HOUSING MARKET OUTLOOK

Halifax CMA

Canada Mortgage and Housing Corporation

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Competition Intensifies as Market Contracts

The overall pace of residential construction activity across metro Halifax is expected to ease through the end of next year. While the slump in the traditional single-detached homebuilding sector is forecast to continue, growth in renovation spending and a brisk pace of apartment development will provide some buoyancy to an otherwise soft new construction market.

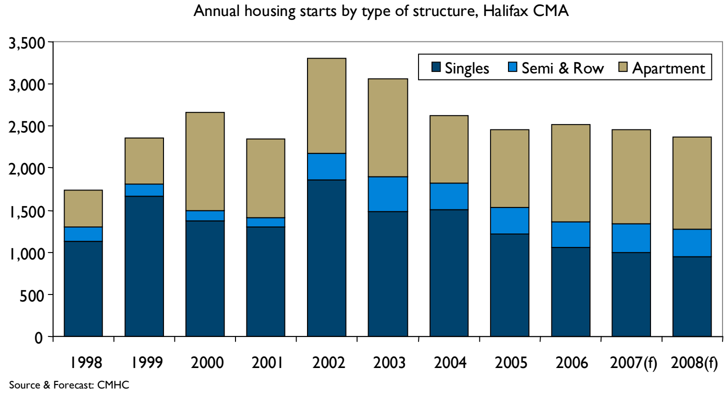
Annual total housing starts are expected to slip 2.4 per cent to 2,450 by the end of this year and another three per cent next year with 2,375 units forecast to break ground. Both single-detached and multiple unit housing starts are forecast to decline moderately in 2007 and 2008. However, while single-detached units are expected to slide to the lowest annual production level in 15 years, multiple unit starts are projected to remain well above the annual average over that same period. As a result, single starts will only contribute

In this Issue

Figure 1

Housing Starts Slide as Single-Detached Homebuilding Sags

Annual housing starts by type of structure, Halifax CMA



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41 per cent of annual total housing starts in 2007 and 2008, in sharp contrast to the 66 per cent share single starts contributed ten years ago.

There are several important factors contributing to the increase in the multiple unit share of total new residential construction activity. From a demographic perspective, household formation is occurring at a faster pace than population growth as baby boomers become empty nesters and their children look for new housing. This phenomenon is generating strong growth in households of one or two persons who often inhabit a multi-unit dwelling either for financial or lifestyle reasons. Young couples may choose to rent or to own a condo for affordability reasons while more mature households may choose a quality apartment or townhouse for ease of maintenance.

From a market perspective, developers are also increasing the size of multi-residential projects as they attempt to manage rising development/construction and operating costs through economies of scale. There may not necessarily be more apartment structures started this year or next compared with recent years, but new buildings will be considerably larger on average than has been true over the past five years. Furthermore, homebuilders are encountering stiff competition from an expanding inventory of substantially renovated homes listed for sale on the resale market which may offer potential buyers the option to live in more mature, established neighbourhoods.

This decided shift in market share of residential construction activity will create both challenges and opportunities within the industry. Homebuilders can expect to find the going tough in the $300,000 to $400,000 price range which just three years ago was sufficiently strong to support widespread speculative construction activity. Fortunately, opportunities for builders will still be found in value-driven semi-detached and townhouse markets through the end of next year, particularly for energy-efficient and technologically-advanced product offerings. Alternatively, homebuilders will find opportunities in the custom new home sector as a larger share of a more discerning homebuyer profile refuse to settle for anything less than the best when building a dream home. This will contribute to strong price growth among new single-detached homes, albeit at a somewhat slower pace than the double-digit growth witnessed over the past two years.

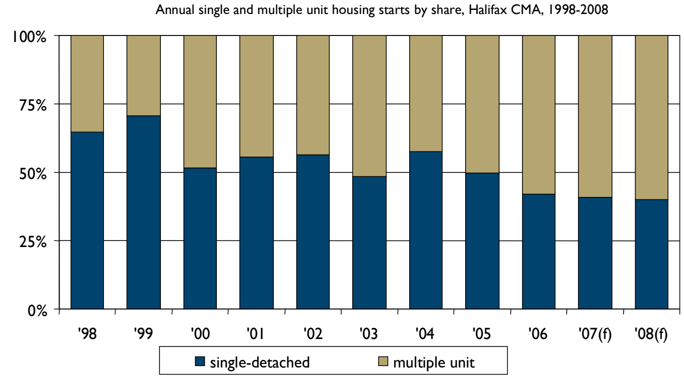
Finally, the combination of rising home purchase transaction costs and potential buyers' demonstrated preference for established neighbourhoods will support further growth in renovation activity which also will be supported by resilient property values, low mortgage rates and increasing liquidity of home equity. While this may generate competition for builders in the medium or long term if those owners decide to list their home for sale, it will provide short term opportunity for builders interested in tackling the unique challenges associated with the renovation business.

In the apartment sector, a boisterous pace of high quality new rental construction will challenge both older rental stock and condominiums for potential occupants. Many renters are expected to 'move-up' into new rental projects when the opportunity arises while those considering renting an apartment or buying a condo may opt for renting to avoid escalating property tax bills and condo fees. This will challenge owners and managers of existing rental properties to attract and keep tenants while it will encourage condo developers to become more innovative to differentiate their product and related lifestyle features

Figure 2

Multi-Unit Housing Starts Account for Almost 60% of Total

Annual single and multiple unit housing starts by share, Halifax CMA, 1998-2008

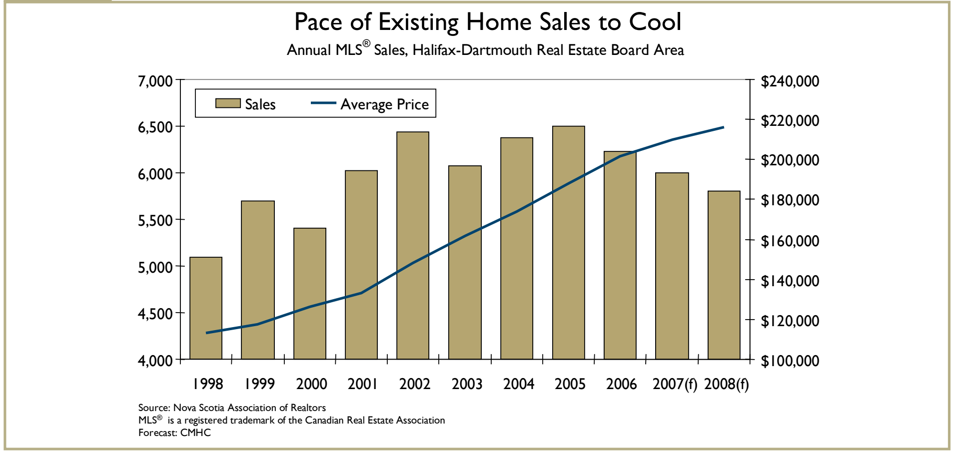


Source & Forecast: CMHC

from an increasingly crowded competitive marketplace.

Although the residential construction market continues its descent from the recent cyclical peak, mortgage rates remain low and demographic trends are providing new opportunities for builders and developers. The key challenges facing the industry over the next two years will be managing high and rising construction costs and satisfying more demanding and knowledgeable housing consumers. As competition across and among all sectors of the industry intensifies, those builders and developers who offer innovative and unique products and who customize their services to meet the exacting needs of their customers will be rewarded for their efforts.

Figure 3



Strong Pace of Existing Home Sales to Cool

Sales of existing homes have reached record levels in Metro Halifax in recent years. Annual sales have averaged nearly 6,300 since 2001 and reached a peak in 2005 at 6,500 sales. The economic and demographic conditions that contributed to these elevated sales volumes have begun to shift since the peak in 2005. Historically low interest rates have nudged up slightly; homeownership costs have been rising including property taxes, heating and electricity costs; strong employment figures have begun to flatten with little growth in the labour market; population growth has slowed; and net-migration patterns have become less favourable than in the recent past. Furthermore, based on CMHC's annual *Consumer Intentions to Buy or Renovate Survey*, the number of first-time home buyers appears to be decreasing. These factors contributed to a four per cent decline in MLS® sales in 2006 and are expected to exert continued pressure in 2007 and 2008.

As the labour market continues to tighten in Halifax, real wages will begin to rise. While this may result in some inflationary pressures in the longer-term, the short-term impact will result in more disposable income and some of the improved consumer confidence that was seen in late 2006 and early 2007.

The effect of strong consumer confidence combined with unusually mild weather conditions and plenty of "like new" inventory of renovated homes contributed to record levels of sales in the early months of 2007. Over the first three months of the year sales exceeded 1,600 – an 11 per cent increase over the same period in 2006. In spite of such strong numbers, it is expected that some of the aforementioned factors will contribute to more sluggish sales levels in the second half of the year.

Overall, sales of existing homes are expected to decline about four per cent in 2007 and another three per cent in 2008. Without further labour market growth, it is expected that sales will remain subdued for the foreseeable future.

At the time of publication, the number of active MLS® listings in Metro Halifax was nearly 3,400. It is expected that this number will peak in June at around 3,800. At these levels there is less than six months inventory of existing homes based on anticipated sales. With tightening inventory levels a few effects may follow. One is that price growth will accelerate and the market will begin to shift to more friendly sellers' conditions reversing the recent trend. Another effect is that with a limited selection of existing homes there will be an increase in demand for custom-built homes. Yet another effect is that with rising prices for both existing homes and new home construction, owners may opt for renovating their current homes.

The existing inventory provides a variety of housing options. Over one-third of active listings are below $200,000 and might be considered entry level. About 40 per cent are between $200,000 and $300,000 and the remaining quarter of the inventory is above $300,000.

In the past five years, the average selling price of an existing home has grown by an average of eight per cent per year. In 2006, the average price reached nearly $202,000 – an increase of seven per cent compared to 2005. With the recent blitz on home sales and inventory levels barely keeping pace, it is expected that MLS® sales prices will rise another four per cent in 2007 reaching about $210,000. Given the anticipated reduction in sales, price growth will slow in 2008 to about three per cent.

Shifting market conditions will put more pressure on the resale home market. Buyers will be expecting to find bargains while sellers will be expecting to maximize gains. Realtors® will be working as hard as ever to reconcile clients' demands and to close deals in this balanced market.

Rising Rental Stock Leads to More Vacancies

Last year was a banner year for rental starts in Metro Halifax. The almost 900 units that began construction in 2006 was nearly double the amount started in 2005. Since 1999, rental starts have averaged a very high 680 units per year and the demand for new units is expected to continue.

Over the next 18-24 months, completions are expected to catch up to some of the ground breaking activity that took place in 2006. Starts will remain strong hovering near the recent annual average. The number of units completed will outpace the number of new starts over the next couple of years. In 2007, completions will be about three times what they were in 2006.

Recent strong economic conditions and favourable demographic trends in Metro Halifax led to high levels of household formation. In particular, the children of the baby boomers have begun leaving the nest and are taking advantage of the opportunities presented by a strong economy. This trend has led to increased demand for rental units and has pushed vacancy rates downward.

In recent years, vacancy rates plummeted from a high of 8.7 per cent in 1996 to a low of 2.3 per cent in 2003. With the average vacancy rate below three per cent for the past several years investors and developers responded to the demand with many new apartment projects. However, given the recent high levels of new construction and the number of soon-to-be completed projects, competition for tenants will begin to heat up and more units will become empty. With all the new rental products on the market it is expected that the overall vacancy rate in Metro will rise from 3.2 to 3.5 per cent in 2007 and rise again in 2008 to about 3.8 per cent.

It is expected that recently and soon-to-be completed buildings will have little trouble filling their units so long as the asking rents are within a reasonable range. As is the norm, higher-end units and luxury units will take longer to rent up. The segment of the market that will be most affected by increased vacancies are older buildings. Older buildings tend to feel the pain of rising costs faster than their newer counterparts due to less energy efficiency, more maintenance costs and less flexibility with raising rents. Older stock will face more difficulty in finding and retaining tenants. Landlords will find it difficult to manage ever-increasing costs and will be forced to sharpen their pencils to make the numbers work.

Average rents in Halifax are expected to rise by about three per cent in 2007 and by another two per cent in 2008. While new buildings will be asking higher rents than ever, the overall stock of rental units will be weighed down by rising vacancy rates. In spite of rising costs, there will be a strong desire to attract and retain tenants than to risk additional vacancies.

Confident Consumers Bolster Vigorous Economy

A combination of tight labour market conditions, tepid inflation and home equity gains have consumers able and willing to spend with confidence. With these conditions forecast to persist through the end of next year, a vigorous metro Halifax economy is expected to continue to be supportive of housing demand over the forecast horizon.

Over the past two years, local annual employment growth stalled at less than one per cent while the unemployment rate has hovered near the five per cent mark. Reports of skilled labour shortages have become more common, suggesting that the stall in labour force expansion may actually have restrained potential growth in employment and related economic growth. Nevertheless, tight labour market conditions have put upward pressure on wages and real income gains are supporting the extension of a prolonged and impressive run in consumer spending, which boasted growth of almost nine per cent last year. This is further bolstered by the absence of any erosion in home equity as the homeownership market shows little indication of an impending correction. Confident consumers are expected to be the driving force behind healthy economic growth in metro Halifax through the end of 2008.

Through the first four months of this year, an expanding labour force has accommodated a rebound in job growth which is expected to result in a net increase of approximately 3,200 jobs this year and roughly another 2,000 next year. Most of this increase in employment is expected to occur in the service sector. Research in Motion has begun construction on their new technical support centre in Bedford with intentions to build a team of up to 1,200 while several financial services companies have announced plans to setup offices in Halifax as well. This will complement a bustling expansion in the retail sector which is also providing some buoyancy to the construction industry as activity eases on the residential side. Unfortunately, manufacturing will continue to struggle with a $0.90 Canadian dollar and intense global competition. The impending closure of Moirs chocolate factory and the loss of almost 600 jobs in Dartmouth are the most recent examples of the challenges faced by the manufacturing sector, although military spending on equipment is expected to partially offset losses elsewhere.

Mortgage rates are also expected to remain supportive of homeownership demand. A combination of a slowing economy, strong Canadian dollar vis-à-vis the U.S. dollar, and moderate inflation will help keep Canadian interest and mortgage rates low over the remainder of this year and in 2008. Short-term mortgage rates will also ease as the prime rate nudges down over the next 12 months while the long-term mortgage rates will rise slightly in line with bond rates. One, three and five-year posted mortgage rates are forecast to be in the 5.75-6.75, 6.00-7.00, and 6.25-7.25 per cent ranges respectively over the rest of this year and in 2008.

Forecast Summary Halifax CMA Spring 2007	2004	2005	2006	2007f	% chg	2008f	% chg
Resale Market							
MLS® Sales	6,371	6,496	6,228	6,000	-3.7	5,800	-3.3
MLS® New Listings	8,973	10,480	10,701	10,800	0.9	10,500	-2.8
MLS® Average Price ($)	173,922	188,115	201,734	210,000	4.1	216,000	2.9
New Home Market							
Starts:							
Single-Detached	1,510	1,216	1,056	1,000	-5.3	950	-5.0
Multiples	1,117	1,235	1,455	1,450	-0.3	1,425	-1.7
Semi-Detached	142	146	154	175	13.6	160	-8.6
Row/Townhouse	166	169	154	160	3.9	160	0.0
Apartments	809	920	1,147	1,115	-2.8	1,105	-0.9
Starts - Total	2,627	2,451	2,511	2,450	-2.4	2,375	-3.1
Average Price ($):							
Single-Detached	233,914	263,663	292,665	317,000	8.3	336,000	6.0
Median Price ($):							
Single-Detached	209,900	235,900	267,000	298,000	11.6	314,000	5.4
New Housing Price Index (% chg.)	2.0	2.8	4.3	2.5	-	2.0	-
Rental Market							
October Vacancy Rate (%)	2.9	3.3	3.2	3.5	0.3	3.8	0.3
Two-bedroom Average Rent (October) ($)	747	762	799	820	2.6	840	2.4
Economic Overview							
Mortgage Rate (1 year) (%)	4.80	5.80	6.30	6.40	0.10	6.29	-0.12
Mortgage Rate (5 year) (%)	6.05	6.30	6.45	6.63	0.18	6.80	0.17
Annual Employment Level	202,300	202,500	204,800	208,000	1.6	210,000	1.0
Employment Growth (%)	3.5	0.1	1.1	1.6	0.4	1.0	-0.6
Unemployment rate (%)	6.0	5.8	5.0	4.9	-	4.6	-
Net Migration	899	-179	326	600	84.0	750	25.0

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Source: CMHC (Starts and Completions Survey, Market Absorption Survey), adapted from Statistics Canada (CANSIM), Nova Scotia Association of Realtors, Statistics Canada (CANSIM)

NOTE: Rental universe = Privately initiated rental apartment structures of three units and over

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