Financial Post – November 21, 2024

Bank of Canada rate cuts rescued housing market from 'implosion,' says CoStar economist

Canada's economy is expected grow by 1.4 per cent next year

Jordan Gowling || November 21, 2024

A "sold" sign in front of newly built homes in Vaughan, Ont. on Nov. 7, 2023. PHOTO BY COLE BURSTON/BLOOMBERG

The Bank of Canada's recent interest rate cuts may have saved the housing market from collapse, but they won't be enough to restore previous levels of activity, the chief economist of real estate analytics giant CoStar Group Inc. said this week.

“I think the housing market just chugs along, basically the rate cuts are rescuing it from implosion, but it’s not necessarily going to take off again,” Carl Gomez said in an interview with the Financial Post on Wednesday. “If you look where mortgage rates are today, they’ve come down a little bit but not a heck of a lot and they’re certainly not going back to the lows they were over the last decade. So the housing market will get revived but it’s not going to blow up again like it did before.”

Gomez added that most of the mortgages and debt that people use to buy real estate is priced off of bond yields, which are dictated by the market, not the Bank of Canada. U.S. bond yields, which influence Canadian bond yields, went up following the re-election of Donald Trump, as it signalled a pick-up in economic activity and inflationary spending, reigniting market concerns around inflation. The Bank of Canada policy rate currently sits at 3.75 per cent, after four consecutive cuts this year.

“The Government of Canada 10-year bond yields — a benchmark proxy for longer term bond yields — has stayed around three and half per cent,” he said. “Which means that even though the Bank of Canada has been cutting interest rates, the long term bond yields that determine the market have remained around that three per cent.”

CoStar Group, a real estate company that provides marketing services and analytics for property markets, released its 2025 outlook for Canada on Wednesday. The forecast highlighted Canada’s weakened economy, which is currently growing well below its potential output.

“When we adjust GDP growth by population, unfortunately, we have been in a recession for almost two years now,” Gomez said during a webinar presentation. “If you look at per capita GDP growth adjusted for population growth — the outsized population growth since about 2023 — we’ve been declining.”

Gomez says Canada’s economy is expected grow by 1.4 per cent next year, but there remains two major risks to that outlook that could shave off a full percentage point from growth over the next two years: potential trade disruptions from U.S. President Donald Trump and Canada’s recently announced cuts to its immigration targets, which means negative population growth.

Additionally, Gomez noted households remain in a “bunker” mentality, so a rebound in consumption next year is uncertain. While the mortgage renewal cycle has moved off the previous “cliff” warnings as the central bank cuts rates, it should remain a factored-in risk going into next year, according to Gomez.

“Consumer spending is 60 to 70 per cent of the economy,” Gomez said. “So there is still going to be an impact there, even as rates move down and we move away from a cliff.”

Another important factor to watch going into next year will be the labour market. The forecast notes mortgage arrears and unemployment are heavily correlated and higher job losses could impact the number of households that are unable to make their monthly mortgage payments.

Looking to inflation, the CoStar forecast reports Canada has entered a deflationary period, with the inflation rate closer to 0.85 per cent when shelter prices are stripped away from the consumer price index. Gomez thinks the Bank of Canada should continue to cut and cut fast, back to a neutral rate of around 2.5 per cent.

“If anything, with inflation at target, the policy rate should be more at a neutral level,” said Gomez. “That’s why I still think there is an onus for them to be cutting, and they probably should be front-loading their cuts right now, for risk of what could happen to the economy if you fall behind the curve.”