Housing Market Digest

Greater Toronto Area, May 2018

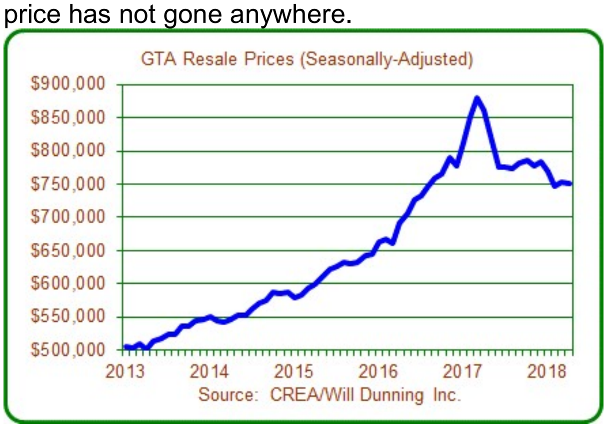
Synopsis: In a modern economy, one of the worst things that can happen is falling house prices. This is not guaranteed to happen, but the risks are mounting, especially in areas with weak local economies. That risk is lower in the GTA, due to chronic under-supply.

Resale Market

The sales rate continues to deteriorate. For April the annualized rate in the GTA was just 68,100 (and the March rate was adjusted downwards to 68,900 from the initial report of 74,400). As commented before, based on the population, a normal sales rate for the GTA would be around 100,000. The slowdown in Toronto has been severe, despite a very strong economy: increased interest rates and the duo of stress tests are weighing very heavily on the housing market. This, in turn is going to impair the broader economy during the coming months.

Housing market situations are even more dire in places that were already weak economically (such as Alberta and Saskatchewan). I sure hope the federal government is paying attention and is preparing the policy changes (reducing severity) that must be made during the next few months.

The average price has increased for four consecutive months. This is a normal seasonal event. After seasonal adjustment, the average price has not gone anywhere.



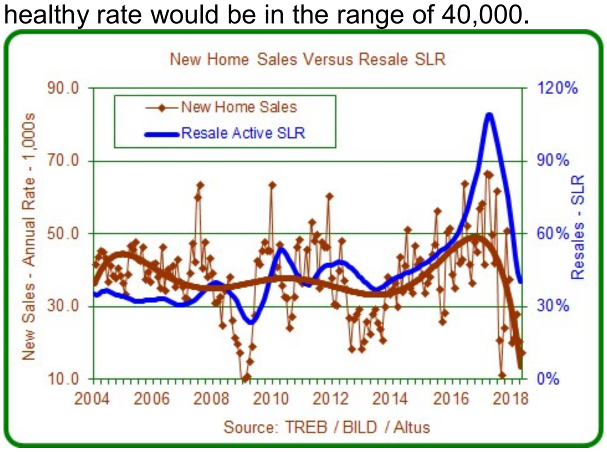
New Homes Market

This month, you have to work extra hard to understand my comments. My theory of the housing market says that new homes activity is highly influenced by the resale market. When the resale market is tight (as shown by a high sales-to-listings ratio) new home sales should be strong. Etc. In these charts, I am using the ratio of sales to active listings.

For new low-rises, the relationship has shifted. For the first four years, new home sales were quite strong. Then, after the recession, even though the resale market got tighter, new home sales fell: there was a sort-of relationship, but new low-rise sales were weaker than they should have been. Then, the relationship totally broke down during 2016, and new sales failed to respond to extremely tight conditions for resales. The result is that after a decade of under-production, the stock of low-rise homes in the GTA is at least 100,000 less than it should be, which sets the stage for excessive price growth. The current situation (a weaker state-of-balance for resales, but still with under-production) will mean that the under-supply situation will get worse.

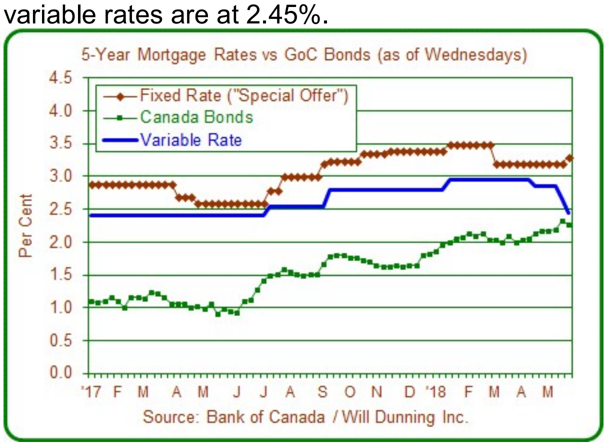
The chart for high-rises is even harder to read, because sales are so volatile. When a trend line is added (the thick brown line), a relationship can be seen between sales versus the state of the resale market – and the relationship has been sustained: apartment sales have "made sense", as they have behaved the way that my theory says they should. During the period of an extremely tight resale market, new apartment sales were very strong. With the recent sharp drop in the resale SLR, apartment sales have also slowed sharply.

Combining low-rise and high-rise sales, this chart indicates that total new home sales are still far too low. The sales rate for May was just 17,700. A healthy rate would be in the range of 40,000.



Interest Rates

Bond yields increased earlier this month (but have retreated in the last few days, to 2.19% for 5-year GoCs, as of Friday the 25th). Shrinking mortgage demand has meant greater competition among lenders: fixed rates have not kept up with bond yields, and variable rates have dropped sharply. My opinion-estimate of a "special offer" rate for 5-year fixed mortgages from major lenders is 3.3%; variable rates are at 2.45%.



The Outlook

Forecasts have not been updated. Just a month after I did these forecasts, it looks like the housing downturn this year might be even worse than I expected. The combination of higher interest rates and the duo of stress tests will continue to weigh very heavily on home-buying. This will gradually impair job creation.

Toronto Indicators		
	2017	2018
Job Growth	2.3%	2.0%
Resales (units)	93,158	78,400
Sales-to-New-Listings Ratio	52.0%	50.6%
Ch. in Avg. Resale Price	11.9%	-1.1%
GTA New Home Sales		
Low-Rise	7,714	5,200
High-Rise	36,429	22,800
Total	44,143	28,000
Housing Starts		
Low-Rise Ownership	18,525	9,800
Condo Apartment	17,849	28,400
Rentals	2,364	3,400
Total	38,738	41,600
Apartment Vacancy Rate	1.0%	0.8%
Rent Increase	4.4%	4.8%
Source: forecasts by Will Dunning Inc. (Apr 25/18)		

Other News

I was in Vancouver last Thursday, where I gave a presentation on housing markets to a large room full of mortgage professionals. (Thank you The Mortgage Centre and Mortgage Architects!) I thought it went well. I'd be happy to do the same for you (for a very modest fee, naturally).

The slide set is available in the Recent Reports section of www.wdunning.com. Of course, you will have to imagine the witty narrative that creates a story line.

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