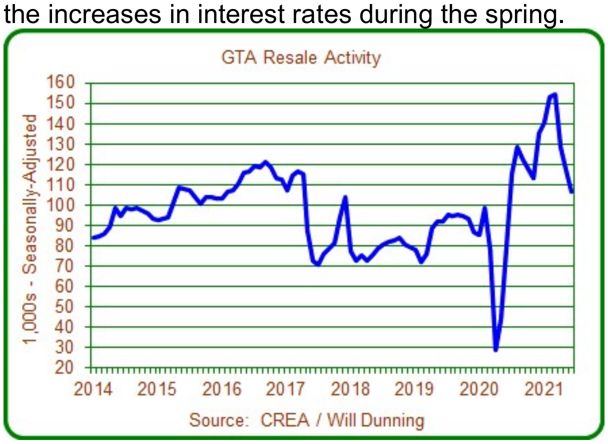
Housing Market Digest

Greater Toronto Area, July 2021

Sales activity has slowed sharply, to a level that is healthy and sustainable. Inadequate production of new housing over the past two decades will continue to haunt us for a long time.

Resale Markets

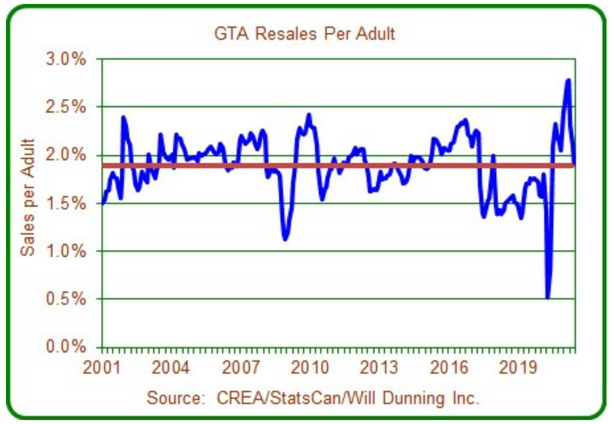
Sales activity has decelerated quite sharply in the GTA. The annualized sales rate for June (106,600, based on 11,106 actual sales) was 31% below the all-time record (154,700) that was set in March. The wild ride seen recently is due to the record low interest rates earlier this year (I argued last month that affordability in the GTA has been excellent), combined with the "sorting process" that was stimulated by Covid-19. There was a rush into the market as rates rose during March but that has now ended. I also expect that there is a lot more price resistance in the market, especially considering the mathematical consequences of the increases in interest rates during the spring.



The Bank of Canada commented a few months ago that it saw evidence of home sales being driven by "extrapolative expectations" (purchases being unduly influenced by expectations that there would be further large price rises). I wasn't entirely convinced, because a vast majority of home buyers work very hard on their decisions, giving careful consideration to their needs, their finances, and their changing circumstances. Plus, affordability was excellent at that time (even in the face of sharply higher prices): there were fundamental conditions that were very supportive of the exceptional sales volumes. I see that the BoC dropped that language in their new Monetary Policy Report (released on July 14).

The sorting process has abated, but I think it will remain a significant factor in the housing market for some time, as people settle into new work arrangements and become more confident about their long-term situations. Part of the sorting process is movement away from the GTA (and other high-cost communities) to smaller cities that have lower housing costs and are less demanding travel-wise. For some time, demand will probably be stronger in those "move to" places than in the GTA.

While sales have slowed in the GTA, I would not describe them as soft. The population-adjusted sales rate for June was almost exactly equal to the long-term average. By contrast, the rate for all of Canada in June was 14% above average, indicative of the shift of demand away from high-cost communities.



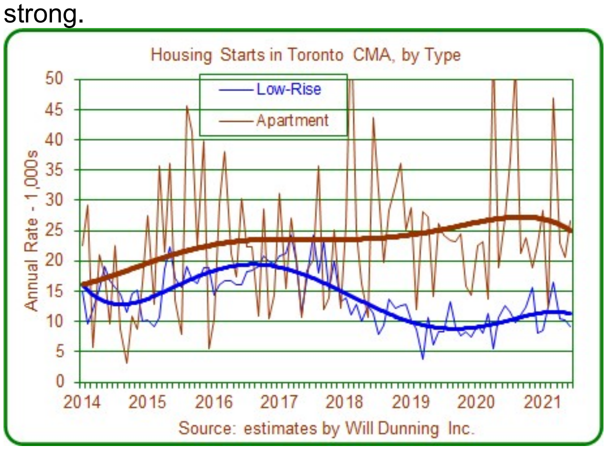
There is some confusion about price trends. Discussion focuses on year-over-year growth, and misses that pricing has been roughly flat since March. Also, price indexes also aren't yet showing the deceleration that is occurring (because their construction involves some smoothing). As an alternative, for many years I have used a Frankenstein price calculation (a fixed-weight average of the median prices by house type that are reported by TRREB).

Price growth has paused despite the fact that the sales-to-new-listings ratio is still elevated (64% in June versus the balanced market threshold of 53%). As I commented last month, I see a possibility of a partial correction, due to price resistance and the end of the urgency that was seen earlier. While I am still reluctant to be very forward-looking, I don't foresee a bloodbath: it will still be the case that there is a huge undersupply of housing within the GTA which will continue to affect pricing for some time.

Housing Starts

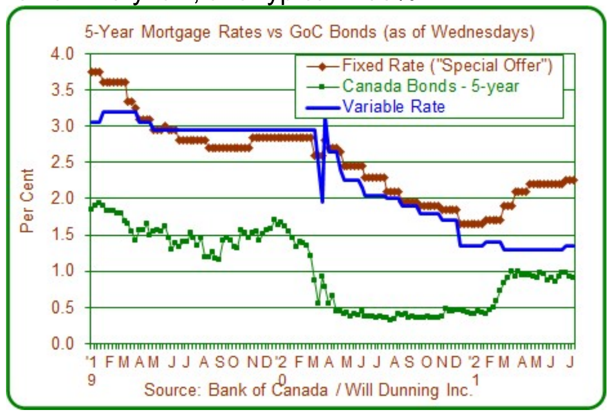
Housing starts have increased sharply in Canada. During the first half of this year, the annualized sales rate (294,000) was 56% higher than the average for the prior decade. But, new housing construction remains sluggish in the Toronto CMA.

Low-rise starts had shown a slight improvement, but that appears to have ended (or, at best, to have paused). The low-rise trend is still far below what is needed by the growing population and to make in-roads on the huge supply deficit that has accumulated during the past 15-20 years. As I've commented previously, we need to see a starts rate for low-rises of 30,000 or higher. The current trend at about 12,000 points to a further worsening of shortages. Apartment activity varies from month-to-month, but the trend remains very strong.



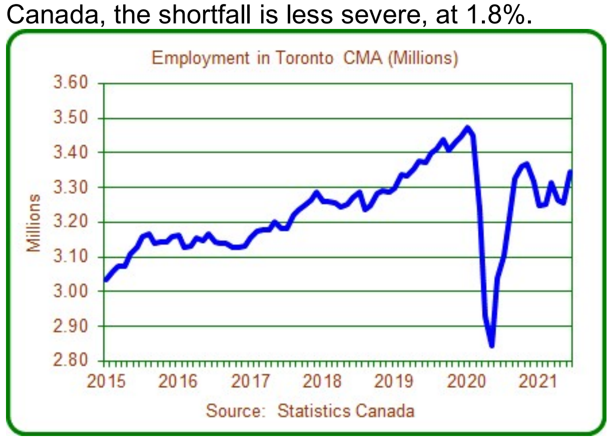
Interest Rates

Interest rates have shown little change since March. Yields for 5-year Government of Canada bonds remain just under 1% (currently 0.9%). I have fractionally raised my opinion-estimate of the typical "special offer" rate for 5-year fixed-rate mortgages (to 2.25%). This is about 1.35 point above the GoC bond yield – this continues to show a competitive lending market. Variable rates remain very low, at a typical 1.35%.



Employment

Employment has still only partially recovered in the Toronto CMA. As of June, it is estimated to be 3.0% lower than in February 2020. For all of Canada, the shortfall is less severe, at 1.8%.



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