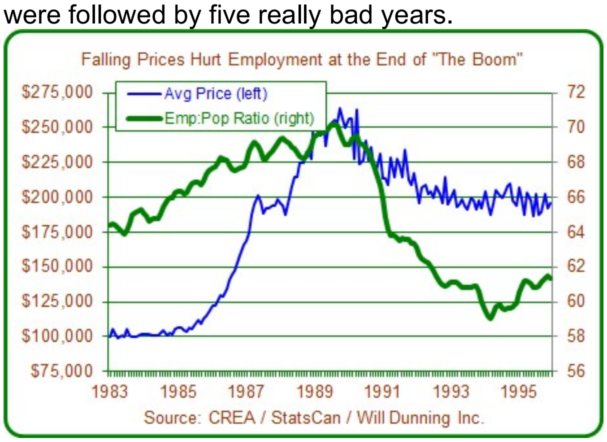
Housing Market Digest

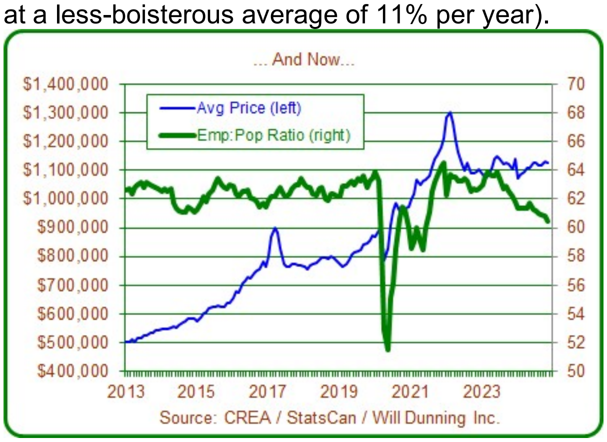
Greater Toronto Area, December 2024

Is this Time Different?

The late 1980s was a really exciting time in the GTA (and it spilled outwards across a lot of the province). Prices rose very rapidly, by about 25% per year for four years. A powerful feedback loop got established. "The Boom" started with an increasingly healthy employment situation, which stimulated housing demand, causing accelerating house price growth, which in turn stimulated increased job creation, and so on. It all ended with a sharp rise in mortgage interest rates (from less than 11% to more than 13%), which caused that feedback loop to work in reverse. Four great years were followed by five really bad years.



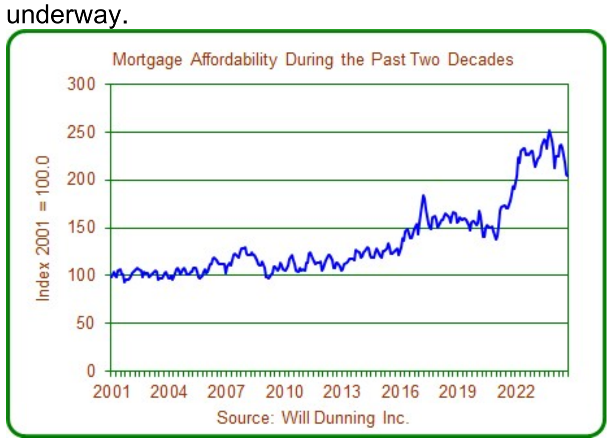
Subsequently, there was a period of very rapid price growth during early 2013 to early 2022 (but at a less-boisterous average of 11% per year).



There are some significant similarities between the two periods, which should cause us to wonder if there is a risk of an economic crash. But, there are also two important differences.

Firstly, the powerful feedback loop seen during "The Boom" probably wasn't repeated this time. (That said: during the past decade, the population has gotten older, and increased retirement should have caused the employment-to-population ratio to fall by about 1 percentage point. While there is a lot of noise in the data, it appears to me that the emp:pop ratio actually increased slightly. I think there was a weak feedback loop.)

Secondly, there was a true housing market bubble during The Boom. On the other hand, there was some froth in the past decade, but it didn't satisfy any good definition of a bubble: price growth was mostly the result of falling interest rates, which created "affordability space" in which prices could rise. There might have been a bit of a bubble during 2016/17, but not before then. Mortgage costs have gotten dreadful during the past two years, due to the unexpected enormous increase in interest rates, and a correction might now be underway.

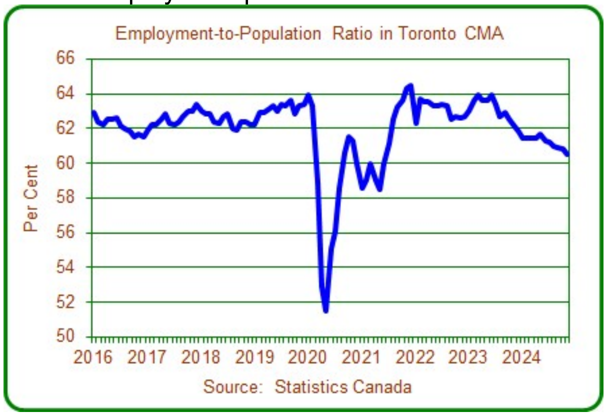


On the other hand, during The Boom, mortgage affordability got really bad because expectations about prices became self-fulfilling – that is the key characteristic of a bubble. There was a lot of reckless behaviour (by consumers and also by builders)

This leaves us with a lot of uncertainty about the outlook – will we see an economic crash like the first half of the 1990s? The two key considerations are:

- Current affordability is unsustainable. Until it significantly improves, home buying (for resales and new homes) will remain very weak. Interest rates probably won't fall by enough to restore healthy affordability. Therefore, to what extent will home prices fall?

- The employment situation in the GTA appears to have weakened a great deal during the past year (as indicated by the employment-to-population ratio). Will "forced sales" generate significant downward pressure on prices? And, will there be a feedback loop in which prices and employment push each other downwards?



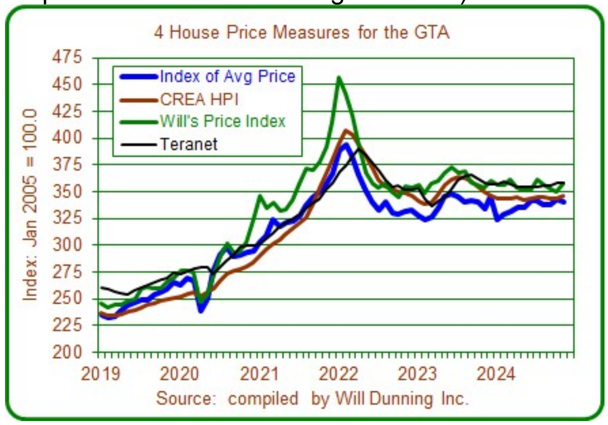
I don't have answers to these questions, but they matter a lot.

Resale Activity

Reductions in interest rates have caused sales to increase for four consecutive months. But, the annualized rate of 77,400 for November is still 31% below the long-term population-adjusted average. Moreover, the current sales rate is similar to the other temporary (interest rate driven) blips that were seen a year ago and during the spring of 2023. (For all of Canada, the shortfall is 7% - this high-cost market is still badly impaired).

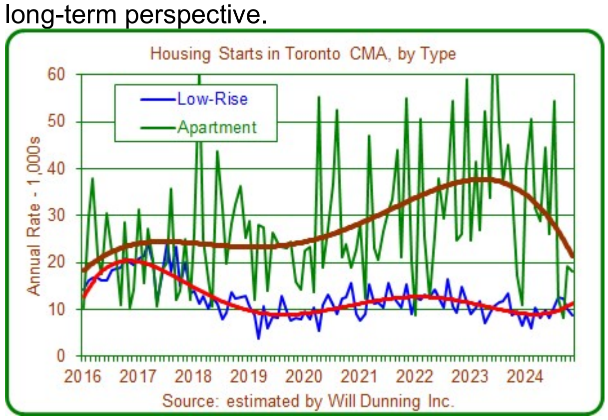
The flow of new listings into the market is still inhibited (on a population-adjusted basis it was 8% below average in November). The sales-to-new-listings ratio has improved, but at 43% it remains far below the balanced market threshold of 52%.

It appears that pricing is still flat in the GTA (unlike the rest of the country, where prices have responded to the recent surge of sales).



New Construction

Housing construction in the Toronto CMA (whether measured by starts or building permit approvals) has fallen compared to 2021-23, but it is still similar to earlier years. I am surprised by this, especially that apartment activity is still strong in a long-term perspective.



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