

Urban Futures' By The Numbers - US Housing Starts -

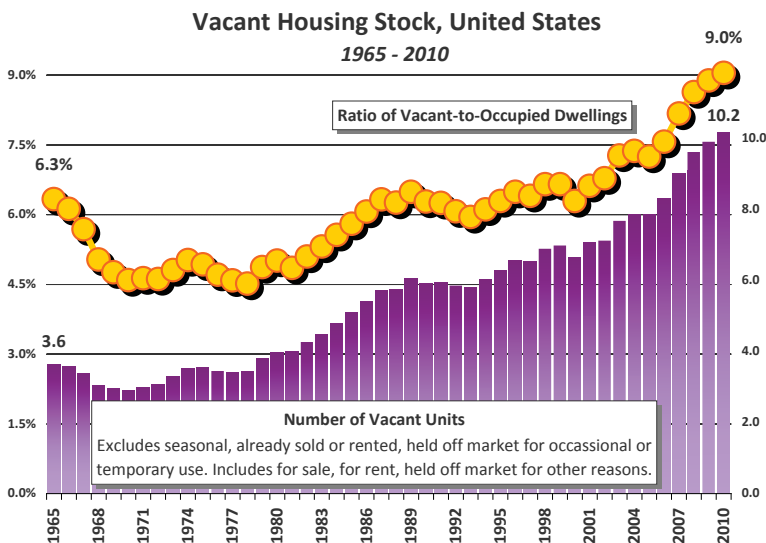
Factors impacting the United States' housing market, and in particular new residential construction, are of significance not only to those south of the 49th parallel, but to residents in many regions throughout Canada who depend on the US as a destination for wood product exports. It is within the context of 61 percent of BC's, 15 percent of Quebec's, and eight percent of Alberta's lumber exports (by value) going to the United States that a short-term outlook for recovery in the US housing market is considered.

The future of the residential construction industry in the US will be shaped by three distinct factors which, while related, are currently pulling the market in different directions. The first, and most fundamental, is on the supply side: the dead hand of the past represented by the staggering inventory of vacant dwellings which, to this point in time, continues to grow. In addition to their potential to absorb a share of any new housing demand, their depressed values are working to further hold down the value of both the existing stock and new construction.

The second factor is the persistently high level of unemployment in the US, which saps demand for both the existing stock and new construction. Until a growing share of the workforce not only has a regular pay cheque once again but also some confidence that they will continue to have one, demand for both the existing stock and new construction will continue to be depressed.

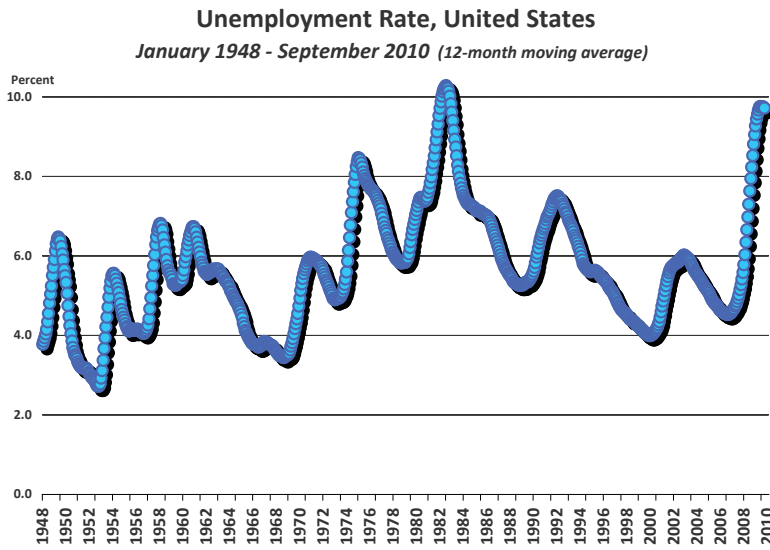
In spite of the dark shadows cast by excess supply and weak demand due to economic conditions, demographic change and the need to house a growing and changing population may provide some light. In time a growing population will both eliminate the excess supply of vacant units and move the market back towards healthy levels of new construction. Thus, in terms of fundamentals, the question is not *if* demand will return, but rather *when*. The following sections briefly consider these issues and provide an outlook for the recovery of housing construction in the United States.

Excess Inventory



Current estimates show that there are over ten million vacant housing units in the United States (not counting units that may be seasonally, occasionally, or temporarily occupied). This represents a nine percent vacancy ratio, meaning that for every 100 occupied units there are nine that are standing vacant. If the long-run average vacancy rate of 6.3 percent (which prevailed from 1986 to 2000) can be considered a benchmark, then using this ratio would see total vacancy in the range of 7.1 million units today. This points to roughly 2.9 million units that the market must absorb before it returns to normal conditions. As this represents almost two years of housing starts at long-run average levels, the scale of current vacancy could impose significant drag on construction activity in the coming years.

Unemployment

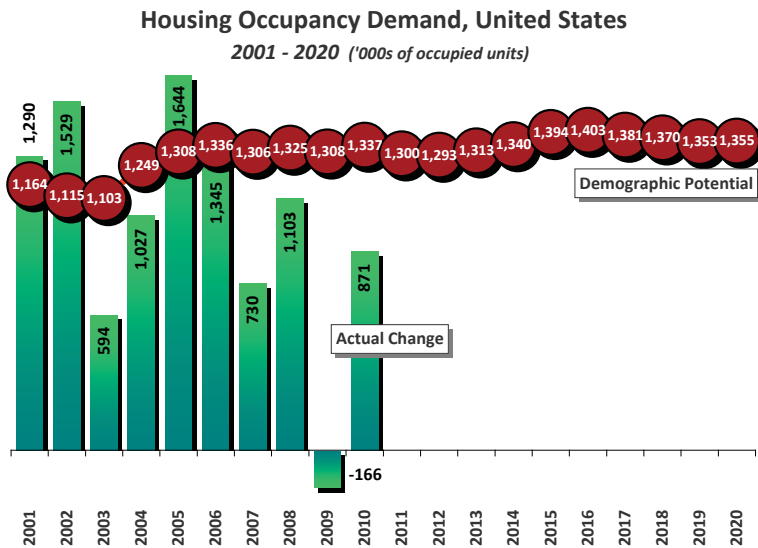


Only once before in the post-World War II period has the US unemployment rate been in the ten percent range that it currently sits in. The shock of this high unemployment rate has put downward pressure on both sales and construction activity and, to the extent that it remains high, it will continue to do so.

While the past two months have seen the unemployment rate begin to ease, if history is any indication it could take up to five years to return to the average six percent level that prevailed over the mid-1960s to mid-2000s period. Housing demand will still grow, but it will do so only slowly, as it will take time for employment to grow and the unemployment rate to fall back towards long-run average levels.

Demographics and Demand

What may serve to counter these short- and medium-term challenges is the reality that over the long-term a growing and changing population needs to be accommodated. Current estimates are that over the next ten years the population in the United States will grow by 34 million people, the equivalent of a current-day Canada.



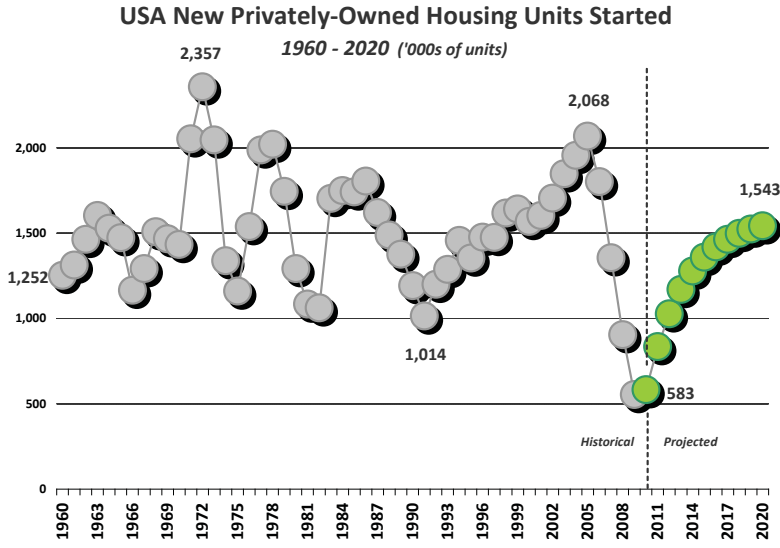
This reality can be measured as occupancy demand, which at its core is a function of the demographic composition of the population and their lifecycle housing preferences. Occupancy demand, however, is constrained by incomes and prices, resulting in short-term disconnects between actual and potential occupancy. For example, over the past decade, annual increases in potential occupancy have moved in the range of 1.1 million to 1.3 million additional households. Economic and housing market conditions, on the other hand, have imparted much more variance on actual occupancy demand, ranging from a high of 1.64 million additional households between 2004 and 2005 to the contraction of

166,000 between 2008 and 2009. Overall, potential and actual demand have averaged, respectively, 1.3 million and 1.0 million net additional units annually over the past decade.

The next decade of population growth indicates that potential housing demand in the US should increase by an average of 1.3 million households per year. Over the next decade, it will be these 13 million households that will provide the mechanism for the reduction of excess vacancy that will be required to bring residential construction activity back towards normal levels.

The Outlook for US Housing Starts

So what do these opposing forces mean for housing starts south of the border? Looking back, over the past decade annual starts averaged 1.5 million units, with the previous decade averaging 1.3 million units. While the past three years have been the worst on record (the 500,000-odd starts of the past two years represented one-quarter of the number started in 2003 and 2004), starts were well above their long-run average for the six years preceding the recent lows (peaking at the 2.1 million units started in 2005).



In light of the relatively slow pace of both job growth and unemployment rate declines, and given the magnitude of the existing stock of vacant units, it is expected that it will take in the order of six to eight years before residential construction activity returns to its long-run average. Embodied in this outlook is the inventory of almost three million vacant (and therefore excess) units, which on their own will require several years before they are cleared away and growth in occupancy demand generated by population growth can be again equated to

construction activity. Although it is expected that 2011 will be a much better year than both 2009 and 2010 (starts are expected to be in the range of 800,000 units), the number of annual starts is not expected to return to the 1.5 million long-run average until after 2018.

It is important to note that this assessment of the US residential construction market is based on an underlying expectation of slow improvement in the US economy, including corresponding declines in the unemployment rate and increases in employment. However, it should also be noted that anything that serves to inhibit market adjustments will prolong the duration of the recovery in US housing starts.