

Visit noattacks.org

Before your child feels like a fish out of water.



THE GLOBE AND MAIL

February 9, 2010

Five warning signs of a bubble

By Tavia Grant
Globe and Mail Update

It's tough to spot an asset bubble until it pops. But here are five indicators in the housing market to watch

The trick with asset bubbles is you only know they were bubbles once they pop.

But there are warning signs.

With Canadian house prices approaching record highs, debate is heating up over whether Canada's housing market is in one. So far, few economists say the market is in bubble territory - though they expect the sector will gradually lose some steam later this year.

One exception is Bank of Nova Scotia. "The country is in a price bubble," economists Derek Holt and Karen Cordes said in a Tuesday note.

Here are five elements to watch in assessing whether a bubble is forming.

1. Affordability

Affordability is generally defined as the portion of pre-tax household income needed to service the costs of owning a home. And affordability is deteriorating as Canadian house prices rise. Homeownership costs rose in the third quarter of last year - the first gain in more than a year - as prices rose and mortgage rates inched higher, according to Royal Bank of Canada's most recent quarterly report.

Are we in a housing bubble? Share your thoughts at The Globe's forums

2. House prices

Sharp, sudden price increases can signal a problem. National house prices jumped 19 per cent in December from a year earlier and are seen climbing another 5.4 per cent to a record this year, the Canadian Real Estate Association says. Some of that percentage increase should be taken with a grain of salt though, as the comparison is with unusually low year-earlier activity, while big moves in some markets - such as Vancouver - skew the national average. Price increases on a weighted basis - which account for provincial proportions of privately owned housing stock - climbed 3.9 per cent last year.

3. Delinquencies

Canada's low rate of housing delinquencies underscores how different the situation is from the U.S.

Bubbles:

- Five bubbles set to burst in 2010
- Beware the gold bubble
- Housing market has big cracks
- Merrill warns of housing bubble
- Floating high on a delicate housing bubble
- Why China may be overheating
- Watch video: Bubble generation

Arrears - or the portion of mortgage holders who have gone three or more straight months without making a payment - were 0.44 per cent in November, according to Canadian Bankers Association statistics. It may seem a small portion, but is still the highest level in seven years.

4. Borrowing costs

Canada's key lending rate remains at a record low of 0.25 per cent and the Bank of Canada expects it will stay that way until the summer. The question is not whether rates will rise later this year, but how quickly. Any sudden increase in lending rates could see mortgage carrying costs balloon, putting additional burden on already strained household debt.

5. Regulations

Loose regulations have contributed to past bubble formations. In Canada, the heads of the country's six largest banks are calling on the federal government to tighten rules around buying a house. Getting mortgage insurance from CMHC or one of its competitors requires a 5-per-cent down payment, and the maximum amortization period is 35 years. Finance Minister Jim Flaherty said this weekend he sees no signs of a housing bubble in Canada - though there are "some signals" that are concerning. "There are certain tools available to the government if we choose to use some or all of them," he said.