

SPOTLIGHT ON HOUSING

New Construction in Quebec and Ontario Is Going at Full Tilt

After finishing 2020 on a strong note, residential housing starts in Quebec shattered an all-time record in January. Construction has been so active since then that forecasts were revised sharply upward in March. The context is also very favourable in Ontario, which is also experiencing sustained demand. In 2020, a number of factors gave numerous buyers some financial leeway, including lower mortgage rates, strong household income growth and low consumer spending. These temporary factors should subside in 2021, diminishing even further in 2022. The post-pandemic period will therefore reduce the pressure on new construction, especially single-family homes.

Soaring Housing Starts

Residential housing starts began 2021 at an exceptionally high level in Quebec. The particularly mild winter and builders' fears of restrictions like in spring 2020, namely the temporary shutdown of construction sites for a few weeks to contain the second wave, likely led to the acceleration of a number of projects.

In addition, despite the very strong activity in January and February, many contractors already have their order books full for the coming months. Forecasts for 2021 were therefore revised upward with 60,000 housing starts in Quebec. This is more than a 10% increase for a second year in a row and the highest level since the end of the 1980s (graph 1). In Ontario, new construction is also promising to be more sustained this year with 83,700 housing starts, a 3.0% increase from 2020.

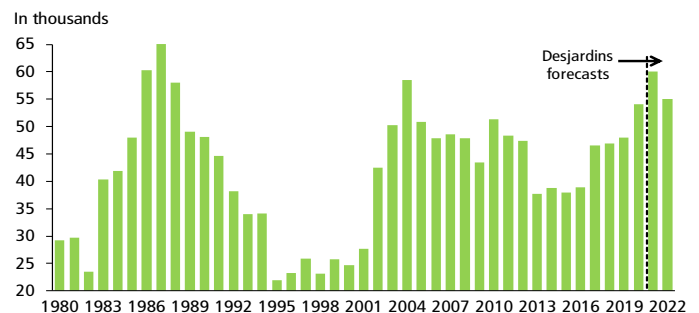
Homes Dominate Growth

Residential construction this year will be stimulated primarily by single-family homes. In January and February already, this type of housing starts nearly doubled compared to the same period last year (centres of 10,000 inhabitants or more). Growth will therefore be accelerated in 2021 (graph 2). This market segment is expected to slow in 2022, however, as the post-pandemic era will bring the pendulum swinging back to some extent in favour of housing that is more affordable and closer to urban centres.

For the time being, many trends continue to drive demand for new homes.

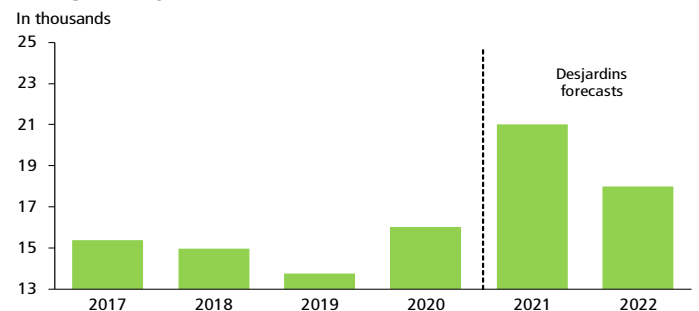
1. The steady decline in the number of properties for sale on the current market, particularly in Quebec and Ontario, is steering many buyers to construction. In the two provinces, the sales

GRAPH 1
Housing starts: record high in Quebec



Sources: Canada Mortgage and Housing Corporation and Desjardins, Economic Studies

GRAPH 2
Housing starts for single-family homes in Quebec will be even stronger this year



Sources: Canada Mortgage and Housing Corporation and Desjardins, Economic Studies

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NOTE TO READERS: The letters k, M and B are used in texts and tables to refer to thousands, millions and billions respectively.

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mandate of real estate agents and brokers are insufficient to meet demand. As a result, existing home sales have been stabilizing in Quebec over the past few months and dropping in a number of markets in Ontario. Many buyers are therefore looking at new homes. The resale market will be analyzed in depth in the next edition of Spotlight on Housing this spring.

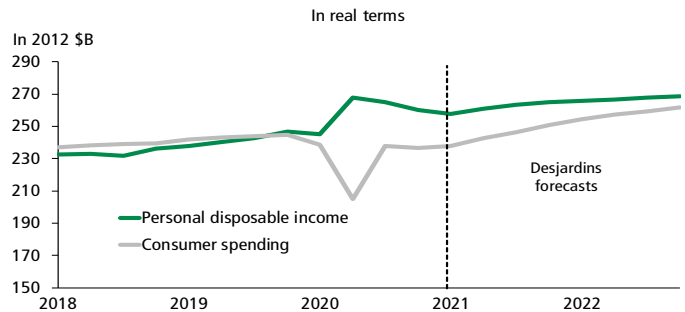
2. Migration outside major centres, which has accelerated with the pandemic. Telework reduces travel constraints and increases the need for space. Greater availability of land at lower prices than in major metropolitan areas is also behind the boom in home construction.
3. Overall, households' financial situation has improved since the beginning of the health crisis. After-tax income growth has been significantly higher than consumption growth for the past year (graph 3). Some expenses are still low, such as restaurant meals, travel and entertainment, freeing up large sums for savings or real estate investments. For many households, the purchase of a new home would not have been possible with the usual pace of spending.
4. Low mortgage rates, which declined significantly at the start of the crisis. Variable mortgage rates plunged 150 basis points in March 2020 and have stayed low since then. This is due to the reduction in key rates by the Bank of Canada, which announced a status quo until 2023. Fixed mortgage rates were also down until very recently.

Under such circumstances, the quickly rising prices of detached homes are not curbing demand yet. As soon as the uncertainty surrounding the pandemic eases and social distancing measures are loosened, leisure spending should return to normal. Less money will therefore be available for residential real estate, and single-family homes should be less popular.

The rise in fixed mortgage rates will also have a chilling effect, especially as of next year. The upswing in medium- and long-term federal bond yields over the past few weeks (graph 4) is beginning to put upward pressure on promotional fixed rates. The movement should continue gradually, which will drive monthly payments for new mortgages higher.

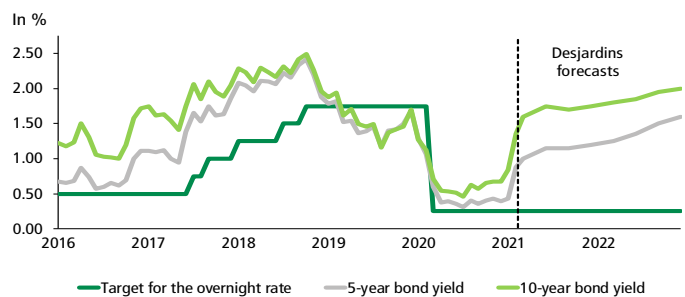
Lastly, skyrocketing material prices are adding costs to new homes, which will end up cooling home buyers' heels (box on page 3). The 5% minimum down payment is also becoming more difficult for first-time home buyers to save. Condos, which are less expensive, could potentially become the preferred option.

GRAPH 3
The gap between after-tax income and consumption gave Quebecers some financial leeway



Sources: Institut de la statistique du Québec and Desjardins, Economic Studies

GRAPH 4
Canadian long-term interest rates are moving away from their lows



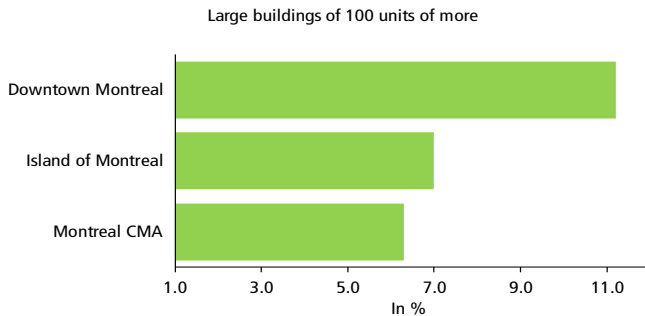
Sources: Datastream and Desjardins, Economic Studies

Rental Apartments and Condos

Rental apartments and condos in central neighbourhoods on the Island of Montreal and in downtown Toronto and Ottawa have been abandoned since the start of the pandemic. The population's migration out of major centres, which has accelerated, and the decline in international immigration helped free up apartments in central neighbourhoods.

The rental vacancy rate jumped in downtown Montreal, Toronto and Ottawa, particularly in high-rise buildings (graph 5 on page 3). The number of condos for sale or rent has multiplied. Facing a lack of occupants, investors put some buildings up for sale and urban dwellers tried to get rid of their apartments. In smaller markets, however, the share of apartments for rent has remained fairly low (graph 6 on page 3).

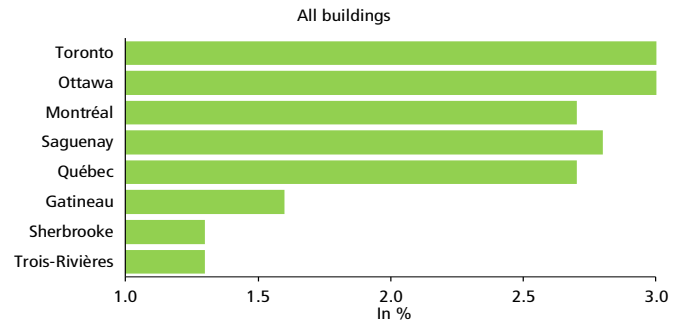
GRAPH 5
Vacancy rate in large rental buildings higher in 2020



CMA: census metropolitan area
Sources: Canada Mortgage and Housing Corporation and Desjardins, Economic Studies

Local and international students' eventual return to classes on university campuses and the influx of foreign workers should help the rental market recover gradually. The market segments that suffered during the pandemic will surely experience renewed interest when the effects dissipate. In addition, some households that moved away from major centres during the pandemic will likely reposition themselves with a return to the workplace, even if it is part time.

GRAPH 6
Rental apartment vacancy rate by CMA in 2020



CMA: census metropolitan area
Sources: Canada Mortgage and Housing Corporation and Desjardins, Economic Studies

Despite these temporary difficulties, new apartment construction has been strong in Montreal since the beginning of the year. January and February saw housing starts for over 3,000 rental units, more than a 30% increase from the same period last year. Construction of approximately 2,000 condos has begun, more than double the number in January and February 2020. Elsewhere in Quebec, condo housing starts were virtually non-existent. Rental housing starts were down significantly in all metropolitan areas, except in Montreal and Quebec, which saw a sharp increase.

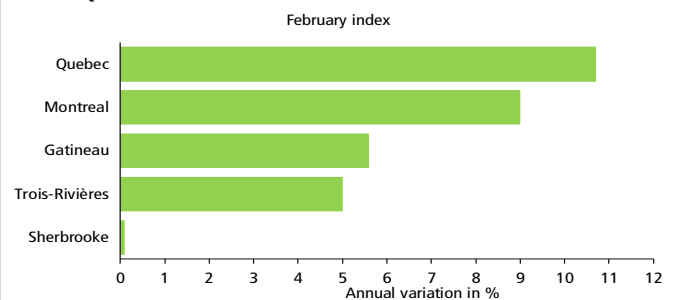
BOX
New home prices skyrocket

New home prices have continued to rise across the country, hitting the highest monthly increase in three decades in February. Annual growth in Canada is 7.0% and is even nearing 10% in some major metropolitan areas of Quebec and Ontario. The sharpest increase in new home prices was seen in Kitchener-Cambridge-Waterloo (+16.0%) and Ottawa (+15.0%) in February. The metropolitan areas of Quebec (+10.7%) and Montreal (+9.0%) stand out as well. Outside of these major centres, however, prices are not climbing as quickly (graph 7).

The rising costs are being driven by strong North American demand and low building material inventories since the start of the pandemic. The strength of new construction and renovations notably drove up lumber prices, which are expected to remain high for several more months.

In the space of a few weeks, the cost of building a home sometimes increases several tens of thousands of dollars. Some builders are protecting themselves with a specific clause in sales contracts stating that the buyer is responsible for covering any overages. Other developers are absorbing the additional costs, which erodes their profit margins almost entirely. However, some builders are imposing an additional delivery charge, even though there are no legal provisions for this. Buyers will often pay an additional amount to avoid a legal battle and move into their new home as planned. The borrowed amount will be higher than initially planned. Those who had already reached their debt limit risk abandoning their purchase plan.

GRAPH 7
The rise in new home prices over the past year differs depending on the Quebec CMA

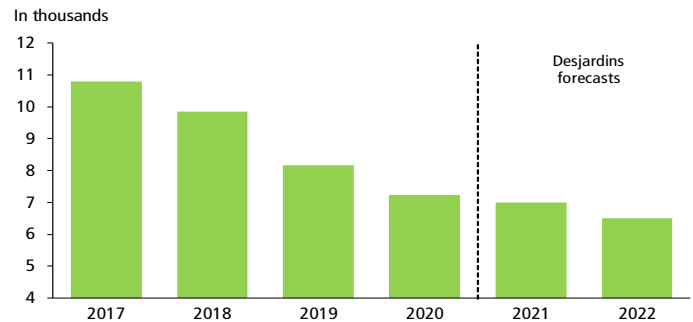


CMA: census metropolitan area
Sources: Statistics Canada and Desjardins, Economic Studies

It would be surprising for apartment construction to maintain such a high pace throughout the year. Condo housing starts have been down for a number of years, and the trend is expected to continue in 2021 (graph 8). The conventional rental segment, which has seen strong growth over the past few years, was expected to go through an adjustment period, in theory. Astonishingly, new construction does not appear to be slowing in Montreal. International immigration may take several years to catch up, however, and the eventual return of the people who moved to the outskirts of major centres is far from a sure thing. The forecasts for rental housing starts are nevertheless not negative like before, and the level will be relatively high from a historical standpoint (graph 9). Home construction will be the one to post the liveliest growth this year, but the trend could be reversed as of 2022 (table on page 5).

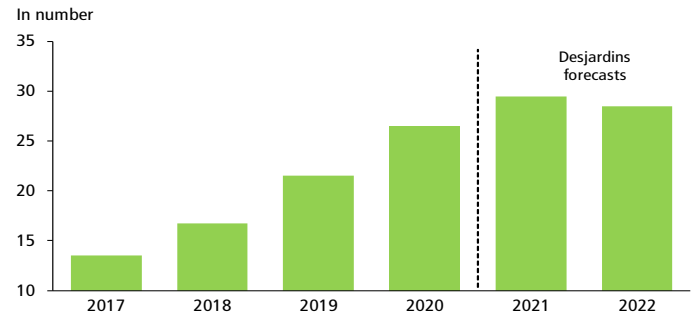
Hélène Bégin, Senior Economist

GRAPH 8
Condo housing starts in Quebec: the decline continues



Sources: Canada Mortgage and Housing Corporation and Desjardins, Economic Studies

GRAPH 9
Housing starts for conventional rental apartments: numbers will remain fairly high in Quebec



Sources: Canada Mortgage and Housing Corporation and Desjardins, Economic Studies

TABLE
Quebec housing market outlook 2021–2022

	2018	2019	2020	2021f	2022f
New housing market					
New construction (\$B)	12.0	11.7	12.7	13.8	13.0
Annual variation (%)	16.1	-1.9	7.8	8.9	-5.8
Housing starts	46,874	47,967	54,066	60,000	55,000
Annual variation (%)	0.8	2.3	12.7	11.0	-8.3
House	14,968	13,742	15,995	21,000	18,000
Annual variation (%)	-2.6	-8.2	16.4	31.3	-14.3
Single-detached	10,060	8,989	10,861	---	---
Annual variation (%)	-6.1	-10.6	20.8	---	---
Semi-detached	2,995	2,966	3,514	---	---
Annual variation (%)	6.2	-1.0	18.5	---	---
Row housing unit	1,913	1,787	1,620	---	---
Annual variation (%)	4.3	-6.6	-9.3	---	---
Apartment	31,906	34,225	38,071	39,000	37,000
Annual variation (%)	2.5	7.3	11.2	2.4	-5.1
Condo ¹	9,860	8,172	7,222	7,000	6,500
Annual variation (%)	-8.7	-17.1	-11.6	-3.1	-7.1
Rental ¹	20,503	24,861	28,709	29,500	28,500
Annual variation (%)	6.5	21.3	15.5	2.8	-3.4
Conventional rental ²	16,752	21,536	26,554	27,500	26,300
Annual variation (%)	24.0	28.6	23.3	3.6	-4.4
Retirement home ²	3,565	3,159	2,017	2,000	2,200
Annual variation (%)	-35.4	-11.4	-36.2	-0.8	10.0
Resale market					
Unit sales	86,451	96,636	112,971	118,590	110,000
Annual variation (%)	4.7	11.8	16.9	5.0	-7.2
Weighted average price (\$k)	308	324	377	450	460
Annual variation (%)	5.2	5.2	16.5	19.4	2.2
Sales volume (\$B)	26.3	30.5	42.6	53.4	50.6
Annual variation (%)	9.1	15.8	39.7	25.4	-5.2
Other indicators					
Vacancy rate for rental units ³ (%)	2.3	1.8	2.5	3.2	3.5
Average rent ³ (\$)	761	800	844	865	890
Annual variation (%)	3.4	5.1	5.5	2.5	2.9
Renovation spending ⁴ (\$B)	13.7	14.2	12.4	14.3	14.8
Annual variation (%)	6.0	3.9	-13.0	15.6	3.5

f: forecasts; ¹ Urban centres with populations of 10,000 and over, the total is slightly below the total for provincial apartments shown above; ² Included in rental units; ³ Three units or more, biannual survey of 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