ECONOMIC VIEWPOINT

Desjardins Housing Outlook:

Will Falling Rates Send Home Prices Soaring?

By Randall Bartlett, Senior Director of Canadian Economics, Kari Norman, Economist, and Maëlle Boulais-Préseault, Economist

Highlights

- Falling interest rates have provided a tailwind to the Canadian housing market, and this is expected to continue through next year as rates fall further. Quebec and Alberta have been leading the resurgence in housing market activity among the big provinces, which isn't likely to change in the near term.
- But the rebound nationally so far has been more muted than previously expected, reflecting a tepid advance in sales in Canada's most unaffordable markets, including Toronto and Vancouver. The condo market in these major centres has been especially lacklustre, with smaller cities continuing to see strong price increases. Federal policy changes aimed at supporting first-time homebuyers should help, but only on the margins, as greater demand will ultimately push prices higher and undo some affordability gains.
- Homebuilding activity is expected to be soft in 2025, as interest rates remain elevated despite ongoing cuts, residential construction costs are high and the available construction labour force is limited. Ontario and British Columbia are expected to see the greatest decline in housing starts, albeit from a relatively high level thanks to the multifamily segment.
- Of course, if the Bank of Canada decides to accelerate the pace of interest rate cuts to offset the disinflationary forces of weaker-than-expected economic activity, this would spur a more rapid resurgence in Canada's housing market. Only time will tell if the Bank deems it necessary to hit the gas on the Canadian economy.

A lot has changed since we published our last Housing Market Outlook in early June. At that time, we explored the potential impact that impending interest rate cuts could have on the Canadian housing market. Since then, the Bank of Canada (BoC) has cut the policy rate by a total of 125 basis points over the course of its last four interest rate decisions. Local housing markets have responded in ways that were both predictable and surprising and that may portend future developments against the backdrop of a rapidly shifting policy landscape.

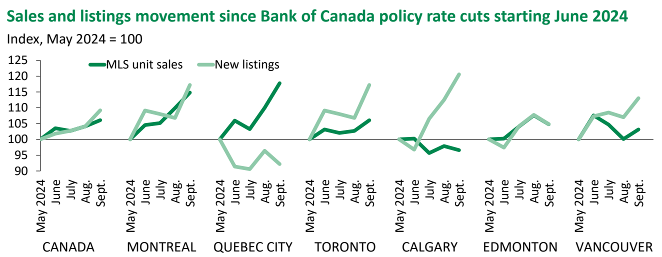
Recent Housing Market Developments Are Full of Surprises

The Canadian housing market has experienced considerable volatility in recent years due to both the COVID-19 pandemic and fluctuating borrowing rates. Exceptionally low interest rates during the early part of the pandemic helped to spur home sales. Prices rose due to high demand, particularly in smaller communities and among larger home types. Then, a series of BoC rate hikes through 2022 and 2023 made homeownership much less affordable, and sales tumbled. However, prices fell by far less, as fewer listings and a gradual but partial return to in-office work helped to arrest the decline. Surging population growth also helped to maintain a base of demand, particularly among new immigrants to Canada (as opposed to non-permanent residents (NPRs), who are much more likely to rent).

NOTE TO READERS: The letters k, M and B are used in texts and tables to refer to thousands, millions and billions respectively. **IMPORTANT:** This document is based on public information and may under no circumstances be used or construed as a commitment by Desjardins Group. While the information provided has been determined on the basis of data obtained from sources that are deemed to be reliable, Desjardins Group in no way warrants that the information is accurate or complete. The document is provided solely for information purposes and does not constitute an offer or solicitation for purchase or sale. Desjardins Group takes no responsibility for the consequences of any decision whatsoever made on the basis of the data contained herein and does not hereby undertake to provide any advice, notably in the area of investment services. Data on prices and margins is provided for information purposes and may be modified at any time based on such factors as market conditions. The past performances and projections expressed herein are no guarantee of future performance. Unless otherwise indicated, the opinions and forecasts contained herein are those of the document's authors and do not represent the opinions of any other person or the official position of Desjardins Group. Copyright © 2024, Desjardins Group. All rights reserved.

All these factors have remained in play since interest rate cuts began in June. But the response of the existing home market to lower borrowing costs has been tepid nationally and mixed across local markets. In the big cities of Toronto, Vancouver and Calgary, listings have been well outpacing sales (graph 1), pushing these markets toward greater balance or even favouring buyers in the case of Toronto. In contrast, Quebec City is experiencing the inverse, with rising sales and falling listings, putting it in a seller's market.

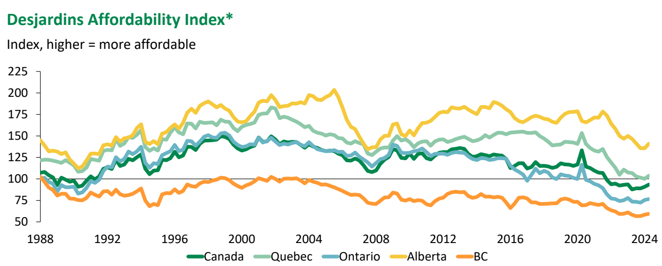
Graph 1
The Housing Market Response to Lower Rates Has Been Mixed So Far



Canadian Real Estate Association and Desjardins Economic Studies

This dynamic has predictably resulted in price gains, with Quebec and other more affordable provinces generally seeing the biggest moves since rates have come down. Relative affordability seems to have been an important factor contributing to the recent rebound in housing market activity (graph 2). Indeed, as we've highlighted previously in the context of interprovincial migration, people in their prime homebuying years have pulled up stakes and left more unaffordable regions of the country.

Graph 2
Alberta and Quebec Remain the Most Affordable of the Big Provinces

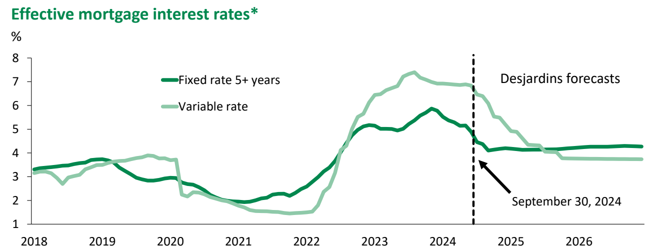


* Assumes a 20% down payment
Canadian Real Estate Association and Desjardins Economic Studies

How Low Could Mortgage Rates Go?

Following the Bank of Canada's 50-basis-point rate cut in October, we're expecting another rate cut in December and five more for 2025, each at 25 basis points. Altogether, this would bring the BoC policy rate down from 5.00% in early 2024 to 2.25% by the end of 2025. But as we recently reported, these widely anticipated rate cuts have already been priced into fixed mortgage rates. Variable rates will likely come down in proportion to policy rate cuts, but they're starting from a higher level than fixed mortgage rates (graph 3). And no matter how you slice it, the outlook is for mortgage rates to be higher than not only pandemic lows, but also pre-COVID levels.

Graph 3
5-Year Mortgage Rates May Have Bottomed Out



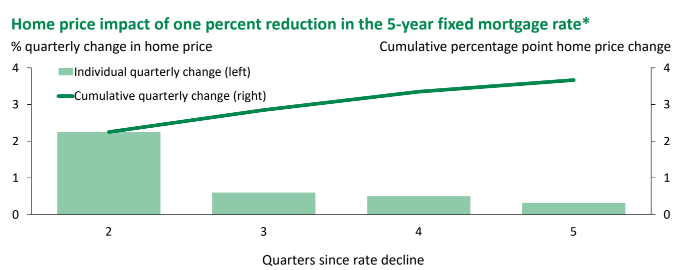
*Average cash advance rates posted by chartered banks
Bank of Canada and Desjardins Economic Studies

When Rates Go Low, Home Prices Go High

Falling interest rates lower the cost of borrowing, making monthly mortgage payments relatively more affordable for prospective homebuyers. Assuming incomes and employment continue to advance at a pace in line with our October Economic and Financial Outlook, the pool of qualified buyers will likely expand. That affordability boost should cause demand to increase. This begs the question: will home prices follow demand higher?

The answer is almost unequivocally yes. Lower borrowing costs increase buyers' purchasing power, enabling them to bid up property prices. This trend has been evident historically, albeit with a lag of a couple of quarters (graph 4). And recent work by the Bank of Canada (2022) has determined that, at least in the case of the US, the home price response to changes in interest rates may be even faster.

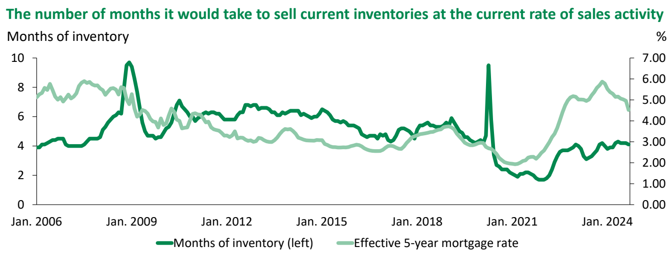
Graph 4
Lower Rates Boost Home Prices Most Noticeably After a Few Months



*Controls for labour market and housing market conditions; only the 2-quarter lagged rate cut is significant at the 10% level
Desjardins Economic Studies

While falling interest rates are generally linked with higher home prices, the extent of this effect can vary by region, depending on local supply and demand conditions. Regions with more balanced sales-to-listings ratios and larger inventories may experience a more moderate price appreciation. Nationally, rate cuts have been strongly associated with inventories falling and the sales-to-listings ratio moving toward seller's market territory (graph 5). This happens because buyers act quickly as homeownership becomes more affordable, thereby bidding up prices and erasing some of the affordability gains.

Graph 5
Mortgage Rate Cuts Are Often Correlated with Falling Inventory

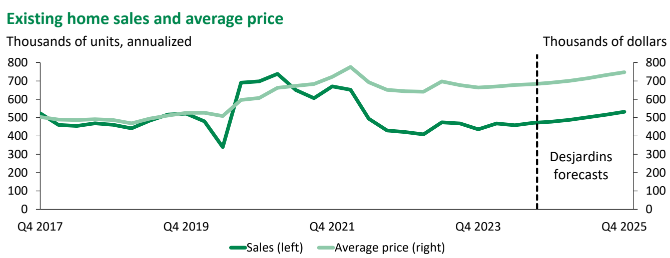


Canadian Real Estate Association, Bank of Canada and Desjardins Economic Studies

Where Do We See the Housing Market Going?

With interest rates set to fall further and policies being introduced to spur demand (see box 1 on page 4), our forecast is for a steady but subdued rebound in the Canadian housing market (graph 6). Existing home sales and prices should grind higher through the end of 2025, but still-high borrowing costs, an ongoing lack of affordability and slower population growth should act as headwinds to a more robust rebound.

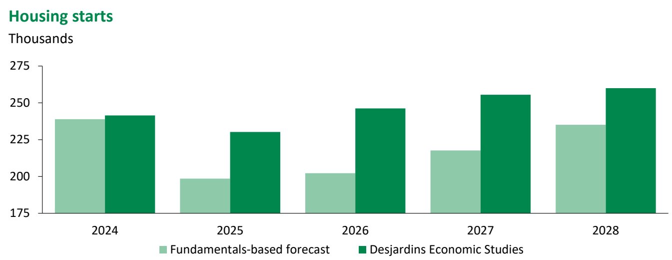
Graph 6
Home Sales and Prices Should Grind Gradually Higher on Lower Rates



Canadian Real Estate Association and Desjardins Economic Studies

Housing starts are a different story. Having outperformed (outside of Quebec) since interest rates ratcheted up starting in early 2022, they are very gradually coming down to earth. Multi-unit starts had been the big driver of homebuilding in many markets over the past couple of years, but falling condo presales are weighing on new construction (box 1 on page 4). We expect this to continue as interest rates remain elevated despite recent cuts, residential construction costs are high and the available construction labour force is limited. Quebec's housing starts dropped more acutely in 2023 given that they are largely concentrated in rental apartments. While lower interest rates have helped housing starts recover in 2024, the upside potential appears limited given these same constraints. For these reasons, we have called into question the ambitious homebuilding plans laid out by the Government of Canada (graph 7). We expect only a fraction of the additional housing will be built relative to federal plans, which will make a return to affordability all the more challenging.

Graph 7
Federal Housing Supply Policies Should Lead Starts Higher



Canada Mortgage and Housing Corporation and Desjardins Economic Studies

What If the Bank of Canada Cuts Rates Faster and Deeper?

While this outlook for a middling housing market rebound may not inspire many, an accelerated pace of rate cuts could spur additional sales activity by improving near-term affordability. For illustration, if the Bank were to reduce the policy rate at twice the pace we're currently expecting, not only would mortgage payments be lower and home sales higher, but economic growth, the labour market and incomes would improve along with it. Housing starts would also pick up, albeit after the surge in sales, eventually leading to greater supply as well. However, in that intervening period between sales rising and new housing stock becoming available, prices would also advance as the housing market moves into seller's territory (graph 8 on page 4). This would offset much of the affordability gains for potential new homebuyers.

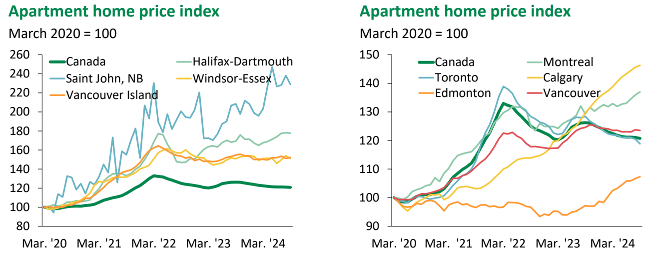
Box 1: Focus on Condos

One of the most notable trends in the Canadian housing market is the divergence between single-family homes and condos. In March 2022, condo prices peaked at 33% higher than at the start of the pandemic. On average they have dropped back, settling in at about 21% higher than pre-COVID prices. The biggest cumulative increases have been in smaller centres such as Saint John, NB; Halifax-Dartmouth, NS; Windsor-Essex, ON and Vancouver Island, although prices have been climbing rapidly in Alberta more lately (graph A).

Recent policy changes making real estate investing less profitable—such as constraints placed on short-term rentals—have led to a noticeable buildup in condo inventory in the Greater Toronto Area (GTA). Other urban centres have not experienced the same degree of inventory buildup.

On the other hand, recent federal government announcements permitting 30-year mortgages for all first-time homebuyers and all buyers of newly built homes, as well as extending mortgage insurance to homes of up to $1.5 million, may result in increased interest in properties in the more affordable end of the spectrum. In high-priced markets like Toronto and Vancouver, condos tend to frequently fall into this group. All else equal, the improvement in affordability from these policies would be notable, on the order of a 5–10% reduction in a household's monthly mortgage payment (table A). However, the resulting price response should ultimately reduce the savings generated.

Graph A
Condo Prices Have Grown Faster in Smaller Cities Since March 2020



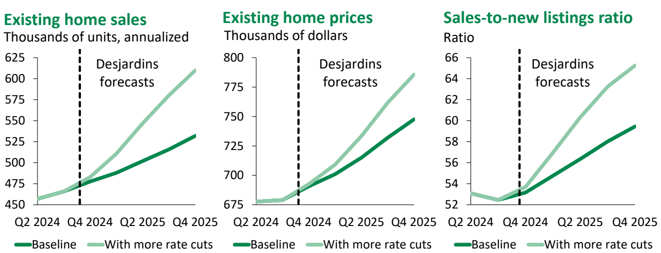
Canadian Real Estate Association and Desjardins Economic Studies

Table A
The New 30-Year Mortgages Increase Purchasing Power

	MLS benchmark price of apartment	New purchasing power	Increase in purchasing power	Additional downpayment required	Monthly payment at 25-year amortization	Monthly payment at 30-year amortization	Change in monthly payment
Greater Montreal	$410,900	$447,800	$36,900	$1,840	$2,360	$2,170	-$190
Greater Toronto	$668,300	$730,800	$62,500	$6,250	$3,790	$3,480	-$310
Ottawa	$417,100	$454,500	$37,400	$1,870	$2,400	$2,200	-$200
Calgary	$350,300	$381,700	$31,400	$1,570	$2,010	$1,850	-$170
Greater Vancouver	$768,100	$839,600	$71,500	$7,150	$4,330	$3,980	-$360
CANADA	**$521,100**	**$570,400**	**$49,300**	**$4,930**	**$2,990**	**$2,740**	**-$250**

Note: 5% mortgage rate compounded semi-annually; 4% mortgage insurance rate; downpayment of 5% up to $500k and 10% for $500k and above as required by CMHC; numbers may not add up due to rounding.
Canadian Real Estate Association and Desjardins Economic Studies

Graph 8
More and Deeper Cuts Would Push Sales and Prices Even Higher



Canadian Real Estate Association and Desjardins Economic Studies

Conclusion

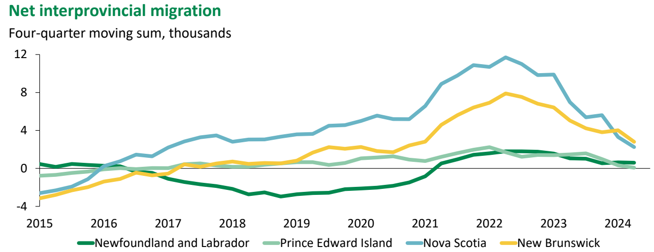
While home sales and prices are expected to grind higher on the back of gradual rate cuts, this could be accelerated if the Bank of Canada feels the need to cut interest rates more quickly. Recent measures introduced by the federal government to spur demand should also provide a modest tailwind to housing market activity. But strained affordability remains an issue, and new housing supply is expected to be slow to materialize. And even then, we expect it to be insufficient to restore affordability in most markets. Recent measures to slow population growth could instead prove more effective in taking pressure off demand and prices.

ATLANTIC REGION

Canada's East Coast has had among the most interesting housing markets to watch in recent years. Following a prolonged period of sluggish economic and population growth, the pandemic led to a surge in newcomers to the region looking for affordable housing in an era of remote work opportunities. This was followed by a spike in newcomers from abroad. Surging population gains pushed home prices higher. The rate of interprovincial migration peaked in 2022 and has since pulled back dramatically, dropping below pre-pandemic levels in Nova Scotia and PEI (graph 9). On the other hand, Atlantic Canada is less reliant on non-permanent residents (NPRs) for population growth, and thus population growth will be less affected by Ottawa's planned reduction.

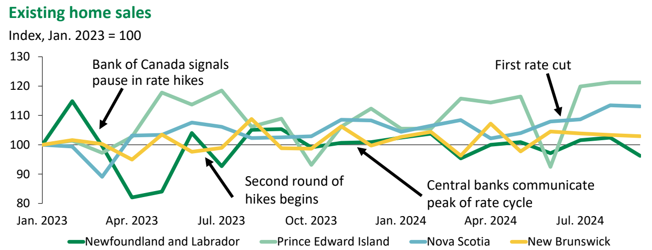
Home sales in the region were more resilient to monetary policy tightening than other parts of the country (graph 10). It's still early days in this round of rate cuts, and time will tell whether home sales and prices pick up steam. But for Islanders and Blue Nosers in PEI and Nova Scotia, respectively, lower borrowing costs seem to be putting wind in the housing market's sails.

Graph 9
The Interprovincial Migration Boom Continues to Fade



Statistics Canada and Desjardins Economic Studies

Graph 10
Housing Markets in Atlantic Canada Have Shown Little Response to Interest Rate Movements



Canadian Real Estate Association and Desjardins Economic Studies

QUEBEC

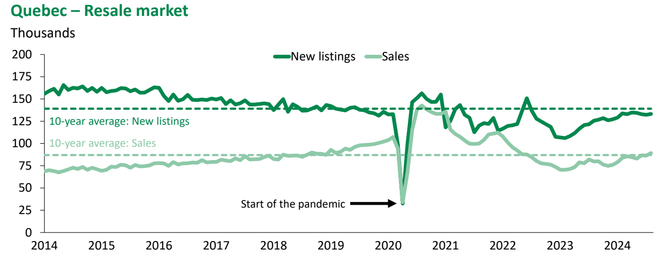
The Quebec housing market stands out from other provinces and is now on a clear upswing. Housing starts continued to recover across Quebec in the second quarter, even though they retreated in the third quarter. Rental units still account for 75% of that growth. Construction should grow more moderately in the next few months, but home building activity should overall remain supported by lower financing costs and incentives rolled out by many municipalities. We expect annual housing starts in Quebec to grow by 14.3% this year and another 4.5% next year. Construction of single-family homes and condominiums should rise by around 10% in 2024 and 4% in 2025. Rental apartment starts are on track to climb 30% this year and approximately 10% the following year.

Existing home sales through real estate brokers are improving in Quebec, after reaching their cyclical low in spring 2023 (excluding the temporary nosedive at the start of the pandemic). Recently, sales even returned to their 10-year average (graph 11). But as the saying goes, all real estate is local, and that's certainly the case in Quebec right now. Places like Quebec City and Sherbrooke are seeing sales gains north of 25% year-over-year, bringing bidding wars back, whereas Montreal and Gatineau are less exuberant, though still far stronger than the national average when it comes to sales momentum.

The total number of new existing property listings (houses, condos and plexes) is also close to its 10-year average. Last spring, the average time to sell was nearly five months, as it has been since fall 2022. At the peak of the pandemic real estate frenzy, average selling times were around two months, but the 10-year average is eight months. So while no longer torrid, Quebec's real estate market can hardly be described as fully back in balance, let alone a buyer's market.

Looking ahead, the recently announced loosening in mortgage insurance requirements will free up some pent-up demand in Quebec. Home ownership has not slipped as far out of the reach of first-time homebuyers as in some other large provinces. With a tightly supplied market and rental apartments continuing to dominate new construction, this should keep house prices rising. After the annual gain of 7% that we are tracking for 2024, we expect the average price to climb by another 8% in 2025. As a result, the affordability relief from lower interest rates and the conditional ability to obtain mortgage insurance on 30-year mortgages will be offset by higher prices.

Graph 11
Property Supply and Demand: Back to the 10-Year Average



Canadian Real Estate Association and Desjardins Economic Studies

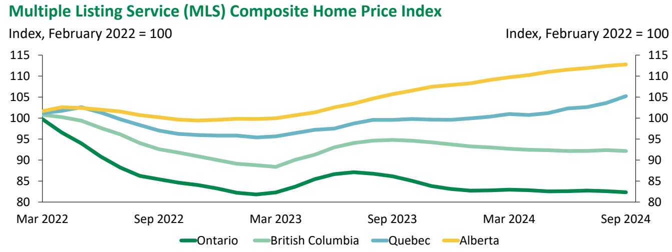
ONTARIO

Ontario stands out among Canadian provinces for the depth of its housing market doldrums and the lack of response to falling interest rates. Only British Columbia has seen the average home price perform worse among Canada's provinces since rates have come down. Looking at the benchmark price for a comparison across unit types, which provides a more apples-to-apples comparison of homes by accounting for their characteristics, the province performs even worse (graph 12).

The same is true when it comes to sales activity's response to falling interest rates, which has been muted in Ontario relative to other provinces. In contrast, new listings have shot up in the province, as sellers have stepped into the market even as buyers have remained on the sidelines. As a result, the Ontario housing market has become a buyer's market. And nowhere is this more true than in the Greater Toronto Area (graph 13), which is home to a large share of Ontario real estate transactions.

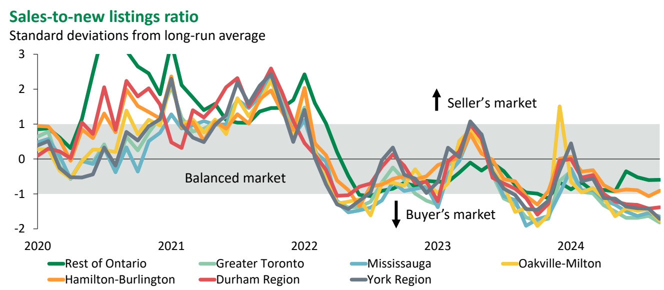
Looking ahead, the federal government's planned reduction in non-permanent residents is likely to hit Ontario particularly hard, weighing on housing demand. This should mitigate the home price gains relative to other provinces and support some improvement in affordability as incomes have an opportunity to close some of the gap with prices. But we still don't expect affordability to return to pre-pandemic levels any time soon.

Graph 12
Ontario Home Price Growth Has Been Lagging Other Markets



Canadian Real Estate Association and Desjardins Economic Studies

Graph 13
The Greater Toronto Area Is a Buyer's Market



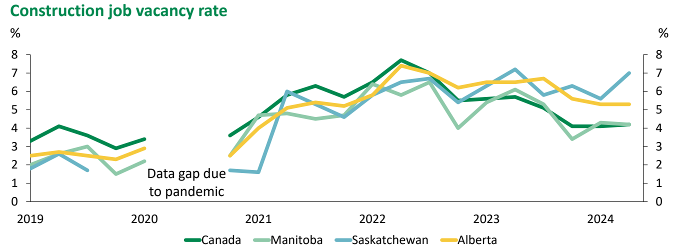
Canadian Real Estate Association and Desjardins Economic Studies

PRAIRIE PROVINCES

Desjardins Economic Studies has frequently highlighted the persistence of high job vacancies in construction and its potential impact on housing construction. Alberta's and Saskatchewan's job vacancy rates in the sector are even higher than the Canadian average (graph 14). Hiring in residential construction is no doubt competing with the resource sector for all manner of skilled tradespeople. The industry faces additional headwinds, with high—albeit falling—financing costs and inflation in the cost of construction materials.

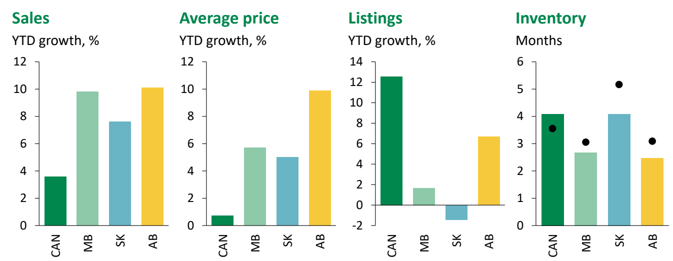
The resale housing market in Western Canada has outpaced the national average in 2024 to date (graph 15). Sales volumes are growing faster. Prices, particularly in Alberta, are higher in 2024 than they were a year ago, whereas they have stagnated nationally. Listings growth has fallen in Saskatchewan. In Manitoba and Alberta, listings growth has lagged behind sales volume growth. As a result, the number of months of inventory in the three western provinces has fallen from the same period a year ago, in contrast to the national average. Alberta continues to be the beneficiary of inflows of people from other provinces, which should help to keep the housing market going strong through 2025. However, this also means that Alberta's affordability advantage relative to some other provinces will continue to diminish.

Graph 14
Construction Labour Shortages Persist



Statistics Canada and Desjardins Economic Studies

Graph 15
The Resale Home Market Is Strong in Western Provinces



YTD growth: January to September 2024 as compared to January to September 2023
Months of inventory: Vertical bars are the average for Jan.–Sep. 2024; dots are the average for Jan.–Sep. 2023
Canadian Real Estate Association and Desjardins Economic Studies

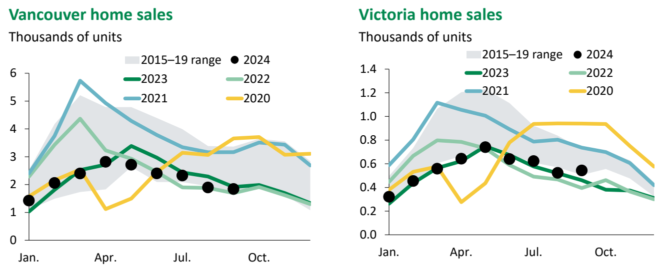
BRITISH COLUMBIA

The housing market in BC shows a great deal of weakness as we head into the final months of 2024. The province's highly indebted consumers have felt the pinch of higher rates when renewing their mortgages over the past couple of years, and that will continue even as rates start to come down.

Home prices are starting to fall in BC, particularly in Vancouver where the average price (seasonally adjusted) has fallen more than 5% from June to September of this year. Inventories have continued to climb and are now sitting at more than 6 months. Home sales in 2024 are at the low end of seasonal norms in both Vancouver and Victoria (graph 16). We anticipate BC's housing market to turn the corner in 2025, with home sales growing about 7% and prices picking up in line with the national average of 6.4%.

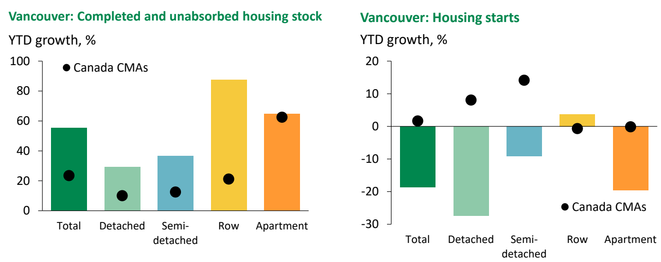
In new construction, Vancouver's completed and unabsorbed housing stock has climbed 55%, while new construction has fallen 18% this year as compared to the same period a year ago (graph 17). Looking forward, next year we expect housing starts in BC to fall faster than the national average, to about 39k from about 45k this year.

Graph 16
BC Home Sales Continue to Lag in 2024



Canadian Real Estate Association and Desjardins Economic Studies

Graph 17
Vancouver's Housing Construction Is Struggling



YTD growth: January to September 2024 as compared to January to September 2023
Canada Mortgage and Housing Corporation and Desjardins Economic Studies

FORECAST TABLES

TABLE 1
Canada: Major housing indicators by province

	2019	2020	2021	2022	2023	2024f	2025f
ANNUAL % CHANGE (UNLESS OTHERWISE INDICATED)							
Existing home sales – Canada	**6.5**	**12.5**	**21.1**	**-25.1**	**-11.2**	**5.2**	**8.7**
Newfoundland and Labrador	9.7	14.4	45.8	-7.1	-15.1	2.0	7.4
Prince Edward Island	-6.8	9.8	14.9	-18.2	-5.4	5.2	8.7
Nova Scotia	10.8	13.2	14.0	-21.7	-17.4	6.6	9.7
New Brunswick	13.1	13.4	21.8	-20.4	-13.7	2.7	7.4
Quebec	11.4	16.4	-2.4	-20.4	-12.8	15.0	8.4
Ontario	9.0	8.8	19.8	-32.1	-12.3	0.9	7.8
Manitoba	8.5	14.3	17.2	-20.1	-10.0	10.1	10.5
Saskatchewan	1.5	24.6	24.1	-11.7	-3.3	8.3	11.3
Alberta	-0.2	4.4	53.7	-1.8	-9.1	10.9	11.9
British Columbia	-1.4	21.2	32.8	-35.1	-9.2	-2.4	7.1
Average home resale price – Canada	**2.4**	**11.5**	**22.9**	**0.8**	**-2.9**	**1.5**	**6.4**
Newfoundland and Labrador	-3.1	1.3	10.5	7.1	0.9	7.7	6.0
Prince Edward Island	11.2	17.9	22.6	13.9	-1.7	1.2	6.6
Nova Scotia	8.1	12.5	24.1	13.4	3.4	6.6	7.9
New Brunswick	2.8	9.5	27.1	16.9	2.5	9.7	7.5
Quebec	5.3	15.0	20.4	9.7	0.3	7.1	8.0
Ontario	6.2	14.7	25.2	4.3	-5.1	-0.4	4.2
Manitoba	0.2	4.0	10.2	6.9	-2.7	6.0	7.1
Saskatchewan	-0.6	2.0	7.1	0.4	-0.8	5.3	7.9
Alberta	-2.7	0.7	9.3	4.7	1.3	10.0	10.6
British Columbia	-1.3	10.5	19.9	5.3	-1.4	2.4	6.4
Housing starts (thousands) – Canada	**208.7**	**217.9**	**271.9**	**261.8**	**240.3**	**240.1**	**228.9**
Newfoundland and Labrador	0.9	0.8	1.0	1.4	1.0	1.7	1.4
Prince Edward Island	1.5	1.2	1.3	1.3	1.1	1.6	1.4
Nova Scotia	4.7	4.9	6.0	5.7	7.2	7.8	6.6
New Brunswick	2.9	3.5	3.8	4.7	4.5	6.1	5.7
Quebec	48.0	54.1	68.0	57.1	38.9	44.5	46.4
Ontario	69.0	81.3	100.1	96.1	89.3	76.3	68.0
Manitoba	6.9	7.3	8.0	8.1	7.1	7.0	7.1
Saskatchewan	2.4	3.1	4.2	4.2	4.6	4.5	4.6
Alberta	27.3	24.0	31.9	36.5	36.0	46.0	48.7
British Columbia	44.9	37.7	47.6	46.7	50.5	44.6	39.1

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