



Better Housing Outcomes for the Canadian Economy

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Outline

- 1) Inherent Economic Features of Housing Markets.
- 2) More Problematic Housing Outcomes: Merit good effects.
 - affordability: homelessness; rental burdens; attaining homeownership.
- 3) These Adverse Housing Outcomes More than Merit Good Effects
 - STABILITY (known), WEALTH (ignored), PRODUCTIVITY (mostly unrecognised).
- 4) 'Causes': prices outpace incomes (system); rising inequality ('Resource' (non-market) and 'System' (supply-demand) solutions).
- 5) Current Policy Focus on Supply Challenges.
- 6) Questions for Policy and Governance, Finding Answers.



I. Applied Economics for Housing

Academic economics (and Finance Ministries) often use reductionist mainstream models that are important/but insufficient to capture all that is important. Key aspects include:

- 1) Housing is a stock of multiple characteristics of technical and locational 'capitals'.
- 2) Production requires design, land assembly, planning, financing, and complex construction involving labour, materials, and capital markets with market failures. An inherently 'slow' system involving 5 to 10pc of GDP.
- 3) Once produced, homes are spatially fixed capital (with national markets a system of sub-systems).
- 4) Different attributes of housing are used (with other resources) to meet demands for shelter, space, location relative to household activities, neighbourhood amenities etc.
- 5) It is the largest share (20-25pc) of household consumption (double for poorest households)
- 6) Housing is also a major capital asset of owners and mortgages their main debt.
- 7) Demands driven by incomes, equity, population growth and interest rates is a 'fast' system.
- 8) Consequently, markets are often out of equilibrium, with disequilibrium reinforcers.

HOUSING MARKETS, AND ESPECIALLY METROPOLITAN MARKETS, ARE OFTEN NOT WELL FUNCTIONING SYSTEMS WITH ONLY MERIT GOOD (SOCIAL) POLICY EFFECTS. THEY ARE COMPLEX, RECURSIVE, EMERGENT, IMPORTANT ECONOMIC SYSTEMS. WE FAIL TO ANALYSE AND GOVERN THEM AS SUCH!

II. Growing Trinity of Problematic Outcomes.

Merit good, social policy thinking dominates Canadian and other OECD housing policy debates, focussed around ill-defined and diffuse notions of 'affordability' and need. Not recent, not post-Covid but growing **since 1990's** (Canada later than many)

- Rising levels of homelessness and rooflessness
- Rising rental burdens in all rental sectors, growing queues for non-market
- Rising proportions of younger Canadians rationed out of home-ownership

Problematic Outcomes on all these indicators are INCREASING despite the near \$90 billion national housing strategy (NHS) for 2017-25. Major multi-sector policy settings in 'non-housing' policy areas drive these problem totals faster 'Housing Policy' can fix them. Need to rethink policy governance, scope wider than merit good focus and new emphasis on modernisation of non-market provision and development industry. *Why? More than Social: More than Local.*

III. And the Economic Policy Questions...

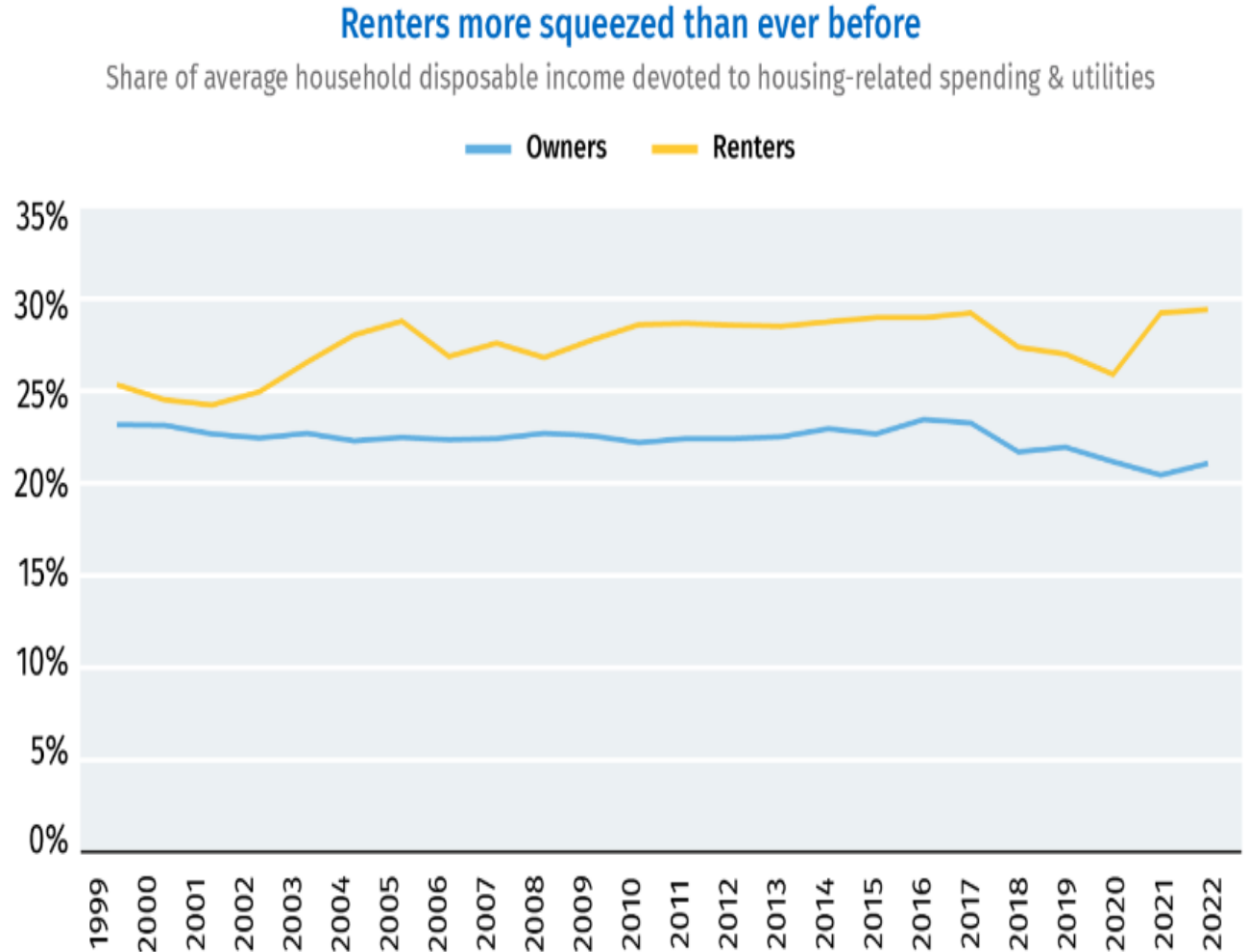
- 1) Longstanding focus on effects of constructing, maintaining, selling homes and multiplier effects on employment/incomes (Keynesian view) and equity effects on enhancing cyclical amplitudes. Recently financial stability (monetary policy and prudential regulation). **Known, recognised**. Canada under-researched, cf. USA!
- 2) Major effects of the returns from holding housing assets and shifting levels and patterns of home ownership on the distribution of wealth (now potentially negative): Canada research weak. **Known, Unexplored**.
- 3) Housing Outcomes Impact Productivity: quality, size, mobility affect human capital accumulation and use over life cycle. Locational choices impact overall labour supply and labour market matching process (not just a transport issue); asset returns shape use of investible funds by households/ firms away from human and business capital. As housing costs 'eat' the gains from agglomeration economies, firms and business leaders recognise this, e.g. Toronto Board of Trade, recent Alberta paper but CHRA paper and claim illustrates how poor this area of research in Canada is. **Largely Unrecognised in Governments, Unexplored**.

HOUSING POLICYMAKERS ARE BEGINNING TO FACTOR THE NET ZERO EFFECTS OF HOUSING QUALITY AND LOCATION EFFECTS INTO ENVIRONMENTAL POLICY ARGUMENTS BUT THE ECONOMIC CONSEQUENCES OF HOUSING POLICIES, AND THEY ARE NOT ALL LOCAL AND NOT ALL PROVINCIAL, ARE NOT SYSTEMATICALLY AUDITED BY ANY GOVERNMENT AT ANY LEVEL IN CANADA. BIG CITIES DO BETTER THAN MOST. NEED INTEGRATED TABLES AND POLICY ACTIONS AT ALL SCALES.

Changing Shares of Disposable Income Devoted to Housing and Utilities.

Freestone, C. Royal Bank of Canada. **Proof Point:** Canadian renters face higher hurdles to accumulating wealth than homeowners. March 2024.

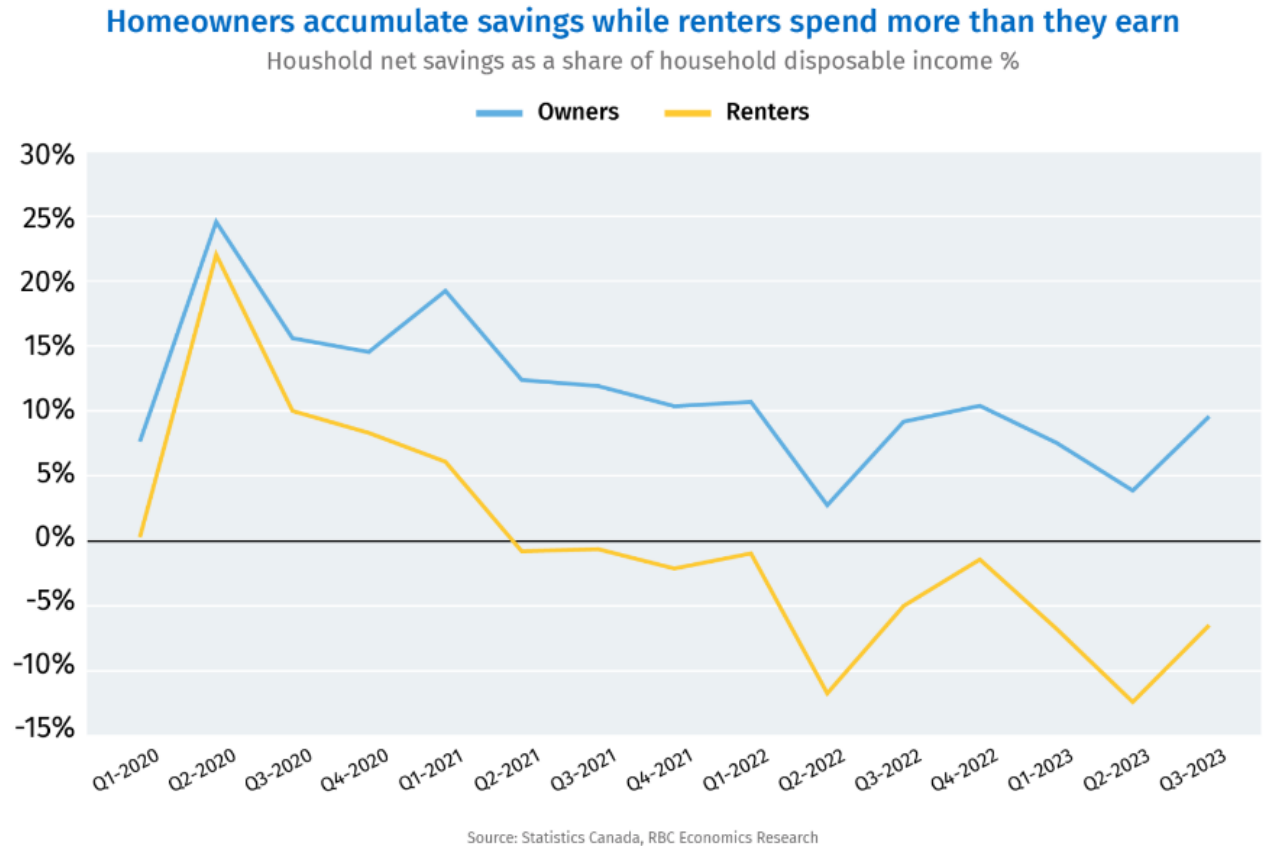
This figure highlights the importance of housing in consumption expenditures, the ways in which rental sector spending erodes savings capacities more significantly since the 1990's and the particular difficulties of renters in the post-covid period.



Source: Statistics Canada, RBC Economics Research

House Deposit Formation Difficulties Post-Covid.

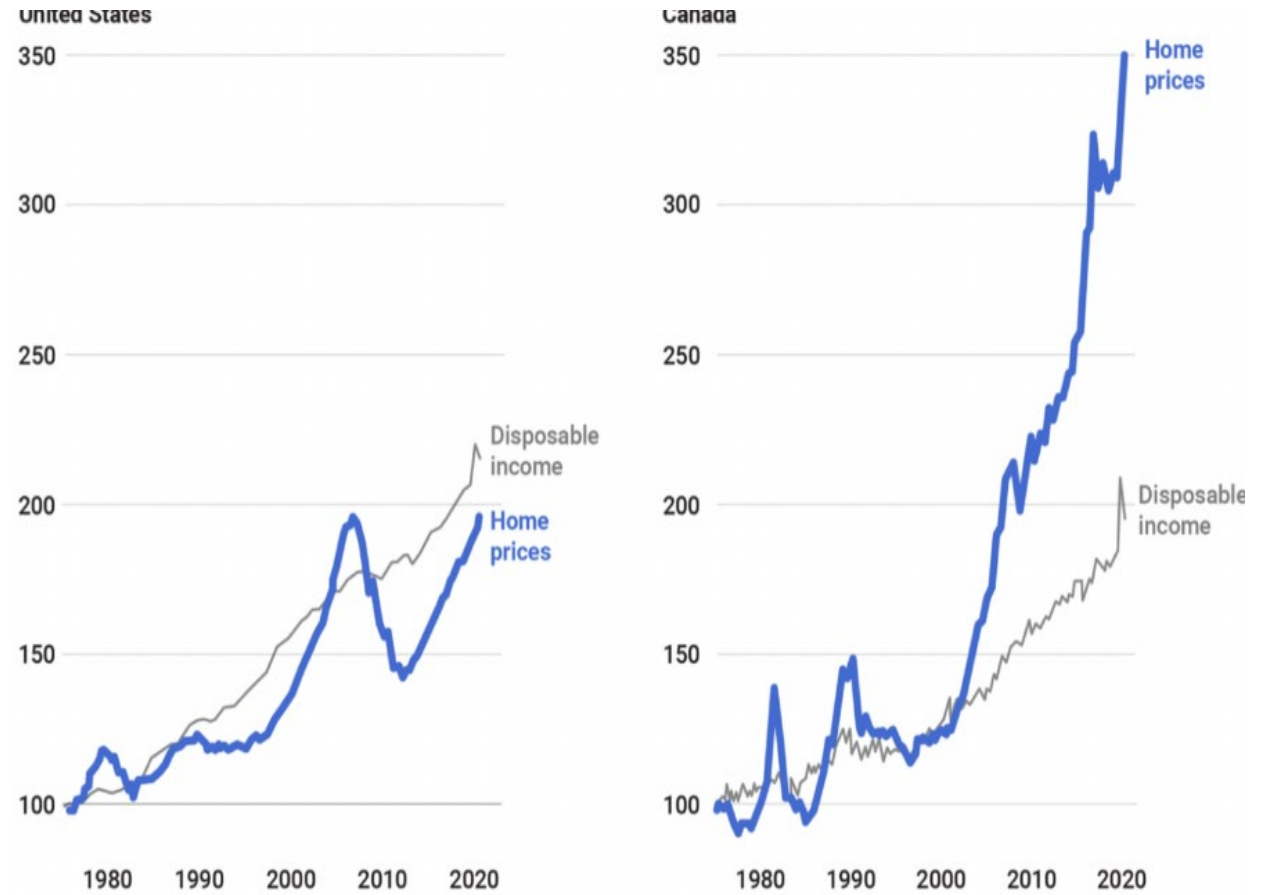
Freestone, C. Royal Bank of Canada. **Proof Point:** Canadian renters face higher hurdles to accumulating wealth than homeowners. March 2024.



Average Nominal House Prices for Canada and USA

OECD figures suggest that in wider international contrasts, Canada had an average house price to income ratio of just over 6 that was relatively low for Anglophone economies. However, in the subsequent 22 years that ratio rose faster than in most countries, almost doubling- the UK, Australia and New Zealand increased by 50pc- countries such as Finland, Italy and Ireland saw the ratio hardly increase.

The evolution of nominal house prices relative to disposable incomes in the USA and Canada from 1980 to 2020 also highlights the marked unlinking of house prices and disposable incomes in this millenium.



Notes: Real disposable income and real home price index. Rebased to 1975 (100). Timeframe is 1975 Q1 to Q4 2020. Sources: Mack, A., and E. Martinez-Garcia, 2011. "A cross-country quarterly database of real house prices: A methodological note." Globalization and Monetary Policy Institute working paper No. 99. Federal Reserve Bank of Dallas, author calculations, 2021.

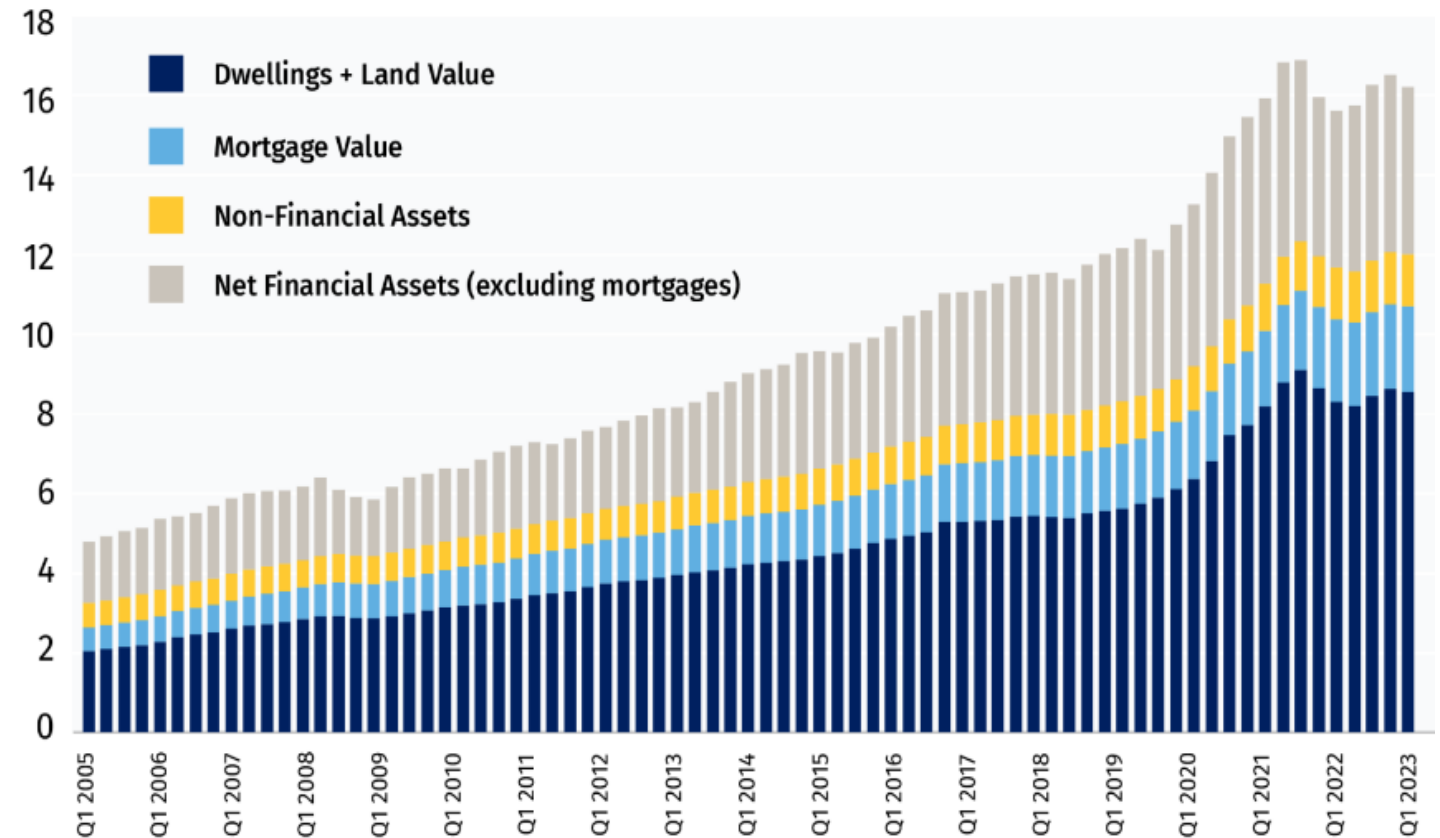
Housing Wealth as Key Driver of Overall Net Worth.

Sourced from

Freestone, C. Royal Bank of Canada. **Proof Point:** Canadian renters face higher hurdles to accumulating wealth than homeowners. March 2024.

Soaring home equity accounts for majority of the boost to net worth

Market value of household net worth, millions of CAD\$



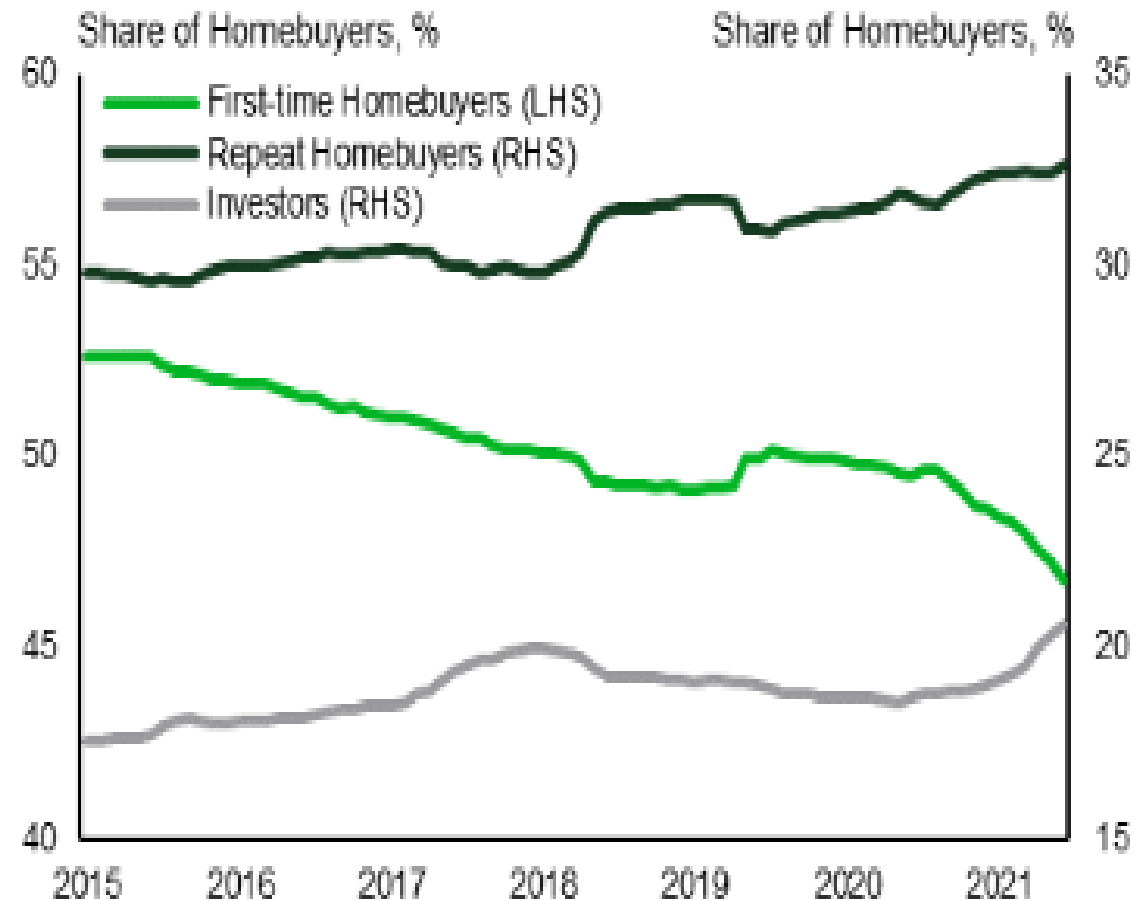
Source: Statistique Canada, DRF Économie

Search for Housing as Investment Displaces First Home-Owners.

Chart is copied from

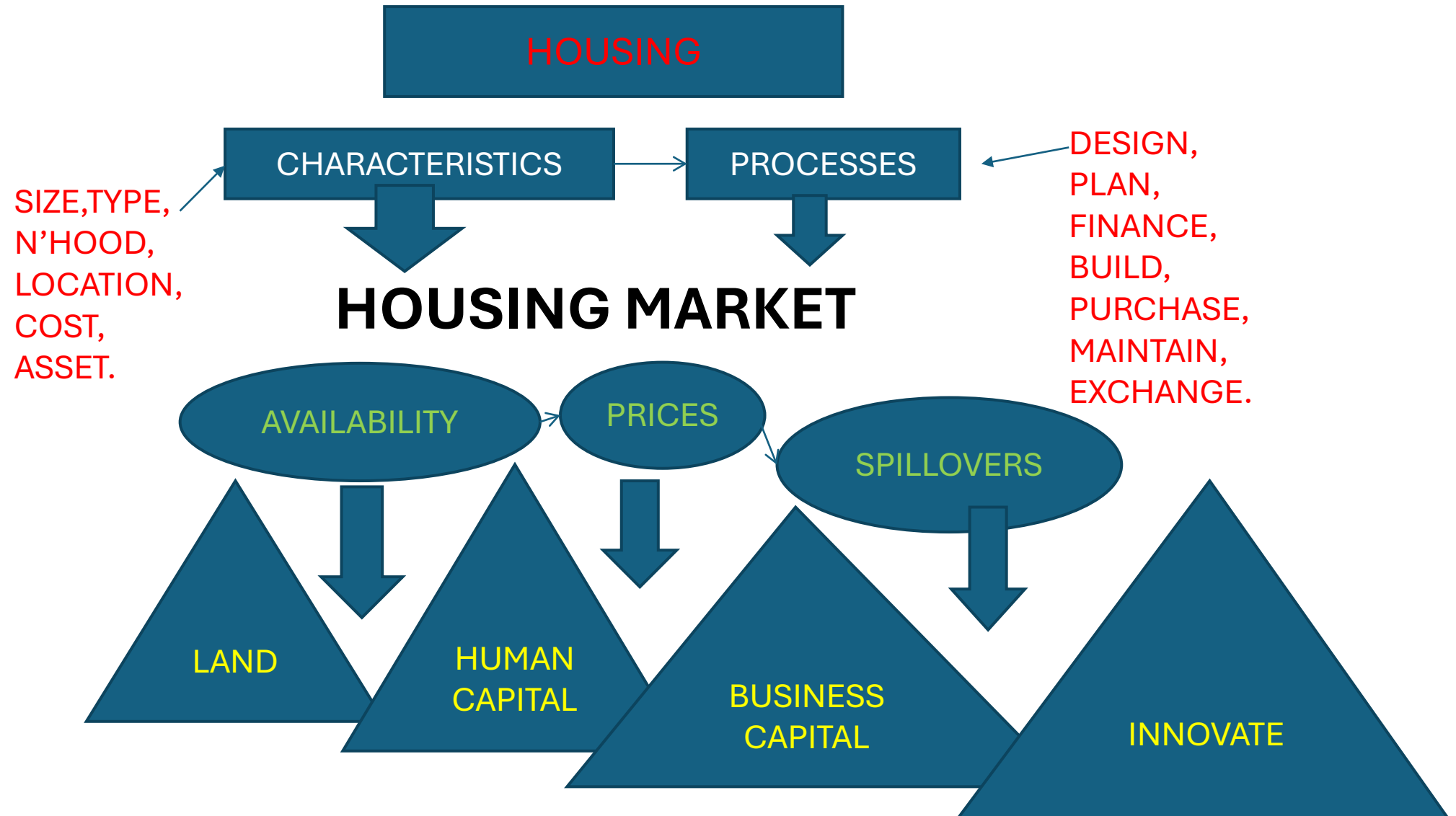
Digging Beneath The Surface: Is Housing Perpetuating A Wealth Divide in Canada?

Caranci.B.,Fong.F.,and Gebreselassie. M. TD Review October 5, 2022.



Source: Bank of Canada, TD Economics. Last observation: June 2021.

SIMPLE REFRAMING HOUSING-ECONOMY CONNECTIONS



IV. WHY? PROBLEM CAUSES

The dominant 'merit good' mentality of housing policy debate envisages affordability problems resolved by 'more housing rights', an 'end to financialisation' of housing, and more public resources for housing. The first two arguments are wrong, and the third is fiscally unlikely.

In broad terms problematic outcomes reflect:

1. The static real incomes of the poor with growing merit good needs (that may require more public resources but more efficient provision systems too).
2. The sustained inability to ensure that house prices (quality adjusted) do not rise ahead of incomes. This is a system management problem; in part it is a fundamental failure of the ways in which housing systems are understood and governed in Canada and the political choices influenced by housing outcomes (and this may change).

The mainstream economics profession has highlighted a low price elasticity of supply, primarily attributable to planning, as the key system failure. This makes housing supply and construction the focus of policy discussion and we stick with that discussion here. However, the empirical evidence of planning as the dominant and ubiquitous cause on supply inflexibility is highly contentious. We believe systematic supply side audits are required for all metropolitan/regional systems. The 'planning' explanation is just too convenient for central banks and finance ministries and other ministries that boost housing demands (immigration, overseas students etc) in excusing them from exploring how policies have contributed to the current problematic outcomes.

But what about supply?

VI. Supply: Inelastic and Complicated.

1. Housing supply is (unlike the 'production functions' of economic theory) neither smooth nor uniform.

- 100's of steps from envisioning to building approval
- 1,000's of steps from putting a shovel in the ground to cutting a ribbon.

All involving the coordination of multiple markets including land, finance, materials, professional services and labour organised into multiple trades/subtrades. Critically involved working with several departments in governments, and not just planning, and utilities. It is a 'slow' system.

2. Housing supply more complicated today than 30 years ago?

- Major increase in regulatory burdens Cutbacks in the capacity of planning departments to develop effective strategies and approval timelines.
- It is estimated that 25-30% of construction costs are attributed to fees, levies and taxes from various departments in 3-orders of government and utilities like; water, power and telcos, which to varying degrees create obstacles to the efficient delivery of supply.

Now politics and press argue for more supply, Andrew Coyne (Globe and Mail) asks why we can't be building as many homes proportionately as we did from 1950's to 1970's. Too many targets being easily estimated that are much more difficult to attain. National debate figures potentially unrealistic. There are severe capacity constraints.

Key Limitations

Not just increased regulatory burden but market shortages and failures in complex supply chains

- Think about supply chain blockages rather elasticity estimates
 - Shortages of skilled labour (market failures, shifting worker preferences. Gaps in skills, education and immigration policies)
 - Inadequate supplies on infrastructure serviced, accessible land
 - Traditional building approaches (modular needs expansion)
 - Responses of development firms to market shortages
 - Cost of development finance/equity (current constraint)

Canada Urgently Needs a National Housing Supply Commission, with Regional and Metropolitan 'Feeders', to understand, explore and speed-up the supply process. Why is this not already done? Surely it is CMHC's job to improve capacity rather than simply observe it needs to be improved!



MAJOR QUESTIONS

We have touched on an impossibly wide range of issues and key questions arise.

On Governance

- How can each level of governance develop a cross-silo strategy to deliver the best housing outcomes rather than palliative strategies
- Can The Federal government continue to remake cross-order relations to recognise the wider than local drivers and outcomes of housing policies

On Substance

- Can Productivity and Redistributive aspects of housing become central to policy
- Has Prudential regulation over-emphasised ‘derisking’ of consumer choices, and what have been the housing consequences of stress testing and ‘quantitative easing’
- Can improving system effectiveness, of non-profits and the development industry, be given a new emphasis: have subsidies and spend failed to incentivise more efficient outcomes?
- Do we need a comprehensive analysis of fiscal policy effects on housing outcomes?
- Can supply approval and completions processes become flexible and quicker?

On Answers, How can we raise applied economics discussion of the Canadian housing system (a regular cross sectoral discussion/research network). Within academia can we get serious economists to take housing seriously? Are there any economics Ph.D. students working on the Canadian housing system. If not, why not? And what are SSHRC and CMHC doing about it?

DO WE NEED A NEW APPLIED ECONOMICS INFORMED NARRATIVE OF CANADIAN HOUSING SYSTEMS AND HOUSING POLICIES?

Links and References

REFERENCES.

A. Canadian Housing Evidence Collaborative (SSHRC-CMHC Centre), McMaster University. The following papers can be located under Research Papers on the Home Page of the CHEC website <https://CHEC-CCRL.ca> Project summaries and presentation videos are also located at the same site. They were all produced in the second half of 2023.

- I. A SYSTEMS APPROACH TO HOUSING POLICIES. PAPER 1 THINKING SYSTEMS FOR BETTER HOUSING OUTCOMES AND GOVERNANCE Duncan MacLennan and Jinqiao Long.
- II. A SYSTEMS APPROACH TO HOUSING POLICIES. PAPER 2 HOUSING AS A SPATIAL, ECONOMIC SYSTEM: KEY OUTCOMES. Duncan MacLennan and Jinqiao Long.
- III. A SYSTEMS APPROACH TO HOUSING POLICIES. PAPER 3 HOUSING SYSTEM OUTCOMES AND NET ZERO CARBON. Duncan MacLennan and Jinqiao Long.
- IV. BUILDING FEDERAL FOUNDATIONS FOR GOVERNING THE HOUSING SYSTEM. Duncan MacLennan and Jinqiao Long.

B. City Futures Research Centre, UNSW, Sydney. The CHEC papers were prepared for CMHC in response to an earlier series of papers prepared in Australia in 2021-22. These papers are located on the website of the City Futures Research Centre at the University of New South Wales, at <https://cityfutures.adu.unsw.au>

- MacLennan, D. 2021. Housing: Taming the Elephant in the Economy.
- MacLennan, D., Leishman, C. and Goel, S. (2021) Housing in the Economy: Scale, Cycles and Stability.
- MacLennan, D. Long, J. and Leishman, C. (2021) Housing Wealth: All that Glitters is Not Gold.
- MacLennan, D, and Long, J. (2021) Housing and Productivity: All, or Nothing at All?

C. Recent Summary Publications on Housing and Productivity.

- MacLennan, D. and Long, J. (2024) A Missing Perspective in Housing Economics: Productivity. Chapter 8, pp 149-162 in *The Routledge Handbook of Housing Economics*. Abingdon and New York.
- MacLennan, D., Miao, J., Christie, L. and Long, J. (2021) 'Raising Productivity and Housing the Economy', in P. McCann and T. Vorley (ed), *Productivity and the Pandemic: Challenges and Insights from Covid-19*, Edward Elgar Publishing: pp. 191-204.