Here's what a prominent U.S. publication, Bloomberg Business Week, recently wrote about the Vancouver housing market:

Bubble or not?

By Bryant Urstadt

The Olympics are over, and the Village is for sale. The complex in Vancouver, British Columbia, that housed the athletes during the 2010 Winter Olympics has been converted into 1,100 luxury condos. About 450 have been pre-sold, and the sales of the remainder may well render a verdict on a mystery that looms over this city like Grouse Mountain: Did Canada prudently steer its way clear of the worst of the financial crisis only to be rewarded with a massive housing bubble of its own?

On a bright, warm Saturday in late June, couples and families wandered through the empty village, which has been renamed Millenium Water. It opened for public tours last month and draws about 100 people a day. Millenium Water is a city of the future, built with enviro-touches like green roofs and automatic shades that moderate the temperature inside the apartments. An 815-square-foot, one-bedroom apartment is on sale for C$879,000, which works out to C$1,078 per square foot, or $12 higher than the average price in Manhattan, according to The Corcoran Report. (A Canadian dollar is currently worth about U.S. 96 cents.)

Brokers are rock stars, cabbies flip condos, and shacks are going for $1 million.

Millenium Water isn't in downtown Manhattan, of course. It's not even in downtown Vancouver, which is across an inlet known as False Creek. It isn't really even in a neighborhood; the nearest establishment is the sales office for another condo development. If all this is starting to sound a little irrationally exuberant, especially given the shaky international outlook, well, that's Vancouver for you.

"Real estate is like a sport here," says Tracie McTavish, president of Rennie Marketing Systems, which is overseeing the sale of Millenium Water. In the last 12 months alone, the average home price has risen 14%, to around C$1 million. One can look at charts to understand how long and intense the climb in prices has been, with inflation-adjusted prices of an average home in Vancouver doubling in the last 35 years, but it is much more fun to watch The Vancouver Real Estate Market Roller Coaster, a video posted by the anonymous owner of the website Vancouver Condo Info. Using software called NoLimits, the programmer turned that graph of inflation-adjusted home prices into a high-definition roller-coaster ride. Starting with a warning, "Please fasten your safety belt. Keep arms and assets inside ride at all times," the years float by like mileposts during the ride: 1979, 1980, a long climb up to 1981, and then a harrowing drop down to 1983. But it is the ride up from 2000 to 2010 that is the steepest, and that, except for a brief drop in 2008, seems to go on forever.

The video ends with an imagined plunge into the ocean.

To a visitor, it can seem as if Vancouver's main industry is real estate, like it used to seem in Las Vegas or Orange County. A newcomer, emerging from the gate for international arrivals, is greeted with three separate backlit billboards, all offering architects' renderings of planned communities. Aspac Developments promises that they're "building a legacy of excellence." Concord Pacific describes each of its multiple developments as "a master planned world unto itself with park, schools, daycares, shops, restaurants, and resort-style amenities." Polygon calls itself "Vancouver's Builder of Choice," and offers contact information in English and Chinese. Driving out of the airport and up Vancouver's main thoroughfare, Granville Street, one notices billboards for brokers and advertisements on the backs of buses for Realtors and developments.

"Some of the brokers in Vancouver think they're rock stars," says Grant Connell, a broker with Sotheby's (BID). According to Connell, they are getting paid like them, too. "Many have made $500,000 or $1 million this year," he says. Connell, a former professional tennis player who spent years on tour, is among Sotheby's top-producing brokers. As of June of this year, he had amassed 52 "ends," as he calls a completed sale.

The market in Vancouver wasn't entirely unscathed by the financial crisis. Like the rest of the world, it took a hit. But prices rebounded, and the average home in the city is now about 10 percent above the pre-crash peak. On a driving tour, winding up a twisted knot of roads in the West Vancouver neighborhood, which stretches up a slope with a view of the bay and the mountains, Connell slows down by two similar homes. "I sold the first for $4 million right when it came on," he says. "The second was a little later to market. It took a long time to sell for $3 million. There's your 25 percent 2008 correction right there."

As Canada headed into 2009, Canadians jumped back into buying homes. Home prices in Canada have been strong from coast to coast, especially relative to the U.S. Vancouver prices, however, have run with special gusto.

In the second half of 2009, says Connell, "it was just spastic." He points to a narrow lot right on the beach, a vacant slot between two nice homes. "That was a $5.2 million sale last year," he says. "They tore down the home but never built anything."

In Vancouver, new developments are pre-sold via "assignment letters," or commitments to buy. Throughout 2009, say Connell and others, assignment letters were being flipped. "The minute I actually heard a taxi driver talking about flipping assignments," says Connell, "I knew something had to give."

Canada was supposed to have been safe from flippers, teardowns, bidding wars, and the other markers of the bubble that covered the States. Its banking system was voted the soundest by the World Economic Forum's most recent Global Competitiveness Report, and even President Obama has praised the country for being "a pretty good manager of the financial system and the economy in ways that we haven't always been." The mortgage default rate in Canada is less than half a percent, compared to

3.73 percent in the U.S., and its first quarter 2010 gross domestic product growth was a robust 6.1 percent. Reflecting its strength, Canada has been among the first of the developed nations to raise interest rates, pushing them up a quarter of a point on June 1, officially declaring its recession over.

"It could be that investors see Canada entering a renaissance," says David Rosenberg, chief economist at Toronto-based portfolio manager Gluskin Sheff. "As the old saying goes, in the land of the blind, the one-eyed man is King." Or as James Grant, editor of Grant's Interest Rate Observer, put it in a recent newsletter: "Such nice people, the Canadians—and solvent, too."

Canada's banking system is healthy in part because it went through a reform after a crisis in the early '90s. Though Canadian banks are among the largest in the world, and appear similar to the big American ones, they are much more tightly regulated—in ways that keep loan quality high and increase banks' incentives to hold those loans. Terms are largely dictated by the Bank of Canada; borrowers putting less than 20 percent down, for example, are required to purchase insurance from providers like Genworth or the Canadian Mortgage & Housing Corporation. Unlike in the U.S., the big Canadian banks write the majority of those loans. Lastly, the majority of Canadian loans are recourse, meaning that lenders can go after a borrower's earnings and assets; walking away is a very unattractive option. All this has made Canadian home loans sound and banks stable.

"Everybody always has a take on Vancouver (real estate) and nobody ever seems to be right."

– Grant Connell, Sotheby's International Realty Canada

All that safety and stability has come with a price. It may have overinflated prices. At least that's how some doubters see it. One Vancouver wag has actually been affixing "certified bubble pricing" stickers to Realtors' signs. Also among the skeptics is Petr Pospisil, a teacher in Vancouver who created a website called "Crack Shack or Mansion," in which the visitor attempts to guess whether a pictured bungalow is a bombed-out home of little value or a real Vancouver listing with a price of over a million Canadian dollars. Pospisil, alternately concerned and amused by what he saw as an irrational mania for real estate, got 30,000 views on the first day he put up the site. Within five days, 200,000 had played the game.

"Canadians defend their bubbles, especially here in Vancouver," says Pospisil. "People get angry when you tell them it's a bubble. They say it's different here, that this is such a beautiful place and everything is different. Everywhere there is a bubble, they say it's different."

Professionals like Robert Hogue, a senior economist at RBC Royal Bank, use less exciting language but fundamentally agree. "The type of price increases that we've seen in Vancouver are unlikely to be sustained," says Hogue. "There might be some downside risk to that market."

Some, like Garth Turner, a financial writer and former member of Parliament, see Canada going all the way down the road the U.S. took. "My basic view," he says, "is that we have a Canadian version of the U.S. real estate bubble. Not exactly the same, but close enough. We've relaxed lending standards, we have high unemployment, and we've reached a point of unsustainability in the housing market. I see real estate values falling shockingly."

Rosenberg notes three factors that have spurred home sales in recent months. First, as in the U.S., near-zero interest rates have kept mortgage prices at historic lows, sustaining demand for housing. Until June 1, the overnight rate target set by the Bank of Canada was one-quarter of a percent. It is now half a percent and expected to rise. Second, the Canadian Mortgage & Housing Corporation, Canada's hybrid version of the Housing & Urban Development Dept. and Fannie Mae, announced in February that in April it would be moderately tightening its standards for loans, decreasing the maximum length of loans from 40 years to 35 and increasing minimum down payments for certain types of loans. Third, a sales tax on services in Ontario and British Columbia goes into effect on July 1. The imminence of all three together has likely pushed some buyers to jump into the market, especially in Ontario and B.C.

Cameron Muir, chief economist for the British Columbia Real Estate Assn., argues for Vancouver's special situation, as do many in the trade. "Vancouver has had the highest prices in Canada for some time," says Muir. "The geography is constrained. You've got the Pacific on the West, the mountains to the north, the U.S. border to the south, and land reserves to the east. That puts tremendous upward pressure on land prices. We also have solid population growth with a sizeable proportion of immigrants." Vancouver is a city of just over 2 million, and Muir expects 40,000 immigrants this year. On top of that, says Muir, there are "high-networth Asian purchasers buying as investments, as second homes, or for satellite families."

Mainland China buyers are a fixture in conversations about Vancouver real estate, though reliable data on their numbers is elusive. "I'd say over half our high-end listings go to China buyers," says Connell. "Yesterday we did an open house for a $3.5 million home, and six groups came through. They were all Chinese."

Broker Andrew Hasman sees 70 to 80 percent of his high-end listings go to mainland Chinese. He oversaw an open house recently for a $1.8 million home. Of 100 visitors, 91 were from China. Spend enough time speaking with Rosenberg, Hasman, Muir, and others, and prices in Canada seem to make a kind of sense, a rational response to market forces that just so happens to have pushed prices way above the norm.

Like many brokers, Connell acknowledges that things are overheated. "I see it more stalling than anything. Units are starting to sit," he says, opening the door to a $3.8 million four-bedroom penthouse in Vancouver's downtown, in the seven-year-old Classico building. Decks on two sides look out over the tankers moored in English Bay, and Grouse Mountain beyond. It is a second home, full of stainless steel, granite, and floor-to-ceiling windows. At $1,688 a square foot, it is well over Manhattan's average. "This would have been snapped up just a couple of weeks ago," says Connell. But he's not overly concerned. "Everybody always has a take on Vancouver," he adds, "and nobody ever seems to be right." ■