FALL 2018
HOUSING MARKET DIGEST
RENTAL MARKET IN CANADA

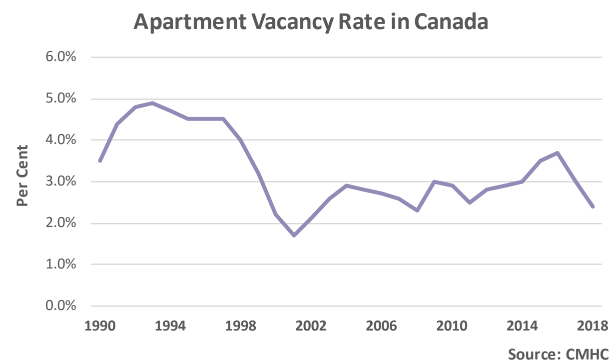
MORTGAGE PROFESSIONALS CANADA

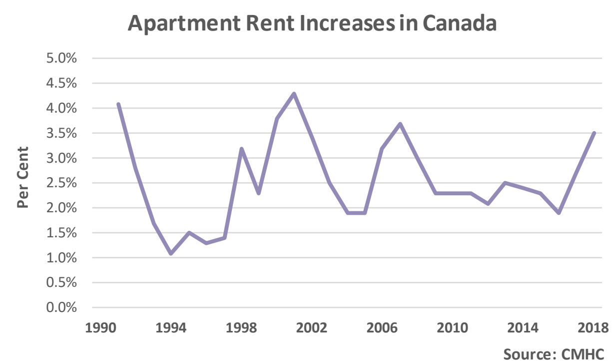
A Falling Vacancy Rate

Once per year, Canada Mortgage and Housing Corporation provides a comprehensive review of rental markets across Canada. The survey occurs during the first half of October. Results for this year were released on November 28.

For October 2018, the vacancy rate was 2.4%, which was a substantial drop from the 3.0% rate recorded a year earlier. The vacancy rate for 2018 is far below the average of 3.3% for the entire period shown in this chart. The reduction in vacancies resulted in more rapid rent increases, at 3.5% this year. Over the entire period shown, the average increase was 2.6%. This data shows that the situation has become increasingly challenging for Canada's tenants.

Vacancy rates fell in 7 of the 10 provinces. Manitoba, BC, and Ontario saw small increases in their vacancy rates. These three provinces also saw the most rapid rent increases. The lowest vacancy rate is now in PEI, followed by BC and Ontario. The highest vacancy rates are in the three provinces where economies have been hurt by the plunge in oil prices (Saskatchewan, Newfoundland and Labrador, and Alberta). These provinces saw the weakest rent increases.





Vacancy Rates and Rent Increases, by Province			
	Vacancy Rate		***Rent Increase***
Province	***2017***	***2018***	***2018***
Newfoundland and Labrador	6.60%	6.00%	1.20%
Prince Edward Island	1.20%	0.30%	2.90%
Nova Scotia	2.60%	2.00%	1.90%
New Brunswick	4.10%	3.20%	3.00%
Quebec	3.40%	2.30%	2.40%
Ontario	1.60%	1.80%	4.80%
Manitoba	2.70%	2.90%	3.90%
Saskatchewan	9.30%	8.70%	0.00%
Alberta	7.50%	5.50%	1.60%
British Columbia	1.30%	1.40%	6.10%
Canada	3.00%	2.40%	3.50%

Source: CMHC

Interpretation

Since the data is collected only once per year, it is difficult to construct any models for analysis or forecasting of rental markets. The author's experimentation over many years, for many different communities across Canada, has resulted in statistical models that have low "reliability". But, those low-reliability results have been surprisingly consistent, and have led to a conclusion: the two most important drivers of changes for the vacancy rate are job creation during the past year (which allows more people to buy or rent housing) and total completions of housing during the past year.

Interpretation (Continued)

It is tempting to expect that completions of new purpose-built rental apartments would be important, but the author's analysis has found that this is rarely the case.

On reflection, this makes sense:

- The rental market is part of a complex housing system in which there are very large flows between ownership and renting, and between different forms of housing.
- Expansion of the total stock of housing offers people more choice: even when people move into new home ownership dwellings, that move sets of a chain of other moves. Much of the time, that chain of moves includes someone moving out of a rental, which creates an opportunity for a new tenant.
- Moreover, the tenure on a new dwelling is not fixed for all time. In particular, it is well known that many new condominium apartments are occupied as rentals. In addition, some low-rise dwellings (single-detached, semi-detached, and town homes) are ostensibly built for ownership but are made available as rentals.

It is also tempting to expect that changes in resale market activity will affect the rental market. But, once again while the statistical analysis produces unreliable results, over many repetitions it has been found that resale activity has little effect on vacancy rates. This also makes sense on reflection. Most of the time a resale transaction does not add to total demand for housing (the buyer usually moves out of a different dwelling) and it usually does not alter the total supply of housing (unless the new buyer adds or removes a basement apartment).

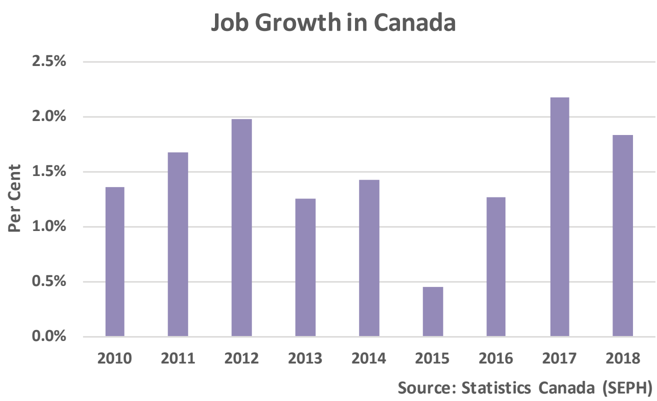
Employment Trends

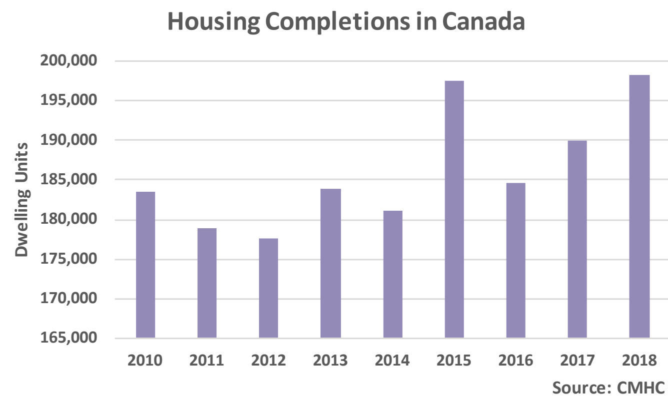
Our impressions about the employment situation are largely based on data from Statistics Canada's Labour Force Survey ("LFS"). This data indicates that during the year up to this September, employment in Canada expanded by 1.2%. This is slower than the rate of population growth (1.3%), and this therefore should be considered a mediocre result. Based on this data, we would expect that housing demand would be weak, and the drop in the vacancy rate this year would be a surprise.

However, the data from the LFS is derived from a sample survey and like all such surveys, it can produce errors. Statistics Canada has a second survey (Survey of Employment, Payrolls and Hours, or "SEPH"), which is based on data from employers, and is therefore likely to produce more-accurate data. This data receives much less attention because it is published almost two months after the LFS (the most recent data is for August). The two datasets usually tell similar stories. At present, however, SEPH shows growth of 1.8% (as of August) versus the 1.2% shown by the LFS (as of September). Over the entire period shown in this chart, job growth averaged 1.5% per year. Strong job growth in both 2017 and 2018 helps to explain the drops in the vacancy rates that were seen in both years.

Employment Trends (Continued)

Housing completions were at above average levels during 2017 and 2018 (the chart shows the figures for 12-month periods ending in September). These elevated volumes of new housing supply provided some relief for rental markets. Without this additional housing supply, the drops in the vacancy rates in 2017 and 2018 would have been even larger than they were.

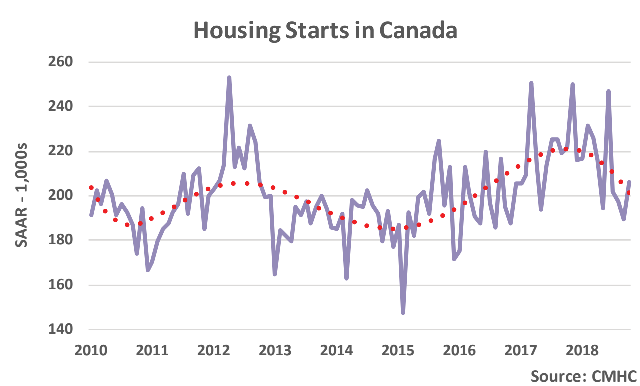




Looking Forward

The mortgage stress tests have resulted in reduced buying of new and existing homes. It takes some time for changes in purchases of new homes to translate in reduced housing starts (and even longer for housing completions to be affected). Increasingly, it appears that housing starts have peaked, and may have started to fall. The next chart illustrates that total housing starts were very strong during 2016 and 2017, but the trend has started to fall during 2018. A more detailed examination would show that housing starts have turned sharply for low-rise dwellings (single-detached, semi-detached, and town homes) but remain very strong for apartments. During 2019, starts for apartments will gradually reflect the reductions in sales that have occurred this year. This is explored in more detailed within the Housing Market Digest reports (for Canada and the regions) that can be found here: https://goo.gl/kJ6mcC

Following from these trends for housing starts, housing completions are expected to fall only slightly during the coming year, meaning that new housing supply will continue to provide some relief for the rental sector. However, housing completions are expected to fall considerably during 2020.



Looking Forward (Continued)

As for employment, higher interest rates can be expected to gradually weigh on job creation during 2019 and 2020.

For 2019, a combination of continued high levels of housing completions and a slowdown of job creation should mean that there will be little change in the apartment vacancy rate (perhaps a drop to 2.3% from the 2.4% seen in 2018). The low vacancy rate can be expected to result in continued rapid rent increases, at a rate of at least 3%.

During 2020, the reduction of housing completions that will result from the mortgage stress tests will add to pressures in the rental sector. For 2020, the vacancy rate is expected to drop further (approaching 2.0%) and rent increases will quicken.

Government Policies at Cross Purposes

The federal government has announced plans to make major expenditures in support of affordable housing ($40 billion over 10 years). The federally-mandated mortgage stress tests, by reducing movements out of renting, will add to pressures within rental housing markets, and are operating at cross-purposes to the National Housing Strategy.