MONTHLY HOUSING MARKET UPDATE

June 15, 2016

Home resales in Canada (finally!) slow down in May… but not prices

- The long-awaited cooling of Canada's housing market may be finally at hand. Home resale activity eased for the first time in five months in May 2016. The Canadian Real Estate Association (CREA) reported this morning that resales in Canada fell 2.8% in May to 544,500 units (seasonally adjusted and annualized) from April's all-time high of 560,300 units. Resales were still up solidly by 9.6% compared to a year ago.

- The encouraging news was that some of Canada's hottest markets led the decline. While the majority of local markets experienced a slowdown in May, the bulk of the monthly decline occurred British Columbia (down 4.9% from April) and Ontario (down 2.4%). Home resales fell for a third-consecutive month by 4.8% in the Vancouver area and by 7.7% in the Fraser Valley. Activity was little changed in the Toronto area (up by 0.4%) but fell in many other local markets in Ontario including Ottawa, Windsor and London.

- Activity improved slightly for a fourth-straight month in Calgary (with resales rising 1.6% from April); yet, it remained markedly weaker (down 11.3%) than it was a year ago.

- Elsewhere across the country, a number of markets recorded sizable monthly declines, including Halifax (-7.2%), Saskatoon (-6.7%) and Winnipeg (-3.8%). Regina (up 2.5%) and Montreal (up 1.2%) were among the few exceptions registering increases.

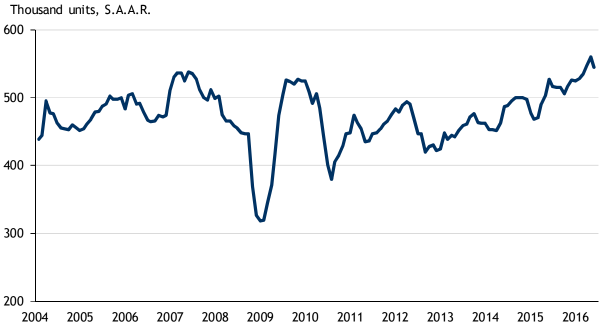
- The supply side continued to contract with new listings falling 3.2% in Canada, which reflected further widespread declines across local markets (including in Toronto, the Fraser Valley, Montreal, Calgary and Edmonton). New listings rose slightly for the second consecutive month in the Vancouver area.

- Despite the slowing in resales, home prices continued to rise strongly in Canada in May. The composite MLS Home Price Index (HPI) in fact further accelerated to an annual rate of 12.5% from 10.3% in April and 5.3% in May 2015. Of particular concern are the parabolic trajectories in Greater Vancouver and the Fraser Valley where the annual rate of increase in the MLS HPI has reached 29.7% and 31.7%, respectively. The Toronto area also showed an acceleration in the rate to 15.0% in May from 10.7% at the start of this year.

May Snapshot

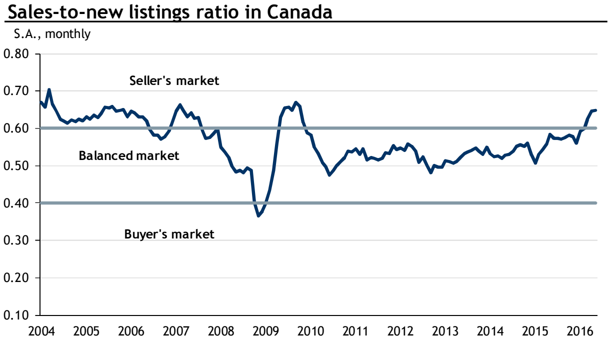
Region	Home resales Y/Y %change	New listings Y/Y %change	MLS HPI (Composite) Y/Y %change	Sales-to-new listings ratio
Canada	9.6	-4.1	12.5	0.65
Toronto	9.9	-6.9	15.0	0.76
Montreal	1.9	-10.4	1.9	0.56
Vancouver	18.5	12.4	29.7	0.77
Calgary	-11.3	6.6	-4.0	0.55

Home resales in Canada



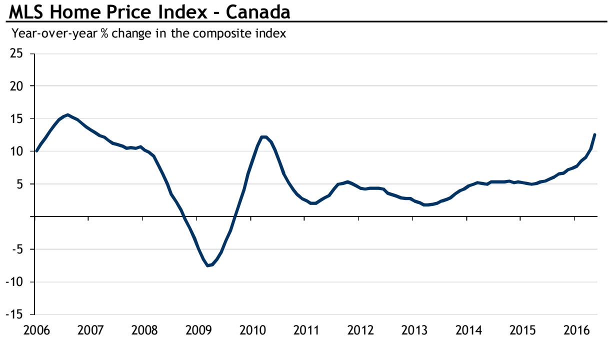
Source: CREA, RBC Economics Research

Sales-to-new listings ratio in Canada



Source: CREA, RBC Economics Research

MLS Home Price Index - Canada



Source: CREA, RBC Economics Research

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- With demand-supply conditions continuing to favour sellers heavily in Canada's 'hot' markets, it is unlikely that the price trajectories will change in the near term in Vancouver, the Fraser Valley and Toronto—as well as other vibrant markets such as Victoria and Hamilton.

A positive development…

It is not often that we cheer a decline in activity but the easing in home resales in May reported this morning should be seen as a positive development for Canada's housing market. There has been growing concerns that supercharged demand in a few areas—albeit pivotal markets or pockets within markets—in the context of constrained supply is overheating conditions to a dangerous degree. Therefore, any indications of a cooling in demand—or at least, a cooling in activity—in markets such as Vancouver and Toronto is a welcome tentative sign that the heat may be on its way to a more tolerable degree.

…but demand-supply conditions remain intensely tight

Still, significantly more cooling in demand is necessary in Vancouver (and the Fraser Valley) and Toronto to relieve the current intense upward pressure on prices in those markets. Alternatively, an increase in supply of homes for sale would do the trick; however, the recent trend has been the complete opposite: fewer and fewer current owners put their homes up for sale. This phenomenon has been quite puzzling to us—usually rising prices attract more sellers on the market—although, some analysts have conjectured that poor affordability likely represents a significant disincentive to move. We have long been of the view that intensifying affordability stress will be among the factors contributing to a 'soft landing' in Canada's housing market; however, we believed the effect would work itself primarily through the demand side (particularly weighing on demand from first-time buyers), and much less so on the supply side of the equation. If stretched affordability is indeed restraining supply, it would imply that the speed of rebalancing in those hot markets is likely to be slow—or at least, slower than would be the case if an increasing number of homes were listed for sale. If true, therefore, tight demand-supply conditions and rapid price increases in Vancouver and Toronto are likely to remain in the near term.

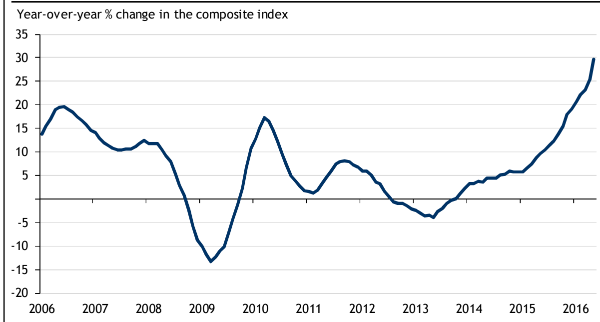
Situation stabilizing in Calgary?

While the current focus in housing trends in Canada is rightly on the 'hot' markets, we are encouraged to see in this morning's statistics that at the other end of the spectrum the situation in Calgary's market—which has been severely challenged by the downturn in the energy sector and the provincial recession—appears to have stabilized in the past few months. Home resales have risen for four consecutive months (albeit from very low levels) and the sales-to-new listings ratio has picked up and suggests more balanced conditions. Home prices continued to fall in May—the MLS HPI was down 3.9% relative to a year ago—however, there is reason to believe that the pace of decline may moderate in the period ahead if activity continues to rebound.

Set for a record year in 2016

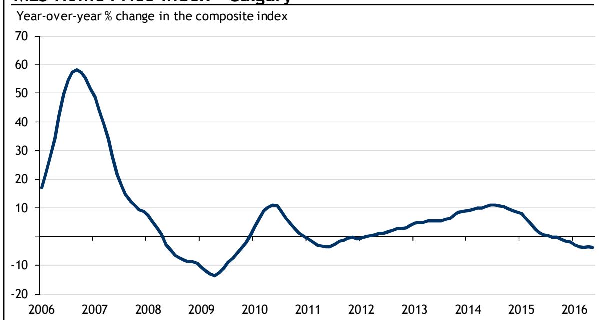
Strong activity to date—resales averaging slightly less than 543,000 units on an annualized basis in the first five months of this year—has set a path to record-high home resales in Canada in 2016. We have revised our forecast for the year accordingly to 551,000 units, which assumes a partial rebound from the decline in May during the second half of this year. Such a level would constitute a solid 9.0% increase from 2015. We see booming activity in British Columbia as the main driver of this increase,

MLS Home Price Index - Vancouver



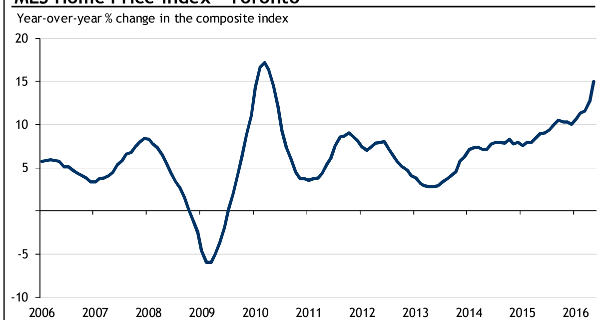
Source: CREA, RBC Economics Research

MLS Home Price Index - Calgary



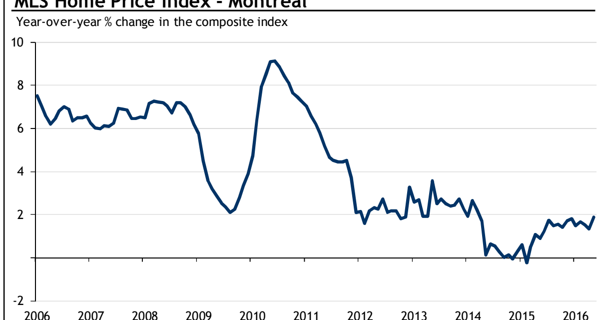
Source: CREA, RBC Economics Research

MLS Home Price Index - Toronto



Source: CREA, RBC Economics Research

MLS Home Price Index - Montreal



Source: CREA, RBC Economics Research

with solid gains in Ontario, Manitoba and Quebec also contributing. We expect the downturn in Alberta and Saskatchewan to continue, thereby resulting in a second-straight annual decline in home resales for both provinces. We project home prices to rise by 5.0% nationally in 2016—matching the rate of increase in 2015—lifted mainly by a surge in British Columbia and a solid advance in Ontario, which would more than offset modest declines in Alberta and Saskatchewan.