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## HOUSING MARKET

## OUTLOOK

Québec

Canada Mortgage and Housing Corporation

[www.cmhc.ca](http://www.cmhc.ca)**Economic and demographic context slightly less favourable**

Gradually rising mortgage rates in recent quarters, along with more modest employment growth in the Québec area, will contribute to a certain slowdown in demand for housing somewhat from now until the end of 2006 and in 2007. In addition to these less favourable economic indicators, demographic growth will be increasingly weaker and net migration will decrease slightly on account of a less attractive job market. No sharp decrease in activity is to be expected, however, as mortgage rates will still be relatively low, no job losses are anticipated and net migration will remain positive. The turnaround in the trends will therefore take place slowly.

After posting an exceptional performance since the beginning of the decade, the Québec census metropolitan area (CMA) labour market will evolve at a much more modest pace in 2006 and 2007. While the average annual employment growth rate was 2.9 per cent during the period from 2001 to 2005, compared to 1.7 per cent for the province overall, the rate of growth will rather be closer to 1 per cent in 2006 and 2007. In concrete terms, 3,000 and 4,000 jobs should be created in 2006 and 2007, respectively.

The unemployment rate will be about 5.5 per cent, keeping the Québec CMA among the areas with the lowest unemployment rates in the country.

The factors explaining the more moderate employment growth include the continued impact of the provincial government's decision to replace only one in two retiring employees. Still in the area of services, the rising interest rates and energy costs have already slowed, and will continue to slow, consumer spending, which will have an impact on employment in the trade sector. As well, the strength of the Canadian dollar and increased competition from foreign companies will also limit job creation in the manufacturing sector. Activity in the construction sector, for its part, has been very vigorous in recent years thanks to the real estate boom, but will also lose strength. Fortunately, the economy of the provincial capital area will benefit from the spin-offs resulting from the preparations for Québec City's 400th anniversary celebrations to be held in 2008. It is anticipated that public investments will total an estimated \$250 million, of which 60 per cent will be spent on the construction of permanent infrastructure.

FALL 2006

**IN THIS ISSUE****1 Economic and demographic context slightly less favourable****2 Mortgage rates have peaked****2 Resale market : activity maintains its momentum****3 New home market : starts to keep falling****3 Rental market : more and more available units****5 FORECAST SUMMARY**

## Mortgage rates have peaked

As a result of the combined effect of the economic slowdown, the strength of the Canadian dollar against the U.S. currency and low inflation, Canadian interest and mortgage rates will remain low in the fourth quarter of 2006 and in 2007.

Mortgage rates went up by 1.0 to 1.5 percentage points between September 2005 and September 2006. It is anticipated that the rates will stay low over the next two or three quarters, during which time they should fall by 25 to 75 basis points before starting to rise again. In the fourth quarter of 2006 and in 2007, the posted rates for one-year, three-year and five-year mortgages should range from 5.50 per cent to 6.50 per cent, from 5.75 per cent to 6.75 per cent and from 6.00 per cent to 7.00 per cent, respectively.

## Resale market: activity maintains its momentum

In 2006, the strong activity observed on the resale market in 2005 will continue at a barely slower pace. In all, 7,045 sales were recorded on the Service inter-agences / Multiple Listing Service (S.I.A. / MLS)<sup>®</sup> network in 2005. In 2006, sales will fall slightly to 7,000 units. The trend will continue in 2007, when 6,900 transactions are expected, for a decrease of just 1.4 per cent. With such results, it can be said that resale market is maintaining its momentum.

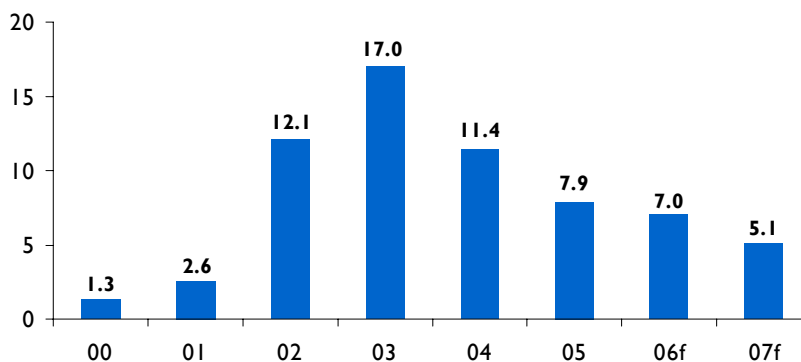
Despite the latest mortgage rate hikes at the beginning of the year, housing demand will therefore remain relatively stable in 2006 and 2007. The vigorous demand for existing homes will be supported, in part, by the job creation rate in the Québec CMA, which, at 3.9 per cent, was among the strongest in the province in 2005, and by the rela-

tively low interest rate levels. At the same time as demand is stabilizing, supply continues to grow, which is contributing to lengthening the listing periods. In fact, listing periods averaged at 56 days in the third quarter of 2006, compared to 40 days at the height of the market in 2003. S.I.A. / MLS<sup>®</sup> listings, which went up in 2005 (+20 per cent), will continue to rise in 2006 and 2007, but at a slower pace, with increases of 10 per cent and 14 per cent, respectively. Many households want to take advantage of the significant gain

As well, the resale market is evolving. Fifteen years ago, single-detached houses represented 74 per cent of the sales, while the share of condominiums was 9 per cent. During the first nine months of 2006, condominium transactions accounted for 21 per cent of S.I.A. / MLS<sup>®</sup> sales, and the share of single-detached homes fell to 61 per cent. Condominiums are therefore becoming more and more popular among an aging population, who wants to do away with certain maintenance tasks and seeks security,

## Growth in Prices Gradually Slowing

Change in Median MLS<sup>®</sup> Price (%) – Québec Area



Source: Chambre immobilière de Québec, CMHC compilation and forecasts  
f: forecasts

in the value of their property in recent years, in order to buy another home that will better suit their needs or to return to renting.

Given the greater supply of properties for sale on market, pressure on prices is easing, but barely. Price hikes of more than 10 per cent are definitely behind us, but the increases remain steady. The median price of properties, which rose by 8 per cent in 2005, will climb by 7 per cent in 2006 and by 5 per cent in 2007, a sign that the market will remain favourable to sellers.

and also among a broader client group, who sees this type of housing as a more economical way to access homeownership. The many condominiums built in recent years helped stimulate the resale market. Condominium sales will rise by close to 12 per cent in 2006, while single-detached home sales are expected to fall by 5 per cent. However, the growth in condominium prices will be below the average for all housing types combined, on account of the relatively abundant supply of units for sale. The seller-to-buyer ratio of 7.6 to 1 observed in the third quarter of 2006 indicates

that this market is practically balanced<sup>1</sup>. The price of condominiums is therefore expected to rise by around 5 per cent in 2006 and 3 per cent in 2007.

It can also be seen that, the more the properties are expensive, the more the market eases, with resulting higher seller-to-buyer ratios and longer listing periods. In fact, for single-detached, semi-detached and row homes priced at under \$150,000, the seller-to-buyer ratios are below 4 to 1 and the listing periods vary between 30 and 45 days, indicating a continued overheating market, or extreme seller's market. Conversely, above the \$200,000 mark, the seller-to-buyer ratios rise to 11 to 1 and the listing periods climb to 90 days, signifying a buyer's market. For condominiums, the trend is similar, but the indicators are higher in all price ranges, given the more abundant supply.

## New home market: starts to keep falling

After five years of growth, residential construction registered a first decline of 6 per cent in 2005. This downward trend will intensify in 2006 and 2007, as starts volumes should reach 5,100 units in 2006 and 4,400 units in 2007, for decreases of 13 per cent and 14 per cent, respectively. Several factors account for this slowdown. There are more and more existing properties for sale, particularly in the case of more expensive properties and in the condominium segment, and the vacancy rates are going back up for both traditional and retirement rental housing. In addition, demographic growth is slowing, which is reducing the need to build new dwellings. However, since these factors are evolving gradually, the decline in starts will also be gradual

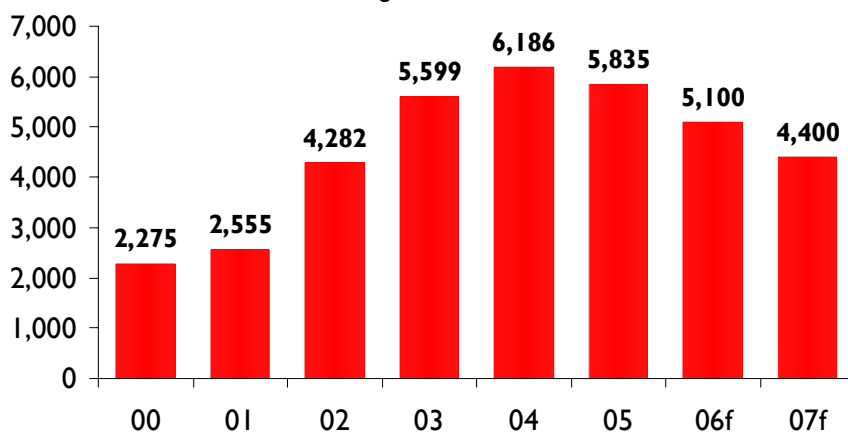
over the 2006-2007 period. It should be recalled that the situation was different during the 1990s, when decreases in activity of up to 50 per cent had been recorded certain years.

Freehold homes<sup>2</sup> are the least affected by the decrease in starts. The decline was effectively marginal in 2005 and will again be less significant than the drops registered in the other market segments in 2006, with an expected 3,000 starts (-9 per cent). Even if the market is easing, the context continues to favour sellers in the case of freehold homes, and there is still a shortage of properties for sale on the market, which justifies the need to build new houses. In 2007, construction is expected to get under way on 2,650 freehold homes, or 12 per cent fewer than in 2006. Given the increasingly higher prices, the share of single-detached houses is tending to decrease in favour of semi-detached and row homes, which are generally less expensive, and duplexes, for which the rental income can help reduce the financial burden. The share of single-detached houses, which was around 90 per cent at the beginning of the decade, will fall back to about 75 per cent in 2006 and 2007.

However, the condominium market will be more affected by the slowdown in construction. The inventory of new unsold condominiums, which was practically non-existent at the beginning of 2003, stood at around 350 units in September 2006. In addition, there are close to 1,000 condominiums for sale on the S.I.A. / MLS® network. As mentioned earlier, the existing condominium market is now practically balanced. In this context, developers will demonstrate more caution, and starts should therefore fall to 900 units in 2006

## Residential Construction: Smooth Landing Continues

Total Housing Starts – Québec Area



Source: CMHC  
f: forecasts

<sup>1</sup> It should be noted that, on a balanced market, which equally favours buyers and sellers, the seller-to-buyer ratio stands between 8 and 10 to 1. A ratio below 8 to 1 signifies a seller's market, while a ratio above 10 to 1 indicates a buyer's market.

<sup>2</sup> Freehold homes include detached, semi-detached and row houses, as well as duplexes.

(-20 per cent) and then to 750 units in 2007 (-17 per cent). While there is no cause for alarm for the moment, certain sectors should be watched more closely, as they are characterized by either an already balanced existing home market or a longer duration of supply<sup>3</sup> than on the new home market. These sectors are the Québec Haute-Ville and Basse-Ville districts, as well as Sainte-Foy, Charlesbourg and Lévis.

Rental housing construction will also slow down. There should be 1,200 starts in 2006 and 1,000 in 2007, for decreases of 16 per cent and 17 per cent, respectively. The gradual rise in the vacancy rates for traditional and retirement rental housing will limit the addition of new units. In the case of traditional units, the saturation of the existing upper-range market, particularly in the Sainte-Foy sector, and the impossibility to build privately initiated affordable housing will contribute to restricting construction.

As for retirement housing, activity was intense in 2005, as 650 new units were started. The arrival of these units in 2006 will drive up the vacancy rate. It can therefore be expected that new retirement housing construction will take place at a more modest pace in 2006 and 2007.

## Rental market: more and more available units

The upward trend in the vacancy rate for traditional rental housing, which began in 2003, will continue. The vacancy rate, which was 1.4 per cent in October 2005, should therefore reach 1.8 per cent in 2006 and 2.2 per cent in 2007. The increase in the construction of rental and condominium hous-

ing in recent years and a weakening demand, particularly due to more moderate employment growth and the resulting slowdown in migration, explain this rise in the vacancy rate.

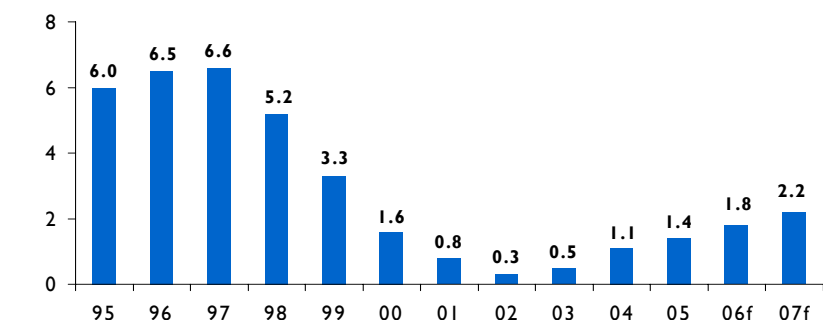
Just like on the resale market, conditions on the rental market vary significantly depending on the rent range. For two-bedroom units renting for \$900 or over, there has been a surplus since 2004 and, in 2005, the vacancy rate reached 7.0 per cent. Although the vacancy rate is expected to decrease, given the few luxury units that will be arriving on the market, the surplus will persist in 2006 and 2007. In the case of the most affordable units (under \$600), the opposite holds true, as the vacancy rate attained 0.6 per cent. Since the private sector cannot build housing units at this price, notably on account of overly high construction costs, the supply is growing very slowly. In the mid-range category (\$600 to \$899), the vacancy rate was

1.5 per cent in 2005, and it is in this category that the vacancy rate will increase the most in 2006 and 2007. In fact, in this rent range, wood-and-brick structures can still be built. The vacancy rate should therefore continue to rise, particularly in the outlying sectors, where lands are better suited to the construction of lower-density, wood-and-brick buildings.

Normally, as the supply of units increases, the pressure on rents decreases. The rise in the average rent, which peaked at 4.5 per cent in 2004, slowed to 3.4 per cent in 2005. According to our forecasts, the average rent can be expected to increase by 2.5 per cent in 2006 and by 2.0 per cent in 2007. It should be noted, however, that the increase in the average rent could be greater in 2007, depending on the impact that the new assessment roll will have on the tax bills for income properties.

## Vacancy Rate to Keep Rising

Vacancy Rate (%) – Québec Area



Source: CMHC  
f: forecasts

<sup>3</sup> The duration of supply is the period (in months) required to absorb the units that are unoccupied or under construction.

# Forecast Summary

## Québec Census Metropolitan Area

### Fall 2006

	2004	2005	2006f	2007f	2005/2004	2006/2007
<b>RESALE MARKET <sup>1</sup></b>						
<b>MLS® sales</b>						
Total	6,257	7,045	7,000	6,900	-0.6%	-1.4%
Single-detached	3,962	4,415	4,200	4,050	-4.9%	-3.6%
Semi-detached and row	887	943	975	950	3.4%	-2.6%
Condominium	1,123	1,364	1,525	1,600	11.8%	4.9%
Duplex	285	323	300	300	-7.1%	0.0%
<b>Active MLS® listings</b>						
Total (annual average)	2,612	3,180	3,500	4,000	10.1%	14.3%
<b>Median MLS® price (\$)</b>						
Total	127,281	137,351	147,000	154,500	7.0%	5.1%
Single-detached	134,850	146,557	158,500	168,000	8.1%	6.0%
Semi-detached and row	112,534	121,435	130,000	136,500	7.1%	5.0%
Condominium	108,041	118,591	125,000	129,000	5.4%	3.2%
<b>NEW HOME MARKET</b>						
<b>Starts</b>						
Total	6,186	5,835	5,100	4,400	-12.6%	-13.7%
Freehold	3,311	3,284	3,000	2,650	-8.6%	-11.7%
Condominium	1,200	1,131	900	750	-20.4%	-16.7%
Rental	1,675	1,420	1,200	1,000	-15.5%	-16.7%
<b>New Housing Price Index</b>						
1997 = 100	129.30	134.90	142.30	148	5.5%	4.0%
<b>RENTAL MARKET (%)</b>						
Vacancy rate (October)	1.1	1.4	1.8	2.2	--	--
Change in rents (2-bedroom)	4.5	3.4	2.5	2.0	--	--
<b>ECONOMIC OVERVIEW</b>						
Mortgage rate - 1-year (%)	4.6	5.1	6.3	(5.5 - 6.5)	--	--
Mortgage rate - 5-year (%)	6.2	6.0	6.7	(6.0 - 7.0)	--	--
Employment level	363.4	377.6	380.6	384.6	0.8%	1.1%
Unemployment rate (%)	5.8	5.6	5.2	5.5	--	--

<sup>1</sup> The publication of MLS® data is made possible thanks to the collaboration of the Chambre immobilière de Québec (CIQ).

f: CMHC forecasts

Sources: CMHC, CIQ and Statistics Canada

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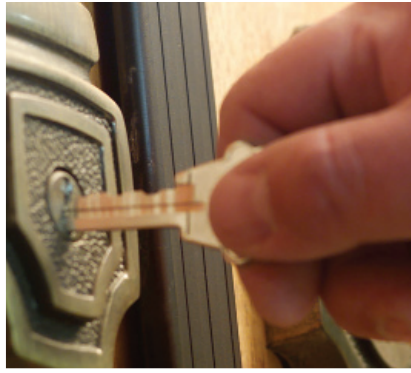
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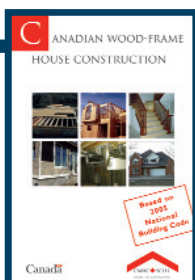
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