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GTA HOUSING PULSE

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CANADIAN HOUSING MARKET FORECASTS: OUR TOP PICK

In this issue, we review current forecasts for home price growth in Canada over 2020 and 2021 and implications for the GTA market. We also provide our favourite pick.

Data from the Canadian Real Estate Association last week showed that the introduction of virtual platforms for open houses and offers helped restore some activity to the GTA market in May. However, sales were still down 53% from last year and existing average home prices were 11% below their February peak (although up 3.0% year-over-year).

With the market bottoming, there remains a great deal of uncertainty over the speed of the recovery. At the start of the pandemic, forecasters were expecting the downturn to be short-lived and for the market to snap back quickly once lockdowns were eased. However, physical distancing measures have been in place for far longer than forecasters had anticipated. Figure 2 shows that expectations for home price growth in 2021 have been lowered considerably. In just the last month;

- Only two forecasts (out of the nine surveyed) are still expecting a full recovery in home prices in 2021. We expect further downgrades to these views in the near-future;
- Most forecasts now call for home prices to show no growth over the rest of 2020 and 2021; and
- A few expect that home prices will continue to fall over the next year and a half.

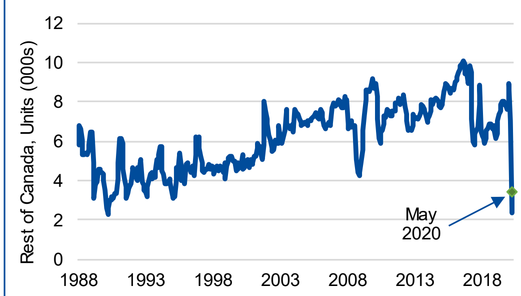
The more positive outlooks expect home prices in large urban areas such as the GTA to outperform other Canadian markets, while pessimistic forecasts expect urban-markets to underperform..

So, with a wide range of expectations for average home price growth, who is right? The data so far supports the view of those who expect stable market conditions for the GTA.

Arguments against the overly optimistic outlooks include:
The view that home prices have bottomed and will rise moderately for the rest of this year and for 2021 are predicated on housing demand outpacing new listings. But, there may be further potential for existing home sales to outpace new listings;

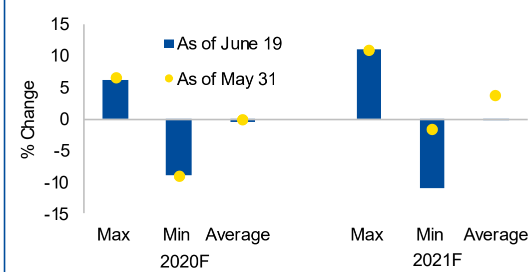
- **Employment remains heavily depressed.** Figure 3 shows that the job market has been an important driver of home sales in the GTA since 2016. While Canada began recouping some COVID-related job losses in May (+200k jobs), the GTA lost another 88k jobs - bringing the tally to 627k since February. Even as lockdowns ease, the return to pre-COVID employment is unlikely in 2020;
- **RBC estimates that immigration will be cut in half this year** (Figure 4) in Canada. Without immigration, the GTA's population would be declining.

Figure 1: MLS Resales, GTA, 1988 - May 2020



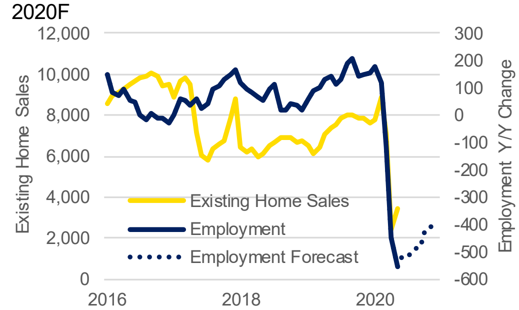
Source: CUR, based on data from CREA

Figure 2: Distribution of Two-Year Ahead Forecasts for Canadian MLS Average Home Price Growth



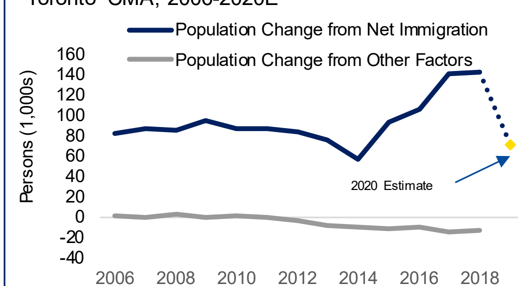
Source: CUR, based on economic forecasts from TD, RBC, CIBC, Scotiabank, BMO, National Bank, Royal LePAge, CMHC

Figure 3: Employment vs. Home Sales, GTA, 2016-2020F



Source: CUR, based on data from CREA and Statistics Canada

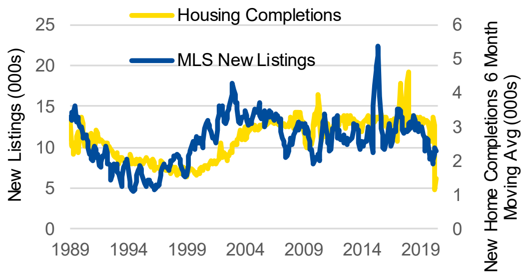
Figure 4: Population Change by Component, Toronto CMA, 2006-2020E



Source: CUR, based on data from Statistics Canada, RBC

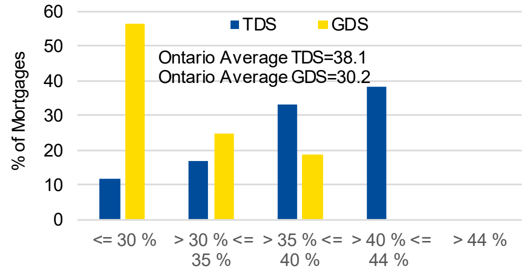
- **New listings likely to outperform weak demand.** Figure 5 shows that new listings in the existing home market grow on par with new construction. The completion of new units helps support the availability of housing for sale, even on the existing home market. Because the construction industry experienced short-lived and very limited shut-downs, completions have remained at pre-COVID levels. Therefore listings could rebound faster than existing home sales; and
- **New CMHC guidelines for insured mortgage approvals introduced last week might offset some of the recent improvements in housing affordability.** Qualifying insured borrowers will now require a credit score of at least 680, a gross debt service/total debt service ratio of no more than 35/40, and cannot have borrowed their down payment. While the majority of mortgage borrowers already meet credit score requirements, over 19% and 38% of insured borrowers take out loans with GDS/TDS greater than 35/40, respectively (Figure 6).

Figure 5: MLS New Listings vs. Housing Completions, 1989-2019



Source: CUR, based on data from CREA and Statistics Canada

Figure 6: Share of Transactional CMHC Insured Mortgages by Gross Debt Service (GDS) and Total Debt Service (TDS) Ratio, Ontario, Q4 2019



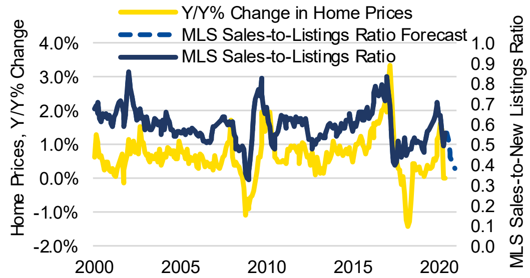
Source: CUR, based on CMHC data

The distribution of job losses (mostly occurring in lower wage industries) and the drop in immigration is particularly challenging for the rental market. Urbanation has released preliminary data indicating decreasing rental prices as of the first quarter of this year. The rental market weakness will bleed into the housing market through decreased investment demand.

Arguments against relatively negative projections include:
The more pessimistic forecasts assume that the economic recovery for COVID-19 will be slow and the economic hit will be the event that pushes indebted households over a debt cliff, but that might be too pessimistic of a view;

- Affordability has improved for those who still have a job and do not need an insured mortgage. Even with an unprecedented drop in household income, the drop in interest rates combined with moderately lower home prices has led to an improvement in housing affordability; and
- Mortgage delinquencies are unlikely to reach crisis levels. Bank of Canada research highlighted in **CUR's last housing pulse** showed that government stimulus programs will help keep the majority of homeowners from defaulting on their mortgages. Mortgage delinquencies will rise through the crisis, which could put some downward pressure on market activity, but not enough to support a highly negative home price scenario.

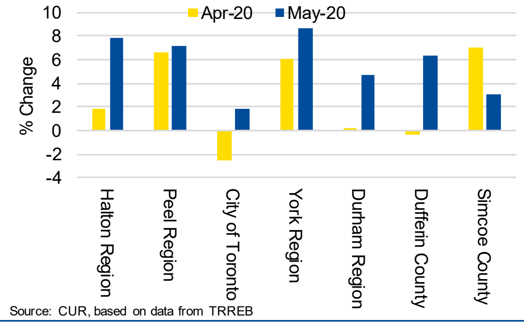
Figure 7: MLS Sales-to-New Listings Ratio and Annual Home Price Growth, GTA, 2000-2020



Source: CUR, based on data from CREA

416 condos to bear brunt of the weakness for the rest of 2020
When we balance the downside and upside risks, the view that home prices will remain stable throughout the rest of the year seems like the most likely scenario. Even in a scenario where sales only make up half of their losses by year end and listings jump back to pre-COVID levels, the sales-to-listings ratio would range between 40 and 50; a level that would be consistent with flat home prices (Figure 7). However, there is likely to be a wide variance in the performance across regions in the GTA and by housing type. The condo market in the 416 market could underperform the rest in 2020;

Figure 8: MLS Avg Home Sale Prices, Y/Y % Change, GTA, April 2019 and April 2020



Source: CUR, based on data from TRREB

- Last week's TRREB data showed that the jump in existing home prices in May was more subdued in the 416, due to condos, than in the 905 region (Figure 8);
- Over 80% of the rental market is in the 416 market, which will disproportionately be impacted by reduced immigration and the job losses that have occurred so far; and
- The condo market (especially in the 416 market) accounts for a large share of the units under construction. Of the 2,942 units completed in the GTA in May, 2,369 were apartments. Of the 76,183 units currently under construction in the GTA, 51,600 are apartments in city of Toronto.