RESEARCH BRIEF
CANADA HOUSING MARKET

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Canada's Housing Market May Be Entering a New Stage of its Cyclical Downturn

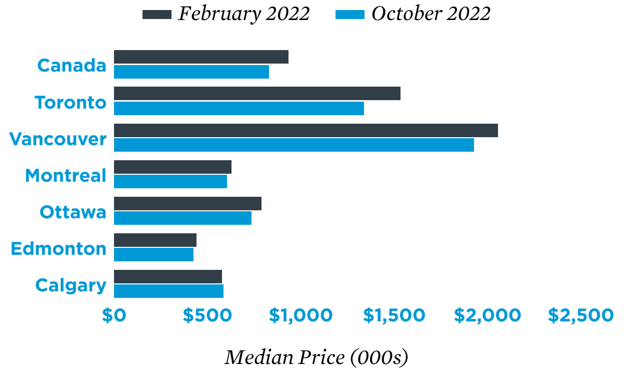
Housing market slowdown beginning to moderate. Home prices are down roughly 10 per cent from the peak witnessed in February, and the year-over-year change in prices turned negative for the first time in three years in October, declining by 1.9 per cent. Nonetheless, the 1.4 per cent month-over-month drop in housing prices during the most recent period was the smallest since March, creating a more optimistic outlook. Furthermore, existing home sales were up 1.3 per cent monthly in October, the first increase since interest rates began to rise, potentially suggesting that buyers and sellers are coming to terms with the new environment of elevated borrowing costs and slightly lower prices. While Canada's housing market is starting to show signs of an impending inflection point, elevated interest rates will likely keep market activity muted into early 2023. Price corrections, however, could be entering a more moderate period, suggesting Canada's housing market may begin to stabilize sooner than expected.

Mortgage rates could be nearing peak. This year, the Bank of Canada has raised its overnight rate by 350 basis points, translating into both fixed and variable rate mortgages nearing the 5.5-6.0 per cent range. Housing affordability, as a result, has become an even greater challenge for a growing share of Canadians. Nonetheless, with government bond yields beginning to decline, mortgage rates may be nearing their peak in the coming months. The transaction market, however, may not see a significant uptick in activity due to persistent affordability challenges. Price stabilization, on the other hand, is becoming a possibility due to limited supply, as well as buyers and sellers coming to terms with the new transaction environment.

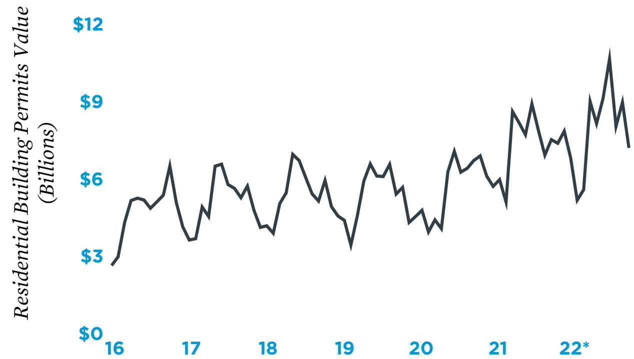
Long-term affordability likely to remain a challenge. While early signs are beginning to suggest that Canada's housing market slowdown may be easing, development continues to weaken. New home sales are down 91 per cent year-over-year, which is weaker than the depths witnessed at the onset of the pandemic, as well as the 2008/2009 financial crisis. This will likely translate into a sharp fall in building activity next year, as developers rely on pre-construction sales to fund projects. Furthermore, in the third quarter, the value of residential building permits issued for single-family homes was down 9.0 per cent, and multifamily was down 2.6 per cent when compared to the prior quarter. Supply, as a result, will likely be restricted further in the long term, hindering affordability to a greater extent in an already expensive market, while encouraging potential buyers to remain in the apartment rental sector.

Apartment rentals play a key role in providing relief. Rising borrowing costs and still elevated prices continue to keep potential homeowners on the sidelines. Apartments, in turn, act as an affordable housing solution for many Canadians. As a result, national vacancy is continuing to tighten, while rental rates grow due to robust demand and limited supply. Meanwhile, high interest rates are causing banks to tighten their lending requirements, in turn hindering development activity as the feasibility of new projects is being questioned. With ownership remaining a challenge, new rental supply is needed in order to provide relief to Canada's expensive housing market. Governments and developers will need to find creative ways to increase housing options nationwide, in order to balance supply and demand in both the ownership and rental markets.

Home Prices Down From Peak Across Country



Pipeline Softens Amid Rising Interest Rates



* Through September 2022

Sources: IPA Research Services; Altus Data Solutions; Bank of Canada; Canada Mortgage and Housing Corporation; Capital Economics; CoStar Group, Inc.; Statistics Canada