

WEEKLY COMMENTARY

Kicking the Housing Correction Can down the Road in Canada

Randall Bartlett, Senior Director of Canadian Economics

Canada's housing market correction increasingly looks to be finding a bottom. Existing home sales have risen nationally in four of the six months through March 2023, while the average sale price has gained ground two months in a row. At the same time, new listings continue to drop and push inventories lower, propelling the national sales-to-new listings ratio back into seller's territory in March for the first time since April 2022. Going forward, we expect sales and the average home price to remain broadly unchanged into the middle of 2023 before picking up in the second half of the year.

While the average home price is down nearly 20% from its February 2022 pandemic peak, circumstances could have been much worse. On the demand side, surging population growth, a tight labour market, substantial pandemic-era savings, a declining price-to-rent ratio, and interest rates that are past their peak have all helped to provide a foundation to demand. Meanwhile, falling listings combined with a decline in housing presales and starts have all but guaranteed that new housing supply won't rescue those Canadians hoping for a meaningful improvement in housing affordability.

But the stabilization in the Canadian housing market is due to more than these drivers of housing supply and demand. Roughly three-quarters of all outstanding variable-rate mortgages with a fixed payment have seen the interest owed portion exceed the monthly fixed payment. This should have resulted in higher monthly payments or a lump sum payment to make up for the shortfall. However, a cursory look at the mortgage books of Canadian banks suggests lenders have made accommodations for many borrowers with these mortgages. Simply put, some lenders have extended the mortgage amortization period rather than increasing payment amounts. So instead of having variable-rate mortgage borrowers pony up the extra cost today, some financial institutions are allowing them to add the difference to their outstanding principal. As a result, over 20% of Canadian

mortgages at the Big Six banks had an amortization of more than 30 years in Q1 2023. In fact, as much as a third of some financial institutions' outstanding mortgage balances have amortizations of over 30 years. There was barely any mortgage in this situation as recently as Q1 2022.

This has created a conundrum for economic forecasters. In the past, if interest rates had increased to today's levels at the fastest pace in a generation, the recent housing correction would have been deeper than it was. Indeed, the rapid rise in interest rates was expected to cause an acceleration in listings and mortgage defaults, exacerbating the housing market rout. This should have led to a larger drag from residential investment as well as weaker consumption as household credit would have been more constrained. However, many Canadians were able to punt the impact of higher borrowing costs down the field to the time of renewal. This could mean the economic quake that many were expecting may be more of a sustained tremor, dampening economic growth over a longer period of time. Indeed, given that the bulk of credit extended at low interest rates was originated in 2020 and 2021, we could be a couple of years away from feeling the full weight of rate increases.

The one saving grace for many of these borrowers is that inflation is falling. In Canada, that has prompted the central bank to take a prolonged pause on interest rate hikes. In fact, markets believe its next move will be a cut. We are of the view that it could happen before the year is out. That might help some borrowers avoid the worst of higher borrowing costs. But they may not be able to avoid them altogether, having just kicked the can down the road.

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What to Watch For

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WEDNESDAY, May 10 - 8:30

April	m/m
Consensus	0.4%
Desjardins	0.4%
March	0.1%

FRIDAY, May 12 - 10:00

May	Index
Consensus	63.0
Desjardins	63.5
April	63.5

WEDNESDAY, May 10 - 21:30

April	y/y
Consensus	0.3%
March	0.7%

THURSDAY, May 11 - 7:00

May	
Consensus	4.50%
Desjardins	4.50%
March 23	4.25%

FRIDAY, May 12 - 2:00

Q1	q/q
Consensus	0.1%
Q4	0.1%

UNITED STATES

Consumer price index (April) – The consumer price index (CPI) was down on a year-over-year basis in March, falling from 6.0% in February to 5.0%. Price gains remained high, but it looks like the worst of the inflationary wave has passed, at least when it comes to the headline measure. CPI was also relatively weak on a month-over-month basis in March, rising just 0.1%. We expect it to come in higher in April on the back of a 5.4% surge in gasoline prices. Growth in food prices is also likely to have ticked up higher in April after remaining nearly flat in March. Stripping out food and energy, CPI probably rose 0.3% on a month-over-month basis, slightly less than in previous months. The all items index likely grew 0.4% month-over-month and was flat year-over-year at 5.0%, with core inflation edging down from 5.6% to 5.4%.

University of Michigan consumer sentiment index (May – preliminary) – We’ve been getting mixed signals from the consumer sentiment indexes the past few months. April saw a rise in the University of Michigan index but a dip in its Conference Board counterpart. There seems to be no clear direction for confidence as the economy remains strong but so does uncertainty. Lower oil and gasoline prices over the past two weeks could give a boost to May consumer sentiment, but the stock market is struggling and the risks around the US debt ceiling have grown. We don’t expect much movement in the University of Michigan index between the final April and preliminary May readings. That said, any developments involving the debt ceiling or banking sector in the next few days could swing things either way.

OVERSEAS


China: Consumer price index (April) – While it may seem like inflation has the whole world in its grip despite easing, China’s economy has been largely spared. In March, inflation stood at just 0.7%, both core and headline. China’s reopening at the end of 2022 even helped push inflationary pressure down rather than up, in contrast to the experience of most advanced economies. Will April’s print tell the same story?


United Kingdom: Bank of England meeting (May) – With inflation still hovering around 10%, the Bank of England (BoE) can’t really let up on monetary tightening now. We’re forecasting another 25 basis point rate hike and will be interested to see what the BoE signals about its next moves. The economy is showing signs of slowing, but will it be enough to convince the BoE that inflation is on its way back down to 2%? It seems more likely that further rate hikes will remain on the table.

United Kingdom: Real GDP (first quarter) – The UK economy avoided a technical recession by recording non-annualized real GDP growth of 0.1% in Q4 2022 following Q3’s 0.1% contraction. Barring a March surprise, the UK economy was likely back in growth territory in Q1 2023. Monthly GDP figures for the first two months of the year show carry-over growth of 0.1%. PMI readings suggest economic activity picked up in March, but other indicators are less positive, including a 0.9% drop in retail sales.

Economic Indicators

Week of May 8 to 12, 2023

Day	Time	Indicator	Period	Consensus		Previous reading
UNITED STATES						
MONDAY 8	10:00	Wholesale inventories – final (m/m)	March	0.1%	0.1%	0.1%
TUESDAY 9	8:30	Speech by Federal Reserve Governor P. Jefferson				
	12:05	Speech by Federal Reserve Bank of New York President J. Williams				
WEDNESDAY 10	8:30	Consumer price index				
		Total (m/m)	April	0.4%	0.4%	0.1%
		Excluding food and energy (m/m)	April	0.3%	0.3%	0.4%
		Total (y/y)	April	5.0%	5.0%	5.0%
		Excluding food and energy (y/y)	April	5.4%	5.4%	5.6%
	14:00	Federal budget (US\$B)	April	n/a	n/a	-378.1
THURSDAY 11	8:30	Initial unemployment claims	May 1–5	n/a	247,000	242,000
	8:30	Producer price index				
		Total (m/m)	April	0.3%	0.4%	-0.5%
		Excluding food and energy (m/m)	April	0.3%	0.2%	-0.1%
	10:15	Speech by Federal Reserve Governor C. Waller				
FRIDAY 12	8:30	Export prices (m/m)	April	0.3%	0.6%	-0.3%
	8:30	Import prices (m/m)	April	0.3%	0.6%	-0.6%
	10:00	University of Michigan consumer sentiment index – preliminary	May	62.8	63.5	63.5
	19:30	Speech by Federal Reserve Bank of St. Louis President J. Bullard and by Federal Reserve Governor P. Jefferson				
CANADA						
MONDAY 8	---	---				
TUESDAY 9	---	---				
WEDNESDAY 10	8:30	Building permits (m/m)	March	n/a	-2.9%	8.6%
THURSDAY 11	---	---				
FRIDAY 12	10:30	Release of the Bank of Canada's Senior Loan Officer Survey				

NOTE: Each week, Desjardins Economic Studies takes part in the Bloomberg survey for Canada and the United States. Approximately 15 economists are consulted for the Canadian survey and a hundred or so for the United States. The abbreviations m/m, q/q and y/y correspond to month-over-month, quarter-over-quarter and year-over-year change respectively. Following the quarter, the abbreviations f, s and t correspond to first estimate, second estimate and third estimate respectively. Times shown are daylight saving time (GMT - 4 hours).  Desjardins Economic Studies forecast.

Economic Indicators

Week of May 8 to 12, 2023

Country	Time	Indicator	Period	Consensus		Previous reading		
				m/m (q/q)	y/y	m/m (q/q)	y/y	
OVERSEAS								
MONDAY 8								
China	---	Trade balance (US\$B)	April	70.25		88.19		
Germany	2:00	Industrial production	March	-1.5%	1.8%	2.0%	0.6%	
TUESDAY 9								
France	2:45	Trade balance (€B)	March	n/a		-9,904		
France	2:45	Current account (€B)	March	n/a		-3.0		
WEDNESDAY 10								
Japan	1:00	Leading indicator – preliminary	March	97.9		98.0		
Japan	1:00	Coincident index – preliminary	March	98.7		98.6		
Germany	2:00	Consumer price index – final	April	0.4%	7.2%	0.4%	7.2%	
Italy	4:00	Industrial production	March	0.3%	-1.7%	-0.2%	-2.3%	
Japan	19:50	Current account (¥B)	March	1,358.3		1,089.2		
Japan	19:50	Trade balance (¥B)	March	-450.0		-604.1		
China	21:30	Consumer price index	April		0.3%		0.7%	
China	21:30	Producer price index	April		-3.2%		-2.5%	
THURSDAY 11								
United Kingdom	7:00	Bank of England meeting	May	4.50%		4.25%		
FRIDAY 12								
Germany	---	Current account (€B)	March	n/a		22.6		
United Kingdom	2:00	Real GDP – preliminary	Q1	0.1%	0.2%	0.1%	0.6%	
United Kingdom	2:00	Monthly GDP	March	0.0%		0.0%		
United Kingdom	2:00	Industrial production	March	0.0%	-2.9%	-0.2%	-3.1%	
United Kingdom	2:00	Index of services	March	0.0%		-0.1%		
United Kingdom	2:00	Construction	March	-0.2%	3.6%	2.4%	5.7%	
United Kingdom	2:00	Trade balance (€M)	March	-5,000		-4,805		
France	2:45	Consumer price index – final	April	0.6%	5.9%	0.6%	5.9%	

NOTE: Unlike release times for US and Canadian economic data, release times for overseas economic data are approximate. Publication dates are provided for information only. The abbreviations m/m, q/q and y/y correspond to month-over-month, quarter-over-quarter and year-over-year change respectively. Times shown are daylight saving time (GMT - 4 hours).