



In Focus

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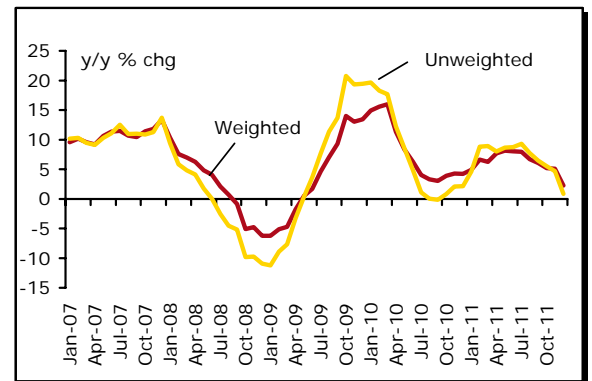
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The Housing Market—A Clear Softening Trend

There are clear signs that the Canadian housing market is softening. While sales activity rose by 1.8% in December 2011, the number of new listed homes rises by 3%. This led to a modest decline in the national sales to new listing ratio from 55.5 to 54.8. Clearly this is still a well-balanced picture, but the trend is of a slowing market.

As for prices, the 0.9% (y/y) increase in December was the slowest pace since October 2010. On a 3-month moving average basis, the national average price is now rising by 3.6%—again the slowest pace since late 2010, revealing a clear slowing trajectory. Note that the softening trend is in both the simple average measure and the weighted average measure of house prices, suggesting that the softening is more general in nature. However the widening gap between the weighted measure and the simple average measure suggests that high-end properties in large centers experience somewhat more significant pressures. And this trajectory will continue in the coming months, reflecting a generally slowing market but also the fact that the surge in sales of high-end properties seen in early 2011 is unlikely to repeat—a factor that will work as a negative for prices in the near term. In fact, it is highly probable that the first quarter of 2012 will see the first year-over-year decline in prices since the recession. This is already happening in BC, where the year-over-year measure was down by 1.7% in December—the first decline since June 2009.

Chart
National Residential Average Price



Source: CREA, CIBC

While we do not see house prices crashing, we do believe that house prices in Canada will level off in the near future and might start trending downward modestly. Further out, the most likely scenario is that the eventual increase in interest rates will lead to a decline in prices (probably in the magnitude of 10%-15%). But given the current balanced affordability position, the more significant adjustment will be in housing market fundamentals that are likely to catch up with prices in the coming years—paving the way for a healthier housing market later in the decade.

Indeed a softening in house prices in the next year or so is a necessary condition for such a soft-landing scenario. If the pace of house price increases accelerates during that period, then a year or two from now the likelihood of a violent price correction will be higher than it is now.

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