Housing Market Digest

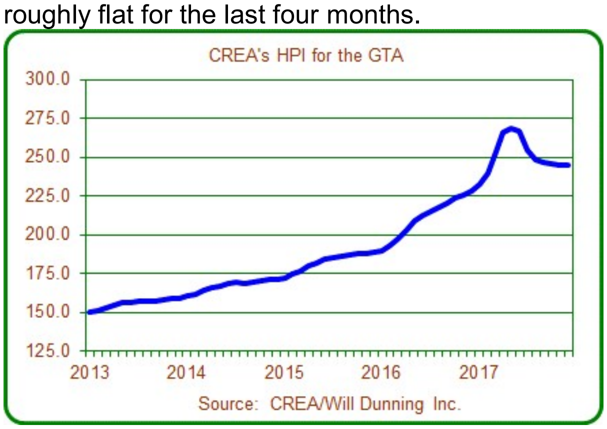
Greater Toronto Area, January 2018

Synopsis: regarding house prices, there is a lot of bad commentary now, based on year-over-year comparisons of average prices. Looking at recent price movements (and for a price index, rather than using averages), there is a Goldilocks story happening right now: the market is calm, with stable prices. This won't last, of course. Forecasts have been updated.

Resale Market

CREA's estimate of seasonally-adjusted sales for December was a bit lower than the guess I showed last month. Still, the final number (annualized rate of 105,000) is quite healthy, in a Goldilocks' zone. This represents a continuation of recovery from the mini-crash last spring, as well as a response to better in-flows of new listings. Plus, there may have been a bit of acceleration by people wanting to avoid the mortgage stress test that took effect on Jan. 1. For 2018, higher interest rates are a negative. Plus, the stress test will likely cause sales to be lower than they ought to be.

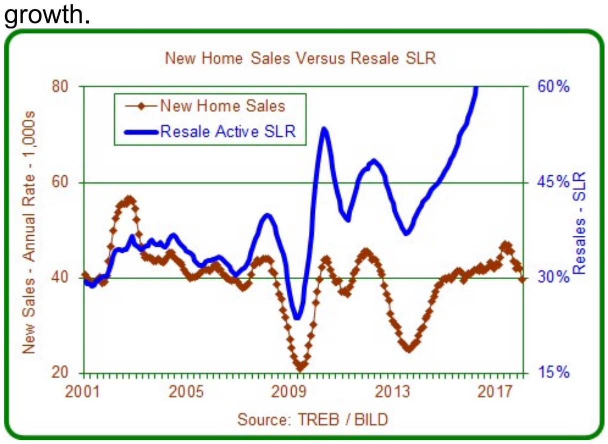
CREA's House Price Index for the GTA has been roughly flat for the last four months.



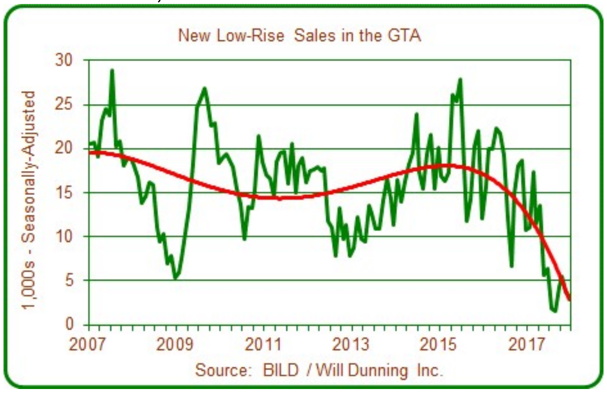
The reduction in sales combined with an improved flow of new listings into the market has brought a sharp drop of the sales-to-new-listings ratio. It is now slightly below the "balanced market" level (low 50%s), which is resulting in price moderation.

New Homes Market

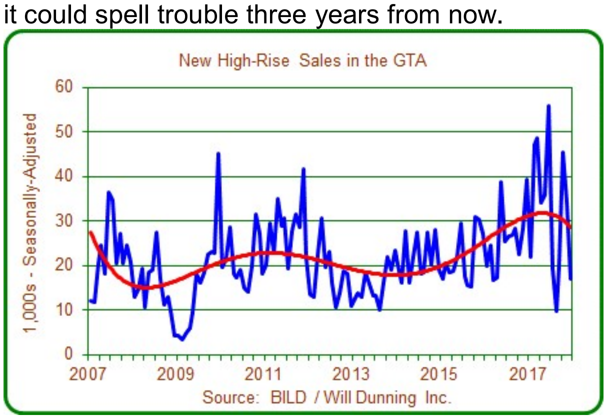
My theory of the housing market says that new housing activity should be closely related to the sales-to-listings ratio: a high ratio leads to price growth, which causes activity to shift from resales to new construction. In this chart, I am using active listings, rather than new listings. Also, it uses smoothed data, to keep it readable. The chart shows that new home sales behaved according to the theory during the "oughties" but not since. During the past decade, new home sales have not responded adequately to the tightened resale market, and in consequence the resale market has become increasingly tight. Lack of newly-constructed dwellings eventually caused the SNLR to literally run off the chart. For the past decade, the new housing shortfall has exceeded 20,000 units per year. The shortfall is not just driving prices to unnecessarily high levels, and preventing people from becoming home owners - the chronic housing shortage is clearly hurting tenants, through extremely low vacancies and rapid rent growth.



Low-rise activity remains shockingly weak. Total sales for 2017 were just 7,714. They should have exceeded 20,000



Sales of condominium apartments have increased, totaling 36,429 for the year. I would argue that investors and speculators have a useful function. Not enough owner-occupants would be willing to buy 2 or 3 years in advance. Therefore, the presale buyers allow the builders to get the financing they need. But, this carries a risk, if the buyers aren't paying enough attention to what the demand will be for the completed apartments. I suspect that this disconnect is now underway, and it could spell trouble three years from now.



For 2018, I am forecasting a substantial drop of condo apartment sales, to the level where they should be. Yet, it is highly possible that investors and speculators will continue to shop with great enthusiasm. For low-rises, it is highly possible that sales will once again be far too low (due to lack of supply), which will further worsen the supply crisis.

Interest Rates

Bond yields have increased. The yield for 5-year GoCs is now (as of January 30) 2.08%, which is 1.3 points higher than the average for 2015/16. Mortgage rates have not fully followed bond yields. The spread between fixed rates (advertised "special offer" from major lenders, which I currently place at 3.5%) versus bonds is now just 1.4 points versus a long-term average of about 1.8 points. Consequently, we are likely to see some further increases for mortgage rates in the near term. For variable rate mortgages, my opinion-estimate is now 3.05%. Lower rates can be negotiated.

Employment

A year ago, Statistics Canada was substantially under-estimating job creation for Toronto CMA. Now, it is grossly over-estimating.

The Outlook

Forecasts have been updated.

Toronto Indicators		
	2017	2018
Job Growth	2.2%	3.6%
Resales (units)	92,688	89,400
Sales-to-New-Listings Ratio	51.9%	50.6%
Ch. in Avg. Resale Price	12.0%	-1.2%
GTA New Home Sales		
Low-Rise	7,714	7,900
High-Rise	36,429	20,000
Total	44,143	27,900
Housing Starts		
Low-Rise Ownership	18,525	9,900
Condo Apartment	17,849	27,300
Rentals	2,364	2,500
Total	38,738	39,700
Apartment Vacancy Rate	1.0%	0.7%
Rent Increase	4.4%	3.7%
Source: forecasts by Will Dunning Inc. (Jan. 30/18)		

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