Housing affordability worsened in Toronto, eased in Vancouver at the end of 2016

- Housing affordability remained strained in Canada; however, it did not get any worse in the fourth quarter of 2016.
- Overall stability masked diverging regional trends: housing affordability deteriorated in Toronto and other parts of Southern Ontario, while it eased in Vancouver for the first time in more than three years.
- Despite seeing some relief at the end of 2016, would-be buyers in Vancouver continue to face the highest affordability hurdle in Canada—by a long shot.
- In Toronto, affordability reached its poorest level since 1990. Stress is most intense in the single-detached home segment; however, it is also present to a lesser degree in the condo apartment segment.
- Affordability levels remain close to historical norms in the majority of other markets in Canada. Exceptions include Calgary (better-than-usual affordability) and Victoria (more strained than it has been historically).
- Affordability stress is bound to intensify in Toronto in the near term, stoking already elevated risks and raising the need for targeted policy intervention.

Affordability erosion takes a pause at the national level,...
The cost of owning a home at market price in Canada continued to take an abnormally large bite of household income in the fourth quarter of 2016. The encouraging news, however, is that a string of six consecutive quarterly increases came to an end. RBC’s aggregate affordability measure was unchanged in the latest period at 44.2%—still the most stressed level since late-2008. There were small offsetting changes within housing categories, however: the measure for single-detached homes fell marginally by 0.1 percentage points to 49.2% and the measure for condominium apartments edged upwardly by 0.2 percentage points to 35.9% (an increase in the measure represents a deterioration in affordability).

...although not in Toronto where the level is the worst since 1990
The stability of affordability, nation-wide, masked diverging trends across local markets. Most concerning was further erosion in the Toronto area, where surging home prices boosted homeownership costs (based on current market values) to their highest level as a share of household income since the second quarter of 1990. In fact, RBC’s aggregate measure for the area (64.6% in the fourth quar-
ter) was the second-highest on record since the middle of the 1980s. The severe strain afflicting Toronto-area buyers primarily reflects elevated and still-rapidly escalating single-detached home prices (resulting from a shortage of supply relative to strong demand); however, increasing condo apartment values also contributed. RBC’s affordability data strongly indicate that the Toronto-area market is in a high-risk zone.

**Vancouver sees welcome improvement from severe strain**

Housing affordability improved in the Vancouver area for the first time in almost three years. Some reprieve from intense stress resulted from a sharp slowdown in home resale activity since the spring of 2016 generating a cooling effect on single-detached home prices by the late stages of the year. RBC’s measure for single-detached homes in the area fell the most since the first quarter of 2009 (when the global financial crisis was in full swing). No such affordability relief took place in the condo apartment segment, however, as RBC’s condo measure rose slightly for a seventh-straight quarter. A succession of policy actions from both the federal and BC governments—including a 15% tax on purchases by foreign buyers in Metro Vancouver—contributed to the decline in home resales in the area.

**Signs that affordability stress seeps into regions near hot spots**

We also see signs that the squeeze on affordability in Toronto and Vancouver is spreading to nearby regions. In Southern Ontario, markets such as Hamilton and St. Catharines showed evidence of higher-than-usual affordability-related stress lately based on trends for mortgage carrying costs (a variant of RBC’s affordability measure that excludes property taxes and utilities). In British Columbia, Victoria has experienced booming demand in the past year which has propelled prices significantly higher and RBC’s aggregate measure to a level well above its long-term average.

**Affordability unlikely to be a constraint in other parts of Canada**

Outside of Southern Ontario and a few BC regions, affordability levels and trends continued to be fairly neutral in the majority of markets in the fourth quarter. RBC’s measures generally stood near long-run averages, thereby indicating little in the way of undue affordability-related stress. Saskatoon, Regina, St. John’s and Ottawa saw some small improvement in the latest quarter, while Montreal, Halifax and Edmonton recorded modest deterioration. Calgary continued to stand out for its historically attractive affordability level despite experiencing marginal erosion in the latest period.

**More of the same in the near term**

Recent affordability trends are likely to persist in the near term. Unrelenting tightness in demand-supply conditions in the Toronto area, other parts of Southern Ontario and Victoria is poised to keep fueling rapid price increases and further erode affordability in these markets. More balanced conditions in Vancouver and the majority of other markets across Canada should lead to comparatively subdued price variations. For Vancouver, this leaves the door open to more affordability relief for buyers. Elsewhere, this would support the continuation of incremental changes.

**Growing risks in Toronto call for policy intervention?**

Rapid degradation of affordability in the Toronto area and other parts of Southern Ontario—and the likelihood that the situation will worsen further if left unchecked—is a significant concern. Ever rising homeownership costs to levels that impose excessive burdens for many buyers in the region substantially raise the vulnerability to an unexpected shock. Policy measures implemented to date by the federal government—most recently in October and November 2016—to cool Canada’s ‘hot markets’ down so far have had little discernable restraining effects on markets in Southern Ontario, despite our earlier belief that they would slow demand down materially. It would be prudent for policymakers (especially at the provincial and local level) to consider implementing additional policy measures designed specifically to address growing market risks in the Toronto area and the rest of Southern Ontario in order to minimize or prevent potentially destabilizing developments down the road.
British Columbia

Victoria – Loss of affordability taking a bite out of resale activity?
The wave of home buying in Victoria seen since in 2015 lost momentum in the latter stages of 2016. One of the factors that previously attracted buyers in the area—reasonable affordability levels, especially compared to Vancouver—lost a fair degree of appeal in the past year because a spike in home prices pressured homeownership costs significantly upward more recently. RBC’s aggregate reached a six-year high of 55.1% in the fourth quarter of 2016, up 6.6 percentage points from a year earlier. In fact, this year-over-year deterioration was the third largest among local markets in Canada after the increases recorded in Vancouver and Toronto. Demand-supply conditions continued to be exceptionally tight at the start of 2017, which suggests that intense upward price pressure is likely to persist in the near term and that affordability is at risk of eroding further.

Vancouver area – Affordability relief unlikely to matter much
Vancouver-area buyers finally saw some affordability relief in the fourth quarter when RBC’s aggregate measure fell for the first time—by 5.2 percentage points—in almost three years. Such relief unlikely made much of a difference, however, because homeownership costs remain incredibly steep. RBC’s aggregate measure was 84.8% in the fourth quarter, which clearly indicates that owning a home at current market prices—especially a single-detached home—is still out of reach for a typical area household. Owning a condo apartment is less of a stretch (RBC’s measure was 46.1%); however, it too is beyond the grasp of many households. A succession of policy measures has dampened resale activity substantially since reaching an all-time high in early 2016, and demand-supply conditions have become more balanced in the past half-year. Sky-high prices for single-detached homes have weakened modestly in recent months, although this was not the case of condo prices which remained on an upward trajectory.

Alberta

Calgary – Attractive affordability likely to get more attention
Housing affordability has not been a big story in Calgary in the past couple of years; the provincial recession was the centre of attention, and for good reasons. Surging unemployment, the loss of confidence and weakening demographic flows drove buyers away from the market, causing resale activity to plummet and home prices to soften. All the while, housing affordability hovered at historically attractive levels—near the best on record since the mid-1980s—but given the grim economic circumstances, this factor did not register much with buyers. Affordability may become a bigger story going forward, however. As confidence in the market gradually rebuilds amid improving economic conditions—we have seen ‘green shoots’ lately—Calgary’s attractive affordability is likely to become a more significant draw for buyers. Such may be already the case with home resales trending slightly upwardly recently. RBC’s aggregate measure for the area was little changed at 33.8% in the fourth quarter, still significantly below its long-run average of 40.3%.

Edmonton – Turning a corner
The slowly deteriorating trend in affordability in Edmonton persisted in the fourth quarter; however, this did not pose any significant risk to the market. RBC’s aggregate measure—35.4% in the latest period, up by just 0.2 percentage points from the third quarter—remained well within historical norms. In fact, the modest increase in the measure in the past year is likely a sign that the market is firming up, following a period of softness in early 2016. We
note that home resales have had a solid start to 2017 (up 20% year over year in the first two months) and that demand-supply conditions have tightened moderately. These developments suggest that the Edmonton market is possibly turning a corner. Still, with a local unemployment rate at a decades-high of more than 8%, prospects for a quick rebound in confidence are dim at this stage, which may temper the speed recovery in the market.

**Saskatchewan**

**Saskatoon — Still waiting for a recovery to take hold**

A market recovery remains elusive in Saskatoon. The increase in home resales recorded in the third quarter of 2016—only the second quarterly gain since mid-2014—was largely reversed in the fourth quarter. Demand-supply conditions also weakened late last year, putting buyers more firmly into the driver’s seat and maintaining downward pressure on prices. Such pressure was exacerbated by a sharp rise in the inventory of recently built but still unsold units in the multi-dwelling segment. Despite weakening prices and slightly improving affordability, buyers showed little desire to jump in, no doubt nervous about their economic prospects. Saskatoon’s jobless rate surged to a decades-high of 7.6% in the late stages of 2016, and has eased only modestly since then. Housing affordability is unlikely to be an issue for buyers. RBC’s aggregate measure was 32.0% in the fourth quarter, slightly below the long-term average of 32.9% and down by 0.9 percentage points relative to the third quarter.

**Regina — Mild improvement continuing**

The state of the housing market continued to improve mildly in Regina in the late stages of 2016 with home resale strengthening further, the inventory of newly built but unsold units falling and demand-supply conditions remaining in balance. Housing affordability likely neither stimulated nor hindered activity in the area because it continued to be close to historical norms. RBC’s aggregate measure was 29.3% in the fourth quarter, which only modestly exceeded the long-run average of 27.8%. While the measure fell by 0.8 percentage points in the latest period, this came on the heels of a larger increase of 1.1 percentage points in the third quarter, such that the flat trend in the measure in place since 2014 was maintained.

**Manitoba**

**Winnipeg — Maintaining a firm tone**

Winnipeg’s housing market maintained a firm tone at the end of 2016 amid fairly neutral affordability conditions. Home resales moderated only slightly after reaching record-high levels earlier in the year, thereby making 2016 the strongest year ever in terms transactions at almost 12,900 units. Robust demand and diminishing supply tightened the market, although not enough to increase upward pressure on prices. A fairly tame pricing environment in turn kept affordability pressures at bay, which stayed within historical norms. RBC’s aggregate measure was unchanged at 30.4% in the fourth quarter, just slightly above the long-term average of 29.8%. A softening in Winnipeg’s job market in the past year—the area’s unemployment rate rose to its highest level (6.9% in December) more than 15 years—poses a downside risk to the market; however, we expect such weakness to be temporary given positive prospects for the provincial economy.
Ontario

Toronto area – Sounding the alarm bell
Contrary to our expectations, policy measures implemented last spring and fall by the federal government to cool Canada’s hot housing markets have had few discernable restraining effects on the Toronto-area market. Quite the contrary, we observe that demand has continued to grow, supply (listings) has dwindled further and prices are still going through the roof—at an accelerating pace of all things. These factors have crushed (already poor) housing affordability, with RBC’s aggregate measure reaching the second-worst level on record for the area since the mid-1980s in the fourth quarter of 2016 (64.6%). The last time affordability was in such a state (in 1990), Toronto’s housing market subsequently fell into a deep and prolonged slump. The situation is different this time because most of the affordability stress is concentrated in the single-detached segment—whereas it was pervasive in 1990—however, recent acceleration in condo prices tells us that stress soon will mount significantly in this segment too. Left unchecked, this situation will get worse, putting at high risk Canada’s largest housing market. Further policy intervention would be prudent to avoid a 1990s-style outcome.

Ottawa – Healthy trends persist
Affordability trends remain relatively healthy in the National Capital area, where RBC’s aggregate measure inched lower by 0.2 percentage points to 35.6% in the fourth quarter, still only modestly above the 34.0% average since the mid-1980s. In contrast to the situation in the southern part of the province, we see few signs of overheating or undue affordability stress in the Ottawa-area market. This provides a favourable environment for buyers who have been further emboldened by a marked strengthening in the regional job market since the second half of 2016. Home resales set a new record high of 15,800 units last year despite a slow start to the year. Momentum was quite strong in the late stages of the year. Demand-supply conditions tightened up; however, they remained balanced, keeping price pressures contained. Brisk demand helped reduce the previously elevated inventory of recently built but still unsold units.

Quebec

Montreal area – Strong labour market fueling homebuyer demand
The cost of owning a home in the Montreal area has trended slightly upwardly as a share of household income in 2016; however, this is unlikely to be much of an obstacle to buyers. RBC’s aggregate measure of 40.2% in the fourth quarter was still within historical norms, being reasonably close to its long-run average of 38.3%. The recent uptrend in the measure—it rose by 0.3 percentage points from its level in the third quarter and by 1.3 percentage points from a year ago—has coincided with a strengthening housing market activity. Home resales were up by 7% year over year in the fourth quarter. Homebuyer demand is benefiting from a sharp improvement in Montreal’s job market. Employment growth has picked up solidly in the past year (almost 85,000 net new jobs were created in the last 12 months) and the unemployment rate fell by its lowest level (6.6%) in nine years at the start of 2017.

Quebec City – Affordability issues may be holding back buyers
Slight deteriorating trends in affordability continued to prevail in the Quebec City market and likely exerted some degree of undue stress on area buyers. While it has been the case that affordability levels have departed from histori-
ment. By the end of the year, upward price pressure had significantly with the area’s unemployment rate surging to almost 10% at the end of last year. With such an economic storm undermining confidence, home demand and supply back into balance. The good news was that home resales picked up modestly in the fourth quarter; however, gains over the entire 2016 were meagre.

Atlantic Canada

**Saint John – Still Canada’s affordability leader**

Canadians looking to buy an affordable home should be considering moving to Saint John as this market is the most affordable among the markets that we cover. RBC’s aggregate measure of 25.8% in the fourth quarter—up only marginally by 0.1 percentage points from the third quarter—was once again the lowest in our coverage and miles below the national average of 44.2%. In fact, it is more affordable to own a single-detached home in Saint John than a condo apartment in many cities in Canada. Favourable affordability possibly played a role in home resales picking up noticeably last year, reaching a seven-year high of 1,900 units. Such brisk activity helped to firm demand-supply conditions, which became balanced on a sustained basis for the first time since 2011. More balanced conditions supported modestly stronger price increases.

**Halifax – The market recovery continues**

The Halifax market continued to recover in 2016 with home resales rising for the second-consecutive year by 6.6% to almost 5,200 units. Despite this gain, the general tone of the market was somewhat soft as resales remained 15% below their level in 2012 and price increases were subdued. That being said, demand-supply conditions followed a modestly firming trend thanks to growing demand and declining listings. Buyers in the area benefited from generally attractive affordability levels. RBC’s aggregate measure (31.1% in the fourth quarter) remained below its long-term average (32.7%) during the entire year. The measure increased modestly by 0.3 percentage points in the latest period. Stronger population growth in area also likely contributed to boost homebuyer demand last year.

**St. John’s – Economy not affordability is the biggest issue**

Housing affordability trends have been generally static since 2014 in St. John’s, and this continued to be the case in the late stages of 2016. RBC’s aggregate measure stood at 26.6% in the fourth quarter, which was little changed from the year-ago level. It also matched the long-run average, thereby suggesting that affordability unlikely posed an unusual challenge to buyers. What no doubt represented a much bigger issue for buyers was the very tough economic conditions in the province. St. John’s job market has suffered significantly with the area’s unemployment rate surging to almost 10% at the end of last year. With such an economic storm undermining confidence, home resales fell to their lowest level (4,100 units) since 2006 last year and demand-supply conditions weakened sharply, providing buyers with plenty of choice by the end of the year. Under these conditions, upward price pressure has been strictly contained—with outright declines observed in the condo segment.
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 based on the average market price for single-family detached homes and condo apartments, as well as for an overall aggregate of all housing types in a given market.

Current home prices are sourced from Brookfield RPS, and established from sales prices from monthly transactions, which are filtered to remove extreme values and other outliers.

The aggregate of all categories includes information on prices for housing styles not covered in this report (semi-detached, row houses, townhouses and flexes) in addition to prices for single-family detached homes and condominium apartments. In general, single-family detached homes and condo apartments represent the bulk of the owned housing stock across Canadian markets.

The affordability 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 14 major urban markets in Canada and a national composite. 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 home. 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.

Summary tables

<table>
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<tr>
<th>Aggregate of all categories</th>
<th>Market</th>
<th>Q4 2016 ($)</th>
<th>Price Q/Q % ch.</th>
<th>Y/Y % ch.</th>
<th>RBC Housing Affordability Measure Q4 2016 (%)</th>
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<th>Condominium apartment</th>
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Source: Brookfield RPS, Statistics Canada, Bank of Canada, Royal LePage, 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 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.

The dashed line represents the long-term average for the market.
Source: Brookfield RPS, Statistics Canada, Bank of Canada, Royal LePage, RBC Economics Research
Aggregate home price

Source: Brookfield RPS, RBC Economics Research
Home sales-to-new listings ratio

Source: Canadian Real Estate Association, RBC Economics Research

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