QFREB
Québec Federation of Real Estate Boards

A WORD FROM THE ECONOMIST

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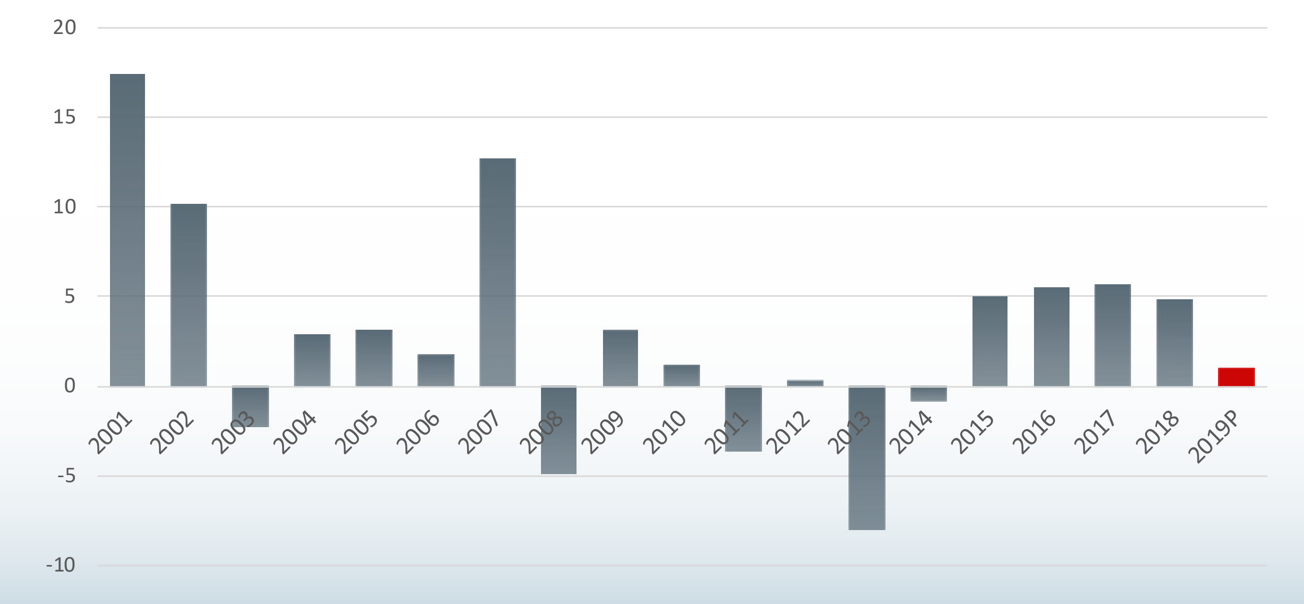
HOW AFFORDABLE IS REAL ESTATE IN QUÉBEC?

Québec's real estate market is more active than ever. The number of residential transactions has been growing by about 5 per cent annually since 2015. However, despite the province's economic vitality and consumer confidence, we still expect there to be a slowdown in residential sales growth in 2019. In fact, we estimate that sales growth will be in the order of 1 per cent this year in Québec.

One of the reasons we anticipate a slowdown in sales is the recent deterioration of real estate affordability in Québec. Maintaining sustained sales growth depends mainly on the link between homeownership constraints (i.e., mortgage rules, interest rates, property prices) and households' ability to pay.

To understand and quantify the interaction between these determinants of the strength of the real estate market, we calculated a real estate affordability index for the province and for each of its six census metropolitan areas (CMAs).

Graph 1: Annual change in sales in the province of Québec (%)



Source: QFREB by the Centris system

Methodology

For the calculation of our affordability index, based on calculations by the National Association of Realtors, we are assuming a 20 per cent down payment and, as a condition for obtaining a mortgage, the monthly payment (based on the median price of a single-family home) does not exceed 25 per cent of the median household income.

To interpret the index, you should know that a level of 100 means that a household earning the median income has exactly enough income to qualify for a mortgage on a median-priced single-family home. An index above 100 means that a family earning the median income has more than enough income to qualify for a mortgage on a median-priced home. Thus, an affordability index of 120 means that a family earning the median income has 120 per cent of the income needed to qualify for a mortgage covering 80 per cent of the value of a median-priced single-family home. In short, the more the index exceeds 100, the more the family is able to afford a median-priced home.

When comparing Montréal with Canada's three other major markets, we calculated the affordability index in relation to the average residential price for these four cities, rather than the median price of single-family homes. Thus, this index should not be compared with that of Québec's CMAs, as it is meant to situate Montréal's market in relation to Canada's other major markets.

The situation in Québec and its CMAs

Table 1	December 2018		
	Median price (single-family home) ($)	Median income (household) ($)	Affordability index
Province of Québec	252,000	54,563	129
Montréal CMA	327,450	56,860	103
Québec City CMA	249,000	58,090	139
Gatineau CMA	254,500	59,856	140
Sherbrooke CMA	198,500	49,467	148
Trois-Rivières CMA	168,000	50,617	179
Saguenay CMA	171,500	51,868	180

Source: Statistics Canada and QFREB by the Centris system

In Québec, a family earning the median income had, in December 2018, 129 per cent of the income needed to qualify for a mortgage on a median-priced single-family home. This suggests that affordability is generally very good in Québec, as an index above 100 indicates that Québec families generally have ample means to take on monthly mortgage payments.

However, the level of affordability varies greatly from one region to another. It is lower in large urban centers such as Montréal, Québec City and Gatineau, and higher in remote areas such as Sherbrooke, Trois-Rivières and Saguenay.

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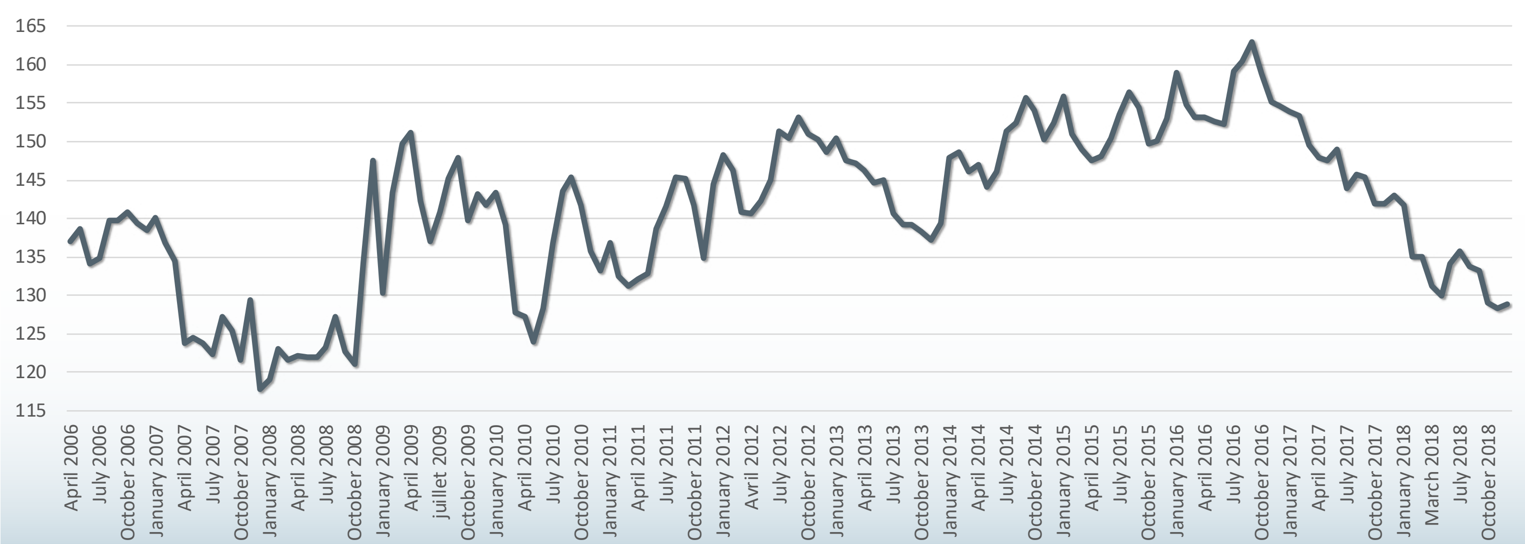
Property prices are largely influenced by supply and demand. When we think of a *big city*, we think of a *large population pool* and *high demand for housing*, and therefore *upward pressure on prices*. In fact, the low affordability level in Montréal, Québec City and Gatineau is mainly due to higher property prices than elsewhere and family income levels that are barely higher than in remote regions.

In the Montréal CMA, a household earning the median income had 103 per cent of the income needed to qualify for a mortgage on a median-priced single-family home in December 2018. This is the CMA where affordability is lowest. How can this be explained? The median income in Montréal is lower than in Québec City and Gatineau, while the median price of a single-family home is about $75,000 more than the provincial average. It is therefore not surprising that Montréal families have a harder time entering the real estate market.

As for households in the Québec City and Gatineau CMAs, they have a median income that is slightly higher than the provincial average, while property prices are close to the provincial average. Thus, in December 2018, the average family in Québec City earned 139 per cent of the income needed to qualify for a typical mortgage, and the average family in Gatineau earned 140 per cent. Because they have greater financial means than the minimum income needed to qualify for a typical mortgage, households in Québec City and Gatineau have easier access to homeownership. In fact, they have easier access than families in the province as a whole whose median income covered 129 per cent of the cost of a mortgage. Thus, the higher incomes in these two CMAs help compensate for the purchase price, which overall represents a heavier financial burden than in remote regions where income is lower but properties are much more affordable.

In the Sherbrooke, Trois-Rivières and Saguenay CMAs, household income is lower than in the province as a whole, but remains at a very acceptable level, while properties are much more affordable. This explains why, in December 2018, Sherbrooke families earned 148 per cent of the income needed to qualify for a mortgage, while families in Trois-Rivières earned 179 per cent and those in Saguenay, 180 per cent. In fact, families in these regions, who earn about $50,000 annually, have ample means to make mortgage payments for properties that range from $160,000 to $200,000, depending on the region.

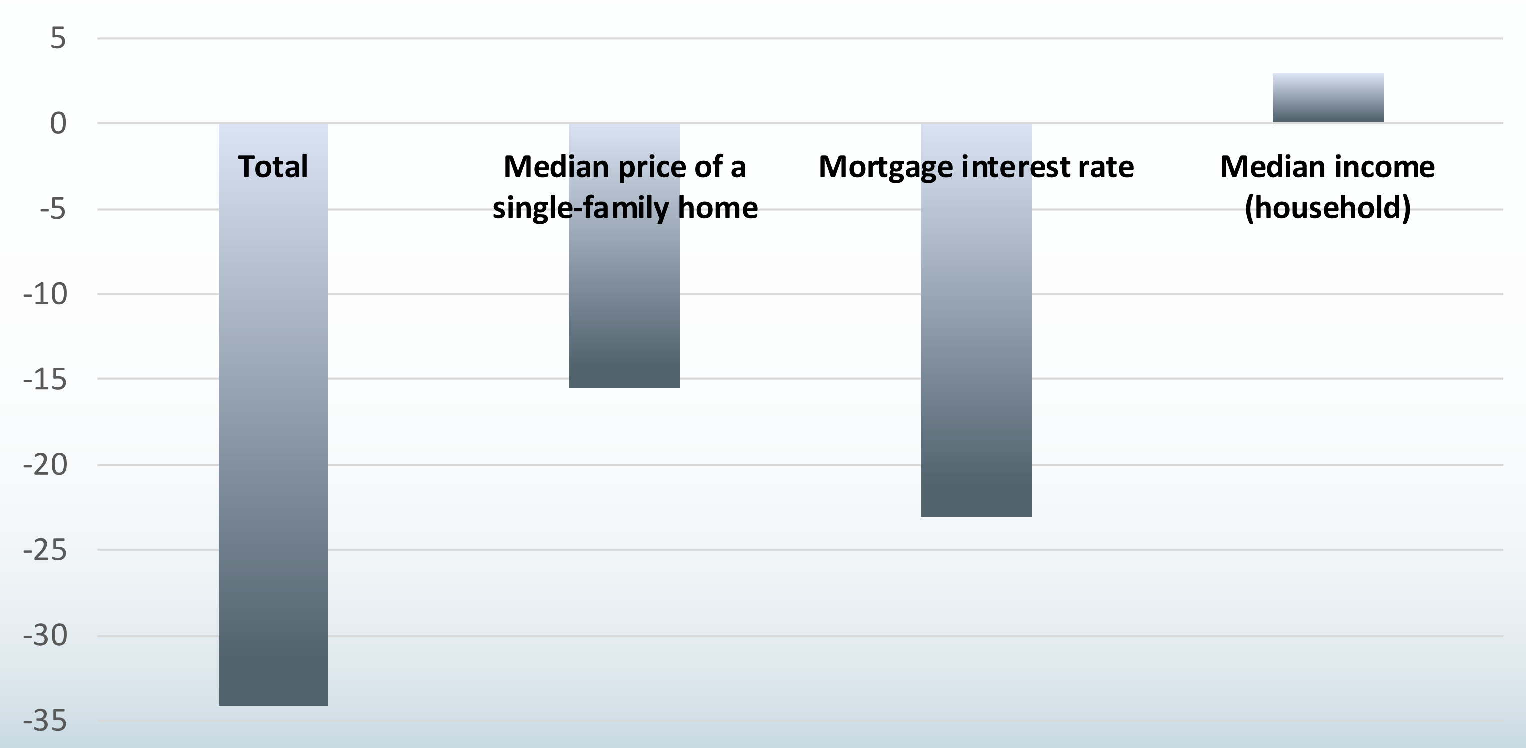
Graph 2: Real estate affordability index in the province of Québec



Source: QFREB by the Centris system

At the provincial level, affordability has always fluctuated at levels above 100, and thus remains affordable at all times, as shown in Graph 2. However, the affordability index has been on a downward trend since September 2016 and has just reached its lowest level since June 2010. This seems surprising given the current strength of the economy but, in fact, it stems in part from the robustness of the market: property price growth has been faster than income growth. Thus, the market is less accessible for families whose salaries have not increased at the same pace as property prices.

Graph 3: Contribution of factors to the drop in affordability between September 2016 and December 2018



Source: QFREB by the Centris system, Conference Board and Statistics Canada

In recent years, the rise in mortgage interest rates has accentuated this dynamic between property prices and incomes. Graph 3 shows that median price has a greater effect on affordability than income, but that the most significant factor is interest rates. Assuming all variables are constant except for the median price of a single-family home, we calculate that this factor alone reduced the affordability level by just over 15 points. In the same vein, the increase in median income had a positive effect of a few points on the index. In contrast, however, mortgage rates had a stronger negative effect than the other two variables, at almost 25 points. It is therefore through the combined effect of these three factors that Québec experienced a decrease of about 35 points in its affordability index between September 2016 and December 2018.

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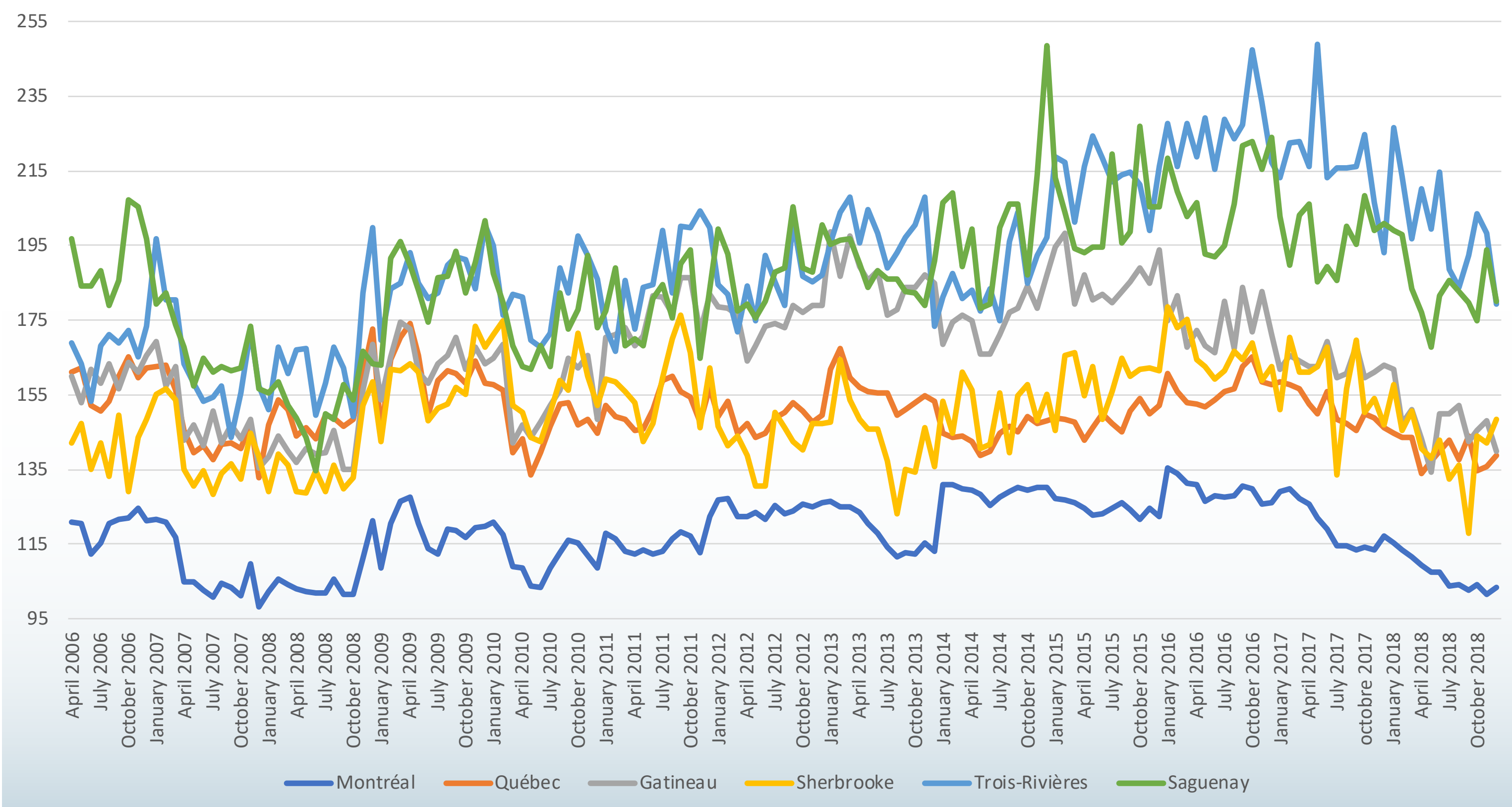
Graph 4: Real estate affordability index in Québec's six census metropolitan areas



Source: QFREB by the Centris system

As for Québec's CMAs, graph 4 shows that they all appear to follow the same trends and react to the same shocks, while maintaining different levels of affordability.

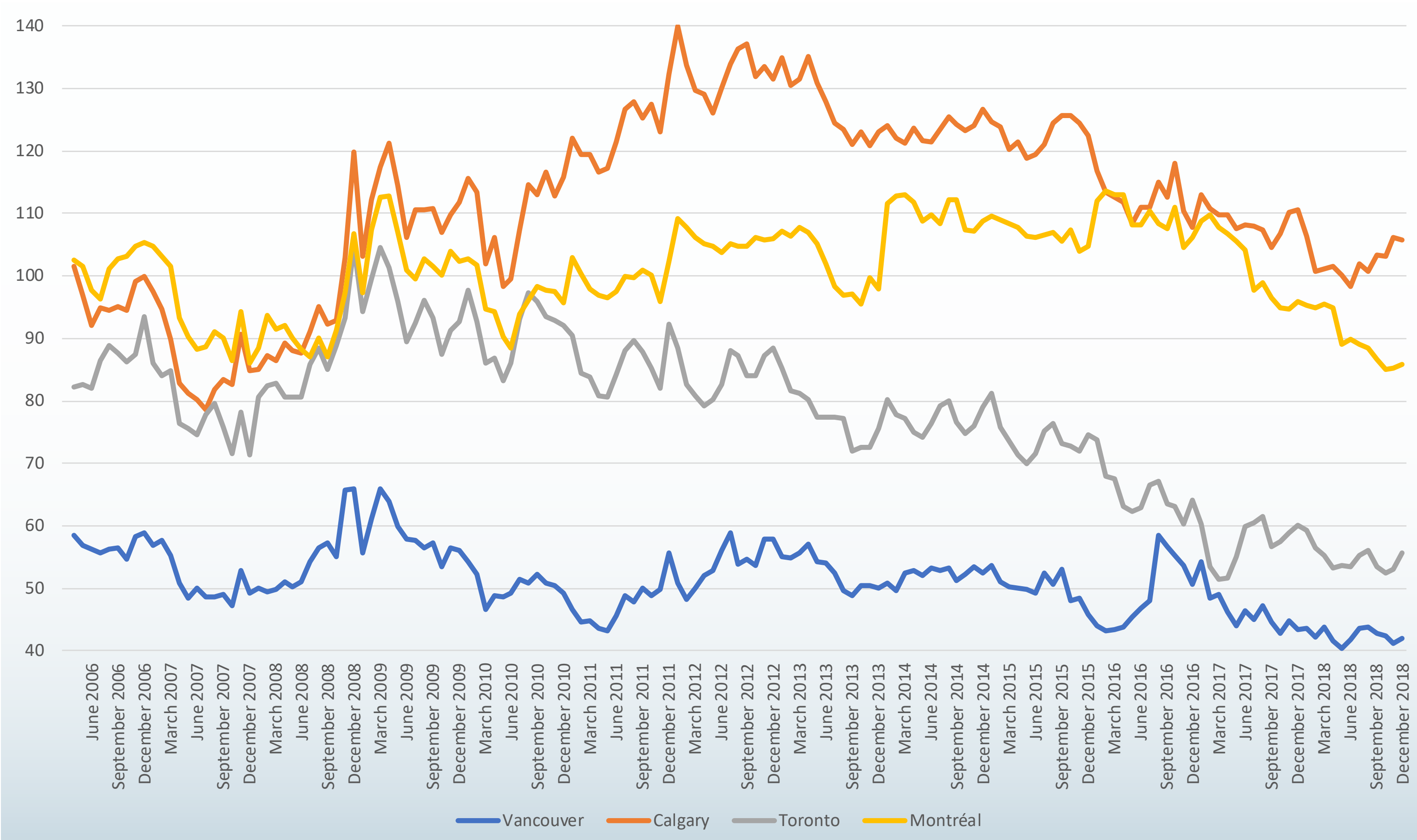
Affordability in all of the province's CMAs began to decline in early 2016, and this decline seems to be continuing today. Once again, we note the clear difference between the affordability level in the Montréal CMA and that of the other CMAs. Despite the economy running at full throttle, families in the province have been seeing their real estate purchasing power decrease since 2016, which is why we believe that sales in Québec will not be able to continue growing at an annual rate of 5 per cent forever.

Major Canadian cities

From a Canadian perspective, it's important to remember that despite the deterioration of affordability in Québec, the situation in our province is still enviable, as graph 5 illustrates.

Following the introduction in January 2018 of the stress test by the Office of the Superintendent of Financial Institutions (OSFI), which requires households to qualify for a mortgage by adding 200 basis points to their interest rate, most major Canadian markets experienced a substantial decrease in the number of transactions. Québec is one of the provinces that did a better job of weathering this new deal, and whose housing market has remained strong.

Graph 5: Real estate affordability index in Canada's main markets



Source: CREA and QFREB by the Centris system

In fact, Montréal is historically much more affordable than Vancouver and Toronto, where families have higher incomes than in Québec but face exorbitant property prices. Calgary is the most affordable market of the four, as property prices are fairly similar to those of Québec, but annual incomes are about $20,000 higher.

Table 2

	December 2018		
	Average residential price ($)	Median income (household) ($)	Affordability index
Vancouver CMA	1,026,938	72,543	42
Toronto CMA	750,180	70,226	58
Montréal CMA	394,373	56,860	86*
Calgary CMA	432,368	76,810	106

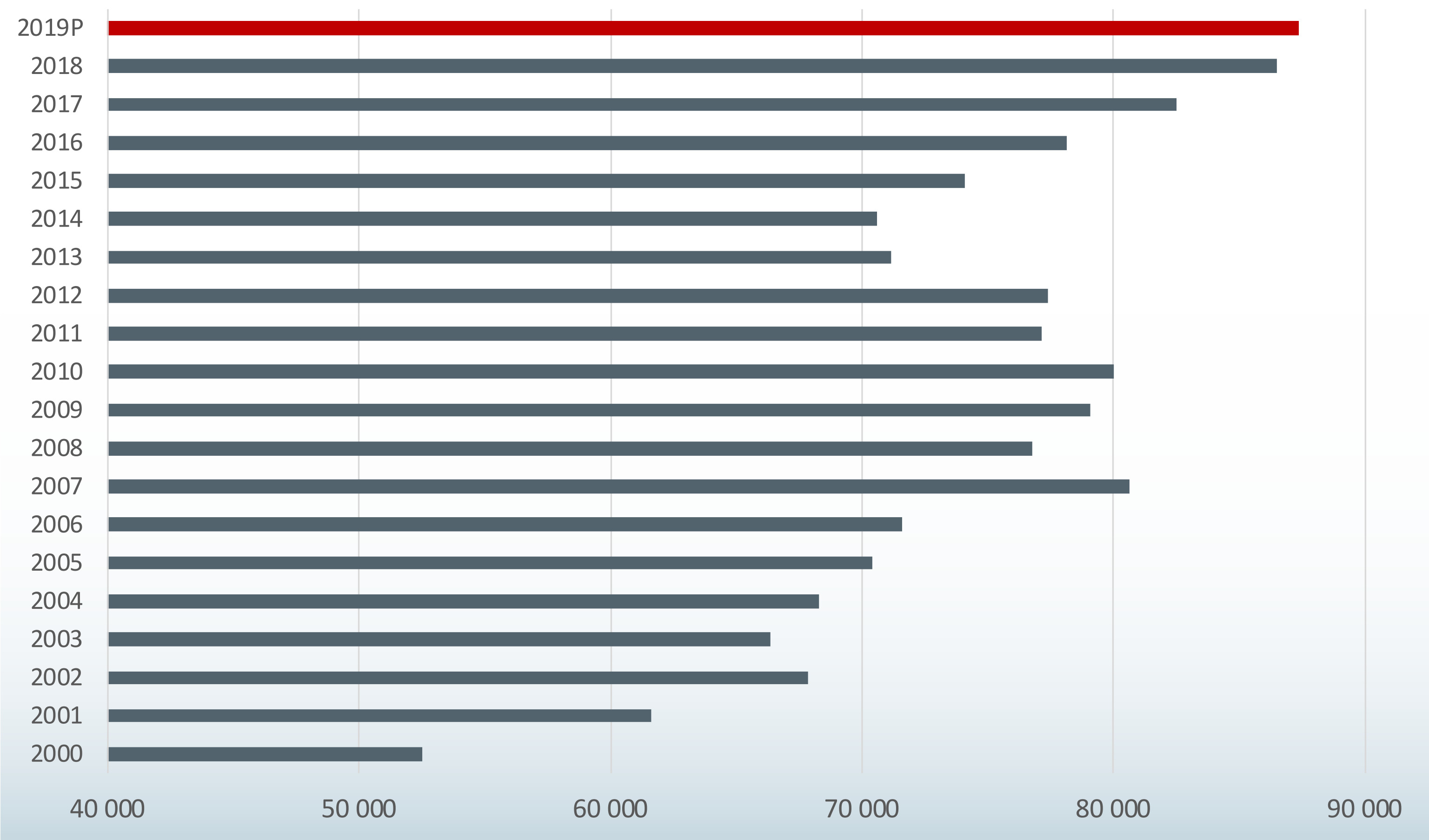
Source: CREA and QFREB by the Centris system

* This table shows the average residential price rather than the median price of a single-family home. As a result, the index for the Montréal CMA is not the same as in the rest of this document.

Québec's outlook for 2019

As we have seen, the affordability index for the province of Québec has deteriorated and is at the same level as in 2008. A similar dynamic can be observed in the province's most populous CMA, Montréal. For these reasons, we anticipate lower sales growth this year, in the order of 1 per cent. However, this situation is far from worrisome, as a slowdown in sales growth still implies positive growth. In other words, even if sales growth were to slow in 2019, the number of transactions would not decrease, and we should still set a new record for the number of sales across Québec. Graph 6 shows the projected level of sales for 2019, which is still higher than in previous years.

Graph 6: Number of residential sales in the province of Québec



Source: QFREB by the Centris system

In summary, we believe that a market slowdown is possible, probably in the second half of the year, given the deterioration in affordability. That said, this pause would temper the rise in property prices relative to the growth of family incomes and would ensure a certain stability in home sales in Québec without the risk of overheating, which could have adverse consequences.

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