

HOUSING MARKET OUTLOOK

Sherbrooke CMA



Canada Mortgage and Housing Corporation

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Several factors remain positive for the housing market

On a demographic level, two significant factors are supporting demand for housing. First of all, international migration has increased considerably since the year 2000, and 1,040 people came to settle in the area last year. The need to house these newcomers is encouraging real estate developers, by putting upward pressure on the overall

demand for rental housing. As well, the increase in the number of households during the period from 2001 to 2006 (5,900 households) was greater than the rise registered over the period from 1996 to 2001 (4,700 households). This result confounds forecasters' predictions and pushes back the downward trend in residential construction arising from demographic changes. If there are any decreases in housing starts over the next few years, they will be of a cyclical nature, and therefore short-lived.

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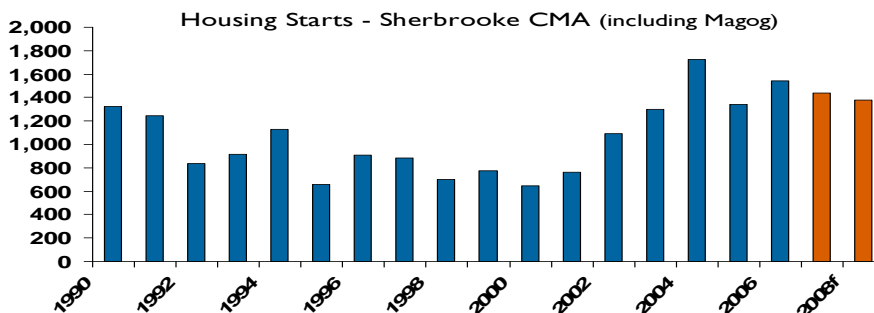
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Figure 1

Housing Starts Begin to Fall



Source: CMHC f: forecasts

Several economic factors are also helping to fuel housing demand. Firstly, despite a few pitfalls, the Quebec economy remains dynamic even though it has already been on the rise for 10 years. In the Estrie area, GDP growth was 3.4 per cent in 2006. This year and next, the pay equity settlement by the Quebec government will breathe new life into the economy, as impacted employees received an average of \$5,300 at the end of March 2007, and other smaller payments will follow.

Secondly, job creation will continue in the Sherbrooke census metropolitan area (CMA), with 800 new positions being added in each of 2007 and 2008. In fact, the job losses in the manufacturing sector, on account of the competition from Asia and the strength of the Canadian dollar against the U.S. dollar, will be more than offset by the job gains in the construction and service sectors. The construction industry will be stimulated by many ongoing and upcoming investment projects in the area, including the planned construction of the centre of excellence in computer engineering and the facilities of the multinational Charles River Laboratories. In the service sector, call centres are among the enterprises that will create jobs.

Lastly, incomes are growing, and the disposable income of young families is on the rise. Various tax changes, particularly the arrival of \$7-a-day daycare, have made it such that, from 1997 to 2007, the disposable income of families with two children under the age of 5 years has risen, in many cases, by \$10,000 per year, or \$833 per month¹. The latest

measure, which dates back to August 2006, is the Universal Child Care Benefit, paid by the federal government in instalments of \$100 per month per child. Income growth is an important variable in the equation, when considering the purchase of a home.

The only shadow on the horizon will come from the slight rise in mortgage rates, which, combined with the rapid increase in home prices, will require additional financial effort on the part of first-time buyers, mainly in 2008. Mortgage rates are expected to remain flat through the end of 2007. While still low by historical norms, mortgage rates are expected to rise gradually by 25-50 basis points in 2008. The one year posted mortgage rate is forecast to be in the 6.50-7.50 per cent range, while three and five year posted mortgage rates are forecast to be in the 6.75-7.75 per cent range in 2008.

Resale market remains very vigorous

The strength of the economy at the beginning of the year surprised several observers. It should be noted that, after a period of economic growth as long as the one that is currently prevailing, every little cloud leads to fear of a storm, bringing to mind that everything that goes up eventually comes back down.

Now that the nervousness has passed, the resale market has regained strength. Sales, which had declined in the first quarter, rebounded astonishingly (+25 per cent) in the following three months.

Listings continue to rise, but their growth appears to be slowing down somewhat. As for prices, they went up by 7 per cent in the second quarter. The intense activity on the market is even more apparent when Magog is excluded from the results for the Sherbrooke CMA. In this case, with a price hike of 11 per cent and a seller-to-buyer ratio of 5 to 1, the market is practically overheating. In the Magog area, the market is more balanced.

In the overall Sherbrooke CMA, sales registered on the Multiple Listing Service® (MLS®) will rise by 4.0 per cent in 2007, to a total of 1,860. A further increase is anticipated in 2008, when there should be 1,935 existing property transactions. This strong demand will be supported a continued solid economy, favourable financing conditions and a relatively significant supply of properties for sale. As well, around one third of the increase in transactions will result from the more frequent use of real estate agents on the part of sellers. This will especially be the case in Magog, where the market share of agents could rise from 67 per cent in 2006 to 75 per cent in 2007, on account of the less tight market conditions in this area.

The recent rise in births in the area is another factor that will support sales of new and existing homes over the coming months. The arrival of a child is a privileged time to access homeownership. Young generation Xers had told us a few years ago that this was a major trigger in the decision to buy a home. A new addition to the family can also lead to a move when a need for more space is felt. Current tax measures are tending to improve the financial

¹ Source: "Les familles, plus riches que jamais", *Affaires Plus*, July 2007, p. 14.

position of young families, helping to lessen the impact of major price increases and mortgage rate hikes.

Overall, the market will continue to favour sellers throughout the forecast period. The seller-to-buyer ratio will therefore remain below 8 to 1. The growth in prices will stay robust and exceed inflation, with increases of 5.0 per cent in 2007 and 4.5 per cent in 2008. In addition to the tight market conditions, the demographic trends (steady influx of newcomers into the area) and good economic performance (growth in incomes and employment) are fuelling the surge in prices. In particular, the pay equity settlement will temporarily boost incomes in 2007 and 2008. The average price of the properties sold through the MLS® will reach \$169,300 this year and \$173,600 next year.

Residential construction expected to slow down

Housing starts will begin to edge down (-6.8 per cent) this year, falling from 1,545 units in 2006 to 1,440 in 2007. This trend will continue in 2008, when starts should decrease to 1,380 units. Despite this slight decline, residential construction will still be very dynamic, as the level of production will remain above the annual average of 1,050 units recorded since the beginning of the 1990s. This performance will be attributable to the low mortgage rates that are facilitating the development of real estate projects, a local economy that is promoting job creation and the arrival of a large number of immigrants.

The decrease in activity will be mainly due to the multiple-family housing segment, as foundations will be laid for 157 fewer units this year than in 2006. It should be recalled that, last year, the construction of a 279-unit retirement home had driven up starts in this segment. Experience shows that projects of this size rarely get under way two years in a row. The largest building that will be started in 2007 will comprise only 80 units, once again intended for seniors. However, the low vacancy rate for rental housing and the arrival of around 1,000 immigrants per year will boost the production of traditional rental housing units. As well, foundations will be laid for a few condominium, semi-detached and row dwellings (fewer than 100 in all), which will bring total multi-family housing starts to 800 units this year. About 100 fewer units will be started next year, following an increase of half a percentage point in the vacancy rate.

The production of single-detached houses reached a low point last year, as 640 units will be started this year, compared to 588 in 2006. Some 40 more units will be built in 2008. The ever-increasing choice of existing homes for sale and the significant gap between new and existing house prices are limiting the possibilities of an increase in the production of single-detached home starts.

In the Sherbrooke CMA (excluding Magog), the average price of single-detached houses will rise by 6.0 per cent and 5.0 per cent in 2007 and 2008, respectively, to \$202,700 this year and \$212,800 next year. The significant growth in the move-up buyer group is affecting the

distribution of new home sales and pushing up the average price. In 2004, only 19 per cent of new single-detached houses were selling for \$200,000 or more. This proportion rose to 30 per cent in 2005 and then to 40 per cent in 2006. In absolute figures, this share represented slightly over 200 houses in 2006. It should also be mentioned that, in recent years, the employment situation has constantly favoured buyers aged from 45 to 64 years, a target client group for expensive homes.

Builders often wonder about the housing intentions of baby boomers. A recent study² on the migration of people aged from 55 to 65 years over the period from 1995 to 2005 provides us with information on the preferences of the oldest baby boomers. In the Estrie area, it can be noted that the urban zones gained 230 older baby boomers over 10 years. The volume of moves is not very significant as, during this period, there were 665 arrivals and 435 departures. The rural portion of the Estrie area, for its part, gained 267 older baby boomers (676 arrivals and 409 departures). The moves occur mainly between the rural and urban zones of the Estrie area: those who lived in the country come to the city, and the city dwellers move out to country. In the rural zones, the second greatest population movement comes from residents of Montréal and the urban zones of the Montérégie area. Therefore, few older baby boomers make a radical change in their place of residence. In fact, when they move, they stay within the zone where they lived. For many, the choice of moving closer to nature does not strike a chord. In any case, this choice does not result in a

² Source: *La migration interne de 55 à 65 ans au cours de la décennie 1995-2005*, Institut de la statistique du Québec, by Chantal Girard, excerpt from the publication *La situation démographique au Québec. Bilan 2006*.

permanent move to a rural zone, but may rather be made through the purchase of a second home or a move to a neighbourhood where nature is more present.

Higher percentage of unoccupied rental housing units in sight

Between the 2005 and 2006 surveys, 431 new units were added to the rental housing stock. By the 2007 survey, it is expected that there will be 675 more new apartments. This increase will result in part from the construction of a 279-unit housing project, which has been ready to occupy since July. The gain will also be attributable to the

low percentage of unoccupied units, which is prompting developers to start up new projects.

The rapid growth in supply comes at a time when demand for rental housing is on the rise thanks to the arrival of a significant number of immigrants. In addition, the development of a new retirement home will stimulate demand on the part of seniors. Given that there are very few vacant units in retirement homes, part of the latent demand may be expressed. However, the deterioration of the youth employment situation since the beginning of the year could limit the increase in demand for rental housing.

Overall, we should see a rise in the vacancy rate in October, with the rise in demand being insufficient to meet the growth in supply. The vacancy rate should reach 1.7 per cent. The market will therefore resume its easing course, after taking a year's break. For 2008, the rate is expected to reach 1.8 per cent.

With the market remaining tight all in all, and a break having been observed in the easing trend in 2006, an increase in rents above the hike recorded last year is anticipated for 2007. The average rent for two-bedroom units should reach \$530, compared to \$515 in 2006.

Forecast Summary (1)							
Sherbrooke CMA							
Fall 2007							
	2004	2005	2006	2007f	% chg	2008f	% chg
Resale Market							
MLS® Sales	1,778	1,829	1,789	1,860	4.0%	1,935	4.0%
MLS® New Listings	707	859	1,052	1,150	9.3%	1,225	6.5%
MLS® Average Price (\$)	\$140,800	\$156,300	\$164,400	\$172,600	5.0%	\$180,400	4.5%
New Home Market							
Starts:							
Single-Detached	680	714	588	640	8.8%	680	6.3%
Multiples	1,048	629	957	800	-16.4%	700	-12.5%
Starts - Total	1,728	1,343	1,545	1,440	-6.8%	1,380	-4.2%
Average Price (\$) - excluding Magog:							
Single-Detached	\$155,603	\$177,100	\$191,177	\$202,700	6.0%	\$212,800	5.0%
New Housing Price Index (% chg) (Que.)							
	6.3	4.9	4.4				
Rental Market - excluding Magog							
October Vacancy Rate (%)	0.9%	1.2%	1.2%	1.7%		1.8%	
Two-bedroom Average Rent (October) (\$)	\$495	\$505	\$515	\$530	2.5%	\$540	2.0%
Economic Overview							
Mortgage Rate (1 year) (%)	4.80%	5.80%	6.30%	6.86%	-	7.19%	-
Mortgage Rate (5 year) (%)	6.05%	6.30%	6.45%	7.02%	-	7.41%	-
Annual Employment Level - excluding Magog	81,100	80,900	81,900	82,700	1.0%	83,500	1.0%
Unemployment rate (%) - excluding Magog	6.9%	7.3%	7.9%	7.5%		7.4%	
Net Migration - excluding Magog	1,210	1,334	1,353	1,400	3.5%	1,450	3.6%

(1) According to Statistics Canada's new definition, the Sherbrooke CMA now includes the municipality of Magog. Statistics have been adjusted except where indicated. MLS® is a registered trademark of the Canadian Real Estate Association (CREA).

Source: CMHC (Starts and Completions Survey, Market Absorption Survey), adapted from Statistics Canada (CANSIM), CREA, Statistics Canada (CANSIM)

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

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