

SPOTLIGHT ON HOUSING

Quebec's Resale Market Has Stabilized, but New Home Construction Has Continued to Slide

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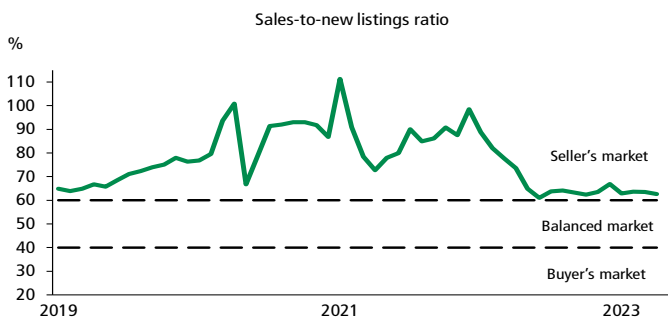
The effects of the steep interest rate hikes that began in Q1 2022, throwing a wrench into the residential housing market, seem to be easing, at least for now. After a period of declining resale prices, things have levelled off somewhat in recent months. Still, it's probably just a pause. We're in for a more challenging economic environment in the coming quarters, with a short, moderate recession still forecast for Quebec in 2023, which will soften the labour market and, in turn, the housing market. The current reprieve for the resale market is therefore likely to be short-lived.

The new home construction market, on the other hand, has continued to slide: the high cost of land, materials and labour is compounding the growing financing challenges faced by many developers. The creation of new rental housing is slowing, putting increased pressure on rent prices.

A Short-Lived Reprieve for the Real Estate Market?

While all the attention has been on [the Canadian resale market gaining strength](#), the situation is more tenuous in Quebec. While a slight increase in the housing inventory has seen prices level off somewhat, on the whole it remains a seller's market, if only just (graph 1).

GRAPH 1
Quebec's Housing Market Is Almost Back to Balanced Territory

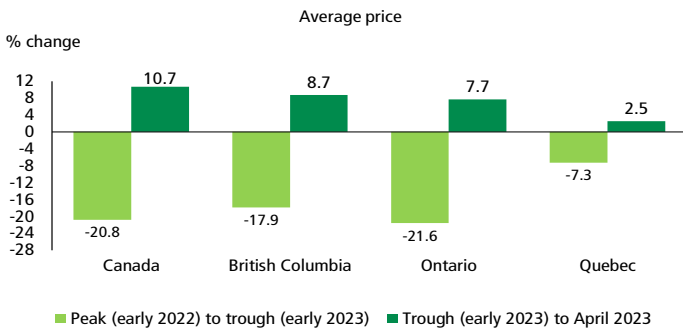


Sources: Canadian Real Estate Association and Desjardins Economic Studies

In Canada, a jump in sales while the housing supply is at a 20-year low has resulted in tighter market conditions. The return of a much more seller-friendly market sent the average home price up 10.7% in the space of just three months, shooting up 5.7% in April alone. In Quebec, the average home price rose by just 2.5% over the same period, remaining flat in April. Unlike in other provinces, Ontario in particular, Quebec's pool of property listings continues to grow, even if it remains relatively limited from a historical perspective. Weak sales recovery over the past few months has meant there hasn't been much upward pressure on prices.

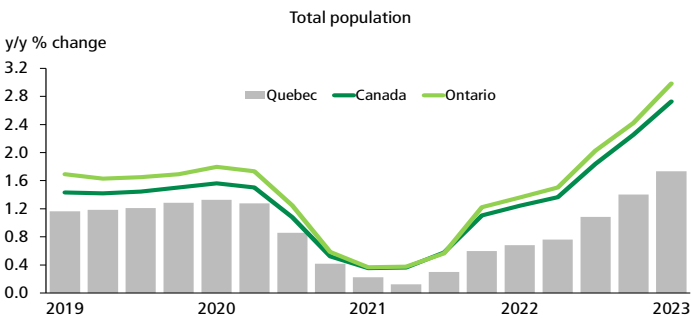
Quebec's 7.3% drop in average prices between spring 2022 and the beginning of 2023 was small compared to other regions (graph 2 on page 2). There are certain Canadian markets—Vancouver and Toronto, for instance—that have a history of more pronounced real estate cycles, which has a ricochet effect on the province as a whole. That's what's happening again here. A sharp uptick in population growth in some provinces (graph 3 on page 2), driven by immigration, has added fuel to the residential housing market. Despite a recent improvement, markedly slower growth in Quebec is tempering the recent rebound in activity.

GRAPH 2
Quebec Experienced a Smaller Correction, but Also a Smaller Recent Rebound



Sources: Canadian Real Estate Association and Desjardins Economic Studies

GRAPH 3
Slower Population Growth in Quebec Means Less Support for the Residential Real Estate Market



Sources: Statistics Canada and Desjardins Economic Studies

Still, this spring has been a particularly active one for the resale market—which comes as a surprise considering the two new federal restrictions in effect since January 1, 2023. A ban on real estate purchases by non-residents and tax penalties for house flipping, both described in our last [Spotlight on Housing](#), haven't stopped Canada's resale market from rebounding.

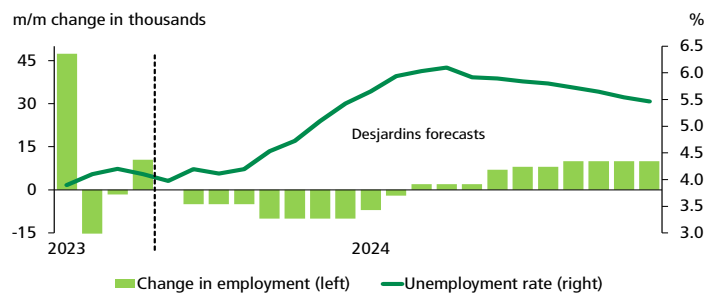
Do Home Prices Have Further to Fall?

While the initial wave of price corrections brought on by the steep interest rate hikes seems to be behind us, we could see the start of a second wave in the second half of 2023, on the back of expected deteriorations in the labour market. The economic slowdown in Quebec has already caused real GDP to level out somewhat in early 2023, with a contraction in the forecast for the coming months.

And it doesn't look like the labour market will come out unscathed. Even with unemployment at 4.1% in April, not far off the all-time low of 3.9%, there are signs of a slowdown. Employment insurance claims are trending up and job openings have fallen significantly from their summer 2022 peak. Quebec's employment figures have also been uneven the last few months, seesawing between gains and losses. We can expect a decline to set in as of mid-2023 as the effects of the recession start to

bite (graph 4). Unemployment is projected to reach about 6%, which will shake consumer confidence, particularly the residential housing market.

GRAPH 4
The Labour Market Will Suffer the Effects of a Moderate Recession

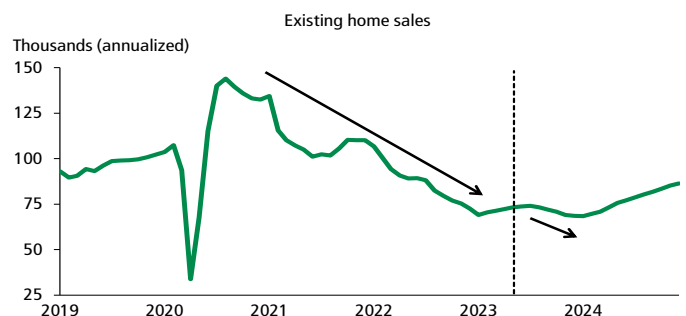


Sources: Statistics Canada and Desjardins Economic Studies

Although the resale market looks to be recovering somewhat after last year's downturn, it's only a matter of time before job losses have an effect. Housing demand is therefore expected to weaken in the second half of the year (graph 5) with supply continuing to grow. That should balance out the market, maybe even shifting momentum toward the buyer's side in Quebec.

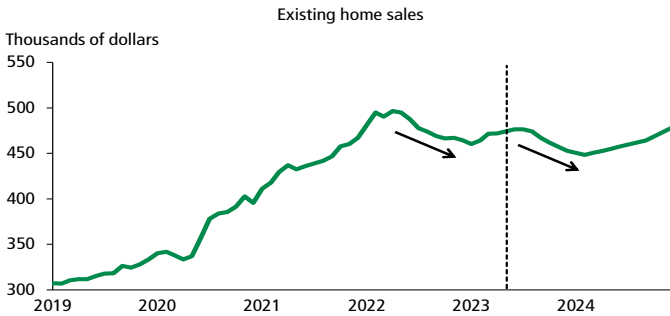
It should also bring average prices down by about 5% between Q3 2023 and Q1 2024, similar to what we saw last year (graph 6 on page 3). Between the two waves of corrections, we expect an overall 10% decrease in average prices between the February 2022 peak and an early 2024 trough. That won't bring them back to anywhere near their 2019 pre-pandemic level, however. Our previous scenario had forecast a 17% decline, with prices falling steadily through to the end of 2023. Although the outlook for the economy and the labour market is unchanged, we've adjusted our forecast to factor in the recent minor uptick in prices. We continue to predict a gradual recovery in the resale

GRAPH 5
A Sustained Recovery in Quebec Home Sales Isn't Expected Before 2024



Sources: Canadian Real Estate Association and Desjardins Economic Studies

GRAPH 6
Despite a Second Wave of Corrections, Prices Will Remain Well Above 2019 Levels



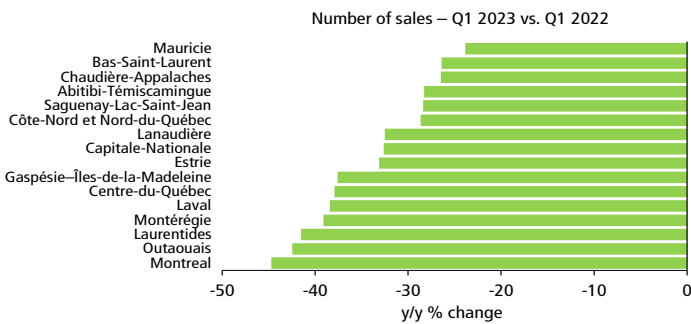
Sources: Canadian Real Estate Association and Desjardins Economic Studies

market in 2024, with interest rates set to come down, but not as low as they were during the pandemic.

Differing Regional Realities

Even though the past few months have seen a slight improvement in Quebec’s resale market, the year-over-year picture remains pretty bleak. At the regional level, existing home sales have continued to fall since last year, and it looks to be a province-wide phenomenon. The first quarter of 2023 saw bigger contractions than in 2022, with the outskirts of Montreal and the Outaouais region once again recording the most substantial declines, coming in at more than 40% (graph 7). Even though all administrative regions have recorded a drop of at least 20%, the ones least hard hit have been those with the most affordable markets, where mortgages tend to be smaller.

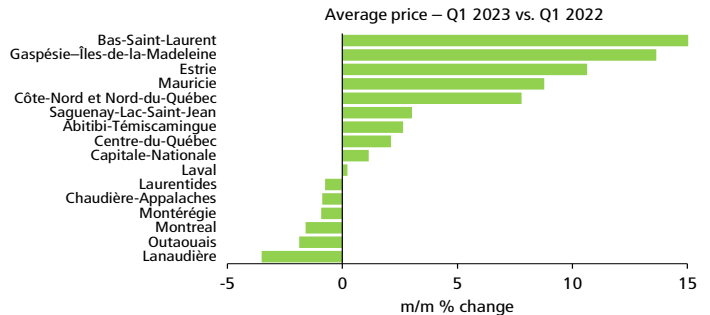
GRAPH 7
Existing Home Sales Continue to Fall All across Quebec



Sources: JLR Land Title Solutions (an Equifax company) and Desjardins Economic Studies

That means the higher interest rates have had less of an impact on the real estate market in some regions. There’s also been wide regional variation in average sale price fluctuations. Generally speaking, prices have fallen more steeply in markets where there’s been overbidding, particularly the Island of Montreal and the surrounding areas, as well as the Outaouais region (graph 8).

GRAPH 8
Average Home Prices on the Island of Montreal and in Many Surrounding Regions Were Down Early This Year



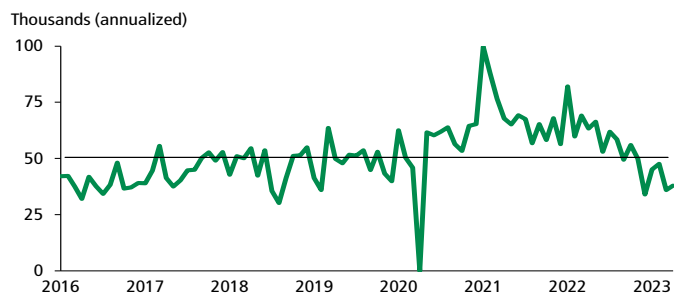
Sources: JLR Land Title Solutions (an Equifax company) and Desjardins Economic Studies

Average prices continue to climb, however, in regions of Quebec where buyers have mostly been spared from bidding wars. There hasn’t been a price correction in the province’s easternmost and northern regions, or in the Quebec City and central Quebec regions, which are still seeing prices rise compared to last year. That said, even though there have been a few holdouts so far, most regions are expected to record price declines this year. Deteriorating economic and labour market conditions will be fairly widespread across the province, which will impact the residential real estate market.

New Home Construction Is Falling More Sharply than Last Year Everywhere Except Trois-Rivières

On the new home construction front, it looks like things are going from bad to worse. New projects are down significantly across all market segments: single-family homes, condominiums and rental housing. The falloff in activity is province-wide, affecting most major and mid-sized urban centres. On an annualized basis, housing starts fell by nearly 35,000 units in March and April (graph 9). We haven’t seen two consecutive months of such lows since 2016. We’ve downgraded our forecast as a result of the weak activity observed since the start of 2023.

GRAPH 9
Housing Starts Are Now Well Under 50,000 Units



Sources: Canada Mortgage and Housing Corporation and Desjardins Economic Studies

TABLE 1
Housing Starts Are Down across Most of Quebec's Urban Centres

CMA	Homeowner units	Rental units	Condominium units	Total
	Q1 2022 to Q1 2023	Q1 2022 to Q1 2023	Q1 2022 to Q1 2023	Q1 2022 to Q1 2023
	% change	% change	% change	% change
Gatineau	-27	-39	0	-37
Montreal	-62	-41	-29	-41
Quebec City	-57	-51	***	-49
Saguenay	-68	-8	-100	-58
Sherbrooke	-64	-28	***	-38
Trois-Rivières	28	64	0	53
Population of 100,000+	-57	-41	-23	-41
Population of 50,000 to 99,999	-37	-49	-100	-56
Population of 10,000 to 49,999	-41	-11	0	-17

CMA: Census metropolitan area; *** : absolute value over 100%.

Sources: Canada Mortgage and Housing Corporation and Desjardins Economic Studies

After declining 15.8% in 2022, housing starts are now projected to fall another 30% this year.

Residential housing starts were down across all of Quebec's census metropolitan areas (CMAs) in Q1 2023, with the exception of Trois-Rivières (table 1). It's a CMA experiencing rapid population growth, and the development of its "Energy Transition Valley" has proven to be a boon for the entire region, attracting workers to move there. The economic upswing has meant a sharp rise in housing construction in Trois-Rivières and the surrounding areas.

Bigger Growth in Small Communities

After the new construction boom of the pandemic years, housing starts decreased less in smaller communities of between 10,000 and 50,000 inhabitants. They were down a total of 17% in Q1 2023 versus the same period in 2022. As a comparison, housing starts in major urban centres (100,000+ inhabitants) and mid-size centres (50,000 to 100,000 inhabitants) were down 41% and 56%, respectively. As the cost of building materials has stabilized and last year's supply issues have improved, small communities that had to delay projects are now gradually starting them up again. These regions also tend to have a larger inventory of available land, and at lower cost, which supports new builds. Just like with the resale market, the lower values of new properties in small communities have mitigated the impact of higher interest rates on monthly mortgage payments, which means fewer buyers are put off from taking the plunge.

Grim Conditions for the Rental Market

Last year's slump in rental housing starts has continued into 2023. Higher interest rates have changed the equation for many multi-unit housing projects, which have had to be amended, delayed or cancelled. In many cases, the down payment needed to finance a new build is now too high and the monthly loan payments too steep for many in the industry. That's on top of the high cost of land, materials and labour, all of which is exacerbating financing woes for many developers. Another cost factor is the decision by some cities to introduce

royalties to fund public infrastructure for new projects. Others, in contrast, have opted for the tax credit route, like the density bonus offered by Trois-Rivières. Rather than charge royalties on new housing, the city has introduced a property tax credit for new builds of 8 or more units with a density of at least 40 units per hectare. It's an example of how tax policy can be used to incentivize new rental housing projects and encourage density.

In summary, there are multiple factors currently weighing on new construction, and things will remain difficult until interest rates go down. Despite the desperate need for new rental housing, the creation of new stock is waning, putting increased pressure on rent prices. Given the strong demand from households that are no longer able to get on the property ladder and an increase in new renters, Quebec's vacancy rate is expected to fall to nearly 1% this year, down from 1.7% in 2022 (table 2 on page 5). While it's the rental housing segment that's borne the brunt of the drop-off in new construction, the housing crunch remains an issue in all regions across Quebec.

TABLE 2
Quebec housing market outlook 2023–2024

	2019	2020	2021	2022	2023f	2024f
New housing market						
New construction (\$B)	11.7	13.0	17.6	16.4	11.5	13.4
Year-over-year change (%)	-1.9	10.7	35.4	-7.1	-29.7	16.5
Housing starts	47,967	54,066	67,810	57,107	40,700	47,000
Year-over-year change (%)	2.3	12.7	25.4	-15.8	-28.7	15.5
Houses	13,742	15,995	21,091	16,825	11,500	13,000
Year-over-year change (%)	-8.2	16.4	31.9	-20.2	-31.6	13.0
Single-detached	8,989	10,861	14,826.0	---	---	---
Year-over-year change (%)	-10.6	20.8	36.5	---	---	---
Semi-detached	2,966	3,514	4,175.0	---	---	---
Year-over-year change (%)	-1.0	18.5	18.8	---	---	---
Row housing units	1,787	1,620	2,090.0	---	---	---
Year-over-year change (%)	-6.6	-9.3	29.0	---	---	---
Apartments	34,225	38,071	46,719	40,282	29,200	37,000
Year-over-year change (%)	7.3	11.2	22.7	-13.8	-27.5	26.7
Condos ¹	8,172	7,222	8,032	6,913	5,500	6,500
Year-over-year change (%)	-17.1	-11.6	11.2	-13.9	-20.4	18.2
Rentals ¹	24,861	28,709	35,659	31,123	23,000	27,500
Year-over-year change (%)	21.3	15.5	24.2	-12.7	-26.1	19.6
Conventional rentals ²	21,536	26,554	33,049	30,078	22,000	26,500
Year-over-year change (%)	28.6	23.3	24.5	-9.0	-26.9	20.5
Retirement homes ²	3,159	2,017	2,567	980	1,000	1,000
Year-over-year change (%)	-11.4	-36.2	27.3	-61.8	2.0	0.0
Resale market						
Unit sales	96,349	112,159	109,467	87,112	71,475	77,550
Year-over-year change (%)	11.4	16.4	-2.4	-20.4	-18.0	8.5
Weighted average price (\$k)	324	377	438	484	467	460
Year-over-year change (%)	5.2	16.4	16.4	10.3	-3.4	-1.6
Sales volume (\$B)	30.4	40.0	46.3	40.5	33.4	35.7
Year-over-year change (%)	15.5	31.5	15.8	-12.7	-17.5	6.8
Other indicators						
Vacancy rate for rental units ³ (%)	1.8	2.4	2.5	1.7	1.2	1.0
Average rent ³ (\$)	800	845	874	952	1,050	1,125
Year-over-year change (%)	5.1	5.6	3.4	8.9	10.3	7.1
Renovation spending ⁴ (\$B)	14.2	14.4	19.2	23.2	20.5	21.5
Year-over-year change (%)	3.9	1.3	33.1	21.2	-11.7	4.9

f: forecasts; ¹ Urban centres with populations of 10,000 or more, the total is slightly below the total for provincial apartments shown above; ² Included in rental units;

³ Three units or more, biannual survey conducted in the fall; ⁴ Maintenance and repair expenditures are excluded.

Sources: Canada Mortgage and Housing Corporation, Canadian Real Estate Association, Statistics Canada and Desjardins Economic Studies