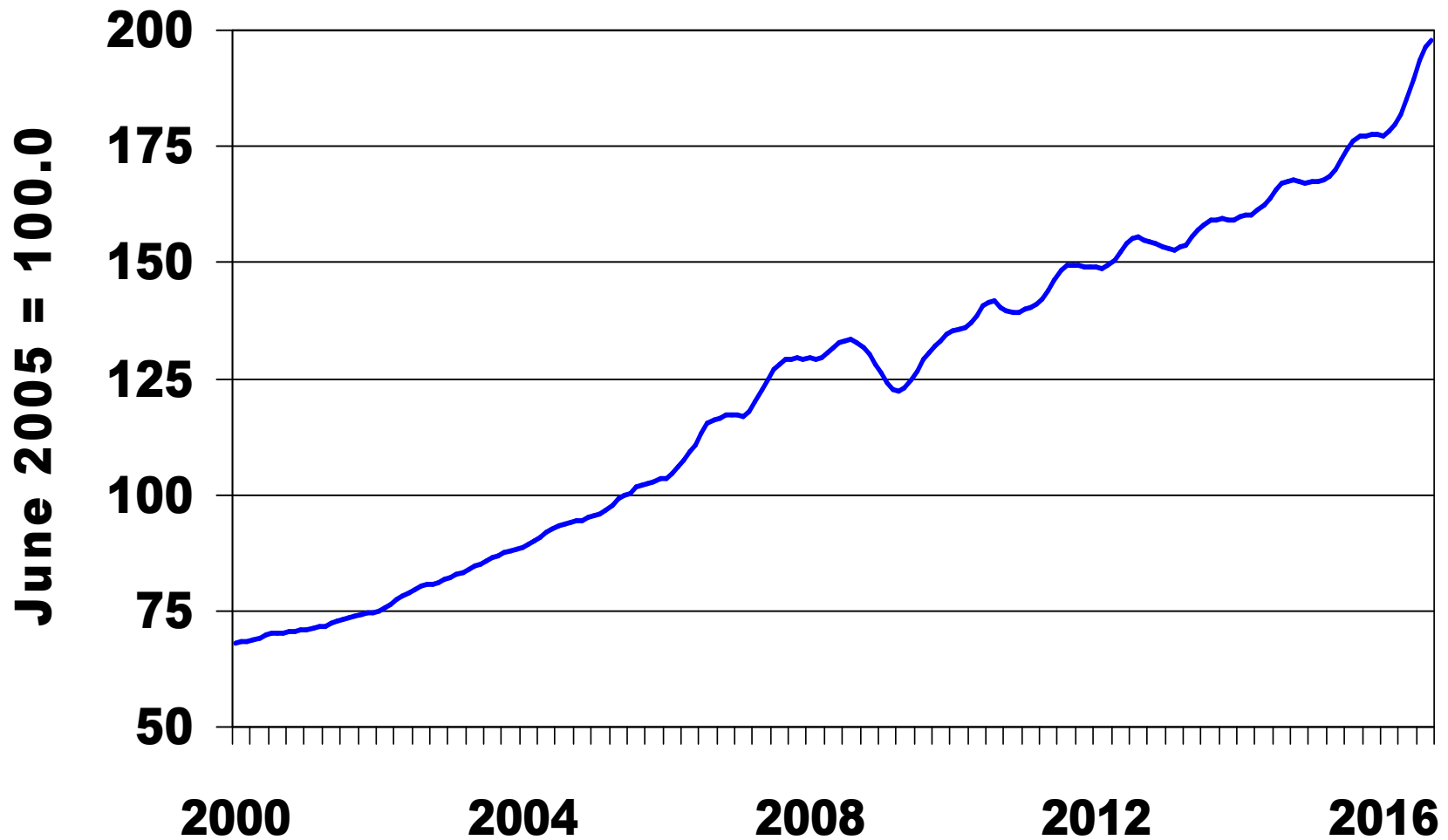
Source: Statistics Canada

# SLR Shows “Sellers’ Market” in Canada



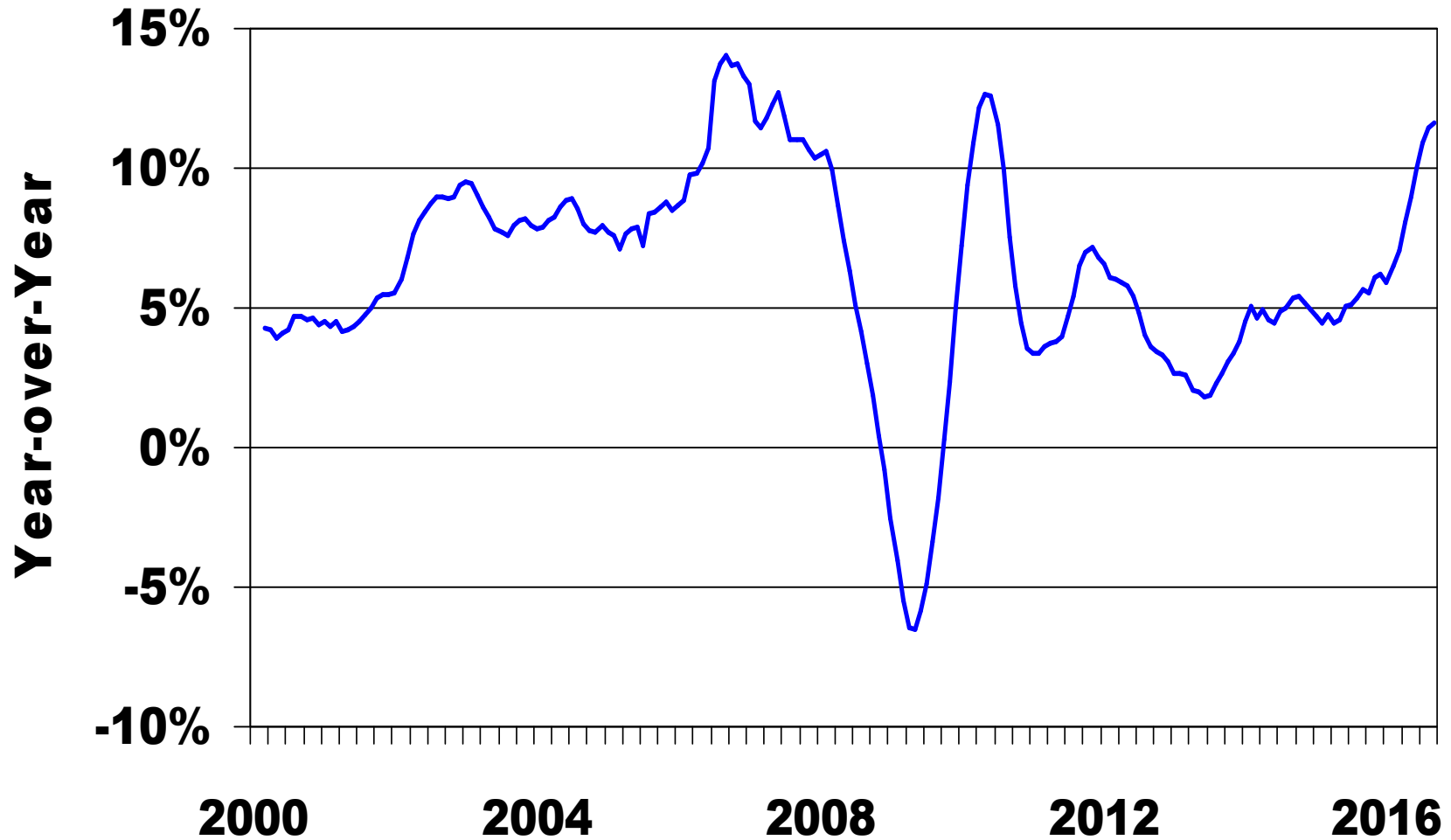
Source: CREA / Will Dunning

# Teranet Index Shows Acceleration



Source: Teranet/National Bank

# Recent Surge in Price Growth



Source: Teranet/National Bank / Will Dunning

# The “B-word” Has Been Used Liberally

- Canada’s housing markets might be the “most overvalued in the world” – OECD, The Economist...
- Conclusions based on incomplete concepts and flawed data
- Low interest rates have generated “affordability space”
- That said, Vancouver and Toronto have started to verge into bubble territory



# What is a Bubble?

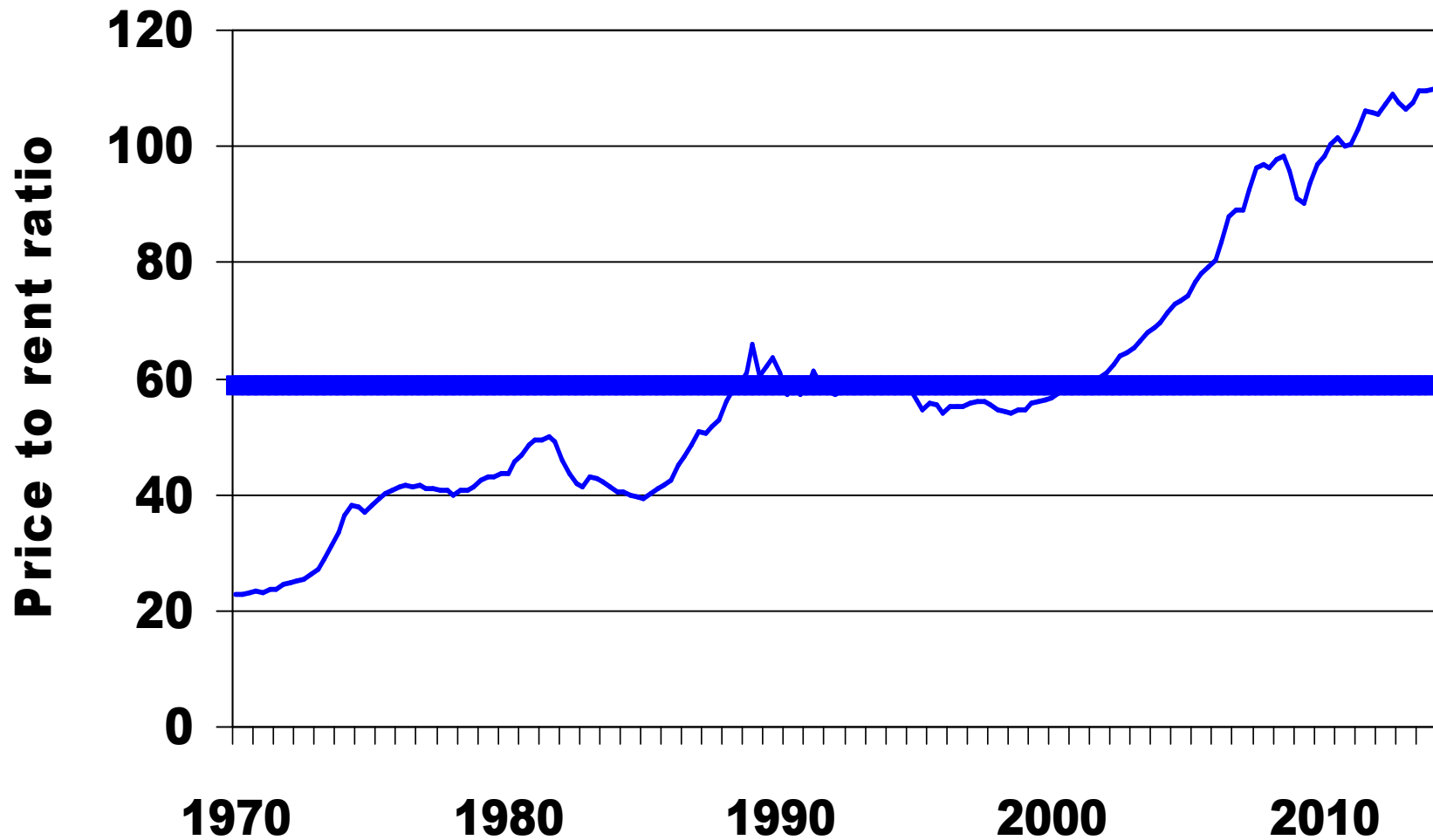
Joseph Stiglitz:

- *If the reason that the price is high today is only because investors believe that the selling price will be high tomorrow - when "fundamental" factors do not seem to justify such a price - then a bubble exists.*

# Analysis Approaches

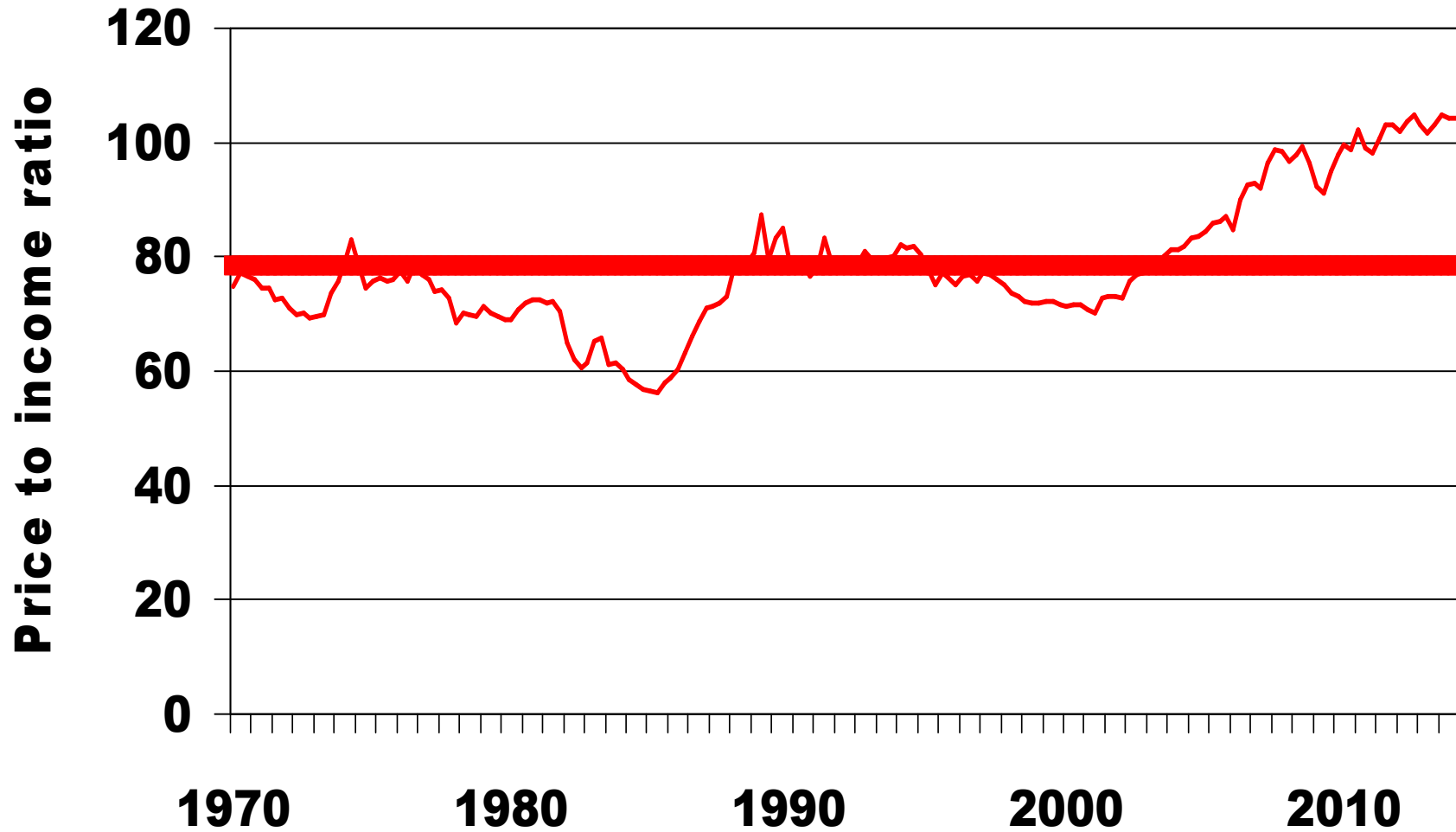
- Standard approach looks at prices versus rents or incomes.
- But, housing is an asset in addition to a consumption good.
- Need to incorporate interest rates:
  - Home ownership as an investment – capitalization rates (“How to Dissect a Housing Bubble”).
  - Similarly, compare costs of home ownership with renting equivalent accommodation.
  - Mortgage cost relative to incomes.

# OECD – 87% Overvaluation Based on Rents



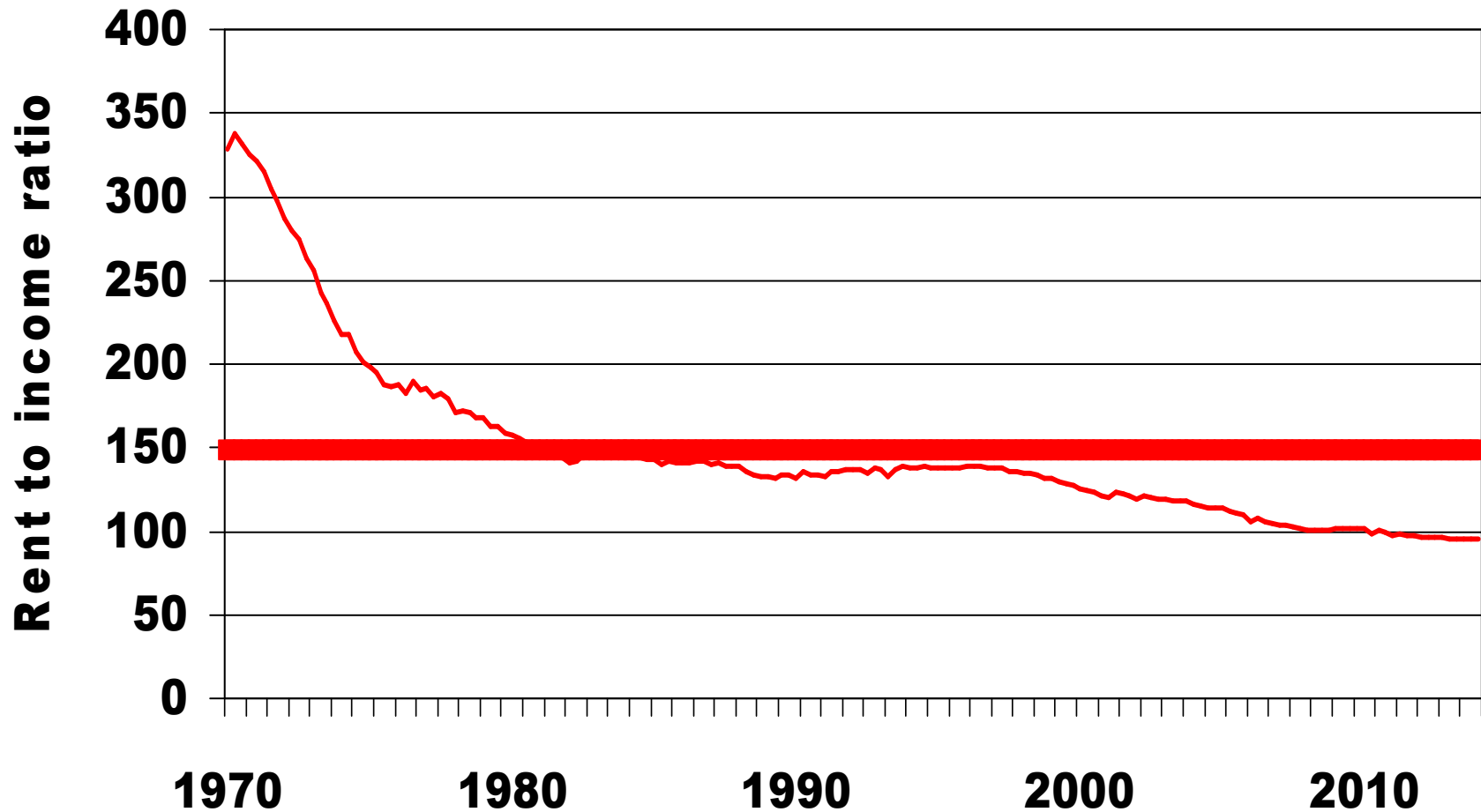
Source: OECD

# OECD – 33% Based on Incomes



Source: OECD

# OECD Implies Rents are 36% Undervalued Based on Incomes



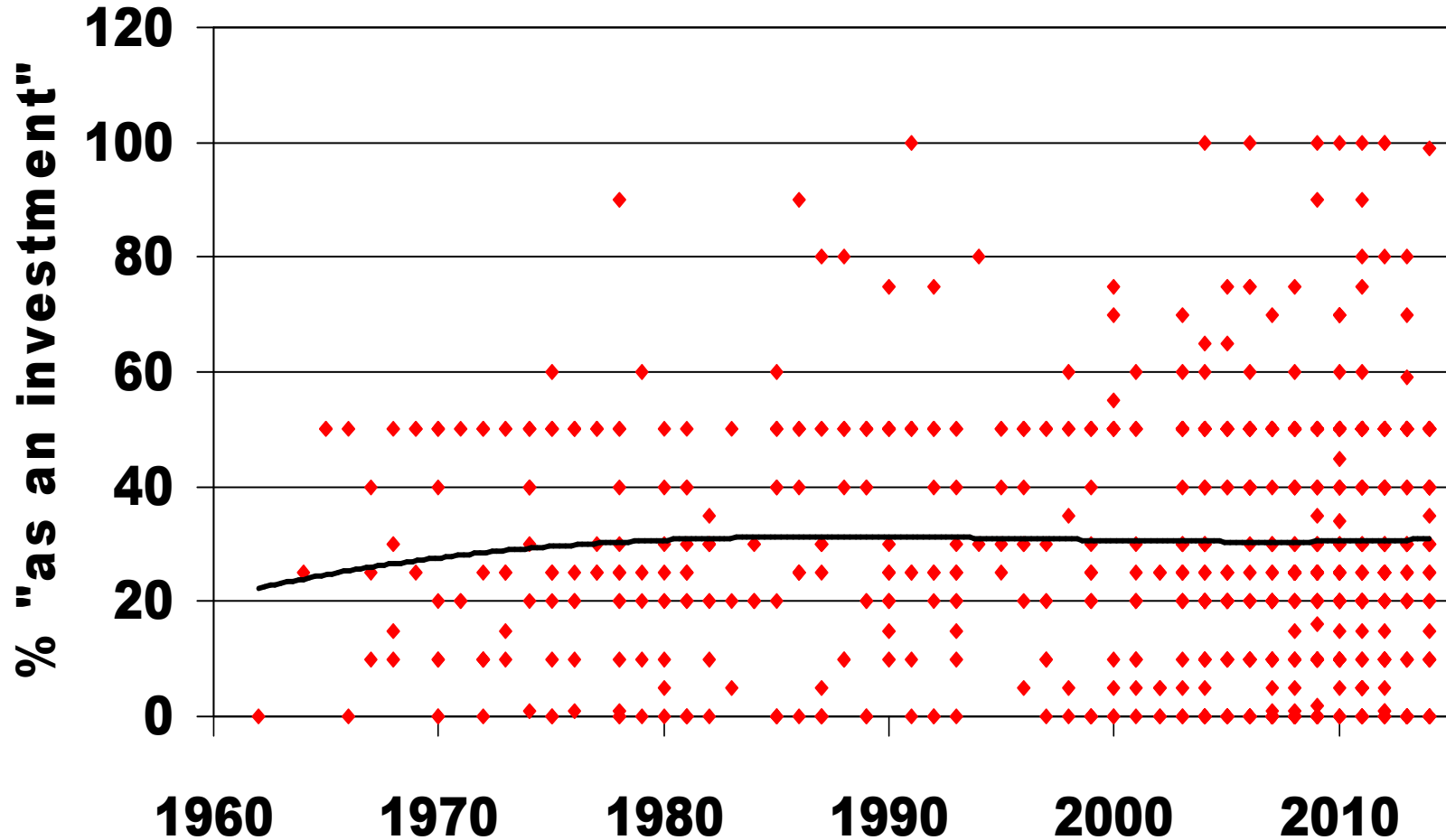
Source: Will Dunning, using OECD data

# Critique of OECD Analysis

“How to Dissect a Housing Bubble”

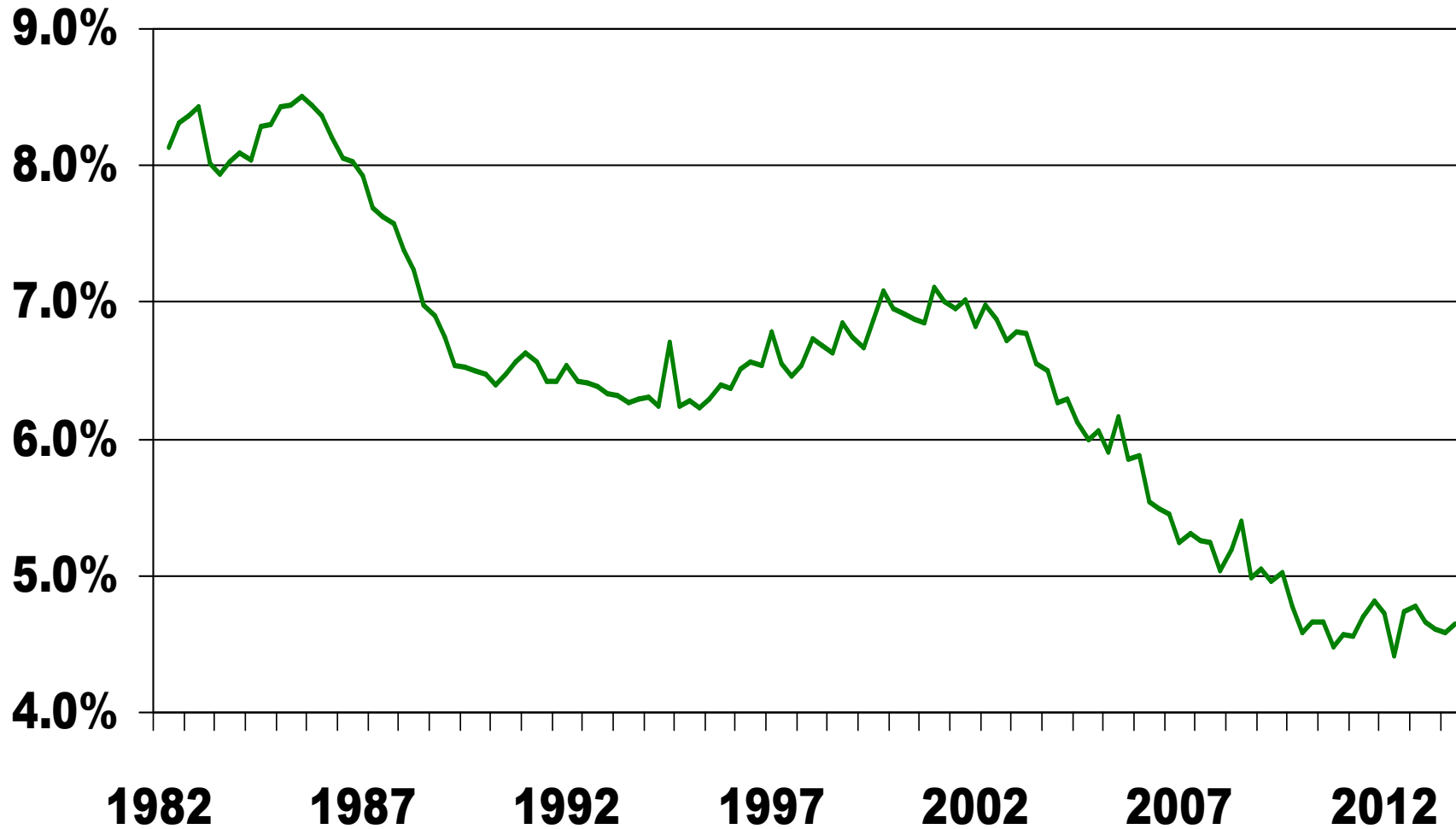
- Rent data not fit for the purpose.
- Should we rely on the price-to-income ratio?
- Interest rates are key.
- Housing is not just a place to live...
- Data from Royal LePage House Price Survey used to calculate capitalization rates

# Housing is Partly an Investment (by Year of 1<sup>st</sup> Purchase)



Source: Mortgage Professionals Canada

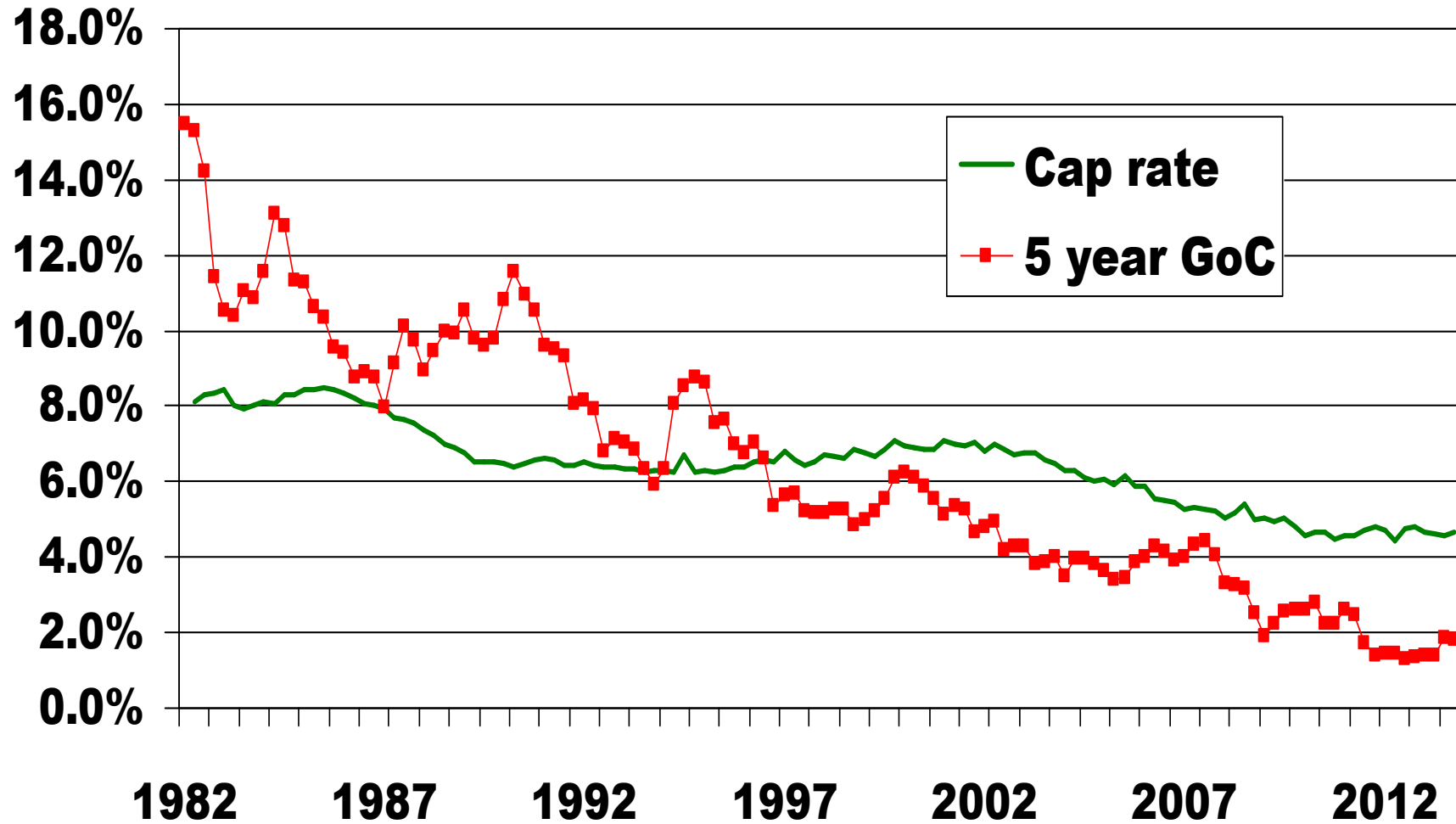
# Cap Rates Have Fallen for Canadian Housing



Source: Will Dunning, using Royal LePage data

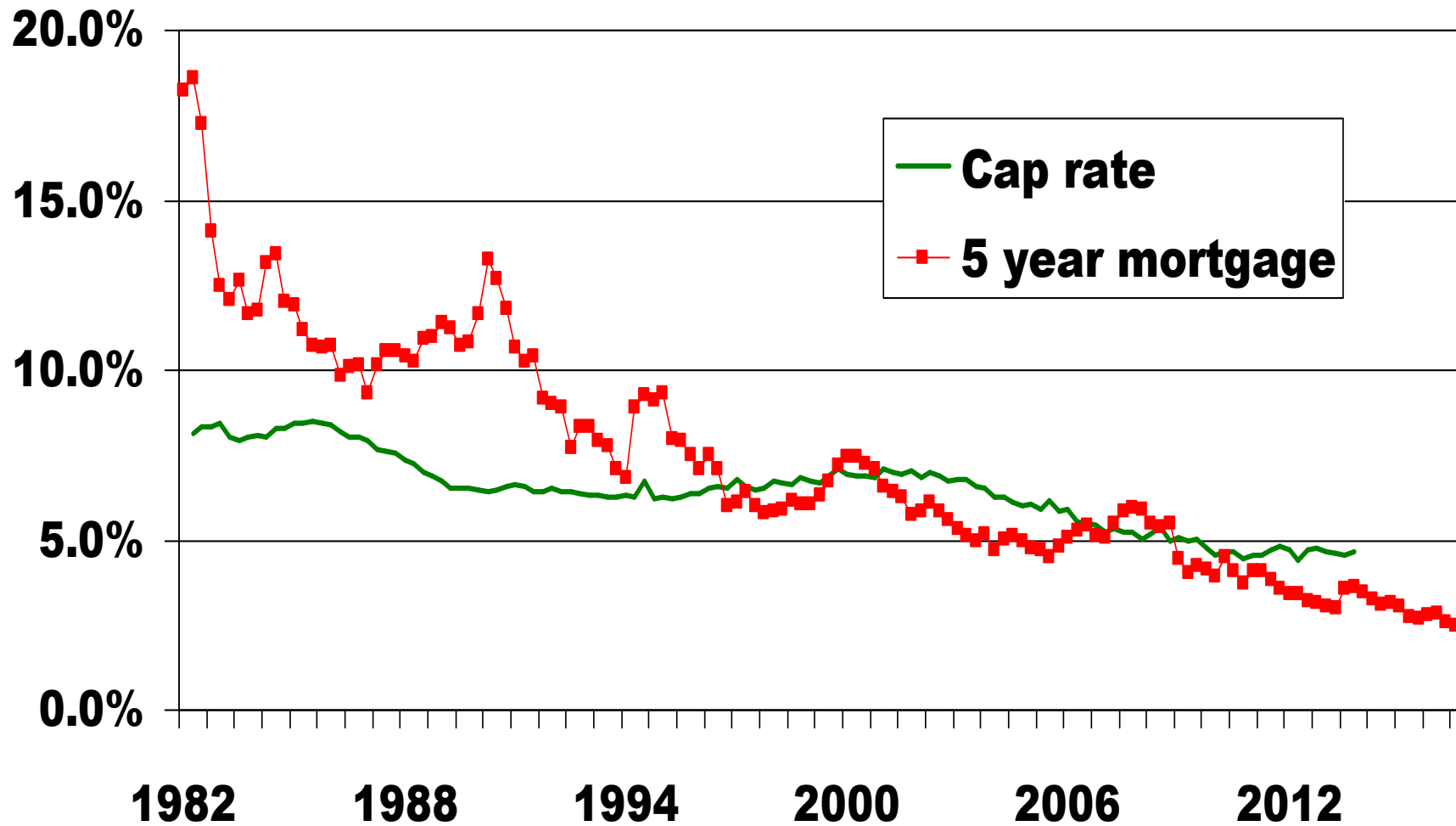


## ... So Have Bond Yields



Source: Will Dunning, using Royal LePage and BoC data

## ... And Mortgage Rates



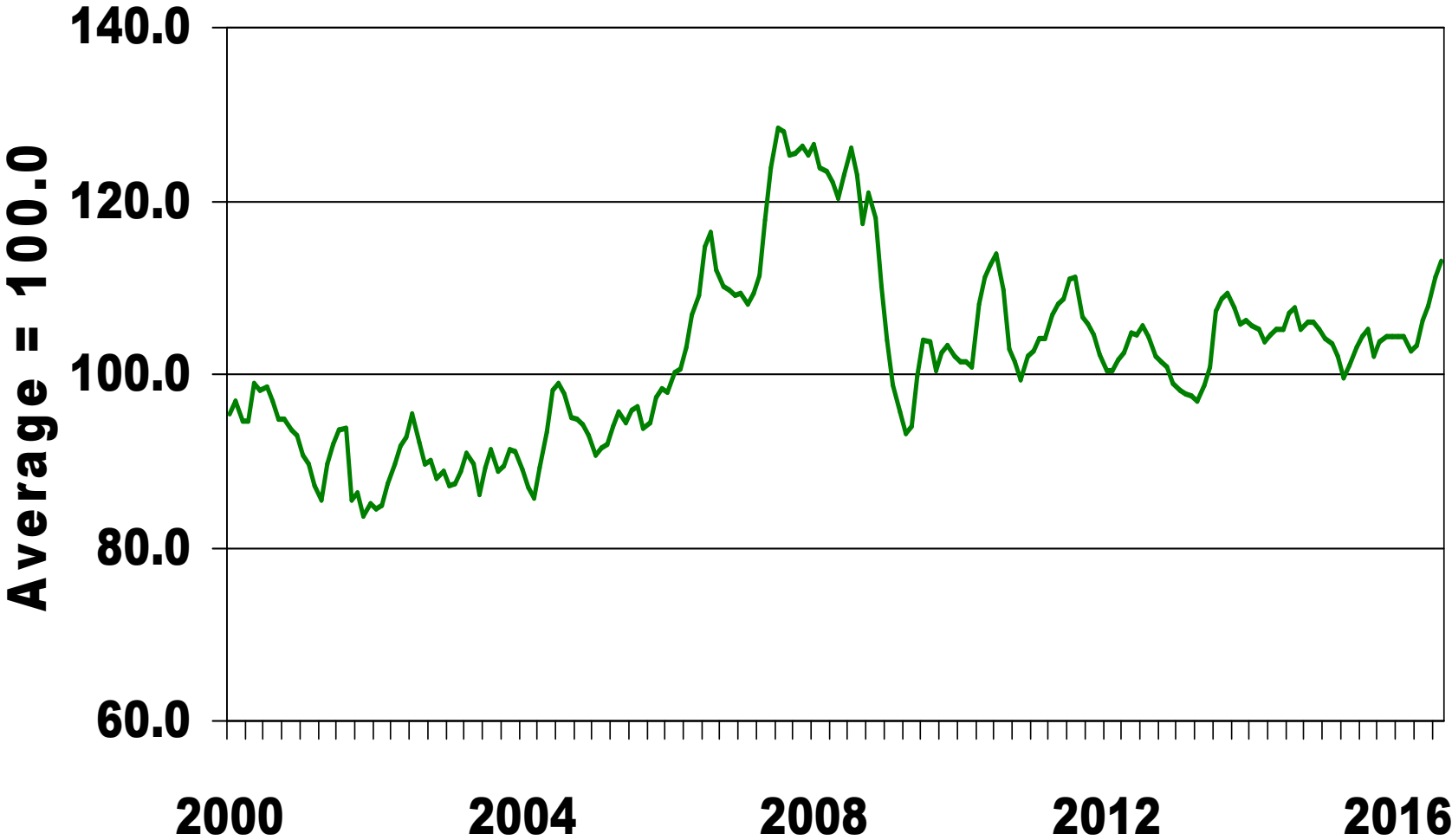
Source: Will Dunning

# Revisiting the OECD Approach

But, use the ratio of mortgage costs (not house prices) to incomes:

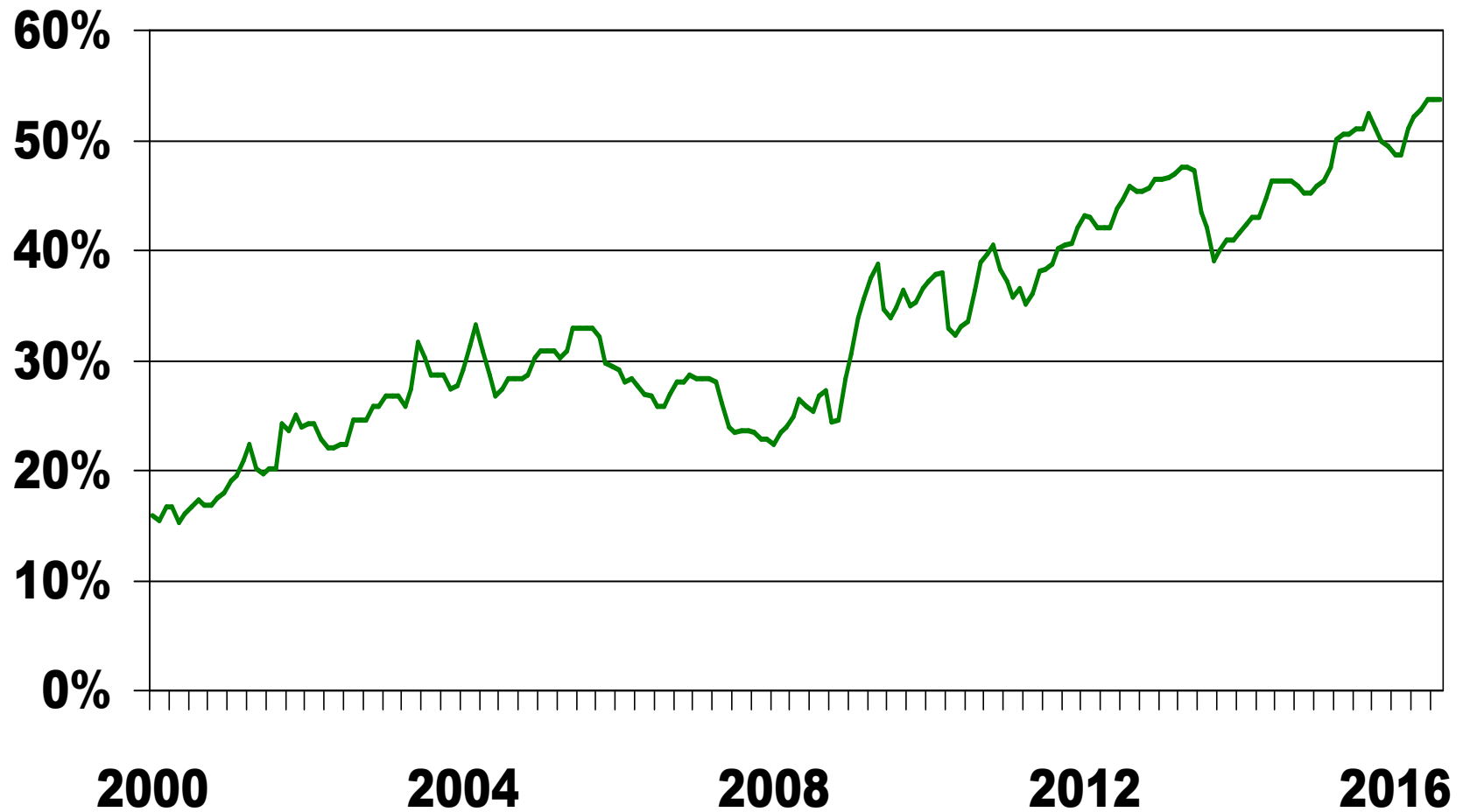
- Further, distinguish between the mortgage cost versus the interest cost
- Principal repayment goes to the owner's bottom line
- Discussion and Charts for 11 major markets in section 5.0 of: [http://mortgageproscan.ca/frontend/web/pdf/LookingforBalanceJune2016Final\\_1468594116.pdf](http://mortgageproscan.ca/frontend/web/pdf/LookingforBalanceJune2016Final_1468594116.pdf)
- All show interest cost ratios far below long-term averages

# Mortgage Costs vs Wages



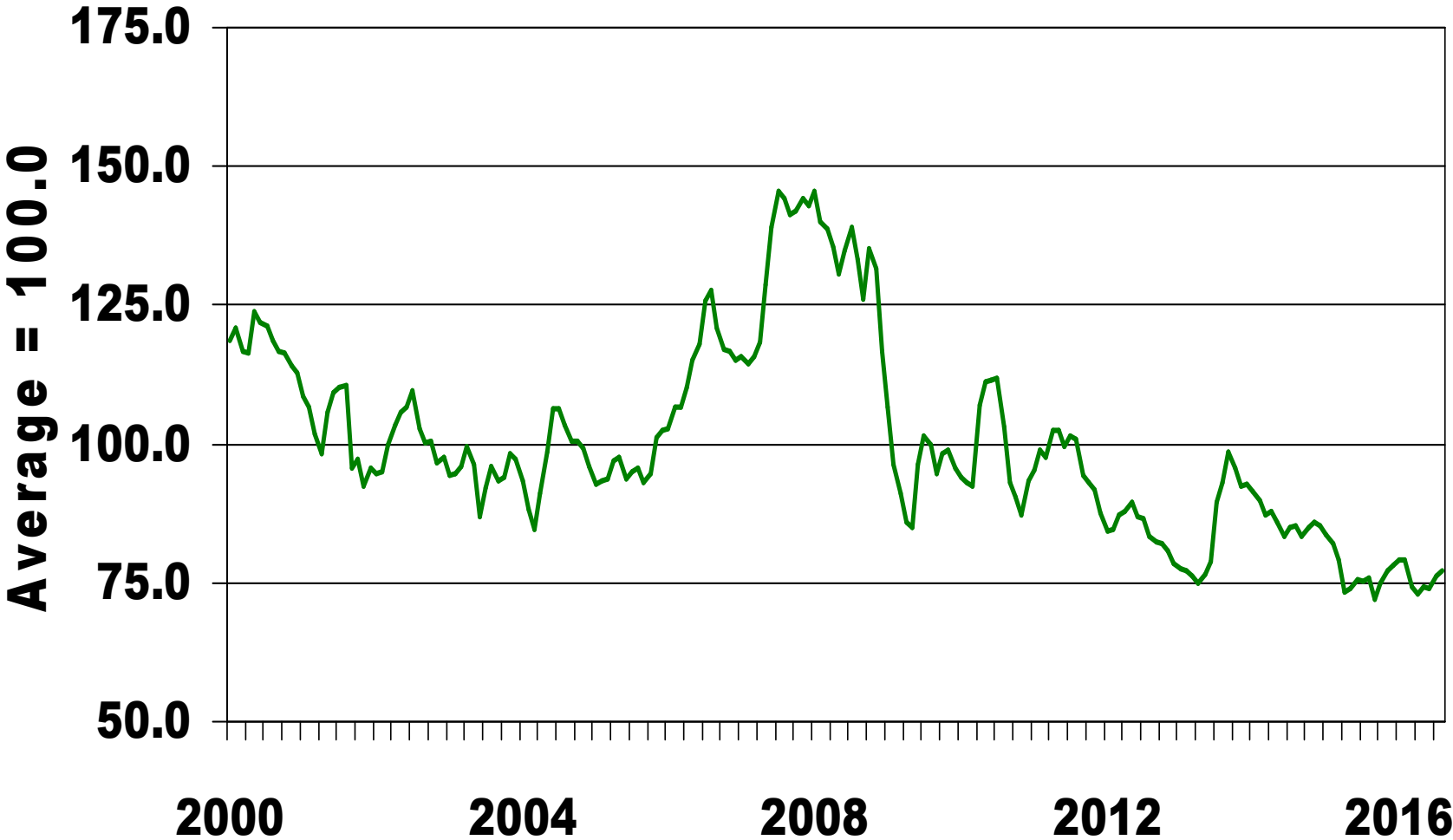
Source: calculations by Will Dunning

# Principal Repaid as % of First Payment



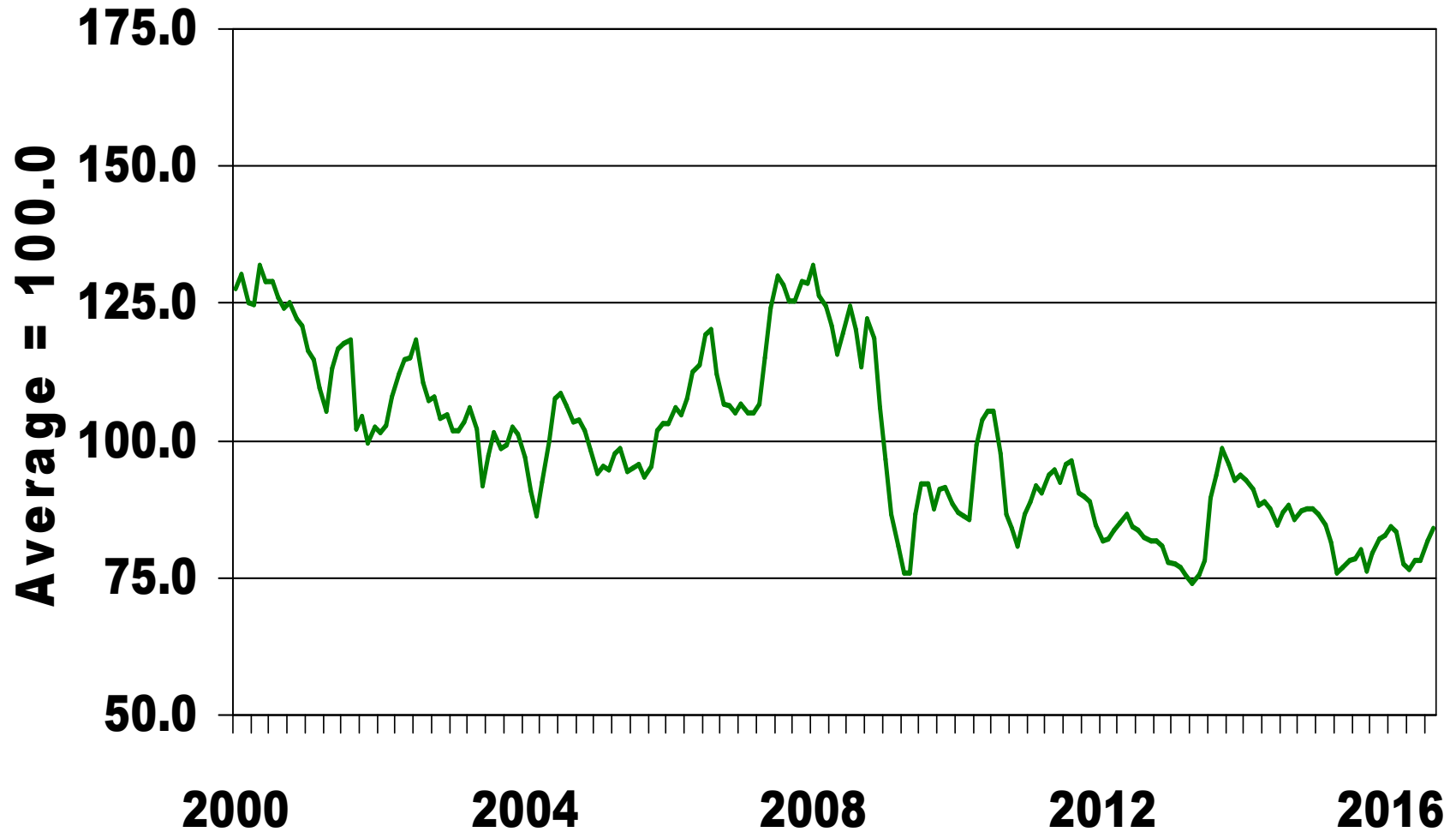
**25-year amortization; 5-year fixed rate mortgage**

# Net Mortgage Cost (Interest) vs Wages



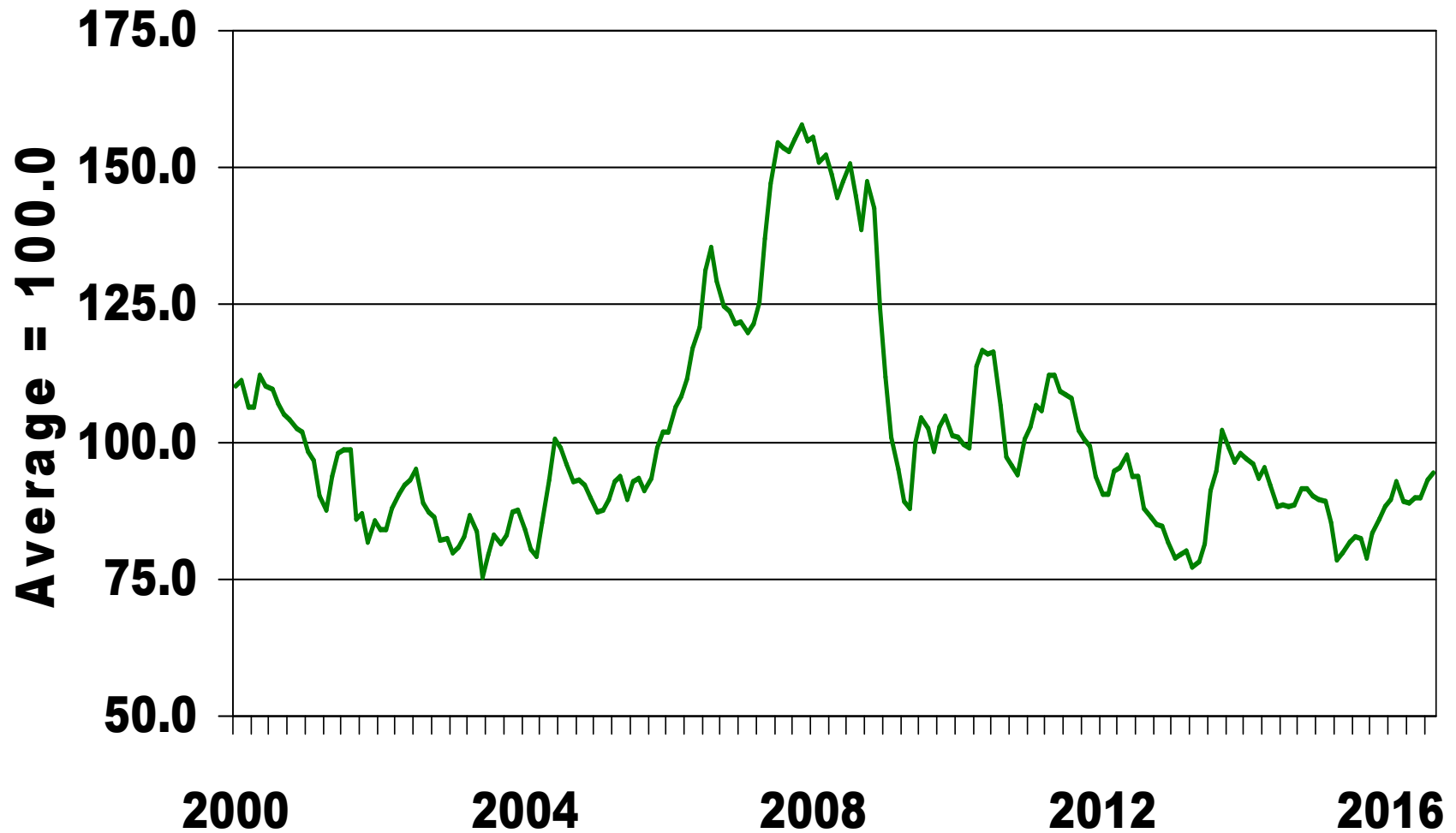
Source: calculations by Will Dunning

# Toronto Net Mortgage Cost Index



Source: calculations by Will Dunning

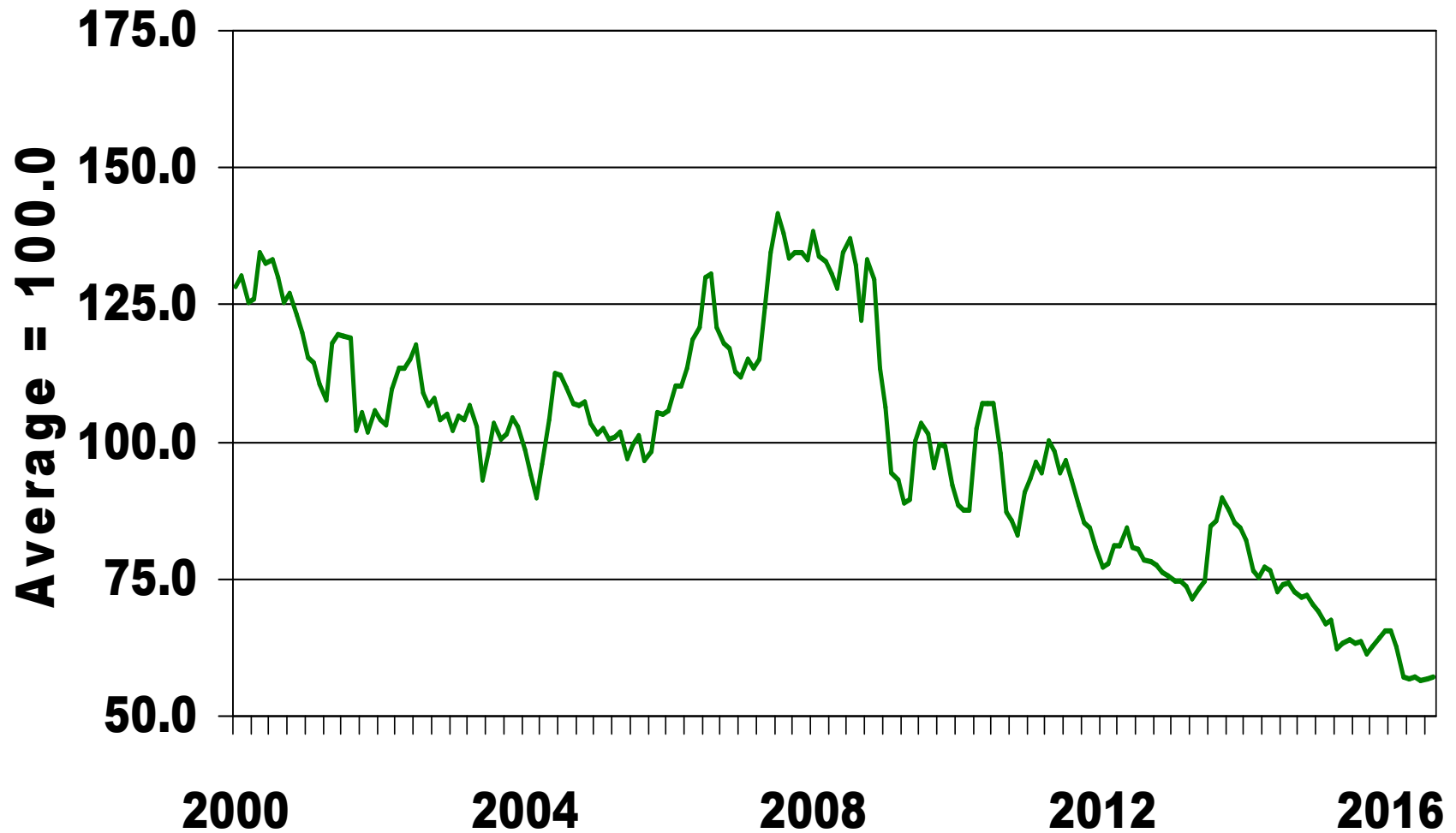
# Vancouver Net Mortgage Cost Index



Source: calculations by Will Dunning



# Halifax Net Mortgage Cost Index



Source: calculations by Will Dunning

# Current Deviations from Long-Term Average

Major Market	Deviation
Victoria	-27.6%
Vancouver	-5.5%
Calgary	-41.2%
Edmonton	-39.7%
Winnipeg	-26.1%
Hamilton	-19.6%
Toronto	-15.9%
Ottawa-Gatineau	-37.8%
Montreal	-35.3%
Quebec	-32.7%
Halifax	-42.8%

# Thoughts on the “Deep Dive”

Ultra low interest rates have created “affordability space” in which house prices could rise

Prices do not need to fill that space – depends on local supply-demand conditions

- What are the supply/demand factors in Vancouver and Toronto?
- Are current trends the result of normal market factors or extraordinary conditions?
- In particular, is a “speculative motive” generating “self-fulfilling expectations”?

Foreign buyers

- First steps being taken
- Did BC go too far?
- Did Ottawa go far enough?

Policy matters

- Prior changes to mortgage insurance policy have deliberately suppressed housing activity and impaired the economy.

# October 3<sup>rd</sup> Policy Announcement

## *7 ways that the housing market has been disrupted*

1. Direct impacts on potential buyers
2. Reduced move-up and move-down buying
3. Weaker job growth further reduces housing demand
4. Hesitation due to potential price reductions
5. Reduced housing starts
6. Buyers of new homes unable to close
7. Reduced housing completions will mean lower vacancy rates and faster rent increases

Impacts on the broader economy

# About Will Dunning

Analysis of housing markets since 1982

Services include:

- Custom research on economics and housing markets.
- Briefings and presentations.

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