Housing and Mortgage Market Review

Rising inflation forces the Bank of Canada's hand

By Ben Rabidoux

Mortgage Professionals Canada is pleased to share the July issue of our monthly report on key market findings and analysis to help support Canada's mortgage broker channel.

We have partnered with analyst Ben Rabidoux, who each month provides MPC members with a review of the latest housing and economic data and rate trends. He breaks down what the data means and spells out the implications for Canadian consumers—your clients.

We look forward to arming our members with powerful insight into the housing and mortgage markets and hope you enjoy this latest report.

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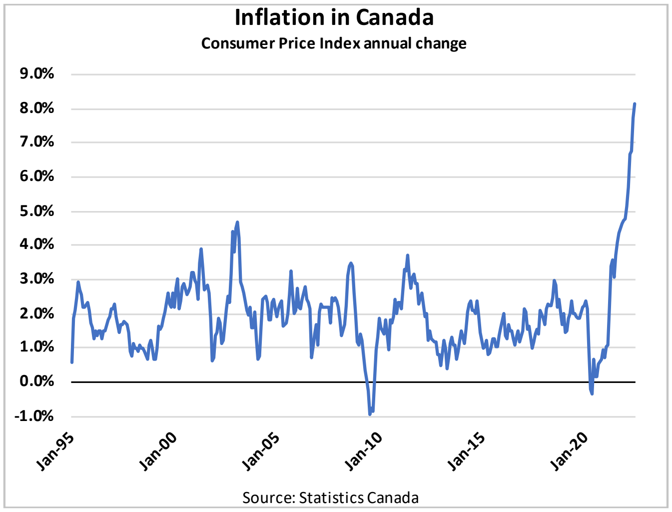
The Bank of Canada has taken their inflation fight to a new level, surprising markets with a 100-bps (1%) rate hike in July. It was the largest single hike since the 1990s.

The Bank is now recognizing that inflationary forces are stronger and more persistent than they previously anticipated. Headline CPI came in at 8.1% in June, the strongest such reading since early 1983!

But the bigger concern is that inflation expectations continue to rise. From the Bank's Monetary Policy Report:



> *Businesses and consumers increasingly think that inflation will be higher for longer, and they are more uncertain about the future path of inflation. This points to an increasing risk that elevated inflation will become entrenched.*
>
> *[...] Inflation expectations have a direct impact on inflation because they are factored in when firms set wages and prices.*

In other words, if people THINK inflation will be high, they will demand higher wages today. And with the unemployment rate at a record low of just 4.9% and with nearly one million job vacancies, employees have a lot of bargaining power.

Consumers and businesses are also more likely to spend more today if they think inflation will remain high. After all, who wants to pay 10% more next year when you can buy that gadget today. This extra demand creates the very inflation that consumers worry about in a self-reinforcing cycle.

This is why the Bank of Canada is in automatic tightening mode at the moment. They will continue to hike rates until two things happen:

- Inflation shows signs of moderating
- Expectations of future inflation begin to cool

In other words, they will hike until people are more fearful of recession than they are of inflation.

Canadian consumers are already getting fearful and pessimistic. The latest consumer confidence readings are near the lows seen in the early days of the pandemic.

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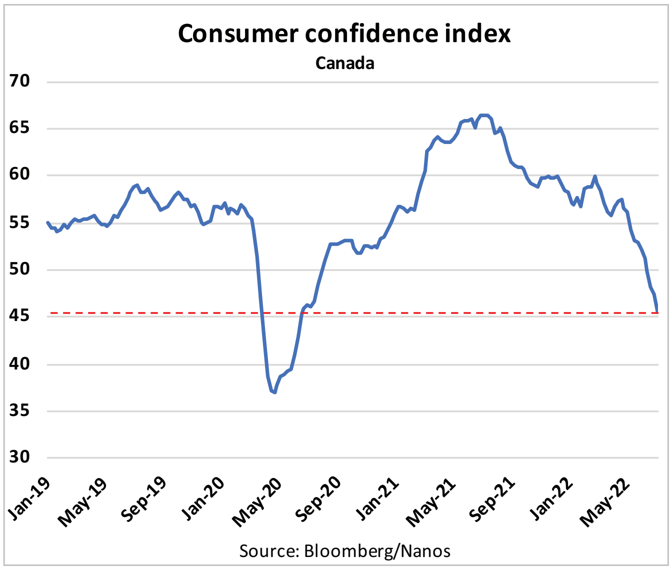
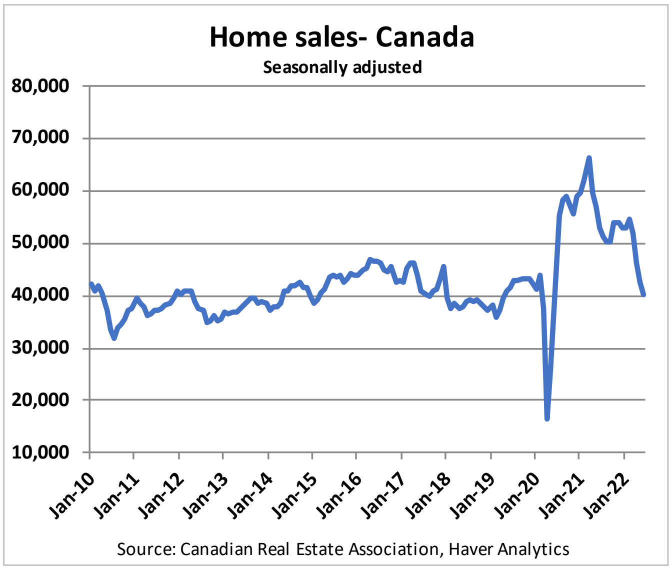
What it means: Coupled with the fact that key commodities like oil, natural gas, copper and other base metals have fallen sharply in recent weeks, we could be seeing early signs that inflation and inflation expectations are starting to roll over. And if that's the case, it suggests that the worst of this rate-hike cycle is perhaps already behind us.



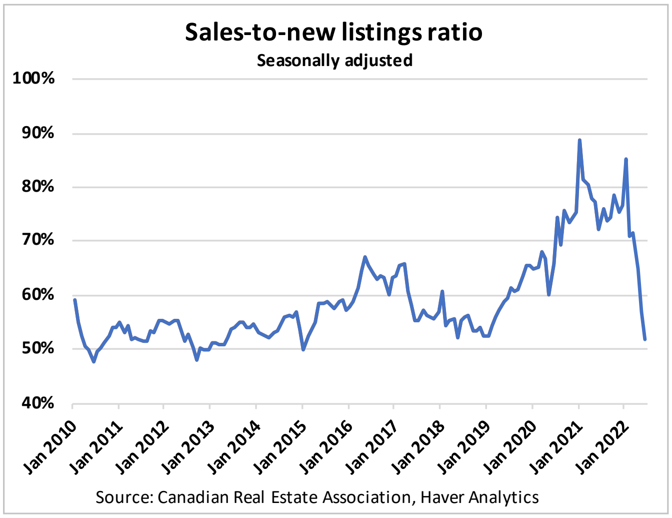


Home sales tumble as affordability worsens

Home sales nationally fell by 23.9% year-over-year in June and were down 5.6% month-over-month in seasonally adjusted terms, led by steep drops in B.C. (-10.2% m/m) and Ontario (-8.1% m/m).

The key metric to watch as we move through the summer is the flow of new listings coming to market. Prior cycles in 2009 and 2015 in B.C. and 2017 in Ontario all followed a general pattern of declining sales and prices, followed by a steep drop in new supply within six months, which ultimately helped stabilize the market.

While there are no signs of a wave of panic selling, **new listings did rise 4.1% m/m in June to build on a 4.7% increase in May. It was the highest level of new listings since Q1 2021**. Ontario saw an 11.1% m/m increase in new listings. That's not a good sign for those hoping for a 2017-style rebound.



The market balance continues to deteriorate, with the sales-to-new listings ratio hitting lows last seen in 2015.

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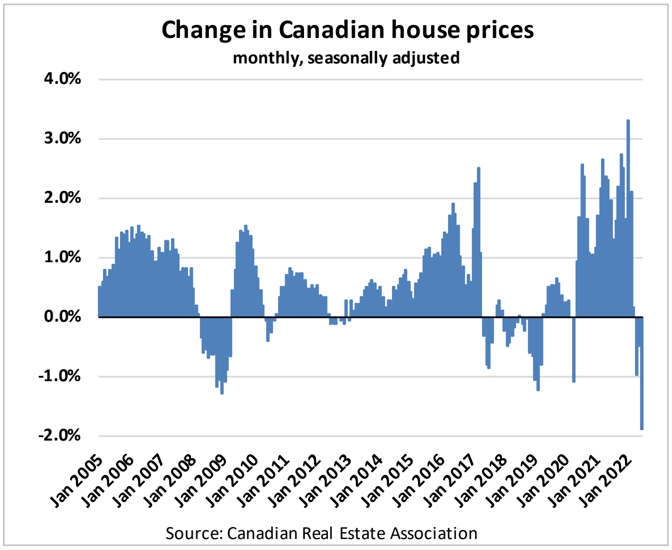
With new listings up and sales way down, active inventory continues to build—it was up another 7.1% last month in seasonally adjusted terms. This continues to be the fastest inventory build nationally since 2010.

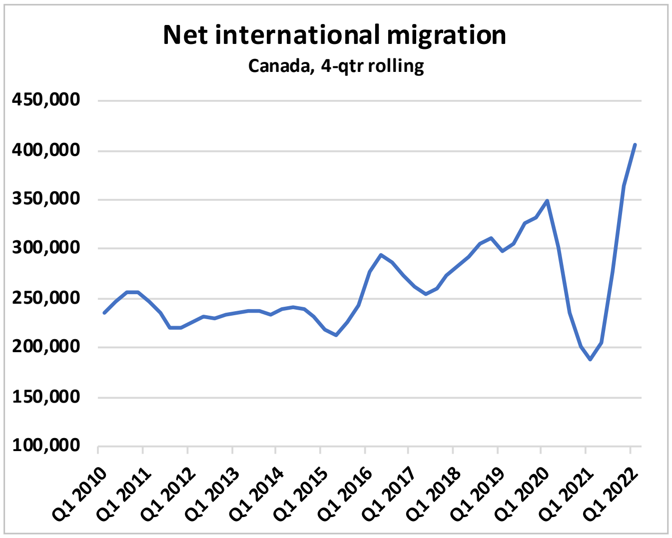
On the house price front, the MLS HPI posted the largest single monthly decline since at least 2005.

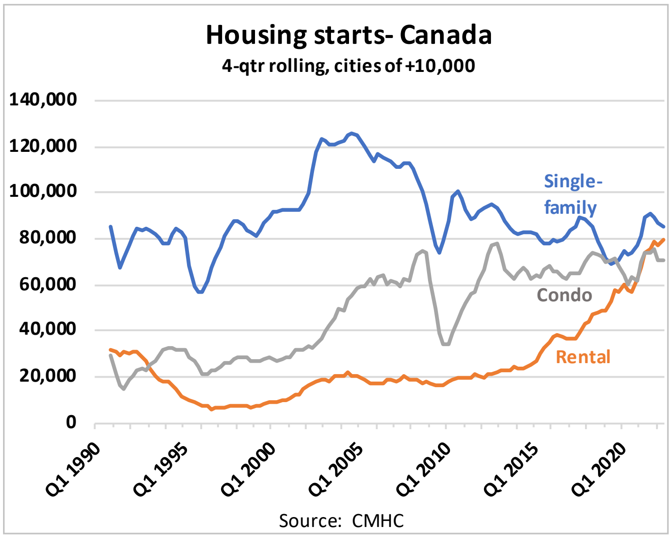


In the near term, rising rates and deteriorating affordability will continue to constrain demand until affordability is improved, either via falling rates or a further reduction in house prices.

Reason for optimism: Long-term supply/demand dynamics are still solid

In spite of a very challenging affordability picture in the near term, longer term fundamentals still look very positive. Canada's population grew by over 500,000 in the past year alone, bolstered by record immigration.





Meanwhile, single-family housing starts remain well below average levels over the past 20 years.

What it means: The impact of rising rates will likely slow market activity for some time, but strong supply/demand fundamentals will eventually put a floor under prices.

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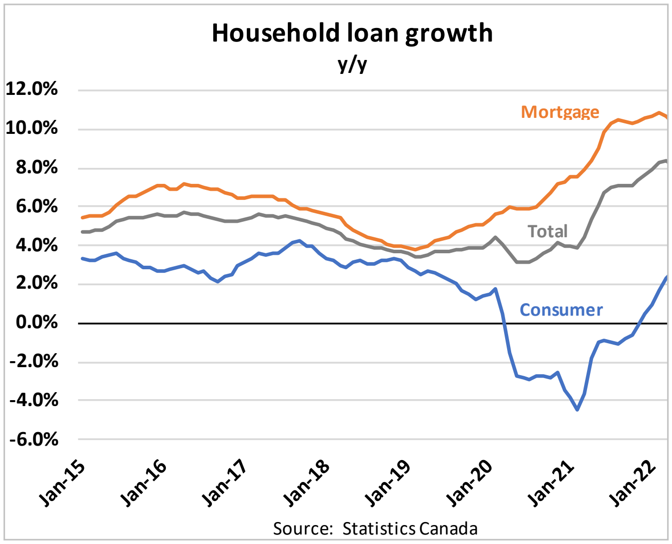
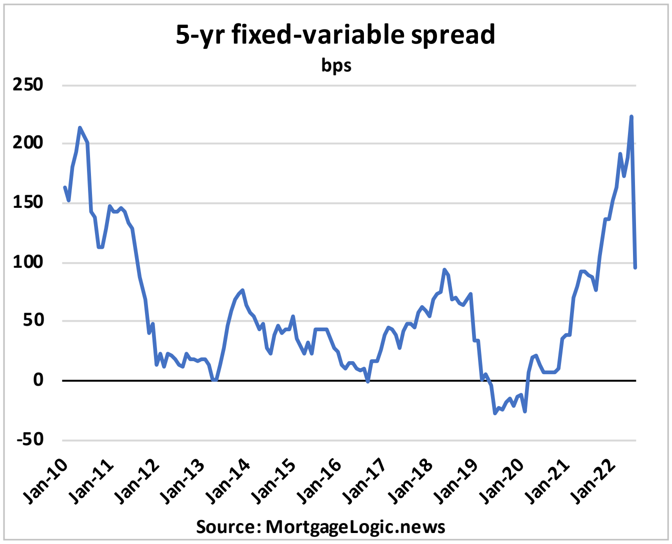
Mortgage market update: Big push into variable rates continues

After hitting a 14-year high earlier this year, mortgage growth is showing early signs of topping out. Growth has decelerated sharply in the past two months.

Borrowers continue to opt for variable-rate mortgages, which have accounted for 54% of new originations since the start of the year. In part, this is due to what has been a historically large gap between fixed and variable mortgage rates.

Last week's 100-bps rate hike from the Bank of Canada is helping to narrow that gap, but it still remains well above normal levels.





**Any forecasts contained in this report are accurate as of the date indicated.*

Ben Rabidoux is the founder of Edge Realty Analytics (www.edgeanalytics.ca), which equips top real estate and mortgage professionals with timely research and insightful marketing infographics to help them stand apart from the competition and stay engaged with their clients and prospects.

He is also the founder and president of North Cove Advisors, a market research firm serving institutional and high net worth clients since 2013 that is consistently ranked top 5 for Canadian economic coverage by Brendan Wood International.

He is a frequent guest and contributor in major media outlets, including Bloomberg, The Wall Street Journal, Reuters, The Globe and Mail, The Toronto Star, Macleans, and many others.