Canadian Real Estate Is Getting Irrational

Description

According to *The Globe and Mail*, “The proportion of million-dollar detached homes in Vancouver jumped from just 11 per cent a decade ago to more than 90 per cent last year.” Most of the homes priced under $1 million were on busy streets or tiny lots, or had been torn down. Across the board, the statistics are staggering. This year the Greater Vancouver Area saw the average home price increase by 25%, with a median selling price of $1,098,599.

Many experts are now calling the extreme surge in prices “irrational.”

This year, Royal LePage expects Vancouver prices to rise another 27% along with a 15% rise in the Toronto market. “I believe it is the highest value put forward by a serious forecasting agency since the turn of the century,” said Royal LePage’s CEO.

Contagion risks are growing

“Alongside skyrocketing prices of single-family homes, we have seen an uptick in the rate of price appreciation for condominiums over 1,000 square feet, when compared to smaller units in this market,” Royal LePage’s CEO commented. “This may indicate that families being priced out of the single-family detached home market in Vancouver are looking upwards to condominiums.”

According to a new analysis from the Broadbent Institute in Ottawa, the average Canadian home now costs more than 400 weeks’ worth of earnings. That’s up from 200 weeks of labour time in 1970 and 300 weeks in 1990.

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The Economist recently reported that Canada’s housing prices are 35% overvalued when compared to Canadian incomes. A potential real estate plunge–an event that is increasingly becoming an inevitability–could stretch Canadian citizens past their breaking points.

A new survey by **Bank of Montreal** (TSX:BMO)(NYSE:BMO) found that almost a quarter of Canada’s citizens are still living paycheque to paycheque. Roughly 25% of respondents said they had hardly anything set aside, and more than half reported having less than $10,000 in emergency funds.

According to research from **Genworth MI Canada Inc.** (TSX:MIC), many buyers are borrowing money from their family and friends to buy homes. The typical first-time buyer in Genworth's research paid about $293,000 for a first property. Almost a third of them got money from close acquaintances to help afford their down payments.

"Current and recent buyers need to devote many more weeks of labour time to the financing of their home than their predecessors," says Marc Lavoie, a policy fellow at the Broadbent Institute. "No wonder so many young prospective buyers, especially those in major cities, feel that owning a residential unit is more like a long-distance dream."

If the real estate market even hiccups, it could have a domino effect fairly quickly given that homeowners are already stretched. Judging by what happened in the U.S., market downside of 50% or more is not out of the question.

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