HOUSING MARKET INSIGHT
Ontario

CANADA MORTGAGE AND HOUSING CORPORATION

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"Although the average growth rate of home renovations is not likely to match that of the last couple of decades, the province is still set to see an increase. Ontarians are aging, the housing stock is aging, home prices are on the rise and more homebuyers are turning to the resale market — all these factors support renovation spending."

Ted Tsiakopoulos
Regional Economist, Ontario

Ontario Renovation Spending Poised For Additional Growth

Highlights

- Ontario home renovation activity represents growing share of Ontario economy
- Higher end alteration and improvement projects capturing bulk of spending
- Aging households behind much of the spending in recent years with more spending to come
- Vibrant resale market, aging rental and ownership stock and growing home equity wealth will support the renovation market
- Southwestern Ontario represents the biggest potential for growth, GTA the least potential

Ontario Renovation Market – A Growing Share of Ontario Economy

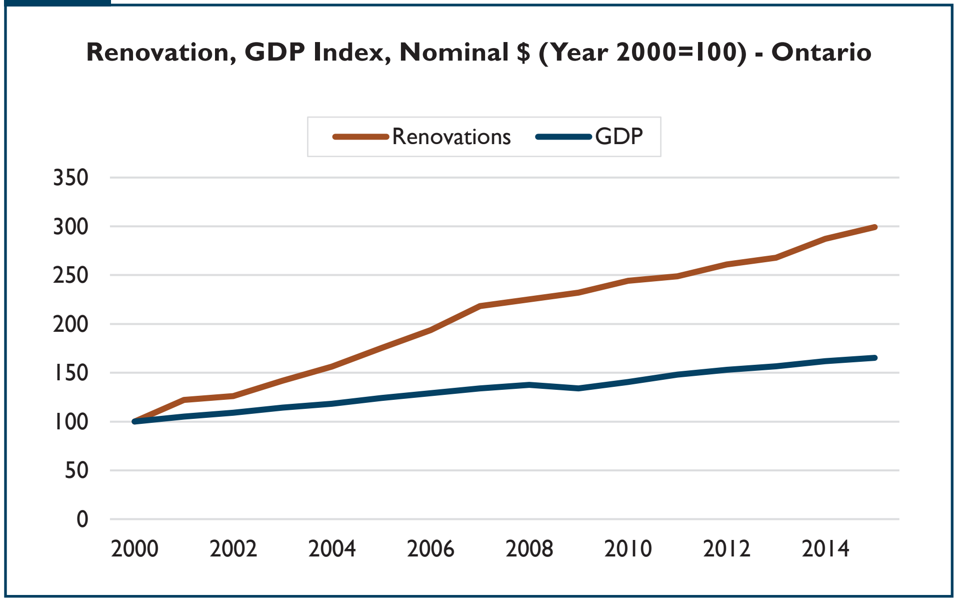
While total renovation spending was unable to match the rate of growth registered during the pre-2008 period, the renovation market has nearly doubled in size[1] relative to the broader economy since the year 2000 and is poised to reach nearly four per cent of GDP in the years ahead. A number of distinct forces were at play driving the growth in renovation spending during the pre-2008 and post 2008 period. A cyclical upturn in the Ontario economy combined with a collapse in interest rates helped fuel the renovation market as we entered the new millennium. When the economy is growing it generates the jobs that are needed to support spending on housing and in turn renovations. In addition, lower interest rates sparked growth in mortgage credit which in turn helped finance renovation projects. Meanwhile, the post-2008 period saw the provincial economy and mortgage credit market contribute less support to the renovation market. Instead, renovation tax credits and wealth had a more pronounced effect. The market has also overtaken the new construction market in terms of investment dollars spent. Moving forward, demographics are likely to play an even bigger role in shaping renovation spending.

While the economy drives renovation spending, a feedback effect is also felt by the economy from additional growth in the renovation market. For example, an additional billion dollars of new value added investment in the Ontario renovation market, generates over 5,000 additional direct jobs[2] across the province, according to the latest Statistics Canada data. In addition, suppliers/ building material retailers are also positively impacted by the additional spending by households on renovation projects and this creates more spinoff jobs know as indirect jobs. Indirect jobs amount to an additional 4,000 jobs from this shock to renovation spending.

Renovation Market Driven By Resale Activity

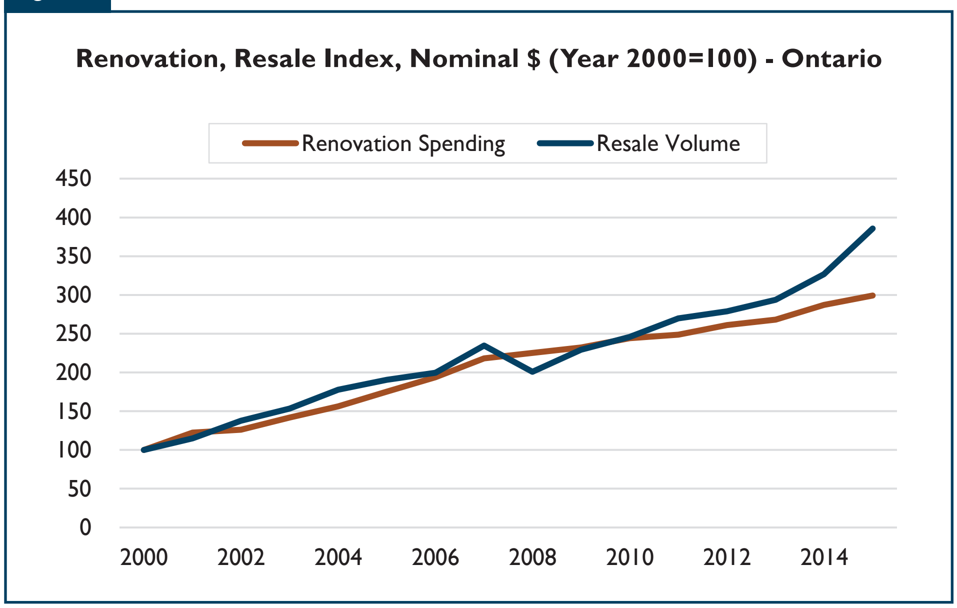
There is a strong correlation between resale activity and renovation spending when observing historical data. In fact, CMHC analysis indicates that Ontario households undertake renovation work typically within 12 months of an existing home purchase. The bulk of spending, roughly 75 per cent of all projects, have comprised alteration and improvements whose purpose is to add value to the home. With resale activity[3] running at record levels in 2015 and in early 2016, this suggests renovation spending is poised for additional growth. In 2015 alone, Ontario's renovation market was estimated at about 25 billion dollars[4]. In recent years, popular projects[5] included: remodelling of rooms which includes basement upgrades, painting and wallpapering, heating and air-condition and landscaping.

Figure 1



Source: CMHC adapted from Statistics Canada

Figure 2

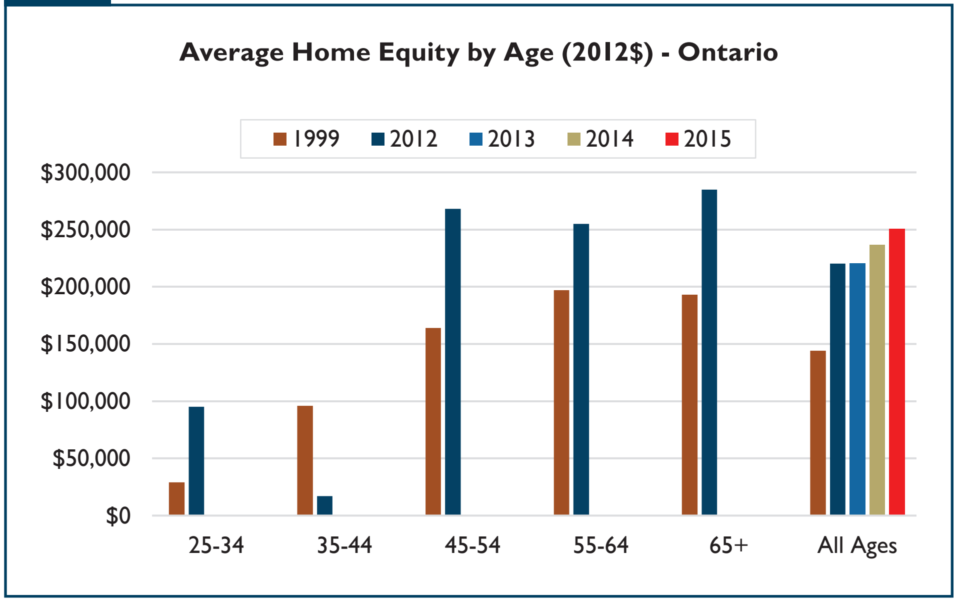


Source: CMHC adapted from Statistics Canada, CREA

Ownership & Rental Stock Aging

Ontario's housing stock is aging. According to the 2011 census, 57 per cent of the entire housing stock was built before 1980. More specifically, approximately 85 per cent of the apartment rental universe was built before 1980. Not surprisingly, in the face of more competing completions for both new ownership and rental units, existing homeowners and landlords looking to sell or rent existing space have undertaken more renovation work. In fact, with more purpose-built and condominium rental units reaching the completion stage in 2014 and 2015, industry contacts suggested existing landlords have invested more dollars in their units to remain competitive. Landlords in Ontario are able to pass on increases in rent exceeding guideline amounts when capital improvements and upgrades have been made to rental units. In addition, new money announced in the 2016 budget geared to repairing and upgrading the existing social housing stock will provide additional support to the renovation market.

Figure 3



Source: Statistics Canada SFS, Equifax, CMHC calculations

Improving Home Equity Supports Renovation Spending

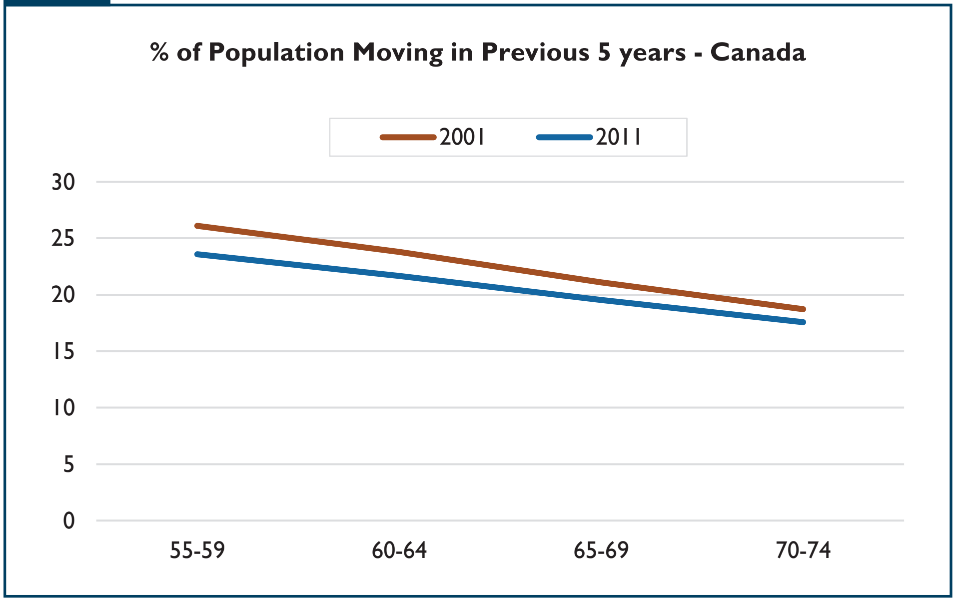
As indicated in the opening, improving home equity wealth impacted renovation spending in a more pronounced way during the post 2008 period and will likely continue to do so in the years to come, despite weaker price growth. Between 1999 and 2012, Statistics Canada Survey of Financial Security indicated that home equity grew accounting for about 1/3 of all household wealth in Ontario. Since 2012, with interest rates trending lower and growth in average home prices easily exceeding the growth in mortgage credit outstanding, home equity[6] continued to rise. While lower interest rates contributed to improving equity as borrowers contributed more against principal versus interest payments, price gains since 2012 were the biggest contributor to growth in home equity. Current estimates suggest that the average homeowner equity in Ontario has grown by 14 per cent since 2012[7]. If trends in home equity by age over the period 1999-2012 persist, most of this growth in home equity since 2012 was likely concentrated among aging households. When rising prices boost home equity, households feel wealthier and thus are encouraged to invest in their homes.

Do I Move or Do I Renovate? Aging Households Will Vote for the Latter

Households aged 55 to 74 will be contributing most to the growth in Ontario household formation in the next several years[8]. While younger millennial households aged 25 to 34 will also be growing, high debt loads and declining affordability will make ownership and renovation spending considerations more prohibitive for this group. CMHC demographic projections suggests households aged 55-64 will comprise nearly 1.1 million Ontario households by 2017. With a historical average propensity to renovate at 35 per cent based on CMHC and Statistics Canada data, this suggests nearly 400K households could be in the market to renovate their homes. This would be in line with recent data from Statistics Canada's Survey of Household Spending which found that households over the age of 40 were more likely to be in the renovation market in recent years.

Historical census data indicates that as much as 80 per cent of households over the age of 55 age in place and prefer not to move. This is due to declining mobility when households age. In fact, households only move if health and finances necessitate this or to be closer to family and friends. In addition, undersupplied resale markets combined with rising transaction costs stemming from realtor fees and land transfer taxes would further discourage mobility among older households. Housing needs change as a household ages which will require adapting the current home to meet ever changing needs. In addition, with a large share of young adults staying home longer due to economic and academic considerations, the need for space will remain important.

Figure 4



Source: Statistics Canada Census

Ontario Households Use Borrowed Funds to Finance Renovations

Historically, Ontario households have relied on borrowed funds to finance[9] renovation spending. In fact, lines of credit, borrowing against home equity and personal loans have represented the major sources of funds particularly during the pre-2008 period. Despite that households have tapped into their housing wealth to finance their renovation spending, it has still resulted in improving home equity. This is explained by the fact that average home prices have outpaced growth in mortgage debt, particularly in recent years. With aging households over the age of 55 driving renovation spending in the years to come, home equity will likely continue to be a source of funds for renovation work even with modest increases expected in home prices.

Southwestern Ontario Centres Poised for Stronger Growth in Spending

An aging population will play a bigger role in driving renovation spending in the years to come. While the economy and resale market activity will contribute less to the growth in renovation spending on average across Ontario, this effect will not be uniform across all urban centres. In fact, there is reason to believe that growth rates in renovation spending should vary by urban centre given different demographic, economic and local housing conditions more generally.

While representing a smaller share of the provincial economy and housing market, southwestern Ontario centers such as Windsor[10] offer the greatest growth potential.

A combination of relatively higher than average employment, higher housing affordability levels, higher than average median age and continued pent-up demand based on a historically low sales to population ratio indicates high potential for growth in home sales and renovation spending. From a macroeconomic perspective, a low Canadian dollar and improving non-energy sector performance should provide underlying support to the local economy and housing market.

Meanwhile, the GTA represents less potential for growth in renovation spending. More modest job growth expected ahead, low affordability levels, a below provincial average median age and less pent-up demand due to a historically high sales to population ratio will translate to more modest growth in renovation spending. Indeed, Toronto remains vulnerable to a housing adjustment owing to rising imbalances[11] which could dampen home price increases and in turn the incentive and confidence to invest in upgrades.

ENDNOTES

[1] Statistics Canada Quarterly Economic Accounts

[2] Statistics Canada Input-Output Multipliers 2010

[3] Canadian Real Estate Association (CREA)

[4] Statistics Canada Quarterly Economic Accounts & Survey of Household Spending (SHS)

[5] Statistics Canada Survey of Household Spending (SHS), 2010-2014

[6] CMHC calculations based on CBA, CREA, Equifax Canada data

[7] Equifax Canada Data, 2012-2016

[8] CMHC Potential Housing Demand Model Projections, Ontario

[9] Altus FIRM Survey

[10] CMHC Ontario Housing Market Outlook Highlights, Spring 2016 edition

[11] CMHC Housing Market Assessment (HMA), July 2016 edition

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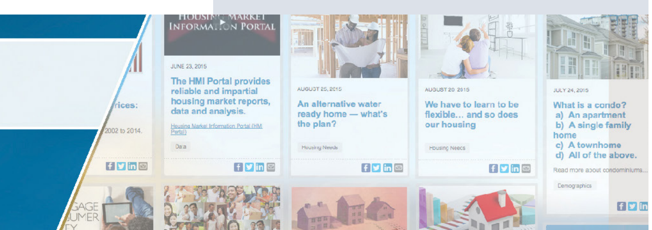

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