

# H

# OUSING NOW

Canada

## YOUR LINK TO THE HOUSING MARKET

Canada Mortgage and Housing Corporation

www.cmhc.ca

### Canadian Market Overview

OCTOBER 2005

#### New Home Market

##### *Housing starts up sharply*

The seasonally adjusted annual rate<sup>1</sup> of housing starts was 229,600 units in September, up from 205,400 units in August.

Housing starts across Canada remain strong and are on track with our expectations for the year. Low mortgage rates and increasing full-time employment in recent years are continuing

to fuel high levels of housing starts in 2005.

##### *Both urban single and multiple starts rose in September*

The seasonally adjusted annual rate of urban starts rose 13.8 per cent to 199,800 units in September, due to strong increases in both multiple and single starts. Multiple starts rose 17.6 per cent to 103,400 units, while single starts were up 9.9 per cent to 96,400 units in

continued on page 2...

#### In this Issue:

Canadian Market Overview ..... 1

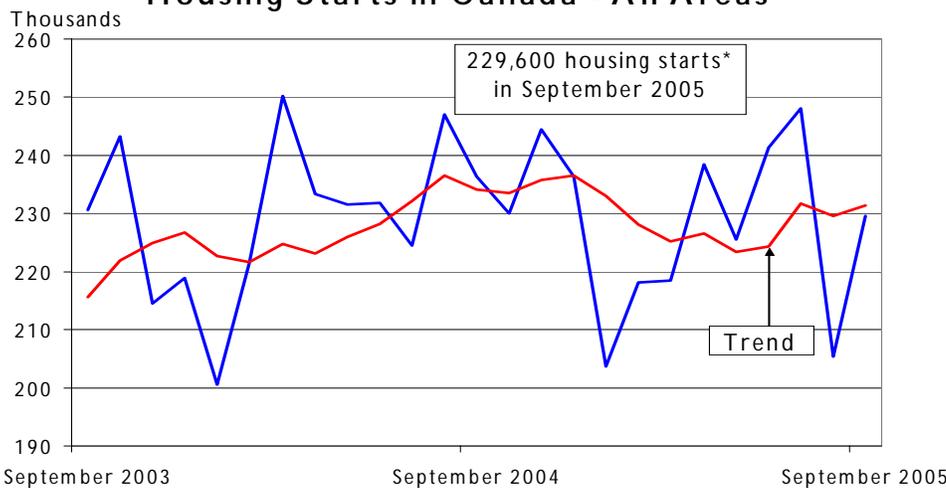
Variable rate mortgages attractive ..... 4

How has the residential real estate market stacked up against the equity market in Canada? ..... 6

#### Tables:

Starts Statistics ..... 8

Housing Starts in Canada - All Areas\*



Source: CMHC

\*Seasonally adjusted at annual rates

Monthly housing starts numbers published in Housing Now Canada are final and may differ from the preliminary numbers in the starts press release

<sup>1</sup> All starts figures, other than actual starts, are seasonally adjusted annual rates (SAAR) that are monthly figures adjusted to remove normal seasonal variation and multiplied by 12 to reflect annual levels.



September compared to August. The stronger performance of multiple starts compared to single starts is the result of rising house prices which can shift demand toward less expensive multi-family homes. Urban multiple starts are poised to outnumber urban single starts in 2005 for the first time since 1993.

***Urban starts increased in the Prairies, Quebec, Ontario, and British Columbia***

Urban housing starts were up across all regions except for the Atlantic in September. Housing starts were up 19.5 per cent to 45,400 units in the Prairies, 17.9 per cent to 45,400 units in Quebec, 12.7 per cent to 65,500 units in Ontario, and 11.4 per cent to 35,100 units in British Columbia. In the Atlantic region, the seasonally adjusted annual rate of urban starts fell 11.6 per cent to 8,400 units.

Rural starts in September were estimated at a seasonally adjusted annual rate of 29,800 units.

***Year-to-date actual urban starts are lower than in the same period last year***

For the first nine months of 2005, actual urban starts were 4.7 per cent lower than in the same period in 2004. Year-to-date single starts decreased 10.1 per cent, while multiple starts increased 1.1 per cent compared to the same period last year.

Across the regions, on a year-to-date basis, actual urban starts were up in the Prairies (7.0 per cent), but were down in Quebec (10.7 per cent), Ontario (7.8 per cent), the Atlantic (4.6 per cent), and British Columbia (2.2 per cent).

***New house prices in August remain strong***

The year-over-year increase in the price of new homes, as measured by the New Housing Price index (NHPI), was 4.6 per cent in August 2005, down from 4.7 per cent in July. Strong demand for housing, higher building material and labour costs, as well as increasing land values, contributed to the increase in house prices.

**Existing Home Market**

***MLS® sales establish new record in August***

Seasonally adjusted MLS® (Multiple Listings Service) sales were up 5.4 per cent to 43,444 units in August, compared to 41,220 units in July. August's result is the strongest level of MLS® sales on record.

Year-to-date MLS® actual sales from January to August 2005, at 342,351 units, were up 3.3 per cent from the same period in 2004.

***MLS® new listings increased in August***

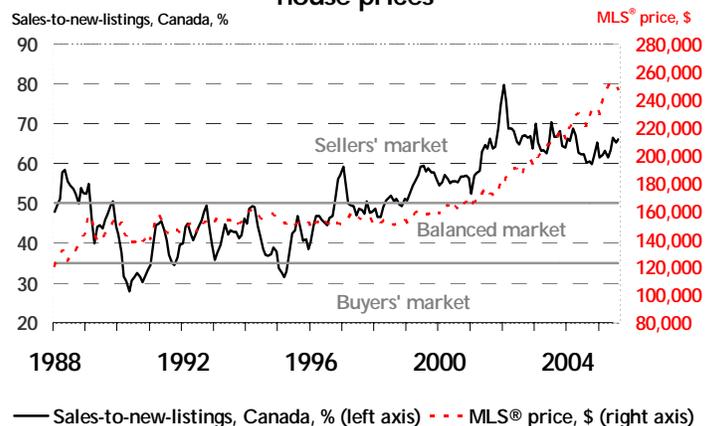
Seasonally adjusted MLS® new listings increased by 4.1 per cent in August to 65,822 units, compared to 63,206 units in the previous month.

Actual new listings for the first eight months of 2005 were up 4.0 per cent over the same period in 2004.

***Sellers' market conditions across Canada continue to support strong growth in house prices***

An indicator of price pressure in the existing home market is the sales-to-new-listings ratio<sup>1</sup>.

**Sellers' market continues to support rising house prices**



Sources: CMHC, Canadian Real Estate Board (CREA), MLS®

**continued on page 3...**

<sup>1</sup> Taking the Canadian market as a whole, a sales-to-new-listings ratio below 35 per cent has historically accompanied prices that are rising at a rate that is less than inflation, a situation known as a *buyers' market*. A sales-to-new-listings ratio above 50 per cent is associated with a *sellers' market*. In a sellers' market, home prices generally rise more rapidly than overall inflation. When the sales-to-new-listings ratio is between these thresholds, the market is said to be *balanced*.

New listings are a gauge of supply of existing homes, while MLS® sales are a proxy for demand.

The sales-to-new-listings ratio for Canada remained in sellers' market territory in August, at about 66 per cent. The Canada-wide average MLS® price increased by 9.7 per cent in the first eight months of 2005 compared to the same period in 2004.

## Economic conditions

In September, employment remained relatively unchanged from August as increases in full-time employment were offset by decreases in part-time employment. Nevertheless, the unemployment rate edged down to 6.7 per cent in September. Total employment for the third quarter of 2005 grew by 31,000 jobs. This was lower than the 79,000 jobs gained in the second quarter of 2005. The sectors that saw substantial growth in September were the information, recreation and culture sector (20,000 jobs) and the educational sector (14,000 jobs). On the other hand, employment in the finance, insurance, real estate and leasing sector (-29,000 jobs) and the business, building and other support services sector (-12,000 jobs) fell in September.

Employment in September 2005 was up 1.2 per cent compared to a year ago.

The seasonally adjusted employment-to-population ratio remains close to historical peak levels. In other words, a near record share of Canadians are employed, which is supporting high levels of consumer confidence and strong demand for housing.

The Bank of Canada raised its target for the overnight lending rate by a quarter of a percentage point to 3.0 per cent on October 18<sup>th</sup> following a similar move on September 7<sup>th</sup>. An economy that is operating close to full capacity and an attempt to keep inflation in line with the target were cited as factors prompting the hike in the rate. Nevertheless, monetary conditions remain stimulative.

In September, the price of goods and services included in the Consumer Price Index (CPI) basket increased 3.4 per cent compared to September 2004. The large increase was mainly due to higher gasoline prices, while men's and women's clothing contributed as well. These increases were restrained by lower prices for computer equipment and supplies. ■

---

---

Contributors: Ali Manouchehri

Ed Heese

Bob Dugan

Julie Taylor

---

---

## Questions:

Julie Taylor at 1-613-748-2239

or [jtaylor@cmhc-schl.gc.ca](mailto:jtaylor@cmhc-schl.gc.ca)

To subscribe: 1-613-748-2006 or

<http://www.cmhc-schl.gc.ca/mktinfo/store>

© Canada Mortgage and Housing Corporation, 2005.

All rights reserved. Canada Mortgage and Housing Corporation hereby grants permission to the subscriber to produce one electronic copy and to print one hard copy for the subscriber's personal use only. No part of this publication may be reproduced, modified, or redistributed in any form or by any means, for any purposes (including but not limited to sales) other than those noted above, without the prior written permission of Canada Mortgage and Housing Corporation.

Product # 63830-2005-10

## Variable rate mortgages attractive

Canadians have many options when it comes to financing their homes, such as whether to go with a fixed or variable rate mortgage. With the posted five-year mortgage rate at 50 year lows, many home buyers may be wondering if now is the time to lock in.

### Mortgage term selection

Choosing the best mortgage term, whether renewing an existing mortgage or getting a mortgage for the first time, has been a riddle for Canadian mortgage borrowers since the widespread introduction of short-term mortgage instruments in the early 1980s. Should they lock into a longer term mortgage or should they go short and roll their mortgage over period after period?

Canadians face a multitude of mortgage terms ranging from variable rate to 25-year closed mortgages. However the five-year closed mortgage term remains the most popular according to the latest Financial Industry Research Monitor Survey<sup>1</sup>.

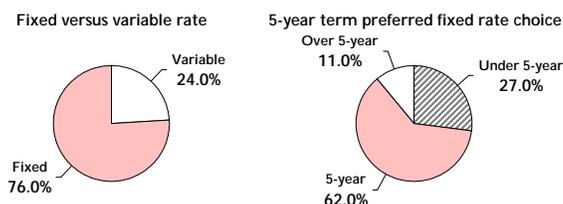
### Optimal mortgage term

The optimal term is defined here as the one which, over the term of the mortgage, results in the lowest mortgage interest cost paid by the borrower.

### Variable rate mortgage: a cost-effective option

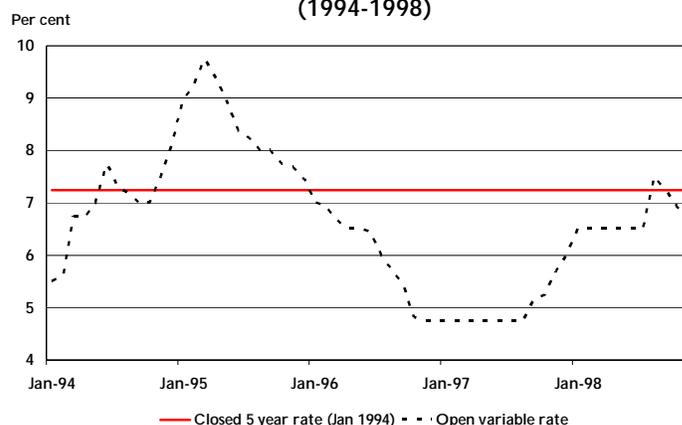
We used monthly variable open and fixed five-year closed mortgage rates to compare interest costs over five year periods for a \$100,000 mortgage. Monthly payments for the variable rate mortgage were kept at the same level as that of a five-year closed mortgage originated at the same time. As a result, the proportion of the monthly payment that is applied against the principal on a variable rate mortgage will vary with fluctuations in interest rates. Between 1993 and 2000, mortgage rates trended down. Therefore over any given 5 year period between 1993 and 2000, variable mortgage rates were on average lower than the fixed rate available at the start of the period. For example, a mortgage with a fixed-rate for a 5-year term beginning in January of 1994, would have a mortgage rate of 7.25 per cent over the entire term (see second graph above).

### 5-year mortgage term most popular



Sources: CMHC, Clayton Research and Ipsos-Reid, The FIRM Residential Mortgage Survey, March 2005

Fixed five-year rate (1994-1998) vs. variable rate (1994-1998)



Source: CMHC, Bank of Canada

However, the variable mortgage rate was below 7.25 per cent for most of the five year period from January 1994 to December 1998. As a result, a larger proportion of the monthly payments would have been applied to the principal for variable rate mortgages. This reflects the fact that variable rates were almost always lower than the fixed five-year rate between 1993 and the present. Because of this interest savings,

continued on page 6....

<sup>1</sup> Financial Industry Research Monitor (FIRM) survey, March and June 2005, ClaytonResearch/Ipsos-NPD

continued: Variable rate mortgages attractive

variable rate mortgages have become increasingly popular. In the first half of 2005, 38 per cent of people obtaining or renewing a mortgage chose a variable rate up from 19 per cent in 2003.

*Discounting makes the five-year term more attractive*

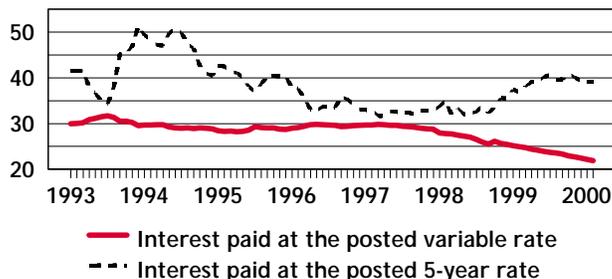
The variable rate mortgage may not always prove to be the least costly if mortgage rates rise substantially over the five year horizon or if the five-year negotiated rate incorporates a large discount from the posted rate.

Mortgage rate discounting was not common prior to the mid-1990s and it is difficult to obtain data on the size of discount. As a proxy for discounts on the five-year mortgage rate, we used the difference between the rate posted by chartered banks and the lowest five-year mortgage rate offered by lenders, as captured in the CANNEX<sup>2</sup> monthly survey. The same approach was used for the variable rate. We estimate that the discount on the five-year mortgage rate has averaged more than one percentage point since 1996, while the estimated discount on variable rate mortgages is smaller at about a quarter of a percentage point. Recalculating interest costs over a five-year period using the estimated discounted rather than the posted mortgage rates narrows the gap in interest costs between the fixed and variable rate mortgages. For the five-year period beginning in 1997 the interest costs for five-year fixed and variable rate mortgages were virtually equal. However, decreases in interest rates have resulted in lower interest costs on variable rate mortgages relative to five-year fixed rate mortgage terms entered into in 1998 to 2000.

*In summary*

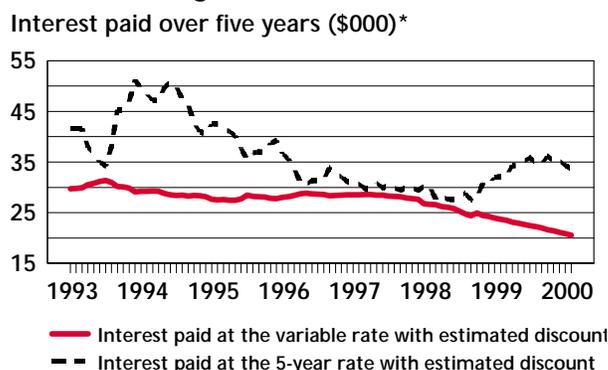
Mortgage rates have trended lower since 1993. In this environment, variable rate open mortgages have generally been cheaper than locking in a medium or long term mortgage. Looking ahead,

**Variable rate mortgages cost less**  
Interest paid over five years (\$000)\*



\* Interest paid over five years for a \$100,000 mortgage amortized over 25 years  
Sources: CMHC, CANNEX

**Discounting lowers cost of fixed rate**



\* Note: Based on \$100,000 mortgage amortized over 25 years  
Sources: CMHC, CANNEX

whether a fixed or variable rate mortgage is most effective depends on how mortgage rates evolve. In a falling interest rate environment like the one witnessed from 2000 to 2002, holders of variable rate mortgages benefit from the decrease, while longer term mortgage holders' rates do not change. This can lead to a cost advantage for variable rate mortgages. However, mortgage rates can also rise and when they do, variable rate mortgage holders are exposed to rising interest costs, while holders of fixed rate mortgages are not. Ultimately the choice between variable and fixed mortgages will depend on each individual's appetite for risk and their financial ability to weather a period of higher mortgage rates. ■

<sup>2</sup> Cannex Financial Exchanges Limited, survey of mortgage lenders last Wednesday of the month, data was available for 1993-2005 period for most frequently posted rates (mode) and for 1996-2005 for the lowest rate posted.

## How has the residential real estate market stacked up against the equity market in Canada?

In contrast to equity markets, residential real estate assets have registered a relatively steady price-earnings multiple<sup>1</sup> over the past 15 years. Growth in the residential real estate market has also outperformed the equity and bond markets in recent years. A combination of a relatively stable price-earnings multiple and high yields has made the Canadian residential real estate increasingly attractive to investors and homebuyers alike.

The price-earnings multiple is used in financial analysis to broadly determine if a stock or an equity index is over/under valued. To evaluate the price-earnings multiple of equities, the TSE300 Index and the associated price-earnings multiples were used as the benchmark here.<sup>2</sup>

To estimate the trend in the price earnings multiple for real estate investment in Canada, we used the average home price and divided it by the income generated from the annual average rent for a three-bedroom unit.

As depicted in the following graph, the trend in residential real estate price-earnings multiple have been far more stable than the equity market multiples for Canada over the past 15

years. With rapidly rising house prices since 2002, the estimated index for the price-earnings multiple for real estate climbed slightly from about 101 to 117. This pales compared to the increase in the price-earnings multiple for equities in the late 1990s that coincided with the high-tech bubble. The relatively stable price-earnings multiple for real estate supports the concept that residential real estate is well priced and provides added evidence that there is no real estate bubble in Canada.

*Residential real estate has offered a very attractive growth rate in recent years*

How has growth in residential real estate compared to alternative investments in recent years? We compare the growth on three investments: bonds, equities, and real estate.

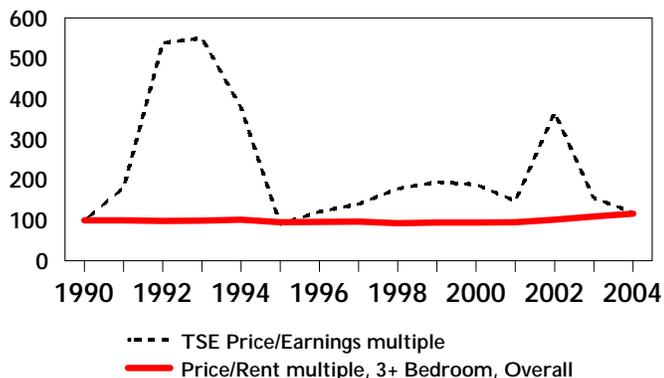
The growth rate for the equity market is measured by annual percentage change of the TSE300 price index. The growth rate for the residential real estate market is approximated by measuring the increase in average home price sold through real estate boards<sup>3</sup>. The growth rate for bonds is the yield on 10-year Government of Canada bonds.

The residential real estate market has outperformed both the equity and bond markets in terms of average growth over the

continued on page 7....

### Residential real estate multiples far more stable

Price-earnings multiples for residential real estate and TSE Index (1990=100)



Sources: CMHC, CREA, Statistics Canada

<sup>1</sup> Price-Earnings multiple is the ratio of market price of a security to its annual earnings. It applies to a single security as well as to a market as a whole.

<sup>2</sup> The price-earnings multiples for TSE were adjusted to exclude the missing data (July 2001-July 2002) caused by negative earnings.

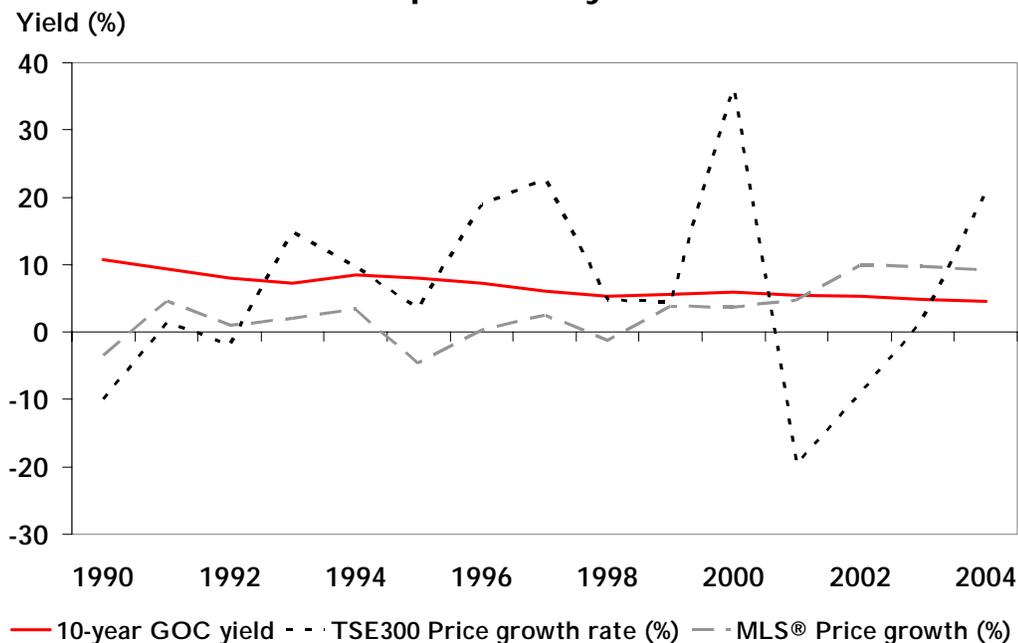
<sup>3</sup> The use of the average house price is based on the fact that it represents a wide array of homes and is a good representative of the underlying housing stock.

## continued: How has the residential real estate market stack up against the equity market in Canada?

past five years, however, the growth in equities started to pull ahead of growth on real estate in 2003. Residential real estate has offered an average annual growth of 6.8 per cent compared to 5.8 per cent for equities and 5.3 per cent for bonds during 1999-2004.

In summary, residential real estate has exhibited a relatively stable price-earnings multiple and an attractive rate of growth in the past five years making it a good investment vehicle. ■

### Residential real estate has done well in the past five years



Sources: CMHC, CREA, Statistics Canada

## This Month's Housing Data (SAAR)

	2004	Q1:05	Q2:05	Q3:05	M7:05	M8:05	M9:05
<b>Housing starts, units, 000s</b>							
<b>Canada. Total. All areas</b>	233.4	213.3	235.4	227.7	248.1	205.4	229.6
Per cent change from previous period	6.9	-10.0	10.4	-3.3	2.8	-17.2	11.8
<b>Canada. Total. Rural areas</b>	29.0	28.7	34.1	29.8	29.8	29.8	29.8
Per cent change from previous period	9.5	-5.6	18.8	-12.6	-12.6	0.0	0.0
<b>Canada. Total. Urban areas</b>	204.4	184.6	201.3	197.9	218.3	175.6	199.8
Per cent change from previous period	6.5	-10.6	9.0	-1.7	5.4	-19.6	13.8
<b>Canada. Single. Urban areas</b>	103.9	93.4	98.6	91.7	91.3	87.7	96.4
Per cent change from previous period	3.6	-8.9	5.6	-7.0	-7.2	-3.9	9.9
<b>Canada. Multiple. Urban areas</b>	100.5	91.2	102.7	106.2	127.0	87.9	103.4
Per cent change from previous period	9.7	-12.3	12.6	3.4	16.7	-30.8	17.6
<b>Newfoundland. Total. All areas</b>	2.9	3.1	2.5	2.7	2.5	2.7	3.1
Per cent change from previous period	6.6	6.9	-19.4	8.0	8.7	8.0	14.8
<b>Prince Edward Island. Total. All areas</b>	0.9	1.5	1.0	0.8	0.7	1.0	0.9
Per cent change from previous period	12.9	114.3	-33.3	-20.0	-30.0	42.9	-10.0
<b>Nova Scotia. Total. All areas</b>	4.7	4.0	5.4	4.7	4.6	5.4	3.9
Per cent change from previous period	-7.4	-14.9	35.0	-13.0	15.0	17.4	-27.8
<b>New Brunswick. Total. All areas</b>	3.9	3.2	4.3	4.0	3.8	4.0	4.1
Per cent change from previous period	-12.1	-20.0	34.4	-7.0	-11.6	5.3	2.5
<b>Quebec. Total. All areas</b>	58.4	55.1	52.6	50.3	52.8	45.7	52.6
Per cent change from previous period	16.2	-9.1	-4.5	-4.4	1.7	-13.4	15.1
<b>Ontario. Total. All areas</b>	85.1	71.3	88.2	78.2	100.2	63.5	70.9
Per cent change from previous period	-0.1	-15.5	23.7	-11.3	-3.3	-36.6	11.7
<b>Manitoba. Total. All areas</b>	4.4	4.3	4.4	5.5	6.2	5.9	4.5
Per cent change from previous period	5.6	7.5	2.3	25.0	21.6	-4.8	-23.7
<b>Saskatchewan. Total. All areas</b>	3.8	2.5	3.3	3.8	3.7	4.0	3.7
Per cent change from previous period	14.1	-40.5	32.0	15.2	-14.0	8.1	-7.5
<b>Alberta. Total. All areas</b>	36.3	36.7	41.6	40.4	36.9	37.5	46.6
Per cent change from previous period	0.3	-7.3	13.4	-2.9	7.6	1.6	24.3
<b>British Columbia. Total. All areas</b>	32.9	31.6	32.1	37.3	36.7	35.7	39.3
Per cent change from previous period	25.8	-0.6	1.6	16.2	20.3	-2.7	10.1

SOURCE: CMHC, Starts and Completions Survey. All data are seasonally adjusted and annualized. This seasonally adjusted data goes through stages of revision at different times through the yearly cycle resulting in finalization of preliminary data. These revisions take place at the end of each month, quarter and year.

## Annual rate of housing starts, urban areas\*

	2004	Q1:05	Q2:05	Q3:05	M7:05	M8:05	M9:05
Canada	204.4	184.6	201.3	197.9	218.3	175.6	199.8
Newfoundland	2.1	2.5	1.7	1.9	1.7	1.9	2.3
Prince Edward Island	0.6	1.1	0.5	0.5	0.4	0.7	0.6
Nova Scotia	3.3	2.5	3.9	3.4	3.3	4.1	2.6
New Brunswick	2.6	1.8	3.0	2.8	2.6	2.8	2.9
Québec	46.7	41.6	40.0	43.1	45.6	38.5	45.4
Ontario	79.9	69.4	81.3	72.8	94.8	58.1	65.5
Manitoba	2.9	2.7	2.7	3.4	4.1	3.8	2.4
Saskatchewan	3.1	2.0	2.8	2.6	2.5	2.8	2.5
Alberta	32.2	32.0	35.8	34.3	30.8	31.4	40.5
British Columbia	30.9	29.0	29.6	33.1	32.5	31.5	35.1

\* Thousands of units, seasonally adjusted and annualized.

## This Month's Major Housing Indicators

	2004	Q1:05	Q2:05	Q3:05	M7:05	M8:05	M9:05
<b>New Housing</b>							
New & unoccupied singles & semis, units 000s	5.2	5.7	5.5	5.0	5.1	4.9	4.9
Per cent change from same period previous year	9.3	12.5	4.1	-0.7	3.0	-2.0	-3.0
New & unoccupied row & apartments, units 000s	6.7	8.8	9.3	9.3	9.5	9.5	8.9
Per cent change from same period previous year	18.9	49.6	54.0	38.4	44.6	43.5	27.7
New House Price Index, 1997=100	123.2	126.5	128.4	n.a.	129.5	130.0	n.a.
Per cent change from same period previous year	5.5	5.1	4.7	n.a.	4.7	4.6	n.a.
<b>Existing Housing</b>							
MLS <sup>®</sup> resales*, units 000s	461.1	454.3	491.6	n.a.	494.6	521.3	n.a.
Per cent change from same period previous year	6.0	-0.1	2.9	n.a.	6.5	13.7	n.a.
MLS <sup>®</sup> average resale price*, \$C 000s	226.2	239.2	246.5	n.a.	250.1	251.2	n.a.
Per cent change from same period previous year	9.2	8.8	8.9	n.a.	12.7	10.0	n.a.
<b>Mortgage Market</b>							
1-Year Mortgage Rate, % (period average)	4.59	4.88	4.83	4.97	4.90	5.00	5.00
5-Year Mortgage Rate, % (period average)	6.23	6.12	5.90	5.80	5.80	5.80	5.80

SOURCES: CMHC, Statistics Canada, Bank of Canada, The Canadian Real Estate Association.

n.a. Figures not available

\* Seasonally adjusted and annualized (SAAR).

\*\* Annual and quarterly data is actual. Monthly data is seasonally adjusted.