



# MADISON'S TIMBER PREVIEW

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The US National Association of Home Builders' annual International Builders' Show, held at the Las Vegas Convention Center on January 19-22, was meant to address a key industry roadblock. Homebuilders have seen land development and home construction loans all but dry up since the financial crisis erupted in autumn 2008. Many have had to walk away from half-finished projects or even shut down. Some private equity funds, seeing the potential to charge up to 20 per cent interest, have started to cautiously bankroll some lower risk projects, despite the danger that the fragile housing recovery could stall. More than a dozen investment funds and a handful of lenders received a throng of homebuilders at the IBS looking for a financial lifeline.

"We're missing opportunities," Michael Sivage, CEO of Sivage Homes in Albuquerque, NM, told ABC News. "I've got three developments right now that if financing were more available, they'd already be under way."

Up to 85 per cent of builders said access to credit has been getting progressively worse in the past 18 months, according to a quarterly survey by the NAHB. Data compiled by the FDIC shows that home construction loans were down 51 per cent in 3Q 2009 from the peak in 2006. Delinquencies on loans to home builders, meanwhile, hit 27 per cent for 3Q 2009 and were even higher for condos, at 41 per cent. Sivage, who also builds homes in San Antonio, TX, was hoping to line up financing through a fund. The builder has trouble sourcing expansion funding even though it sold 300 homes last year — a 20 per cent increase from 2008 — and is profitable, according to ABC News.

"Only 15 to 20 per cent of the builders are even going out seeking credit," said NAHB economist David Crowe. "Eighty to 90 per cent of our builders get their loans from banks and thrifts. And 75 per cent say credit conditions are worse."

Even when they have contracts from qualified buyers, some homebuilders are having a tough time finding a bank to extend them credit. Attendance to this year's International Builders' Show was down considerably; there were only about 500,000 square feet of exhibits — less than half of the space the show offered when the housing boom was near its peak.

Another stumbling block in the housing rebound is the appraisal process, which by nature takes a look back at where the housing market has recently been, and the view in that direction is pretty bleak. When builders and buyers agree on a purchase price, if the appraisal falls short, it can kill the deal.

"A third of the builders say they have lost a sale because of low appraisals," Crowe said.

However building industry analysts acknowledge that the view ahead and toward next year's building market is a lot brighter than it was a year ago. Some critical aspects of home building have undergone a shift however, particularly in terms of home size.

"The average new home size actually declined in 2009," Rose Quint, an economics researcher for the NAHB, said at the convention. "There has been almost 30 years of growth in the size of homes." In the last couple of years, there has been almost a 10 per cent drop in the median size of homes started in the US, according to NAHB statistics. The average size of a new home that was completed in 2009 fell to 2,480 square feet from 2,520 square feet in 2008. The last time the average completed-home size fell by a statistically significant amount was 1982. And the median size of homes started in 2009 but not yet finished fell further, to 2,094 square feet. The average new home size has been more than 2,000 square feet since the late 1980s.

Homeowners surveyed by Better Homes and Gardens magazine in November said downsizing was becoming a bigger priority: 36 per cent said that they expected their next home to be "somewhat smaller" or "much smaller" than their current home versus 32 per cent who chose that response in 2008.

"Our builders resoundingly say they are going to build lower-priced models and smaller homes," Quint said. "In 2009, that meant a decline of new single-family prices of about 9 per cent."

Two other trends in home construction are contributing to the declining square footages: The prominence of first-time buyers in the housing market and the increasing number of households with members 55 and older who are buying homes. First-time buyers, driven into the market in good part by the availability of a US\$8,000 tax credit, are more likely to compromise on home size in exchange for a lower price. And the over-55 crowd tends to purchase single-story homes, which generally are smaller due to land costs that favour the more-efficient two-story plans.

The trend toward smaller homes encompasses other cost-reducing features, such as energy-efficient windows, and layouts that encourage comfort and togetherness. Not surprisingly, those are some of the features home buyers say they want now, according to an annual survey of home-buyer preferences. For all of 2009, an estimated 554,000 homes were started, down 39 per cent from 2008 and the lowest since 1945.

In another trend, US home owners are focussing on remodelling rather than buying a newer, bigger home. Remodelling activity fell more than 30 per cent from its peak in 2007, but is set to pick up again this year as the recession loosens its grip and home sales continue to rebound, according to a remodeling-market indicator released by the NAHB on January 21.

Homeowners are projected to spend just under US\$104 billion at an annualized rate on home improvements in 1Q 2010, down from US\$110 billion in the 4Q 2009 and US\$118 billion in the 1Q 2009. But activity is expected to rise to US\$107.7 billion in 2Q and \$110.9 billion in the 3Q 2010, according to the Leading Indicator of Remodeling Activity calculated by the Remodeling Futures Program at Harvard University's Joint Center for Housing Studies.

"Sales of existing homes are on the rise, and home sales are the best indicator of remodeling activity. Home-price declines have been moderating in most markets across the country. Financing costs are also favourable, although credit availability remains tight for many households," said Kermit Baker, director of the Program.

Remodeling work by homeowners peaked in early 2007 at US\$146.2 billion, about a year after the housing market itself peaked. Most homeowners perform major work on their houses within three to six months of purchasing an existing home. Baker said the strongest segments of the remodelling industry today were nuts-and-bolts replacement projects such as windows, siding, roofs and heating and cooling systems. That is starting to give way to more discretionary projects such as traditional kitchen and bath work. Even those projects, Baker said, "tend to be a good deal smaller than they used to be."

A telling statistic about consumer affinity for smaller homes is: sales of new homes priced at \$150,000 and less were up almost 20 per cent in 2009, while sales of new houses priced at \$300,000 were down compared to 2008.

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