THE SARETSKY REPORT

MAY 2021

SARETSKY
GROUP

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OPENING THOUGHTS

Let me paint a picture for you. Last May, at the onset of the pandemic, economic and housing activity completely shuts down. The world goes into panic mode. In an effort to prevent an economic depression and a wave of defaults, the government along with the central bank, decide to essentially print money and hand it out to anyone who needs it. When the economy begins to re-open in June/July and with people still largely constrained to staying home, people decide they need more space and or a change of scenery. What ensues is an unprecedented migration, people start moving, and why not? Life is short, money is cheap and the banks are happy to lend. A national housing boom gripes the nation, home prices accelerate at their fastest clip ever.

Fast forward nearly a year later, record sales, record prices, and a ton of buyer demand pulled forward. What's left? Fewer buyers.

Finally there is light at the end of the tunnel, the pandemic could be nearing an end. Over 65% of Canadians have received at least one dose of vaccine. Social distancing rules are easing, restaurants and bars are re-opening, and people are desperate to get out of the house. With that in mind, doesn't it seem logical to expect house shopping to take less of a priority moving forward? Remember the bulk of home purchases over the past year were heavily influenced by the pandemic.

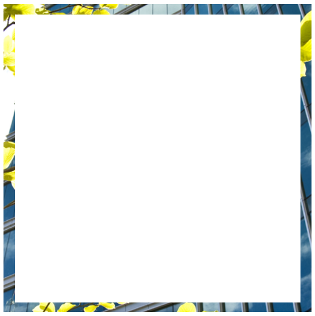
So here we are. If you had read The Saretsky Report last month you'll notice I highlighted a gradual slowdown forming across all levels of the housing market. Sure enough, that sentiment is now shared across the industry. Lets start at the national level before shifting over to Vancouver. National home sales fell 12.5% month-over-month in April, and once May sales figures are released it will likely note another monthly decline. Don't get me wrong the headlines still look great, and the market remains strong, however, March was in fact the top for sales activity. This doesn't mean prices will start falling, at least not yet. In fact, you're likely to see the opposite in the coming months. The national home price index has always been a lagging indicator, usually by 3-5 months. In other words, national home prices which were up 23% year-over-year in April will probably rise to 25% or more in the coming months. What comes after that is surely a deceleration in price growth.

It's a similar story here in Vancouver. Slowing sales, more inventory, fewer offers. Home sales, when compared to last May during the start of the pandemic, were up 185%. However, when we zoom out, we can see this was only the sixth strongest month of May over the past 20 years. (insert chart) Meanwhile, new listings remain elevated, surging 93% from last year and coming in at the second strongest over the past 20 years. Prices, as measured by the home price index will continue to trend higher in the coming months, but again, this is a lagging indicator. The reality is, if you're selling a house today you're probably not getting as much as you would have back in February or March when inventory was in short supply.

Moving forward the housing market is still in good shape but will undergo a stress test, literally and figuratively. The increased mortgage stress test is now in place, reducing borrowing power by about 4.5%. Further, year-over-year base effects will get hard to beat from July onwards. What I mean by this is it is almost a certainty that home sales will decline on a year-over-year basis from July through December.

In summary, a much needed cooling appears underway. However, monetary policy remains accommodative, and government policy will likely remain favourable for the rest of the year when you consider that residential investment was responsible for 54% of GDP growth in the first quarter. Housing continues to be the pillar for the economic recovery plan.

Steve

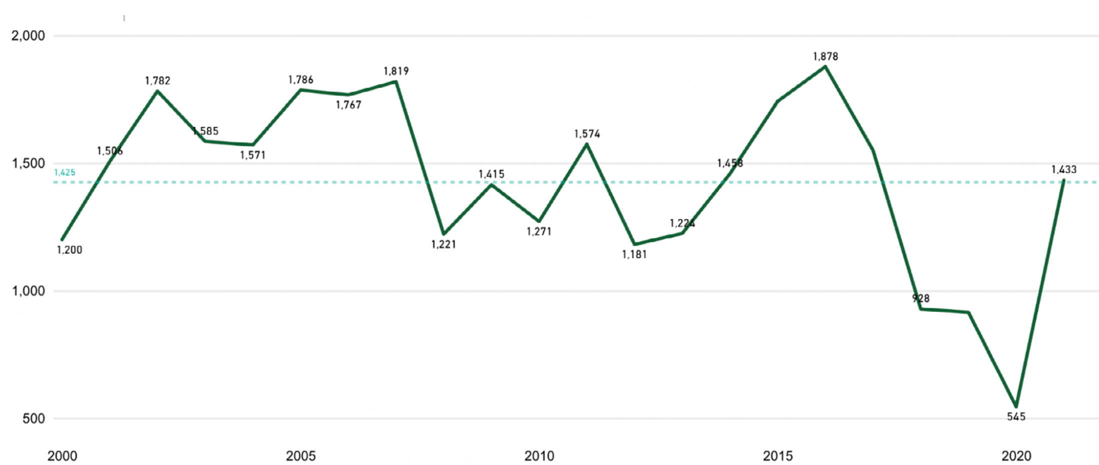


DETACHED HOUSING MARKET UPDATE

The detached market has been responsible for the majority of the strength in the housing market. While sales were up 163% from last year due to weak base effects, they were ultimately right in line with the 20 year average for the month.

Greater Vancouver Detached Sales in May

Source: REBGV, Steve Saretsky



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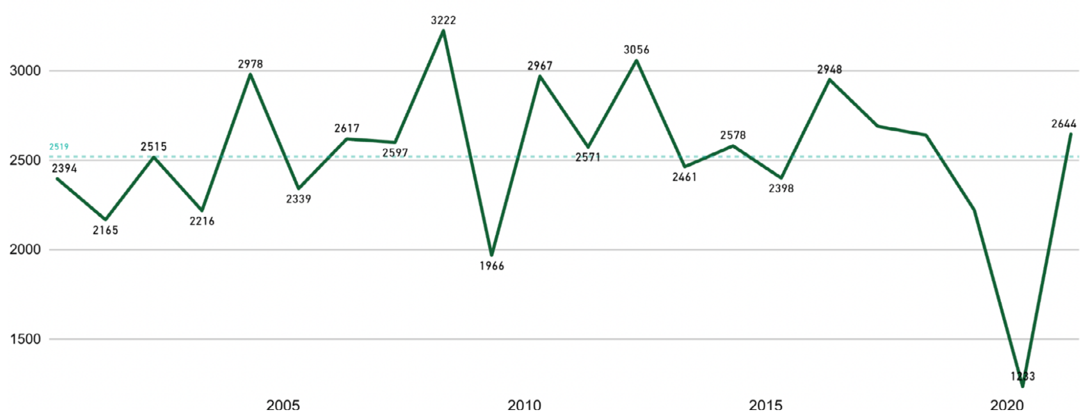
Sales are slowing and so too are new listings. Keep in mind this is part of a seasonal trend as housing activity typically always slows heading into the summer months. New listings were up 114% from last year but have contracted for two consecutive months.

Greater Vancouver Detached New Listings in May

Source: REBGV, Steve Saretsky



What's most important here is that months of inventory for sale is growing, releasing pressure on the housing market. This is encouraging news for buyers as the months of inventory has grown from 2 in March to 3.4 in May. We reach a balanced market at 4 months of supply.

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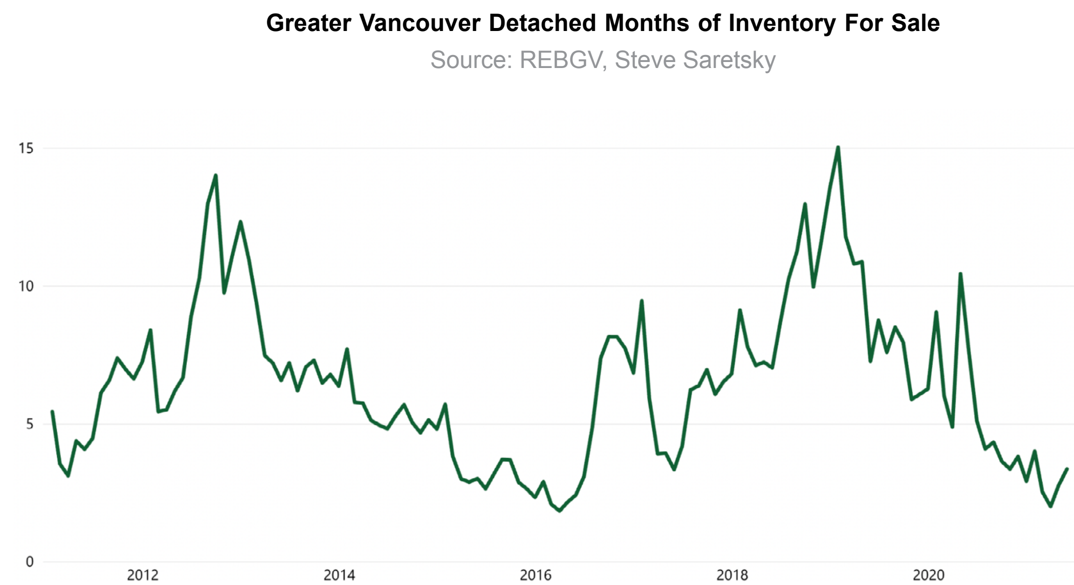
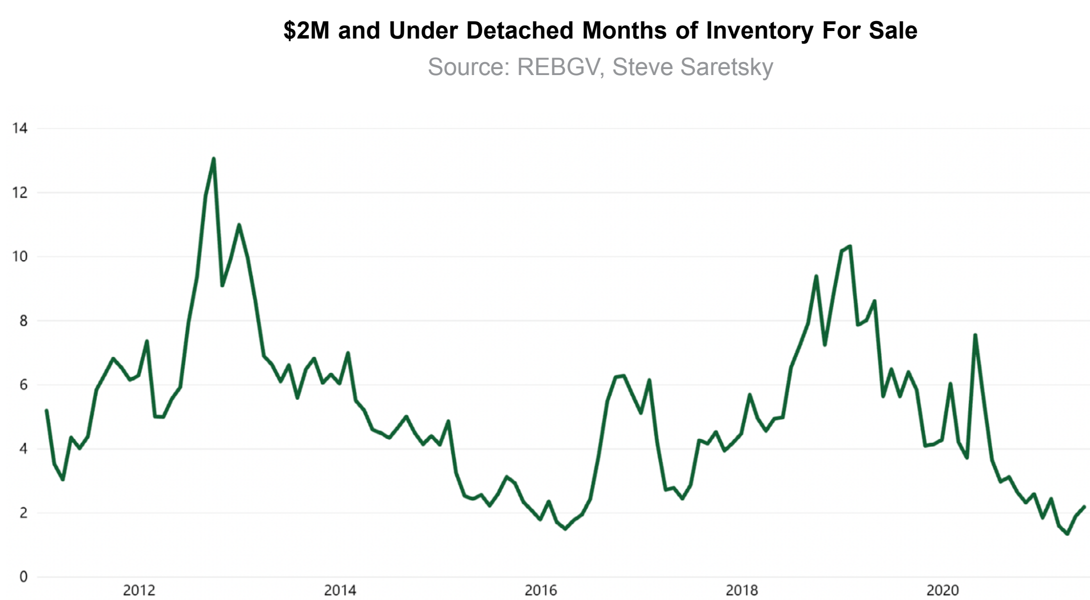


While inventory conditions are improving, things remain incredibly tight in the $2M and under detached housing market. Months of inventory for sale sits at just 2.2, however that's up from a record low of 1.3 in March.



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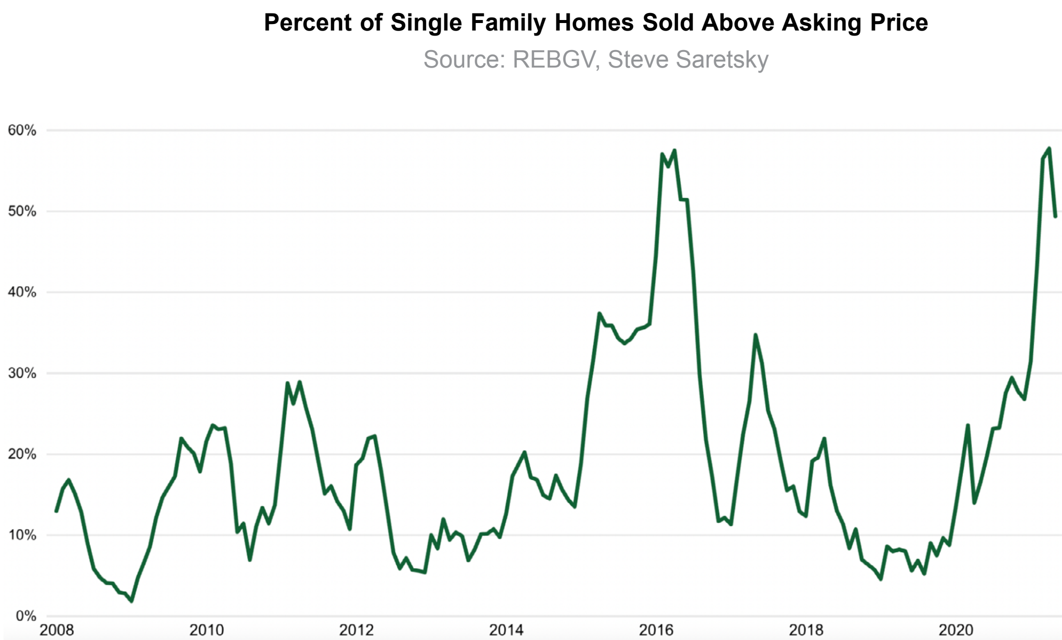
As inventory slowly recovers it is beginning to ease the number of bidding wars. Back in February/ March it wouldn't be uncommon to see a house get 7-8 offers for example. Today a similar house is fetching around 2-3 offers. Still competitive, but less of a frenzy. This is showing up in the percentage of listings sold above the asking price, which slipped down to 49% in May.



That takes us to prices. While the recent increase in inventory is helping to ease price growth, the home price index continues to march higher. The HPI for Greater Vancouver detached homes is now up 23% from last year.

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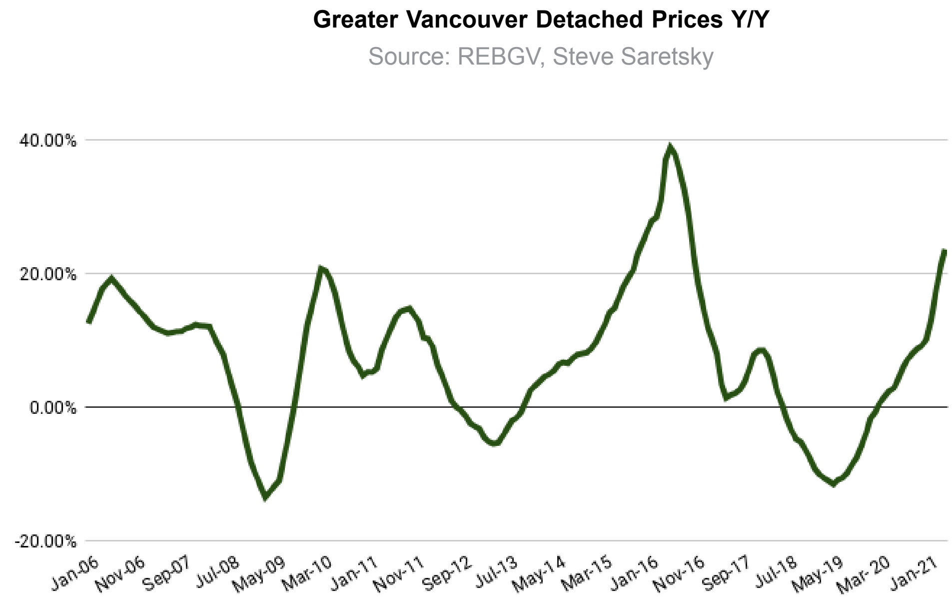
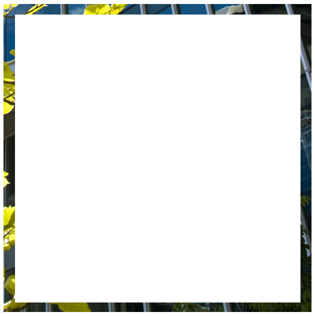


Similar to my comments in last months report, the detached market has arguably peaked for this cycle. However, it remains a sellers market and buyers can still expect competition on houses, particularly at the entry levels.



CONDO HOUSING MARKET UPDATE

Greater Vancouver condo sales had a massive jump, growing 212% from last May due to weak base effects. Even without the weak base effects this was still the second best May for condo sales in the last 20 years.

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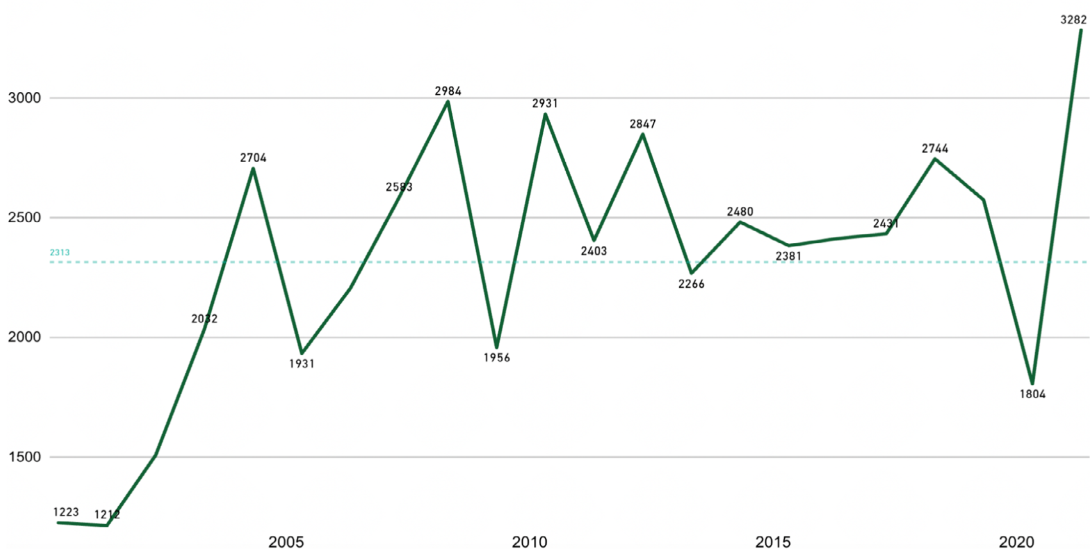
This was another huge month for new listings, setting a new record for the month of May with over 3000 new condo listings.

Greater Vancouver Condo New Listings in May”

Source: REBGV, Steve Saretsky



So we have really strong sales and record new listings, what does this all mean? Months of inventory for sale helps to cut through the noise here. There is just 2.3 months of inventory for sale in the condo market, indicative of a sellers market.

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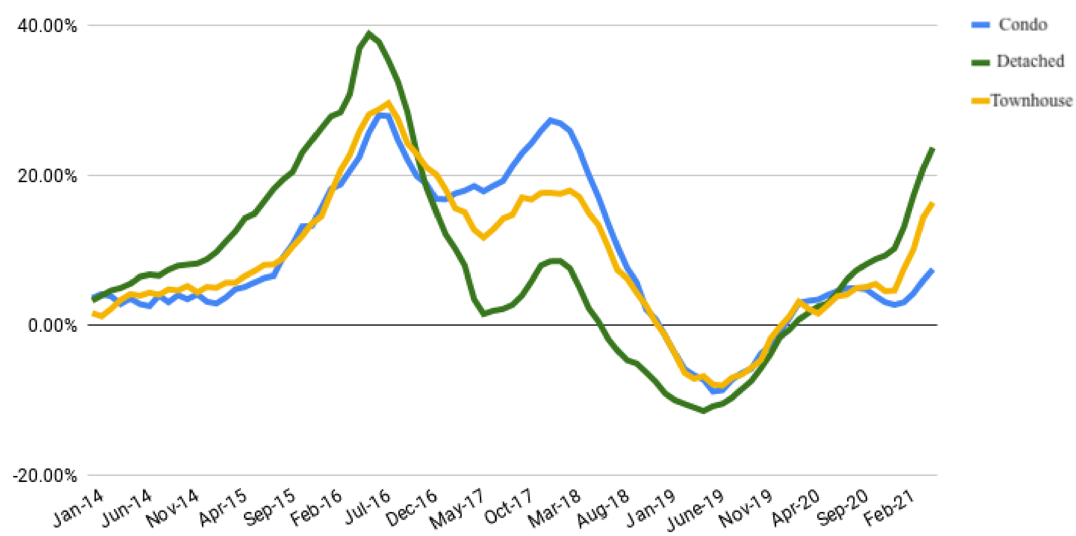
Months of Inventory For Sale

Source: REBGV, Steve Saretsky

We are going to need a lot more inventory to slow condo price growth, which is now playing catch up with the detached and townhouse markets. Condo prices are up 7% year-over-year but still lagging the rest of the market.

Price Growth Y/Y

Source: REBGV, Steve Saretsky



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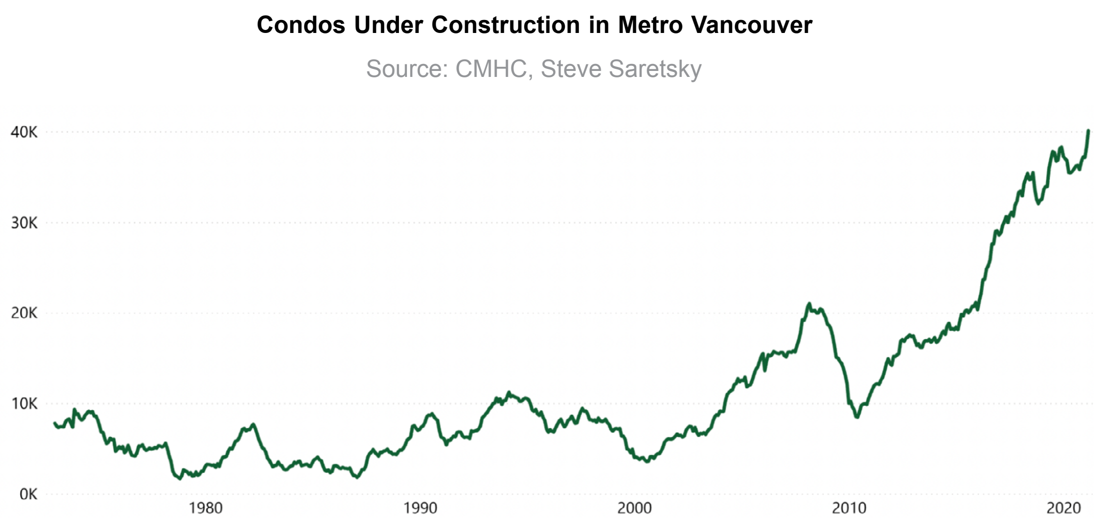
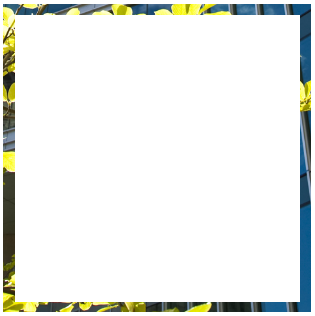
One thing that might ultimately keep condo prices from catching up is the number of new condos under construction. These condos will eventually complete and a chunk of them will land on the resale market. This is worth keeping an eye on in the next couple of years



For now the condo market remains strong and based on current inventory levels, higher prices seem inevitable in the very near term.



BUILDING SAVINGS BY TAKING ON DEBT?

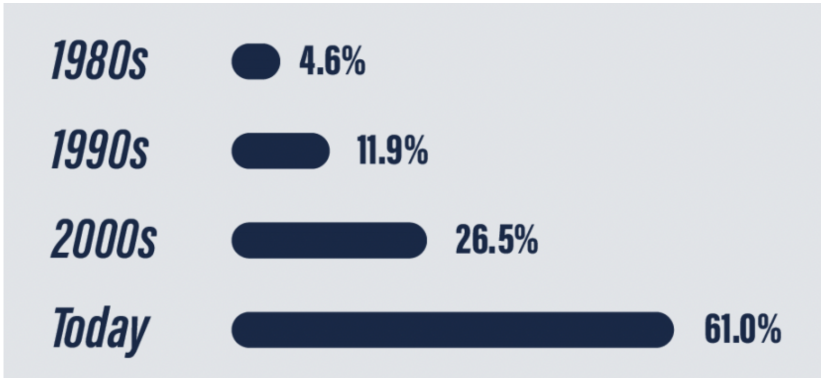
I remember watching an interview with CIBC's chief economist, Benjamin Tal, about a month ago. Tal said that nearly 40% of recent condo investors in Toronto were cash flow negative on their investments. According to research from CIBC & Urbanation, investors are viewing these negative cash flow condos as savings vehicles for the long run. I thought this was absolutely insane on the surface, but I think there are some interesting take-aways here.

Firstly, I do not recommend investing in negative cash flow properties but lets dissect this a little further. Right now, you can borrow at 1.5% on a variable rate mortgage. Not bad when you consider Canada's M2 Money supply growth has expanded by nearly 20% in a year, this is outright currency debasement. Then we look further and see that CPI inflation recently ticked in at 3%. This means REAL mortgage rates today are effectively -1.5% (inflation rate minus borrowing rate). Essentially you are being compensated to take on debt.

Ok, now lets get into the more technical aspects. Per research from Edge Analytics, due to insanely low mortgage rates today, 61% of the average homeowner's very first mortgage payment goes towards paying off the principal. This was just 4.6% in the 1980's and 11.9% in the 1990's.

Percent of First Mortgage Payment Towards Principle

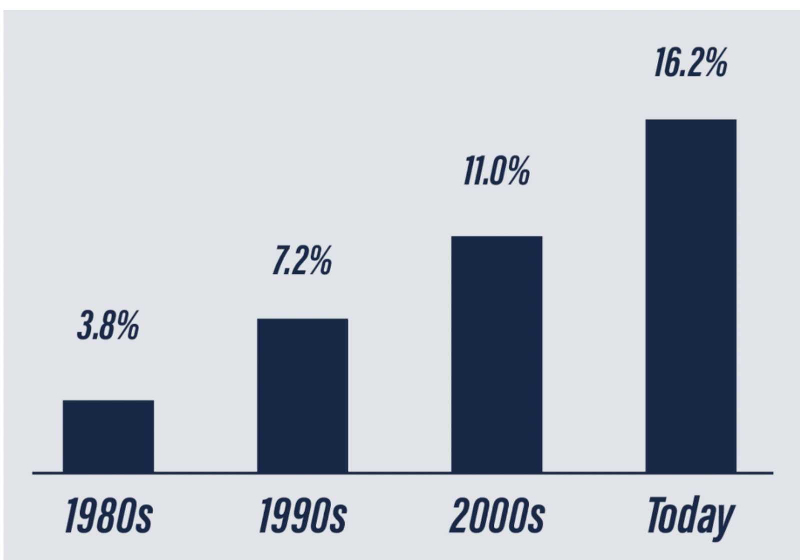
Source: Edge Analytics



To put this into perspective, at the end of a standard 5 year mortgage term, homeowners in the 1980's paid off just 3.8% of the outstanding mortgage. At today's ultra low interest rates homeowners now pay off 16.2% of their total mortgage in the first 5 years on average.

Percent of Total Mortgage Paid Off After 5 Years

Source: Edge Analytics



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I think there are a lot of perverse negative consequences of zero/negative interest rates. However, there's no denying that it encourages and ultimately rewards investors to take on debt, while ultimately punishing savers. This is exactly the opposite of what most of us were taught in school or by our parents.

ABOUT STEVE

Steve Saretsky is a Vancouver residential Realtor and author behind one of Vancouver's most popular real estate blogs. Steve is widely considered a thought leader in the industry with regular appearances on BNN, CBC, CKNW, CTV and as a contributor to BC Business Magazine. Steve has advised developers, hedge funds, and fund managers on the Vancouver housing market and is a regular speaker at industry events.

Steve Saretsky provides real estate services throughout Greater Vancouver. To inquire about listing or buying a property, please email: steve@stevesaretsky.com.

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