WEEKLY COMMENTARY

When It Comes to Housing Supply, We're Livin' on a Prayer

By Jimmy Jean, Vice-President, Chief Economist and Strategist

The latest federal budget focused heavily on housing affordability, a major social issue. The dream of home ownership is slipping away for many Canadian households. Low interest rates, strong population growth, the rush to buy before prices and mortgage rates rise further, and increased speculative activity have all driven up demand.

Supply hasn't kept up despite a fairly high level of housing starts in recent years. Hence today's record-low housing inventories. The Canadian Real Estate Association's MLS® Home Price Index has risen by an average of 15% over the past two years. The Desjardins Affordability Index for Canada sank to its lowest level in almost 15 years, illustrating the widening gap between price and income growth.

So we were expecting to see a 2022 federal budget with a lot of strong measures to boost the housing supply. What we found was a clearly stated problem: Canada will need to double its current pace of homebuilding to meet demand over the next decade. For context, in the last 5 years, Canadian housing starts have averaged about 230,000 per year.

But we didn't find a very convincing strategy. The government announced a Housing Accelerator Fund aimed at building 100,000 units over five years. That averages out to just 20,000 units per year. It also announced funding for 6,000 affordable housing units over two years. And while the budget mentioned 4,300 units for the vulnerable and 6,000 co-op units, the funding for these programs was already included in prior initiatives. In other words, it's not new money. Big picture? There's a significant gap between the current pace of homebuilding and the supply that will be needed every year, but by our estimate, the budget measures would close less than 20% of the annual gap, and only in the first few years of the projection period. Some of the remaining gap in the federal government's plans could be filled by units promised in the 2017 National Housing Strategy, but the success of this initiative has been mixed.

And then there's the demand side of the equation. Against the fairly modest additional housing supply that is being proposed, there may be a bump up in demand from the doubling of the First-Time Home Buyers' Tax Credit, as well as from the introduction of the First Home Savings Account, to be launched next year. While the government did ban foreign buyers for two years, available data indicates that non-residents play a fairly marginal role in today's housing market. The anti-flipping tax measure was a positive step to discourage speculation, but it's unclear how much additional supply it will free up.

Ultimately, the aggressive monetary policy tightening on display this week from the Bank of Canada should cool demand for housing. But unfortunately, monetary policy can't build homes. In fact, higher rates will represent a headwind for residential investment. So will labour shortages, as the number of unfilled construction jobs has nearly tripled in the past year. To be sure, measures taken in the budget to increase supply are a step in the right direction. But given the importance of adequate housing supply to Canada's economic outlook, we'll have to pray for more decisive policy in the future.

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Week in Review

By Randall Bartlett, Senior Director of Canadian Economics, Francis Généreux, Senior Economist, Lorenzo Tessier-Moreau, Senior Economist, and Hendrix Vachon, Senior Economist

- **The Bank of Canada announced an increase in the target overnight rate from 0.50% to 1.00%** — the first time we've seen an interest rate hike of this size since May 2000. The BoC has also announced the ending of reinvestment, and it will begin quantitative tightening, effective April 25. During the press conference, Governor Macklem chose to set Canadians up for another round of aggressive action in June by suggesting that the Bank could continue to raise rates 'forcefully', if needed. That opens the door to another 50bp hike at the next announcement. Still, we see the overnight policy rate ending the year around 2%. We see scope for some further tightening in 2023, but don't believe the BoC will match the Fed in taking rates above 3%, given the greater weight of real estate in the Canadian economy.

- **Bond yields continued to climb early in the week.** The U.S. 10-year yield surpassed 2.80%. Signs of moderation in U.S. inflation helped reverse the trend in bond yields. Investors are also more worried about future economic growth, which is hurting the stock markets, but benefiting the bond market. The fact that the Bank of Canada showed much more unease over inflation, in addition to raising the estimate for its neutral rate, contributed to a reduction in the spread between the Canadian and U.S. bond yields Wednesday.

- **Canadian manufacturing sales increased for the fifth consecutive month in February**, besting our call and consensus with a 4.2% m/m advance in the month. Manufacturing sales volumes were up 2.2% in February, making clear that this wasn't just a price story. And if you were looking for a meaningful impact of the blockades at the Ambassador Bridge and other major border crossings, you won't find it in February's manufacturing data. Among industries, 14 of 21 reported higher sales, led by the motor vehicle (+25.0%), food (+5.3%), petroleum and coal (+6.7%), and wood (+8.5%) industries. In contrast, sales of computer and electronic products decreased the most, down 7.9% in February. Total manufacturing sales rose 19.5% on a year-over-year basis in February.

- **Wholesale sales fell 0.4% m/m in February**, underperforming our view and that of consensus for the first decline since July 2021. Lower sales were posted in the personal and household goods, building material and supplies, and motor vehicle and motor vehicle accessories and parts subsectors, while sales in all other subsectors increased. Volumes of wholesale goods sold fell 1.4% in February. Notably, the value of wholesale inventories reached another record high in February, making the last nine of ten months record breaking.

- **Retail sales rose 0.5% in March in the United States.** This is a result similar to the consensus expectation. The strongest growth obviously stems from the 8.9% increase in the value of sales at service stations. Excluding these and purchases at car dealerships (-1.9%), retail sales advanced by only 0.3%. However, there were good increases in clothing (+2.6%), electronic goods (+3.3%), goods associated with leisure activities (+3.3%) and general merchandise stores (+5.4%). Nonstore retailers' sales, however, fell 6.4% in March. In general, we see an acceleration in real consumption for the first quarter, but the situation should be slower from the second quarter.

- **US consumer confidence has improved** according to the University of Michigan index. It rose from 59.4 in March (a low since the summer of 2011) to 65.7 according to April's preliminary version. The recent drop in gasoline prices from mid-March highs appears to have helped household sentiment.

- The U.S. consumer price index (CPI) jumped 1.2% in March after rising 0.8% in February. Energy prices soared 11.0% in March, the largest monthly increase since September 2005. Core CPI, which strips out food and energy, edged up 0.3% in March, the slowest pace since September. The all-items index rose 8.5% for the 12 months ending in March, up from 7.9% in February. It's the largest 12-month increase since December 1981. Core inflation rose from 6.4% to 6.5%, the biggest 12-month change since August 1982. **Inflation was up again in March**, but we've probably already seen the peak 12-month increase or will soon.

- **The producer price index (PPI) also rose sharply in March** in the United States, with a monthly increase of 1.4%. Unlike the CPI, growth in the price of goods, excluding food and energy, remained strong at 1.1% after two successive gains of 0.8%.

What to Watch For

By Royce Mendes, Managing Director and Head of Macro Strategy,
Randall Bartlett, Senior Director of Canadian Economics, and Francis Généreux, Senior Economist

UNITED STATES

TUESDAY April 19 - 8:30

March	
Consensus	1,748,000
Desjardins	1,800,000
February	**1,769,000**

Housing starts (March) – After a short-lived decline in January, housing starts jumped 6.8% in February. Another increase is expected for March. Building permit numbers are still quite high, which bodes well for new construction, even though it continues to be constrained by supply issues. The weather was fairly mild in March, except in the Midwest. Employment in residential construction faltered somewhat in March. The gain should therefore be rather modest. We expect housing starts to hit 1,800,000 units.

WEDNESDAY April 20 - 10:00

March	
Consensus	5,800,000
Desjardins	5,800,000
February	**6,020,000**

Existing home sales (March) – Home resales plunged 7.2% in February after gaining 6.6% in January and declining 3.8% in December. Another contraction is expected in March as signalled mainly by pending sales, which were down once again last month for a total decrease of 14.3% over the last 4 months. Some regional data are also reporting lower resales. Existing home sales are forecast to hit 5,800,000 units.

THURSDAY April 21 - 10:00

March	m/m
Consensus	0.3%
Desjardins	0.4%
February	**0.3%**

Leading indicator (March) – After dipping 0.5% in January, its first decline since the early months of the pandemic, the leading indicator advanced 0.3% in February. A slightly higher increase is expected for March. The main contributor will be the drop in jobless claims. The interest rate gap as well as hours worked will also contribute positively but be offset in large part by the other indicators, especially consumer confidence. All things considered, the leading indicator should be up 0.4%.

CANADA

TUESDAY April 19 - 8:30

March	
Consensus	250,000
Desjardins	243,000
February	**247,300**

Canadian housing starts (March) – Housing starts are expected to give back some of their February advance, as activity settles around a more typical, albeit still elevated, pace in March. With income growth remaining solid, the market for existing homes tight, and permitting activity near record levels, it is really only rising interest rates that could act against activity at this point. And while the federal government also put additional resources on the table in Budget 2022, this is not expected to show up in the data for several month to come.

TUESDAY April 19 - 8:30

March	m/m
Consensus	n/a
Desjardins	-4.4%
February	**4.6%**

Canadian existing home sales (March) – Existing home sales in Canada are expected to give back much of February's advance in March, as buyers began to show concern over higher prices and rising interest rates. Indeed, the Toronto Regional Real Estate Board showed a substantial drop in seasonally-adjusted transactions in March while sales activities in other major Canadian cities were more mixed. As a result, we expect existing home sales in Canada to decrease by 4.4% m/m in March 2022, to about 55,600 units.

WEDNESDAY April 20 - 8:30	
March	**m/m**
Consensus	1.0%
Desjardins	0.9%
February	**1.0%**

Consumer price index (March) – Inflation likely hit its highest level in 30 years in March, but that should represent a peak. Surging global energy prices following Russia's invasion of Ukraine pushed domestic costs materially higher during the month. Food prices were also boosted by the conflict. That will result in a 0.9% month-over-month increase in headline prices, leaving the annual pace of inflation tracking 6.1%. A strong increase in core prices was likely the result of persistent supply chain disruptions and a surge in demand for services as the economy continued to reopen after the Omicron wave. The 4.0% core inflation print that we have penciled in would match the highest reading since the early 2000s. Looking ahead, however, with inflation calculations starting to lap strong year ago levels, the annual rate of headline inflation should begin to decelerate. Along with some aggressive tightening in monetary conditions by the Bank of Canada, the April data should be the first sign that inflation is beginning a long journey back down to the 2% target.

FRIDAY April 22 - 8:30	
February	**m/m**
Consensus	-0.2%
Desjardins	-0.4%
January	**3.2%**

Canadian retail sales (February) – Despite seasonally-adjusted gasoline prices pushing the overall cost of retail goods higher, retail sales are expected to post a modest contraction in February after a substantial advance in the prior month. The total volume of retail sales activity is expected to have dipped meaningfully in February as Canadians opted to venture back out to restaurant and bars as they reopened from Omicron lockdowns as opposed to ordering goods online. Further, a decline in new auto sales back to late 2021 levels took a bit of the shine off of January's bounce.

OVERSEAS

SUNDAY April 17 - 22:00	
Q1 2022	**y/y**
Consensus	4.2%
Q4 2021	**4.0%**

China: real GDP (Q1) – The annual variation in China's real GDP continued to slow at the end of 2021 to reach 4%. Still, this was hiding the quarterly variation's surprising growth (+1.6%, the most in a year). The data released for the first quarter of 2022 up to and including February were rather good, with the annual variations in retail sales and industrial output up sharply. That said, the latest lockdowns, especially in Shanghai, due to the rise in the number of COVID-19 cases and the Chinese authorities' strict policy in this regard probably weighed heavily on economic activity in March. The first hint of this was the drop in the PMI indexes last month. The data to be released on Sunday evening will provide more insight.

FRIDAY April 22 - 4:00	
January	
Consensus	53.9
January	**54.9**

Eurozone: PMI index (April – preliminary) – While the confidence of European households clearly deteriorated in March in response to the war in Ukraine and higher energy prices, the PMI indexes remained rather resilient. The Euroland composite index went from 55.5 to 54.9, which is still in line with fairly solid economic growth in the eurozone. April's data will tell us whether business conditions are still looking good or if cracks are starting to show.

Economic Indicators

Week of April 18 to 22, 2022

Day	Hour	Indicator	Period	Consensus	Desjardins forecast	Previous data
UNITED STATES						
MONDAY 18	10:00	NAHB housing market index	April	77	n/a	79
	16:00	Speech of the Federal Reserve Bank of St. Louis President, J. Bullard				
TUESDAY 19	8:30	Housing starts (ann. rate)	March	1,748,000	1,800,000	1,769,000
	8:30	Building permits (ann. rate)	March	1,839,000	1,850,000	1,865,000
	12:05	Speech of the Federal Reserve Bank of Chicago President, C. Evans				
WEDNESDAY 20	10:00	Existing home sales (ann. rate)	March	5,800,000	5,800,000	6,020,000
	10:30	Speech of the Federal Reserve Bank of San Francisco President, M. Daly				
	11:30	Speech of the Federal Reserve Bank of Chicago President, C. Evans				
	14:00	Release of the *Beige Book*				
THURSDAY 21	8:30	Initial unemployment claims	April 11-15	n/a	182,000	185,000
	8:30	Philadelphia Fed index	April	21,0	17.0	27.4
	10:00	Leading indicator (m/m)	March	0.3%	0.4%	0.3%
FRIDAY 22	---	---				

Day	Hour	Indicator	Period	Consensus	Desjardins forecast	Previous data
CANADA						
MONDAY 18	---	---				
TUESDAY 19	8:15	Housing starts (ann. rate)	March	250,000	243,000	247,300
	8:30	International transactions in securities ($B)	Feb.	n/a	n/a	13.49
	9:00	Existing home sales	March	n/a	-4.4%	4.6%
WEDNESDAY 20	8:30	Consumer price index				
		Total (m/m)	March	1.0%	0.9%	1.0%
		Total (y/y)	March	6.2%	6.1%	5.7%
THURSDAY 21	---	---				
FRIDAY 22	8:30	Industrial product price index (m/m)	March	n/a	2.1%	3.1%
	8:30	Raw materials price index (m/m)	March	n/a	7.6%	6.0%
	8:30	Retail sales				
		Total (m/m)	Feb.	-0.2%	-0.4%	3.2%
		Excluding automobiles (m/m)	Feb.	0.5%	-0.1%	2.5%

NOTE: Desjardins, Economic Studies are involved every week 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 monthly, quarterly and yearly variation respectively. Following the quarter, the abbreviations f, s and t correspond to first estimate, second estimate and third estimate respectively. The times shown are Eastern Standard Time (GMT - 4 hours). Forecast of Desjardins, Economic Studies of the Desjardins Group.

Economic Indicators

Week of April 18 to 22, 2022

Country	Hour	Indicator	Period	Consensus m/m (q/q)	Consensus y/y	Previous data m/m (q/q)	Previous data y/y
OVERSEAS							
SUNDAY 17							
China	22:00	Real GDP	Q1	0.7%	4.2%	1.6%	4.0%
China	22:00	Industrial production	March		4.0%		4.3%
China	22:00	Retail sales	March		-3.0%		1.7%
MONDAY 18							
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TUESDAY 19							
Japan	0:30	Industrial production – final	Feb.	n/a	n/a	0.1%	0.2%
Japan	19:50	Trade balance (¥B)	March	-495.1		-1,031	
WEDNESDAY 20							
Germany	2:00	Producer price index	March	2.7%	30.0%	1.4%	25.9%
Italy	4:00	Trade balance (€M)	Feb.	n/a		-5,052	
Euro zone	5:00	Trade balance (€B)	Feb.	n/a		-7.7	
Euro zone	5:00	Industrial production	Feb.	0.2%	1.0%	0.0%	-1.3%
THURSDAY 21							
France	2:45	Business confidence	April	105		107	
France	2:45	Production outlook	April	-6		-2	
Euro zone	5:00	Construction	Feb.	n/a	n/a	3.9%	4.1%
Euro zone	5:00	Consumer price index – final	March	2.5%	5.9%	2.5%	5.9%
Euro zone	10:00	Consumer confidence – preliminary	April	-20.0		-18.7	
United Kingdom	19:01	Consumer confidence	April	-33		-31	
Japan	19:30	Consumer price index	March		1.2%		0.9%
Japan	20:30	PMI composite index – preliminary	April	n/a		50.3	
Japan	20:30	PMI manufacturing index – preliminary	April	n/a		54.1	
Japan	20:30	PMI services index – preliminary	April	n/a		49.4	
FRIDAY 22							
United Kingdom	2:00	Retail sales	March	-0.2%	2.9%	-0.3%	7.0%
France	3:15	PMI composite index – preliminary	April	55.0		56.3	
France	3:15	PMI manufacturing index – preliminary	April	53.0		54.7	
France	3:15	PMI services index – preliminary	April	56.5		57.4	
Germany	3:30	PMI composite index – preliminary	April	54.1		55.1	
Germany	3:30	PMI manufacturing index – preliminary	April	54.5		56.9	
Germany	3:30	PMI services index – preliminary	April	55.5		56.1	
Euro zone	4:00	Current account (€B)	Feb.	n/a		22.6	
Euro zone	4:00	PMI composite index – preliminary	April	53.9		54.9	
Euro zone	4:00	PMI manufacturing index – preliminary	April	54.6		56.5	
Euro zone	4:00	PMI services index – preliminary	April	55.0		55.6	
United Kingdom	4:30	PMI composite index – preliminary	April	58.8		60.9	
United Kingdom	4:30	PMI manufacturing index – preliminary	April	54.0		55.2	
United Kingdom	4:30	PMI services index – preliminary	April	60.0		62.6	

NOTE: In contrast to the situation in Canada and the United States, disclosure of overseas economic fi gures is much more approximate. The day of publication is therefore shown for information purposes only. The abbreviations m/m, q/q and y/y correspond to monthly, quarterly and yearly variation respectively. The times shown are Eastern Standard Time (GMT - 4 hours).