

ECONOMIC VIEWPOINT



Quebec: Consequences of Demographic Change for the Real Estate Market

In the Long Term, Where Will Prices Head in the Different Regions?

Over a long period, housing prices are largely influenced by demographic factors. Unfavourable trends will intensify in the next few years in several parts of Quebec. A university study¹ carried out in partnership with Desjardins Group's Economic Studies assessed their impacts. Long-term projections were established to discern how average property prices will evolve in real terms. The specific results for each of the province's regions are presented over about a 15-year horizon, along with the explanatory factors. Generally speaking, we are initially expecting prices to dip in real terms over several years. The magnitude and length of the decline periods vary among the regions, but the differences are not large. The downside movement will be followed by an upswing that will allow most regions to recoup the lost ground. Nominally—that is, without excluding inflation—in most regions, average prices will continue to rise over the long term, but at a much slower pace than in 2018.

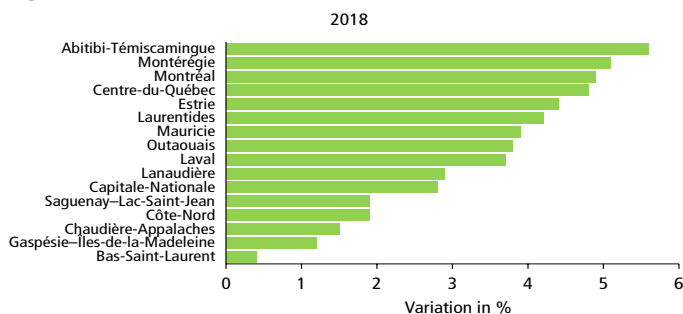
The Past Is No Indication of the Future

The resale market had an exceptional year in 2018 thanks to a very good economic situation in most parts of the province. The number of existing properties sold hit a historic peak, and average price growth accelerated to 5.2% on a nominal basis province-wide. Even once we remove Quebec's 1.7% annual inflation, average prices still increased more than 3% in real

terms in 2018. Growth was fairly widespread in both nominal and real terms, that is, the price change that excludes inflation, in the different regions (graphs 1 and 2).

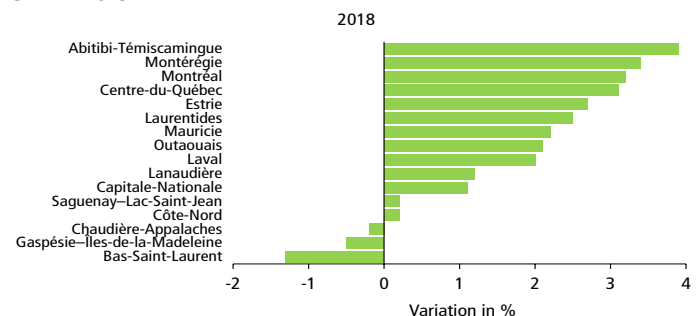
Several factors stimulated the housing market in 2018. Firstly, the provincial unemployment rate was a very low 5.5% last year; indeed, it was under 6% in nearly all regions. Then there was

GRAPH 1
Average property prices in nominal terms: increase in all Quebec regions



Sources: Quebec Federation of Real Estate Boards via Centris® and Desjardins, Economic Studies

GRAPH 2
Average property prices in real terms: the picture by region is generally good



Sources: Quebec Federation of Real Estate Boards via Centris®, Statistics Canada and Desjardins, Economic Studies

¹ Josué DESBIENS, *Impact des changements démographiques sur le marché immobilier québécois*, Master of economics thesis, Université Laval, 2018, 62 p.

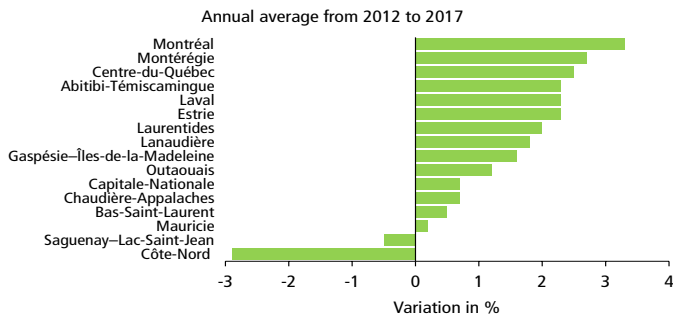
better net migration in the metropolitan areas, as well as outside the major centres, thanks to heightened recruiting of foreign workers in the context of a labour shortage. Lastly, the rental housing market firmed up, with a vacancy rate below 3.0% in nearly all Quebec regions, putting pressure on demand and prices for other types of housing.

Eager buyers combined with a drop in the number of properties on the market even triggered some overheating in the Montreal market. In addition, instances of bidding proliferated in 2018. In fact, in about 10% of cases in Montreal, and more in some neighbourhoods, the sale price was higher than the listed price.² The real estate cycle is well ahead of the rest of the province.

Although 2018 stands out for its widespread price growth, it will not always be this way. Activity was weaker in the five previous years, from 2012 to 2017, even though the Quebec economy's growth cycle was well underway and the province's unemployment rate was around 7.5% on average from 2012 to 2017, which is relatively low. Some regions saw average prices drop during this period, several regions posted increases, and the Island of Montreal posted the strongest growth (graphs 3 and 4). Each of Quebec's regions has its own specific economic situation and local demographic. Regional real estate markets therefore have different dynamics during certain periods. Several factors influence property purchases, particularly, the evolution of households' disposable income, interest rate levels, and mortgage credit conditions.³

In terms of supply, i.e., the number of units available, new construction plays an important role. In short, a variety of factors dictate how housing prices evolve.

GRAPH 3
Average property prices in nominal terms: five years of more subdued growth than in the past

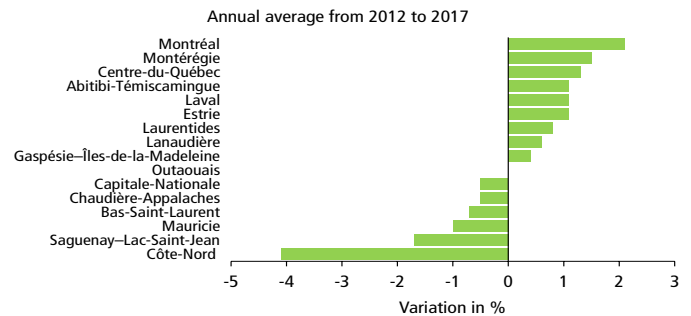


Sources: Quebec Federation of Real Estate Boards via Centris® and Desjardins, Economic Studies

² *A Growing Number of Properties Are Selling Above the Asking Price*, Québec Federation of Real Estate Boards, *A Word from the Economist*, May 2018, 6 p.

³ Lawrence SCHEMBRI, *The Long-Term Evolution of House Prices: An International Perspective*, Bank of Canada, remarks made to the Canadian Association for Business Economics, Kingston, August 25, 2015, 19 p.

GRAPH 4
Average property prices in real terms: five years not as favourable as 2018



Sources: Quebec Federation of Real Estate Boards via Centris®, Statistics Canada and Desjardins, Economic Studies

Beyond short-term fluctuations, movement by average prices is largely dependent on demographics, as shown by the results of a university study that looked specifically at this issue. Regional disparities have been visible for several years, and the dynamic will also be different over the longer term.

STUDY HIGHLIGHTS

Demographics

- ▶ Regional demographic trends have a big impact on the forecast evolution of residential real estate prices over the next 10 to 15 years.
- ▶ Long-term price variations differ across Quebec's administrative regions.
- ▶ To various degrees, population movements (migration) and natural growth (births minus deaths) both affect long-term regional home price projections.
- ▶ The population's age make-up also has a substantial impact on price growth, particularly the proportion of 25- to 54-year-olds (positive impact) and proportion of people aged 65 or older (negative effect).
- ▶ Of the demographic variables, migration has the biggest influence on long-term price adjustment.

Incomes

- ▶ Beyond demographics, the variation in real income per capita by administrative region is also critical to the change in housing prices.
- ▶ The evolution of real income per capita income makes it possible to better pinpoint the economic conditions in different regions according to each region's industrial structure.
- ▶ The change in per capita disposable income in each region has a different impact on prices.

- ▶ A change in income has a different impact on real estate prices in rural and urban areas. Population density affects price sensitivity, which is stronger in the Quebec and Montreal areas, for example.

Other Factors

- ▶ In addition to demographics, per capita income and population density, other elements also influence the price trajectory, such as mortgage interest rates and homebuilding. The projections take all these factors into account.
- ▶ Of the numerous factors identified, migration has the biggest influence on the long-term price adjustment regionally speaking.

Projection Assumptions

- ▶ The increase in per capita disposable income in each of Quebec’s regions is the average pace for the last 10 years.
- ▶ Regional housing starts remain stable at the average for the last 10 years.
- ▶ Inflation is set at 2.0% per year for each administrative region.

Data Sources

- ▶ The historic demographic data and projections used come from the Institut de la statistique du Québec.
- ▶ Net migration, natural growth and the population of the two age groups (25 to 54 years and 65 and older) are the demographic indicators used. They are all expressed as a percentage of the population of each region.
- ▶ Net migration for each region corresponds to the balance of arrivals and departures of individuals from and to the province’s regions, the rest of Canada, and the rest of the world.
- ▶ Natural population growth is the number of births minus the number of deaths on a regional basis.
- ▶ A partnership between Desjardins, Economic Studies and Université Laval’s department of economics made it possible to complete this research project, in the form of a master’s thesis by Josué Desbiens, under the supervision of Associate Professor Kevin Moran. The long-term projections established and analysis of all the results are drawn from this research.

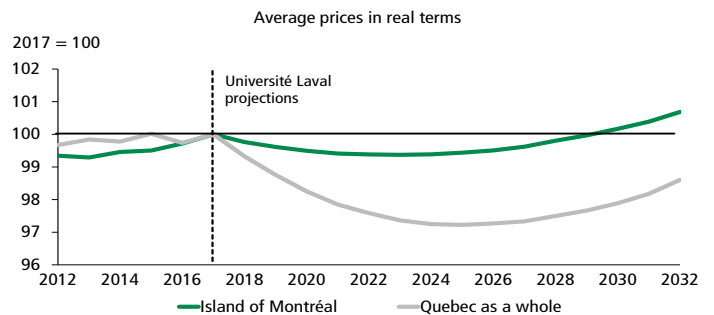
Limitation on Interpreting Results

- ▶ In some Quebec administrative regions, the history for some of the data required to calculate long-term projections is insufficiently extensive. These regions are Bas-Saint-Laurent, Gaspésie–Îles-de-la-Madeleine and Centre-du-Québec.
- ▶ Some of the regions’ missing data was replaced with provincial data and incorporated into the rest of the available data, making it possible to identify a fairly reliable trend for future price evolution.

Regional Results

- ▶ Quebec as a whole: the average price in real terms should fall by about 3% over the next 10 years or so. After that, prices are expected to improve slowly.
- ▶ The magnitude and length of the decline periods vary among the regions, but the differences are not large. The decrease projected over several years is less than 3.5% in each region.
- ▶ Island of Montreal: better demographic trends than those of the province will restrict the decline by average price in real terms (graph 5).

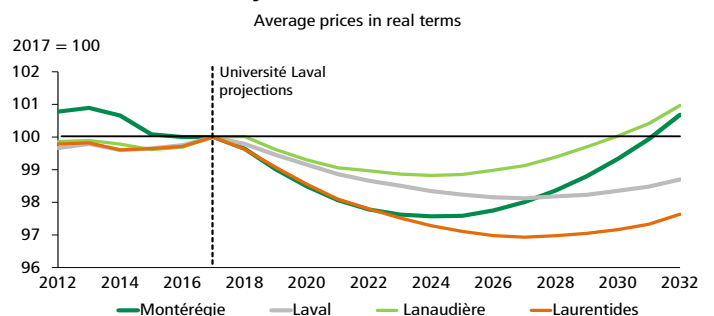
GRAPH 5
Montréal area: better demographics on the island will keep home prices from pulling back sharply



Sources: Université Laval’s department of economics and Desjardins, Economic Studies

- ▶ The Island of Montreal differs from the other administrative regions. Several factors explain the distinction: faster total population growth, net positive migration, and slower population ageing than in the rest of the province.
- ▶ The regions surrounding the Island of Montreal (graph 6) should see average prices in real terms drop for several years, then turn around. Lanaudière and Montérégie will recoup all of the ground lost within about 15 years. The Laval and Laurentides regions will see prices edge up just slightly in about 10 years.

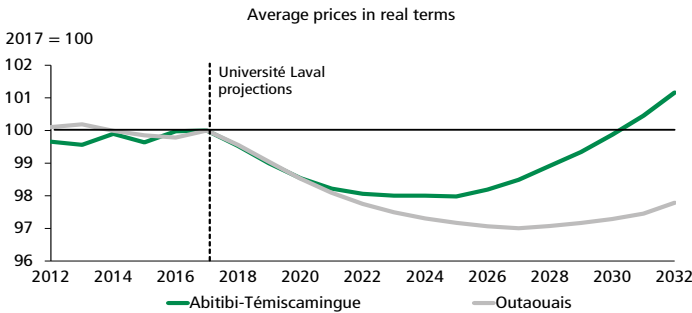
GRAPH 6
Regions around Montréal: a slight decline by home prices will be unavoidable for a few years



Sources: Université Laval’s department of economics and Desjardins, Economic Studies

- ▶ Regions in western Quebec: the Outaouais and Abitibi-Témiscamingue regions will see similar pullbacks by average prices in real terms (graph 7). However, Abitibi-Témiscamingue is projected to see a full recovery within about 15 years. Outaouais will not manage to come back over the long term.

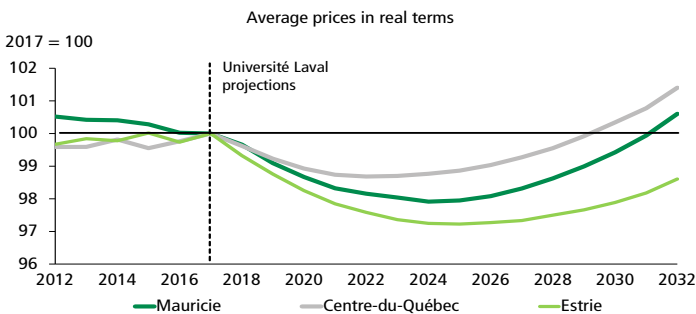
GRAPH 7
Regions in western Quebec: home prices will rise more quickly in Abitibi than Outaouais



Sources: Université Laval's department of economics and Desjardins, Economic Studies

- ▶ Central regions of Quebec: average prices in real terms will rise after pulling back for a period (graph 8). In Mauricie, the rapid rise in the number of elderly and slowing natural population growth will be only partially offset by net positive migration and an increase in the population. In Estrie, the results are more negative due to less favourable migration than in Mauricie. In real terms, prices will pull back for a shorter period in Centre-du-Québec.

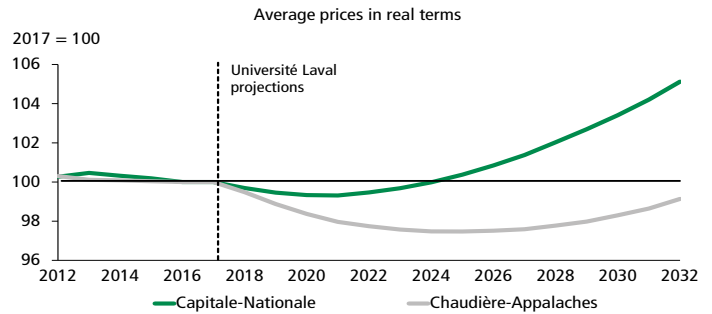
GRAPH 8
Central regions of Quebec: home prices will rise after pulling back for a period



Sources: Université Laval's department of economics and Desjardins, Economic Studies

- ▶ Regions in eastern central Quebec: two regions have already been seeing stable average prices in real terms for several years. The Capitale-Nationale region should return to an uptrend shortly. The Chaudière-Appalaches region should see several years of extended weakness (graph 9).

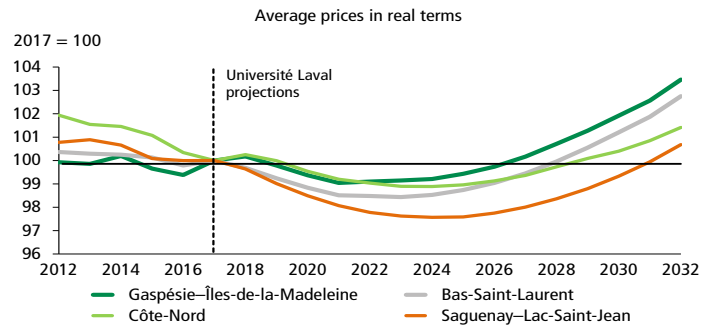
GRAPH 9
Regions in central-eastern Quebec: the period of home price stability is ending



Sources: Université Laval's department of economics and Desjardins, Economic Studies

- ▶ Regions in eastern Quebec: average prices in real terms will slide slightly for several years before coming up (graph 10).

GRAPH 10
Regions in eastern Quebec: several years of slight declines in home prices, rising after that



Sources: Université Laval's department of economics and Desjardins, Economic Studies

- ▶ Côte-Nord and Gaspésie-Îles-de-la-Madeleine are the only two Quebec regions where total population is declining and net migration is almost zero.
- ▶ In Bas-Saint-Laurent, the decline by prices in real terms will be unavoidable in the coming years, but modest. The total population will increase over the long-term horizon.
- ▶ In Saguenay-Lac-Saint-Jean, average prices in real terms have fallen in recent years, and should keep edging down until 2023. After that, net positive migration and population growth will foster a period of recovery.

Conclusion: An Adjustment Period Is Coming

Beyond the fairly widespread rise by home prices in 2018, the longer-term trends do not promise to be as favourable. In each of Quebec's regions, demographic factors will have an influence on the evolution of average prices in real terms in about the next 15 years. Generally, a slight pullback lasting several years is initially expected in each region. This period of decline will be

followed by an upswing that will allow most regions to recoup the lost ground.

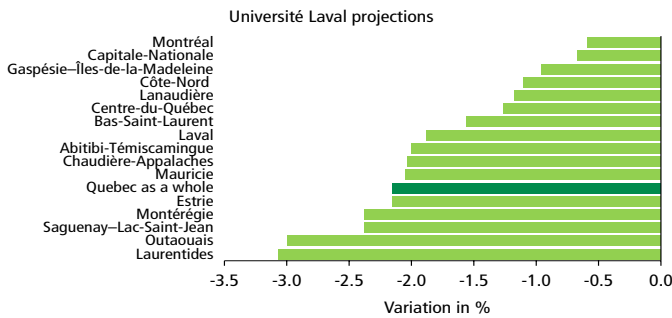
For Quebec as a whole, the average price in real terms should fall by about 3% over roughly 10 years, with a slow improvement projected subsequently. The magnitude and length of the decline periods vary among the regions, but the differences are not large. The decrease projected over several years is less than 3.5% in each of the administrative regions analyzed. This is a fairly small adjustment that will occur over a long period following the strong price growth of the last 20 years.

According to university research results, no region will see prices fall in real terms, but they will retreat a little in several parts of the province. The small looming pullback, staggered over a long horizon, does not really represent a major upheaval. According to the projections established, all administrative regions will see average prices in real terms decline for a time (graph 11).

rest of Quebec. Several factors explain the distinction: faster total population growth, net positive migration, and slower population ageing in Montreal than in the rest of the province.

The price adjustment will be slight compared with the adjustment seen in the 1990s, when Quebec’s real estate market went through a tough period, due to high interest rates and to the fact that the recession drove the unemployment rate up. On a nominal basis, prices declined slightly, but real terms they went through a long correction period (graph 12). Prices in real terms were even stagnant for a brief period a few years ago. The long-term projections presented here do not take into consideration the end of the economic cycle and potential recession that could occur between 2020 and 2025. The U.S. economy’s expansion cycle, which is poised to hit a record for longevity, could end soon. An economic slowdown or even contraction would take Canada and Quebec along in its wake, and could trigger a sharp correction by home prices in several parts of the province.

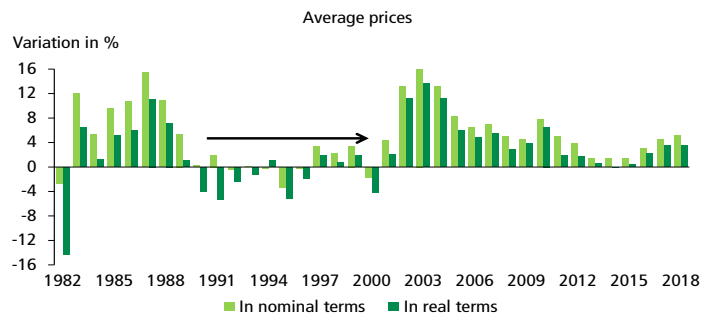
GRAPH 11
Average property prices in real terms: a decline spread over several years until prices bottom out in each region



Sources: Université Laval’s department of economics and Desjardins, Economic Studies

Prices will not bottom out in the same year in each of Quebec’s regions (table 1). The forecast decline is short in some areas, and longer in others. With more positive long-term demographic trends, the Island of Montreal will be much less affected than the

GRAPH 12
Quebec’s housing market went through a tough period in the 1990s



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

A distinction is required here: the results of the price changes are all expressed in real terms, that is, the change in prices that excludes projected annual inflation of 2.0% for the projection horizon. The change in real terms corresponds to the net change in the value of properties. This is a good indicator for assessing the increase in a household’s real estate assets, i.e., the increase in the real value of the wealth associated with a home.

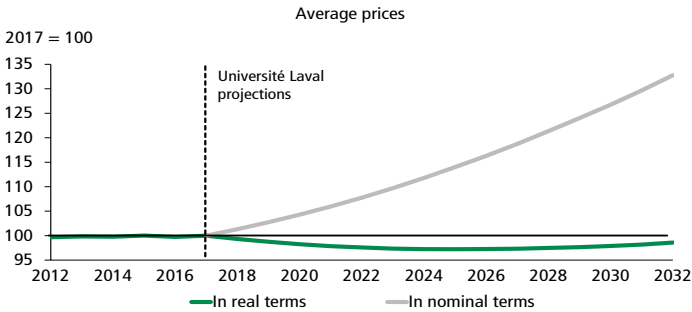
TABLE 1
Average property prices in real terms: which year will each region hit bottom?

BOTTOM	NUMBER OF REGIONS	NAME OF REGION
2020	1	Capitale-Nationale
2021	3	Centre-du-Québec, Montréal, Gaspésie-Îles-de-la-Madeleine
2023	5	Abitibi-Témiscamingue, Bas-Saint-Laurent, Côte-Nord, Montérégie, Saguenay-Lac-Saint-Jean
2024	3	Chaudière-Appalaches, Estrie, Lanaudière
2025	1	Mauricie
2027	3	Laval, Laurentides, Outaouais

Sources: Université Laval’s department of economics and Desjardins, Economic Studies

If the price projection had been done on a nominal basis, the results would have been more positive in each of Quebec’s regions. Provincially, the projection horizon would be characterized by a slight increase in average prices (graphs 13 and 14 on page 6). With this approach, the mortgage credit awarded, based on the purchase of the property, would continue to rise. However, the pace would be slower than it was in the past. Demographics would have an impact by limiting growth by business volume without triggering an extended downturn.

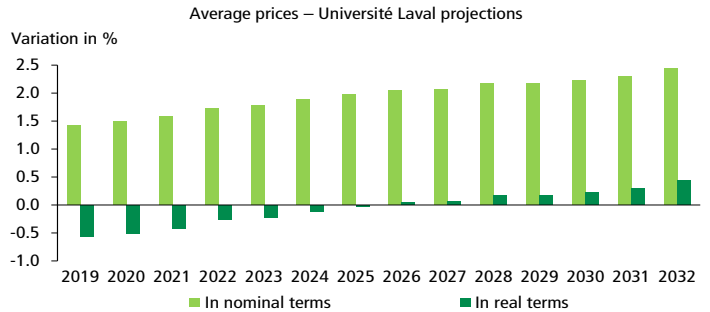
GRAPH 13
Quebec as a whole: based on the projections, prices will drop in real terms and keep rising in nominal terms



Sources: Université Laval's department of economics and Desjardins, Economic Studies

A decrease could nevertheless occur for a short period due to an unexpected economic reversal, but should not persist for many years. This study reveals long-term trends and does not aim to predict short-term fluctuations in average home prices. Note that demographics will lead to a period of gradual adjustment without triggering a brutal price drop in Québec's different regions.

GRAPH 14
Quebec as a whole: based on the projections, prices will drop in real terms and keep rising in nominal terms



Sources: Université Laval's department of economics and Desjardins, Economic Studies

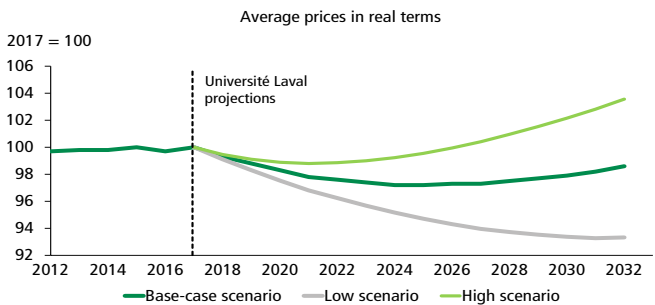
Hélène Bégin, Senior Economist

With the collaboration of Josué Desbiens, a student at Université Laval and author of the master's thesis on the subject. Kevin Moran, an associate professor in Université Laval's department of economics, made a significant contribution to the project's success, thanks to his supervision of the research (box).

BOX
Université Laval projection scenario

The research results presented in this document come from the base-case scenario, which calls for average prices in real terms to dip by about 3% over a 10-year period province-wide. The trajectory could be slightly different based on the other two scenarios, which make it possible to establish a forecast range based on the trend's standard deviation (graph 15). In the low scenario, average prices in real terms would drop by about 6.5%, bottoming out in 2031. In the high scenario, the decrease would be around 1%, with the bottom reached in 2021. Long-term projections include some uncertainty, and the narrow forecast range indicates a fairly small risk of error at the provincial level (table 2).

GRAPH 15
Quebec as a whole: according to the three projection scenarios, prices will dip within a fairly limited range



Sources: Université Laval's department of economics and Desjardins, Economic Studies

TABLE 2
Quebec as a whole: summary of projections for average property prices according to three scenarios

PERIOD	PRICE LOW SCENARIO		PRICE BASE CASE SCENARIO		PRICE HIGH SCENARIO	
	Nominal*	Real**	Nominal*	Real**	Nominal*	Real**
Variation in \$						
2017–2025	17,844	-15,504	21,354	-8,483	24,864	-1,463
2025–2032	35,980	-4,338	45,633	4,095	54,994	11,701
Variation in %						
2017–2025	6.1	-5.3	7.3	-2.9	8.5	0.5
2025–2032	12.3	-1.5	15.6	1.4	18.8	4.0

*In dollars; ** In 2017 dollars.
Sources: Université Laval's department of economics and Desjardins, Economic Studies