



Bank of Canada to Homebuyers: Don't Buy Right Now!

Description

Last Tuesday, November 23, Deputy Governor of the Bank of Canada Paul Beaudry warned homebuyers that certain regions of Canada could experience a market correction in the near future.

Notwithstanding that warning, homebuyers still seem undeterred in their quest for a house. In fact, in a recent RE/MAX report, nearly half of Canadians surveyed view real estate as one of the best investment options over the next year, with RE/MAX Canada itself expecting average real estate prices to inflate another 9.2% in 2022.

With Beaudry's warning firm in mind, as well as the ongoing flood of homebuyers in the market, let's take at the primary reason why the Bank of Canada is suggesting now is not the best time to buy a home.

Homebuyers' expectations are extrapolative

Recall that "extrapolative expectations" is an economic phrase that refers to our habit of determining the future value of an asset based on the recent past. For instance, if a stock's value rises over three consecutive weeks, with little or no dips, investors might expect the stock to continue rising on the fourth week. In this way, investors assume an upward trend will continue, even though they have no fundamental basis for this belief.

In Beaudry's view, homebuyers' expectations are extrapolative in the sense that they expect the last two years of price hikes to continue into 2022. As Beaudry points out, this leads to the "fear of missing out." Homebuyers believe home prices will keep going up forever. If they don't buy now, so the logic goes, homebuyers will miss out on a "deal."

But little evidence substantiates this claim, aside from the heavy demand we're feeling *today*. In fact, Fitch and Moody, two of the three big credit agencies, have labelled Canada's hottest markets, particularly those in Toronto, Vancouver, Hamilton, and Ontario, as overvalued. In other words, the physical structure isn't worth the price you pay. That begs the question — just how much more overvalued can we get?

And then there are the expected mortgage rate hikes. The Bank of Canada has warned us numerous times that this will happen sometime in 2022. Will demand be red hot when mortgages are more expensive? Will the higher cost of lending coupled with the overinflated cost of a home cause a correction? Beaudry seems to think so.

Should you buy a home in 2022?

I'd say examine your motives first. If you're buying a house now because you don't want to miss out on a "deal," you might want to reconsider. You're assuming prices will continue to rise, even though prices literally *can't* keep going up. At a certain point, demand will cool, and the price you agree to pay on your house will start to seem absurd.

However, if you're absolutely certain you need to buy a home now (or, like, yesterday), don't get me wrong — you might need to buy a house, high prices or not. Mortgage rates will most likely go up in 2022, meaning you have a small window of time to lock into a historically low mortgage rate. Otherwise, it might be wiser to wait until 2022 to see how the real estate market fares under new mortgage rates.

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