Unsold Condo Units in the GTA Market—An Assessment of Vulnerability

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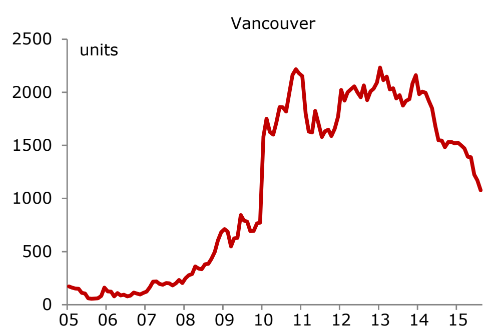
It's well established by now that the condo markets in both Vancouver and Toronto acted as stabilizing forces, by alleviating the pressure due to lack of land supply, and by introducing an element of affordability to ultra-expensive low-rise markets. But is it too much of the good thing?

The big question is to what extent the condo markets in both centres are overshooting. The answer, of course, is multi-dimensional, but a good starting point is to assess the trajectory of recently completed and unabsorbed units. An increase here suggests that developers are finding it increasingly hard to sell completed units—usually a first sign of troubles ahead.

Focusing only on that matrix, the situation in Vancouver is actually improving with the number of unabsorbed units falling over the past year from just over 2,000 to the current 1,100 (Chart 1). The situation in Toronto is much more interesting. Between December 2014 and May of this year, the number of unabsorbed units rose from less than 1,000 to close to 3,000—a level that is even higher than those seen in the early 1990s (Chart 2). This meteoric assent was not only highlighted by the Bank of Canada as a sign of vulnerability but also by various short-Canada investors—using that surge as the ultimate illustration of the bubbly Toronto condo market.

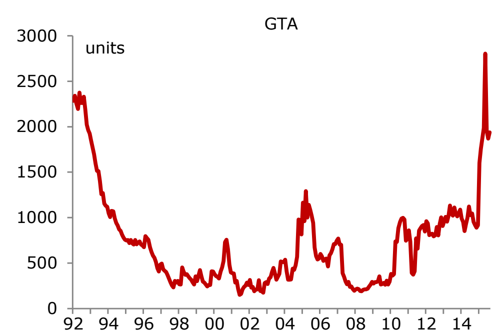
As you can observe from another look at Chart 2, since then we have seen another dramatic move, with the number of unabsorbed units falling by over 800 in only one month. In absence of an economic shock this kind of volatility is suspicious at best.

Chart 1
Completed and Unabsorbed Apartments



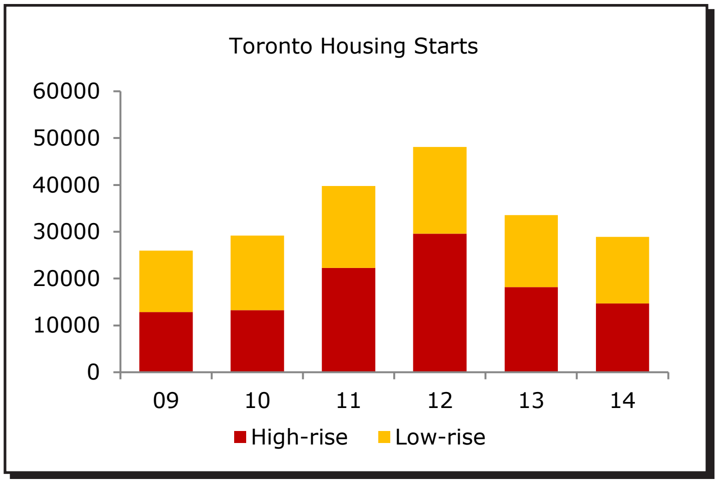
Source: CMHC, CIBC

Chart 2
Completed and Unabsorbed Apartments



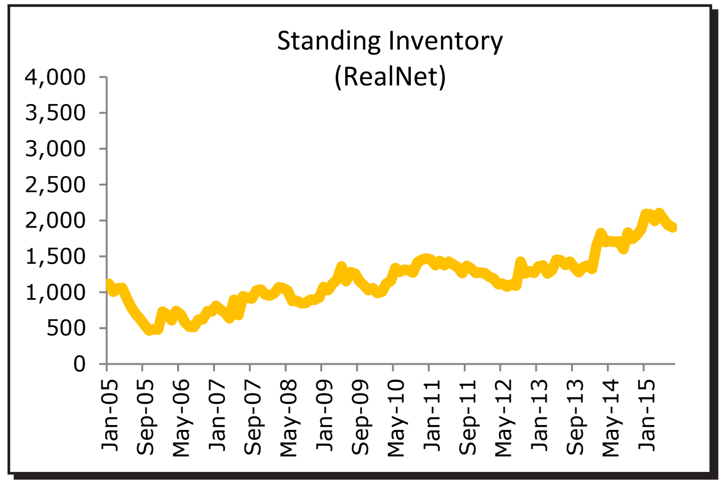
Source: CMHC, CIBC

Chart 3
Record Starts in 2012



Source: CMHC, CIBC

Chart 5
Toronto's Unabsorbed Condo Units—
Alternative Measures Are Less Volatile

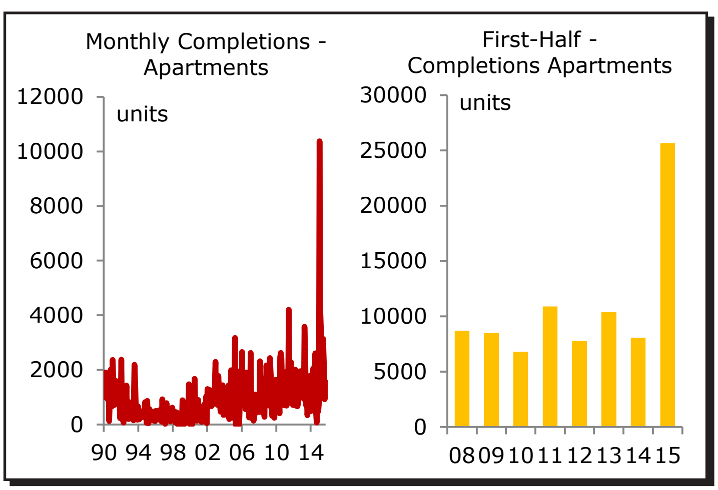


Source: RealNet, CIBC

So what's happening here? A quick glance at Chart 3 might give us a clue. In 2012 the GTA registered a record number of housing starts (just under 50,000) of which close to 30,000 were condos. When you start you usually complete. So towards late 2014 and early 2015 we have seen a notable increase in the number of completions. Now, registering a completion is more art than science, as different data providers use different criteria. And for some reason, CMHC has decided to register no less than 10,000 completions in the month of January alone. As can easily be seen in Chart 4, such a level is highly abnormal. According to CMHC, the GTA has seen no less than 26,000 condo completions in the first half of the year—three times more than the level seen in previous years. Other data providers such as RealNet have chosen to distribute their completion count more evenly—a fact that resulted in a less volatile count of unabsorbed units (Chart 5).

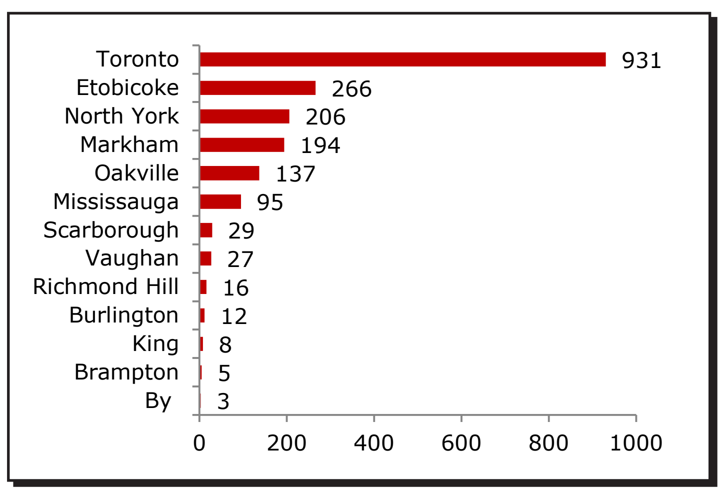
So now, after the recent decline in the CMHC measure, both measures (CMHC and RealNet) show roughly the same number of unabsorbed units—around 2,000—clearly higher than it was a year ago, but without the drama.

Chart 4
GTA Completions—
Do You Spot Something Abnormal?



Source: CMHC, CIBC

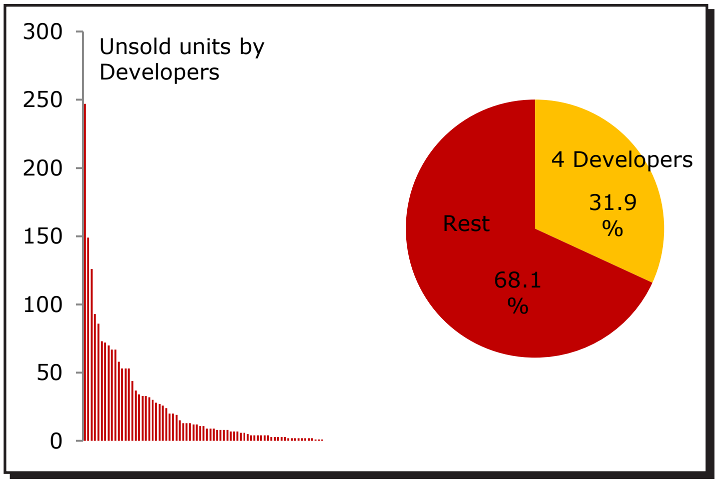
Chart 6
Apartments—
Completed and Unabsorbed



Source: RealNet, CIBC

Chart 7

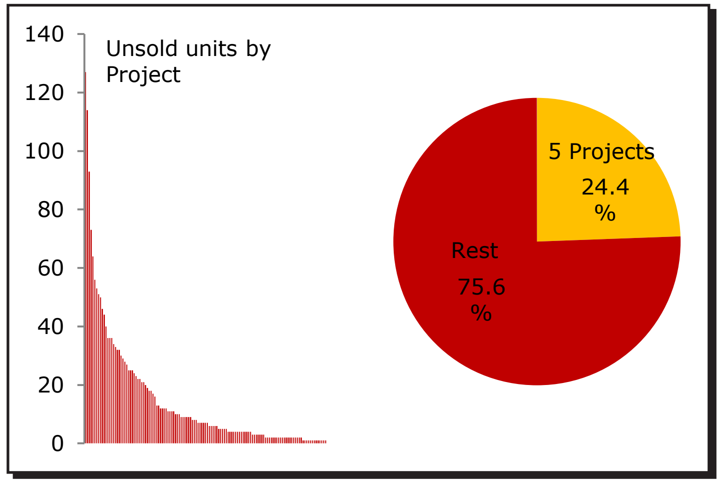
Completed and Unabsorbed Apartments by Developers—An Uneven Distribution



Source: RealNet, CIBC

Chart 8

Completed and Unabsorbed Apartments by Projects



Source: RealNet, CIBC

After establishing what the correct number is, we can dig deeper and look at the distribution of those unabsorbed units. No surprise that the city of Toronto accounts for roughly half of that count (Chart 6). What is more surprising is the distribution of those units by developers and by projects. A quick glance at Chart 7 reveals a distribution that is hardly uniform. In fact, almost one-third of all unabsorbed units in the GTA are concentrated among only four developers (out of 77). By project, the situation is not very different. One quarter of all unabsorbed units are concentrated among five projects (out of 139) (Chart 8).

To be sure, the GTA's condo market will be tested as interest rates start rising in the coming years, and increased resale activity from domestic condo investors will result in excess supply and some downward pressure on prices. But for now, those who look at the rise in unabsorbed units as a sign of increased vulnerability are barking up the wrong tree.