

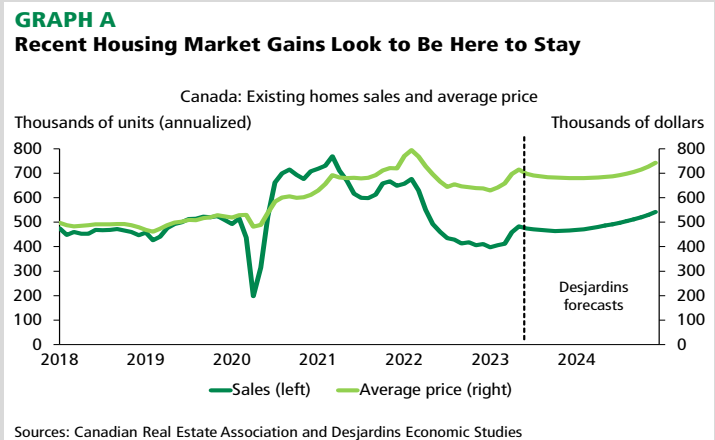
ECONOMIC VIEWPOINT

Canadian Residential Real Estate Outlook: For Better and for Worse, Canada's Housing Market Is Back

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Highlights

- ▶ Canada's housing market has rebounded sharply since March 2023. We think much of the recent gains are going to have staying power (graph A), leading to a further erosion of affordability.
- ▶ Housing demand is particularly strong in Canada, as surging population growth, a tight labour market and amassed pandemic-era savings provide a tailwind to activity. That said, some of this should be offset by higher interest rates. At the same time, new housing supply is expected to cool somewhat going forward, providing further support to prices.
- ▶ At the provincial level, sales activity has been particularly strong in British Columbia and Ontario since the beginning of 2023, and this has helped to push national prices higher. These are also the primary destinations for international immigrants. But a lack of affordability has forced younger residents to look further afield for housing, with Alberta being the primary destination. Other Prairie provinces are also benefitting from solid economic growth and better affordability. The same is true for the Atlantic provinces. Quebec's housing market hasn't seen the surge in activity that other big provinces have recently, but things look to be going from bad to worse on the new home construction front. This is the case at the national level as well.



Activity in Canada's housing market is back with a vengeance. But what's propelling it higher? Is it going to last? And what parts of the country are likely to be the most impacted?

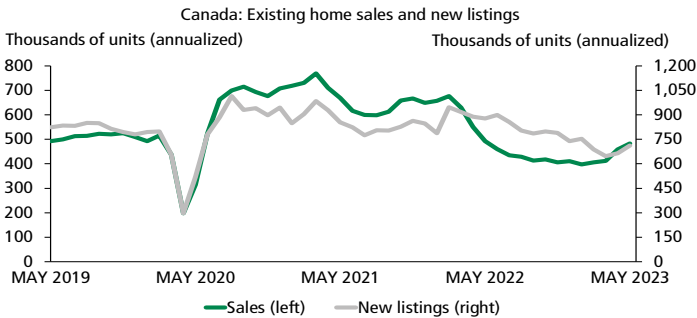
Housing Correction? What Housing Correction?

It was once believed that there were immutable laws of housing market physics. The most fundamental of these is that when interest rates go up and stay up, the housing market slows. And this is what we observed starting in early 2022. As the Bank of Canada began hiking rates from near-zero levels, home sales and prices fell sharply.

But that was then. By early 2023, the housing market had stabilized, coinciding with a prolonged pause in interest rates. Then came April of this year, when existing home sales made a sharp move higher. And May data suggest this change in direction may not have been a fluke.

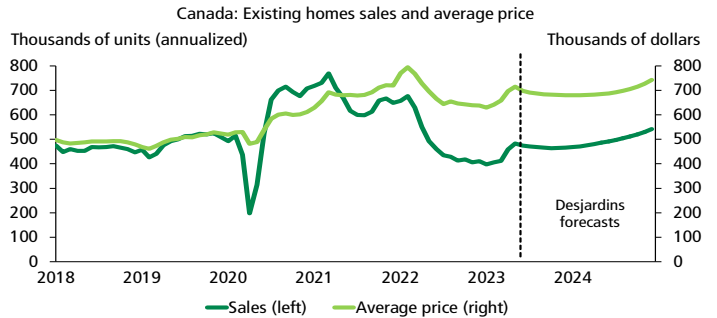
At the same time that sales have surged, listings have languished (graph 1 on page 2). Together, these indicators conspired to return the Canadian housing market back to seller's territory in March, and it hasn't looked back since (graph 2 on page 2). This has helped to push home prices higher as well, in part because

GRAPH 1
Home Sales Have Surged While New Listings Have Languished



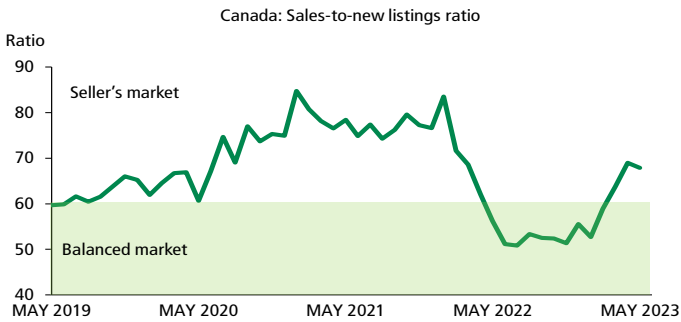
Sources: Canadian Real Estate Association and Desjardins Economic Studies

GRAPH 4
Recent Housing Market Gains Look to Be Here to Stay



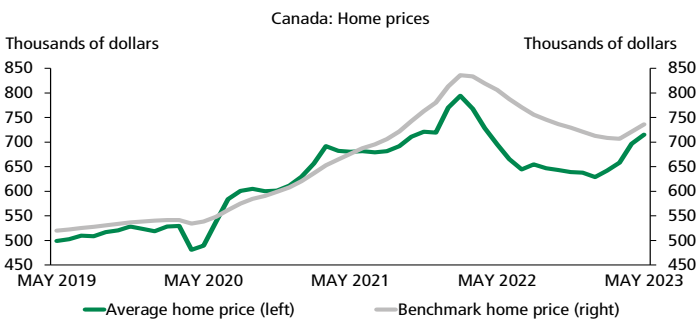
Sources: Canadian Real Estate Association and Desjardins Economic Studies

GRAPH 2
Canada's Housing Market Has Returned to Seller's Territory



Sources: Canadian Real Estate Association and Desjardins Economic Studies

GRAPH 3
Home Prices Are Climbing as the Housing Market Rebounds



Sources: Canadian Real Estate Association and Desjardins Economic Studies

recent sales activity and price gains have been concentrated in Canada's most expensive major cities (graph 3).

At the Bottom, There Is Nowhere to Go but Up

Looking ahead, we expect the recent jump in home sales and average prices to have some staying power (graph 4). There are a few reasons for this.

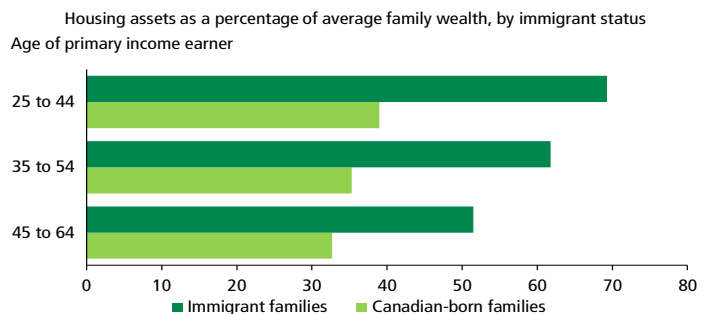
Drivers of Housing Demand

First, population growth is playing a key role in spurring renewed demand, driven by an elevated pace of immigration (graph 5). This current influx is far more than delayed immigration from early in the pandemic. Research by Statistics Canada has found that immigrants play an outsized role in Canada's housing market. They are more likely to own condominium apartments, row houses and semi-detached houses than Canadian-born homeowners. Housing is also likely to make up a larger share of the wealth of immigrant families (graph 6).

GRAPH 5
Population Growth Is Increasing at the Fastest Pace in Decades



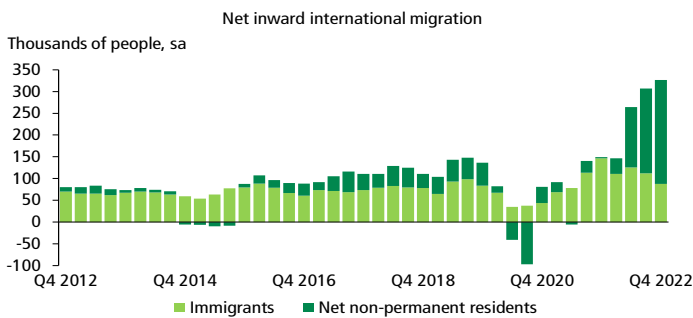
GRAPH 6
Real Estate Makes Up a Large Share of Immigrant Family Wealth



Sources: Statistics Canada and Desjardins Economic Studies

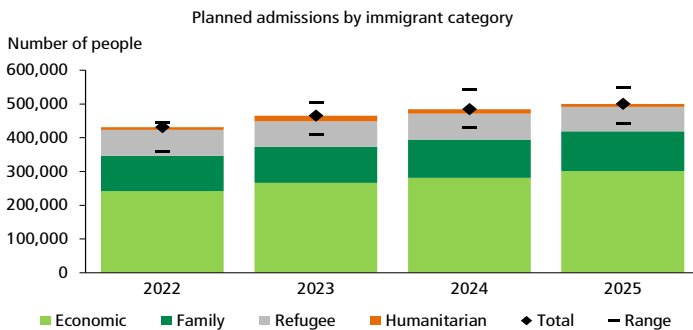
But the recent surge in population isn't just due to a rising number of immigrants. There has been an even more rapid increase in the number of non-permanent residents (graph 7). And while the federal government has provided targets for the number of future immigrants (graph 8), we don't know what the path for future non-permanent residents will be. This suggests some additional upside risk to our housing forecast.

GRAPH 7
Non-permanent Residents Are Driving the Number of Newcomers



Sources: Statistics Canada and Desjardins Economic Studies

GRAPH 8
Immigration to Canada Is Expected to Keep Setting New Records

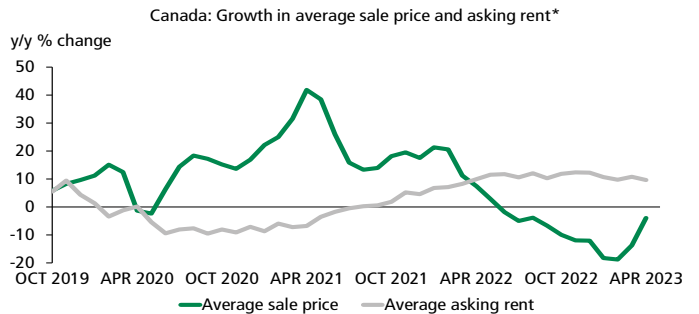


Sources: Immigration, Refugees and Citizenship Canada and Desjardins Economic Studies

Due to Canada's surging population, rents for new tenants have moved considerably higher as demand for all forms of housing has surged (graph 9). When paired with the recent decline in home prices, this has improved the math for some prospective homebuyers as price-to-rent ratios have moved lower.

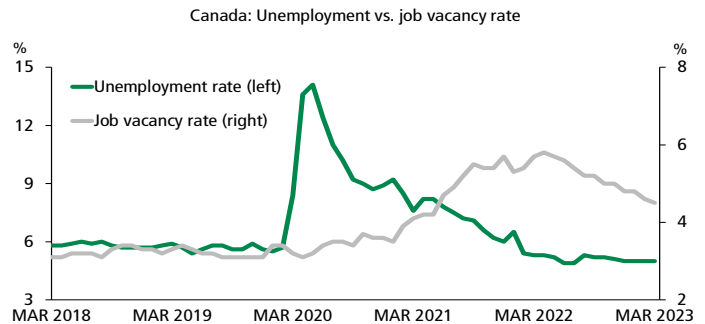
The Canadian job market is also providing a tailwind to home sales in Canada, as sustained employment and income gains have left households in a better financial position. Indeed, the job vacancy rate remains elevated and the unemployment rate is near its all-time low despite the surge in newcomers to Canada (graph 10). And while the May jobs data showed the first decline in employment since August 2022, it was entirely due to a drop among Canadians ages 15 to 24 and looks to be caused by anomalies related to summer jobs. As such, we don't think it says

GRAPH 9
Demand Has Been Pushing Asking Rents to New Highs



*Average sale price and asking rent for all unit types
Sources: Canadian Real Estate Association, Rentals.ca, Urbanation and Desjardins Economic Studies

GRAPH 10
Unemployment Remains Low but the Job Vacancy Rate Has Peaked

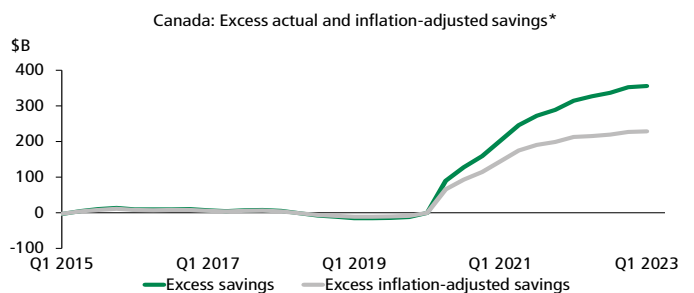


Sources: Statistics Canada and Desjardins Economic Studies

much of anything about the state of the Canadian labour market and won't mean much for monetary policy in Canada in the near term.

Sustained income growth isn't the only factor providing a tailwind to household wealth. During the pandemic, Canadians also amassed an enormous amount of savings (graph 11). And while these savings are disproportionately concentrated in the

GRAPH 11
Canadians Amassed Enormous Savings during the Pandemic

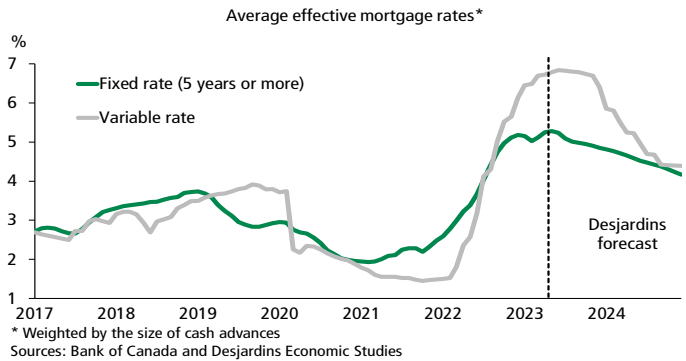


*The underlying trend is based on the 5-year cumulative average growth rate from Q4 2014 to Q4 2019
Sources: Statistics Canada and Desjardins Economic Studies

most affluent households, it is just one more factor contributing to the rebound in Canada’s housing market.

In this context, the final piece of the housing demand puzzle is interest rates. When the Bank of Canada announced its conditional pause on rate hikes in January 2023, markets took this as a sign that the central bank’s next move would likely be a cut. However, inflation hasn’t played ball. After gradually falling to 4.4% in March 2023—from a high of 8.1% in June 2022—it moved a tick higher in April. Further, a broad group of core inflation measures seem to be stuck in the 3.5% to 4.5% range (graph 12). When combined with surging housing market activity, real GDP growth and a tight labour market, this prompted the Bank to hike at its June meeting and signal that more rate increases may be on the way. Indeed, we expect one more 25 basis point hike will be delivered in July, with the door left open to more (graph 13).

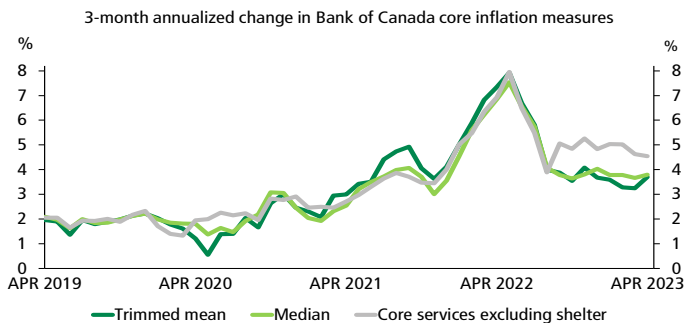
GRAPH 14
Borrowing Costs Have Risen Sharply but Are near Their Peak



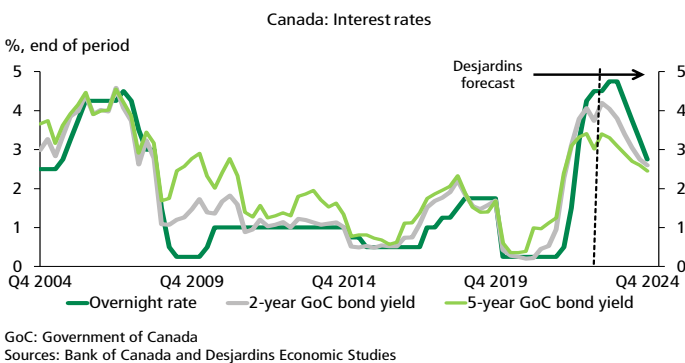
prospective homeowners think twice before entering the housing market due to the greater likelihood of more rate hikes to come.

But there’s a catch. As Milton Friedman once said, monetary policy works with long and variable lags. This means last year’s rate hikes haven’t been fully felt yet, let alone the most recent rate hike in June. However, not all Canadians, and particularly homeowners, are feeling the impact of higher interest rates equally. According to our research, there is a large group of homeowners with fixed-payment variable-rate mortgages that haven’t seen the full impact of the additional interest costs. This is because some have not been required to pay the interest portion of their mortgage payment that exceeds their monthly payment amount (graph 15). Instead, it has been added to their principal. This is equivalent to having extended the amortization period of their mortgages, blunting the impact of higher interest rates in the process (graph 16 on page 5). As we have written previously, this only means that there is likely to be more housing and economic pain down the road. Ultimately, lenders will need to get paid.

GRAPH 12
Core Inflation Came Down Quickly but Is Proving to Be Sticky

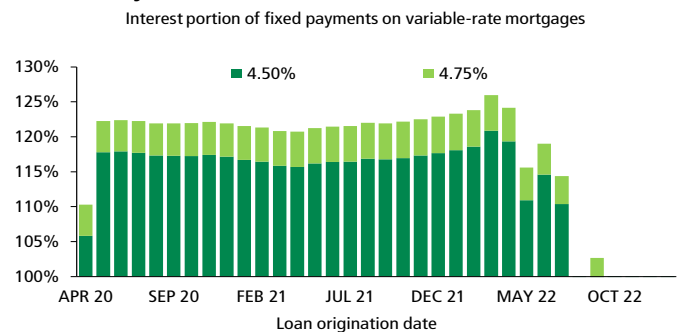


GRAPH 13
The Bank Is Expected to Hike at Least Once More before 2023 Is Out

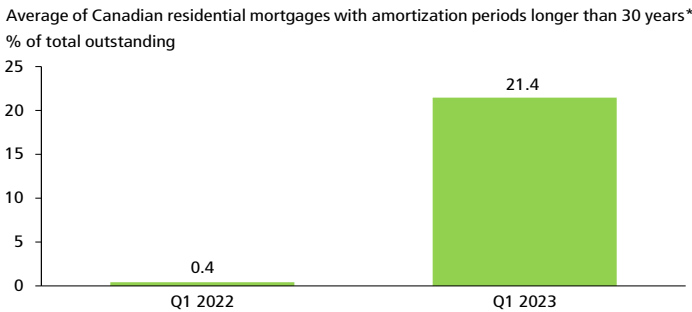


We think this will help to keep a lid on further increases in housing market activity in the next few quarters. Short-term interest rates have gone up, pushing borrowing costs higher (graph 14). The Bank of Canada has also demonstrated it’s serious about beating inflation. This should make some

GRAPH 15
The Interest Cost on Variable-Rate Mortgages Has Risen Dramatically



GRAPH 16
Some Homeowners Have Yet to Feel the Impact of Higher Rates



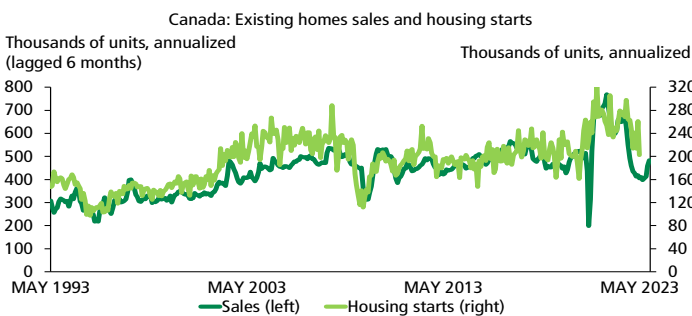
*Average is weighted by outstanding mortgage balances of the Big Six commercial banks
Sources: Commercial bank financial documents, Bank of Canada and Desjardins Economic Studies

Lack of Housing Supply

Despite higher interest rates, housing demand is expected to remain strong in the foreseeable future. But what about the housing supply in Canada?

Home construction has managed to hold up pretty well during the recent period of higher interest rates. Typically, housing starts follow resales by about six months, but they too have managed to defy gravity during the recent market correction (graph 17). However, if history is any guide, we don't expect elevated housing starts to last, as resale activity is still well below its pandemic peak.

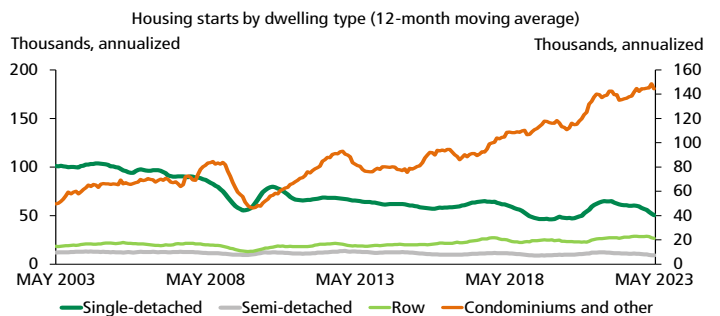
GRAPH 17
The Dearth of Supply Should Get Worse as Housing Starts Fall



Sources: Canada Mortgage and Housing Corporation, Canadian Real Estate Association and Desjardins Economic Studies

Further, most housing starts are condos (graph 18). As we discussed in our second report on the economic circumstances of Canadian youth, these homes continue to get smaller while detached homes get larger. According to the [Canada Mortgage and Housing Corporation](#), this is also emblematic of the dearth of supply in the "missing middle," which includes townhomes, duplexes and triplexes, and low- and medium-rise apartments. Taken together, this suggests a lack of new housing that is adequate to meet the needs of prospective homebuyers, which will help to keep upward pressure on home prices. And despite

GRAPH 18
Housing Starts Have Become Dominated by Condos



Sources: Canada Mortgage and Housing Corporation and Desjardins Economic Studies

ambitious policy announcements to the contrary, there is little meaningful relief in sight from any level of government.

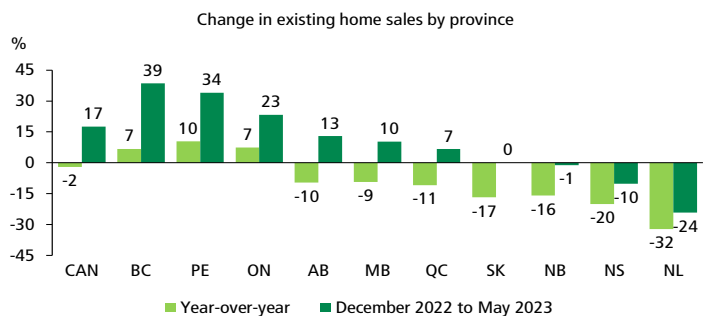
Let's Get Provincial

While the state of the national housing market is interesting, all housing is local. And developments in the housing market aren't the same in every province and city.

British Columbia

Starting with the West Coast, resale activity in BC has taken off in 2023 (graph 19). Concentrated in the Greater Vancouver Area, the shift toward resale activity in Canada's most expensive city has helped to push home prices higher in the province and brought up the national average.

GRAPH 19
Home Sales Have Taken Off in BC

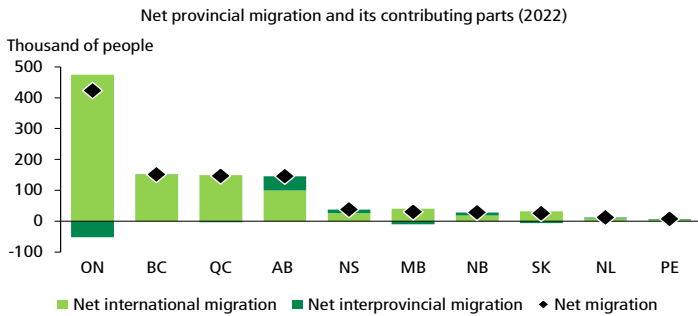


Sources: Canadian Real Estate Association and Desjardins Economic Studies

Ontario

But it isn't just a BC story. In Ontario, sales have increased by 37% since the end of 2022, and prices have edged higher as a result. This has been particularly pronounced in the Greater Toronto Area. International migration largely explains the surging population growth that has propelled housing demand in Ontario (graph 20 on page 6). That has more than offset the fastest pace of interprovincial population outflow on record, as

GRAPH 20
Ontario Is Receiving Nearly Half of the Immigrants to Canada



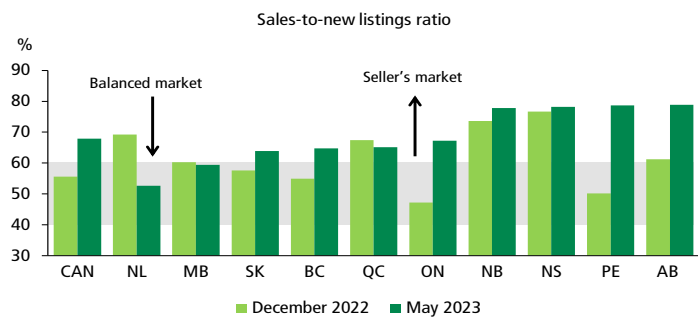
Sources: Statistics Canada and Desjardins Economic Studies

the sustained erosion in housing affordability has pushed young adults to seek greener pastures. (See our recent [report](#) for more information on the migration of young adults within Canada.)

Prairie Provinces

And where are these young Canadians going? They're going west. Alberta has been the primary destination of choice, thanks to its greater affordability and booming economy on the back of elevated commodity prices. (For more information, see our latest [provincial economic forecast](#).) The story is similar in Saskatchewan and Manitoba. Indeed, their respective housing markets are among the few in Canada that remain in or near balanced territory (graph 21).

GRAPH 21
Many Provincial Housing Markets Have Returned to a Seller's Market

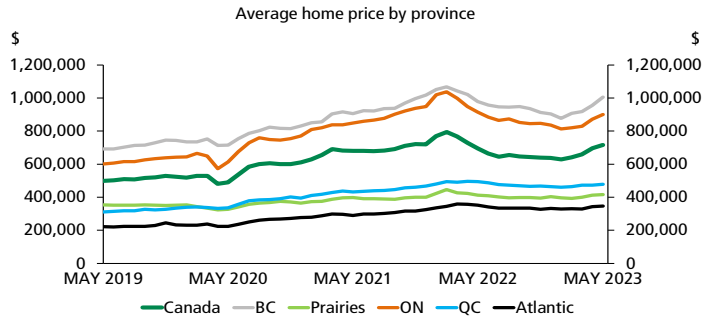


Sources: Canadian Real Estate Association and Desjardins Economic Studies

Atlantic Provinces

Speaking of housing affordability, the Atlantic provinces consistently top the list for the lowest-priced jurisdictions in Canada. And despite sustained population inflows from Central Canada during and since the pandemic, this hasn't changed (graph 22). However, it has had the unfortunate impact of pushing home prices significantly higher and making them further out of reach of prospective local homebuyers.

GRAPH 22
The Atlantic Provinces Remain the Most Affordable in Canada



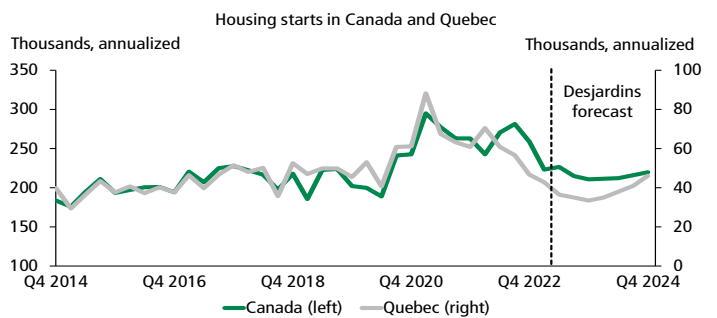
Sources: Canadian Real Estate Association and Desjardins Economic Studies

Quebec

While all the attention has been on the Canadian resale market gaining strength, the situation is more tenuous in Quebec. A slight increase in the housing inventory has seen prices level off somewhat, but on the whole it remains a seller's market, if only just.

On the new home construction front, it looks like things are going from bad to worse. New projects are down significantly across all market segments: single-family homes, condominiums and rental housing. The falloff in activity is province-wide, affecting most major and mid-sized urban centres. On an annualized basis, housing starts fell by nearly 30,000 units in May. We've downgraded our forecast again as a result of the weak activity observed since the start of 2023 (graph 23).

GRAPH 23
Housing Starts Are Expected to Fall Further before Rebounding



Sources: Canada Mortgage and Housing Corporation and Desjardins Economic Studies

For more information on our Quebec housing market outlook, please see [Spotlight on Housing: Quebec's Resale Market Has Stabilized, but New Home Construction Has Continued to Slide](#).

Conclusion

Canada's housing market has rebounded sharply since March 2023. We think much of the recent gains are going to have staying power, leading to a further erosion of affordability. Housing demand is particularly strong in Canada, as surging population growth, a tight labour market and amassed

pandemic-era savings provide a tailwind to activity. That said, some of this should be offset by higher interest rates. At the same time, new housing supply is expected to cool somewhat going forward, providing further support to prices. Unless something is done urgently to increase supply, affordability will get a lot worse before it has any hope of getting better.

TABLE

Canada: Major housing market indicators by province

	2019	2020	2021	2022	2023f	2024f
ANNUAL AVERAGE IN % (UNLESS OTHERWISE INDICATED)						
Existing home sales – Canada	6.5	12.6	20.5	-25.2	-9.1	10.0
Newfoundland and Labrador	9.7	14.7	45.5	-7.1	-0.2	-26.9
Prince Edward Island	-6.8	9.7	14.8	-18.1	-13.5	22.9
Nova Scotia	10.9	13.2	14.1	-21.7	-20.0	-5.1
New Brunswick	12.6	13.7	22.4	-20.5	-13.8	4.7
Quebec	11.4	16.4	-2.4	-20.4	-13.5	9.5
Ontario	9.0	8.8	18.5	-32.3	-16.8	24.1
Manitoba	8.5	14.3	17.2	-20.1	-19.3	6.1
Saskatchewan	1.5	24.6	24.1	-11.7	-10.8	12.3
Alberta	-0.1	4.3	53.6	-1.9	-22.4	28.7
British Columbia	-1.5	21.5	32.9	-35.2	-22.8	39.5
Average home prices – Canada	2.5	12.9	21.3	2.4	-1.7	2.9
Newfoundland and Labrador	-3.3	3.1	9.9	6.8	-4.2	-0.4
Prince Edward Island	12.2	18.8	20.6	13.8	-2.4	1.6
Nova Scotia	7.9	13.7	23.1	14.9	1.3	4.2
New Brunswick	2.9	10.5	26.0	17.6	0.0	6.9
Quebec	5.2	16.4	16.4	10.3	-3.0	-2.4
Ontario	6.4	16.0	23.6	6.8	-5.5	3.7
Manitoba	-0.1	4.4	9.8	7.9	-4.7	3.1
Saskatchewan	-0.4	2.5	6.9	0.6	-0.4	4.1
Alberta	-2.7	1.2	9.2	5.3	0.5	4.9
British Columbia	-1.5	11.6	18.7	7.4	-3.2	1.2
Housing starts – Canada (thousands of units)	208.7	217.8	271.2	261.8	218.7	214.8
Newfoundland and Labrador	0.9	0.8	1.0	1.4	1.0	0.9
Prince Edward Island	1.5	1.2	1.3	1.3	0.8	0.8
Nova Scotia	4.7	4.9	6.0	5.7	4.4	4.3
New Brunswick	2.9	3.5	3.8	4.7	2.9	2.9
Quebec	48.0	54.1	67.8	57.1	37.0	40.0
Ontario	69.0	81.3	99.6	96.1	86.1	80.9
Manitoba	6.9	7.3	8.0	8.1	6.7	6.3
Saskatchewan	2.4	3.1	4.2	4.2	3.4	3.3
Alberta	27.3	24.0	31.9	36.5	29.8	29.5
British Columbia	44.9	37.7	47.6	46.7	46.7	45.9

f: forecasts

Sources: Canadian Real Estate Association, Canada Mortgage and Housing Corporation and Desjardins Economic Studies