Rental Housing Strategy – Study # 1

Submitted to:

City of Vancouver

by:

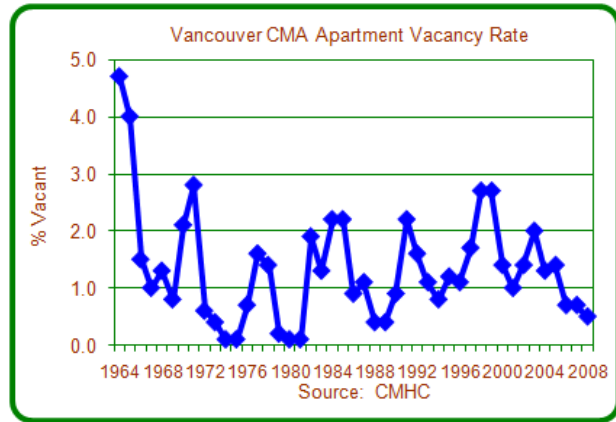## Will Dunning Inc

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Summary and Conclusions

Introduction

The City of Vancouver and Metro Vancouver (used interchangeably here with "Vancouver CMA") have one of the tightest rental markets in the country, both currently and historically. The chart illustrates the cycles seen in the Vancouver CMA rental market over the past 45 years. During those 45 years, the Vancouver CMA vacancy rate has averaged just 1.3%. For the past three years, the vacancy rate has been well below 1%, indicating a critical shortage of rental opportunities, and has resulted in rent increases that have exceeded overall inflation. Rent increases in the City of Vancouver have been 3.8% in 2006, 5.5% in 2007, and 3.9% in 2008.

This study has been completed for the City of Vancouver by Will Dunning Inc., to assist City staff with the development of a rental housing strategy. The City strategy involves the development of policies and tools to encourage the preservation and expansion of the rental housing stock.

The scope of this study is to review rental housing demand and supply over a 15 year period. Scenarios are developed for rental housing demand, as well as for the evolution of housing need. Conclusions are drawn on gaps and pressures on the rental housing supply.

In addition to this introductory section, this report includes four major sections:

- Part 2 reviews current data on housing need within the City and discusses factors that have and will influence the evolution of housing need.
- Part 3 discusses the rental apartment market within the Vancouver CMA and the City. It develops housing market forecasts, including forecasts of vacancy rates and rent increases to 2012.
- Part 4 looks at factors that will influence the long-term demand for rental housing and uses a demographic model to estimate potential requirements for additional rental housing in the City, to 2021. Three scenarios are provided.
- Part 5 uses a different demographic model to project changes in housing need for the City's renters, to 2021. Four scenarios are developed.

This introductory section summarizes each of the major sections of the report. It concludes with a discussion of Implications (starting on Page 8), which highlights the very substantial challenges facing the rental sector within the City.

Housing Needs in the City of Vancouver

Renters in the City of Vancouver have an above-average share of housing affordability problems. In 2006, 30% of the City's renters were in "core housing need", a rate higher than the national average of 27%. Just over 35,000 renter households in the City are in core need.

The core housing need concept combines three housing problems:

- Housing affordability – paying 30% or more of household income for shelter (including rent plus tenant-paid utilities).
- Suitability – living in a dwelling that has fewer bedrooms than required (based on a national standard).
- Adequacy - living in a dwelling that is in need of major repair.

The core need concept includes an income test: households who could in theory afford to rent a median priced unit are not counted in the core need totals. Many households who have housing problems have incomes above the applicable thresholds and they are counted as not being in core housing need. However, because of the chronically low vacancy rates in the Vancouver rental market, lack of choice is forcing them to pay more than the threshold amounts – they are not "voluntarily over-consuming". Consequently the true extent of housing needs within the City is greater than indicated by the core need data.

For City renter households in need, the cost for adequate and suitable housing was more than they could afford, by an average of $4,005 per year or $334 per month (in 2006). In total, this affordability gap was $141 million in 2006.

By far the most common housing need problem is affordability: among those who were included in the core need analysis, 27.0% of renters had an affordability problem (alone or in combination with another problem); 6.8% had a suitability (crowding) problem; and 3.7% had an adequacy (need for repair) problem.

The incidence (percentage) of renters in core need is highest for lone parent families (a very high rate of 48.4%) and non-family households (singles living alone or sharing with unrelated people, with an incidence of 32.3%). The incidences are below average for couples without children (18.4%) and couples with children (27.2%). Within the City of Vancouver, 63% of renters core need is for non-family households. For all of Canada, this group has a lower (but still substantial) 54% share of core need among renters.

By age group, the incidence of core need is highest for renter households in retirement ages (at 41.7% for those aged 65 to 74 and 44.3% for those aged 75 and older. These two age groups account for 18% of the total.

Table 1-1 Renter Households in Core Need by Age Group of Household Maintainer in the City of Vancouver versus Canada, 2006			
	Vancouver City		Canada
Age Group	Households in Core Need	% in Core Need	
15-24	2,085	27.4%	24.7%
25-34	7,040	22.1%	22.0%
35-44	8,530	29.3%	28.6%
45-54	6,975	32.9%	27.4%
55-64	4,310	35.1%	29.2%
65-74	2,900	41.7%	30.8%
75 and over	3,325	44.3%	31.8%
All Ages	35,160	30.2%	27.2%
Source: CMHC (Census-based housing indicators and data)			

During 2001 to 2006, the number of renters in the City of Vancouver in core need fell from 36,930 to 35,160, and the incidence of core need fell from 30.9% to 30.2%.

Factors that contributed to the improvement include:

- Gross rents (rents plus tenant-paid utilities) increased by 9.7%.
- Incomes (per adult) grew more rapidly, with the average increasing by 17.9%. The median income (the point at which one-half have higher incomes and one-half have lower incomes) rose by 12.8%.

Based on these changes in incomes and rents, the incidence of housing need should have improved by even more than it did. The lesser improvement is due to shifting of upper income tenants to home ownership, which left behind a core of tenants with less ability to afford housing.

A further consideration is that the number and percentage of the City's tenants who pay from 30% to 99.9% of their income for shelter improved very little. The number fell by just 265 households (less than the drop of 1,770 shown by the core need estimates) and the percentage fell by just 0.2 percentage points (versus the 0.7 point drop in the core need estimates). The reason for this discrepancy is that more households in 2006 were considered to be over-consuming. As discussed earlier, given the state of the City's rental market this can't be considered "voluntary over-consumption" and it further confirms that housing needs within the City are greater than indicated by the core need data. The Census data shows that 45,315 City tenants paid from 30% to 99.9% of their income for shelter in 2006, far more than the 35,160 renters considered to be in core need.

The Rental Housing Market

Persistently low vacancy rates within the City can be attributed largely to limited growth of the rental supply. The even lower vacancy rates seen during the past three years (up to October 2008) are the consequence of rapid job creation and income growth, which has stimulated new household formation and demand for all forms of housing.

Low vacancy rates have resulted in rapid rent increases – the average rent in the City's private sector rental apartment market increased by 11.6% during 2005 to 2008, or an average of 3.7% per year. This is almost double the overall inflation rate for Vancouver, which was 2.1% per year over the same period.
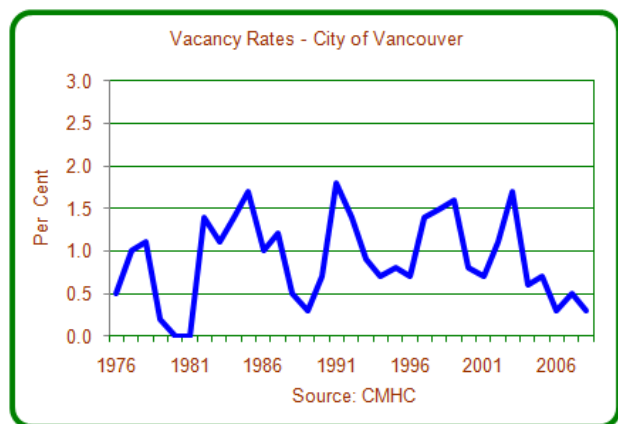
There is some prospect that vacancy rates will be higher during the next three years than during the past three:

- The economic recession will reduce housing demand – fewer new households will move into rentals, and some tenants may move back to the family home or double-up with others.
- Meanwhile, completions of housing that is now under construction will result in movements out of the rental sector.

Forecasts developed here suggest that vacancy rates for the Vancouver CMA and the City may be in the ranges shown in the following table. The rise of vacancy rates and the softening of rent increases will initially be more rapid and more substantial in the CMA as a whole than in the City, but vacancy rates would soon start to tighten in the CMA. For the City, there may be a longer period of (gradual) rises in vacancies, due to high volumes of housing completions that will result in moves out of the rental sector.

The forecasting model employed here estimates that the "balanced market" vacancy rate (the rate at which rents would tend to increase at the same rate as overall inflation) for the Vancouver CMA is 1.9% and lower for the City at 1.4%. Based on the vacancy rate forecasts, rent increases are projected to more slowly during 2008 to 2012 than during 2005 to 2008.

Data from CMHC shows that as of April 2009, the vacancy rate in the Vancouver CMA was 1.9%, up sharply from a year earlier (0.9%), and rent increases have decelerated. These changes are consistent with the forecast. Unfortunately, April data is not available for the City.

The forecasts developed here incorporate the impacts of the recession, followed by a modest recovery in which the level of employment rises at about the same rate as the population. However, if the economy recoveries more rapidly, vacancy rates would tighten more rapidly and rent increases during 2010 and 2012 would be stronger than suggested in the table.

Table 1-2 Rental Market Forecasts for the Vancouver CMA and the City of Vancouver		
	Vancouver CMA	City of Vancouver
Vacancy Rates		
2008 Actual	0.5%	0.3%
2009	2.6%	0.7%
2010	2.1% to 2.2%	0.9%
2011	1.6% to 1.8%	0.9% to 1.0%
2012	0.8% to 1.3%	1.1% to 1.2%
Average Annual Rent Increase		
2005-2008 Actual	3.8%	3.7%
2008-2012	0.8% to 1.2%	2.1% to 2.2%
Source: Will Dunning Inc.		

Demographic Projections of Potential Housing Demand

A demographic model is used to project potential requirements for new housing. The model starts with projections of future populations (which were developed by BC Stats, the central statistical agency of the Provincial government). The housing projection model applies data on housing choices (structural types of dwellings and housing tenures) by age group, to the projected future populations.

The total number of occupied dwelling units within the City is projected to expand by 22.4% during 2006 to 2021. Table 1-3 summarizes the projections for rental demand. All of the scenarios suggest that the rental sector will expand more slowly than the average (and more slowly compared to the ownership sector), with the consequence that over time rentals will represent a falling share of the City's housing stock. The slower growth for rentals is partly due to the aging of the population – older households are more likely to be home owners. In the second and third scenarios, an additional factor is increased home ownership within the various age groups. The projections suggest that most of the rental demand will be within apartment buildings rather than low-rise types of dwellings.

Key assumptions for the three scenarios are:

- The first scenario assumes that for each age group the choice rates will be held at 2006 levels.
- The second scenario reflects that there has been substantial shifting to home ownership – it assumes that tenure choice rates would shift further to home ownership during 2006 to 2011, but then be stable after 2011.
- The third scenario reflects that there has been a shift away from low-rise housing forms towards apartments, and assumes that this will continue (in addition to the shifting of tenure choices).

The second scenario might be said to reflect changes in consumer preferences, whereas the third scenario is a possible outcome in an environment where firstly, there are constraints on the capacity to provide additional low-rise dwellings, and secondly, reduced housing affordability is forcing consumers to make compromises. In actuality, these two conditions are closely related, since a major driver of cost increases is the limited capacity for new development.

The three scenarios indicate that the need for new rental supply is in a range of 1,000 to 1,500 units per year. By contrast, actual growth in the inventory of occupied rental units has been considerably less, averaging about 450 units per year during 1996 to 2006.

Table 1-3 Three Scenarios for Rental Housing Requirements in the City of Vancouver			
	Scenario 1 Demographic Change Only	Scenario 2 Shifting Tenure Choices	Scenario 3 Shifts in Dwelling Types and Tenure Choices
# of Renter Households in 2021 (versus 131,525 in 2006)	154,190	146,600	151,250
% Change versus 2006	17.2%	11.5%	15.0%
Growth of Renter Households per Year During 2006-2021			
Low-rise	313	277	-106
Apartments	1,198	728	1,421
Total	1,511	1,005	1,315
% of Housing Tenant-Occupied in 2021 (versus 51.9% in 2006)	49.7%	47.3%	48.8%
Source: Will Dunning Inc.			

The estimates in Table 1-3 are "projections", not "forecasts". They extrapolate factors and conditions that we can see today. Actual future outcomes will be influenced by changes that we cannot foresee.

The housing projections are based on projections of population (generated by BC Stats). The projections assume relatively strong rates of population growth for the City. For example, the City's projected population growth rate for 2006 to 2011 (7.1% in total) is more rapid than the actual rate of growth for 2001 to 2006 (5.9%). The population projections are based on "natural growth" and assumptions about migration. However, where growth occurs within the broader region will be influenced by any development constraints as well as the types and costs of housing that can be developed. It is possible that migration and actual population growth (and therefore household formation) will be less than projected - population growth and household formation that "should" occur within the City might happen elsewhere.

Projections of Core Need for Renters

A second demographic model is used to project numbers (and percentages) of renter households in the City that will be in core housing need during 2006 to 2021. Similar to the first model, it applies age specific choices and characteristics to the projected future populations. In this analysis, four scenarios are developed. All four scenarios indicate that the numbers of renter households in need will rise during 2006 to 2021.

- The first scenario assumes stability for each age group for the key "choice rates" (household formation rates, types of households formed, and tenure choices). It also assumes that the incidences of housing need will be stable for each group within the population. This scenario provides a starting point by dealing only with demographic forces (population growth and aging). This scenario suggests that the number of renter households in need would increase, and the overall incidence of need would rise.
- The second scenario moves beyond the demographic forces, by incorporating a shift to home ownership during 2006 to 2011, as well as recent trends for incomes and rents that will influence incidences of core housing need (it is reasonable to expect that rapid rent increases have raised the incidences). The choice rates and incidences of need are held constant after 2011. This scenario shows slower growth in the number of renter households. But, since most households that exit from rentals to become home owners are not in core need, there would be little change in the actual number of renters in need. Since there would be fewer renter households, the incidence of need would rise further.
- The third scenario adds a demographic shift – longer life spans for males, which has the potential to shape future household formation rates. For example, this should result in fewer elderly females living alone and increase the number of married couples in those age brackets; it could potentially influence remarriage rates for lone parents. These changes in household type patterns would also result in some shifting in tenure choices, so that rental demand would grow less rapidly than in the prior scenarios. However, in this scenario, the total number of renters in core need is not altered very much and so the incidence of need increases.
- The fourth scenario adds the impact of increasing education. As today's more educated young people age, average incomes should increase in older age brackets. This would reduce the numbers of households in need and the incidence. It is possible that there could be a further impact, if the higher incomes result in more shifting to home

ownership. However, the available data is not conclusive on this point, so the number of renter households is assumed to be unaffected.

This set of four scenarios incorporates some of the major demographic and economic forces that are likely to influence future trends for core housing need among the City's renters. The first two scenarios indicate that there will be pressures for increased need, due to a growing and aging population, as well as due to rising rent levels. On the other hand, the third and fourth scenarios suggest that there are some positive social and demographic forces that will restrain the growth of need. Overall, in combination these scenarios suggest that there will be further expansion of housing problems among the City's renters.

	Scenario 1 Demographic Change Only	Scenario 2 Shifting Tenure Choices and Economic Circumstances	Scenario 3 Layering on Shifts in Male:Female Ratios	Scenario 4 Adding Impact of Increased Education on Incomes
Table 1-4 _Four Scenarios for Core Housing Need Among Renter Households in the City of Vancouver_				
Growth in Renter Households				
# in core need analysis in 2021 (vs 116,510 in 2006)	137,454	134,045	131,431	131,431
Change per Year versus 2006	1,396	1,169	995	995
% Change versus 2006	18.0%	15.1%	12.8%	12.8%
Core Need Among Renters in 2021				
# in Core Need (vs.35,140 in 2006)	42,440	42,278	41,963	38,410
Incidence (vs. 30.2% in 2006)	30.9%	31.5%	31.9%	29.2%
Total Affordability Gap (in 2006 dollars, vs $141 million in 2006)	$171 million	$170 million	$170 million	$156 million
Source: Will Dunning Inc.				

Implications

Currently, the city does not have enough rental housing, particularly for families and for those with lower incomes, and this is reflected in the persistently low vacancy rates. Pressure on rents and on tenant affordability would be reduced if there were sustained increases in vacancy rates, which would reduce rent increases and might even reduce the absolute level of rents.

- Forecasts developed here indicate that the Vancouver CMA and City vacancy rates are likely to be higher during 2009 to 2012 than they have been in recent years, and rent increases will be muted. These anticipated changes are the consequence of economic recession. They are short term changes and do not represent the long-term change that is needed.
- To generate sustained increases in vacancy rates, to alleviate the persistent rental market crisis, requires persistent expansion of the housing supply.
- Increased rental supplies would have the most direct effects on vacancy rates, but expansion of home ownership opportunities, by drawing tenants out of the rental market, would be beneficial to the tenants who remain.

The City of Vancouver has seen some new additions of rental supply, partly through construction of purpose-built rental projects, as well as creation of secondary apartment units within the low-rise housing stock, and through conversions of existing low-rise dwelling from owner-occupancy to rental. Each of these sources, however, provides modest amounts of new rental supply. The largest source of new rentals appears to be investor-owned condominium apartments (although there is uncertainty about how much rental supply is generated by this source). Meanwhile, there are removals from the rental inventory, due to conversions of existing dwellings from rental to ownership, as well as by demolitions. Census data shows that the number of occupied rental units in 2006 (131,535) was virtually unchanged from 2001 (131,420). This indicates that during 2001 to 2006, inflows of supplies into the rental sector were roughly matched by outflows. The implication is that while population growth should be resulting in increased demand for rentals, lack of supply has prevented that potential demand from becoming actual demand.

A further consideration is that losses from the rental inventory will frequently be in the lower parts of the rental spectrum but most additions will be in the upper parts of the spectrum. The consequence is that while the rental inventory may be stable in overall numbers, it appears to be shrinking at lower rent levels. This study has found evidence that lack of rental opportunities has constrained rental demand, and especially for low income households (Census data suggests that household formation has been constrained in the lower parts of the income spectrum).

As was noted earlier, there is already a shortage of rental opportunities for those with modest incomes, and for families. The projections indicate that this situation will intensify and the shortages will become even worse. The consequences of this are (and this can be expected to continue for as long as supply shortages persist):

- Households that should be located within the City (due to work or for other reasons) move away from the City in order to find appropriate housing opportunities.
- Household formation is reduced (for example, doubling-up with unrelated people, or in multi-generational family situations).
- There are high and rising levels of severe housing affordability problems.
- Increasing numbers of individuals and households are homeless or at risk of homelessness.

The suppression of renter demand (especially among those with low incomes) has limited the numbers of households in core need and the incidence of need: it may seem paradoxical that if more rental housing was available, there would be more need. The flipside of this is that a future expansion of rental housing opportunities, especially at lower rents, would mean more formation of renter households - it would likely increase the number of households with housing needs, and might even increase the incidence of need.

Vacancy rates are lowest and rents are highest in the western and central areas of the City (CMHC survey zones 1 to 6). The greatest needs for additional supply are in those areas. However, due to vacancy chains (sequences of moves that occur after one tenant moves) supplies of new ownership and rental housing elsewhere in the City will provide some relief across the City (however, there is a risk that this process of "sorting" will increase polarization within the neighbourhoods of the City). Similarly, while new supplies of higher end rental and ownership housing do not directly benefit those in need, the process of vacancy chains means that any expansions of the housing supply provide some relief.

Whether a person is employed full-time is one of the best predictors of core need status. Strategies that promote community economic development and encourage labour force participation have the potential to positively influence housing affordability.

Similarly, increases in education that have actually occurred have the potential to reduce housing needs in future. Further promotion of education and skills training may be beneficial in long-term strategies to reduce housing needs.

About Will Dunning and Will Dunning Inc.

Will Dunning has been studying housing markets since 1982. For 16 years he worked at Canada Mortgage and Housing Corporation in various market analysis positions. For his last six years at CMHC he was the manager of the market analysis department at the Toronto Branch, and was responsible for all aspects of economic, demographic, and market analysis for the Greater Toronto Area.

Will has a Bachelor of Arts degree in Economics from McGill University and a Master of Arts degree in Economics from the University of British Columbia. In the fall of 2000 he established Will Dunning Inc, which specializes in the economic and demographic analysis of housing markets, and particularly rental housing markets.