

Special Report

Economics and Strategy



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FINANCIAL MARKETS

How brain gain sustains the Canadian housing market

Matthieu Arseneau

How brain gain sustains the Canadian housing market

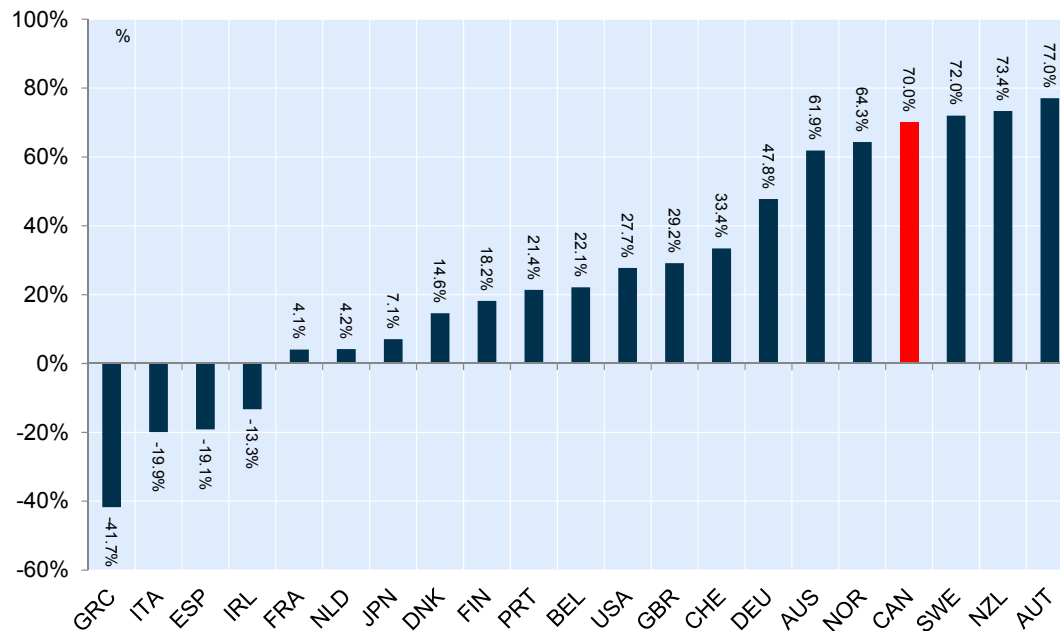
By Matthieu Arseneau

Since the Great Recession of 2008–09, many observers have been looking askance the Canadian housing market, their skepticism heightened by the role of the U.S. housing market in triggering that recession and its disastrous consequences.

It is true that the path of Canadian home prices in the current cycle has been such as to raise questions. Their rise from 2008 to 2018 was among the steepest in the OECD countries.

Canada: The rise in home prices raises questions

Cumulative rise in home prices from 2008 to 2018 (Selected countries)



NBF Economics and Strategy (data via OECD)

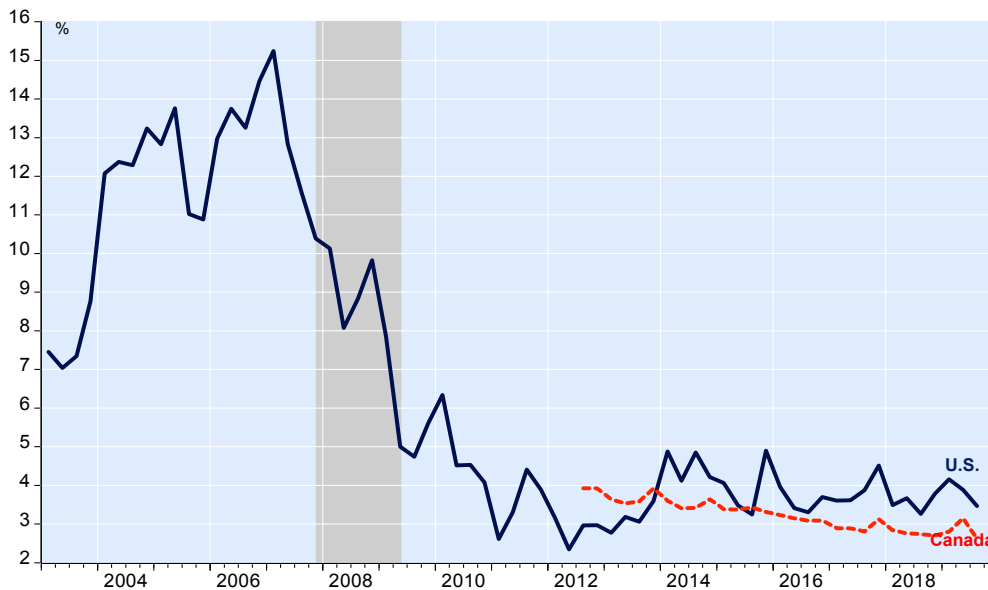
In contrast to the U.S. housing boom, which was stimulated by a relaxation of mortgage lending standards, the Canadian boom has taken place despite a tightening of regulatory conditions. Among government measures introduced since 2008:

- maximum amortization period reduced in stages from 40 to 25 years for insured mortgages;
- minimum down payment raised for insured mortgages;
- borrowers must now qualify for rates higher than those contracted (commonly referred to as B-20 stress testing).

Moreover, Canadian financial institutions have shown caution in recent years in the proportion of new mortgages granted to borrowers with low credit ratings, a proportion that in Canada has been stable at only a quarter of the U.S. average during the high-flying years of 2004 to 2007 (chart).

Canada: Lending standards not a source of concern

Share of mortgages originations with low credit scores (Score < 620)

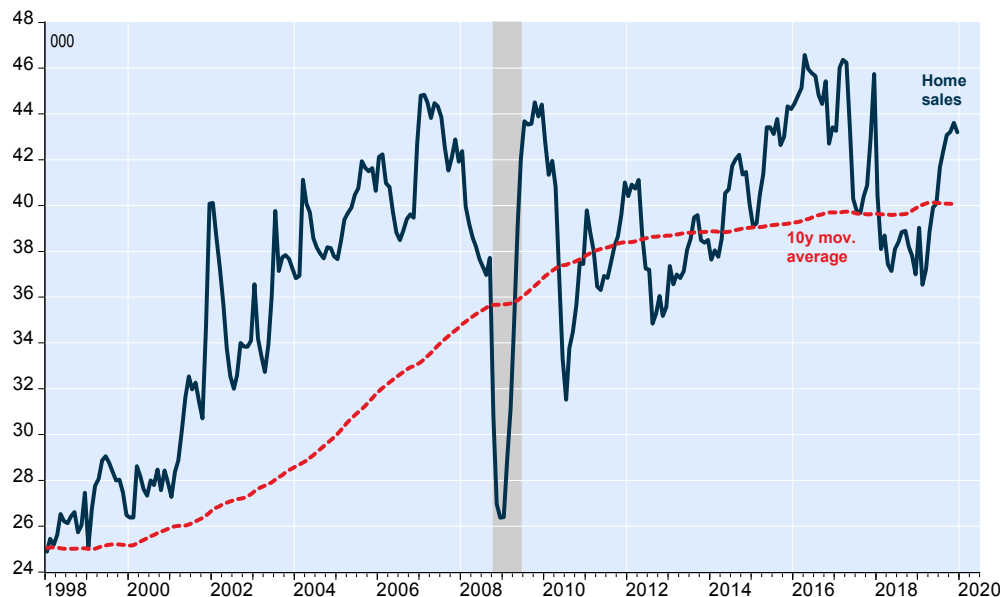


NBF Economics and Strategy (data via Equifax and Federal Reserve of New York)

In 2018 the Canadian housing market slowed markedly on the introduction of stress tests and the tax on purchases by foreigners in Ontario. Some observers began to fear political decision-makers had gone too far in their restrictive measures. Some saw these measures, in conjunction with rising interest rates, as putting an end to the vigour of the Canadian housing market. But in 2019 home sales rebounded strongly (chart). A retreat of interest rates was certainly a contributing factor, but not the only one. Over the last decade, and especially in 2019, the Canadian housing market has enjoyed lift from the country's demographics.

Canada: A housing market revival?

Number of home sales



NBF Economics and Strategy (data via CREA)

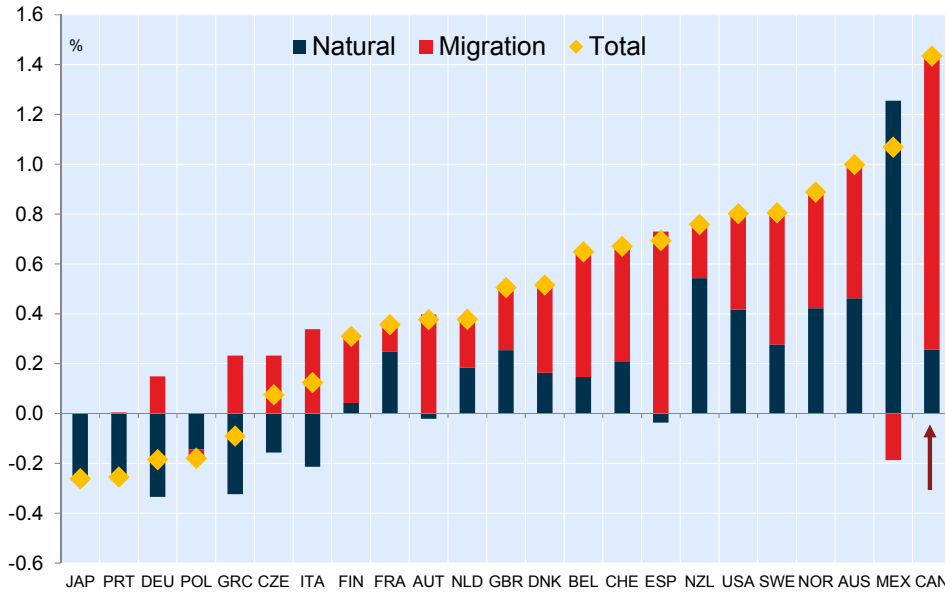
A population boom

Canada's population has been among the fastest-growing of the OECD countries for years now. But last year's 1.4% gain was exceptional, the highest in almost three decades. The gain in absolute terms was 530,000, more than the increase for France and England together, though their combined population is three times that of Canada.

And more than 80% of Canada's 2019 increase was due to net migration (chart).

Canada: Leading OECD countries in terms of population growth

2019 population growth, natural vs. caused by migration

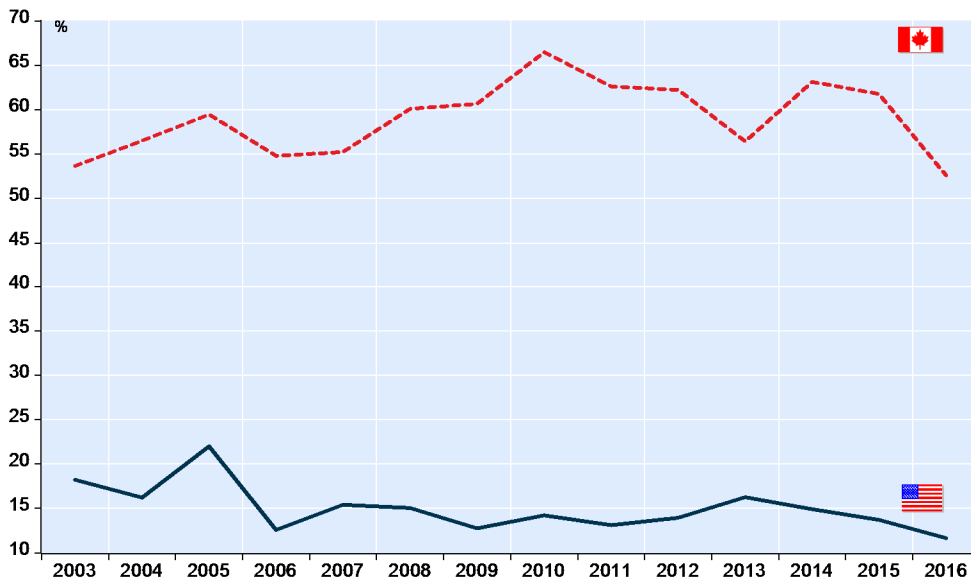


NBF Economics and Strategy (data via Statistics Canada and U.S. Census)

As we have often noted before, immigration to Canada stands out not only for its volume but for its composition. OECD data show that about 60% of the annual inflow of permanent residents are "economic" immigrants – applicants selected for "their ability to become economically established in Canada." That's four times the percentage for U.S. immigration (chart).

Canada: Immigration policy tilted to economic category

"Economic category" admissions to permanent residence as a share of total immigration

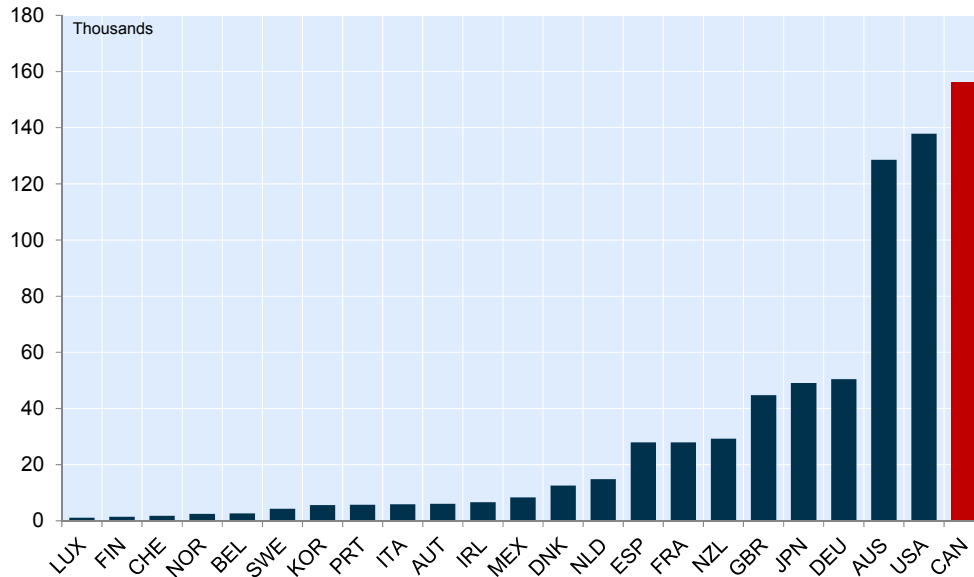


NBF Economics and Strategy (OECD data <https://data.oecd.org/migration/permanent-immigrant-inflows.htm#indicator-chart>)

In 2016, the most recent year for which the OECD has reported, almost 160,000 of those granted permanent residence in Canada were economic immigrants – more than the absolute number of such immigrants to the U.S. though the latter has 10 times Canada's population. Canada is now undeniably the biggest talent raider in the OECD.

Canada: Highest inflow of workforce-ready immigrants in the OECD

Annual "economic category" admissions to permanent residence (2016)

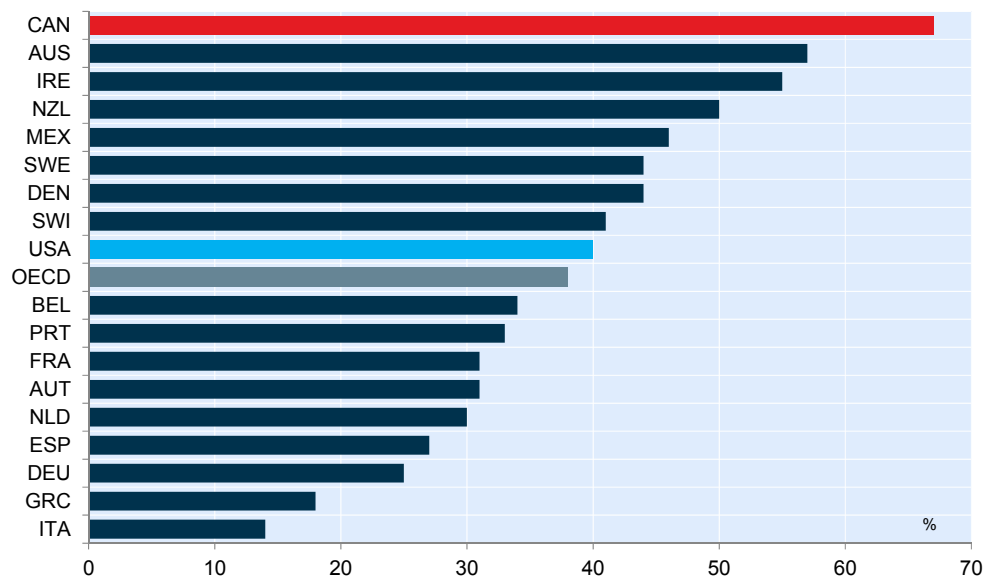


NBF Economics and Strategy (OECD data <https://data.oecd.org/migration/permanent-immigrant-inflows.htm#indicator-chart>)

Of its foreign-born population of working age (15 to 64), almost 70% have had post-secondary education, by far the largest proportion in the OECD and almost 30 percentage points higher than the proportion for the U.S. (chart).

Canada: foreign-born population is highly educated

Percentage of foreign-born 15-64 with post-secondary education (2017)

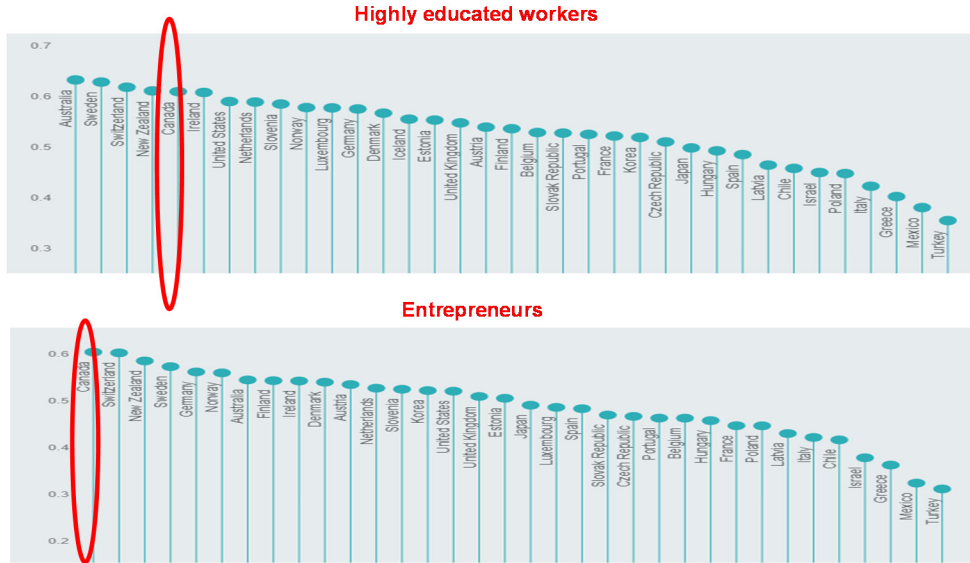


NBF Economics and Strategy (data via OECD)

According to the OECD, Canada has an environment highly attractive to the most able people. It ranks fifth for its offering of what skilled workers want and first for what entrepreneurs want (chart).

Canada: Among the best in global competition for talent

OECD talent attractiveness report (2019)

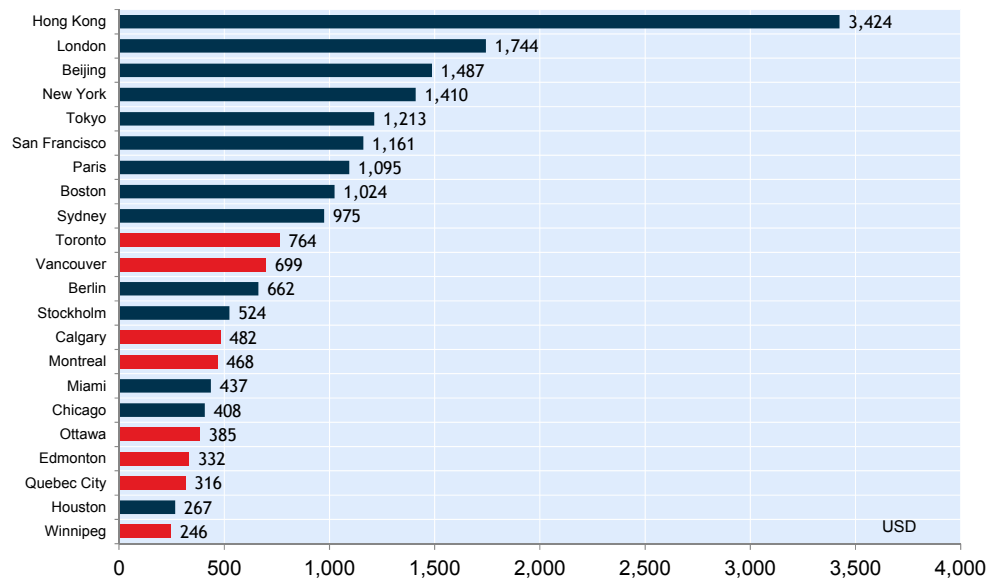


* Ranking based on quality of opportunities, income and tax, future prospects, family environments, inclusiveness and quality of life.
NBF Economics and Strategy (data via OECD)

Notwithstanding the home price increases of recent years, we doubt that the attractiveness of Canadian cities has been braked by affordability questions. The prices of its city-centre housing do not seem extreme relative to comparable apartments in other cities in the world (chart).

World: Perspective on downtown living cost

Price per square feet in USD for downtown living (June 2019)



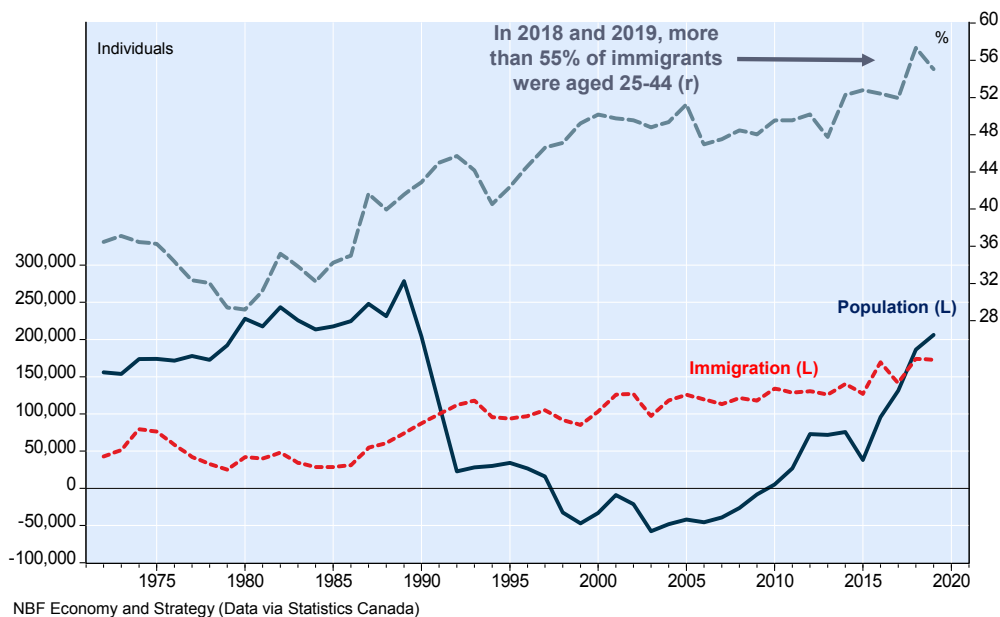
* For a 645 sq.ft. apartment
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A key age group: 25- to 44-year-olds

As noted above, Canada's population as a whole grew at a record pace in 2019, but what about the 25- to 44-year-old cohort that is crucial to household formation and housing prices? In 2019, like the population as a whole, this age group grew more than in any year since 1990. Almost all the growth was due to immigration, which is increasingly concentrated in this cohort. In 2018 and 2019 this age group accounted for more than 55% of immigrants, unprecedented in the last 50 years.

Canada: Perspective on first-time homebuyers cohort

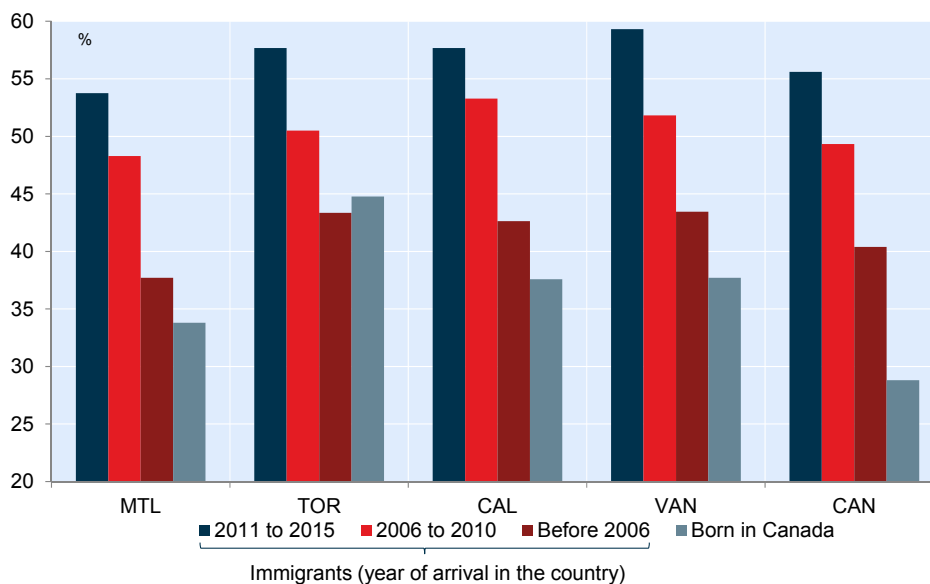
Change in population and immigration, 25-44



We can learn more about 25- to 44-year-old new arrivals in the most recent census, that of 2016. Countrywide, 55% of those who arrived in the five years preceding the census (2011-15) hold a bachelor's degree, a proportion higher than among those arriving earlier and, very strikingly, 27 percentage points higher than among those born in Canada (chart) – a huge difference.

Canada: Perspective on education of population aged 25-44

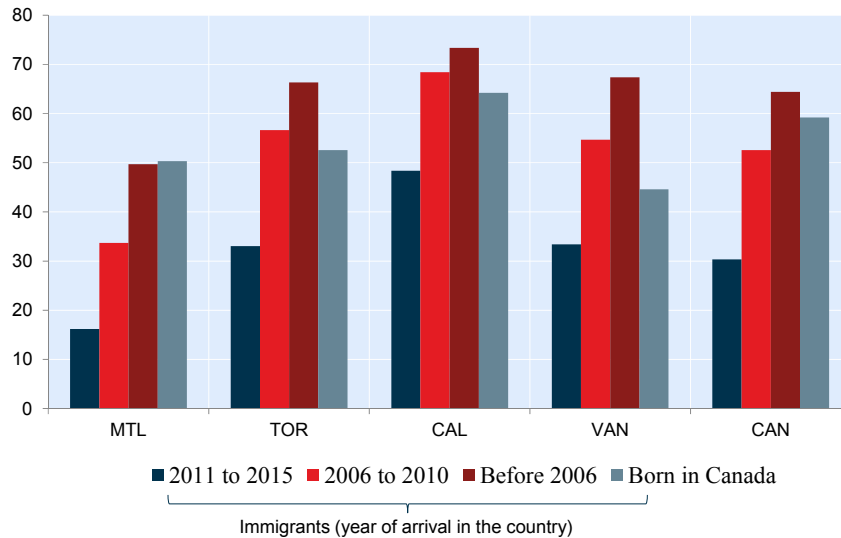
Share of population aged 25-44 having a bachelor degree - 2016



The census also reports that many become homeowners quite soon. No fewer than 30% of the 25- to 44-year-old immigrants arriving in the previous five years were homeowners. Among those who arrived between five and 10 years previously, 53% were homeowners, only 6 points less than the percentage for Canadian-born. In Toronto, Vancouver and Calgary their ownership rates were even higher than those of Canadian born (chart).

Canada: Homeownership rate of population aged 25-44

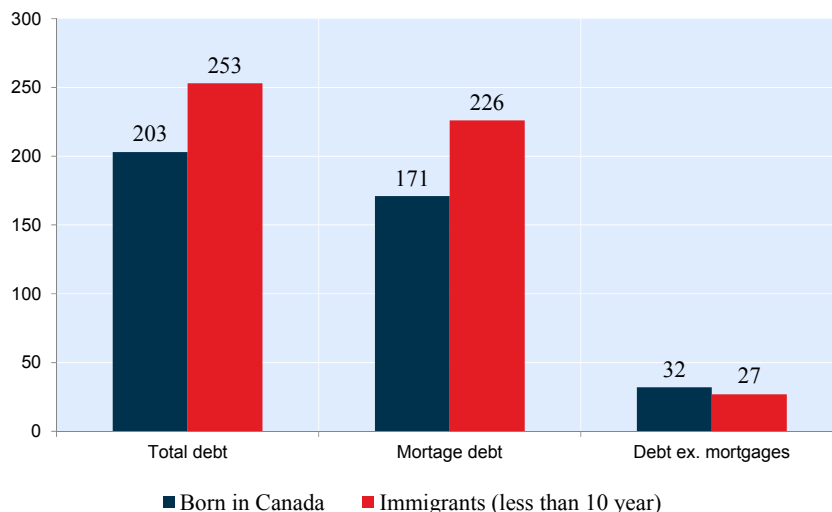
Homeownership rate (2016)



The appetite of immigrants for real estate is corroborated by a 2019 Statistics Canada [study](#).¹ It reports that 25- to 44-year-old immigrants have a ratio of debt to disposable income 25% higher than that of native-born Canadians, a difference due entirely to mortgage debt (chart).

Canada: Perspective on indebtedness of population aged 25-44

Debt to disposable income of population aged 25-44 (2016)



But the StatCan findings are reassuring about this higher debt of immigrants. Against expectations, all indicators of financial vulnerability show them in better shape than Canadian-born. Among credit-card holders, for instance, 58% usually paid off their balances every month compared to 52% for Canadian-born families. Only 2% had taken out payday loans in the previous three years compared to 6% for Canadian-born families.

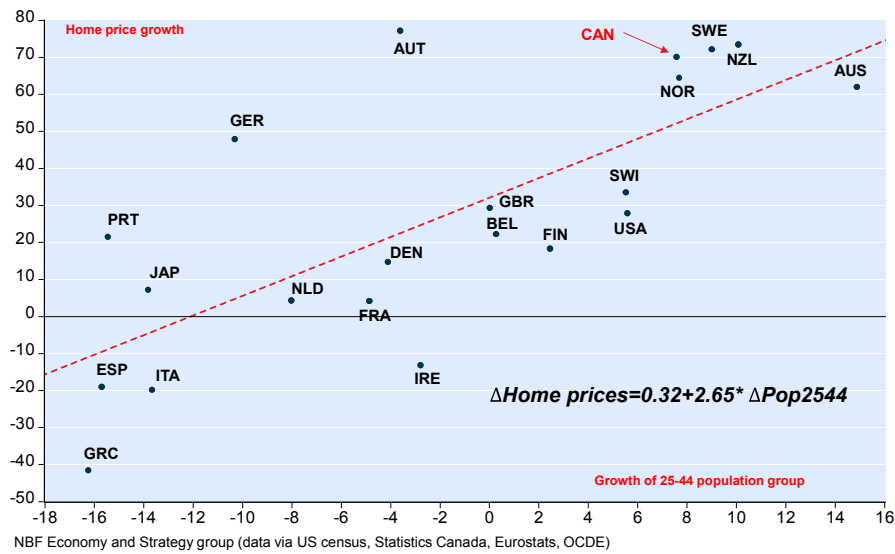
¹ René Morissette, "The Wealth of Immigrant Families in Canada," Statistics Canada, April 16, 2019.

Conclusion

Some see the rise of home prices in recent years as a serious vulnerability for the Canadian financial system. We do not share their pessimism. The vigour of the Canadian housing market is based elsewhere than in lax lending standards such as those that fuelled the U.S. housing boom leading to the Great Recession. Canada's immigration policy is unique in both its aggressiveness and its penchant for "economic" immigrants, those selected for "their ability to become economically established in Canada." Year in year out, about 60% of immigrants are in this category. Moreover, immigration is more concentrated in the 25- to 44-year-old age group than ever before. The growth or contraction of this cohort, crucial for household formation, correlates perceptibly with divergences among countries in housing asset prices since 2008 (chart). In every country, including Canada, in which this cohort grew more than 7% from 2008 to 2018, home prices rose at least 60% over the same period.

Canada: Demographics are crucial for housing assets

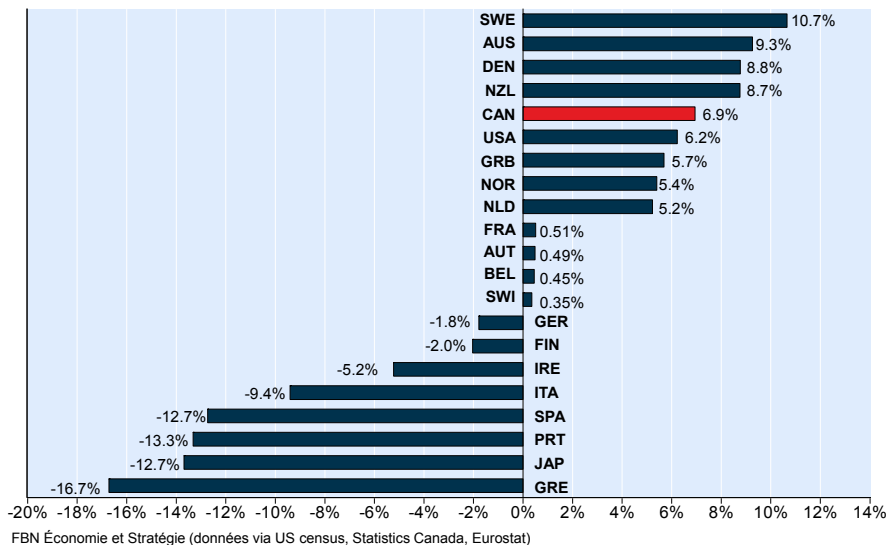
Change in home prices and change in population aged 25-44, 2008-2018



What about the coming decade? The Canadian government does not intend to slow the pace of immigration. On the contrary, it has raised its target from 300,000 in 2017 to 350,000 in 2021. Statistics Canada projects that the 25- to 44-year-old cohort will grow 6.9% over the next 10 years, keeping the country in an excellent relative position (chart). In other words, the vigour of the Canadian housing market is soundly based and set to continue confounding the skeptics.

Canada: Demographic remains supportive in the next decade

Growth of 25-44 population group (2020 à 2030)



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