

Soft landing seen for Canada's housing market

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The real estate market appears poised for a soft landing rather than a crash, in a cooling trend the Bank of Canada says is both “expected and welcome.”

Sheryl Kennedy, the central bank's deputy governor, said Canada's financial prudence has helped it sidestep the sharp home price declines being experienced in countries including the U.S., Britain and Spain.

“The Canadian housing market does not appear to be characterized by excess supply at this time,” she said in the text of a speech delivered yesterday in Banff, Alta. “The proportion of unoccupied, newly built dwellings in most cities remains below historical averages, suggesting that a major widespread reversal in house prices is unlikely in the near term.”

In the past decade, prices of existing homes in Canada have risen by about 55 per cent, while new-home prices have risen by about 27 per cent. As one of the country's largest housing booms loses steam, most economists are forecasting a small increase in prices this year that will keep pace with the central bank's 2-per-cent target for inflation.

It's a much different story in the U.S. market, where home prices dropped by 14.1 per cent year over year in the first quarter of 2008, according Standard & Poor's/Case Shiller national home price index.

That record price decline occurred at a pace five times faster than that of the last U.S. housing recession, according to the index's quarterly report, released last month.

Much of Canada's housing boom was the result of supply catching up with pent-up demand that followed the downturn of the late 1980s and early 1990s, according to Ms. Kennedy.

Canada's conservative mortgage culture has helped protect it from the excesses seen during the U.S. boom, which had a much larger amount of subprime mortgages, she added.

As the housing market cools, the Bank of Canada can worry less about the sector as a driver of inflation, said Michael Gregory, senior economist at BMO Nesbitt Burns Inc.

“This speech would have been a lot different if we still had double-digit price gains on new and existing homes,” he said in an interview.

The central bank now has a more pressing concern on its hands in soaring commodity prices, he said. In the real estate market, the issue has shifted to how much cooling prices could put a damper on consumer confidence, he added.

Despite her fairly positive outlook, Ms. Kennedy cautioned that Canada can't afford to become complacent about the real estate market, noting it took a decade for prices and sales to rebound after the bust of the late 1980s.

To that end, the central bank is keeping an eye on "challenges," including ensuring that mortgage innovations, including 40-year amortization products and "near-prime" mortgages, don't detract from prudent lending practices.

Ms. Kennedy's comments suggest the "the jury is still out" at the Bank of Canada regarding the value of these innovations compared with their potential risks, Mr. Gregory said.