Housing Market Digest

Greater Toronto Area, February 2023

Interest Rates and the Economy

In the Canada edition, I talked about my expectations for the economy. The bottom line: as many as a half million Canadians could lose their jobs during the coming two years, with impacts becoming increasingly intense during the second half of this year and into 2024.

In the GTA, the job losses are likely to be proportionally greater, because our high housing prices have two big negative effects: we have a more-elevated level of indebtedness, which means consumer spending will be impaired more badly, plus our housing market downturn is more severe. Perhaps one-third of the coming job losses will occur in the GTA.

There is a narrative that existing housing shortages mean that there will be upward pressure on house prices in the coming years. And, I suppose I have contributed to that narrative by pointing out that due to high interest rates and the resulting drop in new home sales, in five years the shortages will be even worse.

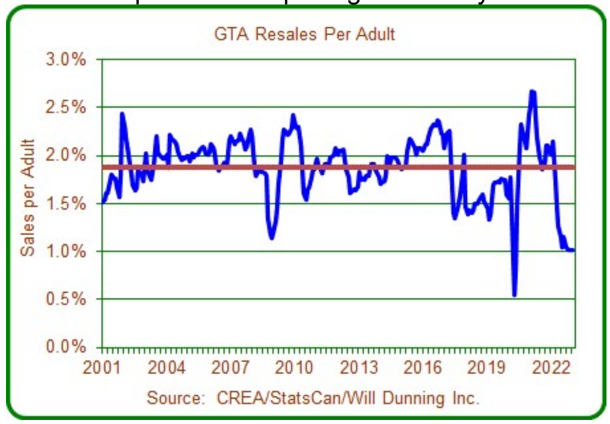
But, the path for prices is not going to be a straight line upwards. I'm fairly certain that price reductions aren't finished yet, because we aren't yet seeing the economic consequences of the rate increases that happened during the past half-year. It is possible (but I'm not saying this as a definite forecast) that five years from now prices might not be any higher than at present (and they could possibly be lower than at present).

There is a great deal hanging on how long the Bank of Canada stays married to its idea that it needs to weaken the economy. That very important policy factor is unpredictable.

Resale Market

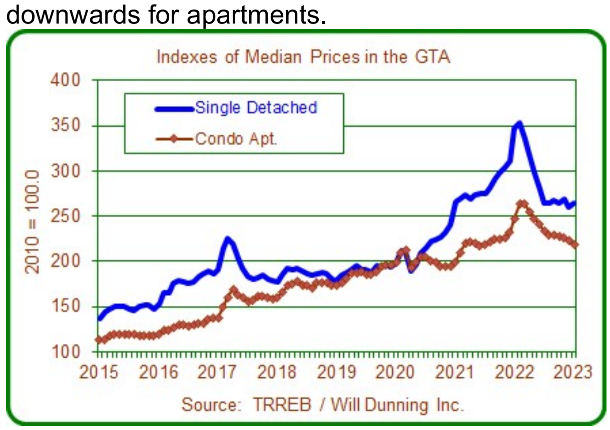
Activity has been surprisingly stable recently (in terms of sales and listings). The sales rate for January remained quite low at an annualized rate of 58,300. On a population-adjusted basis, this is still 45% below the long-term average. For all of Canada, January sales were 28% below average.

Flows of new listings into the market and the inventory of active listings are both at below-average levels. We aren't yet seeing evidence of listings being forced by unaffordable mortgage costs, but that might come later this year. As well, there is risk that future job losses could force increased numbers of people to sell involuntarily. Increased resale market supply could intensify downward pressure on pricing later this year.



The sales-to-new-listings ratio slipped in January, to 39.3%. It remains well below the balanced market threshold (which I estimate as 52%).

Based on median prices, values for single-detached homes have fallen by 25% since last February, but by 17% for condo apartments. The recent data suggests that pricing is currently roughly stable in the low-rise sector, but drifting downwards for apartments.



Employment

During the past two months, Statistics Canada's reports on the employment situation have shown very large increases for the country (69,000 in December and 150,000 in January). In part, this is an offset of sluggish estimates during the summer. It is also possible that sharp increases in mortgage costs are forcing some stay-at-home parents to take jobs.

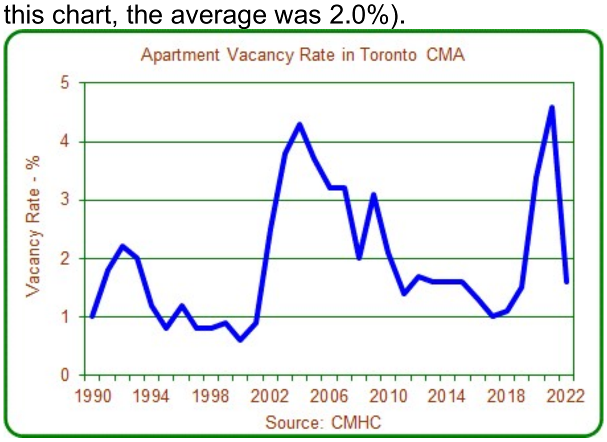
For the Toronto CMA, the estimates for the past year are not impressive (and the share of the adult population that has jobs has fallen compared to last winter).

Rental Market

CMHC reports that for the Toronto CMA, the apartment vacancy rate for October 2022 was 1.6%, down very sharply from 4.6% a year earlier. Rents rose by an estimated 6.2% (versus the unusually low 1.0% estimated for 2021. For most tenants, rent increases were constrained by provincial rent regulations. Using some new data generated in the 2022 survey, CMHC estimated that for apartments for which there was a change of occupancy, rents increased by almost 30%.

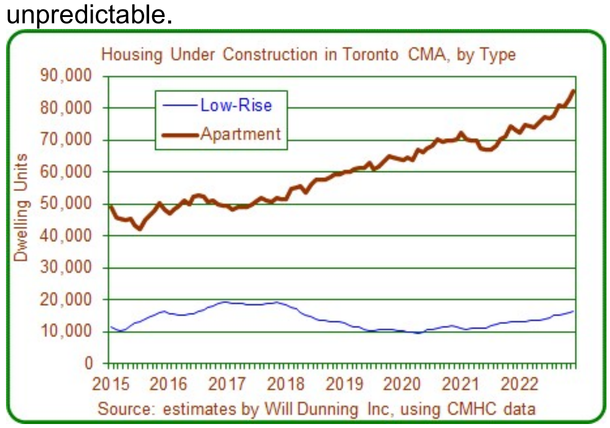
This very sharp drop in the vacancy rate and the increased pressure on rents can be attributed to the rebounding employment situation and population growth (including an influx of returning students). Statistics Canada estimates that during the year up to last July 1, the Toronto CMA population grew by 2.1%. Since then, the growth may have been even more rapid (due to movements by international students and people on work permits). During the prior five years, population growth averaged 1.3% per year/

The vacancy rate for 2022, while too low, was not unusual historically (during the period shown in this chart, the average was 2.0%).



Repeating myself: for the past three decades, investor-owned condos have been the natural form for new rentals. Private market purpose-built will remain marginal. This is because individuals can decide to invest at lower rent levels than companies, reits, etc. Therefore, if there is a lump of purpose-built activity it means that rents are getting higher than they need to be and there will be excess building.

The very large volume of apartments now under construction means that, once enough of it is available for occupancy, vacancies for newish buildings will be considerably higher than they are now and their rents should be considerably lower. But, conditions will still be tight for the older affordable inventory. In my opinion, the supply of apartments is excessive, but the supply of family-friendly housing is far below requirements, and the total supply under construction is much too low. How this combination will play-out is unpredictable.



Tenants in new buildings are vulnerable to excessive rent increases and have inadequate security-of-tenure. What needs to be done now is to agree on what tenant-protections are appropriate.

How to Reach Will Dunning Inc.

Email: wdunning@sympatico.ca
Web site: www.wdunning.com
Twitter: @LooseCannonEcon

Disclaimer of Liability