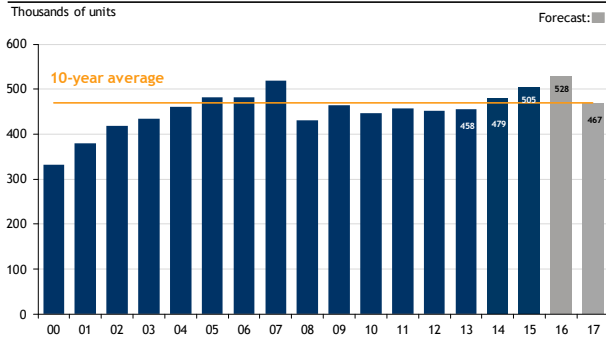


## CANADIAN HOUSING FORECAST

November 7, 2016

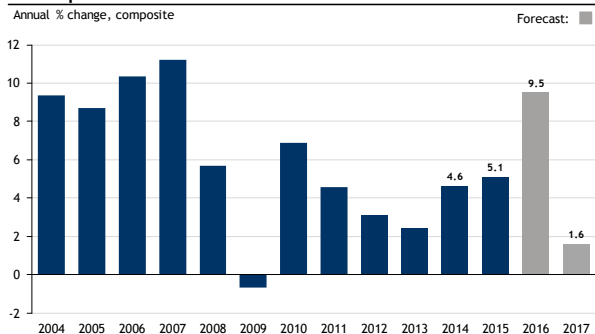
### Policy-engineered cooldown to dampen resales and curb price increases in 2017

#### Home resales: Canada



Source: Canadian Real Estate Association, RBC Economics Research

#### Home prices in Canada



Source: Brookfield RPS, Royal LePage, CREA, RBC Economics Research

**Robert Hogue**  
Senior Economist  
(416) 974-6192  
robert.hogue@rbc.com

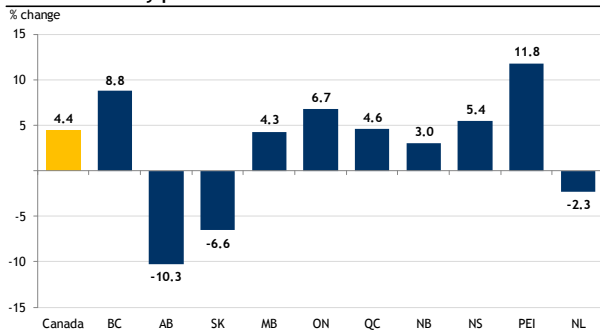
- We expect that new policy measures at both the federal and provincial levels aimed at addressing housing market risks will have cooling effect across Canada in the months ahead.
- We have revised our forecasts for home resales and prices for the coming year accordingly. Nationally, our updated base case calls for a decline of 11.5% in home resales and modest increase of 1.6% in the benchmark price in 2017, following solid advances of 4.4% and 9.5% in 2016, respectively.
- Our working assumptions are that the tightening of mortgage insurance criteria set forth by the federal government on October 3, 2016, will dampen home resales by close to 8% relative to our previous baseline and slow the pace of price increases by approximately 0.5 percentage points in Canada in 2017. Our base case scenario also assumes that the impact will vary across the country—with the more significant effect on home resales being felt in high-priced markets in Ontario and British Columbia.
- We project home resales to fall in all provinces in 2017 with declines ranging from less than 3% in Manitoba to approximately 24% in British Columbia. Still, we expect benchmark prices to continue to rise (on an annual basis) in the majority of provincial markets except Newfoundland and Labrador, Alberta and Saskatchewan. Continued property value appreciation in most provinces in part would reflect broadly supportive demand-supply conditions going into this period of softening sales.
- In British Columbia, we believe that the policy changes introduced by the provincial government since the spring—including the implementation of a 15% tax on purchases by foreign nationals in Metro Vancouver on August 2, 2016—will contribute to the significant drop in home resales that we project for 2017 from record levels in 2016; however, other factors such as overstretched housing affordability in the Vancouver area also will play a significant role.
- While we downgraded our housing market outlook, we remain of the view that our base case scenario would qualify as a soft landing posing little threat to the stability of the market, even in British Columbia.
- There is an unusually high degree of risk around this outlook, however, both on the downside and on the upside. Much of this uncertainty stems from the difficulty to gauge the market's reaction to the new policy measures, as well as the potential for further policy intervention to cool the market—we assume none at the present time.

**Forecast assumptions**

%, unless specified otherwise

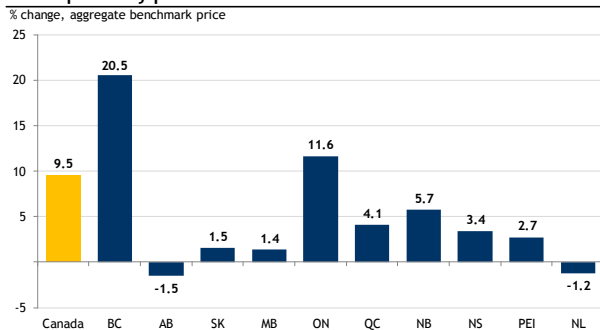
	2015	2016f	2017f
BoC overnight rate (year-end)	0.50	0.50	0.50
5-year bond yield (year-end)	0.73	0.75	1.35
Population growth (y/y)	0.9	1.2	1.1
Oil prices (WTI, avg. US\$/bbl)	49	44	56
<b>Unemployment rate</b>			
Canada	6.9	7.0	6.8
British Columbia	6.2	6.1	5.8
Alberta	6.0	7.9	7.5
Saskatchewan	5.0	6.4	6.5
Manitoba	5.6	5.9	5.7
Ontario	6.8	6.5	6.1
Quebec	7.6	7.3	7.2
Atlantic	10.0	10.1	10.3

**Home resales by province - 2016**



Source: Canadian Real Estate Association, RBC Economics Research

**Home prices by province - 2016**



Source: Brookfield RPS, RBC Economics Research

**2016 shaping up to be a banner year for Canada’s housing market**

Housing market activity has been brisk so far in 2016 despite moderating this spring and summer from record-high levels this past winter. Home resales in Canada were up strongly by 7.7% in the first nine months of 2016. We expect the remaining months of 2016 to show a marked decline, however, due to the ongoing cooling in the Vancouver market and dampening effect of new measures announced by the federal government in October across markets in Canada (more on this below). We project that home resales will increase by 4.4% to an all-time high of 527,900 units nationally in 2016. We expect hefty annual gains in Prince Edward Island (11.8%), British Columbia (8.8%) and Ontario (6.7%)—all three provincial markets are poised to set new records. Sales in Manitoba (14,600 units) also are headed toward a new historical mark. We project declines in Alberta (-10.3%), Saskatchewan (-6.6%) and Newfoundland and Labrador (-2.3%), where economic downturns significantly hamper activity.

**Big leaps in home prices recorded in BC and Ontario markets**

Diverging demand-supply conditions have produced a wide range of price outcomes across local markets in Canada in 2016; however, it has been the rapid appreciation in Vancouver, Toronto and their surrounding regions that has dominated the national measure. The overall benchmark price in Canada is on pace to rise by a very strong 9.5% in 2016, which would represent the biggest advance in nine years. Led by ballooning property values in the Vancouver area, we expect the BC benchmark to post a giant 20.5% leap from 2015. Similarly, fueled by outsized increases in the Toronto area, we expect the Ontario benchmark to climb by a 27-year high rate of 11.6%. Elsewhere across the country, price changes are much more subdued. We expect small to moderate gains in New Brunswick (5.7%), Quebec (4.1%), Prince Edward Island (2.7%), Saskatchewan (1.5%) and Manitoba (1.4%), and small declines in Alberta (-1.5%), and Newfoundland and Labrador (-1.2%).

**Macroeconomic landscape still generally supportive in 2017;...**

Looking ahead, our base case scenario for Canada’s economy should provide support to housing demand in this country in 2017. Interest rates are likely to remain low—we expect that the Bank of Canada will leave its overnight rate unchanged at 0.50% throughout 2017 and longer-term bond yields to drift modestly higher—and growth in the economy to be sustained, thereby contributing to a modest strengthening of labour market conditions. We expect the economic situation will begin to improve in Alberta and Saskatchewan (although not in Newfoundland and Labrador where we project a fourth-consecutive year of contraction), which would boost homebuyer confidence in these provinces.

**...however, policy-engineered dampening is bound to rule the day**

Nonetheless, despite a generally constructive macroeconomic landscape, we project home resales to decline moderately in Canada and price increases to slow down significantly in 2017. Overstretched affordability conditions in Canada’s most expensive markets are poised to restrain homebuyer demand—especially if longer-term interest rates rise as we expect—however, we see recent policy action as the bigger factor at play. Importantly, we expect rule changes at the federal level will have a dampening effect on home buying activity across all provinces, not just for Canada’s hot markets.

**New mortgage insurance rules to reduce resales by about 8%**

We estimate that the more stringent criteria for mortgage insurance announced by Finance Minister Bill Morneau on October 3, 2016—which include a rise in the interest rate used to qualify high-ratio mortgage borrowers opting for a fixed rate with a term of five years or more (effective October 17, 2016) and stricter standards for mortgage portfolio insurance (effective November 30, 2016)—could affect buyers in

about one in five sales in Canada. Of these buyers (who are predominantly in the market for the first time), we assume that between one-third and one-half no longer will qualify for a mortgage on the same terms and amounts as they would have been entitled prior to the changes. At this admittedly very early stage, we peg the impact of these new mortgage insurance rules on home resales to be a decline of roughly 8% nationwide relative to our previous baseline.

**BC government also is intent on cooling the Vancouver-area market**

In addition to policy measures at the federal level, there have been a number of policy moves taken this year by the BC government specifically to address affordability issues and housing market risks in the Vancouver area. These moves include a rejigging of the property transfer tax on newly built homes, the collection of data on foreign buyers (which began in early June 2016), the end of self-regulation for the province’s real estate industry, and the introduction of a new 15% tax on purchases by foreign nationals on August 2, 2016. These moves already have contributed to a significant decline in home resale activity since an all-time high was set this past winter in the province. We believe that, collectively, they constitute a strong signal to both buyers (including speculators) and sellers that the BC government is intent on cooling the Vancouver market down. We expect that this signal will continue to reverberate loudly during most of 2017 and, in conjunction with federal measures, will bring about a substantial decline of 23.8% in home resales and moderation in price increases to just 1.9% in the province next year.

**Home resales projected to fall by 11.5% in Canada in 2017,...**

After generating much of the heat at the national level in the past two years, we expect the BC market—and more specifically, the Vancouver-area market—will be a major source of cooling for activity nationwide in 2017. We project home resales to fall by 11.5% next year in Canada with almost half of this decline occurring in British Columbia. That being said, we expect the dampening effects of the federal measures announced recently to cause home resales to drop in all provincial markets, with declines ranging from 2.7% in Manitoba to 21.1% in Prince Edward Island (among provinces other than British Columbia). Our base case scenario calls for a third-consecutive year of decline in Alberta (-5.1%), and the first drop in five years in Ontario (-10.6%) and the first in three years in Quebec (-4.0%).

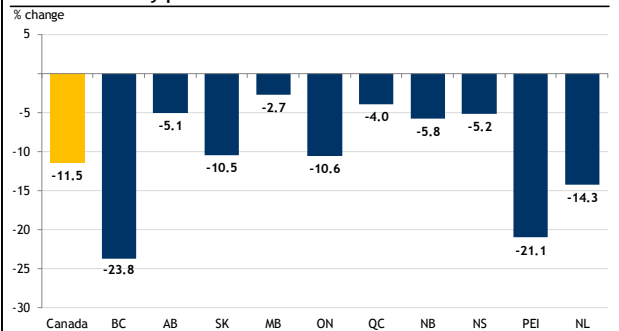
**...causing prices to increase at a much slower rate of 1.6%**

In turn, we expect that weakening resale activity will erode sellers’ pricing power; yet, for the national and majority of provincial (and local) markets we do not project prices to fall outright (on an annual basis) because we expect demand-supply conditions to remain balanced next year. Rather, our base case for 2017 shows benchmark prices continuing to rise at much slower rates. For Canada, we forecast the benchmark price to increase by only 1.6% in 2017 (compared to 9.5% in 2016). Our outlook for prices calls for a 3.0% rise in Ontario (which would represent the weakest rate in eight years in that province) and a 1.2% advance in Quebec. On the other hand, we expect three provincial markets—Alberta, Saskatchewan, and Newfoundland and Labrador—will be characterized by demand-supply conditions tilted in favour of buyers, thereby leading benchmark prices to fall outright next year. In the case of both Alberta, and Newfoundland and Labrador, this would be the second-straight annual price drop; and in the case of Saskatchewan, this would be the second decline in three years.

**Unusually high degree of uncertainty**

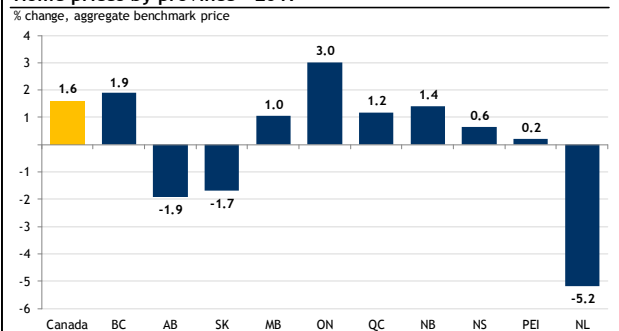
Forecasting Canada’s housing market is particularly difficult at this juncture given the central role that policy is playing and likely to continue to play in the period ahead. Thus, we see substantial risks to our

**Home resales by province - 2017**



Source: Canadian Real Estate Association, RBC Economics Research

**Home prices by province - 2017**



Source: Brookfield RPS, RBC Economics Research

base case, both on the upside and on the downside. First, the near-term impact of recent policy measures may be overstated although also potentially understated. Earlier rounds of mortgage insurance rule tightening in Canada provide only partial guidance for assessing the current episode because, among several contrasting factors, we do not expect interest rates to fall to soften the blow this time around—such that we will be in largely uncharted territory. And second, the potential for further policy intervention continues to be higher than usual at all levels of government and across all regulatory bodies. There are genuine concerns being expressed by policymakers and regulators about affordability in a number of ‘hot markets’ and the longer-term financial health of households which could well prompt additional measures. Unfortunately, we are largely in the dark about 1) what the policy trigger points are and 2) what tools or remedy would be put forward. For instance, it is entirely unclear to us what an acceptable ‘housing affordability level’ is for policymakers in expensive markets such as Vancouver and Toronto, which makes it challenging to assess the progress and success of measures undertaken. Our base case scenario assumes no further policy action. We will continue to monitor housing market developments closely and stand ready to revise our outlook as necessary.

Home resales forecast (units)												
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016f	2017f
Canada*	482,000	519,700	430,400	464,200	445,600	457,300	452,200	455,400	479,300	505,500	527,900	467,100
	<i>-0.2</i>	<i>7.8</i>	<i>-17.2</i>	<i>7.9</i>	<i>-4.0</i>	<i>2.6</i>	<i>-1.1</i>	<i>0.7</i>	<i>5.2</i>	<i>5.5</i>	<i>4.4</i>	<i>-11.5</i>
British Columbia	96,700	102,800	68,900	85,000	74,600	76,700	67,600	72,900	84,000	102,500	111,500	85,000
	<i>-9.0</i>	<i>6.3</i>	<i>-33.0</i>	<i>23.4</i>	<i>-12.2</i>	<i>2.8</i>	<i>-11.9</i>	<i>7.8</i>	<i>15.2</i>	<i>22.0</i>	<i>8.8</i>	<i>-23.8</i>
Alberta	74,000	71,000	56,000	57,500	49,700	53,800	60,400	66,100	71,800	56,500	50,700	48,100
	<i>13.0</i>	<i>-4.1</i>	<i>-21.1</i>	<i>2.7</i>	<i>-13.6</i>	<i>8.2</i>	<i>12.3</i>	<i>9.4</i>	<i>8.6</i>	<i>-21.3</i>	<i>-10.3</i>	<i>-5.1</i>
Saskatchewan	9,500	12,500	10,400	11,100	10,900	13,100	13,800	13,500	13,700	12,200	11,400	10,200
	<i>9.2</i>	<i>31.6</i>	<i>-16.8</i>	<i>6.7</i>	<i>-1.8</i>	<i>20.2</i>	<i>5.3</i>	<i>-2.2</i>	<i>1.5</i>	<i>-10.9</i>	<i>-6.6</i>	<i>-10.5</i>
Manitoba	13,000	13,900	13,400	13,100	13,100	13,900	13,900	13,700	13,800	14,000	14,600	14,200
	<i>1.6</i>	<i>6.9</i>	<i>-3.6</i>	<i>-2.2</i>	<i>0.0</i>	<i>6.1</i>	<i>0.0</i>	<i>-1.4</i>	<i>0.7</i>	<i>1.4</i>	<i>4.3</i>	<i>-2.7</i>
Ontario	194,100	212,200	179,900	195,100	194,400	199,300	195,700	196,400	204,200	223,800	238,900	213,500
	<i>-1.0</i>	<i>9.3</i>	<i>-15.2</i>	<i>8.4</i>	<i>-0.4</i>	<i>2.5</i>	<i>-1.8</i>	<i>0.4</i>	<i>4.0</i>	<i>9.6</i>	<i>6.7</i>	<i>-10.6</i>
Quebec	71,600	80,600	76,800	79,100	80,000	77,200	77,400	71,200	70,600	74,100	77,500	74,400
	<i>1.7</i>	<i>12.6</i>	<i>-4.7</i>	<i>3.0</i>	<i>1.1</i>	<i>-3.5</i>	<i>0.3</i>	<i>-8.0</i>	<i>-0.8</i>	<i>5.0</i>	<i>4.6</i>	<i>-4.0</i>
New Brunswick	7,100	8,200	7,600	7,000	6,700	6,600	6,400	6,300	6,300	6,700	6,900	6,500
	<i>4.4</i>	<i>15.5</i>	<i>-7.3</i>	<i>-7.9</i>	<i>-4.3</i>	<i>-1.5</i>	<i>-3.0</i>	<i>-1.6</i>	<i>0.0</i>	<i>6.3</i>	<i>3.0</i>	<i>-5.8</i>
Nova Scotia	10,600	11,700	10,700	9,900	10,000	10,300	10,400	9,100	8,900	9,200	9,700	9,200
	<i>-1.9</i>	<i>10.4</i>	<i>-8.5</i>	<i>-7.5</i>	<i>1.0</i>	<i>3.0</i>	<i>1.0</i>	<i>-12.5</i>	<i>-2.2</i>	<i>3.4</i>	<i>5.4</i>	<i>-5.2</i>
Prince Edward Island	1,500	1,800	1,500	1,400	1,500	1,500	1,500	1,400	1,400	1,700	1,900	1,500
	<i>7.1</i>	<i>20.0</i>	<i>-16.7</i>	<i>-6.7</i>	<i>7.1</i>	<i>0.0</i>	<i>0.0</i>	<i>-6.7</i>	<i>0.0</i>	<i>21.4</i>	<i>11.8</i>	<i>-21.1</i>
Newfoundland & Labrador	3,500	4,500	4,700	4,400	4,200	4,500	4,700	4,300	4,100	4,300	4,200	3,600
	<i>9.4</i>	<i>28.6</i>	<i>4.4</i>	<i>-6.4</i>	<i>-4.5</i>	<i>7.1</i>	<i>4.4</i>	<i>-8.5</i>	<i>-4.7</i>	<i>4.9</i>	<i>-2.3</i>	<i>-14.3</i>

\* Includes sales in the Territories.

Annual percent changes are in italics.

Source: Canadian Real Estate Association, RBC Economics Research

Home price forecast												
Aggregate price	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016f	2017f
Canada	266,600	296,500	313,300	311,200	332,600	347,800	358,500	367,000	383,900	403,400	441,800	448,900
	<i>10.3</i>	<i>11.2</i>	<i>5.7</i>	<i>-0.7</i>	<i>6.9</i>	<i>4.6</i>	<i>3.1</i>	<i>2.4</i>	<i>4.6</i>	<i>5.1</i>	<i>9.5</i>	<i>1.6</i>
British Columbia	405,900	459,700	498,300	476,800	506,700	533,900	531,500	530,000	565,200	609,700	734,700	748,700
	<i>16.5</i>	<i>13.3</i>	<i>8.4</i>	<i>-4.3</i>	<i>6.3</i>	<i>5.4</i>	<i>-0.4</i>	<i>-0.3</i>	<i>6.6</i>	<i>7.9</i>	<i>20.5</i>	<i>1.9</i>
Alberta	298,700	379,500	381,900	361,500	374,700	379,500	386,300	399,100	419,300	425,200	419,000	411,000
	<i>27.2</i>	<i>27.1</i>	<i>0.6</i>	<i>-5.3</i>	<i>3.7</i>	<i>1.3</i>	<i>1.8</i>	<i>3.3</i>	<i>5.1</i>	<i>1.4</i>	<i>-1.5</i>	<i>-1.9</i>
Saskatchewan	159,600	208,100	267,000	262,600	278,300	287,800	306,800	318,300	322,000	320,500	325,400	319,900
	<i>10.9</i>	<i>30.4</i>	<i>28.3</i>	<i>-1.6</i>	<i>6.0</i>	<i>3.4</i>	<i>6.6</i>	<i>3.7</i>	<i>1.2</i>	<i>-0.5</i>	<i>1.5</i>	<i>-1.7</i>
Manitoba	161,700	178,900	198,300	204,500	225,500	238,500	252,100	261,300	270,400	273,700	277,400	280,300
	<i>10.2</i>	<i>10.6</i>	<i>10.8</i>	<i>3.1</i>	<i>10.3</i>	<i>5.8</i>	<i>5.7</i>	<i>3.6</i>	<i>3.5</i>	<i>1.2</i>	<i>1.4</i>	<i>1.0</i>
Ontario	278,700	294,900	308,800	310,200	335,600	352,000	369,300	382,300	402,000	430,800	480,900	495,400
	<i>5.5</i>	<i>5.8</i>	<i>4.7</i>	<i>0.5</i>	<i>8.2</i>	<i>4.9</i>	<i>4.9</i>	<i>3.5</i>	<i>5.2</i>	<i>7.2</i>	<i>11.6</i>	<i>3.0</i>
Quebec	198,200	213,100	229,100	239,500	257,300	272,900	280,100	283,900	288,500	293,500	305,400	309,000
	<i>4.6</i>	<i>7.5</i>	<i>7.5</i>	<i>4.5</i>	<i>7.4</i>	<i>6.1</i>	<i>2.6</i>	<i>1.4</i>	<i>1.6</i>	<i>1.7</i>	<i>4.1</i>	<i>1.2</i>
New Brunswick	144,900	294,900	164,800	167,200	173,100	179,500	182,600	185,700	189,300	188,800	199,600	202,400
	<i>7.1</i>	<i>103.5</i>	<i>-44.1</i>	<i>1.5</i>	<i>3.5</i>	<i>3.7</i>	<i>1.7</i>	<i>1.7</i>	<i>1.9</i>	<i>-0.3</i>	<i>5.7</i>	<i>1.4</i>
Nova Scotia	169,300	213,100	193,200	195,000	204,100	211,300	219,100	219,400	222,500	225,600	233,300	234,800
	<i>5.9</i>	<i>25.9</i>	<i>-9.3</i>	<i>0.9</i>	<i>4.7</i>	<i>3.5</i>	<i>3.7</i>	<i>0.1</i>	<i>1.4</i>	<i>1.4</i>	<i>3.4</i>	<i>0.6</i>
Prince Edward Island	149,200	294,900	170,200	178,100	180,300	177,400	188,000	190,000	189,300	197,000	202,300	202,700
	<i>4.4</i>	<i>97.7</i>	<i>-42.3</i>	<i>4.6</i>	<i>1.2</i>	<i>-1.6</i>	<i>6.0</i>	<i>1.1</i>	<i>-0.4</i>	<i>4.1</i>	<i>2.7</i>	<i>0.2</i>
Newfoundland & Labrador	145,300	213,100	178,100	205,900	226,400	241,100	253,400	269,900	276,800	281,800	278,400	264,000
	<i>3.4</i>	<i>46.7</i>	<i>-16.4</i>	<i>15.6</i>	<i>10.0</i>	<i>6.5</i>	<i>5.1</i>	<i>6.5</i>	<i>2.6</i>	<i>1.8</i>	<i>-1.2</i>	<i>-5.2</i>

Annual percent changes are in italics.

Source: Brookfield RPS, Royal LePage, Statistics Canada, RBC Economics Research

The material contained in this report is the property of Royal Bank of Canada and may not be reproduced in any way, in whole or in part, without express authorization of the copyright holder in writing. The statements and statistics contained herein have been prepared by RBC Economics Research based on information from sources considered to be reliable. We make no representation or warranty, express or implied, as to its accuracy or completeness. This publication is for the information of investors and business persons and does not constitute an offer to sell or a solicitation to buy securities.