

B.C. Market Housing Trends, Bubbles, Cycles, and Outlook

Urban Development Institute - Victoria

Wednesday, June 14, 2006

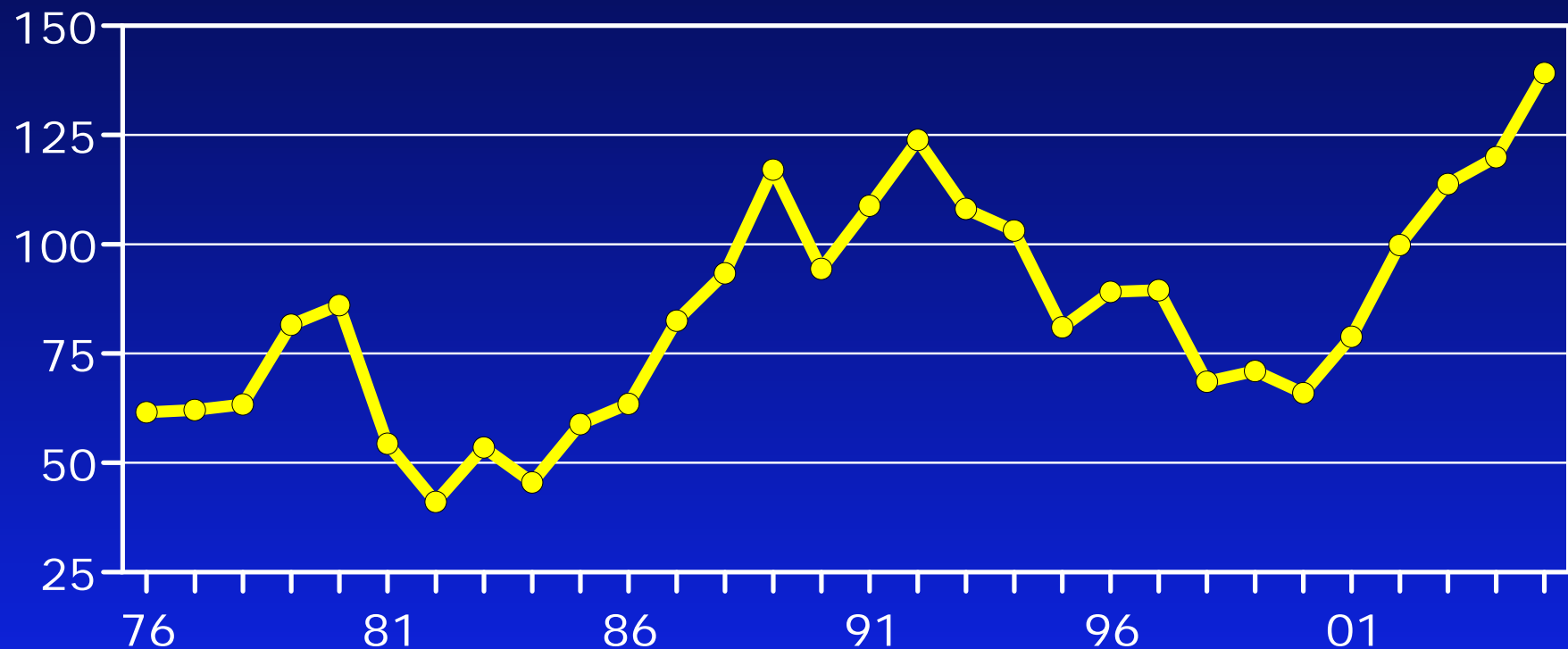
Helmut Pastrick
Chief Economist
Credit Union Central of British Columbia



Housing sales up five consecutive years

Housing Sales, B.C., Annually

Units - Thousands



Source: Landcor Data Corp.

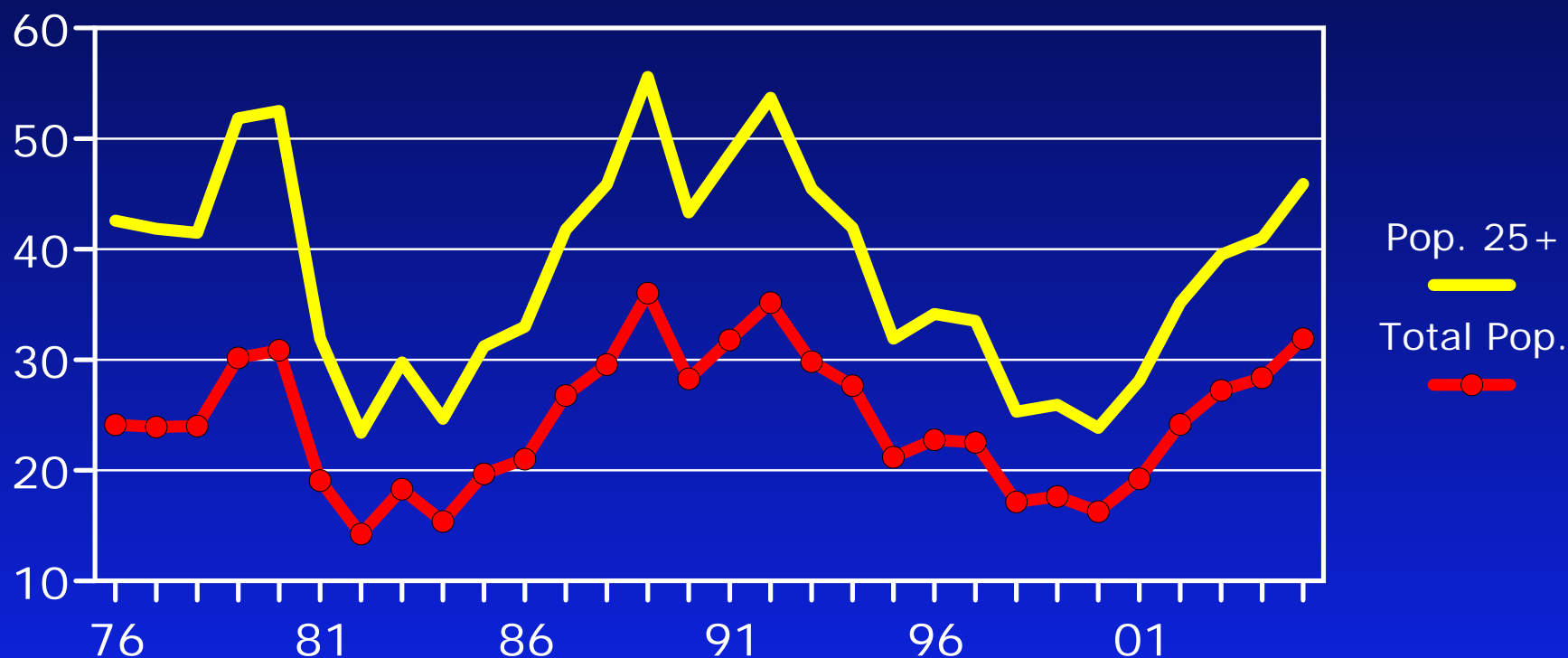
Latest: 2005



Current sales activity below previous highs when adjusted for market size

Housing Sales Adjusted for Population, B.C.

Units per 1,000 persons



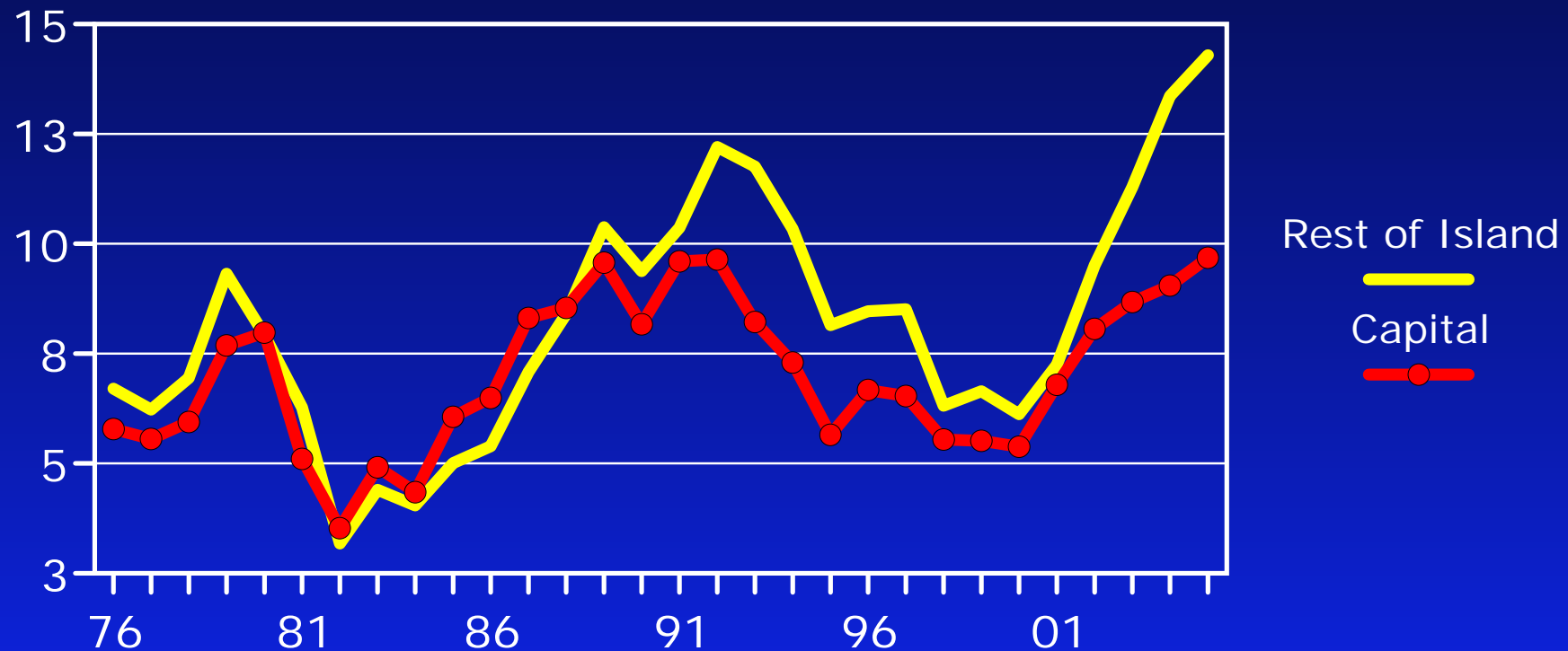
Source: Landcor Data Corp., Statistics Canada, CUCBC. Latest: 2005



Larger sales gains outside Capital region

Housing Sales by Region, Vancouver Island

Units - Thousands



Source: Landcor Data Corp.

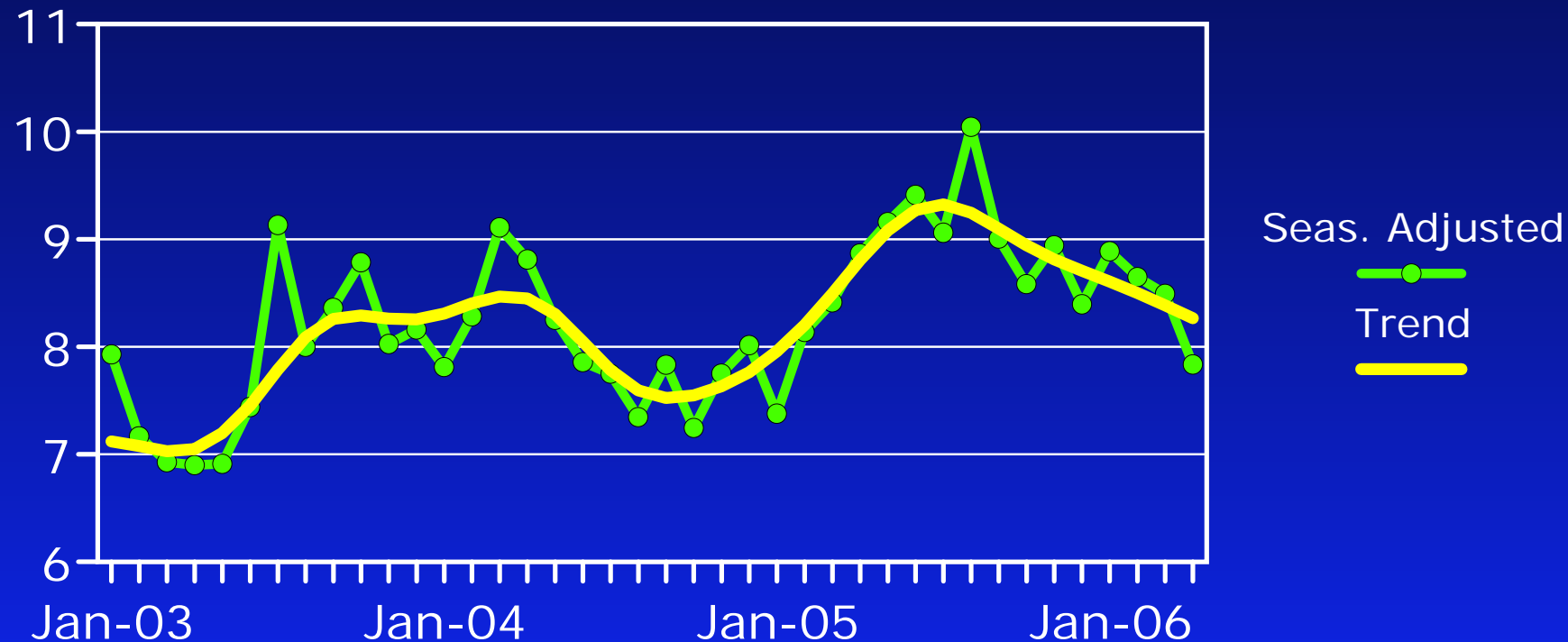
Latest: 2005



Monthly sales off mid-2005 high, on mild downtrend

MLS Residential Sales, B.C.

Units - Thousands



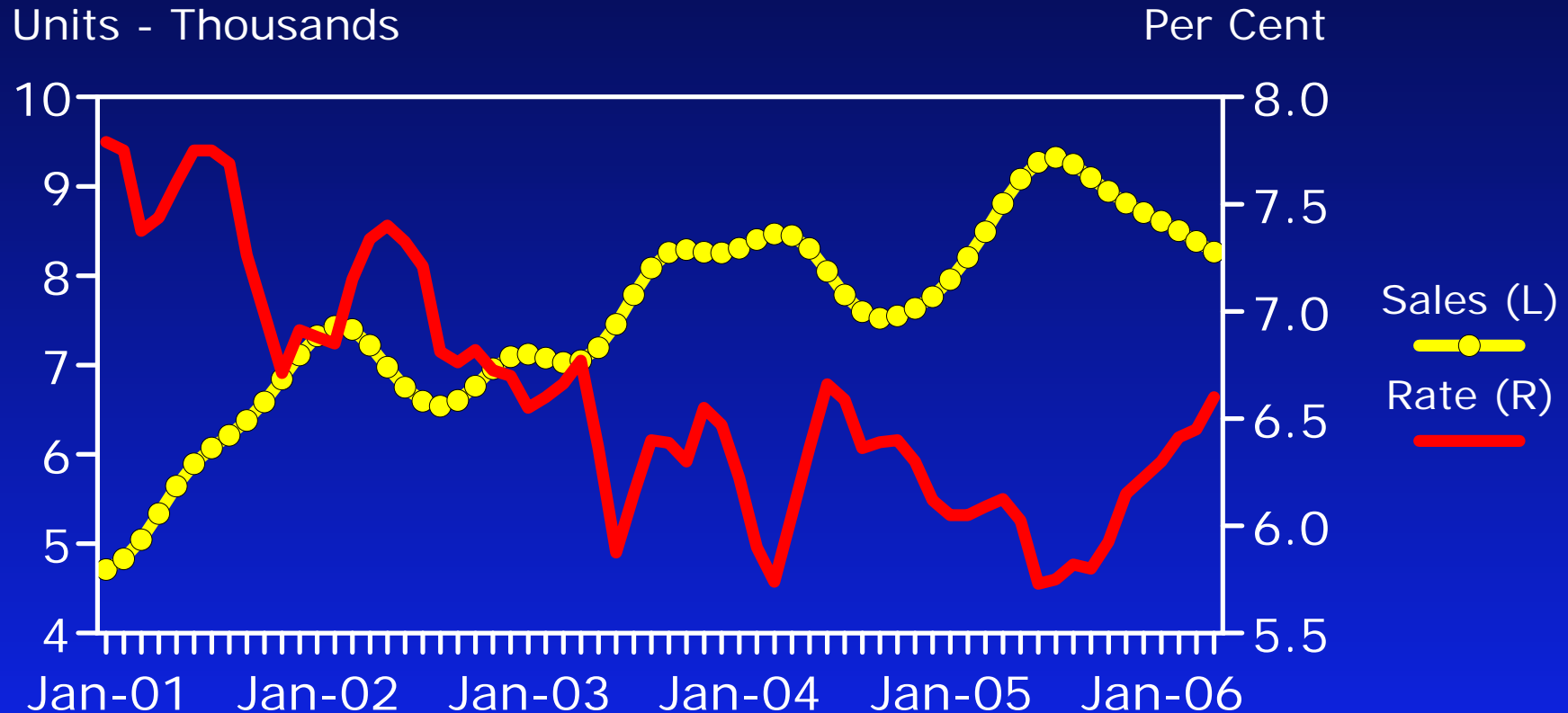
Source: CREA, CUCBC.

Latest: Apr. 2006



Rising mortgage rates turn down unit sales from July 2005 high

B.C. MLS Residential Sales Trend and 5 Yr. Mortgage Rate

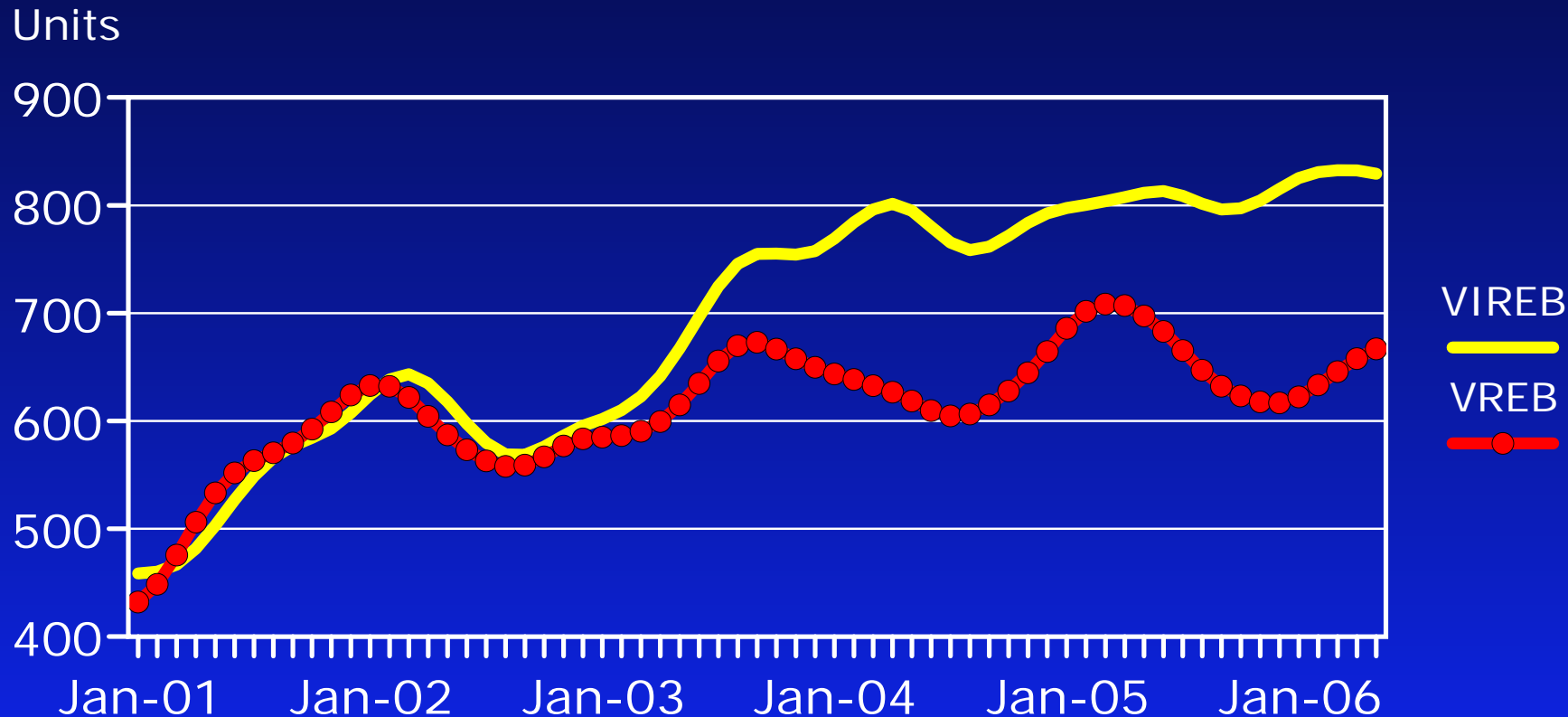


Source: CREA, Bank of Canada, CUCBC. Latest: Apr. 2006



Vancouver Island REB sales holding up under higher rates

MLS Res. Sales Trends, Victoria and Vancouver Island REBs



Source: CREA, CUCBC.

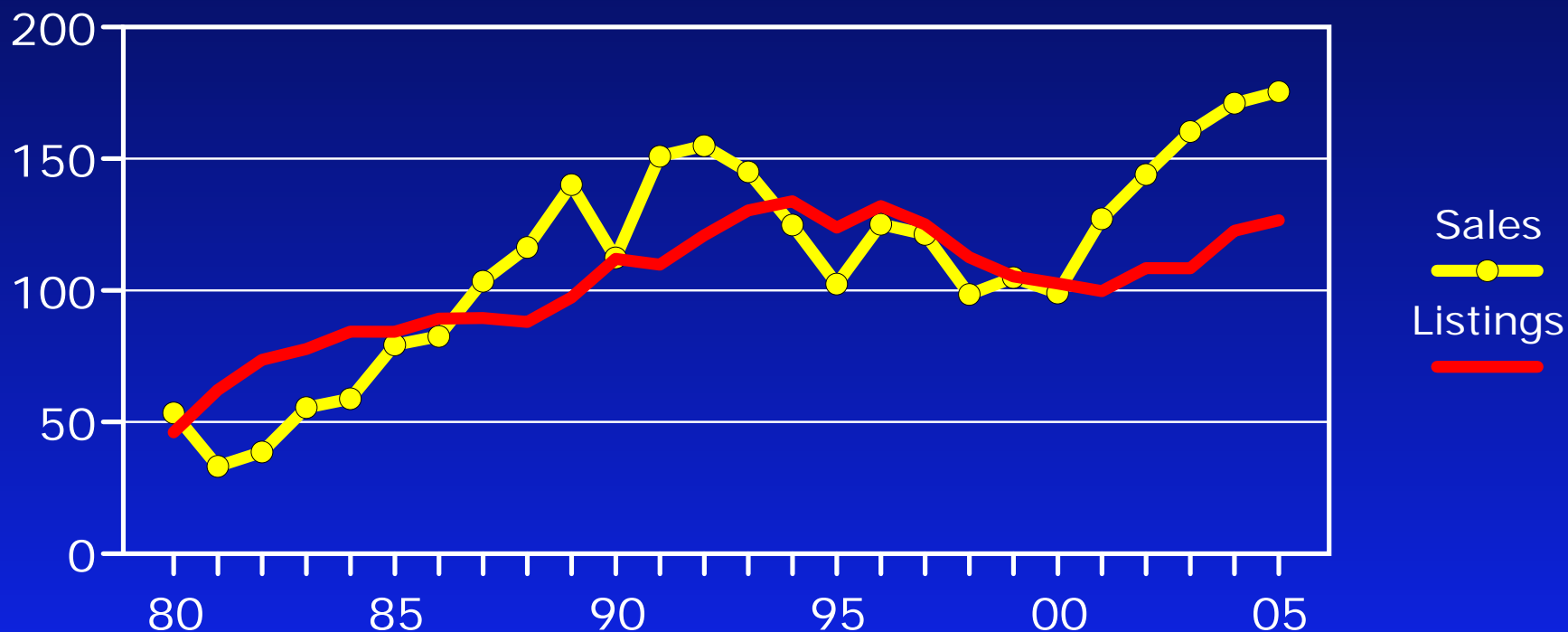
Latest: May 2006



Listings well below sales volume resulting in tight market conditions

MLS Residential Sales and Listings Trends, Vancouver Island REBs, Annually

Index 1980-2000=100



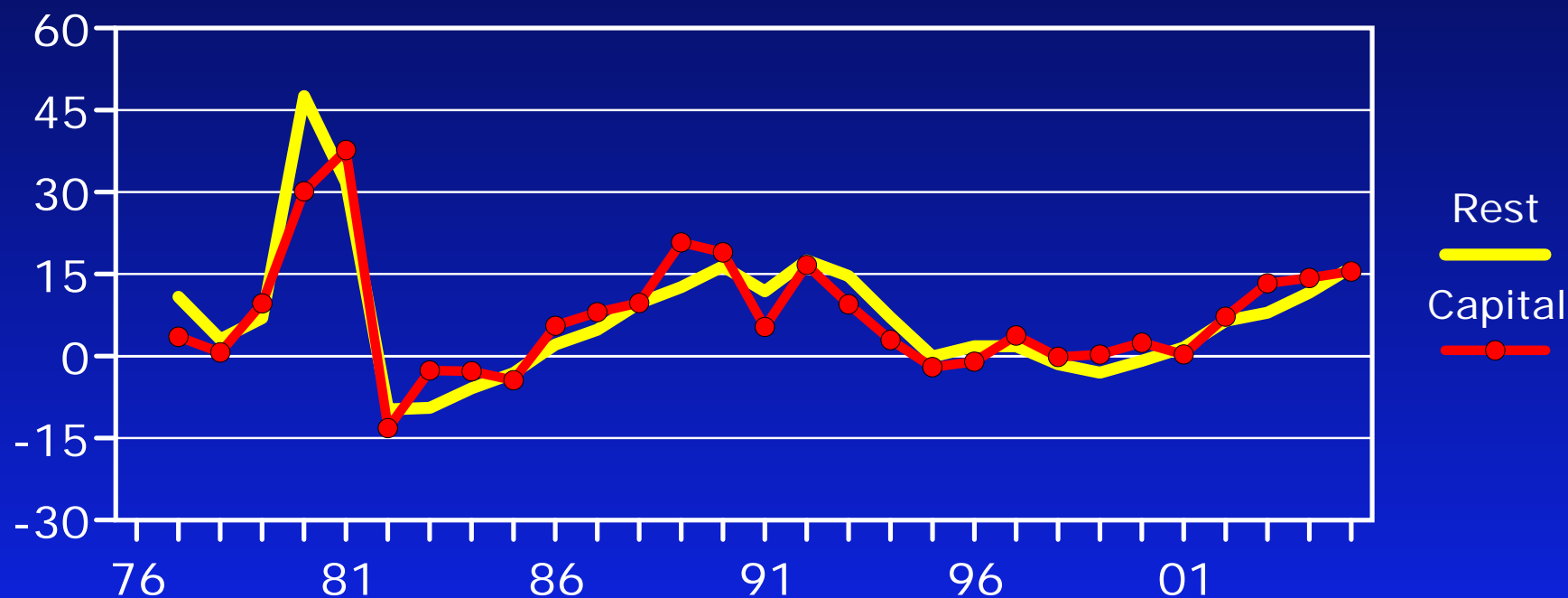
Source: VREB, CUCBC.



Prices up about 15% last year

Percentage Change in Housing Average Sales Price,
Capital Region and Rest of Island

Per Cent



Source: Landcor Data Corp, CUCBC.

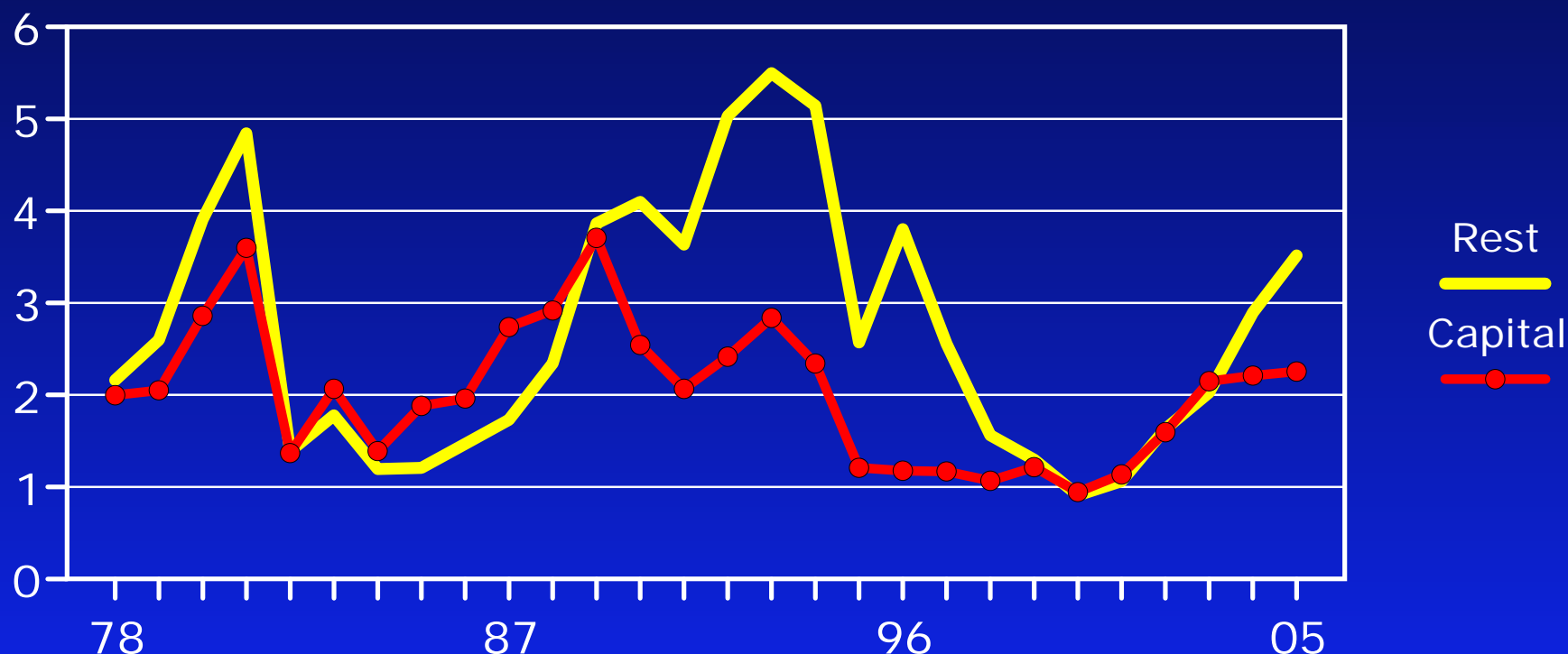
Latest: 2005



New construction rising from low levels

Housing Permits, Capital Region and Rest of Island

Units - Thousands



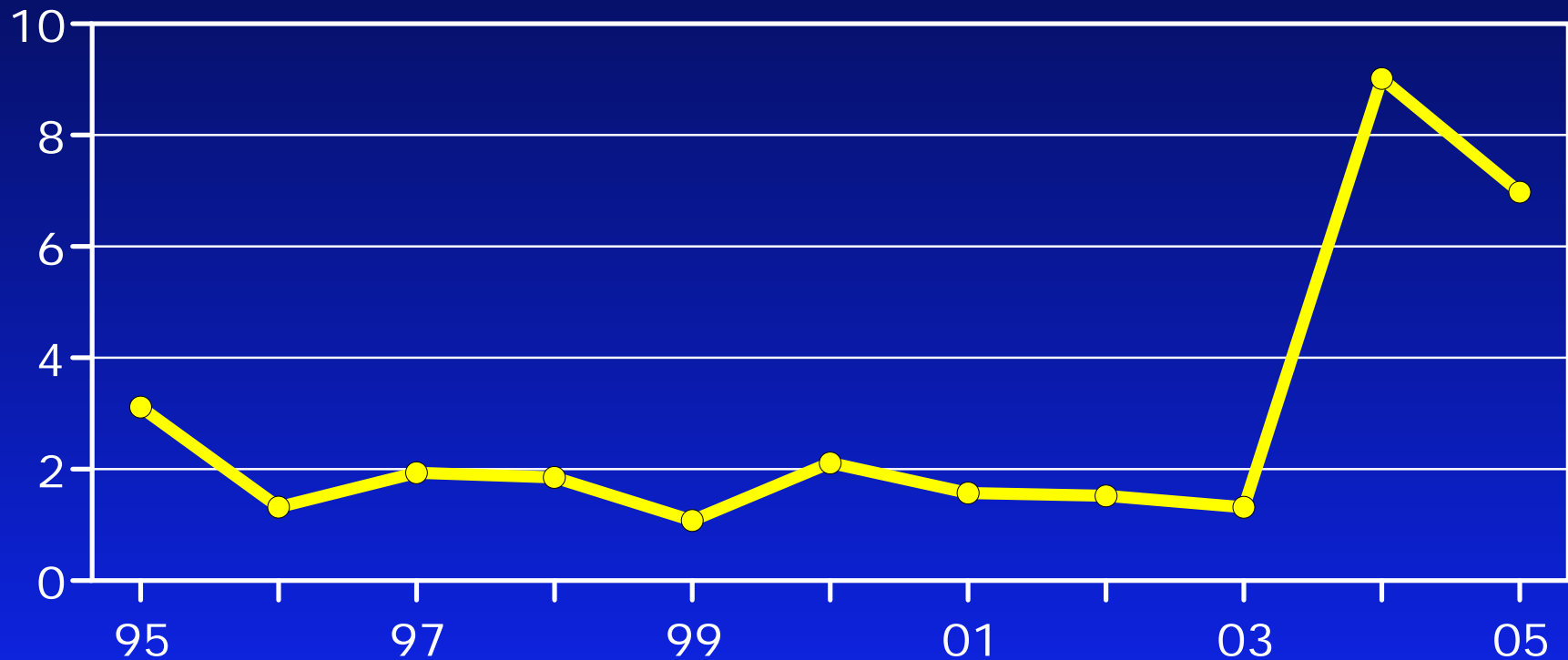
Source: Statistics Canada



Construction costs shoot up

Change in Apartment Construction Cost Index, GVRD

Per Cent



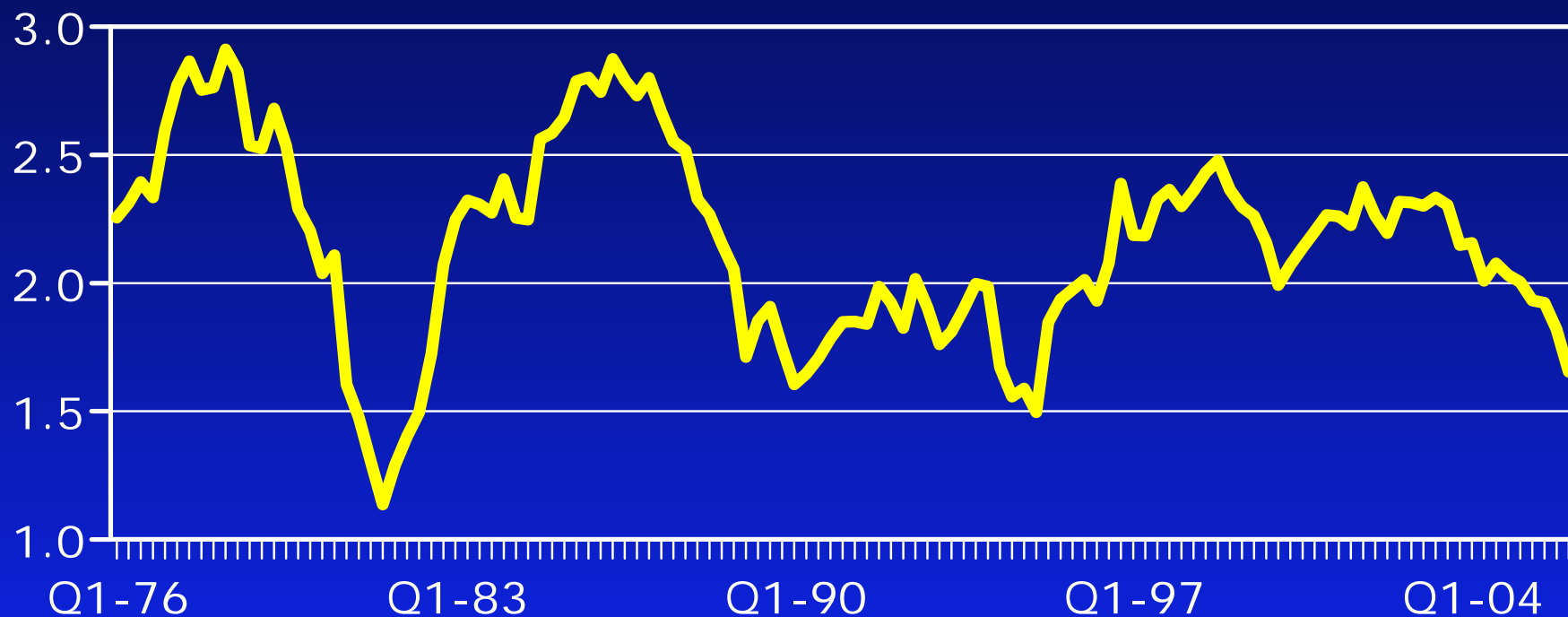
Source: Statistics Canada.



Buyer affordability deteriorating

B.C. Home Buyer Affordability Index, Quarterly

Ratio - Income/Principal & Interest Payment



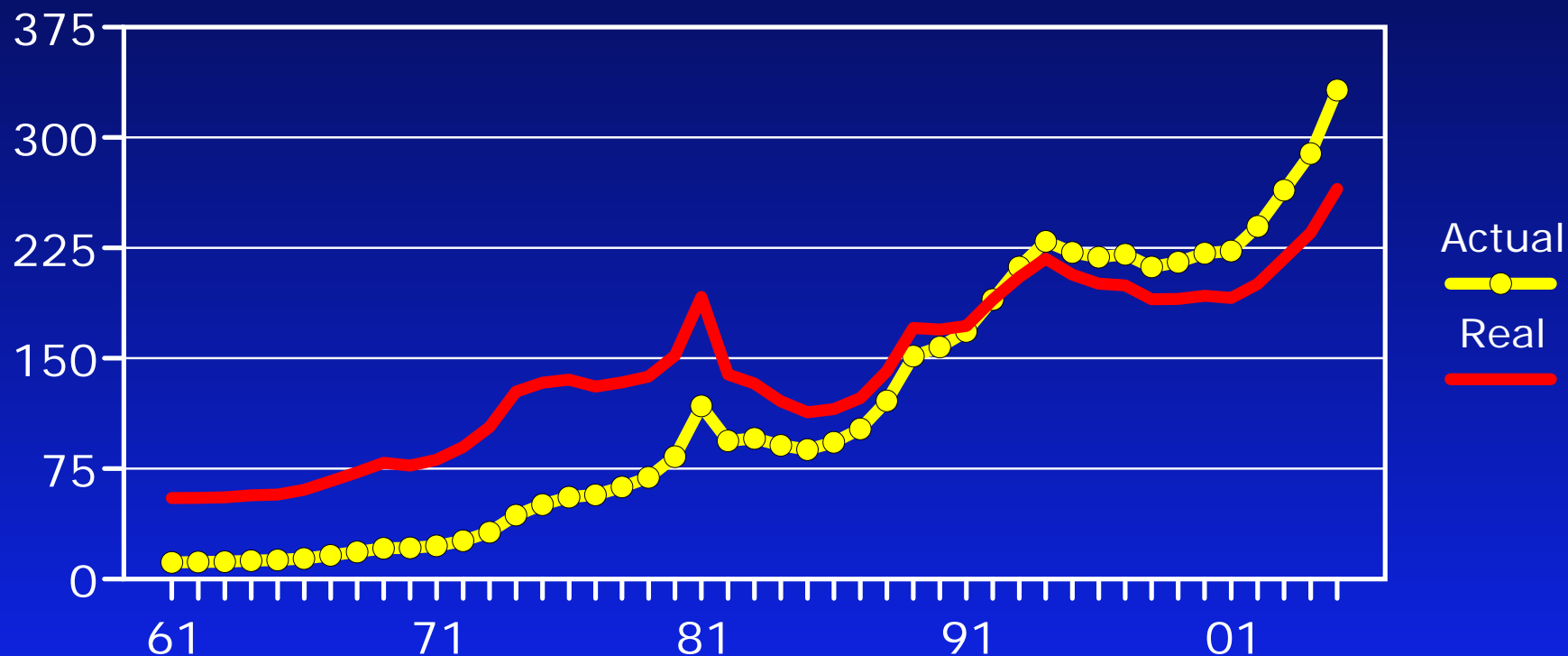
Source: CUCBC. Based on average sales price, 5 year mortgage rate, average weekly wages.
Note: A rise/fall indicates improving/deteriorating affordability. Latest: 2006 Q1



Long term run-up in B.C. housing prices

MLS Residential Average Sales Price, B.C.

Dollars - Thousands



Source: CREA, CUCBC. Real: inflation adjusted

Latest: 2005



Housing Bubble Points:

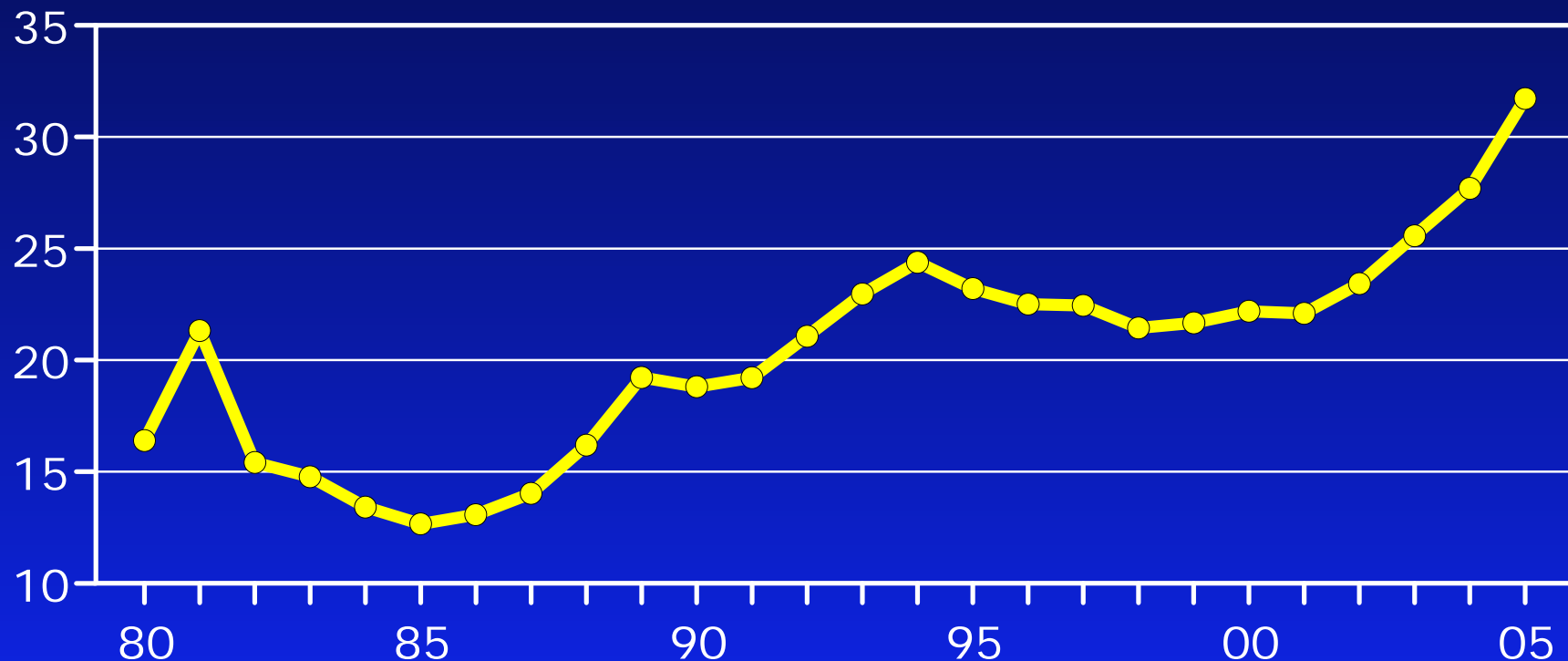
- High price growth is not sufficient evidence of a bubble nor is a price drop
- Housing differs from other assets due to higher transaction costs, less liquid markets, and shelter need negates liquidation need



Price increases outstrip rents, ownership housing overvalued?

B.C. Housing Price and Rent Trends

Price/Annual Rent Ratio

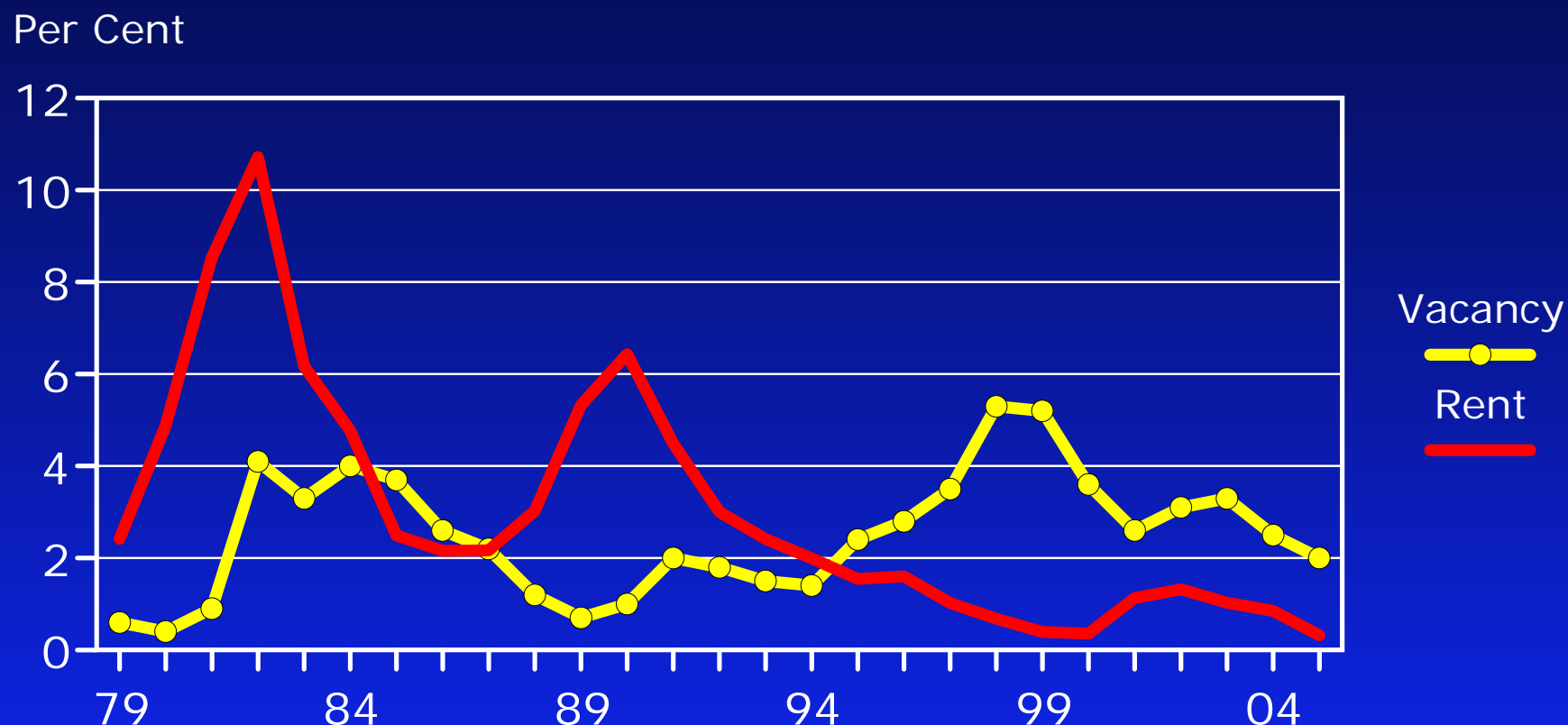


Source: CUCBC.



Low rent increases last ten years

Change in CPI Rent Index and Rental Vacancy Rate, B.C.



Source: Statistics Canada, CMHC.

Latest: 2005



Housing Valuation:

- Fundamental value of homeownership housing difficult to determine
- Price/rent most applicable to income investor, less applicable to principal homeowner
- Capital gain important part of overall return
- Net user cost preferable method



Net User Cost of Home-owning =

- Foregone interest of alternative investment
- Property taxes and insurance
- Depreciation and maintenance
- Owning vs renting risk premium
- minus Expected capital gain

Source: FRBNY Staff Report No. 218, Assessing High House Prices: Bubbles, Fundamentals, and Misperceptions



Net user cost valuation of housing prices

Property: Std. Two-Storey	Price	Rent	Other User Costs	Exp. Cap. Gain	Net User Cost	Valuation
North Delta	359,000	1,400	9.8	5.4	4.4	391,000
North Vancouver	610,000	2,000	9.5	6.5	3.0	793,500
West Vancouver	880,000	2,500	9.4	6.7	2.7	1,134,200

Valuation = Annual Rent/Net User Cost

Expected capital gain = Compound annual rate of price appreciation since 1976

Source: Royal LePage Survey of Canadian House Prices, Q1 2006,
REBGV, Landcor Data Corp., CUCBC.



If expected capital gain reduced by 2% per year, housing prices overvalued

Property: Std. Two-Storey	Price	Rent	Other User Costs	Exp. Cap. Gain	Net User Cost	Valuation
North Delta	359,000	1,400	9.8	3.4	6.4	262,500
North Vancouver	610,000	2,000	9.5	4.5	5.0	480,000
West Vancouver	880,000	2,500	9.4	4.7	4.7	638,300

Valuation = Annual Rent/Net User Cost

Expected capital gain = Compound annual rate of price appreciation since 1976

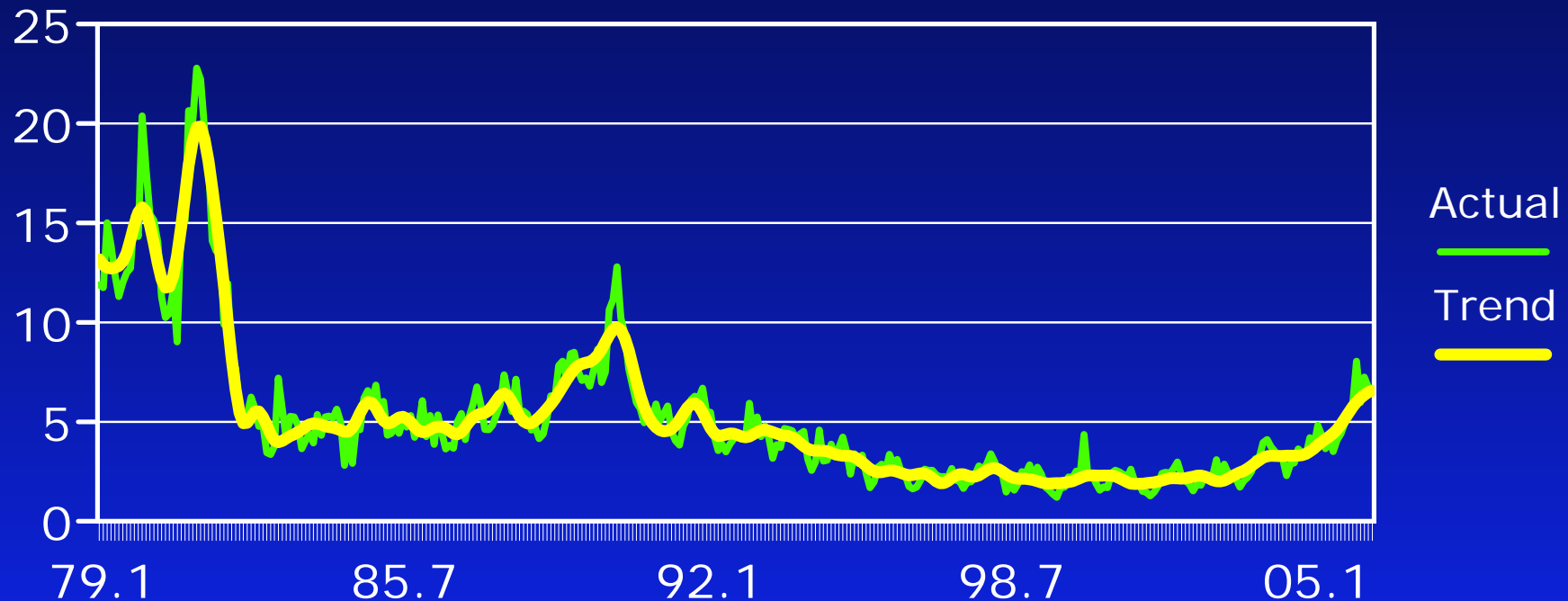
Source: Royal LePage Survey of Canadian House Prices, Q1 2006,
REBGV, Landcor Data Corp., CUCBC.



Speculation indicator rising, remains well below previous highs

B.C. Housing Sales Held Less Than 6 Months

Per Cent of Total Sales



Source: Landcor Data Corp, CUCBC.

Latest: April 2006

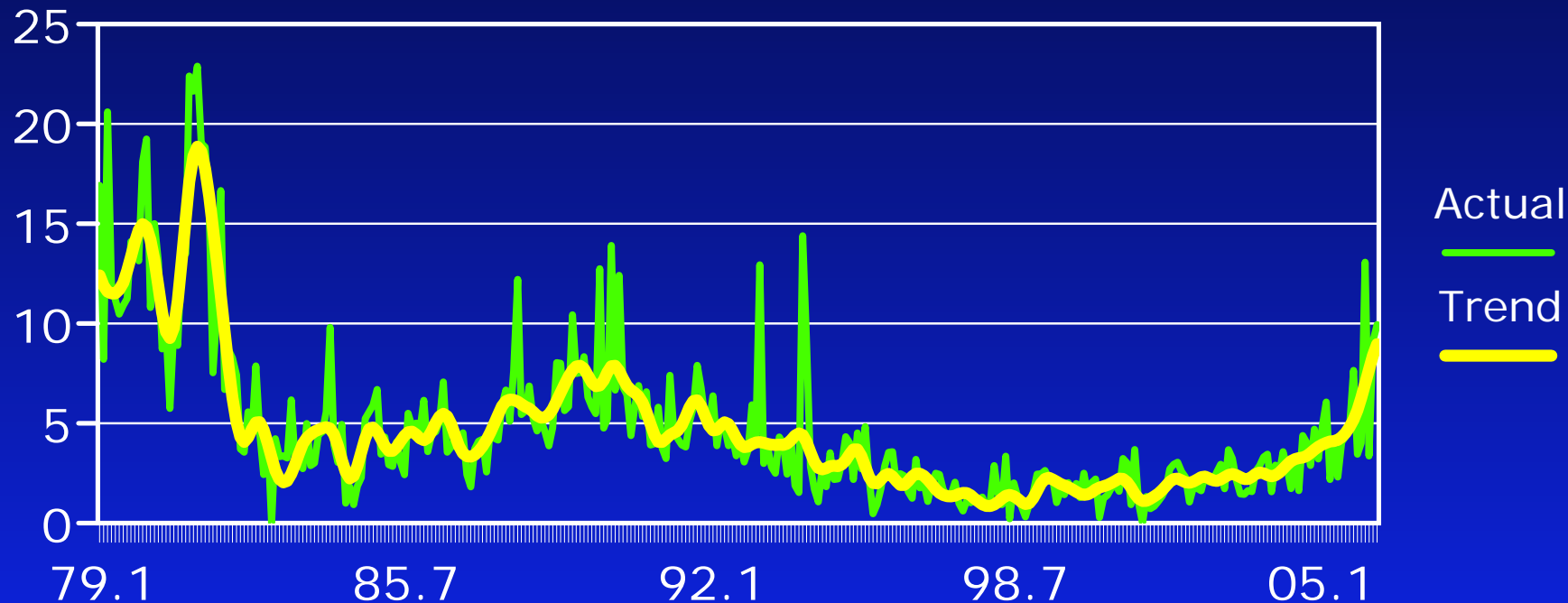
Note: Excludes presales prior to construction completion.



Speculation rising in Capital region

Capital Region Housing Sales Held Less Than 6 Months

Per Cent of Total Sales



Source: Landcor Data Corp, CUCBC.

Latest: April 2006

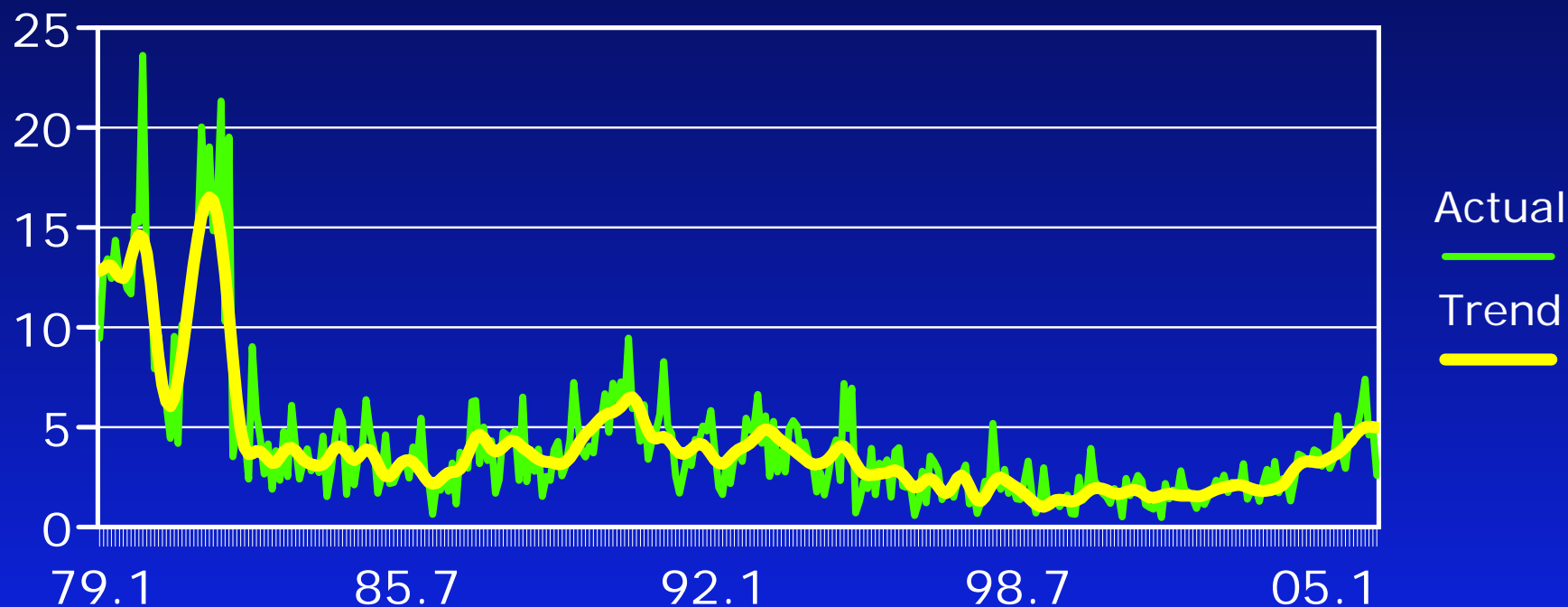
Note: Excludes presales prior to construction completion.



Speculation lower outside Capital region

Rest of Island Housing Sales Held Less Than 6 Months

Per Cent of Total Sales



Source: Landcor Data Corp, CUCBC.

Latest: April 2006

Note: Excludes presales prior to construction completion.



Housing Bubble Points:

- Necessary and sufficient condition is a high level of speculation
- No market-wide housing bubble currently exists, but one could develop
- Sub-market specific bubble could exist, e.g., downtown Vancouver high-rise condos
- Bubble apparent only after the fact, if then



Causes of a Real Estate Market Downturn:

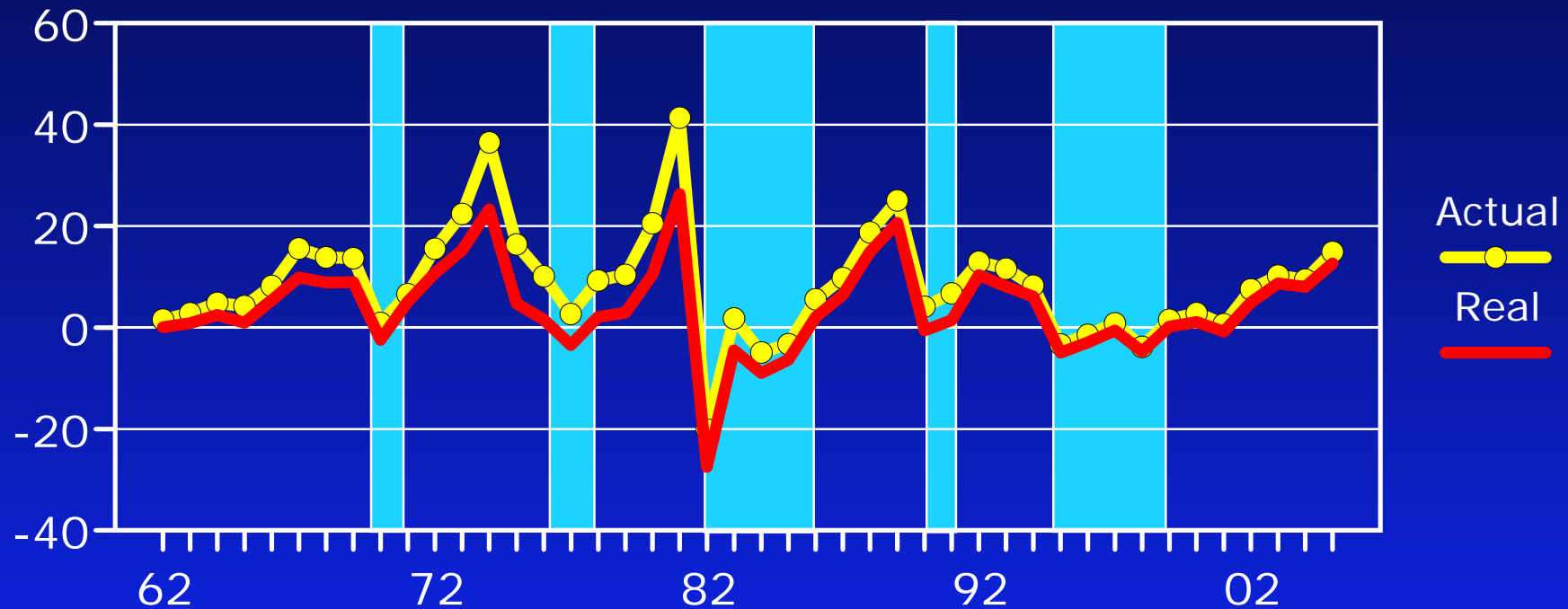
- Most often due to external factors
- Substantial and sustained negative changes to demand drivers - large increase in mortgage rates, rising unemployment, falling in-migration
- Macro shock, oil price shock, geo-political event
- High housing prices alone not usual cause



Cyclical pattern in housing prices; long weak period 1995 to 2001

Percentage Change in MLS Average Sales Price, B.C.

Per Cent



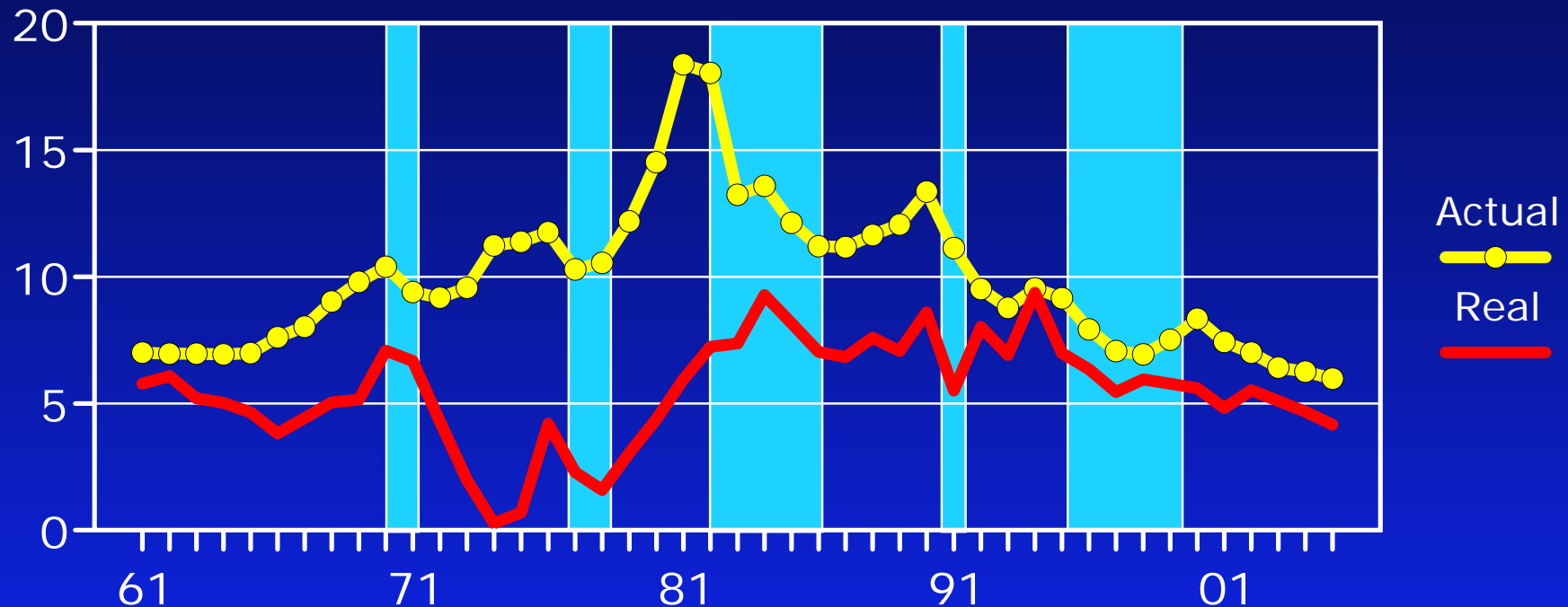
Source: CREA, CUCBC. Actual deflated by BC consumer prices. Latest: 2005
Shaded areas represent housing price recessions.



Mortgage rates on sustained rise before price peaks

Five-Year Mortgage Rate, Actual and Inflation-Adjusted

Per Cent



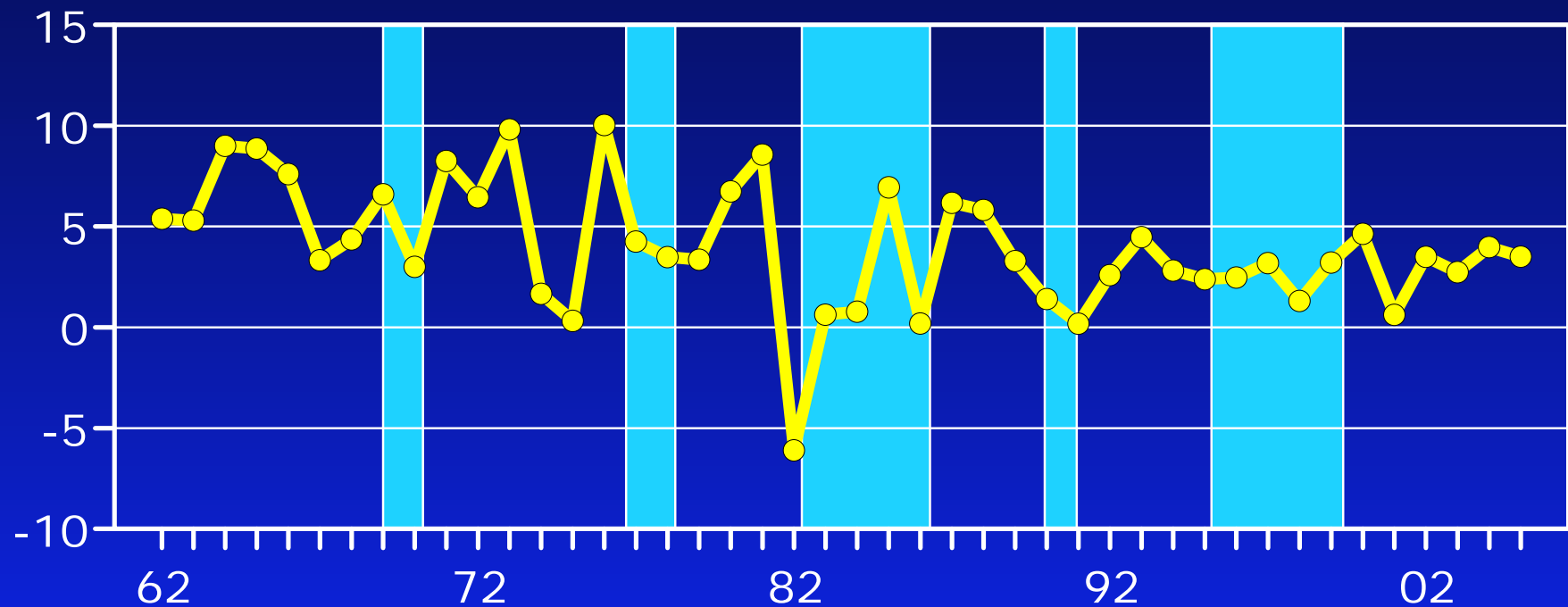
Source: Statistics Canada, CUCBC. Actual deflated by CPI. Latest: 2005
Shaded areas represent housing price recessions.



Economic growth usually lower during housing price recessions

Per Cent Change in Real GDP, B.C.

Per Cent



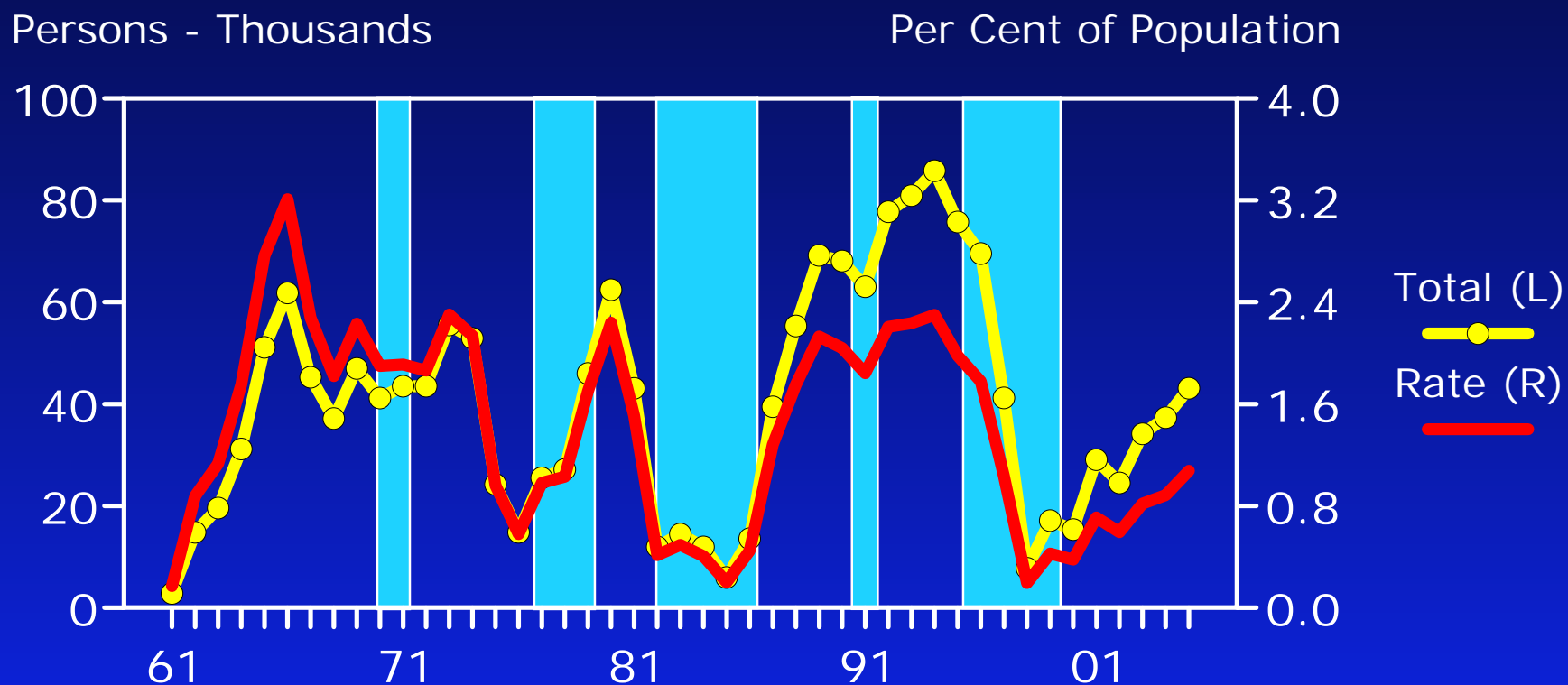
Source: Statistics Canada, CUCBC.
Shaded areas represent housing price recessions.

Latest: 2005



Drop in migration often precedes housing price peak

Total Net Migration and Net Migration Rate, B.C.



Source: Statistics Canada, CUCBC.
Shaded areas represent housing price recessions.

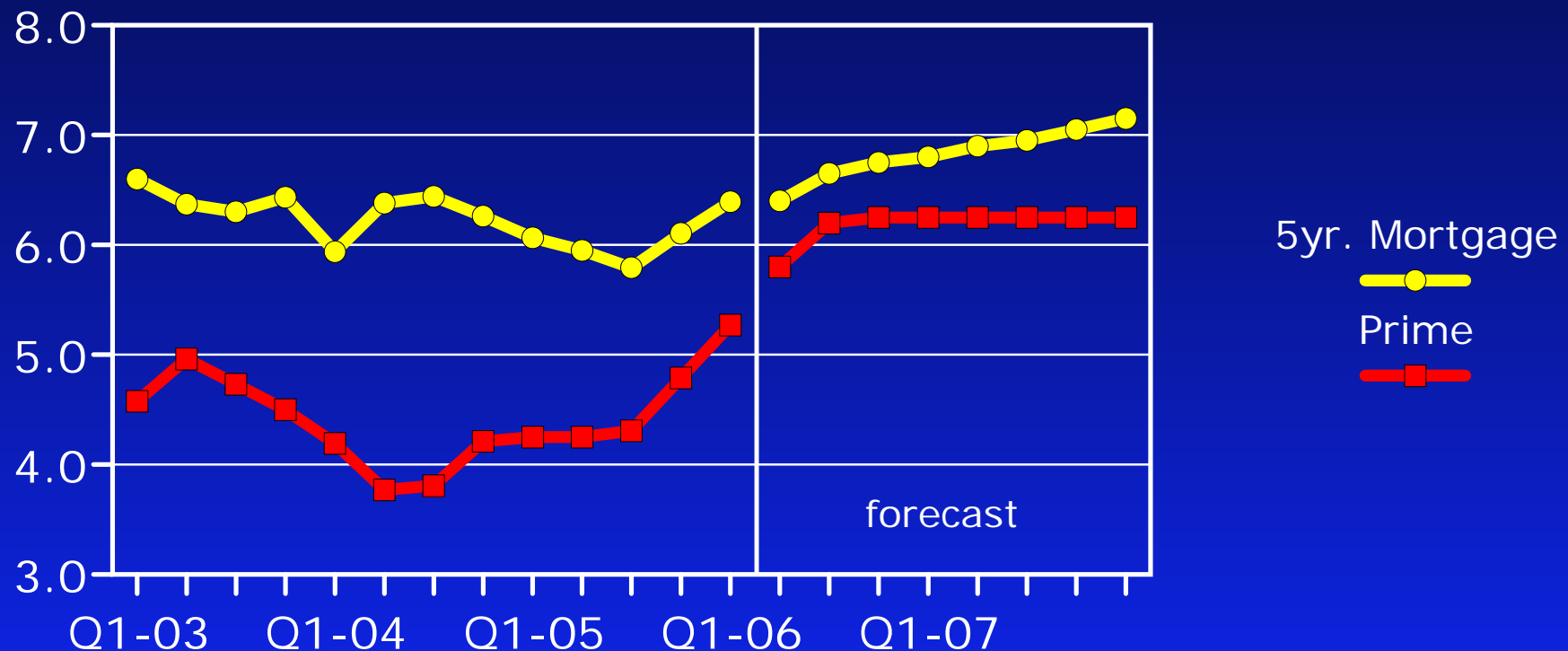
Latest: 2005



End to Bank rate increases near, modest increase in longer term rates

Interest Rate Forecast, Quarterly

Per Cent



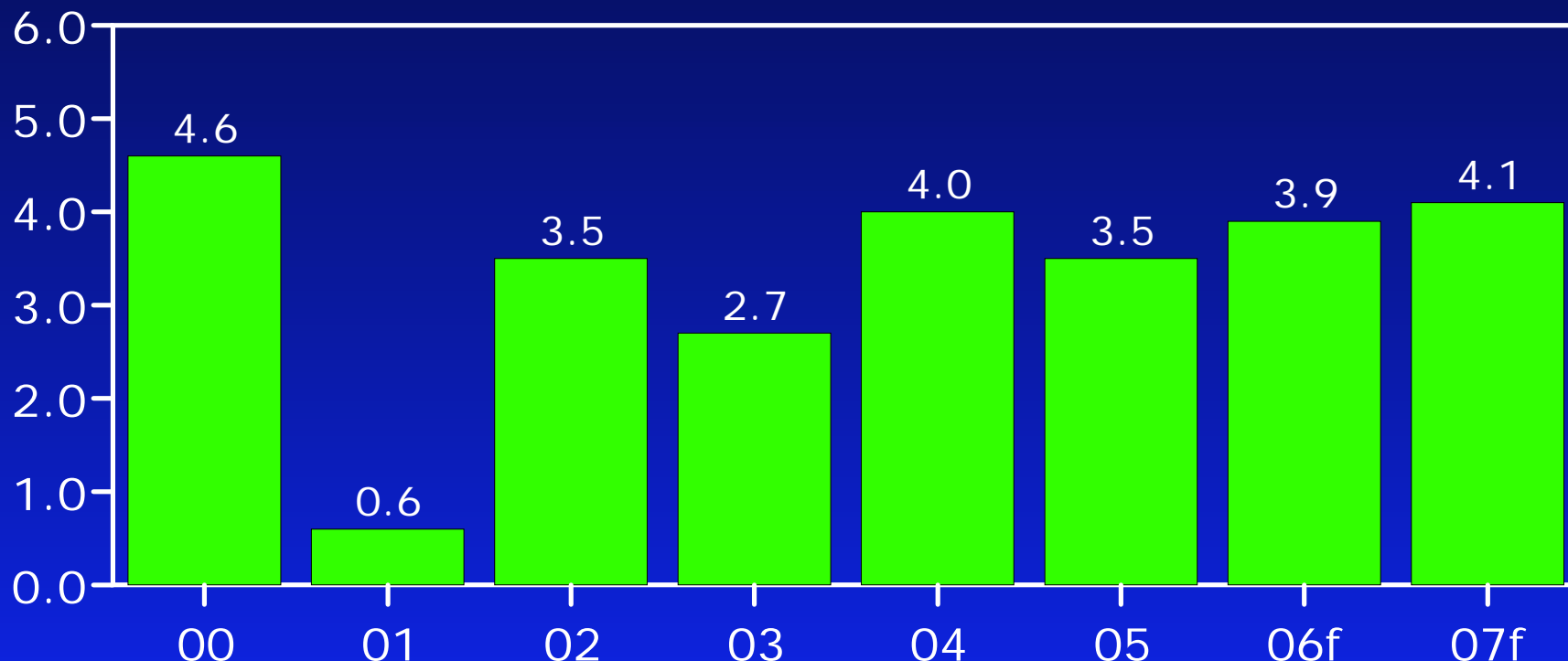
Source: Bank of Canada, CUCBC. Note: Quarter averages.



Strong economic growth next two years

B.C. Real Gross Domestic Product Growth

Per Cent



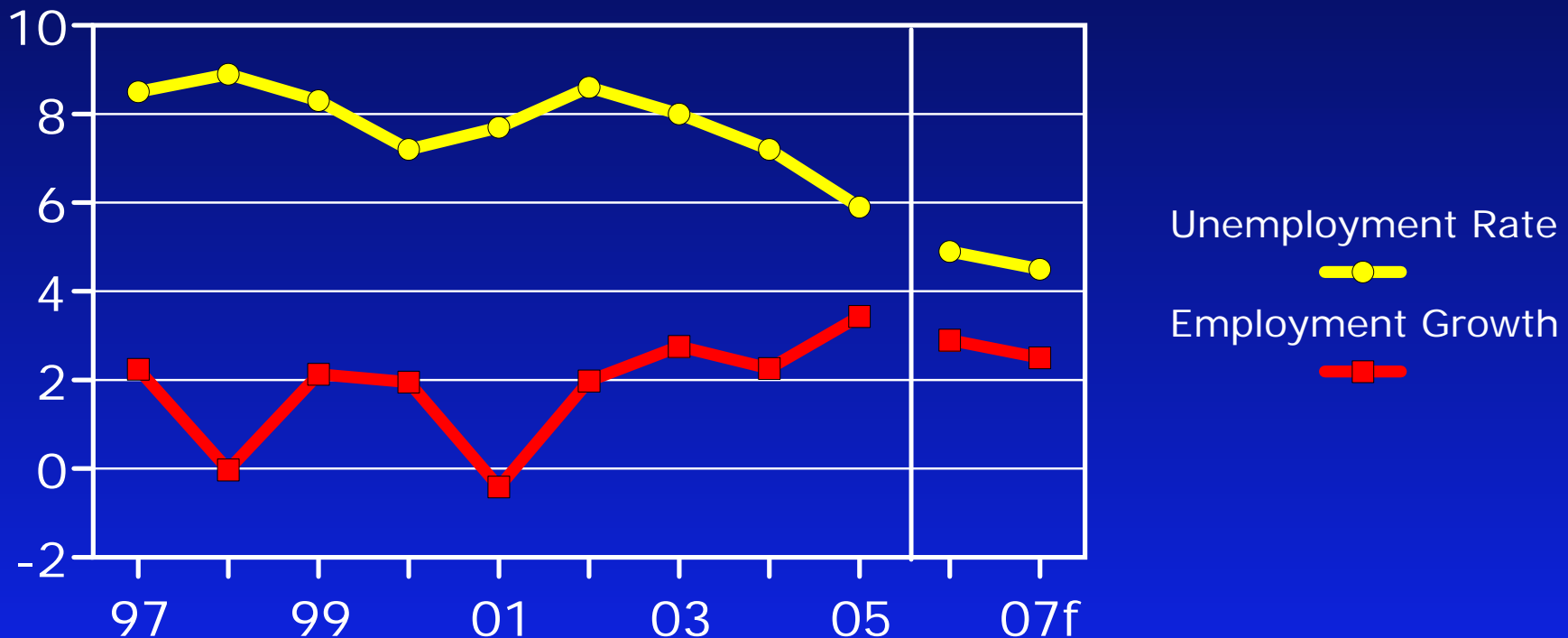
Source: Statistics Canada, CUCBC.



Tighter labour market ahead

B.C. Labour Market Indicators, Actual and Forecast

Per Cent



Source: Statistics Canada, CUCBC.



Wages rising at faster pace

Percentage Change in B.C. Fixed-Weighted Hourly Earnings

Per Cent

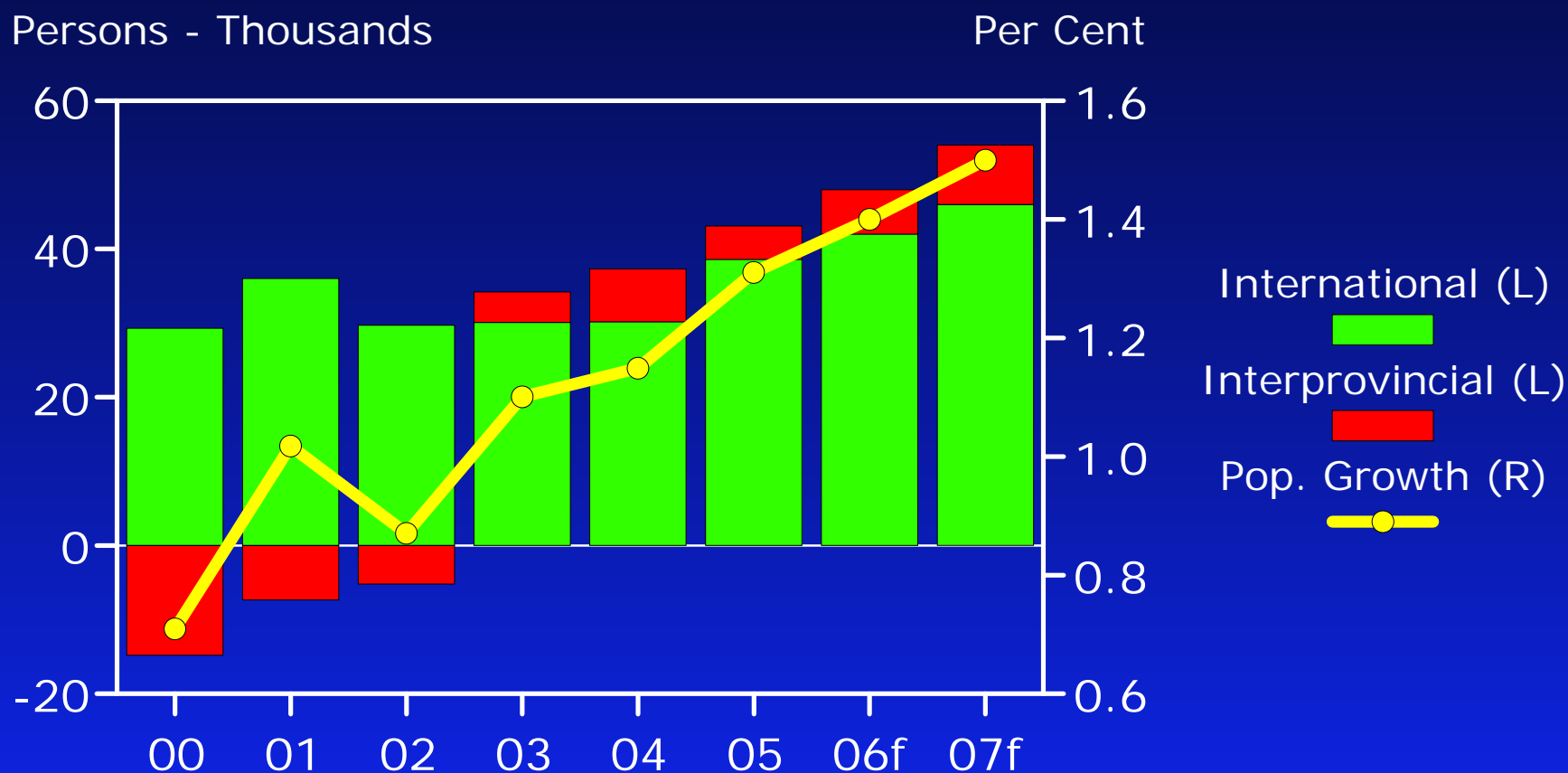


Source: Statistics Canada, CUCBC.



Migration rising

B.C. Net Migration by Type and Population Growth Rate



Source: Statistics Canada.CUCBC



Three end-of-cycle scenarios:

- Negative external event or shock occurs with sudden and large impact on housing market - prices drop more than 20% - prob. 10%
- Rising rates or economic slowdown reduces sales and excess supply results - prices drop 10% to 20% - prob. 30%
- Supply grows at faster pace than demand resulting in 'gradual soft landing' - prices fall less than 10% - prob. 60%



Further gains ahead for housing market

Housing Forecast	2004	2005	2006f	2007f
BC Housing Sales ¹ , % chg.	5.4	16.0	-4.1	6.3
BC Housing Listings ² , % chg.	11.7	-0.2	-1.3	3.6
BC Avg. Sales Price ² , % chg.	10.9	14.7	13.8	7.3
BC Housing Starts, % chg.	24.9	5.3	11.1	4.9

f = forecast, 1. Landcor Data Corp. 2. MLS Residential



For B.C. economic analysis and
information visit our
website at:

www.cucbc.com/publications/economics

Savings & Credit Unions of British Columbia

