



Spotlight **Canada** **Residential Market**

Spring 2014



Notes about the publication

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Spotlight Canada Residential Market



Canada's housing market remained resilient during the global downturn with steady growth recorded

Canada's economic prosperity since 2008 sets it apart from most other North Atlantic economies. Canada's avoidance of the financial crisis that beset its neighbours so severely, both to the south and across the Atlantic, has meant its real estate markets have taken a very different path to those of the USA and Europe.

Apart from a brief hiatus in 2008, Canada's housing markets are almost unique among industrialised countries in having grown at a similar rate as their pre-crisis trajectory. This means that the Canadian residential market stands in deep contrast to that of the USA. Capital values are at an historical high and yields are relatively suppressed in cities where demand has been high from overseas investors.

This leaves few buying opportunities for those seeking distressed sales and high future price growth in urban properties. Having said

this, economic growth has fuelled rental growth too, so there are still some cities where high yields look compelling to overseas buyers.

Outside of the major conurbations, there are still some opportunities for bargain-hunting and capital growth. Leisure resorts in Canada are still relatively low priced and potentially high-yielding. As American and European economies recover, the potential for renewed second home purchasing will increase and a scarcity of supply should lead to price growth.

We expect the first wave of overseas investment to be in established resorts like Whistler but anticipate that there is also scope for further leisure-market development in places like Nova Scotia. Here both coastal and inland recreation is poised to capture a prosperous domestic second home market and to attract new, US holiday makers and buyers. The prospects for both income returns and growth have the potential to attract an even wider-spread of buyers from Europe, Asia and beyond. ■

SUMMARY

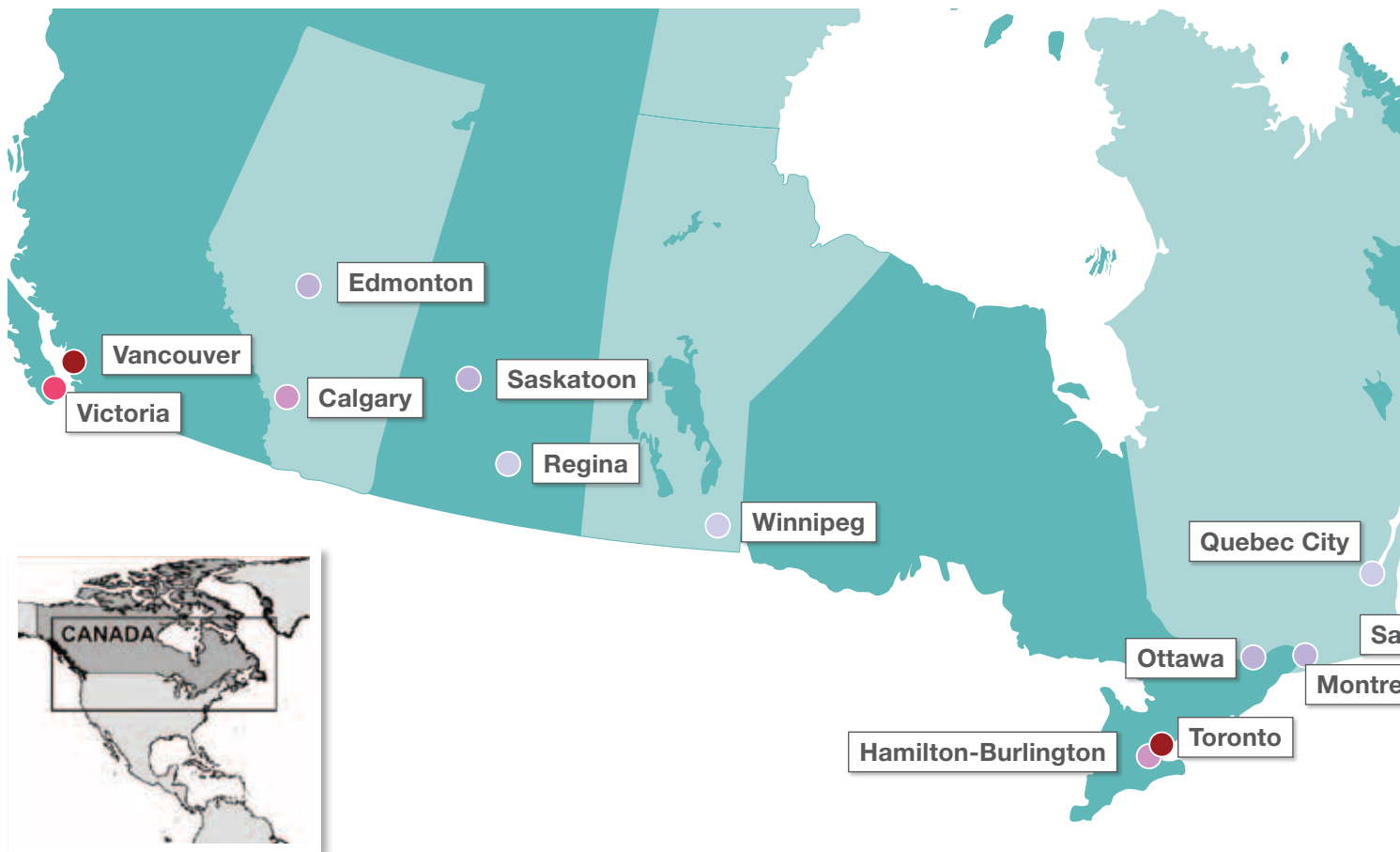
An overview of the market

- Canada weathered the global financial crisis better than many other industrialised countries, supported by a well regulated financial services sector and global demand for its natural resources.
- Canada's biggest cities have been recipients of new Asian wealth flowing into global urban enclaves. This, together with a resilient domestic housing market pushed up prices by 19% in Montreal, 16% in Vancouver, and 30% in Toronto between 2009 and 2013.
- Leisure enclaves, particularly ski resorts, suffered as demand for second homes waned due to domestic, US and European buyers withdrawing from the market. Prices bottomed out in 2012 and there are now buyer opportunities.
- Economic recovery in the US and Europe is expected to bring new overseas buyers to Canada's leisure hotspots. This should lead to price rises.
- Canada's economy is rebalancing from domestic, consumption-driven growth toward export-led growth as the world economy recovers.



MAP 1

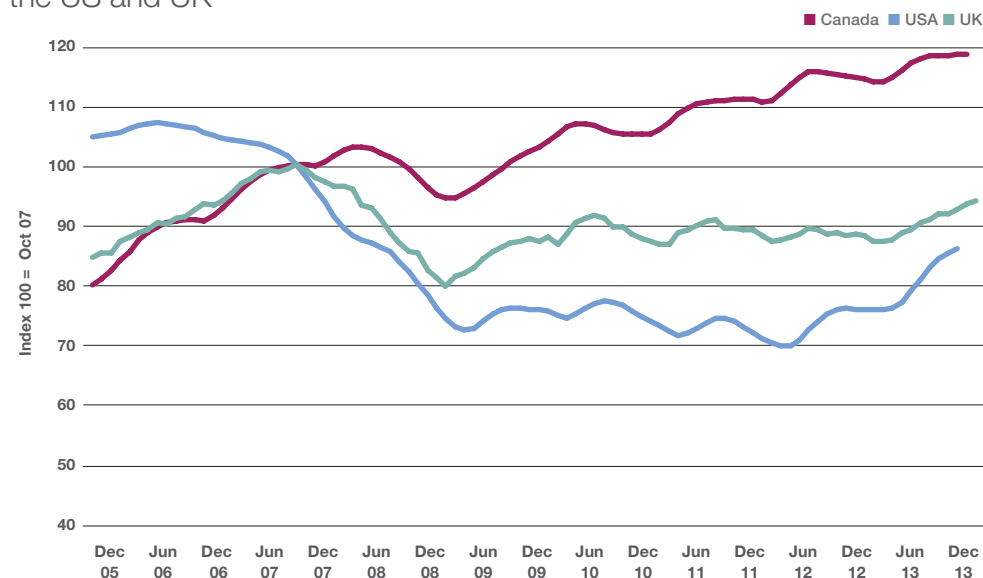
Average house prices in Canada's major cities



Source: Savills World Research / Canadian Real Estate Association

GRAPH 1

Canadian house price performance Benchmarked against the US and UK



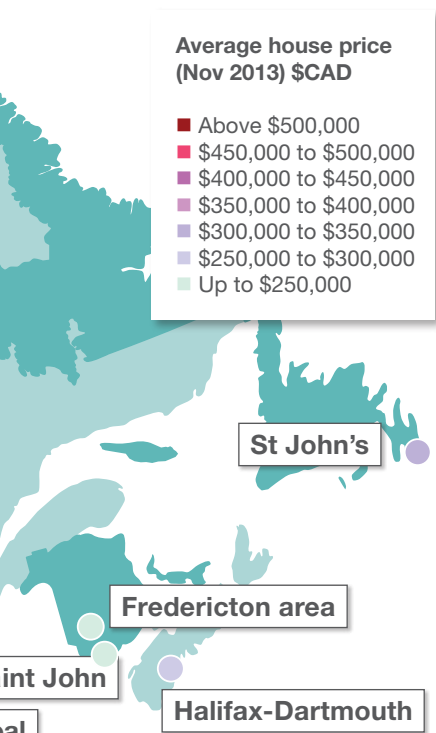
Source: Savills World Research / MLS Home Price Index / Case Shiller / Nationwide

Canadian economy & residential market

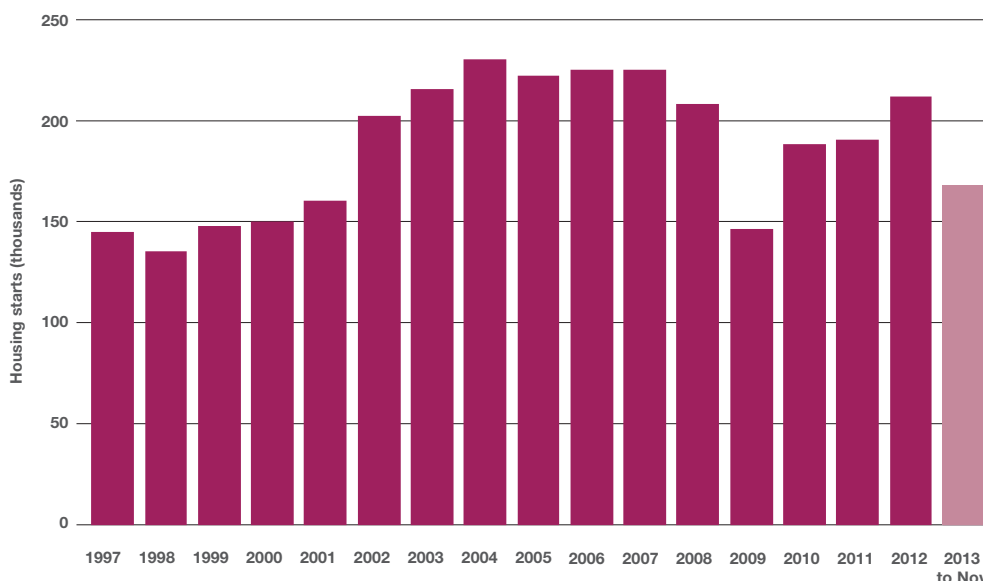
Canada is the world's second largest country by area and is rich in natural resources. It is a net exporter of energy and is home to the world's third largest oil reserves.

Large primary industries are complemented by a highly developed service, manufacturing and retail sectors. Canada is considered a wealthy, stable and safe country. It ranks high in international measures of education, government transparency, civil liberties, quality of life, and economic freedom.

Canada weathered the global financial crisis better than many of its industrialised peers. The country's strong and well regulated banking industry limited exposure to bad debt, while its natural resources and energy sectors benefited from surging



GRAPH 2
Canadian housing starts



Source: Savills World Research / Canadian Mortgage and Housing Association

for their wealth at a time of global economic turmoil. They have been pouring money into Canada's major cities. Pre-sales to international buyers have helped to forward-fund new schemes. Housing starts recovered quickly to pre-crunch levels after a brief slow down in 2009 (Graph 2). Migration and population growth has created demand and prevented oversupply.

A side effect of Canada's buoyant residential market has been the accumulation of record-high household debt. Total credit market debt (including mortgages) stood at a record 163.7% of all disposable income in Q3 2013.

Despite this high level of personal indebtedness, levels of equity employed in home ownership is high; 41% of homeowners have no mortgage.

Canada has stringent rules on mortgage lending. Mortgages with deposits of less than 20% are required by law to be insured. The mortgage market remains healthy and defaults are low; just 0.3% of mortgages in 2013 – their lowest level since 2008.

As the Canadian economy rebalances from domestic, consumption-driven growth toward export-led growth following US and global economic recovery, the size of household debt is expected to reduce in relation to disposable income. ■

demand in rapidly growing Asian economies. GDP dipped by just 2.8% in 2009, compared to falls of 3.1% in the US and 4.4% in the Euro area.

Canada's residential markets proved resilient during the global economic downturn. House prices fell by just 9% between May 2008 and March 2009, in contrast to the US and UK, for example, which saw falls of 54% and 26% from peak to trough, respectively. Since 2009, Canada's residential markets have recorded price growth of 26%, with values now 15% above their 2008 high, according to the MLS home price index. The market has remained fluid, with annual transaction levels relatively stable (see Graph 1).

Low interest rates and a resilient economy have supported the domestic market for housing. Meanwhile, international investors have sought out Canadian real estate as a 'safe haven'

TABLE 1
Prime prices compared
Price comparison between selected cities

City	Average prime value psqft (\$USD)
Hong Kong	\$3,900
London	\$1,900
Paris	\$1,600
Moscow	\$1,400
Tokyo	\$1,400
Singapore	\$1,400
New York	\$1,200
Shanghai	\$1,100
San Francisco	\$790
Los Angeles	\$760
Miami	\$700
Vancouver	\$660
Mumbai	\$620
Toronto	\$590
Sydney	\$550
Chicago	\$550
Montreal	\$480

Source: Savills World Research

CANADIAN CITIES

Canada's biggest cities are renowned for the quality of life they offer residents. The Economist Intelligence Unit ranks Vancouver and Toronto as the world's third and fourth most liveable cities, citing availability of goods and services, low personal risk, and effective infrastructure as key attributes.

The quality of life available and the transparent and open business environment of an English speaking country has put Canadian cities high on the shopping list for many international investors.

Strong rental markets with vacancy rates of just 3% have been offset by rapidly appreciating capital values, and softening yields. For many investors capital gains have been spectacular. Prices in Toronto appreciated by 45% between June 2006 and November 2013, at a time when those in North American cities south of the border were falling.

Prices in New York, for example, fell by 20% over the same period. In spite of Canadian price growth, absolute prime price levels are still lower than those in many major US centres (though notably, the more international markets of Vancouver and Toronto are higher priced than Chicago). Most notably, Canadian city values are, substantially below those of the top tier of world cities (see table 1, page 5).

Toronto

■ **Population (metro):** 5.1 million

■ **Average price Nov 2013:** \$485,328

■ **Capital value growth, year to Nov 13:** 3.3%

Located on the north-western shore of Lake Ontario, Toronto is Canada's most populous city. It is a financial capital, international centre of business and the most multicultural city in Canada. Some 48% of its residents are foreign born.

Toronto's residential market has been characterised by a shortage of inventory among single family homes in the last year. This has put upward pressure on prices across the whole market.

Prices rose by 6.1% in the year to

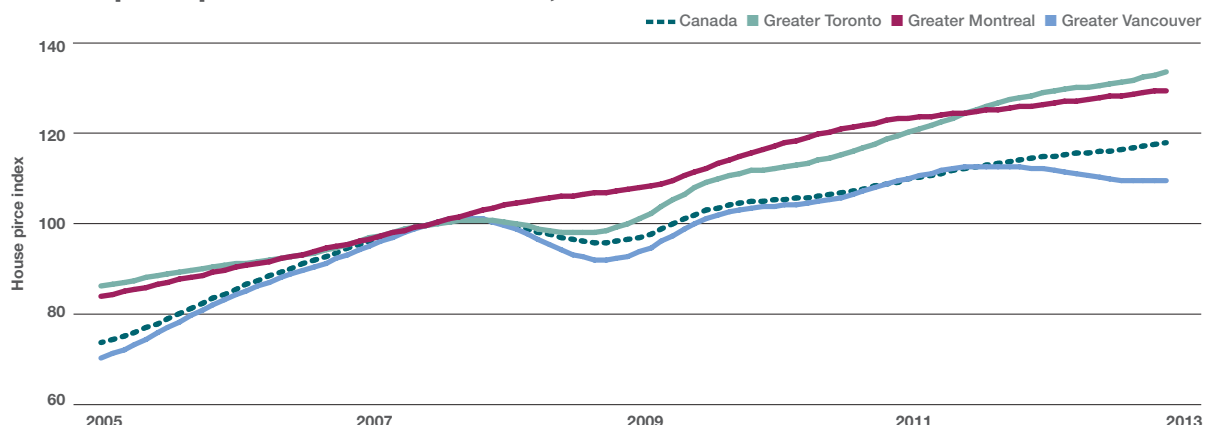
November 2012 although the rate of growth slowed somewhat in 2013 – to 3.3%, according to the MLS index. The city's rental market remains buoyant, underpinned by young professional migrants and corporate tenants. Yields are above 5%, and can exceed 6% on condominiums.

Toronto has two distinct prime residential markets. Toronto North is suburban and attracts families, while urban Toronto offers downtown living for professionals – singles and couples – with easy access to entertainment and employment.

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 "Toronto is
 Canada's most
 populous city"



GRAPH 3 **House price performance in Toronto, Montreal and Vancouver**



Source: MLS

Montreal

- **Population (metro):** 3.6 million
- **Average price Nov 2013:** \$326,850
- **Capital value growth, year to Nov 13:** 2.3%

Montreal is located north-east of Toronto on the St Lawrence River, and is the second largest city in Canada. With a population of 1.9 million, it is one of the largest French speaking cities in the world. It is a centre of culture, arts, aerospace, technology and the media.

In Quebec society long term renting is a cultural norm, so there is a lower propensity for home ownership than in Anglophone parts of the country. The city enjoys rental vacancy rates of just 2.8%,

and yields in excess of 7%. Capital values are among the lowest in urban Canada.

Housing starts fell by 27% in the 11 months to November 2013, although prices still grew by 2.3%

over the same period, and are forecast to continue to see modest appreciation in 2014. The city's residential market is currently a buyer's one, the result of high supply in preceding years.



Vancouver

- **Population (metro):** 2.1 million
- **Average price Nov 2013:** \$682,215
- **Capital value growth, year to Nov 13:** -2.1%

Vancouver is situated on the west coast and is the most densely populated city in Canada. Surrounded by water on three sides, Vancouver enjoys a spectacular waterfront setting. Offering easy access to the neighbouring mountains and ski resorts, residents enjoy a range of leisure pursuits on their doorstep.

Growth, restricted by the city's position between the Strait of Georgia to the west and mountains to the north and east, has pushed new development – and prices – skywards.

Capital values in the Vancouver housing market increased by 20% between September 2009 and July 2012, as investment poured into the city's residential real estate. It is Canada's most expensive real estate market. Yields are low at just over 4%.

Pacific-facing Vancouver has a long history of Asian immigration, with



large Chinese diaspora. Chinese buyers have been behind much of the new investment in the city in recent years.

These buyers favour the city's modern, high-rise condominium product, as well as single family homes, with the West Side the most desired area and commanding the highest prices.

The city has seen high supply in recent years (19,027 starts in 2012,

10% above the 10 year average), and reliance on investor markets has left it exposed to shifts in sentiment. Prices slipped by 2.1% in the year to November 2013, while housing starts fell by 5% over the same period. ■

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 "Capital values in Vancouver increased by 20% between September 2009 and July 2012"

LEISURE ENCLAVES

Canada welcomes 16 million tourists a year, attracted by its beautiful natural environment, ski resorts, coasts, lakes and associated outdoor activities. Some of these visitors decide to make Canada a more permanent base, purchasing a second home in one of the country's many leisure enclaves. Buyers from the US, Europe and Asia complement those Canadians who already own second homes in the country.

Case study: Nova Scotia

Nova Scotia is dubbed 'Canada's ocean playground'. Its climate is moderated by the Atlantic Ocean that surrounds it, and is known for its culture, scenery and coastline. Of the 184 golf courses in the Atlantic provinces in Canada, 40% are in

Nova Scotia. In 2012 Nova Scotia was visited by 484,300 international tourists up by 7.9% on the year before, the largest increase of any Canadian province.

Nova Scotia's residential market has seen much more stable prices than many of the country's biggest cities. According to the Teranet / National Bank of Canada house price index, the average annual growth rate in Halifax over the last four years has been 3.2%, compared to 6.5% in Toronto, for example. This reflects an, as yet, more domestic and stable local market for housing, in contrast to the more well-known leisure resorts of major cities. Nova Scotia has the potential to become a major bolt-hole to the large east coast cities – of both the US and Canada – in the way that Whistler is to Vancouver on the west coast.

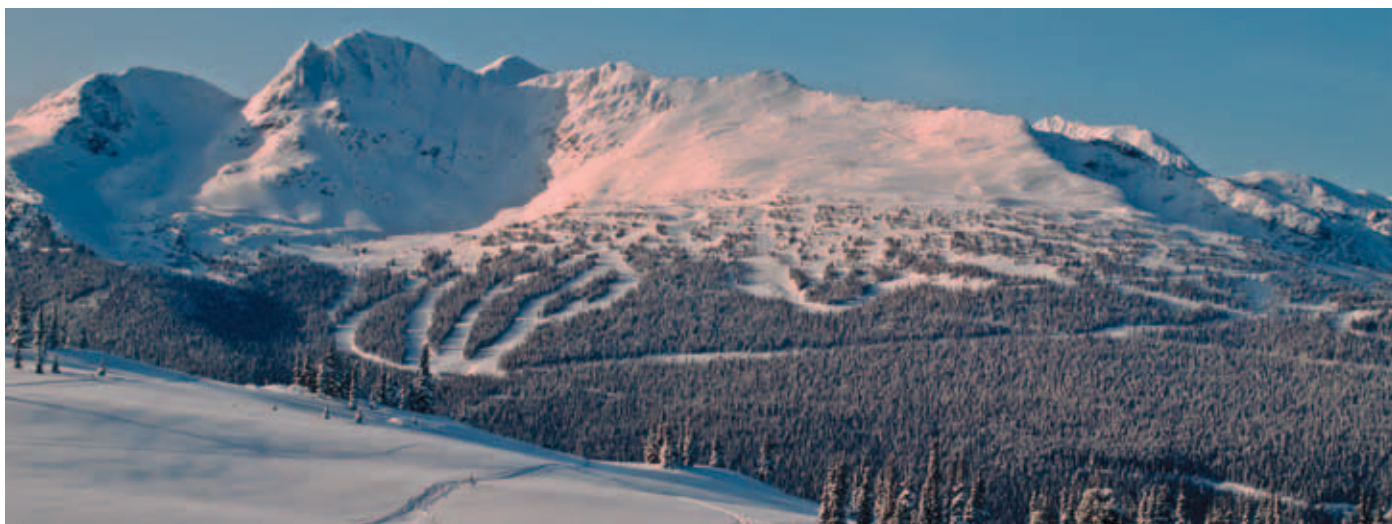
In the coming years a buoyant Nova Scotian economy will fuel wealth

generation and new domestic second home buyers. Job creation will be boosted by a \$25 billion government shipbuilding contract recently awarded to Halifax.

International buyers are also present. Americans are returning to the market as the US economy recovers, while Brits have remained a constant presence. Flight time from Halifax to London is less than six hours, making Nova Scotia one of the most accessible North American destinations for Europeans.

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"Nova Scotia has the potential to become a major bolt-hole to the large east coast cities"
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Case study: Whistler

Just 125 kilometres from Vancouver, Whistler played host to the 2010 Winter Olympics and is one of the world's most exclusive ski resorts. It attracts tourists and second home purchasers from around the world. Annual snowfall of 11.9 metres ensures a long and reliable ski season and Whistler is widely recognised as one of the best ski resorts globally.

With a permanent population of just under 10,000 residents, Whistler has a large second home market. As with other discretionary purchases, Whistler's residential market suffered during the global economic downturn. US buyers, historically a

key purchaser group were put off by a strong Canadian dollar.

Highway improvements for the Winter Olympics made the resort more accessible from Vancouver. In turn, shorter stays became viable, and second homes less necessary.

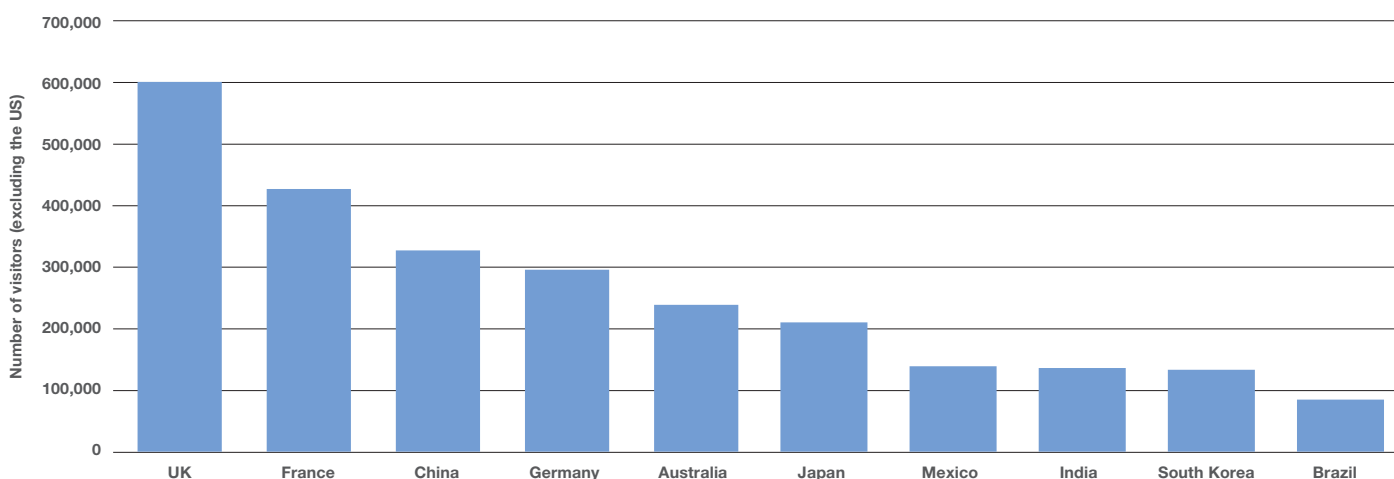
In contrast to nearby Vancouver, prices in Whistler last peaked in 2008, falling by around 25% to a

low in 2012. Values have begun to appreciate in the last year as Whistler positions itself as a year-round destination, and savvy buyers snap up the best product at discounted prices.

The majority of home buyers in Whistler are Canadian, many hailing from neighbouring Vancouver. At the very top tiers of the market, buyers from the US, Europe, Asia and Russia are also present. ■

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 "Values have begun to appreciate in the last year as Whistler positions itself as a year round destination"

GRAPH 4 Major international visitor groups to Canada, excluding the United States, Jan-Nov 2013



Source: Canadian Tourism Commission



OUTLOOK

The future of the market

- Canada's residential market has been supported by low interest rates, a strong domestic economy and a steady flow of international buyers into its major cities.
- As in many locations, asset price growth is expected to ameliorate in the wake of future interest rate increases. A key indicator of an overheated market in these circumstances are low rental yields. With income returns over 5%, we do not see that most Canadian markets will be vulnerable to price falls.
- While some of Canada's major cities may now look more fully valued on this yield basis, the country's leisure enclaves, with lower capital values appear increasingly attractive investment propositions. There are deals to be done in those locations where prices have now bottomed out.
- Canada has seen plenty of overseas buyers since 2008, but these have hailed mainly from Asia, favouring urban, rather than resort, locations.
- A resurgence in the second home market is anticipated as broader economic recovery in the US and Europe brings new overseas buyers to Canada's leisure hotspots.

Savills team

World Research



Yolande Barnes
World Research
+44 (0) 20 7409 8899
ybarnes@savills.com



Paul Tostevin
World Research
+44 (0) 20 7016 3883
ptostevin@savills.com



Lucy Greenwood
World Research
+44 (0) 20 7016 3882
lgreenwood@savills.com



Joanna Leverett
Residential International
+44 (0) 20 7409 8899
jleverett@savills.com

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33 Margaret Street
London W1G 0JD
+44 (0) 20 7499 8644

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