

Canadian house prices: Be afraid. Be very afraid

By Michael Babad

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Be afraid as Canadian housing markets rebound.

The Bank of Canada certainly is concerned, and is watching as housing continues to perk up after having slumped in the wake of federal mortgage-qualification stress tests that came into effect in early 2018, aimed at heading off any meltdown.

As *The Globe and Mail's* David Parkinson reports, central bank Governor Stephen Poloz cited the rebound in a speech last week, raising red flags.

“Should this housing rebound continue, we will be watching for signs of extrapolative expectations returning to certain major housing markets - in other words, froth,” Mr. Poloz said.

“The fact is, the fundamental demand for housing appears to be outpacing our ability to build new homes, which can put renewed upward pressure on prices,” he added.

“It can be very unhealthy when the situation becomes speculative because it can lead to a sudden downdraft in house prices later, with wider implications for the economy.”

The “good news,” as Mr. Poloz sees it, is that the stress tests are taking care of riskier debt.

But that won't stop home prices from rising further, notably in the Toronto and Vancouver areas, pressuring the market and making an affordability crisis even worse in certain centres.

“Owning a home in Vancouver, Toronto and Victoria, in particular, continues to be an impossible dream for many,” said Royal Bank of Canada senior economist Robert Hogue, though affordability has improved somewhat.

“And in Montreal and Ottawa, ownership costs have started to pinch,” he added in his latest report on what it takes to own a home.

“Outside these major markets, however, the bar is generally more achievable.”

Consider, for example, that owning a home takes 77.3 per cent of one's income in Vancouver, and 65.6 per cent in Toronto, according to Mr. Hogue.

We'll get a fuller picture Wednesday when the Canadian Real Estate Association releases its December report on sales and prices.

Benjamin Reitzes, Bank of Montreal's Canadian rates and macro strategist, expects the report to show sales surged 16 per cent from a year earlier.

Average prices are forecast to climb about 10 per cent, the fastest rate since 2016, Mr. Reitzes said, with the MLS home price index up 3 per cent, the fastest in about two years.

We've already seen December results from some local real estate boards, highlighting the rebound.

Sales in Toronto, for example, climbed almost 17.5 per cent from a year earlier, while those in Vancouver shot up more than 88 per cent.

“This marked an impressive turnaround from the very weak conditions prevailing at the start of 2019,” RBC's Mr. Hogue said in a separate report.

“There's been increasing evidence since then that buyers have adjusted to earlier policy changes - including the mortgage stress test,” he added.

“Modest declines in mortgage rates over the first half of the year also helped spur demand. The bigger issue now is low inventories.”

We're not seeing prices rise at the stunning paces that prompted action from the federal, B.C. and Ontario governments. But a close watch is needed.

"While home prices in some major Canadian cities aren't bubbling away at the 30-per-cent to 40-per-cent clip of early 2017, they are clearly gaining steam," warned BMO senior economist Sal Guatieri, noting Toronto prices jumped almost 7.5 per cent in December from low levels of a year earlier.

As for Vancouver, the benchmark price is still below that of a year earlier.

"But not for much longer - it's been rising month over month over the last five months," said RBC's Mr. Hogue.

"Home prices are poised to maintain an upward trajectory in the period ahead - quite possibly rising above year-ago levels by the spring (or even earlier)," he added.

"After seeing some affordability reprieve over the past couple of years, Vancouver buyers will again find it harder to achieve their home ownership dream in 2020."