

HOUSING MARKET OUTLOOK

Sherbrooke CMA



CANADA MORTGAGE AND HOUSING CORPORATION

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MLS® sales to soar and housing starts to decrease slightly in 2010¹

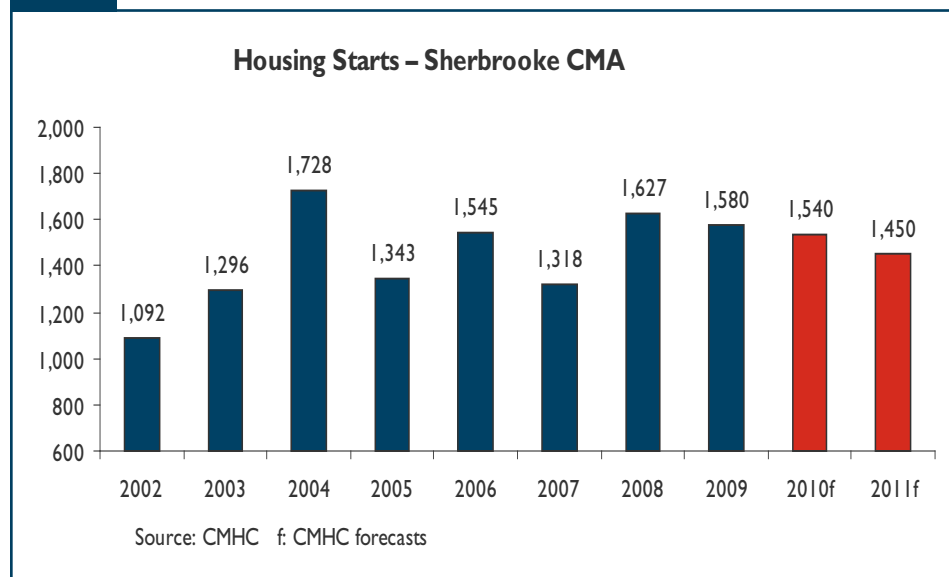
Low mortgage rates, combined with the current economic recovery, will impact the Sherbrooke census metropolitan area (CMA) real estate market this year. Compared to 2009, sales registered through the Multiple

Listing Service (MLS)® will rise by 6 per cent, while housing starts will drop by 3 per cent as a result of the high level of housing activity observed in 2009, and not the deterioration of economic conditions..

Employment to recover

During the first six months of 2009, the average number of jobs² decreased by about 2 per cent

Figure 1



¹ The forecasts included in this document are based on information available as of April 23, 2010.

² Source: Statistics Canada (LFS). Data for the Sherbrooke CMA exclude the city of Magog.

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but then increased by the same percentage in the second half of the year. Therefore, the number of people employed in the CMA remained relatively stable in 2009, at 83,500.

In 2010, the improvement in global economic conditions will increase job prospects in the Sherbrooke CMA, where 1,000 jobs will be created, for a total of 84,300 jobs (+1 per cent). In 2011, the number of employed people will reach 85,500 (+1.5 per cent). This upward trend can be explained by the lag that is generally observed between an economic recovery and the ensuing upturn in employment, as companies are more prudent in their hiring decisions.

As mentioned in the last issue of the *Housing Market Outlook* report for the Sherbrooke CMA, several factors will help boost the economy and, in turn, housing activity in Sherbrooke over the coming year. First, the capital of the Eastern Townships should benefit from several economic stimuli in the next few months, such as government investments in infrastructure and road projects, not to mention the economic spinoffs from the many non-residential construction projects under way. Second, with the decreasing uncertainty on the markets, the private sector will now also fuel the economic growth. And third, several organizations will be seeking new talent in the Sherbrooke area this year.

Mortgage rates

The Bank of Canada cut the target for the overnight rate in the early months of 2009. The rate was 1.50 per cent at the start of 2009 and has since fallen to 0.25 per cent. Looking ahead, we expect that short-term interest rates

will begin to rise in the second half of 2010.

With the overnight rate expected to increase in the coming months, mortgage rates have begun to rise. According to CMHC's base case scenario, posted mortgage rates will gradually increase throughout the course of 2010, but will do so at a slow pace. For 2010, the one-year posted mortgage rate is assumed to be in the 3.6-4.8 per cent range, while three- and five-year posted mortgage rates are forecast to be in the 4.2-6.7 per cent range. For 2011, the one-year posted mortgage rate is assumed to be in the 5.0-6.0 per cent range, while three- and five-year posted mortgage rates are forecast to be in the 5.6-7.2 per cent range.

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

Net migration on the rise

The recent demographic changes at the provincial level (significant rise in immigration and lower interprovincial deficit) will no doubt have had an impact on net migration in the Sherbrooke area in 2009. Given that the Sherbrooke CMA receives about 2 per cent of the immigrants arriving in Quebec each year, a greater number of new residents will settle in the CMA. In addition, and as mentioned previously, the depth of the economic downturn in the rest of Canada certainly discouraged workers from leaving the area, which improved net interprovincial migration. Finally, data compiled by the Institut de la statistique du Québec

(ISQ)³ show that the Sherbrooke area attracted people from other areas of the province in 2009, another factor that contributed to the higher net migration.

For all these reasons, net migration in the Sherbrooke CMA should reach 1,650 people in 2009, compared to 1,559 in 2008 (+6 per cent). In 2010 and 2011, net migration in the CMA should continue to rise, but less significantly than in 2009. While the government targets should bring about an increase in the number of immigrants in the area during those two years, Western Canada will attract workers from Quebec, and the Sherbrooke area, thanks to improved economic conditions.

In 2010 and 2011, 1,675 and 1,700 migrants, respectively, will be added to the CMA population, which will lead to an increase in housing demand (especially rental).

Resale market : Seller's market

The resale market⁴ in the Sherbrooke CMA evolved in two different directions in 2009. After decreasing by 4 per cent and 6 per cent in the first and second quarters, MLS® sales climbed by 13 per cent and 11 per cent in the third and fourth quarters. In all, 1,803 existing homes were sold in the CMA in 2009, for an increase of 2 per cent over 2008. This growth resulted from a combination of two factors: first, there was some catching up—supported by the low interest rates—in relation to the low levels of activity recorded in second half of 2008 and, second, a number of purchases were moved up on account of the anticipated increase in mortgage interest rates in 2010.

³ Source: Institut de la statistique du Québec, use of the insured persons registration file (FIPA) of the Régie de l'assurance maladie du Québec (RAMQ).

⁴ Source : QFREB by Centris®

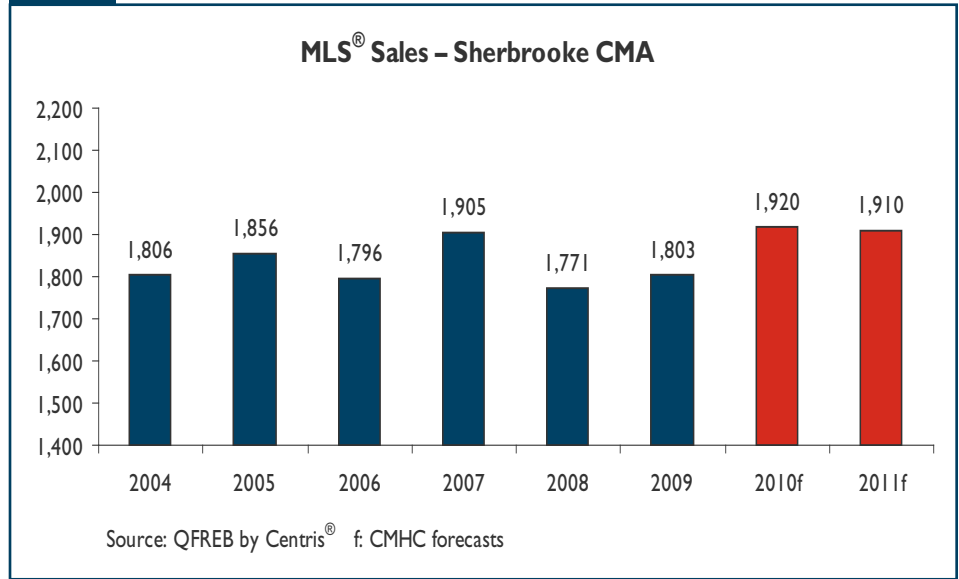
Buyers continued to move up their purchases in the first quarter of 2010, as sales rose by 17 per cent.

While sales increased, active listings decreased, falling by 4 per cent in 2009 and by 11 per cent in the first quarter of 2010. This drop reflected the strong demand on the resale market but could also have been due to the aging of the population. In fact, the growth in the number of seniors, who are generally sellers rather than buyers, will be relatively slow over the next few years, which will limit the potential number of homes for sale.

With this increase in demand and decrease in supply, the resale market shifted from balanced to seller's market conditions in the Sherbrooke CMA in 2009⁵. The average price climbed by 3 per cent between 2008 and 2009 and continued to rise in the first quarter of 2010.

Currently, economic fundamentals suggest that resale market activity will remain strong in 2010. The favourable employment and financing conditions, which should however deteriorate slightly, will prompt many households to buy a home. We therefore expect MLS® sales to rise by 6 per cent this year, to 1,920 units. It should be mentioned, though, that the increases will be less and less significant as the year progresses, on account of the high level of activity registered in the second half of 2009. On the supply side, for the same reasons as above, the number of MLS® listings will decrease by 2 per cent in 2010, to 1,300 units. Given the growing demand for existing homes and the decreasing supply in the Sherbrooke CMA, the market will become even more favourable to sellers this year. Consequently, the average price will post a sustained increase (+5 per

Figure 2



cent), climbing from \$193,245 to \$203,000.

While these results suggest that sales and the average price will rise in the CMA in 2010, it should be noted that the situation will be slightly different in two of the large sectors of the CMA, namely, the cities Sherbrooke and Magog. In the case of MLS® sales, the previously mentioned economic fundamentals will apply to both Sherbrooke and Magog. Increases will therefore be registered in both these sectors. As for the average price, however, it is important to note that, contrary to the overall CMA, the Magog area market remains favourable to buyers. Therefore, the average price should rise less significantly there than in the CMA.

In 2011, two major factors will limit MLS® sales. First, given the higher mortgage rates, fewer households will want to buy a home. Second, the fact that purchases will be moved up throughout this year will shrink the pool of potential buyers in 2011. The only factor that will support demand

next year will be the stronger job creation in the CMA. In all, 1,910 existing homes will change hands in 2011, about the same number as this year. As a result of the weaker demand, the average price will rise by only 2 per cent next year, a much smaller increase than the 5-per-cent hike expected for this year.

Housing starts to decrease slightly in 2010

In the Sherbrooke CMA, foundations were laid for 668 single-detached homes in 2009, down 13 per cent from a year earlier. It should be recalled, however, that 802 such houses had been started in 2008—the highest level in the last 20 years. In addition, in times of economic uncertainty, as was the case last year, families usually turn to more affordable housing types, such as semi-detached and row homes.

In 2010, the decrease in single-detached home construction is expected to continue. The earlier-than-planned purchases, which we

⁵ The market is deemed favourable to sellers in the case of single-family homes, balanced in the case of plexes and favourable to buyers in the case of condominiums.

mentioned in the previous section, probably mean that many first-time buyers are entering the market. These households, who often have a more limited budget than repeat buyers, will continue to opt for less costly dwellings over new single-detached homes. In addition, since mortgage rates will climb throughout 2010, and consequently cause monthly mortgage payments to rise, sales of new single-detached houses should slow down. This being said, in the near term, the relative tightness on the resale market will fuel single-detached home building, notably.

Contrary to single-detached home construction, multiple-unit (semi-detached, row and apartment) housing starts grew significantly in 2009 (+11 per cent). In addition, from January to March 2010, such starts were up notably over the first quarter of 2009. Even with this gain, though, only 900 multiple housing units should be started in 2010, down 1 per cent from last year. This turnaround can be mainly explained by the expected slowdown in rental apartment construction. As explained in the last section of this report, the rental housing vacancy rate has been steadily increasing for the past three 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 2010⁶. Foundations will be laid for 450 rental apartment units⁷ this year, compared to nearly 650 units in 2009. As was the case last year, no major retirement housing projects are expected to get under way in 2010. It should be noted that several retirement homes were

built in the CMA these past few years, at a time when demand was slowing⁸. The vacancy rate for retirement homes is therefore relatively high and should remain high for a few more years.

Relative housing affordability is a topic that was mentioned earlier to explain the decreasing popularity of single-detached houses observed in the Sherbrooke CMA in 2009. Semi-detached and row homes are housing categories that managed to do quite well last year, with 171 starts in the CMA, or more than double the number recorded in 2008. A similar level of activity had not been observed since the 1990s and the years that followed. The same phenomenon will occur this year, as around 250 new semi-detached and row housing units will be recorded in the Sherbrooke area. It is important to keep in mind that the limited supply of such houses on the resale market is another factor that will boost semi-detached and row home construction this year. As for condominiums, which are another affordable housing type, there should be about 50 more units started in 2010 than the 100 or so built last year.

In 2011, foundations will be laid for 1,560 dwellings, down 1 per cent from the 1,540 units that will be started in 2010. As a result of the rise in mortgage rates and the smaller pool of buyers resulting from earlier-than-planned purchases, fewer single-detached homes will get under way. The same reasoning can be applied to the semi-detached and row homes, but it is possible that demand for such dwellings, which are less expensive, will not be as affected by the increase

in interest rates. It should be added that there will also be fewer rental apartment starts next year.

Rental market conditions to soften

According to the results of the latest Rental Market Survey conducted by CMHC in October 2009, the rental apartment vacancy rate⁹ increased again in the Sherbrooke CMA. After climbing by 0.4 of a percentage point in 2008, to 2.8 per cent, this rate continued to rise in 2009, reaching 3.9 per cent. The rental market has now been easing more significantly for the past three years in the Sherbrooke area.

The report on this survey also indicates that the greater proportion of renter households now buying homes was one of the factors that accounted for these vacancy rate hikes. Sales of existing and new homes have remained strong in recent years, suggesting that many renter households became homeowners. As was already mentioned earlier, this homeownership trend should continue in 2010, thereby curbing demand for rental units. All in all, only the growth in net migration and improving youth employment in the CMA will support demand on the rental market over the coming year. In addition, rental apartment starts were very significant last year, which will increase supply on the market. For all these reasons, the vacancy rate will reach 4.5 per cent in 2010, up 0.6 of a percentage point over 2009. For its part, the average rent for two-bedroom apartments will reach \$560 this year.

⁶ There is usually a lag between the number of rental apartment starts and changes in the vacancy rate. While this is not our reference scenario, a high level of rental apartment starts could still be observed for a few years, despite the steady rise in the vacancy rate.

⁷ Rental apartments, including duplexes and co-operative housing units.

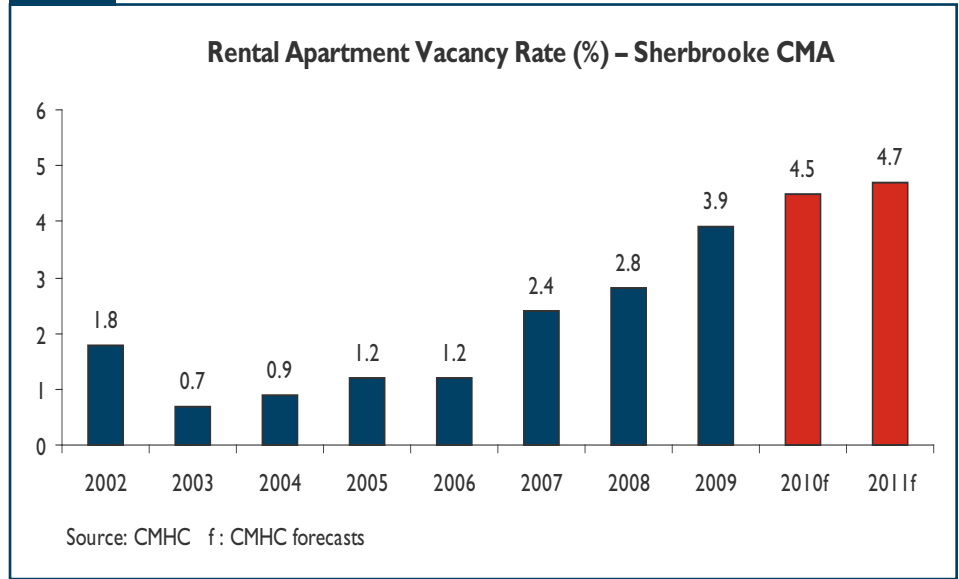
⁸ In fact, many of the people now aged 75 years or older, who account for a significant share of retirement home clients, were born during the Great Depression of the 1930s, a period when the birth rate was lower.

⁹ Privately initiated rental apartment buildings with three or more units.

As was the case in 2009, the vacancy rate increases will be smaller in the west and central districts of the city of Sherbrooke¹⁰. It should be recalled that these districts are home to many students and immigrants, who make up large client groups on the rental market.

In 2011, the weaker movement of renters to homeownership will allow demand for rental accommodations to pick up, while supply will grow only slightly. The vacancy rate should therefore reach 4.7 per cent next year, up slightly over 2010.

Figure 3



¹⁰ Prior to the mergers of 2002.

Forecast Summary Sherbrooke CMA ¹ Spring 2010							
	2007	2008	2009	2010f	% chg	2011f	% chg
Resale Market²							
MLS [®] Sales	1,905	1,771	1,803	1,920	6	1,910	-1
MLS [®] Active Listings	1,144	1,376	1,321	1,300	-2	1,310	1
MLS [®] Average Price (\$)	\$183,120	\$187,669	\$193,245	\$203,000	5	\$207,000	2
New Home Market							
Starts:							
Single-Detached	666	802	668	660	-1	625	-5
Multiples	652	825	912	900	-1	825	-8
Starts - Total	1,318	1,627	1,580	1,560	-1	1,450	-7
Average Price (\$) - excluding Magog:							
Single-Detached	\$191,177	\$195,868	\$197,904	\$200,000	1	\$202,000	1
Rental Market³							
October Vacancy Rate (%)	2.4	2.8	3.9	4.5	-	4.7	-
Two-bedroom Average Rent (October) (\$)	\$529	\$543	\$553	\$560	-	\$565	-
Economic Overview							
Mortgage Rate (1 year) (%)	6.90	6.70	4.02	4.23	-	5.56	-
Mortgage Rate (5 year) (%)	7.07	7.06	5.63	6.20	-	7.06	-
Annual Employment Level - excluding Magog	84,100	83,000	83,500	84,300	1	85,500	1
Unemployment rate (%) - excluding Magog	6.4	6.2	6.9	7.9	-	7.9	-
Net Migration ⁴ - excluding Magog	1,467	1,559	1,650	1,675	2	1,700	1

MLS[®] 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.

² Source: QFREB by Centris[®]

³ Privately initiated rental apartment structures of three units and over

⁴ Migration data for 2009 is a forecast

Source: CMHC (Starts and Completions Survey, Market Absorption Survey), adapted from Statistics Canada (CANSIM), Statistics Canada (CANSIM), QFREB by Centris[®]. CMHC Forecast (2010-2011)

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