

Housing Market Digest

Greater Toronto Area, July 2020

Synopsis: why are the mortgage stress tests based on an interest rate increase of almost three points, when everybody knows that isn't going to happen?

I'm Still Experiencing Elevated Uncertainty

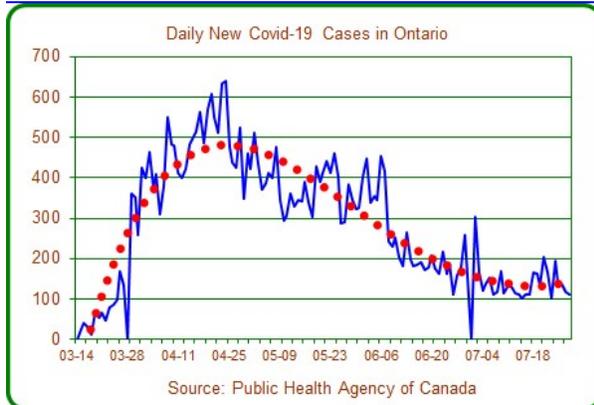
Last month's edition of HMD was about uncertainty. If you didn't read it, please do.

In my economics training (4 decades ago) there was very little discussion about limits to our knowledge, cognitive biases, how difficult it is for us to change our minds... Now, we are getting daily epistemological reminders.

There certainly is some good news (it might be more accurate to say "less bad" rather than "good"). I am definitely feeling less fearful. But, I still think it's crucially important to believe that the situation is precarious, and while it can be very tempting to let down one's guard, we must not.

This chart includes data up to July 28. Updated data can be obtained here:

<https://health-infobase.canada.ca/src/data/covidLive/covid19.csv>

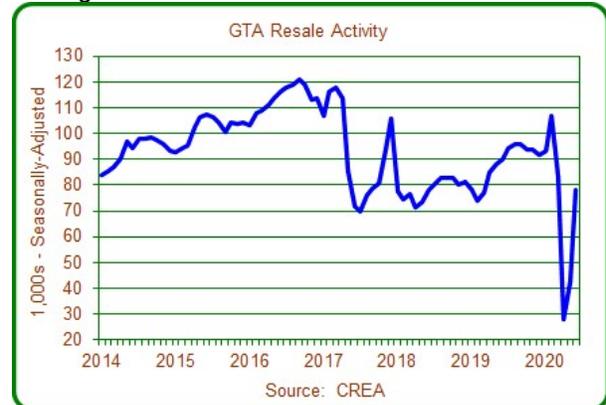


Resale Market

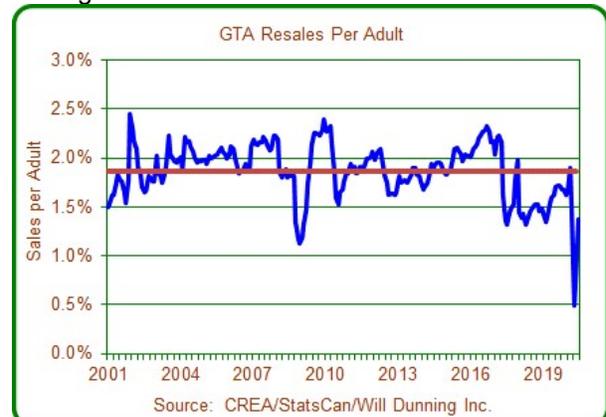
Speaking of cognitive biases, people will have very different reactions to the evolving data from the resale market. Some people might see the jump in June as a sign that the emergency is coming to an end. Others might question the judgement of people who are buying homes at this time. Myself, I see ambiguity.

Sales in June were at an annualized rate of 78,200, up from 27,800 in April and 42,600 in May. For the entire second quarter, the average sales rate was 49,500. Over the long term (2001 to the present), the average rate was 87,200. By this

measure, second quarter sales were 43% below average.



The population is growing, and on-going construction means that there are more homes that could potentially be sold. Making an adjustment for population growth, the long-term average sales rate is currently 106,000. By this measure, sales in the second quarter were 53% below average. Even for June, the strong rebound left sales at 26% below the population-adjusted average.



Anecdotal reports suggest that there will be a further rise in the sales rate for July.

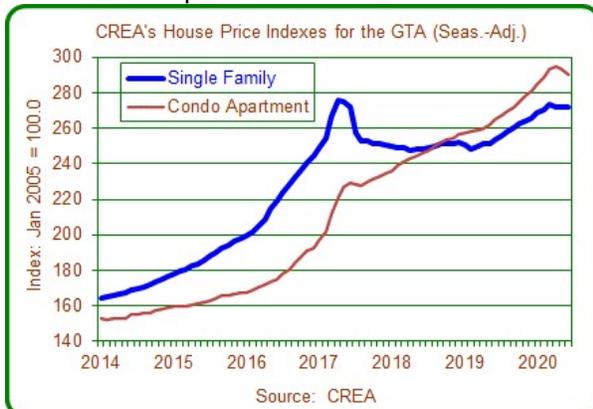
How should we interpret this data? I'm not sure. What we care about is what happens next, and as I've been saying, the evolving data has not given us reliable clues about what will happen during the coming months.

The flow of new listings into the market also dropped very sharply and has partially recovered. As of June, new listings were 23% below the population-adjusted average.

The sales-to-new-listings ratio has been in the 50s for four consecutive months. This is close to the threshold (53%) that I estimate for a balanced market.



Corresponding to the shift in the state-of-balance in the market, there has been an abrupt end to the rapid price growth that was seen earlier. By these estimates, prices have flattened for single-detached homes, and might be eroding for condominium apartments.

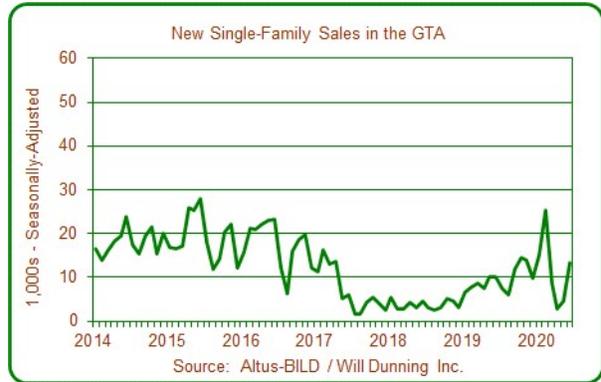


These price indexes get less attention than they should, as most commentary is based on changes in the average price. But, the average price has become very volatile, due to rapid changes in composition (the locations and types of homes sold).

New Homes Market

Sales have also been badly disrupted in the new homes market. Low-rise activity showed some improvement in June, but apartment activity remains badly weakened.

For the entire second quarter, total new home sales (low-rise plus apartments) were at an annualized rate of just 12,600, whereas the market requirement is in the area of 40,000 to 45,000.



Interest Rates

Bond yields are currently making unusually small movements, and are at extremely low levels. So far in July, the average yield for 5-year Government of Canada bonds is just 0.35%.

My opinion-estimate of a typical advertised "special offer" mortgage interest rate (5-year fixed-rate, advertised by major lenders) is now the lowest-ever, at just 2.1%. For variable rates, my opinion estimate is 2.0%. The mortgage stress tests currently use a rate of 4.94%.

I'm looking forward to seeing you again.

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