

# SPOTLIGHT ON HOUSING

## The Market Has Turned: Home Prices Will Continue to Fall in Quebec and Ontario

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The housing market rolled over this spring. High prices and rising mortgage rates have eroded [affordability](#), sales are down and inventory is on the rise. As a result, we've quickly gone from a seller's market to balanced territory. Buyers are waiting on the sidelines, and in some markets where overbidding was rampant, prices are coming back to earth. By the end of next year, prices are expected to tumble 17% in Quebec and 24% in Ontario. Meanwhile supply shortages, high material costs and rapidly rising interest rates are putting the brakes on new construction and renovation. Look for fewer of these projects in the coming quarters in both provinces.

### Existing Home Sales Have Fallen off a Cliff

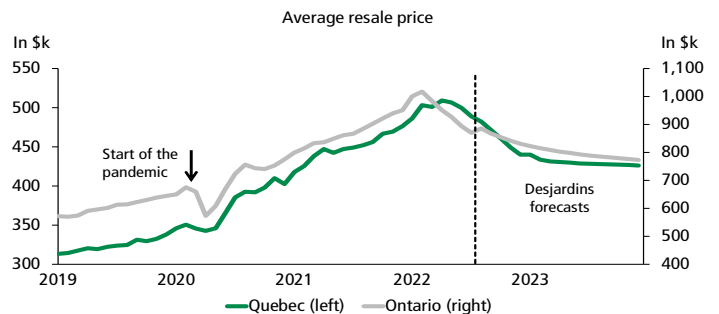
As discussed in a recent [Economic Viewpoint](#), Canada's housing market has corrected quickly over the past few months. Average prices in Ontario and British Columbia are down nearly 15% and 10% respectively from their February peak. Prices in Quebec started falling two months later, but haven't dropped as much. There the average price (box on page 2) topped out around \$510,000 in April before slipping 4.0% to below \$490,000 in July.

And while Quebec home prices have moved in line with June's forecasts, those figures have been revised downwards. It's now expected that by the end of 2023, prices will have fallen 17% from their peak rather than 12% as predicted in June. We think prices in Ontario will fall 24% over the same period compared to 18% previously.

There are two factors behind this updated forecast: quickly deteriorating market conditions and mortgage rate hikes, which have been bigger and faster than anticipated. Despite this correction, prices will still end 2023 higher than they were at the start of the pandemic. We expect them to be about 20% higher in Quebec and 15% higher in Ontario (graph 1).

**GRAPH 1**

**Prices will continue to decline but remain above pre-pandemic levels**



Sources: Canadian Real Estate Association and Desjardins, Economic Studies

### Will We Move from a Balanced Market to a Buyer's Market?

Quebec and Ontario quickly went from pandemic-fuelled seller's markets to balanced territory (graph 2 on page 2). In the coming months, they could even become buyer's markets as sales decline further (graph 3 on page 2). In other words, homes could go for less than asking in some markets. That would be quite a change from the recent buying frenzy. For now, overbidding is becoming a thing of the past in many areas as homes are selling closer to list price.

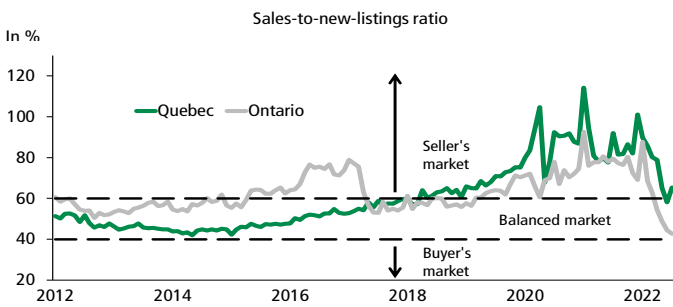
**BOX**

**How is the average price calculated?**

The average price is actually a weighted average price that adjusts for variations in the types of properties sold (single-family homes, condominiums and 2–5 unit plexes) and their location. This method ensures that price changes aren't simply the result of such variations. It also reduces variability over time and better reflects price movements.

**GRAPH 2**

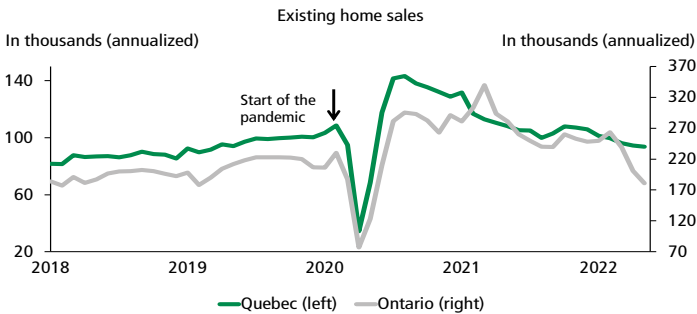
**The market quickly returned to balanced territory**



Sources: Canadian Real Estate Association and Desjardins, Economic Studies

**GRAPH 3**

**Sales of existing homes continue to fall and are already below pre-pandemic levels**



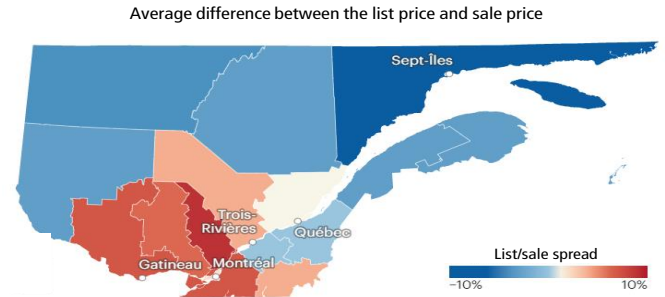
Sources: Canadian Real Estate Association and Desjardins, Economic Studies

**Overbidding Is on the Decline**

In many markets, prices were inflated by overbidding up until the first quarter of this year (graph 4). Overbidding is when multiple buyers make an offer on the same property and the home sells for more than list price. But as demand cools and inventory grows, overbidding is becoming less common in many areas. Homes are selling for closer to asking, pushing prices lower. Prices for single-family homes have soared out of the reach of many households since the start of the pandemic. Those prices could fall the most. Prices for condos and plexes will also decline, but probably not as much.

**GRAPH 4**

**Overbidding was widespread in Quebec in the first quarter of 2022**



Sources: Quebec Professional Association of Real Estate Brokers by the Centris system, Le Devoir and Desjardins, Economic Studies

**Outlying Regions Will Likely See a Smaller Price Drop**

Some areas of Quebec will see bigger price declines than others. Markets that saw less or no overbidding should hold up better. This is the case for outlying regions, especially in the eastern and northern parts of the province.

Monthly data is more volatile at the regional level, so it's difficult to accurately identify peaks and troughs. Forecasts are therefore based on annual averages to allow for more accurate comparisons. In Quebec, the average price started to decline this spring and is expected to fall around 10% in 2023. But the situation will vary by market (table 1).

**TABLE 1**

**2023 Quebec regional forecasts: Year-over-year change in average sale price**

QUEBEC ADMINISTRATIVE REGION	PRICE CHANGE
Bas-Saint-Laurent	- Little or no change
Saguenay–Lac-Saint-Jean	- Little or no change
Capitale-Nationale	- Little or no change
Mauricie	↓ Moderate decline
Estrie	↓ Large decline
Montreal	↓ Moderate decline
Outaouais	↓ Large decline
Abitibi-Témiscamingue	- Little or no change
Côte-Nord	- Little or no change
Nord-du-Québec	- Little or no change
Gaspésie–Îles-de-la-Madeleine	↓ Moderate decline
Chaudière-Appalaches	↓ Moderate decline
Laval	↓ Large decline
Lanaudière	↓ Large decline
Laurentides	↓ Large decline
Montréal	↓ Large decline
Centre-du-Québec	↓ Moderate decline
<b>Census metropolitan area (CMA)</b>	
Saguenay CMA	- Little or no change
Québec CMA	- Little or no change
Sherbrooke CMA	↓ Large decline
Trois-Rivières CMA	↓ Moderate decline
Montreal CMA	↓ Large decline
Gatineau CMA	↓ Large decline
<b>All of Quebec</b>	↓ Large decline

Source: Desjardins, Economic Studies

Of the province's six census metropolitan areas (CMAs), only Quebec and Saguenay may avoid price declines. We continue to see strong activity in the Quebec CMA as people buy up the increased inventory. Sales remain brisk, and the market is still under pressure. But a slowdown is coming, and prices are expected to stabilize somewhat.

In Greater Montreal, prices began to fall this spring as overbidding subsided. Rising mortgage rates have shrunk the buyer pool and inventory is creeping up. We expect to see this correction continue, with prices falling at least 20%.

### Prices Are Already down across Ontario

According to the Desjardins Affordability Index, almost every major market in Ontario was unaffordable in the first quarter of this year. And rapidly rising mortgage rates have sidelined many more buyers since.

Prices have started to fall in almost every Ontario CMA. In many of them, prices plunged 10% to 30% between their February peak and July. So far, some of the biggest declines are in the Greater Toronto Area. Overbidding was rampant there until early this year, but prices have been coming down fast ever since. That said, hybrid work arrangements and high levels of international immigration will moderate the correction in the coming months. The average home price in Ontario plunged about 15% from February to July and is expected to fall 24% by the end of next year.

### Affordability Won't Improve Anytime Soon

A buyer's ability to purchase a home depends on three factors: their income, the sale price and prevailing interest rates. But because the last two factors move in opposite directions, lower prices won't improve affordability anytime soon. Home prices will continue to decline next year, and mortgage rates should begin to fall towards the end of 2023. At that point, we should finally see affordability improve.

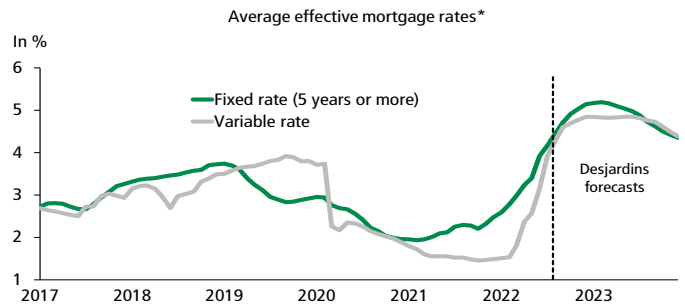
### Interest Rates Are Set to Rise Further

Mortgage rates will likely climb in the near term (graph 5), especially variable rates, which are linked to the Bank of Canada's (BoC) key rate. The Bank is expected to hike rates a few more times this year, bringing the key rate to 3.25%. But as Canada's economy weakens and inflationary pressures ease, the BoC will probably start cutting rates towards the end of next year. Markets seem to be predicting this already as bond yields have likely peaked. As a result, fixed mortgage rates may not rise for much longer.

### The Stress Test Is Getting Harder

The [federal government's minimum qualifying rate](#) is making things especially tough for borrowers right now. The rate was last updated in June 2021 and kept unchanged at its December review. To qualify for a mortgage and determine their maximum

**GRAPH 5**  
Mortgage rates are rising rapidly in Canada



\* Weighted by the size of cash advances.  
Sources: Bank of Canada and Desjardins, Economic Studies

loan amount, borrowers must pass a stress test. Basically, they have to qualify at a higher rate than the one offered by their lender. The rate used for this stress test is either 5.25% or the mortgage rate offered plus 2%, whichever is greater.

Early this year when mortgage rates were low, borrowers were able to qualify with the 5.25% "floor" rate. But now that five-year fixed rates are between 5.0% and 6.0%, they have to qualify with an interest rate of 7.0% to 8.0%.

This has had a number of effects on the housing market:

- ▶ Far fewer borrowers can qualify for a mortgage.
- ▶ Those who can qualify are able to borrow much less.
- ▶ Borrowers who are refinancing will be approved for less.

The minimum qualifying rate is meant to protect borrowers from financial difficulty in the event interest rates go up or their income goes down. If mortgage rates rise further this year as predicted, the stress test will get even harder. The housing market will therefore continue to contract until late 2023. Sales and prices will continue to decline, as will new construction and renovation activity.

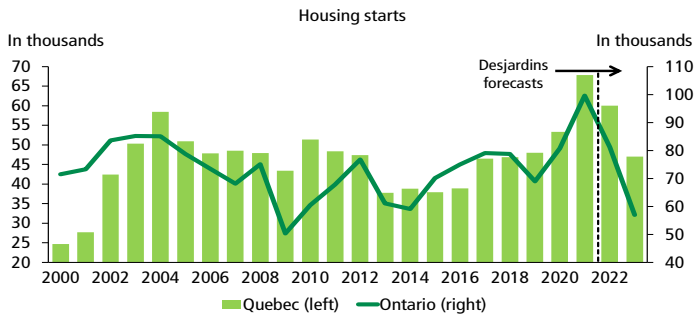
### Less Construction and Renovation

Many potential buyers will have to put their new builds on hold due to rising borrowing costs and high prices. In the meantime, homeowners who can afford to can renovate. But after surging during the pandemic, renovation spending is expected to slow.

Soaring material prices have sent renovation costs through the roof. Renovation spending was up nearly 40% last year in dollar terms when lumber prices were at their height. Material prices have since gone down slightly, keeping a lid on renovation price growth in nominal terms. Over the next few quarters, renovation spending is expected to fall as households contend with higher borrowing costs.

New construction will take a bigger hit. In Quebec, housing starts are expected to decline by 11.5% this year and 21.7% next year (table 2 on page 5). Although Ontario housing starts remained strong in the first half of the year, they're poised to drop close to 20% in 2022 and 30% in 2023 (graph 6).

**GRAPH 6**  
**Residential construction is expected to decline sharply after hitting a record high in 2021**



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

Single-family starts will fall more sharply after spiking in the early waves of the pandemic. More affordable housing such as semi-detached homes, row houses and condominiums will see a smaller decline. These types of homes tend to be popular with first-time buyers, but demand for them will likely cool.

Many households will continue to rent, putting additional pressure on the rental market. High building costs and faster-than-expected rate hikes are jeopardizing the profitability of some projects. Highly leveraged developers are having to cancel or postpone projects, while those in better financial shape are moving forward with new construction. But rental apartment construction has already started to slow slightly.

**TABLE 2**  
**Quebec housing market outlook 2022–2023**

	2019	2020	2021	2022f	2023f
<b>New housing market</b>					
<b>New construction (\$B)</b>	11.7	13.0	17.6	16.0	13.0
Year-over-year change (%)	-1.9	10.7	35.4	-9.1	-18.8
<b>Housing starts</b>	47,967	53,364	67,810	60,000	47,000
Year-over-year change (%)	2.3	11.3	27.1	-11.5	-21.7
<b>Houses</b>	13,742	15,502	21,091	14,000	9,000
Year-over-year change (%)	-8.2	12.8	36.1	-33.6	-35.7
<b>Single-detached</b>	8,989	10,437	14,826.0	---	---
Year-over-year change (%)	-10.6	16.1	42.1	---	---
<b>Semi-detached</b>	2,966	3,457	4,175.0	---	---
Year-over-year change (%)	-1.0	16.6	20.8	---	---
<b>Row housing units</b>	1,787	1,608	2,090.0	---	---
Year-over-year change (%)	-6.6	-10.0	30.0	---	---
<b>Apartments</b>	34,225	37,862	46,719	46,000	38,000
Year-over-year change (%)	7.3	10.6	23.4	-1.5	-17.4
<b>Condos</b> <sup>1</sup>	8,172	7,222	8,032	7,000	5,500
Year-over-year change (%)	-17.1	-11.6	11.2	-12.8	-21.4
<b>Rentals</b> <sup>1</sup>	24,861	28,709	35,659	35,000	31,500
Year-over-year change (%)	21.3	15.5	24.2	-1.8	-10.0
<b>Conventional rentals</b> <sup>2</sup>	21,536	26,554	33,049	32,500	29,500
Year-over-year change (%)	28.6	23.3	24.5	-1.7	-9.2
<b>Retirement homes</b> <sup>2</sup>	3,159	2,017	2,567	2,500	2,000
Year-over-year change (%)	-11.4	-36.2	27.3	-2.6	-20.0
<b>Resale market</b>					
<b>Unit sales</b>	96,349	112,162	109,473	91,268	75,900
Year-over-year change (%)	11.4	16.4	-2.4	-16.6	-16.8
<b>Weighted average price (\$k)</b>	324	377	448	482	426
Year-over-year change (%)	5.2	16.4	18.9	7.5	-11.6
<b>Sales volume (\$B)</b>	30.5	40.0	46.8	44.0	32.3
Year-over-year change (%)	15.9	31.1	17.1	-6.1	-26.5
<b>Other indicators</b>					
<b>Vacancy rate for rental units</b> <sup>3</sup> (%)	1.8	2.5	2.5	1.8	1.5
<b>Average rent</b> <sup>3</sup> (\$)	800	844	873	915	965
Year-over-year change (%)	5.1	3.8	3.6	4.8	5.5
<b>Renovation spending</b> <sup>4</sup> (\$B)	14.2	14.2	19.9	23.5	20.0
Year-over-year change (%)	3.9	0.1	40.1	17.9	-14.9

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

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

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