Regional housing affordability at crosscurrents in Canada in Q1

Contrasting provincial housing trends continued to be largely offsetting in the first quarter of 2015 such that overall housing affordability in Canada remained little changed from the previous quarter. A decline in mortgage rates early this year contributed to an improvement in affordability in many markets and housing categories where home price increases were subdued (or where prices declined); on the other hand, markets experiencing stronger price advances (e.g., Toronto and to some extent Vancouver) saw affordability deteriorate. In the aggregate, RBC’s national affordability measures edged only slightly lower in two of three housing categories in the latest period, down by 0.3 percentage points to 27.1% for condominium apartments and by 0.2 percentage points to 47.9% for two-storey homes (a decrease represents an improvement in affordability). The measure for detached bungalow was unchanged at 42.7%. Trends in the national measures have been fairly flat since 2010 at levels near or slightly above long-term averages.

Ownership costs ease in the Prairies…

The plunge in oil prices was a significant differentiating factor for markets dependent on the oil and gas industry. It tipped the demand-supply scale in favour of buyers, thereby causing home prices to soften and ownership costs to ease in these markets in the first quarter. RBC’s affordability measures for Alberta fell the most among the provinces, although the picture in Saskatchewan was more nuanced because a small decline in household income partly counteracted the effect of lower prices in most housing categories. At the local level, Calgary and Edmonton showed the biggest improvement in affordability in the first quarter.

…as well as in Quebec and in the Atlantic region…

It also became more affordable to own a home at market prices in most housing categories in Quebec and Atlantic Canada in the first quarter. Ownership costs have been contained by fairly weak market conditions (in part resulting from a rise in the supply of new condo units) since early 2014 in these regions. In fact, RBC’s measures for Quebec and Atlantic Canada generally have pursued downward courses in the past year such that these regions showed some of the greater improvement in affordability in Canada relative to year-ago levels.

…but continued to rise in Toronto and Vancouver

At the other end of the spectrum, solid price increases continued to erode housing affordability in the Toronto-area market. Strong price gains for single-detached homes also squeezed already poor affordability in the Vancouver, although there was some reprieve in the condo segment, where prices inched a little lower. Both Toronto and Vancouver have been Canada’s housing ‘hot spots’ so far this year despite broadly deteriorating affordability trends.

Little affordability-related stress outside Vancouver and Toronto

Generally speaking, housing affordability remains fairly neutral in Canada
with limited signs of undue stress being exerted on homebuyers. Both at the national level and in the majority of local markets, RBC’s affordability measures are still quite close to their long-term average, thereby suggesting that current conditions are within historical norms. The two main exceptions are Vancouver and Toronto where high and rising prices make it a stretch for a typical household to own a home at today’s market values, especially in the single-detached segments (the bar on condo ownership is comparatively much less of a hurdle). In the case of Vancouver, poor affordability has long been the reality. In the case of Toronto, however, the situation mostly reflects slippage in the past four years or so.

**Contrasting regional pictures to persist in the near term**

The contrasting regional affordability pictures across Canada are likely to persist in the near term. We expect that balanced demand-supply conditions in the majority of local markets will continue to support generally modest price increases and fairly stable levels of affordability. The likelihood of small price declines in markets dependent on the oil industry suggests that home ownership costs may fall further in Alberta, Saskatchewan, and possibly parts of Atlantic Canada. With sellers firmly in command in Vancouver and Toronto, we expect strong price momentum to erode affordability further in these markets, particularly in the single-detached segments. A recent surge in condo completions in Toronto, however, ultimately may contribute to lower condo ownership costs somewhat in the period ahead. Looking further afield, the eventual normalization of monetary policy has the potential to affect housing affordability adversely across Canada. RBC expects the Bank of Canada to start raising the overnight rate in the second quarter of 2016. Exceptionally low interest rates have been a key factor maintaining housing affordability at mostly manageable levels in recent years. The effect on affordability of a rise in interest rates would be most visible in high-priced markets.

**Resale market activity was strong this spring**

Home resale activity picked up smartly this spring following a temporary slowdown during the winter months caused in part by unusually poor weather conditions in many areas of the country. National resales rose by 11.2% in between February and May to a level (521,400 units, annualized) above the 10-year average of 469,200 units. Homebuyer demand is strongest in Vancouver and Toronto, where it exceeds available supply; however, there were signs of revival emerging in some previously soft markets (including Montreal and Ottawa). The rout in Alberta and Saskatchewan stabilized recently as confidence began to return, thereby suggesting that downward price pressure may abate in the coming months in markets such as Calgary, Edmonton, and Saskatoon. We expect that home resales in Canada will rise modestly by 1.5% to 488,500 units in 2015 from 481,200 units in 2014. The projected increase mainly reflects strength in British Columbia and Ontario, with modest contributions also coming from mild gains in other oil-consuming provinces. Our forecast sees partial offsets from declines in Alberta (down nearly 21%) and Saskatchewan (down close to 13%).
British Columbia – Vancouver still skews provincial affordability

The latest read on housing affordability in British Columbia showed that developments varied by housing categories but still signalled the presence of greater than average pressure. RBC’s measures for the province eased for condo apartments (down 0.4 percentage points to 32.9%) and two-storey homes (down 0.1 percentage points to 72.8%) in the first quarter of 2015, while the measure for bungalows rose by 1.0 percentage point to 69.3%. All measures remained above long-term averages—substantially so in the case of single-detached segments. That being said, poor affordability at the provincial level primarily reflected the extreme situation in Vancouver. Home ownership continued to be comparatively more affordable in other areas of the province. Despite the presence of affordability pressure, provincial home resales rose further in the first quarter. Most of the advance took place in Vancouver (which registered a 12% gain); however, markets such as Victoria, Fraser Valley, and South Okanagan also recorded hefty increases.

Alberta – The worst may be over

Housing markets in Alberta experienced a particularly violent bout of anxiety in the face of plummeting oil prices at the start of 2015. Sellers rushed to list their homes, and buyers hit the pause button; the combination of which dramatically loosened demand-supply conditions that turned the table squarely in favour in buyers. Following a period of rapid price increases in 2013 and most of 2014, property values came under downward pressure in the first quarter of 2015. While a shock of this nature raises many risks, a positive side effect was that housing affordability improved significantly across the board in the province. RBC’s affordability measures fell by 1.0 percentage points for two-storey homes (to 33.0%), by 0.7 percentage points for bungalows (to 31.8%), and by 0.6 percentage points for condo apartments (to 19.9%). Generally speaking, the measures stood at attractive levels both from a historical perspective and from provincial comparison basis, which are likely to help limit the extent of the correction. Indeed, resale activity stabilized recently, thereby suggesting that the worst may be over for the market.

Saskatchewan – Jitters may be subsiding

Saskatchewan’s housing market also was affected by a case of the jitters in the early months of 2015, although some areas of the province such as Regina were already challenged by plentiful supply prior to the oil price plunge. Home resales plummeted by more than 16% in the province in the first quarter of this year, which contributed to price declines across most housing segments. The effect on affordability was partly muted by moderation in household income, however. A slight 0.2% drop in household income entirely offset the effect of a 0.4% price decline in the two-storey category, and counteracted most of the 0.9% drop in condo apartment prices. RBC’s measure for two-storey homes was unchanged at 37.9%, and the measure for condos inched only 0.1 percentage points lower to 24.7%. The measure for bungalows rose by 0.3 percentage points to 33.9% (bungalow prices rose slightly). Recent monthly statistics show that home resales picked up this spring in the province with gains recorded in Saskatoon and in a number of smaller markets including Moose Jaw.
Manitoba – Affordability as regular as it gets; market remains well supplied

The affordability of single-detached homes and condo apartments evolved in opposite directions in the first quarter. RBC’s measures rose by 0.3 percentage points for both bungalows (to 35.6%) and two-storey homes (to 36.9%), while the measure for condos fell noticeably by 1.1 percentage points to 22.2%. A wave of new multi-unit completions in Winnipeg in 2014 caused some absorption issues, which ultimately weighed on condo prices in the resale market recently. Soft condo sale activity also contributed to the price weakness in this segment in the first quarter. On the other hand, resales of single-detached homes firmed up so far in 2015, thereby helping to support price increases in these categories—although leading to some modest deterioration in affordability in the first quarter. Overall, current housing affordability conditions in the province do not pose unusual challenges for homebuyers, as RBC’s affordability measures remain remarkably close to long-term averages.

Ontario – Split between single-detached and condos persists

The main theme of Ontario’s housing affordability story continues to be the split between trends for single-detached homes and condos apartments. Owning a bungalow or a two-storey home at market prices in the province has become less and less affordable in the past four years or so, whereas the weight of owning a condo has remained quite constant. In the fourth quarter of 2014, there was further deterioration in the single-detached categories, while the condo segment saw a slight improvement. RBC’s measures for bungalows and two-storey homes both rose by 0.3 percentage points (to 45.5% and 51.7%, respectively). The measure for condos edged lower by 0.2 percentage points to 28.9%. To a large extent, the diverging trends in recent years has reflected the shift in the mix of new construction in the province toward multi-unit structures, with about half as many single-family homes being built compared to 10 years ago. The relative scarcity of single-family homes in the face of growing demand, therefore, has fuelled stronger price increases compared to the well supplied condo segment. Home resale activity was quite brisk this spring in markets such as Toronto, Hamilton, London, Windsor, and to a lesser extent, Ottawa, after an uneven winter period.

Quebec – Affordability at multi-year best levels

After remaining mostly steady for years, housing affordability improved progressively during 2014 and continued to do so in the first quarter of 2015. RBC’s measures fell in all three categories in the latest period: by 0.3 percentage points for both bungalows (to 32.9%) and two-storey homes (to 41.1%), and by 0.1 percentage points for condo apartments (to 25.5%). The declines in the past year in Quebec marked some of the more significant improvement among the provinces. Quebec homebuyers now enjoy the most affordable conditions in the province in nearly six years for single-family homes and 10 years for condos; however, these more favourable conditions do not yet constitute a major draw for homebuyers. In the first quarter, home resales were still 5.4% below the 10-year average, although activity picked up materially this spring. The resumption of job creation since the beginning of 2015 in the province—after a year of stagnation in 2014, there were close to 50,000 new jobs created between January and May—likely has begun to revitalize housing demand. This factor and the more favourable affordability picture should be positive for home resales in the period ahead.
Atlantic – Affordability still attractive, still improving

The lingering effect of earlier softness in home resale markets led to further improvement in housing affordability in the Atlantic region in the first quarter. The cost of owning a home in the region generally has been under downward pressure since late 2013 due to bouts of weak demand and increases in homes available for sale in key markets. Although there were signs that demand–supply conditions firmed up in the latest period, prices for single-detached homes edged lower, thereby contributing to drops in RBC’s affordability measures for bungalows (down 0.7 percentage points to 29.4%) and two-storey homes (down 0.5 percentage points to 34.0%). Both measures reached their lowest levels in nearly 10 years. The measure for condos was unchanged at 25.0%, which was still within close range of an eight-year low. Current affordability conditions in Atlantic Canada remain among the more attractive in Canada. Home resale activity slowed in the first quarter across the region, in part due to unusually poor weather. Areas such as Halifax, Moncton, and Saint John saw resales fall noticeably relative to the fourth quarter of 2014. Despite weaker resales, demand–supply conditions generally tightened in the region because of a plunge in new listings in many local markets (also likely resulting from the adverse weather).

Major city markets

Vancouver – Sizzle puts added pressure on affordability

The sizzle is back in Vancouver’s housing market, and strong price increases for single-family homes in the first quarter of 2015 further pressured already poor affordability levels in the area. Home resales rose for the fourth-consecutive quarter in the latest period to their highest level in more than five years. Sellers did not keep pace with growing demand from homebuyers, especially for single-detached homes, thereby causing the demand–supply equation to tilt even more in favour of sellers. The condo segment was better supplied, however, thanks to increased multi-unit construction in the past couple of years, which contributed to put a lid on condo prices. RBC’s affordability measure for bungalows posted its biggest increase in three years—2.8 percentage points to 85.6%. The measure for two-storey homes also rose, although less dramatically, by 0.9 percentage points to 86.9%. The measure for condos bucked the trend in easing by 0.5 percentage points to 39.6%. Accelerating price advances this spring (Vancouver boasted the fastest rate of appreciation among Canada’s largest cities most recently) suggest that affordability will likely deteriorate further in the term in the area.

Calgary – Favourable affordability conditions unlikely top of mind right now

Calgary’s housing market was under intense pressure early this year when the plunge in oil prices shook confidence on both sides of the selling equation. Within a few short months, the market swung sharply from favouring sellers to favouring buyers, thereby causing the earlier rapid pace of price increases to start running in reverse. The upside of this stunning turn of events was that it helped improve housing affordability across the board in the area. RBC’s measures fell for all categories in the first quarter, declining by 1.5 percentage points for two-storey homes (to 32.6%), 1.0 percentage point for bungalows (to 32.8%), and 0.6 percentage points for condo apartments (to 19.4%). Nonetheless, housing affordability may not be top of the mind for homebuyers at this juncture—uncertainty about global oil markets and, above all, Alberta’s...
economy likely are dominant considerations. More recent developments show that the freefall in resale activity has stabilized this spring. The next stage for the market likely will be shaped by news on the economy (and the job market in particular).

**Toronto – Single-detached home affordability inching closer to risky levels**

Little by little, housing affordability is deteriorating ever closer to the historically poor levels of 1990 for single-detached homes in the Toronto area. In the first quarter of 2015, RBC’s measures for bungalows (57.3%) and two-storey homes (67.0%) in the area rose (by 0.6 and 1.5 percentage points, respectively) to their highest points in more than 24 years. Approaching the 1990 levels may signal that risks are mounting in the Toronto market, because those were associated with a housing bubble at the time and then followed by a steep and prolonged downward correction in prices during the first half of the 1990s. A key difference this time, however, is that condo affordability remains largely in check—the trend in RBC’s measure barely deteriorated in the past five years (it inched higher by just 0.2 percentage points in the first quarter). This means that there remain more reasonably priced housing options in today’s market, which was not the case in 1990. Condo prices are unlikely to escalate in the near term, because a surge in new condo completions in the first few months of 2015 is bound to keep the resale market flush with available condo units.

**Ottawa – Plentiful supply helping to improve affordability**

Owning a home at market prices in the Ottawa area became slightly more affordable across all housing categories in the first quarter. RBC’s measures fell by 0.6 percentage points for both bungalows (to 35.4%) and two-storey homes (to 37.1%), and by 0.3 percentage points for condo apartments (to 23.7%). The improvement came amid stalling home prices in the early months of 2015 as demand-supply conditions continued to weaken. Home resales fell modestly in the first quarter when properties put up for sale increased quite noticeably. Part of this rise in new listings reflected higher levels of condo completions in the past year, and many of those units remained unabsorbed in the first quarter. Despite the setback in resales this winter, there are signs that positive demand momentum is building. Home resales have run ahead of year-ago levels for three successive quarters, and more recent data suggest that they will do so again in the second quarter of 2015. Plentiful condo supply likely will continue to be key factor weighing on prices in the near term.

**Montreal – Positive affordability trends still in place**

Housing affordability in the Montreal area continued to be on a steadily improving trend in the early part of 2015. First-quarter readings showed improvement in all three housing categories with RBC’s measures falling by 0.4 percentage points to 47.8% for two-storey homes, 0.2 percentage points to 37.2% for bungalows, and 0.1 percentage points to 29.2% for condo apartments. These declines followed a series of sizeable drops during 2014, such that Montreal experienced some of the larger reductions in the burden of home ownership in the past year among Canada’s top urban areas. Property values have stagnated (or even diminished slightly in some case) in the face of soft demand and a strong supply of condo units. Elevated levels of new condo construction in recent years have resulted in a high inventory of unsold condos in the area, which likely will take time to clear. The good news is that homebuyer demand picked up noticeably this spring, likely in part reflecting a strengthening in local employment.
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 two-storey 1,500 square feet. 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 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).

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* 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