

# HOUSING MARKET OUTLOOK

## Sherbrooke CMA



CANADA MORTGAGE AND HOUSING CORPORATION

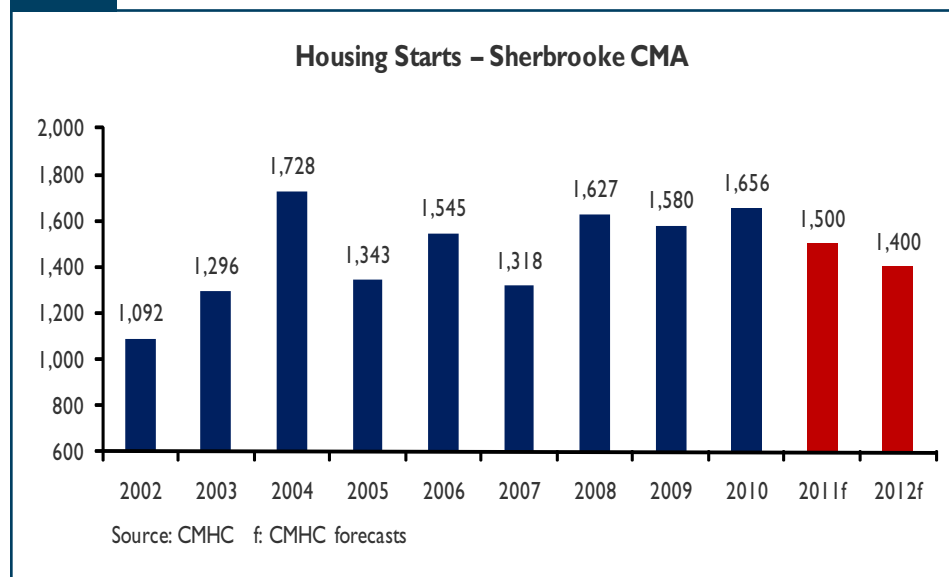
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### New phase in the Sherbrooke housing market<sup>1</sup>

Anticipating an increase in mortgage rates, a number of Sherbrooke households likely moved up their home purchases into 2010. Homeowner and condominium housing starts reached an all-time high last year in the Sherbrooke census

metropolitan area (CMA). However, these earlier-than-planned home purchases resulted in a decrease in the pool of potential buyers for 2011. Therefore, housing starts will drop by 9 per cent this year. MLS® existing home sales, for their part, will grow slightly (+2 per cent), as the slowdown in activity on the resale market began sooner than on the new home market in 2010. It should be mentioned that employment growth in the area over

Figure 1



<sup>1</sup> The forecasts included in this document are based on information available as of April 28, 2011.

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the next two years will help boost the real estate market.

## Employment to increase in 2011

In 2010, the Sherbrooke CMA<sup>2</sup> had 92,600 jobs, down 4 per cent from the same period in 2009. Most of the job losses occurred at the beginning of 2010, and the Sherbrooke labour market has been improving ever since. In the first quarter of 2011, employment had even surpassed pre-recession levels.

Thanks to improving economic conditions, employment growth in the Sherbrooke area will be in the 6-per-cent range this year (98,000 jobs). This may seem high at first glance, but it should be taken into account that the labour market contracted significantly last year before rebounding. Several roadwork projects are also expected in the Estrie area this year, which should continue to stimulate the local economy. In 2012, employment in the Sherbrooke CMA will reach 99,500 jobs, up 1.5 per cent from 2011. The vigorous job market will therefore be a factor that will stimulate demand on the housing market in the CMA next year.

## Mortgage rates

On April 12th, the Bank of Canada announced that it was leaving the Target for the Overnight Rate unchanged at 1.0 per cent. The last increase in the overnight rate occurred on September 8, 2010 when

the Bank of Canada raised it by 25 basis points. The Bank of Canada is expected to resume raising the overnight rate in the fourth quarter of 2011. Mortgage rates, particularly short term mortgage rates and variable mortgage rates, are expected to remain at historically low levels.

According to CMHC's base case scenario, posted mortgage rates will remain relatively flat in 2011 before increasing moderately in 2012. For 2011, the one-year posted mortgage rate is assumed to be in the 3.1 to 3.5 per cent range, while three and five-year posted mortgage rates are forecast to be in the 4.1 to 5.6 per cent range. For 2012, the one-year posted mortgage rate is assumed to be in the 3.4 to 4.3 per cent range, while three and five-year posted mortgage rates are forecast to be in the 4.2 to 6.3 per cent range.

Rates could, however, increase at a faster pace if the economy ends up recovering more quickly than presently anticipated. Conversely, rate increases could be more muted if the economic recovery is more modest in nature.

## Net migration to remain stable

In 2010, net migration in the Sherbrooke CMA reached an all-time high of 1,866 people. This high level was largely attributable to the record number of immigrants and also to Sherbrooke's appeal among residents from other areas of Quebec, despite a

contraction in employment.

Over the next few years, we expect these two migration components to remain stable. In fact, between 52,500 and 55,000 immigrants<sup>3</sup> will probably be admitted into Quebec in 2011. In the following years, about 50,000 immigrants<sup>4</sup> could settle in the province of Quebec. The demographic changes observed at the provincial level will no doubt have an impact on net migration in the Sherbrooke area. Given that the CMA receives about 2 to 3 per cent of the immigrants arriving in Quebec each year, a corresponding number of new residents will settle in Sherbrooke. And, as was the case in 2010, the Sherbrooke area will continue to welcome many people from other areas of Quebec.

For both these reasons, net migration in the Sherbrooke CMA will reach close to 1,850 people in 2011. In the short term, these newcomers will no doubt stimulate demand for housing (especially rental dwellings).

## MLS® sales to increase slightly in 2011

The resale market in the Sherbrooke CMA evolved in two different directions in 2010. After posting an increase of 17 per cent in the first quarter of 2010, MLS® sales<sup>5</sup> registered decreases varying between 5 per cent and 15 per cent in the next three quarters. These slowdowns were mainly due to the end of the home purchase move-up effect mentioned

<sup>2</sup> In 2011, Statistics Canada made methodological changes to the Labour Force Survey (LFS). In fact, until December 2010, labour force estimates were calculated using the population data from the 2001 Census. Since January 2011, these estimates have been adjusted based on the population data from the 2006 Census. Also, the CMAs are now based on the 2006 Census geographical boundaries, rather than on the boundaries from the 2001 Census. In the case of the Sherbrooke CMA, the LFS data for the city of Magog are now included in those of the CMA. Historical data (up to 1996) were also adjusted to take these changes into account.

<sup>3</sup> According to the latest Quebec immigration plan forecasts for 2011 issued by the Quebec Ministère de l'Immigration et des Communautés culturelles.

<sup>4</sup> According to the consultation paper entitled "La planification de l'immigration au Québec pour la période 2012-2015," published by the Quebec Ministère de l'Immigration et des Communautés culturelles.

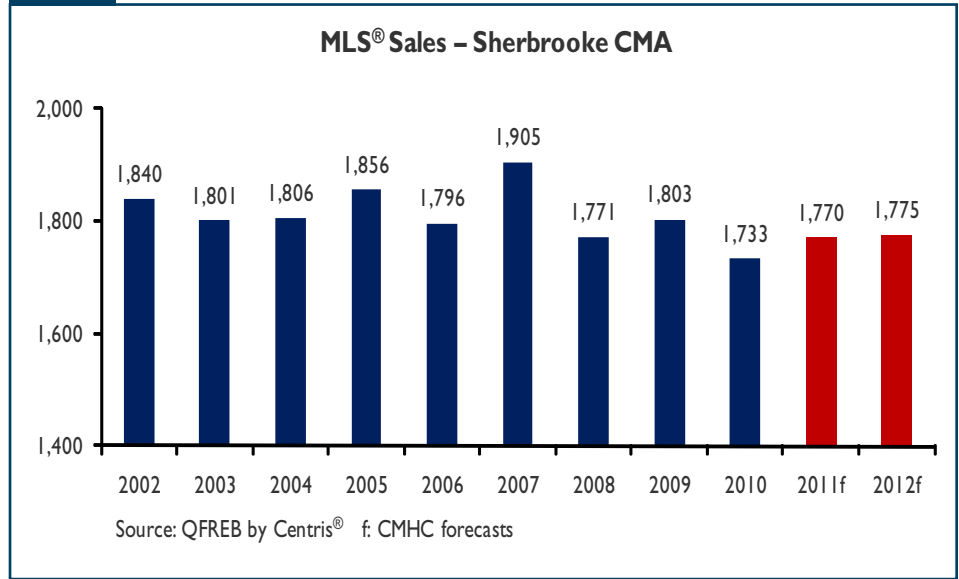
<sup>5</sup> Source : QFREB by Centris®

earlier. However, it should not be forgotten either that the construction of affordable semi-detached and row homes was fairly strong in Sherbrooke last year, which provided significant competition to the resale market. This downward trend continued in the first quarter of 2011, with MLS® sales decreasing by 10 per cent year over year

For the remainder of 2011, the economic fundamentals suggest that resale market activity will increase slightly. As mentioned earlier, MLS® sales will benefit from a more favourable job market. Also, financing conditions will remain favourable to consumers. It should be recalled that the growing supply of existing homes from year to year increases, by the same token, the potential pool of MLS® sales in the Sherbrooke area. In this context, we expect MLS® sales to rise slightly this year, to close to 1,800 units (+2 per cent). With regard to this forecast, two significant aspects must be mentioned. First, condominium sales should do particularly well in 2011, as was the case in 2010<sup>6</sup>. These generally more affordable units can attract first-time buyers and aging clients seeking a home that requires less maintenance.

On the supply side, active MLS® listings have been growing steadily in the Sherbrooke area since the middle of 2010. This was when demand softened on the resale market. As no major changes are expected on the demand side of the MLS® market next year, active listings will rise moderately in 2011, attaining 1,365 units (+2 per cent). As a result, a larger choice of existing homes for sale will be available to households seeking to buy a property next year in the CMA.

Figure 2



The combination of these factors (slight increase in demand and supply) will result in a balanced market that will slowly become more favourable to buyers in 2011. This slight easing of the market will bring about a smaller increase in the average price this year (4 per cent in 2011, versus 6 per cent in 2010). The MLS® average price of homes will reach \$212,500. In 2012, rising mortgage rates will limit the positive impact of the labour market on the resale market. Following several jolts since the middle of 2009, the resale market should be far more stable in 2012. The average price will then attain \$218,000, for an increase of 3 per cent in relation to 2011.

### Housing starts to decrease in 2011

In 2010, foundations were laid for 1,656 housing units in the Sherbrooke CMA, an all-time high. Of these, 1,099 units were intended for the freehold and condominium housing markets, another record for the area. The new home market was in fact very active

during the first six months of 2010, demonstrating that a move-up effect also occurred on this market.

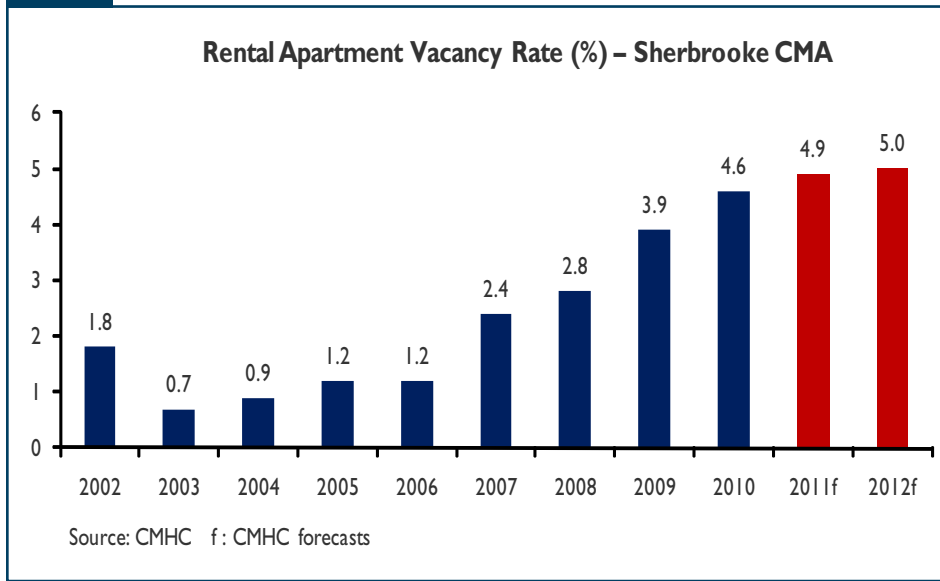
That being said, 1,500 dwellings will be started in 2011, down 9 per cent from 2010. Freehold home starts will decrease, given the reduced pool of potential buyers this year (as a result of the move-up effect mentioned above).

However, this decline conceals opposing dynamics: while single-detached housing starts will drop by 10 per cent (to 515 units), semi-detached and row housing starts will remain at their 2010 level (about 300 units). It should be noted that the results from the last few quarters tend to confirm that single-detached homes have been losing ground to semi-detached and row homes, which are a generally more affordable housing type.

In the condominium segment, housing starts will decrease this year, with about 100 units getting under way in 2011, compared to 132 in 2010. It

<sup>6</sup> Contrary to MLS® sales of single-family houses and plexes, condominium transactions increased in 2010.

Figure 3



should be mentioned however that, with only 8 per cent of starts last year, condominiums remain a relatively small market in the Sherbrooke area. Among all homeownership dwelling types, the decrease in single-detached housing starts will be primarily responsible for the decline in activity in the Sherbrooke CMA this year.

In the rental apartment segment<sup>7</sup>, housing starts will also decrease next year in the Sherbrooke CMA. As will be explained in the last section of this report, the rental housing vacancy rate has been steadily increasing for the past four years in the CMA. Among Quebec's major urban centres, the capital of the Eastern Townships has the highest proportion of vacant rental units, and this trend should continue in 2011. The construction of a large volume of affordable housing units in the CMA over the last few years probably prompted many renters to become homeowners, which explains the successive vacancy

rate increases.

This year, 500 rental apartment units will therefore be started, compared to nearly 640 last year. Consumer preferences for newer, more modern apartments and social housing projects are factors that will limit this decrease in 2011. Finally, it should be mentioned that no major retirement housing projects are expected to get under way this year<sup>8</sup>. In this regard, let's mention that several retirement homes were built in the CMA these past few years, at a time when demand was slowing<sup>9</sup>. This market is therefore currently in an absorption phase.

Next year, a total of 1,400 units will be started in the Sherbrooke CMA (-7 per cent). Rising mortgage rates will restrict the movement to homeownership and therefore limit home construction. Rental apartment starts will also drop, with many units already vacant on the Sherbrooke rental market. Employment growth in

the capital of the Eastern Townships will nevertheless support the new home market in 2012 and, at the same time, limit the drop in housing starts.

As an indication, we should point out that the expected drop in housing starts is in line with net household formation in the Sherbrooke CMA. In fact, it is generally accepted that, over the medium and long terms, housing starts closely follow net household formation. These past few years, net household formation in the Sherbrooke CMA has varied between 1,000 and 1,200 households per year, while housing starts have ranged from 1,300 units to 1,700 units annually, well above demographic needs.

### Rental market to ease slightly

According to the results of the latest CMHC Rental Market Survey conducted in October 2010, the rental apartment vacancy rate<sup>10</sup> increased again in the Sherbrooke CMA. After climbing by 1.1 percentage points in 2009, to 3.9 per cent, this rate continued to rise in 2010, reaching 4.6 per cent. The rental market has now been easing more significantly for the past four years in the Sherbrooke area, mainly as a result of a strong shift to homeownership. It should be mentioned that the increase in the size of the rental housing stock also contributed to the rise in the vacancy rate, but to a lesser extent.

As was already substantially demonstrated earlier, this homeownership trend, while not stopping altogether, will slow down in 2011 in the Sherbrooke CMA. This will

<sup>7</sup> In this case, rental apartments include duplexes and co-operative housing units.

<sup>8</sup> However, expansions to some existing retirement homes are planned in the Sherbrooke CMA in 2011.

<sup>9</sup> In fact, many of the people now aged 75 years or older, who account for a significant share of retirement home clients, were born during the Great Depression of the 1930s, a period when the birth rate was lower.

<sup>10</sup> Privately initiated rental apartment structures of three units and over

help maintain and even boost demand for rental units. In addition, gains in youth employment, an important client group on the rental market, will once again support demand on this market. Another significant factor is the record number of migrants who arrived in the Sherbrooke CMA or will be arriving in the area over the coming year. Most of these new migrants, when they arrive, will be

looking for an apartment, which will again favour the rental market. In spite of this steady demand, it should not be forgotten that more units will be added to the rental housing stock, increasing supply on this market.

Under these conditions, the vacancy rate will reach 4.9 per cent in 2011, up marginally over 2010, while the average monthly rent for two-

bedroom apartments will reach \$580 this year.

The factors fuelling rental housing demand this year will again do so next year, such that the vacancy rate should stabilize at about 5 per cent in 2012.

Forecast Summary Sherbrooke CMA <sup>(1)</sup> Spring 2011							
	2008	2009	2010	2011f	% chg	2012f	% chg
<b>Resale Market</b>							
MLS <sup>®</sup> Sales	1,771	1,801	1,730	1,770	2.3	1,775	0.3
MLS <sup>®</sup> Active Listings	1,376	1,321	1,333	1,365	2.4	1,375	0.7
MLS <sup>®</sup> Average Price (\$)	187,669	193,247	204,441	212,500	3.9	218,000	2.6
<b>New Home Market</b>							
<b>Starts:</b>							
Single-Detached	802	668	570	515	-9.6	500	-2.9
Multiples	825	912	1,086	985	-9.3	900	-8.6
Starts - Total	1,627	1,580	1,656	1,500	-9.4	1,400	-6.7
<b>Average Price (\$) - excluding Magog:</b>							
Single-Detached	197,904	197,990	238,487	245,000	2.7	250,000	2.0
<b>New Housing Price Index (% chg) (Que.)</b>							
	5.0	3.1	3.1	n.a.	-	n.a.	-
<b>Rental Market - excluding Magog in 2006</b>							
October Vacancy Rate (%)	2.8	3.9	4.6	4.9	-	5	-
Two-bedroom Average Rent (October) (\$)	543	553	566	580	-	590	-
<b>Economic Overview</b>							
Mortgage Rate (1 year) (%)	6.70	4.02	3.49	3.23	-	3.76	-
Mortgage Rate (5 year) (%)	7.06	5.63	5.61	5.45	-	5.94	-
Annual Employment Level	94,300	96,800	92,600	98,000	5.8	99,500	1.5
Unemployment rate (%)	6.3	6.6	7.6	7.2	-	7.0	-
Net Migration	1,221	1,800	1,866	1,850	-0.9	1,800	-2.7

MLS<sup>®</sup> is a registered trademark of the Canadian Real Estate Association (CREA)

(1) According to Statistics Canada's new definition, the Sherbrooke CMA now includes the municipality of Magog. Statistics have been adjusted except where indicated.

Source: CMHC (Starts and Completions Survey, Market Absorption Survey), adapted from Statistics Canada (CANSIM), QFREB by Centris®, Statistics Canada. CMHC Forecast (2011-2012).

**NOTE:** Rental universe = Privately initiated rental apartment structures of three units and over

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