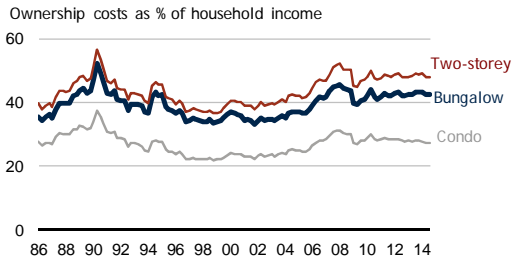


## HOUSING TRENDS AND AFFORDABILITY

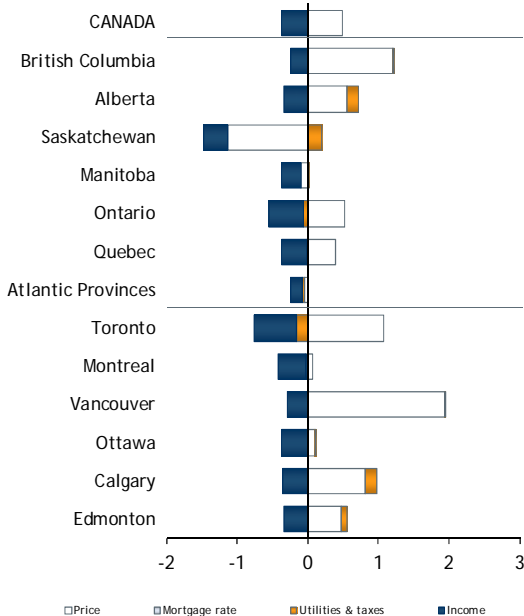
November 2014

### RBC Housing Affordability Measures - Canada



### Factors contributing to the change in the RBC affordability measure

Percentage point change from a quarter ago (detached bungalow)



Source: Statistics Canada, Royal LePage, RBC Economics Research

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## Housing affordability predominantly improved across Canada in the third quarter of 2014

Despite generally increasing home prices, home ownership became more affordable in most of Canada (albeit slightly so) in the third quarter of 2014. Carrying the costs of ownership became a little lighter for the majority of housing types thanks to small reductions in utility costs in many parts of the country, low and steady interest rates, and broadly rising household income. Even markets such as Toronto, where affordability eroded persistently in the past four years, saw some relief. The same could not be said for Canada's other currently 'hot' markets, Vancouver and Calgary, however—although in the case of Calgary, housing affordability remains quite attractive. At the national level, RBC's affordability measures eased in two of three housing categories: decreasing by 0.2 percentage points to 47.8% for two storey homes and 0.3 percentage points to 27.1% for condominium apartments, and inching higher by 0.1 percentage point to 42.6% for detached bungalows (a decrease represents an improvement in affordability).

### Price drops help lower the costs of ownership in Saskatchewan and for condo buyers in Quebec

Recent declines in home prices in Saskatchewan generated some of the bigger improvements in affordability among local and provincial markets in the latest period. A sizable improvement was also registered in the condo segment in Quebec—similarly reflecting a drop in prices. Overall, better affordability conditions emerged primarily on the condo side across Canada, with a strong majority of markets showing a decline in RBC's condo measures. Improvements were somewhat less generalized geographically on the single-family homes side.

### Recent departure from generally flat trend in recent years

Moderation of the RBC measures at the national level in the third quarter represented the third such easing for the single-family home categories in the past year and the fourth straight for the condo category. In all cases, RBC's affordability levels now stand below year-ago levels. These recent developments contrast with the predominantly flat trend in recent years, whereby RBC's measures alternated between periods of improvement and deterioration.

### Little evidence of affordability pressures outside Vancouver and Toronto

Nonetheless, the latest readings still show the measures exceeding long-term averages for single-family homes at the national level, thereby suggesting the persistence of mild affordability-related pressures. It continues to be the case, however, that the bulk of those pressures originates almost entirely from Vancouver and Toronto, where affordability remains the most stretched in Canada. There is little evidence of undue affordability stress in other markets, with the possible exception of two-storey homes in Montreal. For condo apartments, RBC's measures more closely match long-term averages for all markets ex-

cept Vancouver (and possibly Toronto). Condos continue to be the more affordable ownership option in every market, which largely explains the popularity of this type of housing in Canada in the past many years.

### Home resale activity showing few signs of letting up

The overall tone of Canada's housing market continues to be quite solid at this late stage of 2014, with home resales sustained near the highest levels since early 2010. In October 2014, nationwide resales increased for the eighth time in the past nine months. That being said, conditions continue to vary substantially across markets. Strength at the national level primarily reflects robust activity in a trio of 'hot' markets—namely Calgary, Toronto, and Vancouver—where the supply of homes for sale remains tight relative to solid homebuyer demand. Heat in these markets overshadows balanced or soft conditions elsewhere in the country. This split picture translates into contrasting price trends, whereby property appreciation in Calgary, Toronto, and Vancouver far outpaces appreciation in other markets.

### Higher interest rates would reverse recent improvements in affordability

Part of the vigour in the Canadian market since spring can be attributed to unexpected declines in fixed-mortgage rates earlier this year, although we believe that this effect will dissipate in the months ahead. In fact, we expect interest rates to become a dampening factor during the coming year. We anticipate that the Bank of Canada will raise its overnight rate in mid-2015 and that longer-term rates will start their upward climb well before then. The combination of gradually increasing interest rates and higher home prices would work to reverse the improvement in housing affordability that took place in the past year and weigh more heavily on homebuyer demand in Canada. We believe that the next stage of the housing cycle, therefore, will be a transition toward lower resale levels and more subdued rates of price increases. This transition should gather strength once interest rates show a material advance toward reaching normal levels.

## Provincial overviews

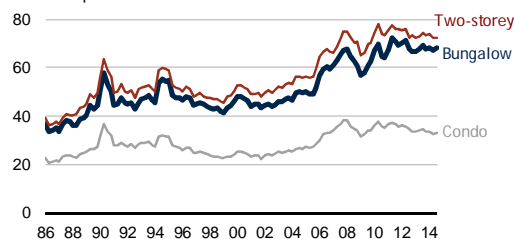
### British Columbia – On the up and up

The 2011–2012 housing downturn in British Columbia clearly is a distant memory by now, with steady gains registered since last year not just in Vancouver but also in the majority of local markets. In the third quarter of 2014, overall home resales in the province increased by a solid 4.0%, further adding to an even stronger 10.4% advance in the second quarter, and moved above the 10-year average level for the first time since the end of 2009. Vancouver accounted for only one-third of the increase in quarterly sales in the past year. Home prices are picking up across the province; however, the pace remains generally subdued outside the Vancouver-area market. Amid this broad market strengthening, housing affordability has come under pressure once again in the third quarter. RBC's measures rose for all housing categories in the province by between 0.2 and 1.0 percentage points. Affordability continues to compare poorly against historical norms in the province and measures elsewhere in the country, although this largely reflects the extreme conditions prevailing in Vancouver.

## RBC Housing Affordability Measures

### British Columbia

Ownership costs as % of household income



Source: Statistics Canada, Royal LePage, RBC Economics Research

### Alberta – Reaching new heights despite oil market turbulence

Economic uncertainty associated with the recent slide in crude oil prices so far does not seem to have fazed Alberta homebuyers one bit. Not only have home resales further increased in the third quarter (by 0.9% relative to the second quarter) but also they have set a new record-high for the period. A strong economy and rapid population growth continue to trump any possible worries that Alberta's energy boom might turn into a bust in the near future. Another supporting factor for the provincial market remains attractive affordability, despite some deterioration lately. As a share of household income, homeownership costs are still fairly low in Alberta—both compared to long-term and national averages. In the third quarter, RBC's measures climbed modestly by 0.4 percentage points for both bungalows and two-storey homes (to 32.3% and 33.7%, respectively). The measure for condo eased by 0.2 percentage points to 19.9%, which was the lowest level among the provinces.

### Saskatchewan – Homebuyers still active but supply keeps creeping higher

Home resale activity in Saskatchewan stabilized at an elevated level in the third quarter, following a snapback in the second quarter from a weather-induced slowdown at the start of 2014. While the number of homes sold on the Multiple Listing Service (MLS) system fell modestly (by 1.4%) in the third quarter relative to the second quarter, it still set a high watermark for a third quarter in the province. More recently, however, the main challenge in Saskatchewan has been a significant increase in homes available for sale—partly resulting from a rise in new unit completions. New listings have grown consistently more than resales since 2012, which softened demand-supply conditions enough by 2013 to cause price drops in Regina, and now they are threatening the same in other markets such as Saskatoon. Price declines contributed to significant improvement in affordability in the third quarter, especially in the bungalow segment. RBC's measures fell by 1.3 percentage points for bungalows (the largest such decline in the country), and by 0.4 percentage points for both two-storey homes and condominium apartments.

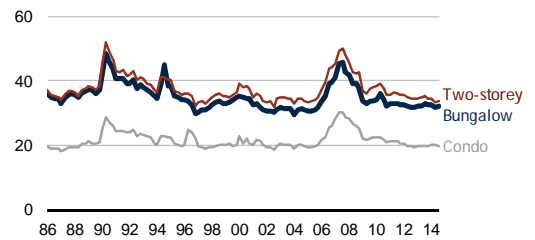
### Manitoba – Surging listings supersede solid demand

Highly motivated buyers drove up home sales to a new record level for a third quarter in Manitoba in the most recent period. While this impressive feat would normally qualify as the main headline, it was superseded by even higher heights attained in the supply of homes available for sale in the province. New listings, which have been on a steep incline since last year, showed a very strong year-over-year increase of 13% in the third quarter of 2014 as they reached their highest level since 1995. The sharp rise in new listings coincided with a wave of completions of new housing units in the Winnipeg area in the latter part of 2013 and early part of 2014. Consequently, despite robust resale activity, demand-supply conditions continued to loosen in the Manitoba market in the third quarter, thereby causing prices to decelerate further in most categories. Housing affordability predominantly improved in the latest period, much as has been the case since the middle of

## RBC Housing Affordability Measures

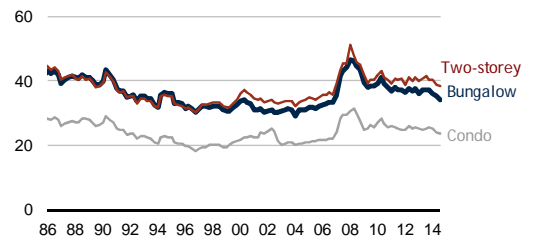
### Alberta

Ownership costs as % of household income



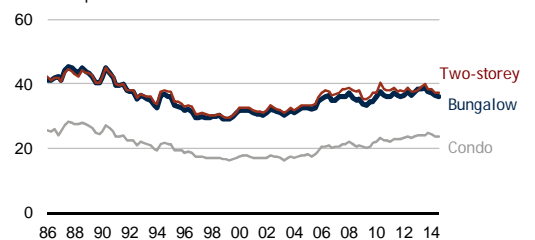
### Saskatchewan

Ownership costs as % of household income



### Manitoba

Ownership costs as % of household income

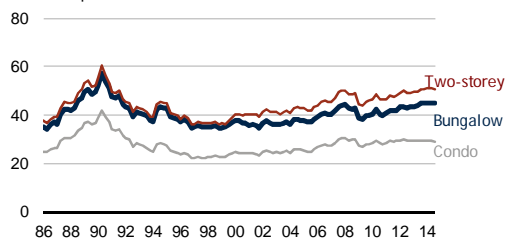


Source: Statistics Canada, Royal LePage, RBC Economics Research

## RBC Housing Affordability Measures

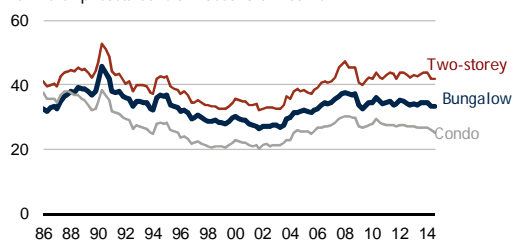
### Ontario

Ownership costs as % of household income



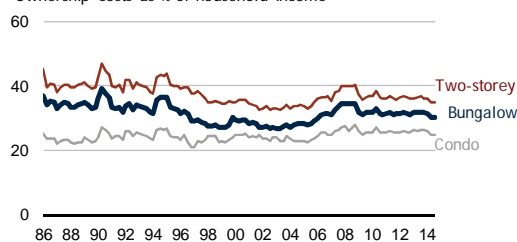
### Quebec

Ownership costs as % of household income



### Atlantic Provinces

Ownership costs as % of household income



Source: Statistics Canada, Royal LePage, RBC Economics Research

2013. RBC's measures for bungalows and condo apartments fell by 0.4 percentage points and 0.2 percentage points, respectively, while the measure for two-storey homes increased by 0.2 percentage points.

### Ontario – Not ready to pack it in, as affordability improves slightly

Ontario's home resale market recorded its second-best third quarter ever in the latest period, clearly demonstrating that it is by no means ready to pack it in. Homebuyer demand continues to be bolstered by low mortgage rates, generally positive economic conditions, and, especially, still-rapid population growth in major urban centres (which attract large shares of immigrants). At the margin, homebuyers benefited from some modest improvement in housing affordability in the past two quarters (four quarters in the case of condo affordability), although affordability still appears to be moderately strained in the province—mostly in the Toronto area. In the third quarter, there was some small relief arising from a drop in utility costs. This drop, along with income gains, more than offset the effect of further property appreciation and contributed to RBC's measures edging lower across all housing categories. The measures fell between 0.1 percentage points and 0.4 percentage points.

### Quebec – Housing activity perks up...finally

Housing market activity remained historically soft in Quebec but picked up noticeably in the third quarter. After reaching a five-year low at the start of 2014 and posting a modest increase of 0.8% in the second quarter, home resales rose by 6.5% in the third quarter, which was the biggest quarterly advance in three years. This gain helped to narrow the gap between realised sales and the 10-year average to 2.3% from 8.2% in the second quarter. Housing affordability continued to improve for the most part in the province, reaching the most attractive levels in years. RBC's measures eased by 0.8 percentage points to 25.0% for condo apartments and by 0.4 percentage points to 41.6% for two-storey homes. The measure for bungalows remained unchanged at 33.4%. In the case of the condo segment, the decline was the fourth in a row and reflected downward pressure being exerted on prices. The provincial market faces a plentiful supply of condos at this stage, in part due to a sharp increase in new unit completions this year.

### Atlantic – Rebound in resales reverses part of a two-year slide

Atlantic Canada's residential real estate market emerged from a 10-year low in the third quarter. Home resales increased by 9.2% in the region, which was the strongest quarterly advance since the first quarter of 2007, with hefty gains registered in Moncton (28%), Saint John (22%), Fredericton (21%), and Halifax (12%). Nonetheless, the third-quarter pick-up in activity reversed less than half the 20% slide that took place between early 2012 and early 2014 in the region. During that period, demand-supply conditions loosened quite noticeably in several local markets, thereby causing prices to slow down to a crawl or even decline in some areas. Meanwhile, housing affordability continues to be generally favourable to homebuyers in Atlantic Canada. RBC's measures for the region have been below long-term averages for all housing categories for some time now and are still among the lower measures in the country. The

measure for bungalows eased further by 0.3 percentage points in the third quarter; however, the measures for two-storey homes and condo apartments edged slightly higher by 0.1 percentage points and 0.2 percentage points, respectively.

## Major city markets

### Vancouver – Resales rise above 10-year average despite affordability deterioration

Severely strained affordability conditions have been a reality for nearly a decade now in the Vancouver-area market and do not appear to be a factor holding back homebuyers in any significant way. Despite wide swings in home resale activity since 2008, the market consistently proved to be resilient by recovering from each downturn. Such continues to be the case in the third quarter, as Vancouver-area resales rose above the 10-year average for the first time since early 2011, thereby reversing the substantial drop that took place during 2011 and 2012. The current upswing tightened the demand-supply equation to the point that sellers once again hold the upper hand in setting prices. This year, Vancouver returned to being among the markets showing the stronger price increases in Canada. Faster property appreciation necessarily applies further pressure on already-poor affordability, although the effect was more than offset earlier this year by declines in fixed-mortgage rates. In the third quarter, however, mortgage rates remain static and affordability deteriorated across the board in the Vancouver area. RBC's measures rose between 0.4 percentage points and 1.6 percentage points.

### Calgary – Housing boom continues, unimpeded by affordability issues

The boom continues in the Calgary-area market with home resales setting back-to-back quarterly record highs in the past two quarters. While homebuyer demand has been strong and rising for some time in the area, the latest leg-up in activity may be attributed to a sharp increase in new listings (up 17% cumulatively in the second and third quarters), which eased some of the supply constraints that buyers faced earlier. Nonetheless, despite this rise in new listings, demand still outweighs available supply in the area (albeit just modestly less so than earlier this year). This situation maintains a strong bid on home prices. Calgary prices continue to rise at the fastest pace in Canada (between 9% and 12% year over year depending on the housing type). Housing affordability deteriorated in the third quarter; however, it remained quite attractive from a historical perspective and in comparison to other Canadian cities. Affordability is being preserved by the high and rising levels of household income in the area.

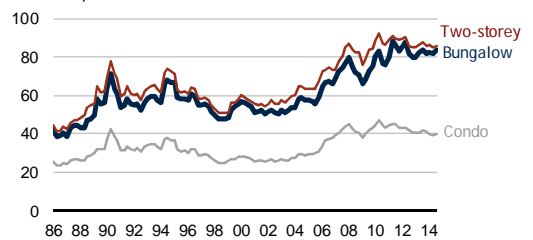
### Toronto – Ownership bar still high but market keeps on rolling

Toronto saw some respite from the deteriorating trend in affordability in the third quarter; however, owning a home—especially a single-detached home—at market price still appears to be a stretch for a typical household in the area. RBC's measures fell by 1.1 percentage points for two-storey homes and by 0.2 percentage points for condo apartments in the latest period, while the measure for bungalows rose by 0.3 percentage points. Despite the improvement in two of the measures, affordability still compares unfavourably to levels that pre-

## RBC Housing Affordability Measures

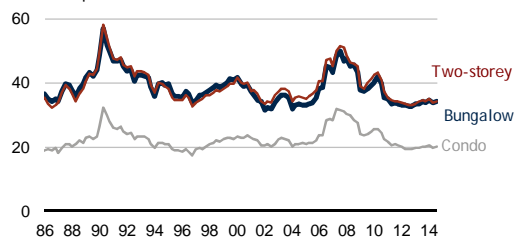
### Vancouver

Ownership costs as % of household income



### Calgary

Ownership costs as % of household income



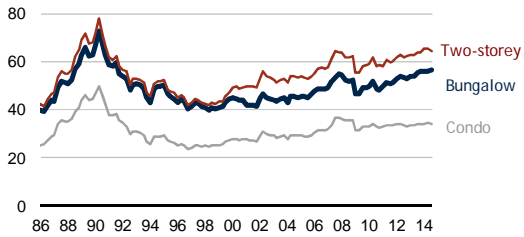
Source: Statistics Canada, Royal LePage, RBC Economics Research



## RBC Housing Affordability Measures

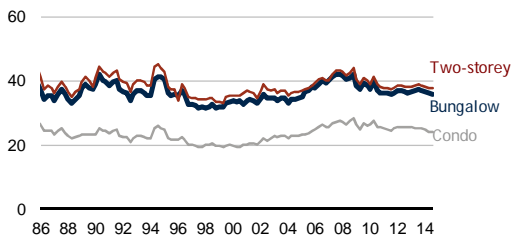
### Toronto

Ownership costs as % of household income



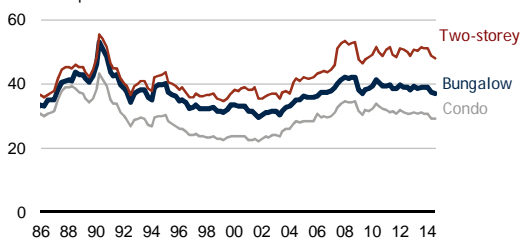
### Ottawa

Ownership costs as % of household income



### Montreal

Ownership costs as % of household income



Source: Statistics Canada, Royal LePage, RBC Economics Research

vailed a year ago and, more importantly, to the long-run averages for the area. That being said, any affordability stress does not seem to bother homebuyers, however. Toronto-area home resales continued to power ahead in the third quarter, posting their second-best total ever for that period of the year. In fact, results might have been even stronger were it not for a small decline in new listings, which may have restrained activity in the quarter. The market remains tilted in favour of sellers, which is a condition that will likely sustain a solid pace of price increases in the near term.

### Ottawa – Market recovery continues while supply still plentiful

The Ottawa-area market continues to recover from the low point that it reached at the start of 2014. Home resales advanced by 2.9% in the third quarter, following a substantial gain of 5.7% in the second quarter. These back-to-back gains lifted the number of homes sold to 14,500 units (annualized) or slightly above the 10-year average for the area (14,200 units), which suggests that activity has returned to a normal level by now. The Ottawa market continues to face a plentiful supply of homes for sale; however, the demand-supply balance tightened slightly in the third quarter, thereby helping to curb the downward pressure on prices that has built up during the past year. Housing affordability has been on an improving trajectory since the middle of 2013, and a further improvement was registered in the latest period. RBC's measures fell modestly in all housing categories by between 0.1 percentage points and 0.3 percentage points. All measures currently stand slightly below long-run averages, thereby implying that housing affordability unlikely represents an obstacle to homebuyers at this juncture.

### Montreal – Initiating its long awaited comeback?

The Montreal-area market showed signs that it is finally emerging from its multi-year slump in the third quarter. Home resales picked up smartly in the latest period to their highest level in three years after reaching a decade-low level in the previous quarter. If this is indeed the start of a turnaround, then there remains considerable lost ground for which to make up, however. Despite the gain, the number of units sold in the third quarter was still more than 16% below the 10-year average for the period. At this stage, pricing conditions continue to be fairly soft. There is abundant supply relative to the current level of demand, especially in the condo segment where inventories are historically high. The upside of minimal price gains, however, is that housing affordability continues to improve in the area. RBC's measures decreased for the second-consecutive period for all housing types, declining by between 0.2 percentage points and 0.6 percentage points in the third quarter. The measures for bungalows and condo apartments now closely match their long-term norms in the area, thereby suggesting that affordability considerations are unlikely to interfere with the market's recovery in the near term.

## How the RBC Housing Affordability Measures work

The RBC Housing Affordability Measures show the proportion of median pre-tax household income that would be required to service the cost of mortgage payments (principal and interest), property taxes, and utilities on a detached bungalow, a standard two-storey home and a standard condo (excluding maintenance fees) at the going market prices.

The qualifier 'standard' is meant to distinguish between an average dwelling and an 'executive' or 'luxury' version. In terms of square footage, a standard condo has an inside floor area of 900 square feet, a bungalow 1,200 square feet, and a standard two-storey 1,500 square feet.

The measures are based on a 25% down payment, a 25-year mortgage loan at a five-year fixed rate, and are estimated on a quarterly basis for each province and for Montreal, Toronto, Ottawa, Calgary, Edmonton, and Vancouver-metropolitan areas. The measures use household income rather than family income to account for the growing number of unattached individuals in the housing market. The measure is based on quarterly estimates of this annual income, created by annualizing and weighting average weekly earnings by province and by urban area. (Median household income is used instead of the arithmetic mean to avoid distortions caused by extreme values at either end of the income distribution scale. The median represents the value below and above which lays an equal number of observations.)

The RBC Housing Affordability Measure is based on gross household income estimates and, therefore, does not show the effect of various provincial property-tax credits, which could alter relative levels of affordability.

The higher the measure, the more difficult it is to afford a house. For example, an affordability measure of 50% means that home ownership costs, including mortgage payments, utilities, and property taxes take up 50% of a typical household's pre-tax income.

Qualifying income is the minimum annual income used by lenders to measure the ability of a borrower to make mortgage payments. Typically, no more than 32% of a borrower's gross annual income should go to 'mortgage expenses'—principal, interest, property taxes, and heating costs (plus maintenance fees for condos).

## Summary tables

### Detached bungalow

Region	Average Price			Qualifying Income (\$) Q3 2014	RBC Housing Affordability Measure			
	Q3 2014 (\$)	Q/Q % ch.	Y/Y % ch.		Q3 2014 (%)	Q/Q Ppt. ch.	Y/Y Ppt. ch.	Avg. since '85 (%)
Canada*	402,100	1.5	5.9	81,800	42.6	0.1	-0.8	39.2
British Columbia	663,400	2.1	6.2	122,300	68.2	1.0	-0.9	50.8
Alberta	405,700	2.2	8.1	82,300	32.3	0.4	-0.5	35.1
Saskatchewan	341,900	-4.2	-3.2	71,600	34.1	-1.3	-3.1	36.0
Manitoba	313,300	-0.4	0.4	67,000	35.9	-0.4	-2.8	35.7
Ontario	436,700	1.5	6.8	90,100	44.7	-0.1	-0.1	40.3
Quebec	263,100	1.6	5.2	56,400	33.4	0.0	-0.9	33.3
Atlantic	223,500	-0.2	0.2	51,800	30.0	-0.3	-1.7	31.7
Toronto	628,900	2.4	8.7	122,200	56.3	0.3	0.7	48.8
Montreal	303,700	0.2	2.6	64,000	37.0	-0.3	-1.8	36.9
Vancouver	884,400	2.7	7.3	159,200	83.6	1.6	-0.3	60.5
Ottawa	404,400	0.4	1.2	89,100	35.7	-0.3	-1.5	36.4
Calgary	515,800	2.9	10.8	98,700	34.2	0.6	0.2	38.5
Edmonton	360,400	2.0	6.0	75,800	31.9	0.2	-1.2	33.3

### Standard two-storey

Region	Average Price			Qualifying Income (\$) Q3 2014	RBC Housing Affordability Measure			
	Q3 2014 (\$)	Q/Q % ch.	Y/Y % ch.		Q3 2014 (%)	Q/Q Ppt. ch.	Y/Y Ppt. ch.	Avg. since '85 (%)
Canada*	447,100	0.8	5.1	91,900	47.8	-0.2	-1.2	43.7
British Columbia	697,900	0.7	4.6	129,800	72.4	0.2	-1.8	56.0
Alberta	410,200	2.2	5.1	86,000	33.7	0.4	-1.3	37.6
Saskatchewan	381,200	-0.9	-1.7	80,500	38.3	-0.4	-3.0	37.4
Manitoba	323,600	1.7	1.5	69,400	37.2	0.2	-2.5	36.6
Ontario	490,100	0.7	7.1	101,800	50.5	-0.4	0.0	44.1
Quebec	330,100	0.3	3.1	70,300	41.6	-0.4	-1.8	39.9
Atlantic	252,600	1.5	0.6	60,200	34.9	0.1	-1.8	37.9
Toronto	709,400	-0.4	8.1	139,400	64.2	-1.1	0.5	54.5
Montreal	401,300	-0.1	0.2	82,900	47.9	-0.6	-3.4	42.6
Vancouver	896,400	0.9	4.8	162,900	85.6	0.4	-2.0	65.6
Ottawa	412,600	1.0	1.2	93,500	37.5	-0.1	-1.4	38.6
Calgary	499,800	2.1	9.2	98,800	34.3	0.4	-0.1	38.9
Edmonton	394,500	2.0	5.3	84,100	35.4	0.2	-1.6	36.5

### Standard condominium

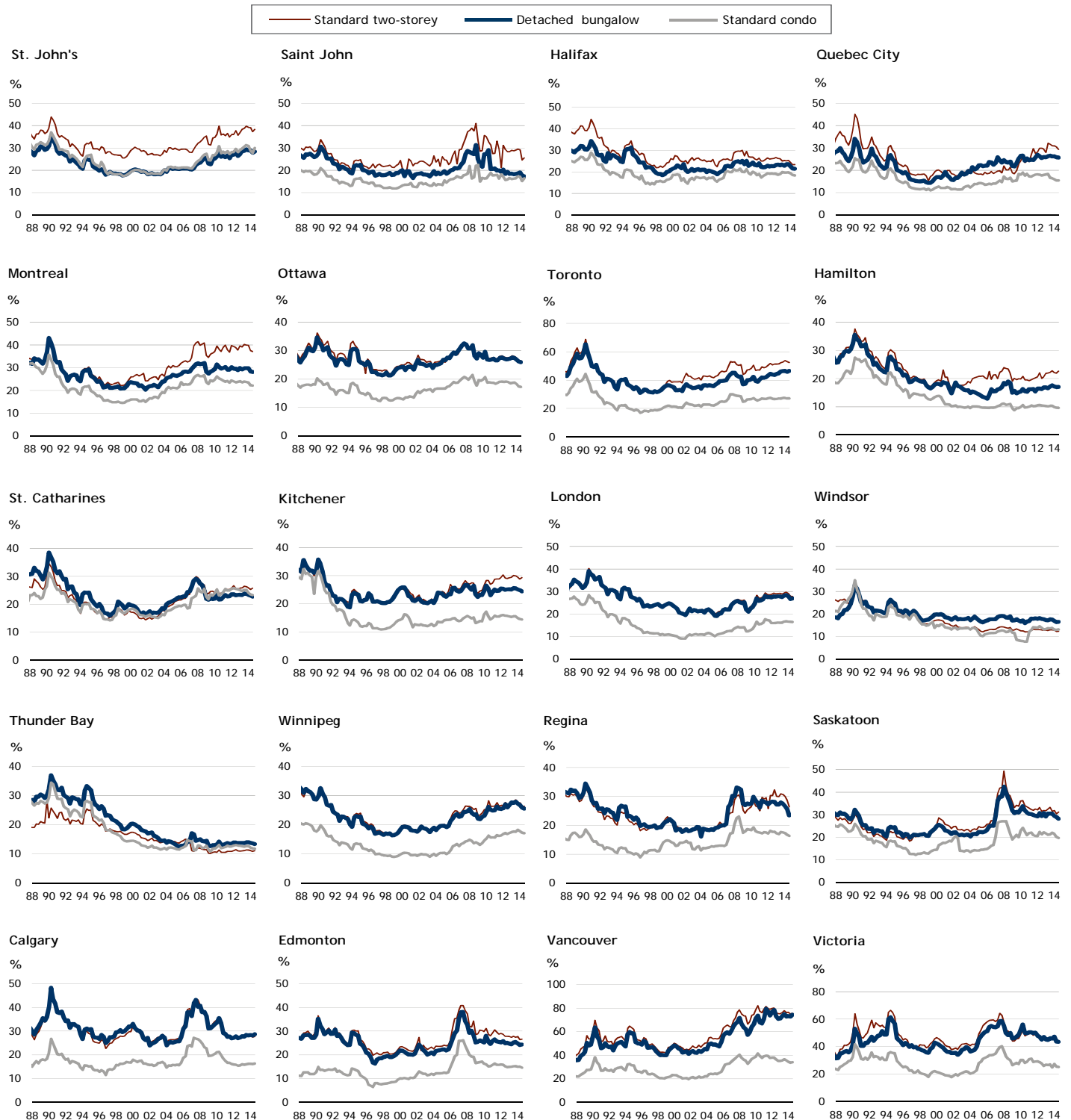
Region	Average Price			Qualifying Income (\$) Q3 2014	RBC Housing Affordability Measure			
	Q3 2014 (\$)	Q/Q % ch.	Y/Y % ch.		Q3 2014 (%)	Q/Q Ppt. ch.	Y/Y Ppt. ch.	Avg. since '85 (%)
Canada*	248,100	0.0	3.5	52,100	27.1	-0.3	-1.0	27.0
British Columbia	307,100	1.5	1.0	59,100	33.0	0.3	-1.8	28.5
Alberta	242,800	-0.9	11.0	50,700	19.9	-0.2	0.1	21.6
Saskatchewan	238,500	-1.5	0.9	50,000	23.8	-0.4	-1.4	24.0
Manitoba	210,100	-0.2	6.8	43,900	23.5	-0.2	-0.7	21.3
Ontario	275,000	0.7	4.8	58,600	29.1	-0.2	-0.5	27.6
Quebec	194,300	-2.6	-0.6	42,200	25.0	-0.8	-1.8	27.6
Atlantic	190,800	1.9	1.2	42,900	24.9	0.2	-1.2	24.5
Toronto	366,300	1.0	7.9	73,900	34.1	-0.2	0.3	31.3
Montreal	239,300	0.6	0.6	50,200	29.0	-0.2	-1.9	29.5
Vancouver	406,000	2.2	0.8	75,600	39.7	0.6	-2.3	33.0
Ottawa	268,800	0.2	-0.3	59,700	23.9	-0.2	-1.2	23.5
Calgary	294,200	2.7	11.8	58,100	20.1	0.3	0.2	22.3
Edmonton	216,300	-1.7	5.8	46,400	19.5	-0.4	-0.8	18.3

\* Population weighted average

Source: Royal LePage, Statistics Canada, RBC Economics Research

## Mortgage carrying costs by city

Our standard RBC Housing Affordability Measure captures the proportion of median pre-tax household income required to service the cost of a mortgage on an existing housing unit at going market prices, including principal and interest, property taxes and utilities; the modified measure used here includes the cost of servicing a mortgage, but excludes property taxes and utilities due to data constraint in the smaller CMAs. This measure is based on a 25% down payment, a 25-year mortgage loan at a five-year fixed rate, and is estimated on a quarterly basis. The higher the measure, the more difficult it is to afford a house.

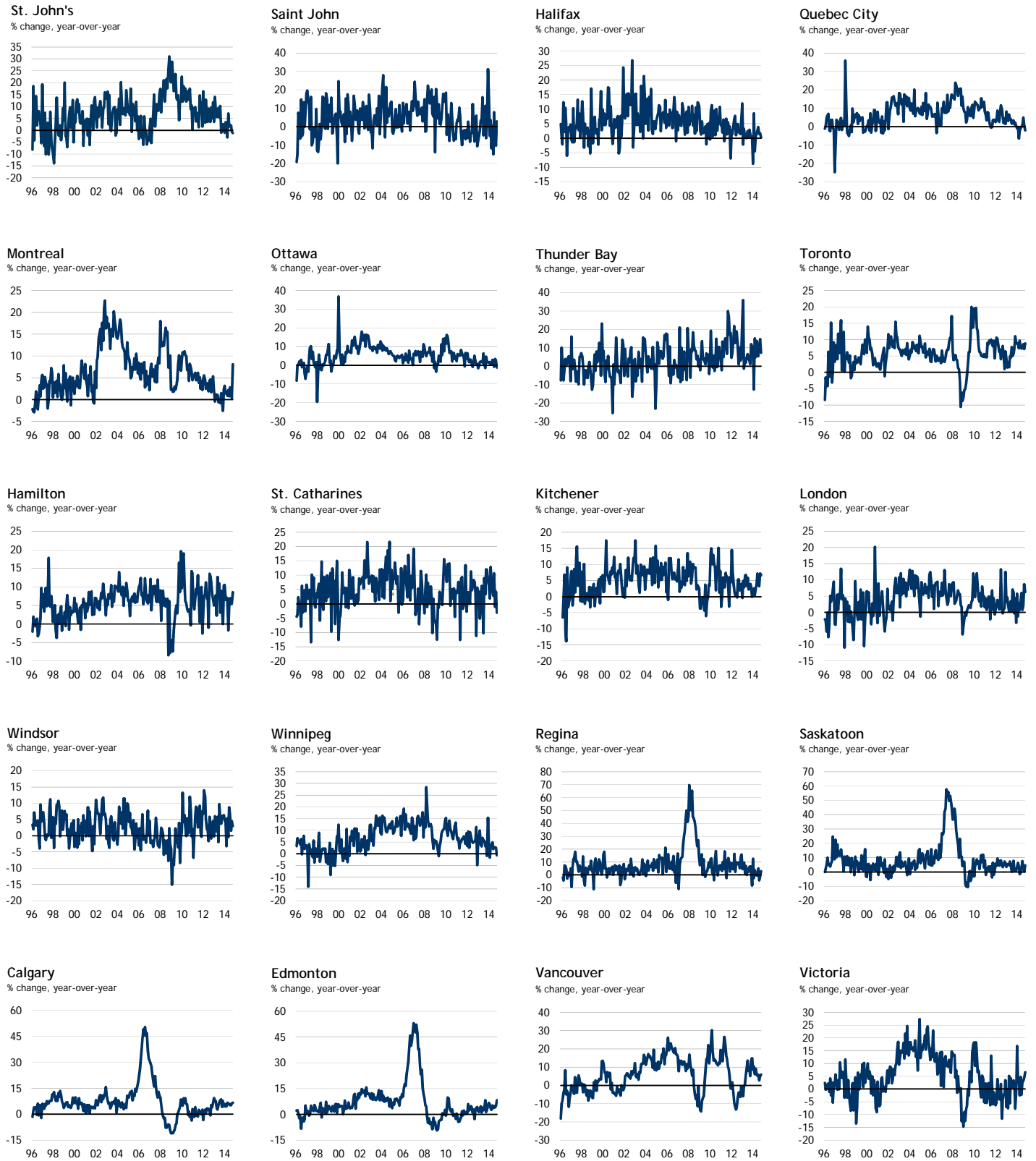


Source: Statistics Canada, Royal LePage, RBC Economics Research





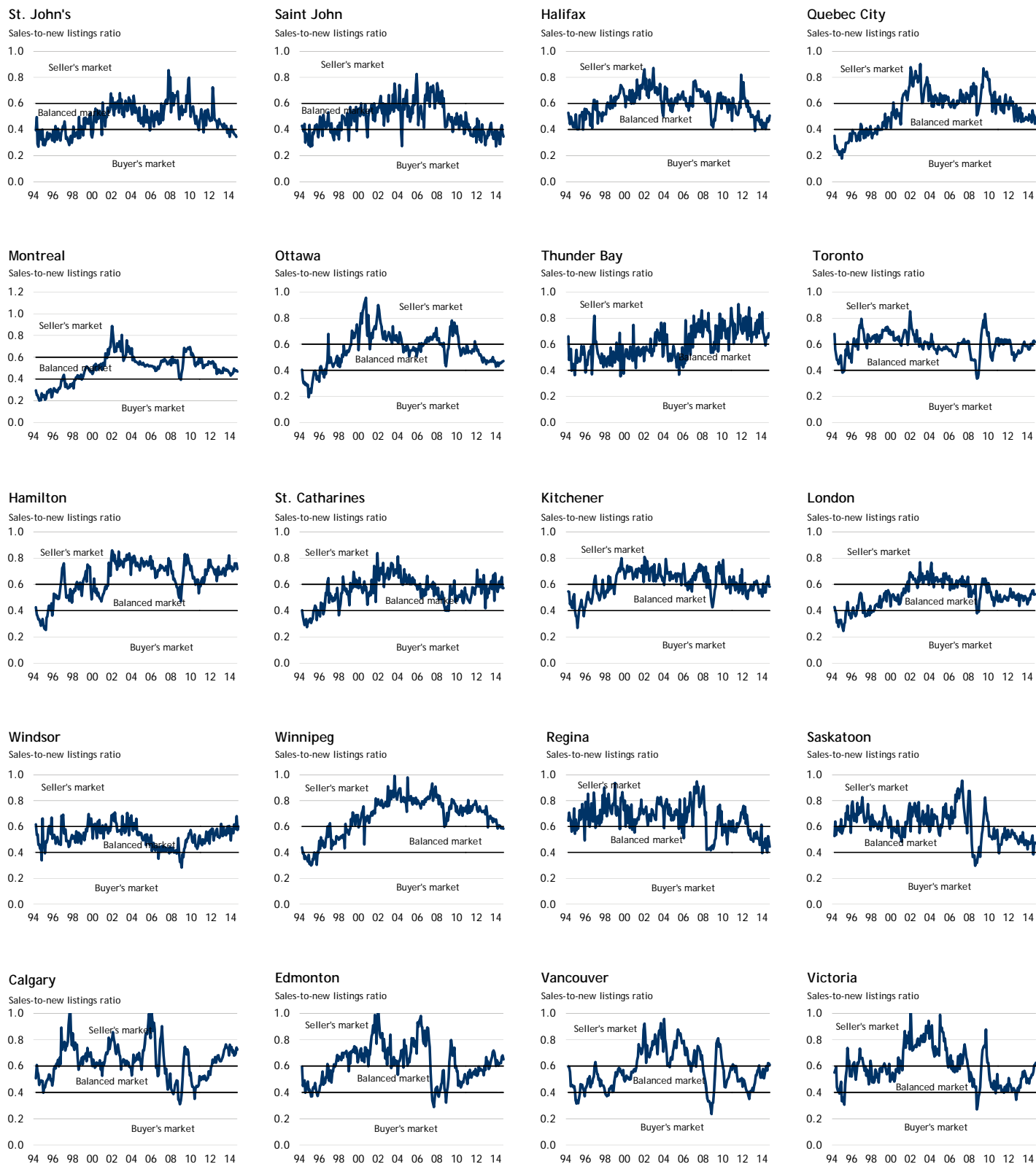
# Average price of homes sold on the MLS system



Source: Canadian Real Estate Association, RBC Economics Research



# Home sales-to-new listings ratio



Source: Canadian Real Estate Association, RBC Economics Research



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