HOUSING MARKET OUTLOOK

Canada Mortgage and Housing Corporation

Montréal

www.cmhc.ca

FALL - WINTER 2002

IN THIS ISSUE

ECONOMIC OVERVIEW

U.S. economy: sand in the gears

The U.S. economic recovery is currently experiencing some difficulties. After the brief recession period in 2001, it seemed that the recovery was well under way, with economic activity having risen 2.7 per cent in the fourth quarter of 2001 and 5.5 per cent (annual rate) in the first quarter of 2002. Since then, however, several indicators have been showing less encouraging signs. Growth slowed to just 1.1 per cent in the second quarter, industrial production is anemic, employment is down, investment spending is declining and consumer confidence has fallen considerably. As well, the manufacturing sector is still contending with a significant excess capacity. Finally, given the weakness of the global economy, the U.S. cannot very well count on external trade to give its economy a fresh boost, as evidenced by its growing current account deficit.

Fortunately, though, our neighbours to the south are benefiting from very low interest rates and an accommodative fiscal policy. But, all in all, the recovery will be more difficult than expected. It would seem that there is little risk of falling back into a recession, according to most experts, but a rather mitigated performance should certainly be anticipated for the second quarter. Growth will be positive but weak. This situation in the United States will of course have repercussions on our level of exports, as just under 85 per cent of our exports (province of Quebec) are destined to the United States.

Lastly, another sign that economic activity is slowing on the other side of the border: housing starts registered a third straight monthly decrease in August.

Canadian economy posting a better performance

Everyone is amazed and overjoyed, as the Canadian economy is showing that it has an iron constitution despite the gloomy conditions affecting our principal trading partner. The gross domestic product went up 6.2 per cent in the first quarter and 4.3 per cent (annual rate) in the second. The manufacturing sector is holding up, consumers are continuing to increase their spending, business investment is posting renewed growth and the labour market performance is phenomenal (+386,000

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jobs during the first eight months of the year). In fact, Canada is on its well way to achieving the highest growth rate among the G7 countries. And how is residential construction doing in all that? Very well, thank you. Residential construction spending rose at an annualized rate of 36 per cent in the first quarter and then eased slightly in the second quarter (-2 per cent).

Labour market: beyond all expectations

The news concerning job creation in Montréal has exceeded all expectations. From January to August, 50,500 jobs were created in the Montréal area, more than during each of the last three years. The Montérégie area was particularly dynamic, which is pointing to a very hot real estate market next year on the South Shore of Montréal.

Mortgage rates: just how low will they go?

The bursting of the speculative bubble, geopolitical uncertainty, prospects of declining corporate profits and financial scandals: all these factors have combined to cause a certain depression on North American stock markets. In Canada, the benchmark index (now the S&P/TSX composite index, formerly the TSE 300) lost 45 per cent of its value since it peaked in August 2000.

In fact, the slump on the securities market is helping the real estate market. This stagnation contributed to bringing down the bond rates and, consequently, the mortgage rates. At the time of writing, most large financial institutions were offering mortgage financing, for a five-year term, at a rate of 6.65 per cent, the lowest level since December . . . 1956.

Mortgage rates will stay at very similar levels from now until the end of the year. A small additional decrease is not impossible over the coming weeks, if the stock markets continue their descent into hell and if investors turn to the bond markets. However, once stability returns to the stock exchanges, mortgage rates will very likely start rising again. As a result, next year, these rates could go up by about 50 to 100 basis points for a five-year term. Still, with the cost of a five-year mortgage loan reaching at most 7.75 per cent, the rates will remain extremely low from a historical standpoint.

This slight increase in the rates should not overly cool down the real estate market, but it could very well curb the current sharp rise in existing home prices, as it will oblige some buyers to show greater moderation in their purchase offers. At any rate, one thing is certain: the combined effect of the price hikes on the existing home market and the increase in mortgage rates will make homeownership less accessible next year.

RESALE MARKET

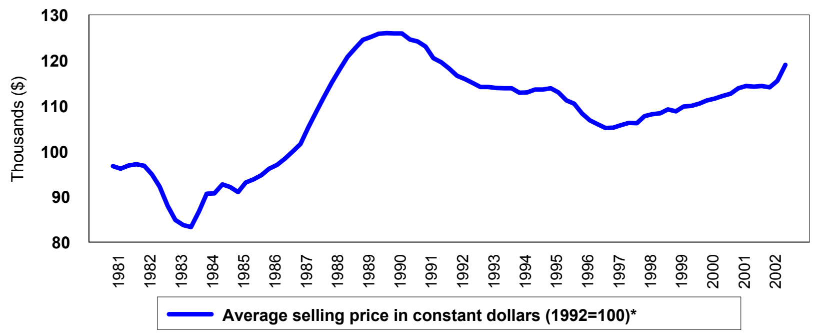
2002: a memorable year for the resale market

The year 2002 will be a memorable one for the resale market. A year ago, on account of a rather gloomy economic outlook, there was every indication that the market would slow down. And, yet, the very opposite happened. Nobody will forget the euphoria on the resale market, when properties for sale vanished like hot cakes and home prices soared. In 2002, the resale market reached a peak with 36,000 sales (+6 per cent), and all property types registered major price increases. Condominiums especially stood out, with an increase of 20 per cent in their average selling price ($140,000), practically double the hike for single-family homes ($154,000) and plexes with 2 to 5 units ($181,000).

This context is reminiscent of that which prevailed in the late 1980s, and many will remember that the market had quickly tumbled after the economy was hit by a recession in the early 1990s. Is there any cause for concern? Are we not in a speculative bubble that could burst? Several factors suggest that the real estate market will not collapse again. First, while existing home prices may be rising significantly, we should not lose sight of the fact that the market is on the point of fully recovering the ground that it lost following its collapse, during the first half of the 1990s.

There are now far fewer sellers per buyer than in 1991, and the economic conditions, along with the strong job creation in the area for the last few years, are favouring the market. But, above all, the mortgage rates and the scarcity of rental housing have been the factors supporting a strong demand on the resale market in 2002. At this time, there is every indication that, in 2003, the context will be the same and the market will remain solid. Also, many households would rather invest their savings on the real estate market than on the securities market, which is still losing speed.

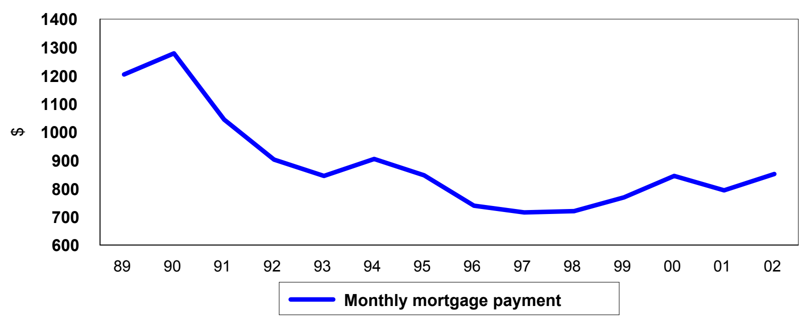
Recovery Not Yet Fully Completed
Average Selling Price* (constant dollars)
Montréal CMA



Source: CREA
*: 4-quarter moving average

Despite the fact that homes are more expensive on the market, homeownership still remains accessible. For a slightly higher price in constant dollars than the 1990 level, the monthly mortgage payments for an existing single-family house purchased in 2002 ($852*) are 33 per cent lower than in 1990 ($1,278*). The mortgage rates make all the difference on the wallet. The rate for a five-year mortgage loan stood at 13.4 per cent in 1990, compared to 7.1 per cent in 2002. Without such low mortgage rates, household budgets would have been more limited. This would make for a less dynamic market, which would have continued to recover, but at a slower pace.

Mortgage Rates Make All the Difference on the Wallet
Existing Single-Family Homes
Montréal CMA



Sources: CMHC and GMREB
Loan financed at 90%, amortized over 25 years, for a 5-year term
Average price in constant dollars (1992=100)

* mortgage loan financed at 90 per cent, amortized over 25 years, for a five-year term

Less and less choice on the market

As mentioned earlier, demand for existing homes will remain solid over the coming year. However, the market is facing a supply problem. Potential buyers have less and less choice on the market, and there is every indication that the situation will not improve in 2003. As long as the labour market continues to do well and mortgage rates stay low, the choice of properties for sale will remain very limited. Supply is all the more reduced by the fact that some potential sellers are not putting their current property on the market for fear of not finding another home, once theirs is sold. In 2003, listings will decline again (-11 per cent) and bottom out.

Resales will decline in 2003 but prices will keep rising

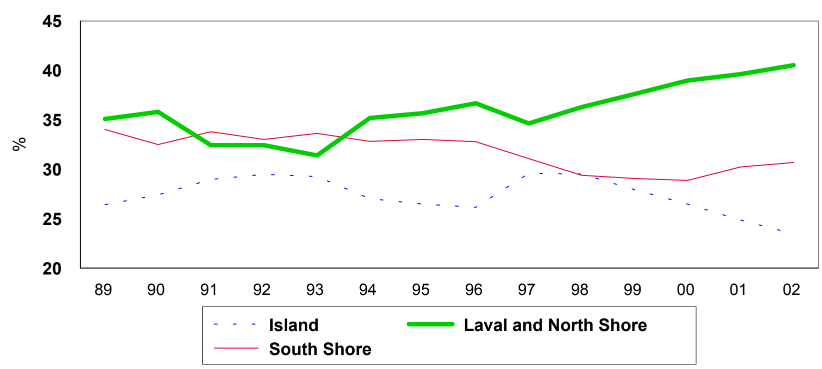
In this context of scarce supply, demand for existing homes will slow down somewhat, not for lack of any buyers, but because these buyers will not find any properties meeting their criteria and because homes will be more and more expensive. In all, 34,000 transactions will be registered through the MLS® network, down by 6 per cent. While this may be the first decrease in activity since 1995, the number of transactions will still be comparable to the level recorded in 2001, which was an excellent year. Activity will decline for all housing types. Single-family home and condominium transactions will fall by 6 per cent and plex sales will drop by 5 per cent.

The market will continue to favour sellers, which will reduce the negotiating power of buyers. Consequently, prices on the resale market will continue to record significant hikes, well above inflation. The average price for a single-family home will increase by 8 per cent ($166,000) and that for a plex will go up by 7 per cent ($193,000). As for condominiums, their average price will post a new rise of 8 per cent ($151,000), a clearly more modest gain than in 2002 (+20 per cent).

Single-family homes in the suburbs will continue to stand out

The single-family home resale market will continue to stand out in the suburbs, particularly in Laval and on the North Shore. The share of single-family home transactions in the suburbs will keep rising, to the detriment of the proportion garnered by the Island of Montréal. On a market where properties are more and more expensive, it is perfectly logical that buyers would privilege sectors where the homes are more affordable, all the more so since, with the tight rental market, many of these buyers are taking the plunge into homeownership. For example, in 2002, a buyer will have had to pay $223,000 for a single-family house on the Island of Montréal, compared to $128,000 in the Laval and North Shore sector and $135,000 on the South Shore.

Suburbs Gaining in Popularity
Distribution of Single-Family Home Resales
Montréal CMA



Sources: CMHC and GMREB

Existing Single-Family Home Market
Level of % Change, 2002 to 2003, by Submarket

	Sales		Average Price		Active Listings		Sellers per buyer	
Submarket	**2002**	**2003**	**2002**	**2003**	**2002**	**2003**	**2002**	**2003**
Island of Montréal	**5,600**	**5,400**	**223,000**	**240,000**	**1,750**	**1,500**	**4**	**3**
Change from previous year	**0%**	**-4%**	**14%**	**8%**	**-31%**	**-14%**	**--**	**--**
Laval and North-Shore	9,400	9,000	128,000	138,000	2,800	2,400	4	3
Change from previous year	5%	-4%	13%	8%	-37%	-14%	--	--
South-Shore	**7,400**	**6,800**	**135,000**	**145,000**	**2,200**	**2,000**	**4**	**4**
Change from previous year	**9%**	**-8%**	**10%**	**7%**	**-35%**	**-9%**	**--**	**--**
Total Montréal Area*	23,600	22,300	154,000	155,000	7,250	6,300	4	3
Change from previous year	5%	-6%	12%	8%	-34%	-13%	--	--

* The sum of the submarkets does not correspond to the metropolitan area on account of the MRC of Vaudreuil-Soulanges.

Source: CMHC, GMREB

The Island of Montréal is not being outdone, though, as it accounts for over 70 per cent of all condominium and plex transactions on the Greater Montréal area market. These housing types are in fact representative of its housing stock. The Island of Montréal alone effectively makes up around 40 per cent of the overall resale market (single-family houses, condominiums and plexes), for a greater market share than those of the Laval and North Shore (30 per cent) and South Shore (25 per cent) sectors.

NEW HOME MARKET

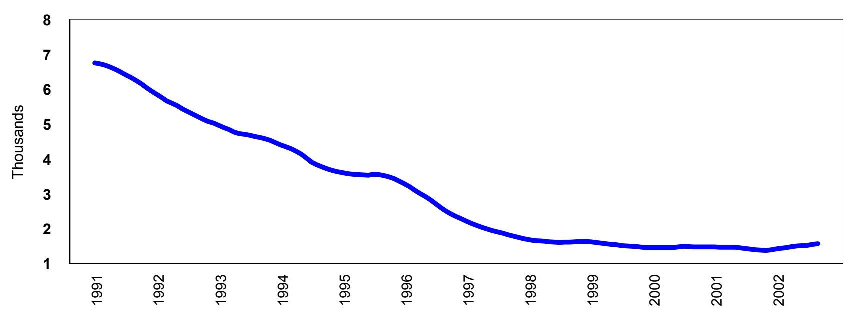
Residential construction will stay red-hot

Builders had not seen such a busy year in a long time. Residential construction will have made a major leap in the Greater Montréal area during 2002, with a total of 20,500 housing starts, or 54 per cent more than in 2001. It should be noted that the year 2002 is posting the best results in the last 11 years. Another very good year is in store for the housing sector, as construction is not about to get any less busy. In 2003, starts will continue to rise, but at a slower pace. In all, 22,500 new job sites will be enumerated over the coming year, for an increase of 10 per cent in residential construction.

Several factors account for this success. Just like the resale market, residential construction is benefiting from the prevailing economic growth, the good job creation in the Montréal area and the low mortgage rates. As well, the dynamics on the resale market are having an impact on home building. Since it is more difficult for households to find an existing property, many are turning to the new home market. This is supporting high levels of activity in the homeowner housing construction segment. In addition, with the scarcity of rental housing, apartment construction will start to grow, a trend that will further intensify during 2003.

The construction industry is in a much better position than in the early 1990s. Orders are flowing in but, above all, inventories are very low. There is no over-construction, and this is another factor suggesting that housing starts will stay high in 2003. At essentially comparable levels of activity, the inventory of new unoccupied homes was nearly six times smaller at the end of September 2002 than at the beginning of 1991. The life of the inventory is also shorter: 0.9 months in September 2002, compared to 3.6 months at the end of 1991.

Inventories at Low Levels
Total Completed but Unoccupied Units
Montréal CMA



Source: CMHC
12-month moving average

New Single-family Home Market
Level of % Change, 2002 to 2003, by Submarket

Submarket	Sales 2002	Sales 2003	Sales Chg.	Average Price / Detached 2002	Average Price / Detached 2003	Average Price / Detached Chg.	Average Price / Semi-Detached 2002	Average Price / Semi-Detached 2003	Average Price / Semi-Detached Chg.
Island of Montréal	**1,400**	**1,300**	**-7%**	**300,000**	**319,000**	**6%**	**182,000**	**195,000**	**7%**
Laval and North-Shore	5,700	5,800	2%	**180,000**	**188,000**	4%	**127,000**	**133,000**	5%
South-Shore	**3,500**	**3,800**	**9%**	**172,000**	**181,000**	**5%**	**128,000**	**136,000**	**6%**
Total Montréal Area*	11,700	12,000	3%	**190,000**	**199,000**	5%	**146,000**	**155,000**	6%

* The sum of the submarkets does not correspond to the metropolitan area on account of the MRC of Vaudreuil-Soulanges.

Source: CMHC, GMREB

2003 will be another good year for single-family homes and condominiums

The growth that began a few years ago in the homeowner housing construction sector will continue next year, but at a slower pace than in 2002. Essentially, this market segment will still be benefiting from the scarce supply on the resale market. After posting a spectacular gain in 2002 (+49 per cent), single-family home building will rise again in 2003. A total of 12,000 new sites will be enumerated, for an increase of 3 per cent. As for condominiums, their growth will be exceptional in 2002 (+54 per cent), but will slow down slightly next year, as such starts (5,700 units) will sustain a small decrease of 2 per cent. Once again, the suburbs will continue to attract homeowners, which explains why the single-family home segment will record an increase, while the condominium segment will have a somewhat less prosperous year.

On account of the labour shortage and the rising costs of construction materials, new home prices will go up by about 5 per cent. As a result, the average price of a new single-detached house will attain $199,000 and that of a new semi-detached home will reach $155,000. Demand will continue to be concentrated in the mid to upper ranges, that is, $150,000 or over for detached homes and $125,000 for semi-detached houses.

Condominiums, for their part, are favoured by both builders and buyers. First-time buyers appreciate dwellings of this type on account of their low cost, and baby boomers like them because they want a smaller home requiring less maintenance. Units priced between $150,000 and $200,000 remain the winning formula. It is not that there is no longer any interest in upper-range condominiums, but rather that this market is currently quite well served in the more upscale sectors on the Island of Montréal.

Geographical distribution: same dynamics as on the existing home market

The geographical distribution of single-family home and condominium starts is the same as that of existing home sales. Almost all single-family home starts (around 80 per cent) are in the suburbs, while more than half of all condominium job sites are concentrated on the Island of Montréal (around 60 per cent). For reasons of affordability, the single-family home market is performing better in the suburbs. Condominiums are an urban product that makes perfect sense in large cities, where homes are generally more expensive. This is why the condominium market is mainly concentrated and developed in Montréal.

RENTAL MARKET

Slightly more units under construction...

Finally, rental housing construction is waking up to a certain extent. From January to September, such starts increased by 153 per cent. Even with this apparently spectacular result, the level of activity remains low. During the first nine months of the year, foundations were laid for 2,179 rental units, while a total of 3,000 starts is forecast for this year. Like for the other housing types (single-family homes and condominiums), this will consequently be the best year since 1991. However, a major difference can be noted between these two years: in 1991, the vacancy rate stood at 7.2 per cent, which suggests that there was some speculative building while, in October 2001, this rate was just 0.6 per cent. We were now therefore entitled to anticipate a vigorous recovery in rental construction. Even with some renewed activity this year and an impressive number of households having left the rental market to access homeownership, this will not be sufficient to reverse the downward trend in the vacancy rate that has now been prevailing for the past seven years.

... but slightly fewer units available for rent

Although there has been an increase in the supply, it will not be able to offset the heavily inflated demand resulting from employment gains among young people and the massive arrival of newcomers in the Montréal area. The 42,000 jobs that have gone to young people aged from 15 to 24 years in the last four years will continue to prompt the formation of young households and, consequently, to stimulate demand for rental housing. Also, last year, the Montréal metropolitan area saw over 25,000 newcomers swell the ranks of its population. By comparison, this is nine times more than in 1996.

As a result, the rental market has tightened even more in the Greater Montréal area. Our current rental market survey, the results of which will be known in November, should reveal a vacancy rate of just 0.3 per cent, the lowest level ever recorded.

Little improvement in sight for 2003

Next year, activity will intensify on job sites, as 4,800 starts are anticipated. The *Affordable Housing Québec* and *Accès-Logis* programs will give a boost to the construction of social or community housing, as well as privately initiated dwellings (for the terms and conditions of these programs, visit the site www.shq.gouv.qc.ca).

Under the private component of the *Affordable Housing Québec* program, in which the federal government participates, through CMHC, financial assistance is granted for the production of affordable housing units. Without this assistance, it would be difficult, even impossible, to produce such dwellings, given the high construction costs that would command much higher rents than the current market rates—if any profits were to be made.

Even with these efforts made by all levels of government, the improvement in the situation will be slim if demand continues to soar the way it is going now. We forecast that the vacancy rate will begin to rise again very slightly, reaching 0.5 per cent in 2003. It will therefore remain hard to find a dwelling, and the rental market will continue to favour landlords. For this reason, we anticipate rental increases of about 4 per cent in 2003.

As well, retirement home construction, which offers greater profitability to developers on account of the higher rents, will continue at a rate of around 1,000 units per year. A few large projects of this type are already planned for next year in the eastern part of the city of Montréal, notably in Saint-Léonard.

Outlook over the longer term

Since the real estate market is not perfectly synchronized with job creation, it should be able to benefit until 2004 from the jobs created during 2001 and 2002 in the Montréal area. In general, it takes around five quarters on the existing home market and eight quarters on the new home market before the impact of job creation can be observed. However, if a slightly larger increase in mortgage rates is noted, this could slow down the market and curb the growth in prices. While the real estate market is going full tilt thanks to historically low mortgage rates, it is quite obvious that the risks associated mortgage loans are greater. When their mortgages come up for renewal, many households could find themselves in a less favourable financial position if, in a few years, mortgage rates are somewhat higher than they are now.

There is good reason to keep an eye on the changes in the economy of our neighbours to the south that will have an impact on ours. In the event of a recession, the real estate market would slow down. It is unlikely, however, that a collapse like that which occurred in the early 1990s will happen again. As mentioned earlier, the real estate market is now in a much better position than it was in the early 1990s. On the resale market, the supply of properties for sale has bottomed out, and seller-to-buyer ratios have never been so low. The residential construction industry, for its part, is better managing its inventories, and there is much less building on speculation. Major projects are started up when a sufficient number of units have been presold. Also, we should not lose sight of the fact that the scarcity of rental housing is another factor indicating that, in the event of a slowdown, the rental market will not be in a position to deteriorate rapidly. In fact, several indicators show that the real estate market is solid. Should there be a slowdown, the market could possibly sustain a decrease, but such a decline would be much more modest than that which it sustained at the time of the last recession.

For more information about this publication, please contact:

Sandra Girard, Marie-Christine Rioux or Paul Cardinal

Market Analysts

at

1 866 855-5711

Forecast Summary

Montréal Metropolitan Area
October 2002

	2000	2001	2002*	2003*	Chg. (%) 2002 vs 2001	Chg. (%) 2003 vs 2002
RESALE MARKET						
MLS Sales (1)						
Single-family houses	20,058	22,501	23,600	22,300	5%	-6%
Condominiums	5,184	6,188	6,700	6,300	8%	-6%
Plexes (2 to 5 units)	4,313	5,295	5,700	5,400	8%	-5%
Total	29,555	33,984	36,000	34,000	6%	-6%
Active MLS listings						
Single-family houses	13,076	10,989	7,300	6,300	-34%	-14%
Condominiums	3,718	2,915	1,800	1,700	-38%	-6%
Plexes (2 to 5 units)	4,340	3,586	2,300	2,200	-36%	-4%
Total	21,133	17,490	11,400	10,200	-35%	-11%
Average MLS price						
Single-family houses	132,362	137,907	154,000	166,000	12%	8%
Condominiums	114,241	116,337	140,000	151,000	20%	8%
Plexes (2 to 5 units)	153,776	163,078	181,000	193,000	11%	7%
NEW HOME MARKET						
Housing Starts						
Single-family houses	7,551	7,868	11,700	12,000	49%	3%
Condominiums	3,539	3,763	5,800	5,700	54%	-2%
Rental housing units	1,676	1,669	3,000	4,800	80%	60%
Total	12,766	13,300	20,500	22,500	54%	10%
Average new house price						
Detached houses	169,233	177,000	190,000	199,000	7%	5%
Semi-detached houses	129,775	140,000	146,000	155,000	4%	6%
RENTAL MARKET						
Vacancy rate (October) (%)	1.5	0.6	0.3	0.5	--	--
Change in rents (%)	1.2	4.2	4.0	4.0	--	--
ECONOMIC OVERVIEW						
Mortgage rate 1-year (%)	7.8	6.1	5.1	6.3	--	--
Mortgage rate 5-year (%)	8.2	7.4	7.1	7.8	--	--
Employment (in thousand)	1,690	1,706	1,755	1,790	2.9%	2.0%
Job creation or loss (in thousnad)	34	16	49	35	--	--
Unemployment rate (%)	7.7	8.2	8.2	8	--	--

1 The publication of MLS data is made possible thanks to the cooperation of the Greater Montréal real estate Board.
** CMHC Forecast*
Sources: CMHC, GMREB and Statistic Canada

HOUSING MARKET OUTLOOK is CMHC's forecast for new home and resale markets published twice a year for the Montréal area. Issues are released in the Spring and fall of each year. For more information, please contact Customer Service Centre at 1 866 855-5711.