Canadian Housing Outlook

Canadian housing – countdown to liftoff

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The tale of the Canadian housing market in 2025 is a tale of two markets. The low-rise segment will be the first to respond to lower mortgage rates, with still historically low inventories translating increased demand into higher home price inflation. The high-rise segment has been in recessionary territory for the past few quarters and is likely to remain under water for most of 2025, as record-high completions will continue to chase reduced investors' appetite. That should put continued downward pressure on resale condo prices in the coming year, while slower population growth and affordability erosion suggest that we have already reached peak rent inflation.

However, buyers' market conditions will not last for long. By mid-2026, a lack of supply due to the current drought in the condo pre-sale space and an extremely slow increase in purpose built activity will clash with increased demand due to lower interest rates and recent changes to mortgage regulations, resulting in higher price pressures.

Population growth will surprise on the upside in 2025

On October 24, 2024, in an unprecedented move, Canada's Immigration Minister announced targets for the arrival of both temporary and permanent residents for 2025 through 2027. With 96%+ population growth the result of international migration, the Immigration Minister is essentially attempting to manage the population, and is projecting a dramatic shift in Canada's population growth, from an increase of one million, to a decline of 82,000 in one year. A drop of 0.2%.

Targets were reduced for all sub-categories of newcomers including permanent residents, humanitarian and compassionate visas (H&C), refugees, and protected persons receiving permanent residency, as well as foreign workers and students. To achieve these population reductions, the government anticipates reducing new visa issuances to temporary arrivals along with transitioning temporary residents to permanent residency. That is expected to reduce the net number of temporary residents by about 446,000 in 2025 and again in 2026. While this is clearly a step in the right direction towards easing the pressure on the rental market, we doubt that those aggressive targets of de-facto decline in the population in both 2025 and 2026 are achievable.

First, the reality is that the temporary resident population is still rising, and a higher temporary population than expected in 2024 would require even more departures than forecast in 2025 and future years to secure the targeted lower population.

Second, actual arrivals will likely be higher than projected in the government announcement because of elements that the government cannot control – asylum seekers and H&C temporary visa holders. Asylum claims, which are additive to permanent resident visa issuances, are rising fast. Asylum visas to August 2024 were 119,835 year-to-date, up 48.4% from the same period in 2023. Work permit issuances on H&C grounds to August 2024 amounted to 127,920, up 52.6% from the same period in 2023. Appeals by MPs from all parties, provincial legislators, the refugee legal community, and media make H&C cases difficult to ignore.

Furthermore, the reduction in permanent resident visa issuances in 2025 will inevitably place more pressure on asylum and H&C claims, not less. With the share of permanent residents drawn from NPRs living in Canada already high (40%+), it is not credible to suggest that more permanent resident applications from non-permanents residents can achieve status.

The government appears to have assumed that expired visa holders, most of whom aspire for permanent residency but have little prospect of obtaining a permanent visa, will all return to their home country. We doubt that will happen. Consequently, reduced new visa issuances will almost certainly not translate into comparable declines in population. Simply put, the government currently lacks the regulations, processes, and capacity to enforce departures.

As a result, the newly announced policies will likely dramatically add to the estimated 600,000 expired visa holders in Canada without status. We suggest that actual net departures will be close to half the 446,000 assumed currently by the government.

With fewer students and workers arriving, but with higher asylum and H&C claimants, along with an assumed slower rate of departures than projected by the government, our assessment is that the population will likely rise by around 1% in 2025, and again in 2026, down from the current 3% annual pace as of July 1 (Chart 1). This would still translate into a 200K increase in demand for housing units (mostly in the rental space), relative to the slight decline currently projected by policymakers.

The rental market—reaching peak inflation

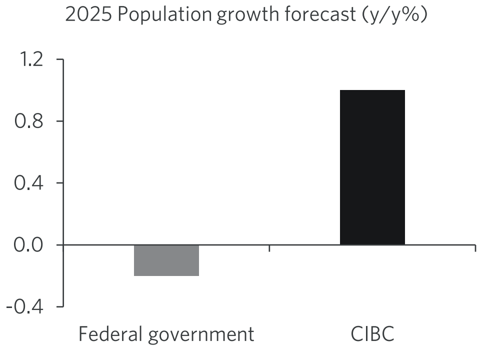
Still, curbing international migration is the right policy at the moment. The linkage between migration and housing costs is clear (Chart 2). There are already early signs of a stabilization in the market due to affordability erosion, with the current growth in asking rates already in negative territory on a year-over-year basis, foreshadowing a further slowdown in the CPI rent measure that is running at 7% y/y. Look for asking rent inflation to enter deeper into negative territory in the coming year as demographic factors take full effect.

Looking beyond the rental market, the downward trajectory in mortgage rates will see a pickup in housing market activity in 2025, but that will largely be a reflection of higher activity in the low-rise segment of the market. Inventories of low-rise units are tight, reflecting the drop off in homebuilding seen during the Bank of Canada's tightening cycle, and that's only now starting to reverse (Chart 3). However, construction in the multi-family space is showing growing signs of fatigue, with the drop in pre-construction sales feeding through to activity with a lag.

Higher mortgage rates, and a significant price gap between new and existing condos have kept investors out of the new construction market. And although the cost of borrowing is retreating, rental rates are starting to do the same, weighing on investor sentiment and resulting in a surge in completed condo units that have been unabsorbed by the market. That's in stark contrast to tighter conditions being seen in the low-rise segment (Chart 4).

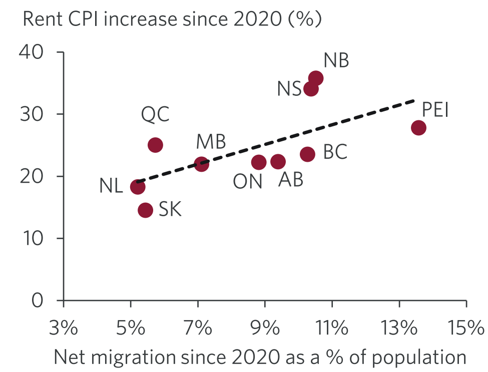
Ontario and BC are clearly the most exposed markets to the slowdown in condo investment, with investors accounting for 70% of buyers in the GTA. And the damage is on full display in the sales-to-new listings ratio, with Toronto and Vancouver being the only major centers across Canada where the market is in buyers' territory, as supply has flooded the condo market (Chart 5).

Chart 1: Canada's population unlikely to decline as government suggests



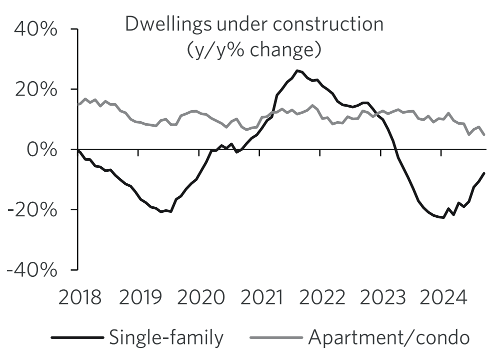
Source: Gov. of Canada, CIBC.

Chart 2: Migration closely linked to higher rental rates



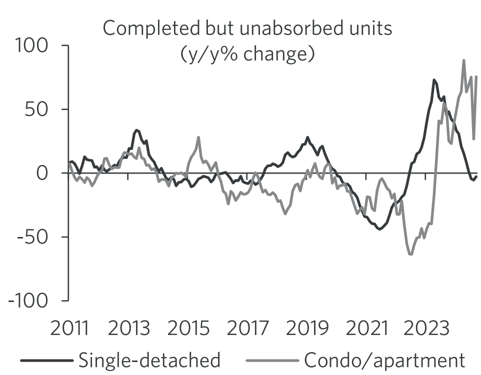
Source: StatCan, CIBC.

Chart 3: Building in low-rise market perking up, opposite for condo space



Source: CMHC, CIBC.

Chart 4: Newly completed condos being left vacant



Source: CMHC, CIBC.

For condo investment to regain its appeal, we have to wait for resale prices to rise, and interest rates to decline more significantly. The current price gap between new and resale condo prices remains near a record high at roughly 60%, and a full 20-percentage points above its long-run average.

The increase in condo inventories and drop in demand will limit the acceleration seen in housing starts in the coming year. We expect housing starts to average 263K (+7% y/y) in 2025 following a modest 2% increase in 2024. That increase will be driven entirely by single-family building, masking weakness in multi-unit starts.

Simply put, the resale condo market is a buyers' market and will remain so during the course of 2025. At one point however, the market will clear. Pent up demand fueled by falling mortgage rates will entice end-users and investors back to the market. But that newly found demand will be met with a severe lack of supply given that current pre-sale activity (future supply) is at a multi-decade low. That market dis-equilibrium will be on full display in 2026 or 2027 and might result in a significant upward pressure on condo prices.

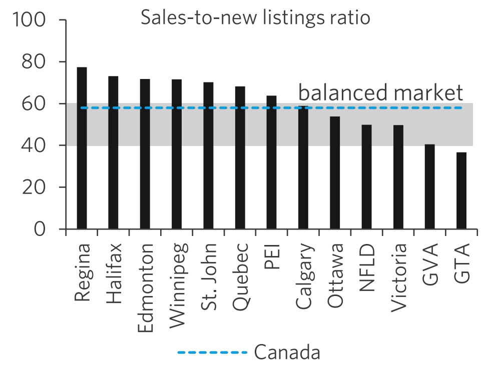
In the resale market, with mortgage rates falling, housing markets across the country are showing signs of stabilizing and turning around in some cases. That's more apparent in cities with better affordability and where condo investment isn't a large share of the housing market, which are now seeing home prices increase (Chart 6). In the overvalued Toronto market, prices are the weakest in the country, reflecting the surge in new listings tied to the condo market.

While 5-year mortgage rates have declined significantly, interest rates are still relatively high and potential buyers are likely listening to the Bank of Canada and waiting for further interest rate relief to offset still elevated home prices before getting into the market. That's reflected in still subdued sales volumes and below par growth in mortgage originations, where the 3-month average annual pace is sitting 6% below year-ago levels (Chart 7). We expect resale activity to rise by 12% in 2025 following a 8% increase in 2024. That will translate into an acceleration in originations, which we expect to rise by 14% next year.

Mortgage payment shock: a micro not a macro story

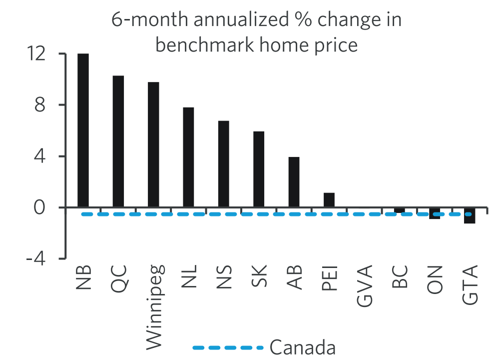
One of the most anticipated events in the mortgage market in 2025 is the repricing of a high volume of mortgages and the potential negative macro impact of the expected mortgage payment shock. A deep dive into the data suggests that fear is overblown. No less than 40% of mortgage volumes that are due to be repriced in 2025 will see de facto lower monthly payments and an additional 10% will see an increase of less than 10% (Chart 8, left). Sure, that leaves 50% of mortgages to be renewed facing an average 20% payment shock, but that doesn't look so scary if you consider the fact that over the past 5 years, both wages and home prices have risen by more than 30%. Overall, from a macro perspective we estimate that the total payment shock in 2025 (including mortgages that face lower payments) will average only 2.5% (Chart 8, right), suggesting that the focus should be on the micro space in terms of the potential increase in delinquency rates.

Chart 5: Toronto and Vancouver markets are the weakest in the country



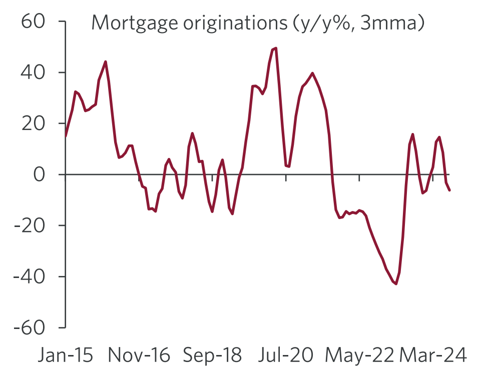
Source: CREA, CIBC.

Chart 6: Home prices turning around in many areas



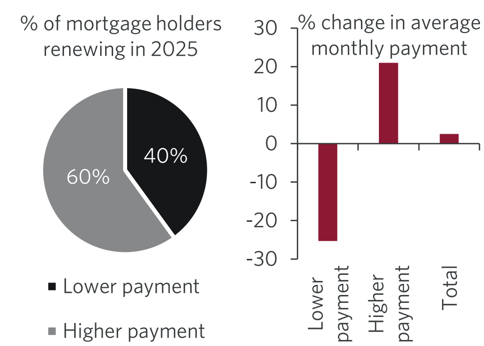
Source: CREA, CIBC.

Chart 7: Mortgage demand still sluggish



Source: StatCan, CIBC.

Chart 8: 40% of mortgage renewals will face lower payments next year (l), leading to only a modest aggregate increase (r)



Source: CIBC.