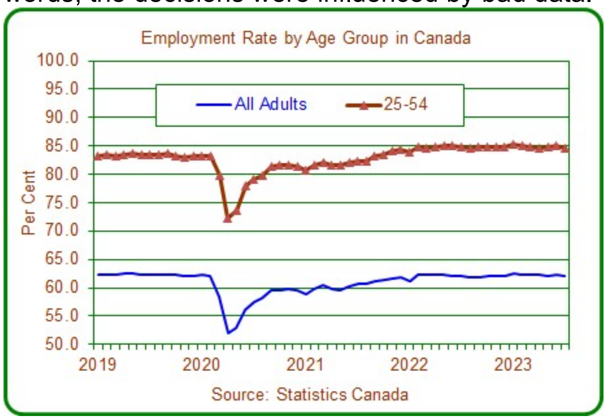
Housing Market Digest

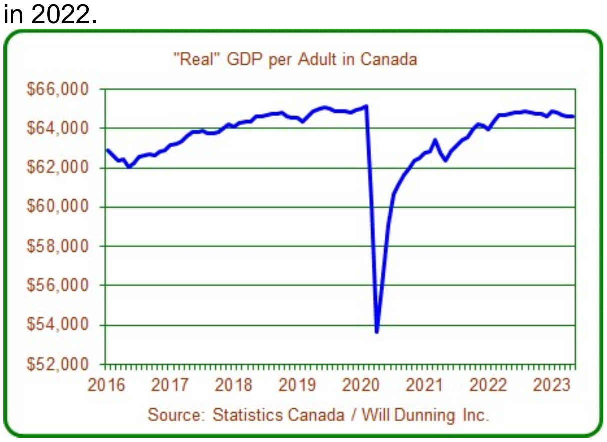
Canada, August 2023

Employment

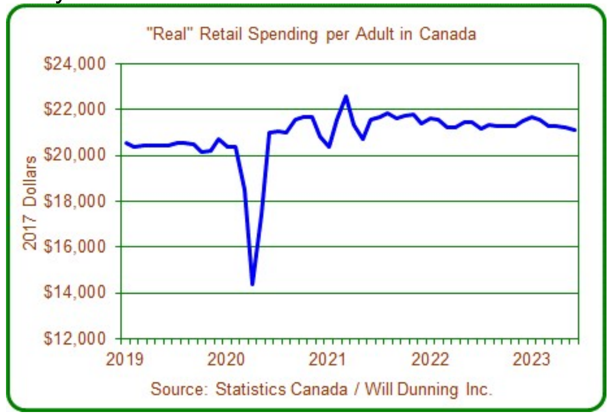
In Statistics Canada's Labour Force Survey, most people are in the sample for 6 months. Therefore, if people leaving the sample have characteristics that are different from people entering the sample, the estimates can change artificially: when there are unusual movements, I wonder if the cause is "sample rotation". In January there was an extreme change in the employment estimate (+150,000). Six months later, a small drop (-6,400) was reported for July. I believe that both of those changes were due to sample rotation. The estimated percentage of Canadian adults who were employed was 62.0% in July, almost identical to the figure for last December (62.1%), and is not materially different than was seen prior to Covid (62.3% in 2019). A further upshot of this data is that the increases in the Bank of Canada policy rate this year have been largely predicated on the supposed strength of the economy. In other words, the decisions were influenced by bad data.



Other major economic indicators continue to indicate that on a population-adjusted basis, elevated interest rates are not yet having an effect. Per capita GDP (inflation-adjusted) is almost exactly the same as in 2018 and 2019, as well as in 2022.



Retail spending (adjusted for inflation and population growth) is almost exactly the same as last year.



But, for both GDP and retail spending, the very recent datapoints are a tiny (but tantalizing) bit softer than previously. It's too soon to say the Canadian economy is starting to turn.

The Bank of Canada

In its report on the inflation rate for July, Statistics Canada said: "The mortgage interest cost index (+30.6%) posted another record year-over-year gain and remained the largest contributor to headline inflation. The all-items excluding mortgage interest cost index rose 2.4% in July."

At this time, the interest rate policy of the Bank of Canada is:

- The primary driver of inflation.
- Creating considerable risks to Canadians' employment, incomes, and their ability to meet their debt obligations.
- In consequence, the greatest risk to the stability of the Canadian financial system is the BoC.
- The BoC policy is depressing new housing construction
- Furthermore, the BoC policy is likely to influence the outcome of the next federal election.

Non-housing inflation has retreated because supply constraints have eased. It isn't because of interest rates - all major indicators except for home sales and residential construction are unchanged (once population growth is considered): the inflation that started in 2011, and now the disinflation, has been on the supply side, not the demand side. I continue to argue that the BoC's intention of softening the economy is a policy error.

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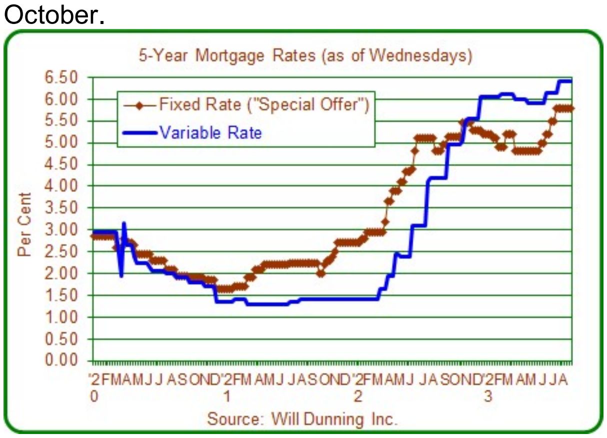
Resale Market

The sales rate was essentially unchanged in July (with a small drop to an annualized rate of 480,300). Activity remains quite weak in historic terms, at 14% below the long-term population-adjusted average (which is now 557,000).

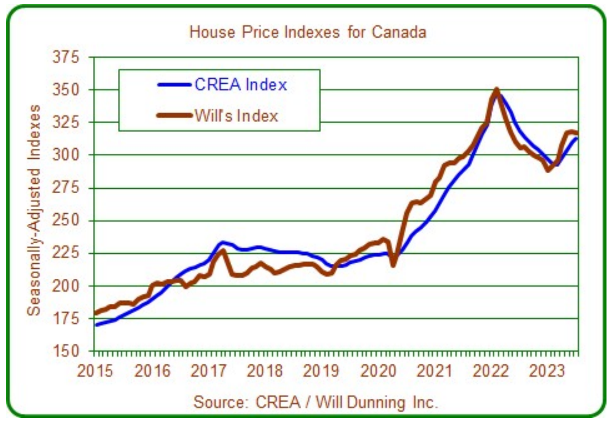
The details are interesting, as there were sales drops in Ontario, BC, and the Atlantic, but rises elsewhere.

I expect that sales are still getting some support from interest rate locks issued during the spring. We won't get a good sense of the effects of current interest rates until September and October.



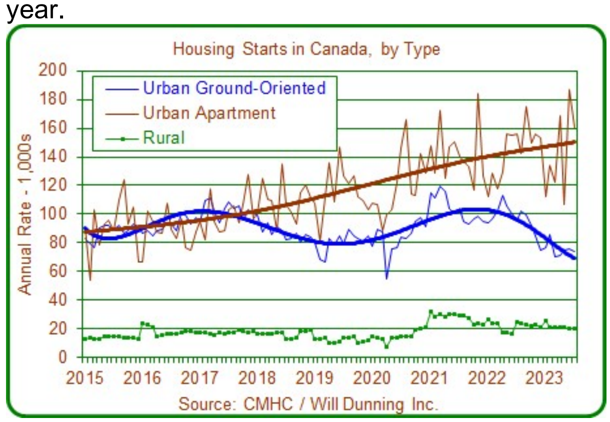
The flow of new listings into the market continues to creep upwards, but from very low levels. Consequently, the sales-to-new-listings ratio is falling, but it is still above the balanced market threshold (59% in July versus the threshold of 52%). Price trends are mixed across the country, but on a national basis, the failing sales-to-listings ratio appears to be bringing some moderation.

As I said last month, I see a possibility that sales will erode sharply during the second half of the year (as new listings continue to expand, and higher interest rates cause a sharp drop in sales).



New Construction

The storyline for housing starts is unchanged: low-rise activity is very weak, while apartment starts are still being supported by decisions made when interest rates were extremely low: this combination is sustaining total starts. I expect starts to be much weaker next year. Correspondingly, employment in residential construction is likely to fall by a considerable amount during the course of next year.



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