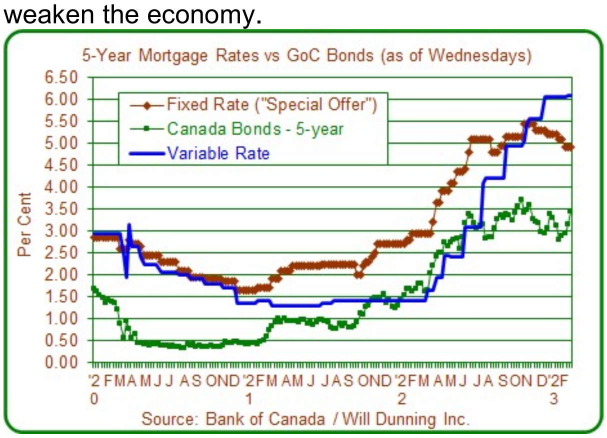
# Housing Market Digest

Canada, February 2023

## Interest Rates

Fixed-rate mortgage rates have crept downwards during the last three months. Late last year, the spread between 5-year GoC bonds and typical fixed rates got fat, at a peak of about 2.35 points (likely because of a heightened sense of risk). Fear has been reduced, and so has the spread, which caused mortgage rates to drift downwards. Today (Feb. 15) with my opinion estimate of the typical rate at 4.9%, and with a recent surge for bond yields, the spread is about 1.5 points, which is close to "normal" (the average over the past 10 years is 1.6 points). So, at this moment, we shouldn't see much change in the 5-year fixed rate. But, this could change, depending on risk sentiments and movements of GoC bond yields. The BoC is now in quantitative tightening mode, and so it would likely lean against any substantive downward move in bond yields. That is, until it has a substantial change of mind about the need to weaken the economy.

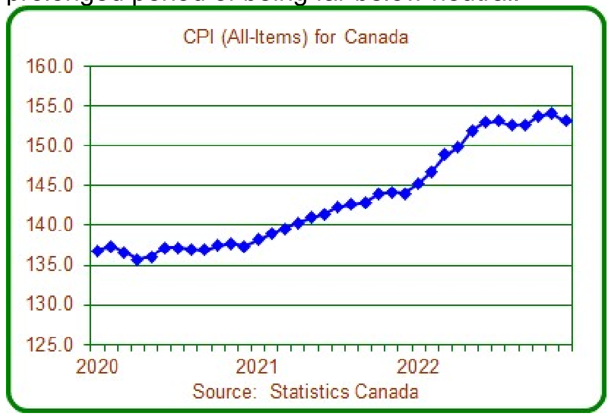



During the summer, I started to think that the most likely course for the Canadian economy is:

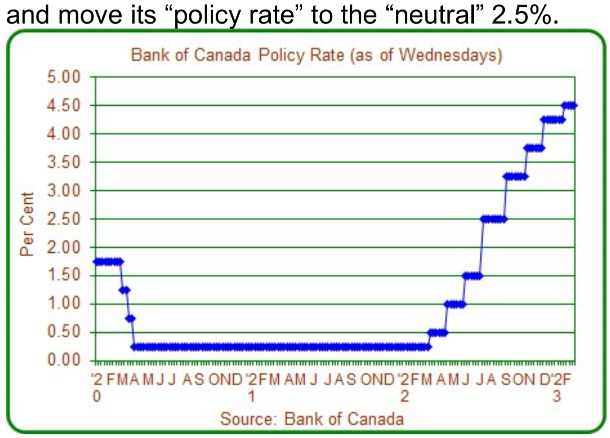
- The impacts of high interest rates will start to develop during the closing months of 2022.
- Evidence will gradually accumulate as data becomes available during the first quarter.
- During the second quarter, the slowdown will become increasingly obvious (and job losses will start to bite noticeably).
- The second half of this year might be quite tough (and this will extend into 2024).

So far, that seems to be what is developing. Apart from employment, key indicators are now starting to turn down. Housing indicators (which lead the economy) are shouting really loudly.

The world experienced a very short period (6 months) of excessive inflation, starting at the beginning of 2022 and ending at mid-year. During the second half, the annualized inflation rate was just 0.3%. The disinflation started because supply-side pressures abated - the turnaround was not caused by the interest rate increases: at the time, at mid-2022, interest rates had just returned to the level the BoC considers "neutral", following a prolonged period of being far below neutral.



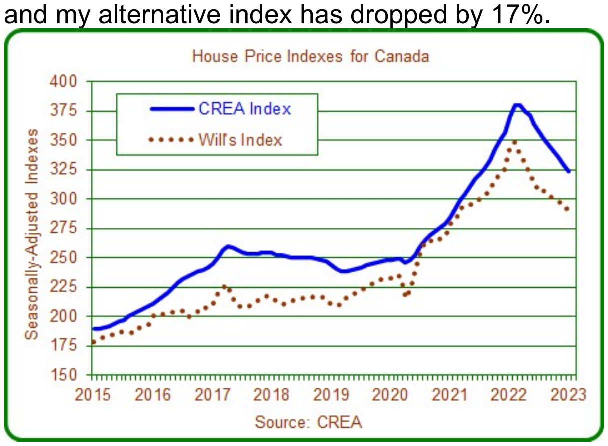

Why is the Bank of Canada still exposing us to the risk of a prolonged economic downturn? It's past time for the Bank of Canada to declare victory, and move its "policy rate" to the "neutral" 2.5%.




## Resale Market

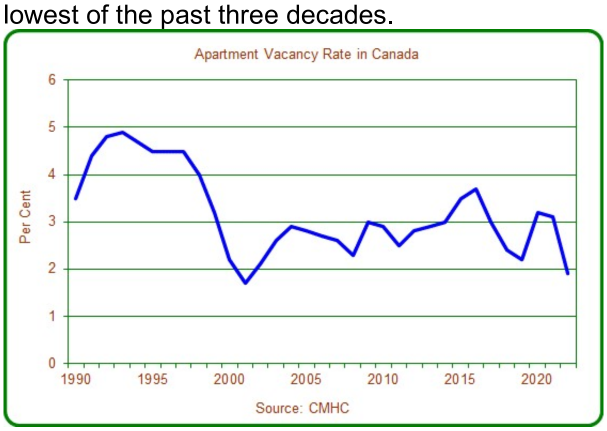
The sales rate fell again in January, to an annualized rate of 395,700. On a population-adjusted basis, this is 28% below the long-term average. The sales-to-new-listings ratio was 50.7% in January, just slightly below the 52% threshold for a balanced market. Flows of listings into the market remain constrained, which is preventing a further drop in the SNLR and in prices. The wild card for this year is to what extent financial hardships (due to unaffordable rises is mortgage costs, but more critically, due to job losses) will result in involuntary decisions to sell, which would raise the number of new listings and active listings in the market. This could create further downward pressure on pricing.


Prices continue to erode. Compared to the peak last February, CREA's price index is down by 15% and my alternative index has dropped by 17%.

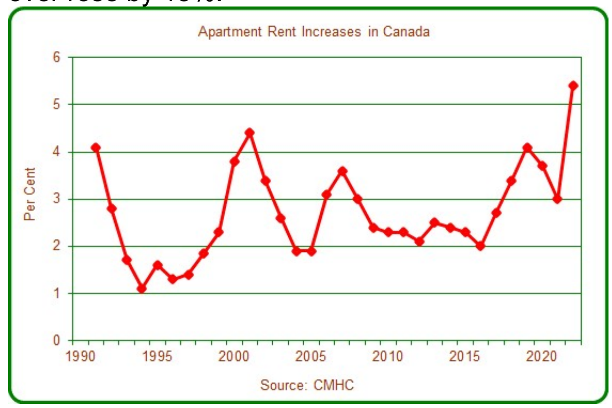



### *Rental Markets.*

A combination of a rebounding employment situation and rapid population growth caused the vacancy rate to fall in 2022: as of October, the apartment vacancy rate of 1.9% was one of the lowest of the past three decades.




Low vacancy rates (and sharp cost rises, notably for energy and interest costs) have encouraged landlords to raise rents rapidly. The survey shows rent growth of 5.4% for the year. This was actually constrained, because most tenants are in rent controlled situations. With some new data, CMHC estimates that rents for apartments that turned-over rose by 18%.




### *Other News*

On February 3rd, I published a report (the first item on this page: [https://www.wdunning.com/recent-reports](https://www.wdunning.com/recent-reports)) which is critical of federal mortgage lending regulations. Once again, I used the "whack-a-mole" analogy to talk about policies that have been futile, because they are based on inadequate theories. And, I argue that the regulations have added to the housing supply shortages across Canada: they may have contributed 200,000 units of the national shortage.

Starting on page 8, there is a discussion about the emerging housing indicators, which point towards a large loss of jobs during this year and next. While housing related impacts will dominate the economic downturn (costing about a quarter million jobs in the coming two years), there are likely to be additional job losses (possibly with a similar magnitude) resulting from reduced consumer spending and business investment. Does the federal government really want to see a half million people lose their jobs?

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