

Housing Market Digest

Greater Toronto Area, March 2022

Condominium Conversion

I commented on this briefly last month: “One sentence in the report [“Report of the Ontario Housing Affordability Task Force”] expresses concern about conversion of rental apartments to condominiums. I don’t share that concern, because conversion doesn’t change total housing supply or demand, it just changes the labels. I’m actually in favour of condo conversion, because it is an affordable step into ownership.”

Now, I know that almost everybody disagrees with me on this, but I have thought about it a lot over the past 20+ years, and I remain convinced that condominium conversion does more good than harm, for multiple reasons, including:

- It puts the housing in the control of the occupants (you’ve heard about “Above Guideline Increases” and “renoviction”, right?).
- Repeatedly, my calculations have told me that the occupants will, in the long-run, be better off in terms of monthly costs as owners than as tenants (in part because it takes the landlords’ profits and overhead out of the calculations).
- In the short term, it is usually more expensive to own, but that is because of the “forced saving” that occurs through repayment of mortgage principal. When that is taken into account, ownership usually cost less than renting an equivalent dwelling.
- In addition, in the City of Toronto, tax rates are lower for condos (2021 total tax rate of 0.611013%) than for existing rentals (1.093384%).
- We don’t need to talk about who benefits from growth in property values.
- I believe that the people who would live in a condo conversion would be essentially the same people who would live in it as a rental, and therefore, conversion would cause little displacement.

While conversion reduces the number of dwellings that we can label as rentals, it also reduces the number of people who rent. Therefore, conversion does not materially alter the balance between supply and demand.

My thinking was highly influenced by a detailed study that was published by the US Department of Housing and Urban Development in 1980 (that is, by a Democratic – Carter – administration):

The Conversion of Rental Housing to Condominiums and Cooperatives: A National Study of Scope, Causes and Impacts

The report is still available, via Amazon (but it costs \$63):

https://www.amazon.ca/Conversion-Rental-Housing-Condominiums-Cooperatives/dp/089499090X/ref=sr_1_1?crd=2L7UHZP2LP5GF&keywords=conversion+of+rental+housing+to+condominium&qid=1645284620&s=books&prefix=conversion+of+rental+housing+to+condominiums%2Cstripbooks%2C62&sr=1-1

For me the relevant section was Chapter 7: *The Interaction of Supply and Demand: Market Effects and Future Volume*.

The HUD analysis included surveys that tracked movements of people out of and into converted buildings. Here is the summary of the conclusions:

Conversions are products of a shift in housing demand, and a corresponding shift in the use of the existing housing supply away from rental toward ownership. The net effect of conversions on the balance of supply and demand can be estimated by considering the pre and post conversion tenure status of households affected by conversion. Those renters who buy contribute to a reduction of overall renter demand; many converted units remain available as rentals; and some tenants move out upon conversion and purchase a unit elsewhere. The cumulative effect of these factors contributes to a significant moderation of the actual supply impact on the rental market. This analysis indicates, nationally, that for every 100 rental units converted, there is a net increase of 5 units for sale to owners' and a net decrease of 5 available rental units. In other words, when changes in demand and supply resulting from conversion are juxtaposed, the effect on the rental market is considerably less than the total of all units converted.

One key concern in the report is about “the extent to which it [conversion] involuntarily displaces prior tenants”. That problem can be lessened through regulation that prevents evictions of tenants who were in place at the time of the conversion. My understanding is that this is covered in section 51 of the existing Ontario Residential Tenancies Act.

Housing Market Digest

Greater Toronto Area, March 2022

The City of Toronto has a condominium conversion policy that, on its face looks reasonable (Policy 8, in Chapter 3 of the Official Plan). But, they couldn't just say "this will never be permitted"; so they had to create conditions that in theory permit conversion but in reality are almost impossible to satisfy.

"The conversion to condominium, or the severance or subdivision, of any building or related group of buildings, containing six or more rental housing units will not be approved unless:

a) all of the rental housing units have rents that exceed mid-range rents at the time of application; or

b) in Council's opinion, the supply and availability of rental housing in the City has returned to a healthy state and is able to meet the housing requirements of current and future residents..."

The concept that all units must have rents above the "mid-range" sort-of looks reasonable at first glance. But, the definition matters: it means that **every unit in the building must have a rent that is at least 50% above the Toronto average rent** (by unit type). Many years ago, I paid CMHC to do analysis on this, using the results from its rental market survey. In 2003, there were 3,315 units in buildings that would satisfy the policy (or 1.3% out of 251,367 total purpose-built rental units within the City of Toronto). I expect that most of those buildings have now been converted.

The alternative second condition gives Council a lot of room to say "no, because we said so".

There are places in Canada where significant amounts of rental-to-condo conversion occur – including London, but also in western Canada.

One notable characteristic of those places is that they have historically had very active supply functions for purpose-built rentals.

I think it's reasonable to say that if investors have the freedom to sell apartments to their occupants, they will be more likely to build. A less-draconian condominium conversion policy would be an additional tool that would help expand the total supply of housing.

Almost every new so-called purpose-built rental project is registered as a condominium, so that the owners can avoid the conversion policy.

Another related point, which my research has told me repeatedly, for many locations across the country: what determines the state of the rental market is the total supply of new housing (for both ownership and rental), not just the supply of new rentals. So, when someone says we need more purpose-built rentals, my reaction is... sure, but not at the expense of other housing options.

All of this said, I think it would be really useful for the Ontario Ministry of Municipal Affairs and Housing to do some research on the effects of condominium conversion, including something like that 40+ year old HUD study.

Toronto Rental Market

During February, CMHC released data from its annual (October) rental market survey. For all of Canada, the apartment vacancy rate fell slightly to 3.1% versus 3.2% in 2020, but still higher than 2.2% in 2019.

Toronto CMA was an outlier, as the apartment vacancy rate rose to 4.6%, versus 3.4% in 2020 and 1.5% in 2019. For apartments in Toronto CMA, I estimate that the balanced market threshold is in the area of 2%. Correspondingly, growth in apartment rents slowed sharply, to just 1.1%. For row housing, the vacancy rate was much lower, at 1.9%. Rent growth appears to be faster for rows (but CMHC did not publish an estimate).

I've been saying that we might be overbuilding apartments (and under-building ground-oriented housing). This data is consistent with that theory.

How to Reach Will Dunning Inc.

Email: wdunning@sympatico.ca
Web site: www.wdunning.com
Twitter: [@LooseCannonEcon](https://twitter.com/LooseCannonEcon)

Disclaimer of Liability

This report has been compiled using data and sources that are believed to be reliable. Will Dunning Inc. accepts no responsibility for any data or conclusions contained herein.

Copyright: Will Dunning Inc. 2022