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The western slump

By Jim Sutherland | June 08, 2011

Like a lot of people in the cottaging enclave of B.C.'s Gulf Islands, Scott Simmons once felt a touch of envy when he looked across the waters toward Washington state's San Juans. Back in 2001, the native Vancouverite made a living renovating and reselling Gulf Island houses and cabins, but property markets there and throughout British Columbia merely plodded along, while prices on the islands south of the border were exploding. If there was a silver lining, it was American buyers who took advantage of Canada's paltry dollar and limp real estate market to snap up bargain-priced vacation homes here. In places like the Gulf Islands, Whistler and the Muskoka region of Ontario, the phenomenon was pronounced enough to provoke a backlash. Should Canadians sit idly by while their cottage country went American?

Today, Simmons is a realtor on Salt Spring Island, and when people in his business think about the San Juans, their emotions run less to envy than to fear and foreboding. In 2005, 469 homes sold on the U.S. islands; by 2010, that number had fallen to 161. From a peak of $480,000 in 2007, median prices had dropped 27% by the first quarter of 2011. Meanwhile, the Gulf Islands enjoyed a boom of their own, with average prices soaring 150% between 2000 and 2008.

But now that boom, too, is emphatically over. Between 2008 and 2010, the average selling price on Salt Spring dropped to $508,000 from $635,000. In May, there were more than 400 listings on an island where, on average, only 15 residences are sold a month. Ozzie Jurock, a prominent Vancouver real estate consultant, recently surveyed the moribund B.C. recreational market on his blog, citing area after area where prices had dropped as much as 50% from the 2007–2008 peak, yet sale activity still lagged. Today, when someone mutters that cottage country is going American, the fear isn't that we're losing prime cottages to foreigners but that we're following the U.S. real estate market down the sinkhole.

While Jurock frames the meltdown in the B.C. and Alberta recreational markets as a buying opportunity, he admits the worst may not be over. Sales in prime western recreational regions are down significantly from 2010, while months of inventory (the time it would take to sell the current listings) are well into double digits. Some of the causes are regional and local, but other factors are relevant to vacation areas across Canada, leading to worries that the malaise could spread east.

The situation in B.C. is all the more remarkable because it goes against the typical pattern. Usually, recreational real estate follows the trend of urban markets, as homeowners take advantage of their growing equity to buy a second place—"the ripples spread out," says Jurock. But this time, the ripples aren't getting beyond city limits, even though in Vancouver prices for single-family homes rose 11% over the past year and now average around $2 million on the city's west side. Why the disparity? The current Vancouver frenzy is largely driven by buyers and speculators from mainland China, and most of that money is staying within city borders.

Another factor to keep in mind is that recreational property hasn't benefited from low interest rates as much as primary residences. While cheap mortgages have enabled more people to afford home ownership, vacation homes are generally not as highly leveraged. What's more, lenders charge significant, and growing, premiums for the second mortgages and home-equity-backed lines of credit that are often used for cottage financing.

As well, points out Jurock, the recreational and retirement property boom of a few years ago was "driven by Dad," whose investing prowess during the stock market run-up put him in a position not only to buy that retirement dream home but to front the kids a down payment for their own place. But, says Jurock, Dad lost the money in the crash, "didn't have the courage" to ride the markets back up, and so no longer has the rich feeling that inspires people to buy second homes.

Then there is the influence of gas prices—both the high ones and the low ones. CIBC economists estimate that more expensive gasoline will cost the average Canadian household an extra $950 this year. Pricey gas hikes the cost of getting to and from a weekend place, of course, while also diminishing cash on hand for discretionary items such as cottages. But in the West, a more significant gas price is that of natural gas, which has been bumping along at historically low levels and is expected to stay there for the next few years. In the Okanagan and other parts of the B.C. interior, dozens of ambitious developments launched in the years before 2008 were predicated largely on selling to Albertans, as were several lakeside developments in that province. Low natural gas prices, combined with changes in the provincial tax regime, probably deserve as much credit as the worldwide economic downturn for the carnage that has subsequently ensued, with at least 40 B.C. resort and condo developments in creditor protection or receivership, according to Jurock.

Finally, Canada's recreational markets—and this goes right across the country—face a formidable competitor today: cheap vacation properties across the border. According to a Leger Marketing poll, one in five Canadians is looking to buy real estate in the U.S., and while many are investors, a third or more are shopping for a second home, according to real estate agents in popular areas such as Florida, Arizona and the Las Vegas area. Canadians who have room in the budget for only one secondary residence are increasingly choosing the snowbird option because of the great deals. Jurock notes that his company regularly sells out its organized group scouting trips south of the border.

Royal Lepage president Phil Soper, for one, downplays the idea that Canadian recreational markets will be affected by the American slump, pointing out that people want to drive, not fly, to a summer place and, in any case, you don't escape summer heat by going to Florida or Arizona. Beyond the West, in fact, market trackers such as Royal Lepage's recreational property survey are seeing signs of a reawakening, as urbanites take advantage of gains in both equity markets and the value of their primary residences to fulfil pent-up cabin, cottage, chalet or fractional-ownership dreams.

But back on Salt Spring, Scott Simmons is seeing the flip side of the phenomenon that keeps Jurock busy guiding Canadians around American vacation spots. He believes about 20% of the listings rapidly accumulating on the island arise from Americans who bought a decade ago when prices in Canada were much lower and the loonie was worth 65¢ in U.S. dollar terms. Now, they want to sell here and buy closer to home in Washington state. Somewhere cheaper and easier to get to. Like the San Juans.