Canadian home resales inched higher in September despite cooling Vancouver market; rate of price increases steadied

- The ‘landing’ of Canada’s home resale market took a pause in September as a modest pickup in activity in a majority of local areas more than offset a further weakening in BC markets.

- This pause is likely to be temporary, however, because we expect the new measures announced by Finance Minister Bill Morneau of October 3 will have a dampening effect on home resales across the country in the coming months.

- In fact, we believe that the new measures—that include more stringent and uniform qualifying rules for mortgage insurance across mortgage types—will both speed up and harden the landing that we previously expected to occur in the year ahead, although they are unlikely to cause a ‘crash’.

- The statistics published this morning by the Canadian Real Estate Association showed that home resales in Canada rose in September for the first time in five months, and that the annual rate of increase in benchmark prices edged downward for the first time in 19 months despite demand-supply conditions remaining slightly favourable to sellers overall.

- This morning’s report confirmed that the Vancouver-area market continued to be in a cooling phase; however, the pace of cooling was revealed to have moderated significantly from the sharp declines in activity observed in July and August. This suggests to us that the impact from the tax on foreign buyers (implemented on August 2) has begun to taper off.

- The report also confirmed that the Toronto-area market remained very strong in September with record-high sales and still-accelerating prices.

- The picture emerging from the September statistics is in line with our earlier assessment that Canada’s housing market is down to only one major ‘heat source’—Toronto—with Vancouver now quickly losing some of its heat.

- While we expect this picture generally to hold in the near term, the new measures announced on October 3 will take centre stage in the coming months and we will be monitoring their market impact very closely. The new measures pose material downside to our current forecast for resales and, to a lesser extent, prices.
Canada’s housing market took a pause from earlier declines
Home resales rose slightly by 0.8% to 529,200 units (seasonally adjusted and annualized) in Canada from August to September, thereby representing the first increase in five months. Widespread gains across local markets (including Toronto, Montreal, Calgary, Edmonton, Halifax and Ottawa) more than offset further declines in BC markets. Relative to a year ago, national home resales were up by 4.2% in September, which represents a slowing from the 10.2% rise recorded in August. The rate of price increases stabilized at the national level after accelerating steadily since the end of 2014. The composite MLS Home Price Index (HPI) rose by 14.4% year-over-year in September, down marginally from 14.7% in August. This was the first decline in 19 months despite demand-supply conditions remaining slightly favourable to sellers overall.

Vancouver market continued to cool
The Vancouver area saw a seventh-straight monthly drop in resales in September, although the rate of decline (-1.7%) moderated significantly from the -9.3% and -18.8% plunges registered in July and August, respectively. This may be evidence that most of the impact on activity from the surprise introduction of a 15% tax on purchases by foreign nationals occurred in August. Despite the small ressale decline in September, demand-supply conditions remained balanced in the area (sales-to-new listings eased only slightly from 0.56 in August to 0.54 in September); yet, benchmark prices (composite MLS HPI) fell month-over-month by 0.7% for the first time in nearly three years. Relative to a year ago, the Vancouver-area benchmark price was still up sharply by 28.2% in September, although this represented a slowing in the pace from a recent high of 32.6% in July. We expect further moderation in the period ahead.

Toronto setting more records
Home resales set yet another record high in the Toronto-area market in September, rising 3.1% in the month to 118,600 units (annualized). The gain was facilitated by an increase of 2.0% in new listings. The demand-supply balance continues to be heavily tilted in favour of sellers in the area. Benchmark prices accelerated further to a rate of 18.0% year-over-year in September from 17.2% in August.

Alberta markets rebounding partially…
Activity in Alberta markets rebounded partially in September from sizable declines in August. Home resales rose by 3.8% in Calgary and by 7.1% in Edmonton in September, following declines of 4.0% and 8.5% in August, respectively. The Calgary market recorded its first year-over-year resale increase (2.7%) in almost two years. Benchmark prices continued to decline, however.

…with most other markets showing gains
Elsewhere across Canada, most other markets posted monthly sales increases in September, including Halifax (4.9%), Ottawa (1.8%), Montreal (1.3%), Regina (1.0%) and Winnipeg (0.9%). The majority of markets remained balanced. Saint John (-19.0%) and Saskatoon (-4.8%) were among the few markets that registered a monthly decline, as buyers in both areas continued to hold a strong hand on prices.

Bigger news came on October 3, when tighter mortgage insurance rules were announced
In terms of implications for the way ahead, we believe that the more significant development has been the new measures announced on October 3 by Federal Finance Minister Bill Morneau (see our commentary for details). Among these new measures will be a rise in the interest rate
used to qualify high-ratio mortgage borrowers (borrowers with a down payment of less than 20%) opting for a fixed rate with a term of five years or more. This change, effective October 17, will affect the largest segment of Canada’s mortgage market. In addition, new, stricter standards for mortgage portfolio insurance that will kick in at the end of November will have a dampening effect on new conventional (low-ratio) mortgages issued by some financial institutions. We estimate that roughly one-in-five housing sales could be affected by these changes, although we expect a proportion of exposed borrowers will still have the ability to qualify, thereby minimizing any decline in sales. We expect the impact from these new rules to be immediate.

**The new rules temper the outlook for the housing market**

The new measures announced on October 3 pose material downside risks to our forecast for home resales and, to a lesser degree, prices for 2017. The new measures are likely to both speed up and harden the ‘landing’ in our base case scenario for Canada, although they are unlikely to cause a ‘crash’. We believe that the dampening effects will be felt in all regions of the country. Our preliminary estimates show a projected decline of nearly 11% in home resales in Canada in 2017 compared to our previous forecast for a 3.7% decline, and a small price decline of 0.2% compared to a rise 2.0% previously. We will firm up our forecast shortly.