Economic Analysis of British Columbia

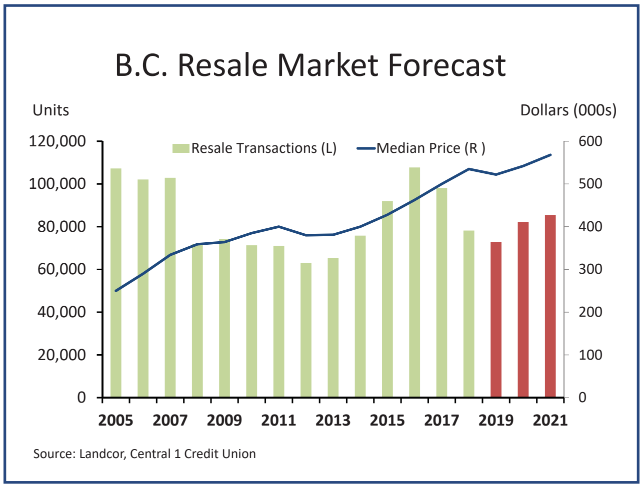
Volume 39 • Issue 5 | ISSN: 0834-3980

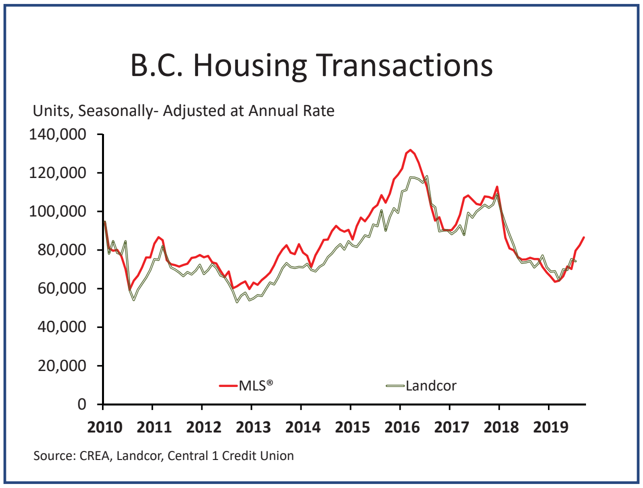
central 1

Resale Market Housing Outlook 2019-2021

Highlights:

- Turnaround in B.C.'s housing market to lift sales and prices
- Low mortgage rates, modest economic growth, and pent up demand to underpin sales performance
- Higher median home values forecast for 2020 and 2021
- Gravity defying housing starts in 2019 to pullback
- Low vacancy rate and rent hikes to continue in rental market





B.C.'s housing market is recovering much quicker than anticipated due to improved affordability and increased housing demand, driven by lower mortgage rates, first-time buyer incentives and population growth boosted by international migration.

After a plunge in early year sales, B.C.'s housing markets have found themselves on firmer footing with MLS® sales up in seven of eight months since February. The demand environment has improved despite many prospective buyers remaining on the sidelines due to federal government mortgage stress tests and various provincial tax measures which continue to curtail purchases by both domestic and foreign buyers, specifically in the highest priced urban areas like Metro Vancouver.

Affordability has improved due to a sharp retrenchment in mortgage rates and lower prices in large urban markets, supported by labour market and population growth. Mortgage rates are down as a result of increased macro-economic uncertainty - which has led to a declining bond yield environment – and competition among lenders. A Central 1 survey of five-year fixed mortgage broker rates points to a decline of 80-100 basis points over the past 12 months to about 2.6 per cent. This is the lowest since mid-2017. However, pass-through of lower rates to consumers has been blunted by a stubbornly high posted rate which has only declined marginally to 5.19

Summary Housing Forecast Table

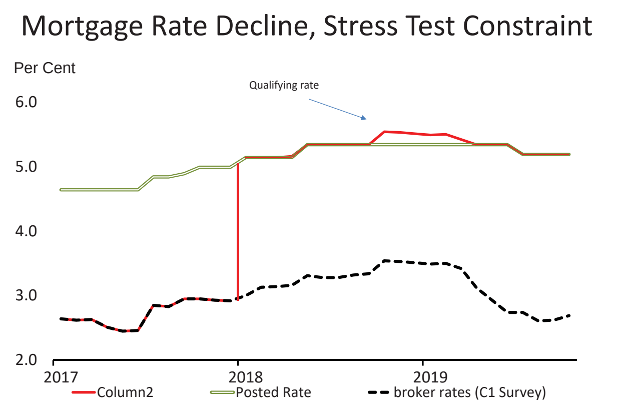
	2016	2017	2018	2019	2020	2021
Residential Transactions, Units	107,702	98,129	78,192	72,860	82,260	85,475
% ch.	17.1	-8.9	-20.3	-6.8	12.9	3.9
Residential Median Transaction Price	462,500	500,000	535,000	522,000	542,000	568,000
% ch.	8.1	8.1	7.0	-2.4	3.8	4.8
Housing Starts	41843	43664	40857	44,000	37,000	39,500
% ch.	33.1	4.4	-6.4	7.7	-15.9	6.8

Landcor, CMHC, Central 1 Credit Union, 2019-2021 forecast per cent. Federally regulated financial institutions and many other lenders are required to qualify purchasers at the higher of the posted rate or contract rate plus two per cent. For those with sufficient down payments, lower rates and prices are driving increased sales. The rate environment will continue to be favourable for buyers. We forecast at least one or possibly two cuts to the Bank of Canada's overnight rate in early 2020 and range-bound yield for five-year Government of Canada bonds. Mortgage rates will edge down further. A modest rebound in rates is expected in late 2020 and 2021, but levels will remain low.

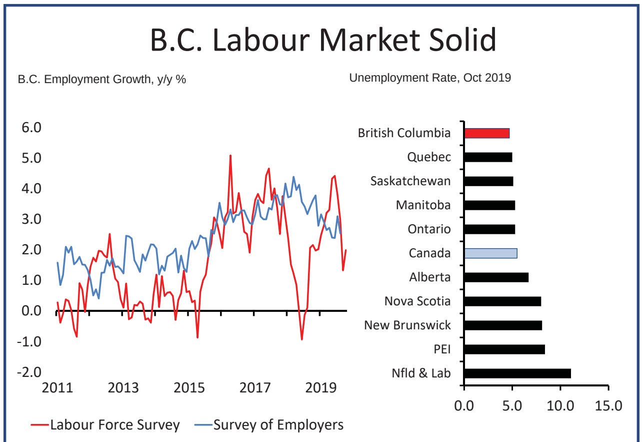
At the same time, the combination of low interest rates, strong levels of hiring and population gains are underpinning housing demand within B.C. Although economic growth slows this year to about a two per cent pace, with drag coming from exports and consumer demand, GDP growth is forecast to remain modest over the coming years, led by major project investment and other non-residential construction. Resource communities face more glaring challenges with a downturn in the forestry sector. Employment growth in the province remains at or near the top of the country, while labour shortages persist - highlighted by unemployment rates below five per cent - resulting in strengthening wage growth. Population is rising at a solid clip of 1.3 per cent driven by high levels of international migration, despite slowing in interprovincial flows. This trend will continue, reflecting federal government intake targets, business demand for skilled labour in a tight labour market environment, and demand for Canadian post-secondary education.

While mortgage stress tests are a constraint, housing demand is being lifted by federal programs such as the Canada Mortgage and Housing Corporation administered First-Time Home Buyer Incentive program which was launched in September and provides a shared equity mortgage for qualified buyers. The program will be particularly beneficial for markets outside Metro Vancouver given lower home prices and comparable incomes.

Home ownership remains out of reach for many households, at least temporarily due to demand constraining government policy. This will contribute to high levels of rental demand, persistence of low vacancy rates and rising rental rates. We anticipate an under supply of construction to emerge in the coming years in response to a weaker sales environment over the past two years which could set the stage for another round of price escalation and rental hikes.



Source: Bank of Canada, Statistics Canada, Central 1

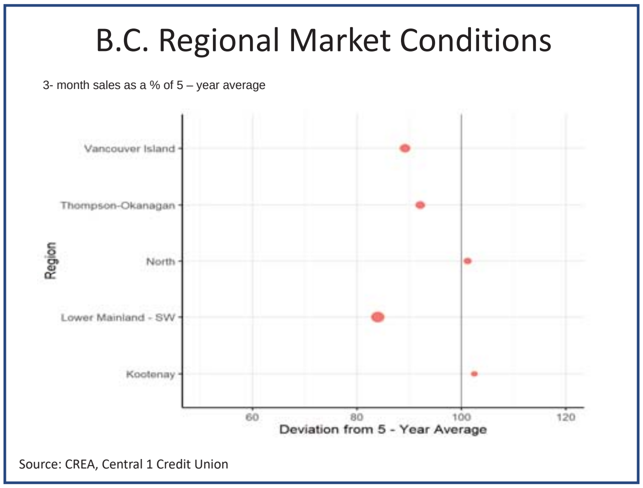


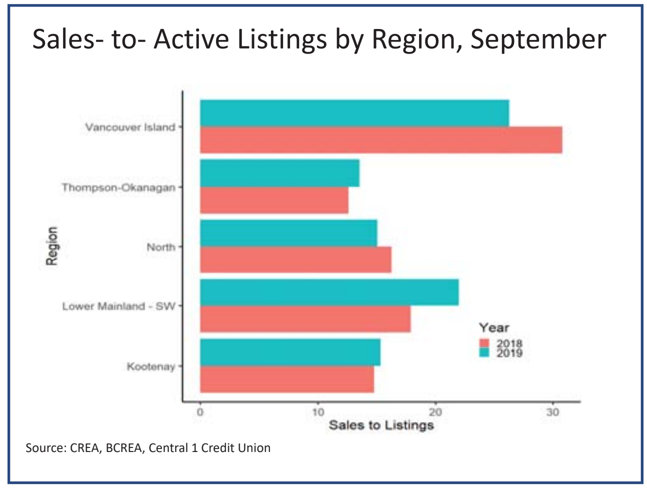
Source: Statistics Canada, Central 1 Credit Union

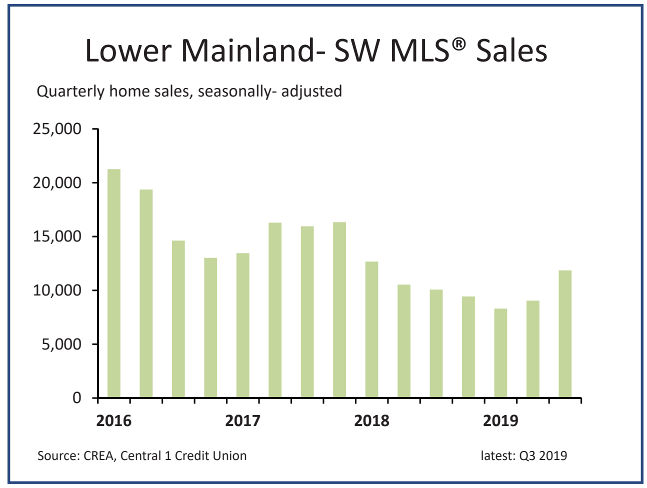
Resale market on the mend after punishing decline

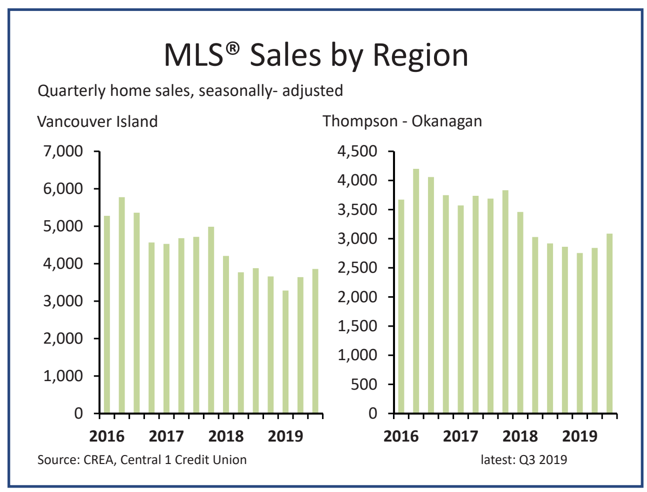
Home sales have returned to more normal levels following over a year of policy induced declines but B.C.'s sales recovery has lagged the rest of Canada. After plumbing recession-like depths in early 2019, MLS® sales have climbed, rebounding strongly since February and are trending near the 10-year average on improved affordability and solid economic conditions. That said, levels are still only 80 per cent of those observed prior to 2018 when mortgage stress tests came into effect, followed by further provincial measures in early 2019, aimed at diminishing demand.

Lower Mainland sales have turned higher after experiencing the brunt of the downturn. A growing number of buyers in the region have idled on the sidelines waiting for improvements in affordability following mortgage stress tests. Significant price declines over the past year and lower borrowing costs have buyers returning to the market among all housing types, particularly in the lower priced condominium sector. Upward sales momentum will likely continue into 2020. Sales in other parts of B.C. were less severely impacted by these









policies which targeted larger more expensive urban markets. Sales have similarly climbed but are still running 80 to 90 per cent of pre-2018 levels. Vancouver Island and some southern interior markets remain buoyed by aging demographics and inflows of semi-retirees, retirees and, to a lesser extent, affordability seekers looking outside the large urban markets. The more recent downturn in forestry sectors is beginning to bite on various local resource-driven economies and housing markets.

Rapid cooling of sales and deterioration of confidence in the housing market led to a significant price correction in Lower Mainland home values and flattening of price levels in most other regions of the province. That said, outside a few pockets in the Lower Mainland, specifically in the highest priced luxury segment, a housing crash this was not.

Dependent on price measure, resale home values in the Lower Mainland declined by about 10 per cent from peak 2018 levels, although magnitude has differed by product type and sub-regional area. On Vancouver Island, Victoria area prices have softened due to declines in the single-detached market, but other areas have continued to experience rising values following a temporary pullback in 2018. Similar price patterns have been observed in the Thompson-Okanagan, and in areas benefitting from large scale investments such as liquefied natural gas plants. Real estate markets in large urban areas have experienced the most significant impacts of government policy.

While the sales declines were deep in many regions, relative stability in home values and gains in some markets owe to low resale inventory. The downturn in the market did not trigger a wave of resale supply. In fact, new listings declined as owners moved to sidelines, minimizing upward pressure on inventory and, by extension, negotiating power on the part of buyers. Sales-to-active ratios have held firm in markets across the province at levels consistent with balanced to sellers' market conditions and are now rising, pointing to upward pressure on prices.

There remains some short-term risk of a temporary condominium oversupply in the Lower Mainland given high levels of units under construction which could enter into resale market inventory once completed, although a significant share of investor-owned units will likely end up in the rental pool.

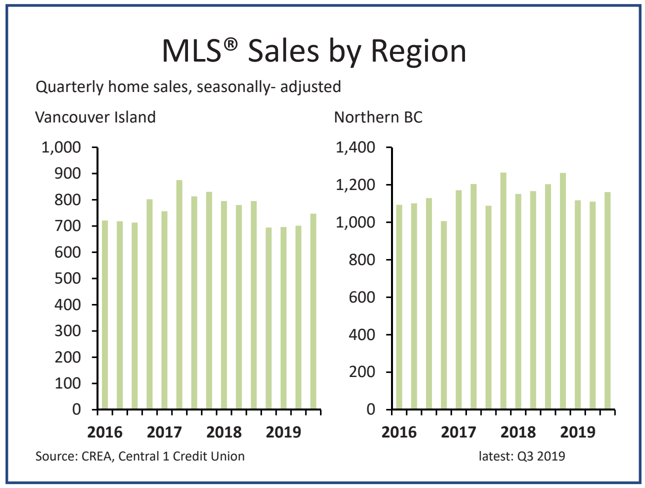
We have upgraded our resale market sales forecast and expect provincial resale transaction to reach 72,860 units this year, marking a seven per cent decline in annual sales, as opposed to our previous forecast for a 10 per cent decline this year. A more vigorous recovery in Lower Mainland sales accounts for most of the increase, with weaker northern B.C. sales cut from the previous outlook. Sales will continue to rise in 2020 and 2021. We expect provincial sales to rise 13 per cent in 2020, followed by a four per cent gain in 2021. This reflects growth in the economy, population, federal programs to support first time home purchases and persistence of low borrowing costs. However, we do not anticipate sales to recover to 2017 levels over the period when resale transactions were just shy of 100,000 units.

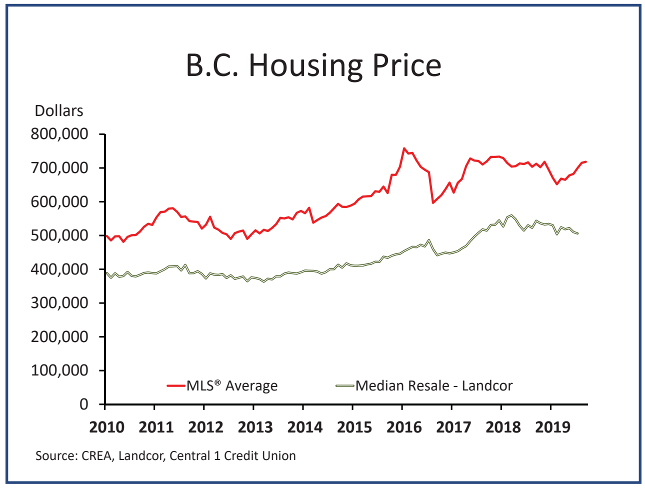
Rising sales and tightening market conditions will lead home values higher, particularly in this constrained supply environment. The provincial median home value for 2019 is still forecast to decline this year, but by a modest 2.4 per cent from 2018 to $522,000 as the trend turns higher. Declines reflect price declines in the larger urban markets, specifically due in Metro Vancouver and Kelowna. Relatively strong gains outside the large metro markets are a significant offset, with mid-sized markets such as Vernon, Kamloops and Prince George recording gains of more than five per cent. Small markets on Vancouver Island are also experiencing upward price momentum.

The stronger sales environment and retreating supply of units for sale in the province will contribute to upward price pressures in the coming year. While we will not see the gains of near 10 per cent observed in some markets in 2016 and 2017, the provincial median value is forecast to rise by 3.8 per cent next year and by more than four per cent in 2021 to $568,000. Metro Vancouver will lead this increase which will undoubtedly bring affordability challenges back in to the spotlight.

Housing starts defy expectations in 2019, pullback is anticipated

New home construction has surprised on the upside and continues to be a positive growth driver in B.C.'s economy. Confounding our early year expectations for a significant deterioration in activity, housing starts have been unscathed by the resale market downturn. A flurry of new construction will lift housing starts to about 44,000 units this year marking a eight per cent gain from 2018. Growth this year has predominantly been driven by a surge in condominium construction in the Vancouver CMA. Elevated construction of rental properties and non- market housing projects have also





boosted starts. Rental starts made up about 26 per cent of activity over the past two years, compared to less than 10 per cent 3-5 years ago reflecting higher rents and municipal incentives despite more stringent rent control measures.

This is not to say that the new home market has been unaffected by government policy headwinds. The lag between housing starts and development/building decisions has likely played a role. Many of the projects started this year were presold in prior years when market conditions were stronger. Long development cycles mean projects will go forward provided presale contracts are in place. Large projects are dominated by Metro Vancouver, which saw a 23 per cent increase in housing starts through the first three quarters on a year-to-date basis, compared to a one per cent increase in other urban markets. In contrast, the drag on current demand is visible in the 20 per cent decline in single-detached starts this year which have short build out periods and are built on contract.

We still anticipate the pace of housing starts to decline by nearly 16 per cent in 2020 to about 37,000 units, led specifically by a pullback in Metro Vancouver area condominium builds. A slump in presale activity this year will delay project construction in 2020 onwards, and we expect a curtailment in condo starts next year. Adding to sluggish presales is a higher level of units under construction and higher new home inventory than seen in prior years, which will drive further caution by builders. The speculation tax and other measures remain a constraint in larger urban markets across the province.

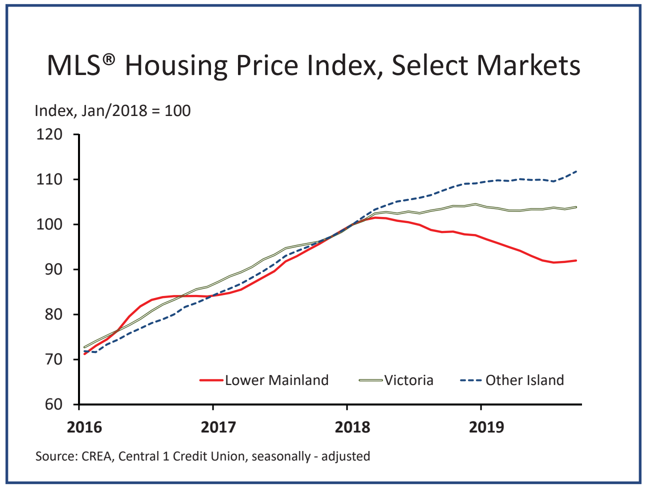
Nevertheless, demand drivers remain supportive of housing construction. While there is no way to be certain about the future, Statistics Canada population projections suggest plausible population growth of one per cent or more through 2030 representing average net gains of more than 55,000 persons per year. Immigration drives these increases, while the aging of the population is a natural offset. In the short-term, elevated inflows of immigration and temporary residents are likely to continue driving demand for both ownership and rental housing. Demand for retiree markets will continue to grow, as will the need for affordable multi-family units. Low mortgage rates will continue to support demand. An increase in housing starts to 39,500 in 2021 is forecast.

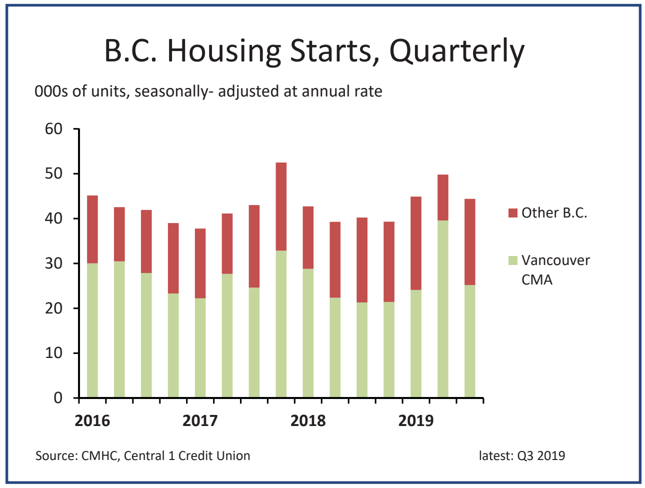
Rental market tightness to persist

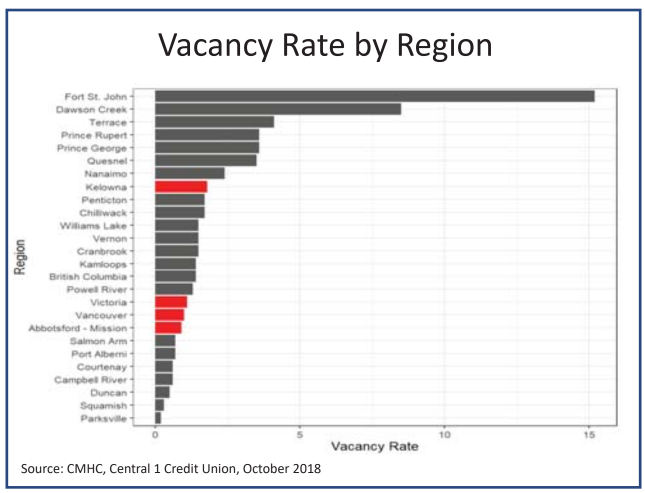
Decades of insufficient construction of purpose-built rental building, rising price trends over the past 10 years and a growing population and economy continue to underpin a tight rental market despite rising rental construction trends in recent years. Mortgage stress tests have further added to rental market pressure with some would-be purchasers having to delay their purchases decisions due to more stringent qualification rates.

Provincially, the purpose-built apartment and row unit rental vacancy rate has held below two per cent for the past five years. The latest values are from October 2018, with a rate of 1.4 per cent. This included rates of about one per cent in the largest urban areas of Metro Vancouver, Abbotsford- Mission and Victoria, while Kelowna's was slightly higher at 1.8 per cent owing to a period of rising rental construction. Trends across the province suggest low vacancy rates on Vancouver Island and southern interior markets, with higher rates in the northern interior.

Not surprisingly, scarce rental availability is driving rents higher. Same-sample rent growth exceeded six per cent for the first time on record last year with sharp gains across the province. Metro Vancouver rents rose 6.1 per cent, while gains in Victoria, Kelowna and Abbotsford-Mission exceeded eight per cent. With



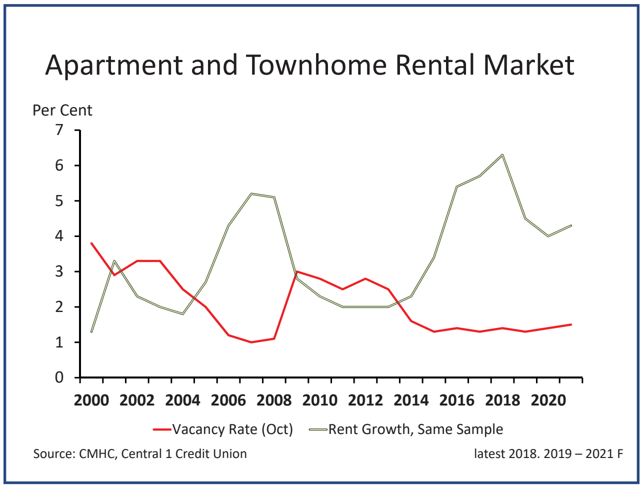




rent growth for existing tenants being constrained by rent control measures, turnover rents growth has been significantly stronger. Average condominium apartment rentals in Victoria and Vancouver rose five per cent, although changes in unit composition is a factor.

Rental unit construction has experienced a notable increase over the past three years as tight market conditions, higher rents, and policies at all levels of government have promoted construction. Approximately 25 per cent of housing starts and completions have been comprised of rental tenure since 2015, compared to less than 10 per cent during the 2000-2010 period. This has contributed to a modest increase in the purpose-built rental supply, although partially offset by demolition of existing stock. A portion of this construction also reflects social housing initiatives and secondary suites in single-detached homes. Additional rental supply is alleviating some pressure in the rental market.

Nevertheless, rent growth remains high. The consumer price index rent index accelerated 3.3 per cent this year, from 1.7 per cent in 2018 with stronger growth in both Vancouver and Victoria relative to other parts of B.C. Acceleration partly reflects changes in estimation methodology for rents introduced in January 2019, meaning year-over-year comparisons for 2019 are not entirely accurate. That said, the rental price index has risen at a quick pace this year. While headline rent growth will be constrained in part by controls on rent growth, turnover rent will remain strong. We forecast rent growth to trend in a range of 4.0 to 4.5 per cent annually with urban areas experiencing stronger hikes. Gains will largely reflect stronger turnover rents as existing tenants will be protected by rent control. A tight labour market and wage appreciation will blunt much of the impact on household budgets.



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Housing Forecast- Table 2

		2016	2017	2018	2019	2020	2021
Residential Transactions	All Units	127,509	117,510	96,180	89,860	99,760	102,475
	% ch	14.1	-7.8	-18.2	-6.6	11.0	2.7
	Resale Component	107,702	98,129	78,192	72,860	82,260	85,475
	% ch	17.1	-8.9	-20.3	-6.8	12.9	3.9
	New Component	19,807	19,381	17,988	17,000	17,500	17,000
	% ch	0.4	-2.2	-7.2	-5.5	2.9	-2.9
Median Price	All Units	456,650	500,000	537,951	535,000	550,000	569,000
	% ch	7.4	9.5	7.6	-0.5	2.8	3.5
	Resale Component	462,500	500,000	535,000	522,000	542,000	568,000
	% ch	8.1	8.1	7.0	-2.4	3.8	4.8
	New Component	434,610	498,900	542,000	570,000	565,000	570,000
	% ch	3.7	14.8	8.6	5.2	-0.9	0.9
MLS® Activity	Sales	112,411	103,957	78,505	75,500	87,000	92,000
	% ch	9.5	-7.5	-24.5	-3.8	15.2	5.7
	Listings	156,820	150,263	148,111	145,400	150,000	151,000
	% ch	2.8	-4.2	-1.4	-1.8	3.2	0.7
	Average Price	690,403	708,890	711,646	692,000	715,000	730,000
	% ch	8.6	2.7	0.4	-2.8	3.3	2.1
Housing Starts, Units	Total	41,843	43,664	40,857	44,000	37,000	39,500
	% ch	33.1	4.4	-6.4	7.7	-15.9	6.8
	Single-Detached	12,278	12,346	11,163	8,400	8,800	9,000
	% ch	20.9	0.6	-9.6	-24.8	4.8	2.3
	Multi-family	29,565	31,318	29,694	35,600	28,200	30,500
	% ch	38.8	5.9	-5.2	19.9	-20.8	8.2
Urban Housing Starts by Tenure	Total	39,498	41,191	38,439	41,800	35,000	37,500
	% ch	32.0	4.3	-6.7	8.7	-16.3	7.1
	Freehold/Condo	29,703	31,702	26,897	31,000	25,000	28,000
	% ch	22.2	6.7	-15.2	15.3	-19.4	12.0
	Rental	9,705	9,489	11,542	10,800	10,000	9,500
	% ch	73.1	-2.2	21.6	-6.4	-7.4	-5.0
Vacancy Rate (%)	Row/Apartment	1.4	1.3	1.4	1.3	1.4	1.5
Average Rent, % Ch., Fixed Sample	Row/Apartment	5.4	5.7	6.3	4.5	4.0	4.3

Landcor, CMHC, CREA, Central 1 Credit Union, 2019-2021 forecast

Annual Residential Resale Transactions

	2016	2017	2018	2019	2020	2021
Vancouver Island/Coast	19,624	18,017	14,881	14,000	15,000	15,500
% ch	31.7	-8.2	-17.4	-5.9	7.1	3.3
Lower Mainland/Southwest	65,575	57,281	42,307	39,000	46,000	48,000
% ch	13.5	-12.6	-26.1	-7.8	17.9	4.3
Thompson/Okanagan	15,086	14,518	12,301	11,500	12,600	13,000
% ch	25.2	-3.8	-15.3	-6.5	9.6	3.2
Kootenay	3,259	3,670	3,665	3,450	3,600	3,700
% ch	20.7	12.6	-0.1	-5.9	4.3	2.8
Cariboo	2,584	2,838	2,768	2,750	2,800	2,900
% ch	7.4	9.8	-2.5	-0.7	1.8	3.6
North Coast	639	659	935	850	870	925
% ch	-10.6	3.1	41.9	-9.1	2.4	6.3
Nechako	413	479	518	510	550	550
% ch	-20.3	16.0	8.1	-1.5	7.8	0.0
Northeast	522	661	811	800	840	900
% ch	-42.7	26.6	22.7	-1.4	5.0	7.1
Province	107,702	98,129	78,192	72,860	82,260	85,475
% ch	17.1	-8.9	-20.3	-6.8	12.9	3.9

Annual Residential Resale Transactions by CMA/CA

	2016	2017	2018	2019	2020	2021
Vancouver CMA	54,123	47,174	34,806	32,300	38,500	40,000
% ch	8.9	-12.8	-26.2	-7.2	19.2	3.9
Abbotsford-Mission CMA	4,840	4,199	3,093	2,850	3,150	3,400
% ch	46.9	-13.2	-26.3	-7.9	10.5	7.9
Victoria CMA	8,485	7,272	5,817	5,850	6,500	7,000
% ch	35.8	-14.3	-20.0	0.6	11.1	7.7
Kelowna CMA	6,149	5,353	4,281	3,950	4,250	4,500
% ch	24.0	-12.9	-20.0	-7.7	7.6	5.9
Chilliwack CA	3,445	3,259	2,411	2,100	2,250	2,400
% ch	53.9	-5.4	-26.0	-12.9	7.1	6.7
Nanaimo CA	2,950	2,796	2,306	2,000	2,100	2,200
% ch	26.7	-5.2	-17.5	-13.3	5.0	4.8
Vernon CA	1,786	1,783	1,543	1,420	1,475	1,550
% ch	40.5	-0.2	-13.5	-8.0	3.9	5.1
Penticton CA	1,527	1,551	1,251	1,200	1,250	1,290
% ch	20.0	1.6	-19.3	-4.1	4.2	3.2
Kamloops CA	2,357	2,492	2,285	2,100	2,200	2,300
% ch	23.0	5.7	-8.3	-8.1	4.8	4.5
Prince George CA	1,485	1,654	1,523	1,600	1,600	1,675
% ch	1.2	11.4	-7.9	5.1	0.0	4.7
For St. John CA	259	304	383	390	420	450
% ch	-48.2	17.4	26.0	1.8	7.7	7.1
Cranbrook CA	479	466	507	500	520	530
% ch	10.1	-2.7	8.8	-1.4	4.0	1.9

Landcor, Central 1 Credit Union, 2019-2021 forecast

Median Annual Residential Price

	2016	2017	2018	2019	2020	2021
Vancouver Island/Coast	382,500	420,000	463,000	479,000	495,000	510,000
% ch	9.3	9.8	10.2	3.5	3.3	3.0
Lower Mainland/Southwest	599,000	640,000	695,000	645,000	670,000	710,000
% ch	10.9	6.8	8.6	-7.2	3.9	6.0
Thompson/Okanagan	355,000	380,000	400,000	420,000	430,000	450,000
% ch	6.3	7.0	5.3	5.0	2.4	4.7
Kootenay	244,000	259,000	274,000	294,000	305,000	315,000
% ch	2.1	6.1	5.8	7.3	3.7	3.3
Cariboo	226,750	239,000	255,000	275,000	285,000	290,000
% ch	2.2	5.4	6.7	7.8	3.6	1.8
North Coast	240,000	240,000	255,000	285,000	290,000	300,000
% ch	0.0	0.0	6.3	11.8	1.8	3.4
Nechako	189,500	209,000	215,750	223,000	235,000	240,000
% ch	3.8	10.3	3.2	3.4	5.4	2.1
Northeast	271,500	285,000	269,500	260,000	275,000	285,000
% ch	-9.5	5.0	-5.4	-3.5	5.8	3.6
Province	462,500	500,000	535,000	522,000	542,000	568,000
% ch	8.1	8.1	7.0	-2.4	3.8	4.8

Median Annual Residential Price by CMA/CA

	2016	2017	2018	2019	2020	2021
Vancouver CMA	668,000	690,000	740,000	690,000	715,000	760,000
% ch	14.2	3.3	7.2	-6.8	3.6	6.3
Abbotsford-Mission CMA	464,000	510,000	560,000	550,000	545,000	570,000
% ch	22.9	9.9	9.8	-1.8	-0.9	4.6
Victoria CMA	506,000	554,000	600,000	600,000	612,000	635,000
% ch	6.8	9.5	8.3	0.0	2.0	3.8
Kelowna CMA	432,000	480,000	525,000	518,000	522,000	545,000
% ch	9.4	11.1	9.4	-1.3	0.8	3.8
Chilliwack CA	368,900	429,900	489,500	487,000	495,000	510,000
% ch	18.6	16.5	13.9	-0.5	1.6	3.0
Nanaimo CA	343,450	395,000	431,500	440,000	450,000	465,000
% ch	8.9	15.0	9.2	2.0	2.3	3.3
Vernon CA	354,600	370,000	386,800	415,000	420,000	430,000
% ch	10.8	4.3	4.5	7.3	1.2	2.4
Penticton CA	323,000	350,000	366,000	390,000	400,000	408,000
% ch	8.0	8.4	4.6	6.6	2.6	2.0
Kamloops CA	336,502	362,450	382,000	415,000	430,000	440,000
% ch	1.5	7.7	5.4	8.6	3.6	2.3
Prince George CA	255,000	265,000	288,765	315,000	321,000	330,000
% ch	5.4	3.9	9.0	9.1	1.9	2.8
For St. John CA	335,000	339,000	328,900	308,000	315,000	325,000
% ch	-4.7	1.2	-3.0	-6.4	2.3	3.2
Cranbrook CA	250,000	270,000	295,000	300,000	305,000	313,000
% ch	0.0	8.0	9.3	1.7	1.7	2.6

Landcor, Central 1 Credit Union, 2019-2021 forecast