

# Globe Investor

## House boom eases market pains



Gains in property prices can come close to or exceed your investing losses, writes

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Enough with the stock market already.

If you want to understand how the financial well-being of Canadians has changed over the past few years, housing prices are at least as important. Unlike stocks, homes are worth a fair bit more than they were a few years ago.

The federal government's Canada Mortgage and Housing Corp. forecasts an average Canadian home price of \$183,600 for 2002 that's up 16.1 per cent from the average 1999 price of \$138,145. The news is even better in the country's biggest cities, where the Canadian Real Estate Association reports an average price increase of 9.5 per cent through the first nine months of this year alone.

Have you been a homeowner for the past few years? Then your house may have risen in value by an amount that comes close to or even exceeds your investing losses.

Even if you have no intention of selling your home, you can take comfort in the fact that the decline in your stocks and equity funds isn't the last word on your personal net worth.

Maybe you're skeptical. You have a right to be, given the hard knocks taken by many stocks and equity funds lately. But then you may not have checked the value of your home lately.

So let's do that. Let's look at the boom in the housing market and the decline in the stock market and see if we can develop a snapshot of the net worth of Canadian homeowners.

We'll start with a sample portfolio of widely held mutual funds that stands as a proxy for your investments. The returns from this portfolio since the beginning of 1999 will be compared with changes in home prices for major cities across

Canada over the same period (1999 was chosen because it was the last big year for the bull market).

Our sample fund portfolio started out with \$100,000 invested on the first business day of 1999 in a couple of Canadian equity funds, a Canadian balanced fund, a U.S. equity fund, a global equity fund and a tech fund (see chart for fund details). As of Sept. 30, these funds had delivered a total loss of 18.3 per cent.

Talk about sorry results. A little more than 31 years in the market and what's left is \$81,700 cents on the dollar (the funds will have risen some since Sept. 30). Fortunately, housing prices in communities across the country have made decent gains over the same period as these funds slumped.

Mind you, these increases aren't stunningly impressive by the standards of a bull market for stocks. You can see this if you apply the projected 16.1-per-cent increase for the average Canadian home from 1999 through 2002 to a \$100,000 investment. You'd get a profit of \$16,100, or 3.8 per cent on a compound annual basis.

Comparing the changing value of a home to an investment portfolio is somewhat more complicated than this, though.

To work through this, let's start with that national average house price mentioned earlier. The estimated price increase here in dollar terms is \$25,455, or \$183,600 minus \$158,145. Match that against the \$18,300 loss in equity funds and you're \$7,155 to the good, on paper at least.

Did you catch the nuance here? The percentage gain in the value of the average house was less than the percentage loss in the investment portfolio, yet it still more than made up for

the decline in those equity funds.

This is because the dollar value of the average home is higher than the value of our pretend fund portfolio. Many Canadians will also find their houses are worth more than their investments.

Now for a complication. These numbers apply if you own 100 per cent of your home and thus have no mortgage.

What if you have limited equity in your home? Through the magic of leverage (using borrowed money), the gains on your home can be strikingly high. Say you owned 25 per cent of the national average home in 1999, when the price was \$158,145. Your equity would be \$39,536 and you would owe \$118,609 in principal (plus lots of interest, but we won't go into that here).

Flash ahead to the end of 2002 and, after aggressively trying to pay down your mortgage, you have the principal whittled down to \$105,000. With the market value of your home now at \$183,600, the difference between what you owe and the price your house could fetch on the market is \$78,600.

On paper, you've about doubled your money. Stock market losses? What stock market losses?

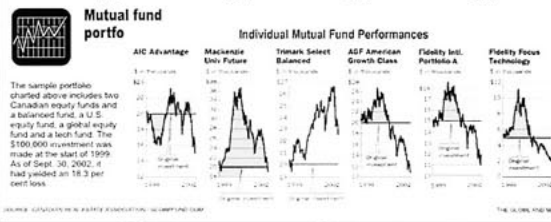
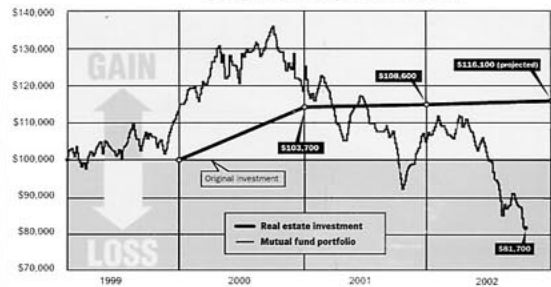
Using the national average house price is fine for general purposes, but it obscures the differences among real estate markets across the country. So let's take a close look at average price increases in five communities across the country:

■ Halifax: The average annual price jumped to \$147,892 as of Sept. 30 from \$118,522 in 1999, a 24.8-per-cent gain that works out to \$29,370.

### Weighing real estate against the markets

City by city	Average price*, 2002	Per cent gain since 1999
Canada	\$183,600	16.1
Calgary	\$201,500	21.2
Edmonton	\$156,883	14.8
Halifax	\$147,892	24.8
Montreal	\$171,727	18.2
Ottawa	\$200,751	24.2
Quebec	\$151,827	18.2
Toronto	\$274,732	20.3
Vancouver	\$246,360	22.7
Winnipeg	\$117,892	24.8
St. John's	\$112,862	17.8

\*Canada figure is an estimate for the whole year; city estimates as of Sept. 30.



If you owned the average Halifax house outright, then you've more than made back the investment losses in our model fund portfolio.

Sounds good, but what if you had a mortgage on that average Halifax home? We'll say for the sake of argument that you owed half the 1999 value of the home, or \$59,261, and that your mortgage payments would reduce this amount by \$10,000.

With your house worth \$147,892 at Sept. 30 and your mortgage principal down to \$49,261, your equity would rise to \$98,631 for a very tidy gain of \$39,370.

■ Montreal: The average resale house price jumped \$22,638 to \$141,167 between 1999 and Sept. 30, or 19.1 per cent. So if you were mortgage-free in this city, you again more than made back investment losses in our model fund portfolio.

Now, how about a situation where you had a mortgage in 1999 and took on a little extra debt, maybe to renovate, so that you owed the bank the same amount at the end of September as you did in 1999? If you owed 20 per cent of the 1999 value of the home, or \$23,706, then your equity would grow to \$117,461 from \$94,823 as your house rose in price. Paper gain: \$22,638.

■ Toronto: Monster gains here in dollar terms. The average price rose \$46,360 to \$274,732 between 1999 and Sept. 30, or 20.3 per cent. Even people with minimal equity did well in this type of environment.

Say you owed 90 per cent of the value of your average-priced Toronto home in 1999, or \$205,535.

If you paid down your principal by \$12,535 over

four years, then rising house prices would have expanded your equity by an impressive \$58,895 over what you had before.

■ Calgary: More good news for homeowners. The average resale house price rose \$30,773, or 18.5 per cent. As in our previous examples, people with limited equity will also have done very well in this city.

■ Vancouver: The comparatively tame average price gain in Canada's most expensive housing market was \$20,372, based on a 7.2-per-cent increase to \$301,535. Still, because of the high home values here, even the small percentage gains can generate decent returns for people with mortgages.

If you were burned by stocks, you'll no doubt want to know if the housing market is vulnerable to the same sort of decline that stocks went into after they peaked in 2000.

Maybe at some future point, but not now.

With mortgage rates as low as they are and with housing price increases levelling off recently, housing affordability has actually improved over where it was earlier this year.

"Reasons to worry about a bubble and about the real estate market getting ahead of itself just aren't there," said Carlos Leitao, an economist and housing affordability expert with Royal Bank of Canada in Montreal.

Something else to consider: By the time the housing market cools, your stocks and equity funds could be on the rise once more. Yes, it could happen.