ECONOMIC VIEWPOINT

Desjardins Affordability Index:

Should You Jump into the Housing Market? And If So, When?

By Marc Desormeaux, Principal Economist

Highlights

- With interest rates falling and home prices expected to rise, some prospective buyers sense an opening after an exceptionally challenging period for affordability. Could the next few months be the right time for them to come off the sidelines?
- Based on our forecast, some prospective buyers may find opportunities in late 2024 and early 2025—with several caveats and additional considerations.
- Regardless, we remain of the view that Canadian housing affordability will improve but not return to pre-pandemic levels over the next 2+ years.
- That result holds under all four of the alternative forecast scenarios we explore in this note. These scenarios are: an extension of mortgage repayment timelines, changes to temporary migration policy, a pronounced spike in new listings and a recession.
- We expect regional differences to persist. Ontario and BC's particularly costly starting points mean that they'll likely remain the most prohibitively expensive markets, while Alberta should continue to stand out as relatively more affordable.

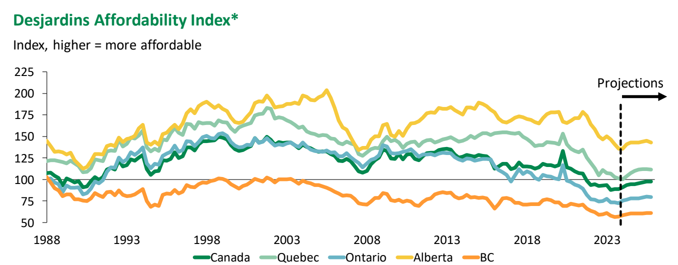
Introduction

It's been an exceptionally challenging period for Canadians seeking to purchase a home, and many have simply given up hope amid decades-high borrowing costs and still-lofty home values. But now, with interest rates falling and home prices expected to rise, some prospective buyers sense an opening. **Could the next few months be the right time for them to come off the sidelines?**

In this note, we update our projections for the Desjardins Affordability Index (DAI) with that question in mind. Of particular interest is how different drivers of affordability have interacted over time and could play out going forward. We also explore alternative scenarios for home prices and affordability, both to assess the potential impacts of recent policy announcements and to debunk some widely accepted myths.

The theme throughout is that while we still expect affordability to improve, it isn't likely to return to pre-pandemic levels within the next few years (graph 1).

Graph 1
A Return to Pre-pandemic Affordability Is Unlikely in the Next Two Years



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

NOTE TO READERS: The letters k, M and B are used in texts and tables to refer to thousands, millions and billions respectively.
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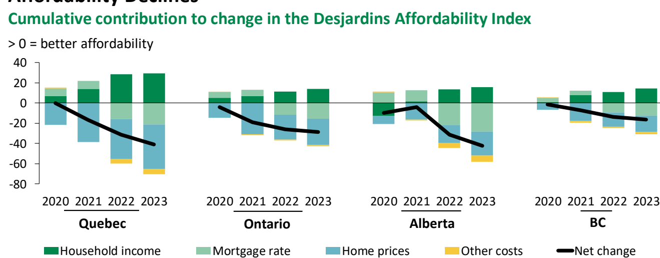
Affordability Should Improve, but Not to Pre-pandemic Levels

Our recent Desjardins Housing Outlook baked in a rebound in home sales and values in late 2024 and 2025 as interest rates come down. However, it assumed the pace of price gains would be weaker than during the pandemic and the hotter quarters during 2015–19.

We remain of the view that affordability will improve but not return to pre-pandemic levels over the next 2+ years. That's partly because multiple drivers of affordability will sometimes work at cross purposes. Lower interest rates will reduce the cost of carrying mortgage debt, but they'll also put upward pressure on home values and by extension monthly mortgage payments. That's in contrast to the past two years, when price gains stalled or fell in most jurisdictions, but higher interest rates negatively contributed to overall affordability. We also don't expect rates to return to the rock-bottom levels seen at times during the past decade. Moreover, income growth will be muted in the coming quarters as the Canadian economy slows. For more information on DAI components and methodology, see this appendix.

We expect affordability in all four of the largest provinces to improve in the quarters ahead but remain worse than in 2015–19. That said, important regional differences should persist. Since the pandemic, affordability has deteriorated less in Ontario and BC than elsewhere in Canada (graph 2), but that's largely because they were already unaffordable and had less room to run. We think those jurisdictions' particularly costly starting points mean they'll remain the most prohibitively expensive. By contrast, the cost of homeownership should remain relatively low in Quebec and Alberta despite the more pronounced erosion of affordability there since late 2019.

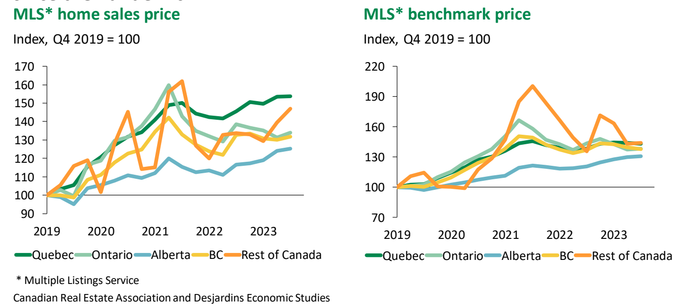
Graph 2
Of the 4 Large Provinces, Quebec and Alberta Have Seen the Biggest Affordability Declines
Cumulative contribution to change in the Desjardins Affordability Index



Statistics Canada, Canada Mortgage and Housing Corporation and Desjardins Economic Studies

Moreover, there are differences in trends and buying opportunities among the more affordable provinces. Quebec, for instance, has seen some of the strongest home price gains in Canada since the start of the pandemic—the primary reason for its recent affordability erosion. Smaller provinces have also seen larger-than-average home value gains (graph 3). As we noted in our coverage of the 2024 Quebec Budget, provincial tax and fee relief looks to have supported incomes, though it may have also stimulated housing demand. Alberta has also seen affordability worsen more recently. Following a double whammy of pandemic restrictions and plunging oil prices that hit its economy particularly hard, a strong recovery and torrid population gains have pushed home values significantly higher. Strikingly, Calgary home prices currently sit 10% above their prior peak in February 2022 and should continue to climb as borrowing costs come down.

Graph 3
Quebec and the Smaller Provinces Have Seen the Biggest Price Run-Ups since the Pandemic

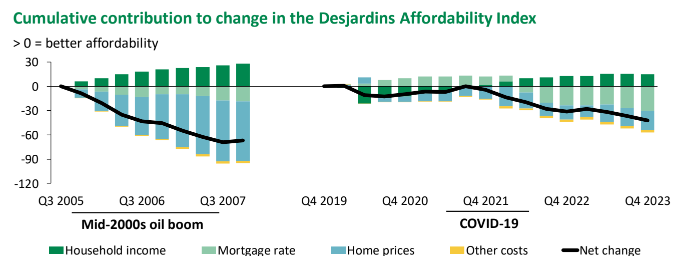


* Multiple Listings Service
Canadian Real Estate Association and Desjardins Economic Studies

Ultimately, from an overall affordability perspective, Alberta still stands out. It's the only one of the four large Canadian provinces whose DAI isn't at a record low. Moreover, its recent deterioration of affordability, while meaningful, hasn't been as severe or rapid as that experienced during the oil boom of 2005–07 that briefly lifted Calgary home prices above Toronto's (graph 4). Relatively strong economic prospects and

Graph 4
COVID-19 Wasn't the Biggest-Ever Hit to Alberta's Affordability

Cumulative contribution to change in the Desjardins Affordability Index



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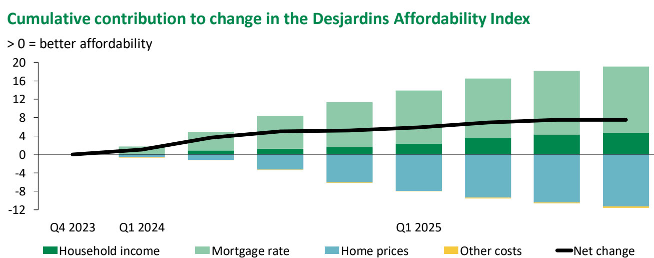
less acute land and supply constraints should continue to support the province's relative affordability.

Should You Jump In, and If So, When?

Any consideration of "timing the market" comes with caveats. The decision to purchase a home—for the first time, to move up or to downsize—is specific to the individual and should reflect their personal financial goals and risk tolerance. Our projections also don't explicitly incorporate sentiment effects that could occur if, say, rates drift lower in anticipation of future central bank rate cuts and drive outsized buyer exuberance. Moreover, the DAI uses the average sale price across all dwelling categories at the national and provincial levels. Opportunities may differ for apartments and detached homes, or between cities or neighbourhoods, for instance.

Based on our forecast, some prospective buyers may find opportunities to come off the sidelines in late 2024 or early 2025. By then, we anticipate that the national DAI will have risen by about five percentage points from current levels—about two-thirds of the affordability improvement expected by end-2025 (graph 5). And optimistically for those seeking to build housing wealth, our projections also include steady price gains beyond that point as rate cuts completed earlier increasingly work their way through the Canadian economy.

Graph 5
Rate Cuts Will Help Homeownership Affordability This Year



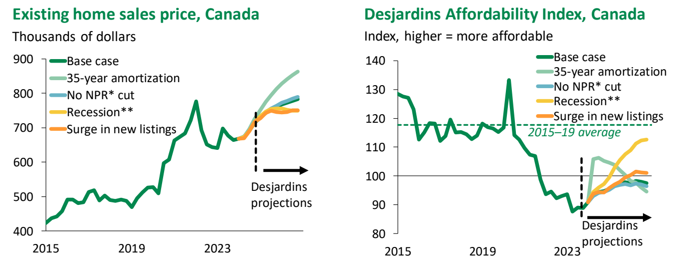
Statistics Canada, Canada Mortgage and Housing Corporation and Desjardins Economic Studies

Busting Myths about Housing Affordability in Canada

Of course, our forecast represents just one of many possible trajectories for the Canadian housing market, so in this note we also project home prices and affordability under four alternative scenarios. To do so, we use Desjardins's analytical framework of Canada's economy.

Our reasons for presenting these scenarios are twofold. First, all four alternative scenarios reinforce our headline view: in none does the DAI return to the 2015–19 average by the end of 2026 (graph 6). Perhaps more importantly, strong opinions about housing abound in Canada. Our hope here is to explore claims that may not be substantiated in a way that positively contributes to policy discussion.

Graph 6
Affordability Is Still Unlikely to Return to Pre-pandemic Levels during the Forecast Window



* Non-permanent resident ** Recession scenario based on 1980s and 1990s recessions plus the Global Financial Crisis
Canadian Real Estate Association and Desjardins Economic Studies

Our first scenario, which assumes mortgage terms increase to 35 years from the current industry standard of 25 years, sees affordability worsening versus the base case in just a few years. Extending the amortization period has been floated in some corners as a solution to Canada's housing crisis because—in isolation—it would reduce mortgage payments and lower the income threshold for loan qualification. However, it would also increase disposable income, which would increase housing demand. Our scenario shows that an immediate amortization adjustment would benefit those fortunate enough to be able to jump into the market right away. But affordability would eventually become even worse than in the base case as initial gains are overcome by a more dramatic rise in home values. To an extent, this could be a shortcoming in all purportedly affordability-improving measures that stoke demand. But this particular scenario also comes with the financial stability risks inherent in longer debt repayment periods.

Our second scenario assesses the impacts of Ottawa's plans to reduce the non-permanent resident (NPR) population by 25%–30% by the end of 2026. Again, we don't see affordability improving meaningfully in the long run under this scenario. For this exercise, we compared our base case DAI projections to a situation where population growth continues at the pace assumed before the announcement (with appropriate adjustments for temporary residents' labour market performance). Our base case affordability projection is slightly better than in the no-NPR cut scenario, but only slightly. That's because while weaker population growth does translate into weaker housing demand, we would also expect it to result in fewer new listings. Over time, it also limits our productive capacity and ultimately our efforts to bring more supply online. NPRs also tend to rent more than the broader Canadian population, so the policy's potential impact on home prices may be limited in any case.

Our third scenario looks at what would happen if listings spike in the months ahead. This is a highly unlikely trajectory: the number of properties for sale rises even more than under the recession scenario. But it could conceivably occur if financially strapped borrowers decide to liquidate their assets amid signs of stronger buyer activity, or if retiring baby boomers decide to shift towards rental accommodation en masse. Assuming per capita listings evolve through 2026 at a pace consistent with the spikes seen during the early 1990s recession and the early 2000s surge does indeed put downward pressure on prices and improve affordability. But our analytical framework doesn't suggest the DAI would get anywhere near its pre-pandemic level.

Our final scenario envisions a recession consistent with the 1980s and 1990s downturns and Global Financial Crisis. Again, it doesn't have the DAI returning to its 2015–19 average by 2026. Ultimately, while economic downturns do usually result in meaningful home value depreciation, they also tend to bring interest rate cuts, the stimulative effects of which mitigate price declines. They also come with layoffs and losses in the income being used to purchase a home. Our recession scenario puts household disposable income more than $20B lower than under our base case by 2025. With that in mind, those hoping for a recession should not only be weighing their homebuying ambitions against immense longer-term economic and social costs; they should also be thinking about how much more affordable a home would actually be for them if their financial situation changed.

Final Thoughts

The last 2+ years have been exceptionally trying for many Canadians seeking to purchase a home. The good news is that we see some relief in the quarters ahead as interest rate cuts reduce the cost of carrying mortgage debt. The bad news is that affordability isn't likely to return to pre-pandemic levels anytime soon. With that in mind, those looking for buying opportunities should (as always) consider the interplay between rates and home prices, as well as relative value propositions in all parts of the country.

Our final message is to policymakers. Our scenario analysis makes the case that there are no quick fixes to Canada's housing affordability crisis, and increasing housing supply is the only sustainable long-run solution. Last year, Desjardins Economic Studies published a guide for doing so. Optimistically, some of the recommendations have since been implemented. But there is more for all levels of government to do. Now is not the time for partisan attacks or blame, but to meet the challenge head-on with multi-year, all-hands-on-deck efforts.